

Essays on the fallacy of property tax for school funding

Dr. G. Terry Madonna & Dr. Michael L. Young

Viewpoint – End property taxes for schools now

Originally Published June 5, 2012 in the Reading Eagle

These days, the word crisis has become a tedious cliché, much overused and abused by those for whom every problem becomes a looming catastrophe. But the unparalleled challenges now confronting the financing of Pennsylvania's public-education system do constitute a genuine crisis, one that if left unsolved threatens to transform Pennsylvania — educationally, economically, culturally, and even socially — into a permanent backwater.

Across the commonwealth, dedicated teachers are being furloughed, vital programs are being curtailed, entire schools are being shut down and an entire generation of students may be losing their access to a quality education. That's just the good news.

Worse is that the furloughs, the cutting and the closings are all going to accelerate in the coming months and years, bringing further assaults upon Pennsylvania's public-education system. The consequent damage to the quality of education, the future of our children and their ability to compete in the emergent global economy cannot be exaggerated.

And whom, or what monster, shall we blame for this monstrous calamity? Are evil teachers unions behind this looming disaster? Or perhaps corrupt politicians, or even grasping school boards? No. None of these "usual suspects" can take the fall for this one. Our financial crisis is not due to greedy teachers, incompetent administrators, angry taxpayers, manipulating political parties or even super PACs.

In fact, the villain behind our educational woes isn't even a person or institution. It's a tax that most of us are all too familiar with: the real estate property tax, better known as simply the property tax.

What about the simple property tax is so atrocious, so flawed and so defective that we ascribe to it most of the contemporary problems of financing public education? That's a good question, one to which a lot of thought has been given.

The (very) short answer produced by legions of public-finance experts is that the property tax is grotesquely unsuited to modern times. It is unfair, expensive to administer, difficult to assess accurately, disconnected from the modern economy and politically repugnant to most taxpayers. Of all America's major taxes, including the income and sales taxes, the property tax is the worst by any measure you care to use.

But bad as the property tax is, its egregious faults are only part of the problem. Even worse is that we are using this most flawed of taxes to finance perhaps the most important function of government: education. We are trying to educate our children on the back of a creaky 19th century antique that barely did the job then, faltered badly in the 20th century, and now is failing spectacularly as we move through the second decade of the 21st.

Must we watch helplessly as our proud tradition of public education withers away, the victim of inert political leadership and ossified public policies? Absolutely not!

Two things seem eminently sensible.

First, we should adopt expeditiously a tax system that finances 21st century education with a 21st century tax. One of the most promising concepts being discussed now is the Property Tax Independence Act, of which Rep. Jim Cox, a Spring Township Republican, is the primary sponsor. The bill would replace the school property tax by increasing the state's personal income tax to 4 percent from 3.07 percent, and expanding and increasing the state's sales and use tax to 7 percent from 6 percent.

Second, we should avoid throwing out the baby with the bath water and recognize that the property tax, for all its limitations, is best fitted to financing Pennsylvania local government. Originally, property-tax revenues were used almost exclusively to finance local-government functions such as public safety and public health. Only over time was the property tax base hijacked to support more and more local education, so that now as much as 80 percent goes to the schools. We should stop using the property tax to finance schools and instead use it only to support nonschool local-government expenditures. This is where the property tax works best.

Neither of these steps requires overall increased taxes. Cox's bill and others proposed over the years would not raise taxes but rather would shift tax burdens from the property tax to a tax more suited to modern times and the needs of public education. Nevertheless, any legislation that envisions tax changes, even tax shifting, will be controversial. Indeed, earlier efforts dating back three decades to bring tax reform to Pennsylvania were rife with dissension.

But let's not kid ourselves. The choice is not between change and no change. Change, almost all of it bad, is happening across the state almost every day as Pennsylvania's school districts adapt to the new realities imposed by relying on the property tax to finance education. The real choice is between having a choice about the future of state public education and having that choice imposed upon us by doing nothing.

