Massachusetts Taxpayers Foundation

April 5, 2019

Further Analysis of Governor Baker's FY 2020 Budget

On January 23, 2019, Governor Charlie Baker filed House 1, the Governor's Budget Recommendation for fiscal year 2020. The bill seeks legislative authorization for $43.2 billion in spending.[1]

In the eight weeks since Governor Charlie Baker released his spending plan for fiscal year 2020, the proposal has been the subject of significant analysis and debate. This policy brief serves as an update and addendum to MTF's original analysis of February 4, 2019.

Major Moving Pieces of the FY20 Budget

A comparison of fiscal 2020 projections to fiscal 2019 estimates highlights the major moving pieces of the Governor's Budget Recommendation. These are summarized in Figure 1.[2]

Tax Revenue

The Consensus Tax Revenue (CTR) agreement between the administration and the legislature establishes common tax revenue assumptions for fiscal 2020 budget planning. On December 31, 2018, the Secretary of Administration and Finance and the Chairs of the House and Senate Ways and Means Committees announced a CTR agreement for the budget development process that projects tax revenue growth of 2.7%, or $770 million, over revised fiscal 2019 benchmarks, excluding tax revenue generated by the sale of recreational marijuana.

The Governor's budget also includes a series of tax revenue initiatives to generate additional revenue. Net of required transfers for other purposes, the CTR agreement

[1] Calculation excludes $607 million for intragovernmental service fund spending that has no net impact on spending or statutory balance.

[2] Fiscal 2019 data as of January 23, 2019. Items express variances between fiscal 2019 and fiscal 2020 estimates as the net impact to statutory balance.

plus the recommended tax initiatives add $1.1 billion in new budgeted revenue in fiscal 2020.[3]

Gaming Revenue

House 1 includes $160 million from additional gaming revenue in fiscal 2020. Most notably, budget projections assume the Encore Boston Harbor casino will open on or before July 1, 2019 and, in combination with revenue from MGM Springfield, generate an additional $98 million in generally available revenue.[4]

Further, the Governor filed legislation to expand and regulate sports wagering on January 22, 2019.[5] Fiscal 2020 estimates anticipate $35 million in revenue from this legislation. The budget also anticipates using $28 million from the Debt Defeasance and Long-Term Liabilities Fund, an off-budget fund supported by gaming revenues, to support relevant costs in fiscal 2020.

EJ Sullivan Courthouse

The Commonwealth has been working through the legal process associated with the sale of the Edward J. Sullivan Courthouse in Cambridge for several years. Budget plans have included revenue associated with the transaction at various points in time since at least fiscal 2014. The Governor's budget assumes the sale will be completed in fiscal 2020, generating $28 million in non-recurring revenue.

Abandoned Property

Abandoned property (also called "unclaimed property") escheats to the Commonwealth after statutorily-defined time periods, depending on the type of asset (stocks, checking accounts, etc.). The Unclaimed Property Division of the Treasurer's office attempts to locate property owners through several mechanisms, including most notably the website findmassmoney.com.[6]

After several rounds of de-mutualization and other initiatives to locate abandoned property that resulted in unusually high revenue from this source between fiscal 2016

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[3] See Appendix I for additional analysis of the CTR agreement and Appendix II for further description of the proposed tax revenue initiatives.

[4] This figure excludes $16 million in gaming revenue scheduled for deposit to the Stabilization Fund.

[5] H.68, An Act Expanding Sports Wagering in the Commonwealth

[6] http://www.findmassmoney.com is maintained by the State Treasurer's Unclaimed Property Division

and fiscal 2019, the Commonwealth expects to generate $81 million from the sale of abandoned property in fiscal 2020, $43 million or 35% less than fiscal 2019.

FY20 Major Moving Pieces vs FY19 Estimates	
Starting Point	
FY19 Balance	***-36.2***
Revenue Changes	**$ Change vs FY19**
Tax Growth	1,105.6
Gaming Revenue	160.5
EJ Sullivan Courthouse	28.3
Abandoned Property	-43.4
EMAC Expiration	-225.9
Subtotal, Revenue Changes	**1,025.0**
Spending Changes	
Education	-323.0
Pensions	-204.2
Other HHS	*-72.8*
MassHealth	*-44.0*
Subtotal, MassHealth and Other HHS	-116.8
State Employee Health Insurance (GIC)	-79.5
Debt Service	-62.5
All Other Changes	-200.1
Subtotal, Spending Changes	**-986.1**
FY20 Balance	***2.6***

Notes:

Figures express net impact on balance

Figures in $ millions. Totals may not add due to rounding.

