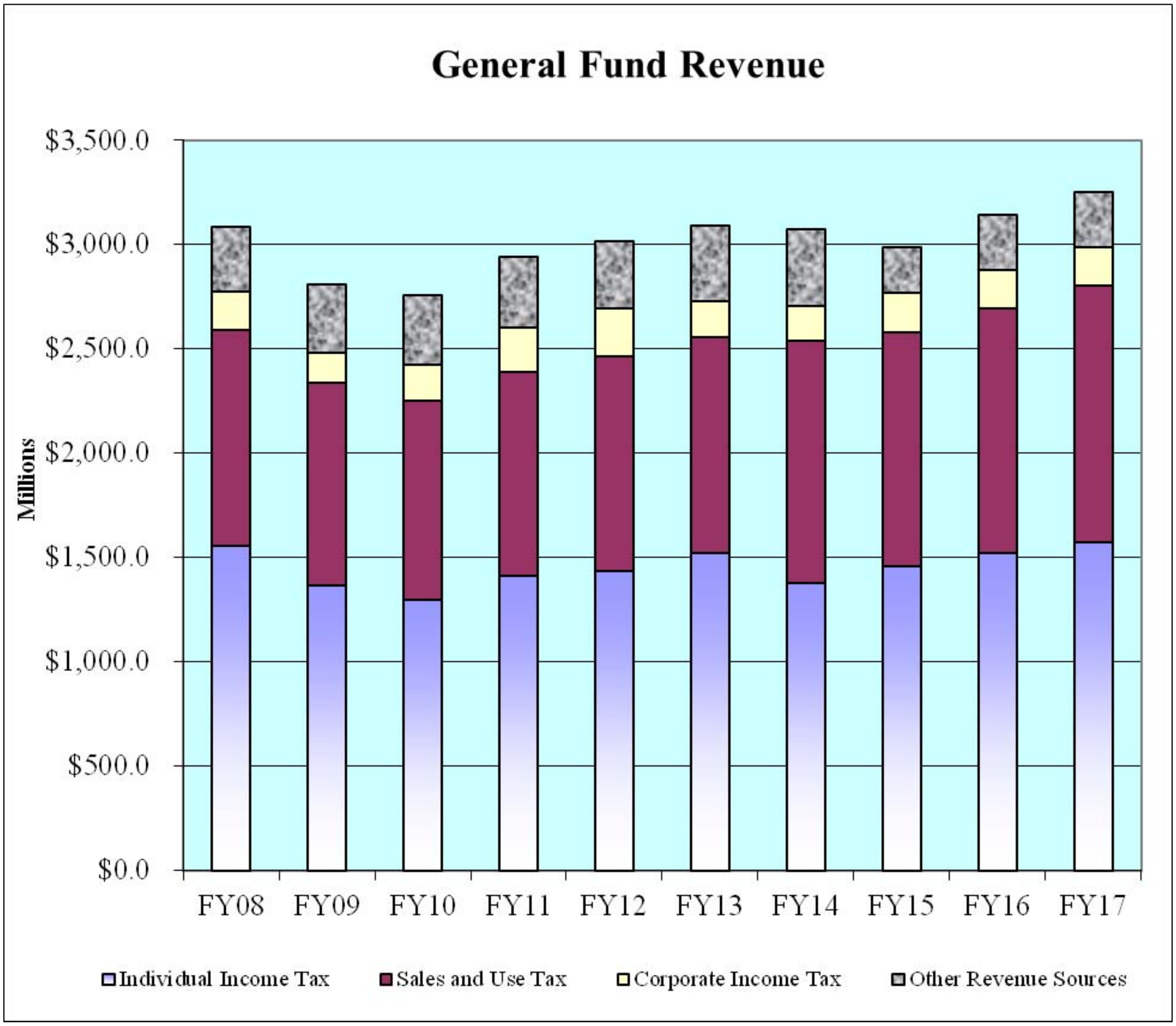
REPORT OF THE MAINE STATE REVENUE FORECASTING COMMITTEE

March 2014



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March 2014 Forecast

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Introduction

The Revenue Forecasting Committee (RFC) met on February 21, 2014 to review and update the current revenue forecast to comply with this year's statutory reporting date of March 1st. The RFC revised its revenue projections through the fiscal year ending June 30, 2017 based on the new economic forecast by the Consensus Economic Forecasting Commission for its February 1st reporting date, updated tax data and a review of recent experience. The RFC updated its forecasts for the General Fund, Highway Fund, Fund for a Healthy Maine and Medicaid/MaineCare Dedicated Revenue Taxes.

Summary of Economic Forecast

This update of the revenue forecast included a review of the economic forecast statutorily due by February 1st, three months after the previous revision. The economic forecast was developed by the Consensus Economic Forecasting Commission (CEFC) at its meeting on January 30.

