



COMMONWEALTH OF PENNSYLVANIA  
OFFICE OF THE GOVERNOR  
HARRISBURG

THE GOVERNOR

February 8, 2006

To the People of Pennsylvania:

In the three years since I took office, I have worked on many fronts to better the lives of all Pennsylvanians. Working together with the members of the General Assembly, my administration has made extraordinary improvements in the efficiency and effectiveness of our state government and equally extraordinary improvements in the services our state government delivers to children, older adults, families, businesses and communities.

My three priorities have been to raise student achievement levels, grow our economy, and improve the quality of life in our cities, towns and rural areas. These priorities have resulted in far-reaching state initiatives that are already showing impressive results. For example, the number of fifth graders meeting the state standards in math and reading has increased significantly since 2002 – from 53 percent to 69 percent of all students in math and from 57 percent to 64 percent of all students in reading. And 20,000 students across the state have been able to earn college credit as they complete their high school graduation requirements.



At the same time, we have seen the unemployment rate fall in Pennsylvania and the number of jobs rise steadily, to an all-time high of 5.73 million in December 2005. Our economic gains have earned us national notice. In a recent ranking of economic growth, Pennsylvania climbed from 46th among the states in 2003 to 15th in 2004, according to the Corporation for Economic Development.

The agenda I set forth in this budget is far-reaching and ambitious. It touches all areas of the Commonwealth, from pre-school education to developing trade partners in the global economy. It builds on the strengths of the three previous budgets I introduced and the General Assembly enacted. Pennsylvania has made great strides since I took office in January 2003. We have done much to improve the lives of our people and brighten their futures. But our work is far from done. This budget provides the resources, and the direction, to continue Pennsylvania's exciting march forward to a better future.

Sincerely

A handwritten signature in black ink that reads "Edward G. Rendell". The signature is fluid and cursive, with "Edward G." on top and "Rendell" on the line below.

Edward G. Rendell



# *Commonwealth of Pennsylvania*

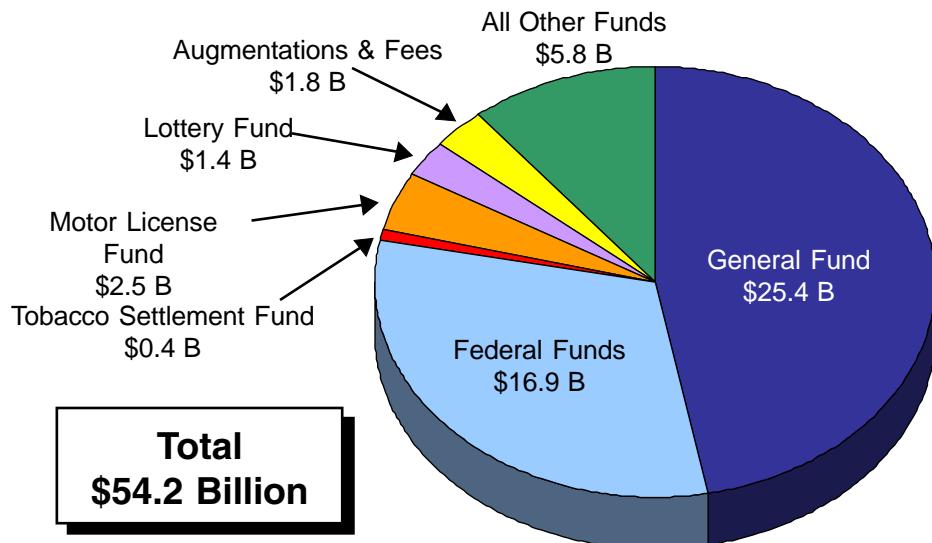
## *2006-07 Budget in Brief*

A complete copy of the *Governor's Executive Budget, Budget in Brief*  
and more budget information can be found on our web site  
<http://www.budget.state.pa.us>  
–click Budget & Financial Rpts–

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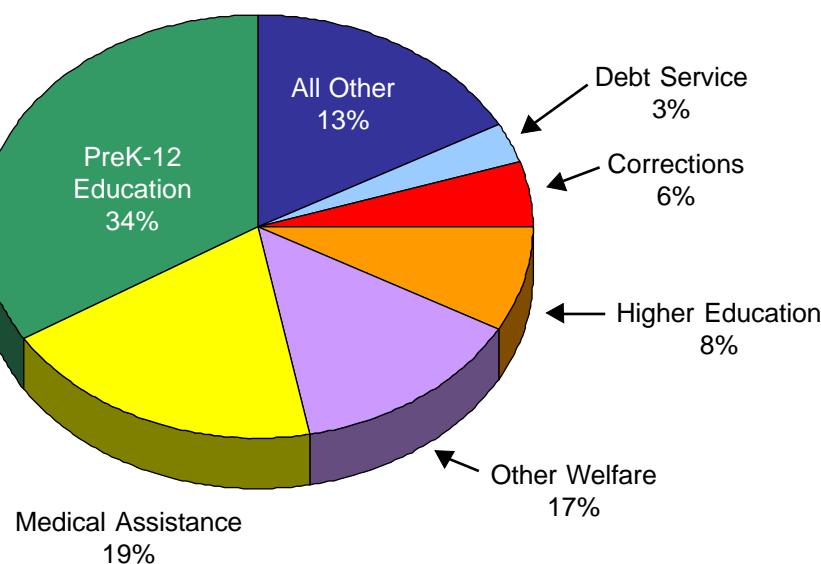
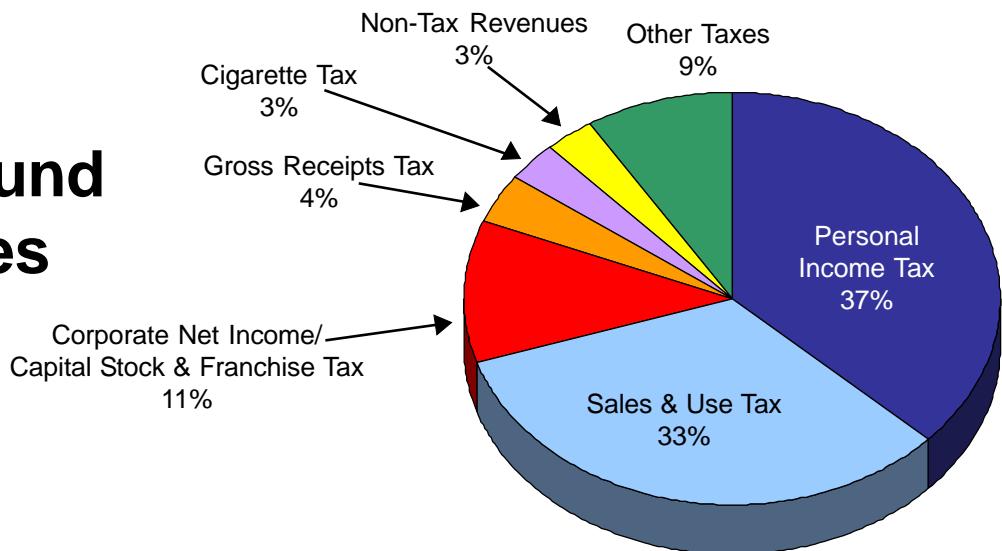
## Budget Overview



## Total Operating Budget

The total Fiscal Year 2006-07 operating budget, including all Commonwealth funds, is \$54.2 billion. The General Fund represents 47 percent of this amount.

## General Fund Revenues



## General Fund Expenditures

**\$25.4 Billion**

# ***2006-07 Budget Highlights***

- ◆ The 2006-07 budget invests in our children, promotes job creation, increases our state's global competitiveness and preserves the social safety net that protects the elderly, disabled and other Pennsylvanians in need.
- ◆ The 2006-07 General Fund budget is \$25.4 billion, an increase of \$923.8 million, or 3.8 percent, over 2005-06.
- ◆ In the 2006-07 budget, \$601.4 million, or nearly two-thirds, of the proposed \$923.8 million increase in General Fund expenditures is for Education.
- ◆ The 2006-07 budget reduces all spending other than education, public welfare and legally mandated debt service by 2.5 percent, while improving many vital state services.
- ◆ The 2006-07 budget holds the line on government and administrative spending – zero increase.
- ◆ The 2006-07 budget has no new taxes or tax increases.
- ◆ The 2006-07 budget re-invests savings realized through innovation and increased efficiency by eliminating waste and improving government operations, with \$841 million in annual savings achieved in 2005-06 and over \$1 billion projected in 2006-07.
- ◆ The 2006-07 budget reduces the Commonwealth's authorized complement by 2,272 positions with no lay-offs or cut-backs in government services. Through attrition and good management, the authorized state complement has been reduced by over 4,000 positions since Governor Rendell took office, with no lay-offs or service reductions.

## ***Promoting Job Creation and Improving PA's Competitiveness***

- ***Jonas Salk Legacy Fund: Accelerating Medical Research in Pennsylvania*** – \$500 million of accelerated investments, which will leverage another \$500 million in matching funds, to promote biomedical research in Pennsylvania
- ***World Trade PA*** – \$15 million to expand and promote the PA export network in key markets, encourage greater foreign investment in PA, and develop an operations center to provide critical export information to businesses
- ***Business and Job Development*** – \$10 million in multi-year grants for new infrastructure and facility improvement projects
- ***Nursing Initiative*** – \$10 million to address the state nursing shortage through the expansion of clinical education opportunities and nursing student retention activities
- ***Highways and Bridges*** – \$130 million of additional new investment in smoother roads and safer bridges
- ***Growing Greener II*** – 2006-07 marks the second year of this landmark \$625 million environmental initiative
- ***Business Tax Cuts to Improve PA's Ability to Compete for Jobs and Investments*** – Over \$221 million in business tax reduction in 2006-07, for a cumulative total of \$1 billion during the Rendell Administration:
  - ***Net Operating Loss Carry-Forward*** – \$7.3 million, by increasing the per business cap from \$2 million to \$3 million
  - ***Research and Development Tax Credit*** – \$40 million, an increase of \$10 million over 2005-06 and \$25 million over 2002-03
  - ***Capital Stock and Franchise Tax*** – Accelerate the phase-out by one tenth of a mill (\$18.3 million) to lower the rate to 4.89 mills, a total reduction of \$204 million compared to 2005-06

## Budget Highlights

### Investing in Our Children, Investing in Our Future

- **PreK-12 Education** – \$8.6 billion in total, a \$517 million, or 6.4 percent increase
- **Basic Education Funding** – \$4.7 billion, a 5 percent increase to support PreK-12 education and assist all school districts in boosting spending toward the statewide foundation level
- **Special Education Funding** – \$38.1 million, a 4 percent increase
- **Accountability Block Grants** – \$250 million, a \$50 million increase. Nearly 80,000 students are benefiting from pre-kindergarten, full-day kindergarten, reduced class sizes and tutoring as a result of 2005-06 Block Grant funding.
- **Science: It's Elementary** – \$10 million, for a new program to provide hands-on learning equipment and intensive teacher training to elementary schools that commit to upgrading their science curriculum
- **Classrooms for the Future** – \$20 million, for a new program to place Internet-equipped laptop computers on each student desk in mathematics, science, English and history high school classrooms and provide multi-media technology for teachers
- **Public Library Subsidy** – \$75.5 million, a \$14.1 million increase. This is the largest amount ever appropriated by the Commonwealth in support of public libraries.
- **Higher Education Programs** – Nearly \$2 billion in total, a 3.7 percent increase
- **Community Colleges** – A \$12.6 million, or 5 percent, increase, including capital funding
- **New Economy Technology Scholarship Program** – \$3.7 million increase to provide grants to 500 more college students and raise the maximum annual grant to \$4,000
- **Dual Enrollment** – \$7 million, a \$2 million increase, to help high school students earn college credit while they complete their high school graduation requirements
- **Project 720** – a total of \$9 million to transform Pennsylvania's high schools
- **Head Start** – \$45 million, a \$15 million increase for Head Start pre-kindergarten classrooms, to serve a total of 6,250 children

### Caring for all Pennsylvanians

- **Cover All Kids** – Inaugural year of a plan to provide access to affordable, comprehensive health care coverage for all uninsured children in Pennsylvania. First-year costs will be \$4.4 million in state funds and \$10.2 million in federal funds for 15,000 children in the first year.
- **PACE Plus Medicare** – \$244.8 million to fund a comprehensive state pharmaceutical benefit that complements Medicare Part D and ensures that PACE enrollees will not incur an increase in out-of-pocket costs, with funding to enable an additional 120,000 people to be served by PACE by June 2007.
- **Medical Assistance** – \$14.2 billion in combined state and federal funds to provide services to 1.9 million people with no reduction in eligibility requirements. Includes statewide expansion of Behavioral Health MA Managed Care.
- **Child Care** – \$663.4 million in combined state and federal funds, an increase of \$112.3 million or 20 percent, to expand services to 16,860 more children, increase the investment in Keystone Stars to improve the quality of early learning experiences, provide for a two percent cost-of-living adjustment, and maintain current programs.
- **Community Mental Retardation** – \$1.5 billion in combined state and federal funds, an increase of \$90.9 million or 6.3 percent, including funds to provide home and community-based services to 806 more people, address new federal Medicaid requirements and provide for a 2 percent cost-of-living adjustment
- **Expanding Services for the Disabled** – \$297.2 million in combined state and federal funds, an increase of \$57.7 million, or 24 percent, including funds to enable 1,500 more individuals to remain in their own homes as an alternative to nursing home care, and provide for a 2 percent cost-of-living adjustment
- **Long-Term Care** – \$4.2 billion in combined state and federal funds to provide nursing home and home and community-based services. Includes funding for 2,800 additional seniors to remain in their homes as an alternative to nursing home care.

