

WHAT MAKES SPECIAL REVENUES SPECIAL?



JUNE 2014



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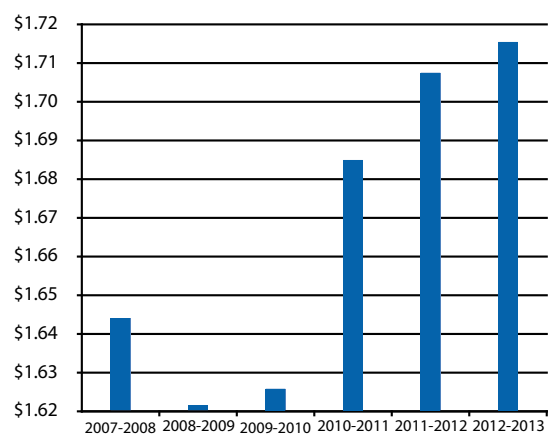
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June 2014

When you fill up your car at the gas station, you pay a motor fuel tax that directly benefits the Highway Department Fund. If a relative from out of state visits and pays for a hotel room in Arkansas, he or she pays a two percent tourism tax that directly credits the Tourism Development Fund. Taxes like these are called “special revenues” and they fund important programs in Arkansas every day.

Special revenues are different from other taxes because all of the money collected goes to specific, predetermined funds. This is why Special revenues are sometimes referred to as “Dedicated Taxes.”

Special revenues are usually more targeted than general revenue collections, like the income tax. The people who pay these taxes and fees often benefit more from the programs they fund. For example, frequent drivers pay more motor fuel tax and therefore help contribute more to maintaining the roads they use. Similarly, frequent travelers contribute more to tourism development. For most special revenues there is usually, but not always, a direct connection between the fee being paid or the item/service being taxed and the programs that special revenue helps fund.

NET SPECIAL REVENUES AVAILABLE FOR DISTRIBUTION
In billions



Motor fuel taxes, for example are used to maintain the state’s highways and roads. It is important to be aware that many special revenue taxes disproportionately impact low- and middle-income families. These families pay a higher share because they spend a larger portion of their income on necessities like motor fuel, and other goods frequently associated with special revenue taxes.

Most state taxes are “general revenues” (like the individual income tax) and are pooled together and then distributed to departments and programs funds based on the agency budgets approved by the Arkansas General Assembly in legislative sessions. During legislative sessions, the legislature devotes more attention to how to allocate/budget general revenues because they have greater flexibility on how to allocate these funds. They devote less time to how to allocate special revenues because the purposes/programs on which special revenues are spent have typically already been spelled out in existing law.¹ It should be noted that some taxes have both a general and special revenue component.

