
Revenues

CHAPTER 3

Most of this report focuses on state and local government expenditures. Even in a report about spending trends, however, it is important to review how government finances its expenditures. Accordingly, this chapter examines changes in state and local government revenues over a 35-year period using data from the Census Bureau. In particular, the chapter addresses the following questions:

- **What are the sources of state and local government revenue in Minnesota and other states? How has the relative share of revenues contributed by state and local taxes changed over time?**
- **How much have overall Minnesota revenues and particular sources of revenues changed over time? Do trends in Minnesota differ from those in other states?**
- **How does the level of revenue collected in Minnesota compare with other states? What accounts for any differences?**

SOURCES OF REVENUE

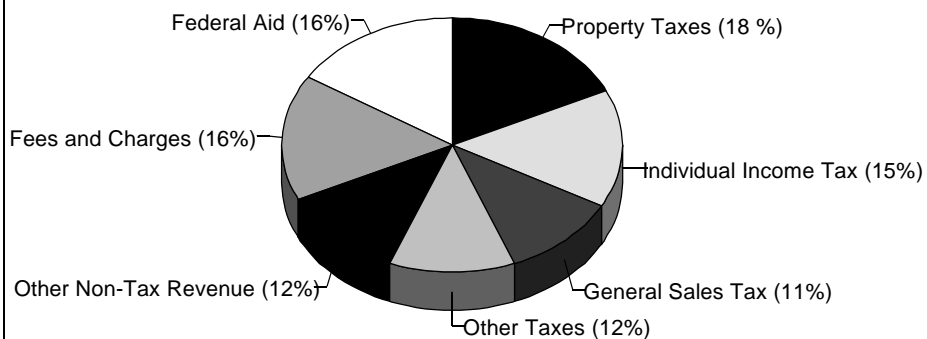
There are six major sources of state and local government revenue in Minnesota:

- Property taxes,
- Individual income taxes,
- General sales taxes,
- Federal aid,
- Charges and fees, and
- Other non-tax revenue.

As Figure 3.1 shows, property taxes accounted for 17.7 percent of state and local government revenue in Minnesota in 1992. The individual income tax and the

In 1992, 56 percent of revenues came from state and local taxes.

Figure 3.1: Sources of State and Local Government Revenue in Minnesota, 1992



Source: U.S. Census Bureau.

general sales tax accounted for 15.3 percent and 11.2 percent of total revenues. Other significant shares of revenue came from federal aid (16.0 percent), charges and fees (15.7 percent), and other non-tax revenue (11.8 percent).¹ Other taxes made up 12.3 percent of revenue.

Overall, 56 percent of total revenue in Minnesota came from state and local taxes, while 43 percent was from other sources. Table 3.1 shows that these overall shares were about the same in other states in 1992. However, other states received

Table 3.1: Sources of State and Local Government Revenue, Minnesota and the United States, 1992

	Minnesota	United States
TAXES		
Property	17.7%	18.3%
Individual Income	15.3	11.9
General Sales	11.2	13.4
Motor Fuel	2.4	2.4
Other Selective Sales	4.0	4.4
Corporate Income	2.2	2.4
Motor Vehicle License	2.0	1.2
Other	1.7	3.2
All state and local taxes	56.5%	57.2%
FEDERAL AID		
	16.0	18.4
NON-TAX SOURCES		
Charges and Fees	15.7	14.1
Miscellaneous	11.8	10.4
All non-tax sources	27.5	24.4
TOTALS	100.0%	100.0%

Source: U.S. Census Bureau.

¹ Other non-tax revenue is called "miscellaneous general revenue" by the Census Bureau and consists of interest earnings, special assessments, proceeds from sales of property, and other miscellaneous revenue.

a slightly higher percentage of their revenues from sales taxes, property taxes, and federal aid than did Minnesota. State and local governments in Minnesota received a higher than average share of their revenues from the individual income tax, fees and other non-tax sources of revenue, and the motor vehicle license tax.

State and local governments have become increasingly reliant on fees and other non-tax sources of revenue.

