value. Courts long tolerated such de facto variations in assessments, but in the latter part of the twentieth century they more vigorously enforced uniformity rules and analogous provisions requiring property to be assessed at full value. Constitutional controversies concerning assessments have also been triggered by state laws that seek to cushion the burden of property taxes on certain uses, like agriculture or open space, by permitting such property to be assessed at a lower percentage of value or according to "current use value" rather than fair market or exchange value. Some state constitutions now expressly authorize differential tax rates or assessments by providing for the "classification" of property into commercial, industrial, residential, and other classes and requiring uniformity of tax treatment only within a class. Some state constitutions also authorize, or require, the exemption of certain property (educational, charitable, religious) from taxation. Even in states that authorize classification or exemption, issues continue to arise concerning the definition of classes, whether a property falls within a particular class, or whether the provision of other tax preferences violates uniformity. As a result state courts may be more involved in reviewing the constitutionality of tax differentials and tax preferences than their federal counterparts.

Substantive Limitations on Local Taxation

Most state constitutions impose some substantive limitations on local taxation. Until recently, reflecting the historic primacy of the property tax in state and local finance, these were focused almost exclusively on that tax. Limitations "first appeared in state statutes in the 1870s and 1880s and were later incorporated in many state constitutions." These were aimed at holding down government spending and protecting property owners. A "second round of constitutional tax limitations appeared during the Depression of the 1930s. They were aimed at forcing tax reductions, thereby stemming the tide of tax delinquencies and tax foreclosures of residential property."[61] A third wave of constitutional limitation of taxation began with California's adoption of Proposition 13 in 1978, and continues to some degree to this day.

These tax limitations have taken a variety of forms, including: (1) limitation on the tax rate; (2) limitation on assessments of particular parcels; (3) limitation on the rate of increase in assessment or the rate of increase in tax due from a taxpayer; (4) limitation on the total levy from the locality as a percentage of the community's assessed valuation; (5) limitation on the rate of increase in the community's total levy.

California's Proposition 13 focuses on limiting tax rates, assessments, and assessment increases. Massachusetts's Proposition 2½, adopted in 1980, addresses the community-wide levy, by limiting the total property tax yield to

2.5 percent of total assessed valuation, and limiting the increase in total revenue raised by the property tax in each locality to 2.5 percent per year.[62] Many older limits also capped local property tax levies as a percentage of local assessed valuation.[63] These different forms of tax limitation can have different incentives for community land use practices, and on local capacity to finance services.

Voter Approval Requirements

Some of the older tax limitations permitted local overrides, and higher rates or levies, if authorized by a local referendum. Proposition 2½ similarly permits local voters to override the 2.5 percent limit on the rate of local property tax revenue increase (but not the 2.5% total levy cap). The round of tax limitations that began with Proposition 13 has given new prominence to the role of the electorate in taxation. Several state constitutions—for example, those of California, Colorado, Michigan, and Missouri—make new local taxes or tax increases subject to voter approval. Similar measures were adopted by voters in Montana and Washington, though the supreme courts of these states held the initiatives violated state constitutional single-subject requirements.[64] Efforts to require voter approval of new taxes or tax increases have also been underway in Arizona, Florida, and Oregon.[65] These go beyond the traditional constitutional focus on the property tax and apply to all local taxes. Indeed, the Missouri measure applies to licenses and fees,[66] although the state's courts have struggled over the application of the voter approval requirement to nontax revenues.[67]

Limitations on State Taxation and Expenditures

In the post–Proposition 13 wave of tax limitation, many states amended their constitutions to constrain state taxation, not just local taxes or the property tax, which were the traditional targets of constitutional regulation. Proposition 13 prohibits any increases in state taxation without approval of two-thirds of each house of the California legislature.[68] The constitutions of a dozen states now require a legislative supermajority (ranging from 60% to 75%) for new or increased state taxes.[69] A number of states have also adopted constitutional or statutory measures that cap either state revenues or state appropriations. Generally, these measures seek to limit any increase in revenues or expenditures to the growth in state personal income, growth in state population, growth in the cost of living, or some combination of these measures, relative to a baseline year.[70]