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BEEN THERE & DONE THAT

Originally published on April 25, 2007

On May 15, Pennsylvania primary voters in most school districts will cast ballots to determine if they will exchange local property tax reductions for either a local earned income tax or a local personal income tax. We don't know in advance how many voters will trade in lower property taxes for higher local income taxes, but we do know in advance that whatever the voters do, it won't matter. It won't matter for the same reason that it doesn't matter in a shell game which shell players look under. The game is fixed.

We know it's fixed because we have played this game before. With respect to the long running property tax shell game, Pennsylvanians have been there and done that. Nevertheless, on May 15th, voters are being asked to go there and do it again.

Some brief background will be helpful. Three times over the last decade, challenged to find a solution for the state's festering property tax problem, the legislature has successively adopted legislation beginning with Act 50 in 1998, followed by Act 72 in 2004, and now Act 1 (2006). All three pieces of legislation have been premised on a single flawed premise, that local governments using local resources can solve the problem of school funding, that somehow if we just let school districts switch one kind of tax for another and cap property taxes, the school funding crisis will go away.

But it hasn't gone away, not in 1998, not in 2004, and not this time. It is still very much with us and it will remain with us until we confront the real problem.

Let's be clear just what that problem is.

What we casually call the property tax problem is actually a bundle of interrelated problems that involve intergovernmental tax bases, inequities, and inadequacies in the property tax and problems funding public education.

The school funding problem is central here. Lawmakers have been funding local public education with a tax, the property tax, better suited to the America of the 19th century than to the 21st--a tax simply not capable of adequately or fairly funding the public schools.

Using the property tax to fund schools has produced an atmosphere of perpetual crisis in local public financing. Under existing law, relying on the property tax to fund local education means there will never be enough money raised to pay for education (tax inadequacy), and the burden of paying for schools will unfairly fall on those least able to pay (tax inequity). It also means we will always have a "property tax problem," that property taxes will continue to go up, and school districts will continue to struggle to control spending.

Spending control figures prominently in the problem. Local school districts possess little or no ability to control many school expenditures. Much of the "uncontrollable spending" is based on unfunded state mandates, such as special education, healthcare, teacher pensions, judicial orders, and shifting enrollments. The state, in effect, requires that local districts perform certain functions, even if state government won't provide sufficient resources for the function to be performed.

The magnitude of “uncontrollable spending” because of state mandates and related causes is starkly illustrated by a single statistic: the number of school districts this year that received exceptions to Act One’s provision that tax increases be limited to the rate of inflation. Fully, 210 districts or 45 percent of the total number received exceptions, most for expenditures such as special education, healthcare, or pension costs over which local districts have little or no discretion.

For these districts this year, and for all districts in any given year, hypothetical limits on property tax increases are little more than a cruel joke.

Does this imply that there is no solution to the property tax problem? Not at all! In fact the solutions are clear and obvious: we can cut spending and/or increase revenues. There is no advanced math necessary here.

Consider the first option, spending cuts. Any meaningful spending cuts would need to take place precisely in those areas of school spending carved out in Act One’s exceptions. These include many of the major drivers of increased spending: special education, teacher pensions, school construction costs, healthcare, No Child Left Behind requirements, and other mandated items.

Spending cuts like these would indeed take pressure off the local property tax base. But it is Pollyannaish to believe this will happen. In fact, there is no popular support for large cuts in education spending, leaving policymakers with the second option-- increasing revenues to pay for education.

The choices here are straightforward. There are only two broad based taxes with the capacity to raise enough revenue: the state sales tax and state income tax. There are no other ways that state or local governments can raise the money to pay for schools. The political leadership of the state continues to deny this fundamental truth and beguiles us into believing that local taxes can do the job, if we only get the right local taxes. But the truth is local tax bases simply won’t stretch far enough to raise sufficient revenues to meet the needs of the schools. You can’t get there from here.

