

Testimony Before the House Appropriations Committee
Dan Hassell, Secretary
Department of Revenue
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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 in the early 1970s to generate funding for programs that benefit older Pennsylvanians. Last fiscal year, the Lottery generated \$1.14 billion to benefit older Pennsylvanians. This was the ninth consecutive year that the Lottery generated more than \$1 billion for the critical programs that benefit our commonwealth's older residents.

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.

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 during the COVID-19 pandemic. Please allow me to share with you an overview of how the department has functioned during this health crisis, as well as several other initiatives that are ongoing.

Functioning During the COVID-19 Pandemic

Similar to many agencies in the public and private sectors, the COVID-19 pandemic created a number of challenges for the Department of Revenue. In mid-March when the first cases of COVID-19 were confirmed in Pennsylvania, we initially closed all of Revenue's and Lottery's offices. This included all Revenue district offices where taxpayers find in-person assistance and our Lottery district offices where players submit their claims for winning tickets.

Closing our Revenue headquarters also meant we were forced to close our main call center, meaning there was no way for our phone agents to receive incoming calls from taxpayers. Customer service was limited to electronic inquiries submitted through our Online Customer Service Center on the department's website. Meanwhile, all of Revenue's noticing and collection activities ceased while our incoming and outgoing paper mail stopped.

As this process played out, there was a significant portion of our workforce that was not equipped to work remotely. That led us to move quickly as possible to equip the majority of our employees to work from home by placing orders for additional laptops. Fortunately, as this process was ongoing, we were able to continue all of our core functions, meaning that revenue continued to flow into the commonwealth's coffers while Lottery drawings and the processing of prize claims continued as usual.

Despite the operational challenges caused by the pandemic, most of our operations returned to normal by the end of summer. By that point, more than 80 percent of our employees were equipped to work remotely. All tax season paper checks had been deposited by this time. We resumed most normal processes for outgoing and incoming mail, tax return review, refund issuance and appeal review. Our Lottery district sales representatives returned to work in the field. We also reopened Revenue and Lottery district offices in a limited capacity, meaning taxpayers and Lottery players could seek in-person assistance by scheduling an appointment and adhering to social distancing and health protocols that were put in place.

In addition to tackling the challenges that our own agency encountered as a result of the pandemic, I'm proud to say that we also offered assistance to other commonwealth agencies. More than 100 of our employees were temporarily reassigned to the departments of Labor and Industry and State. Our staff helped answer inquiries from the public as both of our sister agencies worked through a sizable volume of inquiries concerning unemployment compensation questions and election concerns.

Looking back at the last 11 months, it is amazing to consider the progress we've made and all of the contributions from our staff that helped us work through this unprecedented situation. It is a testament to the hard work and dedication of Revenue and Lottery employees that our agency continued to perform its core functions despite the challenges created by this health crisis. We also received valuable support from staff in other agencies under Governor Wolf's jurisdiction, including the Office of Administration, to continue delivering services for the citizens of our commonwealth.

Providing Support to Pennsylvanians During the Pandemic

As we worked through the operational challenges noted above, we also spent a considerable amount of time contemplating steps the Department of Revenue could take to ease the burdens on our taxpayers during the pandemic. Recognizing that many Pennsylvanians and Pennsylvania businesses were facing their own challenges, we took the step of extending many tax filing and

payment deadlines. This provided more time for our individual and business taxpayers to address their tax obligations so that they could focus on their health and safety.

Recognizing the financial strains imposed by the pandemic, the department also announced the easing of tax enforcement activities. The department took steps to:

- Suspend automatic enforcement actions regarding liens, license revocations and referrals to collection agencies.
- Abate penalties in most cases if taxpayers remitted trust fund taxes they collected.
- Offer audit penalty abatement and 90-day interest relief through December 31, 2020.
- Provide flexibility with scheduling planned audit work.
- Offer to delay payment plans due to hardship and provide flexible terms for new payment plans.
- Redeploy enforcement personnel to provide taxpayer assistance as well as outreach and education on tax compliance.

