

2015/16
BUDGET BRIEFING
Report on Key Issues
HOUSE APPROPRIATIONS COMMITTEE (D)

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Gov. Wolf's 2015/16 Executive Budget Proposal

Please note: This document provides a quick overview of [Gov. Wolf's 2015/16 Executive Budget proposal](#). The House Appropriations Committee (D) will continue to review the budget proposal and provide briefings on specific issues and program areas, as more details become available.

Overview

Gov. Wolf addresses the commonwealth's fiscal crisis head on and lays out a multi-faceted plan to address a myriad of serious state and local public policy challenges. He proposes solutions to complex issues ignored over many years.

- He asks the General Assembly to **reverse the devastating cuts to schools** that have already impaired four years of our children's learning – precious time that is lost and Pennsylvania must no longer squander. He asks the General Assembly to recognize that education and economic prosperity are inextricably linked. His focus on education emphasizes that education is meaningless absent a path to jobs, job creation and the infrastructure necessary to support business.
- He asks the General Assembly to **restore, over three years, the harmful cuts to our county run human service programs**. He proposes to expand community-based services and implement managed long-term care within three years.
- He asks the General Assembly to recognize that local taxes are overly burdensome for many hardworking Pennsylvanians and **proposes dramatic school district property and wage tax relief** worth \$3.8 billion. According to his budget, the proposal eliminates property taxes for 270,000, or nearly 30 percent of senior households. To help renters, up to \$500 will be available in rent relief for households that earn up to \$50,000. He funds this substantial local tax cut with the personal income tax – a tax that most retired senior citizens do not pay. This proposal appears to be a nod to several Republican-supported proposals, which recommended replacing local taxes with state taxes.
- In a further effort to shore up the business environment, he asks the General Assembly to **reduce business taxes**, making the state better able to grow existing businesses and attract new industry. He reduces the artificially high corporate net income tax from 9.99 percent to 4.99 percent by 2017 and supports elimination of the capital stock and franchise tax. Unlike the former administration's business tax policy, Gov. Wolf proposes a balanced approach when cutting business taxes that does not sacrifice investments in education and other core government services.
- He proposes a way to **reduce the pension debt and recommends setting the state's school pension obligation aside in a special account** so future politicians can never again borrow from the pension funds to balance the budget. As a businessman, he supports the reforms put in

place under Act 120 of 2010 that repealed Ridge administration benefit increases for incoming employees. Because of those substantial reforms, the employer pays less than 3 percent of payroll for new employees, which is very competitive compared to private-sector plans. Unfortunately, this message is often lost in the rhetoric, as some politicians blame the pension debt on workers and their retirement benefits.

- Most notably, Gov. Wolf asks the General Assembly to **fix the more than \$2 billion structural deficit with sustainable forms of revenue**. He pays for PreK-12 education increases with a new severance tax on natural gas and balances the budget with the sales and use tax, closing the Delaware loophole for corporate net income taxpayers, tobacco taxes and other adjustments. Republicans and Democrats alike have recognized for some time now the magnitude of the problem that incoming Gov. Wolf inherited, and it is time to roll up our sleeves and get to work.

Combined Operating Budget

Although much emphasis is placed on the General Fund budget, the combined operating budget provides the most accurate representation of spending trends. In recent years, governors have shifted spending among funds to help balance the most-watched General Fund budget. When you consider all funds (federal, state, special and other funds), the governor's proposal represents a **total commonwealth operating budget of \$78.6 billion, including \$50.7 billion in non-federal funds**.

After several years of deferring contributions to the Rainy Day Fund, the governor's proposal begins to rebuild the fund with a transfer of 25 percent of the General Fund balance, \$32.3 million, as required under statute. The remaining balance in the General Fund, \$96.8 million, rolls over to the beginning balance for 2016/17.

General Fund

Gov. Wolf's proposed 2015/16 state General Fund budget of \$29.9 billion increases state expenditures by \$836.5 million, or 2.8 percent (after adjusting for proposed supplemental appropriations and lapses). This growth in spending assumes that Pennsylvania's payment to the school pension fund is moved into a special restricted revenue account for 2015/16.

A closer look reveals that the effective growth rate is 5.4 percent for the budget year (or \$1.7 billion), the same effective growth rate as in Gov. Corbett's last budget. The effective growth rate in expenditures more fairly compares fiscal years because it takes into account the following:

- The \$869.9 million in delayed payments and expenditures shifted offline under former Gov. Corbett artificially suppressed 2014/15 spending, thereby understating growth in an effort to balance the budget.
- The \$1.75 billion shifted to a newly proposed restricted account for school pension payments under Gov. Wolf, thereby understating 2015/16 spending by \$1.75 billion.

This increase is largely comprised of Gov. Wolf's commitment to restore former Gov. Corbett's budget cuts, especially the cuts he made to education. Other key provisions include proposals to:

- Reduce property and wage taxes by \$3.8 billion, including the more than \$600 million in gaming revenue already dedicated to property tax relief, which will directly benefit homeowners, renters, workers and businesses. In communities where homeowners reach the maximum reduction allowed by law, the remaining funds will be used to reduce the millage rate for homeowners and businesses. (See the property tax section on Page 20 for more information.)

- Close the more than \$2 billion structural budget deficit left by the Corbett administration with sustainable sources of revenue.
- Create a dedicated special restricted revenue account for Pennsylvania’s required payment to the Public School Employees’ Retirement System (PSERS) Fund to ensure future pension payments are made in full.

The governor expects 2014/15 General Fund revenues to meet the current forecast, with revenues just \$4.1 million, or 0.01 percent, below the official estimate. The Independent Fiscal Office revised its estimates in January 2015 projecting the fiscal year would close with revenues just \$26 million above the official estimate. Although fiscal year-to-date collections were \$377.7 million above estimate at the end of February, there are several one-time transfers scheduled for the end of the year that are not likely to materialize. For example, the official estimate assumed revenue from leases on state forest land from non-impact surface drilling and casino fees, which are no longer expected to occur in the current fiscal year.

Gov. Wolf’s fiscal year 2015/16 General Fund budget projects 1.5 percent revenue growth (\$448.3 million) reflecting numerous one-time revenue sources used in 2014/15 that will not recur next year. This 1.5 percent revenue growth rate does not include Gov. Wolf’s proposed revenue modifications. These modifications worth \$4.55 billion in 2015/16 (\$4.66 billion before adjusting for \$108.1 million in refunds) add an estimated \$2.5 billion in net new revenue for the General Fund after accounting for \$2.14 billion that the governor proposes to transfer to the property tax relief fund, with disbursements starting in 2016/17.

Tax and Revenue Package Highlights	
<i>(\$ Amounts in Millions)</i>	
Tax Type	
Property and Wage Tax Relief , Including Rent Rebates (2016/17)	\$ (3,800.0)
Tax Type	2015/16
Corporate Net Income Tax - Rate Decrease with Combined Reporting	\$ (249.3)
Severance Tax - 5% of value plus \$0.047 per Mcf	\$ 165.7
Net Personal Income Tax - Increase from 3.07% to 3.7%	\$ 2,302.2
Sales and Use Tax - Increase from 6% to 6.6% and base expansion	\$ 1,554.3
Cigarette Tax - Increase state rate by \$1.00 per pack	\$ 358.4
Other Tobacco Products - 40% of wholesale price	\$ 84.1
Bank Shares Tax - Rate at 1.25%	\$ 339.2
	\$ 4,554.6

See the Tax and Revenue Changes section on Page 20 for more information.

