

From The Morning Call
April 29, 2007

The climb to high taxes

By Spencer Soper Of The Morning Call

Twenty years ago, the average Pennsylvania family forked over \$6,871 in taxes to state and local governments. That was \$550 less than the typical American family, or enough savings for a nice lawn mower.

This year, that same family will pay \$11,013, or \$41 less than the national average.

Forget that new lawn mower. The difference today might buy a few bags of fertilizer.

An analysis of statistics and projections by The Morning Call found that there was once a considerable gap separating the state and local tax burden for Pennsylvanians with that of the average American. It reflected long-held beliefs about government's place in a state with industrial roots. Keep government humble. Keep taxes down. The economy will take care of itself.

But the gap has narrowed, most acutely since 2000, and today is merely a fraction of a percent. The trend is not just a result of higher taxes. Population stagnation and slow income growth also played a role. The combined effect shows Pennsylvanians losing ground to the average American, and their incomes aren't keeping pace with their tax bills.

Gov. Ed Rendell's budget plan, which includes a series of tax hikes to shore up the state budget and expand programs, would continue Pennsylvania's path from a low-tax to a high-tax state. If his budget passes, Pennsylvanians next year likely would pay more in state and local taxes than the average American for the first time in at least 38 years.

The trend underscores changes that are redefining Pennsylvania's political foundation and its government's reach into pocketbooks. The change can't be attributed to any single cause. Instead, it's been a response to demographics and government spending.

But the result is clear: Government is emerging from the shadows to take a more aggressive role in shaping the state's economy and its residents' quality of life. And it is taking a greater share of your income to do it.

"Historically, Pennsylvania has been an entrepreneurial, individualistic political state," said Michael Young, a public policy analyst in Harrisburg. "Government was frowned upon, spending was tightly controlled and business ran the show."

"The state's culture is slowly changing," he said. "Essentially, the more developed an economy gets, the more dependent it is on government spending."

Feeling the squeeze

Haycock Township resident Helen Kondracki, 74, is struggling to pay the growing burden.

She worries rising taxes could force her out of the house she and her husband built in Bucks County more than 30 years ago. They get by on their pensions and Social Security, but taxes take more of that money every year. Most

of their retirement income is exempt from state income taxes, but rising property tax bills are taking a toll.

When adjusted for inflation, her property tax climbed 73 percent to \$4,016 in the 20 years up to 2006. Personal incomes in Pennsylvania over that time rose 34 percent.

"My taxes are like a tsunami, the way the rates have gone up," Kondracki said. "We're falling further and further behind."

The rising taxes have stretched her fixed income so much that it is difficult to pay her other household expenses. There was a recent heating oil delivery and car repair, as well as financing payments on a new heating system. To save money, they've already cut back on trips to visit a daughter in Kentucky, and rather than vacation, they take walks in nearby Nockamixon State Park.

Her handy husband, who once could fix everything, is 79 now, and less able to scramble up a ladder to clean the gutters or maneuver beneath the sink to stop a leak. Meanwhile, things in their brick-and-stucco house are starting to go.

"It's tough on senior citizens," she said. "We grew up with our pensions and Social Security based on incomes in previous decades, but our taxes are based on this decade."

Climbing the ladder

As recently as 2000, Pennsylvania ranked 37th in the nation in terms of its state and local tax burden, according to the Tax Foundation, a nonpartisan group that monitors government finances. In 2007, the state ranked 24th, jumping past such states as Virginia, South Carolina, Mississippi, Georgia and New Mexico, according to the group.

The group calculates tax burden by looking at all state and local taxes as a percentage of state income. The rank factors all taxes, including property, income and sales taxes residents pay directly. It also factors taxes paid by businesses that are arguably passed along to consumers in what they pay for goods and services.

The ranking factors local property taxes and other levies established by school districts and municipalities. So the shift, which largely occurred during the terms of three governors since 2000, is not entirely attributable to the state.

If the Legislature approves Rendell's budget proposal, Pennsylvania will edge even closer in the rankings to its Northeast neighbors New Jersey, New York and Connecticut, which consistently top the tax burden list.

"It's going to move Pennsylvania significantly," said Curtis Dubay, an economist with the Tax Foundation. "It's a substantial increase that will increase the burden on taxpayers."

The budget package reflects an aggressive government growth campaign by the Democratic governor, and a belief that investing in social programs and economic development outweighs the need to keep taxes down. Rendell's budget predicts the long-term benefits of government investment are greater than the upfront tax cost.

The typical household would pay an extra \$168 in sales tax each year to shore up the state budget and bankroll property tax reductions. Residents would pay an additional \$6 a year for garbage disposal to pay for environmental programs and hazardous waste clean-ups, and \$5 for electricity to pay for alternative power programs and energy conservation. Smokers would cough up another 10 cents a pack to help expand a state-subsidized health insurance program for adults.

