How Tax Cuts for the Rich Trumped Public Investments: The West Virginia Fiscal Year 2024 Budget

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Overview

During the 2023 West Virginia legislative session, lawmakers had the opportunity to use available revenues to address longstanding needs like ensuring PEIA and Medicaid solvency, filling crisis-level staffing vacancies across state agencies, or increasing investments in neglected areas like higher education and child care. But instead, the FY 2024 budget debate was dominated by creating space for tax cuts that overwhelmingly benefit the wealthy and hamstring future budgets for years to come. The FY 2024 budget once again lacked a six-year plan, leaving the impact of the tax cuts on future budgets unclear, and questions about potential future budget deficits unanswered.

Key Findings

- The final FY 2024 budget is $282.8 million above the final enrolled FY 2023 budget, with most of the increase coming from a $2,300 flat public employee pay raise.
- Once again, artificially low revenue estimates were used to manufacture large surpluses to make tax cuts appear more affordable. This resulted in temporary surplus funds that will no longer be available once tax cuts are enacted going toward funding ongoing needs as the base budget shrunk.
- Expensive tax cuts enacted by the Legislature will hurt the state over time, costing nearly $818 million in FY 2025 with triggers that seek to eventually eliminate the personal income tax entirely, at an annual cost of over $2 billion, or about 40 percent of the state's general revenue budget. The personal income tax is the state's only progressive tax and its single largest source of general revenue.
- The state budget was already shrinking before the 2023 tax cuts, leaving needs unmet and future budgets vulnerable to more painful cuts. The final FY 2024 general revenue budget is $591 million less than the FY 2019 budget after adjusting for inflation.

Final Enrolled Budget

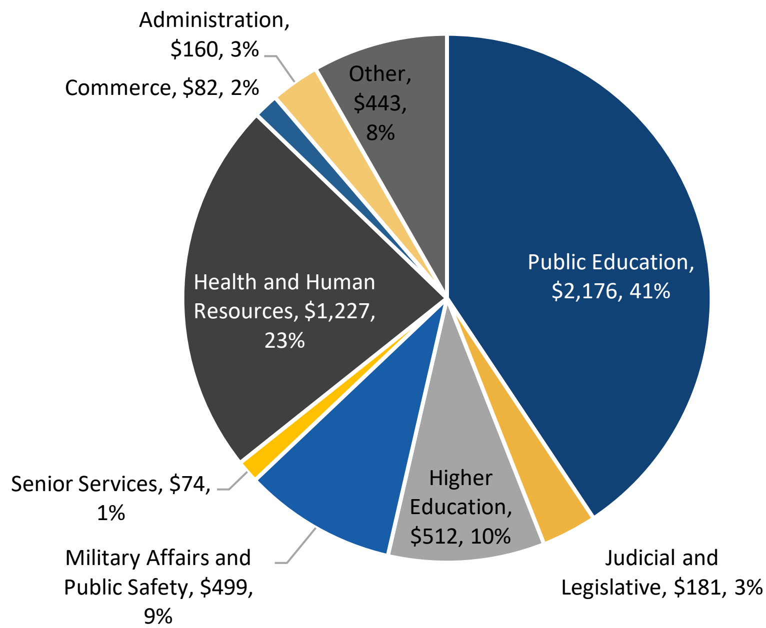
The FY 2024 final enrolled base budget, which includes general revenue and lottery appropriations, totaled $5.35 billion (Figure 1), an increase of $282.8 million over the FY 2023 budget. Much of that increase is from the public employee pay raise, which costs an estimated $120 million. Other notable increases include new state spending for the Public Employees Insurance Agency (PEIA) resulting from SB 268 and for establishment of the Third Grade Success Act via HB 3035, which will provide additional support staff for early elementary school teachers and ensure students are proficient in reading and math by third grade. [1]

[1] WVCBP analysis of House Bill 2024, West Virginia Legislature, 2023 Regular Session.

