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MTF Bulletin

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FY 2023 Budget Conference Committee Preview

Budget conferees are negotiating spending, revenue and policy differences between the House and Senate proposals in order to present a final budget to Governor Baker for the start of fiscal year 2023. For the second straight year, conferees must also significantly revise the budget's tax revenue estimate due to current year collections outpacing original projections by billions.

This Bulletin highlights the major decision points confronting budget-makers, provides a framework for revising tax estimates and assesses how the FY 2023 final budget can accommodate spending priorities and tax relief.

Budget Spending

The House and Senate budgets totaled close to $50.5 billion in line-item spending, with more than 98 percent of all spending common to both budgets. This shared amount will form the foundation of the final conference report and is not subject to negotiations.

FY 2023 Budget Comparison

	House	Senate
Total spend	$50,335	$50,498
Unique earmarks	$95	$137
Other unique	$609	$731
Spending in common	**$49,631**	

$ in millions

The focus of conference committee spending negotiations will be the $1.6 billion in spending unique to either budget. The House budget includes $704.4 million in spending not included in the Senate, while the Senate budget funds $867.8 million in proposals not adopted by the House. This amount of unique spending is a record, and far surpasses the $588 million in unique spending in last year's budget.

Notable House/Senate Spending Differences

	House Unique	Senate Unique	Total Unique
Early education investments	$48	$265	$313
Unique earmarks	$95	$137	$232
Universal school meals	$110	$0	$110
MassDOT subsidy	$0	$62	$62
Developmental disability community programs	$51	$0	$51
Housing	$31	$17	$48
Small business/community grants	$24	$20	$44
Elder care wage increases	$40	$0	$40
Behavioral health investments	$20	$20	$40
Nursing home rates	$0	$40	$40
Higher education endowments/scholarships	$20	$19	$39
Senior care	$0	$36	$36
UGGA	$0	$32	$32
Correctional phone calls	$20	$0	$20

Extension of federal programs created during the pandemic factors heavily in the spending differences. For example, the Senate budget includes $250 million to extend through the first six months of FY 2023 early education stabilization grants, first introduced in the summer of 2021. The House includes $110 million to maintain universal school meals through the coming school year rather than let the federal waiver that loosened standard restrictions expire at the end of June.

During the pandemic, the federal government created or expanded a number of programs that have or will soon sunset. In some instances, like early education, new federal programs have enabled the state to try new funding methods that could serve as a model for future state spending. Because the state is not in a position to simply extend or replace all federal programs policymakers must be careful with the fiscal precedents they set now as they assess the future of these programs.

In order for the final bill to accommodate all House and Senate spending, the bottom line for the conference budget will have to increase by approximately $700 million over the Senate final level.[1] Usually, this level of spending increase would not be possible with available resources. However, the consensus tax revenue figure used for the House and Senate budgets does not reflect current

[1] The conference report may also increase budget spending by a further $600 million to account for the extension of the federal Public Health Emergency through the end of October. The PHE provides states with enhanced Medicaid reimbursements, but also requires that the state maintain MassHealth enrollment. The extension of the PHE should be budget neutral, as the combination of standard and enhanced reimbursement is likely to match or exceed new spending.

reality and needs to be upgraded significantly. That upgrade is likely to support House and Senate spending initiatives.

Budget Revenue

FY 2022 Context

The House and Senate budgets build off of the $36.915 billion consensus tax revenue figure established in January. Since January the revenue landscape has fundamentally changed. FY 2022 tax collections have exceeded projections by $4.4 billion, and are on pace to total more than $40 billion in taxes for the year.

FY 2022 Tax Collection Summary

FY 2022 tax estimate at time of consensus revenue	$35,948
May upgrade	$1,718
Current above benchmark	$2,666
Current pace	**$40,332**
$ in millions	

If current collection trends continue in June, FY 2022 will be the second straight year in which the state has recorded tax revenue growth of more than 20 percent over the prior year. Since FY 2020, tax collections will increase by more than 35 percent. This is more than double any other two-year period in at least 20 years.

