

STATE FISCAL BRIEF

Fiscal Studies Program
The Nelson A. Rockefeller Institute of Government

May 2003
No. 67

A Bad Year: Fiscal Year 2002 Tax Revenue Summary

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Highlights

- ❖ State tax revenue declined by 5.6 percent in fiscal year 2002.
- ❖ Adjusted for legislated tax changes and inflation, the revenue decline was 7.7 percent — the worst decline in over a decade.
- ❖ Net tax increases amounted to \$1.5 billion in fiscal year 2002. The largest increase was in Minnesota, which discontinued a rebate and added a new property tax.
- ❖ The steep tax revenue declines in fiscal year 2002 have created major headaches in state capitals across the country as lawmakers struggle to balance their fiscal year 2003 and 2004 budgets.

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Introduction

State general fund tax revenue declined by 5.6 percent from fiscal year 2001 to fiscal year 2002. This is the largest decline since the Rockefeller Institute of Government began to track state revenue in 1991. (See Table 1.) Adjusting for the effects of legislated tax changes brings the state revenue decline to 6.0 percent. When we also include the effect of inflation, the decline is 7.7 percent. As Table 2 shows, in fiscal year 2002 personal and corporate income tax revenue declined 10.8 and 18.8 percent, respectively, while sales tax revenue grew only weakly.

This report uses the final revenue figures for all states.¹ It also uses the states' own fiscal years. For most states these end June 30, but for some they go as late as the end of September. We present year-over-year growth or decline in revenue for each state, before and after adjusting for the effects of legislated tax changes. For more details on the methodology employed, please see the box titled "Technical Notes."

Tax Revenue Growth

Table 3 shows for each state the year-over-year percentage change in state tax revenue by major tax from fiscal year 2001 to fiscal year 2002. Revenue was not only down on a year-over-year basis, it was also well

short of what states had originally estimated in their fiscal year 2002 budgets. According to a survey by the National Governors' Association and the National Association of State Budget Officers, states collected over \$38 billion less in personal income, corporate income, and sales tax revenue than they had originally budgeted.² In all, forty-one states had lower tax revenue than they had projected for their fiscal year 2002 budgets. This opened huge gaps in their budgets, which many are still struggling to close.

The massive revenue decline in fiscal year 2002 was the result of the recession that started after March 2001 and stretched through at least part of the 2002 fiscal year. The impact of this recession on revenue was the strongest in places such as California and many states in New England and the Mid-Atlantic that generate substantial revenue from investment-related income. However, by the end of the fiscal year revenue was in decline throughout most of the country.³

Personal income tax revenue declined by 10.8 percent for the fiscal year. This was a dramatic reversal from 7.5 percent growth in fiscal year 2001. (See Figure 2.) Nine states had double-digit percentage personal income tax revenue declines in fiscal year 2002.⁴ Five of these states — California, Connecticut, New Jersey, Rhode Island, and Vermont — also had double-digit percentage personal income tax growth in fiscal year

Table 1.
Percentage Growth or Decline in Fiscal Year Tax Revenue,
Adjusted for Legislated Tax Changes and Inflation

<i>Fiscal Year</i>	<i>Total Nominal Growth or Decline</i>	<i>Adjusted Nominal Growth or Decline</i>	<i>Inflation Rate</i>	<i>Adjusted Real Growth or Decline</i>
1992	7.2%	1.7%	3.2%	(1.5)%
1993	5.7	5.2	3.1	2.0
1994	6.0	5.5	2.6	2.8
1995	7.0	6.1	2.8	3.2
1996	5.4	6.3	2.7	3.5
1997	6.2	7.6	2.8	4.6
1998	6.9	8.3	1.8	6.4
1999	5.7	7.4	1.7	5.6
2000	8.7	9.4	2.9	6.3
2001	4.7	6.0	3.4	2.5
2002	(5.6)	(6.0)	1.8	(7.7)

