# How to Reduce the Pressure on the Property Tax and Ease the Fiscal Burden on Struggling Local Governments

A Fiscal Policy Institute Presentation by Frank Mauro
www.fiscalpolicy.org

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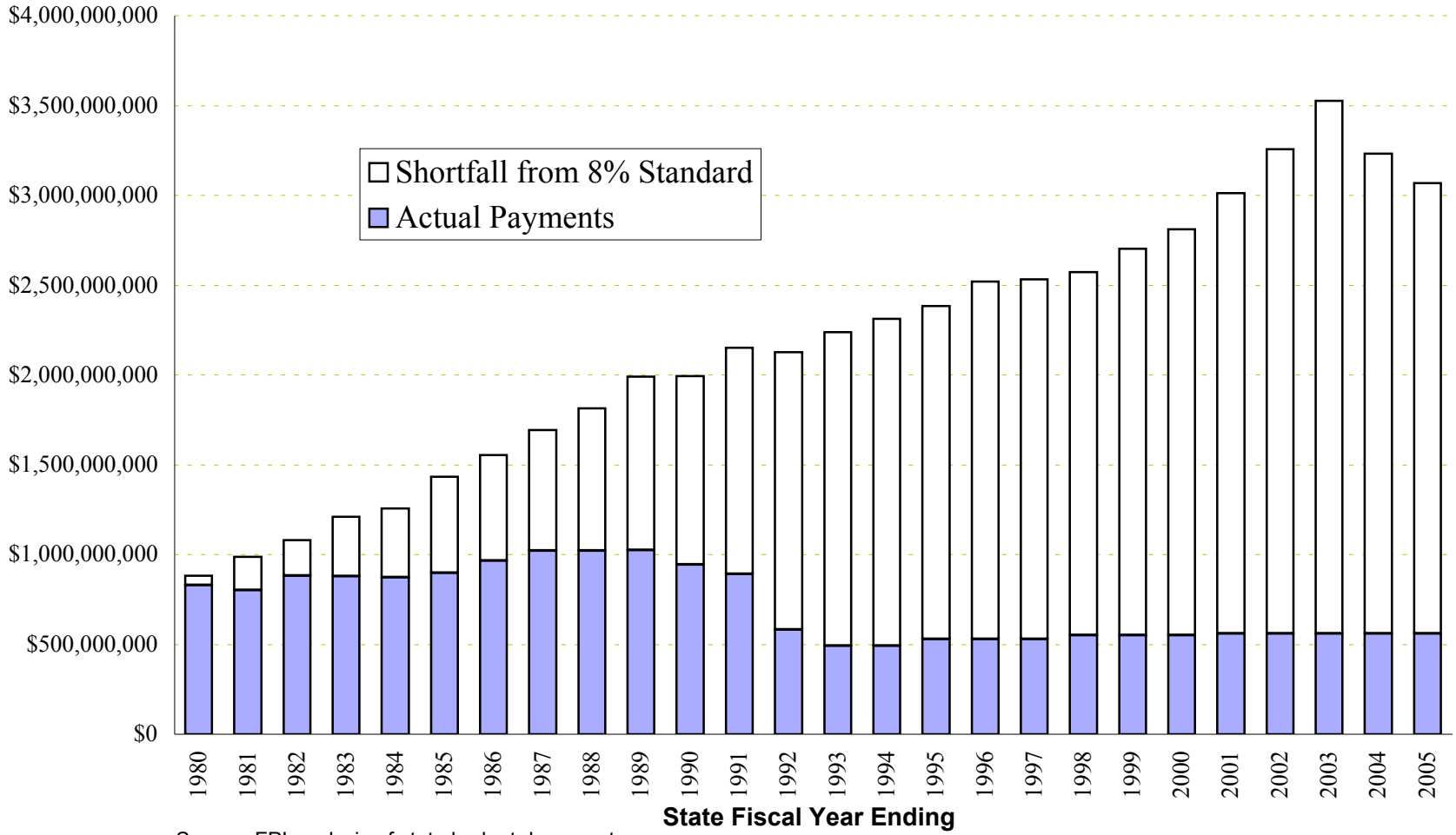
The property tax is an important part of New York State's state-local tax system. But state policies have placed great pressure on this tax base and institutionalized unnecessary inequities in the operation of this tax.

New York has also established an incredible number of property tax exemptions which are intended to deal with this tax's negative aspects but which instead serve to make the tax more inequitable.

The governor and the legislature should undertake a comprehensive reevaluation of all of the state's real property tax relief programs and work toward an integrated circuit breaker-like variation of STAR that is consistent with the principles of horizontal and vertical equity.

Even more importantly, New York's state-local fiscal relationships should be reworked in ways that recognize the fact that tax base resources (from taxable income to taxable sales to the full value of taxable real property) are not by some magic divided among localities in the same proportions as needs.

# New York State has cut its revenue sharing with local governments to help balance its own budget.




Source: FPI analysis of state budget documents.

