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Property Tax Restrictions on School Board Taxing Authority in Pennsylvania[1]

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Introduction

Historically, in Pennsylvania, the property tax has been the only significant local revenue source over which school boards have had authority, and their authority to raise property tax rates was unrestricted. This flexibility has proved helpful especially when the state has enacted unfunded mandates. However, in 2006, the state enacted legislation to limit school boards' property tax authority with no change to existing mandates or increase in state funding. The purpose of this study was to analyze local school boards' taxing authority, pre- and post-enactment of Special Session Act 1 in 2006,[2] in terms of its percent share of school districts' total budget in order to better understand the impact of the new limits, in general, and, specifically, with regard to state-mandated contributions to the state pension fund for school district employees.

Background

Pennsylvania relies heavily on local revenues to fund elementary and secondary public education. For the 2011-2012 school year,[3] the most recent year for which Pennsylvania Department of Education data were available, local funding sources represented 59.8% of total school district funding in comparison to a state share of 33.5% and a federal share of 4.4%.[4] In contrast, the latest national data available, which were for 2011, indicated the national average was 43.4% local, 44.1% state, and 12.5% federal. (U.S. Department of Education 2013). According to these data, Pennsylvania ranked 44th in state support; that is, only six states provided a lower percentage of state aid to school districts. In Pennsylvania, a significant component of state aid is funding for instruction, referred to as "basic education funding." Over the past 40 years, basic education funding, as a percentage of instructional expense reported by districts, has declined from 51% in 1971 to 31% in 2013 (Bissett and Hillman 2013).

Mandates

In Pennsylvania, the local funding burden falls primarily on the property tax, which represents 72% of total local revenue (Pennsylvania Department of Education n.d.a). This is particularly relevant for school district funding since the decline in state funding share has not been accompanied by a decrease in mandates from the state or federal levels. Pennsylvania state mandates encompass a wide range of areas, such as buildings and construction, charter schools, collective bargaining and other personnel issues, district operations, educational programs, services to students, and school health services. (See the Appendix for a more detailed description of these.)

Special Session Act 1 of 2006: "The Taxpayer Relief Act" [5]

Prior to 2006, Pennsylvania school boards had unlimited local property taxing authority; that is, they had the authority to raise the tax millage rate yearly as they deemed necessary to meet expenses. However, during the 2006-2007 school year, Act 1 was implemented, a law that has had a substantial impact on Pennsylvania school finance because it restricts property tax growth (and school boards' taxing authority) to an inflationary index that sets an annual maximum percent of property tax millage growth (Pennsylvania Department of Education n.d.b). Certain limited exceptions for greater expenditure growth, e.g., pensions, special education, and pre-established debt service, may be utilized by the school board to allow an increase beyond the index rate. However, the law requires that proposed property tax rate increases greater than the district index and permissible exceptions are subject to public referenda.

Permissible property tax rate limits are tied to the average of two wage indices, one federal and one state, to create a base index. The federal Employment Cost Index component uses the annual figure for the previous 12-month period beginning July 1 and ending June 30. It specifically tracks rates for elementary and secondary schools as reported the Bureau of Labor Statistics of the U.S. Department of Labor. The state component, the Pennsylvania State Average Weekly Wage, is determined by the Pennsylvania Department of Labor and Industry. Prior to 2011, it was calculated using data from the preceding calendar year. Now, it uses a 36-month moving average.

These two indices are combined in equal weights to establish the base index. The base index is modified upward for poorer districts using a state district wealth measure to calculate an adjusted index for each qualified district. The adjusted index provides poorer districts with additional taxing capacity. As shown in Figure 1, upon implementation for Fiscal Year (FY)2007, the initial base index was 3.9%, and the maximum district-adjusted index was 6.3%. However, post-recession, the base index dropped dramatically to a low of 1.4% in FY2012 due to the slow economic recovery. The maximum district-adjusted index also fell to a low of 1.8% that fiscal year (Pennsylvania Department of Education n.d.b).

School board authority to increase property taxes remains limited by this law. As indicated in Table 1, in the three years prior to the law, the statewide average increases in property tax collections, inclusive of assessment growth, ranged from 6.1% to 7.3%, while in the years after Act 1 implementation, the average increases fell dramatically, and it was 2.9% for 2012.[6]

Methodology

All school districts except Philadelphia were included in the analyses (n = 499). Philadelphia was excluded because it is fiscally dependent on the city for its local tax revenues. The study used actual FY2012 data and a mix of actual and projected data for FY2013 through FY2015. For these three years, actual data were comprised of Act 1 indices and pension rates while projections were used for total budget and salary growth by district.

