

An Odd Love Affair With Property Taxes in New Hampshire

by Billy Hamilton



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Billy Hamilton is the executive vice chancellor and CFO of the Texas A&M University System. In 2015 Hamilton led Texas Republican Gov. Greg Abbott's Strike Force on the Health and Human Services Commission to complete a management analysis of the agency. Before

that, Hamilton was the deputy comptroller for the Texas Office of the Comptroller of Public Accounts from 1990 until he retired in 2006. He is also a private consultant, advising on numerous state tax matters.

In this installment of State Tax Merry-Go-Round, Hamilton looks at the latest school funding issues in New Hampshire.

New Hampshire is one of the smallest states in terms of square miles and population, but it distinguishes itself by having one of the oddest state and local tax systems in the country.

The state gets most of its revenue from the property tax, business taxes, and a rooms and meals tax. It also does a thriving business along its highways selling tax-free alcoholic beverages and cigarettes to visitors from neighboring states in its state-run liquor stores. It doesn't have a general sales or income tax.

The liquor stores are a major tourist attraction, along with the state's quaint towns, fall leaves, and glorious expanses of wilderness. Here's how one article described two liquor stores located across from each other just off Interstate 93 in Hooksett, New Hampshire: "Liquor Stores #66 and #67 lie on either side of the interstate. Each building also contains a mall/rest stop that incorporates a neon-

lit diner beneath a cloud-painted ceiling, a souvenir store, and a host of other small businesses — by design, there's not a McDonald's or Dunkin' Donuts in sight."¹ The state stores are offering curbside and in-store pickup during the pandemic, and sales were up 13.5 percent between March 1 and May 13, compared with the same period last year.

All in all, it's an amazing state to visit or live in, which I briefly considered doing after college, not long before I landed a job in Texas state government where my boss liked to toss in comparisons to "tiny New Hampshire" in all of his speeches, probably without ever visiting. I've visited the state, and for years, I jogged in a faded T-shirt, bought at a New Hampshire liquor store, that read: "Live Free or Die," the state's feisty motto.

With all due respect to John Denver, New Hampshire, not West Virginia, is almost heaven, give or take some hard winters and something called "frost heaves," which are unexpected (and hazardous) shifts in the road surface caused by a combination of freezing temperatures and soil defrosting. They pose periodic problems for drivers passing through New Hampshire on their way from Boston to Bangor — or at least they did when I made that trip regularly. Maybe things have changed. I haven't visited recently.

But even most almost-perfect paradises have their problems, and one of New Hampshire's problems is its oddball tax system. The problem is familiar to any state where one revenue source dominates state or local finances. Overreliance leads to rates that are too high and taxpayer unhappiness. In New Hampshire, these problems are compounded because the one tax that

¹Kara Newman, "How New Hampshire's Liquor Stores Became Must-Visit Travel Destinations," *SevenFifty Daily*, Dec. 18, 2017.

dominates both state and local finances — the property tax — turns up in survey after survey as America’s least favorite tax.

Myth and Reality

An article in the *New Hampshire Business Review* from 2018 explained the often misunderstood role of property taxes in New Hampshire’s fiscal system: “The myth in New Hampshire is that we run the state on ‘sin taxes’ — cigarettes, alcohol and gambling. The reality is that more than two-thirds of all state and local taxes in New Hampshire are property taxes.”²

As a result, property taxes are depressingly high. Recent Census Bureau data show that New Hampshire homeowners pay the third highest property tax bills in the country. The median property tax bill on a \$205,000 home (the median-priced home in the United States) is nearly \$4,500, an effective tax rate of 2.2 percent.³

Another myth is that the state, which is relatively wealthy in aggregate and independent by nature, doesn’t spend much on government. Not exactly true. A recent ranking, again using Census data, showed that state and local governments in New Hampshire spent \$8,222 per capita in 2017, a long way from the most spending per capita nationally but still higher than 11 other states: Arizona, Idaho, Indiana, Florida, Georgia, Missouri, Nevada, North Carolina, Oklahoma, Tennessee, and Texas.⁴

Over the years, various officials have offered plans to reform New Hampshire taxes, often to their subsequent political regret. The last step the state took to better balance its tax system was to add a business enterprise tax to its existing business profits tax (BPT) in 1993. The BPT, originally enacted in 1970, is assessed on business income in the state at the rate of 8.2 percent. The business enterprise tax is assessed on something called the “taxable enterprise value tax base,” which is the sum of all compensation, interest,

and dividends paid by the company, taxed at a rate of 0.72 percent.

