

VERMONT DEPARTMENT OF TAXES

YEAR USED TO CALCULATE PROPERTY TAX ADJUSTMENTS

Act 46 of 2015, Sec. 48. YEAR USED TO CALCULATE PROPERTY TAX ADJUSTMENTS

On or before January 15, 2016, the Commissioner of Taxes shall report to the General Assembly on the steps that would be required to transition to calculation of the property tax adjustments under 32 V.S.A. chapter 154 on a current-year basis. As used in this section, “a current-year basis” means using the current year’s homestead adjusted tax rates, the current year’s assessed property values, and the taxable income from the prior calendar year to calculate a property tax adjustment filed in the current claim year. In preparing the report, the Commissioner shall consult with the Vermont Association of Listers and Assessors, the Vermont League of Cities and Towns, and any other interested stakeholders identified by the Commissioner.

YEAR USED TO CALCULATE PROPERTY TAX ADJUSTMENTS

SUBMITTED TO

The Vermont General Assembly

SUBMITTED BY

Mary Peterson, Commissioner
Department of Taxes

PREPARED BY

Jake Feldman, Research Statistician
Policy, Outreach, and Legislative Affairs
Department of Taxes

Rebecca Sameroff, Senior Fiscal Analyst
Policy, Outreach, and Legislative Affairs
Department of Taxes

Candace Morgan, Director
Policy, Outreach, and Legislative Affairs
Department of Taxes

IN CONSULTATION WITH

Division of Property, Valuation and Review - Department of Taxes
Vermont Association of Listers and Assessors
Vermont League of Cities and Towns

DATE SUBMITTED

January 15, 2016

Contents

OVERVIEW	1
HISTORY	1
CONSIDERATIONS WITH THE “LOOKBACK” Mechanics	2
POTENTIAL ALTERNATIVES Current-Year Assessed Property Values Current-Year Municipal Tax Rates	4
ADDITIONAL CONSIDERATIONS	10

Overview

Act 60, the Equal Education Opportunity Act of 1997, changed the state's education funding system. The education property tax, which had been managed at the town level until that point, became a statewide tax, thereby allowing education property tax revenue to be distributed more equally among Vermont's towns. At the same time, it was decided that resident homeowners should be allowed to pay an education tax based on their income instead of on the value of their property. Various strategies have been tried and discarded since Act 60 to make this income based payment system a possibility, and each has its pros and cons.

History

Property tax adjustments ("PTAs" or "income sensitivity adjustments") adjust qualified taxpayers' property taxes down to a certain percentage of their income. A property tax adjustment can have two components, commonly known as the "prebate" and the "rebate." Everyone who gets an adjustment gets a prebate, which is a reduction of their education property taxes based on their income. Taxpayers with household income less than \$47,000 are additionally eligible for a rebate if the sum of their education property taxes and municipal property taxes still exceeds a certain (different) percentage of their household income after the prebate has been applied. This policy is often called the "circuit breaker" because it "turns on" when that lower income threshold is reached. About 112,000 of the 170,000 taxpayers who submitted a homestead declaration in 2014 received a property tax adjustment, and 35,000 of those 112,000 also met the circuit breaker criteria.

Some form of state-administered, income based property tax adjustment system has existed in Vermont since 1970. At first, the maximum credit was \$300 and only people over 65 whose property taxes exceeded 7% of their household income qualified. Between 1970 and 1997 there were numerous changes to the maximum credit, the income thresholds for eligibility, and the percentage of income that property taxes had to exceed for the claimant to get an adjustment. When Act 60 created a statewide education property tax in 1997 the system became more complex. The existing adjustment system (which at that point was for households with income up to \$47,000 and looked at the sum of municipal *and* education property taxes) evolved into the rebate portion of the new system. The new system added the prebate component, separately applied for, which only looked at educational property tax. It was called the prebate because it looked ahead to the coming tax bill. A snapshot from FY2006 shows:

Table 1: Fiscal Year 2006 Prebates and Rebates

	Prebate	Rebate
Household Income	Previous (Calendar Year)	Previous (Calendar Year)
House-site Value	Current (Fiscal Year)	Previous (Fiscal Year)
Education Taxes	Current (Fiscal Year)	Previous (Fiscal Year)
Municipal Taxes	-----na-----	Previous (Fiscal Year)

