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ateMTF Bulletin

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FY 2025 AND FY 2026 TAX REVENUE FORECAST – RISKS ABOUND

Fiscal Year (FY) 2025 and FY 2026 tax revenues are projected to rebound to positive growth, after non-surtax revenue declines in FY 2022 and FY 2023; but overarching questions about the global economy and federal policy changes cloud the state’s larger fiscal picture. The Massachusetts Taxpayers Foundation (MTF) projects non-surtax revenues of \$40.9 billion in FY 2026, an increase of 3.1 percent over the revised FY 2025 estimate of \$39.7 billion. Gains in personal income taxes (PIT) and corporate taxes drive growth, as sales tax revenue growth lags and other taxes recover from faltering estate tax collections.

Based on the preliminary Department of Revenue surtax estimate of \$2.199 billion in FY 2024 collections, MTF estimates income surtax collections of \$2.5 billion in FY 2025 and \$2.6 billion in FY 2026.

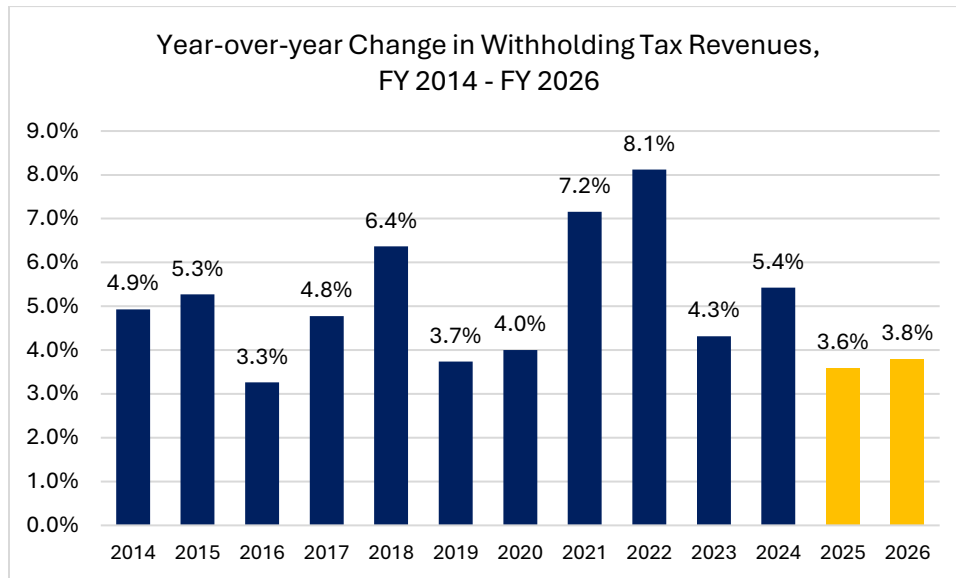
Table 1 - Tax Revenue Forecast

	FY 2023	FY 2024	FY 2025	FY 2026	2025 v 2026	
					\$	%
PIT (non-surtax)	21,539	21,917	22,693	23,596	903	4.0%
Withholding	16,602	17,503	18,133	18,822	689	3.8%
Cap gains	2,280	2,070	2,153	2,265	112	5.2%
Other	2,657	2,344	2,408	2,509	102	4.2%
Sales	9,403	9,323	9,527	9,636	110	1.2%
Corp	5,054	4,833	4,997	5,182	185	3.7%
Other	2,924	2,528	2,452	2,490	38	1.6%
Total	38,920	38,600	39,670	40,905	1,235	3.1%
4% Surtax	242	2,199	2,451	2,619		

WITHHOLDING INCOME TAX REVENUE GROWTH MODERATES

Non-surtax withholding income tax revenues are expected to increase by \$630 million in FY 2025 and by a further \$689 million in FY 2026, reaching a total of \$18.8 billion (Table 1). These increases represent a moderation in growth to 3.6 percent and 3.8 percent respectively, which remains below the 10-year average of 5 percent (chart below).

