

**Revenue Estimating Conference
Minutes
March 22, 2013**

Members Present: Dave Roederer, Holly Lyons, David Underwood.

Mr. Roederer called the Revenue Estimating Conference to order at 10:00 am.

Approval of December 12, 2012 Minutes

Mr. Roederer called for a motion to approve the December 12, 2012 minutes as they are written. Mr. Underwood made the motion to approve the minutes and Ms. Lyons seconded the motion. All voted in favor and the motion was carried unanimously.

Mr. Roederer began with a brief explanation of the numbers. He stated that each of the members look at various sources and independently draw their own conclusions, then bring them to this meeting and try to figure out the differences.

Ms. Lyons stated since the last meeting in December, the U.S. economy has continued to grow, albeit slowly. Some economists have called the growth weak or sluggish, but there is growth. The economy is chugging along at a very modest pace, despite some pretty serious headwinds. The federal fiscal policy passed in January, specifically the expiration of the payroll tax holiday, and sequestration of \$53 billion in fed funds could have knocked the economy off its course but so far it hasn't seemed to. However, the uncertainty surrounding the federal action was, and continues to be, a real drag on the economy both nationally and in the state.

Overall growth in the U.S. gross domestic product, or GDP, ended calendar year 2012 and was up 2.2% compared to 1.8% in 2011, but still below average. The national forecast is for 4% growth in 2014. Non-farm employment is also showing positive growth at 3.2% and initial unemployment claims continue to be down. Wage and salary income growth is positive; it is projected to grow at an above average rate. Other indicators, such as personal income, retail sales, the consumer price index, are all positive and while none of them could be considered strong, there is nothing to suggest an impending downturn.

Recent consumer confidence indicators are up, which is a bit of a pleasant surprise given all the uncertainty around the federal fiscal policy and the reduced disposable income that taxpayers had due to the expiration of the payroll holiday tax. Some of the same factors that concerned us in December still exist- uncertainty of the federal fiscal policy/fiscal cliff and the unknown impact of the federal sequestration imposed on March 1st; also the impact of the drought and recent forecast calling for continued drought through this spring and summer. Volatility of gas prices is a concern and the recent events at Cyprus are a strong reminder that global flare-ups could impact the economy and throw it off its course.

Turning our attention to Iowa, the LSA estimate is optimistic for the remaining three months of fiscal year 2013 at 6% growth, versus the December REC estimate of 3.3%. There is more of a “steady as she goes” estimate for fiscal year 2014 of 3.5% growth, compared to the December REC estimate of 3.4%. The Department of Revenue’s leading indicators index came out yesterday and was positive again after a brief drop in December. There was a large surge in personal income tax receipts in December and January for a couple of reasons. December tax estimate payments were higher as taxpayers anticipated higher tax rates on January 1st due to the federal action. Companies also accelerated bonus and dividend payments to taxpayers for the same reason. This will have a flipside, as there will probably be fewer payments with the actual tax returns that come in, but it should balance out. At this same time, we have yet to see the impact of the farm tax returns since the federal fiscal policy uncertainty led to a change in filing dates from March 1st to April 15th. Many farmers are anticipating record income this year due to high commodity prices and despite the drought.

The Bureau of Labor Statistics made very positive revisions to Iowa 2012 employment numbers earlier this week, indicating that we had more people employed than originally estimated, and that helps explain the accelerating withholding tax receipts over the last year. Employment is predicted to grow, but at a slow pace, approximately 1% in fiscal year 2014. Corporate taxes provided much of the revenue growth in Iowa last year, actually over the last couple years, but we continue to project that that will slow considerably for the remainder of fiscal years 2013 and 2014. Finally, the Iowa Business Council survey indicates that 90% of the businesses surveyed expect steady or increased sales over the next six months and 86% expect increased or steady employment and capital spending. So the LSA estimate for the remaining three months of fiscal year 2013 is optimistic and is steady for fiscal year 2014. Iowa continues to need job, wage and salary growth if we are to reach the revenue growth rates of a strong or robust economy.

Mr. Underwood stated the level of uncertainty that we are dealing with today has certainly been reduced since the meeting in December, so that gives us a little bit better feeling because of all the things that Holly mentioned. A lot of things have happened since December, not only the inauguration of a President and a Pope, but just recently looking at the economic reports, existing US home sales hit a three-year high; builders are caught off guard by a surge in demand for new homes; Congress has approved a temporary spending bill, at least to keep government running through the end of September; and the NCAA wrestling tournament floods the city of Des Moines.

