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Multistate: Revenue Growth Continues to Moderate; Some Signs of Budget Stress Appear

State tax revenue growth continues to grow slowly, if at all, according to recent reports. The most comprehensive look in the State Tax and Economic Review by Lucy Dadayan at the Tax Policy Center indicates that for the 12 months ending March 31, 2024 (three-fourths of FY 2024 for most states), state revenues increased by only 2.2 percent in nominal terms and declined by 0.6 percent after adjustment for inflation. This rather tepid growth continued through the 2nd quarter of 2024 with the median state growth in all taxes coming in a 1.0 percent in nominal terms. This trend of moderating to negative real growth first began to appear in late 2022 after two years of double-digit increases in state tax increases.

Further complicating state budget-making in some states, federal assistance to states and localities provided by the American Rescue Plan to offset the budgetary impacts of the pandemic is no longer available. In total, state and local governments received about $350 billion under the plan, some portion of which (as much as one-third in the early years) was used to offset the impact of reduced revenues on current government services. Additionally, over one-half of the states enacted significant state reductions from 2021-2023, with most states focusing on personal and corporate income rate reductions, according to the Tax Foundation.

These pressures are surfacing in some states as they prepare the FY 2026 budget for consideration by state legislatures in January. Rhode Island, for example, is requiring state agencies to submit budget requests at two different levels and are looking at a $400 million structural budget deficit in FY 2026, a figure expected to increase in future years. Additionally, Iowa recently deferred a corporate tax rate reduction as FY 2024 corporate income tax revenues fell short of the required $700 million level needed to trigger a rate reduction for 2025 as specified in legislation passed earlier. On a broader basis, the Pew Trusts examined long-term budget estimates (extending to at least FY 2028) produced in a dozen states. It found that at least seven states were expecting structural deficits over the period. There were a variety of contributing factors, including slowing revenue growth, enacted tax cuts, and various budget pressures such as the aging population, transportation needs, and Medicaid costs. On the bright side, state rainy day funds and other available budget balances remain near all-time highs and can provide some near term relief if a state so chooses. Stay tuned to TWIST for further updates on state fiscal conditions.