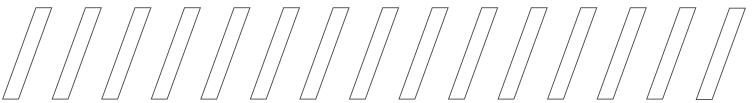




EXTENSION



## COVID-19 RESPONSE

# ANALYSIS OF KNOWN AND POTENTIAL IMPACTS OF COVID-19 ON LOCAL GOVERNMENTS

Learn about impacts to local governments due to the COVID-19 virus.

### INTRODUCTION

The novel corona virus known as COVID-19 is impacting the entire planet's population with far-ranging implications. The virus has changed commerce, employment, health-care and many other aspects of daily life. Public services, particularly those provided by local governments, are the topic of this paper. More specifically, this is an examination of local government revenue and expenditure — fiscal aspects. Local government bodies in Oklahoma include schools districts, cities, towns and county governments. Other local government bodies such as public libraries, emergency medical services (EMS) and fire districts are not addressed directly.

COVID-19 has altered daily living so as to alter both the revenues and expenditures of local governments. Both city and county governments in Oklahoma rely heavily upon sales taxes. Temporary closure of non-essential businesses, such as restaurants, altered sales tax collections. Temporary closure of non-essential businesses, such as restaurants, altered sales tax collections. At the same time, sales of staples may have increased temporarily as citizens stocked up on groceries and other items. School districts rely heavily on property taxes as well as state funds, which have been diminished. The state is experiencing a revenue failure in fiscal year 2020 and expects a relatively large decrease of revenue (and budget) in fiscal year 2021. State revenues are heavily affected by sales tax, income tax and gross production taxes on oil and gas. Oil and gas taxes are a percentage of product value, and those values have declined drastically. Furthermore, state income tax collections have declined and will remain at reduced levels due to the large increases in unemployment.

On the other hand, federal government and Federal Reserve Bank actions are helping offset and mediate the adverse impacts. Checks to individual taxpayers, loans and grants to business, assistance to state and local governments combined with lowered interest rates and increased liquidity are all having an ameliorating effect. As businesses, trade and travel reopen, the primary questions are will the economy bounce back quickly (as some forecast), and will the virus re-emerge, dampening the recovery? For Oklahoma, the international oil market also is important. Over supply of oil combined with reduced demand resulted in the lowest price per barrel in decades. Wells are being shut down and drilling suspended. Jobs are lost. When will prices (and gross production tax revenue) recover?

In the following pages, consideration is given to revenues of local governments, particularly sales tax, use tax, property tax and local utilities. Data are presented on trends, the recent history and prospects for the future. That is, consideration is given to the likely and potential impact of the virus on the primary revenue streams.

### CONTACT

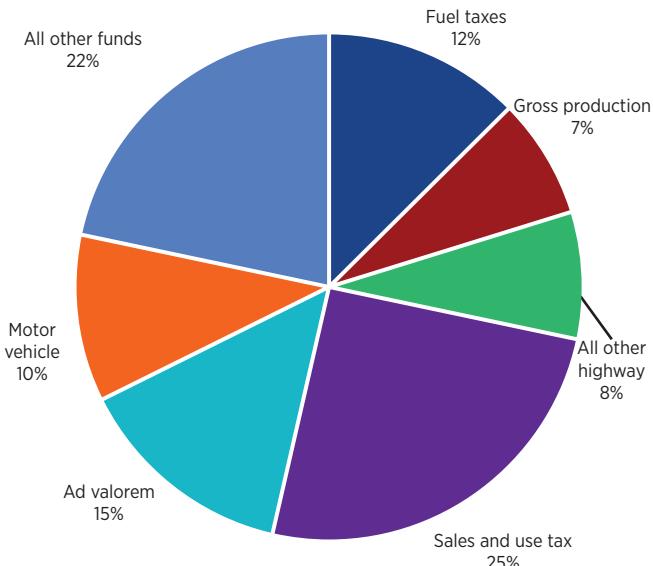
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**Statewide**

**FY 2014**

Ad valorem	280,478,638
Sales and use tax	321,319,016
Fuel tax	120,444,365
Motor vehicle	100,464,274
Gross production	83,446,230
All other	325,154,833
<b>Total county revenue</b>	<b>1,231,307,355</b>

