



GOVERNOR YOUNGKIN'S PROPOSED 2026-2028 BUDGET

Economic Outlook and Revenue Forecast

A BRIEFING FOR THE SENATE FINANCE & APPROPRIATIONS,
HOUSE APPROPRIATIONS, AND HOUSE FINANCE COMMITTEES

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December 17, 2025

TOPICS FOR DISCUSSION

FISCAL YEAR 2025 YEAR-IN-REVIEW

FISCAL YEAR 2026 YEAR-TO-DATE REVENUE COLLECTIONS

CURRENT ECONOMIC CONDITIONS AND DECEMBER REVENUE FORECAST

LONGER-TERM OUTLOOK

SUMMARY

Fiscal Year-to-Date

- Through the first five months of FY 2026, general fund revenues are up 5.2% year-over-year, driven mainly by growth in individual income tax. Relative to the official forecast assumed in Chapter 725, revenues to date are \$484 million higher than projected.
- Recently released economic data show that the U.S. added 108,000 jobs in September and 64,000 jobs in November. October's data indicated a month-over-month decline of 105,000 which was driven by a reduction in the federal workforce as some federal employees who accepted a deferred resignation offer came off federal payrolls. Private sector employment is growing, and unemployment is stable.
- Virginia payroll withholding, the best indicator of economic performance and largest component of General Fund revenue, has grown 5.9% year-to-date versus last year and is ahead of projections by \$414 million. Federal actions have not had the adverse impact widely anticipated given Virginia's unique agency profile with more than 70% in national defense and intelligence activities.
- Sales tax collections, up 5.8% fiscal year-to-date, indicate continued strength of the consumer in Virginia.

SUMMARY (cont'd)

Revenue Outlook

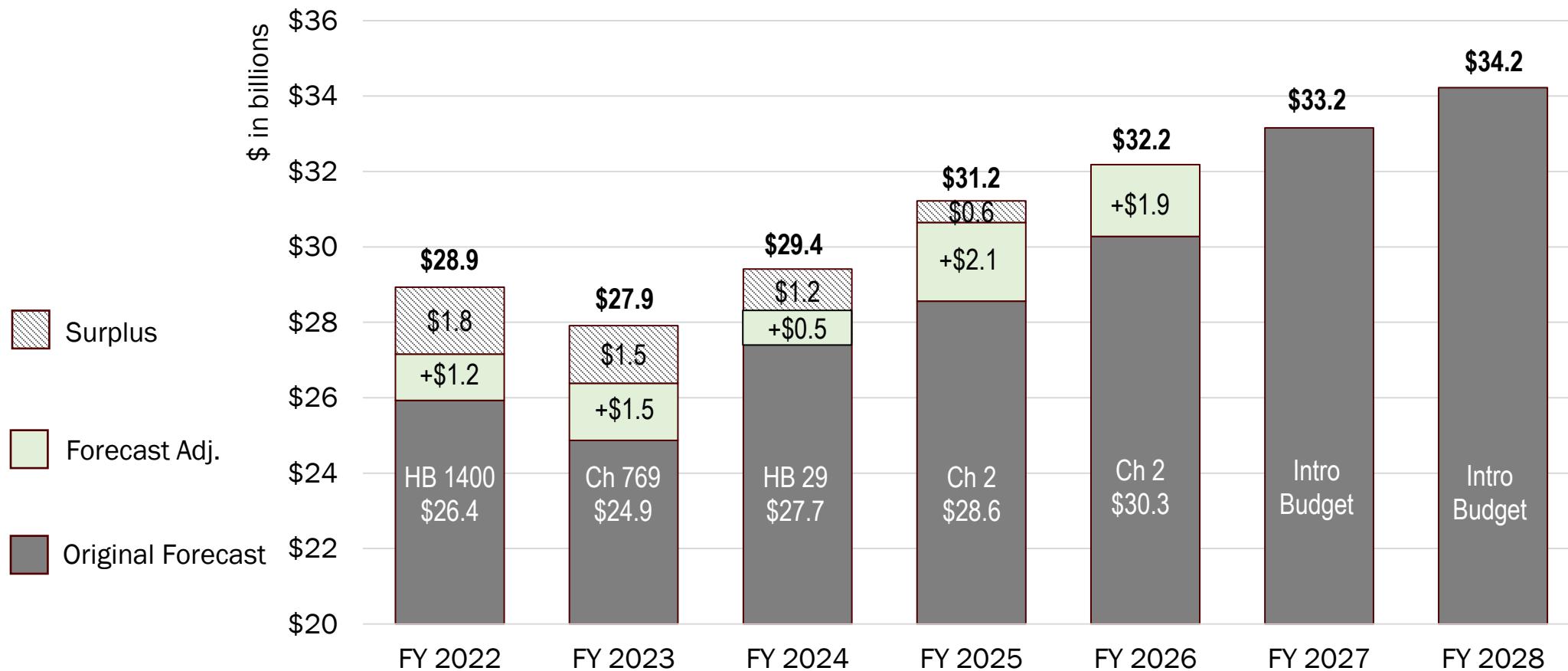
- Comparing FY 2025 revenues adjusted for tax policy to the FY 2022 forecast released in December 2021, revenues have grown by an average annual growth rate of 8.0%.
- Last fiscal year, net revenues grew 6.1%, and this fiscal year-to-date, revenues have grown 5.2%.
- The budget introduced today requires General Fund revenues to grow 3.0% this fiscal year. With year-to-date performance so strong, that equals just 1.9% for the next seven months. Fiscal Years 2027 and 2028 are forecasted at similarly prudent levels of 3.0% and 3.2% respectively. (These growth rates are based on the GACRE approved forecasts of 3.3%, 3.5% and 3.6% with the addition of new tax policy adjustments.)
- After a period of uncertainty around federal trade and tax policy earlier this year, greater clarity exists around tax policy in the now-enacted federal “One Big Beautiful Bill,” and a new tariff regime is now largely in place.
- The U.S. economy has been exceeding many economists’ expectations; and new corporate tax policies and onshoring activity will support further investment and growth.
- Continued job growth is supported by historic economic development announcements in Virginia with commitments of \$156 billion in capital investment creating more than 85,000 projected new direct and indirect jobs in Virginia by the end of the 2026-28 biennium, along with 40,000 construction jobs. The unprecedented investment is also generating over 40,000 construction jobs, with nearly 15,000 net new construction jobs created through September. Additional permanent and construction jobs are forecast beyond the biennial budget period.

THE GOVERNOR'S INTRODUCED BUDGET CONTINUES INVESTMENTS IN SHARED PRIORITIES AND TAX RELIEF

- Accounting for revenue forecast adjustments, carried forward balances and other identified resources, the Governor's introduced budget invests \$6.4 billion GF between FY 2026 and FY 2028 in new operating and capital spending while providing \$730 million in tax relief.
 - \$857.9 million in FY 26, \$2.7 billion in FY27 and \$2.8 billion in FY 28.
- Makes critical investments in shared priorities including:
 - \$2.6 billion GF to fund the Medicaid forecast while implementing reasonable strategies to bend the cost curve
 - \$1.0 billion GF in compensation actions for teachers, support positions, sheriffs and state employees (**2% bonus in FY26 / 2% salary increases in both FY27 and FY28**)
 - \$543.8 million GF in K-12 rebenchmarking costs without reducing new ratios adopted last year
 - \$328.1 million GF (+\$141.9 million NGF) in Natural Resources to address both point and nonpoint source pollution reduction efforts
 - \$270 million GF in Public Safety, including Virginia State Police and DOC inmate medical care
- Includes almost \$2 billion in new capital outlay authorization
 - \$890 million GF and \$1.1 billion in authorized debt and restores majority of projects that were paused in May.
- Provides more than \$730 million in new, ongoing, tax relief over the three years.
 - Makes permanent the increases to the standard deduction, pass-through entity taxes, and increased refundability of the Earned Income Tax Credit
 - Substantially conforms to the major tax provisions of HR 1
 - No tax on tips, overtime, car loan interest
 - Modernizes Virginia's tax code with Market Based Sourcing
 - Extends Data Center Sales and Use Tax Exemption to 2050
- Maintains a combined fund balance of \$4.3 billion in Virginia's Revenue Reserve and Revenue Stabilization Funds (15% of certified revenues).

GF REVENUES HAVE EXCEEDED REVISED FORECASTS

DECEMBER FORECAST CONSISTENT WITH RECENT TRENDS



**Revenue totals are net of tax policy impacts. Enacted tax savings total approximately \$9 billion through FY 2026. FY 2023 revenues include revenue reductions attributable to tax policy changes, including rebates.*

REVENUE IMPACT FROM MAJOR TAX POLICY ACTIONS

Tax Relief Measures (\$ in millions)	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028	FY 2029	FY 2030
Increase Standard Deduction (phased to \$8,750/\$17,500)	(\$1,015.8)	(\$755.5)	(\$821.1)	(\$903.9)	(\$900.0)	(\$913.7)	(\$929.1)	(\$942.7)
Eliminate State Tax on Groceries (1.5%)	(115.0)	(267.2)	(272.5)	(273.6)	(316.7)	(325.0)	(334.4)	(344.8)
Refundable Earned Income Tax Credit (phased to 20% of Federal)	(159.0)	(156.0)	(159.6)	(190.0)	(201.8)	(206.7)	(206.7)	(206.5)
Military Retirement Subtraction	(145.0)	(193.8)	(215.4)	(229.1)	(236.6)	(244.8)	(244.4)	(244.2)
Increase Business Interest Deduction (phased to 50%)	(15.3)	(21.2)	(33.9)	(35.3)	(36.7)	(38.2)	(39.2)	(40.4)
Reduce Estimated Payment Threshold	-	-	-	(10.4)	(1.1)	(1.1)	(1.1)	(1.1)
Conformity to H.R.1	-	-	-	(101.6)	(148.6)	(183.2)	(115.7)	(65.4)
Market-Based Sourcing	-	-	-	-	-	(29.1)	(4.0)	9.2
Total Permanent Tax Cuts	(\$1,450.1)	(\$1,393.7)	(\$1,502.5)	(\$1,743.9)	(\$1,841.5)	(\$1,941.8)	(\$1,874.7)	(\$1,835.9)
Tax Rebates*	(1,048.6)	(906.8)	(977.8)	-	-	-	-	-
No Tax on Car Loan Interest (25% in TY26, 50% for TY27 and TY28)	-	-	-	-	(15.0)	(38.3)	(26.2)	(5.4)
No Tax on Tips (25% in TY26, 50% for TY27 and TY28)	-	-	-	-	(18.3)	(35.2)	(26.3)	(6.1)
No Tax on Overtime (25% in TY26, 50% for TY27 and TY28)	-	-	-	-	(60.6)	(104.4)	(52.2)	(9.0)
Total Permanent + Temporary Tax Cuts	(\$2,498.7)	(\$2,300.5)	(\$2,480.3)	(\$1,743.9)	(\$1,935.4)	(\$2,119.7)	(\$1,979.4)	(\$1,856.4)

*FY23 rebates are a reduction in net revenues. FY24 and FY25 were appropriated rebates.

FISCAL YEAR 2025 GENERAL FUND REVENUES TOTALLED \$31.2 BILLION, A GROWTH RATE OF OVER 6 PERCENT

SOURCE, \$ Mil	<u>Actuals</u>				<u>Chapter 725</u>		
	FY 2024	FY 2025	YoY Growth \$	YoY Growth %	FY 2025 Forecast	Forecast Growth %	Forecast Variance \$
Withholding	\$16,718.2	\$17,561.2	\$842.9	5.0%	\$17,580.8	5.2%	\$ (19.7)
Non-withholding	6,563.7	7,518.7	955.0	14.5%	6,788.9	3.4%	729.8
IIT Refunds	(2,971.5)	(3,187.4)	(215.9)	7.3%	(2,811.6)	-5.4%	(375.8)
Net Individual Income	\$20,310.4	\$21,892.4	\$1,582.0	7.8%	\$21,558.1	6.1%	\$334.3
Sales & Use Tax	4,709.7	4,812.7	103.1	2.2%	4,797.9	1.9%	14.8
Corporate Income Tax	1,907.1	1,878.6	(28.5)	-1.5%	1,791.5	-6.1%	87.1
Insurance	468.2	541.5	73.3	15.6%	485.7	3.7%	55.7
Wills, Suits, Deeds	406.5	471.2	64.7	15.9%	457.6	12.6%	13.5
Interest Income	699.8	593.8	(106.0)	-15.1%	617.1	-11.8%	(23.4)
All Other	946.7	1,042.9	96.2	10.2%	952.9	0.7%	90.0
Total GF Revenues	\$29,448.2	\$31,233.0	\$1,784.8	6.1%	\$30,661.0	4.1%	\$572.0

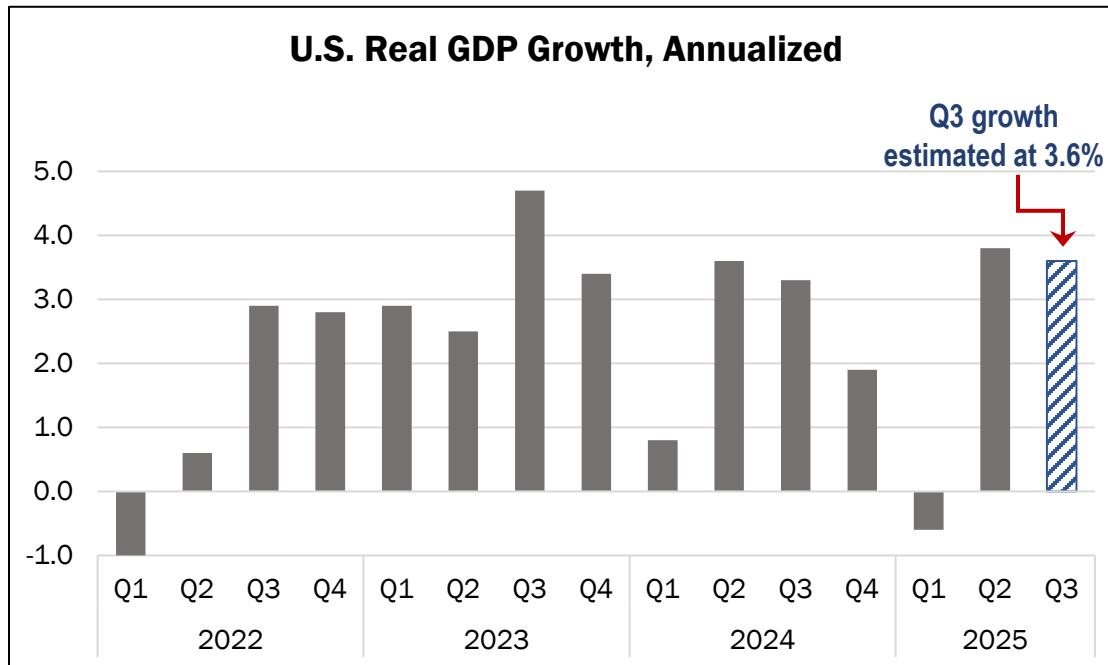
- Fiscal Year 2025 General Fund revenues were \$1.8 billion higher (6.1%) than Fiscal Year 2024 and ended with a surplus of \$572 million.
- Individual income tax accounted for the majority (\$1,582 million) of the year-over-year increase, growing 7.8%.