Since 1957, in both Minnesota and other states:

- **The share of government revenue coming from state and local taxes has declined.**
- **The portion of revenues financed from fees and other non-tax sources has increased.**
- **The share of revenues from federal aid has increased but was lower in 1992 than its peak in the mid- to late-1970s.**

Tables 3.2 and 3.3 show that these trends are similar in both Minnesota and other states. The data also show that the share of revenues from both the individual income tax and the general sales tax has increased. The declining share accounted for by all taxes is largely due to the substantial decrease in the share of revenues from property taxes. In Minnesota, the share of revenues from property taxes declined from 38 percent in 1957 to 18 percent in 1992. Decreasing shares from other taxes such as the motor fuel tax and the motor vehicle license tax also contributed to decreased relative reliance on taxes to fund state and local government spending.

Table 3.2: Percentage of State and Local Revenue from Various Sources, Minnesota, 1957-92

	<u>1957</u>	<u>1962</u>	<u>1967</u>	<u>1972</u>	<u>1977</u>	<u>1982</u>	<u>1987</u>	<u>1992</u>
Property	38.3%	39.0%	32.6%	25.6%	18.1%	14.8%	16.8%	17.7%
Individual Income	7.9	10.0	13.0	13.8	16.1	16.3	16.0	15.3
General Sales	NA	NA	NA	7.8	7.9	9.3	10.2	11.2
Motor Fuel	6.2	4.9	4.6	3.9	3.3	2.7	2.5	2.4
Other Sales	7.5	6.6	5.7	5.2	5.7	4.5	4.3	4.0
Corporate Income	2.7	2.9	3.6	3.2	4.3	3.4	2.9	2.2
Motor Vehicle License	4.3	3.5	2.9	2.0	1.8	1.7	1.9	2.0
Other	<u>7.1</u>	<u>4.1</u>	<u>3.2</u>	<u>2.6</u>	<u>3.4</u>	<u>2.8</u>	<u>1.3</u>	<u>1.7</u>
All Taxes	74.0%	71.0%	65.6%	64.1%	60.5%	55.5%	55.9%	56.5%
Federal Aid	9.8	12.3	16.4	16.8	20.9	18.7	15.7	16.0
Charges and Fees	10.4	10.1	11.0	11.9	11.3	14.1	13.9	15.7
Miscellaneous Non-Tax	<u>5.8</u>	<u>6.6</u>	<u>7.0</u>	<u>7.2</u>	<u>7.3</u>	<u>11.7</u>	<u>14.5</u>	<u>11.8</u>
Totals	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Source: U.S. Census Bureau.

Table 3.3: Percentage of State and Local Revenue from Various Sources, United States, 1957-92

	<u>1957</u>	<u>1962</u>	<u>1967</u>	<u>1972</u>	<u>1977</u>	<u>1982</u>	<u>1987</u>	<u>1992</u>
Property	33.7%	32.7%	28.6%	25.6%	21.9%	17.9%	17.6%	18.3%
Individual Income	4.6	5.2	6.4	9.1	10.3	11.1	12.2	11.9
General Sales	10.6	10.4	11.1	12.1	12.8	13.2	14.1	13.4
Motor Fuel	7.5	6.4	5.3	4.3	3.2	2.3	2.3	2.4
Other Sales	6.8	6.4	6.1	5.9	5.3	4.9	4.6	4.4
Corporate Income	2.6	2.2	2.4	2.6	3.2	3.3	3.3	2.4
Motor Vehicle License	3.6	2.9	2.5	2.0	1.6	1.3	1.3	1.2
Other	<u>6.2</u>	<u>5.1</u>	<u>4.5</u>	<u>3.7</u>	<u>3.4</u>	<u>4.1</u>	<u>3.5</u>	<u>3.2</u>
All Taxes	75.5%	71.3%	66.9%	65.4%	61.7%	58.2%	58.9%	57.2%
Federal Aid	10.1	13.5	16.8	18.7	21.9	19.1	16.7	18.4
Charges and Fees	9.9	10.8	11.5	11.3	10.9	12.4	12.7	14.1
Miscellaneous Non-Tax	<u>4.5</u>	<u>4.4</u>	<u>4.8</u>	<u>4.6</u>	<u>5.5</u>	<u>10.3</u>	<u>11.6</u>	<u>10.4</u>
Totals	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Source: U.S. Census Bureau.

TRENDS

Annual state and local government revenues have grown significantly over the last 35 years. In Minnesota, revenues grew from \$0.8 billion in 1957 to \$19.6 billion in 1992 -- an increase of 2,316 percent. The revenues of all state and local governments in the United States increased even faster (2,450 percent) -- going from \$38.2 billion to \$973.3 billion.

