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## Focus On The Property Tax

An organization called "Citizens For 25% Amendment" is spearheading a move which they hope will result in a constitutional amendment to lower the property tax assessment level from 50% of true and fair value to 25%.

The proponents of the lowered assessment level assert and are no doubt honestly convinced that, if the 50% assessment level were enforced, property taxes in this state would *automatically* double or triple, which, of course, is a frightening thought to home owners who don't understand the role of the assessment level in the determination of the tax.

The role of the assessment level is simply to determine the value of the property against which the millage will be applied.

The League opposes this proposed change in the constitution primarily because, according to our 1965 League consensus on fiscal issues, we agreed that, in order to equalize and strengthen the property tax, "flexibility and recognition of changing times and needs is important in the tax policy." And if the assessment level were lowered, it would serve to make our property tax laws more inflexible than they are at present. Ideally, the League believes that specific figures and details such as assessment levels, millage limits, classification, etc., should be left to legislative determination according to the needs of the time.

The League also opposes the proposed constitutional amendment because it contains no provision for equalization of the property tax within or among counties. The League's strongest position on the property tax states that "equality and uniformity both within and among counties in the administration of the property tax are of major importance."

Some of the proponents of a 25% assessment level considered the desirability of including a section that would enforce uniformity in the administration of the tax, but for some reason it was decided unnecessary. They say that if the assessment level is lowered there "will be" uniformity because county assessors have indicated they would comply. One can safely assume that this belief is not based on the history of the property tax administration in this state.

Additional doubts as to whether there "will be" uniform property tax administration if the assessment level were lowered are raised by the fact that among those supporting the measure are many farm and grower organizations. The average assessment level on farm property in this state is 10% of true and fair value and, though we may be underestimating the generosity of farmers, it seems hard to believe that they would support a proposal that they thought would increase their property taxes by 250%. (This would not necessarily happen, of course, but one must assume that those who support the measure believe that property taxes rise and fall with the assessment level).

There is no doubt that the property tax with all its ramifications is difficult to understand. The League has spent years studying it, and most of us still get confused at times. Therefore, for the benefit of those of us whose brilliance and wit is undeniable when all but we are asleep in the night, but who sometimes have trouble getting our point across at a dinner party, the following explanation of assessment levels and millage rates may

be useful:

School districts are financed in part by property tax revenues. Suppose the property tax revenue needed by a school district amounts to \$100,000. (Round figures are less treacherous for those of us schooled in old math.) Now, suppose 14 mills levied against 50% of the true and fair value of the property in the school district will produce \$100,000. If a 50% assessment level is enforced and if you have a \$10,000 house (property, actually), your tax for the support of your school will be 14 mills levied against \$5,000 (50% of the value of your property), or \$70. If the assessment level were 100% of true and fair value, the total millage needed to meet the school budget would be 7. You'd still pay \$70. And if the assessment level were 25%, the necessary millage would be 28 applied against 25% of your \$10,000 property. And you would still pay \$70.

It is harder and far more time consuming to inform than it is to frighten, but, hopefully, we can do the job.

## Focus On State Fiscal Fitness

Adults in all parts of the world look upon their taxes and their children with an equal lack of objectivity. One's taxes are fundamentally bad and one's children are basically good and we're happier if these issues are not confused with the facts.

A story in the *New York Times* for January 28, 1966, illustrates this peculiarly irrational approach to the subject of taxes on the part of a citizen of Colombia.

According to the *Times*, "The talk at the dinner table got around to taxes, and the host, an importer, told his guests. 'We had a bad year. I cleared \$40,000 and my lawyer was furious that I paid \$35 in taxes. He said that if I insisted on paying taxes I didn't need him.'

"When the North Americans at his table failed to join in the general laughter, their host added with some feeling. 'I would gladly pay whatever you Yankees pay on such profits if I didn't live in Colombia.'

"He went on to relate the cost of educating his children abroad, the numerous bribes he offered in the normal course of business; how much his bodyguards charged; the expenses involved in getting a phone installed in his new home; and 'all the money we spend on services that you people take for granted.'

"The North Americans then suggested that if Colombians paid taxes perhaps they could have good schools and other services, to which the Colombian answered 'I am a Latin American and I will believe that when I see it—and *then* pay.'

How nice it would be if we could feel comfortably smug about the misguided citizen of Colombia who thinks the expenditures should be made before the revenue is raised. Unfortunately, however, it appears that a reluctance to pay for desired services is common to most of us.

