

## Taxing Thoughts

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# TAXING THOUGHTS

MARC J. MAROTTA\*

Early in his administration, Governor Doyle articulated his core economic goals for Wisconsin, including competing at the high end by upgrading our workforce through such initiatives as investing in job training and in early-stage ventures into the new economy, raising wages at all levels, streamlining our regulatory system, and improving Wisconsin's tax structure. When he announced his "Grow Wisconsin" plan last year, he said it was not going to just sit on a shelf—and he meant it.

I am proud to report that we have already made real progress. We started with the budget. Faced with a \$3.2 billion deficit—the largest in our history and one of the worst per capita deficits in the nation—we balanced the budget without raising taxes. We did not raise corporate taxes. We did not raise income taxes. We did not raise sales taxes. In fact, we did not raise *any* taxes. And we did all this without resorting to inflexible limits, like those proposed as part of the so-called "Taxpayer Bill of Rights" ("TABOR"), which I will discuss later.

## I. POSITIONING WISCONSIN FOR ECONOMIC GROWTH

Controlling spending and taxes was probably the most important thing we could do to put Wisconsin's economy back on track. It sends a signal to the business community that Wisconsin can take care of its challenges in a responsible, forward-looking manner. And the Doyle Administration has done much more in the past year to position our state to create jobs and promote economic opportunity. Many of these ideas had languished in the legislature for years—but in less than a year, we got them done.

For example, the Governor signed the Financial Modernization Act, a bill that will pump hundreds of millions of dollars of new investment into Wisconsin to help prepare our state to compete in a global economy. Earlier, he signed the Regulatory Reform Act, which will cut approval times for air and water permits and promote job expansion. Another new law creates a sales tax exemption for fuel and electricity used in manufacturing, which will help Wisconsin companies compete more effectively with manufacturers in

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other states and overseas. And he signed a bill—which previous administrations failed to pass—creating a “single sales factor,” thereby eliminating what amounted to a tax on companies that create jobs.

Dozens of other initiatives, large and small, have been completed, from launching the Business Wizard (an online service that helps small businesses more easily navigate the state’s regulatory framework) to expanding technology zone tax credits. And dozens of other projects are underway. All of these initiatives will make Wisconsin more competitive.

They reflect our dual fiscal priorities of reducing taxes while also protecting core public services. Wisconsin is in the upper-middle range of per capita spending on state and local services. But our expenditures are highest in areas that contribute to our economic growth, including education, medical care, public safety, and transportation. Also, in Wisconsin most state revenues are shared with schools and local governments to support education and vital services, such as police and fire protection.

The record shows that we generally get what we pay for. Wisconsin students consistently rank high in reading, math, and science proficiency, and we benefit from relatively high levels of childhood immunization. But we also face substantial pressure in all of these areas. For example, our Medical Assistance and Badger Care caseloads have increased 11%, to over 600,000 since 2000. For all states, this will be an ongoing challenge.

Wisconsin already has an array of tax and spending limits in place to help control expenditure growth at both the state and local levels. Most general state spending is limited to the growth rate of personal income; school districts face spending caps; county mill rates are held to the 1992 level; and Expenditure Restraint Payments encourage municipalities to limit annual budget growth to a factor linked to inflation and new construction.

As a result of a move from the requirement that the state fund two-thirds of K–12 public education costs and a reduction in shared revenue payments, some predicted double-digit property tax increases. However, the Governor, in taking the lead at the state level to cut our government without raising taxes, was able to work with local municipal, county, and school district leaders to reduce spending and to hold the line on property taxes. While property taxes in Wisconsin are still too high, 2003 municipal tax levies rose 3.3%, the lowest increase in at least 14 years, and K–12 school districts restrained their spending growth to the lowest level in at least 7 years. As a result, last year the average Wisconsin homeowner saw the smallest property tax increase since 1999, and a new report from the Tax Foundation indicates that our state/local tax burden has fallen dramatically—from 12.4% of personal income in 1995 to 11.1% this year. Clearly, more work needs to be done on that front.

## II. IMPLICATIONS OF A TABOR AMENDMENT

Given this progress, what are the implications of a TABOR constitutional amendment similar to the one in place in Colorado? One predictable outcome is that TABOR would reduce state and local spending—that is the point after all. But what services would be impacted most by these cuts is less predictable. Due to demographic pressures, Colorado has increased spending on welfare and corrections programs despite TABOR. The result has been sharp restrictions on investments in infrastructure improvements (such as highways and education).

Across a wide range of quality-of-life indicators, I doubt that many of us would want to trade places with Colorado. Wisconsin ranks 10th in childhood immunizations, Colorado ranks 50th. We rank 1st in ACT scores, Colorado ranks 40th. Wisconsin's high school graduation rate ranks us 8th, compared to 35th for Colorado.

