



COMMONWEALTH of VIRGINIA

Office of the Governor

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MEMORANDUM

TO: The Honorable Timothy M. Kaine
THROUGH: The Honorable William H. Leighty
FROM: Jody M. Wagner
SUBJECT: April Revenue Data

This month's revenue report incorporates the revised general fund revenue forecast that reflects actions of the 2007 General Assembly. Under the revised forecast, general fund revenues are projected to grow 6.5 percent in fiscal year 2007.

April is a significant month for revenue collections. In addition to normal collections in withholding and sales taxes, final payments for tax year 2006 and the first estimated payment for tax year 2007 are due from corporations. A large amount of estimated and final payments from individuals, which are due May 1, are also typically received in April.

Total general fund revenue collections grew 2.5 percent in April compared to April 2006. On a year-to-date basis, revenues grew 3.6 percent over the same period last year, significantly behind the annual forecast of 6.5 percent. Collections of individual nonwithholding and corporate income taxes are trailing their forecasts. In addition, of particular note, individual income tax refunds have significantly exceeded expectations, further dampening growth.

Two factors are distorting growth – the end of the Accelerated Sales Tax Program in fiscal year 2006 and the controlled production at TAX due to implementation of new systems, which slowed processing of individual and corporate refunds during the first half of last fiscal year. Adjusting for these factors, revenues grew 2.9 percent through April of fiscal year 2007, behind the adjusted forecast of 5.4 percent annual growth.

National Economic Indicators

Most national indicators depict a slowdown in the expansion of the economy. The national housing market and oil prices continue to be the significant factors affecting the short-term outlook.

- According to the advance estimate, real GDP grew 1.3 percent in the first quarter of 2007, the slowest growth in four years. Growth was below expectations and significantly slower than the 2.5 percent posted in the fourth quarter of last year. The most significant drag on the economy is homebuilding, which cut one percentage point from growth. Real investment in residential structures has fallen for six consecutive quarters and is 17 percent below its peak.

- Employers added a modest 88,000 jobs to payrolls in April, and gains for prior months were revised down. The weakness was most evident in construction, manufacturing, retail trade, and finance. In a separate report, the unemployment rate rose slightly from 4.4 to 4.5 percent.
- Initial claims for unemployment fell by 21,000 to 305,000 during the last week of April. The four-week moving average fell slightly, from 333,000 to 329,000 and is consistent with an expanding economy.
- Inflation remains contained. An increase in energy prices pushed the Consumer Price Index up 0.6 percent in March, following a 0.4 percent increase in February. Core inflation, excluding food and energy, increased 0.1 percent in March resulting in growth of 2.5 percent over the last year.
- The Institute of Supply Management index increased from 50.9 to 54.7 in April, the largest monthly increase since September 2005. This is a significant improvement from the sluggish growth over the last two quarters.
- The Conference Board's index of leading indicators rose 0.1 percent to 137.4 in March, the first increase since December.
- The Conference Board's index of consumer confidence fell from 108.2 to 104.0 in April, the second monthly decline following four consecutive gains. Both the expectations and current conditions components declined, with most of the weakness in the assessment of current conditions.

Virginia Economy

In Virginia, payroll employment grew 1.2 percent in March. Northern Virginia posted job growth of 2.0 percent in March. Jobs grew by 1.3 percent in Hampton Roads, 2.0 percent in Richmond-Petersburg, and 2.0 percent in the western MSAs. The unemployment rate fell from 3.2 percent to 3.1 percent in March.

The Virginia leading index fell 0.5 percent in March, its first decline in four months. An increase in building permits offset the negative impact of falling auto registrations and rising initial unemployment claims. The regional indices fell in nine of the state's eleven metropolitan areas in March. The indices in Hampton Roads and Harrisonburg increased for the month.

April Revenue Collections

April is a significant month for revenue collections. In addition to normal collections in withholding and sales taxes, final payments for tax year 2006 and the first estimated payment for tax year 2007 are due from corporations. A large amount of estimated and final payments from individuals, which are due May 1, are also received in April.

Individual Income Tax Withholding (54% of general fund revenues): Despite an additional deposit day compared with April of 2006, collections of payroll withholding taxes grew a modest 4.9 percent in April. Year-to-date withholding growth is 5.7 percent, matching the projected annual growth rate. Collections must grow 5.2 percent in the May-June period to attain the annual forecast; however, growth in the previous three months has been below 5.0 percent.

