



THE VOLCKER ALLIANCE

Empowering and Inspiring Public Servants

October 26, 2023

**Critical US State and
Local Budget Issues:
Slowing Revenues,
Recession, and
Infrastructure
Opportunities**



2023 Annual Conference, Denver

Lauren Larson

**Former State Budget Director, Colorado &
President, National Association of State Budget Officers**

Never let a good crisis go to waste

Colorado's Forward-Looking Response

Increasing planning tools to address stimulus complexity

Attention to recurring vs one-time investments

Long range planning to manage fed funds roll-off

Maximizing investments

Avoiding peanut butter spread

Planning for infrastructure match dollars, supporting local capacity

Recession preparedness

Building reserves

Scenario planning

Complexity of Stimulus Data

Much More than SLFRF

Colorado stimulus in \$ billions

ARPA State and Local Fiscal Rec Funds (SLFRF)	\$3.83
ARPA Direct to Agencies*	\$3.55
State General Fund	\$1.27
Total Stimulus Funds**	\$8.45

*Excludes FMAP and Direct to Education

**Excludes IIJA, IRA, CHIPS Act

Significant Amounts in Non-Appropriated Funds

An amount about equal to Colorado's SLFRF was sent direct to agencies

Snapshot of Federal Direct-To-Agency Stimulus Allocations, by Department	
Department	Total Allocation Currently Tracked (\$M)
CDA	\$2
CDE	\$181
CDHS	\$260
CDEC*	\$601
CDPHE	\$926
DOLA	\$662
GOV	\$32
HCPF	\$583
LG	\$16
OEDIT	\$117
OIT	\$171
Total	\$3,551

Source: Colorado OSPB FY24 budget
11/1/2022

*some amounts appropriated

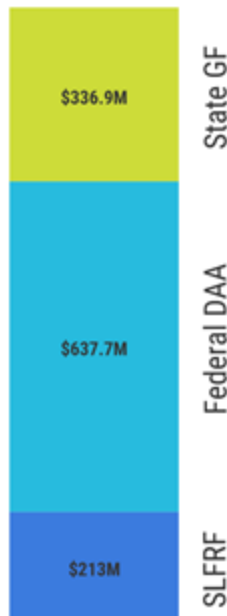
Agencies Face Complexity of Fund Sources, Deadlines and Requirements

Colorado Examples

DOLA: Affordable Housing

Direct to Agency Awards:

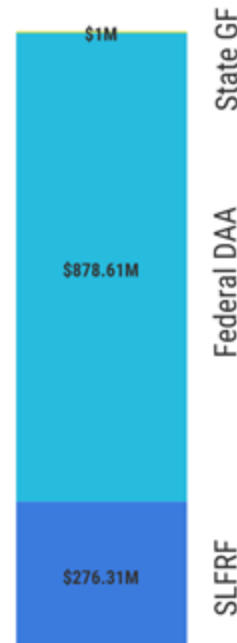
- ERA (\$456.1M)
- Homeowner Assistance (\$175M)
- Vouchers (\$6.5M)



CDPHE: Public Health

Direct to Agency Awards:

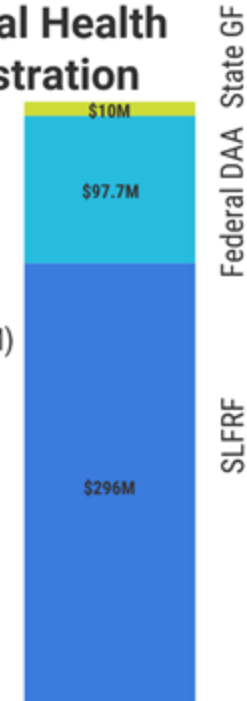
- CDC (\$878.61M)



Behavioral Health Administration

SLFRF Awards:

- 2021 (\$84.8M)
- 2022 (\$211.2M)



Source: Colorado Recovery Office

Tracking Roll-off Will Be Even Harder

Appropriation Methods for Backfilling ARPA Roll-off: Colorado Examples

ARPA Investment	Implementing Agency	Total General Fund Invested in FY 2023-24 Budget	Appropriation Method	Program Description
Rapid Mental Health Response for Colorado Youth ("I Matter")	CDHS	\$6.0	Previously approved by legislature through HB 22-1243 Fiscal Note. In FY 2023-24 Budget, see: BHA TA-49.	The "I Matter" program, managed by the Colorado Behavioral Health Administration, provides access to mental health and substance use disorder services for youth, including addressing needs that may have resulted from the COVID-19 pandemic. The program provides youth with six free therapy sessions and reimburses participating licensed therapists.
Home and Community-Based Services (HCBS) - Base Minimum Wage Increase	HCPF	\$63.2	Previously approved by JBC in FY 2022-23 budget (R-10). In FY 2023-24 budget, see: HCPF TA-28.	HCPF's proposed plan for ARPA one-time enhanced federal funding for HCBS was approved by the Centers for Medicare and Medicaid Services (CMS) and the Joint Budget Committee (JBC) in September 2021. That plan included increasing rates for certain HCBS services with a requirement for providers to pay at least \$15 per hour base wage for frontline staff providing direct hands-on care.
Contracted Mental Health Residential Beds	HCPF	\$11.5	Previously approved by legislature through HB 22-1303 Fiscal Note. In FY 2023-24 budget, see: HCPF TA-43.	HB 22-1303 appropriated ARPA SLFRF funds to increase the number of residential behavioral health beds statewide. This includes 107 beds that are being contracted by CDHS, with HCPF seeking waiver approval for federal funding starting in FY 2023-24. The fiscal note for this bill assumes that beginning in FY 2023-24, federal Medicaid funds will support the 107 contracted beds, split evenly between the General Fund and federal funds. This means that the FY 2023-24 budget includes an annualized amount to meet the General Fund match required for the beds to be funded by Medicaid.
Waitlist Prevention for Children's Behavioral Health Services	BHA	\$3.0	Previously approved by JBC through Fall 2022 1331 supplemental.	The Children and Youth Mental Health Treatment Act (CYMHTA) services support families with children as an alternative to child welfare involvement when a dependency and neglect action is not warranted. This \$3M investment is vital in order to limit the occurrences of children needing to enter the child welfare system. Services may include mental health treatment services and care management, including any residential treatment, community-based care, or any post-residential follow-up services that may be appropriate.

Source: Colorado OSPB FY24 budget
11/1/2022

Planning for Federal Funds Roll-Off

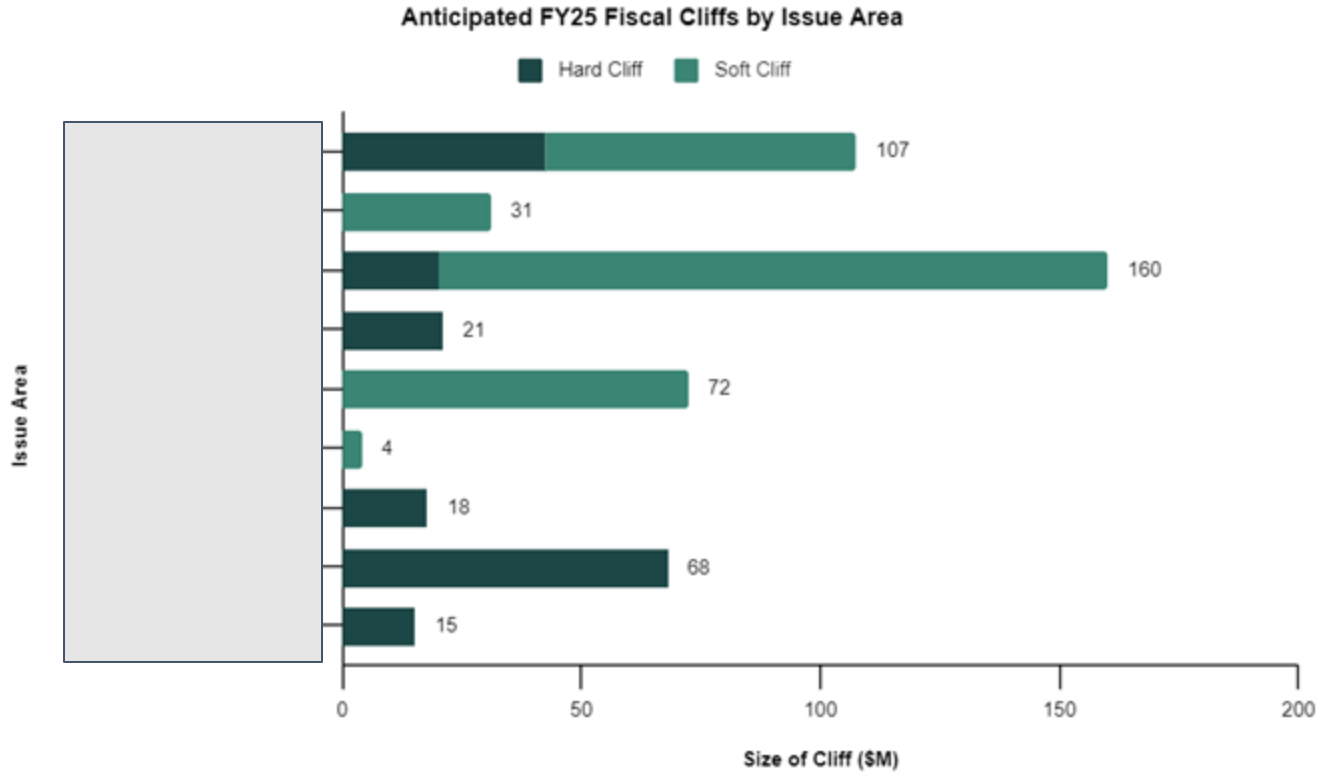
Early Planning Efforts Crucial to Avoid Structural Deficit

