Lincoln Institute
of Land Policy

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TAX BASE SHARING: LOCAL RESPONSE TO FISCAL FEDERALISM

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The Lincoln Institute of Land Policy created the Land Policy Roundtable, composed of informed persons from the academic, business-industrial, and governmental communities to identify major or emerging issues in land policy, to analyze and evaluate their impact, to generate research, discussion, and publication on these topics, to draw them to the attention of policy makers and government officials, and to prepare materials for instructional use.

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I. INTRODUCTION

Most metropolitan areas in the United States are composed of a large number of politically autonomous local governments. These governments rely very heavily on the taxation of real property for the financing of local public services. Although this system of local public finance is deeply rooted in American history, it is increasingly being blamed for generating a number of serious problems. The heavy reliance on the property tax often leads to intense competition among jurisdictions for new tax base. The result of this competition is that fiscal conditions often dictate the pattern of metropolitan area land use and development. New development thus often occurs in areas that are undesirable from the standpoint of the welfare of the entire metropolitan area. The competition among local governments for tax base also provides them with a strong incentive to prohibit any land use that does not generate more local tax revenue than the costs of providing local public services. This practice can motivate local governments to zone out poor families and to oppose any efforts at regional land-use planning.

The heavy reliance on the local property tax also leads to a highly uneven spatial distribution of fiscal resources within most metropolitan areas. This in turn leads to severe fiscal strains on many central cities, which continue to lose both middle and high income residents and businesses to the suburbs. These fiscal problems are exacerbated because the population remaining in the cities includes high concentrations of groups, such as the poor and the aged, that tend to place high demands for public services on the local public sector. This situation, of the uneven spatial distribution of fiscal resources and needs, is often referred to as one of fiscal disparities.

Policy proposals to reform the current system of local public finance have generally taken the form of metropolitan areawide governments or regional provision of selected public services. It is however unclear how effective these regional strategies will be in solving areawide problems, in particular the fiscal problems of central cities. Furthermore, the political opposition to regional governments appears, if anything, harder and harder to overcome.

It is thus not surprising that considerable interest has been shown in a relatively new policy instrument called *tax base sharing*. Tax base sharing provides a mechanism through which the fiscal benefits of growth within a metropolitan area can be shared by all the residents of the area, regardless of where the actual development occurs. Tax base sharing has the important political advantage of not requiring a new level of government, and not destroying the fundamental autonomy of local governments to make their own expenditure and taxing decisions.

The nation's first experience with tax base sharing is in the twin cities (Minneapolis-Saint Paul) metropolitan area of Minnesota. In 1971 the Minnesota State Legislature enacted the Metropolitan Fiscal Disparities Act (Minn. Statutes, Ch. 273F) that established a tax base sharing plan for the seven-county metropolitan area. Under the legislation all jurisdictions within the area share 40% of the areawide growth of commercial–industrial tax base.

II. THE MINNESOTA STATUTE

The Minnesota Fiscal Disparities Act was passed only after stormy debate; indeed, by the margin of one vote. Of the 31 senators who voted against the bill,

twelve were from the seven-county area covered by the Act and 19 were from outstate Minnesota. Passed in 1971, the Act did not go into operation until the end of 1975, having been held up by litigation. While it was greeted with national acclaim as a breakthrough in dealing with metropolitan problems, to be fully appreciated, one must consider its origins.

A. Background: Why Base Sharing?

It is important to keep in mind, also, that, increasingly, over the past decade major commercial and industrial complexes have been concentrated in a few large areas, rather than being spread throughout the Twin Cities area. The sites for our major regional shopping centers are clearly identified already and are limited to a few largely prosperous suburbs. The same is true of our largest industrial parks. What really is happening to our Twin Cities area, therefore, is that very few of our municipalities are "balanced" in the sense that within the borders of a community there will be a wide variety of housing types as well as commercial and industrial areas.

REGIONAL AWARENESS

We have had a long history of awareness of regional problems and of the necessity to apply regional solutions to these problems. Although it may sound paradoxical, we have, at the same time, jealously protected the rights of our many local villages and cities. We have tended to regard as regional problems only those which cannot be handled adequately at the municipal level.

At the same time we in the Legislature have fully realized that the decisions on freeways, transit lines, airports, residential, commerical, and industrial development, and on open space, have a major effect on the local property tax base of the various governments in our area. For example, in the early 1960's a large power plant was built along the beautiful St. Croix River in the legislative district represented by Rep. Howard Albertson, who is chairman of our House Metropolitan and Urban Affairs Committee. Many critics of the power plant decision have argued that the St. Croix valley should have been kept in its natural state. Albertson frankly admits that the prospect of a substanital addition to the property tax base was a major factor in his support of the power plant. He has responded to his critics by saying: "If we are to provide open space for the rest of the metropolitan area, then we ought to receive some of the tax benefit from industry which locates elsewhere in the area."

If certain land is best suited for open space, from an areawide standpoint, should the local government or governments affected suffer all the loss of tax base as a result? Or, if it is determined that an airport should be located in one part of the area, should only the communities in the immediate vicinity reap the benefit from the industrial and commercial growth which will accompany such an airport?

HOW THE IDEA EMERGED

During the early part of 1968 Warren Preeshl, a member of the Citizens League's Fiscal Disparities Committee, had spent every Thursday night participating in discussions of the fiscal problems of local government in the metropolitan area. Preeshl, a municipal bond dealer, who also was serving on a suburban school board, had a long, intimate relationship with local government fiscal problems. As a member of the Citizens League committee he listened patiently to builders, public officials, fiscal experts, planners, economists, and others describe repeatedly the difficulties with the local property tax. What these people were saying went beyond the more common complaints about the tax, such as its failure to relate adequately to ability to pay and the poor administration of the property tax. What kept recurring was a somewhat different theme: The property tax was interfering with the way local officials wanted their communities to grow.

No, interfering is not an adequate word to describe the situation. *The property tax was dictating their urban growth decisions.* Put another way, they were captives of the property tax.

Preeshl had heard how suburban communities were ringing the central cities of Minneapolis and St. Paul with restrictive residential zoning ordinances and building codes designed specifically to keep out low-income families who live in dwellings that don't "pay their own way" in property taxes. He heard how one community, desperate for local property tax base, agreed to allow two big ugly billboards at a cloverleaf as the price to get a business located within its village limits. He heard of another community, possessing a beautiful potential park area along the Minnesota River, giving in to pressure for industrial development rather than keep the land in its natural state. And another community that used its political influence to get a new interchange on an interstate highway only 800 feet from another interchange already built, simply to improve access for a potential industrial area, thereby building its local tax base.

He heard the superintendent of the school district with the highest tax rate in the Twin Cities area, a suburban district almost 100% lower-income residential, begging for industrial tax base but knowing that the hope was largely futile because few industries would ever consider locating there, given the high tax rate. Later in the committee discussions he heard about various parts of the Twin Cities area fighting for the location of a new airport, expecting tax bonanzas as a result.

Through all this discussion, Preeshl learned—if he didn't know already as a local government official—that no local government really wants to take actions that are against the benefit of the entire area. But, given the rules of the game—winner take all—they *simply have no choice*. After one of these Citizens League committee meetings in mid-summer 1968, Preeshl sat down and wrote a memorandum—a memorandum which later turned out to be the proposal which we have put into bill form. He shoved the memo in his desk and didn't tell anyone about it for almost six months. Then, early in December the Citizens League committee was debating many options. Someone suggested that you could abolish all, or a substantial portion, of the property tax and use some other form of taxation as a replacement. Someone else suggested the establishment of a metropolitan property taxing district, with distribution of the revenue back to local government. Another idea was to impose a new non-property tax to keep the property tax from expanding further, and hopefully to reduce it.

Preeshl, a believer in strong local government and in keeping decisions about tax rates as close to the people as possible, was disturbed about the thrust of these other suggestions. Someone else, it appeared, not local government, would be setting a tax rate and then determining how the revenue would be distributed back to the various units of government. It appeared as if you would have to turn to some kind of metropolitan government for implementation. Moreover, you would have to pick and choose among the various overlapping units of government, school districts, municipalities, counties, etc.—and we have plenty of them in the Twin Cities area, more than 300.

Charles Weaver, "Breaking the Tyranny of the Local Property Tax," NTA Proceedings, 1970, pp. 209-212.

B. Formulation: Implementing an Innovation.

CHAPTER 473F. METROPOLITAN REVENUE DISTRIBUTION (NEW)

Sec.		Sec.	
473F.01	Purpose.	473F.08	Taxable value.
473F.02	Definitions.	473F.09	Adjustments in dates.
473F.03	Administrative auditor.	473F.10	Reassessments and omitted property.
473F.04	Assessed valuation: 1971.		

473F.05 Assessed valuation: 1972 and subsequent years.
473F.06 Increase in assessed valuation.
473F.07 Computation of area-wide tax base.
473F.11 Late levies.
473F.12 Distributions from municipal equity account.
473F.13 Change in status of municipality.

473F.01 Purpose

The legislature finds it desirable to improve the revenue raising and distribution system in the seven county Twin Cities area to accomplish the following objectives:

(1) To provide a way for local governments to share in the resources generated by the growth of the area, without removing any resources which local governments already have:

(2) To increase the likelihood of orderly urban development by reducing the impact of fiscal considerations on the location of business and residential growth and of highways, transit facilities and airports:

(3) To establish incentives for all parts of the area to work for the growth of the area as a whole:

(4) To provide a way whereby the area's resources can be made available within and through the existing system of local governments and local decision making;

(5) To help communities in different stages of development by making resources increasingly available to communities at those early stages of development and redevelopment when financial pressures on them are the greatest;

Subd. 14. "Fiscal capacity" of a municipality means its valuation, determined as of January 2 of any year, divided by its population, determined as of a date in the same year.

Subd. 15. "Average fiscal capacity" of municipalities means the sum of the valuations of all municipalities, determined as of January 2 of any year, divided by the sum of their populations, determined as of a date in the same year.

473F.04 Assessed valuation: 1971

On or before November 20, 1972, the assessors within each county in the area shall determine and certify to the county auditor the assessed valuation in 1971 of commercial-industrial property subject to taxation within each municipality in his county.

Laws 1971, Ex.Sess., c.24, § 4, eff. July 24, 1971.

473F.05 Assessed valuation: 1972 and subsequent years

On or before November 20 of 1972 and each subsequent year, the assessors within each county in the area shall determine and certify to the county auditor the assessed valuation in that year of commercial-industrial property subject to taxation within each municipality in his county.

Laws 1971, Ex.Sess., c.24, § 5, eff. July 24, 1971.

473F.06 Increase in assessed valuation

On or before September 1 of 1976 and each subsequent year, the auditor of each county in the area shall determine the amount, if any, by which the assessed valuation determined in the preceding year pursuant to section 473F.05, of commercial-industrial property subject to taxation within each municipality in his county exceeds the assessed valuation in 1971 of commercial-industrial property subject to taxation within that municipality.

473F.07 Computation of area-wide tax base

Subdivision 1. Each county auditor shall certify the determinations pursuant to sections 473F.04, 473F.05, and 473F.06 to the administrative auditor on or before November 20 of each year. The administrative auditor shall determine the sum of the amounts certified pursuant to section 473F.06, and divide that sum by two and one half. The resulting amount shall be known as the "area-wide tax base for .... (year)."

Subd. 2. The commissioner of revenue shall certify to the administrative auditor, on or before November 20 of each year, the population of each municipality for the preceding year, the proportion of that population which resides within the area, the average fiscal capacity of municipalities for the preceding year, and the fiscal capacity of each municipality for the preceding year.

Subd. 3. The administrative auditor shall determine, for each municipality, the product of (a) its population, (b) the proportion which the average fiscal capacity of municipalities for the preceding year bears to the fiscal capacity of that municipality for the preceding year, and (c) two. The product shall be the area-wide tax base distribution index for that municipality, provided that (a) if the product in the case of any municipality is less than its population, its index shall be increased to its populaiton, and (b) if a municipality is located partly within and partly without the area its index shall be that which is otherwise determined hereunder, multiplied by the proportion which its population residing within the area bears to its total population as of the preceding year.

Subd. 4. The administrative auditor shall determine the proportion which the index of each municipality bears to the sum of the indices of all municipalities. In the case of each municipality, he shall then multiply this proportion by the area-wide tax base.

