

News Release

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MTF Forecast: Modest Growth in Tax Revenues in 2016

Tax revenues will increase by \$1.1 billion, or 4.5 percent, to \$25.5 billion in fiscal 2016, extending the trend of modest tax collections that has averaged just over 4 percent annual growth for the past five years, according to a new forecast released today by the Massachusetts Taxpayers Foundation (Figure 1 on page 3).

For fiscal 2015, the Foundation projects tax revenues of \$24.4 billion, slightly higher than the original benchmark of \$23.39 billion and \$95 million above the revised consensus forecast of \$24.31 billion.¹ This would be an increase of \$1 billion, or 4.4 percent, over the \$23.37 billion in taxes collected in fiscal 2014.

Three variables – an income tax rate reduction, one-time corporate tax settlements in excess of \$10 million, and capital gains tax revenues – affect the Foundation’s FY 2015 and FY 2016 revenue projections and add to the current budget challenges:

- Automatic income tax cut – the Foundation’s forecast assumes that all conditions will be met to trigger an income tax rate reduction from 5.15 percent to 5.10 percent on January 1, 2016 due to continued economic growth and low inflation. Therefore our FY 2016 estimate is \$72 million less than it would be if the rate remains unchanged. The Foundation recommends including the income tax rate reduction in the FY 2016 consensus revenue forecast.
- One-time corporate tax settlements in excess of \$10 million – the Foundation does not include any estimates of one-time corporate tax settlements in excess of \$10 million in its FY 2015 and FY 2016 forecasts other than the \$24 million in settlements reached as of December 2014. Since the 2015 budget anticipates \$240 million in these payments, over \$200 million more than the amount collected half-way through the fiscal year, there is the potential for additional budget exposures.

¹ The FY 2015 revenue benchmark was revised down to \$24.31 billion from \$24.39 billion, a reduction of \$75 million due to the cut in the income tax rate from 5.20 percent to 5.15 percent on January 1, 2015 (\$70 million) and repeal of the gas tax index (\$5 million).

- Capital gains tax revenues – although the Foundation’s FY 2015 revenue forecast is consistent with the consensus benchmark, our \$1.4 billion estimate of capital gains tax revenues requires a deposit of \$330 million into the stabilization fund – instead of the \$122 million anticipated in the consensus revenue forecast – and poses another substantial problem for the 2015 budget. The Foundation projects capital gains tax revenues to increase from \$1.07 billion in fiscal 2014 to \$1.40 billion in 2015 and fall back to \$1.29 billion in 2016 (Table 1).

In 2011, the state established a \$1 billion cap on the amount of capital gains tax revenues that could be used to support the budget and in 2012 it adjusted that threshold by the average annual rate of growth of the U.S. gross domestic product over the previous five-year period. The cap for fiscal 2015 is \$1.05 billion and an estimated \$1.09 billion for fiscal 2016. Capital gains tax revenues in excess of the established cap for a fiscal year must be deposited into the state’s stabilization fund.²

In fiscal 2015, capital gains tax revenues of \$1.4 billion would require the state to deposit a total of \$350 million into the stabilization fund. This means that an additional \$230 million in tax revenues (on top of the \$122 million already excluded from the 2015 budget) cannot be used to support operating expenditures creating yet another fiscal exposure.

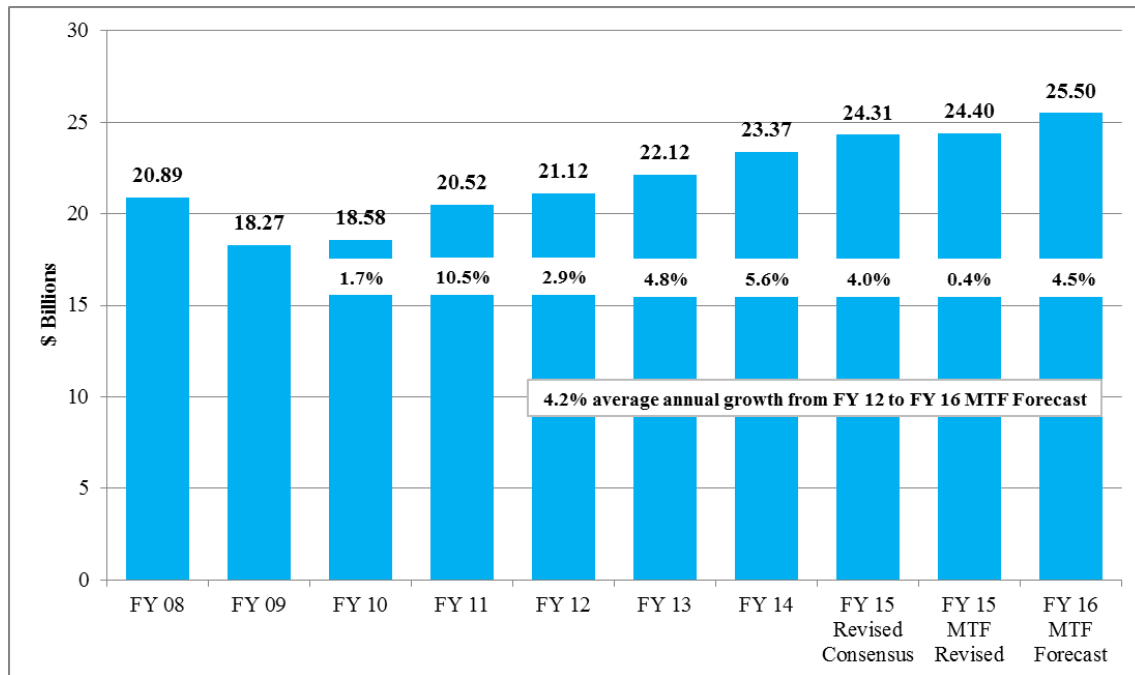
The Foundation’s projection of \$1.29 billion in capital gains tax revenues in fiscal 2016 would result in \$200 million above the established caps, requiring that it be deposited into the stabilization fund.