**Figure 1. Average county sources of revenue, general, highway and cash funds, FY 2014.**

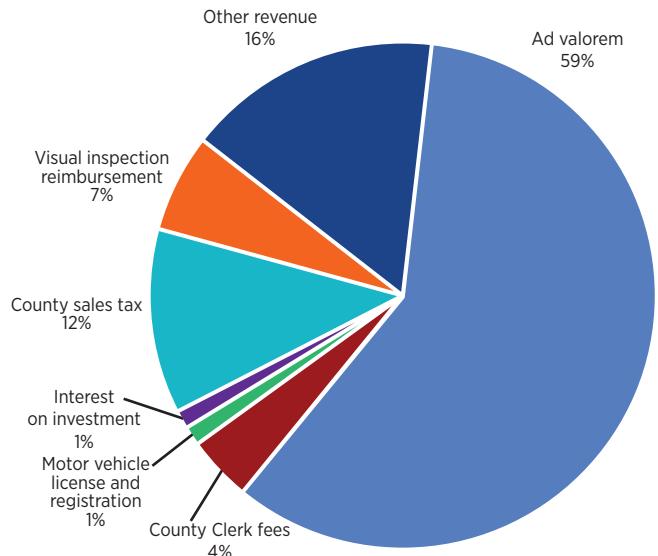
Source: Abstract of County General, Highway and Cash Funds, FY 2014 (<http://agecon.okstate.edu/ctp/index.asp?type=publications>)

Additionally, attention is given to the mitigating factors provided largely by federal funding. A brief look is given to expenditures.

The findings are that sales tax revenue has declined and will likely remain at reduced levels until economic recovery occurs. Hypotheses of pandemic management and rate of recovery vary widely. State and federal transfer payments to schools appear to be maintaining funding levels in the next fiscal year. Property taxes are based on pre-pandemic valuations, so negative impacts, except for potential non-payments, are limited. Next year could be a different story if recovery does not occur in the latter quarters of this calendar year. Cities and towns relying on sales tax and service and user fees may be hardest hit. Next, counties, schools and cities, respectively, are discussed. Unfortunately, this uncharted territory clouds the path ahead.

## COUNTY GOVERNMENT

County governments in Oklahoma operate on several funds, the largest two being the county general fund and the county highway fund. Counties often have several special revenue funds, commonly referred to as cash funds.



**Figure 2. Average county general fund revenue sources, FY 2016.**

Source: Abstract of County General, Highway and Cash Funds, FY 2016 (<http://agecon.okstate.edu/ctp/index.asp?type=publications>)

Figure 1 shows the overall funding for this set of funds – general, highway and cash funds. Prior to 1984, when county government first received authorization to adopt a sales tax, the property tax was by far the largest single source of revenue. Note sales and use tax are combined in Figure 1. Use tax is essentially sales tax collected and remitted to Oklahoma from out-of-state vendors. Over time, more and more out-of-state vendors have agreed to honor Oklahoma sales tax rates. Gross production tax revenues to counties are apportioned strictly for county road and bridge purposes and, by law, are based on production from the prior year (68 O.S. § 1004). So, gross production revenue allocated to counties will not be reduced until next year.

Figure 2 shows the continued dominance of property tax as the primary source of county general fund revenue, comprising 59% in fiscal year 2016. Note the presence of county sales tax in the figure. County governments have the option of placing sales tax in either the county general fund or in one or more county special revenue (cash) funds. A relatively small number of counties place their sales tax revenue in their general fund, hence the lesser percentage in Figure 2 relative to Figure 1.

Table 1 provides a recent history of statewide totals of county sales, use and ad valorem (property) tax. The decline in sales tax from 2015 to 2018 is largely associated with the decline in oil price followed by a rebound in fiscal year 2019. Higher oil prices mean more jobs, more personal income and more purchases. Use tax is correlated but is more variable. Ad valorem (property) tax is widely acknowledged for relative consistency and less variation

