

analysis

Nevada's 2003 Tax Increases

Underlying Assumptions and Resulting Impact

by Robert Schmidt and Charles F. Barr*

Executive Summary

During the 2003 legislative tax debate, we pointed out in a published study¹ that state income and expense projections issued by the Governor's Task Force on Tax Policy were based on an unrealistically "high estimate of future revenue needs and a very pessimistic estimate of future revenue growth from existing sources."

As is now widely recognized, events have proven these assertions to be true. The result is that tax collections today now run far ahead of Task Force estimates, while many programs are requiring less money than forecasts suggested.

This matters because the Task Force analysis was based upon repeated assertions that the additional tax funds were necessary to simply keep Nevada's existing programs solvent. In simple terms, Nevada fiscal policy was explained as basically allowing the State to break even. Today's growing budget surplus was never a public goal.

For responsible legislators and all parties interested in Nevada's fiscal planning, the crucial question is: Why did the preparation of the Nevada budget fail? What methodological errors resulted in the Task Force failing so dramatically? The primary purpose of this report is to show where the critical errors in method occurred.

For example, some have asserted that the

state missed its forecasts by only a "bit." Such rationalization is, unfortunately, neither useful nor correct. Moreover, the mistakes are important, since many of the advisors who helped facilitate the 2003 tax increases continue to influence government policy.

Two examples illustrate the critical and fundamental flaws in the official analyses:

- ◆ Had the legislature held FY 2004 general fund spending to FY 2003 appropriation levels, after adjustment for inflation and population increases, the FY 2004 budget would have generated a modest surplus for the year without any tax increase!
- ◆ The official budget systematically overstated revenue needs. For example, the TANF (Temporary Assistance for Needy Families) caseload is currently 42 percent below Governor Guinn's prediction.

So far, however, there has been no movement by the architects of the 2003 tax increases to repeal any of these levies. Left to their own devices, many policymakers are likely to discover additional "needs" that will eat up the entire surplus, soon requiring even higher taxes. To prevent more raids on the pockets of Nevada's taxpayers, new, structural safeguards may well be necessary. A Colorado-style Taxpayer Bill of Rights is one promising approach.

¹ Schmidt, Robert and Charles Barr, *Nevada's Proposed 2003-2005 Budget: Review & Analysis*. Citizens for Prosperity and Responsibility, 2003. On the web at: www.cprnevada.com.

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INTRODUCTION

In the words of the Legislative Counsel Bureau, “The Governor’s Task Force on Tax Policy in Nevada was created by Assembly Concurrent Resolution 1 (ACR 1) of the 17th Special Session (2001).”¹

The panel was charged with examining an alleged “structural deficit” that was causing a disparity between the growth in general fund revenues from the state’s current revenue sources and the growth in public spending supposedly needed to maintain current governmental services to the people of the State of Nevada.² ACR 1 required the Task Force to suggest changes to the current tax structure that would broaden the state’s tax base and reduce reliance on what tax increase proponents characterized as the state’s supposedly volatile or cyclical revenue sources.³ The resolution required that a final report including the recommendations of the Task Force be provided to the Governor and the Legislature by November 15, 2002.⁴

In 2003, we examined future revenue requirements facing the State of Nevada in light of the proposed tax increases on Nevada’s citizens.⁵ As is well known, the main arguments in support of the “absolute necessity” for the tax hike in 2003 as presented during the legislative session relied specifically on the findings of the Governor’s Task Force on Tax Policy in Nevada.⁶ As we pointed out at that time, “many of the assumptions underlying the budget are inconsistent with both empirical and theoretical evidence.” We also noted that the Task Force projections were based on a rather surprisingly “high estimate of future revenue needs and a very pessimistic esti-

mate of future revenue growth from existing sources.”⁷ The net effect of these projections was a built-in *necessity* for a tax increase—*simply by definition*.

As we pointed out during the 2003 Nevada Legislative session, the Task Force’s calculations were based upon poor methodology. Additionally, domination of the Task Force by beneficiaries of tax restructuring and higher taxes was bound to suggest a “Jack Horner” approach.⁸ Notwithstanding the flaws in the Task Force report, however, its authors ultimately saw most of the tax increases they advocated passed into law. The one exception was the Gross Receipts Tax.

Now, less than 18 months later, Nevada taxpayers are being compelled, by law, to underwrite a tremendous buildup of state revenues, as tax collections are running far ahead of the Task Force projections. At the same time, many of the supposedly critically escalating “public needs,” such as the welfare caseload, are posting mild increases and in some cases significant *declines*—not the rapid increases projected by the Governor and Task Force.

It is now apparent that Nevada’s citizens, and to some extent Nevada legislators, were misled by faulty and unreliable methodology into supporting a set of unnecessary tax increases. This is the unfortunate legacy of the prior budget process. How did this happen? How can these significant errors be avoided in the future?

In this report, we will revisit the basic assumptions and methodology that led to glaring errors. We will suggest how future projections can be based more

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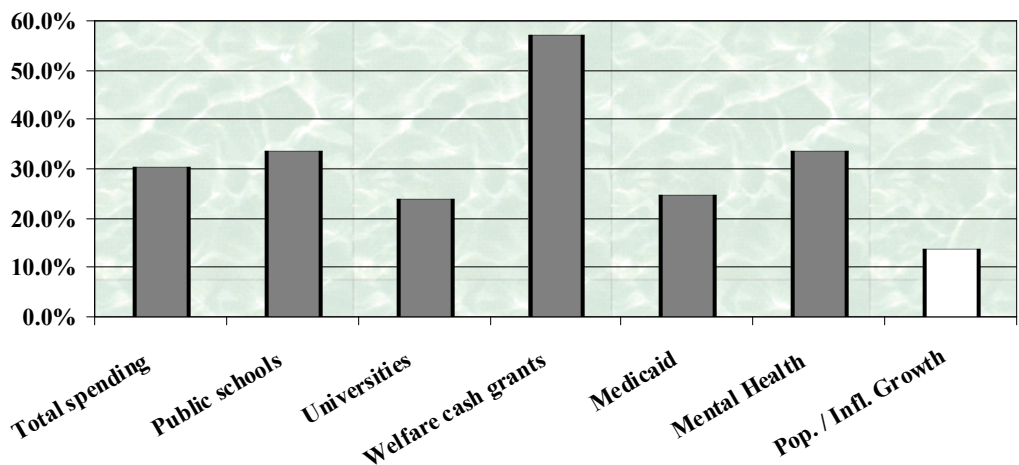
soundly upon historical evidence and economic common sense.