The prebates were sent straight to the claimant as a check and the rebates were applied as a tax credit if the claimant was filing their application with their income tax return or sent as a check if not. The prebate was meant to help qualified people with their upcoming property taxes, but the check didn't necessarily arrive by the time their first property tax payment was due, even if the form was filed with the claimant's income tax return in April. That's because the state needed to know the house-site value for the upcoming fiscal year, and the grand list was finalized at different times for

different towns. This complicated prebate payment schedule was laid out in statute (Sec. 3. 32 V.S.A. § 6066a (repealed 2006)):

Payments will be made by the latest of: August 1, for claims filed by April 15; 45 days after the claim is filed, for claims filed after April 15; or 30 days prior to the first education property tax installment is due for the claimant’s municipality in the fiscal year which begins in the calendar year in which the claim is filed; or 25 days after the Town’s grand list had been transmitted[...]

Besides the check not arriving in time for the first property tax bill for many people, some policy makers sensed that their constituents weren’t fully aware that the check was related to property taxes because the timing of the check arrival wasn’t coordinated with the property tax bill.

During the 2006 legislative session changes were made. The three forms that people had to submit were reduced to two: a homestead declaration and a property tax adjustment claim - both due by April 15. Instead of tax credits or checks sent directly to taxpayers, the adjustment amount was communicated to the towns, who then subtracted it from people’s property tax bills. And to make sure every town had enough time to process the adjustments and apply them to the first property tax bill installment, the state guaranteed that they would send the adjustments by July 1. To achieve that goal, the information used to compute the prebate shifted to the same year as the information used to calculate the rebate and that’s the way it’s been ever since. The names “prebate” and “rebate” stuck even though both things were now tied to the previous year.

Table 2: Fiscal Years 2007- 2016 Prebates and Rebates

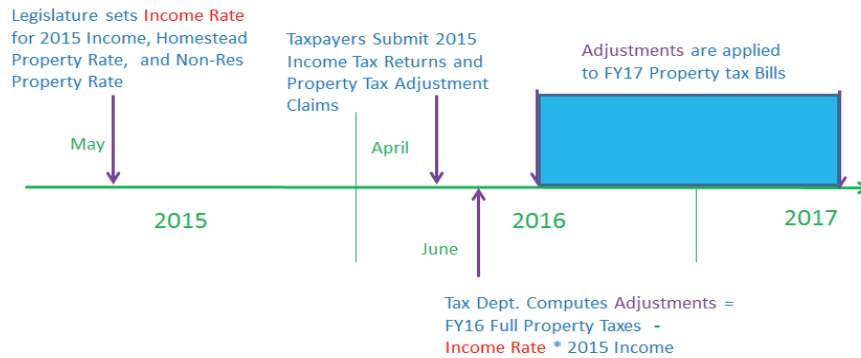
	Prebate	Rebate
Household Income	Previous (Calendar Year)	Previous (Calendar Year)
House-site Value	Previous (Fiscal Year)	Previous (Fiscal Year)
Education Taxes	Previous (Fiscal Year)	Previous (Fiscal Year)
Municipal Taxes	-----na-----	Previous (Fiscal Year)

Considerations with the “Lookback”

Table 2 shows the way things stand now – the adjustment calculation is completely based on previous year information, but is applied to the current year tax bill. Switching to all previous year information for computing property tax adjustments solved many problems, but it created some confusion with respect to timing. The lookback means that a taxpayer’s adjustment amount is sensitive to the previous year’s property taxes, rather than the property taxes to which the adjustment is being applied.

Every year the legislature sets a state-wide base income rate along with a base homestead property rate and a base non-residential property rate (going forward the Legislature will set yields which will determine rates). The two property rates have an immediate impact, but the income rate sits idle until the following fiscal year.