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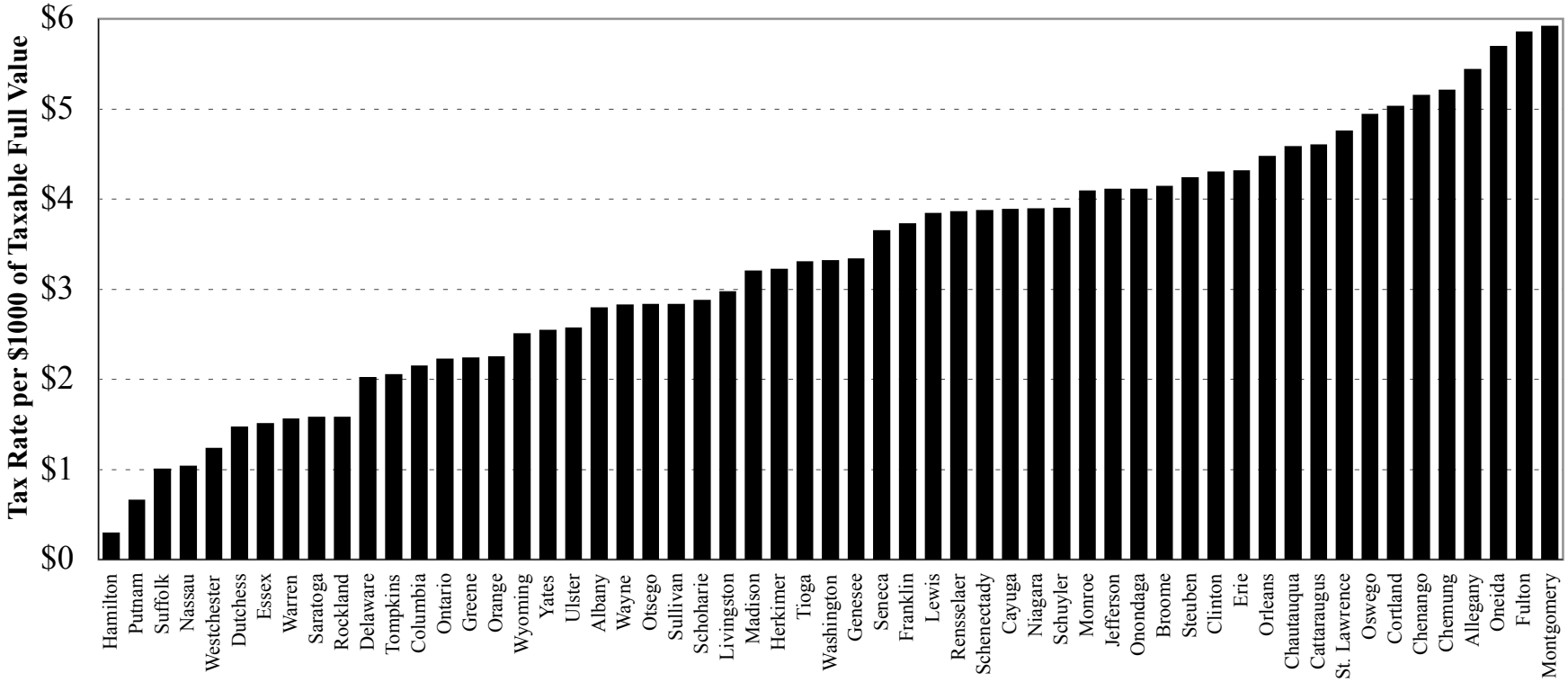
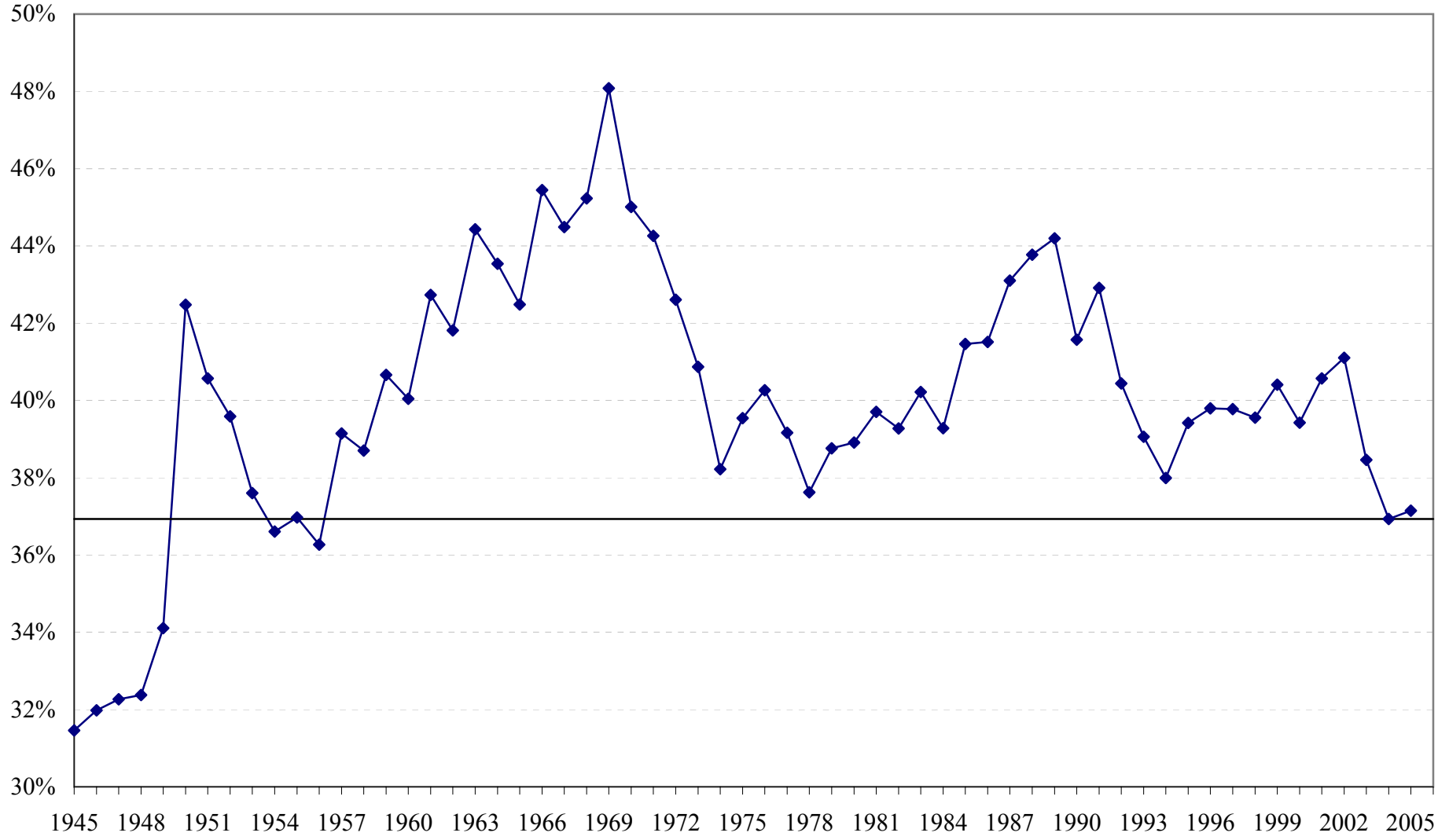
## New York's method of financing Medicaid places great pressure on counties with weak tax bases relative to their concentrations of needy individuals.

Tax Rate Per $1000 of Taxable Full Value Necessary to Cover Local Share of Medicaid Costs, excluding New York City at $9.78 per $1000.



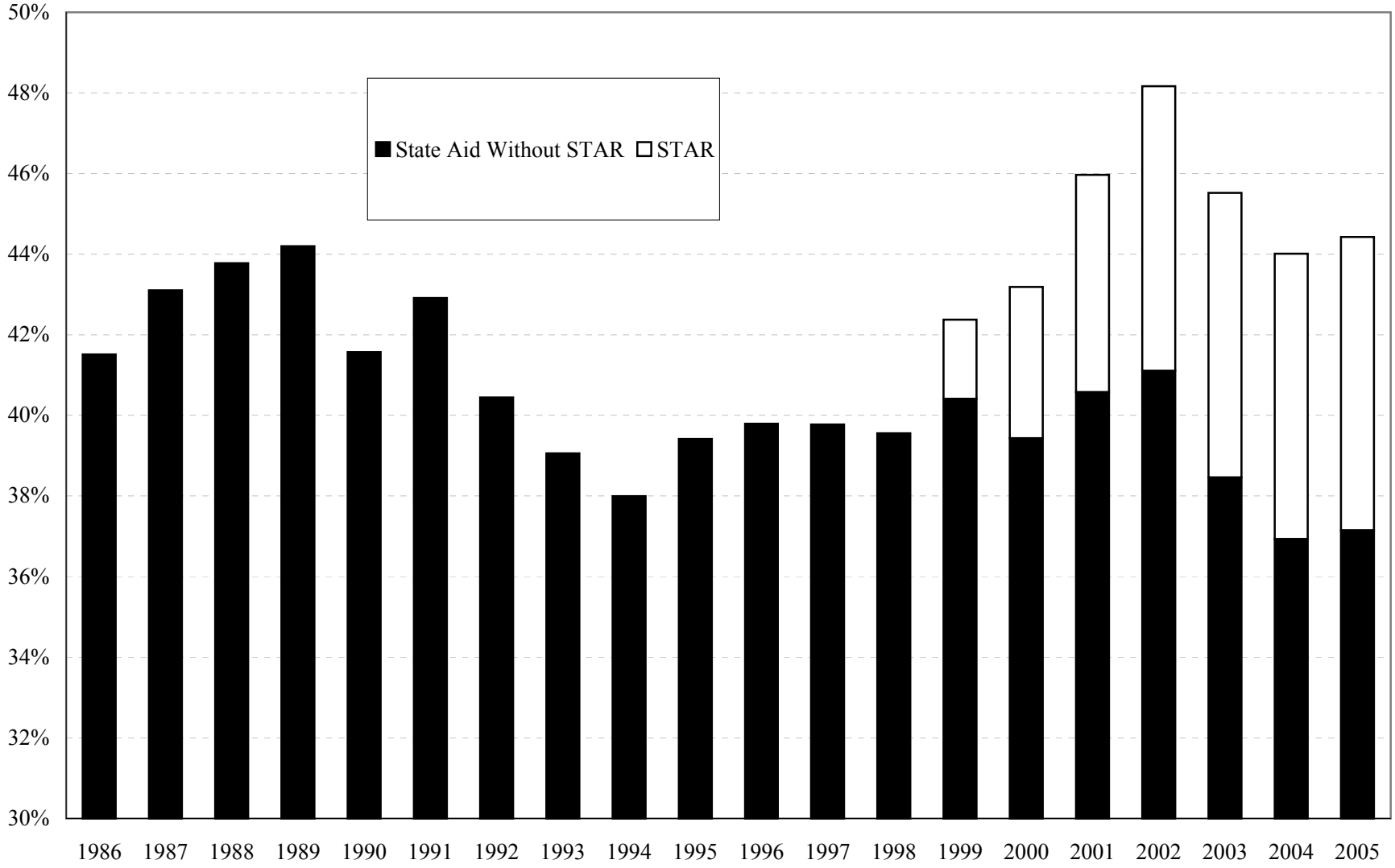

Sources: 2003 Medicaid Expenditures from NYS Department of Health. 2003 full value from Office of State Comptroller.

