United States Government Accountability Office

Report to Congressional Committees

July 2021

STATE AND LOCAL GOVERNMENTS

Fiscal Conditions During the COVID-19 Pandemic in Selected States

Accessible Version

A Century of Non-Partisan Fact-Based Work

GAO-21-562

GAO Highlights

Highlights of GAO-21-562, a report to congressional committees

Why GAO Did This Study

The COVID-19 pandemic and related policies had a rapid and severe effect on the U.S. economy, including state and local governments. To limit social contact and slow the spread of the pandemic, nearly all states implemented policies that limited certain economic activities. Relief laws, including the CARES Act, provided appropriations to state and local governments to address the public health and economic threats posed by the pandemic.

The CARES Act includes a provision for GAO to report on COVID-19 pandemic oversight efforts. This report examines (1) changes in revenues and expenditures for the state and local government sector since the onset of the pandemic, (2) changes in revenues and expenditures for selected states, (3) actions selected states took to address changes in revenues and expenditures, and (4) factors that affected the selected states' capacity to implement federal programs.
To conduct this work, GAO analyzed state and local government revenue and expenditure data from the U.S. Census Bureau and the Bureau of Economic Analysis's National Income and Product Accounts. GAO analyzed state budget and other relevant documents and interviewed budget officials in eight states that represented a range of factors, including number of COVID-19 cases, revenue sources, and geographic region. GAO also interviewed organizations that represent state and local governments and experts that provide financial and credit risk information to state and local governments.

View GAO-21-562. For more information, contact Michelle Sager at (202) 512-6806 or SagerM@gao.gov.

July 2021

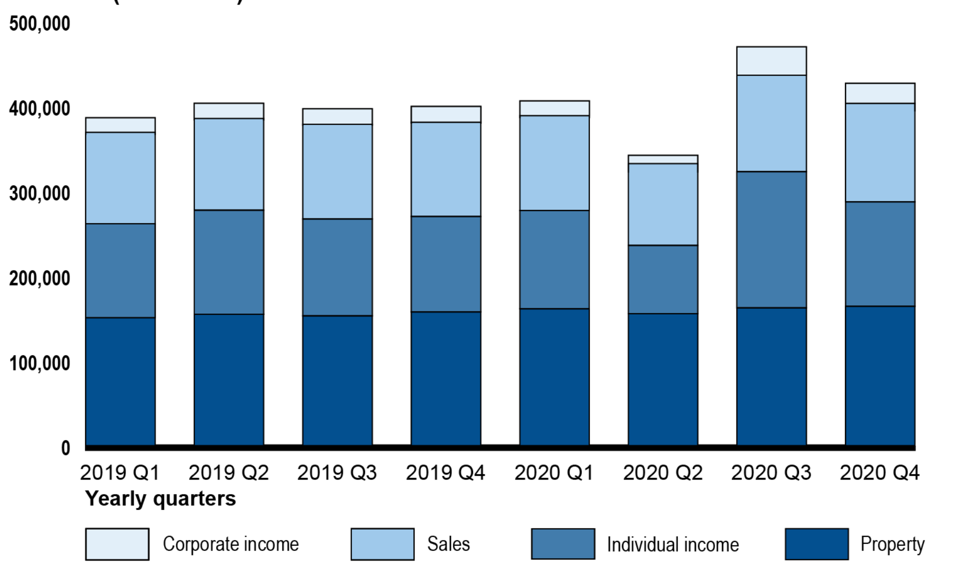
STATE AND LOCAL GOVERNMENTS

Fiscal Conditions During the COVID-19 Pandemic in Selected States

What GAO Found

State and local government revenues from individual, corporate, and sales taxes declined about $61 billion in the second quarter of 2020 compared to the second quarter in 2019 and rebounded in the third and fourth quarters of 2020. State and local government expenditures remained largely flat throughout 2020 as state and local governments increased expenditures in some areas but limited spending in other areas.

State and Local Government Revenues, First Quarter 2019 through Fourth Quarter 2020



Source: GAO analysis of U.S. Census Bureau data. | GAO-21-562

Data table for State and Local Government Revenues, First Quarter 2019 through Fourth Quarter 2020

	Property	Individual income	Sales	Corporate income
2019 Q1	150525	110747	107482	17301
2019 Q2	154636	122412	107936	18060
2019 Q3	152693	114037	111478	18357
2019 Q4	157457	112223	110846	18785
2020 Q1	161110	115590	111597	17505
2020 Q2	155441	80296	96129	9831
2020 Q3	162182	160377	113342	33489
2020 Q4	164050	122897	115892	23586

Among the eight states GAO selected, those highly reliant on tax revenues from the energy and tourism and leisure sectors were particularly vulnerable to the economic effects of the pandemic. Other states saw varying levels of revenue declines based on factors such as the duration of business shutdowns. Some selected states revised their revenue forecasts downward as the pandemic progressed and some states' revenue declines were not as severe as initially projected by the revised revenue forecasts.

Most selected states increased public health and safety expenditures and cut spending in other areas. Six states took actions aimed at reducing spending, including hiring freezes or furloughs. Half of the selected states used reserve funds to help balance their budgets. Officials from most states reported that their proposed budgets did not include tax or fee increases.

Five of the eight selected states used the federal assistance they received, including Coronavirus Relief Funds (CRF), to help bolster their states' capacity to implement federal programs. In particular, states used CRF to help manage the increased demand for services due to COVID-19, such as administering unemployment insurance benefits.

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Abbreviations

BEA	Bureau of Economic Analysis
BLS	U.S. Bureau of Labor Statistics
Bureau	U.S. Census Bureau
CDC	Centers for Disease Control and Prevention
COVID-19	Coronavirus Disease 2019
CRF	Coronavirus Relief Fund
GDP	gross domestic product
FFCRA	Families First Coronavirus Response Act
FMAP	Federal Medical Assistance Percentage
NASBO	National Association of State Budget Officers
NIPA	National Income and Product Accounts
PMO	Project Management Office
Treasury	Department of the Treasury
UI	Unemployment Insurance

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July 15, 2021

Congressional Committees

The Coronavirus Disease 2019 (COVID-19) pandemic and related policies that limited certain economic activities had a rapid and severe effect on the U.S. economy, including state and local governments. State and local government revenues decreased and certain expenditures increased as these governments grappled with reduced economic activity and increased demand for public health services in 2020.

To limit social contact and slow the spread of the COVID-19 pandemic, nearly all states implemented policies that had the effect of limiting certain economic activities. Widespread business closures led to immediate and substantial job losses and resulted in reduced revenue. Reduced economic activity included declines in industrial production, retail sales, and personal income. While these areas of the economy have since recovered to varying degrees, state and local governments faced immediate fiscal pressures.

Four COVID-19 relief laws, including the CARES Act, were enacted as of September 2020 to address the public health and economic effects posed by the COVID-19 pandemic.[1] These laws provided an estimated $335 billion in funds to agencies for assisting U.S. states, localities, territories, and tribal governments in their responses to the COVID-19 pandemic.

The CARES Act appropriated $150 billion to the Department of the Treasury (Treasury) for the Coronavirus Relief Fund (CRF) for direct assistance to states, localities, territories, and tribal governments for necessary expenses incurred due to the COVID-19 public health

[1]Paycheck Protection Program and Health Care Enhancement Act, Pub. L. No. 116-139, 134 Stat. 620 (2020); CARES Act, Pub. L. No. 116-136, 134 Stat. 281 (2020); Families First Coronavirus Response Act, Pub. L. No. 116-127, 134 Stat. 178 (2020) (FFCRA); and Coronavirus Preparedness and Response Supplemental Appropriations Act, 2020, Pub. L. No. 116-123, 134 Stat.146 (2020).

emergency.[2] Under the CARES Act, CRF payments are allocated to the 50 states and eligible localities based on their populations, with no state receiving less than $1.25 billion.[3] More recently, the American Rescue Plan Act of 2021 appropriated $362 billion to Treasury in direct aid to states, localities, territories, and tribal governments through the Coronavirus State and Local Fiscal Recovery Fund to address the continued impact of COVID-19 on the economy, public health, state and local governments, individuals, and businesses.[4]

The CARES Act includes a provision for us to report on our ongoing monitoring and oversight efforts related to the COVID-19 pandemic.[5] This report examines (1) what is known about changes in revenues and expenditures for the state and local government sector since the onset of the pandemic, (2) how revenues and expenditures have changed since the onset of the pandemic for selected states, (3) what actions selected states have taken to address changes in revenues and expenditures, and (4) what factors have affected the selected states' capacity to implement federal programs.

