



April 28, 2011

Update on State General Revenue Collections Third Quarter FY 2011

Tom Kruckemeyer, Director of Fiscal Policy and Chief Economist

After falling by 9.1 percent in Fiscal Year (FY) 2010 overall, Missouri's General Revenue (GR) increased by 6.5 percent for FY 2011 to date, compared to the previous year's collections at the same point. For the most recent quarter of the fiscal year, ending March 31st, general revenues rose 10.9 percent. This marks the fourth consecutive quarter of revenue growth. While the state economic and revenue situation is still uncertain, the sustained revenue growth indicates that the worst of Missouri's revenue decline has likely ended.

However, after experiencing the largest sustained revenue decline since the Great Depression, the state continues to confront an enormous revenue problem. As context, in FY 2010 Missouri's net GR total of \$6.774 billion was *\$1.23 billion less* than the \$8.003 billion collected in FY 2008. Moreover, net GR collections for the quarter ending March 31, 2011 totaled \$1.507 billion – still *below the \$1.52 billion that was collected in the same quarter of FY 2006.*

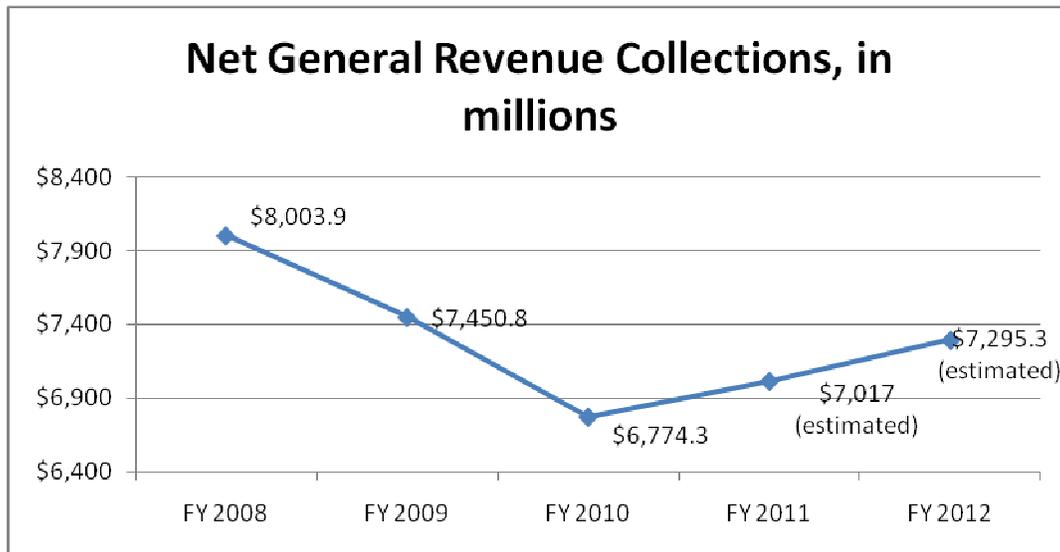
Missouri General Revenue Increases through Third Quarter of Fiscal Year 2011

Missouri's net General Revenue (GR) collections increased by 9.2 percent in March and are up 6.5 percent for FY 2011 to date.

- The increase in March collections was led by a 20.3 percent jump in net individual income tax collections. A 4.7 percent decline in GR Refunds was also a key factor in the strong March collections.
- Gross sales tax collections fell 5.7 percent in March and are up only 0.7 percent for FY 2011 overall. The state will need improvement in this area if strong revenue growth is to be sustained over time.

While four consecutive quarters of positive revenue growth is good news for Missouri, by any historical standard, the Missouri revenue situation remains in the doldrums. With the national economic recovery still proceeding at slow pace, uncertainty with respect to the federal budget and continued international turmoil, the state budget outlook is guarded at best. In addition, revenue losses associated with state tax cuts enacted over the last four years are scheduled to grow.

