REVENUE ESTIMATES

In 2020 there was a dramatic decline in economic activity in the second quarter, followed by an uneven recovery for the remainder of the year. For 2021, the economy, buoyed by multiple rounds of federal stimulus, an accommodative monetary policy, a massive vaccination program and the consequent reopening of the economy, appears poised for rapid expansion through the remainder of 2021 and continued growth in 2022 and beyond. This improvement in the projected path of economic activity has led to a significant improvement in the revenue forecast. In addition to the improved economic picture, stock markets have continued to show strength, and wage withholding has continued to outpace even the upgraded wage growth forecast; both factors lead to higher revenue projections. All three major revenue sources are expected to show significant increases relative to the Governor's Budget forecast. The changes in the three largest tax sources are:

- Personal income tax revenues are revised up by almost $38 billion due to a more optimistic economic outlook, but particularly wages, proprietorship income, and capital gains.
- Sales tax receipts have been revised upward by $4.5 billion due to an upgraded forecast for taxable consumer spending and private investment.
- Corporation tax revenues are up almost $4.6 billion based on strong cash receipts and faster than anticipated recovery from the economic impacts of the COVID-19 Pandemic.

After accounting for transfers, which includes loan repayments as well as automatic and discretionary transfers to the Rainy Day Fund, baseline General Fund revenues at the May Revision forecast are up relative to the Governor's Budget by $41.6 billion over the budget window; lower than the Governor's Budget by $224 million in 2019-20, and higher by $24.3 billion in 2020-21 and $17.6 billion in 2021-22.

On March 29, 2021, the federal government delayed the Internal Revenue Service tax filing deadline for personal income tax returns, along with payments associated with those returns, from April 15 to May 17. The state conformed to the federal deadline. It is anticipated that a large amount of personal income tax payments that would typically be received in April will be deferred until May. The delay in receiving payments is not expected to affect revenue as the deferred payments will be received in the same fiscal year; however, it does increase the near-term uncertainty of the May Revision forecast as less was known about April payments prior to the forecast than in a typical year.

The General Fund Revenue Forecast table compares the revenue forecasts by source in the Governor's Budget to the May Revision forecast.

2021-22 May Revision
General Fund Revenue Forecast
(Dollars in Millions)

Source	2021-22 Governor's Budget	May Revision	Change From Governor's Budget Forecast	
Fiscal 2019-20: Preliminary				
Personal Income Tax	$99,509	$99,599	$89	0.1%
Sales & Use Tax	25,495	25,509	13	0.1%
Corporation Tax	14,035	13,954	-82	-0.6%
Insurance Tax	3,128	3,135	7	0.2%
Alcoholic Beverage	383	383	0	0.0%
Cigarette	60	60	0	0.0%
Pooled Money Interest	516	521	5	0.9%
Other Revenues	1,943	1,923	-21	-1.1%
Subtotal	$145,070	$145,082	$12	0.0%
Transfers[1/]	-4,447	-4,682	-235	5.3%
Total	**$140,623**	**$140,400**	**-$224**	-0.2%
Fiscal 2020-21				
Personal Income Tax	$102,208	$124,151	$21,942	21.5%
Sales & Use Tax	$26,508	$27,936	1,428	5.4%
Corporation Tax	$16,948	$20,120	3,172	18.7%
Insurance Tax	$3,253	$3,348	95	2.9%
Alcoholic Beverage	$385	$385	0	0.0%
Cigarette	$55	$60	5	9.6%
Pooled Money Interest	$105	$126	21	20.3%
Other Revenues	$4,158	$3,215	-944	-22.7%
Subtotal	$153,621	$179,342	$25,721	16.7%
Transfers[1/]	9,121	7,678	-1,443	-15.8%
Total	**$162,742**	**$187,020**	**$24,277**	14.9%
Fiscal 2021-22				
Personal Income Tax	$107,360	$123,298	$15,938	14.8%
Sales & Use Tax	$25,925	$28,986	3,061	11.8%
Corporation Tax	$16,636	$18,106	1,470	8.8%
Insurance Tax	$3,319	$3,428	109	3.3%
Alcoholic Beverage	$389	$390	0	0.1%
Cigarette	$46	$58	12	25.2%
Pooled Money Interest	$22	$83	61	272.8%
Other Revenues	$7,876	$7,397	-479	-6.1%
Subtotal	$161,574	$181,745	$20,171	12.5%
Transfers[1/]	-3,204	-5,824	-2,620	81.8%
Total	**$158,370**	**$175,921**	**$17,551**	11.1%
Three-Year Total			**$41,605**	

Totals may not add because of rounding.

