

**MINUTES OF THE MEETING OF THE  
STATE OF NEVADA ECONOMIC FORUM  
November 2, 2004**

The meeting of the State of Nevada Economic Forum (created by Senate Bill 23, 1993) was scheduled for 9:00 a.m. on Tuesday, November 2, 2004, at the Legislative Building, 401 South Carson Street, Room 3138, Carson City, Nevada with videoconference to the Grant Sawyer State Office Building, 555 East Washington Avenue, Room 4412 Las Vegas, Nevada.

**ECONOMIC FORUM MEMBERS PRESENT:**

Michael Small, Chairman  
Deborah Pierce, Vice Chairman  
Cary Fisher  
Leo Seevers  
William Martin

**STAFF:**

Mark Stevens, Assembly Fiscal Analyst, Fiscal Analysis Division  
Gary Ghiggeri, Senate Fiscal Analyst, Fiscal Analysis Division  
Russell Guindon, Deputy Fiscal Analyst, Fiscal Analysis Division  
Bill Anderson, Economist, Executive Budget Office  
Keith Norberg, Deputy Fiscal Analyst, Fiscal Analysis Division  
Donna Thomas, Secretary, Fiscal Analysis Division

**EXHIBITS:**

- Exhibit A - Meeting Notice and Agenda
- Exhibit B - Attendance Record
- Exhibit C - Meeting Packet
- Exhibit D - The U.S. and Nevada Economic Outlook, 2004 - 2007, PowerPoint presentation used by James Diffley, Global Insight
- Exhibit E - Fiscal Analysis Division Forecast Information for the Major General Fund Revenues
- Exhibit F - Nevada Economy in Brief and Nevada's Top 100 Demand Occupations provided by the Nevada Department of Employment, Training and Rehabilitation
- Exhibit G - Nevada 2004 Economic Overview and Outlook provided by Robert Murdock, Nevada Department of Employment, Training and Rehabilitation
- Exhibit H - Gaming Control Board – Gaming Revenue Forecasts – 2005-2007
- Exhibit I - Department of Administration – Budget and Planning Division – General Fund Revenue Forecasts – October 2004
- Exhibit J - Department of Taxation – Major Tax Projections Memorandum dated November 1, 2004
- Exhibit K - Fiscal Analysis Division - Growth in Statewide Taxable Sales

**EXHIBITS MAY BE REVIEWED AT THE RESEARCH LIBRARY OF THE LEGISLATIVE COUNSEL BUREAU, CARSON CITY, NEVADA, UPON REQUEST.**

**I. Roll Call**

Chairman Small called the meeting of the State of Nevada Economic Forum to order at 9:00 a.m. The Secretary called the roll; all members were present.

**II. Approval of the September 29, 2004 Meeting Minutes**

Chairman Small asked for a motion to approve the September 29, 2004, meeting minutes. Russell Guindon, Deputy Fiscal Analyst, Fiscal Analysis Division noted that in the haste to get the minutes together for the packet, there were a few substantive corrections that needed to be made to the minutes. He noted on page 14 of the meeting packet, (Exhibit C), the figure \$333.8 million should be \$333,800. Also, on page 17, the figure in the first paragraph should be 0.9% instead of 9%. Mr. Guindon stated the changes were made to the final minutes for approval. He stated that some minor non-substantive

corrections were made to the minutes.

Mr. Martin commented on a statement he made at the September 29, 2004 meeting, page 15 of the meeting packet, where he questioned if the Economic Forum had the power to reverse any taxes. He asked that the record reflect that he fully understood the power of the Forum and was not trying to circumvent the Legislature. He made that comment in jest in reference to the bank tax and he would be more restrained with his humor in the future

**MR. SEEVERS MOVED TO APPROVE THE SEPTEMBER 29, 2004 MINUTES AS AMENDED.**

**MR. MARTIN SECONDED THE MOTION, WHICH CARRIED UNANIMOUSLY.**

### **III. Presentation on the National, Regional and State Economic Outlook**

James Diffley, Director, U.S. Regional Services Group, Global Insight said he would present the U.S. economic outlook, the state economic outlook and discuss the two large tax revenue sources that he projected for the Forum. Copies of the color slides used during Mr. Diffley's PowerPoint presentation were provided to the members (Exhibit D).

Mr. Diffley commented that 2004 started with a lot of promise for the U.S. economy and Gross Domestic Product (GDP) growth had been strong but the country was stuck in what

many called a "jobless recovery" and 2004 was the year the country was predicted to see significant employment growth. He noted there was significant employment growth the first four months of 2004. However, while employment continued to grow throughout the entire year, it had not grown as fast as hoped and there was a "fall back" in terms of the strength of the outlook. The problem with a lack of growth in employment was that in the business cycle recovery, the consumer sector had been the strongest part of the economy. Mr. Diffley stated that business investments had lagged and business spending had crashed in part because of the collapse of the high-tech sector which put the economy into a recession. He said Nevada recovered from the recession largely due to the strong housing market and strong consumer spending; particularly in car sales. Mr. Diffley said that consumer spending could not last forever and they knew employment growth had to eventually come and buttress the consumer spending or consumers would not continue to spend at that rate. In the spring of 2004, the slowdown in employment came because the job market did not expand as hoped and because of oil prices which directly impacted consumer budgets and their ability to spend on other goods due to the cost of driving resulting from gasoline prices. Also, he noted the home heating oil season coming to the colder parts of the country would cause a drag moving forward.

Mr. Diffley stated business spending had been strong and looking at the table on page 2, (Exhibit D), first quarter GDP growth was 4.5%, slowing to 3.3% in the second quarter. Growth in consumption in the second quarter slowed dramatically from 4.1% to 1.6%; however, business investment finally spiked up to double-digit rates. He stated there was a drag in the foreign sector primarily because the U.S. economy had been stronger than other economies and the U.S. was importing more than exporting because the demand was lacking from the rest of the world. He noted that after he prepared the slides, the Bureau of Economic Analysis released the initial estimate of the third quarter GDP numbers and the numbers were short of the consensus. The consensus forecast for the third quarter was up approximately 4.5% and Global Insight's forecast for the third quarter GDP was 4.2%; actual was 3.7%.

Mr. Diffley noted that consumption spending was up 4.6% and it was projected at 4.7%. He stated that the 4.7% growth in consumption spending was unsustainable and the savings rate in the third quarter was at its lowest rate in the post-war period and the state could not continue to rely on consumer spending. The third quarter numbers showed less momentum in final sales and final demand from consumers, businesses, government and foreign sector than what was thought. Furthermore, the oil price outlook was getting worse, not better. He said it was projected that the world price of oil would remain above \$50 a barrel through the first quarter of 2005. Mr. Diffley said a turnaround in the rundown in inventories of automobile manufactures was largely responsible for GDP looking strong in the third quarter, but is projected to be negative in the fourth quarter. He said they were looking at more of a slowdown in the fourth quarter than the projected increase of 3.4% in the current forecast. Currently, Global Insight was revising the forecast and would soon have the new forecast of the U.S. economy based on the most recent data. Moving forward, the 3.4% growth in GDP in the fourth quarter and the 3.5% growth in the first quarter were roughly the rate of sustainable growth in the U.S. economy given the productivity and labor force and other factors.

Continuing, Mr. Diffley said that Nevada was especially interested in the world-wide outlook because of the importance of Asian tourism in particular. On the comprehensive graph of the world economy, page 3 of his presentation; the world, excluding the U.S, was only up to 4% in 2004 after lagging U.S. growth for much of the last two years which caused

deterioration in the balance of payments. Japan finally had a good year in 2004 with a little weaker growth going forward. Also, he noted that emerging Europe was doing well and finally catching up.

Mr. Diffley continued with the oil outlook and said oil prices were a leading indicator of consumer spending. He said the index of consumer sentiment was produced by two different groups; Conference Board Index and the University of Michigan Sentiment Index. The declines in 2001 and 2002 were due to the 9-11 recession and there was a sharp increase in consumer sentiment through 2003; however, in 2004 the tide turned and went negative. Oil prices were above \$50 per barrel and should remain there. In 2005, oil prices were expected to average \$46 a barrel: higher than the \$41 per barrel expected for 2005 and it would cost the nation about 0.2% in GDP growth. Mr. Diffley said that oil was not as important as it used to be, and the graph on page 5 of his presentation measured the value of oil imports. He said in the late 1970's into 1980, between 2% and 3% of GDP was a good measure of the importance of oil and the drain that high oil prices at that time caused to the U.S. economy. The 1980's and 1990's were much more benign. The current situation was still less than 1.5% of GDP. In a crisis scenario, if oil prices shot up to \$60 a barrel, this scenario would only push the percent of GDP up to 2.2%, still less than it was at the peaks in the 1970's and 1980's. He said it was expected that oil prices in 2006 would fall below \$36 per barrel.

Mr. Diffley moved on to page 6 of his presentation and said the oil market had been tighter than thought and the demand from China on world oil markets was important. He said the impacts to the U.S. economy for every \$10 price increase in oil were:

- U.S. GDP was lowered by 0.4% in the first year and 0.3% in the second year.
- Prices in the U.S. were 0.7% higher in the first year and 0.3% in the second year.
- Some lost exports and slower world growth leading to lower exports which would further impact the GDP.

The industry effects were:

- Automobile, airlines and other transportation which affected Nevada tourism.
- Utility costs.
- Chemical industry.
- Heavy manufacturing industry.

Continuing, Mr. Diffley said the forecast summary, in an annual rate going forward and subject to a slight revision in the GDP number for the third quarter, real GDP growth slowed from the 4.4% in 2004, came in above the 4% rate posted in 2003; slowed to 3.4% in 2005 which was a more sustainable rate; 2.9% in FY 2006 and 3.2% in FY 2007. The Consumer Price Index (CPI) inflation was benign and the most recent GDP release gave further evidence that core inflation was less than 2%. He believed with the federal funds rate already low, the federal government would raise interest rates in December 2004, but in the current environment, with growth slowing and the oil prices and employment not moving up as thought, that would be the last increase in interest rates for some time. Previously, forecasters thought that the federal government would ratchet rates up in December and a few more times in 2005. The federal funds rate would move up slowly, by 2007, to 3.5% rate. The oil price in 2005 will be revised from \$41 per barrel to \$46 per barrel, up from the average and similar amount in 2004. He reiterated that oil prices were forecasted to be at or below \$36 per barrel in FY 2006.

Mr. Diffley stated that housing starts were at a tremendous peak with almost 2 million units per year being sold. He said 2004 rates were expected to be at the rate of 2003 and then slowing to 1.7% by 2007.

The unemployment rate would stabilize and one of the reasons the unemployment rate would not go down as dramatically as thought when payroll jobs increased, was because people had dropped out of the labor force and then re-entered the labor force, so both labor force and jobs were increasing at the same time.

Concluding, Mr. Diffley said the U.S. economy growth had downshifted and the huge final domestic demand surge ended in the first quarter. The remainder of 2004 was slower and 3.4% growth in 2005 was capacity growth of what was expected long-term. Inflation, due to oil prices, imports and reduced auto sales slowed GDP substantially in the second quarter. Jobs finally surged in 2004 then backed off some although a positive scenario for job growth was still anticipated in the United States. Mr. Diffley said final demand overall was still strong with travel and transportation. He noted that non-residential construction was the last piece of the puzzle that had been very weak with high office vacancies across the country. However, that was expected to turn around in 2005 in addition to new sources of growth. GDP was 3.7% growth for the remaining months of 2004.

Mr. Diffley stated that oil prices were rising causing a risk to the economy, but he did not think it was a substantial risk. He

indicated that the import drain was also a risk factor for the economy. Job growth was faltering and is not at a level fast enough to get the nation back on track in terms of the labor market. Also, he noted there was the "geopolitical" uncertainty surrounding Iraq and North Korea. He added that concerns were occurring regarding home prices in significant areas of the United States being over-valued which could result in a negative collapse in home prices causing a further pull-back in consumer spending. Mr. Diffley stated that although it was a risk, there was only a couple areas in the country where that was a likely possibility. Another risk to the economy was the major dollar decline which had been falling and was relatively low, but there was an enormous budget deficit and trade imbalance and a risk of flight from the dollar resulting in a much lower dollar value. Coupled with that, was an interest rate shock of 8% on long term rates which would reduce investments in the United States.

Regarding the graph on page 2, (Exhibit D), Mr. Martin noted Mr. Diffley said the business fixed investment went up to double-digit percentage, 14.4% in the fourth quarter and asked if it was correct that he was projecting a 1.7% growth in the following quarter. Mr. Diffley explained that a bonus depreciation allowance that expired at the end of 2004 caused a surge in business investment to be started in 2004 and the timing would result in a let down in the first quarter of 2005. He said it was not a structural problem with demands, just a timing issue to meet tax requirements.

Mr. SeEVERS questioned the forecast summary numbers (page 7 of the handout) that showed the federal funds rate at 3.5% and the CPI inflation at 1.7%; indicating those percentages seemed counterintuitive. Responding, Mr. Diffley said it would be counterintuitive if the economy was not growing by 2006 and 2007. The 3.5% brought the Federal Reserve Bank back to a more neutral policy where it was not acting to stimulate the economy. He said it could stimulate the economy, but the counterintuitive part that Mr. SeEVERS mentioned was if inflation was that low, there was plenty of lead way for the federal government to keep rates low. However, the assumption in the chart was that the economy would be growing at a capacity rate, a full employment rate, so the feds did not need to stimulate the economy.

Ms. Pierce asked for clarification from Mr. Diffley and wondered if Nevada was one of the states he was referring to when he mentioned home prices were over-valued in certain parts of the country. Mr. Diffley replied that Southern California and New York metro were the two areas he was referring to when he mentioned the over-valued home prices.

Mr. Fisher interjected that he recently read that the business fixed investment was already dropping off. Mr. Diffley replied that it was still double-digit in the most recent release. He said there were some monthly numbers that showed a cooling and the Purchasing Managers' Index recently showed some slowing; but it was still at double-digit rates.

Mr. Fisher commented that he had heard the previous oil administer for Saudi Arabia said that United States projections for Saudi production for the next five to ten years was highly optimistic, unrealistic and he believed that it was true for other producers all over the world. Mr. Diffley responded that the market was very tight and Saudi Arabia indicated in early 2004 they wanted to increase production to lower the price of oil, but was simply not able to have as much of an effect. He said there was a concern over that tightness and Iraq would help the issues in Venezuela. In addition, another scare in 2004 was the Soviet Union situation with political ramifications between the ownership of oil companies and the government.

Mr. Fisher asked Mr. Diffley if he was using the administration numbers or did he generate his own numbers when forecasting? Mr. Diffley replied that Global Insight had their own numbers and he was not using administration numbers.

Moving forward to the Nevada Overview, Mr. Diffley said that Nevada was number one in all states for employment growth and had 4.6% employment growth year-over-year through the most recent month report. As of September, the unemployment rate dipped under 4%; a gradual decline from being above 5% previously. He said that all sectors were advancing; construction advanced by approximately 12,000 jobs (11.5%) over the past twelve months. Professional and business services had approximately 9,000 (7.2%) new job growth. Leisure and hospitality had over 7,000 new jobs and all the travel sectors across the country were finally back to healthy levels after the disruption caused during 2001. Also, gold mining was growing after a number of years of decline.

