

SECTION - 2

Questions and Answers

1. Letter of August 18, 2006 From the Department of Education
2. WEBCAST Questions August 2, 2006
3. WEBCAST Questions September 19, 2006

W
C
S
D

T
A
X

C
O
M
M
I
S
I
O
N

2
0
0
6



COMMONWEALTH OF PENNSYLVANIA
DEPARTMENT OF EDUCATION
333 MARKET STREET
HARRISBURG, PA 17126-0333
www.pde.state.pa.us

August 18, 2006

Dear Superintendents:

I am writing to you today to address an issue concerning a provision in Special Session Act 1 of 2006 that has caused a number of inquiries by school districts.

Section 331.2(a) requires each school district to submit a referendum question to the electors at the primary election of 2007 seeking approval to levy, assess and collect an earned income and net profits tax ("EIT") or a personal income tax ("PIT") for the purpose of annually funding homestead and farmstead exclusions.

Section 331.2(c) mandates that this proposed rate of income tax shall not exceed the rate required to provide for the maximum homestead and farmstead exclusion (under 53 Pa. C.S. § 8586). It also provides that the proposed rate shall be sufficient to fund a minimum of 50% of the maximum homestead exclusion, with the exception that the board of school directors is not required to propose an EIT increase that exceeds 1% (or a PIT increase that exceeds the equivalent of a 1% EIT). **The existing EIT rate does not count toward that 1% increase.** Notably, these provisions mean the following:

(1) a school district **may** propose any level of EIT or PIT that would provide for homestead and farmstead exclusions, so long as the revenue generated by such an EIT or PIT does not provide for an exclusion that exceeds the maximum permitted by law; and

(2) a school district that currently levies an earned income tax **must** ask voters whether they want to levy an **additional** EIT or PIT that will fund the minimum level of homestead and farmstead exclusions, with the caveat that the district need not ask for a **increase** that exceeds 1% (the existing EIT rate does not count toward that 1% increase); and

(3) a school district that currently does not levy an earned income tax **must** ask voters whether they want to levy an EIT or PIT that will fund the minimum level of homestead and farmstead exclusions, also with the caveat that the district need not ask for a rate that would exceed 1%.

For example, a school district that currently levies and collects 0.5% earned income tax may ask voters to increase the EIT by 1% (or perhaps more, if item 1 above were applicable), to a total of 1.5%. In this case, 0.5% will continue to be used for school district operations and the additional 1% will be used to annually fund homestead and farmstead exclusions.

Department staff are available to provide assistance as your school district implements the provisions of Act 1. Do not hesitate to contact Barbara Nelson or Benjamin Hanft at (717) 787-5423 or ra-propertytax@state.pa.us.

Sincerely,

A handwritten signature in cursive script that reads "Gerald L. Zahorchak".

Gerald L. Zahorchak, D.Ed.

What Tax Study Commission Members Need To Know
September 19, 2006
WEBCAST QUESTIONS

1. **What if the industry sectors used in the SAWW do not reflect employment of local taxpayers or industries in the district?** The Act 1 index does not distinguish between areas of the Commonwealth. The Index is based on the SAWW or Statewide Average Weekly Wage. This is a Statewide measure and is not regionalized. The other half of the index is the Employment Cost Index for Elementary and Secondary Education which is national employment data.

2. **Does the PIT also include capital gains?** PIT includes eight (8) classes of income that are taxable. These include; compensation; interest; dividends; net profits from operation of a business, profession, or farm; net gains or income from disposition of tangible or intangible property; net gains or income from rents, royalties, patents and copyrights; net gains or income derived through estates or trusts; and gambling or lottery winnings with the exception of PA State Lottery winnings won on or after July 21, 1983. According to the PA Department of Revenue, some capital gains on mutual fund investment are taxable under the PIT.

3. **What happens if the taxpayers vote down the ballot question?** The school district is limited to increasing taxes up to the index plus any exceptions authorized by PDE or the Court of Common Pleas in your county. . Any new or altered tax sought in the referendum question could not be levied unless approved by majority vote in the school district.