There are and continue to be some negative items also. Talking with the employers around the state, they are still very cautious in their hiring – it’s hire at the last minute, very little anticipatory hiring going on. Overtime still lags behind some of the record overtime numbers that we’d seen in the past and of course that has a significant impact on the personal income tax. Ethanol, which has been pretty strong, has some significant challenges ahead in Congress, and the impact that it might be listening to some of the people that run the ethanol plants in Iowa. They are operating on marginal costing, not profitability costing and fortunately they’ve been able to get the supply to keep their plants open, which has not been universal across the

country. So there are some challenges there, and we still have the question of whether it's going to rain or not this spring and summer for a good crop. Farmers did okay and they'll see a little bit of a surge in income because a lot of them did get their insurance checks last year. There is some doubt there as to whether or not that is going to leave the farmers the ability to really increase their profits much more this year than what they are going to report for last year. But as Holly said, it's a little too early because they haven't filed yet so we haven't gotten a good handle on that. With electronic filing we've got some good information and things look pretty good, but there are still a lot of returns out there yet to be filed. Optimistic, much more so than in December now that we have some things settled, but still no surge in growth that's out there that I can see.

Mr. Roederer echoed what Ms. Lyons had pointed out- that there is uncertainty, and I think we're probably into a world now where it will always have some uncertainty on the international. We used to look at it more from a perspective of 'Do we think there is going to be a war someplace?' and what that impact would be. But as we've gotten more to a global economy, it's not just physical wars that we need to be worried about, but we need to take a hard look at what is going on financially throughout all of these markets. There is such a tie-in from one country to another and that is something we are always going to have to be concerned with.

From a national perspective, we are inching more on solid ground as far as our economy goes. I wouldn't say that we are rushing into it, or rapidly going into it, but we are starting to at least move in the right direction. We are seeing somewhat of a modest job pace, certainly not what we would expect coming out of a recession like this and Mr. Underwood mentioned that there is a great reluctance on employers throughout the country to be expanding their workforce. We know that one of those factors is what the impact is going to be on the affordable health care act, once you get to a certain number of people that starts having all kinds of consequences for you. I think it's going to be awhile before business and industry has that all figured out. We have started to see a slight increase in housing throughout the country but still consumer and business is very fragile. The alternative minimum tax, as both Holly and David mentioned, has been resolved and the federal tax cuts are now more certain so that isn't something we're going to have to look at every year, which we were for awhile. Federal sequestration has started and as Holly pointed out, so far the economy seems to be able to handle that. We do need to know that ratchets up a little more each year and goes on for nine years, so we'll have to see how that all plays out. Congress passed a continuing resolution and in the same form, between the House and the Senate, the President has indicated that he is going to approve that. Again, that doesn't resolve it but it does give us some breathing room.

That really only leaves the question mark out there is about the debt ceiling, which we reach I believe, in the middle of next month-estimates vary on that. I don't hear any real serious discussion that they won't extend that or raise the debt ceiling. If that were not to be done, obviously that would have major consequences but it appears that Congress is going to do that.

Looking at Iowa, it's quite clear by the numbers that the economy has outperformed our estimates for FY'12 and so far it is for fiscal year '13. Fiscal year '13 is looking pretty strong; our corporate taxes are somewhat weaker, sales and use tax seem to be stable; but I think there is still a real caution out there which was expressed by my colleagues- we still have a number of Iowans without jobs, I'm still concerned about the housing. If you look at the Department of Revenue's six month average- one month we're up, next month we're down, another month we're up- I think the last few months have still been stronger and the phone calls I've made to people in that business are starting to feel better about it, but I still think unless Iowan's are working and if housing is not strong, that our economy is going to be somewhat weak. Employers in Iowa are no different than the employers nationally; they are also reluctant to be expanding their workforce, at least at this time. The drought that both my colleagues had mentioned appears to be easing, with the last information that at least came out this morning from the weather bureau. I think the reason how people look at the drought is so important is because it's going to determine a lot of the behavior of what our people in agriculture do. Some are indicating that they will be planting as normal, maybe using a different type of seed that is more drought-resistant, but the big question is what they are going to do with their livestock. Are they going to keep their herds up or are they going to decrease those quite a bit, not knowing what the cost is going to be in order to feed them, and I don't think that we know. All in all, we're encouraged by what is going on in the economy but it seems like every time we just get to the brink where you think 'okay now we're just really going to start growing quite rapidly', something comes up or some negatives that hold us back.

In December, it was estimated that the alternative minimum tax would at least be extended and Congress has now permanently taken care of that, so that number was already factored in. However, the tax cuts were not factored in December. The estimates were based on the fact that all those tax cuts would expire and some of those tax cuts have been made permanently. Holly mentioned that there has been a delay in returns coming in. That has nothing to do with anything that the Department of Revenue has done, but because of the tax changes and the permanency of some of the tax cuts in Washington, they did delay when they would start receiving returns. It has also been pointed out that farm returns have not come in yet. They are generally due on March 1st, but they were extended to April 15th with the tax changes. So there is not quite the information there would be in a normal year. In December, the estimate was \$6.5 billion. The FY'13 and FY'14 numbers will now be re-visited to see what has taken place. In short, in FY'13, Legislative Service Agency is suggesting there will be an additional \$169.9 million and the Governor's representative is saying that there would be \$74.4 million, so there is a difference of \$95.5 million. For FY'14, the LSA number is \$180.8 million more and the Governor's representative is \$76.0 million more, for a difference of \$104.8 million. Those differences need to be bridged and a consensus agreed upon for what is between that. The increased amount is due to the tax cuts not originally being figured in here, which in FY'13 is an additional \$13.0 million for the state that was not have factored in. For FY'14, it's about \$62.0 million. The major differences are in the personal income tax and refunds. Personal income tax is about 50% of the state's revenue, sales tax is about 35%, and corporate income tax is 10%. That's why the focus is, for the most part, usually on those three.

