

## Commonwealth of Pennsylvania

# 2008-09 Budget Update

**Mary A. Soderberg**  
*Secretary of the Budget*

**October 6, 2008**

## Economic Outlook

**Finance officials “are concerned at the prospect of even slower growth – or even outright revenue declines – over the next year to 18 months. I don’t think there’s any question you’re going to see across-the-board cuts in a lot of states.”**

*– Scott Pattison, Executive Director  
National Association of State Budget Officers  
Wall Street Journal Online, October 1, 2008*



# Senate Appropriation Hearing

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## Examples: State Program Cuts

- Programs are being cut across multiple areas of state government services. For example:
  - New York State agencies are implementing operational expense reductions of more than 10 percent from the Executive Budget issued in January for \$1.1 billion in savings, and Governor Paterson and the legislature partnered to enact another \$427 million in budget reductions in an unprecedented August special session
    - With the ongoing downturn, Governor Paterson has called for renewed meetings to consider an additional round of cuts
  - The State of Maryland budget approved in April included more than \$500 million in reduced expenditures, including cuts or delays to funding for Chesapeake Bay cleanup, a health care insurance expansion and state contributions to retiree health care obligations
    - Maryland Governor O'Malley has directed state agencies to identify further budget cuts of up to 5 percent more to address an additional \$1 billion deficit now projected for 2010

**“We are in profound economic crisis.** We have already taken extraordinary action to contain state spending, but the events that have unfolded in our state and nation over the last two weeks have created an urgent need for a reassessment of the current year’s budget and the planning for next year’s.”

- New York Governor David Paterson (September 25, 2008)

Sources: Iris J. Lav and Elizabeth Hudgins, Center on Budget and Policy Priorities, “Facing Deficits, Many States Are Imposing Cuts That Hurt Vulnerable Residents” (March 13, 2008); Washington Post, “Restraint in Bleak Times for Maryland (April 8, 2008); baltimoresun.com “The issues” (April 8, 2008)

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## Examples: State Program Cuts

**“States are in a world of hurt.”**

– Steve Kreisberg, AFSCME Director of Collective Bargaining (September 30, 2008)

- The adopted New Jersey 2009 fiscal year budget eliminated two state agencies, reduced the state workforce by 3,000, cut funds for hospital charity care by 15 percent and slashed aid for municipalities. Overall budget cuts totaled \$600 million
  - New Jersey Governor Corzine has directed his cabinet to develop options for further 5 percent reductions across all departments for an additional budget cut of \$500 million
- Illinois Governor Blagojevich cut \$1.4 billion from the 2009 fiscal year budget, announcing the elimination of 450 child welfare jobs, the closing of 25 state parks and historic sites, and severe cuts in substance abuse centers and mental health treatment
  - While the Illinois legislature has proposed partial restoration using one-time sweeps from special funds, August revenues are now down an estimated \$457 million from the same time last year and next steps remain uncertain
- Massachusetts Governor Patrick is seeking expanded emergency budget cut authority with tax collections \$200 million below prior-year levels

Sources: Iris J. Lav and Elizabeth Hudgins, Center on Budget and Policy Priorities, “Facing Deficits, Many States Are Imposing Cuts That Hurt Vulnerable Residents” (March 13, 2008); WNBC “N.J. State Budget Cuts Would Fell 9 State Parks, 80 Workers” (April 1, 2008); Stateline.org, “States act to cushion Wall St. meltdown” (September 30, 2008); Philadelphia Inquirer, “Trying times lead Rendell, Corzine to cuts” (October 2, 2008); The Daily Journal, “Plunging revenues may mean more cuts statewide” (October 2, 2008); The State Journal-Register, “Budget issues far from decided” (September 29, 2008)

