

## HIGHLIGHTS

- State tax collections were weak in the first quarter of 2008, rising only 1.7 percent over a year earlier.
- After adjusting for legislated tax changes and inflation in state and local government purchases, state tax revenue declined by 5.3 percent. This is the third quarter in a row that total adjusted revenue growth showed a decline. Sales tax revenues produced no growth for the first time in six years.
- The economy has experienced widespread and significant weakening since the close of the January-March quarter. Revenues may be relatively strong during the April-June quarter, but positive cash flows will largely reflect tax payments based on 2007 activity. Such strength is likely to dissipate after June. The underlying trend for states is negative; budget cuts and other gap-closing measures likely loom ahead.
- Local tax collections declined slightly during the January-March quarter in inflation-adjusted terms, due to weakness in both property and sales taxes.
- Inflation in state and local government costs remained above 6 percent for the first quarter of 2008, continuing a recent trend of significantly higher increases than those in the broader economy.

## State Taxes Slow Yet Again, and Further Weakening Appears Likely

### *Mid-Year Budget Cuts May Lie Ahead*

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### Tax Revenue Change

State tax revenue increased 1.7 percent in the January-March quarter of 2008 compared to the same quarter the year before. This nominal growth rate slowed for the third quarter in a row and was the slowest since the first quarter of 2003. Changes in nominal tax revenues for the last 37 quarters are shown in Table 2.

Inflation for goods and services purchased by the state and local sector, as measured by the state and local government consumption expenditure index, was more than 6 percent compared to a year earlier for the second straight quarter — far above the 2.2 percent for the economy as a whole. (For more on this trend, see discussion of “Rising Cost Pressures on States and Localities” in the Rockefeller Institute’s March 2008 State Revenue Report.<sup>1</sup>) When the effects of enacted tax cuts and inflation for state and local government purchases are considered, real adjusted state tax revenue decreased by 5.3 percent (see Table 1). That, too, was the weakest performance since January-March 2003. The pattern of growth in state tax revenue, adjusted for inflation and enacted tax increases from 1991 to the present, is illustrated in Figure 1.

All three major state taxes showed weakness in the first quarter of 2008:

- ✓ Personal income tax revenue increased 4.4 percent compared to a year earlier, up slightly from the fourth quarter’s 4.0 rate but still tepid.
- ✓ The corporate income tax declined for the third consecutive quarter, although the rate of decline slowed to 5.1 percent compared with 15.3 percent in the fourth quarter of 2007.
- ✓ Sales tax collections were essentially flat, registering a slight decline of 0.04 percent, according to the Institute’s survey of state revenue agencies. (This change rounds to 0.0 percent in the tables in this report.)

States collected \$155.3 billion in the first quarter of calendar 2008, as shown in Table 10. Some \$64.0 billion, or 41 percent, was from personal income taxes. Another \$55.0 billion, or 35 percent, represented sales taxes, while corporate income taxes contributed \$10.0 billion. Collections from all other taxes totaled \$26.3 billion for the quarter. For fiscal year 2008 to date (July 2007 through March 2008), state tax revenues were \$455.4 billion, up 3.0 percent from the same period last year.

Total growth in state tax revenue in the first quarter of 2008 was barely one-third the historical average over the previous 37 quarters of 4.9 percent. Total tax revenue declined in the Southeast and Rocky Mountain regions, and growth was in the single

Table 1 Quarterly State Tax Revenue Adjusted for Legislated Tax Changes and Inflation Year-Over-Year Percent Change				
	Total Nominal Change	Adjusted Nominal Change	Inflation Rate	Adjusted Real Change
<b>2008</b>				
Jan.-March	1.7 %	0.6 %	6.2 %	(5.3) %
<b>2007</b>				
Oct.-Dec.	2.6	1.8	6.1	(4.1)
July-Sept.	4.7	4.3	5.2	(0.8)
April-June	6.1	7.2	5.1	2.0
Jan.-March	4.8	5.8	5.2	0.6
<b>2006</b>				
Oct.-Dec.	4.3	5.0	4.1	0.8
July-Sept.	4.6	5.5	5.2	0.2
April-June	9.9	9.9	6.3	3.4
Jan.-March	6.8	6.8	6.1	0.6
<b>2005</b>				
Oct.-Dec.	7.6	7.7	6.7	0.9
July-Sept.	9.3	9.7	6.7	2.8
April-June	13.2	12.9	6.2	6.3
Jan.-March	11.4	9.5	5.9	3.4
<b>2004</b>				
Oct.-Dec.	7.8	7.3	5.7	1.5
July-Sept.	8.6	8.1	4.6	3.4
April-June	11.2	9.0	3.9	4.9
Jan.-March	8.1	7.0	3.0	3.9
<b>2003</b>				
Oct.-Dec.	7.3	4.9	3.8	1.0
July-Sept.	4.5	2.6	3.9	(1.2)
April-June	3.2	0.4	3.9	(3.4)
Jan.-March	1.4	(1.0)	4.7	(5.4)
<b>2002</b>				
Oct.-Dec.	1.9	0.3	3.3	(2.9)
July-Sept.	2.5	0.7	2.7	(2.0)
April-June	(10.6)	(12.1)	2.2	(14.0)
Jan.-March	(7.8)	(8.2)	1.7	(9.7)
<b>2001</b>				
Oct.-Dec.	(2.7)	(2.2)	2.0	(4.1)
July-Sept.	(3.1)	(2.4)	2.6	(4.9)
April-June	2.5	4.2	3.3	0.8
Jan.-March	5.1	6.3	3.6	2.6
<b>2000</b>				
Oct.-Dec.	4.0	5.0	4.2	0.7
July-Sept.	7.1	7.7	4.5	3.0
April-June	11.4	11.8	4.5	6.9
Jan.-March	9.7	10.4	4.8	5.3
<b>1999</b>				
Oct.-Dec.	7.4	8.4	3.7	4.5
July-Sept.	6.1	6.7	3.2	3.4
April-June	5.0	8.0	2.7	5.1
Jan.-March	4.8	6.5	2.0	4.4

Source: Individual state data, analysis by Rockefeller Institute. Legislated tax changes by National Conference of State Legislatures (NCSL). Inflation is measured by BEA State and Local Government Consumption Expenditures and Gross Investment Price Index.

Table 2 Quarterly State Tax Revenue By Major Tax, Year-Over-Year Percent Change				
	PIT	CIT	Sales	Total
<b>2008</b>				
Jan.-March	4.4 %	(5.1) %	0.0 %	1.7 %
<b>2007</b>				
Oct.-Dec.	4.0	(15.3)	2.3	2.6
July-Sept.	6.3	(2.8)	3.1	4.7
April-June	8.7	2.5	3.1	6.1
Jan.-March	6.8	14.3	2.8	4.8
<b>2006</b>				
Oct.-Dec.	4.0	16.8	5.0	4.3
July-Sept.	6.6	11.1	4.1	4.6
April-June	15.1	14.7	5.7	9.9
Jan.-March	10.6	(13.8)	6.6	6.8
<b>2005</b>				
Oct.-Dec.	5.7	24.8	5.5	7.6
July-Sept.	9.0	25.4	7.8	9.3
April-June	18.2	21.9	7.9	13.2
Jan.-March	11.6	61.6	6.1	11.4
<b>2004</b>				
Oct.-Dec.	8.8	27.0	6.0	7.8
July-Sept.	8.3	23.2	5.8	8.6
April-June	15.6	13.6	7.1	11.2
Jan.-March	8.7	15.2	8.3	8.1
<b>2003</b>				
Oct.-Dec.	6.6	11.1	6.6	7.3
July-Sept.	5.1	9.0	3.7	4.5
April-June	(0.9)	17.9	2.9	3.1
Jan.-March	(3.1)	10.3	1.9	1.4
<b>2002</b>				
Oct.-Dec.	(0.7)	22.4	0.7	1.9
July-Sept.	(1.6)	4.8	3.8	2.5
April-June	(22.3)	(11.7)	1.5	(10.4)
Jan.-March	(14.3)	(16.1)	(1.0)	(7.8)
<b>2001</b>				
Oct.-Dec.	(2.7)	(31.8)	1.0	(2.7)
July-Sept.	(3.7)	(24.0)	0.0	(3.1)
April-June	5.4	(13.1)	0.5	2.5
Jan.-March	8.7	(9.1)	3.4	5.1
<b>2000</b>				
Oct.-Dec.	5.8	(7.7)	4.2	4.0
July-Sept.	11.0	5.7	4.6	7.1
April-June	18.8	4.2	7.3	11.4
Jan.-March	13.6	8.0	8.2	9.7
<b>1999</b>				
Oct.-Dec.	9.1	3.8	7.3	7.4
July-Sept.	7.6	1.4	6.7	6.1
April-June	6.0	(2.1)	7.3	5.0
Jan.-March	6.6	(2.6)	6.1	4.8

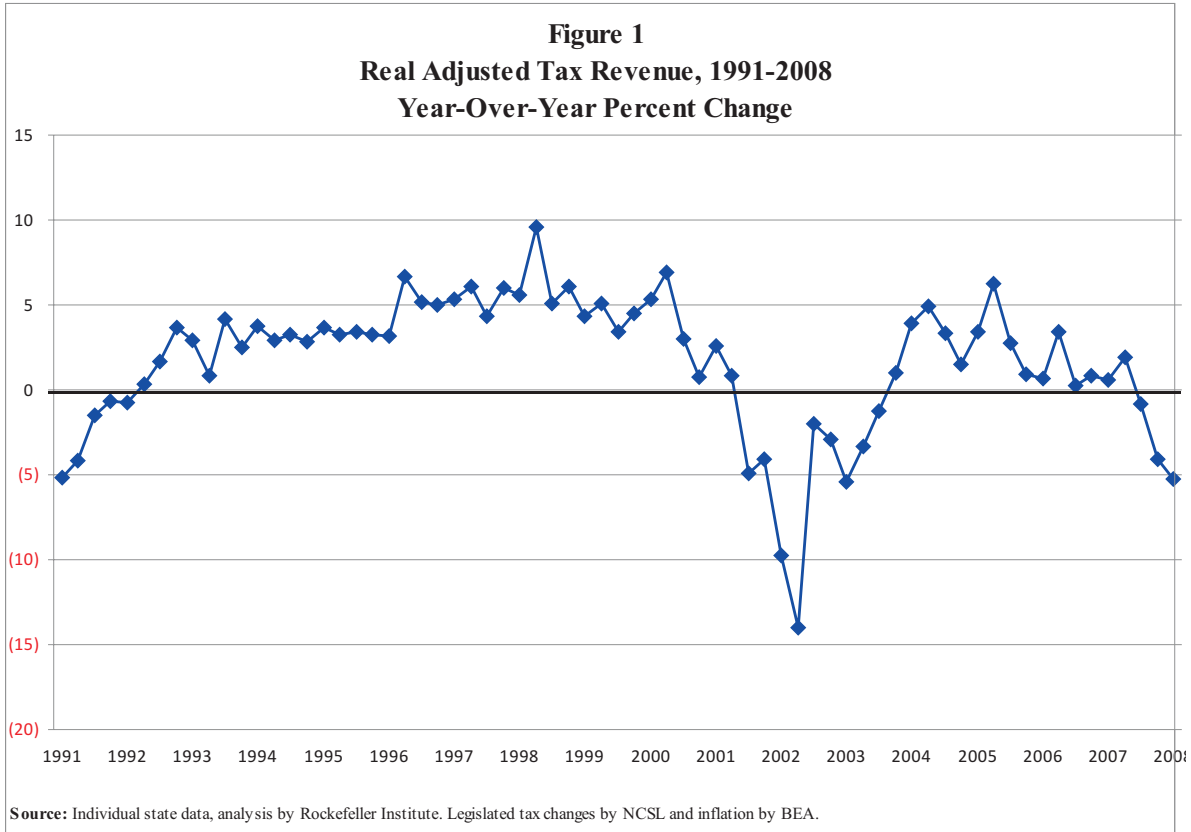
Source: Individual state data, analysis by Rockefeller Institute.

digits in all other regions. The New England states showed the strongest overall revenue growth of 5.3 percent, while the Southeast states saw revenue decline by 2.6 percent. Growth of 10 percent or more was recorded in only four states, while 15 states had revenue declines for the quarter. Table 3 shows the growth by state and region for the states' three major taxes and total taxes.

Total collections were up more than 10 percent in Alaska, Iowa, North Dakota, and West Virginia. Total revenues fell by more than 10 percent in

Arizona, Montana, and Florida; Georgia, Idaho, Mississippi, Nebraska, Nevada, New Jersey, North Carolina, Ohio, Oklahoma, Rhode Island, South Carolina, and Utah showed smaller declines.

According to Rockefeller Institute analysis of data from the National Conference of State Legislatures, legislated changes decreased total tax revenue in the Plains, Southeast, Southwest, and Rocky Mountain states. Ohio registered the largest net tax cuts for a single state, with a reduction of \$269 million. Figure 2 shows tax revenue adjusted for legislated changes, by region. Table 4 shows the overall effect of legislated tax changes and processing



variations. Table 5 shows the percentage change in each state’s total tax revenue, adjusted for legislated tax changes and inflation.