Andrew C. Bagley, MTF’s Director of Research and Public Affairs, presented the Foundation’s economic and revenue forecast to members of the House and Senate Ways and Means Committees and the Secretary of Administration and Finance at their annual consensus revenue hearing at the State House today.

“It’s alarming that even with employment gains and a healthier economic climate, the state faces a monumental budget shortfall in fiscal 2015 and substantial challenges in 2016,” Bagley said. “Increases in non-discretionary spending for Medicaid, pensions, and retiree health care combined with additional funding for the MBTA and School Building Authority will consume most, if not all of the \$1.1 billion in new tax revenues. As a result, there will be virtually no additional revenues for the remainder of the 2016 budget.”

² Ninety percent of the transferred funds remain in the stabilization fund and 10 percent are divided equally and transferred to the State Retiree Benefits Trust Fund and the Commonwealth’s Pension Liability Fund.

Figure 1 – State Tax Revenues, 2008 – 2016



Personal Income Taxes

A slight improvement in personal income tax revenues derives from continued growth in employment and gains in wages that will generate a \$621 million, or 4.4 percent, increase in personal income taxes in fiscal 2016, according to the Foundation’s forecast. This increase will be offset by a decline of \$110 million in capital gains tax revenues in FY 2016 from FY 2015. As a result, overall growth in FY 2016 will be less than FY 2015 when personal income taxes are projected to increase by \$811 million, or 6.1 percent (Table 1 on the following page).

The Foundation forecasts that the state will add 58,000 jobs in fiscal 2016, a 1.6 percent increase and roughly comparable to the gains in fiscal 2015. The fiscal 2016 job estimate reflects the slow but steady growth of the state’s economy that will see the unemployment rate fall from its current 5.8 percent to 5.4 percent, the lowest point since July 2008.

Personal incomes are expected to increase by 5.7 percent in 2016, up from 4.4 percent in 2015. This growth is driven by a 6.5 percent jump in average wages and salaries in 2016, compared to 4.3 percent in 2015.

The state’s growth in employment and personal income tracks the national economic recovery. Private sector job creation in the U.S. increased by 2.7 million or 2.4 percent in 2014 and is projected to grow by 3.2 million or 2.7 percent in 2015, according to Moody’s Analytics’ January 2015 forecast.

Table 1 – State Tax Revenues by Category

(\$ millions)

	FY 14 Actual	MTF FY 15 Forecast	\$ Change 15 vs 14	% Change 15 vs 14	MTF FY 16 Forecast	\$ Change 16 vs 15	% Change 16 vs 15
Income Tax	13,202	14,013	811	6.1%	14,634	621	4.4%
Capital Gains	1,069	1,398	329	30.8%	1,288	-110	-7.9%
Sales	5,496	5,785	289	5.3%	6,016	231	4.0%
Corporate and Business	2,510	2,383	-127	-5.1%	2,506	123	5.2%
All Other	2,162	2,223	61	2.8%	2,346	123	5.5%
Total	23,370	24,404	1,034	4.4%	25,502	1,098	4.5%

Sales Taxes

The Foundation projects that sales taxes will grow by 4.0 percent to \$6.02 billion in fiscal 2016, slightly less than the 5.3 percent increase in fiscal 2015 which was driven in part by a 10 percent increase in sales tax revenues for motor vehicles over FY 2014. Sales tax revenues since November 2013 have been buttressed by an agreement with Amazon to collect taxes on online purchases adding approximately \$30 million in FY 2014 and \$50 million in FY 2015 or roughly 1 percent of total sales tax revenues.

Corporate and Business Taxes

Fiscal 2016 corporate and business taxes are projected to increase by \$123 million to \$2.51 billion, a 5.2 percent increase over 2015 driven by strong corporate profits. On the other hand, fiscal 2015 corporate and business tax revenues are expected to decline by \$127 million or 5.1 percent from fiscal 2014 because of \$436 million in one-time corporate tax settlements in excess of \$10 million in FY 2014 compared to just \$24 million in the Foundation's FY 2015 forecast. If not for the inclusion of the \$436 million in one-time corporate settlements in FY 2014, corporate and business taxes would show a 10 percent annual growth from FY 2014 to FY 2016.

