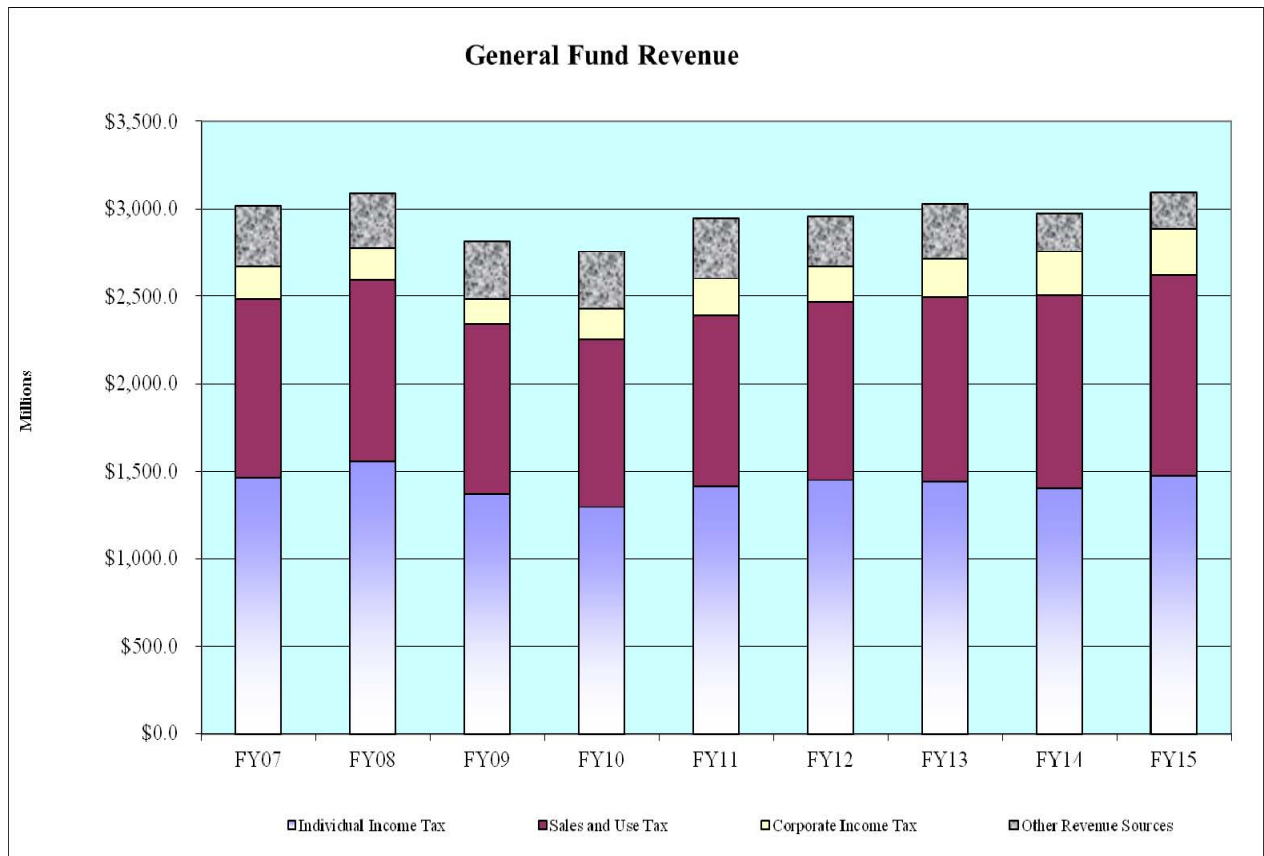


# REPORT OF THE MAINE STATE REVENUE FORECASTING COMMITTEE

December 2011



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## Introduction

The Revenue Forecasting Committee (RFC) met on November 18, 2011 to review and update the current revenue forecast to comply with the statutory reporting date of December 1<sup>st</sup>. The RFC has revised its revenue projections through the fiscal year ending June 30, 2015 for the General Fund, Highway Fund, Fund for a Healthy Maine and Medicaid Dedicated Revenue Taxes.

## Economic Forecast

This update of the revenue forecast began with an updated economic forecast statutorily due by November 1<sup>st</sup>. That economic forecast was developed by the Consensus Economic Forecasting Commission (CEFC) at its meeting on October 24, 2011. The CEFC reviewed and discussed various economic scenarios and again expressed concern over the lack of job growth and the likelihood that certain employment measures would be revised downward from projections. At the date of the meeting the European debt crisis was focused on Greece. Since then the attention has been refocused on Italy. With few signs of significant economic progress in the near term, the CEFC agreed with and adopted most of the macroeconomic assumptions favored by IHS Global Insights' baseline forecast updated in October 2011. The revised forecast reduced assumptions for employment and personal income. A copy of the November 2011 report of the CEFC and other economic information providing the basis for this revenue forecast is included in Appendix E.

