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# *MTF Bulletin*

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## FY 2022 Budget Conference Summary

The House and Senate have enacted a $48.1 billion fiscal year (FY) 2022 budget, about a week after the start of the new fiscal year. The budget now moves to the Governor's desk, where he has ten days to sign the budget and return vetoes and amendments.

### FY 2022 Revenue

The critical fiscal question before budget conferees was how to adjust underlying revenue assumptions in light of strong tax collections in FY 2021. The conference committee elected to upgrade tax revenues by $4.23 billion, from the original $30.12 billion to $34.35 billion. This upgrade falls within the range of reasonable revenue estimates presented by MTF in its conference preview, as it implies revenue growth of about one percent compared to likely FY 2021 collections.

*Figure 1. Conference Committee Tax Revenue Adjustment*

| | Consensus Revenue | Conference Adjustment | Difference |
|---|---|---|---|
| Tax revenue assumption | $30,120 | $34,350 | $4,230 |
| Pre-budget transfers | -$5,629 | -$5,751 | -$122 |
| Excess cap gains | -$165 | -$1,263 | -$1,098 |
| Set aside for SOA | $0 | -$350 | -$350 |
| Set aside for pension | $0 | -$250 | -$250 |
| **Remaining tax revenue** | **$24,326** | **$26,736** | **$2,410** |

*$ in millions*

The conference committee budget assumes that $2.6 billion in FY 2022 tax revenue will be capital gains collections. This level of capital gains would result in the automatic transfer of $1.26 billion to the state's Stabilization Fund and other reserves. The automatic transfer to reserves is equal to the level of capital gains collections in excess of the $1.352 threshold amount established for FY 2022.

The conference committee tax revenue upgrade enables budget-makers to eliminate planned usage of one-time revenues, notably a draw from the Stabilization Fund, to balance the budget. In total, the conference committee report eliminates more than $1.8 billion in one-time resources or other questionable budget assumptions while also increasing funding for several underfunded accounts by $50 million. The conference report does continue to rely on $50 million in tax settlement revenue; given ample tax collections, it is advisable to eliminate this assumption for the purpose of the budget.

The conference committee budget also includes $90 million in revenue related to a Senate proposal to allow partnerships and other eligible businesses to pay state income tax at the entity level, thereby lessening the federal income tax burdens for effected taxpayers. As explained here, the Senate proposal would result in additional revenue for the state. This new tax revenue is offset by an assumed FY 2022 revenue loss of $18.6 million due to a Senate provision that makes the state's child tax credit fully refundable and a proposal first put forward by the Administration to extend the tax deductibility of MEFA college savings plans. The conference report retains a provision to delay implementation of a state charitable tax deduction, but does not include Senate language to allow debit card purchase of lottery tickets.

## FY 2022 Spending

The conference committee budget includes $48.1 billion in total spending. This level includes all spending included in either the House or Senate budgets and adds approximately $90 million in new spending. In total, the conference committee report adds approximately $350 million in line-item spending and increases pre-budget transfers (which are tied to tax revenue) by $122.7 million. The conference report also eliminates a $200 million savings assumption which reduced bottom line spending in both the House and Senate budgets.

*Figure 2 FY 2022 Spending Comparison*

| | FY 2021 Current | FY 2022 Gov | FY 2022 House Final | FY 2022 Senate Final | FY 2022 Conference |
|---|---|---|---|---|---|
| Line item spending | $45,840.0 | $45,399.9 | $47,234.2 | $47,251.7 | $47,613.9 |
| MATF | $537.2 | $456.5 | $471.4 | $471.4 | $471.4 |
| **Line item & MATF** | **$46,377.2** | **$45,856.3** | **$47,705.6** | **$47,723.1** | **$48,085.2** |
| **Pre-budget transfers** | $5,331.0 | $5,628.6 | $5,628.6 | $5,628.6 | $5,751.3 |
| **Supp assumption** | $173.9 | $0.0 | $0.0 | $0.0 | $0.0 |
| Assumed reversions | -$109.6 | $0.0 | -$200.0 | -$200.0 | $0.0 |
| **Total Spend** | $51,772.5 | $51,484.9 | $53,134.2 | $53,151.7 | $53,836.5 |
| **Difference v. conference** | $2,064.0 | $2,351.6 | $702.3 | $684.9 | NA |

In spite of the significant tax revenue upgrade, budget conferees heeded MTF's recommendation to not add significant new budget spending not proposed by either the House or Senate. Instead, budget conferees set aside $600 million of the estimated surplus to apply to long-term spending obligations. Of this amount, $350 million is to a trust fund used to support implementation of the Student Opportunity Act (SOA) and $250 million to make a supplemental payment to the state's unfunded pension liability. Based on the pension's assumed annual rate of return (7 percent), this supplement will reduce the state's pension liability by $690 million over the next 15 years. The conference budget also adds $50 million in spending to fully fund expected snow and ice costs for FY 2022 and provides smaller spending increases of approximately $45 million to a variety of

House and Senate priorities. These spending increases include $18.4 million in added funding for workforce development programs about half of which ($9.4 million) is added to support for career technical institutes. With this increase, the budget provides appropriate levels of funding for a series of accounts that have often been underfunded in recent years and contributed to annual budget deficits.