Figure 1: Net impact on balance of major moving pieces in FY20 vs FY19 estimates

EMAC Expiration

In Governor Baker's FY2018 budget proposal, he proposed to assess employers almost $700 million annually to help offset the growing cost of MassHealth benefits that he attributed to employers dropping coverage. MTF played a critical role in identifying reasons for the growth in MassHealth not attributable to employers that resulted in a more narrowly crafted and temporary assessment known as the enhanced Employer Medical Assistance Contribution (EMAC).[7]

The charge is scheduled to expire at the end of calendar year 2019. The Governor's fiscal 2020 budget includes $87 million in enhanced EMAC revenue, a decrease of $226 million compared to fiscal 2019 as it phases out.

If the fiscal 2020 budget picture deteriorates materially either during the planning process or through the fall, there may be attempts to extend the EMAC that will be met with considerable resistance from employers.

Education

Education finance reform is arguably the centerpiece of the Governor's policy agenda for the current legislative session. The Governor seeks a host of changes to the funding formulas that direct education-related aid to cities and towns in the Commonwealth, known as Chapter 70, and for charter school reimbursement costs.

The Chapter 70 reforms increase estimated spending for this item by $200 million in fiscal 2020 as part of a seven-year phase-in effort for the reform package. Charter school reimbursements would increase by an additional $16 million under the plan.

The Governor's budget proposal also implies significant new net costs versus fiscal 2019 related to early education and care ($56 million) and higher education funding for UMass, the state university system, and community colleges ($51 million).

Pensions

The triennial pension funding schedule governing contributions to the state retirement system increases by 8.9% annually. In fiscal 2020, this increase will direct an additional $233 million to the Pension Liabilities Trust Fund, for a total contribution of $2.84 billion. The increases are partially offset by charges to federal grants and other funds supporting employee compensation, resulting in a net increase of $204 million. The triennial schedule will be revisited again as part of the fiscal 2021 budget development process.

[7] See, for example, The Baker Administration's Proposed Fair Share Assessment, March 10, 2018

MassHealth and Other Health and Human Services

<u>MassHealth</u>

MassHealth Growth Analysis				
With FY19/FY20 Timing Shift	**FY19**	**FY20**	**$ Change**	**% Change**
Total Spending	16,528.5	16,538.8	10.3	0.1%
Revenue Offsets	9,899.5	9,865.7	-33.7	-0.3%
Net Spending	6,629.1	6,673.1	44.0	0.7%
Without FY19/FY20 Timing Shift				
Total Spending	16,306.3	16,761.0	454.7	2.8%
Revenue Offsets	9,777.2	9,987.9	210.7	2.2%
Net Spending	6,529.1	6,773.1	244.0	3.7%

Notes:

Figures in $ millions

Revenue offsets exclude enhanced EMAC

Figure 2: Impact of FY19/FY20 Timing Shift on MassHealth Spending Growth

As published, MassHealth spending growth is projected to increase only $10 million, or 0.1% over fiscal 2019. The Governor's Budget Recommendation assumed $222 million gross, $100 million in net costs that could belong in fiscal 2019 or fiscal 2020 are "pulled forward" to fiscal 2019. Without this timing change, the total spending growth rate would be 2.8% over the adjusted fiscal 2019 base, and 3.7% growth on a net basis as depicted in Figure 2. In either scenario, the rate of growth is significantly smaller than the growth rate earlier in the decade.

MassHealth is required by federal law to make timely payments to providers regardless of statutory authorization. As a result, the legislature does not need to act proactively for the timing shift to occur. If fiscal 2019 tax revenues fall substantially short of expectations, budget managers may choose not to execute this timing shift, reducing costs in the current year at the direct expense of fiscal 2020 of up to $100 million on a net basis.

Other Health and Human Services

Health and human services other than MassHealth represent a fast-growing component of the Commonwealth's budget. As filed, the Governor's budget anticipates $73 million in net new costs associated with programming in this area.

Notably, projections include $91 million in net new spending at the Department of Developmental Services (DDS) to support individuals with intellectual and developmental disabilities. Additional net increases at the Department of Mental Health, the Department of Public Health, the Department of Children and Families, and other agencies are offset by other related revenue changes with a positive impact to balance of $18 million. This amount includes a reserve to increase rates for service providers that will be distributed to numerous agencies, including DDS.

State Employee Health Insurance

The Commonwealth provides health insurance for more than 440,000 people. Though the Group Insurance Commission (GIC) has made significant efforts to control costs in recent years, the rising cost associated with providing health insurance coverage is a challenge for many employers, including the Commonwealth.