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Education

Gov. Wolf's proposed budget provides an **additional \$1 billion through a combination of education funding and cost saving reforms**, which includes the following:

- \$662 million in PreK-12 funding
 - \$400 million in basic education funding
 - \$100 million in special education funding
 - \$120 million in early childhood funding
 - \$42 million in other K-12 appropriations (after including a requested \$15 million supplemental increase for social security in 2014/15)
- \$148 million for institutions of higher education, both public and private
- \$25.5 million in additional PHEAA business earnings to augment state appropriations for higher education
- \$10.6 million for other PHEAA programs
- \$162 million in savings to school districts through cyber charter funding reforms

The budget anticipates that, including all funding, reforms and property tax relief, the overall state share of education funding will now be more than 50 percent.

PreK-12

Gov. Wolf's 2015/16 budget proposal **increases overall PreK-12 funding by \$662 million**, for total funding of \$9.85 billion. This total excludes the \$1.75 billion pension payment moved to a special restricted revenue account. (See the pension section on Page 8 for more information.) Furthermore, the governor makes a four-year commitment to increase overall PreK-12 education funding by \$2 billion.

Basic Education Funding

The governor proposes to increase the **basic education funding (BEF)** subsidy by \$400 million, or 7 percent, for total funding of \$6.13 billion. This subsidy payment includes a full restoration of the Accountability Block Grant and Educational Assistance Program funding, plus a 10 percent reimbursement for charter school payments. These three restorations were eliminated during the Corbett administration.

Traditionally, the BEF funding formula has changed each year. Currently, a Basic Education Funding Commission, established by the General Assembly, is scheduled to present a new funding formula in June 2015. Gov. Wolf's proposed budget indicates a willingness to enact a new BEF formula, based upon adequacy, equity, predictability and accountability, to take effect in the 2016/17 school year.

Special Education

The governor proposes to increase **special education funding (SEF)** by \$100 million, or 9.6 percent, for total funding of nearly \$1.15 billion. In 2014/15, a new special education funding formula was enacted based upon the recommendations of the Special Education Funding Commission and the proposed formula continues the transition to this new formula. Gov. Wolf advocates for moving the current SEF formula language from the Fiscal Code into a permanent section of the Public School Code.

Early Childhood

This budget proposes a goal for **universal Pre-K** education for all 3- and 4-year olds in Pennsylvania. As a first step, the proposed budget increases funding for early childhood education by \$120 million, including:

- \$100 million, or 103 percent, for **Pre-K Counts**, which provides early learning opportunities for children – for total funding of \$197.3 million.
- \$20 million, or 51 percent, for **Head Start Supplemental Assistance**, which provides early learning opportunities for economically disadvantaged children – for total funding of \$59.2 million.

The budget proposal also endorses early education policy changes, including:

- Allows Head Start Supplemental Assistance funds to be used for home-based pre-school;
- Allows Pre-K providers to use a portion of their funding for transportation;
- Establishes an early childhood workgroup to study programmatic changes;
- Extends the highest priority to special groups (such as teen parents and children in foster care); and
- Analyzes the early learning workforce, in conjunction with the Department of Labor and Industry, to identify and address current employment issues.

Career and Technical Education

The governor's budget increases funding for initiatives to prepare students for careers after high school graduation as part of the "Jobs that Pay" initiative, including:

- \$23 million, or 37.1 percent, for **Career and Technical Education** – for total funding of \$85 million; and
- \$2 million, or 67 percent, for **Career and Technical Education Equipment Grants** – for total funding of \$5 million. In the prior two fiscal years, this appropriation was included by the legislature.

Dual Enrollment

The proposed budget recommends a \$9 million appropriation to fund the **Dual Enrollment** program, which allows high school students to earn college credits. Funds for this program are derived from PHEAA earnings.

Other Programs

The governor proposes other appropriation changes, including:

- Increasing the **Adult and Family Literacy** subsidy by \$4.6 million, or 38.1 percent, for total funding of nearly \$16.7 million.
- Increasing the two nonpublic school appropriations by 7 percent, the same percentage increase as the basic education subsidy:
 - Increasing **Services to Nonpublic Schools** by \$6 million, for total funding of \$92.4 million.
 - Increasing **Textbooks, Materials and Equipment for Nonpublic Schools** by \$1.8 million, for total funding of \$28.1 million.
- Flat funding the **Public Library Subsidy** at \$53.5 million.
- Reducing the **Library Access** (Power Library, interlibrary delivery and electronic library catalog) by \$250,000, or 8.1 percent, for total funding of \$2.8 million.

- Flat funding for the **Authority Rentals and Sinking Funds (PLANCON), PA Assessment and Safe School Initiative.**

Education Initiatives

Gov. Wolf’s proposal includes additional education initiatives, such as:

- Reforming cyber charter school funding by instituting a standard reimbursement rate of \$5,950 for regular education students and additional funding for special education students (\$3,035 for Category 1, \$16,482 for Category 2 and \$38,437 for Category 3 students). These funding changes are anticipated to save school districts \$162 million each year.
- Instituting increased accountability in education, including mandates to school districts that receive substantial increases.
- Requiring charter and cyber charter schools to reimburse school districts when the charter schools audited expenditures are less than tuition revenue.
- Challenging school districts to save money by working together and with Intermediate Units.

Higher Education

Gov. Wolf’s budget proposal increases total state appropriations for higher education by \$159 million. He allocates most of the additional funds to institutions of higher education, as shown in the chart below.

Funding for Institutions of Higher Education				
<i>(\$ Amounts in Thousands)</i>				
Institution Type	2014/15 Available	2015/16 Budget	\$ Change	% Change
Community Colleges	\$215,667	\$230,723	\$15,056	7.0%
Pennsylvania State System of Higher Education	\$412,751	\$458,053	\$45,302	11.0%
Penn State University - Including Penn College of Technology	\$231,694	\$282,549	\$50,855	21.9%
University of Pittsburgh	\$136,293	\$151,211	\$14,918	10.9%
Temple University	\$139,917	\$155,361	\$15,444	11.0%
Lincoln University	\$13,163	\$14,084	\$921	7.0%
Thaddeus Stevens College of Technology	\$12,332	\$13,195	\$863	7.0%
Institutional Assistance Grants (Under PHEAA)	\$24,389	\$29,389	\$5,000	20.5%
TOTAL	\$1,186,206	\$1,334,565	\$148,359	12.5%

The governor’s proposal represents the first widespread and meaningful increase for colleges and universities since Gov. Corbett significantly cut state support in 2011/12. That year, institutions experienced budget cuts and mid-year freezes ranging from 5 to 23 percent, depending on the type of institution. Although the General Assembly passed some smaller targeted increases for higher education in budgets since 2011/12, **Gov. Wolf’s plan indicates that he intends to fully restore the remaining cuts over the next two years.**

Under the Pennsylvania Higher Education Assistance Agency (PHEAA), Gov. Wolf proposes a **\$10 million expansion of the Ready to Succeed scholarships** launched in last year’s budget, which are available to middle-class students with outstanding academic achievement. The governor also proposes additional support for students at Cheyney University and Lincoln University through increased funding of \$466,000 for the Bond-Hill Scholarships and \$475,000 for the Cheyney Keystone Academy.

