Analysis of Fiscal Policy in Nevada

An Overview of the Approach and Findings of the Governor's Task Force on Tax Policy in Nevada

Presentation Overview

♦ Assembly Concurrent Resolution 1
– Requirements
– Fundamental assumptions

♦ Task Force approach
– Phase I: assumption validation & problem assessment

– Phase II: Analysis of revenue alternatives & Task Force recommendations

Presentation Approach

- ♦ Assembly Concurrent Resolution 1 provides a road map

- ♦ Reflects the "stepwise" process undertaken by the Task Force

- ♦ Analytical elements highlighted for illustrative purposes

- ♦ Policy considerations discussed, but limited by the Task Force's belief that policy questions were best left to the Legislature

3

Assembly Concurrent Resolution 1

Requirements & Assumptions

A.C.R. 1 - Requirements

- ♦ Task Force appointments

- ♦ The identification of taxes to be reviewed at first meeting

- ♦ A collective review of fees and charges

- ♦ Solicitation of the executive branch, businesses, labor organizations, and local governments

5

A.C.R. 1 – Requirements (cont.)

- ♦ Consideration of lowering the retail sales and use tax rate

- ♦ The development of one or more proposal to:
  - – Carry out the state's need to provide additional revenue for state programs;
  - – Stabilize the tax base; and
  - – Reduce the long-term structural deficit of the state budget

- ♦ "[A]ny recommended legislation must include a plan to broaden the tax base so that it is reflective of the diversity of the state's economy…"

6

A.C.R. 1 – Assumptions

- Nevada's population is growing faster than its public revenues

- It is becoming increasingly costly to provide needed public services

- A disparity between revenues from ***current revenue sources*** and public spending needed to maintain ***current governmental services*** has created a "structural deficit"

- A broad-based tax structure that is reflective of the diversity of Nevada's economy is a desirable public policy

Questions Presented

- What is the extent of the disparity between public revenue growth and the cost to maintain current service levels?

- Is this problem short term, or is it systemic?

- What are the underlying factors contributing to the problem, and how might they be mitigated?

The Task Force's Approach
Key Findings

Task Force Approach

♦ Step 1: Review of the state's economy and development of baseline assumptions

♦ Step 2: Review state's fiscal system, including historical revenue and spending trends

♦ Step 3: Defining the framework of the state's fiscal problem (*i.e.*, what is a structural deficit?)

Task Force Approach (cont.)

♦ Step 4: General fund outlook (measuring the extent of the problem)

♦ Step 5: State-to-state comparison of revenues and expenditures

♦ Step 6: Comparative analysis of revenue alternatives

Task Force Approach (cont.)

♦ Step 7: Recommendation development and scenario testing

♦ Step 8: Identification of additional and supplemental issues/considerations

Key Findings:
Economic Overview

♦ Population and employment growth are slowing

♦ Nevada's economy is diversifying, but remains among the narrowest in the nation

♦ Nevada's economy is not recession proof

♦ Persons over the age of 65 and ages 5 through 17 have grown to represent an increasing share of the state's population

13

Key Findings:
State's Fiscal System

♦ Constitutional and policy constraints have made the state's fiscal system inflexible

♦ The state's revenue system is particularly narrow

♦ Considerable use of earmarking

♦ Inflation-adjusted, per capita revenues have been declining, similar trend with regard to revenue as a percentage of personal income

14

Key Findings:
Defining the Problem

- Structural deficit is defined as a revenue / expenditure imbalance

- Revenue stability & sufficiency are both issues

- Selected contributing factors:
  - Changing demographics
  - Economic diversification and relative tax contribution
  - Less construction activity
  - Revenue sources not adjusting with inflation
  - Internet market penetration

Key Findings:
Nevada Fiscal Outlook (General Fund)

- Projected revenue growth: 4%
- Projected expenditure growth: 6%

- Projected gap in 2003-05: $705 million
- Projected gap in 2009-11: $1.4 billion

- Annual inflation-adjusted, per capita growth:
  - Revenues: -1%
  - Expenditures: +1%

Key Findings:
Nevada's Place Among the 50 States

♦ Nevada ranks 30th nationally in state taxes generated per capita and 32nd in state taxes generated as a percentage of income

♦ Sales and gross receipts taxes accounted for 86 percent of all state taxes, double the national and western states average

♦ Nevada ranked 50th in state and local revenues received from the federal government per capita

17

Key Findings:
Comparative Analysis of Revenues

♦ There is no perfect tax, nor a perfect fiscal system

♦ Taxes focused on by the Task Force were those:
  – That "broadened" the tax base;
  – That increased overall system equity and stability;
  – With relatively with low compliance and administrative costs;
  – Managed cash flow; and
  – Addressed inflation issues

♦ More of an effort in information gathering as opposed to a statistical measure of preference

18

Key Findings:
Additional Considerations

♦ Expenditure accountability is important

♦ Technological investments are necessary

♦ The state's sales and use tax bases remains narrow

♦ Increasing the state's proportional allocation of federal funds should be a priority

♦ Unfunded mandates may be increasingly problematic

♦ Economic diversity is important to Nevada's future

♦ Fiscal analysis is an on-going process

19

Key Findings:
Recommendations & Scenario Testing

♦ Several alternatives were evaluated

♦ Task Force recommendations:

– Provided sufficient revenues to sustain current service levels through 2011;

– Balanced near-term cash flow and longer term structural objectives;

– Reflected the diversity of the state's economy and attempted to spread the burden over all "taxpayer groups" (no silver bullet);

– Included measures to increase system efficiency, stability, and equity;

– Adjusted taxes which have eroded due to inflation and were considerably lower compared to other western states; and

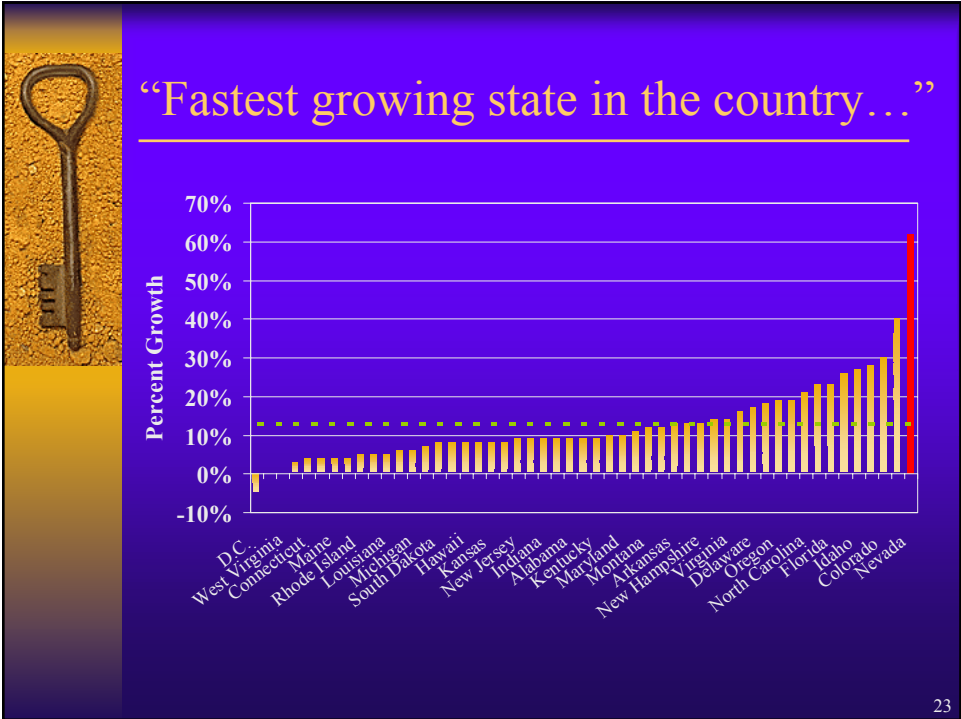– Included two new levies: 1) State Admissions and Amusement Tax and 2) State Activity Tax

20

Phase I: Assumption Validation and Problem Assessment

Validation of Assumptions

Clause 1

"Nevada is the fastest growing state in the country, with the biggest gains being made in the populations of school-aged children and senior citizens…"

"Fastest growing state in the country…"

A bar chart titled with y-axis "Percent Growth" ranging from -10% to 70%, with states along the x-axis: D.C., West Virginia, Connecticut, Maine, Rhode Island, Louisiana, Michigan, South Dakota, Hawaii, Kansas, New Jersey, Indiana, Alabama, Kentucky, Maryland, Montana, Arkansas, New Hampshire, Virginia, Delaware, Oregon, North Carolina, Florida, Idaho, Colorado, Nevada.

"Biggest gains being made in the populations of school-aged children and senior citizens…"

Selected Population Groups Per 100 Residents
1990 and 2001

Population Groups	1990	2001	Relative Growth
School-Aged Children	17.2	18.0	4.9%
Seniors	10.5	11.1	6.3%

Validation of Assumptions

Clause 2

"The rate of growth of Nevada's population is much faster than the rate of growth of its public revenue…"

"Growth of…population is…faster than…growth of…public revenue…"
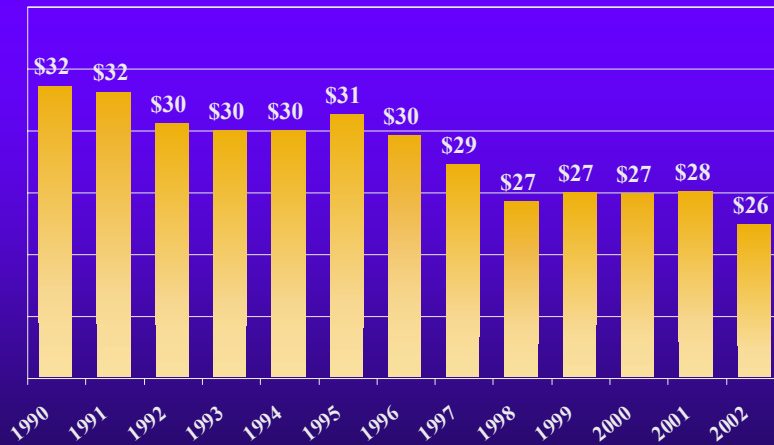
♦ Inflation adjusted revenues per capita
  – State of Nevada
    • 1992: $2,110
    • 2001: $2,010

