

New Jersey Governor, 1974 - (Byrne)

PROPOSED EDUCATION REFORM-PROPERTY TAX RELIEF PROGRAM

MAY, 1974

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A program to solve the education -tax problem thrust upon the public agenda by the Supreme Court decision will ultimately involve School finance, a definition of a "thorough and efficient system", a look at the problem of municipal overburden, and a tax program. This paper deals with school finance and "thorough and efficient".

School Finance

The Court found that the present system of school finance is unconstitutional because of the discrepancies in per pupil spending among school districts.

The trial court found the constitutional demand had not been met and did so on the basis of discrepancies in dollar input per pupil. We agree. We deal with the problem in those terms because dollar input is plainly relevant....The constitutional mandate could not be said to be satisfied unless we were to suppose the unlikely proposition that the lowest level of dollar performance happens to coincide with the constitutional mandate and that all efforts beyond the lowest level are attributable to local decisions to do more than the State was obliged to do.

Robinson v. Cahill
62 N.J. at 515

School monies are raised primarily from local property taxation. Property wealth varies widely among school districts. This variation is at the root of the discrepancies in school spending per pupil. For example, some districts, such as Englewood Cliffs, have ten times as much property wealth per pupil as others, such as Willingboro, and can raise substantially more money at lower tax rates. Englewood Cliffs spends about twice as much per pupil as Willingboro at less than half the tax effort.

Basic Plan

Our plan is to place every pupil in New Jersey on an equal fiscal base. The State will guarantee an equalized valuation per pupil. The average equalized valuation per pupil is now \$53,000. If the State guarantees twice the average, or \$106,000, the plan would work as follows. A district with average property wealth per pupil would receive one half of its school budget from the State. A district with \$106,000 would receive no state aid. A poor district, say one with only \$26,500 per pupil, would get 75 percent state aid.

Under this plan, every pupil in New Jersey would have equal fiscal backing. It will no longer matter if the child lives in a community of great wealth or little wealth.

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1. Six percent of the districts with three percent of the pupils have equalized valuation above \$106,000. These extremely wealthy districts will get no state aid, but they will still have an advantage over the remainder of the districts in terms of wealth per pupil. They will remain as exceptions to the equalization principle, exceptions which can be tolerated because they are so few in numbers.

The presumption is that poor districts spend less because of fiscal constraints. Once these constraints are lifted by this plan, these districts will be able to concentrate on raising the quality of their education, rather than eking out a passable budget. However, there is a limit to the amount of increased spending that can be usefully planned and absorbed from one year to another. Therefore, there should be a limit on the permissible annual budget increases. This limit should be greater for the lower spending districts and less for the higher spending districts so that the discrepancies in per pupil spending are narrowed and eliminated over time by a process of levelling upward - not downward. Moreover, we are seeking better education, not merely more spending, so that increases will be made upon a thoughtful plan to improve the quality of education.

The higher spending districts will also be permitted to increase spending, but at a lower rate. After a point, the State will stop sharing. This point might be the 65th percentile of per pupil spending; in any case it should be high enough to assure that enough money is available for a sound education. The reason for a cut-off in state aid is that the state should concentrate on raising the quality of education in those districts which are more likely to be offering less than a thorough and efficient system of education. It should not be subsidizing extra costs for districts which are presumably already above that level, at least not until all districts have attained it. Furthermore, the cut-off will somewhat retard increased spending at the higher levels and speed the elimination of the per pupil spending disparities.

At the very highest spending levels, where per pupil costs approach the annual tuition at exclusive private schools, there should be a dampening of further increases. At these

levels, there could be either an absolute limit on spending increases, a limit on increased staffing per pupil, or a "recapture" provision.

Excess Costs

Some pupils cost more to educate than others, as the Court and existing statutes recognize. The plan would take this excess cost into account in the following manner. Categories of high cost pupils, such as handicapped, vocational, and bilingual, would be identified. The excess cost of educating each category would be paid to the districts by the state. There would be a category of excess costs for compensatory education defined to include those pupils who are eligible for Title I assistance. The amount of excess costs per pupil would be determined according to existing spending patterns until the educational evaluations conducted under the "Thorough and Efficient" procedures showed whether these amounts are appropriate. The aid for excess costs would be tied to

needed educational inputs; it would not be a hidden means of skewing the aid distribution to one class of districts or another.

Capital Construction

The State will share in the cost of debt service for capital construction or the same equalizing approach - that is - with a guaranteed valuation of \$106,000 for every district. It will also extend its emergency building aid program in which the State pays the full cost of school building programs in selected high priority areas.

To summarize, the new school finance system would have these attributes:

- 1) A guaranteed valuation behind each pupil;
- 2) Spending limits, more liberal for the low-spending districts and progressively more restrictive for the high spending districts.
- 3) Full State funding of the excess cost of educating special kinds of students.
- 4) Shared-cost approach to debt service and fully funded building program for priority school building needs.

Total Cost

The effect of this plan, on the whole, would be to raise the State's share of the total education budget from about 30 percent to about 50 percent by substituting state revenues for local property taxes. The State would assume approximately \$550 million now being raised locally.

