



Racine County, Wisconsin

County Tax Structures: Sales Tax Policy Discussion

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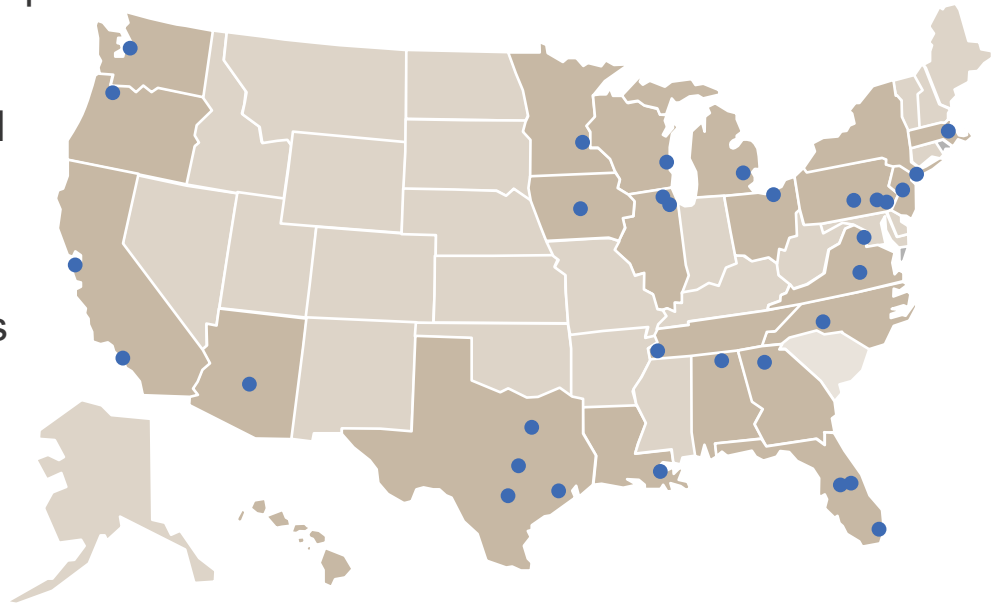
Today's Agenda

- Introduction to PFM
- Background on county revenue structures in the U.S.
- Current revenue challenges
- Racine revenue structure
- Wisconsin county revenue structure
- Revenue structure SWOT analysis
- Local option sales tax
 - History
 - SWOT analysis
- Summary and conclusion



Introduction to PFM Group Consulting

- **PFM Group Consulting** works at the intersection of policy, operations, and budgeting to help solve our clients' toughest problems. Our experienced consultants focus on the complex challenges faced by public sector leaders and deliver in-depth analysis.
- **Randall Bauer, Director** leads PFM Group Consulting's tax policy practice. He has managed over 50 state and county tax-related projects over his 19 years at PFM. Prior to joining PFM, Randy was the Budget Director for the State of Iowa and a Senior Adviser on budget, tax, and economic development issues for the Iowa State Senate.
- PFM currently has over 300 employees located in 32 offices and locations across the United States, including an office in Milwaukee.
- PFM's Financial Advisory practice is the current Financial Advisor to Racine County.