This is an important issue, because when faulty methodologies are used to justify highly controversial tax increases like those of the 2003 legislative session, in many quarters the integrity of state government itself will tend, as we have seen, to be brought into question. The use of “worst case scenarios” to predict

future revenue needs and tax collections gives taxpayers a distorted picture of Nevada government’s economic health. In the short run, this may work to the advantage of those who stand to benefit from higher levels of state spending. In the long run, however, such an approach will undermine confidence in the state government’s ability to accurately assess and report its future needs.

BUDGETED SPENDING INCREASES

**Figure 1. Increase in 2003-05 General Fund Budget,
Compared to 2001-03 Budget**



Sources: See endnote 9

The 2003-05 spending hike followed on the heels of another spending increase, approved by legislators in the previous biennium.

Figure 1 shows the percentage increases in the overall 2003-05 general fund budget, as well as education and human resources categories within that budget, compared to the budget for the previous biennium. The overall spending increase was more

than more than *twice* the estimated percentage increase in population and inflation combined for the two-year period.⁹ Furthermore, this followed on the heels of another significant spending hike approved by legislators for the previous biennium.

Establishing a Reasonable Baseline

As noted in our 2003 report, the Task Force inflated future revenue needs by insisting that the cyclically high 2001-03 budget, adopted just before the September 11 terrorist attacks, be used as a baseline. At the time the 2001-03 budget was adopted, the Legislature presumed that the robust economic growth of the late 1990s would continue indefinitely, and that this sizeable spending increase would require no tax increases to fund it. As the Governor's Task Force itself pointed out, "It is noteworthy that between FY 2000-01 and FY 2002-03, the State's general fund budget increased by nearly 25 percent, or from \$1.6 billion to \$2.0 billion. This increase exceeded population and inflation growth by nearly 10 percent and represents the largest two-year increase in State appropriations reported during the study period."¹⁰

The September 11, 2001 terrorist attacks occurred a few months after this budget was adopted, dealing a severe shock to Nevada's economy and reducing state and local tax revenues. But it was unacceptable to assume that this "worst case" scenario would henceforth be the norm for the Nevada economy. In no other state of which we are aware was any reliable methodology employed to make the assumption that a terrorist-impaired economy would be the new permanent condition.

In fact, notwithstanding the Task Force projections of a severe deficit, the Guinn administration still continued to spend general fund revenues at a rate 3.1 percent above 1999-2001 levels—even after adjusting for inflation and population growth.¹¹ These additional expenditures amounted to a total of \$114 million.¹² In the course of this spending, the State essentially depleted its General Fund reserves—the so-called "rainy day

fund."

Governor Guinn then cited the shortfall in the reserve fund—along with dire predictions of another terrorist attack—to justify his proposal for a "temporary" tax increase of \$74 million for the final quarter of the 2001-2003 biennium.¹³ He then proposed a general fund budget increase for the 2003-2005 biennium of more than 28 percent.

One item within the Governor's proposed budget is especially noteworthy, because it reveals the anomalous priorities behind formulation of state tax policy. After proposing the largest tax increase by far in Nevada history (allegedly needed to maintain the state's existing services), Governor Guinn proposed even higher taxes in order to fund several new projects.

Here's the rationale, as offered in the 2003-05 Executive Budget in Brief:

Nearly all of the General Fund appropriations represent spending necessary to continue State programs under existing conditions (the "base" budget) and for "maintenance" purposes—to maintain existing programs after taking into account a variety of factors, such as caseload growth, new mandates, etc. The remainder, *just 3.1 percent, is budgeted for program "enhancements"*. (Emphasis in the original.)¹⁴

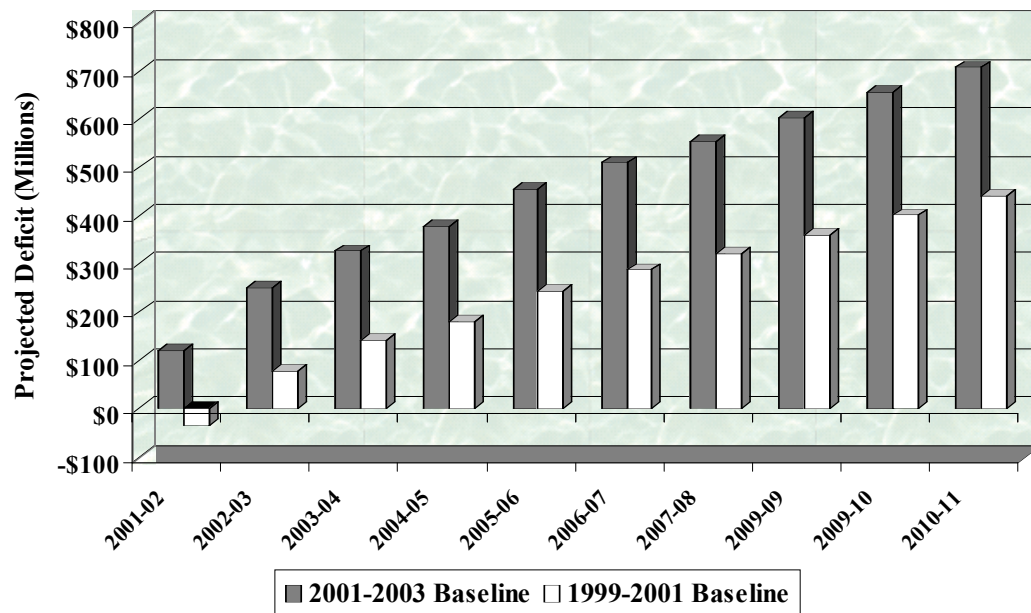
Unfortunately, this account essentially evades the real magnitude, for Nevada families, of that "remainder." The "just 3.1 percent," after all, was on proposed spending for the 2003-2005 biennium of \$4.81 billion. It therefore amounted to \$149.1 million, or \$251 for every Nevada family of four. And this was just a portion of the massive overall tax increase.

