MINUTES

(Subject to Approval by the Committee)

TAX EXEMPTIONS INTERIM COMMITTEE

Joe R. Williams Building, East Conference Room, Boise, Idaho

August 2, 2007

The meeting was called to order at 9:03 a.m. by Co-chair Representative Dennis Lake. Other committee members present were: Co-chair Senator Brent Hill, Senator Joe Stegner, Senator Tim Corder, Senator Lee Heinrich, Senator Jeff Siddoway, Senator David Langhorst, Senator Diane Bilyeu, Representative Gary Collins, Representative Jim Clark, Representative Mike Moyle, Representative Dell Raybould, Representative Nicole LeFavour, and Representative Bill Killen. Staff members present were Mike Nugent, Eric Milstead, and Jennifer O'Kief.

Others present included: Jack Lyman, Idaho Mining Association; Skip Smyser, Connolly & Smyser, Chtd.; Jeremy Pisca, Evans Keane, LLP; Jim Farrel, Lynn Young and Joe Gallegos, AARP; Bob McQuade, Ada County Assessor; John Watts, Veritas Advisors; Phil Syrdal, BioIdaho; Mike Huntington, Intermountain Gas Co.; Robin Nettinga, Idaho Education Association (IEA); Don Reading, Ben Johnson and Associates; Russ Hendricks, Farm Bureau; Keith Allred, President, The Common Interest Dan John, State Tax Commission; Charlie Brown, Retired Educators' Association of Idaho; Alex LaBeau and Mark Dunham, Idaho Association of Commerce & Industry (IACI); Paul Jackson, Farmers Insurance; Randy Nelson, Associated Taxpayers of Idaho (ATI); Tom Ryder, J. R. Simplot Company; Judith Brown, Director, Idaho Center on Budget and Tax Policy, United Vision for Idaho; Dr. Stephen Cooke, University of Idaho, Department of Agricultural Economics & Rural Sociology; Toni Lawson, Idaho Hospital Association (IHA); Norm Semanko, Idaho Water Users Association; Brent Olmstead, Milk Producers of Idaho; Dawn Justice, Idaho Bankers Association; Phil Davidson, Post Register; Jim Rehder, Idaho County Commissioner; Representative Brandon Durst, District 18; Jessica McDonald and Kevin Price, Idaho Association of Realtors (IAR); Jan Rogers, Southern Idaho Economic Development Organization(SIEDO); Bibiana Nertney, Randy Shroll, Carl Wilgus, Jim Ellick, Don Dietrich and Capree Bell, Idaho Department of Commerce; Sharon Burke, Idaho Association of Counties; Mike Ferguson, Division of Financial Management (DFM); Ralph Hallquist, Boise Metro Chamber of Commerce; Robb Hicken and Eddie Kovsky, Idaho Business Review; Ken Dey, Idaho Statesman; and Steve Rector, Idaho Housing and Finance Association (IHFA).

Randy Shroll, **Manager, Business Development, Idaho Department of Commerce**, was the first speaker. **Mr. Shroll** took the privilege of introducing **Mr. Jim Ellick**, the new Director of the Department of Commerce. **Mr. Ellick** gave a brief history of his background, of which thirty-two years had been spent in the technology sector in the Silicon Valley. He invited each of the members to stop by his office..."My door is always open."

Mr. Shroll provided a packet including a PowerPoint presentation. A copy is available in the Legislative Services Office. He said they currently have about ninety-five companies they are working with ranging from Fortune 100 companies to small manufacturers looking to expand or relocate in Idaho. **Mr. Shroll** referred to an annual survey taken by corporations throughout America, illustrating ratings of "site selection" factors, that are considered important when they are looking to assign a new facility. He noted that, consistently, selections among the top ten factors were labor costs, corporate tax rate, state and local incentives, tax exemptions, availability of skilled labor and proximity to major markets.

Mr. Shroll gave an example of a recent study that was done of a particular manufacturing company, showing a cost comparison of doing business in Idaho as compared to California, Washington, Kentucky and others. Some of the costs included were labor, fringe benefits, worker's compensation, insurance, unemployment insurance and utility costs. On an annual basis, there was a savings in locating in Idaho of $777,418 over California. Savings over other states that were considered ranged from $106,000 to $227,000. He said it is important that these costs remain stable.

