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# **The 1996 One Percent Initiative in Idaho**

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## *The 1996 One Percent Initiative In Idaho*

### Abstract:

The 1996 One Percent Initiative in Idaho would have limited property tax rates and the local government expenditures while shifting public school funding to the state. This study shows that Idaho's property tax is unfair and that the proponents tried to use the voters dissatisfaction to reduce government spending.

## **“The Solution”**

The One Percent Initiative was on Idaho’s ballot in November. This initiative was offered as a solution to Idaho’s public finance problems. The 1996 version of the Initiative was much different and more complex than the One Percent Initiative in 1992. In fact, I would say that the 1996 One Percent Initiative was really five initiatives in one.

The “brand name section” of the One Percent Initiative would limit the maximum property tax on property owners to 1% of the taxable value after exemptions are applied. Additional revenues beyond this 1% cap could be raised by local government only if a 67% super-majority of those voting support the idea. In 1992 these requirements made up the entire One Percent Initiative. The 1996 One-percent Initiative has four more provisions.

The “second provision” within the 1996 One-percent Initiative would limit all increases in local taxing districts’ expenditures in a year to the “increase in the cost of living index used for computing Social Security benefits.” Any additional expenditures above this amount would require approval of a majority of the voters in the tax district.

The “third provision” would mandate the provision of local fire, police, and emergency medical services at “a level equal to or greater than that in effect as of October 1,1996.”

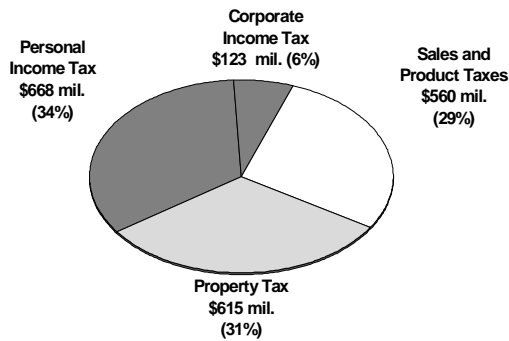
The “fourth provision” would mandate all the existing exemptions to property taxation including the \$50,000 homeowners’ exemption, agricultural and timber use value exemption, and the senior citizens’ circuit breaker. Any changes in these exemptions would require a “vote of the people.”

The “fifth provision” within the 1996 One-percent Initiative would mandate the state legislature to “fund all public education exclusively from general fund and other state and federal revenue sources, by an amount necessary to replace all property tax revenue of all public education.” This increase in state expenditures is to be met through “growth” in the income and sales tax base and “reduced” state expenditures on “other less essential state programs.” Local school boards are to retain “policy-making control, authority, jurisdiction, and structure.”

**Idaho's Tax Revenues**

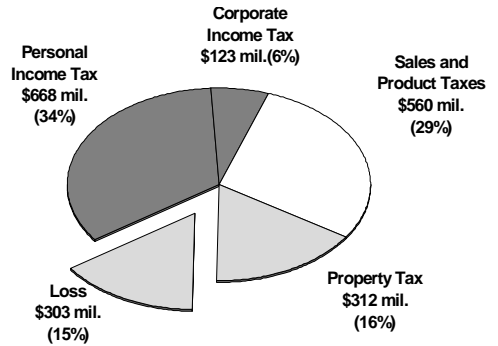
In 1996, Idaho's revenues from all state and local government taxes were about \$2 billion (\$1.966 billion) or about 10% of the gross state product. Tax revenues from the property taxes were \$615 million or 31% of the total. Sales and product taxes raised 29%, and personal income taxes 34%, and corporate income tax 6% of the total. Using the Attorney General's opinion, the Idaho State Tax Commission has estimated that the reduction in property tax revenue from the One Percent Initiative in

**Figure 1. Idaho State & Local Public Revenues: FY 1996**



Total State and Local Revenues = \$1.96 billion

**Figure 2. Idaho State & Local Public Rev. with 1%: FY 1996**



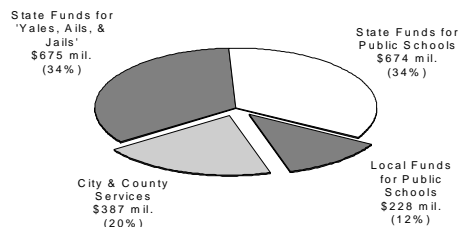
Impact of 1% Initiative = -\$303 million

fiscal year 1996 would have been \$303 million. This represents 15% of all state and local tax revenues (Idaho Legislative Services Office, 1995; Idaho State Tax Commission, 1996).

