



September 30, 2016

The Honorable Rod Skoe, Chair
Senate Tax Committee
3211 Minnesota Senate Building
St. Paul, MN 55155

The Honorable Greg Davids, Chair
House Tax Committee
585 State Office Building
St. Paul, MN 55155

The Honorable Julianne Ortman
Ranking Minority Member
Senate Tax Committee
119 State Office Building
St. Paul, MN 55155

The Honorable Paul Marquart
House Tax Committee
261 State Office Building
St. Paul, MN 55155

The Honorable Richard Cohen, Chair
Senate Finance Committee
3235 Minnesota Senate Building
St. Paul, MN 55155

The Honorable Jim Knoblach, Chair
House Ways and Means Committee
453 State Office Building
St. Paul, MN 55155

The Honorable Michelle Fischbach
Ranking Minority Member
Senate Finance Committee
15 State Office Building
St. Paul, MN 55155

The Honorable Lyndon Carlson Sr.
Ranking Minority Member
House Ways and Means Committee
283 State Office Building
St. Paul, MN 55155

RE: 2016 Budget Reserve Report

Dear Senators and Representatives:

In accordance with [2015 Minnesota Session Laws, chapter 77, article 2, section 7](#), the commissioner of Minnesota Management and Budget (MMB) must develop and annually review a methodology for evaluating the adequacy of the state's budget reserve based on the volatility of Minnesota's general fund tax structure.

The laws also require the commissioner to report by September 30 of each year the percentage of the current biennium's general fund non-dedicated revenue that is recommended as a budget reserve to the chairs and ranking minority members of the Senate Committee on Finance, the House of Representatives Committee on Ways and Means, and the Senate and House of Representatives Committees on Taxes. Please find MMB's September 2016 *Budget Reserve Report* attached below.

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As required by statute, MMB will continue to evaluate the adequacy of the statutory budget reserve based on any significant changes in the tax system.

Sincerely,

A handwritten signature in black ink, appearing to read "Myron Frans". The signature is fluid and cursive, with a prominent initial "M" and a long, sweeping tail.

Myron Frans
Commissioner

cc: Governor Mark Dayton
Eric Nauman, Senate Counsel, Research & Fiscal Analysis
Jay Willms, Senate Counsel, Research & Fiscal Analysis
Bill Marx, House Fiscal Analysis
Katherine Schill, House Fiscal Analysis
Cynthia Templin, House Fiscal Analysis

Budget Reserve Recommendation

To adequately manage the underlying risks in Minnesota's general fund tax revenue system, Minnesota Management and Budget (MMB) recommends a budget reserve target of 4.9 percent¹ of the current biennium's general fund non-dedicated revenues, or a \$2.052 billion budget reserve for the 2016-17 biennium.² Minnesota's current budget reserve is \$1.597 billion, or 3.8 percent of FY 2016-17 revenues.

Budget Reserve Summary: September 2016

	Current \$ Level	% of FY 2016-17 Non-Dedicated Revenues
MMB FY2016-17 Recommendation	\$2.052 billion	4.9%
Current Budget Reserve Account	\$1.597 billion	3.8%
Difference	\$0.455 billion	

The recommended reserve level is based on MMB's assessment of volatility in Minnesota's revenue system. We examine the variability over time of the state's major tax bases and changes in the composition of tax revenues. The recommended reserve level assumes the budget is structurally balanced through the remainder of the biennium, and policymakers desire a 95 percent level of confidence that a biennial deficit generated by revenue volatility will not exceed the budget reserve.

We have reviewed the revenue volatility model and updated it to reflect both an additional year of data and tax law changes enacted by the 2016 legislature. The result of those updates is a higher estimated degree of revenue system volatility. Consequently, we have increased the recommended percentage of revenues to 4.9 from the 4.8 percent recommendation in our September 2015 report.

The target is for the budget reserve account alone. Minnesota also has a cash flow account, which is intended to offset potential cash shortages caused by a mismatch between monthly revenue collections and spending. The cash flow account is currently funded at \$350 million.

¹ Rounded to the nearest tenth of a percent.

² Based on end of 2016 legislative session *General Fund Balance Analysis*.