

Commonwealth of Pennsylvania

2003-04

Governor's

Executive Budget

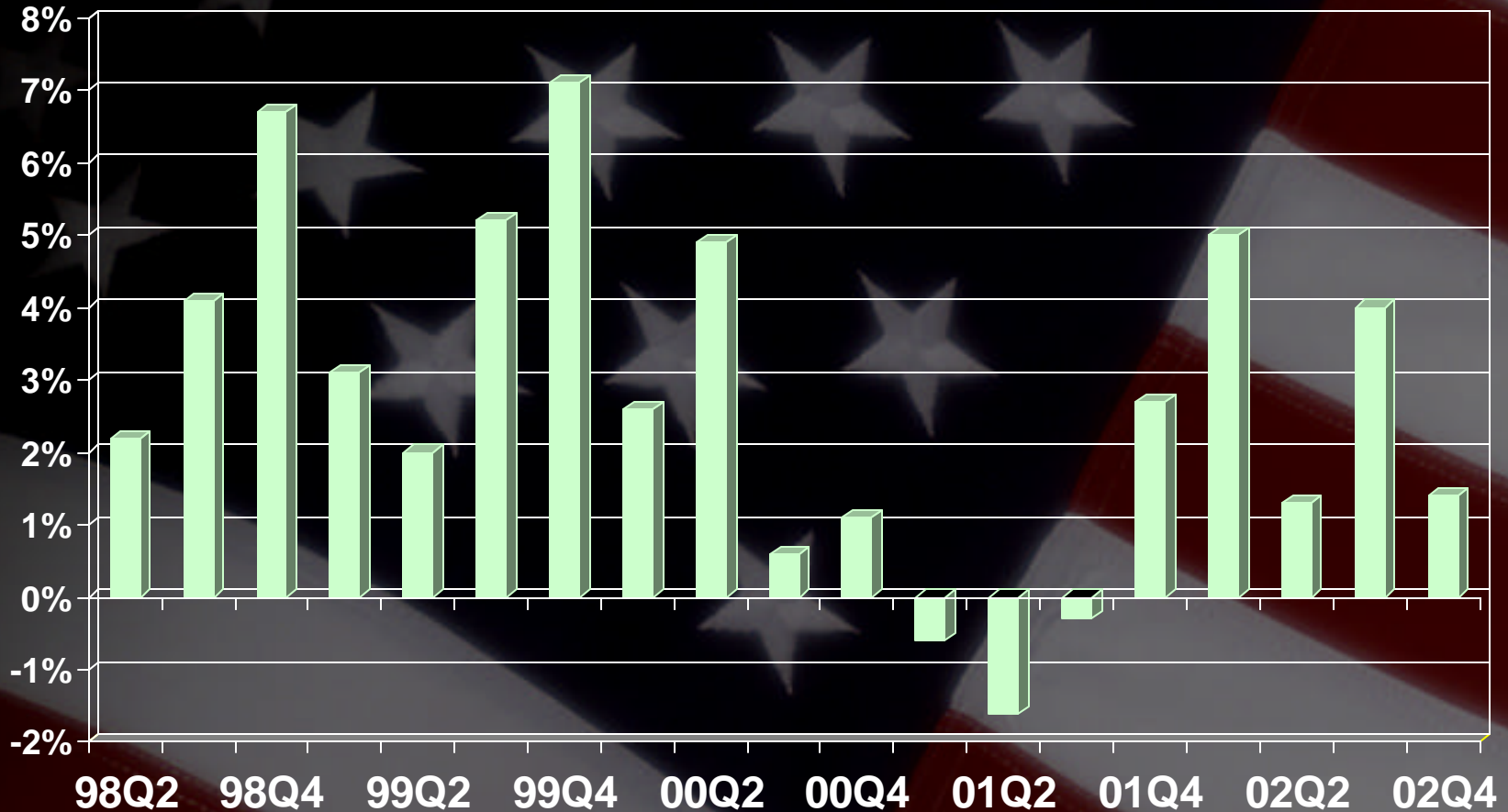


Edward G. Rendell

Governor

Real Gross Domestic Product

Unprecedented Growth
Followed by Sudden Recession
Followed by Fitful Recovery

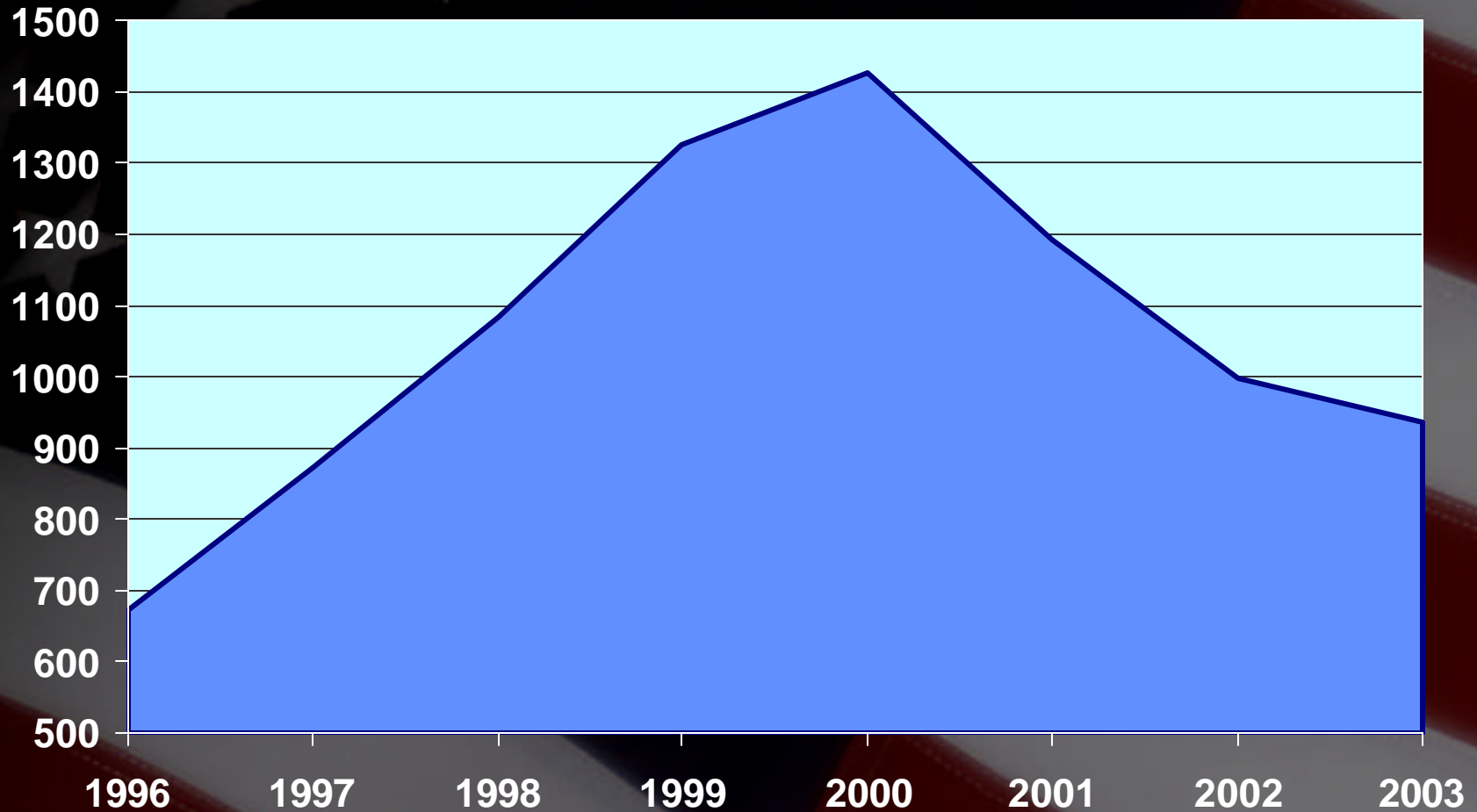


Source: Global Insight Inc./U.S. Bureau of Economic Analysis – Annualized Growth by Quarter/Actual

