Massachusetts Taxpayers Foundation

333 WASHINGTON STREET
BOSTON, MA 02108-5170
617-720-1000

October 17, 2017

FY 2017 Fiscal Year Close Out

MTF

Last week the House and Senate passed separate versions of the final supplemental budget necessary to close out fiscal year 2017. This brief assesses the final FY 2017 budget gap and looks at the strategies the Administration and the Legislature is relying on to end the year in balance.

Budget Gap

The state has been confronted with three separate budget gaps in FY 2017. In October, in light of expected declines in sales tax revenues and spending needs unaccounted for in the original budget, Governor Baker's Administration identified a $294 million budget gap and identified solutions which, at the time, did not require midyear budget cuts. In December a further gap of $98 million, was solved through 9C cuts.

Figure 1. Midyear Budget Gaps Through December

October gap	-$294
Solutions	
Trust fund balance sweeps	$126
Unexpected federal revenues	$92
MBTA & SBA savings	$31
Voluntary separation program	$25
Legal settlement	$20
December gap	-$98
Solutions	
9C cuts	$119
Revenue offset	-$21
Fiscal condition as of January	$0

Unfortunately, the real fiscal difficulties of FY 2017 occurred in the last half of the year as tax revenues fell $452 million short and spending increased by $78 million. It is this combination of declining tax revenues and spending increases that policymakers have continued to grapple with through the middle of October.

Figure 2. End of Year Gap

Tax shortfall post December	-$452
Additional spending needs	
Snow & ice	-$34
Sheriffs	-$28
Other	-$16
Total end of year gap	-$530

In total, the state's midyear budget gap for FY 2017 is $922 million and its causes can be organized as follows:

Figure 3. Causes of the FY 2017 Budget Gap

Category	Amount	% of Total
Tax Downgrades		
October downgrade	$175	68.0%
Shortfall post December	$452	
Underfunded Accounts		
DOC & Sheriffs	$77	32.0%
Snow & Ice	$64	
CPCS	$57	
Labor costs	$23	
Family Homelessness	$21	
Other	$53	
Total	***$922***	***100.0%***

The causes of this year's gaps are all too familiar: revenue estimates that were too optimistic and spending obligations not fully funded in the original budget. As Figure 1 shows, $392 million of the $922 gap has been closed, leaving $530 million yet to be addressed.

It is important to note that these gap presentations are over simplifications. The budget has thousands of moving revenue and spending parts and just as several unanticipated spending needs arose in the second half of the year, these were largely offset by spending obligations that were not ultimately necessary. Those offsets are presented in the budget solutions below, but could be used to adjust the gaps shown above.

Budget Solutions

If the causes of FY 2017's fiscal problems are not surprising, neither are the solutions that are being relied upon: one-time revenues (largely from trust fund balance sweeps), non-tax revenue increases and forcing appropriated funds to go unspent (commonly called reversions). Unfortunately, final non-tax revenue and reversion information is not yet available and so the part they play in balancing the budget can only be estimated.

Figure 4. Likely End of Year Budget Solutions

FY 2017 Solutions	
Known	
Trust fund balance sweeps	$57
Lottery revenues	$19
Supplemental budget	$15
Estimated	
Reversions	$125
Initial deficiencies not requiring action	$90
Non-tax revenue (federal)	$200
Non-tax revenue (other)	$25
Total solutions	***$531***

Once again, the state relies on trust fund balance sweeps to make up for tax shortfalls.. The Administration has notified the Legislature of their intent to transfer up to $140 million in trust revenues to the General Fund. However, most of this trust revenue was already assumed in earlier gap closing exercises, leaving $57 million in new trust revenue to close the year end gap. In addition, a $19 million is generated through higher than expected lottery revenues and two technical provisions included in the final supplemental provide a further $15 million.

By comparing the Commonwealth's most recent information statement (released on September 27th) with earlier information statements, we can infer non-tax sources of revenue that will help the budget situation. It appears that these sources will provide approximately $225 million toward the state's budget solution.

The reversion estimate in Figure 4 is based on reversion totals from recent years. Total reversions for FY 2017 will likely exceed $350 million. However, as MTF noted last year, $200 million of that amount was already budgeted for in the original FY 2017 budget, meaning that only reversions in excess of that amount will help to close the final budget gap. Finally, several deficiencies the Administration had tracked throughout the year did not materialize, reducing the final gap by $90 million.

Implications for FY 2018

The FY 2018 budget picture remains in flux as the Legislature completes budget veto overrides and the fiscal impact of health care reform legislation remains unclear. The state's FY 2017 experience is not a template for ongoing budget success. Overestimating likely tax revenues while simultaneously underestimating spending needs has now hamstrung the state budget for three consecutive years. Hopefully, the FY 2018 Conference Committee's significant reduction of estimated tax revenue available coupled with the $100 million set aside to address underfunded accounts will reduce the likelihood of a budget deficit. However, if all of the Governor's spending vetoes are overridden without an offsetting increase in tax collections, we are likely to see a repeat performance of the FY 2017 budget balancing act.