

Statistical Brief

Recessions Matter for State Tax Collections

The 1990-1991 recession was particularly challenging for State government finances. For fiscal year 1991, States experienced only a 3.3 percent rate of tax growth—the smallest rate of increase since the 2.7 percent increase following the 1957-58 recession.

This Statistical Brief presents and discusses U.S. Census Bureau data on State government taxes and finances.

Sales and Personal Income Taxes Dominate Collections

Of the \$311 billion in taxes collected by State governments in 1991, 65 percent (just over \$200 billion) came from the general sales and personal income taxes. State revenues are thus more sensitive to events that sway collections from these two tax categories than to events affecting other tax sources.

Recessions Affect Consumer Spending and Personal Earnings

Recessions are events with “big-time” consequences for State tax growth rates and revenue totals through their effects on retail

sales and personal income. During a recession:

- Consumer spending and retail sales fall, decreasing the growth of sales tax collections, if not their total amount.
- Higher unemployment and fewer work hours result in reduced income from personal earnings which, in turn, slows the growth in income tax collections.

The 1990-91 recession differed from previous recessions in two important ways that directly and adversely affected tax collection levels:

- First, there was very little inflation. During recessions

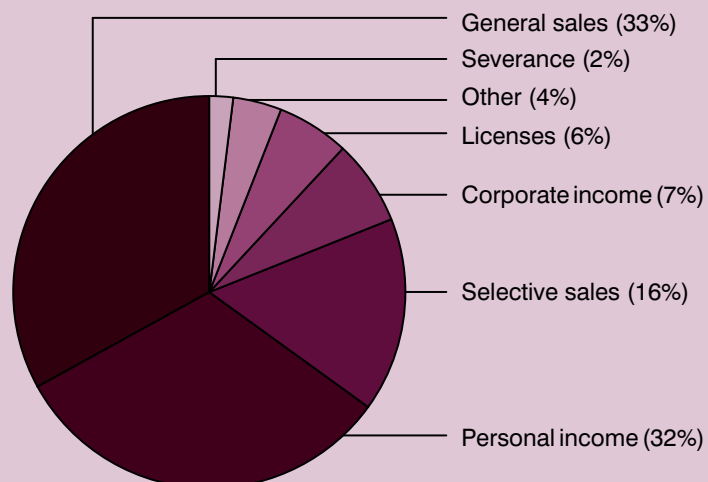
since 1970, inflation meant higher prices and increased sales tax collections. Inflation also pushed personal earnings into higher brackets, which enhanced income tax collections.

- Second, consumer spending (in real terms) fell slightly. In previous recessions, on average, consumer spending had slightly increased, which helped sustain sales tax revenue growth.

Tax Consequences Vary by State

Although the overall averages show that State tax revenue growth suffers from recession, some States escape the recessionary crunch.

Only Two Tax Sources Accounted for Nearly Two-Thirds of 1991 Collections



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States that rely most heavily on recession-sensitive sources of taxation should fare the worst. Those that rely the least on such sources should fare the best. The data bear this out.

- The 39 States that impose both a general sales and an individual income tax had only a 2.6 percent rate of tax growth in 1991, well below the 3.3 percent national average.
- The rate of tax growth in the seven States that have no personal income tax was 6.8 percent, and in the 5 States with no general sales tax, was 8.9 percent.
- Alaska — imposing neither a general sales tax nor a personal income tax—experienced a 17 percent rate of tax growth. Alaska relies upon a recession-indifferent tax source: about 89 percent of Alaskan State taxes come from the private business sector, which is dominated by the oil industry.

State Tax Collections Sustain State Expenditures

During 1991, about 56 percent of the dollars used for State expenditures came from State taxes. Put another way, tax collections are the States' primary funding source for meeting expenses.

After every recession (with a 1-year lag), this ratio drops. The 1991 figure—the lowest since 1950—represented a decline of three full percentage points from 1990 when tax revenues accounted for 59 percent of funds used for general expenditures.

Other funding sources States use for general expenditures include payments from the Federal government, service charges, and increased borrowing. However, Federal aid, with the exception of Medicaid, has not grown significantly. Charges are

only a small share of State revenues, and increased borrowing is not an option for many States that have statutory debt limitations.

Recessions Force States to Make Choices

The effect of a recession on State tax collections, therefore, often translates into one or more of the following policy alternatives:

- Change the tax structure to rely less upon recession-sensitive taxes.
- Raise the tax rate to increase tax collection totals.
- Seek additional funding from nontax sources of State revenues, such as Federal aid.
- Cut expenditures to match available revenues.
- Borrow funds (debt financing) to cover the difference between available revenues and expenditure commitments.

This is one of a series of occasional reports from the Census Bureau that provide timely information about our people and economy. The data presented come from an annual survey of government finances, are subject to sampling and nonsampling errors, and have been tested and found to meet applicable standards. See appendices of the reports cited below for a complete description of statistical methods, quality, and limitations.

Data Sources

State Government Tax Collections in 1991, State Government Finances in 1991, and Quarterly Summary of Federal, State, and Local Government Tax Collections.

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