



Task Force on Comprehensive Revenue Restructuring

January 24, 2008

Tom Potiowsky and George Naughton
Department of Administrative Services



Lessons from our History:

Strong Economic Growth during the
1990's

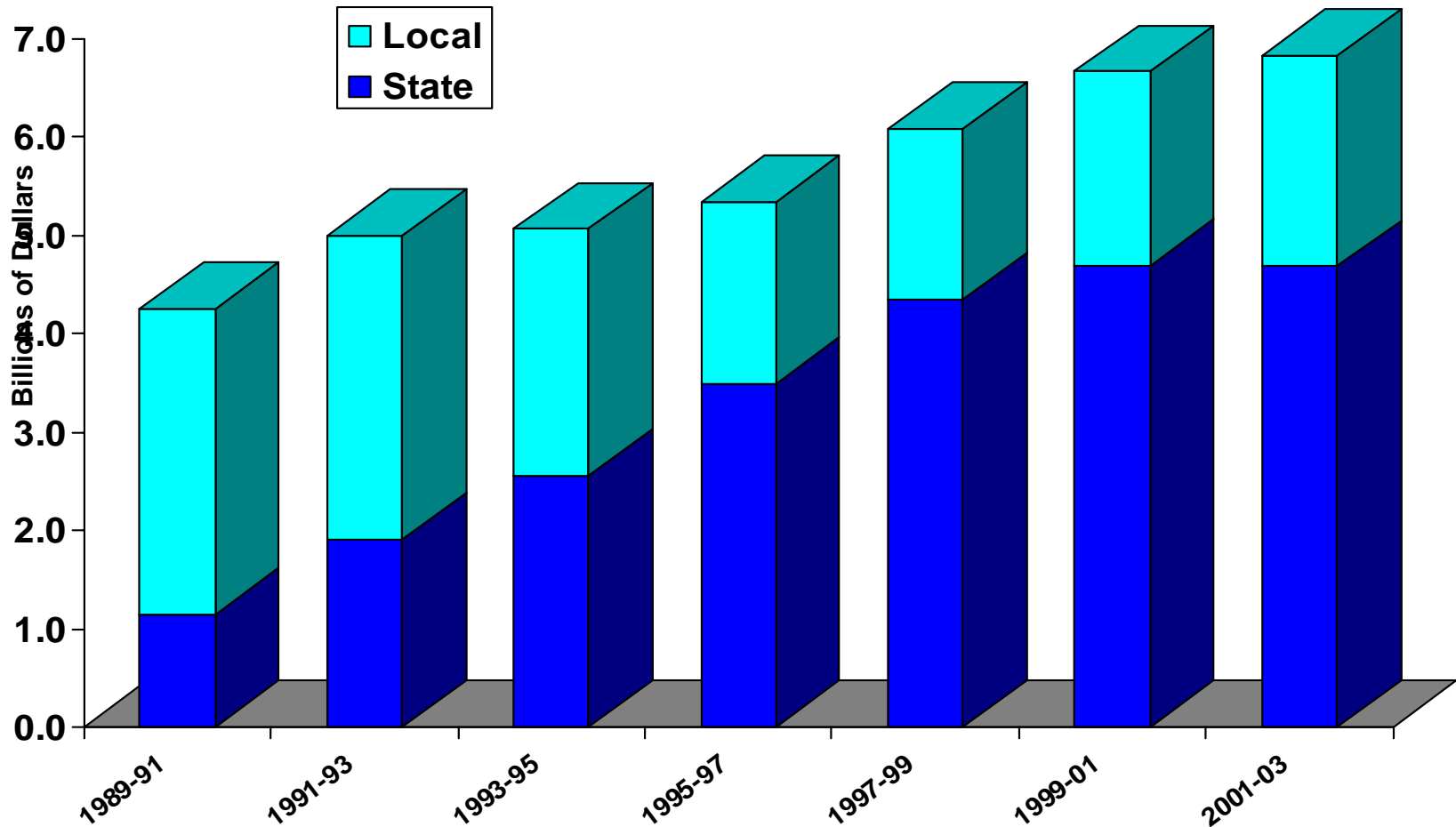


1990's: State enjoyed huge economic growth and diversification

- Total gross state product increased by 98% from 1991-2001.
- High-tech industry growth.
- Population growth – 11th fastest growing state.
- Personal income grew at annual rate of 5.6%, exceeding the nation.
- Exports increased by a compound annual rate of 5.8%.
- State General Fund grew from \$4,628.1 million in 1989-91 to \$10,121.8 million in 1999-2001 – dollars primarily went to K-12, Oregon Health Plan, and Public Safety.
- Kicker returned for personal income tax filers 7 times, totaling over \$1.5 billion; for corporate tax filers 5 times, totaling over \$400 million.

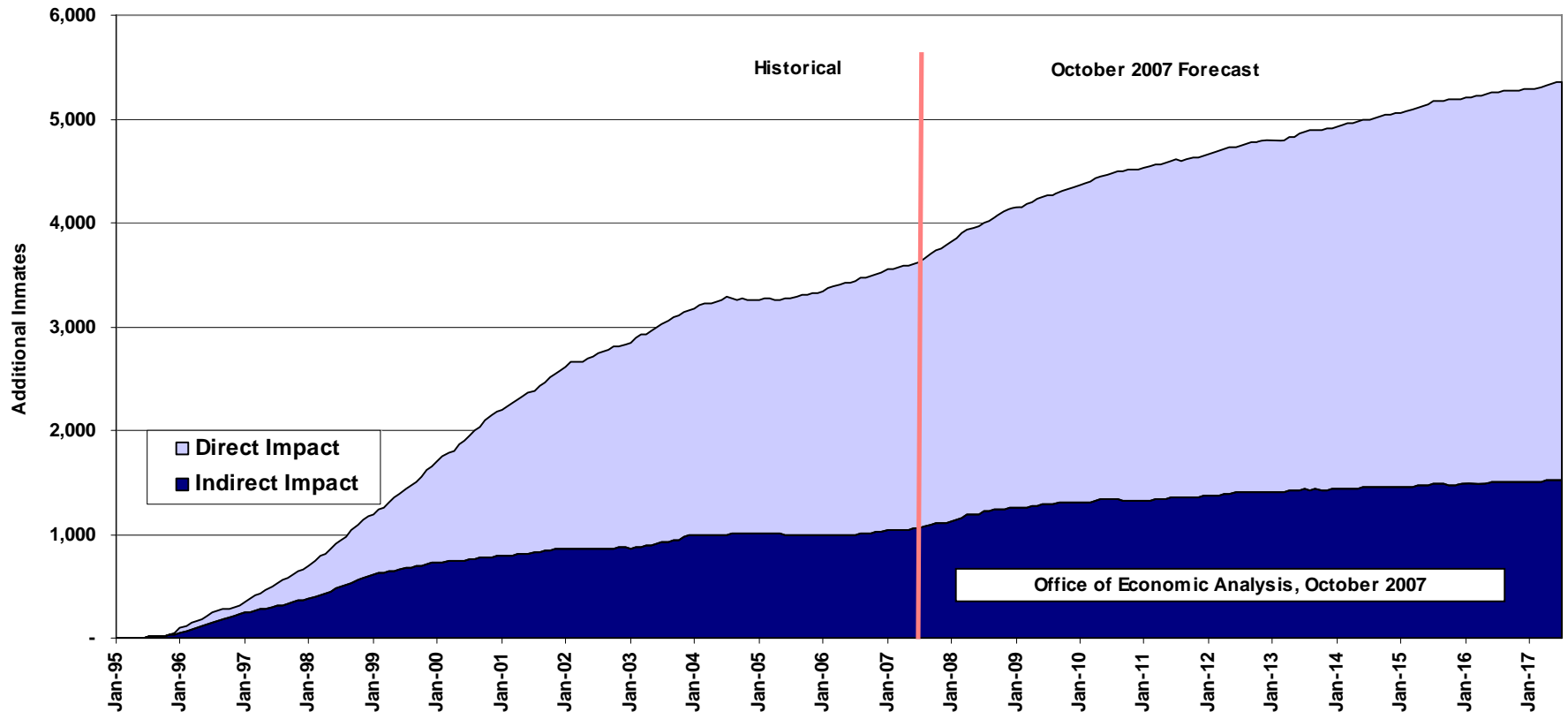


State and Local Resources for K-12 School Funding





Estimated Impact of Measure 11 on Oregon's Prison System





Impact of 2001-03 Recession on State Budget



2001-03

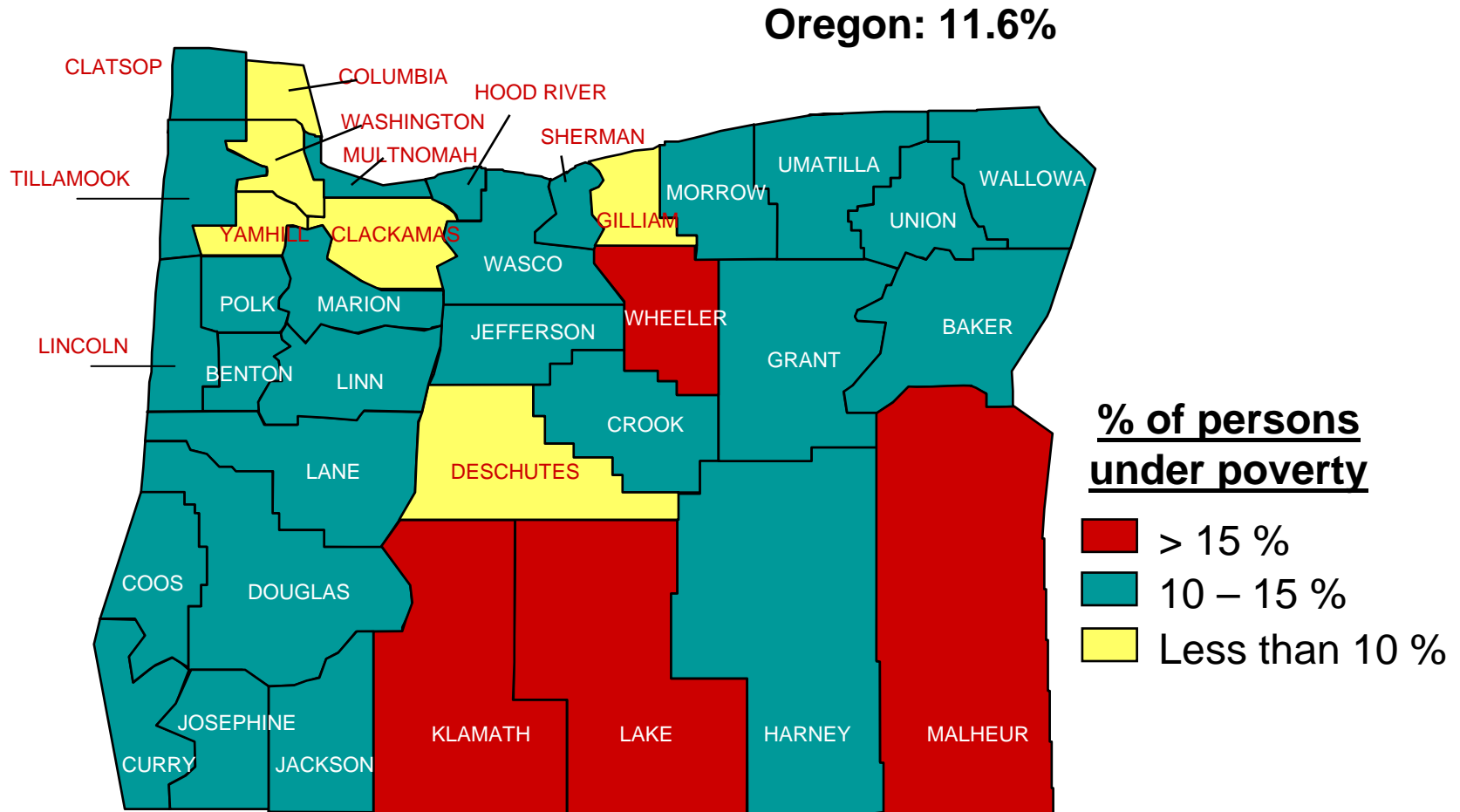
- Close of Session forecast projects \$12.1 billion General Fund/Lottery Funds (\$11.45 GF/\$0.65 LF). Legislature approves expenditures of \$12 billion. Preliminary 2003-05 forecast is approximately \$13 billion (GF plus Lottery).
- Quarterly General Fund forecasts demonstrate effects of recession:

	2001-03	2003-05
September 2001	11,159.4	12,313.0
December 2001	10,747.5	11,944.8
March 2002	10,604.0	11,973.9
June 2002	10,098.2	11,528.3
September 2002	9,718.6	11,392.5
December 2002	9,585.6	10,880.5

- Five special sessions plus a rebalance during the 2003 regular session to rebalance the budget using one-time resources, program reductions, and additional revenues.

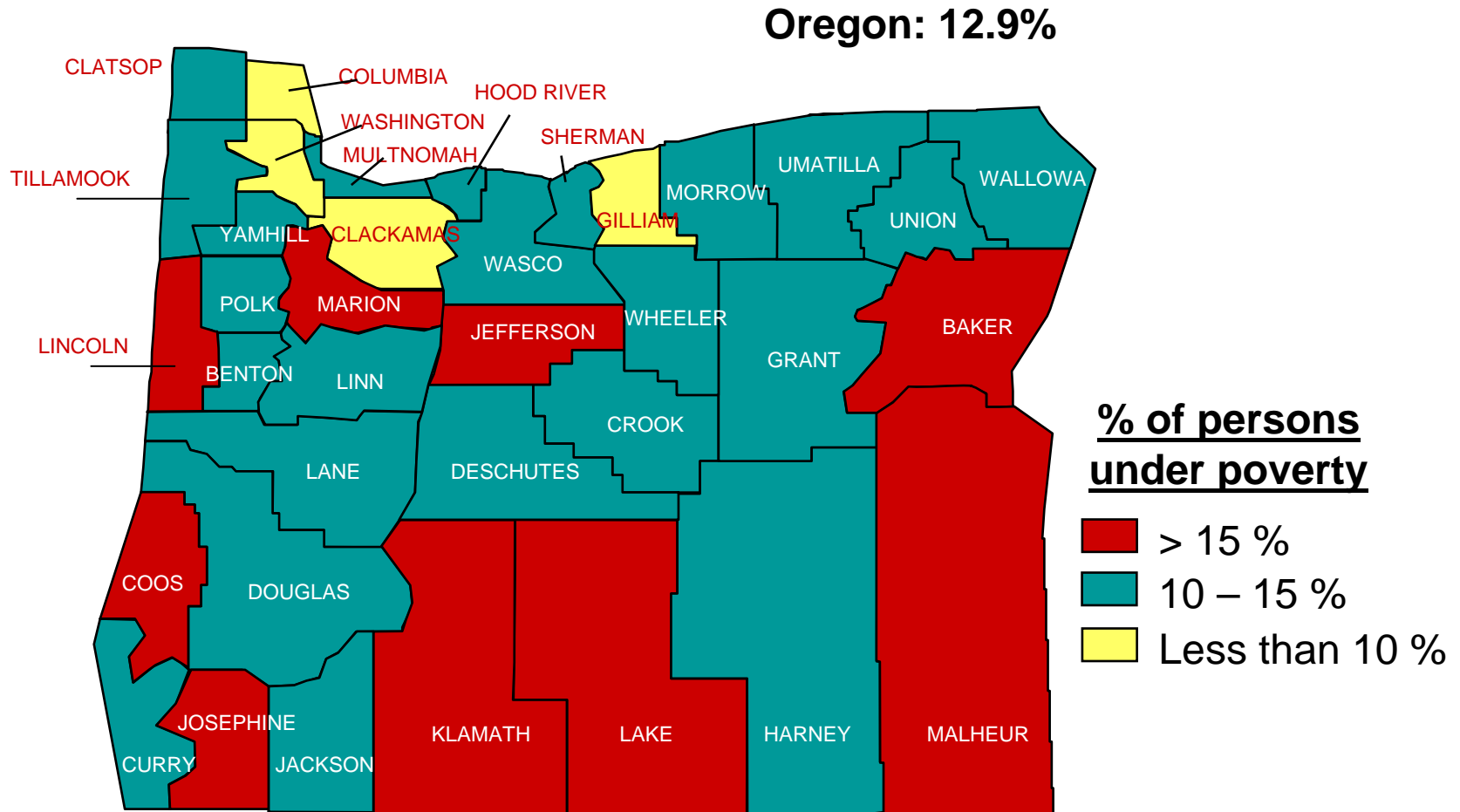


Poverty Rate, 1999





Estimated Poverty Rate, 2004

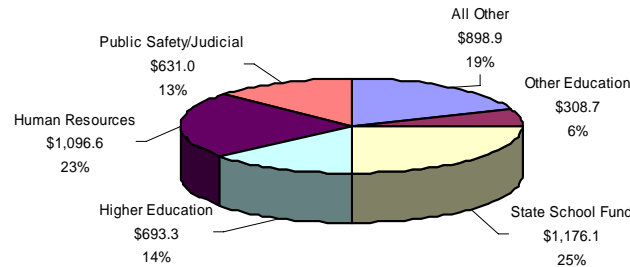




Approved General Fund & Lottery Funds

1989-91 General & Lottery Fund Expenditures

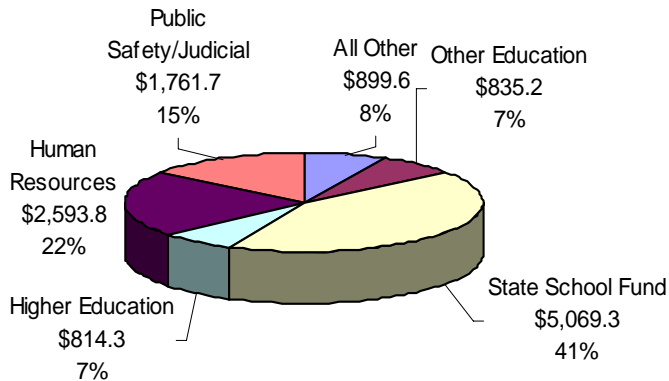
Total: \$4,804.6 Million



2001-03 Legislatively Approved General Fund & Lottery Funds

Budget - Close of Session

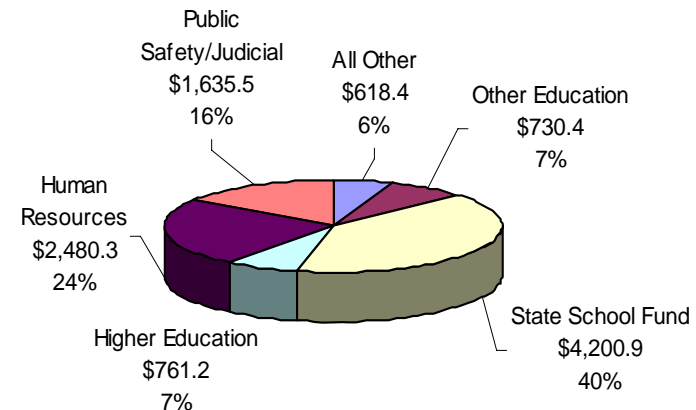
Total: \$11,973.9



2001-03 Legislatively Approved General Fund & Lottery Funds

Budget - End of Biennium

Total: \$10,426.7





Economic Recovery in 2003



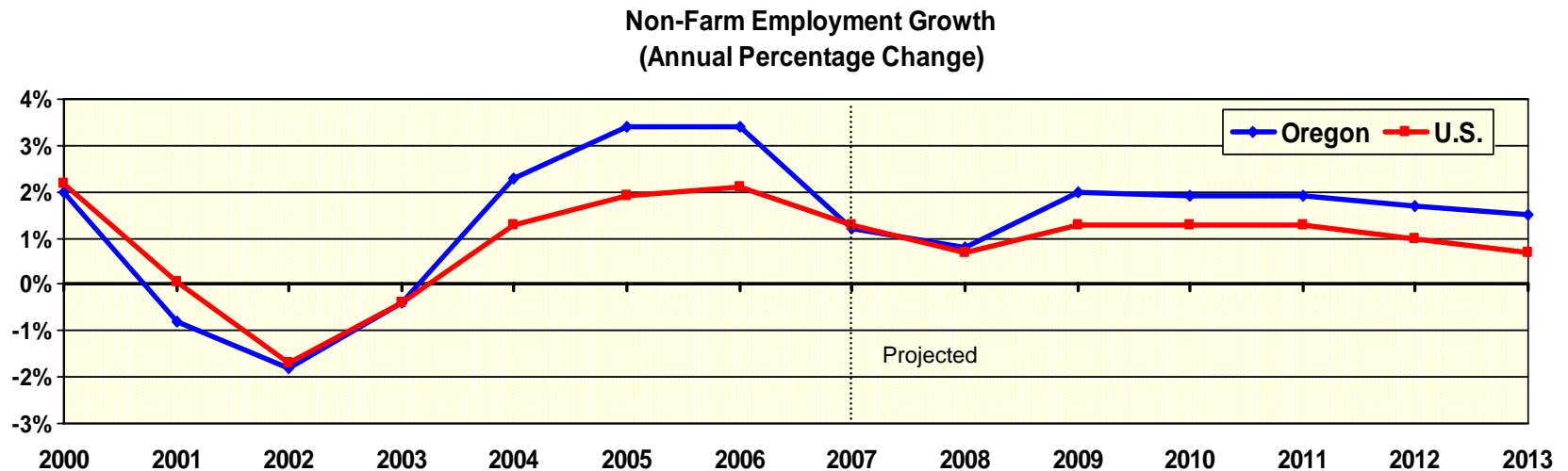
Highlights of Oregon Economy

- After the recession of 2001-03, Oregon experienced three years of strong economic growth. During this period, Oregon's economic indicators exceeded national averages.
- Employment picture in Oregon was extremely strong beginning in 2003
 - 2.3% annual growth in calendar year 2004
 - 3.4% annual growth in calendar years 2005 and 2006
 - For all three years, Oregon's employment growth was between one and one-and-a-half percentage points higher than the national average.
- Oregon's basic strengths
 - Diverse economy with substantial international presence
 - Relatively lower energy costs
 - A high quality of life
 - Well-educated workforce
 - Affordable housing
 - Business cost advantages
 - Pacific Rim orientation
 - Strong population growth due mainly to in-migration