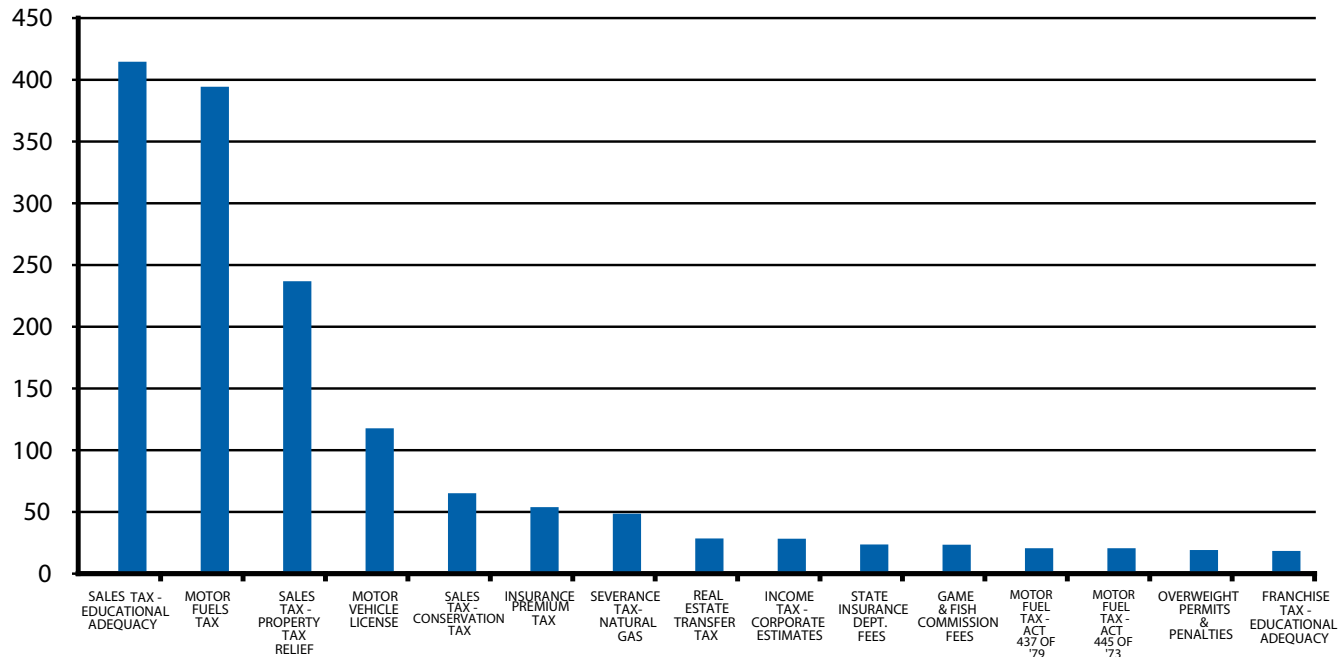
Although special revenues get less attention, they still represent about 10 percent of all state and federal revenue in Arkansas.² In 2013 general revenue collections in Arkansas totaled \$5 billion while special revenue collections amounted to \$1.7 billion.³ Special revenues in Arkansas experienced a dip during the recession but have since shown steady increases.

It is typical for tax revenue to follow overall economic patterns because during leaner times people are spending less on taxable goods and services, especially on purchases they view as less essential in nature.

Before the enactment of the revenue stabilization law in 1945, all revenues were collected for specific purposes. Essentially, all taxes were special revenues. This created a problematic, inflexible budget where “some services became ‘over funded’ while others were ‘short’” regardless of the importance of the program.⁴

SPECIAL REVENUE COLLECTIONS REFLECT ECONOMIC CHANGES

In millions



Today the revenue stabilization law allows general revenues to be funded in order of priority as determined by the legislature.⁵ Now, special revenues only make up part of the budget, and they are not distributed according to the revenue stabilization law.⁶

What are the advantages and disadvantages of special revenues?

Gaining funding through a special revenue tax can be a way of protecting that fund account in the future. Once their purposes are spelled in existing law, policymakers may be less willing to change or redirect where the proceeds of a dedicated or special revenue source should go. In contrast, policymakers are more willing to direct how any new growth in general revenue is to be spent.

It is important, however, to ensure that lawmakers don't neglect projects funded with special revenues. If a program or service has a special or dedicated revenue source, policymakers may think (or just want to justify) that they have already taken care of that it, and may be less willing to dedicate new general revenue to that program or service when new funding is needed.

Special revenues also sometimes make funding increases an easier sell because policymakers and the public are often more agreeable to an increase in a particular fee or tax when there is a relatively clear connection between the tax source and the services/programs they fund (such as increases gas or fuel taxes and the maintenance of roads).

Some special revenue taxes target certain behaviors, such as consuming too much soda, that could have undesirable consequences. The tax on soft drinks, for example, was passed in 1992 and its proceeds go into the Medicaid program trust fund.

Special or dedicated revenue streams, however, are sometimes not perfectly linked to the funds they benefit. Particular groups or consumers are sometimes asked to pick up the tab for a program or service which is not directly connected to the tax they are paying.

One recent example was a three percent beer tax passed in 2001 and 2003 to close a budget gap and help keep funding for quality early childhood programs from being cut.

