Budget Footnotes

A NEWSLETTER OF THE OHIO LEGISLATIVE SERVICE COMMISSION JUNE 2004

FISCAL OVERVIEW

— Allan Lundell

The U.S. economy continued to expand at a vigorous pace in May. Total nonfarm payroll employment increased by 248,000 in May, following increases of 353,000 in March and 346,000 in April. Employment has increased by 1.2 million in 2004 and is up by 1.4 million from the cyclical low reached in August 2003. The estimate of first-quarter growth in real gross domestic product was revised up from 4.2% to 4.4%, and forecasts are for strong growth to continue. As the economy moves along in expansion mode, policy concerns will shift from insufficient employment to increasing inflation.

For May, total General Revenue Fund (GRF) revenue was $385 million below the original estimate and $335 million below the revised estimate. As expected, the April revenue bubble created by the accelerated processing of income tax returns deflated in May. April income tax revenues were boosted as returns expected to be processed in May were processed in April. However, this April boost reduced the amount of revenue reported for May. The Memorial Day holiday may have also affected the amount of revenue from the corporate franchise tax and cigarette tax reported for the month of May. Payments made over the Memorial Day weekend were reported not for May, but for June. This appears to be true for the domestic insurance tax too. As of May 28, the last working day of May, domestic insurance tax receipts for the month were $131 million, the amount reported in Table 2. On June 1, reported receipts for this tax were $33 million, an amount that almost erased the negative variance for May.

Through May, total GRF revenue is $255 million (1.2%) below the original estimate. Total tax revenue is $248 million (1.5%) below estimate and revenue from the major taxes is $140 million (0.9%) below estimate. Revenue from the "other" taxes, mostly the cigarette tax and the estate tax, is $109 million (9.7%) below estimate.[1] Compared to the revised estimates, total GRF revenue is $3 million (0.01%) below estimate, state-source revenue is $39 million (0.2%) below estimate, tax revenue is $0.5 million (0.003%) above estimate, and revenue from the major taxes is $69 million (0.5%) above estimate.

Volume 27, Number 10

Budget Footnotes examines the fiscal position of the state General Revenue Fund on a periodic basis.

For questions or comments regarding specific sections:

GRF Revenue:
Allan Lundell 644-7788

GRF Spending:
Steve Mansfield 728-4815

Legislative Service Commission
77 South High Street, 9th Floor
Columbus, Ohio 43215

Telephone: (614)466-3615

Table 1
General Revenue Fund
Simplified Cash Statement
($ in millions)

	Month of May	Fiscal Year 2004 to Date	Last Year	Difference
Beginning Cash Balance	-$123.1	$396.5		
Revenue + Transfers	$1,938.8	$21,408.5		
Available Resources	$1,815.7	$21,805.1		
Disbursements + Transfers	$1,985.0	$21,974.4		
Ending Cash Balances	-$169.3	-$169.3	-$542.6	$373.3
Encumbrances and Accts. Payable		$290.6	$322.1	-$31.6
Unobligated Balance		**-$459.9**	**-$864.7**	**$404.8**
BSF Balance		$180.7	$962.2	-$781.5
Combined GRF and BSF Balance		**-$279.2**	**$97.6**	**-$376.7**

Through the first 11 months of FY 2004, total GRF revenue is up $1,718 million (8.7%) compared to FY 2003. The revenue growth is almost entirely due to the increase in the state sales tax rate and an increase in federal grants. If revenue from the sales tax and federal grants is subtracted from total GRF revenue, the resulting state-source revenue from sources other than the sales tax is up $28 million (0.3%) compared to FY 2003.

Disbursements were $45 million greater than estimate in May. Fiscal year-to-date GRF disbursements are $196 million (0.9%) below estimate. Disbursements for primary and secondary education for the fiscal year are $3 million (0.1%) below estimate and disbursements for welfare and human services are $51 million (0.5%) below estimate. Disbursements for Healthcare/Medicaid are $36 million (0.4%) above estimate. Year-to-date total disbursements are up 3.8% compared to FY 2003.

As shown in Table 1, the GRF began May with a negative cash balance of -$123 million. Revenue, including transfers-in, for May was $1,939 million. Disbursements, including transfers-out, were $1,985 million. The monthly deficit of $46 million brought the fiscal year-to-date cash balance to -$169 million. Due to the timing of revenues and disbursements, the cash balance is generally negative early in the fiscal year before turning positive later in the year. If revenues and disbursements had met their original estimates, the fiscal year-to-date cash balance would have been -$111 million, $58 million higher (less negative) than the actual level. If revenues and disbursements had met their revised estimates, the fiscal year-to-date cash balance would have been -$363 million, $194 million lower than the actual level. If revenues and disbursements equal their estimates for June ($2,445 million and $1,862 million, respectively), the monthly surplus of $583 million would result in a year-end cash balance of $413 million.

The fiscal year-to-date cash balance of -$169 million is $690 million higher (less negative) than a year ago.[2] Year-to-date encumbrances of $291 million combine with the cash balance to yield an unobligated balance of -$460 million, which is $721 million higher than a year ago. Looking at just the unobligated balance indicates that the state's financial situation in terms of current-year performance has improved compared to a year ago. The $181 million balance in the Budget

Stabilization Fund (BSF) is $247 million less than a year ago, so the combined GRF and BSF balance of -$279 million is $474 million higher than it was at this time last year. If one looks at the combined GRF and BSF balance, the state's financial situation in terms of ability to withstand an economic shock has improved from a year ago but remains far from robust.

[1] The "other" or "minor" taxes are the foreign insurance tax, the domestic insurance tax, the business and property tax, the cigarette tax, the alcoholic beverage tax, the liquor gallonage tax, and the estate tax.

[2] An incorrect cell reference in the spreadsheet used by LSC to create Table 1 resulted in the reporting of the wrong amounts in the "Last Year" column in the previous editions of *Budget Footnotes* for FY 2004.

TRACKING THE ECONOMY

¾ Phil Cummins

Economic indicators during the past month continue to show the national economy expanding at a vigorous pace. Inflation-adjusted gross domestic product (GDP) growth in the first quarter was revised upward slightly to a 4.4% annual rate. Another strong quarter appears likely to be reported when the initial second-quarter estimate is released next month. Nonfarm payroll employment rose nearly 250,000 in May, the third consecutive sizable increase. Industrial production posted another strong gain last month. Purchasing managers in both the manufacturing and nonmanufacturing sectors again saw strong gains in economic activity, along with widespread cost increases and some shortages. Retail sales rose sharply in May, an indication that total consumer spending is growing at a brisk pace in the second quarter, with particular strength in durable goods. Housing market activity remains at high levels, but construction starts and home sales have slowed from their peaks. Inflation, measured by producer finished goods prices and consumer prices, jumped in May, primarily as a result of higher energy and food prices. Some prices have eased since then. The nation's central bank is widely expected to begin tightening monetary policy by increasing its target for federal funds when it meets at the end of this month.

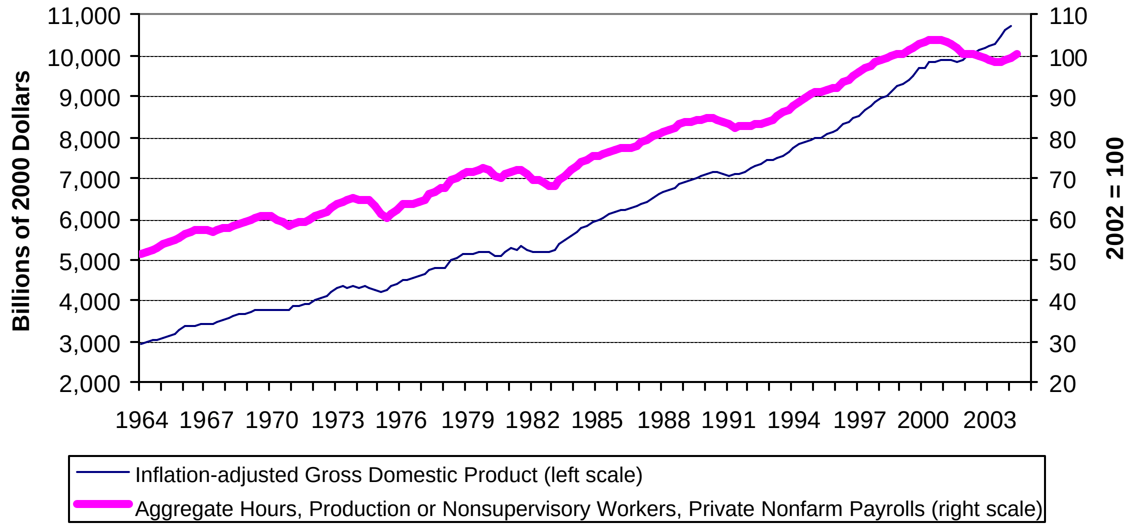
Third Consecutive Large Increase in Payroll Employment

Employment nationwide continued to expand at a rapid rate in May, while the national unemployment rate was unchanged at 5.6%. Total nonfarm payrolls rose by 248,000 in May, after even larger gains in March and April, to 1.4 million above the cyclical low reached in August 2003. Employment is still 1.3 million below its March 2001 peak. Manufacturing employment has been growing since January but remains 2.5 million lower than in March 2001. Increases in jobs this year have been widespread among industries, including mining and construction as well as several service-producing industries.

Employment in Ohio has been recovering in 2004 from what probably will be the cyclical low in December 2003. Unemployment declined in May to 327,000 people, 5.6% of the labor force, down from 5.8% in April. Total nonfarm payroll employment rose 1,100 in May from a downward revised April level, reflecting an increase in the number of jobs in industries providing service. Employment in goods-producing industries fell mainly because of a decline of 900 workers at Ohio manufacturers. From December through May, total employment rose 30,900 or 0.6%, manufacturing employment rose 1,000 or 0.1%, and nonmanufacturing employment rose 29,900 or 0.7%. Total employment last month remained 250,000 below the peak in mid-2000, and Ohio manufacturing accounted for four of every five jobs lost during this period. The peak for Ohio manufacturing employment was in 1969.

Total hours of American workers on their jobs is a key input in the production process, for which monthly estimates are released more promptly than measures of output. Aggregate hours of production or nonsupervisory workers on private nonagricultural payrolls combines data on the number of workers who are paid by the hour and on their average weekly hours. It measures hours paid, an approximation of hours worked. An index of aggregate hours for the United States is shown in Chart 1, superimposed on a plot of gross domestic product in dollars of constant purchasing power. The series on aggregate hours is not fully comparable to GDP, since the index of hours excludes some segments of the economy that are part of the broader measure, such as agriculture and the self-employed. Over the years, the aggregate hours index has grown more slowly than

Chart 1: Total Production and Worker Hours



GDP, as rising productive capability has enabled American workers to produce more for each hour of effort, making possible our rising standard of living. In past decades, slowdowns or upturns in aggregate hours frequently have coincided with similar variations in GDP. Recently, however, the aggregate hours index declined for 11 consecutive quarters, from 2001 through most of 2003, while GDP turned up following the 2001 recession and has been rising for 10 straight quarters. The aggregate hours index has been increasing briskly this year. It is plotted in Chart 1 through May, and its recent rise is an indication that GDP in the second quarter, for which official estimates are not yet available, probably also is expanding at a rapid pace.

