

HdL[®] Companies

TEXAS ESD SALES TAX:

CURRENT STATE OF AFFAIRS AND
FORECASTING

SAFE-D WEB CONFERENCE

JULY 2020

Topics to Cover

- ★ Understanding Sales Tax Allocations
 - Overview of Statewide Sales Tax Trends
 - ESD Sales Tax Trends
 - Forecasting: Examining the Outlook for ESDs

Allocation Payment Detail

- Why are Current Period Collections so important?
- Allocation period vs Activity period (July allocation is May activity)

Allocation Period: Jan 2020		
(A)	Total Collections: (=B+C+D+E+F+G)	159,985.64
(B)	Prior Period Collections:	5,431.36
★	(C) Current Period Collections: ★	154,230.10
(D)	Future Period Collections:	446.05
(E)	Audit Collections:	-1,083.87
(F)	Unidentified Collections:	25.12
(G)	Single Local Rate Collections:	936.88
(H)	Service Fee: (2% of A)	3,199.71
(I)	Current Retained: (2% of C)	3,135.72
(J)	Prior Retained: (2% Prior month C)	2,546.80
(K)	Net Payment: (A-(H+I)+J)	156,197.01

Available Here!



[LINK](#)



Activity vs Allocation Schedule

Tax Collected	January	February	March	April	May	June	July	August	September	October	November	December
	↓	↓	↓	↓	↓	↓	↓	↓	↓	↓	↓	↓
Paid to the T CPA	February	March	April	May	June	July	August	September	October	November	December	January
	↓	↓	↓	↓	↓	↓	↓	↓	↓	↓	↓	↓
Allocated to Jurisdictions	March	April	May*	June	July	August*	September	October	November*	December	January	February**

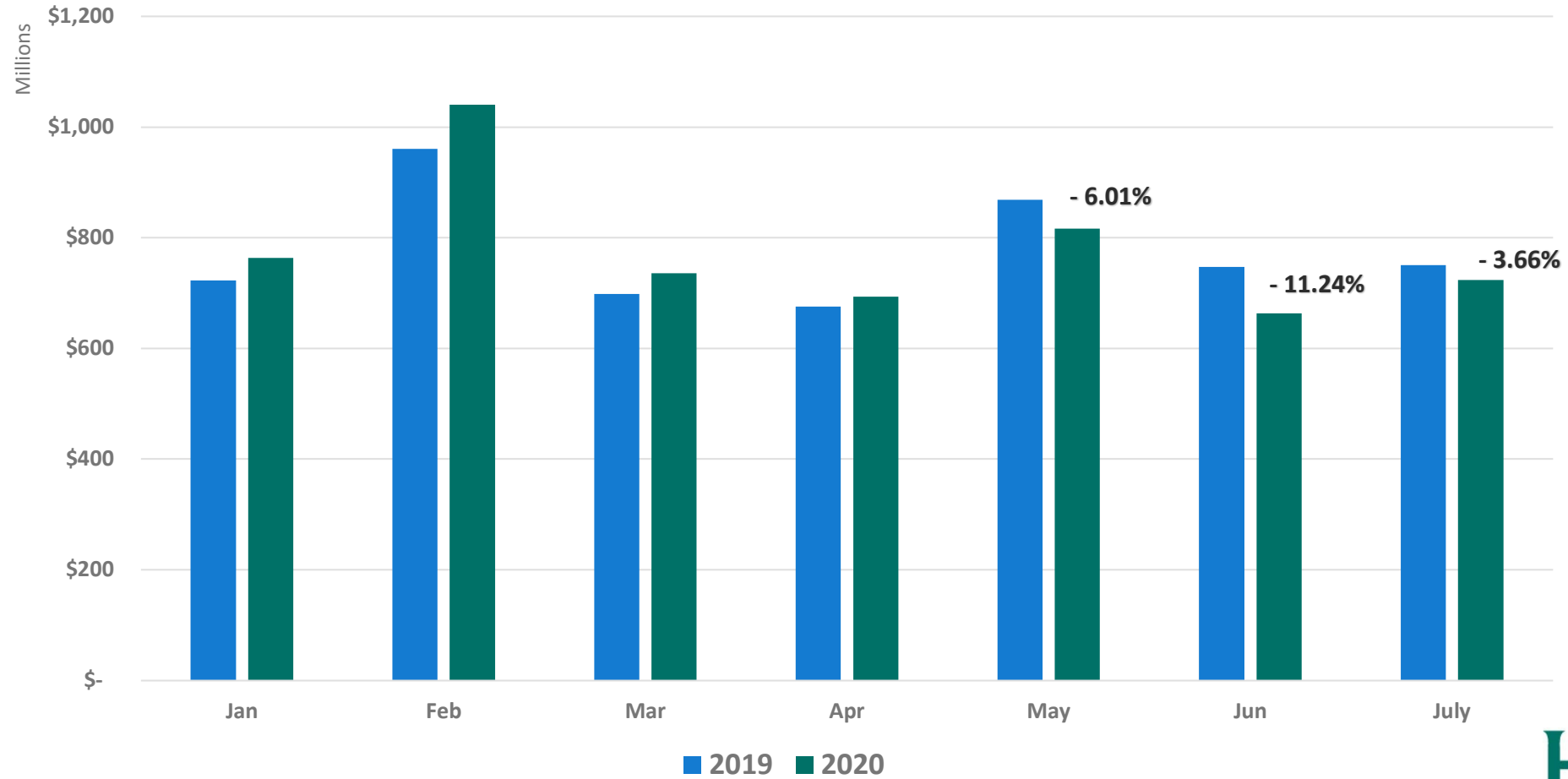
* indicates allocation month that includes quarterly filing taxpayers