Representative Lake asked how much of the savings are due to tax incentives. **Mr. Shroll** said that none are directly related. However, if you take these cost savings and add to them the tax savings through the investment tax credit and other tax incentives, then the number would actually grow. **Representative Lake** asked how much the "bottom line," is going to grow. **Mr. Shroll** said that it really depends on the business. **Mr. Shroll** said that they do not actually see those numbers until after the company has made the investment in Idaho, then they would apply for those tax credits.

Mr. Shroll said that another important factor for them is the ability at the local level to form urban renewal districts and offer tax increment financing. **Mr. Shroll** said that the specific tax exemptions that come up the most are the investment tax credit, sales tax production exemption, new employee tax credit, research activity credit, and other incentives, such as the Workforce Training Fund and the Directors Closing Fund.

Senator Corder asked what method is used to determine if they get paid back. **Mr. Shroll** said that they do not have a particular method. They know from the history of other communities that have used tax increment financing that when you give something up on the front end, after the bonds are paid off and those taxes go back on the roll, that money is going to be repaid and be a good return on investment. **Senator Corder** asked if they tracked whether they are goods or services or whether they are losing or gaining jobs on either side of the equation? **Mr. Shroll** said they track jobs and the quality of the jobs and payroll. But as far as a timeline when they break even and move forward, there is currently nothing in place to allow them to do that. **Senator Corder** asked, "No document... that you can actually prove?" **Mr. Shroll,** "No document, but it might be something to work on, though. It makes a lot of sense."

Representative LeFavour asked what kinds of studies had been done on large retail businesses, or incentives to relocate to the area and what the net gain or loss in jobs is in terms of local competition with similar locally-owned businesses. **Mr. Shroll** said they have not. They work primarily on commercial and industrial projects. However, they work very closely with communities with established retail companies.

Mr. Shroll noted that they have seen basically no value in the corporate headquarter investment credit.

While they have had a lot of interest in the small employers' capital investment credit, they are not aware of any companies where it has been used yet. He highlighted several reasons why businesses prosper in Idaho, some of which were: Idaho offers an inspiring lifestyle; finds and trains workers, stimulating greater profits; and augments local governments with infrastructure improvements.

Representative Killen, regarding HB261 that dealt with bio-tech companies, asked if he had made any observations. **Mr. Shroll** said that they have reviewed the bill and are familiar with the intent. He said, speaking for himself, they are always in favor of those things that give them "quivers to our quill" to help them do their job better. "Return on investment, those would be dollars wisely spent I believe."

Senator Hill asked **Mr. Shroll** what his thoughts were regarding tax savings as businesses consider the problem of our high corporate income tax rate and asked, "Do you think you would be willing to forgo some of those 'arrows in your quiver' to have a smaller quiver?" **Mr. Shroll** said that the whole idea is to be able to open the sales cycle with a client. There are many times a client will look at their website and "be gone" because of our corporate tax rate compared to other areas, and ..."We don't even know they were looking at us." If they can reach them at that point, they would be able to discuss the high corporate tax rate issue, but also discuss the other exemptions that would bring that overall rate down. He said that given the choice, the lower tax rate would be the way to go, over tax exemptions.

Senator Hill, referring to the sales tax production exemption incentive, asked if that was not a fairly common exemption in most states. **Mr. Shroll** said that it was, as was the investment tax credit. He thinks Idaho's is more progressive inasmuch as the carry-forward provision has been raised to fourteen years. **Senator Bilyeu** asked what other areas of taxation should we be looking at in order to be more competitive? **Mr. Shroll** said that really depends on the client and who the competition is and what they offer. He said that the Workforce Training Fund is one of the most useful tools they have because the availability of skilled labor is such a huge issue to many of these companies. The director's ability to have a fund to help with some of the costs of relocating or expanding is huge as well.

Mr. Shroll deferred to **Don Dietrich, Administrator, Economic Development Division. Mr. Dietrich** said they are in the process of looking at some of the more progressive tax incentives other states are considering. He commented that they appreciate what the Legislature has done for them, in allowing them to offer incentives to their prospective clients. However, they never see the backside of what is happening. They believe they have plenty of other incentives "to lean on" that the state provides to new prospective companies. The tax side of the equation doesn't often factor in heavily to what it is they do.

