

Virginia Budgeting, Past, Present, and Future -- A Dickensian Perspective?

*Presentation to VACO's Finance Committee
August 15, 2019*



Joe Flores
Deputy Secretary of Finance
Commonwealth of Virginia
www.finance.virginia.gov

Outline

Look Back at the 2019 Session and Review Recent Tax Policy Changes

What's Keeping Us Up At Night? Current and Emerging Issues

Fall Budget Development

Concluding Thoughts

Going into the 2019 Session...

- **Heightened interest in tax policy**
 - Conformity to federal Tax Cuts and Jobs Act (TCJA)
 - Possible tax policy changes
- **Supplemental budget issues would need to be addressed**
 - Mandatory spending items
 - Clean up issues from the 2018 Session
- **Lingering tensions from 2018 Session**
- **Politics would filter into policy decisions – it's an election year!**

The TCJA Was Projected to Add Almost \$600 million In New General Fund Revenue (and growing) Each Year

Estimated Virginia Revenue Impact of the TCJA Fiscal Years 2019 to 2024 (Includes Residents and Nonresidents)

	(\$Millions)					
By Source	2019	2020	2021	2022	2023	2024
Individual Provisions	532.1	443.8	466.7	492.5	520.0	546.1
Business Provisions	29.4	114.6	181.5	300.3	417.2	398.2
International Provisions	32.6	52.7	5.5	5.8	6.0	6.3
Total, All Provisions	594.2	611.1	653.7	798.7	943.2	950.6

	(\$Millions)						
By Provisions	2019	2020	2021	2022	2023	2024	
Temporary Provisions (Expiring after 2025)	517.3	433.6	455.7	480.4	506.8	532.5	← One-time
Permanent Provisions	76.9	177.5	198.0	318.3	436.4	418.1	← Ongoing
Total, All Provisions	594.2	611.1	653.7	798.7	943.2	950.6	

- Most of the individual provisions are temporary and expire after 2025; the only substantial individual provision that is permanent is related to alternative inflation measures.
- Due to the likely timing of Virginia's conformity to the federal provisions, the full impact for Taxable Year 2018 is recognized in fiscal year 2019.
- Nonresidents account for approximately 11% of revenues.

Business leaders and economists optimistic about Commonwealth's revenue outlook



Strong general fund revenue growth coupled with the implications of conforming to the TCJA, resulted in \$2.2 billion in additional resources for policymakers to allocate during the 2018-20 biennium.



More than half of the new revenues -- \$1.2 billion -- was expected as a result of conforming to federal tax policy changes; typically conformity is not controversial.



Conformity resulted in more revenue to the Commonwealth as the federal government placed limits on itemized deductions and doubled the standard deduction at the federal level.

- This latter change provided an incentive for Virginia taxpayers to take the standard deduction (instead of itemizing), resulting in higher state tax obligations and additional revenue to Virginia.

Large Surplus' Are Unusual During “Off” Years

The Governor and General Assembly took different approaches when deciding how to allocate new general fund revenue.

	Governor's Proposed Budget FY 2018-20 Biennium
New spending*	\$2,446.0 million
New savings	(334.1) million
Net new spending	\$2,111.9 million
Tax relief	\$243.5 million
* Includes funds proposed for deposit to the Revenue Reserve and Revenue Stabilization Funds.	

Governor's Plan Balanced Spending & Saving Proposals

Set aside funds for a rainy day (\$1.1 billion GF)

Addressed current obligations and strategic investments (\$1.1 billion GF)

- Fully fund health and long-term care services for Medicaid enrollees
- Strengthen Virginia's educational system (i.e., free up resources for school construction)
- Invest in broadband and workforce development
- Maintaining our commitment to economic development
- Expand access to mental health services and housing
- Improve infrastructure with investments in transportation, water quality, and clean energy
- Enhance school safety, public safety, and election security
- Increase employee compensation and benefits

Provided limited tax relief by making the Earned Income Tax Credit refundable and raising threshold for businesses subject to the Accelerated Sales Tax (\$243.5 million GF)

General Assembly Focused More on Tax Relief

- The General Assembly funded many of the Governor’s priorities but at lesser amounts.
 - Some initiatives were rejected (i.e., making EITC refundable and deposit to Transportation Infrastructure Bank) while others were significantly reduced (i.e., funding for broadband and stormwater local assistance).
- General Assembly added resources to keep tuition flat and provide incentives for economic development (i.e., Micron).

	Governor’s Proposed Budget FY 2018-20 Biennium	FINAL Approved Budget FY 2018-20 Biennium
New spending*	\$2,446.0 million	\$2,124.6 million
New savings	(334.1) million	(566.7) million
Net new spending	\$2,111.9 million	\$1,557.9 million
Tax relief	\$243.5 million	\$1,003.2 million

* Includes funds proposed for deposit to the Revenue Reserve and Revenue Stabilization Funds.

A Majority of Anticipated General Fund Revenue from the TCJA will be Returned to Taxpayers or Not Collected

Of the \$1.2 billion in general fund revenues expected from conformity during the 2018-20 biennium, \$976 million was earmarked for tax relief.

