

# School District Property Tax Forecast



The Independent Fiscal Office (IFO) has issued periodic school district property tax forecasts in response to legislative requests and public interest. This report provides an updated forecast to facilitate discussion of proposals that contemplate changes to school property taxes. The most recent school property tax data published by the Pennsylvania Department of Education (PDE, or department) is for fiscal year (FY) 2018-19. For that year, current-year collections were \$13.9 billion, Act 1 allocations were \$533 million and delinquent collections were \$551 million, resulting in a total of \$15.0 billion for school district revenues related to the property tax.<sup>1</sup> The department plans to release actual collections for FY 2019-20 in late Spring 2020. This report provides estimates for that year and FY 2020-21 based on an IFO analysis of millage rate and property tax assessment data. Projections for FY 2021-22 through FY 2025-26 are made based on the statutory, economic and structural factors that affect growth rates of school property taxes.

## Forecast Overview

**Table 1** provides the IFO’s estimate of school district property taxes for FY 2019-20 and FY 2020-21, as well as projections for FY 2021-22 to FY 2025-26. The estimated total property tax collections for FY 2019-20 and FY 2020-21 are \$15.4 billion and \$15.1 billion, respectively. The estimate for FY 2019-20 current-year collections is based on individual school district tax rates published by PDE and an assumed tax base growth of 1 percent. Tax base growth is informed by taxable assessed values published by the State Tax Equalization Board (STEB). Data on Act 1 allocations are released by PDE each fiscal year, and the amounts for FY 2019-20 and FY 2020-21 are actual amounts. The estimate for delinquent collections in FY 2019-20 is based on recent trends.

**Table 1: School District Property Tax Forecast**

|                                | Actual        | Estimate      |               | Forecast      |               |               |               |               |
|--------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
|                                | 2018-19       | 2019-20       | 2020-21       | 2021-22       | 2022-23       | 2023-24       | 2024-25       | 2025-26       |
| Current-Year                   | \$13,930      | \$14,301      | \$14,109      | \$14,595      | \$15,155      | \$15,795      | \$16,405      | \$16,985      |
| Act 1 Allocations <sup>1</sup> | 533           | 534           | 535           | 535           | 535           | 535           | 535           | 535           |
| Delinquent <sup>2</sup>        | <u>551</u>    | <u>565</u>    | <u>488</u>    | <u>616</u>    | <u>618</u>    | <u>622</u>    | <u>645</u>    | <u>668</u>    |
| <b>Total</b>                   | <b>15,014</b> | <b>15,400</b> | <b>15,131</b> | <b>15,746</b> | <b>16,308</b> | <b>16,952</b> | <b>17,585</b> | <b>18,188</b> |

Note: Dollar amounts in millions.

1 Actuals through FY 2020-21. Estimated at \$535 million thereafter.

2 Reported by PDE for FY 2018-19. Estimated by IFO thereafter.

The estimated decline in current-year collections in FY 2020-21 is the result of flat millage rates combined with a projected tax base reduction of 1.5 percent due to economic distress related to the COVID-19 pandemic. A July 2020 IFO report projected that current-year school district property taxes could be reduced by 1.9 percent statewide due to various factors related to the pandemic.<sup>2</sup> This analysis reflects a more moderate decline. Delinquent collections from prior years are also projected to decline in FY 2020-21, by approximately \$70 million, or 12 percent of prior year collections. For that \$70 million loss, the

<sup>1</sup> Current-year collections, also referred to as “current and interim collections,” are receipts from non-delinquent property taxes levied for the current fiscal year. Act 1 allocations are distributions of slots revenue from the Property Tax Relief Fund to reduce property taxes collected from homestead properties. Delinquent collections are receipts from property taxes levied in a prior fiscal year.

<sup>2</sup> Factors that can impact growth rates are (1) the share of payments made in the discount, base and penalty periods, (2) late/delinquent payments from prior years and (3) changes in total assessed value from normal economic growth and/or appeals. See <http://www.ifo.state.pa.us/download.cfm?file=Resources/Documents/RB-2020-COVID-19%20Local%20Revenue%20Impact.pdf>.

analysis assumes that \$40 million is shifted to FY 2021-22, \$20 million is shifted to FY 2022-23 and \$10 million is not recouped.