Industrial production increased 1.1% in May, partly as a result of a 4% surge in electricity generation. The index for total manufacturing production increased 0.9%, rising to just 0.3% below its June 2000 peak, prior to the 2001 recession. Increases in manufacturing output in May were widespread among industry groups. Motor vehicle and parts production was an exception and has been trimmed in the last three months after sizable increases earlier. In spite of the substantial recovery in total manufacturing output, estimated utilization of factory productive capacity, at 76.4% in May, remains well short of levels reached in past recoveries. Growth in productive capacity was unusually rapid in the second half of the 1990s.

Purchasing Managers See Further Expansion and Rising Costs

Production, orders, backlogs, and employment rose in May at manufacturers nationwide, according to purchasing managers participating in the Institute for Supply Management's monthly survey. Those reporting higher production and new orders at their employers outnumbered those seeing reductions for the 13th consecutive month. Employment gains were most widespread since 1973. Price increases were also widespread, raising concerns among survey respondents about higher materials costs, particularly for energy. Steel, aluminum, and electronic components remained in short supply. Purchasing managers participating in a comparable survey of nonmanufacturers reported rising business activity, orders, backlogs, employment, and inventories in May, accompanied by widespread price increases and shortages of steel, cement, and a few other products.

Overview of Business Conditions

Reports in the Federal Reserve's "Beige Book," which summarizes comments on economic conditions from business people and others, indicate expanding production and sales in most parts of the country and across a broad range of industries, accompanied by rising input prices, particularly for energy-related products, building materials, and steel, as well as for health insurance for workers. Some businesses are succeeding in passing cost increases along to their customers. Hiring is picking up, though reports are mixed, and pay levels are generally steady but with scattered increases. Some car dealers noted a shift toward buying lighter, more fuel-efficient vehicles in response to high gasoline prices. In the Cleveland Federal Reserve District, which includes Ohio, manufacturers' production levels are generally higher than a year earlier, and most expect modest growth during the rest of this year. Some steel producers are operating near capacity, while others are constrained by raw materials shortages. However, steel scrap prices have declined recently. Some manufacturers have been hiring, at stable wage rates. Future hiring is expected to be limited. Retailers are resorting to markdowns less often, except at car dealers where incentives recently have been increased. The near-record pace of housing construction has slowed recently, attributed to higher interest rates. Commercial building is showing increasing signs of improvement.

Consumer Spending Growing Briskly

Total retail sales rose 1.2% from April to May, when they were 8.9% above a year earlier. Motor vehicle dealer sales strengthened after slowing in April. Service station sales jumped in May as a result of the higher cost of gasoline. Prices for gasoline have declined in June. Abstracting from these month-to-month fluctuations, on a three-month average basis, retail sales were 8.4% ahead of a year earlier in the latest period. Building materials, appliances, electronics, restaurants and bars, and furniture sales were strong, as were sales at gas stations, warehouse clubs and discounters, and nonstore retailers (Internet and catalog sales).

Though financial conditions of individual households vary widely, in the aggregate households have recovered – based on their net worth – from the downturn that began in 2000. According to estimates compiled by the Federal Reserve System, the total net worth of

Household Balance Sheet

Includes not-for-profit organizations

	1998	1999	2000	2001	2002	2003	1Q2004
	trillions of dollars, end of period						
Real estate	10.5	11.4	12.5	13.6	14.9	16.4	16.6
Other tangible assets	2.7	2.8	3.0	3.2	3.3	3.4	3.5
Deposits and currency	3.9	4.1	4.4	4.9	5.1	5.3	5.5
Credit market instruments	2.2	2.4	2.2	2.1	2.0	2.2	2.1
Corporate equities	7.1	9.2	7.7	6.3	4.7	5.9	5.8
Mutual fund shares	2.4	3.0	2.9	2.7	2.4	3.2	3.4
Pension fund reserves	8.2	9.1	9.1	8.7	8.0	9.3	9.4
Equity in noncorporate business	4.4	4.6	5.0	5.1	5.3	5.7	5.7
Other financial assets	2.3	2.6	2.7	2.7	2.6	2.9	2.9
Total assets	43.6	49.2	49.5	49.3	48.3	54.1	55.0
Home mortgages	4.1	4.5	4.8	5.3	6.0	6.7	6.9
Other liabilities	2.2	2.4	2.6	2.7	2.7	2.9	2.9
Total liabilities	6.2	6.8	7.4	8.0	8.7	9.6	9.8
Net worth	37.4	42.3	42.1	41.3	39.6	44.5	45.2

households[1] rose to a new all-time peak at the end of 2003 and increased further in this year's first quarter, rising to $45.2 trillion. Household net worth previously peaked in the first quarter of 2000 and then fell for two and one-half years. During this period, declines in the value of corporate equities held directly and through mutual funds and pension funds,[2] along with smaller declines in some other securities, more than offset large gains in real estate values and smaller increases in holdings of liquid financial assets and equity in noncorporate businesses. The stock market recovery last year and continued large gains in real estate reversed the decline in net worth. However, the estimated rate of increase in the value of household-owned real estate in the first quarter was the slowest since 1997. Household liabilities grew throughout this period, rising more rapidly than personal incomes but about in line with the rate of increase in the value of tangible assets. As interest rates fell, households refinanced mortgages, lowering the cost of the mortgages and monetizing part of their increase in home equity.

Growth of Construction Activity Mostly Residential

Housing starts fell 1% in May to a 1.97 million-unit annual rate, 5% below the recent peak in December 2003. The number of new residential units started in recent months has been the strongest since the 1970s, when government subsidies boosted multiunit construction. Single-family starts in May were 2% below November's all-time peak, in monthly statistics begun in 1959. New-home sales fell sharply in April, declining 12% from an all-time peak in March, in statistics dating from 1963. The drop was particularly sharp in the South, and declines were reported for other regions except the Midwest, where sales rose 11%. Existing home sales, reported by the National Association of Realtors, rose 2.5% in April to a near-record pace.

Residential building activity has not been as strong in Ohio as elsewhere in the nation. The number of permits for construction of new homes and apartments was higher in the first four months of 2004 than a year earlier, in Ohio and the nation as a whole, continuing the uptrend of the previous three years, as shown in Chart 2. But the number of permits issued in Ohio during January through April was 4% higher than a year earlier, much less than the 14% increase nationwide.

In the first four months of 2004, the dollar value of new construction spending in the United States was 8% higher than a year earlier. Virtually all of the increase was in the housing sector. Private residential building was 15% above a year earlier. Public construction was 4% higher than in January-April 2003. Private nonresidential building was

Chart 2: New Privately Owned Housing Units Authorized by Building Permits

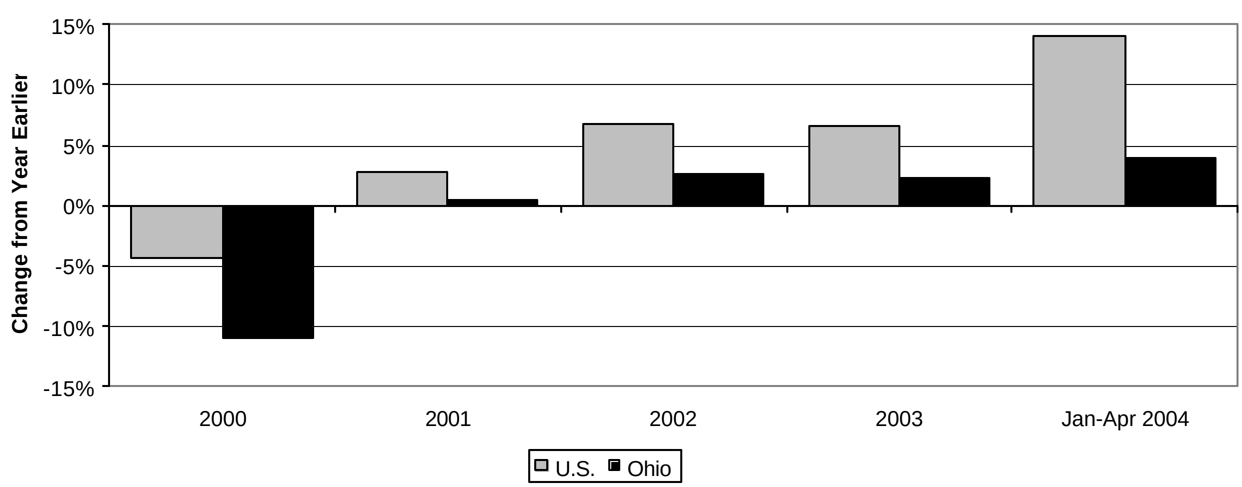
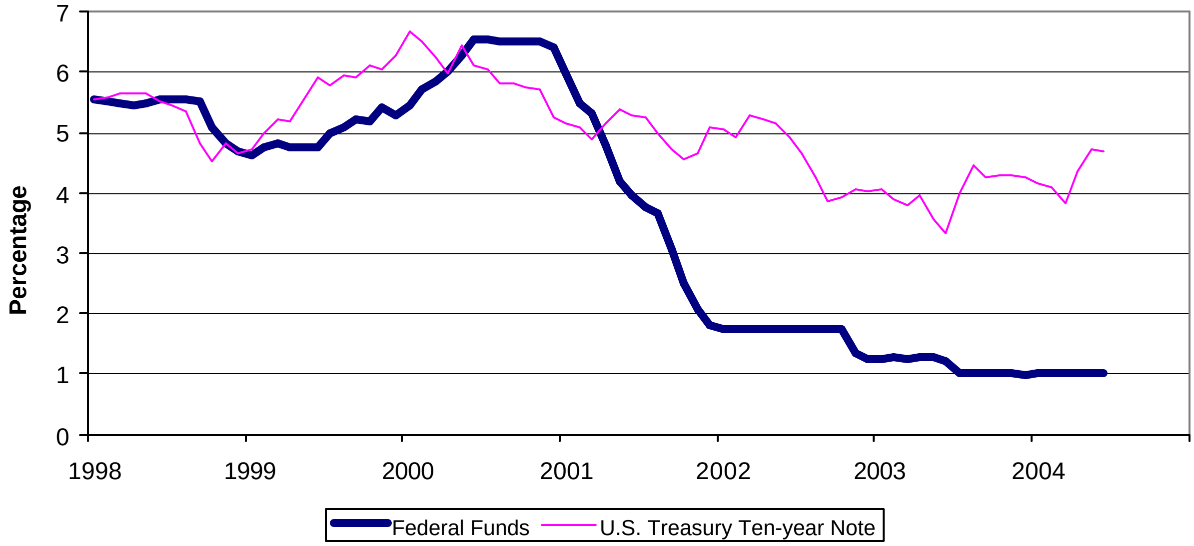


Chart 3: Selected Interest Rates



1% lower than a year earlier. Though construction of some types of nonresidential structures, including office and health care buildings, is up from a year ago, industrial projects are still declining.

