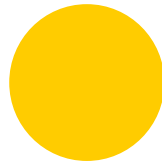


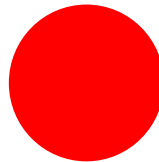
Why Tax Relief and Reform?



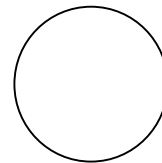
Equity,



Efficiency,



Adequacy



for a healthy Tennessee

Presented to
the Tennessee Tax Structure Study Commission

By
Tennesseans for Fair Taxation

July 31, 2003

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Introduction



Tennesseans for Fair Taxation appreciates the willingness of each member of the Tennessee Tax Structure Study Commission to serve the People of Tennessee. Yours is not an easy task. To say that this Commission holds the state's future in its hands—for reasons we will spell out within this presentation—is no exaggeration.

TFT has been engaged in the issue of tax reform since 1984. In recent years our state-wide grassroots coalition has grown to more than thirty member groups and hundreds of individuals, for a combined membership of many thousands throughout the state, with representation in every county. TFT is made up of people from all walks of life, who are concerned about the continued fiscal crisis that the state and people of Tennessee face.

TFT is truly grassroots, with our volunteer members working for positive change in Local Organizing Committees (LOC's). Currently, there are LOC's in Jackson, Knoxville, Nashville, and Oak Ridge; and coming together in Chattanooga, Clarksville and Memphis. We have offices in Knoxville and Nashville, with five staff (two full-time). Both our membership and outreach work puts us in touch with people from every income strata and most occupations.

Although a diverse group, we are also unified by our understanding of the need to reform our tax structure so that it meets three vital criteria: equity, efficiency, and adequacy.

Equity: TFT believes that our current system of sales taxation is wrong because those at the bottom of the income scale pay much more than those at the top. The system should be fair, with the tax burden distributed as evenly as possible among all taxpayers.

Efficiency: TFT believes that a state government in perennial fiscal crisis cannot be anything but unproductive. How can elected officials, private and public agencies, business and individuals be proactive when having to constantly react to problems caused by an antiquated system? The time and energy spent each year dealing with our state's constant budget troubles is woefully wasteful. TFT desires a system that neither relies too heavily on one source of revenue nor is overly complex in its structure or delivery.

Adequacy: TFT believes a state that has the 16th largest population, ranks 49th in spending per capita, and enacts large cuts into an already under-funded state budget will continue to stay in crisis. Such a system ensures that Tennessee will remain at the bottom in high-tech jobs, degreed workers, and overall health while staying at the top in number of bankruptcies, high school dropouts, and infant mortality. TFT calls for a system that ensures enough revenue to provide for the general health and welfare its citizenry.

In the following pages, TFT will show how so many of the state's challenges are fundamentally brought about by our dysfunctional and regressive tax system, and how real tax relief and reform is the vital step in resolving these problems. We will "connect the dots" of equity, efficiency and adequacy. We'll explain how lack of these three criteria keep us in recurring fiscal crisis, and why they are essential for a healthy Tennessee.

We will also outline our solution and address support for tax reform by the Silent Majority. Despite inaccurate information to the contrary, there is convincing evidence that most of the public favors the type of balanced tax relief and reform that TFT continues to put forward.

Inequity: Our Tax System is Unfair



Tennessee has one of the most inequitable tax systems in the nation. Two nonpartisan sources, the Institute on Taxation and Economic Policy (ITEP) and Congressional Quarterly, rank Tennessee as third and first, respectively, among worst states with regard to taxing those at the lowest income levels more than those at the highest. Economists call placing the tax burden on those least able to pay regressive. We call it unfair.

For example, a Tennessee family making less than \$22,000 a year pays more than three times the taxes as a portion of their income than a family making ten times that much. This is what TFT means when we say our system is unfair!

Why is Tennessee's tax system so unfair?

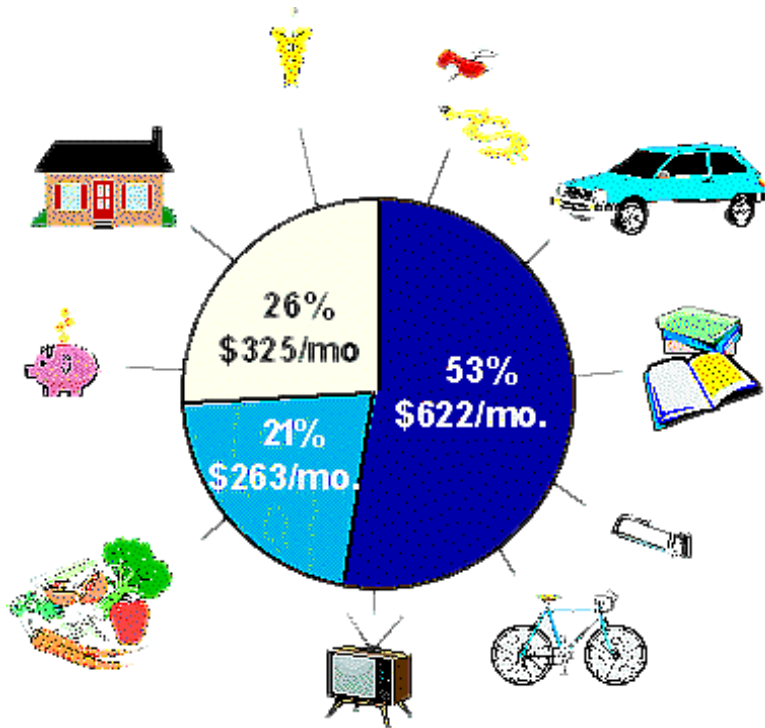
- Unlike other states that rely on a variety of revenue sources, Tennessee raises nearly 61% of its state revenue from sales taxes, alone, and almost 80% from sales and selective sales taxes (gas, alcohol, etc.), combined.¹
- Tennessee, at a maximum of 9.75%, has the highest average sales tax rate in the nation. **And**, Tennessee taxes food; 33 states do not.
- Sales and other consumption taxes place a heavier burden on low- and middle-income families by taxing what people spend on basic necessities and other goods, rather than on their total income.
- As household income rises, a smaller portion of income is spent on food, clothing, transportation and other goods subject to sales tax.
- High-income families spend more of their budget on services, savings and investments, thereby shielding their income from the sales tax.