Figure 1: Income Rate Timeline



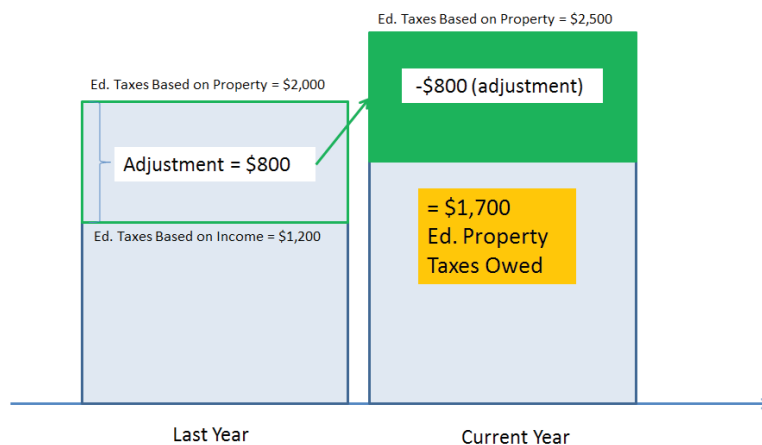
The homestead property rate and the income rate are both affected by a town’s per pupil spending. If a town spends 25% above the per-pupil base amount, both its homestead rate and its income rate will be 25% higher than the respective state-wide base rates. Every taxpayer will see that 25% higher homestead rate reflected on their property tax bills, but because of the lookback, the income rate won’t come into play until adjustments are calculated for the following fiscal year’s property tax bills.

Mechanics

Property tax adjustments are based on the prior-year but netted out of current-year property taxes. Therefore an income-sensitized taxpayer’s property tax bill is a mix of current-year ingredients (including property value, CLA, and tax rates) and prior-year ingredients (the adjustment).

Suppose a household made \$60,000 last year and suppose that for the town they live in the applicable percentage of income was 2% for education property taxes. 2% of \$60,000 is \$1,200. Their education taxes on property last year were \$2,000 so this household is entitled to an adjustment for \$2,000 - \$1,200 = \$800 from last year that will be applied in the coming fiscal year. If property tax rates spike in their town by 25% to \$2,500, this household pays \$1,700/\$60,000 = 2.83% of their income in the current year. Figure 2 shows this situation:

Figure 2: Property Tax Adjustment with the Lookback



This example shows what happens when education property tax rates go up, which has been the case in many towns the past several years. If the rates are staying the same the lookback is not as much of an issue, and if property tax rates are going down the lookback is actually to the taxpayer’s advantage. Again, this is because the size of the adjustment is based on the prior year’s property tax bill, not the bill to which the adjustment is being applied.

There is an additional “lookback” in Vermont’s adjustment system that is outside the statutory charge of this report – the income component. Property tax adjustments are currently based on a taxpayer’s income from the previous calendar year. Incomes may change dramatically from year to year in a taxpayer’s life, so when a taxpayer gets their adjustment, they’re not necessarily experiencing the same income that the adjustment was based on. Despite this problem, the same prior-year income would be used in a new “current-year” adjustment system. Prior-year income is, in practice, the most current income we have because annual household income is not known until the year is complete. Any attempt to account for true current-year income would involve estimation and an arduous reconciliation process.

Potential Alternatives

It would be impossible to line every element into the current year, including income, unless a reconciliation process is employed. This has been tried previously, and also has caused issues with the Affordable Care Act. If using current year income is impractical, a more modest goal might be to base property tax adjustments on property tax rates and property value from the current fiscal year. This would require some substantial changes made to statute and various areas of program administration. Here’s what this new system would look like (compare to Table 2):

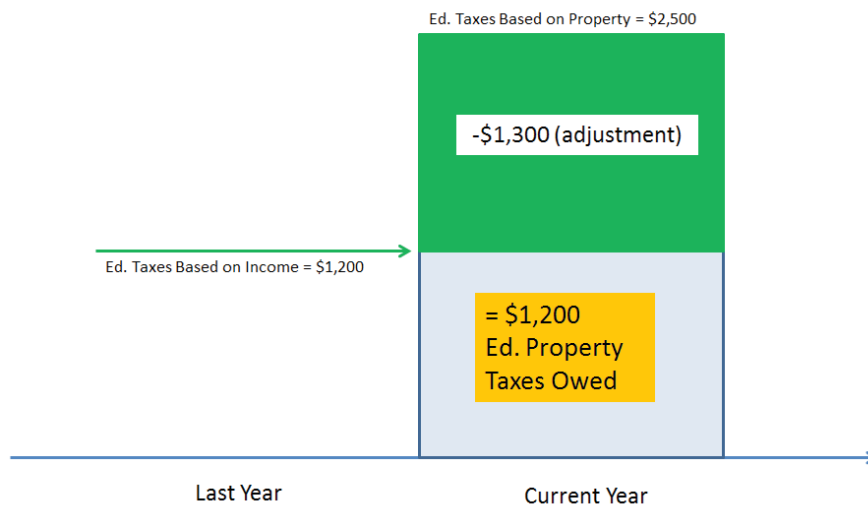
Table 3: Prebates and Rebates with No Lookback

