Legislative Fiscal Bureau

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State of Wisconsin

May 15, 2023

Senator Howard Marklein, Senate Chair
Representative Mark Born, Assembly Chair
Joint Committee on Finance
State Capitol
Madison, WI 53702

Dear Senator Marklein and Representative Born:

On January 25, 2023, this office distributed its estimates of general fund revenues and expenditures for the 2022-23 fiscal year and tax collection projections for each year of the next biennium. Recently, tax collection data for April, 2023, became available and S&P Global released its May, 2023, forecast of the national economy.

Based upon our review of the collections data and the new economic forecast, we believe that tax collections will be lower than the January 25 report by $365.2 million in 2022-23, $148.0 million in 2023-24, and $241.9 million in 2024-25. The three-year reduction is $755.1 million, or -1.16%.

2022-23

Although general fund tax collections are estimated to be $365.2 million below the previous projection, that amount is offset by anticipated expenditure reductions of $141.7 million above those of our January report. The $141.7 million consists of a reduction in debt service payments ($8.5 million), a lapse from the appropriation of the State Public Defender ($9.7 million), and an increased lapse of $123.5 million in the GPR appropriation for the Medical Assistance (MA) program.

The net result of these estimates is that the projected gross balance in the general fund for 2022-23 will be $6,877.0 million, which is $223.5 million lower than the January projection of $7,100.5 million.

The total estimated GPR lapse in MA is projected at $898.3 million. Of this amount, $774.8 million was included in the January report. Most of the MA budget surplus that has accumulated during the biennium is attributable to an enhanced federal matching rate that has been in effect longer than was anticipated at the time of the Legislature's deliberations on the 2021-23 budget. The increase in this lapse from the prior estimate is primarily due to an increase in revenues available for

MA expenditures in the medical assistance trust fund, and higher collections of drug manufacturer rebate revenue, which are used to offset program expenditures.

The general fund condition statement for 2022-23, which incorporates the information of this report, is shown in Table 1.

TABLE 1

Estimated 2022-23 General Fund Condition Statement

	2022-23
Revenues	
Opening Balance, July 1	$4,298,919,000
Taxes	20,988,100,000
Departmental Revenues	
Tribal Gaming	0
Other	712,036,300
Total Available	$25,999,055,300
Appropriations, Transfers, and Reserves	
Gross Appropriations	$19,731,372,000
Sum Sufficient Reestimates	36,759,800
Transfers to:	
Transportation Fund	97,289,300
MA Trust Fund	527,783,700
UI Trust Fund	60,000,000
Compensation Reserves	105,951,600
Less Lapses	-1,437,059,700
Net Appropriations	$19,122,096,700
Balances	
Gross Balance	$6,876,958,600
Less Required Statutory Balance	-95,000,000
Net Balance, June 30	$6,781,958,600

General Fund Tax Collections

S&P Global's May, 2023, economic forecast projects stronger economic growth in nominal terms than the January forecast, which was used in preparing the earlier tax revenue estimates. Personal income, personal consumption expenditures (PCE), employment, nominal gross domestic product (GDP), and economic profits are expected to improve in 2023 through 2025, compared to the January forecast. Inflation expectations, as measured by the consumer price index (CPI), have increased over the three-year period relative to January, resulting in limited change to real GDP under the May forecast. The January forecast had anticipated a mild recession in the first and second quarter of 2023, whereas the May forecast no longer anticipates a recession in 2023. In general, the higher forecast is primarily driven by higher estimates for 2023 than previously estimated, with lower growth rates in 2024 and 2025 relative to the January forecast. Table 2 outlines the May, 2023, economic forecast by S&P Global.