To illustrate the concept of percentage of income taxed under our system of sales taxation, let's look at two family budgets:

In our state, a family with take-home pay of \$15,000 per year has approximately 75% of their budget subject to sales taxation. While a family with take-home pay of \$100,000 has approximately 25% of their budget is subject to tax.

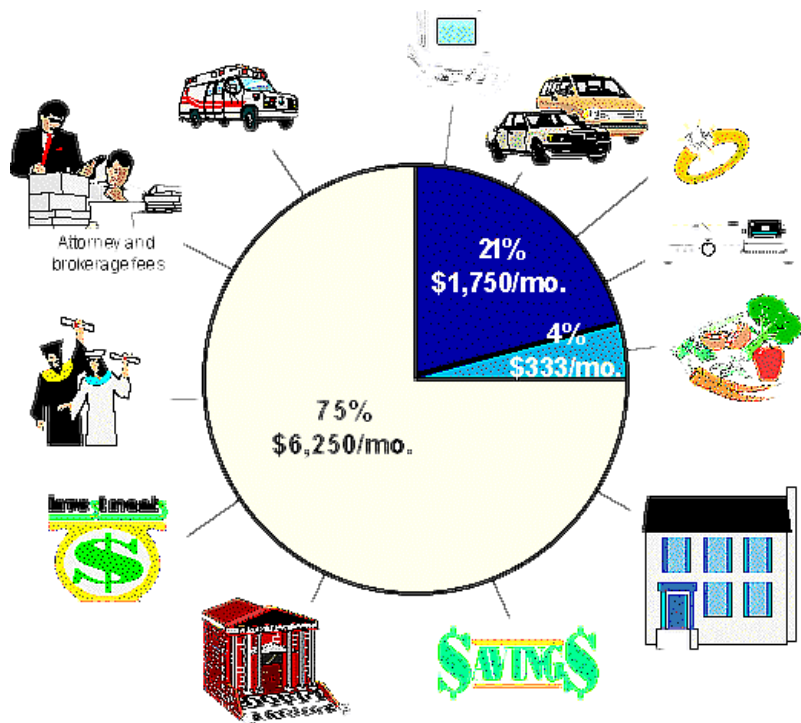
- **Tennessee has the nation's highest average food tax of 8.35% (as high as 8.75%).**
- Tennessee is one of the hand-full of states that still taxes food.
- It doesn't take much math to figure it out why the food tax is unfair. Just because someone makes ten times what the average Tennessean makes, it doesn't mean they are going to eat ten times as much.
- Groceries represent 1/5th of the budget of a family making less than \$20,000 while it only represents 1/25th of the budget of a family making \$70,000 or more.
- By eliminating the tax on food, the average family would save enough annually to buy a whole month's worth of groceries.

Family One:
\$15,000 income;
75% subject to
sales taxation



	Food for home consumption: <u>8.75%</u> sales tax.
	Other tangible goods: <u>9.75%</u> sales tax.
	Expenses where <u>sales tax is typically not applied.</u>

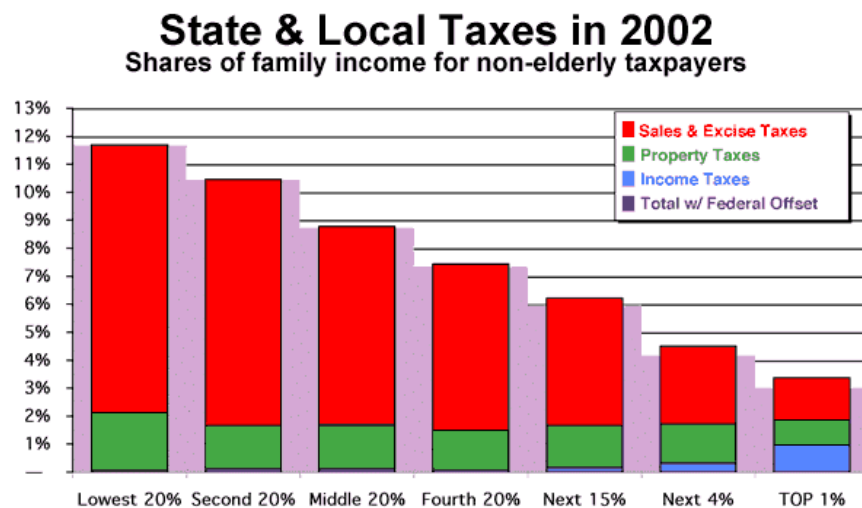
Family Two:
\$100,000 income;
25% subject to
sales taxation



