



# Education Brief

## Taxpayer Relief Act

Act 1 of 2006 (Special Session No. 1)

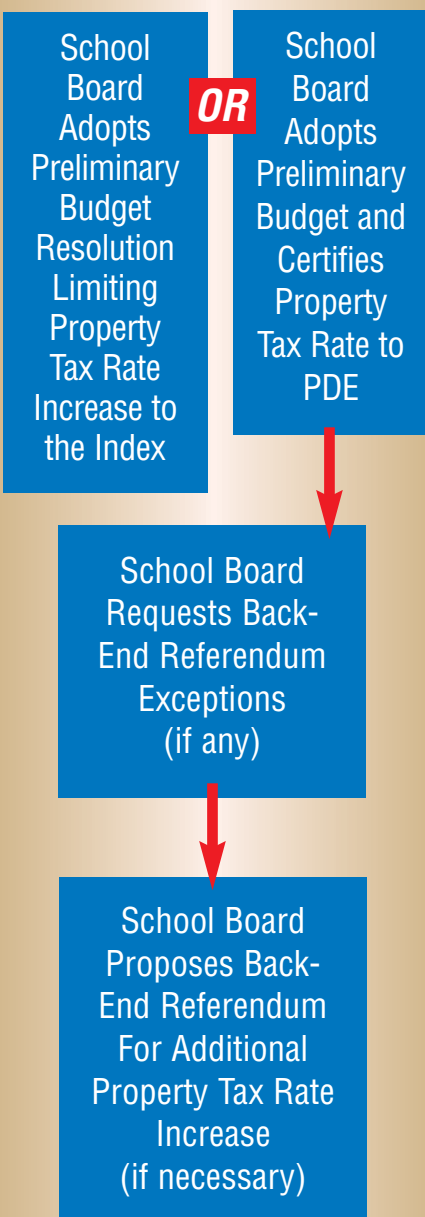
Senator James J. Rhoades

### OVERVIEW

The Taxpayer Relief Act, Act 1 of 2006 (Special Session No. 1), limits school district property tax rate increases to an annually-calculated inflationary percentage, unless school district voters approve an additional increase through a back-end referendum. Act 1 also allows school district residents to reduce property taxes by authorizing additional income taxes.

This Brief will summarize timelines and decision-making chronologies that Act 1 establishes to ensure that tax increase limitations are enforced and to define local tax options available to school district residents.

### Budget, Tax Rate and Back-End Referendum Process



### Timelines for Budget Adoption and Referendum Questions

In order to establish a clear timeline for a school district to make budget and tax decisions, Act 1 sets forth a series of deadlines for the adoption of its budget and property tax rates.

This is a key component of the new law, because it ensures that a school district makes decisions about its property tax rates in time to publish a back-end referendum question requesting a tax increase above the index, if such an increase is required.

Under Act 1, a school district is now required to provide the Department of Education (PDE) with its proposed property tax rates, so that it can be certified as within the Act 1 limitations.

### Act 1 2007 Deadlines

Action	Deadline
School District Submits Preliminary Budget Resolution (if adopted)	January 30
PDE Certifies School District Tax Rate in Resolution	February 9
School District Adopts Preliminary Budget	February 14
School District Submits Preliminary Budget to PDE	February 19
PDE Certifies School District Tax Rate	March 1
School District Requests Exceptions (if any)	March 1
School District Approves Local Income Tax Question	March 13
PDE Rules on Exceptions	March 21
School District Submits Back-end Referendum Question (if applicable)	March 26
Primary Election	May 15

## Preliminary Budget Resolutions

To date, 192 school districts have adopted resolutions indicating that they will not increase property tax rates in excess of the index for FY 2007-2008, which ranges from 3.4% to 5.4%, depending on a school district's economic profile.

A school district that adopts such a resolution

certifies that it will not seek a tax increase that exceeds the index and is ineligible to request back-end referendum exceptions.

A school district that does not adopt a resolution limiting its tax increase to the index must take action on a preliminary budget no later than February 14.