The Maine and U.S. economies continued along the path of gradual improvement since the CEFC met in October 2013, with Maine's economy continuing to grow more slowly than the nation as a whole.

Personal income in Maine grew 2.5% year-over-year in the first three quarters of 2013, while wage and salary income, which makes up around half of total personal income, grew 2.7% over the same period. The debt-to-income level for Maine businesses and households jumped to pre-recession levels in the second quarter of 2013. The Consumer Price Index was 1.5% higher in December 2013 than it was in December 2012.

Nationwide, consumer sentiment increased 9.9% month-over-month in December while small business optimism increased 1.5% over the month and was up 6.7% over the previous year's level. The price of crude oil decreased 0.3% in the fourth quarter of 2013 to around $109 per barrel. Heating oil prices increased slightly through the current heating season while gasoline prices remained relatively steady.

Existing single-family home sales in Maine were up 11.5% in December 2013 compared to December 2012 and housing permits for the December 2012-November 2013 year were 14.4% higher than the previous 12-month period. The median home price in the Portland Metropolitan Statistical Area (York, Cumberland, and Sagadahoc Counties) increased 5.3% year-over-year in the third quarter of 2013. Mortgage delinquency rates remain above pre-recession levels but below peak crisis levels. The foreclosure rate in Maine declined in the third quarter of 2013 although it remained above the national rate for a fifth straight quarter.

With only one or two new data points, much of the forecast was left unchanged from the December 2013 forecast. Wage and salary employment, inflation, and several components of personal income were left unchanged. The major revisions to the forecast were to corporate profits and dividends, interest, and rent. Transfer payments were adjusted for 2013 and 2014. Non-farm proprietors' income was adjusted for 2013 only. In each of these cases, the forecast was adjusted to accept the IHS Economics baseline forecast.

The forecasts for wage and salary employment, wage and salary income, and supplements to wages and salaries remain below the Moody's Analytics and IHS Economics forecasts in most years. This is a result of the consensus that these forecasts are based on overly optimistic population projections for the state of Maine, causing employment forecasts, among other things, to grow at an unattainable rate. For this reason, employment and the components of income most closely correlated with employment levels were left unchanged from the previous downward revision.

Total personal income was left unchanged for 2013 and revised downwards by a tenth of a percentage point for each year of 2014-2017. The CEFC accepted the baseline forecast from IHS Economics for corporate profits for all years.

A copy of the February 2014 report of the CEFC and other economic information providing the basis for this revenue forecast is included in Appendix E.

Summary of Revenue Forecast

This new RFC revenue forecast essentially reaffirms the December 1, 2013 revenue forecast. Given the rather modest nature of the adjustments to the economic variables in the CEFC forecast, the economic forecast was not a significant factor in the revisions in this revenue forecast. With the major General Fund taxes tracking very close to budget and very little new data since the last revenue forecast, the RFC is not recommending any significant changes from its last forecast.

The review of recent performance and data related to non-tax revenue lines by a number of different state agencies and staff in the Office of Fiscal and Program Review and the Bureau of the Budget also produced only modest net changes to the fall forecast. The consensus recommendations of this process were reviewed by the RFC at its meeting on February 21st and were accepted. The following tables and narratives highlight the final changes to each of the major funds and revenue sources projected by the RFC as part of this revenue forecast. More detail on each of the funds and revenue sources is provided in the various appendices.

General Fund Summary

	FY13 Actual	FY14	FY15	FY16	FY17
Current Forecast	$3,094,383,842	$3,074,377,614	$3,275,813,158	$3,141,373,000	$3,254,534,076
Annual % Growth	2.6%	-0.6%	6.6%	-4.1%	3.6%
Net Increase (Decrease)		($223,125)	$2,488,233	$63,134	($636,866)
Revised Forecast	$3,094,383,842	$3,074,154,489	$3,278,301,391	$3,141,436,134	$3,253,897,210
Annual % Growth	2.6%	-0.7%	6.6%	-4.2%	3.6%

General Fund revenue estimates were revised downward by $0.2 million in FY14 and upward by $2.5 million in FY15 (upward by $2.3 million for the 2014-2015 biennium). The forecasts for the major tax lines were left unchanged in this forecast. Changes in the forecast for milk prices and adjustments to revenue from liquor sales and lottery operations were the major factors in this forecast.

While sales tax revenues are over budget through January by $4.7 million, consumer sales activity has slowed significantly since late fall. The surplus since the last forecast represents weak sales activity, but not as weak as projected. Adjusting for the sales tax increase, year-over-year growth for November and December was only 1.6%; well below the 6.4% average for the three month period ending in October.

The new revenue forecast assumes similar growth for January and February and then picking up to approximately 4% for the remainder of FY14. These assumptions result in no change for this tax line.