Figure 1

West Virginia's FY 2024 Base Budget Appropriations

FY 2024 appropriations from general revenue, lottery, and excess lottery (millions)



Source: FY 2024 Enrolled Budget

After several years of flat budgets, the FY 2024 budget fails to even keep pace with inflation, much less leave space for many new investments, essentially resulting in cuts by attrition. This has resulted in public services and agencies being able to do less over time and driving some of the crises that have recently emerged. After adjusting for inflation, the FY 2024 general revenue budget is $591 million less than the FY 2019 budget.[2] One example of the erosion of public investments due to flat budgets can be seen in higher education. After adjusting for inflation, general revenue allocations for higher education have shrunk by 25 percent since 2013 and have declined overall as a share of the state budget, shrinking higher education as a priority as other programs and even tax cuts have taken precedence. Over that same period, tuition has skyrocketed by 57.7 percent at four-year institutions and 81.2 percent at two-year institutions. Enrollment has also declined significantly over the same period, likely due to the dramatic cost increases on students leading to unaffordability. [3]

Low Revenue Estimates Continue to Influence Budget Narrative

As of March 2023, West Virginia's FY 2023 budget is running a healthy surplus, with revenue collections exceeding estimates by $1.27 billion. However, much of that revenue surplus is due to artificially low revenue estimates from the past three fiscal years. Despite the state experiencing a slow and steady recovery since the pandemic, revenue estimates have been consistently set below actual collections from the previous year,

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[2] WVCBP analysis of West Virginia Budget Office and Bureau for Labor Statistics data.

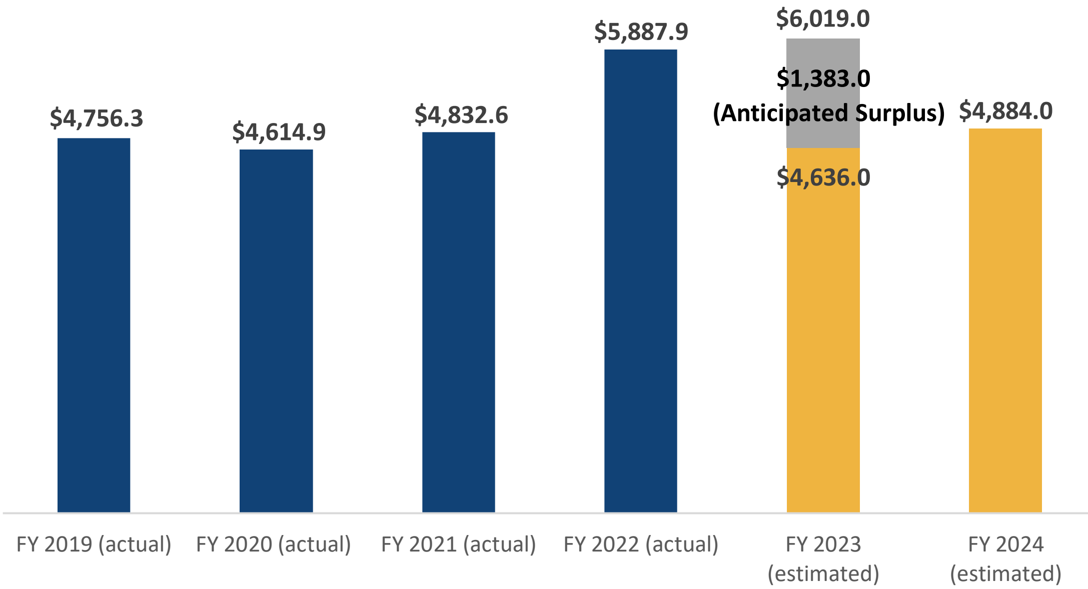
[3] Kelly Allen, "State Higher Education Investments Down 25 Percent Over Last Decade, Could Worsen with Amendment 2," West Virginia Center on Budget and Policy, October 20, 2022, https://wvpolicy.org/state-higher-education-investments-down-25-percent-over-last-decade-could-worsen-with-amendment-2/.

including years strongly negatively impacted by the pandemic. The revenue estimate for FY 2024 is only $248 million above the estimate for FY 2023, despite FY 2023 already running a $1.27 billion surplus (Figure 2).[4]

Figure 2

Low Revenue Estimates Help Manufacture Surpluses

West Virginia general revenue collections, FY 2019 – FY 2024, actual and estimated (millions)



Source: WVCBP analysis of WV State Budget Office data
Note: FY 2020 and FY 2021 adjusted to correct for deferred collections and CARES Act reimbursements

