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Our Taxes: Comparing Texas with Other States for 1997

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Texas Taxes at a Glance

For the state of Texas, the major source of revenue is sales taxes. For local governments, the major source of revenue is the property tax.

Texas is one of only four states with neither a corporate nor a personal income tax.

The state and local tax system of Texas is regressive. Lower-income families pay a higher percentage of their income in taxes than do higher-income families.

Texas ranks:

- C 40th in state and local taxes per capita. The average Texan paid \$2,251 in all state and local taxes for fiscal year 1997, below the national median of \$2,521.
- C 45th in state and local taxes per \$1,000 of personal income. For every \$1,000 of personal income, the average Texan pays \$94 in state and local taxes, or about 9.4 percent of personal income. This is below the national median of \$105.
- C 19th in property taxes per capita, \$845, and 16th in property taxes per \$1,000 of personal income, \$35.
- C 10th in sales taxes (all general and selective sales taxes) per capita, \$1,126, and 11th in sales taxes per \$1,000 of personal income, \$47.
- C 32nd in combined corporate income and franchise taxes, \$95 per capita, or \$4 per \$1,000 of personal income.
- C 40th in federal revenues per capita, \$767, and 35th in federal revenues per \$1000 of personal income.

Our Taxes: Comparing Texas with Other States

Judith I. Stallmann

Currently there is a national debate about federal taxes. Within Texas the state budget, of which taxes are a major component, is also a current topic of debate. In addition, at the local level, tax abatements for economic development are a continuing subject of debate. The objective of this report is to provide basic information about the Texas state and local tax system and its potential impacts on particular businesses and on citizens of different incomes.

Although considered a low-tax state, when comparing all state and local taxes in the United States, Texas ranks high on certain taxes, particularly the sales tax and the property tax. Texas ranks 40th in the nation in 1997 on state and local taxes per capita. In 1993 Texas ranked 35th. Although the overall tax burden is low compared to other states, the burden of the sales and property taxes ranks relatively high. In addition, the burden of these two taxes may disadvantage certain types of businesses. Texans have chosen not to impose a personal income tax or a broad-based corporate income tax. Because of the mix of state and local taxes, the tax system is regressive—that is, low-income families pay a higher percentage of their income in state and local taxes than do higher income families.

This report is based on data from the Texas Comptroller and the 1997 Census of Governments, the most complete set of data available across all states. While dollar amounts of taxes have changed, the objective of this paper is to make comparisons among states and the relative ranking of states has not changed substantially.

Texas State Taxes

Texas state taxes include the general sales and use tax, motor vehicle and manufactured-home tax, motor fuels tax and corporate franchise tax. These taxes provided 85 percent of state tax revenues in 1996. But taxes provide only 51 percent of state revenues, down from 61 percent in 1978 (Figure 1). Federal revenues are an increasingly important share of state revenues, growing from 25 percent of state revenues in 1978 to 30 percent in 2000. Licenses, fees, permits fines and penalties have increased from 5 percent of state revenues in 1978 to nearly 9 percent currently. Lottery proceeds, a relatively new source of state revenues, currently contribute about 3 percent of state revenues.

Texas Local Taxes

The major tax for all local governments and special districts is the property tax, which provides 85 percent of all local and special district tax revenues. Within state-regulated limits, local governments may also impose a general sales tax, a hotel/motel tax and a mixed-drink tax. Thus, these taxes vary throughout the state.

Establishing a basis of comparison

Comparing taxes across states may seem straightforward, but state tax systems vary in types of taxes, tax rates and tax levies. To compare taxes among states requires establishing a basis of comparison:

C Taxes are measured per resident.

Because state populations vary, comparing total taxes collected by each state is not useful. Instead, the average tax on an individual resident of the state--a per capita tax--is a better way to measure the relative burden of a state's tax system on its residents. The per capita tax is a measure of the average tax burden.

C Taxes are also measured per \$1,000 of personal income.

Tax systems may also be compared among states by the amount of taxes paid per \$1,000 of personal income. This comparison is useful because average incomes vary among states. A state with low per-capita income may also have a low per-capita tax, but its tax per \$1,000 of income, or its tax as a percentage of income, may be high. This is sometimes referred to as tax effort. Tax effort is often used in allocating revenues from federal to state and local governments. Government jurisdictions with higher effort may qualify for relatively more federal funds than those with lower efforts.

C Similar taxes must be aggregated.

For example, the Census Bureau aggregates the general sales tax, motor vehicle and manufactured home sales tax, hotel and motel tax and other selective sales taxes in Texas.

C State and local taxes are reported together rather than separately.

In some states, for example, the property tax is collected by both local and state governments, whereas in other states it is collected only by local government. To compare property taxes meaningfully across states, all property taxes, both state and local, must be included.

C All taxes collected by a state are counted as being paid by residents of that state.