YEAR-OVER-YEAR REVENUES HAVE GROWN 5.2 PERCENT; AHEAD OF CH. 725 YTD FORECAST BY \$484 MILLION

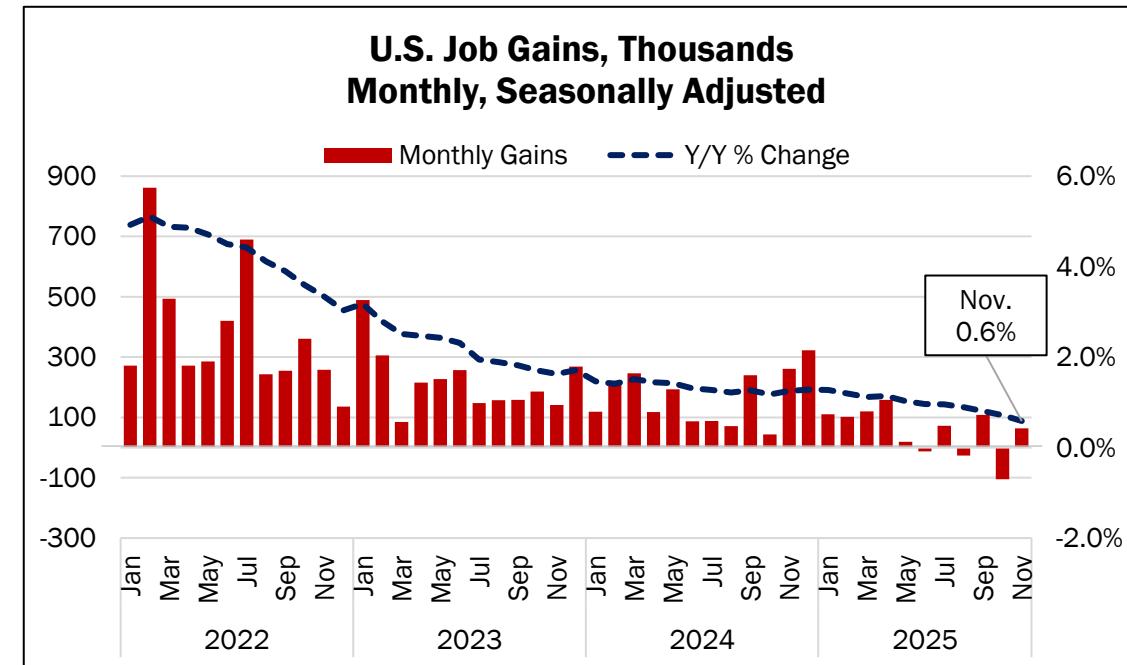
SOURCE, \$ Mil	Year-Over-Year Growth FYTD				Forecast Variance FYTD			
	FY 25	FY 26	Change \$	Change %	Actuals	Projected	Variance \$	Variance %
Withholding	\$7,007.2	\$7,421.2	\$414.0	5.9%	\$7,421.2	\$7,088.1	333.1	4.7%
Non-withholding	1,700.0	1,626.5	(73.5)	-4.3%	1,626.5	1,365.5	261.0	19.1%
IIT Refunds	(894.1)	(682.4)	211.8	-23.7%	(682.4)	(683.9)	1.5	-0.2%
Net Individual Income	\$7,813.1	\$8,365.3	\$552.3	7.1%	\$8,365.3	\$7,769.7	\$595.6	7.7%
Sales & Use Tax	2,010.9	2,128.1	117.3	5.8%	2,128.1	2,087.7	40.4	1.9%
Corporate Income Tax	469.9	373.1	(96.8)	-20.6%	373.1	559.3	(186.2)	-33.3%
Wills, Suits, Deeds	195.2	219.5	24.3	12.4%	219.5	221.4	(1.9)	-0.8%
Interest Income	385.8	381.9	(3.9)	-1.0%	381.9	369.5	12.4	3.4%
All Other	331.5	316.7	(14.8)	-4.5%	316.7	293.4	23.3	7.9%
Total GF Revenues	\$11,206.3	\$11,784.7	\$578.4	5.2%	\$11,784.7	\$11,301.0	\$483.6	4.3%

- Year-to-date revenues have grown \$578 million (5.2%) relative to Fiscal Year 2025 and are \$483.6 million (4.3%) over the Chapter 725 forecast.
- The majority of the growth has occurred in payroll withholding which has performed well above expectations. Collections of payroll withholding taxes are up 5.9% year-to-date.
- Sales and use taxes have also come in strong, growing 5.8% year-to-date.

U.S. ECONOMY CONTINUES GROWING AT A HEALTHY PACE



Source: Bureau of Economic Analysis; Atlanta Fed GDPNow estimate for Q4 (12/11/25).

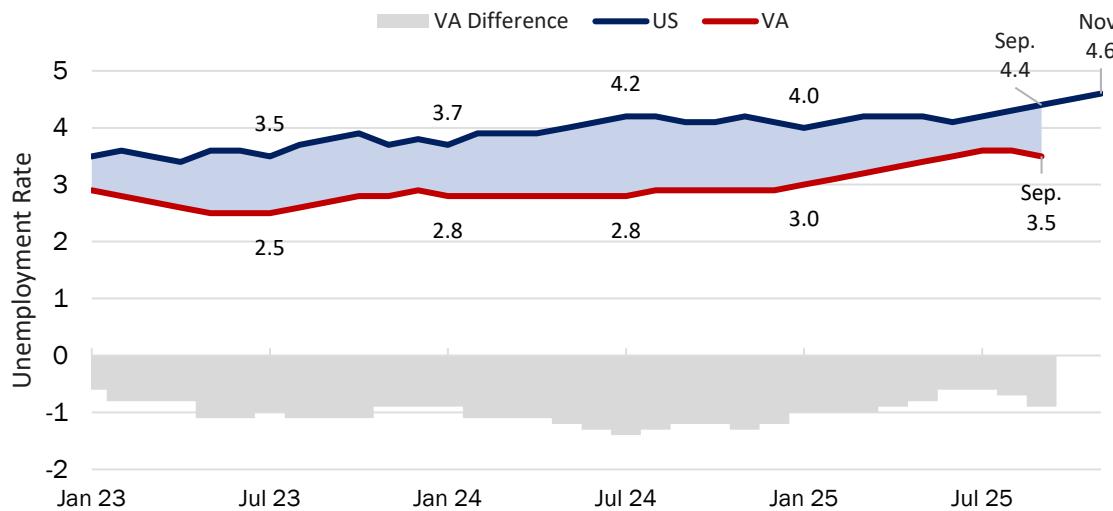


Source: Bureau of Labor Statistics.

- Real GDP growth remains strong, growing at a 3.8% annual rate in the second quarter. Third quarter growth is estimated at 3.6%.
- The U.S. Jobs report for November showed an increase of 64,000 jobs with modest revisions to August and September, along with the introduction of preliminary October data. Year-over-year U.S. employment is up 0.6%.

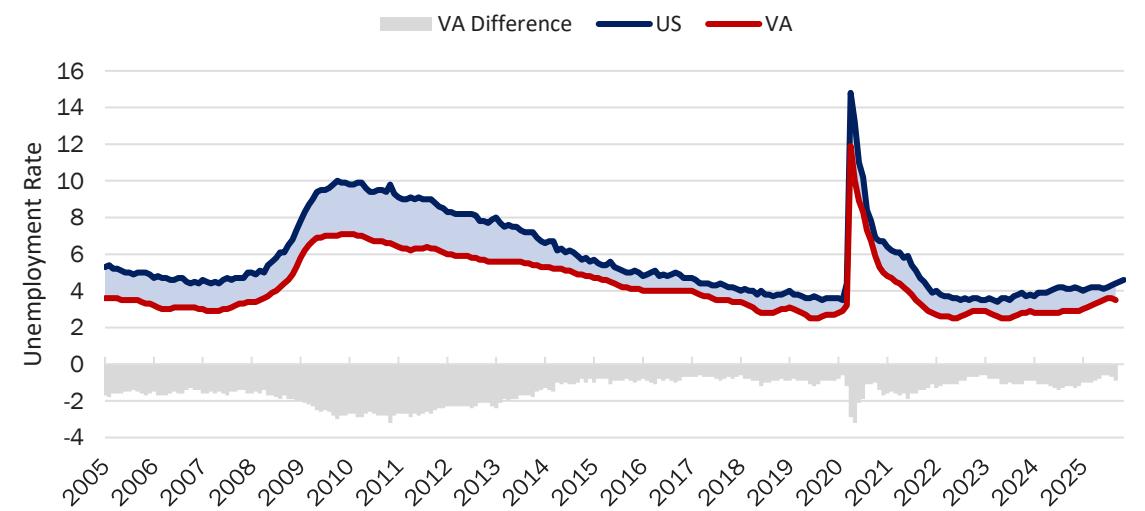
VA UNEMPLOYMENT RATE OUTPERFORMS THE NATION

Virginia Sep. Unemployment Rate is 90bp Below US



Source: Bureau of Labor Statistics; FRED.

Unemployment Rate Performance, Long-Term

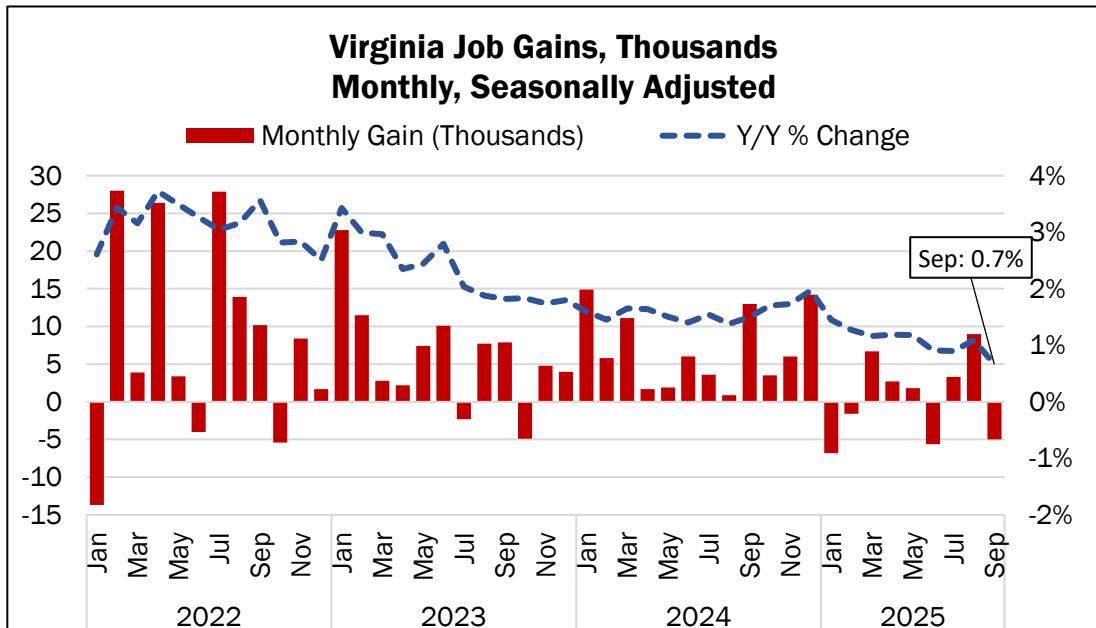


Source: Bureau of Labor Statistics; FRED.

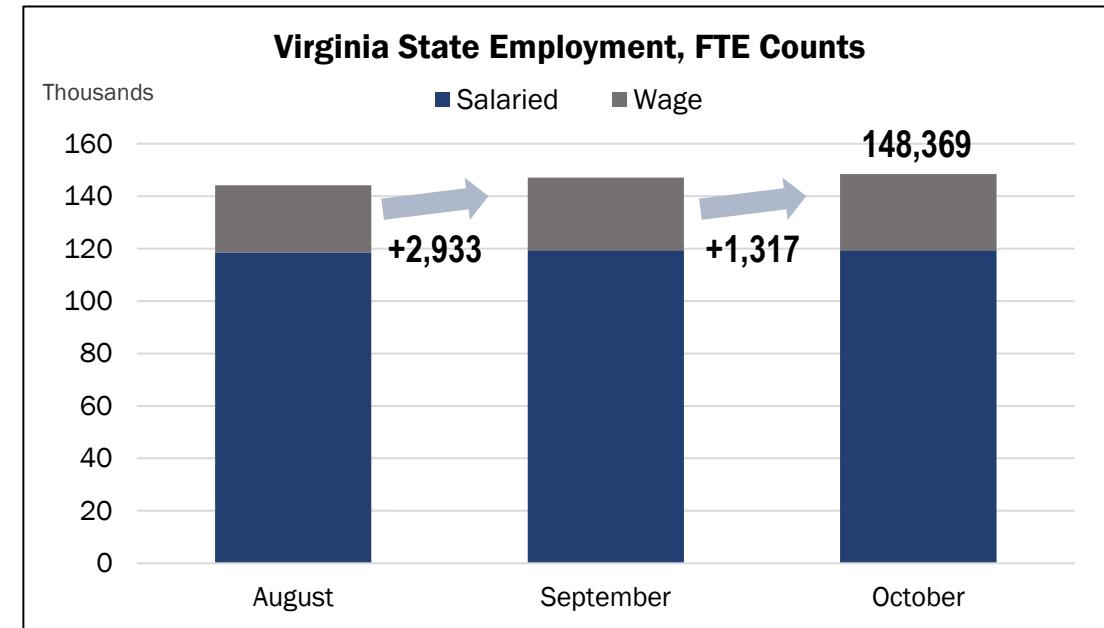
- While unemployment in Virginia has trended up over the past two quarters, it remains near historically low levels of 3.5% versus 4.4% nationally in September and below the 20-year average of 4.3%. Virginia saw a 0.1 percentage point decrease in September from August.
- Additionally, Virginia job openings increased in the latest month of August standing at 222,000 or roughly 1.4 job openings per unemployed person in Virginia vs 1.0 nationally.
- The U.S. unemployment rate increased slightly over two months to 4.6% in November. October data is missing due to the government shutdown.

YEAR-OVER-YEAR JOB GROWTH POSITIVE THROUGH SEPTEMBER

BLS SEASONAL ADJUSTMENTS OBSCURE REAL STATE GOVERNMENT JOB GROWTH



Source: Bureau of Labor Statistics.



