



# MONTANA LEGISLATIVE BRANCH

## Legislative Fiscal Division

Room 110 Capitol Building \* P.O. Box 201711 \* Helena, MT 59620-1711 \* (406) 444-2986 \* FAX (406) 444-3036

**Director**  
AMY CARLSON

DATE: March 20, 2017

TO: Sen. Scott Sales, Senate President  
Rep. Austin Knudsen, House Speaker  
Sen. Mark Blasdel, Chair, Senate Tax Committee  
Rep. Jeff Essmann, Chair, House Tax Committee  
Sen. Fred Thomas, Senate Majority Leader  
Rep. Ron Ehli, House Majority Leader  
Sen. Jon Sesso, Senate Minority Leader  
Rep. Jenny Eck, House Minority Leader

FROM: LFD Revenue Team

RE: General Fund Revenue Forecast Update #3

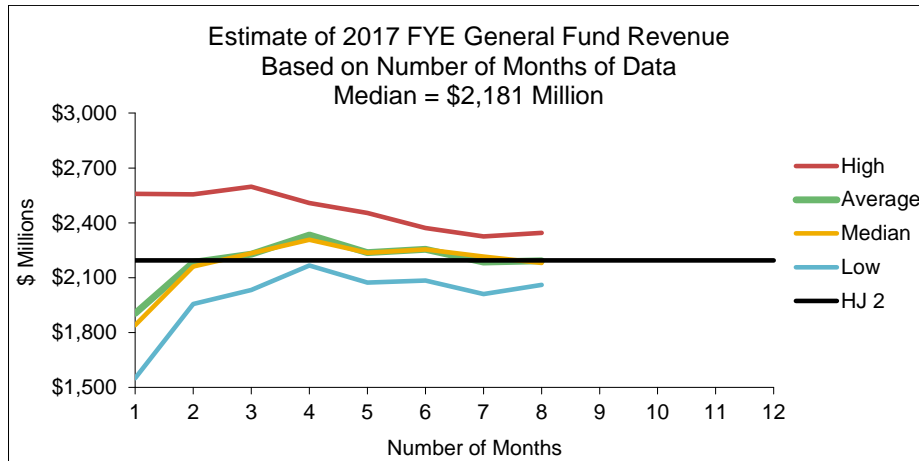
### GENERAL FUND REVENUE SUMMARY

This is the third of the monthly revenue forecast updates throughout the 2017 Session designed to brief the legislature on recent economic trends and the corresponding outlook for the 2019 Biennium general fund revenue estimate. This update is based on actual revenue collections received through the end of February 2017, and updated national and Montana forecasts from IHS.

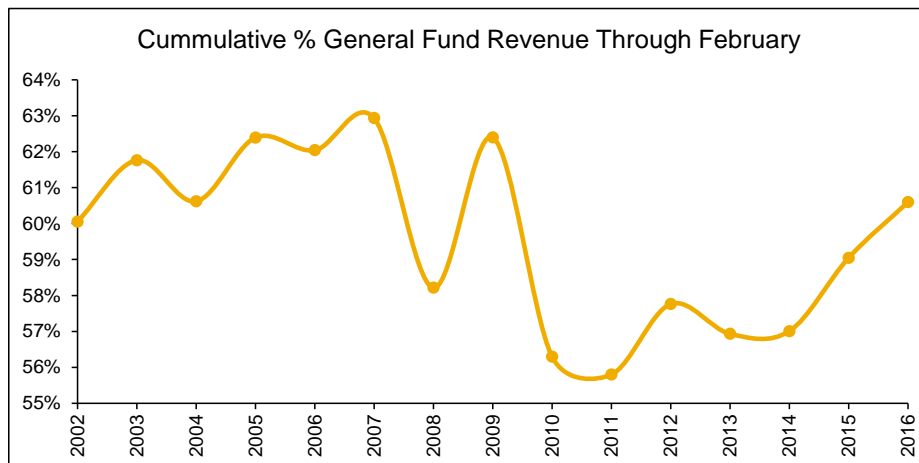
FY 2017 general fund revenues through the end of February are \$34.0 million or 2.6% higher than FY 2016 revenues through the same period; this increase is below the anticipated growth of 3.4%. Over one-third of total general fund revenue is typically booked in the state accounting system (SABHRS) in the fourth quarter of the fiscal year. Individual income, corporation income, and oil & natural gas taxes are all anticipated to have strong fourth quarter collections relative to FY 2016, which would lead to total FY 2017 collections in line with or above the estimate contained in HJ 2

