

**REVENUE STABILIZATION FUND**

**CALCULATIONS  
FOR THE YEAR ENDED  
JUNE 30, 2010**

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**Auditor of  
Public Accounts**

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**COMMONWEALTH OF VIRGINIA**



# Commonwealth of Virginia

Auditor of Public Accounts  
P.O. Box 1295  
Richmond, Virginia 23218

Walter J. Kucharski, Auditor

October 28, 2010

Dear General Assembly Member:

## REVENUE STABILIZATION FUND

This Office is providing a report of the required calculations for the Revenue Stabilization Fund. Appendix A provides historical information concerning the establishment of the Revenue Stabilization Fund and the requirements surrounding it.

### CALCULATION OF MAXIMUM FUND ALLOWED

<u>Years</u>	<u>Tax Revenues (In Thousands)</u>
2008	\$14,227,165
2009	\$13,246,119
2010	\$13,159,414
Average for three years	\$13,544,233
Maximum fund allowed (10% of average)	\$ 1,354,423

During the 2009 and 2010 sessions, the General Assembly passed legislation proposing an amendment to the Virginia Constitution increasing the maximum fund allowed from ten percent to 15 percent of the Commonwealth's certified average annual tax revenues for the three fiscal years immediately preceding the current year. This proposed Constitutional amendment is on the November 2, 2010, ballot.

### CALCULATION OF CONSTITUTIONAL DEPOSIT

As a result of changes in the tax structure enacted by the 2004 General Assembly, there have been both increases and decreases in the taxes used to perform the calculation of the mandatory deposit into the Revenue Stabilization Fund. The Virginia Constitution permits the exclusion, in whole or in part, of the growth in tax revenues resulting from increases in tax rates or the repeal of exemptions from the computation of the mandatory deposit for a period up to six years after the effective year of the change. Therefore, beginning with fiscal year 2005 and continuing through fiscal year 2010, we performed two calculations: one including the effect of the tax increases and exemption repeals and the other excluding the effect of the tax increases and exemption repeals. This is the last year we will perform two calculations, as it is the sixth year in the six year period. For fiscal year 2010, neither calculation method requires a deposit to the fund.

Calculation: Including Tax Increases and Exemption Repeals

Including the effect of tax increases and exemption repeals, certified tax revenues decreased by 0.65 percent between fiscal years 2009 and 2010, and the average revenue growth for the preceding six years was 6.02 percent. Under the provisions of the Revenue Stabilization Fund, the difference between last year's revenue decline and the average growth is a *negative* 6.67 percent.

Since the difference between last year's revenue decline and the average growth is negative, there is no requirement to make a deposit to the fund. Exhibit 1 provides the certified tax revenue amounts used in the calculation, which includes the effect of the tax increases and exemption repeals.

Calculation: Excluding Tax Increases and Exemption Repeals

Excluding the effect of tax increases and exemption repeals, certified tax revenues decreased by 0.94 percent between fiscal years 2009 and 2010, and the average growth for the preceding six years was 5.17 percent. Under the provisions of the Revenue Stabilization Fund, the difference between last year's revenue decline and the average growth is a *negative* 6.11 percent.

Since the difference between last year's revenue decline and the average growth is negative, there is no requirement to make a deposit to the fund. Exhibit 1 provides the certified tax revenue amounts used in the calculation, which excludes the effect of the tax increases and exemption repeals.

To perform this calculation, we used estimates provided by the Department of Taxation (Taxation) for the effect of tax increases and exemption repeals on certified tax revenues for fiscal year 2010. We reviewed Taxation's methodology and data to arrive at the estimated amounts to ensure the amounts were reasonable. Taxation could not establish a methodology to estimate the additional tax revenue associated with the elimination of the common carrier sales and use tax exemption; therefore, we could not eliminate the effect of this tax change from the calculation. Below is Taxation's estimate of the effect of tax increases and exemption repeals.

**FISCAL YEAR 2010 EFFECT OF TAX INCREASES AND EXEMPTION REPEALS  
(IN THOUSANDS)**

<u>Tax Source</u>	<u>Tax Category Affected</u>	<u>Amount</u>
State sales and use tax rate	State sales and use	\$ 446,599*
Income adjusted age deduction	Individual and fiduciary income	73,700
Public service corporation exemption	State sales and use	56,100
Delaware holding companies deduction	Corporate income	39,900
Pass-through entities tax base	Individual and fiduciary income	8,600

\* Amount based on actual collections as recorded in the Commonwealth Accounting and Reporting System.

