State and Local Taxation

Inquire: Taxation and Revenues for the State and Local Governments

Overview
State and local governments must have money to operate. They collect this money from a variety of sources: fees, licenses, lotteries, and other sources. However, by far the largest single source of revenue for state and local governments is taxes.

Big Question: Who collects my money, the state or the local governments?

Watch: The Lottery - A Bane or a Blessing?
So, you buy a lottery ticket. It only costs a dollar, and it gives you a chance to win millions of dollars and retire for the rest of your life. Even if you lose, you donated a good portion of your dollar to local public services — probably public education.

The numbers look like this: out of every dollar spent on a lottery ticket, 34 cents go into public education, 58 cents go to the winners’ payments, and six cents are paid to retailers.*

How can this be a bad thing?

Critics of lotteries point to the statistics:
- The numbers do not lie. You will not win the lottery. The chances of winning are often over one in 100 million. You have a much better chance of being struck by lightning!
- Someone is spending a lot of money on tickets. In 2012, writers/researchers for Bloomberg Business determined that, on average, every person in Georgia had spent $471 on lottery tickets. But, not everyone in Georgia had bought even one ticket.**
- So who is spending all this money? A study published in the Journal of Gambling Studies reported that the portion of the population in the bottom 20% in income spent the most on lottery tickets. In fact, the bottom 20% spent an average of more than twice as much as the wealthy lottery players. The poor in the bottom 20% averaged $433 a year in lottery spending versus $193 per year for the wealthy. It is true that those who can afford it the least are spending by far the most on a game they have no real chance of ever winning. That’s how we are funding our public education.***

Is this really how we want to fund public education? Are we preying on the hopes and dreams of those who can least afford it? But, is it really society’s job to police who buys lottery tickets? Isn’t this a country
built on freedom of choice? Besides, the most frequent lottery players are those with incomes between $36,000 and $89,999. About 56% of that group bought tickets in the last year.***

As state and local governments continue to try creatively raising revenue for the services people expect, all of these arguments will continue, without any actual resolution. Nonetheless, each of us must make our own decision. Is the lottery the great blessing for public education, or is it a great bane on our society that punishes those who can least afford it?


**Young, Elise and McIntyre, Alex; Georgia Lottery Players Suckers Spending Most for Least (2012); Bloomberg/Business, March 14, 2012; https://www.bloomberg.com/news/articles/2012-03-14/georgia-lottery-players-suckers-spending-most-for-least; Date Accessed: Monday, July 16, 2018


Read: But in this World Nothing can be Said to be Certain, Except Death and Taxes

Paying taxes is surely everyone’s least favorite government-related activity. But, taxing citizens is one of the concurrent powers of government. Federal, state, and local levels all have the power to tax.

Of course, people expect state and local governments to provide services such as police protection, education, highway building and maintenance, welfare programs, and hospitals and health care. Taxes are a major source of income to pay for these services and many others that hit close to home. For most people, their local and state tax money pays for very visible services that they generally take for granted, except when something goes wrong with garbage collection, traffic lights, or snow removal. People are most likely to get involved with local and state governments when these basic services go wrong.

Expenses

The single biggest expenditure in all states is education, with the average state and the localities within it spending just less than one-quarter of its budget for public schools. Funding for education comes primarily from the local school district budget, but most state governments give a great deal of financial and administrative support to schools. Other big budget items for state and local governments are the following:

- Public welfare;
- Health care;
- Highways;
- Police and fire protection;
- Interest on debt;
- Utilities and liquor stores.

Each of these items is less than 10% of state and local expenditures in most states, but together they make up a good portion of the expenses.
Income

Counties, townships, cities, and states collect some of their money from licenses and fees and state-operated businesses, but about half of state revenue comes from taxes. Two other sources of income are grants from the federal government and, in some states, lotteries. Most states and localities levy three types of taxes:

1. Sales taxes are the most important source of revenue for states. These taxes are placed on various products, and customers pay the tax when they buy them. Today 45 states have a general sales tax that applies to most goods, although food is usually excluded, and sometimes clothing is exempt. Some cities also collect sales tax.

2. Income taxes are imposed by all but a handful of states on personal and corporate incomes. Personal income taxes are generally progressive; that is, they are graduated so that the rate goes up with the size of the income. States generally do not allow local governments to levy income taxes, but some municipalities impose a payroll tax on people that work within their borders.

3. Property taxes provide the chief source of income for local governments today. Taxes are levied on land, buildings, and personal dwellings. Property must be assessed for its value, and most cities employ tax assessors for that job. Property taxes are controversial because other types of property, such as stocks, bonds, and bank accounts, generally are not taxed. Those who hold "real" property, then, pay a disproportionate share of the taxes.