Subd. 5. The product of the multiplication prescribed by subdivision 4 shall be known as the "area-wide tax base for ...... (year) attributable to ....(municipality)." The administrative auditor shall certify such product to the auditor of the county in which the municipality is located on or before November 25.

Laws 1971, Ex.Sess., c. 24, § 7, eff. July 24, 1971. Amended by Laws 1973, c. 492, § 14: Laws 1976, c. 191, § 5; Laws 1976, c. 231, §§ 31, 32, eff. April 10, 1976.

Laws 1976, c. 191, § 15, provides that "this act is effective for taxes levied in 1976 and payable in 1977 and all subsequent years."

473F.08 Taxable value

Subdivision 1. The county auditor shall determine the taxable value of each governmental unit within his county in the manner prescribed by this section.

Subd. 2. The taxable value of a governmental unit is its assessed valuation, as determined in accordance with other provisions of law, subject to the following adjustments:

(a) There shall be subtracted from its assessed valuation, in each municipality in which the governmental unit exercises ad valorem taxing jurisdiction, an amount which bears the same proportion to 40 percent of the amount certified in that year pursuant to section 473F.06 in respect to that municipality as the total preceding year's assessed valuation of commercial-industrial property which is subject to the taxing jurisdiction of the governmental unit within the municipality bears to the total preceding year's assessed valuation of commercial-industrial property within the municipality.

(b) There shall be added to its assessed valuation, in each municipality in which the governmental unit exercises ad valorem taxing jurisdiction, an amount which bears the same proportion to the area-wide base for the year attributable to that municipality as the total preceding year's assessed valuation of residential property which is subject to the taxing jurisdiction of the governmental unit within the municipality bears to the total preceding year's assessed valuation of residential property of the municipality.

Subd. 3. On or before October 15 of 1976 and each subsequent year, the county auditor shall apportion the levy of each governmental unit in his county in the manner prescribed by this subdivision. He shall:

(a) Determine the area-wide portion of the levy for each governmental unit by multiplying the nonagricultural mill rate of the governmental unit for

the preceding levy year times the distribution value set forth in section 473F.08, subdivision 2, clause (b): and

(b) Determine the local portion of the current year's levy by subtracting the resulting amount from clause (a) from the governmental unit's current year's total levy.

Subd. 4. In 1972 and subsequent years, the county auditor shall divide that portion of the levy determined pursuant to subdivision 3, clause (b), by the assessed valuation of the governmental unit, less that portion subtracted from assessed valuation pursuant to subdivision 2, clause (a). The resulting rate shall apply to all taxable property except commercial-industrial property, which shall be taxed in accordance with subdivision 6.

Subd. 5. On or before November 30 of 1972 and each subsequent year, the county auditor shall certify to the administrative auditor that portion of the levy of each governmental unit determined pursuant to subdivision 3, clause (a). The administrative auditor shall then determine the rate of taxation sufficient to yield an amount equal to the sum of such levies from the area-wide tax base. On or before December 5 the administrative auditor shall certify said rate to each of the county auditors.

Subd. 5a. If a governmental unit is located in two or more counties, the computations and certifications required by subdivisions 3 to 5 with respect to it shall be made by the county auditor who is responsible under other provisions of law for allocating its levies between or among the affected counties.

Subd. 6. The rate of taxation determined in accordance with subdivision 5 shall apply in the taxation of each item of commercial-industrial property subject to taxation within a municipality to that portion of the assessed valuation of the item which bears the same proportion to its total assessed valuation as 40 percent of the amount determined pursuant to section 473F.06 in respect to the municipality in which the property is taxable bears to the amount determined pursuant to section 473F.05. The rate of taxation determined in accordance with subdivision 4 shall apply in the taxation of the remainder of the assessed valuation of the item.

In effect, the statute transfers tax base from one jurisdiction to another. How will a community experiencing rapid commercial/industrial (C/I) growth fare, compared to a largely residential community? A large community with a relatively stable C/I base? What is the measure of value which is shared?

How will assessment practices affect the workings of the statute? Minnesota law requires that property be assessed at market value. (M.R.S., ch. 273.11). Although, in general the quality of real estate assessment in Minnesota is quite high, here as elsewhere it is exceedingly difficult to accurately and consistently assess the market value of business property. Can local assessors thwart the purpose of the statute by undervaluing C/I properties? Do they have a motivation to do so? If so, will this allow competition for development to persist? Is reform of assessment practices a prerequisite to base sharing? Note that the formula for fiscal capacity uses market value.

Under the scheme, a local government's property tax revenue comes from two sources. The amount of revenue a locality wishes to raise—its total levy—is divided by its net base (the local base, decreased by its contribution to, and increased by its distribution from, the areawide base) to determine the local rate. The local portion of the total levy is computed by multiplying the local rate by the local base; this portion is generated directly. The total levy less the local levy is the areawide portion; the areawide levies of all municipalities are aggregated and divided by the areawide base to yield the areawide rate. Commercial-Industrial property is subject to both the local and areawide rates—the areawide rate is applied to that portion of the value of a given parcel which bears the same

proportion to the value of the property as 40% bears to the total assessed value of commercial-industrial property in the municipality. Each municipality's areawide levy is met from these revenues. The local rate is applied to the remaining portion of each C/I parcel.

Does the definition section of governmental units raise special problems with respect to determining both the contribution to and the distribution from the areawide tax base?

> Governmental units other than municipalities determine both their contribution to and their share of the area-wide tax base on the basis of the municipalities wholly or partly within their boundaries.[91] When the boundaries of a governmental unit do not coincide with municipal lines, the unit may be either the beneficiary or the victim of the uneven distribution of residential and commercial-industrial property in the divided municipality. For example, if a municipality is located within two governmental units so that one of the units possesses a large percentage of the residential valuation of the municipality while the other unit has a large percentage of the municipality's commercial-industrial valuation, the former unit will contribute little to the area-wide tax base but will receive a large share in the population-based distribution. For similar reasons, the latter unit will "lose" in the distribution. If the governmental unit in which the residential area is located also has a high fiscal capacity relative to the other unit, such a result would be contrary to the statute's intent. This effect will be significant, however, only when the governmental units cover a relatively small area; over large areas such uneven distributions should tend to balance out.
>
> Robert Freilich, "Minnesota's Fiscal Disparities Act...," 59 Minnesota Law Review 927, 950.

Are there any special provisions for the transition period? As a legislator contemplating the introduction of an Act similar to the Minnesota statute, how would you deal with the question that even if the benefits received by the residents of the area are equalized, inequities may nevertheless arise during the period in which the act is being implemented, due to capitalization of tax rates into property values? See Wallace Oates, "The Effects of Property Taxes and Local Public Spending on Property Values," 77 *Journal of Political Economy* 957, 958-959, 1969.

The following is an illustration of the mechanics of the Minnesota statute.

ILLUSTRATION OF THE WORKINGS OF THE FISCAL DISPARITIES ACT

Consider a metropolitan area in which three municipalities, A, B, and C, comprise a county, W. For purposes of this illustration, these four entities will be assumed to constitute the only existing governmental units. A is a central city beset with urban problems, B is a highly developed inner ring suburb, and C is a developing outer ring suburb.* The following data is postulated:**

		A	B	C	W
Population	1971	50,000	20,000	5,000	75,000
	1972	49,000	20,000	6,000	75,000
Valuation***	1971	$400	$140	$60	$600
Assessed valuation	1972	$105	$50	$20	$175
C-I assessed valn.	1971	$23.0	$4.9	$3.0	
C-I assessed valn.	1972	$23.5	$5.0	$3.5	
C-I growth		$ .5	$ .1	$ .5	
40% C-I growth		$ .2	$ .04	$ .2	

The effect of the Fiscal Disparities Act on the metropolitan area can be studied through the use of this data.

1. Calculation of fiscal capacity and area-wide tax base:****

Fiscal capacity for 1971 (f.c. = valn./pop.) (§473F.02(14))

for A = $400/50,000 = 8,000
for B = $140/20,000 = 7,000
for C = $60/5,000 = 12,000

Average fiscal capacity for 1971 (§473F.02(15))

($400 + $140 + $60) / (50,000 + 20,000 + 5,000) = 8,000

Area-wide tax base (§473F.07 (1))

$.2 + $.04 + $.2 = $.44

2. Determination of a municipality's distribution from the area-wide tax base:

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The area-wide tax base distribution index (pop. × ((avg. f.c. 1971) / (f.c. 1971)) × 2) (§473F.07 (3))

for A = 49,000 × (8,000 / 8,000) × 2 = 98,000
for B = 20,000 × (8,000 / 7,000) × 2 = 45,714
for C = 6,000 × (8,000 / 12,000) × 2 = 8,000

The sum of these indices = 98,000 + 45,714 + 8,000 = 151,714

The area-wide tax base for 1972 (((index) / (indices)) × (area-wide tax base)) attributable (§473F.07(4), (5))

to A = (98,000 / 151,714) × $.44 = $.2842
to B = (45,714 / 151,714) × $.44 = $.1326
to C = (8,000 / 151,714) × $.44 = $.0232

Therefore:

	Assessed Valuation		
	Contribution	Distribution	Net
A	$.2000	$.2842	$.0842
B	$.0400	$.1326	$.0926
C	$.2000	$.0232	− $.1768

C is a net loser to the area-wide tax base while A and B gain on balance.

3. Calculation of taxable value for each governmental unit:

((assessed valn.) — (contribution to area-wide tax base) + (distribution therefrom))

for A	for B	for C	
$105.0000	$50.0000	$20.0000	(§473F.08(2))
− .2000	− .0400	− .2000	(§473F.08(2)(a))
+ .2842	+ .1326	+ .0232	(§473F.08(2)(b))
$105.0842	$50.0926	$19.8232	

for W

$175.0000 (§473F.08(2))
−((.2 + .04 + .2) = .44) (§473F.08(2)(a))
+((.2842 + .1326 + .0232) = .44) (§473F.08(2)(b))
$175.0000

4. Determination of levy:

After the taxable value for their governmental unit has been calculated, officials can decide upon the amount they wish to levy. Suppose A decides on a levy of $12.6, B $2.25, C $.7, and W $17.5. These are total levies, which must be apportioned among the local and area-wide tax bases.

The taxable resources available to each unit (local tax base + area-wide share)

A = $104.8000 + $.2842 = $105.0842
B = $49.9600 + $.1326 = $50.0926
C = $19.8000 + $.0232 = $19.8232
W = $174.5600 + $.4400 = $175.0000

Unit's area-wide levy (((area-wide share) / (taxable value)) × (total levy))
(§473F.08.(3)(a))
Unit's local levy ((total levy) − (area-wide levy)) (§473F.08(3)(b))
for A area-wide levy = (.2842/105.0842) × 12.6 = $.03408
local levy = 12.6 − .03408 = $12.56592
for B area-wide levy = (.1326/50.0926) × 2.25 = $.00596
local levy = 2.25 − .00596 = .$2.24404

for C area-wide levy = (.0232/19.8232) × .7 = $.00082
local levy = .7 − .00082 = $.69918
for W area-wide levy = (.4400/175.0000) × 17.5 = $.04400
local levy = 17.5 − .04400 = $17.45600

5. Calculation of tax rates:

The local tax rate ((unit's local levy)/(unit's local tax base))
(§473F.08(4))

with respect to municipalities
for A = (12.56592) / (104.8000) = .11990 = 119.90 mills
for B = (2.24404) / (49.9600) = .04492 = 44.92 mills
for C = (.69918) / (19.8000) = .03531 = 35.31 mills
with respect to the county
W = (17.45600) / (174.5600) = .10000 = 100.00 mills

The local tax rate is the tax levied on all taxable property except commercial-industrial property. Thus, for noncommercial-industrial property, the tax rate is
in A 119.90 + 100.00 = 219.90 mills
in B 44.92 + 100.00 = 144.92 mills
in C 35.31 + 100.00 = 135.31 mills

The area-wide tax rate (§473F.08(5))
The area-wide levy = $.03408 + $.00596 + $.00082 + $.04400 = $.08486
The area-wide tax rate ((area-wide levy) / (area-wide tax base))
= (.08486)/(.44)
= .19286 = 192.86 mills

The tax rate on commercial-industry property (((40% C-I growth) / (C-I assessed valn. 1972)) × area-wide tax rate) + (((C-I assessed valn. 1972—40% C-I growth)/C-I assessed valn. 1972)) × local tax rate)
(§473F.08(6))
in A = ((.2/23.5) × 192.86) + ((23.3/23.5) × 219.90) = 219.67 mills
in B = ((.04/5) × 192.86) + ((4.96/5) × 144.92) = 145.30 mills
in C = ((.2/3.5) × 192.86) + ((3.3/3.5) × 135.31) = 138.60 mills

Prior to the passage of the Fiscal Disparities Act, tax rates would have been (unit's tax rate = unit's levy/unit's assessed valn.)

	municipal		county			
in A =	(12.6/105)	+ (17.5/175) =	.12000	+ .10000	=	220.00 mills
in B =	(2.25/50)	+ (17.5/175) =	.04500	+ .10000	=	145.00 mills
in C =	(.7/20)	+ (17.5/175) =	.03500	+ .10000	=	135.00 mills

on both commercial-industrial and other property.