The Governor's Task Force did not

Despite Task Force projections of a severe deficit, the Guinn administration continued to spend general fund revenues at a rate 3.1 percent above 1999-2001 levels – even after adjusting for inflation and population growth.

Setting a more realistic baseline would have slashed the projected deficit for the 10-year period 2001-2011 from \$4.57 billion to \$2.43 billion – a reduction of nearly half.

Figure 2. Effect of Different Baselines on Projected Annual General Fund Deficits, 2001-2011



Source: Governor's Task Force on Tax Policy, Revenue and Expenditure Projections

suggest that any of the huge spending increases of the previous biennium be rolled back. Instead, it continued insisting that the high 2001-03 budget should be used as a baseline for determining the appropriate level of state services. Given the context, this stance was, at best, disingenuous.

In the CPR study, we suggested that a more appropriate baseline would be the spending levels approved for the 1999-2001 budget, adjusted for population

growth and inflation, and suggested that the “add-ons” placed in the 2001-03 budget be removed.¹⁵ As demonstrated by Figure 2, setting a more realistic baseline would have reduced the 2001-03 deficit by nearly 88 percent, from \$372 million¹⁶ to a mere \$46 million. This more realistic baseline would also have slashed the projected deficit for the 10-year period 2001-2011 from \$4.57 billion to \$2.43 billion—a reduction of nearly half.

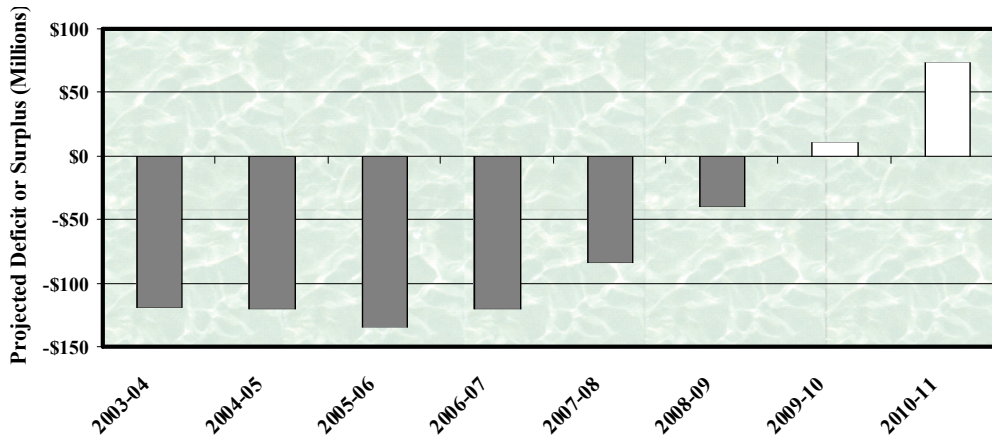
Projecting Future Revenue Growth

In addition to explicitly endorsing the 2001-03 spending increases, the Governor’s Task Force further inflated the projected deficit by assuming an annual growth rate in General Fund revenues of only 3.9 percent per year.¹⁷ This was another dubious assumption.

As the CPR study pointed out in

advance, this was an extremely pessimistic forecast, given that the compound annual increase in General Fund revenue between 1989 and 2001 was 7.3 percent, and for State revenue as a whole it was 8.4 percent.¹⁸ Moreover, this was a 12-year period that included two recessions as well as the first Gulf War.

Figure 3. Annual General Fund Deficits, 2003 to 2011, Using 1999-2001 Baseline and 6.5% Revenue Growth Rate



Source: Calculations Based on Governor's Task Force on Tax Policy, Revenue and Expenditure Projections (Note: These calculations presume the Task Force projections of much higher revenue requirements for education and welfare.)

Our analysis suggested that a more reasonable (and still conservative) projected annual revenue growth rate would be 6.5 percent.¹⁹ Utilizing this scenario and a 1999-2001 baseline, the deficit for the eight-year 2003-2011 period would have declined to an average of \$67 million per year—*less than 13 percent of the Task Force estimate.*

What's more, the presumed annual deficit would have begun falling steeply in 2006, disappearing and becoming a surplus by 2009. (See Figure 3.) We therefore concluded that any remaining deficit could be dealt with by a more modest tax increase, one less than one-fourth the size of that proposed by the Governor.

The new, higher tax rates are fueling a massive transfer of money from Nevada's residents and businesses to state and local government.

NEVADA'S ACTUAL NUMBERS

In the two years since the Governor's Task Force released its projections, many components of Nevada's general fund revenues (such as sales taxes, which were not increased in the 2003 legislative session) have shot up at rates of return even higher than our own conservative estimates, and considerably higher than inflation and population growth combined.

As the 2003 tax increases have been

phased in, Nevada's economic recovery and the new, higher tax rates are combining to fuel a massive transfer of money from Nevada's residents and businesses to state and local government.

Although Nevada's economic growth rate will be slowed by the recent tax increases, it can still be expected under any reasonable scenario to outperform the low near-term predictions of the Governor's Task Force.

Much of the tax increase, it was said, was needed to fund entirely new programs sought by the Governor — notwithstanding his claims of a fiscal emergency.

