



COMMONWEALTH of VIRGINIA
Office of the Governor

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October 15, 2008

MEMORANDUM

TO: The Honorable Timothy M. Kaine

THROUGH: The Honorable Wayne M. Turnage

FROM: Richard D. Brown 

SUBJECT: September Revenue Data

September completes the first quarter of the fiscal year and is a significant month for revenue collections. Estimated payments from individuals, corporations, and insurance premiums are all due in September, along with regular monthly collections in withholding, sales, and other sources.

The effects of the financial turmoil that began with Fannie Mae and Freddie Mac early in the month are evident in September collections. Monthly total general fund revenue collections fell 7.4 percent in September, despite two more deposit days than September of last year. Although the extra deposit days boosted withholding collections, collections of sales tax declined by 3.9 percent and corporate collections dropped 10.9 percent. On a year-to-date basis, total revenues declined 4.2 percent in the first quarter of the fiscal year, below the annual forecast of 2.0 percent growth.

National Economic Indicators

Most recent indicators suggest the short-term outlook for the national economy remains bleak, as the financial crisis appears to have dragged the economy into recession.

- The labor market contracted for the ninth consecutive month in September, with payroll employment falling by 159,000 jobs. The economy has shed 760,000 jobs since December. Education and healthcare is the only major sector that continues to expand. In a separate report, the unemployment rate was unchanged at 6.1 percent.

- Initial claims for unemployment fell by 20,000 to 478,000 during the week ending October 4, as the impact from hurricanes Gustav and Ike eased. The four-week moving average rose slightly from 474,000 to 483,000.
- Although prices remain elevated, they appear to have peaked in July. After increasing 0.8 percent in July, the Consumer Price Index (CPI) fell 0.1 percent in August for an annual growth of 5.4 percent. Core inflation, excluding food and energy, rose by 0.2 percent in August, with annual growth unchanged at 2.5 percent.
- The manufacturing sector contracted in September. The Institute of Supply Management index fell from 49.9 to 43.5, its lowest level since 2001. Although demand for U.S. exports has so far limited the severity of the downturn in manufacturing, the outlook for global economies is worsening.
- The Conference Board's index of leading indicators fell 0.5 percent to 100.8 in August, the third decline in the past four months. The weakness in the leading index suggests that the national economy will continue to weaken.
- The Conference Board's index of consumer confidence rose modestly in September from 58.5 to 59.8. A fall in the current situation component was offset by a strong increase in the expectations component. Since many responses to the survey were received before the recent financial turmoil, it is likely to be revised downward in future reports.
- To deal with the financial crisis, central banks around the globe have lowered interest rates. In addition to the federal government bailout, the Federal Reserve lowered the federal funds rate by 50 basis points to 1.50 percent on October 8.

Virginia Economy

In Virginia, payroll employment grew 0.5 percent in August. Northern Virginia posted job growth of 1.1 percent in August. Jobs grew by 2.2 percent in Hampton Roads and 0.5 percent in Richmond-Petersburg. The unemployment rate rose slightly from 4.5 percent to 4.6 percent in August.

The Virginia Leading Index grew 0.3 percent in July, only the third increase in the last twelve months. All three components contributed to the increase. However, on a year-over-year basis, auto registrations and building permits are significantly below last July's levels and initial claims for unemployment are much higher. The leading index increased in five of the eleven metro areas in July. The indices increased in Harrisonburg, Charlottesville, Winchester, Blacksburg, and Bristol, and contracted in all other MSAs.

September Revenue Collections

Monthly total general fund revenue collections fell 7.4 percent in September, despite two more deposit days than September of last year. Although the extra deposit days boosted withholding collections, collections of sales tax fell by 3.9 percent and corporate collections dropped 10.9 percent. On a year-to-date basis, total revenues declined 4.2 percent in the first quarter of the fiscal year, below the annual forecast of 2.0 percent growth. Adjusted for the repeal of the estate tax and transfers to transportation from insurance and recordation per HB 3202, first quarter collections declined 0.4 percent, only the third time on record (along with fiscal year 1990 and fiscal year 2002) that first quarter collections have declined.

Net Individual Income Tax (67% of general fund revenues): For the first quarter of the fiscal year, net individual income tax increased 3.4 percent from the same period last year, trailing the annual estimate of 6.5 percent. Performance in each component of individual income tax is as follows:

Individual Income Tax Withholding (59% of general fund revenues): With two additional deposit days, collections of payroll withholding taxes grew 6.2 percent in September. Year-to-date withholding growth is 5.5 percent, lagging the projected annual growth rate of 6.4 percent.

Individual Income Tax Nonwithholding (19% of general fund revenues): The first estimated payment in fiscal year 2009 was due in September. Year to date, collections through September were \$406.5 million compared with \$394.1 million in the same period last year, growing 3.1 percent compared with the annual estimate of 6.9 percent.

Individual Income Tax Refunds: Through September, \$127.2 million has been refunded compared with \$83.6 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 August sales, fell 3.9 percent in September. On a year-to-date basis, collections have fallen 2.0 percent, far behind the annual estimate of 4.9 percent growth. Large payments related to housing continue to decline from prior year levels.

Corporate Income Tax (4% of general fund revenues): The first estimated payment for fiscal year 2009 was due in September. Collections in corporate income tax fell 10.9 percent in September. On a year-to-date basis, collections in this source have fallen 12.1 percent from the first quarter of last year, close to expectations. Payments from large corporations in the finance, housing, and investment sectors fell over 50% from the first quarter of last year.

Wills, Suits, Deeds, Contracts (2% of general fund revenues): Collections of wills, suits, deeds, and contracts – mainly recordation tax collections – fell 22.4 percent in the month of September, and are down 30.9 percent on a year-to-date basis. 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 23.5 percent.

Other Revenue Sources

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

	<u>Year-to-Date</u>	<u>Annual Estimate</u>
Insurance Premiums (2% GF revenues)*	-100.0%	-25.7%
Interest Income (1% GF revenues)	-29.3%	-35.5%
ABC Taxes (1% GF revenues)	-7.2%	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 booked.*

All Other Revenue (3% of general fund revenues): Receipts in All Other Revenue fell 24.2 percent in September – \$27.8 million compared with \$36.7 million in September 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 24.5 percent from the same period in fiscal year 2008, ahead of the annual estimate of a 26.7 percent decline.

Lottery Revenues: Net income for September 2008 totaled \$34.6 million, a decline of 5.3 percent from September 2007. Year-to-date, net income is down 10.2 percent, trailing the annual estimate of 1.3 percent growth. However, the first quarter of last year was significantly enhanced by the growth of the Mega Millions jackpot to \$330 million.

Summary

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In light of current revenue performance, the Governor presented an official revision to the revenue estimates for fiscal year 2009 and 2010 on October 9. This revised revenue forecast reduces total general fund revenues and transfers for the 2008-2010 biennium by \$2.5 billion (7.4 percent) from the official forecast. Revenues are now expected to decline 4.0 percent in fiscal year 2009. The projected decline for fiscal year 2009 represents the second worst performance on record (outside of fiscal year 2002) and a major revision from the 2.0 percent growth projected in the official forecast. Total general fund revenues are projected to increase a sluggish 3.6 percent in fiscal year 2010. These official revisions will be incorporated into next month's revenue report covering the revenue collections for October.