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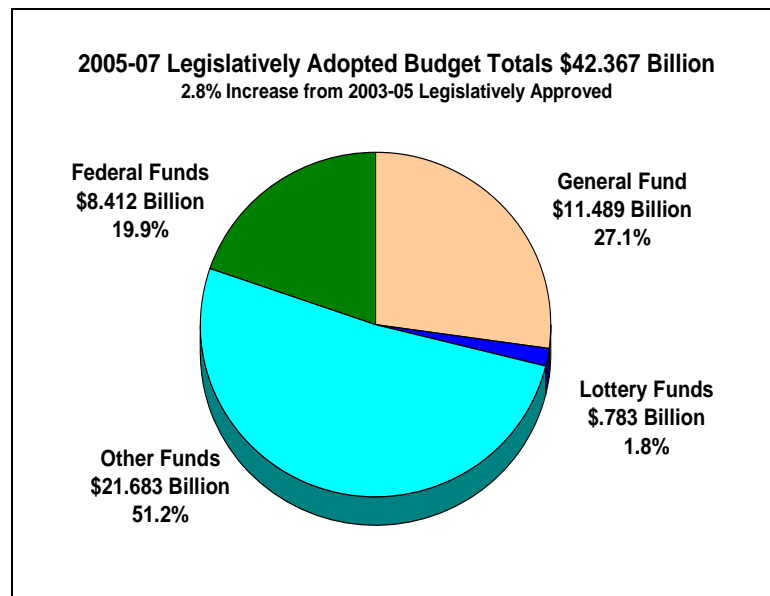
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2005-07 Budget Highlights

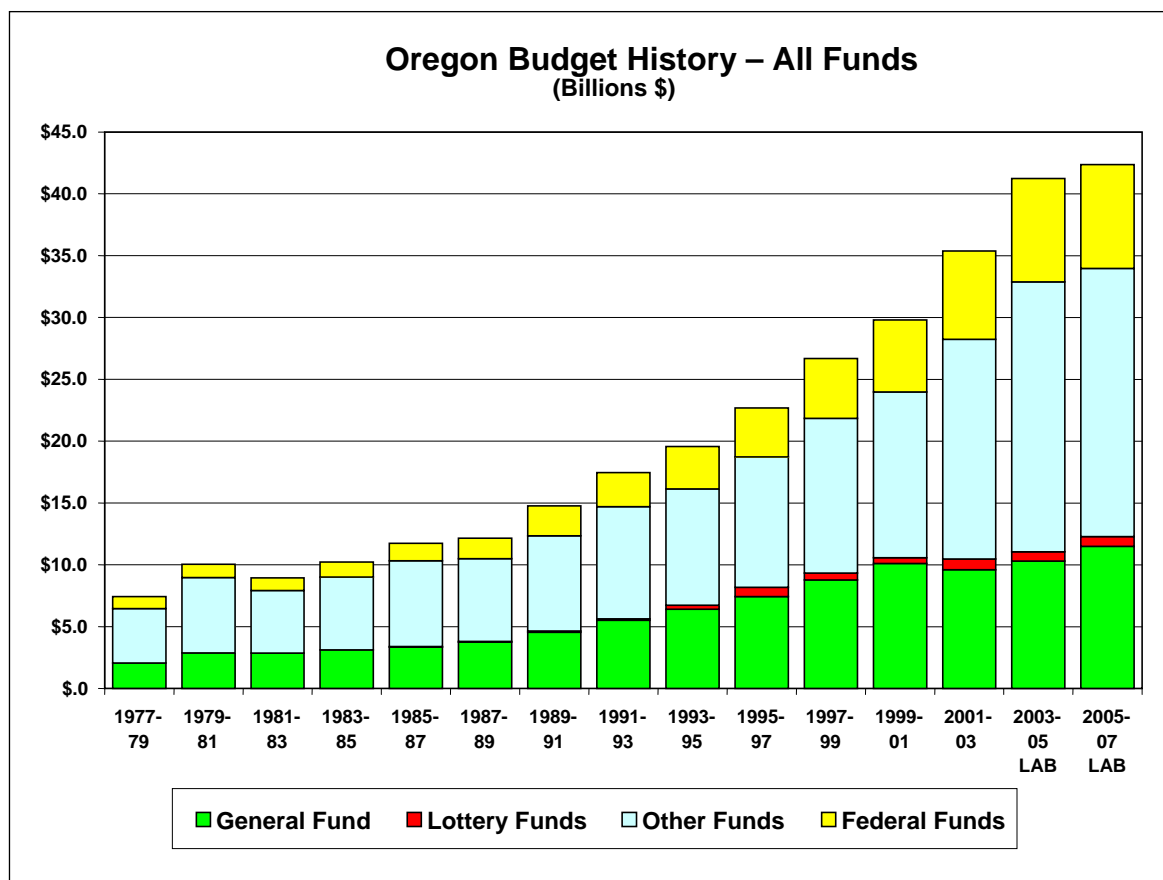
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Budget Overview