Revenue Needs for Education

A centerpiece of Governor Guinn's spending program was the education budget. General Fund spending on education during the 2001-03 biennium totaled \$1,989.9 million.²⁰ For the 2003-05 biennium budget, "the Governor has recommended General Fund appropriations for education of \$1.29 billion for FY 2003-04, a 30.4 percent increase over FY 2002-03, and \$1.35 billion for FY 2004-05, an additional 4.3 percent increase."²¹ Included in this package was a 24.2 percent increase for the biennium in General Fund appropriations for the University and Community College System (UCCSN),²² a 29.5 percent increase in the Distributive School Account (DSA) for K-12 students,²³ with the remainder earmarked for other programs.

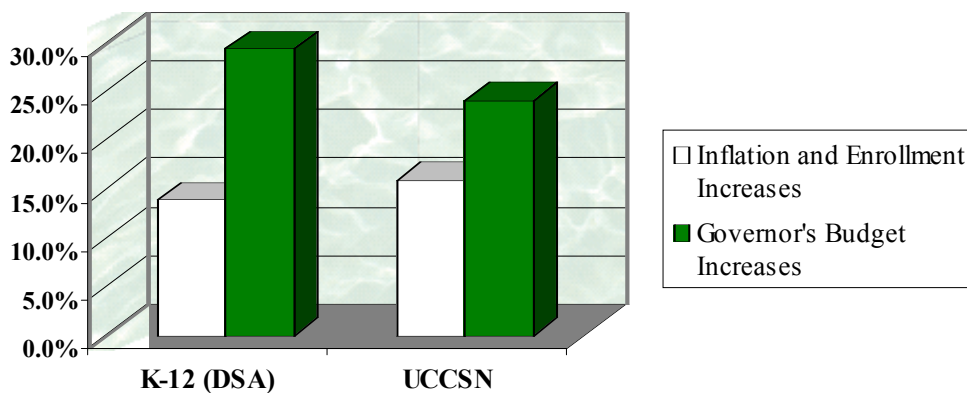
The Governor's education budget came in at nearly 6 percent higher than the amount recommended by his Task Force.²⁴ Much of this increase, it was said, was needed to fund entirely new programs sought by the Governor —

notwithstanding his claims of a fiscal emergency. Examples included \$24.2 million to establish more than 400 full-day kindergarten classes at an unspecified number of schools, and \$60 million for a new Technology Center at UNLV.

How did these major spending increases compare with increases in enrollment and inflation? For the 2003-04 and 2004-05 school years combined, K-12 enrollment increased by only 8.6 percent, while UCCSN enrollment increased by 10.6 percent. The Consumer Price Index increased 4.9 percent during the two-year period from September 2002 to September 2004.

Thus, maintaining the General Fund contribution to education at existing levels would have required an increase of 13.9 percent in K-12 spending and 16.0 percent in UCCSN spending. Instead, the education spending increase proposed by Governor Guinn was more than double what would have been necessary to allow for inflation and enrollment increases.

Figure 4. Increases in Nevada's Education Spending for 2003-05 Biennium



Source: U.S. Bureau of Labor Statistics, Also see endnotes 20, 23.

Medicare and Other Welfare Programs

For the 2003-05 biennium, Governor Guinn requested a general fund budget of \$1,364.1 million for Human Services, which administers Nevada’s welfare programs.²⁵ This represented a 30.4 percent increase from the budget approved for the 2001-03 biennium, and far greater than the combined increase in population and inflation. To justify this massive increase in welfare spending, Guinn argued that,

By FY 2005, Medicaid caseloads are expected to total over 200,000, more than double their level from as recently as FY 1999. Increases of 18,000-20,000 per year are expected in the 2003-2005 biennium. TANF (Temporary Assistance for Needy

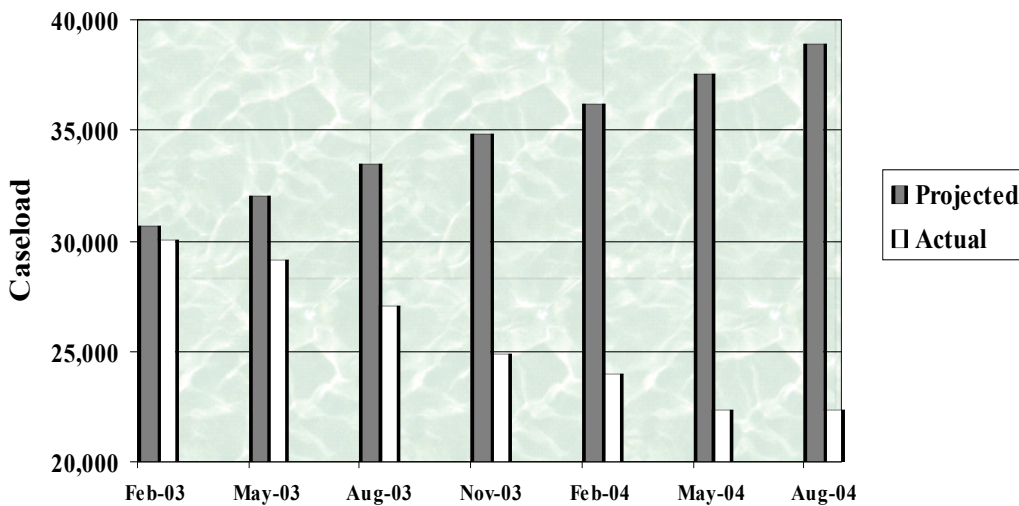
Families) recipients are also forecast to continue rising at a pronounced clip. Annual caseload gains of 5,000-6,000 are expected.²⁶

Like most independent researchers, our team came to opposite conclusions. We pointed out that “caseloads (the number of people assisted) are declining to more normal levels as the Nevada economy continues to recover.”²⁷ We further stated: “Given this circumstance, one would expect inflation-adjusted welfare spending to decline along with the caseloads.”²⁸

Figure 5 compares what the Governor told Nevadans they faced with what actually occurred.

For the current biennium, the Governor requested a 30.4 percent increase even over the budget approved for the previous biennium.

