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REPORT

ON

MODEL SALES TAX

The Committee:

FOR THE MINORITY: Gaulda Hahn

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MODEL SALES TAX
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REPORT ON
MODEL SALES TAX

To The Board of Governors,
City Club of Portland:

INTRODUCTION

As an outgrowth of the March 12, 1984, City Club Report on Oregon's Tax System, the Board of Governors established a study committee in May, 1984, and charged it to:

"...draft a model sales tax proposal designed to achieve the tax goals expressed in the City Club's Report on Oregon's Tax System, and which has a strong chance of being enacted into law."

The 1984 tax report found that the overall level of Oregon's state and local taxes is not excessive when compared to other states, ranking near the middle in total per capita state and local taxes. However, Oregon differs significantly from other states in its relative reliance upon certain types of taxes. In 1979-81 Oregon was second nationally in per capita personal income tax collected. In 1982, Oregon ranked 12th nationally in per capita property taxes. On the other hand, Oregon is one of only five states without a general retail sales tax. See Table 1 for state-by-state comparison of taxes.

In the past, the 1984 tax study found, Oregon's taxing system has served its citizens adequately. It is one of the more progressive in the country, and it appears to be fairly and efficiently administered. However, the report concluded, the economic and political context has changed, and Oregon now needs property tax relief. Public education depends too heavily on the property tax and the present educational system cannot be maintained unless this dependency is reduced. In addition, the existing climate of uncertainty and the potential for passage of an initiative severely limiting property tax rates affects the health and growth of the Oregon economy. It is not feasible for Oregon to reduce either property taxes or personal income taxes significantly by increasing reliance on other existing taxes. Therefore, another revenue source is needed.

The Majority's recommendations, adopted by the membership of the City Club, included: (1) the state should enact a broad-based retail sales tax covering goods and services as the best means available to fund property tax relief; (2) if property tax relief is enacted, the remnants of the former 30 percent property tax relief program should be eliminated; and (3) the personal income tax, which is among the highest in the nation, should not be increased, but sales tax revenue should be used to reduce the income tax only if the net effect of all changes would not make the system more regressive.

Recommendations of the Majority in this report vary from recommendations in the Report on Oregon's Tax System in three respects. First, the Majority recommends exempting services from the sales tax. Second, the Majority recommends retention of the 30 percent property tax relief program. Third, the Majority recommends that a portion of sales tax revenue be dedi-
cated to personal income tax relief. Clearly, this would result in lowering the direct tax burden on individuals when compared to business. Nevertheless, this recommendation has been made by the Majority without a specific determination that the net effect of the overall sales tax proposal would not make the tax system more regressive. Because a sales tax is inherently regressive, the Majority does recommend rebates for low-income residents, exemptions from sales tax and retention of existing real property tax relief programs to reduce regressivity.

As a follow up to the report on Oregon's Tax System, this report is intended to serve two purposes. First, it provides background information needed to evaluate sales tax proposals. Second, it recommends specific features which should be included in any sales tax package referred by the Legislature to Oregon voters.

One aspect of sales taxation beyond the scope of this report is the formula by which sales tax revenues should be distributed to local governments and school districts. Structuring the formula will be a complex task for the legislature.

I. BACKGROUND

A. History of Sales Tax in the United States.

The sales tax is a recent development in public finance in the United States. The first sales tax was adopted by Mississippi in 1932. Twenty-three other states and the District of Columbia followed suit during the Great Depression. Since World War II, 21 more states have adopted the sales tax, bringing the total to 45 states and the District of Columbia.

B. Recent Sales Tax and Real Property Tax Limitation Proposals in Oregon

1. 1969 Sales Tax Ballot Measure. Oregonians voted on a sales tax most recently at a June 3, 1969 special election. The measure called for a 3 percent tax aimed at raising $100 million annually to offset property taxes. Proposed exemptions to the sales tax included food, prescription drugs, feed, seed, fertilizer, services and labor, cigarettes, gasoline, and property used or consumed in industrial processing. A Portland City Club committee opposed the measure on grounds that it provided no substantial additional revenue and it was not clear that relief from property tax would be distributed equitably. The voters defeated the measure by a ratio of about 8 to 1.

2. 1983 Legislative Sales Tax Proposals. Two major sales tax proposals were introduced and considered during the 1983 general and special legislative sessions. HJR 34, containing constitutional provisions, and HB 2001, containing statutory implementing provisions, were sponsored by Representatives Peter Courtney and Tony Van Vliet. They provided a 4 percent sales tax on all goods and services, exempting medical and hospital services, food, prescription drugs, utilities, livestock, feed, seed, fertilizer, pesticides and raw ingredients used in the manufacture of a product. This package failed to receive sufficient votes in the House Revenue Committee and was never voted on by the House. The House Revenue Committee was also unable to approve any other sales tax proposal.
In response to inaction of the House Revenue Committee, the Speaker of the House appointed the Select Committee on Property Tax Relief in mid-session to consider a sales tax bill. The committee reported out HB 3019 and HJR 37. These two measures, containing constitutional amendments and detailed statutory provisions, also imposed a 4 percent sales tax on the sales of goods and services subject to exemptions similar to those in HJR 34 and HB 2001. In addition, they imposed a limitation on state and local government expenditures.

These two measures passed the House of Representatives in June of 1983 but failed to pass in the Senate. Thus, the regular session of the Legislature adjourned without approving a sales tax bill.

A special legislative session was held from September 14 to October 4, 1983. It passed HB 3026 and SJR 30 which were substantially the same as HB 3019 and HJR 37, with one exception. SJR 30 required that separate majorities of the governing bodies of the school districts, cities and counties in the state request the Secretary of State to place the sales tax proposal on the statewide ballot before a vote of the people could be held.

The constitutionality of SJR 30 was challenged by a group of legislators. On February 1, 1984, the Oregon Supreme Court ruled that the procedure requiring a majority of local governmental entities to approve the submission of the constitutional amendment violated Article XVII, Section 1, of the Oregon Constitution. That Article empowers the Legislature to submit proposed constitutional amendments to the voters for approval. The Supreme Court held that this legislative power could not be delegated to local governmental entities by requiring their ratification.

Shortly after the Oregon Supreme Court issued its opinion, a group representing business interests, Taxpayers for a Better Economy (TBE), attempted to gather signatures to put a sales tax proposal on the November ballot. The TBE proposal called for a sales tax of 5 percent on retail goods only and proposed a strict spending limitation on the state and local governmental entities. TBE supporters were unable to gather sufficient signatures by the deadline in July and no sales tax proposal was on the November, 1984, general election ballot.

3. Recent Real Property Tax Limitation Measures. Since 1968, measures to limit or to reduce property taxes have been placed on six of the last nine general election ballots by initiative petition. See summary in Table 2. All six measures were defeated. But the margin of defeat in the two most recent elections was extremely narrow. The vote in 1982 was 504,836 in favor and 515,626 against, for a margin of 1.06 percent. In November 1984, the margin was 1.38 percent, with 599,424 votes in favor and 616,252 against.

C. Tax Revenues and Spending Under Existing Oregon Law.

The 1984 City Club Report on Oregon's Tax System explains Oregon's present system of taxation in detail. However, a brief review of certain aspects of Oregon's system is necessary for an understanding of sales tax proposals.
1. Revenue Sources and Spending at State Level.

a. State Revenues. The state estimates that total state revenue for 1983-85 will be $12,916.2 million, of which $3,191.0 million will go into the General Fund. The remaining $9,725.2 million will be dedicated to specific uses not relevant to this report such as bonded construction, federally funded programs and the retirement system.

Of the $3,191.0 million General Fund revenues, $2,462.0 million (or 77.2 percent) will come from personal income taxes and $292.0 million (or 9.2 percent) will come from corporate income taxes.

Under existing law, Oregon personal income tax rates run from 4 percent, to a high of 10 percent for all taxable income in excess of $5,000 on a single return or $10,000 on a joint return. (For certain years through 1984 the rates ran from 4.2 percent to 10.8 percent because of a temporary 8 percent surcharge). Oregon’s per capita personal income tax is among the highest in the country. This is because of Oregon’s relatively high rate structure and relatively low income level at which a taxpayer reaches the maximum rate.

The Oregon corporate income tax rate is a flat 7.5 percent. In 1980 Oregon had the 13th highest corporate income tax per capita in the country.

b. Use of General Fund Revenues. For 1983-85, out of General Fund revenues estimated to be $3,191.0 million, the following amounts will be paid to fund primary and secondary education (which would otherwise be lost to school districts or funded by property taxes), and for direct property tax relief:

1. $880 million for Basic School Support.
2. $236 million for real property tax relief under the 30 percent property tax relief program described below.
3. $175 million for real property tax relief under the homeowners and renters refund program (HARRP).

Additionally, for 1985-87, approximately $28 million will be paid out of the General Fund for the elderly property tax deferral program (which for 1983-85 is funded from other sources).

2. Revenue Sources at Local Level. Local governmental entities include counties, cities, school districts, and special districts of various types such as water districts. Each entity has its own sources of funding and its own budget for spending. Sources of funding relevant to consideration of a sales tax are discussed below.

a. Real Property Tax. Under Oregon law, each local taxing district has a "tax base." This is the dollar amount the district may spend, from property tax dollars, for the year in question. Under the Oregon Constitution, a permanent tax base may increase by only 6 percent per year without voter approval. Additionally, voters can approve (1) a larger permanent tax base, (2) a "special" levy for one year, or (3) a "serial" levy for more than one year.
Each year, for each taxing district, a tax rate is computed by dividing the tax base by the assessed value of all taxable property in the district. Taxable property includes non-exempt real property and certain business personal property. For example, if a school district has a tax base of $150,000 for the year, and taxable property with an assessed value of $10,000,000, the tax rate will be 1.5 percent or $15 per $1,000 of assessed valuation.

Statewide, the average consolidated property tax rate is $20.79 per $1,000 of assessed value. On an individual county level, for fiscal year 1983-84, property tax rates varied from a low of $11.40 per $1,000 in Curry County to a high of $28.54 per $1,000 in Sherman County.

Dependence on the real property tax as a source of revenue varies greatly among the four categories of local governmental entities. Whereas in 1982-83 school districts received 47.1 percent of their total operating revenue from property taxes, counties received only 19.8 percent.

On a statewide basis, of all real property taxes collected from 1976 to 1982, approximately 68 percent went to school districts and the remaining 32 percent to cities, counties and special districts. Thus, public concern over the level of property tax is, to a large extent, concern over local funding of school districts.

b. Timber Tax. Oregon imposes a severance tax on private timber at the time it is cut. In recent years this has generated approximately $50 million per year, of which approximately 97 percent is paid to local governments. However, in 1983-84, due to a weak forest products market, collections dropped to $25.5 million.

c. Basic School Support. In 1983-85, out of estimated General Fund revenues of $3,191 million, $880 million will be paid for Basic School Support to primary and secondary school districts based on a statutory formula. On a statewide basis, Basic School Support will provide 31.3 percent of the operating funds used by school districts. These income tax dollars are a direct substitute for property tax dollars to fund local schools.

d. Other Sources. Local taxing districts also receive substantial revenues from timber sales on federal lands, profits from state forest lands, and miscellaneous fees and taxes. See City Club Report on Oregon's Tax System.


a. Homeowners and Renters Refund Program (HARRP). A 1971 law provides a property tax refund for each homeowner and renter with a household income of less than $17,500 per year. The amount of relief is graduated based on income, with $750 being the maximum relief available to a homeowner and $375 being the maximum relief available to a renter. During 1983-84, the HARRP program resulted in payments of $78.3 million to homeowners and renters.

b. The 30 Percent Property Tax Relief Program. In 1979 an Oregon law (referred to as the 30 percent property tax relief program in this report) was enacted to provide a payment of up to 30 percent of property taxes levied against owner-occupied principal residences. Renters were also provided relief. The 1979 legislation called for a maximum payment of $800.
By statute the maximum payment has been reduced to $192 for homeowners and $96 for renters for 1983-85. Appropriations by the 1983 Legislature for these programs, however, further reduced these figures to $170 and $85 respectively. The total relief available in 1983-85 is an estimated $236 millions, of which approximately $43 million will be paid out for renters' relief.

c. Senior Citizen Homestead Deferral Program. Under current law, an eligible senior citizen may defer payment of real property taxes assessed against a homestead (principal residence). The resulting debt, plus 6 percent interest, is repaid on the death of the citizen or the sale of the property, whichever occurs first. In 1982, state funding for this program was $9.7 million and the cumulative amount owed by senior citizens was $23 million.

