

# UTAH'S TAX SITUATION

## HIGHLIGHTS

- Considering all taxes and fees (local, state and federal), Utah ranks very near the 50-state average for tax burden, at #28.
- This average ranking is the combination of relatively high state taxes and fees and relatively low local and federal taxes and fees.
- The bulk of Utah's tax revenue is divided among three main taxes, general sales-and-use, personal income, and property.
- Utah is one of many states adopting the Streamlined Sales Tax, a method for collecting sales-and-use taxes on items that often went untaxed, particularly catalog, mail order and internet sales. Utah merchants will implement the new procedures beginning July 1, 2004.

## DID YOU KNOW?

- Utah is one of 17 states that operate a liquor monopoly. All profits from state-owned ABC (Alcoholic Beverage Control) stores go to the state's general fund.
- When inflation is considered, Utah's Motor Fuel Tax is less today than when it was instituted. So, incidentally, is the price of a gallon of gasoline.

Utah Foundation is a nonprofit, nonadvocacy research organization. Our mission is to encourage informed public policy making and to serve as Utah's trusted source for independent, objective research on crucial public policy issues.

D. Douglas Larson, President  
Alan K. Allred, Vice President  
Stephen J. Kroes, Executive Director  
Janice Houston, Director of Research

1414 Highland Dr., Suite 102  
Salt Lake City, UT 84124  
(801) 272-8824 • www.utahfoundation.org

Although Utah's tax system is fairly typical in relying on a balance of property, income, and sales taxes, Utah does have some unique tax policies that set it apart from many states. Most notable is that Utah earmarks 100% of income tax revenues for education funding.

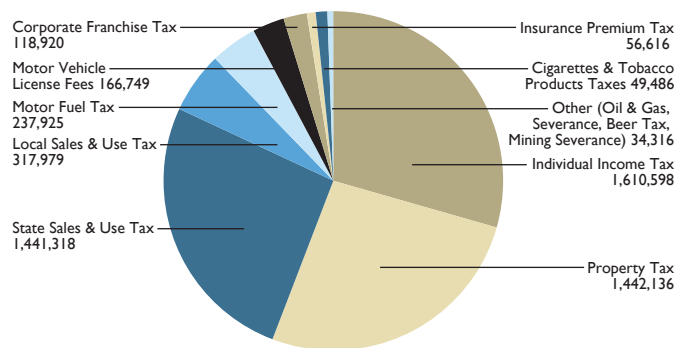
Another important feature of Utah's tax system is the "truth in taxation" law that has resulted in a low property tax burden. And currently, the sales tax is undergoing significant changes designed to make it easier to collect tax on mail-order and internet sales.

Property, personal income, and sales taxes produce 82% of Utah's total state and local tax revenue. This combination of three major taxes with several minor ones provides an income source for government that is more stable than a system that relies heavily on any one tax. Figure 1 shows the sources of state and local tax revenue for 2002, during which sales, property, and personal income tax generated about \$5 billion.

## UTAH'S TAX BURDEN

Measuring tax burden can be a complicated task. One issue to consider is whether to measure the burden per capita (dividing tax revenues by population) or to use a measure that expresses the burden in proportion to income. For this report, Utah Foundation will measure the tax burden in proportion to income. This method more clearly illustrates the financial load placed on residents and businesses to pay for government services. Per capita measurements can easily appear skewed as the result of various factors, such as Utah's large child population as compared to other states.

Figure 1: Utah State & Local Taxes, 2002 (in Thousands)



Another important issue is to decide which taxes or revenues to use as the basis for the comparison. Utah Foundation will use taxes and fees as reported to the Bureau of the Census for this report. Using the Census Bureau provides a standardized set of data for comparison to other states. In addition, including fees has become increasingly important over the last 25 years as a result of government agencies moving to greater fee funding to supplement tax funding.

This report will show that Utah has a high state tax burden, a low local tax burden, and a low federal tax burden. Collectively, these combine to an overall moderate tax burden.

### STATE TAXES AND FEES

As shown in Figure 2, Utah's state tax burden ranks 8th highest in the nation. This is partly the result of funding public education for Utah's substantial student population. Utah's average family size is the largest in the nation, resulting in a large student population and heavy demands on the tax system to fund the education system. Utah's student-age population (ages 5-17) is 20% larger than would be expected for an average state.

**Figure 2: Total Taxes & Fees Per \$1,000 Personal Income**

Mountain States	State Taxes & Fees	National Rank	Local Taxes & Fees	National Rank	State & Local Combined	National Rank
Wyoming	\$78.51	29	\$76.28	3	\$154.80	8
Nevada	69.54	39	58.97	15	128.51	37
New Mexico	114.98	3	41.30	46	156.28	4
Colorado	61.70	47	64.92	6	126.62	40
<b>Utah</b>	<b>99.50</b>	<b>8</b>	<b>51.12</b>	<b>40</b>	<b>150.62</b>	<b>11</b>
Montana	87.26	18	54.53	28	141.79	20
Idaho	90.57	16	54.07	32	144.64	19
Arizona	70.32	38	55.72	24	126.04	43

Mountain States	Federal Taxes & Fees	National Rank	State, Local & Federal Combined	National Rank
Wyoming	\$275.13	3	\$429.93	1
Nevada	260.33	9	388.85	13
New Mexico	229.60	33	385.88	14
Colorado	257.42	11	384.04	16
<b>Utah</b>	<b>221.99</b>	<b>40</b>	<b>372.60</b>	<b>28</b>
Montana	227.74	36	369.53	30
Idaho	223.54	38	368.18	32
Arizona	240.54	21	366.58	34

