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S&P: Approval Of Nontraditional Revenues Dominates Recent Ballot Measures For U.S. State And Local Governments.

Key Takeaways

- Legalization of gaming and drugs continued to expand, with seven states approving new or additional taxing power from nontraditional revenue sources.
- Results from income tax increases were mixed, with the three major initiatives resulting in three different outcomes.
- Only two states had bond referendums on the ballot this year, but they all passed.
- Highlights from local government elections include some changes in property tax exemptions and police reforms in light of recent demonstrations across the country.

Voters weighed in on statewide ballot measures in 22 states on Nov. 3. Many of these were approved, with a clear preference for increasing "sin tax" revenues from gaming and legalized drugs. At S&P Global Ratings, our primary focus on ballot results is how credit quality could be affected; this generally stems from revenue increases and decreases, or a notable rise in expenditures. As more states turn to nontraditional revenue sources to support operations, we are also watching the long-term trend and stability of the new revenues.

Widespread Support Of Nontraditional Revenue Sources Including Gaming/Sports Betting, Marijuana

In recent years, various states have looked to legalization–and subsequently taxation–of retail marijuana. This seemed to continue with overwhelming support from voters, as all such measures on the ballots across the country passed. Arizona, Montana, New Jersey, and South Dakota approved the legalization of recreational marijuana, while voters in Mississippi and South Dakota approved medical marijuana programs. Colorado legalized marijuana some years ago, but this November asked voters for an increase in the nicotine tax, and Oregon increased taxes on tobacco products. We expect that more states will pass measures like this but expect their overall effect on state finances to be marginal. Additionally, as more states legislate these kinds of revenues, we expect that as legalization of marijuana becomes more widespread, the growth of revenues from these taxes will slow over time as marijuana becomes more readily accessible. (See our report, "Is Marijuana Legalization The Answer To States' Budget Pressures?," published Feb. 21. 2019, on RatingsDirect)

Measures to expand gaming and betting also received support, with Nebraska approving three measures including enacting taxes on racetrack activities. Maryland and South Dakota also expanded gaming activities within the states. While not a statewide measure, Louisiana's voters approved sports betting in a majority of its parishes. All states that permit commercial casino gaming levy some form of wagering tax on adjusted gross receipts or gross gaming receipts less any payout for prizes.

Although none of these nontraditional sources make up significant components of a state's revenue, we do view the diversity of revenue sources as a net positive.

Mixed Results For Income Tax Changes

Three states had income tax changes on the ballot (Arizona, Colorado, and Illinois). While a voter initiative to reduce income tax rates passed in Colorado (to 4.55% from 4.63%), in Arizona voters approved an initiative to increase income tax on residents with incomes above $250,000. The measure sets up a separate tax bracket for residents that would increase the top rate to 8% from 4.5% on incomes above $250,000 (or $500,000 for joint filers). The additional revenue derived from the increased tax rate will be used solely to fund education.

Additional revenues at the state level can bode well for state revenue sharing for schools and local governments, and results for state-level tax increases varied. When revenue increases at the state level either enhance—or stave off cuts—to locals, the credit impact can be net positive.

Illinois voters did not approve a legislative measure to replace the state's flat income tax rate with a graduated income tax, which would have been significant in addressing the state's current budget challenges. (For additional information, see our summary report for Illinois published Oct. 7, 2020.) Limited support for increased income taxes is not surprising, particularly during an economic contraction. However, if this trend continues, states will have to look to other options to balance budgets as the effects of the COVID-19 pandemic on state revenues contribute to varying degrees of budget and liquidity stress across states.

There is no immediate credit impact for local governments in Arizona, Illinois, or Colorado as a result of the electorates' vote on income tax, but we are watching how it could affect local operations over the long term.

Few Requests For State Bond Issuances During A Tepid Economic Recovery

Two states, California and New Mexico, included new bond authorization questions this year, unlike in 2018 when six states had bond authorizations on the ballot. New Mexico was successful, as was California. Such authorizations can provide funding for various programs, taking advantage of favorable market conditions. In our view the decline of bond authorization measures could reflect the uncertainty of the recovery from the recent COVID-19 induced recession. S&P Global Ratings has noted that in the decade following the Great Recession state governments generally reduced their overall debt burden. (See "Infrastructure After COVID-19: Risk Of Another Lost Decade Of U.S. State Government Capital Investment," Oct. 2, 2020.)

Local Government: Some Shifts In Who Bears The Property Tax Burden

Across the U.S., voters approved multiple statewide measures that resonate down to the local government level. This includes some indication of an incremental shift in property taxpayers from residents to business, such as more homestead exemptions for segments of society such as veterans and senior citizens. Measures supporting these changes passed in Florida, Virginia, Louisiana, and New Jersey. These changes also represent a shift to more support for the social 'S' in ESG. Exceptions to this include votes in California and Colorado where voters decided not to shift the property tax burden more heavily to businesses:

California's property tax regime under Proposition 13 remains intact: A proposed seismic shift that would have changed the manner in which assessed valuations are determined for business properties (Proposition 15) was narrowly defeated, while amendments to Proposition 13 at the

margins, such as those that benefit seniors, continue to be approved (Proposition 19).
Repeal of the Gallagher Amendment in Colorado (Amendment B) resulted in stopping residents' property tax rollbacks which had ultimately shifted more burden to businesses.

Local Law Enforcement Reforms

Following a summer marked by police protests in the wake of the May killing of George Floyd in Minneapolis, 14 cities and counties had elections addressing policing policies and procedures. Questions were on the ballot in seven states, from California to Ohio. Initiatives designed to change police duties, limit general funds spent on police operations, establish oversight boards and improve transparency found broad support in jurisdictions across the U.S., with 15 of 20 passing. For the most part, the changes are not expected to affect credit quality. However, should they result in notable revenue or expenditure changes that affect a jurisdiction's financial position, there could be an impact.

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