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The Utah Taxpayer

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June 2008 Articles

Utah's Tax Burden Increases but Ranking Improves

Utah's total tax and fee burden as percent of personal income increased from 15.76% in FY2005 (revised) to 16.08% in FY2006. Utah's ranking, however, improved from 5th highest to 8th highest.

Excluding fees, Utah's tax burden, 11.34%, ranks 20th is just slightly above the national average of 11.24%.

When all state and local government revenue is included, Utah ranks 11th highest.

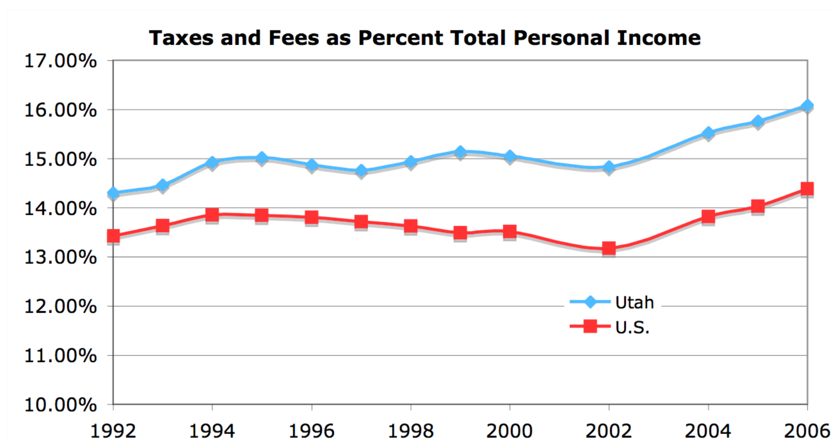
The Utah Taxpayers Association annually calculates tax burdens for all 50 states using data from the US Census Bureau and the Bureau of Economic Analysis. The association uses several tax and spending burden measures to provide a complete picture of Utah's position relative to the rest of the nation. By most broad tax, fee, and revenue measures, Utah ranks above the national average. Utah ranks below the national average in property taxes.

State and Local Tax Burdens and Revenues as Percent of Personal Income, FY2006

Measure	U.S.	Utah	Utah Rank	Utah as % U.S.
All state/local government revenue incl federal	25.77%	28.45%	11	110.4%
State/local government revenue excl federal	21.51%	23.63%	11	109.8%
State/local general revenue from own sources	16.31%	18.17%	11	111.5%
Taxes and fees	14.39%	16.08%	8	111.8%
Taxes/fees less higher education charges	13.62%	14.53%	10	106.7%
Taxes	11.24%	11.34%	20	100.9%
Individual income taxes	2.53%	3.12%	15	123.4%
General sales taxes	2.65%	3.31%	13	124.9%
Motor fuel taxes	0.35%	0.49%	13	141.4%
Property taxes	3.38%	2.57%	38	76.1%
Other taxes not listed above	2.34%	1.85%	34	79.1%

Calculations by Utah Taxpayers Association based on Census Bureau and Bureau of Economic Analysis data.

Utah's tax burdens increased in FY2006, largely due to a growing economy. During economic expansions, individual and corporate income taxes and sales taxes on business inputs increase faster than growth in personal income. These revenues also decline faster than personal income during recessions. The following charts show Utah's and the nation's tax and fee burdens as a percent of personal income from 1992 to 2006.



Calculations by Utah Taxpayers Association based on Census Bureau and Bureau of Economic Analysis data

During the 2006 and 2007 General Sessions, the Legislature cut Utah taxes by more than $400 million. About 85% of these tax cuts directly impacted individuals; 15% impacted business. (See our March 2008 newsletter for more details). The impacts of these tax cuts will begin appearing in next year's report.

