



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: May Revenue Data

May is a very significant month for revenue collections. In addition to normal monthly collections in withholding and sales taxes, estimated and final payments for individual income taxes are due May 1. In addition, corporations with a fiscal year ending other than on December 31 – primarily retailers – have final payments due in May.

Total general fund revenue grew 18.1 percent in May 2006 compared with the same month last year. Strong growth in individual withholding taxes and extraordinary growth in individual nonwithholding taxes offset weak collections in sales and use taxes, recordation taxes, and corporate income taxes. This strong increase in nonwithholding income tax payments provided the foundation for the estimated \$105 million surplus that I communicated to the money committee chairs on June 2, 2006.

On a year-to-date basis, total revenue has grown 10.3 percent. Fiscal year 2006 revenues are overstated on an annual basis because revenue losses from the reduced Accelerated Sales Tax program and the reduction on the sales tax on food that will occur in the last month of this fiscal year are not reflected in collections to date. Accounting for these known revenue losses, total general fund revenues are increasing at 8.5% -- ahead of the annual 7.4% forecast.

National Economic Indicators

Current economic indicators continue to depict the national economy slowing somewhat from the strong growth of the first quarter. Higher interest rates and a cooling housing market are expected to moderate economic growth over the rest of the calendar year.

- Employment indicators were mixed in May. Payroll employment grew by 75,000 jobs in May, well below consensus expectations. The three-month average job gain fell from 180,000 to 125,000. In a separate report, the unemployment rate fell slightly to 4.6 percent.
- Initial claims for unemployment dropped from 337,000 to 302,000 during the last week of May. The four-week moving average fell to 328,000, which remains consistent with a healthy labor market.

- The Conference Board index of leading indicators fell 0.1 percent in April, slightly below expectations. The six-month annualized growth rate fell to 2.9 percent from March's 4.7 percent, and is consistent with strong first quarter growth moderating to slower growth in the second quarter.
- Despite a slight acceleration in April, inflation appears to be controlled. The Consumer Price Index jumped 0.6 percent in April, following a 0.4 percent increase in March. Rising energy prices were responsible for most of the increase, although core inflation rose 0.3 percent for the month, bringing the annual rate of core inflation to 2.3 percent.
- The manufacturing sector remains healthy, although growth slowed in May. The Institute of Supply Management index fell from 57.3 to 54.4 in May.
- The Conference Board's index of consumer confidence dropped 6.6 points to 103.2 in May; however, the index remains in the relatively high range seen prior to Hurricane Katrina. High energy prices, rising interest rates, and the slowing housing market are all drags on consumer confidence.

Virginia Economy

In Virginia, payroll employment grew 1.9 percent in April. Growth in Northern Virginia remained well above the rest of the state, with a 3.3 percent gain. Jobs in the western MSAs grew by 2.1 percent, followed by Hampton Roads with 1.6 percent, and Richmond-Petersburg with 1.4 percent growth. The unemployment rate decreased from 3.2 percent to 3.1 percent in April.

The Virginia Leading Index rose 0.3 percent in April, its third consecutive monthly gain. An increase in auto registrations and a drop in initial claims for unemployment made positive contributions to the index, offsetting a decline in building permits. As was the case last month, ten of the eleven metro areas in Virginia saw an increase in their index, with the leading index for Hampton Roads falling for the month.

May Revenue Collections

Total general fund revenue grew 18.1 percent in May. Strong growth in individual withholding taxes and extraordinary growth in individual nonwithholding taxes offset weak collections in sales and use taxes, recordation taxes, and corporate income taxes. On a year-to-date basis, total revenue has grown 10.3 percent. Fiscal year 2006 revenues are overstated on an annual basis because revenue losses from the reduced Accelerated Sales Tax program and the reduction on the sales tax on food that will occur in the last month of this fiscal year are not reflected in collections to date. Accounting for these known revenue losses, total general fund revenues are increasing at 8.5% -- ahead of the annual 7.4% forecast.

Individual Income Tax Withholding (54% of general fund revenues): Boosted by an extra deposit day, collections of payroll withholding taxes grew 11.7 percent in May. Year-to-date withholding growth is 6.9 percent – ahead of the projected annual growth rate of 6.2 percent.

Individual Income Tax Nonwithholding (17% of general fund revenues): May is a significant month for nonwithholding receipts because final payments for tax year 2005 and the first estimated payment for tax year 2006 are both due May 1.