Michigan's Headlee Amendment is illustrative. In addition to limiting local taxes, the measure establishes a state revenue limit "equal to the product of the ratio of Total State Revenues in fiscal year 1978–79 divided by the Personal

Income of Michigan in calendar year 1977 multiplied by the Personal Income of Michigan in either the prior calendar year or the average of Personal Income of Michigan in the previous three calendar years, whichever is greater."[71] The state legislature is prohibited from imposing "taxes of any kind which, together with all other revenues of the state, federal aid excluded, exceed the revenue limit." In any fiscal year in which total state revenues exceed the revenue limit by 1 percent or more "the excess revenues shall be refunded pro rata based on the liability reported on the Michigan income tax and single business tax (or its successor tax or taxes) annual returns filed following the close of such fiscal year. If the excess is less than 1 percent, this excess may be transferred to the State Budget Stabilization Fund."[72] This limit can be exceeded only if the governor's declaration of emergency is confirmed by two-thirds of the members of each legislative house.[73] Missouri's Hancock Amendment is very similar.[74]

Effects

Empirical research on tax and expenditure limitations (TELs) has found several broad effects, although the effects vary considerably from state to state according to the terms of the specific restrictions.

Reduced Role of the Property Tax

TELs have contributed to the reduction in property taxes as a percentage of personal income and in the role of property taxes in funding local government. Nationwide (including the many states that did not adopt TELs), the property tax share of personal income dropped from 4.1 percent in 1978 to 3.2 percent in 1982, rebounded to 3.7 percent in 1992, and dropped modestly after that. In California, which adopted one of the most stringent property tax limits in the country, the share of county revenue from the property tax dropped from 33.2 percent in 1977–78 to 11.6 percent in 1995–96; the role of the property tax in funding cities and special districts dropped as well.[75]

Increased Role for Nontax Revenue Sources

TELs appear to have contributed to an increase in the role of assessments, fees (including development impact fees) and user and service charges in funding local governments. One study found that for California cities the percentage of current revenue from service charges rose from 25 percent in 1977–78 to 41 percent in 1999–96.[76] Nationwide, by the early 1990s, fees and charges accounted for 14.6 percent of total local revenues and 23 percent of local own-source revenues.[77]

This development has involved both greater state and local efforts to fund public programs out of fees, charges, and assessments imposed on service users and the immediate beneficiaries of government spending—rather then rely on

more redistributive general taxation—and a greater state judicial willingness to expand the notion of what constitutes an assessment, fee, or charge, rather than a tax.

Traditionally courts have ruled that fees and assessments are not taxes—and therefore outside the scope of constitutional tax restrictions—for one of two reasons.

1. In the case of a fee or charge, payment was not coercive but contingent on the payer's decision to use a service, or was intended to offset a cost imposed by the feepayer's activity. Either way, by foregoing the service or the activity, the payer could avoid the fee. So, too, where the size of the fee is based on the amount of the service used, or the extent of the activity triggering regulation, the payer could reduce its liability by reducing its usage or activity. As a result, the payment was considered voluntary, not coercive—with coercion the hallmark of a tax.[78]
2. In the case of assessments, these were traditionally used to fund new government infrastructure—like a street, sidewalk or utility hookup—directly adjacent or connecting to the payer's property. As a result, the payer was provided with a benefit worth at least as much as the assessment. Although the assessment was still coercive—a property owner could not choose to avoid the assessment by declining to have his sidewalk paved—the provision of a special benefit directly to the property owner enabled courts to conclude that the assessment was not a tax in the constitutional sense.[79]