## Summary of Revenue Forecast

The economic variables in the CEFC forecast were used as inputs for Maine Revenue Services' tax models to help project revenue from the major taxes. Data related to non-tax revenue lines were provided by a number of different state agencies and reviewed by staff in the Office of Fiscal and Program Review and the Bureau of the Budget to come up with consensus recommendations. The RFC reviewed Maine Revenue Services' and other staff recommendations at its meeting on November 18<sup>th</sup> and made some adjustments to those recommendations. The following tables and narratives highlight the final changes to each of the major funds and revenue sources accepted by the RFC as its December 2011 update to the revenue forecast. More detail on each of the funds and revenue sources is provided in the various appendices.

### General Fund Summary

	<b>FY11 Actual</b>	<b>FY12</b>	<b>FY13</b>	<b>FY14</b>	<b>FY15</b>
Current Forecast	\$2,944,956,756	\$2,945,628,851	\$3,039,933,432	\$3,020,369,958	\$3,140,244,893
Annual % Growth	6.9%	0.0%	3.2%	-0.6%	4.0%
Net Increase (Decrease)		\$10,645,254	(\$9,643,359)	(\$46,225,103)	(\$45,607,018)
Revised Forecast	\$2,944,956,756	\$2,956,274,105	\$3,030,290,073	\$2,974,144,855	\$3,094,637,875
Annual % Growth	6.9%	0.4%	2.5%	-1.9%	4.1%

General Fund revenue estimates (also refer to Appendix A and other background materials in Appendix F and Appendix G) are being revised upward by \$10.6 million in FY12 and then downward by \$9.6 million in FY13, resulting in a net increase of budgeted revenue for the 2012-2013 biennium of \$1.0 million. The effects of the technical changes as part of targeting the tax models to updated tax data and the better short-term corporate profit growth in the economic forecast offset the slower Personal Income

growth assumptions in FY12. However, beginning in FY13 the effect of slower growth assumptions in the economic forecast outweigh these positive factors and the downward revisions to budgeted General Fund revenue for the 2014-2015 biennium total \$46.2 million in FY14 and \$45.6 million in FY15.

Sales and Use Tax, which for the purposes of the tax models is combined with the Service Provider Tax, is forecast upward for three of the four years of the forecast period. The revisions are the result of the net effect of the changes in several economic assumptions used in the sales and excise tax model, primarily the declines in the savings rate, energy price index changes and aggregate Personal Income growth. The tax model was also targeted to account for growth in taxable sales in the Business Operating sector. The combined net changes for the forecast of these 2 major tax lines are an increase of \$3.3 million in FY12, a decrease of \$2.8 million in FY13, an increase of \$0.5 million in FY14 and an increase of \$9.6 in FY15. Based on recent experience, the RFC is making an ongoing annual adjustment shifting \$3.0 million from the Service Provider Tax portion to the Sales and Use Tax category of the combined taxable sales forecast. **This category is subject to the greatest downside risk, if oil prices affecting heating oil and motor fuel prices do not recede from the current high levels.**

Individual Income Tax estimates are projected upward in FY12 (\$5.4 million) and downward by a similar amount in FY13 (\$5.4 million) before the slower jobs and income growth projections of the economic forecast turn the revisions significantly negative. Individual Income Tax revenue estimates are reduced by \$40.5 million in FY14 and \$46.0 million in FY15. Initially, the effect of adjusting the distribution of taxable income to upper income tax brackets based on recent tax experience increased the starting base high enough to produce a net positive effect in FY12.

Corporate Income Tax revenue is the largest positive influence on the forecast. With many businesses having worked hard to find ways to cut costs, any improvements in income can flow directly through to the bottom line. The significant improvement in the corporate profit growth assumptions in calendar years 2011 and 2012 raised projections by \$20.2 million in FY12 and \$18.7 million in FY13. The growth assumptions in 2013 and beyond are below the previous projections, moderating the increases in the next biennium to \$8.7 million in FY14 and \$4.3 million in FY15.

The net changes to the income and sales tax categories summarized above that affect revenue sharing transfers will increase the amount transferred for municipal revenue sharing in FY12 by \$2.2 million and by \$0.7 million in FY13, but will decrease \$1.3 million in FY14 and \$1.6 million in FY15. After netting out the revenue sharing transfers, these major tax lines result in increased revenue projections of \$36.6 million for the 2012-2013 biennium, but decreased revenue projections of \$60.4 million for the 2014-2015 biennium.

For the other categories, the adjustments were much more consistently negative and virtually eliminated the net increase from the sales and income taxes in the 2012-2013 biennium. Some of these other adjustments include the following:

- \$7.0 million related to the reduction in value of traditional telecommunications property that affects the State's Telecommunications Personal Property Tax;
- \$8.2 million in Estate Tax collections;
- \$3.0 million in cigarette and tobacco products tax revenue;
- \$3.5 million reduction in fine revenue, largely due to budgetary effects on enforcement;
- \$3.8 million reduction of STA-CAP revenue, cost allocation revenue, that has been affected by reduced expenditures, particularly for federal funds and the Highway Fund;

- \$2.3 million in revenue from hunting and fishing licenses, based on a more thorough analysis of sales trends and historical data;
- \$2.4 million related to a Department of Health and Human Services (DHHS) policy decision related to Medicaid Targeted Case Management billing for services provided by DHHS;
- \$2.0 million from Circuitbreaker (Tax and Rent Refund) program from some recent tax appellate decisions on rents;
- \$1.0 million from lower projected General Fund expenditures subject to reimbursement from the Unorganized Territory Property Tax; and
- \$0.8 million from Casino/Racino revenue (despite the addition of table games in Bangor, recent performance has fallen below projections and growth assumptions have been lowered).

