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Washington State Tax Structure Study
Committee Comments on Research Findings
7/12/02

General comments

Nice job on the findings

I would like to see included in the findings information as to overall tax burden for individuals compared with other states and comparisons to other states for sales, property taxes, etc for individuals. Business tax burdens may be harder to show since the B&O tax is on all businesses not just corporations. However, corporate tax burden comparisons with other states would be of interest. I think this would help place WA state taxes in context. DOR already has graphs showing most of this information as we saw at the first meeting.

1. Stability/Volatility

It may be lost in all my papers but I don't think I ever got a copy of the revised short run elasticity measures and short run property tax elasticities weren't shown in the earlier estimates. I would like to see the revised estimates before approving the findings on stability, but without any evidence I would question the statement that "all of Washington's taxes are volatile." In particular, I would question whether the property tax should be described that way. ***(DOR will be sending this information shortly.)***

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Regarding business cycles: The first sentence in the fourth bullet in the findings says: " Washington's business cycles are less volatile than they used to be…". Why use only non-agricultural employment?

Regarding Tax Structure Response to Economic Cycles: The last finding lists four possible policy choices. Number 3 is broader-based taxes and number 4 is a more "diversified portfolio" of taxes. It does not follow that a broader base of taxes or more diversified portfolio would increase stability. This finding only makes sense if one specifies what kind of tax is being added to make the base broader or more diversified.

On this subject some charts or tables would aid the presentation.

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List how volatile taxes used by other states, such as income tax for individuals and corporate income tax, are.

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2. Adequacy of State and Local Revenue

Among the three "main reasons" for spending growth is "longer prison sentences." Extensive discussion of spending is somewhat outside our concern, but I would like to know if an increasing proportion of inmates have been convicted only of drug offenses.

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Growth in Demand for Public Services Compound with Economic Growth

The fifth bullet in this section lists the main reasons that state-spending growth equals or exceeds personal income growth. These points are likely to be questioned and will need data to support them. As I recall this presentation there was good data. How did numbers 2 and 3 happen: demographics, Legislative decision, or other?

The last bullet says that "Increased utilization of health care and special education services also contributed significantly to expenditure growth. " Is this redundant with the point above or is it something different?

Expenditure Outlook and Revenue Adequacy

Is it true that private sector wages increase at a rate exceeding general inflation? We may need to cite some authority for this proposition and some figures would be helpful.

Local Government

The second bullet says, "There is some unused taxing capacity for city government…." It does not appear to me that the fact that some cities in Eastern Washington have not used all of the tax authority available to them has much to do with adequacy of revenue for local governments in general.

The findings under this sub section do not tell us that local governments are hurting which seems to be the point emphasized by several committee members. This not an insignificant omission.

The fourth bullet addresses the city, county and transportation district losses due to the repeal of MVET. If at all possible we need to have something more than an absolute dollar number here. We need percentage or something to illustrate seriousness or insignificance as the case may be.

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How does WA rank in adequacy of state and local revenue compared to other states?
Which counties are closer to their revenue limits and which ones have remaining capacity.

3. Economic Vitality

Under "competitive position of Washington firms," there is the statement that "Washington's B&O tax burden is higher than most states' income taxes." Is that supposed to be "corporate income taxes"?

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I could not disagree more strongly with the statement that "taxes are not one of the most important factors influencing business location decisions." They (taxes) clearly influence the overall business climate and business decisions.

The committee should hold a hearing and get a report from the Port of Kalama, WA. That would provide real-life data on tax incentives. The results are conclusive and clear. Tax incentives produce jobs.

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Tax Incentives and Economic Vitality: The first two bullets seem inconsistent. One talks about facilities and the other about jobs. Most people, including me, would tend to think that the one follows the other.

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"Washington's B&O tax burden is higher than most states' income taxes." An explanation of this statement would be helpful. Is the burden higher based on net income of corporations? Does this statement take into consideration tax burdens of unincorporated businesses?

"Washington's unemployment insurance tax is among the highest of any state for many firms." WHY?

"Washington's industrial insurance tax is among the lowest in the nation for all firms." WHY

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4. Economic Neutrality

Under "intersectoral/vertical equity," the differences in tax rates by industry are more of a neutrality problem than an equity problem. I think they should be included in the neutrality section.

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The first bullet states: “Businesses are increasingly engaged in a variety of strategies to legally minimize their tax obligations in Washington.” I doubt this and I doubt the next sentence that lays it on a decreasing level of federal corporate income tax. Is it a fact that corporate income taxes have decreased? I believe the accounting departments of our businesses are continuously looking for ways to avoid or reduce some state tax and the people they have lunch with from other businesses or their lawyer or accountant waste NO time in passing along something they have seen someone use effectively. The problem is the existence of a place like Nevada, which has, basically, no business tax.

