COMMONWEALTH OF PENNSYLVANIA
HOUSE OF REPRESENTATIVES

APPROPRIATIONS COMMITTEE
BUDGET HEARING

INDEPENDENT FISCAL OFFICE

STATE CAPITOL
HARRISBURG, PENNSYLVANIA
ROOM 140, MAJORITY CAUCUS ROOM

TUESDAY, FEBRUARY 20, 2018
10:00 A.M.

BEFORE:

HONORABLE STANLEY SAYLOR, MAJORITY CHAIRMAN
HONORABLE JOSEPH MARKOSEK, MINORITY CHAIRMAN
HONORABLE KAREN BOBACK
HONORABLE JIM CHRISTIANA
HONORABLE SHERYL DELOZIER
HONORABLE GEORGE DUNBAR
HONORABLE KEITH GREINER
HONORABLE SETH GROVE
HONORABLE DOYLE HEFFLEY
HONORABLE SUE HELM
HONORABLE LEE JAMES
HONORABLE WARREN KAMPF
HONORABLE FRED KELLER
HONORABLE JASON ORTITAY
HONORABLE MIKE PEIFER
HONORABLE MARGUERITE QUINN
HONORABLE BRAD ROAE
HONORABLE JAMIE SANTORA
HONORABLE CURT SONNEY
HONORABLE KEVIN BOYLE
HONORABLE TIM BRIGGS
HONORABLE DONNA BULLOCK
HONORABLE MARY JO DALEY
HONORABLE MARIA DONATUCCI
HONORABLE MARTY FLYNN

BEFORE: *(Continued)*

HONORABLE PATTY KIM
HONORABLE STEPHEN KINSEY
HONORABLE LEANNE KRUEGER-BRANEKY
HONORABLE MIKE O'BRIEN
HONORABLE PETER SCHWEYER

NON-COMMITTEE MEMBERS

HONORABLE FRANK RYAN
HONORABLE CRIS DUSH
HONORABLE KURT MASSER
HONORABLE ELI EVANKOVICH
HONORABLE JAKE WHEATLEY
HONORABLE STEVEN SAMUELSON

COMMITTEE STAFF PRESENT:

DAVID DONLEY
REPUBLICAN EXECUTIVE DIRECTOR
RITCHIE LAFAVER
REPUBLICAN DEPUTY EXECUTIVE DIRECTOR

MIRIAM FOX
DEMOCRATIC EXECUTIVE DIRECTOR
TARA TREES
DEMOCRATIC CHIEF COUNSEL

I N D E X

TESTIFIERS

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SUBMITTED WRITTEN TESTIMONY

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(See submitted written testimony and handouts online.)

P R O C E E D I N G S

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MAJORITY CHAIRMAN SAYLOR: We'll call the Appropriations hearing to order. As we do that, I'm going to ask members of the Appropriations Committee to start off by introducing themselves, and then we'll move into Chairman Markosek's remarks and my own.

So we'll start off -- George.

(Member and staff introductions.)

MAJORITY CHAIRMAN SAYLOR: And I am Chairman of the Appropriations Committee, Stan Saylor, of the 94th District, York County.

I will turn now to Chairman Markosek for his opening comments.

MINORITY CHAIRMAN MARKOSEK: Thank you, Chairman.

We have today the start of the hearing process here with the Director and Deputy Director of the Independent Fiscal Office, aka the IFO.

We're glad you folks are here this morning. Thank you.

It looks like the revenues for the Commonwealth are a little better than they were a year ago, although there's no prediction, so we have to still be careful. But I want to welcome you here today. We certainly look forward to your testimony here, particularly about the revenue and where we're going.

We have some very important issues to talk about, performance-based budgeting and some other things. So we'll look forward to that.

I don't have any questions right now. I'll turn it back to the Chairman.

Thank you.

MAJORITY CHAIRMAN SAYLOR: Thank you, Chairman Markosek.

I want to remind everybody we do have the machines operating. We have them all over the room, so they should be easy to see. Everybody will be given five minutes to speak. When there's 30 seconds left, the yellow button will come on. When your time is up, the red button will come on.

If there is time at the end, we will do a second round of questioning, if so requested by members. So with that, my opening comments today are that we mark the first week of our three bunches of hearings, that Chairman Markosek and I will be under the bright lights and getting a suntan.

While everybody else gets to leave, we

get to sit here, Joe.

But anyhow, traditionally, these hearings have focused on the budget proposals solely for the upcoming fiscal year. However, this year, we wanted to do something a little different. After, I don't know, 50 years of doing the same old things, we wanted to change it.

We wanted to focus on accountability of State tax dollars, our spending, our job creation in Pennsylvania and ensuring that our education system prepares students to succeed in the workplace and in life, reinventing the way government delivers services and improving Pennsylvania communities.

During these three weeks of hearings, we will specifically focus on job creation. And in many of the hearings, we will focus on ways to promote private sector jobs. Several of our hearings will center on reinventing the way government operates.

There will be hearings on the combatting of the scourge of opioid abuse that has been the focus of the media and all of our law enforcement officials and our treatment officials throughout the Commonwealth. The theme of accountability of State spending will run through all the hearings, by the way.

Every year, we hear a case for more spending, but rarely do we drill down to examine if the appropriations in the past have achieved their stated goals. We seem to never look to cull over old programs, instead just build on top of the bureaucracy many times.

Our Committee is charged with being accountable for the hardworking Pennsylvania tax dollars that are spent here. Therefore, we will drill down during these hearings to make sure that we are being proper stewards of the taxpayers' money.

With his fourth budget, the Governor once again is seeking some job-crushing taxes, we believe. In his first budget, he sought a $4.6 billion increase; in his second year, a $2.7 billion tax increase; and in his third year, he sought a billion dollar increase. And in this year, he's seeking $250 million in tax increases.

It's only because what we have been doing here in the General Assembly as Republicans that the Governor has not gotten his large tax increases to fuel State spending. It's time to understand how important it is for us to hold the line on taxes for

Pennsylvania working families, for them to prosper and have money in their pockets.

So going into these budget negotiations, we will continue to hold the line on taxes. We once again will be utilizing the five-minute clock, as I talked about.

And with that, I want to make sure and clear that as we go through this, Chairman Markosek and I expect members to stick with the clock and also testifiers. And we will remind testifiers, every one of them that comes forward, to keep their answers short and concise and to try to directly answer the questions asked by members of the Committee.

With that, I will ask Matt and Mark to please stand and raise your right hands to be sworn in.

(Whereupon, testifiers were sworn in.)

MAJORITY CHAIRMAN SAYLOR: Thank you.

And at this point, we want to also have an understanding we are not having opening comments by the testifiers as we go forward. They have submitted their testimony.

And with that, we'll move forward for the first question, coming from Representative Helm.

REPRESENTATIVE HELM: Thank you, Mr. Chairman.

I would like to talk a little bit about the employment reports. The Labor & Industry Employment Report from January 19th, 2018 shows that PA's employment level fell by 10,000. And our civilian labor declined by 62,000 individuals between December of 2016 and December of 2017.

The Report also shows for the same time period that Pa gained 78,400 non-farm jobs.

Can you walk me through this discrepancy?

And how does the State lose employment but gain non-farm jobs?

Basically, what does this mean for our economy?

But just tell me how that differs.

DIRECTOR KNITTEL: Sure. I can't explain the discrepancy straightforward, but I can say last year, as you noted, on an average basis, year over year, we did increase the net jobs by 66,000. So we took an average from January through December. That was very strong job gains in the Commonwealth.

I will note, going forward there will be what we call a rebenchmark that will occur next month in March, and those numbers will be revised.

So I would just draw caution on the numbers we're seeing currently, whether they will hold up. They are still preliminary. And based on the rebenchmark that will be released next month, they could change considerably.

To your other point about the declining workforce and one of the reasons the unemployment rate is low is because the demographics in Pennsylvania, the working age population is actually contracting right now. And so we can have a contracting workforce, but we're still adding jobs.

