

KANSAS LEGISLATIVE RESEARCH DEPARTMENT

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To: Governor Sam Brownback and Legislative Coordinating Council

From: Kansas Legislative Research Department
Kansas Division of the Budget

Re: State General Fund Receipts Estimates for FY 2014 and FY 2015

Estimates for the State General Fund (SGF) are developed using a consensus process that involves the Legislative Research Department, Division of the Budget, Department of Revenue, and three consulting economists from state universities. This estimate is the base from which the Governor and the Legislature build the annual budget. The Consensus Group met on November 6, 2013, and decreased the estimate for FY 2014 and developed the initial estimate for FY 2015.

For FY 2014, the estimate was decreased by \$29.0 million, or 0.5 percent, below the previous estimate (made in April and subsequently adjusted for legislation enacted during the veto session). Those legislative adjustments to the April estimates had included various sales and income tax adjustments that had increased FY 2014 receipts by \$307.9 million; and the omnibus bill, which increased the previous estimate by an additional \$123.4 million. The revised estimate of \$5.857 billion represents 7.6 percent below final FY 2013 receipts.

The initial estimate for FY 2015 is \$5.917 billion, which is \$60.6 million, or 1.0 percent, above the newly revised FY 2014 figure. Factors influencing this forecast in addition to the state of the economy include the phasing in of various provisions of the new income tax law; as well as a net change of \$46.8 million in transfers out of the SGF (in compliance with current statutory requirements for FY 2015).

Table 1 compares the new FY 2014 and FY 2015 estimates with actual receipts from FY 2013. Table 2 shows the changes in the FY 2014 estimates.

Economic Forecast for Kansas

Although the U.S. economy is continuing its recovery from the Great Recession, the forecasted rate of growth remains slow. The impact of reduced federal spending as a result of sequestration and additional uncertainty from ongoing policy stalemates in Washington have combined to provide a drag on growth. The current assumption is that modest growth will continue in the national and state economies during the forecast period. Nominal Gross Domestic Product is now expected to grow by 3.2 percent in 2013 (the April estimate had been 3.7 percent) and 4.4 percent in 2014 (the April estimate was 4.6 percent); and nominal Kansas Gross State Product is now forecast to grow by 2.6 and 3.8 percent for the two years,

respectively (down from the 3.8 and 4.1 percent estimates used in April). The estimates contained in this memo for FY 2014 and FY 2015 are premised on these forecasts.

Personal Income

Kansas Personal Income (KPI) in 2013 is now expected to increase by 2.0 percent above the 2012 level, down from the April estimate of 3.1 percent. The new forecast calls for KPI growth of 3.5 percent in 2014 (down from the 4.0 percent estimate in April) and 4.4 percent in 2015. The forecasted rate of growth in US personal income remains higher than Kansas for all three years (2.1 percent in 2013; 4.6 percent in 2014; and 5.1 percent in 2015).

New Kansas Income Tax Law

No additional information was provided by the Department of Revenue that would significantly alter the fiscal notes that had been provided during both 2012 and 2013 regarding the estimated impact of multiple changes to the individual income tax enacted over the last two years. The fully annualized impact of the tax year 2013 changes is reflected for the first time in FY 2014, when estimated SGF individual income tax receipts are more than \$730.0 million lower than they would have been if the tax year 2012 structure had remained in place. By the end of FY 2018, cumulative receipts from individual income taxes will have been reduced by more than \$5.2 billion as a result of the new law. The Consensus Group will work with the Department of Revenue to continue to monitor a number of features being phased in over multiple years, including additional rate cuts and accelerated “haircuts” for itemized deductions.

Employment

The most recent monthly data from the Kansas Department of Labor show that total Kansas non-farm employment from August 2012 to August 2013 increased by about 15,400 jobs, with particularly strong growth in the professional and business services sector (9,300 jobs). On the negative side, the data show 5,400 fewer public sector jobs and 400 fewer jobs in construction. Current projections are that overall employment will continue to grow at a relatively modest 1.4 percent in both 2013 and 2014. The current average estimates used by the Department indicate that the overall Kansas unemployment rate, which was 5.7 percent in CY 2012, is expected to be 5.8 percent in CY 2013 and 5.6 percent in CY 2014. The national unemployment rate is expected to remain well above the Kansas rate, with the US rate now forecasted to be 7.9 percent in 2013 and 7.8 percent in 2014.

