Analysis of HB 1776 and SB 1400 of 2012

September 25, 2012

INDEPENDENT FISCAL OFFICE

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The Independent Fiscal Office (IFO) provides revenue projections for use in the state budget process along with impartial and timely analysis of fiscal, economic and budgetary issues to assist Commonwealth residents and the General Assembly in their evaluation of policy decisions. In that capacity, the IFO will not support or oppose any policies it analyzes, and will disclose all methodologies, data sources and assumptions used in published reports and estimates.

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INDEPENDENT FISCAL OFFICE

Second Floor, Rachel Carson State Office Building
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Harrisburg, Pennsylvania 17105

September 25, 2012

To: The Honorable Kerry A. Benninghoff, The Honorable David G. Argall and The Honorable Judith L. Schwank

This report presents the results from an analysis of HB 1776 / SB 1400 of 2012 performed by the Independent Fiscal Office (IFO). The proposed legislation eliminates local school property taxes and replaces those funds with sales and use and income taxes, as well as monies redirected from the Property Tax Relief Fund.

This analysis has two primary objectives. First, it examines whether the new revenue sources are sufficient to replace the property taxes that the proposal eliminates. Second, it examines the general impact on school district funding levels relative to current law. The final section of the analysis contains a discussion of the legislation's potential impact on statutory tax incidence, a distributional analysis, the potential impact on home prices and a comparison of business tax rates for Pennsylvania and surrounding states. Three technical appendices provide additional detail to support this analysis.

Per the policy of the IFO, this report will be posted to the office website three days following transmittal. The IFO welcomes any questions, comments or suggestions regarding the content and methodology of this analysis.

Sincerely,

MATTHEW KNITTEL
Director

Executive Summary

This report provides an analysis of a proposal that replaces local school property taxes with state-funded distributions. The distributions would come from increases to certain state taxes and the redirection of other funds. For this analysis, the Independent Fiscal Office (IFO) identified two primary objectives: (1) determine if the proposed distributions would be sufficient to replace school property taxes that would have been levied; and (2) determine if additional revenues would be sufficient to fund the proposed distributions. The analysis also discusses potential economic and distributional impacts of the proposal.

The proposal has been introduced as two separate pieces of legislation (House Bill 1776, P.N. 3369 and Senate Bill 1400, P.N. 2123), and the bills are currently pending before the General Assembly. This analysis also considers amendments submitted by the sponsors of the legislation to the IFO. (An overview, along with a copy of each amendment, is included in Technical Appendix C.) The two bills are identical for the purpose of this analysis, and all references to "the proposal" include both pieces of legislation and the aforementioned amendments to those bills.

Overview of the Proposal

The proposal makes many changes to current law, but the components that relate to this fiscal analysis can be summarized as follows:

- The proposal repeals the ability of school districts to levy a property tax, except that districts may retain a property tax sufficient to service debt that was in existence on December 31, 2011.
- School districts would receive distributions from a new Education Stabilization Fund (ESF) in lieu of their ability to levy a property tax. The distributions would be based on FY 2012-13 property tax collections, less debt service and adjusted annually by a cost of living factor.
- Four revenue sources would fund the new ESF:
    - An expansion of the state sales and use tax base.
    - An increase in the state sales and use tax rate from 6 to 7 percent.
    - An increase in the state personal income tax from 3.07 to 4.01 percent.
    - A redirection of certain monies transmitted to school districts through the Property Tax Relief Fund and used for property tax relief.

Assumptions

Due to data limitations and various ambiguities in the proposal, the analysis incorporates many assumptions. Key assumptions are as follows:

- The additional revenues generated by the personal income tax rate increase, the sales and use tax rate increase and the sales and use tax base expansion are deposited into the new ESF. The General Fund is held harmless from the tax rate and base changes.

- The 0.947 percent transfer of sales and use tax revenues to the Public Transportation Assistance Fund is repealed, and it is replaced by a 1.01 percent transfer to a new Public Transportation Reserve Fund. The existing 4.4 percent transfer of sales and use tax revenues to the Public Transportation Trust Fund is maintained, and it applies to all revenues derived from the sales and use tax.
- The redirection of monies from the Property Tax Relief Fund is limited to funds that allow school districts to provide property tax relief to homeowners. Those monies are transferred to the ESF. The monies in the Property Tax Relief Fund that support the Property Tax / Rent Rebate Program, the supplemental senior citizen tax reduction program and Philadelphia wage tax relief remain in that fund.
- ESF distributions to school districts include the following:
    - The state property tax reduction allocations redirected from the Property Tax Relief Fund.
    - Annual adjustments to account for the retirement of existing debt and the resulting decline in property taxes levied to service that debt.
- The analysis starts with FY 2013-14 because it represents the first full fiscal year for the elimination of school property taxes and distributions from the ESF. It also represents the first full fiscal year for new tax revenues that support the ESF.

The technical appendix provides a more detailed description of the assumptions used in this analysis.

Summary of Results

The analysis finds that revenues provided by the proposal would be insufficient to replace the school property taxes it eliminates. The shortfall is $1.51 billion in FY 2013-14, growing to $2.02 billion in FY 2017-18. (See Tables 1 and 2.) The total shortfall can be decomposed into two parts:

- The revenue sources for the ESF would be insufficient to provide for the mandated distributions to school districts. This shortfall is $1.36 billion in FY 2013-14, declining to $0.87 billion in FY 2017-18.
- Distributions to school districts from the ESF would be insufficient to replace the school property taxes that are eliminated. This shortfall is $0.15 billion in FY 2013-14, growing to $1.15 billion in FY 2017-18.

Other results include the following:

- An analysis of the proposal's statutory tax incidence suggests a net decline of $2.27 billion for business entities and a net increase of $0.24 billion for non-business entities. (See Table 7.)
- A distributional analysis finds that retired homeowners would realize the largest relative tax cut and working age renters would realize the largest relative tax increase. (See Table 8.)
- The elimination of school property taxes will increase the market value of housing because a portion of current property taxes are capitalized into home prices. Based on available research, the analysis assumes that one-third of current property taxes are capitalized into home values. It

is likely that capitalization rates will vary substantially across the Commonwealth, with higher rates in more developed areas.

- The impact of the proposal on general business conditions is unclear. Although the elimination of property taxes clearly provides significant tax relief to businesses, some will pay more for certain inputs due to the higher sales and use tax rate. Owners and shareholders of pass through entities will face higher marginal tax rates on their business income. Finally, business entities will not realize the full benefit of the property tax cut due to reduced deductions for federal income tax purposes.
- Although it is possible that the proposal results in higher employment levels, the analysis does not attempt to quantify that effect. Certain businesses will realize reductions in operating costs through the elimination of property taxes, but others must attempt to pass higher prices forward to consumers in a competitive market (e.g., clothing retailers).
- The elimination of school property taxes would increase the federal tax liability of Pennsylvanians who itemize by approximately $550 million in FY 2013-14. Those amounts are not directly included in the analysis because they do not affect the revenue neutrality of the proposal.
- Secondary effects of the proposal include net gains in corporate net income tax revenues (due to the elimination of the school property tax deduction) and realty transfer tax revenues (due to higher home prices). The analysis projects those additional revenues would total $40-$80 million per year over the five-year window. Those amounts are not included in the analysis because they are not deposited into the ESF and do not affect the revenue neutrality of the proposal.

Table 1
Overview of Property Tax Replacement
(fiscal year, $ millions)

	2013-14	2014-15	2015-16	2016-17	2017-18
DEDICATED REVENUES					
Sales & Use Tax - Rate & Base Expansion	$5,211	$5,472	$5,751	$6,028	$6,302
Personal Income Tax - Rate Increase	3,361	3,543	3,716	3,886	4,049
Property Tax Relief Fund - Transfers	526	539	552	566	580
Subtotal of Dedicated Revenues	9,098	9,554	10,019	10,480	10,931
PROPERTY TAX REPLACEMENT					
Property Tax Forecast	12,678	13,184	13,704	14,103	14,497
Offset for Debt Service Payments	-2,071	-1,939	-1,807	-1,675	-1,543
Property Tax Replacement Baseline	10,607	11,245	11,897	12,428	12,954
NET ANNUAL IMPACT	**-1,509**	**-1,691**	**-1,878**	**-1,948**	**-2,023**

Table 2
Detail - Education Stabilization Fund (ESF) and School District Impact
(fiscal year, $ millions)

	2013-14	2014-15	2015-16	2016-17	2017-18
EDUCATION STABILIZATION FUND					
REVENUES					
Sales & Use Tax – Rate & Base Expansion	$5,211	$5,472	$5,751	$6,028	$6,302
Personal Income Tax - Rate Increase	3,361	3,543	3,716	3,886	4,049
Property Tax Relief Fund - Transfers	526	539	552	566	580
Subtotal of ESF Revenue	9,098	9,554	10,019	10,480	10,931
EXPENDITURES					
Distributions to School Districts	10,453	10,744	11,097	11,437	11,802
Revenues less Expenditures	-1,355	-1,190	-1,078	-957	-871
SCHOOL DISTRICT IMPACT					
PROPERTY TAX BASELINE					
Property Tax Forecast	12,678	13,184	13,704	14,103	14,497
Offset for Debt Service Payments	-2,071	-1,939	-1,807	-1,675	-1,543
Property Tax Replacement Baseline	10,607	11,245	11,897	12,428	12,954
REPLACEMENT FUNDING					
Distributions to School Districts	10,453	10,744	11,097	11,437	11,802
Surplus or Shortfall for Payments to School Districts	-154	-501	-800	-991	-1,152
SUMMARY					
ESF – Surplus or Shortfall	-1,355	-1,190	-1,078	-957	-871
School District Distributions – Surplus or Shortfall	-154	-501	-800	-991	-1,152
NET ANNUAL IMPACT	**-1,509**	**-1,691**	**-1,878**	**-1,948**	**-2,023**

Analysis of HB 1776 and SB 1400

This section of the analysis provides detail on the impact of HB 1776 / SB 1400 for three tax sources: sales and use, personal income and property taxes.[1] For each tax source, the text provides a brief description of (1) the provisions that affect tax revenues, (2) the general methodology and assumptions used to estimate revenue impacts and (3) any secondary revenue effects of the proposal. For the remainder of the text, the analysis refers to HB 1776 / SB 1400, as amended, as the "proposal."

The proposal makes substantive changes to the Pennsylvania tax code and could impact the long-term growth rate of the Pennsylvania economy. However, this analysis does not include macroeconomic "feedback" effects, such as the potential impact on long-term economic growth or employment levels. The analysis assumes that total after-tax consumption remains constant unless changes to tax law, such as the property tax cut, alter the amount of disposable income available. Due to this convention, an increase in sales tax revenues implies a corresponding reduction in business sales.

All revenue estimates include impacts on taxpayer behavior that result from changes to the tax code. The technical appendix discusses the behavioral assumptions used for this analysis. The analysis also includes ancillary or secondary effects from changes to tax law. Secondary effects occur when a change in one tax source has implications for another tax source. For example, the elimination of school property taxes increases disposable income and spending, so it will also increase sales tax revenues. When possible, the analysis separately itemizes these secondary effects. The text discusses secondary effects with the primary tax change that triggers them, but for revenue tables and tabulations, they are included with the revenue source that is affected. In this example, the text describes the positive effect that elimination of property taxes has on sales tax revenues, but that secondary effect will be included with other sales tax revenues in all tabulations.

To derive estimates of "baseline" (i.e., current law) revenues, the analysis uses the economic assumptions provided by IHS Global Insight for September 2012. The technical appendix lists the primary economic assumptions that drive baseline revenue projections.

The analysis uses a five-year budget window that extends through FY 2017-18. The five-year budget window serves two purposes. First, it displays results when the forecast assumes that the economy reverts to a "normal" rate of growth. The economic forecast used for this analysis assumes that the U.S. and Pennsylvania economies return to full output and employment levels by calendar year 2018. Second, the five-year budget window allows tax changes to become "fully phased in." For example, the analysis assumes that compliance rates for newly taxed goods and services will increase over time as taxpayers become aware of their new tax obligations. The Department of Revenue will need to educate taxpayers and hire support staff to process new taxpayers impacted by the sales tax base expansion.[2]

[1] Sales and use tax is commonly referred to as sales tax. Sales tax will be used throughout the remainder of this analysis.

[2] For FY 2013-14, the Department of Revenue estimates that 117,000 new sales tax licensees will need to register with the department. For the sales tax base expansion, the department projects that it will require an additional 31 staff. The projected cost for labor, mailings and computer programming is approximately $4 million.

The tables in this section provide further detail of the summary totals from the Executive Summary. Additional revenue detail may be found in the technical appendix.

Sales Tax Base Expansion and Rate Increase

Description

The proposal provides for the expansion of the sales tax base and an increase in the tax rate from 6 to 7 percent. All goods and services will be subject to tax unless specifically exempted. The new levy is effective January 1, 2013. The base expansion includes the following goods and services:

Goods

- All food and beverage items currently not taxable, except for items that qualify for the Women, Infants and Children (WIC) program (e.g., certain cereals, cheese, eggs, fruit, milk, bread), as well as any purchases made through the Supplemental Nutrition and Assistance Program (SNAP, formerly food stamps).
- All clothing, shoes and apparel that sell for more than $50 at retail.
- Various personal hygiene products such as toothpaste, toothbrushes, toilet paper, diapers, pre-moistened wipes and other miscellaneous products.
- Non-prescription drugs and medicines such as pain relievers, cold medicines, aspirins and antacids. Other sundry pharmaceutical items such as ice bags, gauze, slings, cough drops, contact lens solution, vitamins, diet supplements and pills are also taxed.[3] (Medical devices such as eyeglasses, hearing aids, wheelchairs, dentures, walkers and canes remain exempt.)
- Caskets, burial vaults and markers for gravesites.
- Textbooks purchased by individuals.
- All magazines not purchased at a retail establishment and all newspapers (includes electronic subscriptions).
- All candy and gum (includes sales made through vending machines).
- The sale of horses delivered out of state and horses used exclusively for commercial racing activities, as well as feed, bedding and grooming supplies for such horses.
- State and federal flags and direct mail order catalogs.

Services (excludes all business to business sales unless noted)

- Legal services (domestic relations and criminal matters remain exempt).
- Architectural, engineering and related.
- Accounting, auditing and bookkeeping.
- Specialized design and customized programming.
- Advertising and public relations.

[3] For a complete list of medical and pharmaceutical items that are currently not taxed, see the Department of Revenue's Retailer's Guide: http://www.revenue.state.pa.us/portal/server.pt/community/sales___use_tax/14702.

- Services to building and dwellings.
- Scientific, environmental and consulting.
- Information.
- Scientific research and development.
- Parking lot and garage services.
- Investment counseling and advice.
- Amusements and recreation (e.g., bowling, movies and professional sporting events).
- Waste management and remediation services (includes business).
- Towing services.
- Intrastate transportation of persons.
- Educational services (meals and activity fees only, excludes payments for tuition).
- Veterinarian services.
- Basic cable.
- Certain laundry (linens and industrial launderers).
- Funeral and cremation.
- Personal care (e.g., beauty parlors, barbers, nail care and diet centers).
- Nursing and residential care facilities.
- Social assistance (e.g., community housing and vocational rehabilitation).
- Day care services.

The technical appendix provides a brief description of the types of services included in these broad categories and itemizes the specific services that are assumed taxable or remain exempt under the proposal.

Other miscellaneous changes to sales tax law include: (1) a $300 annual cap on vendor discounts, (2) an alternative method retailers may use to remit sales tax, (3) the elimination of use tax on all telecommunication services (business and non-business) and (4) an expansion of the exemption for purchases made by certain educational entities (non-public schools, charter schools, cyber charter schools, vocational schools and supervisor and home education programs).

Revenue Impact

The analysis finds that the rate increase from 6 to 7 percent against the current tax base generates $1.53 billion in FY 2013-14 and $1.78 billion in FY 2017-18. (See Table 3.) Those amounts do not include transfers to the transportation funds, which reduce gross revenues by approximately $100 million per year. The analysis assumes that the tax increase is fully passed forward to consumers, and consumers would purchase fewer taxable items in response to higher tax rates. It also assumes a minor increase in non-compliance rates due to the higher tax rate. The technical appendix provides a discussion of those assumptions.

Following the rate increase, the analysis considers the revenue impact of the sales tax base expansion. The proposal provides that all goods and services will be taxed unless specifically exempted. Despite that broad language, there are certain instances where it is not clear which services should be included in the base expansion. Moreover, to determine which services to include in the base expansion, the analysis considered several factors such as: (1) the ability to administer the taxation of certain services by the Department of Revenue, (2) the ability of sellers to recharacterize sales to effectively escape taxation and (3) the provision of health services by non-profit vs. for-profit entities. These issues deserve special note because their treatment may not coincide with the intention of the bill's sponsors. More specifically:

- Intrastate transport of freight by a Pennsylvania company would be taxable because the proposal does not specifically exclude it. Due to administrability concerns, the analysis excludes those services from the base expansion.
- The proposal excludes "the sale at retail of tuition," but does not explicitly define tuition. The analysis excludes payments for any type of educational service. Hence, the exemption includes educational services not typically considered "tuition" such as instruction provided by business and secretarial schools, computer training, flight training, fine arts schools, sports and recreational instruction, exam preparation and automobile driving schools. If policymakers intend to tax those services, it might be necessary to specify explicitly that they do not qualify for the broad tuition exemption as firms might simply recharacterize fees as "tuition." [4]
- The proposal exempts tuition, but it does not exempt payments for board and activity fees. The analysis includes those payments in the base expansion, but excludes room charges because they resemble rental payments, which are exempt under the base expansion.
- The proposal exempts "the sale at retail of medical or dental services, including charges for office visits" and "the sale at retail or use of goods or services that are part of a Medicare Part B transaction." This exemption is too broadly defined to allow precise estimation of the health or social services that would be subject to tax under the base expansion. Following consultation with the Department of Revenue, the analysis includes all services for Home Health Care, Other Ambulatory Health Care, Nursing and Residential Care Facilities and Social Assistance (e.g., family services, relief services and day cares) in the base expansion. However, the analysis excludes services provided by tax-exempt or charitable entities. It should be stressed that the revenue estimate for this service category is very sensitive to this "bright line" distinction. In general, sales of goods and services by non-profit entities need not be excluded from the base expansion if the purchasing entity is also not exempt. The technical appendix provides further detail regarding the types of health and social services included in the base expansion.

The analysis projects that base expansion generates $3.58 billion in FY 2013-14 and $4.39 billion in FY 2017-18. (See Table 3.) Significant base expansion items include certain food items ($1.23 billion in FY 2013-14), recreation ($570 million), clothing over $50 ($418 million), non-prescription drugs ($126 million), certain health care and nursing services ($612 million). Two provisions reduce revenues: the residential and business exemption for telecommunication services (-$341 million) and an expanded exemption for purchases made by certain entities (-$37 million).

[4] The Economic Census for Pennsylvania reports that sales of these educational services by entities subject to federal income tax totaled $1.2 billion for 2007. A 7 percent tax rate implies potential revenues of roughly $85 million.

Table 3
Sales Tax: Rate Increase and Base Expansion
(fiscal year, $ millions)

	2013-14	2014-15	2015-16	2016-17	2017-18
Increase Rate From 6% to 7%	$1,533	$1,601	$1,664	$1,721	$1,776
Transfers	-83	-87	-90	-93	-96
Base Expansion at 7% Rate					
Goods					
Food – Excludes WIC Items	1,228	1,282	1,338	1,391	1,443
Food Exemption for SNAP	-118	-117	-117	-115	-113
Candy and Gum	92	96	100	105	110
Personal Hygiene Product	48	50	52	54	56
Newspapers and Magazines	33	33	34	35	36
Clothing and Footwear Over $50	418	439	463	487	514
Non-Prescription Drugs	126	131	137	143	148
All Other	49	51	54	56	59
Services					
Personal Services	235	246	258	270	283
Business Services	94	98	103	108	112
Exclude All Telecommunications	-341	-341	-341	-341	-341
Recreation	570	589	611	633	655
Health	612	651	698	748	797
Professional Services	378	395	414	434	453
Transportation and Storage	136	142	148	156	163
Waste Management and Remediation	89	93	97	102	107
Education	98	102	107	112	117
Miscellaneous Provisions					
Miscellaneous Goods and Services	12	13	14	14	15
Expand Exempt Entities	-37	-39	-41	-42	-44
Cap on Vendor Discounts	64	67	70	73	75
Transfers	-204	-215	-227	-239	-251
Sub-Total Base Expansion	3,580	3,766	3,972	4,183	4,394
Secondary Effects					
Personal Income Tax - Individuals	-147	-155	-163	-170	-175
Property Tax – Individuals	319	337	357	375	392
Property Tax – Federal Itemizers	-25	-26	-27	-29	-30
Property Tax – Pass Throughs	34	36	38	41	42
Total Sales Tax	**5,211**	**5,472**	**5,751**	**6,028**	**6,302**

Secondary Effects

Under the rate increase and base expansion, certain consumers will suspend or reduce their consumption of newly taxed items. Based on consumer response assumptions, the analysis projects a minor reduction in the quantity of newly taxed items purchased. As noted, the analysis assumes that total after-tax spending does not change if disposable income does not also change. Hence, the sales tax increase produces a reduction in business sales and profits and an offsetting impact on corporate and personal income tax revenues of approximately $10 million per year. The technical appendix provides further detail regarding the assumptions used to estimate these effects.

Municipal Impact

The expansion of the state sales tax base also expands the base for local sales tax. Allegheny County (1 percent) and Philadelphia (2 percent) are the only two political subdivisions that have a local sales tax. The table outlines the additional revenues that could be remitted due to the base expansion.

Impact of the Base Expansion on Local Sales Tax Collections
(fiscal year, $ millions)[1/]

Fiscal Year	Allegheny County	City of Philadelphia[2/]	Total
2013-14	$101	$148	$249
2014-15	105	77	182
2015-16	110	80	190
2016-17	115	84	199
2017-18	121	88	209

1/ Local sales tax revenues are excluded from all revenue tabulations in this analysis.

2/ Under section 1003 of the Municipal Pension Plan Funding Standard and Recovery Act (act of Dec. 18, 1984, P.L. 1005, No. 205), one percentage point of the current two percent Philadelphia sales tax rate will expire on July 1, 2014. This analysis incorporates the rate reduction into the estimates presented in this table.

