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Consumption taxes can finance public education

Income tax aficionados spend a great deal of time looking for problems needing their economically dangerous solution. Most recently, that problem has been education finance. Not any longer.

On Oct. 22, President Bush signed the "American Jobs Creation Act of 2004." Among other things, the legislation re-established the itemized deduction of state and local sales taxes, thus restoring a critical income tax deduction lost to Texans in the late 1980s. While significant for many reasons, it bears directly on the school finance debate.

As the Legislature has grappled with alternatives to public school finance, consumption taxes have been the only agreed-upon ingredient in nearly every plan. Every plan except those promoted by income-tax-now advocates.

Dr. George Zodrow, writing for the Joint Select Committee's final report argued, "Broadening the sales tax base to include a wider variety of consumer goods and services is generally desirable."

Additionally, the substance of Senate Bill 2 (2003 regular session), at least one plan developed by Dr. Caroline Hoxby, and elements of the Governor's plan relied on consumption taxes as a means of raising revenue to both finance a cut in property taxes and eliminate the current system of recapture.

There are good reasons that consumption taxes consistently appear as a reasonable alternative to the property tax to fund schools.

Consumption taxes are built on the fact that consumers almost always pay all the taxes, and in that way, they are fair and broad-based.

Former Governor Bush's tax panel affirmed this point: "While both businesses and individuals pay taxes, ultimately the bulk of business taxes is passed on to individuals, either directly through higher prices, or indirectly through lower wages, dividends and investment returns."

Put another way, businesses are simply tax collectors for the state - they don't pay taxes, people do. Consumption taxes just make the process more transparent.

That very transparency makes them fair and predictable. The fact that homeowners complain about their property taxes is manifestly one of the few good features of

the current system: they know what they are paying and must write a check each year to a Central Appraisal District.

The most insidious taxes are those hidden from view, or where the taxpayer doesn't have a clue he is paying the bill anyway. The best system would require direct payments from the taxpayer to the state or to local school districts to fund public education. Consumption taxes are similar to property taxes in that respect.

Additionally, consumption taxes have been a remarkably reliable source of revenue since their adoption being adopted in 1961. In today's dollar, Texas taxpayers paid \$7.3 billion in state taxes in 1972.

By 2001, the amount had grown to \$22.7 billion—a 6.2 percent average annual increase. Economic and population growth accounted for 43.4 percent of the increase, and net legislative changes (tax increases less tax relief) accounted for the remainder—56.6 percent.

According to economist Ray Perryman, "The expanded sales tax base is superior to property taxes, franchise taxes, and the current sales tax base. It has slightly, but not materially, less expansion capacity than the base of a gross receipts tax or a business activity tax, two other alternatives that are receiving at least some attention."

In 2005 the Legislative Budget Board estimates school taxes would bring in about \$17.5 billion for maintenance and operations (M&O). By broadening the sales tax, it is possible to reduce the school M&O property tax significantly while reducing the sales tax rate. Across the state, local sales tax rates would drop due to the broader tax base.

Reducing property taxes significantly would provide a substantial increase in investment. The long run result would be increased economic growth and, ultimately, more jobs than would otherwise exist in this state.

Finally, net revenues would gradually rise, making further rate decreases possible in the future.

Now that Congress and President Bush have made sales taxes deductible again, consumption taxes are an even more attractive alternative for financing public education.

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