In fact, many taxes are paid by out-of-state residents. For example, out-of-state tourists pay sales taxes and hotel/motel taxes. For popular tourism states, these tax revenues can be substantial. Out-of-state business owners and stockholders pay part of business property taxes, corporate income taxes and corporate franchise taxes.

Continued

Establishing a basis of comparison, continued

The more a state exports its taxes to out-of-state residents, the lower the actual tax burden is on state residents. Exporting taxes to out-of-state residents, however, is not reflected in this report because of lack of information on tax exporting.

C Individual and business taxes are aggregated.

Property taxes, for example, include those paid by both individuals and businesses. It might seem that only individual taxes should be included in the per-capita calculation and that business taxes should be calculated separately, as an average per business. Individual and business taxes, however, are aggregated because all taxes, including business taxes, ultimately are paid by individuals.

Owners of unincorporated businesses (individuals) pay business taxes. Corporate stockholders pay business taxes in the form of personal income taxes on dividends, capital gains taxes, and lower dividends, because dividends are allocated after corporate taxes are paid.

Just as not all state residents pay property taxes, not all residents pay business taxes. The data give an average, some residents pay less (perhaps even zero tax) and others pay more. In Texas, individuals pay 40 percent of all state and local taxes and businesses pay 60 percent.

Businesses pay other taxes in addition to the corporate income tax, including severance taxes, sales taxes on their purchases and property taxes. Unfortunately, it is not possible to separate the businesses' share of some of these taxes from the taxes paid by individuals. A similar calculation would be needed for every state. This would be needed to determine the impact of the state's tax structure on the competitiveness of its businesses.

Overview of U.S. State and Local Taxes

Although tax structures among states have many similarities, they also have some important differences (see sidebar, "Establishing a basis of comparison"). The most significant differences among states are whether or not they have:

- C A general sales tax,
- C An individual income tax, and
- C A corporate income tax.

All states tax property, gasoline, tobacco and alcohol, either at the state or local level, or both.

Alaska, Delaware, Montana, New Hampshire and Oregon have no general sales tax. Texas is one of seven states with no individual income tax. The others are Alaska, Florida, Nevada, South Dakota, Washington and Wyoming. In addition, New Hampshire and Tennessee tax only interest and dividend income and are often listed among the states with no individual income tax.

Texas, Nevada, Washington and Wyoming have neither a corporate income tax nor individual income tax. South Dakota has no individual income tax and also has no broad-based corporate income tax, but does tax banks.

Because states choose not to impose certain taxes, they often must impose higher rates for other taxes. For example, although it has no individual or corporate income tax, Texas has among the highest sales and property taxes.

Texas ranked 40th in the nation on state and local taxes per capita, down from its rank of 35th in 1993 (Stallmann and Jones). The average Texan paid \$2,251 in all state and local taxes for fiscal year 1997 (Table 1), the year with the most complete information available. Texans averaged \$270 less than the national average of \$2,521 per capita, which is calculated by adding the total taxes paid across all states and dividing by the national population. The national median is \$2,521 per capita in the state of Iowa. Half the states have a tax higher than the median, and half have a tax lower than the median (Figure 2). Because the comparisons include the District of

Table 1: State and Local Taxes, Fiscal 1997

| | Taxes Per Capita and State | Taxes Per \$1,000 of Personal Income and State |
|-----------------------------------|---------------------------------------|---|
| United States Average | \$2721 | \$104.95 |
| Median | 2521 Iowa | 104.87 Indiana |
| Maximum | 4988 Washington, D.C. ¹ | 146.76 Alaska |
| Minimum | 1842 Alabama | 84.27 Tennessee |
| Texas Average and rank | 2251 40 | 93.78 45 |

Source: Census Bureau, 1997 and BEA

¹ Second-ranked Connecticut is \$4203.

Columbia, the median state is the one ranking 26th. The lowest per capita taxes are in Alabama, at \$1,535; the highest, Washington, D.C., at \$4,988.

Texas ranks 45th in state and local taxes per \$1,000 of personal income, down from 40th in 1993. For every \$1,000 of personal income, the average Texan pays \$94 in state and local taxes, or about 9 percent of personal income. This is below the national average of \$105 and below the median of \$105 (Table 1). By either measure, the state qualifies as a low-tax state (Figure 3).

Alaska has the highest state and local taxes per \$1,000 of income, \$216. It ranks 4th in per capita taxes. Because a large share of Alaska's taxes are oil and mineral severance taxes, much of the tax burden is exported from the state to fuel consumers elsewhere.

Because it is a low tax state, Texas is generally competitive for business (Jones, Stallmann and Tanyeri-Abur). But competitiveness is also affected by a state's mix of taxes. Because it has neither a personal income tax nor a corporate income tax, Texas relies heavily on sales and property taxes. These taxes may affect some sectors of the economy more than others, reducing the competitiveness of the most affected sectors.