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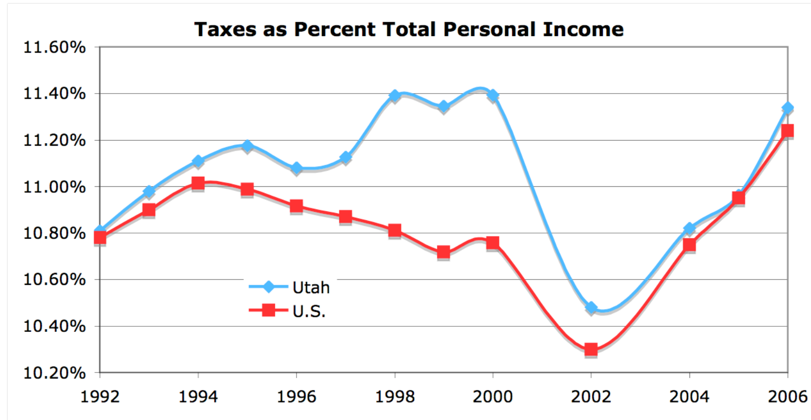
States without individual income taxes generally have lower total tax and fee burdens

Should voluntary fees be included in the analysis?

Fees should be included in tax burden analyses for the following reasons:

1. Even if fees are "voluntary" such as tuition at public universities, government still has an obligation to keep fees as low as reasonably possible.
2. Even though fees are frequently a preferable method for financing certain government functions, such as water and transportation, elected officials can pretend to cut taxes or slow the growth in government by increasing reliance on user fees. Governments frequently increase fees to avoid increasing taxes.



Calculations by Utah Taxpayers Association based on Census Bureau and Bureau of Economic Analysis data

States without individual income taxes generally have lower overall burdens

As demonstrated in the following chart states without individual income taxes generally have lower total tax and fee burdens. This finding dispels the "balloon effect" which posits if one form of taxation is low, total tax burden will always still be about average because the low tax will be offset by higher taxes elsewhere. (It's called the "balloon effect" because when one end of a balloon is squeezed, the other end gets bigger). While the "balloon effect" is frequently observed, it is by no means universally observed as the following table demonstrates.

States without individual income tax

State	Tax and Fee Burden as %TPI	Tax/Fee Burden as % U.S.	Rank
Washington	14.43%	100.3%	26
Florida	13.65%	94.9%	36
Nevada	13.18%	91.6%	40
Texas	12.34%	85.6%	44
Tennessee	12.15%	84.4%	48
South Dakota	11.24%	78.1%	49
New Hampshire	11.05%	76.8%	50
U.S. average	14.39%	100.0%	N/A

Calculations by Utah Taxpayers Association based on Census Bureau and Bureau of Economic Analysis data

Nine states do not impose taxes on individual income. Two of these states – Tennessee and New Hampshire – impose taxes on dividends and interest. Two other states – Alaska and Wyoming – have higher tax burdens and are not included in this analysis, because they export taxes to other states through severance taxes on natural resources.

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Four states do not impose state and local sales taxes: Delaware, Montana, New Hampshire (which also does not impose an individual income tax), and Oregon. Alaska does not impose a state sales tax, but many local governments do. States that do not impose sales taxes tend to rank in the middle of tax and fee burdens: Delaware, (22nd); Oregon, (24th); Montana, 32nd).

My Corner - by Howard Stephenson

South Salt Lake, West Jordan and Sandy: Why we need transparency in local government

Cities across the state are preparing their final budgets for the coming fiscal year which begins July 1. Unfortunately that means we're hearing about a lot of shenanigans. As an elected official, I understand the pressures Mayors and City Councils face, especially when revenue forecasts are declining. Sometimes that means having to either cut services or increase taxes, both painful options.

Much of that pain stems from the fact that the average citizen doesn't understand his city's needs. All she sees is a new municipal energy tax, higher property taxes, or more dandelions at her neighborhood park.

In some ways, it is no surprise that taxpayers don't understand their city's budget. While I've made a career scrutinizing city, county and state budgets, most people have more important things

Even recognizing these competing priorities, elected officials must shoulder the blame that citizens don't understand the budget.

to do, like going to their children's baseball games and dance recitals, and managing their own family budgets. With so many things competing for attention, most citizens simply don't have the time to dissect the city's budget. They count on elected officials to do the job for which they were elected.

