

From Property Tax to? Revenue Sources, Tradeoffs, Trends

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Introduction to ITEP



The Institute on Taxation and Economic Policy (ITEP)

Non-profit

Non-partisan research organization

Federal, state, and local tax policy issues

Mission:

Ensure elected officials, media, and general public have access to accurate, timely, and straightforward information that allows them to understand the effects of current and proposed tax policies with an emphasis on tax-incidence analysis.

Revenue Options for Reducing Property Taxes...



- Start with the tax at issue:
 - Opportunities to broaden the property tax base, lower the rates?
- Then look to other existing revenue sources:
 - Major: Sales, Motor Fuel
 - Minor: Excise taxes
- New revenue sources
- Lessons from other states

Property Tax



Property Tax Base Expansion



- Review Current Tax Expenditures
- Big ticket items:
 - Commercial appraisals
 - Agriculture evaluations
 - Homestead exemptions
 - Chapter 313 abatements

Property Tax Base Expansion



- Questions to ask about the big ticket items:
 - Is everyone paying their fair share?
 - Adjustments to be made to better target property tax relief to those who need it more?
 - Even if local school districts have control over their Chapter 313 abatements, are their processes or supports that could be put in place that better enable them to make fully informed decisions re: whether such abatements continue to serve their interests?

Ensuring Economic Development Accountability



- Best Practices for tax breaks:
 - Disclosure: How much do the breaks cost and what public results benefited?
 - Strict job quality standards: Are new jobs being subsidized b/c of inadequate wages and benefits?
 - Money-back guarantee: What happens if promised economic benefits aren't met?

Ensuring Economic Development Accountability



- Best Practices for tax breaks, cont'd:
 - Automatic review of giveaways: Every incentive should come under periodic review to ensure that the ineffective ones are eliminated.
 - Establishing an economic development policy with clear goals, objectives, and strategies: Knowing what you're trying to accomplish helps you know what questions to ask to ensure that expenditures are helping you achieve your larger economic development goals.

Sales Tax



Strategies for Sales Tax Reform



- Strategy #1: Broaden the base
 - Creates new revenues at the state & local level
- Strategy #2: Increase rate
- Strategy #3: Combination

