



MONTANA LEGISLATIVE BRANCH

Legislative Fiscal Division

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Director
AMY CARLSON

DATE: January 21, 2019

TO: Sen. Scott Sales, Senate President
Rep. Greg Hertz, House Speaker
Sen. Roger Webb, Chair, Senate Tax Committee
Rep. Alan Redfield, Chair, House Tax Committee
Sen. Fred Thomas, Senate Majority Leader
Rep. Brad Tschida, House Majority Leader
Sen. Jon Sesso, Senate Minority Leader
Rep. Casey Schreiner, House Minority Leader

FROM: LFD Revenue Team

RE: General Fund Revenue Forecast Update #1

GENERAL FUND REVENUE SUMMARY

This is the first of the monthly revenue forecast updates throughout the 2019 Session designed to brief the legislature on recent economic trends and the corresponding outlook for the 2021 Biennium general fund revenue estimate. This update is based on actual revenue collections received through the end of December 2018, and updated national and Montana forecasts from IHS.

FY 2019 general fund revenues through the end of December are \$6.9 million or 0.6% above FY 2018 revenues through the same period. Note that total year-to-date growth of 0.6% is influenced by the timing of one-time-only transfers in FY 2018. When one-time-only transfers are excluded, the ongoing revenue is above last year by 6.1%, and above the anticipated growth of 3.4%. A portion of the 6.1% increase in ongoing revenue—about \$27 million—is due to a timing issue in property tax collections, which typically resolves by the end of January. In addition, income tax payment timing may or may not be reducing year-to-date collections, which should also be clearer by next month.

Two analyses of possible fiscal-year-end revenue collections based year-to-date revenue are provided in the appendix. However, given the significant variability between December and January individual income tax estimated payments and property tax remissions by counties to the state, the extrapolations are particularly variable until January collections are complete. Based on data through December, the median values suggest final revenue collections in the range of 0.1% below to 3.8% above HJ 2.

Forecast Update Based on New Data

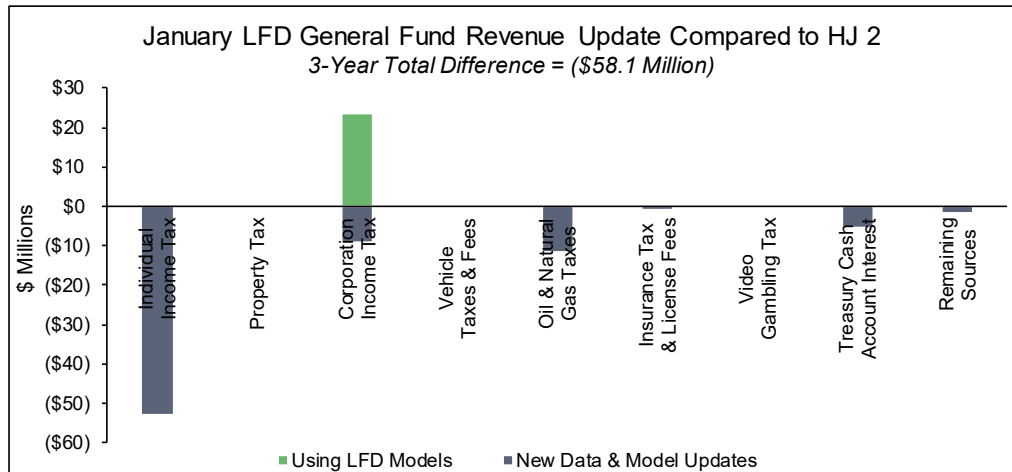
The January economic forecasts from IHS combined with LFD revenue models generates a general fund revenue forecast that is \$58.1 million lower than the official estimate in HJ 2 over the three-year forecast period. The table below shows the HJ 2 estimate and the LFD January update based on revised assumptions.

