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Fiscal Pressures and Revenue Diversification in the Great Plains

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Fiscal Pressures and Revenue Diversification in the Great Plains

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Introduction

Fiscal pressures have forced many Great Plains states to restructure their tax systems in recent years. The costs of general government, health care, education, and other factors have placed ever-growing pressures on state and local governments in the region. Once dominant tax sources are being replaced by what policy makers hope is an optimal mix of property, sales, income, and other taxes.

Policy makers are attempting to reformulate tax structures for several reasons:

- To fund government services more efficiently and in less distortionary ways;
- To fund services fairly and equitably;
- To consider externalities and spillover effects that cross state and/or regional lines;
- To consider the internal changes brought by trade patterns and international competitiveness.

In light of these motivations, we will examine sources of significant fiscal pressure on state and local governments and the changes that have taken place in revenue diversification among the Great Plains states from 1986 to 1992.

Sources of Fiscal Pressure

Table 1 shows that all ten of the Great Plains states have per capita expenditure levels below the U.S. average of $3,589. Spending in Nebraska ranks fifth among the ten states. While the overall level of government expenditures is low among the Great Plains states, there are clear differences in expenditure emphases in these states compared to the nation. The Great Plains states as a whole allocate a larger share of direct expenditures for education than the U.S. average. All ten Great Plains states spend less than the U.S. average for welfare.

While the overall level of government expenditures is low among the Great Plains states, there are clear differences in expenditure emphases in these states compared to the nation.

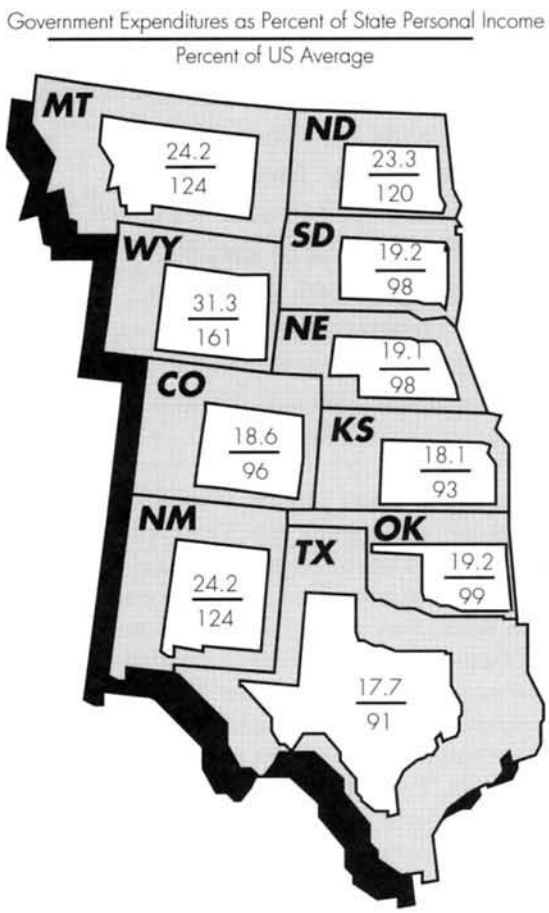
The Great Plains states picture changes, however, when expenditure levels are computed as a percent of income. While government expenditures measured in absolute terms are relatively low in the Great Plains states, they are high relative to income for some of them. Figure 1 illustrates state and local government expenditures as a percent of total state personal income and compares the state ratio to the U.S. average ratio of government expenditures to personal income. Four of the Great Plains states have very high levels of expenditure relative to income. Wyoming ranks highest with a expenditure to income ratio at 161% of the U.S. average. Nebraska ranks among the states with ratios below the U.S. average.

