Like the Phoenix, the Estimate will Rise

by Stuart Greenfield, Ph.D.

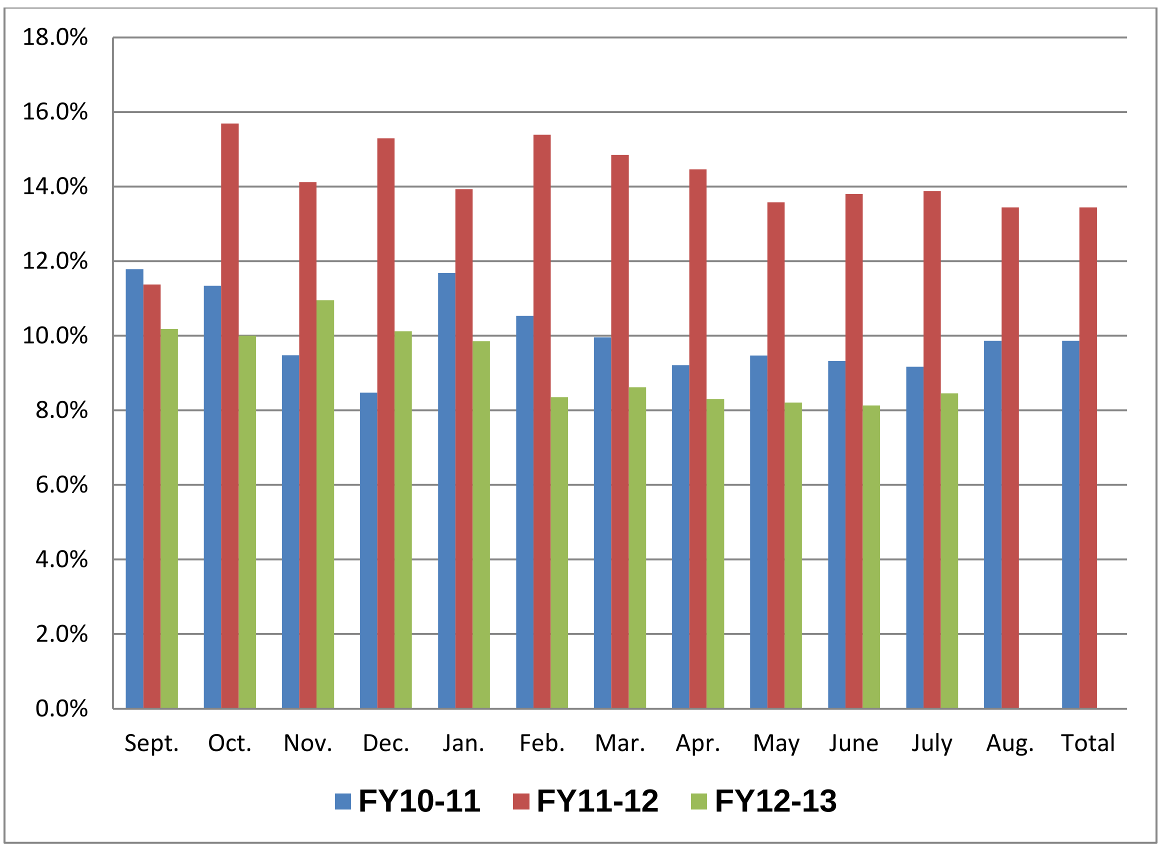
As our legislators egressed from Austin after the 3rd Called Session of the 83rd Legislature, they were able to provide schemes to provide additional funding for water and for transportation. Not wanting to appropriate funds that are/would be available, our legislators made a principled decision and will allow voters to decide whether to fund these undertakings. I'm quite sure when the next Profiles in Courage Awards are announced members of the 83rd Legislature will be front and to the right.

It now appears that with Comptroller Combs announcement of $900 million in additional severance tax collections for FY13, the estimate for total tax collections for FY13 will be within 1 percent of actual FY13 tax collections. One must commend the Revenue Estimating staff at the Comptroller's Office for their spot-on tax estimate for FY13. While the current year was increased, there was no change in the estimate for the FY14-15 biennium.