**Idaho's Tax Expenditures**

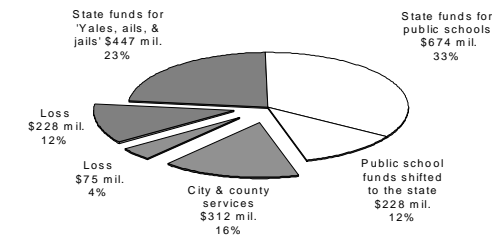
In fiscal year 1996, state and local government expenditures were also about \$2 billion (\$1.964 billion). State government expenditures were \$1.35 billion. These funds were about equally divided between public education (\$674.0 million) and all other services of state government (\$675 million). These other state services include higher and other education (\$247 million), health and welfare (\$244

**Figure 3. Idaho State & Local Public Expenditures: FY 1996**



State & Local Expenditures = \$1.96 billion

**Figure 4. Idaho State & Local Expend. with the 1%: FY 1996**



Impact of the 1% Initiative = -\$303 million

million), corrections (\$112 million), and all other (\$72 million). Local government spent \$615 million in 1996 with \$228 million for public education and \$387 million for cities, counties, road and bridge, and all others.

If the One Percent Initiative were in effect in fiscal year 1996, the \$303 million reduction in property tax revenue would reduce state and local public expenditures in the following way. City, county, road and bridge and other non-school tax district expenditures would be reduced by \$75 million. The \$228 million in local public school spending would be shifted to the state. This \$228 million includes all locally provided public school operating, insurance, overrides, facilities, and emergency funds. Finally, the state's spending on health, welfare ("Ails"), higher and other education ("Yales"), corrections ("Jails"), and other non-public school services would be reduced by an equivalent \$228 million. The Initiative would reduce local and state expenditures services by approximately \$75 million and \$228 million respectively. This equals a 1:3 ratio of relative loss of funds for local and state services. The result is a kind of "billiard ball effect" in which a \$303 million local property tax revenue reduction along with shifting school funding responsibilities results in a \$228 million state expenditure cut in "Yales, Ails, & Jails."

#### **Is There a Problem with Property Taxes in Idaho?**

The One Percent Initiative seems to imply 1) that city, county, and state expenditures are out of line and need to be restrained; 2) that the property tax effort in the state is out of proportion to sales or income taxes, and 3) that the property tax is unfair. Lets look at each of these assumptions

#### **Are Idaho's City and County Government Expenditures Out of Line?**

Property tax revenues in Idaho are levied only by local governments to pay for local public services and facilities. The \$615 million in property taxes are spent on roads (13%), city services (20%), county services (25%), and public schools (42%). The property tax is raised from assessments on three types of real estate and personal property: single and multifamily residences (50%), commercial and utility (40%), and agriculture and timber (10%) (Idaho State Tax Commission, 1993).

Between 1989-93, Idaho's property tax revenues grew about 10% per year. This growth is the result of the growth in the property tax rates (3%/year) and in the property tax base (7%/year) (Idaho Universities Policy Research Group, Jan. 1994). The rate of inflation over this period was about 3% per year. So the annual real growth in property taxes in Idaho on average from 1989-93 was about 7%.



Between 1990-95, Idaho's population grew about 3% per year or three times the national average (US Bureau of the Census). Thus, on a per person basis, real property taxes increased about 4% per year from about 1990-1993.

Is this too much of an increase in property taxes for the increase in population? In a study of 248 large US counties, Ladd found that a rapidly growing areas' population growth increases per capita spending levels of local government. "... The results are clear; rapid population growth is associated with large increases in per capita spending, especially in the areas of transportation and interest on general debt ..." (Ladd, "Effects of Population Growth ..." Structuring Direct Aid, 1993).

In 1993, a home owning family of four from Boise paid about 2.3% of their \$25,000 personal income in property taxes, 1.6% in income taxes, and 2.2% in sales taxes. The national average for property taxes as a percent of income at this income level is 3.4% with half paying at least 2.9. Of the major cities in the surrounding states, only by living in Cheyenne, WY (1.6%) or Salt Lake City, UT (2.2%) would this family pay lower property taxes (Government of the District of Columbia, Tax Rates and Burdens, June 1994).

