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MTF Brief

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Update on the FY 2022 Fiscal Picture

Fiscal year 2023 began several months ago, but the loose ends of an eventful FY 2022 provides a more intriguing budget plotline. Unprecedented tax collections, outstanding spending bills, and close to $3 billion in taxpayer refunds combine for a fascinating and confusing fiscal picture with major implications for tax and spending decisions in the months ahead.

This Brief provides an update on the state's FY 2022 fiscal situation as we await final action on economic development and supplemental spending vehicles.

Initial FY 2022 Surplus

In order to understand how 62F rebates, supplemental budget spending, and the pending economic development bill all interact, it is first essential to understand the level of resources that remain unexpended. Prior to the payment of tax rebates or future spending bills, the state has approximately $5.3 billion in available resources.

Initial FY 2022 Surplus Estimate

Taxes above original benchmark	$6,654
Capital gains above benchmark	-$1,262
Dedicated to SBA/MBTA	-$224
Starting balance	$106
Supplemental spending to date	-$1,781
Additional federal revenue	$988
Reversions	$625
Non-tax revenue	$225
Initial surplus	**$5,331**

$ in millions

There are three major contributors to this unprecedented surplus:

- Surging tax collections – the state ended FY 2022 with $41.1 billion in tax collections – approximately $6.7 billion (20 percent) more than the original tax benchmark. Even after accounting for automatic transfers to the Stabilization Fund, the MBTA, School Building Authority, and other funds, $5.3 billion in surplus tax revenue remains.

- Federal COVID funds – several sources of one-time federal funds add more than $1 billion to the state's coffers. FEMA and the federal Health and Human Services agency continue to reimburse many of the state's COVID-related expenditures, such as testing, vaccination, and treatment. In addition, the state has been able to apply several hundred million in remaining CARES Act Coronavirus Relief Funds to offset public safety spending in FY 2022. The MTF estimate does not include reimbursements related to additional COVID spending proposed in Governor Baker's closeout supplemental budget.
- Reversions and non-tax revenue – each year, several hundred million dollars in appropriations go unspent and "revert" to the General Fund. Since the pandemic began, reversions have increased and will amount to more than $600 million in FY 2022. In addition to the availability of temporary federal resources, another cause for reversions is the inability to expend resources at a pace commensurate with appropriation levels for new and expanded programs. In addition, several major nontax revenue sources add more than $200 million to available resources.

These sources of surplus revenue are offset by $1.8 billion in supplemental spending to date, resulting in the initial surplus of $5.3 billion.

62F Payments

This unprecedented growth in tax revenues triggered a mandatory giveback of $2.94 billion to income taxpayers under chapter 62F of the General Laws. The law measures actual tax collections against growth in state wage and salary data, and requires tax revenues above the allowable level be returned to Massachusetts taxpayers based on their tax liability for the previous year. DOR and the State Auditor agree that in FY 2022, tax collections were $2.94 billion above the allowable level.

Technically, the 62F payments will occur in FY 2023, but effectively the funds will come from the FY 2022 surplus. Governor Baker's proposed closeout supplemental budget accomplishes this by setting aside $2.94 billion of the surplus to cover the cost of the payments. Should that proposal not be adopted, a large portion of the FY 2022 surplus will go to the Stabilization Fund and 62F payments would come out of ongoing FY 2023 tax revenues. After accounting for 62F payments, the remaining surplus is $2.4 billion.

FY 2022 Surplus after 62F Payments

Initial surplus	$5,331
62F Rebates	$2,941
Surplus after 62F	**$2,390**
$ in millions	

FY 2022 Closeout Supplemental Budget

Typically, the final spending bill in any fiscal year is a closeout supplemental budget that resolves all outstanding deficiencies. Enactment of a deficiency budget allows the comptroller to close the books on the fiscal year. Traditionally this bill occurs in early fall so that the comptroller can finalize mandated financial reports, though it has been delayed as late as December in recent years.

At the end of August, Governor Baker filed a $1.6 billion spending bill that covers outstanding deficiencies and obligations, but also proposes new spending to cover COVID recovery needs, improve MBTA safety, and a number of ongoing Administration spending initiatives.

Governor Baker's Closeout Spending Proposal

Category	Gross Cost	Net Cost
MassHealth	$492.0	$0.0
COVID costs	$400.0	$108.0
Administration initiative	$305.2	$305.2
MBTA	$200.0	$200.0
MassDOT	$66.7	$66.7
Deficiency	$77.7	$77.7
Other	$50.1	$50.1
CBAs	$30.4	$30.4
Total	**$1,622.2**	**$838.2**

$ in millions

The legislature will now determine the final composition of the final closeout supplemental budget and, in the process, the amount of FY 2022 resources available for the pending economic development bill.