In the United States "key projections relating to expenditure requirements (since the Second World War) have been generally understated, resulting in revenue requirements being underestimated. In consequence, the real extent of the demands on the state-local tax system have not been foreseen; nor, even more importantly, state and local governments have been unwilling to raise taxes sufficiently to produce the revenue that ultimately proved to be needed."<sup>1</sup>

Furthermore, when legislators and governors have found it necessary to raise taxes "more than one elected official has believed the voters retired him from office for such action. The turnover among state governors has been high the past ten years or more. Men campaign against rising taxes, succeed in winning the governorship and then when confronted with the reality of the state's needs, they raise taxes and are themselves replaced by new men not yet troubled by citizen program demands."<sup>2</sup>

The citizen from Colombia said it more simply, but the problem there and here seems to be much the same.

Speaking in Seattle recently, Mr. L. L. Ecker-Racz<sup>3</sup> said, "Another fact of life for state and local government is an acute sensitivity to tax competition for business and industry. Although the importance of tax differentials to business success is grossly exaggerated, the impact of the competitive tax argument on legislators and local governing boards can hardly be overstated. Fear of losing business to another state or city haunts every political leader, and spokesmen for business have become very skilled in exploiting his fears."

In this connection, Miss Penniman told League members in Chicago that, "One of my favorite stories concerns Oregon that historically has placed its major emphasis on income taxes and its neighbor, Washington, that has avoided the income tax and emphasized sales and property taxes. More than ten years ago a study of taxes and industrial locations was made in Oregon that concluded that such exclusive use of the income tax was harmful and pointed to how much better off the State of Washington was with no income tax. Almost simultaneously, a study of the business climate in Washington called attention to how much better off Oregon was with possibly lower and certainly a different tax emphasis than Washington! The other fellow's problems just seem easier to bear than our own."

Despite the mental aberrations that occasionally occur when taxes are considered, more and more people are studying the subject calmly and are presenting their conclusions to the public. League members in Washington have studied the issue for many years and it is gratifying to find experts in the field with conclusions similar to ours.

## **EQUITY**

The League has agreed to "support measures which would remove inequities in the distribution of the tax burden."

In this connection, Mr. E. Elwood Ford<sup>4</sup> asks, "What is a fair tax? How do you tax people equally? It is doubtless true that there would be nothing more unequal than an equal tax on people with unequal ability to pay. Any other system of taxation requires some individuals to pay, directly or indirectly, heavier taxes than others.

"'Ability to pay' is probably the doctrine of tax distribution most often cited today. Behind the ability doctrine is the principle that government costs are incurred for general social purposes and are an obligation of society rather than of particular individuals. This obligation must be distributed among the individuals composing the social unit in a manner which takes account of hardship and seeks to reduce it. 'Ability' is a vague term, however, and has been given many interpretations. Each of the objective measures of 'ability' including the income standard suffers from the same shortcoming—it fails to actually measure ability."

Though equity seems difficult to define precisely, both Mr. Ford and the League find it a desirable goal.

## **THE SALES TAX**

The League has agreed that the sales tax is a regressive tax and, by adding a graduated net income tax, we've concluded that the sales tax on food and drugs could and should be reduced or, preferably, eliminated.

In a paper prepared for the Indiana Senate Finance Committee, Mr. Charles F. Bonser<sup>5</sup> wrote, "Much of the dissatisfaction with a sales tax stems from the fact that the tax is regressive—that low income families spend a higher proportion of their income on taxable purchases than do higher income families. In addition, even within the same income classifications, the larger the family the more it spends on taxable purchases. Thus, contrary to current income practices which allow personal exemptions for each dependent, the sales tax discriminates against large families.

"Food exemption greatly reduces the regressiveness of the sales tax, and in fact apparently eliminates it for most income levels. Exemption also greatly reduces the tax burden on lower income groups and the relatively heavy burden on large families. On the other hand, food exemption reduces revenue from the sales tax by 15 to 20 per cent.

"The states have been reluctant to provide any exemption for medicine, even though in terms of policy, this exemption would have substantial justification. The incidence of illness is very unevenly distributed among the population. Expensive drugs and medicines can place a very heavy drain on the resources of lower income groups; it is unfortunate to add a sales tax burden."

### **THE INCOME TAX**

The League supports a graduated net income tax, and Mr. Ecker-Racz, speaking to delegates to the Governor's Conference in Seattle said, "This state's overriding fiscal need is for a tax source capable of generating an increasing amount of revenue, to keep pace with the persistent growth in expenditures. Your political leadership will want to add the further specification that this be accomplished without too frequent recourse to tax rate increases.

"This specification—revenue growth without tax rate increases—is uniquely the monopoly of one tax alone, the income tax. In recent years, each 10 per cent rise in national income generally has produced a 15 to 18 per cent rise in state income tax collections. In contrast, it has added less than 10 per cent to consumer tax collections.

"Last year, \$500 million of your state government's \$600 million tax collections came from consumer taxes and nearly half of the remaining \$100 million from property taxes. Little wonder that the take of consumer taxes out of personal incomes here is nearly double that of the national average (6.4% vs. 3.4%).