59 Minnesota Law Review 927, 961-963.

C. Challenge: Constitutionality of the Statute

Almost immediately after the statute was passed, it was challenged by the city of Burnsville as violating the Minnesota Constitution's uniformity clause, which reads: "Taxes shall be uniform upon the same class of subjects, and shall be levied and collected for public purposes." Minn. Const., Art.9, § 1. After the District Court held the statute unconstitutional, the Supreme Court reversed.

VILLAGE OF BURNSVILLE V. ONISHUK, 301 Minn 137, 222 N.W. 2d 523 (1974).

2. Plaintiffs stress the language in Maltby and other cases which define uniformity in terms of a "special interest" to be enjoyed by those on whom the tax burden falls. The attack on c.24 is based on the premise that taxes can only be levied to pay for debts incurred by the taxing district having the responsibility for providing goods and services to those who bear the tax. Here, it is argued, the district simply acts as a conduit for its constituent systems of government to redistribute revenues among those units which have the burden of providing services. Plaintiffs point out that the act specifies no new responsibilities for the metropolitan area to assume. They cite a rule adopted as early as 1864 in Sanborn v. Commrs. of Rice County, 9 Minn. 273, 278 (Gil. 258, 262), where we said:

". . . [A] tax cannot be imposed exclusively on any subdivision of the state, to pay an indebtedness or claim which is not peculiarly the debt of such subdivision or to raise money for any purpose not peculiarly for the benefit of such subdivision."

In essence, the issue then is whether those units of government within the metropolitan area which in a given year contribute more of their tax base to the pool than is redistributed to them are sufficiently benefited to meet the constitutional requirement of uniformity. A number of Minnesota cases are cited by both parties for support of their positions. A brief discussion of them is in order. The Maltby case which we have quoted involved the construction by the county of a road and approach to a bridge in Burnsville, the expense of which under the statute was to be borne by adjacent communities in proportion to the benefits each realized from the project. We sustained the validity of the statutory authority for assessing individual units of government, notwithstanding the fact that the improvement was located in only one of them. The test of uniformity there applied was the particular unit's interest in the improvement, rather than the location of the improvement.

3. Two of our decisions have held that the uniformity clause applies to distribution of revenue as well as to the levy of taxes. State and City of New Prague v. County of Scott, 195 Minn. 111, 261 N.W. 863 (1935); Village of Robbinsdale v. County of Hennepin, 199 Minn. 203, 271 N.W. 491 (1937). We are invited by defendants to reconsider and overrule those cases to the extent they held that uniformity in distribution is required.

Robbinsdale held unconstitutional a statute which permitted municipalities other than cities of the first and second class to recover from Hennepin County 75 percent of what the municipality spent for poor relief in excess of a 1-mill tax on municipal property. The city of Minneapolis paid 92 percent of the taxes levied by the county, but was excluded from participating in the reimbursement. Robbinsdale argued that since the levy was uniform, Minn. Const. art. 9, § 1, was satisfied notwithstanding the distribution was not uniform. This distinction we rejected, citing New Prague. We concluded by saying (199 Minn. 207, 271 N.W. 493):

". . . It is settled law in this state that where it clearly appears that the tax imposed in no way pertains to the district taxed and that it was imposed and apportioned without any reference whatsoever to any special interest on the part of such district in the purpose to be accomplished, the tax so imposed is unconstitutional as in violation of the uniformity clause."

Subsequently, in City of Jackson v. County of Jackson, 214 Minn. 244, 7 N.W.2d 753 (1943), we said that the purpose of a tax must pertain to the district taxed, that poor relief was not the obligation or concern of the county, and that to reimburse from county funds municipalities providing poor relief did not pertain to any purpose of the county, which was the district taxed. In other words, county funds could not be used to pay obligations imposed by law on its political subdivisions without violating the

uniformity clause.

[5] 4. Plaintiffs argue with considerable force that these cases preclude the metropolitan area from disbursing area-wide tax revenues to individual municipalities. We agree that a literal reading of our prior opinions supports plaintiffs' position. Our decision to reverse therefore hinges on what we deem to be a developing concept of the meaning of the word "benefit." It seems to us that the phrase "special benefit" no longer adequately serves the constitutional requirement of uniformity. In a seven-county area which is heavily populated, we are of the opinion that it is no longer necessary for units of government providing tax revenue to receive the kind of tangible and specific benefits to which our court has previously referred in order to satisfy the uniformity clause. We moved away from the strict application of the "special benefits" rule in Visina v. Freeman, 252 Minn. 177, 195, 89 N.W.2d 635, 650 (1958). There, we sustained a statutory scheme which imposed taxes in varying amounts on separate units of government which received in different degrees general benefits from the establishment of the Port Authority of Duluth. We there said (252 Minn. 193, 89 N.W.2d 648):

"While the plain meaning of language used in our fundamental law may not be tampered with to accomplish a desired result no matter how archaic it has become by virtue of social and economic changes which have occurred since its adoption, neither should the proper interpretation of constitutional provisions ignore such changes. In determining whether an act of the legislature contravenes a constitutional provision we should endeavor to interpret the provision in the light of existing conditions, particularly when those conditions could not have been foreseen at the time the constitution was adopted."

In disposing of the contention that the Port Authority Act was in violation of Minn. Const. art. 9, § 1, we observed that absolute equality of taxation has never been required or attained; that there are always those who must pay taxes from which they derive no *direct* benefit; and that the legislature may constitutionally apportion taxes among those who bear the financial burden if they have a reasonable relationship to the benefits to be derived.

5. Without unduly protracting this opinion, it is appropriate to comment on San Antonio School District v. Rodriguez, 411 U.S. 1, 93 S.Ct. 1278, 36 L.Ed.2d 16 (1973).

" 'The broad discretion as to classification possessed by a legislature in the field of taxation has long been recognized . . . [T]he passage of time has only served to underscore the wisdom of that recognition of the large area of discretion which is needed by a legislature in formulating sound tax policies. . . . It has . . . been pointed out that in taxation, even more than in other fields, legislatures possess the greatest freedom in classification. Since the members of a legislature necessarily enjoy a familiarity with local conditions which this Court cannot have, the presumption of constitutionality can be overcome only by the most explicit demonstration that a classification is a hostile and oppressive discrimination against particular persons and classes . .' Madden v. Kentucky, 309 U.S. 83, 87-88 [60 S.Ct. 406, 408, 84 L.Ed. 590, 593] (1940)."

The court went on to say (411 U.S. 41, 83 S.Ct. 1301, 36 L.Ed.2d 48):

". . . No scheme of taxation, whether the tax is imposed on property, income, or purchases of goods and services, has yet been devised which is free of all discriminatory impact. In such a complex arena in which no perfect alternatives exist, the Court does well not to impose too rigorous a standard of scrutiny lest all local fiscal schemes become subjects of criticism under the Equal Protection Clause."

Finally, in upholding the reliance of Texas school authorities on local property taxes to finance the system, the United States Supreme Court encouraged "innovative new thinking" in school funding but left the

ultimate solution to lawmakers and "the democratic pressures of those who elect them." 411 U.S. 58, 59, 93 S.Ct. 1310, 36 L.Ed.2d 58.

The broad principles in the Rodriguez decision to which we have alluded are pertinent to the resolution of the fiscal disparities problems to which the Minnesota legislature addressed itself in adopting c. 24. The fiscal disparities statute is a bold and imaginative departure from conventional devices for balancing the benefits and burdens of taxation. As we have suggested, we are quick to concede that a strict application of our prior decisions would require us to lean strongly for affirmance. The trial court cannot be faulted for reading those decisions as it did. Nevertheless, we are today dealing with a viable, fluid, transient society where traditional concepts of what confers a tax benefit may be too parochial.

We find the arguments of defendants persuasive. Under existing tax practices, in order to improve their fiscal capacity, local units of government vie for commerce and industry to improve the fiscal capacity of its residents without considering the resulting impact on long-range planning and the utilization of their resources. The seven-county metropolitan area, it is pointed out, has a high degree of mobility and political, social, and economic interdependence. There is an increasing use of facilities in one municipality by those who reside or work in a different municipality. The payment of taxes in a metropolitan area may have only slight relationship to the use and enjoyment which residents make of other areas in the district. Defendants argue effectively that the indiscriminate encouragement of commerce and industry in a particular municipality may detrimentally and irretrievably affect policies and plans for the development of parks and open spaces and frustrate well-considered housing policies for both low-income and moderate-income residences. The Fiscal Disparities Act recognizes that to some extent the location of commercial-industrial development may be irrelevant to the question of the cost of services which are added to a municipality's budget occasioned by the location of such a development within its boundaries. It should be borne in mind that all commercial-industrial property except 40 percent of its increment since January 1971 remains in the tax base for the municipality where it is located.

In other words, in terms of traditional balancing of benefits and burdens, the benefits conferred on residents of a particular municipality because of the location of commercial-industrial development within its boundaries may far exceed the burdens imposed on that municipality by virtue of the additional cost of servicing and policing the particular development which has located there. It is the theory of the Fiscal Disparities Act that the residents of highly developed commercial-industrial areas *do* enjoy direct benefits from the existence of adjacent municipalities which provide open spaces, lakes, parks, golf courses, zoos, fair-grounds, low-density housing areas, churches, schools, and hospitals.

[6] We have concluded that the statutory scheme for revenue sharing embodied in c. 24 reaches a constitutional accommodation between the tax burdens imposed and the benefits derived therefrom to a degree which satisfies the requirements of the uniformity provisions of Minn. Const. art. 9, § 1.

Once the special benefit requirement is relaxed, what limitations are still imposed on base sharing by the uniformity clause? If the benefit requirement is met as the court claims by the interdependence of governmental units, what degree of interdependence is required? How is that interdependence to be measured?

D. Exploration: The Elements of a Base-Sharing Scheme

The Minnesota Statute was designed with a particular problem in mind —reducing the role played by the property tax in land use decisions. Several

other states have begun to consider similar legislation, to carry out various objectives. Consider the following elements of a base sharing scheme as they relate to both the economic dynamics and the political realities constraining local governments in metropolitan areas.

1. Growth

Given the context in which the Minnesota statute was passed—competition for commercial-industrial development—it is not surprising that only increments to the tax base are shared. It is fully consistent with the purpose of reducing this competition that the growth in C/I valuation, particularly new plants, industrial parks, shopping centers and the like, is shared.

If the scheme is credited with a broader purpose, that of reducing fiscal disparities, it need not be limited to growth. Provision could be made to share existing tax base. Yet if this is the objective, the extent to which sharing increments to the base will reduce disparities depends on the rate of growth in the area. A robust regional economy will experience far more redistribution than a stagnant one. Finally, poorer jurisdictions experiencing rapid growth may, depending on the distribution formula, be net contributors, despite a low per capita base. What possibilities are there for sharing existing base? This would, of course, result in an absolute reduction in the base of the more wealthy jurisdictions, something not required by sharing growth. Would this impair chances for passage of the legislation? What would sharing existing base imply for the central cities of most metropolitan areas?

2. Types of Valuation Shared

The Minnesota scheme shares only growth in commercial-industrial valuation. Why isn't residential growth shared? A proposal being considered in Alberta, Canada, designed to distribute the benefits of investment in natural resource extraction industries, excludes not only growth in residential and farm valuation, but also increases in land assessment, and the value of public utility distribution lines from the shared base. See Alberta Provincial-Municipal Finance Council, *Proposal For Property Tax Growth Sharing,* December, 1976. The New Jersey statute, discussed below, is part of a regional development plan and covers all types of property except railroads. If the purpose of a base-sharing scheme is to reduce disparities, what types of property should be subject to base sharing? What assumptions are made about the source of those disparities? How important are political factors in deciding whether residential property should be included?

