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Property Taxes in Connecticut:
How Over-Reliance Thwarts Towns' Ability to Provide Essential Services

CONNECTICUT CONFERENCE OF MUNICIPALITIES

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Property Taxes in Connecticut: How Over-Reliance Thwarts Towns' Ability to Provide Essential Services

INTRODUCTION

Towns and cities in Connecticut are responsible for providing the majority of public services in our state: preK-12 education; public safety; roads and other infrastructure; elderly and youth services; other social services; recreation; and wastewater treatment, among others. They must do so while meeting numerous mandates, often underfunded or unfunded, from both the federal and state governments.

Funding for these critical local public services can come from various sources, including taxes, user fees and charges, revenue sharing, and state and federal aid. In Connecticut, however, there is one revenue source that provides the majority of local funding – the property tax. A property-tax dependent system only works fairly if two conditions exist: (1) the property and income wealth of a community can generate enough property tax revenue at a reasonable cost to taxpayers to meet the need for public services; or (2) state aid is sufficient to fill local revenue gaps. For many communities in our state, neither condition exists.

It is increasingly clear that the over-reliance on the property tax is inadequate for funding local government services in Connecticut, particularly preK-12 public education, and is no longer advisable nor sustainable.

What worked in 1814 doesn't work in 2014.

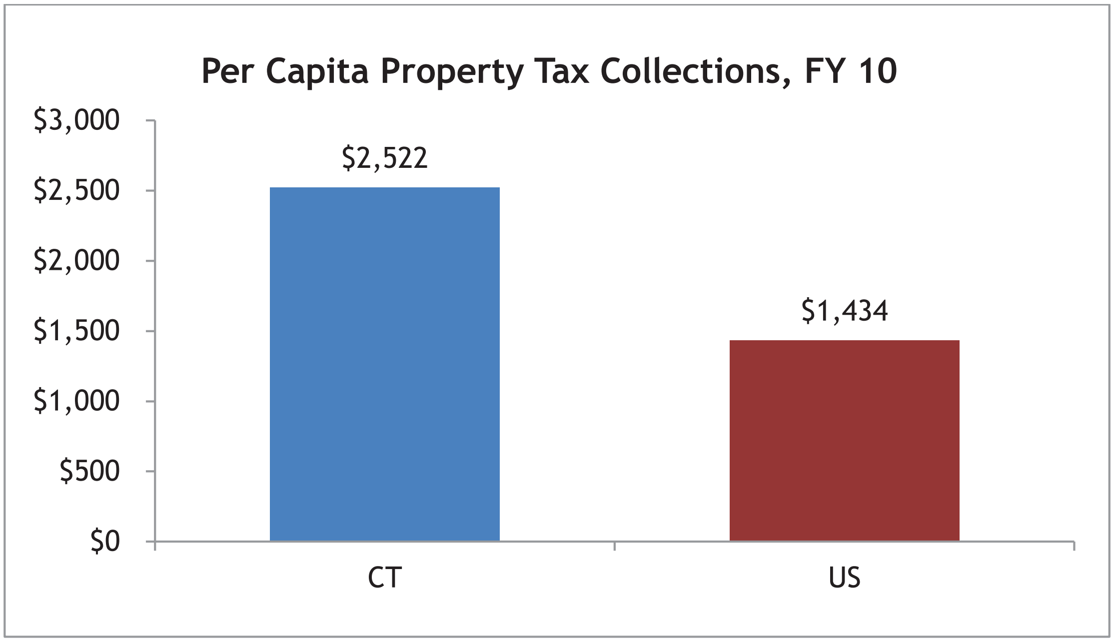
PROPERTY TAX DEPENDENCE

The property tax is the single largest tax on residents and businesses in our state. The property tax is income-blind and profit-blind. It is due and payable whether a resident has a job or not, or whether a business turns a profit or not.

The property tax levy on residents and businesses in Connecticut was $9.22 billion in 2012.[1]

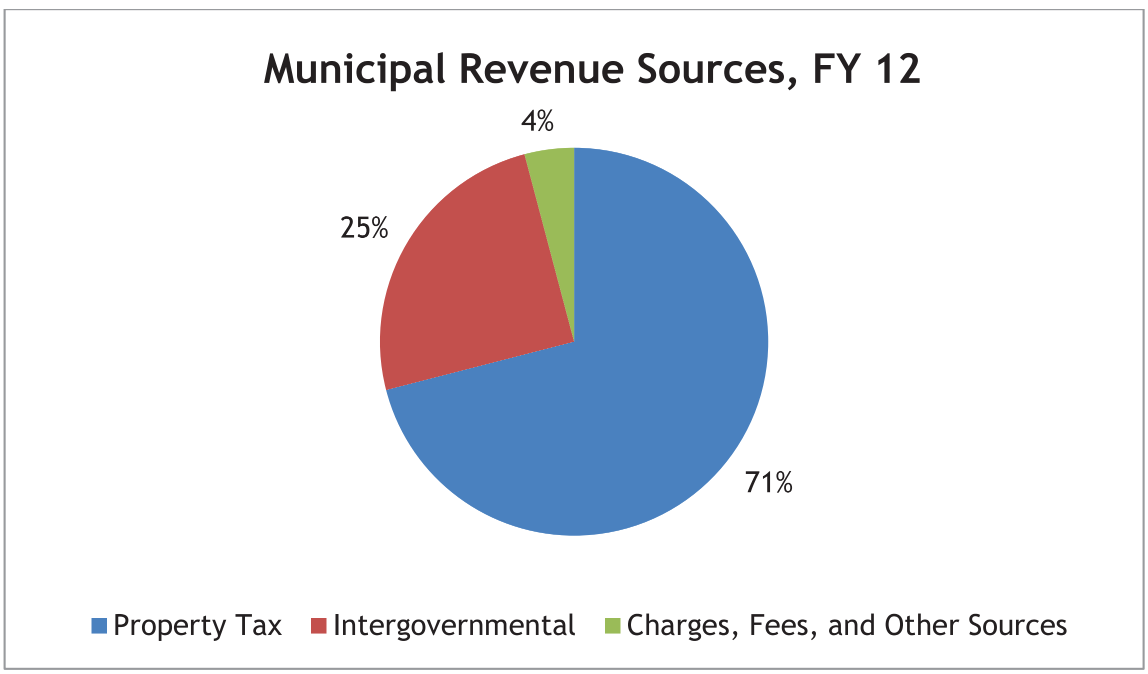
The per capita property tax burden in Connecticut is $2,522, an amount that is almost twice the national average of $1,434 - and 3rd highest in the nation. Connecticut ranks 8th in property taxes paid as a percentage of median home value (1.70 percent for Connecticut vs. 1.14 percent for the US).[2]

[1] OPM, *Municipal Fiscal Indicators*, 2008-2012.
[2] Tax Foundation, 2010 Data.



Source: Tax Foundation, latest data available.

Statewide, 71 percent of municipal revenue comes from property taxes. Most of the rest, 25 percent, comes from intergovernmental revenue, mostly in the form of state aid. Some Connecticut municipalities are almost totally dependent on property taxes to fund local government. Fifteen towns depend on property taxes for at least 90 percent of all their revenue. Another 50 municipalities rely on property taxes for at least 80 percent of their revenue.[3]



Source: OPM, *Municipal Fiscal Indicators,* 2008-2012.

[3] OPM, *Municipal Fiscal Indicators*, 2008-2012.

Connecticut is more dependent on property taxes to fund local government than any other state in the nation.[4]

Connecticut is the most reliant state in the nation on property taxes to fund preK-12 public education.[5] **That means that the educational opportunity of a child in our state is directly tied to the property tax wealth of the community in which he or she lives.**

Property Tax Facts:

- Connecticut's biggest state-local tax
- Regressive: Income/profit blind
- Property and income wealth vary widely from town to town in Connecticut
- Connecticut is more dependent on it than any other state
- Biggest tax on Connecticut businesses
- 71% of all municipal revenue
- Primary funder of PreK-12 public education in Connecticut

The property tax accounts for 37 percent of all state and local taxes paid in our state. In FY 12, Connecticut businesses paid over $700 million in state corporate income taxes, but over $1 billion in local property taxes.[6]

WHY IS CONNECTICUT SO RELIANT ON THE PROPERTY TAX?

The revenue options available to Connecticut towns and cities are limited by state statute. The property tax is the only tax over which municipalities have significant authority. Municipalities can levy a conveyance tax on real estate transactions, but that tax rate is set by the State and provides a relatively small amount of revenue.