Reduced job openings offer one indication of a softening labor market in the state. In September 2023, there were 1.9 job openings per unemployed person in Massachusetts. One year later, that ratio fell to 1.3 as the number of openings declined and the number of unemployed residents climbed. Another indicator comparing job growth with the change in the state’s labor force shows a modest increase in private sector jobs of 30,000 over the past 12 months while the civilian labor force jumped 100,000. These data suggest a more modest pace in wage and salary growth.¹



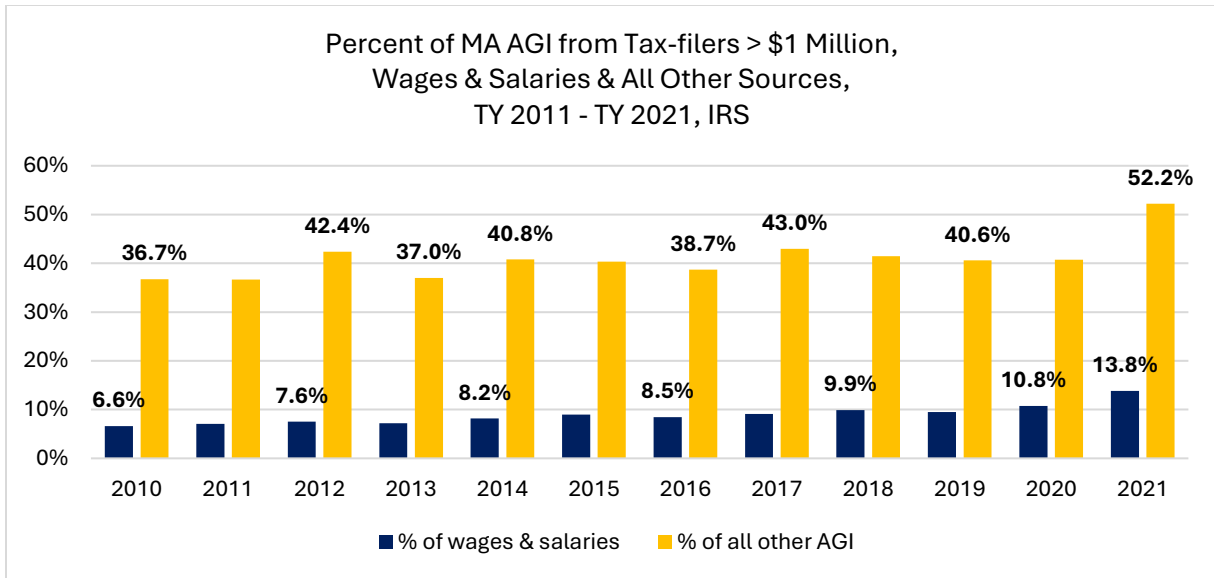
NON-WITHHOLDING TAX COLLECTIONS RETURN TO TREND

MTF estimates non-withholding tax revenues at \$4.8 billion in FY 2026, up from \$4.6 billion in FY 2025, representing growth rates of 4.7 percent and 3.3 percent respectively.

Non-surtax capital gains and other non-withholding tax revenues from sources that include interest, dividends, and partnership/S Corporations, fell by \$525 million in FY 2024, a 10 percent drop from the previous year. In contrast, surtax capital gains and other non-withholding tax revenues reached \$1.74 billion, and that figure is likely to increase once FY 2024 surtax revenues are certified.

As shown in the table below, Adjusted Gross Income (AGI) from wages and salaries of tax-filers earning more than \$1 million represented approximately 11 percent of the state total from Tax Years (TY) 2017 – TY 2021. However, non-withholding AGI for these same tax-filers averaged 44 percent, demonstrating a confluence with surtax revenues. In fact, non-withholding income tax revenues accounted for nearly 80 percent of surtax revenues in FY 2023 and FY 2024.

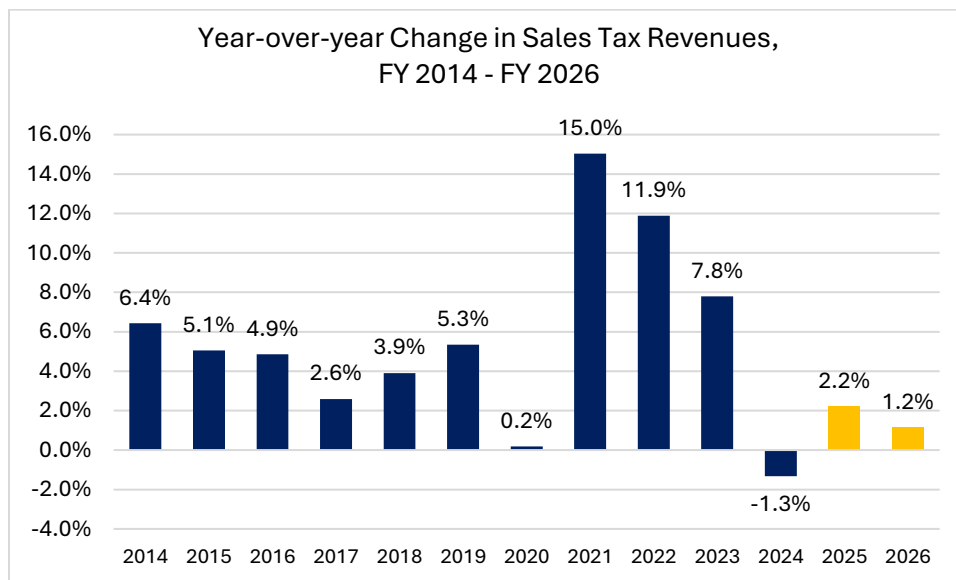
¹ See MTF’s Massachusetts Demographics Have Slowed the Economy; Could International Immigration Revive Growth? Slide 22, December 2024.