In recent years, many state courts have come to embrace a broader view of the permissible uses of fees and assessments. Some state courts have validated regulatory fees without tying a particular firm's fee to the costs attributable to that firm—thereby reducing the ability of the firm to use changes in its behavior to control its fee and thus undermining the "voluntary" nature of the fee.[80] So, too, many state courts have sustained a dramatically expanded use of the assessment to finance traditional municipal services and programs that provide diffuse benefits to relatively large areas, with the payer's assessment calculated based on his property value. Despite the close resemblance to the property tax, courts have upheld such assessments when the area benefited is less than the entire municipality.[81]

Combining the assessment and fee concepts, many state courts have upheld development impact fees, which require developers to pay in advance for a host of municipal services and improvements—including new roads, new schools, and expansions of water supply and sewage systems—required by the population growth attributable to the development. These charges are based on property, impose costs that are presumably passed along in increased property

prices to new home buyers, and pay for traditional municipal services. But viewed as assessments or fees they are not subject to state constitutional constraints on taxation.[82]

To be sure, some courts have attempted to police the fee/tax line more closely and have required that to avoid treatment as a tax the fee must be truly voluntary and calibrated according to the payer's use or the cost the payer imposes.[83] Moreover, some fairly recent state constitutional amendments explicitly impose voter approval requirements on fees and special assessments.[84]

Nevertheless, it appears that much as the debt limitations stimulated the proliferation of new forms of public borrowing that avoid the constitutional "debt" label, the tax limitations have spawned a host of revenue-raising devices that avoid the constitutional "tax" label. As with debt, a significant share of state and local revenue is now raised by devices not subject to tax limits, although, unlike the case with debt, most state and local revenue is still raised by constitutional taxes. Like the debt limits, the tax limits have also added to the complexity of local government structures by inspiring states and localities to create special districts and other limited-purpose governments that are not subject to constitutional restrictions.[85]

Moreover, the rise of nontax revenue sources has reduced the ability of states and especially local governments to engage in redistributive programs. The key to the exemption of fees, charges and assessments from the label of "tax" is that they provide the payers with a benefit at least equal to their payments (or to the social costs imposed by the payer's behavior). By definition, this precludes the use of fees and assessments to finance broadly redistributive activities. Assessments and fees enable those willing and able to pay for higher levels of service for themselves to do so, but the poor remain dependent on the votes of the community as a whole to approve the taxes necessary for the services that benefit them.

Shift in Power to the States

TELs imposed on local governments may have contributed to a shift in power to the states. The fiscal limits on local governments are typically more stringent than those imposed on the states, and they have made local governments more dependent on state aid. For California counties, for example, the share of revenue from intergovernmental transfers rose from 50.6 percent in 1977–78 to 64.1 percent in 1995–96.[86] With limits on local property taxation, the state also now plays a greater role in allocating local property revenues among competing local governments.

Reduction in Local Revenue Growth

Even with the growth in intergovernmental aid, new taxes, and nontax local revenues, TELs appear to have reduced local revenue growth. To be sure, the

impact of the TELs has varied from state to state, according to the stringency of the limits, changes in the economy, and subsequent state legislative or constitutional action. But for the most part, revenues in states with TELs have grown more slowly than in states without them.[87] To that extent, then, state constitutional limitations on taxation have succeeded where the state limitations on debt appear to have failed. But this poses more directly the question of whether this is an appropriate goal for state constitutions.

THE REFORM AGENDA

Initial Considerations

Two initial considerations ought to shape the general question of what public finance restrictions ought to be in state constitutions. First, what matters need to be constitutionalized, that is, placed beyond the day-to-day control of the political process and instead entrenched in the fundamental structure of the states? Second, even if in theory a rule or principle ought to constrain ordinary politics and be protected from politics rather than subject to politics, is constitutionalization an effective means of obtaining that goal? Considering these considerations in light of the purposes, history, and contemporary applications of the state public finance provisions leads to two paradoxical outcomes.