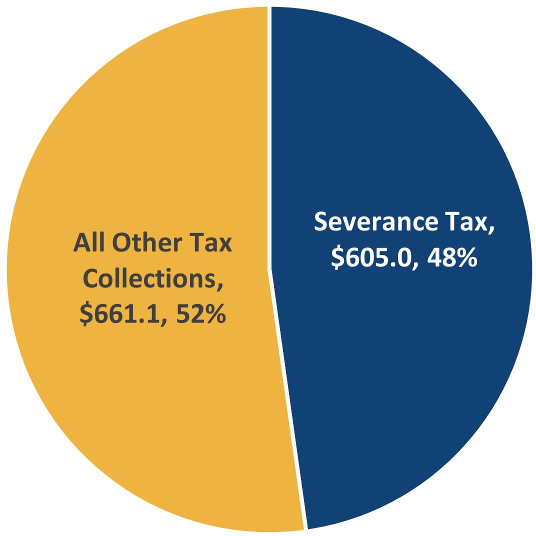
However, nearly half of the “surplus” is from severance tax collections above estimates (Figure 3), which are the result of high energy prices due to factors outside of West Virginia’s control and are expected to decline in the coming years as natural gas prices decline.[5]

[4] WVCBP analysis of Budget Office and Senate Committee on Finance data.
[5] Kelly Allen and Sean O’Leary, “Governor Justice Adjusts Revenue Estimates Upward as Natural Gas Prices Drop Dramatically,” West Virginia Center on Budget and Policy, March 3, 2023, https://wvpolicy.org/governor-justice-adjusts-revenue-estimates-upward-as-natural-gas-prices-drop-dramatically.

Figure 3

Nearly Half of FY 2023 "Surplus" Tax Collections are From the Severance Tax

FY 2023 tax collections above estimates by source, July – March (millions)



Source: WVCBP analysis of WV State Budget Office data

While revenue estimates are intended to be knowledgeable forecasts of expected revenues, the Justice Administration has instead admitted to manipulating these estimates to control the size of the budget. Governor Justice's budget official testified in December that revenue estimates are based on "budget needs" rather than the economic outlook. Meanwhile, Governor Justice has repeatedly bragged about four years of flat budgets, driven by flat revenue estimates, which have directly created the surpluses that were used to make the case for 2023's tax cuts.[6]

Years of flat revenue estimates have also prevented needed spending. West Virginia's executive-controlled revenue estimating process is a fairly unique one, with most states merging input from the legislature, the executive, and outside experts rather than placing the responsibility solely with the executive.[7] Under West Virginia's flawed system, legislators are bound by the governor's revenue estimates and are unable to appropriate anything above it, aside from utilizing "back of the budget" surplus allocations which are only funded if surpluses come in and thus cannot be built into agency or program budgets by nature. This has essentially meant that for several years, lawmakers could approve very little needed new spending without raising taxes or cutting other spending. This budgetary restraint is directly responsible for multiple crises which have emerged due to lack of investments, including looming PEIA and Medicaid shortfalls, public agency employee vacancies, and reductions in child care subsidies.

[6] Testimony in front of the West Virginia Legislature's Joint Standing Committee on Finance, meeting held Monday, December 5, 2022 at 9:00am.

[7] Elizabeth McNichol, "Improving State Revenue Forecasting: Best Practices for a More Trusted and Reliable Revenue Estimate," Center on Budget and Policy Priorities, September 2014, https://www.cbpp.org/research/state-budget-and-tax/improving-state-revenue-forecasting-best-practices-for-a-more-trusted.