	Prebate	Rebate
Household Income	Previous (Calendar Year)	Previous (Calendar Year)
House-site Value	Current (Fiscal Year)	Current (Fiscal Year)
Education Taxes	Current (Fiscal Year)	Current (Fiscal Year)
Municipal Taxes	-----na-----	Current (Fiscal Year)

Here’s how this change would affect the taxpayer in the example in the last section:

Suppose a household made \$60,000 last year and for the town they live in the applicable percentage of income is 2% for education property taxes. 2% of \$60,000 is \$1,200. Their education taxes this year are \$2,500 so this household is entitled to an adjustment of \$2,500 - \$1,200 = \$1,300, which is applied to their bill, bringing their educational property tax liability down to \$1,200.

Figure 3: Property Tax Adjustment on a Current Year Basis



To compute adjustments on a current-year basis, the Department would need to know five key ingredients:

- The prior year's household income
- The current year's equalized education tax rate for the town
- The current year's applicable percentage of income for the town
- The current year's assessed property values
- The current year's municipal tax rates (for the circuit breaker program)

Three of the bullets are darkened because they are information we have, so there's no need to change anything. Household income would be the same household income that's used now, reported on the household income form along with the homestead declaration and property tax adjustment claim by April 15. The education tax rates and applicable percentage of income are both determined by the Agency of Education and communicated to the Tax Department in the spring, so that's information we have too (although if a town must revote its school budget that may complicate matters). The two things that the Tax Department doesn't have, but would definitely need, are current-year property values and current-year municipal tax rates.

The current-year property values would be needed for all 112,000 households that get adjustments. The current-year municipal rates would be needed for the 35,000 households with income below \$47,000 that get the circuit breaker (rebate). We will present, separately, the options and issues for getting these pieces of information in time to compute adjustments on a current-year basis. **The Tax Department is not making any recommendation at this time and the order and numbering of the options is for ease of reference only.**

Current-Year Assessed Property Values

The property values the tax department uses to compute adjustments come from each town’s grand list. Currently, we are using the previous year’s grand list which is final and free of errors when we go to compute adjustments. In a new, lookback-free system, we would need to switch to using the current-year’s grand list.

Table 4: Current Grand List Calendar

	Assessment ("as of") date	Homestead Declarations Filed	Latest Abstract Can be Lodged	Grievances must be Filed by	Grievances Hearings End	Result of Grievance Mailed	Latest Grand List Can be Lodged	Appeals to BCA and BCA Hearings + Errors and Omissions
Small Towns	1-Apr	15-Apr	4-Jun	19-Jun	2-Jul	9-Jul	25-Jul	-----through 30-Dec-----
Large Towns	1-Apr	15-Apr	24-Jun	9-Jul	22-Jul	29-Jul	14-Aug	-----through 30-Dec-----

Table 4 provides a rough outline of the existing grand list process for small and large towns. Switching to the current-year grand list would be complicated because as you can see from the above table it is still far from final in late June when property tax adjustments need to be computed (so that they can be distributed to towns by July 1st).

Here are a few options for getting current-year property values in time and the corresponding issues that would need to be addressed:

Option 1: Move the grand list calendar up

Table 5: Moved-Up Grand List Calendar

	Assessment ("as of") date	Homestead Declarations Filed	Latest Abstract Can be Lodged	Grievances must be Filed by	Grievances Hearings End	Result of Grievance Mailed	Latest Grand List Can be Lodged	Appeals to BCA and BCA Hearings + Errors and Omissions
Small Towns	1-Dec	15-Apr	4-Feb	19-Feb	2-Mar	9-Mar	25-Mar	-----through 30-May-----
Large Towns	1-Dec	15-Apr	24-Feb	9-Mar	22-Mar	29-Mar	12-Apr	-----through 30-May-----

An option that has been explored in the past is moving the calendar of grand list activities earlier in the year. The revised grand list calendar above, provided by Vermont Assessors and Listers Association (VALA), would allow ample time for listers to resolve property values so that they would be ready for the Tax Department’s calculation of adjustments by July 1. The revised calendar moves the valuation “as of” date from April 1 to December 1. This is central to the grand list process because the value of a property is determined based on its condition “as of” that date. For example, currently a building under construction is only taxed based on whatever state the building is in on April 1 even if it improves significantly after that date.

