



INDEPENDENT FISCAL OFFICE

Second Floor, Rachel Carson State Office Building
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Harrisburg, Pennsylvania 17105

March 11, 2015

The Honorable Jay Costa
Democratic Leader
Senate of Pennsylvania
535 Main Capitol Building
Harrisburg, PA 17120

The Honorable Vincent J. Hughes
Democratic Chairman
Senate Appropriations Committee
545 Main Capitol Building
Harrisburg, PA 17120

Dear Senators Costa and Hughes:

This letter is in response to your request that the Independent Fiscal Office (IFO) make certain computations regarding a potential proposal to provide school property tax rebates. The proposal would provide a rebate to the owner(s) of a homestead property equal to the amount of school property tax paid, not to exceed the statewide average school property tax bill.

The request asked that the IFO provide the following estimates:

- School property tax collections (for all properties and for homesteads only) through FY 2019-20.
- The number of properties that may qualify as homesteads, the average school property tax paid by homesteads and the median school property tax paid by homesteads.
- The total funds necessary to provide each homestead owner with a rebate equal to: (1) the statewide average school property tax paid (without regard to a cap); (2) the impact of capping the rebate at the amount of school property tax actually paid; and (3) the aggregate difference in the cost of providing the rebates at the uncapped and capped amounts.
- The number of homestead owners who would have their school property taxes effectively eliminated by the proposed rebate.
- The revenue generated for (1) a 0.1 percentage point increase in the rate of the personal income tax; and (2) a 1.0 percentage point increase in the rate of the sales and use tax.

In addition to providing the estimates noted above, the IFO was asked to analyze the sustainability of the program in future years based on projections of school property taxes and the revenues available from possible increases in (1) personal income tax; (2) sales and use tax; (3) casino gaming revenues; and (4) state lottery funds dedicated to property tax rebates under the Senior Citizens Property Tax and Rent Rebate Program. The specific sources and amounts of the funds to support the proposed rebates were not identified; therefore, the response provides a general analysis by comparing the rate of increase for school

property tax collections with the rates of increase for the various potential revenue sources identified in the request.

The analysis uses data from the Pennsylvania Department of Education, the State Tax Equalization Board and the U.S. Census' American Community Survey to make projections relevant to the rebate program. For example, the IFO estimates that FY 2013-14 school property taxes paid by property owners (and collected by school districts) totals approximately \$12.0 billion. The IFO further estimates that 3.2 million properties would qualify as homesteads under the rebate program, an amount that includes an assumption for additional homeowners who will apply and qualify for the program due to the size and availability of the rebates. Based on the number of homesteads assumed to participate in the rebate program, the IFO attributes approximately \$6.4 billion of FY 2013-14 school property tax collections to owners of homesteads.

The statewide average property tax paid by homesteads (after the Act 1 property tax reductions) is estimated to be \$1,990. A rebate equal to the statewide average for each homestead (without regard to a cap) would cost about \$6.4 billion. If the rebate is capped at the lesser of the statewide average or the actual school property tax paid, the program would cost \$3.9 billion, a difference of \$2.5 billion. Approximately 1.2 million homesteads pay more than the statewide average and would receive a rebate equal to \$1,990. The remaining 2.0 million homesteads would receive a rebate equal to the amount actually paid, thus effectively eliminating school property taxes for such homesteads.

Finally, the sustainability of the proposal is evaluated by comparing the growth rates for current and interim school property taxes to various alternate revenue sources. In general, the rate of growth for personal income tax and sales and use tax is estimated to meet or exceed the property tax growth rate. A more detailed sustainability analysis is not feasible because information on the funding to support the rebate is not available.

The IFO's analysis is summarized, and additional information is provided, in the four enclosures described below.

- **Enclosure 1** provides the school property tax forecast for FY 2013-14 through FY 2019-20. Separate tables provide detail for all properties and for homestead properties. (The estimates in this enclosure do not contain any assumptions related to the qualification of additional homestead properties due to the availability of a rebate under the proposal.) The baseline forecast for all properties is identical to the forecast contained in a letter to Senators Argall, Folmer, Schwank and Yudichak in December 2014. The estimates for homestead properties are based on the December 2014 forecast and the methodologies outlined in a September 2013 letter to Representatives Benninghoff and Mundy. (Copies of these letters are available on the IFO website.)
- **Enclosure 2** contains IFO estimates for various items identified in the request. Specifically, the enclosure provides the number of homesteads, average and median school property taxes paid, the costs of the proposed rebate (with and without a cap based on the statewide average school

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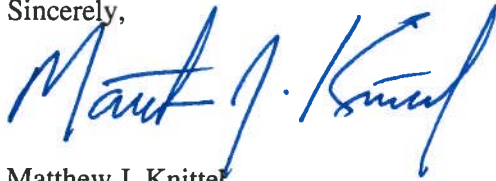
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property tax paid), and the number of homesteads for which school property taxes would be eliminated. The estimates for average and median school property taxes paid, as well as the estimated costs and impacts of the proposed rebate, are based on FY 2013-14.