Figure 1 | **Base and Maximum District-Adjusted Indices: 2007-2015**

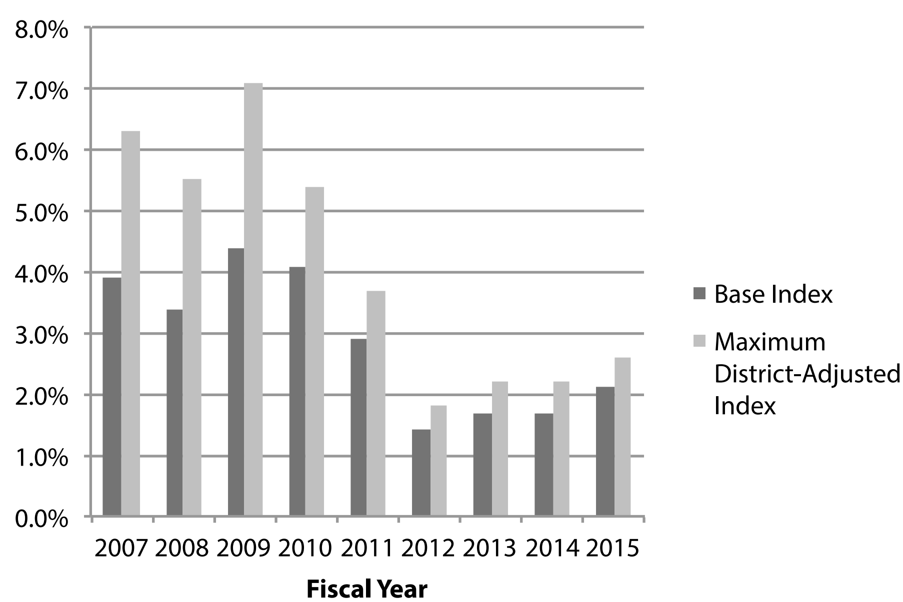

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Table 1 | **Property Tax Collections: 2003-2015**

Year	Current and Interim Real Estate Taxes Collected ($)	Percent Change
2003	7,762,009,750	
2004	8,304,228,974	7.0%
2005	8,909,888,069	7.3%
2006	9,450,862,131	6.1%
2007	10,010,719,092	5.9%
2008	10,474,050,306	4.6%
2009	10,438,463,356	-0.3%
2010	10,759,581,531	3.1%
2011	11,153,412,490	3.7%
2012	11,480,468,871	2.9%
2013*	11.537,871,216	0.5%
2014*	11,768,628,640	2.0%
2015*	12,004,001,213	2.0%
Source: Pennsylvania Department of Education.		
* Estimates based on maximum Act 1 increases for each school district. The estimated amounts may overstate the actual real estate tax revenues since not all districts levy the maximum increases.		

The steps to determine school board taxing authority and to compare this authority with pension contributions were, as follows:

1. Property tax as a percent of total expenditures was determined for each district. Descriptive statistics–minimum, maximum, average, and median values–were calculated.
2. Next, each district's adjusted index was calculated for 2012-2015. This represented the maximum permissible tax rate increase for each district by year and allowed a comparison over time.
3. Each district's property tax share was multiplied by the district's adjusted index to determine board tax authority as a percent of the total budget for each year. Descriptive statistics were also calculated.
4. To determine the impact of pension contributions, contributions were calculated using 2012 payroll data with a 1% annual growth for each succeeding year, multiplied by the projected Employer Cost Rate for each year.[7]
5. Each district's taxing authority was then compared to the budget share required by their mandated pension contribution.

Findings

In 2012, property tax revenues represented 41.65% of the average school district's total budget, with an extremely wide range, from 7.25% for a very property-poor district to 90.01% for a very property-wealthy district. (See Table 2.) The median value of 39.5% was close to the mean indicating a normal distribution. Over the four years in the study, these values varied little. As a reference point, at a 42% average property tax share, a district would require an adjusted index of 2.4% to provide board tax authority equivalent to 1% of the total budget. Any district with a lower property tax share of the total budget or an adjusted index lower than 2.4% would not have sufficient taxing authority to cover a 1% cost budget increase.