Mr. Diffley noted that through the second quarter of 2004, personal income had approximately 9% year-over-year growth. Gross state product had doubled since 1994 and now exceeded \$90 billion.

Moving to page 10 of his presentation, Mr. Diffley stated that the forecast summary for Nevada averaged 4.3% employment growth for 2004 then slowed in 2005 to 3.8% and just under 3% in 2006 and 2007 after the construction cycle eased off. However, employment growth still remained number one in the country by a substantial amount.

Income growth was over 8% in 2004, projected to be over 7% in 2005 and near 7% in 2006 and 2007. Housing starts were also extremely robust in Nevada as they had been in the nation and will slow down, but still remained above 40,000 units in

their estimations of multi-family units in Las Vegas with a gradual slowing to 45,000 units in 2005 and 42,000 units in 2006 and 41,000 units in 2007.

Nevada job growth, relative to the United States, was under zero percent from the middle of 2001, before 9-11, and did not turn positive until the beginning of 2004, although Nevada had a shorter spell of negative job growth than the rest of the country. He noted the gap between Nevada and the United States will be approximately 2% in the longer-term forecast to year 2007.

Referring to page 13 of his presentation, Mr. Diffley said the map showed an overview of the average annual employment growth in the United States forecasted for five years. Nevada was one of the states leading in employment growth and he believed California would be one of the strongest states, above the average for the United States. Employment growth in Southern California had been exceptional and counter-balanced the bubble burst in San Jose and Silicon Valley during the downturn. Mr. Diffley said the Southern California defense industry was strong with the United States defense expanding trade with China which was a tremendous boom for Southern California with all the shipping coming through to the rest of the United States. Housing prices were out-of-sight in California and that state also had the best commercial real estate investment opportunities in the country.

Mr. Diffley said the jobless recovery was over and questioned when states would return to the level of jobs seen at the beginning of the downturn in early 2001. Nevada and the states shaded in red on the map, page 14 of his presentation, (Exhibit D), had already regained their jobs lost last year but many would not see the job levels they had in 2000 until the end of the decade. He said the state of Maryland had done tremendously well as far as federal government spending, defense spending and health care research and development.

Mr. Diffley said Nevada was among the top states in personal income growth as was California income; an important determinant for Nevada demand. He said that migration was a long-term driver of labor force growth in the states and also the long-term indicator of what states were attractive. He added that Nevada attracted approximately 60,000 new residents in 2003, but Florida led the states in migration. He noted that California had led in migration of foreign immigrants and now was not as attractive, in fact was losing migrants to areas like Nevada. Also, he noted that Maryland made the top ten states this year for migration due to the strength of their economy. Mr. Diffley said he believed that Nevada would continue to lead the country in the short-term outlook with substantial employment and income growth.

Concluding, Mr. Diffley said he also provided two tax revenue sources in his forecast to the Forum; gaming fees and sales tax. He said there was a 21% increase in gaming revenues in FY 2004. Factoring out the tax hike in Nevada and the surge in fee adjustments that occurred month-to-month in 2004, the state gaming fees were up 7.4% for 2004. He said there was strong growth and it was an indication of recovery in the gaming markets in Nevada. He said if the adjustments had not been made, his forecast for 2005 would be +3.8%. Nevada was coming off a very strong 2004, so ratcheting down in the growth rate should not be interpreted as a sign of weakness, rather a sign of continued strength and the state was not giving back revenues from the peak. He said that 3.8% growth was the unadjusted level and the actual number forecasted showed a slight decline of -0.7% entirely due to the \$34 million fee adjustment that was added in FY 2004. Moving forward to FY 2006, 3.6% was forecasted in underlying growth in gaming fees and 2.7% in FY 2007.

Mr. Diffley said he used an econometric model of gaming fees which included hotel rooms and took into account the 2005 opening of the Wynn property. Other explanatory variables used were Nevada employment levels and overall U.S. forecast of spending on amusement and recreation. California income and California/Oregon casinos were also used as a variable when forecasting the gaming fees. He noted the major risks, long-term versus short-term, was that California had two referendum regarding tribal gaming casinos that were important to California but ultimately important to Nevada. The California market was potentially enormous and Nevada benefited from California residents coming to the state to gamble and Nevada needed to be wary of the development of the tribal casinos in California. He added that another risk to Nevada gaming was internet gambling which had the potential to siphon off some of the existing business in Nevada.

Turning to the sales tax forecast, page 19 of his presentation, (Exhibit D), Mr. Diffley indicated that sales tax had a strong base in FY 2004 largely due to construction and auto sales which generated revenue of approximately 14% in FY 2004. He said Global Insight's forecast showed a slowing for the out-years at a smooth rate of 5.4% in FY 2005; 5.3% in FY 2006 and 5.2% in FY 2007. It was a reasonably strong growth particularly off the high base so it was not a sign of weakening. He said the explanatory variables were Nevada employment, construction employment which drives business-to-business spending and the level of consumer prices. Also, Global Insight took into account the swing in auto sales with a small downward swing after the strong 2003 and 2004.

Chairman Small asked Mr. Diffley to comment on the California referendum he referred to when discussing the gaming fee

risks and how it would impact Nevada.

Mr. Diffley replied that the plan by the Governor of California would allow a substantial expansion in slot machines at five tribes with which he signed compacts. The tradeoff would be an increase in revenues to the state of California from the tribes and it would be effectively a revenue tax on the revenues from the slots. He said there would be a substantial increase in slots if the Governor's proposal passed. He noted it was a contentious issue because other tribes were against the referendum but if passed it would open a tremendous amount of slot activity in California.

Chairman Small asked Mr. Diffley to expand on the \$34 million adjustment for the gaming fees.

Responding, Mr. Diffley explained that there were collection numbers each month and then there were adjustments to those collections slotted to those months based on previous revenues that had now been accounted for. The fact it was \$34 million for the fiscal year as a whole, meant that they were not revenues that actually came in during that fiscal year but had come in earlier. Chairman Small asked if it had to do with the three month prepayment. Mr. Guindon interjected that it was the three month prepayment and he referred to the Fiscal Analysis Division's packet, page 5, (Exhibit E), which showed the estimated fee adjustment and the \$34.2 million that the EFA was in FY 2004 and the net effect of that in FY 2004 was almost a \$40 million impact. He stated that all the agencies were trying to make the same adjustment in their forecasts and it was not a repeatable thing and the adjustment had to be done to the FY 2005 forecast for that effect. He pointed out the Global Insight forecast was on page 87 of the meeting packet (Exhibit C).

Chairman Small asked Mr. Diffley if he expected Nevada inflation rates to approximate the inflation rates from the United States. Mr. Diffley said inflation rates did not vary much across the states. He said the current forecast for 2005 for Nevada was 2.1% in 2005 and 1.5% in 2006 which was similar to the United States. He said the major difference was the rates of home prices and appreciation across the states.

## **VI. Presentation on the State Employment Outlook**

Robert Murdock, Chief, Research and Analysis Division, Department of Employment, Training and Rehabilitation (DETR) stated that he would make a presentation on the Nevada labor market, work force information and an overview of what DETR anticipated to occur over the next few years. He referred to a handout that was given to the Forum members for their review, Nevada Economy in Brief and Nevada's Top 100 Demand Occupations, (Exhibit F). Also, he noted that copies of the color slides used during his presentation were provided to the members (Exhibit G).

Mr. Murdock explained that the labor force was counted by the county where the worker lived, a measure of people 16 years and older and the unemployment rate. Employment was counted by the county where the workplace was located. He noted there was a difference in the labor force numbers and the employment numbers for a county for industrial employment. Mr. Murdock said since the last time he made a presentation, DETR changed the way they classified industries. Previously DETR used the Standard Industry Classification (SIC) and currently used The North American Industry Classification System (NAICS). He said with the new system, DETR had a better way of looking at the economy and the service sector and it downplayed some of the manufacturing regime used in the 1930's when the first system was designed.

Mr. Murdock referred to page 4 of his handout, (Exhibit G) and pointed out the major industry groups under the old SIC and the new groups under the NAICS. He noted that in many instances they were the same; however, mining had changed to natural resources and mining and trade was combined with transportation and utilities. He said there was an information sector that was new and the professional & business services, education and health services and leisure & hospitality had expanded out of other services. He reiterated that the chart showed the differences and how DETR looked at the economy.

Continuing, Mr. Murdock said the goods producing industry in the NAICS system were goods that produced a tangible product which was basically natural resources, construction and manufacturing. The service producing industries were growth industries that offered specialized skills entertainment, finance, etc. Mr. Murdock said that Nevada had two metropolitan statistical areas (MSA) which was the major areas in the state: Las Vegas and Reno. He noted that Carson City was now designated as a metropolitan statistical area and would be coming on-line in January 2005. The labor market area (LMA) was economically integrated areas within commuting distance and included Carson City (soon to be an MSA) and Elko. Mr. Murdock said the roughly eight of ten jobs and eight out of ten people lived in Las Vegas MSA. The Mohave County in Arizona was part of Las Vegas MSA but would be removed in January 2005 leaving just Clark and Nye County in the Las Vegas MSA.

Looking at Nevada's economy compared to the rest of the nation, page 9 of his presentation, (Exhibit G), Mr. Murdock noted that Nevada had extremely strong job growth and had exceeded the U.S. and California's economy every year since 1984 and Nevada had not lost jobs annually since 1982. Compared to unemployment rates, California was much higher than Nevada and the national numbers. Nevada oscillates up and below the national rate but currently Nevada was significantly below the national rate. On page 9 of his presentation, Nevada had a spike in unemployment in 2002 due to 9-11 but since the spring of 2002 unemployment was improving and continued to improve.

Moving to job growth, Mr. Murdock said job growth had rebounded since 2002 and continued to be strong in all areas of the state. The structure of employment nationally showed a fairly disaggregated economy and was diversified around the NAICS coded industries. Nevada's largest employment was in the leisure and hospitality sector; the manufacturing, trade and government sector was smaller. Looking at Las Vegas employment, the leisure and hospitality sector was the largest MSA employment and construction was higher than the rest of the state. Reno's employment makeup had less government, slightly more trade and construction was somewhat higher. He said that Reno had a more diversified economy and jobs were spread around through different industries than the Las Vegas market.

Turning to page 16 of his presentation, Mr. Murdock said the chart showed Nevada's unemployment rate in 2002 was 6.8% as the state was coming out of the recession. Unemployment dropped down in 2003 to 4.7%, 4.3% estimated for 2004 and there was a slight increase projected for the outlying years of 2005, 2006 and 2007. He said the numbers were somewhat of an increase but still remained below the national numbers by a significant amount.

Industrial employment growth on page 17 of his presentation showed Nevada maintained a positive growth atmosphere of 2,615 jobs in 2002. Industrial employment jumped in 2003 to 35,165 jobs as the state entered into a recovery period and 48,679 jobs in 2004. Looking to the outlying years, there should be a continued strong gain with the projects coming on-line and the growth in Las Vegas where eight out of ten jobs were being formed. Mr. Murdock said DETR does not see a let down in the employment gains and the state will be approaching 50,000 new jobs in 2007.

Mr. Murdock continued and said that natural resources were slightly down in 2003 and employment growth and construction was the driving force of the economy in 2003. The housing starts in Nevada were phenomenal in 2003 and even though it was unsustainable, a tremendous influx of people moving to the state continued. A slowdown in telecommunications also continued due to the downsizing and professional services were off. Moving to 2004, Mr. Murdock said there was a different outlook in the employment and the industries that were moving into the state. Construction was still strong and professional business services and educational and health services had turned around. Also, the hotel and gaming industry were much stronger in 2004.

Moving to employment growth in 2005, all industries were looking even stronger and the growth was not so segmented. Mr. Murdock noted that the telecommunications and information technology sector was the only industry not forecasted to come back in 2005 but again construction, leisure and hospitality were very strong. Looking at employment growth in 2006 and 2007, a broader advance in the industries was forecasted and there was continued strength in most sectors with the exception of information technology. The leisure sector was strong due to the properties that were anticipated to open. He said the natural resources sector; mainly mining was showing strong growth after being very weak for many years when the gold prices were depressed. With the new properties coming on-line and the start of new mines, slight growth was anticipated and a slight increase in those jobs was currently occurring. The information and technology sector would finally shake out in 2006 and 2007.

Concluding, Mr. Murdock said that Nevada did not have any reason for pessimism in the economy at this point, but there was no control over the external shocks like terrorism or the oil situation that would affect the economy.

Mr. Fisher pointed out that based on the historical data and projections; it appeared the state would have net job loss in information technology for five years in a row. Mr. Murdock responded the loss was gradual and as telecommunications changed, fewer people were required. He said the total industry has lost approximately 15,600 jobs and on a monthly basis the industry lost 100 jobs in October 2004.

Ms. Pierce said comparing 2005, 2006 and 2007 a buildup of growth in the education health services was seen and by 2007 it was over 5% growth. She questioned whether the growth was mainly in the health services sector and what caused the growth in this area. Mr. Murdock replied that the public school systems were classified in education services rather than government. He noted there was a strong growth in education services to meet the demand in Nevada with 50,000 people coming into the labor market and the total population gains was a tremendous load on the school systems. He said that both education and health was causing the growth and as more people moved into the state, health services and out-patient types of health services were becoming more popular.

Ms. Pierce said she was wondering if Nevada had become more of an aging population with many retired people moving from California and if so, did that influence the projections? Mr. Murdock responded that he did not believe it had an influence on the projections and many of the individuals moving to the state were relatively young.

Chairman Small asked what considerations DETR had with respect to companies moving into Nevada, what were the trends, and how had it affected the projections?

Mr. Murdock said that DETR assigned a business code to new businesses moving into the state and they looked at the number of people the business employed and were able to track the numbers over the years to come up with the projections. He said that DETR conducted industry and occupational projections and looked at growth rates for the next two to ten years and were able to give a detailed picture, by industry, of where the new businesses were coming from. In addition, DETR looked at historical trends, what they could see happening and models were built per industry. Also, occupational information was collected from the businesses and added to the industry projections and the information was applied to the occupational information DETR received every six months and then they were able to project the growth factors. In addition, the numbers were adjusted by replacement rates over the expected rates from demographics of the population on how people were going to retire or die. He noted a difficult area to project was the unnamed supply; the people moving into the state. He said DETR did not know those new people and their occupation until they found employment. He concluded that DETR looked at the occupational industry output by area.

Chairman Small asked Mr. Murdock if the state was doing a good job of bringing new businesses into the state. Mr. Murdock responded there was a good diversification of businesses coming to the state. He said diversification was a hard issue to pin down as far as what was coming into and what would benefit the state. He reiterated that construction, manufacturing had taken off. Also, warehousing and transportation were doing well because of the proximity to the markets in California and the growth rates in other industries were surpassing the leisure industry.