"If this troubles you, you will want to consider going for the next revenue increment to a tax that exempts your economically disadvantaged citizens and, in distributing its burden among the others, takes account of differences in family obligations through a system of exemptions for dependents.

"The income tax can do these things, and in addition can serve as the vehicle for removing the sting of the sales tax on food or provide property tax relief to those of your elders who, with fixed incomes, are trying to live out their remaining years in their own homes.

"In your state an additional factor merits careful consideration; i.e., the possibility of using the corporate income tax to de-emphasize the business gross receipts tax and possibly also the property tax on business personal property, especially inventories.

"While net income taxes can take a sizable bite of corporate profits, business men trouble about them only when they are privileged to enjoy a profit. They very much prefer them to property and gross income taxes, because the latter are with them, whether they make a profit or suffer a loss."

### **THE PROPERTY TAX**

Some of Mr. Ecker-Racz's remarks on the property tax sounded so familiar it was hard to believe that he wasn't reading League material. He said:

"For some time the property tax is likely to remain the heart of local taxation. Compared with many parts of the country, tax rates here are low. The national average tax rate is probably half again as high as yours and in many places twice and three times as high. One has no doubt, however, that as the years roll by the property tax bite will grow. That prospect underscores the urgency of doing what you can to improve it.

"What needs doing to make the property tax more acceptable should be crystal clear by now to most Washingtonians. It has been repeated often enough with singular unanimity by a long succession of executive, legislative, and other study groups.

"What does it take?

"It takes an assessor who is a professionally trained person with career status. Ability to win elections provides no assurance of professional competence.

"It takes a tax law the assessor can administer, live with, work with, and be honest about.

"It takes an assessment district large enough to support a staff that has the technical competence in all of the specialized kinds of properties involved in today's world.

"It takes a state agency staffed with people who have the authority and competence to supervise the assessor, evaluate his qualifications, look over his shoulders to see that he is doing an adequate job, and failing that, help him mend his ways.

"The taxpayer, too, must be given his due. He must be supplied with information and a quick, efficient and economical appeals procedure. To this end, the legislature should mandate that the state tax department make annual local assessment-sales ratio studies, that it publicize its findings; and that such findings qualify as admissible evidence when offered on behalf of aggrieved taxpayers seeking redress."

#### THINGS TO COME

One interesting area of state and local financing that the League has not tried to study is that of predicting the future. Mr. Conlon, speaking to League members in Chicago last February, agreed to speculate about state and local taxation and expenditures in the 1970's. He expressed regret that in the area of taxes he had not found that "On A Clear Day You Can See Forever" simply because as far as state and local finances are concerned there are no clear days for looking ahead. However, he was brave enough to say, "My own guess as to the future is that we are likely to see a continued rise in the level of state-local expenditures, although at a rate of increase somewhat slower than that which we have had in recent years. If this is so, I expect it will be necessary to raise state-local tax rates. It seems to me that if our resources continue to grow there are many claims that will be made against them.

"This might sound to you like some variation of Parkinson's Law that expenditure rises to meet revenue. Perhaps there is an element of that kind implicit in my view, but if so I should point out that it is one deeply imbedded in American tradition. Indeed, Alexander Hamilton described it in one of the Federalist papers practically in terms of a general principle of political development. Hamilton said: 'I believe it may be regarded as a position warranted by the history of mankind that, in the usual progress of things, *the necessities of a nation, in every state of its existence, will be found at least equal to its resources.*'

"I am inclined to look for substantial increases in governmental expenditures in urban areas in the 1970's to deal with the complexities that arise from the process of what might be called urbanization.

"There are some tides now running which might affect property tax revenues. Property tax administration is improving and judicial remedies affording relief in cases of discrimination are now commonplace. In general, this means that the homeowner will have to bear his full share of the tax. It also means there will be more requests for exemptions and special treatment. For example, an old age property tax exemption has been enacted in some states already and it is sure to be accepted in many others. The preoccupation of legislators with a good tax climate is gradually leading to exemptions or special treatment of various kinds of personal property used in business. These exemptions, which include the so-called free port laws, reduce the tax base

and, once they are widely accepted and recognized, become a factor that cannot be disregarded by other states and localities in view of the inter-state competition for new and expanded industrial investments. The homestead and veterans' exemptions have been with us for some time but probably will not change very much. However, some new types of exemptions are receiving consideration and more might be heard of them. These are the preferential assessment programs for agricultural land and the assessment freeze. All in all, these developments suggest that it is quite possible the property tax is moving gradually but inevitably in the direction of a classified tax on real estate. To this potential restriction of the base must be added the renewed interest now being evidenced in rate ceilings.

"Either or both of these policies would inhibit the productivity of the tax relative to growth in the economy because increases in tax rates and assessment ratios have been significant factors in this respect during the post war period.