Strategy #1: Broaden the Sales Tax Base

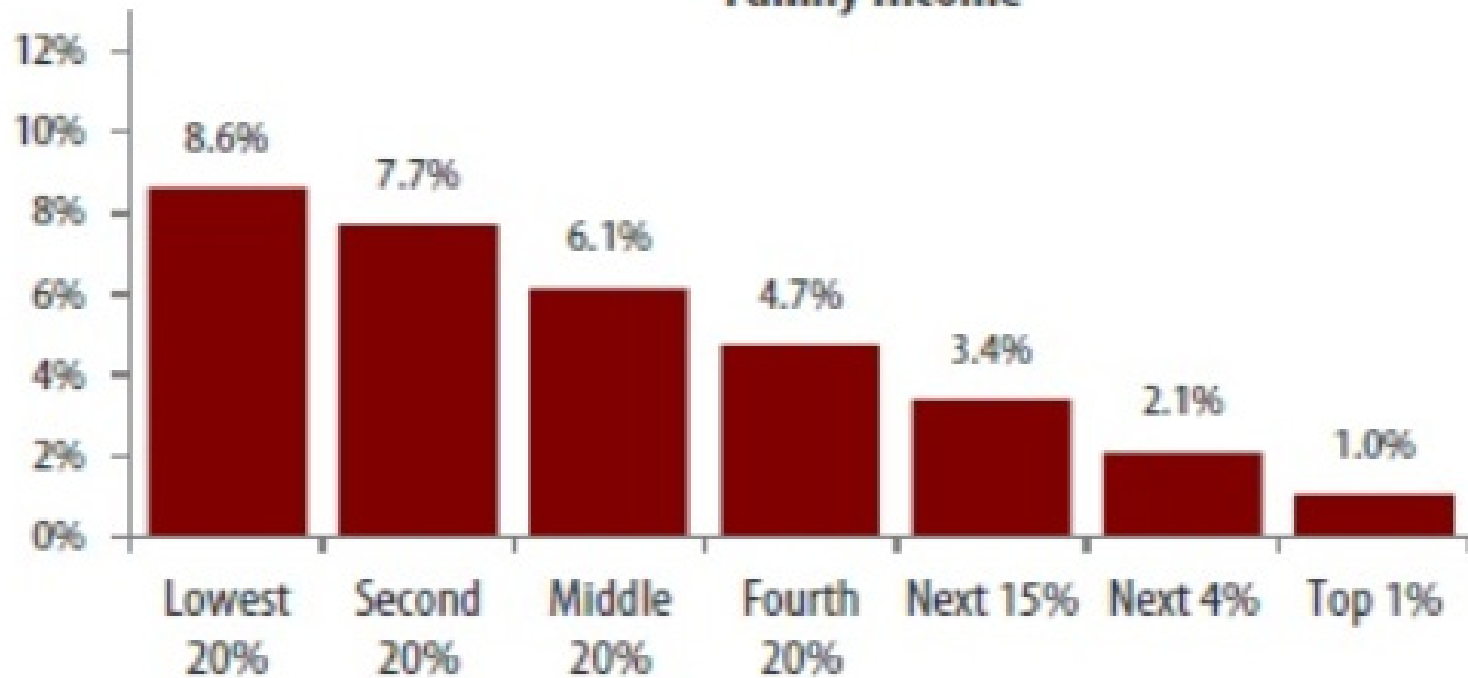


- Review Current Tax Expenditures
- Items of note:
 - Groceries (\$3 billion)
 - Non-prescription drugs (\$260 million)
 - ✦ Some states working to tax opioids (KY, NY)
- Other:
 - Newspapers, magazines (\$60 million)
 - Sales tax holidays (\$70 million)

Caution Against Eliminating Sales Tax Exemption for Groceries



Sales & Excise Tax Share of Family Income



Sales Taxes are Regressive



- Low- and middle-income taxpayers pay a higher percentage of their incomes in sales taxes than those with higher incomes.
- According to Consumer Expenditure Survey data, ITEP estimates that low-income families typically spend $\frac{3}{4}$ of their income on sales-taxable items, while middle-income families spend about $\frac{1}{2}$, and upper-income families spend roughly $\frac{1}{6}$.

State Responses to Sales Tax Regressivity



- Nothing
- Exempt certain retail items that make up a larger share of low- and middle-income families purchases entirely from the sales tax (exempt entirely or tax at a lower rate)
 - E.g., groceries
- Enact targeted, refundable credits.

Challenges to Eliminating Grocery Exemption in TX



- 1) Most states administer through a personal income tax
- 2) Little precedence in non-income tax states
 - South Dakota rebate for sales tax on food pre-2012
 - Washington state's refundable EITC
- 3) Politically a very contentious issue
- 4) Exemption ensures intended beneficiaries received relief (no "opt-in" requirement).