And so, Pennsylvania voters continue to be ensnared in a long running shell game in which political leaders cynically provide us with choices that make no difference, while they perversely refuse to own up to the real problem or provide any real solution to the school funding problem.

Once again on May 15th, voters will go to the polls to pretend that they are making real decisions that will have real consequences. They won’t. Nor will the charade conclude until the policymakers conclude they can’t spoof the voters any longer. Sadly, there is no sign of that so far.

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Dr. Mark W. Hendrickson

TIME TO ABOLISH ANTIQUATED PROPERTY TAX

Originally published on July 10, 2007

Property taxes in Pennsylvania appear locked into a long-term uptrend. In recent years, there have been huge increases in the portion of the property tax that finances county government. County officials have levied these increases to pay for the unfunded mandates imposed by the state government in Harrisburg. The largest share of the property tax funds the public school districts, and virtually nobody foresees a time when the expenditures of those districts will stop rising. These ongoing pressures for additional tax revenues raise the question: Is it politically and economically feasible to continue raising property taxes in the coming years?

Some might look at the results of a recent ballot proposal in Lawrence County and conclude that Pennsylvanians prefer a property tax over others types of taxes, but this conclusion is unwarranted. When offered the opportunity to receive a modest reduction in the public-school portion of their property tax in exchange for a 1 percent increase in their earned income tax, voters in every school district in the county overwhelmingly voted against it. The context here is crucial. Voters were not opposed to property tax relief, but to a package deal that represented an overall tax increase.

We have a political stalemate in Pennsylvania, because Harrisburg has mandated that the only permissible reform to public-school funding must be structured like the Lawrence County proposals. The psychology is all wrong. It's hard for voters to get excited about a proposal that makes an obnoxious, already-high tax just a little less high (i.e., the property tax) at the price of ratcheting up another obnoxious tax -- the income tax -- when the federal/state/local taking of income is already at an uncomfortable level. If Harrisburg really wants reform, it needs to emulate the boldness of the Michigan government in the 1990s, when it totally scrapped the property tax for school funding, and replaced it with a 2 percent hike in the state sales tax. I suspect that Pennsylvania voters would be far more comfortable with an increase in one type of taxation if it were offset by the complete removal of another type of taxation. If you give Pennsylvania voters the chance to eliminate one part of their tax bill completely, then tax reform has a fighting chance for approval.

The larger, more fundamental problem here is the property tax itself. This form of taxation is totally antiquated, appropriate in America's 19th-century agrarian society, but out of place today. In the 1800s, when there was no income tax and it was considered none of the government's business how much money anybody made, the property tax served as a proxy for one's income. This made a lot of sense then, because it was logical to assume that the citizen farming 80 acres had a higher income than one farming only 40 acres. Today, though, the homesteads of most Americans are not their source of income, but merely where they live. Why, then, take more money from a citizen with a house of 1,500 square feet than one with 900? One of the elementary principles of prudent taxation is that, in order to avoid harming citizens, taxes should take into consideration the individual's ability to pay. Today, one's ability to pay depends far more on one's income than on the size of one's house. To continue taxing people as if their house were generating their income is absurd.

An additional fault of the property tax is that it can jeopardize home ownership. On the surface, it appears that once a person has paid off the mortgage on his house, then he owns it free and clear, but this is not so. If the homeowner falls on hard

times and can't pay his property taxes, the sheriff comes and confiscates the house. Under the present system, a person doesn't really "own" his home completely, but in effect rents it from the local government which permits him to keep it only so long as the "owner" continues to pay taxes on it. We have heard of senior citizens -- wonderful, law-abiding citizens who worked hard for decades to buy their own home -- having to sell their home because they couldn't afford the taxes. This is abominable. And how many of America's homeless persons became so because they fell on hard times and were evicted from their homes because they couldn't pay their property tax?

In an era when it has been the federal government's policy to facilitate home ownership as a central feature of "the American dream," it is anomalous for local governments to make it difficult for some citizens to keep their homes. The property tax is outmoded, unfair, irrational and destructive. It's time to abolish it.

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