

PROPERTY TAX OR SALES TAX? FUNDING TRANSIT INVESTMENTS IN SALT LAKE COUNTY

Local business and government leaders have been examining funding options for transit improvements in Salt Lake County. A property tax-funded bond is slated for the November ballot, but some have questioned whether a sales tax increase would be a better alternative. The Salt Lake Chamber asked Utah Foundation to analyze the potential impacts on businesses and households of a property tax increase compared to a sales tax increase.

These transit improvements would extend the Utah Transit Authority (UTA) TRAX light rail service to South Jordan, Draper, Salt Lake International Airport, and West Valley at a cost of around \$1.3 billion. Some of the costs would be funded through federal grants, and about \$900 million would need local funding. These TRAX extensions would be completed by 2015, and this is an acceleration of projects that were originally slated to be built over a longer time horizon. Community and business leaders have asked for consideration of such an accelerated timeline to avoid a near-tripling of traffic congestion predicted by 2030.

To accomplish this accelerated building schedule, local government leaders requested Salt Lake County to place a general obligation bond on the ballot for voter approval in November 2006. As is the norm with local general obligation bonds, this proposal would include an increase in county property tax rates to provide funds for bond debt service.

OVERVIEW

Comparing a property tax sufficient to service a \$900 million 30-year G.O. bond to a ¼-cent sales tax increase, either option would impose nearly the same aggregate tax burden on the business community. However, the business share of the overall tax burden is higher with the property tax than with the sales tax. For households, the sales tax imposes a significantly larger aggregate tax burden than the property tax.

Because household consumption is much larger in the aggregate than business consumption and the homeowner property base is much larger than business property, households would pay more than businesses under either tax scenario, even though the effective

property tax rate on businesses is nearly twice as high as the rate on homeowners.

Different types of businesses would be impacted differently by either tax. For example, a business with large property holdings but small taxable consumption, such as the owner of a commercial office tower, would see a much larger impact from the property tax.

The sales tax option provides the following advantages and disadvantages:

Advantages

- Greater taxpayer/voter support
- Revenue grows with economy
- Future revenue could be used for additional projects or operating costs
- Tourists share in the tax burden

Disadvantages

- High current sales tax burden, although the tax rate in Salt Lake County is low compared to other western cities
- Limited legal and political headroom
- Higher burden on households
- Non-deductible for household federal taxes

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The property tax option provides the following advantages and disadvantages:

Advantages

- Limited term and declining rate benefits taxpayers
- Authority to levy tax exists now
- Low current property tax burden
- Fairly equal division of aggregate tax burden between households and businesses
- Deductible on household federal tax returns

Disadvantages

- Debt proposed is close to county debt limit
- Lower taxpayer/voter support
- Minor tourist share in tax burden
- Does not grow with economy

Either option would generate revenues sufficient to build the projects proposed by UTA. Because of the desire (for simplicity's sake) to work with increments of ¼ cent on the sales tax, the sales tax increase would provide more revenue than the property tax proposal. The property tax option would generate a smaller revenue stream because the tax rate would decline each year as property values rise so that only what is needed for a predetermined debt service would be levied. The sales tax would increase each year as the economy grows and could allow debt to be retired more quickly. The property tax would sunset when the bonds are paid off, while the sales tax could continue in perpetuity to fund other capital projects or operating costs (although a sales tax authorization could be written with a sunset as well).

Which option is chosen depends on desired plans for future UTA infrastructure and services. If all that is needed is a limited-term revenue solely for capital projects, the property tax fits well. The fact that the authority to levy the tax already exists is a significant advantage. If an ongoing revenue stream for future projects or potential operating revenues is more attractive, the sales tax option may be worth pursuing. This effort could delay implementation, so the decision may also be affected by how urgent the timeline is for levying the tax and beginning construction.

PROPERTY TAX ALTERNATIVE

According to estimates from Zions Public Finance, this project could be financed with a series of four 30-year bonds totaling \$902 million. The debt service on these bonds would be financed by property tax rates that would vary by year as the bonds are issued in phases, with the full debt incurred by 2011. By the sixth year of bond payment, the debt service in this plan would peak at about \$58.5 million per year and remain at that level through year 30. As the value of property increases, the property tax rate required to service the debt payments decreases. The tax in 2012 would be about \$100 on a \$200,000 home and would decline in subsequent years. For business property, the tax would equal nearly \$91 for each \$100,000 of property value, or \$909 per \$1 million in property value.