Here’s where the imbalance comes in. While the state collects about \$1 billion or so annually combined from its second and third largest tax sources, business taxes and room and meal taxes, the state and its local governments collect more than \$3.7 billion a year in property taxes. One predictable result of that overreliance is that the state has had school funding problems for decades because property values provide a stable tax base but aren’t evenly distributed geographically. Some areas of the state are property rich and some are property poor, and school funding based on property taxation is, without state equalization, unevenly distributed. That means tax rates in poorer districts have to be higher to produce the same amount of money as rich districts. They often can’t do that without breaking taxpayers’ backs, which is a problem, both as a matter of education policy and, in New Hampshire, because of the constitutional requirement for the state to provide an “adequate education.”

Even the state’s attempts at balancing funding are a problem. If the state attempts to fund all districts to level them up to equal the richest districts, the cost is prohibitive, and if they level down to the poorest districts, it’s political suicide. So lawmakers wind up trying to strike a balance, a task at which they sometimes succeed but just as often fail, ending up in court as a result.

The state faced landmark lawsuits challenging its school funding system in the 1990s, culminating in what is known as the *Claremont II* decision in 1997, in which the New Hampshire Supreme Court ruled that a reformed system must fund basic education expenditures from a tax with a rate that does not vary across the state’s school districts.⁵ In 1999 the legislature enacted an interim funding plan centered on a temporary statewide property tax to fix the deficiency.

The price tag for providing New Hampshire students with an “adequate” education under the terms of the state constitution was set at \$825 million, but the funding plan raised only about

² Mark Fernald, “NH Has a Revenue Problem: The Property Tax,” *New Hampshire Business Review*, Aug. 3, 2018.

³ Bob Sanders, “Once Again, Property Tax Survey Puts New Hampshire Near the Top,” *New Hampshire Business Review*, Feb. 26, 2020.

⁴ Urban-Brookings Tax Policy Center, “State and Local General Expenditures, Per Capita, 2017” (Apr. 27, 2020).

⁵ *Claremont School District v. Governor of New Hampshire*, 703 A.2d 1353 (N.H. 1997).

\$725 million. Lawmakers recognized they hadn't fixed the problem, and in June 2001, nearly four years after *Claremont II* and after what one study described as "a rancorous two-year public debate," lawmakers enacted a second plan that made the statewide property tax permanent and added sufficient additional revenue to fund an adequate education.⁶

'Bare-Bones Approach'

Years have passed since the *Claremont II* reforms, and the state is once again in court over school funding. In June 2019 Cheshire Superior Court Judge David Ruoff held that the state's funding formula is unconstitutional and issued a 98-page decision painstakingly detailing his conclusions. The state appealed the decision to the state supreme court, which could hear oral arguments this fall, although no date has been set.

By the end of the year, the court is expected to hand down its decision in the lawsuit, answering the question whether the state is meeting its constitutional obligation to pay for an adequate education. The lawsuit contends it's not and should triple the amount of aid it sends to school districts.

The suit was originally brought by the Contoocook Valley School District located in Peterborough, in southern New Hampshire. Twenty-five school districts, including Concord, Manchester, and Nashua, and the state School Boards Association have joined the suit and are asking the court to set July 1, 2021, as the deadline for lawmakers to make needed reforms and "end the injustice and unfairness that continue to afflict our school children and our taxpayers," meaning they want it dealt with in next year's legislative session, which begins in January.

"The current funding formula pays for less than one-third of the actual cost of public K-12 public education in New Hampshire," the school districts argued in a recent court filing. As a result of this "bare-bones approach," they say, "local property owners have continued to pay school taxes at highly unequal rates and another generation of New Hampshire school children

has passed through school systems across the state which have been funded inequitably."