Standard & Poors 500 Index

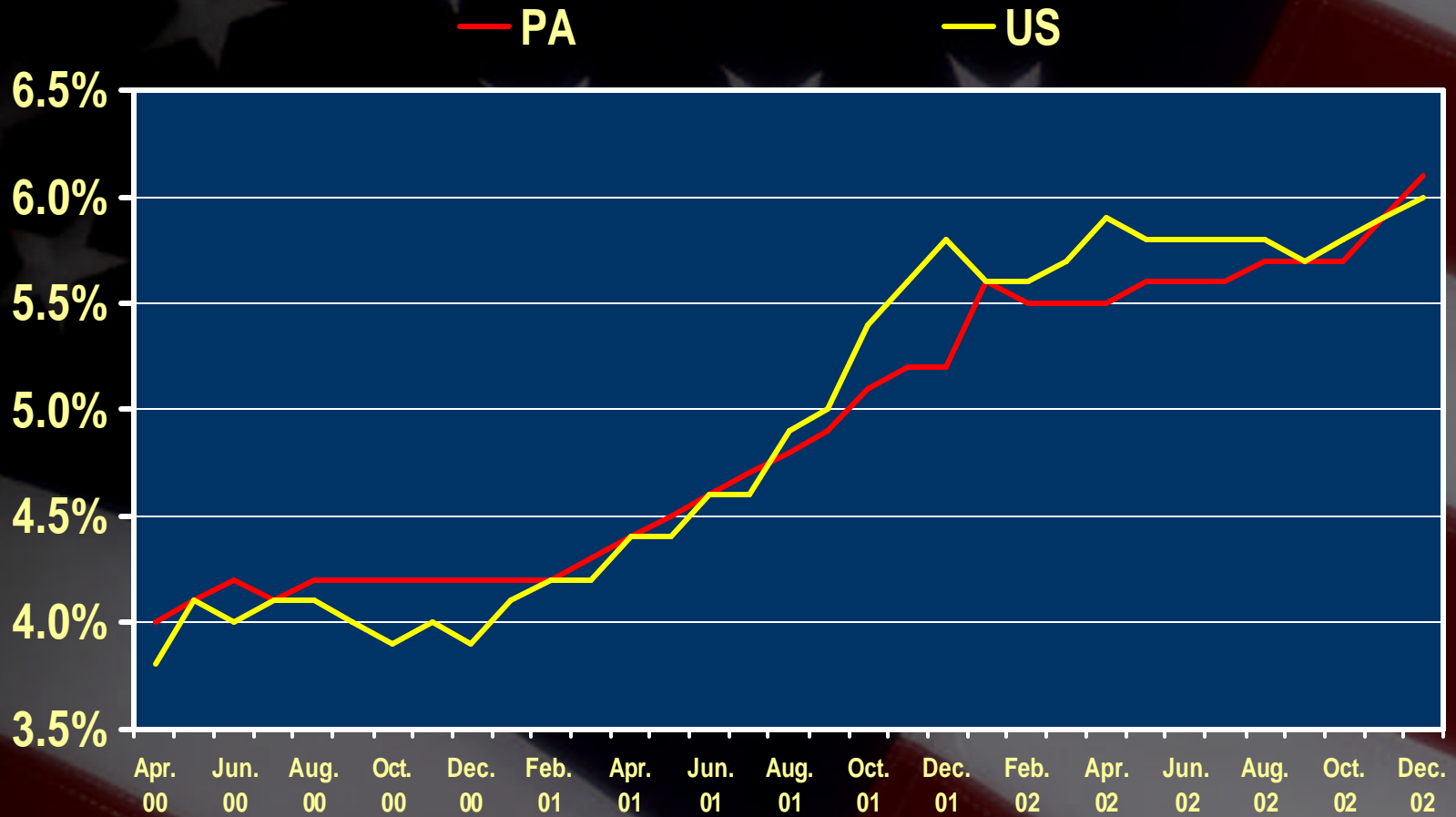
Unprecedented Stock Market Growth in the 90s

Has Been Followed by Sharp Declines



PA and US Unemployment Rates

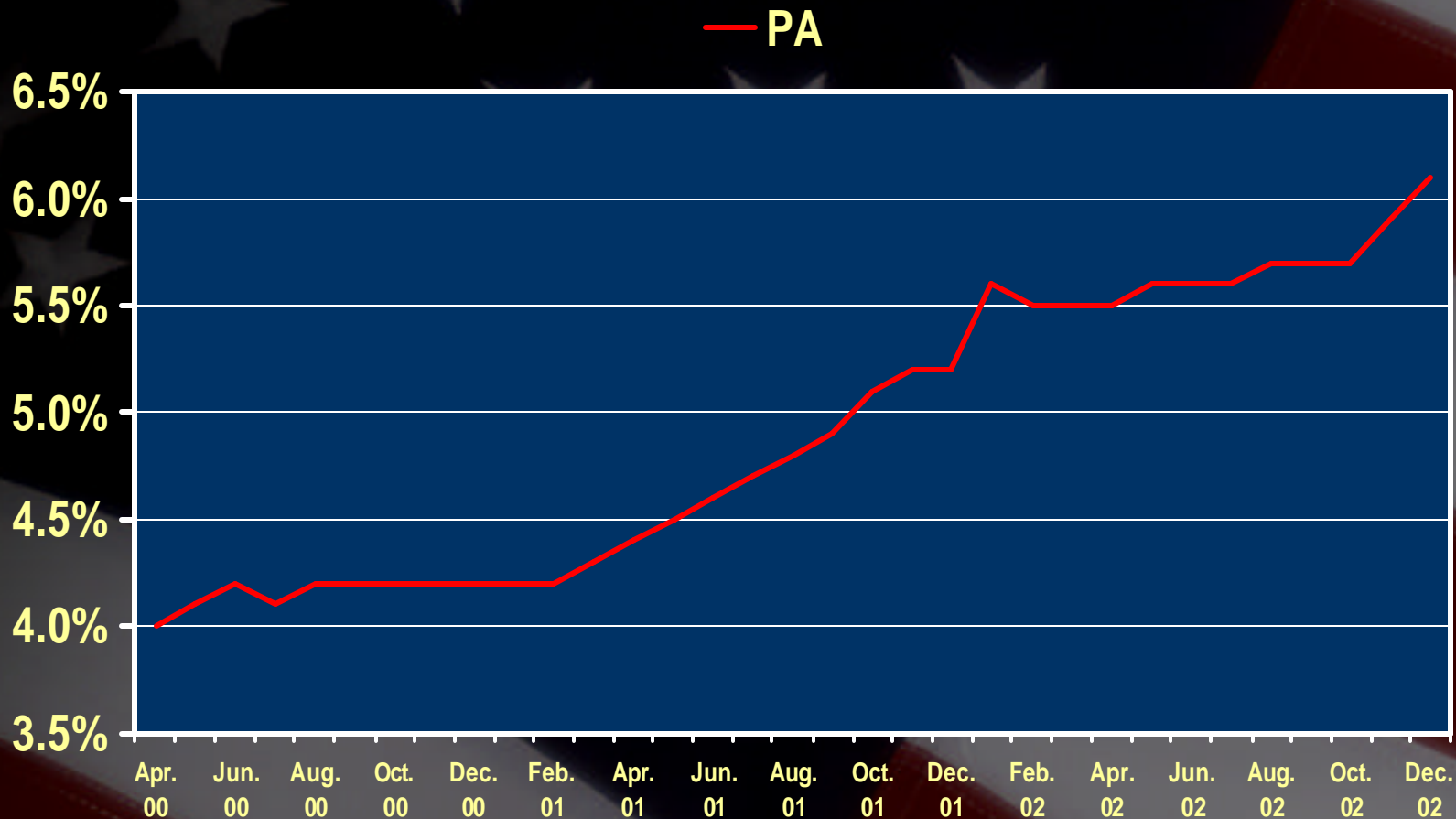
Moving in Tandem – Steadily Upwards



Source: Pa. Dept. of Labor and Industry/U.S. Bureau of Labor Statistics

PA Unemployment Rate

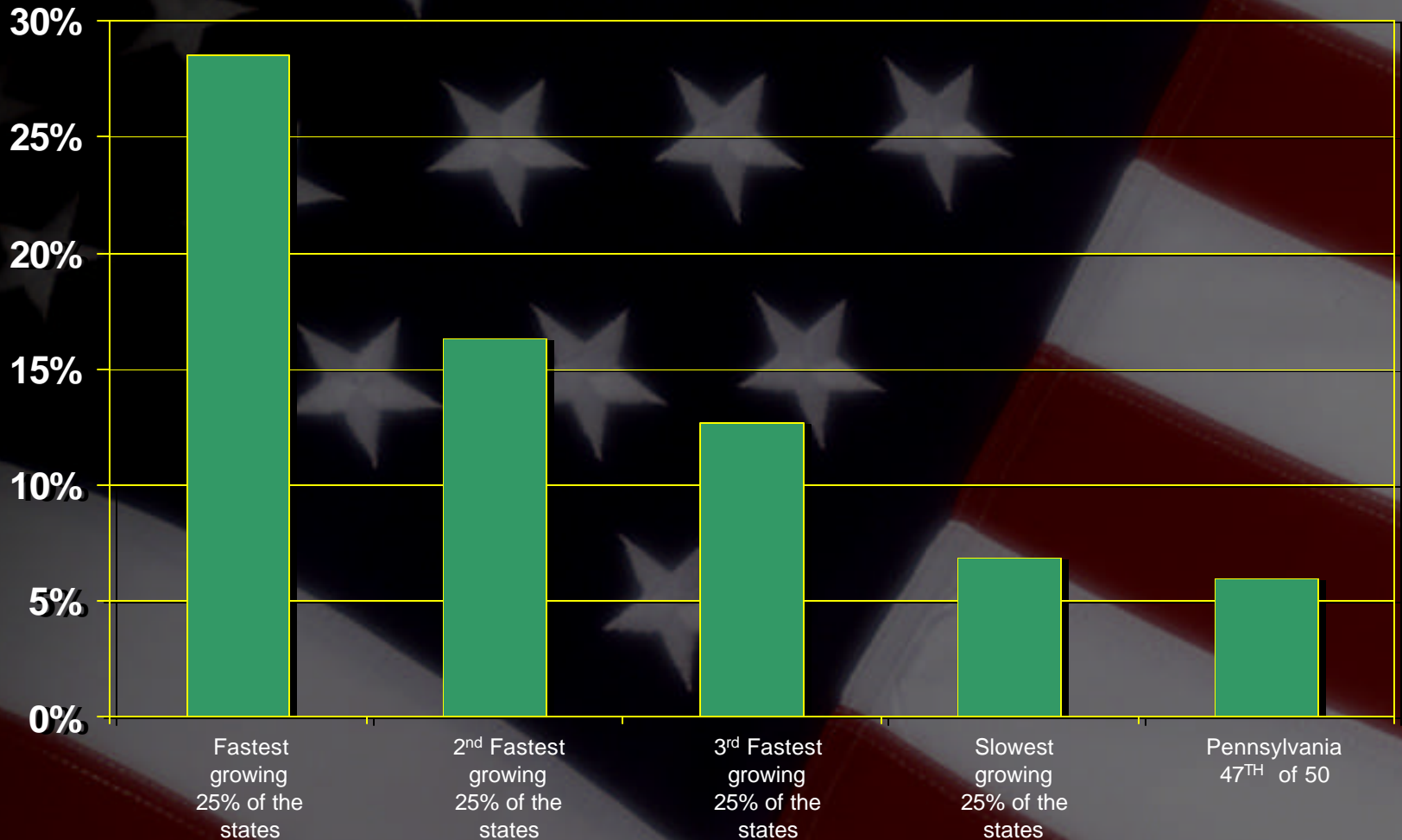
**Growth in Unemployment Rate Accelerated Last Quarter –
Future Prospects are Unclear**



