



## **ABOVE-AVERAGE NEEDS; BELOW-AVERAGE EFFORT**

### **New National Study Ranks Texas 6<sup>th</sup> in Expenditure Need, But 37<sup>th</sup> in Revenue Effort**

A new national study, *Measuring Fiscal Disparities Across the U.S. States*, compares the revenue capacity and expenditure requirements of all 50 states and concludes that Texas has greater requirements for state and local spending than most other states, but makes less effort to raise the necessary revenue. The report is located at [http://www.urban.org/UploadedPDF/311384\\_fiscal\\_disparities.pdf](http://www.urban.org/UploadedPDF/311384_fiscal_disparities.pdf). All data are for fiscal year 2002.

#### **Measuring the Ability to Raise Revenue**

The study, released by the Tax Policy Center in Washington, D.C., and the Federal Reserve Bank of Boston, calculates each state's *revenue capacity*—the total revenue state and local governments could raise if they applied a national-average level of taxes and fees.

The first step is to determine the total tax base available, for instance, the amount of annual sales in a state or the total property value, minus common exemptions. Compared to the national average, Texas has just below the average amount of sales per capita, but only 78% of the average property value per capita.

Then the national-average tax rate is applied to each potential tax base. This gives the revenue capacity per capita. Texas' revenue capacity was \$4,271 per person, compared to a national average of \$4,659, for a ranking of 33<sup>rd</sup> among the 50 states.

#### **Measuring Actual Revenue Effort**

A state's *revenue effort* indicates how much a state and its local governments are taxing their available resources compared to other states. This is computed by dividing each state's actual per capita revenue collections by its theoretical per capita capacity.

Texas' actual revenue per capita was \$4,017—\$254 below its capacity at average tax rates. So even though Texas has a below-average total tax base to start with, it taps these potential revenue sources at a below-average rate. Texas' revenue effort ranks 37<sup>th</sup> among the 50 states.

#### **Measuring the Need for Public Services**

Texas' revenue effort should be compared to its need for revenue.

*Expenditure need* is defined as the amount that a state would have to spend on its residents to provide services typically offered by state and local governments. This calculation takes into account the socio-economic and demographic characteristics of the state, as well as the local cost of providing services. Needs are computed in six categories: K-12 education; higher education; health; highways; police and corrections; and public welfare.

For instance, the relative need for public education spending is determined by the number of school-age children and the proportion of those children living in poverty. This is then adjusted for the cost of providing education in Texas, such as teachers' salaries, compared to other states. (Texas' costs are slightly below the national average.)

The final calculation is to determine the per capita cost of meeting the need for public education, at the national average level of spending given the state's characteristics. Texas would need to spend \$1,659 per capita (not per student), compared to a national average of \$1,427, because of our disproportionately young and low-income population.

When all categories are considered, Texas has an expenditure need that is 7% higher than the national average—the 6<sup>th</sup> highest ranking of any state. Texas' need is \$6,496, compared to the national average of \$6,007.

**Measuring the Effort to Meet that Need**

A separate calculation is made of how much each state actually spends compared to the amount it would need to spend to provide the typical level of services. Texas spends only 79% of the amount calculated as necessary to meet the needs of its residents at the average national level—only \$5,127 per capita compared to a calculated need of \$6,456—ranking Texas 47<sup>th</sup> of the 50 states in *expenditure effort*.

**Calculating the Ability to Meet Needs**

The final calculation compares a state's revenue capacity (its ability to fund services) with its expenditure need (the cost of necessary services) to determine a state's *fiscal capacity*. A state with a low measure of fiscal capacity has a relatively high amount of need but a relatively low revenue base. This description fits Texas. Texas ranks 6<sup>th</sup> highest in need but 33<sup>rd</sup> in revenue capacity. Taken together, this gives Texas a rank of 39<sup>th</sup> in fiscal capacity.

