

Is Proposition 13 to Blame for California's Fiscal Crisis?

By Jason Clemens and Jon Coupal

When California voters approved Proposition 13 by a landslide in 1978 they launched a nationwide revolt for lower taxes. Critics now blame that revolt for our current fiscal crisis. That charge needs to be considered in the light of actual data about property taxes in California.

Prop 13 limits property taxes to 1 percent of the cash value of property or the market value of a property depending on when it was purchased, with subsequent annual increases limited to 2 percent. Prop 13 also imposes a two-thirds majority requirement on the state legislature for increasing taxes — either by increasing rates or changing the way taxes are calculated.

These provisions have caused Senator Barbara Boxer, Nobel economist Paul Krugman, and a cadre of pundits to cry foul. The standard story is that these restrictions (a) force the state to rely more heavily on other taxes like personal income taxes because it can't raise enough from property taxes, and (b) they prevent the legislature from raising taxes even in times of crisis. The actual tax data tell a different story.

First, the limits imposed on property taxes by Prop 13 no doubt delivered benefits to homeowners for more than three decades. That relief, however, was mitigated when housing prices began to eclipse income gains early this decade. The run-up in housing prices and the accordant increase in property tax assessments for those purchasing homes post-2000 meant huge revenue gains for government. Any Californian who purchased a home in the last decade knows full well the burden property taxes place on their personal finances. Indeed, according to the latest census data, California ranks 19th in terms of the aggregate level of disposable income required to pay property taxes.

Boxer, Krugman and company are fundamentally mistaken when they argue that the state relies less on property taxes because of Prop 13 compared to other states. Again, census data indicates that California ranks ninth-highest for its reliance on property taxes. Put differently, a full 41 states rely less on property taxes than California.

Specifically, local governments in California collect a little over one-third (34.3 percent) of their revenues from property taxes. Alabama, which ranks first, collects 44.4 percent of its revenues from property taxes. Contrast this reliance to some of California's neighbors: Arizona 36.4 percent, Nevada 34.8 percent, and Utah 38.8 percent. This refutes the notion that California is a low property tax state and that Prop 13 has skewed the overall revenue mix in some bizarre manner.

California's heavy reliance on personal income taxes—10th highest of the 50 states—simply cannot be a function of our light use of property taxes. Further, our heavy use of property taxes and personal income taxes hasn't meant low taxes in other areas; we have a fairly high corporate income tax rate and the highest state sales tax rate in the country. These high personal income, corporate income, and sales tax rates dismantle another popular assertion of Prop 13 opponents.

They charge that the measure impedes the state government from implementing budgets, even in times of crisis. What the data actually show is that the state government and their local counterparts

have had very little trouble raising taxes to the point of being markedly uncompetitive and dangerously eroding the incentives for work effort, savings, investment, and entrepreneurship. These form the bedrock of a prosperous economy, now little in evidence.

The state's budget crisis has continued unabated despite the many so-called fixes of the past two years. The state's Legislative Analyst's Office recently estimated that the state is facing a \$20.7 billion shortfall. The state's bond rating was already the lowest in the country when Standard and Poor recently reduced it again.

Blaming these fiscal woes on a lack of revenue because of Prop 13 makes for an easy sound bite, but the charge is factually baseless and counterproductive. To overcome our current crisis, California needs a serious debate on solutions, based on actual tax data, not on urban legend and rhetoric.

<> Jason Clemens is the director of research and the coordinator of the California Prosperity Project at the Pacific Research Institute (www.pacificresearch.org) and Jon Coupal is the president of the Howard Jarvis Taxpayers Association (www.hjta.org).