In addition, relying heavily on sales taxes makes the Texas tax system regressive. That is, lower-income families pay a higher percentage of their income in taxes than do higher income families (Table 2). The Office of the Comptroller projects that in fiscal 2002 the lowest income families will pay approximately 27.74% of their income in taxes while the highest income families will pay only 4.43% of their income in taxes.

Property tax

Property taxes are a major source of revenue for local governments, but only a minor source for state governments. Seven states have no state property tax (Texas, Delaware, Iowa, New York, South Dakota, Tennessee and Utah) and many more have only a minimal or selective property tax. Virginia, for example, taxes railroad property at the state level only (Spar).

Another difference among states, and even among local governments within a state, are the exemptions and special treatments for property taxes. For example, some states exempt some portion of the value of a home. The Texas Constitution was

Table 2: Incidence of Selected Texas State and Local Taxes

| Decile | Decile 1: | Decile 2: | Decile 3: | Decile 4: | Decile 5: | Decile 6: | Decile 7: | Decile 8: | Decile 9: | Decile 10: |
|--|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|---------------------|--------------------|
| Family Income | less than \$10,250 | \$10,250 to 17,876 | \$17,876 to 25,056 | \$25,056 to 32,312 | \$32,312 to 40,431 | \$40,431 to 51,146 | \$51,146 to 64,577 | \$64,577 to 82,950 | \$82,950 to 114,409 | \$114,409 and over |
| Total limited sales and use tax | | | | | | | | | | |
| Tax paid (\$millions) | \$486.80 | \$543.50 | \$622.70 | \$815.20 | \$939.70 | \$1,098.20 | \$1,245.40 | \$1,449.20 | \$1,788.90 | \$2,332.30 |
| Percentage of Tax Paid | 3.20% | 3.60% | 4.20% | 5.40% | 6.30% | 7.30% | 8.30% | 9.70% | 11.90% | 15.50% |
| Tax as percentage of income | 10.70% | 5.00% | 3.80% | 3.50% | 3.30% | 3.10% | 2.80% | 2.50% | 2.40% | 1.60% |
| Franchise Tax | | | | | | | | | | |
| Tax paid (\$millions) | \$104.70 | \$111.90 | \$111.90 | \$127.90 | \$130.80 | \$138.10 | \$148.30 | \$161.40 | \$177.40 | \$241.30 |
| Percentage of Tax Paid | 5.50% | 5.90% | 5.90% | 6.70% | 6.80% | 7.20% | 7.80% | 8.40% | 9.30% | 12.60% |
| Tax as percentage of income | 2.30% | 1.00% | 0.70% | 0.60% | 0.50% | 0.40% | 0.30% | 0.30% | 0.20% | 0.20% |
| Gasoline | | | | | | | | | | |
| Tax paid (\$millions) | \$97.20 | \$114.40 | \$131.50 | \$162.00 | \$173.40 | \$196.30 | \$224.90 | \$238.20 | \$261.10 | \$306.80 |
| Percentage of Tax Paid | 5.10% | 6.00% | 6.90% | 8.50% | 9.10% | 10.30% | 11.80% | 12.50% | 13.70% | 16.10% |
| Tax as percentage of income | 2.20% | 1.10% | 0.80% | 0.70% | 0.60% | 0.60% | 0.50% | 0.40% | 0.40% | 0.20% |
| Motor Vehicle | | | | | | | | | | |
| Tax paid (\$millions) | \$88.20 | \$100.10 | \$128.70 | \$166.90 | \$207.40 | \$243.10 | \$264.60 | \$326.60 | \$386.20 | \$472.00 |
| Percentage of Tax Paid | 3.10% | 3.60% | 4.60% | 5.90% | 7.40% | 8.60% | 9.40% | 11.60% | 13.70% | 16.80% |
| Tax as percentage of income | 1.90% | 0.90% | 0.80% | 0.70% | 0.70% | 0.70% | 0.60% | 0.60% | 0.50% | 0.30% |
| School Property | | | | | | | | | | |
| Tax paid (\$millions) | \$480.50 | \$581.80 | \$630.30 | \$819.50 | \$883.00 | \$1,097.50 | \$1,278.90 | \$1,583.00 | \$2,055.30 | \$2,899.20 |
| Percentage of Tax Paid | 3.20% | 3.90% | 4.20% | 5.50% | 6.00% | 7.40% | 8.60% | 10.70% | 13.90% | 19.50% |
| Tax as percentage of income | 10.60% | 5.30% | 3.90% | 3.60% | 3.10% | 3.10% | 2.90% | 2.80% | 2.70% | 2.00% |
| Natural Gas | | | | | | | | | | |
| Tax paid (\$millions) | \$2.00 | \$7.40 | \$13.20 | \$19.60 | \$25.50 | \$36.30 | \$45.60 | \$60.30 | \$91.20 | \$189.30 |
| Percentage of Tax Paid | 0.20% | 0.80% | 1.40% | 2.10% | 2.80% | 4.00% | 5.00% | 6.60% | 10.00% | 20.70% |
| Tax as percentage of income | 0.04% | 0.07% | 0.08% | 0.08% | 0.09% | 0.10% | 0.10% | 0.11% | 0.12% | 0.13% |
| Total | | | | | | | | | | |
| Tax paid (\$millions) | \$1,259.40 | \$1,459.10 | \$1,638.30 | \$2,111.10 | \$2,359.80 | \$2,809.50 | \$3,207.70 | \$3,818.70 | \$4,760.10 | \$6,440.90 |
| Tax as percentage of income | 27.74% | 13.37% | 10.08% | 9.18% | 8.29% | 8.00% | 7.20% | 6.71% | 6.32% | 4.43% |

