



COMMONWEALTH of VIRGINIA

Office of the Governor

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MEMORANDUM

TO: The Honorable Mark R. Warner

THROUGH: The Honorable William H. Leighty

FROM: John M. Bennett

SUBJECT: February Revenue Data

This month's revenue report reflects in the first column the revised revenue forecast provided to the General Assembly on January 31, 2005. The mid-session forecast increased projected fiscal year 2005 revenues by \$249.0 million. The revised growth rates required to attain the forecast are listed in the last column. Total general fund revenue is now forecast to grow 10.3 percent.

February is not normally a major collections month. No estimated payments for individuals or corporations are due, so collections in these areas flow from out-of-cycle payments or compliance activity by the Tax Department. Collections for the month are dominated by normal withholding and sales taxes, as well as recordation taxes.

Total general fund revenue collections grew 11.3 percent in February. Collections for sales taxes (reflecting January sales) and recordation taxes were principally responsible. A small number of one-time payments by individuals also contributed. Adjusting for the rate increase in sales and recordation taxes enacted in HB 5018, underlying revenue growth in February was 7.0 percent.

Through February, revenues have grown 14.1 percent above the same period last year, well ahead of the mid-session required growth of 10.3 percent. Because revenues grew 15.4 percent during the last four months of fiscal year 2004, the year-to-date growth rate is expected to moderate over the remainder of the fiscal year.

National Economic Indicators

Most economic indicators continue to depict a healthy national economy, although the recent trends in employment growth remain sub-par.

- Real GDP grew 3.8 percent in the fourth quarter of 2004, revised up from 3.1 percent.

- The labor market increased ahead of expectations in February. Payroll employment grew by 262,000 jobs, while January gains were revised downward to 132,000. Even with the strong showing in February, three-month and six-month trends remain below what would be expected given other economic indicators.

- Initial claims for unemployment fell to 310,000 during the last week in February. The four-week moving average fell to 307,000, consistent with an expanding job market, and an improvement over recent trends.
- Activity in the manufacturing sector continues to slow. The Institute of Supply Management index fell to 55.3 in February -- the lowest reading since August of 2003.
- The Conference Board's index of leading indicators fell 0.3 percent in January, with six of its ten components declining. Consumer expectations and vendor performance accounted for much of the decrease.
- Following a solid increase in January, the Conference Board's index of consumer confidence fell 1.1 points to 104.0 in February. The "present situation" component increased for the fourth consecutive month, while the "future expectations" component declined.
- The consumer price index rose 0.1 percent in January, restrained by the second monthly decline in energy prices. Core inflation rose at an annualized rate of 2.3 percent.

Virginia Economy

The federal government has now approved re-benchmarked employment data for calendar year 2003 and 2004, based on unemployment insurance reports provided by all employers to the VEC. The re-benchmarked information is now being analyzed and will result in revised estimates of employment growth for the state and for each region for 2003 and 2004.

The federal government has also identified a revised group of 10,000 firms who are asked to submit employment surveys to the VEC each month. January is the first month that this revised group of firms reported employment results.

In Virginia, this revised group of firms reported payroll employment growth of 2.8 percent in January compared with the same month last year. Northern Virginia firms reported payroll growth of 5.6 percent, followed by Richmond-Petersburg and Hampton Roads, each with 2.3 percent growth. The unemployment rate increased to 3.7 percent in January.

The Virginia Leading Economic Index increased 0.4 percent in January, following a decline of 0.2 percent in December. Strong growth in auto registrations and lower initial unemployment claims made positive contributions to the January index, but were offset somewhat by decreases in building permits and a lower U.S. leading index. On a regional basis, the indexes for Bristol, Lynchburg, Danville, Charlottesville, Northern Virginia, and Hampton Roads grew in January. In Richmond, the index registered no change, while the index for Roanoke declined.

February Revenue Collections

Total general fund revenue collections grew 11.3 percent in February. Collections for sales taxes (reflecting January sales) and recordation taxes were principally responsible. A small number of one-time payments by individuals also contributed. Adjusting for the rate increase in sales and recordation taxes enacted in HB 5018, underlying revenue growth in February was 7.0 percent. Through February, revenues have grown 14.1 percent above the same period last year, well ahead of the mid-session required growth of 10.3 percent.