3. Percent of Growth Shared

From the perspective of intergovernmental competition, what proportion of growth should be shared? The various proposals select an apparently arbitrary figure—40% in Minnesota, 50% in Alberta, 60% in Maryland. Do these figures reflect an attempt to reach a proper distribution of the tax base or are they merely an acceptable political solution? What things should be taken into account in establishing this figure? How does the percentage shared affect land use decisions?

4. Distribution Formula

Under the Minnesota Act, a municipality's area-wide tax base distribution index is proportional to its population and inversely proportional to its fiscal capacity, unless the municipality's fiscal capacity exceeds twice the average fiscal capacity of the area, in which case its distribution index equals its population.

84. A municipality's area-wide tax base distribution index is equal to the product of its population, the average fiscal capacity for the area divided by the municipality's fiscal capacity, and two:

$$\text{Pop.} \times ((\text{avg. f.c.}) / (\text{f.c.})) \times 2$$

MINN. STAT. § 473F.07(3) (1974). Since the average fiscal capacity, *id.* § 473F.02(15), is a constant for each municipality, if K is designated as 2 × (avg. f.c.), a municipality's share of the area-wide tax base equals:

$$\text{Pop.} \times ((\text{avg. f.c.}) / (\text{f.c.})) \times 2 = K \times ((\text{pop}) / (\text{f.c.})).$$

85. The formula used in the calculation of a municipality's area-wide tax distribution index does not take account of the amount by which a municipality's fiscal capacity exceeds twice the average fiscal capacity; the possibility exists, therefore, that a particular municipality could receive an unneeded additional amount of the area-wide tax base. This situation arises because of the presence of the numeral two as a factor in the formula and because the index is not allowed to be less than a municipality's population. *Id.* § 473F.07 (3).

59 Minn. Law Rev. 927, 948.

What effect will this have on fiscal disparities? What exactly does the concept of fiscal disparities mean? The tax base distribution formula distributes tax base on the basis of communities' fiscal capacity. What is the relationship between fiscal disparities and fiscal capacity? In the Minnesota legislation fiscal capacity is defined as the per capita market value of real property. What would be the effect on the distribution of tax base if the legislation defined fiscal capacity as per capita personal income? Should the distribution formula use a broader definition of fiscal capacity or fiscal disparities—one that includes other sources of local resources such as intergovernmental grants-in-aid? Fiscal disparities are also caused by the unequal spatial distribution of fiscal needs, particularly those created by concentrations of certain population groups that appear to require above-average levels of public services, and hence greater public expenditures. How should one measure these fiscal needs in the context of a tax base sharing distribution formula?

How could the distribution formula affect land use decisions? To the extent that municipalities attempt to zone out high-expenditure populations for fiscal reasons, could the distribution formula be used to alter the fiscal calculus and open the suburbs to low income housing? What about open space? As you read the materials on the New Jersey statute, observe how the distribution formula used there is designed to realize the statute's purposes.

5. The Size of the Region

How large an area should be included in a base-sharing plan? Does this depend on the purpose of the particular proposal? If the objective is to reduce competition for C/I development, the region should be defined in terms of the market for C/I development; as the area grows, the boundary may need to be expanded. For some activities, there is an economic basis for defining the relevant area. The increment from a power plant, the output of which is consumed within the metropolitan area, should be shared with the entire area. The increment from a shopping center, serving only a portion of the region, should be shared only with that portion. This approach presents two problems: first, it goes too far. It suggests, for example, that the increment from a manufacturing plant with a national market should be shared nationally. Secondly, it would be impossible to administer this approach. Nevertheless, what does it suggest about strictly local development? Should a corner grocery store, for example, be excluded from the

scheme?

If the purpose is to reduce disparities, how should the region be defined? Is there an economic basis for defining the region? From the standpoint of administration, is such a basis any more feasible with respect to reducing disparities than with respect to reducing competition? Does it suggest clear limits? What role do political factors play in determining the boundary?

One argument for sharing the fiscal benefits of development is that a new development may force residents of an entire area to incur the costs of that development in the form of added congestion or environmental degradation. As long as people are not compensated for bearing these extra costs, these costs are referred to as external effects or *external* costs. Can this concept of external costs be used to help define a region to be included in a tax base sharing plan?

III. AN IDEA IN ACTION: EFFECTS OF THE STATUTE

Proponents of Base Sharing have identified several benefits which will accrue to metropolitan areas adopting the idea. These include:

1. The reduction of interjurisdictional competition.
2. Relief from the property tax burden on residential property.
3. Elimination of incentives for fiscal zoning.
4. Encouragihg the preservation of open space.
5. Preservation of the autonomy of local taxing units.
6. Reduction in fiscal disparities and, as a result, greater independence of local public services from local property valuation.
7. Encouragement of orderly urban development by sharing revenues and facilitating cooperation.

(See Katherine Lyall, "Tax Base Sharing: A Fiscal Aid Toward More Rational Land Use Planning," 41 *Journal of the American Institute of Planners* 90 (1970); Margaret Simms, "Metropolitan Tax Base Sharing: Is It The Solution To Metropolitan Fiscal Problems?" The Urban Institute, forthcoming.

In evaluating these claims, recall the different elements of a base-sharing scheme and consider how different elements could be changed to facilitate alternative purposes.

A. Fiscal Disparities

Fiscal disparities, which came into greatest prominence in the series of equal protection litigations for the provision of education, represent an unequal distribution of the property tax base. This results in inequities in the tax rates which residents of different local governing units need to pay in order to obtain the same level of public services.

To some commentators, these disparities are part of the market-basket of choices which the system provides to the American consumer. This is the core of a proposition first articulated by Charles Tiebout. See Tiebout, "A Pure Theory of Local Expenditures," 64 *Journal of Political Economy* 416 (1956).

> In 1956, Charles Tiebout presented an intriguing analysis of how individual preferences for public goods could be satisfied within a system of local governments. In general terms, Tiebout's theory envisions (1) a number of localities each offering a different menu of public goods and (2) a population of perfectly mobile individuals each choosing to take up residence in that community coming closest to matching his preferred mix of public goods and services. It is conceptually possible that each individual could find a locality offering the exact quantity and variety of desired public

> services. If it were possible to charge each individual on the basis of his consumption of public goods, individual preferences for local goods (and taxes) would be perfectly satisfied, and the intra-national population distribution would move to an equilibrium.[1]
>
> The Tiebout model's assumption of perfect individual mobility in choosing between localities creates a substitute for the market process in reconciling differing individual preferences for local public goods. The objective of this paper, however, is to show that although a static population distribution can exist such that all individual preferences for local public goods are satisfied, the equilibrium of this distribution is dynamically unstable. The population distribution fails to maintain equilibrium because when taxes on income or wealth rather than user charges finance the public sector, differences in per capita income or wealth between localities and the unequal distribution of income and wealth within each community can provide a motive for moving which may be independent of the individual's preferred menu of public goods.
>
> An explanation of fiscally induced migration follows. The mix and volume of local expenditures are determined through nonmarket political processes, and the benefits of these expenditures presumably accrue equally to each resident of the community. However, the taxes to pay for the public goods are usually based on property values, on sales, or on income. Therefore, roughly speaking, real income is redistributed from rich to poor within each locality.[2] Thus, an individual who is relatively rich in his locality may find it advantageous to migrate to another locality where given his existing income and wealth, he will be relatively poor. It is also apparent that a relatively poor person might find it advantageous to move to a richer town in order to secure an even larger real income transfer. The pattern of migration would follow a cycle. There is an economic motivation for the relatively rich to leave a locality to escape the burden of financing poorer people. The poorer people, however, might be expected to follow closely behind thus creating the conditions for a repetition of the cycle.
>
> J.R. Aronson and E. Schwartz, "Financing Public Goods and the Distribution of Population in a System of Local Governments," 26 National Tax Journal 137, 138 (1973).

To stabilize this pattern, localities use zoning restrictions, preferential treatment for industry and other devices to protect and enlarge their tax base. The result is disparities in the per-capita tax base available to finance local services.

Is the focus on the variance in per capita tax base appropriate? If the objective is to equalize the ability to provide services, is it realistic to abstract from the variance in expenditure needs? Is there a better operational definition of fiscal disparities? As you read the following material, try to formulate an appropriate concept for the purposes of both legislation and litigation. Are they the same? How is your concept tailored to meet the purposes of the statute? The requirements of proof? Do political considerations play a role?

1. Fiscal Disparities: Constitutional Limitations

a) *San Antonio School Board v. Rodriguez, 411 U.S. 1 (1972).*

Plaintiffs challenged the Texas school finance system on equal protection grounds. The Texas system consisted of two elements. Local school districts raised revenue in the traditional manner. In addition, they received money from the Minimum Foundation Program, a state program designed to have an equalizing effect on expenditure levels. This program was funded with relatively larger contributions from the wealthier districts, and money was distributed on a matching basis. Nevertheless, due to inequalities in the distribution of the tax base, wealthy districts were able to raise more local revenues than their poorer

counterparts, and with a lower tax rate; thus, expenditure inequalities persisted.

The Court, in an opinion by Justice Powell, denied the equal protection claim. First, it rejected the argument that the differences in expenditures between districts constituted discrimination on the basis of a suspect class —wealth: "For these two reasons—the absence of any evidence that the financing system discriminated against any definable category of 'poor' people or that it results in the absolute deprivation of education—the disadvantaged class is not susceptible to identification in fundamental terms. . . . . . . [T]he system of alleged discrimination and the class it defines have none of the traditional indicia of suspectness. . ." 411 U.S. 1, 25, 28. Powell then rejected the claim that the system deprived residents of poorer districts of a fundamental right:

> Even if it were conceded that some identifiable quantum of education is a Constitutionally protected prerequisite to the meaningful exercise of [the rights to speak and to vote], we have no indication that the present levels of educational expenditures in Texas provide an education that falls short. . . . . no charge could be made that the system fails to provide each child with an opportunity to acquire the basic minimal skills . . . . . necessary for [the exercise of other Constitutional rights.]
>
> 411 U.S. 1, 36, 37.

Powell then turned to the underlying federalism issue.

> It must be remembered, also, that every claim arising under the Equal Protection Clause has implications for the relationship between national and state power under our federal system. Questions of federalism are always inherent in the process of determining whether a State's laws are to be accorded the traditional presumption of constitutionality, or are to be subjected instead to rigorous judicial scrutiny. While "[t]he maintenance of the principles of federalism is a foremost consideration in interpreting any of the pertinent constitutional provisions under which this Court examines state action,"[88] it would be difficult to imagine a case having a greater potential impact on our federal system than the one now before us, in which we are urged to abrogate systems of financing public education presently in existence in virtually every State.
>
> The foregoing considerations buttress our conclusion that Texas' system of public school finance is an inappropriate candidate for strict judicial scrutiny. These same considerations are relevant to the determination whether that system, with its conceded imperfections, nevertheless bears some rational relationship to a legitimate state purpose. It is to this question that we next turn our attention.
>
> [The state purpose identified was local control of education.]
>
> The persistence of attachment to government at the lowest level where education is concerned reflects the depth of commitment of its supporters. In part, local control means, as Professor Coleman suggests, the freedom to devote more money to the education of one's children. Equally important, however, is the opportunity it offers for participation in the decisionmaking process that determines how those local tax dollars will be spent. Each locality is free to tailor local programs to local needs. Pluralism also affords some opportunity for experimentation, innovation, and a healthy competition for educational excellence.
>
> Appellees do not question the propriety of Texas' dedication to local control of education. To the contrary, they attack the school-financing system precisely because, in their view, it does not provide the same level of local control and fiscal flexibility in all districts. Appellees suggest that local control could be preserved and promoted under other financing systems that resulted in more equality in educational expenditures. While it

is no doubt true that reliance on local property taxation for school revenues provides less freedom of choice with respect to expenditures for some districts than for others.[107]

Appellees further urge that the Texas system is unconstitutionally arbitrary because it allows the availability of local taxable resources to turn on "happenstance." They see no justification for a system that allows, as they contend, the quality of education to fluctuate on the basis of the fortuitous positioning of the boundary lines of political subdivisions and the location of valuable commercial and industrial property. But any scheme of local taxation—indeed the very existence of identifiable local governmental units—requires the establishment of jurisdictional boundaries that are inevitably arbitrary. It is equally inevitable that some localities are going to be blessed with more taxable assets than others.[110] Nor is local wealth a static quantity. Changes in the level of taxable wealth within any district may result from any number of events, some of which local residents can and do influence. For instance, commercial and industrial enterprises may be encouraged to locate within a district by various actions—public and private.