Colorado Example: “Big Ten” Exercise

- With hundreds of stimulus programs, how does a small budget staff plan for federal funds roll-off?
- OSPB evaluated the 10 largest fed funds programs to develop a preliminary estimate of potential fiscal cliffs as stimulus rolls off (June 2022)
- Categories of cliffs
 - **Hard cliffs** = commitments already made through stimulus legislation to provide ongoing General Fund support (about \$200 million per year)
 - **Soft cliffs** = funding pressures we expect to arise as one-time stimulus funds roll off (about \$300 million per year)
 - **Watch list** = other programs/recipients that received significant federal funds and may raise on-going funding issues (\$ billions)

Early Governor Input on Large Dollar Cliffs

Pro Forma Roll-Off Decision Tool



Early Planning Drives Action to Prevent Structural Deficit

More Solutions for Solving Colorado's Roll-Off Challenges

- Governor's early feedback informed OSPB's 5-year structural balance modeling used to set budget targets for agencies.
- FY25 Budget guidance to agencies included:
 - Hard targets for stimulus repurposing
 - Strict rules for General Fund backfill requests
- Early planning informed request to legislature for long-range planning FTE resources—secured during the 2023 legislative session

Maximizing Investments

Avoiding Peanut Butter Spread

SLFRF Distribution Agreement with Legislature
Based on Statewide Listening Tour

ARPA SLFRF **\$3.83**

$\frac{1}{3}$ Budget stabilization

$\frac{1}{3}$ Transformational investments
-affordable housing
-behavioral health
-workforce

$\frac{1}{3}$ Economic recovery (UITF and shovel-ready transpo)

IIJA \$4-7 Billion Impact for Colorado

Investment Category	CO Estimate- Low Range (\$M)	CO Estimate- High Range (\$M)	Total Match Needs- High Range (\$M)
Airports	\$430M	\$849M	\$149.4M
Broadband	\$427M	\$712M	\$138M
Electric Vehicles and Buses	\$57M	\$220M	\$27M
Environmental	\$345M	\$372M	\$0M
Power and Grid	\$283M	\$1,239M	\$128M
Passenger and Freight Rail	\$28M	\$237M	\$42M
Public Transit	\$227M	\$247M	\$54M
Ports/Waterways	\$356M	\$356M	\$0M
Resiliency	\$121M	\$316M	\$12M
Roads, Bridges & Major Projects	\$1,000M	\$1,507M	\$378M
Safety & Research	\$16M	\$149M	\$24M
Water Infrastructure	\$856M	\$936M	\$85M
Grand Total	\$4,145M	\$7,139M	\$1,049M

Source: Colorado OSPB Forecast Sept 2022

\$1B Match Need? Much Is Covered in Base

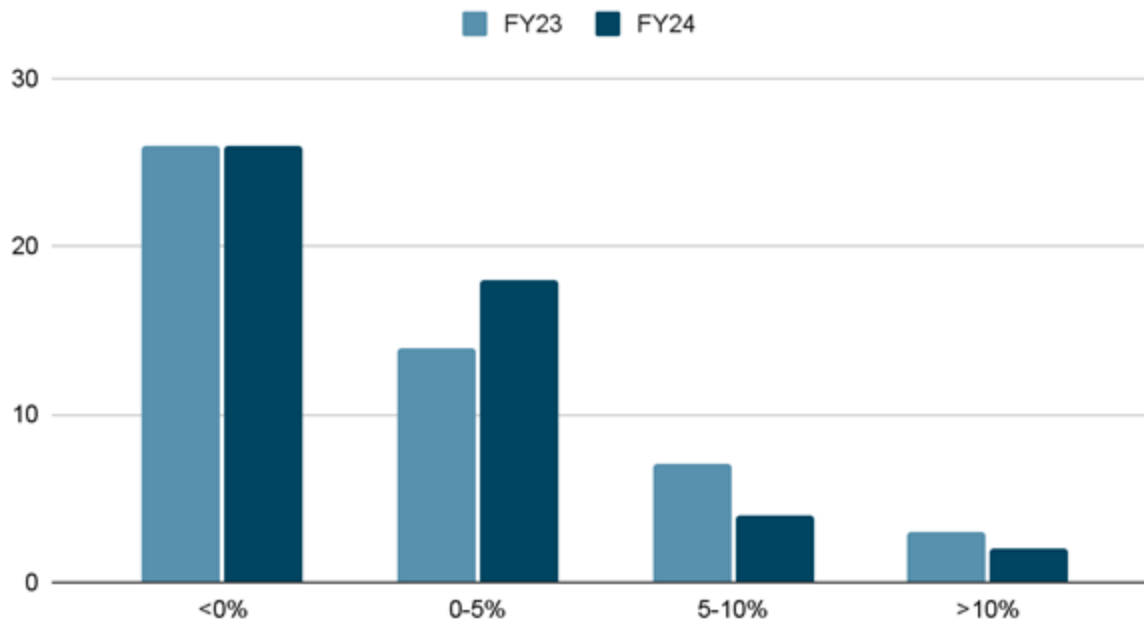
Investment Area	Estimated Agency Match Support Need(\$M)	Estimated Agency Match Estimate Includes:
Transportation	61.2	\$41.8M estimate for match need on rail projects, an additional \$10M for Front Range Rail and \$9.4M estimate for match need on transit programs.
Water	47	\$47.0 M for water programs to replace lead lines, increase funds for the elimination of harmful chemicals and particulates in drinking water, and other water projects.
Power & Grid	1.5	\$1.5M match needed for phase 1 of Hydrogen Hubs - a four-state partnership with neighboring states to design, construct and deliver a hydrogen hub facility for alternative energy.
Broadband (OIT)	51.6	\$51.6M to increase broadband access in hard to connect rural areas and historically left behind areas.
Local & Tribal Match Needs	10	\$10M in resources to support match needs from local agencies applying directly for projects that are not eligible for states.
<i>Total Match Need for IJJA Programs</i>	171.3	This reflects the total outstanding match need that has been identified across the State government and includes an additional 10M in local and tribal government match support.

Source: Colorado OSPB FY24 budget 11/1/2022, *updated*

Recession preparedness

Putting tax cuts in context

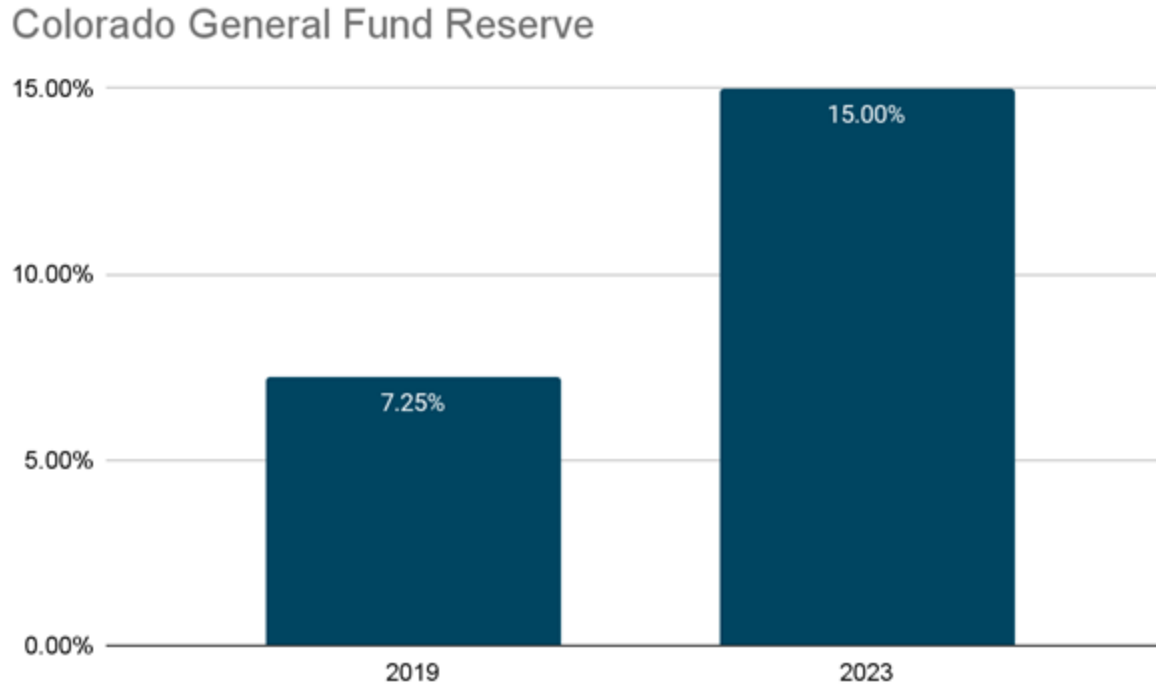
Revenue projections by number of states



- Average projections - 0.3% FY23 -0.7% FY24
- However this includes policy changes
- And is coming off two record high years +16.6% FY21 +16.3% FY22
- Forecasts vary widely by state