Higher Energy and Food Costs Push Inflation Higher in May

Producer prices for finished goods jumped 0.8% from April to May, to 5.0% above a year earlier, the largest one-year increase in this index since 1990. Much of these increases resulted from sharply higher prices for food and energy. Excluding food and energy, producer prices for finished goods rose 0.3% last month to 1.7% above May 2003. At earlier stages of production, food and energy prices were also sharply higher in May, but prices for other goods have also risen substantially over the past year. Intermediate goods prices rose 1.1% last month to 7.1% above a year earlier. Crude goods prices rose 2.8%, to 22% above May 2003. Excluding food and energy, intermediate goods prices were 5.1% higher than a year earlier. The producer price index for crude materials excluding food and energy fell in April and May, reflecting in part an easing of scrap metals prices. Nevertheless, prices for these basic industrial materials were 22% higher than in May 2003 as a result of large increases earlier this year and in last year's second half.

The consumer price index rose 0.6% in May, the largest one-month increase in this inflation measure since 2001. Sharply higher prices for energy, +4.6%, and food, +0.9%, accounted for much of the increase. Gasoline prices rose 8.1% in May to an all-time high. In June, prices for gasoline have followed crude oil prices lower. Milk prices rose 14.7% in May, their largest one-month advance since the end of wartime price controls in 1946. Prices for meats, vegetables, and fruit also rose. The all-items consumer price index in May was 3.1% higher than a year earlier. However, excluding energy and food, consumer prices rose a more modest 0.2% in May, to 1.7% above a year earlier.

Higher Short-term Interest Rates Expected

Financial market participants appear to continue to expect that the Federal Reserve will begin raising its target for federal funds at its meeting June 29-30. Market interest rates rose in April and May in anticipation of monetary tightening. Central bank officials in speeches recently have drawn attention to the upward pressures on prices that have become more evident this year. Chairman Greenspan on June 8, after discussing several indicators of inflation, noted that the central bank still expects its monetary tightening to be "measured" but will do what is necessary to maintain price stability.[3] A few days earlier, another Federal Reserve governor emphasized that the central bank's federal funds target, currently 1%, "will not be consistent, over time, with … preserving price stability."[4] The federal funds rate and a representative longer-term market interest rate, the Treasury ten-year note yield, are shown in Chart 3. The data plotted in the chart are monthly averages, except that the values for the current month are as of June 15.

[1] These data include not-for-profit organizations in the household sector, reflecting that sector's treatment in the Federal Reserve System's flow of funds accounts on which this discussion is based.

[2] The flow of funds accounts include pension fund reserves among household assets.

[3] Remarks by Chairman Alan Greenspan at the International Monetary Conference, London, England (via satellite), June 8, 2004.

[4] Remarks by Governor Donald L. Kohn, National Economists Club meeting, Washington, D.C., June 4, 2004.

Status of the General Revenue Fund

REVENUE

— Allan Lundell and Jean Botomogno

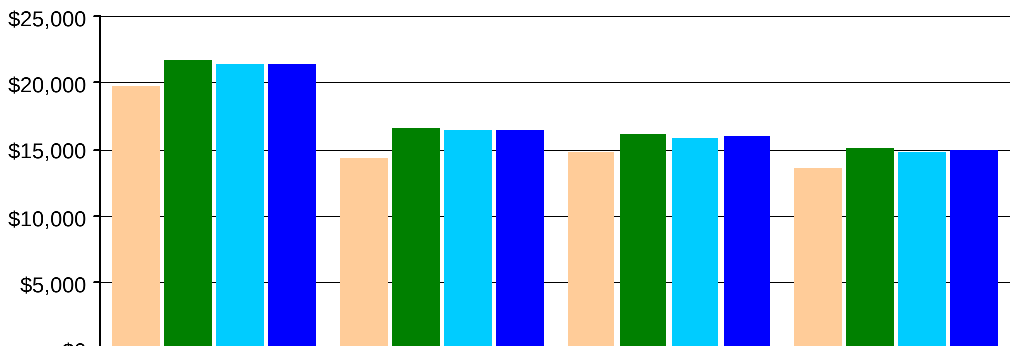
Monthly revenue collections fell below estimate in May. Total GRF revenue of $1,938.8 million was $385.2 million (16.6%) below original estimate and GRF revenue less federal grants (state-source revenue) was $417.4 million (21.2%) below estimate.[1] Total tax revenue was $346.0 million (18.5%) below estimate and revenue from the major taxes was $275.8 million (17.4%) below estimate.[2] Personal income tax revenue, which exceeded estimate by $185.6 million (18.6%) in April, fell below estimate by $185.2 million (28.8%) in May.

Through the first 11 months of this fiscal year total GRF revenue is $255.2 million (1.2%) below estimate. State-source revenue is $287.0 million (1.7%) below estimate, and total tax revenue is $248.4 million (1.5%) below estimate. Revenue from the major taxes, which is expected to account for 69% of total GRF revenue and 89% of state-source revenue for the fiscal year, is $139.8 million (0.9%) below the original estimate.

Compared to the revised estimates, total GRF revenue was $335.3 million (14.7%) below estimate in May and state-source revenue was $367.4 million (19.2%) below estimate. Total tax revenue was $305.7 million (16.7%) below estimate and revenue from the major taxes was $236.6 million (15.3%) below estimate. Year-to-date total GRF revenue is $3.0 million (0.01%) below the revised estimate and state-source revenue is $38.7 million (0.2%) below estimate. Total tax revenue is $0.5 million (0.003%) above estimate and revenue from the major taxes is $68.5 million (0.5%) above estimate.

Through May, GRF revenue is up 8.7% compared to FY 2003. State-source revenue is up 7.1% and revenue from federal grants is up 14.5%, partly due to one-time revenue. Total tax revenue is up 7.7% and revenue from the major taxes is up 9.25%. Total GRF revenue is up $1,718.0 million compared to FY 2003, but if the sales tax receipts (up $1,053.5 million) and federal

Chart 1: Year-to-Date GRF Revenue
(in millions of dollars)



	Total GRF Revenue	Total GRF Revenue less Federal Grants	Revenues from Total Taxes	Revenues from Major Taxes
FY 2003	$19,690.50	$14,294.70	$14,783.90	$13,656.00
FY 2004 Original Estimate	$21,663.70	$16,663.00	$16,167.80	$15,048.60
FY 2004 Revised Estimate	$21,411.50	$16,414.80	$15,918.90	$14,840.40
FY 2004 Actual	$21,408.50	$16,376.00	$15,919.40	$14,908.90

grants (up $636.6 million) are not counted, then state-source revenue from sources other than the sales tax is essentially flat, up just $27.9 million (0.3%). Chart 1 compares FY 2004 revenues with FY 2003 revenues and FY 2004 estimates, original and revised.

Personal Income Tax

The GRF received $458.2 million in revenue from the personal income tax in May. This amount was $185.2 million (28.8%) below original estimate. The $579.2 million in revenue collected through withholding was $6.3 million (1.1%) below estimate. Quarterly estimated payments of $10.5 million were $0.5 million (5.0%) above estimate.[3] Refunds totaled $118.2 million in May. This total was $13.2 million (12.6%) above estimate. Distributions to the three local government funds supported by the income tax were $60.9 million greater than estimated. This large variance was due to the timing of the booking of the "clawback" provision of the local government fund freeze and will be balanced out in June.[4]

Revenue from the personal income tax was $136.4 million (22.9%) below the revised estimate for May. Withholding was $3.3 million (0.6%) below estimate, quarterly estimated payments were $0.5 million (5.0%) above estimate, and refunds were $9.6 million (8.9%) above estimate.

Personal income tax revenue was expected to come in below estimate in May. In April, receipts related to the filing of annual returns were $158.2 million above original estimate.[5] The positive variances were thought to be due to an accelerated processing of returns and an unexpected number of returns filed electronically. Returns expected to be processed in May were processed in April. This boosted the revenue reported for April but was expected to reduce the amounts reported for May. In May, receipts related to the filing of annual returns were $121.2 million below the original estimate for May. For April and May combined, these receipts were $37.0 million above the original estimate. In comparison with the revised estimates, receipts related to the filing of annual returns were $231.9 million above estimate in April and $75.3 million below estimate in May. For April and May combined, these receipts were $156.6 million above the revised estimate. Although part of the April "revenue bubble" was given back in May, it appears that the bubble may not have been a bubble after all.

Through May, GRF revenue from the personal income tax totaled $6,794.9 million. The total is $59.9 million (0.9%) below the original estimate. Withholding is $4.6 million (0.07%) below estimate. Quarterly estimated payments are $16.1 million (1.6%) below estimate, revenue from the tax on trusts is $10.8 million (25.1%) above estimate, and refunds are $48.0 million (4.8%) above estimate. For the fiscal year to date, revenue from the personal income tax is $154.9 million (2.3%) above the revised estimate. Withholding is $15.0 million (0.2%) above estimate, quarterly estimated payments are $21.4 million (2.3%) above estimate, and revenue from the tax on trusts is $13.2 million (32.6%) above estimate. Year-to-date refunds are $0.7 million (0.1%) below the revised estimate.

Income tax revenue continues to show just slight growth compared to a year ago. For the fiscal year through April, GRF revenue from the personal income tax is up by 1.9%. Fiscal year-to-date withholding is up by 3.1% compared to FY 2003. Withholding reflects the condition of Ohio's labor market, and the improvement in withholding growth provides some indication that Ohio's labor market is improving. Quarterly estimated payments are down by 5.6% compared to a year earlier and revenue from the tax on trusts is down 7.3%.