Even recognizing these competing priorities, elected officials must shoulder the blame that citizens don't understand the budget. In 30 years of evaluating public finances, I have yet to see a single city, county, school district or other special district publish its budget or annual audit in a searchable, online database. I rarely see any taxing authority provide a copy of its budget in a digital spreadsheet. When these documents are made available, they are either in hard copy, or in a file format that requires the recipient to recreate the spreadsheets before he can analyze it.

To make matters worse, in the last month, 3 cities have resorted to tactics designed to prevent the public from understanding their budgets.

West Jordan Whispering

The *Deseret News* reports that the West Jordan City Council held one budget work session without using microphones. The mics were omitted so that the public couldn't hear what was being said.

According to Mayor Dave Newton, "Certainly we don't want to stop the public from viewing what was going on, but that wasn't the most important part of this, in my opinion. The most important thing was for the council to discuss and weigh these decisions, because these decisions aren't easy, and it's hard when you've got an audience to do that" ("Budget talks inaudible in West Jordan," *Deseret News*, May 7, 2008).

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At the very least, this tactic is a blatant attempt at an end-run around the state's open meeting laws. It is always "hard" for the business of government to move forward when in the light of day. But voters and taxpayers have every right to jealously guard their liberties, and their tax dollars, and preventing observers, even those who sit on the front row, from hearing their elected officials discuss the city budget is corrupt, and offers compelling evidence of the need for transparency in government finance at the local level.

South Salt Lakes Silence

As outragous as the West Jordan example is, South Salt Lake's is equally reprehensible, where a majority of the city council voted to skip altogether any discussion on the proposed budget. Arguing that last year's budget discussions had descended to a "'Spanish Inquisition' of criticism," Council Member Shane Siwik and Council Chair Ray Turner proposed instead to "support the mayor and the administration" by skipping a formal discussion on the proposed budget" ("South Salt Lake Council forgoes budget discussion," *Deseret News*, May 23, 2008).

While the public had the opportunity to review the $21.5 million budget prior to the public hearing, they had no formal opportunity to see how their elected officials were approaching the budget. Instead, as Council Member Siwik indicated, "council members may discuss the budget with city staff following the public hearing."

As with the West Jordan example, the behavior of the South Salt Lake City Council mocks the public who elected them. Citizens deserve thorough, public discussion of the budget. Anything less is a dereliction of duty.

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Sandy's secret bonuses

Another example of the need for transparency is the Sandy "bonusgate" controversy. As has been well-documented, several years ago the *Salt Lake Tribune* submitted GRAMA requests regarding the bonuses provided to Sandy city employees. Sandy Mayor Tom Dolan refused the requests, until the courts ordered the city to release the information.

Once the information came to light, it was clear why the city tried to cover up the bonuses. With no public disclosure and essentially no oversight from the City Council, Mayor Dolan and his top deputies were receiving tens of thousands of dollars in annual bonuses, with virtually no regard to their performance. Meanwhile line employees' annual bonuses were limited to a meager 1 or 2 percent. Sandy backed off their egregious bonus policy, but only when the policy was exposed to the light of day, and only after years of protracted litigation.

Quote of the Month #1

"The most important thing was for the council to discuss and weigh these decisions, because these decisions aren't easy, and it's hard when you've got an audience to do that"
West Jordan Mayor Dave Newton commenting on the reasons they turned the microphones off at a recent public hearing

Source: *Deseret News* 5/7/2008.

In all 3 cases, city officials went out of their way to hide the public's business from the public. To prevent these abuses at the state level, Senator Wayne Niederhauser led the Legislature in adopting the state's first transparency in government finance law, which requires the state to publish an online, free, searchable database of the state's finances. He tried to set the same standards for cities and counties, but they claimed it would be too expensive. In light of these shameless tactics, it's clear that Senator Niederhauser's instinct was correct. Unless they are required to, it seems local officials will not accept the responsibility taxpayers and voters deserve.