January LFD General Fund Revenue Estimate Update (\$ Millions)					
FY	HJ 2	January Update	\$ Difference	HJ 2 Growth	January Update Growth
2018	\$2,405.4	\$2,405.4			
2019	2,463.5	2,454.5	(\$9.1)	2.4%	2.0%
2020	2,513.6	2,483.8	(29.7)	2.0%	1.2%
2021	2,590.7	2,571.4	(19.3)	3.1%	3.5%
3-Yr	\$7,567.7	\$7,509.7	(\$58.1)		

The revised forecast from IHS incorporates the following key assumptions:

- Lower nominal GDP growth—from 5.4% in FY 2019 to 4.5% in FY 2020 and 4.2% in FY 2021—due to slowing global growth, a strong dollar, fading fiscal stimulus, tightening monetary policy, weaker stock prices, and the effects of recent tariffs; HJ 2 assumed 5.4%, 4.8%, and 4.3% respectively
- Lower oil prices: West Texas Intermediate (WTI) prices of \$58/bbl in FY 2019, \$61/bbl in FY 2020 and \$65/bbl in FY 2021, compared to the HJ 2 assumptions of \$71, \$71, and \$67 respectively
- Dampened outlook for Montana wage growth: 4.1% in FY 2019, 4.1% in FY 2020 and 4.4% in FY 2021, compared to the HJ 2 assumptions of 4.6%, 4.3%, and 4.5% respectively

The LFD January 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 was based on the LFD estimate with an adjustment to corporate income tax, most of the decrease in the LFD January update is due to the lower IHS economic outlook, with the remaining difference due to excluding the corporate tax adjustment.



January LFD Update Summary of Changes from HJ 2				
(\$ Millions)				
Revenue Source	FY 2019	FY 2020	FY 2021	3-Yr Total
Individual Income Tax	(\$8.4)	(\$22.7)	(\$21.9)	(\$53.1)
Property Tax	-	(0.0)	(0.1)	(0.1)
Corporation Income Tax	6.0	2.2	6.1	14.3
Vehicle Taxes & Fees	0.2	0.0	0.0	0.3
Oil & Natural Gas Taxes	(5.8)	(6.1)	0.2	(11.7)
Insurance Tax & License Fees	(0.0)	(0.4)	(0.4)	(0.9)
Video Gambling Tax	-	-	-	-
Treasury Cash Account Interest	(0.8)	(2.1)	(2.6)	(5.5)
Remaining Sources	(0.3)	(0.6)	(0.6)	(1.5)
General Fund Total	(9.1)	(29.7)	(19.3)	(58.1)
Guarantee Fund	4.9	0.1	0.1	5.0
General Fund & Guarantee Fund Total	(\$4.2)	(\$29.7)	(\$19.2)	(\$53.0)

NEXT STEPS

Updated revenue forecasts will be published monthly throughout the 2019 Session. The next report will be available in mid-February. Year-to-date analysis in February should give a clearer perspective on the outlook for FY 2019, since the timing issues with property tax and individual income tax collections will be corrected by the end of January.

In addition, new data will be available and incorporated into the LFD February 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 January
- Board of Oil & Gas production data
- Department of Revenue detailed collection data through January

