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State Tax Revenue Growth Slows Sharply in the Third Quarter of 2013 as Atypical Factors That Propped Up Prior Growth Fade

Likely Not a Sign of Economic Slowing — Just More-Normal Growth

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Highlights

- State tax revenue growth slowed sharply in the third quarter of 2013. Year-over-year growth was 6.1 percent, based on preliminary data from the Rockefeller Institute, compared with second quarter growth of 9.0 percent and first-quarter growth of 8.6 percent. This is consistent with our prior analysis, which explained that atypical factors had driven growth up in those earlier quarters.
- Personal income tax revenue growth slowed to 5.3 percent on a year-over-year basis, down from 18.4 percent growth in each of the two previous quarters, and 10.8 percent growth in the fourth quarter of 2012. Withholding taxes on wages were up by 4.4 percent and payments of estimated taxes were up by 11.5 percent. Thirty-five states reported increases in personal income tax collections.
- Sales tax collections increased by 5.6 percent, in line with the prior two quarters, and corporate tax collections rose by 1.9 percent.
- We do not believe the slowdown in tax revenue growth presages a new slowing in the economy. Rather, temporary factors related to federal tax changes that had propped up personal income tax growth in prior quarters have faded away. Tax revenue growth now appears more consistent with continuing modest growth in the economy.
- This is the 15th consecutive quarter that states have reported growth in tax collections on a year-over-year basis.
- Forty-one of 47 early-reporting states reported gains in overall tax collections, while six saw declines.

SPECIAL NOTE: The Census Bureau has delayed the release of state and local government tax revenue data for the third quarter of 2013, due to changes in the survey sample and survey instrument for certain taxes, as well as due to the three-week government shutdown at the beginning of October. The data currently are scheduled to be released along with the fourth quarter of 2013 data on March 31, 2014. In the interim, the Rockefeller Institute will continue to produce timely reports on tax revenue based on preliminary data we collect.

In general, the Rockefeller Institute relies almost exclusively on Census data for historical quarterly tax data analysis. However, the Institute also collects its own state tax revenue data on a monthly basis. Therefore, we decided to release a Special State Revenue Report covering the third quarter of 2013 tax revenues. While the data collected by the Rockefeller Institute are not as comprehensive as Census Bureau data, they are extremely useful for an early read on the economy and for understanding what is happening to state finances.

Preliminary tax collection data for the July-September quarter of 2013 show continued growth in overall state tax collections, as well as for personal income tax and sales tax revenue. However, the growth in overall tax, as well as in personal income tax revenue collections, has softened significantly after two consecutive quarters of robust growth in the first half of 2013.

The Rockefeller Institute's compilation of data from 47 early reporting states shows collections from major tax sources increased by 6.1 percent in nominal terms compared to the third quarter of 2012. Gains were widespread, with 41 states showing an increase in revenues compared to a year earlier. After adjusting for inflation, tax revenues increased by 4.8 percent in the third quarter of 2013, compared to the same quarter of 2012. States' personal income taxes represented a \$3.4 billion, or 5.3 percent, gain and sales taxes a \$3.2 billion, or 5.6 percent, gain for the period. (See Table 1 for national-level changes in revenues since 2007.)

Table 1: Personal Income Taxes Showed Considerable Softening in the Third Quarter of 2013
Percent Change in State Tax Collections vs. Same Quarter Year Ago

Quarter	PIT	CIT	Sales	Total
2007 Q1	8.5	14.8	3.1	5.2
2007 Q2	9.2	1.7	3.5	5.5
2007 Q3	7.0	(4.3)	(0.7)	3.1
2007 Q4	3.8	(14.5)	4.0	3.6
2008 Q1	4.8	(1.4)	0.7	2.6
2008 Q2	8.1	(7.0)	1.0	5.4
2008 Q3	0.9	(13.2)	4.7	2.8
2008 Q4	(1.9)	(23.0)	(5.3)	(4.0)
2009 Q1	(19.4)	(20.2)	(8.4)	(12.2)
2009 Q2	(27.7)	3.0	(9.5)	(16.3)
2009 Q3	(11.5)	(21.3)	(10.1)	(11.0)
2009 Q4	(4.1)	0.7	(4.8)	(3.1)
2010 Q1	3.6	0.3	0.1	3.3
2010 Q2	1.3	(19.0)	5.7	1.9
2010 Q3	3.9	0.5	4.3	5.3
2010 Q4	10.8	12.1	5.1	8.1
2011 Q1	12.6	4.1	6.0	10.2
2011 Q2	15.6	18.3	5.7	11.3
2011 Q3	9.1	0.9	1.6	5.0
2011 Q4	2.8	(3.3)	2.9	3.0
2012 Q1	4.2	3.6	5.0	4.0
2012 Q2	6.0	(3.0)	1.7	4.1
2012 Q3	5.8	8.5	1.8	2.9
2012 Q4	10.8	3.8	2.7	5.3
2013 Q1	18.4	9.3	5.6	8.6
2013 Q2	18.4	11.0	5.3	9.0
2013 Q3	5.3	1.9	5.6	6.1

Source: U.S. Census Bureau (historical data) and Rockefeller Institute of Government (2013 Q3 data).