Existing categories of State aid, amounting to some \$600 million, would be channelled into the new program as well. This will eliminate certain categories of state aid which are of doubtful constitutionality, such as minimum aid and save-harmless. However, for almost all districts, the new state money would more than offset the loss of these aid categories.

Effect on Local Tax Rates

Local governments now raise some \$1.6 billion for education. The new state money will therefore bring about a cut of nearly one-third in the aggregate school tax rates of local governments. Some 94 percent of the school districts, with 97 percent of the pupils will be included in the state aid plan. Almost all of them would get more state aid than

they do now. Of course, the poorer districts would get proportionately more aid. Large amounts of new State aid would go to the older cities. The largest proportional increases would go to those districts which had previously been excluded from "incentive aid" under the Bateman-Tanzman formula but which were not much ahead of the poorest districts in per pupil wealth. For example, in Essex County, Newark, East Orange, and Orange would move to levels of from 65 to more than 80 percent state funding. Newark had already been raised to 64 percent by Bateman aid. But Glen Ridge, Irvington, Belleville, and Bloomfield which had only about 15% in minimum aid before would raise to about 50 percent state funding - with correspondingly large decreases in property taxes. In rural areas with generally lower taxable wealth, almost all districts would move up dramatically in state aid. For example, in Burlington County, 37 districts would have half or more of their school budgets paid through state aid. Every district in Cumberland would be receiving two-thirds or more of their school budgets from state revenues. And so on.

Alternatives

The shared-cost plan can be adapted in various ways to different spending levels and different distribution patterns. Generally, a reduction in the total State share leads to a smaller percentage of state aid for all districts - and a larger number of districts getting less state aid than now and no state aid at all.

The basic alternative to shared-cost is "full-state funding". "Full-state funding" failed to gain acceptance in New Jersey when it was the main part of the Tax Policy Committee program and it has not been adopted in several other States where it was proposed as a solution to school finance problems similar to ours. Hawaii, the only state with a tradition of full state funding, is beginning to move away from it.

The advantage of shared-cost is that it permits local school districts to have flexibility in setting their programs

and budgets. There is no need to set a standardized, centrally directed school budget with rigidified weighting formulas which attempt to take account of any number of variable cost factors.

Summary

The shared cost plan at the proposed guaranteed valuation of \$106,000 per pupil would accomplish these goals:

- 1) It would put the education of every school child in New Jersey (with a very few exceptions) on an equal fiscal footing;
- 2) It would raise the State's share of the total education bill, reducing New Jersey's dependence on the inelastic and inequitable local property tax;
- 3) It would give substantial property tax relief to almost all New Jersey taxing districts;
- 4) It would set the educational system on a sound and equalized financial base which could support the attainment of a thorough and efficient system of education;
- 5) For so major a shift, it would have relatively little impact on the relationship of the school to the parents and the local community.

Thorough and Efficient

In choosing a shared-cost financing plan and rejecting "full-state funding", we have opted for the fullest possible exercise of local discretion and control consistent with the Court decision. We have done this because we believe that the concern and the involvement of parents is the ultimate force for a continuous improvement of the educational system. We have done this also because we do not believe that it is possible to specify in one formula all the variables and all the elements of a "thorough and efficient school system" that comprises 600 school districts with so great a variety of hopes and problems. A school is not a manufacturing assemblyline processing standardized materials into identical molds.

In relying on the diversity of local school districts for the attainment of a thorough and efficient system, we must accept certain constitutional mandates. The State

must assume ultimate responsibility for school performance.

"We repeat that if the State chooses to assign its obligation under the 1875 amendment to local government, the State must do so by a plan which will fulfill the State's continuing obligation. To that end the State must define in some discernible way the educational obligation and must compel the local school districts to raise the money necessary to provide that opportunity."

Robinson v. Cahill
62 N.J. at 519

In defining its educational obligation, the State

must calibrate its standards against the demands of the

labor market.

"Thorough and efficient must be understood to embrace that educational opportunity which is needed in the contemporary setting to equip a child for his role as a citizen and as a competitor in the labor market."

Robinson v. Cahill
62 N.J. at 515

And where those standards are met, the state is

required to compensate for local failures:

"The State has never spelled out the content of the constitutionality mandated educational opportunity. Nor has the state required the school districts to raise monies needed to achieve that unstated standard. Nor is the state aid program designed to compensate for local failures to reach that level."

Robinson v. Cahill
62 N.J. at 519

These then are the minimum components of a thorough

and efficient school program -- a system for discerning

and applying educational standards, a procedure for monitoring and evaluation local schools in light of these standards, and authorization for state action to correct deficiencies in local school operations.

General Standards

In defining specific standards, the legislature labors under the same handicap carried by the Court -- inadequate information about the needs and problems of largely autonomous local school districts. The state is urged by some to proceed anyway, to adopt rigid input or output measures, permanently defining thorough and efficient education in terms of staff-pupil ratios or standardized test results.

The legislation should define the standards of a thorough and efficient education in broad terms which encompass the expected results of education, the maintenance of sufficient inputs needed to achieve those results, and the organizational and procedural elements of the local

school districts which make up the State's educational system.

