S.C. NO. 27351

IN THE SUPREME COURT OF THE STATE OF HAWAIʻI

COUNTY OF KAUAʻI BY ITS COUNTY ATTORNEY LANI D.H. NAKAZAWA; Plaintiff-Appellee, vs. BRYAN J. BAPTISTE, MAYOR, COUNTY OF KAUAʻI, *et al*., Defendants-Appellees, and GORDON G. SMITH, *et al.*, Intervenors-Appellants.	CIVIL NO. 04-1-0272 (Declaratory Judgment) APPEAL FROM FINAL JUDGMENT (filed May 20, 2005) FIFTH CIRCUIT COURT HONORABLE George Masuoka, Judge

MOTION OF REASON FOUNDATION, AMERICANS FOR TAX REFORM, AMERICANS FOR PROSPERITY AND NATIONAL TAXPAYERS UNION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

EXHIBIT "A"

CERTIFICATE OF SERVICE

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MOTION OF REASON FOUNDATION, AMERICANS FOR TAX REFORM, AMERICANS FOR PROSPERITY AND NATIONAL TAXPAYERS UNION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

Pursuant to Haw. R. App. P. 28(g), Reason Foundation, Americans For Tax Reform, Americans For Prosperity and National Taxpayers Union ("Amici") respectfully move for an order permitting them to submit the Brief Amicus Curiae attached hereto as Exhibit "A" in the above-captioned appeal.

IDENTITY AND INTEREST OF AMICI CURIAE

Reason Foundation, Americans For Tax Reform, Americans For Prosperity and National Taxpayers Union are national 501(c)(3) organizations that conduct research and public education on tax policy, law, and government service delivery. Their lengthy and broad experience and knowledge of the law and economics of tax limitations and interest in public policy decisions lead them to lend their research knowledge and expertise to local citizens, community groups, and local governments involved in decision making about tax and tax limitations policy.

AMICI'S ABILITY TO AID RESOLUTION OF THIS CASE

Amici believe that their public policy perspective and litigation experience in constitutional, voting rights and taxation law will provide a helpful perspective to aid the Court in resolution of this case.

For the above reasons, Amici request that its motion to file an amicus curiae brief be granted.

DATED: Honolulu, Hawaiʻi, September 19, 2005.

Respectfully submitted,

STEVEN B. JACOBSON
Attorney for Amici Curiae

EXHIBIT "A"

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COUNTY OF KAUAʻI BY ITS COUNTY ATTORNEY LANI D.H. NAKAZAWA;	)	CIVIL NO. 04-1-0272 (Declaratory Judgment)
Plaintiff-Appellee,	)	APPEAL FROM FINAL JUDGMENT (filed May 20, 2005)
vs.	)	
BRYAN J. BAPTISTE, MAYOR, COUNTY OF KAUAʻI, et al.,	)	FIFTH CIRCUIT COURT
Defendants-Appellees,	)	HONORABLE George Masuoka, Judge
and	)	
GORDON G. SMITH, *et al.*,	)	
Intervenors-Appellants.	)	

BRIEF AMICUS CURIAE OF REASON FOUNDATION, AMERICANS FOR TAX REFORM, AMERICANS FOR PROSPERITY AND NATIONAL TAXPAYERS UNION

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TABLE OF AUTHORITIES

I. Introduction

Pursuant to Haw. R. App. P. 28(g), Reason Foundation, Americans For Tax Reform, Americans For Prosperity and National Taxpayers Union ("Amici") respectfully submit their Brief Amicus Curiae in support of Intervenors-Appellants, and urge reversal of the judgment of the court below.[1]

II. Property Tax Limitations and Local Government Services.

When voters in the County of Kaua'i voted in favor of a Charter amendment limiting real property taxes on resident homeowners, a number of issues on the merits of the amendment remained controversial. One key issue was a contention that a property tax limitation would fundamentally undermine County revenues and ability to delivery vital public services.

This is not a new assertion, but an argument that goes back to the successful tax revolts during the Great Depression.[2] The tax revolts of that era are little known, but were very successful.[3] Indeed, "In 1932 and 1933 alone, 16 states and numerous localities enacted property tax limitations."[4] Even back then, debates over the impact of tax cuts or limitations on public services were a crucial part of the issue.[5]

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1 Dr. Adrian Moore prepared the analysis contained in this Brief.

