State of Wisconsin

Notice of Material Information

Dated January 31, 1997

Some bonds listed in this notice are not subject to the requirements of SEC Rule 15c2-12(b)(5) regarding an agreement to provide continuing disclosure.

Issuer:	State of Wisconsin
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Material Information:	The following document contains new information about revenue collections and projections of financial position for the State of Wisconsin.

- A letter dated January 23, 1997 from the Director of the Legislative Fiscal Bureau to the Joint Committee on Finance of the Wisconsin Legislature containing general fund expenditure and revenue projections for the Legislature as it begins to consider the state's budget and other legislation.

This document provides information which may be material to financial evaluation of the State of Wisconsin, however neither the preparation nor submission of this document constitutes a Listed Material Event pursuant to the State's Master Agreement on Continuing Disclosure.

The undersigned represents that he is the Capital Finance Director, State of Wisconsin Capital Finance Office, which is the office of the State of Wisconsin responsible for providing Annual Reports and giving notice of Listed Material Events when notice is required by the State's Master Agreement on Continuing Disclosure.

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[Legislative Fiscal Bureau Letter Head]

January 23, 1997

Representative Scott Jensen, Assembly Chair
Senator Brian Burke, Senate Chair
Joint Committee on Finance
119 Martin Luther King Blvd.
Madison, WI 53703

Dear Representative Jensen and Senator Burke:

Annually, this office prepares general fund expenditure and revenue projections for the Legislature as it begins to consider the state's budget and other legislation.

In the odd-numbered years, the report includes estimated tax collections and expenditures for the current fiscal year and revenue projections for each year of the next biennium. The purpose of this report is to present the conclusions of our analysis.

Comparison with the Administration's November 20, 1996, Report

On November 20, 1996, the Departments of Administration and Revenue submitted a report to the Governor and Legislature that identified revenue projections for 1996-97 and the 1997-99 biennium. Our analysis indicates that for that three-year period, the state's general fund will realize $150.3 million more than is reflected in the November 20 report. The $150.3 million consists of $62.4 million in 1996-97, $41.1 million in 1997-98 and $46.8 million in 1998-99.

Prior to addressing the reasons fo r this difference, it is important to note the nature of the November 20 document. The DOA report is required, by statute, to be submitted at that time to inform the Governor of the magnitude of agency budget requests and a projection of tax collections. Given its timing in the 1996-97 fiscal year, sufficient data is not available to reestimate certain revenues and expenditures for the current fiscal year. Thus, these numbers were not reestimated by DOA in their report. This is consistent with previous November 20 reports.

1996-97 General Fund Condition Statement

Based upon our analysis, we believe that the gross balance in the state's general fund will be $146.7 million on June 30, 1997. After consideration of the required statutory balance ($92.0 million), the net balance will be $54.7 million. This is shown in Table 1.

The Administration's November 20 report contained a 1996-97 general fund condition statement that showed a gross balance of $84.3 million.

Thus, the projected gross balance of this report ($146.7 million) is $62.4 million greater than that shown in the November 20 report.

The primary reason for the increase in the balance is due to strength in tax collections for the first six months of the current fiscal year. Specifically, our analysis shows that tax collections for 1996-97 will exceed those of the November 20 report by $57.9 million. The remaining difference ($4.5 million) is due to a variety of changes in revenues and expenditures which net to the $4.5 million figure. Most of the increase is due to the individual income tax ($35 million) and the sales tax ($15 million).

