THE EFFECT OF TAX AND SPENDING INITIATIVES ON THE LEVEL OF PUBLIC SERVICES

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The tax revolt which started in 1978 is a very interesting area. It involves our values as a society, our political system, our social structure, and how we institutionalize our responsibilities and relationships within our society. This is also a very good area for public policy education, because the press does a very poor job of looking at developments around the country in local and state finance. The press will occasionally report on initiatives on the ballot or about tax structure within one's own state, but generally they neglect to look at the issue nationwide.

One of the first things I'd like to do is look for criteria upon which to judge the behavior of local or state government. Let me read to you these criteria which I have found.

Two hundred and eight years ago, George Mason put into the Virginia Bill of Rights,

> Government is, or ought, to be instituted for the common benefit of the people, nation or community; of all the various modes and forms of government, that is best which is capable of producing the greatest degree of happiness and safety, and is most effectually secured against the danger of maladministration.

Eight years before, Voltaire said,

> In general, the art of government consists of taking as much money as possible from one class of citizens to give to the other.

As you can see, criteria used even 200 years ago varied a lot and provided no clear guidance on how to judge the performance of government.

Today, I would like to discuss what has been happening to government, and especially to state and local government's revenues, taxes, and services over the last six years — since the passage of Proposition 13 in California in June 1978. My purpose today is not so much to judge, but to describe and explain the events of the last six years.

The first tax revolt probably occurred in 1632 in Massachusetts. In that year, the settlers in Watertown were asked to contribute taxes to build fortifications for the city of Cambridge. As you might guess, they were quite upset about this, but Governor Winthrop of the Massachusetts Bay Colony convinced them that since they had just instituted taxation with representation in the Massachusetts Bay Colony, it was in fact their obligation to contribute these taxes. In 1630, the Massachusetts Bay Company had been changed from a commercial company into an elected assembly, and elective rights were extended to all free men who were members of the colony's Puritan churches.

Many of us may remember reading about the tax rebellion called Shay's Rebellion that took place in 1786 when our country was only a few years old. It consisted literally of an armed uprising against the collection of taxes and debts. Luckily, the rebellion ended with very little bloodshed and our country survived, though certainly it was one of the most serious tax revolts in the history of the United States. Over the past 200 years, there have been waves of tax revolt. Past revolts have been started over income taxes, property taxes, over just about all kinds of taxation issues. It sometimes helps to remember that the recent, and perhaps ongoing, tax revolt is really one in a continuing series of revolts in the history of the country.

It is also important to remember that each of our states has a separate social, political, and economic history, and the statistics which I'll be giving you later are averages over the whole country. It would, of course, be much better to look at the tax revolt in every applicable state, but this would take several days and not the hour that I have now. First, I'd like to set up a little context for the tax revolt which started with the Jarvis-Gann Proposition 13.

From World War II to the late 1970's, all developed noncommunist countries increased their public sectors' share of total GNP or GDP. Right now it ranges from 25 percent to 30 percent of the total economy in Japan and the United States all the way up to 45 percent to 50 percent of the economy in Sweden, Belgium, Norway, and Holland. In addition, it seems generally true that the richer the country is in per capita income, the larger is its public sector. There is not much in the literature that explains why this is so. What, in fact, determines the optimal size or level of the public sector in any given country? One hypothesis that I have formulated is that advanced developed societies need growing public sectors just to maintain acceptable income distribution levels. In the United States in the past few years, the public sector share of GNP has remained constant and the Gini coefficient (a measure of income equality) has indicated a decline in income equality. The evidence for any relationship between the two trends is slight, however, and merits further study.

Nationally, the last two administrations have campaigned with anti-public sector, anti-bureaucracy rhetoric, and it looks like a third national administration will win office this year with precisely the same rhetoric. We've seen these same tendencies in developed countries around the world. The recent election in Canada illustrates the rise of anti-public sector philosophy. Many European countries as well are trying to cut taxes and decrease spending in order to at least bring down growth of their public sectors.

Since World War II, state and local government expenditures have gone up three times as fast as the economy as a whole. Clearly, this trend had to eventually come to a halt, and in the late 1970's it did. The two forces probably most responsible for the tax revolt were very rapid inflation that started in the late 1960's and the decline and levelling off in real household income that began in the early 1970's. These were probably the two forces which, when combined with increasing local and state sector expenditures, provoked the tax revolt of the late 1970's.