Before the revised severance tax estimate, state tax collections were increasing at a rate 50 percent greater than in the Biennial Revenue Estimate (BRE), 8.5 percent compared to 5.4 percent in the January BRE. With the $900 million increase in severance tax collections, the differential is now only 15 percent. Non-severance tax collections will be around $300 million more than in the current estimate, while the severance tax estimate should have been increased by $1 billion. This will result in both the ending cash balance and the transfer to the Rainy Day Fund being more than the current estimate provides.

As show in Figure 1 below, the year-to-date increase in tax collections continues to exceed the growth in the current estimate (8.5 percent v. 7.4 percent). While the current rate of growth is 5 percent less than the growth rate

Figure 1: Cumulative YTD Growth in Tax Collections, various fiscal years



(13.4 percent) in tax revenue collections between FY12 and FY13, this decline in the growth rate in tax collections will increase substantially for FY14. According to the current estimate, the growth in tax collections (Table 1, below) will decline by over 100 percent, from 8.5 percent (FY13) to -0.1 (FY14). Were the current rate of increase for each tax reduced by half, tax collections in FY14 would be $2 billion more than in the current estimate. Should growth rates continue at their current rate, tax collections in FY14 would be $4 billion more than in the current estimate. This would translate to an additional $2 billion more in FY15 tax collections assuming no change in the growth rate in tax collections between FY14 and FY15.

With the significant increase in tax collections for this year, the higher tax base from FY13 along w/ a more precise estimate for FY14, there should be an increase in both the certifiable balance for FY14-15 and the RDF transfer. The certifiable balance for FY14-15 should be increased by $7.5 billion, while the transfer to the RDF should be $1.0 billion more than the current estimate. One would expect these changes to appear in the Comptroller's certification estimate, which will be realized in December.

Table 1: Growth Rates, All Funds Tax Collections by Major Tax, FY12 through FY15

	FY12-13 YTD	***FY12-13 BRE***	***FY13-14 BRE***	***FY14-15 BRE***
Sales Tax	7.8%	8.0%	2.4%	5.8%
Motor Vehicle Sales and Rental Taxes	9.8%	5.2%	4.4%	4.2%
Motor Fuel Taxes	1.7%	3.9%	-2.2%	3.8%
Franchise Tax	6.4%	2.5%	1.7%	0.4%
Insurance Taxes	16.7%	5.7%	7.5%	3.2%
Natural Gas Production Tax	-7.0%	-8.0%	-16.3%	10.9%
Cigarette and Tobacco Taxes	6.9%	9.1%	-10.2%	7.7%
Alcoholic Beverages Taxes	4.8%	6.1%	0.2%	6.2%
Oil Production and Regulation Taxes	41.4%	36.7%	-20.2%	0.6%
Inheritance Tax				
Utility Taxes	-3.0%	-1.6%	1.7%	2.0%
Hotel Occupancy Tax	9.8%	5.2%	4.8%	4.9%
Other Taxes	-0.8%	-8.2%	-0.2%	1.1%
Total Tax Collections	**8.5%**	**7.4%**	**-0.1%**	**5.4%**

Source: Comptroller of Public Accounts

Compared to the estimate for FY12, the estimate for this fiscal year should be considered spot-on. The $3.4 billion increase in year-to-date tax collections is primarily due to the increase in sales tax ($1.7 billion) and in the oil production tax ($800 million). With the substantial increase in the oil production tax and reduced decline in the natural gas tax, the transfer to the Economic Stabilization Fund (the Rainy Day Fund or ESF) is likely to be around $2.4 billion, an amount now recognized by the Comptroller.

While the Comptroller did increase the estimate for severance tax collections for FY13, the estimate for total tax collections in FY13 will be about $500 less than actual collections. This results from increases in Motor Vehicle, Franchise, and Insurance tax collections. While making this assertion is a no-brainer, one month out, non-severance tax collections have shown this trend since the release of the estimate in January.