TABLE 2

Summary of National Economic Indicators
IHS Markit Baseline Forecast May, 2023
($ in Billions)

	2022	2023	2024	2025
Nominal Gross Domestic Product	$25,462.7	$26,806.3	$27,792.1	$28,862.3
Percent Change	9.2%	5.3%	3.7%	3.9%
Real Gross Domestic Product	$20,014.1	$20,251.3	$20,439.6	$20,765.4
Percent Change	2.1%	1.2%	0.9%	1.6%
Consumer Prices (Percent Change)	8.0%	4.2%	2.5%	2.2%
Personal Income	$21,809.0	$23,017.0	$23,954.3	$24,921.3
Percent Change	2.4%	5.5%	4.1%	4.0%
Nominal Personal Consumption Expenditures	$17,357.2	$18,316.2	$18,903.7	$19,608.5
Percent Change	9.1%	5.5%	3.2%	3.7%
Economic Profits	$2,952.6	$3,053.1	$2,986.0	$3,011.0
Percent Change	6.6%	3.4%	-2.2%	0.8%
Unemployment Rate	3.6%	3.6%	4.3%	4.8%
Total Nonfarm Payrolls (Millions)	152.6	155.7	155.6	155.4
Percent Change	4.3%	2.0%	-0.1%	-0.1%
Light Vehicle Sales (Millions of Units)	13.79	14.86	15.70	16.52
Percent Change	-7.7%	7.8%	5.6%	5.2%
Sales of New and Existing Homes (Millions of Units)	5.721	4.832	4.687	5.101
Percent Change	-17.1%	-15.5%	-3.0%	8.8%
Housing Starts (Millions of Units)	1.554	1.338	1.320	1.409
Percent Change	-3.2%	-13.9%	-1.3%	6.8%

The May forecast is based on the following key assumptions. First, the Public Health Emergency (PHE) ends on May 11 (one month earlier than anticipated in the January forecast). Second, the federal debt ceiling is raised in time to avoid a default, a federal budget is passed in time to avoid a federal government shutdown in October, and all federal legislation enacted to date is incorporated into the forecast. The May forecast incorporates the economic impact of the Consolidated Appropriations Act of 2023 (not included in the January forecast), does not include President Biden's plan to cancel a portion of student loan debt, and assumes student loan forbearance expires on July 1. Third, state and local governments experience a limited contraction in spending, with lower tax receipts offset by: (a) federal pandemic relief monies provided under the Infrastructure Investment and Jobs Act; and (b) declining Medicaid benefits, once enhanced eligibility expires with the PHE. Fourth, the Federal Reserve is expected to raise its policy rate to a range of 5% to 5.25% (25 basis points higher than assumed in January) and allow its balance sheet to decline by about one third through 2024. Fifth, the forecast assumes that the current tariffs between the U.S. and China remain in effect. Sixth, growth of real, trade-weighted foreign GDP slows from 3.3% in 2022 to 1.9% in 2023 (higher compared to January), and foreign measures of inflation are expected to recede from 5.9% in 2022 to 2.8% in 2023 (slightly higher compared to January). Finally, the price of Brent crude is expected to decline from $101 per barrel in 2022 to $84 per barrel in 2024 (slightly lower than anticipated in January).

However, the improved forecast for nominal economic growth is more than offset by weaker than expected collections to date. Since this office distributed its estimates of general fund tax collections on January 25, 2023, withholding taxes under the individual income tax, estimated payments and refunds under the corporate income/franchise tax, and cigarette taxes have been the largest contributors to weaker than anticipated growth over the past four months.

Table 3 shows the revised general fund tax collection estimates for 2022-23 and the two years of the next biennium. It should be noted that these revenue estimates reflect current state and federal law, and do not incorporate any of the tax law changes proposed by the Governor in his 2023-25 budget recommendations.

TABLE 3

Projected General Fund Tax Collections
Under Current Law
($ in Millions)

	2021-23 Biennium		2023-25 Biennium	
	2021-22 Actual	2022-23 Estimated	2023-24 Estimated	2024-25 Estimated
Individual Income	$9,214.4	$9,450.0	$9,710.0	$10,160.0
General Sales and Use	6,978.3	7,480.0	7,655.0	7,835.0
Corporate Income/Franchise	2,960.0	2,715.0	2,720.0	2,840.0
Public Utility	383.6	391.0	374.0	370.0
Excise				
Cigarette	482.4	437.0	420.0	407.0
Tobacco Products	94.4	90.0	91.0	93.0
Vapor Products	4.1	7.0	7.7	8.5
Liquor and Wine	64.9	68.0	69.0	71.0
Beer	8.9	8.1	8.1	8.0
Insurance Company	221.8	227.0	236.0	246.0
Miscellaneous Taxes	135.6	115.0	103.0	111.0
Total	$20,548.4	$20,988.1	$21,393.8	$22,149.5
Change from Prior Year		$439.7	$405.7	$755.7
Percent Change		2.1%	1.9%	3.5%