Putting it All Together

Certification of the 62F amount and better information on federal revenues and reversions provides a clearer picture of the resources available to lawmakers as they closeout FY 2022 and act on economic development legislation.

Current FY 2022 Resource Estimate

Taxes above original benchmark	$6,654
Capital gains above benchmark	-$1,262
Dedicated to SBA/MBTA	-$224
Starting balance	$106
Supplemental spending to date	-$1,781
Additional federal revenue	$988
Reversions & non-tax revenue	$625
Non-tax revenue	$225
Initial surplus	**$5,331**
62F Rebates	$2,941
Surplus after 62F	**$2,390**
Gov's closeout	-$1,622
Offsets	$782
Surplus Remaining	**$1,550**
Remaining FRF	$2,266
Total resouces	$3,816

$ in millions

If the Legislature were to pass the Governor's proposal in full, it would leave $1.5 billion in surplus funds for economic development initiatives. However, the legislature is likely to pare down Administration spending initiatives, thereby increasing the resources available for economic development spending. In addition, more than $2.2 billion in federal Fiscal Recovery Funds remain available for investing in economic development and other initiatives.

The House and Senate economic development bills, passed by the respective branches and now pending in a conference committee, included approximately $4 billion in combined spending as well as approximately $500 million in ongoing tax changes that do not affect the FY 2022 surplus. After accounting for 62F payments, the House and Senate can easily accommodate more than $3 billion in economic development spending if they adopt the Governor's plan and $4 billion if they do not move forward with several major spending initiatives included in Governor Baker's closeout.

The FY 2022 Surplus in Context

In FY 2021, prior to action on final spending and ARPA legislation, MTF estimated the budget surplus at $2.1 billion and noted at the time that it was the largest surplus in many years. The FY 2022 surplus, after accounting for $2.94 billion in 62F payments, is even larger. In fact, the FY 2022 and FY 2021 surpluses are double the size of the next largest surplus in recent history – the $1 billion surplus in FY 2019.

These tremendous surpluses have been generated at a time when the state has also made historic deposits into the Rainy Day Fund and historic new investments in housing and primary and secondary education.

Comparison of FY 2019 and FY 2022 Surpluses

	FY 2019	FY 2022
Automatatic Stabilization Deposit	$824.4	$2,316.0
K-12 formula increase	$160.6	$219.6
Increase to RAFT and rental vouchers	$14.3	$88.0
Pre-Closeout surplus	***$1,023.0***	***$2,390.4***

$ in millions

Remaining Spending and Policy Decisions

Recent fiscal developments indicate that the legislature has sufficient resources to support an economic development bill that approaches the $4 billion proposed in the earlier House and Senate versions of the bill. This would include a $300 million deposit to the unemployment insurance trust fund, major investments to spur the creation and investment in attainable housing, and new spending to improve environmental infrastructure and foster energy innovation.

Lawmakers must also finally resolve two outstanding tax proposals. The first pertains to a $500 million one-time tax rebate program for middle-income residents. The proposed program would provide rebates of $250 to $500 to tax filers earning between $38,000 and $100,000 for individuals (with a cap of $150,000 for joint filers). Each of these filers will now receive a 62F tax rebate payment equal to 13 percent of their FY 2021 tax liability. A tax filer needs to have a 2021taxable income (post-credits) of more than $38,461 to receive a 62F rebate of more than $250.

In addition, a package of permanent tax relief proposals also remain in limbo and require resolution. The House and Senate both voted unanimously to advance sizable tax relief for families with dependents, senior citizens, and low-income wage earners. Critical reforms to the estate tax were also proposed, though the two branches differed slightly in details on timing and the mechanics of the estate tax changes. These tax relief proposals have no fiscal impact until at least FY 2023 nor do they impact the FY 2022 surplus.

MTF's spending and policy priorities for the end of FY 2022 legislation, outlined in an earlier Bulletin, remain unchanged. Massachusetts has a unique opportunity to use unprecedented resources to make meaningful investments in areas like housing, energy, and infrastructure that are critical to the state's long-term economic health while also making tax law changes that will benefit high-need families, reduce housing and dependent care costs, and improve the state's competitiveness. Lawmakers must seize this opportunity to do both before this legislative session ends.