  – State of Nevada General Fund
    • 1992: $820
    • 2001: $790

General Fund Revenue Per $1,000 of Personal Income

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
$32	$32	$30	$30	$30	$31	$30	$29	$27	$27	$27	$28	$26

Validation of Assumptions

Clause 3

"Nevada is falling behind in the revenue collections needed for funding K-12 education, for meeting the long-term care needs of its growing senior population, and for keeping pace with soaring energy demands and the costs of those demands; and…"

Validation of Assumptions

Clause 4

"When there is a disparity between the growth in revenues from current revenue sources and the growth in public spending needed to maintain current governmental services, a structural deficit in the state budget arises…"

Problem Assessment

♦ Step 1: project general fund revenue sources

♦ Step 2: model general fund expenditures by category

♦ Step 3: balance revenues and expenditures to identify the extent of the "gap" (should one exist)

Key Assumptions

- Long-term in nature (*e.g.*, applying average growth rates to smooth trends)

- Projection period: FY 2001-02 through FY 2010-11

- Maintaining current service levels

- Existing revenue sources only

- Did not attempt to project/reflect the uncertainty of world events
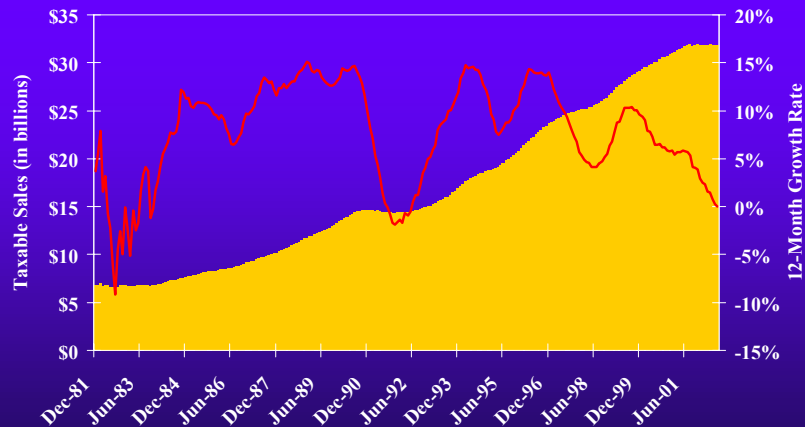
Step 1: Revenue Outlook

Revenues Reviewed

♦ Primary sources
– Retail sales and use
– Gaming fees & taxes
– Insurance premium
– Casino entertainment
– Excise taxes
– Business license
– Mining tax
– Car rental fees

♦ Secondary sources
– Licenses
– Fees
– Fines
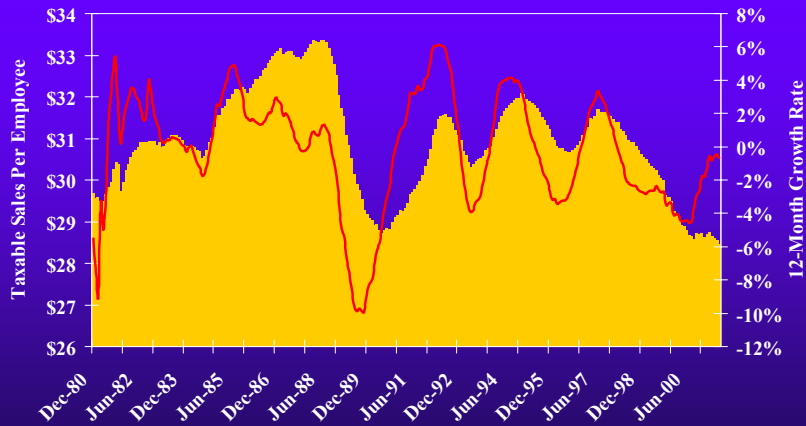– Use of money and property
– Other revenues

33

Taxable Retail Sales, 1981 - 2002

34

Inflation Adjusted Taxable Sales Per Employee, 1980 - 2002

35

Factors Impacting Sales Tax

♦ Less construction activity

♦ Slower economy (domestic and abroad)