TABLE 1

Estimated 1996-97 General Fund Condition Statement

	1996-97
Revenues	
Opening Balance, July 1	$587,689,800
Taxes	8,688,500,000
Less Federal Retirees' Refunds	-13,100,000
Departmental Revenues	150,409,000
Total Available	$9,413,498,800
Appropriations, Transfers and Reserves	
Gross Appropriations	$9,153,611,400
Compensation Reserves	46,382,400
Transfers to:	
Local Government Property Insurance Fund	2,322,600
Property Tax Relief Fund	257,755,900
Less: Lapses and Sum Sufficient Reestimates	-193,300,300
Net	$9,266,772,000
Balances	
Gross Balance	$146,726,800
Less: Required Statutory Balance	-91,999,900
Net Balance, June 30	$54,726,900

Table 1 indicates that the general fund will show a gross balance of $146.7 million at the end of the current fiscal year. This amount will be carried forward as the opening balance of the next biennium. In addition, as shown in Table 1, $257.8 million will be transferred from the general fund to the property tax relief in 1996-97. The property tax relief fund was established in 1995 Act 213 as a reserve to fund property tax relief programs in the 1997-99 biennium. Therefore, the general fund will begin the next biennium with $404.5 million ($146.7 million gross balance of 1996-97 plus $257.8 million from the property tax relief fund).

General Fund Tax Revenues

The following sections provide information regarding general fund tax revenues for 1996-97 and the 1997-99 biennium, beginning with a review of the economy in 1996. This is followed by a discussion of the national economic forecast for 1997 through 1999 and detailed general fund tax revenue projections for the current fiscal year and the next biennium.

Review of the Economy in 1996

Last January, our office prepared general fund revenue estimates for the 1995-97 biennium based on the January, 1996, interim forecast of the U.S. economy by DRI/McGraw-Hill. Under the forecast, economic growth was projected to slow in early 1996 due to reduced consumer spending and the effects of severe winter storms and the shutdown of the federal government. The slowdown in consumer spending was expected to cause an unintended accumulation of inventories which, in turn, would lead to lower growth in industrial production in the first half of 1996. However, the forecast anticipated federal funds rate cuts by the Federal Reserve in the spring of 1996. This stimulus, along with a rebound in consumer spending, was expected to contribute to moderate economic growth in the second half of 1996 and in 1997. Real (inflation-adjusted) gross domestic product (GDP) was projected to grow by 2.1% in 1996 and by 2.7% in 1997, while nominal (current dollar) GDP was expected to increase by 4.2% in 1996 and 4.5% in 1997.

Economic growth in 1996 appears to have been somewhat higher than these projections. Real GDP increased by an estimated 2.3%, or 0.2% more than anticipated. Similarly, nominal GDP grew at an estimated 4.4%, or 0.2% more than the forecast. Inflation, as measured by the Consumer Price Index (CPI), was 2.9% in 1996. Although consumer confidence remained high during the year, spending has moderated. The national unemployment rate was 5.4% in November. However, the widening of the trade deficit was the primary drag on the economy in 1996. According to DRI/McGraw-Hill, the increase in the real trade deficit subtracted 0.7% from real GDP growth.

National Economic Forecast

The revenue estimates prepared by this office are based on the January, 1997, forecast of the economy by DRI/McGraw-Hill. The following is a brief description of the basic elements of the forecast.

The economy is in a period of minicycles that average out to relatively steady annual growth, modest inflation and unemployment with minimal action by the Federal Reserve. There are no apparent serious excesses that are ready to push the economy into recession, but it is also not likely that stronger, long-run economic growth could occur without higher inflation. Gross domestic product is forecast to increase by slightly more than 2% through mid-1997, which will cause the unemployment rate to edge up. Growth should begin to pick up in the second half of 1997. Modest increases in consumer spending and business purchases of equipment along with increased exports should contribute to economic growth. The annual increase in real GDP is forecast to be 2.3% for 1996 through 1998. GDP will grow by 2.1% in 1999. Nominal GDP is estimated to increase by 4.4% in 1996 and 1997 and by 4.6% in 1998 and 1999.

The Federal Reserve is expected to attempt to maintain the current levels of inflation and unemployment by following the tactic of raising interest rates slightly when the economy appears too strong and by reducing rates slightly when the economy appears sluggish. The interest rate adjustments are likely to be small and infrequent until it becomes clear whether inflation or recession is a greater threat to the economy. The forecast assumes that the Federal Reserve will favor a somewhat more restrictive monetary policy and will nudge up the federal funds rate in the Spring of 1997. However, if inflation remains low and consumers spend less than expected, no action will be necessary. If the Federal Reserve raises interest rates in 1997 it probably will be able to reduce them in 1998.