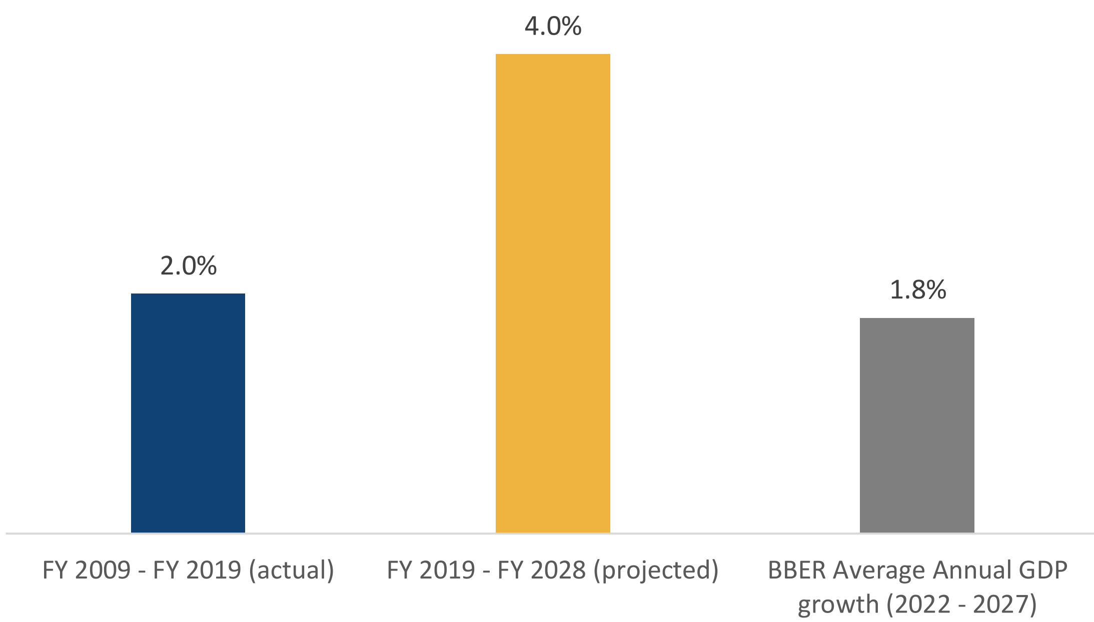
Evidence of the gaming of the revenue estimate process could be readily found during the 2023 legislative session. Initially Governor Justice sent the Legislature a FY 2024 revenue estimate of $4.884 billion. Once a deal was reached on tax cuts, he sent a revenue estimate adjustment letter, revising his revenue projections upward by $850 million, nearly the exact cost of the proposed tax cuts.[8] Essentially, he would not give lawmakers the authority to use that revenue for anything but tax cuts, as he withheld it until they agreed to his tax plan. That revenue simply would not have been made available to lawmakers to allocate to PEIA, economic development, or any other budget needs—only to fund the Governor's preferred tax cuts.

While current and past revenue estimates were intentionally low-balled to make room for tax cuts, future revenue estimates are very optimistic, showing revenue growth doubling over its pre-pandemic rate. These optimistic revenue projections are seemingly designed to make the tax cuts appear more affordable, despite little evidence that the state's economy will actually grow at the rate needed to support that revenue growth (Figure 4).

Figure 4

Optimistic Revenue Estimates Make Tax Cuts Appear Affordable

Average annual general revenue growth (FY 2009 – FY 2019, actual) and (FY 2019 – FY 2028, projected), and projected average annual GDP growth from WVU Bureau of Business and Economic Research



Source: WVCBP analysis of State Budget Office data and WVU BBER 2023 WV Economic Outlook Report

[8] Kelly Allen and Sean O'Leary, "Governor Justice Adjusts Revenue Estimates Upward as Natural Gas Prices Drop Dramatically," West Virginia Center on Budget and Policy, March 3, 2023, https://wvpolicy.org/governor-justice-adjusts-revenue-estimates-upward-as-natural-gas-prices-drop-dramatically/.

Surplus Funds Largely Held for Tax Cuts

During the 2023 legislative session, both chambers focused on the state's revenue "surplus" as a justification for tax cuts, despite the clear need for new spending after four years of austerity forced by flat budgets. The final FY 2024 general revenue budget is 16.2 percent less than the FY 2019 general revenue budget after adjusting for inflation. In addition to leaving very little room for new spending, this has also resulted in increased austerity due to agencies and programs having to make do with less.

Nowhere was this more evident than in the PEIA changes made via SB 268. With artificially low revenue estimates forcing another essentially flat budget, lawmakers were unable to use general revenue appropriations to significantly increase state investments in the insurance program. Facing a $376 million shortfall by 2027, major changes were made to PEIA. One positive change was increasing the reimbursement rate for inpatient hospitalizations to 110 percent of Medicare reimbursement in order to keep the provider network solvent. Other changes will increase costs for the spouses of PEIA plan participants who have health insurance available to them from their employer (regardless of the quality of that coverage), as well as a change in coverage for PEIA enrollees who see medical providers out-of-state. The largest change included in SB 268 requires the plan to enforce a strict 80/20 employer/employee coverage split, which will result in a 24.2 percent premium increase for state employees in July 2023, followed by expected 10 percent premium increases each of the next three years.[9] As the employer, the state will also incur further costs related to the premium increase, with an additional $108 million projected to be needed in FY 2024 alone, followed by 10 percent premium increases each of the next three years, setting up potential future budget challenges as state revenues decline with the phase-in of enacted tax cuts.