Long-Term Employment Trends

Oregon's overall employment trends have mirrored the U.S. with slightly more job loss during the recession but stronger recent and projected growth



Source: Office of Economic Analysis

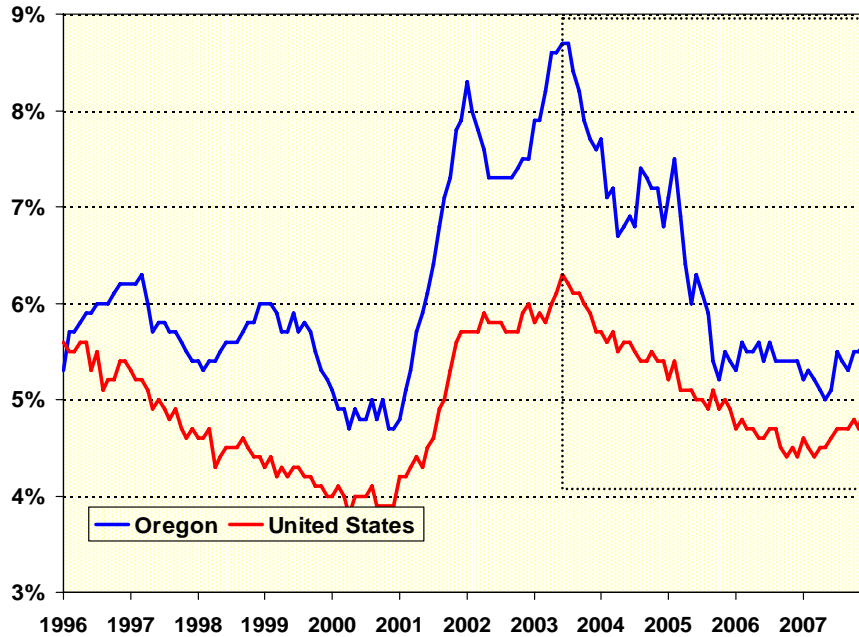
- The Oregon economy follows the path of the national economy
- Job growth turned positive in July 2003
- Oregon's employment growth will continue to be fueled by strong exports, population growth and business investment



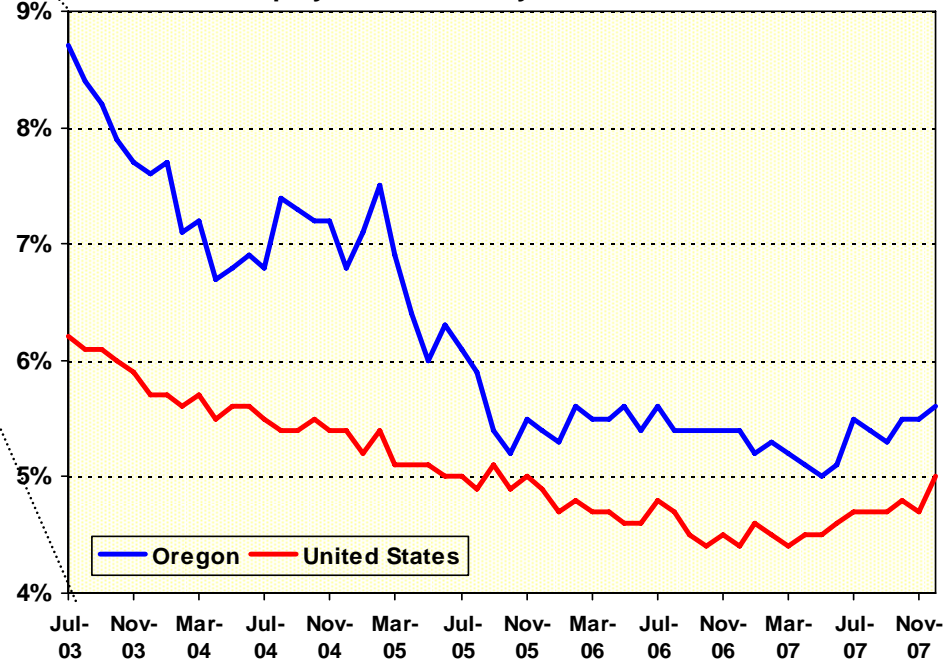
Improving Unemployment Trends

Oregon's unemployment rate, while still higher than the U.S. average, has decreased significantly in the past four years