Including transfers to the State Retiree Benefits Trust Fund (SRBTF) and net of reimbursements from municipalities and offsetting revenue from federal grants and non-budgeted trust funds, GIC spending is expected to increase about $80 million in fiscal 2020, or 8.3% over fiscal 2019.

In recent years, GIC cost projections have significantly exceeded actual costs. In fiscal 2018, for example, the GIC spent $116 million less than authorized by the legislature as a result of cost-control efforts. GIC estimates may represent overly-conservative assumptions about future costs.

Debt Service

The Commonwealth expects to spend almost $2.6 billion on debt service costs in fiscal 2020, an increase of $88 million over the fiscal 2019 projection.

Debt service costs interact with additional funding for the unfunded liabilities associated with Other Post-Employment Benefits (OPEB) through a somewhat complicated arrangement involving the Commonwealth's share of the Master Settlement Agreement (MSA) with tobacco companies. These transfers are calculated based on the annual MSA payment amount but are statutorily required to be paid with unspent balances in certain debt service accounts.

Once the fiscal year begins, fiscal managers must determine whether the unspent balances will be enough to support OPEB transfers, and then account for the difference with general revenue. This arrangement allows planners to essentially double-count debt service spending during the budget development process and acts as "savings" in comparison to the current year. Net of this accounting, in fiscal 2020 debt service costs are expected to rise $63 million over fiscal 2019.

All Other Changes

All other spending and revenue changes have a net cost of $200 million. These items include trial courts ($31 million), unrestricted local aid to cities and towns ($30 million), public safety ($25 million), other non-executive offices and agencies ($21 million), the employer-share costs of providing paid family and medical leave to employees on budgeted accounts ($18 million), sheriffs ($16 million), and other programs and structural adjustments ($59 million).

Total Spending & Trends

As filed, the Governor's spending plan projects total fiscal 2020 budgeted expenditures and transfers of $46.1 billion, includes the annual state contribution to the Pension Liabilities Trust Fund of $2.84 billion, $28 million in spending or transfers authorized in other legislative actions, and an anticipated $26 million in spending authorized in fiscal 2019 and continued into fiscal 2020. In total, this spending level represented growth of $776 million (1.7%) over fiscal 2019 estimates as of January 23, 2019.

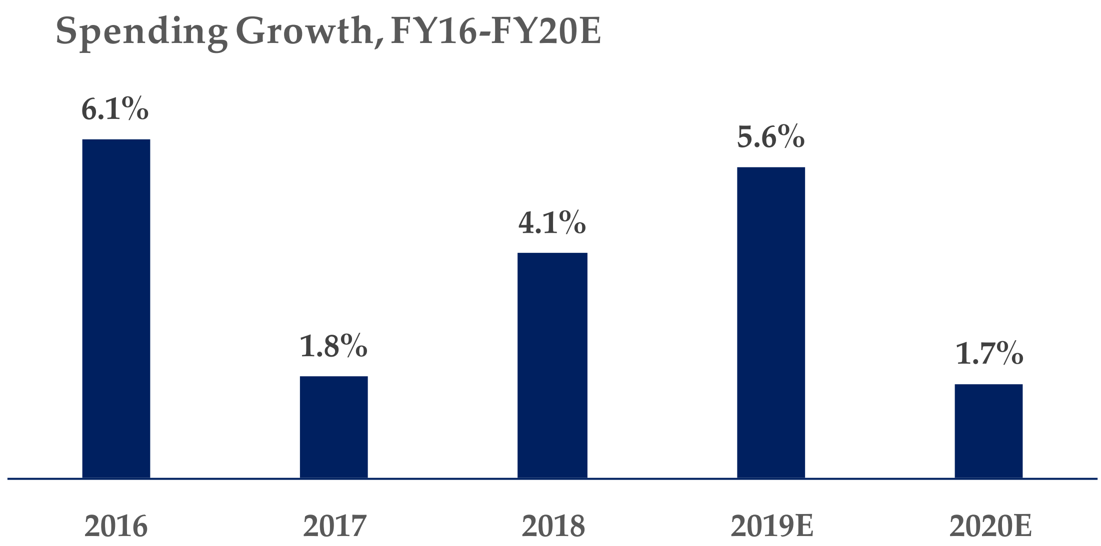

Figure 3: Budgeted Expenditures and Other Uses Growth, FY16-FY20E

Year-over-year growth rates are susceptible to large changes due to revenue or spending in any given year, as depicted in Figure 3. Using a trend analysis based on 4-year rolling compound annual growth rate (CAGR), Commonwealth budgeted spending has moderated in recent years, declining from a high of 5.7% in fiscal 2016 to 3.3% projected in fiscal 2020 as shown in Figure 4. This is largely driven by spending growth changes at MassHealth, supplemental payments to hospitals made through the Medical Assistance Trust Fund (MATF), and other changes.