## Year-to-Date Actual Collections Relative to Historical Patterns

As the fiscal year progresses, the accruing data allows for a closer estimate of final collections based on historical collection patterns. Potential total general fund collections for FY 2017 are calculated using various year-to-date percentages—minimum, maximum, median and average—since FY 2002. The results are shown in the chart below. Based on collections through the end of February, the difference between the high and low amounts is about \$284 million, with the median value about \$14 million below the HJ 2 estimate.



The median value shown in the chart above should be adjusted for two factors: as discussed in the individual income tax section, low refunds in February likely to overstate year-to-date collections; meanwhile, the revenue collection pattern—especially for the months of February and March—has distinctly changed since FY 2002, resulting in a year-to-date comparison which likely understates final collections. The chart below illustrates cumulative percentage through February of general fund revenue collections with adjustments for changes in the Department of Revenue’s accruals and return processing.



The median collection share through February since FY 2002 is 55.65%. A more recent ten-year median is 53.85%, or 1.8% lower. This shift in revenue collection pattern is muting the anticipated final collections in the median calculation depicted in the chart at the top of the page. Adjusting for both the lower refunds and shift in collections results in an adjusted median final collection amount of \$2,216 million, which is consistent with last month and the March updated forecast.

## March Forecast: \$106.2 Million above HJ 2

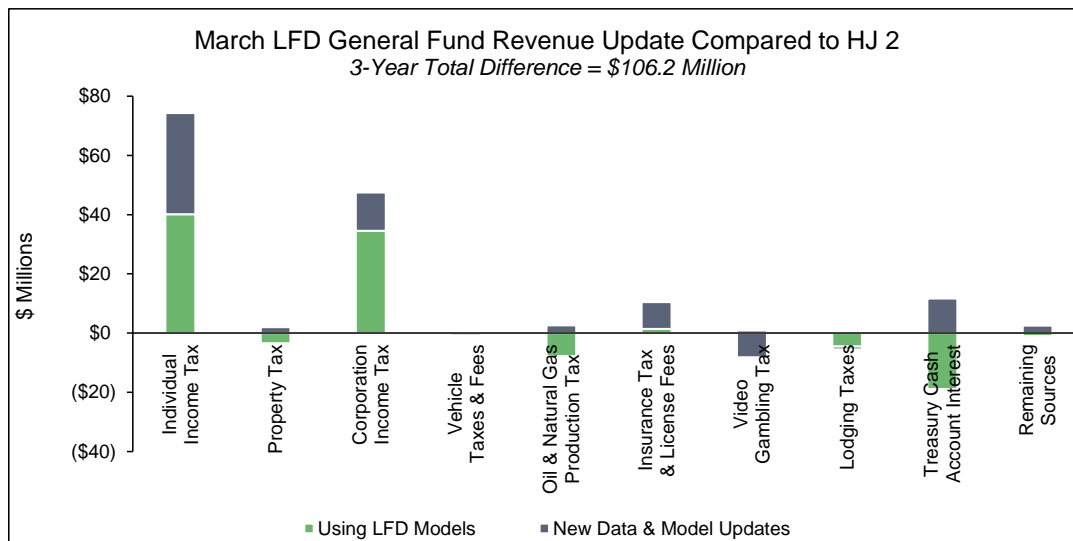
The March economic forecasts from IHS combined with LFD revenue models generates a general fund revenue forecast that is \$106.2 million higher than the official estimate in HJ 2 over the three-year forecast period. The table below shows the HJ 2 estimate and the LFD March update based on revised assumptions.