PROPERTY TAX INCIDENCE ON BUSINESSES AND HOMEOWNERS

An examination of 2004 property tax data shows that in Salt Lake County, business properties account for about 43% of the assessed value of all property. This includes real property, such as land and buildings, and personal property, such as business equipment, boats and recreational vehicles. It also includes property that is centrally assessed by the state, such as utilities, pipelines, airlines, and mines.

Owner-occupied homes are provided a tax exemption of 45% of value, which results in business property being taxed at almost twice the effective rate of homeowner property. Currently, the homeowner's share of the property tax burden is about 57%. If the homeowners' exemption did not exist, the business share of property taxes would be about 30%, rather than the current 43% ratio, and homeowners would pay 70%, simply because there is much more homeowner property than business property in Salt Lake County.

Figure 1: Salt Lake County Assessed Values and Property Taxes Levied, 2004

Line	Class of Property	Assessed Value	Percent of Total	Property Tax	Percent of Total
1	Real Property	\$42,772,474,608	84.5%	\$633,021,124	84.6%
2	Primary Residential	26,870,601,388	53.1%	399,237,611	53.3%
3	Other Residential	1,565,270,250	3.1%	23,492,211	3.1%
4	Commercial & Industrial (Non Farmland Assessment Act)	14,280,623,800	28.2%	209,440,159	28.0%
5	(FAA) Agricultural	2,622,520	0.0%	34,470	0.0%
6	FAA Agricultural	53,356,650	0.1%	816,673	0.1%
7					
8	Personal Property	3,589,879,548	7.1%	52,718,038	7.0%
9	Mobile Homes for Primary Residence	74,534,771	0.1%	1,083,841	0.1%
10	Mobile Homes Non Primary Residence	5,485,380	0.0%	80,349	0.0%
11	Other Personal Property	3,509,859,397	6.9%	51,553,848	6.9%
12					
13	Centrally Assessed Property	3,053,401,531	6.0%	45,837,121	6.1%
14	Airlines	924,916,350	1.8%	14,012,511	1.9%
15	Other Transportation	58,496,747	0.1%	845,050	0.1%
16	Power	638,346,061	1.3%	9,564,415	1.3%
17	Telephone	1,091,895,959	2.2%	16,316,203	2.2%
18	Pipeline & Gas Utilities	339,746,414	0.7%	5,098,942	0.7%
19					
20	Natural Resources	1,183,716,773	2.3%	16,872,228	2.3%
21	Metal Mines	1,095,692,164	2.2%	15,557,310	2.1%
22	Sand & Gravel	87,176,662	0.2%	1,302,890	0.2%
23	Non-Metal Mines	847,947	0.0%	12,028	0.0%
24					
25	TOTAL	\$50,599,472,460	100.0%	\$748,448,511	100.0%
26					
27	Household Property (Lines 2, 3, 9 & 10)	\$28,515,891,789	56.4%	\$423,894,012	56.6%
28	Business Property (All other lines)	\$22,083,580,671	43.6%	\$324,554,499	43.4%

Source: Utah State Tax Commission data from "Utah Property Tax: 2004 Annual Statistical Report."

Figure 2: Examples of Property Tax Increases on Business Taxpayers

Business Type	Property Value	Property Tax*	New Bond Prop. Tax**	% Tax Increase
Car dealership	\$7,380,100	\$85,469	\$6,709	7.8%
Retail "supercenter"	12,804,800	191,099	11,640	6.1%
Retail grocery store	2,655,000	35,231	2,413	6.9%
Large office building	55,557,400	829,138	50,502	6.1%
Small office building	2,297,500	34,287	2,088	6.1%
Bank branch	686,800	8,673	624	7.2%
Large hotel	28,994,000	432,706	26,356	6.1%
Motel	2,056,600	30,693	1,869	6.1%
Medium manufacturer	15,635,400	230,653	14,213	6.2%
Small manufacturer	5,432,500	69,585	4,938	7.1%

*Value and tax are from 2005 property tax statistics.