Figure 5.
Caseload for Temporary Assistance to Needy Families:
Governor Guinn's Projections vs. Reality



Source: Nevada Department of Human Resources, Welfare Division

Once again, an unbiased conservative analysis, based on widely employed and traditional economic forecasting principles proved much closer to the actual results. The TANF (Temporary

Assistance for Needy Families) caseload was 30,231 when the Executive Budget for 2003-05 was released in January, 2003. If Governor Guinn’s forecasts had been accurate, the TANF rolls would

Had the budget been held to previous levels (adjusted for population and inflation), the entire tax increase would have been unnecessary, and a surplus of \$22 million would have resulted.

have shown an increase of 8,700 cases by August 2004. Instead, the caseload *declined* by 7,868, which is 26 percent less than the January 2003 number and *42 percent less than Governor Guinn's*

*dire prediction.*²⁹ (See Figure 5.) Meanwhile, the Medicaid caseload as of August 2004, at 176,506, is 11.7 percent *under* the Guinn administration's estimate of 200,000.³⁰

Predicted vs. Actual Tax Receipts

What the above facts clearly demonstrate, once again, is that actual revenues needed to fund state education and welfare programs were far less than the amount predicted by the Governor and his Task Force. However, thanks to the tax increases that were passed into law on the basis of the faulty economic growth predictions made by the Governor's Task Force, the state is today collecting money at a rate even higher than is needed to fund the 2003-05 budget, *including all the spending increases.*

According to official estimates, the tax increases approved by the Legislature were expected to raise an additional \$835.8 million over the two-year period: \$363.9 million in FY 2004 and \$471.9 million in FY 2005.³¹ We said at the time that these estimates were low, based on the pessimistic projections of revenue growth issued by the Governor's Task Force on Tax Policy.

So what actually *did* occur after the tax hikes went into effect? For FY 2004, general fund revenues totaled \$2.404 billion, which was \$145.3 million (6.4 percent) higher than official predictions.³² Since the tax hikes were designed to fund an increase of \$363.9 million, and instead led to an increase of \$509.2 million, it is clear that the actual tax increase was *40 percent greater* than would have been necessary to fund even the overstated "official" revenue needs claimed by the Governor and the Legislature.

What if Governor Guinn and Nevada's legislators had exhibited fiscal discipline, and kept spending in line with FY 2002-03 appropriations, adjusted for inflation and population increases? General fund appropriations for FY 2003 totaled \$1.892 billion.³³ The inflation increase from June 2003 to June 2004 was 3.27 percent,³⁴ while the State Demographer projected a 2004 population increase of 3.3 percent.³⁵ This translates to a combined (multiplicative) increase of 6.68 percent, which in turn would have produced a more fiscally responsible FY 2004 budget of \$2.018 billion.

The general fund actually took in \$386 million over this amount. This means that *if the budget had been held to previous levels (adjusted for population and inflation), the entire tax increase would have been unnecessary, and a surplus of \$22 million would have resulted.*

Significantly, FY 2004 was only the first year of Nevada's new high-tax regime. As the state's economic growth continues to outpace the overly dismal projections of the Governor's Task Force, it is likely that the size of the annual surplus will grow at a progressively faster rate each year, at the expense of Nevada's taxpayers and the state's economy as a whole. Indeed, the actual surpluses each year will most likely be even larger than that, given the lower-than-predicted growth in welfare caseload.

PROPERTY TAX RATES

Property tax rates were not included in our original CPR study for two reasons. First, the Governor's Task Force had not recommended an immediate increase in property tax rates. Second, in the State of Nevada these rates are largely a major government revenue source for counties and cities. However, it is important to note that approximately two-thirds of the total tax rate in Clark County is under the direct or indirect control of the State.

For example, the total tax rate in FY 2002 in Clark County was \$2.8303 per \$100 of assessed valuation. Only \$0.9062 per \$100 of the assessed valuation of this amount—about 32 percent—is levied at the discretion of the Clark County Board of Commissioners. Approximately 34 percent is used to fund state programs, primarily education. The remaining amount is dedicated to specific programs or projects approved by the voters, and cannot be reallocated for other purposes. For example, over 50 percent of this segment is committed to financing school construction.

Clark and Washoe counties contain most of the State's property tax base. During the seven-year run-up to 2003, rising property values in Washoe County allowed that jurisdiction to not raise its general property tax rate; the county's assessed value jumped from \$5.7 billion in 1995 to \$9.3 billion in 2003. During the same period, Clark County's assessed valuation rose from \$17.8 billion to \$37.6 billion.

The Clark County Assessor's office now estimates that that the county's property rates may increase by another 30-50 percent by 2006. However, some

researchers have suggested that the recent increases may be aberrations that will be self-correcting in the near term as speculation subsides in the Southern Nevada real estate market. Others have suggested that the market is simply making up for years of lagging performance vis-a-vis California's residential property market.

According to Rocky Steele, director of assessment services for Clark County, the taxable value on land increased between 20 percent and 50 percent during the year ending June 30, 2004.³⁶ Land values, which skyrocketed during a 10-month period beginning a year ago, are based on home sales.

Clark County Assessor Mark Schofield has suggested that taxpayers should expect a 10 to 30 percent increase in residential property taxes in July 2005 and a 30 to 50 percent jump in July 2006.³⁷ The increases would reflect the dramatic surge in Clark County land and housing prices over the past nine months. The assessor's office typically uses numbers that are 12 to 18 months behind market prices to determine a home's taxable value. The 8 percent increase in this year's property tax notices mirrors the trend of the past five years.

There has been substantial support for imposition of a cap on property taxes. Governor Guinn, for example, has demanded that this issue be explored by the 2005 Nevada Legislature. We strongly suggest that the governor and legislators encourage more scholarly input when evaluating proposed property tax limitations as well as proposed tax increases.

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The State Taxation Department's last quarter filings in Real Property Transfer Tax – \$37 million – exceeded the original State Legislative projections by over 70 percent.