### **GAMING PERCENTAGE FEE COLLECTIONS**

Chairman Small indicated the Forum would receive presentations regarding Gaming Percentage Fees and then take a short break.

*Russell Guindon, Fiscal Analysis Division*

Mr. Guindon indicated that Table 1, behind tab 5 of the meeting packet (Exhibit C, page 43) provided a history over the past seven years for the general fund revenue sources and growth through the first three months of FY 2005, compared to FY 2004. He stated that Table 1 had been utilized since the beginning of the Economic Forum process so members could see the historical growth for the state's revenue sources.

Continuing, Mr. Guindon stated that Table 2, located on page 57 of the meeting packet, had been provided to the Forum at the previous meeting with some modifications. He noted that Table 2 showed the forecast for FY 2003 and FY 2004 compared to the actual. The Forum's forecast with legislative adjustments approved during the 2003 regular and special sessions for FY 2005 were also presented in Table 2, together with what the Forum's growth rate had been projected and what it would be based on the FY 2004 actuals.

Mr. Guindon pointed out that the category "Total Secretary of State Fees" on Table 2 showed a decline in FY 2005 and a decline in FY 2004, should be corrected to \$82,059,000 which meant a 10.3% growth was expected in FY 2005 and now based on the FY 2004 actual, 9% growth was needed to reach the Forum's forecast. Mr. Guindon said a new set of tables will be provided at the next meeting of the Economic Forum.

Mr. Guindon pointed out that Table 3 was located on page 75 of the meeting packet (Exhibit C). He said Table 3 presented for each general fund general ledger accounts, the forecasts produced by the agency responsible for collecting that revenue source and the estimates of the Fiscal Analysis Division and the Budget Office. Table 3 included the minor forecasts considered by the Technical Advisory Committee (TAC) to the Economic Forum to produce the consensus forecast prepared for the Forum's review and approval.

Mr. Guindon directed the Forum to Table 4 on page 87 of the meeting packet which listed the major general fund revenue sources for which the Forum would be making its forecasts.



Mr. Small asked Mr. Guindon to provide a brief summary of how the Forum's meeting would proceed and conclude. Mr. Guindon outlined the agenda by stating the Forum would be providing forecasts for the seven major revenue sources and presentations for each of those forecasts would be provided to the Forum for their consideration in making a consensus forecast for each revenue source. He reminded the chairman that motions were necessary for each of the revenue sources to reach a consensus.

Mr. Guindon reminded the Forum that the forecasts reached today were preliminary in nature and were used as preliminary numbers to assist the Governor in producing the budget for the next biennium. The Forum would be producing a final set of forecasts on December 1, 2004 for the Governor's use in developing his budget for the 2005-2007 Biennium. Under Agenda Item 6, Mr. Guindon advised that the Forum would be approving the TAC's consensus forecast for the minor revenues. The remainder of the agenda was typical—instructions to staff, public comment.

Ms. Pierce asked if the year-to-date figures on Table 1 of page 45 of the meeting packet represented the number for the first quarter of FY 2005. Mr. Guindon replied affirmatively and said the numbers were for July 1, 2004 through September 30, 2004; comparing that same period to FY 2004. Ms. Pierce said the number listed under the category *Real Property Transfer Tax* appeared to be in error because historically that number ran approximately \$25 million per quarter, yet the table reflected that number at \$3,638,873 for the first quarter which did not appear accurate.

Mr. Guindon said that was an astute observation and explained that the figures in Table 1 came directly from the State Controller's accounting system received at the end of each month. The Department of Taxation collected the information provided by the counties for the real property transfer tax then produces a public report showing how much was recorded. Therefore, the number reflected on Table 1 represented the amount deposited at this point in time into the general ledger account through September 30<sup>th</sup>. He confirmed that the number did not reflect the total quarter because the Department of Taxation had not received all of the information, reconciled, accounted and prepared its public report for the first quarter of FY 2005. However, he stated an updated real property transfer tax number would be available for the December 1<sup>st</sup> meeting of the Economic Forum.

#### *Frank Streshley, Gaming Control Board*

Mr. Streshley provided the Forum with charts regarding Gaming Revenue Forecasts for Fiscal Years 2005-07 (Exhibit\_H). He stated that in forecasting percentage fee collections, the Gaming Control Board (Board) forecasted the state's gaming win for the applicable years and then converted that number into percentage fees collections. He explained that as a starting point for the Board's forecast, a list of property assumptions was created which provided the outlook for the forecast period regarding new property openings, property expansions and known or anticipated closings during the fiscal years being forecast. From those property assumptions, a forecast for the number of slot machines and games expected to come on line during the forecast period was also created. Mr. Streshley said in preparing the property assumption list, the number of new hotel rooms coming on line was projected.

The Board also spent a great deal of time formulating base growth rates for each of the state's 16 reporting market areas such as the Las Vegas Strip, Downtown Las Vegas, Reno, Elko, etc. Mr. Streshley explained that formulating base growth rates was done by examining historical trends and through interviewing the individual property owners within those major reporting areas. He stated that there was a difference in how the Strip was forecast versus the Las Vegas locals market versus Washoe County. He advised the Forum that the Board also received input from some Wall Street analysts and the research department at the Las Vegas Convention and Visitor's Authority. Mr. Streshley indicated that sum of the individual market forecasts produced an estimated total statewide win noting that the Board individually forecast slot win and games win for each of the different markets.

Directing the Forum to his first chart entitled *Gaming Win Forecasts*, Mr. Streshley said the chart outlined the total gaming win for statewide, Clark County and balance of state. Starting in FY 2005, the Board was forecasting statewide gaming win to increase 4.9% and were anticipating 2,500 new slot machines, 130 new games and approximately 4,600 new rooms to come on-line. He said the majority of those new rooms will come on-line at the end of FY 2005 when the Wynn Las Vegas property opens on its targeted date of April 29, 2005. In addition, Mr. Streshley said a new tower would be opening in FY 2005 at the Bellagio which will add 925 new rooms to the market.

Continuing with the first chart, Mr. Streshley said gaming win in Clark County was expected to increase 5.7% with a large part of that growth continuing to be generated from the locals market where the Board was forecasting high single-digit

growth. Strong growth continued to be seen in North Las Vegas and the Boulder Strip. As for the Las Vegas Strip, Mr. Streshley said moderate growth was expected in gaming win until the end of FY 2005 and then there should be a spike in revenues as the first mega-resort opens since the Alladin opened over five years ago. Prior to the Wynn opening, the Board anticipated that revenues would be up but not at the same pace as last year due to the record growth being compared where four of the last six months were double-digit growth.

For the balance of the state, Mr. Streshley stated the Board was forecasting 1.3% growth in FY 2005 with the growth coming from the Reno-Sparks locals market and the Carson Valley. He stated that the small counties were growing annually as well.

For FY 2006, the statewide forecast for gaming win was to increase 6.5% with an anticipated 5,100 new slot machines, 130 new games and approximately 2,100 new casino hotel rooms coming from the openings of the Southcoast property in fall 2005, followed by the Redrock Station property in spring 2006. Mr. Streshley stated that Caesar's Palace was also scheduled for a new tower in FY 2006 with 449 new rooms.

Clark County was forecast to grow 7.6% in FY 2006; similar to FY 2005 whereby the expected strong growth would be in the locals market especially with the two new properties coming on-line that cater to the locals. In addition, FY 2006 would have seen 11 months of new growth from the Wynn property.

Mr. Streshley said that same store sales growth should be strong for all of the major Strip properties in FY 2006 after the opening of the Wynn property. Usually what occurred when a mega-resort opened was the same store sales were boosted with competing properties.

As for the balance of the state, Mr. Streshley indicated that growth in FY 2006 was projected at 1.6% and similar to FY 2005, growth should come from the Reno-Sparks local market and some of the smaller rural areas.

Turning to the FY 2007 forecast, Mr. Streshley said the Board was forecasting statewide gaming win to grow 5.2% with Clark County at 5.8% and the balance of the state at 1.9%. In FY 2007, the Board anticipated approximately 1,900 new slot machines, 80 new games and 3,000 new rooms, all expected from the Palazzo, the new Sands property, with an expected opening date in FY 2007. He said additional property expansions were planned in FY 2007 but the Board had not included those in the forecast until a defined number of units and specific completion dates were obtained and until the properties actually broke ground.

As a side note, Mr. Streshley said the average growth in gaming win for the past ten years was about 4.5% so other than FY 2006, the Board was close to that percentage. As stated earlier, the Board prepared a separate forecast for slot win and games win. He directed the Forum to the chart on page 2 of his handout ([Exhibit H](#)). The Board projected slot win by forecasting the growth in wagering activity or the coin-in per slot machine along with the win percentage. Those two components are combined with the number of forecasted slot units, which included the new properties coming on-line. The chart entitled *Slot Win Forecasts* showed slot win growth over the next three years. After growing 7% last year, the Board projected slot win would increase 5.5% in FY 2005, 6.1% in FY 2006 and 5.5% in FY 2007. He noted that the average growth rate over the past ten years was approximately 5.5%.

Breaking down the slot win over the state, Mr. Streshley said for the base year, Clark County was projected to grow 6.4% and only 2.1% for the balance of the state. He reiterated that the growth was in Clark County with visitation continuing to grow on the Strip and the locals market. That trend was continuing through FY 2006 and FY 2007 with slot win growing in Clark County 6.9% and 6.2%, respectively. For the balance of the state, slot win growth was projected at 1.8% in FY 2006 and 2.2% in FY 2007.

Mr. Streshley stated the chart on page 3 outlined games and tables win. He explained that the Board's methodology for games and tables was the same as described previously for slot win. After increasing 5% in FY 2004, Mr. Streshley said the Board was expecting an increase in FY 2005 of 3.8%, 7.4% in FY 2006 and 4.6% in FY 2007. He indicated that the jump in games and tables win in FY 2006 was due to the opening of the Wynn property and the Southcoast property. Following the Wynn property, the Board projected strong game play, especially the high-end games such as Baccarat which had been recovering over the past 12 months from a big drop-off after September 11, 2001.

Mr. Streshley informed the Forum that games play should also benefit from some of the operators such as the Sands, the Wynn, the MGM and the Mirage opening properties in Macau, China and marketing their Las Vegas Strip properties to those visitors as China relaxes some of their travel restrictions outside the country. He said that trend should materialize over the next 12 months.

The average growth rate for games and tables over the past 12 years was 3.2% and similar to slot win, the growth rates were based on a growing economy over the next three years. Breaking down the state for games and tables win, Mr. Streshley said for the base year growth was projected at 4.6% in Clark County, declining 1.1% for the balance of the state in FY 2005. In FY 2006, Clark County growth in games and tables win was forecast at 8.3% and the balance of state flat, only up .9%. In FY 2007, Clark County growth was anticipated at 5.1% with the balance of the state up only 5.7%.

After forecasting gaming win, Mr. Streshley explained, the Board then converted that to taxable gaming revenue. He said an assumption was needed on how much of the gaming win will become taxable revenue. The difference between gaming win and actual taxable revenue to which the tax credits were applied was credit play. He stated that gaming win included all wagering activity from cash, chips and wagering activity made through the issuance of credit which was mostly on the games side. Mr. Streshley went on to state that wagering activity through credit did not become taxable until the credit was paid off, which could be several months later than the activity and, of course, some of the credit became uncollected.

Directing the Forum to page 6 of the Board's handout, Mr. Streshley said the chart entitled *Taxable Gross Revenue to Win Ratio* showed that the taxable revenue to gaming win had averaged approximately 96.3% over the last ten years. However, the last three years following 9/11 saw an increase to 97.4% which was due to a decrease in tables game play and the associated wagering that was done through credit. As the chart showed, the Board was projecting that the ratio would decline over the next two years as an increase in games and tables occurred. For FY 2005, the ratio was projected at 97%, in FY 2006 with the opening of the new properties the ratio was expected to drop to 95.8%, under the assumptions that the high-end properties were aggressive with their credit properties. In FY 2007, the ratio was projected at 96.2% as credit play normalized.

Returning to page 4 of the handout, the Board's *Percentage Fee Collections Forecast*, in FY 2005 the forecast was estimated at \$685.3 million in collections, increasing only 1.2%, due largely in part to the \$29 million swing in the estimated fee adjustment (EFA) (Exhibit H, page 5). Mr. Streshley said in FY 2005 the Board estimated the EFA at \$4.4 million, which followed last year's EFA of \$34 million as a result of the tax rate increase. Currently, fiscal year-to-date with three months reported, collections were up 6.5% with a negative \$6.2 million EFA. In FY 2006 percentage fees collections were forecast at \$723.6 million, an increase of 5.6% with an EFA of \$7.4 million. For FY 2007, the Board forecasted percentage fees collections at \$761 million, an increase of 5.2% with an EFA of \$4 million.

Mr. Streshley concluded his forecast on gaming percentages fees and indicated he was available to answer any questions.

Chairman Small inquired into the impact of Indian gaming on future projections of gaming percentage fees. In response, Mr. Streshley stated that the only market that had any adjustments in consideration of Indian gaming growth rates was the Reno-Sparks market. He stated that the expansion of tribal gaming had not resulted in quantified material impacts to the Las Vegas market and even the impact to the Reno market was not to the extent that some of the analysts had projected would occur. Mr. Streshley said last year with the opening of Thunder Valley, the Reno market was down 2.6%. The Board took a conservative approach but also believe Indian gaming would continue to expand, mostly affecting the northern part of the state. He stated that the Board would continue to observe what occurred after the election and if material changes were visible (expansion into card clubs and racetracks) then further adjustments would be made.

Mr. Fisher asked how much of Nevada's gaming win was United States sourced and how much was Asian? Mr. Streshley replied that visitor profiles were obtained from Las Vegas which showed how many visitors came from southern and northern California, the east coast and west coast, and international. His recollection of that report was that international visitors amounted to less than 10% and that the international traveler stayed longer and spent more. However, customer profiles did not address the high-end customers who made up a substantial amount of the games play, which had been declining over the years but was now moving back up.

*Bill Anderson, State Budget Office*

Mr. Anderson thanked the Economic Forum for developing preliminary forecasts at the October meeting. He said although the Forum was not obligated to do so, the preliminary forecasts a month earlier than required were extremely helpful to the Budget Office and the Governor's Office in making decisions.

Mr. Anderson stated at the last meeting of the Economic Forum he tried to accomplish three things: 1) Give the Forum a feel for how the Budget Office made its forecasts for the major revenue sources; 2) Give the Forum a feel for the underlying accuracy of those forecast approaches; and 3) Provide to the Forum the Budget Office's preliminary forecast to assist in approaching the revenues under consideration.

With that background information in place, Mr. Anderson indicated he would be able to spend his time at this meeting discussing the specifics of the Budget Office's forecasts, raise some of the strengths and weaknesses and highlight the issues as seen by the Budget Office regarding the major revenue sources.

Mr. Anderson said the percentage fees collections forecast he was presenting was unchanged from his predictions at the September meeting.