Fiscal Year 2010 Activity

In June 2010, in accordance with Item 265 E.2 of Chapter 872 of the 2010 Acts of Assembly, there was a withdrawal of \$295,096,195 from the Fund. There was no deposit to the Revenue Stabilization Fund in fiscal year 2010. Exhibit 2 provides the funding progress of the Fund through June 30, 2010.

## **CALCULATION OF STATUTORY DEPOSIT**

Section 2.2-1829 of the Code of Virginia, as discussed in Appendix A, requires the Governor to include an additional deposit to the Revenue Stabilization Fund in his budget recommendations, if certain conditions occur. Under both calculation methodologies, as shown in Exhibit 3, the growth of certified tax revenues does not meet any of the required conditions. Therefore, the Governor does not need to include an additional deposit in his budget recommendations.

## **CALCULATION OF WITHDRAWAL**

Article X, Section 8 of the Virginia Constitution, as discussed in Appendix A, establishes the requirements for making a withdrawal from the Revenue Stabilization Fund. There are no pending withdrawals from the Fund. However, we have included the information below to assist the General Assembly in considering future withdrawal requests.

A withdrawal from the Fund can occur only if general fund revenues appropriated exceed the revised general fund forecast by more than two percent of certified tax revenues collected in the most recently ended fiscal year. The two percent threshold based on fiscal year 2010 collections is \$263,188,286. In addition, a withdrawal from the Fund can compensate for no more than one-half of the difference between the total general fund revenues appropriated and a revised general fund revenue forecast during a subsequent regular or special legislative session. Finally, a withdrawal from the Fund cannot exceed more than one-half the balance of the Fund. Half of the balance of the Fund as of June 30, 2010, is \$147,579,473.

All actions withdrawing funds from Revenue Stabilization Fund are subject to review and approval by the General Assembly. Exhibit 4 contains detailed information showing the calculations of the amounts above.

## **PROJECTED DEPOSITS AND BALANCES**

To provide information to the General Assembly on the impact of future revenue increases, we have performed pro forma calculations on projected deposits to the Fund using forecasted revenues for fiscal years 2011 through 2016 as shown in Exhibit 5. While there is no mandatory deposit projected for the fiscal year 2011 revenue forecast, there are projected mandatory deposits for forecasted revenues for fiscal years 2012 through 2016. Under certain circumstances, there are statutory requirements for additional deposits; however, none of these conditions occur using the projected revenue forecasts for fiscal years 2011 through 2016.

The Fund will experience growth beginning in fiscal year 2014, when the mandatory deposit projected for 2012 forecasted revenues will occur, but the fund will not reach its maximum allowed level through 2016.

Should you have any questions concerning this information, please contact me.

AUDITOR OF PUBLIC ACCOUNTS

Enclosure

SAH:clj

**Exhibit 1**

**CALCULATIONS USED FOR THE REVENUE STABILIZATION FUND  
INCLUDING THE EFFECT OF TAX INCREASES AND EXEMPTION REPEALS  
(IN THOUSANDS)**

Tax Revenue Required for Computation

Years	Individual and Fiduciary Income Taxes	Corporate Income Tax	State Sales and Use Taxes	Totals	Average Annual Percentage Change	Preceding Six Year Annual Average
2004	7,430,870	434,493	2,582,797	10,448,160	10.50%	5.36%
2005	8,352,488	616,690	3,067,521	12,036,699	15.20%	5.22%
2006	9,264,985	867,116	3,029,949	13,162,050	9.35%	6.05%
2007	9,787,786	879,575	3,274,286	13,941,647	5.92%	5.62%
2008	10,117,132	807,852	3,302,181	14,227,165	2.05%	6.14%
2009	9,481,256	648,032	3,116,831	13,246,119	(6.90)%	7.21%
2010	9,088,732	806,473	3,264,209	13,159,414	(0.65)%	6.02%

**CALCULATIONS USED FOR THE REVENUE STABILIZATION FUND  
EXCLUDING THE EFFECT OF TAX INCREASES AND EXEMPTION REPEALS  
(IN THOUSANDS)**

Tax Revenue Required for Computation

Years	Individual and Fiduciary Income Taxes	Corporate Income Tax	State Sales and Use Taxes	Totals	Average Annual Percentage Change	Preceding Six Year Annual Average
2004	7,430,870	434,493	2,582,797	10,448,160	10.50%	5.36%
2005	8,303,557	584,108	2,742,495	11,630,160	11.31%	5.22%
2006	9,201,966	842,116	2,558,328	12,602,410	8.36%	5.40%
2007	9,716,486	854,575	2,778,779	13,349,840	5.93%	4.80%
2008	10,030,532	777,352	2,810,274	13,618,158	2.01%	5.33%
2009	9,398,156	607,633	2,647,955	12,653,744	(7.08)%	6.40%
2010	9,006,432	766,573	2,761,510	12,534,515	(0.94)%	5.17%