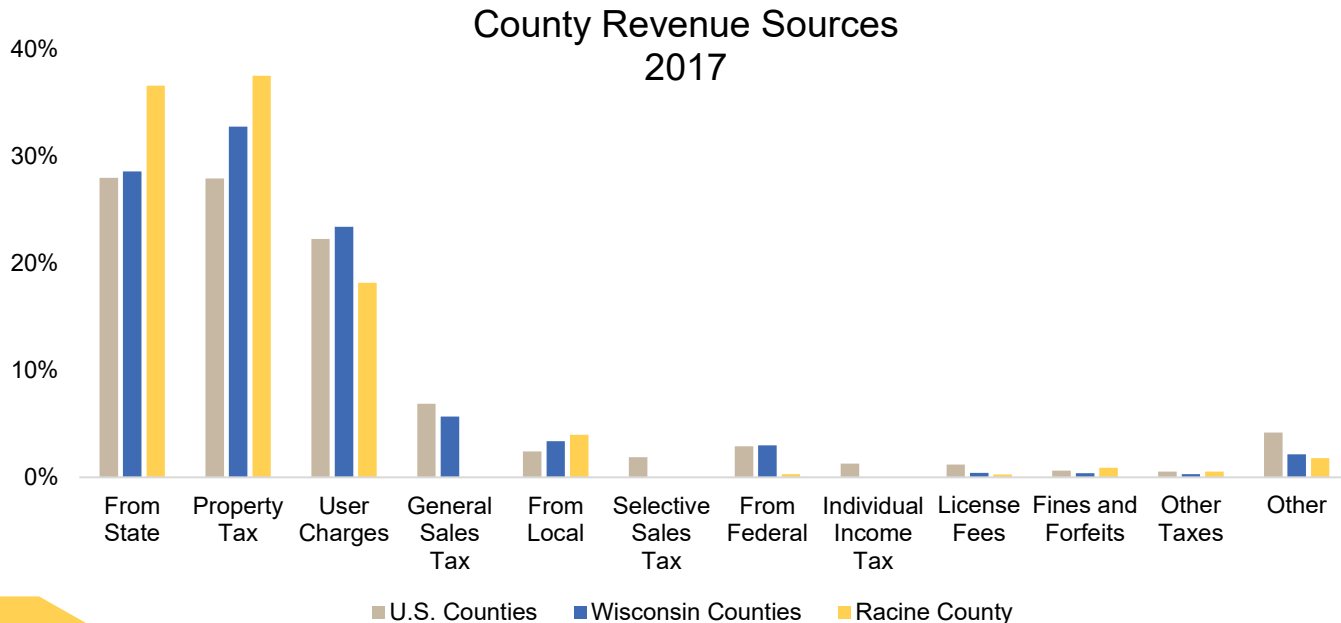


According to PFM Internal Resources as of June 30, 2024



Introduction: County Revenue Sources in the U.S.

- County governments throughout the United States collect revenue from a variety of sources.
 - These include taxes, primarily property, but also often general sales and use taxes.
 - Their own-source revenue also includes fines, fees, permits, and other user charges
 - Other source revenue primarily includes intergovernmental (state and federal) payments.
 - Depending on specific services offered by the County (for example, where there are county hospitals or ambulance services), the specific revenue sources of revenue can vary considerably from government to government.
- The mix of revenues has changed somewhat over time, primarily through a reduction in the reliance on the property tax.