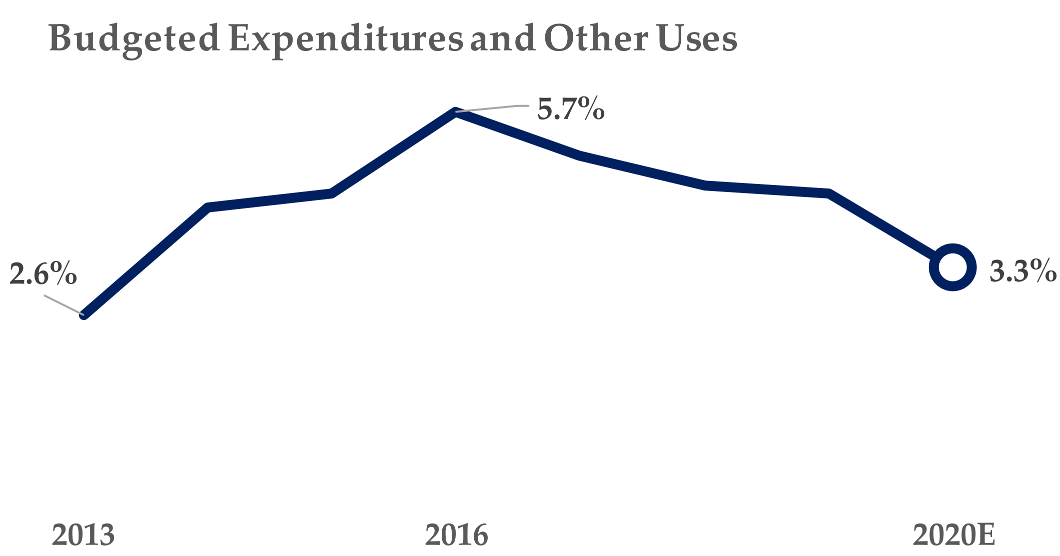

Figure 4: Budgeted Expenditures and Other Uses, 4-YR Rolling CAGR FY16-FY20E

Conclusion

As highlighted in MTF's earlier analysis of February 4, 2019 and the above further analysis, the Governor's Budget Recommendation includes many recommendations advanced by MTF in recent years, such as building reserves in the Stabilization Fund, reducing the structural imbalance between revenue and spending, and taking steps to curtail the rate of growth at MassHealth.

Conversely, it is also apparent the Governor's Budget Recommendation relies on several significant assumptions, such as the passage and implementation of numerous tax revenue initiatives, the MassHealth timing shift, agreement on broad changes to major education cost sharing formulas that govern the relationship between the Commonwealth and cities and towns, and most fundamentally, the continuation of an economic cycle that in July will be longer than any other since the end of World War II. If any of these assumptions do not hold, after a brief respite in fiscal 2018, fiscal managers will be again forced to implement midyear revenue and spending adjustments to achieve balance.

Appendix I: Analysis of Consensus Tax Revenue and Tax Revenue Initiatives

Consensus Tax Revenue

Forecasting tax revenue for the upcoming fiscal year is a key component of the budget development process. Pursuant to state finance law, the Secretary of Administration and Finance and the House and Senate Committees on Ways and Means agree on a Consensus Tax Revenue (CTR) estimate for the upcoming fiscal year.[8] The negotiated figure establishes a common tax revenue estimate available for each budget proposal, excluding revenue committed to the Massachusetts Bay Transportation Authority (MBTA), Massachusetts School Building Authority (MSBA), Workforce Training Trust Fund, and the Pension Liabilities Trust Fund.

On December 31, 2018, the Secretary of Administration and Finance and the Chairs of the House and Senate Ways and Means Committees announced a CTR agreement for the fiscal 2020 budget development process that projects tax revenue growth of 2.7%, or $770 million, over revised fiscal 2019 benchmarks, excluding tax revenue generated by the sale of recreational marijuana. Adjusted for the caveats as shown in Figure 5, the CTR agreement represents assumed tax revenue growth of 3.7%, or $1.04 billion, over the original fiscal 2019 tax estimates.