The total legislatively adopted budget (**LAB**) for the 2005-07 biennium is \$42.367 billion. The adopted budget includes \$12.272 billion in combined General Fund and Lottery Funds, \$21.683 billion Other Funds, and \$8.412 billion Federal Funds. The 2005-07 total budget represents a 3% increase over the 2003-05 biennium's legislatively approved total budget of \$41.234 billion.



The 2005 Legislature completed the second longest session on record at 208 days. This was one day longer than the 1993 session, but 19 fewer than the record of 227 days in 2003. With respect to the budget development process, the 2005 session was unique in several ways. The Joint Committee on Ways and Means held hearings during the first four months of session, discussing agency performance measures and engaging in a prioritization of agency programs. In March, legislative leadership agreed to a self-imposed spending and revenue cap of \$12.393 billion. In mid-April, the Joint Committee on Ways and Means left Salem for a series of public hearings on the budget throughout the state. Hearings were held in five regions of the state; the Committee also held a teleconference to allow testimony from seven additional sites across Oregon.



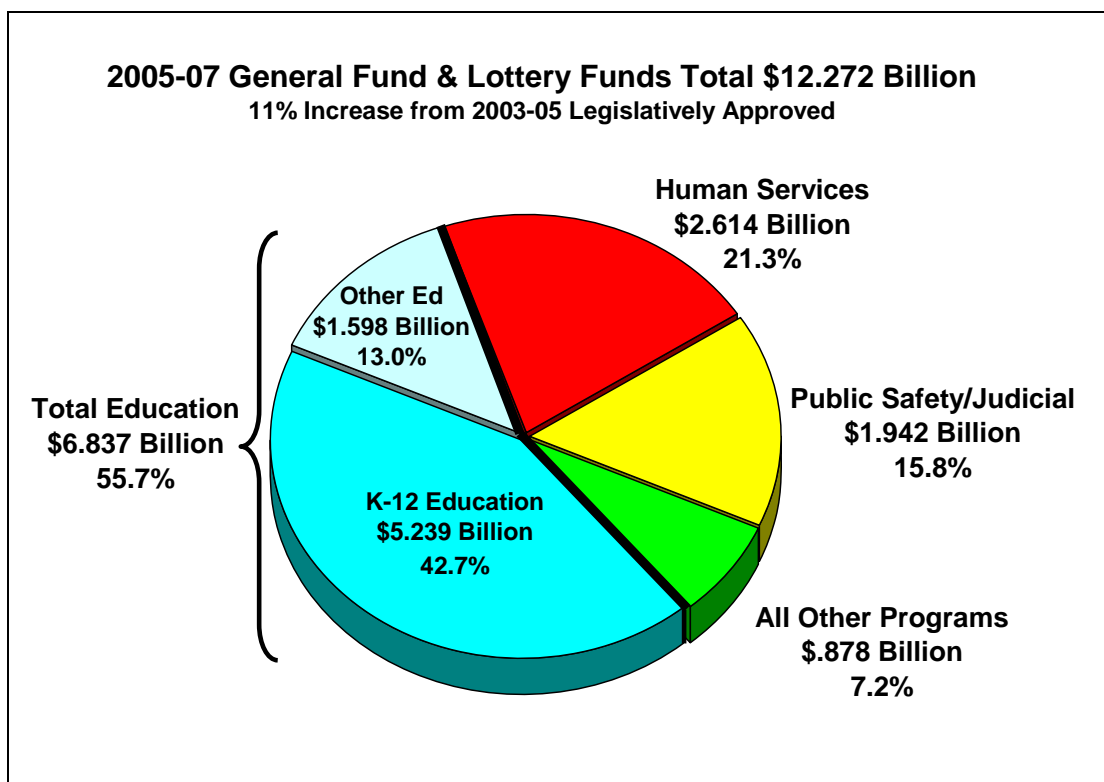
In May, the Joint Committee on Ways and Means turned inactive and special budget committees were formed by the House and Senate leadership. This split the joint appropriation process that is the standard approach for Oregon legislative budget development (a similar split of the joint appropriation process occurred in 1993). Under the split appropriation process, each state agency's budget bill was developed separately by each chamber. Once each chamber had passed a budget for all state agencies, a negotiated agreement allowed those budgets that were passed in identical form by each chamber to be finalized. Legislative leadership then engaged in intensive negotiations over the remaining budgets. The session concluded in August after the Joint Committee on Ways and Means reconvened to develop the final budget bills required to complete the state's balanced budget.

