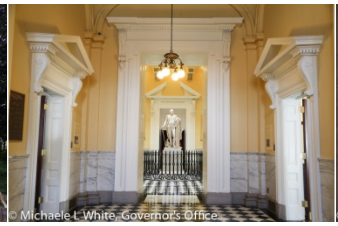
Revenue Forecast



The Commonwealth's total revenue consists of two types of resources: the general fund and nongeneral funds. About half of state revenues are "nongeneral funds," or funds earmarked by law for specific purposes. For example: motor vehicle sales and motor fuel taxes are earmarked by law for transportation programs; students' tuition and other fees support higher education, and federal grants are designated for specific activities.

General fund revenues are derived from general taxes paid by citizens and businesses in Virginia. Since general fund revenue is not dedicated to any particular purpose and can be used for a variety of government programs, these are the funds that the Governor and the General Assembly have the most discretion to spend.

General fund revenues can primarily be attributed to five major revenue sources. The two largest sources are the individual income tax and the sales and use tax. Other major revenue sources are corporate income taxes, wills, suits, deeds, and contract fees, and taxes on insurance company premiums. Miscellaneous taxes and other revenues also contribute to the general fund.

FY 2015 revenue collections rebound smartly

In FY 2015, total general fund revenues rose 8.1 percent to $17,735.6 million, exceeding the official forecast (4.7 percent growth) by $549.6 million. Adjusting for the accelerated sales tax program, total revenues rose 7.9 percent, ahead of the economic-base forecast of 4.5 percent growth.

All major sources except the insurance premiums tax and corporate income tax contributed to the surplus, however, collections of individual nonwithholding and withholding accounted for most of the surplus in FY 2015. Collections in nonwithholding were $316.4 million above the estimate, a variance of 11.6 percent. Payroll withholding finished the year $140.4 million above the estimate, a 1.3 percent variance. Individual refunds were $55.5 million lower than forecast, a net positive for the Commonwealth. Wills, suits and deeds, mainly recordation taxes, exceeded its forecast by $28.0 million. Sales tax collections also contributed $17.6 million to the surplus. Payroll withholding and sales tax collections, 83 percent of total revenues and closely related to economic activity, finished a combined 1.1 percent from forecast. Only two major sources failed to reach expectations: corporate income taxes were $9.0 million short of the forecast, and receipts of insurance premiums taxes fell $19.9 million short of the estimate. Collectively, the five major sources ended the year $529.2 million ahead of the forecast (3.2 percent variance). Also, collections of miscellaneous taxes and other revenues were $20.5 million ahead of the forecast in FY 2015 (3.0 percent variance).

General fund revenue expected to show below-trend growth over the forecast horizon

The general fund revenue forecast for FY 2016 through FY 2018 includes slightly below-trend growth that appears to be the new norm for Virginia's economy.

The General Fund Forecast for FY 2016 through FY 2018				
	Actual 2015	**Forecast 2016**	**Forecast 2017**	**Forecast 2017**
Corporate income	$831.9	$752.8	$778.0	$724.9
Individual income	12,328.7	12,778.0	13,162.4	13,753.2
Insurance premiums	300.6	317.7	330.6	345.3
State sales & uses	3,235.4	3,397.7	3,528.9	3,663.1
Wills, suits, deeds & contract Fees	346.3	373.0	379.4	379.4
Miscellaneous	692.7	689.7	681.1	685.5
Total revenues	**$17,735.6**	**$18,308.9**	**$18,860.3**	**$19,551.4**
ABC profits	$83.3	$80.2	$78.9	$79.5
Sales Tax (0.25%)	352.4	370.0	388.2	401.7
Transfers per the Appropriations Act	198.2	118.7	103.0	103.0
Total transfers	**$633.9**	**$568.9**	**$570.1**	**$584.2**
Total general fund	**$18,369.5**	**$18,877.8**	**$19,430.4**	**$20,135.6**

*Dollars in millions. Excludes balances available for appropriation. Figures may not add due to rounding. Source: Virginia Department of Taxation