Source: NASBO 2023 Fiscal Survey of the States

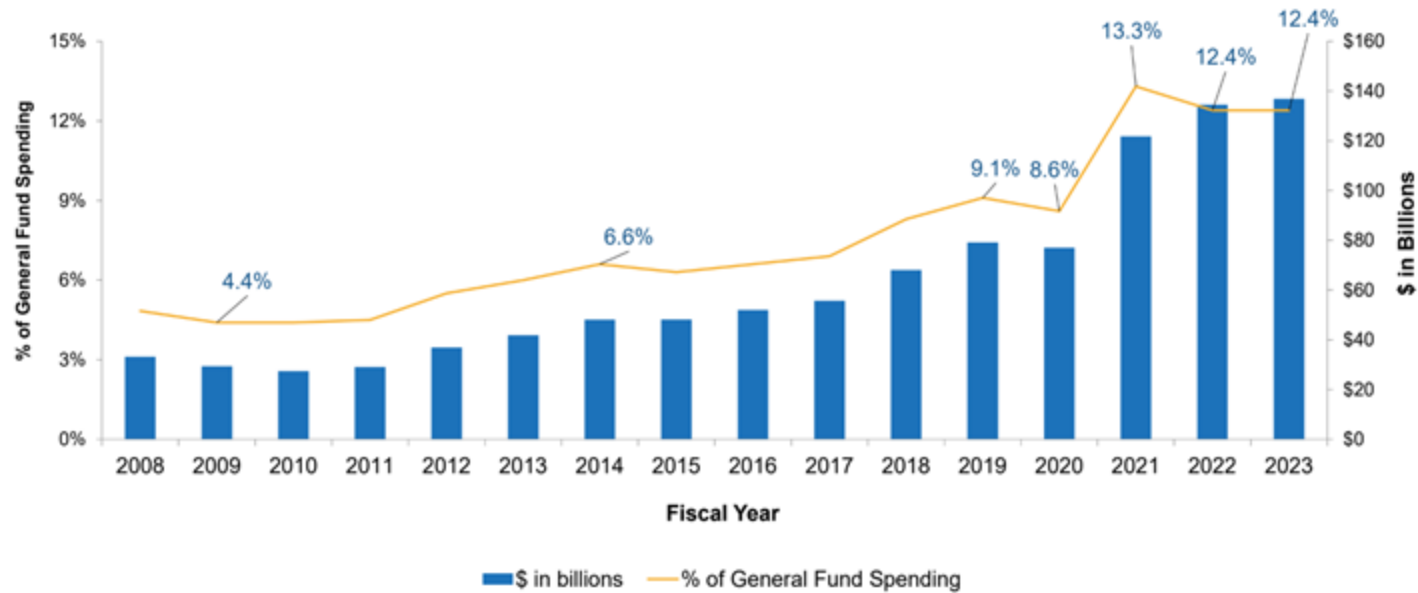
Reserves more than doubled



Rainy day fund strength



State Rainy Day Funds



Source: NASBO Fiscal Survey of States



Source: NASBO 2022 Fiscal Survey of the States



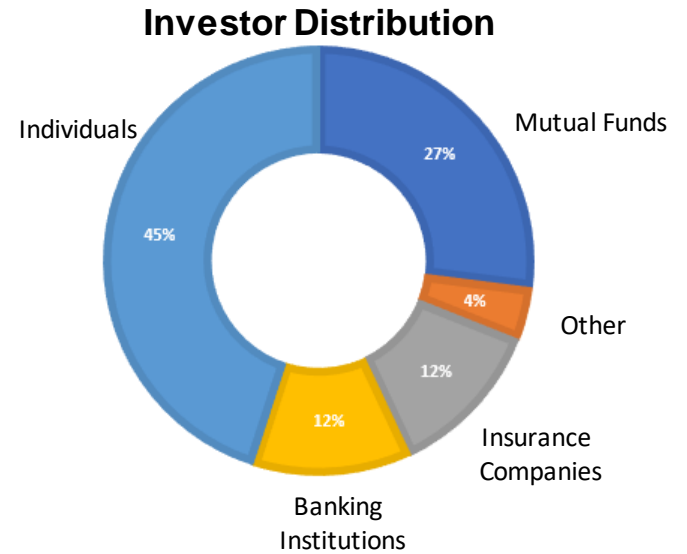
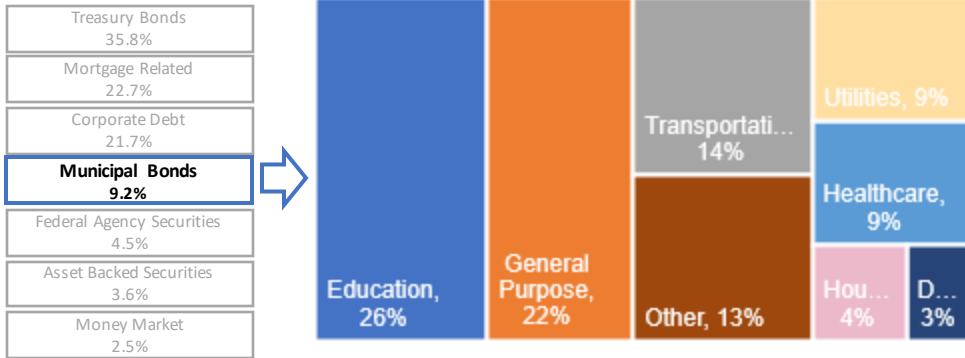
Lauren Larson is an internationally recognized financial expert—a former CFO of a \$40 billion organization with proven results in risk management, operations improvement, and regulatory relief. Larson was appointed by two Governors to be Director of the *Colorado Office of State Planning and Budgeting*, a Cabinet-level position where she led the state’s fiscal response to the COVID-19 pandemic. Her strategy doubled rainy day reserves while achieving all of the Governor’s policy goals. Larson was elected by her CFO peers in the 50 states to be President of the *National Association of State Budget Officers*, a board chair position.

Larson also was a leader at the *White House Office of Management & Budget*, where she served as Chief of the Treasury Branch under Presidents Bush and Obama, managing a \$50 billion budget and ensuring strong fiscal controls for the \$700 billion Troubled Asset Relief Program (TARP). She advanced as a corporate economist at *PricewaterhouseCoopers LLP*, delivered regulatory relief for businesses, and worked internationally in London and Paris. Larson holds degrees from Syracuse University (BA) and the University of Michigan (MPP).

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USPF Market Overview

Municipal Bonds Make Up **9.2%** of the **U.S. Bond Market**
48% Fund **Education** or **General Purpose**



Understanding S&P Global's Ratings

- An issuer's **ability** and **willingness** to pay debt in a **timely** manner
- Credit ratings are **forward looking**
- S&P Global ratings are **opinions**, not guarantees of credit quality or exact measures of the probability that a particular issuer or particular debt issue will default
- The Ratings scale **is relative** and based on the creditworthiness of an issuer or credit quality of an individual debt issue, from strongest to weakest, within a universe of credit risk
- Criteria provide the analytic framework to derive the rating opinion

[Understanding Credit Ratings | S&P Global Ratings \(spglobal.com\)](https://www.spglobal.com/ratings)

US Public Finance Update: Q4 2023

What we're watching

- Higher interest rates and inflation remain headwinds for most issuers from a debt issuance and operating/capital budget perspective
- Extreme weather events continue, requiring swift response and resource allocation. Cost and availability of property insurance are emerging as a challenge

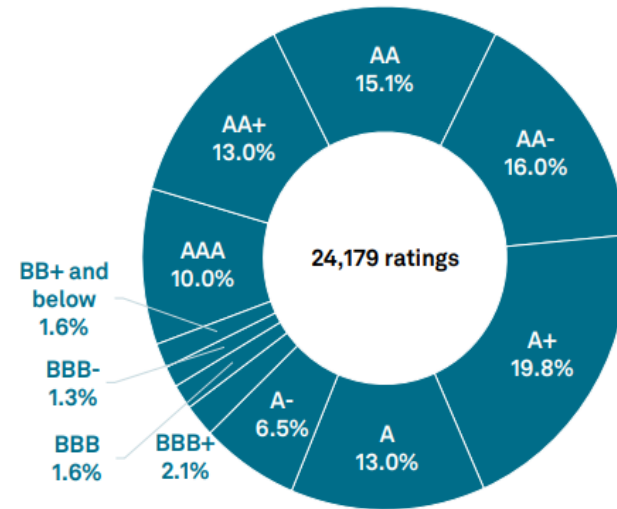
Trends

- Credit conditions have been largely stable, and upgrades have exceeded downgrades this year for most sectors
- The U.S. economy has been resilient, but we expect slower growth ahead. Federal budget deliberations and increased geopolitical tensions could further limit growth
- Federal stimulus and healthy financial reserves continue to provide significant flexibility