Real Property Transfer Tax

Real Property Transfer Tax (RPTT) is a tax collected when an interest in real property is conveyed. It is collected by the County Recorder at the time of recording. The basis for the tax is the actual selling price or the estimated market value of the property.

The previous transfer tax rate was 65 cents per \$500 of value, plus an additional 60 cents per \$500 of value in Clark County (proceeds of which go to the Clark County School District for capital projects). The current rate varies by county in Nevada. All proceeds from the tax increase go to the State. The increase adds about \$520 to the transfer of a \$200,000 residence.

As part of the 2003 tax package, the RPTT was increased effective October 1, 2003. The revenue from this tax was estimated to \$51.4 million in FY2003-2004 and \$69.9 million in FY2004-2005.

However, the continued rise in sales values, investor speculation and the increase in the number of transactions that has fueled property tax increases has also fueled the increase in RPTT. In fact, the State Taxation Department's last quarter filings in Real Property Transfer Tax—\$37 million—exceeded the original State Legislative projections by over 70 percent.

Unlike the assumptions surrounding many of the other tax increases, the residential real estate increases fueling the significant increase in RPTT revenues would have been more difficult to anticipate. Nevertheless, experienced economists would have provided caveats and explanatory commentary regarding the potential impacts of numerous external factors—such as historically low interest rates on the purchase and sale of real property.

ECONOMIC FORECASTING

Everyone who publishes an economic forecast knows that economic forecasting is a humbling task. Many scholars much more experienced than the Task Force and its staff have been proven wrong by the arrival of unforeseen or cataclysmic events. However, most independent scholars typically avoid the type of glaring errors made by the Task Force. These include:

- ◆ Predetermining “structural” needs;
- ◆ Failure to adjust for price elasticities for such items as alcohol and cigarettes;

- ◆ Failure to test and/or document the appropriate assumptions;
- ◆ Foregoing historical trends without cause;
- ◆ Assuming new taxes to be the “obvious” solution, rather than objectively evaluating the revenue requirements necessary for adequate delivery of services.

For example, many economic forecasters may have failed to predict the RPTT revenue windfall that has befallen the state in the last year due to the sudden increase in residential homes sales

and prices. However, understanding the near-term implications of the residual effects of the September 11 disaster is another story.

A whole range of possible events with varying probabilities and effects can be taken into account by tax policymakers. But the influence of possible low-probability events is most evident when serious instability is a much greater threat than usual. It is in these circumstances that the range of possible outcomes is most uncertain, especially when the impact of a given outcome itself may also be especially large. Guarding against such a low-probability, high-impact event can in turn significantly skew tax policy away from that most likely to achieve a community's longer-run objectives for economic development or social policy.

Policymakers giving significant weight to low-probability events face several challenges. One serious potential pitfall is paying so much attention to worst-possible-case scenarios that sight is lost of the main objectives of a living and economically vital community. In effect, policymakers would be overcompensating for earlier events at exactly the wrong time.

A key issue in this regard is judging

when to begin reversing measures that were justified on the basis of the possible recurrence of the high-impact event. The policy actions we have been addressing were sold to lawmakers, in part, on the basis of the effects of major, economy-altering events. It may be difficult to judge when the threat of those events has diminished sufficiently to make unwinding the action—reducing or dropping the policy—advisable. The difficulty is compounded because reasons for the behavior that leads to heightened potential impact of a low-probability event often are not fully understood.

As the threat of the low-probability event—such as the September 11 terrorist attack—recedes into the past, policy may need to compensate over time in the other direction to preserve economic and price stability, and correct the economic imbalances that resulted from implementation of “crisis management” policies.

Nevadans, including their legislative representatives, can reasonably question why such poor methodology was used by both the Guinn Administration and the Task Force. Since the strong assertions of the necessity of major tax increases were based upon this very seriously flawed methodology, it is important that such questions be raised.

One serious potential pitfall is paying so much attention to worst-possible-case scenarios that sight is lost of the main objectives of a living and economically vital community.

CONCLUSION

Where does Nevada go from here? After spending increases outpaced growth in population and inflation during the last two biennial legislative sessions, it is now clear that the faulty methodologies of the Task Force were deployed in support of a campaign to increase, and shift, Nevada's tax burdens. This should never

be allowed to occur again.

Unfortunately, many of the players who actively rationalized the 2003 tax campaign continue at center stage in discussions of Nevada's future revenue needs. If their methodologies and assumptions are not challenged, the next “Task Force” will doubtlessly discover new “revenue needs” that will quickly

Nevada voters desperately need an accounting system geared toward providing a clear and comprehensive picture of the entire state budget.

translate into new taxes on Nevadans.

Our legislators should bear in mind that such faulty methodologies, ignoring history and generally accepted economic theory, necessarily will taint state government itself.

Nevada must also put its fiscal house in order by incorporating “best practices” from around the country, including accounting reforms, priority-based budgeting and a Colorado-style Taxpayers Bill of Rights (TABOR) amendment.

Nevada voters desperately need an accounting system geared toward providing a clear and comprehensive picture of the entire state budget (including its legal subsidiaries, the counties). Such a system must be transparent to, and understandable by, ordinary citizens.

This accounting system should also include a means of evaluating the efficiency and equity consequences of all budgetary decisions. Priority-based

budgeting, used in several states, is such a system. This reform begins with clear identification of core governing functions, agency missions, goals and objectives. Performance measures and performance evaluation then follow naturally—as does a thoroughly intelligent and disciplined budget-writing process. Legislative intent is firmly protected in execution.

Finally, Nevadans should consider embracing structural changes to the state’s fiscal processes—such as a Taxpayer’s Bill of Rights similar to the one that Colorado voters added to that state’s constitution in 1992. Increases in taxes and fees in Colorado, whether state or local, are now capped to not exceed the increase in state population and inflation. Unless taxpayers at a regularly scheduled November election approve of an exception, excess revenues are routinely returned to taxpayers.