Based on our review of collections data and the economic forecast, general fund taxes will be lower than previous estimates by $365.2 million in 2022-23, $148.0 million in 2023-24, and $241.9 million in 2024-25. The three-year decrease is $755.1 million, or 1.16%, primarily reflecting a lower forecast for the corporate income/franchise tax ($455 million), the individual income tax ($360.0 million), and the cigarette tax ($53 million). Estimated revenues from the tobacco products tax, utility tax, insurance tax, and beer tax have also been reduced ($17.7 million). These reductions are partly offset by an increased forecast over the three year period for the general sales and use tax ($110 million), miscellaneous taxes ($16 million), and the vapor products tax ($4.6 million). The estimate for the liquor tax has not been changed.

Individual Income Tax. Total individual income tax collections are estimated at $9,450 million in 2022-23, which represents a decline of 1.7% relative to the January estimate. Growth in year-to-date adjusted withholding collections through April, 2023, relative to the same time period a year prior (-5.9%), is significantly lower than forecast in January. Year-to-date through April, final payments made by taxpayers for tax year 2022, and tax amounts withheld from nonresident members of pass-through entities, are both considerably lower than the forecasted level in January. However, adjusted withholding collections (not including pass-through withholding) are expected to grow by 7.2% over the rest of the year, buoyed by strong near-term projections for wages and salaries.

The January forecast included an assumption that capital gains realizations would decline significantly in tax year 2022 relative to tax year 2021. It appears that this trend has impacted 2022-23 estimated payments as anticipated, which are 16.8% lower through April than the same period in 2021-22. As in January, these estimates assume capital gains realizations will decline further in tax year 2023, and begin to rebound in tax year 2024.

Total individual income tax collections are projected to grow by 5.2% for the remainder of 2022-23 relative to the same time period in 2021-22, driven primarily by expected increases in withholding collections, and a significant decline in total refunds paid to taxpayers. The decline in 2022-23 refunds is partially attributable to the withholding table update that took effect on January 1, 2022, which incorporated several individual income tax reductions enacted since 2014 (the last time the tables were updated). The resulting lower withholding throughout tax year 2022 translates to lower refunds in 2022-23, all else equal.

In 2023-24, total individual income tax revenues are estimated to increase to $9,710 million, representing annual growth of 2.8%. Most of the annual revenue increase in 2023-24 is attributable to projected growth in wages and salaries, which would increase withholding collections. Estimated revenue growth is partly offset by lower projections for estimated payments, associated with year-over-year declines in capital gains realizations predicted for tax year 2023. In 2024-25, total revenues are projected to increase to $10,160 million, constituting annual growth of 4.6%. Continued steady growth in withholding and an anticipated rebound in tax year 2024 capital gains realizations (which would strengthen estimated payments) are two primary factors contributing to higher revenue growth in 2024-25.

General Sales and Use Tax. State sales and use tax revenues are estimated at $7,480 million in 2022-23, which represents growth of 7.2% over the prior year. Sales tax revenues are estimated at $7,655 million in 2023-24 and $7,835 million in 2024-25, reflecting growth of 2.3% and 2.4%, respectively. The estimates have been increased by $55 million in 2023-24 and 2024-25, relative to the January estimates.

The May forecast for taxable PCE in 2023-24 is 0.8 percentage points higher than in the January forecast, which has contributed to the increase in estimated sales tax revenues for fiscal year 2023-24, relative to January. While the projected growth in taxable PCE in the May forecast for 2024-25 exhibits a similar trend to the January forecast, estimated revenues in that year have been increased based on the higher estimated amount in the preceding year.

Corporate Income/Franchise Tax. Corporate income/franchise tax revenues are now projected to be $2,715 million in 2022-23, $2,720 million in 2023-24, and $2,840 million in 2024-25, which reflects reduced annual collections of 8.3% in 2022-23 and annual growth of 0.2% in 2023-24 and 4.4% in 2024-25. Compared to the previous estimates, the reestimates represent decreased revenues of $195 million in 2022-23 and $130 million in 2023-24 and 2024-25 (-$455 million total).

