INITIAL REVENUE ESTIMATE

FY 2023-24

INDEPENDENT FISCAL OFFICE

MAY 2023

Independent Fiscal Office

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INDEPENDENT FISCAL OFFICE

May 24, 2023

The Honorable Members of the Pennsylvania General Assembly:

The Independent Fiscal Office submits this initial revenue estimate in accordance with Sections 604-B (a)(1) and 605-B (a) of the Administrative Code of 1929. This report provides revenue estimates for fiscal year (FY) 2022-23 and FY 2023-24. Pursuant to statute, the office will release a final estimate on June 20, 2023.

This report contains estimates for unrestricted General Fund and Motor License Fund revenues that may be considered for appropriation in the General Appropriations Act. Estimates for the Lottery Fund represent net revenues after the deduction of certain expenses. Federal funds subject to General Fund appropriation are stated separately. A separate report that describes the methodologies used to produce the various revenue estimates included in this report will be posted to the office website after the final estimate is released.

Questions or comments regarding the contents of this report are welcome and can be submitted to contact@ifo.state.pa.us.

Sincerely,

Matthew J. Knittel
Director

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Economic Outlook

This section presents the economic forecast used for the initial revenue estimate. The forecast does not assume a recession occurs in calendar year (CY) 2023 or 2024. However, many analysts believe there is significant potential that the forecast could deteriorate rapidly due to high interest rates, an expected contraction of credit and lending, the resumption of student loan repayments, a potential debt ceiling impasse and the end of funds still flowing from certain stimulus programs (e.g., employee retention credit).

U.S. Economic Forecasts

Table 1.1 displays the most recent U.S. economic forecast published by IHS Markit, Wells Fargo and PNC Bank. Across the three forecasts:

- Real GDP (real gross domestic product, excludes inflation) increases from 1.2% to 1.3% (CY 2023) and from -0.4% to 0.9% (CY 2024).
- The Consumer Price Index (CPI-U) increases from 3.9% to 4.2% (CY 2023) and 1.6% to 2.5% (CY 2024). The latest national data show clear deceleration of consumer inflation: 6.4% (January), 6.0% (February), 5.0% (March) and 4.9% (April).
- U.S. Corporate Profits expand or contract depending on the forecast and year. As discussed in a later subsection, corporate profit margins are contracting from record levels in CY 2022. For that year, corporate non-financial domestic profits as a share of GDP was 8.0%, the highest share since 1968. (Note: PNC does not forecast corporate profits, so the February forecast from the Congressional Budget Office (CBO) is shown in the table.)

Table 1.1
U.S. Macroeconomic Forecasts

	2020	2021	2022	2023	2024
Real GDP					
IHS Markit	-2.8%	5.9%	2.1%	1.2%	0.9%
Wells Fargo	-2.8%	5.9%	2.1%	1.3%	0.3%
PNC Bank	-2.8%	5.9%	2.1%	1.2%	-0.4%
Consumer Price Index					
IHS Markit	1.3%	4.7%	8.0%	4.2%	2.5%
Wells Fargo	1.3%	4.7%	8.0%	3.9%	2.5%
PNC Bank	1.3%	4.7%	8.0%	4.2%	1.6%
U.S. Corporate Profits					
IHS Markit (domestic only)	-3.8%	29.0%	8.4%	6.3%	-3.4%
Wells Fargo (all)	-5.9%	22.6%	6.6%	-5.0%	2.1%
CBO (domestic only)	-3.8%	29.0%	8.4%	-15.8%	-0.6%

Note: PNC forecast from March and CBO from February. Other forecasts published in May.

The three U.S. forecasts project a modest jobs contraction in CY 2024 (not shown), but only one projects a contraction in real GDP. In the latest Wall Street Journal Survey (April), 61% of economists surveyed project that a recession will occur at some point during the next 12 months.

Pennsylvania Economic Forecasts

Table 1.2 displays the IFO economic forecast used for this initial revenue estimate and the most recent forecast published by IHS Markit (released in May). The forecasts project that:

- Real GDP (real gross domestic product, excludes inflation) increases by 1.6% (CY 2023) and 1.2% (CY 2024). The IHS Markit forecast projects similar real growth.
- The Philadelphia CPI-U increases by 4.7% (average for CY 2023) and 3.2% (CY 2024). The IHS Markit forecast projects lower inflation in CY 2024.
- Wages and Salaries paid increases by 5.3% (CY 2023) and 4.1% (CY 2024) (excludes compensation paid to independent contractors). The IHS Markit forecast projects stronger wage growth for CY 2023.
- Payroll Employment expands by 80,000 (CY 2023, annual average) and 24,000 (CY 2024) net jobs. The IHS Markit forecast projects higher job gains for the current year, but a modest contraction next year.

Table 1.2
Pennsylvania Forecasts: Annual Growth or Change

	IFO			IHS Markit		
	2022	2023	2024	2022	2023	2024
Real GDP	2.1%	1.6%	1.2%	2.1%	1.4%	1.0%
Philadelphia CPI-U	7.9%	4.7%	3.2%	7.9%	4.5%	2.5%
Wages-Salaries	9.3%	5.3%	4.1%	9.3%	6.8%	4.2%
Net Payroll Jobs (000s)	227	80	24	231	126	-7

Note: Payroll jobs exclude self-employed and independent contractors.
Source: U.S. Bureau of Economic Analysis and U.S. Bureau of Labor Statistics.

Table 1.3 displays the latest quarterly data for the state economy and the year-over-year (YOY) growth rate or change. (An exception is Real GDP, which is the quarterly annualized growth rate.) The data show the following recent trends:

- Real GDP increased by 3.2% in 2022 Q4. Real GDP data are published with a considerable lag and the latest published data are for 2022 Q4. Values shown are preliminary and could be revised substantially.
- Wage and salary growth decelerated notably in the first half of CY 2023 based on year-to-date collections, but the latest data continue to show solid gains. The deceleration reflects a partial reversion to pre-pandemic growth rates (roughly 4%), with extra strength due to a tight labor market and record low unemployment.

- For 2022 Q2, the Philadelphia CPI-U grew at the fastest rate since 1981. Since then, inflation has decelerated and the latest data show 4.7% YOY growth (April 2023). The economic forecast projects further deceleration to 3.8% by December 2023.
- Data for 2023 Q2 (April only) show that payroll jobs increased by 147,000 (preliminary) from the prior year. The unemployment rate was 4.1% and the labor force participation rate was 62.0%. For April 2019, the unemployment rate was 4.4% and the labor force participation rate was 63.0%.

