



# Property tax elimination raises taxes on middle class to cut taxes for affluent

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## Summary

With ongoing negotiations over the state budget focused on property tax cuts (<http://goo.gl/6R8Bgv>), and the State Senate taking up a bill to eliminate property taxes, this briefing paper compares property tax elimination with two more targeted approaches that would reduce, but not eliminate property taxes: the Republican proposal that passed the Pennsylvania House in May (House Bill 504) and Gov. Wolf's original proposal from March.

We find that property tax elimination would raise taxes on the middle class to give wealthy homeowners and businesses in wealthy communities a tax break. Both targeted approaches would be better for the middle class, but the Wolf proposal would be the best for moderate-income homeowners and would also cut non-residential property taxes the most in lower-income communities, a potential boost to community revitalization.

## Middle Class Loses Out Under Property Tax Elimination

This week the Pennsylvania Senate will consider Senate Bill 76, which would eliminate school property taxes.<sup>1</sup> While we have not examined the tax incidence of the current SB 76, the Institute on Taxation and Economic Policy (ITEP) did estimate for us the tax incidence of a similar proposal several years ago. That proposal, like the current SB 76, promised to eliminate school property taxes through an increase in the sales tax rate to 7 percent, while also applying it to more services, and an increase in the personal income tax rate (to 4.1 percent under the old SB 76 and to 4.34 percent under the new SB 76). One reason the new SB 76 has a larger PIT increase is that the earlier proposal didn't raise enough revenue: even the "new and improved" SB 76 does not raise enough revenue to eliminate property taxes permanently and to adequately and equitably fund schools going forward.

As we explained in our release (<http://goo.gl/YLDSNZ>) last Wednesday, the sales tax falls more heavily on middle-class and low-income families.<sup>2</sup> The property tax also falls more heavily on middle-class and low-income families, but is not as regressive as the sales tax – in part, because the wealthy choose to spend substantially more on housing than the middle class and also to impose high property taxes on themselves to provide more funding for their local schools.

Given these realities, there is a danger that raising the sales tax to eliminate school property taxes will increase taxes on lower-income families to provide tax benefits to higher-income families. Underscoring this danger, ITEP's analysis of the earlier property tax elimination proposal did indeed find that it increased average taxes on middle-income families, while lowering average taxes on the top 20 percent of families. (This proposal also provided a small cut in average taxes for the bottom 20 percent of

families). **Property tax elimination amounted to a middle-class tax hike to pay for tax cuts for affluent families.**

### Targeted Cuts Are Better For Middle Class Families

If property tax cuts are going to be a priority, a smarter approach for the middle class is to provide more targeted relief as a majority of the House proposed to do with the passage of HB 504 in early May, and as Gov. Wolf proposed in his initial budget address in March. Our previous analysis of these two proposals found that the Wolf plan was more targeted to moderate-income homeowners and communities. (For more on the House and Wolf proposals and their allocation formulas, check out our late July trio of briefs (<https://goo.gl/byUWl4>).<sup>3</sup>

To see the wisdom of the targeted approach, and that property tax elimination most benefits high-income families, consider two school districts -- the relatively low-income Reading School District in Berks County and the relatively affluent Wissahickon School District in Montgomery County. If you want to make your own comparisons, download our technical appendix (<https://goo.gl/G3cBRr>) which has data on every school district in Pennsylvania.<sup>4</sup>

Table 1 reveals that SB 76, by eliminating all school property taxes, would cut taxes for the typical homeowner (i.e., “median value homestead”) in the Wissahickon School District by \$3,630. It takes a lot of extra revenue, raised in part from middle-income families via higher sales and income taxes, to eliminate such substantial property taxes used to fund the local schools in affluent places. HB 504’s targeted approach would only give affluent Wissahickon homeowners a property tax cut about half as big (\$1,800). Gov. Wolf’s even more targeted plan would trim the Wissahickon property tax cut further – to about \$1,000. By contrast, Reading homeowners would receive almost the same property tax cut under all three plans – roughly \$700.