March LFD General Fund Revenue Estimate Update (\$ Millions)					
FY	HJ 2	March Update	\$ Difference	HJ 2 Growth	March Update Growth
2016	\$2,121.3	\$2,121.3			
2017	2,194.3	2,219.0	\$24.7	3.4%	4.6%
2018	2,301.4	2,359.1	57.8	4.9%	6.3%
2019	2,452.6	2,476.4	23.8	6.6%	5.0%
3-Yr	\$6,948.3	\$7,054.5	\$106.2		

The revised forecast from IHS incorporates the following key assumptions:

- Selected policies proposed by the new federal administration, including lower personal and corporate tax receipts to the federal government, consistent with the House Republican plan, as well as \$250 billion in additional infrastructure spending over 10 years and a hiring freeze for federal nonmilitary employees. The forecast does not include border adjustment of corporate taxes or expensing of capital expenditures
- Higher federal fund interest rate targets of 1.50% by the end of 2017, 2.25% by the end of 2018, and 3.00% by the end of 2019
- Higher oil prices—West Texas Intermediate (WTI) prices of \$55/bbl in 2017, \$55/bbl in 2018 and \$64/bbl in 2019—lead to renewed growth in US oil production; capital spending has already increased primarily due to drilling for oil and natural gas
- Increasing strength of the dollar through 2017, followed by a steady decline through 2027

The LFD March update changes compared to HJ 2 are shown in the graph below, with fiscal year detail provided in the table on the next page. Since HJ 2 is equivalent to the executive November estimate, which was \$40.6 million below the LFD November estimate over the three year estimate period, 38% of the increase in the LFD March update is due to using LFD revenue models, with the remaining increase due to the improved IHS economic outlook and LFD model revisions.



March LFD Update Summary of Changes from HJ 2				
(\$ Millions)				
Revenue Source	FY 2017	FY 2018	FY 2019	3-Yr Total
Individual Income Tax	\$18.7	\$29.6	\$26.0	\$74.3
Property Tax	0.9	(2.5)	0.2	(1.4)
Corporation Income Tax	6.1	34.2	7.2	47.4
Vehicle Taxes & Fees	1.6	0.3	(3.0)	(1.1)
Oil & Natural Gas Production Tax	0.5	0.4	(6.0)	(5.1)
Insurance Tax & License Fees	2.3	3.0	5.1	10.4
Video Gambling Tax	(3.2)	(2.6)	(1.3)	(7.2)
Lodging Taxes	(0.8)	(1.9)	(2.9)	(5.5)
Treasury Cash Account Interest	(1.5)	(2.9)	(2.8)	(7.2)
Remaining Sources	0.1	0.1	1.2	1.5
General Fund Total	24.7	57.8	23.8	106.2
Guarantee Fund	(1.5)	(1.6)	(3.0)	(6.1)
General Fund & Guarantee Fund Total	\$23.2	\$56.2	\$20.8	\$100.1

## NEXT STEPS

Updated revenue forecasts will be published monthly throughout the 2017 Session. The next report will be available in mid-April. New data will be available and incorporated into the LFD April general fund revenue forecast update. Key sources of new data include the following:

- IHS National & Montana economic forecasts
- IHS reports and analysis
- SABHRS revenue collection data through March
- Board of Oil & Gas production data
- Department of Revenue detailed collection data through March

## YEAR-TO-DATE GENERAL FUND REVENUE

FY 2017 general fund revenues through the end of February are \$34.0 million or 2.6% above FY 2016 revenues through the same period; this increase is below the HJ 2 estimated growth of 3.4%.

