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Senate of Pennsylvania

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December 7, 2015

Senate Bill 76: The Rest of the Story

With respect and high regard for my colleagues in the State Senate and for the Pennsylvania taxpayers who support Senate Bill 76 (SB76), the so-called “Property Tax Independence Act,” I want to outline here some lesser-known and certainly less-heralded aspects of this legislation which informed my judgment and my recent vote on it.

To begin, it would be inexcusable for me to conclude that our current property tax system is without need for change or reform. As I stated in a recent Senate Finance Committee meeting, the system is broken, inequitable and punitive on fixed income seniors as well as on younger, lower income families trying to buy their first home.

Adequately funding public education is an urgent imperative. Protecting the financial security of aging and lower income homeowners is also an urgent imperative. As we consider the passage of legislation to correct what is – for many Pennsylvanians – a very real school property tax crisis, we need to find the proper balance to address both of these simultaneously.

As relates to SB76, if it were approved in its current form by the General Assembly and signed into law by the Governor, it would not immediately eliminate school property taxes in every school district in the state.

Only 8 of our 500 school districts statewide are without debt. This debt was incurred to fund school improvement and school building projects for our children. Like most families, and indeed like most public and private entities, borrowing is a common and necessary practice if done responsibly. Approximately \$25 billion in outstanding debt has been incurred by our school districts and this debt is secured in large part by local school districts’ pledge of FUTURE SCHOOL PROPERTY TAXES. Under the terms of Senate Bill 76, all taxpayers in the 492 school districts with debt would continue to receive a property tax bill until that debt is retired over the next five, ten, fifteen, twenty or even thirty years. Additionally, SB 76 speaks only to school property taxes. All property owners in the state will still continue to receive a local municipal and county property tax bill.

If SB76 were to become law, your personal income tax would increase 61%, from 3.07% to 4.95% and the PA Sales and Use Tax would increase 17%, from 6% to 7% for most Pennsylvanians. Sales taxes in Pittsburgh and Philadelphia would be even higher and we would see some of the highest sales taxes in the nation in our two largest cities. Further, and very importantly, Pennsylvanians would also pay sales taxes on approximately 60 additional products and services including new sales taxes on food, diapers, legal services,

daycare, accounting services, public transportation; advertising and public relations; cable TV; fees at museums and historical sites; behavioral health and substance abuse services; developmental disability and vocational rehabilitation services; personal hygiene products; textbooks; non-prescription drugs; home health care services; nursing care and assisted living facilities, funeral services and caskets. There are dozens more. Senate Bill 76 doesn't immediately provide property tax elimination but it does tax every aspect of our daily lives from the cradle to the grave.

Depending on which data source you cite, SB76 represents a tax shift of between \$12 and \$14 billion – shifting billions of dollars in taxes from property owners onto individuals and small businesses in the form of increased personal income taxes and sales taxes.

It is worth noting that the SB76 tax shift offers an enormous tax break for the commercial and industrial corporate community which currently pays an estimated \$3 billion in local school property taxes. Under SB76, corporate entities such as ExxonMobil, Sheetz, Walmart, PNC Bank, etc., will no longer pay nearly \$3 billion in local school property taxes in this state. That \$3 billion would also be shifted on to individual taxpayers in the form of increased income and sales taxes. The fact is, under SB76 lower income people in Pennsylvania will be paying much higher taxes to provide tax relief to more affluent property owners.

Also, the current federal deduction for property tax payments enjoyed by many Pennsylvanians who itemize deductions in their federal tax filings to the Internal Revenue Service will be lost if SB76 were to become law. The PA Independent Fiscal Office (IFO) reports that the loss in this federal tax deduction will result in \$300 million in additional federal tax liability for individual homeowners and \$290 million in additional tax liability to pass-through entities – shareholders, partners and business owners. That's nearly \$600 million in additional Pennsylvania dollars going to the IRS that will not be spent here.

SB76 also exempts sales tax on business-to-business transactions but not on business-to-consumer transactions. So, if Walmart should engage legal or accounting services, they would not pay sales taxes on those services. If, however, individual taxpayers should seek legal action against Walmart, they would be required to pay sales taxes on those legal services. This, by the way, may be illegal under the uniformity provisions of our PA Constitution.

It is also important to note the other adverse affects SB76 would have on local economies. Small businesses – which account for most of the jobs in this state and which are incorporated as S-Corporations – pay corporate taxes to the state at the Personal Income Tax (PIT) rate. A 61% PIT increase, as suggested in the most recent version of SB76, would significantly cut into the already tight profit margins of these small businesses throughout the state. Businesses, large and small, will be further impacted by the increase in the income taxes and sales taxes because such increases will significantly affect consumer buying power and will change the timing and the frequency of purchasing decisions – particularly those decisions made by lower income earners.

