

TREASURE STATE ENDOWMENT REGIONAL WATER SYSTEM TRUST FUND INTEREST

Revenue Description

Article IX, Section 5 of the Montana Constitution established a permanent trust fund into which at least half of coal severance tax revenue must be deposited. The trust fund is divided into several funds with different purposes. Income from the treasure state endowment regional water system trust fund is to be used for regional water systems.

Projected Revenue

Table 1 shows actual interest earnings for the treasure state endowment regional water system trust fund from FY 2001 through FY 2004 and projections for FY 2005 through FY 2007.

Table 1		
Treasure State Endowment Water System Fund Interest		
(\$ millions)		
<u>Fiscal Year</u>	<u>Interest Earnings</u>	<u>Percent Change</u>
A 2001	\$0.370	NA
A 2002	\$0.640	72.99%
A 2003	\$0.893	39.45%
A 2004	\$1.199	34.25%
F 2005	\$1.469	22.55%
F 2006	\$1.539	4.79%
F 2007	\$1.775	15.28%

Fiscal Year	Interest Earnings (\$ millions)
2001	0.370
2002	0.640
2003	0.893
2004	1.199
2005	1.469
2006	1.539
2007	1.775

Earnings grew from FY 2001 through FY 2004, generally through increasing balances due to contributions from the coal tax. Income in FY 2005 is projected to be higher due to expected capital gains distributions. Decreasing yields due to the replacement of older, high coupon bonds with newer low coupon bonds is expected to dampen interest earnings growth from FY 2005 through FY 2007. Interest earnings are projected to increase through FY 2007 due to the projected rise in the average fund balance.

Forecast Methodology and Projection Calculation

There are five steps to forecasting revenue from the trust fund. First, the average monthly balance of the fund must be projected. Second, this balance is allocated to the two basic types of investment made by the fund. Third, monthly yields are projected for each type of investment. Fourth, the balances for each investment type are multiplied by their respective yields to find monthly interest income. Finally, the twelve months of income are summed to estimate annual interest income. This write-up shows annual totals for each of the steps.

Treasure State Endowment Regional Water System Trust Fund Balance

Half of coal severance tax receipts are deposited in the coal tax trust funds. Beginning in FY 2004, 12.5% of collections are to be deposited in the permanent fund, 25% in the treasure state endowment trust fund, and 12.5% in the treasure state endowment regional water system trust fund (17-5-703, MCA).

Table 2 shows actual coal severance tax receipts and deposits to the components of the coal tax trust fund for FY 2003 and FY 2004 and projections for FY 2005 through FY 2007.

Table 2				
Coal Severance Tax Revenue and Trust Fund Deposits				
(\$ millions)				
Fiscal Year	Severance Tax	Permanent Fund	Treasure State Endowment	Regional Water System Fund
A 2003	\$31.789	\$0.000	\$10.702	\$3.567
A 2004	\$31.371	\$3.336	\$6.672	\$3.336
F 2005	\$35.920	\$4.490	\$8.980	\$4.490
F 2006	\$31.986	\$3.998	\$7.996	\$3.998
F 2007	\$30.865	\$3.858	\$7.716	\$3.858

Coal severance tax is collected quarterly, and the average balance of one of the trusts during a fiscal year equals the beginning balance plus the quarterly deposits, each multiplied by the fraction of the year remaining when the deposit is made. If the deposits are of equal size, the increase in the average balance is 3/8 of the sum of the deposits ($3/8 = 1/4 \times 3/4 + 1/4 \times 1/2 + 1/4 \times 1/4 + 1/4 \times 0$).

Table 3 shows actual treasure state endowment regional water system trust fund average balances for FY 2001 through FY 2004 and projections for FY 2005 through FY 2007.

Table 3 Regional Water System Fund Balance (\$ millions)	
-----Regional Water System-----	
Fiscal Year	Average Balance
A 2001	\$5.130
A 2002	\$9.033
A 2003	\$12.806
A 2004	\$16.810
F 2005	\$20.696
F 2006	\$24.946
F 2007	\$28.830

Annual Trust Fund Yields

The Montana Board of Investments manages the treasure state regional water system fund. The Board of Investments invests trust fund balances in two mutual funds that it manages, the Trust Funds Bond Pool (TFBP) and the Short Term Investment Pool (STIP). The forecasts of the annual yields of these mutual funds are explained in the Interest Earnings Introduction. Payouts on TFPB and STIP are made from the Board of Investments proportional to end-of-month balances in those accounts.

On average from October 2003 through September 2004, the Treasure State Endowment Regional Water System trust fund has been invested 97.91% in TFPB and 2.09% in STIP. The forecast assumes that these percentages will continue to hold through FY 2007.

Treasure State Endowment Regional Water Trust Fund Interest

Table 4 shows the annual average balance, interest earnings, and derived annual yield for FY 2004 through FY 2007. Forecast yield is higher in FY 2005 largely because of substantial expected capital gains in the Trust Fund Bond Pool. Annual yield is expected to decline in FY 2006 and FY 2007 due to decreasing average coupon rates in the same pool. Projected increases in earnings through FY 2007 are driven primarily by projected increases in the average balance.

Table 4 Regional Water System Fund Projected Interest Earnings					
-----Regional Water System Fund-----					
Fiscal Year	Average Balance (\$ millions)		Interest Earnings (\$ millions)		Derived Annual % Yield
A 2004	\$16.810	x	\$1.178	=	7.01%
F 2005	\$20.696	x	\$1.469	=	7.10%
F 2006	\$24.946	x	\$1.539	=	6.17%
F 2007	\$28.830	x	\$1.775	=	6.16%