Tax collections have been strong across the board, with each major collection category growing by at least 8.6 percent, but the strongest growth has been in non-withheld income which has increased 77.6 percent through May. The strength of non-withheld income boosts state coffers in the current year but could prove temporary for two reasons. Capital gains comprise much of this revenue, and they are always volatile and tied to the economic cycle. The Department of Revenue has already certified $3.5 billion in FY 2022 capital gains tax collections through May, $799 million more than the amount assumed by budget-makers. Capital gains collections could easily fall next year if the economy continues to falter.

Second, the state implemented a new pass-through entity tax option this fiscal year, which provides relief from the federal limit on state and local tax deductions and also provides a revenue boost to Massachusetts. This new tax policy has significantly increased payments through non-withheld income tax, but much of the money collected will be paid back in future refunds. DOR does not yet know to what extent the FY 2022 boost in these taxes will be refunded next year.

Even with these caveats in mind, it is likely that the state will collect $3 billion or more in tax collections in FY 2022 than either the House or Senate budgets assumed would be collected in FY 2023. Clearly, budget-makers must adjust the FY 2023 tax estimate. The question is: what adjustment is reasonable and fiscally prudent?

Lesson's from Last Year's Revenue Upgrade

Last year's budget process provides a useful guide as to how the conference committee may adjust its revenue projections. Like this year, tax collections in the first six months of 2021 blew past original expectations, growing by more than 20 percent and totaling $3.915 billion above benchmark by the time conference committee negotiations began. Similar to the current situation, non-withheld income taxes made up more than half of new revenue growth.

2021 v. June 2022 Revenue Picture through May

	FY 2021	FY 2022
Year over Year Growth		
Year-over-year tax revenue growth $	$5,689	$6,519
Year-over-year tax revenue growth %	23.0%	21.4%
Non-withheld income as % of revenue growth	55.4%	50.5%
Growth Against January Benchmark		
$ above benchmark	$3,938	$4,384
Conference budget revenue upgrade	**$4,230**	**TBD**

To reflect the changed tax revenue situation, budget conferees increased the FY 2022 tax revenue estimate by $4.2 billion. However, the uncertain economic outlook and the impact of the pass-through-entity tax change add new complications to this year's reforecast.

Likely FY 2023 Upgrade

In order to determine the upgrade, budget conferees must settle on a projected FY 2023 tax revenue growth rate for both volatile and more stable forms of tax revenue. As noted above, capital gains and other forms of non-withheld income tax have made up a large share of revenue growth, but the continuation of that trend is far from certain. Conferees should account for this uncertainty by assuming that non-withheld income collections decline in FY 2023.

Possible FY 2023 Tax Upgrade Scenarios

		All other tax revenue				
		Flat	**1.5% growth**	**2.5% growth**	**3.5% growth**	**4.5% growth**
Non-withheld income	**Falls by 30%**	$37,945.5	$38,431.2	$38,754.9	$39,078.7	$39,402.5
	Falls by 20%	$38,741.0	***$39,226.7***	***$39,550.4***	***$39,874.2***	$40,198.0
	Falls by 10%	$39,536.5	***$40,022.2***	***$40,345.9***	***$40,669.7***	$40,993.5
	Flat	$40,332.0	$40,817.7	$41,141.4	$41,465.2	$41,789.0

The figure above presents a range of possibilities based on declining or flat non-withheld income and flat or limited growth for other tax categories. The bolded and italicized figures represent a reasonable range of assumptions. At the low end (20 percent decline in non-withheld/1.5 percent growth in other areas), the FY 2023 tax figure would be upgraded by $2.3 billion, while a more optimistic scenario (10 percent decline in non-withheld/3.5 percent growth in other areas), would result in a $3.8 billion upgrade.

The impact of a revenue upgrade on the budget depends on both the total amount and the composition of the upgrade. The table below estimates how two plausible upgrades would affect the budget bottom line.

Budget Impact of Possible Revenue Upgrades

	Scenario 1	Scenario 2
Total upgrade	$2,312.0	$3,754.0
Assumed capital gains	$793.0	$1,190.8
Capital gains to Stabilization Fund	-$793.0	-$1,190.8
Dedicated to MBTA/SBA	-$23.2	-$43.9
Revenue remaining	**$1,495.8**	**$2,519.3**

Capital gains will comprise a large share of any upgrade and all above-threshold capital gains will automatically be set aside for the Stabilization Fund and other long-term liabilities. In addition, one-third of the sales tax revenue upgrade (excluding meals tax) will be split between the MBTA and the School Building Authority. After accounting for these offsets, the upgrades summarized above would increase FY 2023 budget resources by between $1.5 and $2.5 billion.