- **Enclosure 3** provides a sustainability analysis by comparing the projected growth of the personal income tax, the sales and use tax, Act 1 property tax reduction allocations and the property tax/rent rebate program to the projected growth of current and interim homestead school district property tax collections. Growth is measured based on an index using FY 2013-14 as the base year. In addition, enclosure three provides an estimate of the full FY 2015-16 revenue impact for a 0.1 percentage point increase in the personal income tax rate and a 1.0 percentage point increase in the sales and use tax rate.
- **Enclosure 4** describes the data sources and the methodology used to make the estimates.

I hope you find this information useful in your deliberations. Consistent with IFO policy, this letter and the enclosures will be posted to the office's website no later than Friday, March 13, 2015. Please do not hesitate to contact me if you have any questions or comments.

Sincerely,

A handwritten signature in blue ink that reads "Matthew J. Knitter". The signature is written in a cursive style with a large initial "M".

Matthew J. Knitter
Director

Enclosures

Enclosure 1

School Property Tax Forecast - All Properties

(\$ millions)

Revenues	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Current & Interim Collections	11,970	12,335	12,748	13,182	13,592	14,018	14,460
Property Tax Reduction Allocations	525	530	530	530	530	530	530
Subtotal - Current, Interim & PTRA	12,495	12,865	13,278	13,712	14,122	14,548	14,990
Delinquent Collections	412	416	424	437	451	465	479
Total	12,907	13,281	13,702	14,149	14,573	15,013	15,469

School Property Tax Forecast - Estimated Homestead Share

(\$ millions)

Method 1	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Current & Interim Collections	5,598	5,774	5,976	6,189	6,390	6,599	6,815
Property Tax Reduction Allocations	525	530	530	530	530	530	530
Subtotal - Current, Interim & PTRA	6,123	6,304	6,506	6,719	6,920	7,129	7,345
Delinquent Collections	202	204	208	214	221	228	235
Total	6,325	6,508	6,714	6,933	7,141	7,357	7,580

Method 1 Summary: The assessed value of residential property is 70% of the assessed value of all property (STEB). Owner-occupied housing units are 70% of total housing units in PA (U.S. Census Bureau.) Therefore, 49% of the assessed value of all property is attributable to residential property (calculation).

Method 2	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Current & Interim Collections	5,972	6,160	6,375	6,600	6,813	7,035	7,265
Property Tax Reduction Allocations	525	530	530	530	530	530	530
Subtotal - Current, Interim & PTRA	6,497	6,690	6,905	7,130	7,343	7,565	7,795
Delinquent Collections	214	216	220	227	235	242	249
Total	6,711	6,906	7,125	7,357	7,578	7,807	8,044

Method 2 Summary: The assessed value of homestead property is estimated to be 73.4% of the assessed value of residential property and 52% of the assessed value of all property (Legislative Budget and Finance Committee).

Notes: (1) The school property tax forecast is unchanged from the December 2014 forecast detailed in a letter to Senators Argall, Folmer, Schwank and Yudichak. A copy of the letter can be accessed at http://www.ifo.state.pa.us/resources/PDF/SR2014updated_school_district_property_tax_forecast.pdf.

(2) The methods for estimating the homestead share are consistent with the methods outlined in a letter to Representatives Benninghoff and Mundy in September 2013. A copy of the letter can be accessed at: <http://www.ifo.state.pa.us/resources/PDF/SR2013-homestead.pdf>.

Enclosure 2

Summary Statistics	2013-14
Total School Property Tax Levied (SPT) – Excludes Delinquent (\$ millions)	\$12,495
School Property Tax Reduction Allocations (SPTRA) (\$ millions)	\$525
Total School Property Tax Paid – Excludes SPTRA (\$ millions)	\$11,970
Number of Homesteads (increased for added participation due to availability of rebates)	3,223,000
Homestead SPT Paid – Excludes SPTRA and Delinquent (\$ millions)	\$6,414
Average Homestead SPT Paid (\$)	\$1,990
Median for School District Homestead SPT Paid Weighted by Number of Homesteads (\$)	\$1,608
Cost: Average Statewide Homestead SPT Paid for All Homesteads (\$ millions)	\$6,414
Cost: Lower of (1) Statewide Average or (2) Actual Homestead SPT Paid (\$millions)	\$3,945
Excess: Average Rebate for All Homesteads, Less Lower of Average or Actual (\$ millions)	\$2,469
Number of Homesteads Above the Statewide Average SPT	1,183,000
Cost: Rebates for Homesteads Above Statewide Average SPT (\$ millions)	\$2,353
Number of Homesteads Below the Statewide Average SPT	2,040,000
Cost: Rebates for Homesteads Below Statewide Average SPT (\$ millions)	\$1,592