Personal Income Tax Rate Increase

Description

The proposal increases the state personal income tax rate from 3.07 to 4.01 percent. The proposal does not alter any other provisions of the state personal income tax. It also stipulates that school districts may levy, assess and collect a local personal income or earned income tax for general purposes. Local units may specify the rate, which voters must approve by referendum. The proposal provides for tax forgiveness of the levy depending on the income level of residents.

Revenue Impact

Because the Commonwealth levies a flat personal income tax rate, the methodology for the rate increase is straightforward. The analysis increases the current law baseline by the percentage increase in the tax rate (0.94 / 3.07 or 30.6 percent). The analysis then assumes minor reductions in the number of hours

worked and the tax compliance rate due to the rate increase. The personal income tax rate increase generates $3.48 billion in FY 2013-14 and $4.19 billion in FY 2017-18.[5]

For eligible taxpayers, the tax forgiveness credit generally eliminates any tax increase. A similar result likely holds for most individuals claiming the non-resident credit as the Pennsylvania income tax rate remains lower than non-reciprocal states such as New York and Delaware.

If the income tax rate increases, "typical" overpayments by businesses and individuals would increase as well, thereby triggering higher refunds. The final estimate includes the increase in refunds that would be carried on the balance sheet. The technical appendix provides additional detail regarding the behavioral and modeling assumptions used for the personal income tax estimate.

Table 5
Current Versus Proposed Tax Law Personal Income Tax Remittances
(fiscal year, $ millions)

	2013-14	2014-15	2015-16	2016-17	2017-18
Current Law	11,540	12,128	12,717	13,296	13,853
Proposed Law	15,023	15,798	16,564	17,319	18,044
Change	3,483	3,670	3,847	4,023	4,191
Increase in Refunds	-142	-148	-153	-161	-167
Secondary Effects					
PIT – Pass Throughs	-5	-5	-6	-6	-6
Property – Pass Throughs	32	34	36	38	40
Sales – Business	-7	-8	-8	-8	-9
Total PIT	**3,361**	**3,543**	**3,716**	**3,886**	**4,049**

Secondary Effects

The higher income tax rate reduces disposable income and reduces purchases of taxable and non-taxable goods and services. The analysis assumes that 90 percent of the increase in personal income taxes would have been spent and 70 percent of that amount would have been spent on taxable goods under the sales tax base expansion.[6] This implies a secondary effect on sales tax (-$147 million) for FY 2013-14. Business sales and net income also decline, yielding another minor secondary effect (-$5 million) to income taxes.

[5] The analysis does not include the impact of personal income or earned income taxes that may be levied by school districts under the proposal.

[6] The 70 percent share assumption is based on an analysis of consumer spending patterns excluding outlays unlikely to be affected by changes in disposable income, such as mortgage and rent payments, utilities and basic food items. See the technical appendix for further discussion of this assumption.

School Property Tax Elimination and Related Provisions

Description

The proposal provides for the elimination of school property taxes and the replacement of those monies with state-funded distributions from a new Education Stabilization Fund (ESF). The following narrative describes this funding mechanism.

School Property Tax Elimination

The proposal repeals the authority of local school districts to levy, assess and collect any tax on real property for school purposes as of January 1, 2013. The proposal provides that no school district shall incur electoral debt, lease rental debt or non-electoral debt after that effective date. School districts must identify the dollar amount of outstanding debt as of December 31, 2011 and certify that amount with the Department of Revenue. School districts may continue to levy taxes on real property for the purpose of retiring certified debt. The analysis assumes that such taxes may be levied until the debt is fully retired.

Education Stabilization Fund

The proposal creates the ESF and identifies the following revenue sources:

- Revenues from the increase to the sales tax rate and base expansion.[7]
- Revenues from the increase to the personal income tax rate.[8]
- Revenue transferred to or received by the Property Tax Relief Fund under 4 Pa.C.S. Sections 1408(e) and 1409.
- Appropriations.
- Earnings from the fund.

Distributions to School Districts from the Education Stabilization Fund

The proposal requires the Pennsylvania Department of Education (PDE) to make quarterly distributions from the ESF to each school district based on a formula that uses the district's FY 2012-13 property tax collections as the base year.

The base year amount is adjusted by a cost of living factor and reduced by annual payments to service debt that was in existence on December 31, 2011. The cost of living factor is the lesser of the average annual percentage increase in the consumer price index (all urban consumers; PA, NJ, MD) for the preceding calendar year or the percentage increase in the sales tax collected for the previous calendar year.

[7] This analysis assumes that the sponsors intend to deposit the sales tax revenues received under current law into the General Fund and deposit new revenues from the rate increase and base expansion into the ESF. It is unclear whether the language in the proposal is sufficient to achieve this goal or whether the Department of Revenue could administer the provision as written.

[8] As noted in the discussion on the personal income tax, the rate increase will trigger higher refunds. This analysis assumes that the fiscal impact of a change in refunds caused by the rate increase will be reflected in the amounts deposited to the ESF. The legislation does not clearly specify the treatment of such refunds.

Revenue Impact

The analysis projects that $12.68 billion of school property taxes will be levied in FY 2013-14 under current law. Of that amount, $10.61 billion would be eliminated under the proposal. The remaining $2.07 billion would remain to service debt that was in existence on December 31, 2011 (see Table 6). The amount levied for debt service will decline as existing debt is retired. Hence, the school property tax replacement forecast (i.e., the difference between current law property taxes and the declining debt service on existing debt) grows at a rate that exceeds the growth rate of current law property taxes. The implications of that result are discussed later in this section.

Other revenue impacts discussed in this section include:

- The transfer of monies from the Property Tax Relief Fund to the ESF is projected to be $526 million in FY 2013-14.
- The revenue sources dedicated to the ESF are projected to be $9.10 billion in FY 2013-14, which is $1.36 billion less than distributions that would be made by the ESF. The shortfall declines to $0.87 billion for FY 2017-18.
- Distributions from the ESF to school districts would be $10.45 billion in FY 2013-14, which is $154 million less than current law property taxes. The shortfall grows sharply in succeeding fiscal years, reaching $1.15 billion by FY 2017-18.

School Property Tax Elimination

The bottom three lines of Table 6 display (1) the school property tax forecast, (2) the existing debt service forecast and (3) the differential. The differential represents school property taxes that would be eliminated under the proposal. Because those forecasts play a key role in determining whether the proposal is revenue neutral and the impact on school districts, the following discussion provides a detailed overview of the methodology used for those forecasts.

The data used for this analysis are from PDE. Fiscal year 2010-11 represents the most recent data on school district property tax collections. Later years are projections by the IFO. The most recent data for debt service is FY 2009-10. Later years are projections by the IFO.

The school property tax forecast uses provisions of the Taxpayer Relief Act, (hereafter referred to as "Act 1") as the underlying basis to project school property taxes.[9] Act 1 places an effective cap on the amount of revenue a school district may raise from increases to its millage rate.[10] Property tax projections based on the Act 1 cap are likely superior than projections based on historical patterns.[11] For example, average annual growth rates from the preceding five or ten years will likely overstate future property tax collections because those periods include years before the Act 1 provisions were effective or years in which growth permitted by Act 1 was relatively high due to large increases in certain inflationary factors.

The Act 1 provisions limiting school property taxes have two components: (1) an adjusted index for each school district that establishes percentage limits in the allowable millage rate increase; and (2) exceptions

[9] The act of Jun. 27, 2006, Special Session 1, P.L. 1873, No. 1, known as the Taxpayer Relief Act. See section 333 for the statutory provisions limiting the increases in millage rates of school property taxes.

[10] School districts may exceed the Act 1 limitations by seeking the approval of the voters at a referendum, but such occurrences have been very rare. This analysis does not incorporate the approval of referenda.

[11] See technical appendix for historical property tax collections data.

to the adjusted index that school districts may use to seek increases above the adjusted index. Exceptions are limited to certain prescribed circumstances, such as increases in pension costs. Based on the economic forecast and projections from the Department of Labor and Industry, the analysis projects that the Act 1 index will remain below the midpoint of its historical range over the forecast horizon.[12] The analysis assumes that the use of exceptions will increase due to modest increases in the index combined with sharply increasing employer contributions for public school employee pensions.

Some school districts have not increased property taxes to the level permitted by the Act 1 index and exceptions process. Therefore, the analysis incorporates utilization factors to account for such occurrences. Utilization factors initially increase due to pressures on school district budgets from certain costs (mainly pensions), modest increases in the base index, limited availability of federal and state funding and diminishing reserves as fund balances are drawn down. Towards the end of the forecast window, the analysis assumes utilization factors level off and slightly decline as pension costs reach a steady state growth rate.

Table 6
School District Property Tax Forecast
(fiscal year, $ millions)

	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
Property Tax - Prior Year	$11,950	$12,266	$12,678	$13,184	$13,704	$14,103
Revenue from Assessment Growth	72	74	76	79	82	85
Prior Year Adjusted for Growth	12,022	12,340	12,754	13,263	13,786	14,188
Act 1 Index Growth						
Aggregate Index Growth	228	234	319	345	358	383
Index Utilization Factor	65%	70%	75%	75%	70%	65%
Net Index Growth	148	164	239	259	251	249
Act 1 Exceptions						
Pension Exception	79	151	157	144	4	0
Special Ed Exception	66	67	69	71	73	75
Debt Exception	15	14	13	12	11	10
Exceptions Subtotal	160	232	239	227	88	85
Exceptions Utilization Factor	60%	75%	80%	80%	75%	70%
Net Exceptions	96	174	191	182	66	60
Total Act 1 Revenue Growth	244	338	430	441	317	309
Property Tax Forecast	12,266	12,678	13,184	13,704	14,103	14,497
Debt Service Forecast	-2,203	-2,071	-1,939	-1,807	-1,675	-1,543
Property Tax Subject to Replacement	**10,063**	**10,607**	**11,245**	**11,897**	**12,428**	**12,954**

[12] See technical appendix for the IFO's projections of the base index.

Table 6 provides a detailed outline of the methodology used to project current law property taxes and amounts eliminated by the proposal. A line-by-line description is as follows:

- *Prior Year Property Tax* - The value for prior year property tax is the forecast from the prior year without adjustment for debt service. For a discussion of the calculation of the FY 2011-12 estimate, see the technical appendix.
- *Revenue from Assessment Growth* - Assessment growth represents the underlying change in assessments, net of reductions. Assessment growth generates additional property tax revenues prior to any changes in millage rates. Growth in assessments can occur for many reasons, such as new construction, remodeling, reassessments or assessment challenges. Assessment reductions, resulting from appeals by property owners, reduce assessment growth. The analysis assumes that net assessment growth is 0.6 percent per annum.

Calculations relating to the Act 1 index and exceptions are integral to the school property tax forecast. The following points provide detail on the lines in Table 6 relating to Act 1 limitations.

- *Aggregate Index Growth* - The aggregate index growth is the amount by which total school property tax collections could increase assuming that each school district increases its property tax rates up to the maximum amount allowed under its Act 1 adjusted index. The Act 1 adjusted index for each district is determined by the base index with an adjustment for those districts in which the Market Value / Personal Income Aid Ratio is above 0.4. The following aggregate growth rates were calculated using a forecast of the adjusted index for each school district. The technical appendix contains additional detail regarding this adjustment.

2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
1.9%	1.9%	2.5%	2.6%	2.6%	2.7%

- *Index Utilization Factor* - Not all school districts increase millage rates to the maximum permitted by their Act 1 adjusted index. The index utilization factor makes an allowance for this fact by incorporating only a portion of the baseline growth into the property tax forecast. The forecast assumes the utilization factor increases over time as school district budget pressures increase due to pension contributions, federal and state funding constraints and diminishing fund balances. The utilization factor declines after the employer share of pension costs levels off.

- *Net Index Growth* - The net index growth is equal to the aggregate index growth multiplied by the index utilization factor.

- *Pension Exception* - Exceptions for pension contributions are expected to increase sharply in future years as employer contribution rates continue their steady increase. The forecast assumes the following employer rates as reported by the Public School Employees Retirement System (PSERS) actuarial evaluation for the fiscal year ending June 30, 2011. These rates will be revised when the next actuarial evaluation is completed in late 2012 or early 2013.

2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
12.36%	16.75%	21.25%	25.56%	26.26%	26.80%

For FY 2012-13, the forecast uses pension exceptions approved by PDE. For subsequent fiscal years, the IFO projected the pension exception based on projections of aggregate FY 2011-12

school district salaries, expected employer contribution rates, the adjusted Act 1 index for each school district and the estimated state reimbursement for pension payments.[13]

- *Special Education* and *Grandfathered Debt Exceptions* - For FY 2012-13, the forecast uses special education and grandfathered debt exceptions approved by PDE. For subsequent years, the special education exception is increased by the aggregate index growth rate and the grandfathered debt exception is reduced by 15 percent per annum.

- *Exceptions Utilization Factor* - For FY 2012-13, the utilization rate is set to generate net exceptions equal to the amount PDE estimated were used in FY 2011-12.[14] However, for subsequent fiscal years, the forecast assumes the rate will increase due to significant growth in pension contributions, federal and state funding constraints and diminishing fund balances.

- *Net Exceptions* - The dollar amount of exceptions is equal to the value of projected exceptions multiplied by the exceptions utilization factor.

- *Total Act 1 Revenue Growth* - This amount is equal to the sum of net index growth and net exceptions.

The bottom portion of Table 6 incorporates the preceding information to derive the projection of property tax that would be levied by school districts under current law. In addition, it projects the amount of property taxes that would be levied for debt service and calculates the total amount of property tax that would need replacement if school districts were held harmless under the proposal.

Education Stabilization Fund

The revenues dedicated to the ESF for distributions to school districts are projected to be $9.10 billion in FY 2013-14, increasing to $10.93 billion in FY 2017-18. These amounts fall short of the distributions to school districts provided under the proposal. For FY 2013-14 the shortfall is projected to be $1.36 billion, and it declines to $0.87 billion in FY 2017-18. The annual shortfall declines over time because the tax revenues supporting the ESF grow faster than distributions from the fund. The distributions from the ESF are discussed in more detail below.

Prior sections discuss the two primary sources of funding for the ESF, the sales tax and the personal income tax. The other major source of revenue is the transfer of monies from the Property Tax Relief Fund. The analysis assumes that the proposal redirects monies that are allocated to school districts for property tax relief. Funding for the Property Tax / Rent Rebate and supplemental senior citizen tax relief programs and Philadelphia resident and nonresident wage tax relief are assumed to be unchanged.

For FY 2012-13, PDE determined that school districts will receive $526 million for distribution to owners of homestead property as a credit against school property taxes. The analysis assumes that this amount

[13] The act of Jun. 30, 2011, P.L. 148, No. 25 provides that the pension exception shall be calculated using the salaries in the current year or FY 2011-12, whichever is less. This analysis assumes that the FY 2011-12 salaries are the lower of the two years.

[14] See page 7 of the Report on Referendum Exceptions for FY 2012-13, which is accessible at: http://www.portal.state.pa.us/portal/http://www.portal.state.pa.us:80/portal/server.pt/gateway/PTARGS_0_123706_1247785_0_0_18/SSAct1%20RefExcReport%202012-2013%20Apr12.pdf

remains constant in FY 2013-14, and then grows by 2.5 percent per annum in subsequent years. The program is supported by receipts from the 34 percent state tax on revenues from slot machines.

Distributions to School Districts from the ESF

The analysis projects that school districts would receive $10.45 billion from the ESF in FY 2013-14, which is $154 million less than the property taxes eliminated under the proposal (see Table 2). The discrepancy between projections of distributions and property tax elimination increases sharply over time because the cost of living allowance grows slower than current law school property taxes. The proposal specifies that the cost of living factor is equal to the lesser of the growth rate in the consumer price index (CPI) and sales tax revenues. The analysis finds that CPI growth will be the lesser of the two, and was therefore used to extrapolate mandated distributions. The projected growth rate in the CPI from the economic forecast is as follows:

2013-14	2014-15	2015-16	2016-17	2017-18
2.1%	1.3%	1.7%	1.6%	1.8%

The analysis makes three assumptions regarding distributions from the ESF:

- The proposal does not specify whether the FY 2012-13 base year includes the property tax reduction allocations received from the Property Tax Relief Fund. Those amounts are included for the purpose of the analysis.
- The annual reductions in school property tax collections for debt service (as debt is retired) are incorporated into the formula.
- For fiscal years after FY 2013-14, the cost of living adjustments will apply to the immediately preceding year, not to FY 2012-13, as suggested by a strict reading of the proposal.

Secondary Effects

Individuals

The elimination of school property taxes increases the disposable income of property taxpayers. The analysis assumes that 70 percent of the property tax cut goes to individuals. It further assumes that homeowners spend 90 percent of the increase in disposable income, 70 percent of which is spent on taxable items. Hence, the additional spending from the property tax cut increases sales taxes by roughly $319 million for FY 2013-14.

The elimination of property taxes and increase in the personal income tax rate also has direct implications for federal personal income taxes. For taxpayers who itemize on the federal return, the proposal will reduce deductions due to the fact that the lower reduction for property taxes is not offset by the higher deduction for state and local income taxes. Federal income tax data suggest that roughly 1.7 million residents could be affected. The analysis projects that the proposed changes will increase federal income tax liability for Pennsylvania itemizers by approximately $550 million for tax year 2014. The technical appendix provides further detail.

Finally, the reduction in disposable income from higher federal tax liability also triggers a reduction in spending. The analysis assumes that residents would have spent 90 percent of the federal tax increase, 70

percent of which is spent on taxable goods, so that sales tax revenues decline by roughly $25 million for FY 2013-14. Although federal tax liability increases under the proposal, the analysis does not include that impact in revenue estimates because it does not have direct implications regarding the revenue neutrality of the proposal.

Business Entities

The elimination of property taxes increases the pre-tax profits of business entities that remit property tax. Due to the reduced deduction for state and local property taxes, business income subject to federal and state personal and corporate income tax will increase for C corporations and pass through entities (partnerships, S corporations and sole proprietorships). The analysis assumes that (1) the business portion of the property tax cut (30 percent) is split evenly between C corporations and pass through entities, (2) those lower costs are partially offset by higher prices on certain business inputs under the sales tax rate increase (but not base expansion since businesses transactions are generally excluded) and (3) firms face an effective federal income tax rate of 25 percent.[15] For pass though entities, $1.3 billion of net tax cuts (FY 2013-14) flows directly through to individual partners, shareholders and owners as higher business income. As a result, the analysis projects that those individuals will remit roughly $32 million in additional personal income tax. For corporations, the analysis assumes that 42 percent of the $1.3 billion increase in net income is reported on the state corporate income tax return (due to apportionment) yielding a secondary impact of $32 million for FY 2013-14.

Once federal and state income taxes are paid, the income flows through to individuals as higher disposable income. For pass through entities, the analysis assumes that owners and shareholders spend 90 percent of the increase and 70 percent is spent on taxable goods and services, yielding another secondary effect of $34 million in increased sales taxes for FY 2013-14. For C corporations, the corresponding sales tax impact is much less clear since the firm need not pass through the higher after-tax profits as dividends. Moreover, a significant portion of the increase in after-tax profits would accrue to multistate firms and would likely leak from the state economy. For these reasons, the analysis does not attempt to compute a corresponding sales tax offset for C corporations.

Counties and Municipalities

The next section of this analysis discusses the potential impact of property tax elimination on home prices. In general, it is likely that the proposal will cause home prices to increase, and county and municipal governments would collect additional property tax revenues. This analysis does not attempt to quantify the potential magnitude of those additional revenues or the amount of time necessary for higher assessments to take effect.

Realty Transfer Taxes

The proposal should generally increase the market price of homes sold. The analysis assumes that home prices would increase by approximately 10 percent over several years, assuming a property tax capitalization rate of one-third (see next section). Once that effect is full phased in, the analysis projects an increase in realty transfer tax revenues of $25 to $35 million per year. Those revenues accrue to the General Fund and are not included in the analysis.

[15] Cline, Mikesell, Neubig, and Phillips (February 2005). "Sales Taxation of Business Inputs: Existing Tax Distortions and the Consequences of Extending The Sales Tax to Business Services." *State Tax Notes*.

Economic and Distributional Analysis

This section discusses potential economic and distributional implications due to the tax changes under the proposal. The analysis covers four topics: (1) the statutory tax incidence for business and non-business entities, (2) the impact on median homeowners and renters, (3) the general impact on housing prices and (4) potential implications for interstate business competitiveness. The analysis does not address the potential macroeconomic implications of the proposal. The net impact on the Commonwealth's economy is unclear because the benefits from the elimination of school property taxes are partially offset by higher sales and personal income taxes and higher tax liability due to the reduction in property tax deductions for federal income tax purposes.

Business and Non-Business Statutory Tax Incidence

In order to attribute the change in tax revenues to business and non-business entities, the analysis examines the statutory incidence of tax changes. The statutory incidence refers to the entity that has the legal obligation to remit tax. By contrast, the economic incidence refers to the entity that bears the true tax burden. For example, higher sales taxes might not be fully reflected in the final price of a good, despite the fact that the consumer pays a higher rate at the register. If firms cannot pass the tax forward to consumers, the higher tax rate could reduce profits or cause firms to respond through cost reduction efforts, such as lower employment. The tax could also be effectively exported to non-residents. In general, the economic burden of a tax change will depend on the market in which the good or service is sold (e.g., competitive or dominated by few firms), the responsiveness of consumers and the availability of acceptable alternatives.

For the analysis of statutory tax incidence, two points require emphasis. First, the statutory tax incidence need not be representative of the actual economic incidence for firms, consumers and even employees in newly taxed industries. The economic incidence could be very different than the statutory incidence. Second, the business and non-business distinction is artificial because firms cannot bear the incidence of a tax, only owners or shareholders can. Therefore, it might be more useful to view the results as a comparison of statutory tax incidence between business owners and non-business owners. Due to the inherent complexity of the computation, the analysis does not attempt to measure the economic incidence of tax changes under the proposal.

Table 7 attributes revenue impacts to business and non-business entities for sales, income and property taxes. The analysis counts all pass through entities as "businesses" despite the fact that business income is passed directly through to the owners, shareholders or partners of the firm. Farms and agricultural property are also counted as business entities. Finally, the analysis assumes that (1) firms do not bear any of the statutory incidence of the sales tax base expansion and (2) firms remit 39 percent of the sales tax rate increase.[16] (However, it is likely that much of that increase is ultimately passed forward to

[16] Two exceptions are noted. The expansion of the sales tax base to waste disposal and remediation services and dry cleaning services will impact businesses. However, those effects are largely offset by the elimination of tax on business telecommunication services. The business portion of those changes is included with the business portion of the statutory tax incidence. The cap on vendor discounts is also included with business incidence.

consumers.) The analysis does not include the projected increase in federal income taxes for individuals or businesses due to the elimination of local school property taxes.

