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Thomas Allen Moon

William D. Moon

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THE PROPERTY TAX, GOVERNMENTAL SERVICES, AND EQUAL PROTECTION: A RATIONAL ANALYSIS

THOMAS ALLEN MOON†

WILLIAM D. MOON‡

I. THE PROPERTY TAX AND GOVERNMENT SERVICES IN PERSPECTIVE

A. Introduction

RECENTLY, the federal courts have been called upon to determine how state and local governments may distribute the services they perform. Three of these cases[1] have focused on inequities in services supported primarily through the local property tax. The popular press[2] is replete with stories of taxpayer discontent with sharply rising property taxes and static or declining levels of services. This incongruity —

† Member of the Texas Bar. B.A., Texas Christian University, 1964, M.A., 1973; J.D., University of Texas, 1971.

†† Member of the Texas Bar. B.A., Texas Christian University, 1969; J.D., University of Texas, 1971.

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1. Hawkins v. Shaw, 437 F.2d 1286 (5th Cir. 1970), held that municipal corporations must provide municipal services equally to all citizens; Rodriguez v. San Antonio Independent School Dist., 337 F. Supp. 280 (W.D. Tex. 1972), *rev'd*, 93 S. Ct. 1278 (1973), and Serrano v. Priest, 5 Cal. 3d 584, 487 P.2d 1241, 96 Cal. Rptr. 601 (1971), both initially holding education to be a "fundamental interest" have, in light of the recent Supreme Court decision, been overruled, at least as a matter of federal constitutional requirements.

2. Two recent articles, in particular, point out the futility sensed by many at the continuing problem of high taxes and poor services at the state and local level. One predicted that governmental spending by state and local governments throughout the United States will continue to increase for the foreseeable future with a resulting increase in pressure on property owners. U.S. NEWS & WORLD REP., June 7, 1971, at 59–61. The other, an Associated Press story, described the uneven growth rates and unequal property tax burdens, with resulting disparities in the level and quality of public services, among the different communities comprising the major metropolitan areas of the country. Austin Statesman, June 28, 1972, at 84, col. 1. These articles illustrate the intensity of the property tax burden, the unequal availability of local services, and the inequity of some local tax burdens as compared with others. In light of these facts, both articles express resignation about the continuation of these trends and the failure of our institutions to cope with them.

rising taxes and declining services — prompted President Nixon to submit a revenue sharing program intended to alleviate the growing squeeze on local taxpayers. In his revenue sharing message, he stated:

> Nearly three-fourths of their [state and local governments'] tax revenues come from property and sales taxes, which are slow to reflect economic expansion. It is estimated, in fact, that the natural growth in revenues from these sources lags some 40 to 50 per cent behind the growth rate for State and local expenditures. This means that budget expansion at these levels must be financed primarily through new taxes and through frequent increases in existing tax rates.[3]

The attention of the courts thus far has been directed primarily to disparities in the levels of services and only incidentally to the method by which these services are financed. This emphasis upon the property tax is important because it is the largest single source of revenue at the local governmental level.[4]

Although utilization of the property tax in Texas will be the focal point of this Article, the basic thrust of the scheme developed here has general applicability. The study begins with a survey of the uses and theories of assessment of a property tax. Next, the economic consequences of such a tax are explored, with emphasis on the equity of the tax in relation to the services it supports and its effect on resource allocation. Current legal approaches to disparities in state and local services are then examined. After reviewing the current status of the law, an alternative method of approaching these disparities is suggested. Finally, brief illustrations of the alternative approach will be offered, using Texas as a laboratory state. This effort is intended only as a preliminary examination of the problem and does not pretend to supply the definitive answer.

B. Utilization of the Property Tax

As a prelude to this Article, the role of the property tax as a supplier of revenue for the support of governmentally provided services must be placed in perspective. Historically, the various states have utilized the property tax similarly. In large measure, this tax base has been reserved for local governments, with the state governments utiliz-

3. H.R. Doc. No. 92-44, 92d Cong., 1st Sess. 3 (1971).

4. In 1967-68, the property tax accounted for $26,835,300,000 out of a total local tax revenue of $31,171,400,000. The only other significant taxes levied by local governments include sales taxes, accounting for $1,932,000,000, and personal income taxes, accounting for $1,077,000,000. ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS, STATE AND LOCAL FINANCES: SIGNIFICANT FEATURES 1967-1970, at 30 (1969) [hereinafter cited as SIGNIFICANT FEATURES].

ing different revenue sources. Despite this apparent similarity, a basic dissimilarity, which is the focus of this analysis, has arisen among the states. This dissimilarity lies in the different demands the various state governments impose upon local governmental units in financing programs, particularly in the areas of welfare and education. It is the significance and consequences of these differentials that form the factual basis of this Article.[5]

In seeking to identify the relationship of the property tax to service levels, tax equity, and the role that the equal protection clause of the Federal Constitution should play in rationalizing this relationship, specific references will be made to the manner in which Texas employs this tax base. In this respect, Texas is among those states that impose relatively moderate demands upon local taxpayers to support local services, particularly welfare. At the other end of the spectrum, New Jersey is among those states that assign a primary role to the utilization of locally raised property tax revenue in support of public programs.[6] Texas, then, will be used as an example in order to present certain concrete empirical illustrations which are offered only as a point of departure. Throughout this inquiry, certain underlying functional considerations[7] should be kept in mind. In this respect, it is clear that, oftentimes, the support that particular programs will receive will be

5. *See id.* at 53 (Table 18).

6. *Id.* at 50–51 (Table 16).

7. "Functional consideration," as used here, involves the interrelationship between the use of a given tax to support a given service and the ensuing effects among taxpayers and quality of governmental service.

If taxpayers, or purchasers of particular public services, perceive benefits from a particular program and feel that the distribution of the burden of paying for such a program is fair, then the program will probably be well funded. To the extent that this proposition is correct, its converse would seem correct also. Therefore, policymakers' choice of a tax base and its structure would appear to be a critical decision in terms of how well supported a given service will be.

The recent election in El Paso concerning whether the county should be authorized to levy a local property tax to supplement state aid for the El Paso County Junior College underscores the problem. In that election, property owners voted 2 to 1 against the proposal, indicating that, as a class, they perceived little benefit from increased expenditures, at their expense, for a junior college. *See* El Paso Times, Aug. 31, 1972, at 1, col. 3.

Subsequently, one disgruntled property owner justified his negative vote in the following terms:

> [T]he property owner has become tired of being the "fall guy." I do not object to paying a fair share for a worthy program such as the Community College. But what I do object to is being saddled with tax after tax past the saturation point, while others who should share in the cost are reaping the harvest at my expense. When the governments, local, county and state, establish an equitable tax structure, I will support all programs that I deem worthy of support. Until that time comes, I will continue to resist additional taxes, and I will encourage others to do likewise.

El Paso Times, Sept. 5, 1972, at 5, col. 3.

At the outset of this study, then, there should be an awareness that regardless of the merits of a particular program, taxpayer-perceived defects in the tax scheme for financing given programs can result in underfinancing of otherwise "worthy" programs.

largely determined by which tax base is used to supply revenue and how the rates of that tax are skewed. It is within this framework that the uses of the property tax by state government, school districts, and county and special districts will be examined.

1. State Government

While in the broad sense all property taxes are state taxes levied pursuant to the taxing power of the state, "the property tax" is really not a single tax, but rather a cluster of separate taxes utilized by different units of government in different ways with each particular tax sharing only the same name and some of the same underlying aspects. Different amounts of supervision of the property taxes are exercised by different states. Some states exercise broad supervision in terms of what is within the tax base, what assessment ratio should be used, what the maximum and minimum rates should be, how much debt should be allowed on a tax base, and how the rules should be administered, while others exercise very little supervision.[8] Although these administrative problems are important, they are not central to this inquiry.

Initially, under the Texas constitution, the property tax was envisioned as the primary tax source for the general revenue fund.[9] However, its role as a revenue producer has steadily declined, until, in 1951, a constitutional amendment ended the tax altogether.[10] Property taxes continued to be collected at the state level for the support of public education, but even this function has recently been terminated. In 1967, Texans approved a constitutional amendment phasing out the statewide-collected property tax by 1978, thus ending the last major state demand for revenue on property taxpayers.[11] The conclusion by Texas that the property tax is an unsuitable device for financing the

8. For a discussion of the state-local relationship in property tax administration and of policy tensions growing out of this relationship, *see* Shannon, *Conflict Between State Assessment Law and Local Assessment Practice,* in PROPERTY TAXATION USA 39 (R. LINDHOLM ed. 1967).

9. Although in the early years the property tax served as a major revenue source for the state, its importance faded with the emergence of natural resource taxation. In the early 1930's, the depression acted as a catalyst for abolishing it. The lack of uniformity in its administration on both an intracounty and intercounty basis created much public dissatisfaction. To a large extent, each county administered the state property tax as it saw fit. Assessed valuations varied significantly among the counties, and taxable property was frequently omitted from the tax rolls. In short, the state tax burden was spread unevenly among localities, and there was too little public support for this form of taxation to justify renovating its administration. *See* L. ANDERSON, THE STATE PROPERTY TAX IN TEXAS: REQUIEM OR REJUVENATION 1-4 (1963).

10. TEX. CONST. art. VIII, § 1(a).

11. *Id.* § 1(e).

expanding cost of government at the state level,[12] and the consequent reduction of the state's reliance upon such a tax, is typical among the states.

One interesting pattern of misuse of the property tax exists in New Jersey, where the state has constructed a method of financing various welfare programs with local property tax revenues.[13] Although an agency of the state government prescribes rules and regulations for uniform administration, much of the responsibility of paying for these programs has been assigned to county governments. Simply stated, for the broad range of these programs, the counties are required to pay 25 per cent of the cost of the program within each county.[14] County governments have no say, however, in determining benefit levels, or whether or not to tax. Under this scheme they must not only dispense state-determined benefits, but must tax local resources to pay the costs.[15] As might be expected, the incidence of welfare recipients varies among the counties. Illustrating how this results in tax inequity, Essex County has 12.97 per cent of New Jersey's population, but 27.48 per cent of its welfare recipients.[16] Based on the fact that the wealth of the property tax base varies among the counties, the property tax levies to support these programs at the local level will similarly vary significantly, sometimes by as much as 1000 per cent.

The pattern of financing education is that, generally, the states make virtually no effort to impose uniform service levels on disparate tax bases, but rather permit localities to fund services according to local choice. In New Jersey's system of financing welfare, in which the state dictates benefit levels, certain economic pressures are generated by the unequal incidence of the tax on a geographic basis; however, in the general scheme of financing education the economic pressures are avoided, but at the expense of service disparities. The economic effects of both service-level disparaties and its reciprocal, geographic tax-level disparities, will be examined in depth below.[17]

12. The dependence of state governments on property taxes has fallen from over 50 per cent in 1902 to 1.3 per cent in 1962. Presently, then, property taxes represent a negligible source of revenue for state governments. ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS, II THE ROLE OF THE STATES IN STRENGTHENING THE PROPERTY TAX 71 (1963) [hereinafter cited as STRENGTHENING THE PROPERTY TAX].

For a detailed history of the property tax, *see* J. JENSEN, PROPERTY TAXATION IN THE UNITED STATES (1931).

13. These programs include the categorical programs of Old Age Assistance, N.J. REV. STAT. § 44:7-6 (1940); Aid to the Totally and Permanently Disabled, N.J. REV. STAT. § 44:7-41 (Supp. 1972); Aid to the Blind, *Id.* § 44:7-44; Aid to Families with Dependent Children, *Id.* §§ 44:10-1 *et seq.;* and Aid to the Working Poor, *Id.* §§ 44:13-1 *et seq.*

14. *Id.*

15. This method of financing welfare has recently been challenged in a class action suit. Bonnet v. Cahill, Civil No. L-3865-72 (Super. Ct. N.J., filed Oct. 11, 1972).

16. *Id.* at 21-22.

17. *See* text accompanying notes 58-112 *infra.*

2. School Districts

At present, independent school districts in Texas constitute the major drain on the property tax, utilizing 51.2 per cent of the total property tax revenue in 1969.[18] In 1940, only 35 per cent of property tax revenue went to school districts.[19] Since then, schools have increased their percentage share each year and in recent years at an accelerating rate.[20] This situation is ironic because, in Texas, local school districts had been initially denied taxing authority.[21] Subsequently, such authority was conferred in two stages, first in 1883,[22] and then in 1909.[23] Placing taxing responsibility at the local level for a large share of the cost of education has created a seemingly insoluble problem. All local districts do not now and never have had the same tax base.[24] Because of the wide disparities in capability to finance education at the local level, the Texas legislature enacted the Foundation School Program (FSP) in 1949 in an attempt to "equalize" the financial burden among the various school districts for support of the basic programs vital to each district.[25]

It is worthwhile to explore briefly Texas' attempt at state-wide equalization of the property tax, because efforts in this direction

18. Letter from Texas Research League to the author, Mar. 15, 1971, in which total local property taxes are compared with school property taxes (1940–1970) and with projections of school taxes to 1979 (on file with *Villanova Law Review*).

19. *Id.*

20. *Id.*

21. TEX. CONST. art. VII, § 3 (1876).

22. TEX. CONST. art. VII, § 3 (1883).

23. TEX. CONST. art. VII, § 3 (1909).

24. A standard index for measuring the relative tax bases among school districts is the ratio of taxable property to average daily attendance (ADA). The Ector and Edgewood Independent School Districts illustrate the difference in tax bases among Texas school districts of similar size. Ector has a tax base of about $26,000 per ADA, while Edgewood has a tax base of only $3,600 per ADA. Since Edgewood assesses at 35 per cent of market value and Ector at 30 per cent, this disparity is magnified. These figures are computed from information in the following materials: C. BARTLETT, PROPERTY TAXES IN TEXAS SCHOOL DISTRICTS: A STUDY FOR THE GOVERNOR'S COMMITTEE ON PUBLIC SCHOOL EDUCATION (1969); TEXAS EDUCATION AGENCY, ANNUAL STATISTICAL REPORT: 1968–69, PART 2, at 2 (1970) [hereinafter cited as TEA REPORT]; and TEXAS MUNICIPAL ADVISORY COUNCIL, SPECIAL REPORT No. 80, at 35 (1971) [hereinafter cited as MUNICIPAL REPORT].

25. In order to avoid confusion, the FSP applies only to certain elements of the overall program of education. Under the FSP, the state guarantees each school district minimal pupil-teacher ratios and minimal teachers' salaries, as well as certain basic programs including special education, vocational education, kindergarten, and transportation. *See* TEX. EDUC. CODE ANN. §§ 16.01 to .98 (1972). If localities want smaller pupil-teacher ratios, higher teachers' salaries, and additional programs, they must finance them locally from the property tax. School construction is also a purely local concern which, in large part, explains the differences in quality of plant throughout the state. Local expenditures above the FSP are called "enrichment." Capacity to "enrich" education locally will be discussed below. *See* notes 100–12 and accompanying text *infra*. For a brief history of the development and purpose of the FSP, *see* V REPORT OF THE GOVERNOR'S COMMITTEE ON PUBLIC SCHOOL EDUCATION: THE CHALLENGE AND THE CHANCE (1969) [hereinafter cited as COPSE REPORT]. This approach is for the most part typical among the states.

continue to be the approach taken by many states in solving variations in taxable property wealth from district to district.[26] Theoretically, there are three methods of channeling revenue from greater to lesser taxing authorities: the social equity approach, the incentive matching approach, and the political economy approach. In the social equity approach, the state determines the level of performance or the money outlay per unit of need, and equalizes one or the other factor among its constituent school districts; neither the economic capacity nor the tax effort of the districts play any role in determining the amount of the state subsidy. The state provides no incentive for local supplementation. In the incentive, or matching grant approach, the individual districts determine the level of performance or the money outlay per unit of need, and thus no equalization of performance levels, money outlays, fiscal capacity, or tax effort results. In the political economy approach, the state merely equalizes the fiscal potential of the constituent districts, with each district then determining its own outlay per unit of need.[27]

The Texas FSP most nearly resembles the political economy approach by which the state, through a distribution formula, sends greater amounts of state aid to poor districts in an effort to place them in parity with wealthier districts.[28] Texas, as most other states, uses an equalization program to compensate, though only partially, for interdistrict wealth disparities.[29]

To date, however, no state has devised an equalization program or formula based on utilization of the property tax which has proven capable of establishing financial parity among its school districts. In this respect, the inequities of various state formulae have recently attracted the attention of the courts, most notably in *Serrano v. Priest*[30] and *Rodriguez v. San Antonio Independent School District.*[31] In an effort to come to grips with this problem at the political level, Governor William Milliken of Michigan proposed a totally state-financed educa-

26. *See* ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS, STATE AID TO LOCAL GOVERNMENT 31–59 (1969) [hereinafter cited as STATE AID TO LOCAL GOVERNMENT].

27. D. MORGAN & F. HAYDEN, ELEMENTARY AND SECONDARY EDUCATION AID: TOWARD AN OPTIMAL PROGRAM FOR THE STATE GOVERNMENT OF TEXAS 13 (1970).

28. Despite the conceptual similarity of the FSP financing provisions with the political economy approach, significant elements of the incentive matching approach also appear in the distribution formula of state aid to local districts. For a detailed discussion, *see id.* at 56–83.

29. *See* TEX. EDUC. CODE ANN. § 16.74 (1972). The Texas equalization program, as well as those presently utilized by most other states, is a direct outgrowth of an approach pioneered by George Strayer and Robert Haig. For the history of this device of coordinating state aid to local education, *see* G. STRAYER & R. HAIG, THE FINANCING OF EDUCATION IN THE STATE OF NEW YORK (1923).

30. 5 Cal. 3d 584, 487 P.2d 1241, 96 Cal. Rptr. 601 (1971).

31. 337 F. Supp. 280 (W.D. Tex. 1972), *rev'd,* 93 S. Ct. 1278 (1973).

tion program as an alternative to Michigan's heavy reliance on property taxation.[32] In any event, equal educational opportunity, in terms of equalized financial potential, depends upon the development of better formulae for apportioning the property tax burden among localities. Evaluation of whether this search for a better index is worth the effort, or whether a new direction such as the Michigan approach is necessary, must await an analysis of the interdistrict economic effects of property taxation.

3. Cities

Second only to schools, cities in Texas claim the largest share of the property tax. For instance, in 1966 municipalities raised $305.2 million from this tax source which represented 28.7 per cent of the total.[33] Despite passage of a one per cent optional city sales tax, property taxes still provide the major revenue source for Texas cities.[34] Though cities and school districts both rely on the property tax, the role of the tax for each is fundamentally different.

Neither cities nor schools have a local alternative tax source, but cities, unlike schools, have access to outside sources of revenue. These alternative revenue sources for cities are geared to the services municipalities typically perform. Functionally, these include fire and police protection, public safety, health, streets and highways, sanitation, public works, utilities, and general administration. Certain of these services are susceptible to being financed through user charges[35] on the basis of the benefits received. Using Fort Worth as an example, its airport funds and water and sewer operating fund sustain themselves without property tax transfers, while its parks and recreation

32. Pointing to the siphoning of $1.181 billion of property tax revenue for a system of education that tolerates interdistrict per pupil expenditures ranging from $500 to $1200, Governor Milliken proposed the virtual elimination of property taxation for support of education. As alternative revenue sources, he suggested replacing the $700 million in property tax revenue paid by individuals with a personal income tax, and the $500 million paid by businesses with a value-added tax. Address by Governor Milliken, Special Message to the Legislature on Excellence in Education — Equity in Taxation, April 12, 1971, at 5 (mimeograph release on file at *Villanova Law Review*) [hereinafter cited as Address by Governor Milliken].

33. BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, VII CENSUS OF GOVERNMENTS: 1967, STATE REPORTS — TEXAS 29 (1969) [hereinafter cited as STATE REPORTS — TEXAS]. These census reports are published every five years. As a result, the next publication will be based on 1971–72 figures and will be printed in 1973. Except in particular instances, this data is the most recent available.

34. Fort Worth's relative dependence on the property tax points out its continued importance, even after passage of the sales tax. In 1970–71, Fort Worth received $8,500,000 in sales tax revenue as compared with $21,539,098 in property tax revenue. CITY OF FORT WORTH, SUMMARY: ANNUAL BUDGET (1970–71), § 2, at 3 (1970).