Note: Inflation is measured by the Consumer Price Index

**Table 2.
Year-Over-Year Percentage Growth or Decline in State Tax Revenue by Major Tax**

<i>Fiscal Year</i>	<i>PIT</i>	<i>CIT</i>	<i>Sales Tax</i>	<i>Total</i>
1996	7.7%	1.4%	5.5%	5.4%
1997	8.1	5.4	5.2	6.2
1998	11.2	1.0	5.6	6.9
1999	8.1	0.7	6.2	5.7
2000	12.4	4.0	7.3	8.7
2001	7.5	(6.9)	3.2	4.7
2002	(10.8)	(18.8)	0.6	(5.6)

2001. Only five states — Louisiana, New Mexico, Ohio, Oklahoma, and West Virginia — had personal income tax revenue growth in 2002, and in two of these — New Mexico and Ohio — the increases were partially or entirely due to tax increases or processing changes.

Sales tax grew by only 0.6 percent in fiscal year 2002, down from 3.2 percent the year before. Even this lukewarm growth made the sales tax the strongest performing of the major state taxes. Only one state — Arizona — had double-digit growth, the result of a tax increase. In 15 states sales tax collections declined.

Corporate income tax revenue declined by 18.8 percent, on top of a 7.0 percent decline in fiscal year 2001. Only five of the 45 states with a corporate income tax had an increase in collections.

Tax Changes

States implemented over \$1.5 billion in net tax increases in fiscal year 2002. Table 4 illustrates the effects of legislated tax changes on state tax revenue collections. The adjusted revenue growth numbers provide an estimate of each state's underlying tax revenue growth

**Figure 1.
Annual Nominal and Real Year-Over-Year State Tax Revenue Growth,
Adjusted for Legislation**

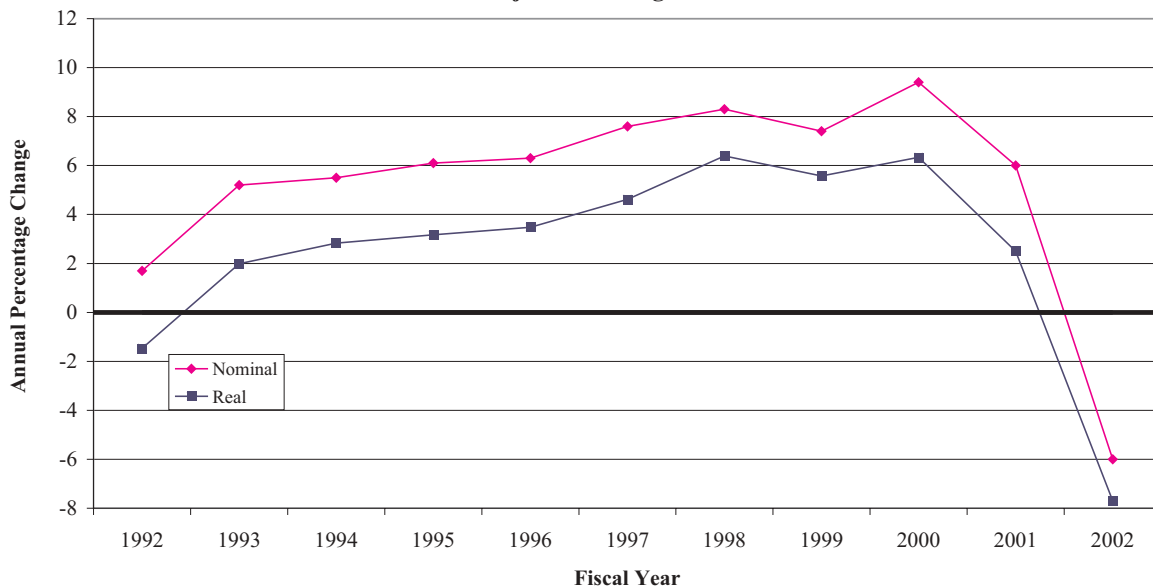


Table 3. Percentage Increase or Decline in Tax Revenue, Fiscal Year 2001 to Fiscal Year 2002