Table 1
State and Local Government Expenditures Per Capita
Great Plains States and U.S. Average, FY 1991

	Total ($)	K-12 Education ($)	K-12 Education (%)	Welfare ($)	Welfare (%)	Health and Hospitals ($)	Health and Hospitals (%)	Higher Education ($)	Higher Education (%)
Colorado	3,418	854	25.0	361	10.6	237	6.9	401	11.7
Kansas	3,200	804	25.1	339	10.6	282	8.8	391	12.2
Montana	3,499	918	26.2	432	12.4	203	5.8	260	7.4
Nebraska	**3,267**	**890**	**27.2**	**390**	**11.9**	**279**	**8.5**	**409**	**12.5**
New Mexico	3,357	831	24.8	367	10.9	320	9.5	438	13.1
North Dakota	3,541	771	21.8	443	12.5	145	4.1	509	14.4
Oklahoma	2,888	731	25.2	384	13.2	302	10.4	287	9.9
South Dakota	2,949	779	26.4	314	10.7	168	5.7	243	8.2
Texas	2,896	803	27.7	318	11.0	262	9.0	319	11.0
Wyoming	2,238	1,261	24.9	331	6.5	530	10.5	498	9.8
U.S. Average	***3,589***	***865***	***24.0***	***504***	***14.0***	***322***	***8.9***	***312***	***8.7***

Source: U.S. Advisory Commission on Intergovernmental Relations, *Significant Features of Fiscal Federalism, Volume 2 Revenues and Expenditures.*

Figure 1
State and Local Direct Expenditure as a Percent of Personal Income and Comparison to U.S. Average, 1991



Education

Nine of the ten Great Plains states allocate a larger fraction of their budgets to K-12 education than the U.S. average. Eight of the ten states also spend more on higher education than the U.S. average. As a result of the relatively high K-12 expenditures per capita in these states, there generally is more reliance on the local property tax as a funding source for education. Nebraska is among the Great Plains states with relatively heavy property tax reliance.

Health Care

Health care expenses are putting fiscal pressure on states. Medicaid expenditures, funded by both federal and state sources, have far exceeded the rate of increase in the general price level. Table 2 provides an overview of Medicaid expenditures in the Great Plains states from 1987 to 1992. Total expenditures approximately doubled over the five year period, and Medicaid accounted for a rising share of state general expenditures in all but one of the states. Medicaid expenditures as a portion of state expenditures in Nebraska rose from 9.6 percent to 11.6 percent during the period.

Given the difficulty of restricting services, the pressure builds to raise taxes to ease these fiscal pressures. While it is tempting to solve the problem with incidental taxes such as cigarette and liquor excise taxes, the scope for doing so is limited. In the absence of a federal solution to the health care financing dilemma, there will be increasing pressure for states to craft their own creative remedies. Unless service cuts are found acceptable, major

Table 2
State Medicaid Expenditures, Selected Years
Total and as a Percent of State General Expenditures
($ millions)

	1987		1990		1992	
	($)	(%)	($)	(%)	($)	(%)
Colorado	399	8.9	584	11.0	985	16.3
Kansas	249	6.9	409	8.6	554	10.1
Montana	144	9.3	172	10.1	250	10.4
Nebraska	**195**	**9.6**	**311**	**11.3**	**401**	**11.6**
New Mexico	192	7.1	279	7.3	483	11.6
North Dakota	166	13.6	174	11.5	200	13.2
Oklahoma	525	10.4	706	11.7	1,009	13.7
South Dakota	114	10.8	160	13.8	229	16.1
Texas	824	4.6	3,069	13.0	6,312	21.2
Wyoming	41	2.4	62	4.5	110	8.3

Source: U.S. Advisory Commission on Intergovernmental Relations, *Significant Features of Fiscal Federalism, Volume 2 Revenues and Expenditures.*

In the absence of a federal solution to the health care financing dilemma, there will be increasing pressure for states to craft their own creative remedies.

state taxes must be considered in order to provide the substantial revenues needed.

State initiatives also are needed to address the growing lack of access to health care. Factors leading to lack of access include the inability of many people to obtain health insurance and a disproportionate rise in the cost of health care as compared to the general price level.

