

## **Fundamental Property Tax Reform – 2008**

Almost everyone in New Jersey knows that despite being one of the richest states in the country, New Jersey is facing a property tax crisis. The Administration has supported a 20% reduction for at least 70% of taxpayers, but it unclear how this would be funded and how long the State will be able to afford it. It is also unclear, even if that goal is reached, whether it will achieve PlanSmart NJ's goal to improve the direction of New Jersey's economy and reduce the many inequities and inefficiencies that are embedded in the system today.

Working with the New Jersey Regional Coalition, PlanSmart NJ has developed a two-stage approach that will put us on the path to achieve both goals. The first recommendation, **targeted state school funding reform**, will provide immediate relief to a large majority of New Jersey taxpayers. The Legislature enacted something like this earlier this year. The other, **regional tax-base sharing**, will provide the structural reform that is needed to address broader concerns over the long-term.

Impact simulations show this two-stage approach will provide substantial property tax relief and provide more resources to improve the quality of New Jersey's education system in the majority of districts. At the same time, these recommendations will reduce the competition among municipalities, helping New Jersey to compete in a global economy.

Sustainable economic growth, will, in turn, provide a more stable fiscal platform for state and local government. In addition, they will set us on the path toward a sustainable land use pattern that will balance jobs and housing, reduce land and resource consumption, reduce racial and economic segregation and improve transportation options.

Regional tax base sharing adds no new taxes. For this reason, its benefits are the most dramatic over the long term. Tax base sharing delivers a stronger regional economy, which, over the long term, needs less State intervention, less state funding.

***Regional tax base sharing requires no consolidations and leaves most of the status quo intact. But experience in Minnesota, however, shows that when competition between municipalities is reduced, cooperation becomes easier to do. Once regional tax base sharing is established, the management of regional systems, such as growth pressure, transportation, wastewater and so forth, become easier to accomplish.***

In the short term, however, tax base sharing provides little relief today for some communities. That is why we recommended using the increased sales tax revenues enacted

last year for new school aid, so that the State can simultaneously reduce local dependence on property taxes, improve the education of New Jersey's children, and significantly lower property taxes for a majority of taxpayers. ***Of course, consolidating school districts will accelerate these benefits.***

***The benefits of school funding reform are immediate, but are costly to the State. If this relief is coupled with tax base sharing reform, towns within a region can stop competing with each other and grow the region's economic base to provide more revenue capacity for the benefit of all. Over time, the burden on the State to supplement revenues can be reduced or shifted to other needed investments.***

New Jersey has a unique opportunity to lower property taxes in a way that will benefit all taxpayers. Together, Regional Tax Base Sharing and new school aid provide structural reform that delivers over both the short and long term at an affordable cost. They address the PlanSmart NJ's agenda to encourage development of the right kind, density, mix, type and amount in the right locations. Now is the time for New Jersey to embrace this change.

### **Regional Tax Base Sharing**

**Problem:** Under the current property tax system, the costs of development are shared by neighboring municipalities, while the added revenues are not. This inequity produces large differences in community wealth and remains a major barrier to revitalization efforts. This creates competition between communities called the "ratables chase." Towns that "lose" this race, are forced to raise taxes as they struggle to maintain services.

For this reason, communities are pressured to continue the "ratables chase," resulting in inefficient development patterns, unnecessarily converting open land into development. Many built-out communities are left with underused infrastructure, while costly new infrastructure in the hinterlands is required to be built.

The competition for jobs, in turn, creates pressure to build new housing where the jobs have located, speeding up the conversion of open land, often at low ex-urban densities. The pressure for housing is often resisted, however, because our tax system requires municipalities to pick up much of the cost of education, creating expenses that outweigh the tax revenue from all but the most expensive housing. This creates an imbalance in the jobs-to-housing ratio, forcing workers to locate further and further away, causing roads to be congested over long commutes.

A vicious cycle continues, sustaining high property tax rates in older towns and hurting New Jersey's present and future.

**Concept:** Regional Tax Base Sharing (RTBS) responds to these issues of inequity, inefficiency and imbalance by sharing a portion of the growth in property tax base within defined regions. Sharing is critical because although traffic, air pollution and water demand

do not follow community boundaries, the revenues from development stay within the lines. This is not a problem only for urban areas and inner-ring suburbs, but outer suburbs and rural areas suffer from the costs of new schools and infrastructure. Under our present system, however, there is no incentive to cooperate for mutual benefit.

