Washington Research Council

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BRIEFLY

The homeowner tax credit proposed by Senate Democrats requires a Constitutional amendment to create a split roll property tax system. Property tax uniformity, required by Constitution, is one of the great strengths of the state system.

Despite assertions to the contrary, the effect of all of the tax breaks since 1993, including Initiative 695, has been to increase the share of taxes paid by business. This flawed property tax proposal further compounds the damage and threatens the state's competitive position for growth and development.

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Senate Democrats Propose Split Roll Property Tax

Senate Democrats were first out of the chute this legislative session with a property tax proposal that would create a classified, or "split roll," property tax system, undoing Washington's constitutional principle of uniform taxation of all real property. This would provide some relief to homeowners, but do nothing for the thousands of businessowners who shoulder one of the nation's highest business tax loads.

Their measure, SJR 8212, would amend the constitution to give homeowners a credit against the state portion of property tax, beginning with a $200 credit next year. In time, this credit could entirely eliminate the state property tax for homeowners.

In unveiling their proposal, Senate Democrats once again pointed to the business tax relief granted by the legislature since 1993, overlooking the fact that much of this "relief" amounted to simply undoing the tax increases imposed by the 1993 legislature. And they ignored the substantial relief that households have received with I-695.

The largest tax reduction since 1993 is in the MVET, which was first reduced by R-49 and then eliminated by I-695. More than 80 percent of this benefits households. The second largest reduction is the property tax cut approved by voters is R-47. Nearly 60 percent of this benefits the owners of single family residential property. On balance, the tax reductions since 1993 provide a greater benefit to households in the coming fiscal year than to business owners.

A 1997 study by the Institute on Taxation and Economic Policy found that businessowners pay over half of the taxes in this state. The reductions since 1993 thus have increased the relative burden on business.

The proponents of SJR 8212 argue that this is not a split roll proposal, which they define as "when one taxpayer gets a tax cut and the rest of the taxpayers have to pay for the tax cut." They say there's no shift because the cut is paid for from the surplus. But the surplus grows on the strength of taxes paid by all taxpayers, including heavily taxed businesses, large and small. These business taxpayers are paying for the tax cut for homeowners. It's a split roll.

The pivotal section of the bill states: "Notwithstanding any other provision of this Constitution, there shall be a credit against property taxes levied for state purposes on owner-occupied residential property. The amount of the credit shall be two hundred dollars for taxes payable in 2001. The credit shall increase each year thereafter by the change in the state personal income for the previous year."

It should be noted that the indexing provision is extraordinary and bears no direct relationship to property values. Annual personal income growth has averaged 7.2 percent over the last 4 years. Growth in personal income reflects increased economic activity, including population growth. Ordinarily a provision like this would adjust for growth by using a *per capita* adjustment. Per capita personal income growth averaged 5.6 percent over the past four years.

In any event, growth in the amount of the credit would not be limited to the growth in personal income, since the measure says, "The legislature may, by statute, increase the amount of the credit."

People who own businesses, including the owners of rental housing, would continue to pay the state property tax as usual, and the legislature could increase their taxes while protecting homeowners through the homeowner credit. If rental property owners receive no benefit, neither will their tenants.

If passed by the legislature, the proposed constitutional amendment would go to the voters in November.

As the Washington Research Council has noted before, uniformity remains one of the great strengths of our state's tax system. Tinkering with the constitution's provision requiring uniform taxation of all real property is a bad idea.

Breaking property tax uniformity would violate one of the basic principles of a good tax system – economic neutrality. According to this principle, the design of a tax system should minimize distortions in economic decision-making. Other things equal, forcing business owners to pay higher property taxes will cause them to shy away from this state.

Addressing a Greater Seattle Chamber of Commerce conference in October, Boeing's chief financial officer, Debby Hopkins, said, "We recently examined the cost of doing business in all the places we currently operate," she said. "We looked at items such as labor costs, property taxes, energy costs and transportation infrastructure. I hate to say it, but out of the 27 locations where Boeing has plants and employees, Washington came out 16th.

Washington only managed to rank as high as that because of low energy rates, Hopkins noted. "This is not a pretty picture. Compared to everywhere else we do business, Washington is below average."

"Right now," she declared, Boeing is looking at where we should locate any future e-commerce subsidiaries. And Washington state isn't even among the top 10 choices."

What is true for Boeing is also true for the state's other employers, from the entrepreneurial startups in the software and biotech fields to the struggling natural resource-based businesses of "the other Washington." We must continue to invest if we are to sustain our existing prosperity and extend it to those who have been left behind.

The 2000 legislative session has just begun. In time, other property tax proposals are likely to emerge, including some that provide substantial relief without requiring a constitutional amendment or worsening the state's precarious competitive position. There are better alternatives.

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