Other Appropriated PHEAA Programs				
(\$ Amounts in Thousands)				
Program	2014/15 Available	2015/16 Budget	\$ Change	% Change
PHEAA Grants to Students	\$344,888	\$344,888	\$0	0.0%
Ready to Succeed Scholarships	\$5,000	\$15,000	\$10,000	200.0%
Pennsylvania Internship Program Grants	\$350	\$0	(\$350)	-100.0%
Matching Payments for Student Aid	\$12,496	\$12,496	\$0	0.0%
Higher Education for the Disadvantaged	\$2,246	\$2,246	\$0	0.0%
Higher Education of Blind or Deaf Students	\$47	\$47	\$0	0.0%
Bond-Hill Scholarships	\$534	\$1,000	\$466	87.3%
Cheyney Keystone Academy	\$1,525	\$2,000	\$475	31.1%
TOTAL	\$367,086	\$377,677	\$10,591	2.9%

Outside of appropriated state support for higher education, the governor asks the PHEAA board to allocate an additional \$25.5 million of PHEAA's business earnings towards a number of initiatives:

- **\$7.5 million for new STEM scholarships** for students seeking careers in science, technology, engineering and math.
- **\$8 million for Loan Forgiveness for Primary Care Physicians** who practice in underserved areas, bringing the total to \$8.5 million. The request would expand the loan forgiveness program, which in prior years has been funded through the Department of Health's primary health care practitioner appropriation and a small amount of PHEAA business earnings.
- **\$1 million for the Targeted Industry Cluster Program (PA-TIP)** scholarships for in-demand certificate and training programs less than two years in length. If approved, PHEAA would provide \$7 million in total for this program.
- **\$9 million for dual enrollment grants** for students to take college classes while in high school.

The governor also requests that PHEAA continue to augment the state grant program and the distance education pilot program with its business earnings at current levels.

Pensions

Gov. Wolf's 2015/16 budget proposal includes a multi-faceted strategy to address the commonwealth's pension funding challenge. The governor proposes to pay the state's required annual employer contribution and debts owed, and provide immediate budget relief to school districts.

To summarize, the proposal includes the following changes:

- Creates a special restricted revenue account to ensure the commonwealth's annual payment for the Public School Employees' Retirement System (PSERS) is not compromised in the future.
- Refinances a portion of the pension-related debt to reduce school districts' annual pension payments and the unfunded liability. Beginning in 2017/18, the proceeds generated from modernizing the commonwealth's wine and spirits system will be used to pay the full cost of the debt service.
- Seeks to reduce fees paid to professional fund managers by moving a greater share of the pension systems' assets to passive investment instruments.
- Permanently eliminates the charter and cyber charter school pension "double dip".

Ensure Employer Contributions and Debt Payments

The governor's proposal creates a special restricted revenue account, composed of monies received from the General Fund, to ensure the state makes its annually required employer contribution payment to Public School Employees' Retirement System (PSERS) and does not shirk its responsibility in the future, as has been done in the past. The governor's budget proposal will continue to make the statutory annual required employer contribution, pursuant to Act 120 of 2010.

To supplement school districts' employer contributions, the proposal includes \$80 million from enhanced revenues from liquor modernization in 2015/16 and is allocated to school districts to reduce their pension payments. Beginning in 2017/18, as a result of the cash infusion of bond proceeds into PSERS, which will pay down the unfunded liability of the system, school districts' pension payment rates will decrease by about 1.6 percent (from 32.0 to 30.4 percent). This action will reduce the annual employer contribution rate paid by the commonwealth, school districts and others by approximately 5 percent, generating savings for all employers.

Refinance the Unfunded Liability

The governor's proposal refinances \$3 billion of PSERS' unfunded liability by issuing bonds and deposits the proceeds into the system's fund, a move intended to reduce the accrued unfunded liability by \$8 billion over 30 years. However, it is important to note that while this strategy may prove to be advantageous, these financial instruments will increase the state's debt service and may involve risks which will require further review and due diligence. Beginning in 2017/18, Pennsylvania will pay debt service costs, estimated to be roughly \$184 million per year, with profits generated by modernizing the state's wine and spirits system.

Investment Fee Proposal

In an effort to reduce investment fees paid to professional fund managers, the governor's proposal includes pension management reforms, such as moving a larger portion of each system's asset allocation to passive, index-based investment approaches, where appropriate. The proposal assumes unspecified investment savings. **However, this strategy involves risks, which require further review and due diligence.** Investment professionals at the pension systems argue that well-intentioned proposals such as this could actually have the unintended consequence of reducing investment returns. They argue that in those limited cases when fees are expensive, the risk-adjusted, long-term investment returns more than make up for the cost, on average.

Eliminate the Pension Double Dip

The governor's budget proposal seeks to permanently eliminate the state's duplicative retirement contribution to charter and cyber-charter schools. The savings from this are estimated to be roughly \$94 million in 2015/16.

Public Employees Retirement Commission (PERC)

The governor's budget proposal includes level funding for PERC. PERC is charged with monitoring public retirement systems in the state to assure their actuarial viability through nonpartisan review of any proposed legislative changes to those plans so the General Assembly can make informed decisions. To more properly reflect PERC's role as an asset to the General Assembly, this budget proposes to move funding for PERC from the Executive Offices section under the oversight of the Governor to the Government Support Agencies section, under the purview of the General Assembly.

Health & Human Services

Human Services

Gov. Wolf's 2015/16 budget proposal for the Department of Human Services (DHS) increases General Fund spending by \$691 million, or 6.2 percent, compared to 2014/15 after including a requested supplemental increase of \$8.7 million. Our preliminary analysis indicates **\$569 million of the increase is necessary to fill the budget hole created by former Gov. Corbett in 2014/15** when he:

- Opted to delay one month of managed care payments to the next fiscal year (worth approximately \$394 million); and
- Raided special funds to pay various Medicaid expenditures in order to reduce General Fund spending (\$82 million from the Lottery Fund and \$93 million from Tobacco Settlement Fund).

Medical Assistance

Gov. Wolf's 2015/16 budget proposal assumes more than 2.9 million Pennsylvanians will be eligible for Medicaid and receive health care coverage through Medical Assistance (MA), the commonwealth's Medicaid program. The proposed budget includes \$4.52 billion in state spending for the three major MA appropriations that fund health care coverage: Capitation (which funds managed care); Fee For Service (this new appropriation funds outpatient and inpatient services, previously funded through separate appropriations); and Medical Assistance for Workers with Disabilities. This represents a \$68 million, or 1.5 percent, increase over 2014/15 after including a requested \$120 million supplemental decrease in appropriations due primarily to a downward adjustment in caseload projections.

The proposed 2015/16 budget reflects two key factors which reduce the need to spend state General Fund revenue on MA health care coverage:

- Effective Jan. 1, 2014, Pennsylvania expanded Medicaid eligibility to include all Pennsylvanians through age 64 with incomes up to 138 percent of the federal poverty level. As a result, adults who previously received health care coverage through the state-funded General Assistance program now receive Medicaid coverage that is currently paid entirely with federal dollars pursuant to the enhanced Medicaid matching provisions in the federal Affordable Care Act. **Moving General Assistance adults to federally-funded Medicaid reduces state spending by \$484 million in 2015/16**, in addition to the approximately \$142 million saved in 2014/15.
- **The governor proposes "revenue maximization projects" in the fee-for-service program, which are anticipated to generate state savings worth \$130 million in 2015/16.** The budget provides no details regarding this proposal; therefore, we are unable provide any specifics at this time.

Long-Term Care

Long-term care is the most expensive component of the MA program and represents the fastest growing part of the DHS budget. Services and supports are provided in institutions (i.e. nursing facilities) as well as community-based settings (typically through waiver programs). **The 2015/16 proposed budget includes \$1.74 billion in state General Funds for long-term services and supports provided to seniors and individuals with physical disabilities. This represents an increase of \$302.5 million, or 21 percent, over 2014/15** after including a requested \$127 million supplemental increase primarily due to higher than anticipated costs and utilization of services. Our preliminary analysis indicates nearly two-thirds, or approximately \$200 million, of the 2015/16 increase is needed to replace non-General Fund revenues that were used to pay for expenditures in 2014/15, but will not be available in 2015/16. The disappearing funds are comprised of Lottery Funds, Tobacco Settlement Funds and enhanced federal

matching funds under the Balancing Incentive Payments program (the enhanced match expires after Sept. 30, 2015).