Sales and Use Tax

In May 2004, revenues from the sales and use tax were below estimates. Total sales and use tax revenues in the month were $651.3 million, $52.0 million (7.4%) below projected revenues. Auto and nonauto tax receipts were $12.7 million (12.4%) and $39.3 million (6.5%) below estimates, respectively. Total sales and use tax receipts in May 2004 were $102.9 million

(18.8%) above May 2003 sales and use tax revenues. As of May 2004, year-to-date total sales and use tax revenues were $6,890.3 million, $43.2 million (0.6%) below August 2003 estimates. Compared to revised estimates of March 2004, year-to-date sales and use tax receipts this month were $44.5 million (0.6%) below projected revenues. In April 2004, the sales and use tax revenues were tracking estimates. With one month of tax collection remaining in FY 2004, it appears unlikely that revenues from the sales and use tax will match projected revenues for the fiscal year. Sales and use tax receipts were $1,053.5 million (18.0%) higher than year-to-date tax receipts in May 2003. The increase in sales and use tax revenue is primarily due to a 20% increase in tax rates, as the tax increased from 5% to 6% of the purchase price in July 2003. Based on tax collections as of May 2004, consumers have spent $1.9 billion (1.6%) less in taxed goods and services in FY 2004 than in FY 2003.[6]

Nonauto Sales and Use Tax

The nonauto sales and use tax in May 2004 was again below estimates, following a poor performance in April 2004. In February and March 2004, this tax source was 2.7% and 4.6% above estimates, respectively. In April 2004, nonauto sales and use tax revenues were 1.5% below projected revenues. In May 2004, tax receipts were $561.5 million, $39.3 million (6.5%) below estimates. Tax receipts partly reflect taxable retail sales activity in the prior month and also taxable retail sales during that month.[7] Compared to nonauto sales and use tax revenues a year ago, tax receipts for the month were $96.5 million (20.8%) above revenues in May 2003. At the 5% sales tax rate, May 2004 nonauto sales and use tax receipts would have been $468.0 million, $3.0 million (0.6%) higher than May 2003 tax receipts. As of May 2004, year-to-date nonauto sales and use tax receipts were $5,866.6 million, $36.4 million (0.6%) below August 2003 estimates. Compared to revised estimates, year-to-date nonauto sales and use tax receipts were $26.0 million (0.4%) below projected revenues. Compared to receipts a year ago, year-to-date nonauto sales tax receipts as of May 2004 increased $895.8 million (18.0%). Based on nonauto sales and use tax collections as of May 2004, consumers have spent $1.6 billion (1.6%) less in taxed nonauto goods and services in FY 2004 than in FY 2003.

Nationwide retail sales (excluding autos) grew 0.7% in May 2004, after a drop of 0.1% in April

Chart 2: Nonauto Sales Tax Variance from August 2003 Estimates
(in millions of dollars)

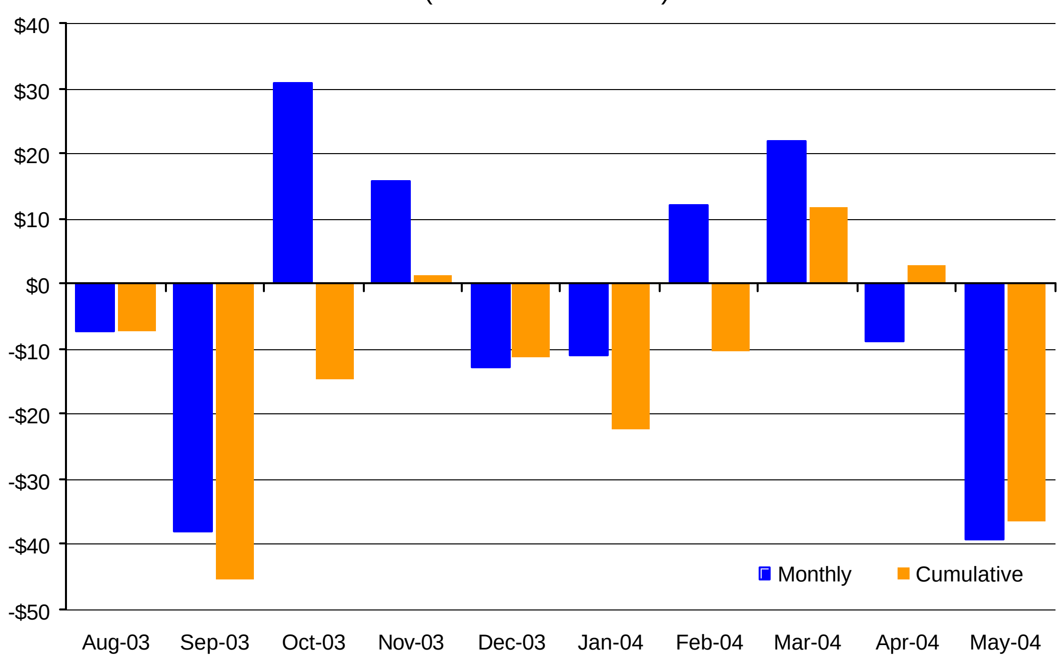
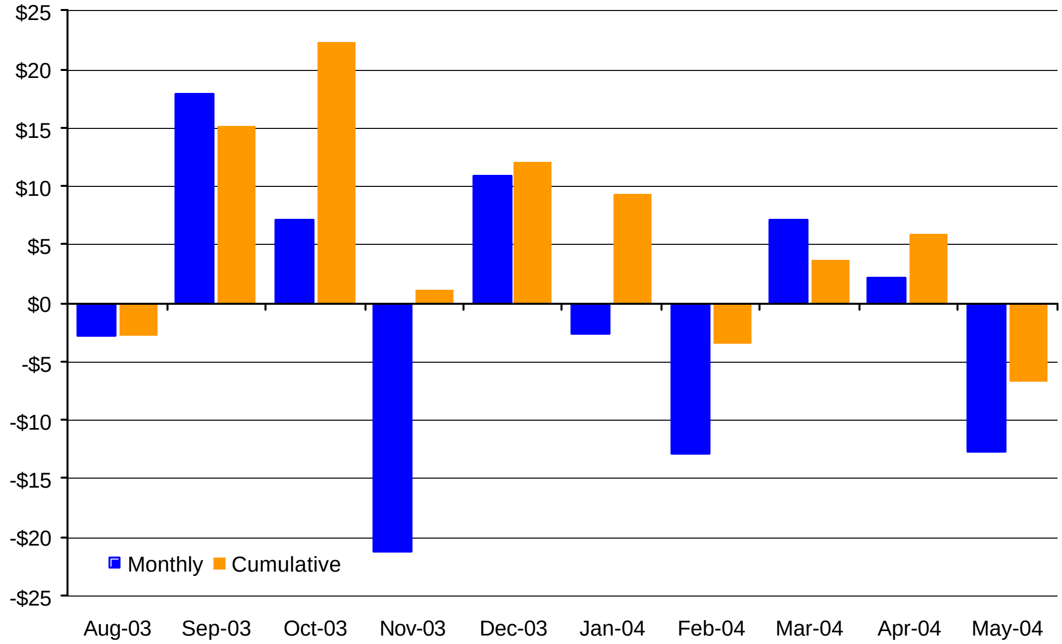


Chart 3: Auto Sales Tax Variance from August 2003 Estimate
(in millions of dollars)



2004. Although positive, the growth in retail sales (excluding autos) in May 2004 was below the average growth of 1.1% in the four preceding months of CY 2004. A spike in gasoline prices powered the advance in retail sales. Gasoline sales were up 4% from April 2004 sales and up 22.5% from sales a year ago. (Gasoline is not included in the nonauto sales taxable base, so this was of no help to sales tax revenues.) Excluding autos and gasoline, retail sales grew only 0.3% in May 2004 from April 2004. Compared to retail sales in the same month a year ago, May 2004 retail sales (excluding autos) were up 9.8%. Excluding autos and gasoline sales, May 2004 retail sales were up 8.6% compared to May 2003 sales. In the first five months of CY 2004, nationwide retail sales (excluding autos) as of May 2004 were 9.3% higher than in the same period in CY 2003, indicating a solid, although unspectacular, growth.

The International Council of Shopping Centers (ICSC) computes an index of chain-stores sales,[8] another measure of health of the retail sector, from data from approximately 72 retailers. The index of chain-stores sales was 5.7% higher in May 2004 than a year earlier, above the year-to-year rise of 4.4% in April 2004, but still below the average increase of 6.6% achieved in the first quarter of CY 2004. Increasing wage gains, tax refunds, and cash from mortgage refinancing helped buoy sales. The rise in gasoline and food prices may have negatively affected certain shoppers, but these factors had limited effect on shoppers in May 2004. Department stores, discount stores, and clothing stores all had strong gains in sales.

Auto Sales Tax

Auto sales and use tax receipts were $89.7 million in May 2004, $12.7 million (12.4%) below both the August 2003 estimates and March 2004 revised estimates. The clerks of court generally make auto tax payments on Monday for taxes collected during the preceding week on motor vehicles, watercraft, and outboard motors titled.[9] Therefore, auto tax receipts largely reflect vehicles sold and titled during the month. Compared to revenues a year ago in the same month, auto sales tax receipts in May 2004 were $6.3 million (7.6%) higher than receipts in FY 2003. At the 5% sales tax rate, May 2004 auto sales tax revenue would have been about $74.7 million, $8.6 million (10.3%) less than May 2003 receipts. As of May 2004, year-to-date auto sales tax receipts were $1,023.7 million, $6.7 million (0.7%) below August 2003 estimates. Year-to-date auto sales and use tax receipts were $18.4 million (1.8%) lower than revised estimates of March 2004. Auto sales and use tax receipts were also $157.7 million (19.3%) higher than receipts through the same period in FY 2003. Adjusted for the sales tax rate increase, year-to-date auto sales and use tax revenues in May 2004 would have been $853.1 million, $12.9 million (1.4%) less than receipts in FY 2003.

Auto sales and use tax receipts in the first two months in CY 2004 were below receipts in the same period last year (even with the rate increase from 5% to 6%). March and April 2004 auto sales and use tax receipts were above FY 2003 tax receipts, although if adjusted for the rate increase, tax receipts would have been lower. Auto sales and use tax receipts were $100 million in June 2003, when potential buyers accelerated their purchases in anticipation of the tax rate increase in July 2003. In FY 2004, auto tax receipts (at the 6% tax rate) have exceeded $100 million in each of four months. Adjusted for the sales tax rate increase, monthly auto sales and use tax receipts have been below that threshold the entire year. Based on auto sales and use tax collections as of May 2004, consumers have spent approximately $250 million (1.5%) less on motor vehicles, watercraft, and outboard motors in FY 2004 than in FY 2003.

Nationwide auto sales, both in number of vehicles sold and dollar amount, increased in May 2004. The U.S. Department of Commerce reported that sales at motor vehicle dealers grew 3.0% in May 2004. Unit sales of autos and light-trucks were 17.8 million on an annualized basis, an increase of 1.4 million units from April 2004 annualized sales. Compared to April 2004, light truck sales in May 2004 increased to 9.8 million units, up from 9.0 million units in the previous month. Car sales grew to 8.0 million units, up from 7.4 million units in April 2004. Compared to sales a year ago, unit sales were up 3.4% and dollar sales were up 6.0% in May 2004.