As the majority of Tennesseans are unfairly burdened by the regressive sales tax, surrounding states are moving to repeal their food taxes:²

- Kentucky eliminated its food tax over 25 years ago;
- Georgia began phasing out of its food tax in October 1996;
- Georgia then eliminated its state food tax in October 1998;
- North Carolina reduced its food tax by one percent in January 1997;
- North Carolina again reduced its food tax one percent in July 1998;
- North Carolina eliminated its remaining state food tax in May 1999;
- Virginia reduced the food tax to 4% in January 2000;
- Missouri reduced its state tax on food by 3% in October 1997.

Because of Tennessee's heavy reliance on the unfair sales tax, which taxes food and other necessities, low- and middle-income families pay far more taxes, as a portion of their income, than the highest income earners.



According to the *Institute on Taxation and Economic Policy* also known as ITEP, Tennessee now ranks third nationally in its terrible ten list of the most regressive tax systems in the country. This inequity is illustrated in the graph above, taken from ITEP's 2003 *Who Pays: A Distributional Analysis of Taxation in the 50 States*. *Congressional Quarterly* actually ranks Tennessee number one as having the most regressive tax system in the nation.

The data is clear: Tennessee is one of the worst of the worst when it comes to fair taxation.

Inefficiency: Our Tax System is Unreliable, Outdated



We hear so much about the need to make both government and business more efficient. How many governments or businesses are operating exactly as they were during the Great Depression or when Disco was the rage? Well, Tennessee for one.

Tennessee's tax laws are truly outdated. Our tax on corporations was drafted in 1976, when there were a limited number of forms for doing business. Now there are S-Corporations, C-Corporations, Professional Corporations, holding companies, REITS, Limited Partnerships and Limited Liability Companies. The federal income tax laws have adjusted to the changing forms of doing business. Tennessee cannot even recognize S-Corporations because under federal tax law that type of corporation is a flow-through entity and taxed at a personal level. Limited liability companies are taxed as C-corporations in this state, even if the business is a single-member Limited Liability Company, which is ignored for federal tax purposes. *Confusing?* Imagine the time and energy spent by businesspeople trying to minimize the tax impact of the unequal ways the state and federal business tax laws!

Many are surprised to learn that our state has a personal income tax. Our personal *income tax* is the Hall Tax. It was enacted in 1931, back when many Tennesseans did not have electricity.

Hall Tax rates and exemptions are basically the same as they were at the height of the Depression. Then, as now, \$1,250 of interest was an outrageous amount for a single person as was \$2,500 for a married couple. Today, many elderly clients pay far more in Hall Tax than in federal taxes, and many owe the state several hundred dollars each year, but have incomes that are too small to require them to even file a Form 1040. Seventy years ago the law distinguished between interest in banks and interest from bonds and money markets. There is no reason for this, except to encourage Tennesseans to put their money in lower return investment vehicles. The Hall Tax has been called the banker's tax, since it punishes those who put their money into other investments.

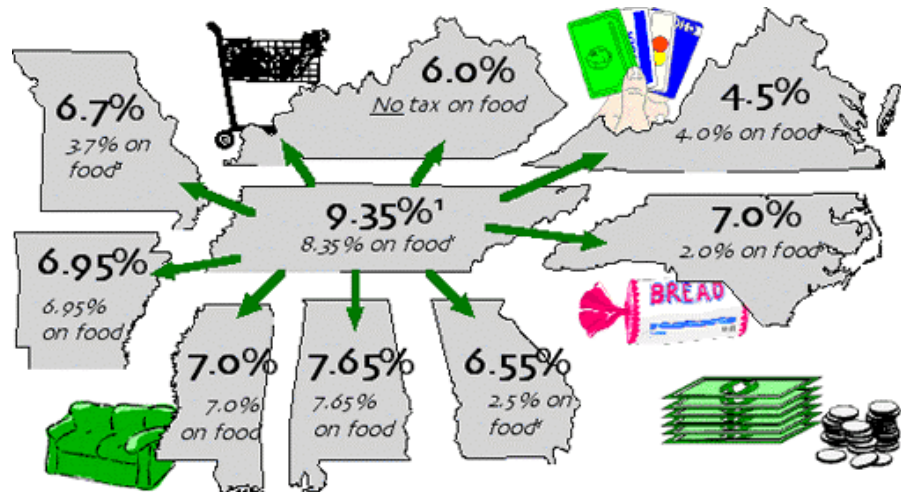
As costly as these outdated structures are to our state and the businesses that operate within our borders, they are nothing compared to the scandalous way we try to fund our state government and critical services with a sales tax. Tennessee has the unfortunate distinction of having the highest combined state and local sales tax of any of our fifty states, at an average rate of 9.35%.