**Exhibit 2**

**SCHEDULE OF FUNDING PROGRESS**

	Amounts ( <u>In Thousands</u> )
Balance at June 30, 2009	\$ 575,064
June 2010 withdrawal	(295,096)
Interest earned during fiscal year 2010	<u>15,191</u>
Total in fund at June 30, 2010*	<u>\$ 295,159</u>
Percentage of maximum fund allowed	22%

\*A fiscal year 2011 deposit is not required based on fiscal year 2009 calculations, and a fiscal year 2012 deposit is not required based on fiscal year 2010 calculations (both including and excluding the effect of tax increases and exemption repeals).

**Exhibit 3**

**CALCULATIONS FOR STATUTORY DEPOSIT**  
(As required by Section 2.2-1829 of the Code Of Virginia)

	<u>Excluding Effect of Tax Increases and Exemption Repeals</u>	<u>Including Effect of Tax Increases and Exemption Repeals</u>
Growth of certified tax revenues collected in most recently ended fiscal year	(0.94)%	(0.65)%
Average revenue growth for the preceding six years multiplied by 1.5	7.76%	9.03%
Increase of estimated general fund revenues for the fiscal year in which the deposit is to be made over general fund revenues for the immediately preceding fiscal year*	2.56%	2.56%

See the Statutory Deposit Section in Appendix A for conditions triggering a deposit.

\*Calculated based on the general fund revenue estimate in Chapter 874 of the 2010 Acts of Assembly.

**Exhibit 4**

**CALCULATIONS FOR WITHDRAWALS**

Calculation of 2 Percent Threshold

	<u>Threshold Amounts (in thousands)</u>
Certified tax revenues collected in most recently ended fiscal year (2010)	\$13,159,414
2 percent of certified tax revenues (threshold established by Virginia Constitution)	\$ 263,188

Calculation of One Half the Balance of the Fund

	<u>Balance Amounts (in thousands)</u>
Revenue Stabilization Fund Balance at June 30, 2010	\$295,159
50 percent of the balance of the Fund	\$147,579



**Exhibit 5**

**PROJECTED DEPOSITS AND BALANCES**

Calculations

We performed our calculations using the Official General Fund Forecast as presented in Chapter 874 of the 2010 Acts of Assembly for fiscal years 2011 and 2012 and the December 2009 General Fund Forecast for growth percentage projections for fiscal years 2013 through 2016. See Appendix A for conditions triggering a Mandatory or Statutory deposit.

**Projected Mandatory Deposits: Fiscal Years 2011 through 2016 (in thousands)**

	Fiscal Year					
	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Corporate Income Tax	\$ 792,800	\$ 838,400	\$ 868,582	\$ 885,085	\$ 923,144	\$ 934,222
Individual and Fiduciary Income Taxes	9,587,700	10,136,500	10,764,963	11,292,446	11,857,068	12,473,636
State Sales and Use Taxes	<u>3,089,700</u>	<u>3,190,000</u>	<u>3,329,497</u>	<u>3,476,219</u>	<u>3,639,836</u>	<u>3,800,234</u>
Total Projected Certified Tax Revenue	<u>\$13,470,200</u>	<u>\$14,164,900</u>	<u>\$14,963,042</u>	<u>\$15,653,750</u>	<u>\$16,420,048</u>	<u>\$17,208,092</u>
Average Annual Percentage Change	2.36%	5.16%	5.63%	4.62%	4.90%	4.80%
Preceding Six Year Annual Average	<u>4.16%</u>	<u>2.02%</u>	<u>1.32%</u>	<u>1.28%</u>	<u>1.70%</u>	<u>3.67%</u>
Difference	<u>(1.80)%</u>	<u>3.14%</u>	<u>4.31%</u>	<u>3.34%</u>	<u>3.19%</u>	<u>1.13%</u>
<b>Required Mandatory Deposit</b>	<b>No Deposit</b>	<b>\$222,058</b>	<b>\$322,553</b>	<b>\$261,485</b>	<b>\$262,067</b>	<b>\$97,300</b>
<b>Deposit Year</b>	<b>N/A</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>