General Fund Revenue Monitoring Report							
(\$ Millions)							
Revenue Source	Actual FY 2016	HJ 2 Est. FY 2017	HJ 2 Est. % Change	YTD FY 2016	YTD FY 2017	YTD Difference	YTD % Change
<b>Largest Seven Sources</b>							
Individual Income Tax	\$1,184.828	\$1,219.776	2.9%	\$833.227	\$856.836	\$23.609	2.8%
Property Tax	257.100	260.150	1.2%	143.816	142.061	(1.755)	-1.2%
Corporation Tax	118.387	140.308	18.5%	76.319	74.151	(2.168)	-2.8%
Vehicle Taxes & Fees	108.480	109.200	0.7%	59.638	63.660	4.022	6.7%
Oil & Natural Gas Taxes	39.083	44.821	14.7%	11.260	10.932	(0.328)	-2.9%
Insurance Tax	69.255	71.102	2.7%	31.397	34.774	3.376	10.8%
Video Gaming Tax	60.554	62.522	3.3%	30.050	29.458	(0.592)	-2.0%
<b>Other Business Taxes</b>							
Drivers License Fee	4.345	4.539	4.5%	2.877	2.679	(0.198)	-6.9%
Investment Licenses	7.212	7.433	3.1%	6.631	6.733	0.102	1.5%
Lodging Facilities Sales Tax	21.493	22.978	6.9%	13.044	12.628	(0.416)	-3.2%
Public Contractor's Tax	2.397	2.510	4.7%	2.524	2.980	0.456	18.1%
Railroad Car Tax	3.594	3.437	-4.4%	3.111	3.528	0.418	13.4%
Rental Car Sales Tax	3.878	3.282	-15.4%	2.700	1.944	(0.756)	-28.0%
Retail Telecom Excise Tax	16.775	16.165	-3.6%	8.569	7.610	(0.959)	-11.2%
<b>Other Natural Resource Taxes</b>							
Coal Severance Tax	14.236	13.225	-7.1%	7.506	8.798	1.292	17.2%
Electrical Energy Tax	4.536	4.595	1.3%	2.374	2.332	(0.042)	-1.8%
Metal Mines Tax	4.221	4.129	-2.2%	0.241	0.095	(0.146)	-60.6%
U.S. Mineral Leasing	16.759	19.610	17.0%	11.854	9.204	(2.650)	-22.4%
Wholesale Energy Trans Tax	3.516	3.502	-0.4%	1.832	1.831	(0.001)	-0.1%
<b>Other Interest Earnings</b>							
Coal Trust Interest Earnings	20.722	19.893	-4.0%	10.152	11.782	1.630	16.1%
TCA Interest Earnings	3.961	5.802	46.5%	1.954	3.071	1.117	57.2%
<b>Other Consumption Taxes</b>							
Beer Tax	3.027	3.029	0.0%	1.766	1.722	(0.043)	-2.5%
Cigarette Tax	31.103	30.980	-0.4%	19.476	18.649	(0.827)	-4.2%
Liquor Excise Tax	19.776	20.596	4.1%	11.558	11.971	0.412	3.6%
Liquor Profits	11.000	11.777	7.1%	-	-	-	-
Lottery Profits	11.963	11.549	-3.5%	2.417	3.267	0.850	35.2%
Tobacco Tax	6.184	6.329	2.4%	3.631	3.663	0.032	0.9%
Wine Tax	2.373	2.412	1.6%	1.426	1.446	0.020	1.4%
<b>Other Sources</b>							
All Other Revenue	41.420	42.518	2.7%	18.436	20.362	1.926	10.4%
Highway Patrol Fines	4.040	4.187	3.6%	2.282	2.222	(0.060)	-2.6%
Nursing Facilities Fee	4.764	4.526	-5.0%	2.395	2.313	(0.082)	-3.4%
Public Institution Reimbursement	16.910	14.083	-16.7%	1.677	7.448	5.772	344.3%
Tobacco Settlement	3.394	3.371	-0.7%	-	0.010	0.010	-
Largest Seven Subtotal	1,837.687	1,907.880	3.8%	1,185.707	1,211.871	26.164	2.2%
Remaining Sources Subtotal	283.601	286.457	1.0%	140.432	148.288	7.856	5.6%
<b>Grand Total</b>	<b>\$2,121.288</b>	<b>\$2,194.337</b>	<b>3.4%</b>	<b>\$1,326.139</b>	<b>\$1,360.160</b>	<b>\$34.021</b>	<b>2.6%</b>

