

REPORT BY THE SENIOR CITIZENS CIRCUIT BREAKER
TAX CREDIT REVIEW SUBCOMMITTEE

November 4, 2010

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Missouri Tax Credit Review Commission

Report of the Senior Citizen Circuit Breaker Tax Credit Review Subcommittee

What follows in this memorandum is the report and recommendations of the Senior Citizens Circuit Breaker Tax Credit Subcommittee (the "Subcommittee") which is hereby submitted to the Tax Credit Review Commission (the "Commission") on November 4, 2010. This Report and the attachments hereto have been submitted in the hope that it will give the Commission guidance and explain the Subcommittee's reasoning in making the recommendations which hereafter follow.

I. Introduction

The Senior Citizens "Circuit Breaker" Tax Credit is governed by Sections 135.010 through 135.030 of the Revised Statutes of Missouri (the "Credit"). The Credit may be claimed by senior citizens, disabled Veterans, persons who are 100% disabled, and certain widows and widowers.¹ A "claimant" of the Credit must meet specified criteria in order to claim the Credit. However, the Credit may be claimed only if the eligible claimant either owns or rents a residential dwelling. The Credit first became effective for calendar year 1973² and was last modified by Senate Bill No. 711 in 2008. The eligibility of tenants ("Renters") to claim the Credit has existed since the date the statute first was enacted.

The Credit gradually phases out as a claimant's income increases such that once a claimant's income (as adjusted) exceeds \$30,000 for individual property owners and \$27,500 for Renters, no credit can be claimed. If the claimant's income is less than \$14,300, then the full Credit is awarded, assuming property tax liability meets or exceeds the credit amount. The Credit phases out as income rises from this minimum base of \$14,300 to the "maximum upper limit" specified in the statute.³ The Missouri Department of Revenue has promulgated a number of explanatory documents including a chart which helps with the computation of the credit to which a claimant may be entitled. Copies of these helpful DOR documents are attached.⁴ When the Commission was first constituted, this Credit was not on the list of credits to be examined and reported on by the Commission. After the Commission's creation, and on or about October 21, 2010, the decision was made to add to the Commission's tasks recommending whether the Credit should be modified.

¹ Section 135.010(1) RSMo.

² HB 149 (1973).

³ Section 135.030 RSMo.

⁴ See attachments 2, 3, and 4 to this Report.

A. **Purpose:** The purpose of the Credit cannot be gleaned from any legislative history. However, it seems obvious that Missouri's motivation in adopting the Credit was not that different than the motivation influencing approximately 18 other states in the U.S. which have adopted other programs to ameliorate the effect of real estate taxes on senior citizens. The typical explanation of a "circuit breaker" tax credit such as Missouri's is as follows:

"Property tax circuit breakers, like the electrical devices that shut off electric power to prevent circuits from overloading, prevent property taxes from "overloading" a family budget by "shutting off" property taxes once they exceed a certain share of the family's income."⁵

Programs similar to the Credit are offered in 18 states in a variety of different forms and with different criteria.⁶ The primary impetus for such programs is the perceived unfairness (disproportion) of the real estate taxes paid by low income families. In 2002, low income families paid an average of 3% of their income in property taxes whereas wealthy taxpayers paid less than 1%.⁷ Accordingly, circuit breaker programs are designed to ameliorate this disproportion.

Presumably the addition of Renters to this Credit was based on the belief that some component of rent is attributable to the real estate taxes payable by the landlord.

The most sympathetic example given as the rationale for property tax relief is an elderly couple who has lived in their house for a long time and who finds the increase in property taxes over the years increasingly burdensome because they are living on a fixed income. The hope is that the relief will allow that couple to remain in their residence.