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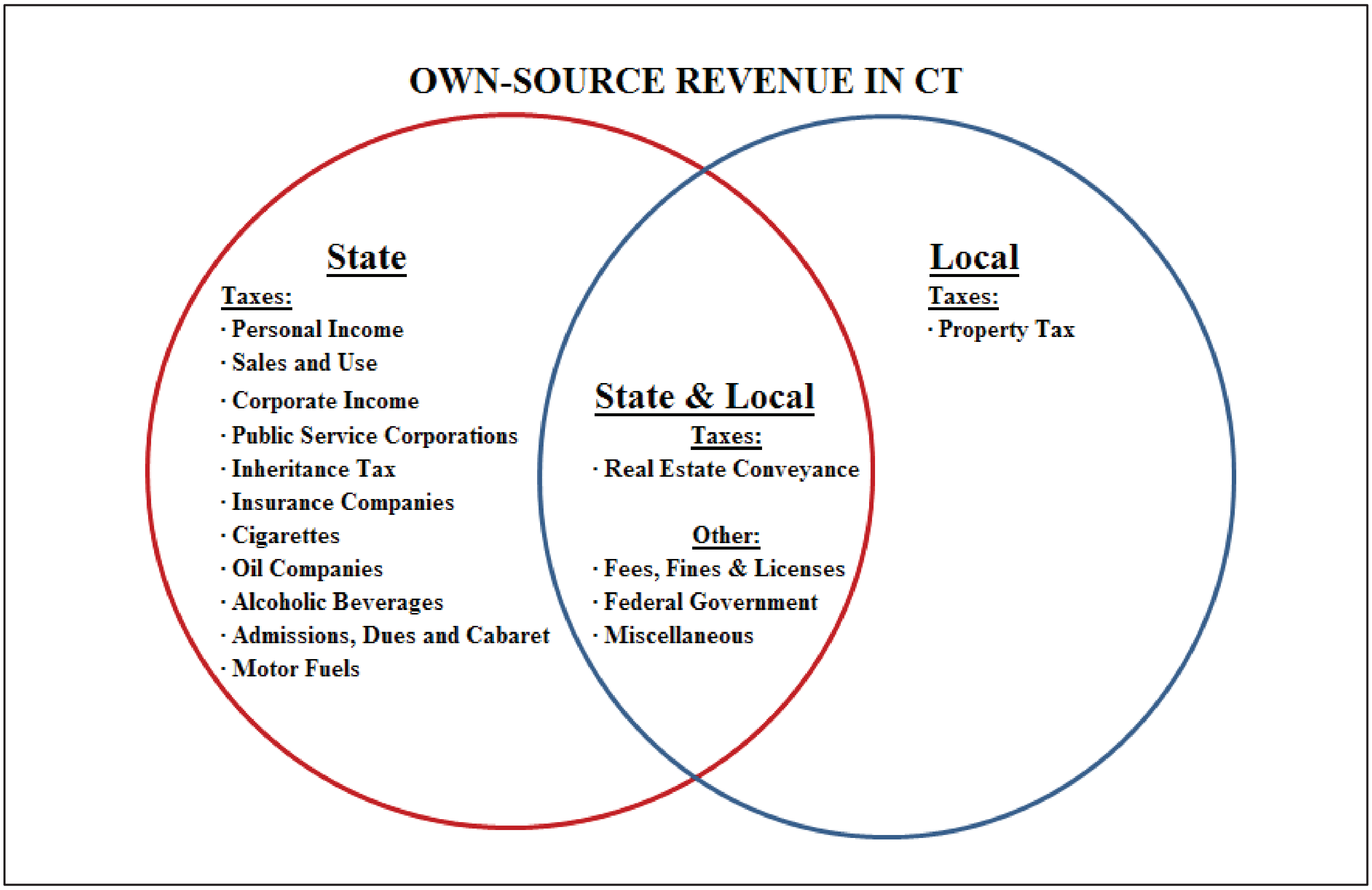
[4] Based on data from the US Census Bureau and the Tax Foundation.
[5] US Census Bureau, *Public Elementary-Secondary Education Finances*, 2012.
[6] CCM estimate.



Source: CCM 2014.

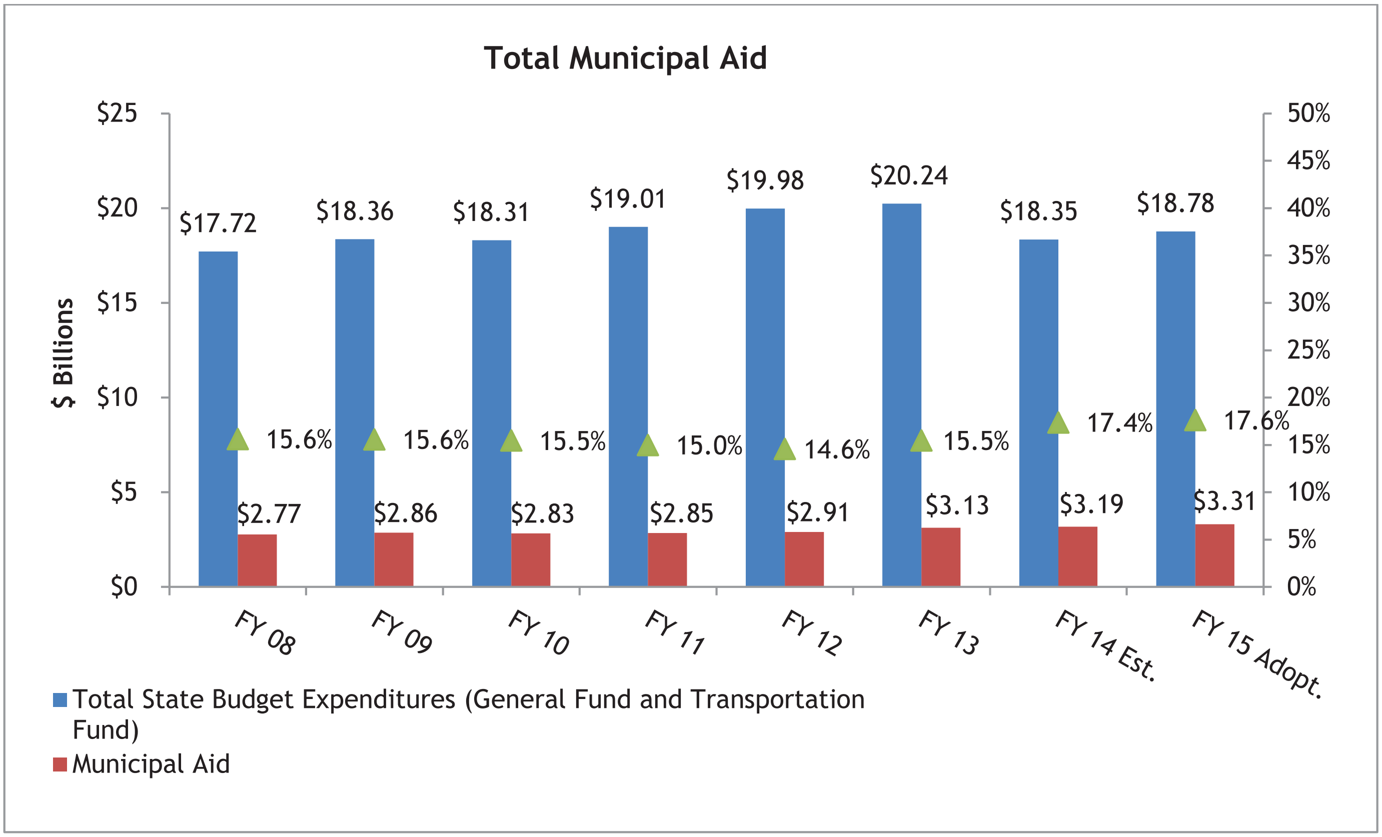
Similarly, municipalities can levy user fees and charges to cover some of the costs of providing services. These are again limited by state law and cannot be used to raise revenue, only to cover necessary costs.

All of this means that, in terms of generating own-source revenue, Connecticut towns and cities are effectively restricted to the regressive and antiquated property tax.

The Uncertainty of Intergovernmental Revenue

After the property tax, the largest revenue source for municipalities is intergovernmental revenue. These payments from the federal and state governments account for about 25 percent of all local revenue, with the vast majority coming from the State. There are significant issues with federal and state funding, however, that increase Hometown Connecticut's reliance on property taxes.

Federal revenues to municipalities often come in the form of competitive grants. The nature of these grants means that funding isn't consistent from year to year, and towns and cities can't rely on that funding as a steady stream of revenue. Add to that the dire fiscal condition of the federal government, and the outlook for consistent and dependable federal funding is anything but positive.



Source: Adopted state budgets; CCM.
Note: Total state budget expenditures are reduced starting in FY 14 due to the removal of the federal share of the Medicaid appropriation totaling approximately $2.8 billion.

State Aid to Municipalities: The Realities

The State provides $3.3 billion in education and non-education aid to towns and cities out of a more than $18.8 billion state budget. This accounts for more than 20 percent of all local revenue. While it represents a substantial amount of money, this funding has failed to keep up with the rising costs of and greater demands for local public services, particularly education services.