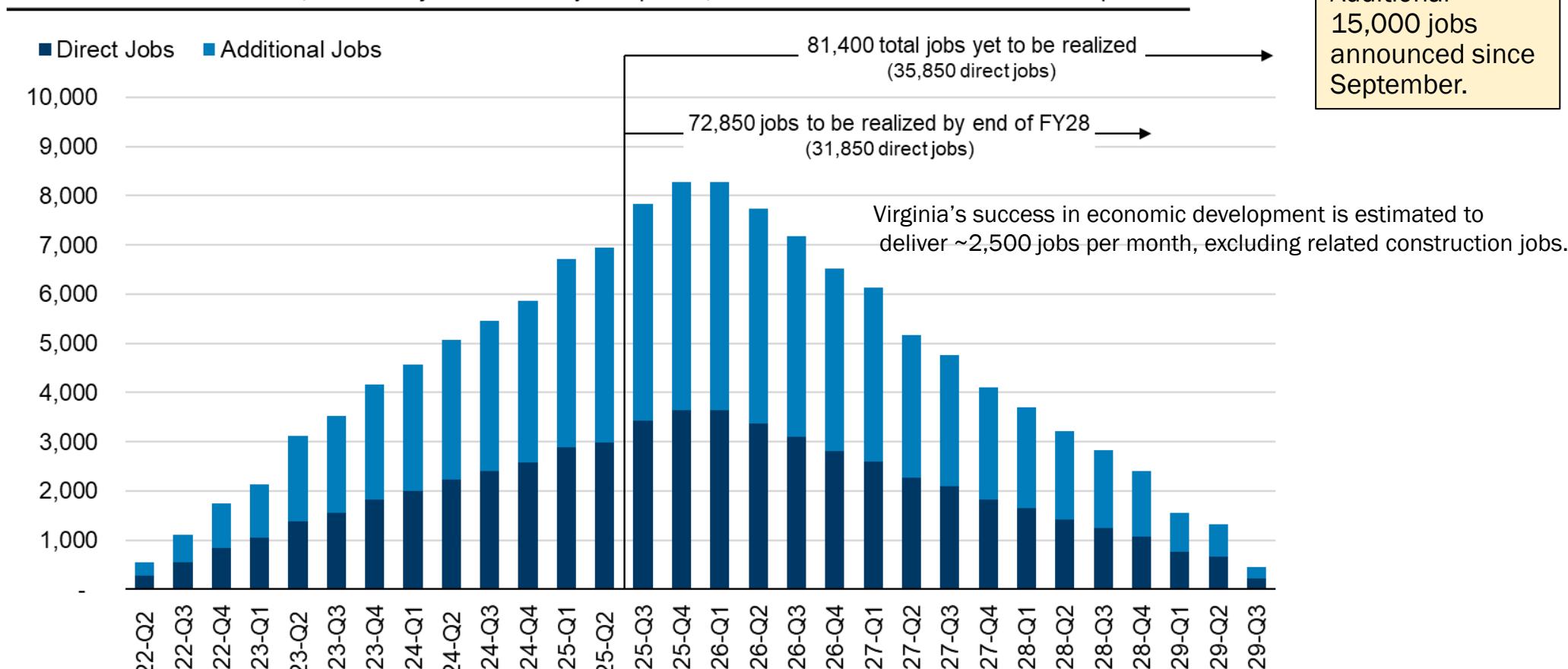
Source: DHRM. Salaried FTEs includes classified, at-will, faculty, and restricted.

- August's preliminary estimate of employment was revised up by 1,800 to +9,000.
- Preliminary seasonally adjusted nonfarm payroll data from BLS show a 5,000-job decrease in September, driven by a model-based reduction in state government employment. Commonwealth administrative payroll records, however, indicate that actual state government employment increased by 2,933 in September and 1,317 in October, underscoring a divergence between the federal model and actual payroll data. A future upward revision is expected.

70,000+ VA JOBS ANNOUNCED SINCE JANUARY 2022 TO BE CREATED BY END OF FY 2028

Timing of estimated job creation from economic development announcements

Estimated* number of direct, additional jobs realized by CY quarter, announcements from Jan 2022 – Sept 2025



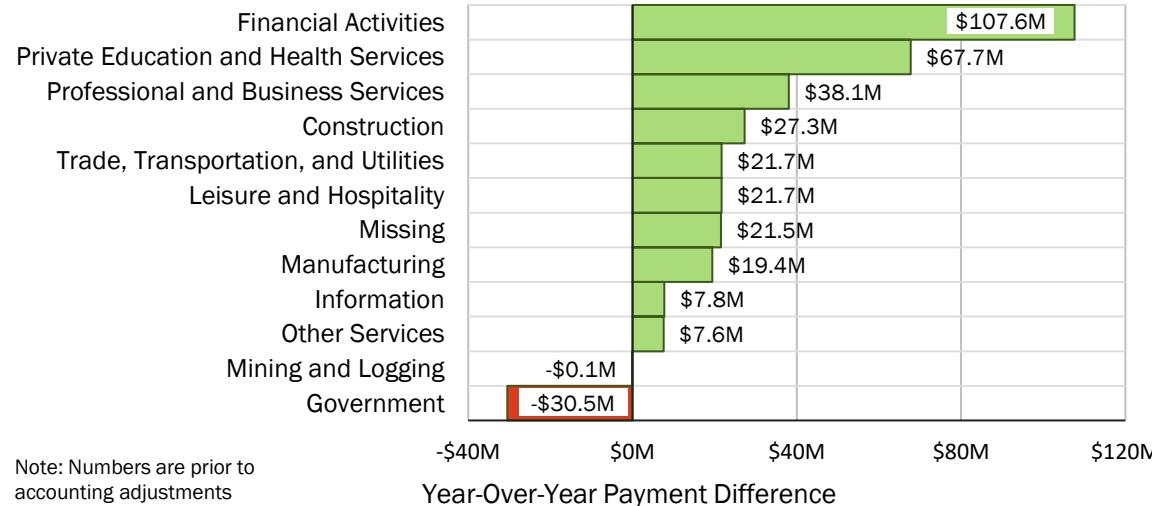
*Includes VEDP-assisted and other traded sector economic development projects tracked by VEDP. Assumes hiring begins one quarter after announcement and a 2-year average ramp, uses detailed IMPLAN multipliers, assumes publicly announced hiring plans do not shift due to company or economic changes. Not based on verified job creation.

Source: VEDP analysis based on the VEDP announcements database.

NON-GOVERNMENT WITHHOLDING GROWTH HAS STRONG START

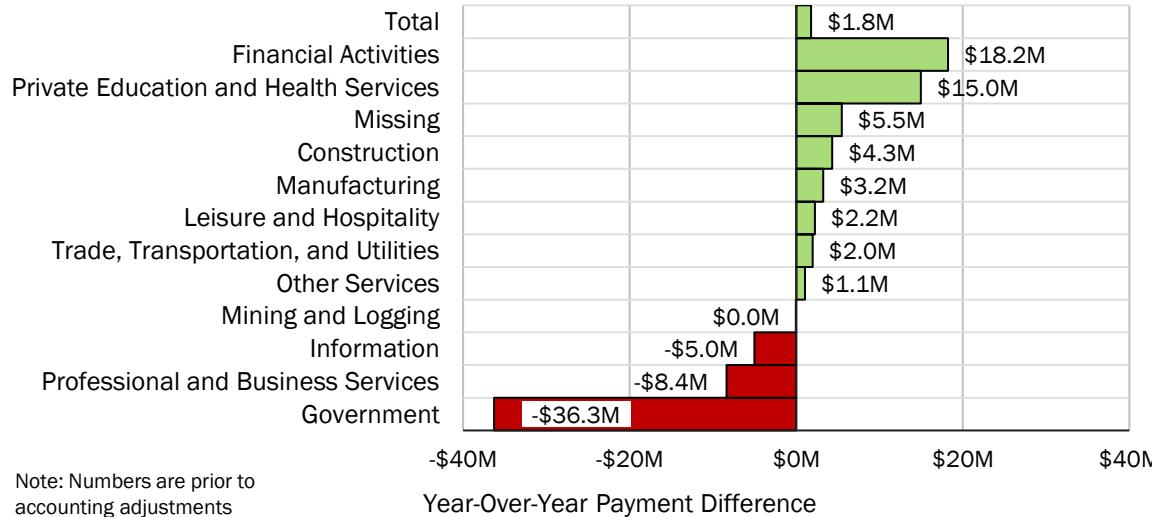
Industry WH Payments FYTD Through November,

FY 2026 vs. FY 2025



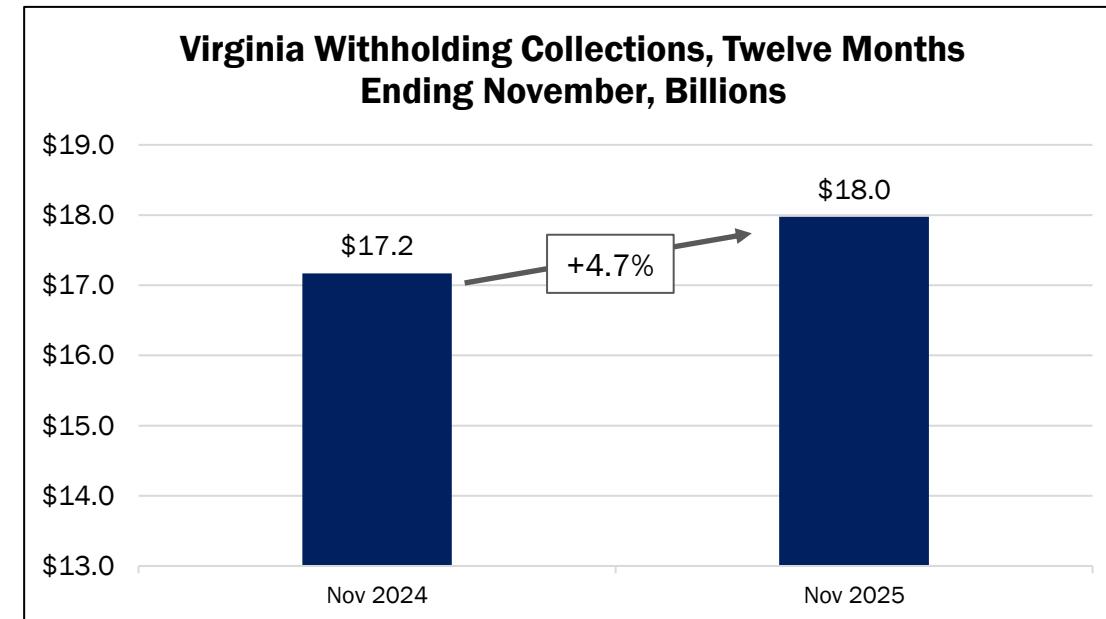
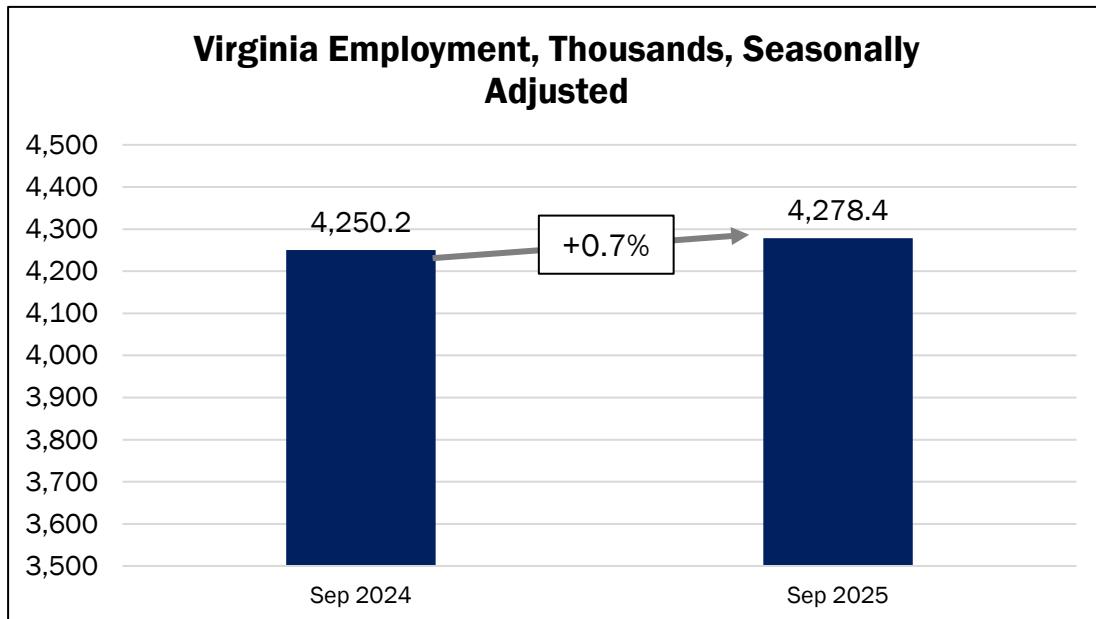
November WH Payments by Industry

FY 2026 vs. FY 2025, Y/Y



- November withholding collections were impacted by the extended federal government shutdown. The declines from federal agencies are expected to rebound as unpaid wages are restored.
- Fiscal-year-to-date FY 2026 is outperforming FY 2025 by \$414 million, or 5.9%.
- Financial activities and education and health services are leading the FY 2026 annual growth.

NON-FARM PAYROLL INCREASED BY 28K, AND WITHHOLDING INCREASED 4.7 PERCENT

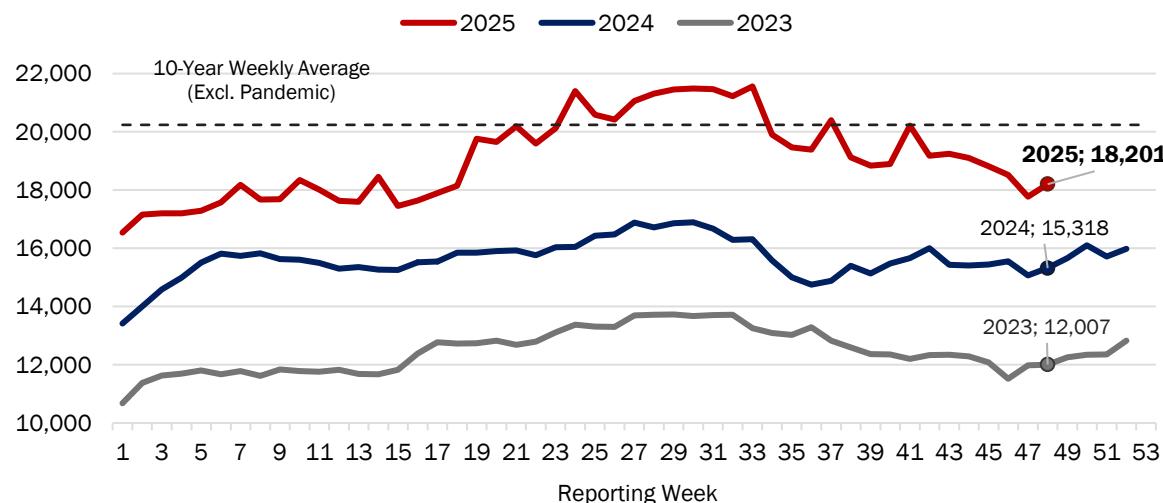


Source: Bureau of Labor Statistics, CES (establishments survey).

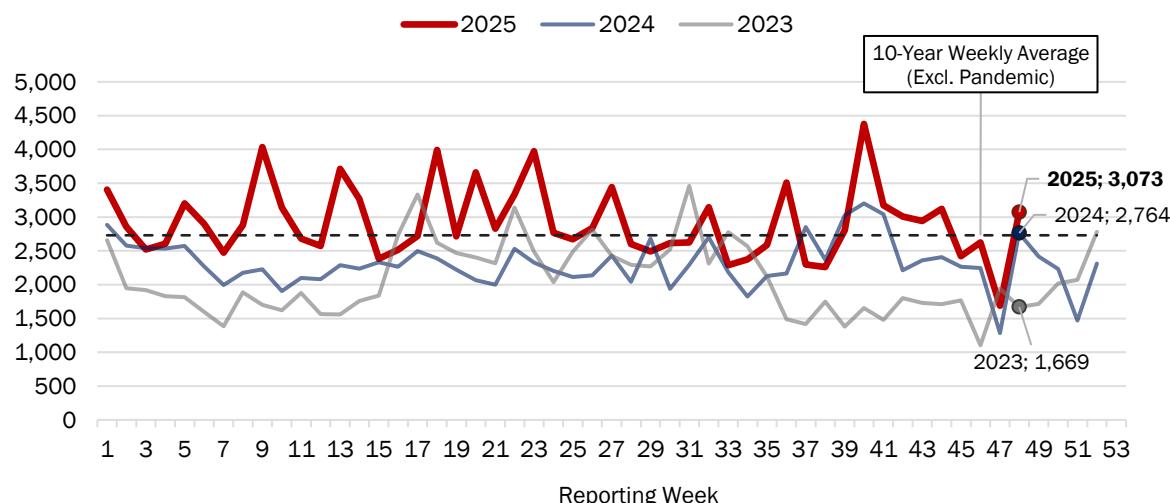
- Payroll withholding growth is highly correlated with growth in Virginia non-agricultural payroll and wages. This implies wage growth of approximately 4% over the year.
- The unemployment rate is calculated using data from the survey of households which suggests employment in Virginia has declined over the last year. However, data from the survey of business establishments – a broader survey of ~18,000 vs ~1,500 in the household survey – shows that Virginia added over 28,000 jobs between September 2024 and September 2025.