[2]Pub. L. No. 116-136, § 5001, 134 Stat. at 501, *codified at* 42 U.S.C. § 801(c). The CARES Act provided more than $2 trillion in emergency assistance and health care response for individuals, families, and businesses affected by COVID-19. As required by the CARES Act, CRF recipients may use the funds to cover costs incurred between March 1, 2020, and December 30, 2020, and that had not accounted for in their most recent budget prior to the act's enactment. This time-frame was extended to December 31, 2021 by the Consolidated Appropriations Act, 2021. Pub. L. No. 116-260, div. N. tit. X, § 1001, 134 Stat. 1182, 2145 (2020).

[3]Pub. L. No. 116-136, § 5001, 134 Stat. at 502, *codified at* 42 U.S.C. § 801(c). Populations as measured by the Census Bureau in 2019. Localities with populations of at least 500,000 may opt to receive disbursements directly from the Department of the Treasury. These direct disbursements are then deducted from the state's allocation, and are equal to the product of (1) the state or territory allocation amount, (2) the share of the state or territory population served by the local government, and (3) 45 percent.

[4]American Rescue Plan Act of 2021, Pub. L. No. 117-2, 135 Stat. 4 (2021). Recipients can use the funds to cover allowable costs incurred by December 31, 2024. We will review actions federal agencies and state and local governments have taken in response to the act in future reporting.

[5]Pub. L. No. 116-136, § 19010, 134 Stat. at 579-81. We regularly issue government-wide reports on the federal response to COVID-19. For the latest report, see GAO, *COVID-19: Sustained Federal Action Is Crucial as Pandemic Enters Its Second Year*, GAO-21-387 (Washington, D.C.: Mar. 31, 2021). Our next government-wide report will be issued on July 19, 2021, and will be available on GAO's website at https://www.gao.gov/coronavirus.

To describe what is known about changes in revenues and expenditures for the state and local government sector, we analyzed data on states' and localities' revenues and expenditures from the U.S. Census Bureau (Bureau) and expenditures from the Bureau of Economic Analysis's (BEA) National Income and Product Accounts (NIPA) for 2019 and 2020. For purposes of this review, we determined that the Bureau and BEA NIPA data were sufficiently reliable for our analysis of state and local government revenues and expenditures. Our data reliability assessment included reviewing relevant documentation and reviewing the data to identify obvious errors or outliers.

To identify how selected states' revenues and expenditures have changed after the onset of the pandemic, actions they took to address these changes, and the factors that affected the selected states' capacity to implement federal programs, we interviewed budget officials in eight states.[6] Those states included:

- Arizona
- Florida
- Michigan
- Nevada
- New Hampshire
- North Carolina
- North Dakota
- Pennsylvania

Combined, these states represent about 20 percent of the U.S. population. We selected these states on the basis of a number of factors, including: range in the number of reported COVID-19 cases per 100,000 as of October 2020, predominant source of tax revenue in the state, and geographic region. A more detailed description of our scope and methodology is included in appendix I.

We conducted this performance audit from August 2020 to July 2021 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain

[6]For purposes of this report, we define state capacity in terms of organizational, human capital, and financial capacity. A more detailed discussion of capacity is included in appendix I.

sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

The nation has experienced the spillover effects of a pandemic on the economy as millions have lost their jobs due to stay-at-home orders and business closures aimed at "flattening the curve," or taking the burden off the health care system by reducing infections to a manageable level. We recently reported that, as of February 2021, indicators for some areas of the country's economy supported by the federal pandemic response had returned to pre-pandemic levels while other areas remained far from their pre-pandemic conditions.[7] Improvements in bond market indicators, for example, suggest that corporate borrowers and state and local governments had access to credit that was somewhat improved compared to before the pandemic.

State and local government revenues partly depend on the overall economy, and actions to stem the spread of the virus drastically reduced economic activity. In the second quarter of 2020 with the onset of the pandemic, gross domestic product (GDP) declined at an annual rate of 31.4 percent. Recent data show that GDP grew at an annual rate of 6.4 percent in the first quarter of 2021 to a level that was about 1 percent smaller than the size of the economy in the fourth quarter of 2019.

Prior to the COVID-19 pandemic, state and local governments experienced overall growth in revenues and expenditures during the past 20 years. As we previously reported, from 1998 to 2018, inflation-adjusted state and local government revenues increased from about $1.6 trillion in 1998 to about $2.6 trillion in 2018. At the same time, we and the National Association of State Budget Officers (NASBO) reported that median state

[7]See GAO, *COVID-19: Sustained Federal Action Is Crucial as Pandemic Enters Its Second Year*, GAO-21-387 (Washington, D.C.: Mar. 31, 2021).

rainy day fund balances as a percentage of total general fund expenditures increased to their highest level in the last 20 years in 2018.[8]

The State and Local Sector Saw an Initial Decline and Subsequent Rebound in Revenues, while Expenditures Remained Largely Flat

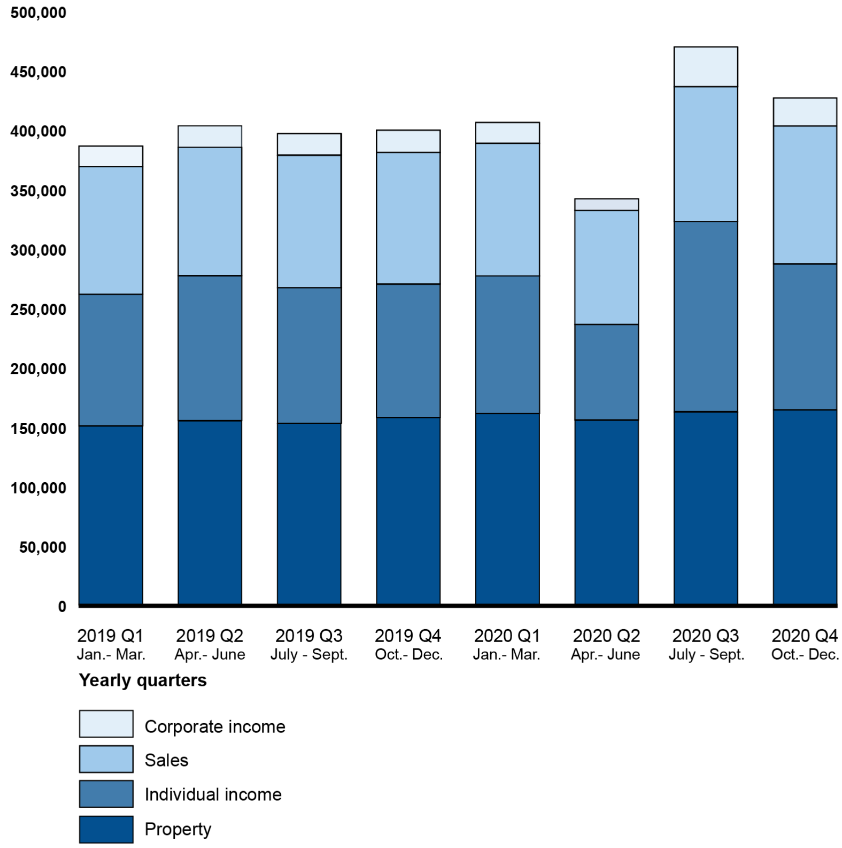
In the aggregate, state and local governments experienced revenue declines after the onset of the pandemic during the second quarter of 2020. As shown in figure 1, state and local government own-source tax revenues decreased by $61.3 billion in the second quarter of 2020, compared to the same period in 2019.[9] In particular, revenues from individual income, corporate income, and sales tax saw a significant decline in the second quarter of 2020 (April through June), compared to the second quarter in 2019, but rebounded in the third and fourth quarters of 2020.[10] Additionally, while property taxes declined in the second quarter of 2020, their rate of decline was significantly lower than other sources of own-source tax revenue such as individual income and sales taxes.

[8]Rainy day funds include state budget stabilization or reserve funds that state governments may use to supplement general fund spending during a revenue downturn or other unanticipated shortfall. Although every state has some type of rainy day fund, deposit and withdrawal rules vary considerably. For additional information, see GAO, *Intergovernmental Issues: Key Trends and Issues Regarding State and Local Sector Finances*, GAO-20-437 (Washington, D.C.: Mar. 23, 2020). See also NASBO, *Budget Processes in the States* (Washington, D.C.: Spring 2021).

[9]Own-source revenue refers to the share of revenue generated from different types of state and local taxes.

[10]Based on the U.S. Census Bureau's *Quarterly Summary of State & Local Government Tax Revenue*. We used the Bureau's four categories of tax data as part of our analysis of the state and local government sector, which included the four categories of own-source revenue: (1) sales; (2) property; (3) corporate income; and (4) individual income. The Bureau's data did not include all types of own-source revenue sources, such as excise taxes or user fees, or other types of revenue, such as federal grants to state and local governments, including COVID-19 pandemic-related funding.