Table 1.  
 Cuts in property taxes for the median homestead under the Wolf proposal and HB 504

| School District        | Wolf property tax cut | HB 504 property tax cut | Property Taxes on the Median Value Homestead | Median Assessed Value 2014-15 |
|------------------------|-----------------------|-------------------------|--|-------------------------------|
| Wissahickon Montgomery | \$995                 | \$1,782                 | \$3,630                                      | \$205,670                     |
| Reading Berks          | \$699                 | \$677                   | \$710  | \$40,800                      |

Source. Pennsylvania Budget and Policy Center

Another key difference between these three proposals concerns the amount of non-residential property tax relief they would provide – i.e., primarily to business owners of commercial property. SB 76 would eliminate all property taxes on non-residential property owners and pay for this by raising taxes on middle-income families.

The Wolf plan would provide small or no property tax cuts for non-residential property owners in affluent school districts (e.g., 0 percent in Wissahickon), but large property tax cuts for non-residential property owners in less affluent school districts (e.g., 97 percent in Reading) -- potentially enough, along with more school funding, to spur community revitalization. By contrast, HB 504 would provide a 20 percent cut in non-residential property taxes in Wissahickon -- to what purpose? -- but only a 45 percent cut in Reading.

Table 2.

Cuts in property taxes for non-residential property owners under the Wolf proposal and HB 504

| School District |            | Wolf property tax cut | HB 504 property tax cut |
|-----------------|------------|-----------------------|-------------------------|
| Wissahickon     | Montgomery | 0%                    | 20%                     |
| Reading         | Berks      | 97%                   | 45%                     |

Source. Pennsylvania Budget and Policy Center

### Conclusion

Property tax elimination would amount to large tax cuts for the wealthy and for businesses paid for by the middle class. The original Republican proposal for more targeted property tax relief would be less generous – but still meaningful – to wealthy homeowners and to businesses in wealthier communities. The original Wolf proposal for property tax relief would be much more generous to middle-class homeowners, renters (an issue not addressed here), and businesses in lower-income communities.

We think a majority of voters and lawmakers – if they understood these differences --would oppose property tax elimination: they don't want to make the Pennsylvania tax system even more unfair, and they don't want to threaten the adequacy of school funding.

In the context of Pennsylvania's budget framework agreement, which includes scaled-down property tax relief (half as much relief or less than the original Wolf and HB 504 proposals), we also think that a majority of voters and lawmakers would favor a variation on the Wolf distribution approach for targeted tax relief. This would benefit the middle class more and would give struggling communities a potentially new lease on life, while giving less of a windfall to mall owners in affluent communities.

<sup>1</sup> Property tax elimination would be paid for by raising the sales tax rate to 7 percent and expanding the sales tax to cover more services; and by raising the personal income tax rate to 4.34 percent.

<sup>2</sup> Mark Price, *Who Pays For An Increase in the Sales Tax: Analysis of the Tax Incidence of an Increase in the Sales Tax from 6% to 7.25%*, Pennsylvania Budget and Policy Center, available online at [http://pennbpc.org/Budget1516\\_WhoPaysSalesTax](http://pennbpc.org/Budget1516_WhoPaysSalesTax)

<sup>3</sup> Pennsylvania Budget and Policy Center, *Follow the Property Tax Money: The Wolf Plan and HB 504 Compared*, available online at <https://pennbpc.org/follow-property-tax-money-wolf-plan-and-hb-504-compared>

<sup>4</sup> Pennsylvania Budget and Policy Center, Online Technical Appendix: Follow the Property Tax Money: The Wolf Plan and HB 504 Compared, [https://pennbpc.org/sites/pennbpc.org/files/PBPC\\_OTL\\_PropertyTaxes.xls](https://pennbpc.org/sites/pennbpc.org/files/PBPC_OTL_PropertyTaxes.xls)