

Testimony Before the House Appropriations Committee
Dan Hassell, Secretary
Department of Revenue
Tuesday, February 15, 2022

Chairman Saylor, Chairman Bradford, and members of the committee, thank you for the opportunity to meet with you today to discuss the budget for the Pennsylvania Department of Revenue. I am Dan Hassell, Secretary for the Department. Joining me today are Amy Gill, Deputy Secretary for Tax Policy, Christin Heidingsfelder, Deputy Secretary for Administration, and Drew Svitko, Executive Director of the Pennsylvania Lottery.

As you know, for more than 90 years the Department of Revenue has been the commonwealth agency tasked with fairly, efficiently and accurately administering the tax laws and revenue programs of the Commonwealth of Pennsylvania. We take great pride in the fact that our daily work to collect and distribute tax monies due to the commonwealth funds the vital programs and services that are essential to all Pennsylvanians.

The department also administers the Pennsylvania Lottery, which was established by law in 1971 to generate funding for programs that benefit older Pennsylvanians. This March, the Lottery will celebrate the 50th anniversary of selling its first ticket. Last fiscal year alone, the Lottery generated a record of more than \$1.238 billion to benefit older Pennsylvanians. This was the 10th consecutive year that the Lottery generated more than \$1 billion for the critical programs that benefit our commonwealth's older residents. Since selling its first ticket in 1972, the Lottery has generated more than \$32.6 billion for those critical senior programs.

This work is an important part of Governor Wolf's initiative to provide Government That Works for the people of Pennsylvania. Meanwhile, we are continuing our efforts to find ways to become more efficient and improve services for Pennsylvanians. The department established several goals in its strategic plan that are designed to improve customer service, enhance our effectiveness in tax compliance and continue boosting sales and net profits for the Lottery in a responsible manner.

Setting these goals has greatly helped the department in its objective to be a leading tax administration and public service agency known for its customer service, integrity, innovation and effectiveness. They have also helped us continue to carry out our mission as we, like others, have taken on the challenges created by the COVID-19 pandemic. Please allow me to provide an overview of some our recent work and important initiatives that are ongoing at our agency.

Success of Revenue Modernization Project

As you know, the department has been working to update its technology and computer systems to replace several legacy tax systems that have been in use at the department for many decades. The department has contracted with Fast Enterprises, LLC, a leader in its industry, to help us

with this work, which I'm proud to report has remained on time and on budget throughout the duration of this project.

Currently, our modernization project team is in the midst of executing a final major phase of the project that will involve transitioning all of the business taxes that our department administers into the Pennsylvania Tax Hub (PATH). This is the integrated tax system that we launched more than three years ago along with myPATH, the online portal where our taxpayers can file tax returns, make payments and access many other services. We expect this final phase covering our business taxes to be completed by the end of this year.

This will be a major accomplishment that follows several other significant phases of our project that are already complete. For example, we recently completed our first tax season with personal income tax (PIT) and the Property Tax/Rent Rebate Program (PTRR) transitioned into PATH. This means that our customers now have new free options available to file their PIT returns and PTRR applications on myPATH. In fact, thousands of Pennsylvanians did just that last year, which helped us take a huge step in improving customer service for our taxpayers. Here are some other statistics and facts that help to tell this great story:

- Since inception of the new system in January 2019, more than 2 million refunds have been issued out of PATH for more than \$952 million, the majority of which were issued electronically via direct deposit.
- Over 10.3 million payments have been processed in PATH for a total of more than \$22 billion. 99.9% of payments processed through PATH have not required manual intervention by a DOR employee.
- Over 31,000 property tax/rent rebate applications have been submitted via myPATH since this new service debuted on November 30, 2020. This is a significant amount when you consider this electronic filing option was never available to Pennsylvania citizens before myPATH.
- myPATH users have remitted over 350,000 payments and more than 350,000 returns so far.
- The new portal provided International Fuel Tax Agreement (IFTA) customers with online self-service options for the first time. Over 85% of IFTA customers are now using myPATH.
- The department has realized more than a 90% reduction in the error rate in IFTA returns received via myPATH when compared to the legacy paper-based system.
- Since it debuted in February 2019, myPATH was been visited more than 1.4 million times while logged in and more than 881,000 times while not logged in.
- Over 66,000 myPATH accounts have been created since inception.

