

IMPACT OF THE PANDEMIC ON MUNICIPAL REVENUES

Our nation and the world are experiencing an unprecedented event with the coronavirus pandemic. Illinois' stay at home order, starting March 21, 2020, caused an immediate reduction in demand by cutting off supply of nonessential goods and services — driving down employment, sales, income, and more.

From where we are today, the timeline to normalcy, both in daily life and economic cycles, is unknown. The region does not yet know what “normal” will look like after the global pandemic. While the current economic situation is not parallel, CMAP looked at the data from the 2007-2009 recession as a comparison, and during this recession overall state revenues dropped 16 percent before they started growing again in 2011.

Currently, it is not known how long the stay at home order will be in place or how it will be lifted, the trajectory and duration of unemployment, and business closures. We also don't know how the pandemic will impact the region's tax base and revenue streams. The possibility of a strategic and slow return to opening offices and businesses confounds our inability to predict the long term impact of an economic downturn on revenues.

It is clear that the pandemic will have an immediate impact on state, county, and municipal revenues. This Policy Brief will provide context and considerations as to how municipalities may be impacted by changes in revenue as a result of COVID-19 restrictions, particularly looking at sales tax, the Local Government Distributive Fund (LGDF), and property tax.

Changes in revenue levels will impact different municipalities in disparate ways

The sum of the coronavirus pandemic's impact on revenues will depend on how municipalities [rely on certain revenue sources](#) for funding their public services and infrastructure. The timing of when municipalities experience the impacts will also differ by revenue source. As an example, property taxes lag real estate value growth, whereas sales and income tax revenues respond quickly to changes in consumption and employment.

While some municipalities rely heavily on property taxes and other locally-imposed revenue sources, others rely on state revenues disbursed to municipalities such as income and sales tax. A third of municipalities in the region rely on a combination of income and sales tax for more than a third of their revenue. Overall, income and sales tax tend to be less stable revenue sources than the property tax. A little less than half of the municipalities in the region rely on property taxes for more than 30 percent of their revenue.

For most communities, the property tax is their most stable form of revenue, with only an average of 2 to [4 percent](#) of property taxes uncollected. For the small percentage of owners unable to pay, state law prescribes a detailed process that provides the property tax revenue by selling unpaid taxes to investors. This helps taxing districts with a significant reliance on property taxes to maintain services.

If an economic downturn results in sustained high levels of unemployment and business closures, individuals and businesses may not be able to pay property taxes. State law requires counties to sell these unpaid taxes to investors. Then, the majority of communities will receive their property tax revenue. However, some communities already experiencing higher levels of nonpayment have less investor interest in buying unpaid taxes, such as those with higher unemployment or more disinvested properties. These communities would see significant reductions in property tax revenue if nonpayment rates increase further and investors continue declining to buy these unpaid taxes.

Some municipalities reliant on sales tax revenue may be more resilient to drops in revenue

As experienced during the 2007-2009 recession, reliance on sales tax revenues generated from the sale of goods is less sustainable during economic downturns. These impacts will likely be greater from those of the last economic recession, where overall sales tax revenues in Illinois dropped 8 percent between FY2008 and FY2009 and another 4 percent in FY2010. Even when sales tax revenue started growing again in FY2011, FY2008 revenue levels were not reached until FY2014.