First, there is much to be said in theory for constitutionalizing the public purpose requirement and restrictions on debt. The fundamental purpose of government—the purpose that justifies the coercive taxation that enables government to pursue its spending and lending programs—is the promotion of the public good. Public purpose is essential to all government action. Moreover, it would be desirable to adopt a constitutional rule limiting the ability of the states and localities to dedicate public funds to private ends. State and local spending presents the classic problem of concentrated benefits for the politically influential few at the expense of costs diffused across the broad polity of taxpayers. Special interest groups have the incentive to lobby and the means to reward legislators who provide them with benefits. But the general public is unlikely to be sharply affected by any one interest group giveaway and lacks both the incentive and the means to police closely spending programs. Thus, there is a case for a public purpose limit on government spending.

So, too, it may be difficult for the public to effectively control debt through ordinary electoral control of state and local officials. As already noted, debt involves a combination of immediate gain followed by a cost at some point in the future. That cost will be felt by future taxpayers who can respond only by punishing future officeholders—who quite often will not be those who voted to incur the debt in the first place. Future debts are likely to be current campaign

issues, and concern about debt may be offset by the benefits from debt-funded programs. Debt limits are justified by the lack of effective political controls over the borrowing decision.

Yet, constitutional public purpose and debt limitations have been largely ineffective. Courts have expanded the notion of public purpose to the point where it encompasses virtually all forms of government activity. If direct assistance to individual private firms can be justified as promoting employment, then the constitutional public purpose requirement can no longer limit government spending. For the most part the courts have held that determining public purpose is a job for the political branches, not the courts. If that is the case, then a constitutional public purpose requirement is purely rhetorical.

The courts have been almost as tolerant of devices that evade debt limits, repeatedly indicating that arrangements that abide by the letter of the law—albeit barely—but not its spirit are constitutional. As several courts have stated, "it is never an illegal evasion of a constitutional provision or prohibition to accomplish a desired result, which is lawful in itself, by discovering or following a legal way to do it."[88] Indeed, the courts have praised debt evasion as a tribute to "the modern science of government" and a "constitutionally acceptable device of modern day progressive government."[89]

Second, limits on aggregate taxation or expenditures seem to have little justification. New or increased taxes, or increased spending levels that must be sustained by new or increased taxes, are immediately apparent to and felt by the voters. As the political power of the antitax movement has demonstrated in recent decades, the public is ready, willing, and able to make its sentiments on taxation known to elected officials. There is little need for constitutional limits to supplement public political control. Yet, such limitations are widespread and have to a considerable degree (at least compared with the debt limits) been enforced by the courts. While they have accepted some evasive devices, courts have been far more protective of the tax limits than the debt limits.[90]

As a result, the limitations that are most defensible in terms of the role of the constitution in addressing defects in the political process have been generally abandoned by the courts, while the limitations that have little constitutional justification have been somewhat more vigorously enforced. This both shapes and complicates the appraisal of the proper role of the state constitution in regulating state and local finance.

Public Purpose

The Public Purpose Requirement

The general public purpose requirement is a dead letter today and probably incapable of constitutional resuscitation. The courts are correct in noting the

broad expansion over the course of the twentieth century of what constitutes a legitimate public purpose. In particular, there is general political acceptance of the belief that government has some responsibility to promote economic development and, especially, employment. Today, the definition of what are the public purposes of government is a deeply political one, which may appropriately be left to the political process, not the courts.

The closer question involves the degree to which a particular program advances the stated public purpose of economic development, and what to do about public programs that provide large benefits to specific private firms as part of promoting the public purpose. Should courts strictly scrutinize the fit between the public end and the means chosen, or the balance between the public and private benefits? The courts have largely concluded that such review is beyond their capacity, and that the question of means as well as ends is a political question, not a judicial one.