Sales tax began in Tennessee the 1940's, long before we became a service-oriented state, had interstate highways, the Shopping Channel, home PC's or the Internet. Yet a few folks in our state stubbornly cling to sales tax as the primary revenue source. Sales tax is unreliable and easy for consumers to avoid. In other words, it is an inefficient way to raise revenue.

Tennesseans are nothing if not resourceful. Yet even if they were not, it would still be easy to avoid paying the highest sales tax in nation. Today, it's a breeze to shop anywhere from home by going online, picking up the phone, or dropping a check in the mail. Yet Tennesseans can also shop the old-fashioned way, customer to merchant. The only difference is that now the merchant happens to be in another state.

Tennessee borders eight states with lower sales tax rates. Approximately fifty percent of Tennesseans live in border communities, including Memphis, Chattanooga, Clarksville, and the Tri Cities. Every day shoppers leave Tennessee to shop in a neighboring state.





- **Cross-border shopping:** In our increasingly mobile society, people driving to neighboring states to avoid Tennessee's high sales tax represent a growing loss of revenue to the state and jobs for our citizens.
- **Internet sales:** Online sales is the fastest growing hole in the sales tax base. State and local revenue loss due to online sales was \$192 million in 2001 and is expected to reach \$808 million by 2011.
- **Mail order shopping:** Catalog shopping is a long-established and continually growing hole in the sales tax base. State revenue lost to mail order sales was \$77 million in 1996 and has continued to grow since then.
- **The service-based economy:** The sales tax is a tax on tangible goods, not services. As we become a more service-oriented economy, the sales tax becomes less and less effective as a revenue source.
- **Investments:** The sales tax applies to basic necessities like food, clothing, home furnishings, and transportation. It does not apply to things like investments, attorney fees, house clearing services, and college tuition. As a result, high-income families pay only a fraction of the taxes that others do.

Tradition and knowledge of the past are valuable as foundations for our rapidly changing culture. But to insist on doing business the same way it was done in the prior century is regressive not progressive. We cannot survive the changes that we must face by clinging to an outmoded tax system. In the business world of today, what was good enough for grandpa and grandma many years ago just won't cut it. Tennessee finds itself at the wrong end of so many lists of measures of well being. Clinging to outdated measures means that we are living in the past and have no future. Who wants that?

Inadequacy: Our Tax System Can't Handle the Basics



Business Week reported in June of this year that: "There's no evidence that state and local spending is out of control.³ Even if spending were out of control in some states, it is not in Tennessee, as *By the Numbers: Tennessee's Rankings 2002* points out:

"There cannot be much waste in state government when the 16th largest state population is served by the 41st largest state government workforce and funded by the 49th or 50th rate of tax revenue."

During the last four years of budget debates, a few loud voices have contended that Tennessee State Government spends too much. These voices are quieter now that the current budget has cut spending and cut services in every area of government and passed along significant cuts to local government in the form of reductions in state shared revenues.

Remember how the gap between revenues and proposed expenditures was closed?

- There was the \$900-million sales tax increase in 2002.
- We continued to take the Tobacco cases settlement payments for the cost of general government. We lost the opportunity to apply these funds to anti-smoking, healthcare or tobacco farmer relief programs.
- Transfer of virtually every special, earmarked or reserve fund with the likelihood that the loss of these funds and their funding sources will be permanent.
- A portion of the previously "untouchable" dedicated fuel tax was transferred to the General Fund, but not permanently. This suggests an annual debate that will pit highway construction against other public needs.
- The loss of "state shared revenue," which is causing both services cuts and tax increases in local governments and school systems.
- We hope the Commission is keeping track of the program cuts and tax increases (like property tax) and will report them with its recommendations.
- A nine-percent across-the-board cut for virtually all state agencies. Programs have been affected to different degrees.
- The human consequences of these program cuts are too much to go into here and now, but the adage "pay me now or pay me more later" applies when government can't do its job on time. Delayed healthcare, educational opportunities denied, and opportunities to purchase environmentally sensitive lands, for example, can only be repaired later at much greater cost or, in many cases, cannot be repaired at all.
- The revenue gap was closed, and some restoration of the "rainy day fund" allowed, by a commitment of an additional 400-million federal dollars for the TennCare program.

Our state's downgraded bond rating is still in place, causing us to pay higher interest to finance our long-term capital investments. "Trim, cut and squeeze" has allowed us to get by for a year,



but it seems unlikely to allow Tennessee to get back to the highest bond rating and the lowest interest rates.

Reduction in federal funding for some programs continues as Congress faces record dollar deficits. The costs of government services are not going down. No one has suggested that "deflation" is likely to reduce the cost of healthcare or government services like fire fighting or the TBI crime lab. The only deflation may be in the cost of an item in a WalMart, which will only serve to reduce the sales tax base.