SALES TAXES SHOW MODERATE REBOUND FROM FY 2024

MTF expects sales tax revenues of \$9.6 billion in FY 2026, an increase of \$100 million from the revised FY 2025 projection of \$9.5 billion.

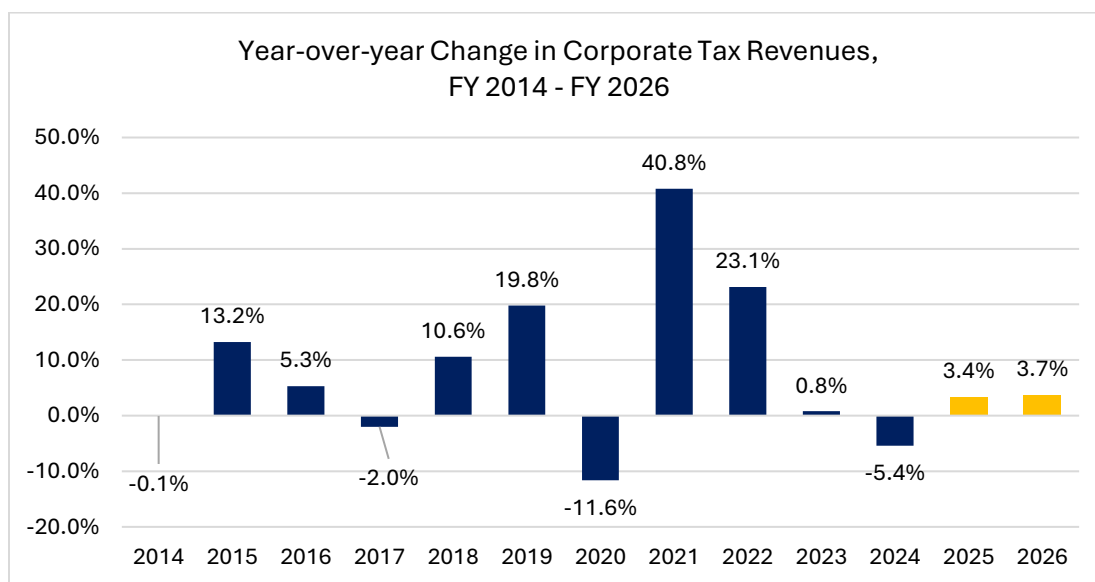
Sales tax revenue growth, which accounted for approximately 24 percent of total revenues in FY 2022 - FY 2024, has declined steadily since the early days of the pandemic when purchases shifted from services to durable goods. Year-over-year growth spiked to 15 percent in FY 2021, fell to 11.9 percent in FY 2022, and then to 7.8 percent in FY 2023 before turning negative at 1.3 percent in FY 2024 (table below).



MTF expects sales tax revenue growth will turn positive, but remain below the 4.7 percent average gains from FY 2014 – FY 2019 as consumers scale back purchases of durable goods and motor vehicles in part due to increasing costs and high interest rates. This projection is consistent with the recent findings from a Retailers Association of Massachusetts (RAM) member survey, that expects a 1.5 percent increase in local holiday shopping sales this season.²

CORPORATE TAXES RECOVER MODESTLY

Corporate taxes should bounce back into positive growth after falling in FY 2024, reaching \$5.2 billion in FY 2026, up \$200 million from \$5 billion in FY 2025.