YEAR-TO-DATE GENERAL FUND REVENUE

General Fund Revenue Monitoring Report							
(\$ Millions)							
Revenue Source	Actual FY 2018	HJ 2 FY 2019	HJ 2 Est. % Change	Dec FY 2018	Dec FY 2019	YTD Difference	YTD % Change
Largest Seven Sources							
Individual Income Tax	\$1,297.777	\$1,359.066	4.7%	\$710.439	\$741.702	\$31.263	4.4%
Property Tax	276.414	283.225	2.5%	115.890	139.010	23.119	19.9%
Corporation Tax	167.100	160.824	-3.8%	91.703	92.402	0.699	0.8%
Vehicle Taxes & Fees	109.540	111.525	1.8%	44.367	46.747	2.380	5.4%
Oil & Natural Gas Taxes	54.508	60.049	10.2%	-	-	-	
Insurance Tax	75.273	77.475	2.9%	25.365	29.936	4.571	18.0%
Video Gaming Tax	60.324	60.158	-0.3%	14.947	15.821	0.874	5.8%
Other Business Taxes							
Drivers License Fee	4.581	4.342	-5.2%	2.128	2.039	(0.089)	-4.2%
Investment Licenses	7.683	7.963	3.6%	0.844	0.895	0.051	6.0%
Lodging Facilities Sales Tax	24.091	25.218	4.7%	10.178	10.523	0.345	3.4%
Public Contractor's Tax	4.267	3.503	-17.9%	4.079	4.639	0.560	13.7%
Railroad Car Tax	3.649	3.492	-4.3%	3.341	3.076	(0.264)	-7.9%
Rental Car Sales Tax	3.719	3.730	0.3%	1.587	1.923	0.336	21.2%
Retail Telecom Excise Tax	13.726	12.889	-6.1%	3.546	3.419	(0.127)	-3.6%
Other Natural Resource Taxes							
Coal Severance Tax	14.107	13.555	-3.9%	3.978	3.971	(0.006)	-0.2%
Electrical Energy Tax	4.302	4.547	5.7%	1.130	0.888	(0.242)	-21.4%
Metal Mines Tax	6.291	6.749	7.3%	0.000	0.016	0.016	68591.6%
U.S. Mineral Leasing	20.139	20.934	3.9%	6.919	8.372	1.453	21.0%
Wholesale Energy Trans Tax	3.628	3.516	-3.1%	0.901	0.773	(0.128)	-14.2%
Other Interest Earnings							
Coal Trust Interest Earnings	17.938	17.088	-4.7%	7.083	7.139	0.056	0.8%
TCA Interest Earnings	10.888	21.514	97.6%	3.312	7.775	4.462	134.7%
Other Consumption Taxes							
Beer Tax	3.002	3.074	2.4%	1.325	1.359	0.034	2.5%
Cigarette Tax	27.755	27.313	-1.6%	13.380	14.298	0.918	6.9%
Liquor Excise Tax	21.007	22.884	8.9%	9.155	9.275	0.120	1.3%
Liquor Profits	12.200	12.900	5.7%	-	-	-	
Lottery Profits	10.699	11.510	7.6%	3.362	2.684	(0.678)	-20.2%
Tobacco Tax	6.058	6.273	3.6%	2.728	2.676	(0.052)	-1.9%
Wine Tax	2.446	2.461	0.6%	1.069	1.092	0.023	2.1%
Other Sources							
All Other Revenue	117.645	90.686	-22.9%	86.039	24.054	(61.985)	-72.0%
Highway Patrol Fines	3.754	3.907	4.1%	1.549	1.611	0.063	4.0%
Nursing Facilities Fee	4.405	4.275	-3.0%	1.108	1.055	(0.053)	-4.8%
Public Institution Reimbursement	13.754	13.887	1.0%	4.384	3.205	(1.179)	-26.9%
Tobacco Settlement	2.778	2.996	7.9%	0.006	0.337	0.331	5464.5%
Ongoing Revenue Subtotal	2,333.618	2,412.503	3.4%	1,107.799	1,175.917	68.117	6.1%
OTO Revenue & Transfers Subtotal	71.829	51.024		68.041	6.793	(61.248)	
Grand Total	\$2,405.447	\$2,463.527	2.4%	\$1,175.841	\$1,182.710	\$6.869	0.6%

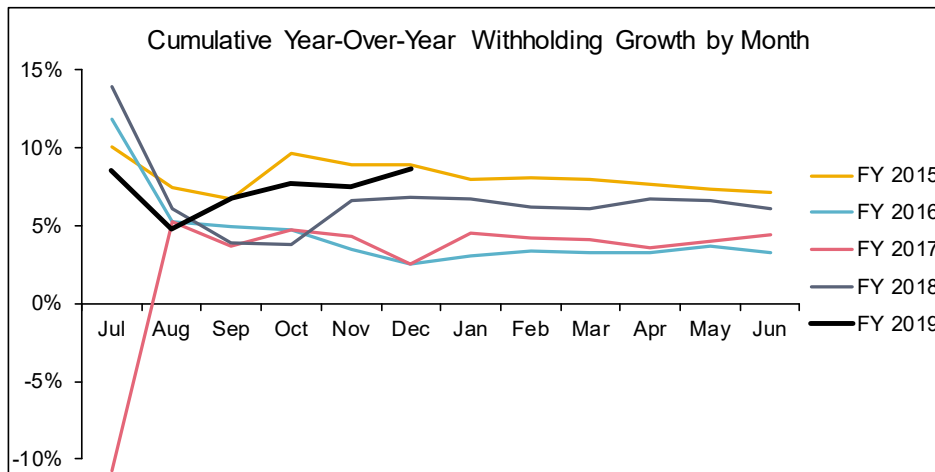
LFD JANUARY REVENUE UPDATE DETAIL BY MAJOR SOURCE