Due to delays in data availability, this report does not include complete figures for New Mexico.

### **Personal Income Tax**

In the first quarter of 2008, personal income tax revenue made up at least 50 percent of total tax revenue in 12 states, and at least 40 percent in 10 more states.

Personal income tax revenue grew 4.4 percent in the January-March 2008 quarter compared to the same quarter in 2007, the third-lowest increase in 19 quarters. The strongest growth in state personal income tax revenue was in the New England region, where collections grew 10.2 percent, followed by the Great Lakes states, at 8.3 percent. Collections decreased by 14.4 percent in the Southwest region<sup>2</sup> and by 2.1 percent in the Rocky Mountain states.

Of the 40 states with a broad-based personal income tax and for which first quarter information is

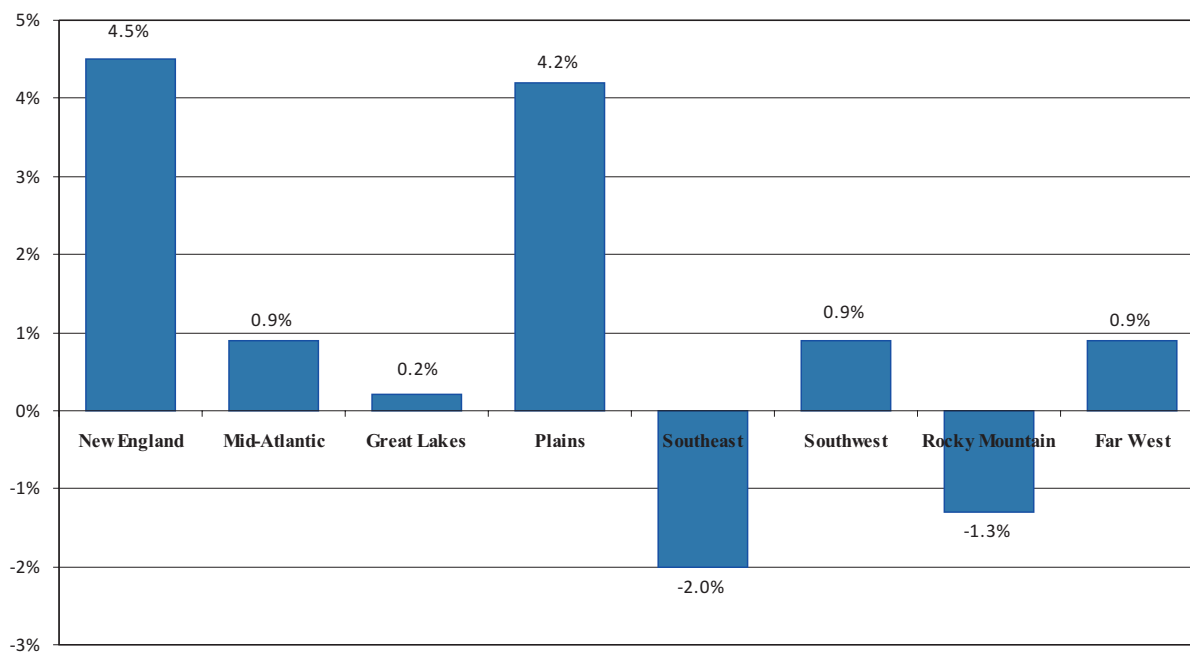
available, 28 reported growth, while nine states had double-digit increases. Wisconsin led the states with growth of 18 percent. Twelve states showed a decline in personal income tax collections, the largest being 33 percent for Mississippi, which was influenced by processing changes.

We can get a clearer picture of collections from the personal income tax by breaking this source down into major component parts for which we have data: withholding and quarterly estimated payments.

### **Withholding**

Withholding is a good indicator of the current strength of personal income tax revenue because it comes largely from current wages and is much less volatile than estimated payments or final settlements. Table 6 shows that withholding for the January-March 2008 quarter was 4.0 percent higher than the same quarter of 2007, and down significantly from the October-December quarter’s 6.6 percent growth. Arkansas, Hawaii, Michigan, North Dakota, West Virginia, and Wisconsin reported strong growth of more than 10 percent.

**Figure 2**  
**Tax Revenue, Adjusted for Legislated Changes,**  
**January-March, 2007 to 2008 Percent Change**



Source: Individual state data, analysis by Rockefeller Institute.

### *Estimated Payments*

The highest-income taxpayers generally pay estimated tax payments (also known as declarations) on their income not subject to withholding tax. This income often comes from investments, such as capital gains realized in the stock market. A strong stock market should eventually translate into capital gains and higher estimated tax payments. Strong business profits also tend to boost these payments.

The first payment for each tax year is due in April in most states. Often it is made on the basis of the previous year's tax liability and may offer little insight into income in the current year. It is not safe to extrapolate trends from this first payment, or often even from the first several payments. In the 35 states for which we have complete data for the first payment, the median payment was 10.4 percent higher than the year earlier (see Table 7). Increases were recorded in 29 of 35 states. Eighteen states reported double-digit growth, with eight states having increases of more than 20 percent. Six states —

Maryland, Missouri, Oklahoma, South Carolina, Virginia, and West Virginia — showed year-over-year declines in estimated payments for the first payment in April 2008.

### *General Sales Tax*

The Rockefeller Institute's survey of data from the states showed that collections in the January-March 2008 quarter were down slightly from the same quarter in 2007 — 0.04 percent — the first decline in six years. This is far weaker than the historical average over the past 37 quarters of 4.4 percent.

Sales tax revenue grew fastest in the Southwest and Mid-Atlantic regions at 4.9 and 2.4 percent, respectively. Maryland had the highest increase nationally, at 8.5 percent, in part reflecting an increase in its rate from 5 percent to 6 percent in January. The Southeast region recorded an overall decline of 3.8 percent and accounted for nine of the 23 states that had declines. South Carolina, Virginia, and Florida had the largest declines at 7.6

**Table 3**  
**Quarterly Tax Revenue by Major Tax, by State**  
**January-March, 2007 to 2008, Percent Change**

	PIT	CIT	Sales	Total
<b>United States</b>	<b>4.4</b>	<b>(5.1)</b>	<b>0.0</b>	<b>1.7</b>
<b>New England</b>	<b>10.2</b>	<b>(9.2)</b>	<b>(0.9)</b>	<b>5.3</b>
Connecticut	6.8	(15.4)	(0.2)	1.9
Maine	4.6	8.4 *	0.3	2.8 *
Massachusetts	14.7	(6.9)	(1.4)	9.6
New Hampshire	NA	(23.3)	NA	5.6 *
Rhode Island	(12.2) *	2.5 *	(5.5)	(6.2) *
Vermont	13.5	(21.6) *	4.9	1.5 *
<b>Mid Atlantic</b>	<b>5.1</b>	<b>16.2 *</b>	<b>2.4 *</b>	<b>3.6 *</b>
Delaware	(3.6)	10.6	NA	0.3 *
Maryland	2.9	15.8 *	8.5 *	6.2 *
New Jersey	0.3	6.9 *	1.1 *	(0.3) *
New York	5.8	17.8 *	4.2	5.2
Pennsylvania	10.0	19.9 ¶	(1.0)	2.8
<b>Great Lakes</b>	<b>8.3</b>	<b>(9.6) *</b>	<b>0.5</b>	<b>2.6 *</b>
Illinois	5.2	22.8 *	0.1	3.6
Indiana	5.5 ¶	(56.0) ¶	3.2	1.7 *
Michigan	13.6 *	(16.8) *	(0.7)	2.1 *
Ohio	4.9 ¶	(15.3) *	0.5	(1.2) ¶
Wisconsin	17.5	(24.6)	(0.1)	8.1 *
<b>Plains</b>	<b>6.8 ¶</b>	<b>(6.0)</b>	<b>0.3</b>	<b>3.8</b>
Iowa	10.2	29.8	5.2	11.4 *
Kansas	8.8	49.4 ¶	(1.3)	5.9
Minnesota	6.1	(28.4)	0.0	1.1
Missouri	9.0	0.0	(3.0)	2.4
Nebraska	(7.8) ¶	9.4	1.3	(1.9) ¶
North Dakota	1.8 ¶	22.0 ¶	2.6	20.2 ¶
South Dakota	NA	NA	5.9	0.4 *
<b>Southeast</b>	<b>1.4 ¶</b>	<b>(10.6)</b>	<b>(3.8)</b>	<b>(2.6)</b>
Alabama	4.4 *	23.7	(1.8)	2.4
Arkansas	11.8	(20.8) ¶	(3.4) ¶	2.8 ¶
Florida	NA	(8.9)	(6.0)	(10.3)
Georgia	(4.9)	(11.4)	(3.0)	(3.8)
Kentucky	10.8	(68.2)	2.5	1.2
Louisiana	4.4 ¶	(32.7) ¶	2.9	0.9 ¶
Mississippi	(32.7) ¶	34.4 ¶	0.4	(1.0) ¶
North Carolina	2.4	(46.0) ¶	(4.1) *	(3.0)
South Carolina	(18.7) ¶	(15.7)	(7.6) ¶	(8.1) ¶
Tennessee	NA	(9.8) *	(0.7)	0.6 *
Virginia	4.5	16.9	(7.0)	0.7
West Virginia	17.3	128.0 ¶	(0.7) ¶	14.1 ¶
<b>Southwest</b>	<b>(14.4) ¶</b>	<b>(56.5) ¶</b>	<b>4.9</b>	<b>0.4</b>
Arizona	(21.0)	(50.2)	(4.7)	(13.6)
New Mexico	ND	ND	ND	ND
Oklahoma	(4.2)	(60.9)	6.8	(5.8)
Texas	NA	NA	6.7	4.4
<b>Rocky Mountain</b>	<b>(2.1)</b>	<b>(17.3)</b>	<b>(1.8) ¶</b>	<b>(2.1)</b>
Colorado	1.2	17.8	(0.6)	1.0
Idaho	(12.9)	(1.3)	(1.9)	(1.0)
Montana	(5.9) *	(41.0)	NA	(10.8) ¶
Utah	(1.3) ¶	(39.2)	(4.7) ¶	(5.6) ¶
Wyoming	NA	NA	4.5	5.8
<b>Far West</b>	<b>2.9</b>	<b>(7.6)</b>	<b>(0.4)</b>	<b>2.6 *</b>
Alaska	NA	(51.0)	NA	152.2 *
California	2.5	(7.9)	(0.9)	0.1
Hawaii	(1.4)	60.8	2.4 ¶	2.0 ¶
Nevada	NA	NA	(5.9)	(4.9)
Oregon	7.9	35.6 ¶	NA	9.5 *
Washington	NA	NA	2.6	0.2

Source: Individual state data, analysis by Rockefeller Institute. See page 11 for notes.

percent, 7.0 percent, and 6.0 percent, respectively. The South Carolina decline was influenced by its elimination of the sales tax on unprepared food in addition to underlying economic trends.

### Corporate Income Tax

Corporate income tax revenue is highly variable because of volatility in corporate profits, and volatility in the timing of tax payments. Many states, such as Delaware, Hawaii, Montana, Rhode Island, and Vermont, collect relatively little revenue from corporate taxes, resulting in large fluctuations in percentage terms. As a result, corporate income tax is an unstable revenue source and many states report sizeable changes from quarter to quarter.

Nominal corporate tax revenue decreased 5.1 percent in the January-March quarter compared to a year earlier, the third consecutive decline. All regions except the Mid-Atlantic reported declines, and the Southwest region reported the largest decline at 56.5 percent. This was heavily influenced by a huge one-time tax payment in Oklahoma in 2007, leading to a large year-over-year decline in 2008. Among 44 states that have a corporate income tax and for which first quarter information is available, 24 showed decreases in corporate tax revenue. Kentucky had the largest decline, reflecting legislative changes and a high level of refunds.

### Underlying Reasons for Trends

State revenue changes result from three kinds of underlying forces: differences in the national and state economies, the ways in which these differences affect each state's tax system, and recently legislated tax changes. The next two sections discuss the first and third reason; see the box on *Tax Structure and Revenue Growth* for discussion of the second reason.