Families and individuals who rent apartments are currently paying their share of property taxes via their rent payments to their landlords who, in turn, pay property taxes on their income properties. If SB76 became law, I am very doubtful that many landlords across the state would reduce rental rates even if their property taxes go down or go away – meaning that renters, often lower income families – will be paying much higher income and sales taxes with little hope for a reduction in their monthly rent.

Some of the proponents of SB76 have been less than forthright with the citizens of this state on ALL of the impacts of this legislation. A pronouncement on the elimination of school property taxes, while very attractive in its own right, has, I believe, obscured some of the other less desirable impacts this legislation could have in our state.

Notwithstanding constant “tweaks” by the makers of the bill to try to win support for it or to address criticisms raised over months and months of debate, a good deal of the data and the analysis that I’ve seen on SB76 indicates not only the regressive nature of the taxes suggested – meaning that tax burdens will be significantly greater on lower income citizens – but it also threatens our capacity to properly and adequately fund K-12 public education in our state – which is a Constitutional obligation.

The Independent Fiscal Office reviewed a prior iteration of SB76 and concluded that it would underfund our K-12 school districts by over \$1 billion within three years of its implementation. Proponents of the legislation cite that the Pennsylvania Constitution protects life, liberty and property. That is correct. They often fail, however, to cite another important provision of the Pennsylvania Constitution which requires that the Commonwealth provide a “thorough and efficient” public education to our children.

The IFO report concluded that if SB76 had been state law from Fiscal Year 2001/02 through Fiscal Year 2012/13, Pennsylvania would have collected between \$9.3 and \$27.5 billion fewer dollars than required to meet the actual year-to-year distributions made to public schools during that decade under the state’s current basic education funding formula.

The IFO noted what many economists conclude, that despite its many flaws, the property tax is more stable and predictable than sales and income taxes. The latter are far more volatile depending upon the performance of our state and national economy. Recessions usually cause sales and income taxes to drop precipitously. In FY 2013/14, for instance, personal income tax and sales tax collections were \$400 million less than what we estimated the state would receive.

Also, while some may consider this a positive consequence of SB76, it bears noting that under this proposal ALL public education funding will be collected by and allocated from Harrisburg. This will serve to centralize power and influence in the state Capitol, diluting the role of elected school boards in public education. The bill also fails to address the implications of SB76 on future cash flows to our local schools. During the current 5 month budget impasse, for instance, local school districts have been relying upon local taxes to bridge a gap that will later be filled by state dollars once a state budget is signed into law. Under SB76, our districts will have no local tax revenue upon which to rely when state funds are not forthcoming from Harrisburg.

Additionally, it is unclear under SB76 how a local school district will be able to responsibly borrow for future school improvement or construction projects under the law. Perhaps only by referendum approval by local voters for the imposition of a local earned income tax, would districts be permitted to incur such debt. As referendums for increased taxes are almost never approved by local voters, would we not face the risk that important school maintenance would be delayed or foregone and that the conditions of our schools would begin to deteriorate?

As I stated earlier, I agree that we need reform and we need to strike a proper balance in the manner in which we fund public education and provide fiscal relief to taxpayers. Included in this “proper balance” has to be consideration of the state’s share of funding K-12 public education. The national average for states’ share is 45%. In Pennsylvania, on average, the state’s share is 34%. As a result, local tax bases throughout the state are bearing two-thirds of the total cost of providing a K-12 public education in Pennsylvania. For every \$1 coming from Harrisburg, local taxpayers are paying \$2 for our public schools.

This imbalance between the state and local share of funding public education is unsustainable and irresponsible. The failure of the state to fund at least half of the cost of public education has put enormous pressure on local school boards to seek funding from local property owners. As a direct result of the \$1

billion cut in public education funding under the Corbett Administration, over 70% of all school districts across the state raised local property taxes.