# During the last several years, State Aid as a percent of public school budgets has been at a 50-year low.



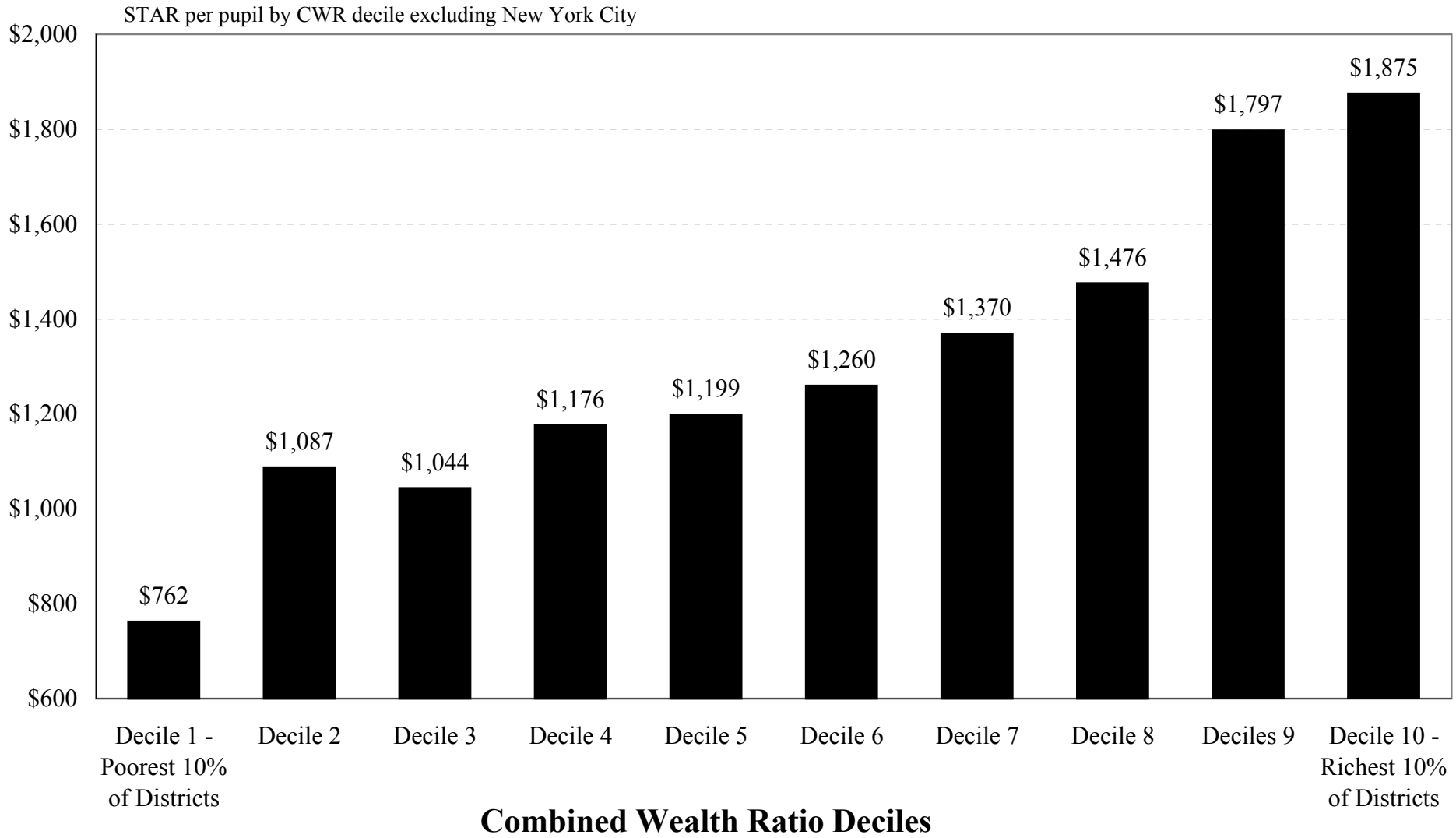

Source: State Education Department, Analysis of School District Finances in NYS SChool Districts, December 2004.

# When STAR is taken into consideration, the State covers a larger share of public school budgets.




Source: State Education Department, Analysis of School District Finances in NYS School Districts, December 2004.

# But STAR is distributed in a very different manner than other state aid to public schools.



## STAR provides much more state revenue per pupil to schools in the New York City suburbs than it provides to schools in New York City and other needy, urban school districts.

| | 2005-2006 STAR Revenue | 2005-2006 Enrollment | Total STAR per Pupil |
|---|---|---|---|
| **5 NYC-Area Suburban Counties** | $1,137,983,549 | 681,378 | $1,670 |
| **State Total/State Average** | $3,163,973,078 | 2,827,978 | $1,119 |
| **Rest of State** | $1,216,628,878 | 1,111,611 | $1,094 |
| **Binghamton** | $6,451,229 | 6,374 | $1,012 |
| **Albany** | $10,225,351 | 10,424 | $981 |
| **Utica** | $9,091,957 | 9,308 | $977 |
| **Newburgh** | $11,823,684 | 12,459 | $949 |
| **New York City -with PIT Supplement** | $809,360,651 | 1,034,989 | $782 |
| **Poughkeepsie** | $2,979,298 | 4,887 | $610 |
| **Syracuse** | $11,709,790 | 22,584 | $518 |
| **Buffalo** | $17,668,614 | 41,388 | $427 |
| **Rochester** | $14,259,434 | 36,710 | $388 |
| **New York City - without PIT Supplement** | $165,360,651 | 1,034,989 | $160 |

# STAR: New York's Flawed Property Tax Relief Mechanism

- Under STAR, all owner-occupied residential dwellings in the state are eligible for a state-funded homestead exemption of at least $30,000. In counties in which the median home value is greater than the statewide median home value, the value of this exemption is prorated upward by the ratio of the county median home value to the statewide median home value. In Westchester County, the county with the highest median home value, this "sales price differential factor" was 2.8833 making the value of the exemption about $86,500 and, according to the Division of the Budget's website, it is estimated to be $90,000 next year.

- Homeowners aged 65 and over, with incomes below $60,000 adjusted upward for changes in the cost of living since 2003 (for the 2006-07 school year this income threshold is $66,050) are eligible for an "enhanced" STAR exemption of $50,000. This exemption is also prorated up in counties with median home values above the statewide median. In this year's Executive Budget, the Governor has proposed to increase the enhanced exemption from $50,000 to $56,800 to reflect increases in the cost of living since 2001.

- In the 2001-2002 school year, the first year in which STAR was fully phased-in, the NYS Office of Real Property Services reported that there were nearly 640,000 "enhanced" STAR exemptions and more than 2.2 million "basic" STAR exemptions representing $118.9 billion in exempt value. It is estimated that in the current school year, these numbers have increased to about 652,000 "enhanced" STAR exemptions and 2.77 million "basic" STAR exemptions.

# STAR disadvantages renters and the needy school districts in which the state's renters are concentrated.

- Because STAR provides reimbursements to school districts only for the property taxes on owner-occupied dwellings, it substantially disadvantages those communities (primarily cities) with large numbers of renters.

- State reimbursements to school districts, during 2005-06, for these STAR property tax exemptions are estimated to be about $2.52 billion with about $163 million (or 6.46%) of that total going to New York City. New York City's low share of the property tax reimbursements is attributable to two factors - its relatively high percentage of renter-occupied dwellings and the special calculations of STAR benefits established for the Big 5 cities. In recognition of the limited benefits that would accrue to New York City under the STAR property tax exemption, the initial STAR legislation established a special New York City STAR Supplement which provides for a state-funded reduction in the NYC resident income tax. This element of the program is providing NYC residents with an estimated $595 million in income tax relief in 2005-06 with the state reimbursing the city that amount, bringing the estimated total cost of the STAR program that year to $3.1 billion with 24% of the benefits going to New York City.

- With STAR representing 40% of the increases in state revenue to school districts since its creation, this serves to undercut the effectiveness of the state aid system in addressing fiscal disparities among school districts. While New York City is treated unfairly by STAR, other school districts with large percentages of renters are treated even worse since they do not benefit from anything like the NYC STAR Supplement.

# The STAR program, as currently structured, is not effectively targeted - thus costing much more than it needs to for the amount of relief that it gives to taxpayers who are overburdened by high property taxes.

- One of the basic flaws of the STAR program is that, with the exception of the "enhanced" STAR available to seniors with income below the $60,000 (adjusted for inflation) cutoff, it provides the same benefit to all homeowners in a particular school district (or in a municipal segment of a school district that is located in more than one municipality) regardless of their income levels, or their property tax bills, or more importantly, the relationship between their income levels and their property tax bills. This creates two significant problems.

  - First, it prevents the program from delivering on its rhetorical premise - that it is designed to protect New Yorkers from being "forced from their homes because of escalating school property taxes."