Figure 1: Net General Revenue Collections, in Millions, FY 2008 - FY 2012



Source: MO Office of Administration

A review of total net GR collections (actual and estimated) over the last five years shows that assuming the state achieves the FY 2012 revenue estimate, **it will still be about \$709 million below the FY 2008 total.**

In recent weeks, the federal budget and the level of the federal budget deficit has been the subject of much debate. It is important to emphasize that if it not were for substantial revenues accruing to the state as a result of the *American Recovery and Reinvestment Act* (approximately \$2.8 billion for fiscal years 2009 through 2012), **Missouri would be facing a budget crisis of much greater magnitude in the current year, FY 2011.**

Detailed Revenue Analysis:

Individual Income Tax (IIT) collections in March 2011 grew 6.0 percent over March 2010. This increase led to a quarterly growth rate of 3.3 percent (relative to the quarter ending March 2010), and a fiscal year to date growth of 3.3 percent. For the quarter, individual income tax withholding rose 3.7 percent relative to this quarter last year. While this is a bit down compared to the prior quarter's 5.0 percent growth, it is still respectable by recent standards. As Figure 1 demonstrates, IIT withholding had declined in five straight quarters prior to turning positive for the four most recent quarters.

Unfortunately, the other key component of IIT had a weak quarter. For the most recent quarter, Declarations/Estimated payments fell 2.1 percent. Mediocre collections coupled with sluggish employment growth leaves the outlook for this tax source guarded.

Figure 2: Missouri Individual Income Tax Collections
Missouri Individual Income Tax Collections Growth Rates Fiscal Years 2007-2010

Year and Quarter	Individual Income Tax Withholding Percent Change versus Same Quarter Previous Year
2007. Quarter 3	5.2%
2007. Quarter 4	8.2%
2008. Quarter 1	7.4%
2008. Quarter 2	2.8%
Total FY 2008	6.0%
2008. Quarter 3	3.2%
2008. Quarter 4	9.0%
2009. Quarter 1	-2.8%
2009. Quarter 2	-5.5%
Total FY 2009	0.9%
2009. Quarter 3	-4.9%
2009. Quarter 4	-11.8%
2010. Quarter 1	-1.8%
2010. Quarter 2	2.5%
Total FY 2010	-4.3%
2010. Quarter 3	1.6%
2010. Quarter 4	5.0%
2011. Quarter 1	3.7%
FY 2011 to date	3.5%

Source: *Missouri Office of Administration*

The following figure more closely examines recent trends in Missouri Wage and Salary growth. The data that now includes each quarter of 2010 shows little growth in Missouri Wage and Salaries. Fortunately, additional modest growth did take place in the 4th quarter of 2010.

Figure 3: Missouri Wage and Salary Growth

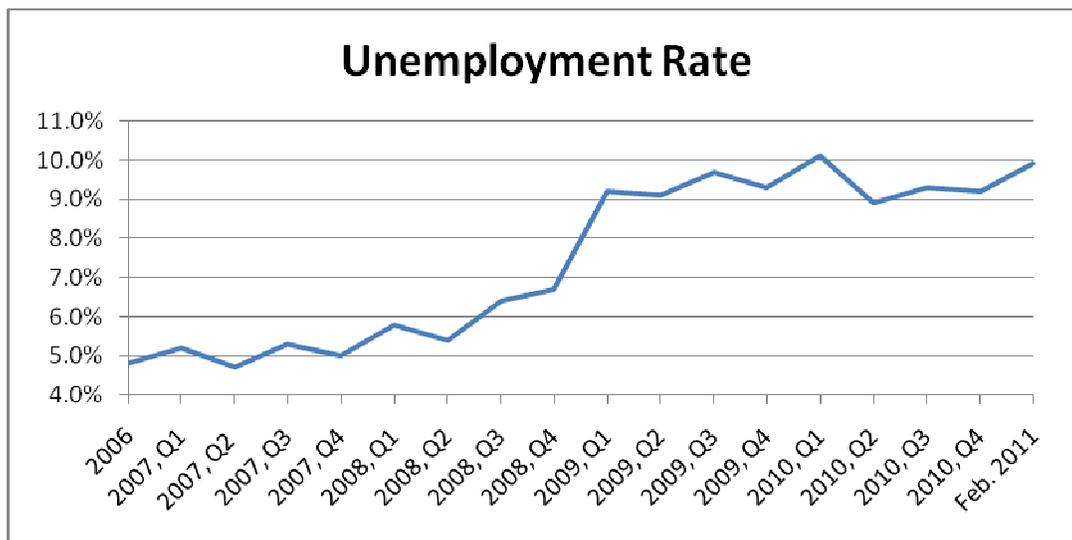
Calendar Year/Quarter	MO Wages & Salaries (in Millions)	Percent Change versus Same Quarter Previous Year
2007. Quarter 1	\$112,656	4.3%
2007. Quarter 2	\$114,428	5.2%
2007. Quarter 3	\$115,200	5.7%
2007. Quarter 4	\$117,317	6.3%
2008. Quarter 1	\$118,175	4.9%
2008. Quarter 2	\$119,630	4.5%