Moreover, if local taxation for local expenditures were an unconstitutional method of providing for education then it might be an equally impermissible means of providing other necessary services customarily financed largely from local property taxes, including local police and fire protection, public health and hospitals, and public utility facilities of various kinds. We perceive no justification for such a severe denigration of local property taxation and control as would follow from appellees' contentions. It has simply never been within the constitutional prerogative of this Court to nullify statewide measures for financing public services merely because the burdens or benefits thereof fall unevenly depending upon the relative wealth of the political subdivisions in which citizens live.

In sum, to the extent that the Texas system of school financing results in unequal expenditures between children who happen to reside in different districts, we cannot say that such disparities are the product of a system that is so irrational as to be invidiously discriminatory.

411 U.S. 1, 49-55.

b) Fiscal Disparities: The State Courts

Several state school finance schemes have been invalidated by state courts using equal protection analysis similar to that rejected in *San Antonio*. See *Serrano v. Priest*, 5 Cal. 3d 584, 487 P. 2d 1241, 96 Cal. Rptr. 601 (1971); *Van Dusartz v. Hatfield* 334 F. Supp. 870 (1971).

Robinson v. Cahill, 62 N.J. 473, 303 A.2d 273 (1972).

Shortly after the decision in *San Antonio*, the New Jersey Supreme Court found that state's method of financing schools unconstitutional, but declined to apply the equal protection analysis. After discussing *San Antonio*, Chief Justice Weintraub continued:

[6] The question whether the equal protection demand of our State Constitution is offended remains for us to decide. Conceivably a State Constitution could be more demanding. For one thing, there is absent the principle of federalism which cautions against too expansive a view of a federal constitutional limitation upon the power and opportunity of the several States to cope with their own problems in the light of their own circumstances. The majority in *Rodriguez* expressly noted that "every claim arising under the Equal Protection Clause has implications for the relationship between national and state power under our federal system," adding that "it would be difficult to imagine a case having a greater potential impact on our federal system than the one now before us, in which we are

urged to abrogate systems of financing public education presently in existence in virtually every State" (93 S. Ct. at 1302).

We go then to the question whether our State guarantee of equal protection is offended.

We hesitate to turn this case upon the State equal protection clause. The reason is that the equal protection clause may be unmanageable if it is called upon to supply categorical answers in the vast area of human needs, choosing those which must be met and a single basis upon which the State must act. The difficulties become apparent in the argument in the case at hand.

We will consider first the claim that there is classification according to "wealth," then the claim that a "fundamental right" is involved, and finally the claim that no "compelling state interest" warrants the statutory treatment of the subject.

[7] Wealth may or may not be an invidious basis for the imposition of a burden or for the enjoyment of a benefit. Wealth is not at all "suspect" as a basis for raising revenues. As to the taxpayer, classifications depend upon or reflect wealth except in the rare case of a head tax. Whether wealth is invidious in its impact upon the enjoyment of rights or benefits is a more complex question, but again it cannot be said to be "suspect" in all settings. Obviously financial lack is a laudable basis when a statute seeks to ameliorate poverty. On the other hand, a net worth or poll tax requirement for voting is today[4] arbitrary.

We can be sure the result would be the same if the right to attend elementary or secondary schools was made to depend upon the net worth of the pupil or of his parents.

The Legislature of course has not conditioned attendance at elementary and secondary schools upon the net worth of the pupil or his parents or even on the payment of a fee. Nor has the Legislature mandated that local government shall limit its current expenditures on the basis of the amount of ratables. The most that can be said is that, the subject having been committed in part to local government, the sums made available for education by local taxation have been influenced by the size of the tax base available for all activities of local government and by the judgment of local authorities as to how much shall be raised for all local needs.

In this respect education is handled no differently than sundry other essential services which are supplied on that basis. A signal feature of home rule as we know it is that the residents of a political subdivision are permitted within substantial limits to decide how much to raise for services which are necessary or sufficiently desirable to justify the exertion of the taxing power. How much will be done by local government may, of course, depend upon the size of its tax base, which, as to local government, is substantially the value of its real property. It is inevitable that expenditures per resident will vary among municipalities, resulting in differences as to benefits and tax burden. If this is held to constitute classification according to "wealth" and therefore "suspect," our political structure will be fundamentally changed.

We need hardly suggest the convulsive implications if home rule is vulnerable upon either of the grounds to which we have referred. Nor need we expound the difficulties of management of judicial solutions if the problem must be met by the courts. We point to the dimensions of the subject to explain why we should not deal with it on the record of this case.

308 A 2d 273,282-283,287

Nor was the requirement that education be a fundamental right helpful, as the term itself lacked any definition, and since the analysis used by Powell in *San Antonio* was "immediately vulnerable." Finally, "if a right is somehow found to be 'fundamental,' there remains the question as to what State interest is

compelling' and there, too, we find little, if any, light.'' 303 A 2d 273,282.

Weintraub found the discrepancies in dollar input per pupil unconstitutional under an 1875 amendment to the New Jersey Constitution which provided: ''The Legislature shall provide for the maintenance and support of a thorough and efficient system of free public schools. . .'' After noting the lack of any illuminating legislative history and discussing several related measures, the court found a requirement of equality:

> [17,18] In the light of the foregoing, it cannot be said the 1875 amendments were intended to insure statewide equality among taxpayers. But we do not doubt that an equal educational opportunity for children was precisely in mind. The mandate that there be maintained and supported ''a thorough and efficient system of free public schools for the instruction of all the children in the State between the ages of five and eighteen years'' can have no other import.
>
> [20] The trial court found the constitutional demand had not been met and did so on the basis of discrepancies in dollar input per pupil. We agree. We deal with the problem in those terms because dollar input is plainly relevant and because we have been shown no other viable criterion for measuring compliance with the constitutional mandate. The constitutional mandate could not be said to be satisfied unless we were to suppose the unlikely proposition that the lowest level of dollar performance happens to coincide with the constitutional mandate and that all efforts beyond the lowest level are attributable to local decisions to do more than the State was obliged to do.

Under *San Antonio,* to what extent must the provision of essential public services be equalized? Is there any such requirement? Justice White's dissent in *San Antonio* argued that 'state interest' in local control asserted by Texas and recognized by Powell required a meaningful option to choose between various tax rates and expenditure levels. Poorer districts, lacking the tax base to support higher expenditures, lack that option; thus, the argument for local control is specious. Will base sharing provide that meaningful option and yet preserve the local control which Powell finds so important? Would base sharing meet the state constitutional requirement in *Robinson?* Weintraub's opinion, including the discussion of the state equal protection claim, was drafted before the opinion in *San Antonio* was announced. Does his approach extend to other areas of local government activity? Is it more helpful than the equal protection analysis? Does Justice White require an equal per-capita tax base or equal expenditures? Weintraub? What characteristics would be required by Justice White? Under Robinson?

2. Effects of the Minnesota Statute on Fiscal Disparities

Though the Act has been in operation for only a short time, its initial effects have been evaluated. The following is from Reschovsky and Knaff, ''Tax Base Sharing: An Assessment of the Minnesota Experience,'' 43 *Journal of the American Institute of Planners 361.*

> Complete data are available only for the first two years of the plan's operation, 1974 and 1975. In 1974, $137 million of tax base was contributed and shared by metropolitan area governments. In 1975 the area-wide base grew to nearly $188 million. In 1974 the area-wide base equalled nearly 7 percent of the value of all commercial-industrial property in the metropolitan area. In 1975 this figure had grown to nearly 9 percent. Over time the area-wide base will approach 40 percent of the total commercial-industrial property tax base. In both 1974 and 1975, of the 195 municipalities in the metropolitan area, 143 experienced a net gain in base from the operation of

the plan; 52 suffered a net loss in base. In both years the two central cities, Minneapolis and St. Paul, experienced a net gain in base from the sharing plan. Of the ten largest suburban communities, five gained and five lost base in each of the first two years. It should be noted that, with only two exceptions, the tax base sharing plan resulted in the 1975 commercial-industrial tax base of each community being higher than its value in 1971. Without tax base sharing, sixteen metropolitan area communities would have had smaller commercial-industrial tax bases in 1975 than in 1971.

3. Evaluation of the Plan's Operation

In evaluating the Minnesota tax base sharing plan, this study looks at the pattern of contributions to and distributions from the areawide base during the plan's first two years, attempting to determine the extent to which the operation of the plan led to a reduction in metropolitan area fiscal disparities. A further assessment attempts to find out whether a reduction of fiscal disparities will, in fact lead to a more efficient and equitable pattern of metropolitan development.

As discussed above, variations in per capita property values and in the distribution of high cost groups of people are major causes of metropolitan area fiscal disparities. In order for a significant reduction in fiscal disparities to occur, tax base sharing must result in a net redistribution of tax base from communities of large per capita tax bases to those with small per capita tax bases, and from places with few high cost residents to places with large concentrations of high cost residents.

The first question addressed is whether communities with large tax bases are in general those communities which are experiencing the largest growth in commercial-industrial property values, and hence making the largest contributions to tax base to the areawide base. To the extent that this pattern exists, communities with large tax bases (high fiscal capacities) will be net contributors of base under the tax base sharing plan. This pattern results because, by definition, a community's distribution from the areawide base is inversely related to the size of its tax base. Table 1 indicates that, on average, larger per capita contributions are made by places with higher fiscal capacities. The relationship is not strong; a number of high fiscal capacity communities contribute relatively small amounts of base, and a few communities with low fiscal capacities make large per capita base contributions. In fact, in 1974 the simple correlation between fiscal capacity and per capita base contributions was only 0.02. In 1975 it was 0.05. When the data on contributions are combined with the data on the distributions from the areawide base, the pattern as expected shows that, on average, low fiscal capacity communities are net recipients or gainers of base and high fiscal capacity places are net contributors.

There are exceptions to this pattern. In both years, approximately one quarter of those communities that experienced the largest net gains in base (over $40 per capita) had fiscal capacities of over $10,000 (the areawide average fiscal capacity was $9,900). In 1975, North Oaks, a rich residential suburb with a per capita tax base and an average resident income more than double the areawide averages, experienced a net gain of base of nearly $20 per capita. Oak Park Heights, with a power plant within its boundaries, has a tax base more than five times the metropolitan area average. Nevertheless, because its commercial-industrial tax base did not *grow*, and because of the lower limit built into the distribution formula, Oak Park Heights gained nearly $45 per capita due to tax base sharing.

Tables 2 and 3 present data on the net impact of base sharing on metropoli-

Table 1.
Number of municipalities classified by size of fiscal base, per capita base contribution, and net gain or loss of base

	1974							1975						
		Per capita contributions							Per capita contributions					
Fiscal capacity: per capita property tax base	# of municipalities	Less than $10	$10 to $40	$40 to $80	$80 to $150	More than $150	Average contributions*	# of municipalities	Less than $10	$10 to $40	$40 to $80	$80 to $150	More than $150	Average contributions*
Less than $5,000	9	3	3	2	1	0	$ 21	9	4	2	2	0	1	$ 30
$ 5,000 – $ 7,500	52	10	22	13	5	2	$ 45	39	3	13	12	8	3	$ 74
$ 7,500 – $10,000	58	9	19	14	9	7	$ 55	58	8	17	12	13	8	$ 52
$10,000 – $15,000	56	16	15	8	12	5	$106	64	13	18	11	10	12	$177
More than $15,000	20	10	5	2	0	3	$161	25	12	4	3	2	4	$223
Totals	195	48	64	39	27	17		195	40	54	40	33	28	

	1974							1975						
		Per capita gain or loss							Per capita gain or loss					
Fiscal capacity: per capita property tax base	# of municipalities	Less than $ – 100	$ – 100 to $0	$0 to $40	$40 to $80	More than $80	Average gain or loss of base*	# of municipalities	Less than $ – 100	$ – 100 to $0	$0 to $40	$40 to $80	More than $80	Average gain or loss of base*
Less than $5,000	9	0	0	1	0	8	$ 187	9	0	0	1	0	8	$ 238
$ 5,000 – $ 7,500	52	0	4	10	25	13	$ 44	39	1	2	5	13	18	$ 54
$ 7,500 – $10,000	58	6	14	17	21	0	$ 14	58	7	9	11	18	13	$ 46
$10,000 – $15,000	56	5	18	15	18	0	$ – 55	64	10	15	10	28	1	$ – 106
More than $15,000	20	3	2	15	0	0	$ – 127	25	4	4	5	12	0	$ – 175
Totals	195	14	38	58	64	21		195	22	30	32	71	40	

**Municipal populations were used as weights in calculating averages. In this way the averages present the impact on the average citizen in each category of municipality.*
Source: Calculated from data supplied by the Minnesota Department of Revenue.

