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The Utah Taxpayer

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October 2008 Articles

Severance Tax Trust Fund on November Ballot

This November, Utahns should vote YES on constitutional amendment B, that would allow the state to deposit any revenues into the permanent state trust fund, not just revenues from the 1998 Master Settlement Agreement (MSA) with major tobacco companies.

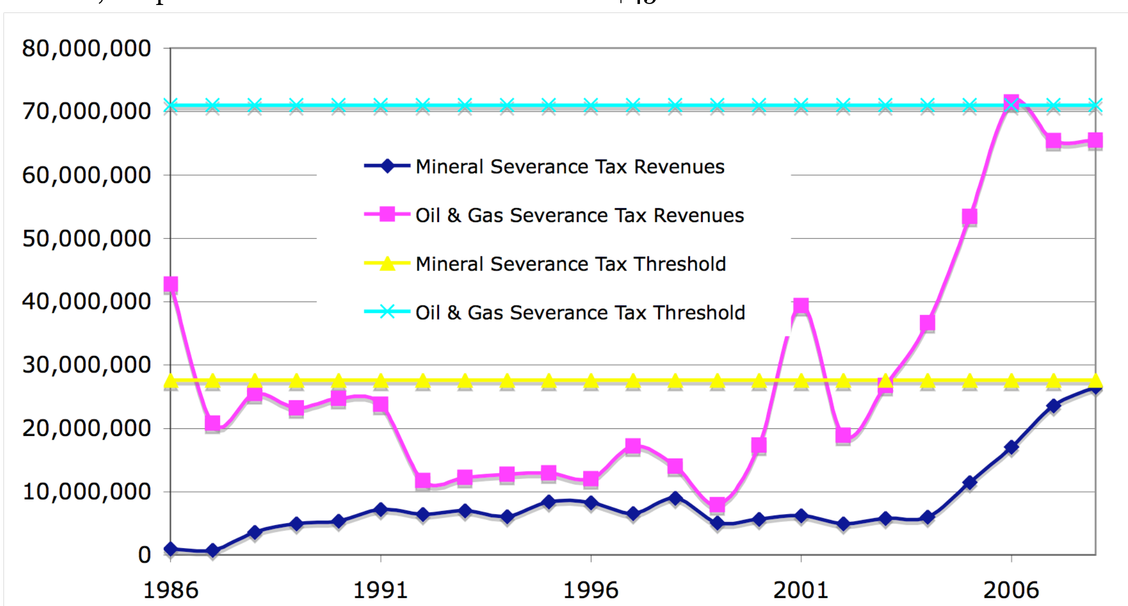
If approved by voters, the state will begin depositing oil, gas, and mineral severance tax revenues above certain thresholds into the state permanent trust fund. This is sound policy for at least three reasons.

1. Severance tax revenues are extremely volatile (see accompanying graph), and depositing these revenues into a trust fund makes more sense than appropriating these revenues for annual ongoing government expenditures.
2. As economic assets such as oil, gas, and minerals are permanently depleted, permanent trust fund reserves take their place.
3. Since severance tax revenues will eventually diminish and disappear, depositing these revenues into a trust fund makes more sense than appropriating these revenues for ongoing general government expenditures that will never diminish.

Unfortunately, the Legislature currently intends to deposit only a small portion of severance tax revenues into the trust fund. The Utah Taxpayers Association hopes that the Legislature eventually reconsiders this approach, but approving the constitutional amendment is a major first step. In the future, increasing severance tax transfers to the trust fund can be accomplished by statutory changes.

Background

In the 2000 General Session, the Utah Legislature passed and Gov. Leavitt signed SJR 14 and SB15. SJR14 was approved by Utah voters in November 2000, thus creating the state permanent trust fund to accept MSA revenues. Initially, based on SB15, 50% of MSA revenues were appropriated to the trust fund, and 50% were appropriated to various programs, including CHIP. During the economic downturn earlier this decade, the amount deposited to the permanent trust fund was reduced. Currently, 40% of MSA revenues are appropriated to the permanent trust fund. At the end of FY2008, the permanent trust fund had a balance of $45.8 million.