In the meantime, the legislature last year created a blue-ribbon panel of lawmakers, attorneys, former state officials, and school administrators to study and improve the funding system. The Commission to Study School Funding began meeting in January in the shadow of the court case.

New Hampshire Public Radio reported in January: "Like school funding committees before it, the 16-member commission will calculate the costs of an adequate education and recommend how the state will fund this."⁷ The commission has been hard at work, meeting 25 times as of July 1, mostly via teleconference. The members reportedly will have a final report ready by August 1.

In a recent interview, state Rep. David Luneau (D), a member of the commission, described its task from the perspective of his district, which is one of the lawsuit plaintiffs: "Students across the state don't have equitable access," he said. "That's going to be a very important mission for the work that the commission does. How do we make sure we're providing that equitable access to students and families across the state?"

In the meantime, property taxes at the state and local level have risen sharply over the years, causing a separate but related problem, which the *New Hampshire Business Review* described this way: "Since New Hampshire 'solved' the education funding crisis in 1999, the total state and local property tax bill in New Hampshire, adjusted for inflation, has increased by 58 percent, far exceeding the growth in the state's economy (37 percent), and outstripping the ability of most people to pay."

One thing on which most people agree is that at current levels, the tax is causing serious local pain in many parts of the state, as a Newport resident described in a letter to the *Concord Monitor*: "Property taxes have crippled many property-poor communities like my hometown, Newport. Families in these communities on average make nearly 20 percent less than the

⁶Daniel Swaine, "How Will New Hampshire Solve Its School Funding Problem? Part 2 of 3," *Fiscal Facts*, Federal Reserve Bank of Boston, Fall 2001.

⁷Sarah Gibson, "With Court Case Looming, Commission Begins to Examine School Funding," New Hampshire Public Radio, Jan. 24, 2020.

average median income in New Hampshire, yet they pay some of the highest property tax rates in the state. Residents are forced to spend upwards of 10 percent or more of their incomes on local property taxes. In effect, young families cannot afford to live in Newport and our senior citizens are forced to leave.”⁸

The Pledge

Going in a different direction — like adopting an income or sales tax — is an alternative, but it’s less obvious in New Hampshire because of “the Pledge,” a promise by politicians not to support income taxes or sales taxes or other forms of what are known as “broad-based taxes.”

You’ve probably heard of politicians nationally taking the Taxpayer Protection Pledge, which the Washington-based group Americans for Tax Reform has pushed since 1986. New Hampshire’s pledge is the original model. It first turned up in the 1950s, when Gov. Hugh Gregg used the term. It became significant politically in 1972, when Gov. Mel Thompson made it a central theme in his first campaign. In the years since, the *New Hampshire Union Leader* has made it a mission to hold politicians accountable on the Pledge. Since 1972 only one person has won the governorship without taking the Pledge: Democrat Jeanne Shaheen, now a U.S. senator, during her last reelection bid in 2000. (She took the Pledge in 1996 and 1998.)

The Pledge has become a fixture of New Hampshire politics and has effectively narrowed the state’s fiscal options to what it already has — taxes on property, rooms and meals, cigarettes, and businesses, plus its liquor store revenue and some income from gambling. The Pledge has become almost a matter of religious faith among Republicans, and Democrats aren’t much better. As one article put it: “That’s made it hard for candidates to raise the issue in campaigns — even though opinion polls suggest there’s actually no clear majority in favor of any tax issue (with some residents supporting a sales tax, some an income tax, and others no tax at all).”⁹ By bundling

⁸ Kathy Hubert, “An Example of the Education Funding Crisis,” *Concord Monitor*, July 10, 2020.

⁹ Emily Corwin, “A History of the Pledge,” New Hampshire Public Radio, *State Impact*, Oct. 10, 2012.

support for either a sales or an income tax into a single pro-tax prohibition, backers of the Pledge have successfully moved the likelihood of a broad-based tax from “implausible to nearly impossible,” Dante Scala, associate professor of political science at the University of New Hampshire, said in the article.