CONTINUED CLAIMS ARE UP YEAR-OVER-YEAR, BUT HAVE DECLINED RECENTLY

Virginia UI Continued Claims Performance, Recent Years



Virginia UI Initial Claims Performance, Recent Years

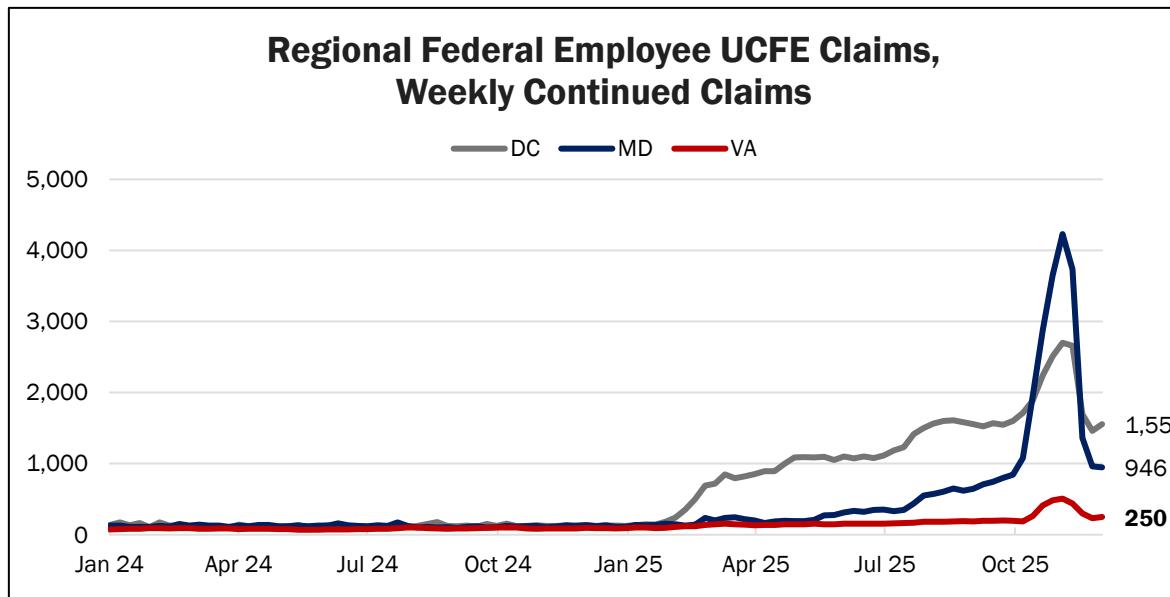


Source: US Department of Labor, Employment and Training Administration.

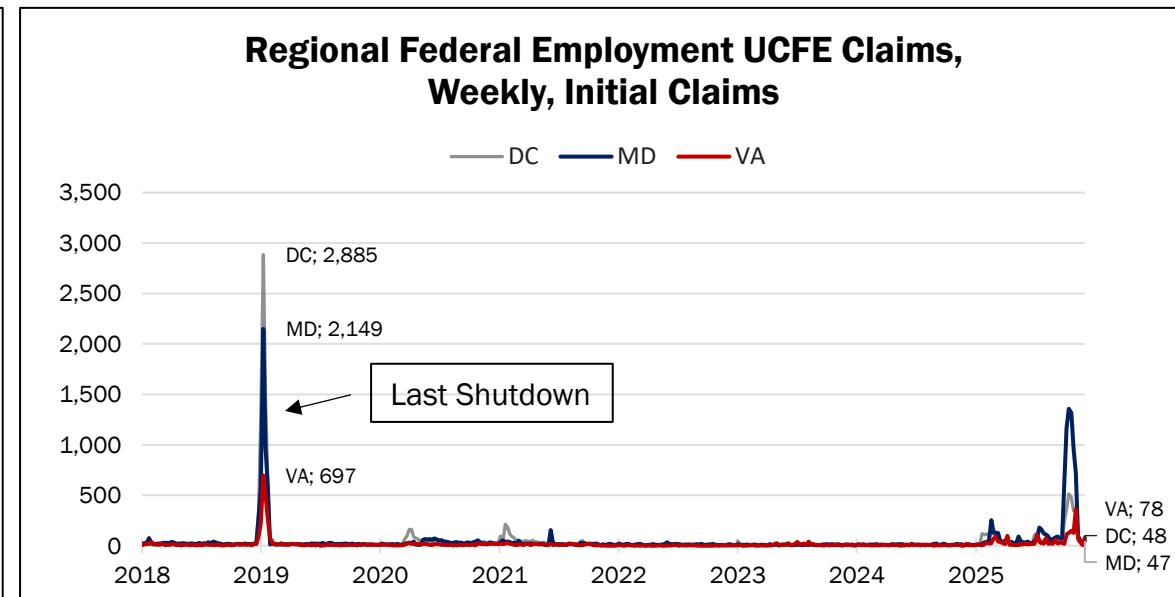
- In the week ending December 6, initial claims increased to 3,073 following the week of Thanksgiving, consistent with typical seasonal patterns.
- Continued claims totaled 18,201 and remain below the 10-year weekly average (excluding pandemic years).
 - After rising midway through the year, continued claims have been receding over the last few months with a recent increase to start December.

Source: US Department of Labor, Employment and Training Administration.

CONTINUED UNEMPLOYMENT CLAIMS FOR VIRGINIA FEDERAL EMPLOYEES REMAIN SIGNIFICANTLY LOWER THAN MD AND DC



Source: US Department of Labor, Employment and Training Administration.



Source: US Department of Labor, Employment and Training Administration.

Federal Employment (Aug '25)

VA: 185,200

MD: 148,000

DC: 184,100

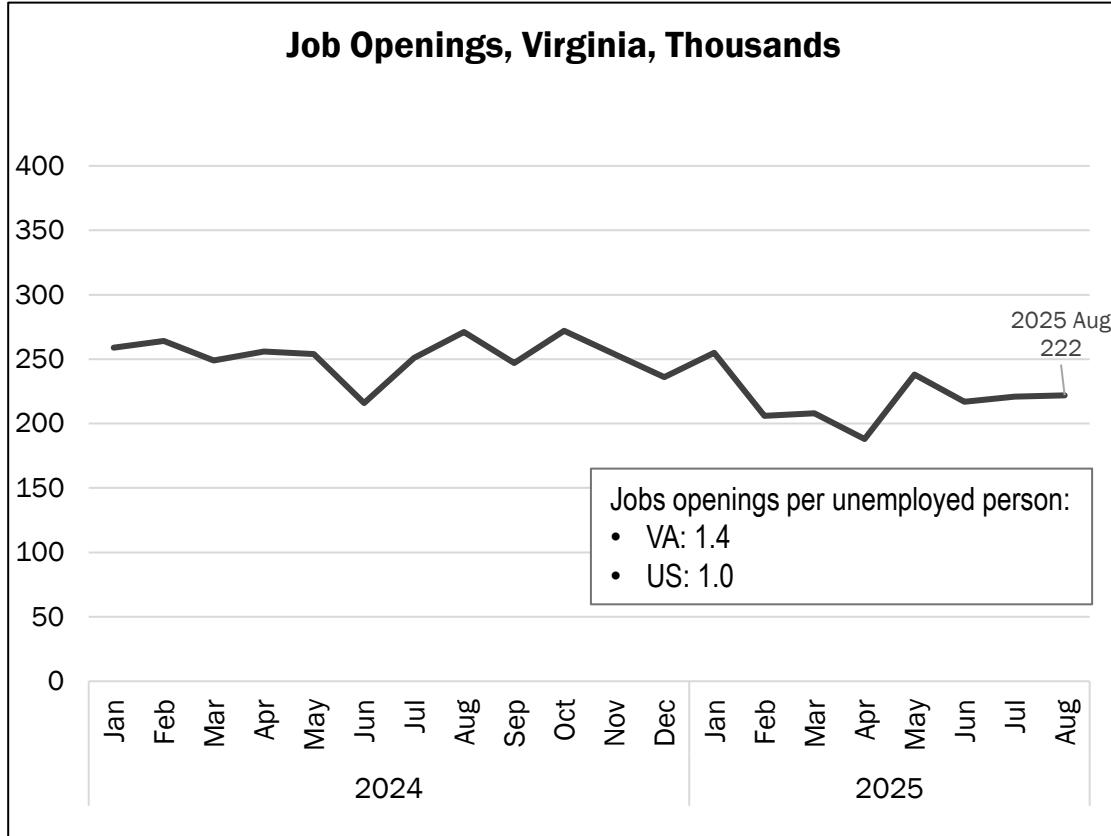
Source: BLS (by place of work, prelim.).

Top 10 Federal Agencies (as of June 2024) -- 72% of federal employment in VA is defense related

1. Dept. of the Navy - 45,662
2. Dept. of Defense - 28,403
3. Dept. of the Army - 15,208
4. Dept. of Veterans Affairs - 12,048
5. Dept. of Homeland Security - 8,928
6. Dept. of the Air Force - 6,497
7. Dept. of Commerce - 6,302
8. Dept. of the Interior - 3,343
9. Dept. of Agriculture - 2,372
10. Dept. of Transportation - 2,296

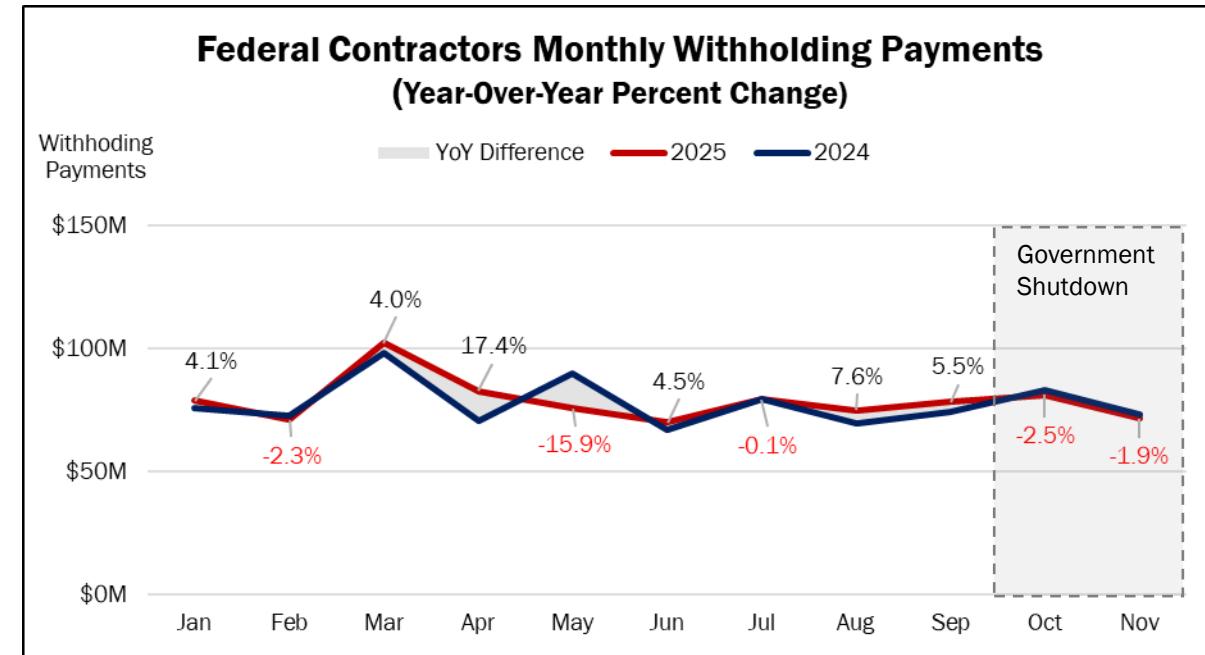
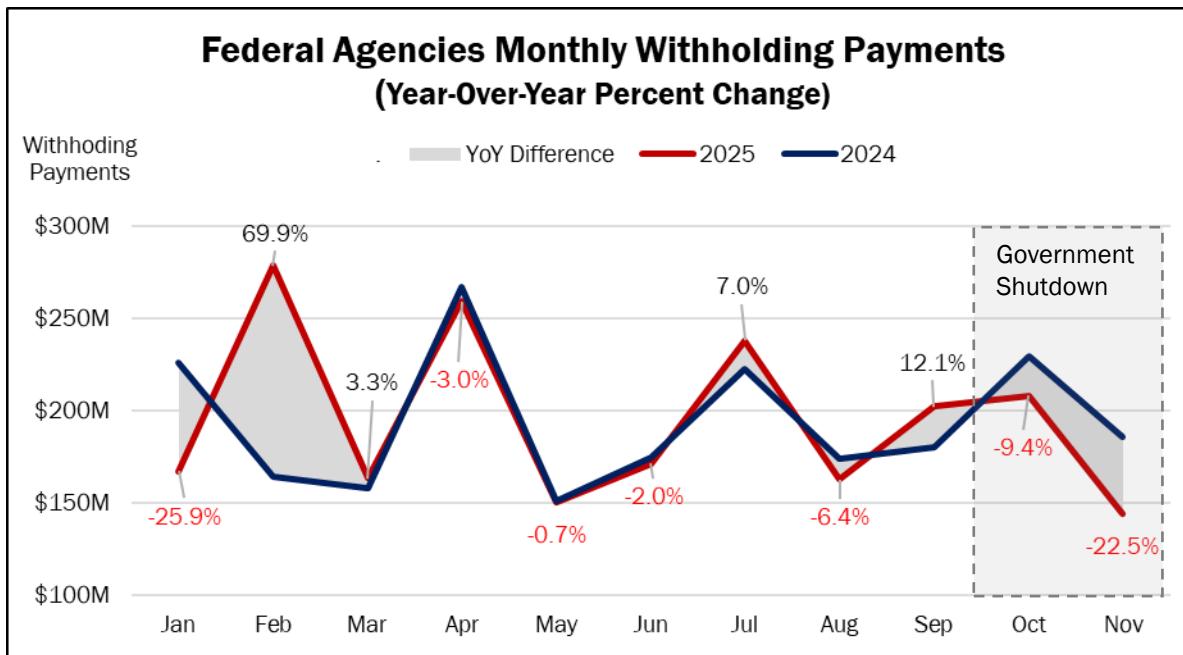
Source: Office of Personnel Management FedScope database.