Senator Langhorst referred to Micron Technology and their most recent decisions to locate in Utah and Virginia and asked what the factors were for these decisions. **Mr. Dietrich** said he wasn't sure, but it could be related to specific workforce training or infrastructure issues. He does not believe it is our tax rates that are driving Micron out of Idaho. **Mr. Shroll** responded to a question from **Senator Corder** by saying that highway accessibility, one of the site selection factors mentioned, refers to quality and the overall transportation system and its proximity to markets.

Ralph Hallquist, **Boise Metro Chamber of Commerce**, was the next speaker. A copy of his complete written testimony is available in the Legislative Services Office. **Mr. Hallquist** outlined the Chamber's position on three specific tax issues.

- *Phase-out of personal property tax*. **Mr. Hallquist** said the Boise Chamber supports a phase-out of the personal property tax.

- *Oppose expansion of the sales tax on additional services*. **Mr. Hallquist** stated that the Boise Chamber opposes taxation on services because of the following: the unfair burden on those who must rely on service providers to a greater degree than other taxpayers, the competitive disadvantage and administrative burden of collection for services delivered out of state, and the competitive advantage for a business that is able to provide professional services in-house.

- *Retention of the sales tax exemption on production equipment*. **Mr. Hallquist** explained that the exemption from sales tax on tangible personal property used in production is the single most important tax incentive to the business community.

In closing, **Mr. Hallquist** highlighted the Chamber's top ten list of efforts that they support to "grow" Idaho's economy, some of which included: local tax incentives, science and technology education, bonding for transportation improvements, venture capital, etc.

Representative LeFavour, regarding removal of the personal property tax, asked what form of tax would they prefer to see businesses pay, in lieu of the potential shift of $115 million to families and other taxpayers. **Mr. Hallquist** said that because this phase-out would be stretched over multiple years, the phasing down will allow those recipient bodies to adjust their spending. Over time, there will be alternative vehicles that would be provided. **Representative LeFavour** reiterated that she would like to know what form of business tax would be preferable to personal property tax so that shift would not occur. **Mr. Hallquist** said that this would be a mechanism of softening the impact of the high corporate income tax rate on businesses. The Chamber would not support transferring that tax elsewhere on business. They would prefer to see some of the administrative burden on businesses taken away.

Representative Killen commented that the vast majority of dollars involve depreciable capital equipment which is tracked anyway for federal tax purposes, so the administrative exercise would continue regardless. **Mr. Hallquist** disagreed, explaining that the capital equipment is extremely tangible and easy to identify. The difficulty is accounting for chairs, file cabinets, software purchases, etc. **Representative Killen** asked if he would consider it to be a good compromise if the exclusion were limited to hard-to-track consumables, but retained for the large trackable items. **Mr. Hallquist** said, "Subject to further definition, absolutely."

Senator Hill, referencing the Chamber's position on the above three tax categories, commented that those items have to be paid for somehow and asked if the Chamber has discussed sufficient ways for government to raise taxes. **Mr. Hallquist** said that they believe this needs to constantly be reevaluated as the local and the global economies change. **Representative Lake** asked whether, if the policy changed to taxing services and lowering the sales tax, making it revenue neutral, the Chamber's position not to tax services would still be the same. **Mr. Hallquist** said that their position would still be the same, since this change would be subject to further definition. He noted that the smaller the business, the greater the burden.

The committee recessed at 9:57 a.m. and reconvened at 10:24 a.m.

Alex LaBeau, **President, Idaho Association of Commerce and Industry (IACI)**, was the next speaker. **Mr. LaBeau** provided a document prepared by IACI entitled, "2008 Tax Policy White Paper." A copy is available in the Legislative Services Office. Prior to the meeting, **Mr. LaBeau** had received a number of questions from **Senator Hill**. The following reflect **Mr. LaBeau's** answers to some of those questions. The first question asked was: How much reliance should be placed on sales tax vs. income tax vs. property tax, given some bordering states that have no sales tax or income tax? **Mr. LaBeau** said they need to be cautious about placing additional reliance on a specific tax because we need to be looking, not only at the competition with our neighbors, but the rest of the world. It is important to maintain low taxes in sales, income and property and, especially, low fees; government relies heavily on fees.