Calendar Year/Quarter	MO Wages & Salaries (in Millions)	Percent Change versus Same Quarter Previous Year
2008. Quarter 3	\$118,441	2.8%
2008. Quarter 4	\$123,757	5.5%
2009. Quarter 1	\$115,572	-2.2%
2009. Quarter 2	\$114,968	-3.9%
2009. Quarter 3	\$114,603	-3.2%
2009. Quarter 4	\$114,074	-7.8%
2010. Quarter 1	\$113,997	-1.4%
2010. Quarter 2	\$114,474	-0.4%
2010. Quarter 3	\$115,773	1.0%
2010. Quarter 4	\$116,781	2.4%

Source: U.S. Dept of Commerce: Bureau of Economic Analysis

In addition, the state's employment situation is still stagnant. While the April-June quarter had an unemployment rate of 8.9 percent, the unemployment rate crept back up during the next two quarters and now stands at 9.9 percent for February of 2011, the latest month available.

Figure 4: Missouri Employment Trends, 2006-2011



Source: U.S. Bureau of Labor Statistics

Overall, IIT has shown fairly solid improvement over the last nine months. Nonetheless, the state will need much more robust job growth in order to return overall individual income tax collections to normal historical standards.

In addition, it should be noted that much of the overall growth in net GR collections is the result of IIT refunds being down 7.0 percent for FY 2011 to date. While an improving economy should lead to a decline in refund growth, it would be prudent to assume that refund growth will return to a more historical rate as the tax filing season continues. A key to any sustained recovery in overall state GR collections will

be a sustained turnaround in this area because IIT accounted for over 65 percent of the Missouri GR fund in FY 2010.

Sales and Use Tax¹ collections fell 5.7 percent in December, which reduced the FY 2011 year-to-date growth rate to 0.7 percent. In recent years, sales tax collection growth has often behaved erratically month to month, making it useful to look at the quarterly growth numbers.

Although sales taxes grew 1.6 percent in the most recent quarter relative to the same quarter last year, this tax has now declined in 11 of the 14 most recent quarters. With the slow growth seen in the last quarter, it is apparent that the overall sales tax situation remains grim. With the national economic recovery proceeding at a sluggish pace, it would reasonable to expect little improvement in this area anytime soon.

Moreover, while state level data on the growth of Internet sales is not available, the U.S. Census reports that national e-commerce retail sales rose from about \$38 billion in the 4th quarter of 2009 to \$44.1 billion in the 4th quarter of 2010, a growth of 16.1 percent.² It is likely that enhanced Internet retail shopping is a factor in the slow growth in Missouri sales tax collections.

Figure 5: Missouri Sales Tax Growth Rates Fiscal Years 2008-2010

Year and Quarter	Regular Sales and Use Tax Percent Change versus Same Quarter Previous Year
2007. Quarter 3	4.0%
2007. Quarter 4	-0.3%
2008. Quarter 1	-2.9%
2008. Quarter 2	-2.0%
Total FY 2008	-0.4%
2008. Quarter 3	-2.3%
2008. Quarter 4	-2.5%
2009. Quarter 1	-5.2%
2009. Quarter 2	-8.3%
Total FY 2009	-4.6%
2009. Quarter 3	-6.7%
2009. Quarter 4	-6.9%
2010. Quarter 1	-6.8%
2010. Quarter 2	1.3%
Total FY 2010	-4.9%
2010. Quarter 3	2.4%
2010. Quarter 4	-1.8%
2011. Quarter 1	1.6%
FY 2011 to date	0.7%