	<i>PIT</i>	<i>CIT</i>	<i>Sales</i>	<i>Total</i>
United States	(10.8)%	(18.8)%	0.6%	(5.6)%
New England	(17.2)	(40.3)	(1.3)	(11.3)
Connecticut	(13.7)	(58.2)	3.5	(11.0)
Maine	(8.4)	(19.5)	2.2	(2.8)
Massachusetts	(20.1)	(37.9)	1.6	(14.6)
New Hampshire	NA	(18.6)	NA	5.6
Rhode Island	(12.4)	(76.9)	5.0	(6.1)
Vermont	(16.6)	(36.7)	(0.2)	(9.7)
Mid-Atlantic	(5.7)	(16.5)	0.8	(3.9)
Delaware	(0.6)	115.2	NA	4.2
Maryland	(6.5)	(26.6)	0.5	(4.6)
New Jersey	(14.4)	(15.7)	4.2	(6.0)
New York	(3.3)	(20.2)	(1.9)	(3.9)
Pennsylvania	(4.7)	(11.5)	1.2	(2.6)
Great Lakes	(4.9)	(12.8)	1.7	(2.2)
Illinois	(6.1)	(18.5)	1.6	(3.7)
Indiana	(6.3)	(17.1)	2.0	(3.8)
Michigan	(8.8)	(5.2)	1.2	(1.5)
Ohio	0.6	(22.2)	1.7	(1.1)
Wisconsin	(4.2)	(5.8)	3.0	(0.7)
Plains	(5.4)	(18.8)	(0.7)	(0.3)
Iowa	(2.2)	(22.4)	0.0	(2.4)
Kansas	(7.5)	(55.6)	2.7	(6.1)
Minnesota	(8.0)	(27.4)	(3.4)	4.0
Missouri	(2.7)	22.7	0.7	(0.9)
Nebraska	(6.0)	(22.0)	1.5	(3.7)
North Dakota	(2.9)	(14.2)	(1.6)	(4.3)
South Dakota	NA	NA	1.3	(0.3)
Southeast	(4.2)	(10.6)	1.8	(1.1)
Alabama	(1.5)	68.8	2.1	2.2
Arkansas	(0.8)	(6.8)	0.9	(0.6)
Florida	NA	(9.4)	1.4	0.8
Georgia	(6.3)	(18.8)	(1.8)	(4.7)
Kentucky	(2.7)	(28.5)	3.2	(0.8)
Louisiana	2.6	(1.7)	(0.2)	1.5
Mississippi	(3.8)	(6.3)	1.8	(0.5)
North Carolina	(3.4)	5.0	7.9	(0.4)
South Carolina	(6.0)	(32.9)	1.3	(3.1)
Tennessee	NA	(25.3)	(0.2)	(2.5)
Virginia	(7.1)	(20.2)	6.9	(3.9)
West Virginia	1.7	(22.7)	3.6	3.8
Southwest	(1.6)	(28.9)	1.5	(2.8)
Arizona	(9.3)	(36.0)	15.3	1.0
New Mexico	13.4	35.5	1.8	(1.1)
Oklahoma	0.3	4.5	(0.4)	(5.1)
Texas	NA	NA	(0.7)	(3.4)
Rocky Mountain	(10.9)	(37.0)	(0.2)	(7.1)
Colorado	(11.8)	(37.4)	(2.5)	(10.1)
Idaho	(18.3)	(45.9)	1.6	(10.2)
Montana	(6.1)	(31.9)	NA	2.3
Utah	(6.0)	(32.0)	0.7	(3.8)
Wyoming	NA	NA	5.7	(2.2)
Far West	(24.5)	(23.5)	(1.9)	(15.3)
Alaska	NA	(13.9)	NA	(28.1)
California	(25.6)	(22.2)	(2.5)	(17.6)
Hawaii	(3.0)	(25.2)	(1.7)	(3.5)
Nevada	NA	NA	1.3	1.5
Oregon	(19.2)	(47.7)	NA	(20.3)
Washington	NA	NA	(0.7)	(1.5)

