Volume 32 February 2007 Number 2

# The Utah Taxpayer

A Publication of the Utah Taxpayers Association
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February 2007 Articles



## Legislative Tax and Spending Issues

The Utah Legislature is in session until midnight February 28, considering dozens of bills that if passed would greatly impact taxpayers. Your Taxpayers Association is advocating for passage of many of these bills and opposing others.

### Bills the Association Supports

#### SB171 (Stephenson) Research Activities Credits

SB171 would simplify Utah's existing R&D tax credit, eliminate provisions which penalize high-growth companies, and encourage additional investment into Utah's growing research and development activities.

The bill will allow companies to claim 5% income tax credit on all qualified research expenses (QRE) as defined by the IRS. The current law allows companies to claim a 6% credit on incremental QREs above a base year.

SB171 will enhance Utah's reputation as the destination for research and development.

#### SJR12/SB18 (Hillyard) Use of Oil and Gas Revenues

SB18 creates the Severance Tax Holding Account and the Infrastructure and Economic Diversification Investment Account. Oil and gas severance taxes above $41 million and mining severance taxes above $9 million will be deposited in the holding account. In FY2006, the oil and gas severance tax generated $71.5 million, and the mining severance tax generated $17 million.

SJR2 is a proposed constitutional amendment. If approved, severance tax revenues in excess of the above cited thresholds will be deposited into the permanent state trust fund created in conjunction with the November 1998 settlement with tobacco companies. Interest from the trust fund can be spent annually by the Legislature. To spend the principal, three-fourths approval of each house and concurrence from the governor are needed.

#### HB148 (Urquhart) Education Vouchers

Would provide means tested vouchers for children to attend private schools.

#### SB13 (Stephenson) Tax Credits for Alternative Power Generation

SB13 reauthorizes and expands and the existing renewable energy tax credit. The credit consists of two parts

- Reauthorization of the investment credit for residential and small commercial projects in which 10% of system construction and installation costs can be claimed as an income tax credit up to a maximum of $2,000 for residential projects and $50,000 for small commercial projects. Investment credit is not refundable.
- Creation of a new production credit of 0.35 cents for each kilowatt-hour produced for large commercial projects. Credit is refundable but cannot be carried forward or carried back.

Fiscal note is $1.2 million in year one and $2.8 million in year two.

**Quote of the Month #1**

***"I don't watch the polls. I just try to do the right things for the right reasons. If I make decisions based on polls, I probably shouldn't be in office."***

- Salt Lake County Mayor Peter Corroon when asked about his decision to reject Real Salt Lake's request for taxpayer subsidies. His decision garnered a 70% support rating in the polls.

Source: *Deseret Morning News*, January 31, 2007

### Utah Taxpayers Legislative Committee Meetings

The Utah Taxpayers Association will be holding legislative committee meetings during the legislative session every Thursday at 7:00 am, in the cafeteria Beehive Room in the East Annex Capitol building. These meetings are open to all members of the association. Updated bill lists will also be available at www.utahtaxpayers.org. Please call 801-972-8814 with any questions.




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Renewable energy producers can invest in many different states. SB13 encourages these companies to invest and produce in Utah.

**SB142 (Stephenson) Expanding Sales Tax Exemption for Business Inputs**

SB142 would expand the existing sales tax exemption for business inputs to include the following industries, phased in over a four-year period:

Manufacturing (switch from SIC to NAICS)-$15.8 million
Mining (excludes oil and gas)-$7.4 million
Computer systems design-$4.2 million
Research/development in physical/engineering/life science - $0.7 million
Total after 100% phase-in- $28.3 million

Taxing business inputs discourages investment. Long-term economic growth depends on investment in high-wage exporting industries that bring wealth into the state or businesses that improve business productivity.

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**SB223 (Niederhauser) Tax Amendments**

Proposes several changes to state individual income taxes. The governor's office anticipates that 80% of taxpayers will switch to the new tax system. If passed, SB223 would reduce individual income taxes by $102 million. Even with this tax cut, government expenditures for transportation and education and almost everything else will continue to grow significantly.