[1/]Includes transfers to Budget Stabilization Account for each year.

LONG-TERM FORECAST

The Long-Term Revenue Forecast table below shows the forecast for the largest three sources of General Fund revenues from 2019-20 through 2024-25. Total General Fund revenues from these sources are expected to increase from $139.1 billion in 2019-20 to $181.3 billion in 2024-25. The majority of the increase occurs in the current year 2020-21 as revenues are expected to surge 23.8 percent.

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	Average Year-Over-Year Growth
Personal Income Tax	$99.6	$124.2	$123.3	$128.5	$131.2	$133.6	6.4%
Sales and Use Tax	$25.5	$27.9	$29.0	$29.1	$29.8	$30.5	3.7%
Corporation Tax	$14.0	$20.1	$18.1	$17.4	$16.8	$17.2	5.9%
Total	**$139.1**	**$172.2**	**$170.4**	**$175.0**	**$177.8**	**$181.3**	5.8%
Growth	-0.3%	23.8%	-1.1%	2.7%	1.6%	2.0%	

Note: Numbers may not add due to rounding.
Source: California Department of Finance, May Revision Forecast

PERSONAL INCOME TAX

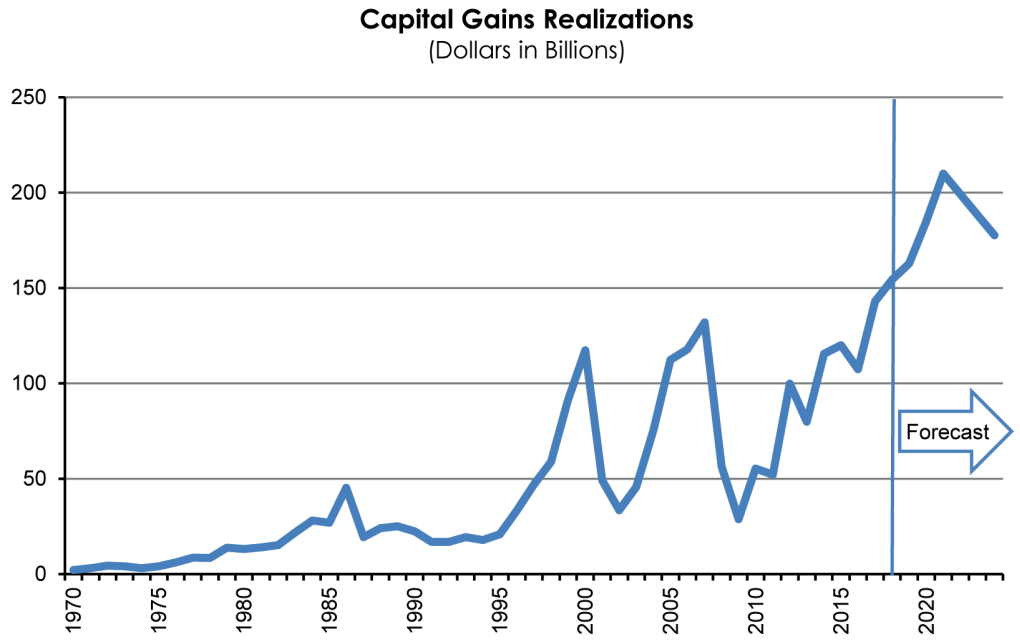
Compared to the Governor's Budget forecast, the personal income tax forecast is higher by $89 million in 2019-20, $21.9 billion in 2020-21, and $15.9 billion in 2021-22. Over the three-year period, the personal income tax forecast reflects a total increase of $38 billion.