Unemployment Rates - 1996 to 2007

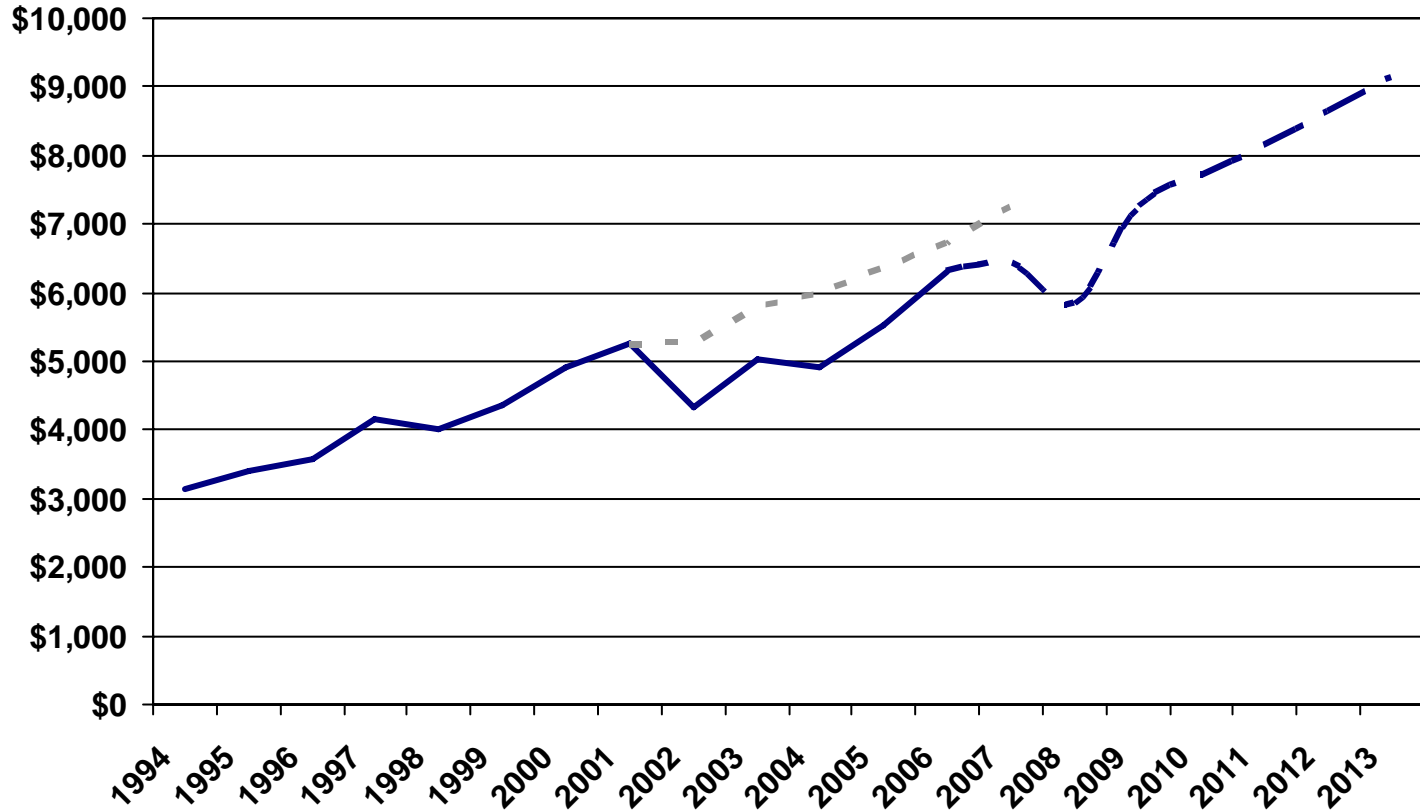


Unemployment Rates July 2003 - December 2007





General Fund Forecast Comparison Fiscal Years, in Millions



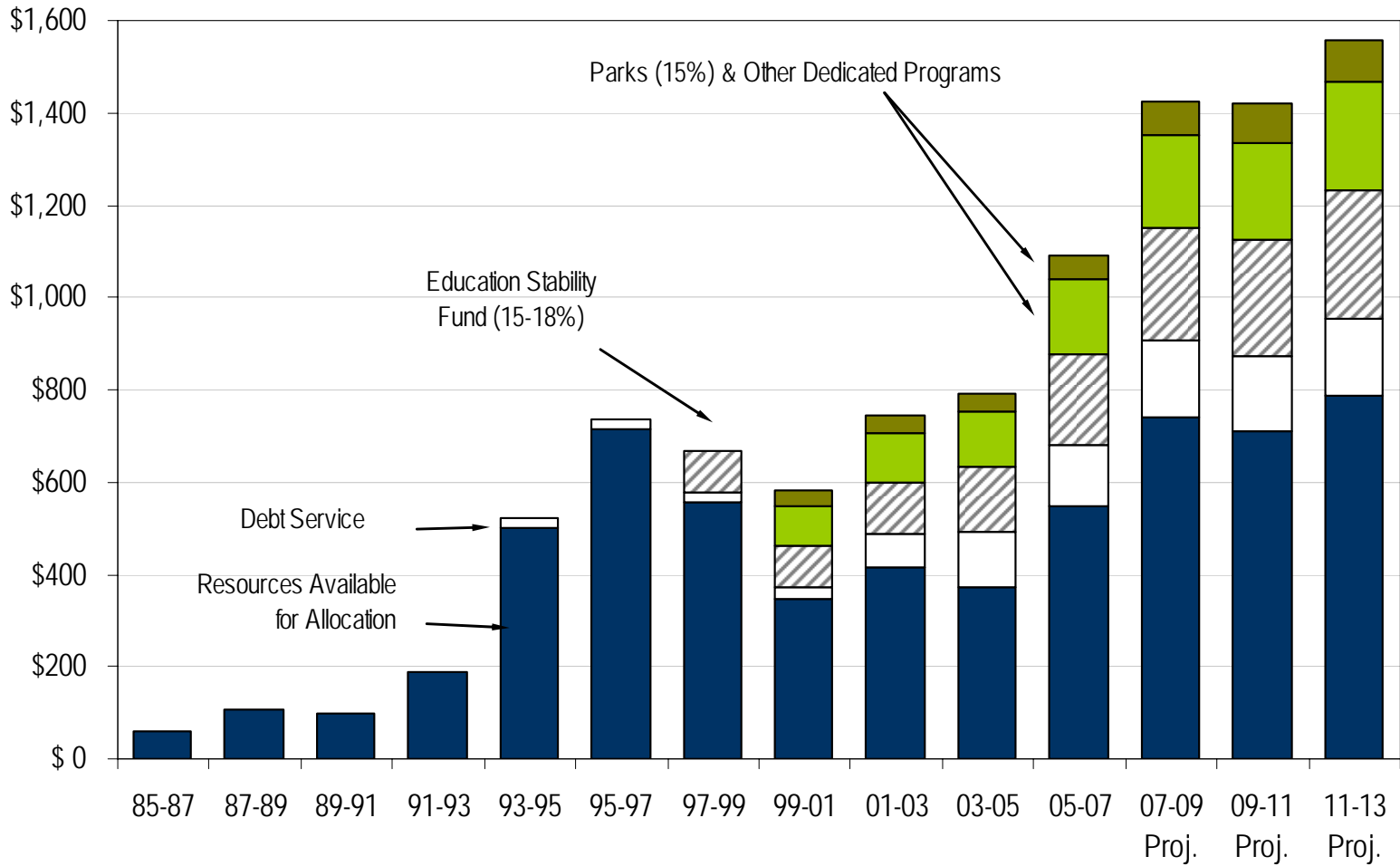
— Actual Revenues

- - - COS 2001 Forecast

- - - December 2007 Forecast



Lottery Resources Available to the State (Millions)



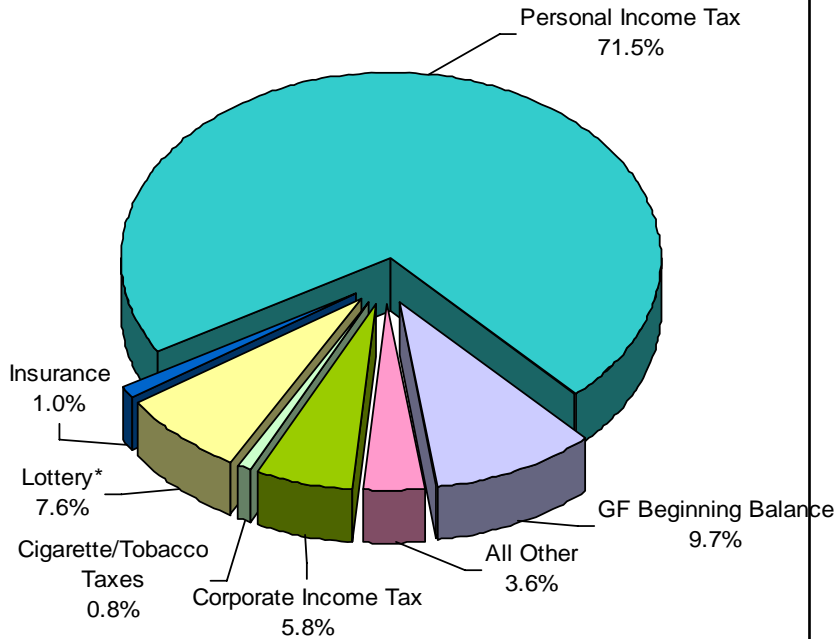
Note: Resources do not include Video Lottery proceeds dedicated to the Counties. Beginning balance is included.

2003-09 debt service figures do not reflect any Education Endowment Fund or reserve earnings designated for debt service on education bonds.



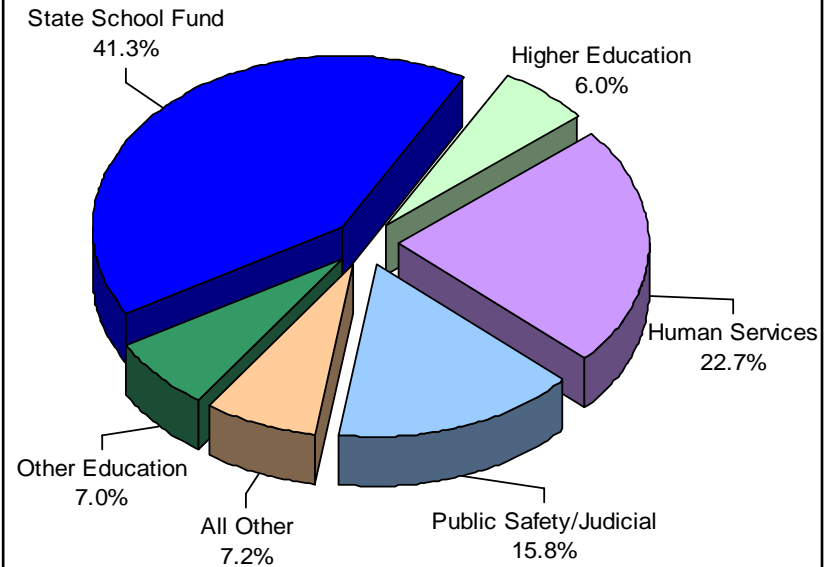
2007-09 Legislatively Adopted Budget General Fund and Lottery Funds

Resources Budgeted Total: \$15,303 Million



* Includes beginning balance & carry forward

Expenditures Total: \$15,106 Million





Increasing Oregon's Budget Reserves

- Continued growth of the Education Stability Fund
 - 18% of biennial net Lottery revenues are dedicated to this reserve account
- Establishment of a Rainy Day Fund in the 2007-09 Budget
 - Seeded with Oregon's projected 2005-07 Corporate Kicker of \$319.3 million
 - All interest earnings on the Rainy Day Fund are retained in the Rainy Day Fund
 - Automatic transfer to the Rainy Day Fund of one percent of Oregon's General Fund expenditures from the State's ending fund balance at the completion of each biennium

Budgeted Reserves		
(\$ Millions)		
	<u>2005-07</u>	<u>2007-09</u>
Education Stability Fund	\$ 236	\$ 468
Rainy Day Fund	--	346 ⁽²⁾
Ending Balance/Emergency Fund	<u>319⁽¹⁾</u>	<u>227</u>
TOTAL	\$ 555	\$ 1,041

⁽¹⁾Reflects Ending Balance after distribution of \$1.2 billion in personal "kicker" distributions

⁽²⁾Reflects \$319.3 million in initial corporate "kicker" deposit and interest earnings

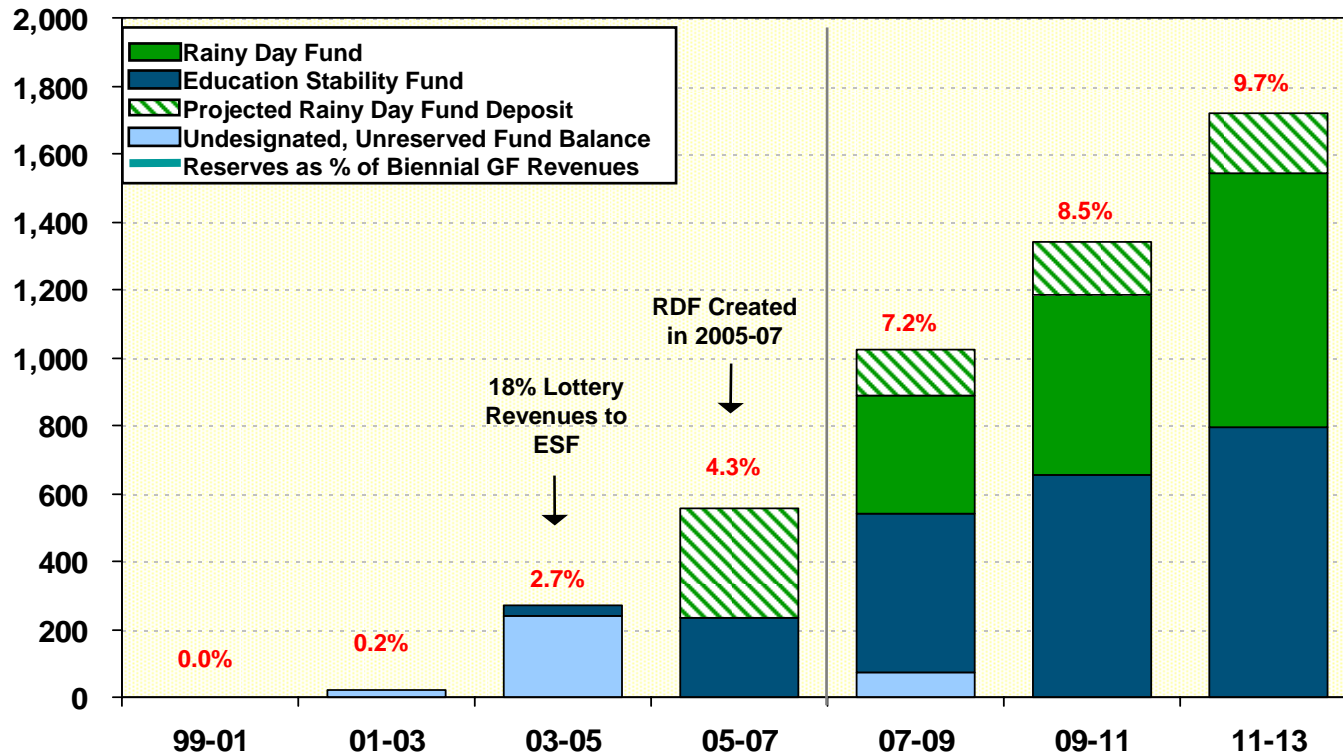
- \$1 billion budgeted reserve for 2007-09 biennium is approximately 7% of anticipated biennial general fund expenditures



Undesignated Fund Balances and Projected Reserves

The State's reserve funds are now legally required and a permanent component of the State's balance sheet

(\$ in millions)





Looking Forward at Budget Drivers



Revenue Methodology

- Revenues are modeled and projected based on relationships between taxable incomes and key economic variables (e.g., capital gains as a function of past and predicted stock market performance).
- Outer-year forecasts are based on long-run historical growth rates.
- OEA consults with the Council of Revenue Forecast Advisors quarterly to discuss recent trends and anticipated issues.