Forecast for the major general fund revenue sources

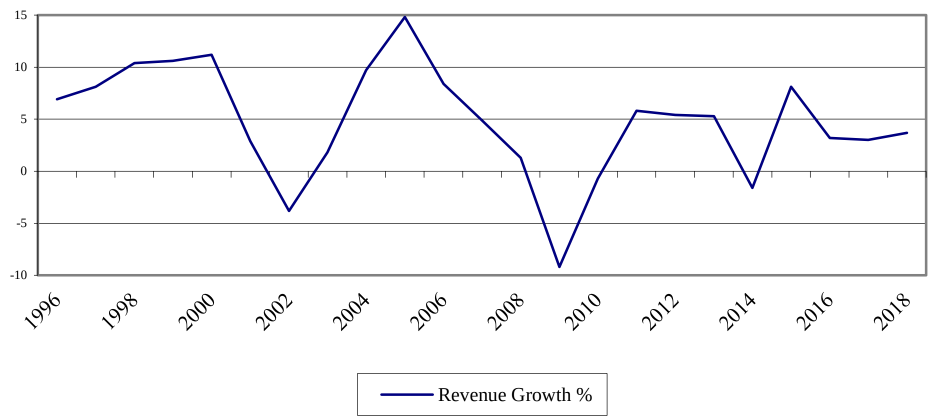
For each of the major categories of general fund revenue, the following describes the actual performance in FY 2015 and the estimate over the forecast horizon.

Individual income taxes

Over 90 percent of the surplus in FY 2015 was attributable to individual income taxes. Collections of net individual income taxes (69 percent of total revenues) rose 9.6 percent in FY 2015, ahead of the annual forecast of 5.0 percent growth. Receipts of $12,328.7 million were $512.4 million above the official estimate, a variance of 4.3 percent from the forecast. Both withholding and nonwithholding exceeded their estimates, with nonwithholding accounting for the bulk of the surplus. In addition, refunds were lower than expected.

The outlook for net individual income taxes in FY 2016 has been revised upward from the official forecast by $558.3 million for growth of 3.6 percent. Collections in this source are predicted to increase 3.0 percent in FY 2017 and 4.5 percent in FY 2018.

General Fund Revenue Growth Remains Below-Trend



Sales and use taxes

Collections of sales and use taxes (19 percent of total revenues) were $3,235.4 million in FY 2015, $17.6 million above the forecast, a variance of 0.5 percent. Collections rose 5.5 percent for the year compared with the forecast of 4.9 percent growth. Adjusting for accelerated sales tax payments received in June, sales tax collections grew 4.9 percent in FY 2015, compared with the economic-base forecast of a 3.9 percent increase.

The sales tax revenue model is based on a direct relationship with total personal income in Virginia. The November standard forecast increases sales tax collections by $74.6 million in FY 2016 for growth of 5.0 percent. Growth in this source is expected to be 3.9 percent in FY 2017, and 3.8 percent in FY 2018.

Corporate income taxes

Corporate income tax collections (5 percent of total revenues), historically the most volatile revenue source, fell short of the forecast. Collections of $831.9 million were $9.0 million below expectations, a forecast variance of 1.1 percent. The fiscal year increase of 9.8 percent trailed the forecast of 11.0 percent growth.

The corporate revenue model considers gross payments and refunds separately. Gross payments are modeled as a function of Virginia specific pre-tax corporate profits and the S&P 500 index. The November standard forecast reduces corporate income tax collections by $67.9 million from the official forecast in FY 2016. Collections are expected to fall by 9.5 percent in FY 2016, rise 3.3 percent in 2017, then fall 6.8 percent in FY 2018.

Insurance company premiums taxes

Another major source to see a deficit, collections of taxes on the premiums of insurance companies (2 percent of total revenues) were $300.6 million in FY 2015 – $19.9 million below the annual estimate. The decline of 6.2 percent trailed the annual estimate of zero growth.