**Table 1. Sum of county sales, use and ad valorem tax revenue, all 77 counties by fiscal year.**

Fiscal Year	Sales Tax	% Change	Use Tax	% Change	Ad Valorem	% Change
2015	372,035,865		34,774,650		293,142,735	
2016	345,587,388	-7.1%	30,927,623	-11.1%	305,870,397	4.3%
2017	324,779,671	-6.0%	29,598,359	-4.3%	316,156,056	3.4%
2018	319,735,727	-1.6%	32,818,516	10.9%	330,914,841	4.7%
2019	338,511,827	5.9%	47,279,507	44.1%	347,913,851	5.1%

Source: Oklahoma Tax Commission and County Financial Database at OSU, respectively.

over time. Ad valorem taxes are based on the valuation of taxable property as of Jan. 1 of the prior year. Hence, fiscal year 2021 revenue is based on the Jan. 1, 2020 taxable value that was established prior to recognition of the virus pandemic.

In summary, county government is exposed to the variability of sales and use tax collections coming out of the virus pandemic. Fortunately, county government has the stability of ad valorem taxes to lean on. Jan. 1, 2020, taxable valuations were established prior to the pandemic outbreak so, unless taxpayers are delinquent on taxes coming due in November 2020, that revenue source will be stable. New property tax valuations will be established Jan. 1, 2021, and that could be a different story unless the effects of the pandemic have largely subsided. County road funding will be affected by subsidence of gross production tax revenue due to the one year lag. Of more immediate impact are the gasoline, diesel and motor vehicle tax allocations that are tied directly to current collections by the state.

## SCHOOL DISTRICTS

According to the Oklahoma Policy Institute, about two-thirds of public school budgets are from government transfer payments (largely state government) and about one-third from local property tax (although proportions will vary from district to district – <https://okpolicy.org/resources/online-budget-guide/revenues/local-government-revenues/>). It also is noteworthy that about two-thirds of all property tax dollars in Oklahoma go to school districts.

Table 2 shows total taxable valuation by fiscal year. Annual percent change from 2016 to 2020 has been close to 5% per year. The 2020 valuations are the basis for fiscal year 2021 taxes and those valuations are not yet available but will likely be similar to the historic growth pattern. Since mill levy rates are fairly consistent from year to year, ad valorem collections for fiscal year 2021 are likely to fall in line (unless there is an increase in delinquent payments). School districts budget no more than 95% of expected collections. Therefore, non-payment rates would have to be significant to disrupt revenue from this source.

The larger concern for 2021 is intergovernmental

**Table 2. Statewide total ad valorem taxable value by fiscal year.**

Fiscal Year	Taxable Valuation	% Change
2016	31,359,203,319	
2017	32,943,129,879	5.1%
2018	34,513,375,045	4.8%
2019	36,184,444,292	4.8%
2020	37,874,850,019	4.7%

Source: County Government Database, OSU

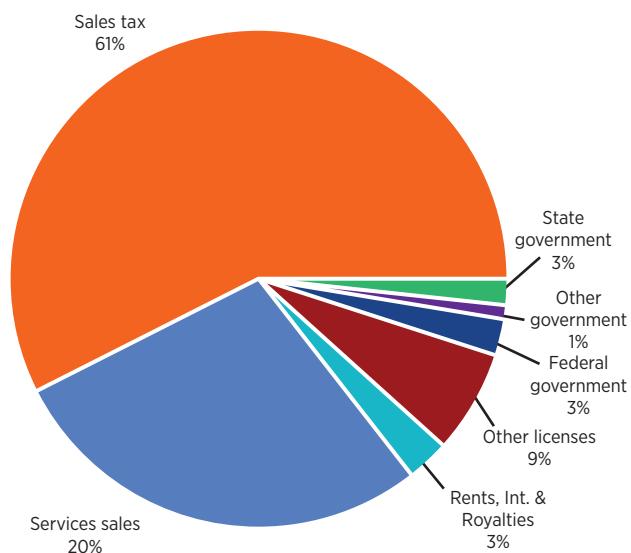
transfers, primarily from the state government. The fiscal 2021 appropriations bill (SB1922) reduced most appropriations by 4% from fiscal 2020 levels but reduced common education by only 2.5% (<https://nondoc.com/2020/05/04/budget-bills-fiscal-year-2021/>). But with the increase in expected federal government dollars, “It will actually be an increase of over 3% for funding of education even though it is a decrease in appropriations,” said House Appropriations and Budget Chairman Kevin Wallace (R-Wellston). According to the May 11, 2020, press release by Joy Hofmeister, State Superintendent of Public Instruction, “Nearly \$145 million in emergency federal relief is now available to Oklahoma school districts. Provided in the federal Coronavirus Aid Relief and Economic Security (CARES) Act, the funds are Oklahoma’s portion of the \$13 billion Elementary and Secondary School Emergency Relief (ESSER) Fund designated for states after the CARES Act was signed into law in March.”