Rest of year expectations

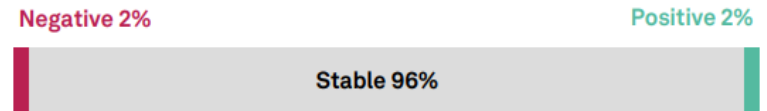
- Our baseline U.S. economic forecast is now for a shallower but more protracted slowdown rather than a recession; however, we don't expect this to disrupt credit stability for most issuers

U.S. Public Finance Ratings Distribution



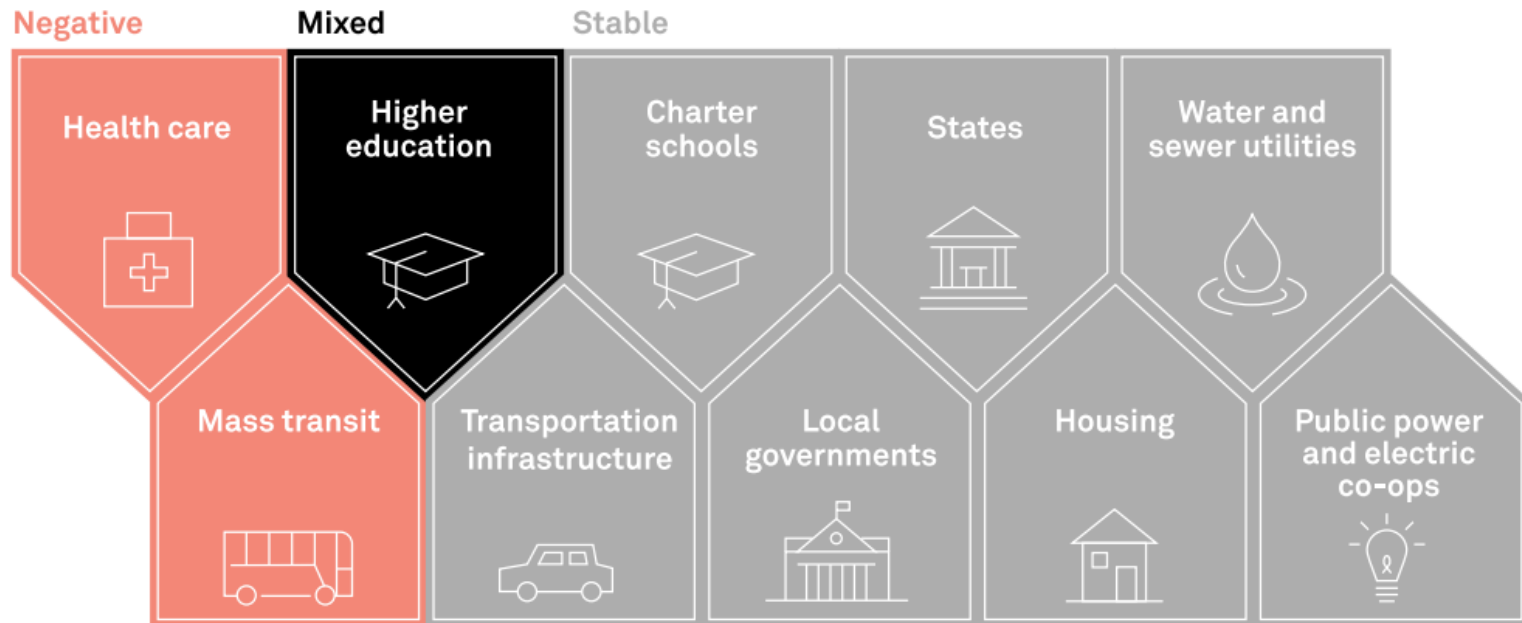
Source: S&P Global Ratings.

Outlook distribution



Source: S&P Global Ratings.

US Public Finance Update: Sector Views



Economic Forecast: Q4-23 Key Indicators

S&P baseline forecast does not include a recession in the next 12 months

As of September 2023	2019	2020	2021	2022	2023f	2024f	2025f	2026f
Real GDP (annual average % change)	2.3	-2.8	5.9	2.1	2.3	1.3	1.4	1.8
Change from June (percentage point)					0.5	0.0	-0.1	-0.1
Real GDP Q4/Q4 (annual average % change)	2.6	-1.5	5.7	0.9	2.2	1.1	1.6	1.9
Change from June (percentage point)					0.9	-0.4	0.0	0.0
Consumer spending (annual average % change)	2.0	-3.0	8.3	2.7	2.5	1.4	1.5	2.1
Equipment investment (annual average % change)	1.3	-10.5	10.3	4.3	-0.8	1.4	1.7	2.2
Nonresidential structures investment (annual average % change)	2.3	-10.1	-6.4	-6.6	7.6	1.1	0.5	3.2
Residential investment (annual average % change)	-1.0	7.2	10.7	-10.6	-11.1	0.7	3.2	1.8
Core CPI (annual average % change)	2.2	1.7	3.6	6.2	4.7	2.6	2.3	2.3
Core CPI Q4/Q4 (annual average % change)	2.3	1.6	5.0	6.0	3.7	2.4	2.3	2.3
Unemployment rate (%)	3.7	8.1	5.4	3.6	3.6	4.1	4.7	4.8
Housing starts (mil.)	1.3	1.4	1.6	1.6	1.4	1.4	1.4	1.4
Light vehicle sales (mil.)	17.0	14.5	15.0	13.8	15.2	15.2	15.5	15.6
10-year Treasury (%)	2.1	0.9	1.4	3.0	3.9	4.0	3.6	3.6

Note: All percentages are annual averages, unless otherwise noted. Core CPI is consumer price index excluding energy and food components. f--Forecast.
Sources: Bureau of Economic Analysis, Bureau of Labor Statistics, The Federal Reserve, S&P Global Market Intelligence Economic Simulink, S&P Global Ratings Economics' forecasts.

USPF Q4 2023 Sector Summary

Local government

What we're watching

- Macroeconomic pressure that affects revenue growth, especially at the state level where shortfalls can trickle down to local governments
- Inflationary pressures or weakening consumer confidence that leads to a pull-back in consumer spending and slow sales tax collections

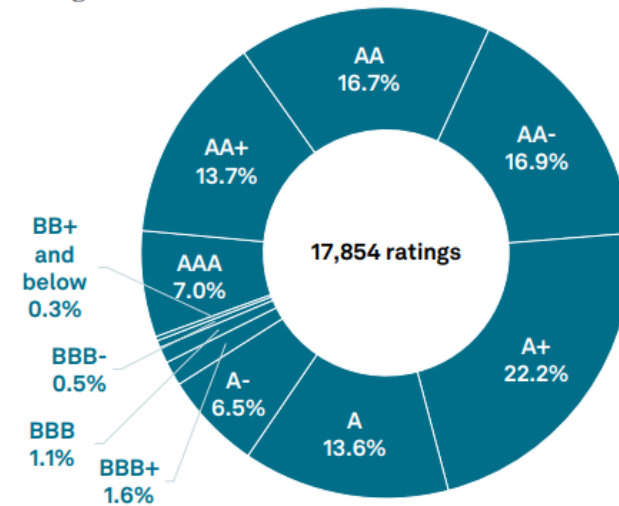
Trends

- Financial stability created by healthy reserves and enhanced by economic growth and pandemic-related federal stimulus
- Labor shortages that create difficulty in hiring workers and require more innovative solutions to staff key positions

Rest of year expectations

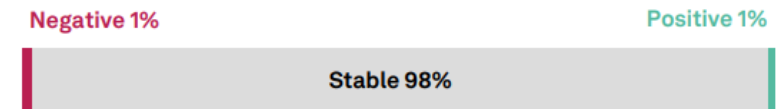
- Continued credit stability stemming from a benign economic environment; support from federal stimulus dollars, which many local governments have yet to spend
- Limited impact to local governments from federal government budget negotiations, although an extended shutdown could have wider-reaching implications for the macro economy

Ratings distribution



Source: S&P Global Ratings.

Outlook distribution



Source: S&P Global Ratings.