B. **Nature of Credit:** The Credit is not an economic development credit, but rather is a social welfare type credit. However, a good argument can be made that by providing the funds which allow property tax payers to remain in their residences also benefits the current economy of the state by not adding another residence to the long list of dwellings for sale during the current recessionary period. Economic studies seem to indicate that for every \$100 increase in annual property taxes, there is a 0.76% increase in the average two-year mobility rate of senior citizens.⁸

⁵ Lyons, Farkas, and Johnson, *The Property Tax Circuit Breaker: And Introduction and Survey of Current Programs*, Center on Budget and Policy Priorities, March 21, 2007.

⁶ *Id.* at page 2.

⁷ Institute on Taxation and Economic Policy, *ITEP Guide to Fair State and Local Taxes*, February 2005.

⁸ Shan, *Property Taxes and Elderly Mobility*, Finance and Economic Discussion Series, Divisions of Research and Statistics and Monetary Affairs, Federal Reserve Board, 2008-50.

Economists consider this increase to be economically significant. However, it is not possible to refine the data to eliminate all other possibilities. Nevertheless, at least intuitively and empirically, it makes sense that if a homeowner wishes to remain in his or her residence, lacks the ability to do so but for a government subsidy, and the cause of the economic distress is sufficiently compelling, that government has a role to play. Thus, in this circumstance, not only the societal goal of preserving homesteads for elderly citizens as well as the beneficial economic effect of doing so are reasons to support this Credit.

The Credit's benefits are much more difficult to ascribe to the component of the Credit attributable to reimbursing Renters. It is impossible to ascribe to that portion of the Credit paid to tenants any beneficial economic effect (except, of course, to the extent that it allows certain landlords to maintain higher rents than might otherwise be the case).

C. **Statistical and Anecdotal Information:** Attached to this report are summaries of financial data obtained from the Missouri Department of Revenues database as to persons claiming the Credit and the economic effect of the Credit upon the state in calendar years 2008 and 2009. Similar statistics are available for previous years, but the two years of data attached provide meaningful insights into how this Credit works and reasonable inferences to be drawn, to-wit:

1. In 2008, the credits claimed under the Circuit Breaker statute totaled \$114,536,560. These credits were utilized slightly more by Renters than by property owners. In 2008, \$59,197,314 of the credits were claimed by Renters versus \$53,886,455 by property owners.

2. In 2009, the percentage of credits claimed by owners and Renters was nearly identical. A total of \$115,891,430 of credits were claimed, \$56,638,297 by Renters, and \$57,837,289 by owners.

3. Of particular significance is the fact that in 2008, that portion of the credits claimed by Renters, claims filed by 100% disabled persons were in greater dollar amounts than those who were senior citizens (\$31,206,102 versus \$26,991,902). Conversely, owners of residences based their claims on being senior citizens instead of being disabled (\$45,288,025 of credits for seniors versus only \$7,286,145 based on disability). The "significance" of this statistic is that it implies that even though they are much smaller in number, disabled persons are completing and filing claims much more frequently than seniors. This, in turn, implies that they are receiving assistance in doing so. The Subcommittee believes that it is reasonable to assume that the various nursing homes and assisted living facilities within the state that are for-profit make it a practice to encourage their residents in this regard. Finally, the Subcommittee believes that those residential facilities that engage in this practice probably are facilities that have benefitted under other state tax credit programs. Thus the Subcommittee believes that the DOR should try to discern from its database whether these suspicions are well-founded, and if so, furnish those

statistics to the Governor and Legislature so that the new policies governing the Renters' Credit or equivalent benefit can be informed by same.

4. Anecdotal reports communicated to both the Department of Revenue and to various legislators indicate that many persons claim the Credit only after being assisted in filling out the necessary paperwork by representatives of the particular residential complex in which they are a tenant. These same anecdotal reports indicate that the amounts of these credits (when collected) are turned over to the various nursing homes, apartment units, etc., as payments towards rent otherwise due (or perhaps in addition).

5. The Credit currently costs the state more than \$115,000,000 per year. It is projected that it will do so for the foreseeable future if it is not modified.