Review Fiscal Year 2013 General Fund Estimates, Accruals, Refunds, School Infrastructure Transfer, and Lottery and Other Transfers

Mr. Underwood stated since meeting in December there have been a number of legislative changes that would impact the estimate. The estimated fiscal impact was used, so for FY'13 it's a \$24.8 million reduction of estimated revenue and for FY'14 that would be \$35.5 million. If everything else was exactly the same except for those changes, the estimates would be lowered. Because of the way that receipts have been coming in and the economic indicators removing some uncertainty, both the LSA and the Governor's appointee have seen more growth than they originally were expecting. From that standpoint we're actually pretty close at this point in time. Of the analysis Mr. Underwood has done of their numbers and estimates, he believes most of the difference is in net corporate tax. Even though it looks like there are some differences on personal income tax, when you net against the personal income tax refunds they both come down to about the same net number. So the only big difference is the net corporate.

Ms. Lyons stated that overall, the receipts growth to date is \$303 million and in order to meet the December REC estimate, an additional \$376 million is needed, which is how close it is to actually meeting the original estimate. In terms of refunds it looks like the big difference is in corporate refunds and Ms. Underwood asked Mr. Roederer if he could explain his refund estimate. Last year corporate refunds were about \$120 million. LSA's estimate is about \$107 million for this current fiscal year and the Governor's appointee's estimate is \$150 million. So there is a considerable difference there. Refunds would have to grow considerably between now and the end of the fiscal year to meet that estimate. Ms. Lyons would like to understand where the Governor's appointee's number comes from.

Mr. Roederer stated that was one of the things his staff had been discussing as well. The Governor's appointee believes that corporate income is still going to grow, but believes that there will also be refunds to go along with it. If it could be proven one way or another, the numbers wouldn't be off.

Ms. Lyons stated she was in the same boat as the Governor's appointee in trying to figure that out. Corporate refunds to date are \$98.6 million, down 16.5%. Refunds are so tricky to try to estimate, it's hard enough to try to estimate the income but then when you have to try to estimate what's going back out, it is even more complicated. So there isn't really a strong answer on either side.

Mr. Underwood stated that since those are difficult, he has to rely on the Department of Revenue in their estimates. They are the ones that have access to returns and can dig into some of that a little bit more. Their corporate refund estimate is just a little over \$156 million for FY'13 and they are \$167 million for FY'14. So if he had to fall back on an estimate, which would be what he would look at. If LSA's FY'13 corporate refunds estimate was increased by \$50 million, taking it to \$157 million, which would be about halfway between the two estimates for the total net receipts.

Mr. Roederer asked Ms. Lyons to comment before any motions were made.

Ms. Lyons stated she can agree with that adjustment and she agrees that Department of Revenue probably has a better handle on this. Ms. Lyons can support that proposal. Mr. Roederer agreed.

Mr. Underwood made a motion to increase the LSA refunds by \$50 million. Ms. Lyons seconded the motion. All voted in favor and the motion was carried unanimously. The growth percentage is 5.2% for fiscal year '13 and the dollar figure is \$6,637,000,000.

Review Fiscal Year 2014 General Fund Estimates, Accruals, Refunds, School Infrastructure Transfer, and Lottery and Other Transfers

Mr. Underwood made a motion to make a \$50 million adjustment to LSA's refund for fiscal year 2014, taking it from \$848 million to \$898 million. Ms. Lyons seconded the motion. All voted in favor and the motion passed unanimously. The growth percentage for FY'14 is 3.5% and the bottom line number is \$6,870,600,000.

Fiscal Year 2013 and 2014 Gambling Revenues Transferred to Other Funds and Interest Earned on Reserve Funds (transferred to Rebuild Iowa Infrastructure Fund)

Ms. Lyons made a motion to move the gambling numbers. Mr. Underwood seconded the motion. All voted in favor and the motion carried unanimously.

Other Business

With no further business, Mr. Underwood made a motion to adjourn the meeting. Ms. Lyons seconded the motion. All voted in favor and the motion passed unanimously. Mr. Roederer called the meeting adjourned.

Respectfully submitted,

Tammy Winters

These minutes were approved at the October 10, 2013 meeting.

Ms. Lyons made a motion to approve the minutes of the March 22, 2013 meeting and the motion was seconded by Mr. Underwood. All members voted in favor of the motion and it was carried unanimously.