** Assumes highest property tax increment from G.O. Bond (.000909) if it were in place in 2005.

Sources: Salt Lake County Assessor (www.slpropertyinfo.org), with calculations by Utah Foundation.

EXAMPLES OF PROPERTY TAX INCREASES

To better illustrate the impact of the property tax increase required to service these bonds, some examples of business taxpayers were obtained through a county database. Obviously, the largest tax increases, in absolute dollars, would fall on companies with large amounts of property, such as a downtown high-rise office building owner or a large hotel. As a percentage of current property taxes, each of these businesses would experience an increase of about six to eight percent. The differences in the percentage tax increase are merely a reflection of how high the current tax rate is on these companies.

Currently, Utah's property tax is low compared to other states. In 2004, when Utah Foundation last performed a ranking on state and local taxes, Utah's property tax burden as a percent of personal income was lower than 35 other states.

SALES TAX ALTERNATIVE

Instead of raising property taxes and issuing general obligation bonds, these TRAX projects could be funded by raising the Salt Lake County sales tax rate by ¼ cent. The county could issue bonds based on the sales tax revenue stream. Revenues from a ¼-cent sales tax would exceed the revenues from the proposed property tax.

A new sales tax for transit projects would not necessarily sunset as the property tax for a G.O. bond would. However, policymakers could choose to place a sunset date on the sales tax increment.

SALES TAX INCIDENCE ON BUSINESSES AND HOUSEHOLDS

The Utah State Tax Commission estimates that businesses pay 31 percent of the total general sales tax in Utah. This calculation does

Figure 4: Sales Tax Rates in the Largest City of Each Western State

City and State	Combined Sales Tax Rate
Seattle, Washington	8.800%
Los Angeles, California	8.250%
Phoenix, Arizona	8.100%
Las Vegas, Nevada	7.750%
Denver, Colorado	7.600%
Albuquerque, New Mexico	6.875%
Salt Lake City, Utah	6.600%
Boise, Idaho	6.000%
Cheyenne, Wyoming	6.000%

Sources: City and state departments of revenue and Utah State Tax Commission.

not refer to the sales tax that is passed on to customers at the cash register, but it is sales taxes on items a business consumes for its own use or taxes on equipment a business purchases for its operations. Figure 3 shows how the Tax Commission estimates the incidence of general sales taxes by type of good purchased. These data only provide information about the types of goods and services purchased, and data are not available to describe how this tax impacts different business sectors as consumers of these goods and services. Therefore, we cannot estimate how a sales tax increase would affect manufacturers versus commercial building owners or other types of businesses as we did with the property tax information earlier.

Nevertheless, we can make some comment about the types of businesses highly impacted by a sales tax increase. Those businesses that purchase very expensive equipment on a regular basis would be significantly impacted. This could include manufacturers, especially high-tech manufacturers, whose equipment can become outdated in a short period, requiring frequent investment. Companies that operate large fleets of automobiles would also face a significant sales tax bill for purchases of vehicles.

Utah's sales tax burden ranked higher than all but eight states when Utah Foundation last analyzed tax burdens. But this is not to say that Utah's sales tax rates are out of line with other states; rather, the sales tax base is broader than in many states because Utah taxes all food. This will change if food for home consumption is eventually exempted from taxation as has been begun with legislation passed this year to phase out the food tax.

To place Utah sales tax rates in context, Figure 4 shows combined state and local sales tax rates in the largest city of each of the western states that have a sales tax. Salt Lake City ranks low, at seventh among the nine cities.