Direct public aid to the private sector is a controversial economic development strategy. Most studies indicate that government financial assistance and tax breaks are relatively minor factors in corporate location decisions.[91] Moreover, corporations have proved adept at playing off competing localities against each other in order to extract government payments or tax exemptions. Even when companies do create new jobs in response to a government incentive, the payments may be short term and the firm may pull up stakes a few years later.[92] Given the difficulties of judicial policing of constitutional limits on economic development programs, a better strategy for promoting the public purpose might be statutory reforms that provide for better record-keeping and public disclosure of the benefits that economic development programs produce so that the ongoing political debate over these programs may be better informed.

Lending of Credit and Subscriptions of Stock

Two specific constitutional limitations on aid to the private sector—the bans on the lending of credit and the limits on public subscriptions of private stock—have fared better. The ban on the lending of credit makes sense. Lending credit in the sense of suretyship generates the fiscal illusion that it is cost-free. Government officials may persuade themselves that the contingent liability will never come due. Given that there is no initial out-of-pocket cost, voters may have little incentive to police these arrangements either. For that very reason, constitutional restriction is appropriate. On the other hand, the stock subscription ban seems to make little sense. Today, the principal effect of the ban is to preclude the government from taking an equity interest in the firms it is assisting, thus eliminating the possibility that the public might gain directly from its investment. It is difficult to see why it is permissible for the government to give public money away but not to get some of it back.

Debt Limitations

As already noted, there is a reasonable case for constitutional limits on debt obligations, yet the courts have been complicit in widespread evasion of these restrictions. The courts seem to be quite sympathetic to the programmatic spending goals—roads, dams, schools, power plants, convention centers, sports arenas, and economic development aid—that the debt limits would thwart. From this perspective, the debt limits appear to get in the way of good government in the era of the modern activist state, not to promote it.

Substantive Limitations

One reason for this lack of judicial sympathy for debt limitation may be the archaic nature of many of the constitutional debt provisions. Absolute debt prohibitions, laughably low dollar limits that date back to the nineteenth century, even carrying capacity percentage limits that are much lower than contemporary debt levels are completely out of step with the needs of modern government. Such provisions inspire, if they do not justify, evasion. One possible reform of the debt limits thus might look to simultaneously raising the level of the debt limit while redefining the limit to include all debts that would be repaid with public funds.

The difficulty would be to decide what is the appropriate debt level. Effective debt limitations require debt ceilings that are appropriate in light of the current ability to finance debt and current needs for debt-funded projects. Thus debt limits ought to be determined by setting debt service as a percentage of revenues, or as they are in some states, as a percentage of a moving average of revenues in recent years.[93] Determining the appropriate ratio of debt service to revenues is more difficult. There does not appear to be any theoretical basis for determining carrying capacity in theory or any consistency in practice among the states that take this approach. At best, any future debt limit is likely to proceed from a baseline of current debt levels. In so doing, however, such a debt limit ought to be based not just on the state's or locality's outstanding general obligation bonds, but on debt service payments for revenue bond, lease-financing, appropriation-backed debt and other obligations ultimately covered by state or local revenues.

Determining the appropriate level for a debt cap would also require adequate definition of the revenues that would be called on to pay these debts. In most states the local debt limit is defined as a percentage of local assessed valuation. Yet non-property-tax revenues play a considerable role in financing many localities. The local government debt cap ought to look to all local revenues, not just assessed valuation or property tax payments.

In short, if debt limits were modernized—and liberalized—to permit borrowing at levels adequate to the needs of today's state and local governments while still protecting the public from unduly burdensome future obligations, the courts might be more willing to enforce the restrictions and less inclined to wink at evasions than has been their practice in recent decades.

Voter Approval and Special Voting Rules

Separate from the question of substantive limitations is the role of voter approval and special legislative voting rules in authorizing debt. Some states subject debt to both substantive limitations and legislative supermajority and/or voter approval requirements; others rely on substantive limits or voter approval alone. Supermajority requirements and voter approval certainly provides an additional hurdle for elected officials who may be too quick to incur debt. The case for voter approval, however, is uncertain. It is not clear that today's voters will do a better job of representing tomorrow's taxpayers. Moreover, if politicians are too tempted to approve new debt, voters may be insufficiently attentive to the potential long-term benefits of the program the debt would finance. Low voter participation in most bond issue elections may reflect a lack of interest in or understanding of the cost and benefit questions that bond issues pose, and the voters who do participate may be unrepresentative of the electorate as a whole.