### Public Safety and Security

- **State Police** – \$6.3 million for 90 additional troopers to support public safety, bringing the State Police to its highest enlisted complement ever
- **First Responders** – \$25 million to continue the Volunteer Company Grants program in 2005-06, and another \$25 million for this program from the State Gaming Fund in 2006-07
- **Pandemic Preparedness** – \$12.3 million in federal grants from the U.S. Department of Health and Human Services for pandemic influenza preparedness during the 2006 federal fiscal year. In state funds, \$500,000 for the Pennsylvania Emergency Management Agency and the Department of Health to coordinate the Commonwealth's avian flu and pandemic preparedness

# 2006-07 General Fund Expenditures

<b>Department</b>	<b>2004-05 Actual</b>	<b>2005-06 Available <sup>1</sup></b>	<b>2006-07 Budget</b>
Aging.....	\$ 35,954	\$ 20,223 <sup>2</sup>	\$ 19,329 <sup>2</sup>
Agriculture.....	81,171	79,197	77,365
Attorney General.....	74,977	81,200	79,200
Auditor General.....	50,179	50,979	49,979
Civil Service Commission.....	1	1	1
Community & Economic Development.....	521,445	513,033	426,502
Conservation and Natural Resources.....	97,178	97,979	96,635
Corrections.....	1,330,876	1,345,590	1,394,215
Education.....	9,406,889	9,699,267	10,278,068
<i>Basic Education (Pre K-12)</i> .....	7,836,304	8,114,207	8,631,273
<i>Higher Education</i> .....	1,464,063 <sup>3</sup>	1,475,481 <sup>3</sup>	1,522,570 <sup>3</sup>
<i>Public Library Subsidy</i> .....	57,914	61,362	75,500
<i>All Other</i> .....	48,608	48,217	48,725
Emergency Management Agency.....	54,154	49,597 <sup>4</sup>	14,657 <sup>4</sup>
Environmental Protection.....	191,105	192,168	177,768
Executive Offices.....	270,230	274,995	236,431
Fish and Boat Commission.....	14	14	16
Gaming Control Board.....	7,500	0	0
General Services.....	110,807	108,423	115,452
Governor's Office.....	7,320	7,400	7,300
Health.....	267,963	259,951	243,175
Higher Education Assistance Agency.....	419,473	428,741	451,347
Historical & Museum Commission.....	37,405	33,352	30,577
Insurance.....	82,513	80,586	76,554
<i>Children's Health Insurance</i> .....	45,423	45,423	47,557
<i>All Other</i> .....	37,090	35,163	28,997
Judiciary.....	261,615	265,305	264,231
Labor & Industry.....	97,936	115,210	113,916
Legislature.....	340,907	346,193	346,193
Lt. Governor's Office.....	1,300	1,363	1,385
Military & Veterans Affairs.....	116,396	121,559	124,848
Probation & Parole Board.....	97,303	99,954	97,325
Public Television Network.....	12,331	12,150	12,013
Public Welfare.....	7,886,399	8,781,697	9,087,313
<i>Medical Assistance</i> .....	4,260,464 <sup>5</sup>	4,753,630 <sup>5</sup>	4,862,515 <sup>5</sup>
<i>Mental Health</i> .....	711,983	722,194	724,298
<i>Mental Retardation</i> .....	927,324	956,889	1,023,577
<i>County Child Welfare</i> .....	632,547	838,526	880,831
<i>Cash Grants</i> .....	384,182	421,717	460,062
<i>All Other</i> .....	969,899	1,088,741	1,136,030
Revenue.....	214,108	174,382 <sup>6</sup>	179,540 <sup>6</sup>
Securities Commission.....	2,371	2,300	2,300
State.....	5,489	5,434	11,942
State Employees Retirement System.....	4	4	4
State Police.....	184,797	157,416 <sup>7</sup>	178,117 <sup>7</sup>
Tax Equalization Board.....	1,317	1,330	1,330
Transportation.....	334,784	325,332	328,925
<i>Mass Transportation Assistance</i> .....	287,815	293,571	299,442
<i>All Other</i> .....	46,969	31,761	29,483
Treasury.....	449,826	769,131	901,313
<i>General Obligation Debt Service</i> .....	399,925 <sup>8</sup>	712,373	852,697
<i>All Other</i> .....	49,901	56,758	48,616
<b>GRAND TOTAL</b>	<b>\$ 23,054,037</b>	<b>\$ 24,501,456</b>	<b>\$ 25,425,266</b>

<sup>1</sup> Includes recommended supplemental appropriations of \$197.419 million.

<sup>2</sup> Reflects transfer of Pre-admission Assessment costs to the Lottery Fund beginning in 2005-06 and transfer of PACE claims processing and other PACE operating costs to the Pharmaceutical Assistance Fund in 2005-06 and 2006-07. Total expenditures accounting for these changes are as follows: 2004-05 Actual = \$35,954,000; 2005-06 Available = \$37,295,000; and 2006-07 Budget = \$35,741,000.

The 2005-06 fiscal year includes increased nonrecurring PACE claims processing costs due to the implementation of Medicare Part D.

<sup>3</sup> Includes State System of Higher Education.

<sup>4</sup> Reflects reduction of nonrecurring disaster recovery costs included in 2004-05 and 2005-06 and the transfer of \$25 million in Volunteer Company Grants to the State Gaming Fund beginning in 2006-07.

<sup>5</sup> Medical Assistance is funded by a variety of state sources and federal funds; only a portion of the costs are supported by the General Fund. For example, in 2006-07 total projected MA expenditures are \$14,173,044,000. Combined MA obligations from the General, Tobacco Settlement and Lottery Fund are as follows: 2004-05 Actual = \$4,337,061,000; 2005-06 Available = \$4,911,414,000; and 2006-07 Budget = \$5,267,271,000.

<sup>6</sup> Reflects transfer of Lottery operations to the Lottery Fund beginning in 2005-06.

<sup>7</sup> An updated cost distribution methodology was implemented in 2005-06, increasing the Motor License Fund share of State Police costs.

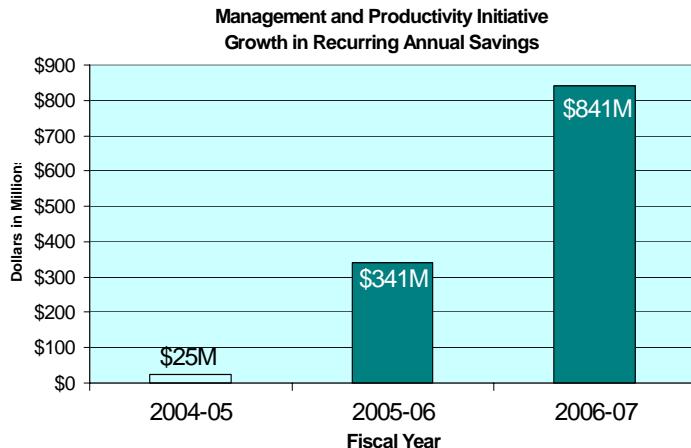
The combined General Fund and Motor License Fund costs are as follows: 2004-05 Actual = \$553,274,000;

2005-06 Available = \$588,168,000; and 2006-07 Budget = \$661,998,000.

<sup>8</sup> Federal Fiscal Relief Funds of \$377.6 million were appropriated in lieu of State General Funds for General Obligation Debt Service in 2004-05.

# Making Government Work Smarter

Governor Rendell has pledged to cut the cost of government and improve the way the Commonwealth works. By developing new business practices and focusing on innovation and efficiency throughout the government, the administration has generated \$841 million in recurring savings in 2005-06, with annual savings expected to exceed \$1 billion in 2006-07.



***"In the coming fiscal year, our savings will grow to a billion dollars or more."***

*– Governor Rendell*

In its first year, the administration focused on making an immediate impact on state operating costs by eliminating unused phone lines, turning off caller-ID, negotiating new lower cost contracts and driving vehicles longer. In 2004-05, management and productivity efforts focused on buying smarter, a practice known as "strategic sourcing." This resulted in major savings on more than a dozen state contracts – for computers, copiers, office supplies and other goods and services. During the 2005-06 fiscal year, every state agency has been challenged to implement additional projects, yielding further savings. Several of these initiatives are highlighted below.

## **Department of Public Welfare – Savings of \$371 Million**

Because it is the largest state agency the Department of Public Welfare (DPW) has been a major focus of the administration's management and productivity efforts over the past year. DPW initiatives have now generated over \$371 million in savings. These include:

### **• Pharmacy Initiatives — Savings of \$83 million**

- \$51 million in savings from instituting a preferred drug list, encouraging less-expensive mail-order filling of prescriptions and other pharmacy cost reductions.
- \$32 million in savings from revised agreements with pharmacies.

### **• Collecting Money Owed — Savings of \$24 Million**

- \$16 million in savings by more effectively identifying and collecting reimbursement for health care costs owed from private insurance companies.
- \$8 million in savings from the identification and denial of fraudulent claims submitted to the Medical Assistance Program.

### **• Re-assessing Program Operations — Savings of \$1.3 Million**

from evaluating treatment practices and the use of facilities in DPW youth development and youth forestry camp programs. The first phase of this project resulted in \$1 million in annual savings by closing two units, and the next stage will save another \$300,000 annually by closing a third center and relocating a treatment program.

- **Using Technology Better — Savings of \$2 Million** from replacing paper checks issued to the approximately 510,000 families eligible to receive child support payments with electronic direct deposit.
- **Improved Contracting —** DPW contracts for more than \$8 billion of goods and services a year, and new purchasing procedures and performance-based contracting are generating significant annual savings.

### **Buying Smarter — Savings of \$154 Million**

In the past two years, the Commonwealth has achieved recurring savings of more than \$154 million, and one-time savings of more than \$6 million, as a result of the strategic sourcing initiative. The Commonwealth has been able to keep agency operating costs 9 percent below 2002-03 levels in part through this successful initiative, which is saving Commonwealth money on everything from paper clips and staples to cars and medical services.

- By using a new bidding process for purchasing police vehicles, the Commonwealth is saving \$816,000 annually, or about \$1,500 on the cost of each new police car.
- The Commonwealth also renewed its truck supplier contract on favorable terms, avoiding a 3 percent market price increase for new trucks and saving the administrative costs associated with re-bidding the contract.
- The Commonwealth is realizing \$20 million in savings, a 31 percent reduction, in information technology technical staffing costs by contracting for short-term technical staffing needs.

## **Creating A More Efficient Government**

The administration has made the development of efficient and innovative business practices a priority across the government. As the following examples demonstrate, these efforts have yielded dramatic savings.

- **Reducing Fleet Costs — Savings of \$40 Million**

Since 2003, the Rendell Administration has been able to eliminate more than 1,000 vehicles, with hundreds more fleet vehicles slated for elimination in the coming fiscal year. In addition the Commonwealth now retires fleet cars at 100,000 miles as opposed to 65,000 miles, while stepping up preventive maintenance to ensure that vehicles remain in good condition as their useful lives are extended. These and other efforts have generated \$33 million in one-time savings for the Commonwealth. And Pennsylvania's smaller and more efficient vehicle fleet is now less expensive to fuel and maintain, saving nearly \$7 million every year.

- **Reducing Energy Costs — Savings of \$2 Million**

The Department of General Services has been using Guaranteed Energy Savings Contracts to pay for energy conservation improvements in a number of Commonwealth buildings. These improvements pay for themselves in energy savings.

- **Get Healthy Initiative — Savings of \$18 Million**

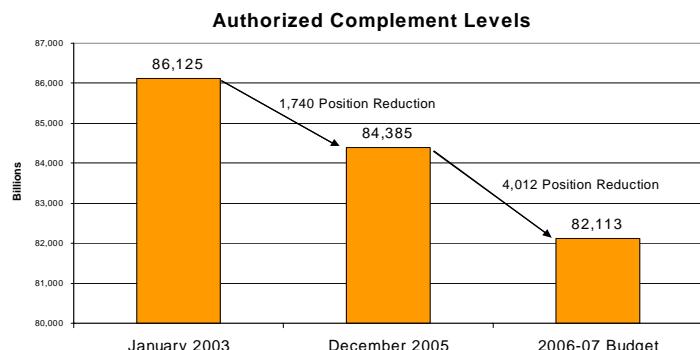
Commonwealth employees are now able to participate in the Get Healthy initiative, which is designed to monitor and improve employees' lifestyles to reduce short-term and long-term medical costs. This initiative is projected to generate \$18 million in annual savings.

