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TO: Members
Wisconsin Legislature

FROM: Bob Lang, Director

SUBJECT: June, 2020, General Fund Tax Collections

This memorandum provides information regarding: (a) general fund tax collections for the month of June, 2020; (b) continuing unemployment insurance claims through the week ending June 27, 2020; and (c) factors affecting the 2019-20 general fund balance.

On January 23, 2020, this office distributed projections of general fund revenues for the 2019-21 biennium. That report, when adjusted for tax law changes enacted under the federal CARES Act and 2019 Wisconsin Acts 181 and 185, estimated that tax collections for 2019-20 would increase by 1.75% ($303 million) over 2018-19 collections and that 2020-21 taxes would increase by 2.0% ($354 million) over the 2019-20 estimate.

Actual tax collections for the first nine months of the 2019-20 fiscal year (through March, 2020) increased by 5.1% over the same period for 2018-19. Although this growth was higher than the projected 1.75%, collections were on target with the estimates as the impact of the individual income tax rate reductions of 2019 Acts 9 and 10 would be realized in the remaining months of the 2019-20 fiscal year.

The contraction following the coronavirus pandemic resulted in the largest month-over-month increase in seasonally adjusted unemployment since the data series began in 1976. The seasonally adjusted unemployment rate in Wisconsin for April, 2020, was 14.1%, which was 11 percentage points higher than the March rate of 3.1%. The increase in the number of unemployed individuals was expected to result in diminished taxable salaries and wages, lower state sales and use tax collections reflecting limited ability for consumers to purchase taxable goods and services, and lower corporate income/franchise taxes due to reduced corporate profits.

Preliminary General Fund Tax Collections, June, 2020

Preliminary information on taxes collected by DOR for the month of June, 2020, is now available. The coronavirus pandemic and its impact on employment and the state's economy continues to manifest in a reduction in tax collections. In addition, estimated payments for income and franchise taxes have been extended from June to July 15 in 2020, which has affected June collections. Preliminary tax collections for June, 2020, were $1,340 million, which is $370 million below collections of June, 2019.

The decline in June, 2020, collections is primarily attributable to two income tax components, which account for 96% of the reduction in collections compared to June, 2019. Reduced estimated payments for income and franchise taxes account for $252 million in lower tax revenue, reflecting the effects of the delayed filing date and the impacts the coronavirus pandemic has had on the economy. Withholding tax payments account for $104 million of the revenue reduction, which reflects the severe decline in employment in the state.

The preliminary collection report for June reflects a continued decline over the previous three months. In April, 2020, collections were $870 million below April, 2019, collections. The reduction in April collections was also impacted by the delayed filing date, as April 2020 estimated payments and final income and franchise tax payments for tax year 2019 were similarly delayed to July 15. In May, 2020, collections were $66 million below those for the same month in 2019. Over the three-month period for April, May, and June of 2020, collections are $1,306 million below the comparable three-month period for 2018-19.

For the 12 months of the 2019-20 fiscal year, collections are $749 million, or 4.7%, below those over the same 12 months of 2018-19. Reduced collections for the 12 months have been affected by the extension of income and franchise tax filing deadlines from April and June to July 15 in 2020. It is important to note, however, that income and franchise tax returns and estimated payments filed by July 15 will accrue to state fiscal year 2019-20 under the state's budgetary cash and modified accrual method of accounting. In describing the state's statutory basis of accounting, the state's annual fiscal reports indicate that: "The state's centralized accounting records remain open until July 31 (August 15 for income and sales and use tax receipts) to permit the state departments to record revenues and expenditures applicable to the fiscal year ended June 30." As a result, preliminary final collections for 2019-20 will not be known before late August.