In an RTBS system, each region is drawn to capture commuters, economic relationships, and varieties in housing. As the tax base grows in each region, the benefits are shared by all communities. Sharing reduces the fiscal pressure to develop, and removes some of the market distortions and barriers in place today.

Communities are no longer enemies competing for the same slices of the ratable “pie” but part of a team that can make the “pie” bigger. By mandating cooperation, RTBS enables all communities to provide basic services at reasonable tax rates.

Once the fiscal pressure is reduced, towns can compete as a region, leveraging far greater assets than they could alone. Coordinated economic development is more efficient and effective, leading to cost savings. Reducing fiscal pressures also allows greater environmental preservation. By adding incentives for development where infrastructure exists, this program also corresponds with New Jersey’s State Plan.

Tax-base sharing has been in use for more than 30 years right here in New Jersey, in the Hackensack Meadowlands. It also has been used since 1971 on a much larger scale – across seven counties and 2.6 million people in the Minneapolis-St. Paul (MN) metropolitan area. ***Both of these examples have survived repeated legal challenges to their constitutionality under each state’s Uniformity Clause.***

***RTBS is not another tax. It is not “revenue-sharing” – towns do not write checks to each other. It also does not affect existing development – the existing tax-base in each town is not shared. RTBS is based on new growth within the region.***

## **How Regional Tax Base Sharing Works**

**1. Establish Regional Boundaries.** We propose combining COAH regions into three RTBS regions. COAH regions are appropriate because they were established, in part, to address wealth disparities, and they describe areas that share a tax base (employment centers) and workers (commuter sheds).

**2. Establish a Base Year,** from which tax base growth is calculated. This year needs to be chosen carefully, to account for unique events.

**3. Define what is to be shared.** We propose sharing growth from the Commercial-Industrial tax base only. This targets the portion of the tax base most important to the regional economy, as well as keeping the system simple.

**4. Pool Portion of New Tax Base.** In both the Meadowlands and Minnesota examples, 60% of new tax base is kept locally, and 40% is collected into a regional pool. This ratio acknowledges that some costs are borne by the community in which development locates, while other costs spread to neighboring communities.

**5. Allocate Shared Tax Base.** The entire regional pool is redistributed to region members based on the number of households. If Newark has 26% of its region's households, it will receive 26% of the shared tax base pool. ***The formula does not take community wealth or personal income into account.***

**6. Provide Protection.** Over time, adjustments may be necessary to the system.

**7. Support RTBS with Comprehensive reform.** ***Although RTBS provides many benefits on its own, it will not solve every problem, and could be complemented by programs such as: Municipal spending controls, targeted state aid programs, affordable housing programs, transit programs, regional plans to guide new development, regional decision-making authority, and "circuit-breakers" for both individuals and municipalities.***

### **School District Aid Reform**

**Problem:** The current school aid formula is not providing the resources for all of New Jersey's districts to provide a quality education. At one extreme are a few very wealthy towns, which spend far more per student than most other districts. And they can do so without high rates of taxation. At the opposite extreme are the Abbott districts, which can educate their children only through the high levels of state aid they receive. Hundreds of districts are caught between these two poles – too poor to spend more, and too rich to be an Abbott district.

**Concept:** This formula both preserves current funding levels to all districts, and provides new aid to the most-stressed districts. By targeting new aid with a different formula, significant reductions in property tax rates are achieved. This is possible by reducing reliance on local property taxes to fund education. Towns unable to spend more per student due to already high tax rates, but which are not poor enough to qualify as an Abbott district, would receive enough resources to provide the quality education every child deserves.

## **How New School Aid Works**

**1. Distribute half the aid using a power-equalizing formula.** This kind of formula targets aid to districts with less than the state average revenue capacity, and raises them the same percentage toward the average. Simulations show districts would move at least 45% of the way up to the average with available resources. Greater resources would move districts closer to the state average.

Revenue capacity is the revenue that a district would receive if it both assessed the statewide average property tax rate (for school districts) against its actual tax base, and received its actual aid from the state and federal governments. This formulation means that you neither penalize nor reward districts that currently assess higher- or lower-than-average tax rates.

**2. Distribute half the aid based on the number of poor children per district.** Poor children are defined as students eligible for free or reduced-cost lunch. While communities with low revenue capacity tend to also have large numbers of poor students, this ensures that all districts with need get additional resources.