

THE

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AUSTIN LETTER

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Dear Client:

Enjoy this month of good cheer – December — because as the New Year begins your elected leaders, and those who want to be your elected leaders, are going to be engaged in a high-decibel battle that will have a major impact on the way you work and live.

Start with the fact that 2006 is an election year. All statewide offices will be on the ballot. **The Texas Legislature – even though 2006 is a year when it is *not* supposed to convene in Austin – will be coming to town, under pressure, to solve a problem it has found unsolvable in the past.** At the same time, every seat in the House and half the Senate seats will be up for grabs. There will even be City Council/Mayoral elections this spring. Turn down the volume control and hang onto your wallet.

It's not just the fact the Legislature is meeting in a special session. **The Lege will be charged with changing the way you pay (or don't pay – yet) taxes.** The Texas Supreme Court ruled a previous legislative decision to help finance local schools was unconstitutional. The so-called legislative Robin Hood plan, it ruled, resulted in an illegal statewide property tax.

And the Supremes said the legislature better come up with another tax scenario before 6/1/06 — or else **many schools around the state will be shut down because no state money will be released to fund education.** Talk about pressure to do something!

So, when will the legislature roll into town? Don't know. It's up to Republican Governor **Rick Perry** to call the special session and he's created a Tax Study Commission, headed by Democrat **John Sharp**, to "study" the issue. The commission has just started its work, so it will take awhile. Best guess: **the special session will be held after the March political primaries** – giving legislators about 60+ days to do what they haven't been able to do for years.

If this timetable holds true, you can look for all those with dogs in this hunt to pour money into legislative races, to seek candidates who share their views to get them to run against incumbents who may not be friendly, etc. Yes, it's about school finance. But in the process of solving the school finance problem, **your ox may be gored by a new, or greater, tax burden than you've carried up to now.** This isn't just a school battle; it's a tax fight and will probably affect you.

Texas touts itself as one of the handful of states without a personal income tax. Is the dreaded “I” word going to be tossed into the tax mix-master when the legislature convenes?

Good question. Yes, there are those lone voices out there who have boldly suggested an income tax is the only way to raise substantial revenue to solve the state’s revenue ills. But, so far, they have been just that – **lone voices, with no broad support.**

By the way, an income tax cannot be levied in Texas without a direct vote of the people. **It’s a huge uphill climb to enact an income tax in the Lone Star State.** First of all, two thirds of both the Texas House and Senate would need to vote in favor of a constitutional amendment to levy an income tax. Then the citizens of Texas would have to amend the constitution to levy the tax upon themselves. And, if the planets aligned just right for all this to happen, the money generated by the income tax could only be spent on education. A personal income tax is not likely.

But you can bet just about every other tax angle will be considered, including new taxes and expanding existing taxes. What are the major tax revenue sources for Texas? In the 2005 fiscal year, state and local taxes generated about \$65 billion. **The biggie in the tax mix is the property tax. It generated about \$31 billion (almost \$17 billion went to public schools).** This chunk of change is the focus of the Supreme Court ruling.

What about other taxes? **The state sales tax is #2 on the list, generating about \$16 billion in 2005, with another \$4.5 billion churned out by the local sales tax portion.** It starts to taper off after the property taxes and sales taxes. Almost \$3 billion was collected on motor fuel taxes, about \$2.8 billion was realized from vehicle sales and rental taxes, another \$2.3 billion came in from oil and gas production taxes, and the corporate franchise tax kicked in about \$2.2 billion. As USSenator **Everett Dirksen** famously uttered decades ago: “A billion here, a billion there, pretty soon it adds up to real money.”

Another revenue source is to “close the loopholes,” instead of “new” taxes. In other words, add more businesses (such as law firms) to the list of those who collect sales taxes. Another way to keep from voting for taxes, legislators historically have looked to additional revenue sources that would not be necessarily be called taxes. Or they’ve taken cover by **increasing what they call “sin taxes” – beer, whiskey, tobacco, etc.**

Look for some interests to start pushing to **legalize casinos**, as an example of how the state can generate new money. After all, they will argue, if someone wants to gamble, it doesn’t hurt anyone else, so let ’em and, in the meantime, the state can rake off a tidy sum from all the bets that are placed in the casinos. Oh, and don’t forget **slot machines** in places other than casinos. Remember the **Texas Lottery** and, before that, **dog and horse racing**, all were legalized during tight financial times in Texas. And didn’t we say in the first story that all this will be taking place with legislators protecting their backsides in an election year. Stay tuned.

