



Proposed State Constitutional Amendment Prohibiting a State Property Tax

Issue

In the 2019 legislative session, legislation filed as SJR3 Niceley would set into motion the process of amending the State Constitution to prevent the state from collecting a state property tax on individuals. Tennessee has not collected a state property tax on individuals since 1949, however this would not affect local governments from collecting property tax. Even though the state is in a very sound fiscal position currently, members of the Senate Finance Committee discussed what the state would do if there is a need for more revenue in an economic downturn. Additionally, members were concerned how credit agencies would view limiting another option for state revenue. Farm Bureau supported SJR3, but the legislation could not garner the votes needed in the committee. Senator Niceley delayed the legislation to 2020. Farm Bureau policy states we strongly oppose a state property tax, but the policy does not mention a constitutional amendment on the issue.

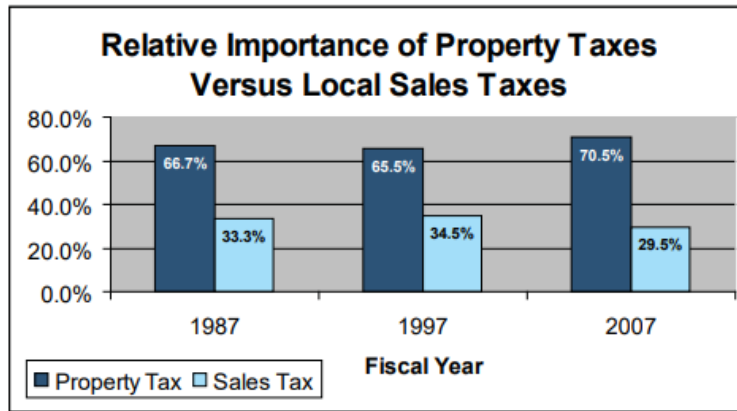
Background

Property taxes date back to ancient times when all worth was believed to come from the land and what it produces. Property and poll taxes (taxes levied as a fixed sum on every adult without reference to income) in American history date all the way back to the original colonies where the taxes were imposed at some point in time in all of the colonies. As the original colonies turned into states, their new constitutions contained language that authorized various forms of taxation. Some states taxed based on value of the land, while others based it on the quality. Furthermore, some state's property tax was based on real property, on the improvements, a combination, and or other categories of personal property. In North Carolina, land was taxed uniformly according to the number of acres, while lots in towns were taxed based on value. Since the Tennessee Territory was originally part of North Carolina, Tennessee's Constitution and laws mirrored that of North Carolina. The Tennessee Constitution of 1796 stated, "All lands are liable to be taxed, and they shall be taxed uniformly, so that no 100 acres shall be taxed higher than another, except town lots."

In Tennessee, as in other states, as the population grew and time progressed there was growing pressure for increased fairness in the taxing system based upon people's ability to pay the tax. This resulted in the case of property taxes being more closely aligned with the value of property. During the 19th century, many states, including Tennessee, amended the taxing sections of their constitutions to ensure that property taxes be based on valuations of property (in Tennessee, "according to value"), not just the quantity of property. This provision was found in the state's 2nd and 3rd Constitutions. Today, the 3rd Constitution, written in 1870, is still the fundamental charter for the State of Tennessee. Section 29 of the Constitution gave the General Assembly power to authorize local taxes similar to those levied by the state, thus local authority to collect property tax.

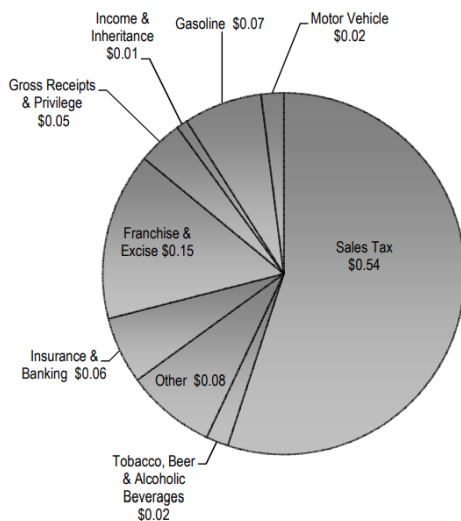
Beginning in 1920, the state revenue system slowly started adding new taxes. The added taxes diversified the state's revenue by being imposed on gasoline, corporate profits, tobacco products, certain forms of income, beer, alcoholic beverages, and retail sales. And then in 1949, the General Assembly repealed the State Property Tax, as other the taxes imposed exceeded the revenue collected from the property tax.