## The Index

The index is an annually-calculated percentage that reflects the percentage increase in property tax rates that a school district may adopt without approval of exceptions or a back-end referendum question.

The index is determined annually for each school district by averaging the percentage increase in the Statewide Average Weekly Wage (SAWW) and Federal employment cost index for elementary and secondary education (ECI) and adjusting it for school districts with MV/PI aid ratios greater than 0.4000.

For FY 2007-2008, the base index is 3.4%. For individual school districts that receive the aid ratio adjustment, the highest index is 5.4%. The base index for FY 2006-2007 was 3.9% and the highest adjusted index was 6.3%.

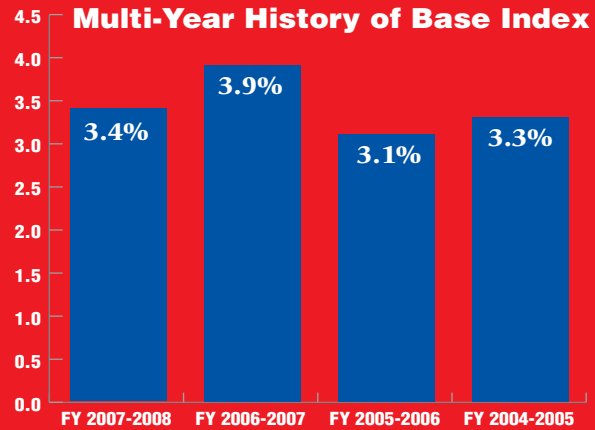
A school district may increase its property tax rate above the index only if it is granted one or more exceptions or if voters approve an additional tax increase through back-end referendum.

### Act 1 Index Controls

FORMULA ELEMENT	FY 2007-2008
Percentage Change in SAWW	2.8%
Percentage Change in ECI	4.0%
Base Index	3.4%
Range of Adjusted Index	3.4% to 5.4%

Data Source: Department of Education

### Multi-Year History of Base Index



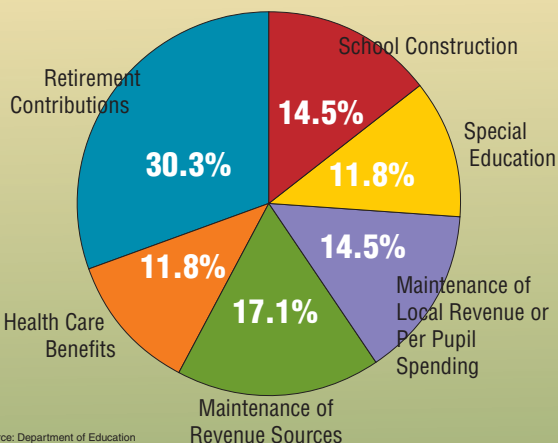
Data Source: Department of Education

## Exceptions to Back-End Referendum

Act 1 allows a school district to request a property tax rate increase greater than the index, without approval of a back-end referendum question, if the school district qualifies for any of ten exceptions.

These exceptions target revenue and spending scenarios that are largely beyond a school district's control and for which property tax rate increases are essential for a school district to balance its budget.

### Exceptions Approved in 2006 Under Act 72



Data Source: Department of Education

To request an exception, a school district must apply to PDE. PDE approves exceptions based on computations set forth in the law. If an exception request is approved, a school district may increase its property tax rate greater than the index, up to the percentage calculated by PDE.

The exceptions available under Act 1 are substantially similar to the exceptions available for the 118 school districts that elected to participate in Act 72 of 2004. In 2006, 76 requests for exceptions were approved.

## Back-End Referendum Questions

If a school district proposes to increase its property tax rate more than the index or the percentage allowed through the approval of any exceptions, school district residents must approve a back-end referendum question at the primary election.

If a back-end referendum question is not approved by the voters, the school district may only increase its property tax rate to the index or to the percentage allowed through the approval of any exceptions.

