

TOBACCO SETTLEMENT TRUST INTEREST

Revenue Description

Montana receives payments from a multi-state settlement with tobacco companies. Forty percent of the receipts from this settlement are deposited in the tobacco settlement trust. Ten percent of interest earnings from this trust fund are retained in the trust and 90% are deposited in a special revenue account and may be appropriated by the Legislature for tobacco prevention and health care programs (17-6-603, MCA).

Historical and Projected Revenue

The tobacco settlement trust was established in January 2001 following passage of Constitutional Amendment 35 in the November 2000 election. Table 1 shows actual distributable interest for FY 2001 through FY 2006 and forecast distributable interest for FY 2007 through FY 2009. Distributable interest is the portion of tobacco trust interest that is not retained by the trust.

Table 1 Tobacco Settlement Trust Distributable Interest (\$ millions)		
Fiscal Year	Interest Revenue	Percent change
A 2001	\$0.071	N/A
A 2002	\$1.015	1326.69%
A 2003	\$1.647	62.22%
A 2004	\$2.403	45.88%
A 2005	\$2.882	19.95%
A 2006	\$3.049	5.78%
F 2007	\$3.731	22.39%
F 2008	\$4.222	13.16%
F 2009	\$4.758	12.68%

Tobacco Trust Interest

Fiscal Year	Interest Earnings (\$ millions)
2001	0.071
2002	1.015
2003	1.647
2004	2.403
2005	2.882
2006	3.049
2007	3.731
2008	4.222
2009	4.758

Tobacco trust interest revenue is growing rapidly because the trust fund balance is growing with the settlement payments made each year. Interest revenue is forecast to be \$3.731 million in FY 2007, \$4.222 million in FY 2008, and \$4.758 million in FY 2009.

Forecast Methodology and Projection Calculation

There are three steps to forecasting interest revenue from the tobacco trust fund.

1. The annual average balance of the fund is projected.
2. The annual average balance by investment type is projected.
3. Interest earnings are forecast by multiplying the balance by the interest rate.

Tobacco Trust Fund Balance

The fund balance increases yearly as 40% of the tobacco settlement payments and 10% of the interest earned on the fund balance are deposited into the trust fund.

Table 2 shows the actual and projected average fund balance, tobacco settlement deposits, retained interest earnings, and total fund deposits from FY 2001 through FY 2009.

The average fund balance is projected to be \$70.988 million in FY 2007, \$82.528 million in FY 2008, and \$96.370 million in FY 2009. The increase in the average fund balance is due to the deposits into the fund. However, the change in the fund balance from year to year does not match total deposits exactly because the fund balance shown is the average fiscal year balance. Total fund deposits are the sum of the settlement deposits and the retained interest earnings, and deposits are projected to be \$10.729 million in FY 2007, \$13.803 million in FY 2008, and \$13.888 million in FY 2009.

Table 2					
Tobacco Trust Fund Balance					
(\$ millions)					
Fiscal Year	Balance	Deposits			
	Average Fund Balance	Tobacco Settlement Deposits	+	Retained Interest Earnings	= Total Fund Deposits
A 2001	\$7.810	\$10.651	+	\$0.099	= \$10.749
A 2002	\$14.565	\$12.432	+	\$0.022	= \$12.454
A 2003	\$27.182	\$12.466	+	\$0.161	= \$12.627
A 2004	\$38.724	\$10.669	+	\$0.289	= \$10.958
A 2005	\$49.693	\$10.828	+	\$0.320	= \$11.149
A 2006	\$60.629	\$9.940	+	\$0.339	= \$10.279
F 2007	\$70.988	\$10.353	+	\$0.376	= \$10.729
F 2008	\$82.528	\$13.339	+	\$0.464	= \$13.803
F 2009	\$96.370	\$13.365	+	\$0.524	= \$13.888

Tobacco Trust Balance by Investment Type

The fund balance is invested in the short term investment pool (STIP) and the trust fund bond pool (TFBP). STIP and TFBP are managed by the Board of Investments and forecasts of annual rates of return for STIP and TFBP are explained in the *Interest Rate Introduction*.

Table 3 shows actual and projected investment of the fund balance for each investment type from FY 2001 through FY 2009. In FY 2007 through FY 2009, 2% of the trust fund balance is expected to be invested in STIP while the remaining 98% is to be invested in TFBP.