Revenue Diversification

Indices of revenue reliance have been computed in order to examine the pattern of revenue source reliance among Great Plains states (Suyderhoud 1994). The higher the value of the index (approaching one) the more diversified is the state's tax structure. The lower the value of the index (approaching zero) the less diversified is the tax structure.

Computing the indices using the three major revenue sources (property, individual income, and sales taxes) the Great Plains states were, on average, less diversified than other states. Four of the Great Plains states ranked among the ten least diversified states in the country (Table 3). Among the Great Plains states, index values ranged from a high of 0.98 in Oklahoma to a low of 0.55 in Montana. The most diversified states in the region, including Nebraska, were those with index scores of 0.89 or greater.

Table 4 modifies the indices by including corporate income tax revenues with individual income tax revenues. The largest changes occurred in Colorado, North Dakota, and Oklahoma all of whom jumped in the relative rankings six to ten places. Nebraska fell three places in the rankings with the inclusion of the corporate tax.

Expanding the list of revenue sources to capture all other revenue sources, including non-tax revenues, had a significant affect on the rankings of Colorado, North Dakota and Oklahoma (Table 5). Each of these states dropped dramatically in the rankings. On the other hand, Nebraska jumped five places in the rankings. Utilizing the expanded list of revenue sources resulted in six of the ten Great Plains states being among the ten least revenue-diversified states in the nation.

Recent Changes

Some of the Great Plains states recently have made major changes in their funding sources. For example, Nebraska raised its state income and sales taxes in 1990 to reduce reliance on property tax funding for public schools. Figure 2 shows estimates of the revenue indices for the Great Plains states in FY 1991. Comparing the major revenue source indices and the modified indices in 1986 with the corresponding 1991 indices reveals that

Table 3
Major Tax Revenue Diversification Indices, FY 1986

	Property Tax Revenue (%)	Individual Income Tax Revenue (%)	General Sales/ Gross Receipts Tax Revenue (%)	Index of Diversification	State Rank
Colorado	41.98	23.58	34.45	0.97	17
Kansas	50.35	22.36	27.28	0.93	29
Montana	75.57	24.43	0.00	0.55	49
Nebraska	**54.94**	**20.88**	**24.18**	**0.89**	**34**
New Mexico	19.97	9.72	70.31	0.68	45
North Dakota	49.51	14.68	35.81	0.91	32
Oklahoma	30.28	26.94	42.78	0.98	14
South Dakota	57.61	0.00	42.38	0.73	40
Texas	61.51	0.00	38.49	0.71	42
Wyoming	72.55	0.00	27.45	0.60	47

Source: Suyderhoud, 1994

Nebraska was among the four states that made significant progress in diversifying their tax sources over the five-year period. A comparison of the indices calculated from all revenue sources shows that each of the Great Plains states improved their revenue diversification from 1986 to 1991.

While all of the Great Plains states have improved their revenue diversification in recent years, Montana, South Dakota, Texas, and Wyoming are still among the least diversified states in the U.S. The principal cause of this lack of revenue diversification is the absence of one of the three major taxes in each of these states: Montana has no sales tax, while South Dakota, Texas, and Wyoming have no income tax.[1] Other tax revenue sources compensate, but still leave these states relatively less diversified than others.

Future Directions

Revenue diversification has been a standard policy prescription for the past generation. The recommendation that state tax structures rely ap-

[1] *While South Dakota has no individual income tax, it does have a corporate income tax.*

Table 4
Modified Tax Revenue Diversification Indices, FY 1986

	Property Tax Revenue (%)	Corporate/Individual Income Tax Revenue (%)	General Sales/ Gross Receipts Tax Revenue (%)	Index of Diversification	State Rank
Colorado	40.8	25.72	33.48	0.98	10
Kansas	47.5	26.76	25.74	0.96	26
Montana	69.77	30.23	0.00	0.63	48
Nebraska	**53.21**	**23.36**	**23.42**	**0.91**	**37**
New Mexico	18.7	15.49	65.82	0.76	42
North Dakota	44.5	23.32	32.18	0.97	22
Oklahoma	29.06	29.88	41.06	0.99	8
South Dakota	55.38	3.87	40.74	0.79	40
Texas	61.51	0.00	38.49	0.71	44
Wyoming	72.55	0.00	27.45	0.60	49