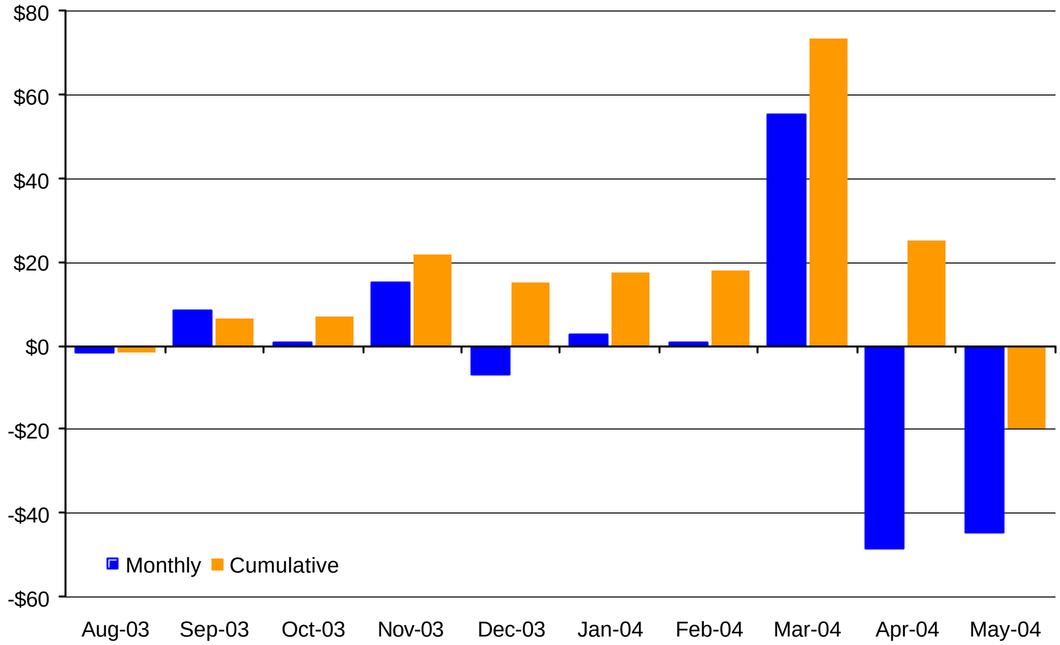
Auto sales in May 2004 confirmed that the level of monthly auto sales is linked to the temporary push or pullback of incentives by automakers. For example, spending by the Big Three (General Motors, Ford, and Chrysler) on rebates and no-interest loans modestly declined by 1.8% per vehicle in April 2004, according to Auto Data Corporation, an auto research firm. Sales dropped and inventories of unsold vehicles increased. In May 2004, automakers increased cashback and financing deals on a wide range of models to slash inventories or to maintain or increase sales. Sales bounced back. On average, consumer incentives rose 11.8% in May 2004 from a year ago, although the increase from April 2004 was modest (manufacturer incentives increased $193 to $3,784 in May 2004). Combined dealer and manufacturer discounts have climbed by 20% in the past 20 months to $5,185 per vehicle, according to CNW/ Marketing Research Inc.

As interest rates are set to increase in the near future, “0% financing” will become more costly to manufacturers, who hope that with an improving economy, they may decrease their reliance on such a strategy to increase sales. However, the actions of automakers and auto dealers suggest that incentives are not going away anytime soon, as they are committed to battle to maintain or gain market share. This strategy has hurt profitability. For example, profit per vehicle in CY 2003 was $2,402, $1,742, and $1,488 for Nissan, Toyota, and Honda, respectively. Incentives for foreign nameplates are on average half of the amount of incentives offered by General Motors, Ford, and Chrysler. Profit per vehicle was $178 for General Motors. Ford and Chrysler lost $48 and $496 per vehicle, respectively.[10] Although profits for the Big Three are constrained by other matters as well, such as the cost of health insurance for thousands of retired workers, incentives play an important role in reducing the profitability of the auto companies.

Corporate Franchise Tax

Major tax receipts under the corporate franchise tax are due in the second half of the fiscal year. Corporate franchise tax payments are due January 31, March 31, and May 31. By May 31 each year, a corporation must pay the difference between its full tax liability and the estimated

Chart 4: Corporate Franchise Tax Variance from August 2003 Estimate
(in millions of dollars)



payments that were due in January and March. May receipts are part of the third and last major corporate franchise tax payment for the May-June payment period.

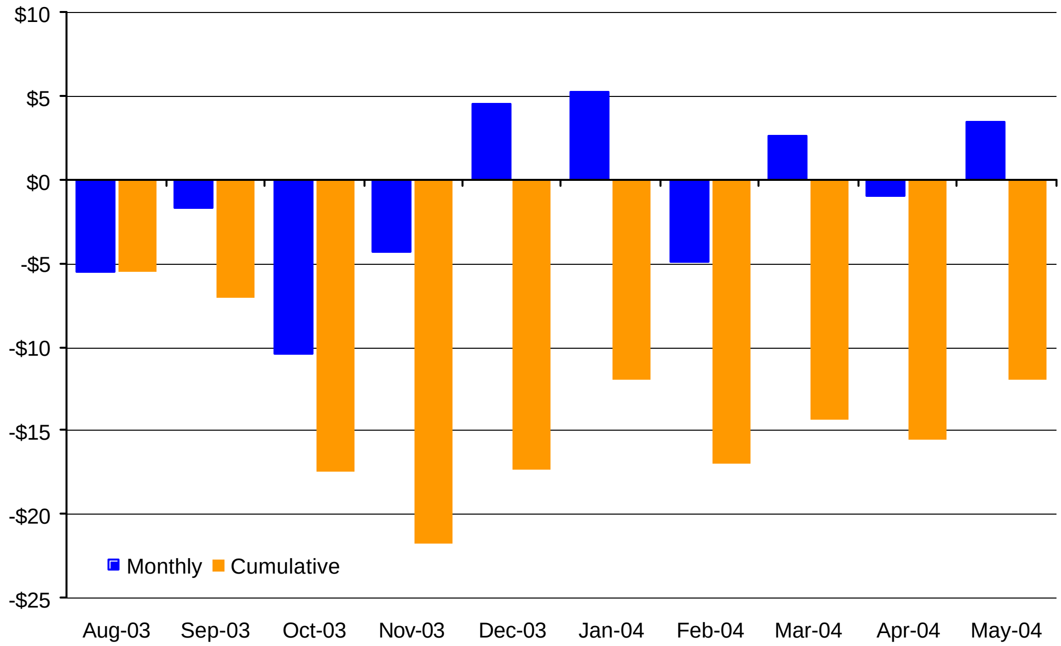
Corporate franchise tax receipts in May 2004 were $114.0 million, $44.6 million (28.1%) below August 2003 estimates and $44.0 million (27.9%) below March 2004 revised estimates. This negative variance is due, in part, to timing issues related to the due date of the receipts during the Memorial Day holiday weekend. Corporate franchise tax receipts were $18.9 million (19.8%) above May 2003 receipts. As of May 2004, year-to-date corporate franchise tax revenues were $709.8 million, $19.7 million (2.7%) below August 2003 estimates. (Year-to-date receipts were $36.8 million, or 4.9%, below revised estimates.) Year-to-date corporate franchise tax receipts were also $85.7 million (13.7%) above FY 2003 revenues in the same period. Although monthly corporate franchise tax receipts are volatile, corporate franchise tax revenues will finish the year ahead of FY 2003 receipts. The Office of Budget and Management increased the full-year GRF estimate for this tax source to $810 million in FY 2004, up from $793 million in the August 2003 estimates. Assuming this occurs, FY 2004 corporate franchise tax revenue would be about 8% above FY 2003 corporate franchise tax revenues.

The U.S. Bureau of Economic Analysis recently released estimates of corporate profits for CY 2002 and CY 2003. Corporate profits from current production (profits with inventory valuation and capital consumption adjustments)[11] grew 17.4% in CY 2002 and 18.3% in CY 2003. Profit from current production is considered the best measure of corporate profits because it is not affected by accounting distortions or inventory valuation changes. Although on the upswing, growth in corporate profits is expected to slow in the next two years.

Cigarette and Other Tobacco Products Tax

Cigarette and other tobacco products tax receipts, at $73.6 million, were $3.5 million (4.9%) above August 2003 estimates and $5.8 million (7.4%) below March 2004 revised estimates. The negative variance from revised estimates is partly due to timing issues related to the Memorial Day holiday weekend. Most of the cigarette and other tobacco products tax payments

Chart 5: Cigarette Tax Variance from August 2003 Estimates
(in millions of dollars)



to the Treasurer of State are made by checks. Thus, although filing of the returns may have occurred by May 31, some of the tax payments were recorded in early June.

Compared to year-ago receipts, monthly revenues in May 2004 were $0.9 million (1.2%) lower than May 2003 receipts. As of May 2004, year-to-date cigarette and other tobacco products receipts were $500.3 million, $12.1 million (2.4%) below August 2003 estimates. (Year-to-date tax receipts were $10.1 million, or 2.0%, below revised estimates.) Year-to-date revenues from this tax source were also $47.9 million (8.7%) below revenues a year ago. From July 2002 through May 2003, the floor tax provided $41.9 million, and total cigarette and other tobacco products tax revenues were $548.2 million. Excluding amounts provided by the floor tax, year-to-date FY 2004 revenues as of May 2004 would have been $5.9 million (1.2%) below receipts in the same period in FY 2003. A year-over-year decrease in cigarette tax receipts of this magnitude would be within historical trend decreases in estimated cigarette consumption of 1% to 2% per year. However, it is also possible that the year-over-year decrease in cigarette tax receipts may be less.

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[1] "Original" estimates for FY 2004 were made by the Office of Budget and Management in August 2003. These estimates were revised in March 2004. The revisions were based on the then year-to-date revenue collections and the economic outlook for the remainder of the fiscal year.

[2] The "major taxes" are the personal income tax, the sales and use tax, the corporate franchise tax, the public utility excise tax, and the kilowatt-hour tax.

[3] Quarterly estimated payments are made by taxpayers who expect to be underwithheld by more than $500. Payments are due on or before April 15, June 15, and September 15 of the tax year and January 15 of the following year. These payments are usually made by taxpayers with significant nonwage income. This income often comes from investments, especially capital gains realized in the stock market. Most estimated payments are made by high-income taxpayers.

[4] The "clawback" provision is based on a comparison of the amounts credited to the local government funds under the temporary stabilization and the amounts that would have been credited to the funds in the absence of the temporary stabilization. The effect of the clawback is that the amounts credited to the local government funds are equal to the minimum of the amounts under the temporary stabilization or the amounts the funds would have received in the absence of the freeze.