VIRGINIA HAS MORE THAN 200,000 JOB OPENINGS



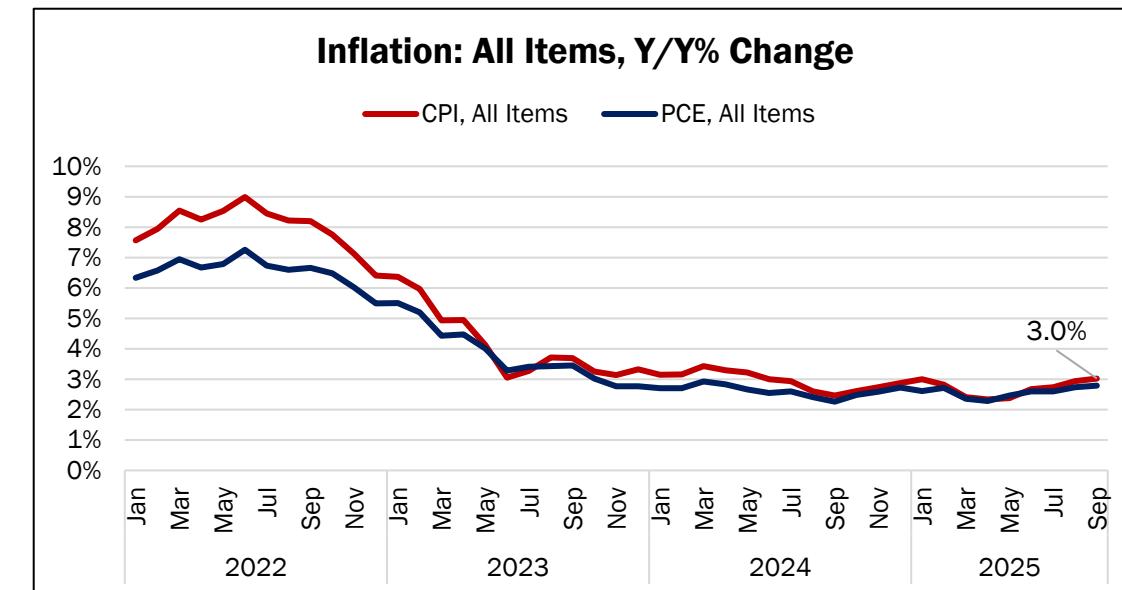
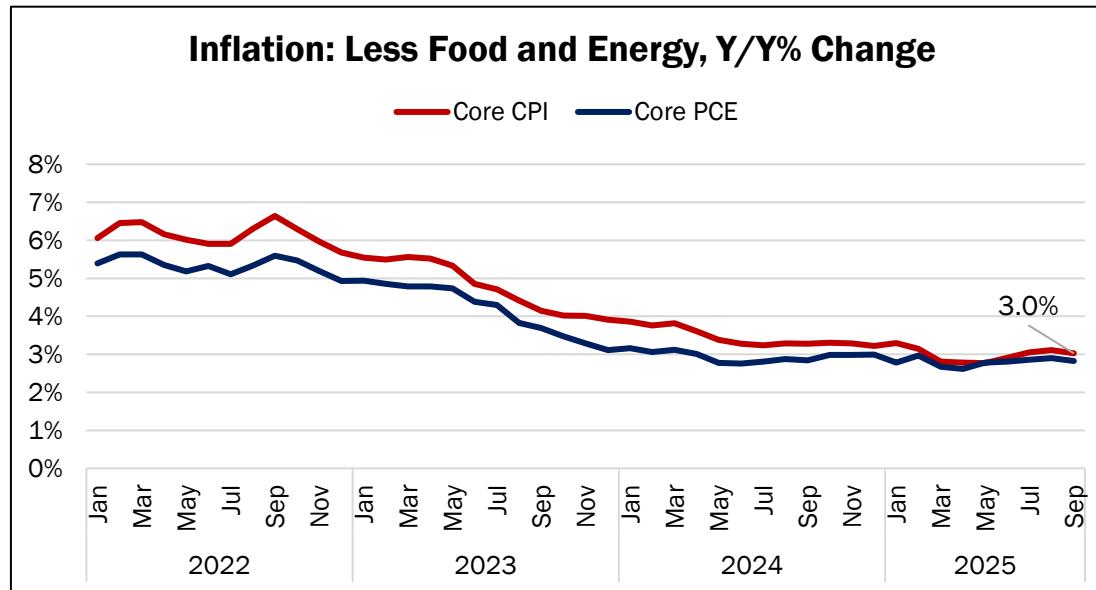
- In addition to low unemployment, job openings in Virginia indicate a healthy statewide labor market.
- Virginia had 222,000 job openings in August 2025, compared to 221,000 openings in July, according to U.S. Bureau of Labor Statistics.
- The job openings rate in Virginia was 4.9% in August, higher than the U.S. rate of 4.3% and unchanged from July.
- Based on more recent data, the U.S. posted a job openings rate of 4.6% in October, 0.3 percentage points higher than the August reading.

PRIOR TO THE SHUTDOWN, FYTD FEDERAL AGENCY WITHHOLDING COLLECTIONS WERE POSITIVE



- To monitor federal spending reductions, withholding payments from the largest federal agencies and contractors who do significant business in Virginia are tracked on a monthly basis.
- Federal withholding payment growth has shown signs of softening but remains positive year-to-date. Timing of payments, such as the ones in January and February, have driven most of the large month-over-month differences prior to October.
- During the first three months of FY 2026 before the shutdown, federal agencies were up 4.5% and federal contractors were up 4.1% year-over-year; with both declining in the government shutdown affected months of October and November.
- With the Federal government shutdown resolved, back payments of wages are expected to be reflected in withholding collections in the coming months.

CORE INFLATION REMAINS AROUND 3 PERCENT



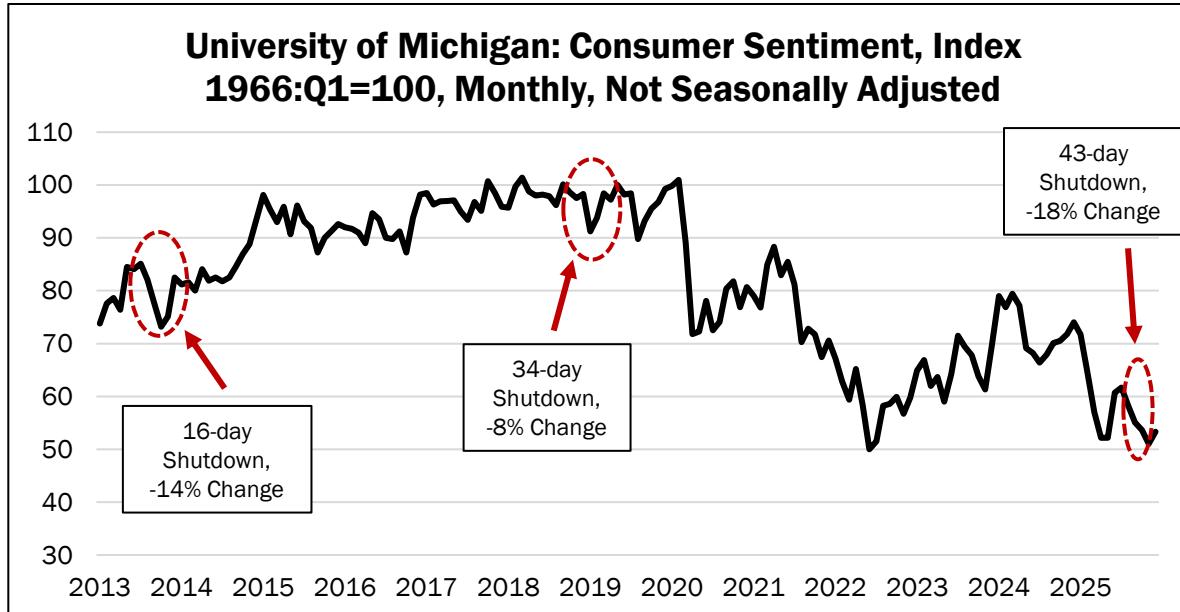
Source: U.S. Bureau of Economic Analysis; Bureau of Labor Statistics.

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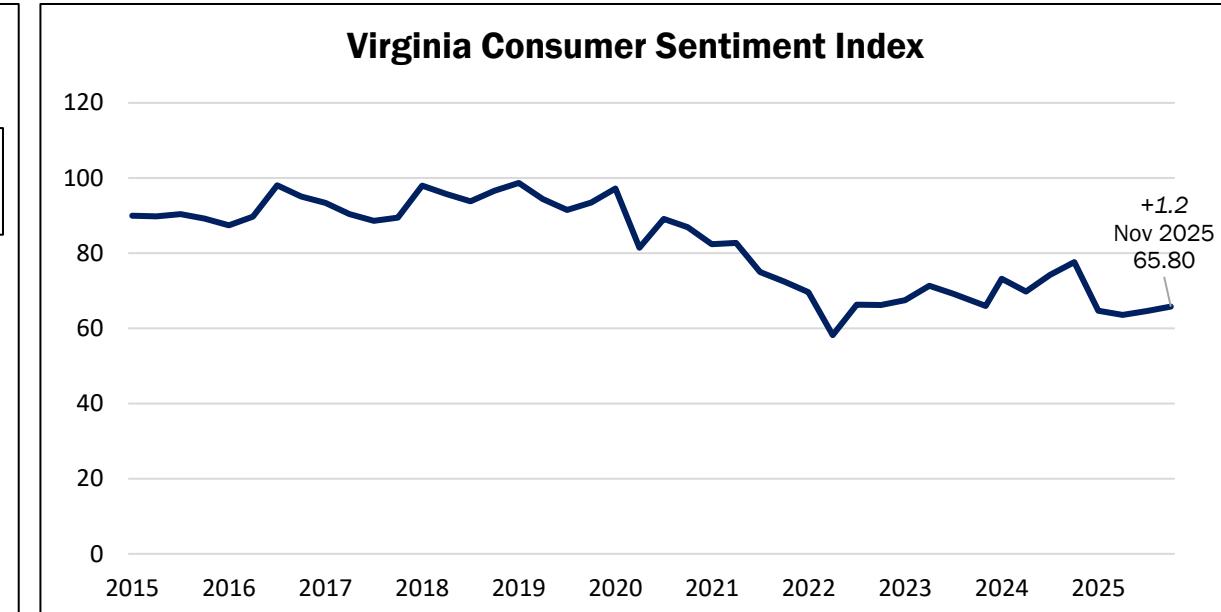
- In September, the Consumer Price Index for all urban consumers increased by 0.3% for the month, a 3.0% year-over-year growth compared to September of last year. Core CPI, which excludes food and energy, increased by 3.0% over last September.
- In September, the Personal Consumption Expenditure Price Index for all items increased by 0.3%, equating to a 2.8% year-over-year growth. Core PCE, the Federal Reserve's preferred inflation measure, increased by 0.2% for the month, which denotes a 2.8% year-over-year increase.

CONSUMER SENTIMENT SHOWS LATEST IMPROVEMENT

SENTIMENT TENDS TO FALL DURING MAJOR GOVERNMENT SHUTDOWNS



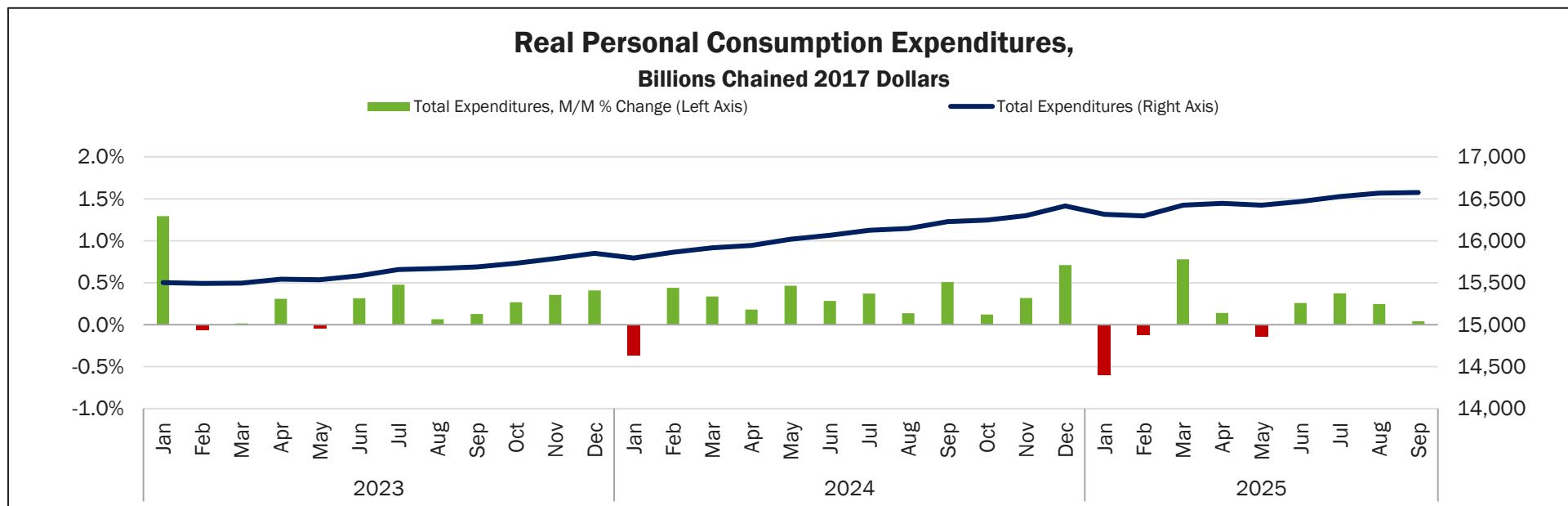
Source: Federal Reserve Bank of St. Louis, University of Michigan



Source: Roanoke College Institute for Policy and Opinion Research

- The University of Michigan consumer sentiment index rose to 53.3 in the preliminary December report after the conclusion of the government shutdown. This was 2.3 points higher than November's 51.0 reading.
- Consumer sentiment in Virginia showed improvement in November according to a Roanoke College quarterly index, improving to 65.8 which was 1.2 points higher than August's 64.6 result.

