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The Tax Revolt Turns 25

by Michael J. New

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June 6 marks the 25th anniversary of California's Proposition 13, the landmark victory of the 1970s tax revolt. Proposition 13 enjoyed immediate success, slashing property taxes and imposing some much needed discipline on state and local spending. Twenty-five years later, however, California's fiscal situation has changed dramatically. State expenditures have soared and the legislature is considering large tax increases to compensate for California's \$35 billion shortfall. Indeed, California's changing fiscal fortunes provide valuable insights for those seeking to limit government in California and elsewhere.

During the late 1970s, anti-tax activists enjoyed considerable success limiting property taxes. However, Proposition 13 easily became the most well known of those efforts. Indeed, Proposition 13 was a tremendous short-term success, reducing taxes by a staggering \$6 billion. Proposition 13's impact, however, went far beyond tax relief. The economic boom that followed Proposition 13 gave credence to the idea that tax cuts were economically beneficial. Furthermore, Proposition 13 generated nationwide momentum for tax reductions. Even President Carter and the Democrat-controlled Congress were motivated to reduce capital gains taxes in the wake of Proposition 13.

As a long-term tax limit, however, Proposition 13 has had a legacy that is decidedly mixed. Though it reduced property taxes, Proposition 13 did not place limits on other forms of taxation. Indeed, after California's expenditure limit was raised in the early 1990s, spending soared, nearly doubling between 1990 and 2001. As a result, California has had to raise the income tax, the sales tax, and taxes on beer, wine, gasoline, and cigarettes to keep pace with these rising expenditures. In fact, during the early 1990s, Gov. Pete Wilson even proposed hiking taxes on snack foods. This cycle of spending and taxing is the root cause of California's current fiscal problems.

Indeed, California's recent fiscal history clearly demonstrates that low taxes can only be preserved when spending is restrained. In fact, during the past 25 years fiscal conservatives in California and elsewhere have attempted to enforce fiscal discipline by enacting Tax and Expenditure Limitations (TEs), which establish limits on expenditure growth. Many studies find TEs to be ineffective. However, in the early 1990s two states, Colorado and Washington, were able to restrain spending by enacting TEs with especially low limits.

The success of Colorado's TEL, the Taxpayer Bill of Rights (TABOR), is probably the most dramatic. TABOR was unique because in addition to setting a low expenditure

limit, it mandated immediate taxpayer refunds of surplus revenues. Shortly after TABOR was enacted, revenue began to exceed the limit. As a result, Colorado taxpayers received a tax rebate every year between 1997 and 2002. During that time, Colorado reduced taxes more than any other state, issuing tax rebates that have totaled more than \$3.2 billion.

Additionally, TABOR has also forced Colorado residents to see the costs inherent in government programs. In other states, residents often support higher spending because they can see the benefits of a particular program, but remain blissfully unaware of the costs that they and other taxpayers will be forced to bear.

However, in Colorado the annual tax rebates bring these tradeoffs into focus. In every year from 1993 to 1999 there was a proposal on the ballot to either raise taxes or increase spending in excess of the TABOR limit. Knowing those initiatives would reduce the size of their annual tax rebate, voters defeated them. In 2001, an initiative to increase spending for Colorado schools did pass. However, Colorado taxpayers still received tax rebates totaling more than \$900 million from fiscal 2001 revenues.

Overall, Proposition 13 enjoyed a great deal of success at lowering taxes, both in California and across the country. However, it has been less successful at keeping taxes low. Indeed, soaring expenditures over the last 25 years have resulted in sharp tax increases in the Golden State.

Still, one important lesson from the 1990s is that well designed expenditure limits can both effectively restrain spending and provide tax relief. Indeed, spending limits modeled after Colorado's Taxpayer Bill of Rights may well be the best strategy for those seeking to reduce the size of government during the next 25 years.

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