Source: Pa. Dept. of Labor and Industry/U.S. Bureau of Labor Statistics

Comparative Job Creation in the States

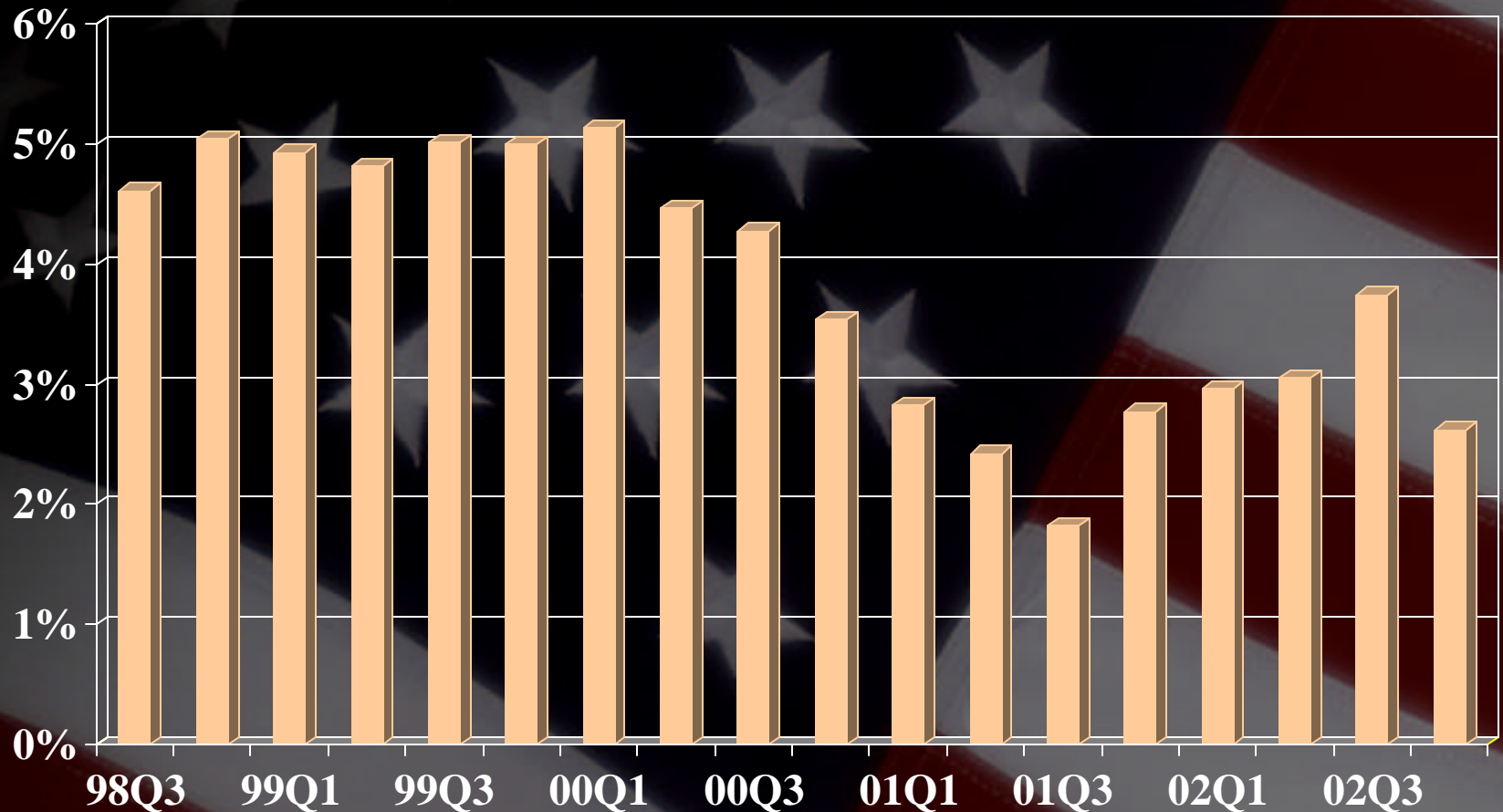
Percent Change in Employment Growth 1992-2002



Source: Corporation for Enterprise Development/U.S. Bureau of Labor Statistics

Real Personal Consumption

The Consumer Has Kept the Economy Going – So Far



Source: Global Insight Inc./U.S. Commerce Department – Year over Year Growth Rate/Actuals

Recent PA Tax Collection Trends

Major General Fund Taxes

Dollars in Millions	Actual Collections 2000-01	Actual Collections 2001-02	Revised Estimated Collections 2002-03	Estimated Collections 2003-04
Personal Income Tax	\$ 7,491.5	\$ 7,138.7	\$ 7,090.4	\$ 7,390.6
Corporate Net Income	1,603.4	1,418.5	1,421.8	1,456.4
Capital Stock & Franchise	1,063.0	913.4	901.6	873.6
Sales and Use	7,203.7	7,292.5	7,518.8	7,767.7
Motor Vehicle	1,080.0	1,161.8	1,215.2	1,234.0
Non-Motor Vehicle	6,123.7	6,130.7	6,303.6	6,533.7
Total	\$17,361.6	\$16,763.1	\$16,932.6	\$17,488.3
Difference from 2000-01		-598.5	-429.0	126.7

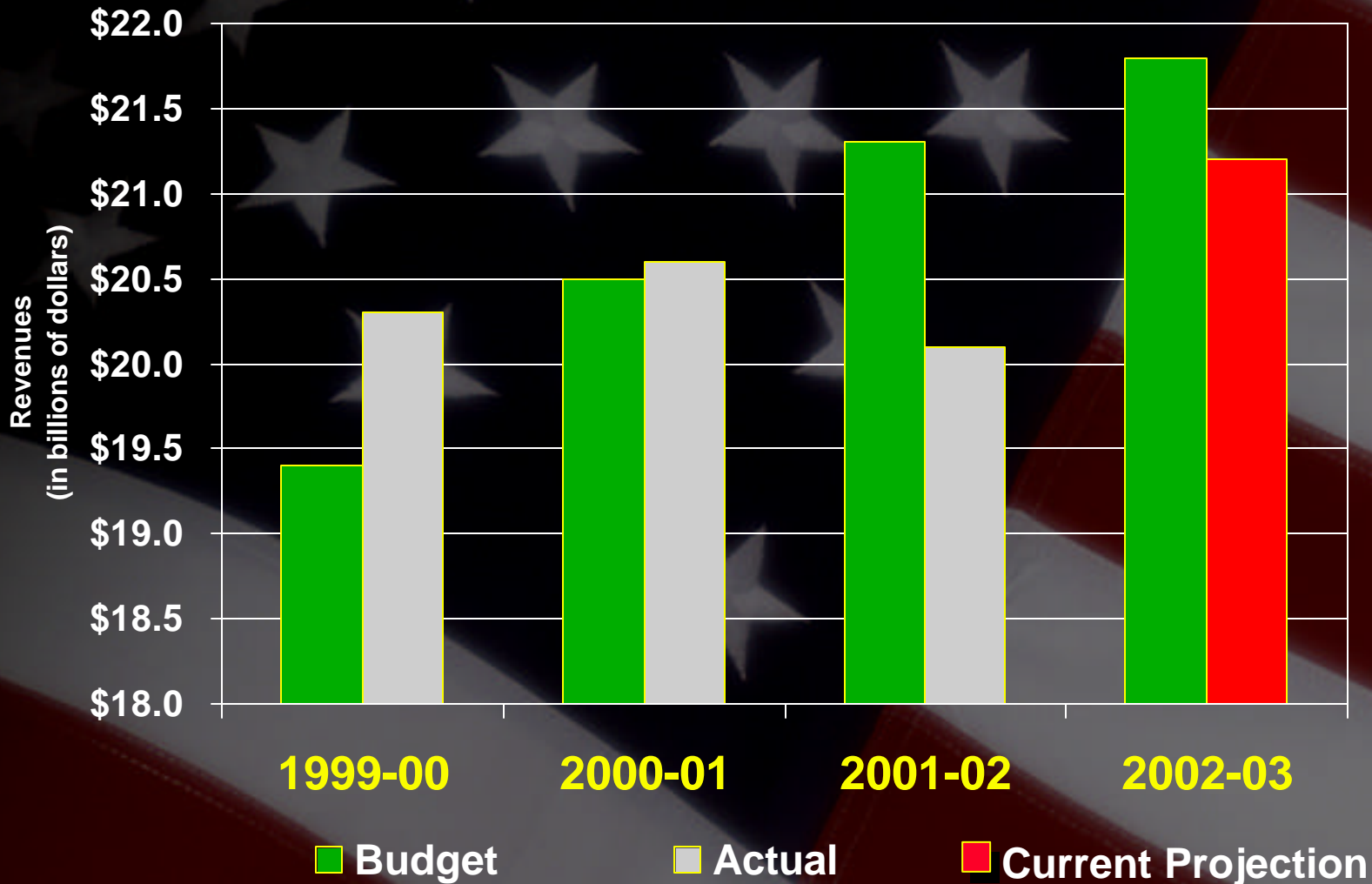
Major General Fund Taxes

Recent Growth/Decline Trends

(percent change)