Technical Notes

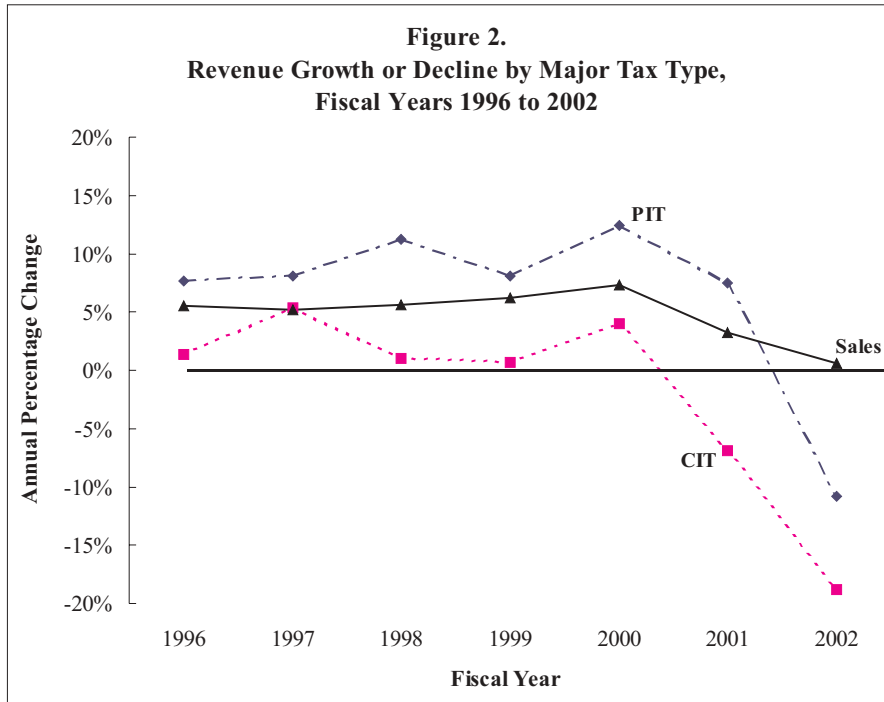
The estimates of “legislated changes” include the effects of changes in tax rates and tax bases and acceleration of tax payments. They also include a very few major non-legislated changes, such as adjustments for changes to the accounting system or for particularly egregious delays in processing of receipts.

We developed the estimated effects of legislated changes in several ways. The starting point is a survey of legislated tax changes published by the National Conference of State Legislatures. We modify the estimates reported by NCSL to take account of differences in the timing of the receipt of revenue. For example, when the sales tax rate is changed, revenue is not usually affected until a month after the effective date of the legislation because businesses are allowed to retain revenue for a few weeks before remitting it to the state. Likewise, if a tax cut took effect in January 2001 and continued throughout fiscal year 2002, part of its effect occurred in fiscal year 2001 and part in fiscal year 2002.

The estimates reported by NCSL are the ones used at the time legislation was enacted. In some cases, states rely on estimates that are too optimistic or pessimistic. For example, a state might anticipate that a sales tax increase would generate an extra \$300 million based on the assumption of strong retail sales. If sales are lower than assumed, the tax increase will produce less than that. The Nelson A. Rockefeller Institute of Government modifies the NCSL-reported estimates with the assistance of revenue estimators after revenue is collected.

Reports on state tax revenue published by the Rockefeller Institute of Government do not cover 100 percent of the taxes collected by states. They use the broadest measure of revenue reported on a timely basis in a single report, but often do not include earmarked taxes like those on motor fuels or taxes collected by agencies other than the revenue department, such as insurance taxes in many states. Various other adjustments are made to revenue to make it as comparable as possible. For more information, please contact the Institute’s Fiscal Studies Program.

In 46 states, Fiscal 2002 was from July 1, 2001 to June 30, 2002. Four states have different fiscal years: Alabama (October 1, 2001 to September 30, 2002), Michigan (same), New York (April 1, 2001 to March 30, 2002) and Texas (September 1, 2001 to August 30, 2002).



Five other states — Arizona, New Hampshire, New Jersey, New Mexico, and North Carolina — had tax hikes that increased growth (or lessened the decline) by more than three percentage points.

The largest tax cut, measured as its effect on general fund revenue growth, was in Oregon, where revenue was depressed by a further 7.8 percentage points over and above the effects of the recession. The cut, amounting to almost \$400 million, resulted largely from a personal income tax rebate. Two other states — Hawaii and Idaho — made cuts reducing growth (or increasing the decline) by over three percentage points.

or decline. The fiscal year 2002 tax increases moderated the decline in state tax revenue by about 0.2 percentage points, meaning that the underlying decline was 5.8 percent.