The task of elaborating upon the general standards, giving them detailed content and the flexibility needed to accommodate diverse local situations, and keeping them current should be delegated to the educational experts in the Department of Education. The Department of Education has been drafting a series of detailed definitions of "thorough and efficient". It has narrowed some of the difficult issues after much discussion with education groups and experts, but more time is needed to arrive at a consensus. In any event, the State Board must take direction from the general standards and philosophy which the Legislature will set.

In keeping its standards current, the Department of Education should be counseled annually by the Commissioner of Labor and Industry, who shall submit a report projecting labor needs and employment qualifications in New Jersey and by

the Commissioner of Higher Education, who shall report on college entry requirements and anticipated enrollment levels.

A special Task Force should also be established to study the business practices of local school systems, looking towards improvements in the efficiency of school financial affairs. Members could include representatives of the Department of Education, the Division of Budget and Accounting, local school boards, and private business. The Task Force should report to the Governor and the Legislature ways to improve school business and financial practices.

Evaluation and Reporting

The second component of the state's education obligation is a system for the ongoing evaluation of school performance and for prompt remedial action where thorough and efficient standards are not met. While the state cannot prescribe all the elements of an idealized school system, it can and -- in the Court's view -- it must provide for continuous evaluation and review of school performance.

The Legislature should direct the State Board to evaluate the performance of each school district and to require annual testing of all students for achievement in reading and mathematical skills as part of this evaluation. Each school district shall be required to conduct a yearly self-evaluation and to develop and implement a plan for correcting deficiencies. The State Department of Education will offer technical assistance in all phases of this activity. These district reports will provide the basis for an annual report by the Commissioner,

to be presented in a form that allows the legislature to know the condition of education in New Jersey.

Corrective Action

The Commission shall review the District reports, the test results, and the findings of the Department's evaluators to determine where the standards of a thorough and efficient education are not being maintained. Where deficiencies are noted, the Department will review the District's own remedial plan and recommend improvements or additions where necessary. In cases where the Department, after an inquiry into the causes of poor performance, determines the local remedial plan to be insufficient, it will recommend its own plan for corrective action -- including suggestions that resources be reallocated or that local spending be increased. If a school district is unwilling or unable to institute corrective measures, it will be certified to the State Board for appropriate action. And in extreme instances

of nonfeasance, the State Board may order corrective action, including -- where drastic circumstances warrant -- the assumption of receivership responsibilities for the direct administration of an uncooperative school district.

Requirements Imposed Upon the State Board by the Funding Plan

Increases in Spending

The funding plan encourages low-spending districts to augment their educational programs and provides the financial wherewithal for them to do so. The intent is to eliminate deficiencies and to raise educational standards, not merely to spend an arbitrarily higher figure. The State Board will have the responsibility for seeing that the intent is carried out.

Excess Costs

The funding plan provides full state funding of the excess cost of educating special categories of students. The intention is that the excess monies thus provided be spent on supplemental education. The State Board will be responsible for setting

reporting and evaluation standards to see that this intent is carried out and that the excess monies are indeed yielding results.

Evolution of Refined Definition of Thorough and Efficient

As a result of the reporting and evaluation procedures required in this program, the State Board will have a developing empirical basis for determining the extent to which school districts are succeeding in their mandate. In addition to its annual reports, after four years of evaluation the Board shall make a comprehensive report to the Governor and to the Legislature as to the efficacy of the new financing plan in producing the desired results. This report shall trace the progress of the local school districts in attaining thorough and efficient standards, shall identify those districts and individual schools which remain below the standards, conclude whether the existing system is proceeding apace to eliminate the remaining deficiencies, and make recommendations, if necessary, for altering the system to speed the elimination of educational deficiencies.

These corrective powers, essential to the state's obligations under the court ruling, should not dilute another element of thorough and efficient education -- the essential preservation of strong local school districts. The strength of New Jersey's school system depends in great measure on the proximity of parents and citizens to school decision-making. Their participation brings a concerned oversight with intimate perspective that no remote governmental agency can match and is essential to a thorough and efficient system of education.

Related Local Property Tax Inequities

An easing of disproportionately high property tax burdens is recognized as an integral concern in school finance reform, particularly where "power equalization" is contemplated.

The (Bateman) Report acknowledges that one difficulty with the design for local fiscal responsibility is that the tax base to which the school districts are remitted is already overloaded, particularly in the major cities, by the other demands for local service.

Robinson v. Cahill
62 NJ at 519

Our school finance plan would equalize tax-ability for school purposes, but the equalized school tax rates would be added to a municipal-county rate which is much higher in some places than in others.

There will inevitably be differences in tax rates from one municipality to another and from one county to another. The types of services, the cost of government, and the levels of efficiency vary. Rather than seeking an arbitrary and practically unattainable equality of municipal tax rates, we approach the overburden problem by finding those governmental costs which ought to be the

shared responsibility of all New Jerseyans, but which fall unjustifiably on local taxpayers. By removing these costs from the local property tax base and placing them on a broad state tax base, we serve both to bring about equity and to ease the municipal overburden.

Some of the programs which might make up a package of property tax relief for municipal overburden are as follows:

1 - County Welfare - \$86 million

The 1974 appropriation by the 21 counties for welfare was \$86 million, including the following programs:

AFDC

Bureau of Children's Services

County Welfare Board Administration

Assistance to the Working Poor

Supplemental Social Security Income

A State assumption of these programs would relieve the county budgets and thereby the local tax bills of this \$86 million.