Consumer spending has been a primary source of growth during the current ec onomic expansion but consumers appear to have become more cautious. After rising for four years, the ratio of consumer debt to income stabilized in the last half of 1996. The growth in both real and nominal personal consumption expenditures is projected to decline from 1996 through the first half of 1997. While spending has slowed, consumer confidence has remained high. The University of Michigan Index of Consumer Sentiment remained at the high level of 96.9 in December, even after dropping 2.3 points. This level of consumer optimism makes it unlikely that consumer spending will be significantly reduced, but some caution will persist. As a result, consumer spending will continue to increase, but only in line with income gains. The annual rate of growth in disposable personal income is projected to be 5.3% in 1997, 5% in 1998 and 4.7% in 1999. Personal consumption expenditures are forecast to increase 5% in 1997, 5.1% in 1998 and 4.9% in 1999. The annual saving rate will remain near 5% during this period.

After strong growth during the past few years, business investment is slowing. Real nonresidential fixed investment increased 9.5% in 1995 and 7.1% in 1996; real equipment outlays increased 10.4% in 1995 and 8.3% in 1996. Business investment grew to 10.6% of GDP in the third quarter of 1996 and is projected to remain near 10.5% for the next few years. At this level, capital stocks are growing at a faster rate than is needed to maintain a constant capital-to-output ratio. Consequently, reduced levels of growth are forecast for real business investment. The annual increase in real nonresidential fixed investment is estimated to be 5.3% in 1997 and to decline to 4.8% in 1998 and 3.5% in 1999. Similarly, real equipment spending will increase by about 6.5% in 1997 and 1998 and 4.4% in 1999. Purchases of computers and communication equipment are expected to make a significant contribution to overall business investment. Construction spending is forecast to be relatively stable between 1997 and 1999.

Imbalance in foreign trade was a significant drag on the economy in 1996. The combination of the strong dollar and substantial domestic demand for imports caused historically high deficits in the merchandise trade and current account balances. Net trade is forecast to be a drag on the economy in 1997, but not as much as in 1996. Beginning in the second half of 1997, both nominal and real exports will grow at a faster rate than imports, and that trend is projected to continue through 1999. However, the faster rate of export growth will not reduce the merchandise trade deficit, which will increase from $195 billion in 1996 to $242.1 billion in 1999, when the balance is projected to stabilize at $240 to $250 billion for the following few years.

TABLE 2

Summary of National Economic Indicators
Data Resources, Inc.
January, 1997
($ in Billions)

	1996	1997	1998	1999
Nominal Gross Domestic Product	$7,571.5	$7,904.5	$8,267.7	$8,647.5
Percent Change	4.4%	4.4%	4.6%	4.6%
Real Gross Domestic Product	$6,900.8	$7,058.8	$7,224.4	$7,377.0
Percent Change	2.3%	2.3%	2.3%	2.1%
Consumer Price Index	2.9%	2.8%	2.8%	2.9%
Personal Income	$6,449.8	$6,772.8	$7,094.6	$7,426.9
Percent Change	5.5%	5.0%	4.8%	4.7%
Personal Consumption Expend.	$5,151.8	$5,406.9	$5,684.5	$5,964.0
Percent Change	4.6%	5.0%	5.1%	4.9%
Corporate Profits Before Tax	$638.2	$635.7	$668.8	$700.9
Percent Change	6.6%	-0.4%	5.2%	4.8%
Unemployment Rate	5.4%	5.5%	5.5%	5.6%

Inflation is projected to remain modest throughout the forecast period. Overall CPI inflation is forecast to be 2.8% in 1997 and 1998 and 2.9% in 1999. The producer price index will decline from 2.6% in 1996 to 1.3% in 1998 as food and energy price inflation decreases. Producer price inflation is then forecast to increase to 1.8% in 1999. Wage inflation has increased over the past few years, but it has been offset by low fringe benefit cost increases. Fringe benefit costs have been primarily restrained by businesses switching from traditional fee-for-service health care plans to managed care. Since this is generally a one-time savings, fringe benefit costs are expected to accelerate over the next few years. However, increases in productivity are expected to hold down unit labor costs.