D. Current Political Climate.

At the time of this report, a sales tax has widespread support from political leaders and numerous interest groups as a means to reduce property taxes and stabilize the source of funding for local schools. It appears likely that the 1985 Legislature will refer a sales tax package to the voters in an election to be held in either the spring or fall of 1985.

Whether the citizens of Oregon will vote in favor of a sales tax is far less certain. Responding to a statewide poll taken between January 7 and 10, 1985, by the survey firm of Bardsley & Haslacher for The Oregonian, 49 percent of adult Oregonians interviewed said they would oppose a 5 percent sales tax dedicated to relieving property taxes. Forty-two percent said they would favor it, and 9 percent were undecided. Asked how they would view a sales tax that would also reduce income tax but offer less property tax relief, 32 percent said they would favor it, 57 percent said they would oppose it, and 11 percent were undecided.

A significant recent development is Governor Vic Atiyeh's strong support for a sales tax. Historically an opponent of the sales tax, Atiyeh announced in early December, 1984, a far-reaching tax proposal which would include a retail sales tax with revenues dedicated entirely to support public education. (See discussion below on Governor's proposal.)

In another major development, two strong supporters of a sales tax, Representative Vera Katz and Senator John Kitzhaber, have been elected Speaker of the House and Senate President, respectively, for the 1985 session of the Legislature. Additionally, Representative Tom Throop of Bend, a leading advocate of a sales tax, will continue to chair the House Revenue Committee. Both Katz and Kitzhaber believe the 1985 Legislature must act decisively in referring a sales tax measure to the voters to overcome a reputation of ineffectiveness gained during the 1983 session.

Business interests, as a whole, are generally perceived to support a sales tax in principle. However, various segments of the business and professional community were opposed to imposition of the sales tax on services in the final sales tax bill that passed the special session in 1983, and would likely oppose any new sales tax bill that included a tax on services. The Taxpayers for a Better Economy (TBE) sales tax initiative (which failed to get on the 1984 ballot because of a lack of signatures) did not tax services and had support within the business community.
The Oregon Education Association (OEA), a major political factor in any proposal to modify school funding, also strongly favors a sales tax. Recently, the OEA has proposed a sales tax package, discussed below.

The most significant opposition to a sales tax comes from organized labor, which perceives the tax to be regressive.

E. Current Sales Tax Proposals.

1. Governor's Proposal. In December, 1984, Governor Atiyeh announced the "Oregon" Plan. He is promoting it as a "comprehensive" program which includes a proposal for a sales tax and corresponding real property tax relief, coupled with a program to upgrade education at all levels.

The Governor's proposal would place in the Constitution a 5 percent sales tax on goods only, with proceeds to be used exclusively for public education through the community college level. Food for home consumption, prescription drugs, home utilities, and real estate would be exempt. School district tax bases would be rolled back an estimated 40 percent and permitted to grow at 6 percent per year (as is the case under current law). There is no provision for income tax reduction. The Governor says he will separately address cuts in income tax.

The Governor's tax package would also provide additional funding and programs for education and economic development. He proposes an "Oregon Action Plan for Excellence" in education, including model curriculum development and statewide testing. He would establish a State Board of Community Colleges and provide an additional $50 million for community college programs. He proposes increased spending for higher education, three academic-industrial research centers at existing campuses and additional state support for economic development activities. The Governor's proposal would result in increased spending for higher education with no offsetting reductions in spending in other areas of the state general fund budget.

2. OEA Initiative. In October, 1984, the OEA filed an initiative petition with the Secretary of State. In filing the petition, the OEA had two goals in mind. First, it was concerned that Ballot Measure No. 2, the real property tax limitation initiative, would be approved by the voters in the November, 1984, election. Thus, the OEA initiative might be perceived by some voters as an alternative for property tax relief if Ballot Measure No. 2 was defeated. Second, after the 1983 legislative session the OEA concluded that it could not persuade the Legislature to refer a sales tax initiative to the voters if the Legislature does not refer an acceptable sales tax package to the voters, the OEA will circulate its initiative petition with the goal of forcing an election in November, 1986.

The OEA initiative calls for a 5 percent retail tax on goods only, with exemptions for food, prescriptions, utilities, agricultural products and ingredients of manufacturing. Eighty percent of the revenues would be dedicated to funding for local schools to provide real property tax relief, and 20 percent would be dedicated to personal income tax relief.

The OEA has traditionally opposed any measure which would directly limit the rate or amount of real property taxation that could be levied by local governmental entities. The OEA initiative, however, would limit the total yearly revenue available to a school district (a combination of basic
school support paid out of state income tax dollars, new sales tax dollars, and remaining property tax dollars) to that amount which the school district had in the preceding fiscal year. This amount could grow each year by a percentage not greater than the per capita growth of personal income in the state during the previous calendar year.

II. POLITICAL CONSIDERATIONS OF A SALES TAX PROPOSAL

In considering which features to recommend for a sales tax proposal, your Committee was guided to a large extent by a recognition of political considerations. One important consideration is the current political climate discussed above. Over the past three years a great deal of time and energy has been spent in attempting to design a sales tax package that would be acceptable to Oregonians. The progress in that area to date was an important consideration in your Committee's deliberations.

An equally important consideration is the attitude of Oregonians toward the sales tax. In this respect, the Majority believes that any sales tax proposal that will be acceptable to the voters must accomplish the following political objectives:

1. **Constitutional Protections.** The proposal must include an amendment to the Constitution specifying goods subject to the sales tax, the maximum rate of taxation, and certain exemptions from sales tax.

2. **Exemptions.** Goods considered to be basic necessities of life must be exempt from taxation. Exempting services would reduce opposition from service providers and businesses which contract extensively for services.

3. **Real Property Tax Relief.** The proposal must result in substantial real property tax relief.

4. **No Increased Spending.** The proposal must result in no immediate increase in governmental spending at any level, and it should not be coupled with any proposal which would increase spending.

5. **Simplicity.** The proposal should be as simple as possible. In particular, limitations on increased governmental spending should be understandable to the general public.

6. **Protection for Citizens with Low Income.** The proposal must include low income credits or rebates to assure the tax burden does not fall heavily on the poor.

7. **Equity for Business and Individuals.** The proposal must be perceived as fair to businesses and individuals. It should minimize the overall shift in direct taxation from business to individuals through a variety of devices.

III. RECOMMENDED FEATURES OF A SALES TAX PACKAGE

This section contains a series of recommendations on desired features of a sales tax package. Table 3 provides a comparison of recommendations of the Majority with features in four recent proposals in Oregon: the Governor's proposal, the OEA initiative, the TBE initiative and the legislative package adopted by the Legislature at the 1983 Special Session.
A. Type of Sales Tax.

1. Alternatives Available. There are three basic types of sales tax:

   a. Single-Stage Sales Tax. A single-stage sales tax is imposed only once for each item purchased by the ultimate consumer. It might be imposed at the manufacturing, wholesale or retail level. Presently, all sales taxes in force in the United States are single-stage sales taxes imposed at the retail level.

   b. Multi-Stage Sales Tax. A multi-stage sales tax is imposed each time goods or goods in process are sold. Thus, a tax might be imposed at various stages of production, at the wholesale level and at the retail level. The multi-stage sales tax is imposed in some European countries.

   c. Value-Added Tax ("VAT"). The VAT is imposed at each stage of production, but taxes only the value added at that stage rather than the total amount of the sales transaction. It also is used in some European countries.

2. Discussion. For a given target level of tax revenue, a multi-stage tax employs a lower tax rate than either a single-stage tax or a VAT. This is because each time a sale occurs during the process of production and distribution the entire value of the item sold is taxed. Therefore the value created in an early production step may be taxed 4 or 5 times at different stages of production, wholesale and retail distribution.

   A multi-stage tax creates economic inequities. Goods that pass through several stages of production and distribution, with sales to a different company at each stage, are taxed more than goods having only one stage from producer to consumer. Large vertically integrated companies pay proportionately less tax than single-stage companies and small businesses—even though they may be competitors.

   Both the multi-stage tax and VAT discriminate in favor of imported goods because those goods are taxed at fewer stages than goods which are produced locally.

   Although the VAT would not discriminate against multi-stage goods and small companies, it could lead to "pyramiding". Each business along the line could include taxes paid at earlier stages in calculating its sales price to attain a target profit margin.

   No other state imposes a VAT and thus manufacturers and wholesalers may be motivated to move out or stay out of a state that imposes it. The number of businesses paying a VAT would be high, increasing the cost of administration.

   A uniform tax rate imposed at a single stage would be the simplest and least costly to administer, although the visible tax rate must be higher than a multi-stage tax rate.

3. Majority Recommendation. For reasons of equity and simplicity, and to be consistent with other states, a single-stage sales tax should be adopted in Oregon.
B. Level at which Tax is Imposed - Manufacturing, Wholesale or Retail Level.

1. Discussion. A single-stage sales tax can be imposed at the manufacturing, wholesale or retail level. Assuming the tax is shifted from retailer to consumer, the retail sales tax results in a uniform overall rate. If the tax is imposed at an earlier stage, the effective rate to the consumer will vary with the retailer's margin. Low-margin items, such as food, would bear a relatively higher burden than high-margin items, such as jewelry. This would generally result in regressivity.

If the tax were imposed before the retail level, the retailer's profit margin would be based on a cost which included the sales tax. This tends to result in pyramiding. Taxing at the retail level avoids pyramiding and thus tends to lower the price to the consumer. A tax at the wholesale level generally results in less pyramiding than does a tax at the manufacturing level.

Imposition of tax at the retail level permits separate quotation of the tax when goods are sold to the consumer. This allows the retailer to quote a lower price, and it heightens awareness among consumers of the magnitude of sales tax being paid.

Since retail price includes the retailer's margin, a retail sales tax rate can be substantially lower than a tax rate at the manufacturer's or wholesaler's level. For example, a 5 percent retail tax and an 8 to 10 percent manufacturer's tax would generate the same sales tax revenue.

The impact of a sales tax on business development is an important consideration. With adoption of a sales tax in Oregon, retailers in the Portland Metropolitan area and other border areas will lose an existing competitive advantage over retailers in adjacent sales tax states. Otherwise, because a retailer is location oriented and could not easily migrate from Oregon to another state to avoid a retail sales tax, a sales tax should not significantly influence the location of retail shops in Oregon. However, imposition of a tax at the manufacturing or wholesale level could cause manufacturers and wholesalers to locate elsewhere.