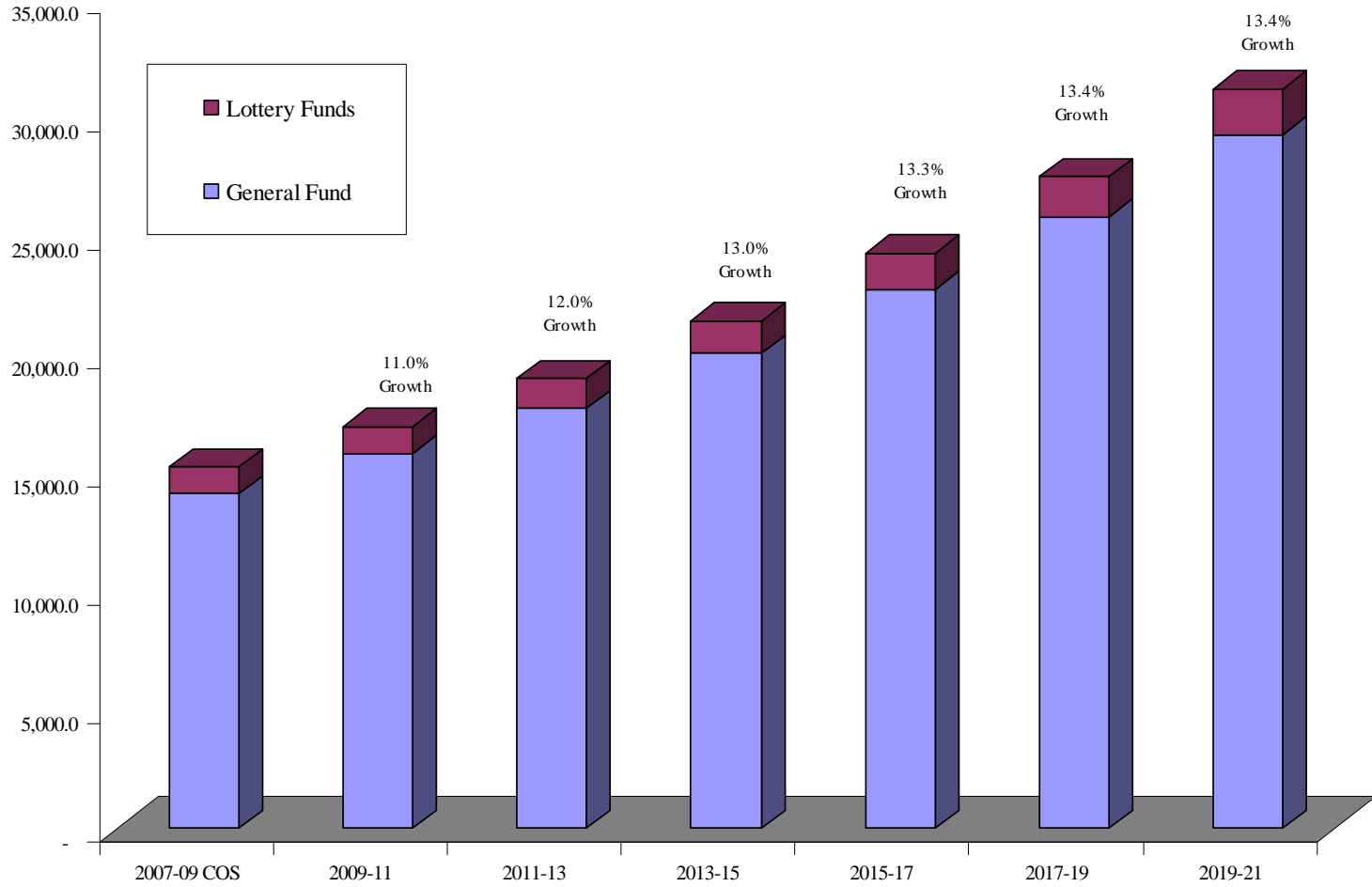


Revenue Drivers

- Revenue Growth Factors
 - Employment
 - Wage Rates
 - Investment Returns
 - Profit Levels
- Long term risks
 - Burgeoning retirement income erodes taxable income base.



Long Term Revenues





What has caused General Fund expenditure growth?

- **Primary**
 - Population
 - Voter Approved Initiatives
 - Legislative Policy decisions
 - Federal Budget Adjustments
- **Secondary**
 - Inflation
 - Lawsuits



Expenditure Methodology

Essential Budget Level (EBL) Approach

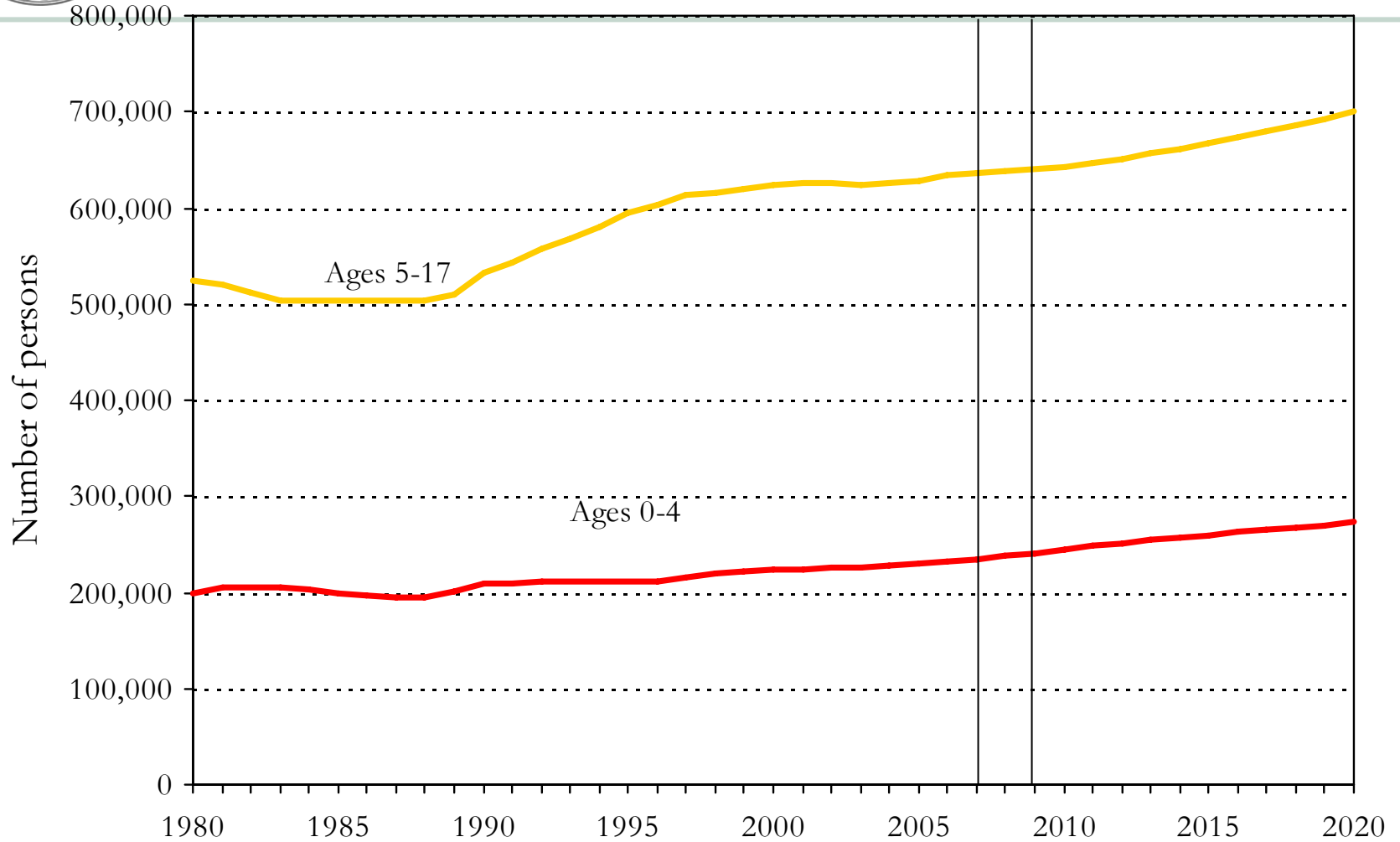
- Phased in/out Legislatively Approved Programs that were starting or ending in 2007-09
- Added Projected Inflationary Increases (general and medical)
- Adjusted Mandated Caseload programs for population changes
- Adjusted Mandated Caseload programs for projected federal funding changes
- Includes debt service only legislative approved projects or new construction that will be driven by mandated caseload programs

