ELECTION 2016 TAXATION, BUDGETS

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VERMONT LEAGUE OF CITIES & TOWNS

Taxation and Budgets – Getting the Job Done in Vermont

The Property Tax. According to the National League of Cities, "property tax" was the hottest budget issue that mayors across the country discussed in their 2016 State of the City speeches. Vermont, where property taxes and taxes in general are election issues, is no different. The property tax is the only tax revenue source that the Vermont Legislature has allowed all but 18 municipalities to use. In those 18 municipalities, voters have adopted and the legislature has approved local authority to levy a one-percent local option tax on either the sales tax or the meals and rooms tax, or both on of them.

"Property taxes have been called the scapegoats of the tax world, 'a catch-all for gripes about potholes, traffic tickets and anything else that ails a local economy,'" writes Christina McFarland in an NLC 2016 State of the Cities report. "A key reason for the blatant disdain of property taxes is that the tax burden is more transparent (annual tax bill) and harder to avoid when compared with sales taxes applied at checkout or income taxes withheld from a paycheck."

The property tax problem of Vermont's cities and towns is accentuated by the impenetrable way in which the education property tax is established, the proportion of the total property tax it constitutes, its sheer amount, and how and to whom it is assessed and collected.

State Budgets. According to a report from the Joint Fiscal Office, the FY16 State of Vermont balance sheet showed budget-adjusted revenues and expenditures of $5,628,665,846. The budget has grown at an annual average of 3.6 percent since FY09.

Balancing the budget hasn't been easy of late. Budget gaps were $176 million in FY12, $50.6 million in FY 2013, and, in November 2014, projected to be $99 million in FY14. By December 2015, the projected budget adjustment need for FY16 was $40 million, including $36 million of Medicaid-related adjustments. For FY17, that figure was $58.5 million, including $53 million of Medicaid pressure. These amounts do evolve throughout the year as revenues and expenses fluctuate. However, addressing budget deficits has been a constant consideration for the Vermont Legislature and administration since the Great Recession of December 2007 through June 2009.

Last month, the Joint Fiscal Office projected an FY18 budget deficit in the $30-40 million range. The Education Fund, however, is expected to have a surplus of $20 million by the end of FY17.

"Recent budget exercises have generally resulted in budget presentations that address the targets by making small operational changes," the Administration's Budget Instructions warns Vermont

agencies as they develop their FY18 budgets. "Finance and Management does not believe this is a sustainable way to approach the budget process. By examining whole programs across state government, the Administration may be more successful addressing the role of state government than perpetuating the expectation that agencies and departments do more with less." To the extent that the state uses stressed revenue sources to address fiscal problems while simultaneously shifting the responsibility of implementing many programs to local governments (almost always without relinquishing oversight authority to them), the squeeze on the municipal property tax continues to tighten. At the same time that school consolidation pursuant to Act 46 of 2015 may bend the curve of education property taxes, there is no guarantee of that, as this year's Act 132 expressed.

Where We Are Today. CNBC ranked Vermont third in the country in terms of quality of life in 2016, but added that "it's a long climb when it comes to workforce and capital." CNBC also ranked Vermont:

- 7th in education
- 40th in the cost of living
- 41st in infrastructure
- 43rd in the cost of doing business

According to the Tax Foundation, a non-partisan tax policy research organization, Vermont's state and local tax burden ranked tenth in the country in 2012 (at 10.3 percent). The Tax Foundation further calculated that Vermont's tax burden has ranged from a high of 11.9 percent of income that Vermonters are paying in state and local taxes in 1977 to a low of 10.0 percent in 2000.

Based upon 2015 figures, the Tax Foundation ranks Vermont 46th in state business tax climate favorability. In 2013, Vermont's tax revenue pie was sliced like this:

- 43.0 percent from property taxes,
- 10.5 percent from sales tax,
- 19.5 percent from individual income tax,
- 3.1 percent from corporate income tax, and
- 23.8 percent from other taxes, including excise, severance, stock transfer, estate and gift taxes.

