

## TAX REVENUE GROWTH SLOWDOWN LIKELY, EXPERTS TELL BUDGET WRITERS

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STATE HOUSE, BOSTON, DEC. 12, 2005....Beacon Hill leaders commenced another budget cycle Monday morning by predicting tax revenues will grow by about 5 percent in the fiscal year ahead, reflecting slower economic growth than in the past two years.

Weak employment growth, recently enacted tax cuts, and lower corporate tax profits are all factors in the forecast of slower tax revenue growth, economic experts told Romney administration officials and legislative leaders, who will try to agree soon on a revenue target that would serve as a common denominator for budget debate and talks over the next six months.

"I think we're still optimistic for next year, just moderately so," said Alan LeBovidge, commissioner of the Department of Revenue, during testimony in which he forecast modest revenue and employment growth for the remainder of fiscal 2006 and a slowed recovery in fiscal 2007.

"While the tax outlook is modestly positive for 2007, weak employment growth will be a significant drag on both the state's economy and the Commonwealth's economy," said Massachusetts Taxpayers Foundation President Michael Widmer.

Since 2003, Widmer said, the Commonwealth has generated jobs at less than half the national average. The country's latest fiscal downturn "was much less severe than it was here," he added.

"We don't have - and I can't say this strongly enough - we don't have a budget surplus, despite what you read in the paper," Widmer said. "With this revenue forecast that we all seem to share, the state's fiscal affairs remain very tight."

State budget writers said they were encouraged by the varying predictions' similarities, but frustrated that the Bay State economy remains far from its heyday of the early decade.

"The good news is that I believe there is consistency in terms of what the revenue estimate will be," said Thomas Trimarco, secretary of the Executive Office of Administration and Finance. He said, "Obviously, on the other side of the equation is: Things are still tight. This does not mean that we're in economically robust times."

Trimarco said the Romney administration is assembling its budget proposal for a January 25 unveiling, and said its crafters would probe the reasons for the Commonwealth's gimpy recovery:

"Point in time, you have to ask the question: Why is this happening?" Trimarco said. "Maybe tax policy has something to do with that, high cost of living has something to do with that."

LeBovidge told lawmakers that state tax receipts this fiscal year may hit \$18 billion and growth next year could net the state as much as \$19 billion.

This year's budget used a \$17.1 billion estimate, which means a revenue surplus is forming and will materialize by June if state government keeps its spending down in line with the budget.

Federal funding and fees also help pay for annual state spending.

Under questioning from Senate Ways and Means Committee Chairwoman Therese Murray (D-Plymouth), LeBovidge acknowledged that "we've had negative job growth in the last couple of months" and said withholding taxes are rising primarily due to wages hikes, not job growth.

LeBovidge predicted a "decent bonus year" in the financial services sector, which will buffet this year's tax receipts. He said tax cuts this year - including senior property tax relief, energy cost defrayment, enticements to movie producers, and rebates of capital gains taxes paid in 2002 - will reduce projected state revenues by \$199 million.

The capital gains tax legislation, signed last week at a press conference well attended by lawmakers from both parties, was linked to legislation raising \$85 million annually by closing corporate tax loopholes, but LeBovidge said Monday that number had dwindled to \$36 million because of the delayed passage.

"We lost \$10 million dollars a month by not passing that in a timely fashion," Murray said later, adding that the revised numbers likely would be recalibrated into future spending.

During the two-hour-plus hearing in Gardner Auditorium, the economic experts enumerated a number of outside factors that would bear on the economy, including overseas export of jobs, the cost of health care insurance to employers, the slowing housing market, and fallout from Hurricane Katrina.

UMass-Boston Associate Professor Alan Clayton-Matthews said the jump in home heating oil costs, up 44 percent from a year ago according to federal Energy Information Administration statistics, will cost the average homeowner \$700 more this season than last, one of a number of external factors that the speakers said likely would have short-term impact on revenue collections and long-term influence on growth.

After Clayton-Matthews described the recent crisis as on par with the early-1990s recession in severity but slower in recovery, Murray said: "Well, I'm depressed. You're usually the optimist."

Later, during an interview in her offices, she told the News Service, "I'm very concerned. They all seemed to be on the same page as far as the problem with job growth, and the brain drain they see because of the insufficient funding of our higher education system."

Murray said she was also worried by testimony that the state's revenue intake is supported disproportionately by growth in the upper income brackets.

"There seems to be this growing gap which is very scary," Murray said. "That's what happened in the '90s, and we relied on these capital gains numbers, and that's why we took such a big fall."

Trimarco said he is unaware of any change in Gov. Mitt Romney's plan to abide by voters' wishes and roll the state income tax rate from 5.3 percent to 5 percent. Asked by Sen. Stephen Brewer (D-Barre) what the loss in revenue that shift would exact, Howard Merkowitz, director of LeBovidge's Office of Tax Policy Analysis, estimated \$610 million.

Romney confirmed today that his budget will call for the income tax rollback.

"I believe that it is incumbent upon us to reduce state spending so that we can provide the tax rate that was voted by the citizens," Romney said, mentioning Attorney General Thomas Reilly's recent qualified support for the rollback. "I think you can expect that my budget will reflect that fact."

David Tuerck, executive director of the Beacon Hill Institute and professor of economics at Suffolk University, said tax revenues grew 7.1 percent in fiscal 2005, are likely to grow 5.5 percent this fiscal year and will likely increase by 5.1 percent in the fiscal year that starts July 1.

"Although Massachusetts lags the national economy, we see strong growth in state tax revenue through the rest of fiscal 2006," said Tuerck. "State tax revenue growth will fall off a bit during fiscal 2007 but will nevertheless reflect continued underlying strength in the state economy."

During the hearing, Murray expressed concern about job losses, rising interest rates, the slowing of the housing market, and people losing health care coverage when they lose their jobs. She asked LeBovidge how much it will cost the government to assist those who lose their jobs. He said he didn't know.

Rep. Alice Wolf (D-Cambridge) said rate of revenue growth will play a major role in determining how much state government can increase local aid to cities and towns.

In response to Rep. John Quinn's (D-Dartmouth) inquiry about the loss of sales tax receipts to a surge in Internet shopping, revenue department officials acknowledged that sales tax collections have softened but could not say how much of that is due to online shopping. Federal efforts to streamline sales tax collections are continuing, they said.

The bloodletting of manufacturing jobs in the state, which some economic experts chalk up in part to the transition of Massachusetts' economic focus to a "knowledge-based economy," has been due primarily to the price of industrial investment here, Widmer said.

"I think the principal loss of manufacturing in the state is due to cost," Widmer said in reply to a question from Rep. Walter Timilty (D-Milton). Asked by Rep. Susan Grant (D-Beverly) to detail the percentage split between losses to domestic states and to other countries, Widmer replied, "Now there's an acceleration of job loss abroad. I have no idea what the percentage is."

Widmer questioned estimates frequently cited in the Beacon Hill debate over introducing slot machines to Massachusetts racetracks. "Racino" revenues, proponents say, could reach \$500 million for the state in the first year.

"Those clearly strike me as too high. They might be, at best, half that," Widmer said, adding that the influx would likely be partially offset by a decline in Lottery revenues.

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