Strategy #1: Broaden the Sales Tax Base

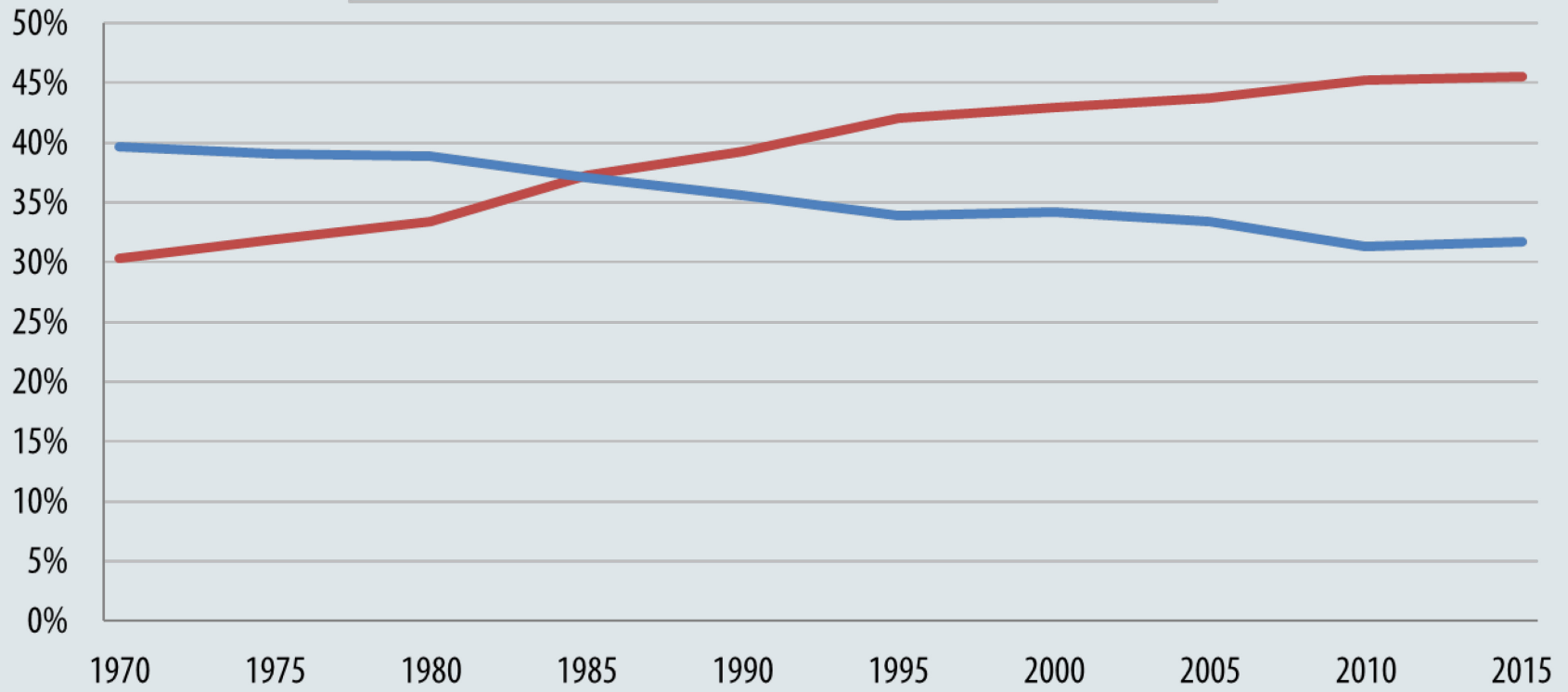


- Expand Base to be responsive to 21st Century Economy
 - Services
 - Digital Goods
- Over time, narrowing base = long-term revenue problem
OR constant rate increases

Base Erosion Over Time



— Services — Typical sales tax base



Source: US Bureau of Economic Analysis, *National Income and Product Accounts, Table 2.4.5U*

Sales Tax on Services



- Texas Currently Taxes 17 Broad Categories of Services
- States that have recently expanded their sales tax bases to include more services:
 - Connecticut
 - North Carolina
 - New Jersey
 - Ohio
 - Rhode Island

Strategy #2: Raise the Rate



- Neighboring states Oklahoma, Arkansas, and Louisiana currently all have higher combined state and local sales tax rates
- Need state general sales tax rate of 8.44% to raise an additional \$10 billion annually
 - New highest combined state & local rate of 10.38% (compare to LA 9.98%)

Motor Fuel Tax



Strategy #1: Raise the Rate



- Texas's gas tax rate is way below average.
 - 20 cents in Texas for gas or diesel, versus a national average of 33.72 cents for gas and 35.51 cents for diesel.
- Last increase to rate was October 1, 1991, >26.5 years ago!
- Only 6 states have gone longer than Texas without an increase, and most have seriously considered gas tax increases in recent years:
 - AK, MS, LA, IL, AZ, and CO