Another question was: Do you believe most businesses would forgo the investment tax credit (ITC) in exchange for repeal of the personal property tax? **Mr. LaBeau** pointed out that eliminating the ITC not only causes a tax increase on business but also on a wide range of individual investors, such as small business people, law firms, farmers, doctors, CPAs, etc. He said he would urge caution because all of the numbers are not in yet and it does impact people very differently. **Mr. LaBeau** answered another earlier question by saying that IACI does not support taxing services in exchange for reducing the sales tax. The current policy provides more than enough revenue to fund and administer government services more easily and reasonably fairly.

Mr. LaBeau stated that IACI proposes that the 2008 Legislature significantly increase the grocery tax credit outlined in HB81, which was $50 million, and immediately eliminate the personal property tax, in total, in one year. Regarding eliminating the personal property tax, **Mr. LaBeau** outlined how they believe this could be accomplished. First, the Idaho State Tax Commission along with interested stakeholders are currently working on developing a comprehensive set of definitions in order to develop a verifiable figure of what the true impact of eliminating this tax would be. Secondly, they believe that the Legislature should start looking at fiscal impacts in a broader sense by using a new forecasting method in developing the fiscal impacts of legislation. Thirdly, they believe the Legislature should participate in the Streamline Sales Tax Project, which is an effort created by state governments to simplify and modernize sales and use tax collection and administration.

Senator Stegner asked if he was suggesting that the Legislature reintroduce HB81. **Mr. LaBeau** said not necessarily HB81, but some variation thereof. In response to another question from **Senator Stegner**, **Mr. LaBeau** said that the $50 million figure gets us roughly to about half of what the average Idahoan spends each year on grocery taxes; essentially cutting their effective tax rate by about half on groceries. In response to another question from **Senator Stegner**, **Mr. LaBeau** said that IACI did not have an objection to the Governor's version of a weighted distribution of that tax credit. They just believe the higher number is affordable.

Senator Stegner asked what the first year revenue would be from internet and catalog sales if the Streamline Sales Tax Project was adopted. **Mr. LaBeau** stated it is estimated the state lost $125 million in FY06 and projected losses in FY08 of over $140 million. He explained that the objection to the Streamline Sales Tax is more in not knowing what specific changes need to be made to our code in order to comply with the Streamline Sales Tax. **Senator Stegner** commented that a significant portion of this money would be derived from vendors outside of the state, which requires a tremendous enforcement effort. He asked if there has been any indication that the money would be instantaneous the first year, or at least in the near future. **Mr. LaBeau** said that the information they have came from a University of Tennessee study and he will get back to the Senator with additional information on that. **Senator Stegner** asked if IACI has considered the corporate income tax issue. **Mr. LaBeau** said that IACI is more focused on growing businesses that are already here. They receive few complaints about the corporate income tax rate, but many regarding personal property tax. "It's tough to comply with, they're tired of it, they don't want to pay it anymore."

Dan John, State Tax Commission, yielded to a question from **Representative Lake** who asked what the estimated amount was that could be collected in subsequent years if the Streamlined Sales Tax Project was adopted. **Mr. John** said that the state would receive several million dollars early on. However, it would take Congress to take the final step to eliminate the barriers to the states. **Representative LeFavour** asked if **Mr. Labeau** was suggesting that the Streamline Sales Tax Project would replace the money that would be shifted to families and other taxpayers. He said that the indications by the Tennessee study are that it is principally business to business transactions. Consequently, they feel that it is appropriate to do the grocery tax credit and personal property tax and utilize existing funds, as well as the Streamline Sales Tax Project to cover the costs associated with these two items. In response to **Representative LeFavour's** question regarding the revenue stream, he said that his understanding was that most of the budget surplus has been coming from individual tax. He said that when the surplus keeps coming back, you've got to wonder where should it go? "How much money do you really need to save for a rainy day?" "Some of that money should probably come back"...to taxpayers.

Representative Clark commented that he would not base a lot of revenue sharing on the Streamline Project, since Congress basically has to act first before the project can be put in place. He also said that there are a few states who are backing out of the project. In response to a question from **Representative Clark, Mr. LaBeau** said he thinks it is a significant revenue source and it is important to keep considering the Streamline Project. **Mr. LaBeau**, at **Representative Killen's** request, said he would provide a copy of the letter regarding the Tennessee study. In response to a question from **Representative LeFavour** regarding the size of the businesses considered in the study, **Mr. LaBeau** said that the study was not based on the size of a specific business, but was based on employers as a whole. Large companies are large employers, so the impact of the personal property tax will affect them differently than the small business.