The balance of \$229 million will remain in the general fund during the 2018-20 biennium and available in future years.

(General fund dollars in millions)

Description	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024
Anticipated General Fund Revenue from the TCJA	\$ 594.2	\$ 611.1	\$ 653.7	\$ 798.7	\$ 943.2	\$ 950.6
Less: Tax Relief, SB 1372 Impact	(\$31.7)	(\$331.2)	(\$228.3)	(\$233.0)	(\$238.7)	(\$243.7)
Less: Revenues to be transferred to Taxpayer Relief Fund	(\$500.5)	(\$112.6)	(\$238.5)	(\$259.5)	(\$281.3)	(\$302.4)
Balance Remaining in the General Fund	\$ 62.1	\$ 167.3	\$ 187.0	\$ 306.2	\$ 423.2	\$ 404.5

Tax Policy Changes from SB1372/HB2529

SB1372/HB 2529 provided tax relief for taxpayers by:

- Providing a one-time refund up to \$110 for individuals or \$220 for married couples from revenues generated in TY 2018.
- Deconforming from the SALT limitation (i.e., allowing taxpayers to deduct local real and personal property taxes without regard to the federal \$10,000 limitation) and increasing the standard deduction by 50% to \$4,500/\$9,000 for individuals/married couples.

Smaller ongoing relief will be provided to businesses.

- Allows a deduction for 20 percent of business interest that is disallowed as a deduction for federal income tax purposes for 2018 and after
- Expands existing Subpart F subtraction from corporation income tax so that it also applies to the global intangible low-taxed income (GILTI) of corporations for 2018 and after

Deconforming from the Pease Limitation that was suspended under the TCJA.

- This change continues to limit the amount of itemized deductions claimed by higher income taxpayers.

What's Keeping Us Up at Night?

Current Issues and Concerns

- **Perception that the Commonwealth is awash in revenue.**
 - We finished FY 2019 with a large surplus – almost \$800 million.
 - But most of the extra revenue was anticipated.
 - TCJA revenues
 - Nonwithholding (i.e., estimated tax payments)
- **Will general fund revenue growth be enough to fund current obligations?**
 - Revenues from withholding and sales taxes appear to be slowing.
 - Revenue growth of 3 to 4 percent may generate \$1.5 billion for the 2020-22 biennium.
 - How much will it cost to fully-fund the Medicaid forecast or Rebenchmark the Standards of Quality?
- **We're now in the longest economic expansion in history.**
 - Can it continue?
 - Warning signs have started to flash.
 - The stock market is on a roller coaster ride.
- **Will the federal government be in a position to help states if the economy slows down?**
 - The federal debt exceeded \$22 trillion this year.
 - Will the federal government even want to help?

Other considerations

- **What budget priorities and other high profile issues are bubbling up?**
 - Rising cost of tuition
 - Affordability of health care
 - Rural broadband
 - State and local taxes
 - Census at state mental health facilities
 - Final implementation of STEP-Virginia
 - Funding for school counselors
 - Water quality and coastal resiliency
 - Early childhood education
 - Salaries for teachers, state employees, and state-supported locals
- **Are We Paying Enough Attention to Infrastructure Issues?**
 - Workforce development
 - Roads and bridges
 - STEM education
- **Who will control the House of Delegates and Senate?**
 - Retirements (and possible defeats) mean new faces in important positions

Fall Budget Development

Official Budget Development Process

- **Capital budget requests sent out in June, base budgets are being reviewed by DPB, and official guidance to agencies will be issued later this month.**
 - Those requests will be reviewed in September and October and tentative decisions will begin to be made in late October and early November
 - Meeting will be held with the Joint Advisory Board of Economists (JABE) in October and the Governor's Advisory Council on Revenue Estimates (GACRE) in late November after which the Tax Department will finalize its revenue estimates.
- **Governor's budget(s) will be unveiled on December 17, 2019.**

Unofficial Budget Development Began Months Ago

- **Secretary and staff have been making site visits since late spring**
- **We've been monitoring executive workgroups as well as legislative committees**
 - Temporary Detention Order (TDO) Workgroup
 - SJ 47 (Deeds Commission)
 - Transportation Workgroup
 - Workload Impact of Body-worn Cameras
- **We've been meeting with advocates and lobbyists to understand their concerns**
- **We've convened two-hour long budget sessions with four agencies to better understand needs outside more hectic fall development**
- **We have a preliminary picture of revenues and expenditures**

Concluding Thoughts

- **There are many unknowns heading into fall budget development**
 - How much revenue is available?
 - Are revenues sufficient to fund our obligations?
 - How much will be left over for initiatives from the Governor or General Assembly?
- **Who will control the House of Delegates and the Senate in January?**
- **Will the US economy continue to expand or are we headed for a slowdown?**
- **How willing (or able) is the federal government to help?**

Contact information:

K. Joseph Flores
Deputy Secretary of Finance
804.692.2575
joe.flores@governor.virginia.gov