It's also important to acknowledge that this success is the result of a great deal of dedication and persistence displayed by our modernization project team, which is comprised of Revenue employees, staff from the Office of Administration's Employment, Banking & Revenue Delivery Center, and employees from Fast Enterprises, LLC. This team has done a fantastic job since the outset of this project. We are very much looking forward to continuing this work of providing new tools and online resources for our customers.

Lottery Success

As noted earlier in my testimony, the Pennsylvania Lottery closed another fantastic fiscal year in 2021-22 by generating more than \$1.238 billion for programs that benefit older Pennsylvanians. This was a record profit year in which we continued to generate funds for senior programs, including property tax and rent rebates, free and reduced-fare transportation, prescription assistance, and more.

Here are some other highlights from the fiscal year that ran from July 1, 2020 to June 30, 2021:

- Sales of Scratch-Off games totaled a record of more than \$3.7 billion, up by \$554.6 million, or over 17 percent, from the previous year and surpassing the previous record of more than \$3.2 billion in 2019-20. These games account for more than 70 percent of total traditional sales.
- Sales of Draw Games — including the PICK family of games and Wild Ball, Treasure Hunt, Cash 5 with Quick Cash, Match 6 Lotto, Millionaire Raffle, Cash4Life®, Powerball®, and Mega Millions® — totaled more than \$1.3 billion for the fiscal year, an increase of \$235.9 million, or 21 percent, from the previous year's total. This fiscal year, there were several large Powerball® and Mega Millions® jackpots that drove sales. That includes a record \$516 Mega Millions® winning ticket sold in Bucks County for the May 21 drawing.
- The Lottery's \$908 million in online play was an increase of \$173 million, or more than 24 percent, from the prior fiscal year.
- Sales of Monitor Games, which include Keno and Xpress Sports games, totaled an estimated \$54.9 million this fiscal year, an increase of more than \$1.2 million, or 2 percent, from the previous fiscal year.
- Traditional game prizes paid to winners grew to a record of more than \$3.418 billion, an increase of nearly \$569 million. A total of 97 winning tickets of \$1 million or more were paid to players during the 2020-21 fiscal year.
- More than \$786.6 million in prizes were paid out to winners of online Lottery games. This was an increase of \$106 million from the prior fiscal year. This does not include prizes paid to winners who purchased Draw Games online.

- More than 9,900 licensed Lottery retailers statewide, many of them small and family-owned businesses, earned an estimated \$329.1 million in sales commissions. That's an increase of \$71.6 million from the previous fiscal year.

As you can see above, our brick-and-mortar retailers continue to be the bedrock of our business. Scratch-Off games are incredibly popular with our players, and sales trends thus far in the 2021-22 fiscal year confirm that is still very much the case.

In addition to the great success that we have seen from our products offered at retail, our online games also continue to be greatly successful. We launched our online games in May of 2018 after the General Assembly passed Act 42 of 2017. We first started selling online by offering internet instant games. We have since launched several draw games online, including Powerball, Mega Millions, Cash4Life and Treasure Hunt. We expect to debut additional draw games online in the near future, which we are confident will be popular with our players.

We are incredibly proud of all of the progress that we've made to incorporate innovative ideas and expand the Lottery's portfolio of products. By becoming more diversified, we are in a better position to continue funding the vital programs that Pennsylvania's older residents rely upon.

However, as we continue to move forward with these efforts to diversify the Lottery's business, we must also acknowledge the tremendous harm that the illegal gambling machines marketed as "skill games" are causing for the Lottery. As we have shared with you in past conversations, these games are rapidly spreading at bars, convenience stores and other locations across Pennsylvania. As a result, they are siphoning off millions of dollars in funding for the senior programs that older Pennsylvanians rely upon.