The revenue from the new three percent tax was desperately needed; politically the new beer tax was one of the few revenue sources that could have been increased in those years; and the new tax helped increase the visibility among the public and policymakers of the need to adequately fund such programs from an end-user perspective.

However, there was little direct connection between the user who paid the tax increase (beer drinkers and beer retailers) and the benefits that resulted from the tax (preventing early childhood programs from being cut). The three percent beer tax was subsequently allowed to sunset in 2007.

Top 15 sources of special revenues FY 2012-2013:

Most of the special revenue collected comes from only about 10 percent of the nearly 150 different special revenue taxes. In fiscal year (FY) 2012-2013, special revenue collections added up to about \$1.8 billion. The top 15 largest revenue collecting taxes totaled \$1.5 billion and made up 85 percent of all special revenues.

The net revenues collected from all special revenue taxes comprised about 22 percent of the state net revenues collected last fiscal year.

1. SALES TAX - EDUCATIONAL ADEQUACY (\$414 MILLION) A 7/8 percent increase in the sales tax that Arkansans pay on everyday purchases goes to the Educational Adequacy Fund.

2. MOTOR FUELS TAX (\$393 MILLION) A 21.5 percent motor fuels tax is added to every gallon of gas pumped at Arkansas gas stations. Revenue from this tax is split between cities (15 percent), counties (15 percent), and the State Highway Department Fund (70 percent).

3. SALES TAX - PROPERTY TAX RELIEF (\$236 MILLION) Another part of the sales tax that Arkansans pay on everyday purchases is for property tax relief. An additional half percent is added to the sales tax to benefit the Property Tax Relief Fund.



4. MOTOR VEHICLE LICENSE (\$117 MILLION) Taxes are applied to motor vehicle (\$20) and motor scooter licenses (\$9). Revenue from this tax is split between cities (15 percent), counties (15 percent), and the State Highway Department Fund (70 percent).

5. SALES TAX - CONSERVATION TAX (\$64 MILLION) The Conservation Tax adds 1/8 percent to the Arkansas Sales Tax. These revenues are split between the Game Protection Fund (45 percent), the Department of Parks and Tourism (45 percent), the Department of Heritage Fund Account (9 percent), and the Keep Arkansas Beautiful Account (1 percent).

6. INSURANCE PREMIUM TAX (\$53 MILLION) Insurance premium taxes are collected from licensed insurance carriers and benefit several funds such as the Policemen's And Firemen's Pension Fund, fire protection, and the Fire and Police Pension Guarantee Fund.

7. SEVERANCE TAX-NATURAL GAS (\$48 MILLION) Producers of natural resources pay a "severance tax" to the Commissioner of Revenues. Different types of resources are taxed at different rates. Newly discovered gas is taxed at a rate of 1.5 percent., the marginal gas severance tax rate is 1.25 percent, and the all-natural gas severance tax rate is five percent.

Revenue from this tax is split between cities (15 percent), counties (15 percent), and the State Highway Department Fund (70 percent).

8. REAL ESTATE TRANSFER TAX (\$28 MILLION) The special revenue portion of the real estate transfer tax benefits the County and Circuit Clerks Continuing Education Fund and the County Aid Fund.

9. INCOME TAX - CORPORATE ESTIMATES (\$27 MILLION) Special revenues funds for this tax are based on the previous year's total collections (6.78 percent) and benefit the Workforce 2000 Fund.