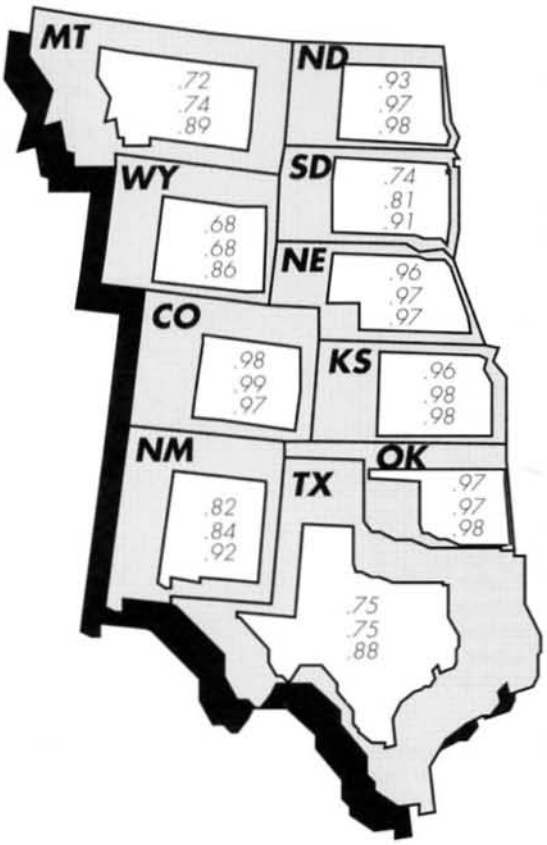
Source: Suyderhoud, 1994

Table 5
Diversification Indices, All Revenue Sources, FY 1986

	Property Tax Revenue (%)	Corporate/Individual Income Tax Revenue (%)	General Sales/ Gross Receipts Tax Revenue (%)	Other Revenue (%)	Index of Diversification	State Rank
Colorado	23.13	14.58	18.98	43.32	0.94	17
Kansas	25.46	14.34	13.79	46.40	0.91	29
Montana	30.67	13.29	0.00	56.04	0.77	44
Nebraska	**27.93**	**12.26**	**12.29**	**47.52**	**0.89**	**32**
New Mexico	5.76	4.77	20.27	69.20	0.63	50
North Dakota	16.85	8.83	12.18	62.15	0.75	45
Oklahoma	12.10	12.44	17.09	58.37	0.80	40
South Dakota	27.27	1.91	20.06	50.76	0.84	38
Texas	26.36	0.00	16.50	57.14	0.77	43
Wyoming	26.49	0.00	10.02	63.49	0.69	49

Source: Suyderhoud, 1994

Figure 2
Revenue Diversification Indices in Great Plains States, FY 1991



proximately equally on property, sales, and income taxes has only recently been questioned. Variations in economic activity and tax policy goals across states suggest that tax structures should be customized to optimize the mix of revenue sources in each state. A technique called optimal revenue portfolio modeling recently has been used by researchers to capture multiple policy objectives and determine the optimal mix of tax revenue sources for given states in the southern and eastern U.S.

Although this technique has not been applied to states in the Great Plains region, we would expect that unique attributes of the Great Plains states and their voting populaces would result in optimal tax portfolios distinct from those of states in other regions. While increased diversification is occurring, there is no reason to believe, or hope, that the Great Plains states' revenue patterns will continue to look increasingly like those of other states.