In the November standard forecast, insurance premiums growth is reduced from 8.7 percent to 5.7 percent in FY 2016, a decrease of $9.1 million. The model calls for a 4.0 percent increase in FY 2017 and a 4.5 percent increase in FY 2018.

Wills, suits, deeds & contract fees

Wills, Suits, Deeds, and Contract Fees (2 percent of total revenues), of which the primary component is the recordation tax, were well ahead of the forecast in FY 2015. The recovering housing market boosted recordation receipts and caused a surplus in this source of $28.0 million, a variance of 8.8 percent. Collections finished the year at $346.3 million, an 11.4 percent increase from FY 2014 and well above the official forecast of 2.4 percent growth.

The revenue model for wills, suits, deeds and contracts is based on mortgage originations and median home prices in Virginia, along with the yield on 30-year treasury bonds. The outlook for recordation taxes drives the other components of this source.

Collections in this source have grown at double-digit rates in ten out of the last eleven months. The November standard forecast for this source is 7.7 percent growth in FY 2016, an upward revision of $54.7 million. The estimate assumes growth of 1.7 percent in FY 2017 followed by no growth over the forecast horizon.

59.2 percent of state revenue is nongeneral fund

Although most public attention is focused on general fund revenue, almost 60 percent of all revenue in the state budget consists of nongeneral funds that are earmarked by law for specific purposes.

Nongeneral fund revenue collections decreased by 1.6 percent in 2015, and are expected to increase by 25.1 percent in 2016, 2.2 percent in 2017, and 1.8 percent in 2018. Nongeneral funds are 59.2 percent of total state revenue during the 2016-2018 biennium.

Federal grants and other contracts

Federal grants are the largest single source of nongeneral fund revenue, about 37 percent of the total. Frequently these grants do not come to the state as simple cash transfers. The federal government mandates many program requirements as conditions of the grants, and often states must provide matching funds. The Medicaid program for indigent health care is an example of a federal entitlement program that requires a state contribution.

In 2015, federal grants and other contracts totaled $9.3 billion. This source is projected to increase by 10.1 percent to $10.2 billion in 2016, decrease by 0.5 percent in 2017 and increase by 0.3 percent in 2018, resulting in projection of $10.2 billion for each year.

Institutional revenue

The second largest class of nongeneral fund revenue is institutional revenue. The principle sources of this revenue are patient fees at teaching hospitals and mental health institutions as well as tuition and fees paid by students at institutions of higher education. In 2016, institutional revenue collections are expected to be $7.0 billion or about 25.8 percent of all nongeneral fund revenue. Institutional revenues are projected to grow to $7.3 billion in 2017 and to $7.6 billion in 2018. Overall institutional revenues are projected to be 26.8 percent of all nongeneral fund revenues over the 2016-2018 biennium. These growth rates reflect the higher cost of services provided by these institutions.

Transportation Fund

State transportation revenue comes from several sources including the motor vehicle fuels tax, the motor vehicle sales and use tax, road taxes, vehicle license fees, state sales tax, interest earnings, and other miscellaneous taxes and fees. Money in this fund is used to support highway construction and maintenance and operating costs. Federal, local, and toll revenues are also used to finance transportation programs.

Fiscal year 2015 total transportation revenues (state taxes and fees) totaled over $3.1 billion, an increase of $330.9 million over last year. Revenue collections grew by 11.8 percent as compared to the official forecast of a 10.0 percent increase, resulting in a forecast variance of 1.6 percent.

For FY 2016 and FY 2017, total fund revenues from state sources, including revenues attributable to HB2313 (2015), are expected to be close to $3.4 billion in FY 2016 and over $3.4 billion in FY 2017. Growth is expected to be 7.3 percent, 2.7 percent, and 2.4 percent in FY 2016 through FY 2018, respectively.

Unemployment insurance fund

Unemployment insurance tax collections rise and fall with trends in the economy.