Individual Income Tax

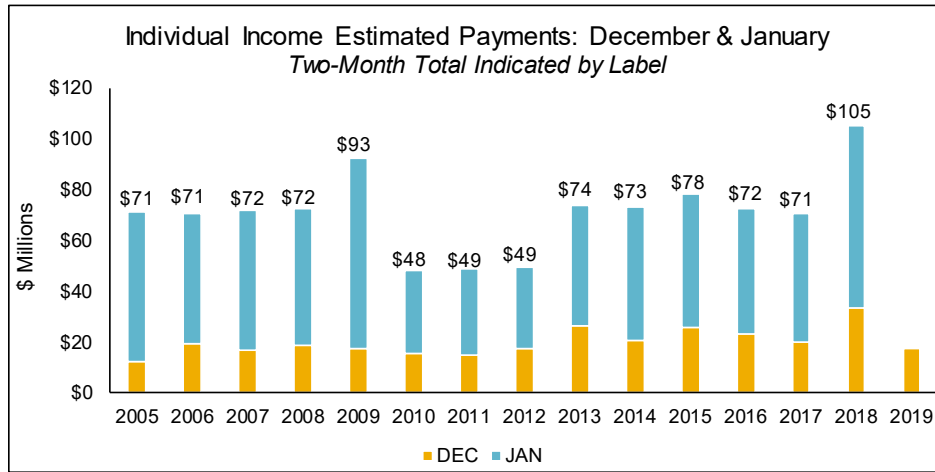
Individual income tax collections through the end of December are \$31.3 million or 4.4% above the year-to-date collections in FY 2018, but below the 4.7% growth anticipated in HJ 2. The year-over-year increase is primarily due to strong withholding growth, which more than offset the decline in December estimated payments.

Individual Income Tax				
(\$ Millions)				
	YTD 2019	YTD 2018	\$ Difference	% Difference
Withholding	\$494.5	\$455.0	\$39.5	8.7%
Estimated Payments	125.6	135.3	(9.7)	-7.2%
Current Year Payments	19.9	19.5	0.4	1.9%
Audit, P&I, Amended	17.8	16.6	1.2	7.4%
Refunds	(86.3)	(77.8)	(8.5)	11.0%
Refund Accrual Reversal	161.9	153.2	8.7	5.7%
Partnership Income Tax	5.6	6.4	(0.8)	-12.5%
Mineral Royalties	2.6	2.1	0.5	22.0%
Total	\$741.7	\$710.4	\$31.3	4.4%

Withholding accounts for over two-thirds of individual income tax and about one-third of total general fund revenue, and is continuing to increase year-over-year growth compared to FY 2018 collections. As shown in the following chart, withholding growth tends to be relatively variable in the first half of the year, but stabilizes by February, allowing for potential assessments of overall fiscal year withholding growth.