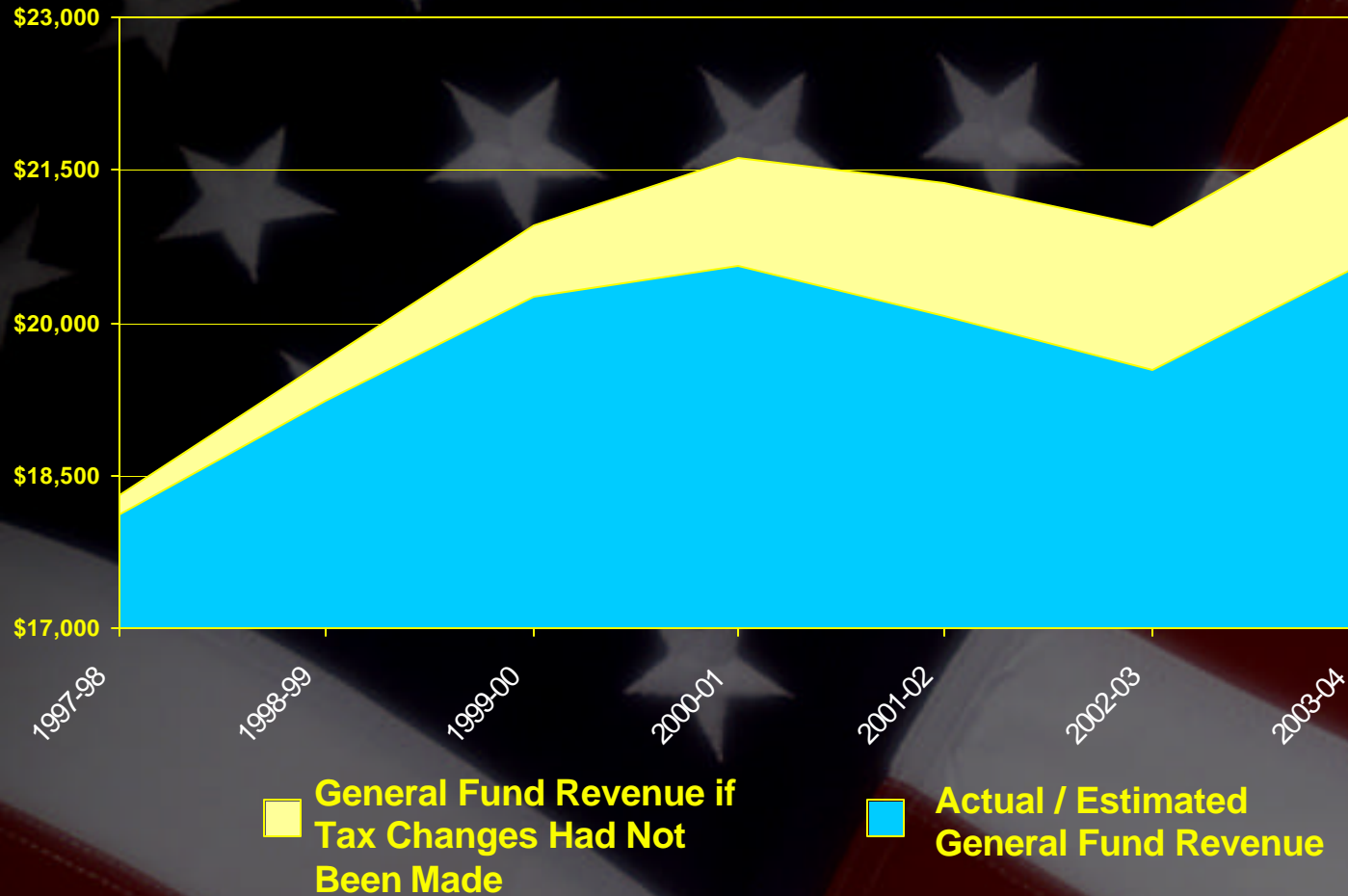


General Fund Revenues Forecast vs. Actual Collections



How Recent Tax Changes Have Reduced PA Revenue Collections

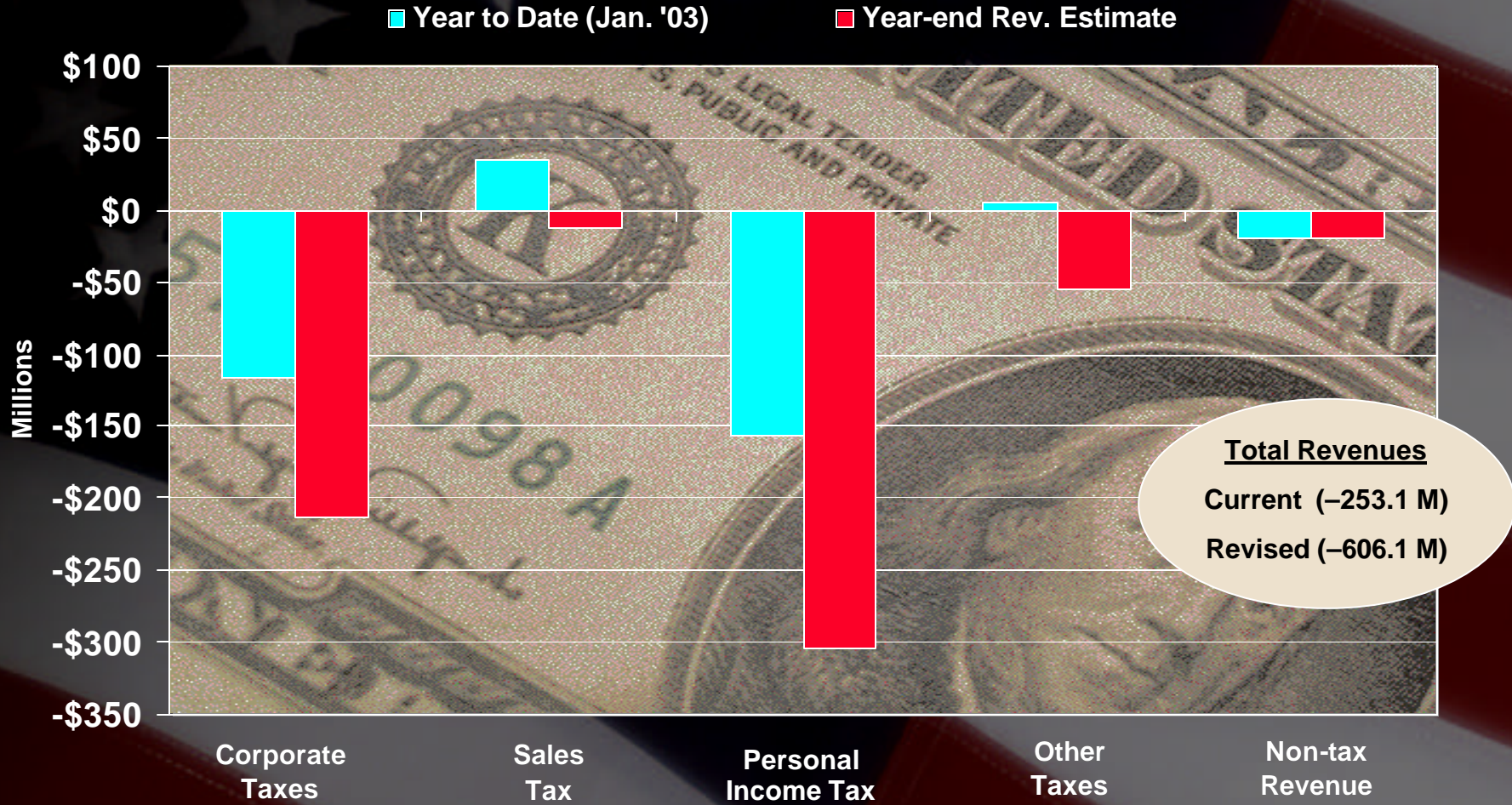
(Collections in Millions)



General Fund base collections represent estimated collections before tax law changes.