Despite the broadly positive news, revenues declined in six of the 47 states for which comparable, early data are available. Table 2 shows state-by-state changes in major tax revenues during the third quarter of 2013 compared to the same quarter a year earlier. Kansas reported the largest decline for the quarter at 9.4 percent, followed by Arizona at 6.5 percent. Large declines in collections in Kansas are partially attributable to legislated changes. Earlier in 2013, the governor of Kansas signed into law a tax-cut measure that would reduce the bottom individual income tax rate to 3.0 percent from 3.5 percent and the top individual income tax rate to 4.9 percent from 6.45 percent in 2013. In addition, Kansas also reduced the sales tax rate from 6.3 percent to 6.15 percent as of July 2013. However, the reduction in sales tax rate was instead of the previously scheduled reduction of temporary tax increase from 6.3 percent to 5.7 percent. The large declines in tax revenues in Arizona were mostly due to expiration of the temporary one-cent sales tax increase that was in place since June 2010.

General Sales Tax

Sales tax collections increased by 5.6 percent in the third quarter of 2013 compared to the same quarter of 2012. With 43 of 45 sales-tax states reporting so far, only six states reported declines in sales tax collections compared with the same quarter last year. Arizona had the largest sales tax decline at 15.0 percent, followed by Georgia at 7.9 percent. The large sales tax decline in Arizona, as mentioned above, is due to expiration of a temporary one-cent increase in sales tax of three years ago. The following four states reported double-digit growth in sales tax collections: California, Connecticut, Minnesota, and New Jersey.

The Far West and New England regions reported the largest increases in sales tax collections at 10.4 and 9.4 percent, respectively.

Personal Income Tax

Personal income taxes made up about 41 percent of total tax revenue reported in the third quarter of 2013. Personal income tax revenues increased by 5.3 percent for the nation compared to the same quarter of 2012. With 40 of 41 states with broad-based personal income taxes reporting so far, 35 states recorded growth in the third quarter of 2013, with four reporting double-digit increases. Among individual states, Kansas reported the largest decline at 19.1 percent, while North Dakota reported the largest increase at 29.6 percent (see Table 2).

All regions reported increases in personal income tax collections. The largest growth was in the Far West and New England regions, where collections increased by 10.8 and 6.9 percent, respectively, in the second quarter of 2013. The strong growth in the Far West region is most attributable to a single state — California — where personal income tax collections grew by \$1.3 billion, or 11.7 percent, in the third quarter of 2013 compared to the same quarter of 2012. If we exclude California, personal income tax collections show a growth of 3.9 percent for the nation and a growth of 5.3 percent for the Far West region in the third quarter of 2013.

Withholding for the July-September 2013 quarter increased by 4.4 percent for the 40 states with broad-based personal income taxes and for which we have complete data. Thirty-six states reported growth in withholding for the third quarter of 2013, while four states reported declines, with West Virginia reporting the largest decline at 5.1 percent. The other three states reporting declines in withholding were Alabama, Maine, and Nebraska. Among individual states, North Dakota and Wisconsin reported the strongest growth in withholding in the third quarter of 2013, at 16.1 and 14 percent, respectively. The Far West region reported the largest growth in withholding at 6.0 percent, while the Rocky Mountain region reported the weakest growth in withholding at 3.3 percent.

The highest-income taxpayers generally make estimated tax payments (also known as declarations) on their income not subject to withholding tax. The first payment for each tax year is due in April in most states and the second, third, and fourth are generally due in June, September, and January. In the 38 states for which we have complete data, the median payment was up by 12.3 percent for the first three payments and by 11.5 percent for the third payment compared to the previous year. Four states reported declines in estimated payments for the first three payments. Kansas reported the largest decline for the first three payments at 30.7 percent, followed by Georgia at 29.9 percent. The other two states reporting declines in estimated payments for the first three payments were North Carolina and West Virginia at 5.0 and 2.3 percent, respectively.

Corporate Income Tax

Among the corporate income tax states, 21 of 43 early reporting states reported declines for the third quarter compared to the same quarter of the previous year, while 22 showed gains. Eleven states reported double-digit declines, while 19 states reported double-digit growth in corporate income tax collections in the third quarter of 2013. The large variation among states' corporate income tax revenues is due to volatility in corporate profits and in the timing of tax payments.