Even as the recession was taking a bite out of many states' revenue, some states continued to implement tax cuts. While 22 states had tax increases, 21 others had tax cuts. The net change was actually very small compared to previous years.

Largest Changes

Of all the regions, the Plains states had the largest tax increase. The extra \$1.0 billion collected there reduced the year-over-year decline in revenue collections by 3.3 percentage points. Virtually all of this was due to tax increases in Minnesota, which are discussed below. On the other hand, the Far West region cut taxes by almost \$700 million. The Rocky Mountain states had the largest tax cuts in percentage terms; their cuts increased the revenue decline there by 1.4 percentage points.

Among the states, the largest tax increase was in Minnesota, where a new property tax and the end of a sales tax rebate increased tax revenue growth by 9.0 percentage points, or over \$1 billion. Without these increases, Minnesota would have had a 5.0 percent revenue decline instead of 4.0 percent revenue growth.

Conclusions

The sharp decline in state tax revenue in fiscal year 2002 was unprecedented in the dozen years that the Rockefeller Institute of Government has tracked state taxes. States that had become used to revenue growth — often very strong — have had to contend with declines. This has created a monumental challenge in balancing state budgets. While states are projecting some net growth in revenue over the next fiscal year, it will be some time before states make up the revenue decline of fiscal year 2002.

Endnotes

- 1 This may not include all accruals for all states.
- 2 National Governors' Association and National Association of State Budget Officers, *Fiscal Survey of the States, November 2002* (Washington, DC, 2002). This survey did not include data from Florida.
- 3 See Nicholas W. Jenny, "Severe Decline in State Tax Revenue," *State Revenue Report No. 46*, December 2001; "A Second Quarter of Decline in State Tax Revenues," *State Revenue Report No. 47*, March 2002;
- 4 California, Colorado, Connecticut, Idaho, Massachusetts, New Jersey, Oregon, Rhode Island, and Vermont.

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Table 4. Effect of Legislation on FY 2002 Revenue Growth or Decline				
	<i>Year-Over-Year Revenue Growth or Decline</i>			
	<i>Amount of Tax Change (millions of dollars)</i>	<i>Actual Collections</i>	<i>Adjusted for Tax Changes</i>	<i>Effect of Tax Changes</i>
United States	\$1,538	(5.6)%	(6.0)%	0.3%
New England	(259)	(11.3)	(10.5)	(0.8)
Connecticut	(224)	(11.0)	(8.3)	(2.6)
Maine	19	(2.8)	(3.6)	0.8
Massachusetts	(160)	(14.6)	(13.7)	(1.0)
New Hampshire	85	5.6	(1.9)	7.6
Rhode Island	21	(6.1)	(7.1)	1.0
Vermont	1	(9.7)	(9.8)	0.1
Mid-Atlantic	(112)	(3.9)	(3.8)	(0.1)
Delaware	0	4.2	4.2	0.0
Maryland	(95)	(4.6)	(3.5)	(1.1)
New Jersey	556	(6.0)	(9.2)	3.1
New York	(374)	(3.9)	(3.0)	(0.9)
Pennsylvania	(200)	(2.6)	(1.6)	(1.0)
Great Lakes	389	(2.2)	(2.7)	0.5
Illinois	175	(3.7)	(4.6)	(0.9)
Indiana	7	(3.8)	(3.9)	0.1
Michigan	(188)	(1.5)	(0.6)	(0.9)
Ohio	354	(1.1)	(3.4)	2.3
Wisconsin	41	(0.7)	(1.2)	0.5
Plains	1,040	(0.3)	(3.6)	3.3
Iowa	(1)	(2.4)	(2.4)	0.0
Kansas	26	(6.1)	(6.7)	0.6
Minnesota	1,030	4.0	(5.0)	9.0
Missouri	0	(0.9)	(0.9)	0.0
Nebraska	(2)	(3.7)	(3.7)	(0.1)
North Dakota	0	(4.3)	(4.3)	0.0
South Dakota	(13)	(0.3)	1.7	(2.0)
Southeast	973	(1.1)	(2.1)	1.0
Alabama	48	2.2	1.4	0.8
Arkansas	48	2.2	1.4	0.8
Florida	(30)	0.8	1.0	(0.2)
Georgia	(5)	(4.7)	(4.6)	0.0
Kentucky	35	(0.8)	(1.3)	0.5
Louisiana	19	1.5	1.1	0.3
Mississippi	2	(0.5)	(0.6)	0.0
North Carolina	631	(0.4)	(5.3)	4.9
South Carolina	20	(3.1)	(3.5)	0.4
Tennessee	0	(2.5)	(2.5)	0.0
Virginia	150	(3.9)	(5.3)	1.4
West Virginia	(5)	3.8	3.9	(0.2)
Southwest	398	(2.8)	(3.7)	0.9
Arizona	386	1.0	(5.3)	6.2
New Mexico	102	(1.1)	(4.4)	3.3
Oklahoma	(16)	(5.1)	(4.8)	(0.3)
Texas	(74)	(3.4)	(3.1)	(0.2)
Rocky Mountains	(205)	(7.1)	(5.7)	(1.4)
Colorado	(69)	(10.1)	(9.0)	(1.1)
Idaho	(128)	(10.2)	(5.0)	(5.2)
Montana	2	2.3	2.2	0.1
Utah	(9)	(3.8)	(3.5)	(0.2)
Wyoming	0	(2.2)	(2.2)	0.0
Far West	(687)	(15.3)	(14.6)	(0.7)
Alaska	0	(28.1)	(28.1)	0.0
California	(51)	(17.6)	(17.6)	(0.1)
Hawaii	(114)	(3.5)	0.2	(3.6)
Nevada	8	1.5	1.2	0.3
Oregon	(394)	(20.3)	(12.5)	(7.8)
Washington	(135)	(1.5)	(0.3)	(1.3)