And one of the reasons for that is the higher labor force participation rate of senior citizens. So there are some things moving in opposite directions that are driving these dynamics.

REPRESENTATIVE HELM: Well, does it also have something to do with the fact that there are people employed in Pennsylvania that don't live in Pennsylvania?

DIRECTOR KNITTEL: That could be contributing to it. There are a number of people who do commute into the State and commute out of the State to work. So that could explain some of the discrepancy.

REPRESENTATIVE HELM: I mean, obviously

we want our PA people to be employed over non-PA people.

DIRECTOR KNITTEL: Yes.

REPRESENTATIVE HELM: Since jobs and taxes kind of go together, can you provide a breakdown of the average State and local tax burden for Pennsylvania compared to the US average?

The data indicates that Pennsylvania has an overall tax burden of 10.42 percent, compared to the national average of 10.28 percent, when measured as a percentage of personal income.

Just curious, how does Pennsylvania's tax burden compare to our surrounding and competing states?

DIRECTOR KNITTEL: So for that comparison, I would refer you to page 15 in the packet that was submitted for the hearings. And this is based on a recent study that my office put together. We put this study out every year, and it ranks Pennsylvania State and local taxes as a share of total State personal income.

And on page 15, we look at Pennsylvania and the surrounding States. And as you noted, what we would call the total tax measure, an effective tax rate, if you will, for Pennsylvania is 10.4.

And for total taxes, you can see most of the States are above us. Ohio and Virginia are lower than us.

And looking across different sources, on some things we are the higher end of it. For example, corporate net income, we rank 11th at 0.5 percent; personal income, we're ranked 17th at 2.7; sales tax, we're rather low because we have a relatively narrow tax base in Pennsylvania; we don't tax food or clothing, and we rank 39th; in property tax, we're about the middle; we have a rank of 21; and then gaming, liquor and tobacco moneys, we're rather high and we rank 8th, which relative to the States surrounding us, it's high relative to them also.

So overall, I would say Pennsylvania is in the middle of the pack. We're slightly higher on some metrics, but lower on others.

REPRESENTATIVE HELM: All right. Thank you.

MAJORITY CHAIRMAN SAYLOR: Before I proceed to Representative Mary Jo Daley for comments, I wanted to introduce other members that are here that are not members of the Committee. I have Representative Eli Evankovich, Representative Dush and Representative Ryan.

Also joining us, who will be asking questions of Chairmen of each of the standing Committees that have oversight, will be asking questions, we have Representative Jake Wheatley, who is the Democratic Chair of the Finance Committee. And he will go at the end after the members have finished all of their questions. And if we are joined by Representative Bernie O'Neill, who is the Republican Chairman of Finance, he will do the same at that time.

With that, Representative Daley.

REPRESENTATIVE DALEY: Thanks, Mr. Chairman.

Good morning. It's good to see you today.

I just wanted to ask, in your opinion, what is the most concerning demographic trend in Pennsylvania?

But also, is there a trend that gives you some cause for optimism?

DIRECTOR KNITTEL: Sure. Regarding the demographic trends, actually, I would point to two that are concerning. One in the near term is the contracting labor force. So currently, Pennsylvania is experiencing a contraction of those aged 20 to 64 and that will continue to happen over the next decade.

One other item that is concerning is the declining fertility rate. In particular, now millenials, as they're approaching household formation and starting families, we're hoping that the fertility rates will not continue to decline and they will, in fact, increase.

One item that does give us a bit of optimism, and I would refer, again, in the packet, I believe on page 10, there is some demographic information. And the latest data from the Census Bureau for 2017 does show that the net outflow from Pennsylvania has been reduced.

So in 2016, we had a net outflow of 50,000 residents. In 2017, that has decreased to 26,000. We're hoping that trend will continue, it will continue to decline and approach zero, perhaps even turn positive in the near term.

REPRESENTATIVE DALEY: Sorry. Do we have information on the age of migration?

DIRECTOR KNITTEL: We do for prior years. For 2017, it's still preliminary, so they haven't released the data, but we have it prior to that, if you're interested.

REPRESENTATIVE DALEY: So clearly it would be good if we had young people moving into the State because that would potentially address both of those concerns that you had with contracting labor force and also the declining fertility rates --

DIRECTOR KNITTEL: Absolutely.

REPRESENTATIVE DALEY: -- hopefully.

DIRECTOR KNITTEL: Yes.

REPRESENTATIVE DALEY: Good. Thank you.

Thanks, Mr. Chairman.

MAJORITY CHAIRMAN SAYLOR: Thank you, Representative.

The next person to testify is Representative Greiner.

REPRESENTATIVE GREINER: Thank you, Mr. Chairman.

I wanted to discuss a little bit about the federal bonus depreciation and the Corporation Tax Bulletin 2017-02. The Federal Tax Cuts and Jobs Act of 2017 provided the schedule for bonus depreciation over several years, initially permitting 100% bonus depreciation for property placed in service after September 27th, 2017.

Now, on December 27th, 2017, the Department of Revenue issued a Corporation Tax

Bulletin, 2017-02, addressing the disallowance and recovery of 100% depreciation. On background, I've worked in public accounting for over 20 years and worked with a lot of businesses.

I guess what I'm wondering, I'm concerned that this message that was sent to the business community with the issue of this bulletin, I'm not sure it was a positive message in light of we're trying to create jobs.

In your opinion, is it sound policy to completely disallow -- to allow the depreciation over the usable life of the business property as the bulletin had prescribed, until when the property is either sold or otherwise disposed of?

I mean, I wanted to ask you that.

And then, are you aware of any other States that have exercised this same type of policy?

DIRECTOR KNITTEL: So regarding the corporate tax bulletin, first, I am not aware of any other States that have allowed the deductions from income tax until the property is sold or disposed of. And under a traditional income tax, one would allow a gradual write-off or depreciation of such assets, so that is traditional.

And as part of our mid-year update, one

of the things we did is we looked at the revenue impact of the corporate tax bulletin, and we think the denial of those deductions would raise about $160 million of revenue in the next fiscal year. We haven't included that in our forecast, but it's that order of magnitude.

REPRESENTATIVE GREINER: I guess in response to that bulletin, HB 2017 was introduced earlier this year and was passed unanimously out of Committee, the Finance Committee, 27 to zero, which I'm also a member of that Committee.

Have you looked at that language in that bill?

And if so, have you done an analysis at this point on that bill?

DIRECTOR KNITTEL: No. At this point, we have not done an analysis, but we will plan to do so.

REPRESENTATIVE GREINER: Very good. Thank you.

One last question. Your written testimony noted that you have not included any revenue impact from the bulletin and you will revisit the assumption with your May 1st Revenue Release.

That being said, I do note that your mid-year update estimates, the impact to the bulletin to increase revenue $50 million in '17-'18, you mentioned that, $160 million the following year.

Please explain how the bulletin changes the calculation of depreciation for Pennsylvania tax purposes and how this change generates additional revenues.

DIRECTOR KNITTEL: So the way the bulletin is currently written, what it would do is it would deny deductions for those claiming 100% depreciation. And if you look at historical trends, we think maybe 60 to 70 percent of the investment in Pennsylvania would opt to claim the full expenses, if allowed to do so.

So for folks claiming -- for firms claiming the 100% expensing, for Pennsylvania tax purposes, they would not be allowed a write-off for their investment. And due to the disallowance of the write-off, it raises the taxable income and therefore increases tax revenues.

REPRESENTATIVE GREINER: Yeah, I mean, I appreciate -- I wanted to get you on record explaining that because I do think it is problematic. We are trying to get business to come here to Pennsylvania. We're the only State that wants to deny that.

And I think it's something that -- I think as we continue here that -- I think it's something we're all probably going to have to look at. So thank you for your time.

Thank you, Mr. Chairman.

MAJORITY CHAIRMAN SAYLOR: Thank you.

