

TAX BASE SHARING

The drive for increased property, income or in some cases sales tax revenue, can lead local governments to make land use decisions that conflict with other planning and economic development goals. A community might reject much needed affordable housing in favor of expensive homes, for example, or forego office building with high-paying jobs in favor of big box retail stores with low-wage jobs, in anticipation of generating more tax revenue with a comparatively smaller burden on public services.

The quest for revenue-generating development creates competition among neighboring jurisdictions, which may engage in bidding wars to offer developers the biggest tax breaks or least stringent environmental regulations. From a regional perspective, providing subsidies for businesses that have already decided to locate in the area is unnecessary and even destructive. A big box store, for example, will cannibalize sales from existing local businesses and shopping centers and, for the region as a whole, there will be no net gain in economic activity.

In metro areas, like Dayton, the “fiscalization of land use” or “cash box zoning,” as the problem is known, fosters sprawl and polarization. Some jurisdictions are winners; others are losers. New suburbs on the urban fringe with extensive new commercial development and relatively affluent homes will have high quality public services with a relatively low tax rate. The central city and older suburbs, with declining commercial centers and lower-income families, will be forced to impose higher tax rates and deliver poorer quality services. This disparity tends to snowball and engender a cycle of sprawl as more middle-income families flee to the suburban fringe.

When all communities in a region like the Dayton Region independently seek to maximize their tax base, a number of problems arise:

- **Accelerated outmigration:** New communities at the edge of the metro area are under pressure to build their tax base, so they encourage the migration of development from older communities. In a slow-growth region like Northeast Ohio, this can be a zero-sum game where new developments (like shopping centers) cannibalize old. This widens fiscal disparities, as new communities grow wealthier at the expense of older communities.
- **Competition rather than cooperation:** In a fragmented region, there's little incentive to cooperate for the greater good. The region struggles to achieve more unified, "all for one and one for all" voice when pursuing economic development.

- **Distorted land use:** Some communities, such as those with a lot of environmentally sensitive land, are pressured to develop at greater intensity than they should. There are costs to whole region when development doesn't happen in the most suitable places.

Regional tax sharing can help to reduce these problems by allowing all communities to benefit from growth anywhere in the region.

Regional tax-base sharing offers one way to alleviate this problem. Under tax-base sharing, all of the municipalities within a metropolitan area agree to share tax proceeds from new development. This eliminates interregional competition; facilitates other planning goals such as preserving open space or maintaining a vibrant downtown; encourages suburbs and central cities to cooperate on regional economic development goals; and leads to a more equitable distribution of tax burdens and public services.

State legislation is generally required to implement regional tax-base sharing. Two regions of the U.S. have adopted this approach: the Twin Cities metropolitan area in Minnesota and the Hackensack Meadowlands area in New Jersey. The California state legislature is currently considering a bill that would establish tax base sharing in the Sacramento metro area.

Minneapolis-St. Paul Fiscal Disparity Plan

Regional tax-base sharing was implemented in the seven-county Twin Cities metro in 1971. Each community contributes 40 percent of the growth of its commercial and industrial property tax base after 1971 to a regional pool. The funds are redistributed based on a formula that takes into account a jurisdiction's population and fiscal capacity (defined as per capita real property valuation).

According to former Minnesota State Representative Myron Orfield, an expert on regional revenue-sharing, the system has reduced tax-base disparities among Twin Cities communities from 50:1 to roughly 12:1. The system has not eliminated disparities, because 60 percent of any new revenue from commercial development remains in the host community. Only about 20 percent of the region's total tax-base is shared.

The Minneapolis- St. Paul region provides a clear example of how a regional tax-base sharing program is successfully implemented. Because of the Fiscal Disparity Plan's success and inventiveness, other metropolitan regions have attempted to mimic plan, yet Minneapolis- St. Paul remains the only region with this type of model.

Advantages of Tax Base Sharing

Tax- base sharing has a number of advantages over state aid programs commonly used to redistribute funds and address tax capacity disparities. First, tax- base sharing does not remove local control over tax rates and collection. Instead, tax- base sharing equalizes tax capacity disparities by using existing taxing mechanisms that municipalities are already comfortable with and have experience using. Second, tax- base sharing reallocates money to jurisdictions from a single, common pool. The existing system of state aid programs is complicated and fractured. Furthermore, tax- base sharing produces more efficient budget decision outcomes than current the system of inter-jurisdictional competition for commercial and industrial development. Fourth, tax- base sharing is flexible. Tax base sharing avoids migration issues and when implemented regionally, tax base sharing does not involve complicated aid formulas to address urban and rural areas very different needs.

Additionally, research results suggest that tax- base sharing can be more effective at reducing tax disparities than current state aid programs. Economic simulations indicate tax sharing reduces tax capacity disparities by 2 percentage points for each point of shared revenues. Existing aid programs only reduce tax base disparities by half a percentage point for every percentage point of aid.