Table 7
Change in Statutory Tax Incidence, FY 2013-14[1/]
($ millions)

	Total	Non-Business	Business
Sales Tax	$5,211	$4,624	$587
Income Tax	3,361	3,038	323
Property Tax	-10,607	-7,425	-3,182
Total Statutory Incidence	**-2,034**	**237**	**-2,272**

1/ Totals exclude $526 million in projected Property Tax Relief Fund transfers to the ESF for FY 2013-14.

Based on these assumptions, the analysis finds that most of the statutory sales tax incidence is borne by non-business entities. For personal income taxes, roughly ten percent of the statutory incidence is borne by business entities. That share is equal to the historical share of business income in the personal income tax base. Another ten percent of the personal income tax burden is borne by capital income such as capital gains, interest and dividends. The analysis includes those amounts with non-business entities. For property taxes, the analysis finds that 30 percent of the tax cut accrues to business entities.[17] The table assumes that businesses do not pass any tax relief through to renters.

Distributional Analysis: Impact of Proposal on Median Homeowners and Renters

Given the substantive tax changes made by the proposal, it is likely that relative tax burdens will change as well. To examine the impact on relative tax burdens, the analysis imposes the tax change on representative groups of Commonwealth residents. The distributional analysis considers four groups of taxpayers: working age homeowners and renters, and retired homeowners and renters. These groups reflect two fundamental characteristics that will drive changes to tax liability under the proposal: housing tenure and age. The proposal provides significant tax relief to all homeowners though the elimination of school property taxes. Age is an important factor due to its implications for income and spending patterns. Most income of retirees is pension and social security income that is exempt from the personal income tax increase. Data also suggest that spending patterns of older consumers are different than their younger counterparts. It is possible that diverse spending patterns imply a shift in relative tax burdens due to the sales tax base expansion.

The analysis compares taxes under current law and the proposal based on income levels and spending patterns for 2010. It uses data from the U.S. Census Bureau to establish median income levels for working age and retired residents based on housing tenure (i.e., homeowner or renter). Data from the Bureau of Labor Statistics' Consumer Expenditure Survey reveal spending patterns by age cohort and, in conjunction with IRS tax return tabulations for Pennsylvania, inform income composition and average levels of itemized deductions by income class.

[17] State Tax Equalization Board: 2011 Market Values and Assessment by Property Class, http://www.steb.state.pa.us/Default.asp.

The distributional analysis is highly stylized and actual outcomes could vary substantially from projected outcomes. Significant assumptions embedded in the analysis include the following: (1) the proposal immediately eliminates 63 to 73 percent of all property taxes, (2) median property tax is $3,000, (3) property taxes comprise roughly 10 percent of payments made by renters, and one-third of the property tax cut is passed through to renters (a rent reduction of 3.3 percent), (4) working age renters pay 28 percent of their income as rent while retirees pay 34 percent, (5) working age homeowners find it advantageous to itemize for federal income tax purposes, while other groups use the standard deduction, (6) all groups are married and file a joint tax return and (7) the working age homeowner and renter have two dependents. The technical appendix contains a more detailed discussion of these assumptions and the data sources upon which they were based.

Table 8 presents the relative change in taxes across the four age cohorts under two scenarios. The first scenario is the "fully phased in" scenario which assumes that all school property taxes have been eliminated (73 percent of total) and renters realize a reduction in rent as a portion of the property tax cut is passed through to them. The second scenario represents the "first year" where school property taxes only fall by 63 percent (non-debt portion) and no relief is passed through to renters.

A summary of results for the "fully phased in" scenario is as follows:

- Working age homeowners realize a tax cut (-7 percent). The analysis finds that the increase in federal income tax (though lower itemized deductions), state income tax and sales tax is more than offset by the reduction in property taxes.
- Retired homeowners realize a significant reduction in taxes (-38 percent). The analysis finds that the property tax reduction easily offsets any increase from higher sales tax. This group realizes a much larger tax cut due to the lack of taxable income at the state level and no increase in federal taxes.
- Working age renters realize a tax increase (+11 percent). The analysis finds that the increase to state income and sales tax exceeds the reduction in property taxes embedded in rental payments. That outcome is based on the assumption that one third of the property tax cut will be pushed forward to renters.
- Retired renters realize a tax increase (+8 percent). The increase in sales tax exceeds the assumed reduction in rental payments.

Relative results for the "first year" scenario are similar, but the benefits to retired homeowners are generally less while renters have a larger tax increase since no rental relief has been passed through. It should be noted that although the percentage increase in tax liability is high for renters, the percentage change appears large because tax liability under current law is relatively low in absolute terms.

These highly stylized examples are best used to compare relative outcomes under current and proposed law for a particular group. They are less useful to compare a projected dollar change in tax liability between two groups. For example, the analysis suggests that retired homeowners benefit relatively more compared to all other groups. Alternatively, all renters generally fare worse than homeowners under the proposal.

Table 8
Distributional Analysis: Homeowners and Renters

	Current Law				Proposed Law			
	Median Homeowner		Median Renter		Median Homeowner		Median Renter	
	Working	Retired	Working	Retired	Working	Retired	Working	Retired
Age Cohort	35-44	65-74	35-44	65-74	35-44	65-74	35-44	65-74
Wage Income	$70,000	$7,500	$32,500	$1,500	$70,000	$7,500	$32,500	$1,500
Social Security	0	16,000	0	13,000	0	16,000	0	13,000
Pension	0	11,500	0	5,500	0	11,500	0	5,500
Business and Capital Income	3,000	3,000	2,000	1,000	3,000	3,000	2,000	1,000
Total Income	**73,000**	**38,000**	**34,500**	**21,000**	**73,000**	**38,000**	**34,500**	**21,000**
Rental Payment	0	0	9,660	7,140	0	0	9,338	6,902
Federal Income Tax/1	3,575	300	0	0	3,785	300	0	0
State Income Tax	2,241	322	1,059	77	2,927	421	1,383	100
Local Income Tax	730	105	345	25	730	105	345	25
Local Property Tax	3,000	3,000	966	714	810	810	647	478
Income and Property Tax/2	**9,546**	**3,727**	**2,370**	**816**	**8,252**	**1,636**	**2,376**	**604**
Sales Taxes	742	580	354	467	1,315	1,058	637	778
Percentage Change, Total Taxes								
Fully-Phased In Scenario					**-7.0%**	**-37.5%**	**10.6%**	**7.7%**
First Year Scenario					**-4.6%**	**-30.8%**	**21.7%**	**25.2%**

1/ Uses federal tax law effective 2011.
2/ Payroll taxes and employee contributions to pension funds are considered non-taxed purchases of social security and pensions. This treatment is consistent with that used by the Consumer Expenditure Survey. Most wage earners have 7.65 percent of their pre-tax income withheld for Social Security. The characterization of those taxes as spending does not affect the general results of the analysis.

Property Taxes and Housing Prices

Economic theory suggests that asset prices should reflect the future stream of benefits that accrue to owners from holding the asset. For example, stock prices should reflect the present value of all future dividend payments, net of taxes. In a similar fashion, home prices should reflect the present value of future property taxes. If one assumes that the supply of land and homes is fixed (i.e., unable to be changed), then the present value of all future property taxes should be fully "capitalized" or built into the current market price of a home. For example, if the median home price is $180,000 and annual school property taxes equal $2,200, then the present value of those future property taxes is $55,000 (30.6 percent of the house price), assuming a real "discount" rate of 4 percent and an asset with infinite life.[18]

However, most studies generally find that property taxes are not fully capitalized into home prices and a consensus does not exist regarding the degree of capitalization. Most empirical estimates place the degree

[18] The discount rate is the rate used to convert future cash flows into present values.

of capitalization from 20 to 50 percent if a real discount rate of 4 percent is used.[19,20] A review of the empirical research suggests that a reasonable property tax capitalization rate might be one-third, assuming a discount rate of 4 percent. For 2014, the analysis assumes that the average amount of local school property taxes eliminated under the proposal will be $2,200. If one assumes a median home price of $180,000, a capitalization rate of one-third and a 4 percent discount rate, then the projected increase in the median home price from property tax repeal would be $18,300 (10.2 percent). To the extent that result occurs, it would take several years to manifest itself. The computation assumes that the level of services provided does not change. It also implicitly assumes that prospective homebuyers do not anticipate that property taxes would be levied again in the future. If they do, then the potential increase in home prices would be less as the housing market weighs that potential outcome.

Due to partial capitalization, the property tax cut produces a windfall gain for current homeowners. Capitalization rates will vary substantially across the state, so that homeowners might realize wide disparities in windfall gains. In general, capitalization rates will likely be higher in areas that are more developed, where there is little ability to expand the existing supply of homes. For those areas, more of the gains from the property tax cut will accrue to current homeowners. For areas that are less developed, prospective homebuyers would benefit too as the supply of housing expands and reduces prices that would have occurred in the absence of the proposal. Benefits would also accrue to home builders, home developers and other land owners who convert current land holdings into new housing plots. Finally, employment would increase in the construction sector as well. The increase would not be permanent since the proposal does not change the underlying demographics that ultimately drive the housing and rental markets.

While most current homeowners would be net winners under the proposal, the net impact on prospective homebuyers is unclear. In theory, even under full capitalization, prospective homebuyers would not be harmed by higher home prices because all future property taxes would be eliminated as well. However, they would still pay higher sales and income taxes. Therefore, the impact on prospective buyers depends on the current level of capitalization and the magnitude of the tax increase from higher sales and income taxes. Prospective buyers also need to consider the possibility that property taxes could be reintroduced. In that case, they would bear much of the incidence of the tax upon implementation.

The net impact of property tax elimination on renters is also inconclusive. Many researchers assume that the supply of rental units is "perfectly elastic" (more units can always be built), implying that landlords immediately pass all property taxes forward to renters, who bear the true burden of the tax. If true, then some portion of the property tax cut should flow through to renters as well. However, other empirical

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[19] Most research uses property tax differentials to explain observed differences in house prices. For example, see King, A. Thomas. 1977 "Estimating Property Tax Capitalization: A Critical Comment." *Journal of Political Economy*. 85(2): 425-31 and Guilfoyle, Jeffrey P. 1998. *The Incidence and Housing Market Effects of Michigan's 1994 School Finance Reforms*. Ph.D. dissertation, Michigan State University. Guilfoyle's findings seem most relevant for this analysis. The author examined prices for the homes sold in Michigan in 1992 and then resold in 1996. In 1994, Michigan reduced local school operating taxes from 34 to 6 mills for homestead property and largely replaced those revenues with a 2 percentage point increase in the sales tax rate and a 50 cent increase in cigarette taxes.

[20] Empirical results will be driven by data quality and various parameters that must be specified by researchers. Perhaps the most sensitive parameter that researchers must specify is the appropriate discount rate to use to derive the present value of future tax payments. There is no agreement on the proper rate to use for that computation. Most empirical research uses a real discount rate between 3 to 5 percent.

studies find that much of the current property tax is borne by landlords.[21] Due to the lack of any clear evidence, the analysis assumes similar benefits to renters and homeowners: renters capture one-third of the property tax cut benefit as the property tax portion of their rental payment (assumed to be 10 percent) falls by one-third. Any reduction in rental payments would require several years to fully manifest itself due to the lock-in effect from contracts and the long lead time required to construct new rental housing. The proposal would likely have a minimal impact on rental payments in the near term.

Potential Implications for Interstate Business Competitiveness

Similar to labor, utility and other operating expenses, property taxes represent a cost of "doing business." Firms will weigh those costs in their location and expansion decisions. Firms will also consider other taxes they must remit such as income, sales and franchise taxes.

Table 9 compares various taxes levied on business property, profits, purchases and capital stock for Pennsylvania and surrounding states. For property taxes, the table compares effective tax rates which represent the percentage of a property's full market value paid in property taxes during a given year. These effective property tax rates are representative of the rate for the largest city in each state and the median level of assessment data within a geographical area. Hence, effective tax rates are useful for broad comparisons and do not reflect the precise value of the tax burden on specific property. Other tax rates generally represent statutory maximums.

A comparison of tax rates reveals the following:

- Property taxes levied on real business property are somewhat higher for Pennsylvania than surrounding states. However, Pennsylvania does not levy property tax on personal business property.
- Pennsylvania levies a flat 9.99 percent rate on net corporate income and a flat 3.07 percent rate on the business profits of pass through entities. Although the corporate income tax rate is higher than all surrounding states, the top rate for pass through business income is lower and remains lower under the proposal.
- The current sales tax rate levied on certain business inputs is generally comparable to other states.
- Assuming complete phase-out of the Capital Stock and Franchise Tax, Pennsylvania is also similar to most surrounding states in that regard (see final column).

It should be noted that tax rates are only one factor that determine the amount of taxes remitted by business entities and their owners. Other relevant factors include applicable apportionment formulas, various state and local tax incentives and the ability to use current and past net operating loss deductions.

Because the proposal eliminates all school property taxes, it reduces business operating costs. A relevant question is the relative importance of property taxes in a typical firm's cost structure. To examine that issue, the IFO used federal corporate income tax data published by the IRS. On their corporate income tax return, firms report the various types of income they receive and itemize costs such as labor, rent,

[21] Carroll, R.J. and Yinger, J. (1994) "Is the Property Tax a Benefit Tax? The Case of Rental Housing," National Tax Journal 47, pp. 295–316). Available: http://ntj.tax.org.

advertising and taxes. Those data can be used to infer the relative size of property taxes for a typical corporation. It should be noted that this analysis is a broad generalization across all U.S. corporations that file tax returns, and results could vary considerably for specific firms in Pennsylvania.

Table 9
Effective Tax Rates

State	Property[4/]			Income[3/]		Sales Tax Rate (State Rate)[3/]	Franchise Tax Rate[4/]
	Commercial Structures	Industrial Structures	Commercial Equipment	Top Corporate Rate	Top Pass Through Rate		
Pennsylvania	4.12%	4.12%	0.00%	9.99%	3.07%	6.00%	0.29%
New Jersey	1.67%	1.67%	0.00%	9.00%	8.97%	7.00%	0.00%
New York	3.88%	3.88%	0.00%	7.10%	8.82%	4.00%	0.15%
Ohio	2.20%	2.22%	0.00%	0.26%[1/]	5.93%	5.50%	0.00%
West Virginia	1.67%	1.67%	1.67%	7.50%	6.50%	6.00%	0.48%
Maryland	2.02%	2.02%	5.67%	8.25%	5.50%	6.00%	0.00%
Delaware	0.87%	0.87%	0.00%	8.70%[2/]	6.75%	0.00%	0.01%
Connecticut	2.71%	2.71%	2.71%	7.50%	6.70%	6.35%	0.31%
Virginia	0.65%	0.65%	1.48%	6.00%	5.75%	5.00%	0.00%
North Carolina	1.08%	1.08%	1.30%	6.90%	7.75%	4.75%	0.15%

Sources: Ernst & Young LLP in conjunction with the Council on State Taxation (April 2011). "Competitiveness of State and Local Business taxes on New Investment." http://dublinecondev.com/pdf/Ohio%20Ranked%203.pdf; Property tax rates are originally from Minnesota Taxpayer's Association: 50-State Property Tax Comparison Study. Other rates from Federal Tax Administration.

1/ Between 2005 and 2010, Ohio phased in a commercial activities tax (CAT) at a rate of 0.26 percent. The tax is levied on business gross receipts, not on corporate profits.

2/ Delaware corporations that maintain and manage intangible investments of corporations, statutory trusts or business trusts may be exempt under Section 1902(b)(8), Title 30, Delaware Code.

3/ Tax rates for tax year 2012 as of January 1, 2012.

4/ Tax rates for calendar year 2009.

Based on the methodology discussed in the technical appendix, the data suggest that local property taxes might comprise roughly 0.4 to 0.9 percent of a firm's total business receipts or sales. The analysis finds that manufacturing firms might be in the mid to upper end of that range, while wholesalers and retailers are on the lower end. Firms that supply "professional, scientific and technical services" such as legal, accounting and architectural services appear on the very low end. The data also show that property taxes comprise a relatively constant share of total costs for small and large firms, regardless of industry.

Another relevant question is the impact of property tax elimination on taxes remitted by businesses. The tabulations from Table 10 suggest that property taxes might comprise roughly one-third of total taxes remitted by businesses to state and local governments. Pennsylvania appears similar to surrounding states in that regard (except Delaware). The elimination of school property taxes would significantly reduce the property tax share and would clearly increase the relative attractiveness of the Commonwealth for business location and expansion. However, some portion of the gain from elimination of property taxes would be offset if firms also pay higher sales tax on certain business inputs as the sales tax rate increases by one percentage point. The tax rate on pass through business income also increases by roughly one percentage point. Finally, businesses would not realize the entire gain from the property tax cut because those costs are deductible for federal income tax purposes. Federal tax data for C corporations show that

most firms that report significant deductions for taxes paid are fully taxable, suggesting an effective income tax rate close to the top statutory rate of 35 percent. If pass through entities are also included, then the average effective income tax rate might be closer to 25 percent for property tax deductions. If true, then roughly one quarter of the property tax cut is reduced through higher federal tax liability.

Table 10
Composition of State and Local Business Taxes By Type, FY 2010-11

State	Property Tax	Sales Tax	Excise and Gross Receipts	Corporate Income	Unemploy. Ins. Tax	Individual Income Tax	License and Other	Total Business Taxes
Pennsylvania	34.80%	14.30%	13.40%	7.80%	10.10%	6.60%	12.90%	100.00%
New Jersey	43.90%	14.60%	9.20%	10.20%	11.10%	5.40%	5.60%	100.00%
New York	35.90%	19.70%	10.60%	14.40%	4.80%	9.40%	5.10%	100.00%
Ohio	34.80%	20.70%	13.20%	3.60%	6.50%	6.20%	15.00%	100.00%
West Virginia	29.70%	9.60%	19.50%	8.40%	5.60%	5.10%	22.00%	100.00%
Maryland	24.50%	17.10%	19.20%	8.30%	9.50%	10.00%	11.40%	100.00%
Delaware	15.20%	0.00%	10.80%	14.90%	4.40%	5.10%	49.60%	100.00%
Connecticut	30.90%	21.70%	11.80%	9.10%	9.90%	11.40%	5.20%	100.00%
Virginia	45.20%	11.80%	15.90%	5.80%	4.10%	6.20%	11.10%	100.00%
North Carolina	29.60%	23.90%	14.60%	8.40%	6.80%	8.10%	8.60%	100.00%

Source: Ernst & Young LLP in conjunction with the Council on State Taxation (July 2012). "Total State and Local Business Taxes." http://www.ey.com/Publication/vwLUAssets/Total_state_and_local_business_taxes_report/$FILE/YY2718_50_State_Tax_Cost_Report.pdf

Due to these offsetting effects, it is difficult to project how the proposal might impact various business owners. Certain business owners, such as small service providers that are pass through entities with relatively little real property, could be worse off due to the higher income and sales tax rate. The same result would hold for owners of small C corporations who pay themselves a wage or dividends from net earnings. Conversely, a large manufacturing corporation with significant real property will likely benefit from the proposal and might expand operations. Furthermore, certain firms affected by the sales tax base expansion, such as clothing retailers, would need to push the 7 percent sales tax forward to consumers to preserve profit margins. If they are unable to do so, then profits would decline or cost cutting measures would become necessary.

It is also not known how much of the property tax cut for businesses would remain in the state. For FY 2013-14, the analysis projects that the business property tax cut would be $3.4 billion, assuming that 30 percent of the tax cut accrues to businesses. To the extent the tax cut flows through to the owners of pass through entities, much of that income will likely remain in the Commonwealth. However, the outcome for multistate corporations is less clear. Those firms could use the higher earnings to expand operations in the Commonwealth. Alternatively, the funds could be used for other purposes such as debt reduction or various needs in out-of-state establishments.

Summary

As noted in the previous section, revenues dedicated to property tax replacement fall short by approximately $1 billion per annum over the five-year window. To offset that shortfall, income or sales tax rates would need to be increased or the sales tax base expanded further. That outcome would not alter much of the general results of this section. Overall, current homeowners appear to gain from the proposal. The impact on renters is less clear, but most renters likely fare worse under the proposal.

Prospective homebuyers (current renters) might fare better or worse depending on their individual circumstances such as age, income composition (taxable versus non-taxable) and even location. Results will also hinge on the amount of relief passed through to renters from the property tax cut. Currently, existing research is not able to definitively address that issue.

A similar result holds for business entities. Certain firms will benefit and the property tax cut could act as an incentive to locate or expand operations in the Commonwealth. Owners of other firms could be adversely affected due to the modifications to sales and income taxes. Those factors seem especially relevant for small pass through entities with little real property, especially if sales or income tax rates are increased to achieve revenue neutrality.

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Technical Appendix A

The analysis uses the economic assumptions from IHS Global Insight forecast for September 2012. Relevant forecasts are as follows:

Economic Forecast

	Calendar Year Growth Rates or Levels						
	2012	2013	2014	2015	2016	2017	2018
Real Gross State Product	1.7%	1.6%	2.4%	2.8%	2.3%	2.0%	1.9%
CPI-U Philadelphia	2.1%	1.3%	1.7%	1.6%	1.8%	1.7%	1.8%
Nominal Wages	3.3%	3.7%	3.9%	4.4%	4.4%	4.1%	3.8%
Payroll Employment	0.7%	1.2%	1.4%	1.5%	1.5%	1.1%	0.7%
Unemployment Rate	7.6%	7.4%	7.0%	6.4%	5.9%	5.6%	5.4%

Data Sources and Methodology for Sales Tax Base Expansion

This section documents the data sources and methodologies used to estimate the revenue impact of the sales tax base expansion. Three primary data sources were used for that purpose: (1) U.S. Personal Consumption Expenditures (Table 2.4.5U in the National Income and Product Accounts, U.S. Bureau of Economic Analysis), (2) the annual Consumer Expenditure Survey (Northeast Region, U.S. Department of Labor) and (3) the 2007 Economic Census for Pennsylvania (U.S. Census Bureau).[22,23,24] Personal Consumption Expenditures details total spending on a broad array of goods and services purchased by U.S. consumers. The Consumer Expenditure Survey provides detail on average consumer expenditures for various good and services based on age, income level or region. The 2007 Economic Census for Pennsylvania provides detail regarding total business sales by industry for firms with establishments in the Commonwealth. To exclude business to business sales, estimates use data from the Input-Output tables from the U.S. Bureau of Economic Analysis. Finally, certain estimates also utilize industry specific data sources. Those instances are noted in the relevant sections.