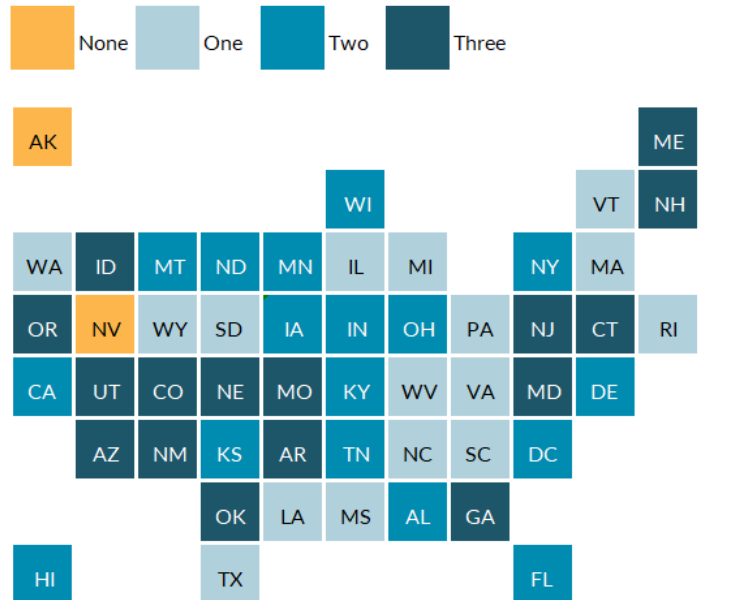




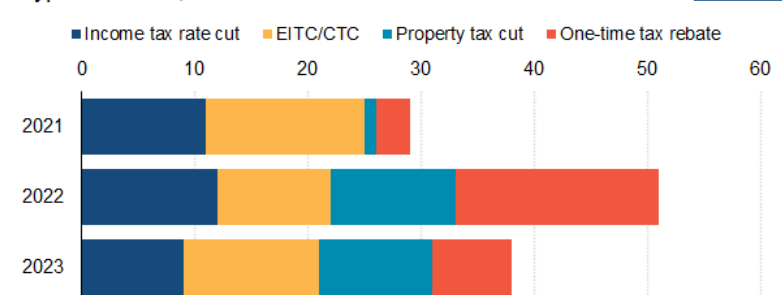
Non-local Revenue Sources Are Drying Up

- COVID relief (\$350 billion) for state and local governments nearing its end.
 - Funds must be committed by 12/31/24.
 - Must be spent by 2026.
- Most states enacted significant tax cuts in recent years.
 - Wisconsin 2021: \$1 billion income tax cut
 - Additional 2024: Child/dependent tax credit
- As a result, forecast state tax collections for 2024 are, on average negative.
 - Highly unusual for a full employment economy
 - Wisconsin made a \$439 million reduction in its biennial revenue forecast.
 - The state still has a strong (but shrinking) budget surplus.
- In general, states look to reduce local assistance during periods of budget pressure.
 - Shared revenue has grown in the past – but there are no guarantees.
 - Implementation of a local option sales tax can prevent cuts to essential services as other revenue sources are reduced.

Number of years each state passed a tax cut
2021 to 2023



Number of tax cuts passed each year
Type of tax cut, 2021 to 2023

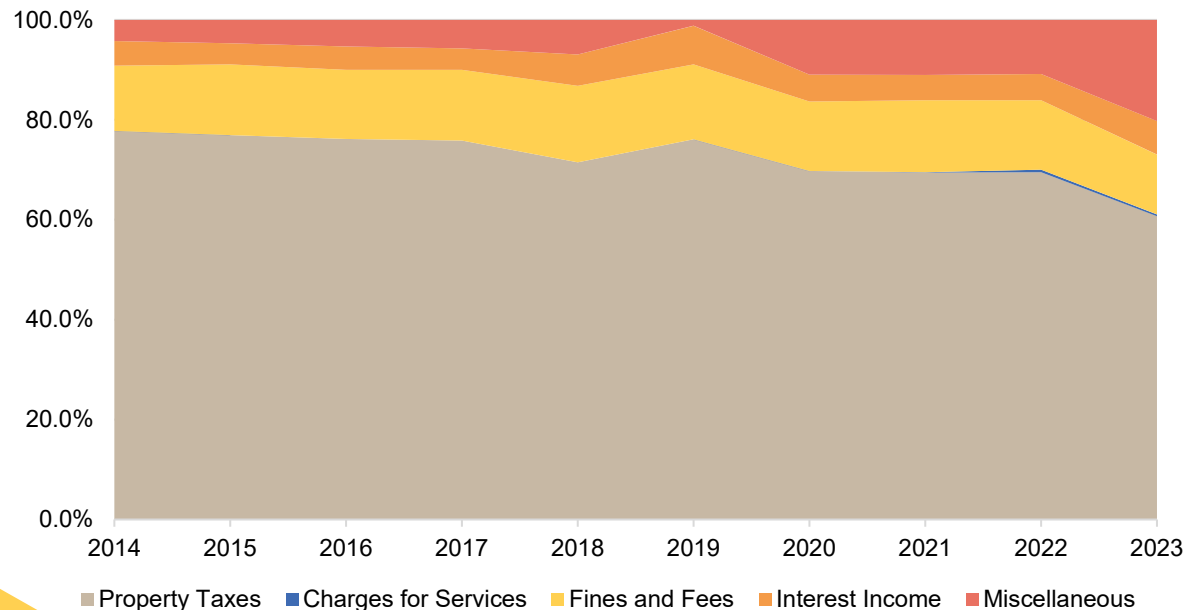




Racine County Own-Source Revenue

- Property taxes make up the majority of Racine County's own-source revenue, or revenue that is originated in Racine County. Despite this, property taxes as a portion of own-source revenue have declined significantly over the past decade, going from 77.8% in 2014 to 60.7% in 2023.
- The effective property tax rate in Racine County is 1.89 mills, compared to the average countywide rate of 2.725 mills. The effective property tax rate reflects the actual property tax burden as a percentage of the property's market value. The lower effective rate suggests that assessed values are lower than market values.