Individual Income Tax. Preliminary individual income tax collections for June, 2020, are $246 million (27.2%) lower than those collected in June, 2019. Year-to-date, individual income tax collections for 2019-20 are $936 million, or 11.0%, lower than the comparable period in 2018-19. Most of the decline in tax collections year-to-date is likely caused by the delayed filing dates for estimated payments and final payments. It is assumed that many individuals have taken advantage of the filing date extension and will wait to make payments closer to the July filing date, which helps explain the precipitous decline in June collections relative to the prior June. Taxpayers who make quarterly estimated payments are typically required to make one such payment on or before June 15 of each year.

Estimated payments and final payments that were otherwise owed in April and June are now due on July 15. Estimated payments year-to-date total $802 million, which are $588 million lower than the comparable period in 2018-19. Individual final payments year-to-date are $409 million, or $281 million lower than the same period a year ago. These reductions partly reflect lower tax payments related to the income tax rate reductions for tax year 2019 enacted under 2019 Acts 9 and 10, but are also skewed by the delayed filing date for individuals. Final payments and refunds for tax year 2019, and April and June estimated payments for tax year 2020, will not be known until after the July 15 filing date.

Preliminary withholding tax collections for June, 2020, were $104 million (15.1%) lower than the same month in the previous year. Although withholding tax collection patterns can be relatively volatile month-to-month, the observed monthly decrease in June withholding relative to the prior June is generally consistent with estimated declines in wages and salaries at the national level.

Year-to-date, withholding collections are higher by $146 million (1.9%) compared to the same 12-month period in 2018-19. This office's June memorandum noted the increased hiring and greater hourly pay enacted by some large retailers during the pandemic, as well as the decline in continuing claims for unemployment benefits since April 18 (a trend which continues). Both of these factors likely contributed to withholding collections being stronger than expected in prior months (adjusted collections grew by 8.4% in May, 2020, relative to the prior May), offsetting a further decline in withholding year-to-date.

Corporate Income/Franchise Tax. Preliminary corporate income/franchise tax collections for June, 2020, are $131 million, which is $108 million less than collected in June of last year, or a decrease of 45%. Similar to individual estimated payments, although some of this reduction is due to a decline in the economy, most corporations have likely taken advantage of the filing date extension and will wait to make payments until July 15. Thus, whether economic decline from the coronavirus pandemic has reduced corporate estimated payments, and if so, to what extent, will not be known until after the July filing date.

Year-to-date collections through June, 2020, are $1,425 million, which is $101 million (7.6%) more than the comparable 12-month period last year. Corporate collections year-to-date are lower than the 12.3% growth rate previously estimated. However, as discussed, additional payments are expected in July due to the filing extension. Thus, it remains reasonable to expect that total collections for the current year will meet, if not exceed, the estimated amount.

Unanticipated tax payments have offset the anticipated economic decline, and associated decrease in tax collections, in 2019-20. A significant amount of corporate income/franchise tax collections accrued to the state in the form of one-time audit payments and increased collections from partnerships under the 2017 Act 368 entity-level tax. According to DOR, several large audit payments were made to the state in the five months following the January estimates such that audit payments in 2019-20 are $191 million higher compared to 2018-19.

Sales and Use Taxes. Preliminary state sales and use tax collections in June generally reflect taxes paid for retail sales occurring in May. The coronavirus pandemic resulted in the Safer-at-Home order, which took effect on March 26, 2020, and remained in effect until May 13, 2020. Sales tax collections for June, 2020, reflected approximately half a month of increased economic activity due to the expiration of the Safer-at-Home order. While June, 2020, sales tax collections were lower than June collections in the previous year by $9 million, or 1.7%, such collections have improved relative to comparable year-over-year sales tax collections in May (10.1% decline) and April (9.9% decline). Sales tax collections through June, 2020, are $91 million above collections in the comparable 12-month period in 2018-19, representing 1.8% growth year-to-date.

