

# THE FISCAL IMPACTS OF COVID-19 ON STATE AND LOCAL BUDGETS

## Agenda



- □ State/Local Budgets during Recessions
  - Great Recession Fiscal Impacts
  - COVID-19 State/Local Fiscal Impacts
- □ State/Local Responses to Budget Impacts
  - Federal Aid
  - State Rainy Day Funds
  - Revenue/Expenditure Changes
- □ REMI Tax-PI and Modeling Methodology for COVID-19
- Model Demonstration in REMI Tax-PI

## Recession Impacts on Both Sides of the Fiscal Balance Sheet



- Decreasing revenue from slowdown in economic activity and shrinking of the tax base
- Increasing government spending demands for public welfare (Medicaid, Unemployment Insurance, etc.)

Increased
Demand for
Public
Expenditures

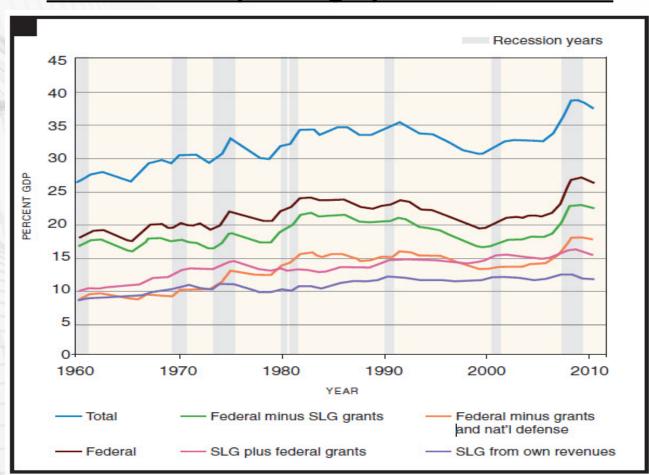
Decreased
Tax Revenue
Generation

what does REMI say? sm

## State and Local Government Expenditures in Recessions



### **Government Spending by Level and Source**



- Fed. government allocated 17% of its budget to SLG grants
- SLG Spending Increased largely from Federal Grants

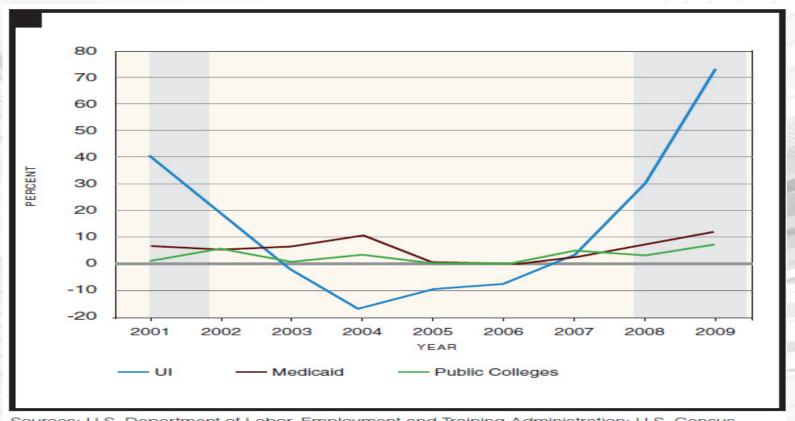
Source: National Income and Product Accounts, 2011.

Source: "State and Local Budgets and the Great Recession" (Brookings, 2012)