Tax- base sharing works just as the name suggests. Each municipality contributes a portion of their tax base to a regional pool. The contribution can be either a percentage of growth in tax base or as a percentage of the current tax base. The affected portion of the tax base can include all types of taxes or can be limited to particular ones. Once the contribution amount and type of tax base affected have been decided, each municipality within a region then receives money from that pool based upon a set of established criteria. The criteria can include: tax capacity, service costs, land-use decisions or other indicators

Legislative History

The Minnesota Fiscal Disparities Act of 1971 was an innovative attempt to address growing concerns within the Minneapolis- St. Paul region. Increasing property tax rates, tax- base and tax- rate disparities, and interjurisdictional competition for development within the region had combined to place an inordinate strain on many municipality's budgets. After a long, bitter legislative and court fight, the Minnesota Fiscal Disparity Act resulted in the Fiscal Disparity Plan. To date, the Minneapolis- St. Paul is the only metropolitan area in the United States that has successfully implemented such a regional tax- base sharing scheme.

Republican Charles R. Weaver, representative from Anoka- a low tax, suburban community, introduced the bill in 1969. At first the bill passed easily through the Minnesota State House, but the State Senate refused to take the bill up. The Senate's initial trepidation certainly was a harbinger of the fight to come in later years. After the first setback in 1969, the fiscal disparity bill was introduced again in 1971. During the second attempt, the bill faced vociferous opposition. A coalition of central, poor suburban and rural legislators provided support for the bill. But they were met by legislators from property wealthy suburban areas.

Critics were particularly aghast that their communities would have to share part of their commercial property base with communities that seemingly could not manage their own finances. One suburban mayor wondered, "How can metro government take 40% of what we have and give it to those who can't operate on 100 percent? Other legislature's criticisms compared the bill with communism. Some particularly ardent critics felt that the bill represented "community socialism or that it was "nothing more than creeping communism. One town board chairman went so far as to say that, "the fiscal disparities law will destroy the state.

Again the bill passed through the State House, though the vote was closer than during the previous attempt in 1969. In fact during the 1971 legislative session, the bill had 24 fewer supporting votes. After a particular rancorous debate in the Senate, the bill narrowly passed. Almost immediately, suburban communities brought suit against the plan. The trial court found the bill unconstitutional, though the law was upheld by the appeal court. Finally, in February 1975, the fiscal disparity law went into effect.

How the Fiscal Disparity Plan works

First, the plan applies to all taxing jurisdictions within the seven county, Minneapolis- St. Paul area. This amounts to 186 cities, villages and townships, 48 school districts, and 60 other taxing authorities. Each jurisdiction is required to contribute 40% of the increase in value from its commercial- industrial property since 1971 to a common, regional pool. Residential property tax increases are not included in the fiscal disparity plan. Each year, a jurisdiction receives a share of money from the pool. Essentially, communities that are experiencing rapid commercial or industrial growth are required to share the benefits with communities whose economies have stagnated.

There are a number of criteria used to determine the amount that each municipality receives. The various criteria include the population and the ratio of the total market value of property per capita in the jurisdiction and the average market value of property per capita in the region. Money is then reallocated on the basis of inverse net commercial tax capacity. Municipalities that have lower

than average market value per capita receive a share of the pool that is greater than their share of the regional population.

The Metropolitan Council, the regional government, believes that tax- base sharing with the Minneapolis- St. Paul makes sense because the region is just one large, interconnected economy. While commercial- industrial development provides needed tax revenue for particular governments, these developments are largely funded through regional and state financing. Without tax- base sharing, only municipality with the new development would benefit, not the other parts of the region that also contributed. The Metropolitan Council believes that, "the ideas underlying tax- base sharing is to allow all cities to share in the commercial- industrial development that is, to a large extent, the result of the regional market and public investments made at the regional and state levels. Thus regional tax- base sharing prevents one municipality benefiting from growth at the expense of the rest of the region. Certainly specific municipalities do not gain the full benefit from the development that occurs within their borders, but proponents argue that region wide benefits more than outweigh any financial loss associated with the fiscal disparity plan.

Outcomes

Orfield in his research finds that the plan has been largely successful at narrowing the regional business tax rate disparities. In 2000, 28% of the region's commercial- industrial tax base was shared between jurisdictions. Gini-coefficient measurements indicate that the program reduced tax base disparities by close to 20%. Furthermore, the ratio between the ninety- fifth to fifth percentile tax base declined by 25%. Finally, within the entire region, tax base disparity has been reduced from 50 to 1 to approximately 12 to 1, but for cities with populations over 9,000 people the ratio of tax base disparity dropped from 18 to 1 to 5 to 1, as measured by per capita commercial industrial value per capita.

The plan provides fiscal benefits for the majority of municipalities in the region. Annually, the plan pool contains roughly 20% of the regional tax base. In 1998, this money was distributed to 137 cities, villages, and townships funding while only 49 were net contributors. Since its inception, the major fund contributors include the area's wealthiest suburbs, such Bloomington, Minnetonka, Eden Prairie, Edina, and Plymouth. Outlying, rural communities, St. Paul and many inner- ring suburban communities have traditionally been the primary recipients. Minneapolis has moved from the primary net recipient in 1980 to the largest contributor in 1990 and back to a net recipient by 1995.

Conclusion

While the Minneapolis- St. Paul region remains the only metropolitan area to have successfully implemented a regional tax base sharing plan, other cities and metro areas can learn from the Fiscal Disparity Plan. The Plan's outcomes certainly attest to the positive impacts that tax base sharing can have for a region. More importantly, though, a tax base sharing program is an adaptable entity that can include portions of the tax base or distribution methods according to a region's needs. This allows regions to create the most efficient distributional system.