Table 2 | **Property Taxes as a Percentage of School District Expenditures: 2012-2015**

Year	2012	2013	2024	2015
Minimum (%)	7.25%	7.40%	7.44%	7.53%
Maximum (%)	90.01%	91.08%	90.81%	90.90%
Average (%)	41.65%	42.32%	42.36%	42.60%
Median (%)	39.81%	40.51%	40.59%	40.83%

An overview of the taxing authority available to school districts is presented in Tables 3.1 through 3.3. Between 2012 and 2015, the average percentage increase in school district taxing authority, using the base index, ranged from 0.72% to 1.09%. (See Table 3.1.) Pension contributions as a percent of school district expenditures increased over this time period, from an average of 0.64% in 2012 to 1.01% in 2015. (See Table 3.2.) School board taxing authority remaining after pension contributions varied by year, ranging from an average of -0.17% in 2014 to 0.08% in both 2012 and 2015. (See Table 3.3.) Median values were similar across all four years denoting a normal distribution.

With a base index of 1.4% for 2012, the average school district taxing authority was 0.72% of the budget. As the base index increased to 1.7% for 2013 and remained at the same level for 2014, the average district taxing authority increased to 0.89%. In 2015, with a base index of 2.1%, the average district taxing authority increased to 1.09%.

Figure 2 shows the distribution of school districts with varying levels of board tax authority for each year of the study. The number of district's with the lowest tax authority (<0.50% of their budget) declined substantially from 127 in 2012 to 32 in 2015. Except for 2012, the bulk of school districts were found to have taxing authority between 0.50% and 1.49% of their budget. With the exception of 2015, only a handful of districts had taxing authority at the high end of 1.50% to 1.99%. No district had a tax authority of 2.00% or more of their budget.[8]

Figure 3 presents the distribution of the remaining board tax authority after meeting the pension funding requirements. Note that in this chart the first group of districts consists of those that have have less than zero percent taxing authority; that is, even after raising the maximum property tax increase allowed under Act 1, they have insufficient funds to pay their pension obligations. The number of districts in this condition ranges from 190 in 2012 to 327 in 2014, and then decreased to 210 in 2015, representing 42% of all school districts.

Looking at the more detailed data for 2014 in Table 3.3, one sees that the average school district taxing authority after pension contributions was -0.17%. This deficit was caused by two primary factors. Using the original index calculation methodology with the prior year value of the state average weekly wage, the 2014 base index would have been 2.1%. However, the calculation procedure was altered by the legislature to use a three year average beginning that year, which had the effect of lowering the base index to 1.7%, the same as the previous year. This change reduced the taxing authority of school boards by approximately 0.20%. At the same time, pension contributions increased, on average, from 0.85% of school district expenditures to 1.06%. As a result, 327 districts (65.6%) had less than zero percent taxing authority after making their mandated pension contribution.

Even for those school districts with a positive balance after pension contributions, there are concerns about whether they have sufficient resources to fund other required and necessary expenditures. For example, in 2015, 495 districts are projected to have less than 0.80% of their taxing authority remaining after using the base index. (See Figure 3.) However, most districts are projected to have even less taxing authority remaining–76% with less than 0.40%, 56% with less than 0.20%, and 42% with a negative percent. The remaining taxing authority would be even less if a district chose levy less than the base index allows.

There is a concern that the conditions described above has led to decreased school district expenditures in other areas of their budgets. For example, in 2012, total school district expenditures decreased 1.3% from the previous year. (See Table 4.) Most major expenditure objects showed decreases ranging from 3.72% for "other" objects to 20.11% for supplies. Salary expenditures decreased 4.1%. According to a 2012 survey by the Pennsylvania Association of School Business Officials and the Pennsylvania Association of School Administrators, school districts eliminated or left vacant nearly 20,000 positions in response to budget shortfalls. Professional and property services expenditures decreased 8.04% and 9.28%, respectively, while property-related expenditures fell 19.31%. On the other hand, benefit expenditures increased 6.39%, of which increases in pension contributions likely played a significant role. Other purchased services expenditures increased 4.92%, largely due to transfers of funds to charter schools (Pennsylvania Department of Education n.d.a).