On average, it would appear that even with the recent big increases in population, Idaho does not have a property tax burden that is out of line either with demand or by comparison to surrounding states or the national average. And yet the 1995 Legislature placed a three percent growth cap on increases in property tax revenues. This limit is determined after the inclusion of new construction and annexations to the tax base (ID Code Section 63-2220A).

### **Is the Use of the Property Tax Greater than Other Taxes in the State?**

Overall, Idaho has a balanced tax structure with a "three-legged stool" of sales, income, and property taxes. The length of these legs is approximately equal as there is 31% in property taxes, 34% in income taxes, and 29% in sales and product taxes. But these legs may not be equally strong. Is the weight of the tax system distributed in proportion to the strength of each leg of the stool?

To measure strength of a tax revenue, we must look at its components: the tax rate and the tax

base. Tax revenues are the product of a base and a rate. A sales tax base is equal to the value of the sales transactions. The value of real estate determines the base for property taxes and the amount of personal income fixes the base of the income tax. A rate is the proportion of the base taxpayers are charged. For example, in Idaho the sales tax rate is 5%, property tax rates (added across districts) average between 0.56 and 2.51%, and the income tax rates are 2.0 to 8.2% depending on the level of income.

The size of the tax base per person is a measure of the ability to pay a tax. The larger the base, then the greater the ability. This tax base per person number can then be compared to the national average and written as a percent. This number represents a measure of Idahoans' ability to pay a tax compared to the national average. This is also called tax capacity.<sup>1</sup> A similar comparison of tax rates results in a measure of Idahoans' willingness to pay a tax or tax effort.<sup>2</sup>

In 1991, the tax bases (ability or capacity) of personal income, sales, and property taxes in Idaho ranged from 72 to 80% of the national average. The tax rates (willingness or effort) on property, sales, and income taxes in Idaho ranged from 82 to 137% of the national average. Idaho's tax structure reveals a strong willingness to raise tax revenues from income taxes. Even with sales tax, Idaho is more willing than able to raise revenues from this source compared to the national average. These numbers suggest that the state tries to compensate for low income and sales tax bases with proportionately higher tax rates.

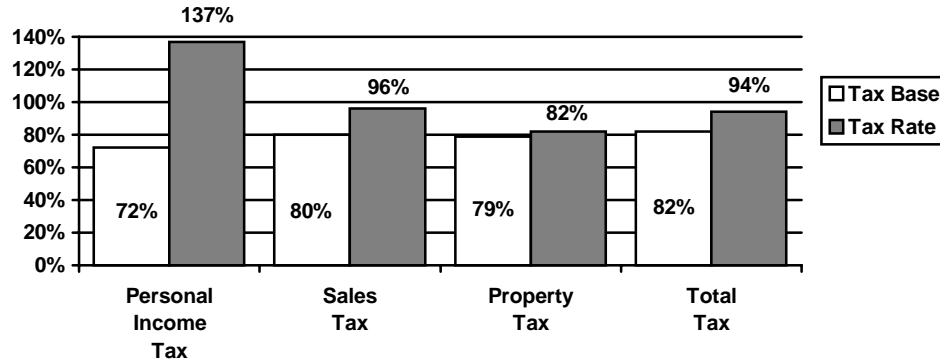
It is only the property tax that willingness equals ability to raise revenues. If we assume that these relationships continue to hold in 1996, then Idaho's tax structure is not over using the property taxes relative to the income and sales taxes. Idaho is under-using its property tax ability to raise revenue when compared to its personal income and the sales taxes. Ironically, this is the tax rate that the One Percent Initiative proposes to cut.

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1. Tax Capacity Index =  $100 * [(nat'l \text{ avg. rate} * \text{state base}) / \text{state pop.}] / [(nat'l \text{ avg. rate} * nat'l \text{ base}) / nat'l \text{ pop.}]$

2. Tax Effort Index =  $100 * [(\text{state rate} * \text{state base}) / \text{state pop.}] / [(nat'l \text{ avg. rate} * \text{state base}) / \text{state pop.}]$

**Figure 5. Idaho's Tax Base and Rates: 1991  
(% of US per person)**



Source: Advisory Commission on Intergovernmental Relations, *State Revenue Capacity and Effort*, M-187, September 1993

**Is Idaho's Property Tax Unfair?**

There are two ways to measure tax fairness. The first measure is based on the ability to pay and is known as vertical equity. The second is based on treating equals equally, called horizontal equity. I shall examine both.