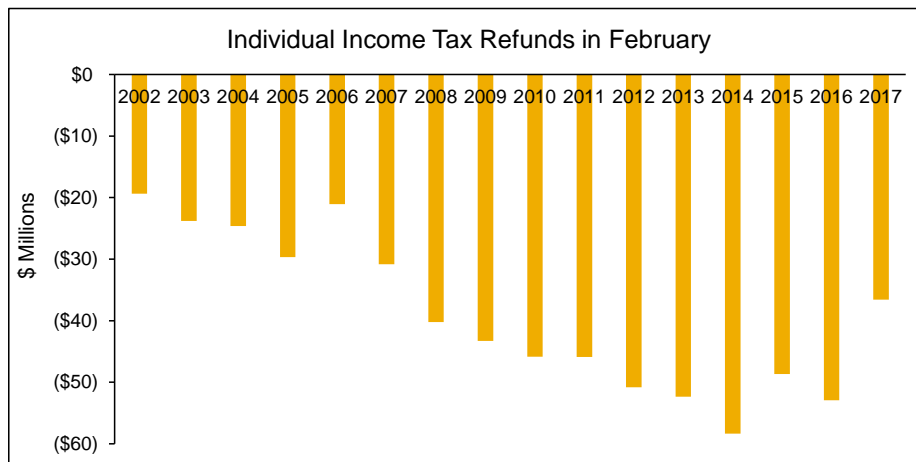
# LFD MARCH REVENUE UPDATE DETAIL BY MAJOR SOURCE

## Individual Income Tax

Individual income tax collections through the end of February are \$23.6 million or 2.8% above the year-to-date collections in FY 2016. Withholding growth is primarily offset by lower estimated payments and audit revenue.

Individual Income Tax				
(\$ Millions)				
	YTD 2017	YTD 2016	\$ Difference	% Difference
Withholding	\$602.6	\$578.1	\$24.6	4.3%
Estimated Payments	171.7	182.2	(10.4)	-5.7%
Current Year Payments	23.0	26.0	(3.0)	-11.7%
Audit, P&I, Amended	22.1	31.9	(9.8)	-30.7%
Refunds	(116.5)	(136.9)	20.4	-14.9%
Refund Accrual Reversal	143.0	140.0	2.9	2.1%
Partnership Income Tax	6.8	6.8	(0.1)	-0.9%
Mineral Royalties	4.1	5.2	(1.0)	-19.9%
<b>Total</b>	<b>\$856.8</b>	<b>\$833.2</b>	<b>\$23.6</b>	<b>2.8%</b>

The chart below shows refunds booked in SABHRS in the month of February. FY 2017 refunds were lower than any year since 2007. According to staff at DOR, refunds are being held longer to ensure employer data matches before issuing refunds, and also to make sure that the fraud manager tool rolled out with the new processing software is operating correctly. In addition, the federal PATH Act of 2015 required the Internal Revenue Service to delay issuing refunds for the Earned Income Tax Credit and Additional Child Tax Credit until February 15 to allow for additional time to check for identity theft. The slowdown in federal refund activity is highlighted here: <http://www.taxprotoday.com/news/tax-credit-processing-delays-immigrant-fears-and-itin-changes-fuel-early-tax-filing-slowdown> Refunds are anticipated to return to a more normal level throughout March and April.



The LFD March update for individual income tax is above the three-year HJ 2 estimate by \$74.3 million, with LFD revenue models accounting for \$40.2 million of the difference. The remaining difference is due to the March IHS improved outlook for wage disbursements, interest rates, corporate profits and stock market growth, as well as updated taxpayer data from the Department of Revenue. The IHS March outlook for wage growth was up somewhat from the IHS February outlook, although a bit lower than the IHS January outlook.

## Property Tax

Property tax collections are below last year by \$1.8 million or 1.2%. In prior months, the decrease was much larger and likely caused by a lag in property tax bills. The current lag was caused by the need for adjustments from the NorthWestern Energy property tax settlement that lowered NorthWestern's market value from \$2.6 billion to \$2.4 billion.