6. There are other housing assistance programs designed to address the same apparent need that the Renters' Credit addresses. Such programs are the Low Income Housing Tax Credit, federal, state, and local assistance programs, etc. The risk that eliminating the Renters' Property Tax Credit would result in the loss of a residence to a disabled or senior tenant seems to be minimal given the existence of these alternate programs.

II. **Recommendation**

The Subcommittee recommends that the portion of the Credit which benefits Renters be eliminated or substantially modified. Accordingly, the Subcommittee believes that the priority category of the Credit is category "B," i.e., a tax credit which, if continued, needs modification. Benefits accruing to Renters under this Credit need to be replaced with a different structure as hereafter described. The Subcommittee does not believe that the portion of the Credit which grants benefits to homeowners who are senior citizens, disabled, or who otherwise are eligible for benefit under the Credit should be modified. Instead, the credits for property owners should be preserved as presently structured. The Subcommittee believes that the portions of the Credit which define the benefit available to senior citizens, disabled veterans, 100% disabled persons, and widows/widowers, and who are owners of residential dwellings are well written, well administered, and do not require modification. Accordingly, what follows in the balance of this report is a discussion of the considerations involved in eliminating, restructuring, or substantially modifying the Credit as it applies to Renters.

III. **Discussion of Alternatives**

The Subcommittee recognizes that its recommendation as set forth above will generate consternation in many circles. The Subcommittee is not unmindful of the pressing need many persons have who rent and do not own their dwellings. The Subcommittee's recommendation of a modification to the benefits afforded these persons is not intended to denigrate or minimize the financial distress many of them experience on a day-to-day basis; rather the Subcommittee hopes that

any benefit provided to these persons will be rationalized, equalized, and structured to conform to a clear legislative intent and purpose. As presently structured, the Credit's benefits to tenants are unequal and do not appear (to the Subcommittee at least) to have a sufficient basis to be continued in its present form.

A. **Present Credit Structure for Tenants:** Renters have been beneficiaries under this statute since the date of its inception. In 1972, Missouri voters approved a Constitutional amendment (Article X, Section 6(a) to the Missouri Constitution) which allowed the General Assembly to "provide for certain tax credits or rebates" for payments of real property taxes in the form of "comparable financial relief . . . [to those benefits afforded homeowners] to persons . . . who occupy rental property as their homes." In 1973, the General Assembly created the Senior Citizen Property Tax Credit Program. Under this original program, owners of homesteads and Renters making less than \$7,500 could claim a credit of up to \$400 to offset property taxes accrued or rent constituting property taxes accrued. "Rent" was defined as being 18% of the gross rent paid by the claimant.

In 1982, voters amended the Constitution to strike the age qualification of 65 from this Section. The General Assembly subsequently expanded the Credit to persons who were disabled veterans, 100% disabled individuals, and claimants 60 years or older who receive surviving spouse social security benefits, and later increased the minimum base and maximum upper limit of income under the program. In 2008, the general assembly expanded the benefits of the program for owners of homesteads by raising the income exemption from \$2,000 to \$4,000 and increasing the maximum award to \$1,100 to homeowners, but leaving the then maximum award at \$750 for Renters. The 2008 amendments to the statute did not benefit Renters, but did not reduce those benefits either.

B. **Anomalies Under the Statute:** Renters entitled to claim the Credit are only those persons who pay "arms length" rental to landlords during the year.⁹ The Credit is not available if the landlord does not pay real estate property taxes.¹⁰ The Credit for Renters is (at least initially) equal to 20% of the gross rents paid by the Renter to the landlord.¹¹ These criteria prompted the following comments and concerns from the Subcommittee:

1. There does not appear to be any rational relationship between the 20% of gross rent paid and the actual property taxes attributable to that tenant's rent. Among the Subcommittee members, it was the common belief that much less than 20% (and probably less than 10%) of a tenant's rent would be attributable to that Tenant's share of real estate taxes due with respect to the property rented.

⁹ Section 135.010(3) RSMo.