Agriculture

The agricultural outlook in 2013 has improved significantly over the drought year of 2012. Subsoil moisture supplies as of late October were rated as short or very short in 53.0 percent of the state (compared to 84.0 percent a year ago); while topsoil moisture was short or very short in 43.0 percent of the state (compared to 66.0 percent). Cattle on feed in Kansas feedlots with 1,000 head or more capacity were at the lowest October 1 inventory level since 1996. Range and pastureland conditions are now rated 36.0 percent poor or very poor (compared to 79.0 percent a year ago). The US All Crops Price Index for October was 203.0 percent of the 1990-92 base, down 35 points from a year earlier. Commodity prices have fallen

significantly in 2013 as a result of increased yields. High input prices, especially energy and fertilizer costs, remain an ongoing concern for the agricultural sector.

Oil and Gas

Driven by foreign demand and volatility in the Middle East, the price of oil thus far in FY 2014 has remained at a relatively high level and is expected to continue to do so for the balance of the forecast period. The forecasted price per taxable barrel of Kansas crude in FY 2014 has remained at \$86, or about \$1 per barrel higher than the \$85.01 final average price for FY 2013. The FY 2015 price is expected to remain in the same general range at \$85 per barrel. As always, significant political tensions around the world provide a great deal of uncertainty about forecasting the price of this commodity. Gross oil production in Kansas, which had been declining steadily for many years, reversed that trend about eight years ago and began increasing. But expectations are now that an accelerated increase from the Mississippian Lime oil play will not be as great as had been originally forecast in 2012, at least in the near future. The current forecast of 48.5 million barrels for FY 2014 and 52.5 million barrels for FY 2015 nevertheless compares favorably to the 33.5 million barrels produced in FY 2005. The repeal of an oil severance tax exemption in 2012 has expanded the percentage of Kansas oil subject to taxation.

The price of natural gas is expected to average \$3.35 per mcf for FY 2014 before increasing to \$3.60 per mcf for FY 2015, based on an industry source's analysis of futures markets. (The previous price forecast for FY 2014 made in April was \$3.75 per mcf.) Factors considered for these estimates included the relationship between crude oil and gas prices, a review of rig count data, the current high storage levels for gas, the overall economic outlook, and the impact of enhanced natural gas production from shale formations elsewhere in the U.S. Kansas natural gas production in FY 2013 of 295.5 million cubic feet represented a significant decrease from the modern era peak of 730.0 million cubic feet in FY 1996 (largely as a result of depletion of reserves in the Hugoton Field). Production is expected to continue to decrease to 285.0 million cubic feet for FY 2014; and 275.0 million cubic feet for FY 2015.

Inflation Rate

The Consumer Price Index for all Urban consumers (CPI-U) is expected to increase by 1.5 percent in 2013. The latest forecast calls for inflation to remain at very moderate levels of 1.9 percent in 2014 and 2.2 percent in 2015.

Interest Rates

The Pooled Money Investment Board (PMIB) is authorized to make investments in US Treasury and Agency securities, highly rated commercial paper and corporate bonds, repurchase agreements and certificates of deposit in Kansas banks. Extremely low idle-fund balances in recent years have required the PMIB to maintain a highly liquid portfolio, which reduces the amount of return available to the pool. In FY 2013, the state earned only 0.18 percent on its SGF portfolio (compared with a 4.26 percent rate as recently as FY 2008). The average rates of return forecast for FY 2014 and FY 2015 remain very low (0.12 percent for each year) and reflect the expected continuation of historically low interest rates.

Economic Forecasts			
	<u>CY 2013*</u>	<u>CY 2014*</u>	<u>CY 2015*</u>
KPI Growth	2.0 %	3.5 %	4.4 %
Inflation (CPI-U)	1.5 %	1.9 %	2.2 %
<hr/>			
	<u>FY 2013</u>	<u>FY 2014*</u>	<u>FY 2015*</u>
SGF Interest	0.18%	0.12%	0.12%
Oil and Gas			
Oil Price per bbl	\$85.01	\$86.00	\$85.00
Gross Prod. (000)	44,629	48,500	52,500
Gas Price per mcf	\$3.01	\$3.35	\$3.60
Gas Taxable Value	736,743	811,538	871,200
* Estimated			