**Proposed changes**

- A flat tax rate of 5%, down from the current 5.35%
- Phased-out credits
    - 6% of either federal standard deduction or itemized deductions (excl state income tax paid)
    - 6% of 75% of federal personal exemptions
  - credits are phased-out at 1.5 cents per dollar of AGI starting at $28,000 for a married couple
- No changes to the current bracketed system

The rate reduction from 5.35% to 5.0% will induce 6% of taxpayers to switch to the new system while the credits will induce 74% to switch to the new system.

Why is this a good idea?

Tax competition has been driving state individual income tax rates down. According our analysis using data from the CCH State Tax Handbook and the Federation of Tax Administrators, top marginal state individual income tax rates have decreased 25% in the past two decades:

1985 7.12%
2006 5.32%

**HB282 (Newbold) Exempting Unprepared Food Purchases from "Boutique" Sales Taxes**

HB282 would exempt unprepared food and food ingredients from local sales taxes such as mass transit, transportation, and ZAP. County-option sales taxes (0.25%) and city/local-option sales taxes (1.0%) will not be impacted by this change. "Boutique" sales taxes are bad tax policy to begin with. Dedicating general tax revenues for specific purposes is bad tax policy because government funding priorities need to compete against each other for prioritization.

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**HB89 (Morley) Government Assistance Expenditure Report**

HB89 requires the Office of Legislative Fiscal Analyst to submit to the Executive Appropriations Committee an annual report of state and federal funds expended to provide financial assistance and services to low-income individuals and families. The report would include expenditures for programs such as, Medicaid, CHIP, general assistance, TANF, food stamps, free and reduced price lunch, WIC, and unemployment insurance

**HB203 (Wyatt) Changing Local Option Sales Tax Distribution Formula**

HB203 would allow voters in counties of the third class or smaller to change the revenue distribution formula generated by the 1.0% local option sales tax.

HB203 would allow qualified counties to increase the population component in the revenue distribution formula of 1.0% local option sales tax if the following occurs:

- Two-thirds of local governments, consisting of all of the cities in the county and the county government itself, agree to submit a proposal to voters to increase the population component in the sales tax distribution formula. (Counties with seven or fewer cities would require 100% approval)
- A majority of voters in the county approve the proposal in a general election.

Real economic growth depends on attracting high wage jobs in industries that export goods and services and improve productivity and efficiency. Retail does not create economic growth but rather follows economic growth

**HB393 (Hughes) Truth in Bonding**

HB393 will require local governments to disclose to voters the property tax impact if proposed bonds are approved by voters, unless the impact is less than $15 per year on a primary residence of average value.

HB393 is a good government bill. When voting on a proposed bond, taxpayers need to know the cost of proposed bonds to their homes and businesses.

## Bills the Association Opposes

**HB102 (D. Clark) severance Tax Amendments**

HB102 would put 9% of the oil and gas severance tax revenues towards the LeRay McAllister fund, Watershed Restoration Program, and the Rangeland Program. Earmarking taxes is bad tax policy.

*HB38 would direct 15% of the transient room tax in Salt Lake County to pay for the Real Salt Lake stadium in Sandy.*

## Other Tax Related Bills

**HB38 (Newbold) Tourism, Recreation, Cultural, and Convention Facilities Tax Amendments**

HB38 would direct 15% of the transient room tax in Salt Lake County to pay for the Real Salt Lake stadium in Sandy.

**SB68 (Waddoups) Tourism, Recreation, Cultural, and Convention Facilities Tax - Imposition, Distribution, and Expenditure of Revenues**

SB68 would direct a portion of the Restaurant tax from counties, and give it to the cities.