GENERAL FUND

Actual and Revised 2002-03 Revenues Compared to Original June 2002 Estimate



One-Time Items Utilized to Balance The 2002-03 General Fund Budget

Revenues:

	<u>Millions</u>
One-Time Benefit – Decoupling from Federal Depreciation Tax Treatment	\$ 350.1
One-Time Benefit – Various Escheat Changes	197.6
Reduction in Scheduled Rate Cut – Capital Stock and Franchise Tax	144.5
One-Time Extraordinary Increase – Transfer from State Stores Fund (over \$50M)	105.0
Loan from Underground Storage Tank Fund	100.0
Other	91.3
Revenue Subtotal	\$ 988.5

Expenditures:

Accelerated Drawdown of Public Welfare’s Intergovernmental Transfer Funds Reserves	\$ 550.0
Reduction in Debt Service Due to Securitization of PA Industrial Development Authority Revenues	258.4
One-Time Use of Unspent Tobacco Settlement Funds Due to Delays in Implementation of Tobacco Fund Programs	198.5
Use of Debt to Fund Projects Previously Funded Out of the Operating Budget	90.0
One-Time Use of Federal Reimbursements to Cover Some Public Welfare Costs	60.0
Other	52.3
Expenditure Subtotal	\$ 1,209.2

TOTAL \$ 2,197.7

The Projected FY 03-04 Budget – Prior to Corrective Action

	(Dollar Amounts in Thousands)			
	2002-03 Available	2003-04 Budget	\$ Change	% Change
Beginning Balance	\$ 142,535	\$ -36,007		
<u>Revenue</u>				
<i>Receipts – Existing Revenue Sources</i>	20,138,900	\$ 20,560,500		
<i>add: New Recurring Revenues (Added in FY2002-03)</i>	692,800	781,000		
Total Recurring Revenues (Budgeted)	20,831,700	21,341,500	\$ 509,800	2.4%
<i>less: Revenue Shortfall – Receipts Lower Than Projection</i> ..	-606,100	.....	
Total Recurring Revenues	20,225,600	21,341,500	\$ 1,115,900	5.5%
<i>add: Non-Recurring Revenue Sources – FY2002-03</i>	988,500	.....	
Total Revenue Prior to Refunds	21,214,100	21,341,500	\$ 127,400	0.6%
<i>less: Refunds</i>	-929,600	-1,062,200		
Total Revenue	\$ 20,284,500	\$ 20,279,300		
<i>add: Prior Year Lapses</i>	93,500	.....	
Funds Available	\$ 20,520,535	\$ 20,243,293	\$ -277,242	-1.4%

The Projected FY 03-04 Budget – Prior to Corrective Action

	(Dollar Amounts in Thousands)			
	2002-03 <u>Available</u>	2003-04 <u>Budget</u>	\$ Change	% Change
Expenditures:				
Initial Appropriation – FY 2003-04 Base		\$ 21,906,326		
<i>add: Projected Increase in Public Welfare Costs</i>		478,477		
<i>add: Increase in School Employees' Retirement Costs</i>		123,181		
<i>add: Projected Increase in Corrections Costs</i>		150,766		
<i>add: All Other Base Cost Adjustments</i>		–12,770		
Appropriations (prior to One-Time Cost Avoidance actions)	\$ 21,906,326	\$ 22,645,980	\$ 739,654	3.4%
<i>less: One-Time Cost Avoidance – FY2002-03</i>	–1,209,200	. . . . .	
Appropriations Adjusted for One-Time Cost Avoidance	\$ 20,697,126	\$ 22,645,980	1,948,854	9.4%
<i>add: Supplemental Appropriations</i>	\$ 16,670	. . . . .	
Total Appropriation	\$ 20,713,796	\$ 22,645,980		
<i>less: Current Year Lapses</i>	–407,254	. . . . .	
Total Expenditures	\$ 20,306,542	\$ 22,645,980	\$ 2,339,438	11.5%
 Preliminary Balance	 \$ 213,993	 \$ –2,402,687		
 Use of Budget Stabilization Fund				
<i>Transfer (to) the Budget Stabilization Fund</i>	\$ –300,000	. . . . .	
<i>less: Transfer from Budget Stabilization Fund</i>	50,000	. . . . .	
Net Transfer (to)/from Budget Stabilization Reserve Fund	–250,000	. . . . .	
 Ending Balance	 \$ –36,007	 \$ –2,402,687		

Proposed FY 2003-04 Budget

AFTER Corrective Budget Balancing Actions

	<u>Millions</u>	
	<u>2002-03</u>	<u>2003-04</u>
Beginning Balance	\$ 143	\$ -36
Receipts	20,370	20,279
Revenue Enhancements	8	518
Funds Available	\$ 20,521	\$ 20,761
2003-04 Initial Appropriation Base ..	. . . .	\$ -22,646
2003-04 Corrective Action .....	. . . .	1,638
Appropriated	- 20,714	- 21,008
Lapses	407	. . . .
Preliminary Balance	\$ 214	\$ -247
Transfer from Rainy Day Fund	50	250
Transfer to Rainy Day Fund	-300	- 1
Ending Balance	\$ -36	\$ 2

The Administration's Approach to Closing the Budget Gap

- ✓ ***Leave no stone unturned***
- ✓ ***Substantially reduce reliance on non-recurring budget balancers***
- ✓ ***Cut bureaucracy first — and deeply as possible // prudent***
- ✓ ***Limit cuts that adversely affect Pennsylvania's people – especially most vulnerable populations***

Economic Assumptions Used to Construct the FY 2003-04 Revenue Estimate

- ✓ **Projection assumes a short / successful war with Iraq ending in the 1st half of 2003.**
- ✓ **Moderate growth in Real GDP is projected in 2003 with greater growth in 2004.**
- ✓ **Consumer and business confidence projected to increase in the 2nd half of 2003.**
- ✓ **Job growth projected to resume in the latter part of 2003.**

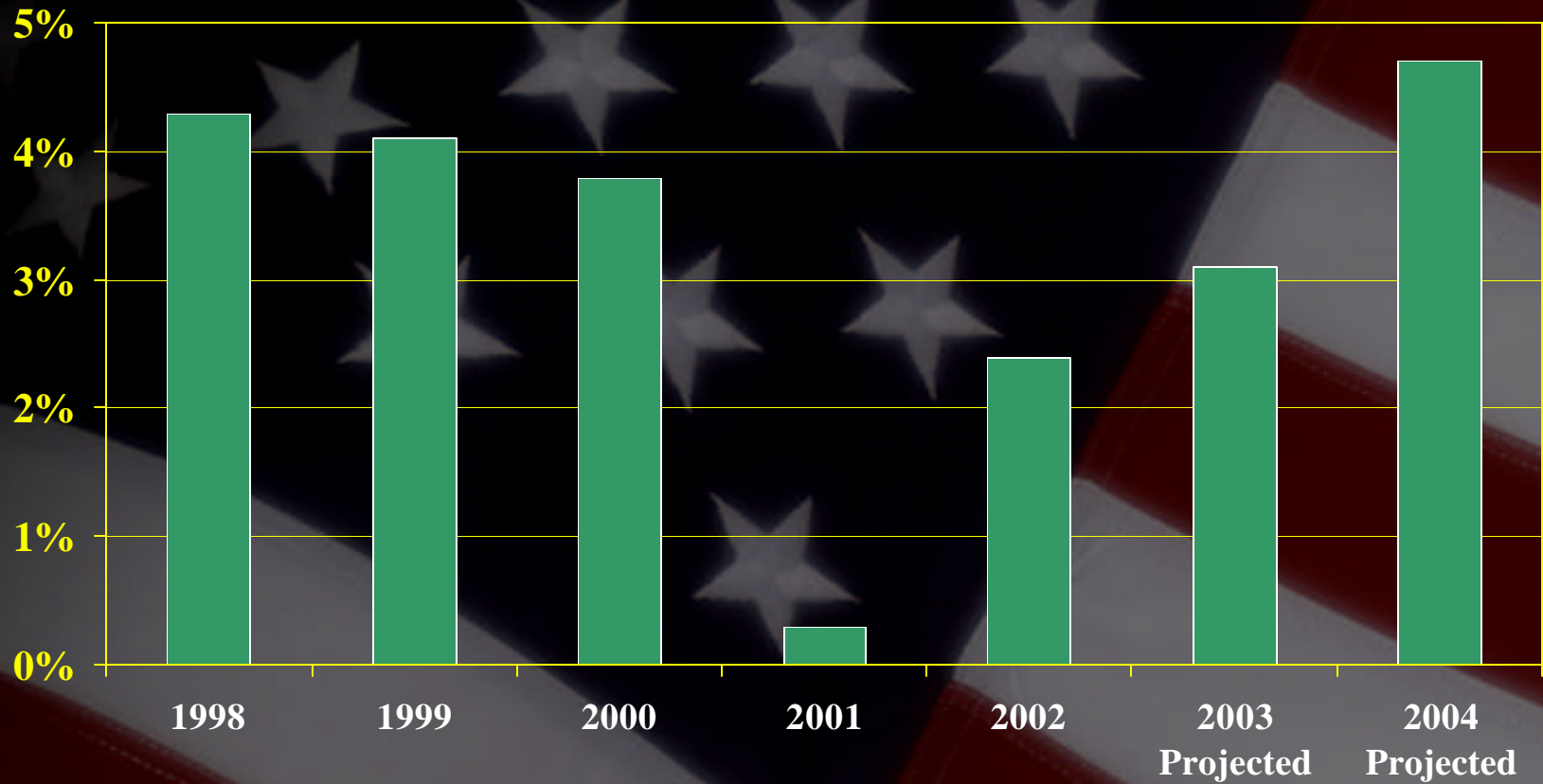
Economic assumptions are far from worst case.