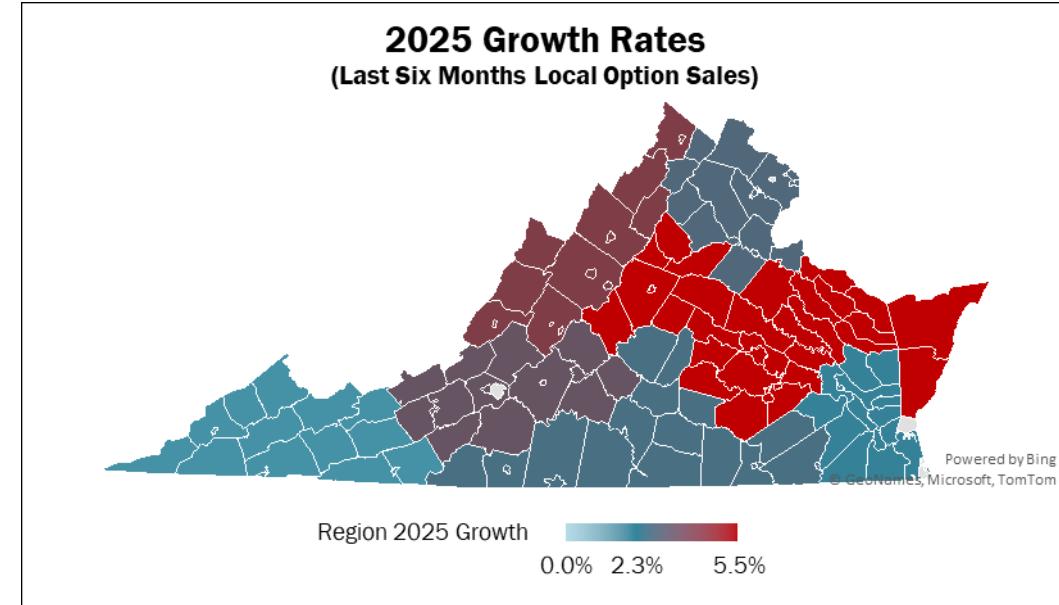
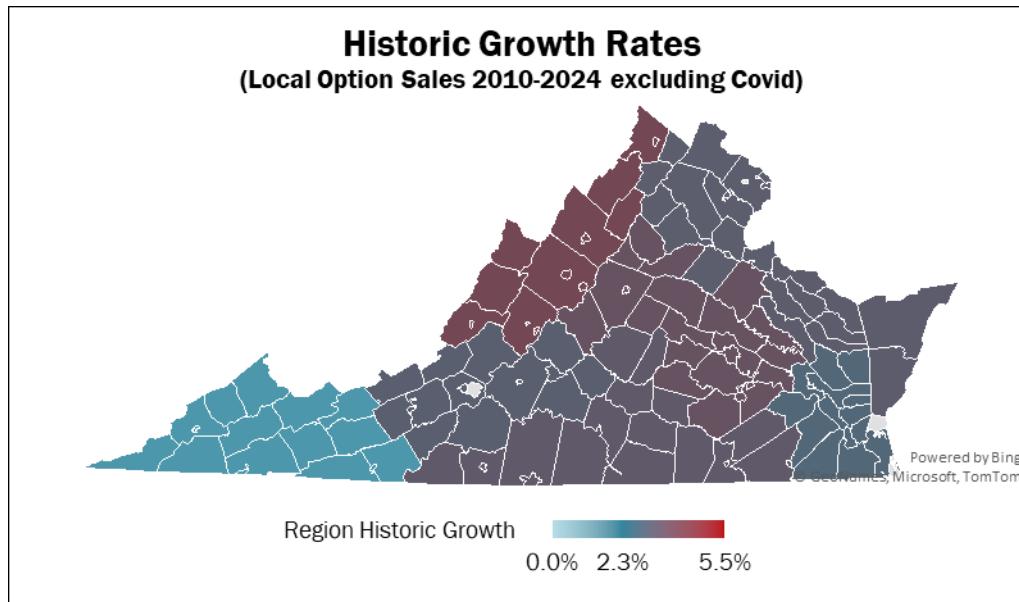
CONSUMERS CONTINUE TO SPEND



Source: Bureau of Economic Analysis; FRED.

- Real personal consumption expenditures have shown moderate growth in recent months following the uncertainty surrounding trade policy and other national economic policies during the opening months of 2025.
- Virginia sales and use tax revenues remain solid, increasing 3.8% year-over-year in November. Year-to-date sales tax collections are up 5.8%.
- CNBC and National Retail Federation's Retail Monitor reported that total retail sales (excluding autos and gas) increased by 0.12% M-o-M during November
- US Census Bureau's Monthly Advance Retail Trade Survey (MARTS) painted a more positive September than CNBC/NRF at 0.1% M-o-M growth.

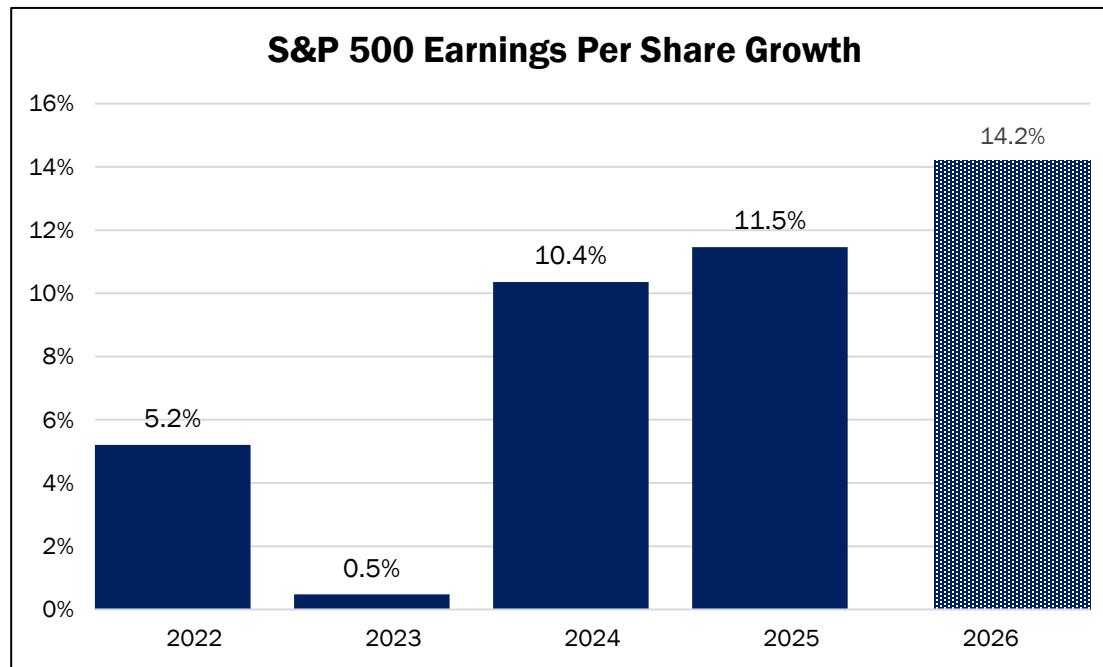
SALES TAX GROWTH REMAINS ABOVE HISTORIC AVERAGE



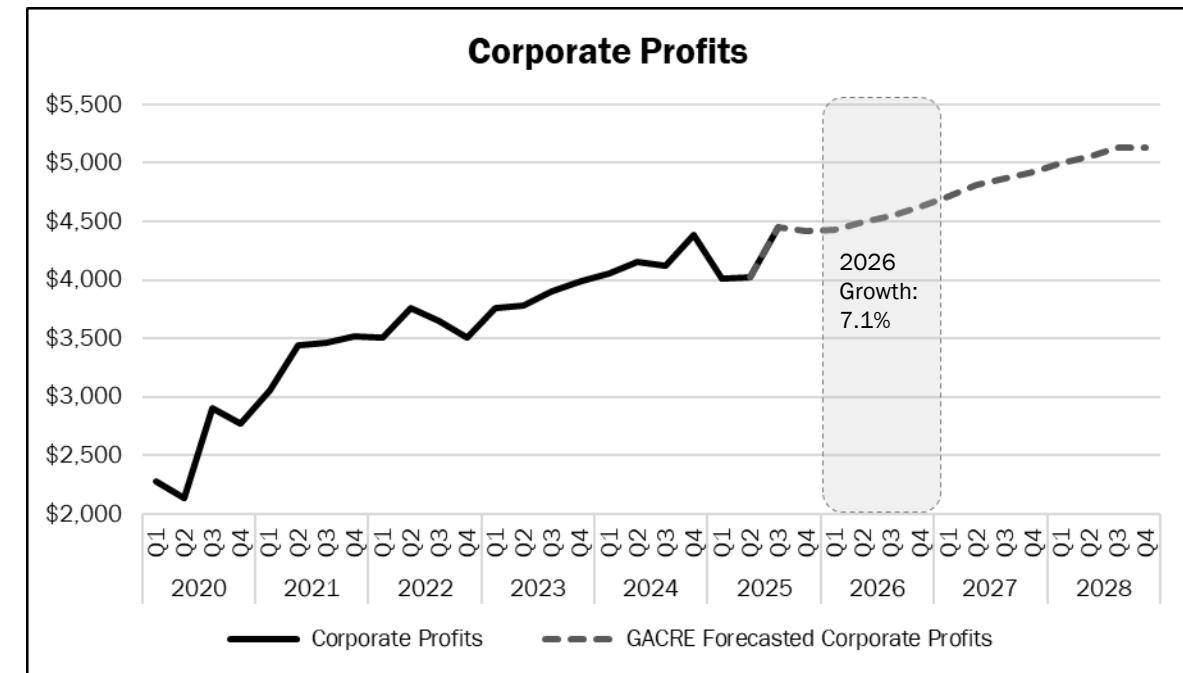
- Sales tax can be analyzed on a regional level by using growth of collections of the local option (1 percent) sales tax.
- In the past six months of sales activity, collections have grown approximately 3.8% statewide, compared to an average historic rate of 3.2%.
- The Central and Eastern regions have performed particularly well above historic norms while the rest of the Commonwealth regions have performed similar to their historic rates.

Region	Historic Growth	2025 Growth
Central	3.5%	7.2%
Eastern	3.2%	9.4%
Hampton Roads	3.0%	2.3%
Northern	3.2%	3.0%
Southside	3.3%	2.8%
Southwest	1.8%	1.9%
Valley	3.8%	4.0%
West Central	3.2%	3.5%
Statewide Average	3.2%	3.8%

CORPORATE PROFITS ARE EXPECTED TO REMAIN STRONG

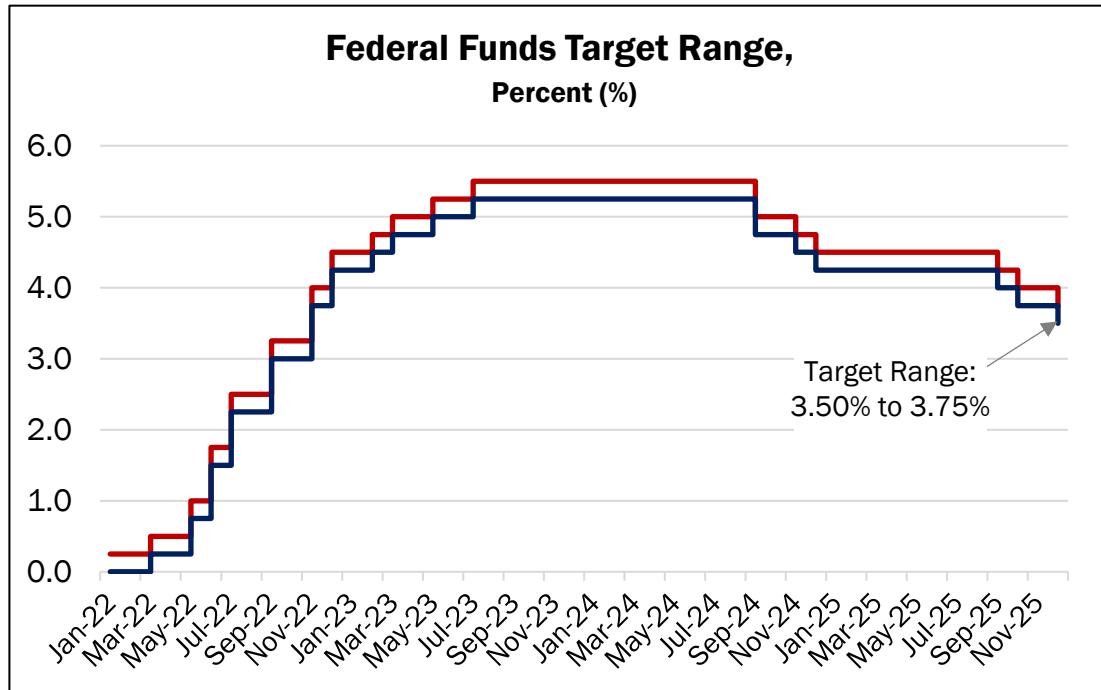


Source: FactSet Earnings Insight December 12, 2025

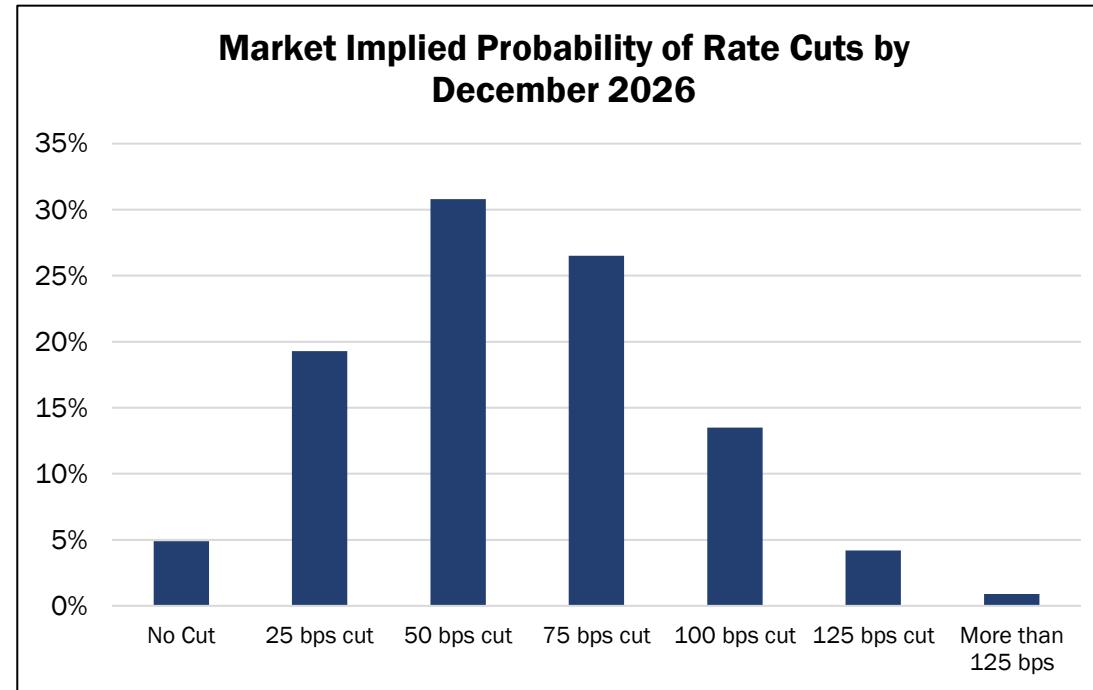


- Corporate earnings have remained strong over the past two years, with earnings per share growing more than 10 percent.
- The GACRE macroeconomic forecast takes a conservative outlook with 7.1 percent growth in overall corporate profits in 2026.
- Projections from market analysts are generally bullish as uncertainties have declined and stimulative tax policies take effect, supporting potential tailwinds in corporate income tax revenues and nonwithholding.

FED CUTS INTEREST RATES BY 25 BPS IN DECEMBER



Source: Federal Reserve of St. Louis.



Source: CME Group, FedWatch Tool (data as of Tuesday, December 16, 2025, 3:55 pm ET). Target rate probabilities for Dec 9, 2026 meeting.

- The FOMC made its third 25 basis point interest rate cut for the year during its December meeting, following its Sep. and Oct. cuts.
- Chairman Powell cited “gradual cooling in the labor market” and unemployment rates which have increased by 0.3 percentage points since June when it was 4.1% as a major reason to lower rates, outweighing potential inflation risks.
- There is an expectation that the Fed will make additional cuts during 2026.