  - Second, it provides a significant amount of relief to a significant number of homeowners for whom property taxes represent only a relatively small percentage of their income.

- The combined result of these two shortcomings is that STAR, as currently structured, costs much more than it needs to for the amount of relief that it actually provides to homeowners who are truly overburdened by their property taxes. Similarly, a reformed STAR program could provide much more relief to those who need it at a greatly reduced cost.

# The STAR program provides different benefits to taxpayers with the same incomes and the same property tax bills - depending on where they live.

- A second basic flaw of the current program is that similarly situated taxpayers are treated very differently depending on where they live. Two taxpayers with the same incomes and the same property tax bills will get very different amounts of relief through STAR if one of those taxpayers lives in one of the seven counties with median home values of the state median, and the other does not.

- While, on average, residents of some communities may have higher incomes and higher property tax bills than people in some other communities, these averages should not serve as the basis for treating two similarly situated New York taxpayers.

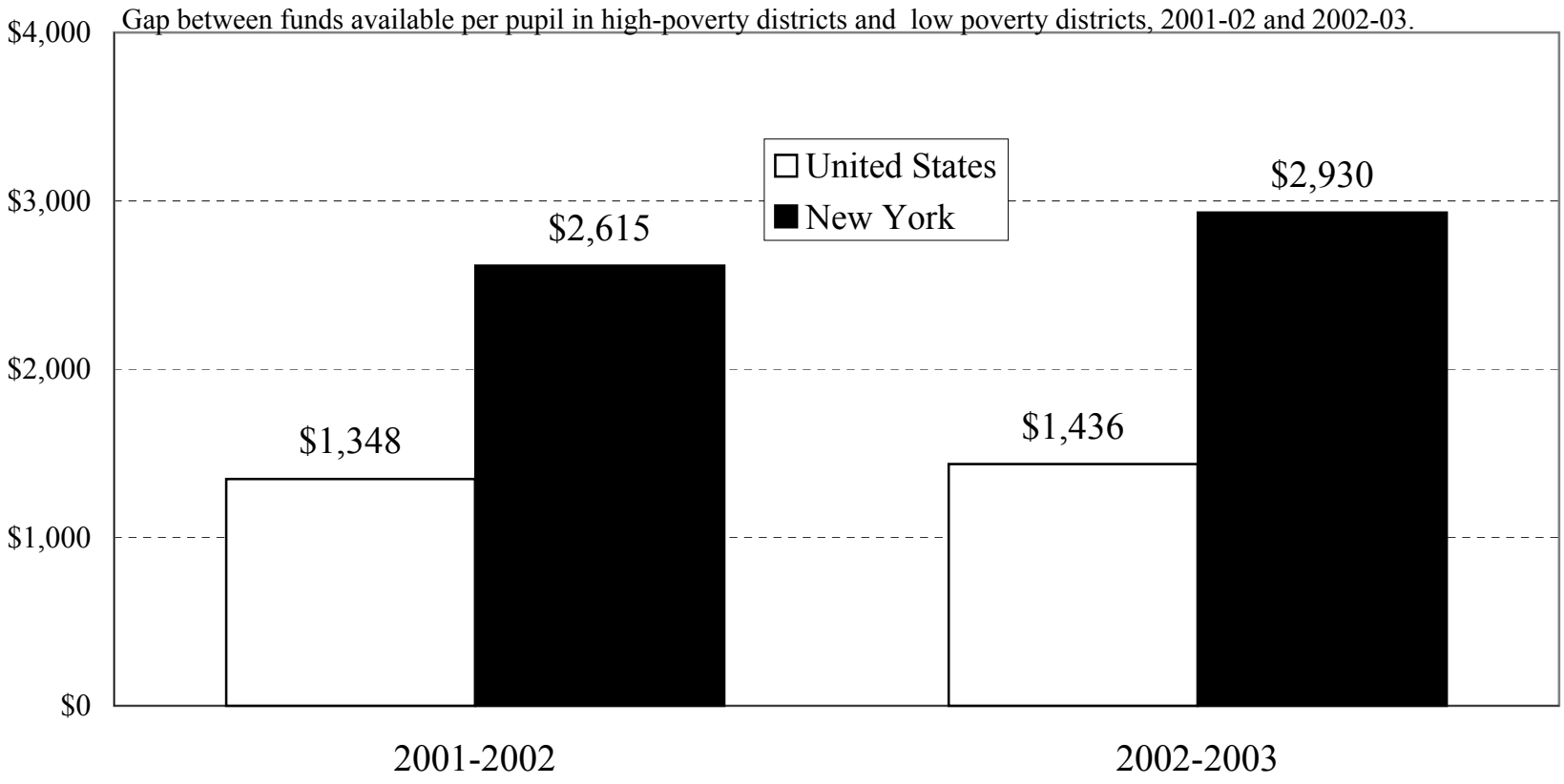
- While a higher percentage of the residents of one community may be in a particular income/property category than the residents of another community, all of the taxpayers with that income/property tax mix should be treated the same.

# Governor Pataki's STAR Plus proposal was fundamentally inconsistent with a statewide solution to the Court of Appeals decision in the CFE case.

- The Governor's proposed STAR Plus Rebate program would have provided $400 rebate checks to residents in districts that limited their spending increases to the lesser of 4% or 120% of the increase in the Consumer Price Index.
- Under the proposal advanced by Gov. Pataki in the proceeding before the Special Masters, 177 of the 639 districts analyzed needed to increase spending for purposes of providing a Sound Basic Education over and above the levels needed to meet ordinary annual changes in the cost of educational inputs. Modifying this model to make the corrections recommended by the Referees in the CFE case, 477 districts would require additional spending over and above inflationary increases.
- A percentage-based spending cap of this type would institutionalize and exacerbate the inequities inherent in the current system, and this particular cap (the lower of 4% or 120% of the CPI[2]) is inconsistent with the costs increases school districts currently face, as documented by the New York State Educational Conference Board has documented the fact that school district costs are increasing at a much faster rate than the change in the CPI.
- The legislation proposed by Gov. Pataki exempt from this proposed cap "court ordered spending to provide a sound basic education" even though Gov. Pataki and the legislative leaders had all said that they want a legislatively-enacted statewide solution to the CFE case without every needy school district in the state having to go to court.

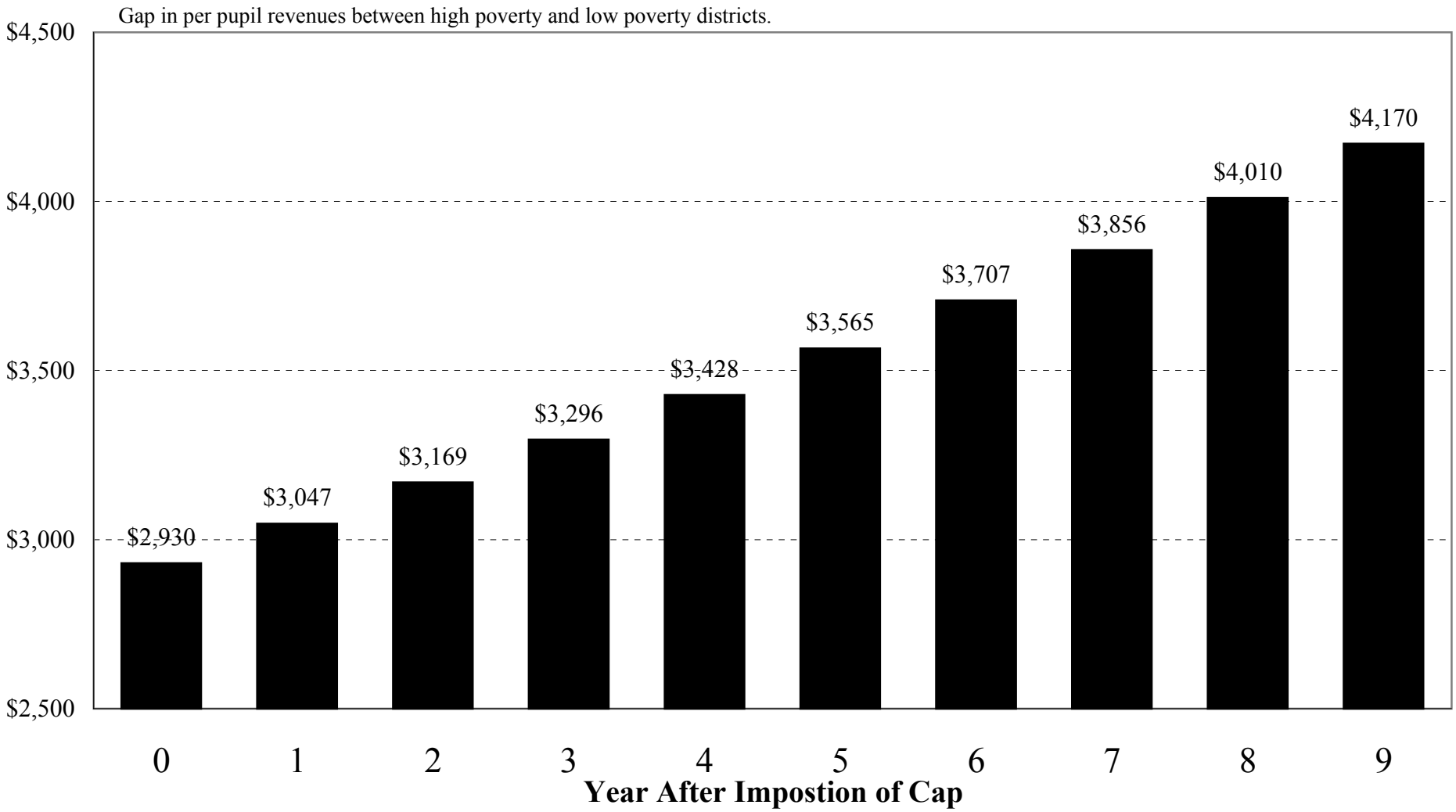
[2] The proposal sets the percentage increase cap using the average of changes in two national CPI indices despite the fact that the experts engaged by the State in the CFE case recommended the use of the NYC regional CPI rather than the national CPI indices. (The NYC regional CPI tends to increase at a faster rate than the national CPI.)