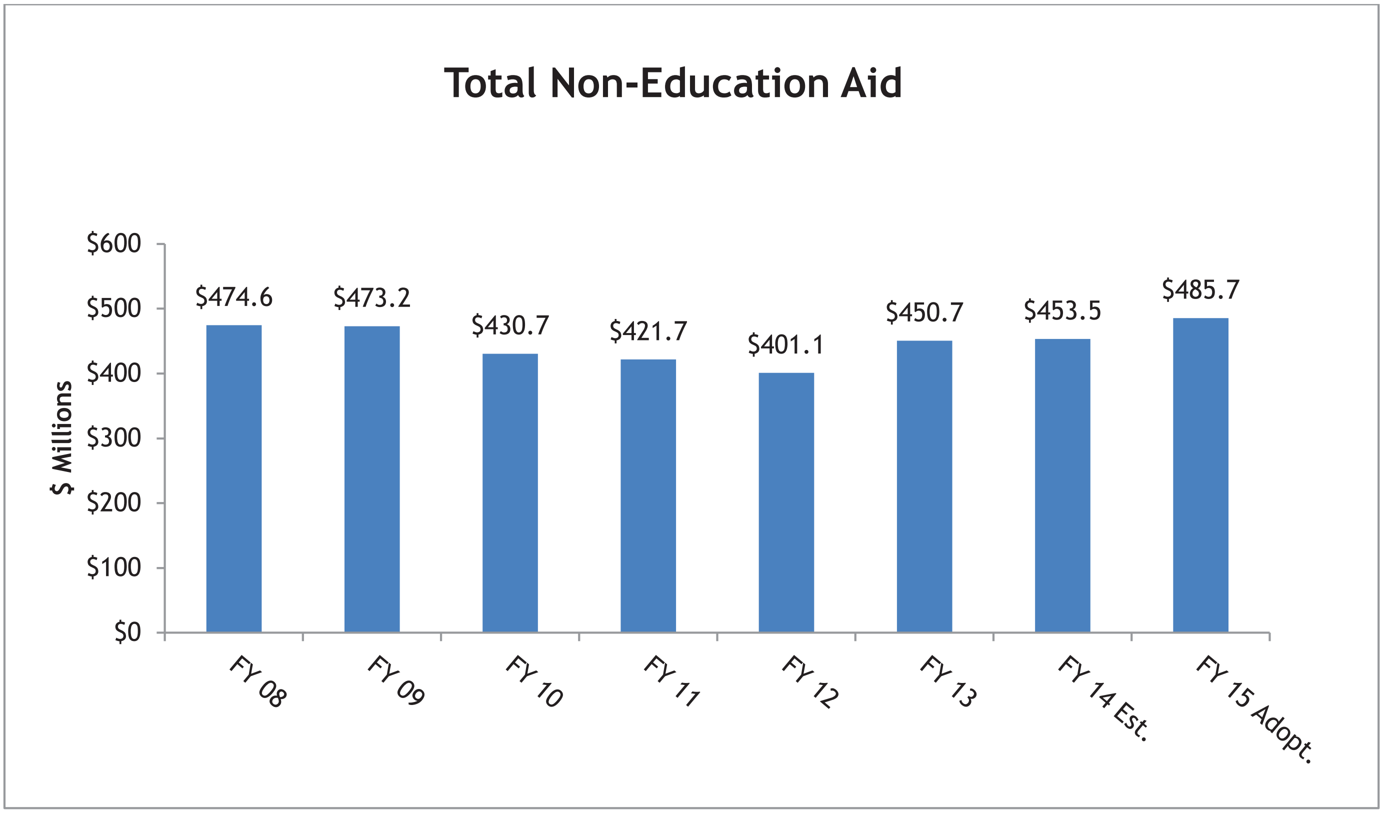
Non-education aid is now only about 15 percent of state aid to municipalities. The other 85 percent comes in the form of education aid.[7]

Let’s take a look at some of the larger state grant programs starting with non-education aid.

Key Non-Education Aid

The amount of non-education aid to municipalities has fluctuated dramatically over the years.

[7] CCM calculation based on FY 15 State Budget.



Source: Adopted state budgets; CCM.

Non-education aid to municipalities is $485.7 million in FY 15, only 15 percent of total state aid to towns and cities.[8]

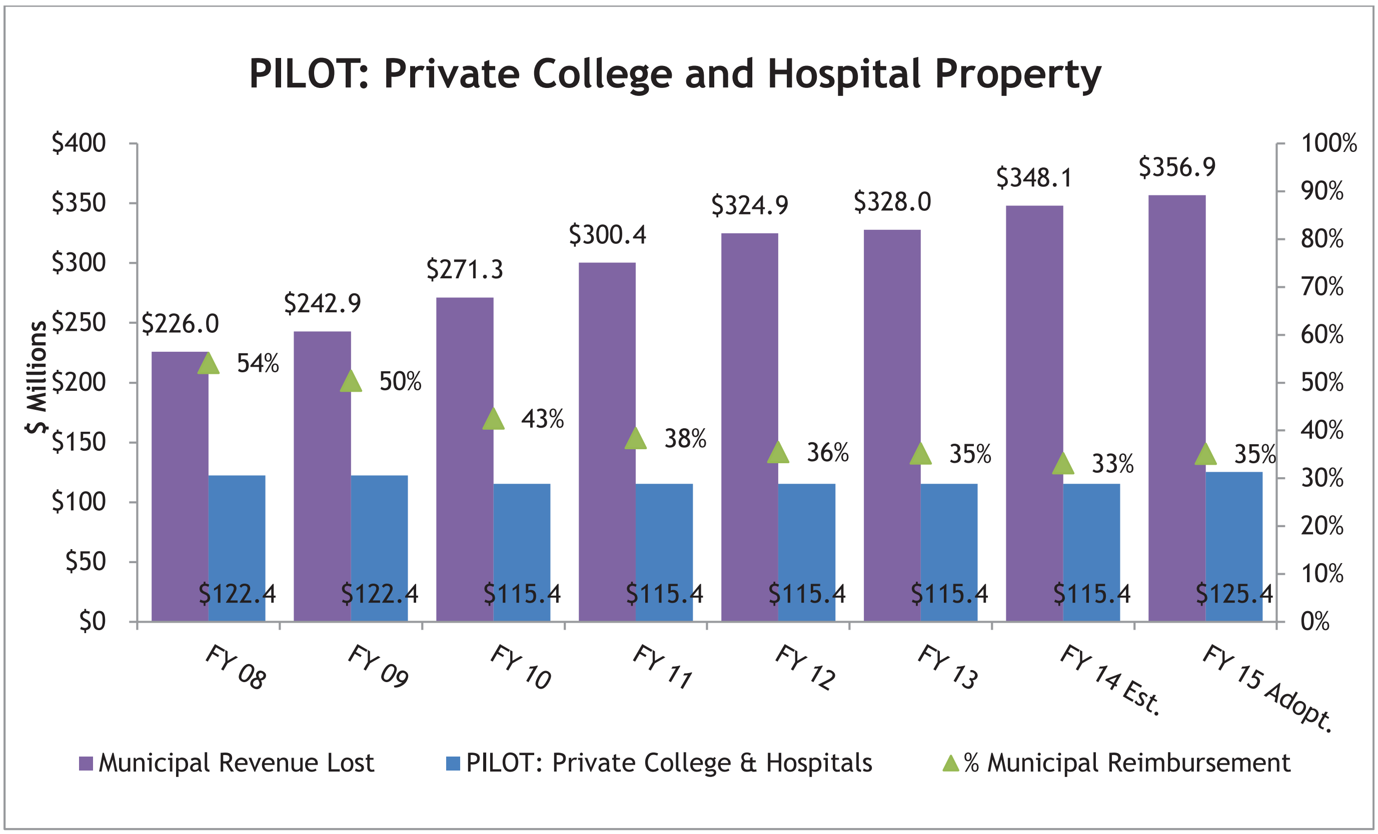
PILOT: Private Colleges & Hospitals

Municipalities receive payments in lieu of taxes (PILOTs) from the State as partial reimbursement of lost property taxes on state-owned and on private college and hospital property. The payments are provided to offset a portion of the lost revenue from state-mandated tax exemptions on this property. This lost revenue totals about $660 million.[9]

The reimbursement rate for tax-exempt private college and hospital property is supposed to be 77 percent. It is actually 35 percent.

[8] CCM calculation based on FY 15 State Budget.

[9] CCM estimate. PILOT reimbursements cover only *real* property and do not include revenue lost from state-mandated exemptions on *personal* property.