The modest annual growth that is forecast is expected to keep the unemployment rate around 5.5% between 1997 and 1999. However, the anticipated action by the Federal Reserve to increase interest rates will cause a slight upward trend in the unemployment rate over the next five years. The unemployment rate is expected to be 5.5% in 1997 and 1998 and 5.6% in 1999.

Table 2 shows the projected values for several economic indicators which underlie our general fund tax revenue estimates for 1996-97 and the 1997-99 biennium.

The primary risk to the forecast is that the economy would expand a little too rapidly before the Federal Reserve increased interest rates. The unemployment rate would remain too low too long, resulting in higher wages and prices. Then the Federal Reserve would be forced to raise interest rates aggressively to control inflation. The result would be a recession in 1999. Alternatively, consumer caution could turn into retrenchment if consumer confidence is shaken by a stock market correction or other external event and the worry over high debt levels increases. This could lead to recession in 1997.

General Fund Tax Projections

Revenue estimates for all sources of state general fund taxes for 1996-97 and for the 1997-99 biennium are shown in Table 3. The estimates are higher than the November 20 projections by the Department of Revenue by $57.9 million in 1996-97, $41.1 million in 1997-98 and $46.8 million in 1998-99. These increases reflect strong monthly tax collections and a slight improvement in the DRI/McGraw-Hill forecast for the latter part of the biennium, since DOR prepared its projections in November.

TABLE 3

Projected General Fund Tax Collections
($ in Millions)

	1995-97 Biennium		1997-99 Biennium	
Source of Tax Revenue	1995-96 Actual	1996-97 Estimated	1997-98 Estimated	1998-99 Estimated
Individual Income*	$4,183.6	$4,465.0	$4,740.0	$5,010.0
General Sales and Use**	2,704.2	2,860.0	3,005.0	3,155.0
Corporate Income & Franchise***	636.0	640.0	637.0	655.0
Public Utility	285.3	295.6	273.7	269.6
Excise				
Cigarettes	198.0	198.0	196.0	194.0
Liquor and Wine	30.8	30.8	30.5	30.5
Beer	9.2	9.0	9.0	9.0
Tobacco Products	7.4	8.4	9.0	9.5
Insurance Company	92.3	92.5	93.0	93.5
Estate	45.6	44.0	45.0	45.0
Miscellaneous Taxes	43.2	45.2	47.2	48.3
TOTAL	$8,235.6	$8,688.5	$9,085.4	$9,519.4
Increase Over Prior Year		$452.9	$396.9	$434.0
Percent Increase		5.5%	4.6%	4.8%

*Individual income tax amounts for 1995-96 and 1996-97 are before deduction of federal retirees' refunds. No refunds will be paid in the 1997-99 biennium.
**Sales tax estimates assume a refund of $10 million in 1997-98 and 1998-99 for the ruling in the Manpower case.
***Corporate income and franchise tax estimates in 1997-98 and 1998-99 are net of refunds totalling $9 million and $10.1 million, respectively, to reflect settlement of the NCR case.

These estimates include adjustments which reflect the recent settlement of two court cases and the conversion of all telephone companies from gross revenues taxation to ad valorem taxation. Specifically, corporate income and franchise tax estimates have been reduced by $9 million in 1997-98 and by $10.1 million in 1998-99 to account for settlement of the NCR Corporation v. Wisconsin Department of Revenue case. In addition, sales tax revenues have been reduced by $10 million in 1997-98 and 1998-99 to account for a recent court decision regarding the taxation of computer software (Wisconsin Department of Revenue v. Manpower International, Inc.). Finally, the annual decreases between 1996-97 and 1998-99 in the utility tax revenue estimates reflect the change in the method of taxing telephone companies from gross revenues taxation to ad valorem taxation, beginning in 1998, as required under current law.