Based on preliminary sales tax data provided by DOR, the economic impact of the coronavirus pandemic and the Safer-at-Home order continued to impact retail industries differently. Taxable retail sales were lower in May of 2020 compared to May in the prior year by 52% for clothing and clothing accessories stores and 38% for food services and drinking establishments. Conversely, May taxable sales in 2020 were higher at nonstore retailers (including remote sellers and marketplace providers) by 110%, building material and garden equipment and supplies stores by 22%, and food and beverage stores by 12%. In contrast to declines of 27% in March and 28% in April of 2020, taxable sales for motor vehicle and parts dealers were higher by 3% in May.

Several factors may have contributed to improved sales tax collections in June, 2020, compared to the previous two months. Taxable sales during May, 2020, represented the end of the Safer-at-Home order, which likely helped increase taxable sales as businesses began to gradually open back up with limited operations, allowing consumers to make purchases that were otherwise postponed. Additional federal transfer payments in the form of federal stimulus checks and the payment of temporary enhanced federal unemployment benefits over the latter half of April and May helped offset reduced consumer purchasing power from reduced wages and salaries. Further, Wisconsin employment in May increased by 74,900 relative to April, which may have improved consumer confidence. Despite these factors, sales tax collections for June were still lower than comparable collections in 2019.

Under 2019 Act 10, individual income tax rates will be reduced to offset the increased sales and use tax collections attributable to remote sellers and marketplace providers. For tax year 2020 and taxable years thereafter, the tax rate reduction is based on the sales and use tax collected from remote sellers and marketplace providers during the 12-month period from October 1, 2019, to September 30, 2020. To the extent that the coronavirus pandemic results in increased taxable sales made by remote sellers and marketplace providers that would have otherwise been in-person taxable sales at physical stores located in Wisconsin, the sales tax revenue used to offset individual income tax rate reductions for tax year 2020 will have a larger fiscal effect than the $119 million income tax reduction estimated under Act 10.

Unemployment Claims

Continuing unemployment insurance (UI) claims measure the number of persons receiving unemployment benefits. Economists tend to view continuing claims as a better gauge of labor market health than initial claims, which can overstate unemployment. Continuing claims account for the number of people that leave the UI system each week because they return to work, exhaust their benefits, or become otherwise ineligible. Additionally, some initial claims get denied, while others are held in a pending status due to processing delays, both of which could lead to discrepancies between the two sets of claims data.

Continuing claims for regular UI in Wisconsin were 321,063 during the week ending April 18, which represents the highest weekly level following the coronavirus outbreak. Since that time, the level of continuing claims has declined every week to 219,797 claims filed for the week ending June 27 (reported on July 9), representing a 32% decline since the April peak. The decline in continuing claims, in part, indicates that claimants were beginning their return to work in late April and continued their return through May and June.

2019-20 General Fund Balance

The January 23, 2020, report, adjusted for tax law changes enacted under the federal CARES Act and 2019 Wisconsin Acts 181 and 185, estimated that the gross balance in the state's general fund on June 30, 2020, would be $1,093 million. That balance will undoubtedly decrease because of reduced tax collections as shown in this report. The extent of the effect of that collection information will not be known until after the July 15 filing deadline for income and franchise taxes. There are, however, some items that will likely mitigate the decline in the 2019-20 balance.

1. It is unlikely that the entire $189 million transfer to the budget stabilization fund from the general fund identified in the January 23 report will occur.

2. The Department of Administration has required certain state agencies to lapse or transfer $70 million from 2019-20 appropriations to the general fund.

3. The administration re-amortized variable rate debt that otherwise would have been paid off in fiscal year 2019-20, and instead scheduled it for repayment over a five-year period starting in the 2021-22 fiscal year. This variable rate debt re-amortization reduced GPR debt service payments by an estimated $66 million in 2019-20.

4. The budget stabilization fund currently has a balance of $655.8 million. Legislation is required in order to access any amounts in the stabilization fund.

This office will continue to monitor tax collection reports, economic forecasts, and federal legislation and inform you of findings that might impact the state's budget. We have provided monthly reports on tax collections for the months of April, May, and June. Our next report will likely be at the end of August when preliminary actual tax collections that accrue to the 2019-20 fiscal year are available.

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