Table 3.1 | **School Board Taxing Authority Increase Using Base Index: 2012-2015**

Year	2012	2013	2024	2015
Minimum	0.15%	0.18%	0.19%	0.23%
Maximum	1.28%	1.63%	1.60%	1.97%
Average	0.72%	0.89%	0.89%	1.09%
Median	0.72%	0.90%	0.89%	1.10%
Base Index	1.4%	1.7%	1.7%	2.1%

Table 3.2 | **Pension Contributions as a Percent of School District Expenditures: 2012-2015**

Year	2012	2013	2024	2015
Minimum	0.01%	0.05%	0.06%	0.06%
Maximum	0.92%	1.12%	1.39%	1.33%
Average	0.64%	0.85%	1.06%	1.01%
Median	0.65%	0.87%	1.08%	1.04%

Table 3.3 | **School Board Taxing Authority Remaining after Pension Contributions: 2012-2015**

Year	2012	2013	2024	2015
Average	0.08%	0.04%	-0.17%	0.08%
Median	0.07%	0.03%	-0.19%	0.06%

Conclusions

The purpose of this article was to present the results of a study that analyzed Pennsylvania local school boards' taxing authority, pre- and post-enactment of Special Session Act 1, "The Taxpayer Relief Act," in 2006, in terms of its percent share of school districts' total budget in order to better understand the impact of the new limits, in general, and, specifically, with regard to state-mandated contributions to the state pension fund for school district employees. Prior to this act, school districts' authority was unrestricted. Act 1 changed all of this, requiring districts to seek local voter approval and/or an exception from the state department of education to exceed state-imposed limits. At the same time, the state imposed significant increases in local school district employee pension contributions. A third complicating factor was the economic recession of 2007-2009 that greatly affected state and local revenues, followed by a weak economic recovery.

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Figure 2 | **Taxing Authority of Pennsylvania School Districts by Percent of Budget: 2012-2015**

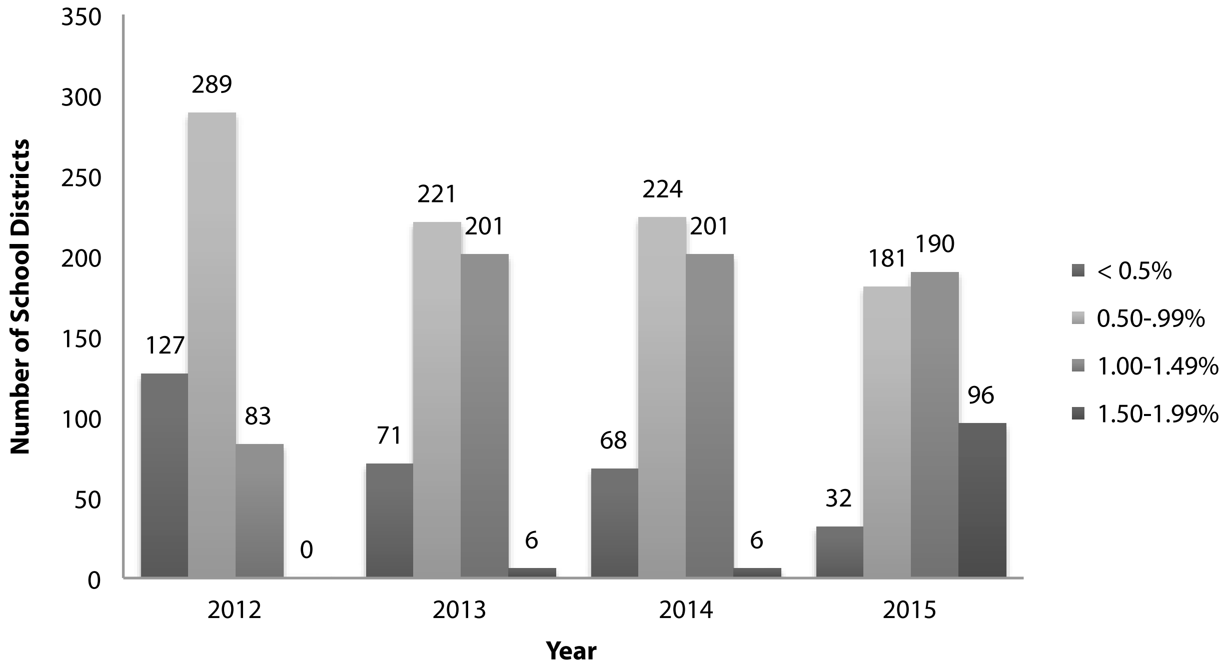

Figure 3 | **Remaining Taxing Authority of School Districts by Percent of Budget at Maximum Allowable Property Tax Less Pension Contributions: 2012-2015**

