



Protecting Philadelphia Families While Addressing the City's Fiscal Crisis



The Search for Budget-Balancing Alternatives

The Challenge:

- Close a \$1.3 billion budget gap in the Five-Year Plan without making draconian cuts to city services.

The Initial, Revenue-Side Proposal:

- Steep increases in property taxes – up 19% overall in 2010 (and up 48% with respect to the City portion of the tax) and 14.5% in 2011 – and a three-year, 1% increase in the sales tax.¹

The Search for Alternatives:

- Council was deeply concerned about the impact of the proposed property tax hike on Philadelphia families, particularly because of the **broken assessment system** under which low-value homes are relatively overvalued, and the **economic pressures** already confronting working families due to the recession.
- Council considered numerous alternatives to the proposed property tax increase for raising additional revenue over the next five years.
- Among other key principles, Council looked for approaches that spread the revenue-raising burden across a wider pool of taxpayers in order to **decrease the cost per resident** and also were **less regressive** than the initial proposal, which, as noted below, fell disproportionately hard on low- and middle-income families.
- The following pages include analysis of the initial budget proposal and a comparison of the sales tax alternative put forward by Council with the initial budget proposal.

1: Proposed “Five-Year Financial and Strategic Plan for Fiscal Years 2010-2014,” pg. 32.



Impact on Philadelphia Families of Initial Proposed Budget

- The chart below shows the impact in Fiscal Year 2010 (“FY10”) on Philadelphia households at different income levels of the budget initially proposed by the administration.²
- As noted below, the proposed tax increases fell hardest on low- and middle-income households.
- Under the initial proposal, an average household earning \$25,000/year would have had a relative tax increase more than **two-and-a-half times greater** than an average household earning \$150,000/year.

Household Income	Additional cost from 19% property tax increase	Additional cost from 1% sales tax increase	Total additional cost	Additional cost as % of household income
\$25,000	\$305	\$81	\$386	1.544%
\$50,000	\$446	\$115	\$561	1.122%
\$75,000	\$490	\$149	\$639	0.852%
\$100,000	\$550	\$213	\$763	0.763%
\$150,000	\$676	\$235	\$911	0.607%

2: Proposed “Five-Year Financial and Strategic Plan for Fiscal Years 2010-2014,” pg. 32.



Concerns About Proposed Property Tax Increase

- Because the property tax is not tied to income or ability to pay, the proposed increase would have fallen particularly hard on **low-income or fixed-income homeowners**.
- The property tax increase would **not have been shared** by all users of Philadelphia's infrastructure and services, as non-resident workers and visitors who benefit from the same are not subject to the property tax.
- Furthermore, current property assessments are **inaccurate, inequitable** (with low-value houses being over-assessed as compared to high-value houses), and **non-uniform**.
- A recent series in *The Philadelphia Inquirer* highlighted pervasive problems at the Board of Revision of Taxes (BRT), which assess Philadelphia property values. BRT officials acknowledged that current assessments are **flawed** and some have been **rigged**.³

3: "Assessment: Broken," Mark Fazlollah and Joseph Tanfani, *The Philadelphia Inquirer*, May 3, 2009.



Concerns About Proposed Property Tax Increase

- Additionally, academic research has established that changes in property tax rates are **capitalized quickly**, meaning that they are built into property values almost immediately,⁴ unlike other taxes, which are lagging indicators.⁵
- Thus, property tax increases **quickly result in lowered property values**. Research by Wharton Professor Bob Inman indicated that a 20% increase in Philadelphia property taxes will reduce market values by 12%.⁶
- The resulting reduction in market value would have **lowered home sale prices** and, accordingly, **reduced the City's revenue** from the Real Estate Transfer Tax.
- Finally, Philadelphians already pay **higher effective property taxes** than residents and businesses in 211 of the 240 townships and boroughs comprising Bucks, Chester, Delaware, and Montgomery counties.⁷

4: "Choosing the Best Mix of Taxes for Philadelphia: An Econometric Analysis of the Impacts of Tax Bases, Tax Revenue, and the Private Economy," pg. 10, October 2003 Econsult Corp. report to The Philadelphia Tax Reform Commission.

5: "Philadelphia Tax Rates and Their Relationship to Tax Bases and Tax Revenues," pg. 20, February 2002 Econsult Corp. report to the Pennsylvania Economy League Eastern Division ("Changes in property tax rates have considerably larger effects on the property tax base than the wage tax has on the wage tax base in the near term.").

6: "Can Philadelphia escape its fiscal crisis with another tax increase?" Inman, Bob; [Business Review \(Federal Reserve Bank of Philadelphia\)](#), Sept./Oct. 92, pg. 5.

7: "City skeptical of recent data for property taxes," Dave Davies, [Philadelphia Daily News](#). April 6, 2009.



Sales Tax Alternative

- The sales tax is paid by both residents and non-residents, and thereby spreads the tax burden across a **broader base**.
- The Pennsylvania sales tax **does not apply to food, clothing, and medicine**, and, as a result, is **less regressive** than a typical sales tax.
- The scenario below proposed: (1) continuing the proposed 1% rate increase for two additional years; and (2) borrowing against the FY13 and FY14 sales tax revenue to raise an additional \$200 million in FY10, with a reasonable assumed cost of borrowing of \$40 million.
- This alternative would help the City bridge the current fiscal crisis by providing sorely needed revenue in FY10 when the City's **cash flow need is the greatest**.

Revenue Source	FY10	FY11	FY12	FY13	FY14	Five-Year Plan Total
1% Sales Tax Increase	\$ 106,475,000	\$ 116,514,000	\$ 118,716,000	\$ 120,000,000	\$ 120,000,000	
Borrowing against FY13 and FY14 Revenue	\$ 200,000,000	N/A	N/A	N/A	N/A	
Annual Total	\$ 306,475,000	\$ 116,514,000	\$ 118,716,000	N/A	N/A	\$ 541,705,000



Impact on Philadelphia Families of Sales Tax Alternative

- The chart below shows the impact in FY10 on typical Philadelphia households at different income levels of the “Sales Tax Alternative,” in combination with the City achieving \$25 million/year in efficiency savings.
- **The average household at all income levels would pay significantly less** under this proposal than under the initial budget proposal.
- Furthermore, because the proposal did not include the inequitable property tax, tax burden would be **spread more evenly** between households at different income levels.

Household Income	Additional cost from 1% sales tax increase	Savings versus proposal	Additional cost, as % of household income, of Sales Tax Alternative + Efficiency Savings (vs. initial proposal)
\$25,000	\$81	\$305	0.324% (vs. 1.544%)
\$50,000	\$115	\$446	0.230% (vs. 1.122%)
\$75,000	\$149	\$490	0.199% (vs. 0.852%)
\$100,000	\$213	\$550	0.213% (vs. 0.763%)
\$150,000	\$235	\$676	0.157% (vs. 0.607%)