These steps were well-received and helped us avoid placing unnecessary burdens on our taxpayers during a tumultuous time. We have since resumed many of our routine compliance and collections activities. However, we are still taking steps to work with our taxpayers due to the fact that many are still struggling due to the pandemic. We plan to continue this customer-focused approach in the months ahead.

I'm also proud to report that the department has taken steps during the COVID-19 pandemic to help claimants of the Property Tax/Rent Rebate Program, which annually provides relief to older and disabled Pennsylvanians. Following the passage of Act 20 of 2020, the department worked with staff from the Treasury Department to distribute more than 310,000 rebates earlier than the normal July 1 distribution date. This action helped to provide nearly \$162 million in relief roughly six weeks ahead of the normal schedule. This allowed us to provide claimants of the program with relief during a time when many of our commonwealth's residents needed the support. This was a great example of our staff working collaboratively with Treasury's employees to quickly implement a commonsense solution that made a big difference for thousands of our older and disabled Pennsylvanians. Since that time, we have continued working to make sure that all claimants receive their rebates as quickly as possible.

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.

In November 2020, we reached an important milestone when our modernization project team successfully transitioned personal income tax (PIT), pass through entity (PTE) processing and the Property Tax/Rent Rebate Program (PTRR) into the Pennsylvania Tax Hub (PATH), the tax system that we launched in early 2019. This was by far our largest and most complex rollout to date for our modernization project and also included implementation of Fast Data Services, a version upgrade, and replacement of a number of our large legacy applications. As a result of our team's work, we have replaced those decades-old applications with a new, cutting edge tax system that will provide more than 6 million Pennsylvanians with access to new electronic filing options through myPATH, our online self-service portal.

For example, myPATH now offers a new option for the electronic filing of personal income tax returns and payments. Additionally, the system also offers an electronic filing option for the Property Tax/Rent Rebate Program. This is the first time in the history of that program that there is an electronic filing option for the older and disabled Pennsylvanians who benefit each year from rebates on property taxes and rent they have paid. These new resources are great examples of our department taking steps to continually improve customer service for the people of Pennsylvania.

I must also acknowledge that this progress 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. Not only did this team of more than 100 work through the Thanksgiving holiday last winter to ensure this rollout involving PIT, PTE and PTRR was completed successfully, but they also achieved this while working remotely due to the COVID-19 pandemic. This was a huge shift that created many challenges, but the project team persevered and kept the project on time and on budget. Here are some other important achievements from this phase of our project:

- The team converted more than 12 million accounts and more than \$13 billion in outstanding payments as part of this rollout. When considering all projects from Fast Enterprises' 23-year history, this was the largest personal income tax rollout in the United States in terms of data converted. Fast Enterprises has worked with tax administration agencies in many jurisdictions throughout the country and across the world.
- More than 680 users were trained in PATH prior to this rollout. This group included personnel from 12 Revenue bureaus and two within the Treasury Department. More than 200 training classes encompassing 38 courses were all conducted remotely, which was a new and unforeseen challenge the project team overcame.
- The project team reviewed legacy taxpayer letters, rewriting many with an emphasis on plain language. Meanwhile, the team reviewed and overhauled our legacy hold and error codes, reducing our total number of codes by 48 percent.

- The project remained on time and on budget despite the fact that a significant portion of our workforce was not equipped to telework when the pandemic reached Pennsylvania. In spite of these difficulties, we stayed on track. That is a testament to the project team's hard work and dedication.

We have recently started work on the next phase of our modernization project, which will focus on transitioning some smaller and miscellaneous taxes and programs into PATH. We expect that phase to be completed in the summer of 2021. After that, we will start the work of transitioning all of our business taxes into the PATH system. We expect that work to conclude late in 2022.

