



WINTER 2021

PERCSPECTIVES ON POLICY

THE PANDEMIC AND TEXAS STATE TAX REVENUE

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The Covid-19 pandemic has played havoc with government budgets at all levels. Here in Texas, state tax collections fell by large amounts in March and April of 2020, and while they have recovered some of the decline, current state tax collections remain well below what they were a year ago.

The Texas fiscal year runs from September through August, and we are currently in fiscal year (FY) 2021. Figure 1 shows monthly tax collections for FY 2018, 2019, 2020, and the first four months of 2021. Looking at the beginning of 2020, it is clear that state tax collections were running well ahead of 2019. As the pandemic hit, tax collections in March and April fell sharply. This was accompanied by reduced demand for certain activities such as air travel and government restrictions on many businesses, especially in the entertainment, accommodation, and food service industries. For the year, tax collections were down 3.4%.

Several taxes were actually up for FY 2020, including the sales tax (up 0.2%), franchise tax (up 4.8%), and insurance taxes (up 5.5%). The franchise tax is interesting because collections were delayed until July, matching the delay in the collection of the federal income tax. This explains the large spike in tax collections for FY 2018 and 2019 in May, and the large spike for FY 2020 in July. Another important aspect of the franchise tax is that it is based on business activity in the prior calendar year, 2019, and so it did not suffer a decline in FY 2020. The picture in FY 2021 may not be so rosy.

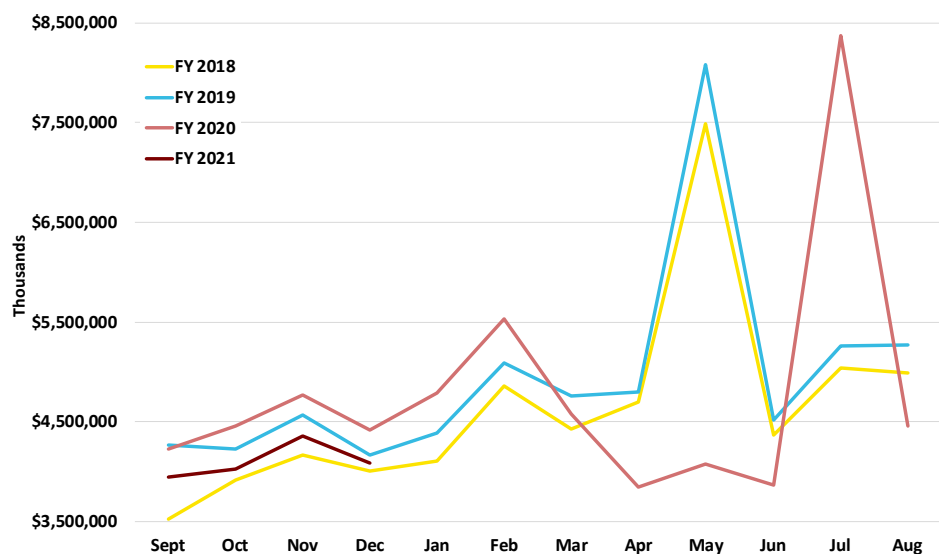
So far, FY 2021 has seen

tax collections running well below FY 2020, and actually below values from FY 2019. Total tax collections in the first four months of FY 2021 have run 8.1% below total tax collections in the first four months of FY 2020.

In terms of state tax dollars raised, Texas' sales tax is by far the largest contributor. In fact, sales taxes in FY 2020 made up 59.4% of all tax collections statewide. The other big tax in Texas that receives much attention, the property tax, supports local government and school districts, but does not directly contribute to state coffers. Sales taxes in the first four months of FY 2021 are running 5.3% below levels from FY 2020. As shown in Figure 2, sales taxes in FY 2021 are basically running at levels seen in FY 2019.

Looking back, it is apparent in the sales tax data that these taxes in FY 2020 were running well ahead of FY 2019 levels until the spring of 2020, but by April had fallen well below the level of prior years, even

FIGURE 1. TOTAL TEXAS TAXES



Source: Texas Comptroller

below levels from FY 2018, before recovering somewhat in mid-summer.

Sales taxes fund state government, but they also fund city governments and many county governments. Locally, in College Station, sales taxes provided 35% of tax revenue in FY 2019, and 33% in Bryan. Brazos County relies heavily on the property tax for