Turning to page 8 of the Budget Office's handout (Exhibit I), Mr. Anderson reminded the Forum that his forecast for percentage fee collections was driven by visitor volume and the impact on win, as well as gaming activity in general. He said the Budget Office also factored into its methodology an underlying historical trend. Looking at pages 10-12 of the handout, the tables entitled *Mean Percent Errors* showed the results of forecasting percentage fees collections for the Budget Office which appeared to be fair; with underlying forecast errors in the mid to single-digit range.

Mr. Anderson stated the forecast for percentage fees collections was presented on page 14 of the handout. Looking at his forecast in comparison to the other forecasters, he would have to make a case for the 0.5% growth rate in FY 2005 because that appeared "out of whack" as was alluded to earlier. He would also need to make the Forum comfortable with the relatively modest 4 to 4.5% growth rate going into the next biennium. However, with respect to the percentage fees collections forecast of the Budget Office, Mr. Anderson said an underlying growth in the tax base was projected at 4 to 4.5% per year, which was driving their forecast. For the most part, the forecasts from all of the agencies had minimal growth, if any, shown in FY 2005. He said that could be explained in the charts on pages 15-16 which related to the EFA. Mr. Anderson said the chart at the bottom of page 15 tracked the EFA for each year over the course of the year. Looking at the May column, the EFA came out at basically zero, as was stated earlier by James Diffley of Global Insight. Mr. Anderson pointed out that in FY 2004 the EFA ended at approximately \$34 million. He pointed out that FY 2005 showed the EFA in a more expected normal pattern. Like Mr. Diffley, the Budget Office believed the EFA would end at zero by the end of the fiscal year.

Mr. Anderson said the chart on the top of page 16 was more simple, *Percentage Fees Breakdown*, and showed the difference between taxable gross revenue and collections from the EFA. He said the chart showed why historically the Budget Office had been ignoring the EFA in its forecasting. Mr. Anderson surmised that the chart showed the EFA was insignificant, but also showed for FY 2005, for the first time, a portion of the total was identifiable. Looking from FY 2004 to FY 2005, the growth from the tax base could be seen but that growth was more or less completely off-set by the loss of the EFA. He reiterated that the underlying growth rate in percentage fees collections was occurring at 4 to 4.5% but it was being off-set by the EFA; which hopefully would answer some of the Forum's concerns expressed earlier.

Regarding year-to-date projections for the percentage fees collections, Mr. Anderson said the win growth for the first three activity months of FY 2005 was approximately 5%, which was in line with the 4 to 4.5% growth rate. He noted through the first three months of FY 2005, games and tables win decreased by approximately 3.4% and it would be interesting to see how the next few months unfolded.

Mr. Anderson indicated stronger growth was seen in taxable gaming revenue which he believed occurred due to technical factors and was typically the case; by the end of the year win and taxable gaming revenue tended to move hand-in-hand. The Budget Office forecast that by the end of the year the figures would be bumping up against some strong year-ago numbers which should moderate growth somewhat, bringing the win growth from the current 5% growth rate closer to 4.5%.

By January 2005, the Budget Office will be comparing back to the first quarter of last year when win was up 10.4%. The second quarter of the calendar year 2005, would be comparing back to a year ago quarter when win was up 9.8% so once that point was reached, moderation should be seen and the year would end in the 4 to 4.5% underlying rate of growth.

Mr. Anderson said the forecast of the Budget Office was structurally sound. Looking at the chart at the bottom of page 16 *Real Win Per Visitor – Annual*, he showed that his forecast was in line with historical trends (also see chart on page 17). He noted that since the mid-1990's the state was in a slight down-trend, with an increase seen in FY 2004 due to the tax rate increase but other than that the projections returned to the historical activity.

Mr. Anderson said he was doubtful that he would see anything in the gaming report expected next week that would change his forecast before the Forum's next meeting on December 1, 2004. He said he certainly did not see that anything could occur in the next month that would cause him to change his outlook for the next biennium beyond tweaking the current year and then growing off of those slightly revised numbers. Therefore, he concluded that he was comfortable with the forecast of

the Budget Office.

Mr. Seevers asked if the Budget Office had made any adjustments in their numbers for the new properties coming on line.

In response, Mr. Anderson said the new properties were considered and he would be discussing that further during the presentations on the Live Entertainment Tax. However, after talking with contacts in Las Vegas, the underlying rate of growth in visitor volume was in the 3-4% range and up to the higher portion of that range when the new Wynn property comes on line and at the lower end of that range this fiscal year. He commented that the other forecasts provided to the Forum showed more of an impact than the Budget Office regarding the new properties coming on-line, but consideration in the forecast of the Budget Office was given to the magnitude of the market. Explaining further, Mr. Anderson said in the late 1990's through the early 2000's with the last round of property expansions, those new rooms translated into approximately a 14-15% increase in capacity. The new property coming on line in FY 2005 was expected to increase capacity by approximately 2% so an impact would definitely be seen. However, the Budget Office questioned whether the results from the late 1990's would be replicated; it all became a question of scale.

Mr. Martin said there used to be a concept relating to amusement parks—that a new feature should be added every year to bring out new people. He said even though the Wynn increase in rooms may only be 2%, a new property tended to fill other hotels with people who wanted to come see the new property. He asked if that concept had been factored into the Budget Office's forecast.

Mr. Anderson replied that the Budget Office approached percentage fees collections from a visitor volume perspective and the underlying rate of growth in the visitor volume was arguably 3%. That would be increased by a full percentage point as a result of the new property, especially the Wynn property so he would affirm that the new properties were factored into the forecast of the Budget Office.

Chairman Small thanked Mr. Anderson for his presentation.

*Russell Guindon, Fiscal Analysis Division*

Mr. Guindon directed the Forum to his handout (Exhibit E) entitled *Fiscal Analysis Division Forecast Information for the Major General Fund Revenues*, specifically Table 1 on page 5 of the handout. He explained that Table 1 summarized historically the slot win, games win, total win, taxable gaming revenue (TGR), the percentage fees collected from taxable gaming revenue and finally the total percentage fees, which was the sum of that collected from the taxable gaming revenue, plus or minus the EFA adjustment. He stated that Table 1 of the handout also included the Fiscal Division's forecast for FY 2005, FY 2006 and FY 2007.

Mr. Guindon stated that the methodology used by the Fiscal Division for forecasting percentage fees collections was almost identical to that used by the Gaming Control Board. However, his methodology did not breakdown the detailed markets. Rather, the Fiscal Division used information from Clark County, Washoe County and balance of state. He indicated those figures were shown in the statewide numbers presented in Table 1.

For the Fiscal Division, Mr. Guindon said the forecast was for slot win to grow 4.9% in FY 2005, after growing 7% last year. He pointed out that the detail for the Fiscal Division's slot forecast was shown on Table 2, page 6 of the handout (Exhibit E). Table 2 also contained historical information as well as the Fiscal Division's forecast for slot win, the win-per-slot, the average number of slot machines in use and the average slot win percent. Mr. Guindon explained that the average slot win percent was the average hold the casino kept from wagering through the machine and the coin-in-per-slot was the handle or the wagering per machine. The Fiscal Division was assuming that slot win would grow 4.9% in FY 2005, 5% in FY 2006 and 5.7% in FY 2007.

Directing the Forum to the column on the far right of Table 2, Mr. Guindon said it could be seen that two relatively strong years of growth in coin-in per slot occurred in FY 2003 and FY 2004 with 3.1% and 4.2% growth, respectively. Growth in coin-in per slot was forecast by the Fiscal Division at 5% for FY 2005, 2.3% in FY 2006 and 2.0% in FY 2007. He explained the reason for the strong slot win growth in FY 2004 and FY 2005 was as had been pointed out during the September meeting—there had been an increase in the coin-in. In looking at the numbers and in conversations with the Gaming Control Board, this was likely due to the switch out of machines—the older-style slot machines were being replaced with the ticket-in, ticket-out (TITO) machines. The TITO machines were popular and tended to be very productive. Mr. Guindon said looking back historically it was evident in the column to the left of the coin-in-per-slot, that the average slot win percent showed an

increase of 0.23% in FY 2004 which was a huge increase in the average hold over the 12 months of a fiscal year.

Mr. Guindon said the slot win definitely went through cycles in terms of changes in the types of machines the manufacturers produced given the demand and what was attempted to be demanded by the player. That pattern was likely to continue in FY 2005 and the productivity or average hold of the machines would continue to increase in FY 2005, FY 2006 and FY 2007. It was expected that slot machines in use would continue to fall in FY 2005 but then by the end of FY 2005, stabilization was expected after the machine change-out occurred. Slot win growth was also expected in FY 2006 and FY 2007 due to the new properties coming on-line and the number of devices expected at that time. However, there was a risk that when machines were added to the market as to whether or not the market would support those new machines. He said the Fiscal Division was anticipating visitor growth to increase in FY 2005 by approximately 3.9%, 5.8% in FY 2006 with a drop back down to 2.1% in FY 2007 because of the year-to-year comparisons.

Table 3 at page 11 of Fiscal Division's handout represented the games side of the market. Mr. Guindon said total game win grew 5% in FY 2004, while the prediction was for growth of 1.4% in FY 2005, 4.1% in FY 2006 and 2.8% in FY 2007. With the average number of games falling for three consecutive years, that trend would be ending in FY 2005, primarily because of the Wynn property which would add close to 100 games. Also, because of the other properties coming on-line, growth would be seen in FY 2006 and FY 2007. Mr. Guindon pointed out that huge increases in the drop per game in FY 2004—almost 11%. However, for the upcoming forecasting cycle an assumption was being made in consideration of the new devices coming on-line that the visitor growth will support the new devices resulting in an increase in the drop or wagering per game in all three forecast years.

While listening to the Gaming Control Board's presentation, and in comparing the Board's games win forecast to the Fiscal Division's forecast, Mr. Guindon would guess that the Fiscal Division's forecast did not include as much of the international market in the forecast as the Gaming Control Board regarding the high-end segment of the market.

Ms. Pierce inquired into the games win forecast for FY 2006 which would include the anticipated opening of the Wynn property for one full year. She agreed with Mr. Guindon that an increase was likely in the win-per-game because the property was expected to bring in a higher end player and more international play as well. She questioned whether the win-per-game had been increased enough. She said it was difficult to determine but reiterated that she agreed there would be an increase in win-per-game when the Wynn property opened.

Mr. Guindon said his forecast included increases in win-per-game in FY 2005 and in the two out years but he understood Ms. Pierce's question to be that his increases might not show enough of an increase. Ms. Pierce said she personally anticipated that the increase in FY 2006 in win-per-games would be a nice increase.

Mr. Small recollected Mr. Guindon's earlier comments that the TITO technology had increased the slot revenue. He asked if the percentage of the numbers of machines already converted was available and the conversion dates for future machines. In response, Mr. Streshley said he did not have the exact percentage of slot machines that had been converted to the TITO technology but the majority Las Vegas Strip properties had been converted or were in the process of converting to TITO machines. He added that in the local markets such as Boulder Strip, North Las Vegas, balance of county the properties were either in the process or had completed the conversion process.

Returning to page 1 of the Fiscal Division handout, Mr. Guindon said given the forecast of slot win and games win a number for total win was obtained. The total win was forecasted to grow 3.7% in FY 2005, 4.7% in FY 2006 and 4.8% in FY 2007. Thereafter, a decision was necessary regarding the credit action to convert the win number to taxable gaming revenue. Mr. Guindon assumed the taxable win ratio would be 97.4% for each of the three forecast years, which was the average over the last three years. No adjustment downward in FY 2006 was made for when the Wynn property came on-line. He said although that might be a valid assumption, he was unsure what number was appropriate so retained the 97.4% figure, with the intent of future analysis after the Wynn property came on-line.

Mr. Guindon said the percentage fees for taxable gaming revenue were forecast to grow 5% in FY 2005 with the assumption of an average tax rate of 6.64%. He added that was an assumption because in FY 2004 ten of the 12 months were at the old rate and two months were at the new rate. That average tax rate of 6.64% was then carried out for all three forecast years. The bump up was seen between the 3.5% taxable gaming revenue growth and the 5% in the percentage fees because a full 12 months in FY 2005 will be collected at the increased tax rate.

As had been discussed, Mr. Guindon stated the EFA played a major role in the Fiscal Division's forecast for FY 2005. Looking at Table 1 on page 5 of the handout, the far right column showed how much the EFA differed from year to year. The

top half of the chart showed the dollar amount difference while the bottom half of the chart showed the percent difference. He said the EFA fluctuated (it was \$5 million one year and -\$5 million the next year); a \$10 million swing in terms of the impact on percentage fee collections.

Mr. Guindon explained that the Fiscal Division estimated the EFA in their forecast by making assumptions of what would occur with the new properties and looking at assumptions relative to the market. He said when no new properties were on the market, the EFA ended up being the difference between the last three months of the current fiscal year compared to the last three months of the prior fiscal year. Since the Fiscal Division did its forecast quarterly, an assumption as to the market, except for the new properties, was determined by looking at the difference between the fourth quarter one year and the fourth quarter the prior year and the net increase between the two figures. Using that methodology, Mr. Guindon had determined an EFA in FY 2005 of \$3 million, which showed growth of 0.2% representing a net decline of approximately 4.9% in overall growth. He pointed out that in FY 2004 the EFA was almost a \$40 million net increase and based on his \$3 million projection the EFA was projected at a \$31 million negative hit against collections.

Continuing with the same methodology for the out years, Mr. Guindon related that the EFA was estimated at \$5.4 million for FY 2006, an approximate \$2.3 million net positive increase. Instead of the percentage fees from taxable growing 4.7%, the total percentage fees should grow 5% which actually added 0.3% increase to the growth rate. Finally, in FY 2007, Mr. Guindon said with the growth occurring in the forecast, the EFA was projected to be approximately \$4.2 million, a -\$1.2 million net negative hit so instead of growing 4.8% off the taxable, the total percentage fee grew 4.6%.

As pointed out by Mr. Streshley of the Gaming Control Board, total percentage fees collections were up 6.5% for the first three months of FY 2005. To hit the forecast of 0.2% a decline in collections on average of 1.7% could occur over the remaining nine months and still reach the forecast. Mr. Guindon said the number may not mean as much as it normally did simply because FY 2005 was not quite "apples to apples" in terms of the tax increase and the huge EFA effects.

Mr. Guindon said he was available to answer any questions.

Chairman Small said he would entertain a motion for a preliminary estimate over the next three years for the percentage fees collections.

MS. PIERCE MOVED TO APPROVE FOR FY 2005 A 0.5% INCREASE, FOR FY 2006 A 5.3% INCREASE AND FOR FY 2007 A 5.0% INCREASE IN PERCENTAGE FEES COLLECTIONS.

MR. SEEVERS SECONDED THE MOTION.

Mr. SeEVERS said the numbers proposed by Ms. Pierce seemed logical although he was in a bit of a quandary due to the EFA fluctuation, but he would go ahead with the motion as presented.

THE MOTION CARRIED UNANIMOUSLY.