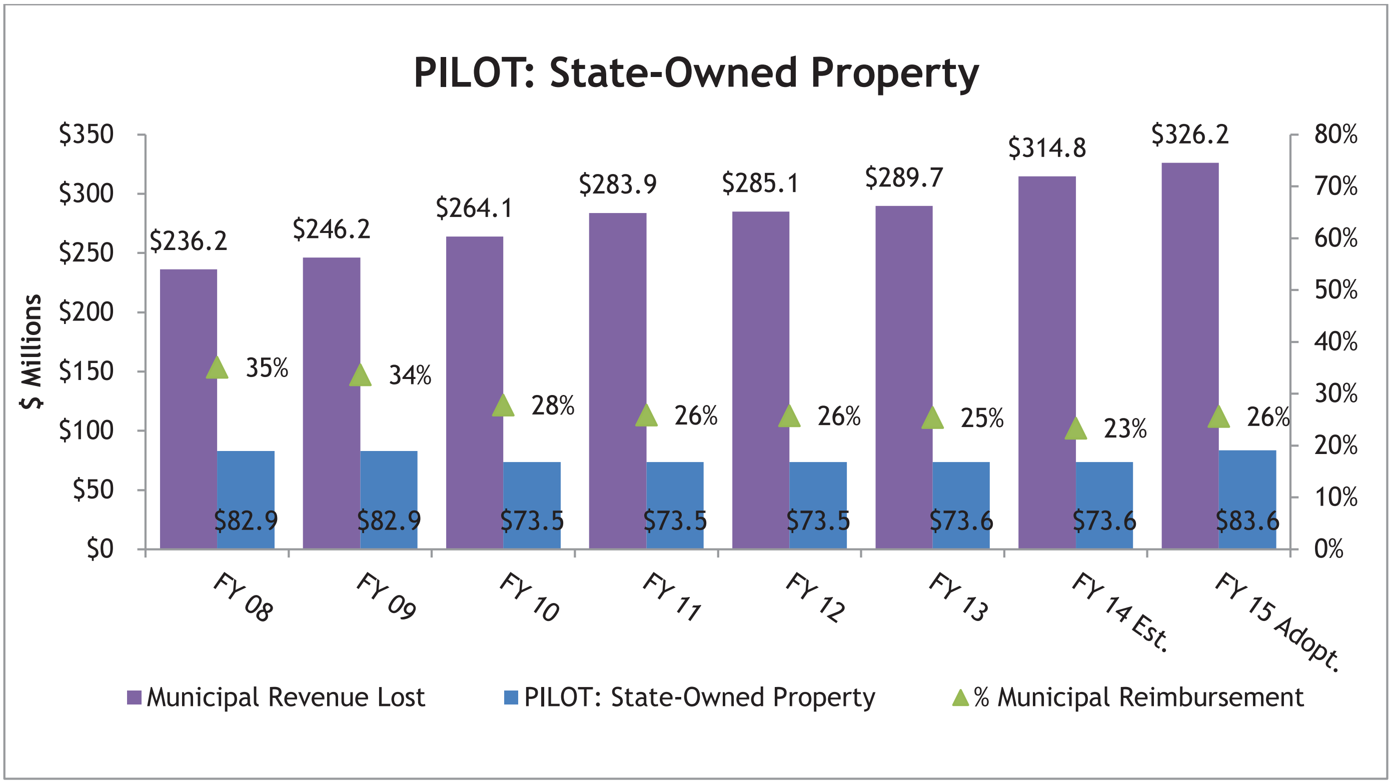
Source: Adopted state budgets; CCM.
Note: This includes only revenue lost on real property and not additional revenue lost on personal property.

PILOT: State-Owned Property

Similarly, the reimbursement rate for most state-owned property is supposed to be 45 percent. It is actually 26 percent.

The actual reimbursement rates are lower due to statutes that allow the amount of the PILOT reimbursements to be reduced on a pro-rated basis when state appropriations are not sufficient. In addition, these PILOT reimbursements cover only real property and do not include revenue lost from state-mandated exemptions on personal property.

Many of our poorer towns and cities host the most tax-exempt property.



Source: Adopted state budgets; CCM.

PILOT: MME – State Commitment Severed

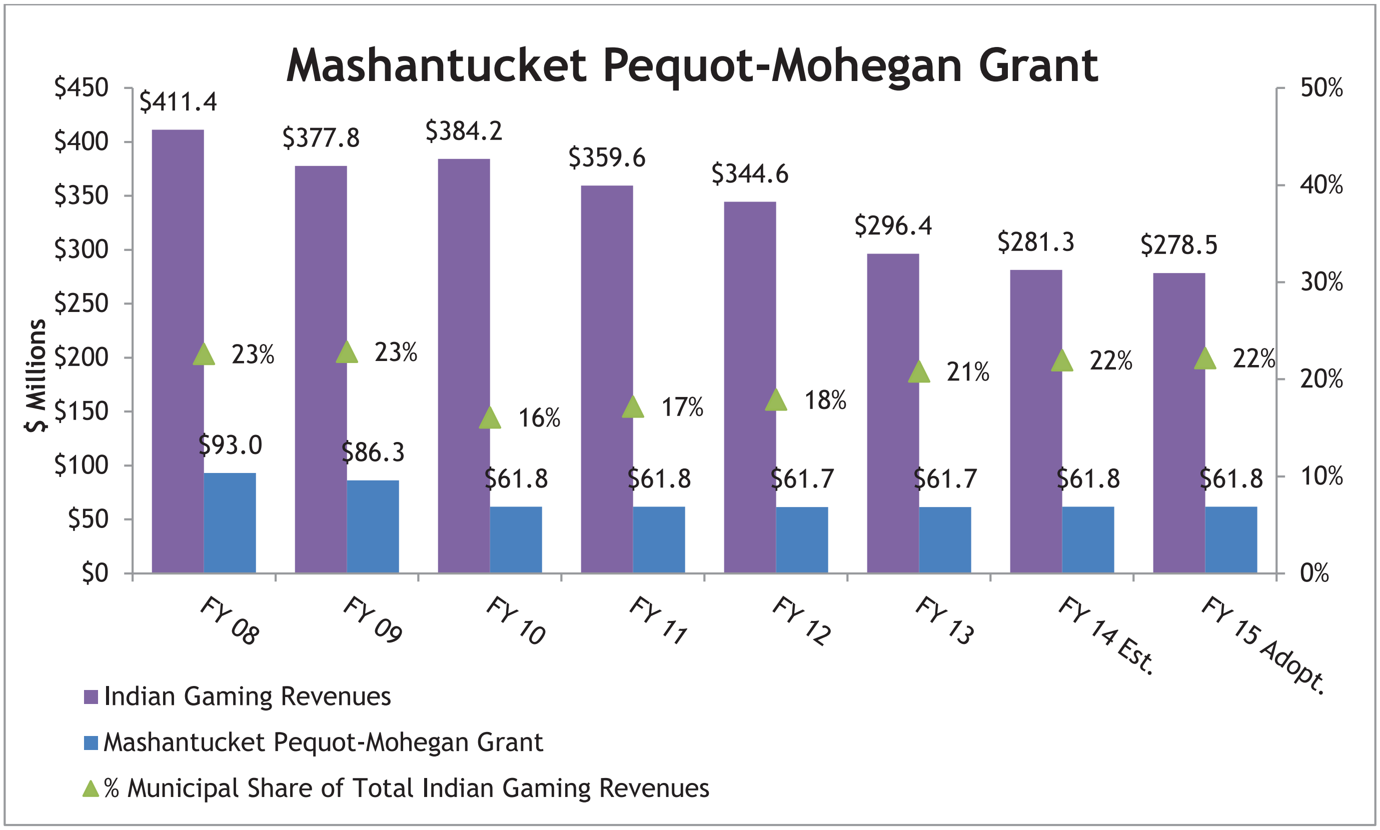
The State mandates that qualified machinery and equipment is exempt from local property taxes. Under the PILOT for manufacturing machinery and equipment (PILOT MME) program, the State was supposed to provide reimbursement to towns and cities in an amount equal to 80 percent of the revenue lost as a result of property tax exemptions. After several years of underfunding the program, the PILOT MME program was eliminated in 2011 and towns and cities lost $50 million in reimbursement.

When PILOT reimbursements fall short, it forces other residential and business property taxpayers to make up the difference. Thus, other property taxpayers are forced to pay for the State's underfunded and unfunded property-tax exemption mandates.

Mashantucket Pequot - Mohegan Grant

The Mashantucket Pequot-Mohegan Fund, which is funded with a portion of slot machine revenues sent to the State by the two Native American casinos, is another significant state aid program. The formula for this grant is based on several components, including the value of state-owned property, private colleges and hospitals, population, grand list strength, and per capita income, among others.

In FY 15, the Pequot-Mohegan grant will provide $61.8 million in revenue to towns and cities, the same as the previous five years. At its inception, municipalities received 78 percent of these gaming revenues. This year they will receive an estimated 22 percent.