Own-Source Revenue, 2014-2023

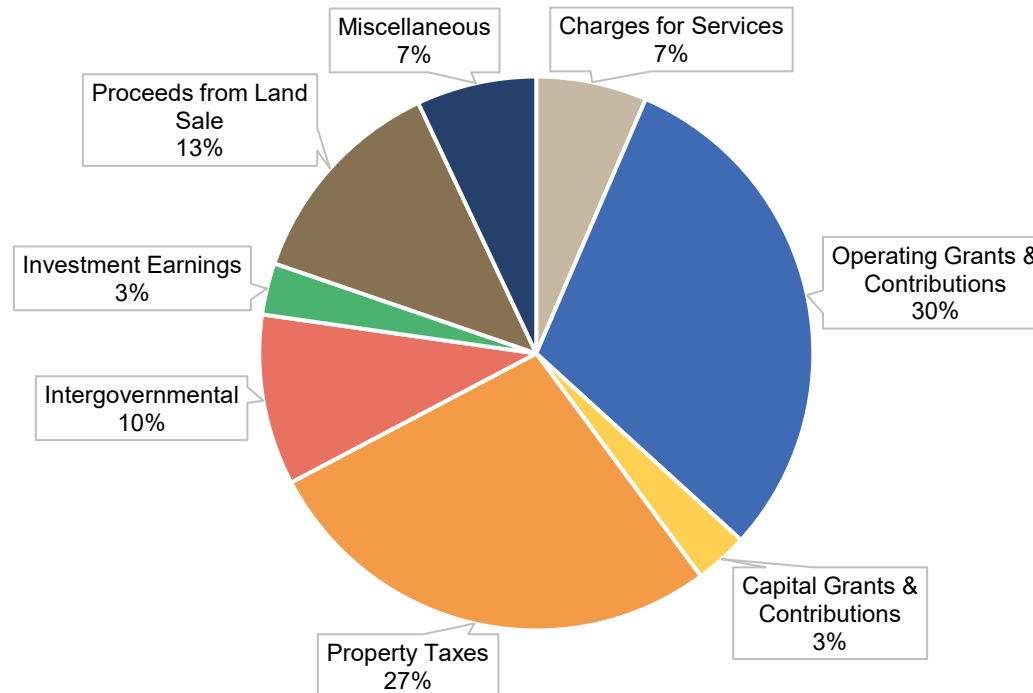




Racine County Revenue Structure (continued)

- While property tax collections have remained consistent since 2018 with a Compound Annual Growth Rate (CAGR) of 3.35%, as a percent of operating revenue, they have gone from 46.7% to 27.4%.
- Operating grants and contributions as a percent of revenue peaked in 2021 at nearly 40%, largely driven by COVID-related ARPA funding. It has been decreasing year-over-year since 2021, falling to 30.3% in 2023.

Revenue by Source - Governmental Activities (2024)

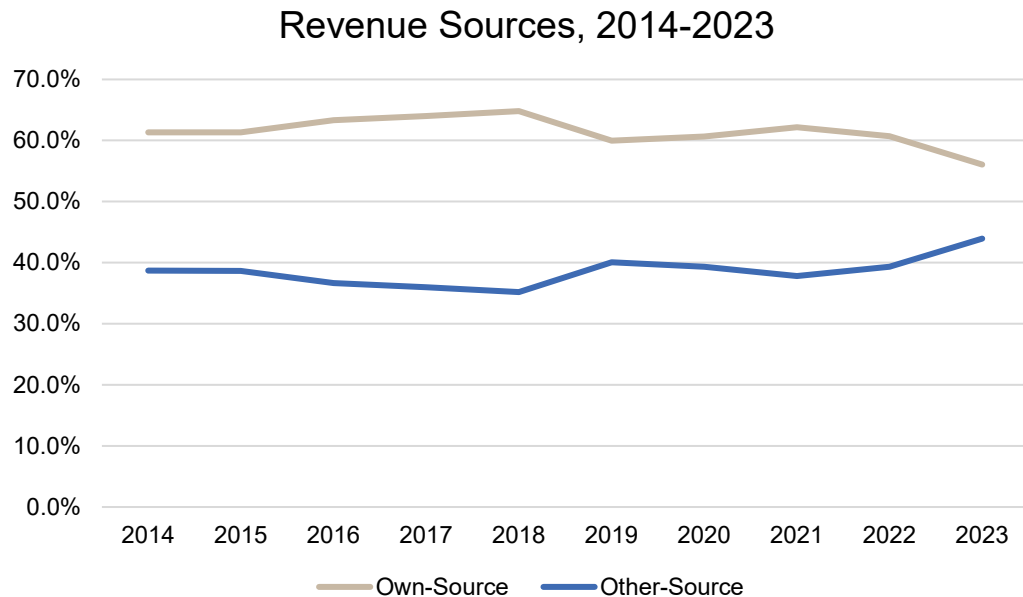


Note: Miscellaneous Revenues include self-funded insurance premiums or rebates, jail canteen revenues, accident and towing reimbursements, sale of materials or equipment, and vending machine revenues.