Representative Bullock.

REPRESENTATIVE BULLOCK: Thank you, Mr. Chairman.

Good morning. How are you?

DIRECTOR KNITTEL: Good morning.

REPRESENTATIVE BULLOCK: So I have a few questions. I'll ask them upfront and then you can follow up with your answers.

The first set of questions is in regard to our investments in childcare and early education. Recently, the IFO issued a study that the economic impact of childcare and early education funding in Pennsylvania supports working families, provides children with significant economic benefits to our State, as well.

Can you summarize those findings?

And in particular, the report notes that the economic multipliers for these programs are much higher than those that we see in other types of State funding and State spending, including tax relief to households. So would this study basically imply that, comparatively speaking, investments and economic activity is generated by investing in programs like childcare and early education more so than in funding tax cuts?

And then the second set of questions I have is a set of questions I ask every year in regards to your hiring and diversity in your hiring. If you can, just point out any changes over the last year that you may have seen in regards to the reports that you provided last year, in regards to the number of women and people of color and other minorities that were hired by your Department.

DIRECTOR KNITTEL: Sure. So regarding your first set of questions, we did put out a research brief last year, late in the year of 2017, that looked at childcare and early funding of education in Pennsylvania. And for the purpose of that research brief, what we did is we looked at the total spending by the State and we looked at the amount of Federal moneys that would be pulled down just due to those programs.

So it was kind of an incremental approach and we tried to isolate and adjust the spending on those programs. And we found, if we did that, that the spending would be about $545 million for the latest year that we looked at, which was '15-'16.

We then applied a multiplier to that direct spending, and the multiplier was about 2.2. And as you noted, that is a fairly high multiplier.

If we're looking at all types of government spending, it's actually one of the higher multipliers. So it has a larger impact on the Pennsylvania economy. And the reason for that is all of the spending really remains in the State. There are State residents that are working in these programs and they tend to spend most of that money in the State, so it has a larger impact.

And just generally, I'll also note that what we found -- and we looked across other States who performed these studies -- is that in terms of a bang for the buck, this rated very high, these programs, across all States. So it wasn't just for Pennsylvania that we found this, but all States found a similar result that for government spending, it did have a larger than typical impact on the State economy and economic activity.

To your second question, on the hiring, last year at this time, my staff, there were 10 individuals that comprised the staff. We had five females, five males. There was one individual of minority status.

Since that time, that individual departed and took a job with DEP. He works with their legal team, their policy shop. And currently, we still have 10 staff and now six of them are female; four of them are male. None of them are minority status currently.

REPRESENTATIVE BULLOCK: Thank you.

I'm sorry. Could you repeat the number that was invested in education and childcare programs?

I missed it. It was five hundred --

DIRECTOR KNITTEL: $545 million.

REPRESENTATIVE BULLOCK: Million?

DIRECTOR KNITTEL: That's State and Federal. And the Federal moneys are just attributable to that program. They would not otherwise be here.

REPRESENTATIVE BULLOCK: Thank you. I understand the importance of investing in our children. And to see that investing in our children is not just investing in their individual success, but in the success of our Commonwealth. So I appreciate you doing that report.

Thank you.

MAJORITY CHAIRMAN SAYLOR: Representative Ortitay.

REPRESENTATIVE ORTITAY: Thank you, Mr. Chairman.

I wanted to focus more on follow-up of your staff questions and hit on a couple of other topics, as well. You said you had 10 staff members.

From the breakdown I have, you have three managers, one office manager and six analysts.

Can you go through kind of what the role as a manager is? Because it seems like having three or four managers out of 10 employees is a lot.

DIRECTOR KNITTEL: Yeah, so our managers are really, I would say, multi-tasking. So at any particular time, we have multiple projects going forward. Some of them are revenue estimates. Some are special studies, such as the child credit. Some will be performance-based budgeting.

So the managers that we have are overseeing multiple projects, even though the ratio, as you noted, is fairly low of management to staff.

REPRESENTATIVE ORTITAY: So they're actually working, doing the analytical work, as well?

DIRECTOR KNITTEL: That is correct.

REPRESENTATIVE ORTITAY: Okay.

The other question, in regards to your appropriation for this year's budget -- I know that we've tasked you with a lot of additional work and responsibility, but are you doing anything to cut costs or operate more efficiently and effectively?

DIRECTOR KNITTEL: The main way we approach that -- and we do keep a very close eye on the data requests that we make and the software that we use. For example, our statistical software that we use to run regressions, we've just cut back on the number of subscriptions. That's a very costly subscription.

We're also reassigning staff. So we do have some new duties coming in from performance-based budgeting. We're looking at the total scope of that project before we do any new hiring. So we're trying to reassign staff and leverage them as much as possible before we hire any new staff.

REPRESENTATIVE ORTITAY: Do you do the

same for technology costs?

I mean, you talked a little bit about licensing fees for different software.

I mean, do you have a bidding process where you have to bid out a certain contract for a piece of technology or software?

DIRECTOR KNITTEL: We do look at multiple providers when we're looking at statistical software or other data that we require.

REPRESENTATIVE ORTITAY: Okay. Thank you.

Just one other question that I have. I was looking through the forecast, I think, since 2012-'13 for your revenue estimates. You've been between a half a percent and I want to say, I think, 2.7 percent from 2016 and '17.

There are some variations in there. And I'm not saying half a percent at three percent is that big of a variation, but when you look at the -- it's $500 million, $100 million, $600 million, that's a big number for us, especially when we're looking at certain programs.

So I was wondering if you guys, over that period of time, have made any material changes into how you forecast revenue.

DIRECTOR KNITTEL: Sure. So as you noted, and we put this document on our website. It has a range from about a half a percentage point, I would say up to about two percent, if we control for the transfer that we didn't receive last year.

But every year, we do revisit our models. We go back and I have the staff break out, you know, what caused this error, was it a technical error, was it an economic error, so that we understand what caused it so that we can address it.

REPRESENTATIVE ORTITAY: All right. That's all I have.

Thank you.

MAJORITY CHAIRMAN SAYLOR: Representative Kinsey.

REPRESENTATIVE KINSEY: Thank you, Mr. Chairman.

Good morning, gentlemen.

The question I have, I want to refer back to page 15 in the information that you shared with us. And actually, I'm going to probably ask two questions, but this one might be a two-part question in and of itself.

You shared with us the State and local tax burden comparison. The question that I have is, how do you come up with that ranking?

Are you looking at combined State and local taxes?

Do you look at per capita as well as per $100 of personal income?

Like, how do we come about to ranking Pennsylvania where we are ranked at, according to the chart that you gave us?

DIRECTOR KNITTEL: Sure. So the data that you see in that chart is based on census and IRS data that they publish and is available on the web sites. So these statistics could be reproduced, if one wanted to.

And the ratios here are very simply all State and local taxes that would be paid over the total income of the State. And we do some per capita measure on another page in the handout that we can discuss, but for this purpose, we just did it relative to the income to get what we refer to as an effective tax rate measure.

REPRESENTATIVE KINSEY: All right. So in this particular chart, then, based on what you just shared -- okay. Then I guess -- okay, that explains how we are ranked for this particular chart.

But you said there are some other factors that go into it that are someplace else in here?

DIRECTOR KNITTEL: Yeah. So another way to do these types of rankings, as you noted, is on a per capita basis.

REPRESENTATIVE KINSEY: Right.

DIRECTOR KNITTEL: And if we go to page -- let me -- in your handout, it is page 9, where we compare Pennsylvania to the surrounding States. And if you look at the bottom two rows, rows 9 and 10, one of them is looking at State and local taxes compared to income, which was from that table.

REPRESENTATIVE KINSEY: Okay.

DIRECTOR KNITTEL: The final line is looking at State and local taxes based on total population. And of course, depending on the metric one uses, the rankings could change and will move around based on that.

REPRESENTATIVE KINSEY: Okay. That's what I was getting at. Let me jump to another question.

