



School Property Tax Reform Must Start with Cost Containment

On June 11th, H.B. 1776, a proposal to end school property taxes, came up for a vote in the House Finance Committee. The Committee believed the proposal contained too many unanswered questions and were not convinced it would raise the necessary revenue to replace all school property taxes. They tabled the bill by a 13 to 11 count (one abstention). Whether or not the bill will be brought back in the future remains to be seen. But it does raise an interesting question: Where and how should school property tax reform begin? The focus should be on the driver of high taxes, to wit: rapidly rising spending.

Most school tax reform proposals have focused on shifting from property taxes to some other tax, usually the income or sales tax. H.B. 1776 was no exception. It had two main sources of revenue that would have been used to replace school real estate taxes: an increase in the income tax of 0.94 percent and a one percent increase to the sales tax with an expanded base. In a previous *Policy Brief*, we questioned whether or not the increase to the income tax and the expanded sales tax base, with eighty-nine exemptions, would generate enough money to replace the \$11.14 billion in school real estate taxes collected by districts in the Commonwealth.

The income and sales taxes are easy targets. For the 2010-2011 fiscal year, the state collected \$10.44 billion on a rate of 3.07 percent for the income tax and \$8.6 billion on a six percent sales tax (with current base). A one percentage point increase to the income tax would generate roughly \$3.4 billion while a one percent increase in the sales tax would generate \$1.43 billion—assuming of course no change in current behavior.

H.B. 1776's proposal would have added a 0.94 percentage point increase to the income tax (\$3.196 billion) and all of the sales tax revenues (increased to seven percent with an expanded base) into an Education Stabilization Fund to replace school district property tax collections. With the expanded tax base, and the eighty-nine exemptions, it was difficult to forecast how much money could have been raised and placed into the fund. Perhaps this uncertainty was a primary reason the bill was tabled.

It is also possible the Committee believed that Pennsylvanians are not willing to accept a tax shift. That is, taxpayers are not fooled by having their money taken from the right pocket instead of the left. Over the years voters at the local level have rejected attempts to shift from property taxes to other local taxes such as a wage tax. Voters know that as the cost of education continues to increase there would be more and more pressure to raise the state income and sales taxes even further in the future to meet the growing expenditures.

In short, one of the main reasons school property taxes have become such a burden is that the cost of education has risen at a rapid pace—53 percent over the last decade while enrollment has changed little. So why not place the focus where it needs to be—on the cost of education? The Legislature has made little progress toward repealing or reducing school district property taxes. Remember the promises made regarding casino gambling and all the money that would be raised to reduce school property taxes?

But there are some measures that would lower the cost. The Legislature could start with eliminating the right of teachers and other school employees to strike. Nothing creates a march toward higher costs, less efficiency and loss of management ability to allocate resources and adopt better management methods than the imbalance of negotiating power created by strikes and threats of strikes. Second, the Legislature could change the law to make it easier for districts to manage personnel and control costs by removing the requirement that teachers cannot be laid off during periods of financial difficulty unless enrollment falls or entire programs are eliminated. This is possibly the most idiotic of all laws on the books regarding cost containment and efficient use of limited resources. Third, the Legislature can remove the prevailing wage requirement for school construction. This measure alone could save hundreds of millions of dollars in needless expenditures.

The cost of education puts pressure on school district finances. For many districts property taxes are the largest source of revenue so property tax rates continue to climb to meet the rising obligation. Eliminating or reducing school district property taxes through a switch to another tax source does not eradicate the main problem which is the cost of education in the Commonwealth. Perhaps by looking at the cost side of the equation, property tax relief can be more readily achieved.

Once the recommended cost containment measures are adopted, the easing of the school tax burden through measures along the lines of H.B. 1776 might be achievable. That is to say, a portion of the taxes could be shifted and thus cap the property tax burden while leaving this important source of local funding of schools in place. For example, a one percentage point increase in the income tax would cover about 30 percent of the school real estate taxes collected. But if this approach were to be taken, and schools shared in the additional income tax to lower property taxes, there would have to be a statutorily imposed permanent freeze on school district property tax millage rates. Moreover, the law should be written to allow property tax revenues to rise only as result of a rising tax base—i.e., the market value of property goes up owing to higher prices or new construction.

If Pennsylvania is serious about the importance of local control of schools, it should allow locals more control over costs, which in turn would allow school districts to rein in property tax burdens.

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