Iowa Fiscal Partnership

BACKGROUNDER

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Iowa's Problem of Priorities

Costly Business Property Tax Cut Excessive — Hurts Family, Kids' Services

Tax cuts have consequences. In the case of the massive commercial property tax cut enacted two years ago, those consequences have become all too real.

Iowa's economy continues to rebound and state revenues are projected to rise nearly 5 percent next year, yet we find ourselves struggling to finance our most important basic services, like education. Why? Because we are giving away most of the increased revenue to commercial property owners, with no public benefit to show for it.

The commercial property tax cut will result in an estimated $277 million hit to the state budget next fiscal year, more than double this year's cost as provisions phase in.[1] This means that the property tax cuts will consume 82 percent of the estimated $338 million in increased state revenue.[2] The small amount remaining is far too little to cover even the normal increases in the cost of providing public services due to inflation.

While the legislation has been sold as a general property tax cut, only 11 percent of the property tax reductions will flow to residential and agricultural property owners next year.[3] The rest goes to owners of commercial property, apartment buildings, industrial facilities, railroads and utilities.

The legislation has two major provisions. A Business Property Tax Credit is entirely state funded and is of more benefit to owners of small properties, since the maximum value of the credit represents a larger share of their taxes. The most costly provision reduces the assessed value of commercial and industrial property to 90 percent of actual value, with the state reimbursing localities for the resulting revenue lost.[4] This provision lavishes the majority of its benefits on large property owners.

About $5 million will flow next year to the 11 largest big-box retailers, none of them Iowa companies.[5] While this is real money flowing out of the Iowa treasury, a few hundred thousand a year to the likes of Wal-Mart or Target is of little import to them, and will have no effect on their decisions to build in Iowa, which are driven by the size of the consumer market here. There was never a case for commercial tax reductions; overall business tax levels in Iowa for a long time have been below the national average — a point you rarely hear, and never from the business lobby.[6]

What exactly are the consequences?

The cost of running schools will keep rising faster than state aid, resulting in layoffs, increased class sizes, program reductions, and more years of outdated textbooks.

The Governor's budget proposes sizable cuts to state health care programs and requires state agencies to finance salary increases by reducing staff, thus reducing state services.

Once again we will not expand the state's preschool program for 4-year-olds, a measure that has been shown to be an effective economic development tool yet fails to help many low-wage workers needing full-time preschool.

Our child care assistance program, with one of the lowest income cutoffs in the country, will keep penalizing families for earning more. Bi-partisan support for funding to improve water quality and expand access to mental health care will likely be for naught.

We have a problem of priorities. We keep underfunding services for average Iowa families — education, health, work supports, natural resources — in order to finance massive tax reductions to businesses that don't need it. And we spend in excess of $350 million each year on business tax credits that continue on autopilot, with no sunset, despite the state's own analyses that fail to find evidence of appreciable benefit to the state from some of the largest of these subsidies.[7]

It is time to admit that the tax cuts enacted in 2013 were excessive, and are causing long term damage to the state. At the very least, the $50 million increase in the business property tax credit portion of those tax cuts scheduled for next year should be delayed or eliminated.

But that is not enough. There should be a moratorium on any further tax cuts or tax credits. All business tax credits should be subject to effective caps and sunsets to force a serious evaluation.

Without such measures, we will continue down the road of tax-cutting our way to mediocrity and shortchanging our children's future.

A shorter version of this piece has appeared as a guest opinion by Peter Fisher, Research Director of the Iowa Policy Project, in The Des Moines Register on March 6, 2015. The Iowa Fiscal Partnership is a joint public policy analysis initiative of two nonpartisan, nonprofit Iowa-based organizations, the Iowa Policy Project and the Child & Family Policy Center. Reports are at www.iowafiscal.org.

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[1] The Legislative Service Agency projects that general fund appropriations resulting from the property tax legislation will total $277.1 million for FY2016: $162 million to replace local revenue lost because the bill reduced commercial and industrial assessments to 90 percent of actual value, $14.9 million in state foundation aid to schools triggered by the reduction in assessed value, and $100 million for the business property tax credit. LSA, Fiscal Services Division, *Summary of FY 2016 Budget andDepartment Requests*, December 8, 2014, page 53. https://www.legis.iowa.gov/docs/publications/LADR/435197.pdf

[2] The $338 million represents the increase in state's net receipts plus transfers, according to the Revenue Estimating Conference, Dec. 12, 2014. http://www.dom.state.ia.us/state/files/FY15/December2014.pdf A new forecast by the REC will be released in mid-March.

[3] Legislative Services Agency, Fiscal Note on SF 295, May 22, 2013. https://www.legis.iowa.gov/DOCS/FiscalNotes/85_1464SVv2_FN.pdf

[4] The state promised to reimburse these losses fully only through FY 2017; after that, local governments will be on the hook for an increasing portion of the lost revenue. In addition, the state is not reimbursing localities for any of the revenue lost from a third provision that reduces the assessed value of residential rental property.

[5] Estimate based on January 2012 taxable values and the statewide average property tax rate on commercial property of 3.77 percent for FY2015. The 11, in order by 2012 valuation statewide and with the location of the corporate headquarters, are Wal-Mart (AR), Target (MN), Menard's (WI), Lowe's (NC), Walgreen's (IL), Kohl's (WI), Younkers (PA), Home Depot (GA), K-Mart (IL), Best Buy (MN), and Sears (IL). The 11 had $1.33 billion in taxable valuation, so that the reduction to 90 percent for January 2014 values amounts to $133 million, assuming valuations before the reduction remained about the same.

[6] *Iowa: Where Business Taxes are Low*. Iowa Fiscal Partnership, March 5, 2014. http://www.iowafiscal.org/iowa-where-business-taxes-are-low/

[7] Iowa Department of Revenue, Contingent Liabilities Report, December 2014 https://tax.iowa.gov/sites/files/idr/Contingent%20Liabilities%20Report%201214.pdf. For evaluations of tax credits by the Iowa Department of Revenue see https://tax.iowa.gov/report/Evaluations?combine=Study; also of note is the *State of Iowa Tax Credit Review Report*, prepared by the Governor's Tax Credit Review Committee, January, 2010. http://www.dom.state.ia.us/tax_credit_review/files/TaxCreditStudyReviewReportFINAL1_8_2010.pdf