Administratively, a retail sales tax is more costly to collect than a tax imposed at the manufacturing or wholesale level. There are five to ten times more retailing firms than manufacturing or wholesaling firms. A final argument in favor of a retail tax is that a retail sale is more clearly identifiable than a final wholesale transaction.

2. Majority Recommendation. For reasons discussed above, the sales tax should be imposed at the retail level.

C. Exemptions from Sales Tax.

1. General Policy Considerations. The 1984 City Club Report on Oregon's Tax System recommended that the state enact "a broad-based retail sales tax covering goods and services as the best means available to fund property tax relief in Oregon." Another recommendation was that the imposition of a sales tax, and any use of the sales tax revenues to reduce income taxes, should not make the overall system of taxation more regressive. The thrust of these recommendations is sound in that a sales tax on a broad base of goods and services will raise greater revenue than a narrowly-based tax.
Also, a tax on services would minimize any shift in the overall direct tax burden from businesses to individuals. A shift will occur if services, which are primarily purchased by businesses, are exempt, and sales tax revenues, generated primarily by individuals who purchase goods, are used to provide tax relief for all real property including business property.

The twin goals—that the sales tax cover a broad base of goods and services and that it not result in greater regressivity—are somewhat conflicting. Thus your Committee has examined and the Majority has made recommendations on a number of exemptions to reduce the sales tax burden on low-income persons. Without exemptions for basic necessities, low-income persons would pay sales tax on a high percentage of their income used to purchase goods, whereas wealthier individuals, with excess funds to save and invest, would pay proportionately less tax. (The sale of stocks and bonds would not be taxed.) Additionally, your Committee concluded that exemptions are needed from a political standpoint if a sales tax is to be adopted by the voters in this state.

In considering how to reduce the impact of a sales tax on low-income individuals, your Committee has examined whether basic necessities should be exempt from tax, or low-income individuals should receive a tax credit or cash rebate each year. Either approach presents problems. If basic necessities are exempt, they must be defined. Once they are exempt from sales tax they will be exempt even if purchased by the well-to-do. On the other hand, if no exemptions are allowed, and a tax credit or cash rebate is granted, the amount of credit or rebate will be inexact, and will require a low-income person to file forms. Also, a rebate or credit may result in a delay from the time the tax is paid in cash until the time a credit or rebate is received.

Finally, because of public attitudes and practices in other states, some exemptions may be necessary for economic as well as political reasons. For example, currently in the state of Washington food for home consumption is exempt from tax. If Oregonians vote in favor of a sales tax proposal which would tax food for home consumption, this might result in a shift of food purchase dollars to Washington.

2. Exemption Categories. A review of sales tax statutes in other states, and recent sales tax proposals originating in Oregon, reveals certain exemption categories which recur frequently. For selected examples see Table 4. Significant categories of exemptions are discussed below.

a. Food for Home Consumption; Certain Meals. Food for home consumption is one of several items generally considered to be basic necessities. Those are goods and services needed to support human existence at a minimal level by U.S. standards. Basic food for home consumption is not a discretionary purchase.

School meals, fund-raising meals by charitable organizations, meals served in boarding houses and residential care facilities, and meals delivered to the elderly or served to the needy by a non-profit organization also warrant an exemption for broad social policy reasons. Often these meals may provide the major or only source of nourishment for various segments of society.
Majority Recommendation. Food for home consumption and meals for school children and the needy and those fund-raising meals provided by charitable organizations should be exempt from sales tax.

b. Medical Needs and Prescription Items. Medical services and prescription medicines and equipment are generally considered to be basic necessities in that they are often essential for the maintenance of health. Items essential for human health should not be subject to a sales tax.

Majority Recommendation. Medical services and prescription medicines and equipment should be exempt from sales tax.

c. Utilities. Utility services such as electricity, oil, gas, water and telephone and other services such as sewage and garbage services are necessary for day-to-day living and maintenance of health.

Majority Recommendation. Utilities should be exempt from sales tax.

d. Production Materials. Many states exempt from sales tax numerous items related to manufacturing and agriculture. The underlying rationale is to promote economic development and to avoid adding to the cost of food or other necessities. With respect to industrial and agricultural items, two different rules have evolved. The "direct use rule" would exempt any machinery, supplies or ingredients directly used or consumed in the processing of a product. The "physical ingredients rule" would exempt only those items which become a part of goods ultimately sold at retail. Under this rule, items consumed in the production process would not be exempt. For example, in the aluminum industry, raw materials which end up in finished aluminum would be exempt. On the other hand, chemicals and other materials consumed in the production process would not be exempt.

The problem with the "direct use rule" is that it would exempt all machinery and materials used in production, further shift the direct tax burden from businesses to individuals, and narrow the base of goods subject to sales tax, thus reducing revenues. On the other hand, without the "physical ingredients rule," the value of physical components in a finished product could be taxed numerous times. Your Committee concluded that ingredients should not be taxed more than once, but equipment and materials used or consumed in production should be taxed.

Majority Recommendation. Oregon should adopt the "physical ingredients rule."

e. Transportation Equipment; Vehicle Trade-Ins. Certain transportation-related items are often exempt from sales tax because they are intricately involved in interstate commerce, or they are expensive items purchased by persons who do not necessarily enjoy the benefits provided by the sales tax. These transportation items might include motor vehicle and aircraft fuel; aircraft, rail cars and trucks sold in or to be used in interstate or foreign commerce; commercial fishing boats; motor vehicles sold to non-residents; and new trucks purchased for use outside the state. These items should be exempt to avoid potential interference with interstate commerce.

A related question is whether, for sales tax purposes, to include in the purchase price of a new vehicle any cash credit received for a used
vehicle which is traded in. For example, if an individual purchases a new car with a price of $10,000 and pays $8,000 cash plus a trade-in vehicle, should the sales tax be imposed on the $10,000 purchase price or the $8,000 price after the trade-in? If the consumer has to pay sales tax on the entire $10,000 cost, he will in effect be paying sales tax on a trade-in for which he may previously have paid sales tax. Taxation of the trade-in value would then amount to double taxation on the same item owned by the same consumer.

Majority Recommendation. Transportation items involved in interstate commerce should be exempt from sales tax. The trade-in allowance for used vehicles should be exempt from sales tax.

f. Services. One of the most controversial issues related to the sales tax is whether services should be included or exempted. If services are exempt, should the exemption apply to all services, or only to certain categories of services? Although the earlier City Club report recommended that a sales tax apply to both goods and services, the Majority made an independent, and perhaps more political, judgment about that issue.

The 1983 Legislature was concerned about the potential shift of tax burden from business to consumers as a result of imposition of a sales tax. This shift occurs because businesses own more property in Oregon than do individuals, and would therefore get a larger share of the property tax relief. However, individuals purchase more retail goods than businesses, thereby paying a larger portion of the sales tax revenues used to provide property tax relief. Additionally, exempting services may benefit high-income individuals more than those with lower income, since many services are expensive. As a result of these concerns, the legislation adopted by the 1983 special session for referral to the voters provided for a tax on almost all services, including those which are used principally by businesses, such as services provided by accountants, gypo loggers, lawyers and janitorial services.

Although a strong argument can be made that a tax on services, primarily consumed by businesses, is warranted, such a tax is perceived by many businesses to be inequitable. For example, if a business is considering whether to have services performed by its employees, or by an outside contractor, a sales tax on services would increase the cost of doing business with the outside service contractor. Small businesses may be forced to use outside contract services because they cannot afford to hire employees to provide the same service, whereas a large business can hire employees to provide the service, thereby avoiding the tax. Additionally, some industries, such as the timber industry, rely heavily on services of independent contractors. Those businesses, and small businesses, would be adversely affected by a sales tax on services.

In a political sense, a tax on services creates substantial interest group opposition. Examples of service-oriented groups that would likely oppose the tax would be the timber industry, the legal and accounting professions, advertising agencies and so forth.

Majority Recommendation. All services should be exempt from the sales tax.

g. Government Purchases. The question arises as to whether state and local governmental entities should be exempt from paying a sales
tax, since the source of revenue which the governmental entity would use to pay the sales tax would be either income tax or property tax revenue. The question also arises whether a city, such as the City of Portland, should have to use property tax dollars to pay sales tax on goods that it purchases in its operations when the sales tax revenue is dedicated to another governmental entity, the local school districts. If the City of Portland is required to pay sales tax, it will have to seek additional property tax revenues in order to pay that 5 percent sales tax on its purchases.

**Majority Recommendation.** All governmental purchases should be exempt from the sales tax.

h. Real Estate Transactions. In most jurisdictions which have a sales tax, real estate sales and lease transactions are exempt from the tax. In some states, Washington, for example, a conveyance tax is imposed on real property transactions, but the conveyance tax rate is much lower than the sales tax rate. Any proposal to subject real estate transactions to sales tax would likely be met with widespread opposition because housing is considered a basic necessity like food, and one which should not be subject to sales tax. Real estate transactions are so large that any proposal to tax such transactions should not be part of the sales tax but should be addressed separately by the Legislature.

**Majority Recommendation.** Real estate transactions should be exempt from the sales tax.

i. Miscellaneous. Numerous other items will warrant consideration by the Legislature as exemptions. Examples include media-related goods, such as newspapers and political periodicals; cigarettes and liquor because they are already taxed; occasional sales by individuals; the bulk sale by a business of substantially all of its assets; and materials used in construction. Your Committee did not have the resources to examine all possible exemptions.

D. Low Income Credits or Rebates.

1. Discussion. Assuming basic necessities were exempt from sales tax, low-income citizens would still have to purchase goods subject to sales tax such as clothing, toiletries and sundries. For this reason, all recent sales tax proposals provide additional relief for low-income households.

Relief could be provided in two ways. First, a low-income taxpayer could receive a tax credit identified on the income tax return. This provides relief after the fact and only to those citizens who pay income tax. Second, relief could be provided in the form of a cash rebate, either before or after the year for which the rebate is granted. A rebate would be available to citizens who do not earn sufficient income to pay income taxes.

2. **Majority Recommendation.** To assure that all low-income citizens receive relief from the impact of a sales tax, the Majority recommends that a sales tax rebate be provided for low-income residents. The amount of rebate should be determined by a graduated schedule, to be established by the Legislature, with the lowest-income residents receiving the largest rebate. Whereas the Minority believes the rebate should be addressed in this report with greater specificity, the Majority would leave specifics of the rebate to the Legislature. The Legislature should determine an appropriate rebate schedule and provide safeguards against abuse.
E. Retailers' Compensation.

1. Background. Retailers will incur administrative costs in collecting the sales tax and remitting it to the state. The administrative burden of the sales tax will vary from retailer to retailer, depending on the type of business, the size of the business, and the method of bookkeeping. A high-volume retailer with computerized cost accounting may not feel the administrative burden as acutely as a small retailer who maintains books by hand.

Nationally, no common pattern exists with respect to retailers' compensation. In Washington, no credit is allowed. Recent proposals in Oregon have called for a credit of 1 to 2 percent of tax collected.

2. Discussion. Your Committee believes collection and remittance of sales tax should not create a financial burden for Oregon retailers. Therefore, the Legislature should determine an appropriate credit to be withheld by retailers as compensation for administrative costs. A variable rate may be appropriately based on sales volume or number of transactions.