## **Increased Demand for Government Programs**



### **Year-over-Year Percentage Change in Caseloads for Selected State Programs**



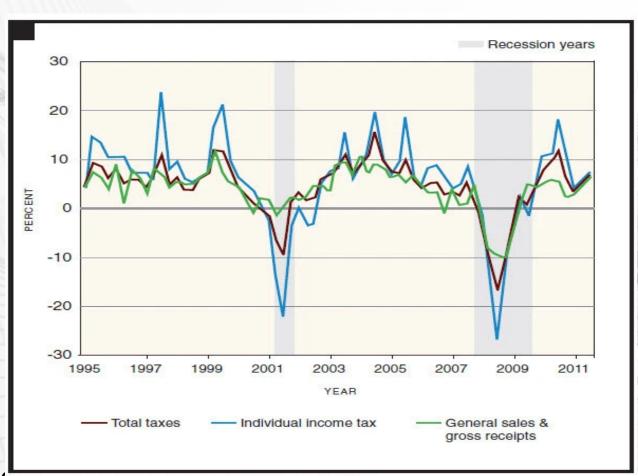
Sources: U.S. Department of Labor, Employment and Training Administration; U.S. Census Bureau Current Population Reports, Health Insurance Coverage in the United States; U.S. what does Census Bureau, Current Population Survey.

Source: "State and Local Budgets and the Great Recession" (Brookings, 2012)

## Recession Impact on State Revenues



### Percentage Change in State Taxes Year-over-Year



### **Q2 2009 Trough:**

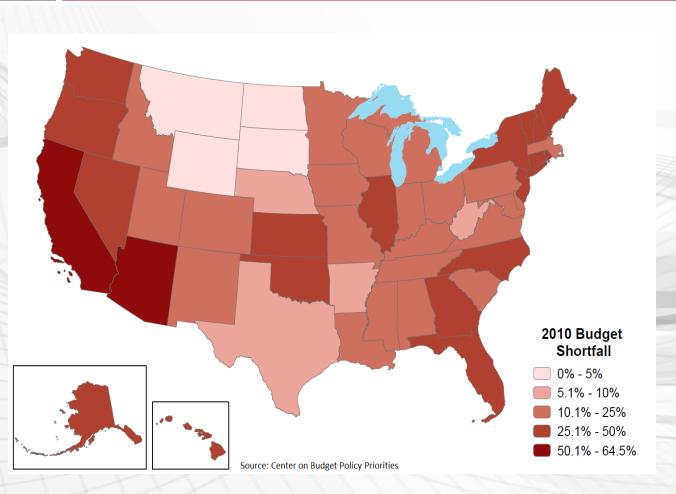
- Total State Taxes: 17% Lower
- Personal Income Taxes: 27% lower

who Source: U.S. Census Bureau, Quarterly Tax Survey, 2011.

Source: "State and Local Budgets and the Great Recession" (Brookings, 2012)

## 2010 State Budget Shortfalls State





## Largest State Shortfalls

1. California: 64.5%

2. Arizona: 57.9%

3. Nevada: 47.6%

4. Illinois: 40.9%

5. New Jersey: 38.4%

## How is this Recession different?





### **State Revenue Impacts**



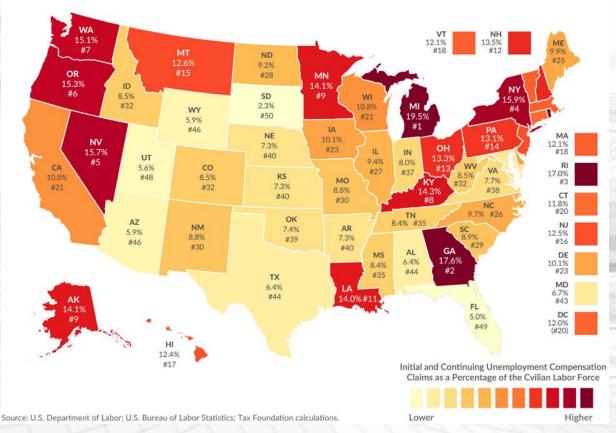
- 1. State Sales Tax
- 2. State Individual Income Taxes
- 3. Tax Filing Extensions
  - All states that tax individual income have extended their tax filing/payment deadline, following the federal action
  - 42 states have extended deadlines beyond July 1, which is the start of many states' FY2021 budgets
- 4. Transportation-driven Revenue Sources
  - State Gas Taxes- state losses could total over a billion dollars
  - Tolls/Turnpike Revenue- over \$100M lost in two months
- 5. State Capital Gains Taxes

