



COMMONWEALTH of VIRGINIA
Office of the Governor

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November 12, 2008

MEMORANDUM

TO: The Honorable Timothy M. Kaine

THROUGH: The Honorable Wayne M. Turnage

FROM: Richard D. Brown 

SUBJECT: October Revenue Data

This month's revenue report reflects the revised official revenue forecast released on October 9. The revised revenue forecast reduces total general fund revenues and transfers for the 2008-2010 biennium by \$2.5 billion (7.4 percent) from the previous official forecast released in February and incorporated in Chapter 879. Revenues are now expected to decline 4.0 percent in fiscal year 2009 and increase 3.6 percent in fiscal year 2010.

October is traditionally not a significant month for revenue collections. Normal monthly collections are due in withholding, sales taxes, and most minor sources. Estimated payments are also filed in October for corporations that use a February through January fiscal year, which are mainly retailers.

The collection of general fund revenues continues to reflect the current economic environment. Total revenues declined 1.0 percent in October -- the third consecutive monthly decline -- with slightly stronger growth in withholding payments offset by larger than expected declines in sales taxes, corporate income taxes, and recordation taxes. On a year-to-date basis, revenues fell 3.5 percent through October, slightly ahead of the revised annual estimate.

National Economic Indicators

Recent indicators continue to indicate that the U.S. economy is likely in recession. Tight credit, a declining labor market, and a slowing global economy will continue to hamper economic growth in the short term.

- Real GDP fell 0.3 percent in the third quarter according to the advance estimate. Consumer spending declined by the largest amount since 1980. Business spending on equipment and software fell for the third straight quarter, the first time that has happened since 2001.
- The labor market contracted for the tenth consecutive month in October, with payroll employment falling by 240,000 jobs. In addition, losses for the two previous months were revised upward by 179,000. In a separate report, the unemployment rate rose from 6.1 to 6.5 percent, above the peak in the most recent downturn.
- Initial claims for unemployment fell by 4,000 to 481,000 during the week ending November 1. The four-week moving average was flat at 477,000, consistent with the trend in a recession.
- Falling energy prices and weakening consumer demand are factors in a decline in consumer prices. Specifically, the consumer price index was flat in September, while the year-ago percentage change was 4.9 percent, down from 5.4 percent in August. Core CPI increased by 0.1 percent and is up 2.5 percent from a year ago, the same rate as the last two months.
- The manufacturing sector contracted for the third consecutive month in October. The Institute of Supply Management index fell from 43.5 to 38.9, its lowest level since the early 1980s. Tight credit and weak demand are likely to impact this sector in the months to come.
- The Conference Board's index of consumer confidence fell in October from 61.4 to 38.0, the lowest level on record back to 1969. Both the current conditions and expectations components fell.
- The Conference Board's index of leading indicators rose 0.3 percent to 100.6 in September. Despite the increase, a larger downward revision to the August report weakened the trend -- leading indicators over the past three months contracted at their fastest rate since 1990.
- The Federal Reserve lowered the federal funds rate by 50 basis points to 1.00 percent on October 29, following the 50-basis point reduction on October 8.

Virginia Economy

In Virginia, payroll employment grew 0.5 percent in September. Northern Virginia posted job growth of 1.0 percent in September. The number of jobs grew by 2.2 percent in Hampton Roads and 0.3 percent in Richmond-Petersburg. The statewide unemployment rate fell from 4.6 percent to 4.2 percent in September.

October Revenue Collections

October is traditionally not a significant month for revenue collections. Normal monthly collections are due in withholding, sales taxes, and most minor sources. Estimated payments are also filed in October for corporations that use a February through January fiscal year, which are mainly retailers.

Total revenues declined 1.0 percent in October -- the third consecutive monthly decline -- with slightly stronger growth in withholding payments offset by larger than expected declines in sales taxes, corporate income taxes, and recordation taxes. On a year-to-date basis, revenues fell 3.5 percent through October, slightly ahead of the revised annual estimate of a 4.0 percent decline. The last time revenue collections contracted for three consecutive months in the first part of a fiscal year was the July through September quarter in fiscal year 1990.

