

State of Maryland Board of Revenue Estimates

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September 30, 2009

Honorable Martin O'Malley
Governor, State of Maryland
State House
Annapolis, MD 21401

Dear Governor O'Malley:

At the beginning of a new budget cycle, the Board of Revenue Estimates has adopted revised general fund revenue estimates for fiscal year 2010 and the first official estimates for fiscal year 2011. We have reviewed the current estimate for fiscal year 2010 in light of the most recent economic data and developments, as well as revenue collections for fiscal year 2009. Based on our analysis, the Board submits to you a revised estimate of general fund revenues for fiscal year 2010 of \$12.314 billion and an estimate of \$12.734 billion for fiscal year 2011. The fiscal year 2010 estimate represents a reduction of \$682.8 million from the March estimate, upon which the fiscal year 2010 budget was based. Reductions to the forecasts of the income taxes, particularly the individual income tax, are primarily responsible for these revisions.

The recession has been ongoing for 20 months, the longest period of economic contraction since the 1930s. Gross domestic product may show growth in the third quarter, and many economists believe the recession has now ended. Even if that is the case, employment and income growth are likely to remain sluggish well into next year, with the national unemployment rate rising above 10% for the first time since early 1983. In addition to cutting jobs, employers have reduced hours—the average hours worked per week was at its lowest level ever at the start of the year—giving employers plenty of leeway before they will need to resume hiring.

Maryland's economy has been battered by the recession. Official statistics show that the State has lost jobs on a year-over-year basis every month since June of 2008, peaking at a 2.6% decline in April 2009. Growth in total personal income and wage and salary income has generally decelerated since the second quarter of 2007. In the first quarter of 2009 personal income increased 2.2%, while wage and salary income grew only 1.4%. These are the lowest figures since 1958 and 1991, respectively. Recently released statistics from the Department of Labor, Licensing and Regulation (DLLR) paint an even bleaker picture—these data, essentially a census of jobs, show a loss of 2.8% in the first quarter rather than the 2.0% loss in the official statistics. Of even greater concern, the DLLR data indicate that total wage and salary income actually fell 2.7% rather than increasing by 1.4%.

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Other measures show the distressed state of Maryland's economy. The unemployment rate has risen steadily from 3.6% at the start of 2008 to 7.3% in July, the highest rate of unemployment since the early 1980s. Only in recent months have home sales increased; with one exception, home sales declined on a year-over-year basis every month from October 2005 to April of this year. And sales are increasing in part because of the continuing decline in prices—the median sales price has fallen in 24 straight months, with double-digit declines in six of the last ten months. Mortgages entering foreclosure have jumped from 0.2% of all loans in mid-2006 to 1.3% of all loans in the second quarter of 2009, while personal bankruptcies have increased more than 40% from 2008 levels.

While many economists now believe the recession may have ended, it will likely be several months, if not longer, before that determination is official. Nonetheless, expectations are for continued job losses nationally through mid-2010, with declines in personal income through at least the end of 2009. Similarly, expectations are that jobs and income will not resume growth until the middle of next year. Employment is forecast to drop 2.9% in 2009, approaching the 3.3% loss of jobs during the 1991 recession. As employers have cut jobs and instituted pay reductions and furloughs, wage and salary income is projected to decline 2.1%. A decline of any magnitude will be only the third since 1949, with the other two in that year (-0.25%) and 1954 (-0.9%). Total personal income (in current dollars) is expected to fall by 0.7%, which would be the first decline on record. Employment is expected to continue to decline in 2010, though as employers restore hours and start hiring towards the end of the year, income growth will improve. By 2011, the economy is expected to be functioning at relatively healthy levels, with some assistance from BRAC activity.

Maryland Economic Forecast

	2009	2010	2011
Employment	-2.9%	-0.4%	1.6%
Personal Income	-0.7%	2.5%	4.7%
Wage & Salary Income	-2.1%	2.7%	5.0%

The forecast for individual income tax revenues in fiscal year 2010 is revised downward by \$480.3 million to \$6.122 billion, a decline of 5.5% from fiscal year 2009. Much of this revision has been expected for some time, as fiscal year 2009 closed \$304 million short of the forecast, largely due to worse than expected results in April for first quarter estimated payments and final payments for tax year 2008. The likely decline in wage and salary income has led to a reduction in the rate of withholding growth from an already weak 2.7% to a decline of 0.4%. This change alone reduces the fiscal year 2010 general fund forecast by approximately \$200 million.

Corporate income tax revenues have been reduced by \$60.5 million, a decline of 10.1%, as corporate profits have fallen ten straight quarters. The forecast for profits calls for stabilization into 2010, with growth resuming afterwards. The 9.3% growth in the general fund forecast for fiscal year 2011 is the result of the end of the distribution of corporate income tax revenue to the Higher Education Investment Fund. Sales taxes are

projected to decline by 2.7% in 2010, resulting in a writedown of \$81.4 million. Sales tax receipts have declined by about 7% in recent months, but as the economy's deterioration ends, steady acceleration in collections is expected. This is particularly the case with construction-related activity, receipts from which have fallen for two consecutive years after adjusting for the increase in the sales tax rate, including a drop of about 15% in fiscal year 2009. As the economy recovers in fiscal year 2011, modest growth of 3.5% is forecast.