2 - Municipal Welfare - \$11.3 million

A State assumption of either the county or municipal welfare programs would require about one year to implement.

3 - Courts - \$38.5 million

The Counties have budgeted \$38.5 million in 1974 for the following: County Courts, Law Library (Superior Courts) District Court, Juvenile and Domestic, Jury Commissioners and Fees, Surrogate, Probation, and Law Library.

The largest court costs are in:

Essex - \$7.3

Bergen - \$4.7

Hudson - \$3.3

In lieu of Tax Payments - \$12.8 million

The State owns property in municipalities throughout New Jersey, but in lieu of tax payments, to help these municipalities provide needed services, are made only to some cities and at rather arbitrary rates. It would cost \$12.8 million to pay the municipalities on the basis of total assessed value of state owned property times a non-school equalized tax rate, excluding land used for roads, bridges, parks, riparian rights, watersheds, reservoirs, wilderness, and open space. Some of the municipalities which would receive sizable amounts of money are: Woodridge, Chesterfield, Montclair, Maurice River, Union Township, Vineland, and Glassboro (from \$170,000 to \$429,000) and Jersey City, Camden, Winslow Township, Ewing, New Brunswick, Piscataway, Hoboken, Parsippany Troy-Hills, Newark, and Trenton (above \$500,000).

Full-taxes on Subsidized Housing - \$47.3 million

Housing for low-income and moderate income families and senior citizens is built in New Jersey with federal or state subsidies. The municipalities which accommodate this type of housing bear the service costs and the school costs (in the case of family housing). They bear a disproportionate share of the burden of the State's housing policy. Moreover, they do not even get the full taxes on this housing, because taxes are abated under one formula or another. This, in a sense, is a double inequity.

The State could make up the difference between full taxes and presently abated taxes for \$35.3 million on housing for families. The housing tax make-up would cost \$12.0 million for senior citizen housing at full tax rates, and less if the non-school tax rate were applied. Eighty-five municipalities would benefit from this program, but the largest inequities would be eliminated in the older cities.

Municipal Aid Formula

The Tax Policy Committee recommended a \$100 million urban aid formula grant which would be distributed to some 220 municipalities based on population, property value, and tax effort. The existing urban aid formula, now at \$36 million, would have been eliminated. Thus, the cost of instituting this recommendation would now be \$64 million. The formula aid could be installed at any desired level. Indeed, the existing formula could be raised instead. The formula aid approach responds to the general tax situation rather than to specific, definable inequities in the distribution of service costs.

A municipal overburden package

A package to relieve the property tax base or functions and costs which belong to a broader base of taxation could be assembled from these elements:

County Welfare	\$ 86.0
Municipal Welfare	\$ 11.3
In Lieu of Taxes	\$ 12.8
Housing Tax Make-up	\$ 47.3
Courts	\$ 38.5
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	\$ 195.9

In addition, a new formula grant or an increase to existing formula grants could give further tax relief, if the state tax base could absorb it.