Per capita income in Vermont in 2014 was $46,428, ranking it 19th in the country. In terms of a property tax burden, Vermont ranked 9th in 2015.

What to Do? How we raise revenue in Vermont to fund the constant appetite for more and newer programs is not only out of balance but also unsustainable. In recent years, we have constantly struggled to find the revenue to fund all the obligations that legislators and administrations have imposed on both themselves and local governments. Little action has been taken in the State House to eliminate programs that might be obsolete or fall to the bottom of the priority heap. At the municipal level, local officials think long and hard before proposing any initiative that would result in an increase in municipal property taxes. These conundrums are not

lost on legislators. However, their impact on property tax burdens seems always less compelling when considered in light of legislative priorities.

The 2009 special legislative session created a three-member Blue Ribbon Tax Structure Commission to prepare a structural analysis of the state's revenue system and offer recommendations for improvements and modernization and a long-term vision. The goal was a tax system that provides sustainability appropriateness and equity. "Vermont's policy makers and citizens have a choice," begins the Introduction to the commission's Final Report of January 2011. "We can rehash the same tax debates that occur perennially here and around the country, or we can engage in a thoughtful debate about the policy choices embedded in the tax system. We can repeat the fictions and assumptions that reinforce our personal preferences, or we can address the facts about our tax system. We can insist that nobody lose in reform or we can acknowledge that change means winners and losers. In short, we can appear to do something about our tax system, or we can do something about our tax system."

A few of the commission's numerous tax policy recommendations have been implemented. Since 2005, the Joint Fiscal Office has written a biennial Tax Expenditure Report that includes history, estimated value, and number of beneficiaries. In 2014, the legislature added a statutory purpose to each tax exemption. The task of choosing which property tax exemptions to eliminate has proven far more difficult. A further commitment to examine the property tax after issuance of the Blue Ribbon Tax Structure Report never came to pass.

A standing joint legislative Government Accountability Committee, also created in 2009, was charged with making recommendations for state government to be more forward-thinking, strategic, and responsive to the long-term needs of Vermonters, including examining areas of redundancy and alignment of financial and staff resources. Last year, a three-member Government Restructuring and Operations Review Commission was created to identify ways to increase government efficiency and productivity in order to reduce spending trends and related resource needs. That commission is hosting the last of a series of public meetings in St. Albans on October 25 and hopes to issue a report by mid-November. More than a few studies have examined the Transportation Fund and how revenue sources can be adjusted in light of long term declines in gas tax revenues. The State Treasurer is currently finalizing an assessment of the financial needs to implement the Vermont Clean Water Act and the Total Maximum Daily Loads (TMDLs) in our larger waterways. She expects to submit her report to the legislature by the end of the year.

Several other efforts are underway to assess our current economic climate and how Vermont might approach growing the economy. One of the most interesting is the Vermont Chamber of Commerce's Vermont Futures Project, which promotes the long-term economic health of Vermont by providing opportunity for Vermonters.

Vermont has a vision of what it wants that contrasts – sometimes sharply – with the reality of what it can afford. The fallout affects all kinds of interests, not the least of which is municipalities' ability to provide their citizens the services they require. This is not news to anyone, and there is no painless fix to the problem. How will the next legislature and administration work to bring revenues and taxes into balance in a sustained way? Revisiting the

Blue Ribbon Tax Structure Commission Report, paying close attention to the findings of the Government Restructuring and Operations Review Commission, and closely tracking the level of success of the school consolidation efforts – and defining success in that context – is a good place to start.

VLCT supports:

- legislation to reform Vermont's income, sales, and property taxes;
- providing sufficient revenue for local government initiatives and reimbursing municipalities for all state-mandated property tax exemptions or providing local voters with the authority to impose municipal service fees on such properties;
- allowing local flexibility in pursuing economic development activity; and
- assessing whether Act 46 has resulted in cost reductions in school district budgets and per-pupil expenditures. The legislature should develop a tangible definition of success.

VLCT opposes:

- all unfunded mandated programs, pre-emption of municipal programs, or shifts in costs to local government; and
- any new state property taxes until a reformed tax structure is adopted.

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