- **Inmate Collections — Savings of \$3 Million**

As part of the Commonwealth's efforts to hold inmates financially accountable for their actions, the Department of Corrections may collect up to 50 percent of an inmate's account balance and monthly income toward court-ordered restitution, fees, fines and costs. Through this program, the Commonwealth receives approximately \$3 million a year.

## **Creating a Smaller, More Efficient Workforce — Savings of \$137 Million**

Since January 2003, the total number of filled salaried positions in the Commonwealth workforce has been reduced through attrition by more than 2,300. This net reduction takes into account 381 new filled salaried positions that have been created as part of the Rendell Administration's commitment to public safety. The administration's efforts to reduce the number of Commonwealth employees through attrition are saving Pennsylvania taxpayers \$137 million per year. The 2006-07 budget will reduce authorized complement levels by



nearly 2,300 positions through attrition - a 4,012 position, or 4.7 percent, reduction since January 2003.

## **Generating New Revenues — \$133 Million**

In addition to reducing costs, many agencies have developed innovative programs to increase revenues. More than \$133 million in new revenues have been generated by the following programs:

- **Pennsylvania Lottery Initiatives — \$99 Million**

The Pennsylvania Lottery has implemented a number of new revenue-generating programs since 2003, including a new raffle drawing, the expansion of instant game offerings and increased lottery promotions.

The Pennsylvania Lottery has introduced player-activated terminals that are expected to generate approximately \$8 million in new revenues annually for programs supporting older Pennsylvanians. The Pennsylvania Lottery was noted in 2004 as one of the fastest growing lotteries in the nation, and net revenues are projected to exceed the prior administration's 2005-06 projections by more than \$99 million.

- **Pennsylvania Liquor Control Board's Consumer-Oriented Initiatives — \$34.3 Million**

The Sunday Sales program began as a pilot program in February 2003. On an average Sunday more than 40,000 customers make purchases totaling at least \$1 million.

In addition, the board has opened 17 liquor stores located in grocery stores. These stores are complemented by seven new outlet stores, plus more than 60 Premium Collection facilities. This fiscal year alone, the board's consumer-oriented initiatives are expected to generate new tax collections of nearly \$34.3 million.

Since the Rendell administration has taken office, hundreds of initiatives implemented by thousands of employees have revolutionized the way the Commonwealth does business across the enterprise. These changes will continue to provide Pennsylvania taxpayers with additional savings and more efficient services in future years.

# *Promoting Job Creation and Improving PA's Competitiveness*

When Governor Rendell was sworn into office in January 2003, Pennsylvania's under-performing economy and stagnant labor force were reeling. The Commonwealth's employment and labor force levels were in dramatic decline, and there were more Pennsylvanians unemployed than at any time in the previous eight years. Perhaps more important, working Pennsylvanians and Pennsylvania businesses were not well positioned to take advantage of changing national and international trends. Governor Rendell responded with a successful combination of job creation, worker training, and business investment and expansion programs to transform Pennsylvania's economy and create new opportunities for employment and investment.

## *More Jobs and a Better-Trained Workforce*

### **Pennsylvania's Economy Gains Momentum**

One of the best measures of an economy's performance is the total number of jobs on employer payrolls. The recent results in Pennsylvania are clear. **Total non-farm payrolls have risen steadily over the last two years, and Pennsylvania reached an all-time high of 5.73 million jobs in December 2005. Pennsylvania has gained jobs every month since March 2005 and for all months except two since February 2004.**

Pennsylvania has also made significant strides in reducing unemployment. The state's unemployment rate averaged 5 percent in 2005, down from 5.5 percent in 2004 and 5.7 percent in 2003. Pennsylvania's unemployment rate was lower than the national rate in six of the last 12 months.

### **Steady Rise in Pennsylvania Jobs (Non-Agriculture)**



### **Job Ready Pennsylvania is Building a Stronger Workforce and a Stronger Economy**

The best way to keep the economy growing is to make sure that Pennsylvania employers feel confident they can find the skilled workers they need. Governor Rendell confronted this challenge head-on in 2005-06 with a new initiative called Job Ready Pennsylvania. Job Ready Pennsylvania is a strategic investment of \$91 million that is building a stronger workforce and a stronger economy by:

- Helping today's workforce obtain the skills needed to compete in the global economy;

- Increasing options for students to receive post-secondary education; and
- Boosting the skills of high school graduates.

By identifying industry clusters and high-priority occupations and by targeting funding to these areas, Job Ready Pennsylvania has better aligned state and local education and workforce spending with the actual needs of employers. The early results for individual programs are encouraging:

- **Building High Schools for the Future.** Seventy-five schools with a combined enrollment of more than 77,000 students are taking part in Project 720, Pennsylvania's high school reform initiative to increase academic rigor.
- **Dual Enrollment for High School Students.** Job Ready Pennsylvania made an initial investment of \$5 million to allow high school students to earn college credit while completing their high school requirements. Nearly 20,000 students from 220 school districts are enrolled in courses in more than 70 colleges and universities.
- **Expanding Tutoring.** Job Ready Pennsylvania has made possible a \$66 million expansion in Educational Assistance Program tutoring. This investment will increase the number of students who receive help to build their skills from 33,000 in 2003-04 to 70,000 in 2005-06.
- **Transforming Career & Technical Education.** "Voc-tech" schools are responsible for training more than 96,000 secondary school students and Job Ready PA is making sure that course credit is transferable and meets industry-approved standards. To date, 115 schools with more than 15,000 students are purchasing new equipment through Job Ready Pennsylvania.
- **Increasing Community College Funding and Stabilizing the Funding Environment.** In 2005-06, Pennsylvania is investing \$22.8 million, or 10 percent, more in community colleges than in 2004-05, the largest funding increase in fifteen years. The Governor's 2006-07 Budget proposes an additional \$12.6 million, or 5 percent, for community colleges.
- **Partnering with Employers to Close Workforce Gaps.** In today's economy, individual firms often cannot afford to pay for solutions to hiring and training bottlenecks on

# Promoting Job Creation and Improving PA's Competitiveness

their own. Increasingly, firms in similar industries form Industry Partnerships. Building on the success of earlier partnerships in manufacturing, 45 partnerships involving 454 companies were created in 2005.

- **Helping Workers Train for Better Jobs.** Job Ready Pennsylvania includes a new \$10 million Pennsylvania Higher Education Assistance Agency grant program for 10,000 independent adult students to help them obtain certificates in high-priority occupations. More than 2,800 adults students have already received grants to take courses at 186 institutions.
- **Keystone Innovation Starter Kits.** Starter Kits help Pennsylvania build on its advantage in higher education and life sciences by attracting top-tier researchers to the Commonwealth's leading colleges, universities and academic medical centers. Sixteen Starter Kit grants totaling \$3 million were awarded in 2005-06.

## Economic Stimulus Program Update

Since April 2004, an interlocking set of economic growth initiatives has been created in Pennsylvania thanks to the Governor's Economic Stimulus Program. The chart to the right presents a status report on Economic Stimulus Program activities to date.

Governor's Economic Stimulus Program Status Report January 2006		
(Dollar Amounts in Thousands)		
Program	Projects Funded	Funds Committed
<b>Infrastructure Projects:</b>		
Business In Our Sites	85	\$210,000
PennWorks, Water/Wastewater Infrastructure	30	\$53,000
Tax Increment Financing	1	\$5,000
Infrastructure Facilities Improvement Program	5	\$3,000
Redevelopment Assistance Capital Program	241	\$656,000
<b>Community Revitalization:</b>		
Main Street Downtown Business Renewal	162	\$15,230
Elm Street Downtown Residential Renewal	64	\$11,830
Enterprise Zones	90	\$13,760
Housing Redevelopment Assistance	243	\$63,380
Homeownership Choice	24	\$25,000
Hometown Streets	226	\$128,500
<b>Business and Other Private-Sector Investments:</b>		
First Industries Fund (Agriculture/Tourism)	148	\$23,000
Second Stage Loan Program	2	\$375
Venture Capital Guarantee Program	7	\$29,500
Keystone Innovation Zones	16	\$4,100
Base Realignment and Closure	Multiple sites	\$4,460
<b>TOTAL</b>	<b>1,344</b>	<b>\$1,246,135</b>

## Improving Economic Competitiveness

The Governor's Economic Stimulus Program is creating an exceptional foundation for continued economic growth in Pennsylvania. The 2006-07 budget builds on this foundation with innovative programs that will enhance Pennsylvania's economic competitiveness at home and throughout the world.

### The Jonas Salk Legacy Fund: Accelerating Medical Research in Pennsylvania

Health care and higher education account for more than one out of every three of Pennsylvania's service-sector jobs. Together they comprise more than 9 percent of Pennsylvania's gross state product, as compared with the national rate of less than 7 percent.

The 2006-07 budget provides funding of up to \$500 million over the next two years to invest in Pennsylvania's life sciences future. These investments will be fully funded by leveraging a portion of Tobacco Settlement Fund revenues. The Jonas Salk Legacy Fund will be created to oversee these investments in research and commercialization activities. Two major types of investments will be eligible for support:

- **Keystone Innovation Starter Kits** to recruit research faculty to Pennsylvania colleges, universities and academic medical centers.
- **Bricks & Mortar Grant Financing** for bioscience facilities, including laboratories, incubators and research parks.

### World Trade PA Initiative

World Trade PA will provide \$15 million in additional support to advance the administration's job-creation and

economic growth strategies through increased global engagement. World Trade PA has three major strategies:

- **Increase Pennsylvania's Share of Trade in Foreign Markets.**
- **Attract New Foreign Direct Investment to Secure Jobs and Capital.**
- **Leverage Global Networks from Pennsylvania's Colleges and Universities.**

### Improving Pennsylvania's Business Tax Climate

- **Further Reduce the Capital Stock and Franchise Tax.** Accelerate phase-out of the Capital Stock and Franchise Tax by an additional tenth of one mill beyond the previously scheduled rate cut for tax year 2006. This accelerated reduction will lower the rate from 4.99 to 4.89 mills and result in \$204 million in savings for Pennsylvania businesses in fiscal year 2006-07.
- **Research and Development Tax Credit.** \$40 million in credits for 2006-07, an increase of \$10 million over 2005-06 and \$25 million over 2002-03.
- **Increasing the Annual Cap on Net Operating Losses** from \$2 million to \$3 million effective January 1, 2007.

# *Investing in our Children, Investing in our Future*

In today's global economy, Pennsylvania is no longer competing only against other states but also against other countries like China, Singapore and India. To ensure economic success for our future workforce and for our state, the Commonwealth must provide all of its students with solid critical thinking skills and strong backgrounds in reading, math and science.

Pennsylvania is making progress. Under Governor Rendell's leadership, student achievement is on the rise. **The number of fifth-graders meeting the state standards in math has increased from 53 percent of our students in 2002 to 69 percent last year and reading scores have increased from 57 percent to 64 percent during the same period.** Students are making gains in reading and math at every grade level.

To make student success possible, the Commonwealth is making targeted investments in its pre-kindergarten through grade 12 and higher education systems. Funding for early childhood, elementary and secondary education is up by nearly \$1.2 billion compared to just three years ago. For the first time ever, more than half of our students are in full-day kindergarten. We are transforming our high schools and giving high school students the opportunity to earn college credit – before they even graduate. Pennsylvania's higher education grant program is helping more families send their children to our world-class colleges and universities. And to better serve our residents and businesses, the Commonwealth has provided financial incentives to community colleges to focus on the well-paying, high-priority occupations of tomorrow.

But more must be done. The scientists, inventors and great thinkers of this new century will not simply appear. They must be nurtured every day in our public school classrooms, local libraries and higher education institutions.

## **Get Ready, Get Set, Go Global**

From the first day of pre-kindergarten to the moment when our students receive their college diplomas, it is up to the Commonwealth's education system to prepare every student for the high-skill jobs of the global economy. The 2006-07 budget builds on Pennsylvania's accomplishments over the last three years by recommending three new initiatives that will make Pennsylvania a leader in readying our students for the jobs of the future, while giving our high-tech businesses the employees they need to survive and thrive.

- **Science: It's Elementary.** This \$10 million initiative will provide hands-on learning equipment and intensive teacher training to elementary schools that commit to upgrading their science curriculum. This program makes every student a scientist in the classroom and gives schools access to a strategy that has been proven successful in not just the nation but also the world.

- **Classrooms for the Future.** The \$20 million Classrooms for the Future technology initiative will make every high school classroom in the Commonwealth a high-tech center of learning. Over the next five years, every high school classroom in the four core subjects will have an Internet-equipped laptop computer on each student desk and multi-media technology at each teacher's fingertips. By investing over the short term, starting with \$20 million in 2006-07, we can help our educators harness the great power of technology in their classrooms. To achieve this goal, this budget also includes \$4 million to provide professional development for teachers and school leaders.
- **From the Classroom to the Board Room.** This budget includes a \$3.7 million increase for the New Economy Technology Scholarship Program that supports students seeking a college degree and a high-tech Pennsylvania job. The program, administered by the Pennsylvania Higher Education Assistance Agency, provides grants of up to \$3,000 a year for three years to students pursuing college degrees in computers, math and science who commit to work in Pennsylvania after graduation. This initiative expands this program to an additional 500 college students and raises the maximum grant to \$4,000.

