


**STATE OF MAINE
REVENUE FORECASTING COMMITTEE**

Members:

Jerome Gerard, Chair, Acting State Tax Assessor
 James Breece, University of Maine System
 Marc Cyr, Principal Analyst, Office of Fiscal and Program Review
 Grant Pennoyer, Director, Office of Fiscal and Program Review
 Catherine Reilly, State Economist
 Ellen Jane Schneiter, State Budget Officer

March 26, 2007

TO: Governor John Baldacci
 Members, 123rd Legislature

FROM:  Jerome Gerard, Chair
 Revenue Forecasting Committee

RE: March 2007 Revenue Forecast

The Revenue Forecasting Committee (RFC) reconvened today to finalize its March revenue forecast. The RFC did not conclude its update for the March 1st reporting deadline in order to gain the benefit of a preliminary review of Corporate Income Tax payments that were due on March 15th. Shortly after the December 2006 forecast, Corporate Income Tax began to come in below revised projections. With a full week's processing, it is now clear that the Corporate Income Tax is not likely to perform at the level reflected in the December projections and that a downward adjustment to this revenue line is warranted.

Presented below is a table summarizing the changes to the General Fund, Highway Fund, Fund for a Healthy Maine and MaineCare Dedicated Revenue Taxes. Separate tables summarizing the effect for each of the funds by the major categories are also attached. A more detailed report will be forthcoming in a couple weeks.

General Fund Summary

	FY07	FY08	FY09	FY10	FY11
Current Forecast	\$3,020,947,915	\$3,078,691,800	\$3,162,051,521	\$3,265,921,996	\$3,320,959,326
Annual % Growth	3.0%	1.9%	2.7%	3.3%	1.7%
Net Increase (Decrease)	(\$33,736,442)	(\$21,003,856)	(\$19,583,936)	(\$20,190,670)	(\$11,407,826)
Revised Forecast	\$2,987,211,473	\$3,057,687,944	\$3,142,467,585	\$3,245,731,326	\$3,309,551,500
Annual % Growth	1.9%	2.4%	2.8%	3.3%	2.0%

Highway Fund Summary

	FY07	FY08	FY09	FY10	FY11
Current Forecast	\$330,757,329	\$340,996,299	\$347,196,520	\$350,245,413	\$356,494,765
Annual % Growth	1.3%	3.1%	1.8%	0.9%	1.8%
Net Increase (Decrease)	\$0	(\$2,100,239)	(\$2,912,734)	(\$2,990,234)	(\$3,643,229)
Revised Forecast	\$330,757,329	\$338,896,060	\$344,283,786	\$347,255,179	\$352,851,536
Annual % Growth	1.3%	2.5%	1.6%	0.9%	1.6%

Fund for a Healthy Maine Summary

	FY07	FY08	FY09	FY10	FY11
Current Forecast	\$46,189,344	\$60,408,950	\$62,815,948	\$67,818,647	\$71,548,715
Annual % Growth	-0.6%	30.8%	4.0%	8.0%	5.5%
Net Increase (Decrease)	\$231,280	\$167,761	\$239,938	\$239,938	\$239,938
Revised Forecast	\$46,420,624	\$60,576,711	\$63,055,886	\$68,058,585	\$71,788,653
Annual % Growth	-0.1%	30.5%	4.1%	7.9%	5.5%

Medicaid/MaineCare Dedicated Revenue Taxes Summary

	FY07	FY08	FY09	FY10	FY11
Current Forecast	\$121,526,004	\$122,825,633	\$124,157,752	\$125,523,174	\$126,922,732
Annual % Growth	2.9%	1.1%	1.1%	1.1%	1.1%
Net Increase (Decrease)	\$3,895,963	\$4,244,849	\$4,602,459	\$4,969,007	\$5,344,719
Revised Forecast	\$125,421,967	\$127,070,482	\$128,760,211	\$130,492,181	\$132,267,451
Annual % Growth	6.2%	1.3%	1.3%	1.3%	1.4%

The General Fund revisions, driven primarily by the Corporate Income Tax changes, represent a \$74.3 million decrease of budgeted revenue for the budget period under consideration by this Legislature. The changes to the Corporate Income Tax represent a reversal of a substantial portion of the upward revision that the RFC recommended in its December 2006 forecast. At that time, the indications were that corporate income tax payments were showing very healthy growth consistent with national trends. It now appears that the spike in receipts at the end of FY06 was a timing issue that is being reversed as this fiscal year moves forward.