Lawmakers also ended the legislative session without addressing many of their own stated priorities including addressing the state of emergency in West Virginia's correctional facilities or pursuing supports for families and children like home visitation, paid parental leave, and child care affordability. Each of these priorities would have required ongoing budget spending, which was largely unavailable with such tremendous focus on tax cuts.[10]

Without much new space for spending beyond public employee pay raises, increased state PEIA costs, and the Third Grade Success Act, the Legislature appropriated $1.17 billion from the anticipated FY 2023 surplus into the FY 2024 budget. The largest appropriated surplus item is $400 million for the Personal Income Tax Reserve Fund, to help pay for the first year of the personal income and personal property tax cut passed by the Legislature. When the first phase of the income tax cuts is enacted, the cost is expected to be nearly $818 million per year. The ultimate cost of the bill could potentially grow to over $2 billion annually, as triggers in the plan are set to fully eliminate the income tax, the state's only progressive tax and its single largest source of general revenue.

The second biggest use of the FY 2023 surplus in FY 2024 is $282 million being sent to the Governor's Civil Contingency Fund to help pay for deferred maintenance for higher education and correctional facilities—another consequence of previous flat budgets. There are also millions dedicated to the School Building Authority, funded with surplus funds rather than base budget appropriations (Figure 5). Using surplus funds for permanent, ongoing costs like maintenance is the result of regularly underfunding state programs and kicking the can down the road on budget obligations.

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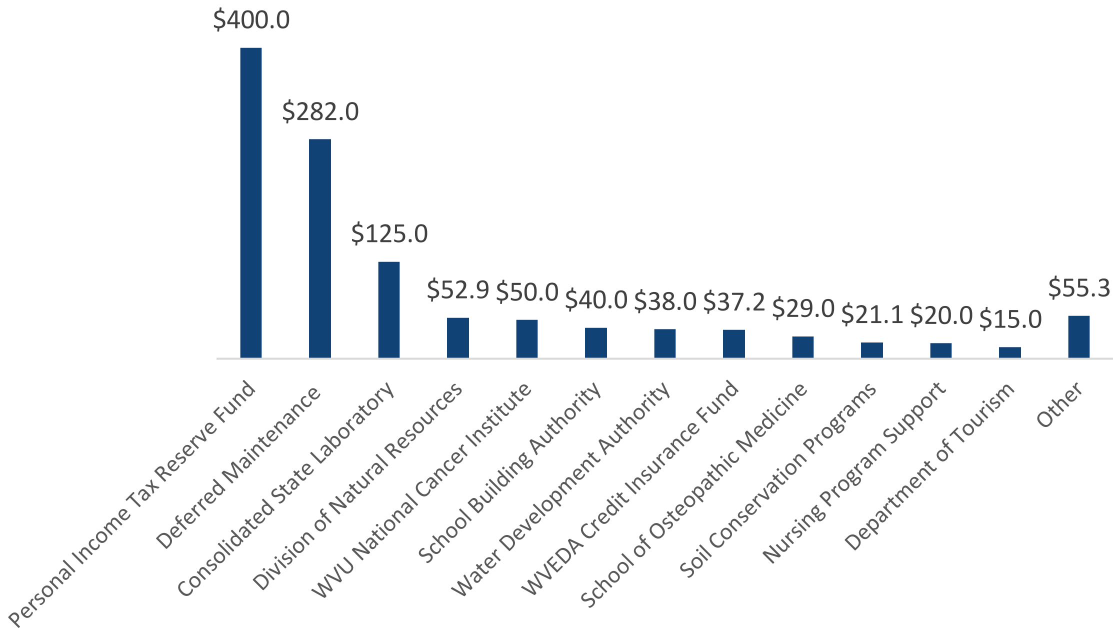
[9] PEIA Finance Board Meeting Presentation, March 30, 2023, https://peia.wv.gov/Forms-Downloads/Documents/Finance_Board/2023%20MAR%2030%20FB%20Presentation%20-%20FINAL.pdf.