Figure 1: State and Local Government Own-Source Tax Revenues (in millions), First Quarter 2019 through Fourth Quarter 2020



Source: GAO analysis of U.S. Census Bureau data. | GAO-21-562

Data table for Figure 1: State and Local Government Own-Source Tax Revenues (in millions), First Quarter 2019 through Fourth Quarter 2020

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Revenues Declined and Then Rebounded

The changes in state and local government tax revenues identified in figure 1 varied by source and were driven by a number of factors:

Individual income taxes. State and local government revenue from individual income taxes decreased 30.5 percent ($35.3 billion) in the second quarter of 2020, followed by a 99.7 percent ($80.1 billion) increase in the third quarter of 2020.[11] According to Moody's Analytics and other organizations, income tax revenue from high-income earners remained strong during the pandemic, supporting states that rely on income tax revenue from high-income earners. Specifically, higher-income earners—who pay more income tax than lower income earners—were able to telework throughout the pandemic, while lower-wage earners, largely in service industries, experienced significant job losses.

Further, federal assistance provided to state and local governments through the CARES Act increased and expanded unemployment insurance benefits for those who lost their jobs due to the pandemic, and unemployment benefits are normally subject to tax under federal and state law.[12] In addition, nearly all state governments that assess an individual income tax joined with the Internal Revenue Service in extending their income tax filing due dates from April 2020 to July 2020.[13] This action may have contributed to a shift in income tax revenue collections, which are normally collected in the first or second quarter of 2020 to the third quarter of 2020. Between 2019 and 2020, state and local

[11]According to the Tax Foundation, forty-one states and the District of Columbia impose broad-based taxes on individual income.

[12]Pub. L. No. 116-136, tit. II, 134 Stat. at 313. In addition, the American Rescue Plan Act of 2021 provides for an allowance of $10,200 of unemployment insurance compensation to be tax free in 2020, if an individual's adjusted gross income is less than $150,000. Pub. L. No. 117-2, § 9042, 135 Stat. at 122.

[13]IRS Notice 2020-23, 2020-18 IRB 742 (Apr. 27, 2020). Notice 2020-23 amplified relief provided in Notice 2020-18 and Notice 2020-20. 2020-15 IRB 590 (Apr. 6, 2020); and 2020-16 IRB 660 (Apr. 13, 2020). The Secretary of the Treasury has statutory authority to postpone filing and payment deadlines for taxpayers affected by a "federally declared disaster," which is any disaster determined by the President to warrant assistance by the federal government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act. 26 U.S.C. §§ 7508A, 165(i)(5)(A). The President's March 13 determination instructed the Secretary of the Treasury to provide relief from tax deadlines to Americans who have been adversely affected by the COVID-19 emergency, as appropriate, pursuant to 26 U.S.C. § 7508A(a).

government revenue from individual income taxes increased 4.3 percent, from $459 billion in 2019 to $479 billion in 2020.

Sales taxes. State and local government revenue from sales taxes decreased 13.9 percent ($15.5 billion) in the second quarter of 2020, reflecting a decline in retail sales at the height of the pandemic during a time of mandatory or voluntary business closures and stay-at-home mandates.[14] By the third quarter of 2020, revenue from state and local sales tax rebounded, reflecting an increase of 17.9 percent ($17.2 billion). According to the Tax Foundation and other experts, consumer spending significantly shifted to remote online sales and thereby contributed to sales tax revenues.

Moody's Analytics, for example, noted that as businesses became subject to mandatory closures, consumer spending remained resilient as taxpayers shifted their purchases online, and that, with recent court decisions affecting tax law changes, more of those purchases were subject to sales tax. For example, as a result of the Supreme Court's ruling in South Dakota v. Wayfair, Inc., states can require out-of-state sellers to collect and remit sales taxes on purchases made from those out-of-state sellers, even if the seller does not have a substantial physical presence in the taxing state.[15] Between 2019 and 2020, revenue from the sector's sales taxes decreased 0.2 percent, from $438 billion in 2019 to $437 billion in 2020.

Property taxes. State and local government revenue from property taxes decreased 3.5 percent ($5.7 billion) in the second quarter of 2020, followed by a 4.3 percent ($6.7 billion) increase in the third quarter of 2020. Compared to the other three categories of own-source revenue (i.e. sales, individual income, and corporate income), revenue from property taxes experienced a lower rate of decline after the onset of the pandemic.

[14]According to the Tax Foundation, forty-five states and the District of Columbia collect statewide sales taxes, while local sales taxes are collected in 38 states.

[15]*South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (2018). In 2017, we reported that states could realize between an estimated $8.5 billion and $13.4 billion in additional state sales tax revenue across all states if all sellers were required to collect taxes on all remote sales at current rates. For additional information, see GAO, *Sales Taxes: States Could Gain Revenue from Expanded Authority, but Businesses Are Likely to Experience Compliance Costs*, GAO-18-114 (Washington, D.C.: Nov. 16, 2017).

Property tax changes often lag behind a fiscal downturn due to the time needed for state and local governments to reassess property values for property tax purposes. There are often significant delays between changes in property values and assessments in addition to limits placed on the growth of property taxes. Local governments—who typically assess and collect the majority of property taxes—may not experience the full effects of changing property tax values on property tax revenues for some time.[16]

In addition, residential housing values continued to appreciate during the pandemic, while commercial real estate experienced stress due to pandemic-related restrictions on economic activity. Between 2019 and 2020, state and local government revenue from property taxes increased 4.5 percent, from $615 billion in 2019 to $643 billion in 2020.

Corporate income taxes. State and local government tax revenue from corporate income taxes decreased 43.8 percent ($7.7 billion) in the second quarter of 2020, followed by a 240.6 percent ($23.7 billion) increase in the third quarter of 2020. Similar to individual income taxes, some states also extended their corporate income tax filing due dates from April 2020 to July 2020, which may have shifted tax revenues from the first or second quarter of 2020 to the third quarter of 2020.

Some states also announced payment relief plans for corporate income taxes, such as waiving penalties for late filing. However, our analysis of Bureau data showed that, in 2019, corporate income taxes represented only about 5 percent of total own-source tax revenues for the state and local government sector. Between 2019 and 2020, state and local government revenue from corporate income taxes increased 16.4 percent, from $73 billion in 2019 to $84 billion in 2020.

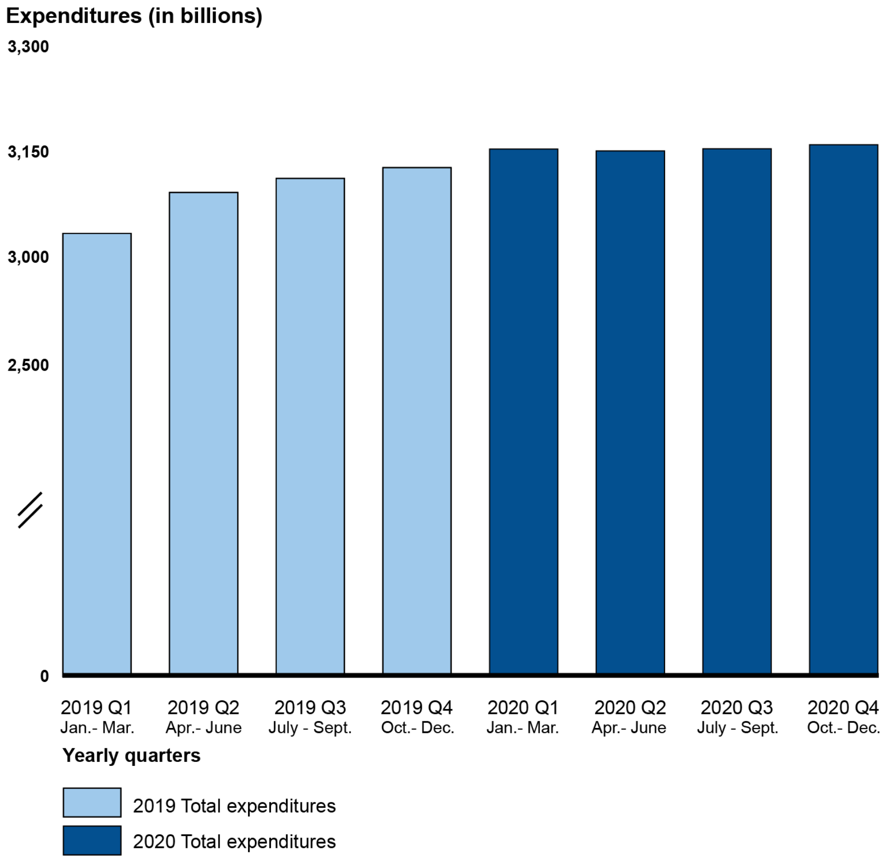
Expenditures Remained Relatively Flat

State and local government expenditures were also affected by the pandemic. According to data from BEA, while state and local government total expenditures grew slightly in 2020, compared to 2019, expenditures

[16]Although property taxes are primarily a local government revenue source, states largely control the conditions under which they are administered. Property tax limits generally are enacted by states and cover an entire state.

remained relatively flat over 2020 (see figure 2).[17] Specifically, state and local government expenditures increased by 1.8 percent ($55.8 billion) between 2019 and 2020. However, from the first quarter of 2020 to the fourth quarter of 2020, state and local government expenditures increased 0.17 percent ($5.5 billion).