** indicates allocation month that includes quarterly and annually filing taxpayers

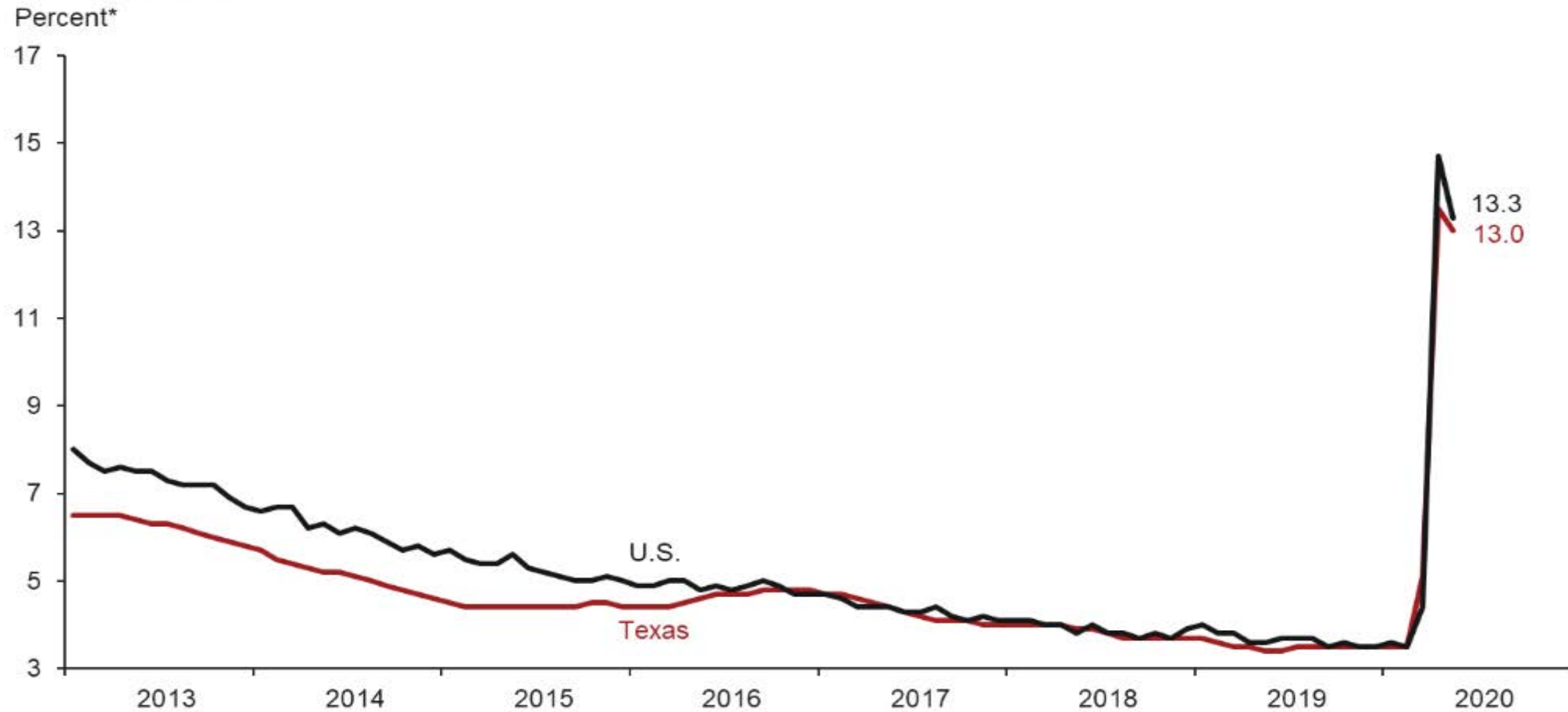
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Statewide Current Period Collections 2020 CYTD vs 2019



Unemployment Rate



*Seasonally adjusted.

SOURCE: Bureau of Labor Statistics; Texas Workforce Commission; adjustments by the Dallas Fed.