<b>Table 4</b>			
<b>Quarterly State Tax Revenue</b>			
<b>Adjusted for Legislated Tax Changes</b>			
<b>Year-Over-Year Percent Change</b>			
	PIT	Sales	Total
<b>2008</b>			
Jan.-March	4.7 %	(1.0) %	0.6 %
<b>2007</b>			
Oct.-Dec.	4.3	1.6	1.8
July-Sept.	7.0	2.3	4.3
April-June	10.7	2.6	7.2
Jan.-March	8.2	2.6	5.8
<b>2006</b>			
Oct.-Dec.	5.3	4.7	5.0
July-Sept.	8.1	4.2	5.5
April-June	15.4	6.5	9.9
Jan.-March	10.9	7.4	6.8
<b>2005</b>			
Oct.-Dec.	6.0	6.4	7.7
July-Sept.	9.2	8.6	9.7
April-June	17.7	7.8	12.9
Jan.-March	11.2	6.0	9.5
<b>2004</b>			
Oct.-Dec.	8.3	5.7	7.3
July-Sept.	7.3	5.6	8.1
April-June	12.6	6.4	9.0
Jan.-March	7.7	6.8	7.0
<b>2003</b>			
Oct.-Dec.	5.3	4.2	4.9
July-Sept.	3.9	1.9	2.6
April-June	(2.0)	1.3	0.4
Jan.-March	(4.4)	1.0	(1.0)
<b>2002</b>			
Oct.-Dec.	(1.6)	0.7	0.3
July-Sept.	(2.1)	2.7	0.7
April-June	(22.5)	0.1	(11.9)
Jan.-March	(14.5)	(2.4)	(8.4)
<b>2001</b>			
Oct.-Dec.	(2.1)	1.2	(2.3)
July-Sept.	(2.8)	0.4	(2.4)
April-June	7.9	0.6	4.2
Jan.-March	10.1	3.7	6.3
<b>2000</b>			
Oct.-Dec.	6.5	5.0	5.0
July-Sept.	11.6	5.6	7.7
April-June	18.6	7.8	11.8
Jan.-March	13.8	8.8	10.4
<b>1999</b>			
Oct.-Dec.	11.0	7.5	8.4
July-Sept.	8.3	6.9	6.7
April-June	12.4	7.3	8.0
Jan.-March	9.9	6.2	6.5

Source: Individual state data, NCSL, analysis by Rockefeller Institute.

Note: The corporate income tax is not included in this table. The quarterly effect of legislation on this tax's revenue is especially uncertain (see Technical Notes).

## National and State Economies

By traditional measures the national economy has weakened significantly and may have slipped into recession. Real gross domestic product grew at a subpar 1.0 percent annual rate in the January-March quarter, and only 0.6 percent in the October-December quarter. Residential investment

<b>Table 5</b>	
<b>Quarterly Total Tax Revenue, by State</b>	
<b>Adjusted for Legislation and Inflation</b>	
<b>January-March, 2007 to 2008, Percent Change</b>	
<b>United States</b>	<b>(5.3) %</b>
<b>New England</b>	<b>(1.6)</b>
Connecticut	(4.6)
Maine	(4.2)
Massachusetts	3.2
New Hampshire	(3.7)
Rhode Island	(17.4)
Vermont	(6.2)
<b>Mid-Atlantic</b>	<b>(5.0)</b>
Delaware	(7.4)
Maryland	(8.9)
New Jersey	(13.7)
New York	(1.8)
Pennsylvania	(3.0)
<b>Great Lakes</b>	<b>(5.6)</b>
Illinois	(3.2)
Indiana	(7.1)
Michigan	(17.1)
Ohio	(1.6)
Wisconsin	(0.8)
<b>Plains</b>	<b>(1.9)</b>
Iowa	3.1
Kansas	0.3
Minnesota	(4.7)
Missouri	(3.5)
Nebraska	(1.2)
North Dakota	17.7
South Dakota	(9.9)
<b>Southeast</b>	<b>(7.7)</b>
Alabama	(4.3)
Arkansas	(0.8)
Florida	(15.5)
Georgia	(9.2)
Kentucky	(4.3)
Louisiana	(2.8)
Mississippi	(5.8)
North Carolina	(9.1)
South Carolina	(7.9)
Tennessee	(7.2)
Virginia	(4.8)
West Virginia	8.8
<b>Southwest</b>	<b>(5.0)</b>
Arizona	(18.6)
New Mexico	ND
Oklahoma	(10.9)
Texas	(1.4)
<b>Rocky Mountain</b>	<b>(7.1)</b>
Colorado	(5.5)
Idaho	(6.8)
Montana	(10.8)
Utah	(9.5)
Wyoming	(0.3)
<b>Far West</b>	<b>(5.0)</b>
Alaska	38.3
California	(5.8)
Hawaii	(2.2)
Nevada	(9.7)
Oregon	(0.5)
Washington	(5.6)

Source: Individual state data, NCSL, analysis by Rockefeller Institute.

See page 11 for notes.

Note: Inflation is measured by BEA State and Local Government Consumption Expenditures and Gross Investment Price Index.

declined at a 24.6 percent rate in the January-March quarter, and durable goods consumption — an important element of state sales tax bases — declined at a 6.0 percent rate.



	2007		2008	
	Apr.-Jun.	July-Sept.	Oct.-Dec.	Jan.-Mar.
<b>United States</b>	<b>6.6 %</b>	<b>6.0 %</b>	<b>6.6 %</b>	<b>4.0 %</b>
<b>New England</b>	<b>6.2</b>	<b>5.6</b>	<b>6.7</b>	<b>4.5</b>
Connecticut	6.3	8.8	7.9	2.6
Maine	3.7	2.4	4.4	6.3
Massachusetts	6.7	5.2	6.5	5.6
Rhode Island	4.1	(1.4)	6.1 *	(0.4) *
Vermont	7.1	6.3 *	7.3	9.5
<b>Mid-Atlantic</b>	<b>8.8</b>	<b>7.2</b>	<b>5.7</b>	<b>3.6</b>
Delaware	0.7	0.0	5.6	(0.3)
Maryland	7.0 *	6.6 *	7.8	3.3
New Jersey	14.3	8.6	2.6	3.5
New York	8.5	9.2	6.0	3.1
Pennsylvania	8.1	2.1	5.5	6.9
<b>Great Lakes</b>	<b>3.8</b>	<b>3.2</b>	<b>5.5</b>	<b>7.5</b>
Illinois	7.0 ¶	2.3	8.1	7.2
Indiana	5.6	7.2	6.0 ¶	7.2 ¶
Michigan	3.2	3.5	11.0 *	10.0 *
Ohio	(4.4)	(1.0) ¶	2.5 ¶	(1.0) ¶
Wisconsin	9.9	7.4	(0.2)	15.9
<b>Plains</b>	<b>6.4</b>	<b>5.8</b>	<b>7.2 ¶</b>	<b>6.7 ¶</b>
Iowa	6.9	5.4	8.3	8.1
Kansas	14.4	6.9	8.9	7.4
Minnesota	4.9	4.8	5.2	6.1
Missouri	5.9	5.2	8.3	7.2
Nebraska	1.2	10.4	8.2 ¶	2.9 ¶
North Dakota	11.5	3.9	9.2 ¶	11.2 ¶
<b>Southeast</b>	<b>8.9</b>	<b>7.0</b>	<b>6.9</b>	<b>4.4 ¶</b>
Alabama	5.0	5.6	4.3 *	5.5 *
Arkansas	7.9 ¶	7.9 ¶	11.5	10.2
Georgia	9.4	6.4	5.6	1.9
Kentucky	6.3	6.1	3.8	7.8
Louisiana	29.5	16.9	15.2 ¶	3.5 ¶
Mississippi	7.9	8.6 ¶	8.6 ¶	3.8 ¶
North Carolina	9.1	7.4 ¶	7.4	3.0
South Carolina	8.0 ¶	3.1 *	8.8 ¶	2.9 ¶
Virginia	8.0	4.7	6.4	5.2
West Virginia	6.7 ¶	23.3	1.2	14.7
<b>Southwest</b>	<b>0.8</b>	<b>3.0</b>	<b>2.9</b>	<b>(1.5) ¶</b>
Arizona	5.2	8.0	1.8	(1.7)
New Mexico	9.5	8.1	11.8 ¶	ND
Oklahoma	(7.4)	(4.5)	0.7	(1.3)
<b>Rocky Mountain</b>	<b>10.2</b>	<b>8.5</b>	<b>8.7</b>	<b>4.1</b>
Colorado	6.9	7.1	8.1	7.5
Idaho	6.6	10.9	9.1	(2.4)
Montana	12.1	14.6	10.1	4.8 *
Utah	17.2 ¶	8.0 ¶	9.2 ¶	1.3 ¶
<b>Far West</b>	<b>4.2</b>	<b>6.0</b>	<b>8.1</b>	<b>1.3</b>
California	4.4	7.1	8.9	0.7
Hawaii	9.5 ¶	3.5 ¶	6.6	20.9
Oregon	1.5	(0.3)	2.4	1.2

Source: Individual state data, analysis by Rockefeller Institute. See page 11 for notes.

Note: Nine states — Alaska, Florida, New Hampshire, Nevada, South Dakota, Tennessee, Texas, Washington, and Wyoming — have no personal income tax and are therefore not shown in this table.

It is helpful to examine economic measures that are more closely related to state tax bases. Most states rely heavily on income taxes and sales taxes, and growth in income and consumption are extremely important to these revenue sources. Figure 3 shows year-over-year growth in two important

sources of income: wages, and the portion of nonwage income typically subject to income taxes.<sup>3</sup> It also shows growth in consumption of goods (excluding services because most states exclude a substantial share of services from the sales tax). All the data are adjusted for inflation. The time period covered is January 2000 through May 2008 (two months after the close of the quarter reported on here).

Several important points are evident:

- ✓ Income and consumption have both slowed sharply.
- ✓ Real consumption is much weaker than wage and nonwage income, with virtually no year-over-year growth in recent months.
- ✓ Income and consumption continued to weaken in April and May (after the period covered by this report), suggesting that tax collections are likely to deteriorate further.
- ✓ Nonwage income historically has been more volatile than either wages or consumption. This income fell extremely sharply in the 2002-2003 period and the recent slowdown in this income — so far — pales in comparison to that period.

Unfortunately, state-by-state data on income and consumption are not available on a timely basis, and so we cannot easily see variation across the country in these trends. Traditionally, the Rockefeller Institute has relied on employment data from the Bureau of Labor Statistics to examine state-by-state economic conditions. These data are relatively timely and are of high quality.

Table 8 shows year-over-year employment growth for the last four quarters. The regional patterns are quite varied: The Great Lakes region has suffered a malaise for at least a year, the Mid-Atlantic, Plains, and New England regions (excepting Rhode Island) have been relatively stable, and other regions have slowed sharply over the last year. The fastest growth continues to occur in the Southwest and Rocky Mountain states, but employment has slowed there as well.

Thanks to work by economists at the Philadelphia Federal Reserve Bank, we now have the ability to supplement employment data with broader and highly timely measures known as “coincident economic indexes” intended to provide information

	April 2006 - January 2007 (All four payments)	December 2006 -January 2007 (Fourth payment)	April 2008 (First payment)
<b>Average (Mean)</b>	<b>11.0 %</b>	<b>8.2 %</b>	<b>26.5 %</b>
<b>Median</b>	<b>10.0</b>	<b>5.8</b>	<b>10.4</b>
Alabama	5.9	(3.3)	14.4
Arizona	ND	ND	ND
Arkansas	17.4	23.5	23.9
California	8.9	9.7	0.5
Colorado	15.6	(1.0)	33.3
Connecticut	16.3	18.7	4.6
Delaware	(2.0)	(12.2)	12.8
Georgia	7.1	(6.6)	341.0
Hawaii	3.6	7.0	28.4
Illinois	17.3	16.8	4.3
Indiana	9.7	4.7	18.4
Iowa	13.9	6.9	15.1
Kansas	18.3	12.1	10.4
Kentucky	49.9	71.4	221.0
Louisiana	12.8	5.9	52.7
Maine	5.3	(4.9)	8.1
Maryland	10.7	5.5	(0.6)
Massachusetts	20.1	27.6	12.0
Michigan	10.2	5.7	13.6
Minnesota	7.8	3.2	ND
Missouri	17.1	17.6	(6.2)
Montana	0.1	19.0	79.2
Nebraska	2.9	(12.6)	16.3
New Jersey	15.4	9.2	4.4
New Mexico	ND	ND	ND
New York	12.5	17.6	50.3
North Carolina	12.6	8.0	1.3
North Dakota	4.7	(6.5)	2.7
Ohio	4.7	4.1	5.0
Oklahoma	2.6	3.2	(6.8)
Oregon	14.8	9.1	8.9
Pennsylvania	17.1	25.0	18.4
Rhode Island	4.1	1.5	14.8
South Carolina	4.5	(6.5)	(14.9)
Vermont	18.2	26.1	6.8
Virginia	2.7	1.9	(13.2)
West Virginia	5.0	(9.1)	(59.5)
Wisconsin	6.9	(2.4)	5.8

Source: Individual state data, analysis by Rockefeller Institute. See page 11 for notes.