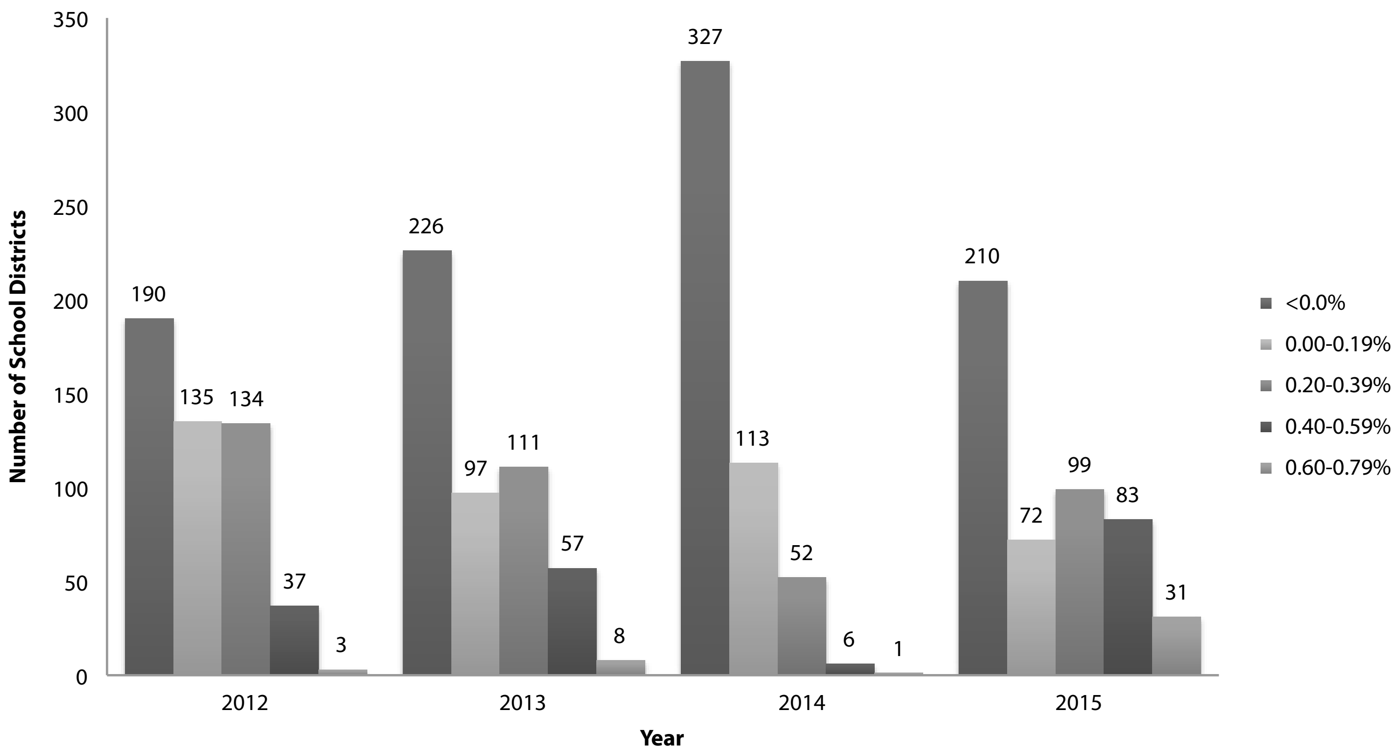

Table 4 | Change in School District Expenditures between 2011 and 2012

Major Expenditure Object	Percent Change (%)
Salaries	-4.19%
Benefits	6.39%
Professional Services	-8.04%
Property Services	-9.28%
Other Purchased Services	4.92%
Supplies	-20.11%
Property	-19.31%
Other Objects	-3.72%
Other Uses of Funds	8.85%
Total	-1.34%

Local property tax increases began to fall immediately after implementation of this law, and in its earlier years the economic recession likely accounted for a portion of the decreases. However, even after the recession had ended, increases continued to fall such that over the course of the year studied, 2012-2015, they bottomed out at 0.5% in 2013. For 2013 and 2014, property tax increases were estimated at 2.0%. However, this is much lower than pre-Act 1 when annual increases were 7.0% and 7.3% in 2004 and 2005, respectively.

