State of South Carolina

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December 17, 2004

The Honorable David H. Wilkins
Speaker of the House of Representatives
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Mr. Speaker and Members of the House:

After a great deal of consideration and study, I have decided to veto H. 3065, a bill which prevents the value of real property from increasing by more than twenty percent for purposes of property tax assessment. Although I believe this bill is a well-intentioned effort to reduce property tax burdens for certain residents who have seen dramatic increases in property values, unfortunately, it is also flawed by constitutional problems and significant shifts of the distribution of state education funding.

Since this bill arrived on my desk, I have carefully listened to the debate for and against the merits of a tax cap from residents, local officials, and business groups from all over the state. I have also studied the constitutional issues and the indirect impacts caused by the tax cap. And in weighing all of these dynamics, I have been guided by my firm and consistent support of tax relief for the citizens of South Carolina. When I was in Congress my voting record was rated number one by the National Taxpayers' Union in votes to limit taxes. Limiting government and its tax load drives my political philosophy, but in the final analysis I have concluded that I cannot sign H. 3065. My primary reason for this is that I believe it is unconstitutional. Ultimately the courts will make the final determination, but it is my duty to state my opinion given my oath of office which is, in part, to uphold the constitution, and I am required to consider this with any bill that comes before me. This bill was further encumbered because it causes a shift in state education funding, and it is, as well, my role to look at large policy implications of any bill and make an assessment. This shift in the distribution of state funding may have been something the General Assembly considered, but at this point it appears to be an unintended consequence rather than an outcome derived by debate.

Constitutional Problems

I believe H. 3065 is unconstitutional for two reasons. First, H. 3065 directly conflicts with Article X, Section 1 and Article III, Section 29 of the South Carolina Constitution which require that tax assessments be based on fair market value of real property. This bill allows certain property owners whose real property value has greatly increased to pay property taxes based on *less than* the

property's fair market value. Therefore, it conflicts with this constitutional requirement because it allows tax assessments to be capped at less than fair market value.

The only way to avoid the requirement that property tax assessments be based on fair market value is by creating a general exemption or homestead exemption from property tax as permitted by Article X, Section 3 of the state constitution. I do not believe H. 3065 satisfies these constitutional exceptions because the tax cap is neither a general exemption nor a homestead exemption. A general exemption from property tax requires that "property" be exempt from taxation. The tax cap does not exempt property, it exempts value. Homestead exemptions are limited to "homesteads" or owner-occupied residential property. The tax cap clearly applies to all real property, not just residential property.

This legal position is supported by a recent decision by Circuit Court Judge Victor Rawl, issued in July 2004 after H. 3065 passed. A lawsuit brought by the City of North Charleston challenging a Charleston County cap, very similar to H. 3065, is currently pending before the South Carolina Supreme Court, which referred the case to Judge Rawl to provide the Supreme Court with findings of fact and conclusions of law regarding the constitutionality of the cap. Judge Rawl concluded that, among other things, the tax cap directly conflicts with the state constitution because the cap is enacted by "a mere statute" which ignores the constitutionally-mandated requirement that tax assessments be based on actual value and fair market value. He also found that the tax cap does not qualify as a general exemption or homestead exemption.

Second, even if the General Assembly intended H. 3065 to be an exemption from property tax, the constitution requires such exemptions receive a two-thirds vote. Article X, Section 3 of the state constitution states that ". . . the General Assembly may provide for exemptions from the property tax . . . *but only with the approval of two-thirds of the members of each House*." The property tax cap section was tacked onto H. 3065 and approved very quickly in the last two days of the legislative session by voice vote rather than a recorded vote in both the House and Senate. Therefore, there is no record that this constitutional requirement was followed.

Shift of State Education Funding

If I were to allow H. 3065 to become law, the net effect of the tax cap on the distribution of state education funding would be significant according to analysis prepared by the Department of Revenue and the State Department of Education. First, the distribution of state education funding would shift from school districts with lower valued property, including the poorest districts in the state, to school districts with higher valued property. This result is contrary to the intent of the Education Finance Act. Second, school districts with higher valued property would be able to contribute less of their local share to education funding and districts with lower valued property would have to contribute more by raising local taxes, or otherwise cut funds to schools.

Currently, under the Education Finance Act the state provides over one billion dollars to public schools using a complicated formula. This formula takes into account the ability of school districts to provide funding on the local level, known as the index of tax paying ability, so that poorer districts

receive more state dollars and wealthier districts receive less. The exemption of property under the cap would distort this formula by making districts with highly appreciating property appear to be less wealthy, and would result in almost every district in the state, including poorer districts, receiving fewer education dollars from the state.

Based on recent analysis compiled by the Department of Revenue and the State Department of Education for the 2006 index of taxpaying ability, if the twenty percent tax cap were applied to the nine counties currently undergoing reassessment, which are Allendale, Bamberg, Beaufort, Berkeley, Colleton, Darlington, Florence, Horry, and Richland, almost every school district in the state would receive less state funding. However, Beaufort County would gain over $8 million more in state funding with the cap, Berkeley County would gain $4.3 million more, and Pickens County would gain over $2 million more. Notably, another coastal county would suffer the greatest cut in state funding – the Horry County school district would lose over $8.2 million with a twenty percent tax cap in place. The Greenville County district would lose over $700,000, Florence County districts would lose close to $700,000, and Richland County districts would lose over $500,000 in state education funding.

This analysis shows that tax caps alter the current education funding formula by shifting state funds away from most school districts in the state, and we believe this to be an unintended consequence that needs further debate.

Finally, I understand that my decision today may not be the most popular; however, because the unintended consequences of H. 3065 are so significant, I believe this course of action is the most responsible to all taxpayers, to public schools and to our state constitution.

I have been and will continue to remain committed to cutting the tax burden for our state's taxpayers to encourage job growth and a more competitive economic climate for South Carolina. As I stated in my 2004 State of the State address, I would welcome a more comprehensive debate of tax reform to include both property tax relief and income tax relief. I am also open to other remedies to this problem – for instance, simply assessing property at the time of sale would protect the property owner with long-held family property while at the same time staying true to the fair market value clause of the state constitution. I am open to exploring this and other ideas with the members of the General Assembly for the benefit of our taxpayers and our education system. Unfortunately, as I have explained, I do not believe a tax cap is the best method of achieving this goal.

For the reasons stated above, I am vetoing H. 3065.

Sincerely,

Mark Sanford