TABLE 2
NUMBER OF MUNICIPALITIES CLASSIFIED BY PERCENTAGE OF FAMILIES WITH LESS THAN $3,000 INCOME AND NET GAIN OR LOSS OF BASE

	1974							1975						
		Per capita gain or loss							Per capita gain or loss					
% of families with income less than $3,000	# of munici-palities	Less than $ – 100	$ – 100 to $0	$0 to $40	$40 to $80	More than $80	Average gain or loss of base*	# of munici-palities	Less than $ – 100	$ – 100 to $0	$0 to $40	$40 to $80	More than $80	Average gain or loss of base*
Less than 5	56	5	21	12	10	8	$ – 39	56	10	15	9	9	13	$ – 63
5 – 10	64	5	12	16	26	5	$ 3	64	7	9	11	25	12	$ – 14
10 – 15	41	2	3	15	17	4	$ 34	41	2	4	8	18	9	$ 67
15 – 20	21	1	2	8	7	3	$ 7	21	2	2	2	12	3	$ – 5
More than 20	13	1	0	7	4	1	$ 31	13	1	0	2	7	3	$ 49
Total	195	14	38	58	64	21		195	22	30	32	71	40	

**Municipal populations were used as weights in calculating averages.*
Source: Calculated from data supplied by the Minnesota Department of Revenue.

TABLE 3
NUMBER OF MUNICIPALITIES CLASSIFIED BY PERCENTAGE OF POPULATION OVER 65 YEARS OF AGE AND NET GAIN OR LOSS OF BASE

	1974							1975						
		Per capita gain or loss							Per capita gain or loss					
% population over 65 years of age	# of munici-palities	Less than $ – 100	$ – 100 to $0	$0 to $40	$40 to $80	More than $80	Average gain or loss of base*	# of munici-palities	Less than $ – 100	$ – 100 to $0	$0 to $40	$40 to $80	More than $80	Average gain or loss of base*
Less than 2	15	1	6	3	2	3	$ – 16	15	2	5	3	1	4	$ – 25
2 – 6	79	6	20	21	27	5	$ – 25	79	13	13	15	24	14	$ – 54
6 – 10	66	4	10	19	25	8	$ – 22	66	4	8	7	35	12	$ – 29
10 – 15	25	3	2	11	6	3	$ 43	25	3	3	7	6	6	$ 59
More than 15	10	0	0	4	4	2	$ 26	10	0	1	0	5	4	$ 73
Total	195	14	38	58	64	21		195	22	30	32	71	40	

Municipal populations were used as weights in calculating averages.
Source: Calculated from data supplied by the Minnesota Department of Revenue.

tan area communities, characterized by two cost related variables: the percentage of families with incomes below $3,000 and the percentage of population over 65 years of age. The presence of poor, who are concentrated in the more urban areas, tends to increase the per unit costs of providing many public services and usually necessitates higher levels of social welfare, and housing related public services. The elderly, who also are concentrated in the more urbanized areas, generally require more medical and recreational services and tend to require higher levels of police protection because of their greater vulnerability to crime.

The data from the first two years of the plan's operation show that, on average, tax base is distributed from places with few elderly and poor to places with larger concentrations of these two groups. This pattern, however, does not hold without exception. A few jurisdictions with high proportions of poor and elderly are net contributors of base, and the twenty-one communities with between 15 and 20 percent poor families, on average, have neither gained nor lost base during the first two years. These results should not be surprising in light of the fact that tax base per capita is distributed inversely to each jurisdiction's fiscal capacity. No account is made in the distribution formula for differences in costs of providing public services. For example, the two central cities, Minneapolis and St. Paul, have the majority of the metropolitan area's high need populations, those that significantly add to the costs of providing local public services. However, because the central cities have near average fiscal capacities, the base distributions they receive do not reflect these special demands made upon their local fiscal capacities.

After two years of experience with tax base sharing, fiscal disparities in the Twin Cities area have been slightly reduced. Over time a larger proportion of the total base will be shared and as long as the relatively high fiscal capacity communities continue to experience growth in their commercial-industrial base, the reduction of fiscal disparities will increase. However, the potential for fiscal disparities reduction is significantly reduced by using a distribution formula that takes no account of factors such as the size of the poverty population or of other groups that put special demands on the local public sector.

The city of Bloomington, in its report "Analysis of Fiscal Disparities," presents a different view of the same facts.

> Many metropolitan area communities have been most concerned about the actual dollar impact of the new Fiscal Disparities Law. It has been generally thought that the impact on individual communities would be significant, but not too significant; helpful, and not detrimental. The information contained in this analysis indicates that none of these assumptions may be true.
>
> Information herein indicates that the matter of taxation under the Fiscal Disparities Act will become a matter of considerable concern for many of our metropolitan area commercial/industrial tax-payers. It appears that up until now, the business community has considered Fiscal Disparities to be just a reshuffling of tax dollars already being levied. They are not prepared for the fact that, in many instances, substantial additional taxes are being collected from them this year for distribution into other communities.
>
> Further, it appears that the relative tax impact on some modestly priced homes in some of the communities affected will be appalling. Nothing was built into the law to prohibit $50 to $100 tax increases on these homes purely as a result of the Fiscal Disparities Act. This will be the case in at least two or three communities which have been forced to contribute a substantial portion of their tax base to the metropolitan pool. . .There is

> nothing in the law to prevent this extremely regressive feature, as a result of which the individual living in a home in St. Paul with an assessor's market value of $100,000 will receive a tax break of $98.25, while the $40,000 homeowner in Shakopee pays an additional $114.31 because of Fiscal Disparities. St. Paul is a net recipient; Shakopee, a net contributor. . .
>
> Business and industry contribute a great deal to the socio-economic life of this area. Some of them are likely to question the means and the motives of their government when they see their 1975 tax bills. Control Data in Bloomington, and one of the area's largest taxpayers, will pay approximately $34,000 more in taxes in 1975 to support the fiscal disparities program. The Radisson South Hotel in Bloomington will pay $13,800 more. In Bloomington, business property will pay an additional $366,000 to support Fiscal Disparities. The Howard Johnson Motor Lodge in Burnsville will pay $2,397 more, while all business in Burnsville will pay an additional $142,000. All to what end? True, some of this money will be distributed back to cities like Crystal where a $30,000 homeowner will realize $19.24. Perhaps considered more important by some is the fact that the Saint Paul Hilton Hotel will realize an $11,574 reduction in its 1975 tax bill, but probably not by its business competitors in Bloomington and Burnsville.
>
> Another inequality in the whole fiscal disparity procedure is the fact that the "sharing" of the 40% of commercial/industrial growth is based on the ideal assumption that all such property will be assessed at the same levels. This is not the case. It is interesting to note that probably the largest recipient under fiscal disparities (City of Saint Paul) is located in Ramsey County, where the commercial/industrial property is valued for tax purposes at about 78% of market value, the lowest of any in the seven county area. . . . . It is difficult to see how anyone can feel that the implementation of such a law can work properly in this sort of situation.

One study applied the Minnesota scheme to a computer model of the economy of the Pittsburgh region. The results indicated a reduction in disparities in per-capita taxes, though less significant than that which occurred in Minnesota, due to slower growth. Interestingly, there was a small positive relationship between net benefits and communities with low family income (an alternative measure of disparities), though there was no such correlation with respect to median community-income groups. See Walter Pilosa, "Metropolitan Tax Base Sharing: Its Potential and Limitations," 4 *Public Finance Quarterly* 215.

More generally, consider again the role played by each of the five elements identified above. Under the Minnesota scheme, redistribution will occur to the extent that wealthy jurisdictions grow and the distribution formula benefits low tax-base localities.

> Residential suburbs generally have a low proportion of commercial-industrial to total assessed valuation. If a residential suburb has a high fiscal capacity—because, for example, of high property values—it may well benefit unduly from the operation of the Act. Such a municipality would contribute relatively little to the area-wide tax base; yet, because distribution is based primarily on population, it would almost certainly be assured of showing a net gain under the statute. Thus, an already superior ability to provide public services to residents would be further enhanced by the Act.[88]
>
> Although a municipality with a high proportion of commerical-industrial to total assessed valuation may have a correspondingly high fiscal capacity, that municipality must provide services such as fire and police protection to the commercial-industrial property. Where the municipality also has a small population, however, it will receive less than it contributes to the area-wide tax base. If the cost of providing services to the commercial-industrial property is greater than the tax revenues that such property will generate after the redistribution mandated by the Act, the

> burden of providing the services will partially fall upon the residents of the municipality.[80] In this respect, the Act may actually hinder the provision of public services in those municipalities with a small population and a fiscal capacity composed primarily of Commercial/Industrial assessed valuation.
>
> 59 Minn. Law Rev. 927, 949

Should a poor community which lands a power plant or develops an industrial park be required to share that gain? Will such anomalies persist or will they be redressed in later years? A low-base municipality which is a net contributor in one year due to a single large project may become a net recipient in later years. Suppose disparities are due in large part to the wide variations in the value of residential property? Should the residential base be shared? From the standpoint of reducing disparities, does it make sense to treat commercial and industrial property the same? Some evidence suggests that wealthier communities tend to get commercial establishments, while poorer ones get industrial firms. Could more redistribution be effected by only sharing commercial growth? See E. Mills and W. Oates, *Fiscal Zoning and Land Use Controls,* pp. 165. If the boundary extends beyond the metropolitan area and encompasses rural communities, will they benefit? Should they? Finally, does reducing disparities require compromising any of the other purposes of base-sharing?

B. Land Use Effects

Equalizing the distribution of fiscal resources would itself be a notable achievement, yet supporters of the proposal have envisioned more. Since local land use policy is highly colored by fiscal concerns, separating fiscal strength from the location of new C/I activity may affect the pattern of that development. How does the statute accomplish this? More specifically, what mechanisms are provided for influencing land use decisions? How does it change the incentives facing the participants in the land development process—communities, developers, landowners, taxpayers, voters? The allocation of land to competing uses is a complex process. To simplify discussion, let us consider three aspects.

1. Fiscal Zoning

It is reasonable to assume that, other things constant, all households prefer to live in a community with the lowest property taxes *per unit of local public services*. Economists refer to this quantity as a "tax-price." Where public services are financed by the property tax, it is the interest of each household to locate in a community with a high per capita property tax base. The larger the tax base, the lower the per household tax bill for any given level of public services. Low income households will thus always attempt to live in communities inhabited by higher income residents with similar public sector tastes. However, the entry of low income households into a wealthy community will raise the "tax-price" faced by all the residents. See "The Theory of Local Public Services and Finance . . .", in E. Mills and W. Oates, *Fiscal Zoning and Land Use Controls,* 1975. This can be prevented by zoning out all households whose entry into a community would raise the "tax-prices" faced by current residents. This can be accomplished by zoning out all households with below average per capita tax base, i.e. the market value of their home, or above average fiscal costs. It is argued that sharing the tax base will help eliminate the incentive for fiscal zoning. How will this be achieved?

It is instructive first to consider how the zoning process affects land use. By prohibiting the high-density residential development which represents the less

expensive range of housing alternatives, municipalities can effectively foreclose low-income/high-expenditure populations. Simultaneously, since space tends to be an income-elastic consumer good, low density development corresponds with a relatively high per-capita tax base. Finally, land can be reserved for C/I development. The conventional wisdom among most local officials is that C/I development will generate a fiscal surplus. Tax base sharing addresses zoning policy only indirectly, by manipulating the fiscal returns from C/I land use.

The major thrust is to reduce the net benefits of C/I growth, by up to 40% of the increment to the tax base. How does this cut? What assumptions are made about the characteristics of—and reasons for—fiscal zoning? If revenues from C/I development are limited, might there be a greater incentive to zone out high-expenditure populations? Is zoning policy colored as much by fiscal concerns as it is by other considerations—race, class, etc.?