However, local governments still rely on property taxes. In fact, property tax remains the most important source of local tax revenue in all but one county according to a 2011 Tennessee Advisory Commission on Intergovernmental Relations (TACIR) report. The exception is Sevier County in which local sales tax revenue exceeds property tax revenue. Furthermore, a separate TACIR report from 2007 shows that local government reliance has grown over time as exhibited by the following graph:

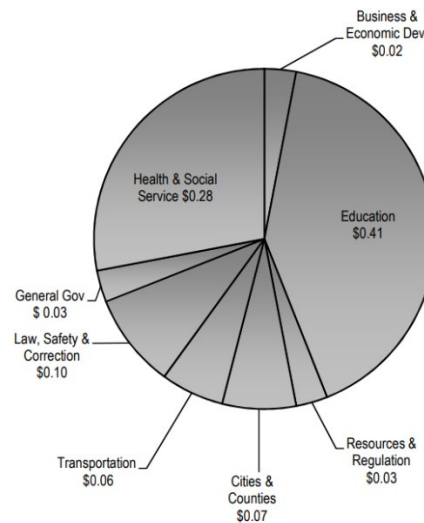


The state budget is divided into separate funds that go to pay different items and the revenue comes from different places. The General Fund, as aptly named, generally pays for the overall workings of the state and the taxes/fees that go into the General Fund are mostly sales and use tax (37.9% of the Fund), taxes on businesses including Franchise and Excise tax (28.3%), Commerce and Insurance Fees (10.9%), other fees applied by the different departments (12.6%), along with other taxes. The Education Fund's revenue comes from a portion of the sales and use tax (94.9% of the Fund), the tobacco tax (4%) and mixed drink tax (1.1%). The Highway Fund's revenue mostly comes from gasoline (45.9% of the Fund), diesel (19.6%) and vehicle registration (28.1%) taxes. The state also performs the duty of collecting some of the tax dollars due to local governments, such as the local portion of the sales and use tax and gasoline tax. In the state budget about half of the funding comes from state tax revenue while just under 40% comes from federal funds, the remaining is made up from revenue from current services the state performs and charges for. The following graphs show where state revenue comes from and how it is spent (FY19-20):

Where Your State Tax Dollar Comes From



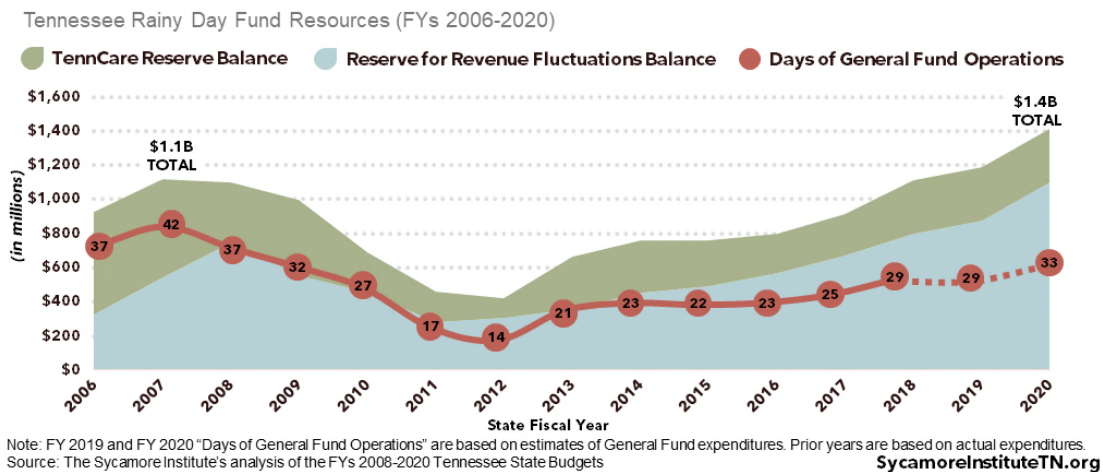
Where Your State Tax Dollar Goes



In the 2014 election cycle, Tennesseans approved a constitutional amendment prohibiting a state tax on personal income. However, the measure did not affect the what is known as the Hall Tax. The Hall Tax is a state tax on capital gains, interest and dividend income. Historically, the Hall Tax was set to 6%. The Hall Income Tax will be eliminated by 2021 in a process of being phased out by the General Assembly. Beginning January 1, 2017, Public Chapter 181, Section 13 of the IMPROVE Act reduces the Hall income tax rate by 1% each tax year through the 2021, starting at 4% for 2017. The Hall income tax is fully repealed for tax years beginning January 1, 2021. The IMPROVE Act also lowered sales tax rate on food and food ingredients from 5% to 4%, plus the applicable local tax rate. Tennessee's sales tax can be a total of up to 9.75%. The state's portion of sales tax is 7% and local jurisdictions (counties and cities) can add up to 2.75%. Tennessee's gift tax was repealed effective January 1, 2012, and state's estate tax was repealed effective January 1, 2016.