Net Individual Income Tax (67% of general fund revenues): For the first four months of the fiscal year, net individual income tax increased 4.1 percent from the same period last year, ahead of the annual estimate of a 0.4 percent decline. Performance in each component of individual income tax is as follows:

Individual Income Tax Withholding (61% of general fund revenues): Collections of payroll withholding taxes grew 5.6 percent in October. Year-to-date withholding growth is 5.5 percent, ahead of the projected annual growth rate of 3.3 percent. Year-to-date growth is slightly inflated by two extra deposit days in September.

Individual Income Tax Nonwithholding (17% of general fund revenues): October is typically a slow month for nonwithholding collections. Year to date, collections through October were \$496.2 million compared with \$495.4 million in the same period last year, growing 0.2 percent compared with the annual estimate of a 7.9 percent decline.

Individual Income Tax Refunds: Through October, \$174.9 million has been refunded compared with \$148.3 million during the same period last year. The growth is primarily attributable to refunds related to overpayments made as the economy has slowed.

Sales Tax (20% of general fund revenues): Collections of sales and use taxes, reflecting September sales, fell 4.2 percent in October. On a year-to-date basis, collections have fallen 2.6 percent, trailing the annual estimate of 0.0 percent growth.

Corporate Income Tax (5% of general fund revenues): October corporate income tax collections include estimated payments from corporations with a February through January fiscal year, including many retailers. Collections in corporate income tax fell 33.1 percent in October. On a year-to-date basis, collections in this source have fallen 14.8 percent from the same period last year, close to expectations.

Wills, Suits, Deeds, Contracts (2% of general fund revenues): Collections of wills, suits, deeds, and contracts – mainly recordation tax collections – fell 38.0 percent in the month of October. Year-to-date, collections in this source are down 32.6 percent, trailing the revised forecast of a 23.9 percent decline. Adjusted for the transfer of 3 cents of the 25 cents per \$100 recordation tax to the Commonwealth Transportation Fund, year-to-date collections are down 25.3 percent.

Other Revenue Sources

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

	<u>Year-to-Date</u>	<u>Annual Estimate</u>
Insurance Premiums (2% GF revenues)*	-100.0%	-35.1%
Interest Income (1% GF revenues)	-26.5%	-38.7%
ABC Taxes (1% GF revenues)	-4.2%	3.6%

**Monthly collections of insurance premiums are being transferred to the Transportation Trust Fund per HB 3202 until the required amount of \$132.3 million has been transferred.*

All Other Revenue (3% of general fund revenues): Receipts in All Other Revenue fell 48.2 percent in October – \$33.2 million compared with \$64.1 million in October of last year. Most of the decline was due to a steep decline in the estate tax. The General Assembly repealed the tax effective July 1, 2007, and estates from deaths prior to that date had up to nine months to file. For the fiscal year-to-date, collections of All Other Revenue fell 33.0 percent from the same period in fiscal year 2008, lagging the annual estimate of a 27.3 percent decline.

Lottery Revenues: Net income for October 2008 totaled \$34.3 million, a decline of 6.9 percent from October 2007. Year-to-date, net income is down 9.4 percent (\$14.8 million), trailing the annual estimate of a 5.5 percent decline. The prize expense rate

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(prizes as a percentage of sales) was 56.4 percent on a year-to-date basis, compared to 55.0 percent last year, accounting for over \$6.0 million of the decline in net income.

Summary

While October is not a significant month for revenue collections, it is the first month that collections are compared to the revised official revenue forecast released on October 9. Total revenues declined 1.0 percent in October -- the third consecutive monthly decline -- with slightly stronger growth in withholding payments offset by larger than expected declines in sales taxes, corporate income taxes, and recordation taxes. On a year-to-date basis, revenues declined 3.5 percent through October, slightly ahead of the revised annual estimate.

A meeting of the Governor's Advisory Board of Economists (GABE) is scheduled for November 14, 2008 to assess any changes in the economy since their meeting in September. This will be followed by a meeting on December 2, 2008 of the Governor's Advisory Council on Revenue Estimates which will evaluate both the GABE recommendations and revenue collections through November.