35. F. MICHELMAN & I. SANDALOW, MATERIALS ON GOVERNMENT IN URBAN AREAS 709–10 (1970).

funds only require 53 per cent and 49 per cent transfers, respectively.[36] Even the general revenue fund, from which most municipal services are financed, required only 49 per cent of its revenue from the property tax.[37] This user tax technique, as an ameliorant to overreliance on property taxation, is utilized in varying degrees by major cities in Texas.[38]

While Texas attempts "equalization" of property tax revenue potential for school districts by means of the FSP, it makes no corresponding effort on behalf of cities. Also, while the state contributes $950.9 million[39] to local school districts, it has no general program of state aid to cities. With respect to this lack of state aid, Texas municipalities, unlike those in other states which have extensive state-aid programs, are not permitted either to supplement welfare or to subsidize public housing programs.[40] Under the Texas approach then, cities support only basic municipal services and not a full range of social and welfare programs.

4. *Counties and Other Political Subdivisions*

In 1967 counties absorbed 17.3 per cent of the Texas property tax and special districts absorbed the remaining 3.7 per cent.[41] Analysis of revenue raised locally reveals that counties use the property tax similarly to cities, with the exception that the legislature has authorized cities to add a one per cent sales tax[42] to lighten the property tax load. Generally speaking, counties, like cities, use a combination of property tax revenue and user and licensing fees to finance their services. On a state-wide average, counties finance approximately 64 per cent of their services through the property tax as compared with only 37 per cent by municipalities.[43] Because of the different roles that counties and cities play in the overall scheme of local government, important differences in their utilization of the property tax exist.

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36. CITY OF FORT WORTH, *supra* note 34, at 26, 27.
37. *Id.* at 13, 15.
38. CITY OF FORT WORTH, FACTS & FIGURES FOR THE FISCAL YEAR ENDING SEPTEMBER 30, 1971, at 107 (1971).
39. This figure represents FSP cost to the state for fiscal year 1972. TEXAS COMPTROLLER OF PUBLIC ACCOUNTS, REVENUE ESTIMATES 1971–73, at 11 (1971).
40. The only subsidy that public housing authorities receive from local governments is an exemption from paying property taxes. Conversely, however, the state constitution forbids these districts to be operated at a profit. TEX. REV. CIV. STAT. ANN. art. 1269k (1963).
41. STATE REPORTS — TEXAS, *supra* note 33.
42. TEX. REV. CIV. STAT. ANN. art. 1066c (Supp. 1972).
43. These figures are computed by finding the respective percentages of property tax revenues to total locally raised revenue, including user charges and utility revenue. State and federal revenue provided to cities and counties is marginal. STATE REPORTS — TEXAS, *supra* note 33. With the passage of the city sales tax, urban reliance on the property tax, as compared with counties, is further reduced.

Counties, unlike cities, have little flexibility in experimenting with the user-charge or licensing-fee concept as an alternative to overburdening the property tax base. Although certain county services parallel and even overlap municipal services, such as roads, law enforcement, and public health and sanitation, county governments serve as the agent of the state rather than as a public corporation organized for the benefit of the citizens within its boundaries. For example, in Texas the state delegates to the counties many of its functions, such as welfare administration, voter registration, automobile licensing, and maintenance of a court system. In large measure, the state, not the county, determines which of these functions are to be financed through fees and which through property taxes. Despite the built-in inflexibility, the pattern of county finance does reflect an effort to make most of the administrative services of the county self-sustaining and to limit use of property taxes for the support of services which benefit property owners more than other citizens.[44] But until Texas moves in the direction of county home rule and consolidation of city-county services, county reliance on the property tax as its basic general revenue source will continue.

Though accounting for only a marginal amount of the total property tax dollar, special districts offer an important illustration. As creatures of the state, these districts, authorized either by the constitution or by statute, permit the citizens of a particular area to form a political subdivision to perform a particular function or functions,[45] and, depending on their purpose, they may or may not possess taxing power.[46] Fire protection, hospitals, airports, housing and urban renewal, drainage, flood control, irrigation, water and soil conservation, and sewage represent some of the services that these governmental units provide.[47]

44. Using Travis County as an example, the special road-and-bridge fund and the farm-to-market road fund are supported by earmarked property taxes. Both of these funds support a service that benefits property owners and property. Without transportation arteries the value of the land would be severely diminished; in this instance, property owners get what they pay for and can determine just how much of a given service they need. Based on this criteria, the overall financing of the special road-and-bridge fund presents an interesting, if rudimentary, illustration of the benefit principle. In addition to property tax revenue, automobile licensing fees and rebates from the state gasoline tax represent a further effort to tax those who benefit from a given service. TRAVIS COUNTY, OPERATING BUDGET: CALENDAR YEAR 1971, at 37 (1971).

Although this plan of taxation does not reflect a precise cost-benefit analysis as a measure of tax liability, it does, nevertheless, reveal a general effort to pay part of the cost of transportation by means of a user-fee concept.

45. *See* W. BENTON, TEXAS: ITS GOVERNMENT AND POLITICS 383-84 (2d ed. 1966).

46. In fact, of the 1001 districts in the state, only 477 have the power to levy property taxes. STATE REPORTS — TEXAS, *supra* note 33, at 13.

47. For a somewhat dated but still useful survey of special districts in Texas, *see* W. THROMBLEY, SPECIAL DISTRICTS AND AUTHORITIES IN TEXAS (1959).

Typically, either local property taxpayers themselves, or city or county governments, organize these instrumentalities to provide locally desired services.[48] Unlike counties, these subdivisions exercise no state functions but exist only to provide services. Most districts need not, and cannot, exist without the support or acquiescence of the property owners within their boundaries. When the local property owners' need or desire for a given service ends, the district may be dissolved;[49] counties, on the other hand, have an independent existence.

For the most part, the services that these districts provide inure principally to the benefit of property owners. As an example, water control and improvement districts serve as a device to make possible programs concerning public water utilities, flood control, drainage, irrigation, and preservation of water.[50] The nature of these services precludes property owners from undertaking the services themselves or from purchasing them from private enterprise. Practicality dictates that a governmental tool, similar in many respects to a private corporation, be organized to meet these needs. In reality, this device is little more than a nonprofit public corporation, retaining only those governmental characteristics, such as the power of eminent domain, necessary to permit it to function successfully. Even the theory of taxation reflects the unique relationship between this kind of governmental entity and the property owner. All water improvement and control districts may tax on a benefit basis instead of levying a property tax. Under the benefit option, property owners finance the district by paying specifically for the benefits that they receive according to a formula established by the local board.[51] Here, just as with municipalities' financing of certain utilities, the user, not the property taxpayer, pays for the benefits received.

While many of the services performed by special districts benefit property owners more directly than the general populace, some do not. Airport, junior college, and hospital districts are examples of governmental services funded by property owners which do not directly benefit them. In each of these instances, the financing of services by means of the property tax must be justified on some basis other than benefits conferred to the service recipient.

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48. *Id.* at 54–59.

49. Water control districts serve as examples of a special district which can be dissolved by the property owners themselves when the service provided by that district is no longer "beneficial" or becomes "impractical." TEX. REV. CIV. STAT. ANN. art. 7880–77b (1954).

50. *See* W. THROMBLEY, *supra* note 47, at 61–65.

51. TEX. REV. CIV. STAT. ANN. art. 7880–30 (1954).

5. Summary

The evolution of the use of the property tax in Texas as a revenue source for the support of governmental services has, for the most part, followed functional lines. With the exception of education and public hospitals, property tax revenue primarily supports local services that offer disproportionate benefits to property owners, thereby establishing a rational and equitable connection between the revenue source and the governmental expenditure. Additionally, Texas property owners have been spared responsibility for supplementing welfare[52] and supporting public housing locally. Since cities, counties, and special districts use the property tax for predominantly local purposes, the state makes no effort at intergovernmental equalization of revenue potential. On the theory that the quality of local services is a local concern, no justification appears for state administration of the property tax for these governmental bodies.[53] Texas, like most other states, has recognized that the property tax is a poor revenue producer for its general revenue fund. As a result, the state has phased out use of the property tax in favor of more broadly based, fast growth taxes. Only in its

52. *See* text accompanying notes 13–16 *supra.*

53. If revenue from various property tax bases can be limited to the support of governmental services having an economic impact coextensive with each tax base (*see* notes 200–38 and accompanying text *infra*), then only those taxpayers within each individual tax base should be heard to complain about tax inequities within their respective subdivisions. If, on the other hand, property tax bases support services with greater economic impact than that which any individual tax base covers, alleged tax inequities in one area will affect all, thus giving every taxpayer in the state an economic interest in fighting for tax equity in every district. The latter pattern, in fact, prompted the court in Weissinger v. Boswell, 330 F. Supp. 615 (M.D. Ala. 1971), to compel the State of Alabama to equalize assessment ratios in all districts throughout the state. A petition in Fort Worth Independent School Dist. v. Edgar, Civil No. 4-1405 (N.D. Tex., filed Feb. 13, 1971), relying on the same theory as *Boswell,* is currently challenging certain aspects of Texas' use of the property tax to finance education. In Texas, the alleged discrimination involves use of county-assessed valuations. At present there is no standardization of county assessment ratios or appraisal techniques. Essentially, both cases seek to use the equal protection clause to guarantee that the state treat all property taxpayers alike and that no locality gain a tax preference at the expense of any other.

A close reading of *Boswell,* however, does not lead to the conclusion that local tax bases supporting local services have to be "equalized" in terms of assessment ratios; the property tax in question in both *Boswell* and *Fort Worth* involved a statewide tax. These cases, as a result, will not necessarily compel "equalized" assessment ratios in cities and special districts. But, where *Boswell* does apply, as with property taxation with statewide impact, if assessment ratios must be "equalized," then logically, appraisal techniques must also be standardized. Presently in Texas, as in most states, there are about as many appraisal techniques as there are tax offices. Therefore, application of *Boswell* could lead to the creation of a single standard with new and massive administrative machinery to enforce it. Considering the problems inherent in administering the property tax equitably within a relatively small area, one can imagine the difficulties of administering the tax statewide.

From an administrative standpoint, then, a strong case can be made that the property tax should be confined to purely local use. Otherwise, the tax will inevitably become either grossly inequitable or too cumbersome to administer. In either case, the unpopularity of this tax, as compared with other taxes, will increase, and the services dependent upon it for financing will suffer.

support of education is the property tax utilized to finance a major governmental service with an extra-local impact. The cost of education, which doubles about every seven or eight years,[54] threatens preemption of property tax revenue at the expense of other governments.

Although the property tax burden in Texas is relatively light, particularly when compared to the Northeast and Far West,[55] the burden is sufficient to deprive various local governments of needed revenue. Moreover, in inflationary times taxpayers especially guard against tax increases. In this respect property owners have the capacity, because of the closeness and immediacy of the taxing jurisdiction, to register their resentment against high taxes by voting down local bond issues.[56] The previously mentioned method of financing welfare in New Jersey, in which disproportionate tax burdens resulted, is a clear example of how municipal services can be starved if a state makes inappropriate demands on a local tax base. With a number of local governments drawing upon the property tax for support, tax responsibility is difficult to place. To ameliorate this problem, some of the strain should be taken off property taxpayers. This reduction of demands upon the property tax for revenue should be across the board, not on a piecemeal basis favoring one group at the expense of another.[57] While financial resources can be allocated to local govern-

54. *See* Letter from Texas Research League, *supra* note 18.

55. Using per capita amounts as the yardstick, Texas raises only $100.02 through the property tax, as compared with $150.54 for the Northeast and $167.22 for the West. California utilizes the property tax more intensively than any other state — at $199.56. BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, II CENSUS OF GOVERNMENTS: 1967, TAXABLE PROPERTY VALUES (1968) [hereinafter cited as TAXABLE PROPERTY VALUES].

56. The process of assignment of a rating to municipal bonds, which involves the concept of "overlapping debt," illustrates the interrelationship of local governments. For instance, municipal bond analysts adhere to a rule of thumb that "overlapping debt (debt incurred by various local governments covering the same property subject to taxation) should not exceed 10% of assessed valuation . . . ." A. RABINOWITZ, MUNICIPAL BOND FINANCE AND ADMINISTRATION 136 (1969). In view of this informally imposed ceiling, questions may be raised concerning how much of this limit each local government should be entitled to preempt from the others.

57. As property tax burdens increase, political pressure builds for tax exemptions. Church property is among the most important of the exemptions in Texas and in the United States. *See* M. LARSON, CHURCH WEALTH AND BUSINESS INCOME (1965). Particularly in recent years, legislatures throughout the country have granted increased exemptions to the elderly. *See* Yung-Ping Chen, *Present Status and Fiscal Significance of Property Tax Exemptions for the Aged,* 18 NAT'L TAX J. 162 (1965). In Wisconsin, the legislature has provided for a program of property tax relief for the poor through the use of tax credits. *See* Quindry & Cook, *Humanization of the Property Tax for Low Income Households,* 22 NAT'L TAX J. 357 (1969). For a penetrating argument against all nongovernmental property tax exemptions, *see* Bennett, *Real Property Tax Exemptions of Non-Profit Organizations,* 2 ASSESSORS J. 34 (1967).

On balance, tax exemptions for some only add to existing inequities. Rather than rewarding those who exercise political muscle in the legislature to gain an exemption at the expense of the remaining taxpayers, a more equitable approach would seem to seek fundamental changes in the use of the property tax. *See* notes 239–45 and accompanying text *infra.*

ments in a variety of ways, such a plan should not be based on the needs of the moment, but upon an awareness of the economic problems involved in using a given tax for a particular purpose. Analysis of the property tax in this context will follow a survey of methods by which the tax burden is apportioned among property owners.

II. TAX EQUITY AND THE ECONOMIC EFFECTS OF THE PROPERTY TAX

Although the property tax has historically been a major source of local revenue, it has theoretical and practical shortcomings that justify a careful examination of its economic effects.[58] Local reliance on the property tax has created inequitable taxing patterns and distortions in resource allocation. By studying the property tax in terms of incidence equity[59] and resource allocation, alternative models of state-local finance can be created that spread the tax burden more fairly and efficiently among the taxpaying population.

A. External Equity

"External equity," a traditional criterion for evaluating a tax, describes how fairly the property tax apportions the cost of governmental services among all taxpayers. It focuses upon the relationship of revenue sources to government expenditures and the relative benefit the taxpayer receives for his tax payment. The concept is grounded in a traditional tax benefit analysis[60] based upon the assumption that those deriving the ultimate benefit of a governmental service should pay for it. Since the component groups of today's society are so

58. This section is intended to give only a general overview of some of the economic effects of the property tax and to point out some of the tax's more serious flaws when used for the support of particular government services. This section is neither exhaustive nor definitive, but does present some of the major problems associated with the tax. Although many of these problems may well be mitigated by the thought reflected in the adage, "an old tax is a fair tax," many still remain. *See generally* Bridges, *Income Elasticity of the Property Tax Base,* 17 NAT'L TAX J. 253 (1964); Harriss, *Economic Evaluation of Real Property Taxes,* 28 PROCEEDINGS ACADEMY POL. SCI. 489 (1967); Rostvold, *Distribution of Property, Retail Sales, and Personal Income Tax Burdens in California: An Empirical Analysis of Inequity in Taxation,* 19 NAT'L TAX J. 38 (1966).

59. "Incidence equity" is a phrase selected to represent a broad evaluation of a particular tax in terms of its incidence; that is, who bears the final economic burden of the tax, and how fairly is the burden of a particular service distributed. *See* Hady, *The Incidence of the Personal Property Tax,* 15 NAT'L TAX J. 368 (1962); Oates, *The Effects of Property Taxes and Local Public Spending on Property Values,* 77 J. POL. ECON. 957 (1969); Sears, *Incidence Profiles of a Real Estate Tax and Earned Income Tax: A Study in the Formal, Differential Incidence of Selected Local Taxes,* 17 NAT'L TAX J. 340 (1964).

60. The benefits-received principle of taxation asserts that households and businesses should purchase the goods and services of government in basically the same manner in which other commodities are bought. C. MCCONNELL, ECONOMICS 150 (3d ed. 1966).

interrelated and the services performed by government so numerous, services supplied to one group of taxpayers often redound to the benefit of many others. Moreover, any of the services may "spillover" and may benefit persons outside the principal governmental jurisdiction that finances and supplies them. Even though it is obviously difficult to weigh and apportion the benefits of a variety of governmental functions among specific family or business units,[61] the approach is still useful.

Regardless of the spillovers and the inherent difficulty in isolating relative benefits, services can appropriately be classified as either private or social.[62] "Private services" are those that can readily be identified as primarily benefitting discrete businesses and family units — such as garbage collection and water and sewer service. Often the benefit is related to the consumer's use or ownership of property. These services more nearly approximate "proprietary"[63] services that could be performed by businesses. "Social services" are those that benefit the community as a whole — such as education, fire and police protection, and welfare. However, as with education, the immediate benefit of many social services may initially be conferred directly on identifiable individuals. Since the line between the two classifications is oftentimes blurred, the final classification may have to be arbitrary.[64]

The classification of the service as social or private should determine how that service is to be financed. Since social services benefit the community as a whole, they should be financed by broadly based taxes; private services should be supported by financing resembling user charges.[65] However, the spillover effect further complicates the

61. The real difficulty arises in the attempt to apportion on a benefit basis the cost of a social service that benefits the whole community. Such services should be supported by broadly based taxes instead of being funded on a benefit basis.

62. The terms "private" and "social" are utilized for the purposes of this study and may differ, in some respects, from other statements. *See, e.g.,* G. BREAK, INTERGOVERNMENTAL FISCAL RELATIONS IN THE UNITED STATES 63-64 (1967).

63. This classification is similar to the traditional tort distinction concerning exceptions to sovereign immunity. The critical point is that these services resemble other privately supplied business services. For example, both water service and garbage collection could be operated as regulated utilities, as electricity service often is. *See, e.g.,* Vickrey, *General and Specific Financing of Urban Services,* in PUBLIC EXPENDITURE DECISIONS IN THE URBAN COMMUNITY 62, 64-70 (H. Schaller ed. 1962).

64. One writer has classified a wide range of governmentally performed services as suitable for local, intermediate, or federal financing based on a combination of the social-private dichotomy and the spillover effect. Local services include, for example, fire protection, police protection, parks and recreation, public libraries, water distribution, and city streets. Intermediate services include air and water pollution control, water supply, parks and recreation, public libraries, sewage and refuse disposal, mass transit, arterial streets and intercity highways, airports, and urban planning and renewal. Federal services include education, parks and recreation, aid to low-income groups, communicable disease control, and research. G. BREAK, *supra* note 62, at 69.

65. User charges refer to payments made by the consumers of a service which are commensurate with the cost of providing them with the service. Payment for water is essentially suited to user charges because the benefit accrues to a discrete unit and can be quantitatively measured.

premise of "pay for what you get." Since spillover is a geographical concept, the optimal area-wide unit for provision of the service should be defined. Those services having the greatest spillover — education and welfare in all forms — should be supported by as large a governmental unit as possible.[66]

Examination of the budget of Fort Worth, Texas, illustrates an approach to the classification problem. For the purposes of this study, the municipally financed services will be limited to the following broad categories: public safety (fire and police protection), traffic engineering, public health, public works (including garbage collection), government administration, parks and recreation, water and sewage, library, and airport. Fort Worth finances these services by a variety of revenue sources, including the property tax, sales tax, user charges, and licenses.[67] It segregates its revenue into the following five earmarked funds: the general fund, the airport fund, the water and sewer fund, the parks and recreation fund, and the library fund. Fort Worth's segregation of the funds and the manner in which it finances each fund is at least suggestive of the aforementioned external equity concept and its classification system.[68]

Those services classified as private should be as nearly self-sufficient as practicable. Since the individual benefit can easily be quantified and identified with a specific user, water and sewer service is an especially good example of a private service capable of supporting itself through user charges. In fact, Fort Worth's water and sewage system is self-sufficient, even though it is the single most costly municipally provided service.[69] Similarly, airport facilities are fully financed by user charges with the result that those deriving the direct benefit of the service pay for it.

On the other hand, the library and parks and recreation funds receive substantial aid from the property tax.[70] However, almost one-fourth of the revenue for the parks and recreation fund is derived from user charges for recreational facilities.[71] Many of the largest

66. Ideally, the geographic bounds of a governmental unit providing a particular service should be coextensive with the spillover effects of the service. Such a structure limits payment for the service to those who receive the benefit. National defense, for example, benefits the entire country and should be financed nationally. The benefits of fire protection, on the other hand, are limited to a small geographic area and should be financed locally.

