

## Trickle Down Economics:

### Anticipating Significant Shifts in Local Political Climates for Library Taxes Following the 2017 Tax Reform Bill

John Chrastka

As a matter of tax policy, trickle down economics have been widely discredited by economists for over 30 years (Petroff, 2015). That has not stopped this Congress and the White House from envisioning (as of this writing) a singularly massive overhaul of the federal tax code that is rife with questionable supply-side policies that is likely to enshrine new inequities in American society for generations. Regardless of how you personally will be impacted by particular exemptions, deductions, reindexing or “trickles,” a loss of nearly \$150 billion dollars in revenue a year (\$1.5 trillion dollars over ten years) will have a significant impact both in the near-term ability of the federal government to fund programs at all levels of government, and to also service debt over the long-term.

In the lead up to this December 2017 bill, there has been little exploration of the shockwave that this loss of revenue will have on local government. As directors and board members for tax supported institutions, it is important for library leaders to understand the impact that federal tax policy has on local revenue in order to anticipate the significant changes coming at all levels of government and the subsequent impact on library budgets. At the federal level, IMLS and IAL funding is included in the current Continuing Budget Resolution (through December 8, 2017) (Peet, 2017). There is every indication that these library programs are anticipated to be funded in the continuing FY 2018 federal budget.

Everything changes with the FY 2019 federal budget. Even with the possibility that automatic “Pay as You Go” sequestrations kick in for the final FY 2018 budget, there is already talk about Congress waiving the PAYGO sequester this year. However, FY 2019 will be authorized and appropriated under the new federal tax scheme. Programs and priorities in the federal budget will be subject not only to political negotiations, but the size of the budget will also be newly capped due to the significant diminishments in federal tax receipts that come into force under the new tax scheme. There will, simply put, be less money to fund programs and services. Programs and services that may be considered optional or ‘nice but not necessary’ will likely be the first casualties in this new scheme.

Already under the first Trump budget—and nested within the budget priorities of Speaker Ryan and other Congressional leaders—is the elimination of IMLS as a federally funded program. IMLS has had enough political support to be sustained in the current budget. What happens to this program when top-level spending is cut in the near-term? If we are facing a structural shortfall of between \$100 billion and \$150 billion dollars a year for the next ten years, what strategies do library leaders need to pursue now to ensure stable federal funding for libraries?

But a singular focus on IMLS funding does this industry a disservice. Within the 2017 tax bill (and as of this writing the final version has not yet come out of conference committee) there are three high-level, significant tax policy changes which need to be anticipated at the local and state levels. These are a cap on property tax deductions, the elimination of deductions for other state and local sales taxes (SALT), and upcoming cuts to federal grant programs and transfers to states. Each, taken alone, are not direct threats on the library funding formula. I would argue, however, that taken together, their combined impact on taxpayers will significantly alter the local tolerance for taxation across the country. All three of these policy developments directly impact the political climate in which local public library and school funding is decided.

#### When Local Deductions Disappear, Local Taxes Will Feel Higher

One conservative commentator in the *National Review* recently said that deducting “...SALT is the opiate of the overtaxed masses” (Murdock, 2017). State and local taxes, along with property taxes, have been part of the regular deductions on one’s federal tax form since 1913. Multiple generations of tax filers have taken either the standard deduction or itemized their deductions to include SALT and property taxes. Uptake varies for itemized deductions, but between 20% and 30% of all filers use these deductions annually (Government Finance Officers Association, 2017). It is interesting to note that only 15% of filers in recent years itemized a charitable deduction. As of this writing, the House and the Senate versions

both propose nearly doubling the standard, or automatic deduction, while eliminating the itemized deductions.

Nearly 1/5th of filers regularly use itemized SALT and/or property deductions. While those filers may or may not experience an individual tax increase, my concern isn't for them in particular. It is for the local political climate in which new property or sales taxes for libraries must be introduced. In our experience at EveryLibrary, rural libraries and school districts commonly receive political pushback and hear opposition to new property taxes from large property-owning farmers. The argument is often framed as one of equity between landowners and households. While some states are more or less regressive than others around the methodology for assessing value or taxing parcels, the largest landowning stakeholders will be confronted with requests for new library funding at the time when they are adjusting to caps on their ability to deduct the costs of ownership from their own federal taxes (Davis et al., 2015). Likewise, in urban or suburban settings where equalized assessed value (EAV) or another system of determining value is in force, stakeholders with the largest personal or commercial holdings will also be capped.

Capping or eliminating property tax exemptions will create additional negative political pressure on municipal and district libraries, as well as school districts' library programs. The states that have been identified as the most at-risk for disruptions when SALT and property tax deductions are capped or eliminated are those with very robust libraries (Spector, 2017). Several of the states require voter approval for budget and bond changes. Every state in that list of SALT-heavy states has city councils, town boards, and county commissions who are sensitive to local voter and property owners' ability to pay existing local taxes, let alone new ones.

### **When Federal Funding Disappears, States and Localities Will Also Suffer**

Local governments are funded most often by various types of taxes on property. Some local governments also use sales taxes and other fees. State government is funded in a variety of ways, either through taxes on income (personal and corporate), property taxes, or sales taxes, along with excise taxes, fees and licenses, and other charges, depending on the state. Some states do not level income tax. Others collect taxes on natural resource exploitation

in the form of severance. Still others tax 'use' rather than sales for major categories of consumption. But it is easy to forget when comparing state tax schemes that the single largest source of funding by type of revenue for each and every state comes in the form of "transfers" from the federal government.