We are very much looking forward to continuing this work of providing new tools and online resources for our customers. We are proud to say that our modernization project has been a great success thus far.

Lottery Success

As noted earlier in my testimony, the Pennsylvania Lottery closed another fantastic fiscal year in 2019-20 by generating \$1.14 billion for programs that benefit older Pennsylvanians. Despite the pandemic, Lottery sales have continued to be strong during the first half of the 2020-21 fiscal year.

Here are some other highlights from the fiscal year that ran from July 1, 2019 to June 30, 2020:

- Lottery sold nearly \$4.47 billion through its traditional games, which include Scratch-Off, Draw and Monitor games. Meanwhile, the Lottery also recorded \$731 million in online play.
- Traditional game prizes paid to winners grew to a record of more than \$2.9 billion, an increase of nearly \$481,000. A total of 79 winning tickets of \$1 million or more were paid to players during the fiscal year.
- Sales of Scratch-Off games totaled a record of more than \$3.2 billion, up by \$213.5 million, or over 7 percent, from the previous year and surpassing the previous record of \$2.9 billion in 2018-19. These games account for close to 72 percent of total sales.
- Sales of Draw Games – including the PICK family of games and Wild Ball, Treasure Hunt, Cash 5, Match 6 Lotto, Millionaire Raffle, Cash4Life®, Powerball®, and Mega Millions® – totaled more than \$1.1 billion for the fiscal year, a decrease of \$253.8 million, or 18.6 percent, from the previous year's total. Unlike the 2018-19 fiscal year, when there were several large Powerball® and Mega Millions® jackpots, there were no record jackpots in multi-state games to drive sales last fiscal year.

- More than \$639 million in prizes were paid out to iLottery winners, in addition to a \$1 million Mega Millions® prize that was awarded to a player who bought a Mega Millions ticket on pailottery.com.
- Sales of Monitor Games, which include Keno and Xpress Sports games, totaled an estimated \$53.7 million this fiscal year, an increase of almost \$7 million, or 15 percent, from the previous fiscal year.
- More than 9,600 licensed Lottery retailers statewide, many of them small and family-owned businesses, earned an estimated \$257 million in sales commissions.

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 2020-21 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 have also been greatly successful. We launched our online games in May of 2018 after the General Assembly passed Act 42 of 2017. Online sales hit the \$1 billion mark just before the second anniversary of the launch of our online games, and we are continually working to offer new online games that appeal to our players. We first started selling online by offering internet instant games. We have since launched several draw games online. That lineup now includes Powerball, Mega Millions, Cash4Life and Treasure Hunt.

We're proud 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 "Pennsylvania Skill Games" are causing for the Lottery. As we have shared with you in past conversation, 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.

Governor Wolf Budget Initiatives

For the upcoming fiscal year's budget, Governor Wolf is proposing a multi-faceted revenue package that is designed to make Pennsylvania a better place to live and work. The plan addresses Pennsylvania's tax system, which is one of the most unfair and regressive in the

country, by expanding the special tax forgiveness credit and changing the Personal Income Tax rate. The COVID-19 pandemic has exposed the inherent unfairness and inequity in our current system, with the most vulnerable Pennsylvanians bearing the brunt of the pandemic while many of the wealthiest became even more prosperous. It is time to remove these barriers. As part of the Governor's plan to cut taxes for working families and businesses, he is also proposing historic investments in education and workforce development.

Creating a More Equitable Tax Structure: The Governor is proposing a significant expansion of the Tax Forgiveness program, which gives Pennsylvanians a refund or reduction of their income tax liabilities depending on their income and family size. Under current Pennsylvania law, the current tax forgiveness thresholds are \$6,500 per claimant and \$9,500 per dependent with a 10% decrease in forgiveness for every \$250 in additional income. The Governor proposes raising those thresholds to \$15,000 per claimant and \$10,000 per dependent with a 1% decrease in forgiveness for every \$500 in additional income. This will greatly expand the number of taxpayers that receive relief from the Personal Income Tax. This proposal is also coupled with an increase of the PIT rate from 3.07% to 4.49%.