Strategy #1: Raise the Rate



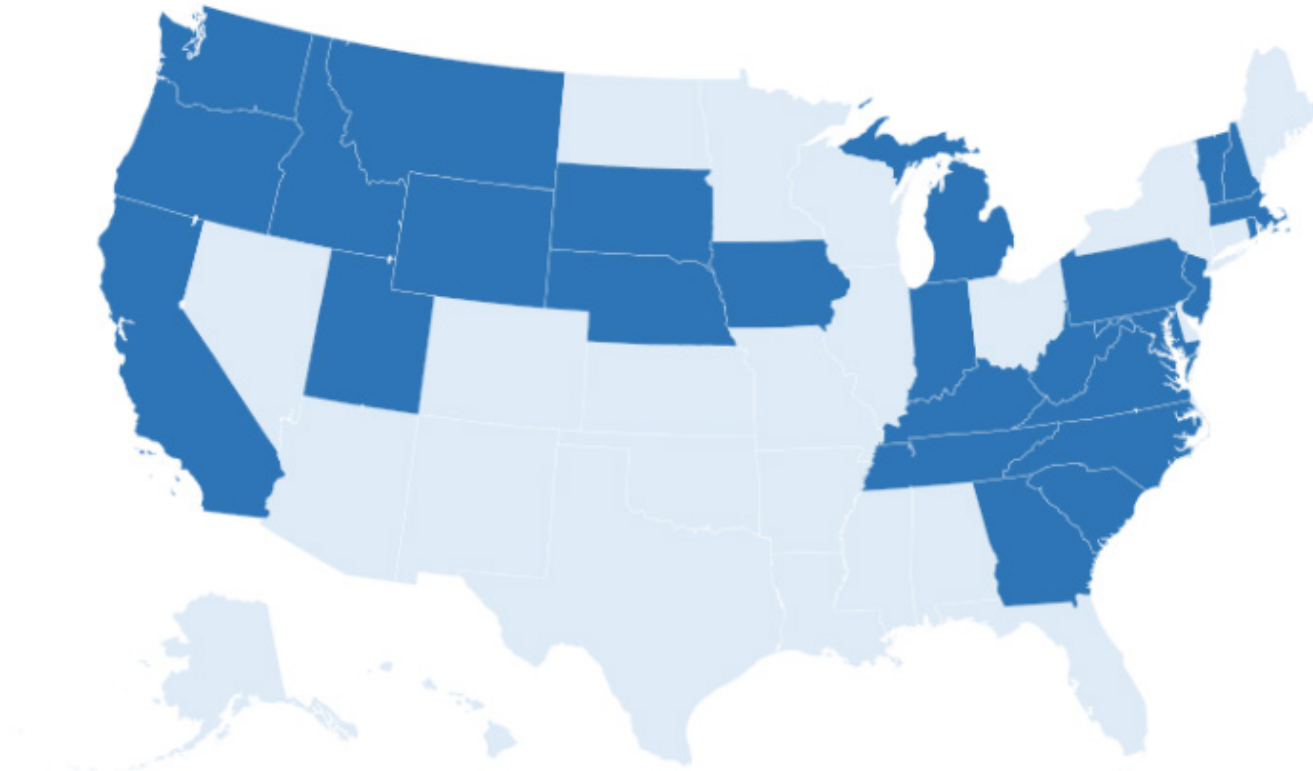
- Be in good company: more than 26 states have increased or reformed their gas taxes since 2013, including Oklahoma.
- Oklahoma just raised its gasoline tax by 3 cents and its diesel tax by 6 cents (among other taxes) to fund teacher pay raises
- Gas tax increases have also been serious proposals recently in neighboring Louisiana and Missouri.

Strategy #1: Raise the Rate



Recent State Gasoline Tax Increases & Reforms

Includes Laws Enacted Between 2013 and 2017



Source: Institute on Taxation and Economic Policy. Reflects laws enacted by July 12, 2017, plus legislation awaiting the governor's signature in Oregon.

Strategy #1: Raise the Rate



- Importance of indexing the rate to stave off further tax erosion
 - Most state gas taxes are unsustainable = generate an increasingly inadequate amount of revenue over time. Fixed-rate state gas taxes are simply incapable of dealing with rising transportation infrastructure costs (or education costs!).
 - An increase in the per-gallon tax rate will bolster state transportation revenues in the short-term, reforms to the basic design of state gas taxes are needed to ensure that revenue growth does not once again fall behind transportation needs.

But Be Sure to Index!



- Indexing options:
 - Link the gas rate to transportation cost growth
 - ✦ The most direct route for ensuring that increases in the price of asphalt, machinery, and other transportation inputs do not prevent states from adequately maintaining their transportation networks.
 - Link the gas rate to the Consumer Price Index (CPI)
 - ✦ Rate of growth in the price of items purchased by a typical consumer.
 - ✦ Improvement over a fixed rate, but can be inadequate in years where growth in cost of transportation inputs exceeds that of other goods (as it did throughout most of the 2000s).

But Be Sure to Index!