The citizens of our State have resorted to the courts in efforts to obtain decent and equitable funding for education, minimum standards for prisons, a Children's Services department that lives up to its name, and to stop the state from taking 5% from every child support check it handled. The Governor and the Legislature should set budget priorities, not courts. But they can only comply with the requirements for programs and the federal cost sharing if the tax system produces adequate revenue.

Many of the effects of the state budget cuts for 2003-2004 have been outlined in the report *Shredding the Safety Net* published in May 2003 by Tennesseans for Fair Taxation, Tennessee Alliance for Progress and Tennessee Partnership on Organizing and Public Policy. Copies of the report have been provided for all committee members; and can also be found on our web site @ www.yourtax.org

Because of our outdated tax system, we have drastically under-funded services.

<p>Tennessee ranks poorly in many measures of social and economic health.</p>	<p>Tennessee is a low-spending state. (per capita)</p>
<ul style="list-style-type: none"> ● 4th in infant mortality ● 10th in number of families in poverty ● 9th in toxic chemical releases ● 42nd in "Condition of Children" index ● 44th overall health of citizens ● 48th in public HS graduation rates ● 44th in high tech jobs ● 1st in personal bankruptcies ● 4th in violent crimes per capita ● 3rd in most tax burden (regressivity) 	<ul style="list-style-type: none"> ● 45th in spending for home and community based care ● 42nd in environmental spending ● 43rd in corrections spending ● 49th in total education spending ● 47th in K-12 education spending ● 42nd ave. salary of state employees ● 47th in state & local expenditures ● 49th in state and local taxes <p><i>NOTE: stats compiled prior to 9% across-the-board 2003 state budget cuts.⁴</i></p>

As Susan Pace Hamill points out in her book *The Least of These: Fair Taxes and the Moral Duty of Christians*, "Although inadequate funding of public schools impacts all of Alabama's children to some degree, children from low-income families suffer the greatest negative effects, including a substantial risk of welfare dependency, imprisonment, a lack of employment skills, and little access to a higher education."

What is the situation here? Shockingly worse than Alabama. In Tennessee in 2001-2002:

- Tennessee's average expenditure per pupil was \$6,349, which ranks F" nationally.⁵
- Three out of four of Tennessee's school systems, or 74%, spent **less** than Tennessee's already poor average for per pupil spending. Perhaps they should be ranked "F" minus.

Some of the worst problems are in Tennessee's rural counties, which contain, arguably, the worst funded schools in the entire nation. Yet one-fourth of all children are educated in these rural schools

*"Saying that Tennessee has a "spending problem" rather than an income problem just does not compute. Any way you look at it, Tennessee is a low tax state and a low spending state," states Graham Greeson, Director of Research for the Tennessee Education Association (TEA). **"What we have is an investment problem....We are not investing sufficiently in those things which will sustain our quality of life: education and workforce preparation.** If we continue to ignore our fiscal crisis, we'll have no ability to attract 21st century jobs, and our personal income growth will sink to the bottom along with our other rankings....Those who oppose reasonable tax reform are helping to doom this state to one of the darkest periods in our history. Once we enter fiscal collapse, it will take us years, if not decades, to recover from it; and ground will be gained by other states that we will never recoup."*⁶

If press reports are an indication, in our State every elected official supports education as a high-priority goal for state funding. Obviously, an adequately funded public school system is **the most critical state and local function** for ensuring that our children enjoy minimum opportunities to achieve an adequate education and improve their lives.

This inadequate funding system and lack of educational opportunity contributes to Tennessee's rural counties stagnating with high unemployment rates.⁷ School under-funding and lack of opportunity certainly have an effect on the high crime rates that Tennessee experiences. As in noted in our *Shredding the Safety Net* report (p.5), Tennessee has the 4th highest violent crime rate in the nation—a problem that is very costly for both individuals and businesses in our state.

A critical and related area is preschool funding. Tennessee spends very little in this area compared to other states. We soon will lose more funding. As reported in the *Tennessean* on July 7, 2003, about \$9 million in short-term federal funding is being cut this summer, leaving only \$6 million in state funding to be split among 150 existing preschool programs. The amount of funding per program will go from \$98,000 to \$40,000 this year. Lawrence County, one of the poorest school systems, will have to cut one of its six classrooms. Local and county governments are now being forced to raise property taxes, if they want to fully fund their children's future.

Other evidence of Tennessee's poor record on children is the fact that the infant mortality rate is above the rate of many third world countries. Last year, the state had an overall infant mortality rate of 9.1 deaths per 1,000 live births, according to *Kids Count: The State of the Child in*

Tennessee, a document produced by the Tennessee Commission on Children and Youth. The 2002 rate puts Tennessee in 47th place in the nation. More startling is the fact that, according to the World Atlas, there are 45 countries with lower infant mortality rates than Tennessee.⁸

Tennessee has a revenue problem, not a spending problem. We cannot solve the state's budget crisis by further cuts, which threaten education, health care, clean air and water, our economy and the quality of life for our families.

Our Solution: Tax Relief and Reform



As the previous sections have demonstrated, in no uncertain terms, Tennessee's tax system is fundamentally flawed. It's unfair. It's inequitable. It's outdated. It's inefficient. It's inadequate. It simply needs to be fixed.