Food

The estimate uses data from U.S. Personal Consumption Expenditures. The estimate apportions national data to Pennsylvania based on the Commonwealth's share of U.S. income. The exclusion for WIC items uses detail supplied by the Bureau of Economic Analysis (Table 2.4.5U – I-O, Personal Consumption Expenditures by Type of Product with 2002 Input-Output Commodity Composition) and miscellaneous product specific data. The exclusion for Supplemental Nutrition Assistance Program (SNAP, formerly known as food stamps) uses data from the Department of Agriculture regarding the dollar amount of SNAP benefits distributed to Pennsylvania. The projection of SNAP benefits uses the national forecast

[22] U.S. Personal Consumption Expenditures are available at: http://www.bea.gov/national/consumer_spending.htm.
[23] The Consumer Expenditure Survey can be found at: http://www.bls.gov/cex/home.htm.
[24] The 2007 Economic Census is available at: http://www.census.gov/econ/census07/.

from the Congressional Budget Office.[25] Due to the historically high level of current benefits, the exclusion for SNAP purchases declines over time.

Candy and Gum

The estimate uses data from U.S. Personal Consumption Expenditures, specifically the Sugar and Sweets category. The estimate apportions national data to Pennsylvania based on the Commonwealth's share of U.S. personal income.

Personal Hygiene Products

This category includes products such as toothbrushes, toothpaste, dental floss, disposable diapers, pre-moistened wipes, incontinence products, toilet paper and feminine hygiene products. The estimate assumes that four products comprise the great majority of these types of hygiene expenditures: disposable diapers, toothpaste, feminine hygiene products and toilet paper. For those items, the estimate uses an average annual cost multiplied by the relevant population that would use such products. For example, average annual diaper expenses for a baby or infant was multiplied by the resident population 0 - 2.5 years of age. A 25 percent gross up is then applied to account for all other items. Data sources used to inform this estimate are provided in the footnote.[26]

Newspapers and Magazines

The estimate uses data from the 2007 Economic Census for Pennsylvania (NAIC 511) and the Magazine Publishers of America. The estimate apportions newspaper subscriptions, periodical subscriptions and sales revenue to Pennsylvania based on the Commonwealth's share of U.S. personal income. Total periodical subscriptions and sales were reduced by 30 percent to account for the exclusion of single copy sales.

Clothing and Footwear

The estimate uses data from U.S. Personal Consumption Expenditures for the "clothing and footwear" category and data from the Connecticut Office of Fiscal Analysis (OFA). The estimate carves out items that sell at retail for less than $50 by applying a percentage derived from the OFA's annual report (and adjusted to Pennsylvania's median income) to total expenditures on clothing and footwear. The estimate further assumes a reduction in cross border clothing sales based on data supplied by the Pennsylvania Retailer's Association.

Non-Prescription Drugs

The estimate uses data from U.S. Personal Consumption Expenditures for the "non-prescription drugs" category. That category includes internal and respiratory over-the-counter drugs (e.g., pain relievers, cold medicine, antacids), vitamins, dietary supplements and aids, non-prescription medical equipment and sundry supplies. The estimate apportions national expenditures to Pennsylvania based on the Commonwealth's share of U.S. personal income.

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[25]See http://www.cbo.gov/publication/43072.

[26]See http://www.realdiaperassociation.org/diaperfacts.php
http://www.statista.com/statistics/192660/us-toothpaste-sales-via-different-sales-channels-in-2010-and-2011/
http://www.mooncupsandkeepers.com/article_cost.html
http://www.usatoday.com/money/advertising/2008-01-08-toilet-paper-marketing_N.htm.

Caskets and Burial Vaults
The estimate uses national average price data and cremation statistics from the National Funeral Directors Association as well as state demographic projections from IHS Global Insight.[27] The number of burials, found by multiplying the number of deaths in Pennsylvania by the percentage that are buried, was multiplied by the average cost of a casket and burial vault.

Textbooks
The estimate uses data from U.S. Personal Consumption Expenditures, specifically the "educational books" category, as well as data from the National Center for Education Statistics (Department of Education).[28] To derive Pennsylvania's share of the national expenditures on textbooks, the national number was multiplied by the Commonwealth's share of enrolled students in U.S. Post-Secondary Title IV Institutions. The average annual cost of textbooks per student in Pennsylvania was found by dividing total expenditures on textbooks in Pennsylvania by the number of post-secondary students in Pennsylvania. The average cost per student was then multiplied by the estimated number of post-secondary students who would purchase textbooks.

Personal Services
The estimate uses data from the 2007 Economic Census for Pennsylvania for the following categories: Linen and Uniform Supply (81233), Personal Care Services (8121) and Other Personal Services (8129) less Parking Lots and Garages (81293, computed separately). The estimate for Parking Lots and Garages (81293) is grossed up by 40 percent to account for receipts from government owned parking facilities, which are not included in the Economic Census. Additionally, ten percent of the receipts from Spectator Sports (7112) and Amusement, Gambling and Recreation (713) are added to this estimate to account for temporary parking from recreational activities.

The projection for Funeral and Cremation services is calculated by multiplying the average cost of a funeral or cremation by the projected number of decedents cremated or buried. The average cost of a funeral or cremation is from the National Funeral Directors Association. The number of deaths by method of disposition is from the Pennsylvania Department of Health. The share of decedents electing burial or cremation is based on actual burials and cremations for 2010. Those percentages are then applied to the Pennsylvania death forecast from IHS Global Insight to derive projections of the number of decedents cremated or buried. The projection is increased by five percent to account for pet cremation and burial services.

Business Services
The estimate uses data from the 2007 Economic Census for Advertising and Public Relations (5418), Other Services to Buildings and Dwellings (56179), Consultation (5416), Scientific Research and Development (5417), Information (519), Custom Programming and Data Processing (5415) and Administrative Services (561). The Administrative Services (561) sub-sector includes Office Administrative Services (5611), Facilities Support Services (5612), Telephone Call Centers (56142), Travel Arrangement and Reservation Services (5615), Investigation and Security Services (5616) and Other Support Services (5619). The estimate uses data from the Input-Output tables from the U.S. Bureau of Economic Analysis to exclude the business portion of total purchases.

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[27] See http://www.nfda.org/media-center/statisticsreports.html#fcosts.
[28] See http://nces.ed.gov/programs/digest/.

The projection for Information (519) is calculated by subtracting the product of the ratio of nonprofit to total establishments as provided in the United States Statistical Abstract and the Library and Archives (51912) subsector to control for the nonprofit exemption.

Recreation Services
The estimate uses data from the 2007 Economic Census for Spectator Sports (7112), Theater, Dance and Musical Arts (7111), Amusement and Gambling (713), and Museums, Historical Sites, Zoos and Parks (712). The estimate for Amusement and Gambling (713) includes Amusement Parks and Arcades (7131), Other Amusement and Recreation Industries (7139), Motion Picture Theaters (512131) and Drive-in Motion Picture Theaters (513132). The estimate reduces expenditures for Spectator Sports and Amusement and Gambling by 30 percent to exclude parking and concession receipts, which are included in total sales. The estimate for Museums, Historical Sites, Zoos and Parks (712) assumes that 25 percent of admission revenues are attributable to tax-exempt entities and are non-taxable. The figure for Dinner Theaters (7111103) within Performing Arts Companies (7111) was reduced to account for currently taxable food and beverage sales.

Basic Cable
An average annual basic cable rate was calculated using the average monthly basic rate obtained from Table 1142: Cable and Premium TV—Summary: 1980 to 2010 in the 2012 Statistical Abstract of the United States. The annual rate was then multiplied by the total number of occupied housing units and a share of total business establishments in Pennsylvania multiplied by an assumed cable saturation rate of 95 percent.

Electronic Media
The estimate uses data from the Recording Industry Association of America and the Association of American Publishers. This category includes eBooks and digital shipments/downloads of music. The estimate apportions national expenditures to Pennsylvania based on the Commonwealth's share of the U.S. income. The estimate applies a 40 percent nexus adjustment to reflect low use tax compliance rates.

Home Health Services
The estimate uses data from the 2007 Economic Census for Home Health Care Services (6216) and Other Ambulatory Health Care Services (6219). It excludes sales by tax-exempt entities and charities.

Nursing Services
The estimate uses data from the 2007 Economic Census for Nursing and Residential Care Facilities (623). It excludes sales by tax-exempt entities and charities.

Social Assistance Services
The estimate uses data from the 2007 Economic Census for Individual and Family Services (6241), Community Food and Housing, and Other Relief Services (6242) and Vocational Rehabilitation Services (6243). It excludes sales by tax-exempt entities and charities.

Day Care Services
The estimate uses data from the 2007 Economic Census for Child Day Care Services (6244). It excludes sales by tax-exempt entities and charities.

Certain Legal Services
The estimate uses data from the 2007 Economic Census for Pennsylvania for Legal Services (5411). The estimate excludes sales related to domestic relations and criminal matters.

Architecture & Engineering Services
The estimate uses data from the 2007 Economic Census for Architectural, Engineering and Related Services (5413).

Accounting & Auditing Services
The estimate uses data from the 2007 Economic Census for Accounting, Tax Preparation, Bookkeeping and Payroll Services (5412).

Specialized Design Services
The estimate uses data from the 2007 Economic Census for Specialized Design Services (5414).

All Other Professional Services
The estimate uses data from the 2007 Economic Census for Other Professional, Scientific and Technical Services (5419) less Veterinary Services (54194).

Veterinary Services
The estimate uses data from the 2007 U.S. Economic Census for Veterinary Services (54194).

Agents and Promoters
The estimate uses data from the 2007 Economic Census for Promoters of Performing Arts, Sports, and Similar Events (7113) and Agents and Managers for Artists, Athletes, Entertainers and Other Public Figures (7114).

Investment Advice
The estimate uses data from the 2007 Economic Census for Investment Advice (52393).

Transportation and Warehousing
Air, Rail, & Water Transportation - The estimate uses data from the 2007 Economic Census for Scheduled Air Transportation (4811), Rail Transportation (Amtrak FY 2011 Ridership), Deep Sea, Coastal, and Great Lakes Water Transportation (4831) and Inland Water Transportation (4832).

Transit & Ground Transportation - The estimate uses data from the 2007 Economic Census for Used Household and Office Goods Moving (48421), Urban Transit Systems (4851), Interurban and Rural Bus Transportation (4852), Taxi and Limousine Service (4853), Charter Bus Industry (4855) and Other Transit and Ground Passenger Transportation (4859).

Scenic & Sightseeing - The estimate uses data from the 2007 Economic Census for Scenic and Sightseeing Transportation (487).

Towing - The estimate uses data from the 2007 Economic Census for Motor Vehicle Towing (48841).

Waste Management
The estimate uses data from the 2007 Economic Census for Waste Management and Remediation Services (562). There is no business to business carve out for this industry.

Board & Activity Fees
The estimate uses data from the National Center for Education Statistics, the U.S. News and World Report and individual institutions. This category includes board and fees from institutions (Commonwealth System of Higher Education, Pennsylvania State System of Higher Education, private doctoral universities and private baccalaureate and master's institutions) that offer academic degrees. A 5 percent gross-up is applied to account for fees from other types of institutions (for profit, < two year, two year, etc.) The estimate uses data on average meal plan expenses, and the share of students who are full-time, part-time, undergraduate and graduate from Pennsylvania educational institutions. The estimate assumes that one-third of projected activity fees will be recharacterized as tuition.

Assumptions Used for Sales Tax Estimates

Sales Tax Compliance
The analysis assumes an implicit baseline sales tax compliance rate of 94 percent under current law. The few studies that examine state sales tax compliance find non-compliance rates of 2 to 12 percent for typical goods subject to sales tax. Tax compliance studies find that tax compliance is inversely related to tax rates. The estimate assumes that the tax compliance rate would fall by one-half percentage point in response to the higher rate.

For items newly taxed, the analysis uses one of two compliance rates depending on the good or service taxed: 85 or 93.5 (current law) percent. The lower compliance rate increases by one percentage point per year over five years as taxpayers become more familiar with their new tax obligations, and the Department of Revenue hires additional staff necessary to maintain adequate enforcement levels. The analysis applies the current law compliance rate to goods sold by firms that already have systems in place to collect and remit sales tax (e.g., certain food items). The lower compliance rate is used for services that will frequently be supplied by small firms (e.g., day care services, barbers, nail salons). Compliance research finds that such firms have much lower compliance rates compared to large firms that sell goods. For example, recent compliance studies by the IRS find that small sole proprietors underreported their business income by more than 50 percent for tax year 2006.[29]

Price Elasticities and Behavior
The analysis assumes that sales taxes are fully passed forward to final consumers, causing a reduction in quantity purchased. To derive that reduction, the analysis applies price elasticities to the computed pre-tax purchases to derive after-tax purchases. In theory, each newly taxed good or service will have a unique price elasticity. However, because the base expansion applies to a broad array of goods and services, the analysis uses a single "average" elasticity of 0.7, which generally represents an average level for most consumer expenditures. An example demonstrates the impact from applying price elasticities. Assume that 100 units of a good are sold at a pre-tax price of $10 that has a price elasticity of 0.7. If the new 7 percent tax is levied and fully passed forward to consumers, then the price increases to $10.70 and

[29] See http://www.irs.gov/pub/irs-news/tax_gap_figures.pdf.

the quantity demanded falls by 0.7 times 7 percent, or 4.9 percent. Total spending on the newly taxed good would fall by roughly the same percentage. However, the analysis also assumes that one-half of the reduction in expenditures shifts to goods that were already taxed (the relative price does not change), so that those purchases are still taxed. The other half shifts to non-taxed alternatives or possibly leaks from the state economy.

Nexus Issues

For many services that are taxed under the base expansion, it is unclear to whom the service will be delivered. The estimates for the base expansion to services use data from the 2007 Economic Census for Pennsylvania, which lists the total sales across industries. Sales figures include sales to out-of-state service recipients who would not be subject to tax under the base expansion. There are no data regarding the share of those sales. The analysis applies a ten percent reduction to all service estimates to eliminate non-taxability due to nexus issues.

Sales Tax Base Expansion Detail
(fiscal year, $ millions)

	2013-14	2014-15	2015-16	2016-17	2017-18
Goods					
Food - Excluding WIC Purchases	$1,228	$1,282	$1,338	$1,391	$1,443
Food Exemption for SNAP	-118	-117	-117	-115	-113
Candy and Gum	92	96	100	105	110
Personal Hygiene	48	50	52	54	56
Newspapers and Magazines	33	33	34	35	36
Clothing and Footwear Over $50	418	439	463	487	514
Non-Prescription Drugs	126	131	137	143	148
Caskets and Burial Vaults	18	19	19	20	21
Textbooks	28	29	31	32	34
Flags and Catalogs	3	3	3	4	4
Services					
Personal					
Dry Cleaning and Laundry	35	37	39	40	42
Personal Care	86	90	94	99	103
Funeral Parlor and Cremation	28	29	30	32	33
Other Personal (haircut, diet)	18	18	19	20	21
Parking Lots and Garages	69	72	75	79	83
Business					
Advertising and Public Relations	1	1	1	1	1
Maintenance Services for Buildings/Homes	12	13	13	14	14
Consulting	0	0	0	0	0
Scientific Research	21	22	23	25	26
Information	12	13	13	14	15
Administrative	47	49	52	54	57
Exempt All Telecommunications	-341	-341	-341	-341	-341
Recreation					
Spectator Sports Admissions	108	112	118	123	129
Theater, Dance, Music, Arts	25	27	28	29	30
Amusement and Gambling	146	153	160	168	176
Museums, Zoos and Parks	36	37	39	41	43
Basic Cable	246	250	254	259	263
Electronic Media	9	10	12	13	13
Health Services (excludes sales by non-profits)					
Home Health Care	159	169	182	195	208
Nursing	357	381	409	439	469
Social Assistance	44	47	51	55	58
Day Care	51	53	56	59	61
Professional					
Legal	131	137	143	150	157
Architecture and Engineering	0	0	0	0	0
Accounting, Auditing and Design	36	38	40	42	44
All Other Professional Services	103	108	113	119	124
Veterinary Fees	64	66	70	73	76
Investment Services	19	20	21	22	23
Agents and Promoters	24	25	27	28	29
Transportation					
Air, Rail and Water Transport	85	89	93	97	102
Transit and Ground Passenger	39	41	43	45	47
Scenic and Sightseeing	4	4	4	4	4
Towing	8	8	9	9	10
Waste Management and Remediation	89	93	97	102	107

	2013-14	2014-15	2015-16	2016-17	2017-18
Education - Meals and Activity Fees	98	102	107	112	117
Miscellaneous Items					
Various Provisions	6	7	7	7	8
Investment in Metal Bullion and Coins	6	6	7	7	7
Expansion of Exempt Entities	-37	-39	-41	-42	-44
Cap on Vendor Discounts	64	67	70	73	75

Itemization of New Taxable Services from HB 1776

NAICs Code					
Sector	Subsector	Industry	Description	Newly Taxable?	Notes
48-49			**Transportation and Warehousing**		
	481		Air Transportation	yes	1
		4811	Scheduled Air Transportation	yes	1
		4812	Nonscheduled Air Transportation	yes	1
	482		Rail Transportation	yes	1
	483		Water Transportation	yes	1
		4831	Deep Sea, Coastal, and Great Lakes Water Transportation	yes	1
		4832	Inland Water Transportation	yes	1
	484		Truck Transportation		
		4841	General Freight Trucking		
		4842	Specialized Freight Trucking		
	485		Transit and Ground Passenger Transportation	yes	1
		4851	Urban Transit Systems	yes	1
		4852	Interurban and Rural Bus Transportation	yes	1
		4853	Taxi and Limousine Service	yes	1
		4854	School and Employee Bus Transportation		
		4855	Charter Bus Industry	yes	1
		4859	Other Transit and Ground Passenger Transportation	partial	
	486		Pipeline Transportation		
		4861	Pipeline Transportation of Crude Oil		
		4862	Pipeline Transportation of Natural Gas		
		4869	Other Pipeline Transportation		
	487		Scenic and Sightseeing Transportation		
		4871	Scenic and Sightseeing Transportation, Land	yes	
		4872	Scenic and Sightseeing Transportation, Water	yes	
		4879	Scenic and Sightseeing Transportation, Other	yes	
	488		Support Activities for Transportation		
		4881	Support Activities for Air Transportation		
		4882	Support Activities for Rail Transportation		
		4883	Support Activities for Water Transportation		
		4884	Support Activities for Road Transportation	partial	2
		4885	Freight Transportation Arrangement		
		4889	Other Support Activities for Transportation		
	491		Postal Service		
	492		Couriers and Messengers		
		4921	Couriers and Express Delivery Services		
		4922	Local Messengers and Local Delivery		
	493		Warehousing and Storage		3
51			**Information**		4
	511		Publishing Industries (except Internet)		

NAICs Code				Newly	
Sector	Subsector	Industry	Description	Taxable?	Notes
		5111	Newspaper, Periodical, Book, and Directory Publishers	yes	5
		5112	Software Publishers	yes	
	512		Motion Picture and Sound Recording Industries		
		5121	Motion Picture and Video Industries	partial	6
		5122	Sound Recording Industries		
	515		Broadcasting (except Internet)		
		5151	Radio and Television Broadcasting		
		5152	Cable and Other Subscription Programming	partial	7
	517		Telecommunications		
		5171	Wired Telecommunications Carriers	yes	8
		5172	Wireless Telecommunications Carriers (except Satellite)	yes	8
		5174	Satellite Telecommunications	yes	8
	518		Data Processing, Hosting, and Related Services		
	519		Other Information Services	yes	9
52			**Finance and Insurance**		
	521		Monetary Authorities-Central Bank		
	522		Credit Intermediation and Related Activities		
		5221	Depository Credit Intermediation		
		5222	Non-depository Credit Intermediation		
		5223	Activities Related to Credit Intermediation		
	523		Securities, Commodity Contracts, and Other		
		5231	Securities, Commodity Contracts and Brokerage		
		5232	Securities and Commodity Exchanges		
		5239	Other Financial Investment Activities	partial	10
	524		Insurance Carriers and Related Activities		
		5241	Insurance Carriers		
		5242	Agencies, Brokerages, and Other Insurance Related Activities		
	525		Funds, Trusts, and Other Financial Vehicles		
		5251	Insurance and Employee Benefit Funds		
		5259	Other Investment Pools and Funds		
53			**Real Estate and Rental and Leasing**		
	531		Real Estate		
		5311	Lessors of Real Estate		
		5312	Offices of Real Estate Agents and Brokers		
		5313	Activities Related to Real Estate		
	532		Rental and Leasing Services		
		5321	Automotive Equipment Rental and Leasing		
		5322	Consumer Goods Rental		
		5323	General Rental Centers		
		5324	Commercial and Industrial Machinery and Equipment Rental		
	533		Lessors of Nonfinancial Intangible Assets		
54			**Professional, Scientific, and Technical Services**		4
	541		Professional, Scientific, and Technical Services		
		5411	Legal Services	partial	
		5412	Accounting, Tax Preparation, Bookkeeping, and Payroll Services	yes	
		5413	Architectural, Engineering, and Related Services	yes	
		5414	Specialized Design Services	yes	
		5415	Computer Systems Design and Related Services	yes	
		5416	Management, Scientific, and Technical Consulting Services	yes	