To rebalance the MA long-term care system and improve efficiencies, **Gov. Wolf proposes to expand community-based services in 2015/16 and implement Managed Long-Term Care within three years.** The rebalancing proposal is across two agencies – DHS and the Department of Aging – with a total of \$38.2 million in General Fund and Lottery Fund revenue budgeted in 2015/16. (See Lottery Fund section on Page 14 for the Department of Aging proposal). **Within DHS, the 2015/16 budget proposes \$31 million in state General Fund revenue to provide community-based services to an additional 3,372 seniors and individuals with physical disabilities:**

- \$13.2 million to provide Aging Waiver services to an additional 1,764 seniors (Home and Community-Based Services appropriation);
- \$1.7 million to serve an additional 144 seniors in the LIFE program (Long-Term Care Managed Care appropriation);
- \$13.8 million to provide waiver services to an additional 1,140 individuals with severe physical disabilities (Services to Persons with Disabilities appropriation); and
- \$2.4 million to provide attendant care to an additional 324 individuals with physical disabilities (Attendant Care appropriation).

Intellectual Disabilities and Autism

Additionally, Gov. Wolf is proposing to expand community-based services to individuals with intellectual disabilities (ID) and autism. For 2015/16, the governor requests \$20.2 million in new General Fund spending to provide services to an additional 1,125 people:

- \$18.9 million to provide ID waiver services to 1,000 individuals with intellectual disabilities who are on the emergency waiting list or are students graduating from special education (ID-Community Waiver Program appropriation).
- \$952,000 to provide ID waiver services to 75 people who currently reside in a state ID center (ID-Community Waiver Program appropriation).
- \$372,000 to provide community services to an additional 50 adults with autism (Autism Intervention and Services appropriation).

County Human Services and Other Programs

Gov. Wolf's proposed budget begins a three-year restoration of former Gov. Corbett's \$84 million cut imposed in 2012/13 on county human services programs in the Human Services Block Grant. **For 2015/16, the governor proposes to restore one-third, or \$27.9 million,** to the counties through increases to seven state appropriations: Mental Health Services (\$18.3 million), Intellectual Disabilities – Community Base Services (\$4.8 million), County Child Welfare (\$1.5 million for special grants), Behavioral Health Services (\$1.6 million), Homeless Assistance (\$685,000), Human Services Development Fund (\$499,000) and Medical Assistance – Fee For Service (\$491,000 for the Act 152 drug and alcohol treatment program).

In addition to the restorations itemized above, the governor proposes the following increases for various human services state appropriations in 2015/16:

- \$4.7 million in **Mental Health Services** to provide home and community-based services for 90 individuals currently residing in state hospitals;
- \$23.9 million in **County Child Welfare** for county needs-based budgets;

- \$2.5 million in Behavioral Health Services to fund a **new initiative aimed at addressing heroin and opioid addiction**;
- \$1 million in Homeless Assistance to fund a **new initiative to reduce homelessness for veterans**;
- \$1.5 million in **Domestic Violence** to provide a 10 percent increase for programs; and
- \$876,000 in **Rape Crisis** to provide a 10 percent increase for programs.

Child Care

Gov. Wolf's budget proposes to use an additional **\$30 million of federal funding** (Child Care Development Block Grant and TANF Block Grant) **for three child care initiatives**, as follows:

- \$17.8 million to provide services for approximately additional 3,600 children of low-income families;
- \$11.4 million to provide increased reimbursement rates to STAR3 and STAR4 programs to incentivize providers to reach higher STARS levels; and
- \$2 million to provide increased add-on rates for high-quality infant and toddler care.

Health

Gov. Wolf proposes a 2.1 percent, or \$4.28 million, increase for the Department of Health. The 2015/16 proposed budget takes a similar approach to past governors' budgets by zeroing out lines for a variety of specific conditions and programs.

The governor proposes an additional \$3 million for the **Chronic Care Management** program, which is an increase of 308 percent compared to the 2014/15 budget. These funds would support the development of a State Health Care Innovation Plan to transform the coordination and delivery of patient care in order to improve outcomes whilst reducing costs.

Gov. Wolf's proposed budget also includes a 21.9 percent, or \$3.85 million, increase in funding for **State Health Care Centers (SHCs)**. This follows a final ruling by the Pennsylvania Supreme Court last November blocking Gov. Corbett's "unlawful closing" of 24 SHCs. The 60 SHCs provide a wide array of public health services, which are particularly critical for medically underserved and rural communities across the commonwealth.

The governor's budget proposes to decrease funding for the **Primary Health Care Practitioner** program by \$2.9 million, which was part of Gov. Corbett's Healthy PA plan. However, the proposed budget also recommends that \$8.5 million in Pennsylvania Higher Education Assistance Agency (PHEAA) business earnings be directed to support current grant recipients and expand the state's loan forgiveness program to recruit and retain doctors to work in medically underserved areas.

Insurance

Gov. Wolf's proposed budget reflects expanding coverage under the **Children's Health Insurance Program (CHIP)** to an additional 15,881 children. The growth in CHIP will require significantly fewer state dollars because the federal matching rates – per state dollar spent on enrollees under 300 percent of federal poverty level (FPL) – increase from 66.3 percent to 89.4 percent. The 2015/16 proposed budget assumes that this will provide \$63 million in additional federal assistance.

The governor's budget proposes to reduce administrative and program funding for CHIP by \$3.4 million (52 percent) and \$83.7 million (75 percent), respectively. This reflects the state savings from the increased federal matching rates, as well as the transition of children in families making less than 133 percent of FPL to Medicaid under the Affordable Care Act (ACA).

The governor’s proposal also directs \$7 million to the **Underground Storage Tank Indemnification Fund (USTIF)** to pay down principal and interest on a \$100 million loan to the General Fund from the USTIF in 2003/04. The original 10-year repayment plan expired in 2014 with an outstanding loan balance of \$81.6 million, including \$67.5 million in unpaid principal. The new repayment plan calls for annual payments of no less than \$7 million through 2029.

Drug & Alcohol Programs

The alarming proliferation of heroin use and opioid addiction is an ongoing challenge for law enforcement, treatment professionals and families throughout the state. To this end, Gov. Wolf proposes \$5 million in new program funding for the **Department of Drug and Alcohol Programs** to provide additional services aimed at addressing the heroin epidemic.

Tobacco Settlement Fund

The 2015/16 budget proposal allocates \$312.1 million of Tobacco Settlement Fund revenue to health-related programs, including:

- \$292.25 million of payments anticipated from tobacco manufacturers in April 2016; and
- \$19.8 million from the strategic contribution payment.

Gov. Wolf proposes the following changes to the allocation formula enacted in Act 71 of 2013 in order to redirect a total of \$23.3 million for health-related purposes in 2015/16:

- Eliminate the 8 percent funding allocation for the PACENET transfer; and
- Increase the funding allocation for health-related purposes from the 22.72 percent in current statute, to 30.72 percent.

In addition to the redirected funds, the governor recommends the strategic contribution payment continue to be appropriated for health-related purposes – namely, the Long-Term Care appropriation in the Department of Human Services, which funds nursing home care for Medical Assistance recipients and Life Science Greenhouses in the Department of Community and Economic Development. This is consistent with how the strategic contribution payment has been spent in all previous budgets.

The table below shows the proposed changes to the statutory formula used to allocate the annual payments the commonwealth receives from tobacco manufacturers. The last column shows the proposed 2015/16 distribution of all Tobacco Settlement Fund revenues, including the strategic contribution payment, to specific programs.