[5] "Receipts related to the filing of annual returns" are payments made by individuals filing their annual returns plus payments made by individuals requesting a filing extension minus refunds.

[6] This does not represent a decrease in actual consumption; rather, it represents a decrease in *taxed* consumption in FY 2004 compared to FY 2003.

[7] Am. Sub. H.B. 40 changed the historical patterns of remittance of sales and use tax receipts starting in April 2003. Under prior law, monthly sales and use tax receipts reflected taxable transactions in the prior month. Under current law, certain large taxpayers must remit sales tax payments in the same month the transactions occur. Thus, monthly sales tax receipts reflect taxable transactions in both the current and the prior month.

[8] Stores of major discounters, department stores, and specialty retailers open at least a year.

[9] There are instances in which full tax remittance does not occur on schedule. For example, in its monthly financial report of May 10, 2004, the Office of Budget and Management reported that one large county was not current with its payments.

[10] The Annual Harbour Report, as reported in the *Wall Street Journal* of June 11, 2004, page A3.

[11] Several measures of corporate profits are available from the Bureau of Economic Analysis, a unit of the United States Department of Commerce.

Table 2
General Revenue Fund Revenue
Actual vs. Estimate
Month of May 2004
($ in thousands)

REVENUE SOURCE				
TAX REVENUE	**Actual**	**Estimate***	**Variance**	**Percent**
Auto Sales	$89,723	$102,447	-$12,724	-12.4%
Nonauto Sales & Use	$561,547	$600,825	-$39,278	-6.5%
Total Sales	$651,270	$703,272	-$52,002	-7.4%
Personal Income	$458,157	$643,350	-$185,193	-28.8%
Corporate Franchise	$113,963	$158,600	-$44,637	-28.1%
Public Utility	$56,844	$47,023	$9,821	20.9%
Kilowatt Hour Excise Tax	$26,060	$29,832	-$3,772	-12.6%
Total Major Taxes	**$1,306,293**	**$1,582,077**	**-$275,784**	**-17.4%**
Foreign Insurance	-$14,077	-$4,600	-$9,477	206.0%
Domestic Insurance	$131,048	$166,600	-$35,552	-21.3%
Business & Property	$14,332	$27,280	-$12,948	-47.5%
Cigarette	$73,464	$70,000	$3,464	4.9%
Alcoholic Beverage	$5,076	$5,520	-$444	-8.0%
Liquor Gallonage	$2,543	$2,400	$143	6.0%
Estate	$5,590	$21,000	-$15,410	-73.4%
Total Other Taxes	$217,976	$288,200	-$70,224	-24.4%
Total Taxes	**$1,524,269**	**$1,870,277**	**-$346,008**	**-18.5%**
NONTAX REVENUE				
Earnings on Investments	$0	$0	$0	---
Licenses and Fees	$1,693	$1,764	-$71	-4.0%
Other Revenue	$9,657	$13,637	-$3,980	-29.2%
Nontax Receipts	$11,350	$15,401	-$4,051	-26.3%
TRANSFERS				
Liquor Transfers	$10,000	$9,000	$1,000	11.1%
Budget Stabilization	$0	$0	$0	---
Other Transfers In	$5,000	$73,300	-$68,300	-93.2%
Total Transfers In	$15,000	$82,300	-$67,300	-81.8%
TOTAL REVENUE less Federal Grants	**$1,550,620**	**$1,967,978**	**-$417,358**	**-21.2%**
Federal Grants	$388,202	$356,081	$32,121	9.0%
TOTAL GRF REVENUE	**$1,938,822**	**$2,324,059**	**-$385,237**	**-16.6%**

* August 2003 estimates of the Office of Budget and Management.

Detail may not sum to total due to rounding.

Table 3
General Revenue Fund Revenue
Actual vs. Estimate
FY 2004 to Date as of May 2004
($ in thousands)

REVENUE SOURCE						
TAX REVENUE	**Actual**	**Estimate***	**Variance**	**Percent**	**FY 2003**	**Percent Change**
Auto Sales	$1,023,668	$1,030,413	-$6,745	-0.7%	$866,066	18.2%
Nonauto Sales & Use	$5,866,645	$5,903,075	-$36,430	-0.6%	$4,970,795	18.0%
Total Sales	$6,890,313	$6,933,488	-$43,175	-0.6%	$5,836,860	18.0%
Personal Income	$6,794,940	$6,854,801	-$59,861	-0.9%	$6,665,704	1.9%
Corporate Franchise	$709,845	$729,561	-$19,716	-2.7%	$624,257	13.7%
Public Utility	$200,390	$184,000	$16,390	8.9%	$211,647	-5.3%
Kilowatt Hour Excise Tax	$313,405	$346,799	-$33,394	-9.6%	$317,570	-1.3%
Total Major Taxes	**$14,908,893**	**$15,048,649**	**-$139,756**	**-0.9%**	**$13,656,039**	**9.2%**
Foreign Insurance	$233,411	$230,000	$3,411	1.5%	$225,134	3.7%
Domestic Insurance	$131,442	$166,800	-$35,358	-21.2%	$159,247	-17.5%
Business & Property	$16,094	$29,266	-$13,172	-45.0%	$28,252	-43.0%
Cigarette	$500,306	$512,400	-$12,094	-2.4%	$548,218	-8.7%
Alcoholic Beverage	$51,504	$54,448	-$2,944	-5.4%	$51,584	-0.2%
Liquor Gallonage	$28,324	$27,354	$970	3.5%	$27,076	4.6%
Estate	$49,473	$98,900	-$49,427	-50.0%	$88,359	-44.0%
Total Other Taxes	$1,010,553	$1,119,168	-$108,615	-9.7%	$1,127,871	-10.4%
Total Taxes	**$15,919,446**	**$16,167,817**	**-$248,371**	**-1.5%**	**$14,783,910**	**7.7%**
NONTAX REVENUE						
Earnings on Investments	$14,820	$18,250	-$3,430	-18.8%	$13,780	7.5%
Licenses and Fees	$46,899	$42,336	$4,563	10.8%	$32,318	45.1%
Other Revenue	$145,657	$159,500	-$13,843	-8.7%	$200,032	-27.2%
Nontax Receipts	$207,375	$220,086	-$12,711	-5.8%	$246,130	-15.7%
TRANSFERS						
Liquor Transfers	$109,000	$96,000	$13,000	13.5%	$106,000	2.8%
Budget Stabilization	$0	$0	$0	---	$0	---
Other Transfers In	$140,208	$179,100	-$38,892	-21.7%	$158,643	-11.6%
Total Transfers In	$249,208	$275,100	-$25,892	-9.4%	$264,643	-5.8%
TOTAL REVENUE less Federal Grants	**$16,376,030**	**$16,663,003**	**-$286,973**	**-1.7%**	**$15,294,684**	**7.1%**
Federal Grants	$5,032,482	$5,000,667	$31,815	0.6%	$4,395,846	14.5%
TOTAL GRF REVENUE	**$21,408,513**	**$21,663,670**	**-$255,157**	**-1.2%**	**$19,690,530**	**8.7%**

* August 2003 estimates of the Office of Budget and Management.

Detail may not sum to total due to rounding.

Disbursements

*— Steve Mansfield**

May's disbursements from the General Revenue Fund (GRF) (excluding transfers) were $48.7 million over the estimate for the month, decreasing the overall negative disbursement variance for the year to date to $224.3 million, or 1.0% of forecast outlays. Actual outlays for FY 2004 to date are 3.6% higher than at the same point in FY 2003.

About $150 million of this year-to-date negative variance is planned to lapse to compensate for a shortfall in revenues that is anticipated by the Office of Budget and Management to be approximately $247 million. Another $100 million in executive-ordered budget reductions was announced in April.

In May, two of the state's four major GRF program categories posted positive disbursement variances, and two posted negative variances (see Figure 1). The Government Operations category increased the size of its negative year-to-date disbursement variance by $6.4 million to $89.0 million; the Welfare and Human Services category reduced its year-to-date negative disbursement variance to $50.9 million with a $80.0 million positive variance for the month; the Property Tax Relief category posted a negative variance of $35.8 million, increasing its year-to-date negative disbursement variance to $44.8 million; and the Education category posted a positive variance of $11.0 million in May, which decreased its negative year-to-date disbursement variance to $12.8 million. In order of magnitude, the three largest program subcategories contributing to the $224.3 million year-to-date negative variance in disbursements from the GRF (excluding transfers) are Other Welfare (-$64.4 million), Justice and Corrections (-$57.2 million), and Property Tax Relief (-$44.8 million). As can be seen in Table 5, all but three of the program subcategories show negative year-to-date disbursement variances.

In the sections that follow, we examine in more detail the disbursement activity in each of the four major GRF program categories in the order of magnitude of its contribution to the year-to-date negative disbursement variance. Summary information about GRF disbursement activity for the most recent month is presented in Table 4 and

Figure 1
GRF Disbursement Variances
by Program Category, FY 2004

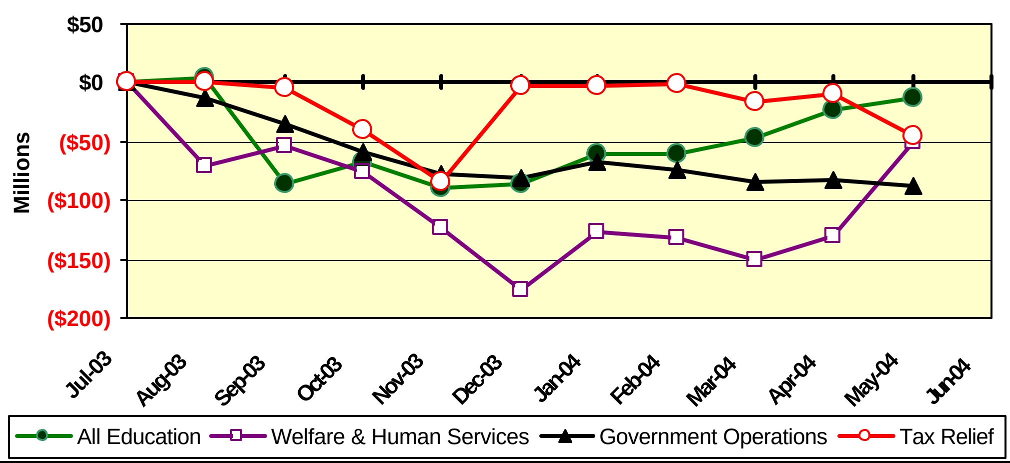

Table 4
General Revenue Fund Disbursements
Actual vs. Estimate
Month of May 2004
($ in thousands)

