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Transcriber's Office

Tax Rate Review Committee  
November 20, 2009

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The Tax Rate Review Committee met at 10:00 a.m. on Friday, November, 20, 2009, in Room 1003 of the State Capitol. Members present: Senator John Wightman, Chairperson; Senator Abbie Cornett; Senator Mike Flood; Senator Lavon Heidemann; Tax Commissioner Doug Ewald. Also present: Mike Calvert, Fiscal Analyst. []

SENATOR WIGHTMAN: I guess everybody is present so we'll go ahead and open the meeting. Good morning, everybody. Can you inform us at to what the report shows? []

MIKE CALVERT: (Exhibit 1) Certainly. This is a...for the record, my name is Michael Calvert, Legislative Fiscal Analyst. This meeting is required in statute to occur between November 15 and November 25. And thank you for making this meeting on such short notice. It was one of the balls that I was juggling, that I dropped. And luckily we picked up on getting this scheduled and the timing is about right. If you go to page 1, this is just the statutes, and the highlighted material on (2) is the specification of the purpose of the meeting. On page 2, you'll see a General Fund Financial Status. This should look familiar. It's the same one that was on your agenda today. This is the outlook as it stood as of Final Reading of the budget bills, LB1, LB2, LB3, LB4, and LB5 as they were on Final Reading. You will see the adjustments on lines 5, 15 and 16, lines 22 and 23, with a net result on line 29 if all enacted as passed this morning, we will be within \$384,407 of balance to the minimum 3 percent reserve for the current biennium. Line 34 gives you a breakdown of the rate and base adjusted revenue growth. They obviously include the revised forecast of the Forecast Board this past October. For the current and ensuing fiscal year, we came off a very low growth, negative growth year in '08-09 of minus 4.4 percent; the current forecast rate/base adjusted, minus 1.3; and the current forecast for the next fiscal '10-11 at about 4 percent. Just as a quick reminder, long-run growth rates, about 5.2 percent over the long haul since 1981. So we're looking at growth rates during this time period that are very, very low. For future years, we use a capped cycling estimating method for future years capped at 7.4 percent per year, which is well above the 5.2 percent average. But if you look at line 35, the five-year average of this status is 2.6 percent--well below the historical norm during that entire time period. A summary statement at the bottom: Cash Reserve Fund balance, starting at 2010-11, and into the foreseeable future under current law, is at \$324.7 million. So a substantial reserve still remains. More detail in terms of the transfers of the Cash Reserve Fund are on page 3. These are also...this flow has been adjusted for special session transactions. Page 4 is more detail with respect to revenue growth and revenue estimates by specific tax type. And page 5...we always like to use charts. At the bottom you can see the cycling nature of revenue growth that we have seen since 1982. And obviously the '09 and '10 values are well below the 5.2 percent average, with the higher growth rates shown in the out two years. So you can see where we are in terms of an overall revenue growth pattern compared to the historical average. When we look at a status for this biennium, we obviously have done estimates for the future two years, and there is a summary

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statement on page 6 outlining the expenditure growth assumptions that we have built in. It is a current law, quote, current service baseline, if you will. And that's all I have. []

SENATOR WIGHTMAN: Just prior, Mike, to where the graph starts in '82 where...and I know '81 was a real low year, or I thought it was. Do we have any years that have gotten as low as '09 has? []

MIKE CALVERT: Not to my recollection. I have...I'm sure we have data going back to prior years. Part of the problem is some of the information prior to 1982 is a little bit sketchy in terms of being able to make adjustments on tax rate and base changes. But I can't recall anything...well, I mean, in my time period. I've been here since 1983. So, yeah, this is about as low as we've gone. []

SENATOR WIGHTMAN: And I think nationally they're saying that we're as low as...as big a drop as there's been since the Depression. []

MIKE CALVERT: Talking to my colleagues in other states, this is about as bad as they've ever seen. []

SENATOR HEIDEMANN: On line 34, on the "Financial Status," on the revenue growth you're at 4.4. What was we in the previous year--it would have been the '07-08 year--do you know? []

MIKE CALVERT: That was over 7 percent. In fact, I think... []

SENATOR HEIDEMANN: The way it looked on that chart... []

MIKE CALVERT: Yeah. If you go to page 5, Senator, there is a Table 2 at the top, "Actual and Projected General Fund Revenue" growth. You'll see '07-08. It was about 7.2. The year before, 7.4. The year before that: 9.9, 9.5, 8.3. And then we had the recession period or the real low growth period in 2001-02, where we had...or actually 2002...I'll get my glasses fixed (laugh). Fiscal year ending 2002 and fiscal year ending 2003 were both negative growth years, rate/base adjusted. []

SENATOR HEIDEMANN: And for those people that don't think we can get to a 7.4, you want to point out that in 2002-03 actual, we had a minus .5 percent revenue growth. The very next year we were at 8.3 percent. []

MIKE CALVERT: It was characterized as a V-shaped recovery at that time. []

SENATOR HEIDEMANN: Very much so. []