Over this period, however, inflation has also been significant. The general price levels faced by state and local governments have increased 536 percent. In addition, population has grown 37 percent in Minnesota and 50 percent throughout the United States. Personal income has increased 1,344 percent in Minnesota and 1,346 percent across the country.

Like expenditure growth, revenue growth should be measured in a way that properly adjusts for changes in price levels and population. In this section, we use two standard methods for measuring revenue growth relative to economic and population changes. These methods are: 1) inflation-adjusted revenues per capita and 2) revenues as a percentage of personal income.

Revenues per Capita

Minnesota's state and local government revenues per capita (in 1992 dollars) grew by 178 percent from \$1,576 in 1957 to \$4,381 in 1992. Figure 3.2 shows that other states experienced similar increases. The national average grew 168 percent from \$1,425 in 1957 to \$3,817 in 1992.

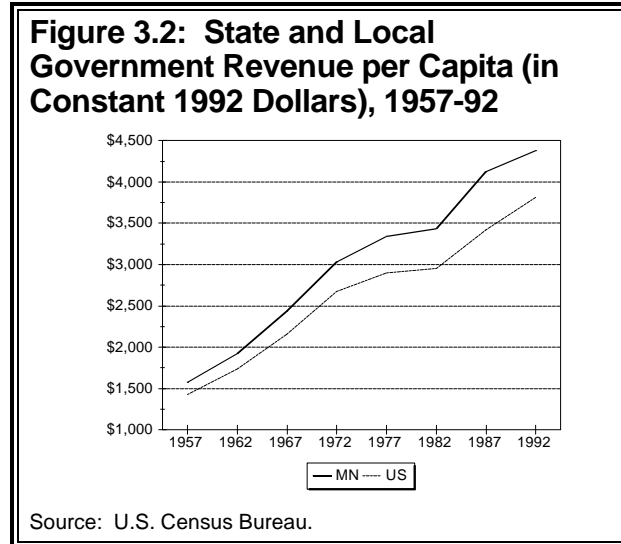
The increase in revenues per capita was not, however, uniform throughout this entire 35-year period. Table 3.4 shows that Minnesota revenues per capita grew 92 percent from 1957 to 1992, or 4.5 percent annually. In contrast, revenue growth

was only 45 percent, or 1.9 percent annually, from 1972 to 1992.

In addition:

- **Taxes grew the slowest of the four major types of revenues.**

From 1972 to 1992, taxes per capita increased 28 percent compared with 37 percent for federal aid, 91 percent for charges and fees, and 136 percent for



Revenues per capita have grown, but taxes have been the slowest growing source of revenues.

miscellaneous non-tax revenues (See Figure 3.3.). The annual rate of growth in tax revenues per capita was 1.2 percent, while charges and miscellaneous revenue grew at annual rates of 3.3 percent and 4.4 percent respectively. Most of the tax growth during these 20 years was in individual income taxes and sales taxes. Property taxes per capita did not change when adjusted for inflation.

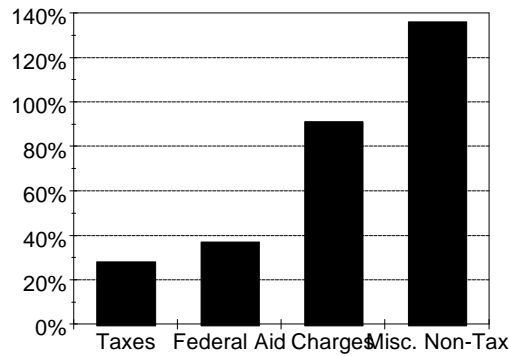
During the earlier period (1957-72), growth in charges and other non-tax revenue was equally strong, but taxes and federal aid increased faster than in the last 20

Table 3.4: Percentage Change in Minnesota Revenues per Capita (in 1992 Dollars), 1957-92

	<u>1957-72</u>	<u>1972-92</u>
Property	29%	0%
Individual Income	233	61
All Sales	138	50
Corporate Income	130	(-3)
Motor Vehicle License	(-13)	50
Other Taxes	<u>(-29)</u>	<u>(-5)</u>
All Taxes	67%	28%
Charges and Fees	119	91
Miscellaneous Non-Tax	<u>139</u>	<u>136</u>
Own Source Revenue	77%	46%
Federal Aid	<u>230</u>	<u>37</u>
All Revenues	92%	45%

Source: U.S. Census Bureau.