In determining retailers' compensation, the Legislature should consider the cash-flow benefit to a retailer collecting sales tax. A retailer will have use of sales tax funds until they are remitted to the state. The collected revenues may either earn interest or reduce borrowing. For example, if sales tax proceeds are remitted on the 15th day of the month following the month of collection, a retailer would have use of funds for an average of 30 days. Assuming a 12 percent annual interest rate, this would result in interest income, or a reduction in interest paid, for the retailer equal to 1 percent of all sales tax collected.

The manner in which retailers' compensation is stated may be important politically. It might be stated as a percentage of the price of goods sold, rather than as a percentage of sales tax collected. A credit of 1/10 of 1 percent of sales price would be the same as a credit of 2 percent of tax revenue (assuming a 5 percent tax rate). Stating the compensation as a rate of 2 percent, however, could lead to the impression that retailers receive 2/5 of the 5 percent sales price and that administrative costs are excessive.

3. Majority Recommendation. The sales tax proposal should include a provision for retailers' compensation.

F. Use of Sales Tax Revenue.

1. Background. Use of sales tax revenue varies from state to state. In many states, sales tax revenues simply become part of the general fund to be appropriated by the state legislature. In other states, sales tax revenues are dedicated in whole or in part for specific purposes.

Recent Oregon proposals have called for dedication of sales tax revenues. The TBE initiative and the OEA initiative would dedicate 80 percent of revenues to basic school support and 20 percent to income tax relief. On the other hand, the Governor's proposal would dedicate 100 percent to basic school support and funding of community colleges.

2. Discussion. From its earliest discussions, your Committee favored dedicating sales tax revenue to particular programs rather than allowing
them to be subsumed within the state's general fund. Although dedication of revenues restricts their use, it also enhances the political viability of a sales tax proposal by letting voters know exactly to what use the revenues will be put.

As the 1984 City Club Report on Oregon's Tax System indicated, 61.9 percent of the property tax revenue raised in 1981 was spent on primary and secondary school education. In view of this relationship, the Majority in that report favored adoption of a sales tax which would decrease the dependence of school funding on local property tax levies. During its discussions, your Committee sought a dedication formula which would achieve this goal. At first glance, dedicating 100 percent to education seemed to be the appropriate response. However, such a formula would unfairly impact households, particularly those with low incomes, since the majority of real property in Oregon is owned by business. Providing for income tax relief would reduce the overall shift in the burden of direct taxation from business to individuals. This is particularly important in light of the Majority's recommendation not to tax services, the bulk of which are paid for by businesses.

In determining an exact formula for revenue dedication, the Committee considered the amount of real property tax relief which a 1.5 percent property tax limitation would provide. Such a limitation would reduce property taxes approximately 32 percent, on average. Thus, we sought to achieve a similar reduction while still allowing for significant income tax relief. Our calculations indicated that these twin goals could be achieved by a formula which dedicated 80 percent of sales tax revenues to education and 20 percent to income tax relief.

A related issue is whether existing real property tax relief programs should be continued (described in Section I.C. above). Your Committee strongly believes HARRP and the senior citizen tax deferral program should be continued if a sales tax is adopted.

A more difficult question is whether the 30 percent property tax relief program, adopted in 1979, should be continued. This program was adopted to provide meaningful real property tax relief. Because it was adopted as a statute, the program has since been revised and the amount of relief has been decreased by the Legislature. However, if the 30 percent property tax relief program is not continued, about $236 million per biennium will become available to the state general fund. It could be used to create new programs or enhance existing programs, and the overall level of state spending and taxes might increase. This would defeat one of the political and policy objectives of a sales tax which is to have the sales tax be a replacement tax and not a new source of revenue.

Your Committee believes the 30 percent property tax relief program should be continued for three reasons. First, it provides tax relief to homeowners and renters only, and thus will reduce the shift of direct tax burden from business to individuals. Second, when compared to real property tax relief generally, it provides relatively greater tax relief for low-value homes. For example, under the 30 percent program, the owner of a $50,000 home and the owner of a $100,000 home might both qualify for the maximum $170 relief each year. On the other hand, under real property tax relief generally, the owner of the more valuable home would receive twice the benefit received by the owner of the less valuable home. Third, the 30 percent program is an existing program benefitting both homeowners and
renters. Politically, if it is discontinued, voters may believe the Legislature is robbing Peter to pay Paul.

3. Majority Recommendation. Eighty percent of sales tax revenue should be dedicated to basic school support, and 20 percent should be dedicated to income tax relief. The existing HARRP, senior citizens deferral program, and the 30 percent property tax relief program should continue.

G. Rate of Tax

1. Discussion. In the 45 states and the District of Columbia which have a sales tax, the rate of tax varies from 2 percent to 8.1 percent (combined state and local sales tax rate). In some states the rate of tax varies among categories of items taxed. The average rate appears to be about 4 percent. See Table 1.

In Washington the state tax is 6.5 percent, and local jurisdictions can impose an additional tax of up to 1.6 percent. In California the state sales tax is 4.5 percent, and various local jurisdictions have the right to impose additional sales tax.

In Oregon, there appears to be little visible political support for allowing a local sales tax. Moreover, most recent sales tax proposals in Oregon have contained prohibitions against local sales taxes.

In Oregon, assuming a 5 percent tax rate, net revenues per year should total about $762 million. Of that amount, $610 million (80 percent) would be available for property tax relief, which on average, would be 38 percent. With a 4 percent tax, the property tax relief would be less than 31 percent.

A 5 percent tax rate appears to be necessary to provide meaningful property and income tax relief. On the other hand, your Committee believes a rate higher than 5 percent might be viewed by voters as excessive.

2. Majority Recommendation. The sales tax rate should be 5 percent.

H. Spending Limitations and Tax Relief

1. Background. Limitations on spending or taxation fall into four general categories.

a. Direct Limitation on Spending. An example of a direct spending limitation can be found in the TBE initiative. The state and each local jurisdiction would be given a spending base equal to the highest spending level over the prior three fiscal periods. Increases in the spending base would be allowed only for increases in population and increases in per capita personal income. Table 5 through Table 9 compare per capita personal income increases since 1969, and population changes since 1978, with increases in property tax levies, General Fund expenditures and Basic School Support.

b. Direct Limitation on Real Property Taxation. A second method of controlling governmental spending is to restrict the level of real property taxation. For example, under 1983 HB 2001 and HJR 20, all sales tax revenues would have been dedicated to Basic School Support. No direct
limitations would have been placed on spending but indirect methods were provided to control spending at the state and local level.

At the state level, "leakage" could occur if moneys in the General Fund, previously used for Basic School Support, (and, thus, indirectly for property tax reduction) were diverted by the state for other purposes. To prevent leakage, HB 2001 would have required state income tax support of the Basic School Fund to be maintained at a specified level. Additionally, all sales tax revenues would have been dedicated to further offset real property taxes.

At the local level, to prevent excessive spending by school districts, HJR 20 would have limited real property taxation for school districts to $2 per $1000 of value. This figure was selected to maintain school spending, at least initially, at approximately the existing level.

c. Direct Limitation on Tax Base. The Governor's proposal provides that each education district shall receive a new tax base equal to its prior year operating budget plus 6 percent, reduced by the difference between (a) state educational aid to the district including sales tax revenues in the first year revenues are available for such aid and (b) state educational aid to the district in the prior year. After a new tax base is established, it could be increased by 6 percent per year in accordance with existing law. Initially, the Governor's proposal contained no other control on taxation or spending. Recently, the Governor has agreed that a limitation on spending at the state level may be necessary politically.

d. OEA's Indirect Limitation on Real Property Taxation. The OEA initiative contains a complex mechanism to reduce real property taxation. To assure that present state support for school districts and community colleges is not reduced, the initiative requires the support to remain at the 1983-85 level, increased or decreased in the same ratio as increases and decreases in the budget for general state governmental expenditures. Considering the severe cutbacks on state agency spending necessitated by the past recession, this OEA formula could result in significant increases in funds for education as tax revenues return to more normal levels in the coming biennium.

In addition to providing a guaranteed level of General Fund support for school districts and community colleges, the OEA initiative dedicates 80 percent of sales tax revenues to support of school districts. If the two sources of state funds available to school districts ever exceed 90 percent of total expenditures for elementary and secondary education in the prior biennium (exclusive of payments on bonded indebtedness), the Legislature may reduce the support level to 90 percent through tax refunds.

These provisions could increase overall spending, especially spending for education, significantly.

2. Discussion. A sales tax would provide a new source of revenue. Absent statutory or constitutional safeguards, overall governmental spending could increase dramatically. As outlined above, recent and current sales tax proposals have included safeguards against increased governmental spending. See Table 3.

Of the various means to limit spending, your Committee believes a direct limitation on spending at the state and local levels is necessary for
voter approval of a sales tax package. No other means can assure voters that spending will not increase. In fact, under the Governor's initial proposal and the OEA proposal spending would increase.

At the state level, the limitation should apply to spending funded by the General Fund. The limitation might apply to all spending including Basic School Support. Or it might apply only to state agency spending, thereby exempting Basic School Support from the limitation. Since increased Basic School Support would reduce real property taxes, and not increase overall spending, it may be appropriate to exempt Basic School Support from the spending limitation.

At the local level, the spending limitation should apply to school districts only since other districts would receive no sales tax revenue. If spending is limited, and school districts receive sales tax revenues, the need for real property tax revenue will be reduced automatically. In districts which now have a current tax base, the tax base will be automatically reduced. In districts without an adequate tax base, the reduced need for real property tax revenue may result in the existing tax base becoming "current." In other words, an existing tax base which is insufficient to fund the school district's budget prior to adoption of a sales tax may be sufficient after the sales tax is in place.

In some school districts, the existing tax base is so low that it will not be current after adoption of the sales tax. For these districts, the Governor's proposal to establish a new tax base for each school district should be given serious consideration.

In general local jurisdictions other than school districts would not be affected by the sales tax proposal. Under current law, the portion of their budget funded by real property tax can increase by 6 percent per year without voter approval.

Although institution of a spending limitation would be extremely complex, it would be understandable in concept to the voting public. In contrast, the OEA initiative is far too complex and other proposals do not directly address the public concern for spending.

3. Majority Recommendation. Spending should be limited at the state level, and at the school district level, to a recent level of spending (i.e., 1984-85, 1983-85, or the highest level in recent years), subject to increases or decreases based on changes in per capita income and population. For school districts, "population" means student population, as determined by a method to be prescribed by the Legislature. The spending limitation would not apply to local taxing districts, such as counties and cities, which would receive no direct benefit from the sales tax. Those districts would continue to be governed by existing law.

1 Existing tax increment financing in urban renewal areas will be affected because the overall real property tax rate will be reduced. This problem must be addressed by the Legislature.
I. Override by Elected Body or Voters.

1. Discussion. If spending is limited, should there be a means to override this limitation? If voters can override the limitation, should the number of elections be limited?

Emergencies may arise which would require increased spending at the state level or in a school district. In such an emergency, the elected body should be allowed to increase spending for temporary periods. Your Committee believes that emergency spending should be authorized by a super-majority of the elected body since the circumstances warranting emergency spending should be unusual. Additionally, any increase in spending authorized on an emergency basis should be effective only during a single fiscal period.

If a spending limitation is to be effective, a permanent override should be accomplished only by vote of the people. The ability to schedule override elections should be limited to assure voters are not worn down by numerous elections called by interested parties.