Budget Policy

The House and Senate budgets include 253 policy sections, of which 58 are common or very similar and 196 are unique.

Budget Policy Sections

Total section	253
In common	58
House unique	82
Senate unique	113
Total unique	**195**

A number of the major policy differences relate to health care. The House included a two-year pilot to expand subsidy eligibly for ConnectorCare, while the Senate included provisions instituting an assessment on health insurance payers, expanding MassHealth's powers to negotiate pharmaceutical and medical device rebates, and protecting state residents from legal liability for providing health services that are illegal in other jurisdictions.

Notable House v. Senate Policy Differences

Title	House	Senate	Description
ConnectorCare expansion pilot	✓	×	Creates a two-year pilot (beginning in June 2023) to increase Connector premium subsidies to 500 percent of FPL
DA & sheriff pay raises	✓	×	Increases the salaries of district attorneys and sheriffs.
Conservation land tax credit	✓	×	Increases the cap on the credit to $5 million for 10.
Drug coupons	✓	×	Extends prescription drug coupons through FY 2026
PFML wage replacement	✓	×	Allows PFML users to use vacation and sick time concurrent with PFML.
Reproductive health protections	×	✓	Makes a number of statutory changes to protect Massachusetts health providers (and other residents) and non-Massachusetts residents from consequences related to the provision of reproductive/gender-affirming health services in Massachusetts that not be authorized in other jurisdictions.
Behavioral health crisis assessment	×	✓	Creates a three-year assessment on health insurance payers to support improvement of behavioral health crisis services. After three years, the HPC is to provide recommendations for ongoing financing.
MassHealth rebate expansion	×	✓	Expands MassHealth's authority to negotiate supplemental rebates for pharmaceuticals and medical devices.
Remote meeting and notarization	×	✓	Extends the legal authorization for remote municipal/board meeting and notary public services.
Indigence assessment	×	✓	Eliminates $150 fee for indigent defendents seeking CPCS representation

Tax Relief

Neither the House nor Senate budgets include major relief proposals, but both branches have stated plans to take up tax relief before the end of session.[2] The scope of the tax relief that ultimately goes to the Governor will be affected by the FY 2023 revenue upgrade.

Revenue Upgrade & Tax Relief[3]

	Scenario 1	Scenario 2
Total upgrade	$2,312.0	$3,754.0
Short-term capital gains adjustment	-$117.0	-$117.0
Assumed capital gains	$676.0	$1,073.8
Capital gains to Stabilization Fund	-$676.0	-$1,073.8
Dedicated to MBTA/SBA	-$23.2	-$43.9
Revenue remaining	**$1,495.8**	**$2,519.3**
Net additional spending	$650.0	$650.0
Governor Baker tax relief (non-cap gains)	$624.0	$624.0
Revenue remaining	**$221.8**	**$1,245.3**

[2] The House and Senate budgets both include provisions to update the state's income tax code to conform to the 2021 federal code.

[3] The Net additional spending is total budget spending not supported by revenues included in either the House or Senate budget.

In both of the plausible upgrade scenarios in the table above, the FY 2023 budget would have ongoing revenue capacity to include House and Senate spending priorities, and the $624 million tax relief package proposed by Governor Baker. In each scenario, the estimated end of year Stabilization Fund balance would exceed $8 billion.

Bottom Line

The task before FY 2023 budget conferees is multi-faceted. Not only must they resolve all spending and policy differences between the two budgets, but they also must determine a plausible and prudent level of tax revenue for FY 2023. The data support a significant upgrade over the tax figure agreed to in January, but budget-makers must use caution as they make their calculations and account for a likely decline in non-withheld income tax.

A reasonable revenue upgrade enables the final FY 2023 budget to include major House and Senate spending priorities while further augmenting the state's reserves. The final FY 2023 budget will also set the stage for consideration of a meaningful and balanced tax package that provides much needed relief to taxpayers.