In the 2007 General Session, the Legislature passed and Gov. Huntsman signed SJR2, which places before the voters the constitutional amendment authorizing non-MSA revenues to be deposited into the permanent state trust fund. In the 2008 General Session, HB58 was passed by the Legislature and signed by Gov. Huntsman, which authorizes oil and gas severance tax revenues above

$71 million and mineral severance tax revenues above $27.6 million to be deposited into the state permanent trust fund, subject to voter approval of constitutional amendment B. Unfortunately, these thresholds are far too high, and it is likely that very little revenue will be placed into the trust fund unless these thresholds are reduced. The Association will lobby for these thresholds to be reduced in the future.

How does the permanent trust fund work?

The permanent trust fund works as a rainy day fund, but accessing trust fund reserves is more difficult than accessing general and education rainy day fund reserves. To access trust fund revenues, the governor and three-quarters of each legislative chamber must vote in favor. To access traditional rainy day funds, only a majority of votes in each chamber and approval from the governor are needed. At the same time, the Legislature can appropriate interest off this trust fund for ongoing programs.

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How much does the state collect in severance taxes?

The state of Utah imposes severance taxes on oil, gas, and metals as they are “severed” from the earth. In recent years, as commodity prices and subsequently production levels have increased, severance tax revenues have skyrocketed as the nearby chart shows.

What have other states done?

In the 1970s, Wyoming and New Mexico created severance tax trust funds. By 2007, New Mexico had more the $4 billion in its trust fund, and Wyoming had nearly $4 billion in its trust fund.

Utah’s mineral severance tax was imposed in 1937, and the oil and gas severance tax was imposed in 1955. Since these taxes were imposed, Utah should have been depositing every dollar of severance tax revenue into a permanent trust fund. Approval of constitutional amendment B will enable the Legislature to correct this mistake. In the future, the Legislature should pass legislation increasing the amount of severance tax dollars deposited into the permanent trust fund.

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My Corner - by Howard Stephenson

Saving Utah’s precious school taxes

School boards have proven that taxpayers cannot trust them to conduct economic development. In 2008, Utah school districts have approved more than $436 million in redevelopment plans. Because schools impose approximately 56% of property taxes, the $436 million in overall RDA plans means school boards took $239 million in education taxes out of the classroom, and gave it to private developers. (Utah law distinguishes between 3 different types of redevelopment agencies, EDA, RDAs and CDAs. For purposes of this article, all kinds of redevelopment agencies are referred to as RDAs or redevelopment)

The last time the Legislature evaluated Utah’s redevelopment laws, they hoped that requiring school boards to opt in would limit RDA growth, particularly for projects which, in the greater community, would occur without subsidies. Given the sobering growth in RDAs just this year, it is clearly time for the Legislature to reevaluate current RDA law.

The problem with Utah’s RDA law, and how to fix it

The fundamental problem is the way Utah distributes sales tax dollars. The portion of sales tax that cities and towns receives is split 50/50: half is distributed based on point of sale, and half is distributed based on population. Because cities can obtain more sales tax revenue if retail outlets build within their boundaries, they have a strong incentive to manipulate the market. They give away property tax revenue of school districts, counties and special taxing districts to increase their sales tax revenues.