Inherent Downward Bias

- Debt Service costs phase-out over time, but are not replaced

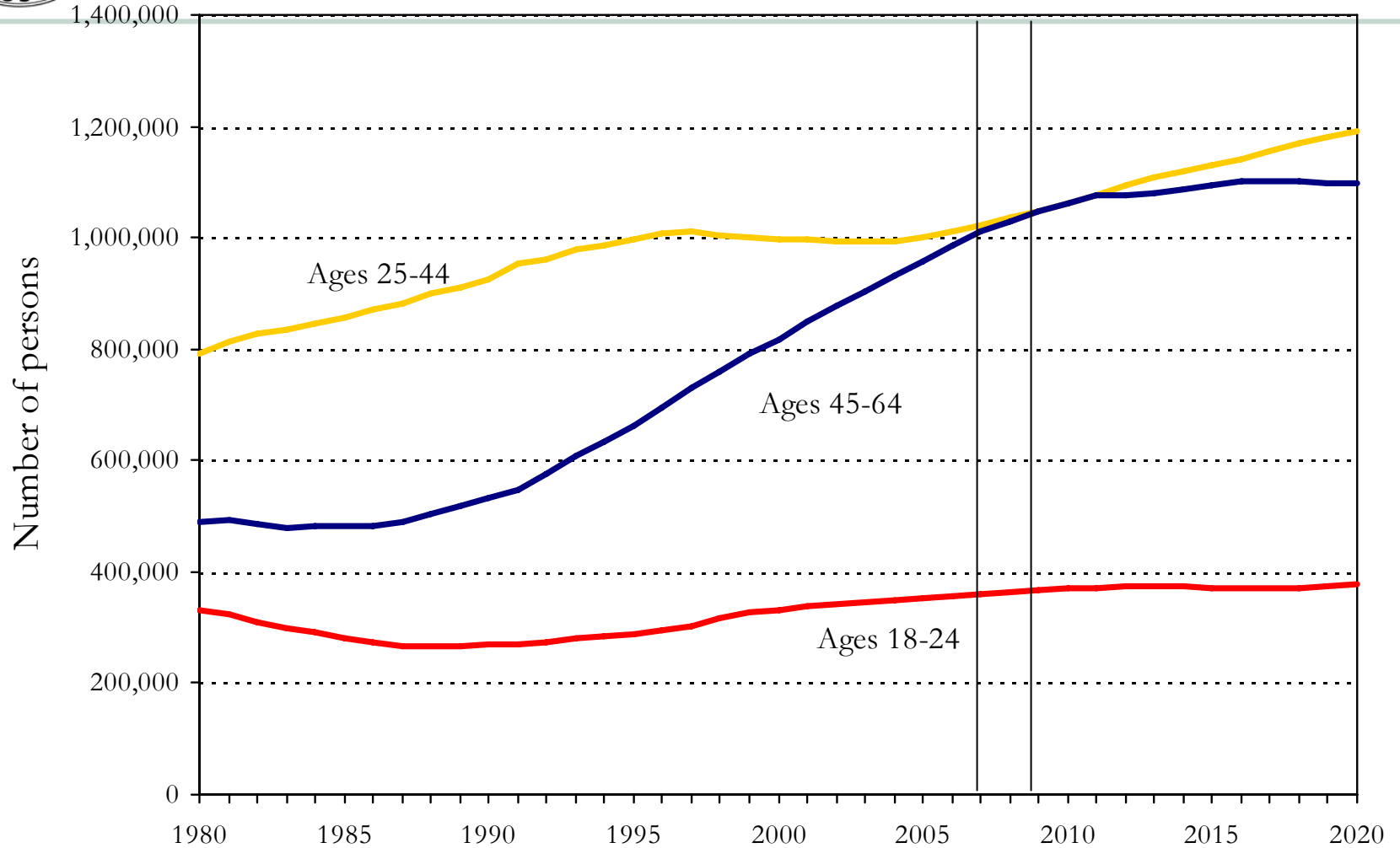


Young-age Population: 1980-2020



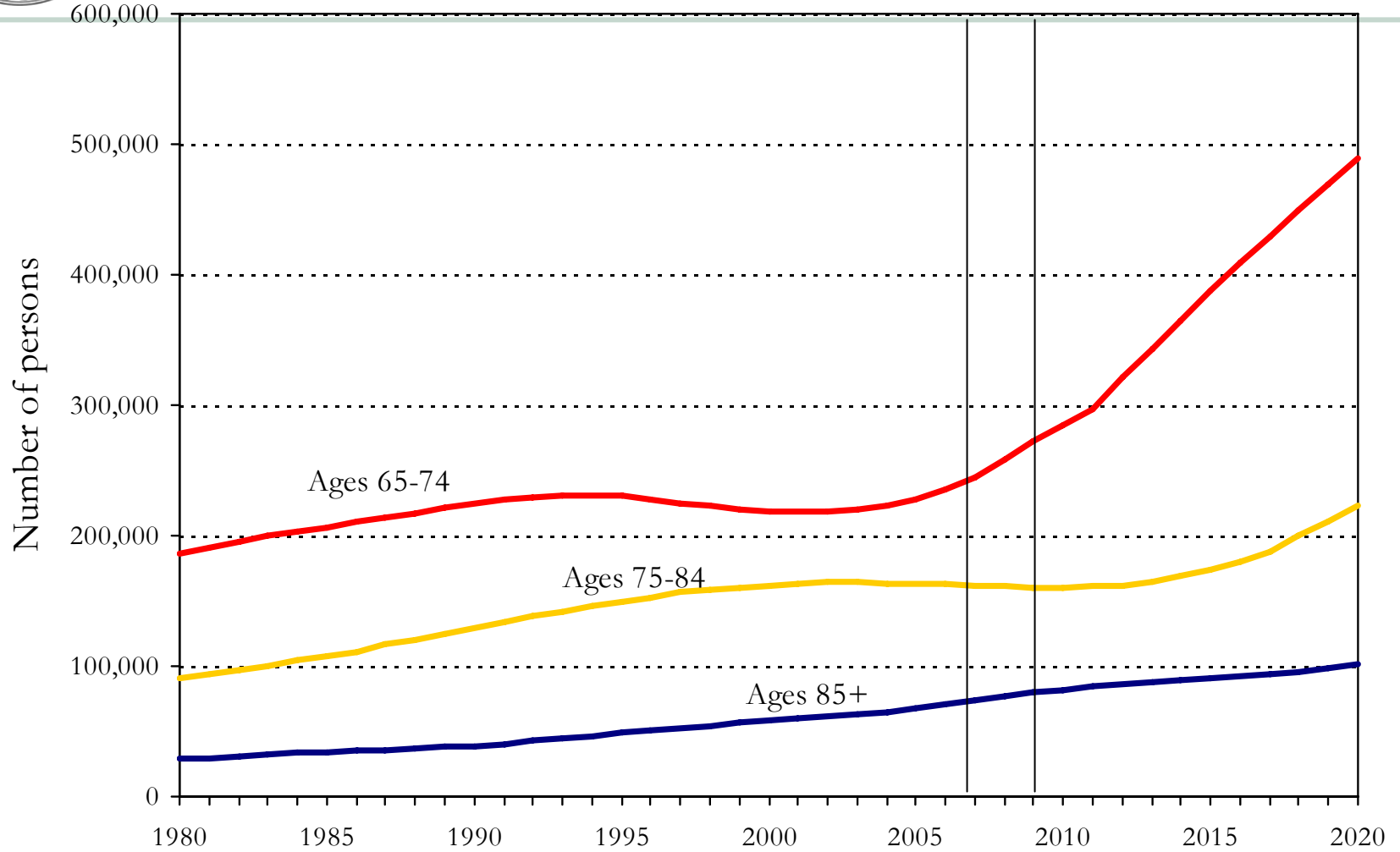


Working-age Population: 1980-2020



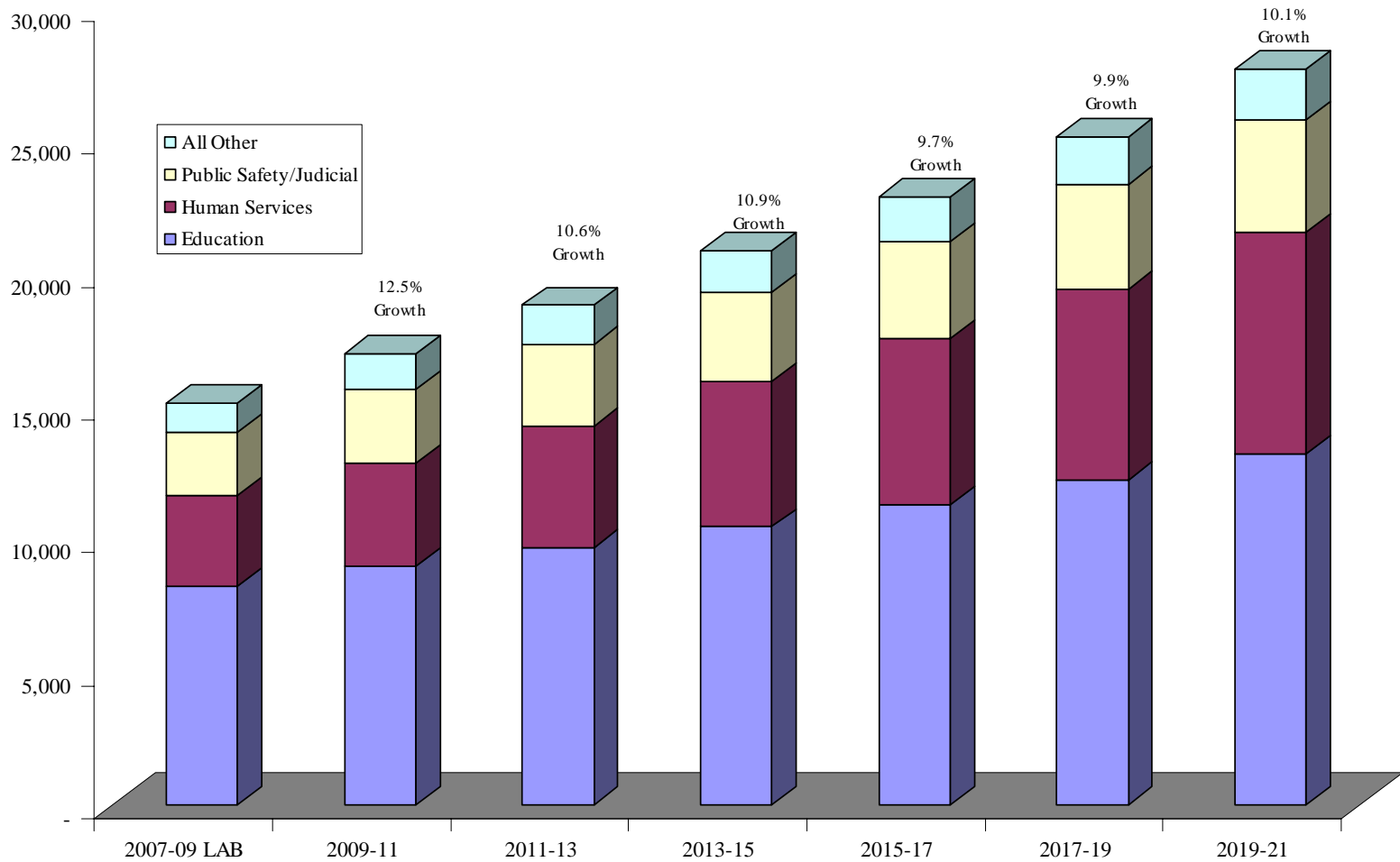


Elderly Population: 1980-2020





Long Term Expenditures





Expenditure Assumptions

Overall

- General and medical inflation factors developed based on national projections
- Used standard essential budget level assumptions for program expansions.