Speaking of next year, the long-suffering airline industry may be rising above the storm clouds of the past five years and actually heading toward blue skies.

In fact, at the rate travel is picking up here at year-end, 2005 may surpass the previous peaks for the industry set in 2000 and surpassed in 2004. You may recall the travel industry as a whole was slacking off in 2001 when the terrorists hijacked four jetliners 9/11/01 and dealt a devastating blow to all forms of US travel for years. **The long, steady climb back appears to be paying off.**

As noted in our previous reports, **Austin-Bergstrom International Airport is reflecting this national return to normalcy.** It would be an exaggeration to say passenger travel at ABIA has been amazing, but it has certainly shown a steady increase. And, you'll recall airlines have been announcing new flights serving the Austin airport, while a new airline (JetBlue) has indicated its intention to begin its first service to Texas with flights to Austin.

What is helping this along? **Fuel prices have been dropping** lately as airline **labor costs have declined.** At the same time, airlines have pared back to **eliminate excess capacity** and this is coinciding with **increased passenger travel.** It's all adding up to a strong tailwind for an industry that has been buffeted by forces of a magnitude that could never have been imagined.

This is not to suggest it is clear sailing from this point forward. There are still a record seven US airlines operating under bankruptcy protection and there will **likely be more turbulence** felt as the shakeout continues. But, for now, many airlines are flying with nearly-full planes and some of them are generating profits.

There is one **major disaster looming** that could affect the big US airlines, especially those that fly to Asia – **avian flu.** Remember SARS? When word of the SARS outbreak spread, flights were cancelled, tourism to destinations where SARS was reported dropped like a rock. Business meetings and conventions were cancelled. Very few wanted to take the risk of becoming ill.

The avian flu outbreak holds the same potential, possibly even on a grander scale. Most authorities are predicting Asia will be the first portion of the globe to feel the effect if the virus mutates to where it can be passed from human-to-human. Because of all the negative publicity about avian flu in these early stages, it is not difficult to predict a **major change in travel habits will occur if the avian flu reaches a level of widespread infection in Asia,** or even if it is concentrated in just a few major Asia cities.

But for now, there is an air of optimism circulating around the airline industry. Wall Street analysts have taken note and are issuing more positive reports about the industry. Seven airline stocks are trading near their 52-week highs. Finally – after five long years.

One of the worst hurricane seasons on record ended this week, and as we warned you at the beginning, the long-overdue Texas/Louisiana gulf coast was in the cross-hairs. The Austin area played an important role aiding our neighbors hit by the twin storms, Katrina and Rita.

Even though the winds, floods and rains did not roar this far inland (unlike previous hurricanes), the Austin area played a significant part in helping those who suffered the most. For instance, the Red Cross received **more than 10,000 applications for Katrina and Rita evacuee households in the Austin/Travis County area.** This number, while large, paled in comparison to the state as a whole where FEMA applications across Texas totaled more than 134,000.

According to a survey of apartment complexes in the Austin/Travis County area conducted by the Community Action Network, **more than 1,274 units were rented** with the help of FEMA and Red Cross vouchers.

A unit could be a family or one person. The three ZIP codes with the most units are **78741 with more than 168 units** in 16 apartment complexes, **78723 with more than 106 units** in 10 apartment complexes, and **78752 with 105 units** in five apartment complexes.

It wasn't just families or apartments opening their homes to those left without shelter, an estimated **1,255 hurricane evacuees enrolled in Central Texas school districts.**

The school district most impacted was Austin ISD with 760 enrolled. The others: Eanes, 35 ... Manor, 57 ... Del Valle, 53 ... Lago Vista, 3 ... Lake Travis, 14 ... **Round Rock, 300+** ... Elgin, 6... and Hays, 27. Austin area institutions of higher education also accepted transfers from the hurricane devastated areas.

Dr. Louis Overholster says the government has come up with a new way to save money on prescription drugs. As he put it: "To save a *little* money, you buy generics. To save a *lot* of money, you buy placebos!"

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