Representative Siddoway asked that, since this state is growing more towards the tourist industry and less from agriculture, mining and forestry, why has IACI had such a resistance toward taxing services? **Mr. LaBeau** said that if services were taxed and the sales tax were lowered, there is no assurance that the latter would not be increased each year. Also the administrative burden and determining value on services is a concern. **Representative Siddoway** asked whether IACI would be more willing to accept a tax on services if there was a guarantee that the sales tax would drop. **Mr. LaBeau** said that hasn't been discussed with his counterparts. However, as it stands without the guarantee, they would not agree to that.

In response to **Senator Bilyeu's** question, **Mr. LaBeau** said that their proposal is to eliminate the personal property tax in one year. Whatever amount the state realizes, would be reimbursed to local people. The state would realize 50% of their cost back. The true cost would probably go down, as more businesses take advantage of this and more revenues are received. **Senator Bilyeu** asked whether his recommendation would be that the counties be reimbursed according to whatever the personal property values were as of 2007. **Mr. LaBeau** said that would probably be the best approach, as long as an additional burden is not placed on assessors. **Representative Lake** pointed out that the personal property tax collections have been fairly constant over the last few years.

Billy Knorpp, RVP Business systems, Member of National Federation of Independent Businesses (NFIB), was the next speaker. His complete PowerPoint presentation will be available at the Legislative Services Office. **Mr. Knorpp** said that small business is what drives the economic environment in our state and the nation. He added that tax policy needs to alleviate cash problems, not exacerbate them. Compliance and administration need to be kept as simple as possible. He noted that policymakers at all levels commonly fail to appreciate the cumulative tax requirements placed on small firms.

Mr. Knorpp described some of the guiding principles of good tax policy, some of which included equity and fairness, certainty, convenience of payment, economy in collection, simplicity, neutrality, economic growth and efficiency, transparency, appropriate government revenues, consistency, competition with other states, etc. **Mr. Knorpp** stated the position that NFIB has taken with regard to tax priorities for the state. It is: do not expand sales tax base to include labor and services, do not create local option tax, and elimination/phase-out of personal property tax.

Mr. Knorpp noted that NFIB makes decisions based on balloting its members. Three times per year ballots are sent to members asking for their opinions on various topics. He noted 93% voted against sales tax on goods being extended to labor and services.

Representative Killen asked whether he would be more accepting if the recordkeeping for personal property tax was limited to only depreciable items. **Mr. Knorpp** said that would help. However, their preference is eliminating that tax completely. The administration for the business and the state is costly to maintain.

Senator Langhorst asked how we stop that tax base from eroding further if we are not going to go after any exemptions and we are not going to tax services. **Mr. Knorpp** said that generally the NFIB supports a broad tax base. The reason for the strong opposition from NFIB members is that a high percentage of small businesses engage heavily in one kind of service or another, such as the barber who does not collect a tax on services. NFIB is concerned that businesses will end up with a higher, more broader tax overall.

In response to another question from **Senator Langhorst**, referring to a local option tax question that was on one of the ballots, **Mr. Knorpp** said that he wasn't sure of the exact question on the ballot, but said, "Local option taxes, no matter how you couch them and what kind of good you're going to do with them, create stress in small businesses and economic disadvantage. In response to a question from **Representative LeFavour**, **Mr. Knorpp** said that the question regarding local option tax was asked about local option taxes in general and did not say specifically what it might fund.

Don Reading, Vice President and Consulting Economist*,* **Ben Johnson Associates**, was the next speaker. His complete PowerPoint presentation is available in the Legislative Services Office. **Mr. Reading** described three of the basic principles of taxation: fairness, efficiency and "pluck the goose," from an historical viewpoint. He noted the meaning of the phrase "pluck the goose." "The art of taxation consists in so plucking the goose as to obtain the largest possible amount of feathers with the smallest possible amount of hissing."

Mr. Reading stated that taxpayer burden is a function of both the tax base and the tax rate, which need to be separated. **Mr. Reading** noted that once the base is calculated, rates can be proportional, progressive or regressive, and that tax simplification does not necessarily equal a proportional flat tax. Regarding individual income tax, **Mr. Reading** said that Idaho's personal income tax is very progressive up to approximately $35,000. Above that it tends to flatten out.

