

STATEMENT OF ALBERT SHANKER, PRESIDENT
AMERICAN FEDERATION OF TEACHERS, AFL-CIO
TO THE HOUSE COMMITTEE ON WAYS & MEANS
ON TAX SIMPLIFICATION LEGISLATION
June 12, 1985

Mr. Chairman, Members of the Committee:

Thank you on behalf of the 610,000 members of the American Federation of Teachers for this opportunity to testify. I will use this occasion to call the Committee's attention to some of the implications President Reagan's tax plan has for public education.

In the opinion of the AFT, the President's tax plan as presented to the Congress will do more harm than good. As we view the elements of the new proposed tax plan, we find President Reagan seeks a continuation of most of the tax preferences enacted in 1981. In addition, the 1985 tax plan would have the effect of severely hamstringing education reform efforts by eliminating the deductibility of taxes paid to state and local governments.

It is important to note that education reform and improvement is now a national issue. This has happened in part because of the efforts President Reagan made in 1983 to call attention to our educational shortcomings. Some of us who had been attempting to focus the nation's attention on the need to improve education welcomed the President's leadership. The AFT invited President Reagan to present his view on education reform to our 1983 convention. The President made a compelling case for education reform as a national issue. Mr. Reagan, however, does not believe that the federal government should pay any of the costs for education reform.

By and large, states and localities have borne the burden of financing school improvements. Federal cutbacks have been enacted across the board for federal programs that aid state and local governments, yet support for education has increased. The taxpayers have been willing to shoulder the cost of increased education spending in return for improvements in education policies. We, in the AFT fear that if federal deductibility of state and local taxes is lost the efforts now underway to improve education will be stymied. Loss of deductibility could cause a serious erosion in education's tax base.

Most of the testimony that this Committee will receive will be based upon projections of conditions that may result from one change or another in tax policy. For state and local governments we must rely upon the so called "tax price" method of calculating the effects that loss of deductibility would have on the ability of state and local government to finance education.

Since 1956, when Mr. Charles Tiebout published an article

entitled, "A Pure Theory of Local Expenditures" in The Journal of Political Economy, "tax price" has been a key concept in public finance literature. The Tiebout model envisions taxpayers "voting with their feet" to find the package of services and taxes that suit their desires. This model has been challenged over the years but no one doubts that government services carry an identifiable price. High officials in the Treasury Department have been known to talk about voters/taxpayers "voting with their feet" to avoid paying high state and local taxes.

The method of calculating the true price of services goes relatively unchallenged: The national average marginal rate under current law is about 28%. Nationwide, under current law, the average itemizing taxpayer pays the following "tax price" for state and local services.

T.P. = \$1 (1 marginal tax rate)
 T.P. = \$1 (1- .28)
 T.P. = \$0.72

The average itemizing taxpayer is paying \$.72 for every dollar received in state and local services. Loss of federal deductibility would mean that itemizing taxpayers would be paying full price for the same services. The loss of deductibility would therefore cause a perception of a sharp increase in the tax price of services such as education. Other favorable developments such as lower rates would not offset the perception that state and local taxes would be sharply higher. The following result would occur:

Current law "tax price"	\$.72
State and Local Services	
Treasury Tax Plan:	
New Tax Price for	
S&L Services:	\$1.00
Perceived Increase	
"tax price"	.28
Percentage Increase	
in "tax price":	.28/.72 = 39%

Some generally accepted guidelines exist for calculating the effect of a 39% increase in the real property tax price. Although there are variations, the Congressional Research Service maintains that "price elasticity" for state and local services is about -0.5. This means that over time voters are likely to respond to a 39% increase in a tax price by demanding that it be cut in half.

If this expectation is accurate we can anticipate a 20% cut in revenue for education. A revenue cut of that magnitude would certainly result in a similar spending cut.

Because education is still heavily financed by the property tax the "tax price" theory is easily applied. Other public services which depend on state income or sales taxes might not be so subject to "tax price" sensitivity and it is possible that base broadening in the Reagan plan could offset losses. We do know that increasing the tax price will result in a reduction of spending at all levels of government. The Advisory Committee on Intergovernmental Relations states that local property taxes pay for about half of the state and local cost of elementary and secondary education. The federal government pays about 7%.