As one should note from Table 1 above, the estimated growth rates in almost every tax in FY14 are **atrocious**. In fact, one might ask whether any professional or even semi-professional economist were involved in the process. Given the recent increase in severance tax collections for FY13, the Comptroller's estimate for total tax collections in FY14 is now negative. Is the "great recession" of 2008 returning, not in any of the forecasts I'm aware of, e.g., http://tinyurl.com/mr2doc4 and http://tinyurl.com/l6nb3nh. Also, according to the Perryman Group, oil production from shale will continue to experience substantial increases, http://tinyurl.com/lbs9ljr. In fact, "the vast amounts of recoverable oil and natural gas will make the Cline Shale go down in history as the largest shale play ever." While one analyst considers Texas, the new Kingdom, **http://tinyurl.com/ka639ae**, most agree Texas would be a major OPEC producer, **http://tinyurl.com/lx3ogkk**.

Were the estimate to follow the historical relationship between the state's economy and state revenue one should expect the "estimated ending certification balance" for FY15 to be around $108 billion, an increase of over $7.5 billion from the current estimate. The transfer to the Rainy Day Fund should be $1.0 billion more, resulting in a balance of over $9 billion in FY15 (after accounting for the $3.9 billion appropriated from the fund in FY13).

Table 2 shows that All Funds Total Net Revenue through July of FY13 is $1.7 billion more than collected in FY12. The primary reason that the increase in total revenue is less than the increase in the BRE is the decline in federal income, a $1.1 billion decrease from FY12. Sales of Goods and Services, and Land Income each declined by over $110 million.

Table 2: All Funds Revenue by Receipt Type (in millions dollars), YTD (through July) FY12 and FY13

	FY2012 YTD	***FY2013 YTD***	Actual Percent Change	Estimated BRE Percent Change
Total Tax Collections	40,070.2	43,458.3	8.5%	7.4%
Federal Income	30,387.8	29,261.3	-3.7%	14.8%
Licenses, Fees, Permits, Fines, and Penalties	6,896.9	7,253.8	5.2%	16.4%
Interest and Investment Income	1,046.9	1,128.1	7.8%	1.8%
Lottery Proceeds 3	1,658.5	1,743.2	5.1%	-5.0%
Sales of Goods and Services	344.4	208.9	-39.3%	4.6%
Settlements of Claims	557.7	593.5	6.4%	-3.9%
Land Income	1,305.2	1,187.4	-9.0%	-19.7%
Contributions to Employee Benefits	0.1	0.1	-31.9%	-6.7%
Other Revenue Sources	4,451.1	4,753.7	6.8%	-5.9%
TOTAL Net Revenue	**86,718.8**	**89,588.4**	**3.3%**	**9.3%**

Source: Comptroller of Public Accounts

While the BRE forecast for tax collections is exceptionally accurate, the estimate for total revenue will be off by $5.6 billion. One should note from Table 2, the decline in federal income is the primary reason for the decline in estimated total revenue. The state should experience a decline of around $4.4 billion from estimated federal income for FY13. This accounts for 80 percent of the reduction in total non-tax revenue.

Total expenditures continue to decline. Through July total state expenditures have declined by 2.3 percent ($2.0 billion). As shown in Table 3, cuts to two items, public assistance payments (-$1.1 billion), and public education payments (-$1.8 billion) exceeded the overall decrease.0

Table 3: All Funds Expenditures by Category (in millions dollars), through July, FY2012 and FY2013

CATEGORY	**FY2012**	**FY2013**	**Percent Change**	**Proportion Expenditure 2013**
Employee Compensation	14,069.5	14,300.2	1.6%	16.9%
Public Assistance Payments	32,378.1	31,288.4	-3.4%	37.1%
Public Education Payments	23,319.0	21,491.3	-7.8%	25.5%
Intergovernmental Payments	3,487.7	3,571.1	2.4%	4.2%
Other Expenditures	13,195.8	13,776.4	4.4%	16.3%
TOTAL EXPENDITURES	**86,450.0**	**84,427.3**	**-2.3%**	**100.0%**

Source: Comptroller of Public Accounts

With the substantial decline in public education expenditures, the proportion of the state budget devoted to public education declined from 27.2 percent in FY12 to 25.5 percent this fiscal year. Had public education expenditures maintained its FY12 proportion, expenditures would be $2.1 billion more. Items (employee compensation, intergovernmental payments, and other expenditures) accounting for 37.2 percent of expenditures had minimal increases.