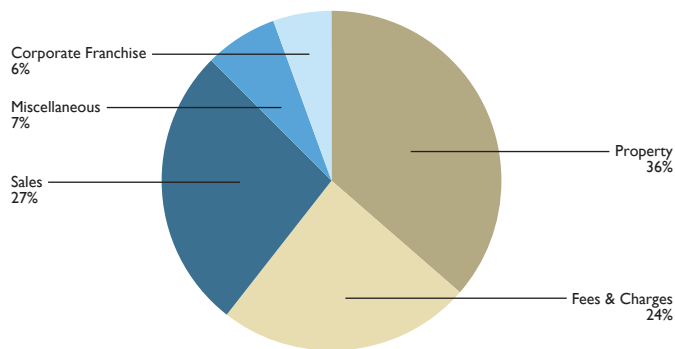
Source: Bureau of the Census, Bureau of Economic Analysis (BEA), Tax Foundation; Calculations by Utah Foundation

### LOCAL TAXES AND FEES

Local governments, including cities, towns, counties, special districts and multipurpose districts receive most of their revenue from local sales taxes (all 29 counties levy the maximum 1% sales tax). Property taxes also comprise a significant portion of local revenues. Figure 3 provides a breakdown of the percentage of local tax revenue by type of tax.

Taxes levied by Utah's local governments are lower than the national average. The Mountain States vary widely, ranging from very low to very high local burdens. A comparison between the local and state tax-and-fee burden shown in Figure 2 shows that states with low local burdens have high state burdens, and vice versa.

**Figure 3: Utah State & Local Taxes, 2002 (in Thousands)**



Source: Utah League of Cities & Towns; Utah State Auditor's Office; Calculations by Utah Foundation

### STATE AND LOCAL TAX-AND-FEE BURDEN

Utah's state and local tax-and-fee burdens translate to about \$151 of every \$1,000 of personal income earned in the state going to pay taxes and government fees. In other words, about 15.1% of personal income is dedicated to paying these taxes and fees. This is the 11th highest in the nation. This is up from 14th according to research that was done by Utah Foundation just a few years ago.

### FEDERAL TAX BURDEN

Utah's federal tax burden is lower than the national average. At \$222 per \$1,000 of personal income, federal taxes paid by Utah residents and businesses rank 40th highest in the nation. This is most likely the result of Utah's larger families (more child tax deductions and credits), high charitable contributions, and lower incomes. Figure 2 highlights the federal tax burden for Utah and the mountain states and provides the national ranks for those states.

It is also interesting to note that Utah pays less to the federal government than it receives back in federal spending, according to a study in the late 1990s by Harvard's Taubman Center for Local and State Government and Senator Daniel Patrick Moynihan. In 1999, Utah paid \$4,034 per capita to the federal government and received back \$4,324. Nationwide, New Mexico received the most money from the federal government for the money it paid (\$4,048 vs. \$7,992), and Connecticut received the least (\$8,064 vs. \$5,224).

For Utahns, the combined total paid to all levels of government is about 37% of personal income. This translates to a moderate overall tax burden, ranking 28th highest in the nation.

### AN OVERVIEW OF UTAH'S MAJOR TAXES

The property tax in Utah has diminished in comparison to other taxes over the past 20 years. It was once the primary source of state and local government revenue, but now comprises only about 26% of state and local taxes and fees. It has never been a popular tax, though it does provide a very stable source of revenue for government. Figure 4 compares property taxes per \$1,000 of personal income for Utah and other states in the Intermountain West as well as providing the national rank for Utah and its neighbors.

**Figure 4: Property Tax**

Mountain States	Per \$1,000 Personal Income	National Rank
1. Montana	\$45.33	6
2. Wyoming	37.87	11
3. Arizona	30.74	23
4. Idaho	28.65	29
5. Colorado	26.98	34
6. <b>Utah</b>	<b>25.28</b>	<b>36</b>
7. Nevada	24.34	39
8. New Mexico	15.84	50

Source: Census, BEA; Calculations by Utah Foundation

In 1985, the Legislature passed the Tax Increase Disclosure Act, more commonly known as “Truth in Taxation.” This law changed the level of property assessment, revised the way tax rates are expressed, and required public notice and hearings whenever a taxing entity intended to raise property tax revenues, even if the increase was due to inflation or normal appreciation of property. In other words, when aggregate property values rise, the accompanying tax rate must be adjusted so that the overall tax charge remains constant; any exception to this procedure requires a local agency to post a notice of public hearing to raise taxes. As a result, fearing negative reactions to such notices, many local governments have looked to other sources, such as impact fees and sales taxes to replace property tax revenue lost to inflation.

Sales tax is perhaps the most unobtrusive to taxpayers because it is paid in hundreds of small transactions. Sales tax also draws revenue from almost all citizens, including visitors to the state, which allows for a broader tax base. It is a regressive tax, however, forcing the poor to spend a larger percentage of their income on essential items that are taxable.

Utah relies heavily on the sales tax, relative to some other Mountain States, as shown in Figure 5. This heavy reliance on sales taxes can be problematic, because the tax grows slower than long-term economic growth, and because the U.S. economy is moving to a greater consumption of services compared to taxable tangible goods.

**Figure 5: General Sales Tax**

Mountain States	Per \$1,000 Personal Income	National Rank
1. New Mexico	\$47.69	2
2. Arizona	38.20	8
3. <b>Utah</b>	<b>35.72</b>	<b>9</b>
4. Nevada	34.90	11
5. Wyoming	34.27	12
6. Colorado	27.68	22
7. Idaho	24.68	32
8. Montana	0.00	48

Source: Census, BEA; Calculations by Utah Foundation

Utah’s individual income tax is the highest of all the Mountain States, and about 15th highest nationally as shown by Figure 6. Most Mountain states are below average in individual income tax burdens, suggesting a general disfavor in the region for the tax.

**Figure 6: Individual Income Tax**

Mountain States	Per \$1,000 Personal Income	National Rank
1. <b>Utah</b>	<b>\$32.04</b>	<b>15</b>
2. Idaho	31.90	16
3. Colorado	26.66	22
4. Montana	25.77	28
5. New Mexico	22.49	36
6. Arizona	18.04	39
7. Nevada	0.00	45
8. Wyoming	0.00	45

In Utah, and in nine other states, the highest income tax bracket begins at less than \$10,000 in taxable income for single filers. This makes the income tax essentially a flat tax, and negates its nominally progressive structure.