Still, debt—with its binding long-term nature—bears some resemblance to a constitutional amendment. Both commit future generations to a long-term course of action. Indeed, debt may be more binding since constitutional provisions may be repealed while debt creates interests protected by the federal Contracts Clause from subsequent state impairment. Most states have long required legislative supermajorities, voter approval, or both for both constitutional amendments and bond issues. It may thus be appropriate to continue to have a similar requirement for debt.

However, it makes little sense to have both a debt cap and a voter approval requirement for borrowing that falls beneath the cap. That would just reinstate the incentive to evasion. So, too, voter approval requirements without substantive limitations have given rise to evasion and judicial acceptance of evasive techniques. A better approach might consist of relying primarily on a substantive cap set by tying annual debt service to a percentage of a moving average of annual revenues, with that percentage based on the current debt service/revenue ratio (including all forms of current debt) and then permitting a jurisdiction to go beyond the limit with the approval of the voters. Referendum voters, thus, would have the ultimate authority over whether debt should exceed the constitutional cap, but debt within the constitutional cap would be treated as an ordinary political matter.

Taxation and Expenditure Limitations

Uniformity

The uniformity requirements are intended to promote the equal treatment of taxpayers but they also reduce the ability of states and localities to take into account the differential effects of similar tax burdens, and to use taxation as a policy-making tool and not just a revenue-raising device. Indeed, in many states

uniformity requirements have been modified with provisions for classification and exemptions, thereby shifting questions of tax preferences and tax policy back to the political process. Uniformity of taxation, subject to some form of classification, seems to be a well-accepted constitutional norm.

Limitations

The tax limitation provisions are more controversial. Tax limits, like debt limits, suppose that the level of taxation is a constitutional matter, rather than one for resolution by current elected officials. But whereas the long-term consequences of debt obligations provide some support for treating debt as a quasi-constitutional matter, tax rates may easily be changed, and politicians who enact high taxes may be punished by the voters in the next election. Certainly as the last two decades have demonstrated, antitax forces are well represented in the political process. It is not clear why further constitutional protection needs to be superimposed on the protections provided by the ability of the voters to vote out of office elected officials who raise taxes.

State constitutional limitations on local taxation seem particularly inappropriate. Local government actions may be more transparent than state decisions and many local governments are subject to effect monitoring, participation, and political control by grassroots taxpayers. Local taxation is further constrained by the vigorous interlocal competition for mobile taxpayers. Given the existence of both significant exit and significant voice opportunities it is unclear what constitutional need state tax limits on localities serve. Moreover, substantive constitutional limits on local taxation seem in tension with local autonomy since they preclude localities where the people are willing to support tax increases from taking such action. Holding all local governments to the same limit seems inconsistent with the recognition of interlocal variation and diversity that animates home rule.

Whatever the theoretical difficulties with constitutional limitations on state and local taxation they are widespread and appear to enjoy considerable popular support. Indeed, whereas the public purpose requirements and debt restrictions largely date back to the nineteenth century—with some twentieth century revisions—many of the tax and expenditure limitations, including some of the most rigorous provisions, are recent developments. Tax limitations are here to stay.

If we are to have tax limitations, are some constitutional provisions preferable to others? As noted, there is considerable variety in the type of tax limitation, including rate caps, levy caps, levy increase caps, and caps on increases in individual taxpayer liabilities. And, of course, within each category, there is interstate and intrastate variation in the number or percentage of the cap.

There is certainly something to be said for limits that aim at protecting taxpayers from sharp swings in their liabilities—swings that result from appreciations