Table 4 shows expenditures by function through July of FY12 and FY13. Almost the entire decline in total expenditures is due to the $2.0 billion reduction in education expenditures. Substantial declines in general government ($300 million) and health and human services ($900 million) offset some of the increase in other government functions. Even with the supplemental appropriations that were enacted and moving the public education payment transfer from September to August, Texans should expect little or no change in Public Education expenditure for FY13, while Health and Human Services expenditures should be around a billion more than the FY12 expenditure. Total expenditures for FY13 should be the same as FY12 expenditures ($94.3 billion)

Table 4: All Funds Expenditures by Function (in millions dollars), through June, FY2012 and FY2013

EXPENDITURES BY FUNCTION	FY2012	FY2013	Change	Percent Change
General Government	2,793.0	2,486.2	(306.8)	-11.0%
Education	30,857.4	28,852.4	(2,005.0)	-6.5%
Employee Benefits	3,051.0	3,163.6	112.6	3.7%
Health and Human Services	35,378.1	34,508.8	(869.3)	-2.5%
Public Safety and Corrections	3,930.1	4,001.6	71.5	1.8%
Transportation	6,209.6	6,863.4	653.8	10.5%
Natural Resources/Recreational Services	1,935.8	2,074.8	139.0	7.2%
Regulatory Services	297.1	321.4	24.3	8.2%
Lottery Winnings Paid	561.2	595.3	34.1	6.1%
Debt Service - Interest	993.8	1,056.0	62.1	6.3%
Capital Outlay	442.8	504.1	61.2	13.8%
TOTAL EXPENDITURES	86,450.0	84,427.3	(2,022.8)	-2.3%

Source: Comptroller of Public Accounts

State tax revenues continue to improve through July of FY13, with tax collections increasing by 8.5 percent compared to FY12. Even with the recent increase in severance tax collections, the growth in FY13 tax collections should be $500 million more than the current revenue estimate.

While tax collections are increasing substantially, total state revenue has only increased by 3.3 percent, as many of the non-tax sources of revenue have experienced negative growth rates. It does not appear that HB10 will reverse the negative growth in federal receipts and federal funds might achieve no growth in income from FY12. The BRE estimated a 14.8% growth in federal income for FY13.

Total state expenditures decreased by 2.3 percent, with the majority of this decrease attributable to the $2.1 billion reduction in education expenditures. With the supplemental appropriations bills, all funds appropriations for FY13 should increase to the amount expended in FY12.

The state score board continues to read “revenue up, expenditures down.” While the Comptroller increased the estimate for severance tax collections for FY13, it is unfortunate that everyone will have to await the release of the Certified Revenue Estimate (CRE) in December for a revised and more accurate estimate for FY14-15. I expect that total tax collections for the coming biennium to be at least $5 billion more than in the current estimate—a non-trivial amount. Should the Texas economy continue on its current growth path, tax collections in the coming biennium should be $10 billion more.

We should expect that the current tax growth rate of -0.1 percent will be substantially increased. The estimated increase in tax receipts for the biennium, 6 percent, is the fourth lowest change in tax collections since the 1960-1961 biennium. In fact, the compound growth in biennium tax revenues has been 16.7 percent, a rate almost triple the estimated rate for the 2014-2015 biennium.

Had a revised estimate for FY14-15 been provided the 83rd Legislature additional funding for water ($2.0 billion), transportation ($1.2 billion), and public education ($??? Billion) could have been provided by augmenting the Appropriation bill. In fact, when the CRE is released in December, one will find there was no need to send two Constitutional amendments to voters so funding could be provided for water and transportation.

My Bottom-line: I expect that the certifiable balance for FY14-15 to be about $7.5 billion more than in the current estimate. I also expect that the transfer to the Rainy Day Fund for FY14-15 to be $5.3 billion, over $1 billion more than in the current estimate. One would have hoped that these additional funds would have been made know during the session, not six months after the 4th sine die.

Dr. Greenfield holds a Ph.D. in economics from the University of Texas. He worked for three Comptrollers of Public Accounts and other Texas state agencies. Since retiring from the state in 2000, Greenfield has taught economics at Austin Community College and University Maryland University College.