Notably, $255 million in enacted tax law changes are embedded in the tax revenue projections, including $179 million in income tax reductions, $65 million in revenue loss for the expanded Earned Income Tax Credit (EITC), $65 million from the loss of one-time corporate deemed repatriation revenue, $8 million from the permanent sales tax holiday, and $6 million in other changes. These are offset by the projected $70 million in additional tax revenue in fiscal 2020 from recreational marijuana.

After adjusting for the tax law changes noted above, the CTR agreement is based on underlying economic growth of 4.6%, and nearly $1.3 billion in additional revenue compared to fiscal 2019. DOR's forecasted midpoint for baseline economic growth was 4.1%, implying the fiscal 2020 benchmarks are $130 million more aggressive than the DOR midpoint forecast.[9]

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[8] M.G.L. Chapter 29, Section 5B

[9] The FY20 DOR Briefing Book indicated 4.2% baseline growth compared to the FY19 benchmark. DOR indicates this is a rounded figure from 4.1%.

The CTR agreement is broadly consistent with the baseline growth assumptions projected by MTF at the time of the CTR hearing. Adjusted for caveats, MTF projections indicated tax revenue growth of 4.6% over the original fiscal 2019 benchmarks, and 3.2% growth over the MTF-recommended revised fiscal 2019 tax estimate. The CTR agreement is $19 million more conservative than the MTF baseline growth assumption.

Consenus Tax Revenue Analysis				Figures in $ millions.
Estimated Tax Revenue Growth	FY19	FY20	$ Change	% Change
Original FY19 Estimate	28,392.3	29,299.0	906.7	3.2%
December Revision	200.0	0	-200.0	-100.0%
Revised FY19	28,592.3	29,299.0	706.7	2.5%
Back out Recreational Marijuana	-63.0	0	63.0	-100.0%
Consensus Tax Revenue (CTR)	**28,529.3**	**29,299.0**	**769.7**	**2.7%**
Add Recreational Marijuana (RM)	63.0	132.5	69.5	110.3%
CTR with RM vs Revised FY19	28,592.3	29,431.5	839.2	2.9%
Back out December Revision	-200.0	0	200.0	-100.0%
CTR with RM vs Original FY19	28,392.3	29,431.5	1,039.2	3.7%
Baseline Tax Revenue Growth				
CTR with RM vs Original FY19	28,392.3	29,431.5	1,039.2	3.7%
Add Tax Law Changes	0	254.6	254.6	
CTR Baseline Tax Revenue vs Original FY19	28,392.3	29,686.1	1,293.8	4.6%
Variance from DOR Forecast				
DOR Midpoint Forecast - Baseline Growth	28,392.3	29,556.4	1,164.1	4.1%
CTR Baseline Tax Revenue vs DOR Midpoint Forecast		**129.7**		
Variance from MTF Forecast				
Original FY19 Estimate	28,392.3	29,469.0	1,076.7	3.8%
Back out RM	-63.0	0.0	63.0	-100.0%
MTF Recommended Revision	459.7	0.0	-459.7	-100.0%
MTF CTR Recommendation	**28,789.0**	**29,469.0**	**680.0**	**2.4%**
Add MTF-Assumed Tax Law Changes	0.0	235.9	235.9	
MTF Baseline Growth	28,789.0	29,704.9	915.9	3.2%
MTF Baseline Growth vs Original FY19	28,392.3	29,704.9	1,312.6	4.6%
CTR Baseline Tax Revenue vs Implied MTF Forecast		**-18.8**		

Notes:

Room occupancy tax modernization was adopted after the CTR agreement was concluded

The midpoint of the DOR FY20 baseline growth forecast was 4.1%, adjusted for rounding

MTF estimates excluded recreational marijuana and assumed the income tax rate would not change in FY20

Figure 5: Comparison of Baseline Growth Assumptions in Consensus Tax Revenue agreement

Appendix II: Tax Revenue Initiatives

Fiscal 2020 projections include tax revenue from thirteen notable initiatives. In sum, these total $699 million in fiscal 2020, of which $317 million is subject to appropriation as proposed by the Governor. Of these, two initiatives are already enacted and eight require further action by the Legislature, and three can or will be accomplished administratively.