2 David T. Beito, *Taxpayers in Revolt: Tax Resistance During the Great Depression* (Chapel Hill: University of North Carolina Press, 1989) provides a thorough history of the depression era tax revolts.

3 Mark Thornton and Chetley Weise, "The Great Depression Tax Revolts Revisited, *Journal of Libertarian Studies*, vo.15, no.3 (2001), pp.95-105, extends Beito's work (see n.2) by examining the conditions of the success of the depression era tax revolts and connections to the repeal of prohibition and to the tax revolts of the 1970s.

4 Arthur O'Sullivan, Terri A. Sexton, and Steven M. Sheffrin, *Property Taxes and Tax Revolts: The Legacy of Proposition 13* (Cambridge: Cambridge University Press, 1995), p. 1.

5 Beito, *supra*, at 60-164.

Modern debates over tax limitations have seen the re-emergence of allegations that reductions in revenue will cripple vital government services.[6] The crux of the arguments is that the public demands increasing levels of public services, and that elected leaders must be allowed to levy taxes sufficient to pay for services demanded or overall quality of life and economic growth will decline.

Taxpayer opinion calls this assertion into question, however. A survey taken on the 20th anniversary of California's Proposition 13 found that California taxpayers had a different opinion of the impact of limiting property taxes.

> A PPIC survey conducted this month . . . found Californians still largely favor most aspects of the initiative. Thirty- eight percent said that property tax limitations imposed by Prop. 13 have had a good effect on local government services, compared with 23 percent who thought the effect had been negative.[7]

Indeed, there are many ways government can respond to property tax limitations.

> The resulting challenge [of property tax limitations] to local budgets has been met in three ways. First, so long as state tax revenues were increasing, the states were able to increase their aid to local governments. Second, several states allowed local governments to enact new taxes. Pennsylvania, for example, empowered the city of Philadelphia to enact a one-percent sales tax and a limited wage tax on its citizens. By far, however, the most important response to local budget challenges has been innovation and cost saving in service delivery. In the name of "reinventing government," many local services were privatized, new labor agreements were negotiated and fees for governmental services were increased to meet the real costs of the service.[8]

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6 Robert Kuttner, *Revolt of the Haves*, (New York: Simon and Shuster, 1980), p.80ff provides an early example of these arguments in the wake of Proposition 13 in California and the ensuing wave of property tax limitations proposals of the late 1970s. A specific version of the argument can be seen in Dirk Johnson, "Taxpayer Revolt in Colorado Raises Alarms about Lost Services," *New York Times*, November 15, 1992, p.18. More recently, Thomas A. Downes and David N. Figlio, "Do Tax and Expenditure Limits Provide a Free Lunch? Evidence on the Link Between Limits and Public Sector Service Quality," *National Tax Journal* , vol 52, no. 1 (1999) pp. 113-28 extensively reviews the literature investigating the impact of tax and expenditure limits on government services.

7 "Studies Find Some Major Criticisms Of Prop. 13 To Be Unfounded," Public Policy Institute of California, September, 1998, http://www.ppic.org/main/pressrelease.asp?i=354.

8 Ellis Katz, "Responses to Change by State and Local Government: Contemporary Experiments in the Laboratories of Democracy," *Issues of Democracy*, vol. 8, no.2, 2003.

In fact, there are four main arguments to counter to the assertion that property tax limitations undermine economic growth and government services.

1. Jurisdictions which have passed tax limitations often experience above average economic growth.
2. Jurisdictions which have passed property tax limitations do not see declines in government revenue.
3. There is little relationship between the level of government revenue and the quality of government services.
4. Limitations on revenue lead to changes in the way services are delivered to cope with new fiscal realities.

A. **Tax Limitations and Economic Growth**

Colorado's tax and expenditure limitation is considered by many to be the most successful and effective such statewide limit in place. It passed in 1992, to dire predictions of doom for the state economy.[9] But between 1995 and 2000 Colorado experience the fastest growth in state product (state equivalent of GDP) of any state in the nation and the second fastest growth in personal income.[10]

California's Proposition 13 was more similar to Kaua'i's charter amendment, strictly a limit on property taxes. UCLA forecasters predicted that Proposition 13 would increase unemployment and damage the state economy.[11] But in the years following the passage of Proposition 13 California's unemployment rate fell and the state's economic growth exceeded the national average.[12]

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9 Stephen Moore and Dean Stansel, "The Great Tax Revolt of 1994," *Reason*, October 1994.