♦ Increasing market penetration by Internet retailers

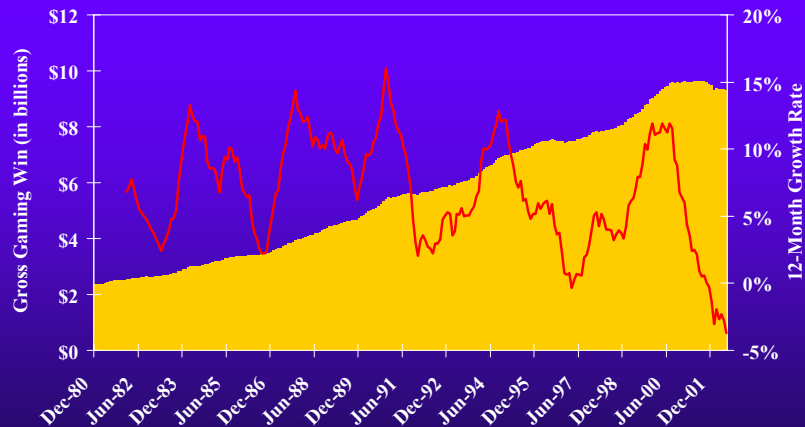♦ Economy diversifying away from tourism

♦ Increased spending on services

36

Illustrative Example

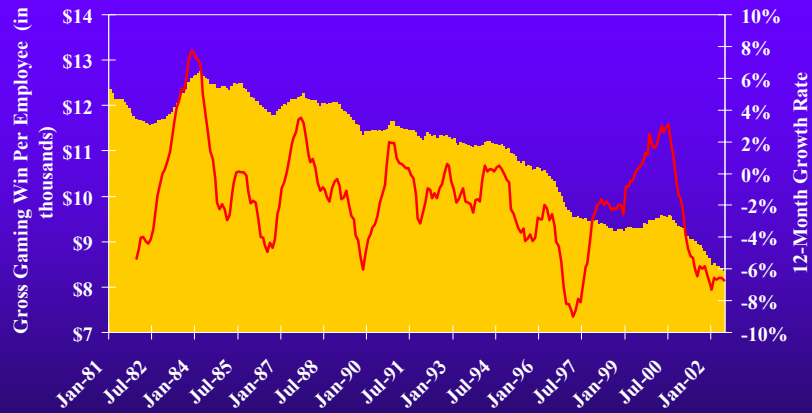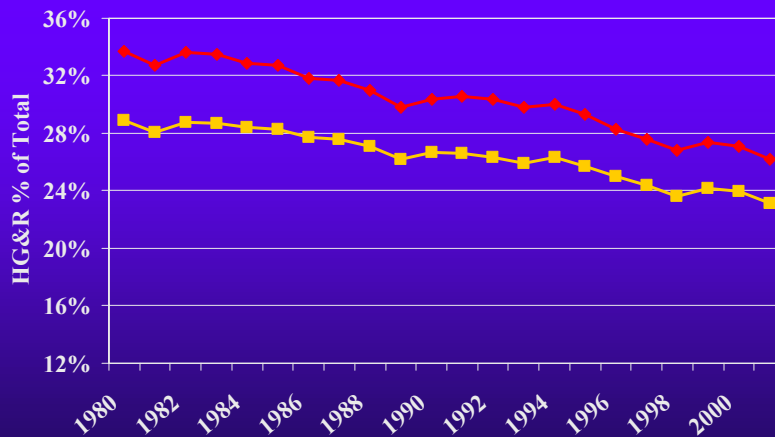|	HH 1	HH 2	Change
Households (HH)	100,000	110,000	+ 10,000
Taxable spending per HH	$10,000	$10,000	$0
Internet spending per HH	$1,000	$1,500	+ $500
Total taxable sales per HH	**$653**	**$616**	**- $37**

Gross Gaming Win, 1980 - 2002

Inflation Adjusted Gross Gaming Win Per Employee, 1981 - 2002

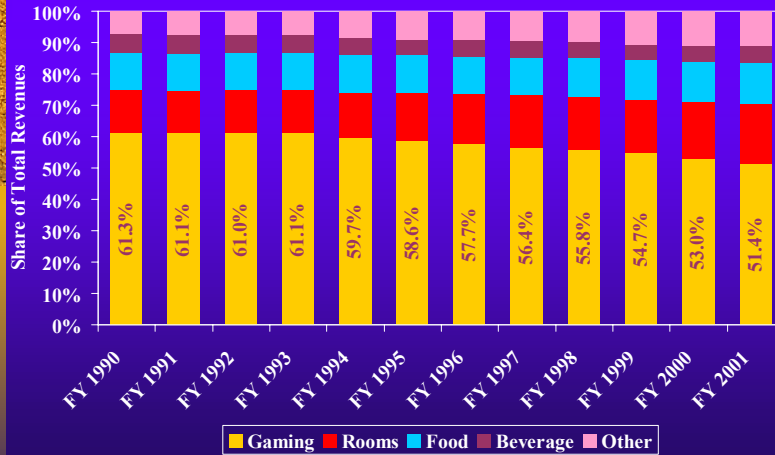# Hotel, Gaming & Recreation as a Percentage of Total Employment, 1980 - 2001