A brief summary of the projected growth and impact of national economic conditions on the major general fund tax sources follows.

Individual Income Tax. Individual income tax receipts are estimated to total $4,465.0 million in 1996-97, which represents a 6.7% increase over 1995-96 collections. Through the end of December, 1996, total income tax collections were $1,783.0 million, or 7.4% higher than collections were at the same time last year. However, the Department of Revenue indicates that this amount is understated by approximately $39 million due to processing delays. If these revenues are added to the December total, year-to-date collections increase to $1,822.4 million, which is 9.8% higher than last year. In addition, withholding payments were 8.1% higher and declaration payments were 22.3% higher than the year-to-date totals for 1995-96.

For the 1997-99 biennium, individual income tax collections are estimated to be $4,740 million in 1997-98 and $5,010 million in 1998-99, an increase of 6.2% and 5.7% over prior year estimates, respectively. National personal income is forecast to increase by 5.0% in 1997, 4.8% in 1998 and 4.7% in 1999. Because of the marginal rate structure of the income tax, collections typically increase faster than personal income.

Federal Retiree Pension Refunds. Under a settlement between the state and certain federal retirees, taxes paid on federal pension income received from 1984 through 1988 were refunded in six installment payments from calendar years 1994 through 1996. These refund payments are shown in the general fund condition statement as a decrease to general fund revenues in 1996-97, outside the amounts shown in Table 3. The last payment of $13.1 million was made in November, 1996.

General Sales and Use Tax. Sales tax revenues totalled $2,704.2 million in 1995-96 and are estimated at $2,860 million in 1996-97, $3,005 million in 1997-98 and $3,155 million in 1998-99. These projections, which are based on past experience and forecast growth in personal consumption expenditures, represent growth rates of 5.8% in 1996-97, 5.1% in 1997-98 and 5.0% in 1998-99.

Through December, 1996, sales tax collections were $1,126.5 million, which is a decline of 0.2% from the same period in 1995-96. However, due to a delay in processing tax payments, the Department of Revenue indicates that this figure is understated by approximately $75 million, which will be included in the collection amount for January, 1997. If an adjustment is made to account for this factor, year-to-date collections total $1,201.2 million, which is 6.5% greater than last year. With anticipated slower growth in personal consumption, sales tax revenues are expected to increase by 5.3% over the remainder of the 1996-97 fiscal year.

Also, as noted, the sales tax estimates for 1997-98 and 1998-99 are re duced by $10 million to account for potential refunds associated with an August, 1996, State Court of Appeals decision relating to the taxation of computer software (Wisconsin Department of Revenue v. Manpower International, Inc.). If these refunds were not included in the sales tax estimates, projected growth would be 5.4% in 1997-98 and 5.0% in 1998-99. At this time, the Department does not have a precise estimate of these refunds or a payment schedule; however, it is likely that payments will be made in the 1997-99 biennium.

Corporate Income and Franchise Tax. Corporate income and franchise taxes are projected to increase slightly (0.6%) from $636 million in 1995-96 to $640 million in 1996-97. Corporate income and franchise tax revenues are estimated to decrease minimally (0.5%) in 1997-98 to $637 million and then to increase 2.8% to $655 million in 1998-99.

Estimated 1996-97 revenues reflect modest growth in collections over the past few years. Corporate income and franchise tax revenues were $631.8 million in 1994-95 and $636 million in 1995-96. Monthly declaration payments and net collections continue that modest growth trend. Also, corporate profits continued to increase during the first three quarters of 1996.