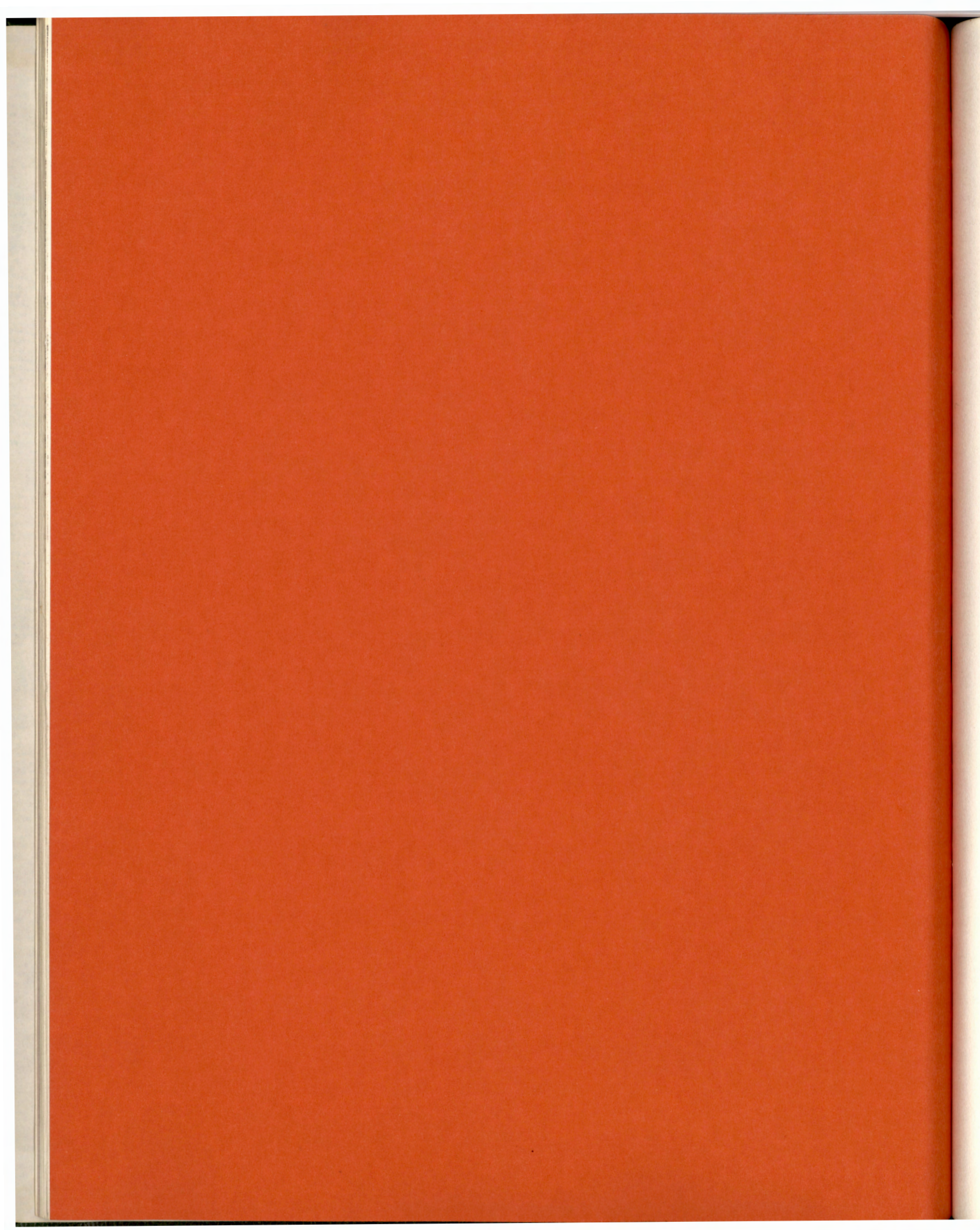
Total Program

1. School Finance Reform - The school program outlined in part I of this paper would transfer some \$550 million from the local property tax base to state tax sources.
2. Municipal Overburden - Further property tax relief obtained by the transfer of certain governmental functions and responsibilities from the local base to the State base would cost some \$200 million for the program outlined above - more if the program were to include a new or increased formula grant to municipalities.
3. Budget Gap - the fiscal year budget for 1974-75 is balanced with a non-recurring surplus of some \$300 million. The expenditures programmed for this surplus, including more than \$150 million in school aid, must be placed upon a continuous revenue base.
4. The program would shift some \$750 million from the local property tax to a broad-based, state tax.

EDUCATION - TAX REFORM

PART II - TAX PROGRAM

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Education - Tax Reform

Part II - Taxes

An earlier paper submitted on May 20, 1974 outlined our response to the Supreme Court's order to reform our public school system. It covered the areas of educational finance and municipal overburden. This paper takes up where that one left off. It will discuss the mechanism by which the State will finance those proposals.

The subsequent discussion of the plan released May 20 involved all legislators and mayors, freeholders, school officials, a wide variety of civic and professional associations, and the public at large. Much of the discussion dealt with the tax program. As a result, this part of the program is built upon a wide sampling of opinion and advice.

THE NEED FOR REPLACEMENT MONEY

The plan guaranteeing a \$106,000 valuation behind all of the school children of our State carries a price tag of \$550 million. This, however, does not represent new money for added spending. Instead, it is replacement money that will be raised by replacement taxes. The plan calls on the State to replace local funds that now finance our school with State funds. The added cost to the State will be balanced by a lower cost to

the taxpayers in the local school district. Our plan calls for State assumption of certain municipal and county costs that will further ease the pressures on the local property taxpayers. In any case, these costs properly are the responsibility of the State. This part will cost roughly \$200 million. Again, this is not new money, and it does not demand new taxes. The \$200 million will replace \$200 million in municipal and county tax revenues with revenues generated by a State tax replacing some of the local property tax. We must also confront the \$300 million revenue gap expected in the next fiscal budget. This sum is provided by a non-recurring surplus this year. In the future, it must be made up from the State's general revenue base.

THE BASIC PLAN

The only equitable way to raise the revenue needed for this program of educational reform and property tax relief is an income tax. To further balance and adjust New Jersey's tax structure, we make the following recommendations;

- 1) A graduated personal income tax which offers the simplicity of the piggyback tax but which closes the door on those who would avoid a fair share of the State tax by preferential treatment they may get in the federal tax system.

2) A constitutional amendment to set a fixed limit on the amount of any New Jerseyan's income - either homeowner or renter - that can be paid in property taxes. This provision will be of special benefit to senior citizens and others on fixed incomes.

3) A constitutionally provided limit on all municipal and county tax rates and a school spending restriction consistent with the constitutionally-mandated education standard so as to insure the permanence of the local property tax relief resulting from our plan.

4) A State Business Stabilization tax on low-taxpaying business and tax havens.

5) Special treatment for tenants, beside the circuit breaker, to allow credit for property taxes paid by them as part of their rent.

THE STATE PERSONAL INCOME TAX

More than forty of the fifty states rely on a personal income tax for a significant part of their revenues. Since 1940, the share of the States' revenues derived from the personal income tax has more than tripled. New Jersey is one of those states which, to date, has chosen not to do so. This increasingly widespread reliance on the income tax is not surprising. The rationale for it is clear and persuasive, notwithstanding New Jersey's repeated refusal to enact such a tax. Now, since the Supreme Court's mandate in Robinson v. Cahill, the rationale is significantly more persuasive.