Current climate is volatile and uncertain.

Assumptions will have to be assessed continually through the Spring to determine if the current revenue estimate continues to be viable.

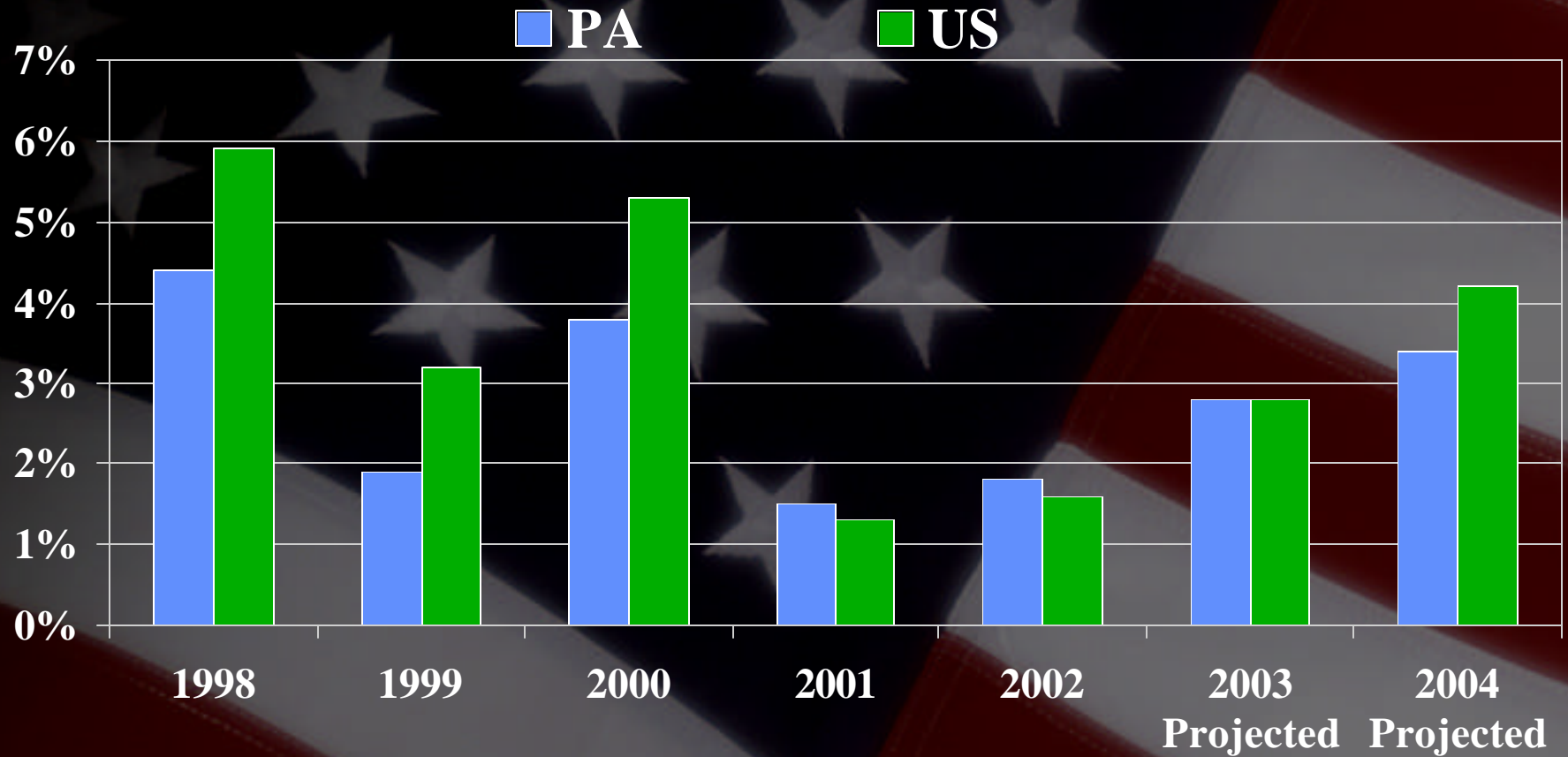
Real Gross Domestic Product

Annual Growth

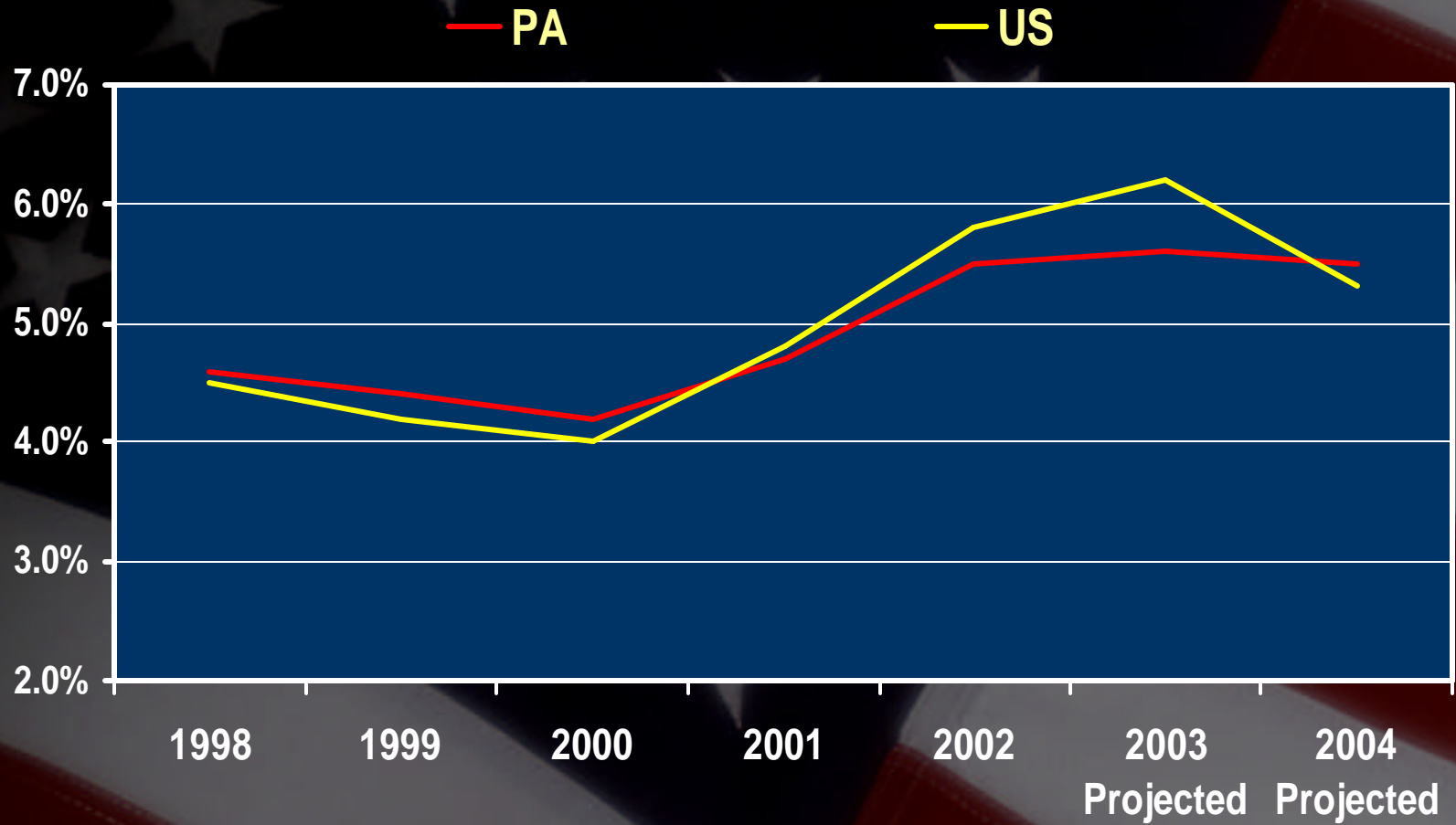


PA and US Real Personal Income

Annual Percent Growth



PA and US Unemployment Rate



2003-04 Revenue Enhancements

- **Tax Revenue:**

Delay Capital Stock and Franchise Phase Out	\$ 52.6 M
Revenue Enforcement Enhancements	\$ 13.5 M
Interest Paid by Commonwealth	\$ 2.3 M

- **Non-Tax Revenue:**

Tobacco Settlement Fund	\$ 330.0 M
Escheats	\$ 90.0 M
Fee Increases	\$ 29.3 M

Sub Total \$ 517.7 M

• **Rainy Day Fund** \$ 250.0 M

TOTAL \$ 767.7 M

2003-04 Revenue Enhancements

Revenue Enforcement Enhancements

- Enhance citation authority
- Tax clearances prior to renewal of business licenses
- Commonwealth parity with local governments on wage garnishment

Fee Increases

- Increase in selected licenses and fees to catch up with inflation
- Some licenses and fees have not been increased in more than 20 years

2003-04 Expenditure Summary

- ✓ The proposed 2003-04 General Fund budget is **\$21.0 Billion**
 - An **increase of \$295 million, or 1.4 %**

Extraordinary Increases over 2002-03 funding levels:

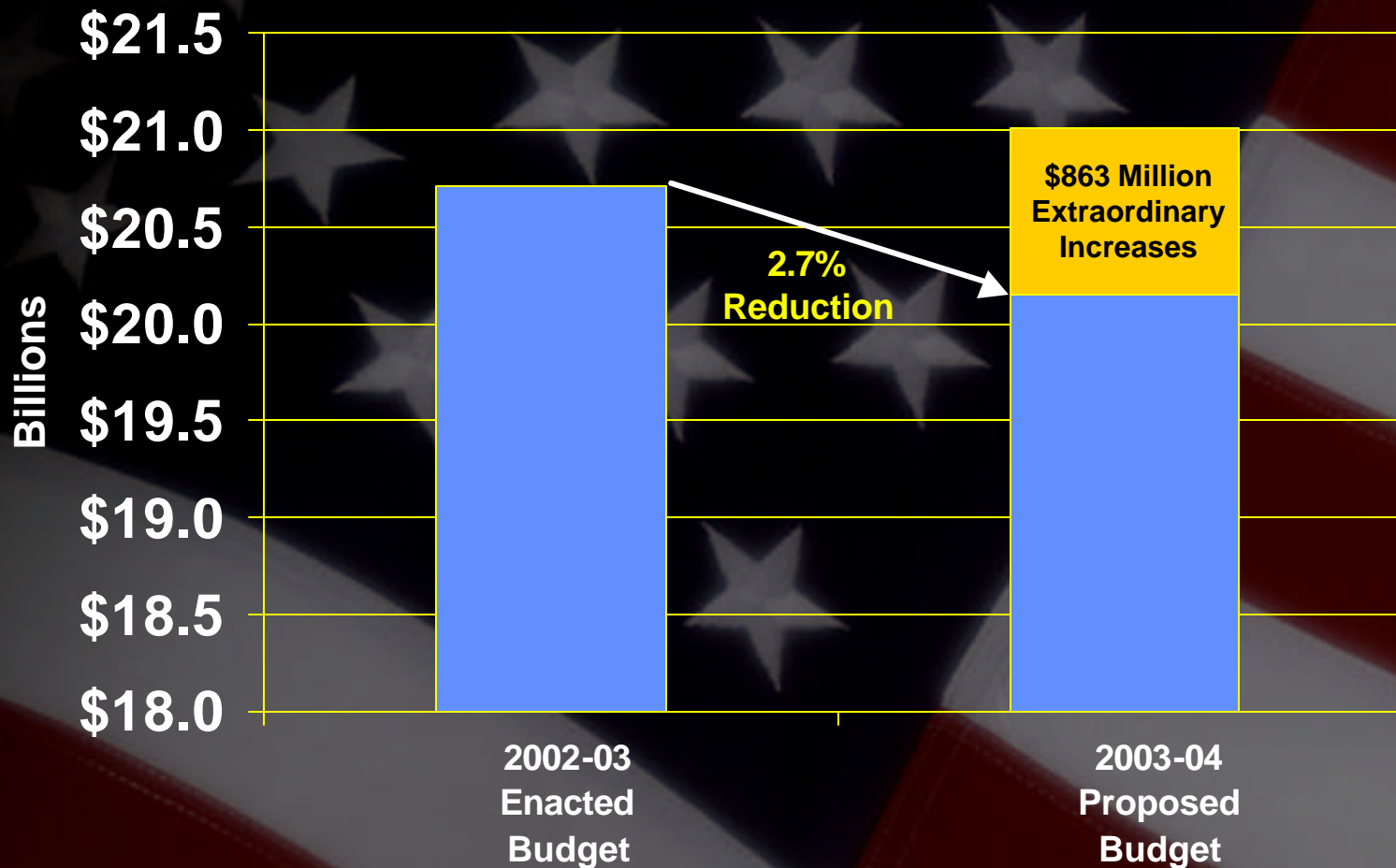
- Medical Assistance	\$ 420 M
- Debt Service	\$ 320 M
- School Employees' Retirement	\$ 123 M

Subtotal	\$ 863 M
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- ✓ The remainder of the General Fund budget has a **net reduction of \$568 million, or 2.7%**, from the 2002-03 enacted budget.

Growth in 2003-04 Expenditures

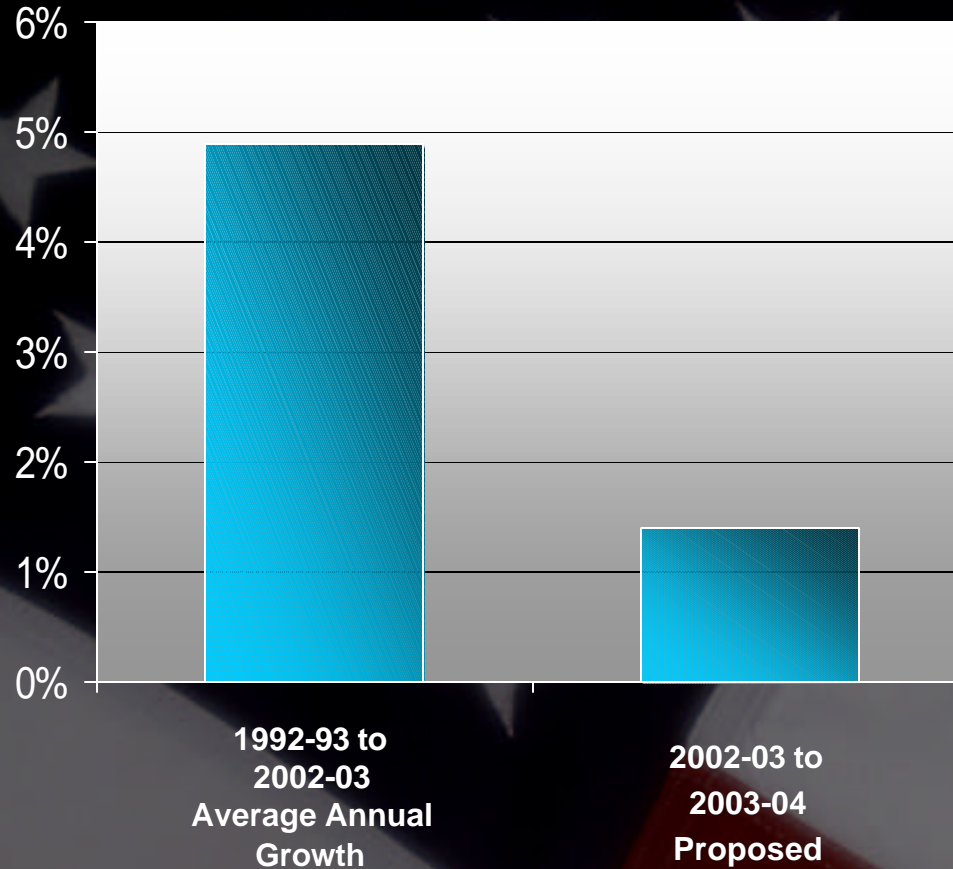
With and Without Extraordinary Expenditure Growth Items



Growth in General Fund Expenditures

The 2003-04 Budget

Compared to Recent Growth Trends



Percentage Growth Rate

2003-04 Expenditures – Reductions

- **Selected Funding Reductions:**

10% Cut in General Government Administration	\$ –211.8 M
Sewage Treatment Plant Operations Grants	\$ –52.1 M
Behavioral Health Services	\$ –47.9 M
Improvement of Library Services	\$ –37.6 M
State-Related Universities	\$ –34.1 M
State System of Higher Education	\$ –22.9 M
Mass Transportation Assistance	\$ –16.1 M

2003-04 Expenditures – Major Items Maintained/Increased

- **Funding Increases:**

Economic Development

Opportunity Grants	\$ 22.0 M
Remodel Pennsylvania Initiative	10.0 M
Main Street Initiative	5.0 M
Elm Street Initiative	5.0 M