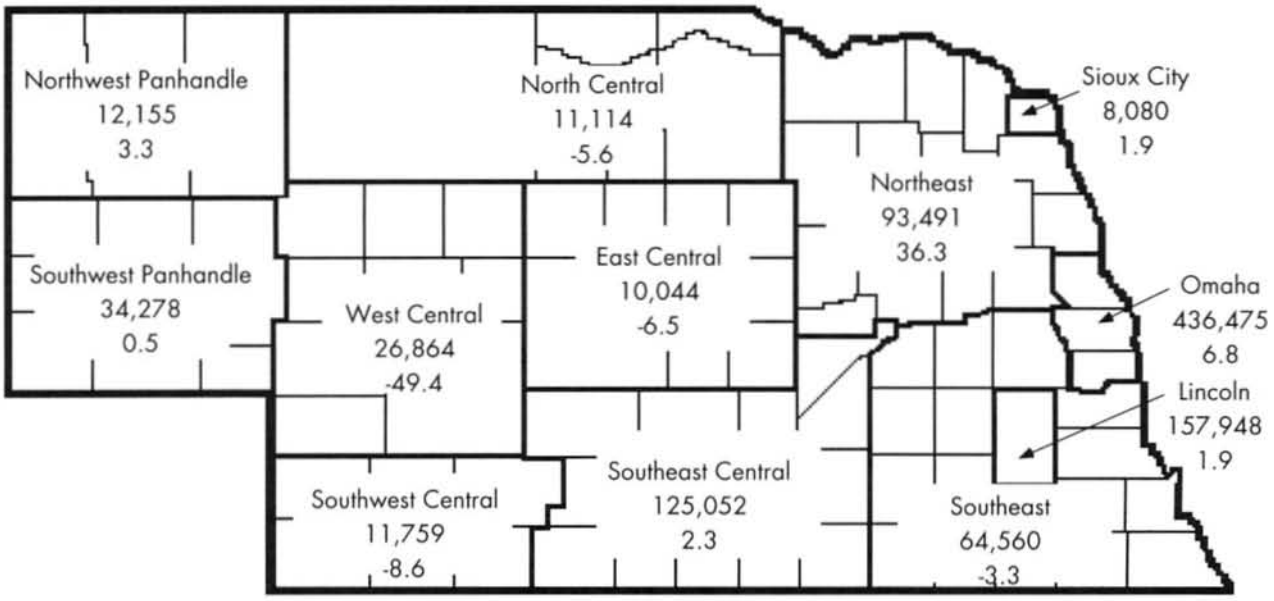
State and local governments in the Great Plains should think creatively about their revenue sources in the face of increasing decentralization of government services over the next several years. A Great Plains regional approach in tax policy could generate significant advantages worthy of consideration.

Reference

Suyderhoud, Jack P., 1994, State-Local Revenue Diversification, Balance, and Fiscal Performance, *Public Finance Quarterly* 22:168-194.

November 1994 Regional Retail Sales and Percent Change from Year Ago

($000)



Price Indices

	January 1995	% Change vs Year Ago	YTD % Change vs Year Ago
Consumer Price Index - U* (1982-84 = 100)			
All Items	150.3	2.8	2.8
Commodities	135.1	2.3	2.3
Services	165.9	3.2	3.2

U* = All urban consumers

Source: U.S. Bureau of Labor Statistics

Employment in Nebraska

	Revised November 1994	Preliminary December 1994	% Change vs Year Ago
Place of Work			
Nonfarm	803,495	794,769	2.9
Manufacturing	108,454	109,017	4.4
Durables	52.494	53,197	6.9
Nondurables	55,960	55,820	2.2
Mining & Construction	35.762	32,678	0.1
TCU*	48,617	49,515	3.7
Trade	201,120	202,053	2.4
Retail	146,423	147,155	1.2
Wholesale	54,697	54,898	5.8
FIRE**	50,496	50,394	-0.1
Services	198,573	197,103	4.6
Government	160,473	154,009	1.6
Place of Residence			
Civilian Labor Force	873,931	862,688	1.2
Unemployment Rate	2.1	2.4	

* Transportation, Communication, and Utilities
** Finance, Insurance, and Real Estate