Figure 3.3: Percentage Increase in Minnesota Revenue per Capita (in Constant 1992 Dollars), 1972-92



Source: U.S. Census Bureau.

years. Taxes grew 67 percent, or 3.5 percent annually. Federal intergovernmental revenue rose 230 percent, or 8.3 percent annually.

Trends in other states were similar to those in Minnesota. Table 3.5 shows that the average changes in overall revenues per capita and tax revenues per capita were slightly less than those in Minnesota. Overall revenues per capita in-

creased 88 percent nationally from 1957 to 1972 and 43 percent from 1972 to 1992. Increases in Minnesota were 92 percent and 45 percent respectively. Nationally, tax revenues per capita grew 63 percent and 25 percent during these two time periods, compared with 67 percent and 28 percent in Minnesota. Revenue from the federal government, however, grew slightly faster in other states. Over the entire 35-year period, federal aid per capita rose 354 percent in Minnesota compared with 390 percent nationally.

Minnesota's overall revenue trends parallel national trends.

Even though taxes were 74 percent of the state and local government revenue in Minnesota in 1957, Table 3.6 shows that taxes accounted for only 53 percent of the inflation-adjusted growth in revenues per capita from 1957 to 1972. Since taxes grew slower than other revenue sources during this period, taxes declined to 64 percent of all revenues in 1972. Over the next 20 years, taxes again grew

Table 3.5: Percentage Change in State and Local Revenues per Capita (in 1992 Dollars), United States, 1957-92

	1957-72	1972-92
Property	43%	2%
Individual Income	271	86
All Sales	70	29
Corporate Income	92	33
Motor Vehicle License	3	(-15)
Other Taxes	13	21
All Taxes	63%	25%
Charges and Fees	114	78
Miscellaneous Non-Tax	91	221
Own Source Revenue	70%	43%
Federal Aid	249	40
All Revenues	88%	43%

Source: U.S. Census Bureau.

Table 3.6: Percentage of per Capita Revenue Growth Explained by Various Sources, Minnesota, 1957-92

	<u>1957-72</u>	<u>1972-92</u>
Property	12%	0%
Individual Income	20	19
General Sales	16	19
Other	<u>5</u>	<u>2</u>
All State and Local Taxes	53%	40%
Charges and Fees	14	24
Miscellaneous Non-Tax	<u>9</u>	<u>22</u>
Own Source Revenue	76%	86%
Federal Aid	<u>24</u>	<u>14</u>
Totals	100%	100%

Source: U.S. Census Bureau.

slower than other revenues, accounting for 40 percent of the growth in revenues per capita. By 1992, taxes were 57 percent of all revenues.

From 1972 to 1992, various non-tax sources of revenue accounted for nearly half (46 percent) of the revenue growth in Minnesota. Growth in federal aid accounted for 14 percent. Individual income taxes and the general sales tax each accounted for 19 percent of the total growth.

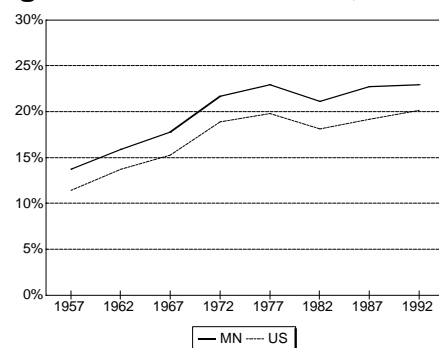
Revenue Growth Compared with Personal Income Growth

State and local government revenues in Minnesota and other states have also grown significantly as a percentage of personal income. As Figure 3.4 shows, Minnesota revenue as a percentage of personal income increased from 13.7 percent in 1957 to 23.0 percent in 1992. Nationally, revenue grew from 11.4 percent to 20.1 percent of personal income.

Table 3.7 shows, however, that:

- **Most of the revenue growth relative to personal income occurred before 1972.**

Figure 3.4: State and Local Government Revenues as a Percentage of Personal Income, 1957-92



Source: U.S. Census Bureau.