**APPENDIX
2003 NEVADA LEGISLATIVE
TAX PACKAGE**

2003 Revenue Plan			Fiscal Year Estimated Revenue (in millions)	
Revenue Source	Tax Rate/Fee	Additional Information	2003- 2004	2004- 2005
Modified Business Tax – General (Senate Bill 8)	Imposes 0.7 percent tax on gross wages paid, lowering to 0.65 percent on July 1, 2004, with deduction for the amount paid by the employer for health insurance or health benefit plans.	New gross wage tax is payable quarterly. Repeals and replaces quarterly business tax of \$25 per employee (\$100 per year). Effective October 1, 2003.	\$139.7	\$181.8
			(\$60.9)	(\$83.8)
Modified Business Tax – Financial Institutions (Senate Bill 8)	Imposes 2 percent tax on gross wages paid by financial institutions with deduction for the amount paid by the employer for health insurance or health benefit plans, plus a \$7,000 annual excise tax for each branch office.	New gross wage tax is payable quarterly. Bank franchise fee of \$1,750 payable quarterly for each branch office in Nevada in excess of one. Wage tax effective October 1, 2003; excise tax effective January 1, 2004.	\$1.3	\$2.6
			\$15.5	\$21.4

Business License Fee (Senate Bill 8)	Creates \$100 annual license fee for businesses.	Annual license fee of \$100 replaces one-time licensing fee of \$25. Effective July 22, 2003.	\$22.1	\$24.5
Gross Gaming Revenue Tax and Restricted Slot Tax (Senate Bill 8)	Increases gross gaming revenue tax rate by 0.5 percent for non-restricted licensees.	3 percent tax on monthly gross gaming revenue up to \$50,000 increased to 3.5 percent. 4 percent tax on monthly gross gaming revenue over \$50,000 and up to \$134,000 increased to 4.5 percent. 6.25 percent tax on monthly gross gaming revenue over \$134,000 increased to 6.75 percent. Effective August 1, 2003.	\$41.0	\$51.1
	Increases fee for operation of slot machines in restricted locations by 33 percent.	Quarterly fees increased from \$61 to \$81 for first five slot machines. For each additional machine over 5, quarterly fees increased from \$305 plus \$106 to \$405 plus \$141. Effective July 22, 2003.	\$2.3	\$2.4
Cigarette Tax (Senate Bill 8)	Increases tax by 45 cents per pack.	Tax of 35 cents/pack (10 cents to counties and 25 cents to State) increased to 80 cents/pack (10 cents to counties and 70 cents to State). Effective July 22, 2003.	\$63.3	\$70.0
Liquor Taxes (Senate Bill 8)	Increases taxes on intoxicating liquors by 75 percent.	Over 22 percent alcohol—increased from \$2.05 to \$3.60 per gallon. 14 to 22 percent alcohol—increased from 75 cents to \$1.30 per gallon. Under 14 percent alcohol—increased from 40 cents to 70 cents per gallon. Beer (malt beverages)—increased from 9 cents to 16 cents per gallon. Effective August 1, 2003.	\$13.9	\$15.5
Live Entertainment Tax (Senate Bill 8)	If maximum seating is less than 7,500—imposes 10 percent tax on admission charge, plus 10 percent tax on food, refreshments, and merchandise. If maximum seating 7,500 or more—imposes 5 percent tax on admission charge only.	Exemptions from tax include: (1) non-gaming establishments with maximum seating less than 300; (2) gaming establishments with maximum seating less than 300 and with less than 51 slots or 6 games or any combination within those limits; (3) nonprofit organizations; (4) boxing matches; (5) private events; and (6) certain accessory entertainment in venues such as trade shows or shopping malls. Changes to existing casino entertainment tax (CET) are effective September 1, 2003, with repeal of CET on January 1, 2004. Live entertainment tax effective January 1, 2004.	\$41.5	\$75.4
Real Property Transfer Tax (Senate Bill 8)	Imposes state tax of \$1.30 per \$500 of value on transfer of real property.	Existing transfer tax is 65 cents per \$500 of value, plus an additional 60 cents per \$500 of value in Clark County (proceeds to school district for capital projects). All proceeds from tax increase go to the State. Increase will add \$520 to transfer tax on \$200,000 residence. Effective October 1, 2003.	\$51.4	\$69.9
Fees to Secretary of State (Senate Bill 2 and Assembly Bill 4)	Increases or creates various fees payable to the Secretary of State.	Bills amend and create fees payable to Secretary of State by businesses and other entities and persons in Chapters 78-90, 92A, 104, 105, 116, and 225 of the <i>Nevada Revised Statutes</i> . Legislative intent stated in S.B. 8 is that fees will not be increased again for a period of ten years. Effective on November 1, 2003, with minor exceptions.	\$18.9	\$25.2

Tax Collection Discounts (Assembly Bill 4)	Reduces collection discounts granted to retailers and wholesalers to offset the costs of collection of certain taxes, and increases fees for certain tax permits.	Reduces collection discounts from: 3 percent down to 0.5 percent for importers, liquor manufacturers, cigarette dealers; and 2 percent down to 0.5 percent for wholesale tobacco products dealers.	\$14.8	\$15.9
		Effective August 1, 2003.		
		Reduces collection discounts from: 1.25 percent down to 0.5 percent for timely payment of sales and use taxes. (Additional revenues are allocated to the State General Fund and the Distributive School Account.)		
		Effective July 1, 2003.		
		Increases sales tax permit fees from \$1 to \$5.		
		Effective July 22, 2003.		