4. **Can the Tax Study Commission recommend no EIT, or should the EIT recommendation be "0?"** The statute does not limit the TSC's recommendations, but the school board is charged with recommending one (1) of three (3) referendum questions addressing an additional EIT, imposing a PIT, or converting an existing EIT to a PIT. There is no option to eliminate a current EIT without imposing an alternate tax, nor is there the opportunity to recommend a 0% EIT. We do not advocate that tax study commissions issue recommendations that can not be adopted by the school board.

5. **What is the effect on commercial or industrial property, if any?** The homestead/farmstead exclusion applications only apply to a domicile, therefore, commercial property or industrial property would not qualify for the exclusion. If a district adopts a procedure where it does not distinguish between homestead/farmstead approved properties and non-approved properties, then the commercial/industrial properties may be able to utilize the installment payment process for the payment of real property taxes. New or increased taxes are income based which would be paid by individuals except for certain sole proprietorships or partnerships. In essence, new taxes and tax relief are for individuals and homeowners.

6. **How does the State know the age of a property owner?** Through information obtained from the 2000 Census.
7. **Can we look into “Clean & Green” abuses – properties which no longer qualify for the discount?** This issue is not in purview of the tax study commission under Act 1.
8. **What is required for the committee to publish the public meetings of the TSC and public hearings?** The “Sunshine Act” requires publication of notice of the place, date, and time of a meeting in a newspaper of general circulation in the political subdivision where the meeting will be held no less than three (3) days in advance of the meeting. Tax study commissions must adhere to the requirements of the Sunshine Law.
9. **The referendum questions do not seem to take into consideration a district that does not currently levy an EIT. How does a district approach this issue?** The Referendum Handbook from The Governor’s Center for Local Government Services states that, “in cases where specific wording for the question is provided by the authorizing law, that wording must be rigidly adhered to; any variation from the statutory form of the question will render the election invalid.” Referendum question 1 is the most suited question to address this issue. An example question might read: “Do you favor imposing an additional 1% earned income tax? The revenue generated from the increased tax rate will be used to reduce taxes on qualified residential properties by \$ XXXX. The current earned income tax is 0%.”
10. **How are IU and Vo-Tech/CTC budgets accommodated?** Act 1 addresses the adoption of the preliminary budget proposal by the school district. The deadline for the adoption of a district preliminary budget is February 14, 2007. IU’s and Vo-Tech/CTC’s would also have to adjust their preliminary budget process in order to provide school district’s with such expenditure information.
11. **The PA Dept of Revenue has not yet established regulations regarding PIT and is not anticipated to do so in time for the May 2007 primary election. Is it reasonable then to consider a PIT for this May referendum when the regulations have not nor are anticipated to be ready to allow our levy/collection?** While Act 1 does indicate that the PA Department of Revenue must adopt PIT regulations, the Department has already posted draft regulations for the collection of the PIT and comments to this draft were received until September 6, 2006. We anticipate that the regulations will be submitted by the Department of Revenue for adoption in time to allow tax study commissions to consider the PIT as an option.
12. **Where can we find income levels by age bracket? What website?** Access the following website – National Center for Educational Statistics: School Demographic System which is also accessible from the PASBO TSC Act 1 Link:

<http://nces.ed.gov/surveys/sdds/selectgeo.asp>

Select “school district” for geography type and then follow prompts. You can access a varied list of data available by clicking on “List of Tables.” Specifically, table P55 provides income levels by age bracket.