**Projected Statutory Deposits: Fiscal Years 2011 through 2016 (in thousands)**

	Fiscal Year					
	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Growth of certified tax revenues collected in most recently ended fiscal year	2.36%	5.16%	5.63%	4.62%	4.90%	4.80%
Average revenue growth for the preceding six years multiplied by 1.5	6.24%	3.03%	1.98%	1.91%	2.55%	5.50%
Increase of estimated general fund revenues for the fiscal year in which the deposit is to be made over general fund revenues for the immediately preceding fiscal year	4.93%	5.20%	4.30%	4.60%	4.50%	N/A*
<b>Required Statutory Deposit</b>	<b>No Deposit</b>	<b>No Deposit</b>	<b>No Deposit</b>	<b>No Deposit</b>	<b>No Deposit</b>	<b>No Deposit</b>

\*The difference of estimates of General Fund revenues between the fiscal year in which the deposit is to be made and the immediately preceding fiscal year could not be calculated for fiscal year 2016 because the growth projections are not available for fiscal year 2017.

**Projected Revenue Stabilization Fund Balance (in thousands)**

	Fiscal Year					
	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Revenue Stabilization Fund Balance*	\$ 295,159	\$ 295,159	\$ 295,159	\$ 517,217	\$ 839,770	\$1,101,255
Maximum Fund Allowed - Current 10% Limitation	\$1,354,423	\$1,329,191	\$1,359,817	\$1,419,938	\$1,492,723	\$1,567,895
Maximum Fund Allowed - Proposed 15% Limitation	\$2,031,635	\$1,993,787	\$2,039,726	\$2,129,907	\$2,239,085	\$2,351,842

\* Assumes no withdrawals and does not include projected interest earnings.

## APPENDIX A HISTORICAL INFORMATION

### Mandatory Deposit

Article X, Section 8 of the Virginia Constitution and the enabling legislation established the Revenue Stabilization Fund, and require this Office to report to the General Assembly the following:

1. certified tax revenues for the calculation of the Revenue Stabilization Fund;
2. the maximum size allowed of the Revenue Stabilization Fund; and
3. the amount of the mandatory deposit to the fund.

The amount in the Revenue Stabilization Fund is not to exceed ten percent of the Commonwealth's average annual tax revenues derived from taxes on income and retail sales as certified by our Office for the three fiscal years immediately preceding. The General Assembly is required to make deposits to the Revenue Stabilization Fund to equal at least 50 percent of the total of: certified tax revenues for the most recently ended fiscal year, multiplied by the difference between the annual percentage increase in certified tax revenues collected for the most recently ended fiscal year, and the average annual percentage increase in certified tax revenues collected for the six fiscal years immediately preceding the most recently ended fiscal year.

Item 256 A of Chapter 874 of the 2010 Acts of Assembly requires this Office to report to the General Assembly on or before November 1<sup>st</sup> of each year.

### Statutory Deposit

Legislation passed during the 2003 General Assembly Session added a requirement for an additional deposit to the Revenue Stabilization Fund under certain conditions. The provisions of this change were effective July 1, 2003. The conditions are as follows:

1. a growth of the certified tax revenues collected in the most recently ended fiscal year of eight percent or greater than the certified tax revenues collected for the immediately preceding fiscal year;
2. a growth of the certified tax revenues for the most recently ended fiscal year greater than 1.5 times the average percentage increase in the certified tax revenues collected in the six fiscal years immediately preceding the most recently ended fiscal year; and
3. the estimate of general fund revenues prepared in accordance with Section 2.2-1503 of the Code of Virginia for the fiscal year in which the deposit is to be made is at least five percent greater than the actual general fund revenues for the immediately preceding fiscal year.

If the above conditions exist, the Governor must include in his budget recommendations, submitted to the General Assembly in the subsequent session, an amount equal to at least 25 percent of the product of the certified tax revenues collected in the most recently ended fiscal year, multiplied by the difference between the annual percentage increase in the certified tax revenues collected for the most recently ended fiscal year and the average annual increase in the certified tax revenues collected in the six fiscal years immediately preceding the most recently ended fiscal year.

## Withdrawals

Per Article X, Section 8 of the Virginia Constitution, the General Assembly may appropriate an amount for transfer from the Fund to compensate for no more than one-half of the difference between the total general fund revenues appropriated and a revised general fund revenue forecast presented to the General Assembly prior to or during a subsequent regular or special legislative session. However, no transfer shall be made unless the general fund revenues appropriated exceed such revised general fund revenue forecast by more than two percent of certified tax revenues collected in the most recently ended fiscal year. Furthermore, no appropriation or transfer from such fund in any fiscal year shall exceed more than one-half of the balance of the Revenue Stabilization Fund.