## ***Early Childhood Education: The Foundation for Student Success***

In 2004-05, Pennsylvania made its first investment in pre-kindergarten by providing funding for Head Start and launching the \$200 million Accountability Block Grant, which school districts could use for pre-kindergarten and other proven academic programs. Governor Rendell's 2005-06 budget doubled Head Start funding to \$30 million, allowing 4,710 children to benefit. The 2006-07 budget adds another \$15 million for Head Start, making this high-quality program available to 6,250 at-risk children.



# *Investing in our Children, Investing in our Future*

GROWTH IN PA's EARLY CHILDHOOD EDUCATION PROGRAMS				
	2004-05	2005-06	2006-07	2007-08
Students in State-funded Head Start expansion .....	2,484	4,710	6,250	10,700
School districts offering full-day kindergarten .....	353	370	385	385

- **Keystone STARS.** This budget includes a \$5.8 million increase to reach another 12,000 children, bringing the number of children served by the program to nearly 160,000 in 2006-07. Keystone STARS offers performance standards, professional development and on-site technical assistance for child care providers, and additional compensation for certified staff.
- **Serving More Children in Child Care.** This budget provides an additional \$5.5 million to help 1,861 more children and their families access quality child care and \$28.3 million to provide child care services to 15,000 additional children in Temporary Assistance to Needy Families (TANF) families and former TANF families working to gain economic independence. In addition, the budget includes the resources to fully unify the subsidized child care program so that families have "one door" for all subsidized child care in their local communities.
- **Helping New Mothers and Their Children.** This budget increases the Nurse Family Partnership program to serve 4,085 families, up from 3,574, and to provide services in 37 counties, up from 33. The Nurse Family Partnership serves first-time, at-risk mothers and their babies. The benefits include continued education for the mothers, improved child development for the children, improved parenting and less child abuse.
- **Early Intervention.** This budget includes \$16 million to provide early intervention services to 5,174 additional children. The Early Intervention program serves children from birth through age five who have a disability or developmental delay. Program services are intended to minimize developmental delays and assist families in meeting the special needs of their children.

This budget also continues the public-private Partnership for Quality Pre-kindergarten, through which public and private funders support dozens of school districts and their community-based early childhood partners to offer high-quality, pre-kindergarten services in local communities.



## *Expanding the Education Accountability Block Grant*

Every day in every Pennsylvania school district, the Education Accountability Block Grant is helping educators boost achievement for the Commonwealth's students. Now in its second year, the Accountability Block Grant provides \$200 million for school districts to invest in academic programs that are proven to help students learn. As a result of this year's Accountability Block Grant:

- More than 3,000 children are enrolled in pre-kindergarten;
- More than 53,000 children are enrolled in full-day kindergarten;
- Nearly 21,000 students in kindergarten through third grade are in smaller classes;
- More than 46,000 struggling students are receiving tutoring; and
- Hundreds of thousands of students are benefiting from the additional training their teachers are receiving.

The 2006-07 budget increases the Accountability Block Grant by \$50 million to help schools to invest in student success.

## *Transforming Pennsylvania's High Schools*

In 2005-06, Pennsylvania took the first steps towards transforming its high schools to ensure that all students graduate with the skills they need for college and high-skill careers. Seventy-five high schools were selected to participate in Project 720, the Commonwealth's pioneering high school reform initiative, and 220 school districts applied for Dual Enrollment grants so their students could earn college credit before graduation.

In addition to launching the Classrooms for the Future technology initiative, this budget significantly expands the scope of high school reform in Pennsylvania in other ways, further demonstrating our commitment to making every day of every student's 720 days of high school count on behalf of the Commonwealth's young adults:

- **Reinvigorating College and Career Counseling.** Students make hundreds of decisions during their school years that dramatically affect their future options, often without even realizing the consequences. In high schools and middle schools, guidance counselors have a new and crucial role to play in helping students explore their career interests and navigate the vital academic choices that will enable them to achieve their goals. This budget includes \$3 million in grants for school districts to upgrade their career counseling programs.

## *Investing in our Children, Investing in our Future*

- **Expanding Project 720.** Project 720 high schools are leading the way in transforming their academic programs to ensure that all students take a rigorous high school curriculum. Last year, more than 160 schools applied to participate in Project 720, but limited funding meant that only 75 could be approved. This budget nearly doubles Project 720 resources from \$4.7 million to \$9 million, allowing up to 30 more schools to participate.
- **Helping More High School Students Earn College Credit.** With \$5 million in first-ever Dual Enrollment funding in 2005-06, an estimated 20,000 Pennsylvania students in 220 school districts are earning college credit even as they complete their high school graduation requirements. This budget increases Dual Enrollment funding by \$2 million.

### **Accountability for Results**

Pennsylvania's schools and school districts have received a historic increase in resources over the last three years, and with these needed funds must come real accountability. This budget includes \$2 million to make school-leader accountability a reality. Principals and superintendents would be eligible for annual incentive bonuses by meeting set targets for increasing student learning in reading and math. In addition to the administrator's own incentive pay, the successful school or school district would receive an equal amount of funding to invest in academic programs.

### **Improving Teacher Quality**

The single most important ingredient for increasing student achievement is an effective teacher in every classroom. Over the last decade, certification by the National Board for Professional Teaching Standards has become the gold standard for teacher excellence. This budget provides \$1.2 million to help 500 Pennsylvania teachers earn National Board certification. In return, recipients will be required to teach in Pennsylvania public schools for at least two years after receiving their National Board certification. Priority will go to teachers in low-achieving school districts, high school math and science teachers and early childhood teachers. This investment will bring Pennsylvania from 45th to 31st place among the states in this certification, and – most important – ensure that our students have the excellent teachers they need and deserve.

### **Retirement Costs**

The Commonwealth pays approximately half of the cost of providing retirement benefits for school employees. In 2006-07, the employer contribution rate is increasing from 4.69 percent of payroll to 6.46 percent. This increased rate raises the cost to the Commonwealth by \$114.3 million, a 44.9 percent increase, to a total of \$368.8 million in 2006-07. School districts' cost for retirement is increasing at the same rate.

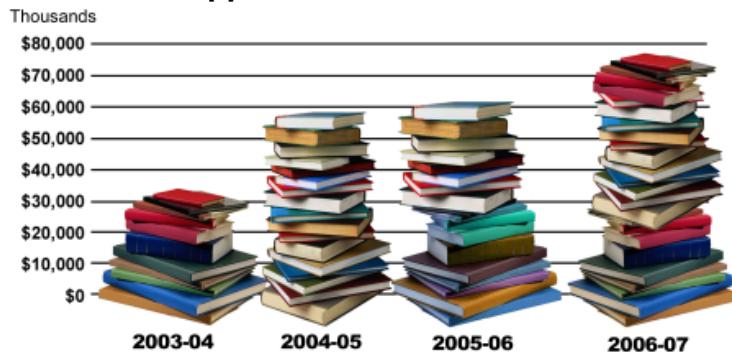
The 2006-07 budget continues to advance Pennsylvania's commitment to its students and to the state's economic well-being. These additional investments will move the Commonwealth even closer to achieving educational success – and opening the doors of opportunity – for every Pennsylvanian.

<b>Key Higher Education Funding:</b> (In Millions)	
INCREASES	TOTAL FUNDING
<b>5% for Community Colleges</b>	
– Operating Costs .....	\$ 222.7
– Capital Costs .....	42.0
<b>4.5% for the State System of Higher Education</b>	\$ 483.0
<b>4.0% for the State-related Universities:</b>	
– Pennsylvania State University .....	\$ 322.4
– University of Pittsburgh .....	163.1
– Temple University .....	168.7
– Lincoln University .....	13.5
<b>3.0% for the Non-State Related Universities and Colleges</b>	\$ 87.5
Higher Education Assistance Agency:	
– <b>4.9% for Grants to Students</b> .....	\$ 386.2
– <b>119.4% for SciTech Scholarships</b> .....	6.8
– <b>3.0% for Institutional Assistance Grants</b> ..	41.4

### **A Historic Investment in Libraries**

Building a knowledge society demands a strong investment in our public libraries. This budget increases library funding by \$14.1 million, bringing the state subsidy for local libraries to \$75.5 million – an all-time high. This increase reaffirms Pennsylvania's current standing as a national leader in state funding for libraries.

### **Support for Public Libraries**



# Caring for All Pennsylvanians

The Commonwealth faces many challenges in the coming year. The federal government continues to reduce its support for programs for the most needy, the cost of health care continues to increase and the number of people seeking help from public-assistance programs continues to rise. In spite of these challenges, this budget adheres to the same principles concerning its public assistance programs that Governor Rendell set forth last year:

- No one currently receiving services in Pennsylvania will lose eligibility;
- Children will not lose any services; and
- Pennsylvania will provide coverage for the growing number of vulnerable individuals and families who require our assistance.

## Protecting Pennsylvania's Most Vulnerable Citizens

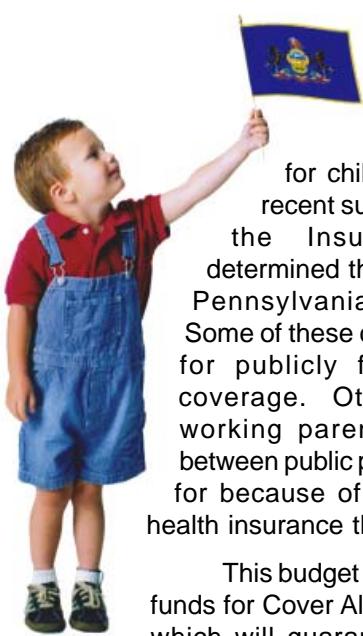
This budget provides an extraordinary increase of \$739 million to expand care for Pennsylvanians in need in 2006-07, representing a 9 percent increase from the 2005-06 appropriated level of state funds. This additional funding will provide a broad array of health and human services to more than 2 million Pennsylvania residents in 2006-07.

In 2006-07, however, the Commonwealth will not just be spending more for health and human service programs. The Commonwealth will also be making these needed investments in a more efficient manner. The safety net reform measures instituted as part of the 2005-06 budget have achieved systemic and fundamental improvements in Pennsylvania's Medical Assistance program. This budget builds upon those successes, proposing several new initiatives that not only will improve the quality, efficiency

and integrity of the Medical Assistance program but also will save \$126 million in 2006-07. These improvements will enable additional investments to be made in programs that support Pennsylvania's children, adults and families in need.

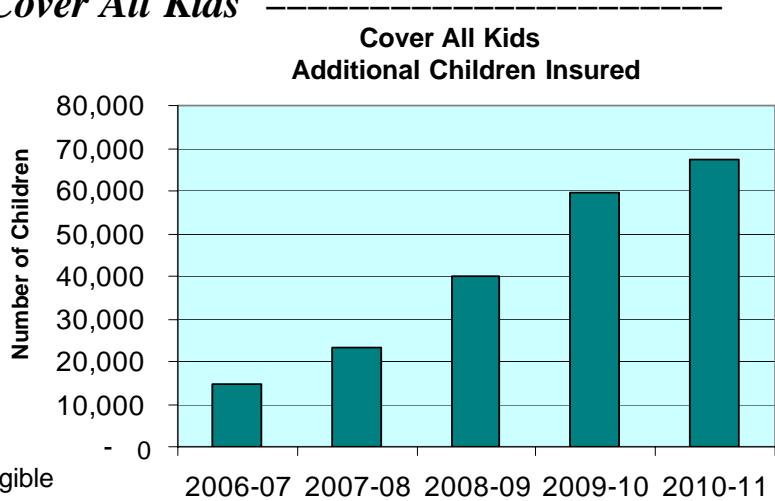
The 2006-07 budget builds upon Governor Rendell's commitment to reduce the number of Pennsylvanians without health care coverage. The 2005-06 budget provided funding to significantly increase the number of children receiving free and subsidized health insurance. This budget takes those efforts to the next level by serving more children who meet current eligibility requirements and by expanding eligibility requirements to provide opportunities for all uninsured children to receive health care coverage.

### Cover All Kids



Although Pennsylvania has one of the highest rates of health care coverage for children in the country, a recent survey commissioned by the Insurance Department determined that 133,589 children in Pennsylvania remain uninsured. Some of these children already qualify for publicly funded health care coverage. Others are children of working parents who are caught between public programs they are not eligible for because of income limits and private health insurance their parents cannot afford.

This budget includes \$14.6 million in total funds for Cover All Kids, a new state program, which will guarantee access to affordable, comprehensive health care coverage for all uninsured children in Pennsylvania. Through enhanced outreach



efforts, federally-approved increases in income eligibility for subsidized coverage and new opportunities for higher-income families to purchase health care coverage at-cost, the Cover All Kids initiative will enroll nearly 15,000 uninsured children in 2006-07 and additional children thereafter.