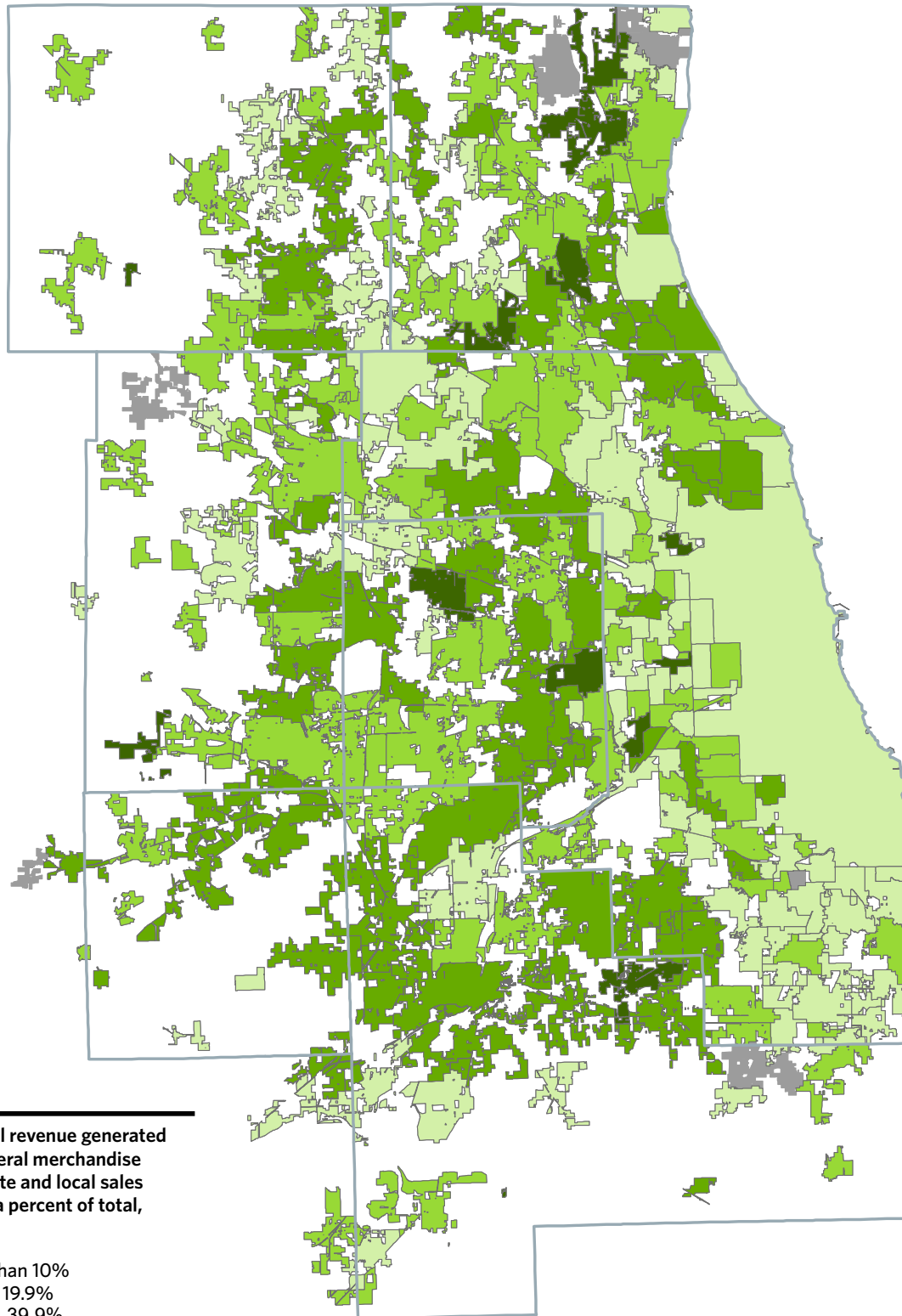
Many municipalities are reliant on sales tax revenues, and more specifically, some municipalities are more reliant on revenues generated from general merchandise sales (e.g. products not immediately available during the stay at home order like clothes, toys, electronics, restaurant sales) than others. General merchandise sales account for more than 75 percent of the sales tax base in three-quarters of the region's municipalities.

Oftentimes, these are communities that have large retailers or malls, and sometimes impose minimal or no municipal property taxes.

Drilling down further, some municipalities have a larger base of sales from general merchandise relative to sales from food, drugs, and medical appliances (products still accessible during the stay at home order). All municipalities receive 1 percentage point of the state sales tax on both general merchandise and food, drugs, and medical appliances. In addition, 185 municipalities in the region impose their own local sales taxes on general merchandise.