Individual Income Tax Nonwithholding (18% of general fund revenues): April is a significant month for nonwithholding collections. Final payments for tax year 2006 and the first estimated payment for tax year 2007 are both due May 1.

April collections were \$646.3 million compared with \$620.7 million in April of last year, a 4.1 percent increase. To date, about 65 percent of the nonwithholding forecast has been collected, and collections during this period are 7.1 percent above the same period last year, which is below the projected annual growth of 10.2 percent.

Typically, a large portion of final payments due May 1 are received in April, however, the amount varies from year to year. Estimated and final payments will continue to be processed in May; therefore, one must consider April and May collections together to accurately assess growth in this source. The final estimated payment for this fiscal year is due June 15.

Individual Income Tax Refunds: In the latter half of calendar year 2005, the transition to a new computer system required TAX to process a limited number of tax returns in the fall, resulting in few refunds for that period. With the

new system in place, TAX returned to a normal schedule for processing this year.

Through April, \$1.4 billion have been refunded compared with \$1.1 billion in the same period last year. For the filing season beginning January 1, about 2.2 million refunds have been issued, compared with 2.1 million issued in the same period last year. The average check size is up a sharp 13 percent compared with the forecast of 5 percent.

For the first ten months of the fiscal year, refunds have already surpassed the forecast of \$1.3 billion. Over the last three years' individual refunds issued in the last two months have been sizable, averaging a total of about \$167 million.

Sales Tax (20% of general fund revenues): Collections of sales and use taxes, reflecting March sales, grew 17.0 percent in April. Five Saturdays in March and Easter falling early in April contributed to the growth. Year-to-date growth in sales and use taxes of 11.2 percent is inflated due to the repeal of the Accelerated Sales Tax program. Adjusting for the repeal of this program, growth in this source was 4.2 percent through April, consistent with the forecast of 4.2 percent growth needed to meet the annual estimate.

Corporate Income Tax (6% of general fund revenues): In April, corporations made their first estimated payment for tax year 2007, and made either a final or extension payment for tax year 2006. A sample of filings by large corporations revealed payments attributable to calendar year 2006 liabilities declined 19 percent as compared to payments last year for calendar year 2005 liabilities. Estimated payments toward calendar year 2007 liability fell 4 percent for the same sample compared to last year's estimated payments for calendar year 2006.

Net collections of corporate income tax were \$147.6 million in April 2007, compared with \$127.4 million in April of last year, however, April 2006 collections were impacted by the delayed processing of corporate refunds that were postponed due to TAX's controlled production. Year-to-date collections are up 0.3 percent compared to the same period last year, trailing the annual projected growth rate of 3.4 percent.

Wills, Suits, Deeds, Contracts (4% of general fund revenues): Wills, suits, deeds, and contracts – mainly recordation tax collections – fell 2.2 percent in April as the housing market continued to slow. Year-to-date collections in this source declined 16.6 percent from last year, close to the estimate of a 20.2 percent decline.

Other Revenue Sources

The following list provides data on April collections for other revenue sources:

	Year-to-Date	Annual Estimate
Insurance Premiums Taxes (3% GF revenues)	-0.4%	2.9%
ABC Taxes (1.0% GF revenues)	3.9%	3.6%
Interest Income (0.6% GF revenues)*	63.3%	104.0%

All Other Revenue: Receipts in All Other Revenue grew 43.1 percent in April – \$37.1 million compared with \$25.9 million in April of last year. Most of the increase was in payments from public service corporations. For the fiscal year-to-date, collections of All Other Revenue are 2.4 percent below the same period in fiscal year 2006, lagging the annual estimate of 3.6 percent growth.

Lottery Revenues: Net income of \$39.0 million in April was 3.2 percent below April of last year mainly due to higher prize expenses. Sales continue to be strong in the daily and scratch games, leading to a 3.1 percent increase in April sales. Year-to-date, net income is down 6.9 percent, better than the forecast of a 10.7 percent decline.

Summary

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Two factors are distorting growth – the end of the Accelerated Sales Tax Program in fiscal year 2006 and the controlled production at TAX due to implementation of new systems, which slowed processing of individual and corporate refunds during the first half of last fiscal year. Adjusting for these factors, revenues grew 2.9 percent through April of fiscal year 2007, behind the adjusted forecast of 5.4 percent annual growth.

Total general fund collections are significantly trailing the annual estimate. May and June are also important collection months, with continued processing of final payments for individual and corporate income taxes in May, and the second estimated payment for individuals, corporations, and insurance companies due in June.