67. CITY OF FORT WORTH, *supra* note 34, at 2–3.

68. Although its classification system differs from the one proposed by this author, Fort Worth's attempt to make many services self-sufficient is consistent with the spirit of the suggested approach. *See* notes 200–38 and accompanying text *infra*.

69. CITY OF FORT WORTH, *supra* note 34, at 2, 8.

70. The parks and recreation fund received $1,728,382 of its $3,365,560 from the property tax. The library fund received $667,031 of its $1,359,781 from the property tax. *Id.* at 3.

71. User charges account for $701,350. *Id.*

recreation expenditures such as maintenance of golf courses, more than support themselves.[72] Again, this activity is particularly susceptible to user charges because the recipient of the benefit is easily identified and because relatively few members of the community use it.

The Fort Worth general fund supports public safety, traffic engineering, public works, and government administration. Most of these services more nearly fall into the social service category.[73] The property tax is responsible for nearly one-half of the revenues constituting the general fund.[74]

B. Internal Equity

"Internal equity" describes how fairly the property tax is apportioned among the members of the class intended to pay it. It focuses upon the ability of the one making the initial payment to shift the ultimate tax burden away from himself.

1. Incidence

Initial property tax payments come from two basic groups, businessmen and homeowners. Businesses typically possess the ability to pass the tax forward to consumers or backward to factors of production, thereby effectively avoiding the tax. Homeowners, on the other hand, must absorb the tax themselves. This ability of some businesses to pass the cost on may very well be determinative of the kinds and quality of services a local government can provide. Consideration of a few hypothetical cases may illustrate the manner in which businesses shift the tax and the likelihood of a particular locality having quality education or any other social service financed by the property tax. Concentrating on the effect of supporting education through the property tax is especially appropriate because education consumes the greatest share of local property taxes.[75]

a. Shifting of the Property Tax Burden

Forward shifting generally occurs where a school district has a firm within its jurisdiction which possesses a substantial degree of market power. Since the firm has at least a limited power to raise prices, an increase in property taxes within that district alone will be

72. Golf courses produce $540,000 in revenue and cost $356,708 to operate. *Id.* at 9, 26.

73. Public safety services also have a private aspect because they benefit individuals through the property they own or occupy.

74. The general fund totals $40,354,390, of which $19,143,685 comes from the property tax. CITY OF FORT WORTH, *supra* note 34, at 2.

75. *See* text accompanying note 18 *supra*.

reflected in a price increase. As long as the firm has market power vis-à-vis its competitors, it will not suffer a significant adverse effect from a unilateral increase in its costs. The real cost of providing the governmental service — education — will be passed on to the firm's consumers. Moreover, these customers will very often reside outside the school district.[76] For example, if the firm happens to be an oil or natural gas company, it will export the tax to consumers throughout the country who will bear the cost of that district's education.[77] Simply because of happenstance, a school district with a "golden" industry is able to provide its children with exceptional educational opportunity with little sacrifice, while a neighboring school district without similar good fortune struggles to provide even minimal educational opportunity.

Andrews County, Texas, is an example of the wealthy district. Per capita expenditures are among the highest in the state,[78] whereas the effective valuation rate is among the lowest.[79] Utilizing a relatively low percentage of true market value for tax assessment, Andrews County provides amazingly high levels of school service. Andrews can accomplish this because it actually sits on an oil field. Moreover, the largest taxpayers in the county, oil companies,[80] seem willing to pay a relatively high, absolute amount of property taxes in order to retain the good will of the community and to attract qualified workers by offering exceptional educational facilities for their children.

Backward shifting occurs where an industry is without power to raise prices and, in order to meet the additional expense of a tax increase, is forced to reduce its costs.[81] Workers may be willing to accept lower wages to retain their jobs, or the firm may be able to reduce overhead in some other fashion. If these events occur, the tax has been shifted backward. Rather than risk the loss of business and the concurrent diminution of tax base and jobs, local districts with comparatively weak businesses may refrain from increasing taxes and thus be unable to finance quality education. Such a situation is especially likely if the district also has poorer residential areas.

76. C. MCCONNELL, *supra* note 60, at 412–15. Demand elasticity is basic to the concept of market power. To have substantial control over price, the firm must sell a product whose demand is relatively constant regardless of price increases, *i.e.*, usually a "necessary" with few close substitutes. *Id.*

77. CABINET TASK FORCE ON OIL IMPORT CONTROL, THE OIL IMPORT QUESTION: A REPORT ON THE RELATIONSHIP OF OIL IMPORTS TO THE NATIONAL SECURITY § 207c (1970).

78. TEA REPORT, *supra* note 24, at 4.

79. C. BARTLETT, *supra* note 24, at App. C.

80. Over 70 per cent of the taxable property in Andrews County is oil and gas. TAXABLE PROPERTY VALUES, *supra* note 55, at 142.

81. C. MCCONNELL, *supra* note 60, at 584.

b. Residential Districts

A district composed primarily of residential areas will itself bear the cost of education. Owner-occupants of residential housing simply lack the ability to shift the tax. However, owners of rental housing more nearly approximate owners of businesses. If the demand for rental housing is relatively inelastic with respect to increases in rent, the tax can easily be passed along. But, if demand for housing declines faster than price increases, the owner must absorb the tax or risk further shrinkage of his market.

If the local district is fortunate enough to be composed of relatively wealthy residential areas, it will probably have good schools. Often the wealthier residential districts have better schools with higher per capita expenditures than poorer districts and at lower effective tax rates.[82] To reiterate, the quality of education is often determined not by the willingness of local residents to make economic sacrifices through higher tax rates, but by relative wealth.

2. Education and Local Support by the Property Tax

Since education is a social service with significant spillover and because it is important to creating real equality of opportunity, most would agree that it should be made available to all children impartially. However, great disparities in local expenditures do exist, and, instead of educational need, the amount of expenditures for education often turns on the economic composition of the local district. Those districts having wealthy residential areas or prosperous industries capable of exporting the tax possess the potential to have quality education; those districts with little or no industry and poor residential areas do not. Since education is such an important social service with substantial spillover, it is submitted that it demands greater state participation and less reliance on the local property tax, even when used only as a supplementary or enrichment device. The property tax seriously violates the internal equity concept because it can be shifted easily in many situations.

C. Regressivity

An important consideration in evaluating any tax in terms of equity is its regressivity. The property tax has been described as the "most important regressive element in the tax structure,"[83] and its

82. *See* note 24 *supra.*

83. TAX FOUNDATION, INC., TAX BURDENS AND BENEFITS OF GOVERNMENTAL EXPENDITURES BY INCOME CLASS, 1961 AND 1965, at 16 (1967). This regressive

regressivity described as being "probably greater than that for any other major tax."[84] When the property tax is used as a source of general revenue and not as a form of user charge, it finances a range of social services that should be supported by broad based taxes levied on an ability to pay formula. Instead of taxing more heavily the relatively wealthy, the property tax falls hardest on lower income groups. However, this regressivity is mitigated by patterns of governmental expenditures. Expenditures such as public housing and welfare, often financed by local property taxes, confer the greatest benefits on poorer groups. One commentator has concluded that "[i]n all cases the impact [of the tax] is markedly progressive: the benefits are substantially larger percentages of the income of lower groups than of higher income groups."[85]

D. Resource Allocation

Neutrality, another traditional criterion for evaluating a tax, describes how the tax affects resource allocation. Ideally, after imposition of the tax, the pattern of allocation should be substantially similar to the pre-tax spending pattern. Two separate considerations emerge as significant subdivisions of this broader concept of neutrality. The first is the effect of the property tax on resource allocation in general, and the second is its effect on locational decisions of businesses.

1. General Effects

On a theoretical level, an unshifted property tax tends to increase the cost of capital by nearly the full extent of the levy and to stimulate a set of adjustments until a new equilibrium is reached. For example, a four per cent tax on half the economy's assets is eventually translated into a two per cent tax on all assets. The cost of the taxed assets has increased so that their return (interest rate) falls to offset the tax. Investment then gravitates to untaxed areas bidding their prices up, until a new equilibrium is reached. The "extra-market" cost of the property tax has altered investment decisions and the pattern of resource allocation. To the degree expenditures move to the untaxed assets, the neutrality principle is violated.[86]

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aspect of the property tax has increased political pressure for tax relief for certain low-income groups. *See* note 57 *supra.*

84. D. NETZER, ECONOMICS OF THE PROPERTY TAX 59 (1966).

85. *Id.* at 60.

86. This generalized analysis of the property tax's effect on resource allocation traces the broad outlines of that presented by Professor Procter Thomson. Thomson, *The Property Tax and the Rate of Interest,* in G. BENSON, THE AMERICAN PROPERTY TAX: ITS HISTORY, ADMINISTRATION, AND ECONOMIC IMPACT (1965).

The property tax should be criticized only if it results in more serious distortions than alternative taxes. However, either a proportional income tax or a consumption tax, both broader based taxes, should produce less distortion. Professor Thomsen estimates that in 1964, to yield revenue of $92.6 billion, the income tax rate would have been 20 per cent, the sales tax rate 22 per cent, and the property tax rate 60–80 per cent.[87] Since the property tax has the narrowest base, it results in greater allocative distortions. Expenditure patterns will be more drastically altered if a relatively few items become much more expensive than if all items become slightly more expensive. Since the property tax has a narrower base and greater distortive effects, it is an inferior source of revenue from the standpoint of neutrality when compared to an income or sales tax.

A corollary to the problem of the scope of the tax base is the more concrete proposition that the property tax is unneutral because it does not fall equally on all industries. Since property tax rates are typically higher for realty than personalty[88] and since human capital is untaxed, labor-intensive industries become relatively more profitable when compared to manufacturing, agriculture, and mining. However, it is probable that higher payrolls, with their payroll taxes, and the higher productivity of capital, offset the property tax advantage reaped by labor-intensive industries.

Even though inter-industry distortions can be mitigated by productivity increases of capital, intra-industry distortions still persist. One commentator has noted the occurrence of this phenomenon within the transportation industry. In 1957, the inherently capital-intensive railroads paid 3.4 per cent of operating revenue in property taxes, while motor carriers paid only 0.4 per cent and air carriers only 0.2 per cent.[89] The property tax appears to have hastened the decline of the railroads' competitive position.

2. *Locational Effects*

Since World War II, many states have actively pursued tax policies designed to attract new industries with additional jobs.[90] Property

87. *Id.* at 124. This assumes that the various taxes are the sole source of revenue and are computed by determining the necessary rate to be applied to a set base — all income, all sales, or all assessed property.

88. *See* D. NETZER, *supra* note 84, at 140–55.

89. *Id.* at 73.

90. Whether or not the new industries actually increase the tax base is questionable. The tax concessions may more than offset the additional valuations. *See* Ross, *Louisiana's Industrial Tax Exemption Program,* 15 LA. BUS. BULL. 46 (1953). *See also* Stober & Falk, *Property Tax Exemption: An Inefficient Subsidy to Industry,* 20 NAT'L TAX J. 386 (1967).

tax exemptions have played a major role in this intergovernmental warfare because of the preëminent position of the tax in local government finance.[91] These exemptions have taken both legislative and administrative forms. Thirteen states[92] specifically authorize local governments to exempt certain "new" industries from local property taxes for a specified period of years. Several states, including Texas,[93] have enacted "freeport" laws exempting business inventories intended for out-of-state sale from taxation. In less formal ways, local governments have sought new industry by negotiating administrative "understandings" to undervalue a business' tax base.[94]

a. Regional Decisions

The nature and economic position of a particular industry shape its view of the importance of tax concessions in its choice of location. Obviously, property tax rates will bear most heavily on capital-intensive industries. Since a local firm in vigorous national or regional competition cannot unilaterally raise prices and pass the tax forward, differential rates play a larger role in its decision than in those of national industries with market power. The result is that, over time, the competitive local industry will feel increasing pressure to relocate or to expand where the tax climate is more favorable. Even though state and local taxes represent a relatively small portion of business costs, differentials may well be determinative of locations at the margin.

Choices among regions will most likely depend on factors such as access to resources, quality and composition of the labor supply, and the local level of public services. The results of one survey[95] ranked the following considerations ahead of state-local tax concessions: community attitude toward industry, good employer-employee relations, productivity of workers, political calm and stability, and educational

91. Although Texas does not permit its localities to use industrial tax bonds, the utilization of this form of property tax subsidy to industry, as it occurs in other states, offers valuable lessons concerning the effects of property tax subsidies to industry. Certain states permit localities to issue general obligation bonds to purchase industrial facilities which are then leased to private firms in order to attract industry to their areas. *See* A. RABINOWITZ, *supra* note 56, at 101–16. Competition among localities in offering this form of subsidy often leads, however, to a misallocation of resources, both in terms of location of industry and preservation of the integrity of local tax bases. *See* ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS, INDUSTRIAL DEVELOPMENT BOND FINANCING (1963) [hereinafter cited as BOND FINANCING].

92. For a collection of these exemption statutes, *see* ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS, STATE-LOCAL TAXATION AND INDUSTRIAL LOCATION 109–10 (1967) [hereinafter cited as STATE-LOCAL TAXATION].

93. TEX. REV. CIV. STAT. ANN. art. 7150f (Supp. 1972).

94. "While the extent of this 'bargaining table' approach to property tax assessment cannot be documented, its existence cannot be denied." STATE-LOCAL TAXATION, *supra* note 92, at 48. No doubt, local assessors are reluctant to admit publicly intentional underassessment.

95. *Id.* at 74–76.

opportunity. Another study[96] ranked labor relations and extent of unionization ahead of tax concessions. Undoubtedly, these other factors are most important in comparing one region to another where relative conditions may differ substantially. But when the choice is narrowed to urban or suburban sites in the same area, the property tax assumes a larger role.

b. Urban-Suburban Decisions

When the locational choice is between urban and suburban sites, the cities tend to lose because of their higher property tax rates and because other cost factors tend to become constant. Although the migration to the suburbs by businesses and homeowners results from many forces, the property tax probably reinforces the trend.[97] Whatever the reasons, as businesses and homeowners make the move, central cities lose their tax base. The declining base, coupled with the increasing demand for public services for the lower income groups remaining in the core of the urban centers, drives rates up.

Fiscal warfare among locally competing jurisdictions has reinforced the forces encouraging moves to the suburbs. The results of the moves are economic dislocations, high effective tax rates, and a mismatching of needs and resources. One commentator has succinctly described the potential for misallocation:

> To the extent that firms are influenced by tax factors, a species of Gresham's Law operates: these firms will tend to gravitate to low tax cost areas. If these low taxes arise from actual economies in the provision of public services, the tax factor reflects a real economic factor and its influence does not distort location from the sites which are most economic. But if this is not the case, tax influences do exercise an undesirable influence by leading firms to locate in places other than those which involve maximum efficiency in the use of resources.[98]

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96. For a summary of the findings of a 1963 study conducted by the Bureau of Business Research, University of South Carolina, *see* Alyea, *Property Tax Inducements to Attract Industry,* in PROPERTY TAXATION USA 139, 150 (R. Lindholm ed. 1969).

97. The forces making for decentralization are so potent that it can be confidently asserted that the tide would not have been stemmed even had there been large property tax differentials in favor of the central cities. In fact, the decentralization process seems to have proceeded no less rapidly in those few areas in which the central city does appear to have an advantage in effective tax rates. Nevertheless, if tax differentials against the central city are widening, which is a distinct possibility at the present time, the likelihood increases that local fiscal arrangements will have an un-neutral locational effect: that businesses and residents who might otherwise have preferred a central city location will choose instead a location in outer portions of the metropolitan areas.
D. NETZER, *supra* note 84, at 123.

98. Due, *Studies of State-Local Tax Influences on Location of Industry,* 14 NAT'L TAX J. 163 (1961).

Although the general distortive effects are hard to document, mismatching of the need for governmental services with potential revenue is more apparent. The central cities, with the greatest need for revenue to meet the needs of the urban poor, lack an adequate tax base. Moreover, the more wealthy suburbs, who least need quality services, finance better services at lower effective rates.[99]

E. An Example

Even though many of the economic effects described in this section are theoretical and difficult to prove, the most serious evil can be easily illustrated. That evil is the inherent propensity to separate needs from resources by reliance on the local property tax to finance those social services with significant spillover, such as education, welfare, public housing, and health. This mismatching is most severe in large urban centers.

1. The Rich District

Ector County, Texas, exemplifies the school district having the ability to provide a high level of educational service with relatively little tax effort by its residents. It spends annually $543 per pupil,[100] seventh among the thirty-nine comparably sized districts within the state. The average expenditure for all districts is $504,[101] and for Ector's group, $469.[102] Ector's expenditures are misleading, however, when compared to the statewide average because larger school districts reach certain economies of scale which return more service per dollar; of the twelve size classifications created by the Texas Education Agency, Ector falls with the second largest,[103] and thus is capable of taking advantage of such economies.

The distribution of property classifications within Ector's tax base is as follows: commercial and industrial, 5.9 per cent; single family houses, 18.8 per cent; and "others," 72.0 per cent.[104] The "other" category represents primarily oil and gas valuations. The various rates imposed on each of the categories are the following:

99. Netzer presents data indicating the greater ability of wealthy suburbs to finance services. Moreover, "richer communities in property value terms can indulge their tastes for more and better public goods at lower, not higher, tax rates since tax rates decline rapidly as property values rise." D. NETZER, *supra* note 84, at 126.

100. TEA REPORT, *supra* note 24, at 2.

101. *Id.* at 1.

102. *Id.* at 13.

103. Ector County is coextensive with the independent school district. It has 23,034 students placing it in Group II, the 10,000–49,999 average daily attendance group. *Id.* at 1.

104. TAXABLE PROPERTY VALUES, *supra* note 55, at 142.

residences, 24 per cent; oil and gas, 35 per cent; and commercial, 31 per cent.[105] A few important conclusions emerge from examination of these figures. First, the bulk of the school support comes from the "other" category — oil and gas assessments. Besides being by far the largest component of the tax base, oil and gas is assessed at the highest rate. Secondly, residences, a relatively small portion of the total tax base, are assessed at the lowest rate. The residents have avoided the full impact of the tax due to the presence of the oil companies.

The frequently quoted and usually self-serving justification offered for maintaining local support of education through the property tax is the importance of local autonomy, with its corollary that those districts which really value education will choose high tax rates. But the 30 per cent actual assessment ratio[106] of Ector belies the real burden borne by the immediate users of education, resident property owners.[107] The residents are not making an economic sacrifice to provide good schools; they are relying on the oil companies to do it for them.

The real cost of education is being exported from Ector via sales of oil and natural gas. Just as consumers of Detroit-made automobiles pay a portion of General Motors' local property taxes, non-Texas consumers of petroleum products pay the oil companies' taxes. To the extent that property taxes exceed the cost of supplying business-related services, such as fire and police protection and water and sewerage service, non-local consumers subsidize local governments. The result is a series of hidden transfer payments that make it virtually impossible to find where the real tax burden lies.

Should a locality be blessed with a "golden" industry, it has the potential to tax that industry to the brink of its competitive position. The locality's position is even more appealing if the industry is a captive one,[108] such as oil or lumbering that cannot relocate. If such local districts were responsible for providing public housing, health, and welfare services, they might well be able to build high rise public housing and provide the members of the community with early retire-

105. C. BARTLETT, *supra* note 24, at App. C.

106. *Id.*

107. "Resident" property owners in this context refers to owners of residential property. Such property owners actually receive a double benefit in the sense that many of these residential families will send their own children to school and will pay no more than a fraction of the cost of their less fortunate counterparts in districts not blessed with the presence of oil companies.

108. In the case of Ector County, since the tax base is largely composed of a non-movable asset such as oil, the businesses paying the tax bill cannot easily threaten to relocate, as other "golden" industries might, in order to hold taxes down. Rather, these companies must pay the designated rate, whether excessive or not, constrained only by whatever political pressures can be brought to bear on local authorities.

ments, all at the expense of the oil companies and, ultimately, their consumers.

