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# MTF Bulletin

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## FY 2023 Consensus Tax Revenue Agreement

Budget leaders from the House, Senate, and Administration have agreed on \$36.9 billion as the consensus tax revenue figure for the fiscal year 2023 budget. Budget makers expect tax revenues to grow by \$967 million (2.7 percent) over estimated FY 2022 collections of \$35.95 billion. The FY 2022 tax revenue figure has also been revised upward by \$1.55 billion over the \$34.4 billion used in crafting the current year budget.

Figure 1. FY 2023 Consensus Tax Revenue Agreement Summary

Original FY 2022 Revenue Benchmark	Revised FY 2022 Revenue Benchmark	FY 2023 Consensus Revenue	\$ increase	% increase
\$34,401	\$35,948	\$36,915	\$967	2.7%

*\$ in millions*

### FY 2023 Agreement in Context

On December 21<sup>st</sup>, MTF, along with the Department of Revenue and other experts participated in the annual Consensus Revenue Hearing, at which the various presenters provided tax projections and economic analysis to the Ways and Means Committees and the Executive Office of Administration and Finance. The revenue projections, summarized in Figure 2., varied, but shared two themes:

1. FY 2022 tax revenues would likely exceed the current benchmark by at least \$1 billion.
  - At the time, year-to-date revenues had exceeded benchmark by \$914 million and through December, tax collections are now on pace to exceed the \$34.4 billion original benchmark by \$1.55 billion.<sup>1</sup>
2. Tax revenue growth is likely to slow in FY 2023.
  - Each estimate projected lower year-over-year tax revenue growth in FY 2023 compared to FY 2022.

<sup>1</sup> Tax collections through December are \$2.1 billion over year-to-date benchmark, but DOR believes that \$593 million of this amount will be refunded to tax payers later in the year, related to the state’s recent adoption of an optional Pass Through Entity tax.

A more general theme common to most presentations was the high degree of uncertainty that colored this year’s projections due to the pandemic and the economic challenges related to labor shortages, inflation and supply chains.

The final tax revenue agreement reflects these consensus themes. The revised FY 2022 revenue estimate assumes 5.3 percent growth over FY 2021, while the FY 2023 figure assumes that growth will slow to 2.7 percent. The \$36.9 billion revenue estimate is close to the median of the revenue projections provided at last month’s hearing.

*Figure 2. FY 2023 Consensus Revenue Hearing Summary*

	Current Benchmark	FY 2022 Est.	v. Current BM	FY 2023 Est.	v. Current BM	v. FY 2022 projection	FY 2023 % v. FY 2022 estimate
DOR Upper	\$34,401	\$36,623	\$2,222	\$37,684	\$3,283	\$1,061	2.9%
DOR Lower		\$35,726	\$1,325	\$36,484	\$2,083	\$758	2.1%
MTF		\$37,223	\$2,822	\$37,633	\$3,232	\$410	1.1%
cSPA		\$35,400	\$999	\$36,500	\$2,099	\$1,100	3.1%
BHI		\$36,106	\$1,705	\$37,047	\$2,646	\$941	2.6%
ACM		\$38,301	\$3,900	\$40,795	\$6,394	\$2,494	6.5%
<i>Median</i>		\$36,365	\$1,964	\$37,340	\$2,939	\$976	2.7%
<b><i>FY 2023 CR Agreement</i></b>		<b><i>\$35,948</i></b>	<b><i>\$1,547</i></b>	<b><i>\$36,915</i></b>	<b><i>\$2,514</i></b>	<b><i>\$967</i></b>	<b><i>2.7%</i></b>

*\$ in millions*

*Pre-Budget Transfers and the Consensus Revenue Agreement*

The consensus revenue agreement also typically includes spending levels for four “pre-budget transfers” that take place outside of the appropriations process and are primarily related to specific debt and pension obligations of the commonwealth. Two of these transfers, one to the state’s School Building Authority and the other to the MBTA, are based on expected sales tax revenues. These guaranteed transfers from the state help improve the creditworthiness of SBA and MBTA when they sell bonds for capital expenditures, thereby saving on borrowing costs.

The third major pre-budget transfer included in the revenue agreement is the state’s annual contribution to the pension fund. This contribution is determined on three-year schedules, last established in the FY 2021 budget.

*Figure 3. FY 2023 Pre-Budget Transfers*

	Guaranteed Amount	Transfer based on CR Agreement	Total Transfer
Workforce Trust Fund	\$0	\$25	\$25
School Building Authority	\$0	\$1,165	\$1,165
MBTA	\$160	\$1,165	\$1,325
Pension fund	\$3,744	\$0	\$3,744
<b>Total pre-budget transfers</b>			<b>\$6,259</b>

*\$ in millions*

### *Estimated Capital Gains Revenue*

The final element of the revenue agreement that will affect next year’s budget is the estimate of capital gains tax revenues to be collected. Capital gains collections are extremely volatile and so lawmakers put in place a law requiring that collections over an annual threshold be automatically deposited in the state’s Stabilization Fund and other liabilities.<sup>2</sup> This mechanism is designed to limit the operating budget’s exposure to unpredictable capital gains trends.<sup>3</sup>

As MTF and DOR recommended in their consensus revenue testimony, the revenue agreement expects capital gains collections to fall significantly in FY 2023 to \$2.277 billion.<sup>4</sup> The capital gains threshold in FY 2023 is \$1.404 billion, which means that \$873 million of the FY 2023 tax figure will automatically be set aside for reserves and not available for the budget.

### *Next Steps*

Governor Baker will submit his eighth budget proposal on January 26<sup>th</sup> which will use the consensus tax figure as its foundation. Total tax revenues assumed in the Governor’s budget will depend on any tax revenue policy proposals put forward or assumed in his bill, but the starting point will be the consensus revenue estimate less several pre-budget transfers and adjustments.

*Figure 4. FY 2023 Tax Revenues Available for Budget*

<b>Consensus revenue</b>	<b>\$ 36,915</b>
<i>Cap. Gains transfer</i>	-\$873.0
<i>Workforce Training</i>	-\$25.0
<i>SBA</i>	-\$1,165.0
<i>MBA</i>	-\$1,325.0
<i>Pension</i>	-\$3,744.0
<b>Taxes remaining for budget</b>	<b>\$ 29,783</b>

*\$ in millions*

In both FY 2020 and FY 2021, unforeseen revenue changes resulted in major revenue adjustments late in the budget process. Budget-makers must remain prepared to adjust this FY 2023 figure should economic circumstances change.

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<sup>2</sup> 90 percent of above benchmark capital gains is dedicated to the Stabilization Fund, while 10 percent is dedicated to pension and retiree health insurance liabilities.

<sup>3</sup> The wisdom of the capital gains threshold is likely to be apparent over the coming year. MTF and DOR expect capital gains collections to reach record levels in FY 2022 and to fall sharply in FY 2023.

<sup>4</sup> MTF estimates FY 2022 capital gains collections of \$2.9 billion, while DOR forecasted a range of \$2.4 to \$2.7 billion.