How will the distribution formula affect zoning policies? Most broadly, base-sharing eliminates the all-or-nothing proposition of the conventional property tax. Thus, simply sharing growth in the tax base will encourage municipalities to cooperate in the location of large manufacturing plants, utilities, industrial parks, etc., at least to the extent that such activities are sought for fiscal reasons. This allows areawide planning decisions to be made without imposing on the autonomy of municipalities with respect to strictly local matters.

As many commentators have noted, base sharing could have a greater impact on fiscal disparities if the distribution formula incorporated indicators of need, such as income, number of school-age children, and the like. Using some index of need would make high expenditure populations less unattractive to municipalities, from a fiscal standpoint. Could the distribution formula be used to induce municipalities to seek specific types of land use. Should it? Would sharing residential valuation make base-sharing more effective in discouraging fiscal zoning? Consider, too, the effect of the percentage of growth shared and the size of the region.

Equalizing the tax base presents both net recipient and net contributing municipalities with the choice of decreasing (increasing) tax rates or increasing (decreasing) the level of services provided. As the Bloomington article illustrates, base sharing has had an effect on tax rates. What effect will this have on fiscal zoning? To the extent that tax rates are capitalized into property values, values in net-contributing jurisdictions will fall. Will this make it easier for low-income groups to buy in? Conversely, will it encourage them to leave municipalities which are net recipients? How will the change in tax rates affect the location of C/I development?

Base sharing may discourage the intensive use of land. It is generally agreed that the property tax levied on both land and improvements, results in less intensive land use than a tax on land alone. If base-sharing results in higher rates in some areas, will this encourage sprawl? Is this consistent with the purpose of the statute?

2. Location Decisions

> At the local level, the Act is likely to affect the location of future commercial-industrial development. Inasmuch as any growth in the assessed valuation of commercial-industrial property is to be shared in part by the entire area, municipalities will have less incentive to attract commercial-industrial development and therefore less desire to offer preferential assessments or to extend public services to areas not otherwise

> requiring them. Residential suburbs, in particular, should have little incentive to encourage commercial-industrial development, because under the Act they can share in the assessed valuation of such property while enduring none of the accompanying congestion or pollution. Developing communities should also have less desire for additional commercial-industrial development, since 40% of its assessed valuation would be subject to the levies of other communities. Insofar as the tax revenues to be generated by the remaining 60% of the new property's assessed valuation—together with the amount received from the area-wide tax base—exceed the costs of services for the development and also offset the nuisance of the development to ear, eye, and lung, commercial and industrial concerns should not be unwelcome. A fine line exists, therefore, between desirable and undesirable developments, especially in view of the uncertainties inherent in the relationship between tax liabilities and service costs.
>
> 59 Minn. Law Rev. 927, 955

Does the Minnesota proposal deal with the location of different types of development, the rate of development, or the intensity of land use? Reducing the tax benefits from new C/I activity makes it less attractive to any given locality; this should discourage competition for such development, affecting the location of firms. Also, discouraging competition should make municipal governments less eager to annex and extend services to outlying areas, resulting in slower and more intense development.

The scheme both alters incentives to municipalities and attempts to influence the inducements facing individual firms. From the standpoint of the individual community, the fiscal benefit calculus is altered by reducing property tax revenues from new development by some fraction. Is the narrow focus on the fiscal benefits from the property tax realistic, or are there other reasons that communities seek C/I development?

> Inver Grove Heights' mayor Eugene Atkins said that he has mixed emotions about new development in his community. While he characterized himself as one of the original supporters of tax base sharing, he now asks the basic question: "What will it get us?" when approached by a prospective new industry. If the industry will provide new jobs for Inver Grove Heights, Mayor Atkins tends to support the prospect of development. But if new development only means "new tax base," the mayor is more skeptical. . . .
>
> "Tax Base Sharing," National Council for Urban Economic Development Information Service, April, 1976, no. 5, p. 5.

Note that the statute treats commercial and industrial property the same. Is this realistic? To some extent, this depends on the characteristics of the relevant region. Because of the high degree of mobility of residents of suburban communities and large cities, the gain to a municipality from new development, in terms of jobs for its residents may be small—many of the jobs will go to residents of other communities. An independent, relatively self-contained community, on the other hand, may be able to retain most of the jobs created by growth. The mobility of suburban residents operates to make commercial activity more attractive. Regional commercial shopping centers attract shoppers from other jurisdictions, importing sales tax revenue, and thus providing an added fiscal benefit to the municipality.

The argument that base sharing, by reducing competition for C/I development, will influence the location of such activity assumes that firms will

respond to differentials in tax rates or to preferential assessments. How significant are these incentives? What about other factors—the availability of materials and labor, the provision of services, and transportation patterns. There is little conclusive empirical work on industrial location, but a representative of a large corporation describes how that company selects the location for a new plant:

> [S]tates are rated by five major factors: Fiscal conditions [45 of 100 points], industrial conditions [30 points], population characteristics [10 points], construction costs [10 points], and the size of [existing] investment in that state. . . . .
>
> When all of these measurements are made, we have some firm ideas about the business climate which have significant impact on our final decision.
>
> Coming down to a specific site in a state is far more involved. When we are evaluating several possible sites for a new plant, we give minute attention to a long list of criteria, grouped in eight major categories. In some cases, the source of raw materials will be the overriding factor in site selection. . . .
>
> Taxes are considered along with other operating costs. While high taxes could preclude a potential site, low taxes are not enough by themselves to attract a new plant—nor are tax moratoriums. We are, frankly, less impressed by this sort of inducement than by the history and trend of taxes and the state's overall economic policy.
>
> Richard Heckert, "Metropolitan Fiscal Disparities," 29 National Tax Journal 336, 337-338.

This suggests that base sharing, insofar as it discourages preferential assessments, is not likely to have much influence on the firm's location. However, Heckert goes on to suggest that the existence of characteristics of metropolitan government may be a favorable factor for the region as a whole. This is because metro reduces competition for taxable property; thus, plants which initially located outside municipalities have less reason to fear annexation in the future.

One of the few empirical studies on the location of C/I activity in metropolitan areas found that tax rates were relatively unimportant in explaining the growth of C/I valuation. While tax rates were negatively correlated with growth, the relationship was not strong. Other variables, including per-capita expenditures, intensity of land use and access to the throughway, had more explanatory power. See W.J. Beeman, *The Property Tax and the Spatial Pattern of Growth Within Urban Areas,* U.L.I. monograph #16, 1969.

Note that base-sharing makes C/I growth less attractive to all municipalities. Is it desirable to discourage such growth in all areas? Could the result be an intensification of urban sprawl? What role does the size of the sharing area play? Will base sharing affect all types of commercial and/or industrial activity the same? Smaller manufacturing and retail establishments are more likely to select a location for non-tax reasons and thus less likely to respond to tax differentials.

Base sharing may also influence the rate and intensity of development. The Minnesota statute is part of a broader package of legislation directed toward providing areawide services. One of the arguments for base sharing is that, by reducing competition for development, location decisions will focus more closely on real economic advantages in markets, labor, and raw materials. Can the availability (or lack) of services be treated as a real economic advantage? If so, how is this to be distinguished from tax incentives? Can communities compete in

the provision of services as well as through tax rates? To the extent that there is service competition, base sharing could discourage the premature extension of water and sewer trunk lines, for example. This would encourage more orderly growth. Communities compete for residential as well as C/I growth—will base sharing alone eliminate that competition, or is greater regional control needed?

If base-sharing is to affect land use, it is clear that only growth must be shared. What effects do the other elements have on land use?

- *The fraction of growth shared.* A larger fraction will reduce and eventually eliminate any fiscal benefits of growth. Why not pool all growth?
- *The size of the region.* To the extent that base-sharing encourages municipalities to exclude C/I development, firms may select sites outside of the base-sharing region. However, assuming firms locate in an area because of advantages inherent in the metropolitan region, a sufficiently large region will prevent that. Does the uniformity requirement as presented in Burnsville limit the size?
- *The distribution of the regional levy.* Under the Minnesota plan, after the area-wide levy on shared growth is determined, all C/I property shares the area levy. (473F.08, subd. 6.) In a recent Maryland proposal, the area levy would have been borne entirely by "new valuation"—the shared fraction would have been taxed at the area-wide average rate. This would have the effect of raising the rates on C/I sites in jurisdictions with below-average tax rates and reducing rates on sites in above-average localities.
- *Types of valuation shared and the distribution of the base.* Reconsider the discussion of fiscal zoning. Does the same analysis apply here?

Finally, how would land-use planning differ after the Act? Does it provide incentives or deterrents to annexation, consolidation, and, perhaps, true metropolitan government?

3. Preservation of Open Space

Under the conventional property tax system, some communities with beautiful areas that should be preserved for park and recreational purposes face incentives to let the land be developed in order to enlarge the tax base. This issue emerged in Minnesota to promote passage of the Fiscal Disparities Act, after a large power plant was built near the Twin Cities on the shore of the scenic St. Croix river. The New Jersey legislature has enacted a statute which focuses more directly on the preservation of open space. *New Jersey Statutes* 13:17-60, et seq.

ARTICLE 9. INTERMUNICIPAL TAX-SHARING

13:17-60. Purpose; report to legislature

(a) The Legislature hereby finds and declares that a vital component of any comprehensive plan for the development of the meadowland district, is a program whereby the financial benefits and liabilities of each constituent municipality, are clearly established and equitably distributed. Article 9 of this act provides for such a program, by the creation of an intermunicipal account, and specifically provides that each constituent municipality will be guaranteed, in perpetuity, against loss of its present existing tax ratable values within the meadowland district occurring by reason of the acquisition of taxable real property, through purchase, eminent domain or gift, by a governmental body or agency to be used for a public purpose, to the extent that such loss of existing tax ratable values is not offset by increased true value of the remaining taxable real property within the district, and will equitably share in the new financial benefits and new costs result-

ing from the development of the meadowland district as a whole. This article further provides that the Hackensack Meadowlands Development Commission shall not be able to receive any funds from the intermunicipal account.

13:17-61. Definitions

As used in this article, unless the content indicates another meaning or intent:

(a) "Adjustment year" means the year in which the respective obligations of the intermunicipal account and the constituent municipalities of the district are due and payable.

(b) "Intermunicipal account" means the administrative device established and administered by the commission to record all the transactions made pursuant to this article for the purpose of calculating the meadowlands adjustment payment for each constituent municipality, and to act as the clearing house for the transfer of the meadowlands adjustment payments among the constituent municipalities are required by this article.

(c) "Meadowlands adjustment payment" means the amount that is payable by each constituent municipality to the intermunicipal account, or the amount that is payable by the intermunicipal account to each municipality, as the commission shall determine the case to be pursuant to the provisions of this article.

(d) "Resident enrollment" means the number of full-time pupils, who are residents of the school district and who are enrolled in day schools on the last day of September during the school year in which calculation of aid is made and are attending the public school of the school district or a school district or State teachers college demonstration school in which the school district of residence pays tuition; school district may count in its enrollment any pupil regularly attending on a full-time basis a county vocational school in the same county for which the school district pays tuition.

(e) "Base year" means the calendar year 1970.

(f) "Comparison year" means the second calendar year preceding the adjustment year.

(g) "Appointment rate" means a rate determined as follows:

(1) The total property taxes levied for local, school, and veteran and senior citizens purposes, as certified pursuant to R.S. 54:4-52, of the municipality in the comparison year, divided by

(2) The aggregate true value of all taxable real property, exclusive of Class II railroad property, located in the municipality, both within and without the district in the comparison year.

13:17-67. Increase or decrease in aggregate true value of taxable real property; determination and calculation of aggregate true value; amount payable to intermunicipal account

(a) As used in this section, except as otherwise specifically provided:

(1) The increase or decrease in aggregate true value of taxable real property for any adjustment year shall be the difference between

(i) The aggregate true value of that portion of taxable real property, exclusive of Class II railroad property, in the municipality located within the district ~~as of October 1 of the year preceding the adjustment~~ in the comparison year, ~~less~~ and

(ii) The aggregate true value of said property in the base year.

