The Property Tax: How Over-Reliance Jeopardizes Connecticut’s Economic Future
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If you have questions concerning this report, please contact Ron Thomas (rthomas@ccm-ct.org) or George Rafael (grafael@ccm-ct.org) of CCM, at 203-498-3000.
September, 2016

Dear Candidates:

Thank you for running for public office in Connecticut.

It is one of the highest callings to serve the residents and businesses of our state at the State Legislature and in the U.S. Congress.


This report represents one very important example of how CCM is here for you as a resource to help you build your knowledge base to best serve Connecticut voters.

If you have any question on this key public policy issue or any other issue affecting Connecticut’s property taxpayers, please contact us at CCM.

And best of luck with your campaign!

Sincerely,

Joe DeLong,
Executive Director,
Connecticut Conference of Municipalities
Introduction

Towns and cities in Connecticut are responsible for providing the majority of public services in our state: elementary and secondary education; public safety; roads and other infrastructure; social services; recreation; and others. They must do so while meeting numerous mandates, often underfunded or unfunded, from both the federal and state government.

Funding for these critical 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 if two conditions exist: (1) the property and income wealth of a community can generate enough revenue at a reasonable cost to taxpayers to meet the need for public services; and (2) state aid is sufficient to fill local revenue gaps. For many communities in our state, neither condition exists.

It is increasingly clear that relying on the property tax to fund local government services in Connecticut is unsustainable.

SUMMARY

Connecticut’s towns and cities rely on the property tax to fund the majority of local services. It is basically “the only game in town.” This over-reliance is caused by a number of issues.

- Lack of other local-source revenue options
- State laws and mandates limiting the effectiveness of the property tax as a revenue generator, particularly regarding tax exemptions
- Uneven and inconsistent non-education aid
- Inadequate state funding of preK-12 public education

There are steps the State can take to address these issues.

- Allow municipalities to collect local-option taxes
- Limit property tax exemptions
- Maintain non-education funding and commit to revenue sharing
- Meet the obligations of funding preK-12 education
The property tax is the single largest tax on residents and businesses in our state. The levy in Connecticut was $9.7 billion in 2014. 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 4th in mean effective property tax rates on owner-occupied housing (1.98 percent for Connecticut v. 1.14 percent for the US).

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. Eleven towns depend on property taxes for at least 90 percent of all their revenue. Another 55 municipalities rely on property taxes for at least 80 percent of their revenue.

The property tax accounts for 39 percent of all state and local general-fund taxes. In FY 14, Connecticut businesses paid over $780 million in state corporate income taxes, but over $1 billion in local property taxes.

Property Tax Exemptions

Another problem created by the over-reliance on the property tax in Connecticut involves state-mandated tax exemptions on real and personal property. There are currently at least 77 mandated property tax exemptions in state statutes, and towns and cities lose staggering amounts of revenue as the result of these exemptions. These State-imposed obligations and State-imposed revenue losses force all municipalities to increase their property tax rates. While the State reimburses municipalities for some of the lost revenue through payments in lieu of taxes (PILOTs), those reimbursements fall short.

Property tax exemptions impact all communities, but they impact some municipalities significantly. For example, in both Hartford and Mansfield, over half the property is exempt from taxation. In New Haven, that number is almost 50 percent. In New London and Windham, more than a third of property is exempt.

The result is that these municipalities have a limited base from which they can generate revenue.
Per Capita Property Tax Collections, FY 10

$2,522

$1,434

Source: Tax Foundation, latest data available

Municipal Revenue Sources, FY 14

- Property Tax: 71%
- Intergovernmental: 25%
- Charges, Fees, and Other Sources: 4%

Source: OPM, Municipal Fiscal Indicators, 2010-2014
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. 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.

Connecticut is one of only 15 states that limit municipalities to raise revenue to the property tax. Twenty-nine states allow at least some municipalities to levy income or sales taxes along with property taxes. Six states allow at least some municipalities to level all three taxes. (See Appendix A.)

Many states also have county governments that levy taxes and provide services, in addition to those at state and municipal levels.

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

The Uncertainty of Intergovernmental Revenue

Following 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 this funding, however, that increase 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.