PROGRAM	Actual	Estimate*	Variance	Percent
Primary & Secondary Education (1)	$538,801	$517,666	$21,134	4.1%
Higher Education	$229,182	$239,366	-$10,184	-4.3%
Total Education	$767,983	$757,033	$10,950	1.4%
Health Care/Medicaid	$644,767	$577,409	$67,357	11.7%
TANF	$3,574	$0	$3,574	---
General/Disability Assistance	$1,774	$1,881	-$107	-5.7%
Other Welfare (2)	$24,009	$27,431	-$3,422	-12.5%
Human Services (3)	$109,064	$96,438	$12,626	13.1%
Total Welfare & Human Services	$783,188	$703,160	$80,028	11.4%
Justice & Corrections	$115,523	$121,352	-$5,829	-4.8%
Environment & Natural Resources	$13,224	$13,786	-$563	-4.1%
Transportation	$1,905	$1,099	$806	73.3%
Development	$7,884	$6,274	$1,610	25.7%
Other Government	$16,129	$18,159	-$2,030	-11.2%
Capital	$0	$412	-$412	-100.0%
Total Government Operations	$154,665	$161,083	-$6,418	-4.0%
Property Tax Relief (4)	$279,158	$315,000	-$35,842	-11.4%
Debt Service	$0	$0	$0	---
Total Program Payments	**$1,984,994**	**$1,936,275**	**$48,719**	**2.5%**
TRANSFERS				
Local Govt Distribution	$0	$0	$0	---
Budget Stabilization	$0	$0	$0	---
Other Transfers Out	$0	$3,225	$0	-100.0%
Total Transfers Out	$0	$3,225	-$3,225	-100.0%
TOTAL GRF USES	**$1,984,994**	**$1,939,500**	**$45,494**	**2.3%**

(1) Includes Primary, Secondary, and Other Education.
(2) Includes the Department of Job and Family Services, exclusive of Medicaid, TANF, and General/Disability Assistance.
(3) Includes Mental Health, Mental Retardation and Developmental Disabilities, and Other Human Services.
(4) Includes property tax rollbacks, homestead exemption, and tangible property tax exemption.

* August 2003 estimates of the Office of Budget and Management.

Detail may not sum to total due to rounding.

Table 5
General Revenue Fund Disbursements
Actual vs. Estimate
FY 2004 to Date as of May 2004
($ in thousands)

PROGRAM	Actual	Estimate*	Variance	Percent	FY 2003	Percent Change
Primary & Secondary Education (1)	$5,935,286	$5,938,722	-$3,436	-0.1%	$5,802,881	2.3%
Higher Education	$2,190,692	$2,200,034	-$9,342	-0.4%	$2,213,772	-1.0%
Total Education	$8,125,977	$8,138,755	-$12,778	-0.2%	$8,016,654	1.4%
Health Care/Medicaid	$8,135,186	$8,099,160	$36,026	0.4%	$7,469,647	8.9%
TANF	$356,927	$356,740	$187	0.1%	$352,059	1.4%
General/Disability Assistance	$20,851	$22,465	-$1,614	-7.2%	$24,027	-13.2%
Other Welfare (2)	$419,571	$483,977	-$64,406	-13.3%	$440,518	-4.8%
Human Services (3)	$1,103,641	$1,124,706	-$21,065	-1.9%	$1,084,355	1.8%
Total Welfare & Human Services	$10,036,175	$10,087,047	-$50,873	-0.5%	$9,370,606	7.1%
Justice & Corrections	$1,732,528	$1,789,722	-$57,194	-3.2%	$1,707,614	1.5%
Environment & Natural Resources	$107,754	$111,555	-$3,801	-3.4%	$112,464	-4.2%
Transportation	$26,352	$25,741	$611	2.4%	$31,328	-15.9%
Development	$129,155	$136,446	-$7,291	-5.3%	$162,222	-20.4%
Other Government	$336,523	$354,047	-$17,525	-4.9%	$355,137	-5.2%
Capital	$0	$3,801	-$3,801	-100.0%	$0	---
Total Government Operations	$2,332,311	$2,421,312	-$89,001	-3.7%	$2,368,764	-1.5%
Property Tax Relief (4)	$1,112,822	$1,157,600	-$44,778	-3.9%	$1,144,213	-2.7%
Debt Service	$313,039	$339,950	-$26,912	-7.9%	$250,527	25.0%
Total Program Payments	**$21,920,324**	**$22,144,665**	**-$224,341**	**-1.0%**	**$21,150,763**	**3.6%**
TRANSFERS						
Local Govt Distribution	$0	$0	$0	---	$0	---
Budget Stabilization	$0	$0	$0	---	$0	---
Other Transfers Out	$54,043	$26,200	$27,843	106.3%	$18,587	190.8%
Total Transfers Out	$54,043	$26,200	$27,843	106.3%	$18,587	190.8%
TOTAL GRF USES	**$21,974,367**	**$22,170,865**	**-$196,498**	**-0.9%**	**$21,169,351**	**3.8%**

(1) Includes Primary, Secondary, and Other Education.
(2) Includes the Department of Job and Family Services, exclusive of Medicaid, TANF, and General/Disability Assistance.
(3) Includes Mental Health, Mental Retardation and Developmental Disabilities, and Other Human Services.
(4) Includes property tax rollbacks, homestead exemption, and tangible property tax exemption.

* August 2003 estimates of the Office of Budget and Management.

Detail may not sum to total due to rounding.

for the year to date is presented in Table 5. A detailed analysis of disbursement activity in the Health Care/Medicaid program is presented in Tables 6 and 7.

Government Operations (-$89.0 million)

With a negative disbursement variance of $6.4 million in May, outlays in the Government Operations category stand at $89.0 million, or 1.5%, under the estimate for the year to date. The bulk of this negative year-to-date variance is accounted for by the Department of Rehabilitation and Correction ($46.4 million under estimate), the Department of Youth Services ($9.9 million under estimate), and the Judiciary/Supreme Court ($9.4 million under estimate).

As we reported in previous months, the Department of Rehabilitation and Correction's year-to-date negative disbursement variance is traceable primarily to line item 501-321, Institutional Operations, which has reflected various shortages in staff, primarily in the northern part of the state. When the Lima Correctional Institution closed in July 2003, some staff positions were eliminated while other positions, particularly corrections officers, were to be moved to other northern institutions and paid for with funds saved from the closing. With the closure delayed in the courts, the personnel adjustments in the northern institutions did not occur.

The bulk of the Department of Youth Services' negative year-to-date variance is traceable to changes in the pattern of disbursements to counties required by the operating budget. Those changes were not reflected in the estimates. The negative variance in disbursements by the Judiciary/Supreme Court stems from a voluntary cut of $6.8 million and some other savings. An offsetting $9.5 million positive variance stemming mostly from disaster-related expenditures was posted by the Department of Public Safety. The remainder of the negative year-to-date variance is spread out in smaller amounts over the budgets of the other state agencies in the category.

Welfare/Human Services (-$50.9 million)

The Welfare/Human Services category posted a positive disbursement variance of $80.0 million in May. For the year to date, outlays in this category stand at $50.9 million below the estimate. Three program subcategories (Health Care/Medicaid, Other Welfare, and Human Services) have significant year-to-date variances and are discussed in more detail in the following paragraphs.

Health Care/Medicaid. Year-to-date disbursements through May in the Health Care/Medicaid program (primarily line item 600-525) are $36.0 million, or 0.4% above the estimate (see Table 6). For May, health care spending was $67.4 million, or 11.7% over the estimate. This is the first time in the fiscal year that this subcategory's year-to-date disbursement variance has been positive. Partially explaining the variance is the timing of payments in the final week of May. Apparently some payments (particularly the payments in the Physicians service category) assumed for June were actually made in May.

The trend of positive disbursement variances in the Nursing Facilities service category continued in May with a $26.8 million positive variance. Disbursements in this service category are $91.9 million over estimate for the year to date. As we noted in previous months, the Department of Job and Family Services reports that "bed days" in nursing facilities are higher than expected, while per diems for Nursing Facilities have behaved as expected.

Separating the number of eligibles in the Covered Families and Children category by service delivery system shows that at this point in the fiscal year enrollment for fee-for-service plans is under the estimate by 19,500, whereas enrollment in managed care plans is over the estimate by nearly 28,000. This pattern of usage is the source of the negative disbursement variances, particularly in the Inpatient Hospitals and All Other service categories.

Table 6
Health Care Spending in FY 2004
Medicaid, ALI 600-525
($ in thousands)

Service Category	May: Actual	May: Estimate	May: Variance	May: Percent Variance	Year-to-Date Spending: Actual thru May	Year-to-Date Spending: Estimate thru May	Year-to-Date Spending: Variance	Year-to-Date Spending: Percent Variance
Nursing Facilities	$196,353	$169,577	$26,775	15.8%	$2,254,812	$2,162,865	$91,947	4.3%
Payments	$227,548	$211,520	$16,028	7.6%	$2,479,833	$2,400,027	$79,806	3.3%
NF Franchise Fees Offset[1]	($31,195)	($41,942)	$10,747	-25.6%	($225,021)	($237,163)	$12,141	-5.1%
ICF/MR	$34,498	$34,157	$342	1.0%	$385,344	$385,380	($36)	0.0%
Payments	$36,206	$35,881	$325	0.9%	$403,998	$404,290	($292)	-0.1%
ICF/MR Franchise Fees Offset	($1,708)	($1,725)	$17	-1.0%	($18,654)	($18,910)	$256	-1.4%
Inpatient Hospitals	$111,682	$103,321	$8,360	8.1%	$1,199,318	$1,218,726	($19,408)	-1.6%
Outpatient Hospitals	$48,544	$46,071	$2,473	5.4%	$535,426	$531,016	$4,410	0.8%
Physicians	$63,259	$46,857	$16,402	35.0%	$532,495	$532,745	($250)	0.0%
Prescription Drugs	$148,430	$139,945	$8,484	6.1%	$1,598,512	$1,583,147	$15,365	1.0%
HMO	$83,133	$78,183	$4,949	6.3%	$915,044	$883,451	$31,593	3.6%
Medicare Buy-In	$14,223	$13,978	$245	1.8%	$146,949	$146,789	$160	0.1%
ODJFS Waiver[2]	$16,982	$18,735	($1,754)	-9.4%	$175,361	$202,352	($26,990)	-13.3%
All Other[3]	$73,693	$75,823	($2,129)	-2.8%	$784,182	$841,188	($57,006)	-6.8%
CHIP II[4]	$6,324	$5,368	$955	17.8%	$65,682	$60,390	$5,292	8.8%
DA Medical[5]	$5,254	$8,091	($2,838)	-35.1%	$75,662	$90,584	($14,922)	-16.5%
Total ALI 600-525	$802,372	$740,107	$62,265	8.4%	$8,668,787	$8,638,633	$30,154	0.3%
DSH Offset	($116,210)	($120,719)	$4,509		($116,210)	($120,719)	$4,509	
Drug Rebates	($41,395)	($41,978)	$583		($380,463)	($378,973)	($1,491)	
FY 2002 Encumbrance	$0	$0	$0		($71,000)	($39,781)	($31,219)	
Prior Period ALI 600-525	$0	$0	$0		$34,073	$0	$34,073	
Total Health Care (Net of Offsets)	**$644,767**	**$577,409**	**$67,357**	**11.7%**	**$8,135,186**	**$8,099,160**	**$36,026**	**0.4%**
Est. Federal Share[6]	$378,450	$338,915	$39,536		$4,775,004	$4,753,858	$21,146	
Est. State Share	$266,316	$238,495	$27,821		$3,360,182	$3,345,301	$14,880	

1. Some of the money generated from nursing home franchise permit fees is used to make payments to nursing facilities to offset GRF nursing facilities spending. The NF franchise fee is $3.30 per bed per day in FY 2002 and is $4.30 per bed per day for FYs 2003 through 2005.
2. Waivers provide home-care alternatives to consumers whose medical conditions/functional abilities would otherwise require long-term care facility residence.
3. "All Other" includes all other health services funded by line item 600-525.
4. CHIP II provides health care coverage for children under age 19 whose family incomes are between 150% and 200% of FPL. The state receives enhanced FMAP for CHIP II.
5. DA Medical is a state-only funded program.
6. The federal madical assistance percentage (FMAP) used in this table is a blended rate of 58.70%.