Table 1.3
Recent Pennsylvania Economic Growth Rates or Change

	2022.1	2022.2	2022.3	2022.4	2023.1	2023.2
Real GDP	-1.1%	-0.9%	3.2%	3.2%	--	--
Wages and Salaries	10.0%	9.5%	9.6%	8.1%	5.3%	5.1%
CPI-U - All Items	7.3%	8.6%	8.1%	7.1%	6.9%	4.7%
Unemployment Rate	4.4%	4.3%	4.3%	4.4%	4.3%	4.1%
Number Unemployed (000s)	285	279	279	282	280	268
Change Payroll Jobs (000s)	261	249	224	189	172	147
Labor Force Participation Rate	61.1%	61.6%	61.7%	61.7%	61.9%	62.0%

Note: All growth rates or changes are year-over-year except Real GDP, which is quarterly annualized. CPI-U for 2023 Q2 is for April only. Labor market data for 2023 Q2 based on April preliminary data only. Data are seasonally adjusted. 2023 Q1 and Q2 Wages and Salaries growth rate based on withholding revenues through May.
Source: U.S. Bureau of Economic Analysis and U.S. Bureau of Labor Statistics.

Pennsylvania Payroll Employment

Table 1.4. compares payroll jobs data from March 2023 to March 2019 (pre-pandemic). Total payroll jobs now exceed their pre-pandemic level by 52,000. Compared to March 2019, sector detail show that:

- The transportation and warehouse (+43,000), professional and technical services (e.g., legal, engineering, +37,000) and social assistance (+25,000) sectors recorded significant job gains. Subsector data (not shown) reveal strong gains for warehousing and storage (+35,700), couriers and messengers (+9,500) and computer system design and related (+9,500). The childcare subsector (included in social assistance) contracted by 2,800 payroll jobs (-5.8%).
- Despite a slow housing market, construction jobs growth continues and exceeds the pre-pandemic level by 7,400 payroll jobs (+3.0%).
- The accommodations-food service sector had the largest relative contraction (-4.5%).
- The nursing and residential care subsector (not shown, included with healthcare) contracted by 27,500 payroll jobs (-13.5%).
- The government sector contracted by 23,500 payroll jobs (-3.3%). Notable contractions occurred for the local government-municipal (excludes school districts, -11,000, -6.1%) and state government-education (i.e., public post-secondary institutions, -7,300, -11.7%) subsectors.

Table 1.4
Change in Payroll Jobs

	March Level (000s)		Number	Percent
	2019	2023	Change	Change
Total Payroll Employment	**6,010**	**6,061**	**52**	**0.9%**
Transportation and Warehouse	271	314	43	15.8
Professional and Technical	360	397	37	10.3
Social Assistance	231	256	25	10.8
Management of Companies	134	148	15	11.0
Finance and Real Estate	328	338	10	3.2
Construction	244	251	7	3.0
All Other (residual)	226	226	0	0.2
Retail and Wholesale Trade	814	813	-1	-0.1
Admin and Waste Management	305	303	-2	-0.7
Private Education	255	253	-3	-1.0
Other Services	259	252	-7	-2.8
Manufacturing	576	565	-11	-1.8
Healthcare	821	803	-19	-2.3
Accommodation-Food Service	468	447	-21	-4.5
All Government	719	695	-24	-3.3

Note: Data are not seasonally adjusted. Excludes self-employed.
Source: U.S. Bureau of Labor Statistics, State and Metro Area Employment.

COVID-19 Impact on Economic Growth and Tax Revenues

On May 11, 2023, the Biden administration declared an end to the COVID-19 public health emergency. During the emergency, numerous federal programs injected nearly $200 billion into the state economy, which had a dramatic impact on General Fund revenues. **Table 1.5** displays four-year cumulative growth rates for economic, financial and General Fund revenues for the most recent quarter or fiscal year compared to the value four years prior. (Economic and financial variables use data from March 2019 to March 2023 or 2019 Q1 to 2023 Q1. General Fund revenues use FY 2018-19 to FY 2022-23 and values for the latter year are estimates.)

During the four-year period, Pennsylvania real GDP expanded by roughly 3.0% (preliminary), consumer inflation increased by 18.8% (final) and nominal GDP (preliminary, includes inflation) expanded by 21.8%. Nominal GDP growth is often used to quantify the overall growth of the state economy and is used as a benchmark for other metrics to assess whether they outperformed economic growth. (That metric, and other metrics that expanded at the same general rate, appear in bold blue font in the table.) Based on that comparison, notable results are as follows:

- Total wages and salaries paid to all payroll workers (+20.4%) grew at roughly the same rate as the state economy.
- Due to federal stimulus, low interest rates and quantitative easing that occurred over most of the four-year period, asset values inflated substantially: the S&P 500 Index climbed 45.0% through

2023 Q1 (end of March) while the average Pennsylvania home value grew 44.5%. In general, high rates of inflation tend to disproportionately benefit asset owners.

- For CY 2022, U.S. non-financial corporate domestic profits reached the highest level (relative to GDP) since 1968. State-level profit metrics are not published, but over the four-year period, corporate net income tax (CNIT) collections expanded by 80%. (Note: this adds back an estimated -$200 million impact in FY 2022-23 due to the phase-in of the CNIT rate reduction.)
- Inheritance tax revenues (45.7%) outperformed economic growth, largely due to the inflation of assets such as stock holdings and homes.
- Personal income tax (PIT) - Other includes non-corporate business profits, capital gains, dividends, rent and taxable interest. Revenues from those income sources (37.5%) outperformed the overall state economy.
- Sales and use tax collections increased 26.2% over the four-year period. Prior to the pandemic, sales tax collections would generally underperform state economic growth barring an expansion of the tax base (e.g., taxation of internet sales). The overperformance is due to the infusion of federal stimulus monies, a shift from purchases of services to goods and the student loan repayment moratorium, which has entered its fourth year.
- Withholding tax revenues expanded by 21.2%, similar to wages and salaries paid and the overall state economy.

Table 1.5
Pandemic Impact on Revenues and Economics

Economics or Assets	2019 Q1	2023 Q1	Growth
Real GDP	$709.0	$730.3	3.0%
Philadelphia CPI-U	253.2	300.9	18.8
Nominal GDP	**$787.9**	**$960.0**	**21.8**
Wages-Salaries	**$351.2**	**$423.0**	**20.4**
S&P 500 Index	2,834	4,109	45.0
PA Home Value Index	226.7	327.5	44.5
FY Revenues	**2018-19**	**2022-23**	**Growth**
Corporate Net Income	$3.40	$6.12	80.0%
Inheritance	$1.05	$1.53	45.7
Personal Income Tax - Other	$3.65	$5.02	37.5
Sales and Use	$11.10	$14.01	26.2
Personal Income Tax - Withheld	**$10.44**	**$12.65**	**21.2**

Note: All dollar values in billions.