According to VALA, the December 1 valuation date may have some benefits over the current April 1 date because it would allow them to do their “outside” work in the fall and the “inside” work in the winter. On the current schedule, they are doing their “outside” work in the late winter/mud season and their “inside” work in the nice part of spring.

Issues:

Any statute and programs that are tied to the current Grand List schedule would need to be changed. The Current Use program, the program that allows Veteran’s to exempt value from their house-site (requiring documentation from the



VA), and VHFA applications would all be affected. Indeed, the April 1 date is referenced many times in Vermont's Title 32 (Taxation and Finance) for property valuation. Here's a list of some of those statutory references:

- § 3482. Property listed at one percent
- § 3485. Records to be kept relating to deeds and mortgages
- § 3603. Construction equipment
- § 3610. Taxation of perpetual leased lands
- § 3618. Business personal property
- § 3651. General rule
- § 3691. General rule
- § 3692. Taxation of boats, outboard motors, and trailer coaches
- § 3755. Eligibility for use value appraisals
- § 3802a. Requirement to provide insurance information
- § 3831. College, university, or fraternity property
- § 3850. Blighted property improvement program
- § 4001. Inventory forms
- § 4041. Examination of property; appraisal
- § 4044. Appraisal of personalty on April 1
- § 4045. Appraisal on other than April 1
- § 4403. Appeal from appraisal made other than on April 1
- § 4605. Assessment when appraisal on other than April 1
- § 4608. Resident ownership ratio
- § 5071. Filing and notice of lien
- § 5404a. Tax stabilization agreements; tax increment financing districts
- § 5405. Determination of equalized education property tax grand list and coefficient of dispersion

Many town level and state level processes would be impacted by a change of the "as of" date. If the "as of" date did change, there would also be various transition year issues to consider. Additionally, many listers and assessors who are used to the current schedule would have to adjust to the new one. VALA reports that many listers spend winters away from Vermont. Under the new system, they would need to be in Vermont through early March to hear grievances.

Reappraisal towns would have an especially hard time with this schedule because many of them have already lined up firms to do reappraisals under the assumption that they could work through the summer and the new grand list values would be in place for the property tax year. If the firms had to complete their work by March or April, this could prove difficult and may jeopardize contracts that are already in place.

Another complicating factor identified by VLCT would be the Current Use Program. Municipalities need to know the "use values" for any properties enrolled in Current Use so they can submit their education grand list. The use values come from the Tax Department and are supposed to be communicated to the town by March 15 but often arrive much later. With a moved up grand list schedule, the use values would have to be communicated to the towns by March 15.

Option 2: Move grand list lodging date from June 24 to June 4th for large towns and use that preliminary lodged value to compute adjustments.

Issues:

The major consequence of using preliminary grand list values for the calculations of PTAs would be more instances of

rebilling taxpayers and the associated administrative burden on the Tax Department. Currently, changes are made to the grand list after June 4 through the grievance process outlined in Table 4. There are thousands of changes made to the initial grand list every year, especially in reappraisal towns. In most of those cases, the property values are being lowered (people usually don't grieve to have their property values increased) so the associated property tax adjustment would also decrease. The Tax Department would have to track these changes and send bills for over-adjustments or account for them some other way.

Current-year municipal tax rates (for the circuit breaker)

If the circuit breaker is to continue as a state-administered program within a new current-year PTA system, the Tax Department would need current-year municipal property tax rates in time to calculate the adjustments. As explained above, currently the circuit breaker (rebate) portion of the PTA is calculated using the prior year's municipal rates.

Towns adopt budgets at town meeting in March and then need to raise the money to support the budget through municipal taxes. Typically, towns wait to set rates until around the time the grand list is lodged (July 25 for small towns and August 14 for large towns) and they are fairly certain of the total property value in their town. Municipal Tax Rates are supposed to be submitted to the Tax Department by August 15 (32 V.S.A. § 5404) but the Tax Department's Division of Property Valuation and Review reports that they sometimes arrive as late as the end of October. It could be that the towns which don't send their first (and in some cases only) bill until late in the calendar year may take their time setting rates and reporting them to the state.