### Highway Fund Summary

	FY11 Actual	FY12	FY13	FY14	FY15
Current Forecast	\$311,351,155	\$316,364,800	\$318,338,584	\$319,458,744	\$319,579,911
Annual % Growth	0.1%	1.6%	0.6%	0.4%	0.0%
Net Increase (Decrease)		\$1,569,931	\$537,166	\$1,676,069	\$3,615,983
Revised Forecast	\$311,351,155	\$317,934,731	\$318,875,750	\$321,134,813	\$323,195,894
Annual % Growth	0.1%	2.1%	0.3%	0.7%	0.6%

Highway Fund revenue estimates (also refer to Appendix B and the RFC's web page) are revised upward by \$1.6 million in FY12, \$0.5 million in FY13, \$1.7 million in FY14 and \$3.6 million in FY15. Economic assumptions related to aggregate Personal Income growth, Consumer Price Index changes and changes in oil and energy prices interacted to produce modest net changes in the projections. Fuel Taxes are being revised upward in this forecast largely based on the underlying economic assumption of declining fuel prices. Without that price decline, the model would have projected Fuel Taxes lower in each year of the forecast. Within the Fuel Taxes category, Gasoline Tax collections were under budget through October; gasoline prices have retreated recently, demand has not yet shown much of a recovery or reaction to the recent declines in gasoline prices. This fuel price assumption and its effect on this revenue forecast will need to be watched carefully. The risk to this forecast is very high, if demand does not react to the recent gasoline price reductions or if record high heating oil prices interfere with the recovery in fuel consumption.

The increases in estimates for the Fuel Taxes category were partially offset by some reductions of estimates for fine revenue and interest earnings.

### Fund for a Healthy Maine Summary

	FY11 Actual	FY12	FY13	FY14	FY15
Current Forecast	\$54,386,707	\$53,623,250	\$53,667,932	\$60,383,598	\$60,052,787
Annual % Growth	-5.5%	-1.4%	0.1%	12.5%	-0.5%
Net Increase (Decrease)		\$904,888	\$311,702	(\$6,108,865)	(\$6,187,485)
Revised Forecast	\$54,386,707	\$54,528,138	\$53,979,634	\$54,274,733	\$53,865,302
Annual % Growth	-5.5%	0.3%	-1.0%	0.5%	-0.8%

For the Fund for a Healthy Maine (FHM), updated projections by the National Association of Attorneys General (NAAG) for tobacco settlement payments increased projections for the current biennium by \$1.2 million, but uncertainty about the timing of the final resolution of litigation surrounding the non-

participating manufacturer's (NPM) adjustment results in the RFC delaying the projected recovery of disputed payments until outside of the forecast period, resulting in a reduction of 2014-2015 revenue projections of \$11.8 million. The impact of lower growth assumptions from the Casino/Racino revenue and lower interest rate assumptions for interest earnings further reduced revenue estimates by \$0.5 million for the next biennium to a total \$12.3 million for the FHM.

### **Medicaid/MaineCare Dedicated Revenue Taxes Summary**

	<b>FY11 Actual</b>	<b>FY12</b>	<b>FY13</b>	<b>FY14</b>	<b>FY15</b>
Current Forecast	\$148,021,777	\$153,594,346	\$154,373,049	\$154,373,049	\$154,373,049
Annual % Growth	5.7%	3.8%	0.5%	0.0%	0.0%
Net Increase (Decrease)		(\$1,747,652)	\$0	\$0	\$0
Revised Forecast	\$148,021,777	\$151,846,694	\$154,373,049	\$154,373,049	\$154,373,049
Annual % Growth	5.7%	2.6%	1.7%	0.0%	0.0%

Medicaid/MaineCare Dedicated Revenue Taxes revenue estimates (also refer to Attachment D) are revised downward on a one-time basis in FY 12 by \$1.7 million based on FY11 payments and actual payments to date.

## **Conclusion**

Both the CEFC and the RFC have once again met in a challenging economic environment. While the economy appears to have regained traction after near zero growth in the first half of the calendar year and events in Washington and Europe during the middle of the summer, a number of challenges remain that could result in much different forecasts when both committees meet again in just a few short months. Economic uncertainties that we will monitor closely between now and the next forecasting exercise include:

- the willingness of consumers to further reduce their savings rate to offset rising energy and food prices;
- the timing and magnitude of the recovery in residential housing;
- the willingness of business to hire additional workers and invest in new plant and equipment;
- volatility in the financial markets;
- continued fears of a default by one or more European government; and
- the outcome of the debate in Washington on the future of U.S. fiscal policy.