What did happen in the late 1970's? What things really did change? During the period 1978-1982:

28 states reduced or restricted their property taxes,
15 states reduced income taxes,
10 states indexed income taxes,
7 states eliminated gift taxes, and
6 states repealed inheritance taxes.

In 1978, federal transfers to state and local governments were $231 per capita. By 1982, this had fallen to $174 per capita, and, in four years, state and local taxes per capita went down 14 percent. In some states, the decline was even greater. State and local taxation per capita went down 29 percent in California. Between 1978 and 1980 property taxes as a proportion of total revenue for state and local government fell from 43 percent to 35 percent of tax collections. And in the same two year period, fees and charges rose from 18 percent to 20 percent of tax collections [1].

The tax revolt did not hit all states with equal force. In three states especially, California, Idaho, and Massachusetts, quite severe property tax limitations were passed. In the four year period from 1978 to 1982, twelve initiatives designed to drastically cut property taxes were introduced onto state ballots. They all were quite severe property tax limitations. In only three states did these initiatives pass, and in all three states special circumstances existed. The first state to pass a property tax initiative was California where property taxes had been rising quite rapidly in recent years due to inflation in property values. As with other states, real household income was not going up, but remained about constant over the few years preceding Proposition 13. In addition, the state had a very, very large surplus which continued to increase and which the pro-tax revolt forces could claim could be used to relieve the property tax burden.

In Idaho, which passed a strong property tax initiative a few months after California did, tax rules had just been changed that would increase homeowner's property taxes. These recent changes in tax rules, which greatly increased property taxes, were enough to cause the property tax revolt to be successful.

In Massachusetts, property taxes had also gone up quite a bit in recent years. In addition, Massachusetts was a relatively high tax burden state, relying heavily on the property tax. In fact, the average property tax in the state at that time was 174 percent of the property tax in the rest of the country. Just the year before the initiative Proposition 2½ passed, property taxes had gone up by about 12 percent [7].

The political science literature is not absolutely certain as to what the forces were that caused property tax revolts to succeed in some states and not in others. It seems that some combination of the following three factors was responsible for the success of various tax revolts: (1) the overall tax load, (2) highly visible taxes, like property taxes, and (3) recent increases in visible taxes.

Tax revolts, like any political change, were not necessarily only about the economic level of taxation. Barbara Anderson, one of the leaders of the 1980 tax revolt in Massachusetts, said, "Our fight is not about money. It's about control. They have to learn, once and for all, that it's our government" [7]. You can see that there was a little bit of populist sentiment involved in this tax revolt as well.

What was the effect on service levels in local communities? Programs that had strong constituencies and strong political support were not hurt at all. Public safety, police and fire, for instance, stayed relatively the same in numbers of employees per thousand population. Generally, across the states, it was not police and fire services that were hurt as a result of the tax revolt, but rather services such as education, welfare, and health. The areas that truly suffered the largest cuts were park and recreation services, public works, overhead and general administration, capital projects of all kinds, maintenance, and analytic staff support of local and state government. The decrease in maintenance expenditures led to the writing of *America in Ruins* in 1981, a book that urged Congress and the various states to do something about our deteriorating infrastructure [2].

There has been a lot of talk about using volunteers to help replace lost personnel in local government services. There has also been a lot written about the privatization of public services, but most of the evidence is merely anecdotal. No hard numbers are available on how important these two tendencies have become since 1978. I suspect they have not been really all that important as replacements for lost public services around the country. Fees and charges have increased tremendously in many places around the country. In California in the three years from 1978 to 1981, the amount collected from fees and charges of all kinds went up 40 percent.

Income distribution, of course, has been affected as well. As the Urban Institute's new book, *The Reagan Record*, points out, the working poor especially have been hurt by the combined decreases and leveling off in public expenditures in the federal government as well as in state and local government [5]. There are also all kinds of unknown impacts on social and economic mobility resulting from the decreases in public sector programs.