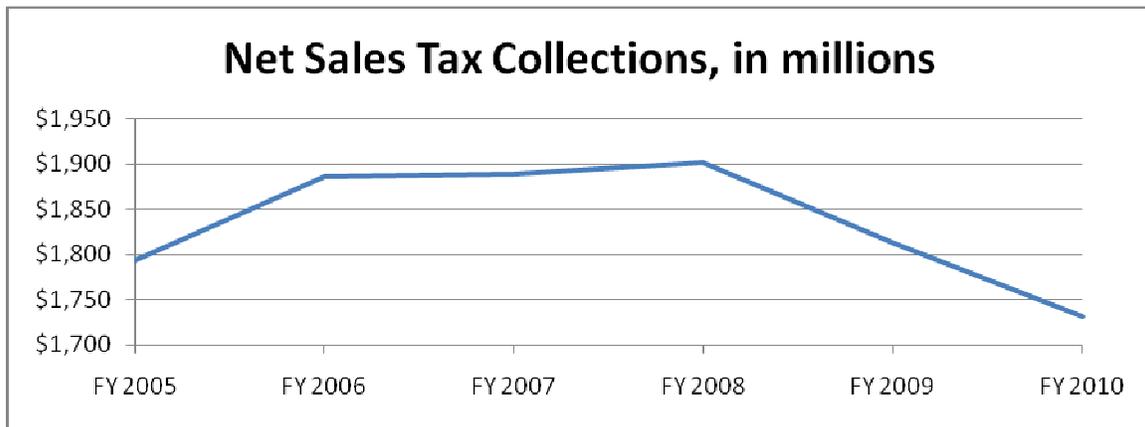
Source: *Missouri Office of Administration*

¹ Please note that in this and subsequent reports, all Sales tax will be considered as “Regular” sales. Since July of 2008, all Motor Vehicle Sales tax has been allocated to Highways and Transportation.

² U.S. Census Website: www.census.gov/retail/mrts/www/data/pdf/ec_current.pdf

As shown below, for FY 2010, net regular sales tax collections have fallen by \$170 million since FY 2008 and are well below the level *attained in FY 2005*.

Figure 6: Net Sales Tax Collection, in millions, FY 2005 – FY 2010



Corporate Income and Franchise Tax collections rose 8.4 percent in March and completed the first nine months of FY 2011 with growth of 8.2 percent. For FY 2011 thus far, corporate tax refunds have declined about 22 percent, allowing for net corporate tax growth of 44 percent. This is a substantial improvement over FY 2010, in which net corporate taxes fell nearly 20 percent.

While strength in this area good news, it must be tempered with some caution. Corporate collections and refunds have a strong tendency to show major fluctuations over relatively short periods. A strong quarter may not be indicative of the longer term trend. In addition, over the last two years, state corporate tax collections fell quite sharply. In FY 2008, net corporate tax collections totaled \$459.3 million. In FY 2010, this tax yielded only \$287.8 million, a decline of over 37 percent in just two years. Even assuming strong growth, the state is several years away from returning to the FY 2008 level for this tax.

The sub-components of this tax demonstrate the irregularity of tax revenue from this source. While declarations increased 15.0 percent over the first nine months of FY 2011, final payments/franchise declined 2.3 percent.

The corporate tax picture is complicated by several factors. An explicit reduction in the corporate franchise tax rate was signed into law in 2009, which is estimated to reduce collections from this source by up to \$14.5 million in FY 2011. In addition, the new federal tax law signed into law by President Obama in December includes a provision to allow more rapid deductions for business investment expenses. The *Center on Budget and Policy Priorities* estimates that this will reduce Missouri revenues by \$143 million over two years.³

Other Revenue Sources: Notable developments in the smaller revenue sources include:

³ “Business Expensing Proposal Would Add to State Fiscal Problems” by Nicholas Johnson and Ashali Singham- *Center on Budget and Policy Priorities* (www.cbpp.org/cms/index.cfm?fa=view+id=3344)

General Revenue Interest earnings continue to decline. For the first nine months of FY 2011, earnings were about \$5.0 million, a decline of 42 percent. With interest rates expected to remain extremely low, this source is not likely to generate much revenue over the coming months.

County Foreign Insurance collections rose 16.7 percent for the first nine months of FY 2011, a strong rebound from the 4.7 percent *decline* in this tax that was seen in FY 2010 overall.

General Revenue Refunds: General Revenue refunds declined 4.7 percent in March, and are *down 8.6 percent* through the end of March, one of the main reasons that the FY 2011 net GR growth rate is at a robust 6.5 percent.