WITH REVENUES WELL AHEAD OF CHAPTER 725, AN UPWARD ADJUSTMENT TO FY 2026 IS APPROPRIATE

SOURCE, \$ Mil	<u>December-July Revenues</u>			YTD Growth	Remaining Growth to Meet Ch. 725	Forecasted Annual Growth
	FY 2025 Actuals	FY 2026 Forecast	Revenues Rqd to Meet Ch. 725			
Withholding	\$10,554.0	\$10,852.2	\$10,519.1	5.9%	-0.3%	2.2%
Non-withholding	5,818.7	5,007.9	4,747.0	-4.3%	-18.4%	-15.2%
IIT Refunds	(2,293.3)	(1,915.7)	(1,917.3)	-23.7%	-16.4%	-18.4%
Net Individual Income	\$14,079.4	\$13,944.4	\$13,348.8	7.1%	-5.2%	-0.8%
Sales & Use Tax	2,801.9	2,899.7	2,859.2	5.8%	2.0%	3.6%
Corporate Income Tax	1,408.7	1,466.2	1,652.4	-20.6%	17.3%	7.8%
Insurance	541.5	503.7	503.7	0.0%	-7.0%	-7.0%
Wills, Suits, Deeds	276.0	335.6	337.5	12.4%	22.3%	18.2%
Interest Income	208.0	263.9	251.5	-1.0%	20.9%	6.7%
All Other	711.4	645.8	622.5	-4.5%	-12.5%	-9.9%
Total GF Revenues	\$20,026.8	\$20,059.3	\$19,575.7	5.2%	-2.3%	0.4%

- Through November, revenues are up 5.2% year-over-year.
- Chapter 725 assumed growth of just 0.4% in Fiscal Year 2026.
- Through the remainder of Fiscal Year 2026, revenues can decline 2.3% and still meet the Ch. 725 forecast.

DECEMBER GENERAL FUND FORECAST FOR FISCAL YEARS 2026-28

Composition of the December Revenue Forecast (GF dollars in millions)

	FY 2026	FY 2027	FY 2028
General Fund Revenues: GACRE	\$32,275.5	\$33,398.4	\$34,615.3
GF Revenue Growth: GACRE	3.3%	3.5%	3.6%
Post-GACRE Adjustments			
Economic Outlook Adjustments	\$0.0	\$0.0	\$0.0
Tax Policy Adjustments	(\$101.6)	(\$242.5)	(\$390.2)
Anticipated Sale of Property	\$8.9	\$0.0	\$0.0
General Fund Revenues: December	\$32,182.8	\$33,155.9	\$34,225.1
GF Revenue Growth: December	3.0%	3.0%	3.2%

Excludes GF transfers. Totals may not sum due to rounding.

THE DECEMBER FORECAST ADDS \$823 MILLION IN GF REVENUES IN FY 2026 AND \$566 MILLION IN FY 2027-2028

SOURCE	<u>Actuals</u> 2025	Fiscal Year 2026			Fiscal Years 2027 & 2028 Biennium			<u>Total</u> Change
		Ch. 725	December	Change	Ch. 725	December	Change	
Withholding	\$ 17,561.2	17,940.3	18,450.3	510.0	37,936.5	39,652.3	1,715.8	2,225.8
Nonwithholding	7,518.7	6,373.4	7,670.6	1,297.2	13,203.6	15,397.2	2,193.7	3,490.9
Refunds	(3,187.4)	(2,599.6)	(3,251.0)	(651.4)	(4,814.9)	(6,910.6)	(2,095.7)	(2,747.1)
Net IIT	\$ 21,892.4	21,714.2	22,869.9	1,155.7	46,325.2	48,139.0	1,813.8	2,969.6
Sales and Use Tax	4,812.7	4,987.4	4,967.6	(19.8)	10,587.0	10,288.3	(298.7)	(318.4)
Corporate Income	1,878.6	2,025.5	1,811.7	(213.9)	4,378.9	3,713.5	(665.4)	(879.2)
Insurance Company Premiums	541.5	503.7	536.9	33.2	1,066.8	1,119.9	53.0	86.3
Wills, Suits, Deeds, and Contract Fees	471.2	557.0	474.1	(82.9)	1,410.3	1,137.4	(272.9)	(355.8)
Interest Income	593.8	633.4	540.7	(92.7)	1,109.4	962.4	(147.0)	(239.7)
Alcohol	308.4	317.5	305.7	(11.8)	649.5	603.3	(46.2)	(58.1)
All Other	734.4	621.7	676.2	54.5	1,287.7	1,417.2	129.5	184.0
Total General Fund Revenues	\$ 31,233.0	31,360.4	32,182.8	822.5	66,814.8	67,381.0	566.2	1,388.7
Transfers	1,501.3	1,572.1	1,935.7	363.6	1,814.4	1,785.6	(28.8)	334.9
Total General Fund	\$ 32,734.3	32,932.5	34,118.6	1,186.1	68,629.2	69,166.6	537.4	1,723.5

Reflects the GACRE forecast adjusted for policy actions.

REVENUES MUST ONLY GROW 1.9 PERCENT OVER THE REMAINDER OF FY 2026 TO MEET THE NEW FORECAST

SOURCE, \$ Mil	December-July Revenues			FY 25 Growth	YTD Growth	Remaining Growth to Meet Dec Forecast	Forecasted Annual Growth
	FY 25 Actuals	FY 26 Dec Forecast	Revenues Rqd to Meet Budget				
Withholding	\$10,554.0	\$10,944.0	\$11,029.1	5.0%	5.9%	4.5%	5.1%
Non-withholding	5,818.7	6,016.2	6,044.1	14.5%	-4.3%	3.9%	2.0%
IIT Refunds	(2,293.3)	(2,420.8)	(2,568.7)	7.3%	-23.7%	12.0%	2.0%
Net Individual Income	\$14,079.4	\$14,539.4	\$14,504.6	7.8%	7.1%	3.0%	4.5%
Sales & Use Tax	2,801.9	2,851.8	2,839.5	2.2%	5.8%	1.3%	3.2%
Corporate Income Tax	1,408.7	1,414.9	1,438.6	-1.5%	-20.6%	2.1%	-3.6%
Insurance	541.5	536.9	536.9	15.6%	0.0%	-0.8%	-0.8%
Wills, Suits, Deeds	276.0	266.7	254.6	15.9%	12.4%	-7.7%	0.6%
Interest Income	208.0	157.9	158.8	-15.1%	-1.0%	-23.6%	-8.9%
All Other	711.4	667.4	665.2	10.2%	-4.5%	-6.5%	-5.8%
Total GF Revenues	\$20,026.8	\$20,435.1	\$20,398.2	6.1%	5.2%	1.9%	3.0%

- The new forecast is for 3.0% growth for Fiscal Year 2026. This is inclusive of proposed tax policy decreasing revenues by 0.2 percentage points.
- Revenues have grown 5.2% through the first five months.
- Revenues need only grow 1.9% over the remainder of the fiscal year to meet the December forecast.

PROPOSED TAX POLICY SAVES TAXPAYERS \$730 MILLION OVER FISCAL YEARS 2026-28

INCLUDES DEDUCTIONS FOR CAR LOAN INTEREST, TIPS AND OVERTIME INCOME

Tax Policy Adjustments (GF dollars in millions)	FY 2026	FY 2027	FY 2028
Tax Conformity, H.R. 1	(\$101.6)	(\$148.6)	(\$183.2)
Market Based Sourcing (effective TY 2027)	-	-	(\$29.1)
No Tax on Tips (25% TY 26, 50% TY 27 and 50% TY 28)	-	(\$18.3)	(\$35.2)
No Tax on Overtime (25% TY 26, 50% TY 27 and 50% TY 28)	-	(\$60.6)	(\$104.4)
No Tax on Car Loan Interest (25% TY 26, 50% TY 27 and 50% TY 28)	-	(\$15.0)	(\$38.3)
Total Policy Adjustments	(\$101.6)	(\$242.5)	(\$390.2)

THE INTRODUCED BUDGET WILL SUBSTANTIALLY CONFORM VIRGINIA TO RECENT FEDERAL TAX CHANGES*

Major Tax Conformity Provisions, H.R. 1 (GF dollars in millions)

	FY 2026	FY 2027	FY 2028
Miscellaneous provisions	\$3.0	\$12.7	\$20.7
1% floor on charitable contributions	4.3	7.7	9.2
0.5% floor on charitable contributions	15.8	40.4	42.5
Restructure of opportunity zones program	10.9	22.9	(27.0)
New limit on the value of itemized deductions (repeal of Pease limit)	(10.2)	(26.1)	(27.9)
Increases section 179 expensing limit to \$2.5 million	(28.2)	(19.3)	(16.1)
Increases the business interest deduction	(33.6)	(16.0)	(14.8)
50% of special depreciation allowance for qualified property	(63.6)	(86.8)	(90.8)
Domestic research deduction* (effective TY26)	-	(84.1)	(79.0)
Total Conformity to H.R. 1	(\$101.6)	(\$148.6)	(\$183.2)

**Deconforms from retroactive and catch-up provisions.*

CONFORMITY EASES THE ADMINISTRATIVE AND COMPLIANCE BURDEN ON THE STATE & TAXPAYERS

Benefits of Conformity

Dept. of Taxation

- Greater taxpayer compliance
- Lower administrative costs
- Fewer deconformity audits needed

Both

- Reliance on federal guidance
- No need to track deconformity items separately
- Fewer forms/worksheets

Taxpayers/Preparers

- Fewer modifications
- Less confusion between federal and state requirements
- Save time and money

TAX POLICY PRIORITIES

Virginia can decrease the tax burden on workers while also modernizing Virginia's antiquated business income tax code with fiscally responsible and sustainable tax policies.

Modernization

Tax Relief

Market-based Sourcing

- Increase Competitiveness & Fairness for Virginia Based Businesses

Permanent Elective PTET

Relief for Working Virginians

- Decrease Taxes on Tips, Overtime & Car Loan Interest

Permanent Increased Standard Deduction & Refundable EITC

TAX RELIEF FOR WORKING VIRGINIANS

No Tax on Car Loan Interest

- A Virginia deduction of 50% of the amount deducted on the taxpayer's federal return (phased-in at 25% for TY 2026) -- Up to \$288 in annual tax savings per return.*
- Federal Provision:
 - Deduction for up to \$10,000 for qualified vehicle loan interest.
 - Phaseout starting at \$100,000/\$200,000 for joint filers.
 - An eligible vehicle is a car, minivan, van, sport utility vehicle, pickup truck, or motorcycle, the final assembly of which occurs in the U.S. Expires for Tax Year 2029 and thereafter.



No Tax on Tips

- A Virginia deduction of 50% of the amount deducted on the taxpayer's federal return (phased-in at 25% for TY 2026) – Up to \$719 in annual tax savings per return.*
- Federal Provision
 - Deduction up to \$25,000 for qualified tips received by an individual in an occupation which traditionally and customarily receives tips.
 - Phaseout starting at \$150,000/\$300,000 for joint filers. Expires for Tax Year 2029 and thereafter.



*Assumes maximum Virginia deductions at 5.75% tax rate. Car loan interest deduction amount is \$10,000 (federal) and \$5,000 (Virginia). Tips deduction is \$25,000 (federal) and \$12,500 (Virginia) for single and joint filers.

TAX RELIEF FOR WORKING VIRGINIANS

No Tax on Overtime

- A Virginia deduction of 50% of the amount deducted on the taxpayer's federal return (phased-in at 25% for TY 2026)
 - Up to \$719 in annual tax savings per return.*
- Federal Provision:
 - Deduction up to \$12,500/\$25,000 for overtime premium pay during a given taxable year.
 - Only overtime pay required by the Fair Labor Standards Act ("FLSA") is eligible.
 - The deduction is only for the "premium" portion of a taxpayers' overtime pay, which is the amount that exceeds their regular rate of pay (i.e. the "half" portion of "time-and-a-half").
 - The deduction is phased out at a rate of \$100 for each \$1,000 if a taxpayer's adjusted gross income exceeds \$150,000/\$300,000 for joint filers.
 - Expires for Tax Year 2029 and thereafter.



*Assumes maximum Virginia deductions at 5.75% tax rate. Overtime deduction is \$12,500 for single filers and \$25,000 for joint filers at the federal level and \$6,250 (single) / \$12,500 (joint) at the state level.

TAX RELIEF FOR WORKING VIRGINIANS

Permanent Increased Standard Deduction

- Virginia's increased standard deduction amount is scheduled to expire on January 1, 2027, but the Governor's proposal would make the increased standard deduction amounts permanent.
- The Virginia standard deduction is currently \$8,750 (single) and \$17,500 (joint).
- Making the increased deduction permanent avoids an effective tax increase of up to \$330 (single) or \$660 (joint).
- Because the extension of the increased Virginia standard deduction is assumed in the official revenue forecast, this proposal would have a \$0 revenue impact on the budget.

Permanent Increased Refundable VA EITC

- Virginia's increased refundable Earned Income Tax Credit ("EITC") amount is scheduled to expire on January 1, 2027, but the Governor's proposal would make the increased refundable VA EITC permanent.
- The refundable VA EITC is currently 20% of the taxpayer's federal EITC amount.
- Because the extension of the increased refundable VA EITC is assumed in the official revenue forecast, this proposal would have a \$0 revenue impact on the budget.

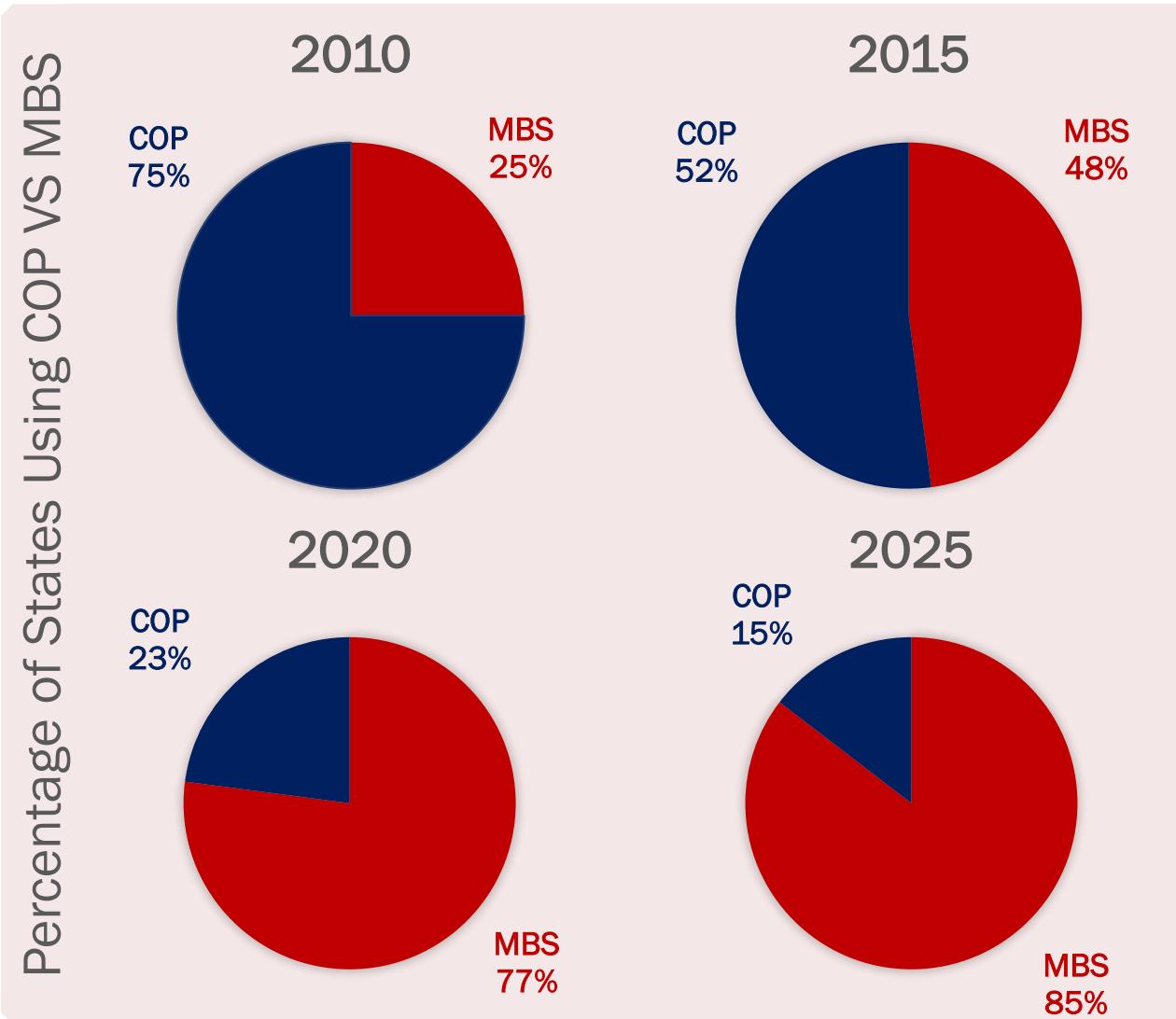
MODERNIZING THE CORPORATE INCOME TAX: MARKET-BASED SOURCING

- Under market-based sourcing (“MBS”), all sales (not just sales of tangible personal property) are treated equally and sourced to where the corporation’s market or customers are located.
- Virginia’s current Cost of Performance (“COP”) method penalizes Virginia-based multi-state service providers by using different rules for sales other than tangible personal property.