[10] West Virginia Center on Budget and Policy, "Passage of HB 2526 Fiscally Reckless, Comes at Cost of Years of Needed Investments," March 7, 2023, https://wvpolicy.org/passage-of-hb-2526-fiscally-reckless-comes-at-cost-of-years-of-needed-investments.

Figure 5
Bulk of Surplus Funds Set Aside for Tax Cuts and Deferred Maintenance
FY 2023 general revenue surplus appropriations for FY 2024 (millions)



Source: WV State Budget Office

Of note, these "surpluses" will likely no longer exist in future years as tax cuts are fully implemented and energy prices continue to decline, leading to lower severance tax revenues. As such, surplus funding—which agencies like the Department of Tourism have regularly received in recent years—could soon no longer be available.

Costly Income Tax Cut Will Hurt Over Time

The biggest piece of legislation affecting the budget is HB 2526, a major income tax cut that will cost the state budget hundreds of millions of dollars annually and overwhelmingly benefit the state's wealthiest households and businesses. The legislation also includes a workaround for the tax cuts rejected by voters via Amendment 2 and contains automatic triggering mechanisms that seek to ultimately eliminate the state's personal income tax at the cost of needed budget investments.

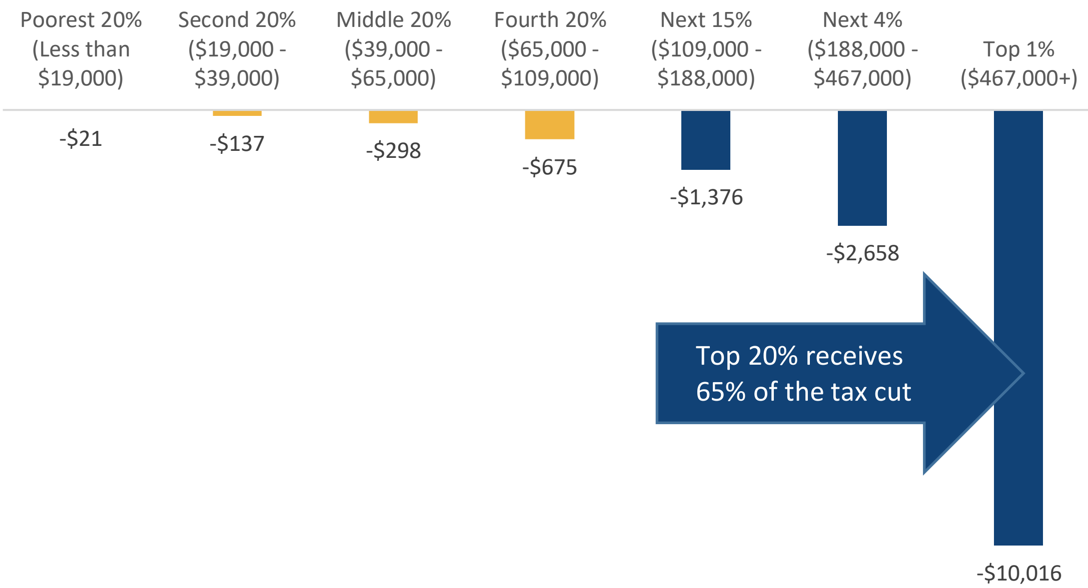
After alarmingly little debate, the enacted tax plan initially cuts the personal income tax by about 21 percent across all brackets. Because the state has marginal, graduated income tax brackets, the across-the-board cuts still overwhelmingly benefit the wealthy, with the top 20 percent of households receiving nearly two out of every three dollars in tax cuts. While the average household will see a tax cut of about $298 annually, or about $11 per biweekly pay period, the tax benefit varies widely by income. The bottom 20 percent of households will receive on average about $21 per year, while the top 1 percent of households will get an average annual tax cut of nearly 500 times as much, at $10,016 per year (Figure 6).[11]

[11] Institute on Taxation and Economic Policy analysis of House Bill 2526, West Virginia Legislature, 2023 Regular Session.