**Please visit www.utahtaxpayers.org for more information on these and other important tax issues and to see the complete Taxpayers Association Watch list.**

### My Corner - by Mike Jerman

# Changes in State Expenditures Highlight Need for Transportation Reform

**(Due to Howard Stephenson serving in the Legislature, this month's My Corner comes from Association Vice President Mike Jerman)**

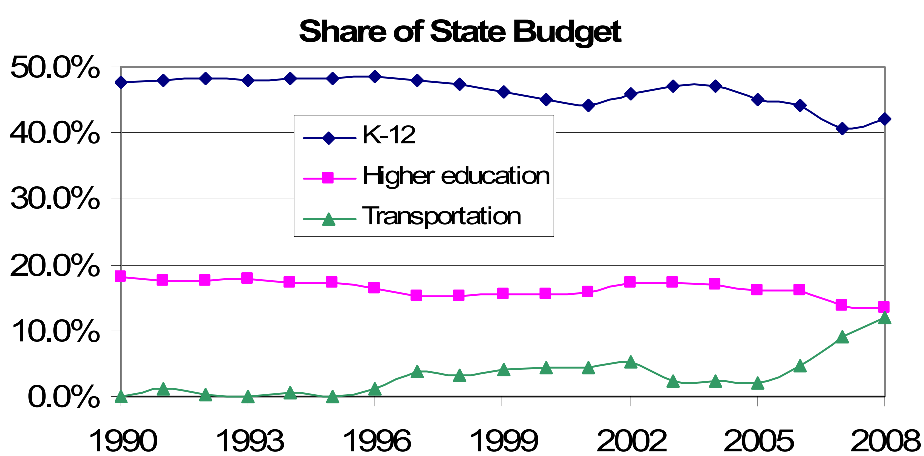
**Share of State Education/Fund General Budget**

| Budget item | 1990 | 2008 | Percent change | Percentage point change |
|---|---|---|---|---|
| MSP | 43.6% | 41.2% | -5.6% | -2.5% |
| Total K-12 incl MSP | 47.8% | 42.2% | -11.7% | -5.6% |
| Higher education operations | 18.0% | 13.4% | -25.3% | -4.6% |
| Transportation | 0.1% | 12.1% | 13,773.7% | 12.0% |
| Corrections | 4.8% | 5.7% | 18.5% | 0.9% |
| Health | 5.0% | 6.5% | 29.7% | 1.5% |

*Calculations by Utah Taxpayers Association based on GOPB data. General fund earmarks are included. FY08 data is based on Gov. Huntsman proposed budget.*

*Since 1990, Utah's state expenditures have changed significantly, as the accompanying charts demonstrate. State spending has shifted from K-12 and higher education to transportation and to a smaller degree corrections and health.*

Since 1990, Utah's state expenditures have changed significantly, as the accompanying charts demonstrate. State spending has shifted from K-12 and higher education to transportation and to a smaller degree corrections and health. Surprisingly, the significant increase in state general fund dollars for transportation has occurred at the same time as significant increases in local sales tax dollars have been used for mass transit, which should have slowed the growth of state general fund dollars for




*Calculations by Utah Taxpayers Association based on GOPB data. FY08 is based on Huntsman's proposed budget. Higher education share excludes capital. GOPB data began separately identifying higher education capital in 1995. Includese earmarks.*

*Utah's current approach to funding transportation is not working and needs to be reformed.*

*In Gov. Huntsman's FY08 budget proposal, $716 million in unrestricted and earmarked general fund dollars will be spent on state and local roads.*

transportation. Some, but certainly not all, of the increased reliance on general fund for transportation can be attributed to the state's decision not to raise gas taxes periodically to account for inflation.

The accompanying charts and graphs demonstrate that Utah's current approach to funding transportation is not working and needs to be reformed.

FY2008 shares for K-12 and higher education operations will probably be lower once FY2008 supplementals are approved.

