

Texas Public Policy Foundation

# Keeping Texas Competitive

## A Legislator's Guide to the Issues 2013-2014



### Strengths of the Sales Tax

#### The Issue

Not all taxes are created equal. Some, like the income tax, discourage work and productivity; others, like the property tax, negatively impact building and improving property; while still others, like the sales tax, adversely affect consumption. In each instance, the type of tax levied yields a different economic outcome depending on the activity being targeted as well as the design and structure of the tax.

Knowing this, the challenge for conservatives then is to develop a tax system that generates an adequate amount of revenue while doing minimal damage to the economy and without influencing consumer behavior on a grand scale.

So what does a system such as this look like? One that relies heavily on consumption taxes.

Of all the major forms of taxation, consumption taxes, or sales taxes, are one of the most preferable for three reasons: they are simple, transparent, and levied only on the end-user.

In terms of simplicity, the tax is among the easiest for taxpayers to understand and pay since the rate is generally known beforehand and levied automatically at the time of purchase. This is a unique feature that sets the sales tax apart from most other taxes laden with time-consuming paperwork and other compliance costs.

Transparency is another important feature of the sales tax. After each purchase, every consumer is provided with a receipt clearly showing the amount of sales tax paid in addition to the price of the actual good. Since the sales tax is acknowledged after every purchase, it is almost impossible to manipulate the tax rate without public knowledge, making this an important safeguard against back-door tax hikes and other stealth maneuvers to raise taxes.

Finally, a conventional sales tax applies only to the end-user, meaning that the person consuming the final product bears the tax's ultimate cost. Consequently, the tax can be administered in a relatively simple manner. The seller need only add the cost of the tax to the final product and collect it on the government's behalf. Such simplicity avoids the need for many of the big bureaucratic organizations associated with other forms of taxes—i.e., appraisal districts, appraisal review boards, income tax departments (in all their various incarnations), etc.—and the need for taxpayers to support them.

As compared to the other major forms of taxation, the sales tax has shown that it is the least intrusive, the easiest to understand and pay, and is generally well-guarded against manipulation. For these reasons, the sales tax is by far the most preferable form of taxation.

#### The Facts

- Consumption taxes or sales taxes are generally simple, transparent, and levied only on the end-user.
- Since the sales tax only affects personal consumption, income, investment, and job creation are not penalized.
- At the state level, Texas levies a 6.25% sales tax rate on consumers, slightly above the national median of 6%.

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- In addition, local governments are also allowed to add a 2% levy to the sales tax rate for a maximum combined rate of 8.25%.
- Texas' heavy reliance on consumption taxes is an attractive feature of its tax system for businesses and entrepreneurs.
- As of August 2012, the Texas economy had helped produce 28 consecutive months of increased state sales tax revenues, according to the Texas Comptroller of Public Accounts.

### Recommendations

- State and local governments should continue to rely on consumption taxes as their main revenue generators.
- Any increase in the sales tax base or the sales tax rate should be accompanied by reductions in other taxes.

### Resources

The Case for Converting from Property Taxes to Sales Taxes by Talmadge Heflin, Texas Public Policy Foundation (Mar. 2008).

Tax Policy and Economic Growth in the States by Barry W. Poulson and Jules G. Kaplan, Texas Public Policy Foundation (Oct. 2007).

All Taxes Are Not Created Equal by Byron Schlomach, Texas Public Policy Foundation (Mar. 2006).