Compared to 2009, the stronger economy of 2010 should result in a reduced refund growth rate. Increased investment income tends to reduce refunds and/or result in increased taxes paid as final returns are filed. Nonetheless, it would be reasonable to assume that refund growth will return to more historically normal levels as the peak tax return season is completed.

In addition, corporate refund growth is erratic on a month to month basis. However, it would be reasonable to assume that refunds will grow at more historical rates during the final quarter of FY 2011. In FY 2010, about 29 percent of refunds were paid during the final quarter of the fiscal year.

Summary and Outlook:

Net GR collections have now increased for four consecutive quarters, including the 10.9 percent growth in the quarter ending March 31st, and individual income tax withholding is on the rise. However, sales and use tax, which has declined in 11 of the last 14 quarters, fell 5.7 percent in March and is up only 0.7 percent for the fiscal year. In addition, much of the current strength comes from a sharp decline in refunds that may not be sustainable.

While there are some encouraging signs in revenue growth, *the \$1.507 billion in net GR collections achieved in the most recent quarter were below the \$1.52 billion net GR collections realized in the January-March quarter of FY 2006.*

Furthermore, even if net GR collections achieve the growth rates called for in the Consensus Revenue Estimate (3.6% & 4.0% in FYs 2011 and 2012 respectively) and grow at 3.0 percent in FY 2013 and beyond, the state would not see net GR collections attain the \$8.0 billion plateau reached in FY 2008 *until FY 2016*. Despite signs of recovery, the state budget outlook is still grim. It is unlikely that the state will be able to adequately fund the GR budget without some actions to enhance revenues.

(See next page for the March and FY 2011 General Revenue Collection table)

Figure 7: March GR Collections and Refunds

Tax Source	March FY 10	March FY 11	Percent Change	FY 2010	FY 2011	Percent Change
Individual Income						
Withholding	375,577	397,486	5.8	3,201,054	3,311,786	3.5
Declarations	10,585	11,274	6.5	370,261	372,672	0.7
Remittances	64,698	69,252	7.0	179,268	190,051	6.0
Fiduciaries	1,901	1,753	(7.8)	6,176	6,772	9.7
Total	452,775	479,768	6.0	3,756,825	3,881,360	3.3
Sales and Use						
Regular	157,149	148,218	(5.7)	1,336,638	1,345,472	0.7
Total	157,149	148,218	(5.7)	1,336,638	1,345,472	0.7
Corporate Tax						
Declarations	15,033	15,534	3.3	185,551	213,357	15.0
Remittances & Corp Franchise	35,008	38,703	10.6	120,494	117,734	(2.3)
Total	50,041	54,237	8.4	306,045	331,091	8.2
Estate	1	45	4400.0	93	1,306	1304.3
Interest	1,088	688	(36.8)	8,532	4,979	(41.6)
Liquor	1,567	1,361	(13.1)	17,735	15,990	(9.8)
Beer	618	552	(10.7)	6,085	5,991	(1.5)
County Foreign Insurance	43,650	41,018	(6.0)	132,421	154,507	16.7
Federal Reimbursements	3,190	14,107	342.2	45,781	88,688	93.7
All other revenues	16,754	16,830	0.5	117,823	111,068	(5.7)
Gross GR collections	726,833	756,823	4.1	5,727,978	5,940,451	3.7
GR Refunds						
Individual Income	228,028	209,366	(8.2)	735,270	683,791	(7.0)
Corp. Income & Franchise	2,199	5,929	169.6	165,875	129,264	(22.1)
Senior Citizen Property	31,956	30,318	(5.1)	87,585	84,459	(3.6)
Sales	1,733	5,047	191.2	40,216	39,239	(2.4)
All other	1,180	1,896	60.7	17,469	19,975	14.3
Total GR Refunds	265,096	252,556	(4.7)	1,046,415	956,728	(8.6)
Net General Revenue	461,737	504,267	9.2	4,681,563	4,983,723	6.5

Source: Missouri Office of Administration

*The mission of the Missouri Budget Project is to advance public policies that improve economic opportunities for all Missourians, particularly low and middle income families, by providing reliable and objective research, analysis and advocacy.
Contact the MBP through our website at www.mobudget.org*