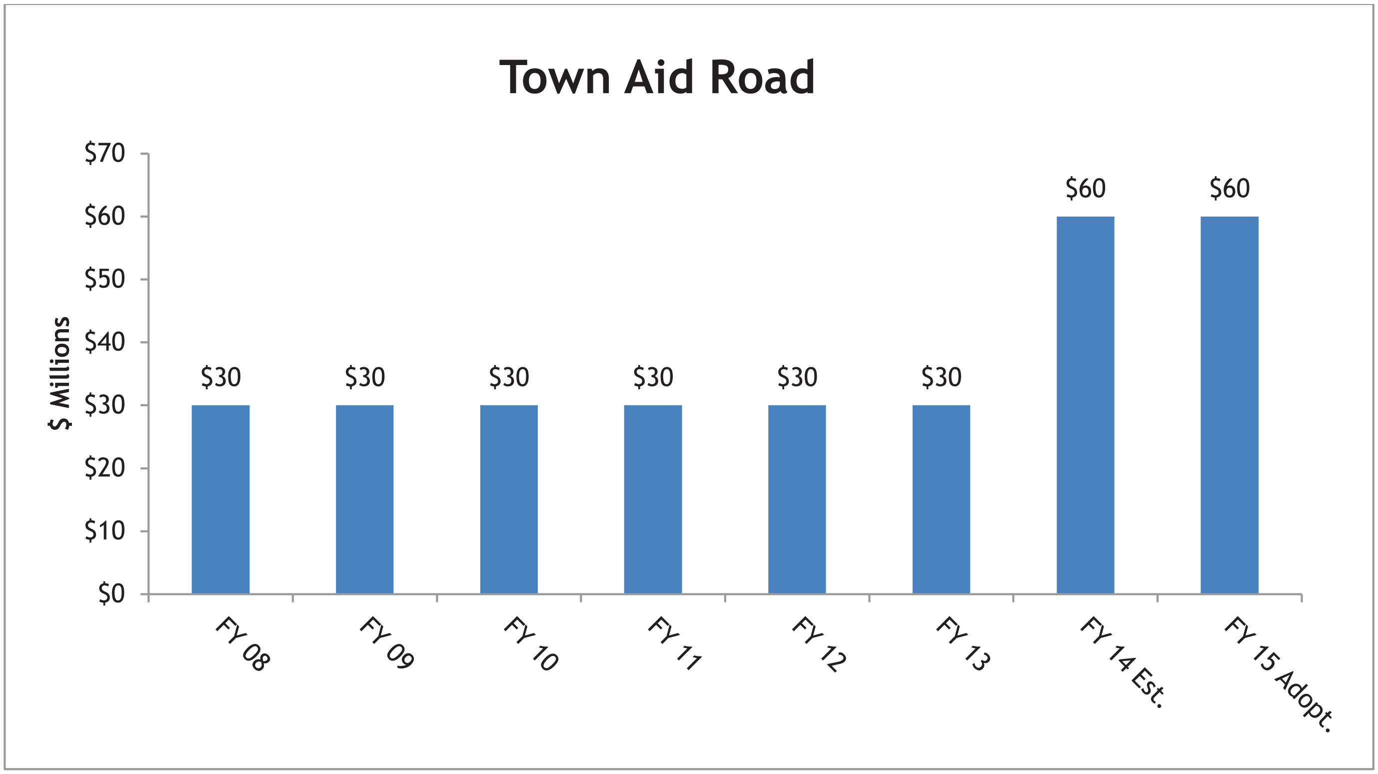


Source: Adopted state budgets; CCM.

Town Aid Road

Another critical grant program is Town Aid Road. This $60 million program provides funding for local road maintenance and improvements. There are more locally-owned road miles than state-owned road miles (17,265 v. 3,733).[10] Unfortunately, even as road maintenance and improvement costs have increased, the grant provided only level funding for seven years, until the welcome doubling of the grant in FY 14. This increase as helped ease the strain on local public works budgets and reduced dependence on the property tax to fund those needs. However, there are still tremendous unmet local infrastructure needs.

[10] State Department of Transportion, 2009 data, latest available.



Source: Adopted state budgets.

LoCIP

The Local Capital Improvement Program (LoCIP) reimburses municipalities for the costs associated with eligible capital improvement projects. Projects must be included in a municipality's five-year capital improvement plan. LoCIP funding has remained flat for many years.

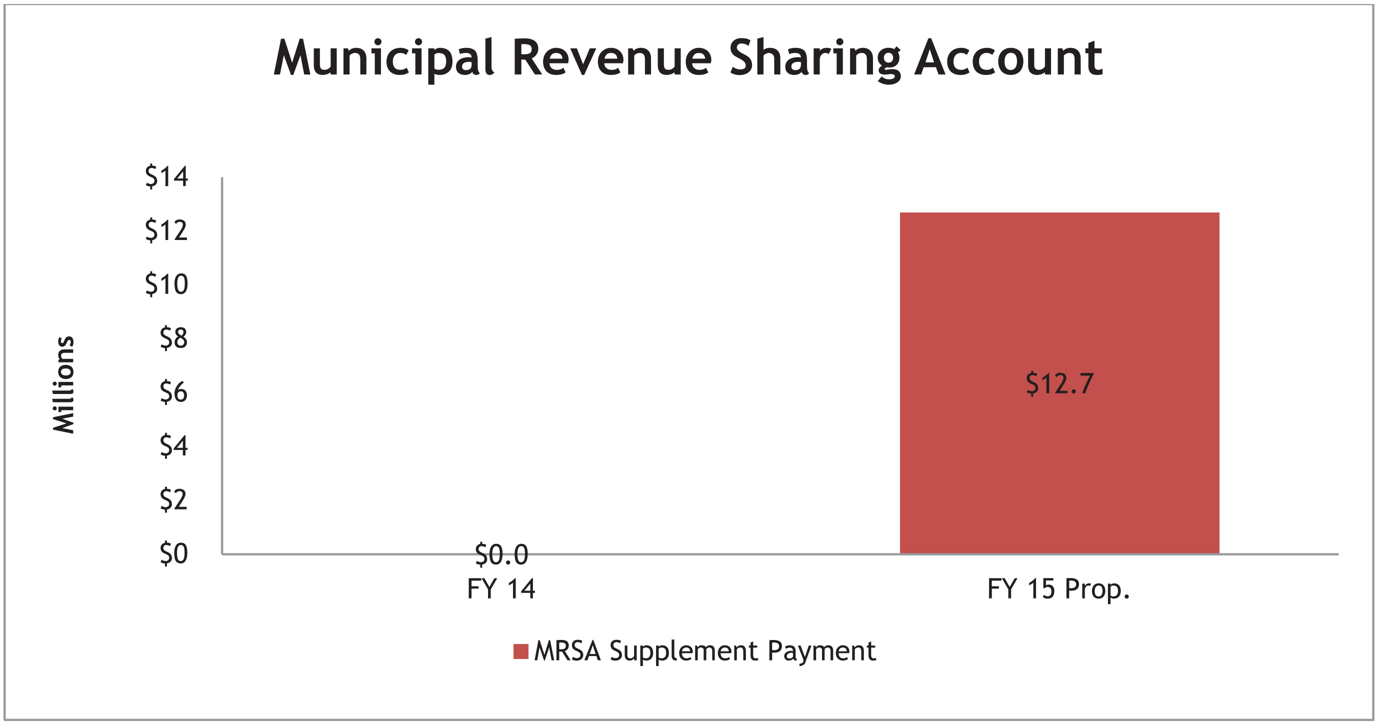
Source: Adopted state budgets.

Municipal Revenue Sharing Account – Promise Unfulfilled

As part of the FY 12-FY 13 biennial state budget, the new groundbreaking Municipal Revenue Sharing Account (MRSA) was created to provide additional financial resources to municipalities. This account is funded through part of the state Sales Tax and part of the state portion of the Real Estate Conveyance Tax.

This marked the first year of direct state-local tax revenue sharing and it established a foundation upon which to reduce the overdependence on property taxes to fund municipal services, particularly preK-12 public education.

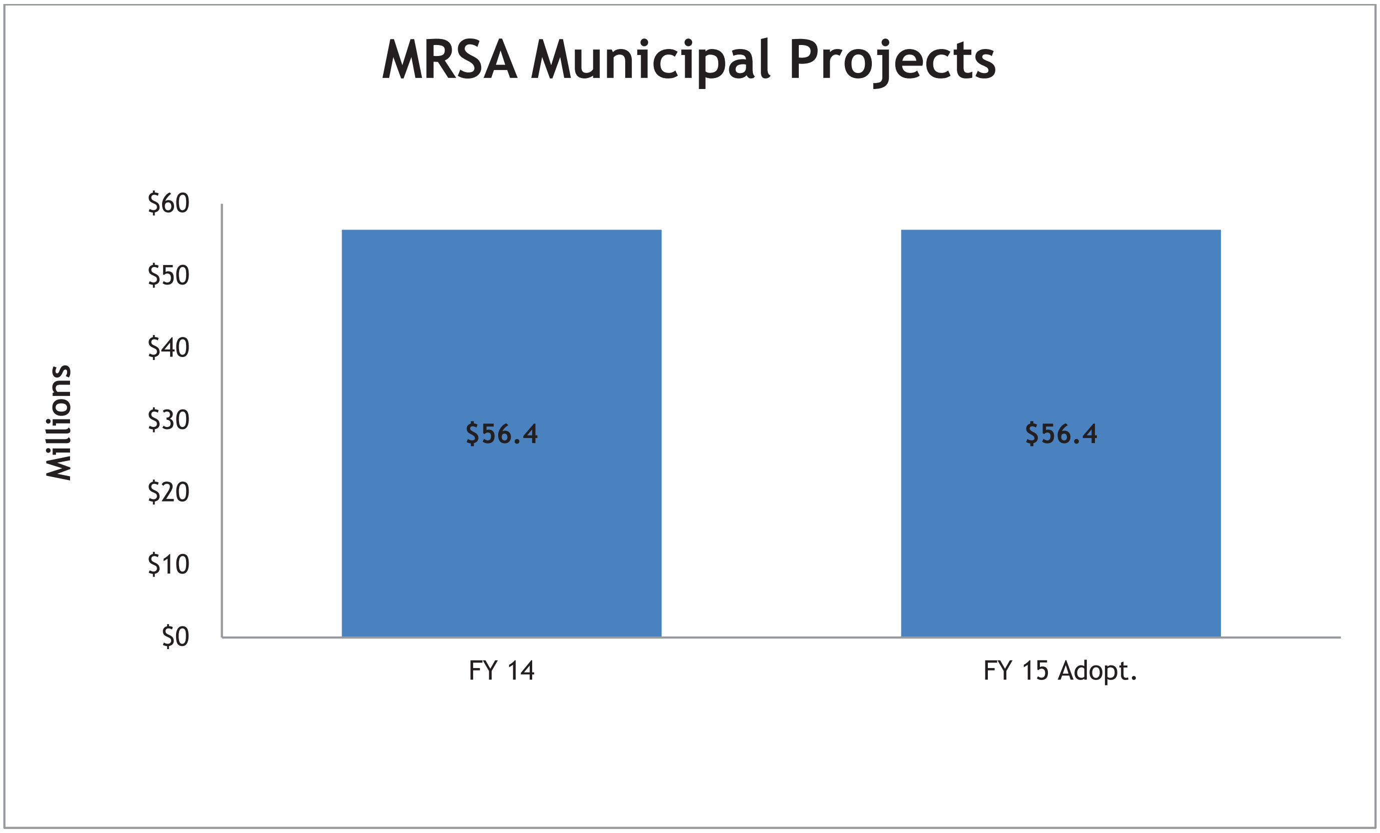
Unfortunately, funding for MRSA was eliminated as part of the FY 14 budget. To make matters worse, the budget eliminated a transfer of the tax revenue into MRSA as of July 1, 2013, resulting in a reduction of at least $12.7 million in the MRSA Supplement Payment. While the $12.7 million was restored to municipalities in FY 15, it is a one-time revenue, and the MRSA account remains unfunded.