¹⁰ Missouri Department of Revenue "Frequently Ask Questions;" 2009 Form MO-PTC, Line 10; 2009 Missouri Property Tax Credit Claim Instructions MO 860-1782 (10-2009), page 2.

¹¹ Section 135.010(7) RSMo.

2. Many nursing homes, assisted living facilities, and apartments for older adults are owned by non-profit corporations or associations. None of these tenants would be eligible to claim the Credit even though their incomes would be similar to those allowed to claim the Credit.

3. Rent in a particular market is determined by many factors (supply and demand, competition, land costs, utility costs, costs of providing additional services, municipal services, etc., etc.). The Subcommittee does not believe that property taxes have any significant effect on rents; rather landlords tend to charge as much as the market will allow them to charge and still maintain relatively full occupancy.

4. Real estate taxes on apartments vary widely throughout the state, and each area's property tax rates vary as well. The Credit is a "one size fits all" Credit which does not differentiate based on true economic circumstances of Renters in a particular vicinity.

5. Many of the facilities which provide housing to Renters who qualify for the Credit are facilities which enjoyed the low-income housing tax credit (state and federal) and perhaps the historic rehabilitation tax credit (state and federal). Other credit programs also may have been applicable to the facility. These tax credits were designed to reduce the cost of the low-income housing facility for elderly or disabled tenants, and thus, in a very real sense, the tenants in those facilities are already receiving the benefit of the state's contribution towards their housing costs. The Subcommittee did not believe that it was appropriate for tenants in facilities whose rent is already subsidized (through other tax credit programs) to be able to benefit under this Credit as well.

6. In short, the Renters able to claim the Credit do not represent a fair distribution of persons throughout the state similarly situated; instead they are persons who have been arbitrarily selected by the language of the statute for the Credit's benefit, even though others virtually identically and similarly situated lease their dwellings from non-profit (property tax exempt) landlords.

C. **True Purpose of Renter's Credit:** The Subcommittee believes that it is not reasonable to conclude that there is a logical and consistent nexus between property taxes paid by a for-profit landlord and the need to provide a subsidy to that landlord's tenants. Instead, a Renter's use of the Credit should be seen for what it is, i.e., a subsidy to lower income persons who meet the criteria of either being disabled or over 65, even though other persons in the same economic circumstance are not eligible for a similar benefit. Thus the Subcommittee believes that if a subsidy is to be provided to persons close to the poverty line or below it, then that subsidy ought to be a grant which is subject to the appropriation process and which achieves what the legislature and Governor believe is its rightful priority among all of the other funding needs of the state. Arbitrarily selecting that benefit for only those persons who rent from for-profit landlords, even though they are already living in a rent assisted facility, does not make economic sense.

D. **Alternatives:** The Subcommittee does not believe that the elimination of the Credit in favor of Renters should occur without there being some attempt to reconcile and ameliorate the distressed economic condition of the poorest among us. Such a grant program could be administered in the same manner as a tax credit program, but be subject to the appropriations process. A rent subsidy for non-property owners who pay rental may be appropriate in this regard, but perhaps tenants in low-income housing tax credit type developments should be ineligible to claim this benefit. Perhaps the benefit should be awarded regardless of where the tenant lives if the income that tenant receives is sufficiently low. In any event, the Subcommittee considered possible modifications to the existing Credit scheme for Renters in lieu of a complete termination of a Renters' credit, to-wit:

1. The Renters credit could be reduced such that only 10% of a tenant's gross rent was taken into account up to a maximum of \$500. This approach would be simple, but would perpetuate the problems with the Credit described above, even though at a lower level of reimbursement.

2. Tenants living in housing developments built with the use of low-income housing tax credits might be deemed ineligible to claim the Credit.

3. A formula could be devised whereby only the actual component of the tenant's rent which was truly attributable to real estate taxes would be taken into account. This would require the disclosure by the landlord of the landlord's gross rents received from all tenants as well as the landlord's actual real estate taxes paid. Many landlords might be uncomfortable in or unwilling to divulge this information. Such information might very well lead to a reassessment of the landlord's property if the landlord were required to divulge that information to any tenant, and in order to make such a formula workable, a landlord would have to be required by statute to make that disclosure.