Utah corporate income or corporate franchise tax collections are slightly lower than average. As with the personal income tax, the Mountain states do not rely on these taxes as heavily as the rest of the country. Two of Utah’s neighbors, Wyoming and Nevada, do not levy a corporate income tax at all. A comparison of this tax is provided in Figure 7.

**Figure 7: Corporate Income Tax**

Mountain States	Per \$1,000 Personal Income	National Rank
1. Montana	\$4.98	15
2. Idaho	4.16	21
3. Arizona	4.12	23
4. New Mexico	4.07	24
5. <b>Utah</b>	<b>3.37</b>	<b>28</b>
6. Colorado	2.46	39
7. Nevada	0.00	48
8. Wyoming	0.00	48

Source: Census, BEA; Calculations by Utah Foundation

Below is a broader discussion of Utah’s taxes.

**PROPERTY TAX**

In 2002, property taxes generated 26% of taxes raised by Utah state and local governments. Property taxes are levied on all residential and commercial property not exempted by law. Primary home owners in Utah enjoy a significant exemption on their property taxes. In 1982, voters authorized the exemption of up to 45% of the value of primary residences. The exemption began at 25% (75% taxable) and

**Figure 8: Timeline of Utah’s Primary Residence Exemption**

Year(s)	Primary Residential Exemption	Taxable Value as Percent of Market Value
1983 - 1990	25%	75%
1991	29.75%	70.25%
1992 - 1993	29.50%	70.50%
1994	32%	68%
1995 - 2004	45%	55%

Source: Utah Tax Commission

gradually expanded to the full 45% (55% taxable), where it remains today. Figure 8 details the timeline of this exemption.

### PROPERTY TAXES AND SCHOOL DISTRICTS

In recent years, the state has not directly levied a property tax. It does require, however, that local districts impose a uniform local levy for school purposes.

This state-mandated local school levy, which for FY 2004-05 is legislated at .001754 per \$1.00 of taxable value, is one of the factors that determine the amount of state aid that a local district will receive under the minimum school program. The formula for calculating the amount of revenue in each district's minimum school basic program begins by providing each district a state-guaranteed amount. From this the basic rate or the local property tax revenue is subtracted. The difference is then provided to each district from the Uniform School Fund. For districts that have large property tax revenues, the possible impact of this formula may be such that they actually send some of their property tax funds to the state to be reallocated. Figure 9 explains this scenario using an example from the Utah State Office of Education. District A is a recipient of state Uniform School Funds, while District B gives the state \$10,500 to be reallocated to other districts. However, as the Utah State Office of Education notes, the 1995 Legislature significantly reduced the Basic Rate levy and subsequent legislatures have reduced it further. Since that initial reduction, no school district has had to forfeit local property tax revenues to be reallocated.

**Figure 9: Hypothetical Reallocation of Local Property Tax Revenue**

District A		District B	
1,000 WPU's 0.000100 Tax Rate =	\$12,500	1,000 WPU's 0.000100 Tax Rate =	\$125,000
1,000 WPU's * \$2,182 =	\$2,182,000	1,000 WPU's * \$2,182 =	\$2,182,000
Minus Tax Revenue 0.0001754	\$219,250	Minus Tax Revenue 0.0001754	\$2,192,500
Shortfall Need & Local Ability	\$1,962,750	Shortfall Need & Local Ability	(\$10,500)
State Gives District	\$1,962,750	District Gives State	\$10,500
District Revenue MSP	\$2,182,000	District Revenue MSP	\$2,182,000

Source: Utah State Office of Education

Beyond the minimum school program basic rate, Utah school districts can levy additional property taxes for operations and capital expenses. The state plays a role in local school building funds through the Capital Outlay Foundation Program. In order to qualify for full participation in the program, local districts must have a capital projects and debt service property tax rate of at least .002400 per dollar of taxable value. If a district levies less than that amount, the proportion of state capital outlay money is reduced accordingly.

The purpose of state involvement in local school district property tax funding is an effort to eliminate the disparity between wealthy and poor districts' ability to fund public education. This concept is known as equalization and Utah does an adequate job of reallocating

funds relative to other states. Some states, such as Arizona and Wyoming, have been embroiled in lawsuits because operations or capital funding for school districts within those states varies greatly between districts.

In addition to these two primary components, local districts have the ability to levy property taxes for any of the following, subject to a vote by the residents of the district or by the district's school board:

- Voted Leeway/Board Leeway
- Reading Achievement Board Leeway Levy
- 10% of Basic
- Voted Capital
- Tort Liability
- Transportation
- Recreation

### INDIVIDUAL INCOME TAX

Taxes on individual income provide the largest single source of tax revenue for Utah state government. In 2002, individual income taxes accounted for about 30% of all state and local tax revenue.

The Utah Legislature adopted the individual income tax in 1931. From the beginning, both individual and corporate income taxes have been used only for public education. In 1996, voters approved a constitutional amendment to allow higher education to also be funded by income tax revenues; accordingly, some income tax revenues are diverted to Higher Education prior to being deposited in the Uniform School Fund.