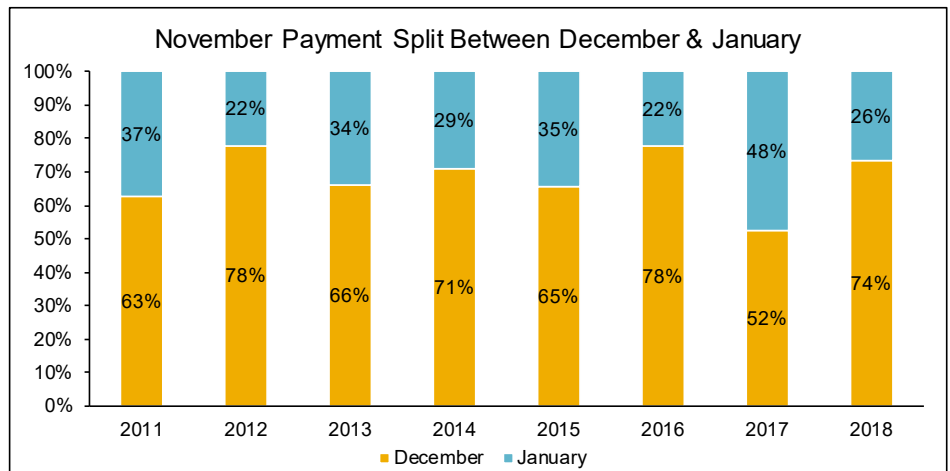
The timing of estimated payments can fluctuate between December and January, so next month's report should clarify expectations for FY 2019. The decline relative to the unusually high combined December and January estimated payments of last year—potentially due to advanced payments made at the end of CY 2017 by taxpayers in response to the new federal cap on state and local tax deductions starting in CY 2018—is not surprising. However, last month's estimated payments were below any December estimate payments amount since FY 2012, as illustrated in the following chart. Estimated payments will be monitored closely to determine whether timing appears to be the primary driver of the decline, or if taxpayers appear to be adjusting their income expectations.



The LFD January update for individual income tax is below the three-year HJ 2 estimate by \$53.1 million. The difference is primarily due to the January IHS lower outlook for wage disbursements, interest rates, corporate profits and stock market growth. Note that the sunset of the charitable endowment credit has been included, which results in an increase in FY 2021 of \$3.5 million.

Property Tax

Property tax collections are above last year by \$23.1 million or 19.9%. The strong growth is likely due to a timing issue that occurs from the November payment being booked partially in December and partially in January. This uneven split of the November payment being booked in either December or January in past years is shown in the following chart. Property tax is anticipated to come in close to the estimate in HJ 2.



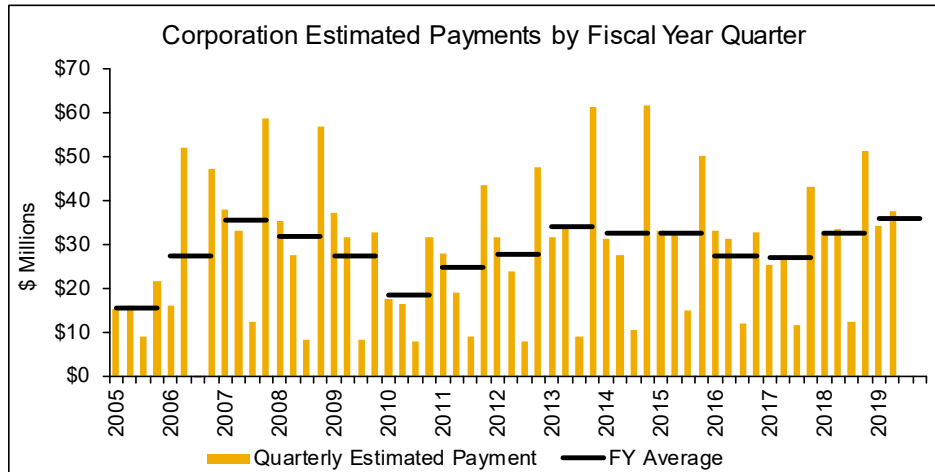
The property tax estimate does not use IHS data, so the three-year decrease of \$0.1 million relative to HJ 2 is due to small updates in the LFD estimate models.

Corporate Income Tax

Corporate income tax collections through the end of December are 0.8% or \$0.7 million above this time in FY 2018. As the adjacent chart shows, higher corporation tax payments in FY 2018 were entirely offset by increases across all other accounts in FY 2019. Estimated payments, the main driver of corporation income tax, showed strong growth of 8.9%.

Corporation Income Tax				
(\$ Millions)				
Account	YTD 2019	YTD 2018	\$ Difference	% Difference
Corporation Tax	\$12.7	\$26.2	(\$13.4)	-51.3%
Estimated Payments	71.5	65.7	5.8	8.9%
Refunds	(4.4)	(5.4)	1.0	-17.7%
Refund Accrual Reversal	4.9	3.3	1.6	46.7%
Audit, P&I, Amended	7.7	1.9	5.8	307.2%
Total	\$92.4	\$91.7	\$0.7	0.8%

The chart below shows that estimated payments in the first two quarters of FY 2019 are above the estimated payments collected in recent years. Estimated payments typically make up 80% of total corporation income tax collections, so if this strong growth continues this source is likely to end up above the HJ 2 estimate.