Fiscal 2020 Tax Initiatives		
Enacted	**Total**	**Budgeted**
Recreational Marijuana	132.5	116.9
Transient Accommodation/Room Occupancy Tax	27.5	27.5
Subtotal, Enacted	**160.0**	**144.4**
Proposed		
Requires legislative action		
Sales Tax Acceleration	306.0	28.6
Deeds/Climate Change	75.0	0.0
Sales Tax Marketplace	41.7	28.4
Opioid gross receipts tax	14.0	14.0
Vaping	6.0	6.0
Sales Tax Integrity	2.0	1.8
Stamp Smokeless Tobacco	0.0	0.0
Requires administrative action only		
Life Sciences	5.0	5.0
Withholding on non-resident property sales	4.0	4.0
Subtotal, Proposed	**453.7**	**87.8**
Other Projections		
Tax-Related Settlements & Judgments	50.0	50.0
Tax Transfers		
Sports Wagering	35.0	35.0
Total Tax Initiatives	**698.7**	**317.2**
Figures in $ millions.		

Figure 6: Fiscal 2020 tax revenue initiatives

Already Enacted

Taxes on recreational marijuana and transient accommodation/room occupancy tax are already enacted in law. The Governor's Budget Recommendation anticipates $160 million in total revenue from these taxes, including $144 million in budgeted revenue.

Recreational Marijuana

The Governor's Budget Recommendation projects a total of $133 million from the sale of recreational marijuana in fiscal 2020, including $84 million from the marijuana excise tax, and $49 million from the regular retail sales tax, of which $16 million is pledged to the MBTA and MSBA. Net of those amounts, the Commonwealth expects to receive $117 million in budgeted tax revenue from the sale of recreational marijuana in fiscal 2020, an increase of $61 million over estimated fiscal 2019 figures.[10]

The retail sale of recreational marijuana began in Massachusetts on November 20, 2018.[11] Budget estimates for fiscal 2019 assume tax revenues of $63 million generated from sales and excise taxes on the sale of recreational marijuana. Though official documents acknowledge such revenues may be lower than projected, these estimates were not revised in December 2018.[12] Through February 2019, the sale of recreational marijuana had generated $5 million in revenue, far below the DOR projections of $26 million on a year-to-date basis.

These projections are highly dependent on the number of recreational marijuana retailers and the volume of sales at those establishments. As with any nascent industry, the tax revenue estimates rely heavily on assumptions that may or may not match actual experience.

Transient Accommodation/Room Occupancy Tax

The budget proposal includes $28 million from expanding the room occupancy tax to transient accommodations, also known as short-term rentals as facilitated by companies such as AirBnB.[13] The enabling legislation was adopted by the Legislature on December

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[10] A portion of the regular retail sales tax collected on recreational marijuana is pledged to the MBTA and MSBA.

[11] "Recreational Marijuana Sales Begin in Massachusetts, First on the East Coast" by Dan Adams, Michael Levenson, and Felicia Gans, Boston Globe, November 20, 2019.

[12] See Commonwealth Information Statement Dated November 29, 2019, page A-14, Other Taxes section.

[13] This tax is also sometimes referred to as the "AirBnB tax".

28, 2018 and envisions an effective date of July 1, 2019.[14] The associated revenue estimate was not included in the CTR agreement for fiscal 2020. Any delay in implementing related regulations and procedures associated with collecting and enforcing the tax may have a material impact on the full-year revenue estimate.

Requires Legislative Action

The Governor's budget includes eight initiatives requiring legislative action. In total, these items are expected to generate $480 million in total tax revenue in fiscal 2020, including $114 million in budgeted revenue.

Sales Tax Acceleration

The single largest initiative of the entire package relates to so-called sales tax acceleration. This measure is not a tax rate change, but rather a tax timing change that has incremental value in fiscal 2020. The Governor's proposal would require sales tax trustees, such as retailers, restaurants, or hotels, to remit sales tax during the final week of each month, rather than on the 20th day of the subsequent month as is current law. This timing change would generate $306 million in one-time revenue as affected businesses will be required to remit sales tax amounts twice in the month of implementation (one payment for "last month's sales tax collections" and one payment for "this month's collections").

As proposed by the Governor, none of this revenue would be allocated to recurring spending. Of the total $306 million, $200 million would be earmarked for non-budgeted special revenue trusts, including $100 million for higher education scholarships, $50 million for one-time costs associated with the Governor's K-12 education finance reform efforts, $30 million for school safety improvement grants, and $20 million to the Clean Water Trust to support drinking water de-leading efforts in schools. Approximately $77 million is pledged to the MBTA and MSBA. The remaining nearly $29 million is proposed to be deposited in the Stabilization Fund.