*This analysis does not include the county and municipal property tax. But they would not be less regressive than the school property tax and might be more regressive because they do not have the \$15,000 homestead exemption, which is a higher percentage of the value of their home for low income families.

Source: Texas Comptroller

amended in 1995 to exempt \$15,000 of the value of homesteads from the school property tax. Homeowners over 65 years old may also receive special exemptions, and local school districts may give home owners additional exemptions. City and county property tax abatements may be given to some businesses.

State and local property taxes in the U.S. average \$817 per capita. Texas imposes \$845 per capita in property tax, which is a local property tax only (Table 3). Texas ranks 19th in property taxes per capita up from 20th in 1993 (Stallmann and Jones). At \$1,587, the New Jersey property tax per capita is the highest in the nation. Alabama has the lowest state and local property tax per capita, \$240 (Figure 4).

People with higher incomes generally own higher-valued properties than those with lower incomes. Thus, a high per-capita property tax may reflect not high tax rates

Table 3: Property Taxes, Fiscal, 1997

| | Taxes Per Capita and State | Tax Per \$1,000 of Personal Income and State |
|-------------------------------|-----------------------------------|---|
| United States Average | \$817 | \$31.52 |
| Median | 762 Colorado | 30.58 Michigan |
| Maximum | 1587 New Jersey | 55.76 New Hampshire |
| Minimum | 240 Alabama | 11.27 Alabama |
| Texas Average and Rank | 845 19 | 35.20 16 |

Source: Census Bureau, 1997 and BEA

but higher-than-average incomes in the state. To compensate for varying levels of income among states, state and local property taxes are compared per \$1,000 of personal income. A state with a relatively high per capita tax and low tax per \$1,000 of personal income would indicate a high-income state.

Texas property taxes per \$1,000 of personal income are \$35, ranking it 16th in the nation. Thus, Texas has similar ranks on both property tax measures. The national average is \$31, and the median is \$31, per \$1,000 of personal income (Figure 5). New Hampshire has the highest state and local property taxes per \$1,000 of income, at \$56; it ranks second in property taxes per capita. Because it has neither an individual income tax nor a general sales tax, New Hampshire heavily taxes property. It is also interesting to note that the states which tax property most heavily are in the Northeast (Figure 5). Alabama ranks lowest on both measures (Table 2), with \$240 per capita and \$11 per \$1,000 of personal income.

Property taxes are paid by property owners. Those not owning property, such as renters, do not pay property tax directly. They typically pay property taxes indirectly, however, as part of their rent. Whether a landlord is able to pass the property tax on to the tenant as part of the rent depends on supply-and-demand conditions in the local rental market. In the short run, if the vacancy rate is high, the landlord may be unable to pass the tax to the renter. However, property taxes are an integral part of the landlord's cost structure for providing rental space, which in the longer-run must be fully covered by rental income. Hence, the property tax is usually incorporated into rental rates.

Local governments in Texas rely heavily on property taxes. This may reduce the competitiveness of capital-intensive firms in Texas. Also, not all types of property are taxed. Individual personal property and intangible property, held as financial instruments, are not taxed. This may cause inefficiencies in the economy because it shifts investment away from taxed real property to untaxed intangible property (Jones, Stallmann and Tanyeri-Abur).

The property tax in Texas is a regressive tax; as family income increases, so does the percentage of income paid in property taxes (Table 2). The lowest income families pay 10.6 percent of their income in school property tax while the highest income families pay 2 percent. The school property tax has a \$15,000 household exemption so it is likely that county and municipal property taxes are even more regressive. About 25% of property taxes are exported to out-of-state property owners (Texas Comptroller).

General and selective sales and use taxes and gross receipts taxes

Because of differences among states, similar taxes must be aggregated into categories. The sales tax category includes the general sales tax, all selective sales taxes and gross receipts taxes. The Census Bureau defines these taxes as: "Taxes on goods and services, measured on the basis of the volume or value of their transfer, upon gross receipts or gross income therefrom, or as an amount per unit sold (gallon, package, etc.); and related taxes based upon use, storage, production, importation, or consumption of goods and services."