source: <https://www.dallasfed.org/research/indicators/tei/2020/tei2006.aspx>



Energy Activity

Dollars per barrel

Number of rigs

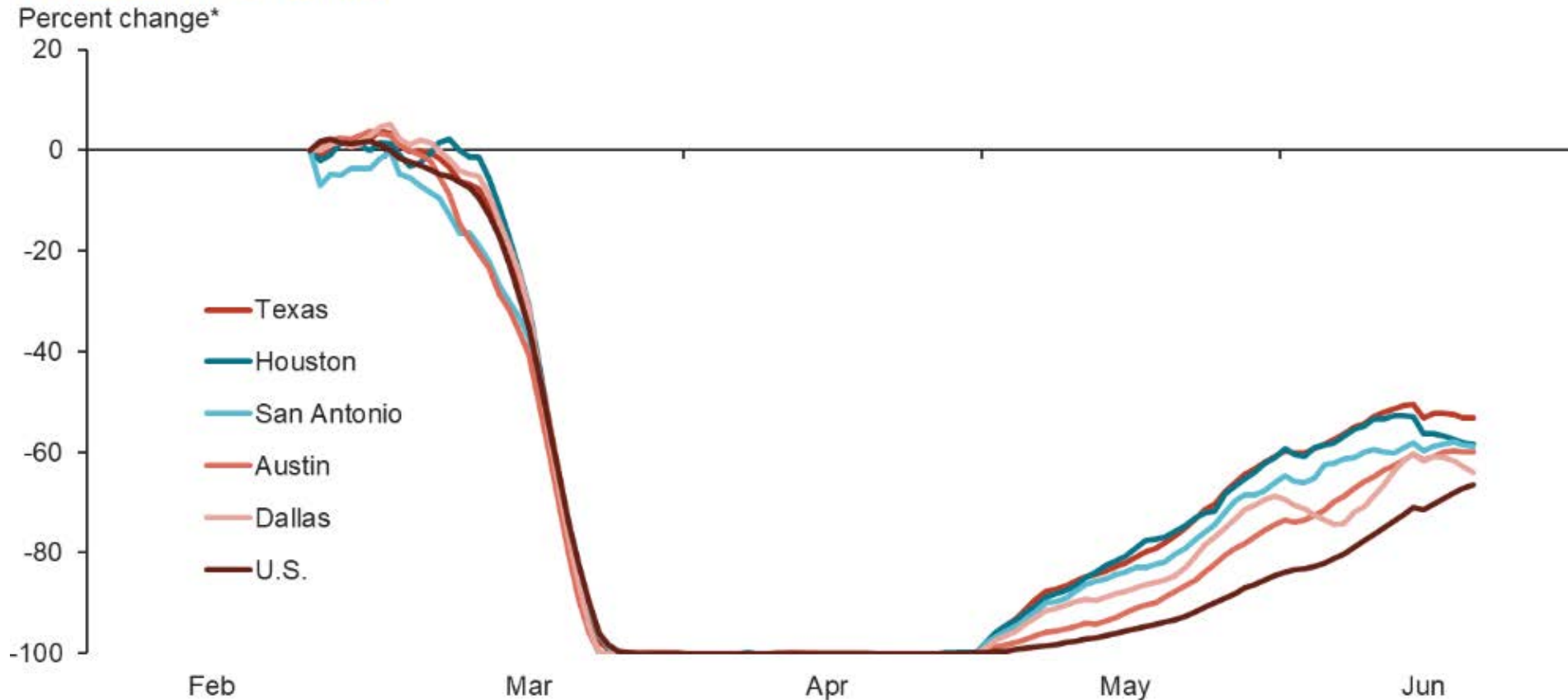


NOTE: Data are through the week ending June 19, 2020. Price is for West Texas Intermediate crude oil.
SOURCE: Baker Hughes; Energy Information Administration.

source: <https://www.dallasfed.org/research/indicators/tei/2020/tei2006.aspx>



Restaurant Reservations



*Year-over-year, seven-day moving average.

NOTE: Data are through June 19, 2020. Data refer to year/year percent change in seated diners at restaurants on the OpenTable network across all channels: online reservations, phone reservations and walk-ins.

SOURCE: OpenTable.

source: <https://www.dallasfed.org/research/indicators/tei/2020/tei2006.aspx>



Major Metro Areas Hit Hardest

Group	May 2020 vs May 2019	June 2020 vs June 2019	July 2020 vs July 2019
Statewide	- 6.01%	- 11.24%	- 3.66%
Five Major Metros	- 10.20%	- 16.80%	- 9.20%
All Other Entities	- 3.13%	- 7.44%	+ 0.11%

Topics to Cover

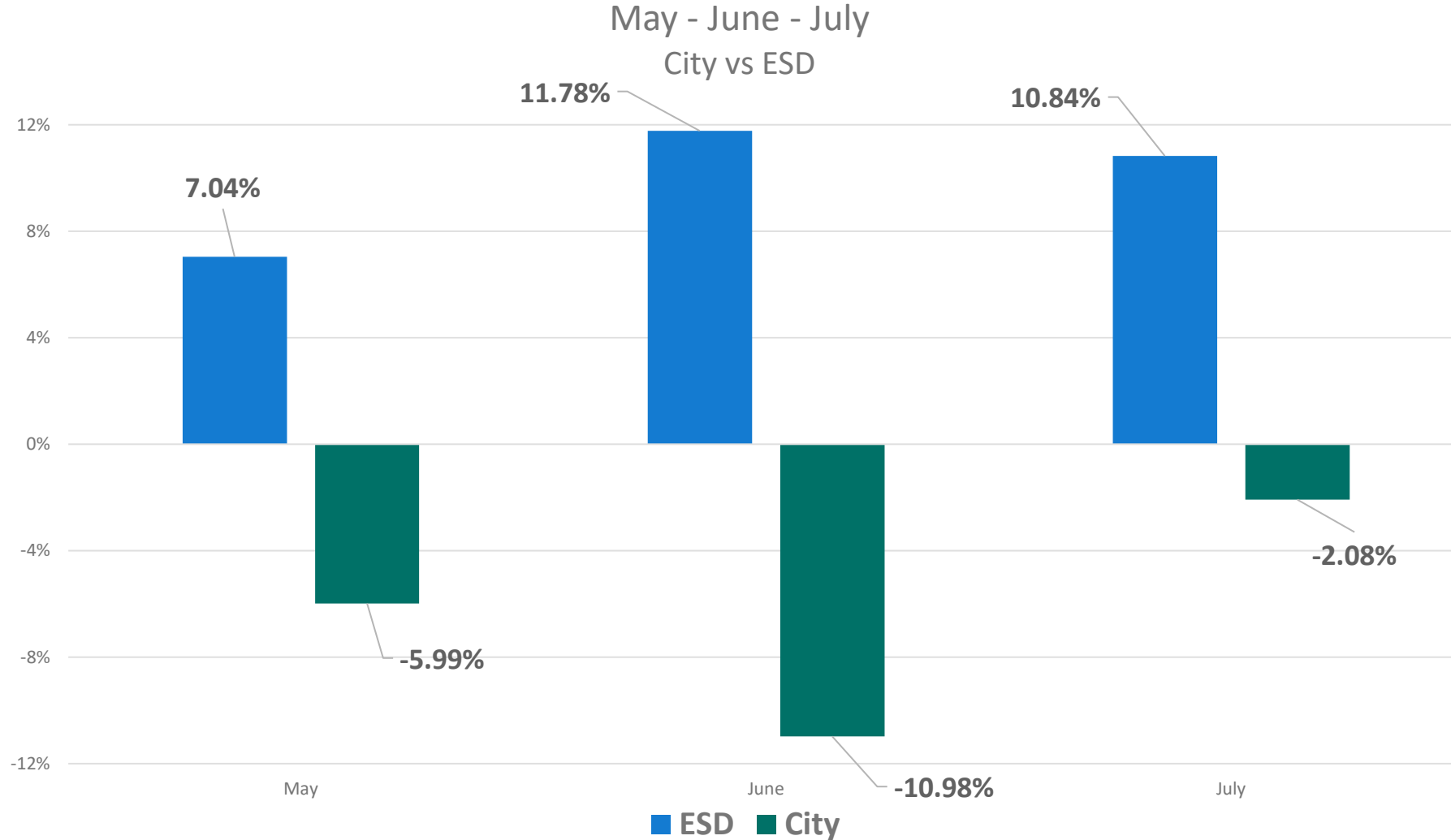
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 - May, June, July impacted by pandemic (June hit hardest)
 - Major Metro areas hit hardest

