EDITOR'S NOTE: As our state and nation continue to confront the COVID-19 pandemic, state fiscal and federal policies will play key roles in ensuring the physical and economic health of Nebraska and its residents. OpenSky Policy Institute staff will be continuously analyzing state and federal policies that impact Nebraskans during this national emergency. This analysis is part of that effort. You can access more of our pandemic-response policy analysis here. We also remind you that OpenSky staff are working remotely during the pandemic response. Remote contact information for staff members can be found here.

The fiscal impacts of the coronavirus are largely unknown at this point, though we do know the chance of the economy entering a recession is becoming ever more likely. Nebraska lawmakers this week will enact an emergency appropriation for the state's COVID-19 response.

Last week we noted that Nebraska may want to join other states that have begun to revisit their revenue expectations for both the current fiscal year and next to account for the economic impact of the pandemic. Here we look at how revenues were affected by historical events and how they can help inform our outlook in the coming years.

Impact of COVID-19 on tax receipts yet unknown, but historical context shows what could be

In order to gauge the potential impact of the coronavirus, we can look at two significant historical events since FY 00 that had a major impact on state general fund receipts: 9/11 and the Great Recession.

In the aftermath of 9/11, actual growth in state general fund receipts declined 3.7%. During the Great Recession -- in which Nebraska fared better than most states[1] -- revenues took an even greater hit. The first fiscal year encompassing the recession and its aftermath -- FY 09 -- saw revenues drop 4.2% compared to the previous year. FY 10 was worse with a decline of 4.6%.

If Nebraska experiences revenue declines from COVID-19 similar to those in the Great Recession, state general fund revenue would decline by $207 million in FY 21 and another $217 million in FY 22[2], rather than increase as currently projected. A drop in revenues of this magnitude would strain the state's ability to fund priorities -- including the response to COVID-19 and policies people need most during recessionary periods -- and could require policymakers to find new revenues just to maintain current service levels.

[1] NPR, "How Every U.S. State Fared Since The Recession, In One Graph," accessed at https://www.npr.org/sections/money/2014/07/03/327719641/how-every-u-s-state-has-fared-since-the-recession-in-1-graph on March, 23, 2020.
[2] This calculation assumes that FY 20 revenues do not meet the February forecast of $5.205 billion and instead and uses the certified forecast of $4.929 billion.

With prominent economists signaling a sharp, severe recession[3] and unemployment rising as high as 20%[4] -- which would be considerably higher than was experienced during the Great Recession -- it is very possible that the impact of COVID-19 could be much greater than the last economic downturn.

History also shows that utilization of benefits such as Medicaid and Unemployment Insurance increases during economic downturns to help state residents stay afloat. The current budget does not account for the impending increase in use of such benefits by Nebraskans who will experience economic difficulties amidst the COVID-19 crisis.

State likely to experience choppy fiscal waters in midst of COVID-19

As of February, tax collections in FY 20 were $255 million ahead of projections. Any money at the end of the current fiscal year in excess of the certified October forecast would be deposited into the state's cash reserve. This assumption is made in the Appropriations Committee's budget proposal, which projected $276 million over forecast in FY 20 being deposited into the cash reserve.[5]

In light of recent events, however, that projection now seems optimistic. As outlined, COVID-19 will affect state receipts this year, but just how much is unknown. Should the $276 million projected excess in tax receipts this year not materialize, the cash reserve would sit at $510 million at the beginning of FY 21 without any withdrawals. However, the Legislature this week will likely authorize an emergency transfer of $83.6 million from the cash reserve to aid the state's response to COVID-19.[6] This emergency transfer will draw down the state's rainy day fund to $426 million.

Further complicating receipts is the fact that the federal government has delayed the tax filing deadline until July 15 and the state has followed suit, although the governor has asked that those who are capable of doing so file their taxes by April 15 to limit the revenue impact to the state.[7] If a significant number of filers were to delay until July 15, it

[3] Moody's Analytics, "COVID-19 and U.S. CRE Property & Transaction Markets," accessed at https://ma.moodys.com/rs/961-KCJ-308/images/3.19.20%20-%20COVID-19%20-%20The%20Potential%20Effects%20on%20the%20US%20Economy%2C%20CRE%20Sectors%2C%20and%20CRE%20Finance%20Markets.pdf on March 20, 2020.
[4] Bloomberg News, "Mnuchin Warns Virus Could Yield 20% Jobless Rate Without Action," accessed at https://www.bloomberg.com/news/articles/2020-03-17/mnuchin-warns-virus-could-yield-20-jobless-rate-without-action-k7wheob8 on March 25, 2020.
[5] Nebraska Legislature, "Appropriations Committee Budget Proposal, Mid-Biennium Budget Adjustments FY2019-20 and FY2020-21," accessed at https://www.nebraskalegislature.gov/pdf/reports/fiscal/2020proposal.pdf on March 20, 2020. (Page 5)
[6] Omaha World-Herald, "Ricketts adds $25 million to emergency appropriations request to help battle coronavirus," accessed at https://www.omaha.com/livewellnebraska/ricketts-adds-million-to-emergency-appropriations-request-to-help-battle/article_c10a329a-9e80-5784-bf95-6e9b2017bcab.html on March 23, 2020.
[7] Omaha World-Herald," Ricketts encourages Nebraskans to file taxes by April 15 despite federal extension," accessed at https://www.omaha.com/livewellnebraska/ricketts-encourages-nebraskans-to-file-taxes-by-april-despite-federal/article_661a5ce7-960c-599d-8b51-4a6e8cec55f6.html on March 23, 2020.

would push those receipts into the next fiscal year and make it difficult to decipher the magnitude of COVID-19's impact on FY 21's revenues, potentially obscuring its impact, at least for a couple of months. While a filing extension could be beneficial for some taxpayers, it will also negatively impact FY 20's tax receipts, as the state has collected an average of 31.2% of the entire year's revenues in the last quarter of the most recent three fiscal years.[8]

If, as many indications point, the economy enters a recession[9] this year, major ramifications will fall upon the state that are not yet accounted for in either the forecast or budget. Sales tax revenues will come in lower during a recession and income tax collections will fall, though the fallout from income taxes this year will be felt more fully in FY 21, the second year of the biennium.

Cash reserve might not be enough to adequately help state weather COVID-19 fallout

If the economic fallout from COVID-19 is similar to that from the Great Recession, the state's cash reserve would likely not be large enough to help the state maintain current service levels, particularly without the $276 million deposit into the fund that was originally expected from this fiscal year. While the cash reserve will sit at $426 million after this week's emergency appropriation, $55 million of that has been authorized as a transfer to fund some capital construction projects in FY 21. This effectively means the state would only have $371 million in cash reserve funds to address the economic fallout from COVID-19 as well as the increased use of Medicaid, Unemployment Insurance and other public benefits.

Conclusion

The threat from COVID-19 hangs over the state in a yet-unknown magnitude. The Governor and policymakers are taking important first steps in fighting the epidemic and ensuring the health of Nebraskans. While the revenue impact of the virus is unknown, history is a useful guide and it shows we may be in for considerable challenges that will require tough but important choices by our state's leaders.

[8] OpenSky analysis of Department of Revenue General Fund Receipts News Releases, accessed at https://revenue.nebraska.gov/about/news-releases/previous-general-funds-receipts-news-releases on March 23, 2020.
[9] IHS Markit, "The global economy: Headed for a recession," accessed at https://ihsmarkit.com/research-analysis/the-global-economy-headed-for-recession.html on March 19, 2020.