By The Numbers: Remote Work Challenges

U.S. share of days worked from home



U.S. remote-capable jobs working 100% onsite



Office occupancy in select cities based on badge swipes



Estimated per person reduction in annual consumer spending in large U.S. cities

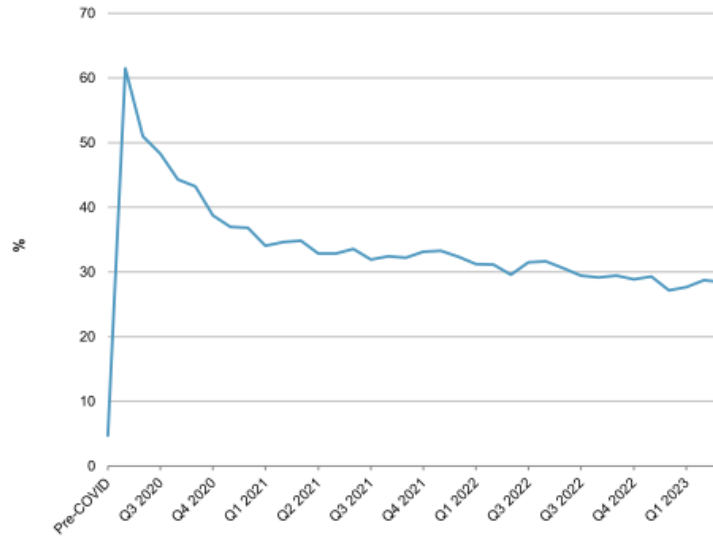


U.S. office vacancy rate (Q1 2020 to Q1 2023)



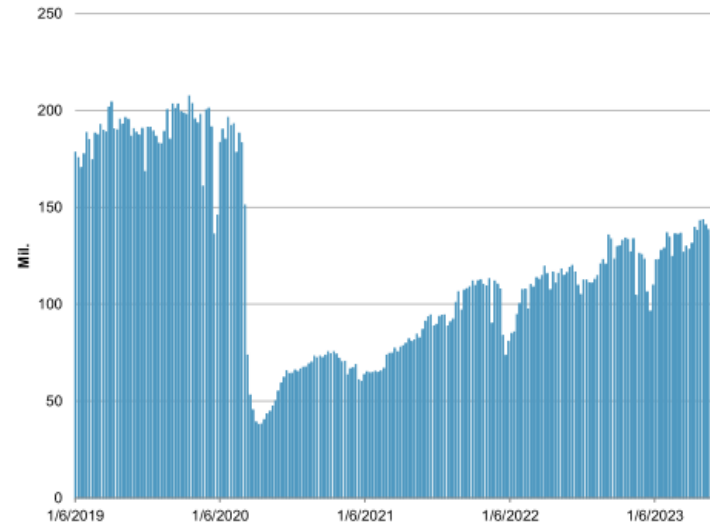
Sources: WFH Research – U.S. Survey of Working Arrangements And Attitudes, Gallup, Kastle Systems' Weekly Occupancy Data: Back to Work Barometer, Cushman & Wakefield, American Public Transportation Assn. Copyright © 2023 by Standard & Poor's Financial Services LLC. All rights reserved.

Percent of full paid days worked from home



Source: WFH Research – U.S. Survey of Working Arrangements And Attitudes.
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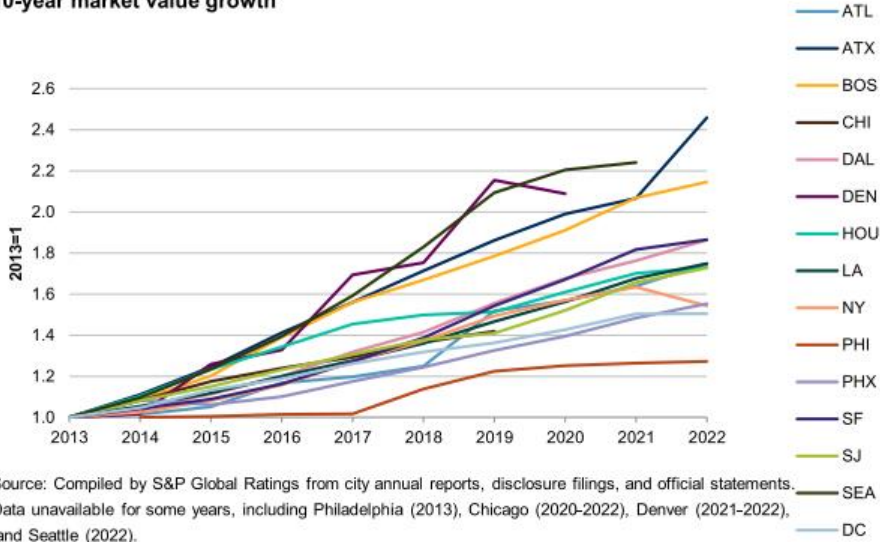
U.S. public transit weekly ridership



Source: American Public Transportation Assn.
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Property Values and Stability

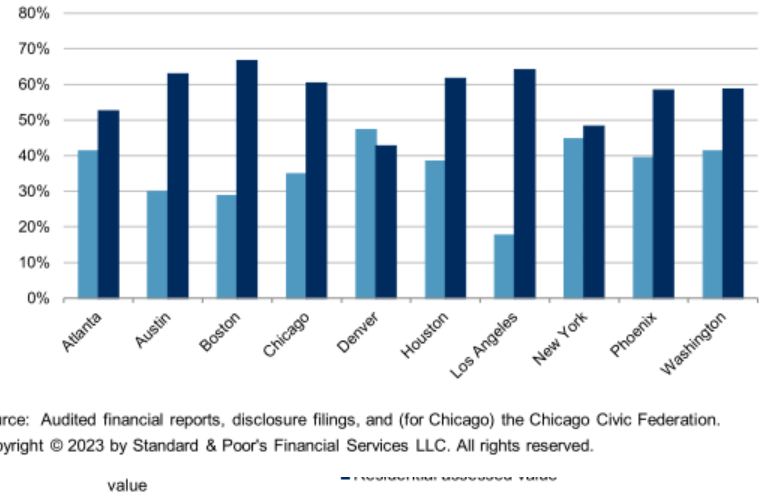
10-year market value growth



Source: Compiled by S&P Global Ratings from city annual reports, disclosure filings, and official statements. Data unavailable for some years, including Philadelphia (2013), Chicago (2020-2022), Denver (2021-2022), and Seattle (2022).

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Assessed value: Commercial versus residential

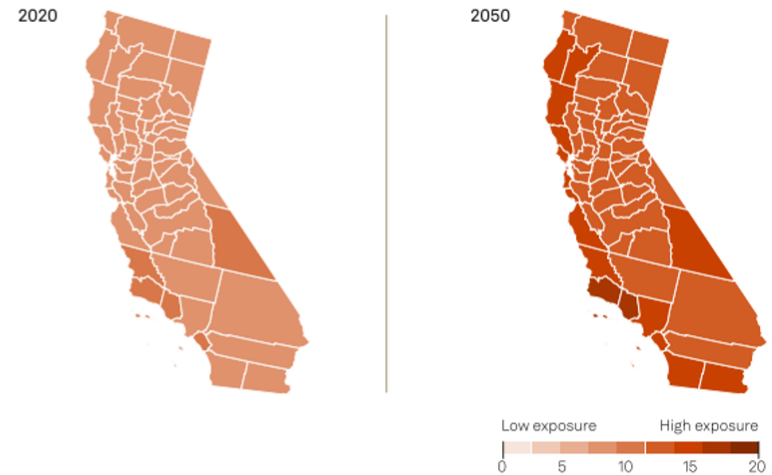


Source: Audited financial reports, disclosure filings, and (for Chicago) the Chicago Civic Federation. Copyright © 2023 by Standard & Poor's Financial Services LLC. All rights reserved.

Extreme Weather Remains On The Radar

- Extreme weather events, including hurricanes, droughts, and flooding remain one of the key emerging risks we're watching for U.S. governments and not-for-profit enterprises
- Through early September 2023, the National Oceanic and Atmospheric Administration reported 23 separate \$1 billion events, leading to more than \$57 billion in costs
- The 2023 reported events exclude Tropical Storms Hilary (Southern California) and Ophelia (Eastern Seaboard)
- By comparison, in 2021 and 2022, there were 20 and 18 \$1 billion events recorded, respectively
- Wildfires are still primarily sparked by lightning, wind, and human activities, but the frequency of these events is increasing and encroaching on communities and populated areas
- Extreme heat can contribute to the prevalence of water shortage conditions as precipitation evaporates more quickly and there is less recharge of underground water sources, which together, can lead to higher wildfire risk due to dry vegetation and lower ground moisture, among other impacts
- When speaking with entities exposed to wildfires, we typically ask about adaptation efforts that may include frequency of vegetation management, ability to acquire fire insurance, and code changes including requirements for more fire-resistant building materials

California's counties exposure to extreme heat 2020 versus 2050 (decadal comparison)



Note: Maps show a change in exposure (represented on a 1 to 100 scale) from S&P Global Sustainable 1's Climate Change Physical Risk dataset. Source: S&P Global Ratings.

What We're Watching



Federal Stimulus

Still providing support;
Waning influence over next
two years



Employment/Wages

Cost to attract and retain
talent is rising; LT budgetary
balance challenges



Inflation & the Economy

CPI waning, but higher
interest rates will stay
creating broad implications



Extreme Weather

Too much—and too little—
water is accelerating
challenges



Government Shutdown

Next Up: Nov. 17
Short shutdowns aren't
same upheaval as long



RTO & Impact on Tax Base

Remaking cities takes time
and money. Can tax revs
wait that long?