The Pledge is again at the center of the political action in this year’s electoral politics, and especially in the campaign for governor, which will pit Republican incumbent Chris Sununu against either Senate Majority Leader Dan Feltes (D) or Andru Volinsky, an attorney and member of the Executive Council of New Hampshire, a part of the state government that advises the governor and supposedly provides a check on his or her power. In the 1990s Volinsky also happened to have been the lead counsel in the *Claremont* school finance litigation.

Volinsky is interesting because he has refused to take the Pledge during his campaign. Instead, he has created a pledge of his own — what he calls “the pledge of the future.” It says, “If I am elected governor, I pledge not to balance the state budget on the backs of local property taxpayers, but instead I will reduce local property taxes for the majority of our state’s citizens.”

Like Sununu, Feltes has pledged to veto a sales or income tax and says he will raise revenue to lower property taxes by closing business tax loopholes. The Democratic primary is set for September 8.

“I don’t think the governor in my experience has ever talked about or tried to reduce the crushing burden of property taxes in New Hampshire,” Volinsky said in an interview after filing. “He acts as if it doesn’t apply to New Hampshire citizens. That is the top reason to replace him. And given my experience on *Claremont*, that makes me the better candidate to challenge him.”

The Property Tax-School Funding Dilemma

So gubernatorial politics will be interesting in New Hampshire this year, and to get a better understanding of how all the pieces fit together, I contacted Daphne Kenyon, a longtime New Hampshire resident who recently moved to a Boston suburb, putting her closer to her job at the Lincoln Institute of Land Policy in Cambridge.

She originally was hired by Lincoln to do a study that became the 2007 report, “The Property Tax-School Funding Dilemma.”¹⁰ She’s working on an update of the report and recently testified before New Hampshire’s school funding commission on the issue. When we talked, she underscored the intertwined relationship between the property tax and school funding. “If you think about property taxes, you have to think about school finance and vice versa,” she said.

Kenyon is an economist and has had a varied career in public finance, working for a time as a professor and department chair in economics at Simmons College; as president of the Josiah Bartlett Center for Public Policy, a New Hampshire think tank; as a consultant; and now as a senior fellow in taxation at the Lincoln Institute.

What qualifies Kenyon as a New Hampshire expert for me is her long residence and a stint on a New Hampshire town council; plus, she’s the only person of my acquaintance who’s actually lived in the state. Beyond that, she’s one of the nation’s leading experts on property taxation and the intersection of property taxes and school finance.

Kenyon also has had long experience with New Hampshire’s quirky tax politics. She revealed — she says for the first time — that in 1982 as a young Dartmouth assistant professor, she served on a secret advisory committee to advise then-Gov. Hugh Gallen during his bid for a third term as governor.

One topic of the secret advisory group was whether the governor should take the Pledge, as he did the first two times he ran for the office. “We advised him not to take the Pledge — and he lost the election,” she said. Despite the setback, Gallen continued to serve as governor until he tragically died because of a blood infection a few days before the inauguration of his successor, John Sununu, the current governor’s father.

Kenyon said the Pledge colors all of the state’s tax decisions, and politicians of all stripes ignore it at their peril. “Jeanne Shaheen is the only politician [who’s] been able to avoid taking the

Pledge in decades,” she said. Shaheen took the Pledge in her first two terms as governor, but she wanted a sales tax to deal with school funding in her third term. She still won the election, but her idea went nowhere. “That choice shadowed her political reputation for a while, but eventually she got out from under it,” Kenyon said. “She was the first governor in 30 years to win without taking the Pledge.”

Kenyon said Volinsky’s proposal is interesting. She agrees that the level of property taxes in the state is a problem, and its role in school finance has caused the state unending difficulties. She’s also well aware of the heavy burden the tax imposes on the average homeowner. “The state does have a property tax circuit breaker, which provides some relief for low- and moderate-income taxpayers,” she said. “But its benefits are meager, and it’s structured to fail.”

“Both Democratic candidates for governor want to provide property tax relief, but then what?” Kenyon asked. She said the state might squeeze some money out of the BPT or the rooms and meals tax, but increases in both those taxes combined would barely make a dent in the school property tax. “The state needs to find a better way to provide property tax relief for those who need it,” she said. But to get the most bang for the buck, the assistance must be narrowly focused. “Personally, I think that with every state, including New Hampshire, losing revenue right now, any major change in the tax system is a non-starter,” she said.