Racine County Revenue Source Changes

- The past five years have seen higher than average reliance on other-source revenues, with own-source revenue declining from 64.8% in 2018 to 56.1% in 2023.

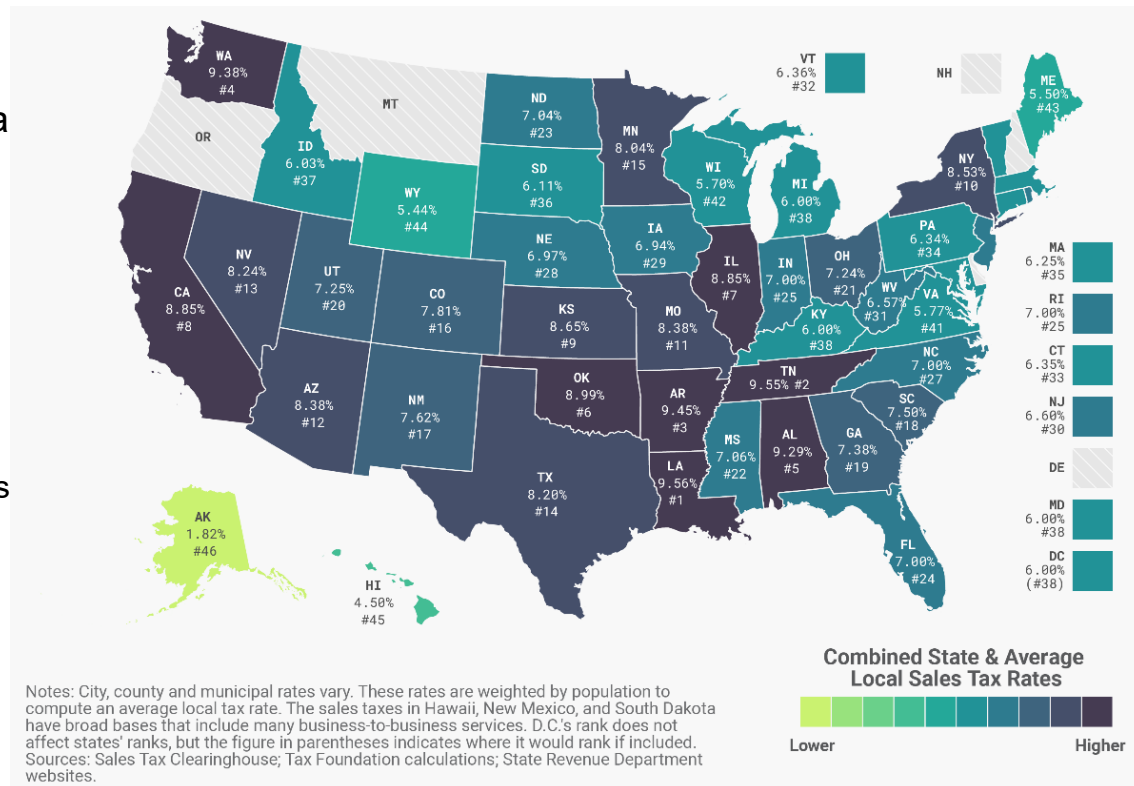




Wisconsin state tax structure – sales and use tax rates

- Sales tax is second largest state revenue source.
- State sales and use tax rate is 5.00% - 18th lowest among states.
- Average local rate is 0.696%, with a high of 2.90%. The City of Milwaukee levies an additional 2.00% rate.
- In most counties the local sales tax rate is a standard 0.5%.
 - Racine is limited to a 0.5% local option rate. The lack of implementation puts its budget at a competitive disadvantage compared to surrounding counties with a local rate imposed.
- Combined state and average local rate is 5.70%.
- This is among the lowest of the states with a sales tax.