10 Based on analysis of data from the U.S. Bureau of Economic Analysis in Michael J. New, *Proposition 13 and State Budget Limitations: Past Successes and Future Options*, CATO Institute Briefing Paper No.83, (Washington, D.C.: CATO Institute, 2003).

11 Alvin Rabushka and Pauline Ryan, *The Tax Revolt*, (Stanford: Hoover Institution Press, 1982), p.26.

12 *Id*. at 84, 86.

Reductions in taxes tend to spur economic activity and growth, not retard them.[13] This makes sense. In general high taxes reduce the money available for economically productive uses. High property taxes reduce the incentive for those most likely to put property to productive uses because the cost of those taxes is dearer to them as it draws money away from the business or property improvements that make it productive.

B. Property Tax Limitations and Government Revenue

Imposing property tax limitations does not necessarily reduce government revenues. Resultant increased economic growth can result in increased government revenues. Moreover, simple tax limitations like Proposition 13 soon evolved into tax and expenditure limitations because limiting the revenues available from one tax source can lead to shifts to other revenue sources rather than spending reductions.[14]

In California, total state and local revenues (in constant 2000 dollars) were $125 billion in 1977, the year before Proposition 13 passed, remained near that level until 1983, and then began to climb, to $270 billion in 2000.[15] While during those years the state's population grew, in per-capita terms, total real public revenues in California were flat between 1978 and 1998.[16]

In the face of property tax limitations, governments shift to other revenue sources. Often this means increases in state aid or local sales or income taxes.[17] In California property tax revenues fell from 5.25 percent of state personal income the year before Proposition 13 passed to

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13 *Do Taxes Effect Economic Growth*, National Center for Policy Analysis, http://taxesandgrowth.ncpa.org/hot_issue/growth/, reviews a series of studies and government reports examining various data on tax reductions and economic performance that almost universally find that tax reductions spur economic activity.

14 See Jason Clemens, et. al., *Tax and Expenditure Limitations The Next Step in Fiscal Discipline*, (Vancouver: Frasier Institute, 2003), and Daniel R. Mullins, "Tax and Expenditure Limitations and the Fiscal Response of Local Government: Asymmetric Intra-Local Fiscal Effects," *Public Budgeting & Finance*, Winter 2004, pp.11-47.

15 New, *Proposition 13 and State Budget Limitations*, p.5, based on calculations from Census data.

16 Michael A. Shires, John Ellwood, and Mary Sprague, *Has Proposition 13 Delivered? The Changing Tax Burden in California*, (San Francisco: Public Policy Institute of California, 1998).

17 Katz, *supra*.

2.75 percent 20 years later, while during the same period sales and income tax revenue climbed from 4.4 percent of state personal income to 6.3 percent.[18]

At the same time, there was a pronounced shift to other local discretionary revenue sources--enterprise revenues, assessments, regulatory fees and taxes, fines and penalties, general service charges, and special taxes such as business license taxes, franchise taxes, real property transfer taxes, and transient lodging taxes.[19] Indeed, so aggressive were local governments at increasing special taxes that in 1996 voters passed Proposition 218 that required a popular vote for all local taxes and a two-thirds majority to approve special taxes.

At the same time, many governments react to tax limitations by increasing reliance on fees. User fees are superior to general taxes for many services, such as parks, water, electricity, etc., because the user of the service or the beneficiary pays for the costs of their usage.

> In addition to legal constraints on state and local taxes, fees also appear to have gained in political popularity with both state and local lawmakers and voters. Some taxpayers perceive taxes as compulsory payments for services from which they do not necessarily benefit. Fees, on the other hand, are perceived as payments for services received by the payer. Although the reality may not always be clear-cut, perceptions frequently guide public policy, and fees do not seem to have the political stigma of taxes.[20]

C. <u>Government Funding Levels and Service Quality</u>

There is little evidence that the quality of government services improves when governments spend more money on them, or of the corollary that reducing spending reduces service quality. Research into school spending is a good example, where "existing research relating spending to student outcomes suggests that the relationship between spending and outcomes is weak, if present at all."[21]

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18 New, *Proposition 13 and State Budget Limitations*, p.4 based on calculations from Census data.