Sources: U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics, Federal Housing Finance Agency.

For the FY 2023-24 revenue estimate, a pertinent issue is whether the overperformance of certain revenue sources can be maintained and extended, or whether there will be partial reversion that reduces some portion of the overperformance. For corporate profits, most analysts expect corporate profit margins to contract (next subsection). If that occurs, then it is likely that stock market indices would remain subdued, which would also impact the consumer outlook and spending.

Corporate Net Income Tax and Corporate Profits

Table 1.6 displays CNIT collections for next fiscal year, the current fiscal year and the past three fiscal years. The second row controls for deposit shifts across years and a preliminary estimate for the net impact of the corporate rate reduction from 9.99% to 8.99% and tax base expansion effective January 1, 2023. The adjusted baseline shows robust growth for the current fiscal year (15.0%) and past two fiscal years. For FY 2023-24, the forecast assumes that corporate profits grow by 3.2% (CY 2023) and contract by 4.9% (CY 2024), and adjusted baseline revenues contract by 2.7% if recent policy changes are excluded.

The bottom portion of the table displays the most recent data from FactSet for S&P 500 net earnings, revenues and profits margins (i.e., profits divided by revenues or sales). Corporate net earnings or profits growth is the product of (1) profit margin growth and (2) revenue growth. For example, if profit margins increase from 10.0% to 10.5% (5.0% growth) and revenues grow by 3%, then net earnings would grow by 8.2%.[1] Data for the last five quarters show that YOY revenue growth slowed notably, while the average profit margin contracted. Both outcomes contributed to an earnings contraction for the latest two quarters. Unexpectedly, data for 2023 Q1 show that profit margins rebounded slightly, so the earnings contraction was modest. Most analysts project that corporate profit margins will come under increased pressure and cause a moderate earnings contraction this calendar year or next.

Table 1.6
Corporate Net Income Tax Revenues and Profits

Revenues ($ millions)	**19-20**	**20-21**	**21-22**	**22-23**	**23-24**
Actual Collections	$2,827	$4,424	$5,323	$5,922	$5,578
Less: Payment Shift or Tax Cut	-350	350	0	-200	-380
Adjusted Baseline	**3,177**	**4,074**	**5,323**	**6,122**	**5,958**
Growth Rate	-6.5%	28.2%	30.7%	15.0%	-2.7%
FactSet S&P 500	**2022.1**	**2022.2**	**2022.3**	**2022.4**	**2023.1**
Net Earnings (YOY growth)	9.4%	5.8%	2.5%	-4.9%	-2.2%
Total Revenues (YOY growth)	13.0%	12.7%	10.9%	5.4%	4.1%
Profit Margin (level)	12.3%	12.2%	11.9%	11.3%	11.5%

[1] The formula is (1 + 5.0%) * (1 + 3.0%) – 1.

A federal tax provision enacted in December 2017 is likely having a significant impact on CNIT revenues, especially final payments for TY 2022 that were remitted February to May 2023.[2] On a YOY basis, those CNIT final payments increased 27%. The provision requires corporations to amortize qualifying research and development expenditures over five years (and other research and development expenditures over 15 years) as opposed to immediate expensing or deduction. The provision is effective for TY 2022 and the U.S. Joint Committee on Taxation estimated that it would increase federal corporate income tax revenues by $24.2 billion in federal fiscal year (FFY) 2022 and $32.9 billion in FFY 2023. The national impact is difficult to translate to Pennsylvania because the provision has a disproportionate impact on certain firms and industries. The CNIT forecast assumes that the provision increased TY 2022 liability by $300 million and is reflected entirely in FY 2022-23 revenues. Because the provision effectively delays deductions, the positive liability impact declines over time and will fall by approximately 25% for TY 2023, while the positive revenue impact declines by roughly 50% in FY 2023-24. Hence, the phase-in of the policy change generates less additional tax revenue going forward from FY 2022-23 and that impact is included in the CNIT forecast.

Sales Tax and Consumer Debt

Table 1.7 displays YOY growth rates for sales and use tax (SUT) collections (2023 Q2 is a projection based on data through May 23rd), consumer debt and two financial metrics (home values and stock market) that impact consumer confidence, outlook and willingness to spend. Following two strong year years, SUT revenue growth has decelerated over the last two quarters and the forecast projects continued deceleration. Notable trends include the following (all growth rates are YOY):

- In total, motor vehicle SUT revenue growth was largely flat for the last three quarters. For those quarters, the Philadelphia CPI-U for used cars declined 6.6%, but increased by 6.1% for new cars (not shown).
- In CY 2022, Pennsylvania consumer auto loan balances grew 9% (not shown), but data for the most recent two quarters show 3.8% growth.
- Pennsylvania consumer credit card balances expanded by 11% to 13% during the past year, while U.S. balances increased by 15% to 16%.
- Pennsylvania average home values continue to increase, but the rate has decelerated rapidly.
- After four quarters of declines, S&P 500 Index growth was positive for 2023 Q2 (though May 19). However, given the projected contraction of corporate profit margins, tighter lending standards and a possible consumer pullback, it is unclear if those gains can be sustained.

[2] The provision was part of the Tax Cuts and Jobs Act, which also reduced the federal corporate income tax rate from 35% to 21%.

Table 1.7
Sales and Use Tax and Consumer Outlook

	2022.2	2022.3	2022.4	2023.1	2023.2
Sales and Use Tax					
Non-Motor Vehicle	3.9%	6.5%	6.9%	3.3%	2.3%
Motor Vehicle	-6.9	5.5	0.0	7.5	-6.0
Debt Burden Balance					
PA Auto Loans	5.0	0.6	2.8	4.8	--
PA Credit Cards	11.0	11.2	12.5	13.0	--
U.S. Credit Cards	14.4	15.6	15.4	16.0	15.5
Wealth Metrics					
PA Home Values	12.9	9.6	8.1	4.2	--
S&P 500 Index	-11.9	-16.8	-19.4	-9.3	10.8

Note: All growth rates are year-over-year.