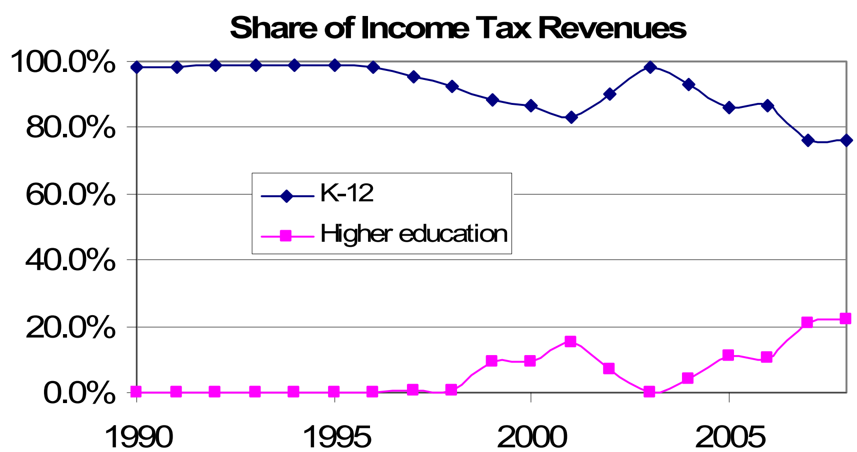
The accompanying chart shows that K-12 and higher education annualized expenditures growth rates (general and education funds only) have exceeded combined inflation and population growth of about 5.5%, but overall education/general fund expenditures including earmarks have grown at much higher rate.

**Annualized Growth Rates, Education and General Funds, FY90 to FY08**

| Budget Area | Annualized Growth Rate |
|---|---|
| K-12 incl MSP | 6.7% |
| Higher education operations | 5.8% |
| Transportation | 41.5% |
| General fund including earmarks | 7.4% |
| Education fund | 8.3% |
| Total general/education fund incl earmarks | 7.9% |

*Calculations by Utah Taxpayers Association based on GOPB data. FY08 data is based on Huntsman's proposed budget.*

As more general fund dollars are being diverted from higher education to transportation, two additional shifts are occurring. First, more income tax dollars are being diverted from K-12 education to higher education. The following chart shows this diversion over time.




*Calculations by Utah Taxpayers Association based on GOPB data. Higher education expenditures include capital. A small percentage of income tax dollars are annually appropriated to the Utah State Tax Commission*

The second shift involves the increased reliance on tuition to cover higher education operations as demonstrated by the accompanying graph.

**How much of the shift in general fund dollars can be attributed to the lack of inflation adjustment in gas tax?**

Unlike sales and income taxes, gas tax revenues do not automatically increase with inflation. However, only a portion of the increased reliance on general fund dollars can be attributed to the lack of gas tax increases. The last gas tax increase became effective in FY98. Assuming 3% annual inflation from 1998 to 2008, the gas tax would need to be increased 35% to recoup inflation.

In Gov. Huntsman's FY08 budget proposal, $716 million in unrestricted and earmarked general fund dollars will be spent on state and local roads. A one cent-per-gallon increase in gas taxes generates slightly less than $14 million per year. Therefore, a 51 cent-per-gallon increase would be needed to generate $716 million per year. This would be a 208% increase in the existing state gas tax, much higher than the 35% inflationary loss since 1998.

**Quote of the Month #2**

***"Is it really fair to expect one system to meet all the needs of our diverse population? I would argue it's not fair to expect the public system to do it all."***
-Carolyn Sharette, director of American Preparatory Academy, speaking as a parent in favor of school choice.
Source: *Salt Lake Tribune*, January 31, 2007

*Utah's state budget is on an unsustainable path. Unless the state implements serious transportation reforms, either taxes will have to be increased significantly and/or K-12 and higher education will continue to receive a smaller share of the budget.*

*Some argue that current growth rates are justified because of the slight decrease in state expenditures during the economic downturn of FY2001 to FY2004.*

**What does this all mean?**

Utah's state budget is on an unsustainable path. Unless the state implements serious transportation reforms, either taxes will have to be increased significantly and/or K-12 and higher education will continue to receive a smaller share of the budget.