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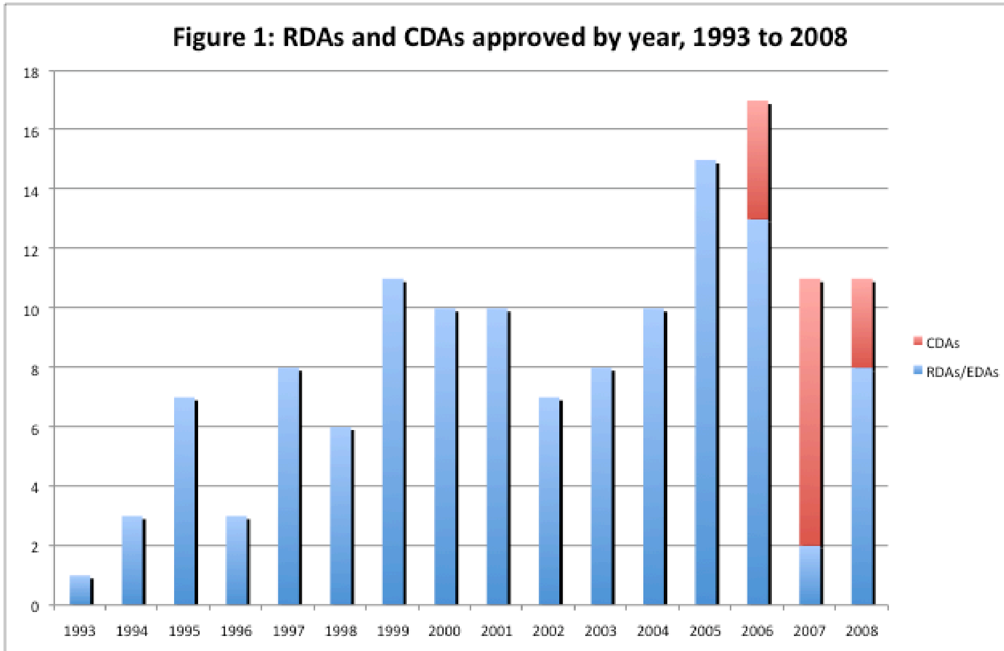
Because school boards control 56% of property tax revenue, cities offer school boards sunny forecasts of “found money” to give away school property taxes to these developers. Unfortunately, virtually every one of these forecasts focus as not on whether the RDA will stimulate new economic activity, but where that economic activity will occur.

The solution is fairly obvious: distribute all sales tax revenue to cities based on population. That simple change would entirely eliminate the tax incentive for cities to subsidize retail development.

How school taxes end up in RDAs

Cities use redevelopment projects to artificially lower the cost for developers to build within their boundaries by using those sales/property taxes to improve the property the city wants developed. Because developers normally pay for the these improvements, these payments amount to little more than corporate welfare.



School boards have proven unable to distinguish between economic development and corporate welfare.

Until 2005, school boards had to vote no, if they did not want their portion of the property tax to be used in an RDA. As Figure 1 (source: Utah State office of Education) shows, few school boards were willing to oppose their mayors and city councils. The 2005 Legislature revised Utah's RDA laws, so that school districts' default position is "out." If a school district wants to participate in an RDA, the school board must vote to opt in. Unfortunately, school boards have proven unable to distinguish between economic development and corporate welfare.

The continuing growth of retail RDAs

As previous editions of the Utah Taxpayer have chronicled, the Granite School Board has proven itself the worst offender. This year alone, they have approved more than $190 million in RDAs, meaning they have taken more than $105 million out of the classrooms they are charged with supporting. And Figure 1 shows that the number of RDA projects continues to grow, despite the 2005 revision to RDA law.

Redevelopment projects approved in 2008

Name	Term (yrs)	Tax Subsidy	City	School Dist.
Southwest Economic Development Project Area	15	$123,712,193	WVC	Granite
Economic Development Project Area No. 3 - Data Center	10	$13,876,320	W Jordan	Jordan
Proctor and Gamble EDA	20	$74,936,963	Tremonton	Box Elder
North Central Economic Development Project Area	15	$22,310,075	WVC	Granite
Cottonwood Mall Urban Renewal Project Area	20	$128,441,476	Holladay	Granite
South Salt Lake Martket Station Survey Area	15	$55,627,777	S Salt Lake	Granite
5400 S. Bangerter Highway Urban Renewal Project Area	15	$17,132,000	Taylorsville	Granite

Source: Utah State Office of Education

As previous editions of the Utah Taxpayer have chronicled, the Granite School Board has proven itself the worst offender.