COMPARISON OF PROPERTY AND SALES TAX IMPACTS ON BUSINESSES AND HOUSEHOLDS

Figure 5 shows projected revenues from either a ¼-cent sales tax or the varying property tax rates needed to support a \$900 million G.O. bond in Salt Lake County. This chart assumes a sales tax would not be implemented until 2008. In terms of total dollars paid, the sales tax and the property tax carry a similar burden for the business community. For households, however, the property tax imposes a lower total burden than the sales tax. In either case, households would pay more than businesses in the

Figure 3: Salt Lake County Taxable Sales by Economic Sector, 2005

Major Economic Sector	Gross Sales 2005*	Household Share**	Household Sales 2005	Business Sales 2005
Agriculture, Forestry & Fishing	\$28,684,551	5.0%	\$1,434,228	\$27,250,323
Mining	88,033,712	1.0%	880,337	87,153,375
Construction	205,994,647	66.7%	137,398,430	68,596,217
Manufacturing	879,567,562	8.0%	70,365,405	809,202,157
Transportation	67,964,271	5.0%	3,398,214	64,566,057
Communications	686,337,049	55.0%	377,485,377	308,851,672
Electric & Gas	716,897,287	55.0%	394,293,508	322,603,779
Wholesale - Durable Goods	2,033,507,472	40.0%	813,402,989	1,220,104,483
Wholesale - Nondurables	395,425,869	40.0%	158,170,348	237,255,521
Retail - Building & Garden	888,584,862	68.0%	604,237,706	284,347,156
Retail - General Merchandise	1,745,424,995	90.0%	1,570,882,496	174,542,500
Retail - Food Stores	1,404,135,013	95.0%	1,333,928,262	70,206,751
Retail - Motor Vehicles	1,995,844,197	75.0%	1,496,883,148	498,961,049
Retail - Apparel & Accessories	510,464,132	92.0%	469,627,001	40,837,131
Retail - Furniture	925,653,826	84.0%	777,549,214	148,104,612
Retail - Eating & Drinking	181,309,743	80.0%	945,047,794	236,261,949
Retail - Miscellaneous	1,273,372,632	91.0%	1,158,769,095	114,603,537
Finance, Insurance & Real Estate	195,090,647	66.7%	130,125,462	64,965,185
Services - Hotel & Lodging	347,989,509	20.0%	69,597,902	278,391,607
Services - Personal	117,389,071	90.0%	105,650,164	11,738,907
Services - Business	676,142,043	33.3%	225,155,300	450,986,743
Services - Auto & Repair	615,193,558	60.0%	369,116,135	246,077,423
Services - Amusement & Rec	334,544,448	66.7%	223,141,147	111,403,301
Services - Health	53,646,619	60.0%	32,187,971	21,458,648
Services - Education	127,545,084	90.0%	114,790,576	12,754,508
Public Administration	41,127,028	66.7%	27,431,728	13,695,300
Private Motor Vehicle Sales	202,498,291	80.0%	161,998,633	40,499,658
Occasional Retail Sales	38,110,286	75.0%	28,582,715	9,527,572
Nondisclosable / Nonclassifiable	7,233,287	50.0%	3,616,644	3,616,644
Total Taxable Sales	\$17,783,711,694		\$11,805,147,925	\$5,978,563,766
Total Household / Business Share			66.4%	33.6%

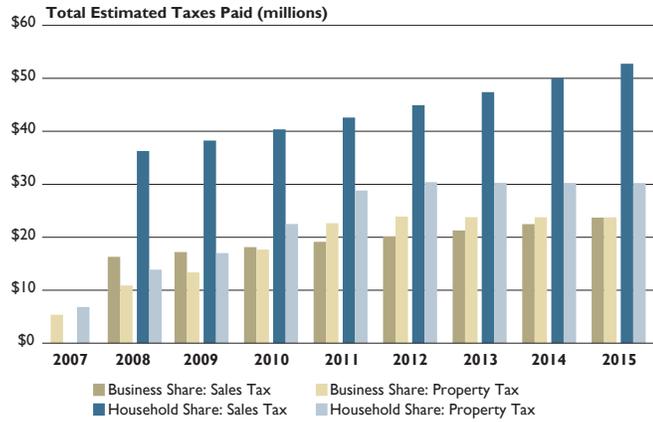
* Compiled from Utah State Tax Commission quarterly reports for 2005.

** Estimates of household share of sales tax burden by Utah State Tax Commission in "Western States' Tax Burdens Fiscal Year 1997-98."

aggregate because household property holdings are larger than business property holdings and household consumption is larger than business consumption. For individual households, however, the effective property tax rate is significantly lower than for a

business, since homeowners receive a 45 percent exemption of value for their primary residence.

Figure 5: Business and Household Impacts of Sales and Property Tax Increases for Transit



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