State General Fund Receipts Estimates

FY 2014. The revised estimate of SGF receipts for FY 2014 is \$5.857 billion, a decrease of \$29.0 million below the previous estimate. Receipts through October had been running \$18.9 million below that forecast. The overall revised estimate is approximately \$484.6 million, or 7.6 percent, below actual FY 2013 receipts (see Table 1). As noted earlier, the FY 2014 estimates include the fully annualized impact of the new tax year 2013 income tax law; as well as the reduced retail sales and compensating tax rate (from 6.3 to 6.15 percent). The FY 2014 figures also include a decreased share of retail sales and compensating use taxes earmarked for deposit in the SGF pursuant to legislation enacted originally in 2010.

Each individual SGF source was reevaluated independently, and consideration was given to revised and updated economic forecasts, collection information from the Departments of Revenue and Insurance, and year-to-date receipts.

The compensating use tax estimate was increased by \$21.3 million; the sales tax estimate by \$12.5 million; and the motor carrier property tax by \$4.0 million. Receipts from these sources were running well ahead of the previous forecast through October.

Reductions of note include the individual income tax (down \$24.7 million); the corporation income tax (down \$10.0 million); and severance taxes (down \$12.2 million). As noted earlier, no significant new information is available at this time regarding the impact of the individual income tax cuts enacted over the last two years, and receipts from this source were running \$38.3 million below the previous forecast through October. The Consensus Group will work over the winter with the Department of Revenue to monitor tax year 2013 returns as they are filed and will have an updated indication of the impact of the new law in April.

Details of the current year's revised estimate are reflected in Table 2.

FY 2015. SGF receipts are estimated to be \$5.917 billion in FY 2015, a figure that is 1.0 percent above the new FY 2014 forecast. This estimate takes into account a new round of income tax rate cuts and itemized deduction changes that are being implemented in tax year 2014 and an increase of \$46.8 million in net transfers from the SGF which will occur absent any change in current law.

Accuracy of Consensus Revenue Estimates

For 39 years, SGF revenue estimates for Kansas have been developed using the consensus revenue estimating process. Besides the three state agencies identified on the first page, the economists currently involved in the process are Joe Sicilian from the University of Kansas, Lance Bachmeier from Kansas State University, and Nancy McCarthy Snyder from Wichita State University. Each of the agencies and individuals involved in the process prepared independent estimates and met on November 6, 2013, to discuss estimates and come to a consensus for each fiscal year.