Consensus has been difficult to achieve on property tax relief efforts suggested in Harrisburg because of the disproportionate ratio of tax burden to state education funds in diverse regions of Pennsylvania. In affluent districts, the state provides proportionately less money to local school districts. Further, a significant proportion of sales and income taxes tend to come from comparatively more affluent communities. So, significant increases in sales and income taxes impose considerable weight on taxpayers in some parts of the state while the amount of funding coming back to these communities from Harrisburg is proportionately less than that which is distributed to poorer or more rural school districts. SB76 has the effect of further aggravating the divide between more affluent and less affluent school districts and all the work done recently at the state level to improve fairness in the basic education funding formula for our public schools is rendered useless. For a thorough, fact-based summary and county by county data on property taxes please review the following link: https://pennbpc.org/sites/pennbpc.org/files/20141002_PropTaxPaper.pdf

Again, as I noted above, the current property tax system is flawed. It is not uniform in its affects on local taxpayers throughout the state and it is often punitive to retirement or fixed-income households. Some counties have acted responsibly in keeping local real estate assessments current and reasonably predictable over time while many other counties have not. In my district in Lackawanna County, for instance, local real estate values have not been reassessed since 1968.

This uneven and somewhat arbitrary local circumstance has been – and will continue to be – punitive on poorer, fixed-income, aging homeowners who want to stay in their homes as long as they can reasonably afford to do so. I acknowledge this crisis for many of our seniors and lower income property owners and I am committed to a responsible solution that can significantly reduce and, if possible, eliminate the property tax burden on these lower income property owners. We must, however, assure sufficient, predictable and reliable state financial support for public education.

The Senate Democratic Caucus proposed such a plan that we called the “PA Home Rebate Plan”. If legislated and signed into law it would have provided RESIDENTIAL property owners a rebate on property taxes paid equal to 100% of the school property taxes paid, not to exceed \$1,990. It also would have provided a \$500 rebate for renters with household incomes of \$50,000 or less.

Under our plan approximately 2 million Pennsylvania homeowners would have their school property taxes effectively eliminated through the rebate which would be equal to the actual amount of school taxes paid. An additional 1.2 million homeowners would receive the maximum rebate to significantly reduce their school property tax burden. According to the Governor’s office, an estimated 800,000 renters would be eligible for the \$500 rebate. For more information on the Senate Democratic Caucus PA Home Rebate Plan please follow this link: <http://www.pasenate.com/pennsylvania-home-rebate-plan>

I favor the “PA Home Rebate Plan” over SB76 because it is not as regressive; it provides significant relief to millions of homeowners and renters; it does not give the corporate community an enormous tax cut by shifting their share of the cost of public education to individual taxpayers; it would not have as serious adverse impact on Pennsylvania’s small business community; it will retain a reasonable measure of local responsibility over public education; and it will ensure no threat to or interruption of cash flow to local school districts.

I have outlined here my concerns about SB76 and I have also suggested a reasonable alternative school property tax relief plan but all of this misses an important set of issues which have been conspicuously absent from this entire debate. These issues are those which, if taken together and addressed properly by

state government, would have extraordinary impact on the future of our state and on the quality of public education going forward. By ensuring more responsible tax policy and greater efficiency and accountability at the state and the local level, they would improve the quality of life for our citizens and bolster economic growth in this Commonwealth. They include but are not limited to the following:

- School district consolidation or the consolidation of school district administrative functions and personnel to achieve more efficiency and to improve purchasing power;
- Consolidation of health care plans for all school district personnel into one plan thus removing the primary issue driving school districts' costs and school district strikes;
- Mandatory, periodic and predictable county reassessment of real estate values or the removal of local reassessment in favor of a statewide and state-level plan for property value reassessment;
- A commitment that the Commonwealth of Pennsylvania meet at least 50% of the total cost of K-12 public education annually;
- Responsible state pension reform that assures fairness to taxpayers while protecting retirement security for our teachers and other school district workers;
- A dramatic reduction in standardized testing which costs the state and local school districts hundreds of millions of dollars and does very little to add value or promise for children in public education;
- Significant charter school – and particularly cyber charter – reform, to ensure equity in performance and outcome expectations and in the per pupil investment we make in all public K-12 schools across the Commonwealth;
- Levying a reasonable and responsible severance tax on the Marcellus Shale natural gas industry in PA to bring us in line with ALL other states with natural gas production and to ensure additional state revenue for investment in public education, thus relieving the local school property tax burden; and
- Closing the so-called Delaware loophole which enables large, multi-national corporations to legally engage in state tax avoidance. Additional revenues achieved by a more fair distribution of the state's overall tax burden would be favorable for individuals and small businesses while enabling proper state investment in public education to reduce the local school property tax burden.

Thank you for your attention and consideration of this rather lengthy explanation.

Sincerely,

A handwritten signature in black ink that reads "John P. Blake". The signature is stylized, with the first letters of the first and last names being large and prominent.

John P. Blake
Senate of Pennsylvania
22nd District