Note: Due to accounting differences, the totals do not exactly match the amounts from Tables 4 and 5.

Source: BOMC8300-R001, BOMC8350-R001&R002 Reports, Ohio Department of Job & Family Services.

Another area within the Health Care/Medicaid program now showing a significant negative disbursement variance is the Disability Assistance (DA) program. The DA program is a state and county-funded effort that provides cash assistance and/or medical assistance to low-income individuals ineligible or not yet eligible for federal public assistance programs. Am. Sub. H.B. 95 of the 125th General Assembly separated the financial and medical assistance components of the program and authorized the adoption of rules to permit establishing maximum benefits, time limits on benefits, caps on the number of persons to receive benefits, and other rules that would allow greater cost controls within the program. With a budgeted amount of $100.7 million for the medical assistance component for the full year, the program is now $14.9 million or 16.5% under estimate. The number of DA-medical recipients has declined by about 14,000 persons since the beginning of the fiscal year. The DA financial assistance program had an original FY 2004 appropriation of $22.8 million. This has been reduced by executive order to $21.5 million, with $20.9 million having been disbursed to date. The number of DA financial assistance recipients has declined by about 4,000 recipients since the beginning of the fiscal year.

Job and Family Services. Disbursements for the Department of Job and Family Services' operating and subsidy programs were $3.4 million under estimate in May and stand at $64.4 million under the estimate for the year to date. In Tables 4 and 5, these disbursements are captured in the Other Welfare subcategory, which excludes the separately tracked Medicaid, TANF, and Disability Assistance programs.

Table 7
FY 2004 to FY 2003 Comparison of Year-to-Date Health Care Spending
($ in thousands)

Service Category	FY 2004 Yr.-to-Date as of May '04	FY 2003 Yr.-to-Date as of May '03	Dollar Change	Percent Increase
Nursing Facilities	$2,254,812	$2,161,516	$93,296	4.3%
Payments	$2,479,833	$2,378,065	$101,769	4.3%
NF Franchise Fees Offset[1]	($225,021)	($216,549)	($8,473)	3.9%
ICF/MR	$385,344	$374,676	$10,668	2.8%
Payments	$403,998	$393,334	$10,664	2.7%
ICF/MR Franchise Fees Offset	($18,654)	($18,659)	$4	0.0%
Inpatient Hospitals	$1,199,318	$1,165,339	$33,979	2.9%
Outpatient Hospitals	$535,426	$494,926	$40,501	8.2%
Physicians	$532,495	$483,647	$48,848	10.1%
Prescription Drugs	$1,598,512	$1,399,994	$198,518	14.2%
HMO	$915,044	$657,103	$257,941	39.3%
Medicare Buy-In	$146,949	$134,197	$12,752	9.5%
ODJFS Waiver[2]	$175,361	$157,350	$18,011	11.4%
All Other[3]	$784,182	$709,794	$74,388	10.5%
CHIP II[4]	$65,682	$54,097	$11,585	21.4%
DA Medical[5]	$75,662	$86,503	($10,841)	-12.5%
Total Health Care	**$8,668,787**	**$7,879,139**	**$789,647**	**10.02%**
DSH Offset	($116,210)	($136,354)	$20,144	
Drug Rebates	($380,463)	($274,233)	($106,230)	
Prior Year Encumbrance	($71,000)	($83,539)	$12,539	
Prior Period ALI 600-525	$34,073	$84,635	($50,562)	
Total Health Care (Net of Offsets)	**$8,135,186**	**$7,469,647**	**$665,538**	**8.91%**
Est. Federal Share[6]	$4,775,004	$4,384,362	$390,642	
Est. State Share	$3,360,182	$3,085,286	$274,896	

1. Some of the money generated from nursing home franchise permit fees is used to make payments to nursing facilities to offset GRF nursing facilities spending. The NF franchise fee is $3.30 per bed per day in FY 2002 and is $4.30 per bed per day for FYs 2003 through 2005.
2. Waivers provide home-care alternatives to consumers whose medical conditions/functional abilities would otherwise require long-term care facility residence.
3. "All Other" includes all other health services funded by line item 600-525.
4. CHIP II provides health care coverage for children under age 19 whose family incomes are between 150% and 200% of FPL. The state receives enhanced FMAP for CHIP II.
5. DA Medical is a state-only funded program.
6. The federal madical assistance percentage (FMAP) used in this table is a blended rate of 58.70%.

Source: BOMC8300-R001, BOMC8350-R001&R002 Reports, Ohio Department of Job & Family Services.

Among the most significant contributors to this negative variance are line items 600-416, 600-321, and 600-528. Line item 600-416, Computer Projects, accounted for $26.6 million of the negative year-to-date disbursement variance. About $14.1 million of this variance can be traced to a budget reduction in the item and to a lapse of $8.9 million in prior-year appropriations for this item. Another $15.4 million of the negative year-to-date disbursement variance can be traced to line item 600-321, Support Services, with $5.7 million of this from the budget reduction. Another significant contributor to the negative year-to-date disbursement variance in this subcategory is line item 600-528, Adoption Services. For the year to date, outlays from this appropriation are $8.8 million below estimate. Like last year, the rate of adoption has grown slower than had been forecast. Line item 600-528 was reduced $1.4 million in its state share appropriation.

MR/DD. The Department of Mental Retardation and Developmental Disabilities is within the Human Services program subcategory. This subcategory also includes the Department of Mental Health and other human service agencies. May's disbursements for the Department of Mental Retardation and Developmental Disabilities were $10.3 million above estimate. For the year to date, however, MR/DD's disbursements are $18.2 million below the estimate. The main reason for the year-to-date variance is a controversy over the Community Alternative Funding System (CAFS) program. April's subsidy payments that were used to pay CAFS providers, along with some other subsidies, were halted upon the filing of a lawsuit in Franklin County. The lawsuit centers on a recent emergency rule filed by the Department of Job and Family Services, which, among other things, modifies reimbursement rates for providers of CAFS services. In May, some subsidy payments resumed and partially made up for the negative variance in the previous month. The line items affected by this situation are 322-417, Supported Living; 322-451, Family Support Services; 322-452, Service and Support Administration; 322-502, County Board Subsidies; and 322-503, Tax Equity.

Tax Relief (-$44.8 million)

The Property Tax Relief program, which carries an FY 2004 GRF appropriation of over $1.3 billion, reimburses school districts and local governments for revenue that is lost due to tax relief provided by state law to property owners and businesses through the homestead exemption, the property tax rollbacks, and the $10,000 tangible tax exemption programs. Tax relief funds are paid to school districts and local governments by the Department of Education and the Department of Taxation, respectively. Each of these departments divides its property tax relief program into two components: real property tax credits/exemptions, and tangible tax exemptions. Total payments under the program were $279 million in May. This was $35.8 million under estimate for the month. This variance increased the negative year-to-date disbursement variance in the program to a net of $44.8 million. The year-to-date variance is composed of variances of $5.3 million under estimate in the Education portion of the program and $39.4 million under the estimate in the Taxation portion of the program. Disbursement variances in the tax relief program are usually traceable to the timing of county auditor requests for reimbursement.

Education (-$12.8 million)

In May, the Education category posted a positive disbursement variance of $11.0 million, reducing the negative year-to-date variance to $12.8 million. The Department of Education posted a $21.1 million positive variance for the month. Disbursements by the Board of Regents partially offset this with a negative variance of $10.2 million.

Department of Education. Having posted a positive disbursement variance of $21.1 million in May, the Department of Education's disbursements for the year to date now stand at $3.4 million below estimate. Disbursements from line item 200-501, Base Cost Funding, were $28.0 million over estimate in May and account for more than the net disbursement variance for the month. This appropriation item is the largest one in the Department's budget, with a total appropriation for FY 2004 of $4,397.1 million. The line item funds school districts according to the base cost formula developed by the General Assembly to provide educational services to Ohio public school students. Average Daily Membership (ADM) figures for FY 2004 came in about 7,000 students above estimate. Special education ADM for FY 2004 came in about 10,000 students above estimate. Also, business personal tangible property values fell more than had been anticipated. (When property values fall, state aid goes up.) For all these reasons, the Department transferred $32.8 million into this line item from other line items. In addition, enacted Sub. H.B. 434 (the Tobacco Settlement Appropriations Act) increases the appropriation for this item by $80 million.

Board of Regents. Disbursements by the Board of Regents were $10.2 million below estimate in May, to stand at $9.3 million below estimate for the year to date. The most significant portion of the month's variance is in line item 235-503, Ohio Instructional Grants, with $3.6 million below estimate. As a result of a $6.2 million payment from this line-item appropriation in FY 2004 to cover FY 2003 expenses, disbursements for instructional grants are $2.8 million over estimate for the year to date. The Ohio Instructional Grant Reconciliation Fund has $4.8 million that is available to support excess obligations to this line item, but it may not be used for a current year obligation. Therefore, the Board of Regents must wait until July 1 to make some of the remaining payments for FY 2004.

**LSC colleagues who contributed to the development of this disbursement report included, in alphabetical order, Sara Anderson, Melaney Carter, Ivy Chen, Phil Cummins, Jamie Doskocil, Laura Potts, David Price, Joseph Rogers, Maria Seaman, and Clay Weidner.*