**Figure 10: Utah Income Tax Brackets, 2004**

State Taxable Income	Single & Married Filing Separate	Head of Household & Filing Jointly
\$0 to \$863	2.3% of state taxable income	2.3% of state taxable income
\$864 to \$1,726	\$20, plus 3.3% of amount over \$863	2.3% of state taxable income
\$1,727 to \$2,588	\$48, plus 4.2% of amount over \$1,726	\$40, plus 3.3% of amount over \$1,726
\$2,589 to \$3,450	\$85, plus 5.2% of amount over \$2,588	\$40, plus 3.3% of amount over \$1,726
\$3,451 to \$4,313	\$129, plus 6.0% of amount over \$3,450	\$97, plus 4.2% of amount over \$3,450
Over \$4,313	\$181, plus 7.0% of amount over \$4,313	\$97, plus 4.2% of amount over \$3,450
\$3,451 to \$5,176		\$97, plus 4.2% of amount over \$3,450
\$5,177 to \$6,900		\$169 plus 5.2% of amount over \$5,176
\$6,901 to \$8,626		\$259 plus 6.0% of amount over \$6,900
Over \$8,626		\$362 plus 7.0% of amount over \$8,626

Source: Utah Tax Commission

The personal income tax in Utah is divided into 6 brackets as shown in Figure 10. The top bracket in 1931 was \$8,000. Four years later, in an effort to increase the income tax yield, the Legislature increased the tax rates and eliminated the top three brackets.

In 1973, separate brackets were created for single or married filing separate and married filing joint. For simplicity, only the brackets and rates for married filing joint are shown here. In 2001, the Legislature raised the 1973 threshold for each bracket by 15%. The result of this is that Utah's tax brackets now look surprisingly similar to their 1935 counterparts, even though residents' incomes have grown significantly since then. The highest single bracket is now \$4,313 (a 13% lower threshold than in 1935), and the highest married filing joint bracket is \$8,626 (a 72% higher threshold than in 1935). By comparison, the consumer price index of inflation increased by 1192% between 1935 and 2001. A \$5,000 taxable income in 1935 was the equivalent of a taxable income of \$64,635 in 2001. These low brackets mean that Utah's income tax is essentially a flat tax, because inflation has pushed most taxpayers into the highest bracket. A single filer working full time at minimum wage pays the same percentage of income tax on his/her wages as does a single filer earning \$100,000.

Nationally, thirteen states have provisions to automatically adjust brackets, personal exemptions or standard deductions for inflation. Utah is not one of them. Greater than 80% of all single filers and greater than 95% of all married joint filers are in the highest bracket. However, Utah is not unique here. Two states have a true flat tax with no exemptions, four more have a flat tax with exemptions, and an additional nine states have top single brackets at or below \$10,000, making them essentially flat taxes.

In addition to changing the brackets, there are two other ways that states can adjust the impact of their income tax. The first is by changing the tax rates. Figure 11 shows the changes in the income tax rate, beginning with the initial 1931 rate, and including the most recent 1981 change. The rates increased with each change, except for the last.

**Figure 11: Utah Income Tax Rate Changes**

Brackets	1931	1935	1965	Brackets	1973	1975	1981	Brackets	2004
\$1000	1.00%	1.00%	2.00%	\$1,500	2.50%	3.00%	2.75%	\$1,727	2.30%
2,000	1.25%	2.00%	3.00%	3,000	3.50%	4.00%	3.75%	3,450	3.30%
3,000	1.50%	3.00%	4.00%	4,500	4.50%	5.00%	4.75%	5,176	4.20%
4,000	1.75%	4.00%	5.00%	6,000	5.50%	6.00%	5.75%	6,900	5.20%
5,000	2.00%	5.00%	6.00%	7,500	6.50%	7.00%	6.75%	8,626	6.00%
6,000	2.50%		6.50%	7,500+	7.25%	8.00%	7.75%	8,626+	7.00%
7,000	3.00%								
8,000	3.50%								
8,000+	4.00%								

Source: Financing Government in Utah, Utah Foundation

The second way that states can adjust the impact of their income tax is by allowing personal exemptions, as shown in Figure 12. Most of the states, including Utah, have proportional exemptions. This means that

**Figure 12: National Comparison of Income Tax Structure**

States without an Income Tax	States with Unique Income Tax Structure	States with Top Bracket Below \$10,000	States that Index for Inflation	States with Nonproportional Exemptions	States that allow Federal Tax Deductions
Alaska	Colorado <sup>1</sup>	Alabama	Arkansas	Alabama	Alabama
Florida	New Hampshire <sup>2</sup>	Connecticut	California	Arizona	Iowa
Nevada	Pennsylvania <sup>1</sup>	Georgia	Idaho	California	Louisiana
South Dakota	Rhode Island <sup>3</sup>	Kentucky	Iowa	Connecticut	Missouri <sup>4</sup>
Texas	Tennessee <sup>2</sup>	Maryland	Maine	Louisiana	Montana
Washington		Mississippi	Michigan	Maine	Oklahoma <sup>4</sup>
Wyoming		Missouri	Minnesota	Massachusetts	Oregon <sup>4</sup>
		Oklahoma	Montana	Mississippi	Utah <sup>5</sup>
		Oregon	Nebraska	New Jersey	New Jersey
		Utah	Ohio	New York	New York
			Oregon	Wisconsin	Wisconsin
			South Carolina		
			Vermont		

Source: Federation of Tax Administrators

- (1) Flat
- (2) Dividends & interest taxable only
- (3) 25% of Federal tax liability
- (4) Deduction is limited to \$10,000 for joint returns and \$5,000 for individuals in Missouri and to \$5,000 in Oregon
- (5) Allows 1/2 of Federal taxes to be deducted

the exemption for a married couple is double that of a single person, and each child is exempted at the rate of a single person. In Utah, singles can take a \$2,325 exemption, married couples a \$4,650 exemption, and an exemption of \$2,325 can be taken for each child.

There are ten states that have nonproportional brackets. In Connecticut, in 2004, a single filer receives an exemption of \$12,500, the largest in the country. Married filers also receive the largest exemption in the country at \$24,000, though this is slightly less than double, resulting in a marriage penalty since a couple cohabitating but filing separately will receive a total of \$25,000 in exemptions. Notably, Connecticut is also the only state that does not offer an exemption for children. There are six additional states that have a lower exemption for children than singles. This contrasts with four states that have exemptions in favor of children.