- 13. If a school district (and voters) elects to use a PIT, is the current EIT eliminated?** Yes, the current EIT would be eliminated. Act 1 specifically addresses this issue. If a Board of School Directors imposes a PIT tax approved by the voters, the board “shall have no authority to impose an earned income and net profits tax...”
- 14. How do school districts located in two (2) counties with two (2) different millage rates determine the median assessment and how do they determine the dollar value of the exclusion? Please access the PASBO web site through the TSC Act 1 link and click on “Minimum and Maximum Exclusion and Variable EIT Rate Calculator – Multi-County.”**
- 15. Can we legally include people who are on welfare or are renting property for the PIT? Act 1 does not address individuals who fall within these classifications. PIT is based on the same criteria as the State Income Tax. If an individual pays the State Income Tax, they would be required to pay the local PIT.**
- 16. If a school district prepares a budget based on anticipated slots/gaming revenues and the revenue is less than what was anticipated, what recourse is open to the district? We recommend that districts do not use gaming fund revenues in the calculations for the 2007-2008 fiscal year budget preparation. Act 1 also provides that on April 15th the Budget Secretary will certify the amount available in the Property Tax Relief Fund & on April 20th the Secretary will notify PDE whether it is authorized to provide districts with property tax reduction allocations so districts will have that information to include in their budgets for the following fiscal year.**
- 17. If taxes are shifted by means of EIT or PIT, could property taxes still be raised in future years subject to the Index? Yes, property taxes could rise equal to the percentage increase of the index and any exceptions that are approved.**
- 18. Is it correct that the proposed EIT or PIT rate that is proposed by the Tax Study Commission be rounded to the nearest 0.1%? Yes, Act 1 provides for the rounding of the EIT or PIT rate to the nearest 0.1%.**
- 19. If the EIT/PIT isn’t raised to the maximum amount allowed now, can it be raised again at a later date? Yes, a future referendum question can be placed on the ballot in the fall election of any odd-numbered year. This question may seek a revision to the**

amount of the current tax or a conversion from the current tax. A TSC must be established each time a referendum question is placed on the ballot.

- 20. How long is the choice afforded by the front end referendum in effect?** The voter decision made at the May 15, 2007 Primary Election will remain in effect for a minimum of two (2) years. At that time, the district can place another referendum question on the ballot in the fall election of any odd-numbered year seeking a revision to or a conversion from the current tax.
- 21. What are the programs that gaming funds will be used for prior to their use for homestead/farmstead relief?** Gaming funds will be distributed in the following areas: compulsive gambling treatment, volunteer fire company grant programs, local law enforcement grants, forest reserves municipal financial relief, and property tax relief.
- 22. If a referendum question is rejected in the May 2007 primary, when is the next time a referendum question may be asked to increase the current EIT or to convert to a PIT?** A district may place a referendum question on the ballot in the fall election of any odd-numbered year.
- 23. If a district adopts a PIT, will the district have access to State and Federal tax returns?** No, districts will not have access to State and Federal tax returns, but Act 1, in addressing the PA Department of Revenue, provides that “the Department of Revenue may permit the proper officer or an authorized agent of a school district imposing a personal income tax ... to inspect the tax returns of any taxpayer of the school district or may furnish to the officer or an authorized agent an abstract of the return of income of any current or former resident of the school district, or supply information concerning any item of income contained in any tax return.”
- 24. When the State begins to distribute funds from gaming revenue, does it affect the minimum and maximum exclusion calculation?** No, it does not affect the min/max exclusion calculation. The gaming funds distributed will further reduce real property tax.
- 25. Upon submittal and approval of the homestead/farmstead exclusion application, how long does an approved application remain valid with the County Assessment Office?** The County Tax Assessment Office may only require a property owner to submit a new application every three (3) years. Each County Assessment Office may establish its own policy concerning how long property approvals will last beyond the initial three (3) year requirement.

26. Will the district have audit rights to verify EIT or PIT? No, districts will not have specific audit rights. There is no provision within Act 1 providing this right to districts. Please see the answer to Question 23.

27. How do county reassessments impact the TSC's decisions? If a county does a countywide reassessment, a Board of School Directors of a district within that county shall reduce its tax rate, if necessary, in the first year of that reassessment so that the percentage increase in taxes levied for that fiscal year, based on the tax duplicate for the preceding year, is less than or equal to the index for that preceding year.

28. How can a district avoid the early budget timeline? A district can maintain the budget timeline as established under section 6-687 of the Public School Code, if the Board of School Directors adopts a resolution no later than 110 days (January 25, 2007) prior to the election date immediately preceding the next fiscal year indicating that the district will not raise the rate of any tax by more than the index or seek exceptions. The impact of this resolution is that the district will not be required to adopt a preliminary budget within the Act 1 timeline.