ESD Sales Tax Trends

- Forecasting: Examining the Outlook for ESDs

2020 vs 2019 YoY Change

Statewide Sales Tax Trends



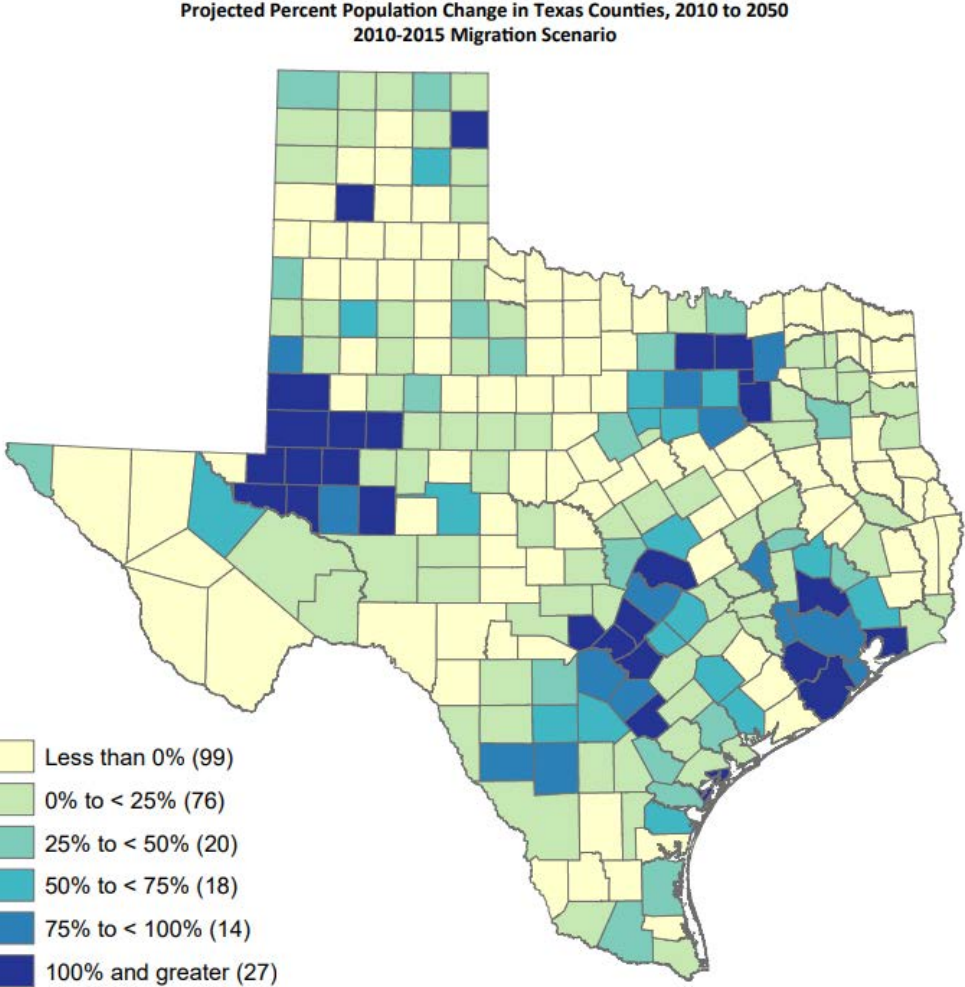
Driving Factors

Reasons why ESD sales tax revenues up when Cities are down

- Organic population growth
- New sales taxes elections and sales tax rate increases
- Influence of Residence-based sales tax
- Internet Retail

Organic Growth in Numbers

- Texas population is projected to reach nearly 35 million by 2030
- Urban centers are growing rapidly, but the fastest growth is projected to occur in the suburban counties as well as in the Permian Basin area
- Roughly 70% of ESDs that currently impose sales tax are located in these suburban counties
- It won't last forever..... will it?



source: https://demographics.texas.gov/Resources/publications/2019/20190128_PopProjectionsBrief.pdf



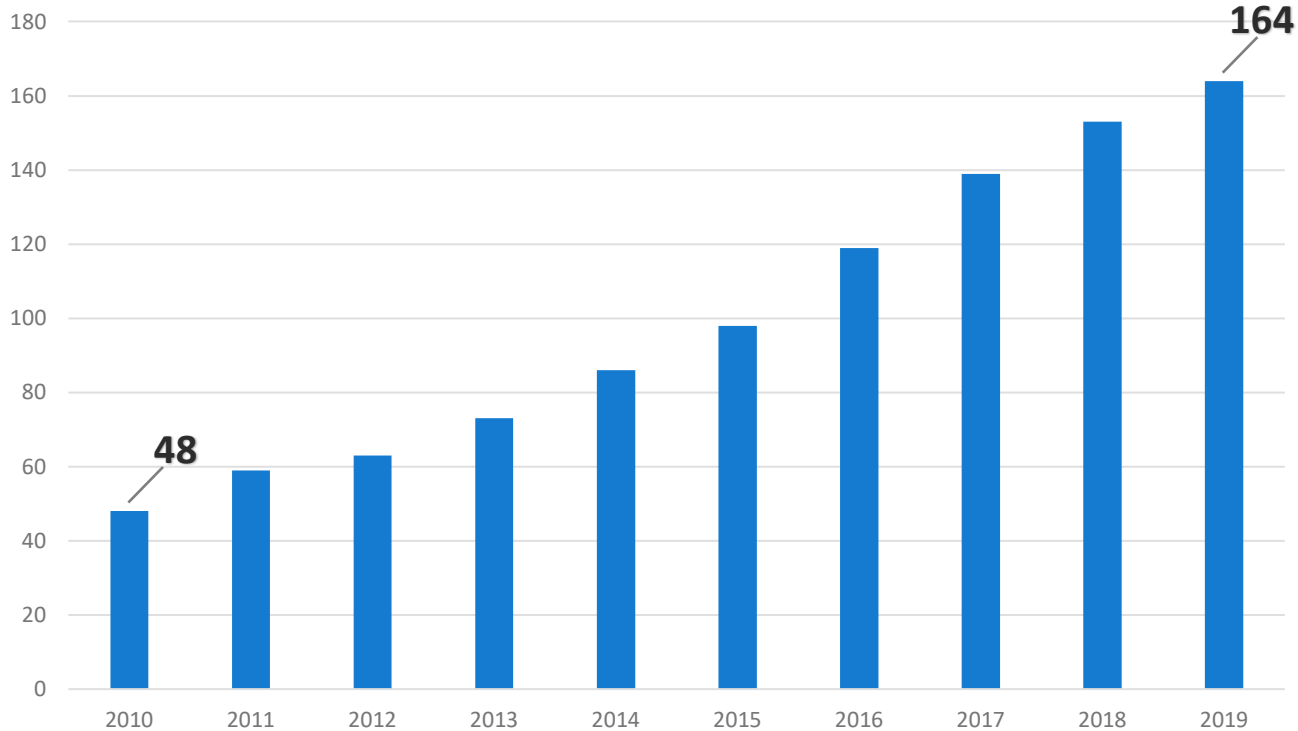
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Reasons why ESD sales tax revenues up when Cities are down