During the forecast period, current-year collections are based on projected revenue growth from (1) typical tax base expansion (also referred to as economic growth) and (2) millage rate increases as limited under Act 1.<sup>3</sup> Act 1 allocations, which have been stable since their inception, are held constant at \$535 million per annum. Delinquent tax collections in FY 2021-22 and FY 2022-23 include monies shifted from FY 2020-21, while the remaining years are based on historical trends. Overall collections are projected to increase by roughly 3.7 percent per annum during the forecast period, reaching \$18.2 billion in FY 2025-26.

## Act 1 Index

Act 1 of 2006, which took effect in FY 2007-08, limits the increase to a school district’s millage rate based on an index, with certain exceptions. This analysis employs the index to estimate the additional revenues school districts could raise through millage increases and then applies a utilization factor, ranging from 65 percent to 75 percent, to reflect index usage. In general, most school districts do not increase millage rates to the full extent permitted by the index. The maximum percentage increase in the school district millage rate is equal to the base index or an adjusted index, depending upon the district’s aid ratio.<sup>4</sup> The base index is calculated by averaging the percentage increase in the Pennsylvania statewide average weekly wage (SAWW) and the employment cost index (ECI) for elementary/secondary schools.<sup>5</sup> School districts with an aid ratio less than 0.4000 utilize the base index. All other districts utilize an adjusted index that is computed by multiplying the base index by the sum of 0.75 and the district’s aid ratio.

**Table 2** provides detail on the projections for current-year collections during the forecast period, including the amounts attributable to economic growth, the Act 1 index and Act 1 exceptions. For this forecast, a statewide weighted average Act 1 index is calculated using the index applicable to each school district (base or adjusted) and weighting it by FY 2018-19 property tax collections. The weighted average index serves as a statewide maximum percentage increase in property tax collections due to higher millage rates.

|  | 2021-22       | 2022-23       | 2023-24       | 2024-25       | 2025-26       |
|--|---------------|---------------|---------------|---------------|---------------|
| Prior Year Base (includes Act 1 Allocations)   | \$14,640      | \$15,130      | \$15,690      | \$16,330      | \$16,940      |
| Revenue Growth - Current-Year                  |               |               |               |               |               |
| Economic Growth (from changes in AV)           | 146           | 151           | 157           | 163           | 169           |
| Act 1 Index and Exceptions                     | 329           | 396           | 466           | 434           | 396           |
| Act 1 Exceptions                               | <u>15</u>     | <u>15</u>     | <u>15</u>     | <u>15</u>     | <u>15</u>     |
| Subtotal - Current-Year Revenue Growth         | 490           | 562           | 638           | 611           | 580           |
| Current-Year Collections and Act 1 Allocations | 15,130        | 15,690        | 16,330        | 16,940        | 17,520        |
| Less: Act 1 Allocations                        | <u>-535</u>   | <u>-535</u>   | <u>-535</u>   | <u>-535</u>   | <u>-535</u>   |
| <b>Current-Year Property Tax Collections</b>   | <b>14,595</b> | <b>15,155</b> | <b>15,795</b> | <b>16,405</b> | <b>16,985</b> |

Note: AV is assessed value.

<sup>3</sup> Act of June 27, 2006, Special Session 1, P.L. 1873, No. 1, known as the “Taxpayer Relief Act.”

<sup>4</sup> The aid ratio is the market value/personal income aid ratio (MV/PI AR) calculated in accordance with section 2501(14) and (14.1) of the Public School Code of 1949. It is used in the calculation of various state subsidies for school districts, including the basic education subsidy. The minimum MV/PI AR is 0.1500. For FY 2020-21, 413 districts had an MV/PI AR of 0.4000 or above, with the maximum being 0.8909. Those 413 school districts represented approximately 60 percent of the current-year taxes collected in FY 2018-19.