Due to stronger wage growth for existing employees, as well as lower unemployment than forecast in the Governor's Budget, taxable wages have been revised higher, which positively impacts personal income tax wage withholding receipts. Typically, wages comprise around 55 percent to 60 percent of all personal income tax receipts. Taxable wages were revised from 1.4 percent growth to 3.7 percent in 2021, and from 3.5 percent growth to 6.3 percent in 2022.

Personal income tax wage withholding receipts were very strong in 2020, with 7.4 percent year-over-year growth, despite the pandemic, compared to 5.6 percent in the Governor's Budget. Further, the first 4 months of 2021 have shown very strong year-over-year growth of 13.9 percent, which continues to reflect a larger share of the wage gains going to high-income earners with higher effective tax rates. As a result,

withholding growth in 2021 has been revised to 7.3 percent compared to 1.3 percent in the Governor's Budget.

The S&P 500 has significantly outperformed the expectations in the Governor's Budget and is forecast to be at 4,147 in the second quarter of 2021. This is a significant upgrade from the Governor's Budget, which assumed that the S&P 500 would be at 3,586 in the second quarter of 2021, or nearly 14 percent lower. This upgraded market forecast leads to a significant increase in the forecast for capital gains realizations from $173 billion to $185 billion in 2020 (see figure with Capital Gains Realizations), $185 billion to $210 billion in 2021, and $177 billion to $199 billion in 2022. Capital gains realizations are forecast to return to a lower level of 4.5 percent of personal income by 2026 at $156 billion as high market valuations are expected to lead to a 2 percent annual decline in the S&P 500 from current levels.



Forecasting revenues associated with capital gains is subject to significant uncertainty because realizations are heavily dependent upon stock market performance and when taxpayers choose to buy or sell stock. Stock market performance is inherently unpredictable. In the last recession, the S&P 500 dropped by over 50 percent; in the technology-driven recession of 2001, it dropped by about 47 percent. The personal income tax forecast includes Propositions 30 and 55 revenues, which are estimated at $9.8 billion in 2019-20 and $11.1 billion in 2020-21. These estimates are higher than the Governor's Budget by $797 million and $1.6 billion, respectively, due primarily to higher wages and capital gains realizations.

The highest-income Californians continue to pay a very large share of the state's personal income tax. For the 2018 tax year, the top one percent of income earners paid over 46 percent of personal income taxes. This percentage has been greater than 40 percent for 14 of the last 15 years.

The personal income tax forecast is significantly affected by two major tax policies. First, the Golden State Stimulus is expected to provide $2.8 billion in tax refunds to 4.5 million low-income households in California. This estimate is up from $2.4 billion in the Governor's Budget and as of early May, $1.5 billion in tax refunds had already been distributed. Second, AB 80 (2021) conformed state law, with modifications, to federal law with regard to the tax treatment of forgiven PPP loans and is expected to decrease personal income tax revenues by $70 million in 2020-21 and $1.5 billion in 2021-22, with an additional $1.6 billion in revenue losses in the subsequent four fiscal years.

SALES AND USE TAX

The sales tax forecast is higher by $1.4 billion in 2020-21 and $3.1 billion in 2021-22. Taxable sales are expected to increase by 8.1 percent in 2020-21 and a further 5.7 percent in 2021-22. In the Governor's Budget, taxable sales were expected to grow 4.1 percent in 2020-21 and decline by 0.8 percent in 2021-22.

Taxable consumer spending is expected to be higher than Governor's Budget by 4.4 percent in 2020-21 and by 11 percent in 2021-22. Taxable sales have remained strong throughout the pandemic, in large part due to a shift in consumer spending from services to durable goods, which are more likely to be taxed. Of the industries that generate significant taxable consumer sales, non-store retailers, building material and garden improvement stores, and new car dealers have seen strong sales growth during the pandemic. This shift from goods to services spending is expected to unwind somewhat as the vaccine rollout continues, lockdowns end, and services become more accessible.

Taxable capital investment, which is expected to be the primary driver of taxable sales growth in 2021-22, is expected to be greater than Governor's Budget by 5.7 percent in 2020-21 and 18.4 percent in 2021-22. Investment is expected to benefit from low interest rates and a ramp-up in businesses' productive capacity in response to increased sales.