Increases in state-mandated pension contributions also strained school district budgets over the course of the years studied in this analysis. Pension contributions as a percent of a school district's budget rose, on average, from 0.64% to 1.09%. The combination of constrained increases in property tax revenues and increases in pension contributions left many school districts with little or no remaining taxing authority to meet budgeted expenditures. In fact, in 2014, two-thirds of school districts had no remaining taxing authority after payment of their pension obligations.

Undoubtedly, the adequacy and stability of the state pension fund, a shared responsibility with local school districts in Pennsylvania, is of critical importance to employees and retirees. However, when coupled with property tax limits and an economic recession, the fiscal burden for many Pennsylvania school districts is overwhelming and threatens their ability to provide required and necessary education services to their students.

Appendix | Examples of State Mandates by Area

Buildings and Construction	Prevailing wage, construction requirements, bid limits, and pest control planning.
Charter Schools	Payments, transportation, special education, extracurricular activities, and transfer of student records.
Collective Bargaining	Seniority requirements for personnel suspensions, salary schedules, minimum salaries and increments, payment of salaries during incapacitation, salary increases, employment protections when programs or classes are transferred to another school entity, workloads, part-time teacher salaries, demotions, substitute teachers, leave for elective public office, and compensation for additional hours of instruction.
District Operations	State report card reporting requirements, school safety reporting requirements, liability insurance, special education due process requirements, due process for disciplinary issues, right-to-know/release of public records, workplace safety committee, and school bus idling.
Educational Programs	Strategic planning, curriculum requirements, LEP program requirements, graduation requirements, assessment requirements, special education/early intervention/extended school year, gifted education, and education of incarcerated students.
Other Personnel Issues	Retirement contributions, sabbaticals, tenure, meeting "highly qualified teacher" requirements, professional development costs for teachers and administrators, and mandated benefits including sick days.
School Health Services Issues	School nurse certification, school nurse to student ratio, and medical and dental examinations.
Student Services	Guidance counseling, psychological services, home and school visitor services, social work services, and student assistance programs.
Transportation Issues	Nonpublic school student transportation, charter school transportation, and out-of-state transportation of students.

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Endnotes

[1] Portions of this study were previously published by Timothy J. Shrom in "Fiscal Outlook for PA Schools," *PASBO* [Pennsylvania Association of School Business Officials] *Report* 33(8):1,12, http://files.pasbo.org/PR/PRFebruary2013.pdf; and by Timothy J. Shrom and William T. Hartman, in "A Commonwealth Conundrum for School Board Authority: Restricted tax Authority AND [caps in original] Mandated Cost Increases," *PASBO Report* 33(10): 6-7, http://files.pasbo.org/PR/PRApril2013.pdf.

[2] Special Session Act 1 of 2006 is referred to as "Act 1" hereafter. Act 1 is also referred to as "The Taxpayer Relief Act."

[3] Hereafter, data years school districts are referred to by the end of their academic year; e.g., school year 2011-2012 will be referred to as 2012.

[4] The Pennsylvania Department of Education referred to 2.3% as "other."

[5] Pennsylvania Department of Education. n.d.b, "The Taxpayer Relief Act: Special Session Act of 2006," http://www.portal.state.pa.us/portal/server.pt/community/property_tax_relief/7452.

[6] The apparent reduction of property tax collections in 2009 was an anomaly caused by a tax reduction initiative that was funded that year whereby state funds replaced a portion of property taxes through a homestead reduction to qualifying properties.

[7] The Employer Contribution Rate (as a percent of payroll) is certified by the state Public School Employees Retirement (PSERS) board. Actual rates were used 2012-2014. For 2015, the projected PSERS board rate was used. The state and school districts share responsibility for school district employee pension contributions. Hence, the result was divided by two to represent the school district share.

[8] For the purposes of this study, the measure of board tax authority did not include exception utilization nor did it anticipate successful local tax referenda campaigns. Since neither referenda results nor exception approvals are fully within board taxing authority, i.e., they require approval from either the state department of education or the voters in the district, this study was limited to each district's adjusted index.

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