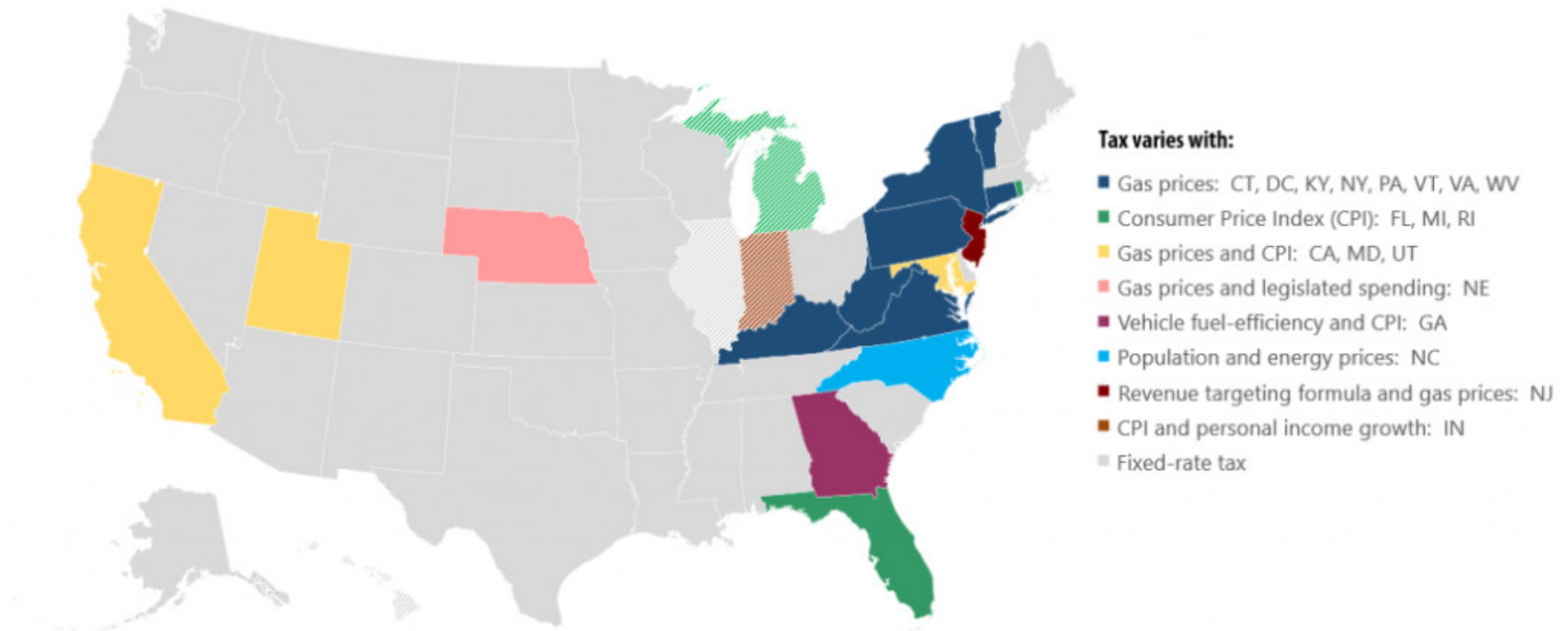


- Indexing options, cont'd:
 - Link the gas rate to the price of gasoline
 - ✦ More familiar to and comfortable for lawmakers since resembles sales tax, but highly volatile.
 - ✦ Several states have abandoned this approach or intervened in order to ensure there isn't dramatic rising and falling.
 - ✦ Options for offsetting volatility:
 - Link to average price over previous 12 months instead of price at the pump
 - Limit maximum rate changes
 - Impose floors or ceilings

Strategy #1: Raise the Rate



States with Variable-Rate Gasoline Taxes



Source: Institute on Taxation and Economic Policy, July 2017. Striped states (HI, IL, IN, and MI) apply their general sales taxes to gasoline, which results in variations in the tax paid per gallon based on the price of fuel.

Strategy #2: New Approaches



- Supplement Motor Fuel Tax
 - Charging fees for electric and hybrid vehicles
 - ✦ Now 17 states
 - ✦ Newly: WV, MI, MN, IN, OK, TN, CA, SC
 - ✦ Previously enacted: GA, WA, WY, ID, CO, MO, NE, NC, VA
 - ✦ Introduced legislation: KS, NH, MT
 - Taxing ride sharing
 - ✦ States: MD, MA, NV, PA, SC
 - ✦ Cities: New York City, Chicago, cities in Massachusetts
 - ✦ Considering: GA, DC, Oakland, CA

Strategy #2: New Approaches



- Mileage Tax
 - Taxing motorists on miles driven rather than gas purchased
 - Exploratory stages
 - ✦ Federal grants (\$95 million) for states to study mileage-based fees and other alternatives to the gas tax. States must match the federal grants 50-50.
 - ✦ 14 western states; coalition of eastern states doing their own testing.
 - ✦ Issues they are still working out: Privacy? Out of state drivers?