Figure 2: State and Local Government Expenditures (annualized in billions), First Quarter 2019 through Fourth Quarter 2020



Source: GAO analysis of Bureau of Economic Analysis data. | GAO-21-562

[17]Based on BEA National Income and Product Accounts, Table 3.3: State and Local Government Current Receipts and Expenditures.

Data table for Figure 2: State and Local Government Expenditures (annualized in billions), First Quarter 2019 through Fourth Quarter 2020

2019 Q1 Jan-Mar	2019 Q2 Apr-Jun	2019 Q3 Jul-Sept	2019 Q4 Oct-Dec	2020 Q1 Jan-Mar	2020 Q2 Apr-Jun	2020 Q3 Jul-Sept	2020 Q4 Oct-Dec
3054.4	3105.7	3123.2	3136.8	3159.9	3157.6	3160.3	3165.4

While state and local governments increased expenditures in some areas to address the pandemic, many also took action to limit spending in other areas. As we have reported, most states and local governments are required to balance their operating budgets, which may limit their ability to increase expenditures to respond to public emergencies or economic downturns that may also decrease their revenues.[18] A number of organizations we interviewed, such as NASBO and the rating agencies, identified a range of changes to state and local government expenditures due to the pandemic:

Public Health. State and local governments increased expenditures in a wide range of public health areas, including testing, personal protective equipment, hazard pay for frontline workers, and other medical expenses.[19] Medicaid and the Children's Health Insurance Program enrollment also increased by 11.7 percent (8.2 million individuals) from February 2020 to November 2020, further increasing state expenditures on public health as these programs are partially funded by state governments.[20]

We recently reported that in the months since the beginning of the pandemic, the number of people covered under Medicaid increased, due in part, to increased applications for Medicaid coverage and requirements under the Families First Coronavirus Response Act for states to maintain Medicaid enrollment for certain beneficiaries regardless of their eligibility.[21] At the same time, we reported that

[18]For additional information, see GAO, *State and Local Governments' Fiscal Outlook*, GAO-20-269SP (Washington, D.C.: Dec.19, 2019).

[19]We have also extensively reported on increased expenditures on public health. For example, see GAO, *COVID-19: Opportunities to Improve Federal Response and Recovery Efforts*, GAO-20-625 (Washington, D.C.: June 25, 2020), and GAO-21-387.

[20]States and the federal government share in financing Medicaid, a health care program for low-income and medically needy individuals. States finance the nonfederal share with state general funds and other sources, such as taxes on health care providers and funds from local governments.

[21]Pub. L. No. 116-127, § 6008, 134 Stat. 178, 208-09 (2020) ("FFCRA").

while increased federal Medicaid funding helped states respond to the public health emergency, it is not permanent and states will face challenges in resuming normal Medicaid activities, including backlogs for re-determining beneficiary eligibility for Medicaid coverage.[22]

K-12 and Higher Education. State and local governments experienced higher expenditures in providing broadband and computer equipment to students for remote learning, child care access, and nutrition programs to underserved communities. We reported, for example, that 74 of the 100 largest school districts in the United States chose distance learning as their only instructional model for the 2020-2021 school year.[23]

Public Transportation. The pandemic affected all modes of public transit, such as buses, subways, light rail, and commuter rail, in urban, rural, and tribal areas. Some transportation authorities, which often rely on user fees as a significant source of funding for operating or capital expenses, decreased services or delayed projects, following a decrease in ridership with the onset of the pandemic and pandemic-related restrictions on travel. For example, we recently reported that the pandemic exacerbated existing funding challenges for commuter rail agencies. Specifically, systems experienced significant declines in ridership and associated fare revenue, and in funding from state and local sales taxes.[24]

State and Local Government Employment. Employee compensation is the largest expenditure for the state and local government sector.[25] We have previously reported on state and local government employment as a timely indicator of state and local fiscal conditions.[26] Based on unemployment data from the Bureau of Labor Statistics, with the onset of the pandemic, state and local government employment decreased by more than 1.5 million jobs on a seasonally-adjusted basis from February 2020 to May 2020. While state and local government employment grew following the initial decrease, based on preliminary data for May 2021, state and local government

[22]See GAO-21-387.

[23]GAO, *Distance Learning: Challenges Providing Services to K-12 English Learners and Students with Disabilities during COVID-19*, GAO-21-43 (Washington, D.C.: Nov.19, 2020).

[24]GAO, *Commuter Rail: Information on Benefits and Funding Challenges for Service in Less Urbanized Communities*, GAO-21-355R (Washington, D.C.: Apr.1, 2021).

[25]GAO-20-269SP.

[26]GAO-21-387.

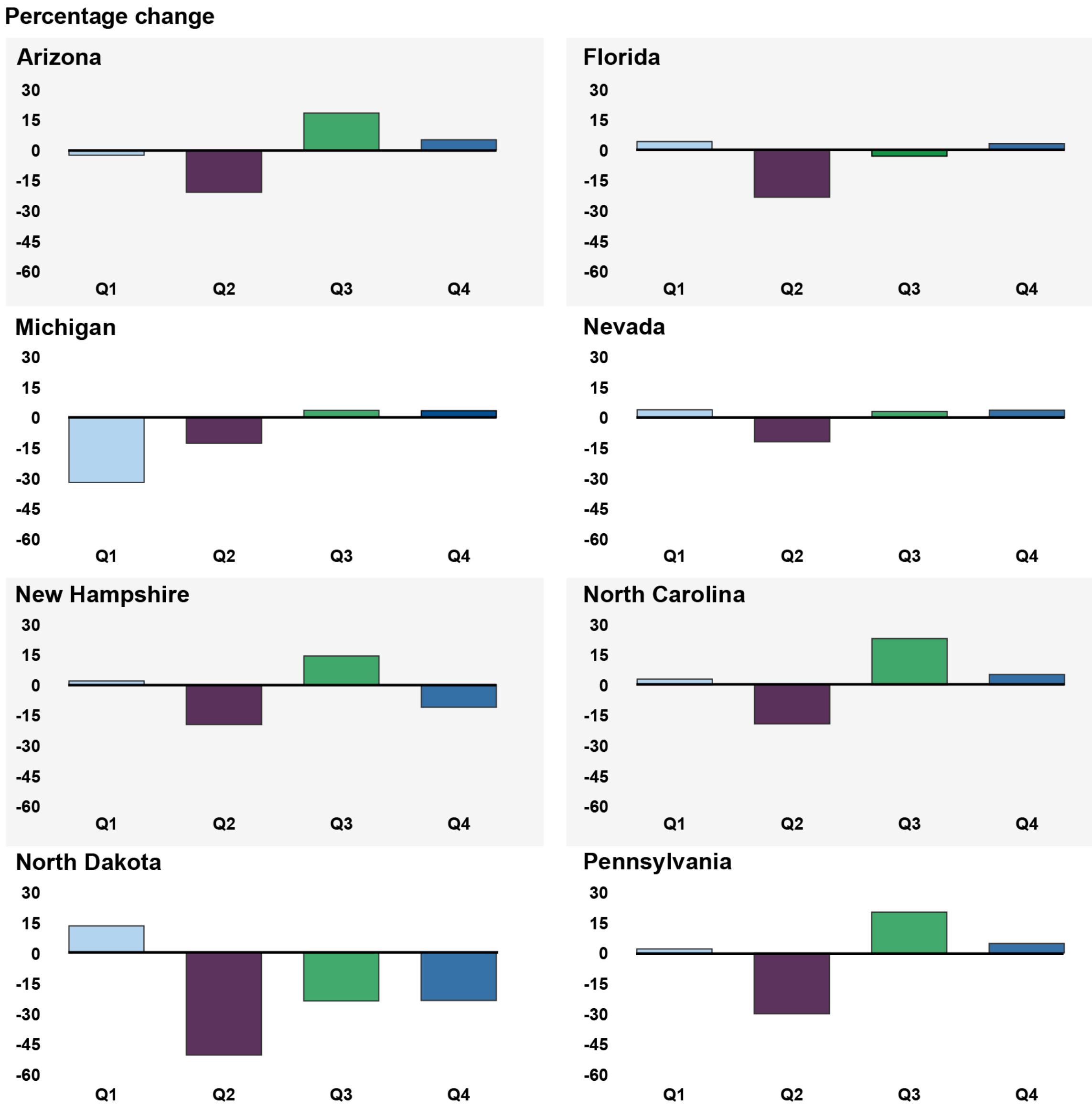
employment still remained about 1.2 million jobs less than pre-pandemic levels.