More importantly, the problem is not going to go away on its own. There are those who argue that we just have to wait for the economy to get better...that these are tough times everywhere as states across the nation are facing massive budget shortfalls. "When the economy gets better, things will start to brighten up," they argue.

This view, however, demonstrates both a lack of understanding of economics and historical memory. Think back to the late 1990's when both the national and state economies were booming. Most states were rolling up record budget surpluses. Many were even cutting taxes. But what about Tennessee?

The root of our state's trouble is found in this excerpt from a 1999 article entitled "Governor Sundquist's Revised Tax Proposal Would Address Long-Standing Problems with Tennessee's Tax System," written by Liz McNichol of the Center for Budget and Policy Priorities.

Tennessee is one of very few states experiencing revenue shortfalls and a budget deficit in the current healthy economic times. Projected revenue for fiscal year 1999-2000 under the current tax structure falls over \$400 million short of the amount needed to finance spending under the Governor's proposed budget.

The state's fiscal problems are not the result of a failure of the state to share in the current expansion. Tennessee's economy has been growing at a healthy rate since the end of the recession of the early 1990's. Employment growth and personal income growth have been above national rates and Tennessee's unemployment rate is below the U.S. average. Nevertheless, Tennessee's reserves are among the smallest of all the states relative to the size of the state's budget; the state has not been able to take advantage of the healthy economy to develop a cushion against future adversity.

Tennessee's fiscal problems lie with the failure of the state's taxes to grow with the economy. Tennessee relies heavily on the sales tax. As in other states, the base of the sales tax is composed mainly of goods rather than services. Spending patterns have been changing with a greater share of consumption being made up of services. As a result, sales tax revenue growth lags growth in the economy. This problem is especially pronounced in the states—including Tennessee—that tax food, because food consumption as a share of total consumption has been declining steadily.

So why was Tennessee's tax system faltering even when times were good? Because Tennessee has a structural problem related to our outdated tax system. What other states are experiencing now is a cyclical problem related to the economy. These are two very different situations.

When the national economy finally recovers—and it will—other states will again achieve a healthy growth in revenue, responding to the “cyclical” economic upturn. Tennessee, however, will still be facing deficit after deficit, year after year, despite any economic upturn. Why? Because we rely upon an antiquated tax structure, with sales tax as the primary source of revenue and incapable of generating sufficient revenue to meet the state’s needs.

What we are facing in Tennessee is a structural problem, and to fix a structural problem, you need to make structural change. That is exactly what TFT and our many coalition partners are proposing doing through comprehensive tax reform.

TAX RELIEF AND REFORM: COMMON-SENSE SOLUTION

Originally founded in 1984, Tennesseans for Fair Taxation is no newcomer to the tax debate. Over the years, we’ve looked at all the options. We’ve studied their impact on families at different income levels. We’ve examined their effects on economic growth and border communities. We’ve looked at the revenue generated for important public services.

In the end, the one solution that rises to the top is comprehensive tax relief and reform. The Tax Relief & Reform Act that TFT worked to get introduced in the 2003 legislative session is the model for what real tax reform looks like. Our plan:

- Eliminates the state and local tax on grocery food and nonprescription drugs;
- Reduces the state sales tax on other items by 2% (leave "sin" taxes at current levels);
- Eliminates the Hall Tax on investment income and replaces it with a broad-based graduated income tax with generous deductions;
- Creates a modest income tax consisting of two tiers of 3.5% and 6.5%, with exemptions of \$15,000 for single filers and \$30,000 for couples, plus an additional \$2,500 per dependent.

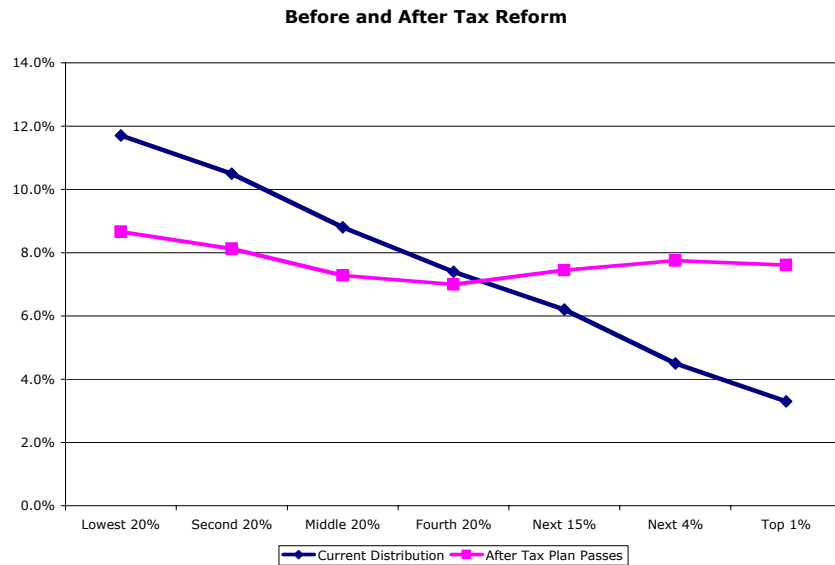
	Single	Head of House	Married (MFJ)
Base exemption	<i>\$0-14,999</i>	<i>\$0-22,499</i>	<i>\$0-29,999</i>
Taxed at 3.5...	<i>\$15,000-29,999</i>	<i>\$22,500-44,999</i>	<i>\$30,000-59,999</i>
Taxed at 6.5...	<i>\$30,000+</i>	<i>\$45,000+</i>	<i>\$60,000+</i>
<i>All taxpayers will receive an additional \$2,500 per dependent deduction.</i>			