Unfortunately, the Granite School Board is hardly the only guilty party. In 2006, the Alpine School Board agreed to pay more than $11 million to help build an Embassy Suites hotel, convention center and BMW dealership off the Pleasant Grove exit of I-15. In 2007 the Provo School Board opted into an RDA designed to keep Zions Bank in Provo.

The problem with these RDAs, as with the overwhelming majority of Utah's RDAs, is that they subsidize retail economic activity. Retail economic activity does not need a subsidy. Whether they offer homes, retail outlets, or office space, retailers follow population. Where the number of rooftops will support a strip mall, a shopping center or an office complex, a plethora of developers are anxious to invest their own money in those retail outlets.

There are rare occasions in which an RDA may be appropriate. For example, if Utah were competing with South Carolina, Texas and Ohio for a Toyota manufacturing plant, an EDA may be appropriate. In that case, the redevelopment project would bring new jobs and new investment into Utah. Those new jobs would increase the population, and naturally increase the amount of retail economic activity. An RDA might also be appropriate if the property itself has negative value. Short of those two instances—when the state is competing with other states for a major manufacturer, and when the land itself has negative value—RDAs are not appropriate.

With the benefit of hindsight, no one should be surprised that school boards haven't distinguished economic development from corporate welfare. School board members are elected to improve student achievement, not stimulate the economy. They may understand union negotiations, testing standards and curriculum, but they don't understand economic development.

The 2009 Legislature needs to protect Utah's precious school tax dollars. The Legislature should make the following changes. Ideally, they should distribute all sales taxes to cities based on the city's population. Failing that, they should ban RDA subsidies of any retail development, and prohibit school boards from participating in RDAs.

The Utah Legislature should ban RDA subsidies of any retail development, and prohibit school boards from participating in RDAs

Budget Shortfalls: Here We Go Again (and it could be worse by January)

Facing an anticipated $272 million shortfall in the FY2009 budget and having to deal with an $82 million shortfall in the recently concluded FY2008 budget, Governor Huntsman and the Utah Legislature decided to address the budget situation in a September special session instead of waiting until January, when the fiscal year would be more than half over.

The Governor and the Legislature wisely decided to cut spending instead of raising taxes or dipping into rainy day funds, although they did dip into non-lapsing balances. Most agency budgets were reduced by 4%. Legislators then "backfilled" a quarter of that with one-time money that will lapse at the end of the fiscal year, reducing the base budget for FY2010. Public education's FY2009 budget was reduced 3% but was then backfilled with an equivalent amount of one-time funds, which also reduces the base budget for FY2010.

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The accompanying chart shows the Governor's and the Legislature's actions.

September Special Session Budget Changes

	Ongoing	One-time	Total
Revenue Shortfall	-272.4	-81.6	-354.0
Budget Reductions	251.0	-90.0	161.0
New Revenue	11.6	170.7	182.3
Unappropriated Balances	10.0	1.0	11.0
Subtotal	272.6	81.7	354.3
Balance	0.2	0.2	0.4

Source: Legislative Fiscal Analyst

Some have argued that spending cuts would be unnecessary if the state had not cut taxes by roughly $400 million in recent years. However, if the state had appropriated these revenues instead of cutting taxes, the state would still be dealing with a shortfall.

Legislators were quick to point out that no one knows how deep or long the recession will be. (We used to say that if we knew the answer to that, we'd be working on Wall Street, but ...). Fortunately the state has stashed extra funds.

Available funds for balancing future budgets

Rainy Day Fund	$414 million
Cash for capital projects incl roads	$423 million
Non-lapsing balances	$388 million

Source: Legislative Fiscal Analyst

We've been through this before

It was only a couple of years ago that the state had to deal with stagnant or declining revenues. In FY2001, education and general fund revenues came in at $3.75 billion. Not until FY2005 did education and general fund revenues surpass the FY2001 level as the accompanying chart shows.