## FY 2022 Surplus and Stabilization Fund

After accounting for all spending, the SOA and pension set asides and anticipated deposits in the Stabilization Fund and other reserves, the conference budget assumes a revenue surplus – approximately $150 million – in the coming year. As MTF recently advised, taking a deliberate approach to the use of any FY 2021 and FY 2022 revenue surpluses is the best course of action because a significant share of recent collections may be temporary in nature and because it enables policymakers to coordinate state surpluses and federal American Recue Plan (ARPA) resources. The conference committee budget adheres to this approach.

*Figure 3. Tax Surplus Detail*

| ***Tax revenue increase*** | ***$4,230*** |
|---|---|
| ***Surplus Offsets*** | |
| Increase in prebudget transfers | -$122 |
| Increase in cap gains surplus | -$1,100 |
| Eliminate one-timers | -$1,600 |
| Eliminate reversion/reduce settlements assumtion | -$285 |
| Additional budget spending | -$375 |
| SOA set aside | -$350 |
| Pension set aside | -$250 |
| ***Surplus remaining*** | ***$148*** |

*$ in millions*

Budget conferees project that the state will end FY 2022 with a Stabilization Fund balance of $5.77 billion. This balance assumes a fund deposit of approximately $1.1 billion from the FY 2021 surplus and a further $1.2 billion in FY 2022. Achieving a balance well in excess of $5 billion is a critical goal for the Commonwealth as we build our economic recovery and prepare for future challenges.

## FY 2022 Policy

The House and Senate budgets included 13 different tax policy proposals. The final conference report adopts 10 of these proposals in whole or in part:

*Figure 4. Resolution of Tax Policy Differences*

| | House | Senate | Conference Report |
|---|---|---|---|
| Permanent film tax credit | ✓ | ✗ | ✓ |
| Film tax credit restrictions | ✗ | ✓ | Partial |
| Pass-through entity SALT change | ✗ | ✓ | ✓ |
| Child & dependent tax credit | ✗ | ✓ | ✓ |
| Disabled employee tax credit | ✓ | ✗ | ✓ |
| Historic rehab credit extension | ✓ | ✗ | ✓ |
| Cranberry bog credit | ✗ | ✓ | ✓ |
| Elimination of transferable medical device credit | ✗ | ✓ | ✓ |
| Elimination of energy patent deduction | ✗ | ✓ | ✓ |
| Elimination of harbor tax credit | ✗ | ✓ | ✓ |
| Rural growth tax credit | ✓ | ✗ | ✗ |
| Conservation land tax credit increase | ✓ | ✗ | ✗ |
| Increased TNC fees | ✗ | ✓ | ✗ |

Figure 5. summarizes the final disposition of several other notable policy sections summarized in MTF's recent conference preview:

*Figure 5. Other Notable Policy Differences*

| Title | Branch of Origin | Summary | Disposition |
|---|---|---|---|
| MassHealth supplemental rebates | Senate | Expands MassHealth's authority to negotiate supplemental rebates for pharmaceuticals and medical devices. | Not included |
| Sheriff salary increase | House | Increases sheriff salaries by between $13,000 and $20,000 (depending on the county). | Included (though raises not tied to DA salary) |
| Employer protections on commissioned pay | Senate | Limits penalties that can be applied to employers of commissioned workers whose pay was impacted by a 2019 SJC ruling. | Not included |
| Wind energy career training program | House | Creates a new wind training program, capitalized with $13 million. | Included |

## Next steps

Governor Baker now has until July 19th to sign the budget. As part of the budget signing process, the Governor can veto spending for individual line items, strike line item language or policy sections and proposed amended language for budget provisions. In most years, spending vetoes are likely if the Administration determines that conference committee appropriations are unsupportable or that conference committee revenue assumptions are unrealistic. Given the strength of tax collections, it is unlikely that the Administration will make spending vetoes in order to balance the budget, but could reduce spending based on policy differences.

*Figure 5. Governor Baker's Veto Actions, FY 2016 – FY 2021*

| | FY 2016 | FY 2017 | FY 2018 | FY 2019 | FY 2020 | FY 2021 |
|---|---|---|---|---|---|---|
| Line items reduced | 96 | 302 | 167 | 45 | 0 | 136 |
| $ reduction | $162.8 | $264.1 | $320.2 | $48.9 | $0.0 | $159.3 |
| Sections vetoed | 21 | 36 | 9 | 0 | 0 | 0 |
| Sections amended | 9 | 23 | 25 | 19 | 9 | 17 |

*$ in millions*

In recent years, the Baker Administration has elected to return policy sections with amendment, rather than veto outright. When a section is returned with amendment, the legislature must decide whether to reject, amend or adopt the Governor's proposal in the form of a new bill. Governor retains the ability to veto amendments once they return to his desk.

In addition to Governor Baker's veto actions, budget-makers must now turn their attention to closing the books on FY 2021 and appropriating Fiscal Recovery Funds, provided through ARPA. The combination of state and federal resources available to assist communities, residents and employers disproportionately impacted by the pandemic must also be used to catalyze the Commonwealth's continued recovery and to shore up the state's medium and long-term fiscal position.