Table 3.7: Percentage Change in Minnesota Revenues Relative to Personal Income, 1957-92

	<u>1957-72</u>	<u>1972-92</u>
Property	6%	(-27)%
Individual Income	174	18
All Sales	95	10
Corporate Income	89	(-29)
Motor Vehicle License	(-28)	10
Other Taxes	<u>(-42)</u>	<u>(-30)</u>
All Taxes	37%	(-7)%
Charges and Fees	80	40
Miscellaneous Non-Tax	<u>96</u>	<u>73</u>
Own Source Revenue	46%	7%
Federal Aid	<u>171</u>	<u>1</u>
All Revenues	58%	6%

Source: U.S. Census Bureau.

Since 1972, taxes have not increased as fast as personal income.

From 1957 to 1972, Minnesota revenues relative to personal income rose 58 percent, while the increase was only 6 percent during the next 20 years.² Taxes relative to personal income grew 37 percent from 1957 to 1972 but declined 7 percent from 1972 to 1992. Despite the drop in relative tax revenues, overall revenues grew 6 percent from 1972 to 1992 largely because of significant growth in charges and other non-tax revenues. Charges and fees rose 40 percent relative to personal income, while other non-tax revenues increased 73 percent.

The national trends were similar to those in Minnesota. Growth in overall revenues relative to personal income was slightly faster nationally. From 1957 to 1972, overall revenues grew 66 percent relative to personal income. The growth slowed to 7 percent from 1972 to 1992. The slightly higher national growth rates were the result of slightly higher growth rates for personal income and personal income per capita in Minnesota.

Another way of comparing revenues with personal income is to calculate "own source" revenues as a percentage of personal income. Own source revenues include all the revenues included above except federal intergovernmental revenue. For Minnesota, own source revenue as a percentage of personal income increased from 12.4 percent of personal income in 1957 to 19.3 percent in 1992. The pattern of growth was similar to that for all revenues, with own source revenue growing 46 percent relative to personal income from 1957 to 1972 and 7 percent from

² This calculation is the percentage increase in state and local government revenues as a percentage of personal income.

1972 to 1992. Nationally, own source revenue increased 50 percent relative to personal income during the earlier period and 7 percent from 1972 to 1992.³

Growth in More Recent Years

Census data on revenues are not available beyond 1992. Actual data for Minnesota have been published, however, by the Minnesota Department of Finance through 1994. The two data sources cannot be directly compared because of differences in the definition of non-tax revenues, but the Finance data can be used to estimate changes in Minnesota revenues from 1992 to 1994.

The Finance data suggest that both overall revenues per capita and own source revenue per capita increased 7 percent in Minnesota from 1992 to 1994. Taxes per capita rose 8 percent, non-tax revenues increased 4 percent, and federal aid grew 11 percent.

Growth relative to personal income was a little lower than per capita growth. Overall revenues grew 4 percent relative to personal income, while own source revenue was up 3 percent. Taxes increased 4 percent relative to personal income, while federal aid grew 7 percent. The growth in non-tax revenues relative to personal income was less than 1 percent.

Over the last two years, the annual rate of growth in revenues per capita has been about 3.6 percent. This is more than the annual growth rate of 2.5 percent for 1982 to 1992 based on Census data. Similarly, the growth relative to personal income over the last two years is larger than indicated by Census data for the previous ten years. The annual rate of growth in revenues relative to personal income was 1.8 percent according to Finance Department data for 1992 to 1994. From 1982 to 1992, revenues grew 0.8 percent relative to personal income.

NATIONAL COMPARISONS

We have already seen that the level of revenues collected in Minnesota is higher than national averages calculated either on a per capita basis or as a percentage of personal income. In this section, we examine these national comparisons in greater detail. We focus on comparisons of revenues per capita, since comparisons using personal income yield similar results.

³ Own source revenue as a percentage of personal income is similar to the "price of government" calculated under Minnesota state law. These figures are, however, a little higher than those calculated by the Minnesota Department of Finance, because the Census Bureau's definitions of interest earnings and other non-tax revenues appear to be more inclusive than those used by Finance.