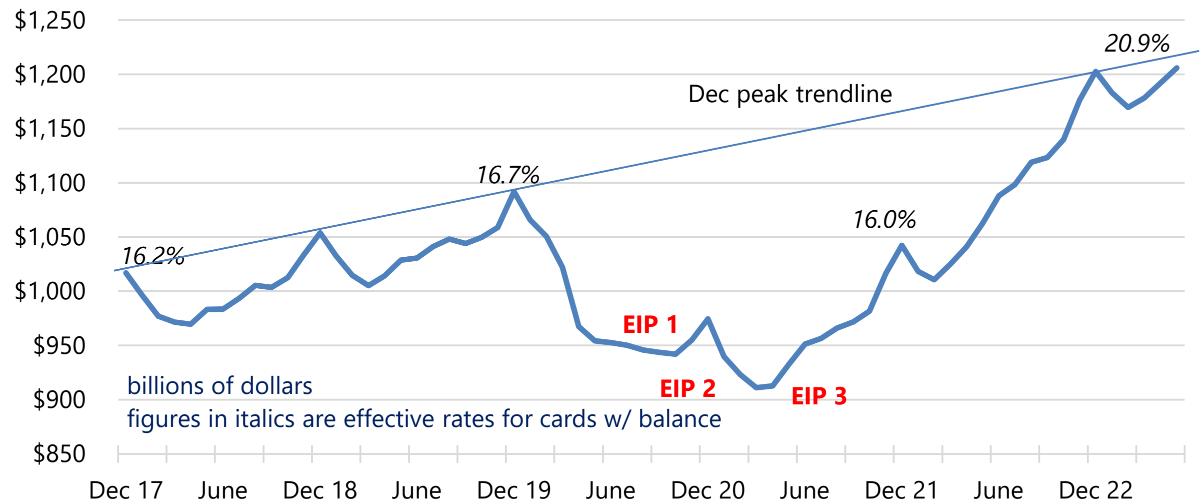
Source: PA indicators from New York Federal Reserve Board and FHFA. U.S. indicators from Federal Reserve Board and Wall Street Journal.

A relevant metric for SUT revenue growth is consumer debt, especially revolving debt like credit cards. Although the data from Table 1.7 show strong growth in credit card debt, most growth simply reflects a reversion to pre-pandemic debt levels. **Figure 1.1** displays trends in U.S. credit card balances. The peaks reflect December and temporary debt incurred due to holiday shopping. The blue trend line indicates that December debt balances increased by $38 billion per annum prior to the pandemic. Consumers used the three economic impact payments (EIPs) to reduce card balances. Since then, balances have reverted rapidly to pre-pandemic levels. The most recent data for April and May (preliminary) suggest that debt levels will cross the peak December trendline much earlier. Due to the end of various pandemic programs (e.g., SNAP emergency allotments, assumed end of student loan moratorium) and elevated inflation, the analysis assumes continued strong growth in credit card debt will constrain spending by lower-income consumers. For upper-income consumers, most researchers find that debt levels remain moderate and residual excess savings could fuel consumption through the end of the year. For example, a May 8 Economic Letter published by the Federal Reserve Board of San Francisco finds that "(d)espite a rapid drawdown of those funds (i.e., savings), estimates suggest a substantial stock of excess savings remains in the aggregate economy."[3]

A key assumption included in the SUT forecast is the resumption of student loan repayments. The moratorium was enacted in March 2020 and has been extended nine times. The analysis assumes that 1.83 million borrowers with an average payment of $350 per month ($7.7 billion per annum) will begin repayments this fall. If one-third of those repayments would have been spent on taxable goods or services, it would generate roughly $150 million in annual SUT revenues. This simple example disregards any second or third round spending impacts when original recipients respend some portion of monies received (i.e., multiplier effects).

[3] See https://www.frbsf.org/wp-content/uploads/sites/4/el2023-11.pdf.

Figure 1.1
U.S. Consumer Credit Card Debt



Note: Data not seasonally adjusted. EIP is economic impact payment.

Source: Federal Reserve Board.

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Initial Revenue Estimate

This section provides revised revenue estimates for FY 2022-23 and initial estimates for FY 2023-24 for the General Fund, Motor License Fund, Lottery Fund and federal funds subject to appropriation. The subsequent pages provide detail on the projected amounts and growth rates for those funds. For this initial revenue estimate, all projections are made on a "current law" basis and exclude any statutory changes or administrative actions proposed in the *2023-24 Executive Budget*.

The General Fund

The Independent Fiscal Office (IFO) released its official FY 2022-23 General Fund revenue estimate of $42.19 billion in June 2022. Since then, revenues primarily led by corporate net income tax (CNIT), non-motor vehicle sales and use tax (SUT) and Treasury, have dramatically outperformed expectations. Based on year-to-date revenue collections and projections for the remainder of the fiscal year, the revised estimate for FY 2022-23 is $44.71 billion, $2.52 billion above the IFO's official estimate. (See **Table 2.1**.) Significant revisions to the FY 2022-23 forecast include:

- CNIT collections are expected to exceed the IFO's official estimate by $1.03 billion. The revision is largely attributable to higher non-financial corporate domestic profits growth rates for CY 2022 and CY 2023 than were assumed in June 2022.
- The revised non-motor SUT estimate is $828 million higher than the IFO's official estimate, primarily due to: (1) strong retail sales from dining out, (2) higher prices (inflation) and (3) the extension of the student loan repayment moratorium.
- Treasury revenues continue to outperform expectations, as the General Fund balance remains high and interest rates increased more rapidly than expected. The revised Treasury estimate of $437 million is $421 million higher than the IFO's official estimate.
- Gross receipts tax collections are expected to exceed the IFO official estimate by $140 million, largely due to much higher than expected energy prices.
- The revised estimate for realty transfer tax is $142 million lower than the IFO's official estimate and represents a decline of 24.5% from the prior fiscal year. The revision is largely driven by unexpectedly weak home sales due to lower home affordability (resulting from high prices and interest rates) and limited housing supply.

For FY 2023-24, the initial estimate is $45.29 billion, an increase of $582 million (1.3%) from the current fiscal year. (See **Table 2.2**.)

