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State Ballot Tax Initiative Outcome Mixed; Modest Revenue Effects - Fitch

Fitch Ratings-New York-11 November 2020: Taxes were on the ballot in a number of states in the 2020 election, and the outcome of these statewide ballot initiatives will have a modest effect on state budgets for the most part, Fitch Ratings says. Voters split in their support of taxes against a backdrop of weakening state revenues. Measures targeting narrow types of activity or those with specific funding purposes fared better.

Notably, Illinois voters rejected a graduated income tax, narrowing the state's fiscal options. This would have replaced the flat tax provided for in the state constitution and would have generated an estimated $1.3 billion in state tax revenue in the second half of the current fiscal year. Budget cuts are likely, but the state may also raise revenues, such as choosing to increase the flat income tax rate. Borrowing is already included in the enacted budget, but additional debt without mitigating structural measures could compound pressures on Illinois' IDR of 'BBB-' with a Negative Rating Outlook.

California voters also rejected a constitutional amendment, Proposition 15, or the "split roll." Had it passed, California's Legislative Analyst's Office estimated it would have increased local property taxes by $8 billion-$12.5 billion per year statewide beginning in 2025, reducing cost pressure on the state to fund schools.

In Colorado, voters approved the reduction of the state income tax rate to 4.55% from 4.63%, which is expected to reduce state revenues by $169.8 million in fiscal 2021-2022. Voters also chose to repeal the Gallagher Amendment, which currently limits residential property to no more than 45% of the total statewide property tax base by essentially reducing assessments when residential property values rise. The repeal will prevent an automatic residential property tax cut anticipated in fiscal 2022 and relieve the state from an estimated $247 million fiscal offset to school districts. Voters also approved a new tax on nicotine vaping products and an increase in existing tobacco taxes, raising fiscal 2021-2022 revenue by an estimated $175.6 million, the majority of which will initially go to K-12 education. Fitch maintains a 'AA'/Stable rating on the Colorado School Credit Enhancement Program, also known as the School District Intercept Program, or SDIP, and a 'AA-'/Stable rating on the Colorado Charter School Moral Obligation Program.

Arizona voters also supported a K-12 tax measure, approving an additional 3.5% tax on higher earners that will raise around $827 million for schools and teacher salaries. Arkansas voters made permanent a roughly $300 million 0.5% percent sales tax increase, first authorized in 2012, to fund transportation infrastructure. Oregon increased the cigarette tax by $2.00 per pack and created a 65% tax on e-cigarettes, generating around $160 million annually revenues for health initiatives and tobacco cessation efforts. The revenue will nominally alleviate pressures on the general fund's $22 billion biennial budget.

Gaming initiatives passed in Maryland, Nebraska, South Dakota and most Louisiana parishes will have a marginal effect on tax revenue. Taxes on related activity such as entertainment, food, and lodging may have secondary revenue benefits, although this is unlikely to materialize until the coronavirus is contained.

Recreational cannabis legalization passed in all states where it was on the ballot: Arizona, Montana, New Jersey and South Dakota. In addition, Mississippi approved medical marijuana. While this provides a new tax source for these states, in all cases Fitch anticipates modest effects on state budgets.

Other notable ballot initiatives, including Alaska's Measure 1 regarding fuel-production taxes, have not been called yet.

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