CORPORATION TAX

The corporation tax forecast is lower by $82 million in 2019-20, higher by $3.2 billion in 2020-21, and higher by $1.5 billion in 2021-22. Due to a lower-than-expected impact of the pandemic on corporation profits, particularly large multi-state corporations that pay the majority of the corporate tax revenues, corporate profits are expected to decline only 3 percent in 2020-21 and then grow 8 percent in 2021-22. In the Governor's Budget, corporate profits were forecast to decline by 7 percent in 2020-21 and grow by 1.8 percent in 2021-22.

The corporation tax forecast includes the impact of two major tax policies that have offsetting revenue impacts. First, AB 80 (2021) conformed state law, with modifications, to federal law with regard to the tax treatment of forgiven PPP loans and is expected to decrease corporation tax revenues by $70 million in 2020-21 and $1.5 billion in 2021-22, with an additional $1.6 billion in revenue losses in the subsequent four fiscal years.

Second, the elective pass-through entity tax is intended to help California business owners by allowing them to partially circumvent the $10,000 limit of state and local tax deductions that was imposed as part of the 2017 federal Tax Cut and Jobs Act. The proposal is intended to be revenue neutral as the tax paid electively by the entity is equal to the credit generated at the entity owner level. However the actual behavior of taxpayers and timing of payments is uncertain, with some personal income taxpayers who are not able to fully use the credits generated potentially electing to pay higher state taxes in return for significantly reduced federal taxes. The proposal is currently scored as increasing corporate tax revenue by $1.3 billion in 2021-22 and $650 million in 2022-23. While the elective pass-through entity tax is scored on a net basis as affecting corporate tax revenues only, it will result in a much larger shift from personal income tax to corporate income tax as personal income tax credits are provided to taxpayers to offset the elective taxes paid at the pass-through entity level.

The corporation tax forecast includes the impact of the temporary suspension of net operating loss usage and limitation on business incentive tax credit usage adopted in the 2020 Budget Act, which was expected to increase corporation tax revenues by $3.7 billion in 2020-21 and $3.3 billion in 2021-22.

INSURANCE TAX

The insurance tax forecast is higher by $95 million in 2020-21 and by $109 million in 2021-22. Insurance tax premiums are expected to increase 6 percent in 2020 versus

growth of 4 percent assumed in the Governor's Budget, and are expected to grow 3 percent in 2021 and 2022, which is unchanged from the Governor's Budget.

CANNABIS EXCISE TAX

Proposition 64, commonly referred to as the Adult Use of Marijuana Act, levies excise taxes on the cultivation and retail sale of both recreational and medical cannabis. The cultivation tax is paid on all recreational and medicinal cultivation of cannabis, and was increased, to adjust for inflation, to $9.65 per ounce of flower, $2.89 per ounce of trim, and $1.35 per ounce of fresh cannabis plant on January 1, 2020. The next increase for inflation is scheduled to occur on January 1, 2022. In addition, there is a 15-percent tax on the retail price of cannabis. Both cannabis excise taxes together generated $491 million in 2019-20. The revenue from excise taxes was revised up from $544 million to $730 million in 2020-21 and from $658 million to $748 million in 2021-22, as cannabis sales during the Pandemic have remained relatively strong

PROPERTY TAX

The property tax is a local revenue source; however, the amount of property tax generated each year has a substantial impact on the state budget because local property tax revenues allocated to K-14 schools generally offset General Fund expenditures.

Preliminary data suggest statewide property tax revenues increased around 5.3 percent in 2020-21, which is 0.7 percentage point higher than the 4.6 percent growth rate anticipated in the Governor's Budget. Property tax revenues are expected to grow 6.4 percent in 2021-22, which is 0.9 percentage point higher than the 5.6 percent growth expected in the Governor's Budget due to strong home price growth and data that shows a higher rate of property transfers in 2020 compared to recent years. Approximately 42 percent ($37.7 billion) of 2021-22 property tax revenues will go to K-14 schools. This includes $2.7 billion that schools are expected to receive in 2021-22 pursuant to the dissolution of redevelopment agencies.