Another complexity with municipal tax rates is that, in a single town, different people may pay different rates. That's because some properties in town might be connected to a municipally maintained system like water and sewer, and some might not. The way the system works now, when a taxpayer submits a property tax adjustment claim they report their own house-site municipal tax from their prior year property tax bill (on line B6). The Tax Department runs a general check to make sure it is "about right" for the town, but there's really no way of knowing exactly. Here's a picture of the property tax adjustment claim form:

Figure 4: PTA Claim Form

SECTION B. PROPERTY TAX ADJUSTMENT CLAIM	
For Household Income up to approx. \$109,000. Attach Schedule HI-144	
To qualify, you must meet the requirements for filing a homestead declaration in addition to the following requirements. ALL eligibility questions must be answered.	
B1. Were you domiciled in VT all of calendar year 2014?	<input type="checkbox"/> Yes, Go to Line B2. <input type="checkbox"/> No, STOP
B2. Were you claimed as a dependent in 2014 by another taxpayer?	<input type="checkbox"/> Yes, STOP <input type="checkbox"/> No, Go to Line B3.
B3. Do you anticipate selling your VT housesite on or before April 1, 2015?	<input type="checkbox"/> Yes, STOP <input type="checkbox"/> No, CONTINUE
Amounts for Lines B4 - B6 are found on the 2014/2015 property tax bill . Round amounts to the nearest dollar.	
B4. Housesite Value	B4. _____ .00
B5. Housesite Education Tax	B5. _____ .00
B6. Housesite Municipal Tax	B6. _____ .00
B7. Ownership Interest	B7. _____ .00 %
B8. Household Income (Schedule HI-144, Line y). Schedule HI-144 MUST be attached.	B8. _____ .00



Any new system, where a town reports its current-year municipal tax rate to the state for adjustment computations would be complicated by widespread discrepancies between what the town reports as the rate and what residents' municipal taxes actually are, unless the town waited to know what each individual taxpayer's total municipal rate was and then sent a complete and accurate list for everyone in the town.

Option 1: Require towns to report municipal tax rates by June 15th

If the grand list was moved up as described in the last section, then towns would have finalized property values on May 31, and could presumably set rates by June 15. This would give the Tax Department enough time to compute adjustments by July 1, but towns may be unwilling or unable to accommodate this change to their rate-setting schedule.

Option 2: Send circuit breaker separately from the adjustment

This option would require the Department to send towns information regarding the adjustment, and then update the files with information regarding the circuit breaker at a later date. For towns that start billing in July, this may cause problems. They would have to credit the state payment to the taxpayer's account and then make changes and re-print any subsequent bills for that taxpayer. An eligible taxpayer in a town where property taxes are paid in installments would also see a bigger first bill compared to the subsequent ones (although the differences would not be huge). Additionally, no matter their billing schedule, towns currently rely on direct state payments for the municipal portion of the circuit breaker on the first of July, so this change would impact towns accounting.

Option 3: If town has not submitted municipal tax rate, use last year's

This idea came from a member of our Tax Technical Working Group on the premise that municipal rates don't change much from year to year, so substituting last year's would not be that outrageous.

Option 4: Continue to use previous fiscal year's municipal taxes for the circuit breaker

This option would keep the circuit breaker (rebate) portion of the PTA on a prior-year basis. This would eliminate the problem of the discrepancies in municipal tax rates within a town and would sidestep forcing the town to determine rates earlier. However, it would be somewhat confusing in light of the moving the rest of the PTA to a current-year basis and seems to contradict the intent of this study.

Option 5: Send the circuit breaker as a check to taxpayers

In this scenario the prebate portion of the PTA would still be computed by the state, communicated to the town, and applied as a credit to the taxpayer's bill. The circuit breaker would be sent separately as a check. The problems with sending property tax adjustments as checks have already been discussed in this report and are easy to understand. However, the circuit breaker portion of a property tax adjustment is generally much less than the prebate portion. Remember – everyone who gets a property tax adjustment gets the prebate. Households with income under \$47,000 get the prebate and the circuit breaker. The average prebate for those taxpayers is about \$1,800 while the average rebate is about \$600.

This option would change the experience of people eligible for the circuit breaker (rebate). These taxpayers would pay their tax bill (now about \$600 higher on average) and subsequently get "made whole" by the circuit breaker check directly from the state. While this would save some administrative complexity for towns, there would be an impact on municipal accounting. Currently towns are accustomed to receiving a direct state payment for the municipal portion of

the circuit breaker on the first of July; but in this scenario, the taxpayer would be made whole by the state, rather than the town.

