The School Tax Relief Program: Bad for Business

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Businesses in New York State should be up in arms about the School Tax Relief program, also known as STAR.

The problem does not lie with that part of STAR that is being implemented this year, namely the property tax exemptions for to low-income elderly homeowners. These exemptions have caused administrative nightmares for assessors but they do not cost very much and are, in principle, a good idea.

Instead, the problem lies with the property tax exemptions given to all homeowners, which will be phased in over the next few years. These exemptions will result in higher property taxes on business and will magnify New York State’s biggest educational problem, namely the relatively low performance of big cities and other poor school districts.

STAR will raise property taxes on business because it gives voters a powerful incentive to spend more on schools. By shifting a share of property tax payments from homeowners to the State, the STAR exemptions lower the effective price of education for local voters. We estimate that the average price cut will be 37 percent. Just as a cut in the price of coffee induces people to buy more coffee, this large cut in the price of education will eventually induce voters to raise educational spending. We estimate that, on average, spending will increase 14 percent and the school tax rate will increase by one-third, thereby significantly boosting taxes on commercial and industrial property.

Because the State’s STAR reimbursements increase with local property tax rates, these rate increases would also boost the cost of STAR by up to one-third above the official $2.24 billion estimate. Business will, of course, pay its share of the state taxes needed to finance this $3 billion
program. Thus, STAR will increase both local and state taxes on business. From a business perspective, STAR is the opposite of tax relief.

STAR contains provisions designed to minimize local school tax increases, but these provisions are far too weak to be effective. One provision, tax-freeze aid, gives districts a financial incentive to keep down rate increases, but its budget is so small that it will be swamped by the incentive to increase property taxes associated with the STAR exemptions. Another set of provisions restrict growth in contingency budget caps, but these caps are only relevant when voters do not approve spending increases.

Business also should care about the large disparities in educational performance between city and suburban districts because they have a large negative impact on the quality of the future workforce in the state. Unfortunately, STAR will magnify these educational disparities because it will shift resources away from city schools toward suburbs. This shift occurs primarily because STAR ignores renters and gives higher exemptions to homeowners in higher-wealth counties. According to the New York Division of the Budget, downstate suburbs enroll only 19% of the students in the state but will receive 32% of the STAR payments. In contrast, the big five cities in the state enroll 43% of the state’s students but their share of the STAR payments will be only 30%. In terms of payments per pupil, STAR will provide $1,646 in downstate suburbs, compared to only $889 in upstate suburbs, $623 in New York City, and $548 in the three large upstate cities. Cost-conscious business groups should be very leery of a $3 billion program that gives so much assistance to school districts that do not need the help at the expense of the truly needy districts.

Some business groups may be tempted to prevent increases in their taxes by pushing for a statewide school property tax limitation. This would be a grave mistake because it would freeze in place existing disparities in local revenue and associated disparities in educational performance. Instead, business groups should support reforms that minimize the incentives for wealthy school districts to raise their taxes. These reforms include the elimination of the higher exemption level in downstate districts and the introduction of a cap on STAR reimbursements. This cap should vary inversely with a district’s wealth and income, so that the state would not subsidize spending increases in wealthy
districts. To raise the long-run quality of the state’s workforce, business groups might also want to support changes in state aid programs and in school management practices that can boost the performance of city schools.

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