Hotel, Gaming & Recreation as a Percentage of Total Wages, 1980 - 2001

HG&R % of Total

32%
28%
24%
20%
16%
12%

1980 1982 1984 1986 1988 1990 1992 1994 1996 1998 2000

Visitors Per Capita, 1990 - 2002

Visitors Per Capita

27
26
25
24
23
22
21
20

FY 1990 FY 1991 FY 1992 FY 1993 FY 1994 FY 1995 FY 1996 FY 1997 FY 1998 FY 1999 FY 2000 FY 2001 FY 2002
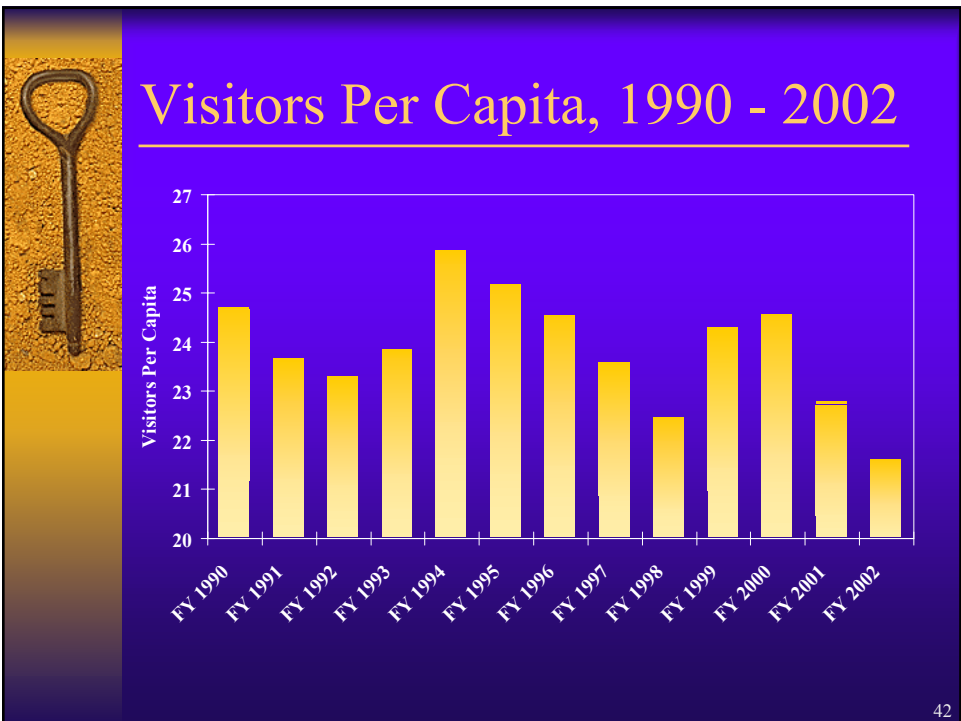
Visitor Spending, 1990 - 2001

Share of Total Revenues

FY 1990	FY 1991	FY 1992	FY 1993	FY 1994	FY 1995	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001
61.3%	61.1%	61.0%	61.1%	59.7%	58.6%	57.7%	56.4%	55.8%	54.7%	53.0%	51.4%

Gaming ■ Rooms ■ Food ■ Beverage ■ Other

43

Illustrative Example

|	Year 1	Year 2	Change
Number of visitors	10,000,000	10,100,000	+ 100,000
Population	1,000,000	1,100,000	+ 100,000
Visitors per capita	10.0	9.2	-0.8
Tax generated per visitor	$10	$10	$0
Total tax collections	$100,000,000	$100,010,000	+ $10,000
Tax collection per capita	**$100**	**$91**	**- $9**

44

Factors Impacting Gaming Tax

- ♦ Visitor spending patterns (gaming vs. non-gaming)

- ♦ Visitor make up (convention vs. tourist)
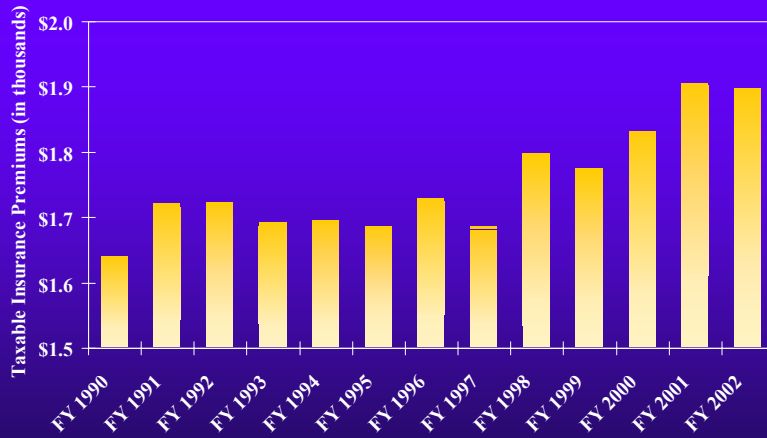
- ♦ Gaming proliferation (California & Arizona)
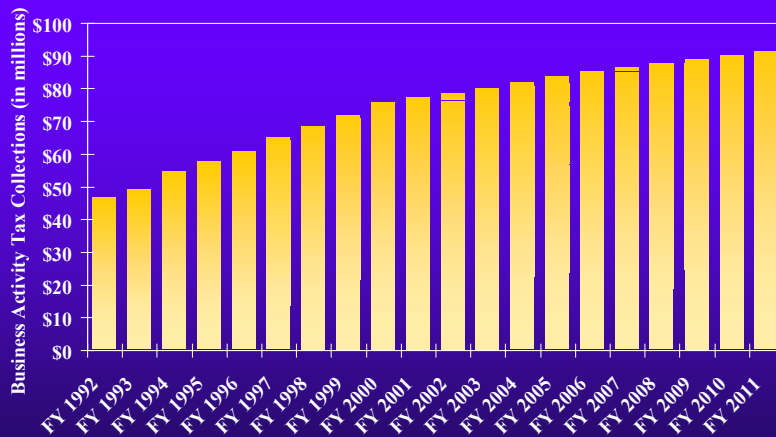
45