- Organic population growth
 - Largest growth rates are in Suburban counties (where ESDs with sales tax are concentrated)
 - Will organic population growth continue?
- New sales taxes elections and sales tax rate increases
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More ESDs Imposing Sales Tax

Total ESD Sales Tax Jurisdictions



Numbers include ESDs imposing a sales tax for the first time and imposing an increased sales tax rate



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 - Will organic population growth continue?
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 - Aggregate ESD sales tax is increasing
- Influence of Residence-based sales tax
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What Comprises Residence-Based Sales Tax

- Many businesses must report local sales tax based on customer address
 - Examples include:
 - Cable service providers
 - Internet service providers
 - Garbage collection companies
 - Telecommunications service providers
- Home-based businesses
 - If orders are received at the home location
- Homebuilders with Direct Pay Permits
 - Some homebuilders have direct pay permits that allow them to self report tax on their materials
 - This can lead to significant short-term spikes in sales tax if the materials are stored in your District
 - Important to consider when forecasting

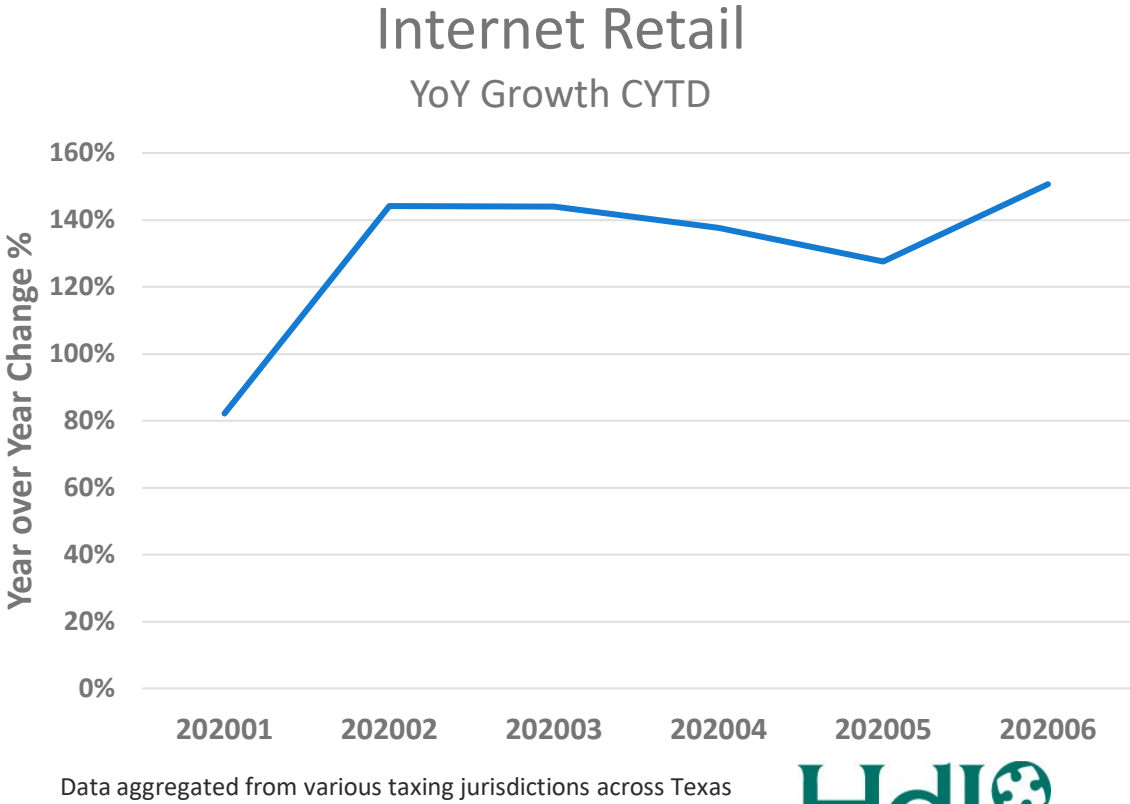
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- Influence of Residence-based sales tax
 - Businesses responsible for reporting based on customer location
 - Home-based businesses
- Internet Retail

What's New With Internet Sales?