We are urging the General Assembly to take action to address these illegal machines and ensure that Pennsylvania seniors will continue to receive property tax relief, meals on wheels, services at senior centers, low-cost prescription drugs and other critical support that the Lottery funds on an annual basis.

In addition to the elimination of illegal competition, another tool which would ensure the Lottery can continue to thrive in a highly-competitive entertainment market is the elimination of the statutory minimum profit margin. The requirement that the Lottery focus on the profit percentage is in direct conflict with the Lottery's mission of generating profit dollars. Act 97 of 2019 provided a temporary reduction of the mandated margin rate of return from 25 percent to 20 percent through June 30, 2024. This budget proposes to eliminate the mandated margin rate of return.

Governor Wolf's Budget Initiatives

During Governor Wolf's two terms as governor, the commonwealth has regained a strong financial position. After inheriting a \$2 billion to \$3 billion deficit, the administration's

responsible fiscal policies have resulted in a surplus. In January 2015, the Rainy Day Fund had a balance of \$231,000. Through key investments of state and federal funds in the infrastructure, workforce, and people of Pennsylvania, the Rainy Day Fund has a current balance of \$2.865 billion. In 2018-19, roughly \$316 million was transferred to the Rainy Day Fund, and the end of 2020-21 allowed for an additional \$2.6 billion deposit. The budget Governor Wolf is proposing continues this trend of fiscal responsibility while allowing unprecedented levels of investments in services that impact the everyday lives of Pennsylvania citizens.

Business Tax Reform — CNIT Rate Reduction and Modernization: Governor Wolf again proposes to reform the way Pennsylvania taxes corporations. This plan will improve the competitiveness of the commonwealth’s economy by lowering the tax rate and expanding our tax base by strengthening addbacks, codifying economic nexus rules and updating the apportionment of intangible receipts, all to level the playing field for businesses in Pennsylvania.

The proposal decreases the corporate net income tax (CNIT) rate from the current 9.99% rate, the second highest in the nation, to 7.99% effective 1/1/23, 6.99% effective for TY 2026, 5.99% by 2027, and on a path to reaching 4.99% in the future. Currently, 29 other states have top marginal rates higher than 5.99%.

Tax Year	2022	2023	2024	2025	2026	2027
CNIT Rate	9.99%	7.99%	7.99%	7.99%	6.99%	5.99%

A lower CNIT rate may make it easier to attract companies that look elsewhere for business expansion or development because of the “sticker shock” of the current tax rate. Furthermore, the Governor’s plan will level the playing field through modernization of our tax structure. Under the proposal:

- The commonwealth would strengthen our existing addbacks for corporations, by adding intercompany management fees and strengthening the addback on intercompany royalties and interest.
- Prior to the COVID-19 pandemic, the Department of Revenue issued Corporation Tax Bulletin 2019-04, related to economic nexus. This proposal aims to codify this already effective policy into statute. Doing so will ensure that businesses that are operating in Pennsylvania, but located out of state, are subject to the same rules as our Pennsylvania based businesses.
- Finally, this proposal seeks to align the current sourcing rules for the sales of intangibles to those used for services. Under current law, receipts from intangible property are apportioned based on the location of the income producing activity and potentially the costs of performance, while receipts from services are subject to market sourcing rules. This proposal will apply market sourcing rules to intangible related receipts.

Together, these three changes make it more difficult for multi-state corporations to shift profits out of Pennsylvania while leveling the playing field for corporations that operate primarily or exclusively in PA while not engaging in tax planning strategies. These changes are all effective for tax year beginning 1/1/23 — same as the rate reduction.

Finally, it’s important to note that when fully phased in, these modernizations and the rate reductions will provide a substantial tax cut for corporations while promoting a level playing field. All impacts are in millions of dollars.

Fiscal Year	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Revenue	0.0	(79.4)	(140.9)	(140.8)	(270.5)	(645.1)

The proposal advances the principles of good tax policy by broadening the corporate tax base and lowering the rate. These changes also promote economic efficiency by removing an incentive that may distort taxpayer behavior and detract from economic growth.