The final \$42.367 billion budget adopted by the Legislature for the 2005-07 biennium represents the smallest total funds percentage increase since the 1987-89 biennium. Although General Fund

and Lottery Funds expenditures were budgeted at 11 percent higher than the previous biennium, Other Funds and Federal Funds experienced only slight changes from the 2003-05 budget period.

The largest funding source in the budget, Other Funds, represents 51 percent of the total expenditures. Other Funds were basically unchanged from the 2003-05 legislatively approved level, down by 0.7 percent, the smallest biennial change since 1987-89. Other Funds are revenues received by the state from fees for registration or licenses, charges for services, specific taxes (such as gasoline and tobacco), and loan programs. These funds are restricted by law for specified purposes.

Nearly 20 percent of the 2005-07 legislatively adopted budget is made up of revenues from the federal government. Federal Funds were up only 0.8 percent in the 2005-07 budget, the smallest increase since a decline in 1981-83. Over the previous five biennial budget periods, Federal Funds have averaged growth of about 19 percent



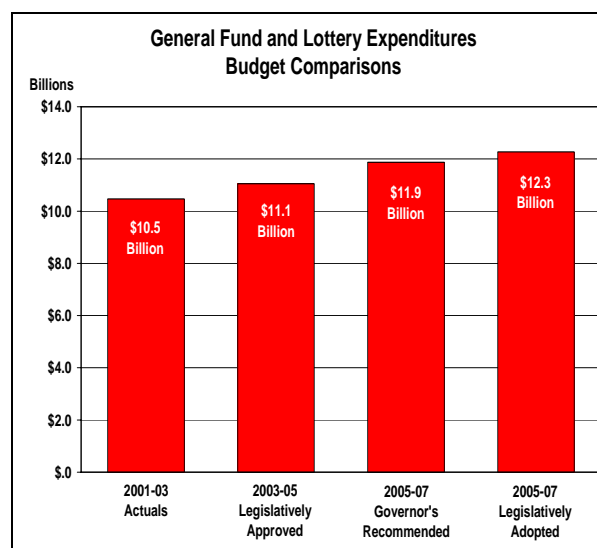
per biennium. Nearly three-fourths of federal funds are received within the Human Services program area.

General Fund and Lottery Expenditures

General Fund and Lottery Funds expenditures, which total \$12.272 billion for the 2005-07 biennium, represent 28.9 percent of the total legislatively adopted budget. Although this percentage is higher than the 26.8 percent share in 2003-05, it is well below the average 34 percent for the period from 1993 through 2003. The reasons for the change in the General Fund and Lottery share of the total budget are the severe drop in General Fund resources during the 2001-03 biennium and an increasing reliance on Other Funds for budget continuity.