**SALES-AND-USE TAX**

In 2003, state sales-and-use taxes generated \$1.441 billion, or 26% of Utah's overall state and local taxes. That made it the second largest source of tax revenue for the state. Local sales-and-use taxes generated another \$318 million, or approximately 6% of all state and local taxes.

**LOCAL SALES TAX**

Beginning in 1959, Utah's counties and municipalities were authorized by the state Legislature to charge their own sales-and-use tax. The local governments can set the level of the tax, subject to voter approval and other tax-levying requirements, up to a maximum of 1%. The state administers the collection and distribution of the tax, retaining up to 2.5% to cover expenses.

As Figure 13 shows, Emery and Millard County share the state's lowest overall state and local sales tax rate and Garfield County claims the highest overall rate. Rates for individual cities can be found at the Tax Commission's website: <http://www.tax.utah.gov/sales/rates.html>.

**Figure 13: County Sales Tax Rates**

County	Tax Rate	County	Tax Rate	County	Tax Rate	County	Tax Rate
Beaver	6.00%	Garfield	7.00%	Piute	6.00%	Tooele	6.00%
Box Elder	6.00%	Grand	6.00%	Rich	6.00%	Uintah	6.50%
Cache	6.10%	Iron	6.00%	Salt Lake	6.60%	Utah	6.00%
Carbon	6.00%	Juab	6.00%	San Juan	6.00%	Wasatch	6.00%
Daggett	6.00%	Kane	6.75%	Sanpete	6.00%	Washington	6.00%
Davis	6.50%	Millard	5.75%	Sevier	6.00%	Wayne	6.00%
Duschene	6.00%	Morgan	6.00%	Summitt	6.10%	Weber	6.50%
Emery	5.75%						

In Box Elder, Cache, Summitt, Tooele, Utah, and Washington Counties, some cities add an additional 0.25% Mass Transit tax.

Source: Utah Tax Commission

### OTHER LOCAL APPORTIONED SALES TAXES

Beyond state and local sales taxes for general use, Utah municipalities and counties may choose to levy any number of local option taxes, subject to voter approval. A brief discussion of some of these options will be discussed below.

- Mass transit
- Rural hospitals
- Botanical, Cultural and Zoological (commonly know as a ZAP tax)
- Highways
- County option
- Town option
- Transient Room Tax
- Resort Communities
- Restaurant Tax
- Rural County Health Care Facilities
- Short-Term Motor Vehicle Leasing
- Tourism Tax

### MASS TRANSIT

Mass transit local option sales taxes of one quarter of one percent are levied by cities in Box Elder, Cache, Summitt, Tooele, Utah, and Wasatch counties to pay for public transit projects. Residents in Salt Lake, Davis, and Weber counties recently agreed to increase their transit tax to one half of one percent. Transit taxes in these three counties are levied by all incorporated municipalities as well as by the counties for unincorporated areas. According to data from the Utah State Tax Commission, mass transit taxes have generated \$101.7 million year-to-date for the fiscal year.

### TRANSIENT ROOM TAX

First approved by the Legislature in 1965, the Transient Room Tax allows all counties to charge a percentage of certified accommodation charges. Charges for accommodation of less than thirty days at hotels, motels, motor courts, etc. are eligible for the tax. The revenues from the tax must be used for the purposes of:

*establishing and promoting recreation, tourism, film production, and conventions; acquiring, leasing, constructing, furnishing, or operating convention meeting rooms, exhibit halls, visitor information centers, museums, and related facilities; acquiring or leasing land required for or related to the purposes listed [above]; and as required to mitigate the impacts of recreation, tourism, or conventions in counties of the fourth, fifth, and sixth class, paying for: solid waste disposal operations; emergency medical services; search and rescue activities; and law enforcement activities. (Utah Code Annotated, Section 17-31-2)*

All 29 counties in Utah charge the maximum 3%. The state collects and then returns the tax for all counties, except Grand County, which collects the tax on its own.

### RESORT COMMUNITY TAX

Some resort cities and towns are eligible to charge an additional general sales tax known as the Resort Community Tax. This tax was first approved by the Legislature in 1988. It provided for an optional 1% tax in any city or town with a transient room capacity equal to or greater than its census population. In 1997, the eligibility requirements were relaxed, and the available tax was increased. Currently, any city or town with a transient room capacity that is equal to or greater than 66% of its census population may charge an additional 1.5% sales tax.

The definition of “transient room capacity” was defined by the 2004 Legislature as the total number of:

- High-Occupancy Lodging units (# of hostel bedrooms x 4)
- Recreational Occupancy Lodging units (# of RV and campground sites that provide electricity, water and sewer x 4)
- Special Occupancy Lodging units (# of custom units)
- Standard Lodging units (# of hotel, motel, condominium bedrooms x 3)

The rationale behind the tax is to allow those cities and towns with higher than normal tourist populations to recoup some of the expense of providing basic municipal services to out-of-state visitors. Sales on items over \$2,500, such as automobiles and manufactured homes, are exempt under the assumption that most purchases of this type are made by citizens of the municipality. The citizens must approve the tax, using the normal voting process.

Only 14 cities and towns currently charge the resort community tax: Alta, Boulder, Brian Head, Garden City, Green River, Kanab, Moab, Monticello, Orderville, Panguitch, Park City, Park City East, Springdale, and Tropic.

#### ZAP TAXES

Cache, Salt Lake, Summit, and Uintah counties have enacted what are commonly referred to as ZAP taxes. ZAP taxes provide sales tax revenue for zoos, arts, and parks within the county that levies them. The rate for ZAP taxes is set at 0.100%, and revenue from the tax has netted \$16.7 million year-to-date for the current fiscal year. The largest percentage of the revenue is raised in Salt Lake County, which has collected \$14.4 million (or 86.4%) of the total year-to-date for FY 2004.