- Marketplace Provider changes
 - Amazon, eBay, Etsy, etc. now responsible for sales tax on all sales made through their platforms
 - Has led to huge year over year spikes in Internet Retail sales tax
- Pandemic leading to even larger % of online shopping
 - This causes a shift in sales tax from the brick and mortar stores (more often in cities) to the purchasers' location (more often in ESDs)



Driving Factors

Reasons why ESD sales tax revenues up when Cities are down

- Organic population growth
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 - Will organic population growth continue?
- New sales taxes elections and sales tax rate increases
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- Influence of Residence-based sales tax
 - Businesses responsible for reporting based on customer location
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- Internet Retail
 - Marketplace Provider rule changes
 - Shift to online shopping due to pandemic

Topics to Cover

- Understanding Sales Tax Allocations
 - Why Current Period Collections are important
 - Understanding the relationship of activity months to allocation months
- Overview of Statewide Sales Tax Trends
 - May, June, July impacted by pandemic (June hit hardest)
 - Major Metro areas hit hardest
- ESD Sales Tax Trends
 - ESDs continue year over year growth
 - Impact of residence-based sales tax

 ◦ Forecasting: Examining the Outlook for ESDs

Forecasting: Where to Start

Establish a baseline that will serve as the backbone of your forecast

- Basic Option: Use Net Payment

- Pros – is based off actual allocations received from the TCPA
- Cons – Does not consider impact of audits, prior/future period payments, nor unusual taxpayer specific payments unlikely to continue

- Better Option: Use Current Period Collections

- Pros – Does consider impact of audits, prior/future period payments
- Cons – Does not consider impact of unusual taxpayer specific payments unlikely to continue

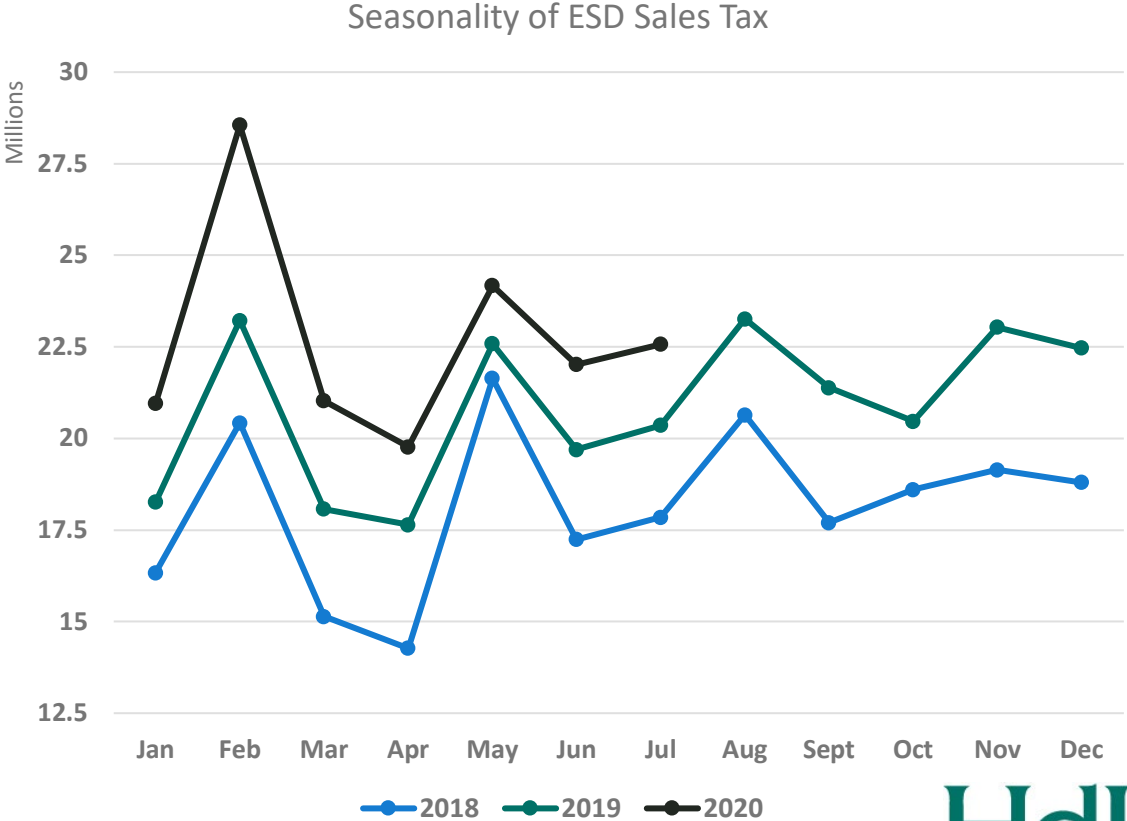
- Best Option: Request and Use Detailed Confidentiality Report

- Pros – Does consider impact of audits, prior/future period payments, and unusual taxpayer specific payments unlikely to continue
- Cons – requires more detailed analysis that can be time consuming

FIND OUT HOW HERE → [Link](#)

Forecasting: Identifying Trends

- Month to month sales tax is not a flat trend line
- Most ESDs experience quarterly spikes due to taxpayers that are only required to file once every 3 months
- February allocation will always be the highest of the year due to December sales activity
- Consider what other factors may influence seasonality in your District (like a nearby lake or annual festival)