The total General Fund and Lottery Funds expenditures of \$12.272 billion for 2005-07 are 11 percent higher than the 2003-05 legislatively approved budget of \$11.052 billion. The 2003-05 legislatively approved budget represents the authorized budget following all Emergency Board actions, reductions automatically

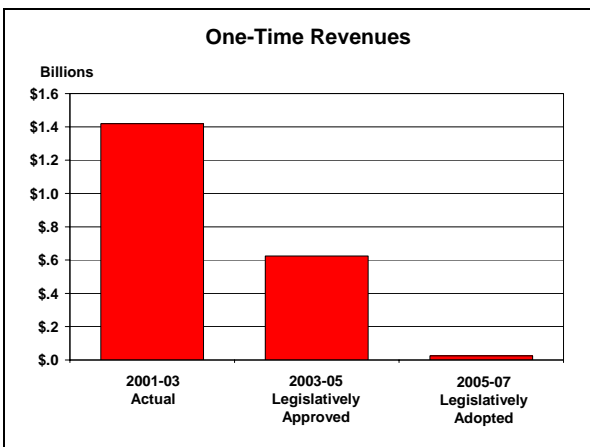
implemented as a result of the voters' defeat of Ballot Measure 30 in February 2004, and various legislative actions taken during the 2005 session to rebalance the budget and adjust limitations for selected agencies.



Nearly 56 percent of the state's General Fund and Lottery expenditures are dedicated to education programs, including \$5.24 billion, or 43 percent of

the total, to the K-12 State School Fund budget. Nearly 93 percent of the state's expenditures are found in the three major program areas of education, human services, and public safety.

About one-third of the \$1.3 billion General Fund and Lottery Funds increase from the 2003-05 LAB to the 2005-07 LAB is due to the Legislature's use of General Fund support to backfill one-time revenues from discretionary sources relied on during the 2003-05 biennium. Reliance on one-time revenues in 2003-05 in part goes back to 2001-03, when the Legislature used approximately \$1 billion of discretionary funds derived from Medicaid Upper Payment Limit (MUPL) revenue, Tobacco Master Settlement Agreement (TMSA) revenue, and the Education Stability Fund as a part of budget rebalancing actions. Additionally, 2001-03 budget balancing actions delayed final General Fund payments into the 2003-05 budget period for K-12 education [\$211 million] and Community Colleges [\$56 million].



For 2003-05, the legislatively approved budget included the use of approximately \$600 million in one-time revenues to replace General Fund. These major one-time sources include:

- \$122 million from the Education Stability Fund for the State School Fund
- \$116 million of federal Jobs and Growth Tax Reconciliation Act funds in the Institutions budget for the Department of Corrections
- \$91.8 million in Other Funds ending balances that were transferred to the General Fund
- \$88.8 million of enhanced federal Medicaid

matching funds in the Department of Human Services

- \$45 million of Other Funds savings from implementation of reforms to the Public Employees Retirement System (PERS) transferred to the General Fund
- \$42.2 million of TMSA funds in the Oregon Health Plan
- \$34 million of General Fund savings from the issuance of pension obligation bonds to pay off the state's unfunded PERS liability
- \$20 million in the natural resource program area from federal Pacific Coastal Salmon Recovery Fund (PCSRF) resources and dedicated Measure 66-Capital Lottery Funds
- \$10 million of Tobacco Use Reduction Account funds in the Oregon Health Plan

Most of these sources of one-time revenues were not available for use in the 2005-07 legislatively adopted budget. The only use of such discretionary funds in the 2005-07 LAB was \$24.5 million of TMSA resources used in the Department of Human Services.

The Lottery Commission's expansion to include line games, and other potential Lottery Commission actions to increase receipts, allowed an additional \$120 million in lottery program funding in the 2005-07 legislatively adopted budget.

More than 75 percent of the \$1.3 billion increase in General Fund and Lottery Funds expenditures from the 2003-05 biennium occurs in three program areas: education, human services, and public safety:

- Education, primarily the State School Fund, increased by \$400 million; this reflects the replacement of one-time funding in 2003-05 from the Education Stability Fund and covers part of increasing salary and benefits costs as well as student growth
- Human Services increased by \$323 million, largely due to replacement of one-time federal fiscal relief funding in 2003-05 and requirements linked to the Medicare Modernization Act
- The Public Safety increase of \$262 million is primarily in the Department of Corrections; this includes the replacement of one-time