Table 2.1
Adjustment to Revenue Estimate for FY 2022-23

	June 2022 Estimate		May 2023 Estimate		Dollar
	Amount	Growth	Amount	Growth	Change
Total General Fund	**$42,187**	**-12.4%**	**$44,710**	**-7.1%**	**$2,523**
Total Tax Revenue	**41,423**	**-4.8**	**43,571**	**0.2**	**2,148**
Total Corporation Taxes	**6,897**	**-5.8**	**8,024**	**9.7**	**1,127**
Corporate Net Income	4,892	-8.1	5,918	11.2	1,026
Gross Receipts	1,045	2.2	1,185	15.9	140
Utility Property	40	2.0	46	15.4	6
Insurance Premiums	475	-1.4	511	6.0	36
Financial Institutions	444	-1.1	365	-18.8	-79
Total Consumption Taxes	**14,673**	**-4.7**	**15,409**	**0.1**	**736**
Sales and Use	13,196	-5.2	14,013	0.7	817
Non-Motor	11,831	-2.0	12,659	4.8	828
Motor	1,365	-25.7	1,354	-26.3	-11
Cigarette	845	-3.3	774	-11.4	-71
Other Tobacco Products	164	9.6	153	2.1	-11
Malt Beverage	24	4.6	23	0.6	-1
Liquor	445	3.2	447	3.6	2
Total Other Taxes	**19,853**	**-4.5**	**20,138**	**-3.1**	**285**
Personal Income	17,366	-4.2	17,668	-2.5	302
Withholding	12,754	6.0	12,651	5.2	-103
Quarterly	2,484	-10.0	2,727	-1.2	243
Annual	2,129	-36.3	2,290	-31.4	161
Realty Transfer	781	-7.8	639	-24.5	-142
Inheritance	1,415	-8.7	1,527	-1.5	112
Gaming	348	13.2	363	17.7	15
Minor and Repealed	-58	-13.2	-60	-17.4	-2
Total Non-Tax Revenue	**764**	**-83.5**	**1,139**	**-75.5**	**375**
State Store Fund Transfers	185	0.0	185	0.0	0
Licenses and Fees	158	-6.0	158	-6.1	0
Treasury	16	-29.8	437	--	421
Escheats	258	-7.4	207	-25.5	-51
Other Miscellaneous	84	--	89	--	5
Fines, Penalties & Interest	63	-5.2	63	-5.7	0

Note: Figures in dollar millions. Detail may not sum to total. Growth rates based on unrounded amounts. Accelerated deposits included in Corporate Net Income.

Table 2.2
General Fund Revenue Estimate for FY 2023-24

	Estimated 2022-23		Projected 2023-24	
	Amount	Growth	Amount	Growth
Total General Fund	**$44,710**	**-7.1%**	**$45,292**	**1.3%**
Total Tax Revenue	**43,571**	**0.2**	**44,111**	**1.2**
Total Corporation Taxes	**8,024**	**9.7**	**7,730**	**-3.7**
Corporate Net Income	5,918	11.2	5,578	-5.8
Gross Receipts	1,185	15.9	1,200	1.3
Utility Property	46	15.4	46	1.1
Insurance Premiums	511	6.0	533	4.3
Financial Institutions	365	-18.8	374	2.5
Total Consumption Taxes	**15,409**	**0.1**	**15,470**	**0.4**
Sales and Use	14,013	0.7	14,093	0.6
Non-Motor	12,659	4.8	12,707	0.4
Motor	1,354	-26.3	1,385	2.3
Cigarette	774	-11.4	731	-5.6
Other Tobacco Products	153	2.1	160	4.9
Malt Beverage	23	0.6	23	1.8
Liquor	447	3.6	464	3.7
Total Other Taxes	**20,138**	**-3.1**	**20,911**	**3.8**
Personal Income	17,668	-2.5	18,404	4.2
Withholding	12,651	5.2	13,240	4.7
Quarterly	2,727	-1.2	2,920	7.1
Annual	2,290	-31.4	2,243	-2.1
Realty Transfer	639	-24.5	641	0.3
Inheritance	1,527	-1.5	1,533	0.4
Gaming	363	17.7	395	8.9
Minor and Repealed	-60	-17.4	-62	-3.5
Total Non-Tax Revenue	**1,139**	**-75.5**	**1,181**	**3.6**
State Store Fund Transfers	185	0.0	222	19.9
Licenses and Fees	158	-6.1	167	5.8
Treasury	437	--	445	1.9
Escheats	207	-25.5	217	4.6
Other Miscellaneous	89	--	66	-26.5
Fines, Penalties & Interest	63	-5.7	64	1.6

Note: Figures in dollar millions. Detail may not sum to total. Growth rates based on unrounded amounts. Accelerated deposits included in Corporate Net Income.

The text that follows provides a brief description of the factors that motivate trends across revenue sources for FY 2022-23 and FY 2023-24.

Corporate Net Income

The revised CNIT estimate for FY 2022-23 is $5.92 billion. The estimate reflects an increase of $1.03 billion from the IFO's official estimate and is $599 million higher than the prior fiscal year. The revision is driven by two factors. First, non-financial corporate domestic profits growth rates for CY 2022 and CY 2023 are considerably higher than assumed in June 2022. The revised (original) corporate profit growth rates are 10.4% (2.0%) for CY 2022 and 3.2% (-5.2%) for CY 2023. The revised growth rates are largely attributable to the ability of corporations to maintain historically high profit margins and push nearly all cost increases forward to final consumers. Second, the revenue impact from the Tax Cuts and Jobs Act of 2017 change from expensing to amortization for certain research and development expenses was larger than assumed (see discussion in prior section).

For FY 2023-24, the preliminary estimate is $5.58 billion, a decline of 5.8% from FY 2022-23. The forecast assumes that corporate profits will contract by 4.9% in CY 2024, which is consistent with most U.S. forecasts that project a profits contraction this year or next. Two other factors also contribute to the decline: (1) the continued phase-in of the corporate rate reduction and base expansion (-$345 million, Act 53 of 2022) and (2) the reduced positive revenue impact from changes enacted by the Tax Cuts and Jobs Act (-$160 million).

Sales and Use

The revised non-motor vehicle SUT estimate for FY 2022-23 is $12.66 billion. Strong retail sales as households spend down savings and incur debt, higher prices (inflation) and various federal policies (e.g., student loan moratorium and expansion of SNAP benefits, now ended) increased FY 2022-23 non-motor vehicle SUT collections more than anticipated. The revised estimate reflects an increase of $828 million from the IFO's official estimate and is 4.8% above revenues from the prior fiscal year.

In addition to the factors noted, a pandemic stimulus program likely had a large, positive (and unanticipated) impact on SUT revenues for FY 2022-23. The employee retention credit (ERC) allows firms with under 500 employees to claim a fully refundable credit (i.e., taxes need not be paid to qualify) up to $7,000 per quarter per employee ($28,000 per year) if (1) the firm asserts that sales declined by 20% or more during a single quarter in 2021 due to the pandemic or (2) the firm qualified as a "recovery start up business" in the third or fourth quarter of 2021. (A much smaller tax credit was also available for 2020.)

