



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: April Revenue Data

This month's revenue report reflects adjustments for actions of the 2002 Session of the General Assembly. Through a variety of actions, the General Assembly added \$85.1 million to the February re-estimate of general fund revenues. With these changes, total general fund revenues are now projected to decline by 1.7 percent this fiscal year.

April collections fell 11.1 percent below collections for April of last year. The drop is primarily due to an unusually large number of individual income tax refunds issued in April and continued sluggish growth in individual income tax collections. On a year-to-date basis, total general fund revenue collections are 3.6 percent below collections for the same period last year.

In order to attain the FY 2002 forecast, individual income tax withholding collections must gain momentum, nonwithholding receipts must not decline more than was forecast, and income tax refunds must stay near their projected total.

National Economic Indicators

Most national economic indicators suggest the economy has entered a slow recovery.

- First quarter real GDP grew 5.8 percent, the fastest growth since the fourth quarter of 1999. Although a slowdown in inventory liquidation accounted for half of the growth, a large portion of the growth was actually attributable to final sales. This is an indication that underlying demand is improving;
- Labor market indicators also suggest that the employment picture is improving marginally. U.S. payrolls expanded by 43,000 jobs in April, although the previous month's gain was revised to estimate a loss of 21,000 jobs;
- A modest increase in the Conference Board's March index of leading indicators suggests the recovery should remain on track through early fall;
- Personal income grew a healthy 0.4 percent in March;
- The Institute of Supply Management index (formerly the NAPM) fell slightly in April, but remained above the critical 50 percent level for the third consecutive month;
- Consumer confidence slipped in April by 2 points to 108.8, driven down by the indicator which measures sentiment about current economic conditions; and
- At its meeting on May 7, the Federal Reserve left interest rates unchanged, noting that information available since the last meeting "confirms that economic activity has been receiving considerable upward impetus from a marked swing in inventory investment. Nonetheless, the degree of the strengthening in final demand over coming quarters, an essential element in sustained economic expansion, is still uncertain."

The Virginia Economy

In March 2002, employment in Virginia declined by 1.4 percent from March of last year. The unemployment rate fell 0.3 percent in March to 4.0 percent, however, and remains well below the national jobless rate of 5.7 percent.

The Virginia Leading Index fell in February after four straight months of growth. Nevertheless, the general trend continues to point toward economic recovery.

April Revenue Collections

April's weak net collections can be attributed primarily to faster processing of individual income tax refunds, although sluggishness in withholding collections also played a part. The sluggish overall growth leaves revenues below the rate required to meet the revenue estimate.

Individual Income Tax Withholding (58% of general fund revenues): Withholding collections increased 2.0 percent over last April, despite an additional deposit day in April this year. Year-to-date growth of 2.6 percent is slightly behind the official estimate of 3.5 percent.

Individual Income Tax Refunds: The total amount of refunds issued in April was \$289.2 million – about \$118.8 million above last April's total. The average refund amount is up 14 percent, about twice as large as the increase on which the revenue estimate was based.

In April, the Department of Taxation issued over 651,000 refunds -- 165,000 more than April of last year. Error rates on returns filed through April are currently running at 7.5 percent, one-half of last year's rate for the same period. Since the beginning of the filing season in January, the Department has issued over 1.9 million refunds – a 436,000 increase over last year.

Individual Income Tax Nonwithholding (14% of general fund revenues): Nonwithholding receipts declined by 3.0 percent in April compared with April of last year. Most of the activity this month represents the early receipt of 2001 individual income tax returns, and the first estimated payment for 2002 tax liabilities. Both were due May 1. April's tax due payments dropped by 14.9 percent. However, estimated payments for tax year 2002 were up 24.2 percent.

Virginia's unique May 1 due date for both tax due and estimated payments makes any analysis premature at this time. A clearer picture will be available by the end of May, when all payments will have been processed. To date, close to 62 percent of the fiscal year's estimated revenues have been received, leaving about \$592.5 million to be collected in the next two months.

Sales Tax (21% of general fund revenues): Sales tax collections for April increased by 2.3 percent. On a year-to-date basis, collections are down 0.1 percent – behind the annual estimate of 0.1 percent growth required by the current forecast (excluding the acceleration of sales tax collections expected in June).

Corporate Income Tax (2.7% of general fund revenues): In April, corporations made their first estimated payment for tax year 2002, along with either a final or extension return for tax year 2001. Collections of corporate income tax were 14.4 percent below April of last year. The year-to-date decline of 20.7 percent slightly trails the estimate of an 18.7 percent decrease.

Insurance Company Premiums (2.6% of general fund revenues): This month's receipts, which represent the first estimated payment on calendar year 2002 premium sales, were 4.7 percent above last April's collections. Year-to-date growth of 10.2 percent is tracking 2.8 percentage points ahead of the annual estimate of 7.4 percent growth.

Other Revenue Sources

The following list provides growth rates in collections of other tax revenues.

	<u>Year to Date</u>	<u>Required to Meet Estimate</u>
ABC Taxes (1.1% GF revenues)	3.2%	2.3%
Interest Income (1.0% GF revenues)	-36.5%	-15.9%
Public Service Corporations (.9% GF revenues)	-12.2%	2.2%

All Other Revenue. Revenue from all other sources increased in April by \$2.9 million over last year. On a year-to-date basis, collections were 10.2 percent above the same period last year, mainly due to collections of taxes on wills, suits, deeds, and contract fees.

Lottery Revenues. With The Big Game jackpot rolling to \$331 million, April was the highest sales and profit month ever for the Lottery. Lottery net income was up \$47 million -- \$17.8 million more than estimated. On a year-to-date

basis, Lottery net income is up 14.0 percent, well above the revised estimate of -0.1 percent.

Summary

Growth in general fund revenues has been negative for five consecutive months, and total year-to-date collections, including Tobacco Settlement revenues, are 3.6 percent below collections for the same period last year. To achieve the fiscal year 2002 forecast, revenue collections for May and June must total \$2,390.8 million (excluding the June sales tax acceleration program).

Although the decline in April revenues was driven by the large number of individual income tax refunds, this refund activity represents real dollars that are no longer available this fiscal year. The volume of refunds processed to date and the average refund size to date exceeds the amounts on which the refund forecast was based.

Payroll withholding needs to gain momentum in the final two months of the fiscal year to reach its forecast. Finally, details on collections of individual estimated and final payments will become clearer as May proceeds.