Individual income tax receipts are over budget by $2.5 million through January. While the total line is close to budget, estimated payments are under budget by $12.3 million and are currently being offset by surpluses on the other sources of individual income tax receipts. The March RFC forecast makes no change to the previous forecast and assumes that slightly stronger final payments and lower refunds will negate the weaker than projected final estimated payment for the 2013 tax year. Even with this assumption, final payments for the 2013 tax year are assumed to be 17.5% lower than 2012 and refunds are projected to be 22.5% higher than 2012.

Some of the increase in refunds is associated with the new Property Tax Fairness Credit (PFTC). Through the middle of February returns processed show the PTFC may not be reducing revenue by as much as estimated during last session's budget negotiations. The RFC has decided to keep the current projection for the PTFC of approximately $35 million for the 2013 tax year and reevaluate after the close of the income tax processing season.

Corporate Income Tax was also slightly over budget through January. However, there remain a number of refund requests that are being reviewed by MRS that may impact FY14 corporate receipts. For that reason and for lack of new data, the RFC has decided not to change the current forecast for corporate income tax receipts.

Although there were no aggregate changes to the totals for the projections of the revenue sharing taxes, the monthly distribution of the sales and income taxes will be adjusted and consequently will result in a shift of the projected Transfers for Municipal Revenue Sharing between FY14 and FY15. The total projected transfers for the 2014-2015 biennium are not affected.

For each forecast, the RFC receives an updated forecast of milk prices. The volatility of milk prices usually produces changes in each forecast affecting both the Milk Handling Fee and Transfers to Maine Milk Pool. The milk price forecast for the March 2014 update reflects an increase in milk prices (see Appendix F). As a result, the projections for Milk Handling Fee revenue are decreased by $0.1 million in FY14, $0.8 million in FY15 and $1.1 million annually in FY16 and FY17. The more significant effect of the revised milk price forecast was on the Transfers to Maine Milk Pool, which were revised downward (a General Fund revenue increase) by $0.3 million in FY14, $2.8 million in FY15 and $2.1 million annually. The Transfers to Maine Milk Pool category is also affected by projections of dedicated revenue from the Oxford Casino. No revisions were included in this forecast for casino revenue.

Revenue from Liquor Sales and Operations was updated in FY14 to reflect the actual profit sharing amount for calendar year 2013 paid to the General Fund. The actual transfer was $1.6 million higher than budgeted.

Lottery revenue was revised downward by $2.25 million in FY14, upward by $0.3 million in FY15. The rebound in FY15 reflects the effect of the first full year of savings related to a new contract. Longer term projections of lottery revenue reflect modest growth, but a decline of $1.0 million from budget in FY16 and $1.7 million in FY17.

The estimates for Transfers to Tax Relief Programs were revised in FY14 by a net downward adjustment of $0.7 million. The Business Equipment Tax Reimbursement (BETR) program was revised upward to reflect lower than anticipated transfers from the General Fund of $0.6 million and the Business Equipment Tax Exemption (BETE) program was revised downward to reflect higher than anticipated transfers of $1.4 million. Future years may need to be adjusted in this coming fall's forecast when the local data is available.

The Finance Industry Fees were adjusted upward in this forecast, similar to the situation in the December forecast. The $0.5 million increase of projections recognizes a portion of the positive variance accumulated through January.

Miscellaneous revenue adjustments for the Department of Health and Human Services revenue sources, one-time increase from concealed weapons permit fees and the General Fund portion of the changes to the gasoline tax estimates (see Highway Fund discussion) result in net increases to budgeted revenue of $0.4 million in FY14 and $0.1 million annually beginning in FY15.

More detail on the other revenue categories can be found in Appendix A and other background materials in Appendix F.

Highway Fund Summary

	FY13 Actual	FY14	FY15	FY16	FY17
Current Forecast	$318,825,700	$308,575,863	$306,789,766	$306,422,199	$306,042,627
Annual % Growth	0.5%	-3.2%	-0.6%	-0.1%	-0.1%
Net Increase (Decrease)		$1,691,348	$1,786,974	$1,800,475	$1,786,975
Revised Forecast	$318,825,700	$310,267,211	$308,576,740	$308,222,674	$307,829,602
Annual % Growth	0.5%	-2.7%	-0.5%	-0.1%	-0.1%

Highway Fund revenue estimates (also see Appendix B) were revised upward by $1.7 million in FY14 and $1.8 million in FY15 ($3.5 million for the 2014-2015 biennium). These revisions result primarily from upward revisions to gasoline tax receipts.

After making no adjustments to the forecast for fuel taxes in the December 2013 forecast, the RFC recognized a $2.0 million increase of projections for gasoline tax in each year of the forecast period, which after various transfers resulted in a net increase of Highway Fund revenue of $1.8 million. The RFC recognized only a portion of the $4.3 million positive variance in the Fuel Taxes category that has accumulated through January. Monthly fluctuations from budget for this category have been common and were the primary reason for the cautious recognition of only a portion of the recent positive variances.