Under the state's stay at home order, many retailers and restaurants that generate sales taxes are closed, driving down revenues for all municipalities. Higher unemployment and business closures could also impact these revenues after the stay at home order is lifted. Municipalities more reliant on their general merchandise base, as opposed to food and drugs, will be most affected. Due to their existing levels of resources and potential reserves, many of these same municipalities may have a greater diversity of resources to weather the effects of the stay at home order and a subsequent economic downturn.

The following map illustrates municipal reliance on sales tax revenue generated from general merchandise sales. Those in dark green are most reliant on general merchandise-based sales tax revenue, and those in light green are least reliant. Across the region, 86 municipalities rely on revenues generated from general merchandise sales for more than 20 percent of their revenue. On the other hand, 96 municipalities rely on these revenues for less than 10 percent of their revenues.



Municipal revenue generated from general merchandise sales, state and local sales taxes as a percent of total, 2018

- Less than 10%
- 10% - 19.9%
- 20% - 39.9%
- 40% - 63.4%
- No data available

Source: Chicago Metropolitan Agency for Planning analysis of Illinois Department of Revenue and Illinois Office of the Comptroller data, 2018
 Note: Revenues include those accruing to general, special, capital, and debt service funds.

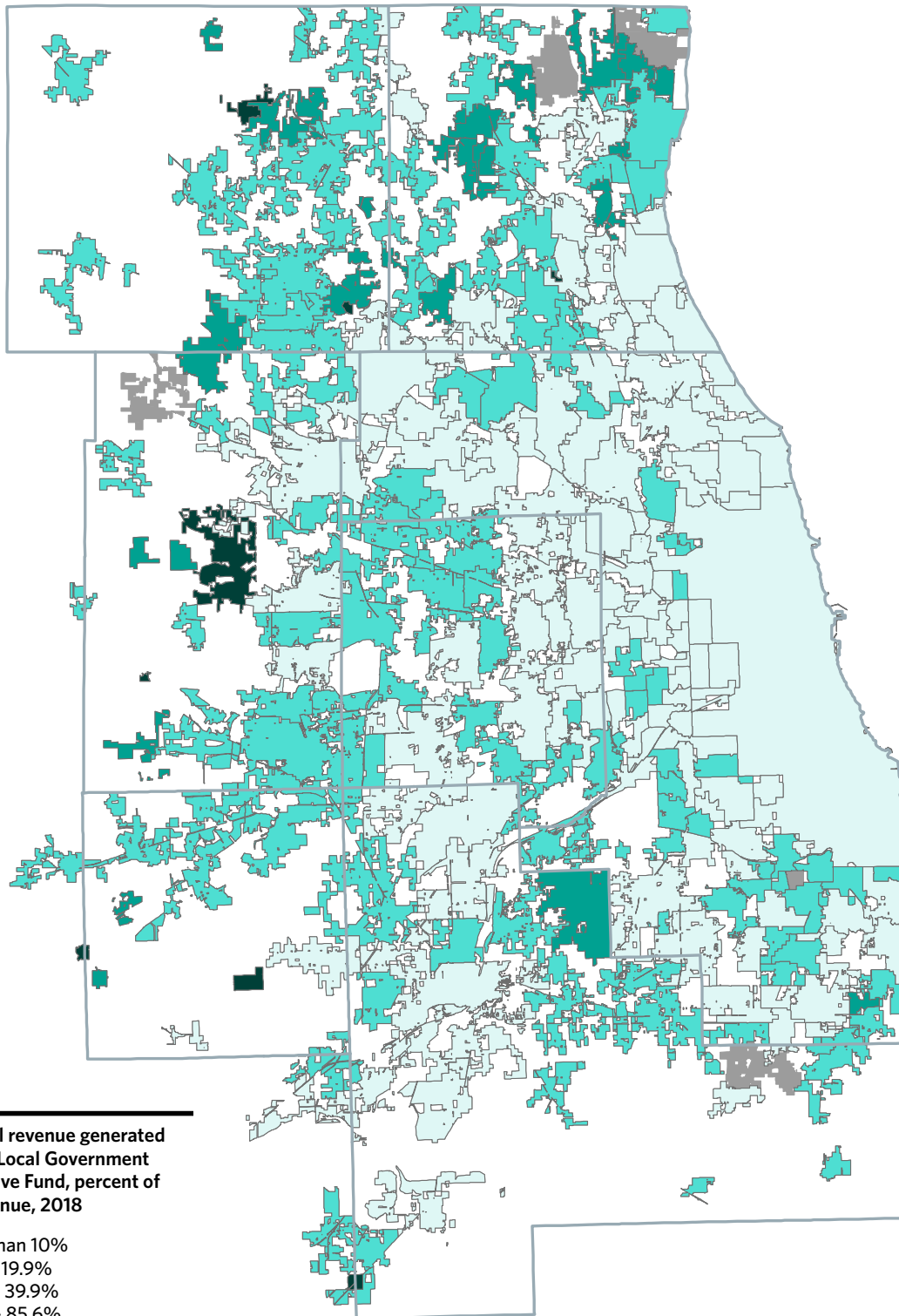
An economic downturn would reduce Local Government Distributive Fund revenues