Mr. Reading made the following suggestions. The first thing he would do would be to extend the sales tax to services, possibly excluding medical. The second would be to sunset all exemptions and do it on a rotating basis, reviewing them in a set number of years. They would disappear if they could not be proven to the Legislature they were valid. The third would be to put in place some kind of hurdles, growth, goals, etc. in order to have a very firm criteria or rating system. In response to a question from **Representative LeFavour**, **Mr. Reading** said that his rationale for excluding medical was political. He said that a fairly clear argument could be made for the disproportionate impact of medical care upon the poor and the less wealthy.

The committee recessed at 12:12 p.m. and reconvened at 1:34 p.m.

Mr. Phil Syrdal, President, **BioIdaho**, was the next speaker. **Mr. Syrdal** said that one of the main purposes of a tax incentive is that it will put something in place, and on the back end, it will give back revenues. One of his major concerns is the issue of cheap land and cheap labor and the lack of the growth of the high-paying jobs in our communities. He believes that, "If we would do one thing to help us create capital in this state and recruit capital from outside into the state, we would quit losing all of our bright young people." He said we are not using the talent we have because we don't have the capital.

Mr. Syrdal said that his main concern is how to raise capital that produces tax revenues and maintains a stable future for our state. He believes that tax incentives are the easiest tool to create capital. The tool of a tax incentive, properly done, can be a targeting device and can help recruit the money and the talent in the state to get the job done. The only way to bring an investor in to put up the high-risk money is through incentives. **Mr. Syrdal** said that he hoped the Legislature will consider strongly supporting the tax incentive approach. Initially, short-term, it is the easiest way to attract capital without having to put in the millions of dollars up front.

In response to a question from **Representative Killen**, **Mr. Syrdal** said that HB261 was the bill that was introduced that was going to provide incentives for biotechnology. **Representative LeFavour** asked in what other states were these prospective investors located. **Mr. Syrdal** said, initially, they hope to reinvigorate Idaho investors. They are also hoping to recruit money from money capitals like California, Washington, Utah, etc., even on the East Coast. "We are hoping to recruit smart money to Idaho." In response to a question from **Representative LeFavour** regarding investment in capital versus investment in payroll, **Mr. Syrdal** said that based on many years of experience in this area, a large bulk of all of these initial investments, given the way it is designed, will go to payroll, about 80 to 90% of the investment.

Representative Raybould asked if legislation could be constructed that would provide an "after the fact" credit. In other words, the investor makes the investment, the business is established, the employees are hired, a product is made, then after the project is established, the investors could apply for credit back against their initial investment. If the assurance was up front, would that be enough to entice the capital to come in? **Mr. Syrdal** said it was possible to design it, but it probably would not be effective because it wouldn't be competitive with the other states. It would also be considered a huge risk to the investor and remove the benefit of the incentive.

Senator Langhorst asked whether he had any observations with regard to the reasons why companies choose to invest in either capital or labor or education. **Mr. Syrdal** said, "What I mean by capital is that we need to energize investment capital to get into businesses that are labor intensive, to get the capital to produce high-paying jobs, to get the capital to produce new ideas and to change the culture of innovation that has languished, in our view." There has been a lack in the generation of businesses coming into Idaho.

The next speaker was **Judith Brown, Director, Idaho Center on Budget and Tax Policy, United Vision for Idaho**. Her complete PowerPoint presentation is available in the Legislative Services Office. **Ms. Brown** said that the tax restructuring since 2002 has had a minor effect on the tax burden overall. Tax re-structuring should seek to make the overall system more equitable. The position the United Vision for Idaho takes is moving toward more of a flat tax. **Ms. Brown** described refundable credits under income tax exemptions, some of which were refundable child tax credits, grocery credits and social engineering.

Representative Raybould asked who would be paying the bulk of social engineering programs that would be instituted by tax credits and refunds. **Ms. Brown** said that it basically comes back to the definition of fairness. **Representative Raybould** commented that he thinks a number of factors need to be taken into consideration; for example, the willingness to take a risk; a risk involved in some of the higher taxpayers probably needs to be rewarded as much as the lower taxpayer. **Representative LeFavour** asked how closely did she think the earned income tax credit would come to making up a disproportionate share of, for example, the sales tax. **Ms. Brown** said that in 2003 when the 1% sales tax was being considered, the cost of an earned income credit at 10% was about $15 million dollars and the cost of taking the sales tax off was about ten times that much. Forty percent of the families with the lowest incomes would have received about 2/3 of the benefit from the earned income credit that they would have received for taking the sales tax off.