Chairman Small asked if any material was available in the meeting packet indicating percentages of total revenue for each revenue source so the Forum could obtain a general idea of the magnitude of the general fund revenue sources.

Mr. Anderson said he did not have the numbers with him.

Mr. Guindon said the figures requested had been provided in the September meeting packet and were as follows:

- Gaming Percentage Fees - approximately 27-28% of the general fund. He explained that that number was based on the previous forecast with the legislative adjustments.
- State Sales Tax - approximately 31-32%.
- Live Entertainment Tax (total including gaming and non-gaming) was approximately 6.4% but actually came in at 5% so the range would be 5-6%.
- Cigarette Tax - approximately 4.7-4.8%
- Modified Business Tax (non-financial) - approximately 6-7%
- Modified Business Tax (financial) - in the 1% range
- Real Property Transfer Tax - in the 2.5-3% range
- Insurance Premium - approximately 8% of the total general fund.

Mr. Guindon said the above percentages were estimates based on the FY 2004-05 projections with legislative adjustments.

Chairman Small said he noticed a trend that percentage fees and sales tax had previously been a larger percentage but were now shrinking as a percentage of total general fund. Mr. Guindon replied that with the tax changes that occurred in S.B. 8 and other bills passed during the 20<sup>th</sup> Special Session, the mix changed and the FY 2003 actual showed percentage fees at approximately 32% so that percentage did decline slightly even with the 0.5% tax increase due to the creation of the modified business tax and the real property transfer tax.

Chairman Small announced a break at 11:05 a.m. The Forum reconvened at 11:25 a.m.

### **LIVE ENTERTAINMENT TAX (GAMING)**

*Frank Streshley, Gaming Control Board*

Frank Streshley of the Gaming Control Board (Board) stated the Board's forecast for the live entertainment tax was based on a forecast of taxable casino entertainment activity. The forecast of taxable activity was based upon an examination of historical growth patterns and more importantly the Board contacted the various properties to find out the new venues. Mr. Streshley said the forecast also incorporated the expected taxable increase due to the opening of new properties and changes within the current taxable entertainment venues at the existing properties. Mr. Streshley noted that the live entertainment tax (LET) was one of the more difficult taxes to forecast as charges for admission, beverage, food and entertainment was not consistent from year-to-year and the entertainment offered was constantly changing along with the price for admission and the durations of some of the production shows. Making it more difficult for this forecast period was the additional large venues with a capacity of 7,500 or more seats with most of the revenue coming from concerts and the Board was unable to predict the concert tours or the pricing structure over the next several years.

Referring to his handout, Gaming Revenue Forecasts, (Exhibit H), Mr. Streshley said there was a tremendous amount of growth in the new high-end entertainment venues and over the next three years; approximately 10,000 seats will be added to the high-end showrooms. When the Board projected their forecast with the new seating capacity in the showrooms, they started out with the base level growth each year of approximately 4% to 5%. Starting with FY 2005, the Board projected the live entertainment tax (LET) would grow 11.6% with \$94.7 million in new collections. Adding to the base level growth, MGM would be opening a new 2,000 seat showroom in November with a Cirque-style show which will have 2,000 seats offering ten shows per week with an average ticket price of \$115 to \$125. Mr. Streshley noted the new ticket price put the venue at the same level as the Celine Dion show added two years ago.

Opening in the spring of 2005, the Mirage will be replacing the Siegfried and Roy show with another Cirque-style show geared toward the Beatles with 2,000 seats; approximately ten shows per week with the average ticket price of \$115 to \$125. In addition, the Wynn Las Vegas will open the first of their two showrooms with 2,000 seats, nine to ten shows per week with the average ticket price of \$125 to \$150.

Moving to FY 2006, the Board forecasted LET to grow 23.9% with \$117.3 million in collections. Mr. Streshley noted that part of the 20% plus growth was from the two new showrooms opening the end of FY 2005 and in addition, the Wynn property would open a second showroom in September 2005 with approximately 1,500 seats. Mr. Streshley was uncertain of the number of shows that would be added to the Wynn property, so their forecast was conservative for the number of shows per week but estimated the average price per ticket would be \$80 to \$100.

Also in September 2005, the Blue Man Group, which was currently performing at the Luxor would be moving to a larger showroom at the Venetian with approximately 500 additional seats with the current ticket price of \$75 to \$80 increasing to approximately \$100. In FY 2007, the Board was forecasting 9.5% growth with total collections of \$128.5 million. In September 2006, the Venetian was expected to open a new showroom with a production of the Phantom of the Opera. Complete details of the showroom size and ticket prices were not available so the forecast was somewhat conservative. In addition, the new Sands Las Vegas property, The Pallazzo was projected to open in 2007 and even though the Board did not have the details on the entertainment venues, a conservative forecast was projected.

In response to a question posed by Chairman Small, Mr. Streshley said the LET applied differently to venues with over 7,500 seats. Currently, five venues had over 7,500 seats: 1) Mandalay Bay with approximately 12,000 seats; 2) MGM with approximately 18,000 seats; 3) Aladdin; 4) Orleans with approximately 10,000 seats which they used for concerts and a triple A hockey team; and 5) Reno Hilton which had a seasonal outdoor amphitheater.



*Bill Anderson, State Budget Office*

Mr. Anderson said the Budget Office LET forecast was driven by visitor volume as well as expectations concerning entertainment-related spending on a per visitor basis. He reiterated the LET was difficult revenue to forecast but since the visitor-based approach was adopted beginning with the October 2000 Economic Forum meeting, good results had been seen when looking at the forecast accuracy analysis. He directed the Forum to page 32 of his handout, Budget Division General Fund Revenue Forecasts, ([Exhibit I](#)), and said the chart showed forecast errors in the low single-digits since the approach was adopted and he was comfortable with the forecast. In looking at the Budget Office forecast, page 33, Mr. Anderson said the one thing that stood out in the forecast was the growth rate in 2006. He noted that the forecast was driven by visitor growth in addition to growth in visitor spending. Referring to the chart on page 31 of his handout, Mr. Anderson said the graph showed tax collections per visitor and how it behaved over time. He pointed out there was a decade-long period of stability that ended in the mid-1990's and as Nevada's market evolved toward an entertainment capital as well as a gaming capital beginning in 1995, growth in the collections per visitor had occurred which reflected the growth in the entertainment component.

Moving to the late-1990's and into 2000, with the expansion of the four or five properties that came on-line during that time, the spending per visitor increased and put the state on a new trajectory. After the most recent round of expansions was absorbed, the state returned to a steady growth pattern and was seeing impacts of the changes in the tax base and the various tax rates associated with the tax. Again, Mr. Anderson said his practice was to focus solely on the Budget forecast but it was safe to assume the reason their projections were relatively low in FY 2006 had to do with how the Budget Office interpreted the likely impacts of the new properties and showrooms coming on-line.

Mr. Anderson said the Budget Office was not convinced that the state had pushed on to the new trajectory with the new round of expansions as occurred in the 1990's but there was precedence for that kind of growth. In the final quarter of 1998, when the Bellagio came on-line, the collections per visitor rose by approximately 12.5% over a year-ago quarter which compared to the underlying growth rate driving the Budget's forecast of approximately 7.5%. Moving to the first quarter of 1999, when the Mandalay Bay came on-line, the growth in collections per visitor was approximately 19%. Second quarter of 1999, the Venetian came on-line and growth in collections per visitor was 27% and in the third quarter of 1999 when the Paris came on-line, growth in collections per visitor was approximately 20%. As previously mentioned, the reason the Budget Office forecast was lower in the percentage fee forecast had to do with scale based on the old casino entertainment tax collections which evolved into the LET. The entertainment market was now about 75% larger than a decade ago based upon the collections.

Concluding, Mr. Anderson said that was what held his forecast down relative to the other forecasts presented and he was fairly confident of his forecast in the short term. He said the precedence was there for a larger forecast in FY 2006 especially with the expected increase in capacity but currently he was not comfortable taking that step.

*Russell Guindon, Fiscal Analysis Division*

Mr. Guindon directed the Forum to page 16 of the Fiscal Analysis Division handout, ([Exhibit E](#)), and said the chart showed the actual LET collections, the Division forecast, inflation-adjusted collections using the Consumer Price Index as the price deflator and Las Vegas visitor volume. The Division's forecast for visitors to Las Vegas is 4% growth in 2005, 5.8% growth in 2006 and again because of the year-over-year comparison, only 2.1% growth in 2007. He noted that the chart also showed the LET and the inflation-adjusted LET collections per visitor. Mr. Guindon concurred with Mr. Anderson and Mr. Streshley that the LET was a difficult revenue source to forecast because the Gaming Control Board only received the total monthly collection amount each month with no information available on the price of the shows, the number of shows or number of patrons. He noted when he compiled the Division forecast, he made assumptions of what he thought the collections per visitor would be over the forecast period multiplied by projections of the number of visitors for each fiscal year and looked at the inflation-adjusted terms; but he would argue that the inflation premium for shows outpaced the Consumer Price Index.

In addition, Mr. Guindon said he used information he obtained from news articles and information provided by the Gaming Control Board on additional shows that would be added to the market over the 2005-2007 forecast period. He realized a lot of capacity could potentially come on-line so he also prepared a base forecast not adding the new shows. Based on that, he made a pessimistic assumption that other than the first quarter in 2004, because of year-to-year tax changes that had to be annualized, the inflation-adjusted LET collections per visitor would show zero growth. Given that and Global Insight's projections for the Consumer Price Index and his projections for the Las Vegas visitor volume; the Division forecasted 9.7% growth in 2005, 7.3% growth in 2006, and 3.8% growth in 2007 in LET collections. He commented the projections were what he called a "base forecast" and it was pessimistic to assume there would be zero growth in inflation-adjusted collections per visitor but he was uncomfortable with the numbers when expected new growth was added.

Mr. Guindon stated starting in FY 1999, there was 13.3% growth in the LET collections per visitor because of the new capacity that came on-line. Continuing, there was 8.4% growth in 2000 in inflation-adjusted collections per visitor, 3% growth in 2001, 3.8% growth in 2002, 4.8% growth in 2003, and 12.9% growth in 2004 due to the tax changes. He noted that in the last six to seven years there was fairly good growth in the inflation-adjusted LET collection per visitor and he would argue by assuming zero, he was being somewhat pessimistic. Given that as his base, Mr. Guindon took into consideration additional capacity from the new shows and the net increase from moving the Blue Man Show from one property to another and calculated the net increase from the move. In FY 2006, under his assumptions, approximately \$6.4 million was generated per quarter once the shows were all on-line and operating. When all the other properties were on-line in FY 2007, under his assumption, approximately \$7.1 million was generated per quarter. He knocked down the projection and assumed the showroom would not be filled at full capacity and since all the properties had less than 7,500 seats, all food, beverage and merchandise sold at the show would be subject to the ten percent tax but he did not include any amounts for food and beverage sales in his projections. He said that once he took all that into account, he projected 13.8% growth in 2005, 28.3% growth in 2006 and 6.2% growth in 2007. He noted the growth slowed down in 2007 because there was more year-to-year with all the capacity that came on-line in the prior fiscal year.

Ms. Pierce commented on the difference between the Budget Office and Fiscal Division's forecast approach for 2006. For instance, when the additional capacity came on-line, the Fiscal Division's projections were driven by that additional capacity and assumed that the new capacity would drive more visitors and more money would be spent on entertainment. Yet, the Budget Office forecast assumed that a substantial number of seats for the new showrooms were going to be filled with patrons that would have been attending other shows and was expecting to see a delusion of occupied seats in the total market. Ms. Pierce asked if her thoughts on the different approaches were a reasonable assumption.

Mr. Anderson responded that it was a reasonable assumption from the perspective of the Budget Office forecast. Mr. Guindon commented that he assumed there would be zero growth in the LET collections for visitors when he did his base forecast. He said that was something that was not observed historically so with all the new capacity coming on-line in the base forecast, he was basically arguing the new properties could be pulling some business away from the existing properties and that was why zero growth was assumed in the LET collections per visitor. He noted that for the 9% growth, 7% growth and 4% growth in his base forecast, when the assumptions were added, he used the average prices that Mr. Streshley provided and assumed the showrooms would only be filled to an average of 80% occupancy. He added that tax collections from food, beverage and merchandise sales from the new shows were not included in the forecast. The Fiscal Division's forecast assumed with the visitor growth shown on page 17 of his handout, patrons would support the shows and could possibly support them more than he had assumed given the assumption of the base forecast.

Mr. Fisher said that looking at the historical data on prior growth, tax collections stayed under 14% net collections per visitor and he asked how the Fiscal Division forecast would change for 2006 if 14% growth in net collections was used per visitor in 2006. Responding, Mr. Guindon said if he let the inflation-adjusted collections per visitor amount of 1.323 in FY 2005 grow by 14% and used his visitor assumption of the \$40.4 million in the price index, instead of \$123.9 million projected, it would be approximately \$117.9 million and would take approximately \$6 million off the estimate.

MR. SEEVERS MOVED TO ACCEPT THE AGENCY FORECAST FOR LET COLLECTIONS OF 11.6% GROWTH FOR FY 2005, 23.9% FOR FY 2006 AND 9.5% GROWTH FOR FY 2007.

Chairman Small asked for a second to the motion.

Ms. Pierce commented she was concerned the projections for FY 2006 were high using the 23.9% growth from the agency and would prefer these projections were lowered but she was comfortable with the projections for FY 2005 and FY 2007.

THE MOTION FAILED DUE TO A LACK OF A SECOND.

Chairman Small said the Forum was only forecasting the LET gaming portion. He asked if there was another motion.

MS. PIERCE MOVED TO ACCEPT THE AGENCY FORECAST OF 11.6% GROWTH FOR FY 2005, LOWER THE NUMBER TO 16% GROWTH IN FY 2006 AND ACCEPT 9.5% GROWTH FOR FY 2007.

Chairman Small asked for a second to the motion.

Mr. Fisher asked if the motion dropped the FY 2006 forecast by approximately \$8 million. Ms. Pierce said that was correct. Mr. Fisher said he would second the motion if there was 18% growth for FY 2006.

THE MOTION FAILED DUE TO A LACK OF A SECOND.

Chairman Small asked for another motion.

Mr. Seevers said it was his understanding that new properties were coming on-line in FY 2006 that would expand the number of showrooms which in his opinion justified the 20% plus growth. Chairman Small confirmed the new venues in the Venetian, MGM, Mirage and Wynn would be opened in 2006.

Mr. Martin said he was persuaded to accept the agency forecast because the shows were typically 90% to 100% capacity shows and he believed whatever Mr. Wynn opened would absolutely be filled or sold out.

Mr. Fisher asked if the Forum would agree on 18% growth instead of the 16% growth for FY 2006 which would result in a \$2 million increase.

Mr. Martin commented that the Forum should not "stick out their necks" too far and needed to be responsible for their estimates.

Chairman Small reminded the Forum that the forecasts were only estimates at this point and the Forum would meet in December 2004 to review and finalize their forecasts.

