THE TAXONOMIST

No Common Sense in the Commonwealth

By Robert S. McIntyre

In November, with much fanfare, Gov. Mark Warner (D-Va.) introduced his "comprehensive tax reform plan." He bragged that it will bring "tax fairness for working families" and "put Virginia back on the path to fiscal integrity." Warner's cheerleaders on *The Washington Post* editorial page have similarly touted the proposal as the solution to "the single most important issue facing the Commonwealth: how to overhaul the state's decrepit tax system to make burdens fairer while generating sufficient revenue to stabilize Virginia's shaky finances." Unfortunately, the rhetoric doesn't match the substance.

To be sure, Virginia's revenue system is in dire need of reform. Right now the state's tax code is both regressive and inadequate. Poor and middle-income Virginians pay far higher shares of their incomes in state and local taxes than do the wealthy. Meanwhile, since fiscal year 2000, state general fund spending in Virginia, adjusted for inflation and population growth, has fallen by 11 percent. That's meant slashed transportation outlays, skyrocketing tuition at state colleges and a variety of other woes.

But Warner's tax plan doesn't solve either of Virginia's big tax problems. Instead, it actually makes Virginia taxes even more regressive. And after a small increase in revenues in its first two years, it raises hardly any new money thereafter. Which is all very disappointing.

The unfairness of Virginia's tax code and its failure to raise enough revenue are closely linked. The best-off 5 percent of Virginians get almost a third of the total income in the state. Letting people in this top group pay far lower tax rates than everyone else is a recipe for fiscal shortfalls.

For quite a while, people have complained that Virginia's top income-tax rate of 5.75 percent kicks in at only $17,000 in taxable income (double that for couples). That means that a single person making, say, $25,000 pays the same marginal rate as someone making 10 or 50 times as much. To address this problem, Warner proposes to add a new top rate on incomes greater than $100,000 (the new bracket wouldn't start until as high as $200,000 for couples). So far, so good. But Warner's new top rate is a joke: It's only half a point higher than the current top rate! If all Warner wanted to do was stop people from fretting that millionaires pay the same rate as waitresses, why not just add a new top rate of 5.76 percent?

To add injury to insult, Warner couples his tiny increase in the top income-tax rate with an almost complete elimination of the state's inheritance tax. This giveaway more than compensates the wealthy for the small amount more they'll pay in income taxes.

On the bright side, Warner would take some small steps to reduce income taxes on low- and moderate-income families, raising the personal exemption by $200 and the standard deduction by $3,000 for couples and $1,000 for singles. But these modest progressivity enhancements are offset by his proposals to sharply increase the state's most regressive taxes: The sales-tax rate would jump from 4.5 percent to 5.5 percent, and the cigarette tax, from 2.5 cents to 25 cents.

When all the dust clears, the poorest fifth of Virginians would pay slightly more in taxes under Warner's plan, the richest Virginians would pay a bit less, and every other income group would pay virtually the same amount that it does now.

Because Warner implements his sales- and excise-tax increases right away while delaying or phasing in most of his tax-cutting measures, he says his plan would add about a billion dollars to state revenues over its first two years. Even in the short run, however, that's equal to only 4 percent of Virginia's discretionary spending. That's not enough to keep programs up with population growth and inflation, not to mention undoing the 11 percent cut in the budget over the past three years.

Once Warner phases in his tax decreases—which include full implementation of the state's currently frozen car-tax reduction—the revenue gains from his plan get even lower. After fiscal 2006, the state will collect only a couple of hundred million dollars a year more than it does under current law—about 1.5 percent of general fund spending. Of course, Warner will no longer be governor after 2006.

It would be nice if *The Washington Post* were right that Warner's plan "would progressively shift tax burdens" and "end budget shortfalls for the rest of the decade while allowing needed spending on education, health care and public safety." But that's simply not the case. Which begs the question: Why is Mark Warner staking his reputation on such a trivial tax plan?

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