In Texas the mixed drinks tax and the utility tax are examples of a gross receipts tax. The general sales and gross receipts taxes are aggregated because both are

based on the gross receipts from a business activity. In the case of a sales tax it is the gross receipts of only specified business activities. Also included in this category are selective sales taxes such as motor fuels, alcohol, tobacco, and hotel and motel taxes.

Texas state government's major revenue source is sales taxes. With sales taxes of \$1126 per capita, Texas ranks 10th highest in the nation, above the national average of \$977 (Table 4). In 1993 Texas ranked 9th in the nation (Stallmann and Jones).

Nevada has the highest per capita sales and gross receipts taxes, at \$1,767 (Figure 6).

As one of the nation's leading tourism states, Nevada receives much of its sales and

Table 4: Sales and Gross Receipts Taxes, Fiscal 1997

| | Taxes Per Capita and State | Taxes Per \$1,000 of Personal Income and State |
|-----------------------------------|---------------------------------------|---|
| United States Average | \$977 | \$37.70 |
| Median | 932 Kansas | 37.08 California |
| Maximum | 1767 Nevada | 64.49 Hawaii |
| Minimum | 256 Oregon ¹ | 10.26 Oregon |
| Texas Average and Rank | 1126 10 | 46.92 11 |

Source: Census Bureau, 1997 and BEA

¹ Alaska, Delaware, Montana, New Hampshire and Oregon have no state general sales tax, only selective sales and gross receipts taxes.

gross receipts taxes from non-residents by heavily taxing activities on which tourists spend money. Kansas has the median per capita tax, \$932; and Oregon has the lowest per capita tax, \$196. Oregon has only selective sales taxes, but no general sales tax.

Alaska, Delaware, Montana, New Hampshire and Oregon have no state general sales tax. They do have sales or gross receipts taxes on some specific items such as gasoline, alcohol and tobacco.

Texas also ranks high on sales taxes per \$1,000 of personal income. Texans pay nearly \$47 of every \$1,000 of personal income in sales taxes (both general and selective). Texas ranks 11th in the nation (Table 3). The national average is \$38 of sales and gross receipts taxes per \$1,000 of personal income; the national median is \$37 (Figure 8). Hawaii ranks highest in sales and gross receipts taxes per \$1000 of personal income. Like Nevada, Hawaii is a major tourist destination and receives much of its sales tax revenues from non-residents. Oregon again ranks lowest.

Texas also exports some of its sales tax. Out-of-state residents pay approximately 25% of the general sales and use taxes, 15% of the gasoline tax and 15% of the motor vehicle sales and use taxes (Texas Comptroller).

In 34 states, local governments can also impose sales taxes (Moody). In Texas, local sales taxes imposed by cities and counties may not exceed a total local rate of 2 percent. Local governments may also impose a hotel-motel and a mixed drinks tax.

The sales tax rate does not completely reflect the tax burden because the burden also depends on how narrow or broad the tax base is. In Texas, the general sales tax applies to some services and to all goods except unprepared foods and prescription drugs. This is a fairly broad base relative to other states.

Because the general sales tax applies to most consumer goods in Texas, it does not affect consumer choices of goods. The tax does not affect the competitiveness of Texas retailers because consumers generally do not cross state lines to shop, except

along borders. The narrower base in services, however, may lead both consumers and businesses to choose untaxed services over taxed services, causing inefficiencies.

The sales taxes businesses pay on their purchases increase their costs, making them less competitive with businesses in other states. Equipment and materials for manufacturing and for farm and ranch use are exempted from sales tax, allowing those industries to remain competitive.

In fiscal 2002 low income families will pay a higher percentage of their income in sales taxes than will higher income families (Table 2). The lowest-income families will pay 10.7% of their income in general sales and use taxes compared with 1.6% for the highest-income families. The lowest-income families will pay 2.2% of their income in gasoline tax, and 1.9% in motor vehicle taxes compared with .2% and .3% for the highest-income families (Texas Comptroller).

Corporate franchise and income taxes

Most states impose a license or franchise tax on corporations for the privilege of doing business within the state. In Texas, this tax applies only to corporations and limited-liability companies. In Texas the tax is more than a nominal fee for a license. The corporate franchise tax has two separate bases, each with a separate tax rate. A tax rate of \$2.50 per \$1,000 is imposed on taxable capital (roughly net worth). A tax rate of 4.5 percent is imposed on earned surplus (profits plus executives' income). Firms must calculate the tax by both methods and pay the higher of the two. Twenty-five states have similar franchise taxes.