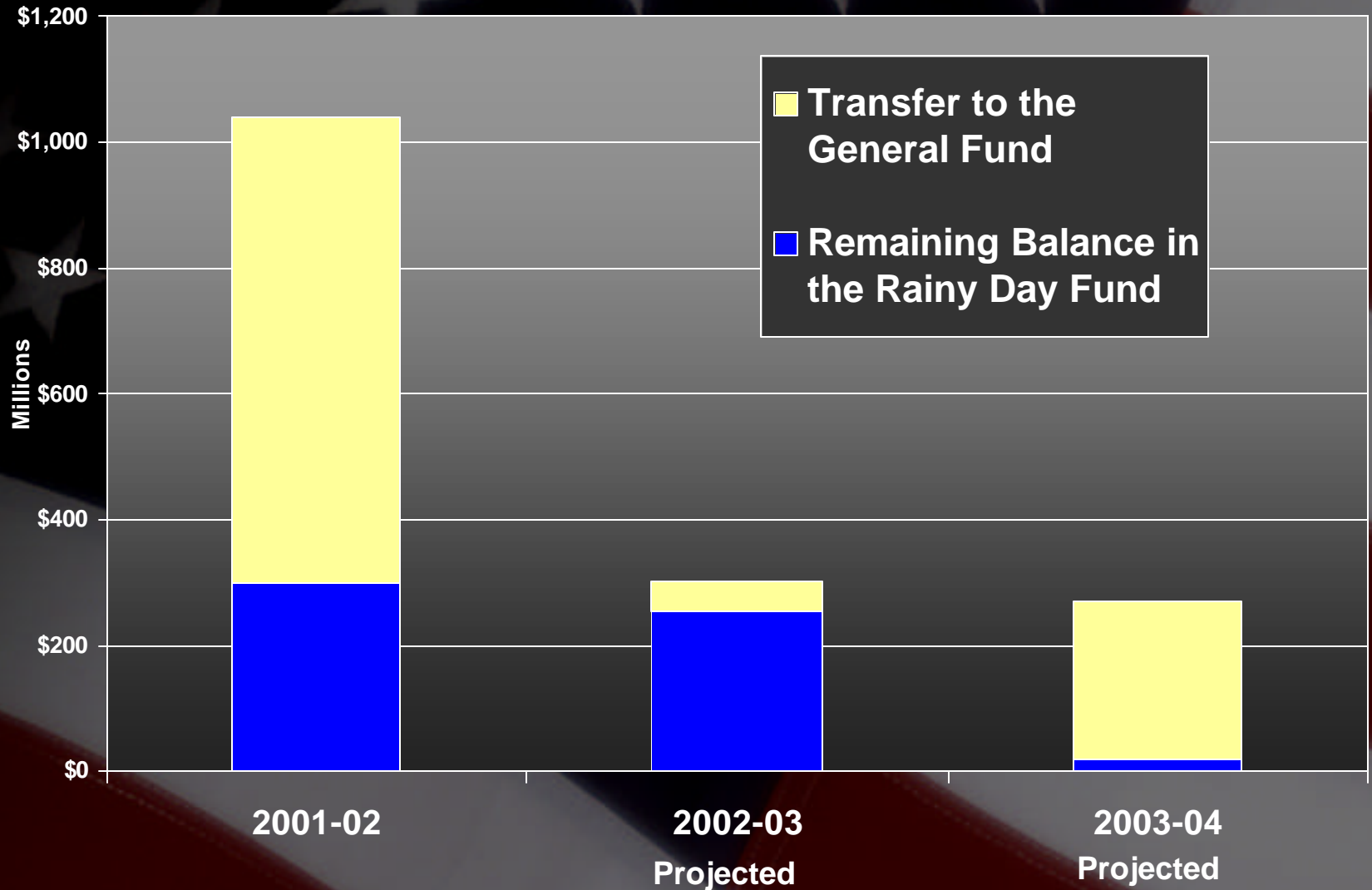
Total	\$ 42.0 M
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Corrections	\$ 32.2 M
Mental Health Services	\$ 31.6 M
Volunteer Company Grants	\$ 25.0 M
Veterans Homes	\$ 7.0 M

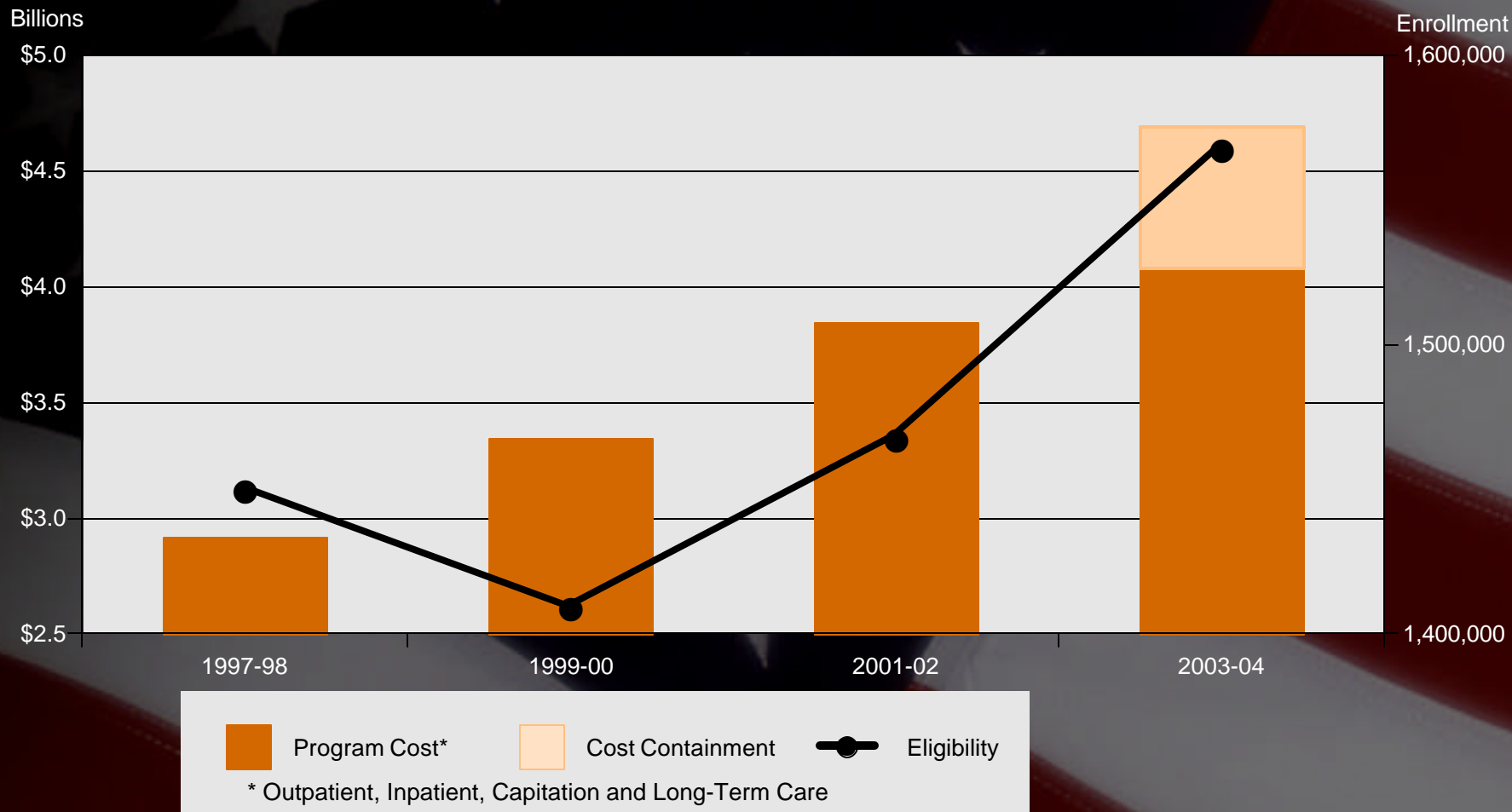
- **Funding Maintained:**

Basic Education Funding	\$ 4,086 M
Special Education	\$ 874.3 M
Grants to Students	\$ 347.9 M

Status of the Rainy Day Fund



PA's Medical Assistance Program Current Cost and Enrollment Trends



PA's Medical Assistance Program

Budget Adjustment Alternatives Rejected

- Eliminate all MA optional services including pharmacy \$355 M
- Eliminate Medically Needy Only category of eligibility \$291 M
- Eliminate all state-only programs
(GA, State Blind Pension) \$255 M

Key Elements of DPW's 2003-04 Medical Assistance Cost Containment Strategy

- ✓ **No Cuts in Eligibility**
- ✓ **No Cuts in Optional Services**
- ✓ **Aggressive Review of Provider Rates**
- ✓ **Slow or No Growth in Most Discretionary Programs**
- ✓ **Some Adjustments to Mandatory Programs**
- ✓ **Rigorous Examination of Business Practices and Program Effectiveness**

Community Care Program Increases

Community Care Program Increases — 1,763 Additional Persons Served

● Mental Retardation	\$ 8.5 M
● Early Intervention	7.9 M
● Developmental Disability Services.....	4.6 M
● Attendant Care	5.7 M
● Mental Health	2.6 M
Total	<u><u>\$29.3 M</u></u>

Other Public Welfare Budget Adjustments

- **Program Reductions –**

Human Services Development Fund	\$	–33.3 M
Homeless Assistance	\$	–1.2 M
Domestic Violence	\$	–0.6 M
Rape Crisis	\$	–0.3 M
Community Based Family Centers	\$	–0.2 M

- **Further Program Reductions Avoided Through –**

Use of Intergovernmental Transfer Reserves	\$	250.0 M
New Resources from Nursing Home Assessment	\$	145.0 M

It could always be worse...

**Other states' current year budget challenges -
compared to PA's \$606 million 2002-03 shortfall**

- ✓ **California – \$8.5 billion**
- ✓ **New York – \$2.5 billion**
- ✓ **New Jersey – \$1.1 billion**
- ✓ **Virginia – \$950 million**
- ✓ **Oregon – \$900 million**

What Happens Next?

- ✓ **The General Assembly conducts hearings to review the impact of the proposed budget on the Commonwealth and its citizens.**
- ✓ **The Revenue Department and the Governor's Budget Office monitor economic trends and actual revenue collections to determine whether the current revenue estimate for 2003-04 is sustainable.**
- ✓ **The Rendell Administration continues to explore all available avenues to enhance non-tax revenues, including Federal sources, to permit the reduction and/or elimination of some cuts in the 2003-04 budget, if possible.**
- ✓ **Governor Rendell submits his proposals to the legislature for property tax relief and tax reform, revitalization of the economy of the Commonwealth, and improved achievement in public schools -- with a detailed funding plan to support these initiatives.**