Collections year-to-date have decreased 6.5% due to: (a) weak March and April estimated payments (-12.5% combined) that are $80 million lower than last year; and (b) refunds that have remained elevated and are $133 million higher relative to last year (70.5%). It is expected that estimated payments and refunds will exhibit continued weakness over the remainder of the year, but improve after the Fall relative to the prior year. Further, the short term growth outlook remains muted, with economic profits forecast to decline slightly by 0.6% in 2023-24 and 0.9% in 2024-25 (an increase relative to the January forecast of -2.0% and -0.6%, respectively), and before-tax book profits forecast to show modest growth of 2.9% in 2023-24 and 0.5% in 2024-25 (a change relative to the January forecast of 0.8% and -0.7%, respectively).

Public Utility Taxes. Public utility tax revenues are estimated at $391 million in 2022-23, $374 million in 2023-24, and $370 million in 2024-25. These estimates have been increased $2 million in 2023-24 and decreased $7 million in 2024-25, relative to the January forecast. The decline in 2024-25 is largely explained by a decline in the anticipated 2024 statewide net property tax rate that is imposed on ad valorem utility taxpayers. This decline is slightly offset by an improved forecast of electricity sales, which positively impacts tax revenues from gross revenues utilities providing such services (private and municipal light, heat, and power companies and electric cooperatives).

Excise Taxes. Excise tax revenues are estimated at $610.1 million in 2022-23, $595.8 million in 2023-24, and $587.5 million in 2024-25, which represents a decline of 6.8% in 2022-23, 2.3% in 2023-24, and 1.4% in 2024-25. These estimates are lower than the previous estimates by $15.2 million in 2022-23, $21.0 million in 2023-24, and $21.9 million in 2024-25.

The majority of the excise tax decline is due to a downward revision in the cigarette tax forecast, with revenues now estimated at $437 million in 2022-23, $420 million in 2023-24, and $407 million in 2024-25. These estimates represent a decline of 9.4% in 2022-23, 3.9% in 2023-24, and 3.1% in 2024-25. When cigarette tax revenues were estimated in January, it was assumed that cigarette tax revenues would continue to decline, but at a slower pace than had been seen year-to-date (-8.0%). However, cigarette tax collections are now down 9.5% year-to-date. This reestimate reflects the ongoing trend of larger declines in cigarette consumption. Weaker than expected tobacco and beer tax collections since January further contributed to the downward revision in excise tax revenues, but were partly offset by an upward revision in vapor.

Insurance Premiums Taxes. Insurance premiums taxes are now projected to be $227 million in 2022-23, $236 million in 2023-24, and $246 million in 2024-25. Compared to the previous estimates, the revised estimates represent decreases in insurance premiums tax revenues of $3 million in 2022-23 and $1 million in 2023-24, and an increase of $1 million in 2024-25. The new estimates reflect year-to-date collections, which have grown by 2.3% through April (lower than the previous forecast).

Miscellaneous Taxes. Miscellaneous tax revenues are estimated at $115 million in 2022-23, $103 million in 2023-24, and $111 million in 2024-25, with revenues declining by 15.2% in 2022-23, and 10.4% in 2023-24, followed by growth of 7.8% in 2024-25. The estimates have increased $8 million in 2022-23, $7 million in 2023-24, and $1 million in 2024-25, relative to the January estimates. The real estate transfer fee makes up the majority of miscellaneous taxes and is the reason for the increased estimates. The January forecast projected a steeper decline in the sales volume and price of existing houses compared to the May forecast. Similarly, real estate transfer fee collections have been stronger than previously anticipated since December, 2022. These factors have increased the overall forecast of miscellaneous tax revenues.

This office will continue to monitor state revenues, expenditures, and economic forecasts, and notify you and your colleagues of any further adjustments that may be necessary.

Sincerely,

Bob Lang

Robert Wm. Lang
Director

RWL/lb
cc: Members, Wisconsin Legislature