Selected States Experienced Varying Degrees of Decreased Revenues and Increased Expenditures

Predominant Revenue Source and Economic Sector Affected Revenue Stream

All eight states in our review experienced varying degrees of declines in own-source revenues after the onset of the pandemic. As shown in figure 3, all states experienced a decrease in own-source revenue of at least 10 percent in the second quarter of 2020, compared to the same quarter in 2019.

Figure 3: Percent Change in the Selected State's Tax Revenues Collected in 2020 Compared to the Same Quarter in 2019



Source: GAO analysis of U.S. Census Bureau data. | GAO-21-562

Data table for Figure 3: Percent Change in the Selected State's Tax Revenues Collected in 2020 Compared to the Same Quarter in 2019

	2020 Q1	2020 Q2	2020 Q3	2020 Q4
Arizona	-2.5%	-20.9%	18.3%	5.1%
Florida	4.2%	-23.3%	-3.0%	3.1%
Michigan	-32.1%	-12.7%	3.6%	3.4%
Nevada	3.8%	-12.0%	3.0%	3.7%
New Hampshire	2.0%	-19.6%	14.3%	-11.0%
North Carolina	2.9%	-19.2%	22.9%	5.2%
North Dakota	13.5%	-50.4%	-23.6%	-23.4%
Pennsylvania	2.0%	-30.1%	20.2%	4.7%

The extent of revenue decreases and increases varied across the eight states, depending on a number of factors. These factors included the state's predominant source of revenue, economic sector, and the extent of the state's mandatory shutdowns of businesses and other parts of the economy in response to escalating COVID-19 cases.

Of the eight states, Census Bureau data showed that North Dakota experienced the largest decline in tax revenues—more than 50 percent in the second quarter of 2020, compared to the same quarter in 2019 (see figure 3). North Dakota relies on revenues from severance tax imposed on oil and gas production, which accounted for 53 percent of the state's revenues in fiscal year 2019.[27] According to state officials, North Dakota experienced an impact from both business restrictions and reduced consumer activity, but also from the unprecedented drop in oil and gas activity and prices. The sudden drop in prices that resulted from the collapse in global demand resulted in a significant decrease in the profitability of North Dakota oil wells. As a result, those wells were immediately shut down. North Dakota's daily production of oil declined from more than 1.5 million barrels of oil per day in February 2020 to less than 900,000 barrels in May and June 2020. According to state officials, through November 2020 of North Dakota's biennial budget period, revenues from oil and gas taxes were below the state's forecast by 24 percent, or about $780 million.[28]

[27]Severance taxes are taxes imposed on the removal of natural products (e.g., oil, gas, other minerals, timber, fish, etc.) from land or water and measured by the value or quantity of products removed or sold.

[28]North Dakota's relevant biennial budget period was 2019-2021, which began July 1, 2019 and ended June 30, 2021, and covered fiscal years 2020 and 2021.

According to North Dakota officials, lower oil and gas production or prices also affected the state's other sources of revenue, such as individual income, corporate income, and sales taxes. Specifically, declines in corporate profits within North Dakota's energy production sector reduced corporate tax revenues, while declines in employment reduced income and sales tax revenues.

In December 2020, North Dakota officials told us the state released its first updated budget forecast for the balance of fiscal year 2021. The state's oil and gas taxes were estimated to decrease by about 35 percent in fiscal year 2021, compared to fiscal year 2020. North Dakota's revenues for four of its other major taxes—sales, motor vehicle, individual income, and corporate income—were estimated to decrease by 9 percent in fiscal year 2021, compared to fiscal year 2020.

Our review of selected states also showed that state economies dependent on sales tax revenues from the tourism and leisure industry were particularly vulnerable to the economic effects of the pandemic.[29] Both Florida and Nevada rely on sales tax for more than half of their own-source revenues and the states' collection of these taxes are heavily dependent on the tourism and leisure industry.

- In Florida, for fiscal year 2019, Census Bureau data showed that sales tax collections provided nearly 80 percent of the state's total general revenue collections. From April through June 2020, the total number of tourists visiting the state of Florida declined 60.3 percent, compared to the same period in 2019. As a result, sales tax revenues from Florida's tourism sector declined more than 11 percent in fiscal year 2020, compared to fiscal year 2019. State officials told us that they did not expect tourism to return to pre-pandemic levels until fiscal year 2022.
- In Nevada, declines in economic activity from reduced tourism and mandatory business closures affected Nevada's sales tax revenues

[29]We have also reported that the pandemic affected some sectors of the economy much more than others, such as leisure and hospitality. For additional information, see GAO-21-387.

and the state's gaming tax collections.[30] Specifically, Nevada's 2 percent sales and use tax, which in fiscal year 2018 comprised about 28 percent of the state's general fund revenues, declined 1.6 percent (more than $20 million) between fiscal year 2019 and fiscal year 2020. Gaming tax collections decreased almost 20 percent between fiscal year 2019 and fiscal year 2020, reducing gaming tax collections by about $156 million.[31] Gaming collections are projected to recover slowly, as indicated by Nevada's fiscal year 2021 through 2023 revenue forecasts.

Extent and Duration of Mandatory Shutdowns Affected Revenue Streams

Further, the extent and duration of mandatory shutdowns of businesses and other parts of the states' economies, in response to rising COVID-19 case counts, was another predominant factor that affected some states' revenue sources and unemployment rates.

- In Pennsylvania, the governor issued a series of orders in March 2020 effectively shutting down the physical locations of all "non-life-sustaining businesses," closing schools and universities statewide, and requiring residents to stay at home. During this time, Pennsylvania's unemployment rate increased significantly, from about 5 percent in March 2020 to more than 16 percent in April 2020. Pennsylvania officials said this increase resulted in declines in individual income tax revenues, while the shutdown of businesses and restrictions on residents' activities and travel resulted in lost revenue from sales, fuel, hospitality, and gaming taxes. These officials also told us that projecting revenues has been challenging, given the performance of the economy, which has seen multiple business shutdowns and re-openings due to the pandemic.

[30]Under Nevada state law, "gaming" means to deal, operate, carry on, conduct, maintain, or expose for play any game as defined in the Nevada Revised Statutes section 463.0152, or to operate an inter-casino linked system. Nev. Rev. Stat. § 463.0153 (1995). In addition, Nevada state law contains provisions on monthly, quarterly, and annual state and county gaming taxes and fees. Nev. Rev. Stat. §§ 463.370-463.400.

[31]According to Nevada's Economic Forum, Nevada's gaming percentage fee tax collections made up almost 19 percent of Nevada's general fund revenues in fiscal year 2018. Created by the state legislature, the Economic Forum is responsible for providing forecasts of Nevada's general fund revenues for each biennium budget period.

- In January 2020, prior to the pandemic, Nevada's unemployment rate was 3.6 percent—the lowest on record for the state. After the onset of the pandemic, the governor ordered closures in mid-March of all non-essential businesses, including gaming establishments. According to Nevada officials, the full economic impact of these business closures occurred in April 2020, when Nevada's unemployment rate rose to more than 30 percent.[32]

  The state's gaming establishments in Nevada closed in March 2020 and started to reopen in June 2020. In response to the growing number of COVID-19 case counts nationally and in the state, Nevada placed some restrictions on business activities in November 2020. Those requirements included capacity limits of 25 percent in businesses such as casinos, restaurants, gyms, conventions and trade shows, and entertainment venues. These actions did not fully shut down businesses that were previously allowed to open. Nevada officials said that the capacity limits created uncertainty for Nevada's economy heading into the holiday season.
- Florida officials told us that business closures in March of 2020, as a result of the pandemic, resulted in a loss of 2 million jobs. Florida's unemployment rate increased by more than 10 percent, from 2.8 percent in February to 14.2 percent in May 2020. Florida's real GDP declined by 30.1 percent in the second quarter of 2020 (April through June).