In 2014, fully 31% of state government budgets were funded by transfers from the federal government (Tax Policy Center, 2017). Sales taxes only accounted for 23% of state revenues. In fact, corporate income taxes were only 2.6% of state revenue nationally. These transfers from the federal to various state governments come in the form of block grants for education and community development, funding for transportation and infrastructure, and health and human services programs, like Medicaid/Medicare, housing, and research. Regardless of projections for individuals or families, the real results of a smaller amount of federal income tax revenue on state government programs across all areas of society will be to shrink programs and services.

We have seen as much in libraries in the past. Even before threatened cuts to IMLS in the 2018 Trump budget, state library agencies (SLA) have faced significant cuts in their state-by-state budget allocations. Federal IMLS funding has been used to the maximum by creative, resourceful, and thoughtful Chief Officers to supplement state funding shortfalls (Institute of Museum and Library Services, 2017). Several SLAs rely on the provision for "maintenance of effort" by state legislatures to leverage federal money. Over time, as state budgets for SLAs were cut, IMLS funding became a larger and larger part of the funding formula. In some cases, as much as 50% of operating revenue for programs administered by a state library comes from IMLS funding (Institute of Museum and Library Services, 2017).

I have previously discussed what the implications would be for state libraries, as well as down-channel impact on local library services, if the Trump cuts were sustained (Chrastka, 2016). What I am extremely concerned about in light of the 2017 tax bill is that the situation of state agencies, relying on federal funding to supplement or underwrite their programs and services, is all too common across every sector of government (The Pew Charitable Trusts, 2014). With the 2017 tax bill, the amount of federal revenue dedicated to state and local government

is about to change drastically. It is not an annual budget adjustment. It is a systemic change to how much money is available to run government. Our state and local governments are not in a position to weather this well. What will happen across state government—and by extension local governments—when the flow of federal funds is so drastically and permanently diminished?

### Yes, New Taxes

Library leaders need to anticipate a major overhaul of each state's tax scheme in response to the 2017 tax bill. Currently, nearly all 41 states with an income tax have 'conformity' with the federal income tax code (Stauffer & Robyn, 2017). Following the 1986 Tax Reform Act, states were faced with needing to evaluate and potentially rework the scope and type of 'linkages' within their state income tax code that corresponded to the federal law. In any significant re-evaluation or re-working of basic revenue schemes, library leaders need to do more than simply monitor the situation. New policy proposals for funding library services need to be innovative and rooted in each state's own tax code.

As states explore their approach to conformity with the federal tax code, library leaders need to actively look for new sources of revenue to fund libraries beyond property or sales taxes. Twenty six states have Republican majorities serving in both houses of their state legislatures alongside Republican governors (Wilson, 2017). Thirty four in total have Republican governors (Leahy, 2017). It is important to recognize that many of the SALT deductions have been in the tax code since 1913. Will states that have Republican majorities have stronger linkages or weaker linkages to the federal code after the Republican-led 2017 reforms? It seems likely to me that the policy priorities of the Heritage Foundation, the American Enterprise Institute, and other anti-tax and anti-government think tanks, that influenced the development of the 2017 federal tax bill, will also influence the development of state tax schemes as well. While each reader could rightly contend that their state tax climate is different than any other, the reality is that a systematic approach by anti-government and anti-tax forces is about to sweep across the tax codes at all levels of government.

I would argue that the most prudent course of action is to engage with the upcoming reforms to state and local tax policy in full force. In general, there are 11 categories of

tax revenue available to states, including: Sales Tax, Taxes on Tobacco and Alcoholic Beverages, Insurance Fees, Fees on Public Utilities, Gaming and Pari-Mutuel, Personal Income Tax, Corporation Income Tax, Motor Fuel Tax, Motor Vehicle Registration Fees, State Property Tax, and Severance (mining, natural resource exploitation) Taxes or Fees (Perez, 2008). As a community, library leaders need to evaluate where new sources of revenue can come from that supplements the current approach to local library funding. Is there a new opportunity in your state within the existing tax for library funding? Whether it is integrating libraries into new or existing 'sin taxes', like gambling or marijuana, or devising entirely new categories of revenue from taxes, fees, or surcharges that include the library, it is incumbent upon us to advance our own policy agenda.

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### About the Author

EveryLibrary's founder is John Chrastka, a long-time library trustee, supporter, and advocate. Mr. Chrastka is a former partner in AssociaDirect, a Chicago-based consultancy focused on supporting associations in membership recruitment, conference, and governance activities. He is a former president and member of the Board of Trustees for the [Berwyn \(IL\) Public Library](#) (2006–2015) and is a former president of the Reaching Across Illinois Libraries System ([RAILS](#)) multi-type library system. Prior to his work at AssociaDirect, he was Director for Membership Development at the American Library Association ([ALA](#)). He is a member of ALA as well as the Illinois Library Association ([ILA](#)), and the American Political Sciences Association ([APSA](#)). He is named a 2014 Mover & Shaker by *Library Journal* and tweets [@mrchrastka](#).