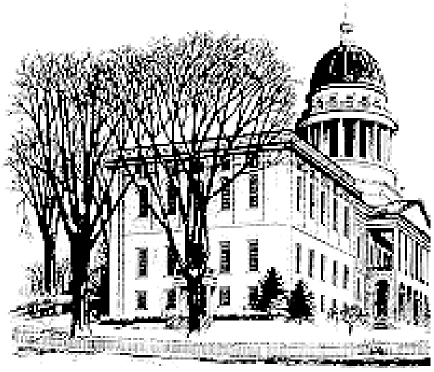

STATE OF MAINE
REVENUE FORECASTING COMMITTEE

March 1, 2022

TO: Governor Janet T. Mills
Members, 130th Legislature

FROM: Christopher Nolan, Chair
Revenue Forecasting Committee

RE: Revenue Forecast Committee March 1, 2022 Report

The Revenue Forecasting Committee (RFC) has concluded its update of the current revenue forecast to comply with its statutory reporting date of March 1st, to incorporate the new economic forecast released by the Consensus Economic Forecasting Commission (CEFC) on February 1, 2022 and to provide a forecast that reflects revenue performance through the first seven months of FY22. Tables showing the changes made to all the funds forecasted by the committee and a detailed presentation that includes the key assumptions made in developing the forecast have been posted to the RFC's web page and are available here. A more complete report will be added to the web page later this week.

General Fund Summary

	FY21 Actual	FY22	FY23	FY24	FY25
Current Forecast	$4,520,591,145	$4,622,327,266	$4,704,460,506	$4,886,311,120	$5,048,378,090
Annual % Growth	13.9%	2.3%	1.8%	3.9%	3.3%
Net Increase (Decrease)	$0	$234,855,224	$176,839,781	$162,631,910	$198,124,938
Revised Forecast	$4,520,591,145	$4,857,182,490	$4,881,300,287	$5,048,943,030	$5,246,503,028
Annual % Growth	13.9%	7.4%	0.5%	3.4%	3.9%

In its March 2022 update, the RFC has revised General Fund revenue estimates upward by $234.9 million for FY22 and by $176.8 million for FY23 for a total increase of $411.7 million (4.4%) for the 2022-2023 biennium. The forecasted rate of year-over-year growth for General Fund revenue for FY22 is 7.4% and for FY23 is 0.5%. The forecast for FY24 General Fund revenue is revised upward by $162.6 million and for FY25 by $198.1 million for a total increase of $360.8 million (3.6%) for the 2024-2025 biennium. As discussed in more detail below, these General Fund revenue changes are largely the result of positive adjustments to the individual and corporate income tax and the sales tax lines.

The RFC has revised Highway Fund revenue estimates upward by $1.4 million for FY22 and by $0.8 million for FY23 for a total increase of $2.2 million (0.3%) for the 2022-2023 biennium. The forecasted rate of year-over-year growth for Highway Fund revenue for FY22 is 0.7% and for FY23 is 0.9%. The forecast for FY24 and FY 25 Highway Fund revenue is revised upward by $0.8 million each year for a total increase of $1.6 million (0.2%) for the 2024-2025 biennium. The Highway Fund revenue changes are largely the result of increases in the motor vehicle registration and fees and other highway fund revenue lines, while net motor fuels revenue remains unchanged with decreases in estimates for gas tax revenue offset by increases in estimates for special fuels tax revenue.

Changes to the General Fund individual income tax are primarily the result of revenue performance during tax year 2021 indicating that tax year 2021 grew by more than previously forecasted, and more optimistic assumptions of wage and salary growth over the remainder of the forecast period. The February CEFC forecast assumes that wages and salaries will increase 7.7% during CY21, 6.5% for the CY22, 5.5% for CY23, 5.0% for CY24, and 4.0% in CY25. The wages and salaries forecast results in an increase in forecasted individual income tax liability of $41.7 million in tax year 2021, $75 million in tax year 2022, $89 million in tax year 2023, and approximately $95 million in tax years 2024 and 2025. Stronger growth in capital gains realizations increases 2021 tax liability by $33 million but has limited impact relative to the December forecast after 2021 as projected decreases in capital gains realizations eventually reduces tax liability from capital gains to levels consistent with tax periods leading up to the pandemic. The revenue increase in FY22 is larger than the later years partly because of timing in receipts. The new forecast continues to assume that taxpayers shifted income into tax year 2021 and out of future tax years in reaction to discussions throughout 2021 of potential tax increases at the federal level. This behavior by high-income taxpayers will boost FY22 revenues at the expense of future fiscal years.

The corporate income tax line has been growing at unusually high year-over-year rates for the last 18 months. Last fiscal year corporate income tax receipts increased by 31.5 percent, and through the first seven months of this fiscal year they have increased by 56.6 percent. Other states with a corporate income tax structure like ours and the federal government have experienced similar growth rates. In this revenue forecast the RFC increased the corporate income tax forecast by $75.0 million in FY22, $62.0 million in FY23, and by $112.3 million in the FY24/25 biennium. Until more detailed information provided on income tax returns is received and analyzed, we can only postulate why corporate income tax revenues have been so high. Three possible explanations that have been discussed are (1) corporate profits, particularly for larger companies, are much stronger than previously estimated, (2) the unique aspects of the pandemic economy have interacted with key provisions of the 2017 federal tax reform act (TCJA) to increase revenue, and (3) corporations in reaction to tax increases discussed in Congress during 2021 shifted income into 2021 to avoid potential future tax increases.

The annual positive adjustments to the General Fund sales and use tax forecast are relatively minor compared to the December revenue forecast and reflect a positive variance of $12.1 million through January and the new economic forecast from the CEFC. While the sales tax forecast assumes year-over-year growth will slow starting in calendar year 2022, the CEFC's economic forecast estimates Maine households will experience income growth capable of sustaining the current level of spending on taxable goods and services. After FY22, annual sales tax growth is forecasted to be between 3.0 and 3.5 percent, reflecting higher inflation and a gradual shift back to in-person non-taxable services as consumers adjust their mix of spending to where it was pre-pandemic.

The significant revenue increases estimated in this forecast reflect Maine's revenue collection experience through the first seven months of FY22, preliminary data on February revenue, and the latest thinking by economic forecasters on the trajectory of the U.S. and Maine economies over the next four years. However, even with the easing of the Omicron variant of the COVID-19 pandemic, with the possibility of new variants and escalating international events, uncertainty has become the norm. Most of the short-term risk to the current revenue forecast is positive, while ongoing issues (inflation, stock and real estate market valuations, supply chain and labor force constraints etc.) facing the economy make the FY23-25 portions of the forecast volatile and susceptible to significant downside risk. The time between this forecast and the next one scheduled for the fall of CY22 provides time for many of the global challenges to be resolved or could result in additional uncertainty, but either way means the long-term part of this forecast will remain uncertain until at least late this year.

cc: Members, Revenue Forecasting Committee
Members, Consensus Economic Forecasting Commission
Jeremy Kennedy, Chief of Staff, Governor's Office
Kirsten Figueroa, Commissioner, DAFS
Clerk of the House
Secretary of the Senate
Suzanne Gresser, Executive Director, Legislative Council