# Caring for All Pennsylvanians

## Pennsylvania's Uninsured Children



According to a recent survey commissioned by the Insurance Department, there are currently 133,589 uninsured children in Pennsylvania. Through the enhanced outreach efforts, broader income eligibility limits for subsidized coverage and new opportunities for higher-income families to purchase health care coverage at-cost, Governor Rendell's Cover All Kids initiative will enroll nearly 15,000 uninsured children in 2006-07 and additional children thereafter.

### **Increasing the Number of Insured Pennsylvanians**

With the 2006-07 budget, Governor Rendell is also expanding health care coverage and services for thousands of low-income adults.

- \$8 million in additional Tobacco Settlement Funds and \$8.7 million in additional Community Health Reinvestment Funds to provide health care coverage for 8,575 additional low-income working adults through the Adult Basic Program representing an increase of 21 percent from 2005-06.
- \$1.7 million in new state funds to provide breast cancer and cervical cancer screening for 4,208 high-risk women ages 40 to 49 whose family income does not exceed 250 percent of the federal poverty level and who do not have other health insurance coverage for these services.

### **Expanding the Availability of Quality Early Childhood Services**

Pennsylvania's economic recovery is creating new jobs and new opportunities, and this budget includes a significant investment to help families achieve self-sufficiency. Quality early childhood programs not only support families in their quest for self-sufficiency, they also promote and support the development of children and their preparation for success in school and life. In 2006-07, the Commonwealth will expand upon its commitment to vulnerable children and their families by expanding high-quality child and family services.

- \$28.3 million in additional funding to provide child care services to 15,000 additional children in families receiving Temporary Assistance to Needy Families (TANF) and former TANF families working to gain economic

independence, and \$5.5 million to provide subsidized child care services to 1,861 additional low-income families.

- \$5.8 million to improve the quality of early childhood learning programs for 12,000 additional children through the expansion of Keystone STARS.
- \$1.5 million in new federal funds, by leveraging existing state funds, to expand the number of families participating in the Nurse Family Partnership program to 4,085 families, an increase of 511 families from 2005-06.
- \$16 million in additional funds to provide early intervention services to 5,174 additional infants, toddlers and pre-school children in 2006-07.

### **Protecting Children and Preserving Families**

Providing services to children and families in their homes and communities improves parenting skills and builds the long-term ability of the family to cope with stressful life circumstances. Under Governor Rendell's leadership, Pennsylvania has maintained a consistent focus on the safety, family stability and well-being of children. The Commonwealth continues to support programs that prevent child abuse and neglect, enable children to stay in their own homes and help low-income and at-risk children and families thrive. This budget includes:

- \$42.3 million in additional funding for County Child Welfare Services to bring the total amount to \$880.3 million.
- \$6.3 million in additional funds to allow more children to be adopted and to continue to provide financial assistance to those who have already been adopted.

#### **CHILDREN PARTICIPATING IN EARLY INTERVENTION**

	2004-05	2005-06	2006-07	2007-08
Dept. of Public Welfare (Birth to Age 2) ....	26,458	28,472	31,300	32,800
Dept. of Education (Ages 3 to 5) .....	36,790	38,189	40,536	41,686

# *Caring for All Pennsylvanians*

## ***Expanding Services for Individuals with Special Needs***

The 2006-07 budget continues to support independence for people with mental and physical disabilities.

- \$16.8 million in additional funds to: provide home and community-based services for 806 additional individuals with mental retardation, implement ten new employment pilot programs for young adults with mental retardation, and implement new management initiatives designed to improve Pennsylvania's timely response to individuals' changing needs and improve the quality and consistency of mental retardation services across the system.
- \$43.8 million to expand the availability of managed behavioral health services, including mental health and substance abuse services, to more than 200,000 additional individuals in 35 additional counties through the Medical Assistance HealthChoices Program. These costs are offset by reductions in the Medical Assistance Fee-For-Service Program.
- \$11.7 million to provide services to an additional 1,500 persons with disabilities through the Attendant Care and Services to Persons with Disabilities programs.

## ***Enhancing Efficiency and Integrity***

Recognizing the long-term challenges presented by increasing cost pressures on the Medical Assistance program, the 2005-06 budget established a set of reforms to control the increase in Medical Assistance program costs. Under the leadership of Governor Rendell, the systemic and fundamental improvements made to Medical Assistance have been successful in stabilizing the program and have positioned the Commonwealth to extend the reach of its critical services.

The 2006-07 budget reflects the Commonwealth's continued efforts to improve the quality, integrity and efficiency of the Medical Assistance program, reducing costs by another \$126 million in the coming fiscal year, through savings of:

- \$16.8 million through selective contracting for some Medical Assistance services;
- \$13 million through improving the use of hospital resources by assessing patients to determine the appropriate level of care and the most appropriate treatment setting;
- \$6.5 million through more aggressive efforts to reduce waste, fraud and abuse;
- \$5.5 million by ensuring that other insurers pay for the health care costs of Medical Assistance recipients when they have an obligation to do so;
- \$15.1 million through two initiatives to maximize federal funding for long-term care services; and
- \$68.8 million through updating hospital supplemental payments to more accurately reflect the resources needed to provide care for Medical Assistance recipients. This budget will continue to provide \$37.9 million in uncompensated care payments through the Tobacco Settlement Fund.

The Commonwealth will also implement pay-for-performance contracts in the Medical Assistance program that promote strong program results.

This budget reaffirms the Commonwealth's commitment to care for all Pennsylvanians and to ensure that the elderly, people with disabilities and low-income families will have access to health care and other critical services.

# *Enhancing Programs for Pennsylvania Seniors*

The Commonwealth has a long tradition of providing a broad range of services and programs for its older residents, including a state pharmaceutical assistance program and, when necessary, long-term living services to provide needed supports. This budget provides for necessary changes in both programs to better address the needs of Pennsylvania's growing elderly population.

## *PACE Plus Medicare: Ensuring That Senior Citizens Maintain Essential Prescription Drug Support*

### **PACE/PACENET: A National Model**

Pennsylvania's state pharmaceutical assistance program known as PACE (for Pharmaceutical Assistance Contract for the Elderly) is one of the largest state-sponsored prescription drug plans operating in the United States and has been in operation for 22 years. Through Act 37 of 2003, PACE was revised to add PACENET to serve additional recipients, bringing the current number of PACE/PACENET enrolled senior citizens to more than 303,000. Because Pennsylvania will be sharing the cost of prescription drug coverage under the new federal prescription plan, the Commonwealth will be able to provide prescription drug coverage to an additional 120,000 seniors.

### **Responding to the New Medicare Prescription Drug Program**

The federal Medicare Modernization Act authorized Medicare Part D, a program to help Medicare beneficiaries with the costs of prescription drugs. This program provides substantial extra help with prescription drug costs for eligible individuals whose income is less than 150 percent of the federal poverty level and whose resources are limited to

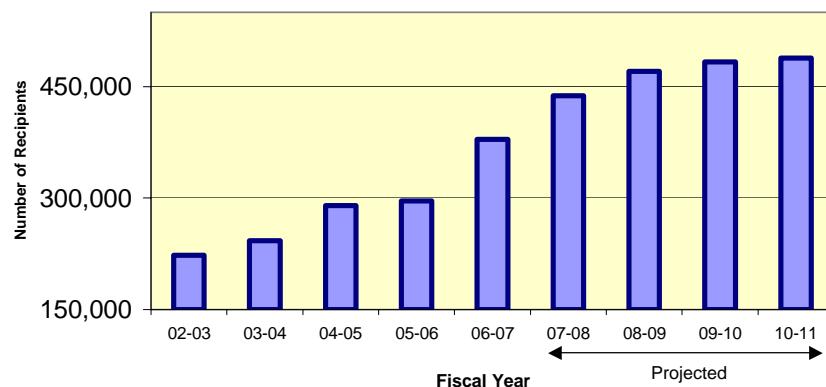
\$10,000 per individual and \$20,000 per couple. This help takes the form of subsidies paid by the federal government to the drug plan in which the Medicare beneficiary is enrolled. The subsidy provides assistance with the premium, deductible, coverage gap and co-payments of the program.

Unlike the continuous coverage provided by PACE/PACENET, Medicare Part D coverage requires recipients with incomes above 150 percent of poverty to incur substantial costs for:

- Plan premiums
- Deductibles
- Higher co-payments than required in PACE/PACENET
- A gap in coverage after the first \$2,250 spent on drugs and a catastrophic benefit that covers most costs only after drug spending exceeds \$5,100
- Restricted formularies and excluded medications

By redesigning the PACE program and creating a new benefit called PACE Plus Medicare, the Commonwealth will address the gaps in the new federal Medicare Part D benefit for PACE/PACENET recipients so that Pennsylvania's seniors will not incur more costs than they otherwise would have paid when their prescriptions were covered by PACE/PACENET.

### **Actual and Projected PACE/PACENET Enrollment**

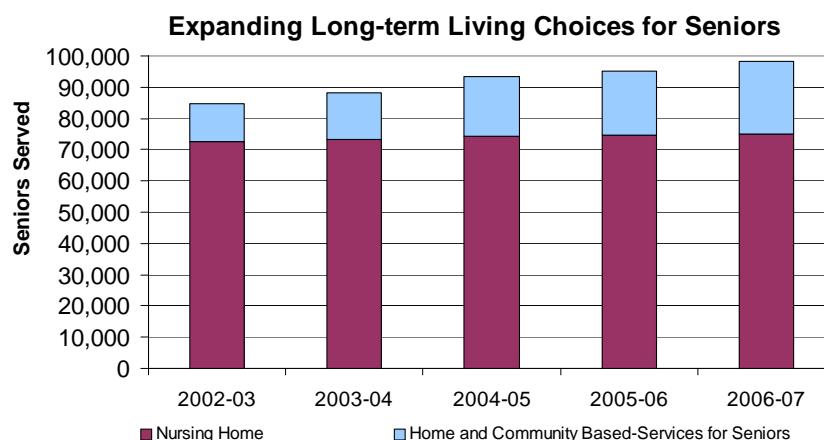


### *Long-Term Living Services – Providing Choice for Pennsylvania’s Seniors*

Under Governor Rendell's leadership, Pennsylvania's recent expansion of Medicaid Home and Community-Based Waiver programs has been successful in providing additional options that enable elderly and disabled individuals to continue to live in their communities. This program expansion has made it possible for more of Pennsylvania's seniors to remain where they want to live – in their homes. The administration has significantly expanded home and community-based programs, increasing participation in the 60+ Waiver program by 70 percent since 2002-03. This budget proposes a further expansion in this program to serve an additional 2,800 people in 2006-07.

Given a choice, an overwhelming number of older Pennsylvanians would prefer to remain in their homes rather than enter a nursing facility. In response to this consumer preference, the Commonwealth is working to "rebalance" the long-term living system so a greater amount and percentage of the Commonwealth's long-term support resources are focused on home and community-based services through the following actions:

- Established the Long-Term Living Council to develop comprehensive, coordinated plans for the future of Medical Assistance long-term living services in the Commonwealth, building upon the successes of the administration's efforts to reform and rebalance the state's long-term-care system.
- Continue to expand Medicaid Home and Community-Based Waiver programs to serve an additional 2,800 seniors in 2006-07. The Commonwealth has increased participation in the 60+ Waiver program by 70 percent since 2002-03 and proposes an additional 14 percent increase in 2006-07.
- Expand efforts to educate and assist nursing home residents who want to return to their homes or communities.
- Streamline the eligibility determination process for consumers to receive in-home services.
- Conduct an extensive study of long-term living demand and supply over the next 20 years to understand how the long-term living industry should look in the future.
- Encourage nursing facilities to reconfigure their businesses to provide an appropriate continuum of supportive services in addition to the skilled nursing services they now provide.



The 2006-07 budget provides:

- \$4.3 million in increased funding to provide for a 2 percent cost of living adjustment for direct care services provided through PENNCARE.
- \$2.1 million in increased State funds to provide services to an additional 240 persons in the PENNCARE Attendant Care Program.

Governor Rendell's goal is to offer eligible Medical Assistance consumers choice in where they receive long-term living services, providing high-quality care to these individuals in the most clinically appropriate and cost-effective environment. This administration believes that consumers' preferences are often to remain in their homes and communities. This budget provides options for an increasing number of Commonwealth seniors to achieve this goal.

# ***Energy and the Environment***

## ***New Industries and a Better Quality of Life for the 21<sup>st</sup> Century***

The businesses and industries Pennsylvania wants to attract and retain have a choice of where they locate. Increasingly, employers judge business locations by their ability to help attract and retain a quality work force. Employers know that workers want the same things we all want – clean air and water, lively neighborhoods and town centers, and abundant green space. That is why improving Pennsylvania's environment and fostering healthy communities has been a major priority of Governor Rendell since he took office in 2003.

