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MTF Bulletin

December 11, 2024

FY 2025 Fiscal Update & FY 2026 Consensus Revenue Hearing

On December 2nd, the Massachusetts Taxpayers Foundation (MTF), along with the Department of Revenue (DOR) and other economic experts participated in the annual Consensus Revenue Hearing. The hearing offers administration and legislative budget leaders an opportunity to assess current revenue assumptions for Fiscal Year (FY) 2025 and evaluate the resources that will be available to support budgeted spending in FY 2026. This brief uses the Consensus Revenue Hearing as the backdrop to examine potential revenue collections in both years.

To put the testimony provided at the Consensus Revenue Hearing into context, this brief begins with an examination of the FY 2025 tax revenue benchmark and collection trends to date. It then provides an overview of the testimony offered at the hearing for FY 2025 and FY 2026; highlighting key themes, commonalities, and differences. The brief concludes with an assessment of the challenges and opportunities facing administration and legislative budget writers heading into the second half of FY 2025 and the FY 2026 budget development process.

Understanding FY 2025 Revenue Collections

Building Up the FY 2025 Revenue Benchmark

In January 2024, budget leaders from the Healey administration, House, and Senate announced a consensus tax revenue figure of $40.202 billion for the FY 2025 budget (excluding surtax revenues). After adding the surtax spending cap of $1.3 billion to that benchmark, total tax revenues available to support budgeted spending were estimated to be $41.502 billion.

Later, the FY 2025 General Appropriations Act (GAA) and the 2024 Housing Bond Bill (known as the Affordable Homes Act) included several revenue-generating initiatives and tax credit programs that are anticipated to impact tax revenue collections this fiscal year. The FY 2025 GAA adopted a range of tax fairness and modernization initiatives, as well as a tax amnesty program that are estimated to collectively provide $160 million in new revenue. The Affordable Homes Act included adjustments to a number of tax credit programs, which carry a cost to the state of approximately $55 million.

The combined impact of these changes increases estimated tax revenue collections in FY 2025 to $41.607 billion. The monthly and year-to-date revenue benchmarks established by DOR are based on this annual total.

FY 2025 Revenue Benchmark Build-Up

	FY 2025 Benchmarks
Non-Surtax Revenue Benchmark	**$40,202**
Surtax Spending Cap	$1,300
Total Revenue Benchmark	**$41,502**
AHA Tax Credit Adjustments	-$55
Tax Fairness & Modernization	$60
Tax Amnesty Program	$100
FY 2025 Expected Tax Collections	**$41,607**

$ in millions

FY 2025 Revenue Collections to Date

Through November, state tax revenue collections for FY 2025 total $14.898 billion, $124 million (0.8 percent) below the year-to-date benchmark and $805 million (5.7 percent) ahead of FY 2024 collections. Throughout FY 2025, the revenue benchmarks set by DOR assume the majority of the revenue growth to take place during the first six months of the fiscal year (6.9 percent growth). During the second half of the fiscal year, the benchmarks assume that revenues will decline compared to the prior year by 1.9 percent.

FY 2025 Revenue Collections v. FY 2024 Actuals & FY 2025 Benchmarks

	FY 2024 YTD	FY 2025 YTD	FY 2024 v. FY 2025	FY 2025 YTD BM	FY 2025 YTD v. BM	% Growth to Date v. BM
Withholding	$6,768	$7,309	$541	$7,253	$56	0.8%
Non-Withholding	**$1,090**	**$1,413**	**$323**	**$1,272**	**$141**	**10.5%**
Sales	$3,907	$3,976	$69	$3,917	-$121	-3.2%
Corporate/Business	$1,226	$1,108	-$118	$1,337	-$229	-17.1%
Other	$1,103	$1,093	-$10	$1,065	$28	2.6%
Total	**$14,094**	**$14,898**	**$805**	**$14,844**	**-$124**	**-0.8%**

$ in millions

In November, monthly revenue collections continued to outpace the prior year, coming in $190 million (8.4 percent) ahead of FY 2024 and exceeding the monthly benchmark by $56 million (2.4 percent). Increases over FY 2024 were predominantly driven by strong collections in withheld and non-withheld income taxes – likely related to the income surtax, as well as the tax amnesty program – as well as the other tax category, due to a bump in estate tax collections.