Will the Legislature’s budget be met by adequate state revenue or will it fall short in fiscal 2021? Overall, for all agencies, the legislature appropriated \$400 million less for 2021 compared to 2020, shoring up shortfalls with Reserve and Rainy Day funds and, to some extent, rejecting the \$1.2 billion dollar shortfall projected by the State Board of Equalization. Obviously, these projections and assumptions leave some risk for 2021 funding. A 2021 budget shortfall is possible, yet a recovery also is possible. Therefore, it remains to be seen how school districts may be affected. As of now, their funding is indicated to be relatively secure.

## CITIES

According to the Oklahoma Policy Institute, "Cities and towns (known collectively as municipalities) collected over \$5.5 billion in 2012 revenues. More than half of all city revenues were user charges (\$3.1 billion), including utilities, a government entity that recovers costs from users to pay all operating and capital expenditures... fees. Indeed, two-thirds of all local user charges were collected by cities. The largest sources of fees were hospitals, followed by water, electric and sewerage charges. After user charges, the sales tax was the second largest revenue source for Oklahoma cities, generating \$1.8 billion." (<https://okpolicy.org/resources/online-budget-guide/revenues/local-government-revenues/>)

The Oklahoma Municipal League illustrates municipal funding in Figure 3.



**Figure 3. Oklahoma municipal revenues FY 2014.**

Source: FY 2014 SA&I forms, Oklahoma State Auditor

Sales tax (and use tax) are a large and important part of city and town (municipal) revenue across the nation and particularly in Oklahoma. As such, municipalities are rightly concerned with the impact of the pandemic. The most recent city sales and use tax data from the Oklahoma Tax Commission is the May 2020 receipts for 517 municipalities in Oklahoma, which were \$146,166,497.33. By contrast, May 2019 receipts were \$160,347,063.53. So, May 2020 receipts were 8.8% less than the same month a year ago (May 2020 receipts reflect March 2020 purchases). Since the impacts of the pandemic were just beginning to be felt in March, the expectation is for greater year-over-year reductions in the June distribution.

Looking at state sales tax collections will provide a more recent indicator of change in sales tax revenue. The Oklahoma Tax Commission reports daily receipts. David Francis at the Oklahoma Tax Commission, said in

an email May 21, 2020, "The daily cash report is all the tax we collected for each tax type, the previous business day. It's what we literally got in. For sales and use tax, it can be anything a merchant paid. Predominantly, from May 20-25, the funds merchants are paying their final payments from the month before and their estimated payments for the first half of the current month. So May 20, 2020, they filed their April 2020 actual reports and payments, and estimated payments for the first half of May." Depending on how well merchants estimate the first half of May, the most recent current report may help evaluate the current trend in sales tax at state, city and county levels because all three apply the sales tax to the same set of goods.

Through the fiscal year to date through May 20, state sales tax receipts are 6.4% less than the prior year to date. That is, collections are \$4,176,419,908 compared with \$4,460,813,268. On the other hand, state use tax collections for the same period are 5.9% more, \$661,505,262 compared with \$624,844,486 last year. Year-to-date figures include July 1 to current. Monthly, particularly recent months, collections may be more enlightening.

Table 3 shows state sales tax collections at the end of each month, December 2019 through May 21, 2020. It also shows the fiscal year to date compared with the prior year. The current year to date has been consistently trailing the prior year, but the difference increased in April and May as the impacts of the virus pandemic set in.

Table 4 shows state use tax collections at the end of each month, December 2019 through May 21, 2020. It also shows the fiscal year to date compared to the prior year. Current year to date has been consistently exceeding the prior year, but the difference decreased in April and May as the impacts of the virus pandemic set in. Month to date collections noticeably increased in April, relative to February and March. Consumers may have been turning more to online purchases as many of them sheltered-in-place. What is clear — purchases from out-of-state vendors have increased year after year. It also is clear that the additional use tax receipts more than offset the reduced sales tax receipts in December 2019 through February 2020, but did not in more recent months. So, if state sales and use tax receipts are combined, fiscal to date through May 21, 2020, trail prior year receipts by almost \$211 million, or 4.1%.