The disadvantages of the property tax have been documented many times over. It places an excessive burden on property

owners and users. It takes a greater bite from the income of the poor than it does from the income of the wealthy. It fosters the accelerated decay of the cities. It falls especially severely on senior citizens, the retired, and others living on fixed incomes. It is relatively inelastic with respect to income. Yet, New Jersey chooses to pay the highest property taxes in the nation. In 1971, 54.4% of state-local revenues came from the local property tax. The national average was only 38.7%. Alternatively, only 1.23% of the state-local revenues came from the personal income tax, while the national average in this instance was 18%.

It is in this context that the Governor recommends a personal income tax for the State of New Jersey. Such a tax is widely recognized as the most fair of all tax sources. It is equitable; that is, it is a tax levied according to one's ability to pay. A recent poll conducted by the Eagleton Institute at Rutgers University shows that 72% of the respondents think that the tax burden should be related to a person's ability to pay. The personal income tax does this.

It is also the most elastic of all taxes. With an estimated elasticity of 1.5, for every 10% increase in personal income, there will be a 15% increase in tax revenues. In other words, the income tax responds much more readily to general

economic growth. The elasticity of New Jersey's current assortment of state-local taxes is only .98, while the elasticity of expenditures is about 1.5. This means that the state and local governments will be faced, as they are this year, with perennial budget gaps of increasing severity--- unless structural changes are made in an attempt to narrow this disparity. The high rate of inflation throughout the economy exacerbates the problem. In summary, the personal income tax's quality of high elasticity will reduce the need for regular-and resented- tax rate increases. This is a problem which has been especially acute with regard to the local property tax, as most New Jersey taxpayers are painfully aware.

Another important advantage of the personal income tax is that it is deductible from the federal income tax. Thus, it would recapture a substantial amount of money flowing out of the State to the federal government. Since State income tax liability can be deducted from the federal income tax, more than 30% of the yield from the personal income tax would be revenues recaptured from the federal government. As the New Jersey Taxpayers Association has pointed out, New Jersey now receives only \$0.62 in federal aid for every \$1.00 that it pays to the federal government. By recapturing some of the funds going to

the federal government and rechanneling them to state purposes, New Jerseyans will benefit from the full value of the tax dollar.

ALTERNATIVE METHODS OF IMPLEMENTING THE INCOME TAX

States can choose from a variety of ways to implement a personal income tax. The alternatives have been widely discussed and debated in New Jersey and in other states. These discussions have not resulted in a consensus, but they have focused attention on the key issues.

These are two major viewpoints. One group stresses simplicity for the taxpayer and for the tax collector. This group favors the "piggy-back" on the federal income tax. In effect, this alternative --- which now exists in Rhode Island and several other states --- is a simple surcharge on the federal tax payment.

The other group stresses equity. They base their case on the belief that the federal tax system contains inequities which should not be built into a New Jersey income tax. They want State autonomy in deciding what exemptions and deductions should be granted. Specifically, the proponents of this view suggest a graduated tax on gross income. Pennsylvania now has such a tax. They do not consider the

use of adjusted gross income satisfactory because this figure incorporates parts of the federal tax that they consider inequitable. For example, they consider the federal treatment of capital gains and tax exempt bond interest to be serious loopholes.

Actually, the virtues of both types of taxes are somewhat exaggerated when they are characterized as simplicity versus equity. The "piggy-back" tax is not as simple as some of its proponents believe. Although federal law provides for federal collection of the "piggy-back", the law does not take effect until at least two states with five percent of the nation's taxpayers choose federal collection. So far, no state has so chosen. Not only will the State still have to administer the tax, but some taxpayers will be required to make additional computations because the State cannot tax interest from federal bonds or income taxed in another state.*

Similarly, while the gross income tax closes some "loopholes", it creates some inequities of its own since it contains neither exemptions for large families nor deductions for heavy medical expenses. Moreover, since it must allow business expenses to be subtracted in the course of computing business income, some deductions will remain even in the gross income figure. The tax on gross income is more complicated

* New Jersey residents will receive a full credit for tax paid on income earned in other states.

than the "piggy-back" for both the taxpayer and the tax collector and requires added bureaucracy.

Eighty-five percent of Rhode Island taxpayers compute their "piggy-back" personal income tax by making a single computation and then submitting a card with only one entry. The cost of administration there is about one dollar per taxpayer. An important advantage of the "piggy-back" is clarity that derives from its simplicity. Every taxpayer will be able to tell immediately how the tax will affect him by referring to his federal tax return. This obviates the need for complex tables and charts showing how various taxpayers in the various towns, income classes, housing levels, and family situation will be affected.

The "piggy-back" tax, for legal reasons, must include some modification of federal tax computations. Additional changes would offset the desired simplicity of the tax, but we propose a credit or deduction for renters so that their imputed property taxes can be set off against income in the same fashion as homeowner property taxes.