Source: Nebraska Department of Labor

City Employment October 1994 Percent Change from Year Ago

The State and Its Trading Centers	Employment (1)
NEBRASKA	2.0
Alliance	2.0
Beatrice	3.7
Bellevue	0.1
Blair	0.1
Broken Bow	5.7
Chadron	2.2
Columbus	3.9
Fairbury	2.3
Falls City	3.0
Fremont	2.5
Grand Island	2.6
Hastings	2.7
Holdrege	4.7
Kearney	3.5
Lexington	2.5
Lincoln	-0.1
McCook	3.0
Nebraska City	3.7
Norfolk	3.0
North Platte	2.7
Ogallala	4.7
Omaha	0.1
Scottsbluff/Gering	3.5
Seward	3.6
Sidney	3.4
South Sioux City	-1.2
York	4.2

(1) As a proxy for city employment, total employment (labor force basis) for the county in which a city is located is used.

Sources: Nebraska Department of Labor

Nonmotor Vehicle Net Taxable Retail Sales in Nebraska Cities

	November 1994 ($000)	% Change vs Year Ago
Omaha	394,165	6.9
Lincoln	156,448	2.0
Grand Island	44,509	4.3
Kearney	26,111	10.6
Norfolk	25,660	6.1
Fremont	20,452	3.0
North Platte	19,676	2.6
Hastings	19,669	4.7
Scottsbluff	18,731	1.6
Columbus	18,518	2.0
Bellevue	14,893	7.8
Beatrice	9,200	0.1
McCook	8,396	-4.3
York	7,896	6.0
La Vista	7,253	20.1
South Sioux City	7,075	0.1
Lexington	6,765	-4.1
Sidney	6,415	9.5
Blair	5,824	8.5
Alliance	5,391	6.8
Nebraska City	4,834	9.3
Ogallala	4,588	3.2
Seward	4,320	1.0
Holdrege	4,231	-13.1
Broken Bow	3,789	-1.5
O'Neill	3,757	-3.2
Gretna	3,732	-7.6
Crete	3,674	-4.2
Chadron	3,302	12.2
Gering	3,278	-12.6
Valentine	3,099	4.1
Fairbury	2,986	-6.5
West Point	2,898	-10.1
Papillion	2,896	-12.1
Cozad	2,698	-5.9
Wayne	2,673	-19.0
Plattsmouth	2,639	2.1
Wahoo	2,258	-4.7
Aurora	2,257	4.5
Ralston	2,246	-4.3
Auburn	2,209	-5.2
Falls City	2,198	-7.7
Schuyler	1,878	-12.6
Ord	1,870	0.5
Gothenburg	1,867	-4.0
Ainsworth	1,770	-10.3
Gordon	1,624	-10.1
Hartington	1,618	-12.1
Minden	1,604	12.0
Albion	1,547	-6.8
Kimball	1,516	-12.5
Hebron	1,487	-10.3
Geneva	1,426	-7.1
David City	1,398	-10.0
Superior	1,361	-9.6
Central City	1,339	-1.2
Imperial	1,317	-14.0
Elkhorn	1,238	-2.1
Neligh	1,165	-4.9
Ceresco	1,165	21.6
St. Paul	1,095	-13.2
Creighton	1,068	2.3
Tekamah	954	-4.1
Stromsburg	949	-6.8
Tecumseh	942	-9.0
Sutton	922	-2.3
Bridgeport	916	-4.5
Syracuse	826	0.7
Valley	766	-23.5
Ashland	758	-31.5
Mitchell	754	-3.9
Grant	737	-0.9
Burwell	693	-5.7
Red Cloud	690	-3.5
Gibbon	673	-0.9
Osceola	668	-4.2
Plainview	620	-8.8
Doniphan	618	45.1
Weeping Water	617	-38.0
Atkinson	616	-18.5
Arapahoe	613	-3.0
Waverly	613	14.4
Milford	592	-12.2
Humphrey	589	-13.0
Ravenna	583	-22.4
Battle Creek	575	-26.0
Alma	574	-3.9
Wisner	561	-14.7
Shelton	553	-19.9
Oakland	546	-5.0
Pierce	532	-16.9
Bloomfield	528	-12.1
Rushville	523	-6.9
Pender	520	-14.2
Fullerton	515	-6.9
Cambridge	513	-6.0
Stanton	492	-6.3
Friend	490	-0.4
Loup City	481	-15.0
Oshkosh	471	17.2
Lyons	455	-14.8
Franklin	449	-12.1
Blue Hill	424	5.2
Humboldt	417	-9.9
Benkelman	409	-8.1
Elgin	407	-3.6
Bayard	407	6.3
Crawford	406	2.0
Chappell	401	5.5
North Bend	398	-1.0
Dakota City	395	106.8
Ponca	388	-1.0
Scribner	377	-10.7
Madison	377	-48.3
Tilden	371	-12.9
Wilber	368	-26.3
Bassett	362	-23.9
Henderson	353	1.4
Clarkson	352	23.1
Wood River	349	-2.2
Oxford	332	-4.0
Wymore	325	-14.0
Randolph	317	0.3
Morrill	315	1.3
Laurel	314	-13.3
Wakefield	308	-19.4
Wauneta	307	-5.2
Shelby	295	-6.3
Crofton	291	-2.3
Hay Springs	287	-16.3
Elwood	286	1.4
Pawnee City	282	-7.2
Osmond	277	-43.8
Emerson	267	-26.0
Louisville	260	-25.9
Curtis	250	-21.6
Minatare	246	22.4
Newman Grove	239	-22.4
Genoa	236	-7.1
Hooper	235	-4.9
Clay Center	232	-21.6
Bennington	230	-3.8
Arnold	229	-7.3
Dodge	219	-9.5
Sutherland	217	-15.2
Eagle	216	38.5
Deshler	200	17.6
Elm Creek	195	-27.5
Cairo	194	-1.0
Juniata	190	-12.8
Hickman	185	-14.4
Utica	182	-5.7
Sargent	168	-24.3
Arlington	162	-31.6
Beaver City	149	4.9
Bertrand	136	-20.0
Springfield	135	10.7
Fairmont	117	-30.8
Kenesaw	115	5.5
Axtell	102	25.9