During the 2019 legislative session a major revenue increase in the budget is to recognize new out-of-state sales tax revenue from online sales using a conservative projection of \$44.69 million for Fiscal Year 19-20. This along with some other, smaller, new sources of revenue allowed the General Assembly and the Governor to fund some other initiatives. The tax cuts included in the current budget were the farm sales tax provisions (water and trailers), elimination the amusement tax on gyms, removing sales tax on fiber optic cable used for internet access, exempted 15 professions required to the pay the \$400 professional privilege tax, exempting state and local sales tax on the lease of a dumpster or other container for waste removal, and repeals the ammunition tax on shotgun shells and metallic cartridges. Looking into the future, there seems to be appetite by the General Assembly to completely do away with the professional privilege tax, which in the Fiscal Year 2018-2019 represented 4.2% of the General Fund revenue.

Another major accomplishment in 2019 pertaining to the budget is the deposit into the state's Rainy Day Fund. The FY 19-20 budget places \$225 million into the Rainy Day Fund. This will put the total to \$1.1 billion. There is also \$300 Million in the TennCare Reserve. The following graph, from the Sycamore Institute of Tennessee depicts the Rainy Day Fund amount compared to the number of days of General Fund operations the Rainy Day Fund represents since 2006.



A legislative priority for Farm Bureau in 2019 but was not successful in passing was SJR3, by Senator Frank Niceley. SJR3 would set into motion the process of amending the State Constitution to prevent the state from collecting a state property tax on individuals. Farm Bureau did not initiate the filing of SJR3 but tried to assist the sponsor to pass the legislation. To amend the State Constitution, a resolution must pass two separate General Assemblies (the second of which it must pass by 2/3rds majority) and then be approved by a majority of voters in an election of the governor.

SJR3 started a discussion among many in the Senate Finance Committee about the financial security of the state. Even though the state is in a very sound fiscal position currently, members of the committee discussed what the state would do if there is a need for more revenue for the state in a downturn in the economy. Additionally, committee members were concerned about what credit agencies would think of limiting another option for state revenue as the state has a Triple A bond rating from each of the three major credit rating agencies. Members of the committee would like to take time to discuss long-term effects of limiting another potential revenue source for state government, even though the state has not used a state property tax on individuals for 70 years.

The discussions with committee members highlighted the need for SJR3. In the future when the state finds itself in need of new revenue, Farm Bureau holds the position that a state property tax should not be an option. The burden of filling the gap in a budget deficit should not be put upon farmers and property owners of the state. Furthermore, local governments are mostly funded through property taxes. SJR3 was assigned to the General Subcommittee of Senate Finance, Ways, and Means Committee which effectively ended the discussion for 2019. However, SJR3 can be brought back up for discussion in 2020. Farm Bureau policy states we strongly oppose a state property tax, but the policy does not mention a constitutional amendment on the issue.

Questions

1. Should the state impose a property tax on individuals?
2. If the state were to have a constitutional amendment prohibiting a property tax, do you believe the state has enough other options to pursue for revenue?
3. Should Tennessee Farm Bureau Policy directly reference a state constitutional amendment prohibiting a state property tax?

Farm Bureau Policy

State and Local Taxes (Partial)

We strongly oppose a statewide property tax and a property tax based on the value of a vehicle. A flat-rate wheel tax is more acceptable to our membership because it broadens the tax base.

Long-term capital gains should be taxed at a reduced rate. We applaud the phasing out of the Hall Income Tax through 2021. Rental income should not be made a part of the Hall Income Tax. If the revenues of both local and state government are considered in a reform proposal, property taxes should be replaced.

Since we cannot foresee all of the various combinations of taxes in an effort to reform our tax structure, the Tennessee Farm Bureau Federation's Board of Directors should analyze the economic impact to Tennessee farmers of any proposal. The Board should adopt the position with the best long-term economic interest of Tennessee farmers.

*Produced in 2019 by the Tennessee Farm Bureau Federation
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