Enclosure 3

Projected Revenue Growth from 2013-14 Base Year

Revenue Source	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Personal Income Tax	1.00	1.05	1.09	1.14	1.19	1.24	1.30
Sales and Use Tax	1.00	1.05	1.09	1.12	1.16	1.20	1.24
Act 1 Prop. Tax Reduction Allocation	1.00	1.01	1.01	1.01	1.01	1.01	1.01
Property Tax/Rent Rebate Program	1.00	1.00	1.02	1.03	1.03	0.99	0.99
Current & Interim Homestead SD Property Tax	1.00	1.03	1.06	1.10	1.14	1.17	1.21

Note: The table displays projected revenue growth from the FY 2013-14 base year (value = 1.0) for each of the specified revenue sources and demonstrates the ability of each revenue source to replace annual current and interim homestead school district property taxes.

PIT Rate Increase

Increase	0.1%	0.5%	1.0%	1.5%	2.0%
2015-16	\$405	\$2,023	\$4,043	\$6,058	\$8,070

Notes: The analysis incorporates minor reductions in the number of hours worked and a slight increase in non-compliance in response to the higher tax rates. In general each 0.1% increase in the PIT rate generates approximately \$400 million. The table reflects a full year impact for FY 2015-16. Amounts are in millions of dollars.

SUT Rate Increase

Increase	1.0%	2.0%	3.0%
2015-16	\$1,547	\$3,048	\$4,500

Notes: The analysis assumes a reduction in the consumption of taxable items and an increase in non-compliance in response to the higher tax rates. In general each 1.0% increase in the SUT rate generates approximately \$1.5 billion. The table reflects a full year impact for FY 2015-16 and assumes that the percent of revenue transferred to the Public Transportation Assistance Fund and the Public Transportation Trust Fund remains unchanged. Amounts are in millions of dollars.

Enclosure 4

Summary of Methodology

The analysis of the proposal utilizes Independent Fiscal Office (IFO) estimates of school property tax collections, by district, for fiscal year 2013-14. The proposal provides that the Act 1 school property tax reduction allocations would remain in place; therefore, the analysis computes a fiscal impact based on the amount of current and interim school property taxes remitted by the homestead owner(s). In addition, the following data, sources and assumptions are utilized;

- Residential property taxes, as a share of total school property taxes by school district, are based on 2013 assessment data published by the State Tax Equalization Board.
- Homestead property as a share of residential property for all school districts is consistent with “Method 2” outlined in an IFO letter to Representatives Benninghoff and Mundy in September 2013. In addition, the share of homestead property is increased by five percentage points to reflect added participation due to the availability of significant rebates in the proposal.
- The number of homesteads for each school district is based on the highest number of homesteads reported for the district by the Pennsylvania Department of Education for fiscal years 2008-09 through 2014-15. The number of homesteads in Philadelphia is based on information published by the Philadelphia Office of Property Assessment. In addition, the number of homesteads for all districts is increased by five percent to reflect added participation due to the availability of significant rebates in the proposal.
- The distribution of school property tax collections is based on the IFO’s analysis of data from the 2009-2013 American Community Survey (ACS) five-year public use microdata sample (PUMS) database produced by the U.S. Census Bureau. Owner-occupied properties in each of 35 groups (counties and groupings of counties) were arrayed, divided into deciles and assigned a percentage representing the share of total home values within the decile. The distribution of school property taxes within each group is assumed to follow the distribution of home values in the group.

The analysis computes the statewide average school property tax paid by homesteads. The distribution of school property taxes, informed by the ACS data, is used to determine the point in the distribution in which the statewide average falls for each school district. This information is used to determine the number of homesteads higher and lower than the statewide average in the district.

- For homesteads with school property taxes that are lower than the statewide average, the analysis estimates: (1) the impact of providing a full rebate; (2) the impact of the rebate capped at the school property tax paid; and (3) the difference between the two amounts. Taxpayers in this category would have their school property taxes eliminated.
- For homesteads with school property taxes that are higher than the statewide average, the analysis estimates the impact of providing a rebate equal to the statewide average. Taxpayers in this category would have their school property taxes reduced by the statewide average school property tax.