2. Majority Recommendation. At the state and school district levels, elected representative assemblies or bodies should have the right to override spending limitations for emergencies for the fiscal period of the override but only by vote of three-fifths (3/5) of the members of each body. Permanent overrides should be allowed only by majority vote of the people at an election which must be held on a Tuesday in the year specified by statute for such a vote. Only one such vote per year should be allowed.

J. Renters' Relief.

1. Discussion. If a sales tax is enacted, renters will pay a new tax and there may be some pressure to provide compensating tax relief. Under the existing 30 percent property tax relief program, an owner-occupied home is afforded real property tax relief. For comparable relief a renter receives an income tax credit of 4.7 percent of rent paid up to a maximum of $85 per year. Without this credit a renter could expect no relief under the 30 percent program, direct or indirect, because direct tax relief is not provided to the owner of rental housing.

Similarly, under the HARRP program, 17 percent of rent paid is assumed to be attributable to real property taxes. A low-income renter is granted relief according to the portion of rent attributable to property tax and the renter's income level.

Any other form of direct renters' relief might unfairly favor renters. For example, under many commercial leases the tenant is liable for taxes. Thus, a reduction in property tax directly benefits the tenant. Additionally, in a competitive commercial or residential rental market, if real property taxes are reduced, presumably rental rates will be also. (The Committee does not accept the argument that lower taxes will not result in reduced rent, although some delay in rent adjustment is anticipated.

Your Committee believes real property tax relief will result in lower rents over time. If the 30 percent property tax relief program is maintained, all residential renters regardless of income, will continue to receive relief under that program. Additionally, as owners find costs of owning property reduced by lower real property taxes, rental rates should be
adjusted accordingly, particularly if the existing oversupply of residential and commercial property persists.

2. Majority Recommendation. Renter's relief should be continued under the 30 percent property tax relief program and HARRP. Sales tax funds should not be used to provide additional renters' relief.

IV. FISCAL IMPACT OF CITY CLUB SALES TAX PROPOSAL

A. Projected Sales Tax Revenues.

1. Projected Revenues. For the Committee's proposal, assuming a 5 percent sales tax is imposed on goods only, subject to exemptions outlined in section III.C.2, estimated gross annual revenue would be $812 million. After allowance for administrative costs, retailers' compensation and low-income tax credits or rebates, net sales tax revenues available would be $762 million. See Table 10 for computations on how gross revenues would be reduced to net revenues.

2. Who Pays the Sales Tax? Because individual consumers would purchase most goods subject to sales tax, based on Legislative Revenue Office estimates, households would pay 63.2 percent of a sales tax, businesses would pay 33.7 percent, and tourists would pay 3.1 percent. Assuming religious and charitable institutions are not exempt from paying sales tax, they will pick up a share of the overall tax burden. Currently, because both their real property and their income is exempt from taxation, they pay no tax under Oregon law.

B. Tax Relief Available Through Sales Tax.

1. Real Property Tax Relief. Assuming 80 percent of net sales tax proceeds are dedicated for use in funding school districts, an estimated $610 million per year would be available for that purpose. Assuming the General Fund continues to provide Basic School Support at the current level, property taxes needed to fund school districts in 1985-86 would be reduced from approximately $1195 million to $585 million, a reduction of 51.0 percent. Because real property taxes support needs other than education, the estimated overall reduction in property taxes would be about 38 percent.

The value of business and rental real property in Oregon exceeds the value of owner-occupied residential real property. Thus, commercial property will receive the majority of any real property tax relief. The Legislative Revenue Office estimates that 41.5 percent of the relief will go to owner-occupied residential property and 58.5 percent of the relief will go to other real property. See Table 10.

2. Comparison with Real Property Tax Relief Anticipated by Defeated Ballot Measure No. 2. Although Ballot Measure No. 2 (the real property tax limitation measure) was defeated by the voters in November 1984, it may be instructive to consider the level of real property relief it would have provided. The Legislative Revenue Office estimated that real property taxes would have been reduced by 32 percent. Assuming total real property tax revenue for 1983-84 of $1588 million, the 32 percent reduction would have amounted to statewide relief of $511 million, less than the $610 million of relief provided by 80 percent of projected net sales tax revenues.
3. Personal Income Tax Relief. Assuming 20 percent of net sales tax proceeds are dedicated to personal income tax relief, $153 million would be available for that purpose in 1985-86. Without such relief, personal income tax revenue for 1985-86 is projected to be $1,077 million. Thus personal income tax relief would average 14.2 percent.

4. Shift of Overall Direct Tax Burden to Individuals. Because the value of business and rental property in Oregon exceeds the value of owner-occupied housing, business and rental property will receive the majority of property tax relief. Similarly, because individuals purchase more goods subject to sales tax than do businesses, there will be an overall shift of the direct tax burden from business to individuals. This shift of direct tax burden from business to individuals is reduced by dedication of 20 percent of sales tax revenue to personal income tax reduction. Nevertheless, based on figures provided by the Legislative Revenue Office, your Committee estimates that the average individual will directly pay slightly more tax each year if your Committee's sales tax package is adopted. See Table 10.

V. AMENDMENTS TO THE OREGON CONSTITUTION

A. Discussion

A state constitution serves, first of all, to structure the institutions by which citizens govern themselves. Second, it states what limits the people have placed on the sovereign power of government. Third, it may expressly declare what inalienable rights have been guaranteed to the people. A state constitution should serve not to gratify immediate interests but to establish relations among a sovereign people for generations to come.

Regarding a sales tax, some states have included virtually every element of a tax in their constitutions. This method elevates matters requiring constant fine-tuning to a level of virtual permanence. However, it has the advantage of assuring the people that they can anticipate the impact of the tax and can control its future impact. Other states have codified the tax scheme entirely in statutes. This approach subjects the people to constant anxiety regarding the level, scope, and purpose of the tax. Conversely, it enables the legislature to respond to changing conditions by altering the basic structure of the tax.

From a purely theoretical perspective, the Oregon Constitution should contain only those elements of a sales tax considered absolutely fundamental to the structuring of government. However, political realities may in part determine what should be considered fundamental. Oregonians are not likely to approve a sales tax unless they can be guaranteed, for example, that the tax will not increase the total revenues of government.

B. Majority Recommendations

With the above constitutional principles and political considerations in mind, the Majority recommends that the following provisions be included in the Oregon Constitution:
1. The type of goods (i.e., tangible personal property sold at retail) subject to sales tax;

2. A maximum tax rate of 5 percent;

3. Exemptions for basic necessities of food, medical needs and utilities;

4. Requirement that the Legislature provide a method of sales tax relief to low-income residents;

5. Requirement that the Legislature provide a method of compensating retailers, with a portion of the sales tax or by delaying the time for remittance of sales tax revenues, for collecting and remitting the sales tax;

6. A dedicated use of sales tax revenues, 80 percent to basic school support and 20 percent to income tax relief, subject to appropriate safeguards;

7. Direct limitations on spending out of the state General Fund and spending by school districts; and

8. A prohibition against local sales taxes in order to assure voters that the door will not be opened to additional layers of taxation.

VI. SUMMARY OF MAJORITY RECOMMENDATIONS

The 1985 Session of the Oregon State Legislature should prepare a sales tax package for referral to the voters. The package should include an amendment to the Oregon Constitution, and a corresponding statute which would become effective if the voters approve the Constitutional amendment.

The features to be included in the Constitutional amendment and the statute are as follows:

1. Constitutional Amendments. The Constitutional amendment should provide the following:

   (a) The tax should be a single-stage sales tax.

   (b) The tax should be imposed at the retail level.

   (c) The tax should be on goods only, subject to exemptions for food for home consumption, prescription equipment and drugs and utilities.

   (d) The maximum rate of tax should be 5 percent.

   (e) The Legislature should be required to provide for sales tax relief for low-income residents.

   (f) The Legislature should be required to provide for retailers' compensation.

   (g) Eighty percent of sales tax revenue should be dedicated to basic school support and 20 percent should be dedicated to personal income tax relief.
(h) Spending out of the state General Fund and at the school district level should be limited to the current level of spending subject to increases or decreases based on per capita income and population.

(i) An emergency override of the spending limitation should be allowed by 3/5 vote of the elected governing body. A permanent override should be allowed by majority vote of citizens at an election to be held not more often than once per year.

(j) A prohibition against local sales taxes should be provided.

2. Statute. The accompanying statute should include the following:

(a) It should provide for additional exemptions from the sales tax including ingredients used in production, certain transportation equipment, vehicle trade-ins, government purchases and real estate transactions.

(b) The rate of tax should be set at 5 percent.

(c) Low-income citizens should be granted a rebate to reflect sales tax paid.

(d) Retailers should be compensated for the administrative costs of collecting and remitting the sales tax.

3. Other Considerations. The HARRP, senior citizens deferral program and the 30 percent property tax relief tax relief program should be continued.

Respectfully submitted,*

Bill Blount
Merrie Buel
Cecile Carpenter
Bill June
F. King Mitchell
Steven Moskowitz
Carolyn Perry
Charlotte Schwartz
Richard Roy, Chair

For the Majority

* The Committee wishes to thank Aaron Jay Besen, a third-year student at Duke Law School, for his assistance with research and his thoughtful comments.
VII. MINORITY DISCUSSION

The Minority agrees with all aspects of the Majority report and recommendations with three exceptions. In the following three ways, the Majority's proposal impedes the chances of the Model Sales Tax being enacted into law, and thus fails to meet the charge of the Board of Governors.

First, the Majority fails to meet one of the goals of the Club's 1984 report on Oregon's Tax System, namely to assure that the net effect of all changes would not make the system more regressive;

Second, the Majority proposal distributes a disproportionate share of the benefits of property tax relief to owners of business property, thus failing to provide meaningful relief to owners of homes; and

Third, the Majority allows too great a shift of the overall tax burden from business to individuals.

A. Regressivity.

The City Club, in adopting the 1984 report on Oregon's Tax System, made very clear that a sales tax would only be favored, "if the net effect of all changes would not make the system more regressive." That report said, "A tax is considered regressive if people with greater incomes pay relatively less."

The Majority's proposal to exempt services from the sales tax could create a significant problem. The Club's 1984 report on Oregon's Tax System states that a tax on services would tend to make a sales tax less regressive since most services are used by businesses, whereas most goods are purchased by individuals. The Majority report, in reference to the exemption of services, states, "Although any method of taxation is inequitable in isolated cases, a sales tax may create inequities for broad industry and interest groups." The Minority contends that exemption of services creates inequities in more than isolated cases, and should be addressed. The Minority believes, however, that the solution lies not in taxing services but in addressing the inequities that result by means of appropriate exemptions and tax relief measures.

As discussed in the Majority report, when services are exempted from the sales tax, it is necessary to increase the rate of tax on goods from 4 percent to 5 percent in order to provide sufficient revenues for meaningful property and income tax relief. This amounts to a 25 percent increase in the sales tax rate. Low-income families, which typically concentrate their spending on essential goods and cannot afford to engage professionals or other providers of services, would be especially hard hit by this increase, notwithstanding rebates and other exemptions.

The primary means of reducing the regressivity of a sales tax is to exempt basic necessities such as food, medicine and utilities from the tax. Without these exemptions, the tax burden would fall even more disproportionately on low-income persons, who spend a large share of their total income on these daily needs. Many other items which would not be covered by the Majority's exemptions consume large portions of the budgets of low-income people, however. For example, vehicles which are necessary for transportation to and from work, and clothing for families with school-age children, are the types of nondiscretionary spending which would be subject
to the sales tax. Additional exemptions, such as clothing purchased in a thrift store or the first $5,000 (or other appropriate amount) of the cost of an automobile, could be considered by the Legislature as ways to further minimize the regressive nature of the retail sales tax. The Minority also contends that the $20,000 homestead exemption (mentioned below) will help minimize regressivity of the overall tax burden.