STATE GENERAL FUND ESTIMATES

Fiscal Year	Adjusted Original Estimate*	Adjusted Final Estimate**	Actual Receipts	Difference from Original Estimate*		Difference from Final Estimate**	
				Amount	Percent	Amount	Percent
1975	\$ --	\$ 614.9	\$ 627.6	\$ --	-- %	\$ 12.7	-- %
1976	676.3	699.7	701.2	24.9	--	1.4	0.2
1977	760.2	760.7	776.5	16.3	2.1	15.8	2.1
1978	830.1	861.2	854.6	24.5	3.0	(6.5)	(0.8)
1979	945.2	1,019.3	1,006.8	61.6	6.5	(12.5)	(1.2)
1980	1,019.3	1,095.9	1,097.8	78.5	7.7	1.9	0.2
1981	1,197.1	1,226.4	1,226.5	29.4	2.5	0.1	--
1982	1,351.3	1,320.0	1,273.0	(78.3)	(5.8)	(47.0)	(3.6)
1983	1,599.2	1,366.9	1,363.6	(235.6)	(14.7)	(3.2)	(0.2)
1984	1,596.7	1,539.0	1,546.9	(49.8)	(3.1)	7.9	0.5
1985	1,697.7	1,679.7	1,658.5	(39.2)	(2.3)	(21.3)	(1.3)
1986	1,731.2	1,666.4	1,641.4	(89.8)	(5.2)	(25.0)	(1.5)
1987	1,903.1	1,764.7	1,778.5	(124.6)	(6.5)	13.8	0.8
1988	1,960.0	2,031.5	2,113.1	153.1	7.8	81.6	4.0
1989	2,007.8	2,206.9	2,228.3	220.5	11.0	21.4	1.0
1990	2,241.2	2,283.3	2,300.5	59.3	2.6	17.2	0.8
1991	2,338.8	2,360.6	2,382.3	43.5	1.9	21.7	0.9
1992	2,478.7	2,454.5	2,465.8	(12.9)	(0.5)	11.3	0.5
1993	2,913.4	2,929.6	2,932.0	18.6	0.6	2.4	0.1
1994	3,040.1	3,126.8	3,175.7	135.6	4.5	48.9	1.6
1995	3,174.4	3,243.9	3,218.8	44.4	1.4	(25.1)	(0.8)
1996	3,428.0	3,409.2	3,448.3	20.3	0.6	39.0	1.1
1997	3,524.8	3,642.4	3,683.8	159.0	4.5	41.4	1.1
1998	3,714.4	3,971.0	4,023.7	309.3	8.3	52.7	1.3
1999	3,844.7	4,051.9	3,978.4	133.7	3.5	(73.4)	(1.8)
2000	4,204.1	4,161.0	4,203.1	(1.0)	--	42.1	1.0
2001	4,420.7	4,408.7	4,415.0	(5.7)	(0.1)	6.4	0.1
2002	4,674.5	4,320.6	4,108.9	(565.6)	(12.1)	(211.7)	(4.9)
2003	4,641.0	4,235.6	4,245.6	(395.4)	(8.5)	9.9	0.2
2004	4,605.5	4,450.5	4,518.7	(86.8)	(1.9)	68.2	1.5
2005	4,490.5	4,793.8	4,841.3	350.8	7.8	47.5	1.0
2006	4,834.0	5,308.7	5,394.4	560.4	11.6	85.7	1.6
2007	5,144.0	5,721.3	5,809.0	665.0	12.9	87.8	1.5
2008	5,700.4	5,736.3	5,693.3	(7.0)	(0.1)	(42.9)	(0.7)
2009	6,185.7	5,709.7	5,587.4	(598.3)	(9.7)	(122.3)	(2.1)
2010	5,974.2	5,291.0	5,191.3	(782.9)	(13.1)	(99.7)	(1.9)
2011	5,851.0	5,775.0	5,882.1	31.1	0.5	107.1	1.9
2012	6,098.9	6,404.3	6,412.8	313.9	5.1	8.5	0.1
2013	6,414.2	6,250.4	6,341.1	(73.1)	(1.1)	90.7	1.5

* The adjusted original estimate is the estimate made in November or December prior to the start of the next fiscal year in July and adjusted to account for legislation enacted, if any, which affected receipts to the SGF.

** The final estimate made in March, April, or June is the adjusted original estimate plus or minus changes subsequently made by the Consensus Estimating Group. It also includes the estimated impact of legislation on receipts.

The table (above) presents estimates compared to actual receipts since FY 1975, the fiscal year for which the current process was initiated. First, the adjusted original estimate is compared to actual collections and then the final estimate is compared to actual receipts.

Concluding Comments

Consensus revenue estimates are based on current federal and state laws and their current interpretation. These estimates will be further adjusted in mid-April prior to the conclusion of the 2014 Legislative Session.