NAICs Code				Newly	
Sector	Subsector	Industry	Description	Taxable?	Notes
		5417	Scientific Research and Development Services	yes	
		5418	Advertising, Public Relations, and Related Services	yes	
		5419	Other Professional, Scientific, and Technical Services	yes	
55			**Management of Companies and Enterprises**		11
56			**Administrative and Support and Waste Management**		
	561		Administrative and Support Services		
		5611	Office Administrative Services	yes	12
		5612	Facilities Support Services	yes	13
		5613	Employment Services		14
		5614	Business Support Services	partial	14
		5615	Travel Arrangement and Reservation Services	yes	12
		5616	Investigation and Security Services	yes	12
		5617	Services to Buildings and Dwellings	partial	14
		5619	Other Support Services	yes	12
	562		Waste Management and Remediation Services	yes	15
		5621	Waste Collection	yes	
		5622	Waste Treatment and Disposal	yes	
		5629	Remediation and Other Waste Management Services	yes	
61			**Educational Services**		
	611		Educational Services		
		6111	Elementary and Secondary Schools		
		6112	Junior Colleges	partial	16
		6113	Colleges, Universities, and Professional Schools	partial	16
		6114	Business Schools and Computer and Management Training		
		6115	Technical and Trade Schools		
		6116	Other Schools and Instruction		
		6117	Educational Support Services		
62			**Health Care and Social Assistance**		
	621		Ambulatory Health Care Services		
		6211	Offices of Physicians		
		6212	Offices of Dentists		
		6213	Offices of Other Health Practitioners		
		6214	Outpatient Care Centers		
		6215	Medical and Diagnostic Laboratories		
		6216	Home Health Care Services	yes	17
		6219	Other Ambulatory Health Care Services	yes	17
	622		Hospitals		
		6221	General Medical and Surgical Hospitals		
		6222	Psychiatric and Substance Abuse Hospitals		
		6223	Specialty (except Psychiatric and Substance Abuse) Hospitals		
	623		Nursing and Residential Care Facilities	yes	18
		6231	Nursing Care Facilities (Skilled Nursing Facilities)	yes	18
		6232	Dev. Disability, Mental Health, and Substance Abuse Facilities	yes	18
		6233	Retirement Communities and Assisted Living Facilities for Elderly	yes	18
		6239	Other Residential Care Facilities	yes	18
	624		Social Assistance	yes	18
		6241	Individual and Family Services	yes	18
		6242	Community Food and Housing, and Other Relief Services	yes	18

NAICs Code				Newly	
Sector	Subsector	Industry	Description	Taxable?	Notes
		6243	Vocational Rehabilitation Services	yes	18
		6244	Child Day Care Services	yes	18
71			**Arts, Entertainment, and Recreation**		
	711		Performing Arts, Spectator Sports, and Related Industries		
		7111	Performing Arts Companies	partial	19
		7112	Spectator Sports	yes	
		7113	Promoters of Performing Arts, Sports, and Similar Events	yes	12
		7114	Agents and Managers for Artists, Athletes, Entertainers	yes	12
		7115	Independent Artists, Writers, and Performers		
	712		Museums, Historical Sites, and Similar Institutions	yes	
	713		Amusement, Gambling, and Recreation Industries		
		7131	Amusement Parks and Arcades	yes	
		7132	Gambling Industries		
		7139	Other Amusement and Recreation Industries	yes	20
72			**Accommodation and Food Services**		14
81			**Other Services (except Public Administration)**		
	811		Repair and Maintenance		14
		8111	Automotive Repair and Maintenance		
		8112	Electronic and Precision Equipment Repair and Maintenance		
		8113	Commercial and Industrial Machinery and Equipment Repair		
		8114	Personal and Household Goods Repair and Maintenance		
	812		Personal and Laundry Services		
		8121	Personal Care Services	yes	
		8122	Death Care Services	yes	21
		8123	Dry Cleaning and Laundry Services	partial	22
		8129	Other Personal Services	yes	

Notes:

1. intrastate transport only, persons only
2. vehicle towing services only
3. Assumed nontaxable due to administrability concerns
4. exclude all business to business services
5. all newspaper and magazine subscriptions
6. movie theaters included with amusements
7. basic cable service only
8. exclude all telecommunications service
9. excludes business to business and non-profit
10. investment advice and counseling
11. generally bank holding companies
12. business to business carve out for sub-sector
13. much provided to exempt gov't entities
14. generally taxed under current law
15. no business to business carve out for sub-sector
16. non-tuition fees and meal plans
17. for profit entities only
18. for profit entities only
19. carve-out for dinner theaters
20. drive-ins and motion picture theatres moved here
21. micro data used
22. includes linens and uniforms

Data Sources and Methodology for Increase in Personal Income Tax (PIT)

The model used to project baseline PIT revenues (i.e., revenues under current law) uses the economic forecast from IHS Global Insight for September 2012. The proposal increases the PIT rate from 3.07 to 4.01 percent. The PIT revenue estimate assumes that the tax forgiveness and resident tax credits increase proportionally with the tax rate (0.94/3.07 x 100 = 30.6%), thereby offsetting any additional tax for residents claiming those credits under current law. The tax forgiveness credit is a credit granted to low income residents. The credit refunds a specified percentage of taxes (10 percent - 100 percent) depending on the taxpayer's income and family size. The resident tax credit is a credit for residents who work in

non-reciprocal states and pay taxes in those states. To prevent individuals from paying state taxes twice (once to the state they work in and once to Pennsylvania), residents working in non-reciprocal states may claim a tax credit for taxes paid to the other state.

The final revenue estimate for the increase in PIT revenues including behavioral adjustments is a response to the higher tax rate. Research by the Congressional Budget Office suggests that the wage elasticity for an average worker is 0.129.[30] That figure implies that a one percentage point decline in after-tax wage income would reduce the number of hours worked by 0.129 percent. The model assumes that after-tax wage income is 78 percent of gross wages. Hence, the revenue estimate for the PIT rate increase was reduced by 0.155 percent (0.94/78 times 0.129) to reflect the reduced incentives to work from higher tax rates.[31] This adjustment reduced revenues from the rate increase by $18.9 million for FY 2013-14.

The estimate also includes an adjustment for higher non-compliance under the tax rate increase. Research shows a positive relation between non-compliance and tax rates. The model assumes an underlying PIT compliance rate of 95 percent that declines to 94.75 percent under the proposal. Hence, the entire PIT baseline falls by 0.26 percent (.25/95) in response to the 31 percent increase in tax rate, or $40 million for FY 2013-14.

The PIT rate increase also affects refunds paid to individuals and businesses. Those refunds do not affect General Fund revenues, but are tracked separately on the balance sheet and are an "expense" for the Commonwealth. The analysis assumes that PIT refunds increase by two-thirds of the percentage increase in PIT remittances. This approach assumes that individuals and firms increase their "normal" PIT overpayments (which are built into the rate increase estimate) in response to the rate increase. However, refunds would increase by less than the percentage increase in remittances as individuals and firms become increasingly sensitive to the large cash flow impact implied by higher levels of overpayments.

Methodology for School Property Tax Elimination and Related Provisions

FY 2011-12 Collections

Actual revenue collections for FY 2011-12 have not been reported by the Pennsylvania Department of Education (PDE), but the millage rates levied by the school districts for that year are available. The forecast was derived by applying the growth rate in the millage for each school district in FY 2011-12 to that district's actual FY 2010-11 collections as reported by PDE. Additional calculations were performed for multi-county school districts to derive a weighted average growth rate based on the percentage of property within each portion of the district. Due to the implementation of countywide reassessments, growth rates for districts located in Adams, Cumberland and Perry counties were derived from information supplied by those districts. The values were summed for each district to determine the aggregate collections.

The base year amount also includes $526 million in property taxes levied by the school districts and paid to the districts through state property tax relief allocations from the Property Tax Relief Fund.

[30] Congressional Budget Office. "The Effect of Tax Changes on Labor Supply in CBO's Microsimulation Tax Model." April 2007. http://www.cbo.gov/publication/18554.

[31] This reduction was only taken on the employee withholding (i.e., earned compensation) part of PIT.

Assessment Growth Rate

The 0.6 percent net growth in assessments primarily represents the underlying growth from new construction. The Independent Fiscal Office (IFO) examined school district data on interim property tax assessments in an attempt to determine the level of such growth. However, the data were determined to be unreliable due to inconsistencies between counties in their treatment of new construction and the differences in reporting by school districts.

The alternate method used by the IFO looked at millage rate increases in the 350 single-county districts that did not implement a reassessment between FY 2005-06 and FY 2010-11. This method isolates the aggregate amount of property tax collections for those districts that could not be explained by millage rate increases. The difference between the projected and actual collections using this method was attributed to underlying assessment growth. The 0.6 percent estimate equals the lowest percentage for the period studied. In the periods immediately preceding the recession, the methodology suggests a rate between 1.5 and 2.0 percent.

Aggregate Index Growth

The amount of index growth is determined by applying the adjusted Act 1 index for each school district to school district's prior year collections.[32] The values are summed and the overall percentage growth rate is determined. It is essentially an average of the adjusted Act 1 index for all districts, weighted by property tax collections. The forecasts for the components of the adjusted Act 1 index are described below.

Forecasts of the Adjusted Act 1 Index - For school districts with a Market Value/Personal Income Aid Ratio (MV/PI AR) greater than 0.400 in the previous year, the adjusted index was calculated by multiplying the base index for the tax year by the sum of 0.75 and the school district's MV/PI AR. School districts with an MV/PI AR less than 0.400 are assigned the base index.

The forecast of the Act 1 base index through FY 2017-18 requires two separate forecasts of the two components that comprise the base index. The base index is equal to the average of the percentage change in the Statewide Average Weekly Wage (SAWW) and the Employer Cost Index (ECI) for secondary and elementary schools. Beginning with the index computed for FY 2013-14, the SAWW component will be calculated using a three-year average. The data for the SAWW forecast was provided to the IFO by the PA Department of Labor and Industry.

The ECI projection of total compensation (benefits and wages) for elementary and secondary schools was computed using historical data from the Bureau of Labor Statistics (BLS) and the forecast of the ECI for all occupations through 2018 from IHS Global Insight. Historical data yield the average share of the index that is wages or compensation. Those shares are assumed constant moving forward. The benefits portion uses the same growth rate as that assumed for the all worker ECI projection from IHS Global Insight. The wage portion assumes that the growth rate for elementary and secondary schools will be slightly less than the all occupations ECI for wages.

[32] The Act 1 Index does not apply to the City of Philadelphia School District. Property tax growth for the district was calculated using historical data and growth rates.

History and Forecast of the Act 1 Base Index (and Components)

Fiscal Year	SAWW[1/]	ECI	Act 1 Base Index
2006-07	4.2%	3.5%	3.9%
2007-08	2.8%	4.0%	3.4%
2008-09	4.3%	4.5%	4.4%
2009-10	4.6%	3.6%	4.1%
2010-11	2.7%	3.0%	2.9%
2011-12	0.9%	1.9%	1.4%
2012-13	2.1%	1.3%	1.7%
2013-14	2.0%	1.4%	1.7%
2014-15	2.7%	1.8%	2.2%
2015-16	2.5%	2.2%	2.3%
2016-17	2.4%	2.3%	2.3%
2017-18	2.3%	2.5%	2.4%

1/ For FY 2013-14 and thereafter the SAWW is calculated based on a three year average.

Market Value/Personal Income Aid Ratio (MV/PI AR) – Ratios were forecasted separately for each school district through FY 2017-18 based on 15 years of historical data. In some cases, only 14 years of data were available. Observations that were more than two standard deviations greater than the sample average (for a school district) were replaced with the average of the observations preceding and following the outlier. If the latest observation, for FY 2012-13, exceeded the sample average by one standard deviation, then it was replaced by the average of the preceding two observations. These adjustments are necessary due to various reporting issues.

A linear trend line was then calculated for the 15 observations. The slope of the trend line was applied to the FY 2012-13 observation, which is the base year. School districts that report no change in their MV/PI AR over the 15 years are kept at their historic rates.

Debt Service Forecast

The debt service forecast is the sum of debt service and debt service fund transfers to sinking funds from the annual financial reports (AFRs) school districts file with PDE. The most recent publicly available data are for FY 2009-10. Debt service for FY 2011-12 was determined by taking FY 2009-10 debt service as a percentage of property tax revenues and applying that percentage to FY 2011-12 property tax collections.

The proposal specifies that property tax can only be levied for debt service for debt in existence on December 31, 2011.[33] The amount of debt service is reduced by six percent of the FY 2011-12 level each year to account for the retirement of debt. Hence, the analysis assumes that all remaining debt will be retired in roughly 17 years (average of eight years remains) and is uniformly spread over those years.

Secondary Effects from Sales Tax Rate Increase and Base Expansion

The analysis assumes that total (after-tax) spending levels remain constant following the sales tax change, so that the dollar amount of business sales falls by the increase in sales tax revenues. The analysis applies an average profit margin of 5.5 percent on reduced business sales, which is evenly split between C corporations (who remit corporate net income tax) and partnerships, S corporations and sole proprietors

[33] It is not clear if the term "debt in existence" refers to debt that has been incurred or debt that has been issued. For the purpose of this analysis, we assume that it means debt that has been issued.

(who remit personal income tax).[34,35] Applying an average effective tax rate of 6 percent to corporate income and 3 percent to pass through income yields a minor revenue offset of $7 million per year.[36]

Secondary Effects from the Elimination of School Property Tax: Individuals

Pennsylvania homeowners who itemize will generally realize a federal income tax increase under the proposal. Federal income tax data show that 1.7 million residents claimed $9.5 billion in state and local income tax deductions on Schedule A of the federal income tax return for tax year 2010 (average of $5,630).[37] Due to the increase in the state personal income tax rate, the analysis assumes that the deduction for state and local income taxes would increase by 0.94 / (3.07 + 1.0) or 23 percent, yielding an increase in itemized deductions for state and local income taxes of $2.2 billion for tax year 2010. Federal tax data also show that 1.7 million residents claimed $7.7 billion of real estate tax deductions (average of $4,434) for tax year 2010. The analysis assumes that the elimination of local school property taxes reduces the federal itemized deduction for real estate taxes by 65 percent ($5.0 billion). It is not completely eliminated because a portion of the deduction is attributable to out-of-state properties, and the levies for municipalities and existing debt service remain under the proposal.

The net reduction in Schedule A itemized deductions, and corresponding increase to federal adjusted gross income (AGI), is then $2.8 billion for tax year 2010. The income characteristics of these itemizers suggests an average effective marginal income tax rate of 25 percent for 2010, yielding an implicit federal tax increase of $0.7 billion.[38] Normal growth and the expiration of certain individual income tax cuts under current law imply significant growth in federal tax liability for higher income individuals from 2010 to 2014. The analysis assumes that the computed tax increase grows by 20 percent ($0.85 billion). However, certain taxpayers would no longer itemize, but would switch to the standard deduction. Hence, the computed tax increase is reduced by one third, yielding a net federal tax increase of $565 million for 2014 for homeowners under the proposal.[39]

Secondary Effects from the Elimination of School Property Tax: Business Entities

The analysis assumes (1) an average effective federal marginal income tax rate of 25 percent for all business entities and (2) the business property tax cut is split evenly between C corporations and pass

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[34] The average profit margin is equal to the average ratio of net income to business receipts for non-financial C corporations, S corporations and partnerships. The computation uses data from IRS' Statistics of Income Division. See http://www.irs.gov/uac/Tax-Stats-2.

[35] For corporations, the analysis assumes that 30 percent of the decline in profits would be reported on the state corporate income tax return (due to the apportionment of net income by multistate firms). This share is computed from data published in *Statistics on Capital Stock/Franchise Tax and Corporate Net Income Tax*, Tax Year 2004 (Department of Revenue).

[36] The analysis does not use the statutory rates of 9.99 percent (corporate income taxes) or 4.01 percent (personal income taxes under the proposal) because some portion of the decrease in pre-tax business profits would merely increase tax losses and not decrease taxable profits.

[37] See http://www.irs.gov/uac/SOI-Tax-Stats---Historic-Table-2.

[38] Both itemized deductions are skewed towards higher income individuals: roughly 52 percent of the property tax deduction and 69 percent of the income tax deduction was claimed by taxpayers reporting federal AGI in excess of $100,000.

[39] Certain taxpayers might also minimize taxes by switching from the local income tax deduction to the local sales tax deduction. For tax year 2010, only 0.2 million residents used the local sales tax option. The Schedule A sales tax deduction can only be used in place of the income tax deduction, which increases under the proposal, not the deduction for local property taxes.

through entities. For state income tax purposes, the analysis assumes an effective tax rate of 3.0 percent for pass through business income and 6.0 percent for corporate net income. [40]

For pass though entities, the analysis assumes that $1.6 billion of net property tax cuts (FY 2013-14) flow through to individual partners, shareholders and owners as higher business income. The analysis assumes that amount is offset by higher business sales tax paid under the sales tax rate increase, for a net amount of $1.3 billion. Finally, the analysis assumes that 85 percent flows through to resident owners liable for personal income tax. Applying the 3 percent effective tax rate yields an offset of $32 million in additional PIT revenues for FY 2013-14. For corporations, the analysis assumes that 42 percent of the $1.3 billion increase in net income is reported on the corporate income tax return (due to apportionment) yielding an offset of $33 million for FY 2013-14 at the 6 percent effective tax rate.[41]

Methodology to Compute Property Tax Share of Business Receipts

The data used to compute the relative size of property taxes for manufacturers, wholesalers and retailers and certain professional firms is from IRS' Corporate Income Tax Returns 2007, Table 5.[42] Per the corporate income tax return instructions, firms should report various taxes paid on line 17 of the Form 1120 or 1120S. The largest portion of reported taxes paid will represent the employer's share of payroll taxes. To remove those amounts, the analysis multiples total wage costs (including compensation of officers and any cost of labor embedded in cost of goods sold) by 7.65 percent (employer's share of Social Security and OASDI). A cut back of 90 percent is applied to those amounts because some employees exceed the wage limit upon which employers must remit payroll tax. The analysis suggests that employer payroll taxes comprise roughly one half of the amount reported on line 17. The analysis assumes that property taxes comprise 85 percent of the residual amount, while other miscellaneous fees and taxes comprise 15 percent. While the property tax share of total taxes reported is not known with certainty, total taxes reported on the corporate income tax return should represent an upper bound regarding the property tax share of total business sales. If all taxes reported were property taxes, they would comprise roughly one to two percent of total sales. The IFO analysis assumes the property tax share is one half that amount, based on the dollar amount of wage income also reported by firms and the associated payroll taxes.

Computation of Marginal Propensities to Consume and Share Spent on Taxable Items

Many of the secondary revenue effects computed for this analysis assume that 90 percent of the change in disposable income is spent (i.e., the "marginal" propensity to consume) and 70 percent is spent on taxable items under the sales tax base expansion. The analysis uses data from the U.S. Consumer Expenditure

[40] The analysis does not use the statutory rates of 9.99 percent (corporate income taxes) or 4.01 percent (personal income taxes under the proposal) because some portion of the increase in pre-tax business profits will merely reduce tax losses, and will not increase taxable profits.

[41] For corporations, the analysis assumes that 30 percent of the decline in profits would be reported on the state corporate income tax return (due to the apportionment of net income by multistate firms). This share is computed from data published in *Statistics on Capital Stock/Franchise Tax and Corporate Net Income Tax*, Tax Year 2004 (Department of Revenue).

[42] See http://www.irs.gov/uac/SOI-Tax-Stats---Corporation-Complete-Report.

Survey (CES) to derive those figures.[43] The survey details average expenditures of consumers on various goods and services based on income, age and region. Data show that the median household income for Pennsylvania was $50,400 for 2006-2010 (U.S. Census Bureau). Given that level, the analysis uses average spending patterns by "consumer units" (i.e., households) with an income level of $40,000 to $59,999 who reside in the northeastern U.S. region (spending patterns are not available on a state basis). The CES data suggest that individuals in that income group consume roughly 90-100 percent of their disposable income. For additional disposable income that is considered "permanent" by the recipient, the share spent would be somewhat lower. Therefore, the analysis uses a figure on the low end of that range.

The share of current and new disposable income spent on taxable items also uses CES data. For each spending category in the CES, the IFO specified the share taxable under current and proposed law. For certain spending categories, only a portion would be subject to tax (e.g., food and clothing). For food expenditures, the share taxed was based on detail from the Personal Consumption Expenditures published by the Bureau of Economic Analysis and an analysis performed by the Pennsylvania Food Merchants Association. The two data sources suggest similar exemptions for food items that would be excluded from tax due to the exclusion for WIC food items.

Based on CES spending patterns and the specification of the share taxable for each spending category, overall sales tax burden can be computed. For any new purchases triggered by changes in disposable income under the proposal, the analysis pro-rates new spending across non-essential items based on spending patterns. For example, if clothing purchases comprise 20 percent of non-essential purchases, then the analysis assumes that 20 percent of the increase in disposable income spent goes towards those purchases. The methodology suggests that roughly 70 percent of additional spending would be taxable if non-essential items are excluded.

Data Sources and Methodology for Distributional Analysis

The distributional analysis uses median incomes for homeowners and renters for two age cohorts: households with an individual older than 65 (generally the head of the household or a spouse) and households with no individuals above age 65. Those tabulations were supplied by the Penn State Data Center using data from the U.S. Census Bureau's American Community Survey (ACS). The analysis also uses data from the CES and IRS to inform the types of income reported by those median households (e.g., wages, social security, pensions, business income, interest, dividends) and certain itemized deductions used in the federal income tax computation. The analysis computes federal income tax based on income level and composition, any itemized or standard deductions claimed and the assumed number of personal exemptions (four for working age, two for retirees). The computation uses tax federal tax law effective in 2011, which may or may not be extended to future years. The working age homeowner minimizes tax liability by itemization, while other groups use the standard deduction. The analysis uses average property taxes based on data compilations by the IFO and assumes the same levels for the two homeowner age cohorts. State income tax is equal to state taxable income multiplied by the applicable tax rate, less any credits for tax forgiveness. Local income tax uses the median local rate (1 percent), also allowing for tax forgiveness. The analysis assumes that the proposal eliminates 73 percent of property tax paid if "fully phased in" and 63 percent in the first year.

[43] See http://www.bls.gov/cex/tables.htm.

The analysis assumes that average rental payments are 28 percent of income for working age renters and 34 percent for retirees. Those shares were informed by data tabulations for Pennsylvania published in the American Housing Survey by the U.S. Census Bureau and the Consumer Expenditure Survey. Property taxes are assumed to comprise 10 percent of rental payments. The analysis reduces that portion of the rental payment by 33 percent due to the elimination of property taxes levied on landlords once the proposal is fully phased in. Federal tax data for partnerships primarily engaged in rental real estate activities suggest that property taxes comprise roughly ten percent of total rental income.