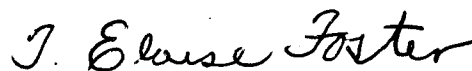
General fund lottery receipts are projected to increase 10.5% in fiscal year 2010, resulting in one of the few positive changes to the estimates. This increase, however, is a function of a return to statistically-expected prize payouts from abnormally high levels in fiscal year 2009. Sales are forecast to grow only 2.1% this year. The estimate for insurance premium taxes has been reduced by \$29.5 million, reflecting the shortfall in fiscal year 2009. Receipts fell 8.8% last year, more than double the second largest decline, in fiscal year 1992. As was the case then, businesses have reduced spending on property and casualty insurance, and premium written for life insurance has fallen off sharply. The tobacco tax forecast has been written down \$18.9 million, reflecting a decline of 6.2%. Based on cigarette pack sales over the past five months, it appears that Maryland's \$1 per pack tax increase effective January 1, 2008, and the federal tax increase of 62 cents per pack effective April 1, 2009 have had a larger impact on sales than expected. The forecast for interest income has been reduced by \$35.0 million, as interest rates are projected to fall yet lower through fiscal year 2010 and the State's balances are very low.

Overall, general fund revenues are now projected to decline by 4.5% in fiscal year 2010, and to grow by a modest 3.4% in fiscal year 2011. The members of the Board recognize all the difficult steps taken to keep the State's budget in balance to date. The \$736 million in budget actions approved by the Board of Public Works in July and August have allowed the State to address the FY 2009 revenue shortfall and begin addressing the FY 2010 shortfall. The Board stands ready to assist you in keeping the State's budget balanced. We will keep you informed of major developments.

Sincerely,



Peter Franchot


Nancy K. Kopp

T. Eloise Foster

Maryland General Fund Revenues
Fiscal Years 2009 - 2011
(\$ in thousands)

	FY 2009			FY 2010				FY 2011	
	Official Estimate	Actual	Difference	Current Estimate	September Revision	Difference	% Growth	September Estimate	% Growth
INCOME TAXES									
Individual	6,781,487	6,477,157	(304,330)	6,602,155	6,121,847	(480,308)	-5.5%	6,358,220	3.9%
Corporations	582,316	550,740	(31,576)	555,510	495,013	(60,497)	-10.1%	541,071	9.3%
Total	7,363,803	7,027,897	(335,906)	7,157,665	6,616,860	(540,805)	-5.8%	6,899,291	4.3%
SALES AND USE TAXES	3,610,951	3,620,431	9,480	3,605,424	3,523,871	(81,553)	-2.7%	3,647,243	3.5%
STATE LOTTERY RECEIPTS	455,843	473,206	17,363	507,103	522,975	15,873	10.5%	530,412	1.4%
OTHER REVENUES									
Business Franchise Taxes	209,236	201,378	(7,858)	216,123	216,123	-	7.3%	216,123	0.0%
Tax on Insurance Companies	298,340	275,203	(23,137)	305,232	275,753	(29,479)	0.2%	281,268	2.0%
Death Taxes	226,555	205,492	(21,063)	177,638	180,209	2,571	-12.3%	178,274	-1.1%
Tobacco Tax	413,773	405,579	(8,194)	399,120	380,250	(18,870)	-6.2%	375,672	-1.2%
Alcoholic Beverages Excises	29,009	29,168	159	29,614	29,512	(102)	1.2%	29,866	1.2%
Motor Vehicle Fuel Tax	6,500	6,500	-	8,386	8,386	-	29.0%	-	-
District Courts	88,323	89,379	1,056	88,750	88,579	(171)	-0.9%	87,515	-1.2%
Clerks of Court	32,445	40,514	8,069	32,801	42,015	9,214	3.7%	40,172	-4.4%
Hospital Patient Recoveries	94,732	96,462	1,730	66,396	65,716	(680)	-31.9%	67,060	2.0%
Interest on Investments	103,000	83,050	(19,950)	73,000	38,000	(35,000)	-54.2%	48,500	27.6%
Miscellaneous	307,946	338,302	30,356	329,769	326,000	(3,769)	-3.6%	332,520	2.0%
Total	1,809,859	1,771,024	(38,835)	1,726,829	1,650,543	(76,286)	-6.8%	1,656,970	0.4%
TOTAL CURRENT REVENUES	13,240,456	12,892,558	(347,898)	12,997,020	12,314,249	(682,771)	-4.5%	12,733,916	3.4%
Extraordinary Revenues	7,917	7,917	-	-	-	-		-	
GRAND TOTAL	13,248,373	12,900,475	(347,898)	12,997,020	12,314,249	(682,771)	-4.5%	12,733,916	3.4%