Sales and use tax receipts are driven by consumer demand. Consumer demand is largely a function of population and income. Record unemployment caused by the pandemic and low oil prices decrease consumer demand. Hence reduced sales tax receipts are expected until economic recovery occurs. Again, the timing of the recovery is uncertain, pending containment of the virus as non-essential businesses and other organizations re-open.

## EXTRA EXPENDITURES

Anecdotal data reported by various local governments

**Table 3. State Sales Tax Receipts, Selected Months and part of May 2020.**

	<i>Month To Date</i>	<i>Fiscal To Date</i>	<i>Prior Year To Date</i>	<i>Difference</i>	<i>Change %</i>
December	407,251,629	2,453,773,716	2,475,245,123	-21,471,406	-0.87
January	415,298,742	2,869,072,458	2,895,179,142	-26,106,684	-0.90
February	356,296,185	3,225,368,643	3,263,863,822	-38,495,179	-1.18
March	368,212,104	3,593,580,747	3,646,891,447	-53,310,701	-1.46
April	368,310,330	3,961,891,076	4,062,460,033	-100,568,957	-2.48
May thru 21st	250,772,526	4,212,663,602	4,465,711,297	-253,047,695	-5.67

Source: OTC Daily Report of Taxes Collected ([https://oktap.tax.ok.gov/OkTAP/Web/\\_/#9](https://oktap.tax.ok.gov/OkTAP/Web/_/#9))

**Table 4. State Use Tax Receipts, Selected Months and part of May 2020.**

	<i>Month To Date</i>	<i>Fiscal To Date</i>	<i>Prior Year To Date</i>	<i>Difference</i>	<i>Change %</i>
December	61,297,050	363,194,170	332,981,123	30,213,047	9.07
January	82,970,067	446,164,237	402,770,287	43,393,950	10.77
February	52,949,409	499,113,646	452,197,226	46,916,421	10.38
March	53,778,029	552,891,675	510,406,089	42,485,586	8.32
April	62,134,635	615,026,310	569,961,841	45,064,469	7.91
May thru 21st	52,319,937	667,346,247	625,214,724	42,131,523	6.74

Source: OTC Daily Report of Taxes Collected ([https://oktap.tax.ok.gov/OkTAP/Web/\\_/#9](https://oktap.tax.ok.gov/OkTAP/Web/_/#9))

point to additional costs imposed upon local governments by the pandemic. These range from equipment for telecommuting (working from home) to forgiving or delaying utility payments to acquisition of person protection equipment (PPE). These costs are real and may be substantial. However, there is no known collection of data available for statewide analysis. Therefore, no speculation is made here about the size and scope of such costs.

## SUMMARY

Local governments in Oklahoma are impacted by COVID-19 depending upon how the virus affects the various funding mechanisms upon which local governments depend. Primary funding mechanisms discussed in this paper are sales (and use) tax, ad valorem (property) tax, intergovernmental transfers (state to local government) and to a lesser extent, service fees (utilities). In the case of sales taxes, there is almost a two-month lag between the time purchases are made and the time the state distributes the receipts to local governments. Therefore, city and county governments are beginning (in May) to see the initial impacts of the virus. Daily state collection reports and State Board of Equalization projections

point toward significant sales tax declines continuing for several months. By contrast, property taxes (affecting schools and counties) will not be affected in fiscal year 2021 unless substantial numbers of taxpayers fail to pay their taxes in December 2020. If virus impacts persist, taxable property values could decline and reduce fiscal year 2022 collections. State transfer payments to local governments, particularly schools, should not decline in fiscal year 2021. The Legislature and Congress have taken actions that should sustain and increase school budgets. Service or user fees are significant revenue sources for many cities and towns. Chief among these are utilities. To the extent that customers are unable or late to pay utilities, revenue will be adversely affected. Federal assistance to individuals and businesses may effectively mediate the revenue losses. Unfortunately, there is no economic model suited to accurately predict the persistence of the pandemic or rate of recovery.