### ***Growing Greener II – A \$625 Million Investment in Environmental Improvement and Community Development***

Pennsylvania is proving that the right kind of environmental policies and initiatives can foster economic growth. In January 2006, Governor Rendell strengthened his commitment to build a partnership between the environment and the economy by announcing \$8.5 million in investments for 25 clean energy projects that will leverage more than \$144 million in private sector investment and create more than 1,000 jobs.



To implement his vision of a green and growing Pennsylvania and address our Commonwealth's most critical environmental concerns, Governor Rendell proposed the Growing Greener II plan. This plan was enacted by the General Assembly and approved by the voters in 2005. The \$625 million, six-year Growing Greener II program will provide:

#### ***Developing Alternative Energy Industries in Pennsylvania***

Because of the growing practical appeal of alternative energy, Governor Rendell has made development of alternative energy technologies and industries a major priority in his economic agenda. These efforts range from promoting new plants that will produce diesel fuel from coal, soybeans and other farm products to the Commonwealth's partnership with Gamesa – the world's third largest manufacturer of wind energy equipment – to build plants in Cambria and Bucks counties employing as many as 400 workers.

Pennsylvania must also remain mindful of those traditional industries that have been the bedrock of Pennsylvania's strong industrial and environmental heritage. This budget proposes more than \$500,000 in new funding to enhance Pennsylvania's

- \$230 million to the Department of Environmental Protection to clean up rivers, streams, abandoned mines and contaminated industrial sites, and finance the development and deployment of advanced energy projects.
- \$217.5 million to the Department of Conservation and Natural Resources for natural areas and open spaces, state parks and local recreational needs.
- \$80 million to the Pennsylvania Department of Agriculture to protect working farms.
- \$50 million to the Department of Community and Economic Development for investments in housing and mixed-use redevelopment projects.
- \$27.5 million to the Pennsylvania Fish and Boat Commission to repair fish hatcheries and aging dams and \$20 million to the Pennsylvania Game Commission for habitat-related facility upgrades and repairs.
- In addition, PennDOT is dedicating at least \$200 million in additional funding to its Home Town Streets program, which redesigns and revitalizes state highways that serve as main streets in communities.

underground mine inspection and mine electrical inspection programs to ensure that Pennsylvania mines remain a safe place to work.

Today, Pennsylvania's companies are sending approximately \$30 billion a year outside our state – and in many cases outside our nation – to buy energy. They are doing so because more affordable energy alternatives are not readily available. Governor Rendell's efforts to build Pennsylvania's energy industries and promote economically viable alternative energy companies aimed to create jobs, keep Pennsylvania energy wealth at home, and give Pennsylvanians a cleaner environment even as our economy grows.

# *Public Safety and Security*

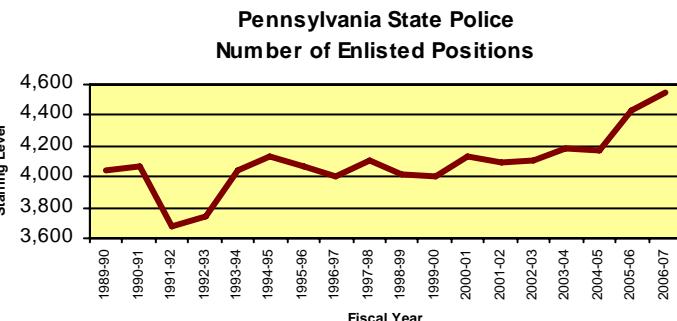
## *A Commonwealth Priority*

One of government's core responsibilities is protecting its citizens. Public safety in the Commonwealth helps to determine the quality of residents' lives and the character of their communities. Governor Rendell has implemented an aggressive and broad-based public safety agenda that will make Pennsylvania and its residents safer. The 2006-07 budget includes a number of public safety initiatives that safeguard Pennsylvania residents by blending support for traditional public safety responsibilities with a comprehensive approach for emergency preparedness.

### **Pennsylvania Is Increasing Its Commitment to Law Enforcement**

In 2005, the Pennsylvania State Police marked 100 years of protecting Pennsylvania's communities and roadways. Recognizing the critical role of the State Police in ensuring public safety in the future, Governor Rendell is proposing an additional 90 trooper positions in 2006-07, bringing the State Police to 4,548 total positions, its highest enlisted complement ever. These 90 trooper positions are in addition to the 180 enlisted personnel included in the 2005-06 budget. The 2006-07 budget assumes that the Pennsylvania State Trooper Association will cease their current effort to block the implementation of

the State Police improved deployment plan so that 30 additional troopers can be hired in 2006, an additional 68 enlisted personnel currently performing desk duties can be transitioned to active law enforcement duties, and 45 experienced corporals can be kept on the road rather than being placed in dispatch centers answering phone calls.



### **Pennsylvania Is Preparing for Public Health Emergencies**

In the post-9/11 world, bio-terrorism has become a serious threat that local, state and national governments must address. This budget includes these initiatives:

- **Public Health Emergency Preparedness and Response.** \$80.8 million in federal funds to develop solutions for bio-terrorism preparedness, notify the medical community of emergency situations and improve the Department of Health's bio-laboratory capabilities.

- **Bio-terrorism Preparedness Measures.** \$8 million to support the National Electronic Disease Surveillance System (NEDSS), an integrated electronic laboratory reporting system that provides on-line reporting and information from laboratories, hospitals and clinicians. \$500,000 to support the Real-time Outbreak Disease Syndromic Surveillance System (RODS), an information-tracking device for Pennsylvania district offices and county health departments.

- **Pandemic Readiness Activities.** Concern about the spread of avian influenza from animals to humans has recently become a top international news story. Pennsylvania has had no reported incidents of avian influenza, but the state is already considered a leader in the prevention, detection and response to avian influenza among animals because of innovative and coordinated programs between the Pennsylvania Department of Agriculture and the Pennsylvania poultry industry.

This budget recommends:

- \$12.3 million in federal grants from the U.S. Department of Health and Human Services for pandemic influenza preparedness during the 2006 federal fiscal year.
- \$500,000 for the Pennsylvania Emergency Management Agency and the Department of Health to coordinate the Commonwealth's statewide avian flu and pandemic preparedness activities.
- \$820,000 for other activities to continue to address this public health priority.

### **Pennsylvania Is Preparing for Natural Disasters**

- **Flood Protection.** \$3.5 million in state funds and \$4.5 million in federal funds for the Hazard Mitigation program to continue the Commonwealth's commitment to safeguarding its residents while maintaining the beauty of its environment.

- **Advanced Security Technology for Safety.** \$4 million for development of a statewide digital map. This map will enable the Commonwealth to share digital imagery data and assist local governments in developing their emergency preparedness plans.

# *Public Safety and Security – A Commonwealth Priority*

## **Pennsylvania Is Increasing Its Emergency Preparedness**

- **Supporting Pennsylvania's First Responders.** \$25 million to continue the Volunteer Company Grants program in 2005-06, and another \$25 million from the State Gaming Fund in 2006-07.
- **Driver's License Security.** \$8.8 million for the first year of a seven-year federal program to create uniform driver's license and personal identification standards. This new program will help prevent identity theft and will strengthen the license credentialing process.
- **Coordination for Emergencies.** The Pennsylvania Emergency Management Agency has been working with the Pennsylvania Office of Homeland Security, the Regional Counter Terrorism Task Forces and other state, local and federal agencies to establish a coordinated approach to response planning. Pennsylvania has integrated a number of new federal programs into its preparedness planning, including:
  - the National Preparedness Goal, to strengthen preparedness for terrorist attacks, major disasters and other emergencies;
  - the National Response Plan, to coordinate state emergency operations centers through the National Emergency Operations Center; and
  - the National Incident Management System, to provide a consistent nationwide approach to incident management.
- **Statewide Radio System.** \$16.9 million for the continued development and operation of the Statewide Radio System, a wireless network that allows for both voice and data communications among all state agencies. This network will be the backbone for interoperable communication across state, federal and local radio systems, resulting in enhanced communications in the event of an emergency.

## **Pennsylvania is Tough on Crime and Working to Reduce the Number of Repeat Offenders**

The Commonwealth is increasing its capacity to incarcerate offenders while at the same time continuing its efforts to address the underlying causes of criminal behavior, improve public safety and reduce victimization.

*Budget highlights include:*

- **Corrections/Probation and Parole.** \$2.1 million to the Department of Corrections to open five new housing units in order to maintain a safe and secure environment for criminals sentenced to the state correctional system. These new units will provide an increase of 920 beds among the following State Correctional Institutions: Camp Hill, Cresson, Laurel Highlands and the State Regional Correction Facility at Mercer.

- **Incarceration and Rehabilitation.** Tackling prison population growth is just one of the incarceration and rehabilitation issues the Commonwealth must address. The horrific nature of sex offenses and the complexity of treating sex offenders require a different approach. Therefore, criminal justice agencies in Pennsylvania are developing a comprehensive statewide containment plan for the treatment and management of sex offenders.

## **Pennsylvania is Responding Proactively to Federal Base Closing Activities**

During the U.S. Department of Defense 2005 military Base Realignment and Closure (BRAC) process, the Commonwealth helped Pennsylvania's military communities and local leaders effectively defend Pennsylvania's 274 military installations from closure or realignment. The results were employment gains at Letterkenny and Tobyhanna army depots, as well as at the Naval Support Activity in Philadelphia. The Commonwealth also successfully defended the 911th Airlift Wing at Pittsburgh International Airport and the 111th Fighter Wing of the Pennsylvania Air National Guard. These federal installations and the active duty, reserve and National Guard personnel that serve on them are vital homeland security and public safety assets, as well as economic engines for many Pennsylvania communities.

*Budget highlights include:*

- \$275,000 for continued funding for the Pennsylvania Base Development efforts that helped prepare Pennsylvania so well for BRAC 2005 and that will help Pennsylvania implement a coordinated strategy of workforce and economic development programs to sustain military installations in the Commonwealth into the future.

## **Pennsylvania is Supporting our Troops**

The Pennsylvania National Guard is one of the best and largest in the nation. Its men and women have been called upon to support the global war on terror in Afghanistan, Iraq and Kosovo. Additionally, Pennsylvania's National Guard deployed more than 2,500 troops to support hurricane-ravaged areas in Louisiana and Mississippi in 2005 – the most of any state outside of the region affected by the hurricanes.

*Budget highlights include:*

- \$300,000 for the implementation of Governor Rendell's Support Our Troops initiative and other veterans' programs. Among its elements is a new Military Family Relief Assistance Program to help soldiers and their families who face emergency situations. In addition, the Pennsylvania National Guard's Educational Assistance program has been improved by extending benefits for soldiers who have deployed since September 11, 2001.

# *Transportation*

## *Key to Pennsylvania Growth and Opportunity*

Pennsylvania's transportation system is a complex network of interstate highways, state and local roads, bridges, railroads, air carriers and public transit agencies. Governor Rendell is committed to increasing the quality and safety of each part of that network and investing resources wisely across the network. By developing creative solutions, Governor Rendell has saved public transit systems from a financial crisis while at the same time increasing the amount of funding available for roads and bridges.

### **Highway and Bridge Investments**

The condition of Pennsylvania's interstate highways improved steadily during the late 1980s and early 1990s to the point where the average rating went from "poor" to "good" in 1997, according to the widely used International Roughness Index (IRI). This trend slowed from 1999 to 2002, with no improvement seen. In 2003, after Governor Rendell took office, interstate highway pavement quality began to improve again.

Accessibility, structural integrity and safety are priorities for our roads and bridges. Under Governor Rendell's leadership, the quality of Pennsylvania's roads and bridges has been improving, and funding for their maintenance and repair has increased significantly. This budget provides significant new investments to continue these efforts.

- **Smoother Roads and Priority Bridges.** \$100 million, or 200 percent, increase to allow highway maintenance resurfacing repairs to increase by 550 miles in the first year and 530 miles in the second year of the program.
- **Bridge Preservation.** \$20 million increase to further expand the bridge restoration program to repair approximately 200 to 250 additional bridges.
- **Emergency Highway and Bridge Repairs.** \$10 million, or a 54 percent, increase to address 15 to 20 more emergency repair situations such as storm repair, slide conditions and sink holes.

This budget also recommends increasing the Highway Maintenance Safety Projects appropriation by \$5 million as a state match for a projected \$34 million federal grant from the federal SAFETEA-LU program. The Safe, Accountable, Flexible, Efficient Transportation Equity Act, A Legacy for Users is a federal law that created a dedicated funding source for states' highway safety improvement programs.

The following chart shows annual spending on PennDOT's bridge program from 1999 to 2006.



### **Public Transit Funding and the Need for an Integrated Transportation Funding Strategy**

Assuring viable transportation options for all Pennsylvanians means the Commonwealth must provide continuing adequate support for its transit agencies. Achieving this has been difficult in the past. Public transit does not have the same predictable, growing funding source that highway and bridge programs have in the Motor License Fund. The transit-funding package enacted in 1991 was intended to solve this problem. However, the revenue sources did not meet the high revenue projections used when the bill was crafted, causing a deficit for the Commonwealth's public transportation spending authority.