Additional Considerations

Timing: There is an argument that it is logical for the income and property tax periods to overlap because you pay your bills based on the money you’re making, not what you made in the previous year. The system we are using now, where everything is looking back, has some overlap. Figures 5 and 6 show what year’s information is used to compute the adjustment that a taxpayer receives on their FY17 property tax bills under the current system and a new no lookback system:

Figure 5: Current System - Some Overlap

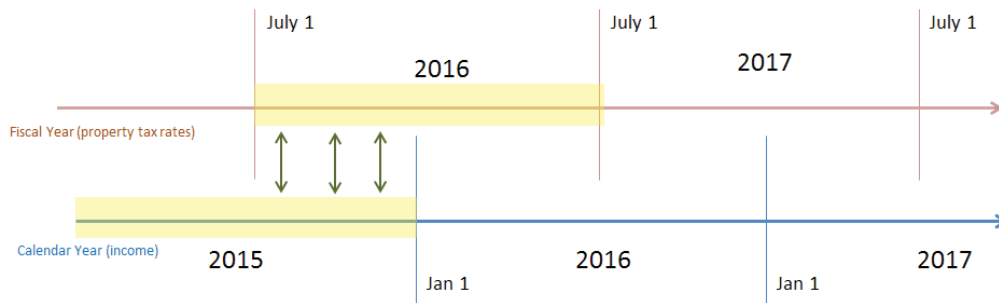
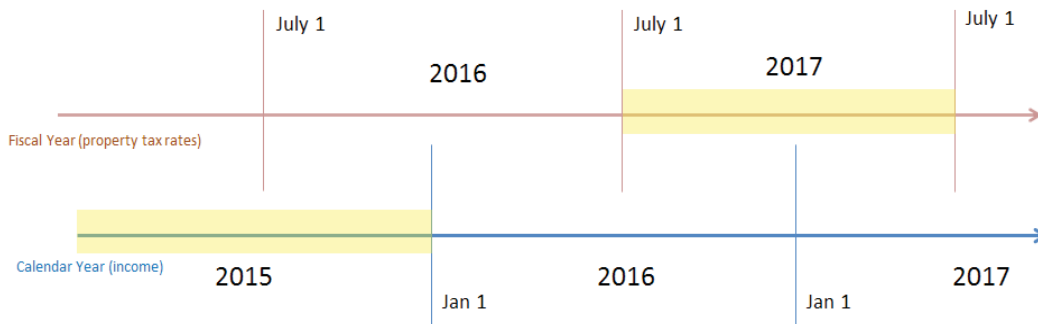


Figure 6: New (No Lookback) System - No Overlap



Communication: The property tax adjustment system is complex, but one advantage of the current system is that a tax preparer or claimant could figure out what the adjustment will be for the coming year fiscal year. If the adjustment system was based on current-year rates and property values, it would be much harder to figure out what a claimant’s adjustment amount will be, because you’d need to know their property value and rates for the current year, which are not determined until sometime in the summer. So the adjustment amount would basically be a black box, where people file the property tax adjustment claim form (Figure 4) and “wait and see.” Lines B4-B6, where filers write their housesite value, education tax, and municipal tax, would no longer be necessary. They would find out their adjustment amount in a

letter from the Tax Department dated July 1.

Cost: The state doesn't send actual money to towns for the prebate or the education tax portion of the circuit breaker – those take the form of lost revenue from the education fund. The only real money that's sent to towns is to “make them whole” for the reduction in people's municipal property taxes because of the circuit breaker. Remember, the circuit breaker looks at the total property tax liability of a claimant after the prebate has been applied. If the total liability is still over a certain percentage of their income, then they get an additional adjustment that is equal to that difference. Part of that overage may be from educational property taxes, and part may be from municipal. The state reimburses towns for the municipal part.

Changing to a current-year system for the prebate and circuit breaker would basically be like vaulting forward one year in the system we have today. Assuming property values stay about the same, this would result in approximately \$5 million of un-realized revenue from the education fund, and an additional \$1 million paid from the general fund for the homeowner rebate. *These figures are rough approximations based on growth in the property tax adjustment program over the past few years. The exact cost of any changes being considered will require more careful analysis.*