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Volker Alliance's State and Local Budgeting in the COVID Era Series

The Revenue Side of "The Fiscal Cliff"— State Tax Policy Changes During and After COVID-19

**Can Chen
Alex Hathaway
Seun Odibo
Meghna Paul
Meera Omar**

**Andrew Young School of Policy Studies
Georgia State University**

**ABFM 2023 Annual Conference, Colorado, CO
October 26, 2023**



THE VOLCKER ALLIANCE
Working for Effective Government



**Georgia State
University**

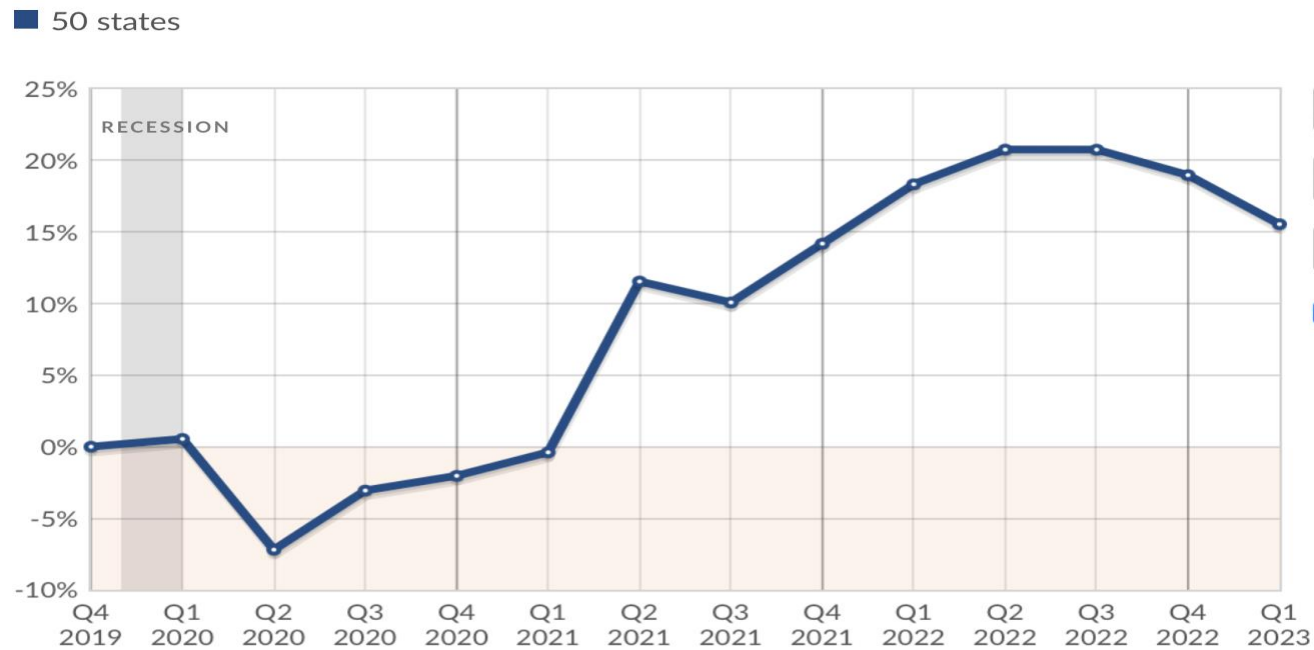
ANDREW YOUNG SCHOOL
OF POLICY STUDIES

- Introduction
- Overview of Pandemic-Era State Tax Relief Measures
- Case Studies: Five Major Types of Pandemic-Era Tax Relief Measures
- Recommendation: Restoring Fiscal Sustainability in the Post-Pandemic Era



- The combination of one-time federal funds and robust tax revenue growth in FY 2021 and 2022 created unanticipated revenue surpluses in many states, putting them in a strong position to enact various tax relief measures

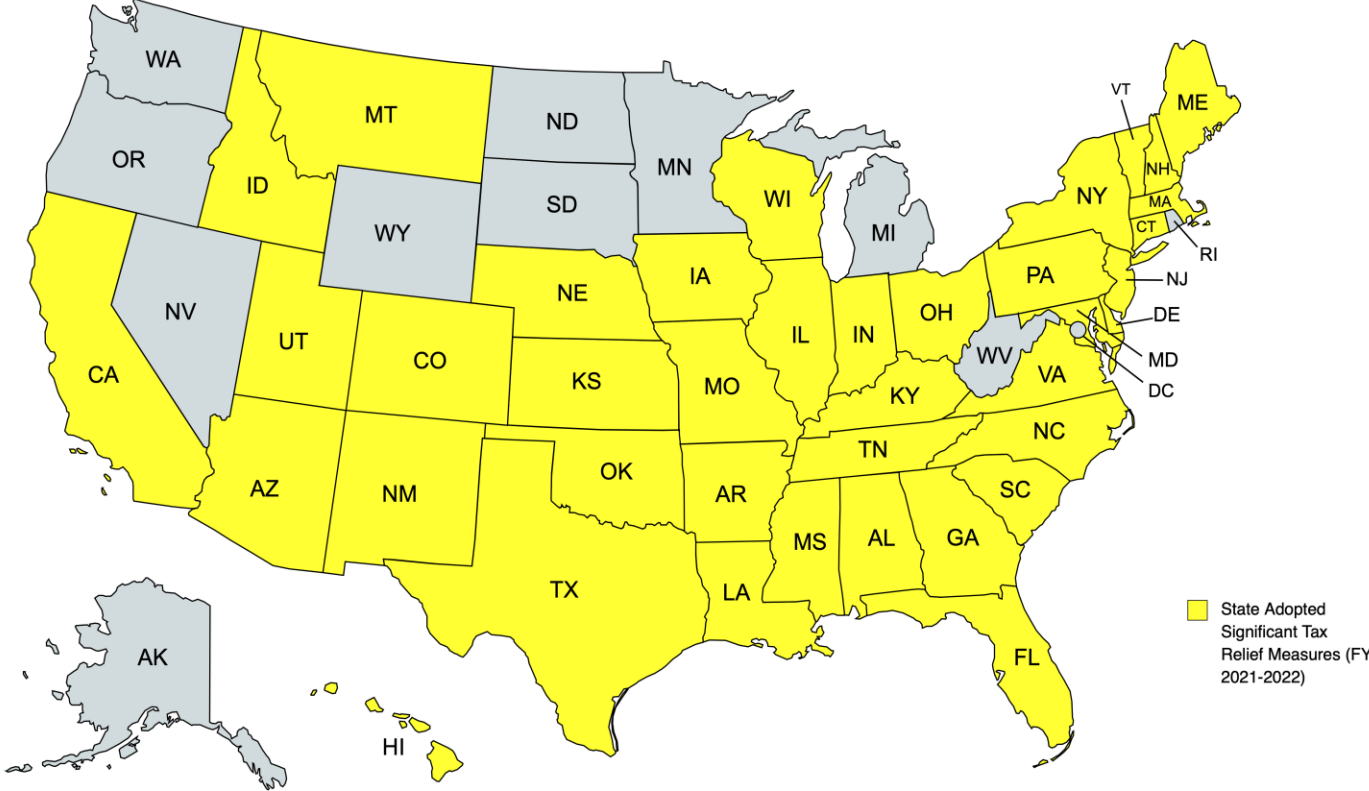
Change in Tax Revenue From Each State's Pre-Pandemic Level



- The first round of tax cuts in FY 2021 predominantly centered on state individual and corporate income taxes
- The second round of tax cuts in FY 2022 were more ambitious and involved a broad mix of policy changes on sales taxes, property taxes, and motor fuels taxes, in addition to state individual and corporate income taxes.