END NOTES

1. <http://www.leg.state.nv.us/71st/Interim/Studies/TaxPolicy/FinalReport/TaxTaskForcehomepage.cfm>
2. In reality, no structural deficit appears to have existed. If the idea was that increasing State expenditures required more taxes, this is not consistent with any legitimate theoretical construct of a structural deficit in the public finance literature. More expenditures requiring more taxes is not structural. See the article Nevada Faces Choices-Not a 'Structural Deficit' at www.npri.org/issues/issues02/language_abuse.htm
3. See http://www.npri.org/issues/issues02/tax_base.htm
4. <http://www.leg.state.nv.us/71st/Interim/Studies/TaxPolicy/FinalReport/TaxTaskForcehomepage.cfm>
5. Schmidt, Robert and Charles Barr, "Nevada's Proposed 2003-2005 Budget: Review & Analysis." Citizens for Prosperity and Responsibility, 2003. On the web at: www.cprnevada.com.
6. "After 12 months of hard work and deliberations, the Task Force delivered a set of recommendations that all Nevadans can have confidence in. Those recommendations serve as the foundation of the plan I will unveil to you this evening." -Governor Kenny Guinn, STATE OF THE STATE ADDRESS, January 20, 2003.
7. Schmidt and Barr, p. 2.
8. Among scholars aware of the long history of government favor granting, references to "Little Jack Horner" hark back to the reputed origins of the famed nursery rhyme. Historically, the real Jack Horner was steward to the Bishop of Glastonbury, from whom King Henry VIII wanted the deeds to 12 English manorial estates that the Glastonbury abbey owned. According to at least one account, Horner pinched the deeds and gave them to Henry, who rewarded Horner with one of them—the manor of Mellis in Somerset, the best (or "plum") of the 12 estates. Thus, in the rhyme, Horner "stuck in his thumb and pulled out a plum and said what a good boy am I."

9. http://www.reviewjournal.com/lvrj_home/2003/Jul-23-Wed-2003/photos/comparison.jpg; Consumer Price Index, All Urban Consumers, at <http://www.bls.gov>; State of Nevada Demographer, <http://www.nsbdc.org/demographer/pubs/>
10. Governor's Task Force on Tax Policy, Section 4: General Fund Outlook, page 4-15.
11. Nevada's general fund appropriations totaled \$3.7524 billion in the 2001-2003 biennium (see 2003-2005 Executive Budget in Brief, page 27), compared to \$3.2019 billion in the 1999-2001 biennium (see 2001-2003 Executive Budget in Brief at <http://budget.state.nv.us/budin-brief01.htm>). Nevada's population on July 1, 2002 (the midpoint of the 2001-2003 budget cycle) was 2,206,022, compared to the state's population of 2,023,378 on July 1, 2000 (the midpoint of the 1999-2001 budget cycle). See <http://www.nsbdc.org/demographer/pubs/images/popul03.pdf>. The Consumer Price Index - All Urban Consumers was 180.1 in July 2002, compared to a reading of 172.8 in July 2000. See www.bls.gov. Calculations using these figures reveal a general fund spending increase of 3.1 percent for the 2001-2003 biennium, after adjusting for population and inflation increases.
12. If general fund spending in the 2001-2003 biennium had been held to 1999-2001 levels, adjusted for population and inflation, the total would have been \$3.6384 billion. Instead, it was \$3.7524 billion. The difference is \$114 million.
13. From the *Las Vegas Review-Journal*, March 6, 2003: "Guinn said he would be forced to make massive cuts in the state and public school budgets if legislators reject the tax increases and the country goes to war with Iraq. 'Our revenues will take a dive, not a slide,' Guinn said about the effects of a pending war. 'You saw what happened with 9-11. Do you think we would have a war with Iraq without an incident?' If tax revenues plummet because tourists stay home during a war, Guinn said he not only would lay off thousands of state employees but would have no choice but to reduce allocations to public schools. That could mean teacher layoffs, he said."
14. *Executive Budget in Brief*, p. 27.
15. Schmidt and Barr, p. 5.
16. Governor's Task Force on Tax Policy in Nevada, Section 4: General Fund Outlook, p. 4-5.
17. Governor's Task Force on Tax Policy, General Fund Outlook: Exhibit 4A-1.
18. Governor's Task Force on Tax Policy, Fiscal System Overview: Exhibit 2A-1.
19. Schmidt and Barr, pp. 6-7.
20. *Executive Budget in Brief*, p. 65.
21. *Executive Budget in Brief*, p. 69.
22. Fiscal Report prepared by the Nevada Legislative Counsel Bureau, p. 72.
23. *Executive Budget in Brief*, p. 65.
24. Governor's Task Force on Tax Policy, *Analysis of Fiscal Policy in Nevada*. Exhibit 4B-1: State of Nevada General Fund Expenditure Projections.
25. Nevada Legislative Counsel Bureau, Fiscal Analysis Division. 2003 Fiscal Report. Online at: <http://www.leg.state.nv.us/lcb/fiscal/Fiscal%20Report/2003/2003FiscalReport.cfm>
26. State of Nevada, Executive Budget in Brief 2003-2005, p. 79.
27. Schmidt and Barr, p. 16.
28. Ibid.
29. Caseload Summaries, September 20, 2004. Nevada Department of Human Resources, Welfare Division
30. Ibid.

31. Revenue Plan Fact Sheet, 20th Special Session - 2003.
32. *Las Vegas Review-Journal*, September 30, 2004.
33. Ibid.
34. U.S. Bureau of Labor Statistics.
35. Nevada State Demographer's Office: Nevada County Population Projections 2004 to 2024, on the web at <http://www.nsbdc.org/demographer/pubs/images/2004proj.pdf>
36. *Las Vegas Review Journal*, November 9, 2004.
37. *Las Vegas Review Journal*, July 2, 2004

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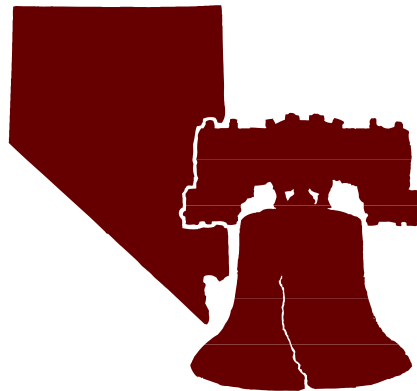
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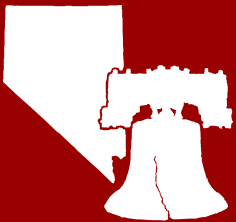
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