IRS processing through early March 2023 shows total ERC paid of $153 billion and a large backlog of claims. (A high proportion of claims has been deemed "very aggressive" or fraudulent by industry professionals.) If total credits paid are $190 billion and the Pennsylvania share is 4.2%, then total state ERC monies are roughly $8 billion, and the great majority would be received in FY 2022-23 by small business owners. The IFO had originally assumed $2 billion of refundable ERC credits would be received in this fiscal year. The additional $6 billion to business owners would have significant implications for spending by recipients, both in their role as small business owners and consumers, because the funds are not restricted to a specific business purpose and can flow to bottom line profits, which then flow to owners, partners and shareholders. Like other stimulus programs, most of these funds will not be available next fiscal year.

Another notable trend that impacted SUT revenues was the dramatic shift in consumer spending from services to durable goods (e.g., furniture, appliances, electronics) in response to the pandemic and related mitigation efforts during 2020 and 2021. However, recent national retail sales data show a reversion of this trend. For March (preliminary) and April (advance), YOY retail sales fell for electronics and appliance stores (-4.5%, -8.2%) and furniture and home furnishing stores (-2.8%, -8.8%), but continue to grow at food services and drinking places (generally taxable, +13.5%, +8.3%).

For motor vehicle SUT, the FY 2022-23 revised estimate is $1.35 billion, a decrease of $11 million from the IFO's official estimate. Motor vehicle sales appear to have recovered from the constraints imposed by shortages of semiconductor chips and other parts. According to J.D. Power, April sales of new vehicles increased by 5.9% from the prior year.[4] April sales data show that new vehicle inventory levels have improved dramatically and are 45% higher than April 2022.

For FY 2023-24, the forecast projects that non-motor vehicle revenues will increase by $48 million (0.4%), and motor vehicle revenues will increase by $32 million (2.3%). The estimate for non-motor vehicle collections assumes that inflation moderates, but still exceeds pre-COVID rates and that the student loan moratorium ends in fall 2023 (see discussion in prior section).

Personal Income

The revised personal income tax (PIT) estimate for FY 2022-23 is $17.67 billion, which is $302 million higher than the IFO's official estimate, a decrease of 2.3% over the prior fiscal year (after adjustments for one-time transfers). The upward revision is due entirely to non-withheld revenues (+$243 million in estimated and +$161 million in annual payments), which were particularly strong during the first six months of the fiscal year (generally attributable to tax years 2022 and 2021, respectively). Since then, payments have largely met expectations. The FY 2022-23 estimate for withholding is $103 million below the official estimate.

For FY 2023-24, the forecast projects $18.40 billion in PIT collections, an increase of 4.2%. Withholding is expected to increase by 4.2% (adjusting for transfers) and non-withheld revenues are projected to increase by 2.9%.

Gross Receipts

The revised gross receipts tax (GRT) estimate for FY 2022-23 is $1.18 billion. This estimate reflects an increase of $140 million from the IFO's official estimate and is 15.9% above revenues from the prior fiscal year. The increase is due to stronger than expected growth in electricity tax liability for TY 2022 compared to the prior year. Data from the U.S. Energy Information Administration (EIA) show that revenue from the sale of electricity in Pennsylvania increased by 20.9% in 2022, almost entirely due to price growth (19.4%). The growth rates for revenues and prices are the strongest rates since data have been published (2001). GRT revenues are projected to increase by 1.3% in FY 2023-24 as electricity tax liability reverts to a more moderate growth rate and revenues from the telecommunications sector continue their long-term decline.

[4] J.D. Power Automotive Forecast, April 2023. See: https://www.jdpower.com/business/press-releases/jd-power-lmc-automotive-forecast-april-2023.

Cigarette

The long-term trend decline in cigarette tax collections moderated during the pandemic when many employees moved to remote work and were able to smoke with fewer restrictions. For FY 2022-23, cigarette tax collections are expected to fall to $774 million, $71 million below the IFO's official estimate and an 11.4% decline from the prior year. This drop in revenues is more dramatic than prior years, likely the result of those same employees returning to the office.

For FY 2023-24, collections are projected to decline $43 million (-5.6%) similar to historical trends. Consistent with prior year estimates, collections are reduced by $115 million for debt service related to the Tobacco Settlement Bonds.

Realty Transfer

The revised realty transfer tax estimate for FY 2022-23 is $639 million, $142 million less than the IFO's official estimate and down 24.5% from the prior fiscal year. The revision is largely driven by unexpectedly weak home sales due to (1) rapid home price appreciation and rising interest rates (i.e., lower home affordability) and (2) limited housing stock due to a reluctance to sell for owners who locked into historically low mortgage rates in 2020 and 2021. For FY 2023-24, collections are impacted by a $20 million increase in the transfer to the Housing Affordability and Rehabilitation Enhancement Fund. After adjusting for the higher transfer, base collections are expected to increase 3.4%, as sales rebound slightly but housing prices remain largely flat.

Inheritance

The revised inheritance tax estimate for FY 2022-23 is $1.53 billion. This estimate reflects an increase of $112 million from the IFO's official estimate. Over the last two fiscal years, growth in inheritance tax collections has largely correlated with growth in the stock market. For FY 2022-23, that relationship diverged as collections (-1.5%) are projected to decline at a slower rate than the S&P 500 Index (-9.6%). This could result from the carryover of two trends from prior fiscal years: (1) stock market and asset value gains and (2) excess deaths resulting from COVID-19. Inheritance tax payments are generally due nine months after the date of death, so trends from the prior fiscal year likely impact FY 2022-23 collections. Collections are projected to be flat for FY 2023-24.

Other Revenue Sources

Other revenue sources that have a notable impact on General Fund revenue trends for FY 2022-23 and FY 2023-24 include:

- The revised gaming estimate for FY 2022-23 is $363 million, an increase of $55 million over the prior fiscal year due primarily to higher than expected collections for sports wagering and iGaming. For FY 2023-24, gaming revenues are expected to increase to $395 million.
- The revised FY 2022-23 Treasury estimate is $437 million, or $421 million higher than the IFO's official estimate. FY 2023-24 collections are projected to increase to $445 million, as short-term interest rates received on the balance plateau but remain elevated.

- The revised escheats estimate of $207 million is $51 million below the IFO's official estimate, due to higher than anticipated claims. For FY 2023-24, escheats collections are projected to increase to $217 million.
- The FY 2023-24 estimate assumes that $222 million will be available for transfer from the State Stores Fund to the General Fund.

The Motor License Fund

The Motor License Fund (MLF) includes various excise taxes levied on a per-gallon basis and revenue from licenses and registration fees. Based on actual year-to-date revenue collections and projections for the remainder of the fiscal year, the revised FY 2022-23 estimate is $2.97 billion, an increase of 3.1% from the prior year and $88 million above the IFO's official estimate.