Education

- State School Fund budget was projected to grow using an EBL model.
- Funding for Opportunity Grants phased-in during 2009-11.
- Debt Service on approved capital construction/deferred maintenance costs within higher education and community college programs was included, but expenditure assumptions do not include any new projects.

Human Services

- Human Service caseloads were projected to increase based on the demographic growth of the client population.
- Oregon Health Plan cost growth was assumed at about 17% for 2009-11 rising to 20% for the following biennium.



Expenditure Assumptions (cont)

Human Services (cont)

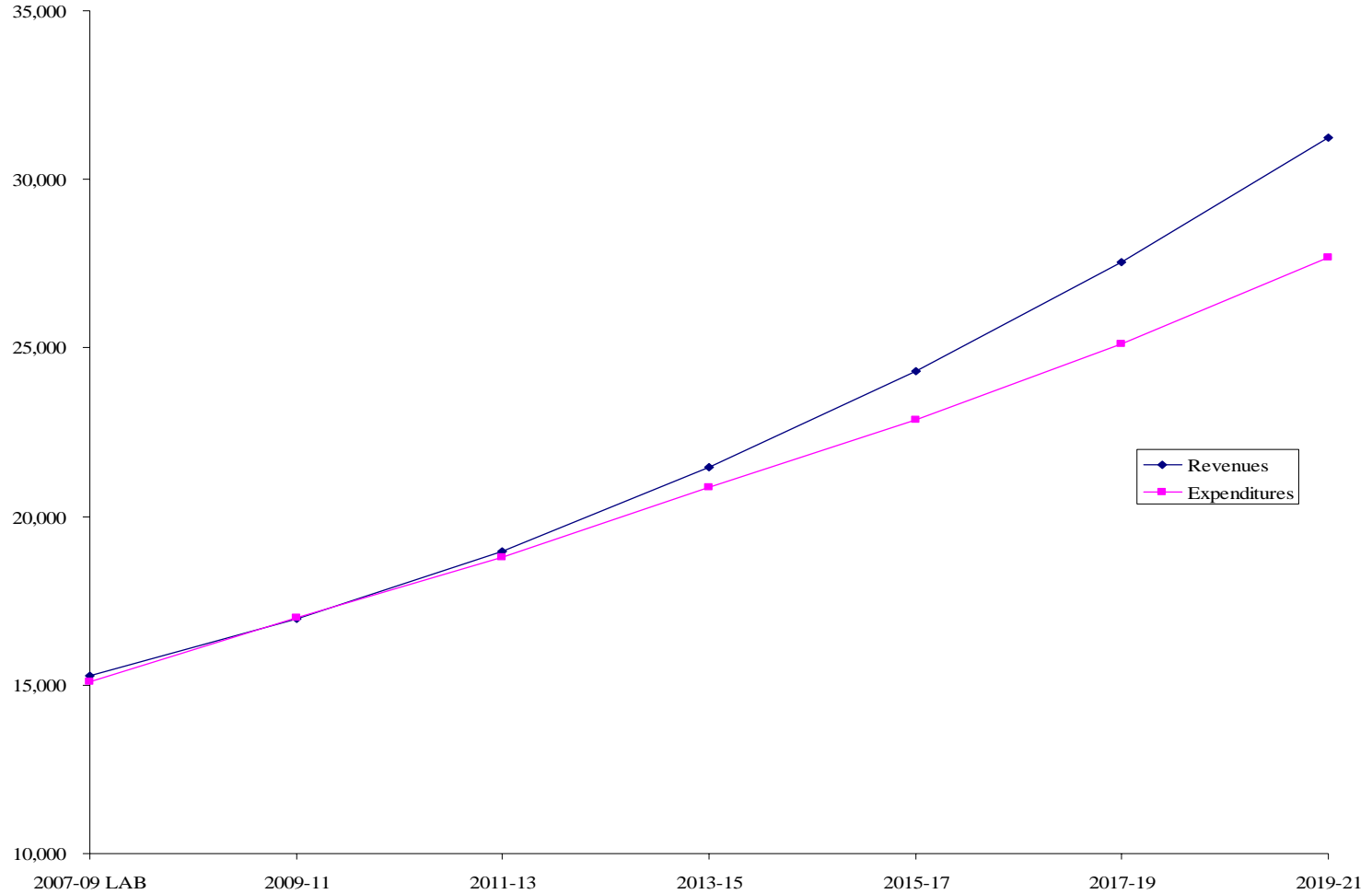
- Assumes that programs funded with Other Funds in 2007-09 will continue to be funded by those revenue sources in 2009-11 and beyond.
- Includes funding changes related to flattened tobacco tax revenue projections and changes in federal match rates.
- Includes construction and operation of new state hospital facilities.

Public Safety

- Caseload growth for public safety programs based on April 2007 prison population forecast.
- It does not include heightened costs of caring for an aging inmate population. Further work on this topic is currently being developed.
- Includes funding for last two projected prisons based on prison population forecasts.
- Does not assume passage of new initiative petitions that may be decided by voters.
- Includes debt services for the Oregon Wireless Interoperability Network.