# New York has the largest gap between the resources available in high-poverty and low-poverty school districts of any state in the nation and that gap is growing.




Source: The Education Trust, "The Funding Gap 2004: Many States Still Shortchange Low-income and Minority Students," October 2004 and "The Funding Gap 2005: Low-Income and Minority Students Shortchanged by Most States," Winter 2005. Available at www2.edtrust.org.

# If Gov. Pataki's STAR Plus Spending Cap were successful in holding all districts to the same percentage increases in spending, this gap would grow wider each year.

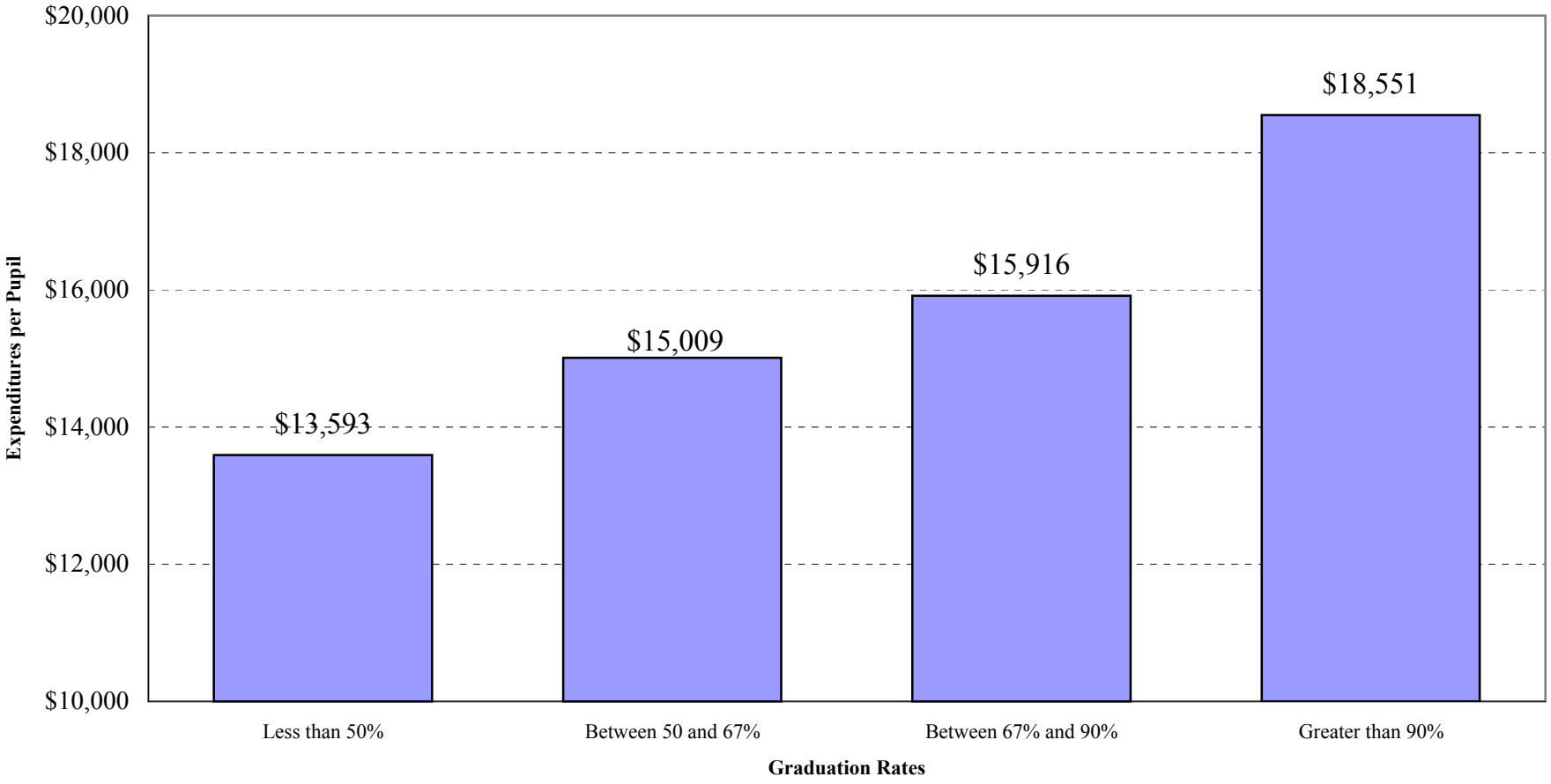


# Impact of a Cap on Increases in School Spending on Two Neighboring Westchester County School Districts

| Base Year Data from Standard & Poor's Model* | | | Four Years Later Assuming that Costs Per Pupil Increase 4% Per Year and that a Spending Cap is Effective in Limiting the Growth in Actual Spending Per Pupil to 4% Per Year | | |
|---|---|---|---|---|---|
| | **Harrison** | **Port Chester** | | **Harrison** | **Port Chester** |
| Enrollment | 3,336 | 3,564 | Enrollment | 3,336 | 3,564 |
| Economically Disadvantaged | 5% | 42% | Economically Disadvantaged | 5% | 42% |
| Estimated Actual Spending Per Pupil | 16,681 | 12,048 | Estimated Actual Spending Per Pupil | 19,515 | 14,095 |
| Needed Resources Per Pupil Under Pataki Proposal | 11,452 | 13,039 | Needed Resources Per Pupil Under Pataki Proposal | 13,397 | 15,254 |
| Over/(Under) | 5,229 | (991) | Over/(Under) | 6,117 | (1,159) |