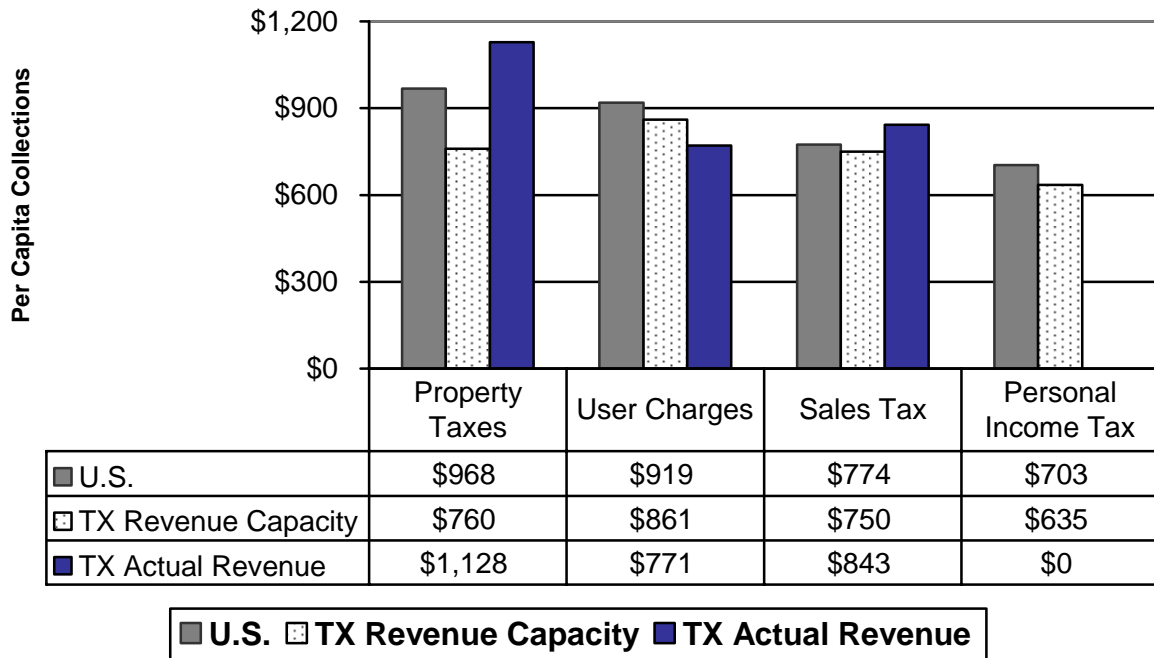
**What Should Texas Do?**

Texas needs to promote the growth of its tax base so that it will be able to better meet the needs of its residents. Over the long term, this will require investments in public services, particularly education, health and human services, and transportation.

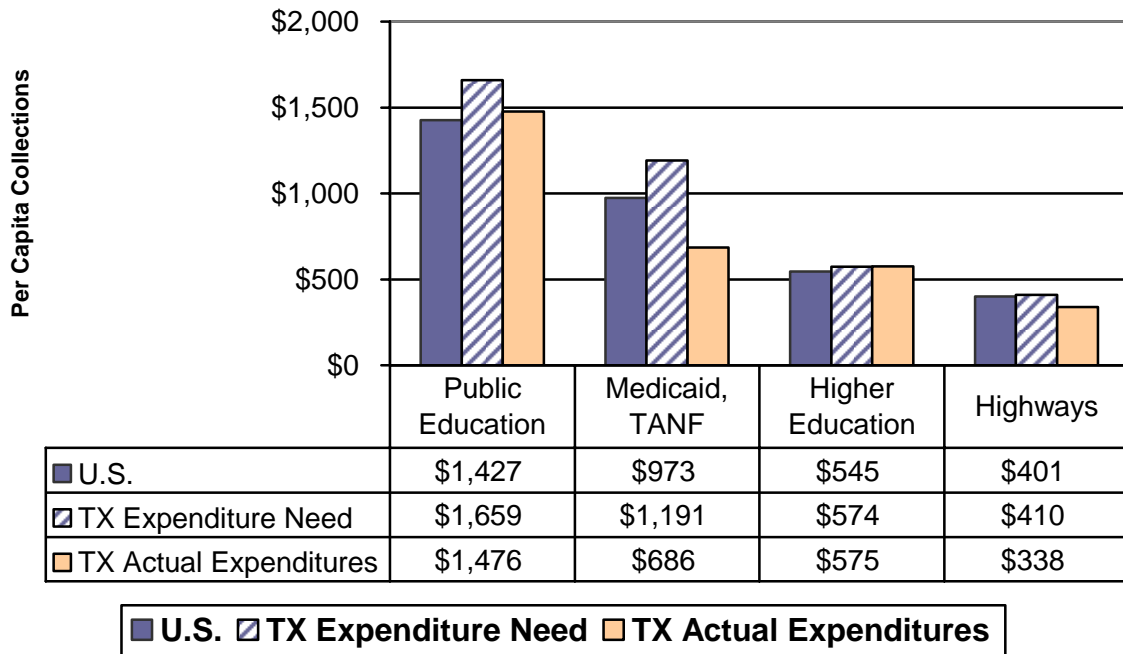
But in the short term, Texas needs to make more effort to tap the resources it does have available. If the state were to make only the national average level of revenue effort, it could generate an additional \$254 per capita—\$5.5 billion per year, \$11 billion over a state fiscal biennium.

	United States	Texas	
Revenue capacity	\$4,659	\$4,271	33 <sup>rd</sup>
Actual revenue	\$4,659	\$4,017	37 <sup>th</sup>
Expenditure need	\$6,007	\$6,456	6 <sup>th</sup>
Actual expenditure	\$6,007	\$5,127	47 <sup>th</sup>
Fiscal capacity	100	86	39 <sup>th</sup>

## Revenue Capacity vs. Actual Revenue, 2002



## Expenditure Need vs. Actual Expenditures, 2002



To make a donation, sign up for E-Mail Updates, or see our work, visit [www.cppp.org](http://www.cppp.org)