The estimated decrease in corporate income and franchise tax revenues in 1997-98, in part, reflects an anticipated slowdown in economic growth in the first half of 1997. In addition, labor costs are expected to increase and excess industrial capacity will make it difficult for corporations to increase prices. However, due to cost-cutting activities over the past several years, businesses are in a relatively sound financial position. This should allow most corporations to be resilient in times of weaker demand. As economic growth picks up in late 1997, profits are projected to rebound, but at a lower growth rate. As a result, corporate income and franchise tax collections are estimated to increase in 1998-99.

The corporate income and franchise tax revenue estimates for the 1997-9 9 biennium are also adjusted to reflect refunds of an estimated $9 million in 1997-98 and $10.1 million in 1998-99 as a result of settlement of the NCR v. Wisconsin Department of Revenue case in September, 1996. Under the settlement, DOR will refund taxes paid on certain dividends received from subsidiary corporations. Total taxes and interest of $38.4 million will be refunded in four installments from September, 1997, through September, 2000. The Circuit Court of Dane County had ruled that these dividends should have been deductible in computing Wisconsin corporate income and franchise tax liability.

Public Utility Taxes. Public utility taxes are estimated to be $295.6 million in 1996-97, $273.7 million in 1997-98 and $269.6 million in 1998-99. This represents an increase of 3.6% in 1996-97 and decreases of 7.4% in 1997-98 and 1.5% in 1998-99.

The decreases in utility tax revenues in 1997-98 and 1998-99 are attributable to the conversion of telecommunications companies from a gross receipts tax to ad valorem taxation beginning with taxes due for 1998; the ad valorem tax is expected to generate less revenue than is collected from the gross receipts tax. A transition fee is imposed on cellular phone companies and local exchange companies, equal to the difference between taxes due under the gross receipts tax and ad valorem tax, which delays the full effect of converting telephone companies until fiscal year 2000-01. However, because resellers and interexchange companies will no longer be paying the gross receipts tax beginning in 1997-98, a decrease in revenues is expected in that year.

Utility tax collections from telecommunications companies totaled $160.1 million in 1995-96 and are estimated at $169.8 million in 1996-97, $146.6 million in 1997-98 and $138.8 million in 1998-99. These estimates represent an increase of 6.1% in 1996-97 and decreases of 13.7% in 1997-98 and 5.3% in 1998-99. Because tax revenues from telecommunications companies make up over half of total utility tax revenues, this pattern of revenue growth and decline is reflected in total utility tax estimates.

Excise Taxes. Excise taxes on cigarettes, tobacco products and alcoholic beverages are projected to total $246.2 million in 1996-97, $244.5 million in 1997-98 and $243.0 million in 1998-99. These estimates reflect minor decreases in collections over time. Cigarette tax collections are expected to decrease by approximately 1% each year while revenues from the tax on tobacco products, which is calculated as a percent of price, are expected to increase each year. The taxes on alcoholic beverages are estimated to remain constant.

Insurance Premiums Tax. Insurance premiums taxes decreased from $94.4 million in 1994-95 to $92.3 million in 1995-96. Premiums taxes are projected to be $92.5 million in 1996-97, $93 million in 1997-98 and $93.5 million in 1998-99. These estimates of minimal growth reflect year-to-date premiums tax collections and industry forecasts. Monthly collections have shown little growth over the previous year. In addition, insurance industry forecasts expect property and causality and life insurance company premiums growth to be sluggish at best.

Estate Tax. The estate tax is projected to generate $44.0 million in 1996-97 and $45.0 million in 1997-98 and 1998-99. These estimates are based on historical levels and estate tax collections to date.

Miscellaneous Taxes. Miscellaneous taxes are estimated to be $45.2 million in 1996-97, $47.2 million in 1997-98 and $48.3 million in 1998-99. The primary component of miscellaneous taxes is the real estate transfer fee, which is expected to show moderate growth in response to projected modest increases in interest rates. Pari-mutuel taxes are estimated to be $2.7 million in each year.

We will continue to monitor national economic forecasts and tax collection data and keep you informed of any further modifications which may be required.

Sincerely,

/s/Robert Wm Lang

Robert Wm. Lang
Director

cc: Members, Wisconsin Legislature