Excise Taxes



Cigarettes



- E-Cigarettes
 - Vapor products subject to sales and use tax but not tobacco tax because don't contain nicotine
 - 7 states plus DC; localities in 3 states
 - ✦ LA, KS, CA, MN, WV, NC, PA, DC
 - ✦ Localities: Alaska, Illinois, Maryland
 - Regressive!
 - Not sustainable revenue sources

Soda



- Soda
 - States
 - ✦ 22 states exclude groceries from their sales tax but tax soda
 - Recent actions:
 - VT eliminated exemption for soda
 - ME eliminate exemption for candy
 - AR declassified soda and candy as “groceries,” subjecting those items to GST rate of 6.5% instead of preferential rate of 1.5%
 - Separate excise taxes
 - AL, AR (just eliminated), TN, VA, WA, WV

Soda



- Soda
 - Localities
 - ✦ CA: Albany, Berkeley, Oakland, San Francisco
 - ✦ CO: Boulder
 - ✦ PA: Philadelphia
 - Campaigns
 - ✦ OR: Portland
 - Repeal
 - ✦ IL: Cook County

Cannabis



- Cannabis
 - More than half of the states have legalized medical and/or retail cannabis
 - States that have voted to legalize retail cannabis sales: AK, CA, CO, ME (blocked by governor), MA, NV, OR, WA
 - Estimates around \$1 billion in new revenue

Franchise Tax



Franchise Tax



- Sources of dissatisfaction:
 - Lack of sensitivity to ability to pay
 - Complexity
 - Revenue forecasting difficulties
- Cutting the rate doesn't make these difficulties go away—it just limits your ability to achieve other tax or spending goals (e.g., cut property taxes, maintain investment in public education)

Lessons from Other States



Lessons from Other Non-Income Tax States?



- States with no or limited income taxes:
 - Alaska, Florida, Nevada, South Dakota, Washington, Wyoming
 - New Hampshire, Tennessee
- How are they faring? Thriving? Facing similar challenges?

States Not Struggling



- States doing ok have unique economies that give them a more stable base
 - Nevada, gambling industry
 - Florida, tourism
- South Dakota:
 - Gov. made a significant commitment to increase teacher salaries, which they did in 2016 by raising the sales tax rate from 4% to 4.5%.
 - Another attempt to raise teacher salaries again this year and bring down the sales tax rate on food—dependent on revenue raise from online sales tax decision.

States Struggling



- Washington:
 - Education funding crisis since 2012
 - Court started levying fine of \$100,000 per day in 2016
 - 2017—raised statewide property tax levy
 - 2018—relying on economic boost (available to them given high reliance on their Business & Occupation tax, which is subject to many of the same complaints as Texas' franchise tax).
 - To sustain this level of funding, looking to new revenue options including tax on capital gains and carbon tax.

States Struggling



- Wyoming:
 - Has faced serious challenges in recent years based on heavier reliance on oil and gas industry.
 - They have been facing pressure to fund education for years but keep patching over the problem rather than enacting a long-term solution.
- Alaska:
 - Suffered big budget gaps and faced with significant cuts in wake of falling oil and gas prices.
 - Over the past two years, have had serious proposals to reinstitute a broad-based personal income tax.

States Struggling



- Tennessee:
 - Struggling with adequately funding transportation infrastructure.
 - Eroding their tax base by phasing out their limited income tax.

Income-Like Taxes



- Some states without an income tax have been reconsidering in recent years:
 - Alaska: Governor proposed broad-based income tax; House passed a version of an income tax
 - Washington: Governor proposed capital gains tax; legislation filed this year
 - Wyoming: Came close to enacting in 1999, but struck gold!
- What are they looking at?
 - Capital gains
 - Payroll tax
 - Broad-based income tax

Summary: Lessons Learned



- Importance of maintaining a diversified tax base
 - WA, FL, and TX have a more diversified tax base so in recent years they haven't suffered as much from fluctuations in the mineral, oil, and gas industries.
- Seek to broaden or add tax bases to further diversify instead of eliminating existing tax sources

Questions?



Thank you for your time and attention!

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