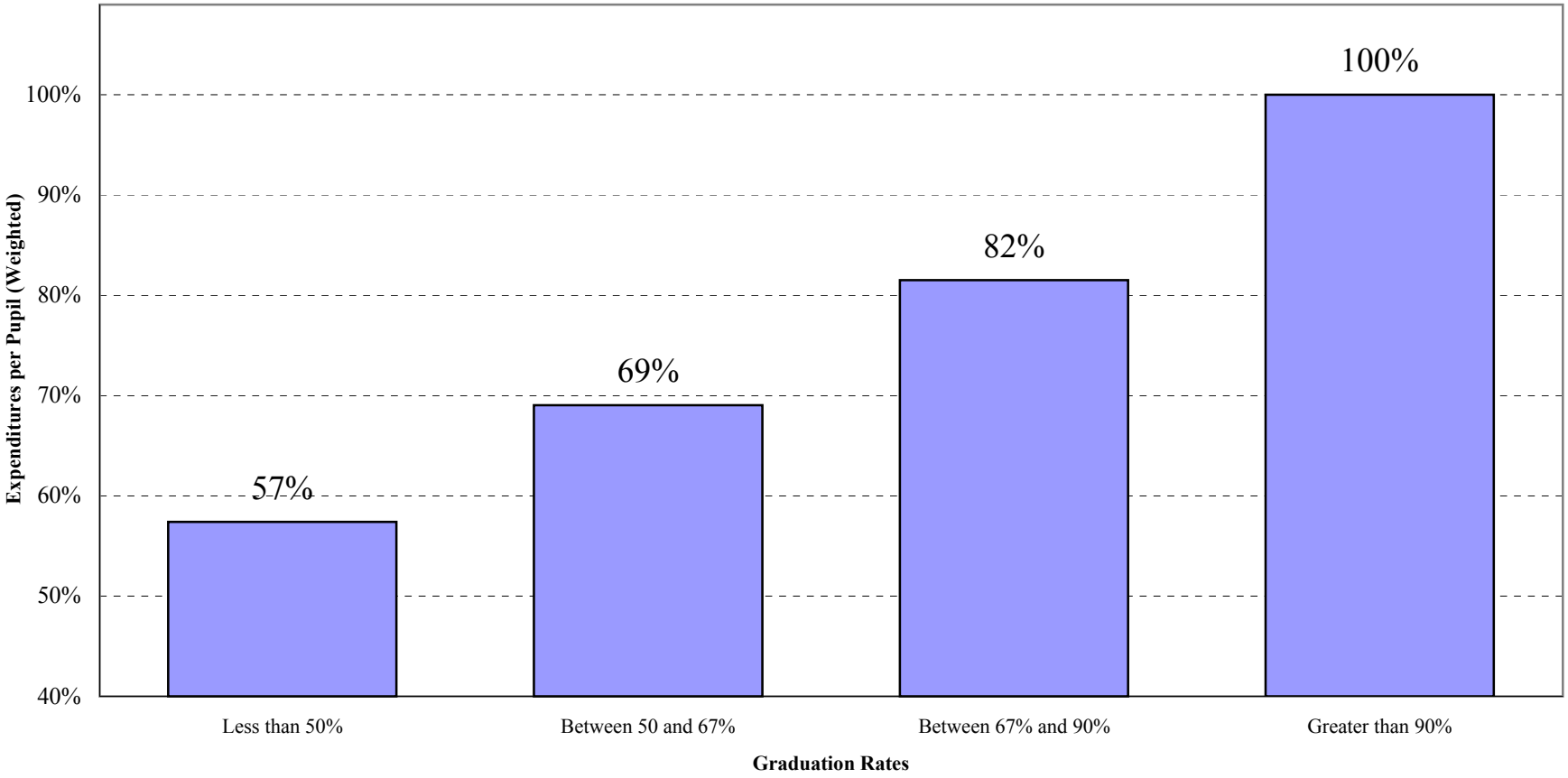
*Expenditures are for the 2002-03 school yesr, in January 2004 dolars, not including debt service and transportation

# Relationship between Spending Per-Pupil and Graduation Rates



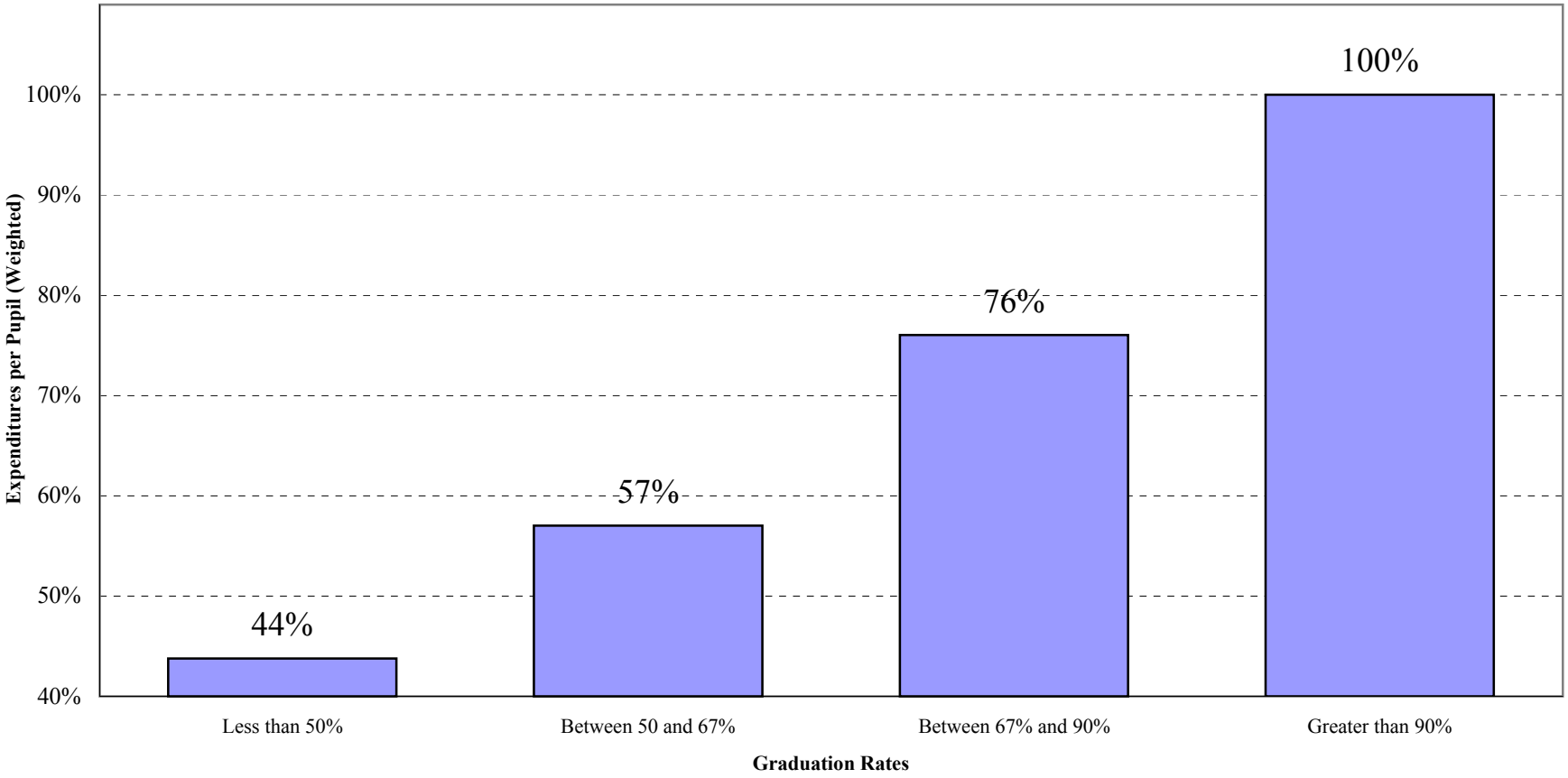
# Relationship between Spending Per-Pupil and Graduation Rates
## (Applying Federal Standards for Spending on Lower Income Students)

Free lunch students weighted at 1.4. Expenses per pupil for districts with graduation rates greater or equal to 90% set at 100%.