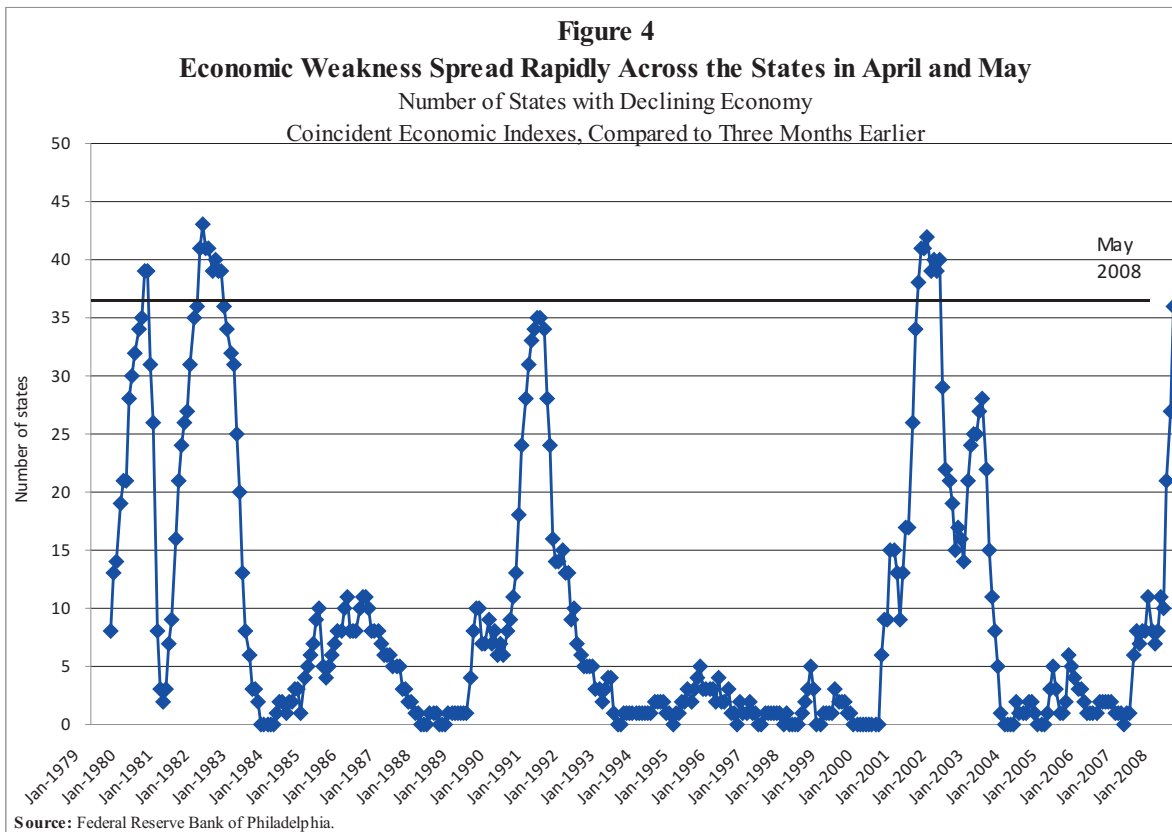
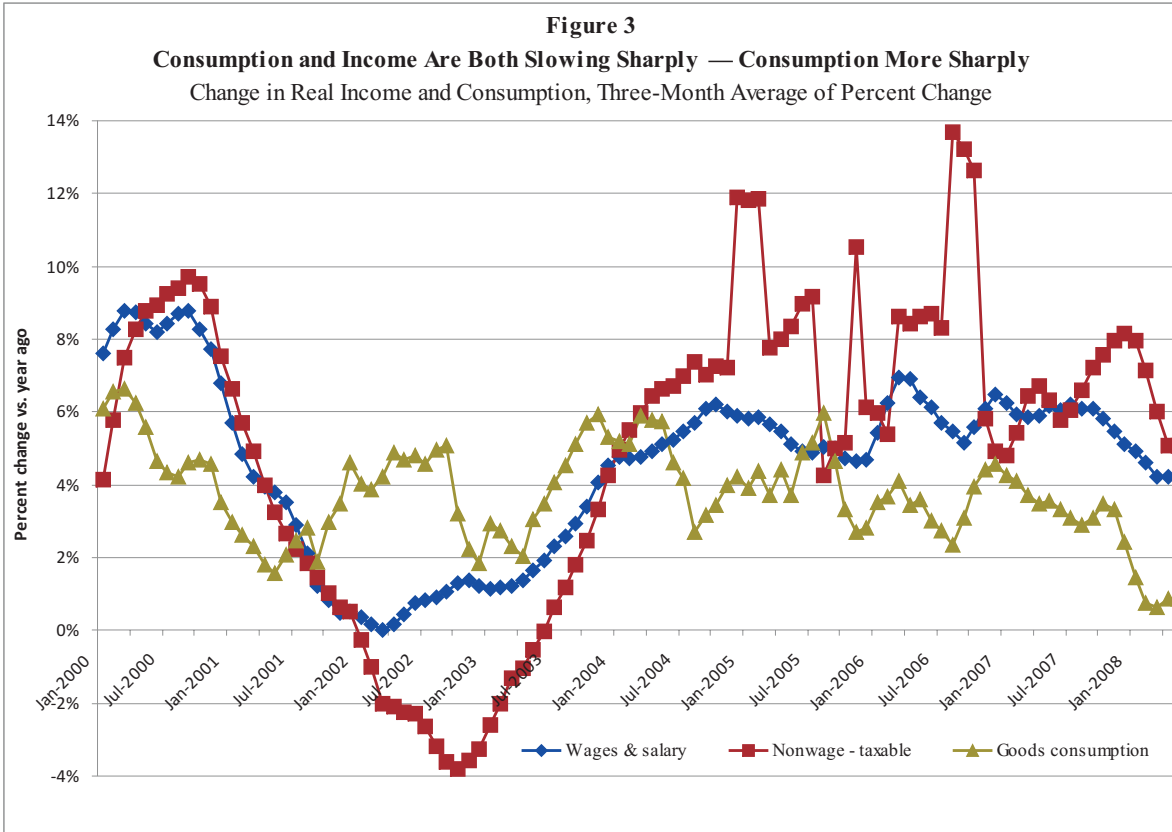
about current economic activity in individual states.<sup>4</sup> They are modeled on a similar measure for the nation as a whole, but due to limited availability of state-level data they are focused on labor market conditions, incorporating information from nonfarm payroll employment, average hours worked in manufacturing, the unemployment rate, and real wage and salary disbursements.

These indexes can be used to measure the scope of economic decline. Figure 4 shows, by month over the last three decades, the number of states that had declining economic activity relative to three months earlier. As recently as February, only 10 states suffered declines, but since then

economic weakening has spread rapidly throughout the country. By May, fully 36 states had declines in economic activity (as measured by the coincident index) compared with three months earlier. The horizontal line drawn to the left of the May 2008 point on the graph shows that declines now appear to be more widespread than in the 1990-91 recession, but slightly less so than in the 2001 and 1980-82 recessions.<sup>5</sup>

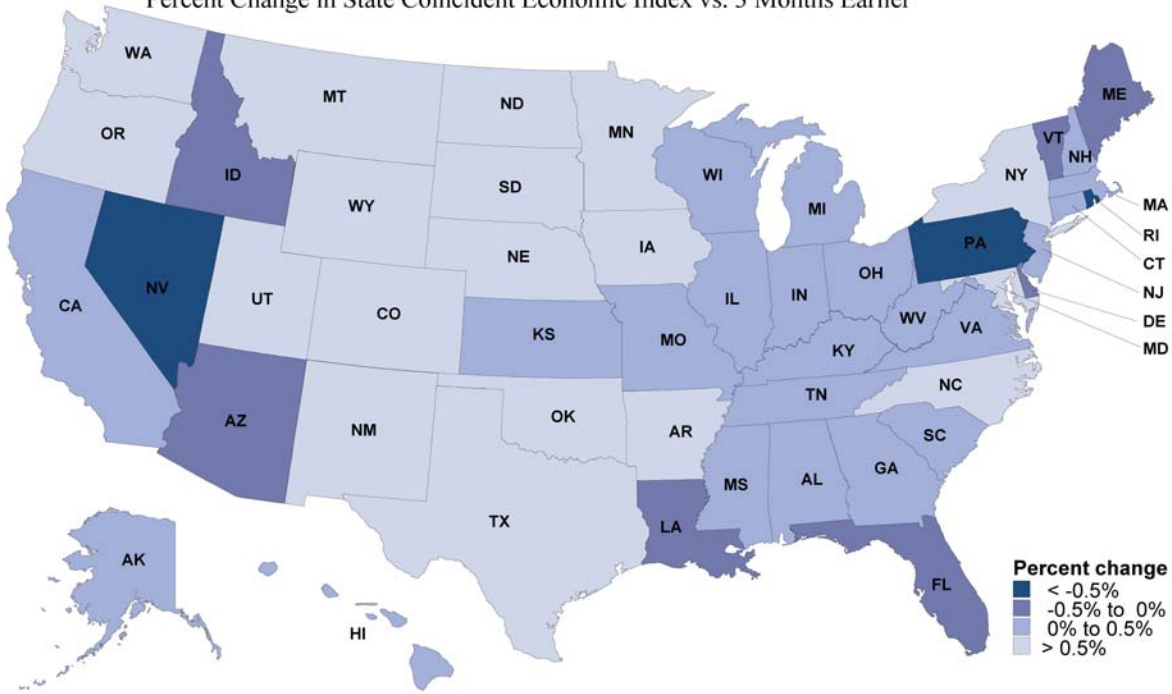
Which states have declined? As of February (the middle of the quarter reported on here) most states were growing, with only Nevada, Pennsylvania, and Rhode Island suffering significant declines and seven other states suffering less-severe





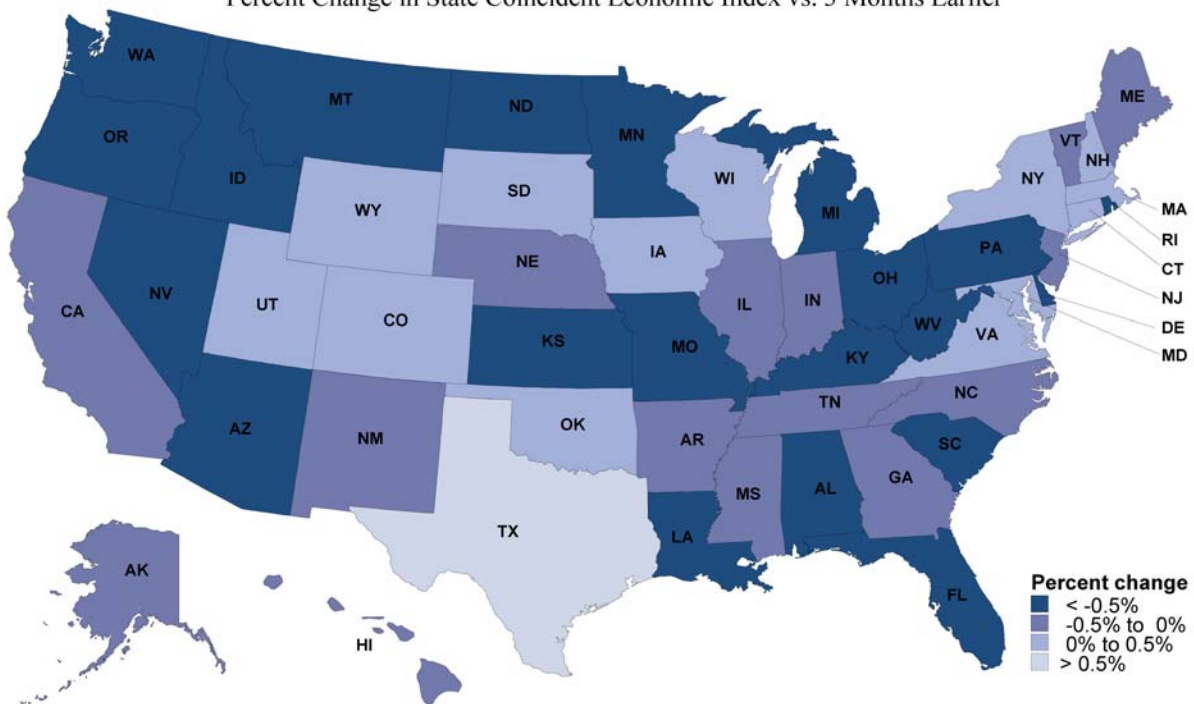
Source: Federal Reserve Bank of Philadelphia.

**Figure 5**  
**In February: Only 10 States had Declining Economies**  
 Percent Change in State Coincident Economic Index vs. 3 Months Earlier



Source: Federal Reserve Bank of Philadelphia.

**Figure 6**  
**In May: 36 States had Declining Economies**  
 Percent Change in State Coincident Economic Index vs. 3 Months Earlier



Source: Federal Reserve Bank of Philadelphia.

declines (Figure 5). Eighteen states grew by more than 0.5 percent that month. In sharp contrast, Figure 6 shows widespread declines by May (the middle of the next quarter), with only Texas growing by more than 0.5 percent.

These figures show the breadth of economic decline but provide little information on the depth of decline. Figure 7 shows the median percentage change compared to three months earlier — in a sense, how the typical state has been faring.<sup>6</sup> Here we can see that the current decline in the typical state is about as bad as it was during the 2001 recession but not yet as bad as in the 1990-91 or 1980-82 recessions. (Although the economy may be almost as weak now as in the last recession, for reasons discussed elsewhere in this report, tax revenue has not yet suffered as much as it did in the last recession.<sup>7</sup>)

The sharp and widespread weakening in April and May bodes ill for the portion of state tax collections in April-June and beyond that is driven by the current economy.