It is important to note that while Maine's corporate income tax is growing at a slower rate than the nation as a whole, the annual growth rate implicit in this forecast is still a solid 11% between FY05 and FY08. Consistent with most national forecasts, the RFC is forecasting much slower growth in corporate receipts beyond FY08.

Apart from the downward revision to the corporate income tax, the modest changes in the economic forecast resulted in only modest changes to the other categories in the General Fund revenue forecast. However, during the current fiscal year ending June 30, 2007 (FY07), this forecast does represent unanticipated downward revision for budget decision makers. In addition to the Corporate Income Tax change, Individual Income Tax was adjusted downward by \$1.5 million for timing issues related to bonus depreciation recapture and \$5.0 million related to additional Business Equipment Tax Reimbursement changes. The Telecommunications Personal Property Tax (within the Public Utilities Tax category) was adjusted for changes in the valuation of those assets. Income from Investments was adjusted downward by just over \$3.0 million annually to reflect a reduction in cash balances and consequently earnings as a result of utilizing internal borrowing rather than Tax Anticipation Note financing.

These negative adjustments were partially offset by some positive adjustments in the General Fund. Revenue from Liquor Sales and Operations and revenue from Liquor Taxes were adjusted upward as were Racino revenues. Revenue collected by the Department of Health and Human Services was also adjusted upward in each year of the forecast.

The amount of revenue realized by the Milk Handling Fee and the Transfer to the Maine Milk Pool are directly determined by milk prices. Because milk prices are very volatile and difficult to forecast, the committee plans to revisit these revenue sources during each forecast session. These revenue sources were first effective in FY06, but became significant revenue items in FY07 when milk prices dropped. The inverse relationship between milk prices and these

revenue sources increased the magnitude of these revenue items. Milk prices are now projected to be higher than the December forecast, resulting in a decline in magnitude and a net positive increase to revenue for these 2 categories.

The preliminary assessment of Highway Fund revenue by the RFC was reaffirmed today. There were no changes to the RFC's December forecast for FY07, but some modest downward revisions in Fuel Taxes resulted from the lower inflation projections in the Consensus Economic Forecasting Commission forecast. The adjustments result in a \$5.0 million downward revision for the 2008-2009 biennium.

The Fund for a Healthy Maine received modest upward adjustments in revenue projections from additional interest earnings and from the strong performance of the Racino revenue. Over the 3 year budget period, this will increase revenue by just under \$640,000. MaineCare Dedicated Revenue Taxes were also revised upward in aggregate based on recent experience. As noted in our February letter, the adjustment to the MaineCare Taxes does not take into account a recent federal restriction added to these taxes that must be addressed by legislative action to change the rate of the tax to bring it within the federal restrictions.

Finally, while the adjustments made today certainly create challenges for the Administration and the Legislature as they work toward a biennial budget, it only represents a 1% change in the total annual forecast of General Fund revenues. Nothing in the national or state economies has fundamentally changed during the intervening months between the December and March revenue forecasts to materially affect this forecast. Today's recommendations correct for a misinterpretation of last year's corporate receipts, and should be viewed as such.

Attachments

cc: Members, Revenue Forecasting Committee
Members, Consensus Economic Forecasting Commission
Jane Lincoln, Chief of Staff, Governor's Office
Ryan Low, Deputy Chief of Staff, Governor's Office
Rebecca Wyke, Commissioner, DAFS
Millie MacFarland, Clerk of the House
Joy O'Brien, Secretary of the Senate
David Boulter, Executive Director, Legislative Council
Legislative Staff Office Directors