Individual Income Tax Withholding (62% of general fund revenues). Withholding collections in February were essentially flat - growing 0.4 percent. This result reflects the collections comparison to a very strong February of 2004, when withholding grew 9.3 percent, rather than underlying economic weakness.

Through February, withholding collections are 7.2 percent above the same period last year - close to the 6.4 percent rate required to meet the mid-session forecast. Because withholding collections grew 9.4 percent during the last four months of fiscal year 2004, the year-to-date growth rate for withholding is expected to moderate further over the remainder of the fiscal year.

Individual Income Tax Nonwithholding (12% of general fund revenues). February is not a significant month for

nonwithholding receipts. A total of \$35.4 million was collected in February, compared to \$18.2 million in February of last year. This increase is attributable to a few large, one-time payments generated by compliance activities.

To date, about 47 percent of the nonwithholding forecast has been collected, and collections are 29.3 percent greater than last year. The majority of the remaining collections in this source will occur in April and May, with both final payments for tax year 2004 and estimated payments for the current year due May 1.

Individual Income Tax Refunds. Refunds this month totaled \$260.7 million compared with \$259.4 million in February of last year. On a year-to-date basis, refunds are \$12.4 million above the same period last year. Growth of 2.7 percent is slightly below the annual estimate of 6.5 percent as TAX heads into the peak processing period for income tax refunds.

For the filing season beginning January 1, about 840,200 refunds have been issued, compared with 835,500 issued in the same period last year.

Sales Tax (22% of general fund revenues). Collections of sales and use taxes, representing January sales, grew 18.4 percent in February. The holiday shopping season (November through January) finished with growth of 10.3 percent -- ahead of expectations.

Year-to-date growth of 14.5 percent is very close to the mid-session forecast of 14.7 percent. Adjusting for the rate increase effective September 1, collections were up 10.7 percent for the month and 8.0 percent year-to-date.

Sales tax collections will need to remain strong for the remainder of the fiscal year in order to meet the forecast. Sales tax collections during the last four months of fiscal year 2004 grew 13.1 percent -- the strongest four-month period since fiscal year 1986.

Corporate Income Tax (3% of general fund revenues). As with individual nonwithholding, February is not a significant month for corporate income tax collections. Corporate income tax collections totaled \$8.6 million in February compared with -\$4.6 million in February of last year. Estimated payments in February were higher than last year, and refunds were significantly lower.

To date, about 51 percent of forecast revenues have been collected. Through February, corporate income tax collections have grown 91.6 percent compared with the same period last year -- well ahead of the mid-session forecast of 29.0 percent growth. Estimated and final payments for most corporations are due April 15.

Other Revenue Sources

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

	Year-to-Date	Required to Meet Estimate
Insurance Premiums Tax (3.0% GF revenues)	6.7%	8.5%
ABC Taxes (1.1% GF revenues)	2.9%	0.1%
Public Service Corporations (0.7% GF revenues)	2.2%	0.6%
Interest Income (0.7% GF revenues)	23.2%	12.4%

All Other Revenue. All Other Revenue grew \$11.4 million in February - 22.4 percent above last year. Collections doubled in the largest component of All Other Revenue -- wills, suits, deeds, and contract fees. Of the \$40.8 million collected in this source, \$36.4 million was recordation tax receipts. Adjusting for the rate increase effective September 1, recordation receipts grew by 28.7 percent. Year-to-date, collections of All Other Revenue are 27.5 percent above the

same period last year -- ahead of the mid-session estimate of 14.1 percent growth.

Lottery Revenues. In February, Lottery net income declined 24.5 percent over last year, due to a decline in Mega Millions sales and higher Pick 3 payouts. The entire decline in sales was in Mega Millions, which had extremely high sales last February as the advertised jackpot rolled through the month, culminating in a \$239 million jackpot won in Virginia. On a year-to-date basis, net income has increased by 0.9 percent, below the annual forecast of 3.8 percent growth. Lottery staff indicated that if significantly higher than expected prize payouts continue, net income will fall below projections.

Summary

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Through February, revenues have grown 14.1 percent above the same period last year, well ahead of the mid-session required growth of 10.3 percent. Because revenues grew 15.4 percent during the last four months of fiscal year 2004, the year-to-date growth rate is expected to moderate over the remainder of the fiscal year.