While the Majority seeks a sales tax rebate for low-income groups, it does not specify an amount. The Minority believes that a sales tax rebate has to be sufficiently large to make the tax package's total impact progressive.

B. Relationship Between Homeowners' Property and Business Property.

The Majority proposes that 80 percent of the sales tax revenue would be used for real property tax relief. This would result, as the Majority discusses, in a decrease in real property taxes estimated at 38 percent, with the relief apportioned equally among classes of property. Because total true cash value of business real property exceeds the total true cash value of homeowner property, business property owners would receive the greater share of the proposed property tax relief. The Legislative Revenue Office estimates that 41.5 percent of relief would go to homeowners and 58.5 percent would go to other real property.

Apportioning the relief equally among all classes of property fails to recognize that it is the homeowners, not businesses, that have cried out for property tax relief. Furthermore, it is the homeowners who have the vast plurality of votes in the state and who will refuse to vote for a sales tax that fails to provide them with meaningful tax relief.

The Majority report states, "A sales tax has widespread support from political leaders and numerous interest groups, but whether the citizens of Oregon favor a sales tax is far less certain." As noted in the Majority report, polls indicate Oregonians might favor a sales tax if it provides real property tax relief. The Minority contends that if voters perceive that property tax relief will not be equitably distributed between business property owners and homeowners in proportion to their contribution to the sales tax, the sales tax could well be defeated.

To the extent to which unequal apportionment of tax relief between owners of business business property and owners of homes creates a shift from higher income to lower income persons, the regressivity of the overall tax burden is accentuated. The group of taxpayers that first sought property tax relief was the homeowners, particularly elderly homeowners on fixed incomes whose homes were being threatened by escalating property taxes. There is still a pressing need for property tax relief to this group.

The Minority believes that a more equitable distribution of property tax relief between business property owners and homeowners is needed. One means of accomplishing a more equitable distribution of sales tax revenue would be a $20,000 (or other appropriate amount) homestead exemption, i.e., eliminating from property tax the first $20,000 of true cash value of a home before the sales tax revenues are apportioned between owners of business property and homeowners.
C. Shift of Burden from Businesses to Individuals.

Although said to be desirable on political and economic grounds, the exemption of services from the sales tax shifts the overall burden of taxation in Oregon from businesses to individuals. Based on 1983 estimates of the Legislative Revenue Office, if both goods and services were subject to sales tax, individuals would pay 59 percent of the sales tax and businesses would pay 37 percent. If the Majority position were adopted, and services were exempt from sales tax, then individuals would pay about 63 percent and businesses, 34 percent. The reason for this shift is that businesses, which are the principal users of services, would escape paying the sales tax on those services, while individuals would purchase a preponderance of the goods that would be taxed under the Majority's proposal. Furthermore, as mentioned previously, the sales tax rate, in order to meet the target amounts necessary for property tax relief and education support, must be raised from 4 percent on both goods and services to a 5 percent rate on goods only. Thus, the exemption of services increases the sales rate by 25 percent.

The political consequences of favoring businesses over individuals, when individuals constitute the entire voting constituency, need to be carefully evaluated by both the City Club and the Legislature. The Minority believes that Oregon's voters will not enact into law the Majority's proposals that shift so much of the sales tax burden from businesses to individuals.

The Minority, therefore, proposes that the tax relief provided by the sales tax be distributed so that the overall tax burden does not shift from businesses to individuals any more than would have been the case in the 1983 special session's sales tax proposal.

VIII. MINORITY RECOMMENDATIONS

The Minority recommends adoption of all of the Majority's summary of recommendations (Section VI) and that the following subsections (b) - (d) be added to Section VI, Paragraph 3(a) so that it reads as follows:

"3. Other Considerations.

'(a) The HARRP, senior citizens deferral program and the 30 percent property tax relief program should be continued.

'(b) The Legislature should add exemptions to the sales tax which would lessen the burden of taxation on low-income persons and ameliorate the regressivity of the sales tax to the greatest extent possible. Among the exemptions to be considered are clothing purchased at thrift stores and the first $5,000 (or other appropriate amount) of the cost of an automobile.

'(c) Real property tax relief resulting from the use of sales tax revenues for basic school support should be apportioned among homeowners' property and business property, with the larger portion of relief going to homeowners' property, according to a formula determined by the Legislature. As one means of apportionment, the
Legislature should adopt the $20,000 property tax homestead exemption.

"(d) Sales tax rebates to low-income groups must be large enough to make the tax package's total impact progressive."

Respectfully submitted,

Gaulda Hahn
For the Minority

Approved by the Research Board and the Board of Governors on February 1, 1985 and ordered published and distributed to the membership for discussion and action on February 15, 1985.
Appendix A

PERSONS INTERVIEWED

Frank McNamara, Public Relations Specialist, Portland School District No. 1

Tom Throop, State Representative, District No. 54

Hardy Myers, attorney, and former Speaker of the House of Representatives (1979 and 1981 sessions)

John Danielson, Oregon Education Association

Gary Carlson, Executive Vice President, Associated Oregon Industries

Ann Jarvis, CPA, Arthur Anderson & Co.; and Chair City Club Report on Oregon’s Tax System

Richard Munn, Director, Oregon Department of Revenue

Richard Peterson, Legislative Revenue Office

Jim Scherzinger, Legislative Revenue Office

Terry Mattock, Executive Director, Oregon Taxpayers Association

William Dawkins, Lobbyist, Oregon Taxpayers Union

Nina Vallion, Attorney

Ken Thrasher, Vice President and Treasurer, Fred Meyer, Inc.

Cheryl Perrin, Vice President, Government Affairs, Fred Meyer, Inc.

Vera Katz, State Representative, District 10 and Speaker of the House for the 1985 legislative session.

Appendix B

PERSONS SURVEYED BY MAIL

Tom Bessonette, Oregon Mutual Insurance Company

Jim Murray, PacifiCorp

Bill Bradley, Reynolds Metals Company

Carl W. Mays, Jr., U.S. Bancorp

Blanche Schroeder, Portland Chamber of Commerce
APPENDIX C
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## Table 1

### Major Taxes and Rates Used by States

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<th>State</th>
<th>Corporation</th>
<th>Individual</th>
<th>General Sales and Use Tax</th>
<th>Gasoline Tax (per gallon)</th>
<th>Cigarette Tax (per pack of 20)</th>
<th>Property Tax</th>
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<td>5% ($F)</td>
<td>2 to 5% ($F)</td>
<td>4% ($F)</td>
<td>11¢</td>
<td>16¢</td>
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<td>4% ($F)</td>
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<td>21¢</td>
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<td>3%</td>
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<td>4.75% ($F)</td>
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<td>5%</td>
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<td>13¢</td>
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<td>Georgia</td>
<td>6%</td>
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<td>3% ($F)</td>
<td>7.5 + 3%</td>
<td>12¢</td>
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<td>17%</td>
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<td>4% ($F)</td>
<td>13%</td>
<td>17%</td>
<td>X</td>
</tr>
<tr>
<td>Virginia</td>
<td>6%</td>
<td>2 to 3.75%</td>
<td>3% ($F)</td>
<td>11%</td>
<td>2.5%</td>
<td>X</td>
</tr>
<tr>
<td>West Virginia</td>
<td>6% to 7%</td>
<td>5.3 to 13%</td>
<td>5% ($F)</td>
<td>10%</td>
<td>17%</td>
<td>X</td>
</tr>
<tr>
<td>Wisconsin</td>
<td>7.9%</td>
<td>3.4 to 10%</td>
<td>5% ($F)</td>
<td>15%</td>
<td>25%</td>
<td>X</td>
</tr>
<tr>
<td>Wyoming</td>
<td>5%</td>
<td>3%</td>
<td>3% ($F)</td>
<td>10%</td>
<td>17%</td>
<td>X</td>
</tr>
<tr>
<td>North Dakota</td>
<td>These 3 states</td>
<td>have no</td>
<td>Corporate income tax</td>
<td>5% ($F)</td>
<td>21%</td>
<td>X</td>
</tr>
<tr>
<td>South Dakota</td>
<td>5%</td>
<td>7.5%</td>
<td>13.15%</td>
<td>15%</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Texas</td>
<td>5.75%</td>
<td>10.25%</td>
<td>13.15%</td>
<td>15%</td>
<td>X</td>
<td>X</td>
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<tr>
<td>Washington</td>
<td>13.15%</td>
<td>10%</td>
<td>13.15%</td>
<td>15%</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>West Virginia</td>
<td>10%</td>
<td>13.15%</td>
<td>13.15%</td>
<td>15%</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Alaska</td>
<td>1 to 4.4%</td>
<td>1% to 4.4%</td>
<td>1% to 4%</td>
<td>1% to 4%</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Delaware</td>
<td>8.7%</td>
<td>1.4 to 13.5%</td>
<td>6% ($F)</td>
<td>16%</td>
<td>23%</td>
<td>X</td>
</tr>
<tr>
<td>Montana</td>
<td>6.75%</td>
<td>2 to 11%</td>
<td>6% ($F)</td>
<td>18%</td>
<td>8%</td>
<td>X</td>
</tr>
<tr>
<td>New Hampshire</td>
<td>3%</td>
<td>3%</td>
<td>3% ($F)</td>
<td>14%</td>
<td>17%</td>
<td>X</td>
</tr>
<tr>
<td>Oregon</td>
<td>7.5%</td>
<td>4.2 to 10.8%</td>
<td>6% ($F)</td>
<td>19%</td>
<td>X</td>
<td>X</td>
</tr>
</tbody>
</table>

* Indicates state levy a property tax.

** Indicates Federal income tax as a deduction.

---

Source: Compiled by Tax Foundation from data reported by Commerce Clearing House.
### TABLE 2
**SUMMARY OF INITIATIVE MEASURES TO REDUCE REAL PROPERTY TAXES**

<table>
<thead>
<tr>
<th>Measure</th>
<th>Vote</th>
<th>Margin</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nov. 5, 1968 &quot;Constitutional Amendment Changing Property Tax Limitation&quot; (State Measure No. 7)</td>
<td>276,451 503,443</td>
<td>29.11%</td>
</tr>
<tr>
<td>Repealed 6% limitation, limited property taxes to 1.5% of market value, exempted existing bonded indebtedness and levies approved in a November election by a majority of 20% of registered voters.</td>
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<td></td>
</tr>
<tr>
<td>Nov. 7, 1972 &quot;Prohibits Property Tax For Operations&quot; (State Measure No. 9)</td>
<td>339,431 551,816</td>
<td>23.88%</td>
</tr>
<tr>
<td>Prohibited the levy of property taxes to pay the operating expenses of elementary schools, high schools and community colleges.</td>
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<td></td>
</tr>
<tr>
<td>Nov. 7, 1978 &quot;Limitation on Ad Valorem Property Tax&quot; (State Measure No. 6)</td>
<td>424,029 453,741</td>
<td>3.39%</td>
</tr>
<tr>
<td>Limited real property taxes to 1.5% of 1975 assessed value or appraised value on later sale of new construction. Allowed 2% annual inflation increase. Required 2/3 vote of each house for new or increased state taxes, 2/3 popular vote for special taxes. Prohibited new ad valorem sales or transaction taxes on real property.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nov. 4, 1980 &quot;Constitutional Real Property Tax Limit Preserving Districts' 1977 Revenue&quot; (State Measure No. 6)</td>
<td>412,781 722,089</td>
<td>27.25%</td>
</tr>
<tr>
<td>Limited ad valorem real property taxes to 1% of 1977 True Cash Value plus amount necessary to provide 85% (100% for emergency services including police, fire, ambulance and paramedic) of 1977-1978 districts revenue. Schools were excluded from the emergency services definition. Taxable values and district revenues</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
could increase 2% annually. Preserved HARRP and renters relief. Prohibited ad
valorem, and all sales transaction taxes
on real property. Required 2/3 legis-
lative or popular vote for tax increases
and levies outside the 6% limitation.