A significant increase in unemployment as a result of the COVID-19 pandemic will reduce individual income tax revenue. An economic downturn would continue this trend, although it remains unclear what employment will look like after the stay at home order is lifted. In addition, business closures and lower economic activity will reduce corporate income tax revenue. During the last economic recession, state income tax revenue dropped 8 percent between FY2008 and FY2009, and another 9 percent in FY2010, although trends and distribution of unemployment were different from the current circumstances. The State may experience greater and more immediate drops in income tax revenue due to the response to the pandemic.

The pandemic's impact on the use tax, which consumers pay on purchases from out-of-state businesses, is unclear. A shelter in place order may have driven up remote sales initially, while driving down sales within Illinois, as consumers switch from buying in stores to online. However, in the following months, higher unemployment would reduce individual's purchasing power, including remote sales. [Use tax revenue](#) will also change starting July 1, 2020 due to The Leveling the Playing Field for Illinois Retail Act, [Public Act 101-0031](#). The statute will require out-of-state retailers to charge Illinois consumers all state and local sales taxes based on where the purchase is delivered, rather than the state use tax. These trends may reduce overall state income and use tax revenue, thereby driving down the amount of funding available in the Local Government Distributive Fund (LGDF). CMAP will continue to monitor the resulting net effect of all of these factors.

Municipalities and counties receive a portion of both state income and use tax revenue, which is shared through the LGDF based on share of the population. As a result, disbursements from the LGDF to municipalities and counties would also be lower. Municipalities with a large residential base, but few businesses, tend to be more reliant on these revenues.

The following map illustrates how reliant municipalities in northeastern Illinois are on LGDF revenues. Most municipalities do not rely heavily on this revenue source, with just 36 using it for more than 20 percent of revenues.



Source: Chicago Metropolitan Agency for Planning analysis of Illinois Department of Revenue and Illinois Office of the Comptroller data, 2018
 Note: Revenues include those accruing to general, special, capital, and debt service funds.

Existing regional challenges are being compounded

Local governments play an essential role in providing public services during a crisis. However, many lack staff or other resources, [limiting their capacity](#) to help residents and businesses. It is important to note that some communities in the region were already caught in a cycle of disinvestment, unable to promote economic development, invest in infrastructure, and otherwise serve their residents. Many communities with lower capacity may also be less [resilient](#) in the face of acute shocks to the economy.