<sup>5</sup> The SAWW is reported by the Pennsylvania Department of Labor and Industry. The ECI is reported by the U.S. Bureau of Labor Statistics.

**Table 3** displays historical detail and the forecast of the Act 1 index (base and weighted average) and its components (SAWW and ECI). The base index and its two components through FY 2021-22 are based on data published by PDE and are forecast by the IFO for subsequent years. The weighted average index is calculated by the IFO for all years. During the forecast period, the base index decreases from 3.5 percent in FY 2022-23 to 2.7 percent in FY 2025-26, and the weighted index decreases from 4.0 percent to 3.1 percent. This outcome is largely driven by a decline in the SAWW during the forecast period. The SAWW, which is projected by the Pennsylvania Department of Labor and Industry, decreases from 4.3 percent to 2.3 percent. The annual SAWW increase is calculated using the growth rate between two overlapping three-year

**Table 3: Act 1 History and Forecast**

| Fiscal Year | SAWW <sup>1</sup> | ECI <sup>2</sup> | Base Index <sup>3</sup> | Weighted Index <sup>4</sup> |
|-------------|-------------------|------------------|-------------------------|-----------------------------|
| 2017-18     | 2.6               | 2.3              | 2.5                     | 2.9                         |
| 2018-19     | 2.2               | 2.6              | 2.4                     | 2.7                         |
| 2019-20     | 2.2               | 2.4              | 2.3                     | 2.6                         |
| 2020-21     | 2.2               | 2.9              | 2.6                     | 3.0                         |
| 2021-22     | 3.1               | 2.9              | 3.0                     | 3.4                         |
| 2022-23     | 4.3               | 2.7              | 3.5                     | 4.0                         |
| 2023-24     | 4.5               | 2.9              | 3.7                     | 4.2                         |
| 2024-25     | 3.6               | 3.0              | 3.3                     | 3.8                         |
| 2025-26     | 2.3               | 3.0              | 2.7                     | 3.1                         |

1 Statewide Average Weekly Wage.

2 Employment Cost Index.

3 Average of the SAWW and ECI.

4 Average of the index for each school district weighted by property tax collections.

(calendar) periods. For example, the increase for FY 2021-22 is equal to the growth in the SAWW between January 2016 – December 2018 and January 2017 – December 2019. The significant increase in the SAWW for FY 2022-23 is largely driven by job losses for low-wage workers in CY 2020 due to the COVID-19 pandemic and related mitigation efforts. That trend reverses itself by the end of the forecast period as those low-wage workers are rehired. For the ECI, there are no available projections for education-specific employment costs for Pennsylvania, so the U.S. ECI for all private workers from IHS Markit is used, with adjustments by the IFO. This component of the index remains relatively flat, increasing from 2.7 in FY 2022-23 to 3.0 in FY 2025-26.

**Table 4 (next page)** provides detail of how the Act 1 index contributes to projections of current-year collections during the forecast period. The utilization rate of 75 percent reflects historical trends in actual school district millage rates and Act 1 indexes. The rate is reduced for FY 2021-22 through FY 2024-25 to account for (1) school districts’ potential sensitivity to millage rate increases after the COVID-19 pandemic and (2) the artificial growth in the SAWW related to the COVID-19 job losses. Not included in the table are utilized Act 1 exceptions, which are projected to add \$15 million to the forecast each year. A school district can utilize Act 1 exceptions in order to increase its millage rate beyond its Act 1 index.<sup>6</sup> The statute currently authorizes four exceptions: pension obligations, special education expenditures, grandfathered debt service and electoral debt service.<sup>7</sup> The forecast projects that school districts will qualify for exceptions valued between \$48 million and \$50 million annually, but school districts are not required to utilize approved exceptions. For example, exceptions valued at \$52.9 million were approved for FY 2019-20, but \$18.6 million (35.0 percent) in exceptions was actually used by school districts to exceed their index.<sup>8</sup> The forecast

<sup>6</sup> The statute also permits a school district to exceed the index by seeking voter approval in a referendum. The forecast does not include any millage increases approved by referendum.