Nov. 2, 1982 "Constitutional Real Property
Tax Limit Preserving 85%
Districts 1979-80 Revenue"
(State Measure No. 3)

Limited real property taxes to 1.5% of 1979
true cash value plus amount necessary to
provide 85% (100% for "essential services") of
districts 1979-1980 revenues. Assessed
values and revenue increases limited to
the lesser of 2% or the rate of inflation
as measured by the Consumer Price Index.
Property constructed after 1979 assessed
as if it had been built in 1979. Required
2/3 vote of the members of both houses or
majority popular vote for any legislative
change in any state taxes for the purpose
of increasing revenues. Changes relating
to real property taxes could only be
enacted by statewide vote, such elections
limited to two per year.

Nov. 7, 1984 "Constitutional Real
Property Tax Limit"
(State Measure No. 2)

Limited real property tax to lesser of
1.5% of 1981 assessed value as adjusted
or amount levied for 1983-1984. Exempted
existing authorized debts. Increase
in assessed value limited to 2% over
prior year's assessed value. Required
state-financed renter relief. New or
increased taxes required majority vote
of 50% of legal voters of taxing unit.
Specified two tax election dates.

Limited licenses, user fees and service
fees to actual cost. Exempted Social
Security benefits from taxation.

Source of vote abstract: Elections Division, Office of Sec-
retary of State, Salem, Oregon
### TABLE 3
SALES TAX COMPARISON

<table>
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<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td><strong>Rate</strong></td>
<td>4%</td>
<td>5%</td>
<td>5%</td>
<td>5%</td>
<td>5%</td>
</tr>
<tr>
<td><strong>Base</strong></td>
<td>Most goods &amp; services</td>
<td>Goods only</td>
<td>Goods only</td>
<td>Goods only</td>
<td>Goods only</td>
</tr>
<tr>
<td><strong>Constit. exemptions:</strong></td>
<td></td>
<td></td>
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<tr>
<td>Food at home</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
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<tr>
<td>Prescriptions</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
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<td>Utilities</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
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<tr>
<td>Real property</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
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<tr>
<td>Rents</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
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<tr>
<td>Medical services</td>
<td>Yes</td>
<td>Yes, by implication</td>
<td>Yes, by implication</td>
<td>Yes, by implication</td>
<td>Yes</td>
</tr>
<tr>
<td>Feed, seed, etc.</td>
<td>Yes</td>
<td>Yes, by implication</td>
<td>Yes, by implication</td>
<td>Yes, by implication</td>
<td>Yes</td>
</tr>
<tr>
<td>Ingredients</td>
<td>No</td>
<td>No</td>
<td>No</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Services</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>New Exemptions</strong></td>
<td>Vote of people required after 2 yrs</td>
<td>Vote of people not required</td>
<td>Vote of people not required</td>
<td>Vote of people not required</td>
<td>Vote of people not required</td>
</tr>
<tr>
<td><strong>Property Tax Relief</strong></td>
<td>100% for property tax relief</td>
<td>80% to schools or property tax relief</td>
<td>80% to schools</td>
<td>100% to schools, comm.colleges, &amp; higher educ.</td>
<td>80% to school districts</td>
</tr>
<tr>
<td><strong>Income Tax Relief</strong></td>
<td>Lower maximum rate to 10% in 1984 (stat.)</td>
<td>Lower maximum rate to 9% personal &amp; freeze corporate rate at 7.5% (Const.)</td>
<td>20% of proceeds to personal income tax (Const.)</td>
<td>Lower maximum rate to 10% in 1985 (stat.)</td>
<td>20% of proceeds to personal income tax relief (Const.)</td>
</tr>
<tr>
<td><strong>Renters</strong></td>
<td>Relief required (Equiv.reg by statute)</td>
<td>Relief maintained at current level</td>
<td>No provision</td>
<td>No provision</td>
<td>Relief maintained at current level</td>
</tr>
<tr>
<td><strong>HARRP</strong></td>
<td>Maintained in statute</td>
<td>Maintained in Constitution</td>
<td>Maintained in statute</td>
<td>Maintained in statute</td>
<td>Maintained in statute</td>
</tr>
<tr>
<td><strong>Low Income Credit</strong></td>
<td>Required, cannot be reduced without vote of people</td>
<td>Not required</td>
<td>Required</td>
<td>Required</td>
<td>Required</td>
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<tr>
<td><strong>Collector Compensation</strong></td>
<td>Required</td>
<td>Required</td>
<td>Required</td>
<td>Required</td>
<td>Required</td>
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<tr>
<td><strong>Severance Taxes</strong></td>
<td>No provision</td>
<td>Proportional reduction</td>
<td>No provision</td>
<td>No provision</td>
<td>No provision</td>
</tr>
<tr>
<td><strong>Local Sales Taxes</strong></td>
<td>Prohibited</td>
<td>Prohibited</td>
<td>Prohibited</td>
<td>Prohibited</td>
<td>Prohibited</td>
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<tr>
<td><strong>Accompanying Statute</strong></td>
<td>HB 3026</td>
<td>None</td>
<td>None</td>
<td>LC 1071-B</td>
<td>Needed</td>
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</tbody>
</table>

Source other than Committee Proposal: Legislative Revenue Office
<table>
<thead>
<tr>
<th>Item</th>
<th>General Form</th>
<th>Applies To</th>
<th>Levy Growth</th>
<th>Elections to Exceed Limit</th>
<th>State Limit Increase</th>
<th>Emergencies</th>
<th>Annexations, Consolidations, etc.</th>
<th>Tax Base Adjustments</th>
<th>Basic and Community College Aid Ceiling</th>
<th>Basic School Support Floor</th>
<th>Community College Aid Floor</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>State &amp; local</td>
<td>Per capita personal income plus popula. (local) personal income (state)</td>
<td>2 per year (May or November)</td>
<td>2/3 vote of Legis. or vote of people</td>
<td>Majority vote of governing body</td>
<td>Legis. can allow increases or decreases by statute</td>
<td>N/A</td>
<td>Covered by statutory expenditure limit</td>
<td>No minimum level</td>
<td>No minimum level</td>
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<tr>
<td>Item</td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td>Covered by state Constit. expend. limit</td>
<td>Must be maintained at 84-85 level plus or minus change in general fund spending</td>
<td>No minimum level</td>
</tr>
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<td></td>
<td>No limit</td>
<td>Must be maintained at 83-85 level plus or minus change in general fund spending</td>
<td>No minimum level</td>
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<td></td>
<td>Covered by state Constit. expend. limit</td>
<td>No minimum level</td>
<td>No minimum level</td>
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<td>No limit</td>
<td>No minimum level</td>
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**SPENDING LIMITATION COMPARISON**

<table>
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<tr>
<th>Item</th>
<th>General Form</th>
<th>Applies To</th>
<th>Levy Growth</th>
<th>Elections to Exceed Limit</th>
<th>State Limit Increase</th>
<th>Emergencies</th>
<th>Annexations, Consolidations, etc.</th>
<th>Tax Base Adjustments</th>
<th>Basic and Community College Aid Ceiling</th>
<th>Basic School Support Floor</th>
<th>Community College Aid Floor</th>
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</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>State &amp; local</td>
<td>Per capita personal income plus popula. (local) personal income (state)</td>
<td>2 per year (May or November)</td>
<td>2/3 vote of Legis. or vote of people</td>
<td>Majority vote of governing body</td>
<td>Legis. can allow increases or decreases by statute</td>
<td>N/A</td>
<td>Covered by statutory expenditure limit</td>
<td>No minimum level</td>
<td>No minimum level</td>
</tr>
<tr>
<td>Item</td>
<td></td>
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<td></td>
<td></td>
<td>Covered by state Constit. expend. limit</td>
<td>Must be maintained at 84-85 level plus or minus change in general fund spending</td>
<td>No minimum level</td>
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<td></td>
<td></td>
<td>No limit</td>
<td>Must be maintained at 83-85 level plus or minus change in general fund spending</td>
<td>No minimum level</td>
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<td></td>
<td></td>
<td></td>
<td>Covered by state Constit. expend. limit</td>
<td>No minimum level</td>
<td>No minimum level</td>
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<td></td>
<td></td>
<td>No limit</td>
<td>No minimum level</td>
<td>No minimum level</td>
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</table>

Source other than Committee Proposal: Legislative Revenue Office
TABLE 4
STATE BY STATE COMPARISON OF EXEMPTIONS

<table>
<thead>
<tr>
<th>State</th>
<th>Manufacturing</th>
<th>Machinery</th>
<th>Rolling Stock</th>
<th>Clothing</th>
<th>Prescription Drugs</th>
<th>Restaurants</th>
<th>Drugs</th>
<th>Isolated Sales</th>
<th>Construction</th>
<th>Materials</th>
<th>Sales to Housing Authority</th>
<th>Newsprint</th>
<th>Electricity</th>
<th>Telephone</th>
<th>Transportation</th>
<th>Printing</th>
<th>Software</th>
<th>Professional Services</th>
</tr>
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<tbody>
<tr>
<td>Alabama</td>
<td></td>
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<td>Arizona</td>
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</table>

Source (goods): Mississippi State Tax Commission, "National Tax Survey, 1980"

Source (services): FISCAL AFFAIRS, NCIL, November 1981
Table 5
OREGON PER CAPITAL PERSONAL INCOME
1969 to 1983

<table>
<thead>
<tr>
<th>Tax Year</th>
<th>Per Capita Personal Income</th>
<th>Percent Increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>1969</td>
<td>$3,520</td>
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</tr>
<tr>
<td>1970</td>
<td>3,719</td>
<td>5.7%</td>
</tr>
<tr>
<td>1971</td>
<td>3,992</td>
<td>7.3%</td>
</tr>
<tr>
<td>1972</td>
<td>4,338</td>
<td>8.7%</td>
</tr>
<tr>
<td>1973</td>
<td>4,829</td>
<td>11.3%</td>
</tr>
<tr>
<td>1974</td>
<td>5,312</td>
<td>10.0%</td>
</tr>
<tr>
<td>1975</td>
<td>5,769</td>
<td>8.6%</td>
</tr>
<tr>
<td>1976</td>
<td>6,368</td>
<td>10.4%</td>
</tr>
<tr>
<td>1977</td>
<td>6,998</td>
<td>9.9%</td>
</tr>
<tr>
<td>1978</td>
<td>7,855</td>
<td>12.2%</td>
</tr>
<tr>
<td>1979</td>
<td>8,676</td>
<td>10.5%</td>
</tr>
<tr>
<td>1980</td>
<td>9,309</td>
<td>7.3%</td>
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<tr>
<td>1981</td>
<td>9,938</td>
<td>6.8%</td>
</tr>
<tr>
<td>1982</td>
<td>10,148</td>
<td>2.1%</td>
</tr>
<tr>
<td>1983</td>
<td>10,740</td>
<td>5.8%</td>
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</tbody>
</table>