Taxable Insurance Premiums, 1990 - 2002
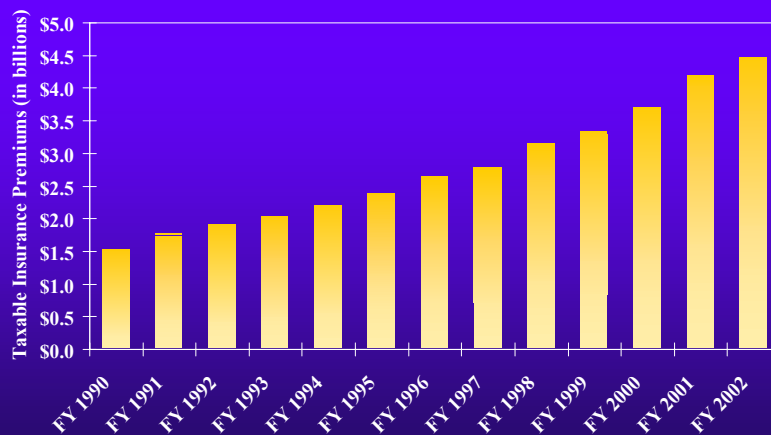
46

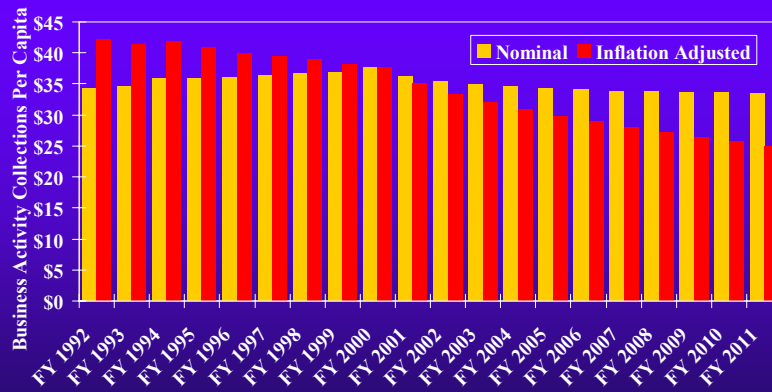## Inflation Adjusted Taxable Insurance Premiums Per Capita, 1990 - 2002

Taxable Insurance Premiums (in thousands)

$2.0	
$1.9	
$1.8	
$1.7	
$1.6	
$1.5	

FY 1990, FY 1991, FY 1992, FY 1993, FY 1994, FY 1995, FY 1996, FY 1997, FY 1998, FY 1999, FY 2000, FY 2001, FY 2002

47

Business License Tax Collections, 1992 - 2011

Business Activity Tax Collections (in millions)

$100	
$90	
$80	
$70	
$60	
$50	
$40	
$30	
$20	
$10	
$0	

FY 1992, FY 1993, FY 1994, FY 1995, FY 1996, FY 1997, FY 1998, FY 1999, FY 2000, FY 2001, FY 2002, FY 2003, FY 2004, FY 2005, FY 2006, FY 2007, FY 2008, FY 2009, FY 2010, FY 2011

48

Business License Tax Collections Per Capita, 1992 - 2011

Key Revenue Findings

♦ Quantitative

– Revenue growth projection: 3.9%

– Inflation adjusted per capita growth: -1.0%

– Largest gains:
  • Insurance premium taxes
  • casino entertainment tax

♦ Qualitative

– Nevada's revenue system is eroding

– Progressive elements help offset regressive design

– Issues will exist regardless of spending levels

Step 2: Expenditure Projections

General Approach (Two-Step)

♦ Baseline development
  – Population
  – Inflation growth

♦ Individual category modeling
  – Caseloads
  – Revenues
  – Transfers
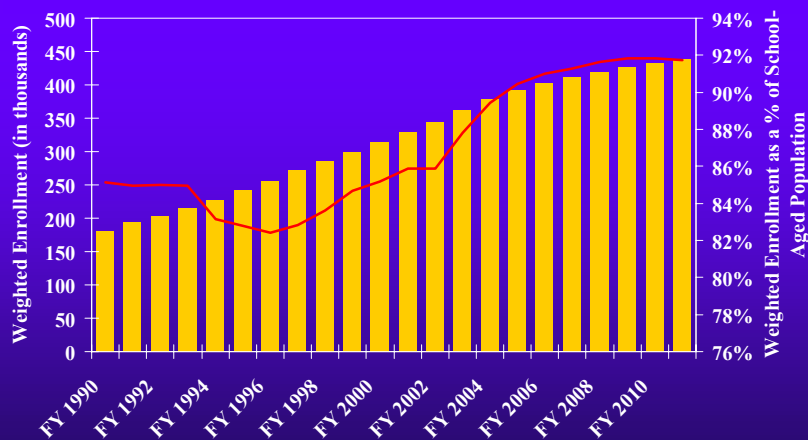 – Federal funding

Spending Areas

- ◆ Constitutional Agencies

- ◆ Education
  - – K-12
  - – UCCSN

- ◆ Finance & Admin.