(2) Aggregate true value of all taxable real property shall be determined by aggregating the assessed value of all real property within the district boundaries in each constituent municipality, ~~as the same may be modified by the county board of taxation upon appeal~~, and dividing said total by the average assessment ratio as promulgated by the Director of the Division of Taxation in the Department of the Treasury for State school aid purposes on October 1 of the respective years for which aggregate true value is to be determined, pursuant to P.L. 1954, c. 86, as amended,[1] as the

same may have been modified by the Division of Tax Appeals. . . .

(b) The amount payable to the intermunicipal account by each constituent municipality in any adjustment year shall be determined in the following manner: the apportionment rate calculated for the comparison year shall be multiplied by the increase, if any, in aggregate true value of taxable real property for such year; provided, however, that the amount payable to the intermunicipal account shall be limited to ten percent of the amount so calculated in the adjustment year 1973 and shall increase four percentage points a year until 50% of the amount so calculated is paid into the intermunicipal account in the adjustment year 1983 and thereafter. . . . .

13:17-68. Computation of guarantee payment payable by Intermunicipal account to each constituent municipality

(a) The guarantee payment payable by the intermunicipal account to each constituent municipality in any adjustment year shall be computed as follows:

(1) If there is a decrease in the aggregate true value of taxable real property of any constituent municipality, as determined pursuant to subsection (a) of section 65 of this act,[1] the commission shall, subject to the provision of subsection (b) of this section, calculate the amount of decreased aggregate true value, occurring in the comparison year, by reason of the acquisition, through purchase, eminent domain or gift, during the year preceding the comparison year, of taxable real property by a governmental body or agency to be used for a public purpose, whereby said taxable real property parcels or portions thereof became exempt from local real property taxes. Such decreased aggregate true value shall be calculated in the same manner as aggregate true value is determined pursuant to subsection (a) of section 65 of this act and shall be based on the assessed value in the year of acquisition, of the parcels or portions thereof affected.

(2) There shall be payable as a guarantee payment from the intermunicipal account to each municipality, an amount to be calculated by multiplying the lesser of

(i) the amount of the decrease in aggregate true value determined pursuant to subsection (a) of section 65 of this act and

(ii) the amount of the decrease, if any, in aggregate true value calculated to be attributable to conversion of taxable property to exempt status, specified in paragraph (1) of this subsection.

by the apportionment rate, as defined in subsection (g) of section 59.1 of this act,[2] determined for the comparison year. If, in any comparison year and with respect to any constituent municipality, no amount of decrease in aggregate true value is found to be attributable to the conversion from taxable to exempt status specified in paragraph (1) of this section, no guarantee payment shall be payable to such municipality in the applicable adjustment year. . . . .

13:17-70. School district services; determination of service payment

For school district services, the service payment payable by the intermunicipal account to any constituent municipality in any adjustment year shall be found by dividing:

(a) The total local school tax levy, as shown on the Table of Aggregates pursuant to R.S. 54:4-52 for the comparison ~~year preceding the adjustment year~~, by the

(b) School resident enrollment on September 30 of such comparison ~~year preceding the adjustment~~ year, as certified pursuant to section 63 of this act,[1] and multiplying the result by the increase, if any, in resident enrollment within the district boundaries of that constituent municipality between September 30, 1969 1970 and September 30 of the comparison ~~year preceding the adjustment~~ year.

13:17-72. Apportionment of balance among constituent municipalities; prohibition of payments to commission

(a) If, in any adjustment year, the amount payable to the constituent municipalities by the intermunicipal account for guarantee payments; and school district service payments, ~~and project payments, plus any payment to the reserve fund as provided in subsection (b) and the payment for the sum of administration of the intermunicipal account as provided by subsection (e)~~ is less than the amount payable to the intermunicipal account pursuant to section 65 of this act,[1] the balance, if any, shall be apportioned among the constituent municipalities in the same ratio as the ~~area of their unimproved and redeveloped lands~~ number of acres within the district of each constituent municipality bears to the total ~~of such unimproved and redeveloped lands~~ number of acres in the district, and shall be known as an apportionment payment. . . . .

13:17-73. Payment of excessive funds to constituent municipalities; reduction of service payments

If, in any adjustment year, the amount payable to the constituent municipalities by the intermunicipal account for guarantee payments; and service payments; and project payments, plus the cost of administering the intermunicipal account exceeds the amount payable to said account pursuant to section 65 of this act,[1] the reserve fund shall be drawn upon to make up the deficit. In the event there is an insufficient amount in the reserve fund, the total service payments payable to all constituent municipalities shall be reduced by the amount of the deficit and the service payment payable to each constituent municipality shall be reduced by the same ratio as the total service payment to all constituent municipalities was reduced. . . . .

L.1972, c. 404, § 71. Amended by L.1972, c. 103, § 10, eff. July 19, 1972.

Note that the New Jersey statute shares tax revenue, not the tax base. Is this an important difference? The plan uses "aggregate real value" of *all* property in determining contributions to the intermunicipal account. The inclusion of residential property will both increase the size of the annual pool, and, depending on how revenue is distributed, improve the potential of the plan for eliminating disparities. The major purpose of this statute is to distribute the tax benefits and burdens of the regional development plan and, as reflected in the distribution process, to compensate localities for the preservation of open space. Is this narrower purpose easier to achieve than the broad policy embraced by the Minnesota statute? Given that purpose, how significant is the inclusion of residential property? In terms of the benefit analysis of the Minnesota Supreme Court, the New Jersey plan focuses on more specific forms of interdependence—the provision and use of parks, open space, and schools. Does this require that residential property be included? The Minnesota court interpreted the statute as embracing a broader interdependence, including jobs and the location of economic activity.

How effective will the New Jersey plan prove in preserving open space? Each municipality contributes a sum equal to the product of the "apportionate rate"—the effective tax rate, excluding county expenses—and a percentage of the growth in the tax base. The fund is distributed in three steps. First, municipalities are compensated for tax revenue lost due to the acquisition of taxable property for open space, to the extent that the decrease in the tax base from such acquisitions is not offset by overall growth in the base. This is called the guarantee payment. Then, school district service payments are computed. Finally, any balance is distributed among communities.

How does the guarantee payment affect different types of municipalities? A rapidly growing community is unlikely to receive any guarantee payment for preserving open space, since such loss in the tax base should be fully offset by growth, though another community not experiencing significant growth but making an equal commitment to open space, will receive partial compensation. Which community is likely to have the greatest need for preserving land?

What incentive does the Minnesota plan give localities for preserving open space? Base sharing makes C/I activity less attractive, but it does not affect the incentives for seeking residential development. Yet it is residential development which creates the need for parkland.

C. Base-Sharing and Public Services

Thus far, we have considered only the revenue side of the fiscal aspects of base-sharing. Yet raising revenue is only a means to an end—providing residents with services. This, too, is the ultimate focus of the fiscal disparities issue. The school finance litigation, after all, was prompted by a wide divergence in the quality of education available to children from different municipalities. Tiebout's paradigm—a fragmented multiplicity of relatively small local governments offering a varied mix of services to satisfy the tastes of different groups of residents—represents, to some, the most efficient scheme of metropolitan organization. Yet its critics attack it for its fragmentation; independent local governments face no incentive to cooperate in addressing areawide problems. In addition, fragmentation rigidifies disparities in local resources and inequities in the provision of services. The apparent alternative is the consolidation of local service providers into a single metropolitan government. The price of uniformity is the loss of efficiency, and perhaps more importantly, local control. The concept of base-sharing emerged from this uncomfortable dilemma, as an attempt to alleviate the problems of fragmentation without the sacrifices required of metropolitan government. Does it represent a workable alternative? Does it supplant the need for areawide government or merely forestall it? These are the questions to be answered as the concept is formulated, implemented, evaluated, and reformulated by the legislatures of various states.

What will the effect of the statute be on the provision of services? Recall the differing approaches articulated by the courts as they grappled with the school finance problem. At one extreme, the majority in *San Antonio* chose to protect local autonomy—and presumably economic efficiency—at the expense of an equal level of services. Conversely, Justice Marshall's dissent and the majority in *Robinson* called for equal per-pupil expenditures, regardless of a locality's fiscal resources and preferences in allocating its tax revenues. Must one choose between these two extremes? Consider the dissent of Justice White, who challenged the majority's holding that inequalities were rationally related to the purpose of local control.

> Neither Texas nor the majority heeds this rule. If the State aims at maximizing local initiative and local choice, by permitting school districts to resort to the real property tax if they choose to do so, it utterly fails in achieving its purpose in districts with property tax bases so low that there is little if any opportunity for interested parents, rich or poor, to augment school district revenues. Requiring the State to establish only that unequal treatment is in furtherance of a permissible goal, without also requiring the State to show that the means chosen to effectuate that goal are rationally related to its achievement, makes equal protection analysis no more than an empty gesture.[6] In my view, the parents and children in Edgewood, and

in like districts, suffer from an invidious discrimination violative of the Equal Protection Clause.

This does not, of course, mean that local control may not be a legitimate goal of a school-financing system. Nor does it mean that the State must guarantee each district an equal per-pupil revenue from the state school-financing system. Nor does it mean, as the majority appears to believe, that, by affirming the decision below, this Court would be "imposing on the States inflexible constitutional restraints that could circumscribe or handicap the continued research and experimentation so vital to finding even partial solutions to educational problems and to keeping abreast of ever-changing conditions." On the contrary, it would merely mean that the State must fashion a financing scheme which provides a rational basis for the maximization of local control, if local control is to remain a goal of the system, and not a scheme with "different treatment be[ing] accorded to persons placed by a statute into different classes on the basis of criteria wholly unrelated to the objective of that statute," *Reed v. Reed*, 404 U.S. 71, 75-76 (1971).

411 U.S. 1, 68-69.

How does base sharing fit into this scheme? Will the Fiscal Disparities Act increase the variety of public services provided by local governments, or will it curtail the range of choice available to metropolitan residents? Does it provide a method for satisfying the dissenters' objections with the *San Antonio* result without imposing the uniformity feared by the majority?

In discussing the impact of the Act on the provision of public services, consideration must go beyond the question whether the Act will indeed have its anticipated effect on the ability of local governments to provide these services. The Fiscal Disparities Act expressly relies on existing local governmental structure and local decisionmaking; in effect, local governments retain discretion in both the raising and the spending of revenues received from the area-wide tax base. Because of this discretion, any increased ability to raise revenues for public services which results from the operation of the Act will not necessarily be converted into such services. Whether a governmental unit which loses under the Act will raise its tax rate to restore the previous level of expenditures for public services or simply reduce the quantum of those services is not controlled by the Act.[94] And a unit which gains under the Act could choose to lower its tax rate or spend the funds on other projects, rather than increase its level of public services.

Thus, if the Act is successful in reducing fiscal disparities, its effect will be to remove the size of the local tax base as a determining factor in local governmental spending decisions, allowing other considerations to be given more weight. The Act thereby enables a governmental unit to fund public services in an amount based to a greater degree on the unit's preference for those services. In this way, the Act tends to equalize the resources of communities, while allowing them the freedom to use their equalized resources as they see fit.

R. Freilich, "Minnesota's Metropolitan Fiscal Disparities Act. . . .," 59 Minnesota Law Review 927, 951-952 (1975).

Is Freilich's approach sufficiently comprehensive to be credible? Certainly net recipients will be more free to fund services according to preference, but what of net contributors? What does the sharing of *growth* have to do with this? Aren't preferences relative to resources, so net contributors are restricted? Within the constraints of the size of the total tax base, though, base sharing does not impose any restrictions on how local governments allocate their resources;

even if the tax base were equalized, disparities in per-capita expenditures could persist. Politically, does this make base sharing more or less acceptable than metropolitan government? Is it an alternative or a compromise?

IV. CONCLUSION

As yet, no states except Minnesota and New Jersey have adopted base-sharing plans, although several—California, Maryland, Michigan, Virginia, Pennsylvania and Alberta, Canada—have considered legislation. Several factors have impeded acceptance, but by far the most significant is the conflict between the property-rich and the property-poor jurisdictions. Base-sharing is by its very nature redistributive, and it is so perceived. This is, perhaps, its tragic flaw: for all its potential in redressing disparities and rationalizing the land use planning process, unless and until local governments face some incentive—from within or without—to work together on regional problems, and for as long as political power resides with wealth, supporters of base-sharing face an uphill fight in state legislatures. Yet, as the Minnesota experience indicates, the interdependencies, and the potential for cooperation, exist.

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