Source: Adopted state budgets; CCM.

A new grant program was included as part of the FY 14-FY 15 biennial budget. The MRSA Municipal Projects grant program was bond-funded at $56.4 million in each year of the biennium. This funding must be used for TAR-related projects, though a municipality can request a waiver and, upon approval, use the funds for other capital-related projects.

This new funding was put in place, in part, to compensate for the loss of revenue due to the elimination of funding for MRSA. One concern, however, is that the money is restricted to certain uses, while MRSA was unrestricted revenue for towns and cities. This result is less flexibility for local officials when making budgetary decisions.



Source: Adopted state budgets.

Regional Performance Incentive Program

Another revenue-sharing program is the Regional Performance Incentive Program (RPIP) grant. It is funded through part of the State Hotel Tax and State Car Rental Tax. Funding is available to Councils of Government (COGs) and municipalities on a competitive basis for regional projects. The goal is to encourage municipalities to jointly participate in projects that lower the costs and tax burden related to providing public services.

Unfortunately, as part of the 2012 deficit mitigation package, $8.5 million was swept from the RPIP into the General Fund. This resulted in a setback for many towns and cities looking for seed money to develop regional shared services.

Stagnating non-education aid puts ever more pressure on the property tax.

Education Aid

Statewide, 59 percent of municipal budgets go to pay for preK-12 public education. At $7.7 billion, preK-12 public education is the single most expensive municipal service in Connecticut.[11]

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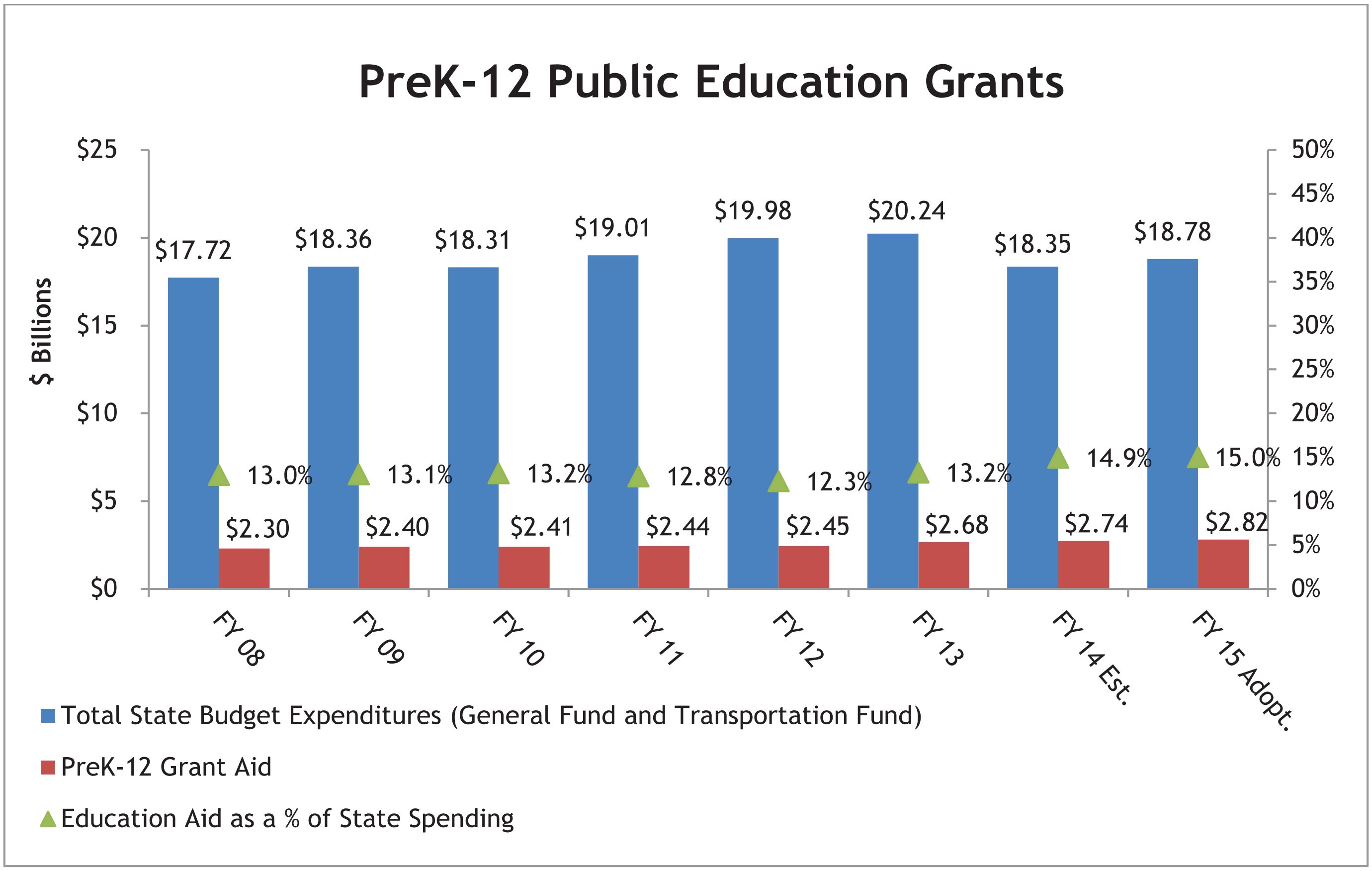
[11] OPM, Municipal Fiscal Indicators, 2008-2012.