Unemployment Insurance tax collections for 2015 were above the projection by $0.7 million, or 0.1 percent. Projected interest revenues were $1.7 million, or 15.7 percent, above the forecast because benefit payments were below the forecast. Unemployment tax collections are expected to decrease to $581.0 million in 2016, $526.9 million in 2017 and $504.3 million in 2018.

Master Tobacco Settlement Agreement Funds

The Master Settlement Agreement (MSA) was signed between the major participating cigarette manufacturers and 45 states, the District of Columbia, and five United States' territories on November 23, 1998. The settlement agreement releases participating manufacturers from past, present, and future smoking-related claims of the states in return for an annual cash payment to the states in perpetuity. These payments are to be adjusted over time for several factors, including inflation and changes in volume of domestic cigarette shipments.

The Commonwealth's plan for the use of MSA funds has three elements. First, legislation passed by the 1999 General Assembly (Chapter 880, 1999 Acts of Assembly) earmarked 60 percent of the allocation in two separate trust funds. The Tobacco Indemnification and Community Revitalization Fund receives 50 percent of the MSA allocation. This share is used to compensate tobacco growers and tobacco quota holders for the economic loss resulting from quota loss or elimination and to promote economic growth and development in tobacco-dependent communities in the Southside and Southwest regions of the state. Recently, the annual amount received by this Fund was securitized and turned into an endowment. Thus, the Fund now receives earnings on this endowment.

The Virginia Tobacco Settlement Fund receives the next 8.5 percent of the MSA allocation for the purposes of preventing tobacco use by minors and reducing childhood obesity. Programs targeted at minors include but are not limited educational and awareness programs.

The final portion of the allocation (41.5 percent) goes to the Virginia Health Care Fund. This Fund can be used to pay for various health care costs faced by the Commonwealth, including the Medicaid program for indigent health care.

For 2016, 2017 and 2018, it is anticipated that the Tobacco Indemnification and Community Revitalization Fund may expend up to 10.0 percent of the endowment, an amount estimated at $70.3 million each year. The Foundation for Healthy Youth is anticipated to take in $9.3 million each year. The Virginia Health Care Fund will receive $48.0 million in 2016, $47.5 million in 2017, and $47.0 million in 2018.

Nongeneral Fund Forecast for the 2016-2018 Biennium

	Actual FY 2015	Forecast FY 2016	Forecast FY 2017	Forecast FY 2018
Motor vehicle fuel tax	$762.0	$924.6	$971.4	$973.8
Unemployment compensation payroll tax	$679.9	$581.0	$526.9	$504.3
Special highway tax from sales tax	$691.8	$876.1	$924.5	$956.8
Motor vehicle sales tax and use tax	$854.5	$893.8	$927.2	$940.7
Other taxes	$1,530.5	$1,505.0	$1,564.5	$1,590.8
Rights and privileges	$1,038.1	$1,007.3	$1,055.7	$1,066.5
Sale of property and commodities	$1,514.4	$1,497.7	$1,525.1	$1,547.3
Assessment & receipts for special	$592.9	$630.1	$661.7	$695.0
Services				
Institutional revenue**	$2,827.7	$6,962.9	$7,319.9	$7,617.5
Interest dividends and rents	$172.3	$181.7	$195.2	$213.1
Federal grants and contracts	$9,298.9	$10,238.6	$10,186.1	$10,215.3
Master Tobacco Settlement Agreement	$57.6	$127.7	$127.2	$126.7
Funds				
Other Revenue	$1,635.9	$1,579.0	$1,605.0	$1,640.1
Total	**$21,656.6**	**$27,005.2**	**$27,590.4**	**$28,087.9**

*Based on December 2015 forecast. Dollars in millions. Figures may not add due to rounding. Total excludes balances and bond proceeds available for appropriation, as well as Literary Fund transactions, and internal service funds.

Source: Department of Planning and Budget, based on data submitted by agencies.

**Per the Management Agreement between the tier 3 schools and the Commonwealth as set forth in Chapters 933 and 943 of the 2006 Acts of Assembly, the tier 3 schools are not required to report actual revenue collections in CARS.