To compare the taxation of corporations across states, corporate franchise taxes and the corporate income taxes were added together for each state (Figure 8). North

Dakota is the only state without a corporate franchise tax. Utah instituted a corporate franchise tax in 1995 (Moody). Four states do not have a corporate income tax—Nevada, Texas, Washington and Wyoming. In addition, South Dakota’s is not broad-based, it applies only to banks. Only New York has a local corporate income tax (Moody).

Delaware ranks first in combined corporate taxes per capita at \$766 (Table 5). There is a wide range in combined corporate taxes, with the lowest combined tax per capita of \$2 in Washington and a median of \$110 in Mississippi (Figure 8). Washington has no corporate income and only a nominal fee for a corporate franchise tax. Instead it relies on a gross receipts tax with 20 different rates, depending on the type of business activity (Moody). Texas, with a tax of \$95 per capita, ranks 32nd in the nation, up from 33rd in 1993 (Stallmann and Jones).

Texas ranks 33rd in combined corporate income and franchise taxes per \$1,000 of personal income. Again, Delaware ranks highest and Washington the lowest (Figure 9).

The corporate franchise tax does not appear to affect the competitiveness of Texas businesses when compared to the combined corporate franchise and income

Table 5: Corporate Income and Franchise Taxes, Fiscal 1997

| | Taxes Per Capita and State | Taxes Per \$1,000 of Personal Income and State |
|------------------------------|-----------------------------------|---|
| United States Average | \$148 | \$5.72 |
| Median | 110 Mississippi | 4.89 Kansas |
| Maximum | 766 | 27.76 |

| | Delaware ¹ | Delaware ² |
|-----------------------------------|-----------------------|-----------------------|
| Minimum | 2 Washington | 0.07 Washington |
| Texas Average and Rank | 95 32 | 3.94 33 |

Source: Census Bureau, 1997 and BEA

¹ Alaska ranks second with \$546 and Washington, D.C., third with \$343.

² Alaska ranks second with \$20.24 and New York third with \$11.

taxes of other states. But the corporate franchise tax may affect competitiveness among businesses within the state. The Texas corporate franchise tax is paid only by corporations and limited-liability companies. Unincorporated businesses in the state that produce the same products or services do not pay the tax, giving them a cost advantage over corporations. Because both corporations and non-corporations must sell products in a competitive market at similar prices, corporations with non-corporate competitors cannot pass on this tax to consumers by adding it to their products' prices. This gives un-incorporated businesses a competitive advantage over corporate businesses in the state.

This can affect the state economy in two ways:

- C Corporations paying the franchise tax earn less profit per unit than businesses not taxed. This reduces the money available for shareholders, reinvestment or other uses.
- C Businesses with corporate franchises may respond to the cost disadvantage of the tax and re-structure the business into an organization not subject to the tax.

Of course, larger corporations may be unable to take this option, but the

franchise tax may impede the development of new and/or small corporations. The franchise tax also is regressive (Table 2). The lowest-income families pay about 2.3% of their incomes in franchise taxes while the highest-income families pay .2%. Out-of-state residents pay approximately 24% of the franchise tax (Texas Comptroller).

Individual income tax

A major difference between Texas and most states is that Texas has no personal income tax. Other states without individual income taxes are Alaska, Florida, Nevada, South Dakota, Washington and Wyoming (Figure 10). New Hampshire and Tennessee also have no broad-based income tax, but do tax interest and dividend income. Local governments in fourteen states can also impose an individual income tax (Moody).

The national average state and local individual income tax is \$594 (Table 6). The median is similar, \$599 per capita. The highest per capita individual income tax is \$1,425 in Washington, D.C. Of the states imposing a broad-based individual income tax, the minimum is \$255 per capita in North Dakota.

Table 6: Individual Income Taxes, Fiscal 1997

| | Taxes Per Capita and State | Taxes Per \$1,000 of Personal Income and State |
|------------------------------|-----------------------------------|---|
| United States Average | \$594 | \$22.91 |
| Median | 599 Utah | 24.28 Arkansas |
| Maximum | 1425 | 40.45 |

| | | |
|-----------------------------------|-------------------------------|-------------------------------|
| | Washington, D.C. ¹ | Washington, D.C. |
| Minimum | 0 6 states ² | 0.00 6 states ⁴ |
| Texas Average and Rank | 0 6 states ³ | 0.00 6 states |

Source: Census Bureau, 1997 and BEA

¹ New York ranks second with \$1,213.

² The minimum for a state that imposes a broad-based individual income tax is \$255 in North Dakota

³ Texas, Alaska, Washington, Nevada, Florida and Wyoming.

⁴ The minimum for a state that imposes a broad-based individual income tax is \$12.21 in North Dakota.

Nationally, the average state and local individual income tax per \$1,000 of personal income is \$23. The median is similar, \$24. Among states with a broad-based individual income tax, the tax per \$1,000 of personal income ranges from \$40 in Washington, D.C. to \$12 in North Dakota (Figure 11).