Compared to the year-to-date benchmarks, sales and corporate tax collections are falling behind by the largest margins, 3 percent and 17.1 percent, respectively.

While revenue growth over the prior year is positive, analyzing what these trends mean for future months and the next fiscal year is difficult due to a lack of information on how much surtax revenue is included in monthly and year-to-date collections. Without that additional data, assessing how revenue collection trends impact the resources available to support budgeted spending becomes challenging, as demonstrated in the following section.

FY 2025 Revenue Collections in Context

Last January, the FY 2025 non-surtax revenue benchmark of $40.202 billion represented 2 percent ($792 million) growth over the revised FY 2024 benchmark of $39.410 billion and 3.5 percent growth ($1.369 billion) over estimated FY 2024 collections of $38.833 billion, which accounted for the fiscal impacts of the 2023 tax relief bill.[1]

Actual revenue collections in FY 2024 totaled $40.800 billion, $1.6 billion (4.2 percent) above FY 2023 and $967 million (2.4 percent) above benchmark. However, this figure also includes DOR's certification of $2.460 billion in surtax revenue.[2] After accounting for those revenues, non-surtax collections in FY 2024 totaled $38.340 billion, $582 million below FY 2023 and $493 million below expectations.

[1] The revised FY 2024 revenue benchmark of $39.410 billion did not account for the costs of tax relief package signed into law by Governor Healey in September 2023. After accounting for those costs, estimated at $577 million, expected FY 2024 revenue collections were $38.833 billion.

[2] On December 6th, DOR announced their final certification of FY 2024 surtax revenue collections, totaling $2.460 billion.

FY 2024 Collections v. FY 2023 and Benchmark

	All Revenues	Non-Surtax Revenues
FY 2023 Revenue Collections	$39,164	$38,922
FY 2024 Revenue Benchmark	$39,835	$38,833
FY 2024 Revenue Collections	$40,800	$38,340
FY 2024 v. FY 2023	**$1,636**	**-$582**
FY 2024 v. Benchmark	**$967**	**-$493**

$ in millions

For FY 2025, the FY 2024 non-surtax revenue shortfall means that a higher rate of growth is required to meet the benchmark set last January and to support the level of spending included in the operating budget. Instead of 3.5 percent revenue growth, FY 2025 non-surtax revenues need to grow by 4.9 percent to meet the original $40.202 billion benchmark.

FY 2025 Estimated & Required Rates of Non-Surtax Revenue Growth

FY 2024 Revenue Benchmark	FY 2025 Revenue Benchmark	FY25 v. FY24 Estimated Growth
$38,833	$40,202	3.5%
FY 2024 Revenue Actuals	**FY 2025 Revenue Benchmark**	**FY25 v. FY24 Required Growth**
$38,340	$40,202	4.9%

$ in millions

Through November, revenues in FY 2025 have grown by 5.7 percent over FY 2024.

While this higher growth rate is positive, comparing year-to-date growth with the 4.9 percent rate required to meet the non-surtax revenue benchmark for FY 2025 is challenging, due to the data limitations mentioned above. The monthly revenue reports from DOR do not separate surtax revenue from all other income tax collections, and so it is not possible to provide a direct comparison of non-surtax revenue growth. Ultimately, enabling comparisons of non-surtax collections against both the prior year and the current year benchmark is vital for providing the most relevant information to budget writers, because it most closely tracks the resources available to support budgeted spending.

But even with these data limitations, year over year growth figures in FY 2025 provide greater insight than in FY 2024, when monthly collections with the surtax were being compared against months prior to the new tax going into effect.[3] However, we do not know if patterns in surtax payments will be the same in FY 2025 as in FY 2024, and so it is not possible to say with certainty that year to date growth paints a positive picture for both surtax and non-surtax collections.