The property tax estimate does not use IHS data, so the three-year decrease of \$1.4 million relative to HJ 2 is due to using LFD estimate models and updated information from the Department of Revenue.

## Corporation Income Tax

Corporation income tax collections through the end of February are 2.8% or \$2.2 million below this time in FY 2016. Lower estimated payments in FY 2017 have been partially offset by higher audits as shown in the adjacent table. Estimated payments typically account for about 80% of total corporation income tax revenue.

Corporation Income Tax (\$ Millions)				
Account	YTD 2017	YTD 2016	\$ Difference	% Difference
Corporation Tax	\$11.5	\$11.0	\$0.5	4.7%
Estimated Payments	60.3	69.1	(8.8)	-12.7%
Refunds	(12.1)	(13.2)	1.1	-8.5%
Refund Accrual Reversal	3.8	4.3	(0.5)	-12.1%
Audit, P&I, Amended	10.6	5.1	5.5	106.6%
<b>Total</b>	<b>\$74.2</b>	<b>\$76.3</b>	<b>(\$2.2)</b>	<b>-2.8%</b>

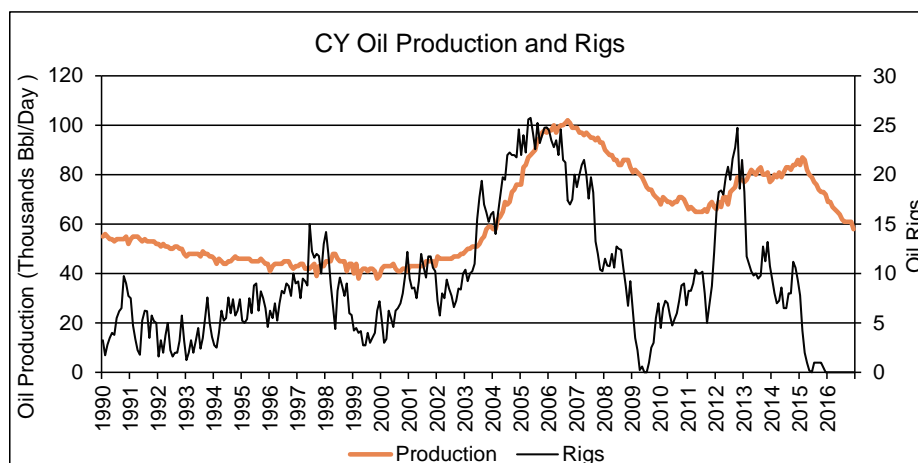
The LFD March update for corporation income tax is above the three-year HJ 2 estimate by \$47.4 million. The LFD revenue models account for \$34.6 million of the difference. The remaining difference is due to the March IHS improved outlook for median home price, which resulted in a higher estimate for financial sector tax liability, and higher oil price in 2017 which led to a higher forecast of manufacturing sector liability in that year.

## Vehicle Fees & Taxes

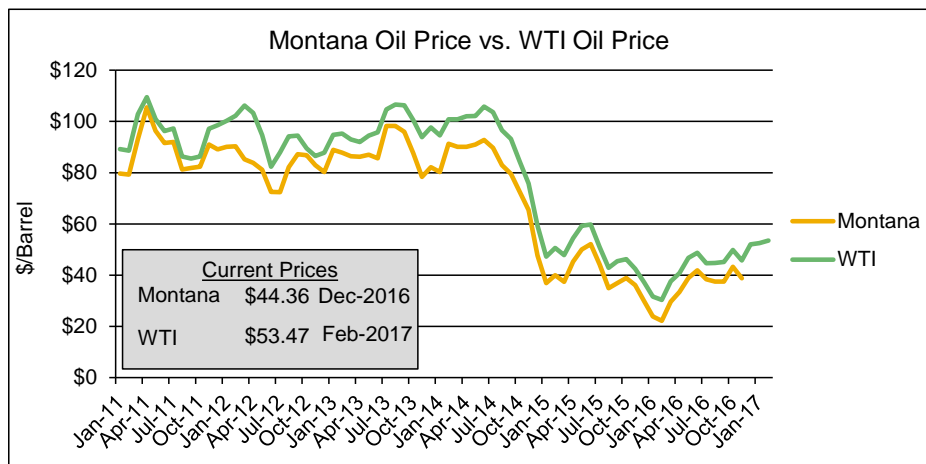
Eight months into FY 2017, vehicle taxes and fees are 6.7% or \$4.0 million above collections from last year at this time. In HJ 2, this source was expected to grow by 0.7%. There appears to be a timing issue between February and March revenue collections being posted to the accounting system, which should clear up by next month's report. The March IHS forecast had a small negative impact on the vehicle fees & taxes estimate, but primary reason for the three-year decrease of \$1.1 million relative to HJ 2 is using LFD estimate models.