The deduction of income and property taxes from total income equals disposable income. The analysis assumes that working age homeowners who report higher disposable income due to the proposal consume 90 percent of their additional income, lower income renters consume 95 percent and the older age cohorts consume all additional income. The share of disposable income spent on taxable goods under current and proposed law uses spending patterns for the two age cohorts from the Consumer Expenditure Survey (see discussion above). For each spending category included in survey, the IFO designated each as taxable or exempt under current and proposed law.

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Technical Appendix B

This appendix contains various tabulations of school property taxes.

Local Property Taxes: Total Collections by Fiscal Year
($ thousands)

Fiscal Year	Total Current & Interim Real Estate Taxes Collected	Act 1 Property Tax Reduction Allocations[1/]	Total Real Estate Taxes (Current and Interim + Allocations)	Increase over Prior Year	Percent Increase	10-Year Average
2010-11	$11,153,189	$530,223	$11,683,412	$396,901	3.7%	5.5%
2009-10	10,759,582	526,929	11,286,511	321,692	3.1%	5.7%
2008-09	10,438,463	526,355	10,964,819	490,768	4.7%	5.9%
2007-08	10,474,050	n.a.	10,474,050	463,331	4.6%	5.9%
2006-07	10,010,719	n.a.	10,010,719	559,857	5.9%	5.8%
2005-06	9,450,862	n.a.	9,450,862	540,974	6.1%	5.7%
2004-05	8,909,888	n.a.	8,909,888	605,659	7.3%	5.4%
2003-04	8,304,229	n.a.	8,304,229	542,219	7.0%	5.2%
2002-03	7,762,010	n.a.	7,762,010	564,558	7.8%	5.1%
2001-02	7,197,452	n.a.	7,197,452	381,838	5.6%	5.0%
2000-01	6,815,614	n.a.	6,815,614	341,480	5.3%	5.3%
1999-00	6,474,134	n.a.	6,474,134	281,673	4.5%	5.9%
1998-99	6,192,461	n.a.	6,192,461	292,668	5.0%	6.4%
1997-98	5,899,793	n.a.	5,899,793	207,669	3.6%	6.7%
1996-97	5,692,124	n.a.	5,692,124	257,023	4.7%	7.1%
1995-96	5,435,101	n.a.	5,435,101	189,004	3.6%	7.3%
1994-95	5,246,097	n.a.	5,246,097	264,978	5.3%	7.6%
1993-94	4,981,119	n.a.	4,981,119	244,889	5.2%	7.9%
1992-93	4,736,231	n.a.	4,736,231	330,954	7.5%	8.0%
1991-92	4,405,277	n.a.	4,405,277	348,451	8.6%	7.9%
1990-91	4,056,826	n.a.	4,056,826	394,131	10.8%	-
1989-90	3,662,695	n.a.	3,662,695	330,573	9.9%	-
1988-89	3,332,123	n.a.	3,332,123	255,208	8.3%	-
1987-88	3,076,915	n.a.	3,076,915	209,524	7.3%	-
1986-87	2,867,391	n.a.	2,867,391	182,348	6.8%	-
1985-86	2,685,043	n.a.	2,685,043	160,810	6.4%	-
1984-85	2,524,233	n.a.	2,524,233	184,798	7.9%	-
1983-84	2,339,435	n.a.	2,339,435	146,334	6.7%	-
1982-83	2,193,101	n.a.	2,193,101	142,122	6.9%	-
1981-82	2,050,979	n.a.	2,050,979	-	-	-
Avg. Increase					**6.2%**	

1/ Excludes allocations for Philadelphia, which are dedicated to wage tax rate reductions. Source: PDE, Finances, AFR Data Detailed, Local Property Taxes Collected, Programs, Property Tax Relief, http://www.portal.state.pa.us/portal/server.pt/community/finances/7671. Additional calculations and compilations performed by the IFO.

Sources of Revenue for Pennsylvania School Districts
(fiscal year, $ millions)

Revenue Source	FY 1995-96 Amount	FY 1995-96 Percent	FY 2000-01 Amount	FY 2000-01 Percent	FY 2005-06 Amount	FY 2005-06 Percent	FY 2010-11 Amount	FY 2010-11 Percent
Local Taxes	$6,916	53.3%	$8,600	55.0%	$11,699	55.8%	$13,460	53.4%
Local Other[1/]	306	2.4%	462	3.0%	694	3.3%	676	2.7%
Local Subtotal	7,222	55.7%	9,062	57.9%	12,394	59.1%	14,136	56.1%
State[2/]	5,182	40.0%	5,841	37.3%	7,410	35.3%	8,595	34.1%
Federal	387	3.0%	566	3.6%	857	4.1%	2,160	8.6%
Other	180	1.4%	177	1.1%	303	1.4%	313	1.2%
Total	**12,970**	**100.0%**	**15,647**	**100.0%**	**20,964**	**100.0%**	**25,204**	**100.0%**

1/ Includes various other sources of local revenue such as cafeteria revenues, donations, student activity fees, revenue received through government entities, etc.

2/ Act 1 Property Tax Relief Allocations to School Districts are classified as State Revenue.

Source: PDE, Finances, Revenue Data for all LEAs, http://www.education.state.pa.us/portal/server.pt/community/finances/7671. Additional calculations and compilations performed by the IFO.

Local Tax Revenues for Pennsylvania School Districts
(fiscal year, $ millions)

Revenue Source	FY 1995-96 Amount	FY 1995-96 Percent	FY 2000-01 Amount	FY 2000-01 Percent	FY 2005-06 Amount	FY 2005-06 Percent	FY 2010-11 Amount	FY 2010-11 Percent
Real Estate Taxes	$5,435	78.6%	$6,816	79.4%	$9,451	80.8%	$11,153	82.8%
Act 1 & 511 Income Taxes	525	7.6%	703	8.2%	976	8.3%	1,125	8.3%
1st Class SD Taxes	182	2.6%	218	2.5%	247	2.1%	267	2.0%
Other 511 Taxes[1/]	292	4.2%	332	3.9%	405	3.5%	254	1.9%
Delinquent Taxes	360	5.2%	446	5.2%	559	4.8%	614	4.5%
Other Taxes[2/]	120	1.7%	67	0.8%	54	0.5%	63	0.5%
Total[3/]	**6,913**	**100.0%**	**8,583**	**100.0%**	**11,692**	**100.0%**	**13,477**	**100.0%**

1/ Includes misc. taxes such as local services, occupational, business privilege, real estate transfers, etc.

2/ Includes public utility, per capita and in-lieu of payments.

3/ Differences in tables due to technical reporting issues.

Source: PDE, Finances, Revenue Data for all LEAs, Act 1/ Act 511/ 1st Class SD Taxes, Detailed AFR Data, Local Revenues, http://www.education.state.pa.us/portal/server.pt/community/finances/7671. Additional calculations and compilations performed by the IFO.

Local Property Taxes: Annual Average Growth Rates by County Ending FY 2010-11[1/, 2/]

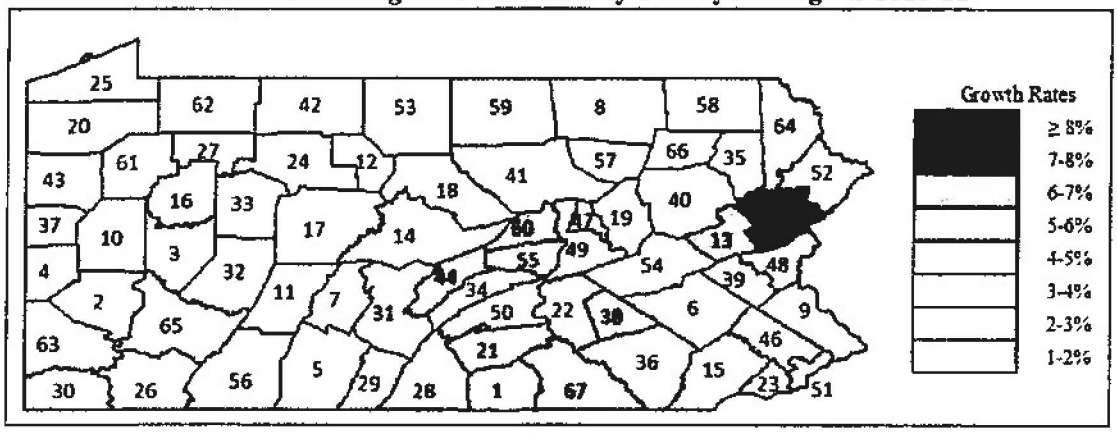
Number	County	5-Year	10-Year	15-Year	Number	County	5-Year	10-Year	15-Year
1	Adams	5.7%	6.4%	6.5%	35	Lackawanna	4.0%	4.8%	4.6%
2	Allegheny	2.4%	3.9%	3.8%	36	Lancaster	5.7%	6.2%	5.8%
3	Armstrong	2.6%	3.6%	3.1%	37	Lawrence	3.4%	4.0%	3.5%
4	Beaver	2.5%	3.0%	3.1%	38	Lebanon	6.2%	6.4%	5.5%
5	Bedford	2.3%	3.0%	3.1%	39	Lehigh	4.6%	6.4%	6.3%
6	Berks	4.7%	6.1%	5.5%	40	Luzerne	4.5%	4.7%	3.9%
7	Blair	4.0%	3.9%	3.9%	41	Lycoming	3.0%	4.4%	3.9%
8	Bradford	5.4%	5.9%	5.2%	42	McKean	1.2%	1.8%	2.3%
9	Bucks	4.3%	5.9%	5.8%	43	Mercer	2.5%	4.1%	4.3%
10	Butler	4.0%	5.2%	5.2%	44	Mifflin	6.5%	3.7%	3.4%
11	Cambria	3.8%	3.0%	2.7%	45	Monroe	7.9%	8.9%	8.3%
12	Cameron	1.3%	1.3%	1.1%	46	Montgomery	4.9%	6.0%	6.0%
13	Carbon	6.1%	6.9%	6.2%	47	Montour	4.3%	4.3%	4.2%
14	Centre	4.7%	6.6%	6.6%	48	Northampton	5.7%	7.1%	7.1%
15	Chester	4.7%	6.9%	7.0%	49	Northumberland	5.6%	5.1%	4.4%
16	Clarion	4.0%	3.5%	3.2%	50	Perry	4.1%	7.0%	6.5%
17	Clearfield	4.0%	4.2%	3.9%	51	Philadelphia	2.0%	3.5%	2.7%
18	Clinton	3.8%	4.3%	3.3%	52	Pike	3.5%	5.4%	5.1%
19	Columbia	3.1%	5.3%	5.3%	53	Potter	1.7%	3.7%	3.7%
20	Crawford	4.1%	4.8%	4.3%	54	Schuylkill	4.0%	4.9%	5.3%
21	Cumberland	5.3%	7.0%	6.3%	55	Snyder	5.2%	5.9%	6.3%
22	Dauphin	4.9%	5.7%	5.3%	56	Somerset	4.1%	4.6%	4.1%
23	Delaware	4.8%	5.5%	5.3%	57	Sullivan	4.3%	4.9%	4.0%
24	Elk	3.2%	2.1%	2.6%	58	Susquehanna	3.9%	4.4%	5.2%
25	Erie	2.4%	4.2%	4.2%	59	Tioga	5.4%	6.7%	6.3%
26	Fayette	2.9%	4.6%	3.9%	60	Union	6.5%	6.8%	5.3%
27	Forest	2.0%	2.4%	2.2%	61	Venango	2.4%	3.3%	3.0%
28	Franklin	5.7%	6.9%	6.1%	62	Warren	1.9%	2.2%	3.3%
29	Fulton	4.5%	4.8%	3.9%	63	Washington	3.9%	4.7%	4.0%
30	Greene	4.2%	4.6%	2.8%	64	Wayne	5.1%	5.8%	5.3%
31	Huntingdon	5.0%	3.8%	2.9%	65	Westmoreland	2.5%	4.4%	4.2%
32	Indiana	4.7%	5.0%	4.8%	66	Wyoming	4.0%	5.2%	4.6%
33	Jefferson	1.8%	2.4%	2.6%	67	York	6.5%	7.9%	7.3%
34	Juniata	2.5%	15.6%	10.8%					

1/ FY 2010-11 includes Act 1 Property Tax Reduction Allocation.

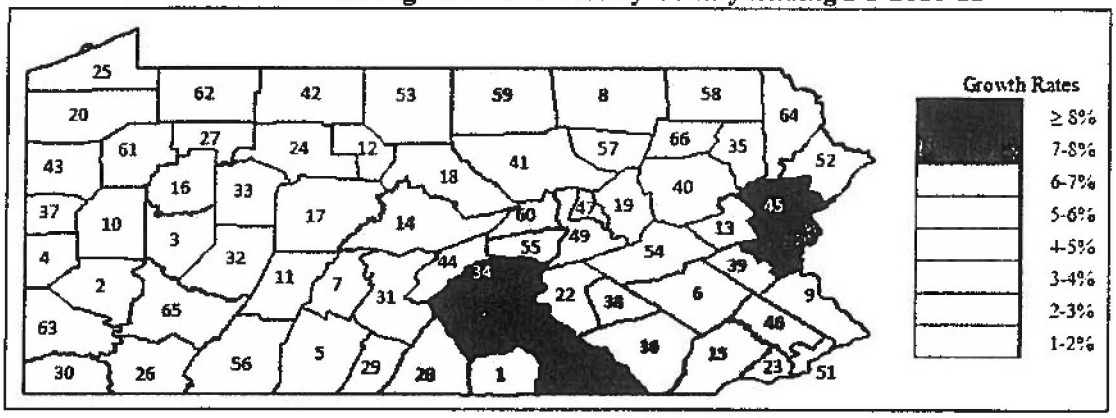
2/ Multi-county school districts are accounted for in their tax county as recorded by PDE.

Source: PDE, Finances, Revenue Data for all LEAs, http://www.education.state.pa.us/portal/server.pt/community/finances/7671. Additional calculations and compilations performed by the IFO.

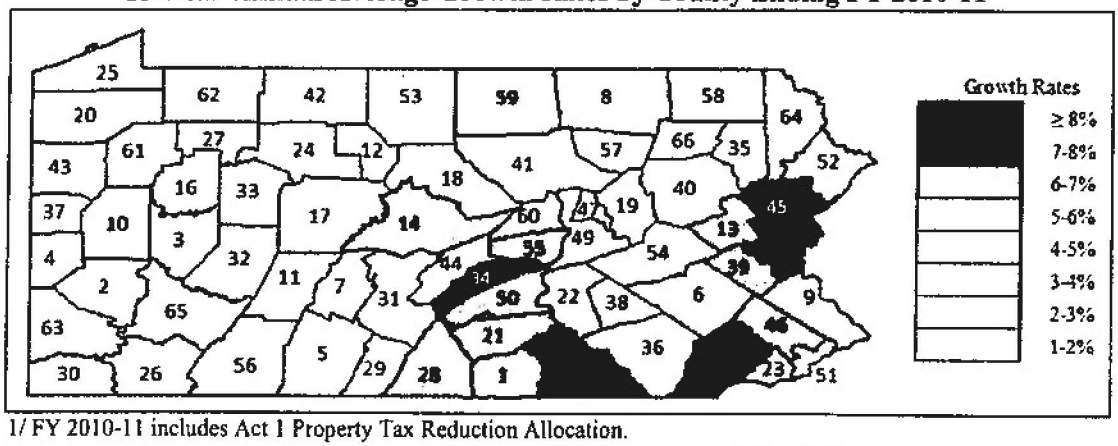
Local Property Taxes:
5-Year Annual Average Growth Rates by County Ending FY 2010-11[1/ 2/]



10-Year Annual Average Growth Rates by County Ending FY 2010-11[1/]



15-Year Annual Average Growth Rates by County Ending FY 2010-11[1/]



1/ FY 2010-11 includes Act 1 Property Tax Reduction Allocation.
2/ Multi-county school districts are accounted for in their tax county as recorded by PDE.
Source: PDE, Finances, Revenue Data for all LEAs, http://www.education.state.pa.us/portal/server.pt/community/finances/7671. Additional calculations and compilations performed by the IFO.

Local Property Taxes: Collections by County for FY 2010-11[1/,2/]

($ thousands)

Rank	County	Real Estate Tax Collections	% Total PA Collections	Rank	County	Real Estate Tax Collections	% Total PA Collections
1	Montgomery	$1,344,583	11.51%	35	Fayette	$49,897	0.43%
2	Allegheny	1,239,289	10.61%	36	Clearfield	48,821	0.42%
3	Bucks	996,615	8.53%	37	Columbia	46,389	0.40%
4	Chester	819,338	7.01%	38	Lawrence	44,406	0.38%
5	Delaware	749,605	6.42%	39	Crawford	43,577	0.37%
6	Philadelphia	544,622	4.66%	40	Pike	40,576	0.35%
7	Lancaster	516,802	4.42%	41	Somerset	40,079	0.34%
8	York	511,690	4.38%	42	Bradford	38,704	0.33%
9	Berks	470,860	4.03%	43	Northumberland	35,274	0.30%
10	Northampton	374,094	3.20%	44	Susquehanna	33,807	0.29%
11	Lehigh	371,945	3.18%	45	Greene	30,765	0.26%
12	Monroe	324,226	2.78%	46	Perry	30,575	0.26%
13	Westmoreland	266,215	2.28%	47	Venango	27,749	0.24%
14	Dauphin	231,877	1.98%	48	Tioga	24,202	0.21%
15	Cumberland	196,323	1.68%	49	Bedford	23,865	0.20%
16	Luzerne	194,567	1.67%	50	Wyoming	22,994	0.20%
17	Erie	169,260	1.45%	51	Snyder	22,707	0.19%
18	Washington	155,518	1.33%	52	Union	21,768	0.19%
19	Lackawanna	141,143	1.21%	53	Clarion	20,057	0.17%
20	Butler	141,018	1.21%	54	Clinton	19,737	0.17%
21	Lebanon	115,525	0.99%	55	Warren	19,722	0.17%
22	Centre	111,977	0.96%	56	McKean	19,336	0.17%
23	Beaver	107,255	0.92%	57	Mifflin	19,006	0.16%
24	Franklin	104,137	0.89%	58	Jefferson	16,071	0.14%
25	Adams	85,440	0.73%	59	Huntingdon	15,826	0.14%
26	Wayne	85,073	0.73%	60	Elk	14,154	0.12%
27	Schuylkill	73,345	0.63%	61	Potter	11,480	0.10%
28	Lycoming	67,623	0.58%	62	Montour	11,470	0.10%
29	Carbon	66,467	0.57%	63	Juniata	10,964	0.09%
30	Mercer	62,768	0.54%	64	Fulton	9,450	0.08%
31	Cambria	59,045	0.51%	65	Sullivan	6,753	0.06%
32	Blair	54,147	0.46%	66	Forest	3,980	0.03%
33	Indiana	53,823	0.46%	67	Cameron	2,750	0.02%
34	Armstrong	50,508	0.43%		**Total[3/]**	**11,683,635**	**100.00%**

1/ FY 2010-11 includes Act 1 Property Tax Reduction Allocation.

2/ Multi-county school districts are accounted for in their tax county as recorded by PDE.

Source: PDE, Finances, Revenue Data for all LEAs, http://www.education.state.pa.us/portal/server.pt/community/finances/7671. Additional calculations and compilations performed by the IFO.

3/ Difference due to rounding.

Local Property Taxes: Real Estate Taxes per Average Daily Membership FY 2010-11[1/,2/]

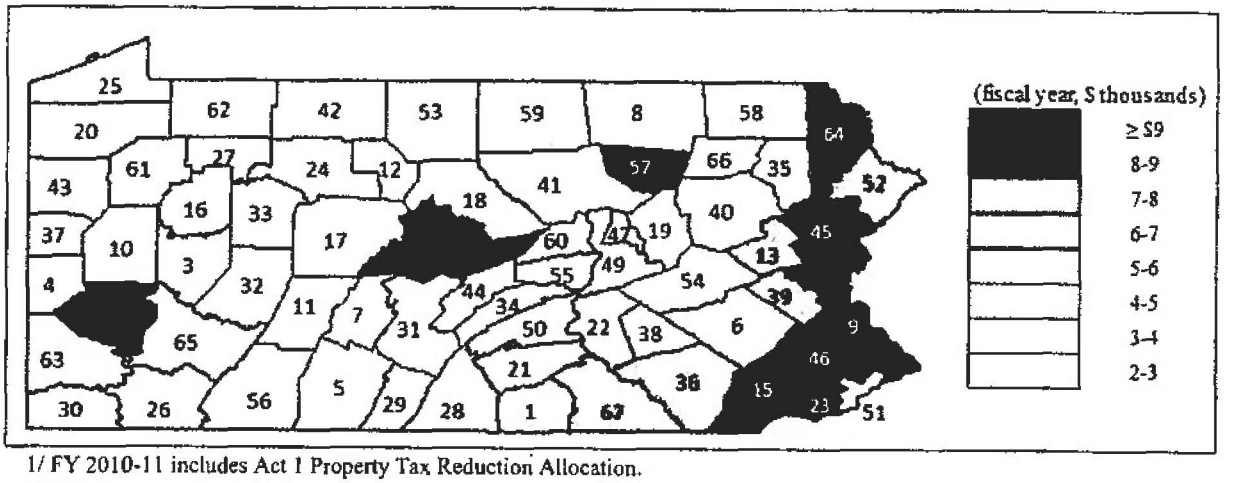
Number	County	FY 2010-11 Real Estate Taxes/ADM	Number	County	FY 2010-11 Real Estate Taxes/ADM
1	Adams	$5,945	35	Lackawanna	$5,129
2	Allegheny	8,057	36	Lancaster	7,402
3	Armstrong	4,874	37	Lawrence	3,265
4	Beaver	4,406	38	Lebanon	5,980
5	Bedford	3,125	39	Lehigh	7,076
6	Berks	6,607	40	Luzerne	4,475
7	Blair	2,989	41	Lycoming	4,053
8	Bradford	3,801	42	McKean	2,996
9	Bucks	10,768	43	Mercer	3,815
10	Butler	5,217	44	Mifflin	3,425
11	Cambria	3,208	45	Monroe	10,494
12	Cameron	3,736	46	Montgomery	12,655
13	Carbon	7,087	47	Montour	4,704
14	Centre	8,271	48	Northampton	8,152
15	Chester	10,876	49	Northumberland	2,804
16	Clarion	3,197	50	Perry	4,572
17	Clearfield	3,671	51	Philadelphia	2,652
18	Clinton	4,210	52	Pike	7,529
19	Columbia	4,569	53	Potter	4,401
20	Crawford	4,304	54	Schuylkill	3,743
21	Cumberland	6,700	55	Snyder	4,467
22	Dauphin	6,251	56	Somerset	3,813
23	Delaware	10,016	57	Sullivan	9,848
24	Elk	3,602	58	Susquehanna	4,746
25	Erie	4,128	59	Tioga	4,192
26	Fayette	2,687	60	Union	5,153
27	Forest	6,732	61	Venango	3,162
28	Franklin	5,304	62	Warren	3,809
29	Fulton	3,949	63	Washington	5,234
30	Greene	5,555	64	Wayne	9,521
31	Huntingdon	2,718	65	Westmoreland	5,166
32	Indiana	5,206	66	Wyoming	5,639
33	Jefferson	3,006	67	York	7,236
34	Juniata	3,457			

1/ FY 2010-11 includes Act 1 Property Tax Reduction Allocation.