May collections were \$542.1 million compared with \$326.0 million in May of last year, a 66.3 percent increase. With the due date of May 1, many of the payments are received in April, so it is important to look at the two months together to assess growth in this source. Together, nonwithholding collections in April and May were 26.8 percent ahead of the same period last year. The growth is extraordinary considering that collections in April and May of 2005 grew 38 percent from the previous year. The last estimated payment to be received for this fiscal year is due June 15.

Individual Income Tax Refunds: This month, TAX issued \$146.4 million in refunds compared with \$108.5 million in May of last year. Fiscal year-to-date, refunds are 2.3 percent above the same period last year. For the filing season beginning January 1, TAX issued about 2.3 million refunds, similar to the number issued in the same period last year.

Sales Tax (19% of general fund revenues): Collections of sales and use taxes, reflecting April sales, fell 1.8 percent

in May. Adjusting for the effects of tax relief on food, growth was 4.4 percent for the month.

Year-to-date growth is 2.7 percent through May, ahead of the estimate of a 3.9 percent decline. However, the reduced Accelerated Sales Tax program will decrease collections by \$200.1 million in June and year-to-date growth is expected to drop to the 3.9 percent forecast decline.

Corporate Income Tax (6% of general fund revenues): May is typically not a significant month in corporate income tax collections, with final or extension payments due mainly from retailers, who typically have a January 31st close to their fiscal year. Such payments vary significantly from year to year. Collections this month totaled \$11.4 million, compared to \$34.9 million received last year. Through May, corporate income tax collections are up 46.7 percent for the year, ahead of the forecast of 38.1 percent growth.

Other Revenue Sources

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

	Year-to-Date	Required to Meet Estimate
Insurance Premiums Taxes (3% GF revenues)	0.2%	5.1%
ABC Taxes (1.0% GF revenues)	6.2%	-0.5%
Public Service Corporations (0.6% GF revenues)	-0.5%	2.6%
Interest Income (0.7% GF revenues)*	25.9%	20.9%

**Approximately 60% of the interest for the current quarter is due to nongeneral funds and will be transferred in June.*

All Other Revenue: Receipts in All Other Revenue fell 5.8 percent in May -- \$88.4 million compared with \$93.8 million in May of last year. Growth in the largest component of all other revenue -- wills, suits, deeds, and contract fees -- drove growth in this source over the last few years. Collections in wills, suits, deeds, and contract fees (mostly recordation tax receipts) fell 5.8 percent in May, the fourth consecutive month of flat or negative growth. Year-to-date growth in this source stands at 21.2 percent, very close to the estimate of 21.3 percent growth. For the fiscal year, collections of All Other Revenue are 5.3 percent above fiscal year 2005, ahead of the annual estimate of 4.0 percent growth.

Lottery Revenues: Lottery net profits decreased 16.0 percent for the month. For the month, all games experienced a decline in sales. The North Carolina Lottery sales impacted Virginia Lottery sales more than expected this month as North Carolina introduced PowerBall to its product mix in May. Year-to-date net income growth rate of 8.4 percent is well ahead of the projected 2.4 percent annual rate.

Transportation Revenues - Motor Fuels Taxes: Motor fuels tax collections increased by 2.7 percent in May and 2.1 percent in fiscal year 2006. The combination of refinery maintenance and the transition to ethanol-based reformulated gasoline drove gas prices considerably higher over the past few weeks which may have reduced consumption. This could adversely affect revenue collections over the next few months. As these supply pressures dissipate, gas prices are expected to soften. The potential for midsummer price spikes exists if demand increases or supply is threatened.

Transportation Revenues – Motor Vehicle Sales Tax: Motor vehicle sales tax collections increased 10.4 percent in May, after falling by 18.8 percent in April. Year-to-date collections are up 2.4 percent in fiscal year 2006. Sales of new vehicles increased 3.9 percent and used vehicles increased 1.3 percent in May.

Summary

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estimated \$105 million surplus that I communicated to the money committee chairs on June 2, 2006.

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June is another significant month for revenue collections, and typically accounts for about 11 to 12 percent of total general fund revenue for the year. June collections include receipts of individual and corporate estimated payments, estimated payments for insurance premiums and corporate franchise fees, along with regular monthly collections in other sources.

June collections must total about \$1.5 billion to meet the forecast for the fiscal year. Receipts last June totaled \$1.7 billion; however, last year's receipts included \$181.6 million in Accelerated Sales Tax payments that will not occur this year. Given the current solid economic climate, total general fund revenues are tracking to be within 1 percent, or less than \$147 million, of the forecast. Preliminary revenues for the fiscal year will be available by mid-July.