MR. FISHER MOVED TO ACCEPT THE AGENCY FORECAST OF 11.6% GROWTH FOR FY 2005, 23.9% GROWTH FOR FY 2006 AND 9.5% GROWTH IN FY 2007.

MR. SEEVERS SECONDED THE MOTION, WHICH CARRIED UNANIMOUSLY.

Live Entertainment Tax (Non-gaming)

Chairman Small informed the Forum that Mr. Guindon reminded him that the LET non-gaming was collected by a different agency and was a different tax that generated little revenue. He said the LET non-gaming seemed smaller than the minor taxes that the Forum did not consider with respect to the major tax category and he was not opposed to adding the LET non-gaming to the minor tax category. He asked if there were any comments or suggestions.

Mr. Seevers concurred with Mr. Small and asked if a motion needed to be made. Mr. Guindon said it would be preferable for the body to make a motion to add the LET non-gaming tax to the minor tax category and he suggested the Forum listen to the presentations then decide on a projection for a complete set of preliminary forecasts. When the Forum addressed Agenda Item VII, Instructions to Technical Advisory Committee (TAC), a motion could be made at that time to direct the TAC to produce the forecast for the LET non-gaming portion.

Chairman Small asked if the motion should be made at this point to move the LET non-gaming to the minor tax category. Mr. Guindon said his preference was to wait until the Forum was on Agenda Item VII. He noted a revenue projection had to be decided upon for the LET non-gaming because the Forum did not previously direct the TAC to produce a forecast and if a revenue projection was not decided upon, there would be a piece missing from the general fund revenue forecast. Also, a decision needed to be made whether to go with the agency, Budget or Fiscal forecast.

MR. FISHER MOVED TO ACCEPT THE AGENCY FORECAST FOR THE LIVE ENTERTAINMENT TAX NON-GAMING.

MR. SEEVERS SECONDED THE MOTION. THE MOTION CARRIED UNANIMOUSLY.

Chairman Small said he would entertain a motion to move the LET non-gaming to the non-major revenue category in the 2005-2007 Legislative Session.

MR. SEEVERS MOVED THAT THE FORUM PLACE THE LIVE ENTERTAINMENT TAX NON-GAMING WITH THE NON-MAJOR REVENUE SOURCES DURING THE 2005-2007 BIENNIUM

MR. MARTIN SECONDED THE MOTION, WHICH CARRIED UNANIMOUSLY.

**2% STATE SALES TAX**

*Chuck Chinnock, Department of Taxation*

Mr. Chinnock provided the Forum with a memorandum including attachments (Exhibit J) dated November 2, 2004, with the subject identified as *Major Tax Projections*. He noted that page 5 of the handout, a chart entitled *2% Sales and Use Tax*, included projections using a logistics model and a graph was included on page 6 of the handout. Additional charts included in the handout were other models used while looking at projections regarding the sales and use tax.

Directing the Forum to page 5 of the handout, Mr. Chinnock said that FY 2004 ended with a record \$38 billion in taxable sales, a 12.8% increase above the prior year. Of course, Clark and Washoe counties were responsible for the majority of that increase. He pointed out that his memorandum indicated that the top five areas of taxable sales included: 1) eating and drinking; 2) automotive dealers; 3) miscellaneous retail; 4) general merchandise; and 5) building materials and hardware were shown to be the highest increases and strongest gains. Mr. Chinnock said similar gains were being seen for the first few months of FY 2005. However, regarding the actual revenue collected, the Department of Taxation (Department) was also showing a similar increase; 13.9%. The actual dollar increase in FY 2004 over FY 2003 was \$95 million.

Mr. Chinnock said the Department looked at monthly and annual regression models, as well as confidence limits, both at 95% and 90% and although strong projections were being seen for FY 2005 over FY 2004, based upon testimony received from Global Insight and others, some softening in key areas of collections was being noted. He said the Department was considering the first few months of FY 2005 to show sound gains, even possibly double-digit, but a slowdown was expected after that. As a result, the Department's forecast for the 2% state sales tax was 6% for FY 2005, 5.7% for FY 2006 and 5.4% for FY 2007.

Mr. Chinnock said that the Department followed the logistics model in making its projections. He pointed out that the estimate from the FY 2004 logistics model (page 5 of the handout) the state sales and use tax collections were \$775 million. Considering the historical increases for the prior years, the fact was that between FY 2003 and FY 2004 there was a \$95 million increase. With the forecasts just presented for this forecast cycle of a 6%, 5.7% and 5.4%, that brought the dollar increase to the range to approximately \$49 million.

Mr. Chinnock indicated he was available to respond to questions.

*Bill Anderson, State Budget Office*

Mr. Anderson said the Budget Office's forecast for state sales tax began on page 1 of his handout (Exhibit I). Just as with Global Insight, the forecast of the Budget Office was driven by jobs and employment, as well as factoring in a historical trend. The Budget Office was quite pleased with the results of their forecasts. Looking at the tables on pages 3 and 4, Mr. Anderson said the underlying forecast errors in their approach fall in the low single-digit range. He argued that the Budget Office did a good job forecasting state sales tax except in 2004 but he was uncertain that any forecasting tool existed that could have forecasted 14% growth in the sales tax collections last year, given the overall economic environment of the state.

For the next biennium, Mr. Anderson said the forecast for the Budget Office was shown on page 5. He said he would need to "make a case" to the Forum speaking to the reduction in growth especially in FY 2006. He said in that process, he would be addressing issues that were raised at the last meeting as well. As was pointed out by Chuck Chinnock of the Department of Taxation, one key trend should unfold—once the state reached the large year-ago increases, it would be difficult to grow from there. For example, from January 2005 to June 2005, the Budget Office would be comparing to a year-ago period when the lowest growth rate was 16% so it was questionable how much growth could occur from that point. In fact, with the limited amount of information available for this year, some warning signals were already beginning to surface. Mr. Anderson said the August collections growth fell by approximately 5 percentage points from where it was in July—from 19% to 14%. He said the largest sales tax category, eating and drinking, had declined for four consecutive months and in August only saw 3% growth. Auto growth was stable, but was the lowest in August from the previous nine months.

Mr. Anderson said his forecast for state sales tax was structurally sound and directed the Forum to the charts on page 7 for more historical information. Those charts showed that the state sales tax collection growth was consistent with historical trends in light of the state's expected job growth. Mr. Anderson said he had two points to make regarding the Forum's discussions during the September meeting.

First, he noted that Mr. Fisher had made the observation that it seemed as though the jobs were the leading indicator of sales tax growth and although he would not offer a lecture on correlation coefficients, there were statistical ways to test that. Without getting into details, he advised that there was a much stronger correlation when comparing on a current basis (similar period of time to similar period of time) than if the measurement was done on a leading or lagging basis. Mr.

Anderson said another discussion that occurred at the September meeting was the correlation between job and sales tax growth. He said none of the relationships in any of the forecasts presented were necessarily one-to-one correlations. In looking at the sales tax growth in the past ten years, it had averaged approximately 8% annually and job growth had averaged approximately 5%, with forecasting approaches picking up the difference. Mr. Anderson said he hoped his comments addressed the concerns brought forth at the September meeting.

Continuing, Mr. Anderson said the sales tax collections per job was another structural indicator used by the Budget Office in forecasting and also fell in line with historical trends. After an unprecedented increase in FY 2004, the Budget Office believed sales tax collections would “take a breather” and return to the historical level by the next biennium. As mentioned previously, the Budget Office met with the Governor’s Office about a year ago to look at the upcoming biennium and there seemed to be two issues driving the forecast of the Budget Office—sales tax and the real property transfer tax. He said the best thing he could do for his boss was to provide a number that would not be changing much as the budget was being developed. Mr. Anderson said he would be watching the sales tax numbers on a monthly basis, as well as the real property transfer tax on a quarterly basis to see how those revenue sources unfolded.

Ms. Pierce asked if the Budget Office had a theory about the large increase in FY 2004 in sales tax since it was evident that the increase did not completely correlate to the job and visitor count. In response, Mr. Anderson said much of the increase could be attributed to relatively easy comparisons especially in the second half of the year. He said that was evident in a couple of revenue sources such as on the gaming side as well. Additionally, spring 2003 was a period of considerable uncertainty on the international front. When the Iraq war started in March, a slow-down had occurred, then stronger numbers occurred in spring 2004. During the second half of FY 2004, the lowest growth rate in sales tax collections was 16%, compared to spring 2003. Mr. Anderson related that some pent up demand was present as people tended to stay close to home for a period of time during war and that was reflected not only in the sales tax numbers but other numbers as well.

#### *Russell Guindon, Fiscal Analysis Division*

Mr. Guindon said the Fiscal Division’s projections for state sales tax began on page 18, but he would direct the Forum to page 19 (Exhibit E) which included the tables representing his forecast. He pointed out that the Fiscal Division was the strongest forecaster for state sales tax for all three forecast years.

Mr. Guindon explained that the Fiscal Division forecasted taxable sales through linear regression analysis which was comparable to methods used by the other forecasters. He noted that the equation generating the 9.8% growth in FY 2005, 6.7% growth in FY 2006 and 6% in FY 2007 as shown on the first table on page 19, modeled taxable sales on a quarterly basis as a function of construction employment, which was used as a proxy to capture the construction cycle that occurred. The other variable included in the Fiscal Division’s forecast was Nevada’s total personal income; used in an attempt to capture the local economy effect outside of the construction effect. Lastly, Mr. Guindon related that another variable included in his sales tax forecast was the Las Vegas visitor count. He recognized that using Las Vegas visitors in an attempt to model statewide taxable sales given the magnitude of the Las Vegas market as a percent of the state was what drove the market in taxable sales increases.

Mr. Guindon said that using the above methodology (function of construction employment, Nevada personal income, and Las Vegas visitor count) with the estimated equation resulted in good statistical properties. He explained further that Bob Murdock’s forecast for construction employment, Global Insight’s forecast for Nevada personal income and his own forecast for Las Vegas visitors were used in developing his forecast. Mr. Guindon stated that he also developed alternative forecasting equations such as instead of using personal income he used construction employment and retail trade to help in his forecasting.

In response to Ms. Pierce’s earlier inquiry, Mr. Guindon related that some of the strength being seen in state sales tax was the retail, even though construction was strong as well as the housing sector related to construction. With the various equations, the end result came into the same range. For instance, for the first year of the forecast cycle, using a variable alternative in the equation the forecast came into the 8.6% to 8.9% range instead of the 9.8% range forecast by the Fiscal Division. Then in FY 2006 the alternative equation used resulted in a 6.7-6.9% range which was also in line with what was used. In FY 2007 the alternative equations used were in the 5.9-6.1% range. Mr. Guindon said using the alternative equations provided some comfort because they generated comparable forecasts.

Turning to the table at the bottom of page 19, Mr. Guindon said the growth rates and variables that went into the various equations were presented.

Looking at table 3B, page 40 of the Fiscal Division's handout, Mr. Guindon stated the table reflected the taxable sales per month for the major categories. He noted that the categories listed accounted for 90% of the taxable sales. Mr. Guindon pointed out that strong growth was seen in these categories for the months listed (FY 2004). However, looking at July and August 2004 (FY 2005) compared to those same months one year ago, double digit growth was experienced at that time as well—32% growth in July 2004 and 37% growth in August 2004 for building materials, hardware and garden as compared to 11% one year ago for each of those months.

Mr. Guindon said the auto sales were still somewhat perplexing—that category continued to increase with growth at 13% and 10% in July and August 2004 compared to 15.4% and 18.2% for the same months one year ago. Mr. Guindon said the category of home furniture, furnishings and equipment was no surprise in terms of the new home sales that had been occurring in the state as well as the appreciation of existing home sales. A reported 18% growth in July 2004 and 43% growth in August 2004 occurred in that category, compared to 12% and 13% of one year ago. Looking at total taxable sales, the state was at 14.5% in July 2004 and 11.8% in August, compared to double digits reported from one year ago.

Mr. Guindon provided the Forum with an additional table regarding taxable sales entitled *Growth in Statewide Taxable Sales (Exhibit K)*. He indicated that his forecasts were done on a quarterly basis and the table would imply that growth should occur at 12.2% in the current quarter, which was now up 13% so to hit the 12.2% for the first quarter of FY 2005, only 10% growth was needed in September. Mr. Guindon said the table included historical information on growth of taxable sales from the third quarter of 1996 through the second quarter of 2004, with projected growth shown in outlined bars through 2007. For the second quarter of FY 2005, 13% growth was projected with 8% growth anticipated in the remainder of FY 2005, 6.5-7% range through the rest of FY 2006 with average growth in the 6% range.

In checking state sales tax collections, Mr. Guindon said he looked back to FY 1981 through FY 2004 and over that 24 year period, actual growth in collections averaged 8%. Of those 24 years, only five years had growth of less than 4% and every one of those years included a shock such as 9/11 or a national economic downturn. Looking at the inflation adjusted only 11 years saw inflation-adjusted growth below 4% and five of those 11 years were due to national downturns. Mr. Guindon said he would continue to monitor his projections, especially to see what fallout might occur after the election and the upcoming holiday season.

Mr. Small asked if bonus depreciation was contemplated in the Fiscal Division's forecast regarding business purchases. Mr. Guindon said that was not explicitly in his forecast.

MR. FISHER MOVED TO APPROVE THE DEPARTMENT OF TAXATION'S FORECAST OF A 6.0% INCREASE IN STATE SALES TAX FOR FY 2005, 5.7% FOR FY 2006 AND 5.4% FOR FY 2007.

MR. SEEVERS SECONDED THE MOTION WHICH CARRIED UNANIMOUSLY.

### **REAL PROPERTY TRANSFER TAX**

*Chuck Chinnock, Department of Taxation*

Mr. Chinnock, Department of Taxation (Department) directed the Forum to his presentation, (Exhibit J) and noted a correction on page 2 of his handout. He said the \$1.30 per \$500 of taxable value of real property transfer tax (RPTT) should be \$2.60 per \$1,000 of taxable value. He stated that the RPTT became effective on October 1, 2003 as a result of legislation passed by the 2003 Legislature. The Department reviewed the taxable value of transfers in Nevada from the various counties from prior years and the historical collections of the \$0.55 component. Referring to the backup material attached to his handout, he said it appeared that FY 2004 was an anomaly with respect to the increase of over 60% in taxable value transfers statewide and questioned that amount that had been collected in the first quarter of FY 2004. The Department conducted a logistics trend model on the RPTT and even with the fact they had a high rate of collections for the first quarter of FY 2005, he did not believe it would continue for the entire fiscal year as in FY 2004. In FY 2004, a limited number of units were available for transfer and sale which caused the market prices to hyper-inflate, especially in Las Vegas. He noted that at one time, Las Vegas had 2,000 units on the market and currently had over 12,000 units on the market, which home builders were offering reduced price incentives to purchase their new homes.

Directing the Forum to page 15 of his handout, Mr. Chinnock said the chart showed projections made to the RPTT. Moving to page 16, the chart showed the logistic trend model with respect to the RPTT and the historical taxable value beginning in

1996 through 2004. In 2004, the chart showed a dramatic jump to \$43.4 billion but he did not believe that would continue in the future. Mr. Chinnock said his estimated taxable revenue projections for RPTT were \$38.6 billion in FY 2005, \$44.8 billion in FY 2006 and \$51.8 billion in FY 2007.