I have attached charts at the end of this statement estimating the effects of increased tax prices on education revenues by state and per student. These charts were prepared by the office of Senator Daniel Patrick Moynihan of New York. We can see from these charts that loss of deductibility could produce a real crisis in education financing.

The President and Treasury Department have made elimination of deductibility for state and local taxes their number one priority. Presidential Assistant Patrick Buchanan has stated that the elimination of deductibility is aimed at the "neo-socialist" states of the Northeast. The President's plan however, is loaded with tax references for politically powerful elements in the private sector. President Reagan would have us believe that "reform" now depends on more sacrifices from the public sector. This is Mr. Reagan's preference, not a true statement of fact. This current opportunity for tax simplification should not become a contest between public and private needs. It is necessary, however, to point out that the President's philosophy seems to be that economic growth and prosperity must come at the expense of the public sector. The AFT believes that quality education, good mass transit, health care and transportation are indispensable to national economic growth and prosperity. Loss of deductibility will impact negatively on all elements of the public sector. It has become clear over the last few years that the availability of public services, especially education, is an important consideration in decisions made by business leaders. A healthy public sector is just as important as a healthy private sector in the equations of economic growth. The Reagan Administration has stated that rate reduction is impossible without the \$38 billion in revenue taken from the public sector through the elimination of deductibility for state and local taxes. We believe that it is very possible to have a tax reform bill and maintain deductions for state and local taxes.

AFL-CIO President Lane Kirkland has presented testimony to this Committee that outlines where revenues can be found to fund tax rate reductions. The AFT endorses the AFL-CIO proposals as the best way to not only reduce tax rates, but restore a measure of equity to the federal tax code.

Like the AFL-CIO, the AFT believes that other elements of

the Reagan tax plan must be revised by the Congress. The proposed new taxes on life support benefits such as health insurance, workers compensation, black lung and death benefits are totally wrong and should be rejected by the Committee. The AFT also opposes the Administration's plan to further tax unemployment compensation.

As I stated earlier, the Administration's plan is not a step forward for most American citizens. Reduction of the maximum rate from 50 - 35% is not a step that helps many citizens. It is especially wrong to use revenues gained from taxing life support benefits to reduce the tax burden on the very rich.

The AFT urges the Congress to pass a fair tax bill. Passage of such a bill will depend upon the determination of the Congress to confront the real special interests in the tax code. State and local tax deductions are not a special interest, rather they are a key to improving education and many other public sector contributions to our nation's economic growth. Retaining federal deductibility preserves the principle that we should not be required to pay taxes on taxes legally levied by other levels of government.

The tax bill before you sacrifices the public interest for private purposes. In the area of education, the Reagan bill establishes a backdoor method of paying for private schools at the expense of public schools. By eliminating the deductibility of public education taxes and allowing the deductibility of private charitable contributions the President's tax plan would provide favored treatment to private schools. Many parochial schools are funded in part by tuition and in part by tax deductible contributions to churches. The AFT does not oppose the allowances in the President's bill for charitable giving, just as we did not oppose allowing non-itemizers to claim a charitable deduction in the 1981 tax bill. We only wish to point out that if deductibility of state and local taxes is lost, a massive inequity will be created as support for private education stays tax deductible while support for public education becomes taxable.

Federal support for all public education through deductibility amounts to approximately \$16.5 billion according to a survey done by the AFT. If this federal support is lost, state and local taxpayers will be required to increase their tax liability by an amount greater than the budget for the U.S. Department of Education as proposed by the President for F.Y. 1986. As education loses tax support, loopholes for the oil industry and for the corporate sector go unchallenged. Ironically, private sector education will benefit from charitable giving, while public schools will have to endure a 20% decline in property tax support. This is the unexamined impact of the President's tax plan.

I urge this committee to correct the inequities in President Reagan's tax bill and to make sure that the Federal Government does no harm to education's tax base. A true tax simplification and equity measure is within reach of the Congress. President Reagan's tax bill is not a step in the direction of equity. I urge you to draft a bill that respects the federal system and provides tax equity for all our citizens in the public and private sector.

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