Global Risks

While the U.S. economy has shown solid growth recently, a range of global risks have reemerged as potential threats to the recovery. Europe is on the brink of a deflationary trap, a downward price spiral that could decimate its economy for years; Japan, the world's third largest economy, struggles to escape from recession; and China's growth continues to slow as it grapples with enormous public and private debt exposures.

Falling oil prices may be a boom for consumers but they create significant financial risks for several countries that rely on commodity exports, as well as U.S. shale oil and gas firms that face mounting debt costs as prices plummet. Geopolitical risks in Russia / Ukraine, the Middle East, and several African countries, along with heightened tensions of terrorism, could pose significant challenges to global economic growth in 2015.

MASSACHUSETTS TAXPAYERS FOUNDATION

FISCAL YEAR FORECAST SUMMARY

MOODY'S ANALYTICS NATIONAL FORECAST

January 2015	2008	2009	2010	2011	2012	2013	<<< History 2014	Forecast >>>	2015	2016
Personal Income (billions of 2000 \$)	10,026	9,747	9,795	10,154	10,357	10,554	10,955	11,448	12,169	
% change	3.4	-2.8	0.5	3.7	2.0	1.9	3.8	4.5	6.3	
Employment (millions)	137.8	134.0	129.7	130.6	132.6	134.8	137.5	140.4	143.9	
% change	0.6	-2.8	-3.2	0.6	1.6	1.6	2.0	2.1	2.5	
Unemployment Rate	5.0	7.6	9.8	9.3	8.5	7.8	6.8	5.8	5.4	
CPI (% change)	3.7	1.0	-0.9	1.8	1.9	1.4	2.1	1.2	2.2	
PPI (% change)	13.4	-12.6	7.5	10.6	-0.9	1.1	2.1	-1.3	3.9	
Federal Discount Rate	4.3	1.2	0.5	0.6	0.8	0.8	0.8	0.8	1.8	
Prime Commercial Rate	6.7	3.9	3.3	3.3	3.3	3.3	3.3	3.3	4.1	
Standard & Poor's 500 Index (% change*)	7.5	-39.1	19.7	10.6	1.8	24.8	13.7	3.6	1.0	

MTF MASS. ECONOMIC FORECAST	2008	2009	2010	2011	2012	2013	<<< History 2014	Forecast >>>	2015	2016
Personal Income (billions of current \$)	329.2	330.3	331.1	349.5	366.4	380.6	391.2	408.6	433.4	
% change	4.5	0.3	0.3	5.5	4.8	3.9	2.8	4.4	6.1	
Personal Income (billions of 2000 \$)	270.4	264.3	260.6	270.2	274.0	275.8	282.8	290.9	308.6	
% change	2.9	-2.3	-1.4	3.7	1.4	0.6	2.5	2.9	6.1	
Total Employment (000s)	3,294	3,240	3,183	3,192	3,253	3,297	3,381	3,463	3,521	
% change	1.0	-1.6	-1.7	0.3	1.9	1.3	2.5	2.4	1.7	
Unemployment Rate	4.6	6.8	8.5	7.8	6.9	6.7	6.6	5.5	5.1	

MTF MASS. TAX FORECAST	2008	2009	2010	2011	2012	2013	<<< History 2014	Forecast >>>	2015	2016
Income Tax (millions \$)	12,498	10,593	10,128	11,570	11,911	12,831	13,202	14,013	14,634	
% change	9.7	-15.2	-4.4	14.2	3.0	7.7	2.9	6.1	4.4	
Sales Tax	4,088	3,870	4,626	4,909	5,059	5,164	5,496	5,785	6,016	
% change	0.5	-5.3	19.5	6.1	3.1	2.1	6.4	5.3	4.0	
Corporations Tax	2,285	1,916	1,936	2,051	2,344	2,262	2,510	2,384	2,506	
% change	-3.4	-16.2	1.1	5.9	14.3	-3.5	11.0	-5.0	5.1	
TOTAL TAXES**	20,645	18,088	18,392	20,346	21,114	22,123	23,369	24,404	25,502	
% change	5.2	-12.4	1.7	10.6	3.8	4.8	5.6	4.4	4.5	
TOTAL TAXES FOR BUDGET***	17,724	15,225	15,657	17,493	18,158	19,105	20,187	21,104	21,877	
% change	4.3	-14.1	2.8	11.7	3.8	5.2	5.7	4.5	3.7	

* Percent change in index for prior calendar year.

** Includes collections from other tax sources not detailed above.

*** Tax revenues available for appropriation in the budget exclude a portion of sales tax receipts dedicated to the MBTA, the Massachusetts School Building Authority, tax revenues dedicated to pension funding, and employer contributions to the Workforce Training Fund.