Continuing, Mr. Chinnock said he applied the rate of \$.55 per \$500 to the taxable value which resulted in \$100.5 million for FY 2005, \$116.4 million for FY 2006 and \$134.7 million for FY 2007. He noted that counties over 400,000 were given a .2% collection allowance and counties with less than 400,000 were given a 1% collection allowance and the numbers reflected the adjustment for collection allowances.

Mr. Martin asked if the projections were broken down between resale and new homes because many people were critical of the reductions in home sales. He was not sure the reductions totally reflected the market and even though some incentives were available, sales were still strong and prices were not expected to drop much. Mr. Chinnock responded said the Department of Taxation did not take that into account but he was sure that Budget and Fiscal took a different approach and looked at other specific indicators.

Responding to a question from Mr. Fisher, Mr. Chinnock said the Department believed that the \$43 billion of RPTT was a spike and the state would see \$38 billion in estimated revenue in the future so they started their projection at \$38 billion and worked up from that point. Mr. Fisher asked if that was based on taxable value not the tax rate. Mr. Chinnock replied that it was based on taxable value.

*Bill Anderson, State Budget Office*

Mr. Anderson stated RPTT was more difficult to forecast than the LET. Since only three quarterly collections had been reported to date, not much historical information was available to produce a forecast. He noted that the Budget Office identified a historical series of RPTT collections and had reported collections based upon a \$0.55 levy on an identical tax base available from the Department of Taxation. Monthly information was available from mid-1998 forward and the Budget Office's outlook utilized historical trends evident in the county tax collections, in conjunction with initial collections of the tax at the state level in generating a forecast.

Directing the Forum to page 36 on his handout, (Exhibit I), Mr. Anderson said collections from the \$0.55 transfer tax at the county level, aggregated up to the state level from 1998 through early 2003 showed a steady growth rate of approximately 12.6% on an average annual basis which was factored into the Budget forecast. The graph on page 36 of his handout showed signs of the "bubble" that took place in the real estate market. He stated that the Budget Office had to feel comfortable with the fact that the \$0.55 levy at the county level was against the identical tax base at the \$1.30 levy and for the three-quarters where there were state collections with the tax and taking the similar collections at the county level and inflating it to the \$1.30 tax rate would result in an identical outcome. With that, the historical information could be inflated up to the \$1.30 level and resulted in a consistent series over time. Moving to the graph on page 37 of his presentation, Mr. Anderson stated the data was annualized reflecting some sign of an abnormally large uptick in FY 2003 and FY 2004.

Moving to the graph on page 38 of his handout, Mr. Anderson said the Budget Office wanted to make sure they had an understanding of the "so-called" real estate bubble; when it started, how big it was and the fiscal impacts. The top chart on page 38 helped identify when the bubble started and showed year-over-year growth in RPTT collections. He settled on the fourth quarter of 2002 as the beginning of the real estate bubble in Nevada. He noted it was peaking in the second quarter of 2004 and as Mr. Chinnock stated, there was approximately \$35 million in that account based upon the most recent collections and it eased off considerably from the prior quarter. However, the state was seeing signs that growth was starting to moderate. He noted the fiscal impact of the bubble was shown at the bottom of page 38 of his handout and if the tax had been in place the last several years, the bubble probably would have generated approximately \$47 million more than it would have if they followed the historical trend. The forecast was presented on page 39 of his handout with approximately \$116.7 million in FY 2005, \$121 million in FY 2006 and \$137 million in FY 2007. He said the 32.6% growth rate was obviously inflated because it compared back to a year-ago period in 2004 with only three-quarterly collections. Mr. Anderson noted that if three quarterly collections were adjusted on an annualized basis, the \$116 million projection represented only 4.2% growth which indicated the bubble was starting to correct itself and the correction would take place into 2006 and return to the normal 12.6% growth rate in 2007.

Finally, the chart on page 40 of his handout showed how he generated the specific forecast. Mr. Anderson said he started his forecast by identifying an "upper" and a "lower" range of possible values and adopted a "middle-of-the-road" approach which incorporated a partial reversal of the bubble's impacts. He noted the lightly shaded bars on the graph showed the FY 2005, FY 2006 and FY 2007 collections if historical trends were followed. He said the white bars on the graph showed what would happen if there was no correction to the bubble and grew at the historical 12.6% growth rate.

Concluding, Mr. Anderson said that was how the Budget Office conducted their forecast and he believed it was reasonable in light of his understanding of the real estate market.

Ms. Pierce commented that Global Insight was projecting that housing starts in Nevada were going to decrease 7.5% in FY 2005 and 5.2% in FY 2006. She wondered how housing starts really correlated with the RPTT because the tax also incorporated resale homes, and if there was a correlation, it seemed that projecting a 4.2% overall increase when the state only collected three-quarters worth of tax in FY 2004 seemed optimistic. She did not think Global Insight's forecast of a 7.5% decrease in housing starts in 2005 was unrealistic.

Responding, Mr. Anderson said housing starts would have an impact on the RPTT and there was a correlation but the end result was that the tax was levied against the value of the starts once the houses were sold. In the Budget Office forecast, moderation was seen and was growing at 4% in FY 2005 and 3.9% in FY 2006. He stated the downturn was expected and housing starts were just one component of that. Against that backdrop, the population was still growing at 4% to 5% a year and it had to be put in the context of the overall environment. To the extent that the housing start information presented by Global Insight pointed to moderation; he believed it was reflected in the Budget forecast.

Mr. Chinnock added that housing starts did impact RPTT but a major component of the RPTT was the amount of property transferred and the value of property transferred. He said the Department was concerned that the value would flatten out and housing starts were lowering with population growth. So, the Department decided to be conservative and accept the fact that the amount of property that was actually going to be transferred would also be reduced.

Ms. Pierce stated that the Department of Taxation's projections were more conservative and actually showed a slight decline when the tax was annualized yet Global Insight was not projecting a decrease in housing prices in Nevada.

Mr. Martin believed the relationship between resale homes and new homes was due to speculators who would "flip" a house a few weeks after purchase which double counted in the projections, cut taxes to new houses and showed up as a resale. He believed the 15,000 houses on the market were still many of the speculator houses. He stated he was more bearish on the number because of the bubble created by such an artificial greed-driven factor as opposed to people moving to a house to reside for five or more years. He agreed that even if housing starts were down 7.5%, he believed the houses would eventually increase to 7.5% to neutralize the number.

*Russell Guindon, Fiscal Analysis Division*

Mr. Guindon reiterated earlier comments that the RPTT was a difficult tax to forecast because agencies did not know how much of the revenue was generated by "flips" or repeat sales, how much was new, how much was on existing residential, and the application to commercial sales. In addition, he noted that if a commercial was similar to a stock transfer, it would not be subject to the RPTT. The Fiscal Division looked at some of the same data used by the other agencies and collected historical information from the Southern Nevada Home Builders Association and the National Association of Realtors to get an idea of the current situation so assumptions could be made.

Mr. Guindon said the taxable amount generated from the RPTT was a preliminary forecast and a "work in progress." He pointed out the table on page 29 of his handout, ([Exhibit E](#)), contained the RPTT forecast methodology and included a forecast produced by Global Insight. As part of the contract with Global Insight, they provided historical information on the median price of existing and new residential single-family home sales and projected out the housing starts and existing single-family home sales.

Directing the Forum to page 29, Mr. Guindon said that column A on the chart provided the estimated single-family new home sales and he took the start number that Global Insight had projected and the value from three-quarters prior, assuming that it took nine months for a start to become a house, and converted it to a home sale. Looking at the national and state data that was available, it did not look like every start became a sale so he assumed 80% of the starts became new homes. Column B of the chart showed the average new single-family home price per Global Insight. Mr. Guindon said the average price of homes was derived by multiplying the median price by a factor of 1.2 as reached by limited Nevada and other western states data. Column C showed the existing single-family home sales which was the value that was forecast by Global Insight. Column D was the existing single-family home price and again the 1.2 factor was used to convert the median value to an average. Column E showed the estimated value of new and existing single-family homes which was the potential taxable base for the RPTT. Taking the information from Column E and multiplying by \$1.30 per \$500 of value to get the implied general fund RPTT collections from single-family homes shown in Column F.



Comparing Column F, the imputed amount generated from single-family home sales, to Column G, the actual amount collected from all types of sales, provides a number indicating the factor necessary to convert the estimate of collections from single-family transactions into a collection amount representing all types of transactions, multi-family, commercial and land sales. Multiplying Fiscal Division's estimate of RPTT collections generated from the forecast of taxable activity from single-family home sales by the 1.335 factor produced the forecast of total RPTT collections generated for each quarter of the forecast period.

Concluding, Mr. Guindon explained that Column I was Fiscal Division's forecast of the amount of revenue generated from the RPTT that would go into the state general fund. Fiscal Division's forecast for RPTT collections was approximately \$134 million in FY 2005, approximately \$124 million in FY 2006 and approximately \$123 million in FY 2007. He said the projections for the RPTT were declining because home sales were included which was the imputation from Global Insight's information that sales for new single-family homes will fall in FY 2006 and FY 2007 but the new single-family home price went up 2.4% and was flat in FY 2007. He noted the latest October 2004 projections declined 8.2% in FY 2006 and 2.1% in FY 2007 for existing single-family home sales.

He concluded that the table on page 29 of the handout presented Fiscal Division's forecasts of the amount of revenue generated from the RPTT using the above methodology based on Global Insight's October 2004 forecast.

Ms. Pierce said she was lost in the translation of how \$98.981 million went to \$134 million; realizing \$98.981 million was only single-family homes and \$134 million included all factors. Mr. Guindon said it was implied because he was able to forecast using Global Insight's projections, the single-family home sales but actual collections were also available for four quarters so the ratio for those four quarters of the actual compared to what was collected from single-family sales could be used with the 1.335 ratio when forecasting by multiplying it by 1.335 to obtain the implied amount generated from land, commercial and multi-family sales.

Ms. Pierce said she appreciated the logic but it seemed to come up with an overly optimistic answer and she was not sure where the logic fault was coming from.

Mr. Martin was confused with the charts in Fiscal Division's handout and asked if the 7.36 estimated new single-family home sales in FY 2005 was for each quarter. Mr. Guindon responded that was the average over the four quarters for that year.

Mr. Martin asked if the apartment conversions to condominiums would drop the value average median price. Mr. Guindon replied that he would be looking at the many different factors in November in an attempt to better understand the RPTT. He reiterated it was a difficult task to forecast and lacked good information on many of the factors involved.

Mr. Fisher commented that he was persuaded by Fiscal Division's approach. He informed the Forum that he had been a real estate broker for 14 years and prices might pull back and be flat, but the bottom does not fall out on housing prices. The structural activity and the speculative activity were driving the pricing bubble and speculative activity was eliminated from the forecast which persuaded him to go with Fiscal's approach.

MR. FISHER MOVED TO ACCEPT FISCAL DIVISION'S ESTIMATES FOR THE REAL PROPERTY TRANSFER TAX OF \$134 MILLION IN FY 2005, \$124 MILLION IN FY 2006 AND \$123 MILLION IN FY 2007.

Chairman Small asked if there was a second.

THE MOTION FAILED DUE TO A LACK OF A SECOND.

Chairman Small asked if there was another motion.

MS. PIERCE MOVED TO ACCEPT THE AGENCY FORECAST.

Chairman Small asked if there was a second to the motion.

THE MOTION FAILED DUE TO A LACK OF A SECOND.

Chairman Small commented that the last column on page 29 of the Fiscal Division's handout combined all the numbers together and showed which forecast in the long run might be higher or lower. Mr. Fisher commented that the Fiscal Division estimate was \$4 million lower than the agency on the combined estimates for the biennium.

MR. FISHER MOVED TO ACCEPT FISCAL DIVISION'S ESTIMATES OF THE REAL PROPERTY

## TRANSFER TAX.

THE MOTION FAILED DUE TO A LACK OF A SECOND.

Ms. Pierce expressed concern for the FY 2005 forecast from the Fiscal Division.

MS. PIERCE MOVED TO ACCEPT THE BUDGET DIVISION'S FORECAST OF 32.6% FOR FY 2005, 3.9% FOR FY 2006 WITH A 10% INCREASE FOR FY 2007.

MR. SEEVERS SECONDED THE MOTION, WHICH CARRIED UNANIMOUSLY.

Mr. Fisher asked what the number was with the 10% increase. Chairman Small indicated that a vote was already taken and the motion carried.

## **INSURANCE PREMIUM TAX**

*Lynne Knack, Department of Taxation*

Ms. Knack, Department of Taxation (Department) commented that the insurance premium tax for FY 2004 collections was \$194 million versus approximately \$174 million for FY 2003 representing a \$20 million gain or 11.6% increase over the previous year. The Department projected this tax by use of linear regression analysis which indicated a 9.8% growth for FY 2005, 9.5% growth for FY 2006 and 9.3% growth for FY 2007. The Department also looked at several factors to test the reasonableness of this result. The average increase in the insurance premium tax over the last five to six years was approximately 9.8% to 10.7%.

Ms. Knack stated that the four quarterly payments in the annual true up account for 92% of the tax collected. The only other component that could have an affect was the premium tax on industrial insurance. Currently, the Division of Industrial Relations (DIR) provides for an assessment against companies for which they are allowed a credit against the premium tax normally owed on industrial insurance. A 33% decrease occurred between FY 2003 and FY 2004 in the tax paid on industrial insurance premiums (from \$7 million to \$4.7 million). Most of the insurance companies were carrying credits in overpaid assessments to DIR and therefore would not be liable for the tax. At the end of FY 2004 there was approximately \$25 million in credit still available to insurance companies that had not been taken. Ms. Knack said the tax paid for insurance premiums on industrial insurance would still remain between the \$4 million to \$5.5 million range and was expected to have an affect, whether it was an increase or decrease, of approximately 1% to 1.5%. The Department projected a 9.8% increase, approximately \$213 million in FY 2005, 9.5% increase for FY 2006, or \$234 million and a 9.3% increase in FY 2007 for approximately \$255 million.

*Bill Anderson, State Budget Office*

Mr. Anderson said the Budget Office forecasted between 10.5% to 11% growth in insurance premium tax collections for FY 2005, FY 2006 and FY 2007 and the forecast was driven by their forecast of real personal income. He noted that his forecast may seem high but historically every forecast presented came in too low and in five of the past seven years these collections had come in above 10% so there was the precedence for this type of growth.