The second bullet states: “Most of these strategies are designed to reduce the level of taxable income, rather than to avoid tax altogether.” Certainly some of “these strategies” avoid <u>all</u> of a certain tax such as the B & O**.**

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The third bullet states: “Strategies to minimize taxes are often inefficient and can be costly to implement. They also increase the complexity and level of effort necessary to review and fairly enforce Washington's tax.” I assume that this means that the strategies are inefficient for the business and costly to the business. Explain why they are inefficient and costly to implement for the business.

The fifth bullet states: “Individuals illegally avoid use tax by making purchases through the Internet, via catalogs of businesses with no taxable nexus in Washington, and making purchases in states with a lower or no (Oregon) sales tax.” How much awareness is there that individuals should pay use taxes on Internet and catalog purchases?

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The quantitative findings on economic neutrality are sparse here. There appears to be mostly anecdotal evidence of non-neutralities resulting from our current tax system. I believe that the

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DOR and the committee economists are trying to get a better handle on quantitative measurement. I think this needs to be done.

5. Equity

Under "benefits received," there is a brief comment about the share of dedicated tax revenue, but earmarking taxes is not the same thing as following the benefits principle. Some earmarked taxes (e.g. gasoline tax for highways) follow the benefits principle, but others are earmarked for political reasons unrelated to benefits.

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Ability to Pay: The second bullet probably refers to households or individuals but we should make that clear.

The third bullets states: “Over a lifetime, taxes become less regressive…” Not sure I really understand (or even believe) this one yet. But is it relevant? People move, people die: shouldn’t tax equity be judged independent of how long you live or how long you live in one place?

Horizontal Equity: The second bullet states: “There is less variation as a percent of spending within spending groups. Spending groups are considered to approximate permanent income.” What principle of equity is under discussion here? I suppose it is the “consumption” principle. He who consumes more should pay more. Or, taxation should be in proportion to consumption. But could anyone suggest that the sales tax motivates rich people to reduce consumption? Nonsense. That would only occur if the rate were progressive.

And in this finding what is meant by the expression “permanent income”?

The third bullet states: “There is significant variation in taxes as a percent of gross income within industry groups”. Do we have to use gross income here? Is net income not available?

There is no finding having to do with consumers who buy goods and consumers who buy services. This is frequently cited as an inequity of a sales tax centered on goods. I doubt there is a dichotomy here—I doubt society can be grouped this way. For those who want to extend the sales tax to services this question seems relevant.

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Intersectoral/Vertical Equity: The second bullet refers to “effective” tax rates. What does that mean? Are findings based on gross income particularly helpful?

In the second sub paragraph of the second bullet there is a reference to small construction firms paying a higher effective tax rate. Can we not assume we are talking about homebuilders here that have a continuing inventory of real property on which they pay property taxes?

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The total of excise and property taxes representations by income groups. Could you have a table so we could see those income groups between low and high income?

Expand information on ability to pay. How does WA overall taxing system compare with other states on ability to pay?

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Vertical equity (listed as "ability to pay"): Can we get some comparisons with other states (or with the federal tax system) as to the relative degree of regressivity? Is there a study forthcoming this fall from a DC thinktank? Also, the findings labeled "intersectoral/vertical equity" should not be included under equity findings. These findings relate more to neutrality than equity. The section labeled "ability to pay" should be labeled "vertical equity."

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I believe that the facts relating to the sales tax as I discussed at our recent meeting should be brought to light and documented in our report. I can’t see how it could be considered regressive.

It should be pointed out that business pays no taxes, rather, it collects them. All taxes are paid by consumers. Any tax increase will fall on the consumers. Any tax change impacts the private citizen.

6. Transparency (Hidden Taxes)

No Comments

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7. Timing of Tax Payments

Try not to use abbreviations for taxes like PUT and REET. People reading the findings may not know what they stand for.

Are property taxes in other states collected in the same manner as in Washington?
Is this tax more lumpy in WA than in other states? Do most people in WA pay their taxes twice a year rather than having the amounts collected through their mortgage payments?

8. Administrative Simplicity

How do the costs of collection for WA compare to same types of costs in other states?

9. Home Ownership

On home ownership: the data needs to be verified by Master Builders of King, Snohomish and other counties. Property taxes do play a large part in home ownership.