2. *The Poor District*

The Mesquite school district's ability to support education is in marked contrast to that of the rich district. Mesquite falls within the same student population group as Ector and should encounter similar economies of scale for its expenditures. Although the exact composition of Mesquite's tax base is not known because such figures are reported only for the county unit, its tax assessment ratios speak for themselves. Mesquite's actual ratio is 78 per cent compared to Ector's 30 per cent.[109] Commercial and industrial property is assessed at 56 per cent of true market value; business personalty at 60 per cent; and residences at 81 per cent.[110] Despite these high rates, Mesquite spends only $373 per pupil, approximately 68 per cent of what Ector spends and almost $100 below the average for its group.[111] Mesquite apparently lacks rich oil and gas properties and other suitable industries to finance its education so that the burden is left to local homeowners.[112]

Reliance on the property tax to finance education predestines Mesquite's school children to inferior educational opportunity as compared to students in Ector. The local effort justification is particularly unpersuasive in this kind of situation since Ector achieves higher per capita expenditures with lower actual assessment ratios. Here, as in many cases, neither need nor local effort determines the quality of the governmental services; instead, the criteria are wealth and chance. The property tax is justifiable as a source of local revenue when it is limited to the financing of those services that tend to benefit individuals through their use of property. But, it cannot be justified as a source of general revenue to finance social services with significant spillover. It results in a mismatching of needs to resources and permits the beneficiaries of services to shift payment to others.

III. DEVELOPING LEGAL APPROACHES AND THEIR CONSEQUENCES

To this point, this Article has shown that reliance on the local property tax to support services leads to an inevitable mismatching

109. TEA REPORT, *supra* note 24, at 5.
110. *Id.*
111. *Id.*
112. Mesquite's only opportunity to increase revenue substantially is to attract industry; yet to attract industry, Mesquite probably must reduce taxes and suffer a decline in already underfinanced services. Under present conditions, then, Mesquite, as well as other cities and school districts in the same predicament, must simply suffer with the problem.

of needs and resources. Therefore, it is necessary to examine next the context in which this problem of the mismatching has arisen and how the action taken by the courts has affected it.

A. Attempts to Deal with the Problem of Disparities

Disparities in local and state services due to the mismatching of needs and resources have been the subject of three important recent cases: *Serrano v. Priest,*[113] *Rodriguez v. San Antonio Independent School District,*[114] and *Hawkins v. Town of Shaw.*[115] In each of these cases the courts addressed the disparities in governmental services; each dealt with taxing patterns only indirectly. *Serrano* and *Rodriguez* raise the problem of disparities in expenditures among residents of the whole state, whereas *Shaw* concerns disparities among residents of a single town.

In *Serrano,* plaintiffs' basic contention was that their children were being denied equal protection of the laws because the method of financing public education used by California inevitably resulted in lower per pupil expenditures in those areas populated by the poor.[116] Reliance upon the local property tax, plaintiffs claimed, constituted an invidious discrimination in the provision of a fundamental service based on classification by wealth. They were able to show substantial disparities in per student expenditures with higher amounts being spent in those areas with higher assessed valuations — generally, those areas where the relatively wealthy lived.[117]

The California Supreme Court was receptive to plaintiffs' attempts to construct their argument within the framework of established equal protection doctrine. Since the court purported to decide the case on both fourteenth amendment and parallel state constitutional grounds, it began by classifying the nature of the child's interest in education. Unable to find direct authority for the proposition that education is a fundamental interest, the court, nevertheless, concluded that education is such an interest, thus requiring application of the "compelling state interest" standard of equal protection.[118] The court concluded that

113. 5 Cal. 3d 584, 487 P.2d 1241, 96 Cal. Rptr. 601 (1971).
114. 337 F. Supp. 280 (W.D. Tex. 1972), *rev'd,* 93 S. Ct. 1278 (1973).
115. 437 F.2d 1286 (5th Cir. 1971).
116. 5 Cal. 3d at 589–91, 487 P.2d at 1244–45, 96 Cal. Rptr. at 604–05.
117. *Id.* at 612, 487 P.2d at 1260, 96 Cal. Rptr. at 620.
118. Although Brown v. Board of Educ., 347 U.S. 483 (1954), was not held to be controlling on the issue of whether or not public education is a fundamental interest, the *Serrano* court quoted approvingly from the Supreme Court's description of the importance of education. In *Brown,* the Court declared:

> Today, education is perhaps the most important function of state and local governments. Compulsory school attendance laws and the great expenditures for education both demonstrate our recognition of the importance of education to our democratic society. It is required in the performance of our most basic public respon-

education is so vital to an individual's chance to be socially and economically successful that it must be considered fundamental.[119] Neither the alleged need for local control and autonomy in school operation nor its corollary, the need for local finance, was found to be such a compelling state interest as to justify the disparities. The court, therefore, found the financing system unconstiutional as a denial of equal protection.

The lower court in *Rodriguez* followed the lead of the California Supreme Court and found the Texas method of financing education in violation of the equal protection clause of the fourteenth amendment.[120] Plaintiffs' contentions were essentially the same as those made in *Serrano* — that the quality of education that the child received was a function of the wealth of his parents and of the school district in which he resided. The *Rodriguez* plaintiffs also were able to show substantial disparities in per pupil expenditures among school districts.[121] Applying the compelling state interest standard, because it likewise found education to be a fundamental interest, the three-judge federal court held that the quality of public education may not be a function of wealth, other than the wealth of the state as a whole.[122]

The *Shaw* case presents a different problem. Shaw, Mississippi, was a small town composed of approximately 1500 whites and 1000 Negroes. Plaintiffs, Negro citizens of Shaw, alleged racial discrimination in the provision of municipal services violative of the equal protection clause of the fourteenth amendment. They indicated that the predominantly white areas had better sewage systems, better fire hydrants, better street lighting, more paved streets, and better water service than the predominantly Negro areas. The majority of these services were financed from general revenues.[123] In reversing the district court, the Fifth Circuit declared that the proper standard for

> sibilities, even service in the armed forces. It is the very foundation of good citizenship. Today it is a principal instrument in awakening the child to cultural values, in preparing him for later professional training, and in helping him to adjust normally to his environment. In these days, it is doubtful that any child may reasonably be expected to succeed in life if he is denied the opportunity to an education. Such an opportunity, where the state has undertaken to provide it, it is a right which must be made available to all on equal terms.

Id. at 493. By relying upon the United States Supreme Court's finding, the California Supreme Court reveals the methodology of the fundamental interest test. Theoretically, as a result, any state provided or state-authorized service that is sufficiently "important" either to individuals or to society may be found to be a fundamental interest.

119. 5 Cal. 3d at 609–11, 487 P.2d at 1258–59, 96 Cal. Rptr. at 618–19. *But see* C. JENCKS, INEQUALITY: A REASSESSMENT OF THE EFFECT OF FAMILY AND SCHOOLING IN AMERICA (1972).

120. 337 F. Supp. at 284.

121. *Id.* at 282.

122. *Id.* at 286.

123. 437 F.2d at 1294 (concurring opinion).

testing the classification was that of compelling state interest, rather than the traditional rational basis test, because the classification was prima facie based on racial discrimination.[124] The Fifth Circuit rejected defendant's claims that the disparities resulted from compelling nonracial factors, such as commercial need in the paving of streets, and directed the town to submit a plan to correct the inequities within a reasonable time.[125]

1. *The* Serrano-Rodriguez *Problem*

Serrano held that "the right to education in our public schools is a fundamental interest which cannot be conditioned on wealth."[126] Similarly, the three-judge panel in *Rodriguez* held that the state must adopt a program that does not "make the quality of public education a function of wealth other than the wealth of the state as a whole."[127] Even though the Supreme Court has rejected this approach,[128] this fact pattern offers a useful illustration of the problem of eliminating service disparities that arise from wealth differentials in the local property tax base. Before examining the available alternatives, it is to be assumed that equality of educational opportunity does not require equal per pupil expenditures among school districts, but does require equal access to financial resources among a state's school districts, independently of the wealth of any particular locality.

As indicated previously, there are three patterns of adjusting intergovernmental financial relationships: social equity, incentive matching, and political economy.[129] Although virtually all states utilize programs falling within one or more of these categories in an attempt to ameliorate imbalances in the local wealth of their subdivisions, these efforts continue to leave wide variations in per pupil expenditures.[130] Since the incentive matching approach is not designed to alleviate interdistrict wealth disparities,[131] there is little point in evaluating its suitability for financing public schools. At the same time, there can be no question that interdistrict wealth disparities would be alleviated by the social equity approach, under which the state would determine "the level of performance or the money outlay per unit of need with

124. *Id.* at 1288.
125. *Id.* at 1293.
126. 5 Cal. 3d at 590, 487 P.2d at 1244, 96 Cal. Rptr. at 604.
127. 337 F. Supp. at 284.
128. San Antonio Independent School Dist. v. Rodriguez, 93 S. Ct. 1278 (1973).
129. *See* text accompanying notes 26–27 *supra.*
130. *See* text accompanying notes 100–12 *supra.*
131. D. MORGAN & F. HAYDEN, *supra* note 27, at 25–35.

performance or outlay both equalized among the districts."[132] Simply stated, the state would function as a single school district for the limited purpose of collecting and dispensing revenue; yet, it could continue to delegate to local districts many of the same functions now performed by these districts. A critical but unanswered question revolves around whether the political economy approach — which requires "equalization by the state of fiscal potential among the constituent school districts, with district determination of outlay per unit of need"[133] — can eliminate interdistrict wealth differentials as the determining factor in the relative availability of services. In other words, through the use of one of several tax redistribution formalae, the state would equalize the revenue-raising potential of all of its districts, thereby making educational expenditures a function of local tax effort. Under this approach, each district would, to a greater or lesser degree, be left free to decide for itself how much it wants to spend on education.

An analysis of the political economy approach and its variants must focus on whether, if utilized, it is possible to achieve "fiscal neutrality"[134] — the elimination of district wealth as a factor in the availability of resources for education. Although many different proposals[135] concerning use of local sales and income taxes are being suggested, these alternatives mark a step forward only in that more broadly based taxes are used to finance a social service with extralocal impact. Use of these tax bases, even with equalization factors, will not necessarily dissolve interdistrict wealth disparities as determinants of the quality of local education. No attempt will be made here to discuss these alternatives as replacements for the local property tax because they presently play only a marginal role in educational finance, and no significant move in their direction appears likely. Instead, analysis of two basic patterns of application of the political economy theory will serve as the basis for evaluating the possibility of divorcing the local property tax from district wealth differentials.

First, local districts could be redrawn in such a way as to equalize the ratio of average daily attendance to property tax base, while leaving

132. *Id.* at 12.

133. *Id.*

134. Rodriguez v. San Antonio Independent School Dist., 337 F. Supp. 280, 284 (W.D. Tex. 1972).

135. For a thorough discussion of the potential use of tax bases other than the property tax in local government finance, *see* Due, *Alternative Tax Sources for Education,* in ECONOMIC FACTORS AFFECTING THE FINANCING OF EDUCATION 291–328 (R. Johns ed. 1970). *See also* SIGNIFICANT FEATURES, *supra* note 4, at 68; Schaefer, *Sales Tax Regressivity Under Alternative Tax Bases and Income Concepts,* 22 NAT'L TAX J. 516 (1969).

the present administrative districts intact. Theoretically then, for a given tax rate, the same revenue would be available for all taxing regions and districts. This approach, nonetheless, would not eliminate wealth factors from denying all districts equal access to financial resources. Even though the equalized tax bases would be numerically equal, they would not necessarily possess the same taxpaying ability. So long as taxpaying ability, a function of economic wealth, is unequal, so also will be the services dependent on it. Although numerically in parity, the composition of these various equalized tax bases will result in varying degrees of tax strain among the individual regions.[136]

As previously noted, the ease of paying the property tax cannot be accurately measured because of existing methods of assessment.[137] For example, businesses, which constitute a large share of the property tax base, do not all earn the same return on capital. Some have a measure of market power and are able to shift the tax forward and export it from the jurisdiction; others are unable to shift it. Obviously, the tax burden for those who cannot shift it will be much heavier. The impossibility of identifying those businesses and the fact that they can not be equitably distributed among taxing regions point to the futility of this method. Moreover, other factors contribute to this futility. Although, in the abstract, education is a social service which benefits all of society, some perceive more immediate benefits than others and arrange their financial decisions accordingly. For example, at an elemental level, retired citizens and childless couples owning considerable realty are not as likely to be interested in quality education supported by a property tax as poor families owning little real estate with many school-age children. Depending upon the incidence of these groups within a given taxing region, economic judgments related

136. "Tax strain" as used herein is a different concept from "tax effort." A recent revenue-sharing bill, H.R. 11950, 92d Cong., 2d Sess. § 104 (1972), illustrates one method of computing tax effort. Under that proposed formula, a state's tax effort would be determined by dividing total state and local revenue by total personal income.

Tax strain, however, is broader and encompasses tax effort, tax incidence (whether the tax is shifted forward or backward), and marginal utility (taxpayer perceptions of the benefits of governmental programs in exchange for loss of income available to purchase private goods). High tax effort, as a result, may or may not indicate intense tax strain. It is the elusive nature of tax strain as a working concept and the inadequacy of tax effort as a realistic means of measuring taxpaying ability among various political subdivisions that point to the futility of achieving "fiscal neutrality" through tax equalization schemes. Since tax strain cannot be quantified, if all political subdivisions of a state are to have equal access to financial resources, the state must provide the financing itself. For a comprehensive analysis of taxpayer-invoked constraints on certain public expenditures based on similar considerations of intense tax strain, *see* Buchanan, *Taxpayer Constraints on Financing Education*, in ECONOMIC FACTORS AFFECTING THE FINANCING OF EDUCATION 265 (R. Johns ed. 1970).

137. Since all capital does not yield the same return, relative property values, or the amount of capital involved in a particular business, bears little relationship to taxpaying ability of one business as compared with another. *See* text accompanying notes 76–81 *supra*.

to relative wealth and taxpaying ability will continue to create disparities in the level of education among different geographic areas of the state.

A second method of effecting equality of access to financial resources for education in all districts via the political economy approach is quite appealing, but no more helpful in eliminating wealth factors. In their original article on this subject, Clune, Coons, and Sugarman suggested "power equalization" as a device for making the local quality of education a function of tax effort, not wealth.[138] Tax effort and wealth, however, are inseparable concepts. A simple illustration will show the mechanics of power equalization which equalizes tax effort.[139] The example posits two equally populated school districts, composed only of residential property. In District *A*, homes average $15,000 and incomes $7500 per family; in District *B*, homes average $30,000 and incomes $15,000 per family. A tax levied at a rate of twenty mills will give each district $450 per unit of average daily attendance. At this point each district enjoys equal expenditures per unit through a power-equalized proportional tax. But since power equalization permits each district to decide for itself how much education it wants, any resulting disparities must be scrutinized to determine whether they are functions of wealth.

THE WEAKNESS OF THE POWER EQUALIZATION MODEL

	District *A*		District *B*
	(figures in dollars)		
Average Income	7,500		15,000
Average Property Values	15,000		30,000
Tax at 20 Mills	300		600
Power Equalization Factor		$\frac{300 + 600}{2}$	
Power Equalized Unit Expenditure for Each District	450		450
After Tax Average Disposable Income	7,200		14,400
Tax at 30 Mills	450		900
Power Equalized Unit Expenditure for Each District	675		675
After Tax Average Disposable Income	7,050		14,100
Cost of Increased Expenditure over Initial 20-Mill Levy	150 for 225		300 for 225

138. Coons, Clune & Sugarman, *Educational Opportunity: A Workable Constitutional Test for State Financial Structures*, 57 CALIF. L. REV. 305 (1969).

139. *See* Table, at 558.

Economic factors indicate that District *A* is likely to spend less than District *B* per unit of educational benefit. If each decides to increase its taxes from twenty to thirty mills, each can spend $675 per average daily attendance unit. To do so, however, families in *A* must reduce their disposable income by $150 to $7050, and families in *B* must reduce theirs from $14,400 to $14,100. In other words, families in *A* are buying $225 in increased expenditures per unit for $150, while families in *B* are buying the same increase for $300. However, in terms of real sacrifice, every dollar taken from the poorer families in District *A* "hurts" much more than each dollar taken from families in District *B*, since a proportional tax falls more heavily on the poor than the relatively more wealthy.[140]

What originally seemed to motivate court action in California and Texas was not so much interdistrict tax disparities as interdistrict service disparities arising from wealth variations. Although power equalization attempts to neutralize variations in district wealth, it only reduces wealth as a contributing factor. Therefore, even if the Supreme Court had affirmed *Rodriguez,* a literal reading of "fiscal neutrality" would disallow differentials in local spending based upon variations in local desires because such desires for education would inevitably be influenced by the relative wealth of each district.

To remove wealth from the equation for providing social services equally to all residents within a state, some variation of the social equity approach must be employed. Although it is not within the scope of this Article to discuss what effect such an approach will have on traditional concepts of local control over education, or any other service, it is likely that such a program would have much less impact than imagined.[141] While wealthy school districts might well face reduced

140. So long as local choice concerning definition of unit need is permitted, wealth variations will affect the amount of economic resources available for a given service. Taxpayer constraints will inevitably create service disparities as the tax ceiling in each district is met. *See* Buchanan, *supra* note 136, at 267–71. In other words, the taxpayers, as a corporate body, will perceive either more or less utility from a given service at the margin. Since a priori judgments of marginal utility for a given service cannot be quantified for individuals — much less political subdivisions — varying degrees of wealth will always result in service disparities regardless of power equalization.

141. Loss of significant local control of services financed by means of the social equity approach, in which the state determines need and provides all economic resources, is by no means inevitable. Various devices do exist for preserving maximum local policy control and administrative flexibility. *See* Address by Governor Milliken, *supra* note 32; *Hearings Before the Select Comm. on Equal Educational Opportunity of the United States Senate,* 92d Cong., 1st Sess. 6862 (1971) (remarks of Professor Yudof). *Contra,* Brazer, *Federal, State, and Local Responsibility for Financing Education,* in ECONOMIC FACTORS AFFECTING THE FINANCING OF EDUCATION 235, 259–60 (R. Johns ed. 1970).

Insofar as education is concerned, cost differentials, or the weighted-student approach might be utilized to preserve maximum local control. For a brief overview

choice in expenditure patterns, many of the poorer districts will experience the opportunity for choice for the first time. In any event, the genuine need for pluralism and decentralization in the administration of education can be met by the state dispensing a significant portion of the resources to each district with no strings attached. Under such a program, each district would continue to be free to manage its own programs and to set its own priorities.

Until recently, most judicial activity has focused upon service level disparities and not on taxes as such. Tax disparities, however, create similar problems of a reciprocal nature. Referring once again to the New Jersey method of financing welfare,[142] overutilization of unequalized local tax bases to finance uniform levels of a social service with significant spillover leads to the converse of *Serrano*. In fact, the New Jersey system amounts to what California would encounter if it sought to comply with *Serrano* by mandating that each school district should spend the same amount per pupil, but that the necessary revenues should be raised solely within the boundaries of each district. The obvious effect of this practice would be to have tax rates move inversely to the wealth of the school district.

While courts have become involved with the constraints which the equal protection clause imposes on the states in discriminating against some individuals and districts in favor of others, they have been reluctant to constrain the taxing discretion of legislatures. In tax matters, the Supreme Court has held that "a classification, though discriminatory, is not arbitrary nor violative of the Equal Protection Clause of the Fourteenth Amendment if any state of facts reasonably can be conceived that would sustain it."[143] For obvious policy reasons, great flexibility has been accorded to states in raising revenue.

With this legal framework and the economic realities of the property tax in mind, the New Jersey pattern of finance can be evaluated. Under that system, county governments are required to provide 25 per cent of the total cost of welfare within their respective

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of the weighting process, *see* McLure & Pence, *Early Childhood and Basic Elementary and Secondary Education*, in PLANNING TO FINANCE EDUCATION 23–27 (Johns, Alexander & Jordan eds. 1971). Under this approach, the state would determine the unit cost of educating various kinds of students, *i.e.*, the physically or mentally handicapped, members of minority groups, urban or rural children, and students in vocational, elementary, or secondary school. After setting a dollar figure for the cost of educating each such student, the state would then distribute funds to each locality according to the number of the various kinds of students within the particular school district. These resources would then be made available to the districts to spend as they might choose, such as for teachers' salaries, decreases in pupil-teacher ratios, improved physical facilities, or an expanded curriculum.

142. *See* notes 13–16 and accompanying text *supra*.