In February 2005, Governor Rendell announced an interim solution that will provide more than \$400 million in non-recurring funding for Pennsylvania's transit agencies over the next two years. This money will come from federal transportation funds provided to Pennsylvania, a major portion of which can be used for either roads or public transit. Without the use of this federal "flex" funding, 13 transit agencies would have faced a funding gap of \$343 million that would have shut down their major transit operations and affected more than 10 million transit passengers.

# Transportation – Key to Pennsylvania Growth and Opportunity

Total Pennsylvania Highway Funding					Flexed Funds for Transit		
	(Dollar Amounts in Millions)				(Dollar Amounts In Millions)		
	State Funding	Federal Funding	Total Funding	Dollar Change	Percent Change	Standard Federal	"Crisis" Federal
2000-01	\$2,943	\$1,112	\$4,055	–	–	\$46	–
2001-02	\$2,940	\$1,272	\$4,212	\$157	3.9%	\$36	–
2002-03	\$2,949	\$1,265	\$4,214	\$2	0.0%	\$31	–
2003-04	\$2,966	\$1,205	\$4,171	(\$43)	-1.0%	\$59	–
2004-05	\$3,124	\$1,081	\$4,205	\$34	0.8%	\$48	\$74
2005-06	\$3,518	\$1,424	\$4,942	\$737	17.5%	\$25	\$202
2006-07	\$3,758	\$1,436	\$5,194	\$252	5.1%	\$25	\$138

Even after “flexing” some additional federal transportation funds to keep the state’s 13 transit agencies operating, Pennsylvania highway spending is still growing substantially, with an anticipated \$252 million increase in total funds in 2006-07. Part of that increase is an additional \$130 million in state funds for the Commonwealth’s highway and bridge infrastructure, including \$100 million for the Smoother Roads and Bridges program, \$20 million for the Bridge Preservation program and \$10 million for the Emergency Highway and Bridge Maintenance Repair program. Pennsylvania highway spending in 2006-07 is 23 percent, or \$980 million, higher than when Governor Rendell took office.

Having achieved a temporary resolution of the transit-funding crisis, Governor Rendell has formed a commission to recommend a strategy to provide adequate, appropriate, sustainable funding for Pennsylvania’s transit systems, roads and bridges. The Transportation Funding and Reform Commission includes four legislative appointees and represents a cooperative effort to identify a permanent solution for public transit funding.

## Increasing Transportation’s Role in Economic Development

The 2006-07 budget enables PennDOT to support 20 additional transportation projects linked to economic development through an \$8 million, or 40 percent, increase to the Pennsylvania Infrastructure Bank. This low-interest loan program offers municipal governments flexible financing opportunities for transportation projects tied to economic development throughout the Commonwealth.

## State Highway and Bridge Construction

- \$613 million in state and \$1.2 billion in federal funds, for new construction and major repairs of highways and bridges.



## State Highway and Bridge Maintenance

- \$1.5 billion in state and \$214 million in federal funds, for the maintenance of the Commonwealth’s bridges and highways.

## Mass Transportation

- \$758 million in state and \$62 million in federal funds, for operating and capital assistance to mass transit agencies, including a \$2.9 million increase in State funding.

## Transit Assistance for Older Pennsylvanians

- \$152.3 million in State Lottery Funds in support of Older Pennsylvanians’ Free and Shared Rides.

## Local Road Maintenance and Construction Payments

- \$334 million to municipal governments for local road maintenance and construction.

## Rail Freight Assistance

- \$10.5 million to provide maintenance and capital support for non-state owned rail lines.

## Air Transportation

- \$8 million in state aviation funds to provide airport development grants for public use airports.

# 2006-07 GENERAL FUND REVENUES

PA Revenue Sources			
Dollars in Millions	Actual Collections 2004-05	Estimated Collections 2005-06	Estimated Collections 2006-07
Personal Income Tax	\$ 8,746.8	\$ 9,331.7	\$ 9,848.9
Sales and Use Tax	\$ 8,000.0	\$ 8,281.0	\$ 8,621.3
Corporate Net Income Tax	\$ 1,921.4	\$ 2,129.0	\$ 2,142.2
Capital Stock and Franchise Tax*	\$ 1,025.9	\$ 1,045.9	\$ 880.2
Gross Receipts Tax	\$ 1,125.9	\$ 1,064.9	\$ 1,113.3
Cigarette Tax	\$ 784.4	\$ 779.9	\$ 768.1
Other Taxes	\$ 2,108.1	\$ 2,193.1	\$ 2,319.3
Non-Tax Revenues	\$ 596.0	\$ 528.1	\$ 656.9
Total	\$ 24,308.5	\$ 25,353.6	\$ 26,350.2
Difference from prior year	\$ 1,480.4	\$ 1,045.1	\$ 996.6
Percentage Difference		4.3%	3.9%

\* Act 46 of 2003 modified the scheduled phaseout of the Capital Stock and Franchise Tax. For tax year 2004 the rate was 6.99 mills. For tax year 2005 the rate was 5.99 mills. For tax year 2006 the rate is 4.99 mills and this budget proposes to accelerate the reduction by an additional 0.1 mills in tax year 2006 after which the rate will then be reduced annually by one mill until the tax is eliminated in 2011.

# 2006-07 MOTOR LICENSE FUND

## INCOME

(Dollars in Millions)



Liquid Fuels Tax — \$1,273  
Licenses and Fees — \$876  
Other — \$130

Total Income .....	\$2,279
Beginning Balance ...	253
<b>TOTAL .....</b>	<b>\$2,532</b>

## OUTGO

(Dollars in Millions)



Maintenance — \$1,064  
Improvement, Design — \$371  
State Police — \$435  
Other — \$257  
Local Subsidy — \$210  
Licensing and Safety — \$138  
Debt Service — \$23

Total Outgo .....	\$2,298
Ending Balance .....	34
<b>TOTAL .....</b>	<b>\$2,532</b>

# 2006-07 GENERAL FUND REVENUES

## **Major Tax Saving Initiatives (2003-04 through 2006-07)**

Dollars in Millions

	<u>2003-04</u>	<u>2004-05</u>	<u>2005-06</u>	<u>2006-07</u>
Continued CSFT Phase Out*	\$ 9.1	\$ 71.8	\$ 213.7	\$ 404.6
Special Poverty Expansion (\$500 per dependent)	-	13.9	13.6	13.3
Research and Development Tax Credit Expansion*	-	15.0	15.0	25.0
Sales Tax Credits (Call Centers)	-	30.0	30.0	30.0
Sales Tax Credits (Telecommunications)	-	40.2	42.6	45.3
Inheritance Tax (recouple to federal return basis)	22.1	55.2	76.7	83.6
Education Improvement Tax Credits	10.0	15.0	19.0	19.0
Keystone Innovation Zone Tax Credits	-	-	-	25.0
Film Production Tax Credit	-	-	10.0	10.0
Keystone Opportunity Zones	-	2.9	2.9	0.9
Malt Beverage Investment Tax Credit	0.9	1.2	1.2	1.2
Expansion of NOL Cap*	-	-	-	7.3
<b>Annual Total .....</b>	<b>\$ 42.1</b>	<b>\$ 245.2</b>	<b>\$ 424.7</b>	<b>\$ 665.2</b>
<b>Cumulative Total .....</b>	<b>\$ 42.1</b>	<b>\$ 287.3</b>	<b>\$ 712.0</b>	<b>\$ 1,377.2</b>

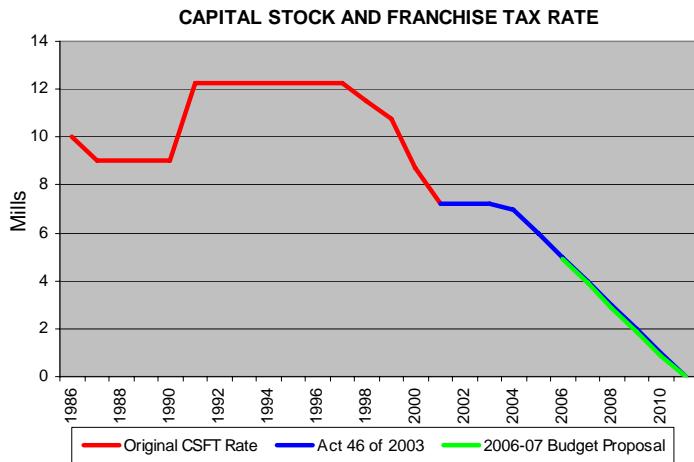
\*Includes additional items proposed in Governor's FY 2006-07 Budget

The 2006-07 budget includes over \$221 million in Tax Cuts

- Effective with tax year 2004, the Capital Stock and Franchise Tax was reduced by a quarter mill from 7.24 mills to 6.99. The rate was reduced an additional 1 mill on January 1, 2005 and 2006 bringing the current rate to 4.99 mills. The FY 2006-07 Budget proposes to accelerate the rate reduction by 0.1 mill in 2006, making the rate 4.89. For each additional tax year, the rate will decline by one mill. Tax savings in the chart above are based on revisions to the rate versus a 7.24 mill base.
- The Research and Development Tax Credit was increased from \$15 million to \$30 million in Act 46 of 2003. The 2006-07 Budget proposes to increase the tax credit by an additional \$10 million to \$40 million.
- The 2006-07 Budget proposes to increase the annual cap on deductions for Net Operating Loss Carryforward from \$2 million to \$3 million effective January 1, 2007.

Other recent tax changes include:

- For calculation of the Special Poverty Provisions for Tax Forgiveness, the dependent allowance was increased from \$9,000 to \$9,500 in Act 46 of 2003. Exemptions remain at \$6,500 for single claimants and \$13,000 for married claimants with no dependents. A family of four with two claimants and two dependents earning less than \$32,000 in taxable income will therefore pay no state income tax.
- Act 46 of 2003 established Sales and Use Tax credits for call centers and extended the processing exemption to cellular telecommunications.
- Revisions to the Inheritance Tax re-coupled Estate Tax to the Federal Estate Tax Provisions, thereby reducing state tax liability.



An additional \$1.2 billion in revenue would be collected in FY 2006-07 if the Capital Stock and Franchise Tax rate had remained at 12.25 mills.

- Education Improvement Tax Credits (EITC) were expanded in Act 48 of 2003 by \$10 million to \$40 million for donations to scholarship organizations that provide personal tuition grants to private schools and non-profit organizations that fund innovative education programs in public schools. Act 48 also permits up to \$5 million in EITC tax credits for donations to pre-school scholarship organizations. Act 46 of 2005 expanded the EITC by an additional \$4 million annually.
- Keystone Innovation Zone Tax Credits were established in Act 12 of 2004 to foster growth in targeted industry segments, namely research and development and other high technology businesses.
- Act 95 of 2004 provided for up to \$10 million in Film Production Tax Credits to be awarded annually. These credits are equal to 20 percent of qualified film production expenses incurred in Pennsylvania.

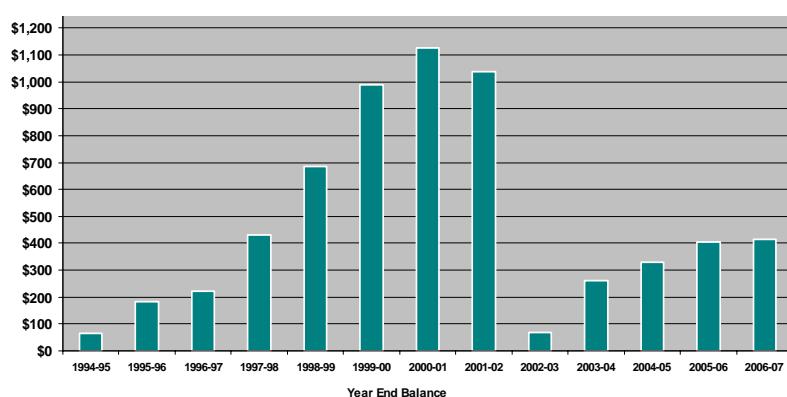
# 2006-07 GENERAL FUND FINANCIAL STATEMENT

	Dollars In Millions		
	2004-05 Actual	2005-06 Available	2006-07 Budget
<b>Beginning Balance.....</b>	\$77	\$365	\$204
<b>Revenue:</b>			
Revenue Receipts .....	\$24,309	\$25,353	\$ 26,350
Less Refunds .....	(1,000)	(1,075)	(1,125)
Total Revenue.....	\$23,309	\$24,278	\$25,225
Prior Year Lapses.....	97	120	---
Funds Available.....	\$23,483	\$24,763	\$25,429
<b>Expenditures:</b>			
Appropriations.....	\$23,054	\$24,304	\$25,425
Supplemental Appropriations.....	---	197	---
Less Current Year Lapses.....	---	(10)	---
Total Expenditures.....	23,054	24,491	25,425
Closing Balance.....	\$429	\$272	\$4
Less Transfer .....			
Budget Stabilization Reserve Fund.....	(64)	(68)	(1)
<b>Ending Balance.....</b>	<b>\$365</b>	<b>\$204</b>	<b>\$3</b>

- The Governor has proposed a General Fund Budget for 2006-07 that increases State spending by \$924 million, or 3.8 percent.
- Increases in debt service of 19.7 percent, increases in Pre K –12 and Higher Education of 5.9 percent and Public Welfare of 3.5 percent are offset by a decrease of 2.5 percent in the remainder of the General Fund budget.