### Tax Law Changes Affecting This Quarter

Another important element affecting trends in tax revenue growth is changes in states' tax laws. When states boost or depress their revenue growth with tax increases or cuts, it can be difficult to draw

#### Key to Interpreting Tables

All percent change tables are based on year-over-year changes.

1/ Indicates data through November 2007 only.

2/ Indicates data through December 2007 only.

3/ Indicates data through June 2007 only.

\* indicates legislation or processing/accounting changes significantly increased tax receipts (by one percentage point or more).

¶ indicates legislation or processing/accounting changes significantly decreased tax receipts.

NA indicates not applicable.

ND indicates no data.

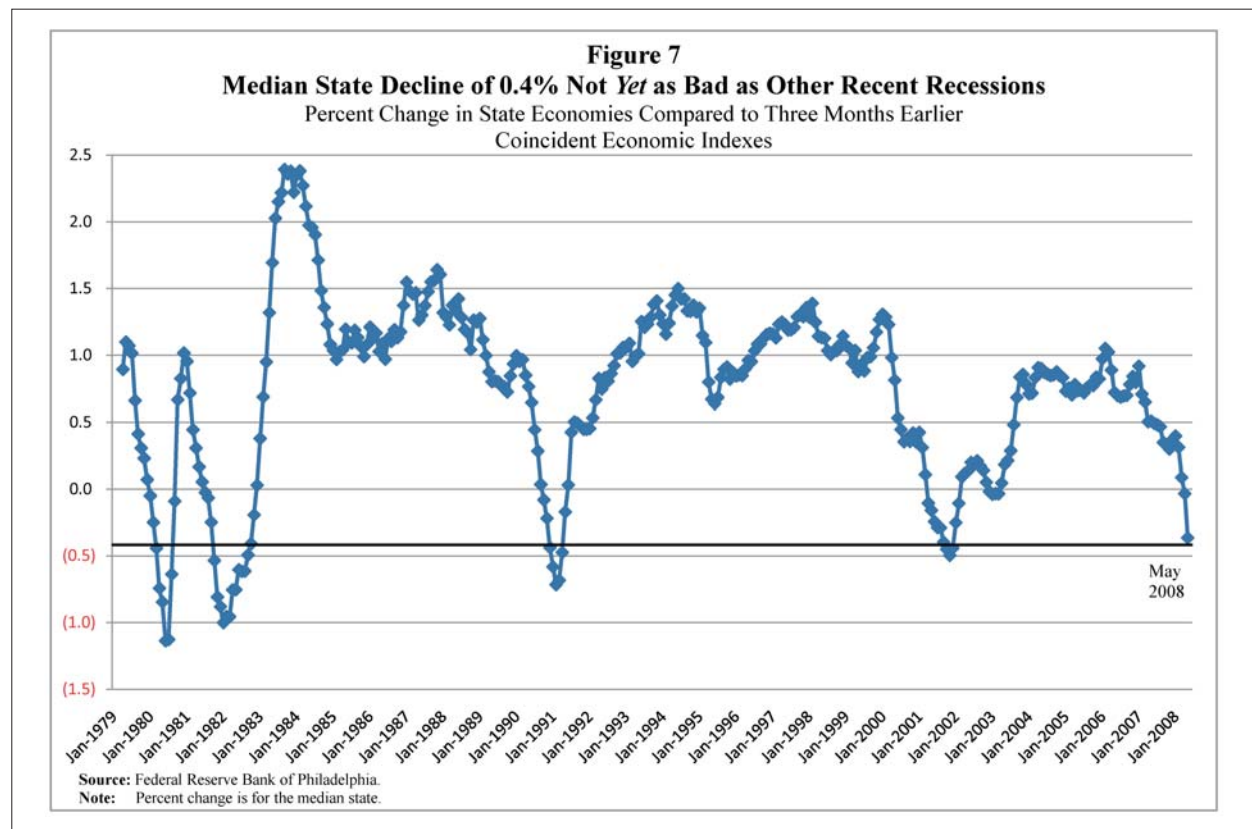
NM indicates not meaningful.

Historical Tables (Tables 1, 2, and 4) have been shortened to provide data only back to 1999. Data through 1991 are available at:

[www.rockinst.org/research/sl\\_finance/2column.aspx?id=828](http://www.rockinst.org/research/sl_finance/2column.aspx?id=828).

	2007		2008	
	Apr.-June	July-Sep.	Oct.-Dec.	Jan.-Mar.
<b>United States</b>	<b>1.2</b>	<b>1.1</b>	<b>0.8</b>	<b>0.7</b>
<b>New England</b>	<b>0.8</b>	<b>0.8</b>	<b>0.6</b>	<b>0.6</b>
Connecticut	1.0	1.1	0.9	0.7
Maine	0.1	0.6	0.5	0.2
Massachusetts	1.1	0.9	0.7	0.8
New Hampshire	0.6	1.3	1.4	1.4
Rhode Island	0.1	(0.3)	(1.1)	(1.4)
Vermont	0.1	(0.0)	(0.2)	0.1
<b>Mid-Atlantic</b>	<b>0.9</b>	<b>0.9</b>	<b>0.7</b>	<b>0.7</b>
Delaware	0.3	0.4	0.2	0.4
Maryland	0.6	0.9	0.9	1.0
New Jersey	0.2	0.1	0.0	0.3
New York	1.4	1.5	1.1	0.9
Pennsylvania	0.8	0.8	0.4	0.4
<b>Great Lakes</b>	<b>0.0</b>	<b>0.1</b>	<b>(0.1)</b>	<b>(0.1)</b>
Illinois	0.9	0.7	0.6	0.5
Indiana	0.5	0.8	0.5	0.5
Michigan	(1.6)	(1.2)	(1.5)	(1.3)
Ohio	(0.2)	(0.2)	(0.2)	(0.0)
Wisconsin	0.7	0.4	0.3	(0.1)
<b>Plains</b>	<b>1.0</b>	<b>1.2</b>	<b>0.8</b>	<b>0.8</b>
Iowa	0.8	0.9	0.6	0.8
Kansas	2.0	2.3	1.4	1.2
Minnesota	0.4	0.6	0.5	0.5
Missouri	0.8	0.9	0.5	0.3
Nebraska	1.6	2.0	1.8	1.9
North Dakota	1.5	1.6	1.5	1.9
South Dakota	2.1	2.1	1.6	1.8
<b>Southeast</b>	<b>1.4</b>	<b>1.1</b>	<b>0.9</b>	<b>0.6</b>
Alabama	1.3	1.2	1.4	0.8
Arkansas	0.4	0.3	0.5	0.3
Florida	0.7	(0.1)	(0.2)	(0.5)
Georgia	1.4	1.4	0.9	0.9
Kentucky	1.3	1.2	1.3	1.3
Louisiana	3.7	3.6	2.8	2.1
Mississippi	1.0	0.8	0.6	0.7
North Carolina	2.8	2.3	1.8	1.6
South Carolina	2.1	3.2	1.6	1.0
Tennessee	0.4	0.5	0.4	0.2
Virginia	0.9	0.9	0.7	0.5
West Virginia	0.3	0.1	(0.1)	0.3
<b>Southwest</b>	<b>2.5</b>	<b>2.3</b>	<b>2.0</b>	<b>1.8</b>
Arizona	1.4	0.9	0.1	0.1
New Mexico	1.3	1.2	1.0	0.6
Oklahoma	1.7	1.7	1.6	1.5
Texas	3.0	2.9	2.6	2.4
<b>Rocky Mountain</b>	<b>3.0</b>	<b>2.8</b>	<b>2.4</b>	<b>2.0</b>
Colorado	2.3	2.5	2.1	2.0
Idaho	3.0	2.4	2.1	0.7
Montana	2.1	2.3	2.2	1.6
Utah	4.4	3.7	3.0	2.4
Wyoming	3.8	3.7	3.4	3.0
<b>Far West</b>	<b>1.1</b>	<b>0.9</b>	<b>0.6</b>	<b>0.4</b>
Alaska	0.5	0.6	0.8	0.6
California	0.8	0.6	0.2	0.1
Hawaii	1.3	0.5	0.4	0.9
Nevada	1.2	0.3	0.3	0.2
Oregon	1.7	1.5	1.1	0.9
Washington	2.6	2.6	2.4	2.0

Source: Bureau of Labor Statistics, analysis by Rockefeller Institute.



any conclusions about their current fiscal condition from nominal collections data. That is why this report attempts to note where such changes have significantly affected each state's revenue growth. We also occasionally note when tax-processing changes have had a major impact on revenue growth, even though these are not due to enacted legislation, as it helps the reader to understand that the apparent growth or decline is not necessarily indicative of underlying trends.

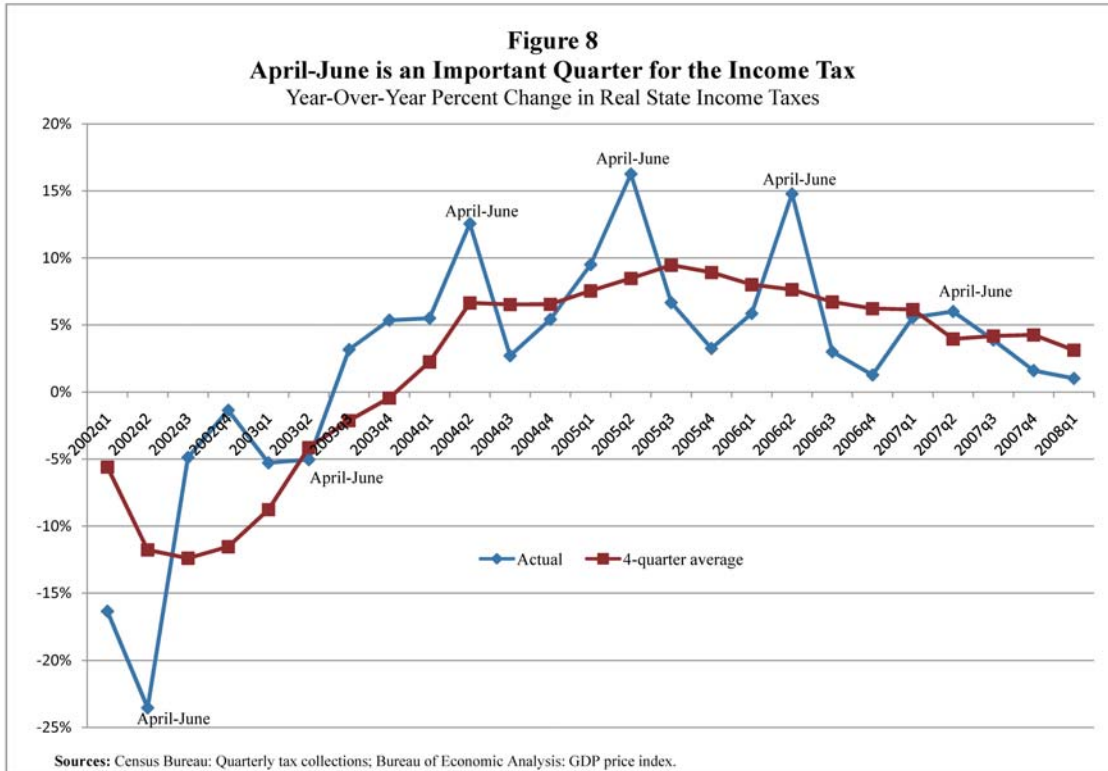
During the January-March 2008 quarter, enacted tax changes and processing variations increased state revenue by an estimated net of nearly \$1.7 billion compared to the same period in 2007. Personal income tax reductions totaled \$185 million. Among all states reporting, legislated changes are estimated to have increased sales tax revenue in the first quarter of 2008 by a net \$531 million. Corporate income tax increased by \$538 million. Taxes collected from other sources, including motor fuel, cigarette/tobacco, and alcohol increased by \$782 million.<sup>8</sup>

## Looking Ahead

### *Last Year's Economy Is Doing Well*

This report is being written as the April-June quarter draws to a close. Historically, this has been the most volatile and important quarter to state governments. It is volatile in large part because state income tax returns for the prior calendar year, typically due on April 15, are filed in this quarter. Payments with these returns can vary significantly from year to year, sometimes increasing tremendously from the year before, while declining dramatically in other years.

These payments are when taxpayers "catch up" on their prior year liability — if they underpaid taxes significantly during the course of the prior tax year, taxpayers may have to make large payments with tax returns, and if they overpaid they may have an opportunity to claim refunds or credits. Often underpayments and overpayments are influenced heavily by nonwage income earned in the prior year, especially stock market gains and income from investments. When the market is up, as it was in 2007, taxpayers may not have made payments during the year



commensurate with their gains and may owe large amounts in April. When the market is down significantly, as it is in 2008, the payments in the next April can be significantly below the prior year.

Figure 8 shows year the over-year percentage change in real income tax collections by quarter, with the April-June quarter marked. The April-June spikes are apparent. They led to a large negative surprise for state governments in 2002, and to positive surprises in 2004, 2005, and 2006. These surprises can wreak havoc on state finances — especially when they are negative — because they come at the end of the typical state fiscal year, often when states are negotiating budgets.