**Tax Study Commissions under Act 1
August 3, 2006
WEBCAST QUESTIONS**

- 1. Should the school solicitor also serve as counsel to the Commission? Each district will have to determine who should serve as counsel to the TSC. The first step is dialogue with the school district solicitor. There is no conflict of interest in the solicitor serving as counsel to the TSC. Accordingly, if the solicitor is comfortable in this role, the solicitor is the logical choice. The bottom line is that both the TSC and the district need legal counsel knowledgeable about Act 1. If the solicitor does not have this knowledge, special counsel should be considered.**

- 2. If board declines slot money, don't we have to ask the voters whether they want us to accept or not? Yes, section 901 specifies that if a board declines the state funding from gaming, a referendum question will be put to the voters asking if they favor the district receiving state funds to reduce property taxes on qualified residential properties. If a majority approves the referendum, the district will receive their property tax reduction allocation beginning in the following fiscal year.**

- 3. There seem to be different interpretations regarding the method for calculating the homestead exclusion. Is the homestead exclusion a flat dollar amount for all taxpayers or is it based on the assessed value of the property? Act 50 dictates that the amount of homestead exclusion and property tax reduction will be the same flat dollar amount for all approved homesteads/farmsteads. Some lawyers have questioned the constitutionality of this provision, because the Constitution authorizes a homestead exclusion "*based on* the assessed value of homestead property." The argument is that a flat dollar amount is not *based on* the assessed value. The tax reduction amount will be a flat dollar amount absent a constitutional challenge.**

- 4. Do you place two questions on the May ballot if you want to raise the EIT and then convert it all to PIT? No, the statute directs districts to place one referendum question on the ballot. Referendum question section 331.2 (e) (iii) states "Do you favor converting the school district's current earned income tax to a personal income tax at x%? The revenue generated from the personal income tax will be used to reduce taxes on qualified residential property by (insert amount of reduction) and to replace the revenue from the school district's current earned income tax. The current earned income tax rate is Z%?"**

- 5. If citizens applied for the homestead exemption under Act 72 do they have to re-apply under Act 1? An application filed and approved under Act 72 is valid for Act 1 and need not be re-submitted.**

- 6. May the school board accept only a portion of the TSC's recommendation?
Yes**

**Tax Study Commissions under Act 1
August 3, 2006**

WEBCAST QUESTIONS

- 7. Are school districts required to annually ask the front-end referendum questions?** No, districts are only required to place a question on next spring's primary election ballot concerning adoption of a new or increased income tax to fund homestead and farmstead tax reductions, but any future EIT or conversion to a PIT will require a new front-end referendum.

- 8. Where would one find accurate age, income, employment and property use characteristics of tax base?** The PASBO website contains several links to good sources of data. You can access this information by going to the SS Act 1 Information and clicking on the Local Tax Study Commission resource page.
- 9. What if we can't find citizens who are interested in serving on the commission?** Act 1 provides no remedy for not being able to find individuals to serve on the TSC. It does though require all school boards to appoint a Local Tax Study Commission by Sept. 14, 2006, to make a nonbinding recommendation to the school board as it relates to the front-end referendum question. School boards can use advertisements, news releases, applications, and other such means to solicit potential members of the TSC.
- 10. How does the district estimate PIT? For example - How do we know what a taxpayer's income that is relative to PIT?** Data on the PIT is available from the PA Department of Education:
http://www.pde.state.pa.us/k12_finances/lib/k12_finances/pi_2004_web.xls See question 20 for a detailed explanation of incomes included in the PIT. Comparative data on the EIT and PIT is available on the PASBO website.
- 11. Does the selection process for the TSC members have to be public? Must the interviews, etc., be done in a public forum?** No, neither the selection process nor the interview process in the selection of the TSC need be open to the public. The school board should though make the Commission member appointments at a public meeting.
- 12. The School board does not have to accept the TSC's recommendation, right? Then why go through all this?** The statute, in section 331, states that the recommendation of the commission is nonbinding and that "the board of school directors shall accept or reject the recommendation of the local tax study commission prior to adopting a resolution." It is statutorily required that a school district go through this process and presumably this will provide helpful analysis from one point of view to the board as they make their decision.
- 13. How do you look at assessed vs. collected EIT and PIT?** If a school board makes the decision to place a referendum question regarding an addition to the EIT or a replacement PIT tax, the amount of the indicated percent should take into account the district's anticipated collection rates for the said tax to properly fund homestead and farmstead tax reductions.