## 2006-07 RAINY DAY FUND

Millions



- Rainy Day Fund balances were built up substantially during the latter part of the 1990s and peaked at more than \$1 billion in 2000-01. The Fund was depleted in order to balance the 2001-02 and 2002-03 General Fund budgets. The current balance in the Fund is \$334 million. The 2006-07 budget projects statutory transfers of \$68 million from 2005-06 and \$1 million from 2006-07. Rating Agencies recommend that reserves of at least 5 percent of annual revenues be held in a Rainy Day

Fund in case of an economic downturn. To meet this criteria, Pennsylvania would have to increase the Rainy Day Fund balance to \$1.32 billion, an increase of \$905 million.

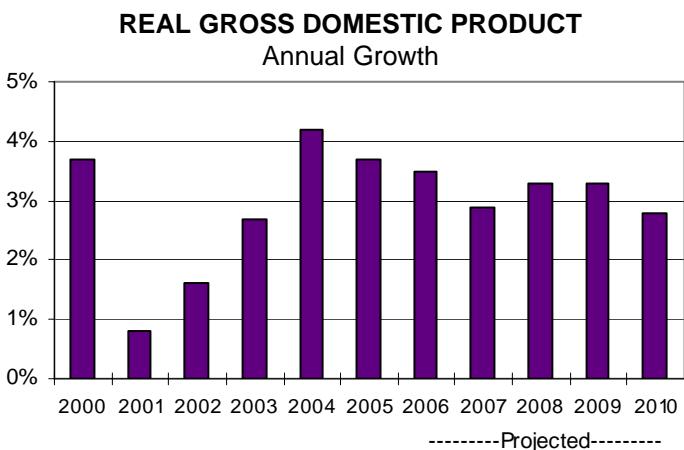
# THE ECONOMIC OUTLOOK FOR 2006-07

## The Forecast is for Moderate Economic Growth

Economic forecasts are a key ingredient in constructing the budget's revenue forecasts and they also help the government project likely levels of demand for many public goods and services.

### Recent Economic Trends

The expansion of the national economy has been steady since 2002, despite repeated external shocks that have occurred in the post-recession period.



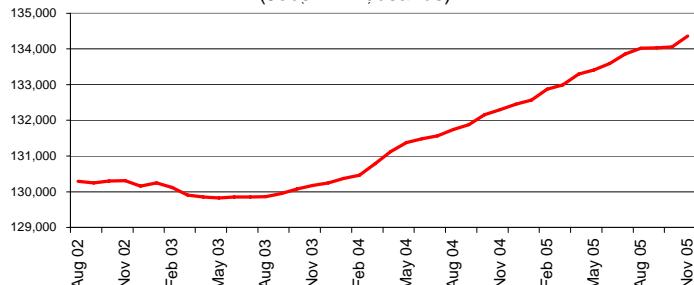
The first two years of the current economic expansion (2002-2003) were characterized by unabated job losses in which more than 3 million jobs were lost despite a moderately growing national economy.

Positive overall job growth in the broader economy returned in 2004 and 2005. Job growth during 2004 added approximately 2.0 million jobs during that year. Employment levels grew faster in 2005 as approximately 2.6 million jobs were added during the past year.

The U.S. unemployment rate currently stands at 4.9 percent, down from its nine-year high of 6.3 percent in June 2003.

### U.S. EMPLOYMENT GROWTH

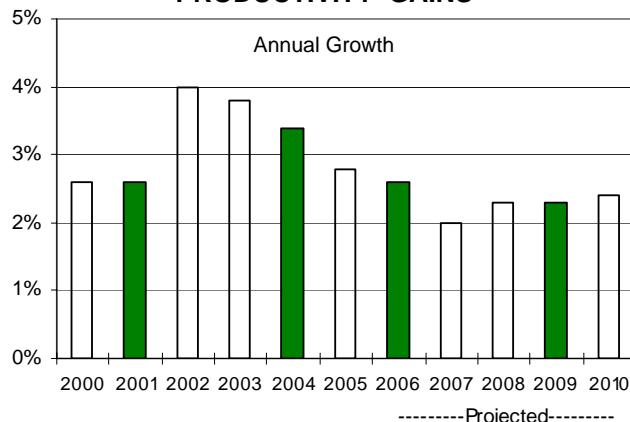
Non-Agricultural  
(Jobs in Thousands)



Productivity gains from 2001 to 2005 have driven the business sector side of the current economic expansion, with a 3.4 percent average annual rate of growth in productivity. This surge exceeds any productivity growth since the 1960s.

The gains in productivity over the last four years have helped to hold inflation in check, but these factors are eroding. Recent output gains have slowed and payrolls are expanding, which is leading in turn to upward pressure on wages and prices.

### PRODUCTIVITY GAINS



After dropping to 1.6 percent annual growth in 2002, inflation has been building over the past three years. Rapidly rising energy costs, rising labor costs, and increases in health care costs combined with a weak dollar pushed inflation to 3.4 percent in 2005

### Forecast For 2006

After experiencing broad-based growth during the past two years, as evidenced by 4.2 percent annual growth in real GDP during 2004 and 3.7 percent in 2005, the economy is expected to slowly throttle down over the next two years. Annual growth in real GDP is projected to moderate to 3.5 percent in 2006 and 3.0 percent in 2007

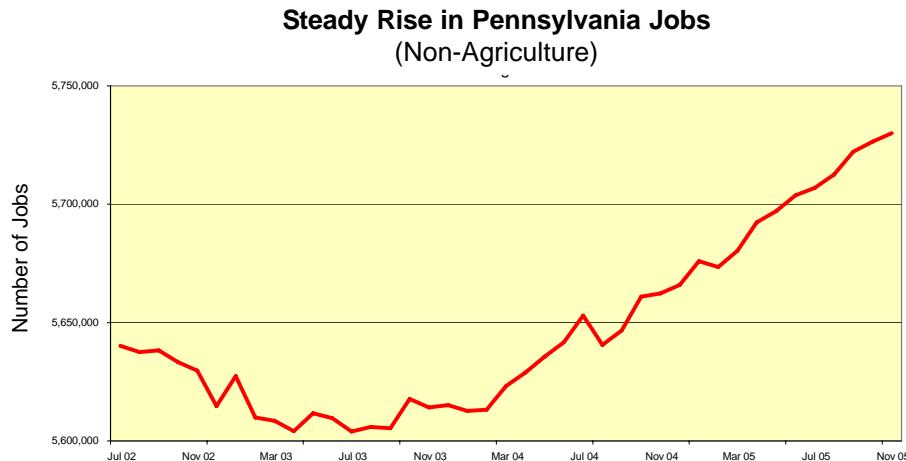
Rising prices, tightening labor markets and rising interest rates are primary causes for slightly lower growth rates in the forecast. The forecasts anticipate that the economic expansion will continue in 2006 as a business-driven expansion.

Moderate job growth of approximately 160,000 per month, or approximately 2 million jobs per year, is expected to continue during 2006. Job growth combined with growth in the labor force will keep the unemployment rate around 4.8 percent. Slower gains in productivity will continue to encourage an increase in payrolls in 2006. Rising interest rates will continue to slow growth in the housing sector.

Inflationary pressures are expected to continue in 2006, as the price of oil will weigh heavily on the economy. A continuation of high oil prices will limit consumer spending and raise costs for businesses.

A continuation of the recent quarter point increases in the federal funds rate is expected in order to slow growth in real GDP to around 3 percent annually.

Interest rates, as measured by the federal funds rate, are projected to rise from their current level of 4.25 percent to around 4.75 percent.



## **The Outlook for Pennsylvania**

The most recent Index of State Economic Momentum, published by State Policy Reports, indicates that the Commonwealth vaulted twelve spots to 30th in total economic momentum in the 2005 Index, as measured by the combination of population growth, personal income growth, and employment growth.

Pennsylvania had been ranked 42nd in total economic momentum the same index in 2004; it now currently outranks all surrounding states except Maryland and Delaware.

The Commonwealth ranked 26th in personal income growth in the 2005 Index, an improvement over the 35th ranking in that category in the same study from 2004 and a 38th ranking in 2003.

In the 2005 Index, Pennsylvania ranked 29th in employment growth, which represents an improvement on the Commonwealth's ranking of 43rd in 2004.

In terms of population growth, Pennsylvania continues to lag behind the national average, ranking 43rd in percent growth in population for 2005. If not for this last factor, Pennsylvania's economy would have ranked even higher than 30th in the Index of State Economic Momentum.

Pennsylvania's labor market started to grow significantly in mid-2003. The growth continued through all of 2004 and 2005.

In 2005 Pennsylvania experienced continued job creation and somewhat slower growth in the overall labor force. This led to a decline in Pennsylvania's unemployment rate, to a low of 4.6 in October 2005.

To date, the Pennsylvania economy has generated more than 100,000 new jobs in the past three years. By November 2005, total non-farm jobs reached a record high of 5.73 million.

Despite an initially slow recovery and continued job losses through 2003, the Commonwealth's growth in real personal income outperformed the national average in 2001 and 2002 and closely trailed growth nationally in 2003.

Personal income growth in Pennsylvania has remained strong and positive. In fact, the Commonwealth actually outperformed the U.S. in terms of annual percent growth in real personal income in 2005. This performance indicates both a strengthening state economy as well as a tightening state labor market.

Thanks to enhanced economic development efforts, an improving business climate (with business costs now roughly equal to the national average) and a strong pattern of positive job creation, Pennsylvania's economy is poised for growth in the near term.

Indicator	Forecast Change in Key US Economic Indicators			
	Annual Percentage Growth*			
	2004	2005p	2006p	2007p
Nominal GDP	7.0	6.5	6.1	4.8
Real GDP	4.2	3.7	3.5	2.9
Real Personal Consumption	3.9	3.5	3.2	3.3
Corporate Profits (After Tax)	11.8	35.3	5.8	-2.0
Unemployment Rate (Rate)	5.5	5.1	4.8	4.9
CPI	2.7	3.4	2.5	1.4
Federal Funds (Rate)	1.3	3.2	4.7	4.8

\*Assumptions contained herein as well as others are incorporated in the 2006-07 fiscal year revenue estimates.  
p=projected

# CAPITAL BUDGET

Fiscal Year 2006-07

	<u>Millions</u>
<b>From Bond Funds</b>	
Agriculture .....	\$ 15.0
Conservation and Natural Resources .....	10.0
Corrections .....	54.3
Education .....	80.4
Emergency Management .....	2.4
Environmental Protection .....	6.8
Historical and Museum Commission .....	6.7
Public Welfare .....	9.6
Transportation-Local Transportation Assistance .....	348.5
Subtotal Bond Funds .....	<u>\$ 533.7</u>
<b>From Current Revenues</b>	
Conservation and Natural Resources .....	\$ 203.9
Transportation-Highways & Bridges .....	963.6
Subtotal Current Revenues .....	<u>\$ 1,167.5</u>
<b>TOTAL CAPITAL PROJECTS TO BE AUTHORIZED .....</b>	<b><u>\$ 1,701.2</u></b>

The Capital Budget process provides for the acquisition, design, construction, and or renovation of new or existing Commonwealth buildings, facilities, physical betterments or improvements.

## Agriculture

*Provides for improvements to the Farm Show Complex, agricultural laboratories and other agricultural-related facilities.*

## Conservation and Natural Resources

*Provides for construction and renovation of support, day use, camping facilities and utility systems at the State parks; construction of district offices, central garages, radio communications systems and rehabilitation of forest roads in forest districts.*

## Corrections

*Provides for construction and renovation of administrative, industrial, educational and housing facilities, and utilities at the State-owned correctional institutions.*

## Education

*Provides for construction expansion, renovation and conversion of classrooms and auxiliary buildings, utilities and recreational facilities for the State System of Higher Education, State-Owned Schools and for the State-Related Universities.*

## Emergency Management Agency

*Provides for construction and renovation at the State Fire Academy, Emergency Operations Centers around the State and other emergency facilities.*

## Environmental Protection

*Provides for construction and improvement projects to protect the environment and the health and safety of citizens using state lands and waterways. These projects include flood protection construction and flood control projects.*

## Historical and Museum Commission

*Provides for restoration and renovation of historic facilities, installation of fire and security systems, development of fixed exhibits and miscellaneous building and utility improvements at Commonwealth owned museums and historic sites.*

## Public Welfare

*Provides for construction and renovation of patient buildings, support facilities and utilities at the state institutions for the mentally ill and mentally retarded, restoration centers and youth development centers.*

## Transportation

*Provides for improvements for local mass transit agencies, rail freight and air transportation projects. Also provides for the construction, and reconstruction of highways and bridges on the Commonwealth road system and major federally designated safety projects.*