We will not have full information on the April-June payments until August or September, but the early reports so far are quite good. Preliminary information suggested that final payments in April were up by more than 12 percent, with increases in many states, but that payments were down in many states in May. Some of April’s healthy growth appears to have been related to processing improvements — faster receipt and depositing of payments from taxpayers — but some may also reflect bona fide increases due to income in

2007. For many states, April payments were above amounts expected. In at least some states, payments for the full April-June quarter may also be above amounts expected, although in others shortfalls on the April-June payments are expected.

Reports from Massachusetts illustrate this phenomenon: In early May, the revenue commissioner announced that April’s total tax collections were up 17 percent over the prior year, “due almost entirely to growth in income tax payments with returns and extensions, both of which reflect past economic activity rather than future economic growth.” The commissioner also noted that “faster processing of tax returns, due in part to heightened use of electronic filing, had probably netted \$60 million to \$70 million in income that otherwise would have been counted in May.” And in her press release for May, the commissioner noted that “tax collections were \$68 million below the May monthly benchmark due largely to rapid processing of tax returns and income from returns in April, which in turn reduced collections in May.”<sup>9</sup>

Several other states reported very similar patterns. For example, Kentucky reported a 36 percent increase in overall tax receipts in April, due in part



to faster processing of tax payments. At the time, the state budget director warned that much of this money would be “given back in May” and indeed May tax receipts were down by 21 percent from 2007.<sup>10</sup> Georgia released similar statements. Pennsylvania was far ahead of its target in April, but May was down year over year and the two-month total was only slightly ahead of expectations.<sup>11</sup>

Judging by reports so far, states appear to have dodged a bullet for 2007 tax returns. But with the stock market down about 10 percent so far this year, investment income for 2008 — which will play a major role in the tax payments to be made next April — could be down as well. This time next year could be quite gloomy.

### ***This Year's Economy Is Looking Worse***

While last year's economy appears to be holding up current revenues, this year's economy is not doing well. As a result, state tax collections for the April-June quarter will be affected by two seemingly contradictory forces. Strong payments with April tax returns in some states will boost cash collections, but these payments are not sustainable. Meanwhile, as discussed earlier, there has been widespread and significant economic weakening around the country in the months since the January-March quarter closed — only 10 states had declining economies in February, but 36 suffered declines in May. The economic weakening already has led to reports of significant weakness in sales taxes in some states. These two forces may lead, on balance, to adequate tax payments in April-June. The support from payments on last year's economy will dissipate after June, however, leaving only the weak current economy and deteriorating tax collections for many states. The fiscal outlook is deteriorating.

### **Conclusions**

National economic trends are holding state revenue growth to the lowest levels in nearly five years. All three major state tax sources showed weakness in the first quarter of 2008 compared to a year earlier, including no growth in the sales tax.

The national economic slowdown — or recession — is depressing state tax revenue and restraining local government tax revenue. To date, the tax revenue

	PIT	CIT	Sales	Total
<b>United States</b>	<b>4.9 %</b>	<b>(7.7) %</b>	<b>1.8 %</b>	<b>3.0 %</b>
<b>New England</b>	<b>8.9</b>	<b>(9.0)</b>	<b>2.0</b>	<b>4.5</b>
Connecticut	9.9	(28.1)	5.4	4.6
Maine	4.9	7.7	1.1	1.8
Massachusetts	9.9	(6.3)	0.7	6.1
New Hampshire	NA	3.0	NA	3.4
Rhode Island	(3.0)	(3.5)	(3.1)	(3.4)
Vermont	9.9	3.7	2.9	3.9
<b>Mid-Atlantic</b>	<b>6.6</b>	<b>(0.1)</b>	<b>3.1</b>	<b>4.1</b>
Delaware	(1.4)	(9.2)	NA	1.9
Maryland	5.2	(13.1)	5.6	4.5
New Jersey	6.1	14.4	4.7	5.3
New York	7.1	(4.8)	3.7	4.7
Pennsylvania	7.1	0.4	0.0	2.0
<b>Great Lakes</b>	<b>6.0</b>	<b>(8.3)</b>	<b>2.5</b>	<b>2.9</b>
Illinois	6.9	4.5	0.6	3.7
Indiana	4.2	(12.0)	3.7	3.0
Michigan	9.8	(4.9)	3.1	4.1
Ohio	2.8	(29.9)	3.4	0.4
Wisconsin	5.9	(13.2)	1.9	3.5
<b>Plains</b>	<b>7.3</b>	<b>(5.0)</b>	<b>1.5</b>	<b>4.4</b>
Iowa	9.6	15.9	5.3	10.5
Kansas	9.2	1.0	(3.3)	3.4
Minnesota	5.9	(20.0)	0.9	1.5
Missouri	8.4	1.5	0.8	3.9
Nebraska	3.8	11.6	1.3	3.0
North Dakota	6.5	23.6	9.8	20.7
South Dakota	NA	NA	7.5	7.5
<b>Southeast</b>	<b>4.7</b>	<b>(12.5)</b>	<b>(1.2)</b>	<b>(0.3)</b>
Alabama	4.8	4.5	0.3	3.2
Arkansas	9.9	0.7	(2.7)	3.6
Florida	NA	(8.6)	(4.7)	(8.6)
Georgia	2.5	5.5	0.0	1.6
Kentucky	8.9	(51.5)	2.6	0.6
Louisiana	6.8	(3.9)	3.1	4.0
Mississippi	(16.4)	7.1	(0.6)	(2.0)
North Carolina	5.3	(32.9)	0.8	0.5
South Carolina	1.3	(4.5)	(3.8)	(1.3)
Tennessee	NA	(12.2)	1.9	2.0
Virginia	5.3	(16.1)	0.1	2.0
West Virginia	15.6	28.6	0.3	8.3
<b>Southwest</b>	<b>(4.3)</b>	<b>(27.7)</b>	<b>5.8</b>	<b>7.3</b>
Arizona	(6.7)	(23.2)	(1.6)	(5.6)
New Mexico /1	8.5	(14.3)	1.2	2.8
Oklahoma	(5.4)	(42.4)	7.4	(1.3)
Texas	NA	NA	7.4	12.2
<b>Rocky Mountain</b>	<b>6.3</b>	<b>(2.4)</b>	<b>3.7</b>	<b>4.8</b>
Colorado	7.1	16.2	6.0	7.1
Idaho	2.9	(3.3)	8.8	6.5
Montana	9.2	(21.0)	NA	6.0
Utah	5.6	(12.6)	(3.0)	0.4
Wyoming	NA	NA	6.5	4.1
<b>Far West</b>	<b>1.3</b>	<b>(7.9)</b>	<b>1.2</b>	<b>2.4</b>
Alaska	NA	(29.6)	NA	124.9
California	4.2	(8.4)	0.2	1.2
Hawaii	1.3	9.2	4.4	3.6
Nevada	NA	NA	(4.0)	(4.1)
Oregon	(23.6)	19.8	NA	(19.3)
Washington	NA	NA	5.7	2.9

Source: Individual state data, analysis by Rockefeller Institute. See page 11 for notes.

/1/ Indicates data through December 2007 only.

weakness has been mild compared with past recessions. However, the seeds of greater fiscal stress are already sown: economic weakness is spreading rapidly and tax revenue from the “continuing” base should be very weak in the April-June quarter,



### Tax Structure and Revenue Growth

Even if economic growth affected all regions and states to exactly the same degree and at exactly the same time, the impact on state revenue would vary because the tax systems used by the states react differently to similar economic situations. States that rely heavily on the personal income tax will tend to see stronger growth in good times, since they benefit from growth in income earned by the highest income individuals. This is most evident in states with more progressive income tax structures, since higher incomes are taxed at the highest rates. The sales tax is also very responsive to economic conditions, but is historically less elastic than the personal income tax, dropping more slowly in bad times and increasing more slowly in good times. States that rely heavily on corporate income or severance taxes often see wild swings in revenue that are not necessarily related to general economic conditions. (Severance taxes are levied on the removal of natural resources, such as oil and natural gas.)

Because high-end incomes are based more heavily upon volatile sources such as stock options and capital gains, growth in personal income tax revenue is far more subject to dramatic fluctuations than it would be if it were based entirely on wages and salaries. Over the last few years, we have seen growth in the stock market and relatively strong growth in corporate profits and other business-related income. In the last recession, we saw the downside of this volatility. Declines in the stock market and other investments pushed personal and corporate income tax collections down much faster than the economy and created large holes in almost every state's budget. As was the case before the 2001 recession, capital gains now constitute a large share of adjusted gross income, and thus contribute a large share of state tax revenues.<sup>12</sup> Such an environment creates relatively high levels of risk for states that depend heavily on personal income tax revenues. Corporate profits and corporate income tax revenue both showed weak numbers in the last two quarters of 2007 and the first quarter of 2008.

Sales tax revenue generally fluctuates less rapidly than corporate income taxes and can be more or less volatile than the personal income depending on the nature of the business cycle. It does not capture spending on services well, which tends to be less volatile than spending on goods taxed under the sales tax. Over the past decade or so, some state tax analysts have expressed concern that as states have removed more stable elements of consumption such as groceries and clothing from their bases, their sales taxes were more subject to plunge as consumers became nervous about spending on optional and big-ticket items. The sales tax generally maintained slow growth in the latest economic downturn, but grew rapidly and remained steady as general economic conditions improved. Sales tax revenue has been weak in each of the last five quarters.

although perhaps partially masked by payments with 2007 tax returns. After June, tax revenue is likely to be extremely weak as most states begin their fiscal years — and such weakness may linger as the year progresses. Many states finalized their 2008-09 budgets during the April-June quarter, when conditions may have misled forecasters into revenue projections that were too rosy. Governors in some states may, then, face difficulty implementing their new budgets — raising the prospect of midyear cuts and other actions to eliminate emerging gaps.

## Endnotes

- 1 Lucy Dadayan and Robert B. Ward, *State Tax Revenue Weakens Still Further, While Costs Rise Sharply*, State Revenue Report 71, March 2008.
- 2 New Mexico is excluded due to lack of data.
- 3 Most newspaper accounts of economic data show growth from one quarter or month to the next, rather than year over year. That is because most economic time series have been adjusted to remove seasonality so that comparisons from one period to the next are meaningful. Government tax data, by contrast, rarely are adjusted to remove seasonal variations and as a result analysts usually examine these time series on a year-over-year basis, thereby comparing data for this year to the same season or period last year and implicitly removing some of the seasonal effects. To make our analysis of economic data comparable to our analysis of tax data, for most purposes in this report we examine economic data on a year-over-year basis.
- 4 Unlike leading indexes, these measure are not designed to predict where the economy is headed; rather, they are intended to tell us where we are now. For a technical discussion of these indexes and their national counterpart, see Crone, Theodore M., and Alan Clayton-Matthews. “Consistent Economic Indexes for the 50 States,” *Review of Economics and Statistics*, 87 (2005), pp. 593-603; Crone, Theodore M. “What a New Set of Indexes Tells Us About State and National Business Cycles,” *Business Review*, Federal Reserve Bank of Philadelphia (First Quarter 2006); and Stock, James H., and Mark W. Watson. “New Indexes of Coincident and Leading Economic Indicators,” *NBER Macroeconomics Annual* (1989), pp. 351-94. The data and several papers are available at [www.philadelphiafed.org/econ/indexes/coincident](http://www.philadelphiafed.org/econ/indexes/coincident).
- 5 The data underlying these indexes are subject to revision, and so tentative conclusions drawn now could change at a later date.
- 6 The median state change generally will not be the same as the national change because it gives every state equal importance — in this measure, California is no more important than Wyoming.
- 7 See Donald J. Boyd, *What Will Happen to State Government Finances in a Recession?*, Nelson A. Rockefeller Institute of Government, January 30, 2008.

- 8 Rockefeller Institute analysis of data from the National Conference of State Legislatures.
- 9 See “5/5/2008 — April Collections of \$2.737 Billion Exceed Benchmark” and “6/3/08 — May Collections Total \$1.494 Billion,” press releases from the Massachusetts Department of Revenue.
- 10 See monthly reports of tax receipts from the Kentucky Office of the State Budget Director (<http://osbd.ky.gov/publications/taxreceipts.htm>).
- 11 See <http://www.ntax.dor.ga.gov/whatsnew.aspx> for Georgia and [http://www.revenue.state.pa.us/revenue/lib/revenue/2008\\_05\\_mrr.PDF](http://www.revenue.state.pa.us/revenue/lib/revenue/2008_05_mrr.PDF) for Pennsylvania.
- 12 Boyd, January 30, 2008.