Table 3 Tobacco Trust Fund Average Balance by Investment Type (\$ millions)					
Fiscal Year	STIP Balance	% Total	TFBP Balance	% Total	Average Balance
A 2001	\$1.750	22%	\$6.060	78%	\$7.810
A 2002	\$1.304	9%	\$13.262	91%	\$14.565
A 2003	\$1.323	5%	\$25.859	95%	\$27.182
A 2004	\$1.141	3%	\$37.583	97%	\$38.724
A 2005	\$1.675	3%	\$48.018	97%	\$49.693
A 2006	\$1.799	3%	\$58.830	97%	\$60.629
F 2007	\$1.380	2%	\$69.608	98%	\$70.988
F 2008	\$1.774	2%	\$80.754	98%	\$82.528
F 2009	\$1.795	2%	\$94.575	98%	\$96.370

Tobacco Trust Interest Earnings

Tobacco trust interest earnings are projected by multiplying the projected balance by the projected interest rate for each investment type. Table 4 shows actual and projected interest income and interest rate for each investment type from FY 2001 through FY 2009.

Table 4 Tobacco Trust Fund Interest Income and Interest Rate (\$ millions)						
Fiscal Year	STIP Income	Interest Rate	TFBP Income	Interest Rate	Total Income	Interest Rate
A 2001	\$0.051	6.98%	\$0.189	7.47%	\$0.240	3.07%
A 2002	\$0.012	0.96%	\$0.949	7.16%	\$0.968	6.64%
A 2003	\$0.014	1.06%	\$1.816	7.02%	\$1.830	6.73%
A 2004	\$0.008	0.70%	\$2.662	7.08%	\$2.670	6.89%
A 2005	\$0.037	2.19%	\$3.166	6.59%	\$3.202	6.44%
A 2006	\$0.067	3.71%	\$3.321	5.64%	\$3.388	5.59%
F 2007	\$0.073	5.27%	\$4.073	5.85%	\$4.146	5.84%
F 2008	\$0.083	4.69%	\$4.608	5.71%	\$4.692	5.68%
F 2009	\$0.086	4.77%	\$5.201	5.50%	\$5.286	5.49%

The STIP and TFBP interest rates are expected to change slightly from FY 2007 through FY 2009. Total tobacco trust fund income increases each year from FY 2007 through FY 2009 because the increasing trust fund balance offsets the lower interest

rates. Total interest earnings are forecast to be \$4.146 million in FY 2007, \$4.692 million in FY 2008, and \$5.286 million in FY 2009.

Table 5 summarizes actual and projected trust fund balances, interest rates, interest earnings, and allocation of interest earnings from FY 2001 through FY 2009. Ten percent of tobacco trust earnings are retained by the trust and 90% are allocated to a state special revenue account. This ratio was not maintained exactly for each year in FY 2001 through FY 2004 due to timing of payments, but the ratio was maintained for FY 2001 and FY 2002 added together and FY 2003 and FY 2004 added together.

Table 5 Tobacco Trust Fund Fund Balance, Rate, Interest Earnings, and Allocation (\$ millions)						
Fiscal Year	Fund Balance, Rate, and Earnings				Allocation	
	Tobacco Trust Fund Balance	Tobacco Trust Rate of Return	Tobacco Trust Interest Earnings	Tobacco Trust Retained Earnings	State Special Revenue Account	
A 2001	\$7.810	x 3.07%	= \$0.240	\$0.099	\$0.071	
A 2002	\$14.565	x 6.64%	= \$0.968	\$0.022	\$1.015	
A 2003	\$27.182	x 6.73%	= \$1.830	\$0.161	\$1.647	
A 2004	\$38.724	x 6.89%	= \$2.670	\$0.289	\$2.403	
A 2005	\$49.693	x 6.44%	= \$3.202	\$0.320	\$2.882	
A 2006	\$60.629	x 5.59%	= \$3.388	\$0.339	\$3.049	
F 2007	\$70.988	x 5.84%	= \$4.146	\$0.415	\$3.731	
F 2008	\$82.528	x 5.68%	= \$4.692	\$0.469	\$4.222	
F 2009	\$96.370	x 5.49%	= \$5.286	\$0.529	\$4.758	

Tobacco trust net interest earnings allocated to the state special revenue account are forecast to be \$3.731 million in FY 2007, \$4.222 million in FY 2008, and \$4.758 million in FY 2009.

Data Sources

Tobacco trust balances and earnings are from the Board of Investments and SABHRS. Projections of tobacco settlement deposits are from the *Tobacco Settlement Revenue* estimation. Projections of the STIP and TFBP interest rates are from *Interest Rate Introduction*.