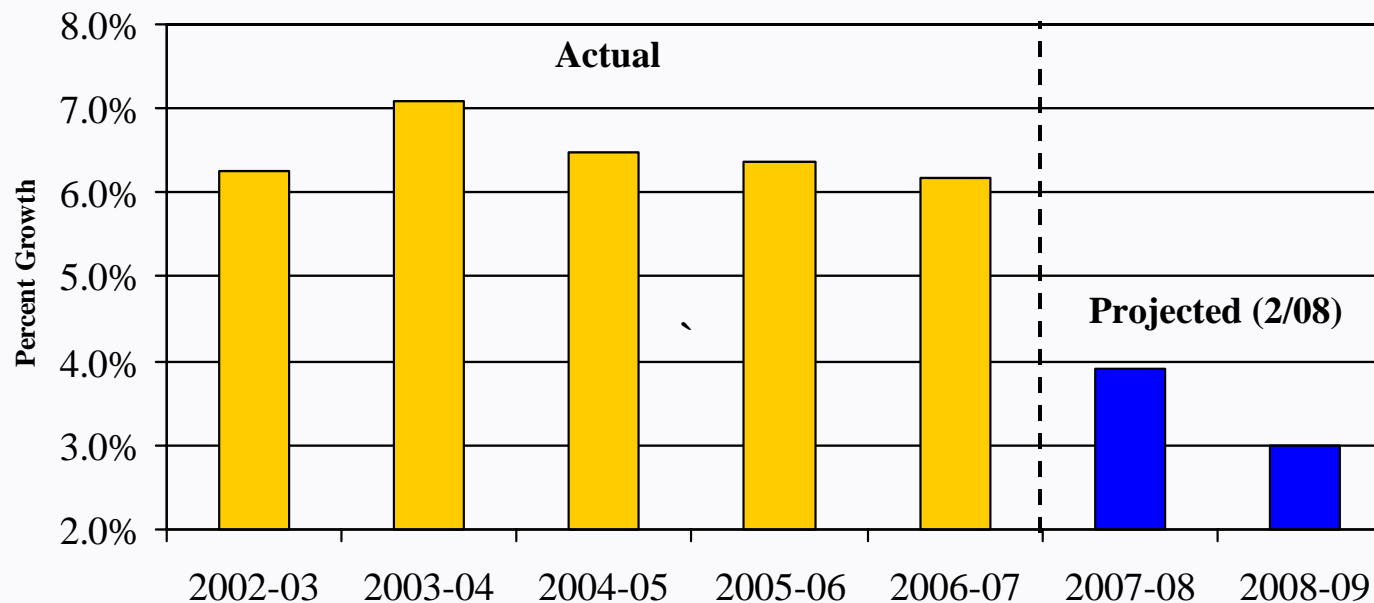
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## General Fund Revenue Growth *2002-03 through 2008-09 estimated*

*This uncertainty about the direction of the national economy has caused Pennsylvania to reduce the projected rate of growth in 2008-09 General Fund revenues to only 3 percent – a reduction of more than 50 percent from the average annual rate of growth the commonwealth experienced between 2002-03 and 2006-07.*