Why Is Connecticut So Reliant On The Property Tax?
Total Municipal Aid

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Total State Budget Expenditures (GF, STF, MRSA)</th>
<th>Municipal Aid</th>
<th>Municipal Aid as % of State Spending</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY 10</td>
<td>18.31</td>
<td>2.83</td>
<td>15.5%</td>
</tr>
<tr>
<td>FY 11</td>
<td>19.01</td>
<td>2.85</td>
<td>15.0%</td>
</tr>
<tr>
<td>FY 12</td>
<td>19.98</td>
<td>2.91</td>
<td>14.6%</td>
</tr>
<tr>
<td>FY 13</td>
<td>20.24</td>
<td>2.98</td>
<td>14.7%</td>
</tr>
<tr>
<td>FY 14</td>
<td>18.35</td>
<td>3.12</td>
<td>17.0%</td>
</tr>
<tr>
<td>FY 15</td>
<td>18.82</td>
<td>3.19</td>
<td>17.0%</td>
</tr>
<tr>
<td>FY 16 Est.</td>
<td>19.51</td>
<td>3.23</td>
<td>16.6%</td>
</tr>
<tr>
<td>FY 17 Adopt.</td>
<td>19.59</td>
<td>3.32</td>
<td>16.9%</td>
</tr>
</tbody>
</table>

Source: Adopted state budgets; CCM

OWN-SOURCE REVENUE IN CT

State Taxes:
- Personal Income
- Sales and Use
- Corporate Income
- Public Service Corporations
- Inheritance Tax
- Insurance Companies
- Cigarettes
- Oil Companies
- Alcoholic Beverages
- Admissions, Dues and Cabaret
- Motor Fuels

Local Taxes:
- Property Tax

State & Local Taxes:
- Real Estate Conveyance

Other:
- Fees, Fines & Licenses
- Federal Government
- Miscellaneous
State Aid to Municipalities

The State provides over $3 billion in education and non-education aid to towns and cities out of a $20 billion state budget. This accounts for more than 20 percent of all local revenue. While this is a substantial amount of money, the funding is not without its issues.

Non-Education Aid

Municipalities receive state funding through a variety of non-education grant programs. The amount of non-education aid has fluctuated dramatically over the years.

While some programs, such as Town Aid Road, have seen an increase in funding in recent years, others, such as Payment in Lieu of Taxes (PILOT), have been reduced. These shifts have created uncertainty in municipal budgeting from year to year. They also impact communities disproportionately. While there may be an overall increase in statewide municipal aid in a given year, a particular municipality may actually see a decrease in funding due to formula calculations and distribution decisions.

Payments in Lieu of Taxes (PILOT)

Municipalities receive payments in lieu of taxes (PILOT) 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 more than $700 million.

The reimbursement rate for private college and hospital property is supposed to be 77 percent of lost revenue. It is estimated to be only 29 percent in the current year. Similarly, the reimbursement rate for state-owned property is supposed to be 45 percent of lost revenue for most property. It is estimated to be only 20 percent in the current year.

Even more concerning than the reimbursement rates themselves is that...
fact that those rates have continued to decrease over time.

**Municipal Revenue Sharing Account**

As part of the FY 12-FY 13 biennial state budget, the Municipal Revenue Sharing Account (MRSA) was created to provide additional revenue 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 over-dependence on property taxes to fund municipal services.

Unfortunately, funding for MRSA was eliminated as part of the FY 14 budget.

In FY 17, MRSA will again be funded through a portion of the state sales tax. While this new revenue is welcome, there have already been indications that future funding is in jeopardy. Even before the first payments have been made, the State has reduced the amounts towns and cities are set to receive.

The revenue-sharing amount for FY 17 was originally estimated to be $109.3 million.\(^\text{12}\) The amount is now expected to be $79.9 million.\(^\text{13}\)

Given the history of MRSA, and the State’s dire fiscal situation, it is clear why municipal officials are so concerned about the long-term viability of this funding source.

**Education Aid**

At $8.1 billion in local cost, preK-12 public education is the single most expensive municipal service in Connecticut.\(^\text{14}\) Statewide, 60 percent of municipal budgets go to pay for preK-12 public education. In some towns, that percentage can be greater than 80 percent of the overall budget.

The Education Cost Sharing (ECS) grant is the State’s largest education grant. It will total just over $2 billion this year. The ECS grant is currently underfunded by at least $600 million under the current formula.\(^\text{15}\)

Special education is a significant cost driver for local government. These costs now approach $2 billion statewide. This spending accounts for over 22 percent of total current expenditures for education in Connecticut.\(^\text{16}\)

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 not been increased in almost a decade. 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, either through reducing other services or increasing taxes on residential and business property taxpayers.