I know that Governor Wolf has talked over the past three years about increasing the minimum wage. I guess my questions is, how does Pennsylvania compare to, I guess what the Governor is requesting and looking at, surrounding States?

How does that factor into the forecast, if the Governor were able to enact his measurement?

I think it was $12.00 per hour.

DIRECTOR KNITTEL: Yes. Again, I'll refer just quickly to the page in the packet. On page 27, we have the minimum wage levels for Pennsylvania and most States for 2018, '19 and '20. And if we look at, for 2018, if we were to rank all of the States on their minimum wage, Pennsylvania would rank 31st, along with about 20 other states that have the Federal minimum of $7.25.

And then you can compare to surrounding States. They're highlighted. So New York in 2018 is at $10.40; Maryland at $9.25; West Virginia at $8.75; New Jersey at $8.60; Ohio at $8.30; and Delaware at $8.25.

We are doing an analysis of the minimum wage and how it would impact the economy. What we found last year, we do think there will be some job contraction, but we do also think it will increase economic activity because the individuals who tend to receive the benefit from a higher minimum wage are more inclined to spend those moneys and spend them in the State.

REPRESENTATIVE KINSEY: Great. Just so

I'm clear, you're talking about basing it on the Governor's proposal of $12.00 per hour?

DIRECTOR KNITTEL: Yeah. That's correct.

REPRESENTATIVE KINSEY: Great. Thank you very much.

Thank you, Mr. Chairman.

MAJORITY CHAIRMAN SAYLOR: Representative Quinn.

REPRESENTATIVE QUINN: Thank you.

Over here. And thank you for always being there for us to give your independent view. Appreciate it.

I want to go back to a question regarding demographics. When you pointed out the change in the trend for the zero to 19-year-old age group, does that capture those leaving the State for college?

DIRECTOR KNITTEL: Yeah. So the way the census tabulates those data is that folks coming into the State, even if they're here for a year or two, if they're here during a survey, they would be counted as a resident.

REPRESENTATIVE QUINN: Okay.

DIRECTOR KNITTEL: And then when they leave, then we lose them.

REPRESENTATIVE QUINN: Have you ever done anything about capturing, you know, how many we retain?

DIRECTOR KNITTEL: Yes, we did. In fact, back in our five-year report, we did look at the inflow and outflow, based on age group. And sure enough, you can see a large inflow, those 18 to 19.

And then about three to four years later, most of them depart, return back home, but not all of them. Some of them do stay. So there is some retention.

REPRESENTATIVE QUINN: Well, I hope mine come back. Now, on to the Federal Tax Cuts and Jobs Act, please. Your written testimony states that the Tax Cuts and Jobs Act will impact the General Fund revenues in three ways, increase in disposable income in Pennsylvania by $6 billion to $8 billion per year; provide additional revenue through the Federal corporation tax cut, which may result in higher wages, reduced prices and higher dividends paid, and provide additional revenues from the broadening of the Federal corporate tax rate.

Additionally, you mention that the final ways our economy will be impacted will be through indirect and induced effects named as dynamic effects, after the first round of spending from the gains and the increase in the disposal income, personal income.

However, your mid-year update provided estimates of the impact to the General Fund revenues, specifically, for the corporate net income tax, sales tax and the personal income tax.

What's the combined impact of the Federal tax changes on the General Fund revenues in the 2017-'18 budget and 2018-'19?

And can you briefly describe how each tax is impacted by the Federal changes?

DIRECTOR KNITTEL: Yeah. Regarding the overall impact for '18-'19, for next fiscal year, we believe it's just a little under $300 million, if we were to look at all of the different sources. About $150 million of that is corporate net income tax and that is due to base broadening, much of it.

The Section 199 deduction was eliminated, and there's a cap on the interest deductions for corporations. For sales and use tax, we thought it was about a $70 million pick-up from the higher disposable income that you had noted and another seventy to eighty in personal income tax from higher dividends and higher capital gains for next year.

But this year, I believe we have a number that's probably closer to a $100 million impact on the General Fund, but there's more uncertainty about that because we're not sure how quickly it will show up.

The Federal withholding tables have already been adjusted so they should be filtering through right now, but how quickly those people spend the money is unclear and whether it will be on taxable items. So we have a bit more confidence on next year as opposed to this year.

REPRESENTATIVE QUINN: So you're saying as we are in the final few months of '18, that's where the uncertainty is, but you're guessing about $100 million?

DIRECTOR KNITTEL: That order of magnitude, based on the Federal base expansion and the additional disposable income that's flowing through to paychecks.

REPRESENTATIVE QUINN: Thank you.

MAJORITY CHAIRMAN SAYLOR: Representative Schweyer.

REPRESENTATIVE SCHWEYER: Thank you, Mr. Chairman.

Good morning. Thank you so much for

being here. Thank you for providing a really robust and, I think, very fair and balanced analysis of where we're at.

One of the topics that I'm personally quite concerned about is our Rainy Day Fund of lack thereof. I think at last estimate, it's something like $250,000, give or take, that we have in our savings account.

I want to talk about that, about a couple of different things. So even though it looks like revenues are doing okay for us, at least compared to when I first arrived here, it seems like at any small, little shift in the economy, any poor decision that the legislature would make by dumping a bunch of money into, you know, tax credits or something like that, that we'd be spending more dollars on that we don't have, could not only impact our baseline projections moving forward, but also would force us to dip into $270,000 or $250,000 and we can't then therefore pay our bills.

So the Rainy Day Fund, specifically, sir, what should it be, where should we be going, what steps should we be taking to protect ourselves against poor decisions that the General Assembly may make, downturns of the economy, more changes from the Federal government that could impact us?

What are some of the things that we should be doing?

What should our target be?

DIRECTOR KNITTEL: Yeah, I think it's, as you know it to be, the Rainy Day Fund currently is slightly above zero, but effectively about zero currently. And I think most would agree that it's prudent management, budget management, to have funds set aside for unexpected downturns or volatility.

And that could happen at any time. We have a very difficult time predicting when, in fact, that will happen.

Regarding the order of magnitude, I've seen numbers on the order of five to six percent of the total spend should be set aside, if it's possible to do so, in order to offset a downturn in the economy.

REPRESENTATIVE SCHWEYER: Okay. So in addition to supporting and sustaining us in a downturn of economy or some other issue, that would affect our bond rating, as well, correct?

DIRECTOR KNITTEL: In theory, it would, yes. If we did have a downturn and we were not prepared for it and, in fact, I think in the latest analyst by S&P, they cited the lack of a Rainy Day Fund as affecting the bond rating.

REPRESENTATIVE SCHWEYER: Okay. So simply by saving some money, either through cuts or through smart budgeting or whatever, we will not only be protecting ourselves in the future, but also save money in our future bond ratings?

DIRECTOR KNITTEL: It should serve both purposes, yes.

REPRESENTATIVE SCHWEYER: Very good. Thank you, sir.

Thank you, Mr. Chairman.

MAJORITY CHAIRMAN SAYLOR: Representative Grove.

REPRESENTATIVE GROVE: Thank you, Chairman.

Gentlemen, good morning.

How are you?

DIRECTOR KNITTEL: Good morning.

REPRESENTATIVE GROVE: Question one, I'm going to go back and review some revenue estimates. Well, it's not an exact science, but January of 2017, actual revenues were going to end the fiscal year short of the official estimate. Roughly, it was about $416.8 million.

Can you kind of review what changed in the first seven months of the fiscal year in 2017-'18, causing the revenue shortfalls?

DIRECTOR KNITTEL: Excuse me, for this year or last year?

REPRESENTATIVE GROVE: It was last year, 2017.

DIRECTOR KNITTEL: Sure. Absolutely.

I would characterize that last year as it was very broad weakness across our big three revenue sources, sales, personal income and corporate net income, really a confluence of events.