Tobacco Settlement Fund			
Expenditures for Health-Related Programs	Act 71 of 2013	Exec Budget 2015/16	
	Allocation %	Allocation %	\$ Millions
Home and Community-Based Services	13%	13%	\$38.0
Tobacco Use Prevention and Cessation	4.5%	4.5%	\$13.2
Health Research - Broad Based	12.6%	12.6%	\$36.8
Health Research - Cancer	1%	1%	\$2.9
Hospital Uncompensated Care	8.18%	8.18%	\$23.9
Medical Assistance for Workers with Disabilities	30%	30.0%	\$87.7
PACeNet Transfer	8%	0%	\$0.0
Health-Related Purposes:	22.72%	30.72%	
Medical Assistance - Long Term Care			\$106.6
Life Sciences Greenhouses			\$3.0
TOTAL			\$312.1

Lottery Fund

Among the many challenges inherited by Gov. Wolf is a Lottery Fund decimated by the previous administration. For 2014/15, former Gov. Corbett used a record \$502 million of Lottery revenues, including most of the \$220 million fund balance carried forward from the prior year, to help pay for Medicaid expenditures and thereby balance the General Fund budget. This is expected to leave a 2014/15 ending balance of \$11.4 million after placing \$75 million in reserve as a buffer against unanticipated expenditures and/or lagging lottery ticket sales.

Gov. Wolf's 2015/16 proposed budget is based on optimistic revenue projections, which assume lottery ticket sales grow 8.3 percent to more than \$4.25 billion and net collections (after paying commissions and field prizes) grow 9 percent to more than \$1.87 billion. The proposed budget assumes this revenue growth can be achieved by expanding points of distribution, optimizing the retailer network, continuing the growth of instant games and implementing a number of modernization initiatives.

The Executive Budget proposes total Lottery Fund spending of \$1.95 billion, which is only \$350,000 more than the current year; this includes \$1.38 billion for programs that benefit seniors as detailed in the chart on the following page. **It would leave an ending balance of \$12.4 million at the close of 2014/15, with no funds held in reserve.**

The table on the following page details the \$1.38 billion of proposed 2015/16 Lottery Fund expenditures for senior programs by agency and appropriation. This represents a net decrease of \$59.6 million compared to the current year, primarily due to reductions in the amount of Lottery Funds used to pay for Medicaid programs in the Department of Human Services (DHS).

As part of his initiative to rebalance long-term care, Gov. Wolf proposes to spend \$7.2 million of lottery revenue as follows:

- \$1.8 million is requested for the PENNCARE appropriation to provide attendant care services for an additional 228 older Pennsylvanians who, at age 60, transfer from the attendant care program in DHS.
- \$5.4 million is requested for the Pre-Admission Assessment appropriation to provide funding for the Area Agencies on Aging (AAAs) to perform the requisite screening of 2,290 individuals to determine their Medicaid eligibility for community-based services and maximize federal funds available to support the AAAs in carrying out this task.

The governor's proposal includes \$2 million for grants to senior centers, the same as the current year. It recommends small increases for PACE, the Property Tax/Rent Rebate program and the Free Transit program.

The 2015/16 budget proposes to use nearly \$420 million of Lottery Fund revenue to help pay for Medicaid expenditures in DHS, which is \$82 million less than what was appropriated for the current budget. The proposal reduces funding for nursing homes (Medical Assistance Long-Term Care appropriation) by \$56.9 million, returning it to the 2013/14 level and reduces funds for the Aging Waiver program (Home and Community-Based Services appropriation) by \$56.9 million. It keeps funding for Medical Assistance Transportation (MATP) at the same amount as currently provided in 2014/15.

Lottery Fund Expenditures for Senior Programs			
<i>(Dollars in Millions)</i>			
State Lottery Fund Expenditures for Senior Programs	Executive Budget		Change from 2014/15
	2014/15 *	2015/16	
Department of Aging:			
PennCARE	\$299.3	\$305.2	\$5.9
Pre-Admission Assessment	\$10.7	\$16.1	\$5.4
Caregiver Support	\$12.1	\$12.1	-
Pharmaceutical Assistance Fund Transfer	\$155.0	\$160.0	\$5.0
Grants to Senior Centers	\$2.0	\$2.0	-
Alzheimer's Outreach	\$0.3	\$0.3	-
Department of Public Welfare:			
Medical Assistance Long-Term Care	\$334.1	\$309.1	-\$25.0
Home and Community Based Services	\$162.6	\$105.7	-\$56.9
Medical Assistance Transportation	\$4.9	\$4.9	-
Department of Revenue:			
Property Tax and Rent Rebate	\$280.6	\$285.2	\$4.6
Department of Transportation:			
Free Transit	\$94.4	\$95.9	\$1.5
Shared Ride	\$86.0	\$86.0	-
TOTAL	\$1,442.0	\$1,382.4	-\$59.6

* Includes a recommended \$3.936 supplemental appropriation increase for PENNCARE.

As we have argued for more than a year, the Lottery Fund simply cannot sustain this level of spending. The Executive Budget shows deficits beginning in 2016/17 at \$70 million and exceeding \$150 million by 2017/18. However, **if revenues do not perform as assumed in this budget proposal, we could see a deficit as soon as 2015/16.** For example, we note that lottery ticket sales grew 2.6 percent in 2013/14 and 6 percent in 2012/13; these rates are well below the 8.4 percent growth assumed for 2015/16. Assuming ticket sales only grow 5 percent during 2015/16 and no changes are made in proposed spending, our analysis indicates the Lottery Fund could be \$16 million in the red by June 30, 2016.

The General Assembly must come up with a way to ensure sufficient funding to support the traditional senior programs under the Lottery Fund. Some may suggest that privatization of the Lottery is a solution. Remember, the lesson learned from Illinois, which was the first state to privatize, is that turning over control to a private manager does not necessarily guarantee a predictable funding source. In fact, the governor of Illinois has since fired the private manager of the lottery.

Transportation

The 2015/16 budget proposal includes \$6 billion in state funding for the Department of Transportation, an increase of \$646 million, or 12 percent. Nearly all of this growth is attributable to the revenue increases authorized by Act 89 of 2013. Total funding increases are offset by a decrease of \$113 million in federal grants due to the declining solvency of the federal Highway Trust Fund and the elimination of limited duration funds made available from the American Recovery and Reinvestment Act (ARRA) of 2009.

The governor's budget proposal recommends increasing the Sales and Use Tax (SUT) from 6.0 percent to 6.6 percent and expanding the base to include services and some products currently exempted, effective Jan. 1, 2016. Roughly 5.4 percent of gross SUT revenues are dedicated for mass transit purposes. Staff estimates that in the first year of implementation, approximately \$87 million in new revenue would be generated if the governor's proposal is enacted. Of this amount, roughly \$62 million would be made available for operating assistance; \$15 million would be for making debt service

payments on prior commitments; and approximately \$10 million for programs of statewide significance. These amounts reflect revenues for approximately half a year. Thus in subsequent years, it is estimated that with growth in the tax base these revenues will more than double.

Law Enforcement, Public Safety & Justice

State Police

Gov. Wolf proposes to increase the State Police general government operations by \$82.7 million, or 9.2 percent, for total funding of \$979.9 million (\$240.6 million from the General Fund and \$739.3 million from the Motor License Fund).

The governor proposes spending \$9 million to fund four cadet classes, for a potential total of 350 troopers. While this appears to be a significant increase, trooper complement remains significantly below authorized levels. Currently, approximately 1,000 troopers are eligible for retirement.

Corrections

Gov. Wolf proposes to consolidate the Department of Corrections and the Board of Probation and Parole by the end of 2015/16 to achieve efficiencies, cost savings and reduce recidivism. This consolidation will have no effect on the independent parole authority of the Board of Probation and Parole.

The overall 2015/16 budget proposal for the department is projected to increase by nearly \$148 million, or 7 percent, for total funding of \$2.26 billion.

In the current budget year (2014/15), the department will receive a \$56 million supplemental appropriation, due to salary increases for corrections officers garnered through arbitration and the need to hire mental health experts.