*Mark Stevens, Fiscal Analysis Division*

Mr. Stevens directed the Forum to page 21 of the Fiscal Division's handout (Exhibit E), which outlined the last five years of growth in the insurance premium tax excluding the workers compensation line of insurance. He stated the Fiscal Division looked at all lines of insurance except workers compensation for the growth rate in the insurance premium tax and during that five-year period, the average growth was 10.2%. Removing the lowest and highest years, the average growth rate for that five-year period was 10.2%. He stated that the Fiscal Division chose a base growth rate of 10% for FY 2005, FY 2006 and FY 2007. He noted the revenue generated from the workers compensation insurance was \$7 million in FY 2003, \$4.7 million in FY 2004 and there were credits for workers' compensation insurers based on assessments paid for DIR expenses. Those credits had gone up every year and in June 2002 the credits were \$16.1 million. In June 2004 the credits were \$26 million which was over 10% of this revenue source on an annual basis that had built up credits that could be taken by insurers in the future. The Fiscal Division left the workers compensation portion of this tax flat in each year of the biennium; \$4.7 million which would drive the growth rate down somewhat. Mr. Stevens said the Fiscal Division was projecting \$212.9 million in FY 2005, a 9.6% increase, \$234 million in FY 2006 a 9.9% increase and \$256.9 million in FY 2007, a 9.8% increase.

Chairman Small asked for a motion on the insurance premium tax.

MR. SEEVERS MOVED TO ACCEPT FISCAL DIVISION'S FORECAST OF A 9.6% INCREASE IN FY 2005, 9.9% IN FY 2006 AND 9.8% IN FY 2007 FOR THE INSURANCE PREMIUM TAX.

MS. PIERCE SECONDED THE MOTION, WHICH CARRIED UNANIMOUSLY.

### **CIGARETTE TAX**

*Lynne Knack, Department of Taxation*

Ms. Knack stated that the general fund portion of the cigarette tax rate was increased effective August 1, 2003 by the 2003 Legislature from \$.25 per package to \$.70 per package. Due to the cigarette wholesalers anticipating the tax increase, they stockpiled their purchases of cigarette tax stamps for a few months prior to the rate increase. Although stamp sales were down by 18% in FY 2004, the Department collected approximately \$107 million or 99% of what the Legislature determined the revenue would be for FY 2004. A factor that had affected the cigarette tax collections in the past was the continued decline in per capita consumption not only nationally but in Nevada which averaged nationally 1.5% to 2% per year over the last ten years.

Ms. Knack indicated that another major factor was the interstate purchase of cigarettes by individuals from bordering states with a higher tax than Nevada. Nevada experienced moderate tax increases in the past because of that but eventually hit the saturation point.

Continuing, Ms. Knack said another factor affecting Nevada was as the taxes were increased, the sale of illegally stamped or contraband cigarettes also increased to avoid the tax. Although the Department performed a regression analysis that resulted in basically a flat rate to approximately a 1% to 2% decrease in the revenue for each year, they submitted their projections as essentially flat for all the three forecasting years. The Department annualized FY 2004 actual collections by eliminating the months with extremely low stamp purchases and recalculated an average collection per month. In addition, the Department made a one-time adjustment for a payment of cigarette tax that was owed of approximately \$1.6 million on a bankruptcy payment that was made in FY 2004. As a result, the Department recalculated the cigarette tax collections to be approximately \$117 million in FY 2005 and flat for FY 2006 and FY 2007.

Chairman Small asked if cigarette sales were flat over the last few years. Ms. Knack replied that consumption had been going down nationally and for awhile the state had one of the lower tax rates compared to the five surrounding states so the state was seeing a small influx of interstate purchases by individuals coming into Nevada and buying cigarettes which resulted in a 2.5% increase in tax collections. Currently, that had reached a saturation point and everything should be flat or a slight reduction in sales. She noted an increase will be seen in FY 2004 because of the annualization of the tax and there was only 11 months in FY 2004 versus a full-year realization of that rate.

*Bill Anderson, State Budget Office*

Mr. Anderson directed the Forum to the chart on page 42 of his handout and said in terms of recent consumption of taxable packages of cigarettes, the chart showed that over the course of the last half year the number of taxable packages sold had settled in month after month at approximately 14 million packages per month and it smoothed out over the course of a three-month moving average. The Budget Office was comfortable settling at 14 million packages per month at a steady tax yield of approximately of \$.70 a pack which resulted in \$117.6 million in collections. He noted the Budget Office was comfortable holding that level steady over the course of the next biennium.

*Russell Guindon, Fiscal Analysis Division*

Turning to page 31 of the handout, (Exhibit E), Mr. Guindon noted the chart showed the cigarette tax forecast and he made assumptions about the average number of packs per month for each of the three fiscal years. The estimates of the average number of packs per fiscal year were based on an analysis of the recent post-tax increase average number of packs per month and also incorporated information on the projected population growth and expected number of visitors to Las Vegas over the next three fiscal years. The chart showed that August 2003 had an increase due to the pre-loading before the tax and then it fell off and he annualized against that which was why he projected an increase in FY 2005, FY 2006 and FY 2006. He said the forecast was at the 14 million mark in terms of packs sold. He noted there was slight growth because of what he assumed for visitor and population growth and once the tax increase worked out into a new equilibrium, there would be growth in packs sold.

MR. SEEVERS MOVED TO ACCEPT THE BUDGET OFFICE FORECAST FOR CIGARETTE TAX OF \$117.6 MILLION IN COLLECTIONS FOR FY 2005, FY 2006 AND FY 2007.

MR. MARTIN SECONDED THE MOTION, WHICH CARRIED UNANIMOUSLY.

### **MODIFIED BUSINESS TAX**

*Lynne Knack, Department of Taxation*

Ms. Knack explained the modified business tax (MBT) became effective October 1, 2003 by the 2003 Legislature and was reported quarterly on the total taxable wages paid by an employer less health care benefits paid by the employer on behalf of his employees. The MBT replaced what was known as the business license tax which was repealed at the same time the MBT became effective. The MBT applied to general businesses at a rate in FY 2004 of .7% through June 30 of FY 2004 and was reduced by statute July 1, 2004 to .65%. In addition, a tax rate of 2% was applied to the taxable wages less health care benefits on financial institutions. Three-quarters of the modified business tax was reported for FY 2004 and the average amount of wages reported per quarter was \$7.8 billion and the average health care deductions were approximately \$562 million per quarter. The industries reporting the higher wage and health care costs in Nevada were the casino hotels, corporate, subsidiary and regional managing offices, physicians, full-service restaurants and new car dealers. The Department developed their revenue projections by annualizing the average wages and health care deductions for each of the components; general business and financial reporting to determine an adjusted FY 2004 base. Tax was calculated at the new rate of .65% for general businesses and 2% for financial institutions. The adjusted base was increased by Employment Security Division's (ESD) projected job growth rate to be 4.4% for FY 2005, 3.8% for FY 2006 and 3.9% for FY 2004. The Department estimated the yield to be approximately \$223 million for FY 2005, \$221 million for FY 2006 and \$230 million for FY 2007.

*Bill Anderson, State Budget Office*

Mr. Anderson directed the Forum to page 25 of his handout and said the forecast was driven by job growth, expected wage inflation and the rate adjustment. The chart on page 26 showed the collections for the first quarter on a per job basis which worked out to be approximately \$49 per economy wide jobs, not just jobs impacted by the tax collection. In addition, wage inflation was factored into the forecast and year-after-year an increase in the average wage structure in Nevada was about 3% annually. Mr. Anderson said the forecast was presented numerically on page 27 of his handout and showed a 6.9% growth in FY 2006 and 7.1% growth in FY 2007. The chart on page 29 contained the components of the MBT forecast with the forecast being split into a base forecast amount with job growth and the state continuing to collect \$49 per job per quarter. The inflation component took into account the 3% year-after-year inflation in the underlying wage structure and was offset in the current year and into the next biennium slightly by a reduction in the tax rate. Beginning in FY 2005, the tax rate will be lowered from .7% to .65% on non-financial institutions.

*Russell Guindon, Fiscal Analysis Division*

Mr. Guindon requested that the Forum produce forecasts for the financial and non-financial pieces of the MBT because the Fiscal Division had a different perspective on MBT than the Budget Office and Department of Taxation. During the 2003 Legislative Session and the 20<sup>th</sup> Special Session there was much deliberation and discussion with regards to having a tax that specifically identified just the financial industry. When the Legislature decided to make the decision for the MBT, they broke it into a non-financial piece which was the .65% rate and also imposed a 2% rate on financial institutions. He noted his responsibility to the Legislature was to forecast each of those pieces separately because bill draft requests (BDR) requesting changes to those taxes were proposed for the 2005 Legislative Session. In addition, he was staffing an interim committee which made a recommendation to change the way financial institutions were defined. He said historically most of the legislatively approved changes to taxes were tied to the Forum forecast. Mr. Guindon stated that if all he had was a forecast of the total, he would not have the ability to tie the changes to the financial or the non-financial portion.

Mr. Guindon reiterated it was important for the Fiscal Division to have both forecasts so that was why he presented them separately in his forecast. He noted that in his haste to get the numbers from the Department of Taxation for the meeting packet he only received the total amount but Ms. Knack has indicated to him that separate forecasts were prepared for the financial and non-financial pieces. Mr. Guindon said since these were preliminary forecasts, a total amount could be

forecasted by the Forum, but he would be requesting a forecast of the financial and non-financial taxes separately at the December meeting.

Chairman Small said the request seemed reasonable and he would request a forecast for the financial and non-financial portion from the Budget Office for the December meeting.

Mr. Guindon directed the Forum to Table 1 and Table 2, page 25 and 26, respectively, of his handout which presented the forecasts for the MBT collections for the non-financial and financial institutions taxes for FY 2005, FY 2006, and FY 2007 on a quarterly and fiscal year basis. The Fiscal Division prepared the forecasts for the non-financial portion of the MBT by using the actual non-government wage and salary disbursements reported by the Bureau of Economic Analysis (BEA) and the projections for this series provided by Global Insight. Mr. Guindon pointed out that he was using the non-government wages because the government sector is not subject to the MBT on non-financial institutions. The ratio of the wages reported by the Department of Taxation for the MBT non-financial tax were compared to the actual wages reported by BEA for non-government employees on a quarterly basis. Mr. Guindon pointed out that Column C of Table 1 presented this ratio for the three quarters of actual data for which the comparison can be made. As shown in the table, the average ratio of Taxation's wages to BEA's reported wages over these three quarters was 81.5% and this is the ratio used by the Fiscal Division to translate Global Insight's wage projections into taxable wages for the purposes of the MBT on non-financial institutions.

Mr. Guindon next referred the Forum to Column D of Table 1 which presented the health care deductions as a percent of the reported wages. Over the three actual quarters for which information is available, the average ratio of health care deduction to wages was 7.3%. For each quarter of the forecast horizon, the ratio of 7.3% was used to determine the amount of the health care credit shown in Column E.

Subtracting the health care credit amount from the projection for wages provides an estimate of the net wages to which the 0.65% tax rate can be applied. This provides an estimate of the amount of taxes generated from the MBT on non-financial institutions for each quarter of the forecast period.

Mr. Guindon then referred the Forum to Table 2 which presented Fiscal Division's forecast for the MBT on financial institutions. He stated the same general methodology was used but the BEA wage base used was for the financial institutions sector. Using Global Insight's projections for wages for the financial institutions sector, an estimate of wages could be produced using the same ratio analysis developed for the MBT on non-financial institutions. Mr. Guindon pointed out that he felt it was important to use the wage base applicable to both the non-financial and financial institutions portions of the MBT because the underlying growth in each tax base may be different between the two taxes. Although the level of health care provided to employees in non-financial versus financial businesses may differ making the amount of the health care credit differ between the two taxes.

Concluding, Mr. Guindon said the financial and non-financial taxes were two taxes with different bases and rates and could potentially have different health care credits.

Chairman Small asked for a motion for the total preliminary forecast for the MBT for FY 2005, FY 2006 and FY 2007.

MS. PIERCE MOVED TO ACCEPT FISCAL DIVISION'S FORECAST FOR THE MODIFIED BUSINESS TAX OF 34.9% FOR FY 2005, 6.7% FOR FY 2006 AND 6.5% FOR FY 2007.

MR. SEEVERS SECONDED THE MOTION, WHICH CARRIED

UNANIMOUSLY.

**VI. Review and Approval of Preliminary Forecasts of Minor General Fund Revenues for FY 2005, FY 2006 and FY 2007 Approved by the Technical Advisory Committee at its October 27, 2004 Meeting.**

Mr. Guindon indicated that Table 5, behind Tab VI of the meeting packet, (Exhibit C), page 93 provided the minor revenue forecasts from the Technical Advisory Committee (TAC). He noted that since the forecasts were similar, the TAC generally accepted the agency's forecast; the largest difference in the forecasts was the net proceeds of minerals tax. He noted that Table 6, page 95 of the meeting packet would be used for the consensus forecast of the Forum for the major revenue sources and included the TAC forecasts for the minor revenues.

Mr. Guindon stated the Forum needed to approve the consensus forecast.

MR. FISHER MOVED TO APPROVE THE MINOR REVENUES  
TECHNICAL ADVISORY COMMITTEE.

FORECASTS PREPARED BY THE

MR. MARTIN SECONDED THE MOTION, WHICH CARRIED UNANIMOUSLY.

**VII. Instructions to Technical Advisory Committee Concerning the Next Meeting.**

Mr. Guindon noted that the TAC would meet again in November to produce and approve the final set of minor revenue forecasts which included the LET non-gaming. In addition, staff from the Budget Office and Fiscal Division were working on a list of outside reviewers and would send a joint letter requesting a forecast for the December 1, 2004 meeting. Also, staff was working on the request from Ms. Pierce for information on the potential impact of Indian gaming to Nevada.

Chairman Small asked if there were any questions. He commented that at the next meeting he wanted to mainly focus on any substantial changes to the preliminary forecast and did not think that each agency or department needed to repeat the process of how they arrived at their forecast. He noted that the Forum would have time to review the preliminary forecasts before the next meeting and any additional questions could be discussed at that time.

Mr. Guindon indicated there would not be any outside presenters at the next meeting. He noted the Forum members would have tables in advance to review and could update the impact of any additional information provided on the base year forecast at the December 1<sup>st</sup> meeting.

Chairman Small thanked staff for the detailed information and time they provided in their forecasts.

Mr. Fisher asked if Global Insight would provide an update at the next meeting. Responding, Mr. Guindon said he would provide an executive summary from Global Insight and a table of the Nevada forecast from Mr. Diffley at the next meeting.

Chairman Small asked if Global Insight could provide information on how their projections had compared to actual results in the past since two of the revenue sources Global Insight forecasted were significantly different from the other forecasts. He believed that information would be helpful in case the Forum chose to move in a different direction or pursue other options.

Mr. Guindon said he presented a table at a prior meeting that compared Global Insight's forecast and could update the sales tax and percentage fees portion for the next meeting. He added that the other categories were problematic to compare because if any of the taxes were repealed or changed, it affected the forecast comparison.

**VIII. Public Testimony**

There was no public testimony.

**IX. Adjournment**

Chairman Small adjourned the meeting at 1:43 p.m.

Submitted by:

\_\_\_\_\_  
Donna Thomas, Committee Secretary

Approved by:

\_\_\_\_\_  
Michael Small, Chairman

\_\_\_\_\_  
Date