Average Annual Increase: 8.3%
Average Biennial Increase: 18.6%

Source: Oregon Taxpayers' Association
Table 6

OREGON POPULATION
1978 to 1984

<table>
<thead>
<tr>
<th>Year (July 1)</th>
<th>Estimated Population</th>
<th>Percent Increase</th>
<th>Combined Percent Increase of Population and Per Capita Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>1978</td>
<td>2,522,000</td>
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<tr>
<td>1979</td>
<td>2,584,000</td>
<td>2.45%</td>
<td>13.2%</td>
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<tr>
<td>1980</td>
<td>2,640,000</td>
<td>2.17</td>
<td>9.6</td>
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<tr>
<td>1981</td>
<td>2,661,000</td>
<td>0.80</td>
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<tr>
<td>1982</td>
<td>2,656,000</td>
<td>(0.19)</td>
<td>1.9</td>
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<tr>
<td>1983</td>
<td>2,635,000</td>
<td>(0.79)</td>
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<tr>
<td>1984</td>
<td>2,660,000</td>
<td>0.95</td>
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Table 7

PROPERTY TAX LEVIES BY TYPE OF GOVERNMENT*
1969-70 TO 1983-84
(millions)

<table>
<thead>
<tr>
<th>Counties</th>
<th>Cities</th>
<th>School Districts</th>
<th>Community College Districts</th>
<th>Special Districts</th>
<th>Total</th>
</tr>
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<tbody>
<tr>
<td>1969-70</td>
<td>$42.4</td>
<td>$62.8</td>
<td>$314.5</td>
<td>$14.3</td>
<td>$18.8</td>
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<tr>
<td>1970-71</td>
<td>44.2</td>
<td>69.3</td>
<td>348.6</td>
<td>18.9</td>
<td>22.2</td>
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<td>1971-72</td>
<td>56.6</td>
<td>73.0</td>
<td>364.5</td>
<td>21.0</td>
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<td>1972-73</td>
<td>59.1</td>
<td>75.2</td>
<td>394.8</td>
<td>22.8</td>
<td>29.4</td>
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<tr>
<td>1973-74</td>
<td>61.3</td>
<td>81.0</td>
<td>394.4</td>
<td>24.2</td>
<td>32.8</td>
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<tr>
<td>1974-75</td>
<td>65.9</td>
<td>91.8</td>
<td>458.9</td>
<td>28.0</td>
<td>39.5</td>
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<tr>
<td>1975-76</td>
<td>71.2</td>
<td>103.1</td>
<td>521.3</td>
<td>33.3</td>
<td>44.4</td>
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<td>1976-77</td>
<td>79.3</td>
<td>115.6</td>
<td>568.5</td>
<td>34.8</td>
<td>54.1</td>
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<tr>
<td>1977-78</td>
<td>85.7</td>
<td>124.4</td>
<td>577.2</td>
<td>39.9</td>
<td>66.0</td>
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<tr>
<td>1978-79</td>
<td>88.1</td>
<td>132.0</td>
<td>575.8</td>
<td>40.9</td>
<td>70.3</td>
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<tr>
<td>1979-80</td>
<td>94.3</td>
<td>152.7</td>
<td>636.2</td>
<td>47.8</td>
<td>73.6</td>
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<tr>
<td>1980-81</td>
<td>107.6</td>
<td>183.9</td>
<td>743.5</td>
<td>56.2</td>
<td>86.7</td>
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<td>1981-82</td>
<td>150.1</td>
<td>206.7</td>
<td>889.8</td>
<td>64.8</td>
<td>104.5</td>
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<tr>
<td>1982-83</td>
<td>159.2</td>
<td>220.4</td>
<td>958.8</td>
<td>70.6</td>
<td>109.5</td>
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<tr>
<td>1983-84</td>
<td>149.0</td>
<td>223.4</td>
<td>1,010.1</td>
<td>73.9</td>
<td>119.0</td>
</tr>
</tbody>
</table>

Average Change
+ 9.9%  + 9.9%  + 8.9%  +12.7%  +14.2%  + 9.6%

*Includes levies for bonded debt.

Source: Oregon Taxpayers' Association
### Table 8

OREGON STATE BUDGET
GENERAL FUND EXPENDITURES
1969-71 to 1983-85

<table>
<thead>
<tr>
<th>Expenditures (millions)</th>
<th>Percent Increase</th>
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<tbody>
<tr>
<td>1969-71</td>
<td>$710.8</td>
</tr>
<tr>
<td>1971-73</td>
<td>768.5</td>
</tr>
<tr>
<td>1973-75</td>
<td>1,036.5</td>
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<tr>
<td>1975-77</td>
<td>1,445.3</td>
</tr>
<tr>
<td>1977-79</td>
<td>2,059.4</td>
</tr>
<tr>
<td>1979-81</td>
<td>2,878.2</td>
</tr>
<tr>
<td>1981-83</td>
<td>2,886.2</td>
</tr>
<tr>
<td>1983-85*</td>
<td>3,139.1</td>
</tr>
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</table>

Average Biennial Increase..................24.8%

*Estimated 9-1-84

Source: Oregon Taxpayers' Association

### Table 9

BASIC SCHOOL SUPPORT FUND

<table>
<thead>
<tr>
<th>Expenditures (millions)</th>
<th>Percent Increase</th>
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<tr>
<td>1969-71</td>
<td>$177.9</td>
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<tr>
<td>1971-73</td>
<td>203.7</td>
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<td>1973-75</td>
<td>314.4</td>
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<tr>
<td>1975-77</td>
<td>418.1</td>
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<tr>
<td>1977-79</td>
<td>610.4</td>
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<tr>
<td>1979-81</td>
<td>790.8</td>
</tr>
<tr>
<td>1981-83</td>
<td>840.5</td>
</tr>
<tr>
<td>1983-85*</td>
<td>880.0</td>
</tr>
</tbody>
</table>

Average Increase.............................26.9%

*Estimated 9-1-84

Source: Oregon Taxpayers' Association
Table 10

FISCAL ANALYSIS OF MAJORITY'S PROPOSAL AND GOVERNOR'S PLAN

The Majority has recommended a 5 percent sales tax on goods only. Eighty percent of net sales tax proceeds would be distributed to school districts, and 20 percent would be available for personal income tax relief. Governmental purchases would be exempt from sales tax, and the existing 30 percent real property tax relief program would be continued.

The Governor has recommended a 5 percent sales tax on goods only. One hundred percent of net sales tax proceeds would be distributed to school districts and community college districts, and none of the sales tax proceeds would be used for personal income tax relief. Governmental purchases would not be exempt, and the existing 30 percent real property tax relief program would be discontinued.

Fiscal information available to the Committee was incomplete. However, the following information was relevant to the Committee deliberations.

1. Sales Tax Revenues. The Legislative Revenue Office has estimated that a 5 percent tax on goods would generate revenues shown below. The Majority's proposal figures have been adjusted since the Governor's plan figures assume that 5 percent of gross revenues will come from sales tax on governmental purchases.

<table>
<thead>
<tr>
<th>Item</th>
<th>Governor's Plan</th>
<th>Majority's Proposal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Revenue</td>
<td>$855.0 million</td>
<td>$812.0 million</td>
</tr>
<tr>
<td>Retailers' Compensation</td>
<td>(17.0)</td>
<td>(16.0)</td>
</tr>
<tr>
<td>Administration</td>
<td>(15.0)</td>
<td>(14.0)</td>
</tr>
<tr>
<td>Low Income Credit</td>
<td>(20.0)</td>
<td>(20.0)</td>
</tr>
<tr>
<td>Net Revenue</td>
<td>$803.0 million</td>
<td>$762.0 million</td>
</tr>
</tbody>
</table>

Although sales tax revenue under the Governor's plan exceeds revenue under the Majority's proposal, the excess represents sales tax paid by governmental agencies. Thus, the excess does not ultimately increase income tax and property tax relief.

2. Who Pays the Sales Tax? The Legislative Revenue Office has estimated the sales tax on goods would be paid by taxpayers as follows:

<table>
<thead>
<tr>
<th>Sales Taxpayer</th>
<th>Governor's Plan</th>
<th>Majority's Proposal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individuals</td>
<td>60%</td>
<td>63.2%</td>
</tr>
<tr>
<td>Businesses</td>
<td>32</td>
<td>33.7</td>
</tr>
<tr>
<td>Tourists</td>
<td>3</td>
<td>3.1</td>
</tr>
<tr>
<td>Government</td>
<td>5</td>
<td>0</td>
</tr>
<tr>
<td>100%</td>
<td>100.0%</td>
<td></td>
</tr>
</tbody>
</table>

3. Real Property Tax Relief. Under the Governor's plan, the existing 30 percent real property tax relief program would be eliminated, thereby increasing real property tax and reducing renter relief by a total of $118 million per year. On the other hand, 100 percent of net sales tax proceeds,
or $803 million per year, would be dedicated to real property tax relief. Thus, net real property tax relief would be $685 million per year.

Under the Majority's proposal, 80 percent of net sales tax proceeds or $610 million per year, would be dedicated to real property tax relief. Additionally, 20 percent of net sales tax proceeds, or $153 million per year, would be dedicated to personal income tax relief.

The Legislative Revenue Office has estimated that 41.5 percent of real property tax is assessed against owner-occupied homes, 16.5 percent is assessed against rental residential property, and 42 percent is assessed against other property.

4. Shift in Direct Taxation to Individuals Under Majority's Proposal and Governor's Plan. Individuals in Oregon would bear a slightly greater share of the overall direct tax burden under the Majority's proposal compared to the current tax structure. Under the Governor's proposal, the shift of direct tax burden to individuals would be greater. Rough figures on an annual basis are shown below. They assume 1/2 of real property tax relief granted to owners of rental residential property will be passed through to renters.

<table>
<thead>
<tr>
<th>Shift to Individuals Under Committee's Proposal</th>
<th>$57 million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales Tax (63.2% of $812 million)</td>
<td>$513 million</td>
</tr>
<tr>
<td>Homeowner Real Property Tax Relief (41.5% of $610.4 million)</td>
<td>(253)</td>
</tr>
<tr>
<td>Real Property Tax Relief Passed through to Renters (1/2 x 16.5% x $610.4 million)</td>
<td>(50)</td>
</tr>
<tr>
<td>Income Tax Relief (20% of $763.0 million)</td>
<td>(153)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Shift to Individuals Under Governor's Plan</th>
<th>$232 million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales Tax (60% of $855 million)</td>
<td>$513 million</td>
</tr>
<tr>
<td>Elimination of 30% Program</td>
<td>118*</td>
</tr>
<tr>
<td>Homeowner Real Property Tax Relief (41.5% of $803 million)</td>
<td>(333)</td>
</tr>
<tr>
<td>Real Property Tax Relief Passed through to Renters (1/2 x 16.5% x $803 million)</td>
<td>(66)</td>
</tr>
</tbody>
</table>

* The Majority has assumed that the $118 million saved by elimination of the 30 percent property tax relief program will be used to fund the Oregon Action Plan for Excellence, and therefore not reduce income taxes. If not, and if the $118 million is used for personal income tax relief, the shift would be reduced from $232 million to $114 million. Elimination of the 30 percent property tax relief program has the effect of shifting property tax relief to businesses, and reapportioning relief available to homeowners in favor of higher value homes.