The Justice Reinvestment Act (JRI) of 2012 was expected to save the commonwealth \$139 million over a five-year period beginning in 2012/13. While the first three years of the initiative only resulted in a savings of less than \$500,000, savings for 2015/16 are expected to reach \$1.4 million. The budget directs these savings to the PA Commission on Crime and Delinquency, the PA Commission on Sentencing and various local law enforcement programs to fight crime on the front end.

At the end of December 2014, there were 50,756 inmates in the state prison system. According to the 2015/16 budget program measures, it will cost the commonwealth \$45,762 per inmate for one year of incarceration. The cost per individual inmate varies depending on several factors including housing placement, type of offense and medical needs.

Board of Probation & Parole

Gov. Wolf proposes to increase funding for the Board of Probation and Parole by \$16.1 million, or 10.3 percent, in 2015/16. As inmates leave prison more quickly under the Justice Reinvestment Initiative (JRI), the board has seen increases in its caseload. Additional funding for the board will also allow it the ability to utilize the latest technology to supervise offenders.

The total proposed budget for the board is \$172.5 million. A proposed increase of \$2.4 million for Improvement of Adult Probation Services will help to reimburse counties for local probation.

Attorney General

The governor proposes to increase funding for the Office of Attorney General in 2015/16 by \$3.2 million, or 3.5 percent, for total funding of \$95.5 million. To assist in dealing with problems related to heroin use, sex trafficking, child sexual abuse and crime fighting, the governor proposes increases for several programs, including an additional \$900,000 for Drug Law Enforcement, \$146,000 for Child Predator Interception and \$64,000 for the Mobile Street Crimes Unit.

Judiciary

Gov. Wolf proposes level funding of \$317.4 million for all levels of the Judiciary.

Environment

Environmental Protection

Gov. Wolf's 2015/16 budget proposal provides increases for the Department of Environmental Protection's two largest appropriations: a \$5.1 million, or 6.1 percent, increase to Environmental Protection Operations and a \$1.2 million, or 4.3 percent, increase for Environmental Program Management. The Environmental Protection Operations appropriation will also receive an annual \$5 million augmentation from the governor's proposed severance tax on natural gas. Similarly, the Well Plugging Account which funds DEP's oil and gas management program will receive \$5 million annually from the proposed severance tax.

The governor also proposes to restore \$316,000 of Gov. Corbett's 54 percent, or \$500,000, cut to the Delaware River Basin Commission. Additionally, he proposes flat funding for the conservation districts, in addition to their share of the unconventional gas well impact fee, which will remain in place for 2015 under the governor's natural gas severance tax proposal.

Conservation and Natural Resources

Shortly after taking office, Gov. Wolf signed an executive order rescinding former Gov. Corbett's "non-surface impact leasing" plan in state parks and forests and reestablished a moratorium on oil and gas development in state parks and state forest lands owned or managed by the Department of Conservation and Natural Resources (DCNR).

Over his four-year term, former Gov. Corbett cut state General Fund support for DCNR by 82 percent, or \$66.4 million, and backfilled it with increased appropriations from the Oil and Gas Lease Fund (OGLF). In 2013/14 and 2014/15, OGLF revenues comprised one-third of DCNR's total budget compared with just nine percent in 2010/11. Gov. Wolf's proposal takes significant steps to reverse this trend by shifting funding for DCNR back to the state's General Fund and away from the OGLF. The governor's proposed budget includes a \$21.9 million, or 240 percent, increase for the appropriations that were heavily subsidized by OGLF revenues under Gov. Corbett.

The 2015/16 budget proposal relies on \$117 million in revenues from the OGLF to help fund DCNR, which is a \$5.5 million decrease from the \$122.5 million provided by the OGLF to DCNR in 2014/15. This marks the first time since 2006/07, before the Marcellus Shale natural gas boom, that the funds transferred or appropriated from the OGLF to DCNR decreased compared with the previous year.

Gov. Wolf's 2015/16 budget proposal does not include funding for Heritage and Other Parks, which has typically been a legislative addition. Heritage and Other Parks received \$2.25 million in 2014/15.

PENNVEST

Gov. Wolf's 2015/16 budget proposal seeks to leverage \$500 million through PENNVEST bonds to address Pennsylvania's deteriorating municipal water and sewer infrastructure. In 2008, Gov. Rendell signed an executive order creating the Sustainable Water Infrastructure Task Force to provide recommendations for addressing the deterioration of Pennsylvania's drinking water and wastewater systems. In its November 2008 report, the task force estimated the commonwealth would need to invest \$113.6 billion over the next 20 years to upgrade, operate, and maintain Pennsylvania's existing water infrastructure: \$25 billion for wastewater systems; \$11.5 billion for drinking water systems and \$77.1 billion for operation and maintenance, replacement and repair, and debt retirement. Gov. Wolf's proposed investment will simultaneously protect the environment, improve the health of Pennsylvania's citizens, and provide opportunities for economic growth and jobs.

Other Areas

Agriculture

Gov. Wolf proposes to increase funding for the Department of Agriculture by nearly \$2.6 million, or 2 percent, in 2015/16 for a total of \$129.5 million.

The governor proposes a significant increase in the **State Food Purchase Program**, which helps to fund food banks in every county. The 2015/16 budget proposes to increase funding for this program by \$3 million, or 16.6 percent, for a total of \$20.3 million.

As is often the case, the governor's proposal eliminates several programs of importance to the legislature: Agricultural Excellence; Agricultural Research; Agricultural Promotion, Education and Exports; Hardwoods Research and Promotion; Livestock Show; Open Dairy Show; Food Marketing and Research; and PA Preferred Program Trademark Licensing.

Community & Economic Development

Gov. Wolf's 2015/16 budget proposal increases funding for the four programs – **Industrial Resource Centers, Small Business Development Centers, Local Development Districts and Industrial Development Assistance** – that were consolidated into the Partnerships for Regional Economic Performance (PREP) appropriation under the previous administration. The Industrial Resource Centers, which previously received roughly half of the PREP appropriation, will no longer be funded through PREP. The PREP appropriation will continue to receive \$11.8 million as it has over the past four years; however, this total will be split among three programs instead of four resulting in almost twice as much funding for the remaining programs. The Industrial Resource Centers will be funded as part of a \$12 million initiative that pairs the state's manufacturing sector with the state's research universities to advance manufacturing in Pennsylvania.

Furthermore, the governor proposes a \$5 million tax credit, funded by eliminating other underperforming or underutilized tax credits, for manufacturing companies that create good-paying, full-time jobs with health benefits.

Gov. Wolf also proposes to launch a **\$675 million bond program** to support economic development initiatives. A portion of the revenue from the proposed severance tax will help pay debt service for this program. This new bond program would:

- Start to repay Gov. Corbett's \$180 million raid of the Machinery and Equipment Loan Fund (MELF) and the Small Business First Fund (SBF) in the 2014/15 budget. The proposal allots

\$100 million to the **Pennsylvania Industrial Development Authority (PIDA)**, the authority which MELF and SBF were folded into under Act 161 of 2014, to assist manufacturers and small businesses in growing their businesses;

- Invest an additional \$250 million in the **Business in Our Sites** program to grow and relocate businesses in the commonwealth;
- Ensure Pennsylvania remains competitive in the 21st century economy by providing \$100 million in technology investments; and
- Provide \$225 million for an **Energy Investment initiative**, including clean energy investments and a “last mile” pipeline program to make natural gas directly available to the manufacturing industry.

Gov. Wolf’s 2015/16 budget proposal restores \$15 million of Gov. Corbett’s \$21 million (77.5 percent) cut to the **Keystone Communities program, which includes the Main Street and Elm Street programs**. Additionally, the governor’s proposed budget includes \$15 million for the **PA Housing Finance Authority** to implement a **Mixed Use Development Program** aimed to increase affordable housing and commercial corridor development.