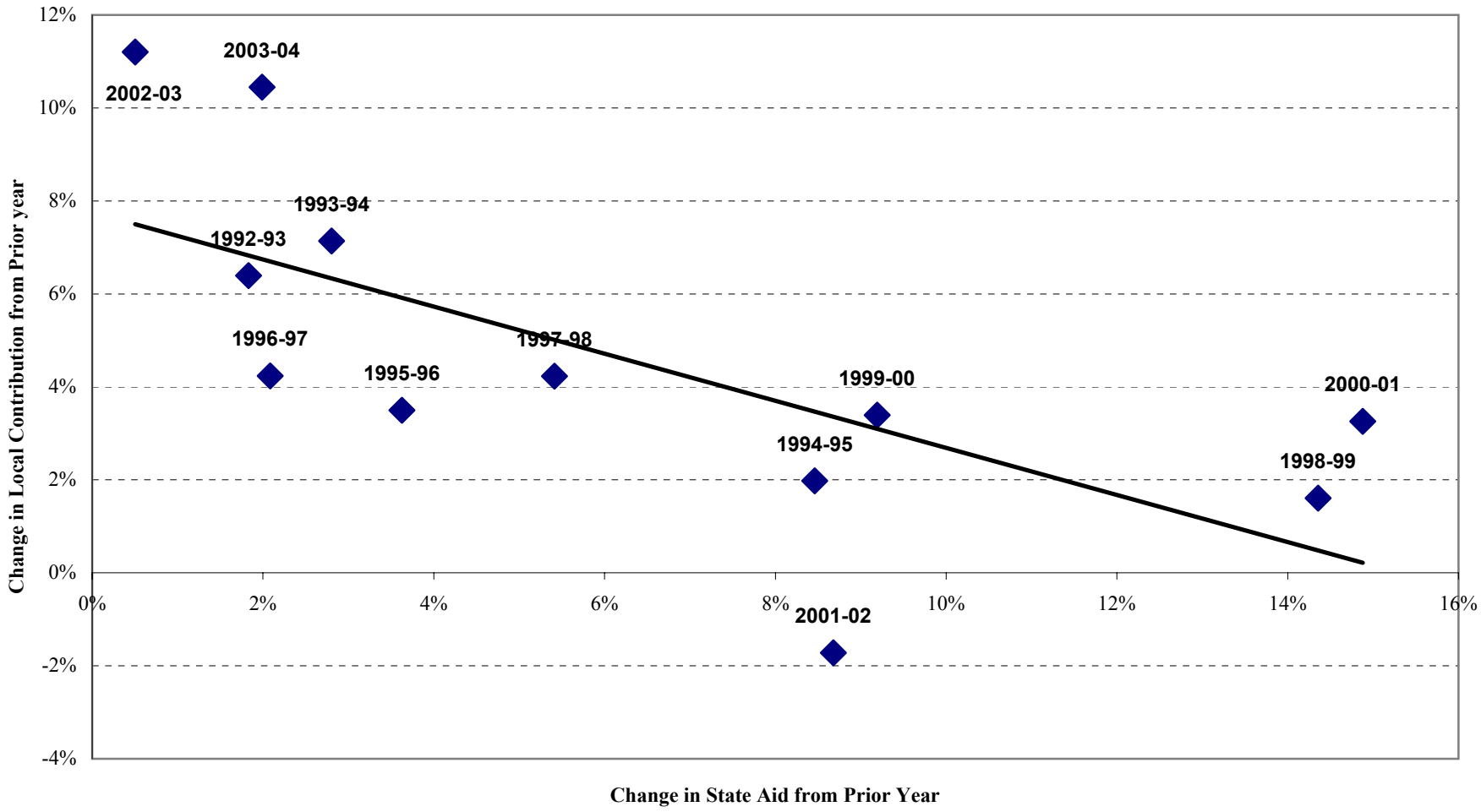


# Relationship between Spending Per Pupil and Graduation Rates
## (Applying NYS Standards for Spending on Lower Income Students)

Free lunch students weighted at 2.0. Expenses per pupil for districts with graduation rates greater or equal to 90% set at 100%.



# Relationship between School Taxes and School Aid

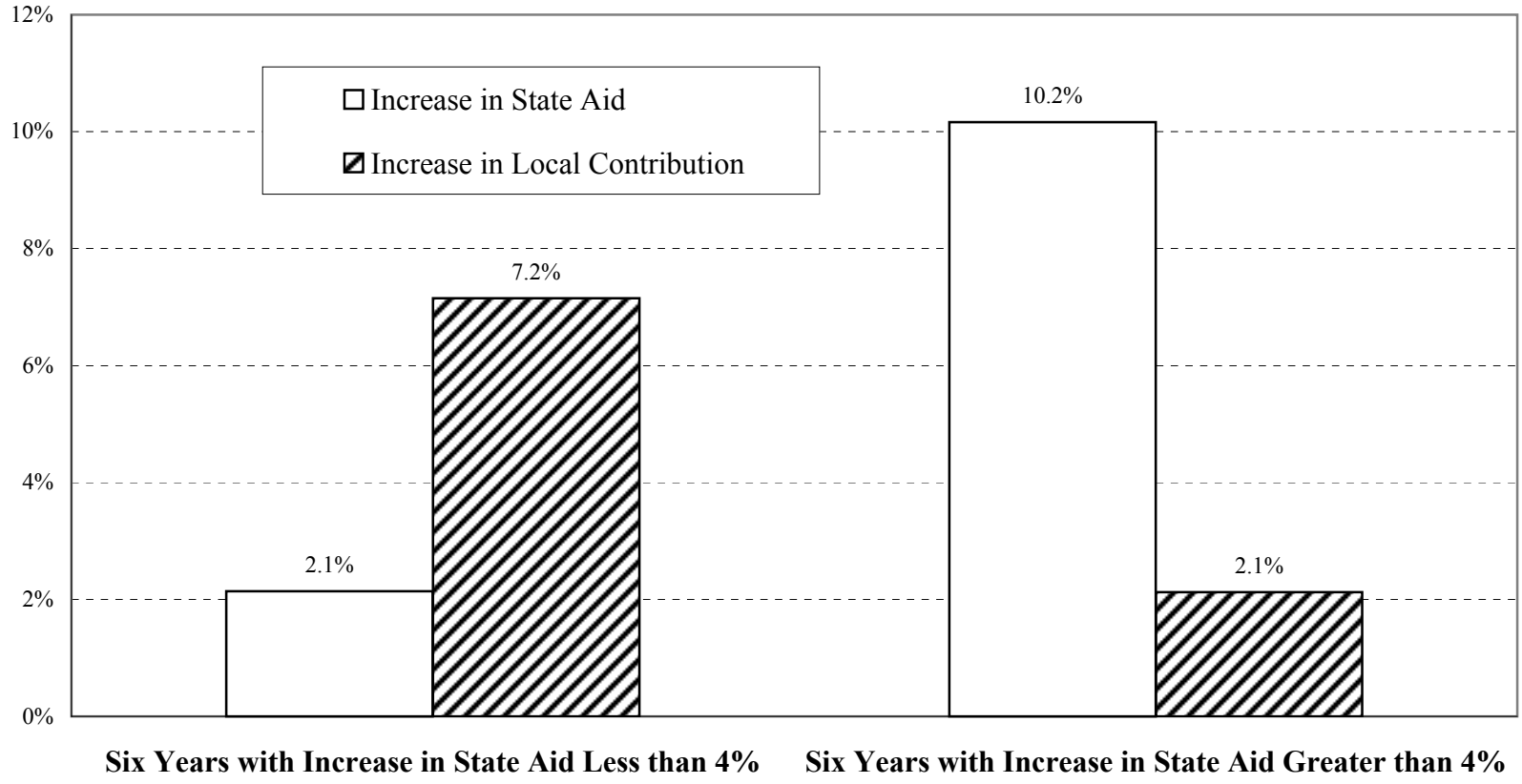


# Trends in School District Budgets, 1992-1993 through 2003-04

| School Year | Percent Change in State Aid from Prior Year | Percent Change in Local Contribution (School Taxes) from Prior Year |
|---|---|---|
| 1992-93 | 1.8% | 6.4% |
| 1993-94 | 2.8% | 7.1% |
| 1994-95 | 8.5% | 2.0% |
| 1995-96 | 3.6% | 3.5% |
| 1996-97 | 2.1% | 4.2% |
| 1997-98 | 5.4% | 4.2% |
| 1998-99 | 14.4% | 1.6% |
| 1999-00 | 9.2% | 3.4% |
| 2000-01 | 14.9% | 3.3% |
| 2001-02 | 8.7% | -1.7% |
| 2002-03 | 0.5% | 11.2% |
| 2003-04 | 2.0% | 10.4% |

Note: The overwhelming majority of district local contributions are from school taxes.