Revenues per Capita

Overall:

- **Minnesota state and local government revenue per capita was 15 percent higher than the national average in 1992.**

Table 3.8 also shows how Minnesota compared nationally in 1992 for the major categories of revenue and for particular types of taxes. Minnesota's tax collections per capita were 14 percent above the national average. Revenue per capita from charges and other non-tax sources were 28 percent and 31 percent higher than their respective national averages. As a result, own source revenue per capita was 18 percent above average. Federal aid per capita was 1 percent below the national average.

In 1992, Minnesota collected 15 percent more revenue per capita than the national average.

Table 3.8: Percentage Difference Between Minnesota Revenues per Capita and the National Average, 1992

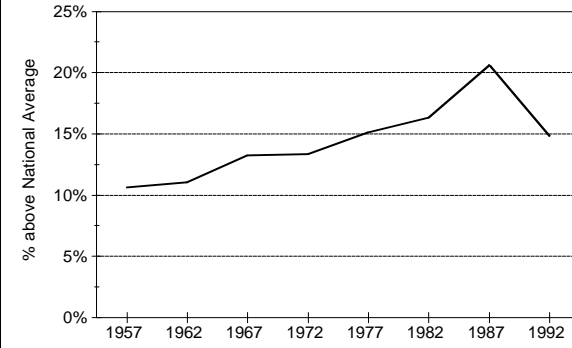
Property	11%
Individual Income	48
General Sales	(-4)
Selective Sales	8
Corporate Income	1
Motor Vehicle License	98
Other	<u>(-37)</u>
All Taxes	14
Charges and Fees	28
Miscellaneous Non-Tax	<u>31</u>
Own Source Revenue	18
Federal Aid	<u>(-1)</u>
All Revenues	15%

Source: U.S. Census Bureau.

Taxes varied considerably in their relationship to national averages. Individual income taxes per capita were 48 percent above average, while general sales tax collections per capita were 4 percent below average. Property taxes per capita were 11 percent above average. Motor vehicle license taxes per capita were 98 percent above the national average, but represent only 2 percent of revenues.

Minnesota's relative rankings have varied somewhat over time, but the general pattern has remained much the same. Figure 3.5 shows that revenues per capita in Minnesota have generally been about 10 to 20 percent above the national average.

Figure 3.5: Percentage Difference Between Minnesota Revenues per Capita and the National Average, 1957-92



Source: U.S. Census Bureau.

Tax Capacity and Tax Effort

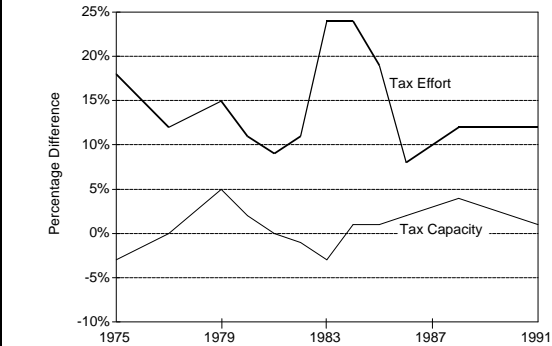
How Minnesota revenues per capita compare with the national average is the product of two factors: 1) tax capacity and 2) tax effort. Tax capacity measures the revenues per capita which would be generated in each state by applying national average tax rates to that state's tax bases. In other words, tax capacity varies across

states only because states differ in the economic bases such as income, property wealth, and sales upon which taxes are levied. Tax effort is the ratio of a state's actual revenues to its estimated capacity. Tax effort measures how states differ in the extent to which they tax a given tax base or tax capacity.

State-by-state estimates of tax capacity and tax effort have been published by the Advisory Commission on Intergovernmental Relations (ACIR). Figure 3.6 shows how Minnesota's relative tax capacity and tax effort have changed between 1975 and 1991. Generally:

- **Minnesota's overall tax capacity has been close to the national average, while its tax effort has generally been about 10 to 20 percent above the national average.**

Figure 3.6: Percentage Difference Between Minnesota's Tax Capacity and Tax Effort and the National Averages, 1975-91



Source: U.S. Census Bureau.

Table 3.9 provides more detailed information for specific taxes. In 1991, tax capacity was 1 percent above the national average, while tax effort was 12 percent above average. As a result of these two factors, overall tax revenues per capita were 13 percent above average.