MIKE CALVERT: Yes. []

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SENATOR CORNETT: And what are we projecting for our recovery from this? []

MIKE CALVERT: Global Insight suggests that it is less of a V-shape and more of a U-shape, or a W actually. []

SENATOR WIGHTMAN: And if it's a W, I'm assume we're in fairly big trouble, or could be. []

MIKE CALVERT: Pardon, I'm sorry? []

SENATOR WIGHTMAN: If it is a W, we could...we probably would not see... []

MIKE CALVERT: Well, arguably, I would say the forecast. Since we use Global Insight as does the Department of Revenue, I can vouch for how we develop a forecast, but basically it is the economic data right out of their estimates. []

SENATOR CORNETT: So if we are at a U rather than a V, what do you see our revenue growth as, (inaudible) W? []

MIKE CALVERT: I would characterize our forecast as compatible with more of a U-shaped. []

SENATOR CORNETT: U-shaped? []

MIKE CALVERT: Um-hum. Just simply because we made no other adjustments. []

SENATOR CORNETT: What type of growth do you expect to see with that U-shaped? []

MIKE CALVERT: Well, in terms of revenue growth as we've got scheduled? []

SENATOR CORNETT: Yes. []

MIKE CALVERT: Current year, minus 1.3 percent. Four percent which is below average. And 7.4 percent is not part of the forecast. That is our own separate methodology using cycling. If it would follow Global Insight's recovery shape, it would probably be something less than that 7.4; something less. []

SENATOR CORNETT: Something less? []

MIKE CALVERT: Yes. I would think it would be probably closer to the average, or above average, slightly. []

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SENATOR CORNETT: Okay. And then if we're looking at the W, which you said they're projecting... []

MIKE CALVERT: Um, I don't know exactly how much that would change it. It might be a little bit of timing. I really don't... []

SENATOR CORNETT: A little bit of timing? When would they...do you know when they projected when they expect us to bottom out again on that W? []

MIKE CALVERT: My recollection was that Global Insight was calling for GDP growth in this, the fourth quarter, to be quite high...above average. It was like somewhere in the neighborhood of 3 to 3.8 percent. []

SENATOR CORNETT: In this quarter? []

MIKE CALVERT: In this quarter. Next quarter was going to be somewhere around 1.8 to 1.9 percent, which is still positive. []

SENATOR CORNETT: So that would be the down again. []

MIKE CALVERT: That would be the other notch of the W. And after that, I don't recall if it got above 2 percent or not, but I think it was a more gradual recovery thereafter. []

SENATOR CORNETT: Okay. []

MIKE CALVERT: Now, the trick in all this is you can talk about GDP and growth rates in that context, but states, regions, are different in how they emerge from recoveries. And also the real trick is how that translates into tax receipts. It may not be a real direct correlation. There might be some lags too. []

SENATOR CORNETT: What area do you foresee those lags in? Personal income? Or do we seem to be...? []

MIKE CALVERT: Um, probably. Probably. Sales tax tends to be quite responsive to the immediate circumstances. Withholding tends to be fairly responsive to immediate circumstances because of employment, wage inflation, and so on and so forth. The hook often is on estimated payments and, more importantly, on final payments--you know, the final reconciliation every April. It's where we either get a nasty or a pleasant surprise. []

SENATOR WIGHTMAN: Mike, what all is included over on page 4 under "Miscellaneous receipts"? []

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MIKE CALVERT: Oh, Page 4? A long laundry list. []

SENATOR WIGHTMAN: Right. Under "Adjusted Growth." It's not a major share of the revenues, is it? []

SENATOR WIGHTMAN: No. Miscellaneous receipts, if you look at the schedule at the top under "Actual/Forecast," it varies around \$200 million a year. Your biggest components will be interest...investment and interest income, the General Fund portion of cigarette tax, liquor tax. We have some licenses and fees that go to the General Fund, and those tend to be on a two-year cycle where we'll get \$12 million to \$14 million one year, and the next year we'll barely get \$100,000 because the schedule is an every other year. []

SENATOR WIGHTMAN: As a percentage of the total revenue, it would be 10 percent or less, or...? []

MIKE CALVERT: Oh, yes. It would be less. Yeah, if you figure \$3.4 billion or \$3.5 billion revenue in a year, \$200 million is less than 10. Probably 6. []

SENATOR WIGHTMAN: Yeah. About 6-7 probably. []

MIKE CALVERT: Sure, comparable to corporate income. Those are the two smallest. []

SENATOR WIGHTMAN: So even though that figure is large as a percentage, it's not going to represent a big loss when you look at the total revenues, probably. []

MIKE CALVERT: Oh, when you look at growth rates? []

SENATOR WIGHTMAN: Yeah. []

MIKE CALVERT: Yeah. Yeah. A 1, 2, 3 percent on a \$200 million base is negligible, and a lot of the variability comes on the interest income side. []

SENATOR WIGHTMAN: Thank you. []

MIKE CALVERT: You're welcome. []

SENATOR WIGHTMAN: Any other questions? []