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 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 report.)
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, reduce non-educations 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.

There are approaches that need to be considered as we seek a way out of the property tax choke-hold.

- 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 over-reliance on the property tax in our state. The ECS grant alone is underfunded by over $600 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 and not individual school districts.

- Fully fund PILOT: The State must fully fund PILOT to provide 100% reimbursement to municipalities for revenue lost due to state-mandated property tax exemptions. In absence of full funding of PILOT, the State should consider eliminating some property tax exemptions.

- Maintain State Revenue Sharing: Renewed funding for the Municipal Revenue Sharing Account is much needed and welcome. The State must commit to maintain this program and not rescind funding in future years.

- Allow Local-Option Taxes: Municipalities should be allowed to levy certain types of local-option taxes in order to reduce property taxes. For example, locally levied sales taxes or hotel taxes can be considered in municipalities where they make sense.

- Allow Regional Tax Levies: Councils of government (COGs) could levy taxes that would fit best with their particular region. COGs comprise chief elected officials, people who are accountable to the voters of their communities for their decisions. For example, a local-option sales tax might drive retail activity to the suburbs and away from cities, but a regional sales tax would not have the same effect. If a retailer wants access to the market of a given region, the tax would apply no matter where it locates. Granting local-option taxing authority to COGs would diversify the municipal revenue base. It would combine the advantages of local-revenue enhancement while tailoring it to regional needs and avoiding negative competition between urban centers and suburbs. It would also be a major step towards increasing regional cooperation and thus improve overall governmental efficiency.
<table>
<thead>
<tr>
<th>State</th>
<th>Notes</th>
<th>State</th>
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</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>Property, sales, income (19 cities)</td>
<td>Nevada</td>
<td>Property</td>
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<tr>
<td>Alaska</td>
<td>Property, sales</td>
<td>New Hampshire</td>
<td>Property</td>
</tr>
<tr>
<td>Arizona</td>
<td>Property (with voter approval), sales</td>
<td>New Jersey</td>
<td>Property,</td>
</tr>
<tr>
<td>Arkansas</td>
<td>Property, sales, income (not used by any municipality)</td>
<td>New Mexico</td>
<td>Property, sales</td>
</tr>
<tr>
<td>California</td>
<td>Property, sales</td>
<td>New York</td>
<td>Property, sales, income (New York City and Yonkers only)</td>
</tr>
<tr>
<td>Colorado</td>
<td>Property, sales</td>
<td>North Carolina</td>
<td>Property</td>
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<tr>
<td>Connecticut</td>
<td>Property</td>
<td>North Dakota</td>
<td>Property, sales</td>
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<tr>
<td>Delaware</td>
<td>Property, income (Wilmington only)</td>
<td>Ohio</td>
<td>Income, property</td>
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<td>Florida</td>
<td>Property</td>
<td>Oklahoma</td>
<td>Sales</td>
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<td>Property, sales</td>
<td>Oregon</td>
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<td>Hawaii</td>
<td>Property (Honolulu is only municipality in Hawaii)</td>
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<td>Property, income, sales (Philadelphia only)</td>
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<td>Rhode Island</td>
<td>Property</td>
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<td>Illinois</td>
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<td>South Carolina</td>
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<td>Property, income</td>
<td>South Dakota</td>
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<td>Virginia</td>
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<td>Property, income (Baltimore</td>
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<td></td>
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<td>Missouri</td>
<td>Property, sales, income (Kansas City and St. Louis only)</td>
<td>Source: National League of Cities, Cities and State Fiscal Structure, 2015</td>
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<tr>
<td>Montana</td>
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<td>Nebraska</td>
<td>Property, sales</td>
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</table>
Appendix B
State-Mandated Property Tax Exemptions

The following property is exempt from taxation per Connecticut General Statutes (C.G.S. §12-81).