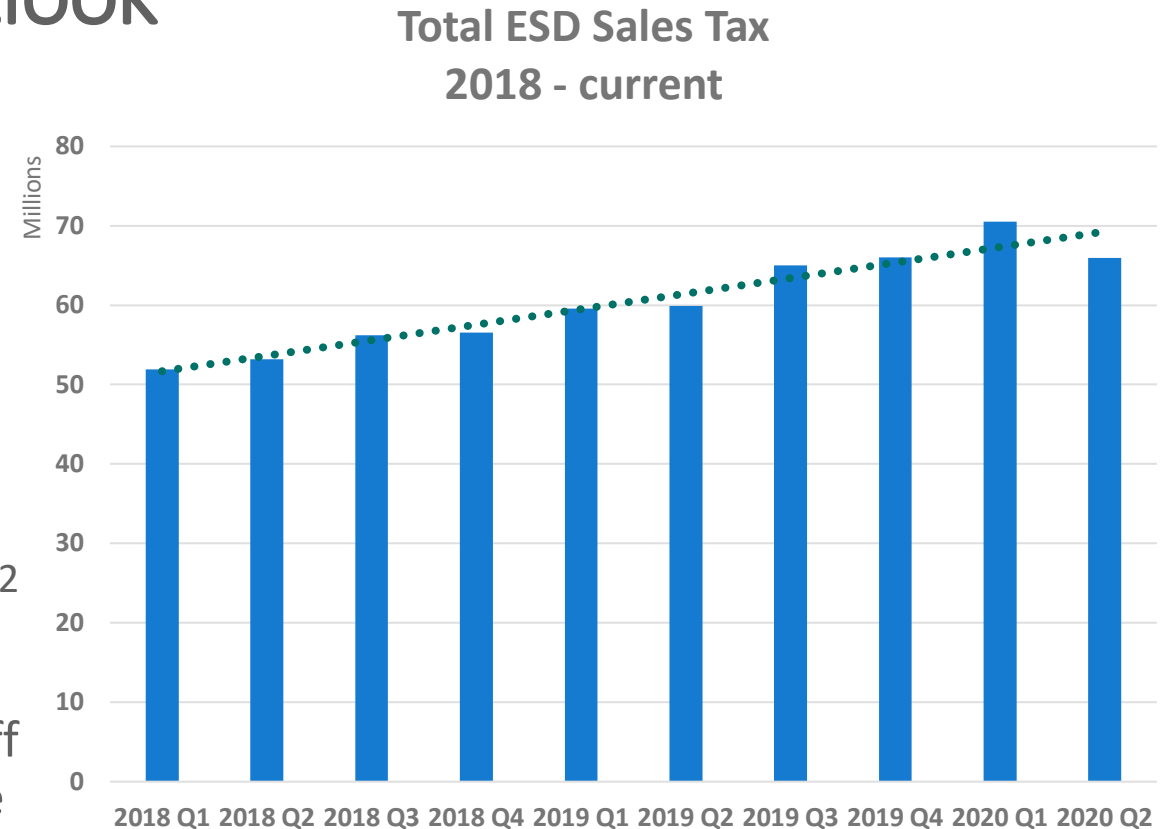


Forecasting: Looking Forward

- Determine what economic conditions impact your District
 - Some ideas include (but are certainly not limited to):
 - Texas Leading Index - [Resource Link](#)
 - Oil and Gas Prices - [Resource Link](#)
 - TX Unemployment Rate - [Resource Link](#)
 - Consumer Price Index - [Resource Link](#)
 - Remember that different types of businesses react differently to economic conditions
- If using Detailed Confidentiality Reports, consider:
 - New businesses that have opened
 - Businesses that have closed
 - Important to NOT forecast on sales tax which is not likely to continue
 - Construction projects
 - Direct pay tax

Forecasting: Near-Term Outlook

- Economists are debating different recovery trends in response to the COVID-19 pandemic (V-curves, U-curves, W-curves)
- For ESDs there is not much to “recover” from
 - Growth is still occurring but slowed slightly in 2020 Q2
- The Internet Retail sales tax increase kicked off in late 2019, so expect YoY growth to continue through the end of 2020



Forecasting: Piecing It All Together

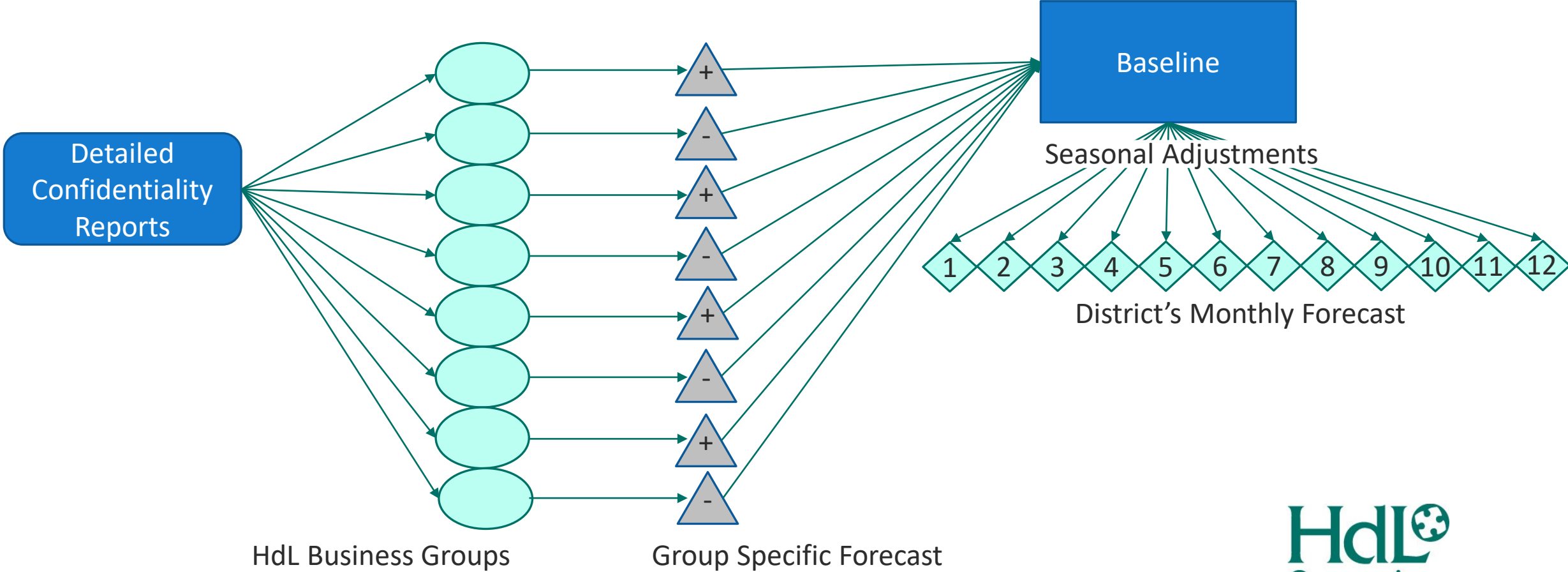
○ General forecasting formula:

Baseline (preferably by month) (adjusted for seasonal trends) × Expected Growth rate (based on economic indicators) = FORECAST

○ What function does sales tax serve in your operational budgets?