In lieu of an individual income tax, Texas relies heavily on the sales tax at the state level, which is not deductible for federal income taxes. The federal government allows people to deduct their state and local income taxes from their federal taxable income, lowering the federal tax paid. Although the lack of an individual income tax is often used as a selling point for Texas, in fact, relying on sales taxes for state revenue increases the federal income tax Texans pay. This affects the state's competitiveness, because that money leaves the state rather than being spent by consumers on products and services within the state. Ironically the state legislature could lower the federal income tax paid by Texans by substituting a state income tax for part or all of the state sales tax.

Income taxes generally are progressive taxes. In most states, the state income tax is "piggy-backed" on the federal income tax and requires little cost for collection.

Despite these apparent advantages, Texans have shown little interest in substituting an income tax for sales or property taxes as a major source of state and local revenues.

Licenses and Miscellaneous Taxes

State and local governments require licenses for many activities. The difference between a license and a tax is that licenses are paid only by those who participate in a particular activity, such as driving a car. The corporate franchise tax is classified as a license, but we have included it with the corporate income tax. There are also many small taxes and fees included here, such as fees and taxes for recording mortgages or stock transfers. The most notable for Texas are severance taxes and estate taxes. While any given fee or tax may be small, when added together they do contribute substantial revenues to state and local governments, about \$49 billion dollars in 1997. Licenses, including motor vehicle and operators licenses contributed about 45% of this amount; miscellaneous taxes, including the estate tax, about 45%; and severance taxes, about 10% (Census Bureau). Severance taxes were an important tax in the history of Texas, but as oil prices fell in the 1990s and as the state diversified, oil became a smaller share of the state's economy and a smaller share of tax revenues.

Alaska receives the most revenue per capita from licenses and miscellaneous taxes, \$1897, nearly three times that of second-ranked Wyoming (Figure 12). Texas ranks 25th, just above the national median and also very close the national average (Table 7). Indiana, collects the least in licenses and miscellaneous taxes, \$62.

Alaska also receives the revenue from licenses and miscellaneous taxes per \$1000 of personal income, \$70, more than three times that of second-ranked Wyoming

(Figure 13). Texas receives nearly \$8 per \$1000 of personal income, ranking 22nd in the nation. Indiana again ranked lowest.

Because this category contains a broad mix of fees and taxes it is difficult to evaluate their impact on the state of Texas relative to other states. These also include

Table 7: Licenses and Miscellaneous Taxes, Fiscal 1997

| | Taxes Per Capita and State | Taxes Per \$1000 of Personal Income and State |
|-------------------------------|-----------------------------------|--|
| United States Average | \$184 | \$7.10 |
| Median | 183 Alabama | 7.20 Virginia |
| Maximum | 1897 Alaska ¹ | 70.28 Alaska ² |
| Minimum | 62 Indiana | 2.61 Indiana |
| Texas Average and Rank | 185 25 | 7.72 22 |

Source: Census Bureau, 1997 and BEA

¹ Wyoming ranks second with \$654, and Delaware third with \$404.

² Wyoming ranks second with \$27.70 and Montana third with \$19.22.

taxes that are tailored to the particular conditions of the state. Severance taxes, for example, are imposed by states with large mineral deposits. Eighteen states do not have a severance tax (Census Bureau). Severance taxes are a way of exporting taxes, if a significant portion of minerals produced are sold outside the state. Although paid by the mineral producer, the tax (or a portion of it) may be added to the mineral's selling price.

The producers' ability to export the tax depends on the competitiveness of the mineral's national and international markets. For example, oil moves internationally from many sources to many consumers. Because all producers must sell at the international

price of oil, producers in a given area cannot pass along a new severance tax unless their costs are lower than average. For other minerals, such as diamonds, supply sources are few and competition in the market limited. For these, much more of a severance tax can be exported to the consumer. Out-of-state residents pay approximately 46% of Texas's natural gas tax (Texas Comptroller). The natural gas tax is a progressive tax. The lowest-income families pay approximately .04% of their incomes in natural gas taxes while the highest-income families pay .13%.

Enterprises, Insurance Trusts, Charges and Miscellaneous

State and local governments may operate enterprises, such as liquor stores, or utilities which provide revenues to the government. This does not include the taxes on utilities or alcohol. In addition to utilities, state and local governments charge for some services and products within other agencies. Special assessments to pay for special capital items are also included as charges. The net proceeds of the lottery are included in the miscellaneous category as well as small sources of revenues that are difficult to classify. In addition, states maintain various insurance trust funds, the investments of which provide revenues to the state for specific uses. These enterprises, charges, insurance funds and miscellaneous revenues contributed approximately \$641 billion in 1997. Within this the insurance trust funds are the largest contributor to revenue, \$247 billion; followed by miscellaneous charges by agencies, \$191 billion. Utilities and liquor stores contributed \$78 billion, interest \$62 billion and special assessments and other charges contributed another \$64 billion (Census Bureau).