**Ability to Pay**

Does the Idaho property tax make allowances for the ability to pay? We know that in 1993 a family of four living in Boise, ID with a personal income of \$25,000 paid about 2.3% of their income in property taxes. This same family making \$50,000 in personal income would spend about 1.5% of their income on property taxes for a house typical in that income category. This example suggests that among homeowners with personal income between \$25,000 and \$50,000, the lower income families pay a larger share of their income on housing and therefore on property taxes. This example suggests that the property tax does not make allowances for ability to pay. This is an important example because in 1993 half the homeowners in Boise have family incomes of \$36, 400 or less (“Tax Rates and Tax Burdens ...,” Government of the District of Columbia, 1994).

Idaho does have a “circuit breaker” or property tax relief program for low income (\$16,510) homeowners 65 or older, widows/widowers, and disabled. There is also a state property tax homeowners exemption for all owner-occupied structures on 50% of the assessed value up to \$50,000 maximum

exemption. The homestead exemption however does not apply to rental property. These exemptions appear to only modestly decrease or even increase the unfairness of the property tax when examined on the basis of ability to pay.

### **Treating Equals Equally**

Is Idaho's property tax fair in the sense of treating equals equally? As stated earlier, cities and counties are very dependent on the property tax to raise revenue. With the large increase in population Idaho, capital facilities are needed for schools, streets, jails, police and fire stations along with drinking water, waste water, and solid waste treatment and disposal primarily to meet the needs of new residents and businesses. This tax burden falls on current property tax payers. Yet current residents and businesses see little if any increase in service levels to themselves even as tax rates and assessments increase.

The shifting of the burden of growth from new to current property tax payers appears to violate the principle of treating equals equally. One way to address this problem is through "impact fees." An impact fees is a way new subdivision taxpayers can pay back current taxpayers who have carried the additional sewer and water expenses by maintaining excess capacity in the system in anticipation of growth. The 1996 legislature permitted the use of the impact fees for cities in Idaho as well as those in Ada county. Not enough time has passed to realize the effect of this legislation on property taxes. However, new school buildings are not included in the impact fee law.

### **Voter Perceptions**

A poll taken in 1993 shows that 73% of Idaho citizens consider the property tax the "least fair" tax when ask to identify unfair taxes among corporate income tax (56%), personal income tax (50%), and sales tax (25%) (Idaho Universities Policy Research Group, 1994).

The perception of voters in Idaho is that local government is more effective in spending tax dollars than state government. Idaho citizens seem to believe that the closer the unit of government is to the voter, the more confidence they can have in its spending decisions.(Idaho Universities Policy Research Group, 1994).

As for state spending priorities, the survey suggests that voters would prefer to increase expenditures on public education (72% agreed), roads (72%), higher education (53%). On the other hand, only a minority wanted to increase spending on corrections (40%) or social services (24%). And yet, between 1990 and 1995, a decreasing share of the state budget was spent on public schools (-2%) and higher education (-2%), and all other spending (-2%) while increasing shares of spending went to health and welfare (5%) and corrections (1%) (Idaho Legislative Service, 1996).

Taken together, these survey results suggest that Idaho citizens like local government expenditures but do not like the property tax as currently instituted to collect the revenues. On the other hand, citizen appear to prefer the state's income and sale tax revenues but not the state's expenditure priorities.

### **Does the Proposed Solution Match the Problem?**

In summary, the data suggests that the state may already be providing too much support (75%) to public schools and perhaps creating too much state intrusion in the local school decision-making process. Also, city and county real expenditures growth (4% per person) does not appear out of line either with the demand of a rapidly increasing population or by comparison to surrounding states or the nation. The property tax effort in Idaho is less than that for either the sale or income taxes. However, there does appear to be a problem with the equity of the property tax. Using either the ability-to-pay or treating-equals-equally criteria, the property tax in Idaho can be shown to be unfair.

How does the 1996 One Percent Initiative solution match up to this description of 'the problem?' The One Percent Initiative would do the following.

- 1) Limit the property taxes (that voters do not like) to provide city and county services (that voters do like and provided by units of government they trust).
- 2) Shift the local share of public education expenditures (an expenditure voters like the most) to the state (a unit of government voters trust less) and fund entirely with sales and income taxes (taxes that they dislike less than property taxes).
- 3) Trust the state legislature and the governor to make public education spending an increasing share of the budget even as it reduces all other state services by a third. This in spite of legislative priorities that have historically moved in the opposite direction.

A vote for the 1996 One Percent Initiative is a vote against a property tax that Idahoans dislike more and a vote in favor of a unit of government that Idahoans trust less.