		Location of Sales for Income Tax Purposes		
Sales of ...		Location of Greatest Cost of Performance	Location Where Property is Delivered, Received or Used	
Tangible Personal Property		N/A		
Intangible Property & Services		Virginia		MBS States
				MBS States & Virginia

TRANSITION FROM COP TO MBS

- Under the Uniform Division of Income for Tax Purposes Act developed in the 1950s, states sourced sales of services and intangibles using Cost of Performance (“COP”).
- Virginia has fallen behind and now is in the minority of states still using the antiquated COP rules.
- MBS ensures Virginia is competitive with other states by:
 - 1) making out-of-state businesses pay their fair share and
 - 2) protecting in-state businesses from double taxation in other MBS states.



MODERNIZING THE CORPORATE INCOME TAX: MARKET-BASED SOURCING

- TAX conducted a workgroup over the summer to consider the impact of Virginia adopting MBS. The workgroup found that adopting MBS would generally be positive for economic development in Virginia.
 - A modification/carve-out was requested by the Defense and Telecom industries respectively due to their unique business models.
- While adopting MBS would result in a negative revenue impact in the first years of implementation due to a lag in compliance from out-of-state taxpayers, **MBS would result in a long-term sustainable revenue gain in later years** when out-of-state compliance normalizes.

MBS Tax Revenue Impact from All Corporations Based on Increasing Levels of Compliance					
(\$ In millions)	FY 2028	FY 2029	FY 2030	FY 2031	Total
Total Impact of MBS with Defense Modification & Telecom Carve-out	(\$29.1)	(\$4.0)	\$9.2	\$17.3	(\$6.6)

MODERNIZING THE PASS-THROUGH ENTITY TAX: MAKING PERMANENT THE ELECTIVE PTET

Why?

Under federal law, the amount of state and local taxes (“SALT”) individuals can deduction on their federal return is limited or “capped,” but businesses are not subject to the SALT cap.

What?

Under current Virginia law, owners of pass-through entities may elect to have the business pay Virginia income tax at the entity level, so their deduction will not be subject to the federal SALT cap.

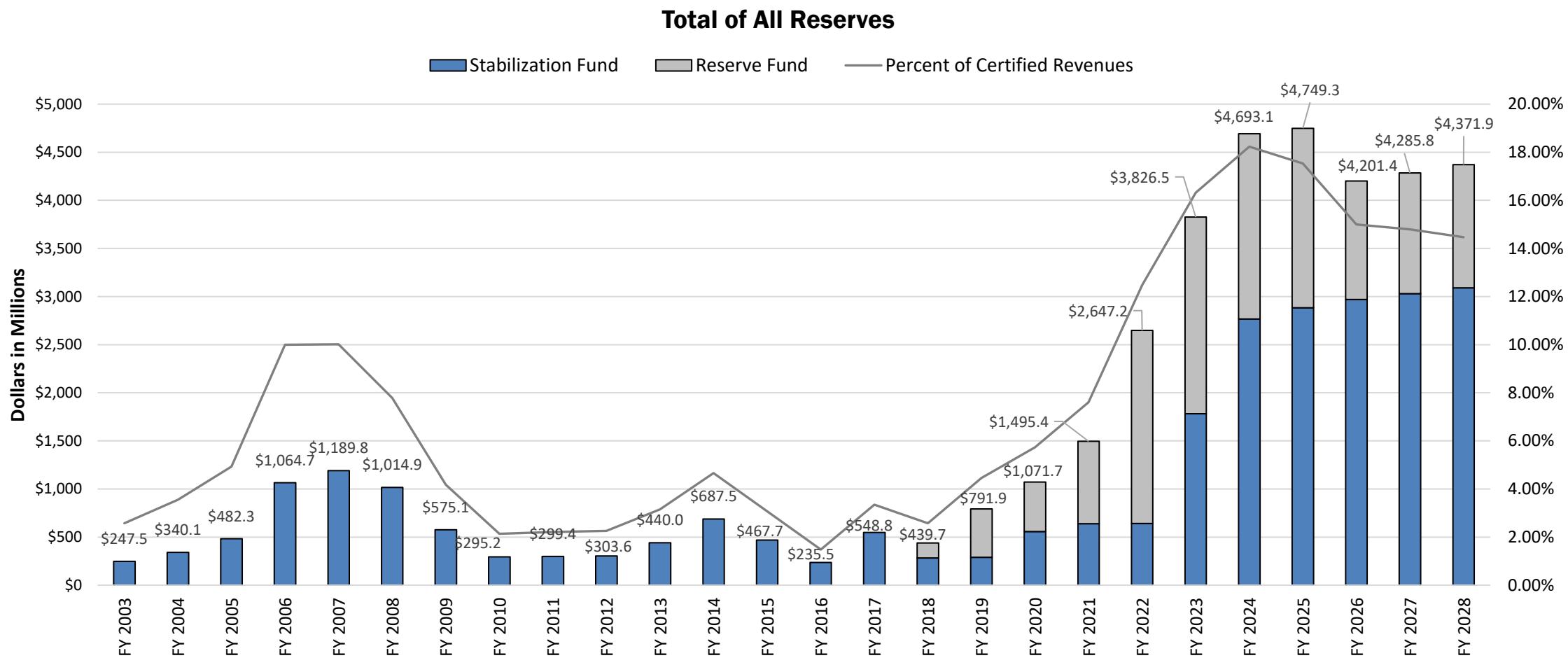
This elective tax is called the “PTET”.

Revenue Impact?

The PTET reduces the amount of federal income tax due, without changing the amount of Virginia income tax due, and as a result the PTET is revenue neutral.

The Virginia PTET is scheduled to expire on January 1, 2027, but the Governor’s proposal would make the elective PTET permanent.

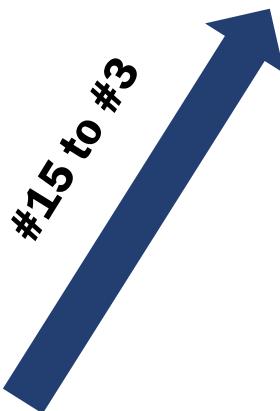
COMBINED RESERVE FUND BALANCES MEET THE 15 PERCENT STATUTORY CAP



VIRGINIA HAS PRIORITIZED RESERVE FUND GROWTH

Rainy Day Funds as Percent of GF Expenditures

Rank	Triple AAA State	FY 2019
1	Texas	19.3%
2	Georgia	11.1%
3	Minnesota *	10.8%
4	South Dakota	10.4%
5	Iowa	10.1%
6	Utah	9.2%
7	Indiana	8.8%
8	Ohio **	8.0%
9	North Carolina	7.8%
10	Missouri	6.8%
11	Tennessee	6.1%
12	Delaware	5.5%
13	Maryland	4.9%
14	Florida	4.5%
15	Virginia	3.7%



Rank	Triple AAA State	FY 2025 ^
1	Texas	28.3%
2	Georgia ***	N/A
3	Virginia	13.0%
4	Ohio	12.7%
5	North Carolina	11.4%
6	Iowa	10.4%
7	Minnesota	9.9%
8	South Dakota	9.3%
9	Tennessee	9.3%
10	Utah	9.3%
11	Maryland ****	7.9%
12	Indiana	7.8%
13	Florida	7.6%
14	Missouri	6.1%
15	Delaware	5.0%

Virginia and NASBO calculations differ.
VA calculation >= 15% of revenues.

Sources: National Association of State Budget Officers "The Fiscal Survey of States" (Fall 2021 and Spring 2025 Reports). * Minnesota was not a triple AAA rated state in 2019. Minnesota was upgraded to triple AAA in July of 2022. ** Ohio was not a triple AAA rated state in 2019. Ohio was upgraded to triple AAA in December of 2023. *** Estimated 2025 Rainy Day Fund balance for Georgia was not available at time of Spring 2025 NASBO Report. Ranking remains at #2 based on 2024 ranking. **** Maryland was downgraded to Aa1 by Moody's in May of 2025 and is no longer a triple AAA rated state. ^ 2025 Rainy Day Fund balances are estimates and do not reflect final official balances.

SUMMARY OF GENERAL FUND RESOURCES

	FY 2026 HB/SB 29	FY 2027 HB/SB 30	FY 2028 HB/SB 30
Revenue			
GACRE Forecast	\$32,275.5	\$33,398.4	\$34,615.3
Tax Policy Changes	(\$101.6)	(\$242.5)	(\$390.2)
Other Revenue Changes	\$8.9		
Total Revenue	\$32,182.8	\$33,155.9	\$34,225.1
Adjustments To Balance			
Amounts Reserved on Balance Sheet from FY 25 Surplus	\$1,463.4		
Impact of Vetoed FY 26 Amounts	\$14.3		
Other Balances/Adjustments	\$291.3	(\$0.5)	(\$0.5)
Total Adjustments to Balance	\$1,769.1	(\$0.5)	(\$0.5)
Transfers			
ABC Profits	\$160.9	\$146.3	\$133.3
K-12 Sales Tax	\$606.9	\$620.5	\$636.4
Other	\$1,167.9	\$124.3	\$124.8
Total Transfers	\$1,935.7	\$891.2	\$894.5
Prior Year Remaining Balance	\$13.3	\$2,124.7	\$721.0
Total GF Resources	\$35,900.9	\$36,171.3	\$35,840.1
Total GF Appropriation (Operating plus Capital)	\$33,776.2	\$35,450.3	\$35,534.7

LONGER-TERM OUTLOOK CONFIRMS STRUCTURAL BALANCE

GENERAL FUND RESOURCES	FY 2026	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032
Prior Year Balance	\$13.3	\$2,124.7	\$721.0	\$305.4	\$13.8	\$387.4	\$1,209.9
Revenue							
Net Individual Income	\$22,869.9	\$23,688.9	\$24,450.1	\$25,397.1	\$26,600.1	\$27,922.7	\$29,249.6
Sales and Use Tax	\$4,967.6	\$5,079.0	\$5,209.3	\$5,359.5	\$5,524.7	\$5,711.2	\$5,873.3
Corporate Income Tax	\$1,811.7	\$1,825.2	\$1,888.3	\$2,087.7	\$2,257.6	\$2,416.2	\$2,587.9
All Other Sources	\$2,533.6	\$2,562.8	\$2,677.4	\$2,797.8	\$2,887.1	\$2,972.3	\$3,062.5
Total Revenue	\$32,182.8	\$33,155.9	\$34,225.1	\$35,642.0	\$37,269.4	\$39,022.4	\$40,773.3
Adjustments to Balance	\$1,769.1	(\$0.5)	(\$0.5)	(\$0.5)	(\$0.5)	(\$0.5)	(\$0.5)
Transfers	\$1,935.7	\$891.2	\$894.5	\$903.1	\$914.6	\$929.5	\$949.3
Total General Fund Resources	\$35,900.9	\$36,171.3	\$35,840.1	\$36,850.0	\$38,197.3	\$40,338.8	\$42,932.0
GENERAL FUND APPROPRIATION	FY 2026	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032
CH 725 Appropriation (FY 26) / Base Budgets	\$32,718.3	\$32,718.3	\$32,718.3	\$32,718.3	\$32,718.3	\$32,718.3	\$32,718.3
Base Adjustments	\$0.0	(\$44.8)	(\$44.8)	(\$44.8)	(\$44.8)	(\$44.8)	(\$44.8)
Other Operating Amendments	\$857.9	\$2,086.7	\$2,661.2	\$3,962.7	\$4,936.4	\$6,255.4	\$7,282.6
Total Operating	\$33,576.2	\$34,760.2	\$35,334.7	\$36,636.2	\$37,610.0	\$38,928.9	\$39,956.1
Capital Outlay	\$200.0	\$690.0	\$200.0	\$200.0	\$200.0	\$200.0	\$200.0
Total GF Appropriation	\$33,776.2	\$35,450.3	\$35,534.7	\$36,836.2	\$37,810.0	\$39,128.9	\$40,156.1
GF BALANCE (RESOURCES LESS APPROPRIATION)	FY 2026	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032
Resources Less Approp - Annual Balance	\$2,111.4	\$721.0	(\$415.7)	\$13.8	\$373.6	\$1,209.9	\$1,566.0
Resources Less Approp - Cumulative/Biennium	\$2,124.7		\$305.4		\$387.4		\$2,775.9

Source: VA Department of Planning and Budget.

CONCLUSION

- Through the first five months of FY 2026, general fund revenues are up 5.2% year-over-year, driven mainly by growth in individual income tax. Relative to the official forecast assumed in Chapter 725, revenues to date are \$484 million higher than projected.
- Virginia payroll withholding, the best indicator of economic performance and largest component of General Fund revenue, has grown 5.9% year-to-date versus last year and is ahead of projections by \$414 million. Federal actions have not had the adverse impact widely anticipated due to Virginia's unique agency profile which is concentrated in defense and intelligence.
- Sales tax collections, up 5.8% fiscal year-to-date, indicate continued strength of the consumer in Virginia.
- The budget introduced today requires General Fund revenues to grow 3.0% this fiscal year. With year-to-date performance so strong, that equals just 1.9% for the next seven months.
- Fiscal Years 2027 and 2028 are forecasted at similarly prudent levels of 3.0% and 3.2%, respectively. (These growth rates are based on the GACRE approved forecasts of 3.3%, 3.5% and 3.6% with the addition of new tax policy adjustments.)
- The conservative forecast underpins the ability to fund shared priorities while maintaining structural balance and safeguarding the Commonwealth's triple AAA bond rating
- The Governor's introduced budget invests more than \$6.4 billion GF in new operating and capital spending while providing \$730 million in tax relief between FY 2026 and FY 2028.
- Critical new investments in shared priorities, including Medicaid, K-12 Rebenchmarking, and increased compensation for teachers, support staff, sheriffs and state employees.