Alaska received \$12,619 per capita from enterprises, insurance trusts, charges and miscellaneous (Table 8). This is \$9,000 more per capita than second-ranked

Table 8: Enterprises, Insurance Trusts, Charges and Miscellaneous, Fiscal 1997

| | Taxes Per Capita and State | Taxes Per \$1000 of Personal Income and State |
|-------------------------------|-----------------------------------|--|
| United States Average | \$2,396 | \$92.42 |
| Median | 2,172 Alabama | 94.32 District of Columbia |
| Maximum | 12,619 Alaska ¹ | 467.55 Alaska ² |
| Minimum | 1,553 Connecticut | 43.57 Connecticut |
| Texas Average and Rank | 2,352 23 | \$97.99 21 |

Source: Census Bureau, 1997 and BEA

¹ Washington ranks second with \$3,408

² Wyoming ranks second with \$143.

Washington. Texas receives \$2352 per capita, ranking 23rd in the nation. This is below the national average, but above the median. Connecticut collected the least per capita, \$1553 (Figure 14).

Alaska also collected the most revenue from enterprises, insurance trusts, charges and miscellaneous per \$1000 of personal income. Once again, its collections were approximately 3 times those of the second-ranked state, Wyoming. Texas ranked 21st, collecting nearly \$98 per \$1000 of personal income, above both the national average and median. Connecticut collected the least per \$1000 of personal income, less than one-tenth of that collected by Alaska (Figure 15).

Because of the variability among states in the enterprises they run, the goods and services for which they charge, the insurance funds they manage, whether or not

they have a lottery and how it is managed, and how the revenues generated may legally be used, it is not possible to evaluate the impact on the state. Generally consumers have little choice on utilities, but utility deregulation will have impacts in the future. The costs of utilities affects the competitiveness of businesses. No analysis of the impact of these taxes on families of different incomes is available.

Federal Government Revenues

Another source of revenues for state and local governments are revenues from the Federal government. These revenues are usually designated for specific programs that the state or local government administers for, or in partnership with, the federal government. It does not include federal expenditures on programs managed by the federal government, such as military bases and the Johnson Space Center.

On average the federal government provides \$913 per capita in revenues to state and local governments. Texas receives less than this, \$767 per capita and ranks 40th in the nation (Table 9). Washington, D.C. receives \$3,772 and Alaska receives \$1,987. Virginia receives the lowest per capita, \$575 (Figure 16).

Texas ranks slightly higher, 35th on federal revenues per \$1000 of personal income. Washington, D.C., again ranks highest with revenues of \$107, \$30 higher than second-ranked Wyoming (Figure 17). Nevada receives the least, \$20. The national average and the median are approximately \$35.

To evaluate the impact of federal revenues, comparing the relative rank of states on revenues received is not sufficient. It is also necessary to compare the taxes and

Table 9: Federal Government Revenues, Fiscal 1997

| | Taxes Per Capita and State | Taxes Per \$1000 of Personal Income and State |
|-------------------------------|---------------------------------------|--|
| United States Average | \$913 | \$35.24 |
| Median | 885 Michigan | 35.66 Georgia |
| Maximum | 3772 Washington, D.C. ¹ | 107.07 Washington, D.C. ² |
| Minimum | 575 Virginia | 20.44 Nevada |
| Texas Average and Rank | 767 40 | 31.95 35 |

Source: Census Bureau, 1997 and BEA

¹ Alaska ranks second with \$1,987.

² Wyoming ranks second with \$76.68.

fees that the citizens and business in each state send to the federal government. In other words, such an evaluation requires the use of net, rather than gross, revenues.

Summary

Compared to the average state and local taxes paid by U.S. residents, Texas taxes are low. The state ranks 40th in the United States on state and local taxes per capita, and 45th on state and local taxes per \$1,000 of personal income. Texans have chosen not to impose a personal income tax or a broad-based corporate income tax. The state does impose a corporate license or franchise tax on corporations and limited liability companies. Although this is not a nominal tax, Texas still ranks low on the combined corporate income and license taxes when compared with other states. Texas ranks high on sales and property taxes. Although the overall tax burden is low, the burden of these two taxes, on which Texas ranks relatively high, may disadvantage some industries.

Despite its low rank on state and local taxes, taxation continues to be a major issue in Texas. The reasons for this may be the heavy reliance on sales and property taxes and the tax incentives given to businesses.

The state and local tax system of Texas is regressive. The Texas Comptroller estimates that in fiscal 2002 the lowest-income families will pay approximately 27.74% of their incomes in taxes compared with approximately 4.43% by the highest-income families (Table 2). Among those taxes for which this analysis is available, only the natural gas tax is progressive.

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