<sup>7</sup> Generally, a school district may establish eligibility for an exception if its costs for an eligible expenditure increase by more than its index.

<sup>8</sup> Report on Referendum Exceptions, Pennsylvania Department of Education, April 2020. See <https://www.education.pa.gov/Documents/Teachers-Administrators/Property%20Tax%20Relief/ReferendumExceptions/2020-21%20Report%20on%20Referendum%20Exceptions.pdf>.

assumes that school districts will utilize approximately 30 percent of approved exceptions each year, equaling \$15 million.

**Table 4: Act 1 Index Detail**

|                                 | 2021-22  | 2022-23  | 2023-24  | 2024-25  | 2025-26  |
|---------------------------------|----------|----------|----------|----------|----------|
| Baseline (PY + Economic Growth) | \$14,790 | \$15,280 | \$15,850 | \$16,490 | \$17,110 |
| Weighted Average Index          | 3.4%     | 4.0%     | 4.2%     | 3.8%     | 3.1%     |
| Potential Growth from Index     | \$506    | \$608    | \$666    | \$619    | \$527    |
| Index Utilization Rate          | 65%      | 65%      | 70%      | 70%      | 75%      |
| Forecast Growth from Index      | \$329    | \$396    | \$466    | \$434    | \$396    |

Note: Dollar amounts in millions.

### Homestead/Owner-Occupied Estimates

A recent amendment to the Pennsylvania Constitution revised the homestead exclusion by removing the limitation that the exclusion shall not exceed one-half of the median assessed value of all homestead property in a local taxing jurisdiction. The revised language permits the exclusion to be up to 100 percent of the assessed value of each homestead property within a jurisdiction.<sup>9</sup>

Generally, property that is used as the primary residence of its owner(s) qualifies as homestead property.<sup>10</sup> To receive the exclusion, the property owner(s) must file an application with the county assessment office, which maintains the records for eligible properties. School districts currently use the homestead exclusion to distribute property tax relief allocated from slots proceeds (Act 1 allocations). A few school districts also increased their earned income taxes under Act 1 to provide for additional homestead exclusions.

**Table 5 (next page)** provides estimates of FY 2019-20 through FY 2025-26 school property tax collections associated with homestead properties (top half of table). The estimates are consistent with the school property tax forecast in Table 1 and are based on properties for which an application has been submitted and approved. Therefore, they exclude properties that meet the qualifications for homestead property, but for which an application has not been submitted. If school property taxes were eliminated through the homestead exclusion, it is likely that qualified properties that have not applied would then apply for a homestead exclusion. In order to estimate the funds needed to implement a full statewide school property tax elimination, the estimated amount of school district property taxes remitted by all owner-occupied properties must be utilized. The bottom half of Table 5 provides estimates for those properties.

In general, the homestead estimates in Table 5 utilize results from a survey of county assessment offices coordinated by the County Commissioners Association on behalf of the IFO.<sup>11</sup> The estimates for Philadelphia are based on data from the Philadelphia Department of Revenue regarding locally-funded tax relief programs for homestead properties. These programs include the homestead exemption, the Longtime Owner Occupants Program (LOOP) and the ten-year abatements for residential units that have been rehabilitated or newly constructed. Based on the survey and data provided, the IFO estimates that

<sup>9</sup> The text of Article VIII, Section 2(b)(vi) of the Pennsylvania Constitution provides that the General Assembly may “[a]uthorize local taxing authorities to exclude from taxation an amount based on the assessed value of homestead property. The exclusions authorized by this clause shall not exceed 100% of the assessed value of each homestead property within a local taxing jurisdiction. A local taxing authority may not increase the millage rate of its tax on real property to pay for these exclusions.”

<sup>10</sup> The statutory definition of “homestead” can be found at 53 Pa.C.S. §8401.