E. **Rejected Alternatives:** The Subcommittee discussed, considered, but ultimately rejected the following additional modifications to the Credit, to-wit:

1. The possibility that some claimants might have a substantial net worth and yet low adjusted gross income was considered. In other words, the Subcommittee considered whether to recommend that a "means test" be introduced so that persons whose net worth was sufficiently large would not be eligible for the Credit, regardless of the amount of their adjusted gross income. Alternatively, the Subcommittee considered whether to disallow the Credit if the Credit was going to be applied to a sufficiently valuable residence. Ultimately, the Subcommittee rejected both of these approaches because verifying a claimant's net worth or determining whether a particular residence was "too valuable" would involve a substantial bureaucratic expense, and it was the impression of the Subcommittee that these type of abuses would be relatively small in number and therefore not very costly to the state.

2. Another approach considered by the Subcommittee was to disallow cash refunds below a certain dollar amount, i.e., require that before a check would be issued by the Department of Revenue, the amount of refund or distribution amount be sufficiently large to warrant the cost of preparing the check. However, the Department of Revenue members advises that the cost of processing a claim under the Credit is about \$2.50 per refund (credit) check issued. The Subcommittee did not consider this cost to be sufficiently large to warrant any type of threshold for a refund.

3. The Circuit Breaker Tax Credit burdens the state while at the same time benefitting local governments. The property tax which is related to the Circuit Breaker Credit is an important source of revenue for local governments. By allowing the local governments to keep the real estate taxes that the state refunds through this Credit is, in effect, an indirect subsidy by the state of local governments. The Subcommittee considered whether there should be some sharing of the cost of these credits by requiring that some portion of the Credit attributable to a particular local government be refunded to the state by the local government. This approach ultimately was rejected because of the fact that most property taxes benefit elementary and secondary public schools, and a reduction in property taxes paid to those schools would, in the final analysis, have to be made up by the state anyway. The utility of reducing the local government's share of property taxes would be nonexistent.

IV. Conclusion

Perhaps it is a measure of the desperate financial straits in which the State of Missouri now finds itself that we must seriously consider cutting a state benefit to those who are truly the "least among us."¹² Of course this reduction in aid presumes that there are literally no other sources more deserving of reduction or elimination than this Credit. The Subcommittee does not believe this to be the case, i.e., while the Subcommittee believes that the Credit in favor of Renters should be revised, studied, and more directly and fairly apportioned, it does not mean that the Subcommittee advocates cutting benefits to this class and demographic of persons. Instead, the Subcommittee recommends that a considerable refinement and more precise targeting of these funds be considered and that the senior citizen property tax credit benefit only those persons who are homeowners.

Respectfully submitted,

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¹² Christian Bible, Matthew 25:40.

**LIST OF ATTACHMENTS
TO REPORT BY
SENIOR CITIZENS CIRCUIT BREAKER TAX REVIEW SUBCOMMITTEE**

1. Property Tax Credit statutory language
2. Eligibility Chart, Property Tax Credit, Missouri Department of Revenue
3. Missouri Department of Revenue, FAQs, Property Tax Credit
4. Missouri Property Tax Credit Claim Instructions, MO 860-1782 (10-2009)
5. Property Tax Credit Utilization Statistics, 2007-2009
6. Lyons, Farkas, and Johnson, *The Property Tax Circuit Breaker: And Introduction and Survey of Current Programs*, Center on Budget and Policy Priorities, March 21, 2007
7. Institute on Taxation and Economic Policy, *ITEP Guide to Fair State and Local Taxes*, February 2005
8. Shan, *Property Taxes and Elderly Mobility*, Finance and Economic Discussion Series, Divisions of Research and Statistics and Monetary Affairs, Federal Reserve Board, 2008-50
9. Historical materials related to enactment of the Property Tax Credit