SENATOR HEIDEMANN: Even as we build our next biennial budget off the next October forecast... []

MIKE CALVERT: Yes. []

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SENATOR HEIDEMANN: ...and a comment that you had made after answering Senator Cornett's question, and you look at the graph on page 5, you're definitely looking at a V-shaped recovery, is that correct? []

MIKE CALVERT: No. You know, our forecast I would characterize as more of a U-shape. They follow that kind of pattern. Now keep in mind, you've got three players in the whole revenue forecasting endeavor. The Department of Revenue contributes revenue forecasts to the Forecasting Board, and then they independently synthesize. I don't know if I can readily characterize the Forecast Board estimates as clearly. It seems to be kind of a compromise between our estimates and the Department of Revenue. I'd still characterize it as somewhat U-shaped. []

SENATOR HEIDEMANN: And I agree with you because when you read the information being provided by Global Insight, they are a little bit more U-shaped. []

MIKE CALVERT: Yes. []

SENATOR HEIDEMANN: And that's the information, next October, if it stays the same, that you will feed to the Forecasting Board...or the Forecasting Board will get just looking at that. And because we build a biennium budget off of that, do you think that you're going to see, according to this graph, that kind of a V-shaped? Or you're actually going to see somewhat a lower revenue growth when the Forecasting Board...? And this is...it's going to be an opinion because you don't know that. []

MIKE CALVERT: Sure. Do I think there's a downside risk that the growth rates could be lower? Yes, I do. One of the wild cards in all of this is--and Tax Commissioner Ewald, you can maybe help me on this--but as I understand it, there is an expiration in federal tax law at the end of calendar 2010 dealing with a preferential tax rate for capital gains, okay? It expires at the federal level. When I looked at the Global Insight forecast that we used, my question to our forecaster was, is there an adjustment in the Global Insight forecast that says, yes, the law goes away; did they adjust the marginal tax rate? And there was an adjustment. So Global Insight was essentially saying that under their current scenario they assume that that policy, that federal policy, that federal tax preference, goes away. The big question becomes, what will be taxpayer behavior in terms of cashing out any capital gains prior to the end of December 2010? Theoretically, if they're in a preferential situation there might be a significant cashing out of capital gains prior to December 2010, and we might see a bounce in individual income tax receipts due to that additional liability. However, if tax... []

SENATOR HEIDEMANN: Which would correct itself. []

MIKE CALVERT: Which will correct itself. Exactly. I mean, if you liquidate that gain, you

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don't have that into the next year or two. The other thing is, though, taxpayer behavior might be governed by what policy considerations might be occurring between now and then, in Washington, D.C., as to an extension. That changes the ball game. []

SENATOR CORNETT: I just want to make sure that I'm reading this correctly. With the graph you have here,... []

MIKE CALVERT: Yes. []

SENATOR CORNETT: ...page 5, even though we're going back up, we're still at a negative growth rate on 2010. []

MIKE CALVERT: Yes. Year over year growth over a prior year. []

SENATOR CORNETT: So... []

MIKE CALVERT: Because the 2010 estimate, we calculate rate/base adjusted about a negative 1.3 percent growth over the prior year. []

SENATOR CORNETT: All right. []

MIKE CALVERT: So, I mean, it's a very weak...very weak growth scenario. []

SENATOR CORNETT: Hence, the deficit and what you see in the outlying? []

MIKE CALVERT: Yeah. I mean that triggered, as much as anything, this special session--that revised forecast. []

SENATOR WIGHTMAN: Other questions? Does anyone have any motions? []

SENATOR FLOOD: I make a motion that we recommend no tax increases and not make a...and as part of that recommendation, that we not recommend a special session be held in addition to the one we're just finishing today. []

SENATOR WIGHTMAN: Do we have a second? []

SENATOR CORNETT: Just sine die, and go right back in. []

SENATOR WIGHTMAN: The motion would be no tax increases and no additional special session. []

SENATOR FLOOD: That's right. []

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SENATOR WIGHTMAN: Do we have a second? []

SENATOR CORNETT: I'll second that. []

SENATOR WIGHTMAN: We have a motion and a second. We'll have a roll call vote. []

CLERK: Senator Wightman. []

SENATOR WIGHTMAN Yes. []

CLERK: Senator Cornett. []

SENATOR CORNETT: Yes. []

CLERK: Commissioner Ewald. []

DOUG EWALD: Yes. []

CLERK: Senator Flood. []

SENATOR FLOOD: Yes. []

CLERK: Senator Heidemann. []

SENATOR HEIDEMANN: Do I get to vote? Oh, I do. (Laugh) Yes. []

SENATOR WIGHTMAN: Motion carried. Do we have any other action to be taken? []

SENATOR FLOOD: I'd move that we adjourn. []

SENATOR HEIDEMANN: I'll second that one. []

SENATOR WIGHTMAN: All in favor say aye. Thank you. []

MIKE CALVERT: Thank you all, very much. []

SENATOR WIGHTMAN: Thank you, Mike, for the report. []