Some Selected States Revised Their Revenue Forecasts Downward for Fiscal Year 2020 and Future Fiscal Years

As a number of states in our review began realizing the effects of the pandemic on their economies, they took steps to revise certain fiscal year revenue projections downward in anticipation of future revenue losses stemming from the pandemic. Michigan, for example, updated its revenue forecast multiple times for fiscal years 2020, 2021, and 2022, as a result of the pandemic. Overall, comparing Michigan's January 2020 revenue forecast to its January 2021 forecast, fiscal year 2020 revenues were revised downward by $164 million, fiscal year 2021 revenues were

[32]In our prior work, we reported that, nationwide, individuals working in the leisure and hospitality sector historically have had the lowest average earnings among sectors and moreover, during the pandemic, have seen the most significant job losses, indicating that many low-wage workers remained out of work as of February 2021. For additional information, see GAO-21-387.

revised $1.2 billion lower than originally anticipated, and fiscal year 2022 revenues are expected to be about $837 million lower than originally forecasted.[33]

Ultimately, some of the selected states' revenues out-performed their revised downward projections for the remainder of fiscal year 2020 and for the first two quarters of fiscal year 2021. For example, according to officials, in May 2020, North Carolina revised its revenue projections considerably downward to account for anticipated fiscal changes due to the pandemic. The state's revised forecast reflected a $4.2 billion reduction in revenues for its 2019-2021 biennium—a $1.6 billion reduction for fiscal year 2019-2020 and a $2.6 billion reduction for fiscal year 2020-2021.

According to North Carolina officials, total state revenue collections out-performed revised projections largely because tax revenue collections were 2.2 percent ($513 million) higher than anticipated in the balance of fiscal year 2020. Officials noted that this was due primarily to unexpected resilience in individual income tax withholding collections and a smaller-than-anticipated decline in sales tax collections.

Sales tax revenues would have fared worse, according to officials, if not for the state's recent policy changes requiring online Internet retailers to collect and remit sales tax on North Carolina purchases. While revenue collections from sales and use taxes and individual income taxes—which accounted for 85 percent of the state's general fund revenues in fiscal year 2020—outperformed the state's revised estimates, each revenue source was 4.7 percent below the state's original 2020 fiscal year target.

In anticipation of revenue losses stemming from the pandemic, Arizona revised its projections for fiscal year 2020 downward in March 2020. State officials told us that the fiscal year 2021 revenues from July through December consistently outperformed the March 2020 revised revenue forecast, but still remained below Arizona's pre-pandemic revenue projections.

[33]Michigan, along with three other states in our review—Arizona, Florida, and Pennsylvania—operates on an annual budget cycle, which means that the budget provides appropriations for 1 fiscal year. The remaining four states in our review—Nevada, New Hampshire, North Carolina, and North Dakota—operate on a biennial budget cycle, which means the budget provides appropriations for 2 fiscal years. Michigan is the only selected state that operates on a fiscal year that runs from October 1 to September 30. The other selected states' fiscal years run from July 1 to June 30.

Similarly, in August 2020, Florida officials told us the state updated its general fund revenue projections for fiscal years 2021 and 2022, including a 10 percent ($3.4 billion) decline for fiscal year 2021 and a 5.6 percent ($2 billion) decline for fiscal year 2022. However, according to state officials, for the September through December time-period, the state collected revenues $1 billion above its revised August projection. Florida officials told us that, in December, the state again updated its fiscal year 2021 revenue forecasts, estimating revenues about $1.5 billion above the revised August projections.

Most Selected States Increased State Expenditures, Particularly on Public Health and Safety

Officials from five states in our review told us that their states saw increased costs associated with public health and safety, such as COVID-19 testing sites, care for vulnerable populations such as additional medical support for nursing homes and correctional facilities, and purchases for personal protective equipment for state and local employees. Some states, such as Arizona and Michigan, also implemented supplemental hazard pay for certain state employees. In Michigan, this included frontline direct care and correctional workers.

For example, officials from North Dakota told us that they expect spending on public health and safety, including COVID-19 testing and vaccine-related expenses, to continue to be significantly higher than usual for the remainder of fiscal year 2021. These additional expenses, according to state officials, required an additional appropriation of $22 million for the state's Department of Health, as part of the state's 2019-2021 biennium budget. As a point of reference, the pre-pandemic budget for the North Dakota Department of Health for fiscal years 2020 and 2021 was $36.3 million.

Most Selected States Took Actions to Address Pandemic-related Changes in Revenues and Expenditures

Most Selected States Took Actions Aimed at Reducing Spending

As a result of reductions in revenues at the onset of the pandemic, six of the eight states in our review took a range of actions to reduce or control spending in some categories. As shown in table 1, six states administered hiring freezes, which took various forms.

- In North Carolina, officials told us state agencies were directed to fill only vacant state government positions that were deemed "mission critical."
- In New Hampshire, the governor ordered a 9-month hiring freeze of all state employee positions in executive branch agencies, with limited exceptions such as positions related to the pandemic response.[34]
- Nevada, in addition to instituting a hiring freeze, enacted 48 hours of unpaid furlough leave for state employees, beginning on January 1, 2021 and ending on June 30, 2021.

[34]New Hampshire's hiring freeze remained in effect from the end of April 2020 through the beginning of February 2021.

Table 1: Selected State Actions to Reduce Spending in Response to the Pandemic

State	Hiring freezes	Furloughs	Discretionary spending freezes and other spending reductions
Arizona	no	no	no
Florida	yes	no	yes
Michigan	yes	no	yes
Nevada	yes	yes	yes
New Hampshire	yes	no	no
North Carolina	yes	no	yes
North Dakota	no	no	no
Pennsylvania	yes	no	yes

Source: GAO analysis of state budget documents and interviews with state officials. I GAO-21-562

Five states imposed freezes on discretionary spending and reduced spending in other areas to respond to declines in state revenues. For example,

- According to officials, Nevada reduced the state's capital improvement funding, such as cancelling renovations for several college and museum buildings and a planned project to upgrade surveillance at a state prison. The state also decreased higher education funding by 19.8 percent and reduced provider rates for Medicaid.
- In Florida, the governor used his line-item veto authority to reduce about $1 billion in spending from the state's approved fiscal year 2021 budget.[35] Specifically, in addition to spending reductions to higher education, the line-item vetoes included, among other things, reductions in spending for public works and affordable housing projects. Florida officials also told us that the governor issued an order for its state agencies to hold back 6 percent of their fiscal year 2021 budget, while state agencies were instructed to identify an additional 2.5 percent in reductions in fiscal year 2021 and 10 percent in spending reductions for fiscal year 2022.
- In Michigan, officials told us that the state had reduced state spending in a number of areas, including schools, universities, and community

[35]In Florida, line-item veto authority refers to the ability of the governor to veto any specific appropriation in a general appropriations bill, but may not veto any qualification or restriction without also vetoing the appropriation to which it relates. Fla. Const., art. III, § 8. According to NASBO, 43 states have reported that their governors have this authority.

colleges; revenue sharing with localities; and the state's judiciary budget. In addition, according to officials from Pennsylvania and North Carolina, both states established provisions to freeze or reduce non-essential spending.

Officials from North Dakota told us that the state has not taken any actions to reduce current biennium spending or services as a result of COVID-19, which they attributed primarily to two issues. First, actual revenues were exceeding the state's legislative revenue forecast by a considerable margin prior to the pandemic, which resulted in a cushion for state revenues. This cushion helped the state absorb some of the initial shortfall from the pandemic. Second, revenue from oil taxes collected in the current biennium is primarily budgeted for and spent in the subsequent biennium. As a consequence, although oil and gas taxes experienced a significant shortfall, officials told us its impact will primarily be felt during the 2021-2023 budget period. However, North Dakota state agencies have been informed that they should expect spending reductions in future budget cycles, with larger agencies needing to anticipate a 15 percent reduction, and smaller agencies a 5 to 10 percent reduction.

Half of the Selected States Used Reserve Funds to Help Balance Their Budgets

Prior to the pandemic, many states had leveraged a long-term economic recovery and growing tax revenues to replenish their rainy day funds—which rose to unprecedented levels for many states.[36] At the time of our review, four of the eight selected states—Arizona, Michigan, Nevada, and Pennsylvania—used all or part of the state's rainy day or budget stabilization funds to help pay for budget needs such as pandemic-related expenses, closing a budget gap, and offsetting revenue losses.[37] For example,

[36]As we mentioned earlier in this report, state rainy day fund balances have increased significantly over the past 20 years.

[37]According to NASBO, with the exception of Vermont, 49 states must balance their budgets.

- State officials told us Arizona used $55 million from its $954 million budget stabilization fund for one-time public health expenses and did not expect to use additional reserve funds moving forward.[38]
- Nevada transferred its entire balance of $401 million from its rainy day fund to its general revenue fund to help close a budget gap for fiscal year 2020.
- Pennsylvania officials told us the state used $100 million of its $340 million in reserve funds to balance its fiscal year 2021 budget.
- According to officials, Michigan used $350 million from its rainy day fund for its fiscal year 2020 budget and plans to replace $210 million of that amount during the fiscal year 2021 budget cycle. Prior to the pandemic, Michigan's rainy day fund balance reflected a 20-year high, with a balance of $1.2 billion.