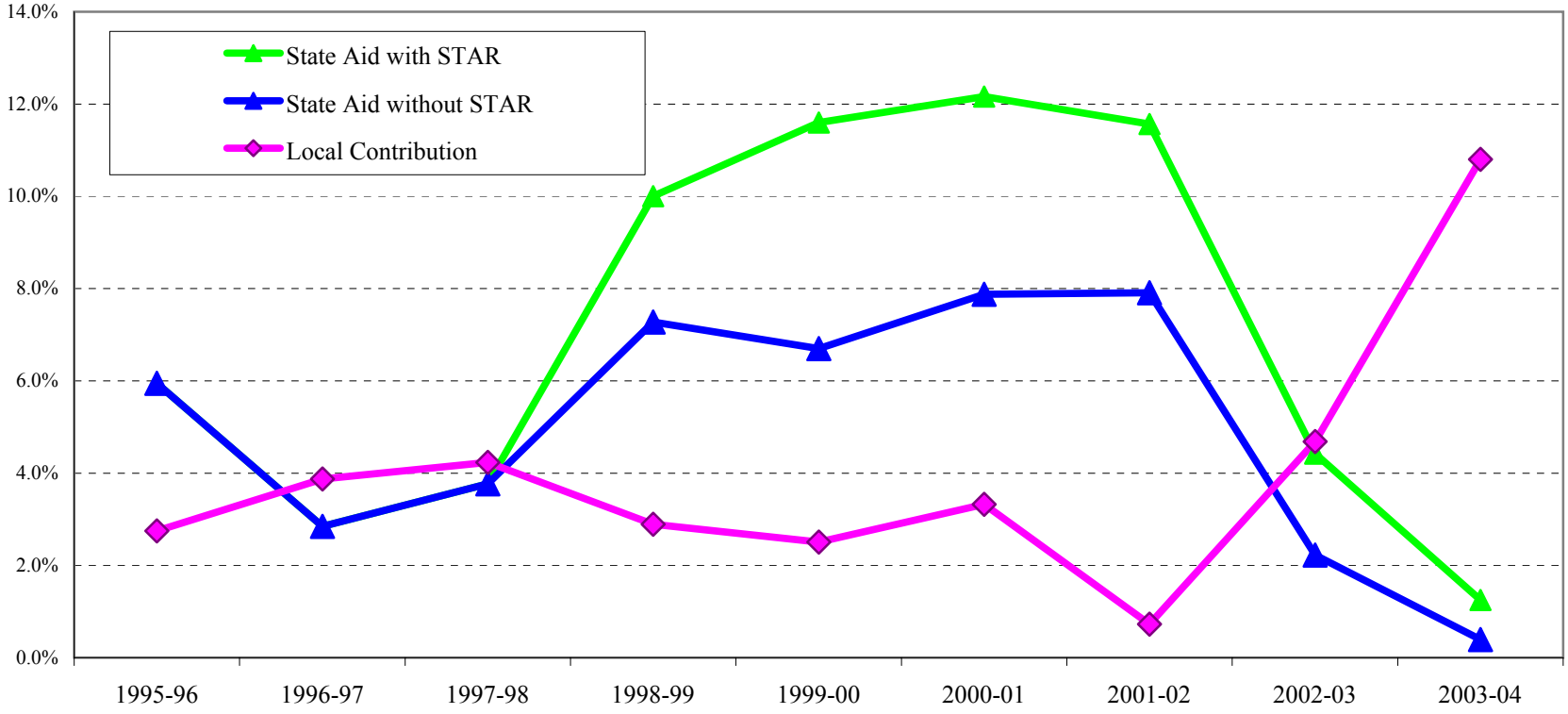
# The Growth in School Property Taxes Is Low in Years When State Aid Increases Are Higher. Property Tax Increases Accelerate when State Aid Increases are Lower.




Data on state aid and local revenues for 1991-1992 to 2003-2004 used to calculate changes from prior year from State Education Departement, Analysis of School Finances in NYS School Districts, January 2006.

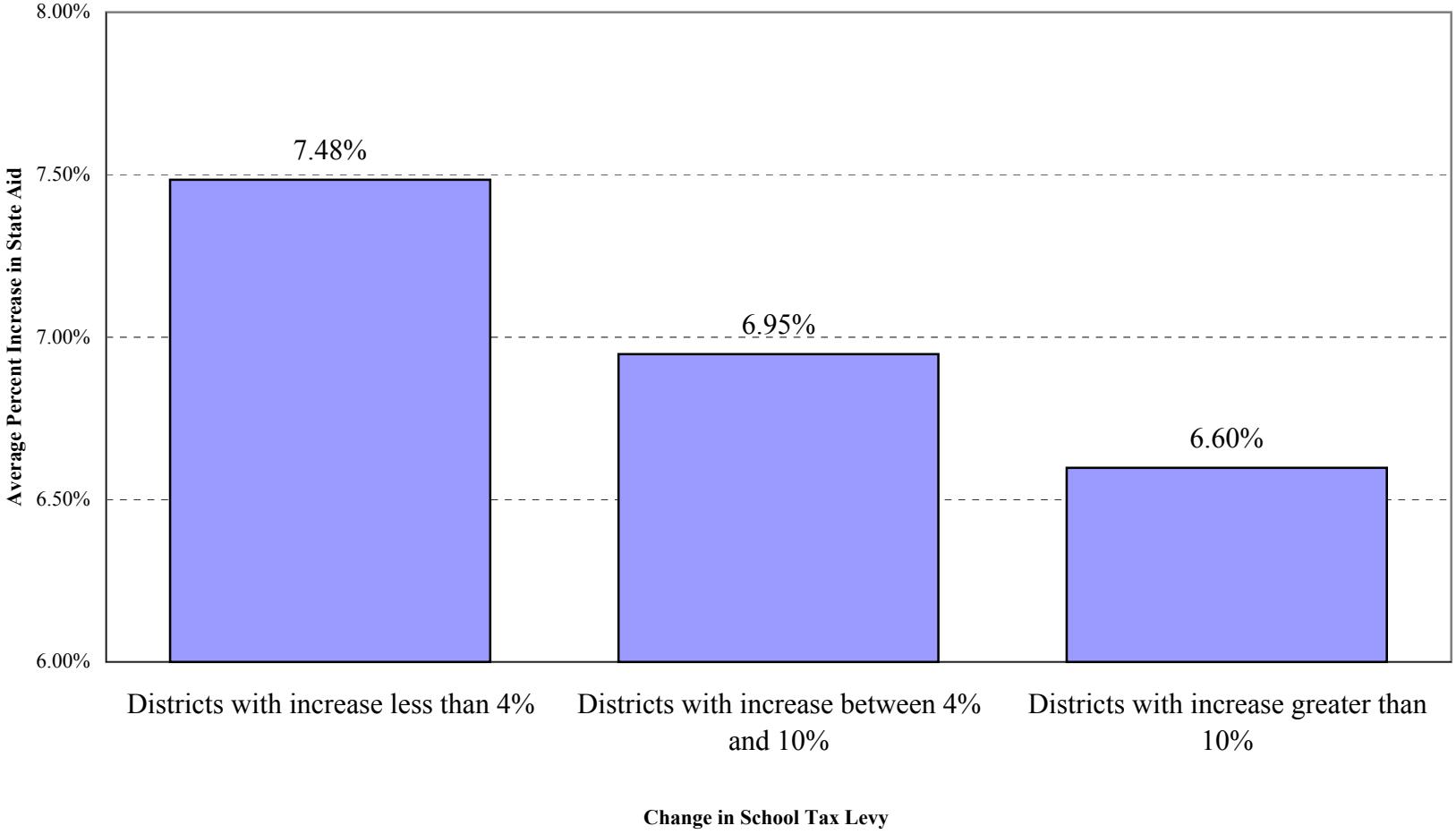
# Historically, Changes in Local Revenues in Support of Education Mirror Changes in State Aid: When State Aid Increases Significantly, Increases in Local Burdens are Moderated

Two-year rolling averages.




Source: Analysis of School Finances in NYS School Districts, New York State Education Department, January 2006.

# Relationship between School Aid Increase and Increase in School Tax Levy: 2006-07



New York State divides responsibility for the financing of important public services between itself and its local governments in ways that place great pressure on local property and sales taxes. This is particularly problematical for those localities that have relatively weak tax bases compared to their needs. It also increases the regressivity of the overall state-local tax system while exacerbating the impact of the property tax's shortcomings.

The governor and the legislature can simultaneously address these fiscal disparities and reduce the pressure that has been placed on the local property tax base by:

1. Implementing a legitimate statewide solution to the court decisions in the Campaign for Fiscal Equity lawsuit.

2. Gradually increasing the state share of Medicaid costs and basing each county's share of Medicaid costs on objective measures of its relative "ability to pay."

3. Restoring the state's commitment to "revenue sharing" with its local governments through a transparent needs-based formula that is honored over time.

4. Eliminating the fiscal disparities in the School Tax Relief (STAR) program that disadvantage city school districts with high percentages of renter-occupied dwellings and high concentrations of needy children. The governor and the legislature should undertake a comprehensive reevaluation of all of the state's real property tax relief programs and work toward an integrated circuit breaker-like variation of STAR that is consistent with the principles of horizontal and vertical equity. In addition, since STAR is both a property tax relief mechanism and a way to deliver state revenue to school districts, it should also be integrated with a legitimate statewide solution to the CFE decision to ensure that it is fair to the upstate cities.

*The Fiscal Policy Institute is a nonpartisan research and education organization that focuses on tax, budget, and economic issues that affect the quality of life and the economic well being of New York State residents.*

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