Property Taxes: Utah vs. California

This summer, the Interim Revenue and Taxation Committee will be discussing acquisition-based valuation for property tax purposes. Acquisition-based valuation is a fundamental component of California's Proposition 13, which California voters passed in 1978. Utah currently uses fair market valuation in which property valuations are based on current assessments by the county assessor.

The association has researched acquisition-based valuation and has come to the following conclusions.

Utah property tax burdens are typically lower than California's

Despite the hype about California's property tax system, Utah's property tax burdens as a percent of personal income are consistently lower than California's, as the following graph demonstrates.

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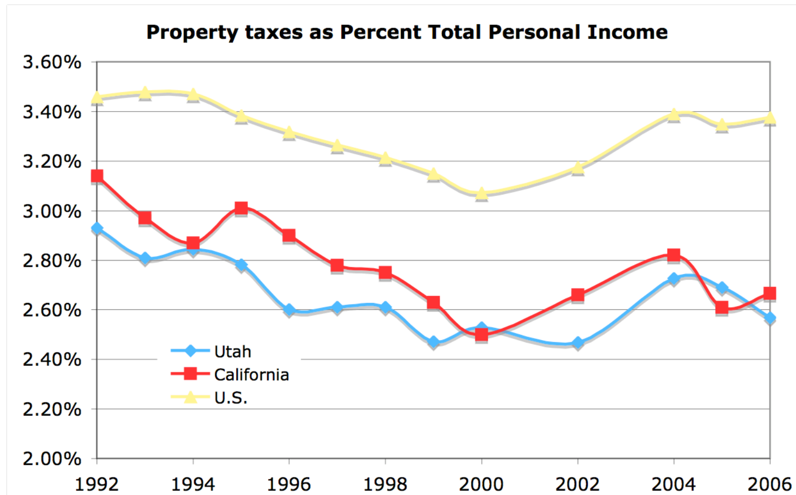
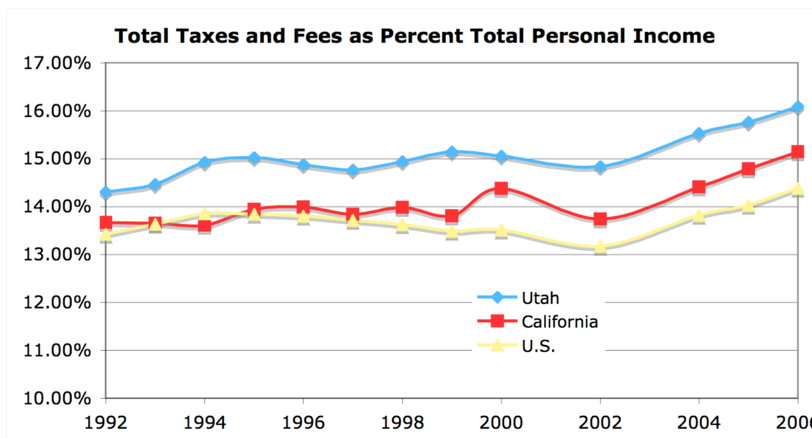


Calculations by Utah Taxpayers Association based on data from Census Bureau and Bureau of Economic Analysis

While several factors contribute to property tax burdens in both states – legislative decisions to cut property taxes, Truth-in-Taxation, caps on growth, acquisition-based valuation and fair market valuation, government efficiency, total government tax and fee burdens – Utah's property tax burdens are lower even though Utah's total tax and fee burdens are higher than California's.

Utah's ability to keep property tax burdens lower than California's even though Utah's total tax and fee burden is higher than California's is evidence that Utah is doing something right with regards to property taxes.



Calculations by Utah Taxpayers Association based on data from Census Bureau and Bureau of Economic Analysis

During the 1990s, the Utah Legislature cut the statewide basic levy for education twice and allowed counties to reduce property taxes in exchange for imposing a 0.25% sales tax. Some of these tax cuts were offset by local governments increasing their property tax levies at the same time because legislative tax cuts and shifts had created additional "headroom" in the property tax.