## Individual Income Tax Base Declines - April 11



#### Unemployment Compensation Claims as a Percentage of the Civilian Workforce

Initial and Continuing Unemployment Compensation Claims as a Percentage of the Civilian Labor Force, April 11, 2020



Over 12% of US civilian labor force applied/receiving unemployment compensation benefits

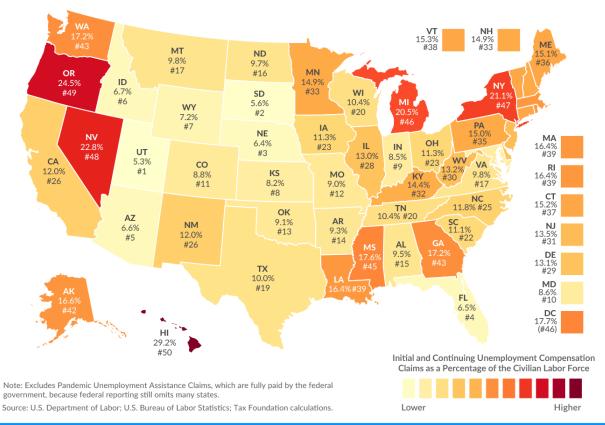
Source: "A Visual Guide to Unemployment Benefit Claims" (Tax Foundation, 2020) what does REMI say? sm

## Individual Income Tax Base Declines - May 23



#### Unemployment Compensation Claims as a Percentage of the Civilian Workforce

Initial and Continuing Regular Unemployment Claims as a Percentage of the Civilian Labor Force, May 23, 2020



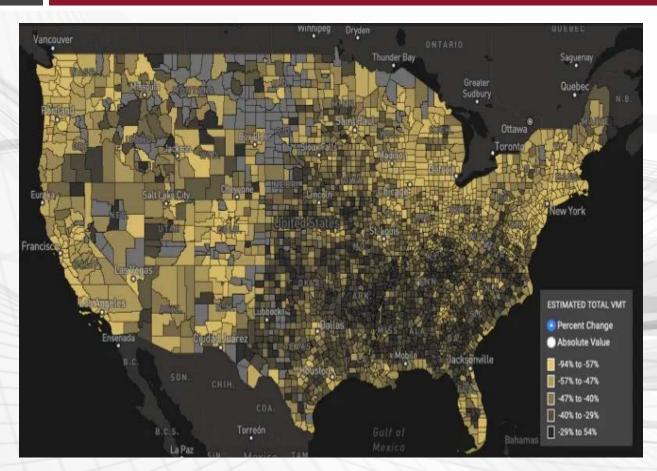
Unemployment percentage claims percentage has increased in 42 states since April

TAX FOUNDATION

@TaxFoundation

### Gas Taxes: VMT Impacts March 2 – March 27





Source: StreetLight Data and Cuebiq

San Francisco, CA 83% decrease

New York City, NY 67% decrease

Chicago, IL 67% decrease

Jacksonville, FL 46% Decrease

Montgomery, AL 32% decrease

## Gas Taxes: VMT Impacts March 1 – April 24



Every metro area down at least 53% since March

Coastal California down least 75% since March

### City and Local Revenue Impacts REMI



- City budget breakdown:
  - 5% from Federal Aid
  - 20-25% from State Aid
  - 70-75% City Revenues



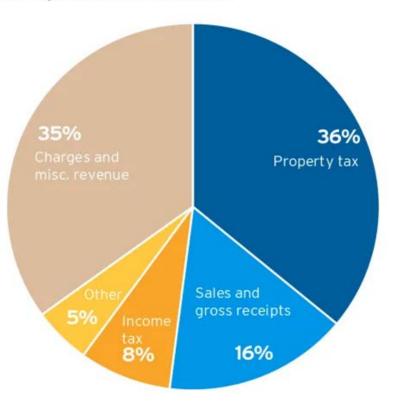
- □ Timing of impact will depend on design of city's tax structure within limits imposed by their states
  - Property Tax and Service Fees/Charges Mid/long term **Impact**
  - Income and Sales Taxes Immediate Impact

Source: Brookings

## Local Revenue Source Composition



#### Composition of municipal own-source revenue



71% of Revenues are from Property Taxes and Misc. Fees/Charges

Source: Authors' calculations of Census of Governments 2017 data.