143. Allied Stores v. Bowers, 358 U.S. 522, 528 (1959).

jurisdictions.[144] Although the amount of benefits is standardized throughout the state, the incidence of welfare recipients per county varies throughout the state. Thus, since some counties have wealthier tax bases than others, this system results in substantial variations of tax rates. Based upon those facts, the constitutionality of the New Jersey property tax has recently been contested.[145]

Moreover, forced interdistrict tax disparities will most likely result in both interregional and interarea locational effects. When one service such as welfare, or when one level of government such as the state, makes exorbitant demands upon a tax base, other governmentally provided services, such as fire and police protection, are certain to suffer. Furthermore, when those who are relatively more wealthy flee high tax enclaves leaving the poor behind, the tax base erodes, thereby driving up rates just to maintain existing service levels. Again, when the legislature seeks to assist the poor by increasing welfare assistance, the poor are required to finance a large portion of this very same assistance.

Other than these problems, a further anomaly exists. The concept of ability to pay as a means of redistributing income downward plays an insignificant role in this system. Tax rates vary on a county-by-county basis. A significant number of poor people will live in counties in which tax rates are high and therefore pay exaggerated amounts of taxes to finance welfare; at the same time, a significant number of wealthy people will live in counties where tax rates are low, and therefore pay reduced amounts to finance welfare. Thus, income is not simply redistributed from the wealthy to the poor, but rather is redistributed from the wealthy to the poor in varying rates depending upon where the taxpayer happens to reside.

The courts must be prepared to grapple with such economic factors if satisfactory results are to be achieved in upcoming challenges to state taxation schemes. Correlation of services and tax bases by courts and legislatures must be the lode star of analysis if these challenges are to be manageable. The problem presented by this illustration, then, should not be regarded as a distinct problem, but rather as one facet of the problem of interdistrict service disparities.

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144. *See* note 13 *supra.*

145. Bonnet v. Cahill, Civil No. L-3865-72 (Super. Ct. N.J., filed Oct. 11, 1972). It was argued therein that "[t]he imposing of taxes and the raising of revenues and its incidence entails a fundamental right of all citizens to fair treatment in defraying the cost of government." Plaintiff's Complaint, *id.* It is unlikely that any court would accept such an argument because it would require the overruling of the *Allied Stores* case, cited favorably in *Rodriguez,* and would involve the judiciary in an unending determination of which taxes are discriminatory. *Cf.* 93 S. Ct. at 1302.

2. The Shaw *Problem*

Intradistrict disparities in the level and quality of municipally run services due to individual wealth variations raise the same economic issues appearing in *Serrano-Rodriguez* and novel ones as well. Central to an understanding of the situation presented by *Shaw* is the realization that all governmentally provided services are not within the same class.[146] Some services are provided by or authorized by municipal governments not because they are governmental or social in nature, but merely because economies of scale dictate that the locality either grant private enterprise a monopoly or undertake to provide the service itself. Utilities are the most notable of this class of services, but others include public transportation, ambulance service, certain recreational facilities, and, perhaps, paving of residential streets[147] and street lighting. To the extent that these services are provided to recipients at less than unit cost, these recipients become the beneficiaries of a form of welfare. It is at this point that the local property tax becomes important because of its continuing role as the mainstay of local finance.

If these services are to be guaranteed to recipients independently of their ability to pay, it is likely that the property tax will be used to meet the cost differential. For example, if the residents of a particular locality decide to maintain low water rates by means of subsidizing a municipally operated water department, this added cost must nevertheless be absorbed in some manner. In such a case, the subsidy will probably be provided from the property tax revenues. This approach has the effect of saddling those in geographic proximity to those who want cheap water, or welfare in kind, with the responsibility for providing it. Under this approach, ability to pay as a basis for redistribution of income from the wealthy to the poor does not even enter into the equation. Since the local property tax is the most likely revenue source to be utilized in providing such a "free" service, the economic consequences of using this device should be understood.

These economic consequences will vary from jurisdiction to jurisdiction depending upon the economic composition of the particular taxing unit. In any event, the cost of living in proximity to poor

146. Since the inquiry in *Shaw* focused on discrimination based on wealth, service analysis did not really enter into the majority's thinking. Once racial discrimination or discrimination based upon wealth is shown, then any disparity in municipally provided or, perhaps, even municipally franchised (*see* Ihrke v. Northern States Power Co., 328 F. Supp. 404 (D. Minn. 1971), *rev'd,* 429 F.2d 566 (8th Cir. 1972)), services can be found to be an "invidious discrimination" in violation of the fourteenth amendment.

147. Texas cities may levy special assessments to pay for street maintenance and improvements on a frontage fee basis rather than on the market value standard. TEX. REV. CIV. STAT. ANN. art. 1082 (1963).

people will inevitably rise. Unfortunately, it is often the marginally poor, not the wealthy, who live near the poor.[148] In certain situations, efforts on the part of a municipality to provide welfare in this manner can produce negative results. Where the residential tax base is composed primarily of low-income housing and little or no business, and a significant number of welfare recipients live within the jurisdiction (who cannot afford to pay for their utilities but who have the political power to compel the city to finance these services via the property tax instead of through user fees), these recipients of "free" services will become the beneficiaries of property tax payments made by homeowners within the community. It should be noted, however, that to the extent these recipients experience rent increases due to this new burden on the property tax, this added cost must be deducted to calculate the net gratuitous benefit. As a result of this approach, the poor finance a portion of the "free" services, while the marginally poor are compelled to pay for the rest.

Income is redistributed progressively if a community is blessed with a "golden" industry. Since these industries possess the power to shift the increased tax forward and export it from the taxing jurisdiction onto consumers elsewhere, a community with such an industry has resources within its boundaries for substantial welfare in kind. The limit on these resources will be reached when the taxes absorb whatever market power the industry possesses. Again serving as a good example of such a district is Ector County, Texas, in which oil and gas constitute over 70 per cent of the property tax base.[149] Since the county meets its present needs through relatively low assessment ratios, it has tremendous financial potential for financing services through the local property tax. If, for instance, Ector taxed at the same rate as its less fortunate neighbor, Mesquite, its citizens could enjoy an extensive range of public services financed largely by consumers of oil and gas.

Of course, these two examples are extreme. Most districts fall somewhere in between. Nevertheless, the level and quality of "free" services will be a function of the taxpaying ability of a given community weighed against its desire for particular services. In this respect, the property tax has an effective ceiling only when voting property owners decide that they get more utility from private services than tax-supported services, and, based on this perception, refuse to permit increased taxation. Since this ceiling will vary among taxing units, both tax and service differentials will develop. As previously

148. STATE AID TO LOCAL GOVERNMENT, *supra* note 26, at 67–69.
149. *See* notes 100–12 and accompanying text *supra*.

noted, such differentials can lead to disaster for certain communities by forcing industries operating at a low margin of profit to relocate in order to avoid high taxation, and by inducing the relatively wealthy residents to flee to jurisdictions with fewer poor people and lower tax burdens.[150]

Compelling cities to provide private municipal services to their residents, independent of the individual's ability to pay, as in *Shaw,* or even permitting cities to undertake this responsibility if they choose through normal political processes, can only lead to tax and service differentials with concomitant dysfunctional economic effects. In short, after local attempts to provide welfare in cash or in kind, the poor will remain poor, the marginally poor will become poorer, and those individuals and industries able to flee high tax enclaves will do so, leaving behind a situation worse than if nothing had been done.[151]

All of this is not to say that nothing can or should be done; rather, in terms of providing welfare and education, nothing can or should be done locally. Local unequal tax bases cannot provide equal social programs with extralocal impact. Disguising welfare payments by providing what are essentially private services independently of the recipient's ability to pay only exacerbates tax and service inequities. Needs and resources are inevitably mismatched.

Still, state government must be accorded flexibility in meeting the needs of its citizens. Certainly, a state should, if it chooses, be permitted to provide welfare in kind to its needy citizens, so long as it provides those services equally throughout its jurisdiction. However, under existing constitutional doctrine, a state has no affirmative responsibility to provide welfare at all. For a state to attempt such a task by making available whatever municipal services that a court or legislature might consider "fundamental" would be policy madness. How much water, sewage, street paving, bus fare, garbage collection, street lighting, recreational facilities, and so forth must the state, through the local governmental unit provide to the indigent? These decisions for nonindigent consumers are made with relative ease because they set their own financial priorities and then buy what they can afford.

150. STATE AID TO LOCAL GOVERNMENT, *supra* note 26, at 69–70.

151. This problem is most acute in the populous cities of the East where property taxes are among the highest in the country. *Cf.* note 55 *supra.* The futility in trying to furnish services that many jurisdictions cannot afford prompted President Nixon to offer revenue-sharing legislation. In pinpointing the pressures on state and local leaders resulting from tax limitations and service demands, the President stated:

> [T]hey [state and local leaders] must cut services or raise taxes to avoid bankruptcy. . . . [T]he problems they face and the public they serve demand expanded programs and lower cost. Competition between taxing jurisdictions for industry and for residents adds further pressures to keep services up and taxes down.

H.R. Doc. No. 92–44, 92d Cong., 1st Sess. 3 (1971).

On what possible basis can government decide how much of each of these services it must provide for indigents? What are minimal or subsistence levels of each of these services? Moreover, just as with education, the only way that ensuing interdistrict disparities in these services could be remedied would be through some form of the social equity approach by which the state, not the locality, determines need and pays the cost. Such an effort would result in centralized bureaucratic decisionmaking on an unimagined scale.[152]

B. Legal Rationales

1. The Compelling Interest Standard and Its Problems

Serrano, Rodriguez, and *Shaw* represent the latest manifestation of a relatively new aspect of the equal protection doctrine. In the last thirty years, the equal protection clause has developed a more stringent test for evaluating certain kinds of governmental action.[153] The traditional equal protection standard considered only whether the questioned classification was rationally related to a legitimate government policy.[154] The newer test, however, requires the state to show a compelling state interest to justify certain legislative classifications when those classifications touch certain fundamental rights or are based on suspect criteria.[155] Suspect classifications include race,[156]

152. Although the most appropriate means for providing welfare, or redistributing income downward, is not the main focus of this study, efficiency in the allocation of resources for providing various public services is relevant to this analysis. Once a service is defined to be a "fundamental interest," or one that must be made available to all regardless of ability to pay, some mode of deciding the extent to which that particular service should be provided to the poor must be developed. In this respect, bureaucratic decisions concerning the needs of the poor are likely to control if in-kind disbursements, rather than cash transfers, are to be made. Cash disbursements would preserve the natural control elements of the market place by permitting indigents to choose for themselves what they want and do not want, while at the same time providing an income floor at the subsistence level.

If welfare is to be provided, cash, or some form of a voucher system for in-kind disbursals, would appear preferable to furnishing in-kind services. However, if municipal services are to be provided to the poor irrespective of the individual ability to pay, then the bureaucracy necessary to achieve these goals would quite likely lead to inefficiency and establish a vested interest for providing more and more "unneeded" services, since bureaucratic strategies in the budgetmaking process can be expected to reflect more the needs of a healthy bureaucracy than an objective assessment of the needs of the service recipients. A. WILDAVSKY, THE POLITICS OF THE BUDGETARY PROCESS 21–31 (1964).

153. *See generally* Tussman & tenBroek, *The Equal Protection of the Laws,* 37 CALIF. L. REV. 341 (1949); *Developments in the Law — Equal Protection,* 82 HARV. L. REV. 1065 (1969).

154. The traditional test is used primarily to evaluate state regulation of economic activity. *See, e.g.,* Ferguson v. Skrupa, 372 U.S. 726 (1963); Railway Express Agency, Inc. v. New York, 336 U.S. 106 (1949).

155. *See, e.g.,* Shapiro v. Thompson, 394 U.S. 618 (1969). A clear expression of the newer doctrine is provided in Justice Harlan's dissent. *Id.* at 658. *See also* 36 Mo. L. REV. 117 (1971), in which the author finds three classifications — the traditional rational basis test for economic regulations, an intermediate compelling interest test for fundamental rights, and a legitimate overriding purpose test for racial classifications.

156. Loving v. Virginia, 388 U.S. 1, 9 (1967).

wealth,[157] and, possibly, any distinction based on the exercise of a constitutional right.[158] Fundamental rights have included voting,[159] indigents' rights to counsel in felony cases[160] and to transcripts for appeals,[161] and the rights of illegitimate children.[162]

a. The Dangers of Using "Fundamental Interest" as a Test

A danger associated with the compelling interest doctrine is its potential for almost infinite expansion. Justice Harlan pointedly described this danger:

> It [the fundamental interest classification] is unfortunate and unnecessary. It is unfortunate because it creates an exception which threatens to swallow the standard equal protection rule. Virtually every state statute affects important rights. . . . [T]o extend the "compelling interest" rule to all cases in which such rights are affected would go far toward making this Court a "super-legislature." This branch of the doctrine is also unnecessary. When the right affected is one assured by the Federal Constitution, any infringement can be dealt with under the Due Process Clause. But when a statute effects only matters not mentioned in the Federal Constitution and is not arbitrary or irrational . . . I know of nothing which entitles this Court to pick out particular activities, characterize them as "fundamental," and give them added protection under an unusually stringent equal protection test.[163]

In *Dandridge v. Williams*,[164] the Supreme Court retreated from its position concerning fundamental interests as expressed in *Shapiro v. Thompson*.[165] Instead of extending the categories of fundamental interests, the Court retreated toward Justice Harlan's position in his *Shapiro* dissent and limited fundamental interests to affirmative constitutional rights.[166] In *Dandridge*, recipients of welfare benefits under the Aid to Families with Dependent Children Program[167] asserted that a state-imposed ceiling on payments violated the equal protection

157. Wealth as a factor has invoked the higher standard when relating to a fundamental right such as voting, Harper v. Virginia Bd. of Elections, 383 U.S. 663, 668 (1966), or an indigent's right to a free transcript on appellate review, Griffin v. Illinois, 351 U.S. 12, 17 (1956).
158. Shapiro v. Thompson, 394 U.S. 618, 634 (1969).
159. Reynolds v. Sims, 377 U.S. 533, 561-62 (1964).
160. Douglas v. California, 372 U.S. 353, 355 (1963).
161. Griffin v. Illinois, 351 U.S. 12, 17 (1956).
162. Weber v. Aetna Cas. & Sur. Co., 406 U.S. 164 (1972); Levy v. Louisiana, 391 U.S. 68 (1968).
163. Shapiro v. Thompson, 394 U.S. 618, 661-62 (1969) (dissenting opinion).
164. 397 U.S. 471 (1970).
165. *Id.* at 484 n.16.
166. *Id.* at 484.
167. 42 U.S.C. §§ 601 *et seq.* (1970).

clause because it discriminated against recipients with especially large families. Although it acknowledged that "administration of public welfare assistance . . . involves the most basic economic needs of impoverished human beings,"[168] the Court found no constitutional justification for applying the compelling interest standard to the state action. Moreover, in the course of validating the state scheme, the Court declared itself to be without constitutional power to "second-guess state officials charged with the difficult responsibility of allocating limited public welfare funds among the myriad of potential recipients,"[169] and characterized the issue before it as one concerning only "state regulation in the social and economic field, [and] not affecting freedoms guaranteed by the Bill of Rights . . . ."[170]

The plaintiffs in *Serrano* and *Rodriguez* sought to test the alleged discrimination by the compelling interest standard, claiming that education is a fundamental right,[171] and that the classifications being challenged were based on a suspect factor, wealth.[172] Similarly, the plaintiffs in *Shaw* attempted to prove that the discriminatory distribution of municipal services therein challenged was based on another suspect factor, race.[173] The courts accepted each of plaintiffs' allegations, thus leaving the door open to further expansion of the fundamental interest concept. Even if the Supreme Court had decided, as the California Supreme Court did,[174] that the more rigid test applies only to classifications concerning fundamental interests, one need not unreasonably stretch his imagination to see that the arguments made in *Shaw* could easily be merged with those of *Serrano:* the necessities of life are the most fundamental human interests; local services, such as water and sewerage, clearly involve such fundamental interests; therefore, any classification based on wealth that touches such fundamental interests is subject to the compelling interest test. Inability to pay thus becomes a discriminatory classification based on wealth.[175]

168. 397 U.S. at 485.
169. *Id.* at 487.
170. *Id.* at 484.
171. Serrano v. Priest, 5 Cal. 3d 584, 605–11, 487 P.2d 1241, 1255–59, 96 Cal. Rptr. 601, 615–19 (1971).
172. *Id.* at 598–605, 487 P.2d at 1250–55, 96 Cal. Rptr. at 610–15.
173. 437 F.2d at 1287–88.
174. The California court read Griffin v. Illinois, 351 U.S. 12 (1956), and Harper v. Virginia Bd. of Elections, 383 U.S. 663 (1966), narrowly and concluded that the compelling interest standard was to be applied to suspect factors, such as wealth, only if they also concerned fundamental interests. The court, nevertheless, found both the fundamental interest and the suspect factor. 5 Cal. 3d at 605–07, 487 P.2d at 1255–56, 96 Cal. Rptr. at 615–16.
175. One writer has suggested the use of the *Shaw* rationale to aid the poor in gaining equality in municipal services. He would combine traditional public utility doctrine with the thrust of Griffin v. Illinois, 351 U.S. 12 (1956), to demonstrate that municipal services must be financed by general revenues and supplied equally, or must withstand challenge under the compelling interest standard. Abascal, *Municipal*

In light of the facility with which the California Supreme Court treated such a concept, in spite of language in *Dandridge* which was apparently intended to limit use of the fundamental interest concept to affirmative rights guaranteed by the Constitution, other courts would have had no difficulty in expanding "fundamental interests" to include almost all locally provided services.[176] If education were considered fundamental, could providing water, gas, electricity, or sewerage service be considered less fundamental? If these services are financed through the property tax and are supplied unevenly because of the relative wealth of different districts, or if they are financed by user charges which the poor cannot afford to pay, they would be subject to a *Serrano-Shaw* style attack.[177]

b. The Dangers of Using "Wealth" as a Classification

A second danger in the application of the compelling interest test in this setting is treating wealth as a suspect classification. In the previous cases in which the doctrine developed, the interests at stake were essentially noneconomic — for example, the right to vote and the indigent's right to a fair trial.[178] Arguably, these interests could have been protected on due process grounds alone, without resort to the equal protection clause[179] because they are affirmatively guaranteed by the Constitution. But unlike the right to vote and the right to fair trial, the provision of basic economic needs is not guaranteed by the Constitution. There is no affirmative right to welfare.[180] Justice Harlan, in his dissent in *Douglas v. California,*[181] recognized how close

Services and Equal Protection: Variation on a Theme by Griffin v. Illinois, 20 HASTINGS L.J. 1367, 1389 (1969).

176. The *Serrano* court noted the possibility that the compelling interest test might be expanded to other services in addition to education. In fact, the court cited *Shaw* as such an example, noting that plaintiffs in *Shaw* had originally alleged discrimination based on wealth only to drop the point on appeal. 5 Cal. 3d at 614–15, 487 P.2d at 1262–63, 96 Cal. Rptr. at 622–23. *See* note 177 *infra.* A fear of such unlimited expansion of the doctrine was clearly a factor in *Rodriguez. See* 93 S. Ct. at 1308–09.

177. Although the majority in *Shaw* did not distinguish services financed through special assessments from those financed from general revenues, the concurring opinion did. 437 F.2d at 1293 (Bell, J., concurring). Judge Bell cited Hadnott v. Prattville, 309 F. Supp. 967 (M.D. Ala. 1970), for the proposition that a city may provide services dependent on special assessments, *i.e.,* sewage, street lighting, street paving, or drainage, and thus not paid for from general revenue, even if disparities result in the level of services received by various residents within a city. This basis, even though narrower than the majority's, remains open to the fundamental interest analysis undertaken in *Serrano-Rodriguez.* Under that approach, street paving, sewage, or water lines, among other services, might be found to be "fundamental," and therefore required to be provided regardless of ability to pay.

178. *See* notes 154–62 and accompanying text *supra.*

179. *See, e.g.,* Shapiro v. Thompson, 394 U.S. 618, 655 (1969) (Harlan, J., dissenting); Douglas v. California, 372 U.S. 353, 361 (1963) (Harlan, J., dissenting); Griffin v. Illinois, 351 U.S. 12, 29 (1956) (Harlan, J., dissenting).

180. Dandridge v. Williams, 397 U.S. 471, 484 (1970).

181. 372 U.S. at 353, 361–62 (1963).

the Court was coming to finding such an affirmative right. He discussed the problem more fully than the Court was later to do in *Dandridge* when it accepted his basic position.

