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COVID-19 and County Sales Tax Revenues

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INTRODUCTION

The spread of the novel coronavirus and the COVID-19 disease has wide ranging health and economic implications for Wisconsin families, businesses, and governments. One of the great difficulties in assessing the magnitude of these challenges is that the landscape seems to be changing daily.

We know with certainty that the spread of this virus will impact the health of many state residents. The pandemic will test our hospitals, our health systems, and our health care workers.

The reaction of the federal government, Wisconsin state government, county and municipal governments, and businesses has been to implement policies to limit the spread of the virus. Among the government policies enacted are:

- bans or restrictions on international travel;
- the closing of bars and restaurants except for carryout or delivery;
- the closing of schools; and
- the closing of "non-essential" businesses and a "safer at home" order lasting until at least April 24th.

Many employers have allowed or required employees to work from home rather than at their usual place of work. In some businesses that have temporarily closed, employees have been laid off or furloughed.

These policies will have major economic impacts in the short term and possibly long term. Federal, state, and local governments are weighing the economic costs of shuttering many businesses and restricting social interaction against the costs of this pandemic getting out of control.

We know in general terms what this means economically. In an international economy, business supply chains are interrupted leading to reduced production. Limitations on bars and restaurants, and the closing of non-essential businesses mean unemployment spikes and financial hardship for both workers and business owners. Consumer spending has declined and will remain at lower levels for at least the next several months.

For economists, forecasting the effects of this interruption is challenging, particularly since the duration of these policies remains uncertain. This memo attempts to provide an early look at one aspect of the COVID-19 pandemic and resulting economic contraction: the impact on county revenues via declines in sales tax collections.

COUNTY SALES TAX REVENUES

Sales taxes are one of many sources of county revenue. The primary revenue sources for counties are the property tax and state aid. Combined, these two sources account for about two-thirds of total county revenue. For the remainder of this year, neither of these revenues should be affected. About 13% of revenues come from a variety of fees and fines. If the COVID-19 crisis affects these, the impact is likely to be small.

The revenue source that will be most impacted in both the short and long term is the sales tax. As of April 1, when Menominee County's tax begins, 68 counties will be imposing the optional 0.5% sales tax. Those that do not impose a local sales tax are Manitowoc, Racine, Waukesha, and Winnebago counties. Outagamie County's tax began January 1, 2020.

For counties with the sales tax, collections averaged about 9% of total revenues in 2018 (the most recent available data). Some counties rely on the tax much more than others. For example, the sales tax accounted for nearly 15% of revenues in Ozaukee County but less than 3% in Florence County.

Last fall to assist county officials in their budget deliberations, *Forward Analytics* provided counties with sales tax estimates for 2020. Due to the severe short-term economic impacts of the pandemic and the policies it has spawned, actual revenues will be less than anticipated. This memo provides initial estimates of the revenue loss due to COVID-19 under two scenarios:

1) A short-term economic interruption; and

2) A deeper, more protracted recession.

<u>Caution</u>: Even the best economic forecasters are uncertain of the magnitude of the impact this crisis will have on the economy and whether that impact will be short-lived or will extend out over a relatively long period. The numbers in this memo should be used with caution. They are indicative of what might be expected should the specified scenarios play out.

SCENARIOS

While the impact of the COVID-19 pandemic will be felt across all industries, dining establishments, hotels and motels, and other tourism related industries will be especially hard hit. For example, the American Hotel & Lodging Association recently projected that 40% of hotel jobs could be lost over the next several months. Those projections were made before Governor Evers' "safer at home" order, so the percentages will likely be higher.

Given the Governor's order, sales tax revenues from hotels and motels will dry up during the end of March through the end of April. While bars and restaurants still can provide carryout, the ban on "in-store" service means revenues from these establishments will drop significantly at least through the end of April. Vehicle sales will be essentially nonexistent during this period. Retail sales will also decline.

What occurs after the "safer at home" order is lifted is uncertain and depends on whether the restrictions on restaurants and bars continue. The best available evidence indicates that social distancing will be required at least through May and possibly through June, meaning the food service restrictions will likely remain at least through the end of May.

The economic impact through the rest of the year depends on the ability to restart the economy after the abrupt shutdown. It will depend partly on the number of businesses that do not make it through this difficult time.

Short-term interruption

The most optimistic scenario involves a short-term economic interruption lasting about three months, with economic activity gradually approaching "normal" over the ensuing six months. Given the "safer at home" order, which lasts through April 24, the largest impacts are felt during the month of April. Given how the county sales tax is collected and distributed, an April interruption is felt mostly in May payments to counties.

Under this scenario, sales in hotels and motels are projected to be 95% below normal in April, 60% below normal in May, and 40% below normal in June. Sales in restaurants and bars fall by 70% in April and May (as social distancing recommendations remain in place), and 30% from normal June levels. Retail sales decline 20% in April and May, and 10% in June. Other taxable sales decline 20% in April and 10% in May and June.

In the second half of the year, sales in each of these industries gradually return to pre-pandemic levels.

Under those conditions, county sales tax revenue during 2020 are estimated to be 8.0% ($37 million) below projected levels. The largest percentage declines are in Sauk (11.8%), Door (11.6%), Sawyer (10.1%), and Vilas (10.0%), counties (see attached table).

Protracted Recession

The more severe scenario is somewhat similar to a Congressional Budget Office pandemic estimate from 2006 and recent estimates from the New York State Association of Counties. Under this scenario, the "safer at home" order is extended for a second month. Thus, sales in hotels and motels are 95% below normal in both April and in May, and 70% in June. Sales in restaurants and bars fall by 70% in April and May, and 40% in June. Retail sales decline by 40% in April and May, and 30% in June. Other taxable sales decline 20% in April and 10% in May and June.

Under these assumptions, 2020 collections are 12% below expected levels, a decline of $55.6 million.

COUNTY EXPERIENCE

The attached table shows sales tax estimates by county. The first column contains 2020 sales tax estimates created in the fall of 2019. The next two columns show estimated declines in percentage and dollar terms based on the milder scenario. The last two columns show the same information under the more severe scenario.

Because prior year sales tax data are not available for Outagamie and Menominee counties, estimates could not be created for those counties.

These figures will be updated as more information becomes available in terms of actual collections and economic forecasts of the impact of COVID-19.