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State general fund revenue growth slowed in last fiscal year

Introduction: Pennsylvania's 2023 fiscal year began on July 1, 2022, and ended June 30, 2023. The Pennsylvania Department of Revenue recently released the general fund revenue collections for that fiscal year. The total of $44.92 billion was 6.7 percent short of the previous fiscal year's mark of $48.13 billion. But the previous year's total was supplemented by a federal stimulus payment of $3.84 billion (8 percent of total) in November 2021. This *Brief* will look at general fund revenue data from fiscal 2010 through fiscal 2023. All data referenced in this *Policy Brief* are taken from the Pennsylvania Department of Revenue.

Growth to general fund revenues

Without the federal stimulus money, fiscal 2022's total general fund revenues came in at $44.92 billion. Thus, fiscal 2023's total was $623.4 million or 1.4 percent higher than the previous year when federal stimulus is excluded. This is not a torrid pace but more along the lines of pre-pandemic average annual year-over-year growth, which, from fiscal 2010 through fiscal 2019, ranged from -0.55 percent (fiscal 2010 to fiscal 2011, the tail end of a deep recession) to 9.15 percent (fiscal 2017 to fiscal 2018). The average growth rate from fiscal 2010 to fiscal 2019 was 2.66 percent. The growth rate from fiscal 2022 to fiscal 2023 was slightly slower than average.

The three largest components of fiscal 2023's general fund revenues are personal income tax (39 percent of the total), sales and use-tax (31 percent) and the corporate net income tax (14 percent). The remaining 16 percent comes from minor tax collections on lesser items such as gaming, realty transfers, bank shares, utility property, cigarettes and alcohol. Also included are non-tax revenue such as liquor store profits, licenses and fees along with fines, penalties and interest.

General fund revenue components

From fiscal 2022 to fiscal 2023 personal income tax collections fell from $18.13 billion to $17.63 billion—a decline of 2.75 percent. Except for the pandemic year of fiscal 2020, it was the only year-to-year drop in the period covered by this *Brief*. This may be more a case of collections in fiscal 2022 being pumped up as inflation soared following the federal government injecting billions in stimulus money into the state's economy following the pandemic driving up not only the prices of goods and services but the price of labor (wages) as well. Fiscal 2023's collections are the second highest in the 13-year period and 25.1 percent higher than pre-pandemic fiscal 2019's total of just $14.10 billion in personal income tax collections.

With the Federal Reserve Bank continuing its fight against inflation by raising interest rates and slowing the pace of economic activity, it is possible fiscal 2024's collections could also be lower than last year. To have back-to-back reductions in personal income tax collections would be unusual. Note that changes in collections from fiscal 2010 to fiscal 2019 were all positive, despite the recession of 2009, which, according to the U.S. Bureau of Economic Analysis, spanned 3rd quarter 2008 and officially lasted through 3rd quarter 2009, although the effects lingered.

The 0.10 percent growth in this year's sales and use-tax collections is the lowest gain over the study period, except for the small reduction (2.5 percent) in fiscal 2020. However, the $14.02 billion in revenue is the highest, just ahead of fiscal 2022's $14.01 billion. With the stimulus and inflation-fueled growth of collections in fiscal 2021 and fiscal 2022, tax revenues rose by 18.7 percent and 9.2 percent, respectively; a slowdown may have been inevitable. Pre-pandemic growth averaged 3.7 percent from fiscal 2010 until fiscal 2019.

Again, given the actions of the Federal Reserve to control inflation through monetary tightening, it's likely the growth in collection of sales and use-tax revenue this year will also be below the pre-pandemic average.

The final category examined is the corporate net income tax (CNIT). As discussed in *Policy Brief Vol. 22, No. 31*, Act 53 of 2022 will cut Pennsylvania's CNIT by five percentage points over nine years. A new legislative proposal in 2023 that was discussed in *Policy Brief, Vol. 23, No. 23,* would expedite those cuts to reach 4.99 percent in 2026 instead of 2031. As of this writing, it hasn't passed.

In January 2023, the first cut of one percentage point was realized, dropping the rate to 8.99 percent. The revenue total for the first six months of calendar 2023 with the new rate was $527.7 million higher (17.9 percent) than it was for the first six months of calendar 2022. While this time frame is too short to reach a firm conclusion about the full-year impact, it is clear the cut to the CNIT thus far has not resulted in a drop in revenue. Much will depend on how the economy performs during the second half of 2023.

For fiscal 2023, the CNIT garnered $6.14 billion, the highest total in the last 10 years and 15.4 percent greater than the previous high in fiscal 2022 ($5.32 billion). From fiscal 2013 through fiscal 2019, CNIT collections ranged from $2.42 billion to $3.40 billion. Corporate net income has obviously been much stronger the last two years than in years before the pandemic despite lower job counts in 2022 than in 2019.

Conclusion

The influx of federal stimulus money in the wake of the pandemic boosted general fund revenue totals in fiscal 2021 and 2022 and promoted even more government spending. But the state will not be receiving any more pandemic stimulus money. While the state hasn't spent it all yet, that deadline is looming. Going forward, the commonwealth must live within its means.

Fiscal 2023's total general fund revenues of $44.92 billion are $10 billion, or 29 percent, greater than pre-pandemic fiscal 2019. Inflation remains a factor in the national and state economies and is still being felt, most likely with the CNIT collection, which is up 80.8 percent since fiscal 2019 and 15.4 percent over fiscal 2022.

Notwithstanding significantly lower job counts in 2021 and 2022 than in 2019, the personal income tax and sales taxes are up 25 and 26 percent, respectively, since pre-pandemic fiscal 2019. However, currently they are down or flat over fiscal 2022. Perhaps this is an indication that the inflationary-fighting tactics of the Federal Reserve are taking hold as can be seen in recent consumer price numbers, or perhaps some businesses are preparing for an anticipated economic downturn (see *Policy Brief, Vol. 23, No. 10*).

The reduction of the CNIT from 9.99 percent to 8.99 percent is a good start. But more needs to be done to make the commonwealth more economically competitive with faster growing states. Implementing Right-to-Work, abolishing the right of transit and teacher unions to strike and eliminating the prevailing wage law will go a long way in reducing the cost of government and reduce the reliance on such high tax collections.

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