#### UTILITY SALES-AND-USE TAXES

Municipalities may impose municipal energy sales-and-use taxes on the sale or use of taxable energy within the municipality of up to 6% of the delivered market value of the taxable energy.

Exactly half of Utah cities and towns charge some form of this tax, with rates ranging from 1% to the full 6%. The majority of cities (80) that levy the tax do so at the highest rate of 6%. Utility companies are responsible to collect the municipal energy sales-and-use tax. The utility companies then forward the money to the state, which returns it to the cities and towns. As a rule, the money goes into the municipal general unrestricted fund. This is different from the Gross Receipts Tax on utilities, which is considered a type of income tax and is therefore administered at the state level and deposited into the Uniform School Fund.

#### SALES TAX ON FOOD

Utah is one of 14 states that charges sales tax on food. States that exempt food from sales tax usually restrict the exemption to food that is consumed “off-premise,” or away from the place where it was purchased. This allows restaurant taxes to draw financial support from tourists and other visitors to the state who take advantage of government services but are not required to pay for them. Utah law allows for an additional 1% sales tax on restaurant food, and only four counties in Utah do not levy the tax: Emery, Millard, Piute, and San Juan. The revenue raised is significant; year-to-date for FY 2004 is \$21.7 million.

Removing the sales tax on food in Utah has been the subject of much debate. Advocates argue that getting rid of the regressive tax is the humane thing to do, since food is essential to sustain life. Detractors point to the fiscal impact an exemption would have. In 2002, taxes on food (sold for off-premise consumption) generated \$218.42 million in sales tax revenue within the state, or 4% of state and local taxes. Approximately 74% of this revenue went to the state general fund, 16% went to cities and counties, and 10% was divided among public transit, highways, counties, zoo, resort, and rural hospital taxing districts.

#### DISTRIBUTION AND STREAMLINED SALES TAX

There has been ongoing disagreement over the distribution of the sales tax. Initially, the state collected all sales taxes and then returned them, minus a 2.5% administration charge, to the cities where the tax was collected. However, suburb cities and other smaller cities with large populations and little economic activity, argued that their citizens were contributing to larger cities’ tax revenues without making comparable contributions to their own. It was unfair to have to provide police, fire, and other services for their citizens without receiving revenue from them. By contrast, the larger cities argued that they required the revenues to provide infrastructure for the businesses and buildings where the suburban dwellers came to work and shop.

A solution was presented in 1981. It proposed changing the distribution of local sales-and-use tax revenues to include population as a factor. 50% of all local sales tax revenue would be returned to the city where the sale was made. The other 50% would be divided based on population. The bill was passed by the Legislature, but vetoed by the governor that year. Two years later, a revised bill was passed into law that provided for a 5-year transition period the 50-50 distribution model.

A more recent development has been the adoption of the Streamlined Sales Tax by the Legislature in 2003. This legislation is part of a nationwide movement that seeks to make it easier for businesses—specifically catalog, internet, and other businesses that operate across state borders—to collect and remit sales taxes. Currently, and until the Streamlined Sales Tax takes effect on July 1st, the sales tax rate on all purchases in Utah depends on the location where the sale is made. For instance, if a customer living in Washington County purchases an item from a store in Salt Lake City, and requests it to be mailed to Washington County, the tax rate for that purchase would be the current 6.6% rate for Salt Lake City. After July 1, if merchandise is shipped to a customer, the point of delivery will determine the tax rate rather than the point of sale. A person who takes possession of the merchandise at the store location will continue to pay the rate determined by the city and county where the business is located.

Within Utah, a “hold harmless” clause provides that the 1% local option sales tax will be returned to the cities and counties where the sale originated. This guarantees that cities and counties with strong retail bases won’t suffer huge revenue losses as a result of the Streamlined Sales Tax. More information on this new method of handling the sales-and-use tax is available at <http://tax.utah.gov/sst/index.html>.

#### CORPORATE FRANCHISE TAX AND CORPORATE INCOME TAX

Utah’s corporate franchise tax is a tax on the privilege to do business in Utah. A related tax is the Corporate Income Tax. For all functional purposes, these two taxes are the same with the distinguishing factor being whether or not a business has a physical presence in the state. Some corporations derive income by doing business with people or corporations in Utah without actually maintaining inventory or occupying commercial space in the state; these are subject to the

Corporate Income Tax. Those corporations that own, rent, or lease space in Utah are required to pay the Corporate Franchise Tax. The current tax rate for both is 5% of net earnings, or \$100, whichever is greater.

Corporate franchise or income tax is complex to administer. Many corporations conduct business across state and national lines. Income that is earned in Utah is taxable in Utah, and likewise for other states and countries. It can be difficult to determine exactly how much of a corporation's annual profit was earned in any given location. In order to make the task more manageable, Utah joined the Multi State Tax Compact, whose stated purposes are to:

- Facilitate proper determination of state and local tax liability of multi-state taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes.
- Promote uniformity or compatibility in significant components of tax systems.
- Facilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration.
- Avoid duplicate taxation.

As recommended by the Multi State Tax Compact, Utah determines the apportionment of a business' taxable income using the formula shown in Figure 14.

**Figure 14: Multi-State Corporate Income / Corporate Franchise Tax Apportionment Formula**

$$\text{Apportionment Factor} = \frac{\frac{\text{Utah Payroll}}{\text{U.S. Payroll}} + \frac{\text{Utah Property}}{\text{U.S. Property}} + \frac{\text{Utah Sales}}{\text{U.S. Sales}}}{3}$$

The bulk of revenues from the Corporate Income and Corporate Franchise Taxes have always gone to the Uniform School Fund. From the tax's inception in 1931 until 1967, revenues were tracked in separate funds, depending on whether they were taxes based on net income or on property ownership. Each fund had 5% withheld for the repayment of any refunds that might be claimed. After that, the property-based fund went into the General Fund, and the income-based fund went into the Uniform School Fund.