<sup>11</sup> Additional details regarding the survey are available in the December 6, 2017 letter to the County Commissioners Association of Pennsylvania. See <http://www.ifo.state.pa.us/Resources/Documents/SR2017-06.pdf>.

approximately 54 percent of current-year school property tax collections are from homestead properties.<sup>12</sup> The same percentage is applied to delinquent tax collections. The Act 1 allocations are used to offset property taxes for homestead properties, and the homestead estimates include 100 percent of such allocations. Table 5 does not include Philadelphia’s locally funded property tax relief for owner-occupied residential properties. The IFO estimates that 40 percent of taxable property in the city is homestead property, but that 34 percent of property tax collections are from homesteads after applying the local tax relief. The differential of six percentage points represents the impact of the local relief.

**Table 5: School Property Tax - Homestead and Owner-Occupied Estimates**

|                            | 2019-20      | 2020-21      | 2021-22      | 2022-23      | 2023-24       | 2024-25       | 2025-26       |
|----------------------------|--------------|--------------|--------------|--------------|---------------|---------------|---------------|
| <u>Homestead Exclusion</u> |              |              |              |              |               |               |               |
| Current-Year               | \$7,722      | \$7,619      | \$7,881      | \$8,184      | \$8,529       | \$8,859       | \$9,172       |
| Act 1 Allocations          | 534          | 535          | 535          | 535          | 535           | 535           | 535           |
| Delinquent                 | <u>305</u>   | <u>263</u>   | <u>333</u>   | <u>334</u>   | <u>336</u>    | <u>349</u>    | <u>360</u>    |
| <b>Total</b>               | <b>8,562</b> | <b>8,417</b> | <b>8,749</b> | <b>9,052</b> | <b>9,400</b>  | <b>9,742</b>  | <b>10,067</b> |
| <u>Owner-Occupied</u>      |              |              |              |              |               |               |               |
| Current-Year               | \$8,294      | \$8,183      | \$8,465      | \$8,790      | \$9,161       | \$9,515       | \$9,851       |
| Act 1 Allocations          | 534          | 535          | 535          | 535          | 535           | 535           | 535           |
| Delinquent                 | <u>328</u>   | <u>283</u>   | <u>358</u>   | <u>358</u>   | <u>361</u>    | <u>374</u>    | <u>387</u>    |
| <b>Total</b>               | <b>9,157</b> | <b>9,001</b> | <b>9,358</b> | <b>9,683</b> | <b>10,057</b> | <b>10,424</b> | <b>10,773</b> |

Note: Dollar amounts in millions.

Proposals to replace property taxes on homesteads may either include or exclude the value of the local relief to determine the revenues that must be replaced. Based on data provided by the U.S. Census Bureau’s American Community Survey and statewide property tax revenue reported by PDE and the Department of Community and Economic Development, the IFO estimates that owner-occupied households remit approximately 58 percent of statewide property taxes. That parameter is applied to current-year and delinquent school property tax collections. The Act 1 allocations are used to offset property taxes for homestead properties, and the homeowner estimates include 100 percent of such allocations.

Despite being included in the estimates throughout this report, the Act 1 allocations would not necessarily be subject to replacement under school property tax elimination. These allocations could be redirected for other purposes or used to offset the net cost of elimination. The treatment of the Act 1 allocations would depend on proposed legislation. Also, other forms of property tax relief provided to homeowners should be considered when calculating the funds necessary for elimination. In 2018, the Property Tax Rent Rebate (PTRR) Program provided \$142.7 million to homeowners. That figure includes all types of property taxes (school, county and municipal), and the IFO estimates that school property taxes account for roughly 70 percent of the total. If the PTRR Program was maintained, then this amount could be subtracted from the net funds necessary to eliminate school property taxes. Finally, it should be noted that property tax implicitly paid by renters is not included in the computations in Table 5.

### Staff Acknowledgements

This report was produced by Jesse Bushman. Questions regarding this report can be directed to [jbushman@ifo.state.pa.us](mailto:jbushman@ifo.state.pa.us).

<sup>12</sup> Additional details are available in Table 3 of the November 6, 2017 letter to Representative Francis X. Ryan. See <http://www.ifo.state.pa.us/Resources/Documents/SR2017-05.pdf>.