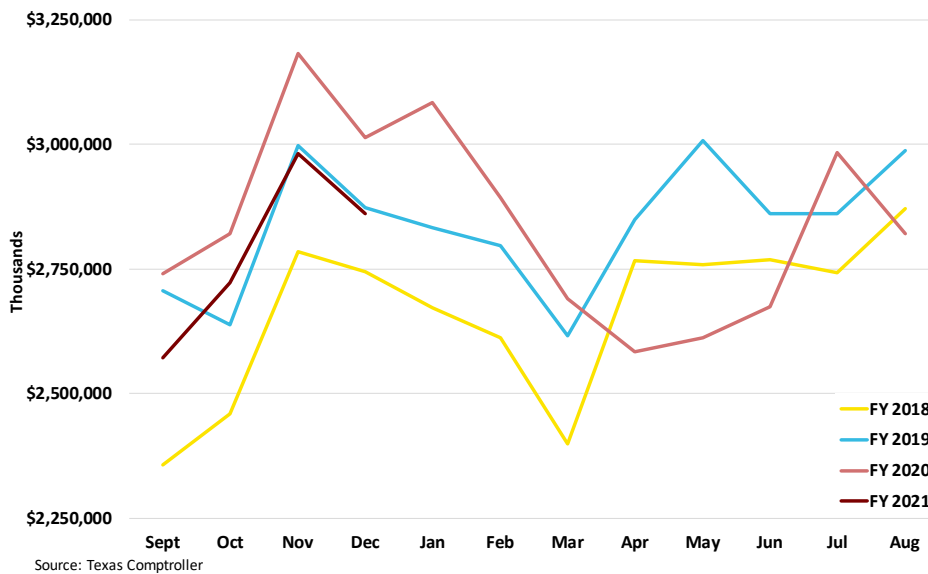
tax collections in April and May, continuing in June and for the rest of FY 2020. In the first four months of FY 2021, these taxes are running 38% below the comparable months of FY 2020, and well below the same period of FY 2019 and even FY 2018.

Two other taxes that contribute smaller amounts to the state tax coffers, but that also contribute

small amounts to local tax coffers, are hotel occupancy taxes and alcoholic beverage taxes. Hotel occupancy taxes were down tremendously in FY 2020 and made up 0.8% of state tax collections. Likewise, in FY 2020, alcoholic beverage taxes made up 2.0% of state tax collections. Like many taxes, hotel occupancy taxes also nose-dived in the spring of FY 2020 and continue to be significantly lower in the first four months of FY 2021 compared to the same months in FY 2020. In Figure 4, the decline in May 2020 is apparent when hotel occupancy tax collections fell

to their low point, about one-sixth the value from May 2019. In the first four months of FY 2021, hotel occupancy taxes are down 41.4% from FY 2020, and indeed these tax collections are running well below all of the prior fiscal years shown in Figure 4.

FIGURE 2. SALES TAXES



funding, but sales taxes provide 19% of its tax revenue as well. Thus, reductions in sales tax collections cause budget woes not just for the state but also for local governments.

Texas also receives a significant portion of its state tax revenue from taxes on the production of oil and natural gas. In FY 2020, a down year, these taxes still amounted to 7.2% of all tax collections and were the fourth largest state tax. (Again, the property tax is not a state tax.) These taxes are assessed on the value of production, and so they vary both with the quantity of production and with the price of either oil or natural gas. The large declines in prices in FY 2020 led to great reductions in these tax collections, as seen in Figure 3. The collapse in oil and natural gas prices in FY 2020 led to huge declines in these

FIGURE 3. OIL AND GAS PRODUCTION TAXES

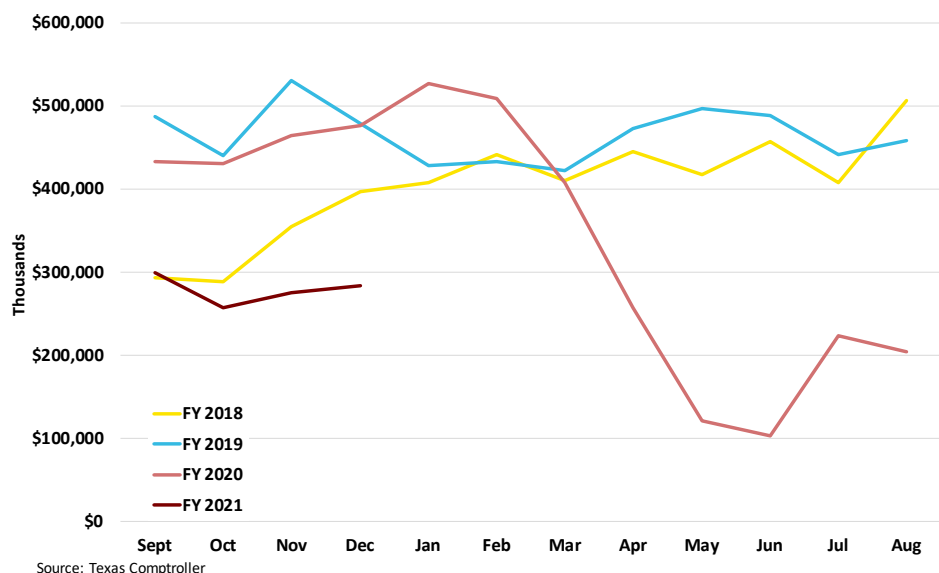
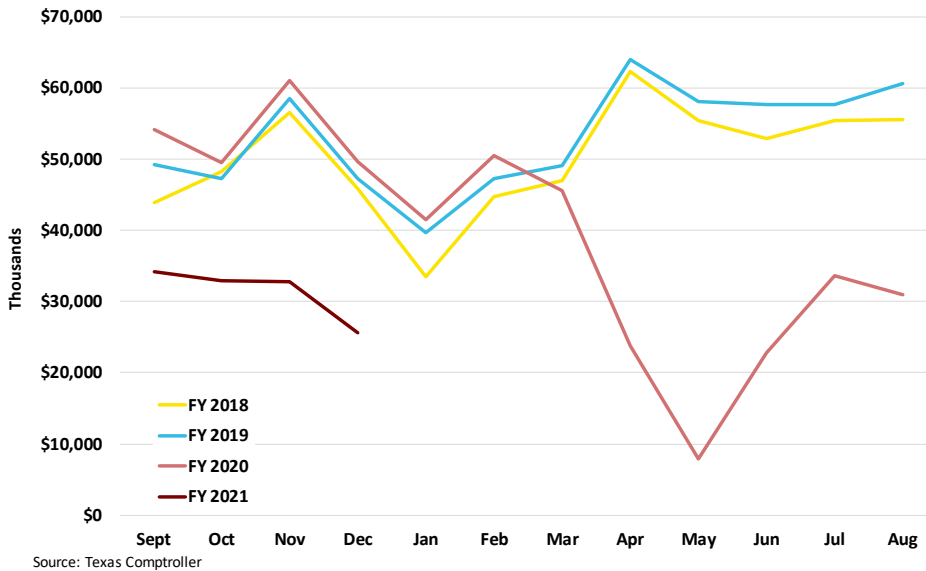