"There are some signs on the horizon which indicate that the personal income tax will find a greater acceptance at the state level in the next decade. The pressure for new revenue will be an important factor in that respect in those states which now rely heavily on consumption (sales) taxes. There is also some feeling that a more effective graduation of tax rates will make the states' systems more responsive growth in the economy and bring the productivity of the revenue systems closer to the growth in expenditure requirements.

"Sales taxes, both general and special, have been heavily utilized at the state level.... The prospect is that more *local* governments will seek to enter the general sales tax field under a program such as that in effect (in some states) where the tax is administered on a uniform basis by the state.

"It is not unlikely that general sales taxes will move toward the five percent level (state-local combined) in many jurisdictions. As the sales tax rate increases, considerations of equity become more pressing (exemption of food, medicines and even of clothing) as does the problem of maintaining a good tax climate for business.

"In addition to the upward movement in rates, it is also likely that there will be some expansion in the base of the sales tax so as to include a range of personal services. This trend is even now well under way. Proposals to include all services within the base of the tax have, for a variety of reasons, made little progress.

"Another factor which may have a bearing on the intensity of state-local tax pressures and, incidentally, on intergovernmental political relationships, is the growing tendency of city hall to by-pass the state capitol and to communicate directly with Washington.

"The reason for this relationship is not difficult to understand. For one thing, the really difficult fiscal problem in the state-local field is that of the imbalance between urban expenditure and urban revenue sources. Then, there is the feeling, particularly on the part of mayors of large cities, that Washington and Congress are much more aware of and responsive to the needs of the cities than are the states and legislatures. The reapportionment of state legislatures may have some bearing on future developments in this area. However, boundary lines and the mobility of resources and people and the preoccupation with maintenance of a favorable tax climate all tend to put a ceiling on the revenue sources which may be exploited by the city. For these reasons, it seems to me, direct payments or grants made in connection with a variety of federally aided functions may be much more important items in local budgets of the 1970's than they are today, and any development of this kind should at least reduce the intensity of the pressure on local tax resources."

Mr. Conlon concluded his talk with an expression of belief that he seemed to feel as deeply and firmly as do members of the League. He said:

"I would like to close with a few comments about a point which strikes me as much more important than the kinds of taxes we have or the level of tax rates. It is the matter of public understanding of the nature of the choice we make when we decide that government shall do this or do that and on what scale and according to what standards. It is true that state legislatures and local governing bodies have constantly increased tax rates

and adopted new taxes to meet costs of expenditures undertaken. But this process has not been without its serious difficulties for responsible political leaders in state and local government.

"We have increased expenditures for a variety of reasons in this era of great scientific, industrial and social development, but fundamentally it is because a majority of the voters have decided that government should do this or that. This is, in effect, a decision on the part of the individual that government shall dispose of some part of his income. But when the economic consequences of these decisions begin to assert themselves in the form of rising taxes, many of these same individuals become quite unhappy and they have a tendency to lay the blame for this situation on those who happen to hold office at the moment.

"This does not make for a healthy civic climate. It invites exploitation by irresponsible politicians since taxation is too often an emotional rather than a rational issue. At the same time it discourages sound political leadership because the reward for facing up to the problem may, too frequently, be certain defeat at the polls.

"What this suggests to me is that one of our most important problems in the fiscal field is how we can bring about a civic climate where the individual voter's decision whether to spend more or less of his income through government is an informed one, made on the basis of consideration of the fiscal and social consequences of the various alternatives open to him."

It seems unlikely that people generally and in the very near future will determine to flex their minds and set out to make their state and local governments fiscally fit. But it does seem that, unlike the citizens of Colombia, Americans are becoming increasingly aware of the fact that a people can have the governmental services they want if they are willing to pay for it in a way that will not hurt anyone unjustly nor benefit another beyond that which is his due.

*Washington State taxes and expenditures* are certain to be an uncommonly important issue in the next session of the legislature which begins January 9, 1967.

Because the League will be concerned with some of the fiscal decisions made at that time, it might be well for League members to file this issue of the Voter for future reference.

1. Charles F. Conlon, Executive Director, Federation of Tax Administrators. From a talk presented at the League of Women Voters of the U. S. Conference on Financing State Government, Chicago, February 17, 1966.
2. Miss Clara Penniman, Chairman, Department of Political Science, University of Wisconsin. From the League meeting on Financing State Government in Chicago in February.
3. L. L. Ecker-Racz, Assistant Director, Advisory Commission on Intergovernmental Relations. From a talk given before The Governor's Conference on "Decisions for Progress," Seattle, Washington June 4, 1966.
4. E. Elwood Ford, Professor, University of Richmond, Virginia.
5. Charles F. Bonser, Resident Director, Commission on State Tax and Financing Policy. From a working paper for a conference on Financing State Government, Indiana, January 18, 1965.