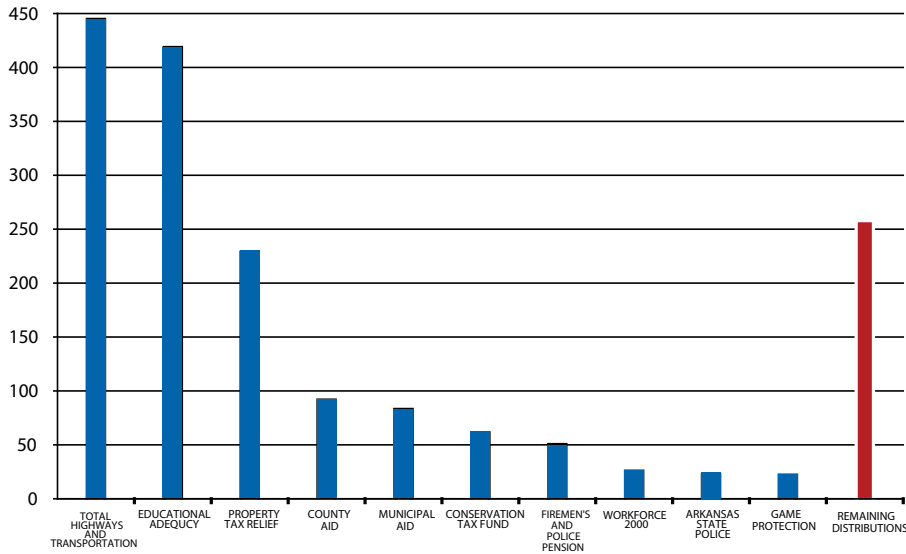
10. STATE INSURANCE DEPARTMENT FEES (\$23 MILLION) Various fees related to insurance certifications and documentation benefit the State Insurance Department Trust Fund.

11. GAME & FISH COMMISSION FEES (\$23 MILLION) The Game and Fish Commission issues licenses and charges fees that benefit the Game Protection Fund.

12. MOTOR FUEL TAX - ACT 437 OF '79 (\$20 MILLION) A one cent per gallon motor fuel tax benefits the State Road Aid Fund.

SPECIAL REVENUES COLLECTED FROM 2012-2013

In millions



13. MOTOR FUEL TAX - ACT 445 OF '73 (\$20 MILLION) A one cent per gallon motor fuel tax benefits the State Central Services Fund.

14. OVERWEIGHT PERMITS & PENALTIES (\$18 MILLION) Vehicles that exceed the maximum load limit are required to pay fees that benefit the Highway Department Fund.

15. FRANCHISE TAX - EDUCATIONAL ADEQUACY (\$17 MILLION) Corporate franchise tax revenues in excess of \$8 million dollars in each fiscal year will benefit the Educational Adequacy Fund.

Top ten special revenue beneficiaries FY2012-2013:

Once a special revenue tax is collected, it is delegated to a certain fund or funds to be spent on specific purposes. It is important to note that a special revenue tax can be allocated among multiple different funds. The following 10 funds received the bulk (85 percent) of the special revenue distributions in FY 2012-2013.

1. TOTAL HIGHWAY AND TRANSPORTATION DEPARTMENT (\$445 MILLION) This fund benefits the Arkansas State Highway and Transportation Department and the State Highway Commission. It is used for maintenance and operations of over 1,200 bridges as well as over 100,000 miles of public roads in Arkansas.⁷

2. EDUCATIONAL ADEQUACY (\$419 MILLION) This fund promotes education reform in Arkansas schools for students in grades K-12.⁸

3. PROPERTY TAX RELIEF (\$230 MILLION) This fund is distributed to each county's treasurer for property tax relief. The property tax relief fund allows an individual to claim up to \$350 in a homestead credit on their annual real estate taxes.⁹

4. COUNTY AID (\$92 MILLION) Seventy five percent of this fund is parceled out equally among Arkansas counties, while the remaining amount is distributed based on population size for "general county purposes."¹⁰

5. MUNICIPAL AID (\$84 MILLION) The Municipal Aid Fund receives money from general and special revenues. The special revenue funding comes from highway revenues and is subject to the Arkansas Highway Revenue Distribution Law.¹¹

6. CONSERVATION TAX FUND (\$62 MILLION) This fund is distributed to programs that benefit the preservation and improvement of Arkansas's natural attractions. These funds include the Game Protection Fund, the Department of Parks and Tourism Fund, the Department of Heritage Fund and the Keep Arkansas Beautiful Fund.