Note: Numbers may not add up due to rounding.

A Bad Year: Fiscal Year 2002 Tax Revenue Summary

Table 5. Tax Revenue, Fiscal Years 2001 and 2002 (in Millions of Dollars)

	<i>Fiscal Year 2001</i>				<i>Fiscal Year 2002</i>			
	<i>PIT</i>	<i>CIT</i>	<i>Sales</i>	<i>Total</i>	<i>PIT</i>	<i>CIT</i>	<i>Sales</i>	<i>Total</i>
United States	\$209,368	\$29,969	\$172,430	\$484,531	\$186,775	\$24,344	\$173,411	\$457,176
New England	16,463	1,697	8,345	31,648	13,633	1,013	8,238	28,060
Connecticut	3,995	359	2,844	8,547	3,446	150	2,743	7,610
Maine	1,168	96	818	2,437	1,070	77	836	2,368
Massachusetts	9,903	945	3,756	16,646	7,913	587	3,696	14,209
New Hampshire	NA	195	NA	1,128	NA	159	NA	1,191
Rhode Island	914	61	713	1,985	801	14	748	1,864
Vermont	484	41	215	905	403	26	215	817
Mid-Atlantic	47,397	6,765	23,754	91,086	44,711	5,651	23,937	87,496
Delaware	718	62	NA	1,708	714	133	NA	1,779
Maryland	4,755	493	2,389	8,255	4,448	362	2,400	7,871
New Jersey	7,989	1,390	5,753	17,829	6,837	1,172	5,997	16,752
New York	26,443	3,217	8,409	43,204	25,574	2,566	8,248	41,519
Pennsylvania	7,492	1,603	7,204	20,091	7,139	1,419	7,293	19,574
Great Lakes	31,145	5,683	26,554	73,258	29,629	4,957	27,017	71,633
Illinois	8,607	1,279	5,992	18,912	8,086	1,043	6,089	18,218
Indiana	3,780	855	3,687	9,052	3,541	709	3,761	8,709
Michigan	6,778	2,093	7,707	20,527	6,182	1,983	7,800	20,211
Ohio	7,263	915	5,936	15,650	7,304	712	6,038	15,474
Wisconsin	4,717	541	3,232	9,117	4,517	509	3,329	9,051
Plains	16,376	1,814	11,202	31,621	15,498	1,473	11,125	31,515
Iowa	2,427	285	1,691	4,776	2,372	221	1,692	4,662
Kansas	1,977	212	1,659	4,145	1,830	94	1,704	3,891
Minnesota	5,916	729	4,348	11,423	5,443	530	4,198	11,880
Missouri	4,583	366	1,804	7,295	4,460	449	1,817	7,231
Nebraska	1,233	138	905	2,457	1,160	108	919	2,366
North Dakota	241	84	344	887	234	72	338	848
South Dakota	NA	NA	451	639	NA	NA	457	637
Southeast	34,986	5,324	43,189	99,879	33,522	4,757	43,946	98,766
Alabama	2,438	180	1,713	5,897	2,400	305	1,748	6,026
Arkansas	1,806	236	1,713	4,010	1,792	220	1,729	3,985
Florida	NA	1,345	13,952	18,921	NA	1,219	14,147	19,073
Georgia	6,926	725	5,126	13,688	6,488	588	5,035	13,048
Kentucky	2,779	290	2,645	6,775	2,703	207	2,729	6,721
Louisiana	1,738	285	2,407	5,936	1,784	280	2,404	6,024
Mississippi	1,034	271	2,314	4,912	994	254	2,355	4,886
North Carolina	7,520	629	3,436	12,870	7,264	660	3,706	12,825
South Carolina	2,499	213	2,000	5,350	2,349	143	2,027	5,183