Raising the Minimum Wage: Governor Wolf is also renewing his call to raise Pennsylvania’s minimum wage to \$12 an hour with a pathway to \$15. The Governor’s proposal raises the minimum wage to \$12 an hour on July 1, 2022 with annual 50 cent increases until reaching \$15 an hour in 2028.

The Governor’s proposal would give raises to an estimated 765,000 workers, provide better financial stability for women, rural, and tipped workers, while enabling thousands of people to work their way off public assistance and grow the economy for everyone.

The minimum wage has not been increased since 2009 and Pennsylvania is surrounded by states with the following minimum wages: Delaware (\$10.50); Maryland (\$12.20); New Jersey (\$13); New York (\$13.20); Ohio (\$9.30); and West Virginia (\$8.75). Additionally, Pennsylvania’s minimum wage of \$7.25 amounts to \$15,080 per year for a full-time worker and cannot support a family, especially as the cost of living for Pennsylvanians increases and purchasing power decreases.

Providing Immediate Relief for Pennsylvanians Impacted by the Pandemic: Governor Wolf is also proposing to use \$1.7 billion in funds from the American Rescue Plan Act (ARPA) to help Pennsylvania fully recover from the pandemic and pave the way for a successful future. This proposal provides support for families and workers, small businesses, the healthcare system, and statewide community revitalization.

The PA Opportunity Program, \$500 million

Pennsylvanians are resilient, yet many workers and families are still covering pandemic-related costs, stabilizing their budgets, and rebuilding their savings.

The PA Opportunity Program would provide much needed relief to workers and families from the high cost of childcare and household expenses and opportunities to complete a degree, credential, or license that will strengthen their skills and increase income — all leading to a better quality of life.

Small Business Support, \$225 million

The COVID Relief Statewide Small Business Assistance Program would provide grants ranging from \$5,000 to \$50,000 to small businesses that have been economically impacted by the pandemic. Among other things, businesses can use these grants to cover operating expenses and access technical assistance, including training and guidance to stabilize and relaunch their businesses. The program would prioritize women- and minority-owned businesses and rural communities. Gov. Wolf proposes to recapitalize this program at \$225 million to help approximately 11,000 additional businesses.

Increased Property Relief for Low-Income Renters & Homeowners, \$204 million

To provide direct property tax relief to Pennsylvanians, Gov. Wolf wants to invest an additional \$204 million into the existing Property Tax Rent Rebate program for a one-time bonus rebate to current program users. This investment would double existing rebates. An estimated 466,000 Pennsylvanians would receive an additional average rebate of \$475.

Support for Pennsylvania’s Healthcare System, \$325 million

This investment would recognize healthcare workers for their heroic dedication and hard work throughout the pandemic and give healthcare providers resources to recruit and retain a skilled workforce. Specifically,

- \$250 million for long-term care recruitment and retention incentives and workforce development initiatives to grow the critical healthcare workforce;
- \$40 million for the behavioral health workforce to expand county mental health programs; and
- \$35 million to expand the student loan forgiveness program at PHEAA to include additional critical healthcare workers.

Investing in Conservation, Recreation & Preservation, \$450 million

Pennsylvania must continue to invest in vital conservation, recreation, preservation, and community revitalization projects and address the threat of climate change. Gov. Wolf’s plan proposes new funding for the Growing Greener conservation and recreation program as well as for agriculture conservation programs, such as the Agricultural Conservation Assistance Program and the existing Agriculture Conservation Excellence Grant Program.

After experiencing record-breaking rainfall and flooding events this past year, this program would make Pennsylvania more resilient in the face of more extreme and frequent weather events caused by climate change. It would support our economy, enhance our communities, and improve quality of life for all Pennsylvanians.

In closing, I look forward to working with each of you in the weeks ahead. Thank you for the opportunity to provide testimony on behalf of the Department and Revenue and the Lottery. My colleagues and I look forward to answering your questions.