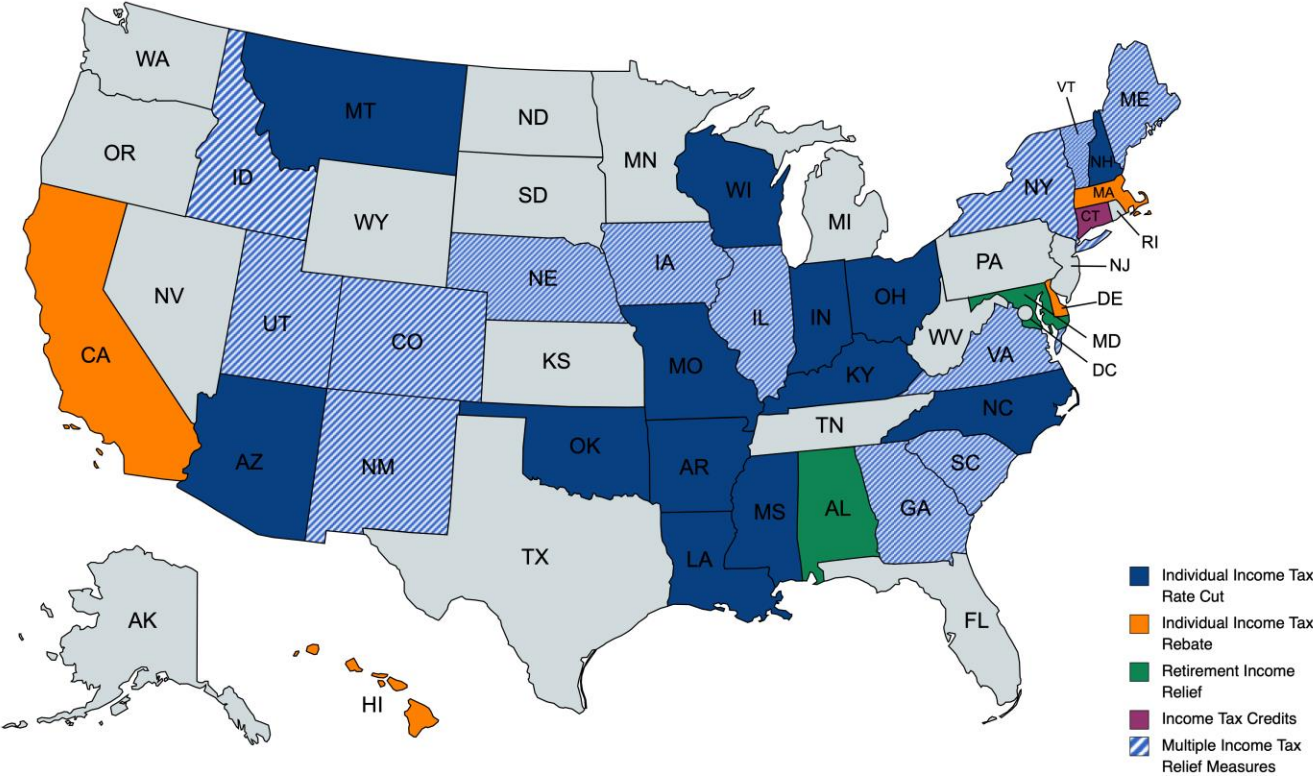
Number of States	Types of Significant Tax Relief Measures	Total Number of Significant Tax Relief Measures
33	Individual Income Tax	54
12	Corporate Income Tax	12
11	Sales Tax	11
8	Gas Tax	8
7	Property Tax	7
Total: 39 States		Total: 92 Measures

Map of State Tax Relief Measures FY 2021-22

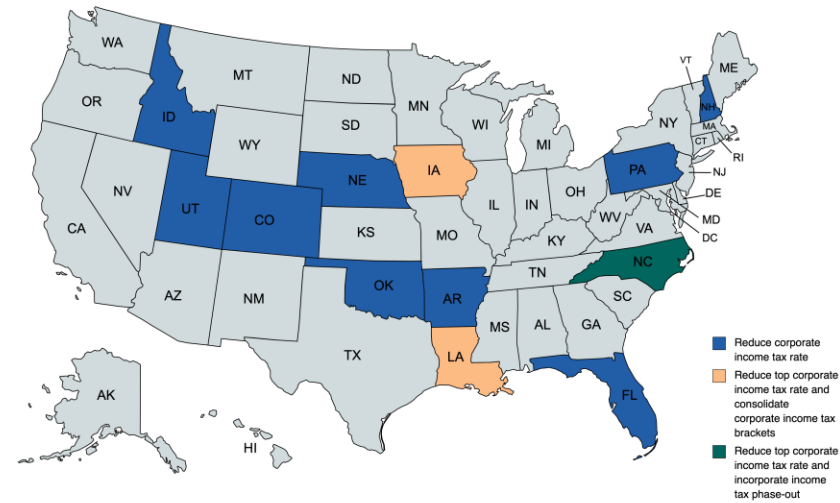


Number of States	Types of Relief Measures	States
21	Individual Income Tax Rate Cut	Arizona, Arkansas, Colorado, Georgia, Idaho, Indiana, Iowa, Kentucky, Louisiana, Mississippi, Missouri, Montana, Nebraska, New Hampshire, New York, North Carolina, Ohio, Oklahoma, South Carolina, Utah, Wisconsin
12	Individual Income Tax Rebate	California, Colorado, Delaware, Georgia, Hawaii, Idaho, Illinois, Massachusetts, Maine, New Mexico, South Carolina, Virginia
10	Retirement Income Relief	Alabama, Connecticut, Georgia, Iowa, Maryland, Nebraska, New Mexico, Utah, Vermont, Virginia
5	Expand or Create Earned Income Tax Credits	Connecticut, Illinois, Maine, New York, Utah
3	Create New Child Tax Credits	Connecticut, New Mexico, Vermont
2	Increase Standard Deductions	Georgia, Virginia

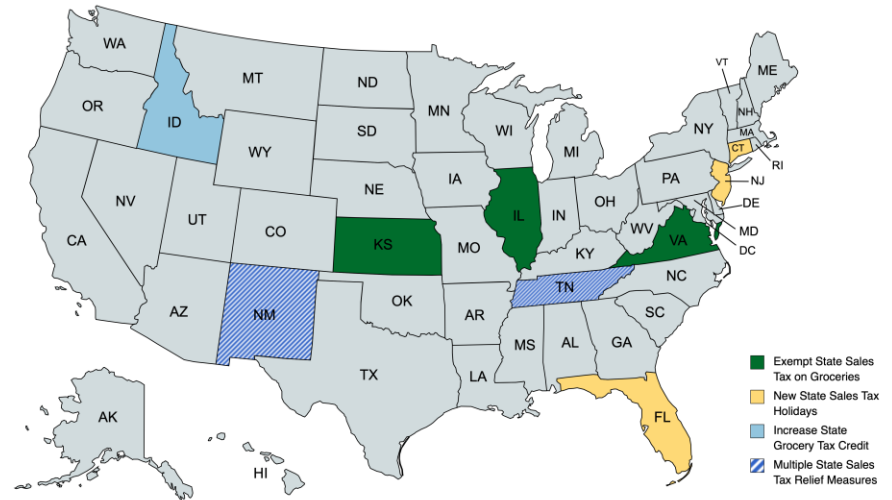
Significant State Individual Income Tax Relief Measures (FY 2021-22)



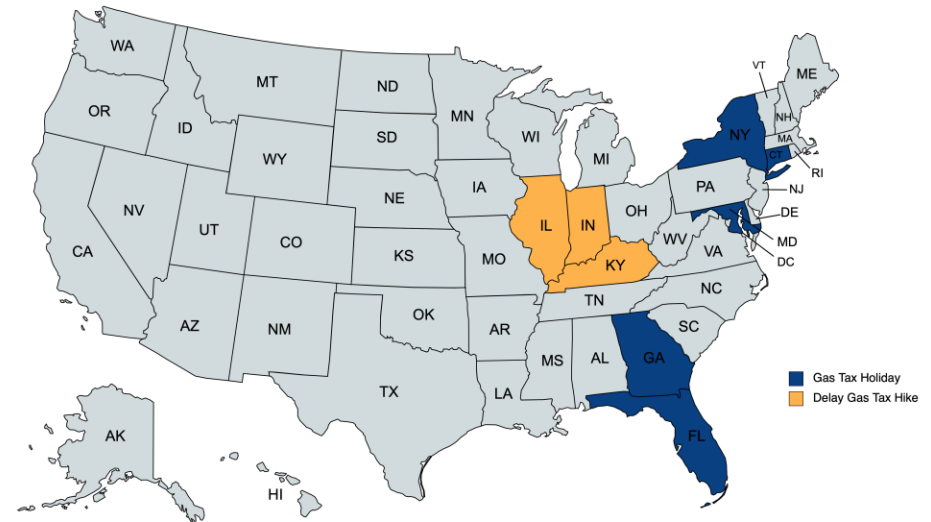
# of States	Types of Relief Measures	States
9	Reduce corporate income tax rate	Arkansas, Florida, Idaho, Nebraska, Oklahoma, New Hampshire, Pennsylvania, Utah, Colorado
2	Reduce top corporate income tax rate and consolidate corporate income tax brackets	Louisiana, Iowa
1	Reduce top corporate income tax rate and incorporate income tax phase-out	North Carolina



# of States	Types of Sales Tax Relief Measures	State
5	New State Sales Tax Holidays	Connecticut, Florida, New Mexico, New Jersey, Tennessee
4	Exempt State Sales Tax on Groceries	Kansas, Virginia, Illinois, Tennessee
1	State Sales Tax Rate Reduction	New Mexico
1	Increase State Grocery Tax Credit	Idaho



# of States	Types of Gas Tax Relief Measures	State
5	Gas Tax Holiday	Connecticut, Florida, Georgia, Maryland, New York
3	Delay Gas Tax Hike	Kentucky, Illinois, Indiana



State Property Tax Relief Measures

# of States	Types of Property Tax Relief Measures	State
4	Property tax rebate credit	Connecticut, Illinois, Nebraska, New York
2	Raise state property tax exemption	Idaho, Texas
1	Reduce property tax assessment rates and taxable valuations	Colorado