**State Taxes Slow Yet Again, and Further Weakening Appears Likely**

	2007				2008			
	Personal Income	Corporate Income	Sales	Total	Personal Income	Corporate Income	Sales	Total
<b>United States</b>	<b>61,287</b>	<b>10,497</b>	<b>55,031</b>	<b>152,732</b>	<b>64,007</b>	<b>9,966</b>	<b>55,009</b>	<b>155,301</b>
<b>New England</b>	<b>4,519</b>	<b>930</b>	<b>2,445</b>	<b>9,971</b>	<b>4,979</b>	<b>845</b>	<b>2,423</b>	<b>10,498</b>
Connecticut	1,509	187	907	3,153	1,612	158	905	3,213
Maine	227	34	234	633	238	37	235	651
Massachusetts	2,460	533	1,006	4,808	2,821	496	992	5,267
New Hampshire	NA	85	NA	419	NA	65	NA	442
Rhode Island	225	70	209	629	197	72	198	590
Vermont	98	22	89	330	111	18	93	335
<b>Mid-Atlantic</b>	<b>18,379</b>	<b>2,384</b>	<b>7,414</b>	<b>34,443</b>	<b>19,320</b>	<b>2,769</b>	<b>7,590</b>	<b>35,689</b>
Delaware	248	19	NA	593	239	21	NA	595
Maryland	1,642	196	852	2,805	1,691	227	924	2,978
New Jersey	2,912	415	2,001	6,428	2,920	443	2,022	6,410
New York	11,066	1,217	2,467	16,555	11,709	1,434	2,571	17,416
Pennsylvania	2,510	536	2,094	8,062	2,760	643	2,073	8,290
<b>Great Lakes</b>	<b>7,952</b>	<b>1,831</b>	<b>7,734</b>	<b>20,047</b>	<b>8,612</b>	<b>1,655</b>	<b>7,775</b>	<b>20,559</b>
Illinois	2,795	448	1,689	5,801	2,941	550	1,691	6,009
Indiana	1,001	87	1,355	2,880	1,056	38	1,399	2,928
Michigan	1,104	384	1,905	3,745	1,254	320	1,891	3,825
Ohio	1,783	648	1,802	4,737	1,870	549	1,811	4,680
Wisconsin	1,269	264	983	2,884	1,491	199	983	3,117
<b>Plains</b>	<b>5,129</b>	<b>639</b>	<b>3,460</b>	<b>10,543</b>	<b>5,478</b>	<b>601</b>	<b>3,471</b>	<b>10,940</b>
Iowa	795	82	468	1,415	876	106	492	1,576
Kansas	542	44	508	1,197	590	65	501	1,267
Minnesota	1,946	340	1,122	3,805	2,063	244	1,122	3,848
Missouri	1,420	84	749	2,786	1,548	84	727	2,852
Nebraska	330	57	341	784	304	63	346	769
North Dakota	96	32	125	342	97	39	128	411
South Dakota	NA	NA	147	214	NA	NA	156	215
<b>Southeast</b>	<b>9,833</b>	<b>2,125</b>	<b>14,883</b>	<b>33,106</b>	<b>9,992</b>	<b>1,882</b>	<b>14,363</b>	<b>32,320</b>
Alabama	843	89	565	2,192	880	110	555	2,244
Arkansas	626	78	556	1,344	700	62	537	1,382
Florida	NA	492	4,991	6,494	NA	448	4,690	5,824
Georgia	1,890	229	1,583	4,114	1,796	203	1,535	3,958
Kentucky	633	121	792	2,173	701	38	811	2,200
Louisiana	673	79	703	1,932	703	53	723	1,950
Mississippi	242	167	786	1,583	163	224	789	1,567
North Carolina	2,163	370	1,195	4,727	2,214	200	1,146	4,585
South Carolina	393	82	643	1,319	319	69	594	1,212
Tennessee	NA	253	1,722	2,632	NA	228	1,711	2,648
Virginia	2,065	119	1,054	3,712	2,157	139	979	3,740
West Virginia	305	47	295	885	358	108	293	1,010
<b>Southwest</b>	<b>1,212</b>	<b>332</b>	<b>7,345</b>	<b>13,377</b>	<b>1,037</b>	<b>144</b>	<b>7,705</b>	<b>13,432</b>
Arizona	735	137	1,153	2,143	581	68	1,099	1,852
New Mexico	ND	ND	ND	ND	ND	ND	ND	ND
Oklahoma	477	195	454	1,448	457	76	485	1,365
Texas	NA	NA	5,738	9,786	NA	NA	6,121	10,215
<b>Rocky Mountain</b>	<b>1,823</b>	<b>162</b>	<b>1,481</b>	<b>4,110</b>	<b>1,784</b>	<b>134</b>	<b>1,455</b>	<b>4,025</b>
Colorado	1,003	47	583	1,655	1,015	55	579	1,671
Idaho	280	24	314	807	244	23	308	799
Montana	167	19	NA	405	158	11	NA	361
Utah	372	72	466	1,066	368	44	444	1,006
Wyoming	NA	NA	118	177	NA	NA	123	188
<b>Far West</b>	<b>12,442</b>	<b>2,095</b>	<b>10,270</b>	<b>27,135</b>	<b>12,804</b>	<b>1,936</b>	<b>10,229</b>	<b>27,839</b>
Alaska	NA	49	NA	380	NA	24	NA	958
California	10,995	1,991	6,893	20,351	11,275	1,834	6,831	20,379
Hawaii	341	9	662	1,116	336	15	678	1,139
Nevada	NA	NA	779	1,002	NA	NA	732	953
Oregon	1,105	46	NA	1,243	1,193	63	NA	1,361
Washington	NA	NA	1,936	3,042	NA	NA	1,987	3,049

Source: Individual state data, analysis by Rockefeller Institute. See page 11 for notes.

### Technical Notes

This report is based on information collected from state officials, most often in state revenue departments, but in some cases from state budget offices and legislative staff. This is the latest in a series of such reports published by the Rockefeller Institute's Fiscal Studies Program (formerly the Center for the Study of the States). The Institute developed this State Revenue Report series as a service for users who sought more current data than those available from the Census Bureau. The Bureau has improved the timeliness of its statistics on state and local tax revenues; readers may wish to consult [www.census.gov](http://www.census.gov) for data that complement the information in this report.

In most states, revenue reported is for the general fund only, but in several states a broader measure of revenue is used. The most important category of excluded revenues in many states is motor fuel taxes. Taxes on health-care providers to fund Medicaid programs are excluded as well.

*California:* Nongeneral fund revenue from a sales tax increase dedicated to local governments is included.

*Michigan:* The Single Business Tax, a type of value-added tax, is treated here as a corporate income tax.

Several caveats are important. First, tax collections during a period as brief as three months are subject to influences that may make their interpretation difficult. For example, a single payment from a large corporation can have a significant effect on corporate tax revenues.

Second, estimates of tax adjustments are imprecise. Typically the adjustments reflect tax legislation; however, they occasionally reflect other atypical changes in revenue. Unfortunately, we cannot speak with every state in every quarter. We discuss tax legislation carefully with the states that have the largest changes, but for states with smaller changes we rely upon our analysis of published sources and upon our earlier conversations with estimators.

Third, revenue estimators cannot predict the quarter-by-quarter impact of certain legislated changes with any confidence. This is true of almost all corporate tax changes, which generally are reflected in highly volatile quarterly estimated tax payments; to a lesser extent it is true of personal income tax changes that are not implemented through withholding.

Finally, many other noneconomic factors affect year-over-year tax revenue growth: changes in payment patterns, large refunds or audits, and administrative changes frequently have significant impacts on tax revenue. It is not possible for us to adjust for all of these factors.

**State Taxes Slow Yet Again, and Further Weakening Appears Likely**

**Table 11**  
**State Tax Revenue, July-March, FY 2007 and FY 2008 (\$ in millions)**

	FY 2007				FY 2008			
	Personal Income	Corporate Income	Sales	Total	Personal Income	Corporate Income	Sales	Total
<b>United States</b>	<b>173,792</b>	<b>32,241</b>	<b>163,399</b>	<b>442,184</b>	<b>182,380</b>	<b>29,750</b>	<b>166,259</b>	<b>455,418</b>
<b>New England</b>	<b>12,728</b>	<b>2,149</b>	<b>6,868</b>	<b>27,090</b>	<b>13,857</b>	<b>1,956</b>	<b>7,004</b>	<b>28,321</b>
Connecticut	3,523	471	2,211	7,533	3,874	339	2,330	7,876
Maine	780	107	688	1,991	818	115	695	2,027
Massachusetts	7,338	1,188	3,053	13,571	8,065	1,113	3,075	14,399
New Hampshire	NA	233	NA	1,203	NA	240	NA	1,245
Rhode Island	729	102	662	1,733	707	98	642	1,675
Vermont	358	49	255	1,058	393	51	262	1,100
<b>Mid-Atlantic</b>	<b>43,111</b>	<b>7,276</b>	<b>21,530</b>	<b>86,090</b>	<b>45,969</b>	<b>7,266</b>	<b>22,187</b>	<b>89,605</b>
Delaware	714	70	NA	1,598	704	63	NA	1,628
Maryland	4,096	520	2,232	7,375	4,309	452	2,357	7,706
New Jersey	6,636	1,575	5,268	15,713	7,043	1,802	5,516	16,541
New York	24,911	3,511	7,668	41,394	26,682	3,343	7,952	43,322
Pennsylvania	6,754	1,600	6,363	20,011	7,231	1,605	6,361	20,408
<b>Great Lakes</b>	<b>24,428</b>	<b>4,421</b>	<b>23,569</b>	<b>61,535</b>	<b>25,884</b>	<b>4,053</b>	<b>24,169</b>	<b>63,349</b>
Illinois	6,989	1,268	5,401	16,113	7,472	1,325	5,435	16,702
Indiana	3,002	513	4,003	8,653	3,130	452	4,150	8,916
Michigan	4,483	1,236	5,895	14,539	4,921	1,176	6,076	15,130
Ohio	5,801	705	5,516	13,433	5,964	495	5,701	13,493
Wisconsin	4,153	698	2,755	8,798	4,398	606	2,807	9,109
<b>Plains</b>	<b>14,036</b>	<b>2,054</b>	<b>10,262</b>	<b>30,508</b>	<b>15,066</b>	<b>1,952</b>	<b>10,415</b>	<b>31,841</b>
Iowa	2,102	274	1,421	4,034	2,304	317	1,496	4,459
Kansas	1,678	254	1,541	3,799	1,832	256	1,489	3,930
Minnesota	5,188	968	3,353	10,995	5,492	774	3,384	11,157
Missouri	3,751	308	2,158	7,706	4,066	313	2,175	8,005
Nebraska	1,099	150	977	2,387	1,140	168	990	2,458
North Dakota	218	100	363	958	233	124	399	1,156
South Dakota	NA	NA	449	628	NA	NA	483	675
<b>Southeast</b>	<b>31,781</b>	<b>7,000</b>	<b>43,403</b>	<b>100,021</b>	<b>33,265</b>	<b>6,122</b>	<b>42,866</b>	<b>99,725</b>
Alabama	2,307	360	1,698	6,157	2,417	376	1,704	6,351
Arkansas	1,687	252	1,668	3,840	1,854	254	1,624	3,979
Florida	NA	1,650	14,474	18,964	NA	1,509	13,795	17,329
Georgia	6,075	610	4,335	12,403	6,228	643	4,336	12,596
Kentucky	2,131	639	2,400	6,851	2,322	310	2,462	6,891
Louisiana	2,049	408	2,098	5,981	2,189	392	2,162	6,223
Mississippi	952	345	2,240	4,606	796	370	2,226	4,514
North Carolina	6,893	1,086	3,733	14,543	7,257	728	3,762	14,615
South Carolina	2,235	205	1,696	4,607	2,265	196	1,631	4,546
Tennessee	NA	646	5,063	7,637	NA	567	5,161	7,790
Virginia	6,547	562	3,128	11,703	6,892	472	3,131	11,938
West Virginia	905	237	869	2,729	1,046	305	872	2,954
<b>Southwest</b>	<b>4,912</b>	<b>1,221</b>	<b>22,834</b>	<b>41,087</b>	<b>4,626</b>	<b>882</b>	<b>24,155</b>	<b>44,013</b>
Arizona	2,522	628	3,381	6,843	2,353	482	3,327	6,461
New Mexico /1	621	208	937	2,174	600	178	948	2,160
Oklahoma	1,769	385	1,385	4,418	1,673	222	1,487	4,359
Texas	NA	NA	17,131	27,652	NA	NA	18,392	31,033
<b>Rocky Mountain</b>	<b>5,923</b>	<b>723</b>	<b>4,264</b>	<b>12,478</b>	<b>6,295</b>	<b>706</b>	<b>4,424</b>	<b>13,078</b>
Colorado	3,030	253	1,656	5,012	3,245	294	1,756	5,366
Idaho	838	104	931	2,284	863	100	1,013	2,433
Montana	497	107	NA	1,039	543	84	NA	1,101
Utah	1,558	260	1,375	3,661	1,644	227	1,333	3,676
Wyoming	NA	NA	302	482	NA	NA	322	502
<b>Far West</b>	<b>36,873</b>	<b>7,398</b>	<b>30,668</b>	<b>83,376</b>	<b>37,343</b>	<b>6,814</b>	<b>31,040</b>	<b>85,412</b>
Alaska	NA	141	NA	1,450	NA	100	NA	3,260
California	32,067	6,989	20,461	61,324	33,404	6,399	20,507	62,084
Hawaii	1,072	39	1,894	3,290	1,086	43	1,978	3,410
Nevada	NA	NA	2,407	3,097	NA	NA	2,310	2,970
Oregon	3,735	228	NA	4,249	2,853	273	NA	3,429
Washington	NA	NA	5,907	9,965	NA	NA	6,245	10,259

Source: Individual state data, analysis by Rockefeller Institute. See page 11 for notes.  
 1/ Indicates data through December 2007 only.