Raising the thresholds for tax forgiveness is long overdue. The thresholds for this program have not been increased since tax year 2003. Accounting for inflation, the parameters for tax year 2021 would need to be over \$48,000 just to keep the same level of income for forgiveness. Conceptually, the increase in tax forgiveness really just helps families keep up with inflation.

Moreover, the increase in tax forgiveness is a commonsense action to uniformly provide additional support to our most vulnerable citizens in Pennsylvania. The PIT proposal also improves the fairness of the commonwealth's tax on individual income by shifting the tax burden from lower income taxpayers to higher income taxpayers. There are also benefits for small business owners. Below are some important facts to consider:

- Under the proposal, 2.8 million families will pay less in PIT in tax year 2021 than they currently do, receiving a total tax cut of \$1.5 billion. The average tax decrease for these families is \$536. The average family income for those affected is almost \$32,900.
- Under current law, a family of four making \$32,000 pays no PIT. Under this proposal, a family of four with income up to \$50,000 pays no PIT. This level is approximately 200% of the federal poverty level for a family of four.
- In tax year 2021, more than 767,000 families who pay tax under current law will now pay \$0. The average tax decrease is almost \$480.
- Over 400,000 business owners will pay less tax under this proposal than they currently do, receiving a total tax cut of over \$240 million.

- For the 727,930 small business owners who earn less than \$100,000, 64% pay the same or less tax after full implementation of this proposal. The average tax decrease is nearly \$600.
- Most current tax forgiveness recipients, some 1.7 million families, will see no change in tax liability.
- In tax year 2021, 1.9 million families will pay more in PIT than they do currently. 83.4% of the tax increase is borne by taxpayers making more than \$100,000 in current taxable income.
- Under the proposal, a single taxpayer with no dependent will pay no tax at \$15,000 in taxable income, and will pay less under the proposal until he/she earns more than \$49,000.
- Under the proposal, married taxpayers with two dependents will pay no tax up to \$50,000 in income, and will pay less under the proposal until they earn more than \$84,000.

With the new PIT rate, Pennsylvania will still have the fourth lowest top marginal rate out of the 43 states that have a PIT. Meanwhile, the Governor's proposal will be a way to update the commonwealth's tax code to deliver historic tax cuts for working class families and low-income Pennsylvanians while helping them build financial security and reach for a brighter future. It's time to put working class and low-income families first, and make our system fairer for those who need help the most.

Implementing Combined Reporting and Phase Down of the CNIT Rate: The Governor's plan proposes to level the playing field for all businesses with the adoption of combined reporting and a coinciding phase down of the corporate tax rate, which currently stands at 9.99 percent rate, the second highest in the nation. The tax rate will be set at 8.99 percent in 2022, 8.29 percent in 2023, 7.49 percent in 2024, 6.99 percent in 2025, and 5.99 percent in 2026. This will make it easier to attract business development that is turned away by the "sticker shock" of the current 9.99 percent tax rate.

At the same time, the Governor is proposing that combined reporting be required for taxpayers who are part of a controlled group of corporations. Under current law, each separate corporation reports Pennsylvania tax on its own income, even if it is part of a larger corporate group. This allows certain corporations to shelter income from tax with Delaware holding companies and similar inter-company transactions within the group.

Under combined reporting, corporations in a group will figure their income for the entire group, and each separate company owes tax on a share of the group income. Transactions between members of the group are eliminated, making it harder to shelter corporate income from state taxation.

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, 2021 with annual 50 cent increases until reaching \$15 an hour in 2027.

The Governor's proposal would give a direct wage increase to 1 million workers, provide better financial stability for women, rural, and tipped workers, enable thousands of people to work their way off public assistance and grow the economy for everyone.

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.