Thus, we recommend a "piggy-back" tax at rates of 1-1/2 to 8 percent of federal taxable income, with the following adjustments: 1) subtraction of interest income from federal bonds; and 2) subtraction of income already taxed in another state.

For those taxpayers who take special ad-

vantages in the federal tax law to pay little or no

taxes on substantial income, we propose a minimum

tax of 3% on gross income. This provision would

make sure that no taxpayer earning more than \$50,000

pays less than 3% of his income to the State of New

Jersey. As a result, no taxpayer can take advantage

of federal preferences for exempt bond interest,

accelerated depreciation, depletion allowance, or

other provisions to escape his fair share of the

tax burden.

The resulting basic tax table is attached:

NEW JERSEY "PIGGY-BACK" PERSONAL INCOME TAX

Rates are progressive from 1.5% on taxable incomes under \$1,000 to 8% on taxable incomes \$25,000 and over

Deductions and Personal Exemptions Allowed
(Family of Four)

<u>ADJUSTED GROSS INCOME</u>	<u>AVERAGE 15% DEDUCTION</u>	<u>EXEMPTION 4 x \$750</u>	<u>TAXABLE INCOME</u>	<u>FEDERAL INCOME TAX</u>	<u>STATE INCOME TAX*</u>
\$ 3,000	\$ 1,500	\$ 3,000	\$ -0-	\$ -0-	\$ -0-
4,000	1,500	3,000	-0-	-0-	-0-
5,000	1,500	3,000	500	70.00	7.50
7,500	1,500	3,000	3,000	450.00	55.00
10,000	1,500	3,000	5,500	905.00	120.00
12,500	1,875	3,000	7,625	1,308.75	186.88
15,000	2,250	3,000	9,750	1,765.00	265.00
20,000	3,000	3,000	14,000	2,760.00	455.00
25,000	3,750	3,000	18,250	3,890.00	690.00
30,000	4,500	3,000	22,500	5,180.00	970.00
50,000	7,500	3,000	39,500	11,915.00	2,315.00
100,000	15,000	3,000	82,000	34,500.00	5,715.00

* State Income Tax is deductible for federal income tax purposes. As a result, an average of 30 percent of New Jersey income tax payments will be money saved from federal tax payments and the out-of-pocket cost to the New Jersey income taxpayer will be an average of 30 percent less than the figures shown in the last column

Its estimated yield for 1975 is \$940 million.

THE CIRCUIT BREAKER

Nearly half of the states---including Michigan, Vermont, Wisconsin, and Oregon---have enacted "circuit-breaker" legislation to provide property tax relief. The "circuit-breaker prevents tax overload in the way that the electrical circuit-breaker guards a home from an overload of electrical current. The tax device will apply to all New Jersey renters and homeowners, but it will be of special benefit to senior citizens and other households on fixed incomes. It is also a form of household insurance against sudden drops in income as a result of unemployment or disability.

This device has several distinct advantages. First, it is a tax relief aimed directly at those who most need it. Second, it requires a minimum of administration and cost. Either the tax relief will be credited against the income tax liability, or it can take the form of a cash rebate. In the latter case, the applicant simply would receive a check in the mail. Third, the relief is provided from State revenues and does not impinge on the unequal revenue pool of local governments. Thus, it is a superior form of homestead exemption. Fourth, for those who qualify and even for those who are approaching an excess property tax burden, the circuit breaker is an absolute limit on property taxes and tax increases.

The circuit-breaker we propose would apply to households at all income levels. The ceiling percentage of income payable

in property taxes---after which point the circuit-breaker is activated---will be graduated from 5% for the lowest income level to 10% for the higher level. The following is a circuit-breaker schedule:

<u>Household Gross Income</u>	<u>Circuit-breaker activated at:</u>
Under \$5,000	5% of income
5,000 to 10,000	6% of income
10,000 to 15,000	7% of income
15,000 to 25,000	8% of income
25,000 and over	10% of income

Tenants would be allowed to count 20% of their rent as property tax.

A family with gross income of \$11,000 and living in a house valued at \$29,000 would benefit from the circuit-breaker in the following manner. Assume a property tax rate of \$4.00, and property taxes of \$1160. But, property taxes are not allowed to exceed 7% of the \$11,000 income, or \$770. The \$390 difference between the actual property tax of \$1160 and the maximum allowable property tax of \$770 would be either credited to the income tax or rebated as cash.

Another example - assume a property tax rate of 2.30 - \$690 in taxes on a \$30,000 house. A family with income of \$8,000 will have a property tax limit of \$480 and will get a \$210 credit - rebate on its income tax - which would be under \$100.

A household earning \$4500 and paying an annual rent

of \$1800 (\$150 a month) would count 20% of the \$1800 rent, or \$360, as property tax. At the \$4500 income level, the circuit breaker is activated at 5% of income, or \$225, in this case. So the household would receive a cash rebate of \$135, since its income is not high enough to trigger income tax payments.

The circuit breaker gives direct property tax relief and sets a limit on property tax increases for those who need it most. Thus, it gives relief to overburdened taxpayers and renters who did not share in the general property tax relief program because they happened to live in communities which were wealthy on the whole.