## General Fund Revenue Growth *Increase from Prior Fiscal Year*



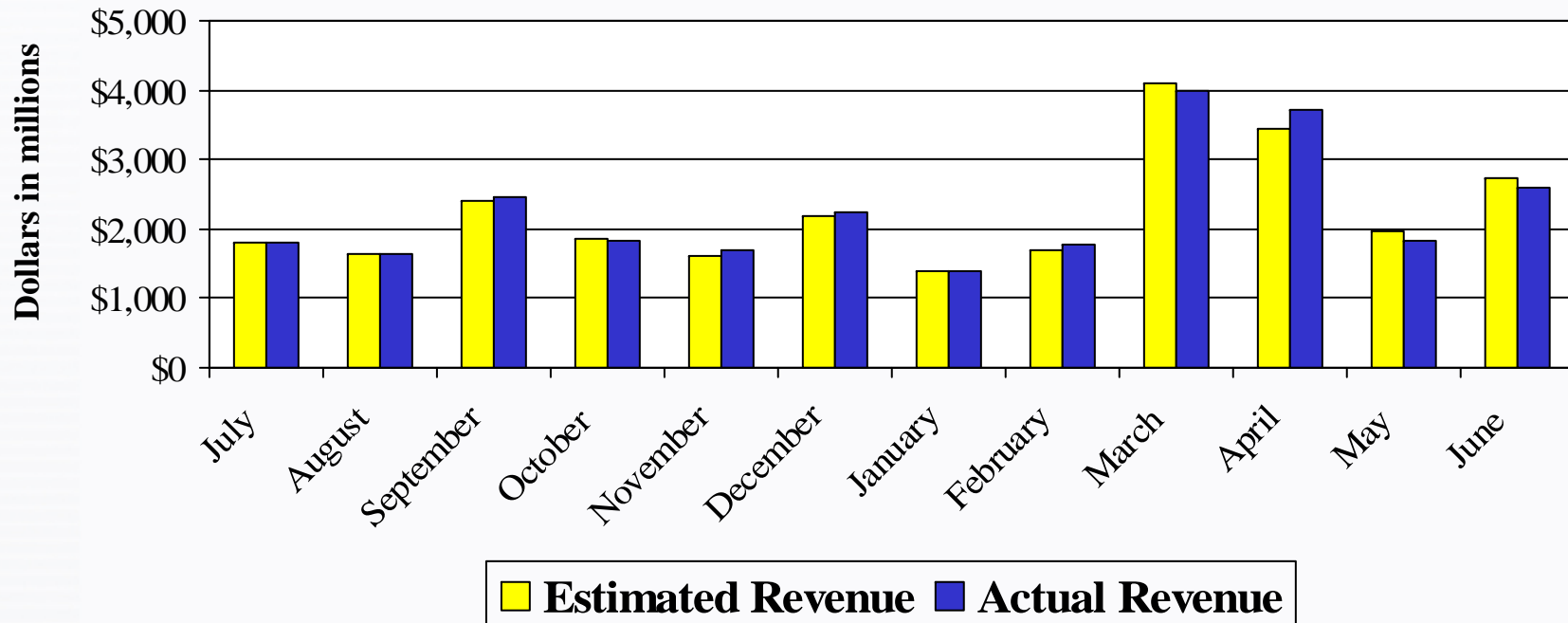
\* 2007-08 includes \$320 million that has been transferred to the new Public Transportation Trust Fund

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## 2007-08 General Fund Revenues *Estimated versus Actual Revenue Collections*

*In three of the last four months of 2007-08, monthly revenue collections were lower than estimated. Even so, collections for the fiscal year ending in June 2008 were \$27.9 billion, or \$167 million more than estimated.*



## **Budget-Balancing Measures During 2008-09 Budget Enactment**

- One-time 2008-09 revenue and expenditure adjustments
- Suspended 2007-08 transfer to the Rainy Day Fund
- Increased 2007-08 and prior-year lapses
- Targeted expenditure reductions
- 1.3 percent across-the-board expenditure reductions



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## Selected 2008-09 General Fund Spending Cuts

*The 2008-09 enacted budget made numerous cuts to the Governor's recommended amounts.*

<u>Department</u>	<u>Appropriation</u>	<u>Dollars</u> <u>(in millions)</u>
Commission on Crime and Delinquency	<i>Police on Patrol</i>	- \$10
Community and Economic Development	<i>Infrastructure Development</i>	- \$10
	<i>Opportunity Grant Program</i>	- \$12
Conservation and Natural Resources	<i>State Parks Operations</i>	- \$1
Corrections	<i>Inmate Education and Training</i>	- \$1
	<i>State Correctional Institutions</i>	- \$25
Education	<i>Special Education</i>	- \$14
	<i>Classrooms for the Future</i>	- \$45
Environmental Protection	<i>Environmental Protection Operations</i>	- \$2
Public Welfare	<i>County Child Welfare</i>	- \$8
	<i>Mental Health Services</i>	- \$5
Revenue	<i>Technology and Process Modernization</i>	- \$5

