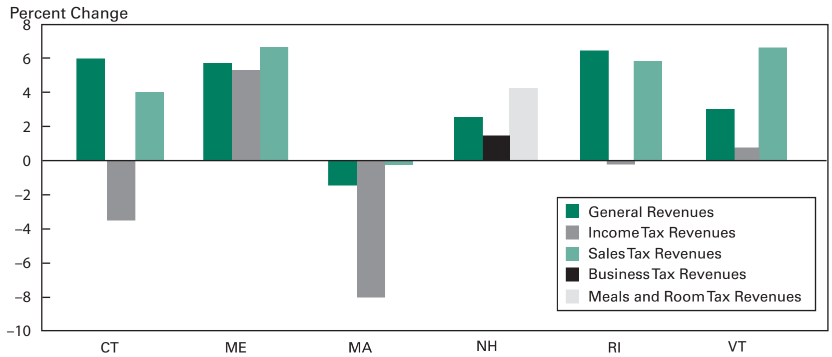
Across *the* Region

Year-to-date revenues for the first four months of FY2003 were above their FY2002 level in most New England states. Hit hard by dramatically diminished tax receipts and/or increased spending pressures, all six states closed FY2002 with deficits that had to be eliminated by end-of-the-year fiscal measures. The improved revenue collections for the first four months of FY2003 were welcome. General revenues were up in Connecticut, Maine, New Hampshire, Rhode Island, and Vermont. Sales tax receipts, driven in large part by car purchases induced by manufacturers' offers of zero percent financing, were up in Connecticut, Maine, Rhode Island, and Vermont; meals and rooms tax receipts were up in New Hampshire. Personal income tax collections were mixed; although higher in Maine and Vermont, they were down slightly in Rhode Island and sharply in Connecticut and Massachusetts.

Total Revenues and Revenues from the Two Largest Taxes, New England States

Collections through October FY2003, Percent Change from FY2002



Six-State Review

Connecticut

The fiscal situation in Connecticut for the second year of its biennial budget cycle, although not as bad as the first, continues to look grim. Connecticut ended FY2002 with a budget deficit of $817 million, or 6.8 percent of general fund spending. Based on financial data collected through November 2002, Connecticut's state comptroller projects that the state will end FY2003 with a deficit of $414.9 million.[1] This estimate, released in December, is $23 million higher than an earlier estimate, reported in November. The increase is largely attributable to lower than expected personal income tax collections and higher than expected spending.

The state's personal income tax receipts (the state's largest source of own-source revenue) were down nearly 4 percent through the first four months of FY2003. These negative numbers were partially offset by larger than expected gains in collections from the sales tax (the state's second largest source of own-source revenue) and corporate profits tax – up roughly 4 percent and 3 percent, respectively, for the same time period.

Expenditures were running roughly 1 percent over budgeted levels as of November. More than 80 percent of the $131.7 million in overspending is attributable to the rising cost of health care, generally, and Medicaid costs, specifically.

In FY2002, legislators voted to use the balance of the $595 million remaining in the state's rainy day fund to

[1]State of Connecticut, Office of the State Comptroller, "Wyman Projects Budget Deficit of $414.9 Million," press release dated December 2, 2002.

cover a portion of the deficit. Lawmakers additionally authorized the issuance of $220 million in economic recovery notes during FY2003. A variety of actions, including spending cuts and tax increases, were taken to address the remaining shortfall. With rainy day funds now depleted, Connecticut may face another round of difficult fiscal decisions should revenues not improve during the remainder of the fiscal year.

Maine

Maine took in $671 million in general fund revenues during the first four months of FY2003 – $22 million, or 3.3 percent, over projections. Total revenues grew this much because personal income tax receipts significantly exceeded budgeted amounts for both the month of October and the fiscal year to date. For the month of October, personal income tax receipts totaled $94 million – 16 percent more than the $81 million that had been projected. For July through October, personal income tax collections totaled more than $307 million – 7.6 percent more than the $285 million that had been budgeted.

Year-to-date performance of the state's second largest revenue source, the sales and use tax, was weaker. For July through October, receipts from the sales and use tax totaled $247.1 million, slightly more than the $243.7 million that had been projected.

In the opinion of Maine's commissioner of administration and financial services, the state's increased personal income tax collections through October do not mark the beginning of a positive revenue trend; rather, they should be viewed as an intertemporal displacement expected to reverse itself by January. The state still faces a challenging fiscal situation.

Maine closed the first year of the biennium (FY2002) with a deficit of $93 million in its general fund budget. An additional deficit of $150 million is predicted for FY2003. Thus, absent remedial measures, the state will likely end its biennial budget cycle in June 2003 with a $243 million deficit, 4.5 percent of its $5.3 billion general fund budget.

Massachusetts

Massachusetts is in difficult financial straits. The state collected $20.7 billion in revenues in FY2002, down $1.2 billion from FY2001 levels. This revenue erosion has continued into FY2003. Through October, the Commonwealth collected $4.6 billion in general revenues, down 1.8 percent from the same months in FY2002. For both FY2002 and FY2003, the decrease is largely attributable to dramatically falling personal income tax receipts. Massachusetts collected $2.5 billion in personal income taxes during the first four months of FY2003, down 8 percent from the same time period a year earlier. Additionally, sales tax receipts in the state were down by 0.2 percent.