What we're finding out now from the latest tax data is that capital gains actually fell last year; dividend payments actually fell last year. And we don't see that until the tax return data comes in. And we think some of that was due to the election, that people defer capital gains in anticipation of a tax cut.

Sales tax was weak, as well. The year prior to that, sales tax grew by three percent. Last year, it only grew by one percent. So for some reason, people weren't spending the income that they were receiving.

And finally, on a corporate side, we had a very unusual occurrence where we had two consecutive years of negative profit growth and that hasn't happened in decades, outside of a recession.

REPRESENTATIVE GROVE: And then, after your mid-year update, published January 25th, 2017, you assumed revenue would continue to decline by $716 million. The Governor presented the executive budget two weeks later, February 7th.

He anticipated revenues would end the fiscal year short by only $374. Basically, he was saying they would exceed the revenue estimate for the next few months.

On June 30th, when the fiscal year ended, actual collections were short by $1.1 billion. It kind of showed the Governor's false assumption on revenue collections, creating the proposed '17-'18 budget.

At what point should there be a correction with the Governor's Office to updating those revenue analyses and at least starting to put some money back in the budgetary reserve?

Should it be done immediately or --

DIRECTOR KNITTEL: I can't speak for them on when it should be done. I can say, for my office, we were seeing the weakness right out of the gate, really. And as you noted, we did pull down our mid-year estimate by about $450 million and then again in May by two hundred, and then the loss of the transfer at the end of another two hundred.

REPRESENTATIVE GROVE: Okay.

Let's go back in time a little bit further. Governor Wolf's proposed budget 2015-'16 proposed a $4.56 billion tax increase. Ironically, had that taken place, his revenue estimate at the time was $35.86 billion; revenue estimate for this current fiscal year is $33.61 billion, based on his proposed budget. It's a difference of about $2.26 billion.

Had that tax been enacted, do you feel we would have had a stronger economy or a weaker economy?

DIRECTOR KNITTEL: I think that's unclear because it depends on how the money would be spent. And I can't say one way or the other whether it would be higher or lower.

REPRESENTATIVE GROVE: Money into -- the tax revenue coming into the State, how it was spent by the State.

DIRECTOR KNITTEL: Correct. So the money taken out of the estate will have a certain multiplier associated with it and then it comes into the State and it is spent and it will have a certain multiplier associated with it, too. So we would have to know how the moneys were spent, so we could make the comparison.

REPRESENTATIVE GROVE: Okay. Fair enough. You've done extensive work on the Federal Tax Cuts and Jobs Act, as well as the minimum wage increase.

Based on your two analyses, what will put Pennsylvania in a better economic standing moving forward, the Governor's proposed minimum wage increase or the Federal Tax Cuts and Jobs Act?

DIRECTOR KNITTEL: I think on that, it will depend on the metrics that one is using. And there are several metrics that could be used for that purpose to decide which one is better or worse than the other.

REPRESENTATIVE GROVE: So I mean, going through your minimum wage estimate, we have direct loss of jobs associated with it.

Is there any loss of jobs associated with the Federal tax cuts?

DIRECTOR KNITTEL: Not that I'm aware of.

REPRESENTATIVE GROVE: Okay. We have

increased money going back to Pennsylvania residents with the tax cuts, all basically income demographics, who is going to see more money, more expenditures in their pockets.

With the minimum wage, you're really looking at a finer portion, correct?

DIRECTOR KNITTEL: It would affect a smaller portion of the population receiving the income increase.

REPRESENTATIVE GROVE: Thank you.

Thank you, Mr. Chairman.

MAJORITY CHAIRMAN SAYLOR: Representative Briggs.

REPRESENTATIVE BRIGGS: Thank you very much for being here today. I just wanted to follow up a little bit more on the bonus depreciation and consequences from the Federal tax changes.

If nothing were to change regarding Pennsylvania and the way we deal with that, what effect would that have on Pennsylvania's revenue?

DIRECTOR KNITTEL: We believe that if Pennsylvania conformed to the Federal Bonus Depreciation, let it be enacted, similar to what happened in 2011-'12, my office believes that would reduce revenue on the order of $500 to $600 million this year and next.

REPRESENTATIVE BRIGGS: So $500 million just for this upcoming fiscal year?

DIRECTOR KNITTEL: Combined this year and next.

REPRESENTATIVE BRIGGS: Okay.

DIRECTOR KNITTEL: Between five and six hundred.

REPRESENTATIVE BRIGGS: So just over two years, five hundred million?

DIRECTOR KNITTEL: Correct.

REPRESENTATIVE BRIGGS: Okay. Thank you.

MAJORITY CHAIRMAN SAYLOR: Representative Kempf.

REPRESENTATIVE KAMPF: Thank you, Mr. Chairman.

Mr. Director, the question I'm asking is sort of a follow-up on Representative Helm's question. It's about jobs in Pennsylvania.

So I have on your report, page 6, Pennsylvania economic trends, you indicate for 2017, jobs created is the number 60,000, right?

And am I right that while the labor force may not be as large because of demographics, right, people age out of the workforce, that's happening all over the country, in terms of raw jobs that are available in Pennsylvania, that number, 60,000, that's the growth in the raw number of jobs that were created in 2017, right?

DIRECTOR KNITTEL: Yes, that's the net gain in the jobs.

REPRESENTATIVE KAMPF: Okay. So it's not just new jobs, but some others went away, it's an additional 60,000 jobs?

DIRECTOR KNITTEL: That is correct.

REPRESENTATIVE KAMPF: Some of them may be filled by people who, say, live in Delaware, New Jersey or Ohio, right?

DIRECTOR KNITTEL: That's possible.

REPRESENTATIVE KAMPF: Okay. So we had from the Labor Department -- I guess it's probably the U.S. Labor Department -- we had 78,400 non-farm jobs for the same year. And that came from a January 19th report.

Any idea why you have 60,000 and we got 78,000?

DIRECTOR KNITTEL: I think there are probably different ways of counting. I'll just take a minute to explain. When we compute our 60,000 here, it's really an average for the entire year and we're comparing it to the average from the prior year.

And I will say, the 60,000 you see here is a projection by my office. The raw number is really 66,000, but there are some unusual aspects in that number that look very strange that I don't think will hold up when this rebenchmark is released in 2018.

So I think the main part of the discrepancy is, one, my office doesn't believe what we're seeing, it was that strong. And we think that's going to be revised down. The second part is I believe we're using the year-over-year average and they might be using the month-over-month, so January compared to last January.

REPRESENTATIVE KAMPF: Okay. All right.

On your page 6, you indicate for 2018, I assume that's a projection for roughly 62,000 new jobs?

DIRECTOR KNITTEL: That's correct.

REPRESENTATIVE KAMPF: Okay. All right.

And that's your projection or is that a projection based on the U.S. Labor Department? In other words, the same methodology you used for 60,000, you're also using in your projection for

61,000 for next year?

DIRECTOR KNITTEL: That's correct. It's a projection by my office.

REPRESENTATIVE KAMPF: Okay. All right. And then I see I still have a little green left.

What is your projection for the '18-'19 budget in terms of State revenue growth?

Is it on the order of $900,000 over last year?

I'm talking about tax and fee revenue, not one-time.

DIRECTOR KNITTEL: Yeah. So in the packet -- I believe, or perhaps we don't have it here.

So we have growth -- we have a projection -- our latest projection at our mid-year was $34.78 million. Next year, we have $33.91, so we do have a reduction projected. The main reason for that is there's a lot of one-time revenues.

REPRESENTATIVE KAMPF: I was asking about tax and free revenue. In other words, what is your projection for '18-'19 over '17-'18?

DIRECTOR KNITTEL: Just for tax and fees, for '17-'18, we have $31.9 billion; for '18-'19, we have $33.2 billion. And that's a growth rate of about four percent.

REPRESENTATIVE KAMPF: Okay. So a growth rate and revenue of about four percent, roughly $1.3 billion in additional revenue?

DIRECTOR KNITTEL: That is correct.