OTHER TAXES TUMBLE

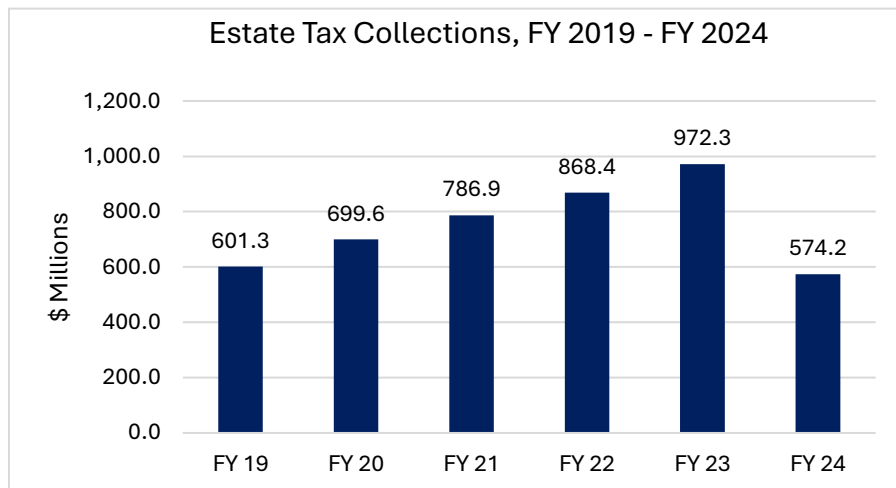
Revenues from other taxes are expected to plateau at just below \$2.5 billion in FY 2025 and FY 2026, well short of the \$2.9 billion in FY 2023.

Other tax revenues³ declined by \$400 million, or 13.6 percent in FY 2024 because estate tax collections fell by \$400 million. A tax law change raising the estate tax threshold to \$2 million from \$1 million was estimated to cost the state roughly \$130 million in FY 2024 and another \$80 million in FY 2025 (table below).

² [RETAILERS ASSOCIATION OF MASSACHUSETTS PREDICTS 1.5% INCREASE IN HOLIDAY SALES](#), November 20, 2024.

³ Other tax revenues consist of motor fuels, room occupancy, estates, cigarettes, alcohol, and deeds among others.

The \$400 million loss in estate tax revenues was triple the forecasted decline for FY 2024. With a further tax change driven decline of \$80 million projected in FY 2025, and the possibility that change of residency may have contributed to the size of the FY 2024 loss, it appears likely that estate tax revenues will experience low to no growth in the current year.



SURTAX REVENUE COLLECTIONS AND PROCESS

Published estimates put FY 2024 surtax revenues at \$2.2 billion, although that figure will likely increase upon final certification by the Department of Revenue. Through Q1 FY 2025, DOR estimates surtax revenue collections total \$399.2 million. Since the start of surtax collections in January 2023, withholding tax revenues account for approximately 25 percent with non-withholding making up the balance. Given these data, MTF estimates FY 2025 surtax revenues will increase to \$2.5 billion and to \$2.6 billion in FY 2026.

As we prepare to develop the FY 2026 budget, MTF recommends several changes to the process established to track and manage surtax revenues:

- The annual tax revenue benchmark should differentiate between surtax and non-surtax collections, and the surtax benchmark should reflect expected collections and not the surtax spending threshold, as was done in FY 2024 and FY 2025;
- Monthly revenue reports should estimate surtax collections for that month and year-to-date; and
- Lawmakers should create a transparent and timely process to allow for reasonable adjustments to the surtax spending threshold after its initial establishment as part of the consensus revenue process.

As we look ahead to the third full fiscal year of surtax revenue collections, each of these changes aims to ensure the ongoing reliability of revenue benchmarks, improve our ability to assess collection trends in real-time, and adjust to economic and revenue changes that occur after the establishment of the surtax revenue threshold used in the budget.

HEADWINDS ARE PERVASIVE, COULD POSE EXISTENTIAL RISK

Global economic, political, and military conflicts loomed over the Massachusetts economy before the November election. In 2024, inflation, migration, the impact of wars in Ukraine and the Middle East, and the possibility of conflicts emerging in other parts of the world all affected the global economy and Massachusetts.

Those factors present in 2024 remain, and the impact of the recent Presidential election adds further wrinkles to our economic outlook. Policy proposals from the Trump administration would have profound economic impacts. The extension and potential expansion of the Tax Cuts and Jobs Act (TCJA) of 2017 could boost state tax revenue collections in the short-term, but could also come at the expense of trillions added to the national debt and major cuts to domestic programs. Should the Administration follow through with aggressive tariff policies, they will drive up the costs of imported goods for both consumers and industrial supply chains. Add the potential for significant deportations of immigrants, and the U.S. may have to cope with far tighter labor markets causing more inflation. Taken together, inflation and the cost of living could increase sufficiently, such that current high interest rates are locked in for the next several years.

Major changes to federal domestic spending would also have immediate impacts on state operating budgets and planned capital spending. Investments in infrastructure, including green energy and climate tech sectors, and key economic sectors, such as the biopharma/life sciences, health care, and higher education are pivotal to the Massachusetts economy.