Deeds/Climate Change

The Governor's Budget Recommendation does not include or assume any budgeted revenue from an increased tax rate assessed on deeds. Instead, companion legislation proposes to change the deeds excise rate from 0.456% to 0.684% starting January 1, 2020, with the incremental value of the increase credited to the Global Warming Solutions

[14] Chapter 337 of the Acts of 2018

Trust Fund.[15] These funds are proposed to be allocated to cities and towns to address climate change without further appropriation by the legislature.

Sales Tax Marketplace

The Governor's Budget Recommendation includes $42 million in total revenue from requiring e-commerce platforms, such as eBay or Etsy, to collect and remit sales tax revenue on behalf of the vendors using their websites. Of this amount, approximately $13 million is pledged to the MBTA and MSBA, while the remaining $28 million would be available for the budget.

However, the draft language associated with this proposal may have unintended consequences. For example, the definition of entities required to remit sales taxes under this proposal may ensnare businesses not contemplated, such as GrubHub and other marketplace facilitators. The complexities associated with clarifying these questions likely requires further review and analysis by legislators before enactment.

Opioid Gross Receipts Tax

The Governor's Budget Recommendation includes $14 million in budgeted tax revenue from implementing a gross receipts tax on opioids sold in the Commonwealth to be paid by opioid manufacturers. Exemptions are identified for opioids sold for certain purposes, such as use in Medication Assisted Treatment (MAT) programs and for use in inpatient settings.

Vaping and E-cigarettes

The Governor's Budget Recommendation includes $6 million in budgeted tax revenue to be generated by extending the cigarette tax or recreational marijuana tax systems to e-cigarettes and vaping supplies.

Sales Tax Integrity

The Governor's Budget Recommendation includes $2 million in total revenue, of which approximately $1.8 million is budgeted, associated with enforcement around so-called "zapper" software, which enables businesses to essentially erase certain transactions in point-of-sale systems in order to avoid paying or remitting tax revenues to the Commonwealth. The $1.8 million in budgeted tax revenue is estimated to be comprised

[15] Senate Bill 10

of approximately $1.2 million in meals tax revenue, with lesser amounts from regular sales tax, corporate tax, and income tax revenues.

Stamp Smokeless Tobacco

The Governor's Budget Recommendation includes legislation to require a tax stamp on smokeless tobacco products, like the tax stamps required for cigarettes. This measure is aimed at reducing the sale of untaxed smokeless tobacco products. The time required to implement this new regime, including acquiring and distributing the necessary equipment, makes it unlikely any additional revenue would be realized from this action until fiscal 2021. The Governor's Budget Recommendation does not assume any revenue from this action.

Sports Wagering

The Governor's Budget Recommendation assumes $35 million in taxes, licensing fees, and other revenues associated with legalizing sports wagering in the Commonwealth in fiscal 2020. Largely modeled on the regulatory regime in New Jersey, this legislation would require vendors to remit a portion of gross gaming revenue daily to the Commonwealth, as is practice for resort-style casinos and slots parlors. In the first instance, this revenue would be paid to the Massachusetts Gaming Commission (MGC) and then subsequently transferred to the budgeted Gaming Local Aid Fund. As a result, it is not counted as tax revenue per se, but as rather as a transfer from MGC.

<u>Require Administrative Action Only</u>

Three initiatives require only administrative action by DOR to generate additional tax revenues, as the statutory authority to do so is already in place. Together, these items add $59 million in budgeted revenue.

Life Science Tax Cap

The Governor's Budget Recommendation includes $5 million associated with enforcing an administrative cap of $20 million on life science tax credits claimed by qualifying businesses in the Commonwealth. The current statute allows DOR to approve up to $25 million in life science tax credits to qualifying applicants, but for several years DOR has administratively enforced a lower cap of $20 million. This initiative assumes the lower cap of $20 million for fiscal 2020.

Withholding on non-resident property sales
The Governor's Budget Recommendation includes $4 million in revenue from requiring tax withholding on the sale of property in the Commonwealth by non-residents. This action can be implemented administratively through regulation by DOR. DOR has not published draft regulation language at this time. While the $4 million revenue estimate is assumed to be available for the budget, it is also assumed to be paid as capital gains tax revenue to the Commonwealth subject to the transfer to the Stabilization Fund if total capital gains revenue exceeds the statutory threshold in fiscal 2020. The Governor's budget assumes all $4 million will be transferred to the Stabilization Fund.

Tax-Related Settlements & and Judgments Exceeding $10 Million Each
The Commonwealth occasionally engages in negotiation and litigation to resolve disputed tax obligations. Prior to fiscal 2009, tax-related settlements and judgments were simply recorded as tax revenue in the relevant category, usually corporate tax, without further distinction. As a result, such tax revenues were implicitly included in tax revenue forecasts.