At the Consensus Revenue Hearing, economic experts differed in their expectations for FY 2025 revenues; however, the majority of testifiers expect that non-surtax revenues in FY 2025 will fall short of benchmark by an average of 0.7 percent ($265 million). This contrasts sharply with surtax revenue collections in FY 2025, which are projected

[3] The four percent surtax on income over $1 million went into effect on January 1, 2023. The surtax did not impact tax revenue collections during the first six months of FY 2023 (July – December 2022).

to reach $2.4 billion; approximately $1.1 billion greater than the surtax spending cap currently reflected in the FY 2025 tax revenue benchmark of $1.3 billion.

FY 2025 Consensus Revenue Projections (no surtax)

Excluding surtax revenue, testifiers at the Consensus Revenue Hearing projected that collections in FY 2025 will exceed FY 2024 collections by an average of $1.7 billion (4.4 percent), but fall below benchmark by an average of $264 million (0.7 percent).

MTF's modeling suggests that non-surtax revenues in FY 2025 will come in above FY 2024 actuals by $1.3 billion (3.5 percent), but miss the benchmark by $637 million (1.6 percent).

Summary of Consensus Revenue Testimony for FY 2025 (n/s = non surtax)

	FY 2024 Collections (n/s)	FY 2025 Benchmark (n/s)	FY 2025 Projection (n/s)	$ v. FY 2024 Collections (n/s)	$ v. FY 2025 Benchmark (n/s)	% v. FY 2025 Benchmark (n/s)	FY 2025 Capital Gains
DOR Upper	$38,340	$40,307	$40,063	$1,723	-$244	-0.6%	$2,419
DOR Lower			$39,447	$1,107	-$860	-2.1%	$2,288
MTF			$39,670	$1,330	-$637	-1.6%	$2,153
cSPA			$40,000	$1,660	-$307	-0.8%	--
ACM			$41,035	$2,695	$728	1.8%	$3,381
Median			***$40,000***	***$1,660***	***-$307***	***-0.8%***	***$2,354***
Average			***$40,043***	***$1,703***	***-$264***	***-0.7%***	***$2,560***

$ in millions

The Department of Revenue (DOR) and MTF were aligned in their expectations that moderate growth in non-surtax withholding income tax collections would bolster revenues in FY 2025. According to MTF's model, withheld income taxes are anticipated to grow by 3.6 percent over FY 2024. At that rate, growth still remains below the ten-year average of five percent, but it is stronger than anticipated growth rates in any other tax category.

A notable outlier among testifiers was Professor Alan Clayton-Matthews' projection that non-surtax revenues in FY 2025 would total $41.035 billion, $2.7 billion ahead of FY 2024 and $728 million (1.8 percent) above benchmark. This high-level of growth appears to be driven by strong capital gains collections, which he anticipates to total $3.4 billion; substantially higher than the average projection amongst the other testifiers of $2.3 billion.

FY 2025 Surtax Revenue Projections

In FY 2025, economic experts were in agreement that surtax revenues would likely reach $2.4 billion, essentially level with DOR's final certification of FY 2024 surtax collections and substantially greater than the $1.3 billion surtax spending cap currently reflected in the FY 2025 revenue benchmark. However, the majority of the projections presented below were based off DOR's preliminary certification of surtax revenues in FY 2024 of $2.199 billion. Had DOR's final figures been available prior to the hearing, it is likely that FY 2025 projections would increase slightly.

Summary of Surtax Revenue Projections in FY 2025 (w/s = with surtax)

	FY 2024 Surtax Actuals	FY 2025 Surtax Cap	FY 2025 Surtax Estimate	Surtax Est. v. FY 2024 Actuals	Surtax Est. v. Spending Cap
DOR Upper	$2,460	$1,300	$2,491	$31	$1,191
DOR Lower			$2,349	-$111	$1,049
MTF			$2,451	-$9	$1,151
cSPA			$2,400	-$60	$1,100
ACM			$2,374	-$86	$1,074
Median			***$2,400***	***-$60***	***$1,100***
Average			***$2,413***	***-$47***	***$1,113***

$ in millions

Summing Up FY 2025

Heading into the second half of FY 2025, the testimony provided at the Consensus Revenue Hearing conveyed several major takeaways for state budget writers:

- First, while non-surtax revenue collections in FY 2025 are projected to fall slightly short of benchmark, all testifiers expect strong growth over FY 2024. Because of this, and the unpredictability of revenue collections during the final six months of the fiscal year, experts did not recommend any adjustments to the FY 2025 revenue benchmarks.
- Second, surtax revenue collections will start from a higher than expected FY 2024 base and greatly exceed the $1.3 billion surtax spending cap currently reflected in the FY 2025 tax revenue benchmarks. This disconnect between actual surtax revenue collections and the surtax spending cap, combined with the lack of data on monthly surtax revenue collections, continues to create challenges. As detailed in our Consensus Revenue Hearing testimony, MTF offered several specific recommendations for policymakers to consider to improve the process to track, collect, and spend surtax revenues.
- Lastly, testifiers highlighted that in FY 2025 and FY 2026, the greatest uncertainties facing the Massachusetts economy will come from the federal government and the potential policy proposals of the Trump administration.

Projecting FY 2026 Revenue Collections

The Consensus Revenue Hearing is the first opportunity to assess the resources that will be available to support the FY 2026 budget. While the final consensus revenue agreement may not be announced for several weeks, looking at economic forecasts for both non-surtax and surtax revenues provides important context for the budget challenges that the administration and legislature are likely to face in the upcoming fiscal year.

FY 2026 Consensus Revenue Projections (no surtax)

Despite expectations that non-surtax revenues in FY 2025 will come in below benchmark, testifiers at the hearing generally expressed optimism that revenues would grow moderately in FY 2026. Excluding surtax revenue, the average growth rate predicted for FY 2026 is 3.97 percent over projected FY 2025 revenues.

Summary of FY 2026 Consensus Revenue Testimony (n/s = no surtax)

	FY 2025 Benchmark	FY 2025 Projection (n/s)	FY 2026 Projection (n/s)	v. FY 2025 Proj. (n/s) $	v. FY 2025 Proj. (n/s) %	FY 2026 Capital Gains
DOR Upper		$40,063	$41,286	$1,223	3.05%	$2,335
DOR Lower		$39,447	$40,206	$759	1.92%	$2,129
MTF	$40,307	$39,670	$40,905	$1,235	3.11%	$2,265
cSPA		$40,000	$42,100	$2,100	5.25%	--
ACM		$41,035	$43,708	$2,673	6.51%	$3,593
Median		***$40,000***	***$41,286***	***$1,235***	***3.11%***	***$2,300***
Average		***$40,043***	***$41,641***	***$1,598***	***3.97%***	***$2,581***

$ in millions

MTF's modelling suggests that non-surtax revenues in FY 2026 will grow by 3.1 percent, reaching $40.9 billion. As in FY 2025, relative strength in withholding income tax collections will support stable year over year revenue growth. Sales and corporate tax revenue collections are both expected to be positive in FY 2026, at 1.2 and 3.7 percent growth, respectively; while other taxes are anticipated to plateau and remain below FY 2023 collections of $2.9 billion.

The average projection for capital gains revenues in FY 2026 is $2.6 billion; approximately $900 million above the projected capital gains threshold of $1.66 billion. Capital gains are an extremely volatile source of state tax revenue, and to limit the reliance of the state budget on this revenue source, all capital gains collections above a statutorily set threshold are automatically deposited into the state's Stabilization Fund.

FY 2026 Surtax Revenue Projections

In FY 2026, the average surtax revenue projection is $2.41 billion, with the majority of testifiers expecting surtax collections to remain essentially level with FY 2025. As mentioned above, the projections included in the table below were mostly based on DOR's preliminary certification of surtax collections in FY 2024, equal to $2.199 billion.

If the final certification of $2.460 billion had been available prior to the hearing, it is likely that these figures would increase slightly. However, with only one full year of surtax revenue data available, it remains extremely challenging to accurately predict future revenue trends.