The picture among the states as well as among the regions is quite varied. The Southwest region reported the largest declines in corporate income tax collections in the third quarter of 2013, at 26.5 percent. Other regions reporting declines were the Great Lakes, Mid-Atlantic, and Rocky Mountain regions. The Plains region recorded the largest growth in corporate income tax collections in the third quarter at 17.6 percent.

The Outlook

The state personal income tax revenue picture in the first two quarters of calendar year 2013 represented the strongest growth since the start of the Great Recession. However, the growth in personal income tax collections in the third quarter of 2013 has softened significantly. The strong growth recorded in the first half of 2013, as discussed in previous State Revenue Reports, were mostly attributable to the acceleration of income to tax year 2012 by some taxpayers driven by the fear of potential federal tax rate increases in tax year 2013. The earlier warnings that the strong growth in personal income tax collections would likely be short-lived are already visible in the third quarter of 2013. And, quite likely, the growth in personal income tax collections would be much softer in the coming quarters compared to the first and second quarters of 2013. However, in most states the overall trend in tax collections for fiscal 2014 is positive.

Table 2: Percent Change in State Tax Revenue

Quarterly Tax Revenue by Major Tax, Early Reporting States
July-September 2012 to 2013, Percent Change

	PIT	CIT	Sales	Total
United States	5.3	1.9	5.6	6.1
New England	6.9	12.5	9.4	8.6
Connecticut	5.8	20.4	22.0	9.4
Maine	(2.0)	8.7	8.3	6.3
Massachusetts	8.4	14.5	6.3	9.1
New Hampshire	NA	10.2	NA	11.4
Rhode Island	4.4	(12.9)	4.9	4.3
Vermont	7.4	(4.7)	(0.0)	7.2
Mid-Atlantic	2.0	(3.5)	5.2	2.5
Delaware	5.9	(14.8)	NA	3.7
Maryland	7.5	(15.1)	1.2	3.1
New Jersey	7.7	(7.5)	10.4	7.4
New York	(0.4)	4.7	5.6	1.6
Pennsylvania	2.8	(4.1)	2.9	1.1
Great Lakes	5.7	(7.1)	5.8	4.3
Illinois	6.1	13.0	7.8	6.4
Indiana	(4.8)	(7.8)	2.5	(0.9)
Michigan	9.8	(53.4)	7.4	3.6
Ohio	3.1	(95.6)	3.9	1.9
Wisconsin	13.5	19.7	9.2	11.7
Plains	2.8	17.6	5.6	9.1
Iowa	3.5	21.5	4.6	4.5
Kansas	(19.1)	(4.9)	(1.9)	(9.4)
Minnesota	8.1	10.8	10.3	9.2
Missouri	4.8	18.3	5.5	5.2
Nebraska	2.0	32.9	5.6	5.1
North Dakota	29.6	NM	5.7	106.1
South Dakota	NA	NA	7.7	4.8
Southeast	4.0	8.5	4.0	4.5
Alabama	5.4	(16.6)	3.9	2.3
Arkansas	1.4	13.9	6.4	4.2
Florida	NA	(0.1)	7.2	5.1
Georgia	4.9	16.0	(7.9)	6.2
Kentucky	3.3	33.4	2.3	4.6
Louisiana	15.3	(53.8)	0.5	3.6
Mississippi	(1.0)	60.0	5.8	7.1
North Carolina	2.9	38.7	5.0	5.5
South Carolina	3.6	(7.7)	4.4	2.5
Tennessee	5.5	(6.0)	3.6	2.1
Virginia	4.0	19.4	7.8	5.0
West Virginia	(4.5)	(8.6)	(0.3)	(1.2)
Southwest	1.0	(26.5)	1.9	7.0
Arizona	6.7	(24.2)	(15.0)	(6.5)

New Mexico	ND	ND	ND	ND
Oklahoma	(8.1)	(30.1)	0.9	(4.2)
Texas	NA	NA	4.7	11.4
Rocky Mountain	5.1	(7.2)	4.0	3.4
Colorado	5.6	(5.9)	5.4	4.6
Idaho	4.0	24.8	4.6	5.1
Montana	ND	(20.6)	NA	1.8
Utah	3.2	(19.9)	1.5	1.0
Wyoming	NA	NA	ND	ND
Far West	10.8	4.3	10.4	10.6
Alaska	NA	ND	NA	ND
California	11.7	1.5	13.2	12.5
Hawaii	4.3	72.4	(5.4)	(2.5)
Nevada	NA	NA	5.8	4.9
Oregon	5.6	15.6	NA	5.5
Washington	NA	NA	7.4	6.9

Source: Individual state data, analysis by Rockefeller Institute.

Notes: NA - not applicable; NM - not meaningful; ND - no data.

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