The LFD January update for corporation income tax is above the three-year HJ 2 estimate by \$14.3 million. The LFD revenue models do not include the \$23.5 million negative adjustment related to federal tax reform that was included in HJ 2; however, the increase was offset by the lower IHS outlook, which reduced the three-year estimate by \$9.2 million.

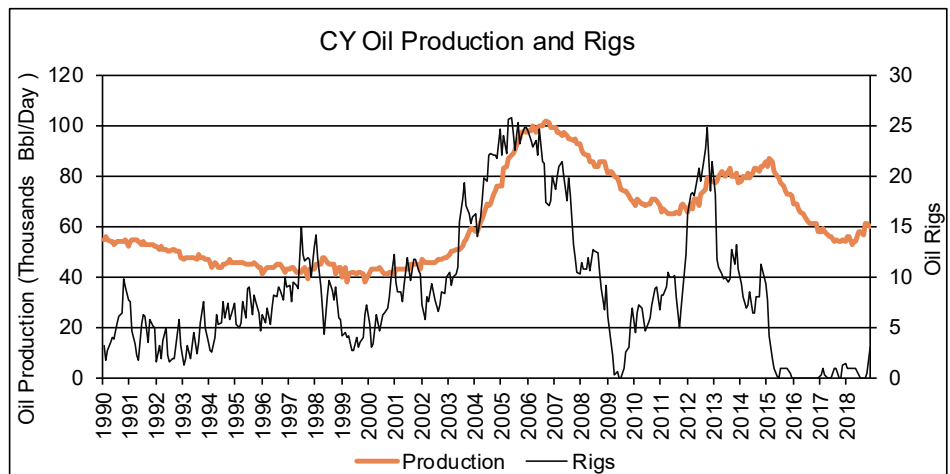
Vehicle Fees & Taxes

Six months into FY 2019, vehicle taxes and fees are 5.4% or \$2.4 million above collections last year. In HJ 2, this source was expected to grow by 1.8%. The increase is driven by a year-to-date increase in light vehicle registrations. It will be interesting to see if this increase continues throughout the fiscal year or if it is simply abnormal timing.

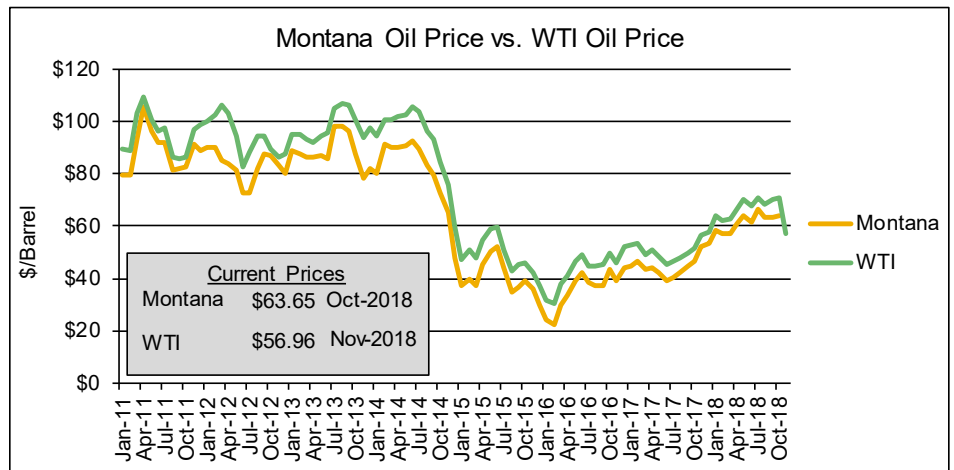
The January IHS forecast increased the vehicle fees & taxes estimate by \$0.3 million over the three years. The difference was driven by an increase in the estimate of new car sales in Montana for FY 2019.