Minnesota's relative tax capacity was fairly close to the national averages for specific types of taxes except for severance taxes which were 92 percent below average. Tax effort varied considerably by type of tax. Tax effort was above average

Table 3.9: Minnesota's Tax Capacity and Tax Effort Compared with the National Average, 1991

	Percentage Difference from National Average for:		
	Tax Capacity	Tax Effort	Tax Revenue Per Capita
Property	(-4)%	12%	8%
Personal Income	4	49	55
General Sales	8	(-9)	(-2)
Selective Sales	(-1)	(-6)	(-7)
License Taxes	2	80	85
Corporation	9	(-2)	7
Estate and Gift	20	(-71)	(-65)
Severance	(-92)	(-72)	(-98)
Other	(-1)	(-25)	(-26)
All Taxes	1%	12%	13%

Source: U.S. Advisory Commission on Intergovernmental Relations.

Minnesota has average tax capacity and above average tax effort.

for individual income taxes (48 percent), property taxes (12 percent), and license taxes (80 percent). Tax effort was below average for all other major tax categories.⁴

The ACIR has also published estimates of capacity and effort which apply to other revenue sources. For 1991, ACIR's broader revenue estimates included user charges, special assessments, rents and royalties, and lottery net income as well as taxes. For this "representative revenue system," ACIR estimated that Minnesota's overall revenue capacity was 1 percent below average, while its revenue effort was 17 percent above average. These factors resulted in overall revenues per capita, as measured by the ACIR, being 16 percent above the national average.

State Aid to Local Governments

Typically, a major component of state budgets is the state aid provided to local governments for a variety of purposes. Expenditure data presented in Chapter 2 do not separately itemize this component and instead count this spending at the local level where it ultimately occurs. It is interesting, however, to see how states vary in the degree to which local governments are dependent on state governments for revenue.

Table 3.10 presents information on state aid to local governments in Minnesota and other states. In general, local governments in Minnesota appear to be more dependent on state government for revenues than in most states. In 1992, state aid to local governments was \$1,072 per capita in Minnesota, or 40 percent higher than

⁴ Tax effort and tax capacity also varied within some of the major categories listed in Table 3.9. For example, within the selective sales tax category, Minnesota's tax effort was above average for the tax on tobacco products (59 percent), the motor fuels sales tax (13 percent), and taxes on distilled spirits (8 percent). Lower than average tax effort on other products and services resulted in overall tax effort for selective sales taxes being 6 percent below average.

Table 3.10: State Aid per Capita to Local Governments, Minnesota and the United States, 1992

Minnesota provides more state aid to local governments than most states.

	<u>Minnesota</u>	<u>National Average</u>	<u>Percentage Difference</u>
Education	\$592	\$484	22%
Public Welfare	161	101	60
General Support	155	62	152
Highways	71	32	120
Health/Hospitals	18	31	(-41)
Sewerage	16	1	1,426
Public Transit	10	16	(-38)
Housing/Community Development	3	3	(-2)
Other	<u>48</u>	<u>40</u>	<u>20</u>
Total	\$1,073	\$769	40%

Source: U.S. Census Bureau.

the national average of \$769.⁵ In Minnesota, state aid per capita to local governments was higher than the national average for education (22 percent), public welfare (60 percent), highways (120 percent), and general support for cities and counties (152 percent). Lower than average state aid per capita occurred for public transit (-38 percent) and housing/community development (-2 percent).

Part of the 40 percent difference in state aid per capita resulted because Minnesota spent 15 percent more overall per capita than other states in 1992. However, after adjusting for this factor, Minnesota state government still provided a higher than average amount of aid to local governments. State aid to local governments as a share of total state and local general revenue in Minnesota was 21 percent above the national average.

SUMMARY

We found that revenue growth for Minnesota's state and local governments was the strongest between 1957 and 1972. Revenue growth slowed considerably since then, but the rate of growth has increased in recent years. Taxes have generally grown the slowest of the major types of revenues. Between 1972 and 1992, tax revenues per capita grew only 28 percent and declined 7 percent relative to personal income.

Minnesota's trends were similar to national trends for state and local governments. The level of revenue collected in Minnesota, however, has consistently been about 10 to 20 percent above the national average. Minnesota has had about average tax capacity but has had a higher level of tax effort than other states.

⁵ These Census Bureau figures on state aid to local governments include some federal aid which is passed through the states and spent at the local level. This is more likely to be a significant factor with categories such as public welfare than with other categories.