> Every financial exaction which the State imposed on a uniform basis is more easily satisfied by the well to do than by the indigent. *Yet I take it that no one would dispute the constitutional power of the State* to levy a uniform sales tax, to charge tuition at a state university, *to fix rates for the purchase of water from a municipal corporation,* to impose a standard fine for criminal violations, or to establish minimum bail for various categories of offenses. . . . And surely, there would be no basis for attacking a state law which provided benefits for the needy simply because those benefits fall short of the goods or services that others could purchase for themselves. Laws such as these do not deny equal protection to the less fortunate for one essential reason: the Equal Protection Clause does not impose on the States "an affirmative duty to lift the handicaps flowing from differences in economic circumstances." To so construe it would be to read into the Constitution a philosophy of leveling that would be foreign to many of our basic concepts of the proper relations between government and society. The State may have a moral obligation to eliminate the evils of poverty, but it is not required by the Equal Protection Clause to give to some whatever others can afford.[182]

By simply classifying services as fundamental or nonfundamental, a court might hold that certain disparities which result from mere inability to pay or from unequal property tax bases violate the equal protection clause. However, in many situations, such a holding would be the equivalent of finding an affirmative constitutional right to publicly supported governmental services, regardless of *Dandridge*. If the particular "fundamental" service involved is financed by user charges or private assessments, forced equality would amount to taxing others to provide the poor with basic services — welfare in kind. Adhering to the *Serrano* and *Shaw* analysis and its use of the compelling interest doctrine would tend to divert a court's attention from this most important and critical fact.

Certainly, when a state undertakes to provide welfare, it should be under the obligation to administer that program impartially, notwithstanding the absence of a duty to institute the program in the first instance. But when the state or locality merely licenses a public utility to perform proprietary services which are financed by private assessments, its relation to the individual is essentially different. It is

182. *Id.* (footnotes omitted).

not attempting to create a welfare program, and it should not be forced to do so. When the locality acts as a municipal corporation for providing services, that government's fiscal interest in making such services self sufficient and privately supported through direct user charges should be adequate justification for resulting disparities based on wealth.

The decision to establish and operate welfare programs, whether by making cash payments or providing services in kind, is a legislative one. In the absence of a constitutional requirement to establish such programs, the judiciary should refrain from interfering and refuse to engraft such a requirement onto the Constitution.

2. *A Middle Ground Rational Basis Test as an Alternative*

While the Supreme Court wisely avoided an adventure into metaphysics by rejecting the fundamental interest and suspect classification analyses, its inaction has left the nation with one of its most critical, unresolved problems. In this respect, all of the Justices were agreed that the problems associated with interdistrict inequities in education are serious and deserve immediate attention.[183] Even though affirmance of the lower court decision on any ground would have involved the judiciary in complex state and local service and tax questions, the Court could have decided the case on the narrower grounds suggested by Justice White in his dissent,[184] and have avoided some of the more blatant dangers.[185]

Justice White would have affirmed the lower court on an alternative basis. In his dissent he outlined the following test:

> The Equal Protection Clause permits discriminations between classes but requires that the classification bear some rational

183. 93 S. Ct. at 1309–10. *See id.* at 1312, 1315 & 1316 (Brennan, White & Marshall, JJ., dissenting).

184. *Id.* at 1314–15 (White, J., dissenting).

185. If the Court had found education to be a fundamental interest, then any different treatment accorded one class as against another would have had to be justified in terms of a compelling state interest. Extending that standard to all aspects of education would have invited the judiciary to substitute its judgment for that of the legislature on critical policy matters.

Illustrating this point, in Mills v. Board of Educ., 348 F. Supp. 866, 876 (D.D.C. 1972), after quoting the same language from Brown v. Board of Educ., 347 U.S. 483, 493 (1954), as had the *Serrano* court (*see* note 118 *supra*), the court held that funding deficiencies in educational programs "cannot be permitted to bear more heavily on the 'exceptional' or handicapped child than on the normal child." 348 F. Supp. at 874–75, 876. Such reasoning could give rise to a situation in which a legislature might find a rational basis for allocating scarce educational resources to normal children rather than to the handicapped, only to have its judgment overruled by a court finding that there existed no compelling state interest justifying the different treatment.

relationship to a permissible object sought to be attained by the statute.[186]

In applying this test, the object to be attained must first be defined. For purposes of illustration, we may assume that the object[187] of free public education is to provide a means for the children of the state to acquire various skills that are deemed useful to society. Once the goal is determined, whatever class discriminations that are found to exist must be evaluated in terms of their relationship to the intended goal. Then, if the discrimination bears no rational relationship to the legislative goal, the discrimination must be judged invalid.

Although some dispute existed over the nature of the class discrimination that the *Rodriguez* plaintiffs demonstrated,[188] at the very

186. 93 S. Ct. at 1314.

187. *Id.* at 1305. In analyzing the problem in terms of the rational basis test, the majority did not attempt to define the object, or purpose, underlying state intervention in education. In other words, the majority apparently found irrelevant questions concerning why the states have created systems of free public education and what they expect to accomplish for their citizens through these programs. Instead, the majority simply reasoned from the premise that local control is in itself a legitimate end. *See id.* Under this analysis, programs that contribute to the end of maximizing local control would appear to be justifiable on that fact alone. This method of analysis, however, is questionable. Local control does not appear to be an end in itself, but rather a means to an end. While there is no such thing as a local control program, there are programs which can best be effected if they are locally controlled. Local control, then, is not an object in itself but rather an attribute of other objects.

By according independent status to the concept of local control, the majority seems to have ignored Griffin v. County School Bd., 377 U.S. 218 (1964). There, the Court was faced with a situation in which one county in the state exercised its local option, consistent with the laws of Virginia, to close its schools in order to avoid integration. The issue in *Griffin* involved "not something which the State has commanded Prince Edward to do — close its public schools and give grants to children in private schools — but rather something which the county with state acquiescence and cooperation has undertaken to do on its own volition . . . ." *Id.* at 228. Speaking for the Court, Justice Black stated that "[w]hatever nonracial grounds might support a State's allowing a county to abandon public schools, the object must be a constitutional one, and grounds of race and opposition to desegregation do not qualify as constitutional." *Id.* at 231 (footnote omitted). Apart from the question of race, the Court did not treat the concept of local control as an object in itself, but rather viewed it as an ingredient of the means chosen to effect the ultimate object of education.

If the majority's reasoning in *Rodriguez* is carried to its logical extreme, there is no reason why a state might not make education a completely local matter. Conceivably, *Griffin* could be read narrowly as a suspect factor case, thereby leaving states free to delegate total responsibility for funding and administering education to local school districts in the name of local autonomy, no matter what disparities might be shown.

One practical consideration that should be raised is the likely future impact of *Rodriguez* on reformation of state funding programs for education. While governors and legislatures do not mind spending money, they are loath to raise it. The *Rodriguez* decision may have the effect of inviting state officials to assign localities a greater, not lesser, role in public school finance, thereby widening already existing disparities. With less vigilance by the courts, state officials may be tempted to pass the revenue-raising buck to local officials who will be confronted with ever-increasing financial demands and no correlative financial resources.

188. Plaintiffs contended that the Texas school financing system discriminated not simply against the poor in some districts but against the poor in general. An under-

least, the Court was confronted with a situation in which the plaintiffs' district had less taxpaying ability[189] than other districts in the state.[190] There was no dispute that the taxpaying ability of the individual districts in Texas determined the availability of resources to be devoted to educational programs within each district.[191] Thus, the Court was faced with the fact that the plaintiffs, and all others who reside in districts with low taxpaying ability, had fewer resources available to meet educational needs. With this aspect of the service delivery scheme established, it was necessary to inquire whether a rational relationship existed between the object of providing public education and the class discrimination that had resulted from the means chosen to effect that end.

Having isolated the disadvantaged class, those who reside in districts with low taxpaying ability, it is necessary to examine the attributes of that class to determine if there is some rational basis for depriving them of the same educational opportunities that the other class enjoys.

There is little hard, empirical evidence concerning the demographic composition of school districts with low taxpaying ability. The plaintiffs, however, asserted that a sufficient correlation existed between the districts in which the poor, the black, and the brown resided and those in which educational expenditures were low,[192] thereby justifying the finding of invidious discrimination. One of the few empirical studies on this subject,[193] however, disputed that assertion. Based upon existing evidence, it must be presumed that there are no significant demographic factors distinguishing those who live in low-taxpaying districts and those who live in high-taxpaying districts.

If this is true, and the majority in *Rodriguez* seemed to accept the proposition, the only distinctions that can be shown between the

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lying assumption of the plaintiffs is that a correlation exists between district wealth, expressed in terms of assessable property per pupil, and personal wealth. *Cf.* 93 S. Ct. at 1290–91. In refusing to accept this premise, the majority cited recent empirical studies: Ridenour & Ridenour, Serrano v. Priest: *Wealth and Kansas School Finance,* 20 KAN. L. REV. 213 (1972); Note, *A Statistical Analysis of the School Finance Decisions: On Winning Battles and Losing Wars,* 81 YALE L.J. 1303 (1972).

189. *See* note 136 and accompanying text *supra.*

190. The issue of measurement of Texas school districts' taxpaying ability was not directly decided by the majority. *See* 93 S. Ct. at 1293. Still, however, it is unlikely that anyone would seriously contend that all districts have the same taxpaying ability. On the basis of the evidence presented by plaintiffs (*see id.* at 1287 n.38), it should be clear that Edgewood, the district in which the appellees reside, is, at the very least, among those districts in Texas with low taxpaying ability.

191. *Id.* at 1303–04.

192. *Id.* at 1282.

193. *See* Note, *supra* note 188, at 1328–29, which documented that "poor" families, as defined by the Bureau of the Census, are not congregated in enclaves with low property assessments. Rather, in Connecticut, where the study was made, the poor were found to live near major industries representing high assessed valuations.

classes relate to those economic factors that determine taxpaying ability. Using one of those factors[194] as an example — the incidence of industries possessing market power subject to property taxation within the district in which a particular student resides — the problem of establishing a rational relationship becomes clearer. In order for there to be a rational relationship between the goal of imparting skills to a student and the means for providing it, some evidence must be shown to support the inference that children who live in geographic proximity to industries with market power are more likely to benefit from exposure to educational programs than those who do not. Significantly, and not controverted by the *Rodriguez* majority, the existence or nonexistence of wealth in a given political subdivision is little more than "happenstance."[195] When analyzed then, the plaintiffs' characterization of the class discrimination as "invidious" is somewhat overstated; rather, the discrimination appears to be simply silly. Happenstance is, by definition, devoid of rationality and classes determined by that criteria bear no rational relationship to any goal.

In its analysis of the rationality of the service delivery system, the *Rodriguez* majority did not concentrate upon its relationship to the objective of providing education. Instead, the Court reasoned that local control in decision making, through the medium of the preservation of independent local access to revenue,[196] is a legitimate state interest in itself.[197] In rebutting this reasoning, Mr. Justice White stated:

> It is not enough that the Texas system before us seeks to achieve the valid, national purpose of maximizing local initiative; the

194. *See* notes 58–112 and accompanying text *supra*.

195. *See* 93 S. Ct. at 1307.

196. In discussing an hypothesized public education system in which each student would have to pay full tuition in order to attend school, the majority suggested that a more compelling reason would exist for finding an invidious discrimination against the "poor." In this situation, the Court recognized that the poor might not receive any education at all. Under the Texas system, however, the Court found the state minimum, as represented by the Foundation School Program, to be "adequate." *Id.* at 1291–92.

This reasoning reveals a basic flaw in the majority's approach to the problem. Of the 50 states, there are presently 50 definitions of "adequate" state participation. *See* STATE AID TO LOCAL GOVERNMENT, *supra* note 26, at 31–59. If the Court is saying that no state aid at all is inadequate, then what is the least state assistance that would be adequate? This kind of determination could involve the courts in a protracted case-by-case exercise if the term "adequate" was intended to have any meaning at all. A safer ground of decision in this respect would be to abandon the concept of adequacy and hold, as the district court did, that adequacy may be a factor only to the extent that expenditures in some districts are more adequate than others. 337 F. Supp. at 284. Utilizing this reasoning, the state would not be obligated to provide any education at all, but to the extent that it does, it must provide the same amount for all.

197. 93 S. Ct. at 1300–01, *quoting* Madden v. Kentucky, 309 U.S. 83 (1940).

> means chosen by the State must also be rationally related to the end sought to be achieved.[198]

Under the rational basis analysis undertaken by Justice White, local control may justify any number of financing schemes devised by the state provided that no scheme results in resources being channeled to districts on a basis unrelated to a valid educational goal.

For the present, and probably for the foreseeable future, the federal judiciary cannot be expected to participate in rationalizing service delivery and tax problems that state and local governments have been experiencing over the last several decades. The primary role of indicating flaws in the manner in which state and local services are provided will now quite likely shift from the federal courts to state courts[199] and legislatures and to the Congress. In any event, whichever institution attempts to modernize and make more equitable the dis-

198. 93 S. Ct. at 1314.

199. Just two weeks after the Supreme Court reversed the *Rodriguez* case, the New Jersey Supreme Court struck down New Jersey's present method of school finance. Robinson v. Cahill, ___ N.J. ___, ___ A.2d ___ (1973). The plaintiff in *Robinson* presented facts to the New Jersey Court similar to those that the plaintiffs in *Rodriguez* had presented to the Supreme Court. Both interdistrict disparities in per pupil expenditures and differentials in the ratio of taxable property per pupil were shown. Unlike the Supreme Court, however, the New Jersey Court accepted per pupil expenditure differentials as indicative of unequal access to equality of educational opportunity. But like the Supreme Court, the New Jersey Court found neither the fundamental interest nor the suspect factor analysis approach helpful. The New Jersey Court, in a clear effort not to entangle itself in the broader issue of which services may be financed locally and therefore unequally among districts decided the case on state constitutional grounds unique to New Jersey. *Id.* at ___, ___ A.2d at ___. Neither state nor federal equal protection theories were used to resolve the problem.

Rather, the New Jersey Court, as the legal basis for its action, seized upon an 1875 amendment to article IV, section 7, paragraph 6, of the 1844 New Jersey Constitution, which provides that:

> The legislature shall provide for the maintenance and support of a thorough and efficient system of free public schools for the instruction of all the children in this state between the ages of 5 and 18 years.

Based upon legal arguments peculiar to New Jersey, the court found that the legislature, by permitting wide disparities in per pupil expenditures to arise among the districts, had not met its constitutionally mandated responsibility to provide a "thorough and efficient system of free public schools." Specifically, the court held that:

> [I]f the State chooses to assign its obligation under the 1875 amendment to local government, the State must do so by a plan which will fulfill the State's continuing obligation. To that end the State must define in some discernible way the educational obligation and must *compel* the local school districts to raise the money necessary to provide that opportunity. . . . Upon the record before us, it may be doubted that the thorough and efficient system of schools required by the 1875 amendment can realistically be met by reliance upon local taxation. The discordant correlations between the educational needs of the school districts and their respective tax bases suggest any such effort would likely fail . . . .

Id. at ___, ___ A.2d at ___. After pointing to inherent difficulties in utilization of local tax bases, the court went on to state:

> Nor do we say that if the State assumes the cost of providing the constitutionally mandated education, it may not authorize local government to go further and to tax to that further end, provided that such authorization does not become a device for diluting the State's mandated responsibility.

Id. at ___, ___ A.2d at ___. This last remark, apparently an attempt to preserve the notion of an individual district's right to spend more on education than its neighbors, raises serious problems, perhaps unforeseen by the court. Beyond the fact that

tribution of both state and local services and tax burdens, its effort must focus upon the role of the local tax base and its limitations.

IV. THE SERVICE ANALYSIS PRINCIPLE AS AN ALTERNATIVE

This section will attempt to develop a systematic approach for handling disparities in all classes of state and local government services. Since the Supreme Court has held that the "fundamental interest" and "suspect factor" analyses are inappropriate analytical frameworks for coping with these problems, a different approach must be developed.

In meeting the needs of its citizens, the state should be accorded flexibility in devising specific service delivery and tax programs.[200]

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it was disparities, large and small, that first attracted the attention of the courts, monitoring these disparities in the context of the court's opinion might well prove impossible.

To illustrate, the court is in effect holding that once the legislature provides for a "thorough and efficient system of free public schools," local districts may then add an increment from their own tax bases on top of this minimum. Such an approach, however, presupposes that "thorough and efficient" can be judicially determined in terms of an absolute dollar amount. Following this reasoning, once the court is satisfied that the legislature has met its responsibility, it may permit the legislature to authorize additional local expenditures. This reasoning ignores the fact that this is essentially the same situation that now exists, except that the basic state aid program has been held constitutionally insufficient. In this respect, the court's opinion gives little guidance at what point it would find that a hypothetical state aid program would be sufficient. This problem of the judiciary defining "thorough and efficient" can only be avoided by confining judicial intervention to determining whether all classes are treated the same or not, if not, does a "rational basis" exist for the discrepancy — the kind of equal protection inquiry suggested by Mr. Justice White in his dissent in *Rodriguez*. *See* text accompanying note 186 *supra*. In other words, the judiciary is better equipped to ensure that the legislature treats all classes the same, than to dictate to the legislature how much education is enough to satisfy the constitutional standard.

New Jersey, then, represents a case in point in which a state court has attacked the problem of irrationalities in school finance. As state courts undertake the problem of coping with the school finance issue in the aftermath of *Rodriguez*, other state and federal courts, as well as the various state legislatures, should benefit from the problems brought to light by these inquiries.

200. In a different context, the Supreme Court has recently held that the one man one vote doctrine of Reynold v. Sims, 377 U.S. 533 (1964), and Kramer v. Union Free School Dist., 395 U.S. 621 (1969), did not extend to water districts. Salyer Land Co. v. Tulare Lake Basin Water Storage Dist., 93 S. Ct. 1224 (1973). Under the challenged California law. CAL. WATER CODE §§ 41000–01 (West 1966), voting is limited to property owners whose votes are weighted on the basis of one vote for each $100 of assessment. The plaintiff attacked the state voting scheme as a denial of equal protection. In rejecting plaintiff's contention, the Court distinguished the instant case from previous cases in which the one man–one vote principle had been ignored by state voting statutes. *See* Cipriano v. City of Hauna, 395 U.S. 701 (1969), where the Court struck down a Louisiana statute which gave only property owners the right to vote in elections to approve the issuance of revenue bonds by a municipal utility, and Kramer v. Union Free School Dist., *supra*, where the Court struck down a voter qualification statute for school districts which limited the vote to owners or lessees of taxable real property located within the district, spouses of property owners, or parents or guardians of children enrolled in the school.

In defining the public policy underlying whether the public in general, as opposed to private landowners in particular, should run water districts, the majority focused on the relationship between the service, water supply, and the recipients, users of irrigation projects. The minority, however, approached the problem differently and instead concentrated upon the nature of the entity providing the service rather than

While maximum flexibility should be accorded the legislature, flexibility should not be permitted to mask irrationality. In this respect, the method chosen by a legislature to meet a legislatively defined need should be rationally related to the purpose behind that need. Therefore, insofar as the property tax is concerned, application of this test requires that the economic effects of property tax financing for particular programs bear some rational relationship to the desired goal of those programs.

A. Categorization of Services

For purposes of analysis, services will be characterized on the basis of two basic principles: (1) consumers of services should pay for what they receive;[201] and (2) the state has no affirmative constitutional duty to provide welfare or to redistribute income downwardly. In view of these principles, services can be classified as (1) private,

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upon the service itself. In this respect, the minority pointed out that water storage districts are considered to be governmental and not proprietary units under California law; that directors of the district are public officers of the state; that the district possesses the power of eminent domain; that it may not be taxed; and that the district possesses governmental immunity against suit. 93 S. Ct. at ——.

The majority apparently grounded its decision on the fact that the district does:

> [N]ot exercise what might be thought of as "normal governmental" authority but [that] its actions disproportionately affect landowners . . . . All of the costs of district projects are assessed against land by assessors in proportion to the benefits received. Likewise, charges for services rendered are collectible from persons receiving their benefit in proportion to the services.

Id. at ——. By focusing upon the nature of the service, the relationship of the recipients to the service, and how the cost of the service is defrayed, instead of relying upon the presence of governmental trappings, it becomes clear that water districts more nearly approximate private utilities than social services run by genuine governmental bodies.