**Table 1
State General Fund Receipts
(Dollars in Thousands)**

	Consensus Estimate November 6, 2013					
	FY 2013 (Actual)		FY 2014 (Revised)		FY 2015	
	Amount	Percent Change	Amount	Percent Change	Amount	Percent Change
Property Tax/Fee:						
Motor Carrier	\$ 28,855	16.3 %	\$ 45,000	56.0 %	\$ 24,000	(46.7) %
Income Taxes:						
Individual	2,931,168	0.8	2,500,000	(14.7)	2,525,000	1.0
Corporation	371,324	30.5	360,000	(3.0)	380,000	5.6
Financial Institutions	32,073	24.1	33,000	2.9	34,500	4.5
Total	\$ 3,334,565	3.6 %	\$ 2,893,000	(13.2) %	\$ 2,939,500	1.6 %
Excise Taxes:						
Retail Sales	\$ 2,184,573	2.3 %	\$ 2,100,000	(3.9) %	\$ 2,160,000	2.9 %
Compensating Use	340,044	4.5	342,000	0.6	355,000	3.8
Cigarette	91,928	(4.9)	90,000	(2.1)	89,000	(1.1)
Tobacco Products	7,057	1.1	7,100	0.6	7,200	1.4
Cereal Malt Bev.	1,855	(10.9)	1,800	(3.0)	1,800	--
Liquor Gallonage	19,057	2.8	19,000	(0.3)	19,500	2.6
Liquor Enforcement	60,512	2.8	65,000	7.4	66,000	1.5
Liquor Drink	9,802	2.9	10,000	2.0	10,300	3.0
Corp. Franchise	(4,167)	(142.4)	6,000	244.0	6,200	3.3
Severance	100,131	(6.6)	128,200	28.0	135,000	5.3
Gas	32,430	(19.5)	30,800	(5.0)	32,300	4.9
Oil	67,700	1.1	97,400	43.9	102,700	5.4
Total	\$ 2,810,791	1.4 %	\$ 2,769,100	(1.5) %	\$ 2,850,000	2.9 %
Other Taxes:						
Insurance Prem.	\$ 156,977	9.6 %	\$ 157,700	0.5 %	\$ 159,700	1.3 %
Miscellaneous	2,010	(26.1)	2,000	(0.5)	2,000	--
Total	\$ 158,986	9.0 %	\$ 159,700	0.4 %	\$ 161,700	1.3 %
Total Taxes	\$ 6,333,197	2.8 %	\$ 5,866,800	(7.4) %	\$ 5,975,200	1.8 %
Other Revenues:						
Interest	\$ 11,057	14.3 %	\$ 12,000	8.5 %	\$ 10,000	(16.7) %
Net Transfers	(60,994)	(133.8)	(71,200)	(16.7)	(118,000)	(65.7)
Agency Earnings	57,864	(6.8)	48,900	(15.5)	49,900	2.0
Total	\$ 7,928	(96.9) %	\$ (10,300)	(229.9) %	\$ (58,100)	(464.1) %
Total Receipts	\$ 6,341,125	(1.1) %	\$ 5,856,500	(7.6) %	\$ 5,917,100	1.0 %

Table 2
State General Fund Receipts
FY 2014 Revised
Comparison of November 2013 Estimate to June 2013 Estimate
(Dollars in Thousands)

	FY 2014 CRE Est. as Adj. For Legis.	FY 2014 CRE Estimate	Difference		
			Amount	Percent Change	
Property Tax/Fee:					
Motor Carrier	\$ 41,000	\$ 45,000	\$ 4,000	9.8 %	
Income Taxes:					
Individual	\$ 2,524,685	\$ 2,500,000	\$ (24,685)	(1.0) %	
Corporation	370,000	360,000	(10,000)	(2.7)	
Financial Institutions	31,000	33,000	2,000	6.5	
Total	\$ 2,925,685	\$ 2,893,000	\$ (32,685)	(1.1) %	
Excise Taxes:					
Retail Sales	\$ 2,087,500	\$ 2,100,000	\$ 12,500	0.6 %	
Compensating Use	320,700	342,000	21,300	6.6	
Cigarette	90,000	90,000	--	--	
Tobacco Products	7,100	7,100	--	--	
Cereal Malt Bev.	1,900	1,800	(100)	(5.3)	
Liquor Gallonage	19,100	19,000	(100)	(0.5)	
Liquor Enforcement	62,000	65,000	3,000	4.8	
Liquor Drink	9,900	10,000	100	1.0	
Corp. Franchise	6,000	6,000	--	--	
Severance	140,377	128,200	(12,177)	(8.7)	
Gas	35,297	30,800	(4,497)	(12.7)	
Oil	105,080	97,400	(7,680)	(7.3)	
Total	\$ 2,744,577	\$ 2,769,100	\$ 24,523	0.9 %	
Other Taxes:					
Insurance Prem.	\$ 160,000	\$ 157,700	\$ (2,300)	(1.4) %	
Miscellaneous	2,000	2,000	--	--	
Total	\$ 162,000	\$ 159,700	\$ (2,300)	(1.4) %	
Total Taxes	\$ 5,873,262	\$ 5,866,800	\$ (6,462)	(0.1) %	
Other Revenues:					
Interest	\$ 10,400	\$ 12,000	\$ 1,600	15.4 %	
Net Transfers	(61,234)	(71,200)	(9,966)	(16.3)	
Agency Earnings	63,098	48,900	(14,198)	(22.5)	
Total Other Revenue	\$ 12,264	\$ (10,300)	\$ (22,564)	(184.0) %	
Total Receipts	\$ 5,885,526	\$ 5,856,500	\$ (29,026)	(0.5) %	