Before budget balancing actions, the Commonwealth faced a budget deficit of $2.3 billion for FY2002. Continuing revenue declines during the first few months of FY2003, coupled with increased spending pressures, are expected to combine to produce a deficit for FY2003 that could exceed $500 million, and it is not impossible that FY2004 could see the deficit again swell beyond $2 billion. The situation is complicated by the fact that balances in the state's major reserve accounts – the budget stabilization fund and the tobacco settlement fund – were tapped to the tune of $1.5 billion in FY2002 and have now dwindled to $300 million and $500 million, respectively.

Both the governor-elect and the speaker of the house have stated publicly that tax increases will not be considered. Spending cuts, however, are being widely discussed. The chairman of the House Appropriations Committee has warned that local aid may be cut by as much as 20 percent, and the governor-elect is looking for roughly $1 billion in inefficiencies to cut in state government.

New Hampshire

The Granite State, unlike the rest of New England, does not impose a personal income tax. Instead, the state relies predominantly on business taxes and a rooms and meals tax.

The $19.2 million in business tax revenues that New Hampshire collected in October fell short of expectations by $2.2 million. Year-to-date through October, the tax yielded $97.5 million. Although up approximately 1.5 percent from last year, these collections were below estimates by $14.3 million, or 13 percent. Since business taxes fund 30 percent of New Hampshire's total general and educational funds, these low returns – relative to expectations – could cause significant fiscal pain for the state should collections not improve by the end of the fiscal year.

The state's second largest source of general revenue, the meals and rooms tax, has also performed below expectations. For July through October, New Hampshire collected $15.5 million from this tax, short of plan by $6.6 million. October revenues from the tax were only 3 percent higher than last October's numbers. Officials had believed that last October's numbers were artificially deflated as a result of the events of September 11, so the lack of significant improvement is troubling to state budget officials.

Although New Hampshire was the only New England state to enjoy year-over-year revenue growth from FY2001 to FY2002, it still ended the first year of its biennial budget cycle with a deficit of $62.6 million, 2.7 percent of budgeted expenditures for the FY2002/2003 biennial budget cycle. Even after corrective action, the state still carried over a $10 million deficit into the current fiscal year. Officials have indicated that this gap will probably be closed through the use of reserves, but if expected revenues should not materialize in FY2003, further action may be necessary.

Rhode Island

Rhode Island's general fund revenues were up by 6.4 percent for the first four months of FY2003 compared with the same period in FY2002. Growth, however, was slower than projected; officials had forecast a 6.9 percent increase.

Personal income tax collections for July through October were down 0.2 percent compared with the same period in FY2002. This decline is attributable, in large part, to a surge in refunds. Additional refunds totaling $6.5 million were made to taxpayers who erroneously overpaid following the introduction of new tax forms.[2]

For the first four months of FY2003, sales and use tax revenues were up by 5.8 percent on a year-over-year basis, exceeding the official estimate of 4.9 percent. Auto sales were probably responsible. Receipts collected by the Registry of Motor Vehicles, including sales taxes and various fees and charges, were up 15.6 percent. This growth, the state's budget office believes, was a function of the zero percent financing offered by automobile manufacturers and is not indicative of a long-term, positive revenue trend. In fact, the budget office sees some evidence of softening in taxable retail sales for FY2003.

Despite the overall growth in Rhode Island's revenues during the early months of FY2003, the state still expects to face a substantial budget deficit, so much so that officials have already set aside $77.3 million in proceeds from its tobacco securitization funds toward closing whatever gap may arise.

Vermont

Vermont is the one positive budgetary scene in an otherwise bleak New England fiscal landscape. Both the state's income and sales tax receipts surged unexpectedly in October, creating a budget surplus. Four months into FY2003, revenues were ahead of expectations by $10 million, or 16 percent.

The state forecast $67.7 million in October revenue and collected $78.5 million. Sales and use tax receipts were particularly strong. Collections for the month, according to Vermont's secretary of administration, were 10.9 percent higher than anticipated and, cumulatively through the first four months of FY2003, 4.4 percent above expectations.

Income tax collections were also remarkably robust. The state collected $36.2 million in personal income withholding taxes in October, 13 percent more than expected. Although the year is young, this increase is a positive sign for a state hit particularly hard by job losses throughout FY2002.

All in all, Vermont has experienced quite a turnaround from the start of the fiscal year. In June, lawmakers approved a $3.3 billion budget for FY2003, but eroding revenues quickly threw it of balance by roughly $39 million. In response, the state passed a corrective package of excise tax increases and spending cuts, including workforce reductions. These actions, coupled with increased tax collections, have turned Vermont's fiscal situation around. If the recent strength in revenues holds, Vermont may be the only New England state to finish FY2003 with a small surplus. **FF**

[2] New tax forms were introduced in Rhode Island so the state's income tax would no longer piggyback on the federal income tax system.

New England Fiscal Facts

Federal Reserve Bank of Boston
P.O. Box 2076
Boston, MA 02106-2076
Change Service Requested

Bulk Rate
U.S. Postage
Paid
Danvers, MA
Permit No. 355