Tennessee	NA	674	4,653	7,675	NA	503	4,646	7,482
Virginia	7,226	364	2,273	11,054	6,711	290	2,430	10,619
West Virginia	1,021	113	956	2,790	1,038	87	991	2,895
Southwest	5,379	920	23,292	43,915	5,292	654	23,651	42,688
Arizona	2,301	541	2,984	6,192	2,087	346	3,439	6,252
New Mexico	906	220	1,290	3,050	1,028	142	1,314	3,017
Oklahoma	2,172	159	1,481	4,804	2,178	166	1,475	4,561
Texas	NA	NA	17,538	29,868	NA	NA	17,422	28,858
Rocky Mountain	7,188	741	4,452	14,381	6,405	467	4,441	13,358
Colorado	3,899	322	1,949	6,356	3,440	202	1,900	5,716
Idaho	1,031	142	775	2,457	842	77	788	2,206
Montana	545	102	NA	1,111	512	69	NA	1,137
Utah	1,713	175	1,431	3,805	1,611	119	1,441	3,661
Wyoming	NA	NA	296	652	NA	NA	313	638
Far West	50,435	7,026	31,643	98,744	38,085	5,373	31,056	83,632
Alaska	NA	61	NA	1,318	NA	52	NA	948
California	44,782	6,532	22,079	76,436	33,338	5,080	21,538	62,957
Hawaii	1,105	61	1,640	3,158	1,072	45	1,612	3,049
Nevada	NA	NA	2,044	2,360	NA	NA	2,070	2,395
Oregon	4,548	373	NA	5,063	3,675	195	NA	4,035
Washington	NA	NA	5,879	10,410	NA	NA	5,836	10,248

About The Nelson A. Rockefeller Institute of Government's Fiscal Studies Program

The Nelson A. Rockefeller Institute of Government, the public policy research arm of the State University of New York, was established in 1982 to bring the resources of the 64-campus SUNY system to bear on public policy issues. The Institute is active nationally in research and special projects on the role of state governments in American federalism and the management and finances of both state and local governments in major areas of domestic public affairs.

The Institute's Fiscal Studies Program, originally called the Center for the Study of the States, was established in May 1990 in response to the growing importance of state governments in the American federal system. Despite the ever-growing role of the states, there is a dearth of high-quality, practical, independent research about state and local programs and finances.

The mission of the Fiscal Studies Program is to help fill this important gap. The Program conducts research on trends affecting all 50 states and serves as a national resource for public officials, the media, public affairs experts, researchers, and others. Donald J. Boyd, who has spent two decades analyzing state and local fiscal issues, is director of Fiscal Studies.

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