Figure 6

Wealthiest West Virginians Benefit the Most From West Virginia's Income Tax Cut

Average tax change by income groups from reducing state income tax rates to 2.36%, 3.15%, 3.54%, 4.72%, and 5.12% (2023 West Virginia incomes)



Source: Institute on Taxation and Economic Policy and West Virginia Center on Budget and Policy

The legislation also provides rebates for the voter-rejected personal property tax cuts from Amendment 2. Taxpayers will be able to file at income tax time for a rebate of 100 percent of their local taxes paid on personal motor vehicles, and businesses with less than $1 million in aggregate appraised value personal property will be able to file for rebates of 50 percent of taxes paid toward the business personal property tax. The tax department estimates these provisions will cost just under $200 million annually, though it remains to be seen how many businesses will qualify for and claim the credits.[12]

What's more, the legislation contains dangerous automatic triggers to further reduce and ultimately eliminate the personal income tax based on revenue growth, meaning all sources of revenue growth (except the severance tax) above inflation will be diverted to personal income tax cuts rather than future budget needs. Trigger mechanisms that create permanent tax cuts are fiscally irresponsible and inherently flawed. Essentially, HB 2526 forced lawmakers to approve future tax cuts with very little information about future agency budget needs or a complete picture of what the tax cuts will cost once fully phased in. This problem is magnified after three years without a six-year budget outlook from the Justice Administration, which would normally show lawmakers expected budget costs in upcoming years.

Once the first phase of tax cuts is enacted, the initial cost is expected to be nearly $818 million per year, or 15 percent of the general revenue budget. Once the triggers are hit over time, the income tax could be fully eliminated, costing over $2 billion dollars annually and wiping out over 40 percent of the budget—the equivalent of what the state spends in total on K-12 public education, one of the biggest areas of the budget.

[12] Fiscal note for House Bill 2526, West Virginia Legislature, 2023 Regular Session.

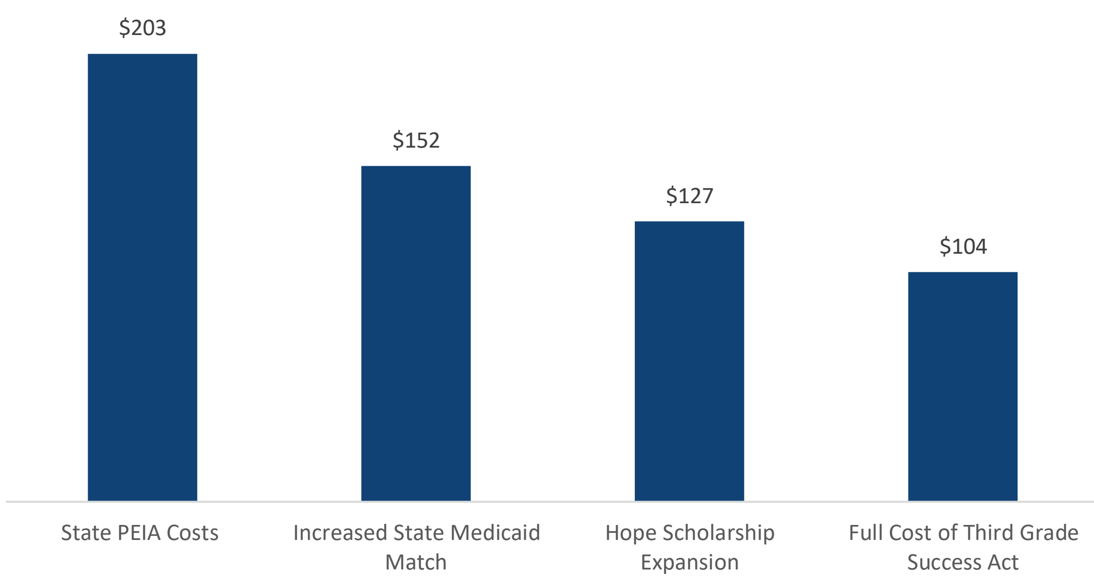
Overall, this legislation is certain to harm low- and middle-income families by reducing the state's ability to invest in current programs and services or to make new needed investments.

Without much debate or a six-year budget plan, lawmakers essentially voted for these major tax changes without any informed idea of what effect they will ultimately have on public services in upcoming years. However, we do know several new costs and programs will have to be incorporated into future budgets, all of which are at risk given this year's tax cuts and future tax cut triggers. New upcoming spending includes the Hope Scholarship expansion, additional employer premiums for PEIA, the full cost of the Third Grade Success Act, and increased state costs for Medicaid (see Figure 7).