Oil & Natural Gas Production Tax

Oil and natural gas production tax collections currently shows no data. This is expected due to the statutory requirement of when taxes are due and the time allowed for the Department of Revenue to determine the distribution of taxes to local governments. Known price and production data suggests that collections for the first quarter of FY 2019 will be larger than FY 2018.



As the previous chart shows, oil production had been declining since the beginning of 2015, as there was at most two rigs operating in the state since early 2015. However, production has increased since the summer of 2018 as up to four rigs moved into the area for the second half of calendar 2018. The increased activity was likely spurred by increased prices, shown below.



The LFD January update for oil & natural gas taxes is below the three-year HJ 2 amount by \$11.7 million. The decrease is due to revised oil prices by IHS. Specifically, the IHS outlook for West Texas Intermediate oil price has been revised downward by \$13/bbl in FY 2019, \$10/bbl in FY 2020, and \$2/bbl in FY 2021.

Insurance Tax

Current insurance tax collections are 18.0% or \$4.6 million above FY 2018 through December, and well above the 2.9% growth anticipated in HJ 2. This appears to be a timing issue, as year-to-date insurance premiums tax collections are at similar levels to FY 2016 and FY 2017. Total collections at this time in FY 2018 were abnormally low and later increased. Insurance premiums tax accounts for over 80% of total insurance tax, and research is ongoing with the State Auditor’s Office to determine whether the increase in insurance premiums tax collections is due to timing or an increase in policies written.

The LFD January update for insurance tax is below the three-year HJ 2 amount by \$0.9 million, primarily due to the reduced IHS outlook for consumer expenditures in the finance and insurance sector.

Video Gambling Tax

Revenue from video gambling is currently \$0.9 million or 5.8% above collections from last year. This source was expected to remain flat in HJ 2. The video gambling tax estimate does not use IHS data, so the January IHS forecast had no impact on the estimate.

TCA Interest Earnings

Treasury cash account interest earnings are \$4.5 million or 134.7% above collections last year at this time, and above the HJ 2 anticipated growth of 97.6%. The increase has been driven by the continued rise in short-term interest rates. The January IHS update decreased the estimate by \$5.5 million over the three-year period, due to lower expectations for short-term interest rates.

Remaining Sources

Revenue from the remaining sources, excluding legislatively authorized transfers and one-time-only revenue, was 0.1% above FY 2018. The January IHS forecast resulted in very small changes to most of the remaining sources. In aggregate, the new data resulted in a decrease of \$1.5 million over the three-year period.

Guarantee Fund

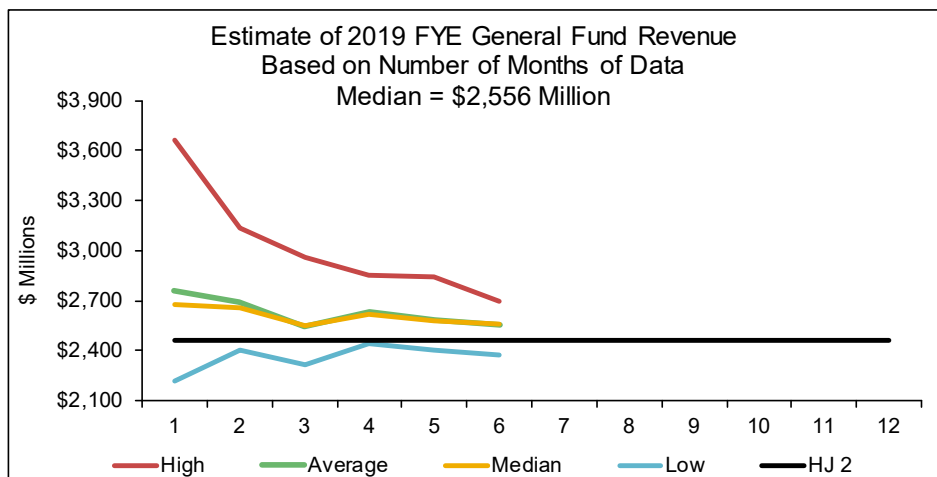
The LFD January update for the guarantee fund is above the three-year HJ 2 amount by \$5.0 million. The increase is due to the inclusion of \$4.8 million in Special Session Transfers to the guarantee Fund in FY 2019 that were not included in HJ 2.