### Types of Back-End Referendum Exceptions

#### Department Approved Exceptions

- School Construction Projects
- Special Education Costs
- School Improvement Plans
- Maintenance of Local Tax Revenue
- Maintenance of Total Revenue
- Health Care Benefits
- Retirement Contributions

#### Local Court Approved Exceptions

- Emergency or Disaster
- Court or Administrative Order
- Immediate Threat of Serious Harm or Injury

### Local Tax Option Process

Tax Study Commission Recommends EIT or PIT and Rate

School Board Decides EIT or PIT and Rate For Referendum

Voters Approve or Disapprove Tax and Rate In Referendum

**IF APPROVED**

Property Tax Relief Provided Through Homestead Exclusion

## Local Income Tax Options and Referendum Questions

Act 1 requires that each school district appoint a local tax study commission to recommend the rate of the earned income (EIT) or personal income tax (PIT) that voters will be required to approve or disapprove in referendum questions proposed at the 2007 primary election.

The income taxes will fund property tax reductions in the school districts. School boards must make final decisions on their referendum questions by March 13.

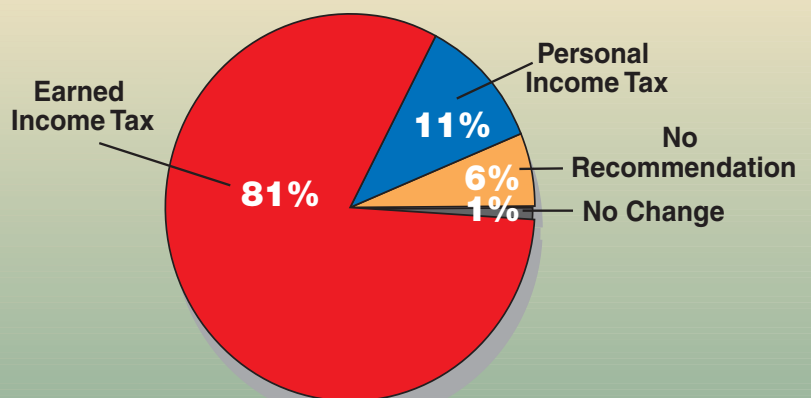
School boards have discretion to determine the tax and the income tax rate, so long as their action will provide proper-

ty tax reductions of 50% of the maximum homestead exclusion allowed by law.

According to the PDE, 309 school districts have so far provided their local tax study commission recommendations to PDE. Of those, 251, or 81%, have recommended the use of the EIT. Thirty-five, or 11%, have recommended the use of the PIT.

Nineteen commissions did not issue recommendations and four recommended no change in the school district's current income tax structure. These options are not authorized by Act 1.

### Local Tax Study Commission Recommendations



Data Source: Department of Education

## The Homestead Exclusion

Act 1 requires that a school district utilize the homestead exclusion to provide any property tax relief approved under the school district's local income tax referendum question.

Authorized through an amendment to the Pennsylvania Constitution, the homestead exclusion allows a school district to exclude from taxation an equal amount for all homestead property in a school district. The maximum homestead

exclusion is 50% of the median assessed value of qualifying residential property in the school district. A residential property owner must apply for a homestead exclusion in order to qualify.

Under Act 1, a referendum question proposing an EIT or PIT must provide residential property tax relief equal to at least 50% of a school district's maximum homestead exclusion.

### Calculating the Homestead Exclusion

#### **Step 1: Determine Median Assessed Value.**

The median assessed value of qualifying residential property in a school district is the assessed value of property in the exact middle when the assessed values of qualifying residential properties are arrayed from highest to lowest.

#### **Step 2: Calculate the Exclusion.**

The maximum homestead exclusion is equal to 50% of the median assessed value of qualifying residential property. The homestead exclusion is determined by the school district but can not exceed the maximum.

#### **Step 3: Deduct the Exclusion from Assessed Value.**

The homestead exclusion is subtracted from the assessed value of each homestead property in the school district. The homestead exclusion must be identical for all eligible residential property taxpayers.

#### **Step 4: Calculate the Tax Liability.**

The assessed value, with the homestead exclusion subtracted, is multiplied by the millage rate in the school district.