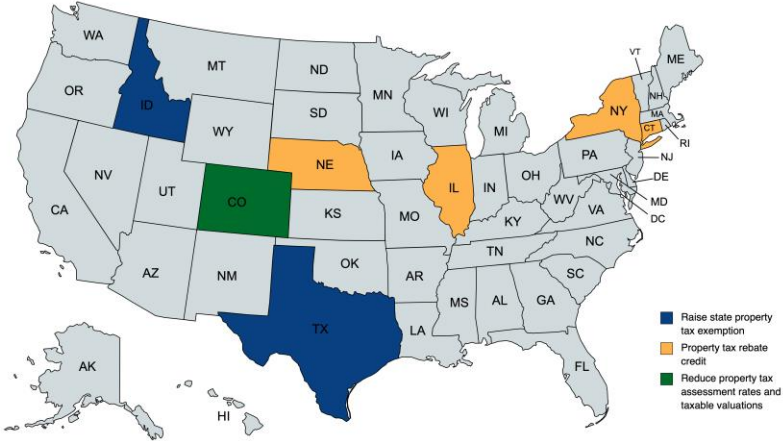


Table 8. Tax Rebate Policies

State	Year	Payment Size	Eligible Taxpayers	Total Value (% GF Exp.) ¹	Funding Source
California	2022	\$200–\$350 per taxpayer or dependent in household	For \$200: Single: <\$250,000 Joint: <\$500,000 For \$250: Single: <\$125,000 Joint: <\$250,000 For \$350: Single: <\$75,000 Joint: <\$150,000	\$9.5 billion (6%)	GF Surplus
Idaho	2022	The greater of 10% of 2020 income OR \$300 for single and \$600 for joint filers	All full-year residents	\$500 million (12%)	GF
	2022	The greater of 12% of 2020 income OR \$75 per taxpayer and dependent	All full-year residents	\$350 million (8% of expenditures)	GF and Tax Relief Fund
Georgia	2022	Single: \$250 Head of household: \$375 Joint: \$500	All residents who filed 2020 and 2021 returns	\$1.6 billion (6%)	
Massachusetts	2022	14.03% of 2021 tax liability	All 2021 taxpayers	\$2.9 billion (9%)	Excess Tax Revenue ²
New Mexico	2022	Single: \$500 Joint: \$1000	All 2021 taxpayers	\$656.7 million (7%)	GF/Tax Stabilization Reserve

Source: Publicly available state budget documents; authors' calculations

¹ Percentage of 2022 Preliminary Actual General Fund Expenditures

² Excess here is defined as “when tax receipts rise significantly faster than salaries and wages do.”

□

Table 9. Individual Income Tax Changes, FY 2022–31

State	Tax Brackets	2022	2023	2024	2025	2026	2031
Iowa	\$0–\$6,000	0.33%–2.25%	4.40%	4.4%	4.4%	3.9%	3.9%
	\$6,001–\$30,000	2.25%–5.96%	4.82%	4.82%	4.82%	3.9%	3.9%
	\$30,001–\$75,000	5.96%–7.44%	5.7%	5.7%	4.82%	3.9%	3.9%
	>\$75,001	7.44%–8.53%	6%	5.7%	4.82%	3.9%	3.9%
Kentucky	All income levels	4.5%	4%	3.5%	3%	2.5%	0% ¹
Mississippi	\$0–\$5,000	0%	0%	0%	0%	0%	0%
	\$5,001–\$10,000	4%	0%	0%	0%	0%	0%
	>\$10,000	5%	5%	4.7%	4.4%	4%	4%
South Carolina	\$0–\$3,200	0%	0%	0%	0%	0%	0%
	\$3,200–\$6,410	3%	3%	3%	3%	3%	3%
	\$6,410–\$9,620	4%	3%	3%	3%	3%	3%
	\$9,620–\$12,820	5%	3%	3%	3%	3%	3%
	\$12,820–\$16,040	6%	3%	3%	3%	3%	3%
	>\$16,040	7%	6.5%	6.4%	6.3%	6.2%	6% ²

Source: Publicly available state budget documents and authors’ calculations; Iowa values are from Tax Foundation

¹ Assuming certain GF receipt criteria are met

² Only 0.1% increases after 2023 are contingent on revenue collection targets.

7

Kansas prioritized reducing tax rates on basic consumption items to help lower-income households. Beginning January 2023, the sales and compensating use tax rate on food and food ingredients was reduced from 6.5 percent to 4 percent. Notably, these changes are part of a mid-term plan to eliminate taxes in this category altogether—Kansas plans to further reduce the rate to 2 percent in January 2024 and abolish it completely the following year.

The estimated cost is approximately \$80 million in FY 2023, \$264 million in FY 2024, \$434 million in FY 2025, and \$534 million in FY 2026.

Illinois also passed a property tax exemption. Under Governor Pritzker's Family Relief Plan, the state issued a one-time, individual property tax rebate to those meeting certain criteria. The plan allows for a rebate up to \$300 for single filers earning up to \$250,000 and for couples up to \$500,000.

Georgia's gas tax, 29.1 cents per gallon, began a tax holiday on March 18, 2022, when the governor signed HB 304 and immediately suspended it through the end of May 2022. Seven extensions were made to reduce the impact of inflation—bringing the gas tax holiday cost to an estimated \$1 billion—which has been funded by the state's \$6.6 billion budget surplus.

- We view **costly and permanent tax cuts, taking effect immediately, as steps closer to a fiscal cliff**—avoidable steps that can negatively impact revenue growth and lead to long-term structural budget challenges, especially when enacted under uncertain economic conditions.
- **State tax cuts in the form of temporary tax rate reductions, temporary tax rebates and holidays, targeted tax exemptions, and expanded tax credits** generally have modest effects on revenues (i.e., short-term revenue losses) and are fiscally sustainable ways of providing pandemic-era tax relief

Implement tax policy changes that are temporary and require reevaluation

Lower-Risk Policy Changes: Illinois

Illinois adopted the Illinois Family Relief Plan in 2022, providing nearly \$1.83 billion in tax policy changes. The plan included one-time individual income and property tax rebates as well as temporary cuts in several sales taxes. For instance, three tax holidays were created, which are temporary by definition: a one-year suspension of the state's 1-percent groceries tax, the delay of the scheduled inflationary increase in the motor fuel tax, and the reduction of sales taxes for qualified clothing/school-related items

Higher-Risk Policy Changes: Wisconsin

Wisconsin passed a series of permanent and expansive tax cuts in state individual income tax during and after the pandemic. In 2022, for example, the state provided tax relief for middle-income taxpayers by cutting the third income tax bracket rate from 6.27 to 5.3 percent for individuals with taxable income between \$24,250 and \$266,930. This permanent rate reduction represents the largest single-year drop in that bracket since the late 1980s and was estimated to lower individual income tax collections by \$1 billion in FY 2022.

Incorporate well-designed revenue trigger mechanisms to make prudent tax measure phase-ins

Lower-Risk Policy Changes: Georgia

Georgia incorporated three triggers that reduce the likelihood of a budget shortfall due to its graduated individual income tax rate reductions. First, the governor's revenue estimate for the succeeding fiscal year must be 3 percent above the revised revenue estimate for the present year. Second, the prior fiscal year's net revenue collection must be higher than each of the preceding five fiscal years of net tax revenue collection. Third, the Revenue Shortfall Reserve must contain a sum that exceeds the amount of the decrease in state revenues projected to occur as a result of the prospective reduction in the tax rates set to occur the following year.

Higher-Risk Policy Changes: Iowa

In June 2021, Iowa adopted a bill that would remove revenue triggers adopted in 2018 as part of a tax reform plan to consolidate its nine individual income tax brackets into four. In the original law, the state would need GF receipts of at least \$8.31 billion and year-over-year GF growth of at least 4 percent in a given year. In FY 2022, the state met the receipts threshold but barely missed its 4-percent growth target, reaching 3.8 percent. With the triggers nearly met, moving forward with the state's tax bracket consolidation is not fiscally imprudent, per se.

Refundable tax credits to provide targeted and more fiscally affordable tax relief measures for those most impacted by the pandemic.

Lower-Risk Policy Changes: Maine

Maine passed a supplemental budget into law in April 2022 that provided several tax relief measures, including refundable tax credits for low- and middle-income property owners and an expansion of the state's Earned Income Tax Credit (EITC) by an average of \$400 per family (costing \$27.6 million). Maine's tax relief measures take a cautious and fiscally responsible approach to state revenues, dedicating nearly 75 percent of the state budget surplus to one-time revenue initiatives

Higher-Risk Policy Changes: Arizona

In 2021, Arizona implemented the largest individual income tax cut in its history. The substantial tax reform streamlined the state's graduated income tax brackets (ranging from 2.59 percent to 4.5 percent) to a single, flat tax rate of 2.5 percent in 2023. These massive, immediate, and untargeted tax reforms are estimated to reduce individual income tax collections by about \$1.9 billion annually when fully phased in—accounting for more than 26 percent of individual income tax revenue collection in FY 2022

Policymakers should consistently account for their fiscal outlook beyond the near future

- Use long-term fiscal planning tools (multi-year forecasts, multi-year fiscal notes, current service baselines, etc.) in budget processes to identify medium- and long-term fiscal challenges (Florida)
- Prepare budget stress tests to anticipate and craft prudent fiscal responses to potential economic downturns (Utah)

Thank You!
Your comments and suggestions are much appreciated!





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October 26, 2023

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