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## State General Revenue Declines Sharply in April: Could Lead to Budget Reductions

*Tom Kruckemeyer, Director of Fiscal Policy and Chief Economist*

Missouri general revenue collections fell steeply in April, leaving the state with a backlog of tax refunds and jeopardizing revenue available for services in the next year. It now seems possible that the state will end Fiscal Year 2014 (FY 2014), which ends on June 30<sup>th</sup>, **at least \$100 million below the estimates.** This could result in mid-year budget withholdings, or reductions, in the budget that was recently approved by state lawmakers.

Missouri general revenue collections net of refunds fell five percent during the month of April compared to April of 2013. As a result of this decline, net general revenue collections have increased by only 0.5 percent overall for the first ten months of fiscal year FY 2014 – well below the estimates assumed by both the Governor and the Legislature of 2.8 percent and 2.0 percent, respectively.

It is also likely that the net general revenue situation is even weaker than these numbers indicate, because the state paid substantially fewer refunds in the latter portion of April 2014 compared to April 2013. **According to the Office of Administration, the state has a backlog of about \$167 million in individual income tax refunds. When these refunds are ultimately paid, it will further reduce the net general revenue growth, unless there is a significant increase in collections over the next two months of the fiscal year.**

### Revenue Summary:

**Individual Income Tax** – Gross individual income tax collections fell 13.5 percent in April and have fallen 0.8 percent during the first ten months of FY 2014.

Some decline was expected, because federal tax law changes in 2012 provided a one-time boost to tax receipts in many states in April 2013.<sup>1</sup> In fact, individual income tax remittance payments grew 56 percent in April 2013 compared to April 2012, and have now declined again, to \$495.5 million in April 2014 from \$662.4 million in April 2013.

In addition to this year's remittance decline, individual income tax withholding growth remains sluggish. Even though withholding rose a respectable 5.1 percent in April, the FY 2014 year-to-date growth rate is only 1.2 percent.

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<sup>1</sup> Federal tax law changes in 2012 made it advantageous for many individuals to realize and thus pay taxes on capital gains, boosting tax receipts in April 2013.

Collections in this area must improve to meet both the Governor's and legislative revenue estimates, which call for 3.2 percent and 3.0 percent individual income growth respectively. Unfortunately, the Missouri unemployment rate remains stubbornly above 6 percent. For March 2014, the UE rate stood at 6.7 percent, about the same as the 6.6 percent rate seen in March of 2013 and greater than the December UE rate, which was 6.0 percent.

***Sales and Use Tax***— Following a sluggish first quarter of 2014, (which saw sales and use tax gross collections decline 2.7 percent), April collections rebounded with an increase of 7.7 percent. This restores the FY 2014 year- to- date growth rate to a respectable 3.6 percent, which is fairly strong performance by recent year standards. In FY 2013, sales and use tax grew by only 1.3 percent. The Governor's and Legislative revenue estimates call for 4.2 percent and 3.6 percent growth in sales tax respectively, and the state remains in position to attain this level.

***Corporate Income/Franchise*** – Gross collections in this area fell 1.7 percent in April, but are up 7.1 percent for the fiscal year overall. While the year-to-date growth rate is fairly good, it is below the rate 11.3 and 8.4 percent growth called for by the Governor's and the Legislative revenue estimates.

***GR Refunds*** –The key to understanding the FY 2014 revenue situation at this juncture is found in the refund column. Through the end of March, GR refunds had increased 4.4 percent. In April, however, GR refunds totaled \$133 million versus \$216 million in April 2013, for a *decrease* of about 38 percent.

Furthermore, from April 18<sup>th</sup> through the end of the month, GR refunds paid out were only \$52 million in April of 2014 versus a total of \$144 million during this period in 2013. The state is obligated by the Constitution to re-pay monies borrowed from the *Budget Reserve Fund* on or before May 15<sup>th</sup>. The state repaid \$350 million to the *Budget Reserve Fund* in April. It would be reasonable to assume refund growth will be strong in May and June, thus putting downward pressure on net GR collections.

## Summary

It is important to note that it is likely that if refunds were being processed and paid at last year's pace, the net GR growth rate through April 30th would have been *negative*. In addition, even though April individual income tax withholding growth was solid, the growth rate after ten months is a sluggish 1.2 percent. Moreover, revenues will also be diminished by the continuing phase out of the state Corporate Franchise tax.

It now seems possible that the state will miss (on the downside) the FY 2014 revenue estimates by \$100 million or more. While a revenue shortfall in FY 2014 is not likely to be large enough to impact FY 2014 spending, problems may well arise in FY 2015 should the state begin the fiscal year with a smaller opening balance than was anticipated.

The overall numbers clearly show that Missouri has no "surplus revenues" and is not in a position to cut taxes and further erode its revenue base. Missouri should be aware of the consequences of declining revenue collections coupled with future significant tax cuts. The state of Kansas, burdened by declining revenues and on-going tax cuts, has seen Moody's Investor Services downgrade the bond rating for the State as well as the University of Kansas and Emporia State University. There can be little doubt that Missouri is heading down a dangerous fiscal path.

## Fiscal Year 2014 General Revenue Collections through April

*Dollars in Millions*

<u>Tax Source</u>	<u>April FY 2013</u>	<u>April FY 2014</u>	<u>Percent Change</u>	<u>FY 2013 YTD</u>	<u>FY 2014 YTD</u>	<u>Percent Change</u>
<b>Individual Income</b>	\$1,138.5	\$985.2	(13.5)	\$5,352.3	\$5,309.5	(0.8)
<b>Sales &amp; Use</b>	\$144.9	\$156.0	7.7	\$1,553.7	\$1,610.2	3.6
<b>Corporate Income/Franchise</b>	\$89.0	\$87.5	(1.7)	\$404.8	\$433.8	7.1
<b>County Foreign Insurance</b>	-\$1.4	\$0.4	NA	\$128.5	\$129.6	0.8
<b>All Other</b>	\$34.4	\$34.1	(0.9)	\$243.1	\$187.7	(22.8)
<b>Gross General Revenue</b>	\$1,405.4	\$1,263.2	(5.6)	\$7,682.4	\$7,670.8	(0.2)
<b>General Revenue Refunds</b>	\$216.0	\$133.3	(38.3)	\$1,014.9	\$967.7	(4.7)
<b>Net General Revenue</b>	<b>\$1,189.4</b>	<b>\$1,129.8</b>	<b>(5.0)</b>	<b>\$6,667.4</b>	<b>\$6,703.1</b>	<b>0.5</b>

Source: *Missouri Office of Administration*