Why this type of Tax Relief and Reform makes sense for Tennessee:

- 80% of Tennesseans will pay less taxes;
- It will create a more level playing field;
- It will raise an additional \$830 million, enough to avoid the proposed 9% across the board cuts (which have now been enacted);
- Because the state income tax can be deducted from federal taxable income, Tennessee taxpayers will save more than \$660 million in federal taxes. In other words, more than 80% of the additional state revenue will be paid for by federal tax savings.

In the end, we must measure the quality of a tax plan not by what it looks like, but by what it does. When we look at what this tax plan does, it is a success across the board.

Common-sense tax relief and reform will eliminate the unjust sales tax on food and non-prescription drugs. Tennessee remains one of a handful of states that still taxes food. This is a tax on life that unfairly burdens those struggling to make ends meet.



This plan will lower taxes for 80% of Tennesseans and create a more level playing field for everyone. The chart above illustrates the point. The blue line represents the relative tax burden across income levels now, while the pink line represents the relative tax burden after tax reform. Clearly, tax reform is about fairness, and by creating a level playing field, we can in fact lower taxes for most Tennesseans.

Our 2003 plan raises \$830 million in much needed state revenue. As you read in the Adequacy section, Tennessee is already ranked at the bottom of nearly every indicator that matters. Further budget cuts are simply not an option.

It will save \$660 million now being sent to Washington. By changing from a sales-tax based system to an income-tax based system, Tennessee can take advantage of federal laws that allow taxpayers to deduct state income taxes from their federal returns, saving Tennessee taxpayers millions. As most of you know, those that are most likely to itemize their federal taxes are typically higher income. As a result, federal deductibility will significantly reduce the added tax burden of those being asked to pay more under tax reform. (The chart above does not include federal deductibility.)

Tax relief and reform will reduce the export of Tennessee shopping dollars. By eliminating the food tax and lowering the sales tax, Tennessee can reduce the incentive for shoppers to leave the state, whether by car, phone, or on-line. Border communities and retailers have suffered long enough under Tennessee's high sales tax. Lowering the sales tax is good for Tennessee consumers and business.

Real tax relief and reform will fix the structural problem by making structural change. By establishing an income tax that is more responsive to economic growth over time, revenue will grow with the economy and reduce the need to raise the tax rate every few years.

By enacting tax reform, we can finally put the chronic budget shortfalls behind us and begin to join the rest of the nation with a more fair, efficient, and adequate tax system.



The Silent Majority



If you took your public opinion cues from Nashville's talk show hosts and some local columnists, you would say that one of Tennessee's unbreakable political rules is: "Thou shalt never advocate an income tax, or else...."

This bit of conventional wisdom has, in fact, represented one of the major barriers to achieving real progress in tax reform in recent years. Yet is the view that most Tennesseans do not support tax reform based on logic and fact? To the contrary, there exists compelling evidence that a Silent Majority today actually supports comprehensive and balanced tax reform, as advocated by Tennesseans for Fair Taxation and many others. And this Silent Majority is growing!

There is one question that tax reform advocates must now answer. How does the Silent Majority become an Outspoken Majority that commands the attention and respect of the General Assembly and the Governor?

Majority Does Support Tax Reform

Statewide Polling	% Support Income Tax Only	% Support Tax Reform Package including income tax
Sweeton's Analysis 1989 - 2001 (11 polls)	27	58 - 61
AARP December 2001	24 - 31	54 - 59
Citizens for Fair Taxes May 2002	25	58
Middle TN Poll (MTSU) Spring 2002	23	46
Fall 2002	22	58
Spring 2003	26	61

The fact that a stealth Silent Majority might exist was first hypothesized by Fred Sweeton, a TFT member from Oak Ridge. Sweeton examined 11 Tennessee tax-related polls taken between 1989 and 2001. These are all well-known, respected, scientific polls, such as those conducted by University of Tennessee and Middle Tennessee State University.

What did Sweeton discover?

- Polls that simply asked the question: "Do you support adopting an income tax in Tennessee?" usually found a positive response rate of about 27%.
- Polls that also mentioned some of the benefits of tax reform—such as a reduced sales tax or repeal of the food tax, along with an income tax—produced an average positive response of 38%, an increase of 11 percentage points.
- Polls that mention the full benefits of tax reform—general sales tax cuts, repeal of the tax on grocery food and non-prescription drugs, repeal of the tax on investment/dividend income (Hall Tax), and an income tax with large front-end

exemptions—revealed a **positive response of 58%**, that's *an increase of 31 percentage points*.