Source: Nebraska Department of Revenue

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County of the Month

Grant

Hyannis—County Seat

Next County of Month

License plate prefix number: 92
Size of county: 775 square miles, ranks 27th in the state
Population: 769 in 1990, a change of -12.3 percent from 1980
Median age: 35 years in Grant County, 33.0 years in Nebraska in 1990
Per capita personal income: $16,831 in 1992, ranks 66th in the state
Net taxable retail sales ($000): $3,522 in 1993, a change of -8.5 percent from 1992; $3,129 during January-November 1994, a change of 5.0 percent from the same period one year ago
Number of business and service establishments: 22 in 1992, 68.2 percent had less than five employees
Unemployment rate: 0.9 percent in Grant County, 2.9 percent in Nebraska for 1993

Nonfarm employment (1993):

	State	Grant County
Wage and salary workers	762,703	153
	(percent of total)	
Manufacturing	13.5%	(D) %
Construction and Mining	4.3	(D)
TCU	6.2	(D)
Retail Trade	18.4	(D)
Wholesale Trade	6.8	(D)
FIRE	6.6	(D)
Services	24.6	8.5
Government	19.6	53.6
Total	100.0%	100.0%

(D) Data unavailable because of disclosure suppression

Agriculture:
Number of farms: 82 in 1992, 92 in 1987
Average farm size: 6,656 acres in 1992
Market value of farm products sold: $11.0 million in 1992 ($133,773 average per farm)

Sources: U.S. Bureau of the Census, U.S. Bureau of Economic Analysis, Nebraska Department of Labor, Nebraska Department of Revenue

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