Combined State and Average Local Sales Tax Rates, January 2024

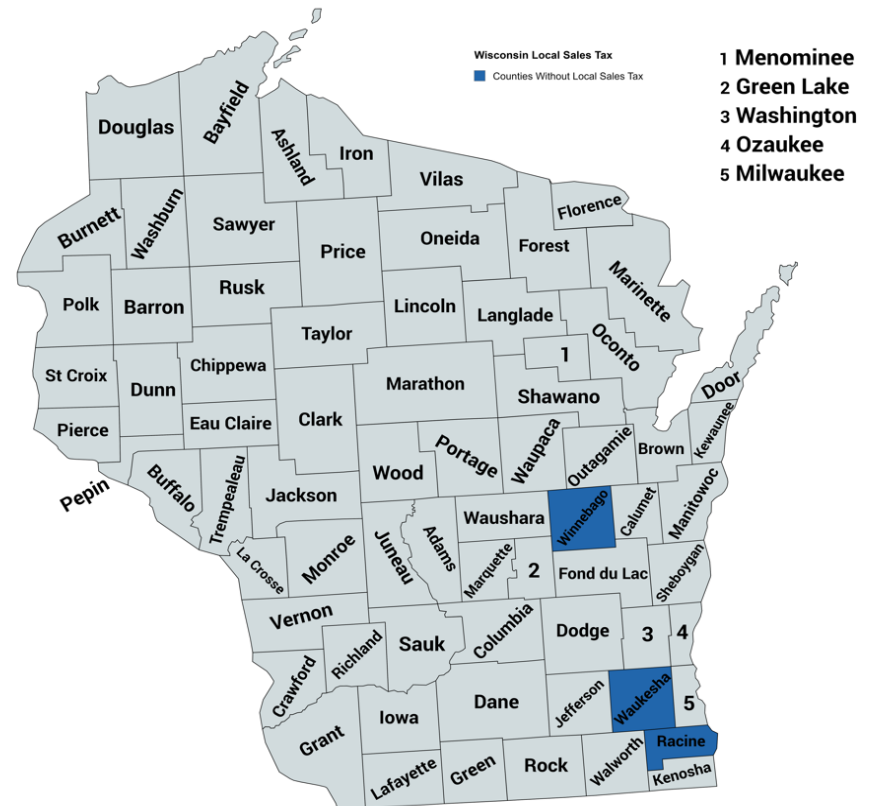


Source: Tax Foundation



Wisconsin Sales and Use Tax Continued

- In 1969, counties were given the authority to impose a sales tax.
 - Barron and Dunn counties were the first to enact a county sales tax (1986).
 - Menominee and Outagamie have been the most recent adopters (2020).
 - The county sales tax rate is fixed at 0.5%, which is 50 cents on a \$100 purchase.
- 69 of Wisconsin's 72 counties levy a local option sales tax. Racine is one of the three counties that does not.
- Manitowoc approved a sales tax in July 2024 to start in January 2025.



Source: Wisconsin Department of Revenue



Local Option Sales Tax: SWOT Analysis

- Revenue options analysis begins with a SWOT (strengths, weaknesses, opportunities, and threats) analysis.
- Strengths identifies alignment with tax policy principles and best practices, such as:
 - Equity: is it fair to similar and different taxpayers?
 - Efficiency: does the tax have substantial effect on the local economy?
 - Sufficiency: Will it generate substantial revenue?
 - Stability: Is it susceptible to large increases/decreases based on market conditions?
 - Ease of administration/compliance: Is it readily understood/easy to administer?
- Weaknesses identifies divergence from tax policy principles and best practices.
- Opportunities focus on how external forces might increase revenue sources or collections. Example: increased use of e-cigarettes has led to it being taxed in 19 states.
- Threats illustrate possible scenarios where tax or revenues are eliminated or reduced. Example: growth of consumption of services has eroded the sales tax base in most states.



County Sales Tax: SWOT Analysis

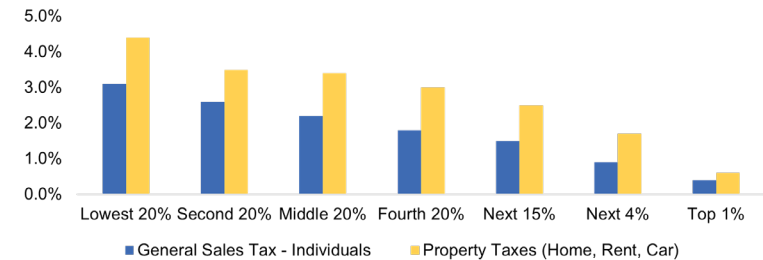
- Strengths identifies alignment with tax policy principles and best practices, such as:
 - Equity: is it fair to similar and different taxpayers? **Taxpayers pay the same rate for taxable goods and services.**
 - Efficiency: does the tax have substantial effect on the local economy? **There is no perfect tax, and it may limit some consumption. However, the surrounding counties mostly all already levy the tax.**
 - Sufficiency: Will it generate substantial revenue? **Estimates are \$20-\$25 million a year.**
 - Stability: Is it susceptible to large increases/decreases based on market conditions? **Sales taxes may decline during economic downturns, but less so than, for example, income taxes.**
 - Ease of administration/compliance: Is it readily understood/easy to administer? **Already levied at the state level, so businesses and consumers are aware of it and used to paying it.**
- Additionally, Revenue diversification is an advantage of adding the sales tax.
 - Primarily relying on a few revenue streams, like property taxes or state grants, creates risk.
 - Economic downturns, policy changes, and real estate market shifts can have negative impacts on these revenue streams. Diversification helps spread the risk, making budgets more resilient.
 - Similarly, constraints on how revenue is used can make it more difficult to respond to revenue fluctuations associated with market changes and operational challenges in a timely manner.