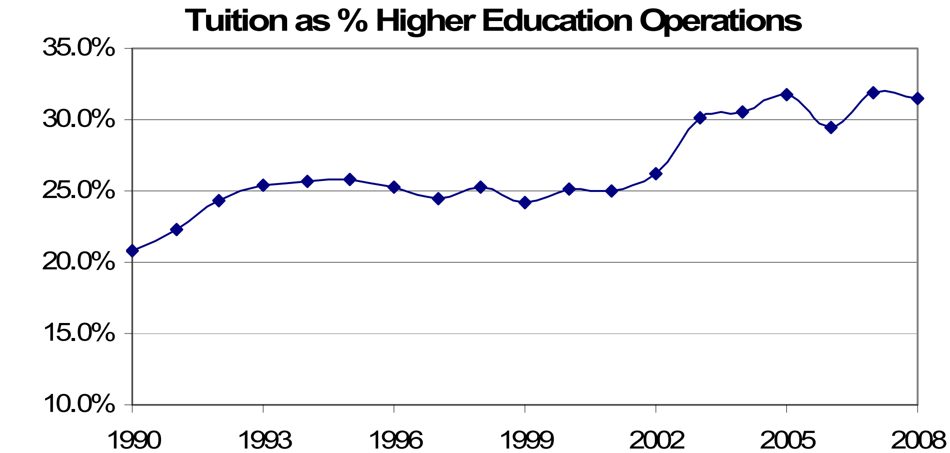
Transportation reform includes the following four key elements:

1) Congestion pricing, which will slow the growth in state transportation expenditures by slowing the growth in vehicle miles traveled and will allow transportation capacity to be used more effectively.

2)Corridor preservation, which will allow the state to slow the long-term growth in expenditures for land acquisition.

3)Requiring road and rail projects to be prioritized side-by-side in one list instead of two.

4)Requiring road and rail projects to compete for the same general funding.




*Calculations by Utah Taxpayers Association based on data from GOPB*

## State Government Spending Growth Accelerates

The Utah Taxpayers Association released a report on state government growth last month. Go to www.utahtaxpayers.org to view the full report. In recent years, state government expenditures have grown at a rate higher than economic growth. Below are several charts that summarize the situation.

**Annualized State Spending Growth**

| | FY04 to FY08 | FY01 to FY08 |
|---|---|---|
| Education/general including earmarks | 13.8% | 7.1% |
| Total state spending less federal | 10.2% | 6.9% |
| Total state spending including federal | 8.3% | 5.8% |
| Inflation/population growth (est) | 5.5% | 5.5% |

*Calculations by Utah Taxpayers Association based on GOPB data*

Some argue that current growth rates are justified because of the slight decrease in state expenditures during the economic downturn of FY2001 to FY2004. Annualized state government growth including the FY2001 – FY2004 period has been higher than combined inflation and population growth as the follow data demonstrates.

**Annualized education/general funds by Governor**

| Governor | Annualized Growth Rate |
|---|---|
| Leavitt | 5.6% |
| Walker | 11.2% |
| Huntsman | 14.6% |
| FY93 to FY08 | 7.7% |

*Calculations by Utah Taxpayers Association based on GOPB data*

State spending – particularly in recent years -- is growing faster than the economy because certain revenue sources grow much faster than the economy during good times (but also decrease much faster than the economy during bad times). These revenue sources include corporate income taxes, sales taxes on business purchases, and individual income taxes on capital gains and dividends.

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## South Valley Sewage District Chooses to Spend $40 Million on Unnecessary Add-Ons

South Valley Sewage District recently voted to require a membrane bioreactor which will cost an extra $40 million in addition to the costs of a new sewage treatment plant. The $40 million will be passed on to the ratepayers in the district. There is no question that expansion of the sewage district was needed, but the district board voted to appease a few property owners by requiring a the plant to be built on a smaller footprint, with an expensive membrane that will cost taxpayers an extra $40 million.

The board's decision came during the 2007 legislative session in which legislators were working to find a resolution to the problem. Your Taxpayers Association is concerned that the district would make people in the district pay the extra amount all for a few property owners.

Because the sewer district board is voted on in separate elections from municipal or general elections, only a few hundred people voted for the elected members of the district board out of tens of thousands of registered voters. Taxpayers in the district are urged to contact the board members and express their disapproval of this excessive spending.

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