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## 2008-09 Enacted General Fund Budget

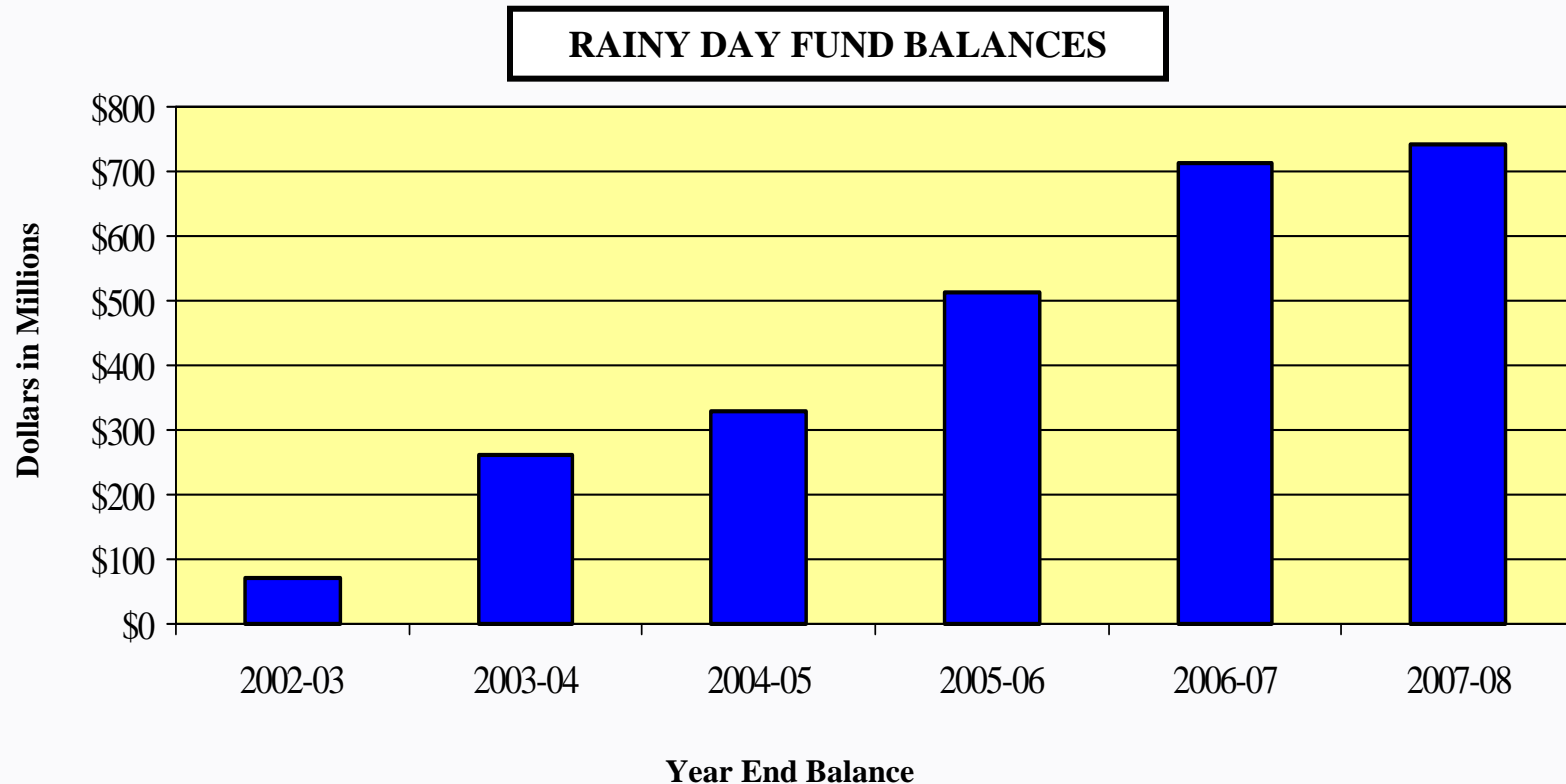
	Dollars in Millions	
	<u>2007-08</u> Actual	<u>2008-09</u> Enacted
Beginning Balance .....	\$ 531	\$ 583
Receipts .....	26,878	27,689
Prior-Year Lapses .....	142	.....
Funds Available .....	<u>\$ 27,551</u>	<u>\$ 28,272</u>
Expenditures .....	\$ - 27,175	\$ - 28,264
Supplemental Appropriations .....	- 7	.....
Current-Year Lapses .....	214	.....
Total Expenditures .....	<u>\$ - 26,968</u>	<u>\$ - 28,264</u>
Preliminary Balance .....	\$ 583	\$ 8
Transfer to Rainy Day Fund .....	.....	- 2
Ending Balance .....	<u><u>\$ 583</u></u>	<u><u>\$ 6</u></u>