**Tax Study Commissions under Act 1
August 3, 2006
WEBCAST QUESTIONS**

14. Is there a penalty if the Tax Study Commission is appointed by the school board in September but after the 14th? There is no penalty in the statute.

15. Does the school board have to appoint the commission by 9/14? Yes, Act 1 requires that a school board appoint a Tax Study Commission by Sept. 14, 2006. This means that a school board should appoint the TSC at an August or early September board meeting.

16. May the board appoint only 3 or 5 members to the commission by 9/14 and then appoint additional members later? The statute explicitly directs the board to appoint 5, 7, or 9 members to the commission by September 14th. An appointment of 3 members by the 14th with an assumption of appointments to follow would not meet the requirements of the statute. The composition of the commission should be set by the 14th.

17. May the school board mandate a recommendation in less than 90 days? The TSC must make a recommendation to the school board within 90 days, but a school board may not mandate a lesser period of time than the 90 days for the TSC to make its recommendation.

18. What if a member is appointed and does not participate or attend the meetings or is disruptive? Are there any repercussions for this member? There are no provisions in the statute for repercussions for this type of member.

19. Is Act 72 repealed? We are an Act 72 District. What of the .1% EIT increase that is already pending? Also, how do we deal with the median homestead exemption in multi-county districts? Act 1 repeals Act 72. The 0.1% increase in the Earned income and Net Profits Tax that participating districts had to enact in order to opt into Act 72 is repealed and cannot be levied or collected. All districts that participated in Act 72 are now bound by all the provisions of Act 1. More information on multi-county school districts will be forthcoming.

20. Explain the difference between EIT versus PIT. The earned income base is made up of taxable compensation combined with net profits. Taxable compensation is income from wages, salaries, tips or any other payment received for services rendered, yet it is reduced by business expenses (thus differentiating this category from gross compensation). Net profits is income, after expenses, from a business, profession, or farm. It includes profits from unincorporated businesses but excludes subchapter S profits allocated to a shareholder (beyond the salary of the shareholder) as long as the salary reflects fair compensation for services rendered. If a larger employer in a school district were to close, this would have a significant negative impact on total earned income revenue. The current personal income base incorporates 8 classes of

Tax Study Commissions under Act 1

August 3, 2006

WEBCAST QUESTIONS

income that are taxable. These include: compensation; interest; dividends; net profits from operation of a business, profession or farm; net gains or income from disposition of tangible or intangible property; net gains or income from rents, royalties, patents and copyrights; net gains or income derived through estates or trusts; and gambling or lottery winnings with the exception of PA State Lottery winnings won on or after July 21, 1983. This is a larger and broader base than the earned income tax base. Large downward fluctuations in the stock market would have a negative impact on PIT revenue. Local PIT will match the State PIT.

- 21. When will the higher EIT or PIT rate become effective and require collection?** Any tax approved by voters in May 2007 will go into effect July 1, 2007.
- 22. What will be the impact or ramifications of an ongoing County tax reassessment?** Reassessment should not affect the TSC recommendation or ultimate homestead tax reduction amount. Reassessment does impact the calculation of the homestead exclusion. Under § 327, the homestead exclusion must be adjusted upward in the initial year of reassessment.
- 23. The additional collection costs for EIT collection - may it be considered an offset to the funds provided for real estate tax reduction? If yes, what about the cost of homestead mailings and other costs not previously assessed to districts prior to Act 1? Yes, additional collection costs for EIT may be considered an offset if the school district employs an outside tax collector and the collection costs are deducted from the tax amounts received by the district, but the costs of homestead mailings and the like, may not be considered an offset and must be born by the district.**
-
- 24. What fiscal year should we use for the data needed to make the calculations for the tax study commission?** Information available from FY2005-06, should be used, however in instances where that is not available, the most up to date information from sources such as PDE or the Department of Revenue should be utilized.
- 25. Are retirees considered employees of the District for Act 1 Tax Study Commission purposes?** No, retirees are not employees of the district. Act 1 does not prohibit service by a retiree on the TSC if that retiree continues to receive benefits (i.e. health-care benefits) paid by the district. However, if you want to be ultra conservative you might decide not to appoint such retirees (or not to appoint multiple members who are retirees) to avoid any possible perceived issues of impropriety or conflict of interest.
- 26. Who is going to monitor the data's accuracy that the Commission will be using to make their decision?** There is no provision in the statute for any sort of external monitoring for commissions, but it does specify that the district will