Economic outcomes in our region frequently reflect racial lines of demarcation. [ON TO 2050 noted](#) that residents of color, particularly black residents, often experience lower incomes and higher unemployment. These same residents may be disproportionately impacted by economic conditions under both COVID-19 restrictions and any resulting economic downturn. Many of these communities may have significant public service needs driven by an economic downturn, and may have challenges weathering business closures, increased need for public services, and other impacts. Moreover, these communities and their residents may experience greater health [impacts from COVID-19](#) itself.

Property tax impacts will be most acute and long lasting for disinvested communities

Municipalities in the seven county metropolitan region vary in terms of their reliance on property tax revenues; municipalities providing services such as fire protection and libraries typically more reliant on property tax revenues compared with those whose services are provided by special districts. Many municipalities are heavily reliant on property taxes because they lack retail and other sales tax-generating development.

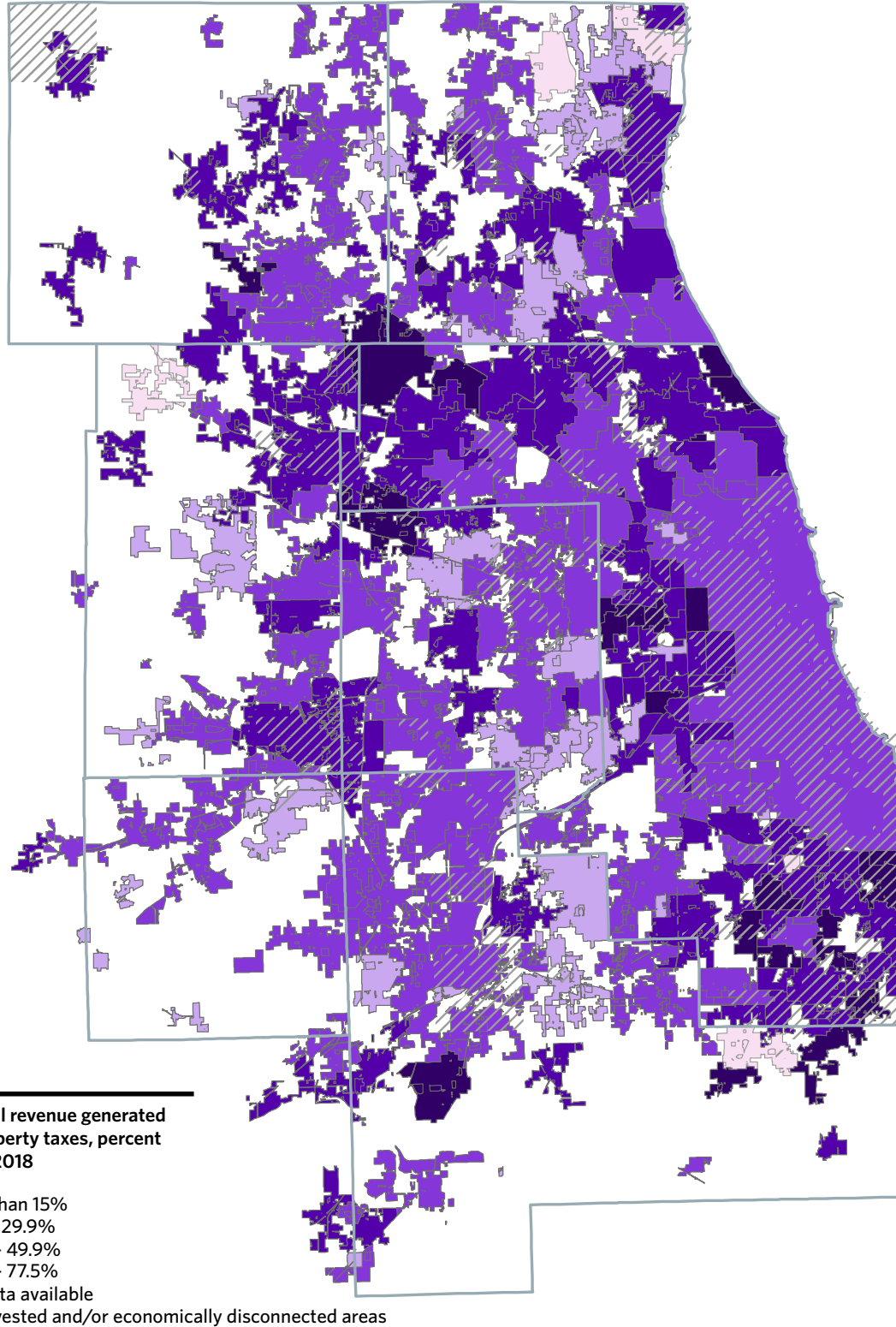
However, for the majority of governmental units in the region, property taxes are the largest source of funding. Individual taxing bodies, including counties, townships, municipalities, special districts, and school districts have their own levy rates that are individually determined by the relationship between their annual financial requests and the assessed value of property within their geographical boundaries.