Figure 7

New Costs Coming Despite Tax Cuts

New upcoming West Virginia state budget expenditures resulting from already-enacted legislation or required spending, FY 2025 – FY 2027 (millions)



Source: WVCBP analysis of WV State Legislature data

Budget Shrinking Before Tax Cuts

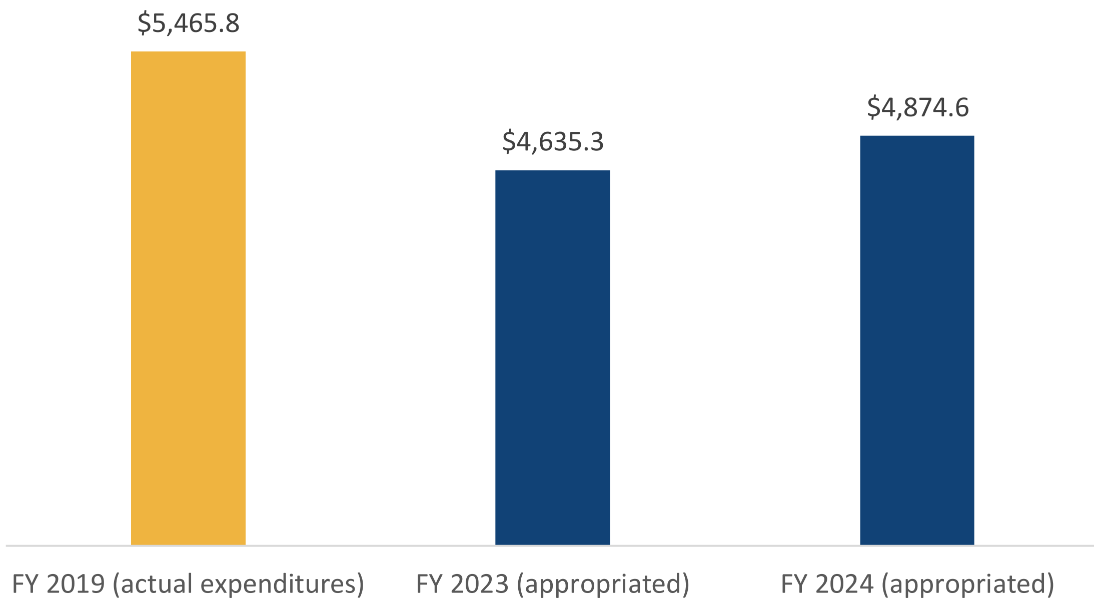
Even before the tax cuts passed during the 2023 legislative session go into effect, West Virginia has seen its budget shrinking over the past several years, resulting in increased needs going unmet. The FY 2024 budget relies on one-time surplus funds to pay for ongoing needs, including tax cuts. While that may not pose a budgetary issue this year, once the tax cuts are fully phased in, enacted legislation fully hits the general revenue budget, and temporary surpluses come back to earth, the Legislature will face difficult decisions that include making more budget cuts, raising other taxes, or both.

After adjusting for inflation, the final FY 2024 general revenue budget is $591.2 million less than FY 2019's expenditures.

Figure 8

FY 2024 Budget Below Pre-pandemic Appropriations

General revenue expenditures, actual (FY 2019) and proposed (FY 2023 and FY 2024), inflation-adjusted 2023 dollars (millions)



Source: WVCBP analysis of State Budget Office data and Bureau of Labor Statistics data

Flat budgets may have created the illusion that the state has room for tax cuts, but those flat budgets have come at a tremendous cost. The state needs actual investment in order to address needs like the looming PEIA crisis, vacancies throughout state government, paying for Medicaid, as well as longstanding needs related to education and the workforce.

Past tax cuts have failed the state repeatedly, forcing cuts to higher education and a lack of investment in K-12 education, yet the FY 2024 budget is going down the same path. West Virginia has a growing need for additional revenue to make necessary investments, not more ineffective tax cuts that will reduce revenue even further.

Conclusion

Once again, the state punted on future budget questions with the FY 2024 budget. No new investments were made to improve higher education, child care affordability, or the state's deadly correctional facilities, while future budgets and Legislatures were saddled with unaffordable and automatic tax cuts. Relying on temporary surpluses and flat budgets are not the answer, and eventually budget pressure from those tax cuts will result in higher taxes elsewhere or further budget cuts. The state's budget should be used to build a stronger and more equitable economy, while finding ways to meet current and future needs. Overall, the FY 2024 budget and tax cuts are moving the state in the wrong direction.