Tax Study Commissions under Act 1

August 3, 2006

WEBCAST QUESTIONS

provide necessary and reasonable support staff to the commission so district administration could reasonably be involved in providing accurate data and analysis.

- 27. Did your 1999 Act 50 commission ask you for what they wanted or did you provide most based on what you thought they would want? Since Act 1 requires a focus on 4 mandatory study items (historic and present district revenue from current taxes; the percentage of total district revenues provided by current taxes; the age, income, employment and property use characteristics of the existing district tax base; and projected district revenue from current taxes, and from the possible new of additional Act 1 EIT or PIT), it would be wise if district employees acting as resource participants in the TSC would provide, review, and answer related questions on these referenced materials.**
- 28. When will we get clarification about the 1% open issue in order to inform our tax commission about what they will be deciding? On August 18, 2006, Secretary of Education, Gerald L. Zahorchak, issued a written opinion in which he stated that, "The existing EIT rate does not count toward that 1% increase." "For example, a school district that currently levies and collects 0.5% earned income tax may ask voters to increase the EIT by 1% (or perhaps more), to a total of 1.5%. In this case, 0.5% will continue to be used for school district operations and the additional 1% will be used to annually fund homestead and farmstead exclusions."**
- 29. Can the TSC recommend a 0% EIT** The TSC can recommend implementing a PIT instead of an EIT, and, that, in effect, would result in a 0% EIT, but the referendum question placed on the ballot by a school board must concern the adoption of a new or an increased income tax to fund homestead and farmstead tax reductions.
- 30. What if voters vote down the May 2007 referendum? If less than a majority of the electors voting on the question approve the referendum, then the new tax rates will not take effect and there will be no tax shift from local property tax to the EIT or PIT.**
- 31. Can the Board opt not to put the question of increasing the EIT or enact a PIT on the ballot? Every school board must submit at the May 2007 primary election a "front-end" voter referendum question concerning adoption of a new or increased income tax to fund homestead and farmstead tax reductions. There is an open legal issue concerning whether a district that already has an EIT rate of 1% or more may opt not to put a question on the ballot.**
- 32. When appointing the Local Tax Study Commission, may the board appoint members as chair, secretary, etc. or is the board required to rely upon the Commission to elect their own members to those positions? The**

**Tax Study Commissions under Act 1
August 3, 2006**

WEBCAST QUESTIONS

indication during the presentation was that it may not. Why not? The board can not appoint the officers of the Commission because the Commission is an independent entity with the right to conduct its affairs as it deems appropriate as long as it is not violating the statute. However, nothing prevents a school board from recommending action, and this may help jump start commission action if the board, either formally or informally, suggests someone to serve as chairperson.

33. All this still applies even if you do not currently have an EIT or PIT? Yes, Act 1 requires either an EIT or a PIT be proposed in those 38 districts that currently do not impose any income tax in order to fund homestead and farmstead tax reductions.

34. Will we use our estimated millage for 07-08 for our calculations? Yes

35. Would a district who has not enacted Act 24, still have the option of Act 24 available? In section 303, Act 1 explicitly retains the Act 24 option. Act 24 allows boards to eliminate the Occupational Assessment Tax and replace it with an increase in the Earned Income Tax (EIT) rate with voter approval. Act 24 does not allow for a shift from the Occupational Assessment Tax to the Personal Income Tax (PIT) and section 303 of Act 1 states "If a school district converts its earned income and net profits tax to a personal income tax under this chapter, the school district may not utilize the Optional Occupation Tax Elimination Act." However, with voter approval, a district can increase either the PIT or the EIT for any reason.