Long Term Budget

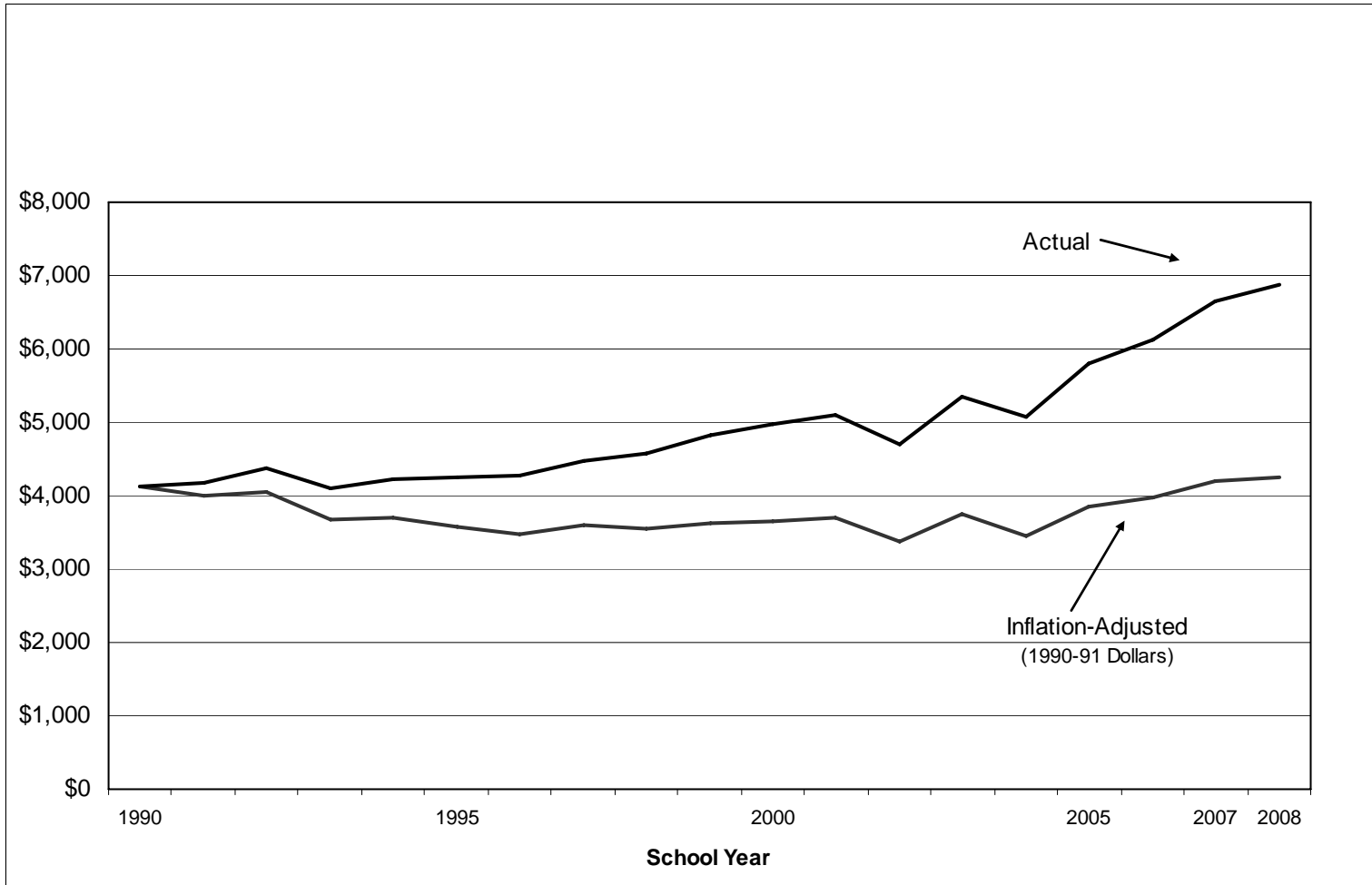




Significant Issues Outside These Expenditure Forecasts



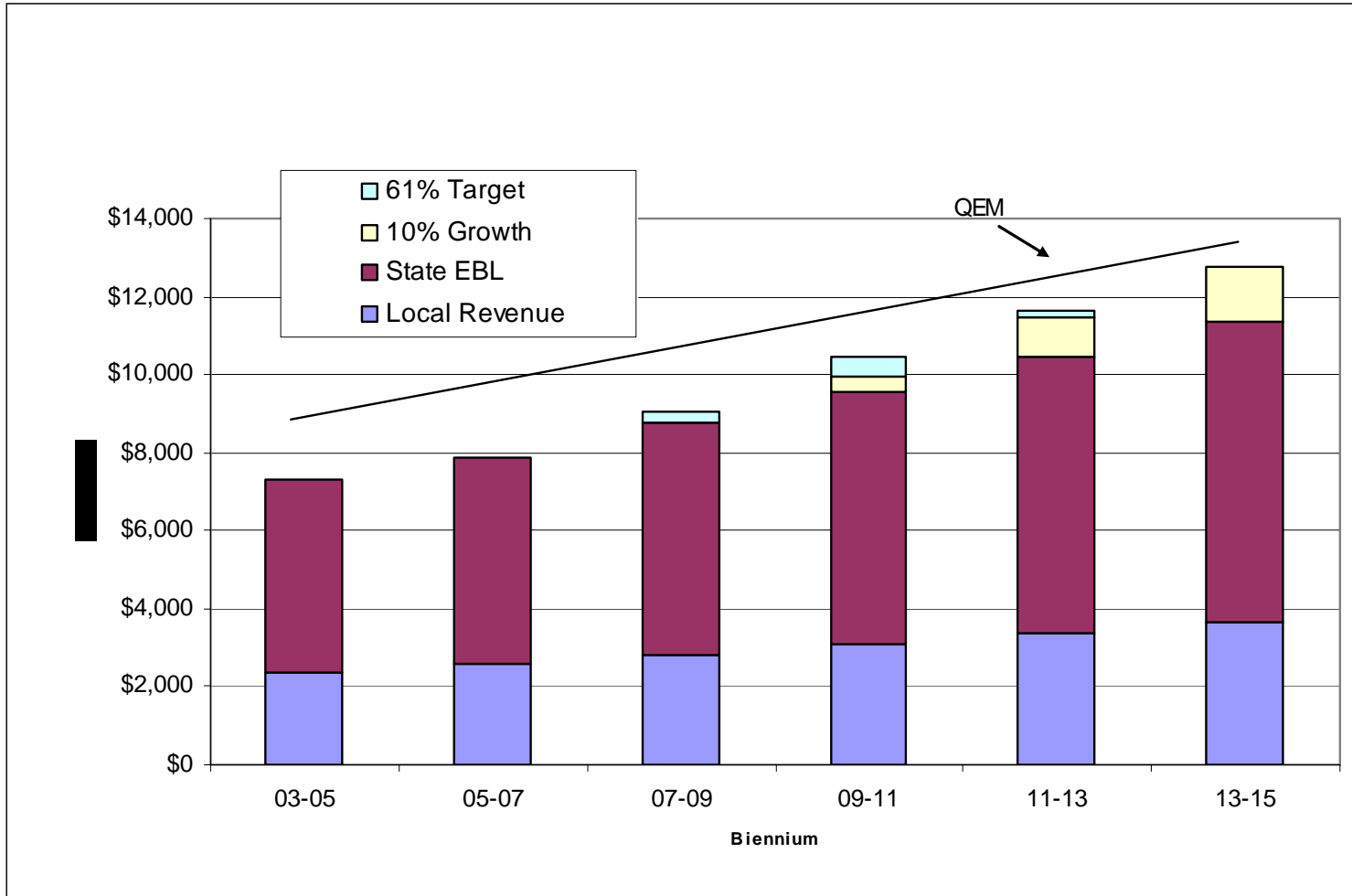
K-12 School Funding per ADMw (State School Fund and School Improvement Fund)





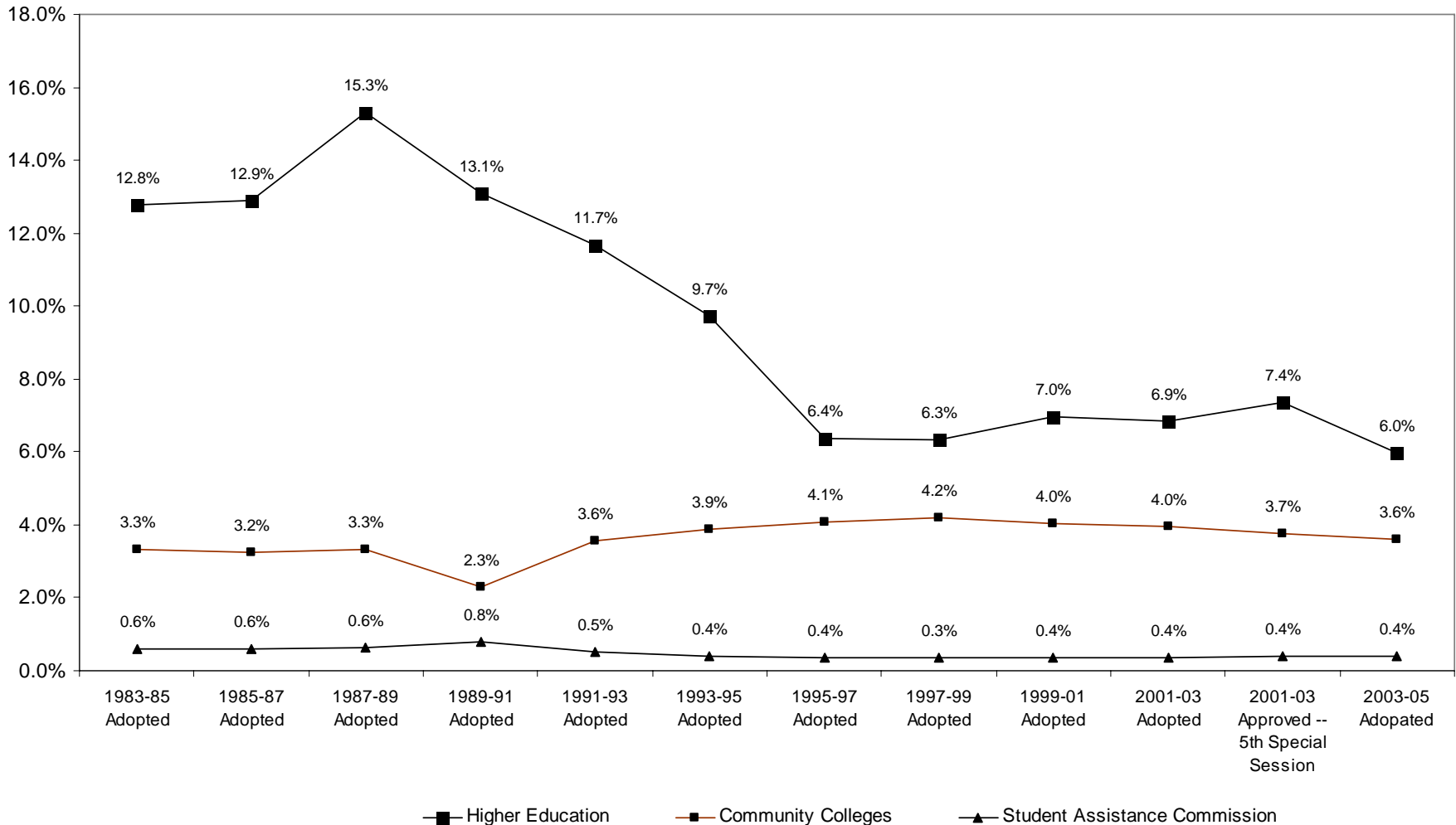
K-12 School Funding Closing the QEM Gap

(“State EBL” only includes State School Fund Base)



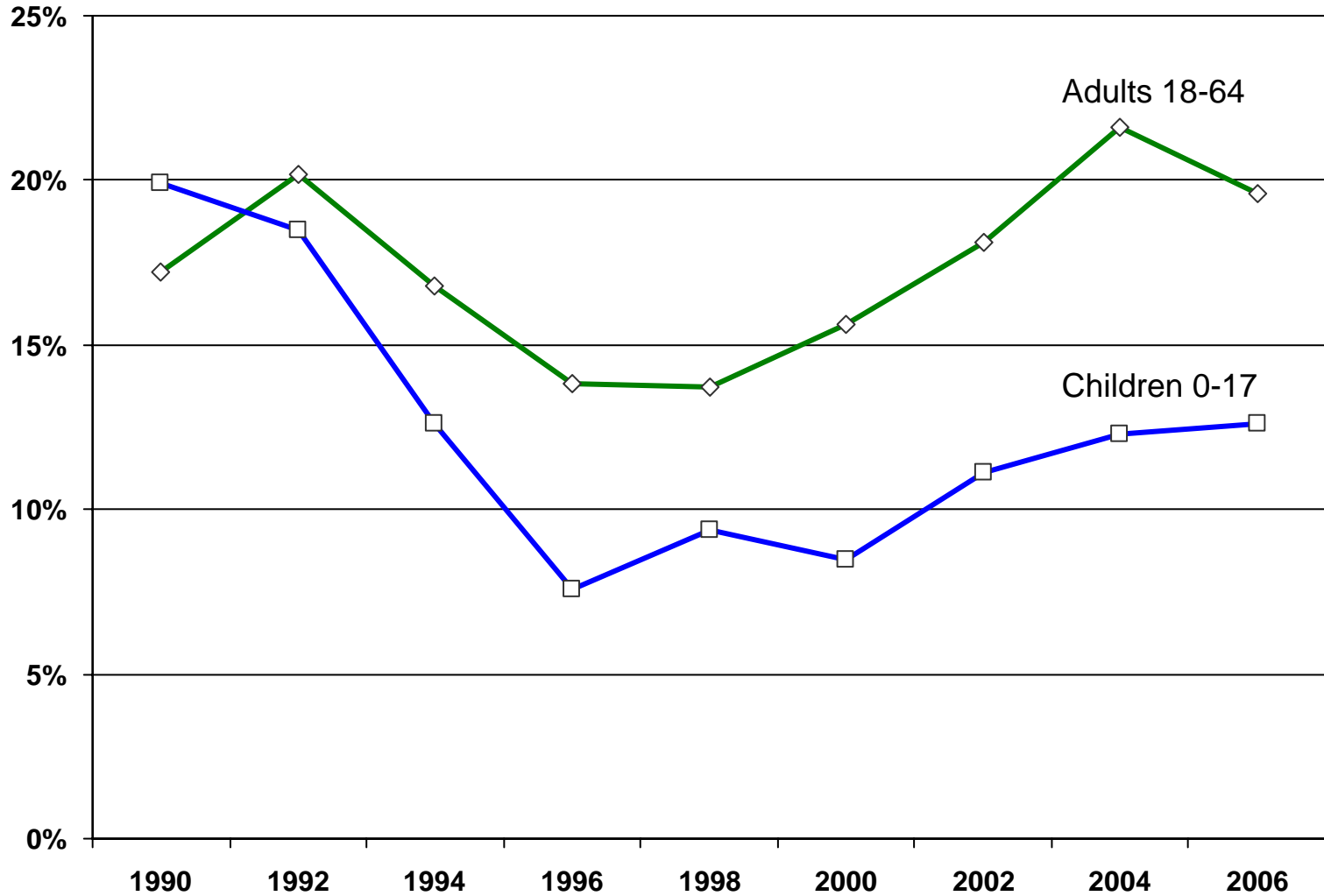


Post-Secondary Education Funding Percent of General Fund and Lottery Funds 1983-85 through 2003-05





Oregon Health Care Uninsurance Rates: 1990-2006



Source: Office for Oregon Health Policy and Research, Oregon Population Survey 2006.



Other Issues

- **Economic Downturn**
- **Federal Budget Adjustments**
- **Additional Lawsuits**
- **Potential Voter Approved Initiatives**
 - **Repeat Property Offenders: Full biennial costs could be between \$275 and \$430 million.**
- **Pent-up Budget Demand**
 - **Deferred Maintenance: Outstanding deferred maintenance costs for state and University owned facilities exceed \$800 million.**
 - **Seismic: Rehabilitation costs could exceed \$750 million depending on approach.**