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## Status of Pennsylvania's Rainy Day Fund

*Through disciplined budget administration, the Rendell Administration has been able to increase the balance in the Rainy Day Fund from \$70 million in 2002-03 to more than \$700 million today, a more than ten-fold increase.*



## 2008-09 Budget Highlights

*The \$28.3 billion General Fund 2008-09 budget was passed by the General Assembly and signed by the Governor on July 4, 2008.*

- The 2008-09 enacted General Fund budget is \$28.3 billion, an increase of \$1.1 billion, or 3.98 percent, over 2007-08. It is \$72.4 million less than the Governor's proposed budget.
- The 2008-09 budget has no tax increases.
- More than 32 percent of the \$1.1 billion increase in the General Fund budget – or \$347.4 million – is for education.
- The 2008-09 General Fund budget increases spending by just 1.3 percent in all areas other than education, public welfare, corrections and probation/parole, while improving many vital state-funded services.
- Administrative spending is only 1.7 percent higher than it was in 2003.

## Moving Toward Energy Independence

*The 2008-09 budget includes an investment of \$665.9 million in alternative and renewable energy deployment, conservation and efficiency, and innovative research and development.*

- ✓ \$180 million for solar energy
- ✓ \$165 million to encourage alternative energy projects
- ✓ \$25 million for green buildings
- ✓ \$25 million for pollution control
- ✓ \$40 million for the Low Income Home Energy Assistance Program
- ✓ \$40 million to support new and promising businesses
- ✓ \$25 million for wind and geothermal
- ✓ \$15.9 million for biomass-based diesel fuel production
- ✓ In addition, \$150 million will be available over eight years to help consumers and small businesses weatherize their properties and adopt conservation tools and to offer tax credits to businesses developing and building alternative energy projects.

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## Infrastructure Initiative