Rendell "sees government playing a role in being able to improve the quality of life, and it needs resources to do that," said Chris Borick, director of the Muhlenberg College Institute of Public Opinion. "To find ways to get the resources and revenue to fund those initiatives, he's been aggressive in terms of his tax policies."

The proposed budget is engineered in a way that makes it difficult to determine the impact on any individual. Some taxes would go up while others go down, but the overall result is more money for government and higher overall taxes for residents.

The Rendell administration cites a different pressure on the state budget: federal funding reductions. Since 2003, Pennsylvania has lost \$2 billion in federal funding that pressured the state to pay for programs for the needy. Much of the growth in state spending represents backfilling money the federal government no longer provides, the administration says.

Steve Kniley, a spokesman for the state's Department of Revenue, said Rendell aims to create a fair, stable tax structure that provides essential services, not the state's position in the Tax Foundation's ranking.

And he countered that any climb in the ranks could be countered by an estimated \$1 billion in gaming revenues that would be used to reduce property taxes once all of the state's new casinos open.

Demographic squeeze

Taxes alone don't explain Pennsylvania's climb up the tax-burden ladder. Population and income also play a role.

Pennsylvania is one of the slowest-growing states in the country. From 2000 to 2006, Pennsylvania's population grew 1.3 percent, lagging the national average of 6.4 percent. Pennsylvania's income growth also lagged the national pace, as higher-wage manufacturing jobs are replaced with lower-paying service jobs.

The effect is a three-way squeeze on taxpayers: proportionally fewer of them who are earning less are paying for a more expensive government.

Adding to the pressure, Pennsylvania has the third-highest percentage of residents 65 and older, behind Florida and West Virginia. Seniors require some of the most expensive welfare programs for medical care. Meanwhile, the state income tax exempts Social Security benefits and most pensions that seniors receive.

Even though Pennsylvania's population is stagnant, sprawl is rampant. A recent study by The Brookings Institution Center on Urban and Metropolitan Policy found that Pennsylvania cities are hollowing out as more of its residents move to the suburban fringes. That translates to higher tax bills because it typically costs more to deliver services to populations that are spread out, according to the study.

"Pennsylvania's economic base is not growing, but the population is moving around," said Mark Muro, an author of the Brookings Institution study. "As you abandon old places, you have costs associated with caring for that old infrastructure, and you have the cost of new services in new communities....No doubt, the state will be under extreme financial pressure."

Hitting the jackpot?

About the only thing that will work to the taxpayer's advantage is the revenue expected to pour into the state's casinos when they are all open, anticipated in 2008. Ultimately, the state expects gambling to generate at least \$1 billion a year that it would use to reduce property taxes that have soared since 2000.

Whether individual homeowners actually save on their property taxes compared with previous years will depend on school and municipal spending. And a new state law that aims to cap school district tax hikes to an inflationary index is full of loopholes.

Still, state officials are confident the state's new industry will translate into property tax savings for Pennsylvania homeowners.

"There will eventually be at least a billion dollars for property tax relief, and that's going to have a significant effect on the tax burden in Pennsylvania," said Kniley, of the state Revenue Department. "It has to."

Rendell has invested considerable political capital in reducing property taxes. It was a primary justification for legalizing gambling and lately is a key selling point for increasing the state sales tax from 6 to 7 percent.

Such an effort is not unique to Pennsylvania.

Property taxes in Pennsylvania and throughout the country began climbing rapidly in 2000. Nationally, property taxes climbed 28 percent from 2000 to 2004, much more than the 18 percent gain in the previous five-year period. In Pennsylvania, property taxes increased 24 percent from 2000 to 2004, and 14 percent from 1995 to 1999.

Across the country, political pressure has mounted to stem the rising property tax tide. Idaho, New Jersey and South Carolina passed laws to replace property tax revenues with sales taxes. This year, Florida, Arkansas and Maine are on the list of states trying to control property taxes.

"Whenever there is a public opinion survey done, property taxes are the least liked or most hated tax," said Harley Duncan, executive director of the National Association of Tax Administrators. "The reasons are, in many cases if your tax payments are not paid in escrow, it all hits at once, which puts it in contrast to payroll or sales taxes paid a little at a time."

If Pennsylvania is able to keep a lid on taxes, it would be welcome news to Kondracki. She fears that long-term hospitalization or nursing care for her or her husband would devastate them financially. When they retired -- she worked in manufacturing, and her husband was a state inspector -- they expected their pensions and Social Security would cover their bills. They didn't predict their taxes would climb so rapidly.

Sitting in her home, Kondracki worried about the future.

"If anything ever happens to my husband, there's no way I could stay here," she said. "With all of the blood, sweat and tears we poured into this place, that's what breaks my heart. I might not be able to stay here in a couple of years because of the taxes."

spencer.soper@mcall.com

610-820-6533

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