7. FIREMEN'S AND POLICE PENSION (\$51 MILLION) The Arkansas Fire and Police Pension Review Board use these funds to help protect the police and fire retirement system from losses.¹²

8. WORKFORCE 2000 (\$26 MILLION) The Work Force 2000 Development Fund is used by the Arkansas Higher Education Coordinating Board to improve the future of Arkansas workers.¹³ These improvements are made primarily through increasing opportunities for higher education, vocational school and other resources.



9. ARKANSAS STATE POLICE (\$23 MILLION) Special revenues help fund the Arkansas State Police's operations budget, which includes expenses like payroll, information technology, maintenance of buildings, and agency vehicles. Most of the funding for this budget comes from other sources, like general revenue, but fees from services like drivers licenses and permits help contribute to the \$23 million in special revenues that helps our police force stay in operation.¹⁴

10. GAME PROTECTION (\$23 MILLION) The Game Protection Fund is financed by special revenue from license plate fees and helps to support the Arkansas Game and Fish Commission.¹⁵

Conclusion

In some states, and Arkansas is no exception, the primary budget battle every year is over new state general revenue growth, e.g., which agency will receive a greater share of new state general revenues. Similar battles are rarely fought over special or dedicated revenue sources, due in part to their restrictive nature.

Special revenues are often overlooked despite the pervasive support of public services and programs like education, police force protection, and road maintenance that they pro-

vide. Special revenues restrict legislative decision making on funding, but they are often a more palatable way of providing funds to important projects and crucial programs that help Arkansas thrive and grow.

If the current anti-tax environment continues to prevail in the Arkansas legislature, the use of special revenues may be increasingly be looked to as a source of new funding, especially for clear well-defined and justifiable purposes. Their use, however, should be carefully analyzed to ensure that low- and middle-income taxpayers who already bare a higher share of the Arkansas tax burden (relative to their incomes) don't bare a greater share of the burden of any increase in the use of special revenues.

Notes

¹<http://www.aradvocates.org/assets/PDFs/Advocates-Guide-FINAL-WEB.pdf>

²<http://www.aradvocates.org/assets/PDFs/Advocates-Guide-FINAL-WEB.pdf>

³<http://www.arkleg.state.ar.us/bureau/research/Publications/Taxpercent20Publications/Annualpercent20Revenuepercent20Report percent202012-2013.pdf>

⁴https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&ved=0CCUQFjAA&url=httppercent3Apercent2Fpercent2Fwww.arkansashouse.orgpercent2Fpublicpercent2Fuserfilespercent2Ffilespercent2FArkansaspercent2520Budget percent2520Process.ppt&ei=QELhUsOQPIfnsASH-4KYBA&usg=AFQjCNEiHNdNLZzoAG6gsiMo_fDILIL8_Q&sig2=UnAw0GZebtq8YIQ9H6jFmg

⁵<http://www.thefreelibrary.com/1945+Act+keeps+State's+budget+consistent.-a0195753659>

⁶<http://www.arkleg.state.ar.us/bureau/legal/Publications/2010 percent20Legislative percent20Drafting percent20Manual.pdf>

⁷http://www.arkansashighways.com/planning_research/policy_analysis/publications/2013_Facts.pdf

⁸<http://www.arkleg.state.ar.us/bureau/legal/Publications/FUNDS percent20LIST percent202013.pdf>

⁹<http://www.arcounties.org/faq/assessor-faqs>

¹⁰http://www.dfa.arkansas.gov/offices/budget/budgetRequests/0074_county_aid.pdf

¹¹http://www.dfa.arkansas.gov/offices/budget/budgetRequests/0076_municipal_aid.pdf

¹²<http://www.arkleg.state.ar.us/bureau/legal/Publications/FUNDS percent20LIST percent202013.pdf>

¹³<http://www.arkleg.state.ar.us/bureau/legal/Publications/FUNDS percent20LIST percent202013.pdf>

¹⁴<http://www.arkleg.state.ar.us/assembly/2011/Summary percent20Budget percent20Manuals/2010TaxHandbook.pdf>

¹⁵<http://www.arkleg.state.ar.us/bureau/legal/Publications/FUNDS percent20LIST percent202013.pdf>

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