- Finally, Sweeton found that when a tax reform package is coupled with increased support for education, the **positive responses grew to 61%**.

Members of TFT asked ourselves: *Can this be true?* If it is true, why do most people seem to believe precisely the opposite conclusion? What is going on here?

The collaborating evidence began to accumulate.

AARP Polling

In December 2001, AARP conducted a scientific poll of its 650,000 members in Tennessee. In response to a question that included the total tax reform package—lower general sales tax, elimination of tax on groceries and non-prescription drugs, elimination of the tax on interest and dividends (Hall Tax) and a broad-based, low-rate tax on personal income with large front-end exemptions—**54% favored such a package**.

When the details of the income tax proposal were spelled out in the next question, such as a family of four earning \$40,000 would likely pay no income tax and less in other sales taxes, **the positive response rate increased to 59%**.

Citizens for Fair Taxes

In May 2002, Citizens for Fair Taxes, conducted a scientific, state-wide poll to measure support for the then Rochelle-Elsea-Head bill that contained the full package of reforms, including a cut in the sales tax, removal of the tax on food and non-prescription drugs, and a graduated income tax. **Fifty-eight (58) percent of the respondents indicated support for such a package**, validating precisely Sweeton's conclusion.

MT Poll and the Silent Majority

Middle Tennessee State University (MTSU) conducts the semi-annual Middle Tennessee (MT) Poll, a scientific statewide survey. In Spring 2002, MTSU found that 46% of respondents favored the full tax reform package, including an income tax. By the fall of 2002, the positive support had increased to 58%. **And this spring, the percentage of positive support had grown to 61%.**

It is equally important to understand that how the question is asked is key. In each of these polls, when a citizen is asked simply whether he or she supports a “state income tax,” without making it clear that it is part of a comprehensive and balanced reform package, support drops back to a level of 25% to 30%. Asking the question this way is like asking a patient whether he or she supports removal of their ailing appendix without making it clear that certain well-defined health benefits are associated with the procedure.

So where are we in trying to gauge the level public support for comprehensive and balanced tax reform? A clear majority of Tennesseans has repeatedly indicated its support for such a package of reforms.

An equally clear level of opposition exists to just tacking a personal income tax on top of our existing taxes. Yet always remember that no serious tax reform advocate—TFT at the forefront—proposes such action.

If all this is true—and TFT is convinced it is true—why does the conventional wisdom persist that Tennesseans are dead set against an income tax?

An excellent question—perhaps the key question in this entire debate. There is an answer . . . it requires linking the Silent Majority that supports tax reform to the Spiral of Silence that obscures and conceals the majority sentiment.

What is the Spiral of Silence?

The Spiral of Silence is a well-established phenomenon that reveals people are less likely to speak out if they feel their stance is opposed by what they think is a majority. This type of response is a natural survival response, most individuals remain silent when they believe their opinion is not in keeping with the group think.

The experts from MTSU put it this way: *“The majority who support an income tax with sales tax cuts don't know they're in the majority. They assume everyone else is against the plan. A vocal, well-organized minority can appear to be a majority. This causes the real majority to sit down and be quiet.”*⁹

How do we break the Spiral of Silence? These polls demonstrate that as people learn more about what tax reform really means, their support increases. Little by little, individuals who comprise the Silent Majority discover they are not alone. Little by little, they gain the courage to speak out. This, in turn, encourages their friends and neighbors to do likewise. Little by little, the downward Spiral of Silence is broken and replaced with an upward **Spiral of Support**. Public education is the key to this transition.

That's where the work of this Commission comes in. Tennesseans for Fair Taxation supports your work because we know that public understanding is the key to causing the Silent Majority to speak out. As you go about your vital work of recommending a way to fix our broken system, please know that a majority of Tennesseans supports comprehensive and balanced tax reform—conventional wisdom and talk show hosts notwithstanding.

End Notes



- ¹ *Distribution of Tennessee State Taxes 2002*, Office of the Comptroller, State of Tennessee
- ² Sales Tax Clearinghouse, 2/21/03, www.taxch.com/Strates.stm
- ³ "Local and State Spending Isn't A Problem," *Business Week*, June 16, 2003
- ⁴ Sources: *State Rankings 2003*, Morgan Quitno; *State Fact Finder 2002*, Congressional Quarterly; *Kids Count 2002*, TN Commission on Children & Youth; "Green and Gold 2000," Institute for Southern Studies; *Tennessee in Perspective 2003: A Statistical View of the "Volunteer State"*, Morgan Quitno
- ⁵ TEA Web Site <http://www.teateachers.org/membercenter/per-pupil-expenditures.php>
- ⁶ TEA Web Site <http://www.teateachers.org/newsctr/2002/jul/04003.php>
- ⁷ State of Tennessee Web Site http://www.state.tn.us/labor-wfd/labor_figures/
- ⁸ World Atlas http://www.geographyiq.com/ranking/ranking_Infant_Mortality_Rate_aall.htm
- ⁹ Middle Tennessee (MT) Poll <http://www.yourtax.org/facts/mtsu-poll03.php3>

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