The governor also proposes to more than double the **Pennsylvania First** appropriation from \$20 million in 2014/15 to \$45 million in 2015/16. The PA First program, which received \$70 million in 2007/08, offers grants for job creation, infrastructure projects, and workforce development through the WEDnet program. This investment will create an estimated 11,000 new jobs and preserve 40,000 existing jobs.

Gov. Wolf proposes to increase funding for the **Infrastructure and Facilities Improvement Program (IFIP)** by \$11 million, or 58 percent. IFIP uses future state tax revenue increments to provide grants to help pay debt service for large construction projects (e.g. hospitals, convention centers, hotels, large retail projects). Gov. Wolf proposes a new \$4 million **Public Television Technology** appropriation and \$775,000 for **Base Realignment and Closure**, which has not received funding for six years.

Labor & Industry

Gov. Wolf submits three major ideas as part of the Department of Labor and Industry’s budget:

- His budget proposes to expand services for Pennsylvanians with disabilities who want to work and live independently by increasing funding for the **Office of Vocational Rehabilitation** by \$5 million (allowing the commonwealth to access additional federal matching dollars) and by including an additional \$406,000 for **Centers for Independent Living**.
- Second, the budget proposal recommends an additional \$9.8 million for **Industry Partnerships**, to allow groups of employers in the same industry to develop training programs to meet their workforce needs.
- Finally, although not an appropriation, Gov. Wolf proposes to **increase the minimum wage** from \$7.25 to \$10.10 per hour and index it to inflation to maintain purchasing power going forward.

The budget proposes level funding for Supported Employment and the two assistive technology appropriations, while eliminating funding for Keystone Works and New Choices/New Options.

Complement

Although Gov. Wolf plans to increase the total number of state employees by a net 109 full-time equivalent authorized positions in 2015/16; however, five agencies will need to cut positions.

Under the governor's proposal, the agencies receiving notable increases include:

- Department of Corrections for enhanced treatment of inmates with serious mental illness (64 positions);
- Board of Probation and Parole for parole supervision and review (30 positions); and
- Department of Environmental Protection for oil and gas related enforcement (50 positions).

Efficiencies

The Governor's Office of Transformation, Innovation, Management and Efficiency (GO-TIME) will work to achieve \$150 million in savings in 2015/16. To date, the administration has identified opportunities to save \$109 million by applying commercial best practices to state contracts; reintroducing reverse auctions; modernizing the technology used to manage the \$1 billion in building and infrastructure projects administered by the Department of General Services; and streamlining and consolidating administrative functions across departments.

Tax & Revenue Changes

The governor proposes major property tax relief paid for with an offsetting increase in the Personal Income Tax and significant tax relief for many businesses that pay the Corporate Net Income Tax and the Capital Stock and Franchise Tax. See the table on Page 25 for more details.

Local Property Tax and Wage Tax Relief

Gov. Wolf proposes significant local tax relief worth approximately \$3.8 billion annually, beginning in 2016/17 including more than \$600 million provided under current law, for homeowners, renters, individuals and businesses in the form of property tax relief, wage tax relief and expanded rent rebates.

The proposal funds the additional local tax relief with the new revenue generated by an increase in the Personal Income Tax. Pennsylvania funds property and wage tax relief under current law with casino gaming and lottery funds.

Under the governor's proposal:

- **Property tax relief** is driven out to homeowners according to the formulas used to distribute the homestead exemption under current law related to casino gaming (Title 4). **The average homeowner will receive a 50 percent cut in property taxes and 270,000 senior households (nearly 30 percent) will have their school property taxes eliminated, according to the Wolf administration.** The tax reduction will target greater relief to high-tax, high poverty communities.
- **Rent rebates** are distributed through the current Property Tax/Rent Rebate program by increasing the income limits for renters from \$15,000 to \$50,000. All age limitations would be removed for renters, and the maximum rebate would be \$500 per household.
- **Millage rates will be reduced** in school districts where the property tax relief exceeds the constitutionally allowed maximum (homestead exemptions are capped under the constitution at 50 percent of the median home value). If the maximum amount of constitutionally allowed property tax relief is distributed, then school districts would reduce their property tax millage rates to match the additional revenue received from the property tax relief. This would benefit all school district property owners, including businesses.

Severance Tax

Gov. Wolf's 2015/16 budget proposal calls for a severance tax on natural gas to primarily help fund schools, regulate the industry and invest in economic and energy development initiatives. The governor proposes the same tax rate as West Virginia: 5 percent on the value of the gas extracted plus 4.7 cents per thousand cubic feet of gas extracted. Gov. Wolf estimates that this severance tax, with an effective date of Jan. 1, 2016, will generate: \$165.7 million in 2015/16; \$1 billion in 2016/17 and \$1.1 billion in 2017/18. While the vast majority of the proposed severance tax revenues will be used to fund schools, the following transfers are also included in the governor's proposal:

- \$10 million is transferred to the Department of Environmental Protection to support additional oil and gas related enforcement.
- Recipients of the current impact fee will receive \$225 million from the severance tax revenues each year beginning in 2016/17 to replace the impact fee.
- Beginning in 2016/17 and thereafter, an annual amount (which administration sources estimate to be \$55 million) is transferred to pay debt service on the \$675 million economic growth bonds.

Personal Income Tax (PIT)

The governor's budget proposal increases the state's Personal Income Tax rate from 3.07 percent to 3.7 percent beginning July 1, 2015. This means taxpayers would pay an effective rate of 3.39 percent for 2015 (3.07 percent for the first half of the year and 3.7 percent for the second half), and taxpayers would pay the full 3.7 percent rate on taxable income beginning in 2016. The revenue generated from the increased portion of 0.63 percent of income is specifically earmarked for property tax relief and wage tax relief.

Proposed Increase in PIT Poverty Provision

The governor proposes to expand the special poverty provisions for tax forgiveness by increasing the eligibility income limit for claimants and first dependents (spouses) from \$6,500 to \$8,700. The income limits for claimants and first dependents have not increased since 1998, and the income limits for dependent children have not increased since 2004. Under the proposal, a married couple with two children will pay no PIT if their eligible household income is \$36,400, compared with \$32,000 under current law. The total income limit for a household increases with the number of dependent children, and partial tax forgiveness is available on a sliding scale for slightly higher income levels. For more information on the current provisions see the committee's [Tax Forgiveness for Personal Income Primer](#).

Many of Pennsylvania's senior citizens also benefit from tax forgiveness. Pennsylvania does not tax most retirement or pension income, including Social Security. Therefore, most retired seniors do not pay PIT, provided their interest, dividends and other earnings or taxable investments do not exceed \$6,500 for an individual or \$13,000 for a married couple.

Tax Forgiveness for Low Income - A History					
Tax Year	ELIGIBILITY INCOME ALLOWANCE			100% TAX FORGIVENESS	
	Claimant	First Dependent (Spouse)	Each Additional Dependent	Two Parent Family with Two Children	One Parent Family with Two Children
Proposed	\$8,700	\$8,700	\$9,500	\$36,400	\$27,700
2004 - 2014	\$6,500	\$6,500	\$9,500	\$32,000	\$25,500
2003	\$6,500	\$6,500	\$9,000	\$31,000	\$24,500
2002	\$6,500	\$6,500	\$9,000	\$31,000	\$24,500
2001	\$6,500	\$6,500	\$8,500	\$30,000	\$23,500
2000	\$6,500	\$6,500	\$7,500	\$28,000	\$21,500
1999	\$6,500	\$6,500	\$6,500	\$26,000	\$19,500
1998	\$6,500	\$6,500	\$6,000	\$25,000	\$19,000

The following table shows the impact of the proposed PIT rate increase for various income levels. The impact of this increase on the state level would be partially offset by the increased federal tax deduction the taxpayer could claim for state income taxes on the federal income tax return. The median household income in Pennsylvania is \$52,500 (*Source: U.S. Census Bureau, 2009-2013 5-Year American Community Survey*).