Ms. Brown said that the share of Idaho property taxes has grown in residential from 49.5% in 1984 to 62.8% in 2005, whereas, property taxes for nonresidential have gone from 50.5% in 1984 to 37.2% in 2005. The shift from non-residential property onto residential property has grown from 2002 to 2005 to $89 million. **Ms. Brown** assured **Representative Lake** that those calculations took into consideration the huge expansion of residential property during that time period. **Representative Raybould** said that during the period from 1984 to 2005, the timber industry had almost disappeared, mines closed as well as other commercial businesses that were huge taxpayers. Along with that, there has been a huge increase in residential property in numbers and the valuation of homes. **Ms. Brown** said that many have come in. Commercial property only grows at about 3% a year, whereas, homeowners' values have been increasing 16% and upward per year. She said that it is reasonable to assume that the balance in the economy between nonresidential property and residential property has stayed the same, so why has the sharing of the property tax burden changed so dramatically.

Ms. Brown highlighted several factors worth consideration, among them were: expanding the homeowner's exemption further; adopting a renter's credit; and broadening the base and tax expenditures versus direct spending. **Ms. Brown** noted that the United States no longer leads the world in terms of education levels. Currently, the United States has basically not improved its education levels, whereas many other countries have. The present tuition credits are helping to make higher education more affordable for upper-income families, but not for lower-income. She said the question arises of whether to consider Idaho's college savings deduction, or needs-based financial aid and broader access to community colleges.

The committee recessed at 2:46 p.m. and reconvened at 3:07 p.m.

Keith Allred, President, The Common Interest, was the next speaker. His complete PowerPoint presentation is available in the Legislative Services Office. He began by giving a background of the founding fathers in their quest to frame the Constitution. Critical to their thinking was the need to understand human nature if you were going to base government by the people. **Mr. Allred** described what he termed, "Confirmatory Bias," which means that people tend to seek out information that confirms pre-existing preferences or beliefs and ignore contradictory information; if there are two opposing parties on a question, more information will often lead to even greater differences.

Based on these founding principles, **Mr. Allred** outlined a portrait of the sophisticated proponents and/or beneficiaries that would participate in, deliberations over a proposed tax break, and all the other taxpayers who would not. He said that from the standpoint of the legislative committee, it looks as if there are many proponents and no opponents, when in fact there are usually many opponents who would bear the burden and few proponents who would benefit. **Mr. Allred** outlined some of the economic principles applied to deliberations on tax breaks, some of which were that a market economy allocates resources more efficiently than any of the rest of us can. Typically a legislature, in general, assumes that the market will not make the right decision. He said that small businesses are the main source of economic gain; however, most do not have the time or resources to pursue tax breaks.

Mr. Allred said that the implications of this analysis are that we tend to adopt tax breaks that will not be publicly supported, and will tend to benefit those who are sophisticated, but who are not the sources of most new jobs and economic growth. “As you punch more holes in the tax code...you’ve got to have a higher rate.” He said that in effect, these tax breaks increase the rate on those who are less sophisticated, but the ones who tend to be the major source of economic gain. He said that broadening the base and lowering the rate will broaden public support and more tax relief will flow to where it will provide more jobs and economic stimulation.

Senator Stegner, referring to broadening the base and the benefit, and the perceived broad public support for that effort, asked about the people who are having to collect the rates, for example, the barber, who would now have to contend with the onerous duty to submit a sales tax report every month, which might motivate that barber to show up at a meeting. Consequently, when you couple that with every impacted service deliverer across the state, all of a sudden, the message the Legislature gets is that this is not broadly supported by the public, but in fact, there is a lot of disdain. **Mr. Allred** said that he would argue that the problem is even larger. There are all aspects of government that affect us in deep ways, depending on the policy. What tends to get our attention is when, “our own ox is being gored.” He agreed that when you round up all of the tax breaks together, then, “you have a whole lot of oxen being gored.” He believes you do start to get the broad public attention in a way that you don’t otherwise. He said that what is at stake here is to lower the rate. If you take it one by one, and not cumulatively, then all you will get are the proponents who want to defend it.

The committee was adjourned at 3:38 p.m.