



# COMMONWEALTH of VIRGINIA

Office of the Governor

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Secretary of Finance

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June 13, 2003

## MEMORANDUM

TO: The Honorable Mark R. Warner

THROUGH: The Honorable William H. Leighty

FROM: John M. Bennett

SUBJECT: May Revenue Data

Revenue collections fell 6.5 percent in May. Year-to-date collections now stand at 1.3 percent above collections for the same period last year - 0.1 percent above the level needed to meet the fiscal year 2003 revenue forecast.

A large portion of the decline in May revenues is attributable to processing changes for nonwithholding collections, which shifted into April a substantial portion of the nonwithholding revenue that would normally have been collected in May.

Although most major sources saw solid growth in May, collections of withholding and sales taxes - which comprise more than 80 percent of revenues - continue to lag the annual estimate. Strong collections in minor sources continue to offset the shortfall in these sources.

### **National Economic Indicators**

The national economy continues to show widespread weakness. However, the recovering stock market and improving consumer confidence suggest that the economic recovery may soon take hold.

- The national labor market remains stalled. Payroll employment fell by 17,000 jobs in May, following a flat April. The unemployment rate rose to 6.1 percent. Job growth is expected to remain weak over the coming months, and most economists expect the unemployment rate to rise higher.

- Initial claims for unemployment rose to 442,000 during the last week of May, a five-week high. The four-week average rose to 430,500. The number of initial claims has consistently exceeded the benchmark 400,000 level since mid-February.

- The manufacturing sector marginally improved in May, but is still contracting. The Institute of Supply Management index rose to 49.4, the first increase since December of last year, but remains below the 50.0 break-even level.

- The Conference Board's index of leading indicators rose 0.1 percent in April, the first increase this year. The index has remained essentially flat over the last year.
- The Conference Board's index of consumer confidence rose in May. Consumers' expectations for the future improved, while their assessment of the current situation dropped.
- After eight consecutive monthly gains, personal income growth was flat in April. Wage and salary income declined for the first time in nine months. Consumer spending dropped 0.1 percent for the month, largely due to falling energy prices. Adjusting for energy prices, real spending grew 0.1 percent.
- Real GDP growth was revised upward to 1.9 percent in the first quarter -- very weak growth for a recovery.
- Federal Reserve Chairman Alan Greenspan has said that although "the acceleration has not yet begun," the gains in the stock market and other indicators "are suggestive of a fairly marked turnaround."

### **Virginia Economy**

In Virginia, payroll employment grew 0.1 percent in April from April of last year. Job growth in the Commonwealth has been essentially flat over the fiscal year. Northern Virginia has posted four consecutive months of modest job gains, with 0.3 percent growth in April.

The Virginia Leading Index fell by 1.0 percent in April -- its third consecutive decline. Weakness in all components of the index suggests economic growth will remain slow in the coming months. Initial claims for unemployment rose almost 11 percent in April, indicating that the labor market in Virginia remains weak. Both auto registrations and building permits declined.

### **May Revenue Collections**

Revenue collections fell 6.5 percent in May. On a year-to-date basis, total revenues are up 1.3 percent through May, tracking very close to the required annual estimate of 1.2 percent growth.

**Individual Income Tax Withholding (62% of general fund revenues):** Collections in withholding fell 1.1 percent below May of last year. Year-to-date withholding growth through May is 2.1 percent - below the annual estimate of 2.7 percent growth. It is highly unlikely that withholding collections will meet the forecast. Until basic labor market conditions improve, withholding collections will remain sluggish.

**Individual Income Tax Refunds:** Refunds this month totaled \$116.1 million, compared with \$127.4 million paid in May of last year. Through May, refunds have exceeded the fiscal year 2003 projection by about \$87 million.

During the current filing season, close to 2.3 million refunds have been issued -- about 36,000 more than the same period last year. The average refund amount is up about 9.0 percent. The Department of Taxation has issued 93 percent of all refunds within 12 days and 98 percent within 30 days. This increased efficiency in the refund process has shifted many returns normally issued in July and August into the current fiscal year.

**Individual Income Tax Nonwithholding (12% of general fund revenues):** Final payments for tax year 2002 are due on May 1st, along with the first estimated payment for tax year 2003. May is therefore normally a significant month for nonwithholding collections. This year, as the result of streamlined processing, the bulk of nonwithholding payments were collected in April. Nonwithholding collections therefore fell 29.0 percent in May, following a 29.0 percent increase in April.

Taken together, nonwithholding payments in April and May were 2.8 percent below the same two months last year. Through May, year-to-date collections are 3.7 percent below collections for the same period last year - ahead of the forecast of a 13.3 percent decline.

**Sales Tax (22% of general fund revenues):** Collections of sales and use tax remained sluggish in May, increasing 1.4 percent above last May. Adjusting for accelerated sales tax payments, year-to-date collections in this source have increased 1.1 percent through May - well below the forecast of 2.7 percent growth. To attain the annual estimate, June sales tax collections must grow 5.0 percent from last year - an unlikely event. A shortfall is therefore expected in this source.

### Other Revenue Sources

The following list provides data on May collections of other key taxes:

	Year-to-Date	Required to Meet Estimate
Corporate Income Tax (3% GF revenues)	17.2%	3.8%
Insurance Premiums Tax (3% GF revenues)	13.4%	6.5%
ABC Taxes (1.1% GF revenues)	2.4%	0.2%
Public Service Corporations (0.9% GF revenues)	20.6%	11.5%
Interest Income (0.7% GF revenues)	-20.0%	-28.3%

**All Other Revenue.** Revenue from all other sources was up 32.0 percent in May -- \$55.5 million compared with \$42.0 million in May of last year. Continued strength in collections of wills, suits, deeds and contract fees (primarily recordation taxes) accounted for most of the growth. On a year-to-date basis, collections of all other revenue were 24.1 percent above the same period last year - ahead of the annual forecast of 19.6 percent growth.

**Lottery Revenues.** In May, Lottery net income declined 0.3 percent over last year. Low Lotto South sales were offset by increased ticket sales for Mega Millions. On a year-to-date basis, growth of 0.4 percent is slightly above the amount needed to meet the current revenue estimate of a 1.1 percent decline.

### Summary

Revenue collections fell 6.5 percent in May. With one month of the fiscal year remaining, total general fund revenue collections are tracking very close to the forecast.

June is another billion-dollar revenue month, with major collections in individual and corporate estimated payments, estimated payments for insurance premiums, corporate franchise fees, and accelerated sales tax collections, along with regular monthly collections in other sources. Total general fund revenues in June must exceed \$1.26 billion in order to meet the fiscal year 2003 forecast. Withholding and sales taxes - which comprise more than 80 percent of general fund revenues - continue to lag their respective estimates and shortfalls are expected in these sources. Continued strength in minor sources will be needed to offset these declines.