Other taxes include inheritance and estate taxes imposed when a person dies and wills property to heirs. Several states have severance taxes, levied on those that extract natural resources such as coal, oil, timber, and gas from the land. Almost all states place special excise taxes (sometimes called "sin taxes") on gasoline, liquor, automobiles, and cigarettes.

Most states get more than a quarter of their income from federal grants that usually come with restrictions as to how the money can be used. Federal grants often go for building projects, such as roads, bridges, and dams, and for education, health care, and welfare.

In recent years, more and more states have turned to lotteries to pay their expenses. Billions of dollars now come from lotteries, with states retaining about one-third of the money as proceeds. Some states designate that the money be spent on something special, such as education, the arts, or building projects.

Lotteries are controversial because some people believe that lotteries hurt lower-income people, who buy most of the tickets.

Taxes, federal grants, fees, licenses, and lotteries support state and local budgets. Most people understand more about where their state and local taxes and fees go than they do about federal expenditures. Perhaps that is because state and local services tend to affect their personal lives more directly. Still, many complain that they do not get their money's worth. It is always easier to recognize the pinch that taxes bring than the services most people take for granted.
Reflect: Pick Your Poison

Poll: Was Reconstruction Effective?

In this lesson, we have talked about a variety of taxes. Which would you prefer: 1) a state income tax that would give you the certainty of knowing exactly how much of your earnings you would pay in taxes each year, or 2) a sales tax, which gives you some control by allowing you to choose what to buy and how much to spend, thereby controlling your taxes?

- state income tax
- state sales tax

Expand: The Power to Tax is the Power to Destroy

While there were numerous reasons the 13 colonies declared their independence on July 4, 1776, nearly every American schoolchild has heard, and memorized, the famous cry, “No taxation without representation!” This cry — this complaint — related back to the rights of Englishmen set forth in the English Bill of Rights, signed in 1689 by William and Mary, as a condition to their being handed the throne and the crown to rule England.

The actual phrase in the English Bill of Rights states, That levying money for or to the use of the Crown by pretence of prerogative, without grant of Parliament, for longer time, or in other manner than the same is or shall be granted, is illegal.* England’s kings had been used to levying taxes and ignoring Parliament, the people’s elected representatives. Recognizing the importance of controlling the power that could destroy their lives, the English said, “No more! Only our elected officials can tax us!”

The colonists argued that taxes imposed by a Parliament that did not contain even one representative elected from the Colonies were illegal by England’s own law.

This power to tax — this power to destroy — from the Constitution through the evolution of the United States is a power that the people have watched and guarded closely to ensure the governments were not crossing any lines. The people gave the national government the power to tax in Article 1, Section 8 of the Constitution. But, where does a state’s power come from? And, perhaps more importantly, where does that power come from for a municipality or a country?

That power comes from the people. The state constitutions give the state legislatures (as representatives of the people) the power, and from those constitutions, the states grant the powers to the cities and counties, whose governments are also representatives of the people.

Nevertheless, citizens invariably complain, “My taxes are too high!” That is until they have a serious accident or fire or any incident that requires the local services to step in to help, and possibly even save their lives. Providing for a society is not cheap: roads, water, sewer, police, fire protection, and education. All of these are services we expect and anticipate will be done well.

“No taxation without representation.” We still hold that value dear in America, at the national level, at the state level, and at the local level. Anytime we complain, “My taxes are too high,” we must remember that we elected those representatives; and, if the taxes really are too high, we can also unelect them!
Lesson Toolbox

Additional Resources and Readings

Taxes: Crash Course Economics #31
- A Crash Course video covering everything you need to know about taxes
  - https://www.youtube.com/watch?v=7Qtr_yA3Prw

Monetary and Fiscal Policy: Crash Course Government and Politics #48
- A Crash Course video covering monetary and fiscal policy
  - https://www.youtube.com/watch?v=_tULRch1PRQ

Taxes: States With Lowest Taxes Growing Fastest
- A video showing state and local taxes based by state
  - https://www.youtube.com/watch?v=TL0T1-Q0alQ

Lesson Glossary

None

Check Your Knowledge

1. All states have severance taxes on coal, oil, timber, and gas from the land.
   A. True
   B. False

2. The single biggest expenditure in all states is health care.
   A. True
   B. False

3. Lotteries are controversial because some people believe that lotteries hurt higher-income people.
   A. True
   B. False

Answer Key:

Citations

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