REPRESENTATIVE KAMPF: And then what is your projected GDP growth for '18-'19?

What's the percentage rate?

DIRECTOR KNITTEL: For Pennsylvania, we have about -- we have 2.3 percent real GDP growth for calendar year 2018.

REPRESENTATIVE KAMPF: Just based on my reading of the newspapers, that sounds a little bit low.

DIRECTOR KNITTEL: Compared to the U.S. projections, they will be lower, but that's typical of Pennsylvania, that we'll run low by .4 to .5, compared to the U.S. growth.

REPRESENTATIVE KAMPF: Okay. Thanks.

MAJORITY CHAIRMAN SAYLOR: Representative Delozier.

REPRESENTATIVE DELOZIER: Thank you, Mr. Chairman.

I have two clarifying questions, if I could ask. My first question is dealing with the corp tax bill that was asked about a little while ago. I just have one clarifying question.

That is, a lot of other formulas in other agencies use depreciation in establishing rate base. My example is the PUC. They use depreciation. When a utility company comes in asking for an increase in rates or anything like that, they use the depreciation as part of the equation.

With this established bulletin from the Governor, will this impact other formulas throughout the State when they can use depreciation and when they can't?

DIRECTOR KNITTEL: Regarding that technical issue, I apologize, I'll have to defer because I'm not sure of the answer.

REPRESENTATIVE DELOZIER: Okay. I'm just concerned that if that's going to go into those types of formulas, we're going to have a lot of changes, especially in our utility rates. So I appreciate that information.

My second question is dealing with the impact fee and what we have right now -- the proposed tax that the Governor has put forward. And I notice that.

In '16, it was estimated that the impact fee was about 4.5 percent, 4.6; and in '17, it was 2.9. With the proposed tax that the Governor has, plus the impact fee, what would you estimate that Pennsylvania's tax rate would be?

DIRECTOR KNITTEL: I'll defer to Mark Ryan for that answer.

REPRESENTATIVE DELOZIER: Okay. Thank you.

DEPUTY DIRECTOR RYAN: We expect that the combined effective tax rate for both the impact fee and the proposed severance tax would be in the vicinity of four and a half percent.

I would break that down by the proposed severance tax would be about 2.5 percent, within a range. It depends partly on the price of natural gas --

REPRESENTATIVE DELOZIER: Sure.

DEPUTY DIRECTOR RYAN: -- and a schedule.

REPRESENTATIVE DELOZIER: Okay.

DEPUTY DIRECTOR RYAN: And then a two percent, based on our expectations going forward that the impact fee in the next year would be closer to two percent.

REPRESENTATIVE DELOZIER: Okay.

DEPUTY DIRECTOR RYAN: It would be in the four-and-a-half-percent range.

REPRESENTATIVE DELOZIER: Okay. Thank you very much. And I have one last question on that issue. This is more technical, and you might have to get back to me on this one, I understand that.

Are you familiar with the PIOGA versus the PUC case regarding the impact fee in and of itself?

DEPUTY DIRECTOR RYAN: Yes.

REPRESENTATIVE DELOZIER: Okay. And with that -- it's been appealed at this point.

Can you give me a feeling as to what you think the impact fiscally would be with the State should that case against the PUC, the impact, dollars that we receive into the State?

DEPUTY DIRECTOR RYAN: I'm going to pull it out of memory. I believe we looked at it, specifically, and it could affect several hundred wells, maybe 700, 800 wells, potentially. I believe the $17 million range, if everyone -- if it was decided against the PUC. So that much could be at risk.

REPRESENTATIVE DELOZIER: And is that just for that case or -- what I'm looking at is, if that case should go against the PUC, that's not the only case we're going to see. And to me, that goes right into the basis of what the impact fee does and how it is collected by the PUC, basically wiping out what the impact fee would have on our General Fund.

DEPUTY DIRECTOR RYAN: Well, we think -- our analysis was based on the qualification of wells as stripper wells.

REPRESENTATIVE DELOZIER: Correct.

DEPUTY DIRECTOR RYAN: If applying the criteria that was used by the plaintiffs and decided by the Commonwealth Court and then appealed to the Supreme Court, if those criteria were applied and the exemption for stripper wells was expanded, we think it would reduce impact fees by about $17 to $18 million.

REPRESENTATIVE DELOZIER: Okay. That's much less than I thought. I actually might follow up with you with some more details, only because some other evaluations have been much higher numbers in reduction of money coming into the State on that issue, should the case go that way and what we have to do in order to remedy that issue.

Thank you very much. I appreciate it.

DEPUTY DIRECTORY RYAN: We would be happy to talk to you about it.

REPRESENTATIVE DELOZIER: Okay. Thank you.

MAJORITY CHAIRMAN SAYLOR: Representative James.

REPRESENTATIVE JAMES: Thank you, Mr. Chairman.

I'm over here. Good morning.

DIRECTOR KNITTEL: Good morning.

REPRESENTATIVE JAMES: Thank you for your testimony.

I would like to turn to a brief discussion on expenditures, please. And it's on page 4 of the economic review update that we have. It's a bold move, I think, when a Department head comes into the Chief Financial Officer and says, hey, I want to raise my expenditures in my Department by 25 percent.

Usually, the CFO says, okay, that's fine. How are you going to justify that?

Do you anticipate that by spending these extra dollars, there will be significant benefits for the Commonwealth?

Where are we on that, please?

DIRECTOR KNITTEL: For the upcoming year, our budget is actually flatlined right now at

$2.2 billion. So currently, we don't have an appropriation increase in the current budget.

REPRESENTATIVE JAMES: Okay. I'm looking at '18-'19. Sorry.

DIRECTOR KNITTEL: Yeah, so in '18-'19, it's also flat. Our total spending is going up and there are a few reasons for that. One of the reasons is that we're increasing staff. We're hiring two new staff in regards to our duties with performance-based budgeting.

So that's the majority of that increase you see from one year to the next. Most of the spending under the operating you can see is rather flat. The data that we need, we already have in-house. So most of the increase in expenditures are related to personnel for those two new staff people.

One of the staff persons is a very senior level staff person who has worked for multiple Commonwealth agencies, and another one would be sort of a mid-level analyst. But both of them are dedicated to performance-based budgeting.

REPRESENTATIVE JAMES: Okay. And again, I see I have a little bit of green light left, as well.

Back home, tax credits generally are kind of warmly received by the business community and others, but we look at it a little differently down here.

I see that you have launched a series of investigations into the existing tax credits. Can you characterize how that's going and the direction of that study?

DIRECTOR KNITTEL: Yeah, absolutely. On the final page of the handout, you'll see our tax credit review schedule along with our performance-based budgeting. We've just started this work.

And the first credits that we'll examine out the door are film production, new jobs and alternative energy production. So currently we're just starting our efforts and we're going to dedicate our resources after the hearing to both this and performance-based budgeting.

But right now, what we're undertaking is a review of all of the work that's been done, all of the research across the different States, so we can see what the best practices are. We're also delving into a very large database. On state tax credit. That's maintained by the Upjohn Institute, and seeing if we can leverage that resource.

REPRESENTATIVE JAMES: Okay. Thank you very much.

Thank you, Mr. Chairman.

MAJORITY CHAIRMAN SAYLOR: Representative Krueger-Braneky.

REPRESENTATIVE KRUEGER-BRANEKY: Thank you, Mr. Chairman. I appreciate you both for being here today.

Since we started a conversation about severance tax, I want to follow that line of questioning. So you said the combined effective rate for severance plus impact fee would be 4.5 percent; did I get that correct?

DEPUTY DIRECTOR RYAN: Approximately. It would vary, depending on the price of gas in any one year, though.

REPRESENTATIVE KRUEGER-BRANEKY: Okay. And what do you know about how that compares with other States that have the fracking industry?

DEPUTY DIRECTOR RYAN: Based on memory, I think it would be pretty much -- it would be fairly comparable. I would say somewhere in the middle, not the highest, not the lowest.