Kenyon also doesn’t see how Sununu can be beat. “People seem to be grateful to governors who have dealt successfully with the pandemic, and Sununu has done a good job so far,” she said. “Unless something happens between now and Election Day that is really bad, I suspect Sununu is unbeatable, regardless of who runs against him.”

‘A Little Bit of a Love Affair’

Despite the political and economic environment, something must be done about the state’s long-simmering school funding issues, Kenyon said, and the latest court case may settle the question by the end of the year. The problem is one of balance. “New Hampshire is a high-

¹⁰ Daphne Kenyon, “The Property Tax-School Funding Dilemma,” Lincoln Institute of Land Policy (2007).

income state, but much of the wealth is in the southern part of the state where New Hampshire is basically a Boston suburb. In the south, property values are much higher than further north. They're also higher around Dartmouth College in Hanover and along the state's 18 miles of Atlantic coastline. In the northern part of the state, where paper mills once flourished, the mills are gone, and people in that part of the state are poorer and land values are lower. Inequities in the distribution of property taxes are inevitable with this division.

"The question is whether the constitution requires the state to pay for an adequate educational system from the first dollar of spending. If that's the ruling, then the state possibly could be forced to fund the whole system statewide, and if that's the case, I don't see how they'll pay for it," Kenyon continued. If the ruling goes the other way, the state could have a normal foundation school program in which much of the funding comes from local revenue, and state resources are used to balance funding across the state. "Whatever the court decides, the remaining issues will be whether the current tax structure is sufficient to bring this long history of school funding problems to an end."

Kenyon said that in the second edition of her report, she and her coauthors will make the point that despite their reputation, property taxes are a good revenue source in some ways if not others. "The property tax is a stable funding source, particularly for school funding, but for the system to work as intended — however intended — you have to have adequate state aid added to the mix. Right now, New Hampshire's school finance system doesn't do that very effectively, it appears. Reports that rate state's school aid systems find that New Hampshire's is regressive, with more funding for low-poverty districts than high-poverty ones."¹¹

Kenyon also pointed out that New Hampshire is unique in how it approaches local tax decision-making. "It's one of the few states where the state doesn't put any limitations on local taxes," she

said, referring to the limitations many states impose on value or tax growth.¹² "So it's really local control," she said.

Towns and schools literally come up with a budget, tell the people what tax rate they want, then hold a meeting and decide what the tax rate will be. Towns in the state handle this process in a couple of ways. Some hold a meeting, and the people present vote on a tax rate. Others hold what amounts to a hearing on the issue, often televised, and then hold a formal public vote later. "In some towns, people literally watch the meeting on television, and if they want to vote, they get in their car and drive to the meeting and vote," Kenyon said, laughing.

That's possible because most towns aren't large, with a few exceptions like Manchester and Nashua. "The town I lived in had 13,000 people," Kenyon said. "That was considered big."

Kenyon said New Hampshire's problem is really simple, even if the solutions aren't: "If you rely on any tax too heavily, the weaknesses eventually come out." Where New Hampshire is concerned, she said, people get one point wrong, despite what they think. "The conventional wisdom is that people in New Hampshire hate the property tax," she said. "But looking at reality, it's hard to conclude they really hate the tax compared to the sales and income tax, which they don't even want to discuss. They may not think so, but New Hampshire has a little bit of a love affair with the property tax," she said with a laugh. ■

¹¹Bruce D. Baker, Matthew Di Carlo, and Mark Weber, "The Adequacy and Fairness of State School Finance Systems," Albert Shanker Institute and Rutgers University Graduate School of Education, p. 22 (2020).

¹²Bethany P. Paquin, "State-Imposed Property Tax Limitations: Trends and Outlook," *State Tax Notes*, Aug. 24, 2015, p. 711. Only four states — Hawaii, New Hampshire, Tennessee, and Vermont — have no major state provision limiting property taxation.