## Appendix: Census Bureau Data on State and Local Tax Revenue

The Rockefeller Institute has for many years collected its own state tax revenue data from the 50 states, in part because quarterly data collected by the Census Bureau ([www.census.gov/govs/www/qtax.html](http://www.census.gov/govs/www/qtax.html)) were not sufficiently timely. This has been changing in recent years, and the Census Bureau data now are far more timely than before. This creates an opportunity for the Institute to enhance our longstanding reports on state tax revenues in ways that we believe will lead to improved reporting and analysis of state and local finance.

In this Appendix, we begin to report on the Census Bureau's data, and their relative strengths and weaknesses. We expect that the Census data will form the backbone of our next full quarterly report, and that we will supplement Census statistics with data we collect to fill selected gaps and to provide occasional early "flash" reports. Our use of the Census data will evolve over time.

### Relative Strengths of the Two Main Sources of Quarterly Tax Data

The Census Bureau data are collected via a survey of the 50 states plus selected local governments, providing data on state government taxes for each of the 50 states plus the District of Columbia, and estimates of national totals for local government taxes (not by state). The data also hold the promise of providing quarterly estimates for individual local governments in the Census Bureau's sample, potentially allowing us to track and report on how a sample of local governments are affected by economic trends such as the recent housing bust. In addition, the Census data form a longer time series than the Rockefeller Institute's data, allowing for additional analysis of how state and local government tax revenue has responded to past recessions.

The Census data are based on a more comprehensive universe of taxes than the convenience sample used by the Institute (which was designed to facilitate fast and easy reporting by states), and captured approximately 15 percent more revenue than the Institute's survey in the latest quarter. They also provide detail on some of the smaller

taxes not lined out in the Institute's survey, such as motor fuel taxes and tobacco taxes. Although these taxes are relatively small, they can be of special interest to some audiences at some times — for example, motor fuel taxes, which often are dedicated for highway purposes, have fallen on a year-over-year basis in six of the last seven quarters due in part to higher gas prices and resulting softness in fuel sales. Tobacco taxes, which are used in some states to secure tobacco settlement bonds, also can be of great interest, particularly in the wake of large tax increases in some states that were intended, in part, to depress tobacco consumption. We may prepare separate analyses of individual smaller taxes from time to time.

The main drawbacks of the Census data are that (1) they are not quite as timely as the Institute's tax data, and (2) initial data reported by the Census Bureau sometimes include estimates for entire states or for individual taxes in selected states, and these estimates must be used with care (in subsequent releases the Census Bureau revises its data, generally replacing estimates with reported values from states). We plan to address these issues in two ways. First, given the widespread availability of data on the Internet, we expect to issue occasional "flash" reports between our regular quarterly reports if interesting trends emerge. These reports generally would be available several weeks sooner than the full quarterly report. Second, we will make adjustments to Census data or to our descriptions of the data when necessary, to take account of any significant estimates incorporated in the data.

In the most recent quarter, the Census data show the same broad patterns as the Institute's data, as Tables A-1 and A-2 below show.

**Table A-1 Census and Institute Data Followed Broadly Similar Patterns By Tax Type**

Growth in State Tax Collections, By Tax Type 2008 January-March Quarter versus Year Ago		
Tax Type	Census	RIG
PIT	3.2%	4.4%
CIT	-2.5%	-5.1%
Sales	0.0%	0.0%
<b>All Taxes</b>	<b>1.4%</b>	<b>1.7%</b>



**Table A-2 Census And Institute Data Followed Broadly Similar Patterns By Region**

<b>Growth in State Tax Collections, By Region</b> 2008 January-March Quarter versus Year Ago		
<b>Region</b>	<b>Census</b>	<b>RIG</b>
New England	5.7%	5.3%
Mid-Atlantic	2.6%	3.6%
Great Lakes	2.6%	2.6%
Plains	4.2%	3.8%
Southeast	-2.4%	-2.4%
Southwest	1.2%	0.4%
Rocky Mountain	-1.2%	-2.1%
Far West	1.6%	2.6%
<b>United States Total</b>	<b>1.4%</b>	<b>1.7%</b>

### Insights From the Most Recent Census Bureau Tax Data

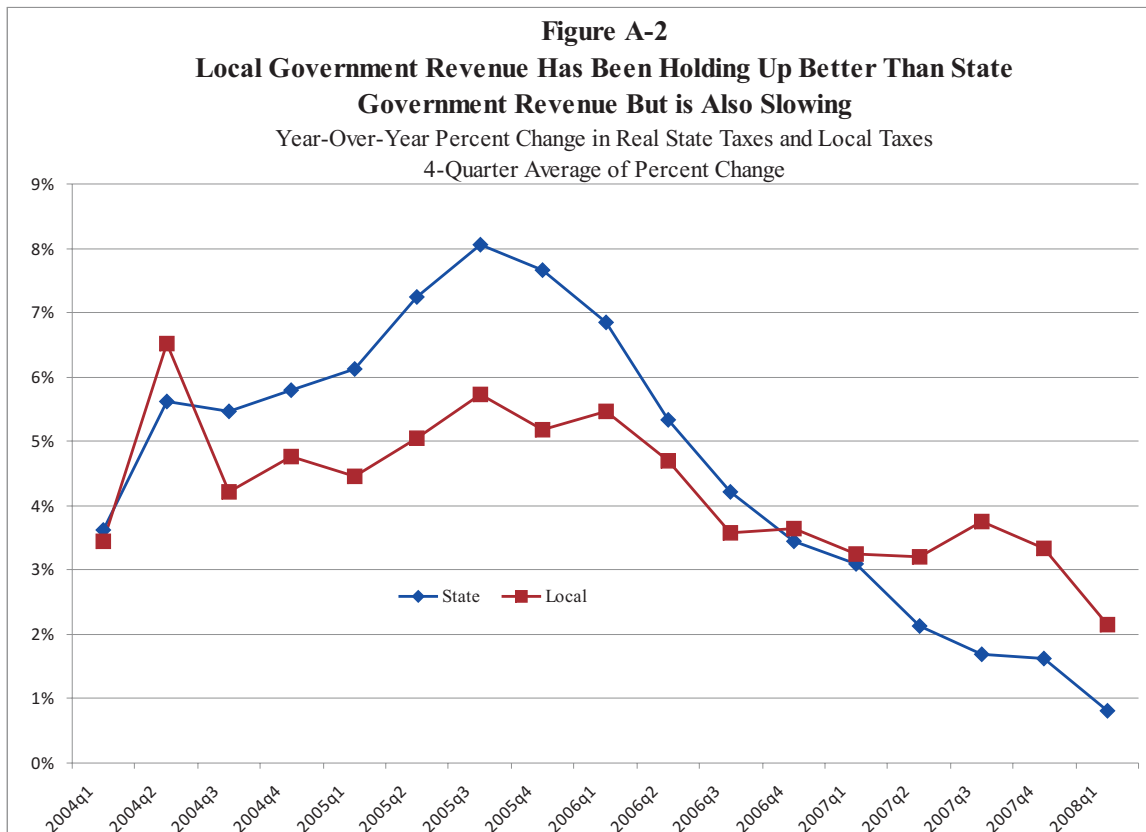
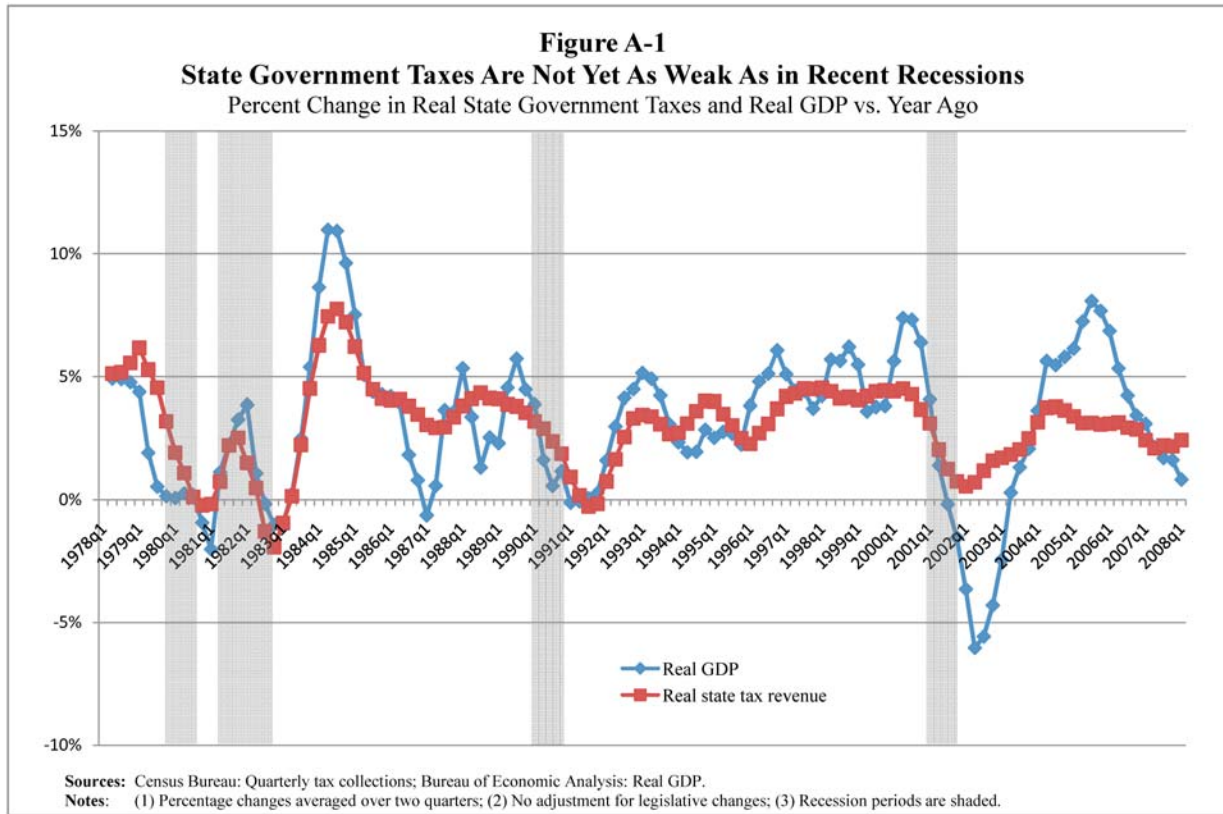
Because the Census Bureau data are available for a long time period, we can examine how state government taxes have fared over several recessions. The following figures look at 4-quarter averages to make some of the longer-term trends easier to see.<sup>1</sup> As Figure A-1 shows, while state tax revenue were extremely weak in real terms in the January-March quarter, taxes were far weaker in each of the last four recessions. This does not mean that the current economy will not be bad for states —

but it does mean that things have not yet become as bad for states as they were in recent recessions.

Because the Census Bureau data include estimates of national totals for local governments, we can see how state and local governments are faring relative to each other. As Figure A-2 shows, local revenue has been weakening also, but is not yet as weak as state tax revenue and has not slowed as sharply.

### Endnote

- 1 The data in the figures in this section are not directly comparable to those elsewhere in this report. First, in this section we adjust the Census Bureau data for inflation using the gross domestic product price index rather than the price index for state and local government consumption expenditures and gross investment, and so the inflation-adjusted numbers below are not directly comparable to those used elsewhere in this report. There are pros and cons to either approach, and we will discuss them fully in the next quarterly report. Second, the percentage changes are shown on a moving-average basis and incorporate information from more than one quarter. Third, as noted in the main text, the Census Bureau definition of total taxes is more comprehensive than the Institute's version. Nonetheless, the two data sources do show broadly similar patterns.



### **About The Nelson A. Rockefeller Institute of Government's Fiscal Studies Program**

The Nelson A. Rockefeller Institute of Government, the public policy research arm of the State University of New York, was established in 1982 to bring the resources of the 64-campus SUNY system to bear on public policy issues. The Institute is active nationally in research and special projects on the role of state governments in American federalism and the management and finances of both state and local governments in major areas of domestic public affairs.

The Institute's Fiscal Studies Program, originally called the Center for the Study of the States, was established in May 1990 in response to the growing importance of state governments in the American federal system. Despite the ever-growing role of the states, there is a dearth of high-quality, practical, independent research about state and local programs and finances.

The mission of the Fiscal Studies Program is to help fill this important gap. The Program conducts research on trends affecting all 50 states and serves as a national resource for public officials, the media, public affairs experts, researchers, and others.

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