REPRESENTATIVE KRUEGER-BRANEKY: Okay.

And I know the Governor has been attempting to propose a severance tax in every budget that he has proposed since he's been in office. In this year's budget, his estimate is a severance tax that would raise $248 million for our budget.

Do you believe that that's a reasonable estimate for the severance tax with this effective rate?

DEPUTY DIRECTOR RYAN: We looked at the proposal and based on our own price and production estimates, we think that estimate is reasonable.

REPRESENTATIVE KRUEGER-BRANEKY: Okay. And given that most of the companies who are engaged in this industry are out-of-State and a lot of the product is shipped out-of-State, about how much of that burden would be shifted outside of Pennsylvania?

DEPUTY DIRECTOR RYAN: We would expect probably in line of about 80 percent would be shifted, based on the usage and consumption of gas in Pennsylvania and the production. So our previous analysis has estimated about 80 percent of the gas is exported.

REPRESENTATIVE KRUEGER-BRANEKY: Okay. So if we were to finally enact a severance tax this year, you believe that 80 percent of the impact would be felt outside of Pennsylvania?

DEPUTY DIRECTOR RYAN: Yeah, that's right.

REPRESENTATIVE KRUEGER-BRANEKY: Okay. Thank you.

MAJORITY CHAIRMAN SAYLOR: Representative Boback.

REPRESENTATIVE BOBACK: Thank you, Mr. Chairman.

Director, based on your testimony and the information that we received, I've been putting the information in little packets on a continuum, starting with 2008, Great Recession, to where we are now, 10 years later, 2018 approximate, without a broad-based tax increase, so we plowed out of that.

I've been monitoring other States, and I think without taxing people through the sky, which we did not do, I think we did all right.

My ask is, where are we going, what's the state of the State, where do you see us heading based on the way we're handling the moneys now and performance-based taxes?

Do you have any suggestions?

What's your opinion?

DIRECTOR KNITTEL: I can't offer a suggestion regarding that. I can say, unlike prior years, we're cautiously optimistic this year about the revenue picture. It's holding up well, even through the month of February currently. Things are holding up well. We do have a little concern about the next few months because it's going to be a lot of volatility, there are a lot of tax law changes.

And so I really have to reserve comment until we see those moneys coming in. And if they hold up, then we're, I think, cautiously optimistic going forward.

REPRESENTATIVE BOBACK: And I will take cautious optimism.

A follow-up question, before you talked about taxes coming in, you said the liquor tax -- I think it was liquor tax -- was eight percent?

You said eight, and I didn't make a note there. You said that was rather high.

The PIT, 17th -- oh, the rating in the nation; we were number eight.

DEPUTY DIRECTORY RYAN: Correct.

REPRESENTATIVE BOBACK: And that was high. What do you attribute that to? Because out of all of the taxes that you cited, that was the highest.

DEPUTY DIRECTOR RYAN: Yeah, so that's really -- that rank of eight is really an amalgam of not only liquor, but of tobacco and gaming. So we put all of those into one basket. And then based on all three of those sources, that gave us the ranking of eight.

REPRESENTATIVE BOBACK: Okay. Thank you very much for your time.

Thank you, Mr. Chairman.

MAJORITY CHAIRMAN SAYLOR: Representative Patty Kim.

REPRESENTATIVE KIM: Hi. Over here.

I have a concern with the recent corporate tax cut. It has left a hole in the budget and a lot of reports say that, you know, Congress is looking at maybe cutting Medicaid to help save costs.

If that happens, what are you -- first of all, looking at this and if we have Medicaid cuts, I think it leaves the burden on the States to pay for it or make up for the costs. Are you looking at this and projecting any scenarios in the near future?

DIRECTOR KNITTEL: We haven't looked at

that issue explicitly recently. In an analysis we did last year related to the higher minimum wage, we were asked to look at the impact that would have on safety net projects.

As you noted, I would expect that if there were cuts there from the Federal government, it would filter through to the States and affect the State spending.

REPRESENTATIVE KIM: That's all I have. Thank you.

MAJORITY CHAIRMAN SAYLOR: Representative Dunbar.

REPRESENTATIVE DUNBAR: Thank you, Mr. Chairman.

First off, a point of clarification in regards to Representative Briggs' question about what would be the cost of if we implemented fully bonus depreciation of Pennsylvania. You had said $500 million over two years, which I'm not doubting, but over the life of it, those assets, it's a revenue neutral thing, correct?

DIRECTOR KNITTEL: It does turn around. It's a timing issue.

REPRESENTATIVE DUNBAR: Okay. Thank you.

And for years, several years, we've sat

here and talked about performance-based budgeting and potentially having it. Now we can actually discuss implementation of it, which is a good thing because of Act 48. I guess the only regret is that Chairman Markosek won't be here to see it implemented.

I understand it's not a panacea to cure all our woes, but it's certainly a step in the right direction, in my opinion, and I appreciate the schedule you've given us on page 29. Just a point of clarification. As you go through, like this year's, Corrections, Board of Probation, Parole, you're going to establish metrics; is that what you're going to do?

DIRECTOR KNITTEL: Yes. We'll work with the agencies to get data in order to develop various types of metrics that can see -- assess whether they're meeting the goals and objectives that they've laid out.

REPRESENTATIVE DUNBAR: Very good. And then next year, you'll go on to the next line of items, but the ones you established in the first year, you're still going to do the measurements every year, though?

DIRECTOR KNITTEL: That's unclear.

REPRESENTATIVE DUNBAR: Okay.

DIRECTOR KNITTEL: It's not laid out in the statute.

REPRESENTATIVE DUNBAR: Okay. I know it's not, that's why I'm asking.

DIRECTOR KNITTEL: Okay. We haven't made any determination yet.

REPRESENTATIVE DUNBAR: Okay.

Also, do you believe, then, that we need some language to clarify that or are you going to put that into some type of regulations or something in future years?

My concern is if you visit it one year, then we don't see it again for five years, we could be missing opportunities.

DIRECTOR KNITTEL: I think it would be good to have some type of follow-up. And it's not once every five years; this would be a continual process.

REPRESENTATIVE DUNBAR: Okay.

Also, as you develop these performance measurements, how are we ensuring that stakeholders are getting a voice in the process?

For instance, if you're looking in the welfare arena and welfare programs, how do we know that like our local non-profits are having an opportunity to have input in it, as well?

DIRECTOR KNITTEL: Our intention is -- and again, starting after the hearings, we're going to make every effort not only to reach out to the agencies, but to also reach out to other stakeholders to get their insights because these people deal with it every day.

REPRESENTATIVE DUNBAR: Exactly.

DIRECTOR KNITTEL: So we want to hear from them.

REPRESENTATIVE DUNBAR: And do you think that is something we should codify, as well, or is that something you can put into some type of regulations as you're developing this?

DIRECTOR KNITTEL: I think we can internalize it as an office practice and make sure those stakeholders are involved.

REPRESENTATIVE DUNBAR: Okay. Continuing along those lines, I'm sure you're familiar with Pew Charitable Trust Results First Initiative. I know you even had a webinar on it in the last couple of weeks.

Is that something that -- HB 599 is sitting in the Senate; is that something that you believe we can incorporate into this process with 599 passing, just based on how Act 48 reads?

DIRECTOR KNITTEL: So I believe there's potential there. And as you noted, we have been investigating that. I do think there is a lot of overlap between Results First and performance-based budgeting. Cost-benefit analysis is an outcome measure, so I do think there's some potential there.

REPRESENTATIVE DUNBAR: I actually am looking forward to future years when we have the information at hand. These hearings will be a lot more entertaining. I can certainly assure you of that.

Just changing gears real fast, revenue estimates for this year, you projected $200 million from Gaming. Based upon our early sale of licenses and auction prices of our licenses, exceeding expectation, we're at $112 million, I believe it is.

Did you change your revenue estimate yet on that in your mid-year or are you planning on it?