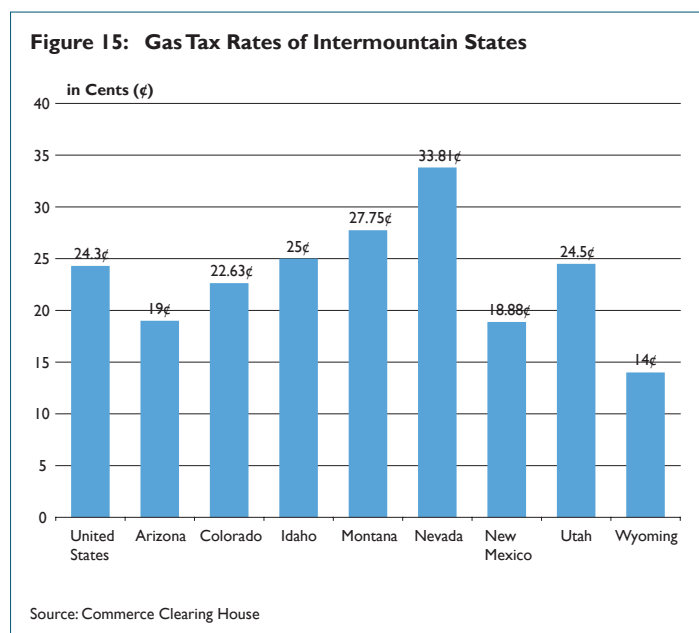
Corporate income and corporate franchise taxes have traditionally been difficult to forecast. Unlike the Individual Income Tax, corporations are able to apply current losses (negative net income) against either previous years' or future years' incomes. This process, called "carry-forward" and "carry-back," has two unwelcome consequences: it makes the calculation and administration of the tax that much more complex; and it makes for a highly volatile revenue source for state government. A proposed solution to control volatility is to levy taxes

against a three-year average, rather than each year.

### MOTOR FUEL TAX

Utah began charging a gasoline tax in 1923. Oregon, the first state to charge the tax, began in 1919. Within a few years, all 48 states and the federal government began charging the tax. The tax was designed to supplement revenue from motor vehicle registrations for building and improving Utah's roads.

The initial tax rate was 2.5 cents per gallon. Utah's motor fuel tax rate in 2004 is 24.5 cents per gallon. Counting for inflation, the 1949 tax of 4.0 cents is equivalent to 29.6 cents today. A gallon of gas at the time cost 27 cents (in 1949, the first year data are available.) The 1949 price of gasoline equates to \$1.98 per gallon today. (Inflation model based on the Consumer Price Index.) As shown in Figure 15, Utah's 24.5 cents per gallon tax is slightly higher than average.



### SEVERANCE TAX

A severance tax is a tax on the process of removing natural resources from the earth. The reasoning behind the tax is that the natural resources in Utah (oil and minerals) belong to the residents of the state as a whole, and when a business recognizes a profit by extracting these materials, the people should be compensated. Some other states have approved severance taxes that apply to the removal of other natural resources, such as coal, timber, and fish. Utah's severance tax applies only to the mining of metalliferous metals (those containing, yielding, or producing metal or metal ore) and oil and gas production.

The distinction between metalliferous and nonmetalliferous mines, as far as the tax code is concerned, began in 1919. In territorial Utah, and until 1916, the only tax on mines was the property tax. In 1916, the Legislature enacted a \$1.00 assessment plus a percent (2% in 1917 and 3% in 1918) of net proceeds on each mine. In 1919, the property tax base for metalliferous mines increased to 3 times the net proceeds,



plus improvements, plus \$5 per acre. Nonmetalliferous mines were assessed the property tax at their full value.

In 1937, the tax base for the severance tax shifted from being property-based to strictly production-based. The taxable value now was 1% of gross proceeds of metalliferous mines, with the first \$20,000 being exempt. In 1947, the exemption covered the first \$50,000. The tax was known as the Mining Occupation Tax, and would go by that name until 1988.

Revenues from the severance tax have historically been deposited in the state's General Fund. At times, a reserve fund was in operation that claimed a portion of revenues. The reserve was intended to smooth out the market fluctuations, yielding a more predictable source of tax income. The reserve fund was permanently discontinued in 1958, and all revenues went directly into the General Fund.

The severance tax on oil and gas did not exist prior to 1955. It had been discussed several times, beginning in 1937, along with a tax on the extraction of coal, but did not become law until 1955. Coal was not included in the tax, and is not taxed currently. The tax on oil and gas was first levied at a rate of 1%, but the rate was increased to 2% in 1959. The current rate of 2.6% was set in 1990.

In 1983, coal and other solid hydrocarbons (gilsonite, ozocerite, elaterite, oil shale, and tar sands) were formally exempted from the severance tax. They had not been subject to the tax previously, but the wording in the statute had not clearly exempted them from the tax.

The severance tax rate for oil is: 3% of the value up to and including the first \$13 per barrel for oil; and 5% of the value from \$13.01 and above per barrel for oil. The severance tax rate for natural gas is: 3% of the value up to and including the first \$1.50 per MCF (1000 cubic feet) for gas; and 5% of the value from \$1.51 and above per MCF for gas. The severance tax rate for natural gas liquids is 4% of the taxable value.

The Oil and Gas Severance Tax is applicable to the extractors of oil, gas, and other hydrocarbon substances, and is based on the value at the well of oil and gas production. In addition, Utah provides a 20% tax credit for renovation of a well. The tax credit may not exceed \$30,000 per well through December 31, 2004.

#### INSURANCE TAX

The Utah Legislature passed the Insurance Premium Tax in 1896. It was the first non-property tax in the state. This tax required all insurance companies doing business in the state to pay a 1.5% tax on their gross premium receipts. In 1935, the rate increased to 2.25%, where it remained for forty years. In 1945, a tax on ocean marine insurance companies was passed. These companies are required to pay a 5% tax on premiums.