Table 2.3
Motor License Fund Summary

	Estimated 2022-23		Projected 2023-24	
	Amount	**Growth**	**Amount**	**Growth**
Total Motor License Fund	**$2,972**	**3.1%**	**$3,133**	**5.4%**
Liquid Fuels Taxes	**1,763**	**0.9**	**1,787**	**1.3**
Oil Company Franchise	935	-1.5	946	1.1
Act 89 OCFT - Liquid Fuels	513	2.7	517	0.7
Act 89 OCFT - Fuels	143	-2.1	147	2.4
Other Liquid Fuels Taxes	172	13.3	178	3.7
Motor Licenses and Fees	**1,145**	**1.6**	**1,286**	**12.3**
Vehicle Registration & Titling	814	-1.8	935	14.8
Registration Other States - IRP	204	30.4	221	8.5
Operator's Licenses	64	-29.7	75	17.9
Other Licenses and Fees	63	24.6	55	-12.9
Other Motor Receipts	**64**	**554.5**	**60**	**-6.4**
Vehicle Fines Clearing Acct	2	64.5	2	15.0
Treasury	61	--	56	-7.9
Transportation	1	-37.5	2	25.0
General Services	0	-37.3	1	25.0

Note: Figures in dollar millions. Detail may not sum to total. Growth rates based on unrounded amounts.

For FY 2023-24, the MLF is projected to increase $161 million (5.4%) and is impacted by two factors:

- Increases for most fees levied under Title 75 (the Vehicle Code) are tied to the rate of inflation, with adjustments occurring in calendar years that end in an odd number. Therefore, the fee increases effective July 1, 2023, are determined based on the change in the CPI-U for the period that begins February 1, 2021, and ends January 31, 2023, or 14.3695%.

- The oil company franchise tax (OFT) rate is calculated annually based on the average wholesale price (AWP) of gasoline and diesel fuel in the prior calendar year. Beginning with CY 2017 and thereafter, the minimum AWP is $2.99 per gallon. For the 12-month period ending September 30, 2022, the Pennsylvania Department of Revenue determined the actual AWP to be $3.17 per gallon. Therefore, the AWP used to calculate the CY 2023 OFT rate was $3.17 per gallon. Effective January 1, 2023, the tax rates for gasoline and diesel were 61.1 and 78.5 cents per gallon, respectively. The FY 2023-24 estimates assume that the AWP falls below the $2.99 minimum for CY 2023 and the tax rates imposed on gasoline and diesel decline to 57.6 and 74.1 cents per gallon, respectively, effective January 1, 2024.

The Lottery Fund

Table 2.4 displays historical sales and the average annual growth rate by category of Lottery game for FY 2015-16 to FY 2019-20, as well as actual collections for the last three fiscal years (FY 2020-21 through FY 2022-23 (April to June are estimates)). After an average growth of 2.0% per annum for the four-year period prior to the pandemic (excludes new iLottery game), sales in all categories substantially increased in FY 2020-21 due to various pandemic-relief programs such as direct payments to individuals and expanded unemployment compensation, then declined in FY 2021-22 as sales reverted to more typical levels.

Table 2.4
Historical Lottery Sales by Category

	15-16	19-20		20-21		21-22		22-23	
	Amt.	Amt.	AAGR	Amt.	Growth	Amt.	Growth	Amt.	Growth
Instant Tickets	$2,793	$3,306	4.3%	$3,902	18.0%	$3,662	-6.1%	$3,526	-3.7%
Numbers Games	581	576	-0.2	681	18.2	638	-6.3	590	-7.5
In-State Lotto	233	254	2.1	271	6.7	261	-3.8	275	5.4
Multistate Lotto	496	270	-14.2	384	42.3	382	-0.5	574	50.3
Raffle and Other	32	64	19.2	65	1.9	66	1.2	61	-6.9
Sub-Total	**4,135**	**4,469**	**2.0**	**5,302**	**18.6**	**5,009**	**-5.5**	**5,026**	**0.4**
iLottery	0	735	--	908	23.5	774	-14.8	937	21.0
Grand Total	**4,135**	**5,205**	**5.9**	**6,211**	**19.3**	**5,783**	**-6.9**	**5,963**	**3.1**

Note: Figures in dollar millions. AAGR is average annual growth rate from FY 15-16 to FY 19-20. Instant Tickets includes Scratch Offs and Fast Play. Other includes Keno and Xpress Sports.

For FY 2022-23, traditional Lottery sales (excludes iLottery) are projected to grow 0.4%, somewhat lower than average pre-pandemic growth (2.0%). Across games, Multistate Lotto outpaced all other sources with 50.3% YOY growth, a record high annual rate. This was primarily due to higher interest rates that increased advertised Powerball and Mega Millions jackpots much faster than prior years, which incentivizes ticket sales.[5] However, the surge in Multistate Lotto sales likely had a negative impact on

[5] Jackpot winners for Powerball and Mega Millions can choose to receive the estimated jackpot in 30 payments over 29 years, or the current cash value of that stream of payments. Both games invest in government-backed securities, and the interest earned from those securities impacts the size of the advertised estimated jackpots. When interest rates rise, the estimated payments over 29 years also increase and the jackpots appear larger given the same cash value.

Instant Tickets and Numbers Games sales as those categories declined by 3.7% and 7.5%, respectively, over FY 2021-22.

Due to the limited history of iLottery, it is displayed separately in Table 2.4. Gross sales expanded 21.0% for FY 2022-23. Sales are divided into actual iLottery games and traditional Lottery games (Multistate Lotto, Numbers and In-State Lotto) played online. While the vast majority (over 94%) of iLottery gross sales in FY 2022-23 are from actual iLottery games, $53.4 million (+$25.7 million or +92.4% over FY 2021-22) are from traditional Lottery play online. The significant increase in traditional Lottery play online is because FY 2022-23 is the first full year Numbers games can be played online and strong online sales within Powerball and Mega Millions.

The initial revenue estimate projects that Lottery Fund net revenues will increase by $6 million (0.3%) for FY 2022-23 and $21 million (1.1%) for FY 2023-24. (See **Table 2.5**.) The first result is driven in part by increases in (1) gross ticket sales for FY 2022-23 (explained above) and (2) field paid prizes and commissions. These increases were partially offset by a small decline in miscellaneous revenue.