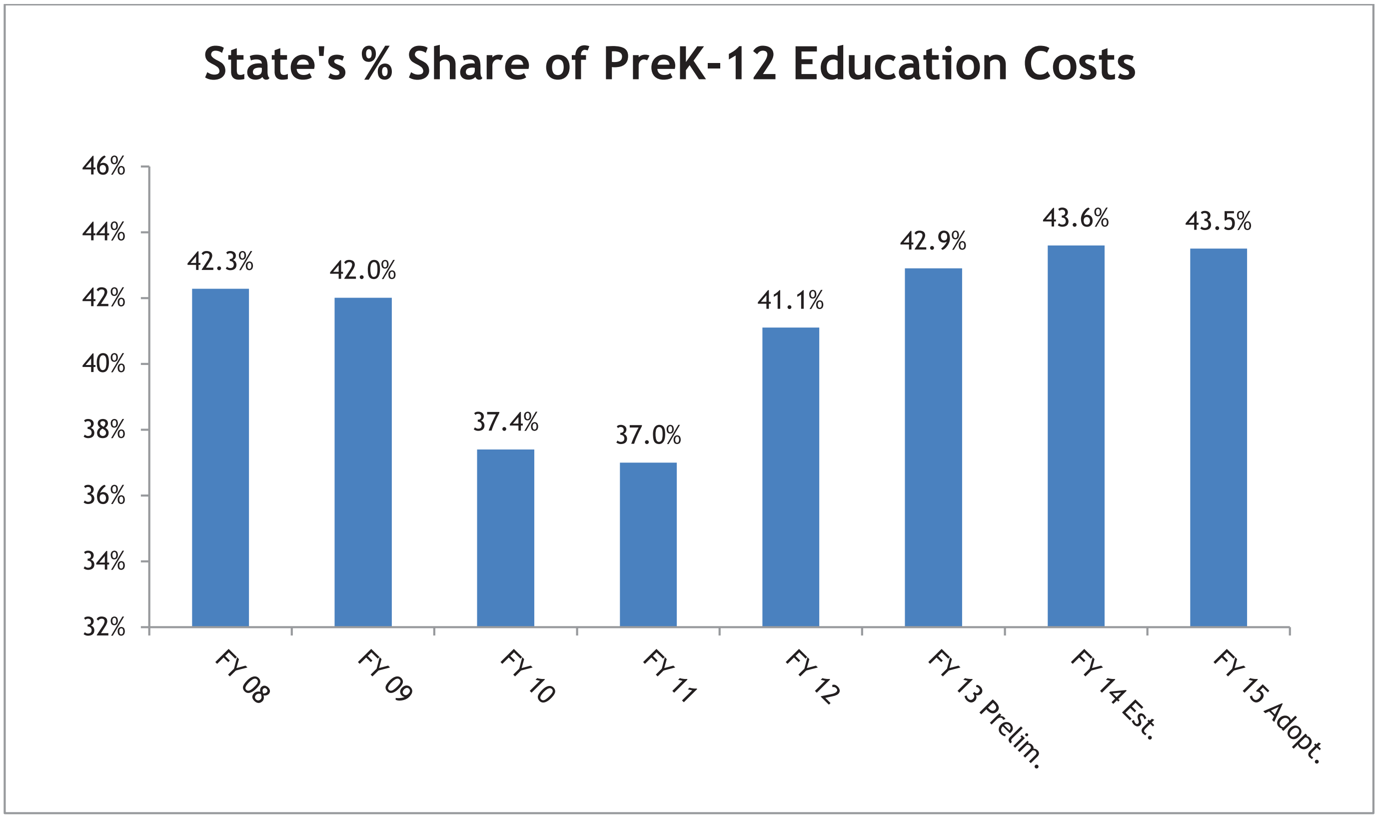


Source: Adopted state budgets; CCM.
Note: Total state budget expenditures are reduced starting in FY 14 due to the removal of the federal share of the Medicaid appropriation totaling approximately $2.8 billion.

Education aid to municipalities is $2.8 billion in FY 15, 85 percent of total state aid to towns and cities.

At least an equal partnership between state and local revenue sources has been a longstanding goal of the Connecticut State Board of Education. In 1989-90, the state share of total education costs reached 45.5 percent, the closest it has ever come to that goal.[12] Any movement toward that mark is important because additional state dollars can reduce dependence on property taxes and lessen the inequity in education funding.[13]

[12] State Department of Education (SDE).
[13] More details on education finance will be provided in an upcoming CCM policy report.



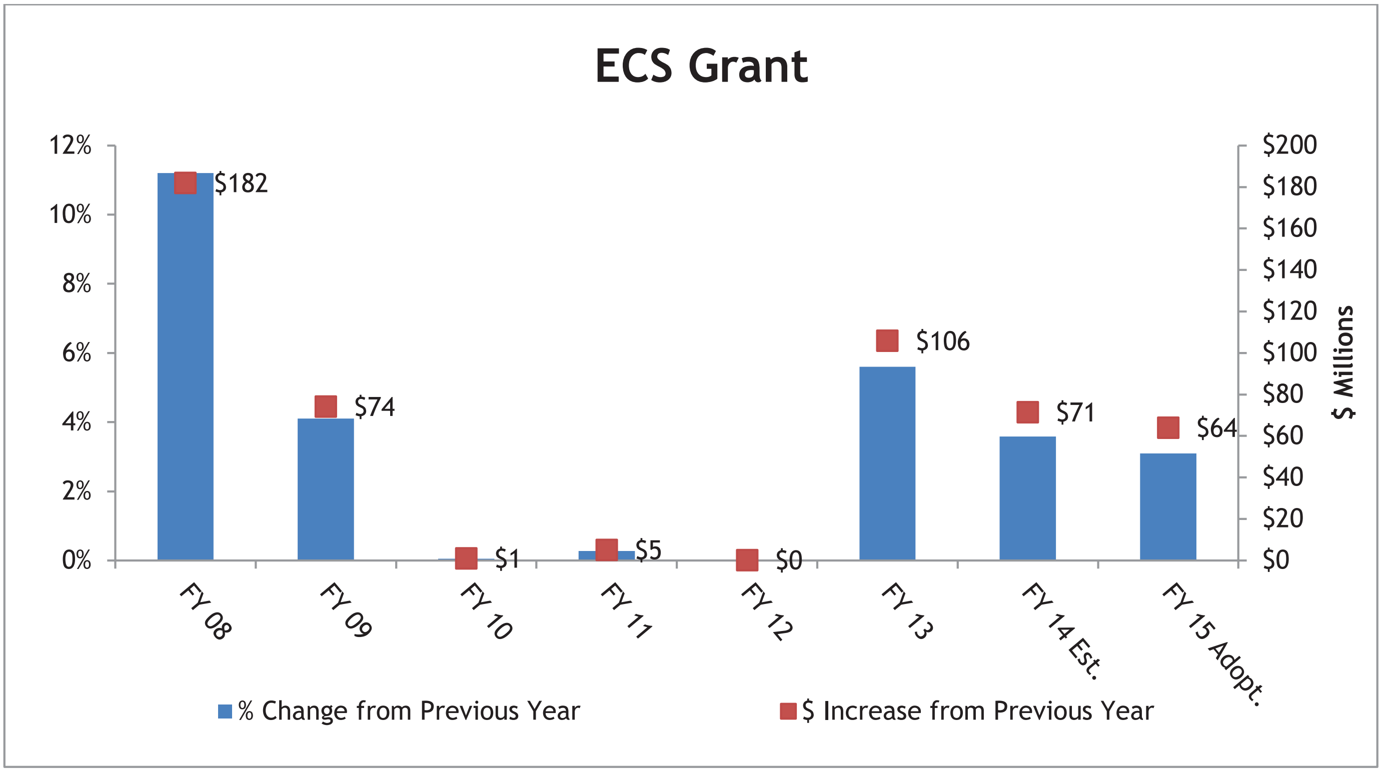
Source: State Department of Education; CCM estimates.

Education Cost Sharing (ECS)

The ECS grant is the State's largest general education assistance grant. It will total $2.07 billion this year. While the recent increases in ECS are welcome, they do little to address the chronic underfunding of ECS. The ECS grant is currently underfunded by about $700 million, and amount that would be shown to be even greater under a proper adequacy study.[14]

The education reform initiatives enacted in 2012 were not accompanied by significant increases in new state dollars. More will be asked of struggling districts in order to leverage modest increases in education aid.

[14] CCM estimate based on SDE data for 2013-14.



Source: Adopted state budgets; State Comptroller reports.
Note: Since FY 13, ECS totals include charter school funding that was moved into the ECS account.

Special Education

Special education is a significant cost driver for local government. These costs now surpass the $1.7 billion mark statewide. This spending accounts for about 22 percent of total current expenditures for education in Connecticut, and annual costs have been growing as much as six percent in recent years.[15]

The State provides the Excess Cost-Student Based grant to help reimburse municipalities for the costs of special education. The grant provides a circuit breaker once the expenditures for a student exceed a certain level, currently 4.5 times the per pupil spending average of the district. So, for example, if a municipality spends an average of $10,000 per pupil, it must spend at least $45,000 for a special-education student before being eligible for any state reimbursement.

Unfortunately, the grant has been level-funded for six years. This means that the state reimbursement has not kept pace with the escalating costs of special education. Without full funding, towns and cities are forced to find other ways to pay for special education. Not surprisingly, the burden falls on residential and business property taxpayers and non-education services.