Acquisition-based valuation is inequitable to young, working families

Acquisition-based valuation's largest single flaw is that it treats property owners inequitably. Households who own their property longer pay lower property taxes than those who own their property for a shorter amount of time, all other things being equal.

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Proponents of acquisition-based valuation cannot adequately explain why a household's obligation to fund government services such as education, public safety, and transportation should be based on how long they have lived in their current residence. After all, everyone's property benefits from public services, not just those who have recently purchased a home.

Acquisition-based valuation is especially harmful to young families moving into a new home and those who move because they change jobs. The following example concerning two identical homes -- one purchased twenty years ago and one purchased this year -- demonstrates the inequity.

Annual increase in home price, 1990 to 2007:	6.8%
Acquisition-based valuation, assuming 6.8% annual increase	
Home purchased 20 years ago:	$100,000
Home purchased this year:	$373,000
Property tax, 1.1% effective nominal tax rate and 55% residential exemption	
Home purchased 30 years ago:	$605
Home purchased this year:	$2,257

Fair market valuation prevents targeting industries with discriminatory property taxes

Departing from the constitutional protections of fair market value opens the possibility of assessing property taxes based on populism instead of sound tax policy. Currently, the Legislature and local governments cannot impose higher, discriminatory property taxes on specific property owners, such as certain types of businesses, because the state constitution mandates that property taxes be based on fair market value.

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Acquisition-based valuation is not economically neutral

Taxes should be economically neutral. An economically neutral tax does not incent or disincent specific economic activity. Acquisition-based valuations discourage home owners from selling their property – just like high capital gains taxes discourage selling of capital assets that have appreciated -- because home owners will experience a huge increase in annual property taxes when they purchase their new home.

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Acquisition-based valuation violates "low rate, broad principle of taxation.

Tax policy experts nearly universally agree that a tax system with low rates and broad, uniform bases, such as a system based on fair market value, is superior to a system that carves out exemptions for specific groups. Acquisition-based valuation exempts valuation growth that occurs after a property is purchased. Assuming a conservative annualized market value growth rate of 5%, a property that is held for thirty years would have more than 75% of its current fair market value exempt from property taxes.

Taxes Now Conference Recordings Available

If you were unable to attend the 30th Annual Utah Taxes Now Conference on May 13 or want to hear the presentations again, you can listen by going to **www.utahtaxpayers.org**. This year's conference was one of the best in years, so you won't want to miss any of the presentations. Go to www.utahtaxpayers.org to see the full agenda

Governor Jon M. Huntsman, Jr. gave an update on the Utah economy, noting job growth 2.1%, 5 times the national average. Gov Huntsman highlighted the fact that we have an internationally competitive business environment and that our pro-business attitude and strong workforce is key to Utah's competitiveness.

Randall O'Toole of the Cato Institute spoke about using market forces to help solve the transportation funding crisis. He demonstrated the need for congestion pricing and how it can be a cost effective way to increase efficiency in public road systems.

A panel of experts including **Senator Sheldon Killpack** talked about our current and future transportation needs and how we can solve the transportation crisis.

Senate President John Valentine discussed three budget issues: rainy day funds, $100 million education set aside, and base budgeting. Today we have $227 million in the education rainy day fund and $187 million in the general rainy day fund, which he said is key to riding the economic wave.

House Speaker Greg Curtis discussed the recent split of the Jordan School district and the tax implications that it may have in the future.

Acquisition-based valuation doesn't adequately offset deficiencies in fair market valuation.

Despite errors in fair market valuations, the current system generates more equitable and accurate valuations than a system that bases valuations on transactions that occurred ten, twenty, or thirty years ago.