FIGURE 4. HOTEL TAXES



Local governments also receive funds from the hotel occupancy tax, and this tax makes up a higher percentage of tax revenue in the cities of College Station and Bryan than it does for the state. Thus, the large reduction in hotel occupancy taxes will cause budget issues not just for the state but also for city governments throughout Texas. In College Station, this tax was 6.7% of all tax revenue in FY 2019, and in Bryan it was 2.5%.

The final graph shows alcoholic beverage taxes. As with most of the other taxes, 2020 alcoholic beverage taxes through February were running ahead of 2019 revenues. But the decline in spring 2020 is apparent here as well and corresponds to closures of bars and restaurants. Collection of this tax is down 26.4% in the first four months of FY 2021 compared to the same months in FY 2020 and is running below collections in all prior fiscal years that appear in the graph.

This tax also contributes to city and county tax revenue. Alcoholic beverage taxes contributed almost 1% of College Station’s FY 2019 tax revenue, and 1% of tax revenue in Brazos County. They made up only 0.3% of Bryan’s tax revenue.

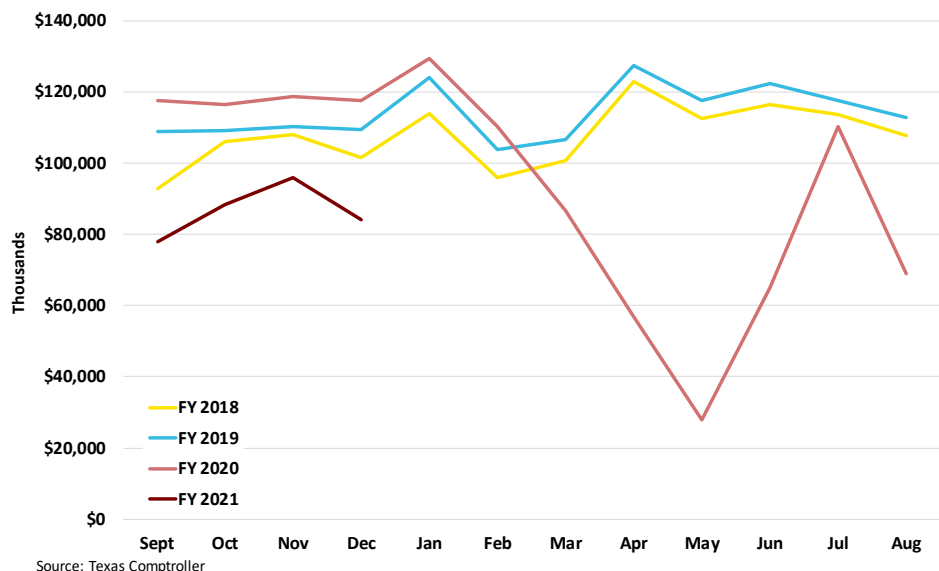
Thus, these taxes are not large contributors to city and county budgets, but they certainly contribute on the margin and have seen a huge percentage decline in collections, causing further problems for city and county governments in the state.

The Texas state legislature is meeting this spring to set the state budget for the next biennium. Texas has a balanced budget requirement, and the Comptroller must provide estimates of available tax revenue for the legislature to consider in setting spending levels for the coming two-year budget cycle. The experience during these first four months of FY 2021 is not encouraging in that regard.

However, the ongoing vaccination campaign promises to restart the economic recovery that has stalled a bit in recent months due to the continuing, if not growing, concern about Covid-19 infections and with the tightening of restrictions on certain businesses. A widely vaccinated population with a safe and effective vaccine will serve the dual purpose of improving public health and improving economic health, and that will in turn help restore the ability of state and local budgets to fund legislative priorities.

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FIGURE 5. ALCOHOLIC BEVERAGE TAXES





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