At the time of our review, budget officials from the remaining four states—Florida, New Hampshire, North Carolina, and North Dakota—told us they had not used any portion of their rainy day funds in fiscal year 2020 to cover costs from the pandemic and North Carolina and North Dakota did not expect to do so for fiscal year 2021.

Officials from Most of the Eight Selected States Reported No Increases in Taxes or Fees in Proposed Budgets

Officials from four of the eight states in our review told us that the states' proposed budgets for fiscal year 2021 would not include an increase in state taxes or the adoption of new taxes as a way to generate revenue. Florida officials said this was the case for the state's proposed budget for fiscal year 2022. Officials from two states—Nevada and North Carolina—told us their state legislature had taken various actions to increase revenues.

- In Nevada, as part of a special legislative session for the state's 2021 budget, the state legislature passed temporary measures to increase state revenues, including a tax amnesty program from February 1, 2021 to April 30, 2021. Specifically, the program waives penalties and

[38]Arizona's reported budget stabilization fund balance is as of January 2021.

interest for businesses and individuals who have unpaid taxes prior to the start of the program.[39]

- In North Carolina, the legislature placed a “floor” on the state’s fuel tax to prevent the formula-driven rate from dropping below a certain level for the duration of fiscal year 2021. The temporary fuel tax floor will prevent the tax rate in 2021 from falling below the 2020 rate (36.1 cents per gallon), as it would have done automatically due to the tax rate being indexed in part to energy inflation.[40] According to North Carolina officials, the state estimated that this change would increase motor fuel tax revenues in the state by $20.2 million in fiscal year 2021 and by $33.4 million in fiscal year 2022.

Most Selected States Cited Federal Assistance as a Factor That Helped Bolster Capacity to Implement Federal Programs

Officials representing five of the eight states—Arizona, Florida, Michigan, Nevada, and New Hampshire, and Arizona—told us that the federal assistance they received, including the CRF, helped bolster their state’s capacity to implement federal programs, as a result of increases in demand for services due to COVID-19.[41] Specifically, these officials told us the states used the CRF to assist with the operation of new and existing assistance programs to support CARES Act or other programs. Three of the five states used CRF funds to help process the increased

[39]Under the program, the tax debt must be paid in full to take advantage of the waiver of penalty and interest.

[40]The fuel tax is indexed to a weighted average of energy inflation and state population growth.

[41]As we discuss in greater detail in appendix I, for purposes of this report, we refer to capacity as both the maintenance of appropriate resources and the ability to effectively manage and utilize those resources.

volume of unemployment claims experienced by the states in the wake of the pandemic.[42]

- According to Florida officials, CRF funding helped the state avoid large layoffs of state government employees as well as the termination of some state programs. For example, using CRF funds, Florida was able to maintain its current level of operations by repurposing existing staff to call centers. These staff helped manage the significant increase in federal assistance applications the state received for programs such as the Temporary Assistance for Needy Families and the Supplemental Nutrition Assistance Program.

  Florida also used CRF funds to bolster its capacity and enhance the state's operations by repurposing hundreds of state employees to help process the state's surge in unemployment claims. Based on data from the Department of Labor, the state received almost 4.8 million unemployment insurance claims between mid-March 2020 and mid-May 2021.
- In Michigan, the state used CRF funds to establish a project management office (PMO) within the state's budget office. The PMO assists state agencies distributing CARES Act funds, including the CRF. The PMO also helps state agencies administer, control, report on, and comply with federal regulations and guidance through the end of the CRF reporting period. In addition to assisting with CRF funding, the PMO is also building the state's capacity to manage other CARES Act programs, such as grants for local governments and a program that provides hazard pay for first responders.

  Michigan experienced a surge in unemployment claims at the onset of the pandemic, with nearly 2.2 million unemployment insurance initial claims filed in the state between mid-March through mid-May of 2020, according to state officials. Michigan officials told us that its unemployment system was not designed to manage such significant increases in unemployment insurance claims and that the state

[42]We also recently reported that the unprecedented volume of new unemployment insurance (UI) claims in the wake of the pandemic posed major challenges for state officials to provide benefits, help with re-employment, and identify and prevent improper payments. At the onset of the pandemic, from March 21 to May 30, 2020, initial UI claims surpassed 42 million—compared to 5.1 million beneficiaries in all of fiscal year 2019—according to data provided by the Department of Labor. At the same time, states were also implementing three new, federally funded programs created by the CARES Act that expand UI eligibility and benefits. For additional information, see GAO-20-625 and GAO-21-387.

needed to add both state employees and outside contractors to support its claims system.

- Nevada also experienced an unprecedented surge in unemployment claims as a result of pandemic-related business closures. The state's unemployment rate increased from 6.4 percent in March 2020 to 29.5 percent the following month. The sudden increase in applications for unemployment benefits represented a 1,400 percent increase in workload for the state agency responsible for processing Nevada's unemployment insurance claims. According to state officials, to help manage the influx of claims, Nevada used its CRF funding to establish a call center with more than 200 positions to respond to calls from those seeking assistance in applying for unemployment benefits. In addition, the state reassigned some state employees to help process the surge in unemployment claims. These efforts helped Nevada address the increase in workload and the resulting backlog of claims for unemployment benefits.
- New Hampshire established the Governor's Office for Economic Recovery and Relief to respond to the COVID-19 pandemic and, according to officials, manage the $1.25 billion the state received in CRF funds. The state staffed the office by repurposing employees from other state agencies. New Hampshire officials told us that, in addition to CRF funding, the state received pandemic-related federal assistance for various programs administered by the state, such as increases in the Federal Medical Assistance Percentage (FMAP) under the Medicaid program.[43] They said that, taken together, these funding sources helped supplement the state's capacity to implement federal programs. Officials also told us that while any changes in the state's capacity to implement federal programs have been minimal, the ongoing audit and reporting requirements associated with CRF funds presented challenges for the state.
- Following the onset of the COVID-19 pandemic, Arizona established an Economic Recovery Management Team to manage state and federal resources allocated to respond to the pandemic. According to state officials, the $1.86 billion the state received in CRF funds helped it respond to the pandemic in a number of different areas including, public health, education, distance learning, and small business support. These officials said that CRF funding allowed state agencies to use less of their appropriated funds and return those funds to the

[43]FFCRA provided a temporary increase in the FMAP for all qualifying states and territories through the end of the quarter in which the public health emergency, including any extensions, ends. Pub. L. No. 116-127, § 6008, at 208-09. For additional information see, GAO-21-387.

state's general fund. Officials said that other federal actions have also helped Arizona, including the more than $545 million in increased FMAP funding. This additional funding allowed Arizona to free up state budget capacity and stabilize health program funding.

Officials from the remaining three states—North Carolina, North Dakota, and Pennsylvania—told us that the pandemic had not affected their capacity to implement federal programs.

We provided excerpts of the draft report to state budget officials in the selected eight states we included in our review. We incorporated their technical comments as appropriate.

We are sending copies of this report to the appropriate congressional committees and other interested parties. In addition, the report will be available at no charge on the GAO website at http://www.gao.gov.

If you or your staff members have any questions about this report, please contact me at (202) 512-6806 or sagerm@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix II.

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The Honorable Richard Shelby
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United States Senate

The Honorable Ron Wyden
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Appendix I: Objectives, Scope, and Methodology

This report examines the fiscal conditions of state and local governments resulting from the Coronavirus Disease 2019 (COVID-19) pandemic. Specifically, the objectives of our review were to examine: (1) what is known about changes in revenues and expenditures for the state and local government sector since the onset of the pandemic, (2) how revenues and expenditures have changed since the onset of the pandemic in selected states, (3) what actions selected states have taken to address changes in revenues and expenditures, and (4) factors that have affected the selected states' capacity to implement federal programs.

To describe what is known about changes in revenues and expenditures for the state and local government sector, we analyzed data on states' and localities' revenues from the U.S. Census Bureau (Bureau) and expenditures from the Bureau of Economic Analysis's (BEA) National Income and Product Accounts (NIPA) for 2019 and 2020. Specifically, we analyzed seasonally-adjusted aggregate data from the Bureau's Quarterly Summary of State and Local Government Tax Revenue to compare changes in select categories of tax revenues collected from quarter to quarter for 2019 to 2020. We used the Bureau's four categories of tax data as part of our analysis, which included the following four categories of own-source revenue: (1) sales; (2) property; (3) corporate income; and (4) individual income. The Bureau's data that we analyzed did not include all types of own-source revenue, such as excise taxes or user fees, or other types of revenue, such as federal grants to state and local governments, including COVID-19 pandemic-related funding.