LIMITS ON LOCAL PROPERTY TAXES

At a time when municipal and county rates have been increasing, it becomes necessary to ensure the permanence of the property tax relief provided for by our plan. To do this, we recommend the imposition of caps on municipal, school, and county property taxes. County and municipal property taxes (excluding debt service) will be permitted to exceed their 1975 rates, after the relief provided by our plan, by not more than 6% in the first year. In emergencies, the cap may be exceeded only with the express approval of the Local Finance Board, or alternatively by a referendum at the local level.

School spending increases will be limited under the School finance legislation. The permissible increase will be greater for low spending districts if new programs are needed to achieve the constitutionally-mandated standard of education. Otherwise, the limits on school spending increases can be exceeded only by local referendum.

THE BUSINESS STABILIZATION TAX

Two issues---the windfall to business and the tax havens---have arisen in almost every discussion of tax reform. Admittedly, business will benefit from the local property tax reduction. While there are those who argue that New Jersey must offer this relief to maintain its economic competitiveness, particularly in the uncertain economic climate of today, there are others who maintain that business can thrive without a tax cut. Often this group also argues that, under the local property tax reform program, business will not be paying its fair share.

The issue is complicated by the need to decide which businesses have indeed received a windfall, and which have received justifiable relief. The fact that not all businesses are the same cannot be ignored. Some already bear a heavy tax burden, while others are not taxed so heavily. A large share of the local property tax relief will fall on urban businesses, which already are being taxed at excessive rates. Our plan focuses much of the local property tax relief to business in urban areas. Forty-five percent of this business tax relief on commercial properties is focused on the 24 urban aid cities. For industrial property, the figure is 42%, and for apartments it is 50%. Such relief should be of considerable aid in spurring the revitalization of the cities.

We recommend a novel solution---the Business Stabilization Tax---to this difficult problem. The State will impose an equalized business property tax of \$3.00, from which businesses will subtract $3/4$ of its equalized local tax rate to determine its Stabilization Tax rate. For example, a business in a municipality with an equalized \$4.00 tax rate will subtract \$3.00 ($3/4$ of \$4.00) from the State property tax rate of \$3.00 and will be left with a Stabilization Tax rate of zero. So this business would pay no Stabilization Tax. On the other hand, a business located in a municipality with low local tax rates would be treated differently. Teterboro, for instance, has a tax rate of \$0.70. After subtracting \$0.53 ($3/4$ of \$0.70) from \$3.00, we find a Stabilization Tax rate for Teterboro of \$2.47.

The average equalized tax rate in 1974 is \$3.69. This average rate would be reduced by slightly over 25% under our education-tax relief program. The proposed average equalized rate for business would then be about \$2.69. The average business would subtract $3/4$ of this \$2.69, or \$2.00, from the \$3.00 State rate and thus establish a Stabilization Tax rate of \$1.00. A business paying the average equalized local property tax rate will therefore continue to pay the same amount of property tax, with the Stabilization Tax offsetting the local property tax relief.

The following table shows how businesses in a handful of municipalities will fare under the Stabilization Tax.

EFFECT OF PROPOSED BUSINESS STABILIZATION TAX
ON SEVEN SELECTED MUNICIPALITIES
1974 RATES

(1)	(2)	(3)	(4)	(5)	
<u>Municipality</u>	<u>Current Equalized Tax Rate</u>	<u>Proposed Equalized Tax Rate</u>	<u>Proposed Stabilization Tax Rate</u> [\$3 - Column 3x\$.75]	<u>Total Proposed Business Property Tax</u> [Column 3 + Column 4]	
					Change
Bayonne	\$ 5.07	\$ 3.93	\$ 0.05	\$ 3.98	-1.09
Atlantic City	6.29	4.93	0.0	4.93	-1.36
Englewood	4.23	4.05	0.0	4.05	.18
Teterboro	.70	.64	2.52	3.16	+2.46
Montclair	5.24	4.07	0.0	4.07	-1.17
Paterson	4.76	3.15	0.64	3.79	-.97
Jersey City	6.10	3.98	0.0	3.98	-2.12

A comparison of Column 2 with Column 5 reveals the real impact of our total tax plan on the businesses in the municipalities shown. The plan includes a \$200 credit against the Stabilization Tax to mitigate its impact on small, neighborhood business.

Clearly, the Business Stabilization Tax focuses on those businesses with low tax burdens---many of which are found in tax havens---and raises their tax rate to about the average level. Businesses already paying \$4 or more, on an equalized basis, will not face any new taxes. In essence, it is a graduated business tax haven tax. Not only does it provide for equity in regard to the distribution of the tax burden between households and business, but it also provides for a greater equity of taxation among businesses. The Stabilization Tax would be imposed after local tax rates are established, so the municipalities will continue to derive the full tax benefits they now get from their business tax base. Thus, the new tax avoids interfering with local tax rates or revenues.

The yield of this tax will be approximately \$200 million.

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Category	Value	Percentage
Category 1	100	100%
Category 2	50	50%
Category 3	25	25%
Category 4	12.5	12.5%
Category 5	6.25	6.25%
Category 6	3.125	3.125%
Category 7	1.5625	1.5625%
Category 8	0.78125	0.78125%
Category 9	0.390625	0.390625%
Category 10	0.1953125	0.1953125%