2005-07 General Fund & Lottery Spending in Legislatively Adopted Budget by Major Program Area							
(Dollars in Millions) ¹							
	2001-03 Actuals ²	2003-05 Legislatively Adopted Budget	2003-05 Legislatively Approved Budget ³	2005-07 Governor's Recommended Budget (GRB)	2005-07 Legislatively Adopted Budget (LAB)	% Change 2005-07 Legislatively Adopted from 2003-05 Leg. Approved	% Change 2005-07 Legislatively Adopted from 2005-07 Gov. Recommended
Education							
K - 12 State School Fund ⁴	\$4,417	\$5,190	\$4,914	\$5,001	\$5,239	6.6%	4.8%
Higher Education ⁵	754	771	764	750	789	3.3%	5.2%
Community Colleges ⁶	382	413	416	394	433	4.0%	10.0%
All Other Education	335	343	343	389	376	9.7%	-3.4%
Total Education	5,888	6,717	6,437	6,534	6,837	6.2%	4.7%
Human Services ⁷	2,393	2,466	2,369	2,517	2,614	10.3%	3.9%
Public Safety ⁸	1,236	1,246	1,236	1,563	1,495	20.9%	-4.4%
Natural Resources	241	221	227	259	278	22.6%	7.6%
All Other Programs ⁹	710	846	782	1,005	1,047	33.8%	4.1%
Total Expenditures	\$10,468	\$11,496	\$11,052	\$11,877	\$12,272	11.0%	3.3%

¹ Amounts may not add due to rounding.

² The 2001-03 Actuals represent expenditures incurred after all 2001-03 Emergency Board actions, the five 2002 special sessions, the allotment reductions due to the December 2002 revenue forecast (adopted in SB 859), the February 2003 statewide budget rebalance actions (adopted in SB 5548), and the final DHS rebalance (adopted in SB 5549).

³ The 2003-05 Legislatively Approved represents expenditure authorizations through all 2003-05 Emergency Board actions, including \$544.6 million in reductions that resulted from voter disapproval of Ballot Measure 30 in February 2004.

⁴ The 2001-03 Actuals reflect a \$262 million Education Stability Fund transfer (now shown as Lottery Funds per HB 5077) to the SSF and a shift of \$211 million General Fund from the 2001-03 SSF payment to the 2003-05 biennium (SB 1022).

⁵ Includes Oregon Health and Science University Public Corporation.

⁶ The 2001-03 Actuals reflects a shift of \$56 million of the 2001-03 CCSF payment to the 2003-05 biennium.

⁷ The General Fund in the 2003-05 LAB was reduced, in part, based on the availability of an additional \$151.4 million in federal revenue from improved federal match rates authorized in the Jobs and Growth Tax Reconciliation Act.

⁸ The 2003-05 LAB was reduced by \$116 million General Fund based on one-time use of federal Jobs and Growth Tax Reconciliation Act funds.

⁹ The 2003-05 LAB included a \$40 million General Purpose Emergency Fund and \$9 million for health benefits. The 2005-07 GRB included \$25 million in the General Purpose Emergency Fund; \$130 million for employee compensation issues; and \$20 million for Home Care Workers compensation. The 2005-07 LAB includes \$30 million General Purpose; \$130 million for employee compensation; \$10 million for Home Care Workers; \$53.8 million for special purpose appropriations to selected agencies.

federal fiscal relief funding in 2003-05 and the effect of voter-mandated, tougher criminal offender sentencing that continues to cause the prison population to grow. The growth has significantly increased operating and debt service costs over time

The increase in the General Fund and Lottery Funds budget from the Governor's recommended level of \$11.9 billion to the legislatively adopted amount of \$12.3 billion reflects an increase in the economic and revenue forecast used to craft the 2005-07 budget. The Governor's proposed General Fund budget was based on the December 2004 forecast. The May 2005 forecast, used to create the legislative

budget, projected an additional \$426 million General Fund above the December 2004 forecast (\$202 million from an increase in the 2003-05 projected ending balance, which becomes the 2005-07 beginning balance, and \$224 million from increases in projected revenues for 2005-07). The table above compares the 2005-07 legislatively adopted General Fund and Lottery Funds budget with 2001-03 actual expenditures and the 2003-05 legislatively approved budget for each program area.

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