Table 2.5
Lottery Fund Summary

	Estimated 2022-23		Projected 2023-24	
	Amount	Growth	Amount	Growth
Total Lottery Fund	**$1,973**	**0.3%**	**$1,994**	**1.1%**
Gross Ticket Sales	5,963	3.1	6,151	3.1
Field Paid Prizes & Commissions	-4,102	4.4	-4,254	3.7
Miscellaneous Revenues	112	-2.9	98	-12.5
Gross Ticket Sales Detail	**5,963**	**3.1**	**6,151**	**3.1**
Instant Tickets	3,526	-3.7	3,646	3.4
Multistate Lotto Games	574	50.3	579	0.9
In-State Lotto	275	5.4	281	2.4
Numbers Games	590	-7.5	590	-0.1
iLottery	937	21.0	993	6.0
Raffle and Other	61	-6.9	62	0.8
Miscellaneous Revenues Detail	**112**	**-2.9**	**98**	**-12.5**
Gaming Fund Transfers	89	-22.2	87	-1.8
Other Miscellaneous Revenue	23	--	10	-54.1

Note: Figures in dollar millions. Due to rounding, detail may not sum to total. Growth rates based on the unrounded amounts. Instant Tickets includes Scratch Offs and Fast Play. Other includes Keno and Xpress Sports.

For FY 2023-24, Lottery ticket sales are expected to revert to growth rates near historical patterns. Highlights include:

- Instant Ticket sales, which include Fast Play, are projected to increase 3.4% as they remain popular with consumers, but there is downside risk due to continued competition from other games.

- Sales of iLottery are expected to rise 6.0% after strong growth in FY 2022-23 due to continued popularity with consumers.
- Multistate Lotto sales are projected to return to a more typical average annual growth rate of 0.9% after a record-setting year in terms of sales growth.
- Numbers Games are expected to remain flat due to players' preference for newer lottery games.

Federal Funds

Federal funds appropriations confer authority to spend money that the federal government may provide, and state agencies request annual spending authority as part of the budget process. A federal funds appropriation does not guarantee funding, and actual funds received and disbursed may be considerably less than the appropriated amounts. Agencies typically request authority to spend all federal funds anticipated for a given fiscal year.

The IFO reviewed Request for Appropriation of Federal Funds (RAFF) forms and reports provided by the Office of the Budget regarding requested federal funds authority. For FY 2022-23, agencies requested $39.05 billion in federal General Fund appropriations. (See **Table 2.6**.) Executive authorizations and non-General Fund requests for appropriations are not included. The Departments of Human Services (DHS), Education (PDE), and Health (DOH) comprise roughly 93% of the General Fund federal spending authority requested by the Commonwealth in FY 2022-23. The Department of Human Services requested $32.58 billion, PDE $3.20 billion and DOH $576 million. For FY 2023-24, the administration projects agencies will require $41.49 billion (6.3%) in base General Fund spending authority.

The text that follows provides highlights for DHS, PDE and DOH for FY 2023-24.

- **DHS** requests authority to spend up to $33.30 billion in federal funds, a 2.2% increase over the current fiscal year. Medical Assistance (MA) payments represent the largest commitment of federal funding ($29.88 billion, 2.4% higher than FY 2022-23) and generally require some level of state matching funds. Children's Health Insurance Program (CHIP) funding is projected to decrease 23.5% to $233 million for FY 2023-24.
- **PDE** requests authority to spend up to $4.54 billion in General Fund federal monies, an increase of 41.7% over the current year. This increase in funding is largely due to (1) Food and Nutrition and (2) the Elementary and Secondary Education Act (ESEA) Title 1 Local Grant Programs.
- **DOH** requests authority to spend up to $589 million in General Fund federal revenue, an increase of 2.4% over the current year. Of that amount, $278 million will be used for the Women, Infants, and Children (WIC) program.

Under the federal Infrastructure Investment and Jobs Act (IIJA), federal funds are available for a variety of infrastructure programs, including energy and power infrastructure, access to broadband internet and water infrastructure. For FY 2022-23, $359 million in federal funds spending authority were requested by DEP ($194 million), DCED ($152 million), Pennsylvania State Police ($8 million), PEMA ($5 million) and DCNR ($0.4 million). For FY 2023-24, an additional $735 million is requested by the following agencies: DCED ($430 million), DEP ($285 million), PEMA ($11 million), the Pennsylvania State Police ($9 million) and DCNR ($0.4 million).

Table 2.6
Federal Funds Summary

	2021-22	Available 2022-23		Projected 2023-24	
	Amount	Amount	Growth	Amount	Growth
Total Federal Funds	**$37,673**	**$39,051**	**3.7%**	**$41,493**	**6.3%**
Human Services	32,075	32,580	1.6	33,295	2.2
Education	2,770	3,205	15.7	4,541	41.7
Health	574	576	0.3	589	2.4
Labor & Industry	525	460	-12.4	491	6.7
Drug & Alcohol	303	308	1.8	278	-9.8
DCED	285	431	51.1	723	67.8
Military & Veterans Affairs	212	247	16.6	236	-4.6
Transportation	206	246	19.8	246	0.0
Executive Offices	202	226	11.9	204	-9.6
DEP	138	333	141.3	470	41.4
Aging	105	109	4.1	115	5.1
Agriculture	99	122	23.2	97	-20.5
DCNR	50	76	53.4	66	-13.1
PEMA	37	42	14.3	48	15.6
State Police	24	32	29.9	34	5.5
All Other	69	58	-15.6	60	2.3

Note: Figures in dollar millions.

In addition to the funds detailed in Table 2.6, the state was allocated federal funds related to a temporary increase in the Federal Medical Assistance Percentage (FMAP) used to calculate federal reimbursements for Medicaid programs. The enhanced FMAP remained in full effect through March 31, 2023 and will be phased-out gradually by December 31, 2023. Enhanced FMAP funds offset $2.47 billion in DHS Medical Assistance program costs in FY 2021-22 and are expected to offset $2.19 billion in FY 2022-23. For FY 2023-24, the enhanced FMAP offset is expected to fall to $515 million.

Table 2.6 also excludes $7.29 billion in payments under the American Rescue Plan Act. This funding is general aid for eligible expenses incurred through CY 2024 and is available for a wide range of uses in response to the health and economic impacts of the COVID-19 pandemic, including support to households and businesses, replacing lost revenue and support for government operations affected by the pandemic. In FY 2021-22, $5.91 billion was appropriated, including $3.84 billion that was transferred to the General Fund as revenue loss replacement. An additional $1.38 billion was appropriated for pandemic response programs, including funds for long-term living facilities and hospital and healthcare workforce assistance for FY 2022-23.