We also analyzed seasonally-adjusted aggregate state and local expenditure data from BEA's NIPA Table 3.3 for 2019 and 2020. We determined that the NIPA data were the most recent available data for the purpose of examining aggregate state and local government expenditures. The NIPA data do not always match state and local government budget data due to methodological differences between how BEA calculates NIPA data and how state and local governments compute their budget data. For purposes of this review, we determined that the BEA NIPA data and Bureau data were sufficiently reliable for our analysis of state and local government revenues and expenditures.

Our data reliability assessment included reviewing relevant documentation and the data to identify obvious errors or outliers. We also reviewed our prior reports and those of other organizations examining state and local government revenues and expenditures since the onset of COVID-19.

To identify how selected states' revenues and expenditures have changed since the onset of the pandemic, what actions they have taken to address these changes, and the factors that affected the selected states' capacity to implement federal programs, we interviewed budget officials in eight states.[1] Those states included:

- Arizona
- Florida
- Michigan
- Nevada
- New Hampshire
- North Carolina
- North Dakota
- Pennsylvania

Combined, these states represent about 20 percent of the U.S. population. We selected those states based on a number of factors.[2]

[1]For purposes of this report, we refer to capacity as both the maintenance of appropriate resources and the ability to effectively manage and utilize those resources. In our prior work, we identified several different types of capacity: organizational (i.e. the degree to which an organization is institutionally prepared for grant management and implementation, including its ability to employ technology for grant oversight and reporting); human capital (i.e. the extent of sufficient staff with the knowledge and technical skills needed to effectively meet its goals and objectives); and financial (i.e. the extent of an organization's ability to meet financial responsibilities related to federal grants, such as matching requirements). For additional information on discussions of capacity, see GAO, *Municipalities in Fiscal Crisis: Federal Agencies Monitored Grants and Assisted Grantees, but More Could Be Done to Share Lessons Learned*, GAO-15-222 (Washington, D.C.: Mar. 20, 2015), and *Grants to State and Local Governments: An Overview of Federal Funding Levels and Selected Challenges,* GAO-12-1016 (Washington, D.C.: Sept. 25, 2012).

[2]For purposes of this report, we did not include tribal governments in the scope of our work as GAO has ongoing work examining the federal response to tribes in the context of the COVID-19 pandemic. For the most recent report, see GAO, *COVID-19: Sustained Federal Action Is Crucial as Pandemic Enters Its Second Year*, GAO-21-387 (Washington, D.C.: Mar. 31, 2021).

First, we obtained data from the Centers for Disease Control and Prevention on the number of reported COVID-19 cases per 100,000 population in each state as of October 19, 2020. We then grouped the states according to low, medium, and high, based on the number of COVID-19 cases per 100,000 population. We also calculated the amount of Coronavirus Relief Fund (CRF) payments that the Department of the Treasury (Treasury) allocated to each state on a per capita basis. That is, we divided the amount of Treasury's allocation of funding for each state by the Bureau's population estimate for each state as of July 1, 2019. We grouped the states according to high, medium, and low CRF allocation per capita. We also used Bureau data on state government tax revenues to identify the predominant revenue source in each state.

Further, using Bureau of Labor Statistics data on percent changes in employment rates for each state between August 2019 and August 2020, we grouped the states according to low-, medium-, and high-percentage changes in unemployment. We also considered the political affiliation of governors in each state, based on categories identified by the National Governors Association, and used the Bureau's division of regions to achieve geographic diversity. Table 2 provides additional detail on the characteristics of the eight states selected for our review.

Table 2: Characteristics of Eight States Selected for Our Review

State	Range in reported COVID-19 cases per 100,000[a]	Range in amount of Coronavirus Relief Fund allocation per capita[b]	Predominant tax revenue source (2019)[c]	Range in year to year percent change in U.S. unemployment[d]	Governor's political affiliation[e]	Census region[f]
Arizona	High	Low	General Sales	Low	Republican	West
Florida	High	Low	General Sales	Medium	Republican	South
Michigan	Low	Low	Individual Income	Medium	Democrat	Midwest
Nevada	Medium	Medium	General Sales	High	Democrat	West
New Hampshire	Low	Medium	Corporation Net Income	Medium	Republican	Northeast
North Carolina	Medium	Low	Individual Income	Low	Democrat	South
North Dakota	High	High	Severance	Low	Republican	Midwest
Pennsylvania	Low	Low	Individual Income	High	Democrat	Northeast

Source: GAO analysis of data from the Centers for Disease Control and Prevention (CDC), U.S. Department of the Treasury (Treasury), Census Bureau, U.S. Bureau of Labor Statistics, and National Governor's Association.

[a]Based on CDC data as of October 19, 2020. According to CDC, case counts include both confirmed and probable cases. For the purposes of this analysis, we grouped the eight states according to low (0 – 1,999), medium (2,000 – 2,999), and high (3,000+) COVID cases per 100,000 individuals, based on each state's COVID cases per 100,000 population.

[b]Represents the maximum allocation of Coronavirus Relief Fund (CRF) payments to states on a per capita basis, based on the fund allocations provided through Treasury. For the purposes of this analysis, we grouped the eight states according to low ($0 - $387.76), medium ($387.77 - $999.99), and high ($1,000+) CRF fund allocation.

[c]Represents the predominant tax revenue source in the state in calendar year 2019.

[d]Based on unemployment changes from August 2019 to August 2020. For the purposes of this analysis, we grouped the eight states according to low (0 – 2.9), medium (3 – 4.9), and high (5+) percentage point changes in unemployment.

[e]Represents the political affiliation of the state governor.

[f]Based on one of four Census Bureau-designated regions, which include Northeast (region 1); Midwest (region 2); South (region 3); and West (region 4).

We then developed and administered a semi-structured interview to state budget officials in the eight selected states regarding how revenues and expenditures in the state have changed since the onset of the pandemic, what actions the states have taken to address these changes, and what factors affected the selected states' capacity to implement federal programs. We also obtained and analyzed state budget and other relevant documents to identify selected states' actual and projected revenues and expenditures for 2020 and 2021, as well as actual or estimated use of reserve funds for 2020. In addition, we obtained documentation related to what actions selected states have taken, or planned to take, in response to revenue declines and spending increases resulting from the pandemic, actions selected states have taken or planned to take to increase revenues, and the amount of federal assistance through the CRF that states have used.

We use the terms “a number of,” “some,” “a majority of” and “most” to characterize the number of states that were similarly situated for a particular issue. Specifically, we defined “a number of” or “some” to characterize two or three states and “a majority of” or “most” as five or more states. The results of our study are not generalizable to all states.

As part of our objective to identify how state revenues changed for the selected eight states after the onset of the pandemic, we also analyzed aggregate data from the Bureau's Quarterly Summary of State and Local Government Tax Revenue, Table 3: State Government Tax Collections by State and Type of Tax. We used these data to examine the percent change in selected state government own-source tax revenue collected in 2020 compared to the same quarter in 2019. The Bureau's Table 3 consists of state government tax data made up of the following five categories of own-source tax revenue: (1) property taxes; (2) sales and gross receipts taxes; (3) license taxes; (4) income taxes; and (5) other taxes.[3] The data in the Bureau's Table 3 do not include funding from federal grants to state and local governments, including COVID-19 pandemic-related funding.

To provide context for and supplement our understanding of changes in the state and local government sector's revenues and expenditures since the onset of the pandemic, we met with a number of associations that represent state and local governments. Those included: the Council of State Governments; National Association of Counties; National Association of State Auditors, Comptrollers, and Treasurers; National Association of State Budget Officers; National Conference of State Legislatures; National Governors Association; National Association of State Treasurers; Government Finance Officers Association; and National League of Cities. Furthermore, we interviewed representatives from credit rating agencies—Fitch Ratings, Moody's Analytics, and S&P Global Ratings—to gain insight on the fiscal impacts of the pandemic on states' and localities' economies. The results of these interviews are not generalizable to the entire state and local government sector.

We conducted this performance audit from August 2020 to July 2021 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

[3]The Bureau's "other taxes" category includes: (1) death and gift; (2) severance; (3) documentary and stock transfer; and (4) other taxes not elsewhere classified.

Appendix II: GAO Contact and Staff Acknowledgments

GAO Contact

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Staff Acknowledgments

In addition to the contact named above, Brenda Rabinowitz (Assistant Director), Anthony Bova (Analyst-in-Charge), and Wade Tanner made key contributions to this report. Ann Czapiewski, Samantha Lalisan, and Farrah Stone also provided support.

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