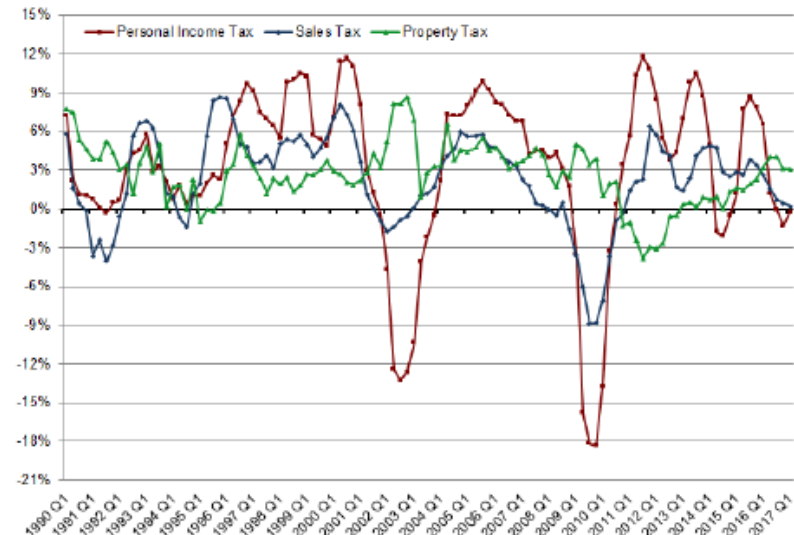
County Sales Tax: SWOT Analysis

- **Weaknesses** identifies divergence from tax policy principles and best practices.
 - Sales taxes are typically regressive, disproportionately impacting lower-income residents.
 - Tax burden analysis looks at the overall percentage of income that is paid in taxes.
 - Wisconsin does exempt groceries and prescription drugs from the sales tax, reducing the negative impacts on lower-income residents.
 - Overall, the Institute on Taxation and Economic Policy ranks Wisconsin's tax structure as **slightly better than average** on equity (23rd of 50 states).
 - Property taxes are regressive and place **an even greater disproportionate burden** on lower-income households.
 - Revenue from sales taxes can fluctuate with the economy, making them less stable than property taxes (but more stable than income taxes).
 - Numerous studies show that sales taxes can lead to cross border competition, particularly for high dollar value durable goods. Racine County borders Waukesha County, which also does not have a county sales tax but is considering one. Implementation in Racine may drive consumers to do more of their shopping in Waukesha. However, the slight difference in tax here makes it less likely (\$100 purchase = \$0.50 additional tax).