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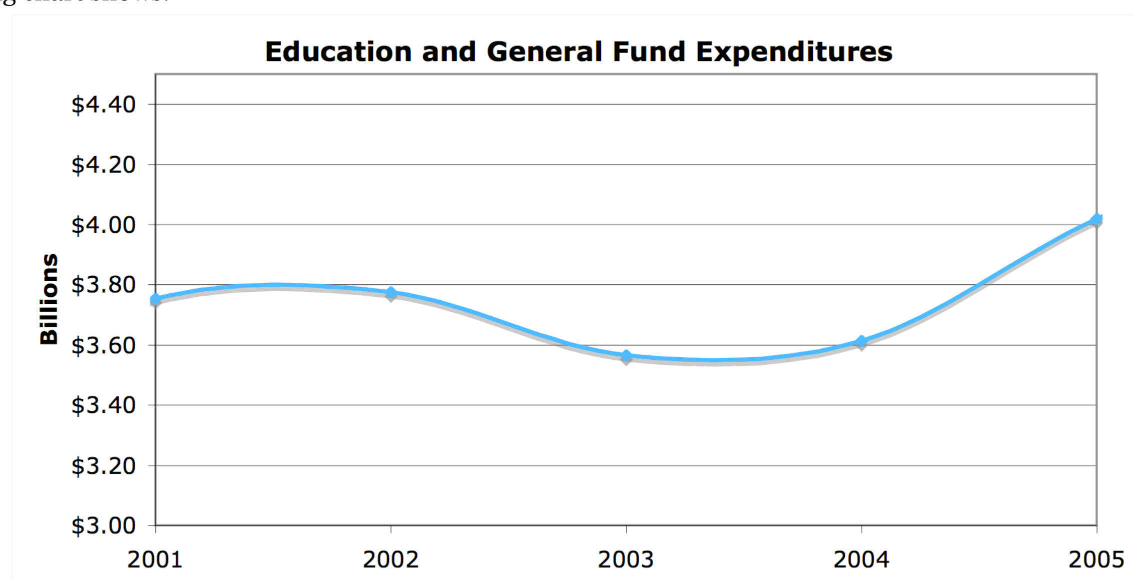

Source: GOPB; includes earmarked sales taxes

Rejecting calls for massive tax increases by the local media, the Utah Legislature decided to cut or freeze spending, largely held public education harmless, and dipped into various funds including the Rainy Day Fund. The Legislature did increase some taxes such as tobacco taxes and imposed a new cable and satellite TV tax.

Overall, the Legislature had to deal with revenue shortfalls of $685 million in FY2002 and FY2003. The accompanying chart shows several of the actions undertaken by the Utah Legislature from FY2002 to FY2003 to balance the budget.

How the Legislature got through the last downturn

Replace capital facility cash with bonding	$120.8 million
Rainy Day Fund	$113.3 million
Budget Reductions	$234.8 million
Tobacco Trust Fund	$38.9 million
Transfer from Centennial Hwy Fund	$66.4 million
Capital, road, other project reduction	$24.3 million

Source: Appropriations Report, Legislative Fiscal Analyst

With the economy already slowing, the last thing Utah should do is discourage retail activity by further raising taxes.

The push for a punitive tobacco tax increase

Elected officials always seem to believe that they know better than the average taxpayer. The latest evidence is a proposal to raise Utah's cigarette tax from $0.695 to $2 per pack. If the tax is approved, the state will use the revenues from this tax, obviously paid exclusively by smokers, to subsidize the healthcare of everyone else.