2/ Multi-county school districts are accounted for in their tax county as recorded by PDE.

Source: PDE, Finances, Revenue Data for all LEAs, Financial Data Elements: ADM, http://www.education.state.pa.us/portal/server.pt/community/finances/7671. Additional calculations and compilations performed by the IFO.

Local Property Taxes: Real Estate Taxes per Average Daily Membership
FY 2010-11[1/,2/]



1/ FY 2010-11 includes Act 1 Property Tax Reduction Allocation.

2/ Multi-county school districts are accounted for in their tax county as recorded by PDE.

Source: PDE, Finances, Revenue Data for all LEAs, http://www.education.state.pa.us/portal/server.pt/community/finances/7671. Additional calculations and compilations performed by the IFO.

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Technical Appendix C

Overview of Amendments to HB 1776 (A12985) and SB 1400 (A13013)

The amendments to House Bill 1776 and Senate Bill 1400 make the following changes to the bills:

- Consolidates the provisions of Chapter 3 (allowing a school district to impose a personal income tax) and Chapter 5 (allowing a school district to impose an earned income tax). The school district may impose either the personal income tax or earned income and net profits tax for general revenue purposes upon the approval of the voters of the district in a referendum. The mechanics for the imposition and operation of the taxes are made consistent with applicable provisions under current law.
- Amends the definition of "sale at retail" under the new sales tax (Chapter 7) to exclude services rendered in the construction, reconstruction, remodeling, repair or maintenance of real estate from tax.
- Deletes the provision that requires all sales tax revenue (except transfers to the Public Transportation Reserve Fund) to be deposited into the Education Stabilization Fund (ESF).
- Inserts language that would require the Department of Revenue to deposit one percentage point of the sales tax collected in the ESF. The sales tax collected on the sale at retail of services and the expanded sales (as defined by a list) would be deposited into the Education Stabilization Fund.
- Deletes language that would have resulted in the repeal of Chapter 13 (Senior Citizens Property Tax and Rent Rebate Assistance) of the Taxpayer Relief Act (Act 1) due to inconsistency. Deletes provisions establishing a replacement program that would have prohibited rebates for property taxes paid in calendar year 2013 and thereafter.
- Changes the base year for distributions to school districts from the ESF from FY 2011-12 to FY 2012-13. Inserts language reducing the base year amount by the amount necessary to fund annual debt service payments for debt in existence on December 31, 2011.
- Eliminates language establishing certain gaming-related funds as revenue sources for the ESF. Replaces those provisions with language indicating that revenues transferred to the Property Tax Relief Fund under 4 Pa.C.S. §1408(e) and 1409 are revenue sources for the ESF.
- Eliminates language that restricted distributions to school districts from the ESF to FY 2012-13 (with distributions for future fiscal years to be determined by a subsequent statute).
- Makes technical changes to the wording of various provisions.

Copies of both amendments are included in the next several pages.

H1776B3369A12985 DMS:EAZ 08/10/12 #90 A12985

AMENDMENTS TO HOUSE BILL NO. 1776

Sponsor:

Printer's No. 3369

1 Amend Bill, page 1, lines 13 and 14, by striking out "and for
2 certain rebates and assistance to senior " in line 13 and
3 "citizens" in line 14

4 Amend Bill, page 1, lines 14 and 15, by striking out "The
5 Local Tax " in line 14 and "Enabling Act," in line 15 and
6 inserting
7 the Public School Code of 1949 and
8 Amend Bill, page 1, lines 16 through 18, by striking out "and
9 provisions relating to senior citizens " in line 16, all of line
10 17 and "Relief Act" in line 18

11 Amend Bill, page 2, lines 1 through 30; page 3, lines 1
12 through 8, by striking out all of said lines on said pages and
13 inserting

14 Chapter 3. Taxation by School Districts
15 Section 301. Scope.
16 Section 302. Definitions.
17 Section 303. Limitation.
18 Section 304. Preemption.
19 Section 305. General tax authorization.
20 Section 306. Referendum.
21 Section 307. Continuity of tax.
22 Section 308. Collections.
23 Section 309. Credits.
24 Section 310. Exemption and special provisions.
25 Section 311. Regulations.
26 Chapter 4. Education Tax
27 Section 401. Education tax.

28 Amend Bill, page 6, lines 19 through 30; page 7, lines 1

- 1 -

1 through 4, by striking out all of said lines on said pages and
2 inserting
3 Chapter 9. (Reserved)
4 Amend Bill, page 9, lines 8 through 30; pages 10 through 22,
5 lines 1 through 30; page 23, lines 1 through 23, by striking out
6 all of said lines on said pages and inserting
7 CHAPTER 3
8 TAXATION BY SCHOOL DISTRICTS
9 Section 301. Scope.
10 This chapter authorizes school districts to levy, assess and
11 collect a tax on personal income or a tax on earned income and
12 net profits as a means of abolishing property taxation by the
13 school district.
14 Section 302. Definitions.
15 The words and phrases used in this chapter shall have the
16 same meanings given to them in the Tax Reform Code of 1971 or
17 The Local Tax Enabling Act unless the context clearly indicates
18 otherwise.
19 Section 303. Limitation.
20 Any tax imposed under this chapter shall be subject to the
21 limitations set forth in Chapter 11.
22 Section 304. Preemption.
23 No act of the General Assembly shall vacate or preempt any
24 resolution passed or adopted under the authority of this
25 chapter, or any other act, providing authority for the
26 imposition of a tax by a school district, unless the act of the
27 General Assembly expressly vacates or preempts the authority to
28 pass or adopt resolutions.
29 Section 305. General tax authorization.
30 (a) General rule.--A board of school directors may, by
31 resolution, levy, assess and collect or provide for the levying,
32 assessment and collection of a tax on personal income or a tax
33 on earned income and net profits for general revenue purposes.
34 (b) Personal income tax.--
35 (1) A board of school directors may levy, assess and
36 collect a tax on the personal income of resident individuals
37 at a rate determined by the board of school directors.
38 (2) A school district which seeks to levy the tax
39 authorized under paragraph (1) must comply with section 306.
40 (3) If a board of school directors seeks to impose a
41 personal income tax under this subsection and the referendum
42 under section 306 is approved by the electorate, the board of
43 school directors shall have no authority to impose an earned
44 income and net profits tax under subsection (c) or any other
45 act.
46 (4) A personal income tax imposed under the authority of

2012/90DMS/HB1776A12985 - 2 -

1 this section shall be levied by the school district on each
2 of the classes of income specified in section 303 of the Tax
3 Reform Code of 1971 and regulations under that section,
4 provisions of which are incorporated by reference into this
5 chapter.
6 (i) Notwithstanding the provisions of section 353(f)
7 of the Tax Reform Code of 1971, the Department of Revenue
8 may permit the proper officer or an authorized agent of a
9 school district imposing a personal income tax pursuant
10 to this chapter to inspect the tax returns of any
11 taxpayer of the school district or may furnish to the
12 officer or an authorized agent an abstract of the return
13 of income of any current or former resident of the school
14 district or supply information concerning any item of
15 income contained in any tax return. The officer or
16 authorized agent of the school district imposing a tax
17 under this chapter shall be furnished the requested
18 information upon payment to the Department of Revenue of
19 the actual cost of providing the requested information.
20 (ii) (A) Except for official purposes or as
21 provided by law, it shall be unlawful for any officer
22 or authorized agent of a school district to do any of
23 the following:
24 (I) Disclose to any other individual or
25 entity the amount or source of income, profits,
26 losses, expenditures or any particular
27 information concerning income, profits, losses or
28 expenditures contained in any return.
29 (II) Permit any other individual or entity
30 to view or examine any return or copy of a return
31 or any book containing any abstract or
32 particulars.
33 (III) Print, publish or publicize in any
34 manner any return; any particular information
35 contained in or concerning the return; any amount
36 or source of income, profits, losses or
37 expenditures in or concerning the return; or any
38 particular information concerning income,
39 profits, losses or expenditures contained in or
40 relating to any return.
41 (B) Any officer or authorized agent of a school
42 district that violates clause (A):
43 (I) May be fined not more than $1,000 or
44 imprisoned for not more than one year, or both.
45 (II) May be removed from office or
46 discharged from employment.
47 (c) Earned income and net profits tax.--
48 (1) A board of school directors may levy, assess and
49 collect a tax on earned income and net profits of resident
50 individuals at a rate determined by the board of school
51 directors.

1 (2) A school district which seeks to levy the tax
2 authorized under paragraph (1) must comply with section 306.
3 (3) If a board of school directors seeks to impose a tax
4 on earned income and net profits under this subsection and
5 the referendum under section 306 is approved by the
6 electorate, the board of school directors shall have no
7 authority to impose a personal income tax under subsection
8 (b) or any other act.
9 Section 306. Referendum.
10 (a) General rule.--In order to levy a personal income tax or
11 an earned income and net profits tax under this chapter, a
12 governing body shall use the procedures set forth in subsections
13 (b), (c), (d), (e), (f) and (g).
14 (b) Approved by electorate.--
15 (1) Subject to notice and public hearing requirements of
16 subsection (g), a governing body may levy the personal income
17 tax or earned income and net profits tax under this chapter
18 only by obtaining the approval of the electorate of the
19 affected school district in a public referendum at only the
20 primary election preceding the fiscal year when the personal
21 income tax or earned income and net profits tax will be
22 initially imposed or the rate increased.
23 (2) The referendum question must state the initial rate
24 of the proposed personal income tax or earned income and net
25 profits tax, the purpose of the tax, the duration of the tax
26 and the amount of revenue to be generated by the
27 implementation of the tax.
28 (3) The question shall be in clear language that is
29 readily understandable by a layperson. For the purpose of
30 illustration, a referendum question may be framed as follows:
31 Do you favor paying a personal income tax of X% for
32 the purpose of X, for X years, which will generate
33 $X?
34 Do you favor paying an earned income and net profits
35 tax of X% for the purpose of X, for X years, which
36 will generate $X?
37 (4) A nonlegal interpretative statement must accompany
38 the question in accordance with section 201.1 of the act of
39 June 3, 1937 (P.L. 1333, No. 320), known as the Pennsylvania
40 Election Code, that includes the following:
41 (i) the initial rate of the personal income or
42 earned income and net profits tax imposed under this
43 chapter; and
44 (ii) the estimated revenues to be derived from the
45 initial rate imposed under this chapter.
46 (c) School district located in more than one county.--In the
47 event a school district is located in more than one county,
48 petitions under this section shall be filed with the election
49 officials of the county in which the administrative offices of
50 the school district are located.
51 (d) Review and certification.--The election officials who

1 receive a petition shall perform all administrative functions in
2 reviewing and certifying the validity of the petition and
3 conduct all necessary communications with the school district.
4 (e) Notification.--
5 (1) If the election officials of the county who receive
6 the petition certify that it is sufficient under this section
7 and determine that a question should be placed on the ballot,
8 the decision shall be communicated to election officials in
9 any other county in which the school district is also
10 located.
11 (2) Election officials in the other county or counties
12 shall cooperate with election officials of the county that
13 receives the petition to ensure that an identical question is
14 placed on the ballot at the same election throughout the
15 entire school district.
16 (f) Certification of results.--Election officials from each
17 county involved shall independently certify the results from
18 their county to the governing body.
19 (g) Adoption of resolution.--
20 (1) In order to levy the tax under this section, the
21 governing body shall adopt a resolution which shall refer to
22 this chapter prior to placing a question on the ballot.
23 (2) Prior to adopting a resolution imposing the tax
24 authorized by this section, the governing body shall give
25 public notice of its intent to adopt the resolution in the
26 manner provided by The Local Tax Enabling Act and shall
27 conduct at least two public hearings regarding the proposed
28 adoption of the resolution. One public hearing shall be
29 conducted during normal business hours and one public hearing
30 shall be conducted during evening hours or on a weekend.
31 Section 307. Continuity of tax.
32 Every tax levied under this chapter shall continue in force
33 on a fiscal year basis without annual reenactment unless the
34 rate of the tax is subsequently changed or the duration placed
35 on the referendum has expired.
36 Section 308. Collections.
37 Any income tax imposed under this chapter shall be subject to
38 the provisions for collection and delinquency found in The Local
39 Tax Enabling Act.
40 Section 309. Credits.
41 (a) Credit.--Except as set forth in subsection (b), the
42 provisions of The Local Tax Enabling Act shall be applied by a
43 board of school directors to determine any credits applicable to
44 a tax imposed under this chapter.
45 (b) Limitation.--Payment of any tax on income to any state
46 other than Pennsylvania or to any political subdivision located
47 outside the boundaries of this Commonwealth by a resident of a
48 school district located in this Commonwealth shall not be
49 credited to and allowed as a deduction from the liability of
50 such person for any income tax imposed by the school district of
51 residence pursuant to this chapter.

1 Section 310. Exemption and special provisions.
2 (a) Earned income and net profits tax.--A school district
3 that imposes an earned income and net profits tax authorized
4 under section 305(c) may exempt from the payment of that tax any
5 person whose total income from all sources is less than $12,000.
6 (b) Applicability to personal income tax.--Section 304 of
7 the Tax Reform Code of 1971 shall apply to any personal income
8 tax levied by a school district under section 305(b).
9 Section 311. Regulations.
10 A school district that imposes:
11 (1) an earned income and net profits tax authorized
12 under section 305(c) shall be subject to the provisions of
13 The Local Tax Enabling Act and may adopt procedures for the
14 processing of claims for credits and exemptions under section
15 309 and 310; or
16 (2) a personal income tax under section 305(b) shall be
17 subject to all regulations adopted by the Department of
18 Revenue in administering the tax due to the Commonwealth
19 under Article III of the Tax Reform Code of 1971.
20 CHAPTER 4
21 Amend Bill, page 23, line 25, by striking out "321" and
22 inserting
23 401
24 Amend Bill, page 24, lines 24 through 30; pages 25 through
25 38, lines 1 through 30; page 39, lines 1 through 6, by striking
26 out all of said lines on said pages
27 Amend Bill, page 56, line 17, by striking out "including" and
28 inserting
29 except
30 Amend Bill, page 79, lines 2 and 3, by striking out
31 "Transactions for which purchase agreements are " in line 2 and
32 all of line 3
33 Amend Bill, page 149, line 10, by inserting after "to" where
34 it occurs the first time
35 increase the rate of the current sales and use tax and
36 Amend Bill, page 149, lines 13 through 16, by striking out
37 all of said lines and inserting
38 (b) Deposit of sales and use tax collected.--The secretary

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1 shall deposit into the Education Stabilization Fund revenues
2 received on or after January 1, 2013, regardless of the
3 transaction date, that equal the portion of the tax imposed by
4 this chapter as follows:
5 (1) Except as otherwise provided in paragraphs (2) and
6 (3), 1% of the tax collected on the sales at retail and use
7 of tangible personal property and services as provided in
8 section 702.
9 (2) All of the tax collected on the sale at retail of
10 services under section 702, including those services subject
11 to the tax as provided under sections 701(k)(4) and (o)(4)
12 and 704(51).
13 (3) All of the tax collected on expanded sales and uses.
14 (c) Definition.--For purposes of this section, "expanded
15 sales and uses" means:
16 (1) The sale at retail or use of disposable diapers;
17 premoistened wipes; incontinence products; colostomy
18 deodorants; toilet paper; sanitary napkins, tampons or
19 similar items used for feminine hygiene; or toothpaste,
20 toothbrushes or dental floss.
21 (2) The sale at retail to, or use by, the United States,
22 this Commonwealth or its instrumentalities or political
23 subdivisions of tangible personal property or services.
24 (3) The sale at retail or use of prescription or
25 nonprescription medicines, drugs or medical supplies,
26 crutches and wheelchairs for the use of cripples and
27 invalids, artificial limbs, artificial eyes and artificial
28 hearing devices when designed to be worn on the person of the
29 purchaser or user, false teeth and materials used by a
30 dentist in dental treatment, eyeglasses when especially
31 designed or prescribed by an ophthalmologist, oculist or
32 optometrist for the personal use of the owner or purchaser
33 and artificial braces and supports designed solely for the
34 use of crippled persons or any other therapeutic, prosthetic
35 or artificial device designed for the use of a particular
36 individual to correct or alleviate a physical incapacity,
37 including, but not limited to, hospital beds, iron lungs, and
38 kidney machines.
39 (4) The sale at retail or use of all vesture, wearing
40 apparel, raiments, garments, footwear and other articles of
41 clothing, except as excluded from the tax under section
42 704(26).
43 (5) The sale at retail or use of food and beverages for
44 human consumption, except as excluded from the tax under
45 section 704(29).
46 (6) The sale at retail or use of newspapers. For
47 purposes of this section, the term "newspaper" shall mean a
48 "legal newspaper" or a publication containing matters of
49 general interest and reports of current events which
50 qualifies as a "newspaper of general circulation" qualified
51 to carry a "legal advertisement" as those terms are defined

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1 in 45 Pa.C.S. § 101 (relating to definitions), not including
2 magazines. The term "newspaper" also includes any printed
3 advertising materials circulated with such newspaper
4 regardless of where or by whom such printed advertising
5 material was produced.
6 (7) The sale at retail or use of caskets and burial
7 vaults for human remains and markers and tombstones for human
8 graves.
9 (8) The sale at retail or use of flags of the United
10 States and the Commonwealth of Pennsylvania.
11 (9) The sale at retail or use of textbooks for use in
12 schools, colleges and universities, either public or private,
13 when purchased in behalf of or through such schools, colleges
14 or universities provided such institutions of learning are
15 recognized by the Department of Education.
16 (10) The sale at retail or use of motion picture film
17 rented or licensed from a distributor for the purpose of
18 commercial exhibition.
19 (11) The sale at retail or use of mail order catalogs
20 and direct mail advertising literature or materials,
21 including electoral literature or materials, such as
22 envelopes, address labels and a one-time license to use a
23 list of names and mailing addresses for each delivery of
24 direct mail advertising literature or materials, including
25 electoral literature or materials, through the United States
26 Postal Service.
27 (12) The sale at retail of horses, if at the time of
28 purchase, the seller is directed to ship or deliver the horse
29 to an out-of-State location, whether or not the charges for
30 shipment are paid for by the seller or the purchaser.
31 (13) The sale at retail of supplies and materials to
32 tourist promotion agencies, which receive grants from the
33 Commonwealth, for distribution to the public as promotional
34 material or the use of such supplies and materials by said
35 agencies for said purposes.
36 (14) The sale at retail or use of materials used in the
37 construction and erection of objects purchased by not-for-
38 profit organizations for purposes of commemoration and
39 memorialization of historical events, provided that the
40 object is erected upon publicly owned property or property to
41 be conveyed to a public entity upon the commemoration or
42 memorialization of the historical event.
43 (15) The sale at retail or use of candy or gum
44 regardless of the location from which the candy or gum is
45 sold.
46 (16) The sale at retail or use of horses to be used
47 exclusively for commercial racing activities and the sale at
48 retail and use of feed, bedding, grooming supplies, riding
49 tack, farrier services, portable stalls and sulkies for
50 horses used exclusively for commercial racing activities.
51 (17) The sale at retail to or use by a construction

1 contractor of building machinery and equipment and services
2 thereto that are:
3 (i) transferred pursuant to a construction contract
4 for any charitable organization, volunteer firemen's
5 organization, volunteer firefighters' relief association,
6 nonprofit educational institution or religious
7 organization for religious purposes, provided that the
8 building machinery and equipment and services thereto are
9 not used in any unrelated trade or business; or
10 (ii) transferred to the United States or the
11 Commonwealth or its instrumentalities or political
12 subdivisions.
13 (18) The sale or use of used prebuilt housing.
14 (19) The sale at retail to or use of food and
15 nonalcoholic beverages by an airline which will transfer the
16 food or nonalcoholic beverages to passengers in connection
17 with the rendering of the airline service.
18 (20) The sale at retail or use of separately stated fees
19 paid pursuant to 13 Pa.C.S. § 9525 (relating to fees).
20 (21) The sale at retail or use of investment metal
21 bullion and investment coins. "Investment metal bullion"
22 means any elementary precious metal which has been put
23 through a process of smelting or refining, including, but not
24 limited to, gold, silver, platinum and palladium, and which
25 is in such state or condition that its value depends upon its
26 content and not its form. "Investment metal bullion" does not
27 include precious metal which has been assembled, fabricated,
28 manufactured or processed in one or more specific and
29 customary industrial, professional, aesthetic or artistic
30 uses. "Investment coins" means numismatic coins or other
31 forms of money and legal tender manufactured of gold, silver,
32 platinum, palladium or other metal and of the United States
33 or any foreign nation with a fair market value greater than
34 any nominal value of such coins. "Investment coins" does not
35 include jewelry or works of art made of coins, nor does it
36 include commemorative medallions.