APPENDIX

As noted at the beginning of this report, the two analyses of possible fiscal-year-end revenue collections based year-to-date revenue produce different results. After January collections are complete, the two independent analyses should produce more similar results. Based on data through December, the median values suggest final revenue collections in the range of 0.1% below to 3.8% above HJ 2.

Year-to-Date Relative to Historical Collection 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 2019 are calculated using various year-to-date percentages—minimum, maximum, median and average—since FY 2002. The results are shown in the graph below. Based on collections through the end of November with a downward adjustment in property tax of \$27 million, the difference between the high and low amounts is about \$327 million, with the average and median values above the HJ 2 estimate.

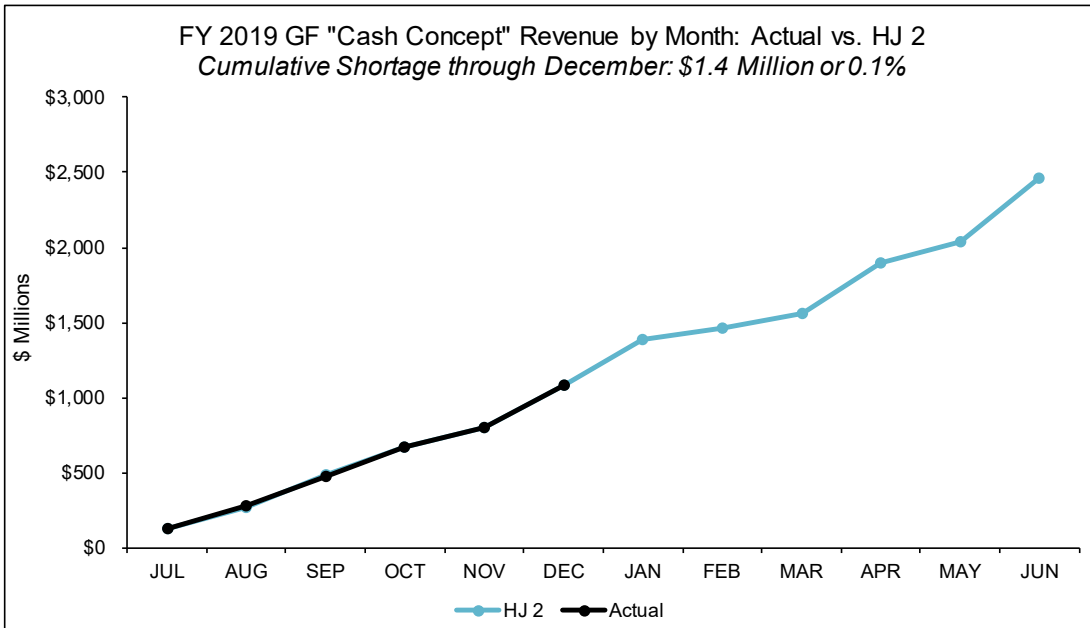


Potential total general fund collections range from a low of \$2,372 million to a high of \$2,699 million, with median and average values of \$2,556 million, or 3.8% above HJ 2. The FY 2019 forecast for total general fund in HJ 2 is \$2,464 million.

Cash Flow Model

The monthly cash flow model is based on state accounting (SABHRS) revenue data by month from FY 2002 to FY 2018, with accruals and subsequent accrual reversals removed. The top seven revenue sources and general fund transfers are modeled separately, with the remaining sources estimated as a group.

The chart below shows modeled cumulative HJ 2 by month with the blue line, and actual collections with the black line. Through December, the cash concept model suggests general fund revenue is below what would be expected based on the official revenue estimate by \$1.4 million or 0.1%. If revenue continues to be below HJ 2 by 0.1% through FY 2019, final collections could be \$3.3 million lower than expected.



Individual income tax has the largest difference with respect to the estimate in HJ 2; based on the cash flow model, individual income tax through December is \$20.2 million below the HJ 2 estimate.