Sales Tax is....	Option	Forecast Basis
A bonus	Basic	Net Payment
Nominal compared to Property Tax	Better	Current Period Collections
Vital to operating budget	Best	Detailed Confidentiality Report

Forecasting: The HdL Approach



HDL CONSENSUS FORECAST - APRIL 2020 STATEWIDE SALES TAX TRENDS

TOTAL MAY '20 -12.8% | JUNE '20 -18.4% | 3Q20 -21.9% | 4Q20 -18.6%

(Based on Sales Tax Allocation Month)

Construction & Manufacturing MAY '20 -10% | JUNE '20 -15%

3Q20 -20% | 4Q20 -25%

This business category includes the oil and gas sector and is impacted by the recent price collapse and the reduction in demand for petroleum products as travel is curtailed. Reports suggest construction projects will continue but at a much slower pace with outdoor environmental factors and the ability to isolate workers from one another working in the favor of this business category. Current project halts and cancellation of projects not yet started are being reported by an increasing number of contractors, with shortages of equipment and materials a contributing factor. As individuals and families shelter in place, home improvement projects are a focus, lifting the near-term performance of home improvement centers such as Lowe's and Home Depot. Nonetheless, reduced overall spending compared to last year is expected. Economic uncertainties are also expected to put pressure on home sales thus hurting contractor-driven sales. US industrial production plunged in March 2020 as factories in a variety of sectors halted work to protect workers from the outbreak. Manufacturing activity is expected to continue to slow due to supply chain constraints, weaker demand, and social distancing in the workplace.

Internet Retail MAY '20 +75% | JUNE '20 +75%

3Q20 +75% | 4Q20 +65%

Substantial growth is projected in this category, fueled by the implementation of the Wayfair Supreme Court ruling beginning in October 2019 (and first reflected in sales tax allocations in December 2019) combined with an increase in online retail transactions. Remote sellers with no physical presence in Texas but marketing taxable products and services in the state are now required to collect and remit sales and use tax, and marketplace providers such as Amazon, Etsy, eBay, and Wal-Mart.com Marketplace must now report sales and use tax on behalf of third-party vendors that utilize their marketplace platforms. The shift from brick-and-mortar shopping to online retail will intensify in response to social distancing.

Restaurants & Entertainment MAY '20 -30% | JUNE '20 -45%

3Q20 -63.3% | 4Q20 -60%

Consistent with the outlook for the General Retail business category, the Restaurant and Entertainment sectors, which include hotels, are expected to experience major impacts due to travel restrictions, and cancellation of festivals, sporting events, concerts, and closures of theme parks, cinemas, museums and historical sites due to social distancing and gathering limitations. Restaurants and other facilities that prepare and serve food are largely restricted to take-out/curb-side pick-up/delivery modes. Consumer spending for food has shifted to grocery store spending in response to shelter-in-place orders. Prolonged shelter-in-place restrictions may impact the long-term outlook for this category as dining habits may change. Even as efforts shift to loosening shelter-in-place restrictions, restaurant seating capacities will be limited in response to social distancing requirements. This industry is most vulnerable to permanent closures as tight operating margins existed prior to the pandemic.

Telecom, Utilities & Other Service Providers MAY '20 +3% | JUNE '20 +3%

3Q20 +3% | 4Q20 +3%

Continued modest growth comparable to pre-COVID-19 levels is expected in this category encompassing telephone, cellular, cable, internet, data and software services, commercial and residential utilities, and waste removal services. The outlook considers an increase in demand for internet, data, and software services prompted by shelter-in-place orders and the deployment of staff and students working and learning from home.

Grocery Stores & Pharmacy MAY '20 +15% | JUNE '20 +7.5%

3Q20 +3.3% | 4Q20 +2.5%

Continued growth in this category is expected with consumers stocking up for quarantine and prolonged school closures. With most dining out options curtailed entirely or limited to take-out/curb-side pick-up/delivery, consumer spending in this category is expected to increase to support eating at home due to social distancing. In addition to major grocery store chains, such as HEB, Kroger, Randall's and Tom Thumb affiliates, this category also includes CVS and Walgreens pharmacies, convenience stores and smaller food marts. Warehouse clubs such as Sam's Club and Costco are also included as data sources suggest these entities respond economically more like grocery stores than general retail establishments.

Professional & Financial Services MAY '20 -3.0% | JUNE '20 -5.0%

3Q20 -13.3% | 4Q20 -15%

This category encompasses services delivered by professionals or other specially-trained personnel across a variety of sectors including healthcare, medical supplies information technology, property management, education, banking, insurance, credit services, and engineering and consulting services not related to the construction industry. A review of historical data suggests these services are not, individually, significant drivers of sales and use tax. As a group, however, they are worthy of note as they tend to react similarly in times of economic uncertainty. Activity across this category is expected to contract at levels consistent with the overall economy.

Other MAY '20 -10% | JUNE '20 -16%

3Q20 -20% | 4Q20 -20%

This is a "catch all" category of businesses not better classified in other categories. HdL has made a concerted effort to review and re-classify businesses to other categories to reduce the significance of this category for forecast purposes. Activity across this category is expected to contract at levels consistent with the overall economy.

General Retail MAY '20 -35% | JUNE '20 -40%

3Q20 -33.3% | 4Q20 -15%

A significant drop in core retail sales is expected as communities implement social distancing measures to flatten the curve of virus spread at the recommendation of health professionals and government leaders. Large shopping centers and popular retailers are experiencing periods of closure in conjunction with shelter in place orders. Brick and mortar retail sales are expected to be bleak through May and June. As consumer confidence drops and unemployment woes set in, it is expected discretionary spending will be curtailed and negatively impact this category throughout the remainder of 2020. Target and Walmart, while incorporating general retail, grocery, and pharmacy components, are included in this category as data suggests these businesses respond economically like other general retail businesses rather than as grocery and pharmacy entities.

Available Here!



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RICHARD FLETCHER

VICE-PRESIDENT OF OPERATIONS & CLIENT SERVICES

RFLETCHER@HDLCOMPANIES.COM

713.358.3972