Summary of FY 2026 Consensus Revenue Testimony (w/s = with surtax)

	FY 2024 Surtax Actuals	FY 2025 Surtax Estimate	FY 2026 Surtax Estimate	FY 2026 v. FY 2025
DOR Upper		$2,491	$2,561	$70
DOR Lower		$2,349	$2,186	-$163
MTF	$2,460	$2,451	$2,619	$168
cSPA		$2,400	$2,400	$0
ACM		$2,374	$2,227	-$147
Median		***$2,400***	***$2,400***	***$0***
Average		***$2,413***	***$2,399***	***-$14***

$ in millions

Summing Up FY 2026

As policymakers assess the testimony provided at the Consensus Revenue Hearing and consider crafting the FY 2026 Consensus Revenue Agreement, they should remain mindful that even positive non-surtax revenue growth may provide limited new resources to support budgeted spending. The projections offered last week support at least a 3 percent growth assumption for non-surtax revenues, consistent with the median projection and in line with long-term historic trends for revenue growth.

Additionally, surtax revenue projections of at least $2.4 billion in FY 2026 suggest that a surtax spending cap in the range of $1.75 billion would allow for a sustainable amount of surtax spending to be incorporated into the operating budget. A surtax spending cap of $1.75 billion would still allow for more than $600 million in above cap collections to be distributed between the Education and Transportation Innovation & Capital Fund (85 percent, $553 million) and the Education and Transportation Reserve Fund (15 percent, $98 million).

Looking Ahead to FY 2025 & FY 2026

FY 2025 Revenue & Spending Trends

At the Consensus Revenue Hearing economic experts were in agreement that non-surtax revenue collections in FY 2025 would likely fall short of benchmark, despite exceeding collections in FY 2024 by over $1.6 billion. To meet the non-surtax revenue benchmark used to build the FY 2025 budget, revenues need to grow by 4.0 percent over FY 2024 collections. To date, total revenues have grown by 5.7 percent over the prior year. While this level of growth is a positive sign, the continued inability of DOR to regularly estimate monthly surtax revenue collections makes it challenging to track non-surtax revenue performance compared to benchmark and assess the resources available to support general budgeted spending.

Yet despite projections that revenues would not meet expectations, testifiers at the hearing did not recommend an adjustment to the FY 2025 benchmark at this time. Given the uncertainties that remain for the final half of the fiscal year, it also appears unlikely that the Healey administration will pursue mid-year spending cuts to the FY 2025 budget.

In the FY 2025 General Appropriations Act (GAA), budget writers exercised restraint to limit year-over-year spending growth to 3.1 percent, consistent with expected revenue growth at the time and a drastic departure from the two prior fiscal years in which spending grew by 6.9 percent (FY 2024) and 9.1 percent (FY 2023). That level of discipline will need to be maintained for the remainder of the year to manage a balanced budget throughout FY 2025, and also serves as an example of what will be required in FY 2026.

FY 2026 Budget Development Process

At the same time that policymakers will be monitoring FY 2025 revenue collections, they will also be undertaking the FY 2026 budget development process. Fortunately, as demonstrated by the testimony at the Consensus Revenue Hearing, revenues are anticipate to grow moderately compared to FY 2025. The average projection for revenue growth in FY 2026 was 3.97 percent, or an increase of $1.6 billion.

However, despite these positive projections, budget writers must continue to constrain year-over-year spending growth. Increasing obligations, like the state's transfer to the Pension Fund, continued implementation of the Student Opportunity Act, and significant early education investments will quickly account for any new resources and leave limited revenues available for new initiatives. As MTF highlighted at the hearing, limiting spending growth to three percent in FY 2026 is necessary; not only to ensure alignment between spending and revenue growth expectations, but also to safeguard the long-term sustainability of the state budget.

Additionally, keeping spending growth in the three percent range allows the state to prepare for and protect against potential policy actions at the federal level. As discussed in MTF's testimony, policy proposals from the Trump administration would have profound economic impacts for Massachusetts. The extension and potential expansion of the Tax Cuts and Jobs Act (TCJA) could boost state tax revenue collections in the short-term, but may also come at the expense of major cuts to domestic programs. These cuts would have immediate impacts on state operating budgets and planned capital spending, and policymakers in Massachusetts should be prepared to respond to these changes with limited notice.

Administration and legislative budget leaders must publish a consensus tax revenue agreement by January 15th. The FY 2025 Consensus Revenue Agreement was announced on January 8th. This decision is one of the most important steps in the state budget development process, as it will inform the revenue foundation for the budget proposals put forward by the Governor, House, and Senate.