B Metropolitan Policy Program

## Local Revenue Impacts by Category



- □ Property Taxes (inelastic)
  - Property tax bills typically reflect values of the property 18-24 months prior to collection
  - Rising unemployment eventually dampens real-estate demand and property tax revenues
- □ Fees and Charges for Services (mixed)
  - Transportation fees (transit, parking, etc.) decreases in short term
  - Trash collection, sewer, water service more stable
- Individual Income Taxes (elastic)
  - Approximately 1 in 10 cities rely most on income taxes
- □ Sales Taxes (elastic)
  - Food Services and Drinking Places, Retail Stores

## **Fiscal Response Tools**



- 1. Federal Aid
  - Coronavirus Relief Fund
  - Unemployment and Medicaid Relief
  - Transportation, Education, Children & Family
- 2. Funds in Reserve (Rainy Day Funds)
- 3. Fiscal Policy Changes
  - Tax increases to raise revenues
  - Budget cuts to decrease expenditures

### **Coronavirus Relief Fund**



- State and local governments will receive \$150 billion in federal aid under the Coronavirus Aid, Relief and Economic Security (CARES) Act
  - Allocation is by population
  - Each state is guaranteed at least \$1.25 billion even if its population share indicates a lesser amount
- Local (County/City) governments with populations of 500,000+ are eligible for aid
  - Localities are permitted to claim 45% of the amount allocated for their population, and their state retains the other 55%
  - The state retains 100% of the amount allocated to populations not within a locality of 500,000+

### **Additional Federal Aid**



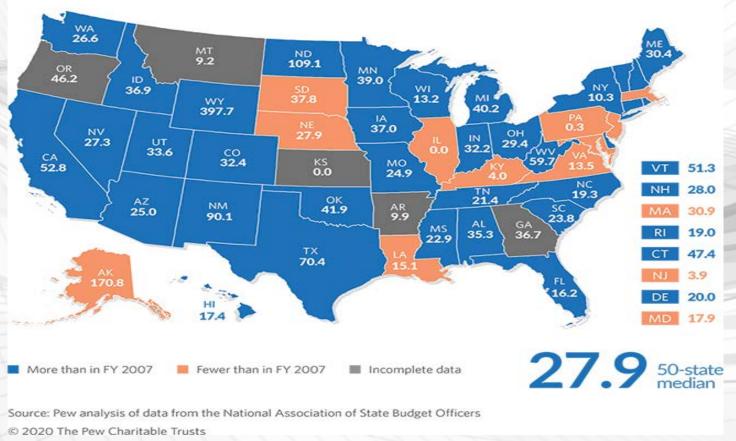
- Unemployment Insurance Relief
  - Federal reimbursement for half of states' 2020 UI payments
- Medicaid Relief
  - 10% increase in Federal Medicaid Match
- Transportation Infrastructure
  - \$25 billion to the FTA for Transit Infrastructure Grants
- Children and Families
  - \$6.3 billion to relief through Administration for Children and Families (Child Care, Community Services, etc.)
- Education
  - \$30 billion to the Department of Education to provide relief to states, school districts, and higher education institutions

## Rainy Day Funds by State: 2007 vs. 2019



#### 34 States' Rainy Day Funds Surpass Pre-Recession Levels

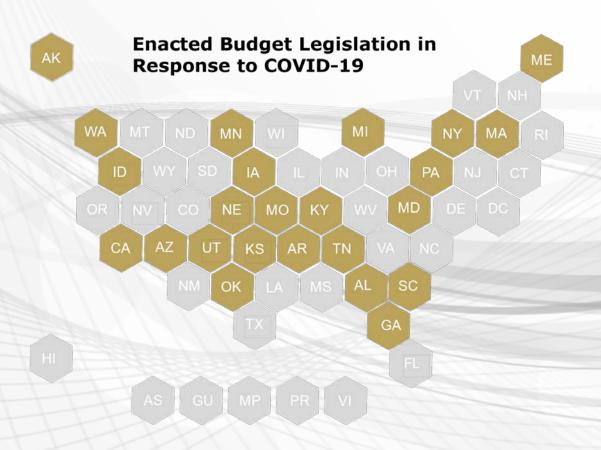
Days each state could run on rainy day funds, FY 2019