GOLDEN STATE STIMULUS II

Chapter 8, Statutes of 2021 (SB 88) enacted the Golden State Stimulus, which is expected to provide about $2.8 billion in tax refunds to low-income Californians to help deal with the economic hardship arising from the pandemic that disproportionately

affected low-income households. First, the Golden State Stimulus provides $600 to low-income households that receive the California EITC for tax year 2020. Second, the Golden State Stimulus provides a $600 payment to taxpayers with Individual Tax Identification Numbers (ITINs) and income of $75,000 or less who were excluded from some of the federal stimulus payments. In total, it is expected that 4.5 million households will receive a Golden State Stimulus payment. SB 88 also authorized 1.6 million payments of $600 to households that participate in the CalWORKs program, the Supplemental Security Income/State Supplementary Payment program, and the Cash Assistance Program for Immigrants.

The May Revision proposes a significant expansion of the Golden State Stimulus. This program significantly increases the reach of the Golden State Stimulus by extending the $600 payments to tax filers that filed a 2020 tax return and have adjusted gross income greater than $0 and up to $75,000, and wages of $75,000 or less but did not receive a payment under the first Golden State Stimulus program.

The May Revision also proposes a $500 payment to most tax filers who filed a 2020 tax return with adjusted gross income greater than $0 and up to $75,000, and wages of $75,000 or less who claim at least one dependent on their return. Receiving a payment under one aspect of Golden State Stimulus II does not preclude a household from also receiving a payment under a different aspect of the program. This program is accounted for as an expenditure rather than a revenue reduction.

TAX INCENTIVES TO STIMULATE ECONOMIC DEVELOPMENT

The May Revision continues the proposals focused on encouraging the economic recovery and the creation of jobs, providing assistance to businesses hurt by the pandemic, and promoting projects to move California closer to its clean-energy climate goals. These revenue measures are expected to cost only $18 million in 2021-22 as much of the costs of these proposals do not occur until later years. The CalCompetes grant program is not a revenue reduction but an expenditure, and the $250 million expenditure is expected to occur in the 2021-22 fiscal year. The proposals include the following:

- Expansion of the Main Street hiring tax credit by allocating $147 million to assist firms who made hires during the current fiscal year.
- One-time expansion of the CalCompetes tax credit allocations by $180 million for 2021-22.

- Creation of a one-time $250 million CalCompetes grant program for businesses that promise to meet one of the following four criteria: establish at least 500 net new jobs; make a significant infrastructure investment; commit to a high-need, high-opportunity area of the state; or receive a designation from the Director of the Governor's Office of Business and Economic Development that the application is a strategic priority of the state.
- One-time expansion of the California Alternative Energy and Advanced Transportation Financing Authority sales tax exclusion by $100 million for 2021.
- One-time expansion of the film credit program with an additional $30 million focused on relocating productions.
- Creation of an elective pass-through entity tax to allow passthrough business owners to use state taxes paid to reduce their federal taxable income.

In addition to these May Revision proposals, the Legislature took early budget action on conforming state law to the federal treatment of Paycheck Protection Program (PPP) forgiven loans. Chapter 17, Statutes of 2021 (AB 80) conformed state law, with modifications, to federal law with regard to the tax treatment of forgiven PPP loans and is expected to decrease personal income tax and corporate tax revenues by $140 million in 2020-21 and $2.9 billion in 2021-22, with an additional $3.2 billion in revenue losses in the subsequent four fiscal years. This conformity will allow a significant majority of the hundreds of thousands of small businesses in California that received a federal PPP loan that will be forgiven to avoid paying tax on that income and to be able to deduct expenses related to the forgiven loan. This tax benefit is not allowed for public companies or for companies that did not have at least a 25-percent reduction in sales in one quarter of 2020 versus a comparable quarter in 2019. AB 80 also conformed state law to federal law with regard to the tax treatment of forgiven advance grants under the federal Economic Injury Disaster Loan (EIDL) program. EIDL advance grants that did not need to be repaid were given to small businesses that operate in low-income communities and were for a maximum of $10,000.

In addition to the proposals aimed at spurring economic growth, the May Revision also removes the sunset on the sales tax exemption for diapers and menstrual products. This permanent exemption will provide ongoing assistance to women and families with young children.