While not directly in point to the analysis suggested in this Article, this holding does establish that certain services performed by governmental entities may still be considered to be essentially private, notwithstanding the fact that a governmental entity is charged with the responsibility for providing the service. An understanding that this distinction exists and that it can be delineated is critical to the alternative method of analysis suggested in this Article.

201. This benefit theory of taxation is well established as constitutional doctrine; for example, the present use of special assessments against property owners to defray the cost of improvements that particularly benefit their property. In Norwood v. Baker, 172 U.S. 269 (1898), the Supreme Court outlined the following rule:

> [T]he principle underlying special assessments to meet the cost of public improvements is that the property upon which they are imposed is peculiarly benefited, and therefore, the owners do not, in fact, pay anything in excess of what they receive by reason of such improvement. . . .
>
> [T]he exaction from the owner of private property of the cost of public improvement in substantial excess of the special benefits accruing to him is, *to the extent of such excess*, a taking, under the guise of taxation, of private property for public use without compensation. We say "substantial excess," because exact equality of taxation is not always attainable, and for that reason the excess of cost over special benefits, unless it be of a material character, ought not to be regarded by a court of equity when its aid is invoked to restrain enforcement of a special assessment.

Id. at 278–79. For a detailed discussion of application of benefit principles of taxation in local governmental finance, *see* E. MCQUILLIN, LAW OF MUNICIPAL CORPORATIONS 18–43 (3d ed. 1950).

(2) social with significant spillover, and (3) social without significant spillover, and the duties of the governmental unit providing them can be defined.

1. Private Services

Private services are those services in which benefits are provided directly, in discrete amounts, to identifiable individuals or family and business units.[202] Private services do, in fact, constitute the bulk of governmental services in our free enterprise society. However, nothing in the Constitution guarantees that income or services be provided by government to the citizenry.[203] Nevertheless, constitutional constraints do exist which affect how government must distribute those benefits that legislative bodies, consistent with their delegated powers, choose to dispense.[204] Absent a legislative decision to convert a private service to a social one, all services, from television repair to health care, to electric power and water, are private, and should be available only to those who can afford to pay for them. The fact that a given service is franchised by the government should be irrelevant in determining whether services are private or social. In view of our historical, and continuing theoretical commitment to private enterprise, publicly provided services should be regarded as private, absent a clear legislative determination that they should be converted, through subsidization, into social services.

The courts' role in dealing with disparities in private services should be limited to the traditional, public utility doctrine. Briefly, a "municipality which provides services similar to those provided by privately owned public utilities has a duty to serve all members of the public within its territorial boundaries in an equal and undiscriminatory manner."[205] Here, the individual's relation to the governmental unit providing the service is essentially that of a consumer to a seller of any commercial product. Although the governmental unit does have a higher duty than the private seller in that it must sell to all,[206] neither

202. *See* note 63 *supra.*
203. *See* text accompanying notes 180–82 *supra.*
204. *See* Goldberg v. Kelly, 397 U.S. 254 (1970).
205. Abascal, *supra* note 175, at 1372. *See* Note, *The Duty of a Public Utility to Render Adequate Service: Its Scope and Enforcement,* 62 COLUM. L. REV. 312 (1962).
206. Even if a utility such as water, gas, or electricity is franchised, but not subsidized, by a local government, there exists some form of "state action" which might expose it to the proscriptions of the fourteenth amendment. In the absence of public subsidization, however, elimination of disparities in the level of public services among both individuals and communities because of variations in the wealth of the respective individuals and communities does not seem appropriate. For example, insofar as education is concerned, a deliberate scheme of subsidization exists because legislative bodies have decided that education is the kind of service that all should have irrespective of ability to pay. Therefore, when some, because of geography,

it nor the private seller has a duty to provide its services or product free to the poor.[207]

Those unable to purchase private services must look for relief to the legislative branch rather than the judicial branch of government. Providing the poor with basic services, whether in kind or by cash transfers to purchase these services, is a political decision. In the absence of a constitutional right to welfare, the courts are an inappropriate forum for gaining equality in the amounts of private services individuals receive. By refraining from guaranteeing equal amounts of private services to the poor, a court maintains both guiding principles. The benefits individuals receive are purchased, and the decision to provide welfare to the poor is left to the legislature.

2. *Social Services*

Social services are those with indivisible benefits which accrue to society at large. Included within this category is the entire array of education and welfare programs, as well as any "private" services that a legislature chooses to subsidize. The critical test, in this respect, focuses upon subsidization. If a legislative body decides that a particular service is sufficiently important or so "fundamental" that society should enjoy the benefit of such a program, in spite of the fact that the private economy will not sustain it, then the legislative decision, to provide that service at less than unit cost to those who cannot other-

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are denied the same level of service that others receive, the fourteenth amendment should be applicable. On the other hand, a city may grant an exclusive franchise to a transportation company to make bus service available to those citizens who are willing to pay for it. The mere granting of an exclusive franchise should not be converted into an obligation on the part of the city to provide free bus service to all who desire it. The granting of the franchise should simply necessitate that rates be the same for all similarly situated citizens and that no citizen who can pay the applicable rate be denied service.

207. *See* note 65 and accompanying text *supra*. As a matter of fact, many of these services are presently being provided on a "free" basis. For instance, it is commonplace for utilities to be subsidized via local property tax transfers. *See* ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS, FACTORS AFFECTING VOTER REACTIONS TO GOVERNMENTAL REORGANIZATION IN METROPOLITAN AREAS 52–53 (1962). This is accomplished by public utilities gaining access to property tax revenue and using such revenue to keep utility rates artificially low. As an example of this practice, water control and improvement districts in Texas may both levy taxes and set water rates to defray costs. TEX. REV. CIV. STAT. ANN. art. 7880–77a (1954). Nothing, however, forbids such a district, if the voter-taxpayers can be persuaded, from using property tax revenue to keep rates low.

Two dysfunctional implications arise from this practice. First, users of water as a class receive "free" water as welfare; that is, they receive water without paying its full cost. Users of water as a class is not a rational class for distributing welfare, since some users of water are quite wealthy. Further compounding the irrationality of this practice, property taxpayers who pay for the "free" water include both rich and poor alike. The net result is that some poor property taxpayers subsidize "free" water for some wealthy water users. Secondly, using the property tax to subsidize "free" private services tends to preempt the property tax from adequately supporting social services. Once again, it should be emphasized that private services should be self-sustaining, thereby leaving the tax base free to pay for social services.

wise afford it, marks the point of conversion from what may have previously been a private service into a public service. Such an effort, in reality, amounts to an attempt to redistribute income downward. A further characteristic of social services is that, although the initial benefit may be conferred directly on an individual, as with welfare or education, the ultimate benefit redounds to society as a whole. For example, since education substantially benefits all of society, all taxpayers should support it; its cost should be defrayed by general revenues; and these revenues should be generated by a broadly based tax, preferably one based on ability to pay, such as a graduated income tax.

Matching recipients of indivisible benefits to the proper tax base is further complicated by the spillover concept.[208] If the tax is actually to be borne by recipients of the benefit, the proper geographical area must be drawn. Since the state is the largest political unit with general welfare powers, it should serve as the basic taxing unit for social services with significant spillover. Ideally, the federal government should help finance those services with the greatest spillover, such as education and welfare. Social services with limited spillover should be financed by a smaller unit. Fire and police protection, for example, benefit only the residents of a particular community or town and should be financed by that unit.

Where the benefit of a service has significant spillover and extends throughout the whole state, it is a "state function" and the whole state should finance it. When performing such a governmental function which benefits all its members, the state should have an affirmative duty to insure equality in the level of service. Therefore, the state cannot permit local subdivisions to exercise local choice over the level of the service to be provided. Because the service is a state function, decisions about the level of that service should be made by the corporate body that receives the benefit and bears the burden of the tax.

3. Spillover

Once individual services have been categorized as either private or social, there is the further question of whether all social services must be provided equally in all geographic areas of the state. Traditionally, states have not been compelled to treat all citizens in all geographic areas alike so long as there existed some rational basis for differentiation.[209] The purpose of this analysis is to ascertain whether

208. *See* STATE AID TO LOCAL GOVERNMENT, *supra* note 26, at 6-7.

209. *See* Abascal, *supra* note 175, at 1372-73; Horowitz & Neitring, *Equal Protection Aspects of Inequalities in Public Education and Public Assistance Programs from Place to Place Within a State,* 15 U.C.L.A.L. REV. 787, 797-800 (1969).

a state scheme for providing various social services with significant spillover out of local tax revenues on a local option theory can be justified on a rational basis test.[210] Brief examples of rational bases for differentiation on a geographic basis might include the following: an irrigation subsidy for all areas in the state of less than 10 inches rainfall; a public utility subsidy for all citizens living in sparsely populated regions; or a public transportation subsidy for mass urban transit in densely populated areas.[211] Social programs, or private services that a legislature converts into social services through subsidization, fall into two distinct categories. Certain social programs, such as fire and police protection, are undertaken as traditional governmental services necessary to permit society to function.[212] Other social programs, however, are undertaken in order to redistribute income downward,[213] to provide welfare-in-kind. An example of these programs is

210. Other writers, most notably Coons, Clune, and Sugarman, have not attacked disparities in education and other services as being violative of the rational basis standard. Instead, the thrust of their attack has been to create a legal argument for bringing education within the "inner circle" of rights subject to the compelling state interest standard. *See* Coons, Clune & Sugarman, *supra* note 138, at 346–51. The purpose of this Article is to analyze services in economic terms in order to determine whether a rational basis does, in fact, exist for permitting interdistrict disparities in certain kinds of services. Central to this analysis is the notion that the existence of substantial "spillover" in itself precludes a state from being able to show *any* rational basis for disparities in service levels.

211. Local option subsidizing of any of these services will inevitably result in similarly situated service recipients receiving disparate amounts of service depending upon the wealth of their respective local tax bases and upon the capacity of their respective tax bases to shift the tax forward and export it away from the jurisdiction. Using the first mentioned subsidy as an example, the lack of any rational basis for local option financing becomes apparent.

If Ector County, Texas, which has a wealthy tax base as a result of vast oil reserves within its boundaries (*see* notes 100–08 and accompanying text *supra*), were to choose to subsidize irrigation on a local option basis, then its citizens could enjoy reduced water cost with little actual cost to themselves. However, the neighboring counties, with relatively poorer tax bases would not be as likely to subsidize irrigation. Assuming all agricultural and market factors to be identical, there is no rational basis for a subsidy program in which a farmer-recipient in Ector County is much more likely to receive a subsidy than an identical farmer-recipient in a neighboring county. If there is a need for subsidizing irrigation to stimulate agricultural development, there is certainly no rationality in subsidizing on the basis of a farmer's geographic proximity to oil. A similar argument may be made for subsidization of public utilities and public transportation. If certain categories of citizens are defined as "needy," *i.e.*, those who need a public utility but who live in a sparsely settled area or those who need mass transit because they live in a congested urban area, making these services available in rough proportion to the incidence of "golden" industries in their respective jurisdictions is irrational on its face.

212. Such governmental functions have been labelled as "uniquely public activities," or have historically been financed from general revenues and have been viewed as not conferring any special benefits to particular individuals or groups. *See* Comment, *Rational Classification Problems in Financing State and Local Government*, 76 YALE L.J. 1206, 1210–12 (1967).

213. The inquiry undertaken by some courts to determine whether the general public or particular individuals benefit from a particular service, *cf.* Hammet v. Philadelphia, 65 Pa. 146 (1869), illustrates the judicial viability of a determination of whether the "primary" purpose and effect of a program is to redistribute income downward, or whether such effect is only "incidental." *See* Erie v. Russell, 148 Pa.

public housing subsidies designed to provide shelter for those otherwise unable to afford it. In an historical, as well as operational, context, housing is not identified with governmental action as such. The government, without attempting to convert this service into a uniquely governmental activity, has merely intruded into this area to meet a politically perceived need.

Insofar as education is concerned, substantial spillover is readily apparent. An entire state benefits from a high level of education in any area; likewise, an entire state will suffer from enclaves of poor education.[214] Other programs, however, raise more difficult questions. The difficulty arises from the imprecision in measurement of the geographic extent of the incidence and impact of benefits.

If the prime effect of a locality offering a social service is to redistribute income downwardly, then such a service has spillover by virtue of that fact alone. This stems from the fact that when one locality, in relation to the others around it, reduces the price of certain services and increases the burden on its tax base, all localities, not just the taxing and spending locality, are affected.[215] Depending upon the economic equation at the time, other localities, in order to compete with the acting locality, must either raise benefits, reduce taxes, or suffer the consequences of inaction. Such redistribution of

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384 (1892). In both of the aforementioned cases, the courts attempted to identify the incidence of benefits of particular programs because in each instance special tax assessments were levied against individual property owners. The challenging taxpayers contested tax liability on the theory that the particular programs involved inured to the benefit of the general populace and, therefore, should not have been paid for by means of special tax assessments directed at a limited number of taxpayers. The Pennsylvania Supreme Court agreed and ruled in favor of the taxpayers.

214. STATE AID TO LOCAL GOVERNMENT, *supra* note 26, at 18–20.

215. Problems involving direct local subsidies to particular businesses in order to attract industry are similar in concept to problems involving tax and service differentials among localities growing out of local option subsidization of services which tend to redistribute income downwardly. Many states permit individual localities, on a local option basis, to grant local tax exemptions or to pledge public credit for building plant facilities for lease-back to private industry in order to attract business activity to their area. *See* Alyea, *supra* note 96, at 141–44. The economic effects of these financial inducements are not confined to the locality granting favors to business or taxing business to subsidize services. The inducements have been characterized as "wasteful, unethical, abortive, insidious, unnecessary, destructive of the tax base, of questionable legality, shortsighted, conducive to suidical inter-community competition, and a handicap to sustainable economic growth and the maximization of national income." *Id.* at 147. *See* BOND FINANCING, *supra* note 91. When one locality acts, it forces others to act, thereby magnifying problems of misallocation of resources among localities within a region.

However, direct subsidies to businesses often are made in the interest of public policy. *See* Port Authority v. Fisher, 275 Minn. 157, 145 N.W.2d 560 (1966). If for instance, a state-level planning body decides to induce industry to locate in a given area, its decision may be quite rational. Transferring such decisions to the state level would reduce, if not eliminate, the irrational economic effects of interdistrict competition, just as centralized state financing of social services with economic spillover would reduce, if not eliminate, disparate service levels among localities.

income is, quite obviously, an improper task to assign to political subdivisions within a state.[216]

Whether and to what extent many social programs have spillover depends upon a given program's income redistributive effects. Redistribution of income may be the "primary" effect of a program, or only an "incidental" effect.[217] Obvious examples of such redistributive services include the cluster of health and welfare programs. Less obvious examples of such services include subsidized utilities and transportation programs. To illustrate the economic problems created by local option financing, one locality offering higher cash welfare payments than surrounding localities has an obvious and immediate impact in terms of interdistrict resource allocation. While not so obvious, one locality offering subsidized utility rates, oftentimes financed through forward shifting of the property tax, also has an impact on interdistrict resource allocation. Thus, while one might argue that certain of these services, sewage for instance, have only local economic impact, local subsidization of these services can have significant extralocal consequences.[218] The tendency of a given service to redistribute income downwardly creates a significant spillover effect.

On the other hand, social programs of governmental nature, not conceived in an effort to redistribute income downwardly, do represent a class of governmental services for which some basis does exist for permitting service levels to be locally determined. If a governmental program is not inherently one with significant spillover, then such a program should be left to the localities within a state to fund and administer. Such programs, because of the limited incidence of benefits, have no significant spillover; that is, service level and tax level disparities among local governments have no appreciable economic impact outside of the localities providing them. Law enforcement and fire protection are examples of such programs; citizens in one district are not significantly affected by the levels of fire and police protection that exist in a neighboring district. Economic effects arising from disparate levels in these basic services are confined, therefore, to the particular localities choosing the levels. Since these services have little impact outside the jurisdiction performing them, the level of service is appropriately determined at the local level. This determination of the existence or nonexistence of spillover, is a scientific and not a metaphysical inquiry.[219]

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216. *See* STATE AID TO LOCAL GOVERNMENT, *supra* note 26, at 65.
217. *See* note 213 *supra*. *See also* Comment, *supra* note 212, at 1207–08.
218. *See* notes 90–99 and accompanying text *supra*.
219. *See* G. BREAK, *supra* note 62, at 176.

B. Problems of Implementation

Local tax bases, whether income, sales, or property, should be limited to the support of local social services. Only in this manner can disparities in the relative level of social services authorized by the state and having a statewide impact be eliminated. In addition to coping with possible equal protection challenges to state action in this area, application of the service analysis principle (SAP) offers both a more scientific approach than the present fundamental interest doctrine and the opportunity for a more efficient utilization of tax dollars.

Application of this principle to Texas would require more conceptual, than practical, changes, because most social services with substantial spillover are presently state operated. As a result of the *Rodriguez* holding, however, education, the largest and most visible such program, will continue to be significantly financed at the local level.

The second major social service with spillover, welfare, is, however, a state-operated program.[220] By denying localities the power to supplement welfare, Texas avoids the many dysfunctional economic effects that confront states such as California.[221] Moreover, Texas local governments apparently do not attempt to provide welfare-in-kind at the expense of property taxpayers.[222] Unquestionably, however, many relatively minor violations of this principle do exist. For example, cities may pledge property tax revenue for support of certain utility bonds,[223] as well as bonds supporting certain recreational projects.[224] Merely because governmental entities perform these services is not sufficient cause to burden taxpayers, as opposed to users, with the expense of financing private services. Inasmuch as any local effort to provide these services via a local tax base will result in interdistrict inequalities, such an effort should raise constitutional problems. Cities and counties in Texas do in large measure try to finance most private services through user and licensing fees and they should be encouraged to continue the practice.[225]

Besides education, the major exception in Texas to the prohibition of localities from providing welfare-in-kind lies in its scheme for estab-

220. The federal and state governments share the total cost of welfare in Texas. The federal government pays approximately 70 per cent of the $905.6 million total. TEXAS LEGISLATIVE BUDGET OFFICE, FISCAL SIZE UP — TEXAS STATE SERVICES 1971–1972, at 46 (1971).

221. California's situation demonstrates the problems arising from permitting local supplementation of federal and state welfare programs. Irrational service and tax patterns exist which penalize *recipients* of welfare in districts where expenditures are low and *taxpayers* in districts where expenditures are high. *See* Horowitz & Neitring, *supra* note 209, at 812–16.

222. *See* text following note 207 *supra.*

223. TEX. REV. CIV. STAT. ANN. art. 1106 (1963).

224. *See* text accompanying note 36 *supra.*

225. *See* text accompanying notes 43–44 *supra.*

lishing and financing public hospitals. Under the Texas constitution, certain cities or counties may, with the permission of the voter-taxpayers, create a hospital district.[226] These hospitals, however, have not been provided equally to the needy in all parts of the state.[227] If this form of welfare-in-kind is to be provided at all, then it ought to be provided to the needy in all parts of the state as a social service with substantial spillover effect. When viewed as a state program, there is little rationality in discriminating against the needy on a geographic basis.

In regard to other locally performed services, to the extent subsidies are needed to make these heretofore private services function properly, such subsidies should be financed at the state level in order to remain within the SAP. Since variants of the user charge method are now being utilized to finance these services, these techniques should be expanded and continued.[228]

Although the task of implementing such an approach is difficult, it is by no means impossible. Certainly, if courts can distinguish between governmental and proprietary services, as they have in the past, categorizing specific governmental programs into one of three categories — social with significant spillover, social without significant spillover, and private — can be accomplished.[229] The changes needed

226. TEX. CONST. art. IX, § 9, provides for the creation of local hospital districts and empowers localities to tax, through the local property tax, in order to pay for these services.

227. The state makes no effort to provide basic state aid for public health facilities. Thus, each district, if a hospital district has been created, spends as much or as little as local taxpayers choose. Clearly, wide disparities exist in the level and quality of this form of welfare-in-kind among the various areas of the state. The Advisory Commission on Intergovernmental Relations has recently suggested a state program of equalization of local property tax bases, in order to enable each locality to enjoy a somewhat equal program. SIGNIFICANT FEATURES, *supra* note 4, at App. ____. Even though this approach would be a significant step forward, it is subject to the same flaws as the system of power-equalization, proposed for the schools. *See* note 140 and accompanying text *supra*.