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## State Budget Legislations REMI





26 states appropriated money from general fund

12 states transferred money from rainy day and reserve funds

Source: NCSL

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## State Level Responses: 2009-2011



## **Revenue** 2009 – 2011

- 40 Increased
- 8 Decreased
- 2 Remained Constant

## **Expenditures** 2009 – 2011

- 34 Cut K-12
- 43 Cut Colleges and Universities
- 31 Cut Healthcare
- 29 Cut Social Services (elderly and disabled)
- 44 Cut Employee
   Compensation

### **About REMI**



REMI's 40-year history of rigorous academic research and software development has led to the development of the industry standard in macroeconomic research methodology:

#### **Input-Output**

Regionalized interindustry relationships

#### **Econometrics**

Behavioral responses to a changing economy

#### **General Equilibrium**

Understanding how supply and demand affects markets over time

#### **Economic Geography**

Effects of geographic concentration of labor and industry

Integrated REMI economic modeling approach



DEPARTMENT of REVENUE
Iowa Department of



Department of Economic and

Community Development



Bank of North Dakota











### What is Tax-PI?



## Answers to "what-if...?" questions about the economic and fiscal effects of policies

- □ Outputs include:
  - **Economic:** Employment by Occupation, Output, Personal Income, GRP, etc. at 70- or 160- industry sectors
  - Demographic: Population, Migration by 808 cohorts
  - **Fiscal:** Revenues such as income tax, sales tax, corporate profits tax; expenditure needs such as education, health care, public safety, public services

### Fiscal-Economic Link in Tax-PI



### **User Calibration**

- Expenditures
- Revenues

### **Build Simulation**

- Economic development
- Tax policy

### **Dynamic Results**

- Demographic
- Economic
- Fiscal

## Methodology: Overview



- Modify Baseline National Forecast to Reflect National COVID-19 Slowdown/Recession Scenario
- 2. Use COVID-19 National Forecast to Drive State/Regional Forecast
- Additional Modifications/What-Ifs for State/ Region
- 4. Fiscal Policy Responses to Budget Shortfalls

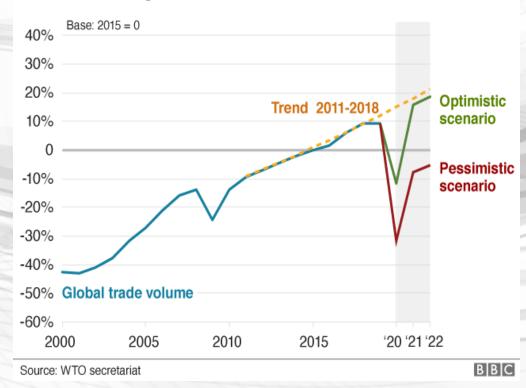
## **COVID-19 Impacts**



- Loss of Productivity,
   Absenteeism, Shutdowns
- 2. Consumer spending
- 3. Supply chain disruption
- 4. Decline in global demand
- 5. Increase mortality rate

### World Trade set to plunge

Growth rate for global trade and WTO scenarios



## Example Fiscal Responses in Tax-PI REMI



### **Revenue Side Responses**

- □ Sales tax increase
  - Policy Variable Affected → Consumer Price Increase
- □ Individual income tax increase
  - Policy Variable Affected → Disposable Personal Income Decrease
- □ Federal Aid Increase

### **Expenditure Side Responses**

- □ K-12 Education Spending Decrease
- **Higher Education Spending Decrease**
- □ Corrections Spending Decrease
- Optional ability- marginal demand for expenditures



### **Model Demonstration**