Stringent limits on state spending could have other, unintended consequences for Wisconsin. If such a constitutional limit had been in place in 1987–88, we could never have achieved two-thirds state funding of local K–12 school costs, and school property taxes would be \$1.3 billion higher today.

## III. POLICY PREFERENCES ARE CHANGING IN WISCONSIN

The push for TABOR also ignores the fact that policy preferences in Wisconsin have been changing in recent years. Decisions built up over 50 years reverse slowly, but change is here. We saw this in the 2002 election, when a clear consensus emerged to avoid any general state tax increase. But even before that, income taxes were cut and indexed. Total state income tax collections actually dropped from about \$6 billion in Fiscal Year (“FY”) 2000 to about \$5.1 billion in FY 2003. State government's tax rankings have also declined in recent years, falling from 9th in the nation in 1999 to 12th in 2002.

The state tax burden is still dropping, reaching a 34-year low of 6.9% of personal income in FY 2003. By contrast, it increased steadily in the 1990s, from 7.4% to a high-point of 8.3% of personal income. Where were the advocates of TABOR then?

The important lesson from our recent history is that the process works when elected officials follow the preferences of the electorate. In today's economic environment, citizens and their elected representatives recognize that taxes do matter and that they do affect our competitive position among our neighbors, across the country, and around the world. The answer is not a

thoughtless formula, but having officials who understand education and economic development—and understand the need to have a competitive business environment and to hold down taxes.

#### IV. TAX RANKING WILL CONTINUE TO DECLINE

Wisconsin's tax ranking will continue to drop simply because we are holding the line while other states are not. Nationally, the April–June 2003 quarter was the sixth straight quarter of overall state tax hikes. In that quarter alone, other states collected \$3.5 billion in new taxes. This includes higher personal income taxes in states like Massachusetts; higher corporate income taxes in states like California and New Jersey; new sales taxes in Ohio, Indiana and Tennessee; and higher tobacco taxes in Pennsylvania and other states.

Just as importantly, as I indicated earlier, Wisconsin has targeted its tax cuts to help stimulate economic growth. While fiscal realities make further tax cuts unlikely in the near-term, targeted tax reforms that promote the Governor's Grow Wisconsin goals remain an option.

#### V. STRENGTHENING THE STATE/LOCAL PARTNERSHIP

The Governor is also determined to strengthen the state/local relationship to encourage cost savings and promote local government decisions that encourage economic growth. This includes a commitment to preserving a reasonable shared revenue formula; respecting local budget decisions, rather than imposing an inequitable "tax freeze" that would have halted local economic development, undermined public education, and ended Wisconsin's tradition of local control; rebuilding the state/local partnership; encouraging cost-savings through cooperative purchasing; and streamlining state programs to improve service delivery to local governments and citizens.

We are especially encouraged by the increasing interest local government officials have shown in managing costs and strengthening local services through cooperation. Examples include:

- The Neenah/Menasha Fire Department consolidation is expected to save \$2 million over the next five years;
- The North Shore Fire Department resulted from the merger of seven separate departments;
- The City of Waupaca regularly meets with surrounding towns to coordinate service delivery;
- A cooperative purchasing effort in southeastern Wisconsin, including counties, cities, villages, towns, and special districts, reduces costs; and

- Many communities, including New Berlin, Butler, and Brookfield jointly provide hazardous material response teams.

## VI. REDUCING COSTS WHILE PRESERVING ESSENTIAL PUBLIC SERVICES

Finding creative ways to reduce local costs, while preserving core services, is essential to our long-term fiscal goals. The same logic applies at the state government level, where we are merging agencies, improving our use of technology, and finding other ways to trim administrative costs.

Rather than pursuing divisive and questionable strategies like TABOR, the legislature should continue working toward sound reforms that create more opportunities for economic growth, while also protecting our high quality of life. For example, we need to work steadily to raise Wisconsin's per capita income and boost it past the national average. Reaching this goal will mean that more families can buy a home, send their kids to college, and have a secure retirement. It will help us invest in education and health care without raising taxes. In fact, if our wages were just at the national average, our deficit would have been \$1.1 billion smaller. In the competitive international environment in which our businesses exist, the legislature should use its time addressing job training, tax policy, the need for early-stage capital, regulatory reform, and other areas that will grow the economy and make a difference for our future.

Our children deserve a strong, vibrant economic future, full of opportunity for all those willing to seize it. The challenges we face as we strive toward this goal may be great, but our potential is even greater. Thank you for all you have done in the past to help grow Wisconsin's economy, and I urge you to continue to work with the Governor and his administration as we move Wisconsin's economy toward its full potential.

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