The good news is that state and local government have survived, and that they have adjusted to the relatively severe cuts in public funding. They have survived by locating new sources of money, such as new taxes and new fees. In addition, special services and fringe programs had been cut — programs like summer school, adult education, and park maintenance. The political principle has been to minimize disruption and to maintain the status quo as much as possible, and to keep mainline programs in place. It has been an effort to try to utilize attrition and hiring freezes, as well as bookkeeping devices, to keep local government going. In addition, new taxes passed in 1981, 1982, 1983, and the economic recovery, which started then, have also been responsible for keeping local government going.

There has certainly been an effect on efficiency in government. There are a lot of stories and reports of government agencies becoming much more productive because of enforced cuts. We also found that in many communities we could get along without some of the marginal programs that previously existed. It's also true that, in some cases, our overall efficiency did drop. The cost of repairing cars was not really integrated into road maintenance procedures in order to arrive at an optimal road maintenance level. Cuts in lighting may have caused more crime. Cuts in social welfare may have caused more drug addiction and more crime. And our educational cuts may have reduced long-run productivity in ways that we can no longer measure at this time. To determine the lasting effects of the tax revolt, there was a state poll in 1983 that indicated that:

41 states had limitations on hiring,
37 states had engaged in program cuts,
32 states had restrictions on state employees' travel,
22 states still had plans to lay off workers,
14 states delayed employee payments, and
7 states put workers on unpaid leave.

Because of the economic recession around 1980 several states found themselves in deep economic trouble and, because of this, many passed new taxes. In 1981 and 1982, thirty-four states passed new taxes. And in 1983, thirty-eight states passed new taxes. These taxes consisted of:

16 states passed new or increased income taxes,
11 states increased their sales taxes,
13 states increased their business taxes,

13 states increased their cigarette taxes,
13 states increased alcohol and beverage taxes,
19 states increased motor fuel taxes, and
17 states increased or opposed miscellaneous taxes [3, p. 16–17].

State and local government did learn some lessons from the tax revolt. These were: (1) if there is a state or local government surplus, then most of this surplus should be shared with the taxpayers, (2) if new taxes are needed, first employ the sin taxes on alcohol, cigarettes, and gasoline; then impose business taxes; and, as a last resort, use taxes on the general voters, and (3) there is a tax revolt community out there that is quite well organized, that has interstate connections, and that knows how to use the mechanisms of government [3].

There are several state tax initiatives on the ballot this year. In November, 1984, Michigan will have an initiative to appeal all tax increases since 1981 and to provide for voter approval of any future tax increases. The state of Oregon has an initiative to restrict property taxes to 1½ percent of market value. Oregon has had similar initiatives on the ballot three times before and in close elections has defeated all three. California has another Jarvis initiative on the ballot which would "close the loopholes in Proposition 13." It would provide for a $1.6 billion property tax refund and would also require a two-thirds vote of the electorate for any new tax or fee increase in any tax district or special district. Massachusetts has an initiative which would eliminate the 7½ percent income tax surcharge its legislature recently passed.

What kinds of things can you put into a public policy program about issues such as tax initiatives? The most important element in a public policy program should be information on how the initiative will work and what the impacts will be on the various segments of the population. Then, a policy program could include taxation alternatives and the impacts they would have in the state. I think it is also relevant to include how your state compares with other states in the union in terms of tax collections and tax programs. I think it is also relevant to include information about how the United States compares with other developed noncommunist countries around the world.

So, where do we find ourselves now? Are we in a new era? Well, the answer is partially yes and partially no. Some things have changed and we are definitely no longer in the pre-1978 era — the golden age of state and local government. Probably due to the introduction of new, or increases in already existing, fees and charges, most of our public sector programs still exist. Senator Moynihan has said that June 6, 1978, when Proposition 13 passed, marked the end of the New Deal. I don't think things have changed that much, but it is true that the date did mark a break in state and local government tax philosophy that had existed since World War II. Because of the new taxes of 1983 and the economic upturn, state and local government in 1983 had a

$7 billion surplus across the United States. Of course, this was not an even surplus. Some states had much larger surpluses than others. But, in general, the financial status in state and local government has improved since the period 1978-1982.

I think the future very much depends upon whether we continue to make economic progress and see increases in real personal income, and on whether our public legislators have learned not to make the mistakes of the past.

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