Many disinvested municipalities are reliant on property tax revenues and may be more likely to experience nonpayment of property taxes this year due to the current economic conditions. Because property taxes are paid in arrears, current year bills reflect property values for 2019. Business closures and potential high levels of sustained unemployment could soon reduce property tax revenue collection. Effects will vary depending on the level and timeliness of payment and whether investors eventually purchase the taxes at the county tax sale.

Less property tax revenue for local governments would reduce the resources available to provide necessary programs and services to meet community needs resulting from the pandemic. Homeowners and business owners unable to pay property taxes may have difficulty keeping their properties as the burden of interest payments on the unpaid taxes adds up, and eventually the following year's tax bill comes due.

Due in part to the 2007-2009 recession, the region's property tax base began to decline in 2010. Following the pandemic, the property tax base may decrease in the coming years due to a potential economic downturn, driving up property tax rates or reducing revenues, depending on the choices made by individual local governments. For communities with [disinvested or economically disconnected areas](#), higher property tax rates could cause additional difficulty in recovering from an economic downturn, as higher tax rates may hinder economic development efforts. Many of these communities already have [high property tax](#) rates, which represent a significant burden on residents and businesses.

The following map compares reliance on property taxes to the region's economically disconnected and disinvested areas. Across the region, 134 municipalities rely on the property tax for more than 30 percent of their revenues. Among those, 26 rely on it for more than half of their revenues.



Source: Chicago Metropolitan Agency for Planning analysis of Illinois Office of the Comptroller data, 2018
 Note: Revenues include those accruing to general, special, capital, and debt service funds.

Local governments will need support to respond to the pandemic

It is expected that all municipalities will experience decreases in one or more revenue sources. The impact of reduced sales tax and LGDF revenues will depend on whether municipalities rely on these revenues relative to other revenues, particularly locally-imposed taxes like property and utility taxes. Many municipalities with economically disconnected and disinvested areas already receive lower levels of sales tax revenue, thus are less affected by drops in sales tax revenue.

However, residents and businesses in these communities will require access to programs and services as a result of the pandemic, COVID-19 restrictions, and potential economic downturn that other communities may take for granted. Communities that already had a substantial revenue base may have other opportunities to ensure public services and programs continue, such as cash reserves or greater ability to shift budget priorities. Communities of color that have already been disconnected from economic opportunity may experience greater impacts. Support and reinvestment should be directed strategically to help those communities most impacted by the economic distress caused by COVID-19.

Some communities in our region are still struggling from the previous recession, including vacancy, abandonment, and poor housing conditions. Reduced municipal revenues, regardless of source, will only make it harder for these communities to sustain the [long-term multipronged strategies](#) that have proven most effective in rebuilding local housing markets.

To build the region's resilience in the recovery from the pandemic, communities will require different kinds of programs based on their needs. CMAP will continue to monitor and analyze data on these revenue sources in order to guide decision-making, as well as work with regional partners to ensure these communities do not experience further disproportionate impacts or experience barriers to accessing funds to help with recovery from the pandemic.

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