Tax Burden by Income Cohort, 2023



Inflation-Adjusted Major Tax Growth Rates

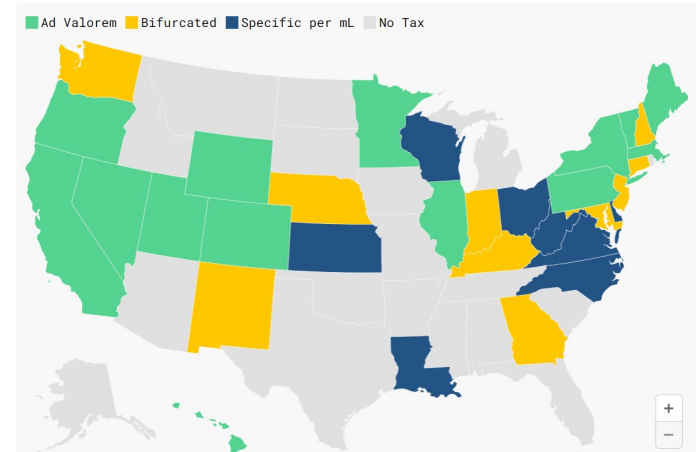




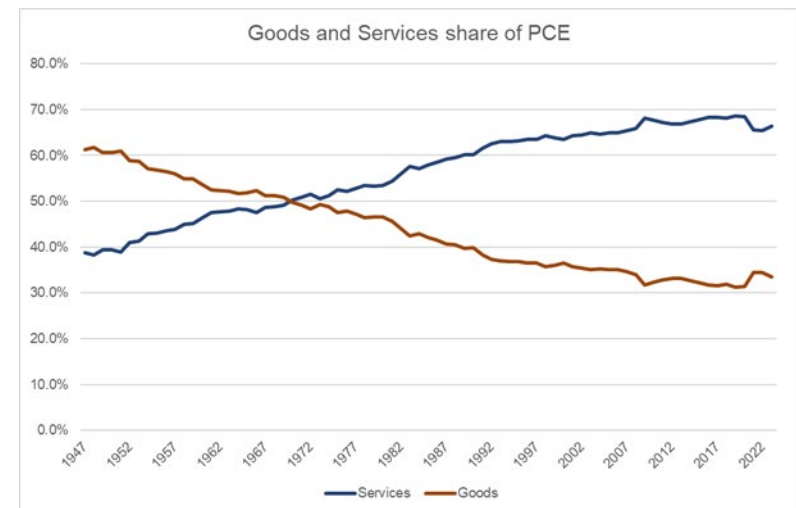
County Sales Tax: SWOT Analysis

- **Opportunities** focus on how external forces might increase revenue sources or collections. Example: Minnesota 1st state to tax e-cigarettes (2011), now 32 states impose them.
 - Sales tax application to digital applications in other states is expanding the tax base – should Wisconsin also do so, there is the likelihood that the revenue forecasts would be increased.
 - A variety of states are shifting away from individual income taxes and toward consumption taxes. This is also often accompanied by base expansion (such as to consumer services).
- **Threats** illustrate externally driven possible scenarios where tax or revenues are eliminated or reduced.
 - The increase in consumption of services has eroded the base in most states.

States that Tax e-Cigarettes, June 1, 2024



Goods and Services share of PCE



Sources: CBS News, Bureau of Economic Analysis, PFM



Summary

- The primary revenue sources for county governments in the U.S. are the property tax, intergovernmental transfers, and charges for services.
 - Sales and use tax are the second largest source of tax revenue.
 - Others vary from state to state and include excise, real estate transfer, and hotel-motel taxes.
 - The mix of revenue has changed somewhat over time, primarily through reduced reliance on the property tax. This is the case for Racine County as well.
- Revenue structures are under pressure.
 - There is no perfect tax – they nearly all result in some loss of economic activity.
 - The major taxes are viewed by the public as too high and unfair.
 - State legislatures (including in Wisconsin) frequently put in place property tax limits.
- Non-local revenue sources are drying up.
 - COVID-related federal assistance must be committed by the end of 2024.
 - States (including Wisconsin) have enacted substantial tax cuts, and revenue growth is declining.
 - As state budgets get tight, state assistance, such as shared revenue, often gets tight as well.
- Most Wisconsin counties have enacted a sales and use tax.
 - Authority granted in 1960, first counties imposed in 1986, 68 out of 72 counties currently use it, with Manitowoc's going into effect in January 2025.
 - As a result, Wisconsin counties in the aggregate rely less on real property tax than Racine County.



Summary: Sales and Use Tax SWOT Analysis

- It generally aligns with key tax policy principles.
 - Same rate, broad base, and widespread use address equity, sufficiency and ease of compliance.
 - It also diversifies the revenue structure, which reduces overall system risk.
- There is no perfect tax, and the sales tax has its flaws as well.
 - It is regressive - lower income households paying a greater percentage of their income as sales tax.
 - Wisconsin does exempt groceries and prescription drugs from sales tax.
 - The property tax in Wisconsin is even more regressive.
 - It may lead to cross-border competition with Waukesha County.
- Future opportunities to expand the sales tax base and collect more revenue.
 - Application to digital goods in other states.
 - Possible to expand the base to include more services.
- Changes in consumption have eroded the sales tax base.
 - Over 50 years, personal consumption has flipped, from 2/3rds tangible goods to 2/3rds services.
 - This is part of the reason sales tax rates have climbed in many states – but may be reaching a psychological ceiling when combined state and local rates get to 10 percent.



Questions and Discussion