19 Michael A. Shires, *Patterns in California Government Revenues Since Proposition 13*, (San Francisco: Public Policy Institute of California, 1999).

20 National Conference of State Legislators, *The Appropriate Role of User Charges in State and Local Finance*, 1999.

21 Downes and Figlio, "Do Tax and Expenditure Limits Provide a Free Lunch," p. 118.

Similar conclusions come from research into other public services. A study of public transit finds:

> These points are illustrated by an analysis of costs at 109 U.S. public transit agencies. The analysis showed that unit costs (costs per mile) vary significantly between public transit agencies. The most expensive public transit agencies spend more than double that of the most efficient public transit agencies in cost per mile. Further, the analysis shows that cost increases vary greatly (costs per mile increased in a range of from 35 percent to more than 100 percent --- inflation was 54 percent). These differences cannot be explained by geographical differences or by differences in service quality.[22]

This same analysis of transit spending and service quality also found that:

> There was, however, a relationship between new revenue available to the public transit agency and the extent of the cost increase. Generally, from 1979 to 1988 the higher the increase in revenues, the greater the cost increases. (Chart: "Public Unit Cost Increases Compared to Increases in Funding")
>
> - Of the 82 agencies that received an increase in funding (inflation adjusted), only six kept their costs within inflation.
> - Of the 27 agencies that received a decrease in funding, nine kept their costs within inflation. Seven of the nine had revenue increases of less than ten percent.[23]

This is a demonstration of the principle that government costs tend to rise to meet revenues available.

Costs to provide a given government service are not fixed, and some governments provide the same service at much lower cost. A recent analysis of the efficiency of government

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22 Wendell Cox & Jean Love, "Controlling the Demand for Taxes," *The Public Purpose*, May 1996.

23 *Id*.

services in the 50 largest cities in the United States found wide variation in the cost effectiveness of local government services.[24]

D. Changing Service Delivery to Meet Fiscal Realities

> By far, however, the most important response to local budget challenges [caused by property tax limitations] has been innovation and cost saving in service delivery. In the name of "reinventing government," many local services were privatized, new labor agreements were negotiated and fees for governmental services were increased to meet the real costs of the service.[25]

If the cost of government services is not fixed, then clearly there must be ways to change service delivery to cope with tax limitations. There is ample room for maintaining service quality while holding costs steady. Outsourcing and privatization of services is a well established means of reducing the costs of service delivery. Other options exist as well. A wide range of service structures and public-private partnerships arise as a means of dealing with scarce resources for public services. A study of tax limitations impact on fire protection services found that tax limitations made it 11 percent more likely that a typical fire department is volunteer and 10 percent more likely they engage in fund raising.[26]

III. Conclusion

Experience with property tax limitations, especially California's Proposition 13, demonstrates that such limitations do not jeopardize government service delivery. Tax decreases tend to stimulate the economy and lead to innovations in revenue sources and service delivery.

Faced with a property tax limitation, the County of Kaua'i has several options to cope:

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[24] Adrian T. Moore, James Nolan, and Geoffrey F. Segal, "Putting Out The Trash: Measuring Municipal Service Efficiency in U.S. Cities," *Urban Affairs Review*, Vol. 40, No. 5, 2005.

[25] Katz, *supra*.

[26] Douglas C. Bice and William H. Hoyt, "The Impact of Mandates and Tax Limits on Voluntary Contributions to Local Public Services: An Application to Fire-Protection Services," *National Tax Journal*, vol.48, March 2000, pp. 79-104.

1. Shift to other revenue sources: Sales and income taxes are less distortionary than property taxes. User fees are superior to taxes because they charge the users of services for their usage and do not charge non-users.
2. Rethink the scope and type of services provided and focus on those that are critical to quality of life.
3. Explore alternative service delivery arrangements to control costs and maintain service levels.

All of these mechanisms have been used by governments facing property tax limitations and they have worked. They will work for Kaua‘i County as well.

DATED: Honolulu, Hawai‘i, ____________________, 2005.

Respectfully submitted,

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Attorney for Amici Curiae

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Defendants-Appellees, and)	HONORABLE George Masuoka, Judge
GORDON G. SMITH, *et al.*,)	
Intervenors-Appellants.)	

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this date, a true and correct copy of the foregoing document was duly served upon the following individuals by mailing said copy, postage prepaid, to their last known addresses as follows:

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