228. Utilization of a "family of user charges" to finance certain services provided by local governments is a major policy conclusion of a leading authority on the property tax — Dick Netzer. *See* D. NETZER, *supra* note 84, at 214–17.

229. Such distinctions are presently made by economists. *See* G. BREAK, *supra* note 62, at 176. The spillover concept, in particular, is recognized as a viable distinction. *See* STATE AID TO LOCAL GOVERNMENT, *supra* note 26, at 6–7; Brazer, *supra* note 141, at 251–53. Certainly courts, with the aid of economists and other experts, can draw these lines. While it is true that these categories would be judge-made, there is nothing novel in this approach. The well-established governmental-proprietary dichotomy used in determining governmental immunity is also a judge-made doctrine. In view of the fact that courts have not hesitated to give meaning to such broad concepts as "excessive profits," Lichter v. United States, 334 U.S. 742 (1948), it is submitted that no barrier, such as lack of justiciable standards or judicial manageability, exists.

Recently, courts have, in fact, shown a new willingness to resolve judicially intricate problems involving governmental services. *See* Wyatt v. Stickney, 344 F. Supp. 387 (M.D. Ala. 1972), in which the court, redressing what it found to be inadequate mental health facilities provided by the State of Alabama, invoked the due process clause to impose certain minimum standards on the state. The court ordered that the number of patients in a multi-patient room not exceed six persons; that

to effect the SAP are primarily conceptual. Tax realignment in Texas, as opposed to the states in the East and the Far West, would not be significant.[230] The primary difficulty with moving in this direction would be the development of planning bodies at the state level to provide social programs with spillover to all residents of the state on a rational and efficient basis. This would not seem to impose insuperable problems.

These conceptual changes, centering on state, instead of local, responsibility for a variety of social services, would not only offer a rational approach to equal protection problems, but would offer policy advantages as well. There is no question but that the present approach, in which localities retain a large share of the responsibility for providing statewide services has failed. Something will have to be done.[231] To date, revenue sharing has emerged as the primary device to ameliorate

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there be a minimum of 80 square feet of floor space per patient in a multi-patient room; that there be one toilet provided each eight patients and a lavatory for each six patients and that the toilets be installed in separate stalls to insure privacy; and that the diet for the patients provide at a minimum, the recommended daily dietary allowances as developed by the National Academy of Sciences. *Id.* at 395–407, App. A. The court arrived at these standards by consulting independent experts in the field of mental health and insisted that the Alabama legislature fund its newly mandated program. *Id.* at 393–94. If a court can undertake a task such as this, certainly it can work with the three categories suggested in this study.

230. The primary effect arising from utilization of this new approach in Texas, with its increased reliance on user charges to finance private services, would be curtailment of property tax, or any local tax, subsidies to various utilities, sanitation, and transportation programs. While tax realignment would not be significant in terms of absolute tax dollars, implementation of the SAP would affect the bond issues of many municipalities and special districts; revenue bonds would have to be substituted for general obligation bonds whenever an instrumentality might seek to finance private services. For a discussion of the distinguishing aspects of revenue bonds, *see* INTERNATIONAL CITY MANAGERS ASSOCIATION, TECHNIQUE OF MUNICIPAL ADMINISTRATION (4th ed. 1958).

231. A variety of options exists for providing social services with spillover effect uniformly throughout the state. Private services may also be subsidized, or in effect be converted to a social service under the SAP as long as the subsidization is undertaken on a rational basis. To illustrate, aid to the needy, aid to citizens in either sparsely or densely populated areas, and aid to the mentally and physically handicapped all constitute rational class distinctions for public subsidies. But aid to any of these classes only if they happen to live in a wealthy district, or denial if they happen to live in a poor district, is irrational.

Using public hospitals as an example, a state should be permitted to act if a need exists to provide such free health services to the needy. Several preferable alternatives to locally financed hospital districts should be explored. For instance, the state itself could fund a program of state hospitals throughout the entire state. Or, several free market-type solutions, based upon Professor Friedman's education voucher scheme could be utilized. *See* Friedman, *The Role of Government in Education,* in ECONOMICS AND THE PUBLIC INTEREST (R. Solo ed. 1955). Under this approach, the state could grant vouchers to all families with an annual income below a fixed figure to be used for the sole purpose of defraying health costs. Such a program also has policy advantages in that it would avoid the bureaucratic nightmare of creating another massive state agency. Under such alternatives, aid would be given the needy in all areas of the state on a uniform basis and not just to the "lucky" needy in certain isolated subdivisions that have, for one reason or another, perceived a need. The only limitation on legislative discretion should be the rational basis test, by which all citizens within a given class, not simply those within a given district, have equal access to any social-spillover programs that exist within the state.

community wealth disparities with regard to statewide social services. It should be emphasized, however, that revenue sharing can only reduce the impact of wealth disparities, not eliminate them as would the SAP.

To illustrate this point, neither of the approaches to revenue sharing[232] offered, as does the SAP, a reallocation of governmental responsibility for providing various services.[233] Rather, the revenue-sharing measures only direct a portion of the federal income tax base to existing governmental structures, thus permitting localities to increase services or reduce taxes.[234] A recent case, *Mathews v. Massell*,[235] points out some problems with permitting localities to choose, from a list of priority items, which services they want and how much they

232. Two versions of revenue sharing were offered to the Congress. In 1971 the Administration offered its approach. H.R. Doc. 92-47, 92d Cong., 1st Sess. (1971) [hereinafter cited as the Administration bill]. In 1972, Wilbur Mills, Chairman of the House Ways and Means Committee, responded by offering his own bill. H.R. 14370, 92d Cong., 2d Sess. (1972) [hereinafter cited as the Mills bill]. In order to illustrate their different underlying theories, both bills are discussed, even though the adopted program more nearly resembles the Mills bill. *See* State and Local Fiscal Assistance Act of 1972, Pub. L. No. 92-512, 86 Stat. 919 [hereinafter cited as Pub. L. No. 92-512].

233. The Administration bill did not attempt to set priorities for local-government expenditure of shared funds, but instead provided a general grant to all political subdivisions to spend as they might choose. The Mills bill, however, set forth priorities which financially encouraged localities to undertake certain tasks with shared funds. As finally enacted, these priorities included:

(1) ordinary and necessary maintenance and operating expenses for
  (A) public safety (including law enforcement, fire protection and building code enforcement),
  (B) environmental protection (including sewage disposal, sanitation, and pollution abatement),
  (C) public transportation (including transit systems and streets and roads),
  (D) health,
  (E) recreation,
  (F) libraries,
  (G) social services for the poor or aged, and
  (H) financial administration, and

(2) ordinary and necessary capital expenditures authorized by law.

Pub. L. No. 92-512, § 1222(a). Thus, under the act as passed on October 20, 1972, local governments may continue to subsidize private services and provide social services with spillover effect. In fact, in view of the formulae for determining federal fund entitlements (*see* note 234 *infra*), governments are encouraged to increase their tax efforts to obtain more federal money. As a result, existing imbalances in service and tax levels will persist.

234. Property tax reduction is not the prime thrust of revenue sharing. While no enforcement machinery exists under revenue-sharing legislation to prevent states and localities from using federal funds to replace local taxes, if states and localities do reduce their taxes, they would eventually be penalized for doing so. *See* note 236 *infra*. General tax effort" (*see* Pub. L. No. 92-512, § 1228(c)), plays a significant role in determining how much each state government (*see id.* § 1225) and each political subdivision within each state (*see id.* § 1227) receives in federal funds. In this respect, federal revenue-sharing formulae are designed to reward intense tax effort. Thus, if a city or state takes federal money and uses it to replace local money, thereby permitting a tax reduction, that same unit of government will, in the future, receive proportionately less funds than those governments that increase service levels and maintain intense tax effort.

Although an initial justification for revenue sharing was to create a means for the federal government to direct resources to local governments so that they might undertake new services and expand old ones, final legislation, however, did not include machinery to guarantee that this goal would be accomplished.

235. Civil No. 17,814 (N.D. Ga., filed March 15, 1973).

are willing to pay for them. In *Massell,* the City of Atlanta spend $4.5 million of federal revenue sharing funds on firemen's salaries, a priority item. At the same time, however, the City reduced the local input by a correlative amount and applied that amount to its water system, thereby permitting a $4.5 million water rate reduction. Plaintiffs then successfully brought a class action to enjoin Atlanta from implementing the scheme to use revenue-sharing funds to reduce water rates rather than provide new and expanded social services. The court held that Atlanta's action constituted a "sham" and enjoined its use of the $4.5 million local fund offset on a nonpriority item.[236] Beyond the issue of who should decide how Atlanta spends its tax dollars, the fact pattern reveals certain basic flaws in the present system of revenue sharing by which federal money is funneled directly to political subdivisions.

In this respect, existing methods of public finance, by which the political subdivisions of a state are often permitted to subsidize private services and are more frequently required to finance certain social services with significant spillover, result, as has been shown, in disparate service levels unrelated to need. Adding an increment of federal revenue-sharing funds to these existing disparities can only exacerbate the mismatching of needs and resources. From a policy viewpoint, since federal revenue-sharing funds are scarce, they should be directed to the area of greatest need, both in programatic and geographic terms, Since the present method of revenue sharing offers additional funds to wealthy subdivisions as well as poor subdivisions, to be devoted to any or all of the full range of priority items, this increment permits the wealthy districts to purchase frills, while the poor district may still be unable to meet basic community needs. Thus, while an Atlanta may reduce its water rates below cost and thereby grant a form of welfare-in-kind to its residents who are users of water, citizens in other areas of Georgia, who may be in as much need[237] of inexpensive water as those in Atlanta, cannot have it. The current approach to revenue sharing, while alleviating future pressure on local tax bases,

236. *Id.* By invoking Pub. L. No. 92-512, § 1222(a) as a substantive constraint on local fiscal decisions, the court ignored the Senate Finance Committee's policy warning:

> [S]ince the local governments are not required to maintain the level of their own prior expenditures in the high priority items . . . they could arrange to use the aid funds to increase their spending for other than high priority items. As a result, provision for the high priority categories, at best, is illusory.

S. REP. No. 92-1050, 92d Cong., 2d Sess. 16 (1972). By reading a substantive requirement into this section, the court has involved the judiciary in local decision making processes relating to purely local concerns. Also, while Atlanta attempted to subsidize water rates, a nonpriority item, there is no practical difference between that and subsidizing public transportation, a priority item; tax dollars from all over the country are used to reduce the rates of a local service.

237. *See* note 207 *supra.*

would not eliminate service and tax disparities for social services with significant spillover. Needs and resources would continue to be mismatched. Localities would continue to decide the level and quality of social services with statewide impact with the inevitable result of continued disparities arising from local wealth differentials.[238] In short, this overlay of federal aid on existing state-local relationships will only lessen for a time growing local tax pressures and will not in any way balance needs with resources.

An increased role for the state, particularly in the revenue raising and the planning phases, is the cornerstone of this Article's theme. The critical relationship is between the states and the federal government, and not that between the federal government and the political subdivisions of the states. Efforts on the part of the federal government to power equalize the thousands of political subdivisions through the infusion of revenue-sharing funds are apt to prove as futile as have state efforts at equalization of local property taxes to support education. Rather, in keeping with the overall federal scheme of government, the state should be the political entity to determine needs and allocate resources in coping with social services with significant spillover effect. Revenue sharing, then, should be confined to the state-federal relationship. The net effect of this approach would be a decreased policy-making role for the federal government, and an increased role for the states. Local governments should be left relatively autonomous with respect to the funding and administering of social services without significant spillover.

Finally, it should be emphasized that this increased role need not threaten traditional concepts of local control of many government services. First, having limited the local property tax to financing local social services, localities will be allowed to tax as they please without outside interference. Secondly, although the state must fund education

238. This issue is the crux of the SAP: social services with significant spillover must not be enriched at the local level. It is not possible to leave these kinds of services to localities or to permit them to define their own needs. Inevitably, regardless of the formula utilized, interdistrict disparities will arise depending on the relative wealth of the political subdivisions. The only means of eliminating these disparities depends upon implementation of the social equity approach (*see* text accompanying note 27 *supra*), by which local jurisdictions are forbidden from determining how much of these statewide services their own localities are to receive.

Permitting localities to subsidize private services has, in fact, already resulted in the waste of scarce resources. It has been shown that certain "wealthy" communities have used revenue-sharing funds to build ice rinks and bathhouses, to buy band uniforms and instruments, to remodel municipal golf courses, and to build municipal stadiums. Phila. Inquirer, Apr. 1, 1973, at 10–A, col. 1. These expenditures, seemingly on low-priority items, should be considered as direct costs against other high-priority expenditures. For example, all potholes in all city streets should be filled before incremental federal funds are used to subsidize golf courses. So long as federal revenue-sharing efforts fail to recognize this effect and fail to implement some variation of the social equity approach, the service disparity problem will persist.

and welfare, states may appropriately delegate much administrative decision making and allocation of priorities to the localities themselves. This need to preserve local discretion should, in fact, preoccupy policy-makers in their application of the social equity approach to revenue redistribution.

V. SOME CONCLUDING POLICY CONSIDERATIONS

It should be emphasized that the twin problems of service disparities and tax inequity are not solely the result of the property tax. These problems would persist, though in a slightly modified form, in the event either sales or income taxes were substituted for the present uses of the property tax. The problem is, in short, definition of which services are appropriately supported by a local tax base, and which ought to be supported by a state tax base. Therefore, the SAP focuses not on which tax base is used, but instead on how a given tax base is used. Its purpose is to match needs and resources and thereby eliminate waste and inefficiency. By making the financing of particular services co-extensive with their economic impact, waste and inequity can be significantly reduced.

Beyond the legal arguments concerning the use of the SAP, certain policy considerations involving continued use of the property tax are also relevant. Under the SAP, property taxation is only proper as long as service disparities among the various taxing jurisdictions are eliminated. Where a service must be provided equally statewide, the state should affirmatively equalize fiscal resources among the various subdivisions. This state responsibility, coupled with the *Weissinger v. Boswell*[239] opinion — calling for standardized assessment ratios guaranteed by the state — would require a new state presence and a new kind of uniform property tax.[240] This new court-compelled property tax appears, however, to apply only to statewide services, and not necessarily to municipalities concerned with local

239. 330 F. Supp. 615 (M.D. Ala. 1971).

240. This state presence could appear in any of a variety of forms. The state itself could centralize property tax assessment and collection in a single state agency with branch offices directly responsible to this central office. At the other extreme, the state could merely grant to some central office the power to oversee local administration of tax assessment and collection. Under the latter approach, the state would only intervene in local tax administration to correct serious abuses.

However, the courts are likely to be confronted by tax administration mechanisms designed to preserve local control and, therefore, create imbalances in assessment and collection procedures. Under the best of conditions, a 20 per cent variation in assessment is likely to exist between two properties of equal market value. D. NETZER, *supra* note 84, at 177-83. The less rigid the administration, or the greater local control of the state tax base, the greater the disparity among properties of equal value. However, guaranteeing enforcement of standardized state appraisal procedures would require the creation of an entirely new assessment and collection apparatus. Thus, the extent of reform in this area is likely to be determined by the courts' willingness to insist upon the creation of a system of tax administration geared to achieve "real" standardization.

needs. Under *Boswell,* twin property tax bases may continue to coexist. Local tax bases assessed at different ratios from other localities, but standardized within the particular subdivision, apparently do not violate the Constitution unless they are used to support a service which must be provided equally throughout the state.

Sound policy reasons counsel against use of a statewide property tax to finance statewide services. Although such a device may be necessary in the short term because of the difficulty of replacing existing property tax revenue with revenue of another sort, use of a statewide property tax should be viewed as only a transitional tax, ameliorating the effect of movement to total, nonproperty tax financing of statewide services. Among the problems involved, a statewide property tax would likely be unmanageable. A more important policy reason, however, is that use by the state of this tax base threatens its preemption from local use. The factors of tax incidence[241] — extent of shifting and exportation potential — establish very real, though intangible, constraints on how much property taxpayers in various political subdivisions throughout the state can or will pay. If the state preempts a sizeable portion of available property tax dollars, then local governments will suffer to the extent that they will be unable to raise sufficient revenue to meet their needs. The effect of a statewide property tax would be to pit the cities against the state in competition for scarce property tax dollars.

Since the underlying theory of the SAP is that the governmental unit bearing the economic impact of a service ought to manage and finance it, the spirit, if not the letter, of the SAP is violated by state preemption of the property tax base. Guaranteeing equalization at the state level of one social service, at the expense of denying an opportunity for localities to fund local social services according to need, is not an acceptable trade-off. As the inability of a number of localities to meet their local needs becomes apparent and political pressures for relief grow, some form of revenue sharing will, quite likely, be utilized by the state to appease the cities. Such a program will only result in subsidization of purely local services in such a way as to preclude a genuine definition of local needs.

Finally, problems involving the property tax and service disparities are similar in origin. One set of problems cannot be solved without solving the other. The difficult solution seems to require elimination or, at least, substantial reduction of the spillover of benefits and the uneven burden of taxes among the various political subdivisions

241. *See* notes 75–82 and accompanying text *supra.*

of the state. Once achieved through utilization of the SAP, the optimum role of the property tax in public finance can be put into perspective.

The property tax should be retained as the mainstay of local finance,[242] but only for financing local social services, those with no significant spillover effect. The property tax should not be used to finance either social services with significant spillover or private services. Local services may be financed, under the SAP, through the use of any tax base — property, sales, or income.

The strongest rationale for continued use of the property tax by local government centers upon the interrelationship between property owners, property, and local social services. Local social services, such as fire and police protection, are identified with the value of property and, therefore, the interests of property owners.[243] The level of each of these services contributes to property values in a more direct and immediate way than the level of these services affects either local income or sales. Property taxpayer-voters, then, may be more willing to pay for quality local services than would either income taxpayer-voters or sales taxpayer-voters. In fact, using the property tax as the prime support for these services gives property taxpayers a vested interest in maintaining quality public services. Furthermore, in a broad sense, these services are incidents of rent, or the total cost of all elements necessary for the use, enjoyment, and appreciation of property.[244]

Other policy justifications for continued use of the property tax include its ease of manageability by local governments. From an administrative standpoint, local governments already have machinery in existence to raise revenue from this tax source, whereas none exists

242. Professor Benson justifies continued intensive use of the property tax because it is uniquely suited to administration at the local level and provides a means to insure local independence and decentralization of government. *See* G. BENSON, THE AMERICAN PROPERTY TAX: ITS HISTORY, ADMINISTRATION, AND ECONOMIC IMPACT 1–10 (1965).

243. *See* notes 47–51 and accompanying text *supra*.

244. Site valuation would appear to be preferable to the present method of assessment by which improvements are assessed along with the value of the land itself. The new suggested role for the property tax envisions it more as an additional expense on the part of land owners to defray the cost of running certain local social programs necessary for the use and enjoyment of property than as a revenue source for redistributing income through a variety of social programs unrelated to property ownership. When viewed as such, a tax on the land itself, appears appropriate. For a thorough discussion of this as well as other aspects of site evaluation, *see* D. NETZER, *supra* note 84, at 197–212.

Another aspect of the advantage of assessing on the basis of site value is the manageability of this alternative as compared with the present system. *Id.* at 198–202. Rather than determining both the locational value of the land and the value of the improvements, only the first element need be considered. Moreover, while fluctuation does exist in the site value of land, such fluctuation is not as extreme as that of improvements. Thus, without discussing the economic effects of this theory of assessment, site valuation appears peculiarly suited to the new role for the property tax under the SAP *See also* F. MICHELMAN & I. SANDALOW, *supra* note 35, at 511–16.

for utilizing either sales or income taxes. There are, in short, no policy reasons against continued property taxation for predominantly local services, and several sound policy reasons for its continued use.

The suggested method of financing services and establishing tax equity as expressed in this Article is not novel. While the SAP is novel to the extent of its use as a legal doctrine, it is but an expression, in large part, of many of the policy views of the Advisory Commission on Intergovernmental Relations appearing in its study of State Aid to Local Government.[245] This analysis offers an alternative to the evolving legal and political approaches, as represented by the fundamental interest doctrine and revenue sharing, for solving intergovernmental financial problems. Hopefully, the SAP will contribute to the reworking, or at least refining of existing efforts to cope with modern problems of public finance.

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245. *See* notes 4, 26 & 91–92 *supra*.