- ◆ Special Purpose Agencies

- ◆ Human Services
  - – Medicaid
  - – Nevada Check-Up

- ◆ Commerce & Industry

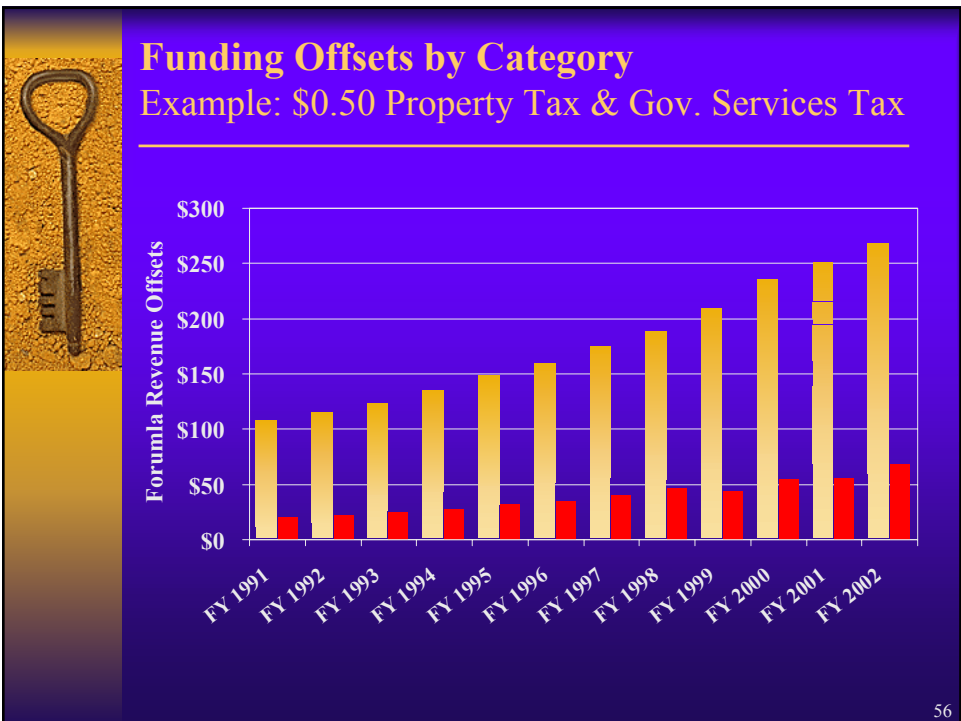- ◆ Public Safety
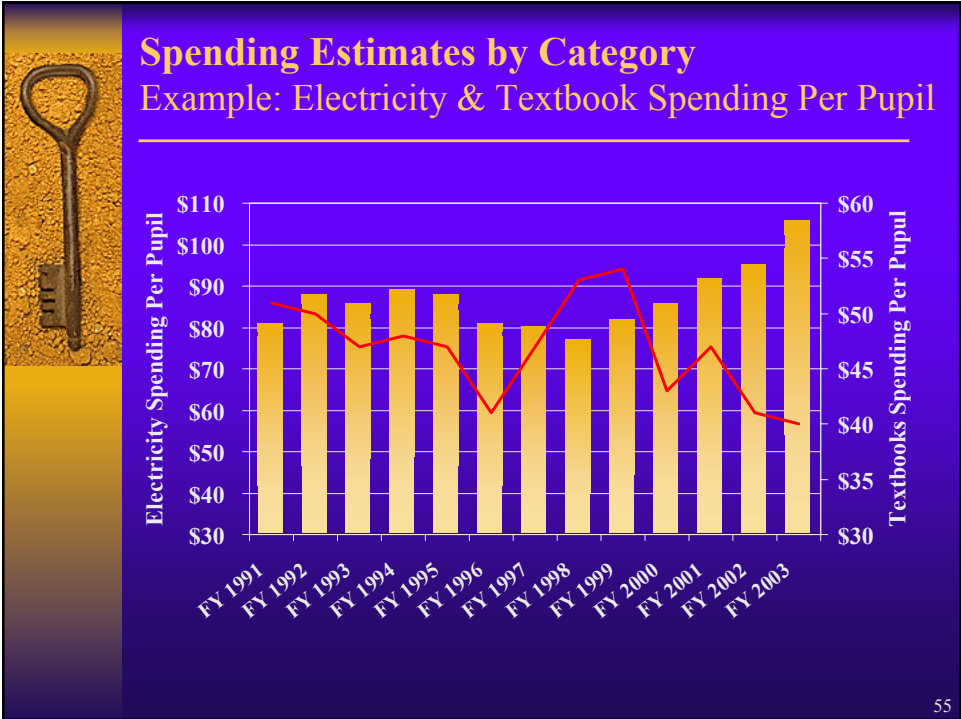 - – Department of Corrections

53

Caseload Estimates
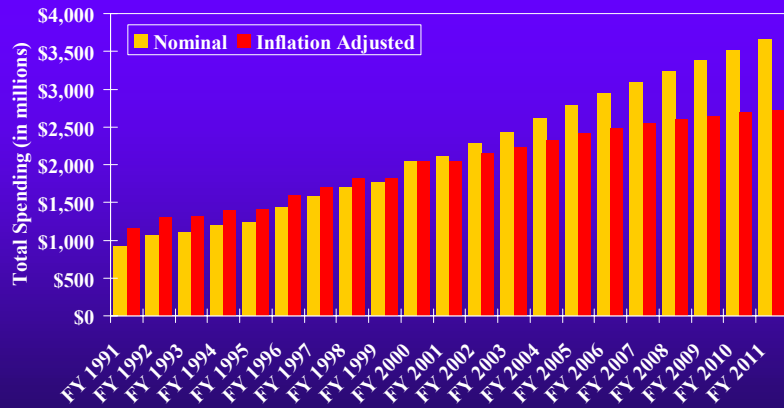### Example: K-12 Education Weighted Enrollment

54

Spending Estimates by Category
Example: Electricity & Textbook Spending Per Pupil