37 Amend Bill, page 149, lines 18 through 30; pages 150 through
38 161, lines 1 through 30; page 162, lines 1 through 8, by
39 striking out all of said lines on said pages and inserting
40 (RESERVED)

41 Amend Bill, page 162, line 18, by striking out "at midnight
42 December 31, 2012" and inserting
43 January 1, 2013

44 Amend Bill, page 163, line 1, by striking out "authorized
45 under Chapter 3"

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1 Amend Bill, page 163, line 2, by striking out "5" and
2 inserting
3 3
4 Amend Bill, page 163, line 4, by striking out "under Chapter
5 5"
6 Amend Bill, page 163, line 5, by striking out "5" and
7 inserting
8 3
9 Amend Bill, page 163, line 6, by striking out "under Chapter
10 3"
11 Amend Bill, page 163, line 18, by striking out "reduce the
12 amount of" and inserting
13 fund the annual debt service payments for
14 Amend Bill, page 164, line 5, by striking out "reduce the
15 amount of" and inserting
16 fund the annual debt service payments for
17 Amend Bill, page 166, line 4, by inserting after "from"
18 school
19 Amend Bill, page 166, line 5, by striking out "tax" and
20 inserting
21 taxes
22 Amend Bill, page 166, line 5, by striking out "2011-2012" and
23 inserting
24 2012-2013 less the amount necessary to fund the annual
25 debt service payments for its outstanding debt in
26 existence on December 31, 2011
27 Amend Bill, page 166, line 22, by striking out "321" and
28 inserting
29 401
30 Amend Bill, page 166, lines 24 through 30; page 167, lines 1
31 and 2, by striking out all of said lines on said pages and

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1 inserting

2 (2) All revenue transferred to or received by the
3 property tax relief fund under:
4 (i) 4 Pa.C.S. § 1408(e) (relating to transfers from
5 State Gaming Fund); and
6 (ii) 4 Pa.C.S. § 1409 (relating to property tax
7 relief fund).

8 Amend Bill, page 167, line 12, by striking out "(a)

9 Initial.--For fiscal year 2012-2013, the" and inserting

10 The

11 Amend Bill, page 167, lines 23 through 25, by striking out

12 all of said lines

13 Amend Bill, page 168, line 6, by striking out all of said

14 line and inserting

15 as provided in section 782.

16 Amend Bill, page 169, lines 29 and 30; page 170, lines 1 and

17 2, by striking out all of said lines on page 169, all of line 1

18 and "(8)" in line 2 on page 170 and inserting

19 (7)

20 Amend Bill, page 170, lines 6 through 9, by striking out all

21 of said lines and inserting

22 Section 1504(b)(6) and Chapter 7 shall apply January 1,
23 2013.

24 Amend Bill, page 170, lines 12 through 16, by striking out

25 all of lines 12 through 15 and "(3)" in line 16 and inserting

26 (1) Section 1504(b)(2) and (8) and Chapters 3 and 4
27 shall take effect January 1, 2013.
28 (2)

SB 1400 (Amendment A13013)

S1400B2123A13013 AJM:EAZ 09/04/12 #90 A13013

AMENDMENTS TO SENATE BILL NO. 1400

Sponsor:

Printer's No. 2123

1 Amend Bill, page 1, lines 13 and 14, by striking out "and for
2 certain rebates and assistance to senior " in line 13 and
3 "citizens" in line 14

4 Amend Bill, page 1, lines 14 and 15, by striking out "The
5 Local Tax " in line 14 and "Enabling Act," in line 15 and
6 inserting
7 the Public School Code of 1949 and
8 Amend Bill, page 1, lines 16 through 18, by striking out "and
9 provisions relating to senior citizens " in line 16, all of line
10 17 and "Relief Act" in line 18

11 Amend Bill, page 1, lines 23 through 25, by striking out all
12 of said lines

13 Amend Bill, page 2, lines 1 through 30; page 3, lines 1
14 through 5, by striking out all of said lines on said pages and
15 inserting
16 Chapter 3. Taxation by School Districts
17 Section 301. Scope.
18 Section 302. Definitions.
19 Section 303. Limitation.
20 Section 304. Preemption.
21 Section 305. General tax authorization.
22 Section 306. Referendum.
23 Section 307. Continuity of tax.
24 Section 308. Collections.
25 Section 309. Credits.
26 Section 310. Exemption and special provisions.
27 Section 311. Regulations.

- 1 -

1 Chapter 4. Education Tax
2 Section 401. Education tax.

3 Amend Bill, page 6, lines 16 through 30; page 7, line 1, by

4 striking out all of said lines on said pages and inserting

5 Chapter 9. (Reserved)

6 Amend Bill, page 9, lines 4 through 30; pages 10 through 22,

7 lines 1 through 30; page 23, lines 1 through 20, by striking out

8 all of said lines on said pages and inserting

9 CHAPTER 3
10 TAXATION BY SCHOOL DISTRICTS
11 Section 301. Scope.
12 This chapter authorizes school districts to levy, assess and
13 collect a tax on personal income or a tax on earned income and
14 net profits as a means of abolishing property taxation by the
15 school district.
16 Section 302. Definitions.
17 The words and phrases used in this chapter shall have the
18 same meanings given to them in the Tax Reform Code of 1971 or
19 the Local Tax Enabling Act unless the context clearly indicates
20 otherwise.
21 Section 303. Limitation.
22 Any tax imposed under this chapter shall be subject to the
23 limitations set forth in Chapter 11.
24 Section 304. Preemption.
25 No act of the General Assembly shall vacate or preempt any
26 resolution passed or adopted under the authority of this
27 chapter, or any other act, providing authority for the
28 imposition of a tax by a school district, unless the act of the
29 General Assembly expressly vacates or preempts the authority to
30 pass or adopt resolutions.
31 Section 305. General tax authorization.
32 (a) General rule.--A board of school directors may, by
33 resolution, levy, assess and collect or provide for the levying,
34 assessment and collection of a tax on personal income or a tax
35 on earned income and net profits for general revenue purposes.
36 (b) Personal income tax.--
37 (1) A board of school directors may levy, assess and
38 collect a tax on the personal income of resident individuals
39 at a rate determined by the board of school directors.
40 (2) A school district which seeks to levy the tax
41 authorized under paragraph (1) must comply with section 306.
42 (3) If a board of school directors seeks to impose a
43 personal income tax under this subsection and the referendum
44 under section 306 is approved by the electorate, the board of
45 school directors shall have no authority to impose an earned
46 income and net profits tax under subsection (c) or any other

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act.

(4) A personal income tax imposed under the authority of this section shall be levied by the school district on each of the classes of income specified in section 303 of the Tax Reform Code of 1971 and regulations under that section, provisions of which are incorporated by reference into this chapter.

(i) Notwithstanding the provisions of section 353(f) of the Tax Reform Code of 1971, the department may permit the proper officer or an authorized agent of a school district imposing a personal income tax pursuant to this chapter 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. The officer or authorized agent of the school district imposing a tax under this chapter shall be furnished the requested information upon payment to the department of the actual cost of providing the requested information.

(ii) (A) Except for official purposes or as provided by law, it shall be unlawful for any officer or authorized agent of a school district to do any of the following:

(I) Disclose to any other individual or entity the amount or source of income, profits, losses, expenditures or any particular information concerning income, profits, losses or expenditures contained in any return.

(II) Permit any other individual or entity to view or examine any return or copy of a return or any book containing any abstract or particulars.

(III) Print, publish or publicize in any manner any return; any particular information contained in or concerning the return; any amount or source of income, profits, losses or expenditures in or concerning the return; or any particular information concerning income, profits, losses or expenditures contained in or relating to any return.

(B) Any officer or authorized agent of a school district that violates clause (A):

(I) May be fined not more than $1,000 or imprisoned for not more than one year, or both.

(II) May be removed from office or discharged from employment.

(c) Earned income and net profits tax.--

(1) A board of school directors may levy, assess and collect a tax on earned income and net profits of resident

1 individuals at a rate determined by the board of school
2 directors.
3 (2) A school district which seeks to levy the tax
4 authorized under paragraph (1) must comply with section 306.
5 (3) If a board of school directors seeks to impose a tax
6 on earned income and net profits under this subsection and
7 the referendum under section 306 is approved by the
8 electorate, the board of school directors shall have no
9 authority to impose a personal income tax under subsection
10 (b) or any other act.
11 Section 306. Referendum.
12 (a) General rule.--In order to levy a personal income tax or
13 an earned income and net profits tax under this chapter, a
14 governing body shall use the procedures set forth in subsections
15 (b), (c), (d), (e), (f) and (g).
16 (b) Approved by electorate.--
17 (1) Subject to notice and public hearing requirements of
18 subsection (g), a governing body may levy the personal income
19 tax or earned income and net profits tax under this chapter
20 only by obtaining the approval of the electorate of the
21 affected school district in a public referendum at only the
22 primary election preceding the fiscal year when the personal
23 income tax or earned income and net profits tax will be
24 initially imposed or the rate increased.
25 (2) The referendum question must state the initial rate
26 of the proposed personal income tax or earned income and net
27 profits tax, the purpose of the tax, the duration of the tax
28 and the amount of revenue to be generated by the
29 implementation of the tax.
30 (3) The question shall be in clear language that is
31 readily understandable by a layperson. For the purpose of
32 illustration, a referendum question may be framed as follows:
33 Do you favor paying a personal income tax of X% for
34 the purpose of X, for X years, which will generate
35 $X?
36 Do you favor paying an earned income and net profits
37 tax of X% for the purpose of X, for X years, which
38 will generate $X?
39 (4) A nonlegal interpretative statement must accompany
40 the question in accordance with section 201.1 of the act of
41 June 3, 1937 (P.L.1333, No.320), known as the Pennsylvania
42 Election Code, that includes the following:
43 (i) the initial rate of the personal income or
44 earned income and net profits tax imposed under this
45 chapter; and
46 (ii) the estimated revenues to be derived from the
47 initial rate imposed under this chapter.
48 (c) School district located in more than one county.--In the
49 event a school district is located in more than one county,
50 petitions under this section shall be filed with the election
51 officials of the county in which the administrative offices of

1 the school district are located.
2 (d) Review and certification.--The election officials who
3 receive a petition shall perform all administrative functions in
4 reviewing and certifying the validity of the petition and
5 conduct all necessary communications with the school district.
6 (e) Notification.--
7 (1) If the election officials of the county who receive
8 the petition certify that it is sufficient under this section
9 and determine that a question should be placed on the ballot,
10 the decision shall be communicated to election officials in
11 any other county in which the school district is also
12 located.
13 (2) Election officials in the other county or counties
14 shall cooperate with election officials of the county that
15 receives the petition to ensure that an identical question is
16 placed on the ballot at the same election throughout the
17 entire school district.
18 (f) Certification of results.--Election officials from each
19 county involved shall independently certify the results from
20 their county to the governing body.
21 (g) Adoption of resolution.--
22 (1) In order to levy the tax under this section, the
23 governing body shall adopt a resolution which shall refer to
24 this chapter prior to placing a question on the ballot.
25 (2) Prior to adopting a resolution imposing the tax
26 authorized by this section, the governing body shall give
27 public notice of its intent to adopt the resolution in the
28 manner provided by the Local Tax Enabling Act and shall
29 conduct at least two public hearings regarding the proposed
30 adoption of the resolution. One public hearing shall be
31 conducted during normal business hours and one public hearing
32 shall be conducted during evening hours or on a weekend.
33 Section 307. Continuity of tax.
34 Every tax levied under this chapter shall continue in force
35 on a fiscal year basis without annual reenactment unless the
36 rate of the tax is subsequently changed or the duration placed
37 on the referendum has expired.
38 Section 308. Collections.
39 Any income tax imposed under this chapter shall be subject to
40 the provisions for collection and delinquency found in the Local
41 Tax Enabling Act.
42 Section 309. Credits.
43 (a) Credit.--Except as set forth in subsection (b), the
44 provisions of the Local Tax Enabling Act shall be applied by a
45 board of school directors to determine any credits applicable to
46 a tax imposed under this chapter.
47 (b) Limitation.--Payment of any tax on income to any state
48 other than Pennsylvania or to any political subdivision located
49 outside the boundaries of this Commonwealth by a resident of a
50 school district located in this Commonwealth shall not be
51 credited to and allowed as a deduction from the liability of

1 such person for any income tax imposed by the school district of
2 residence pursuant to this chapter.
3 Section 310. Exemption and special provisions.
4 (a) Earned income and net profits tax.--A school district
5 that imposes an earned income and net profits tax authorized
6 under section 305(c) may exempt from the payment of that tax any
7 person whose total income from all sources is less than $12,000.
8 (b) Applicability to personal income tax.--Section 304 of
9 the Tax Reform Code of 1971 shall apply to any personal income
10 tax levied by a school district under section 305(b).
11 Section 311. Regulations.
12 A school district that imposes:
13 (1) an earned income and net profits tax authorized
14 under section 305(c) shall be subject to the provisions of
15 the Local Tax Enabling Act and may adopt procedures for the
16 processing of claims for credits and exemptions under
17 sections 309 and 310; or
18 (2) a personal income tax under section 305(b) shall be
19 subject to all regulations adopted by the department in
20 administering the tax due to the Commonwealth under Article
21 III of the Tax Reform Code of 1971.
22 CHAPTER 4
23 Amend Bill, page 23, line 22, by striking out "321" and
24 inserting
25 401
26 Amend Bill, page 24, lines 21 through 30; pages 25 through
27 38, lines 1 through 30; page 39, lines 1 through 3, by striking
28 out all of said lines on said pages
29 Amend Bill, page 56, line 14, by striking out "including" and
30 inserting
31 except
32 Amend Bill, page 78, lines 29 and 30, by striking out
33 "Transactions for which purchase agreements are " in line 29 and
34 all of line 30
35 Amend Bill, page 81, line 17, by striking out "701" and
36 inserting
37 701.1
38 Amend Bill, page 131, line 17, by striking out "701" and

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1 inserting

2 701.1

3 Amend Bill, page 149, line 7, by inserting after "to" where

4 it occurs the first time

5 increase the rate of the current sales and use tax and

6 Amend Bill, page 149, lines 10 through 13, by striking out

7 all of said lines and inserting

8 (b) Deposit of sales and use tax collected.--The secretary
9 shall deposit into the Education Stabilization Fund revenues
10 received on or after January 1, 2013, regardless of the
11 transaction date, that equal the portion of the tax imposed by
12 this chapter as follows:
13 (1) Except as otherwise provided in paragraphs (2) and
14 (3), 1% of the tax collected on the sales at retail and use
15 of tangible personal property and services as provided in
16 section 702.
17 (2) All of the tax collected on the sale at retail of
18 services under section 702, including those services subject
19 to the tax as provided under sections 701.1(k)(4) and (o)(4)
20 and 704(51).
21 (3) All of the tax collected on expanded sales and uses.
22 (c) Definition.--For purposes of this section, "expanded
23 sales and uses" means:
24 (1) The sale at retail or use of disposable diapers;
25 premoistened wipes; incontinence products; colostomy
26 deodorants; toilet paper; sanitary napkins, tampons or
27 similar items used for feminine hygiene; or toothpaste,
28 toothbrushes or dental floss.
29 (2) The sale at retail to, or use by, the United States,
30 this Commonwealth or its instrumentalities or political
31 subdivisions of tangible personal property or services.
32 (3) The sale at retail or use of prescription or
33 nonprescription medicines, drugs or medical supplies,
34 crutches and wheelchairs for the use of cripples and
35 invalids, artificial limbs, artificial eyes and artificial
36 hearing devices when designed to be worn on the person of the
37 purchaser or user, false teeth and materials used by a
38 dentist in dental treatment, eyeglasses when especially
39 designed or prescribed by an ophthalmologist, oculist or
40 optometrist for the personal use of the owner or purchaser
41 and artificial braces and supports designed solely for the
42 use of crippled persons or any other therapeutic, prosthetic
43 or artificial device designed for the use of a particular
44 individual to correct or alleviate a physical incapacity,
45 including, but not limited to, hospital beds, iron lungs, and
46 kidney machines.

(4) The sale at retail or use of all vesture, wearing apparel, raiments, garments, footwear and other articles of clothing, except as excluded from the tax under section 704(26).

(5) The sale at retail or use of food and beverages for human consumption, except as excluded from the tax under section 704(29).

(6) The sale at retail or use of newspapers. For purposes of this section, the term "newspaper" shall mean a "legal newspaper" or a publication containing matters of general interest and reports of current events which qualifies as a "newspaper of general circulation" qualified to carry a "legal advertisement" as those terms are defined in 45 Pa.C.S. § 101 (relating to definitions), not including magazines. The term "newspaper" also includes any printed advertising materials circulated with such newspaper regardless of where or by whom such printed advertising material was produced.

(7) The sale at retail or use of caskets and burial vaults for human remains and markers and tombstones for human graves.

(8) The sale at retail or use of flags of the United States and the Commonwealth of Pennsylvania.

(9) The sale at retail or use of textbooks for use in schools, colleges and universities, either public or private, when purchased in behalf of or through such schools, colleges or universities provided such institutions of learning are recognized by the Department of Education.

(10) The sale at retail or use of motion picture film rented or licensed from a distributor for the purpose of commercial exhibition.

(11) The sale at retail or use of mail order catalogs and direct mail advertising literature or materials, including electoral literature or materials, such as envelopes, address labels and a one-time license to use a list of names and mailing addresses for each delivery of direct mail advertising literature or materials, including electoral literature or materials, through the United States Postal Service.

(12) The sale at retail of horses, if at the time of purchase, the seller is directed to ship or deliver the horse to an out-of-State location, whether or not the charges for shipment are paid for by the seller or the purchaser.

(13) The sale at retail of supplies and materials to tourist promotion agencies, which receive grants from the Commonwealth, for distribution to the public as promotional material or the use of such supplies and materials by said agencies for said purposes.

(14) The sale at retail or use of materials used in the construction and erection of objects purchased by not-for-profit organizations for purposes of commemoration and

1 memorialization of historical events, provided that the
2 object is erected upon publicly owned property or property to
3 be conveyed to a public entity upon the commemoration or
4 memorialization of the historical event.
5 (15) The sale at retail or use of candy or gum
6 regardless of the location from which the candy or gum is
7 sold.
8 (16) The sale at retail or use of horses to be used
9 exclusively for commercial racing activities and the sale at
10 retail and use of feed, bedding, grooming supplies, riding
11 tack, farrier services, portable stalls and sulkies for
12 horses used exclusively for commercial racing activities.
13 (17) The sale at retail to or use by a construction
14 contractor of building machinery and equipment and services
15 thereto that are:
16 (i) transferred pursuant to a construction contract
17 for any charitable organization, volunteer firemen's
18 organization, volunteer firefighters' relief association,
19 nonprofit educational institution or religious
20 organization for religious purposes, provided that the
21 building machinery and equipment and services thereto are
22 not used in any unrelated trade or business; or
23 (ii) transferred to the United States or the
24 Commonwealth or its instrumentalities or political
25 subdivisions.
26 (18) The sale or use of used prebuilt housing.
27 (19) The sale at retail to or use of food and
28 nonalcoholic beverages by an airline which will transfer the
29 food or nonalcoholic beverages to passengers in connection
30 with the rendering of the airline service.
31 (20) The sale at retail or use of separately stated fees
32 paid pursuant to 13 Pa.C.S. § 9525 (relating to fees).
33 (21) The sale at retail or use of investment metal
34 bullion and investment coins. "Investment metal bullion"
35 means any elementary precious metal which has been put
36 through a process of smelting or refining, including, but not
37 limited to, gold, silver, platinum and palladium, and which
38 is in such state or condition that its value depends upon its
39 content and not its form. "Investment metal bullion" does not
40 include precious metal which has been assembled, fabricated,
41 manufactured or processed in one or more specific and
42 customary industrial, professional, aesthetic or artistic
43 uses. "Investment coins" means numismatic coins or other
44 forms of money and legal tender manufactured of gold, silver,
45 platinum, palladium or other metal and of the United States
46 or any foreign nation with a fair market value greater than
47 any nominal value of such coins. "Investment coins" does not
48 include jewelry or works of art made of coins, nor does it
49 include commemorative medallions.

50 Amend Bill, page 149, lines 15 through 30; pages 150 through

161, lines 1 through 30; page 162, lines 1 through 5, by striking out all of said lines on said pages and inserting

(RESERVED)

Amend Bill, page 162, line 15, by striking out "at midnight December 31, 2012" and inserting

January 1, 2013

Amend Bill, page 162, line 28, by striking out "authorized under Chapter 3"

Amend Bill, page 162, line 29, by striking out "5" and inserting

3

Amend Bill, page 163, line 1, by striking out "under Chapter 5"

Amend Bill, page 163, line 2, by striking out "5" and inserting

3

Amend Bill, page 163, line 3, by striking out "under Chapter 3"

Amend Bill, page 163, line 15, by striking out "reduce the amount of" and inserting

fund the annual debt service payments for

Amend Bill, page 164, line 2, by striking out "reduce the amount of" and inserting

fund the annual debt service payments for

Amend Bill, page 165, line 9, by striking out "Department of Revenue" and inserting

department

Amend Bill, page 165, line 16, by striking out "Department of Revenue" and inserting

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1 department

2 Amend Bill, page 165, line 20, by striking out "Department of

3 Revenue" and inserting

4 department

5 Amend Bill, page 166, line 1, by inserting after "from"

6 school

7 Amend Bill, page 166, line 2, by striking out "tax" and

8 inserting

9 taxes

10 Amend Bill, page 166, line 2, by striking out "2011-2012" and

11 inserting

12 2012-2013 less the amount necessary to fund the annual
13 debt service payments for its outstanding debt in
14 existence on December 31, 2011

15 Amend Bill, page 166, line 19, by striking out "321" and

16 inserting

17 401

18 Amend Bill, page 166, lines 21 through 29, by striking out

19 all of said lines and inserting

20 (2) All revenue transferred to or received by the
21 property tax relief fund under:
22 (i) 4 Pa.C.S. § 1408(e) (relating to transfers from
23 State Gaming Fund); and
24 (ii) 4 Pa.C.S. § 1409 (relating to Property Tax
25 Relief Fund).

26 Amend Bill, page 167, line 9, by striking out "(a)

27 Initial.--For fiscal year 2012-2013, the" and inserting

28 The

29 Amend Bill, page 167, lines 20 through 22, by striking out

30 all of said lines

31 Amend Bill, page 168, line 3, by striking out "into the

32 Education Stabilization Fund" and inserting

33 as provided in section 782

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1 Amend Bill, page 169, lines 26 through 29, by striking out
2 all of lines 26 through 28 and "(8)" in line 29 and inserting
3 (7)
4 Amend Bill, page 170, lines 3 through 6, by striking out all
5 of said lines and inserting
6 Chapter 7 and Section 1504(b)(6) shall apply January 1, 2013.
7 Amend Bill, page 170, lines 9 through 13, by striking out all
8 of lines 9 through 12 and "(3)" in line 13 and inserting
9 (1) Chapters 3 and 4 and section 1504(b)(2) and (8)
10 shall take effect January 1, 2013.
11 (2)