Sin taxes, as tobacco taxes are often called, suffer a fatal flaw. Proponents promote these tax increases for contradictory purposes. On the one hand, they hope the tax will cut tobacco use, especially by younger people. On the other hand, they need people to continue smoking and pay the higher tax, so they can fund their pet projects. Those goals cannot both be achieved.

As both the Salt Lake Tribune and the Heartland Institute have pointed out, Utah smokers already pay tens of millions of dollars in tobacco taxes, and these taxes more than pay for the social costs associated with using tobacco. According to Vanderbilt University professor Kip Viscusi, the taxes paid by smokers "equal or exceed the medical care costs associated with smoking" ("Utah cigarette tax is more than meets the eye," Budget and Tax News, Sept. 22, 2008).

Quote of the Month #1

"The price that riders pay, its actually only 10 to 30 percent of the actual operation and maintenance costs."

UTA spokesperson Carrie Bohnsack-Ware on the tax subsidies Utah transit riders receive.

Source: KCPW October 1,2008

In addition, this proposal would significantly harm many of Utah's smaller retailers. Smokers buy cigarettes many places, but at convenience stores revenue from cigarette sales make up a much higher proportion of the store's total revenue than at grocery stores. With the economy already slowing, the last thing Utah should do is discourage retail activity by further raising taxes.

This punitive tax would not stop tobacco use, and could eliminate some of the cigarette tax revenue the state is already receiving.

This dramatic tax increase would also make Utah less economically competitive with its neighbors. If it passes, tobacco sales in Wendover, Evanston and Mesquite will go up as Utah consumers cross the state line to buy cigarettes. Other people would simply buy cigarettes out of state, and then smuggle them into Utah. This punitive tax would not stop tobacco use, and could eliminate some of the cigarette tax revenue the state is already receiving.

Despite these sound policy reasons against this punitive tax increase, Rep. Ray has already declared his plan to push this tax increase during the 2009 Legislature. Like too many elected officials, he believes the state can spend your money better than you. Your Taxpayers Association knows that money should stay in your pocket, which is why we will be ready to oppose this tax increase.

Moratorium on oil shale development expires

House Democrats refuse to allow reasonable drilling off shore

This week Congress took the first step towards expanding America's development of safe, domestic energy supplies. Previously federal law prohibited development of the estimated 800 billion barrels of oil currently locked in the oil shale and tar sands deposits located on the Green River Formation, located in Utah, Wyoming and Colorado. However, they prudently allowed that moratorium to expire on Oct. 1.

Unfortunately, Democrats remain staunchly opposed to developing potentially the nation's richest energy resources in the Alaskan National Wildlife Refuge (ANWAR) and below the coastal continental shelf. They did force a bill through the House that would open drilling for oil under the continental shelf. However, that bill limited drilling to areas at least 50 miles off shore. Analysts agree that the vast majority of recoverable off shore oil is located within the 50-mile limit. Because of these flaws in the bill, Pres. Bush has promised to veto the House bill.

To meet the coming energy shortage, the United States needs to pursue every energy possibility out there: renewable, oil shale, tar sands, off shore drilling, etc.

House Democrats and their extreme environmental allies professed concern about insuring that drilling operations not be visible from shore. However, even on the clearest days drilling rigs just 16 miles from shore are not visible. As Utah Representative Rob Bishop said during the House debate, “We could have done so much more. Instead we will vote on a hollow shell of a bill.” Rep. Chris Cannon joined Rep. Bishop in opposing the bill, while Rep. Jim Matheson supported the bill.

The worldwide spike in the price of oil has prompted countries around the world to expand their oil exploration. No one of these solutions will provide the needed energy sources by itself. To meet the coming energy shortage, the United States needs to pursue every energy possibility out there: renewable, oil shale, tar sands, off shore drilling, etc. The United States is the only country refusing to explore and exploit new energy reserves. And extreme environmentalists’ continuing efforts to prevent this exploration and processing, it may be years, even decades before taxpayers see the benefits of lower energy prices that oil shale, tar sands and off-shore drilling offer.