Funding Offsets by Category
Example: $0.50 Property Tax & Gov. Services Tax

Total Spending Estimates
Example: K-12 Education

Total Spending (in millions) — Nominal, Inflation Adjusted

FY 1991, FY 1992, FY 1993, FY 1994, FY 1995, FY 1996, FY 1997, FY 1998, FY 1999, FY 2000, FY 2001, FY 2002, FY 2003, FY 2004, FY 2005, FY 2006, FY 2007, FY 2008, FY 2009, FY 2010, FY 2011

57

Impact on the State's General Fund
Example: Distributive School Account

DSA Balance

FY 1992, FY 1993, FY 1994, FY 1995, FY 1996, FY 1997, FY 1998, FY 1999, FY 2000, FY 2001, FY 2002, FY 2003
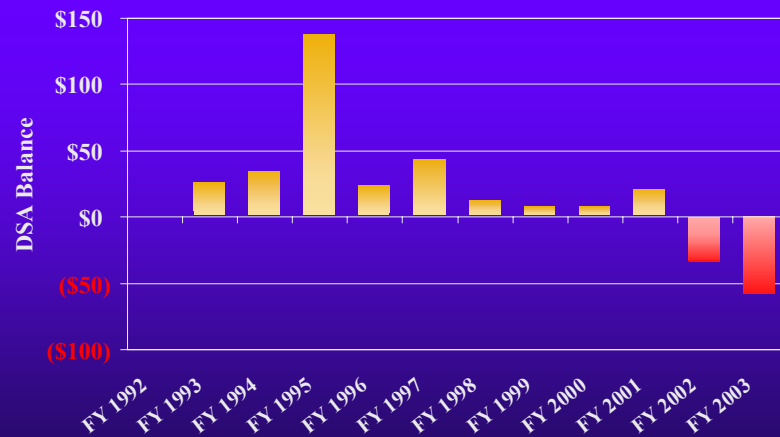
58

Key Expenditure Findings

- Demographic changes are making it increasingly costly to maintain service levels

- Structural considerations are placing an increased burden on the state's general fund

- Certain operating and personnel costs are increasing at rates faster than inflation

- Anticipated inflation rate to maintain current service levels: 6.1%
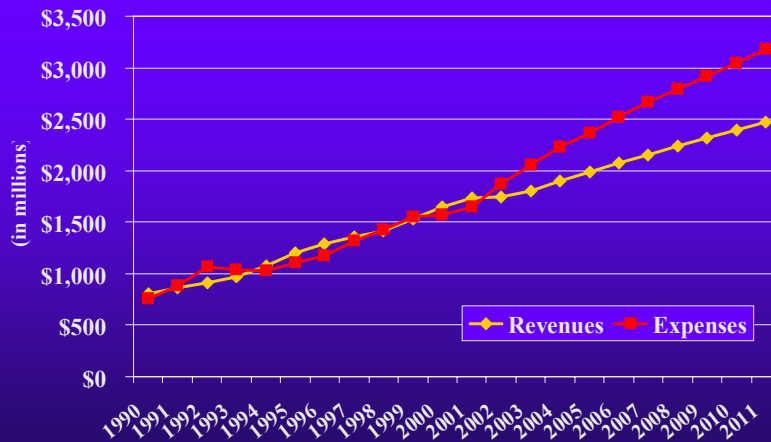
Step 3: Revenue/Expenditure Gap

Fiscal Outlook

♦ Projected revenue growth: 3.9%
♦ Projected expenditure growth: 6.1%

♦ Projected gap in 2003-05: $705 million
♦ Projected gap in 2009-11: $1.4 billion

♦ Annual inflation-adjusted, per capita growth:
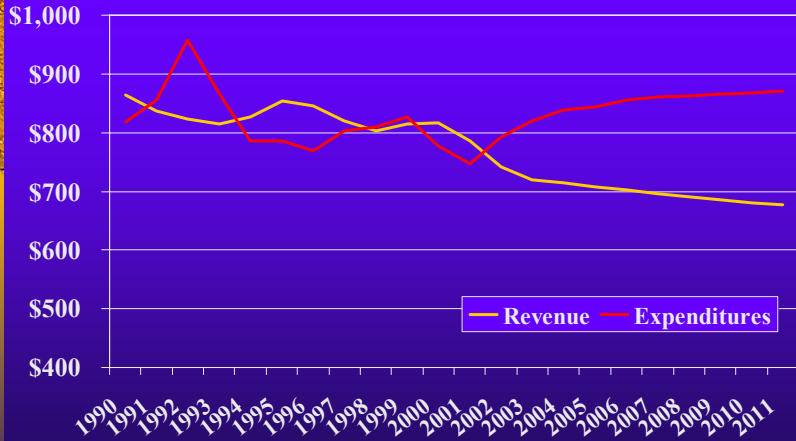 – Revenues: -1.0%
  – Expenditures: +1.0%

61

General Fund Revenues and Expenditures, 1990 - 2011

General Fund Revenues and Expenditures Per Capita, 1990 - 2011

63

Revenue/Expenditure Gap: Summary

	2003-05 Biennium	2009-11 Biennium
Revenues	$3.9 B	$4.9 B
Expenditures	$.4.6 B	$6.2 B
Surplus/**(Deficit)**	($705 M)	($1.4 B)

64