DOR began tracking settlements and judgments exceeding $10 million each by quarter of the fiscal year in 2009, and in fiscal 2012 began tracking such revenues by month.

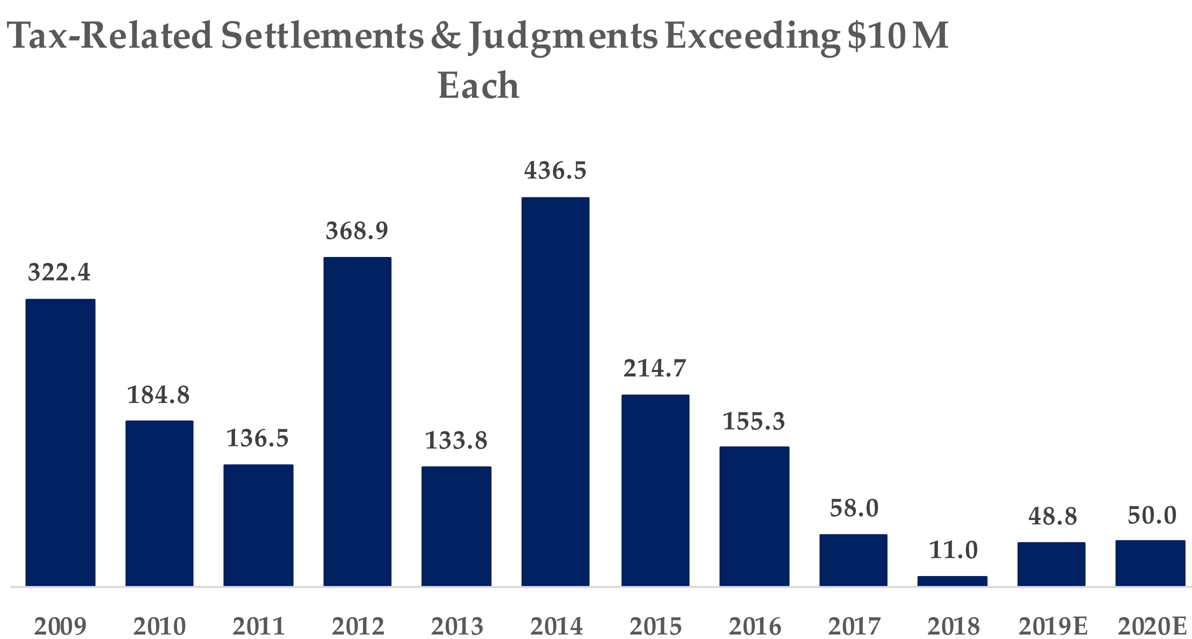

Figure 7: Tax-Related Settlements & Judgments Exceeding $10 Million Each; Figures in $ millions.

In 2011, the Legislature amended state finance law to credit these payments to the Commonwealth Stabilization Fund.[16] This change triggered Stabilization Fund deposits of $375 million in fiscal 2012, $95 million in fiscal 2013, and $414 million in fiscal 2014, though the fiscal 2014 transfer was later withdrawn, resulting in no net deposit in 2014. In total, this law steered a net deposit of $470 million to the Stabilization Fund between fiscal 2012 and fiscal 2014.

In 2014, this law was amended to subject these transfers to a threshold equal to the average settlement and judgments revenue for the previous five years.[17] Since this change was implemented, no settlement and judgment revenue has been deposited to the Stabilization Fund.

By their nature, tax-related settlements and judgments are a very volatile revenue source, but in contrast to other volatile sources, the Commonwealth continues to include this source as budgeted revenue. For example, capital gains tax revenue is a well-known volatile revenue stream. Statute obligates a portion of capital gains tax revenue to the Stabilization Fund to counteract a portion of this volatility. Tax-related settlements and judgments are three times more volatile than capital gains tax revenue.

Given the inherent volatility, MTF has long advocated crediting this revenue to the Stabilization Fund, rather than including it as budgeted revenue. The Governor's Budget Recommendation includes tax-related settlement and judgments revenue of $50 million.

[16] M.G.L. Section 29, Section 2H was amended by the Acts of 2011, Chapter 68, Section 37. Note that all settlements and judgments exceeding $10 million each (tax-related and non-tax-related) are credited to the Stabilization Fund. Typically, non-tax settlements and judgments are received by the Commonwealth's Attorney General.

[17] M.G.L. Section 29, Section 2H was further amended by the Acts of 2014, Chapter 165, Section 47.