1. Property of the United States
2. State property, reservation land held in trust by the state for an Indian tribe.
3. County Property (repealed).
4. Municipal Property.
5. Property held by trustees for public purposes.
6. Property of volunteer fire companies and property devoted to public use.
7. Property used for scientific, educational, literary, historical or charitable purposes.
8. College property.
9. Personal property loaned to tax-exempt educational institutions
10. Property belonging to agricultural or horticultural societies.
11. Property held for cemetery use.
12. Personal property of religious organizations devoted to religious or charitable use.
13. Houses of religious worship.
14. Property of religious organizations used for certain purposes.
15. Houses used by officiating clergymen as dwellings.
16. Hospitals and sanatoriums.
17. Blind persons.
18. Property of veterans’ organizations.
   a. Property of bona fide war veterans’ organization.
   b. Property of the Grand Army the Republic.
19. Veteran’s exemptions.
20. Servicemen and veterans having disability ratings.
21. Disabled veterans with severe disability.
   a. Disabilities.
   b. Exemptions hereunder additional to others. Surviving spouse’s rights.
   c. Municipal option to allow total exemption for residence with respect to which veteran has received assistance for special housing under Title 38 of the United States Code.
22. Surviving spouse or minor child of serviceman or veteran.
23. Serviceman’s surviving spouse receiving federal benefits.
24. Surviving spouse and minor child of veteran receiving compensation from Veteran’s Administration.
25. Surviving parent of deceased serviceman or veteran.
27. Property of Grand Army Posts.
30. Fuel and provisions.
31. Household furniture.
32. Private libraries.
33. Musical instruments.
34. Watches and jewelry.
35. Wearing apparel.
37. Mechanic’s tools.
38. Farming tools.
39. Farm produce.
40. Sheep, goats, and swine.
41. Dairy and beef cattle and oxen.
42. Poultry.
43. Cash.
44. Nursery products.
45. Property of units of Connecticut National Guard.
46. Watercraft owned by non-residents (repealed).
47. Carriages, wagons, and bicycles.
48. Airport improvements.
49. Nonprofit camps or recreational facilities for charitable purposes.
State-Mandated Property Tax Exemptions, continued

The following property is exempt from taxation per Connecticut General Statutes (C.G.S. §12-81).

50. Exemption of manufacturers’ inventories.
51. Water pollution control structures and equipment exempt.
52. Structures and equipment for air pollution control.
53. Motor vehicle of servicemen.
54. Wholesale and retail business inventory.
55. Property of totally disabled persons.
56. Solar energy systems.
57. Class I renewable energy sources and hydropower facilities.
58. Property leased to a charitable, religious, or nonprofit organization.
59. Manufacturing facility in a distressed municipality, targeted investment community, or enterprise zone.
60. Machinery and equipment in a manufacturing facility in a distressed municipality, targeted investment community, or enterprise zone.
61. Vessels used primarily for commercial fishing.
62. Passive solar energy systems.
63. Solar energy electricity generating and cogeneration systems.
64. Vessels.
65. Vanpool vehicles.
66. Motor vehicles leased to state agencies.
67. Beach property belonging to or held in trust for cities.
68. Any livestock used in farming or any horse or pony assessed at less than $1000.
69. Property of the Metropolitan Transportation Authority.
70. Manufacturing and equipment acquired as part of a technological upgrading of a manufacturing process in a distressed municipality or targeted investment community.
71. Any motor vehicle owned by a member of an indigenous Indian tribe or their spouse, and garaged on the reservation of the tribe (PA 89-368)
72. New machinery and equipment, applicable only in the five full assessment years following acquisition.
73. Temporary devices or structures for seasonal production, storage, or protection of plants or plant material.
74. Certain vehicles used to transport freight for hire.
75. Certain health care institutions.
76. New machinery and equipment for biotechnology, after assessment year 2011.
77. Real Property of any Regional Council or Agency

Endnotes

1. Office of Policy and Management (OPM), Municipal Fiscal Indicators, 2010-2014.
3. OPM, Municipal Fiscal Indicators, 2010-2014.
5. CCM Estimate.
6. CGS § 12-81.
7. CCM estimate based on OPM data for 2014 grand lists.
9. CCM estimate based on OPM data for the 2013 grand list year.
10. Ibid.
11. Ibid.
13. Ibid.
15. CCM estimate based on State Department of Education (SDE) data.
16. SDE, 2015 data.
CCM is the state’s largest, nonpartisan organization of municipal leaders, representing towns and cities of all sizes from all corners of the state, with 162 member municipalities.

We come together for one common mission - to improve everyday life for every resident of Connecticut. We share best practices and objective research to help our local leaders govern wisely. We advocate at the state level for issues affecting local taxpayers. And we pool our buying power to negotiate more cost effective services for our communities.

CCM is governed by a board of directors that is elected by the member municipalities. Our board represents municipalities of all sizes, leaders of different political parties, and towns/cities across the state. Our board members also serve on a variety of committees that participate in the development of CCM policy and programs.

Federal representation is provided by CCM in conjunction with the National League of Cities. CCM was founded in 1966.