Can you give us some insight on that?

DIRECTOR KNITTEL: Sure. In our mid-year, originally when we scored out the gaming expansion, we were at $103 million, I believe. And then, as you noted, based on the first two auctions that came in at $50 million and $40 million, we've increased our number and we're now up closer to $175 million for this year.

REPRESENTATIVE DUNBAR: Okay. Just for the many casinos?

DIRECTOR KNITTEL: For the entire package, that would be at $175.

REPRESENTATIVE DUNBAR: Okay. But I thought our revenue from this was $200 million from gaming expansion?

DIRECTOR KNITTEL: The administration's is $200 million, but my office has an internal number of $175 currently.

REPRESENTATIVE DUNBAR: Okay. And that's not increased or it's the --

DIRECTOR KNITTEL: It has increased. We were originally at $103, so we had a conservative number and we raised it up to $175.

REPRESENTATIVE DUNBAR: Okay. And lastly, in the Governor's budget proposal, there is a proposal for combined reporting for 2019-2020. In information I read from you in past years, you have projected about a nine-percent increase, I believe.

And the number you put on it was $300 million; is that still the number you believe we would get from combined reporting?

DIRECTOR KNITTEL: Yeah. So based on the research that we're --

REPRESENTATIVE DUNBAR: Net of any rate changes?

DIRECTOR KNITTEL: Yes. Roughly a 10-percent base expansion.

REPRESENTATIVE DUNBAR: Thank you.

MAJORITY CHAIRMAN SAYLOR: Representative Wheatley.

REPRESENTATIVE WHEATLEY: Thank you, Mr. Chairman.

And thank you for your testimony this morning. I wanted to just ask you to go back around the demographic questioning as we are trying to predict what we want to be as a Commonwealth and where we want to be as a Commonwealth, can you kind of speak to me about tax policy and fiscal policy as it relates to either encouraging, especially those 20 to 64-year-old working population and families who want to start families and support families; tax policies and fiscal policies that either we're doing correctly here or that we need to really take a look at to change.

Specifically, because our Tax Code is, in my opinion, very friendly to our mature population, which as we're looking toward the future, we might need to think of. That's one part of it.

And the the second part is just a comment, but you can add to it. I've heard the comment about our being able to weather this storm from 2008 until today, but what isn't being talked about -- and from a fiscal and a tax policy, maybe you can add some commentary to -- is the fact that my Republican friends demanded a borrowing of $1.5 billion to pay for operating expenses.

So how does that project as we are trying to really get our fiscal house in order in the outgoing years?

So those are my two questions. Thank you.

DIRECTOR KNITTEL: So in regards to your first question on the demographics, our research does show that over time due to the current tax system in Pennsylvania, more of the tax burden is getting shifted on to those aged 20 to 64, and that will continue to happen over the next decade purely due to demographic reasons and the way the Tax Code is structured. So I would raise that as a significant concern as more of that Tax Code is getting shifted onto its smaller aged cohort. And the relative burden is increasing.

Regarding the second point on the budget, what we believe will happen, starting in 1920, is that the debt service on the $1.5 billion securitization will run about, roughly, $100 million per annum. And of course, if that's being used to service debt, that cannot be used for other programs most related to health, all related to health.

REPRESENTATIVE WHEATLEY: Thank you.

MAJORITY CHAIRMAN SAYLOR: I'll recognize Representative Joe Markosek.

MINORITY CHAIRMAN MARKOSEK: Thank you. Just some comments here. Thank you, gentlemen for your testimony.

As usual, it's a lot of data and the State budget is a very complicated thing and our revenue projects are very complicated, as well. And I hope we've provided some light onto those very interesting topics.

A couple of things I just want to mention here. I know it was mentioned the depreciation, the bonus depreciation. While it is revenue neutral over a longer period of time, it could have some effects on the short term.

As we see a bump up in depreciation that's less revenue for the Commonwealth this year. It may work out over time, but I think we all have to keep in mind that that could happen this year.

I also want to say, too, and this has been something that I've said on and on and on here since I've been in this job as Chairman, that we need recurring revenues to balance our budget more so than one-time revenues. I think things being what they are, last year we did some recurring revenues, we borrowed some money. We have gaming money.

All of those are, for the most part, one time or very short-term revenue sources. At the end of the day, and perhaps after some of us are no longer here, the Commonwealth will have to deal with a serious issue of providing more recurring revenues. We cannot borrow or depend on one-time revenues to pay our current expenses.

The last thing I want to mention -- it was brought up by one of our members here -- is the Rainy Day Fund and how important that is.

There was a time here in my career where the Rainy Day Fund consisted of billions of dollars. And those billions of dollars came in handy when we had a downturn in the economy.

We have about $273,000 in the Rainy Day Fund, which I think would run our State government for about 15 minutes. So we really need, as good stewards of taxpayer money -- and I think most taxpayers would agree with this -- we need to put a little bit away each year for a rainy day. That's why they call it the Rainy Day Fund.

So I would hope that -- I'm glad that was brought up today and I appreciate your answers. I would hope that we would all, both parties, see that and to help fund the Rainy Day Fund. I know the Governor has suggested some additional revenues for that.

And I would hope that we could agree to that. So with that, thank you very much. I appreciate your testimony.

MAJORITY CHAIRMAN SAYLOR: Again, Matt and Mark, I want to thank both of you for your testimony today. I also want to thank you for your operation of the IFO. I think you have demonstrated exactly what the General Assembly decided, when it created your Agency, was to be an independent agency to give the General Assembly members a different look than just a partisan view.

So I want to thank you for the great job you guys have been doing and all of your employees at the IFO, as well. I think one of the things that you brought up that -- one of the reasons we really changed these hearings a little bit is what yo brought up in demographics.

It is the fact that the burden of this Commonwealth is falling more and more on those who are 20 to 64 years of age. And one of the things I have been challenging young people who come to see me, and when I'm on college campuses or in high schools, the questions is what do the younger generation and the next generation beyond me want this world to look like?

And I think that's a real concern we all should have because what kind of burden do we want on our younger generation to bear?

You know, I've been to Ireland, where they have a 21 percent sales tax and a 50 percent income tax. You know, if that's what we are saddling our next generation with, we have to look at how we spend dollars and make sure that if somebody is homeless out there, what are we doing to fix that problem?

If somebody is not getting food and we

have children going to school hungry every day, what are we doing to fix that problem?

Because this country has been spending billions and billion of dollars to feed our children as well as adults, yet we still see children going to school hungry, so something is not working.

And I think that the younger generation is going to be a lot tougher on members of the General Assembly and politicians in the future about not solving problems. Just increasing taxes is not the solution. Because that demographic that we have out there in this State is really to bring more revenue in.

We really have to look at keeping our young men and women here in the State, not moving them to other States. And we're seeing a lot of that. There is no State that has better universities and colleges than Pennsylvania, nor more colleges and universities than we have.

Families today are investing billions of dollars here in Pennsylvania, in the education of their children, whether it's through school loans or it's personal loans that they may take out or borrowing from their retirement accounts. And then to see their son or daughter move out-of-State.

What that does, it adds to our costs. When you don't have a daughter or a son or family who are living here anymore, they're in other States when you need assistance, it's now being picked up by the taxpayers of Pennsylvania, rather than having a son or a daughter here who can take you to the doctor's office or help you with certain finances and advisement.

So I appreciate you pointing that out to us, but I think that's something both sides of the aisle have to come to fruition with is really addressing what do we want our next generation to deal with and how we're going to deal with those problems.

So I really appreciate, again, your testimony today. And we'll continue later. These hearings are adjourned until 1:00.

Thank you very much.

(Whereupon, the hearing adjourned.)

C E R T I F I C A T E

I hereby certify that the proceedings are contained fully and accurately in the notes taken by me on the within proceedings and that this is a correct transcript of the same.

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Tracy L. Markle, Court Reporter

Notary Public