## Oil & Natural Gas Production Tax

Through February, oil and gas production taxes are 2.9% or \$0.3 million below last year's collections at this time. This was expected as prices during the first quarter of FY 2016 were higher than those in the first quarter of FY 2017. Moving forward, however, tax collections are expected to exceed FY 2016 collections as prices for the remainder of FY 2017 should be above those seen for the same period in FY 2016.



As the previous chart shows, oil production has been declining since the beginning of 2015, as there has been at most one rig operating in the state since early 2015. The figure below shows Montana's historical oil price compared to West Texas Intermediate (WTI) oil price.



The LFD March update for oil & natural gas taxes is below the three-year HJ 2 amount by \$5.1 million. A reduction of \$7.7 million due to using LFD models is partially offset by a higher IHS outlook for oil price.

## Insurance Tax

Current insurance tax collections are 10.8% or \$3.4 million above FY 2016 through February. About a third of the increase is from the premiums insurance account, in which collections are growing 5.0% over FY 2016 through February. The remainder of the increase is due to strong growth in collections of fire marshal taxes. There should be about \$2.2 million of additional fire marshal tax in FY 2017, with a portion of the increase likely to be ongoing new revenue.

The LFD March update for insurance tax is above the three-year HJ 2 amount by \$10.4 million. A small portion—\$1.4 million—is due to using LFD modeling. Of the remaining \$9.0 million, about three-fourths is due to incorporating additional future fire premium taxes and the rest is due to an improved IHS outlook for consumer expenditures in the finance and insurance sector.

## Video Gambling Tax

Revenue from video gambling is currently \$0.6 million or 2.0% below collections from last year, and below the anticipated growth of 3.3% contained in HJ 2. The LFD March update for video gambling tax is below the three-year HJ 2 amount by \$7.2 million. Based on quarterly revenue collections and a literature review of gambling revenue across the U.S., the modeling for this source has been changed. The new model no longer relies on Montana personal income; instead, it is a time series model that incorporates Montana population.

## Lodging Facilities Sales Tax

Year-to-date lodging facilities sales tax collections are below FY 2016 by \$0.4 million or 3.2%, and below the 6.9% growth anticipated in HJ 2. The March IHS lower outlook for national consumer spending on accommodations had a small negative impact on the lodging facilities sales tax estimate, but primary cause of the \$5.5 million three-year decrease relative to HJ 2 is the use of the LFD revenue model for this source.

## TCA Interest Earnings

To date, TCA interest earnings are \$1.1 million or 57.2% above collections from one year ago. The March IHS higher outlook for short term interest rates coupled with revised LFD modeling designed to incorporate a lower anticipated daily cash balance resulted in a \$7.2 million three-year decrease relative to HJ 2.



## **Remaining Sources**

Revenue from the remaining sources was 5.7% above FY 2016 in aggregate, primarily due to timing. The LFD March update increased \$1.5 million relative to HJ 2. The change includes a reduction of \$1.0 million due to using LFD revenue models, with the March IHS data resulting in an increase of \$2.5 million over the three-year period.

## **Guarantee Fund**

The LFD March update for the guarantee fund is below the three-year HJ 2 amount by \$6.1 million. New information from the Board of Investments on the expected rate of return and updated administration costs from the Department of Natural Resources & Conservation explain the difference with respect to HJ 2.