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Utah already has a 45% primary residential exemption

While the 45% primary residential exemption violates several tax policy principals (low rate and broad base, for example), it is still one of the most generous exemptions in the nation. California's exemption, by comparison, is $7,000, which would equate to a 2.8% exemption on a $250,000 home.

Circuit breaker is a targeted, efficient method for helping low-income elderly

Acquisition-based valuation generally benefits the elderly while harming younger, first-time homebuyers, even though elderly households generally have more disposable wealth than young families. However, some older households have difficulty paying property taxes. Targeted tax breaks for low-income elderly households such as circuit breakers are more efficient than giving property tax breaks to large number of homeowners at the expense of taxpayers in general.

Energy Taxes: Hatch's Opposition Is Key. by Duane Parde

Several months ago, the Senate defeated a proposal that would have placed an additional $21 billion in taxes on U.S. producers of oil and natural gas.

Congress, in its infinite wisdom, is trying to manipulate our tax dollars in the name of social engineering, this time in the energy industry. In the process, our representatives are putting American consumers at risk of even higher energy bills in the future.

Several months ago, the Senate defeated a proposal that would have placed an additional $21 billion in taxes on U.S. producers of oil and natural gas. Just last week, however, Senate Majority Leader Harry Reid joined with several of his colleagues to introduce new legislation with a different mix of energy tax hikes. This bill, or something like it, is likely to be voted on again in the coming months, just in time to take advantage of the recurring rage over summer gas prices. Supporters claim that the revenue generated by these taxes will be used to encourage the development of so-called alternative energy. Reid's legislation goes so far as to impose a windfall profit tax on firms that don't "sufficiently invest" in such research.

That might score a few political points with some constituencies, but it certainly isn't sound economic policy. Improving our energy situation – and the development of resources of all kinds, both alternative and conventional – can't be accomplished by hiking taxes on the very companies that provide us with our most important energy source: oil and natural gas. Increasing taxes on energy producers will lead to higher gas prices, sticking every business and consumer in America with an even higher bill than they suffer from today.

Just last fall, the National Taxpayers Union helped organize a joint letter to Congress signed by 234 economists that urged lawmakers to avoid harmful energy taxes. The signatories, including a Nobel Laureate and professors from institutions such as Harvard University and the University of Chicago, contended that Congress should actually reduce taxes and equalize treatment of all energy sources. They wrote, "History has shown that attempts by the federal government to tax, regulate and subsidize our way to more plentiful and secure energy have failed miserably."

An examination of past U.S. policy lends credence to their position. Congress instituted a windfall profits tax in the 1980s that cut domestic fuel production and increased our dependence on foreign oil imports. During that same era, lawmakers spent $2 billion on the "Synfuels" program, which completely failed to speed the development of alternatives to conventional energy resources. Duplicating these unsuccessful initiatives today would waste valuable time and the taxpayer's money.

The energy industry itself has invested billions in capital in the fuels and alternatives that make the most sense, both technologically and economically. The idea that politicians or bureaucrats are more capable of developing new energy resources than the experts who make their living doing just that is laughable.

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Affordable energy is one of the most serious problems facing our nation today. Family budgets are stretched, and just putting gas in the car, food on the table and a roof overhead is difficult enough without heaping on additional burdens. That's precisely why market forces, not politics, should dictate the development of our energy supply. That's also why sound science, not partisan gamesmanship, should guide energy investments. Adding more taxes to the cost of producing the energy we need is the exact opposite of the policy Congress should pursue.

<u>This is even more true in Utah, where a burgeoning oil sands, gas and coal sector is one of the leading – if not the leading – creator of new jobs. Taxing any domestic fuel producers hurts all.</u>

Fortunately, final approval of these new energy taxes has not occurred. The Senate still has the opportunity to remove the target from the taxpayers' back. Senator Orrin Hatch (R-UT) has opposed this type of tax in the past and must do so again. All concerned taxpayers should contact him and urge him to lead the fight against this potentially disastrous proposal. <u>His vote will be crucial.</u>

Duane Parde is President of the National Taxpayers Union (ntu.org)