Within the broader category of Motor Vehicle Registrations and Fees, the RFC revised estimates for Motor Vehicle Operator License Fees downward by $0.3 million in FY14 only based on recent performance. Other one-time FY14 adjustments to revenue included: a $0.05 million downward adjustment to Income from Investments and a $0.24 upward adjustment to reflect additional revenue accruing to the Highway Fund from the Municipal Excise Tax Reimbursement program.

Fund for a Healthy Maine Summary

	FY13 Actual	FY14	FY15	FY16	FY17
Current Forecast	$50,992,315	$54,705,782	$54,340,982	$53,861,451	$53,384,108
Annual % Growth	-8.1%	7.3%	-0.7%	-0.9%	-0.9%
Net Increase (Decrease)		$1,214,994	$6,343,549	$833,155	$890,662
Revised Forecast	$50,992,315	$55,920,776	$60,684,531	$54,694,606	$54,274,770
Annual % Growth	-8.1%	9.7%	8.5%	-9.9%	-0.8%

The Fund for a Healthy Maine (FHM) revenue forecast was adjusted upward by $1.2 million in FY14 and $6.3 million in FY15. The RFC reviewed and adopted revised estimates of the tobacco settlement payments released by the National Associations of Attorneys General (NAAG), which increased projections of these payments by $1.2 million in FY14 and $0.8 million in FY15. These estimates continue to assume full withholding of disputed payments by participating manufacturers.

There remains a good deal of uncertainty surrounding certain legal proceedings under the Master Settlement Agreement. Maine prevailed in the legal challenge related to the NPM (non-participating manufacturer) adjustment for 2003 calendar year sales. The release of Maine's share of the disputed payments for that sales year, $5.6 million, is being challenged by certain states that were not successful in these proceedings. There is a potential for Maine's share of these disputed payments to be included in the April 2014 payment. The RFC assumes that the states challenging the release of the disputed payments may be successful in delaying the release as part of the April 2014 payment, but ultimately Maine would receive the $5.6 million as part of the April 2015 payment.

As noted in the General Fund section, the RFC recommended no changes to the revenue estimates from casinos. As a result, the 10% percent share of slot machine revenue at Hollywood Casino in Bangor that accrues to the FHM remains as forecasted in the December 2013 forecast.

Medicaid/MaineCare Dedicated Revenue Taxes Summary

	FY13 Actual	FY14	FY15	FY16	FY17
Current Forecast	$153,241,054	$172,021,517	$172,021,517	$172,021,517	$172,021,517
Annual % Growth	0.9%	12.3%	0.0%	0.0%	0.0%
Net Increase (Decrease)		($3,583,841)	($3,583,841)	($3,583,841)	($3,583,841)
Revised Forecast	$153,241,054	$168,437,676	$168,437,676	$168,437,676	$168,437,676
Annual % Growth	0.9%	9.9%	0.0%	0.0%	0.0%

The forecast of Medicaid/MaineCare Dedicated Revenue Taxes revenue was revised downward by $3.6 million in each year of the forecast based on updated information. The most significant revision was the $3.2 million downward revenue adjustment for the Hospital Excise Tax, which was increased beginning in FY14 by the Biennial Budget Bill, PL 2013, c. 368 to modify the hospital tax base year from hospital fiscal years ending during calendar year 2008 to hospital fiscal years ending during calendar year 2012. The estimates for this tax were downgraded to reflect the closing of one hospital and the incorrect reporting of revenue by certain hospitals. Another revenue change in the Biennial Budget Bill increased estimates for the Service Provider Tax - Private Non-medical Institutions. Those estimates were also downgraded based on recent experience by $0.4 million annually. (See Appendix D for more information).

Conclusions

The modest changes in this forecast and the immediately preceding forecasts indicate that we have settled into a period of stable, but slow growth and recovery. The volatile swings during the recent recession and the risks to the forecasts have subsided. Federal budget stability and the lack of pending crisis have contributed to this more stable pattern and should help to sustain it for the immediate future.

However, there are concerns over Maine's demographics with an aging population and little to no population growth. The Consensus Economic Forecasting Commission (CEFC) noted that the Maine forecasts produced by the major economic forecasting firms were too optimistic in their employment outlook given Maine's demographics. While the CEFC adjusted its Maine forecast downward from the forecast provided by IHS Economics, these ad hoc adjustments to the economic model in the income and employment variables may not have adequately captured all the interactive effects on the other variables. The CEFC and the RFC will be working with the major forecasting firms, Moody's Analytics and IHS Economics, to improve the underlying assumptions in their forecasts for Maine.