The number of exemptions to the tax grew from its inception through 1936. The first exemption was for company property on

which state property taxes were paid. Other exemptions included returned premiums, reinsurance premiums, dividends paid to Utahns, premiums for policies issued by domestic benefit or cooperative benefit associations, and fees for licensing exams required by the state.

Most of the revenue from this tax goes into the General Fund. However, beginning in 1935, a portion of the revenues from fire insurance premiums was deposited in the Fireman's Pension Fund. The rate was 25% initially, but 50% of fire insurance premiums as well as 10% of life insurance premiums are currently deposited in the fund.

Other insurance taxes were given separate tax status in 1985 and 1986, including the Workman's Compensation Insurance Tax and Title Insurance Tax. Workman's Compensation Insurance was taxed at 3.25% and Title Insurance was taxed at .45%. The tax on Workman's Compensation Insurance is currently variable between 1 and 8%. Money from the Workman's Compensation Insurance Tax goes to three different funds: .25% goes to the General Fund, 7.25% goes to the Employers Reinsurance Fund, and the balance (92.5%) goes to the Uninsured Employers Fund. In 1997, the Legislature authorized the Labor Commission to impose up to an additional 2% tax on Workman's Compensation insurance premiums to avoid a possible shortfall in the Employers Reinsurance Fund.

#### EXCISE TAXES

Utah passed the Cigarette Tax in 1923, replacing a newly repealed law that made it illegal to buy or sell cigarettes. The Cigarette Tax was the second consumption tax in the state, following the Gasoline Tax, which was also enacted in 1923. The tax charged 2 cents per pack of "small" cigarettes and 4 cents per "large" pack. Also taxed were cigarette papers and tubes at ½ cent per 50 papers and 1 cent per 50 tubes.

The tax rate remained unchanged until 1954, when it doubled. The proceeds from the increase were earmarked for the Uniform School Fund while the initial portion continued to go to the General Fund. It again doubled in 1963, making the tax 8 cents per small pack and 16 cents per large pack. At the same time, the tax for all tobacco products, except cigarettes, changed to 25% of the manufacturer's sales price. All these revenues went to the General Fund until 1969, when a portion of these also went to the Uniform School Fund.

By 1970, all 50 states had a cigarette tax. Utah's was among the lowest. Since 1970, Utah has raised its tax on tobacco several times. In 1991, 3.5 cents were added to both sizes, making the total 26.5 cents for small packs and 38.5 cents for large packs. During the 1990's, public animosity toward tobacco companies grew substantially as a result of alleged withholding of health-cost information on the part of tobacco companies. The Legislature responded by sharply increasing tobacco tax rates. The current rates are (effective May 6, 2002): 69.5 cents per package of 20 cigarettes; and 86.875 cents per package of 25 cigarettes. The tax for all other tobacco products is 35% of the manufacturer's sales price.

Utah receives revenue from alcoholic beverages in several ways. It charges a liquor tax, a beer tax and it is one of 17 states that operate a liquor monopoly. Following the repeal of Prohibition in 1933, the Legislature voted to establish the monopoly, which took effect in 1935. The Legislature also spelled out the profit margin the stores would operate under. Wine was initially given a 30% markup, and intoxicating liquors were given a 40% markup. In 1983, the third successive increase in the allowed markup raised the markup for both wine and liquor to 61%. A portion of the 1983 increase combined with an increase in the beer tax to help fund the Division of Alcoholism and Drugs, which was charged with establishing detoxification centers and improving the educational information available to the public about drug and alcohol abuse. Utah derives another source of income from liquor.

All profits from these state-owned stores go directly to the General Fund. Additionally, revenue from a liquor tax, which started at 4% in 1943, goes to the School Lunch Fund. This rate was increased to 8% in 1965 and to 13% in 1982, where it remains today.

While the profit from the stores is technically not a tax, to exclude it from a discussion of state taxes would yield a distorted picture, both because of the large dollar amount involved and on a comparative basis, since all states either tax alcohol or operate a state monopoly on it.

The beer tax was first established in Utah in 1933, at a time when the sale of beer was illegal in Utah. The beer was produced in the state, but exported for sale outside the state. The tax was \$1 per barrel. In 1935, when the sale of beer again became legal, the tax increased to \$1.20 per barrel for beer sold in the state, and \$.60 per barrel for beer exported to other states. In the same year, a distinction was created that differentiated between “light” beer and “heavy” beer. The new distinction allowed that light beer was taxed at \$.80 per barrel, and heavy beer was taxed at \$1.60. Ten years later, in 1945, the Legislature authorized an increase to \$1.10 per barrel for light beer and \$4.00 per barrel for heavy beer. The most recent increase occurred in 1983, when heavy beer became taxed the same as liquor and wine (13%). At the same time, taxes on light beer jumped to \$11.00 per barrel, a portion of which helped fund the Division of Alcoholism and Drugs.

## CONCLUSION

In examining Utah’s tax system there are several noteworthy components. First, it distributes the tax burden well among different tax types, relative to other states. No single tax provides a disproportionate amount of overall revenue. Second, although the tax burden is distributed well, the burden itself is larger for Utahns than for average Americans. Utah currently ranks 28th nationwide in combined federal, state and local tax burden. Third, Utah is unique both in its demographics, which require it to support a large public education system, and in its method of supporting public education—through a dedicated income tax. Fourth, like many states, Utah is continuing a trend of relying less on the unpopular property tax, even though it is less volatile, and provides a more reliable source of state funding. Finally, Utah’s adoption of the Streamlined Sales Tax will probably boost sales tax revenues, as online and out-of-state merchants that previously did not charge the tax will now be more likely to do so.

This research report was written by Research Intern Lowe Rudd, Executive Director Steve Kroes and Director of Research Janice Houston. Ms. Houston may be reached for comment at (801) 272-8824 or [janice@utahfoundation.org](mailto:janice@utahfoundation.org).