Impact of PIT Increase				
Income	Current PIT paid at 3.07%	PIT liability at 3.7% per Year	Additional PIT per Year	Additional PIT per Biweekly Paycheck
\$ 20,000	\$ 614	\$ 740	\$ 126	\$ 4.85
\$ 40,000	\$ 1,228	\$ 1,480	\$ 252	\$ 9.69
\$ 52,500	\$ 1,612	\$ 1,943	\$ 331	\$ 12.72
\$ 60,000	\$ 1,842	\$ 2,220	\$ 378	\$ 14.54
\$ 80,000	\$ 2,456	\$ 2,960	\$ 504	\$ 19.38
\$ 100,000	\$ 3,070	\$ 3,700	\$ 630	\$ 24.23
\$ 150,000	\$ 4,605	\$ 5,550	\$ 945	\$ 36.35

Sales and Use Tax

The budget proposes to increase the Sales and Use Tax by 0.6 percent, from 6.0 percent to 6.6 percent, and expand the tax to include a variety of new items and services beginning Jan. 1, 2016.

Gov. Wolf proposes to expand the sales and use tax to include 45 items and services that are currently not subject to the tax, except for the items indicated in the chart on the next page. More detail on the proposed list of exemption eliminations will be provided as information becomes available at a later date.

Sales Tax Exemptions that Remain in Effect	
Food	Trade-In Value
Gasoline and Motor Fuels (MLF)	Storage
Physician & dental services	Isolated Sales
Hospitals	Common Carriers
Clothing and Footwear	Water and Sewage Services
Prescription Drugs and Orthopedic Equipment	Exempt Governmental Units
Manufacturing Exemption (Manufacture and Processing)	Tuition (college, vocational training & instruction)
Residential Utilities: Telephone, Fuel Oil/Gas, Electric	Liquor or Malt Beverage Purchased From Retail Dispenser
Purely Public Charities: Charitable Org; Religious Org; Health and Social Assistance Org; Non-Profit Educational Institutions	

Currently, 69 items (tangible personal property or circumstantial transactions) are specifically excluded from the sales tax. Exclusions for items that are commonly considered to be necessities, such as food and clothing, alleviate the regressive nature of the sales tax. Additionally, all services are exempt from sales tax, except for a few that are specifically enumerated. See Pages D46 through D68 of the governor’s executive budget for a list of items that are exempt or excluded from the sales and use tax under current law.

The governor also proposes to cap the current one percent vendor discount for timely remittances at \$25 for monthly filers, \$75 for quarterly filers and \$150 for semi-annual filers.

Tobacco Taxes

The budget proposes to increase the cigarette tax by \$1 per pack, from \$1.60 to \$2.60 per pack. In addition to the cigarette tax, the governor proposes a tax on other tobacco products including large cigars, roll-your-own tobacco, smokeless tobacco and e-cigarettes, effective Oct. 1, 2015. The proposed rate is 40 percent of the wholesale price, which the governor estimates to be equivalent to the tax on cigarettes.

Liquor System Modernization

Rather than selling the liquor system for short-term gain and lose a dependable long-term revenue stream, the governor proposes to modernize the wine and spirits system with reforms such as adding Sunday hours, identifying the most convenient locations for customers and competitive pricing. This will improve customer convenience and increase current profits available to the General Fund. The governor proposes to allocate new revenue from modernization to help school districts and the state meet their future pension obligations. This proposal assumes \$80 million in additional revenue in 2015/16 and transfers of \$185 million annually beginning in 2017/18.

Corporate Net Income Tax

Gov. Wolf proposes to change the corporate net income tax (CNI) by: lowering the tax rate from 9.99 percent to 4.99 percent over three years; instituting mandatory combined reporting and updating the net operating loss cap. The net effect is a revenue loss to the state and a tax reduction to many corporations.

- CNI Rate Reduction – 5.99 percent in tax year 2016; 5.49 percent in tax year 2017; and 4.99 percent in tax year 2018.

- Combined Reporting – Current tax law only allows for separate accounting, which means that the profits of subsidiaries are not reported or taxed in Pennsylvania – this is commonly referred to as the “Delaware loophole”. Combined reporting would require multi-state corporations to add together the profits of all the associated subsidiaries and parent corporations before calculating the amount apportioned to Pennsylvania. Currently, 28 states use combined reporting to calculate corporate taxes.
- CNI Net Operating Loss Cap – The budget proposes to decrease the cap on net operating losses from \$5 million (or 30 percent of income) to \$3 million (or 12.5 percent of income). This change affects approximately 290 businesses.

Capital Stock and Franchise Tax

The governor’s budget includes eliminating the Capital Stock and Franchise Tax in 2016, which follows the current phase-out schedule.

Bank Shares Tax

The budget assumes that legislation is enacted that adjusts the Bank Shares Tax to recoup a shortfall in revenue resulting from tax changes enacted in 2013 (Act 52), changes that were intended to be revenue neutral. The Department of Revenue has issued temporary bulletins attempting to recoup lost revenue; however, it is questionable whether this will withstand a court challenge. The proposal increases the rate from 0.89 percent of the book value of shares to 1.25 percent and is retroactive to tax year 2014, which would result in a lump sum payment due in 2015/16.

Tax and Revenue Package Highlights <i>(\$ Amounts in Millions)</i>		
Tax Type		Impact
Property and Wage Tax Relief Including Rent Rebate Program Expansion	\$ (3,800.0)	Distributions of property tax relief to begin in 2016/17. Renters with household income up to \$50,000 will receive rebates capped at \$500.
Tax Type	2015/16	Impact
Corporate Net Income Tax Rate Decrease with Combined Reporting	\$ (249.3)	Rate will reduce to 5.99% 1/1/2016; 5.49% 1/1/2017; and 4.99% 1/1/2018. Net savings to businesses will be more than \$850 million per year when fully phased-in. Also includes a change to the net operating loss cap.
Capital Stock and Franchise Tax Current law	\$ -	Eliminated beginning Jan. 1, 2016
Severance Tax 5% of value plus \$0.047 per Mcf	\$ 165.7	\$1 billion expected in 2016/17; \$225 million is transferred to replace impact fee beginning in 2016/17.
Personal Income Tax Increase from 3.07% to 3.7%	\$ 2,376.7	Proceeds distributed as property tax relief.
Personal Income Tax Forgiveness to 150% of Poverty	\$ (90.2)	A family of four with income of \$36,400 will pay no income tax.
Personal Income Tax PA lottery winnings at 3.7%	\$ 15.7	
Sales and Use Tax Increase from 6% to 6.6% and base expansion	\$ 1,554.3	Base will expand to include services and items currently exempted. Exemptions will remain for food, clothing and prescription drugs. Also includes capping the sales tax vendor discount.
Cigarette Tax Increase state rate by \$1.00 per pack	\$ 358.4	Increase from \$1.60 per pack to \$2.60 per pack.
Other Tobacco Products 40% of wholesale price	\$ 84.1	Includes cigars, smokeless tobacco, roll-your-own and e-cigarettes.
Bank Shares Tax Revenue Neutral Rate at 1.25%	\$ 339.2	Retroactive fix to recoup revenue back to 2014. Rate going forward will increase from 0.89% to 1.25%.
Tax Credit Elimination of Promoting Employment Across PA	\$ 5.0	
Tax Credit Made in Pennsylvania Tax Credit	\$ (5.0)	Distributed to manufacturing companies for up to 5% of new taxable payroll for companies that increase their payroll by more than \$1 million in a year.
	\$ 4,554.6	

*Tax revenue estimates are net of refunds of \$108.1 million (total revenue modifications before refunds is \$4.66 billion in 2015/16)