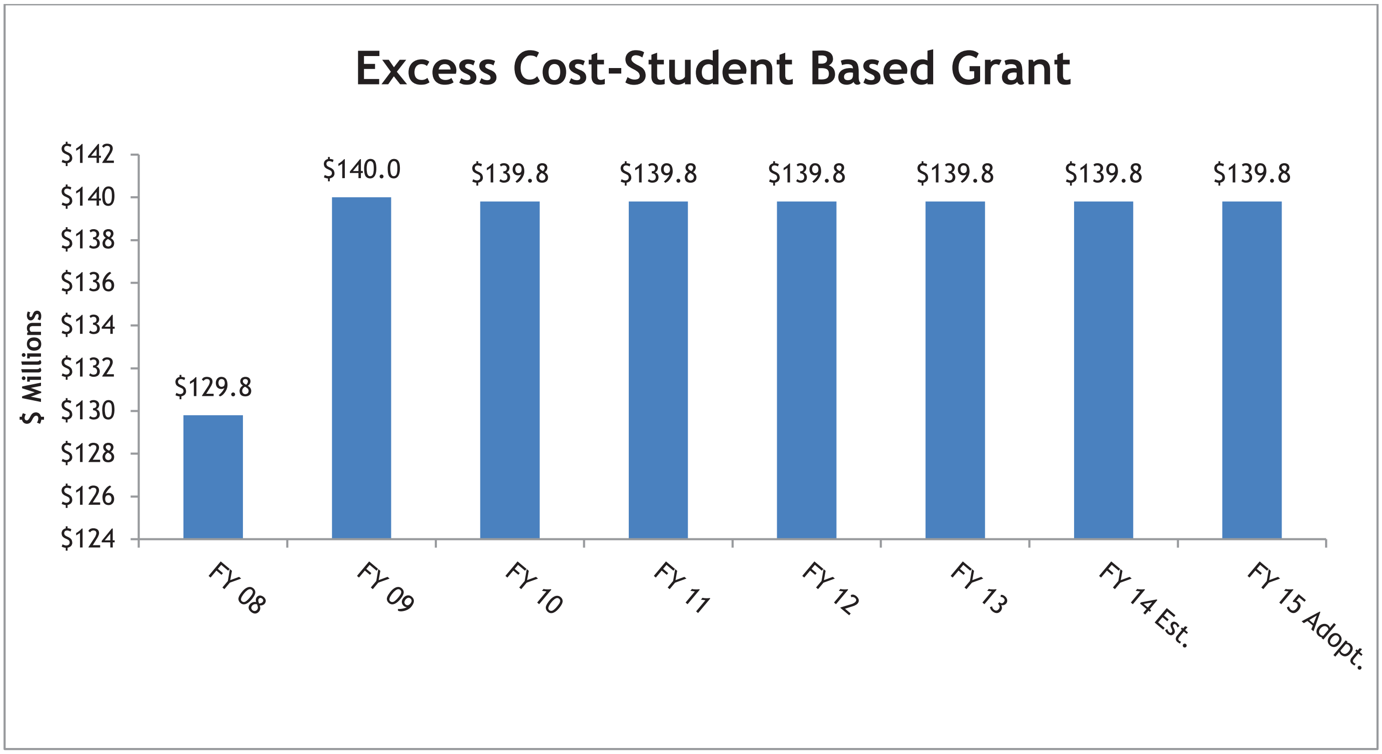
Minimum Budget Requirement MBR

Another education issue that puts pressure on the property tax is the MBR. This state mandate essentially requires towns and cities to budget at least as much on education in the current year as they did the previous year.

[15] SDE, 2012-13 data, latest available

The imposition of the MBR has meant that no matter what efficiencies have been found in education budgets, the budgets cannot be significantly reduced. In an era in which every other state and local agency are having their budgets closely examined, one entity – boards of education – have been held to a different standard and shielded from taxpayer and voter control.

The State, which has chronically underfunded preK-12 public education, instead forces municipalities through the MBR and other mandates to pay for state underfunding. The result: non-education service cutbacks and even higher property taxes.

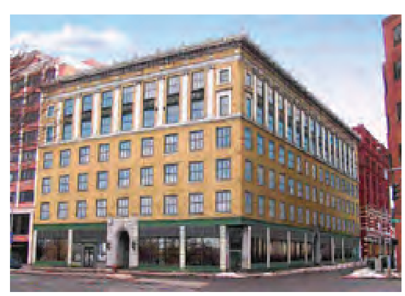


Source: Adopted state budgets; State Comptroller reports.

It is clear that a key to property tax reform in Connecticut is education finance reform. The two are directly linked. Without significant additional state support, towns and cities have few funding options aside from the property tax and diverting funding support from non-education services (police, fire, public works, elderly services, etc.) to deal with escalating regular and special education costs and non-education service costs.

More details on education finance reform will be provided in an upcoming CCM policy report.

Disparities Among Towns and Cities



While all communities in Connecticut have felt the impact of flat to decreasing state aid in the last decade, some have been impacted more than others. There is a significant disparity in property and income wealth among municipalities in our state.

The adjusted equalized net grand list per capita (AENGLC) of the wealthiest town (Greenwich) is more than 60 times greater than that of the poorest town (Hartford). While Connecticut has the highest per-capita income in the nation, per capita income (PCI) in New Canaan is almost six times higher than in Hartford.[16]

The greater the disparity in property and income wealth becomes, the greater the need for additional state aid to help balance the scales.

Disparities are found not only in wealth, but in service demands as well. Urban communities are required to provide a wider array of public services than many less-developed and less-populated towns. Urban communities are the regional hubs of employment, health and social services, culture and entertainment, and tax-exempt property. Many of these large and smaller cities and urbanized towns are among the poorest in Connecticut.

- The poverty rates in Bridgeport, Hartford, New Haven, and Waterbury are at least twice as high as the rate for the state as a whole.
- These cities experience much higher unemployment rates (Hartford – 12.3%, Waterbury – 10.4%, Bridgeport – 10.1%, New Haven – 9.2%) than the state average (6.4%).[17]
- While 34.4 percent of Connecticut's K-12 students are eligible for free/reduced-price meals, over 90 percent are eligible in both Bridgeport and Hartford.[18]
- About 100,000 people commute into Bridgeport, Hartford, New Haven, and Waterbury for employment.[19]

The combination of lower revenue-generating capacity and higher service demand and costs has created significant fiscal hardships for impacted communities, and these difficulties continue to worsen.

In fact, Hartford, New Haven, and Bridgeport are among the poorest cities in America.

HOW CAN WE REDUCE MUNICIPAL DEPENDENCE ON THE PROPERTY TAX?

Over-reliance on the property tax coupled with inadequate state aid, particularly education aid, place Connecticut towns and cities in a severe fiscal bind. Municipalities are forced to raise already onerous property tax rates, cut back non-education services, and divert scarce resources to pay for escalating regular and special-education costs. Connecticut is one of the few states locked into such an antiquated, local-revenue system.

[16] SDE, 2014-15 school year.
[17] CT Department of Labor, June 2014.
[18] SDE, CEDaR, 2010-11 data.
[19] CCM estimate based on DECD Town Profiles.

While there are aspects of local-option taxation that are of particular concern in a small state such as Connecticut, there are other proven approaches that should be on the table as we seek a way out of the property tax chokehold:

1. **Education Finance Reform**: Reforming preK-12 public education finance is a key to property tax reform in Connecticut. Chronic state underfunding of preK-12 public education is the single largest contributor to the overreliance on the property tax in our state. The ECS grant alone is underfunded by about $700 million. Special-education costs are now approaching $2 billion per year and impose staggering per-pupil cost burdens on host communities. Special-education costs should be borne collectively by the State, not individual school districts.

2. **Restore State Revenue Sharing**: The Municipal Revenue Sharing Account (MRSA) was groundbreaking when it was introduced in 2011. This account was funded through part of the State Sales Tax and part of the State Real Estate Conveyance Tax. The elimination of its funding, however, is a cause for concern and will further increase the reliance on property taxes to fund municipal services. Funding for the program should be restored to add to the long-standing municipal aid programs that help fund local government.

3. **Fully Fund PILOT Programs**: The State should increase and fully fund PILOT to provide reimbursement to municipalities for 100 percent of the revenue lost due to state-mandated property tax exemptions. In absence of full funding of PILOT, the State should consider alternatives to property tax exemptions, such as the reverse PILOT proposed in 2014.

4. **Inter-municipal and Regional Collaboration**: State financial and technical assistance incentives for increased inter-municipal and regional collaboration should be expanded. The Regional Performance Incentive Program (RPIP) Grant – funded through a share of the State Hotel Tax and Car Rental Tax – is a great foundation upon which to build stronger incentives and support for cooperative efforts. Providing towns and cities with the tools and authority to deal with service delivery, revenue raising and sharing, and other issues on a regional basis would result in increased efficiencies and a reduction in dependency on single-town grand lists.

5. **Mandate Reform**: The State should eliminate or modify unfunded and underfunded mandates, beginning with the MBR. This would lower the property tax burden without adding additional costs at the state level. (More details on mandates reform will be provided in an upcoming CCM policy report.)

The over-dependence on the property tax is unsustainable, and Hometown Connecticut is in desperate need of revenue assistance. Harnessing the revenue-raising capacity of the State to equitably and adequately fund preK-12 public education and share resources with local governments and regions can reduce the over-reliance on property taxes in Connecticut.

Notes

CCM: THE STATEWIDE ASSOCIATION OF TOWNS AND CITIES

CONNECTICUT CONFERENCE OF MUNICIPALITIES

THE VOICE OF LOCAL GOVERNMENT ™

The Connecticut Conference of Municipalities (CCM) is Connecticut's statewide association of towns and cities. CCM is an inclusionary organization that celebrates the commonalities between, and champions the interests of, urban, suburban and rural communities. CCM represents municipalities at the General Assembly, before the state executive branch and regulatory agencies, and in the courts. CCM provides member towns and cities with a wide array of other services, including management assistance, individualized inquiry service, assistance in municipal labor relations, technical assistance and training, policy development, research and analysis, publications, information programs, and service programs such as workers' compensation and liability-automobile-property insurance, risk management, and energy cost-containment. Federal representation is provided by CCM in conjunction with the National League of Cities. CCM was founded in 1966.

CCM is governed by a Board of Directors, elected by the member municipalities, with due consideration given to geographical representation, municipalities of different sizes, and a balance of political parties. Numerous committees of municipal officials participate in the development of CCM policy and programs. CCM has offices in New Haven (headquarters) and in Hartford.

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