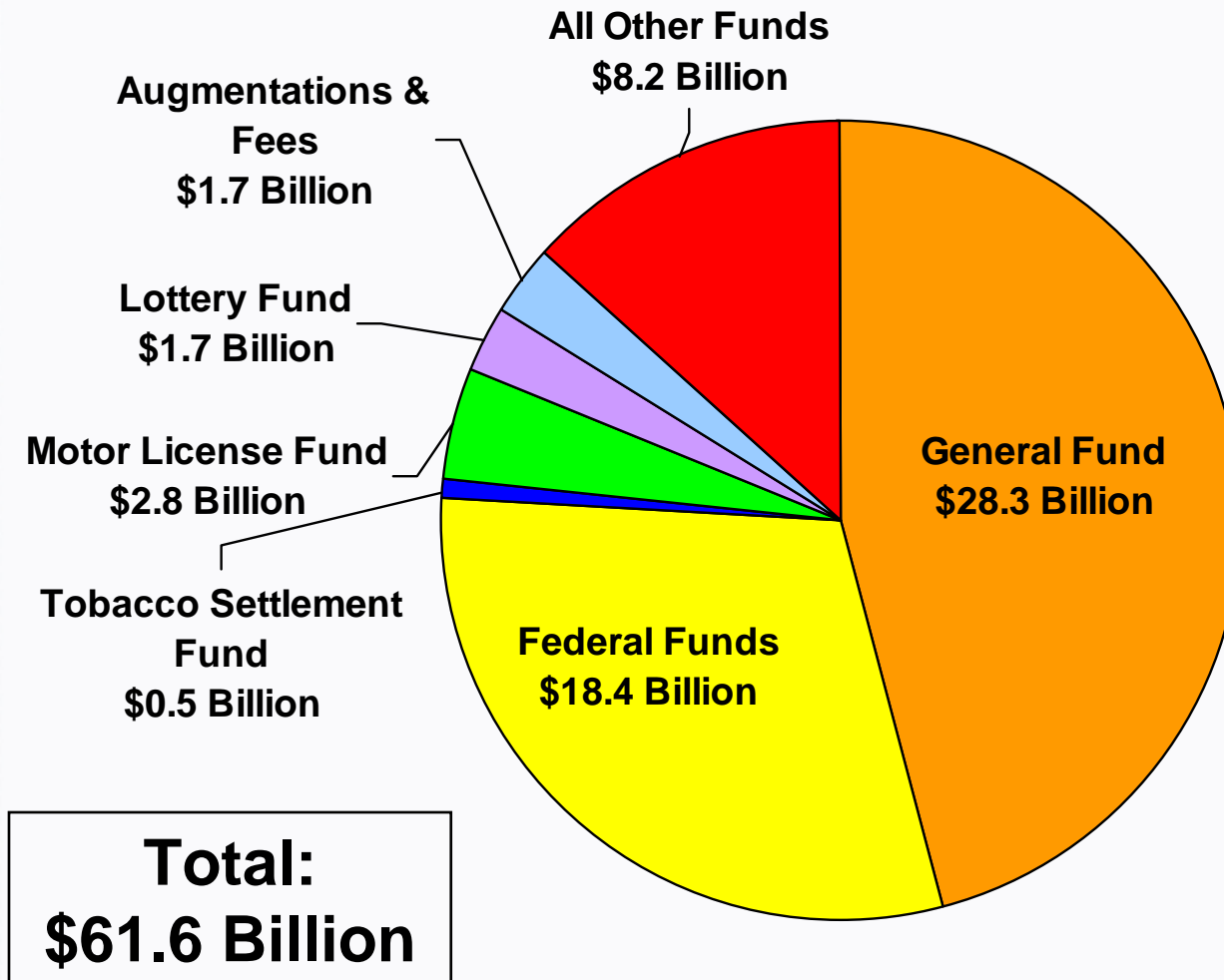
*The 2008-09 budget includes nearly \$2 billion for new infrastructure investments, including repairing and upgrading bridges, water and sewer infrastructure, high-hazard dams, and rail and aviation facilities. These improvements will address problems that were decades in the making and will put thousands of Pennsylvanians to work.*

- ✓ Combined federal and state funding will allow PennDOT to start repairs on 411 bridges this year
- ✓ Including \$350 million in new bond funds to repair the 411 bridges, the budget has \$1.7 billion for the Rebuild Pennsylvania initiative to repair and rebuild structurally deficient bridges across the commonwealth
- ✓ \$800 million to begin rebuilding water and sewer infrastructure and upgrading unsafe dams
- ✓ \$400 million ballot initiative proposed for PENNVEST
- ✓ Redevelopment Assistance Capital Program spending authorization increased by \$800 million to fund community and economic development projects statewide

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## 2008-09 Total Operating Budget



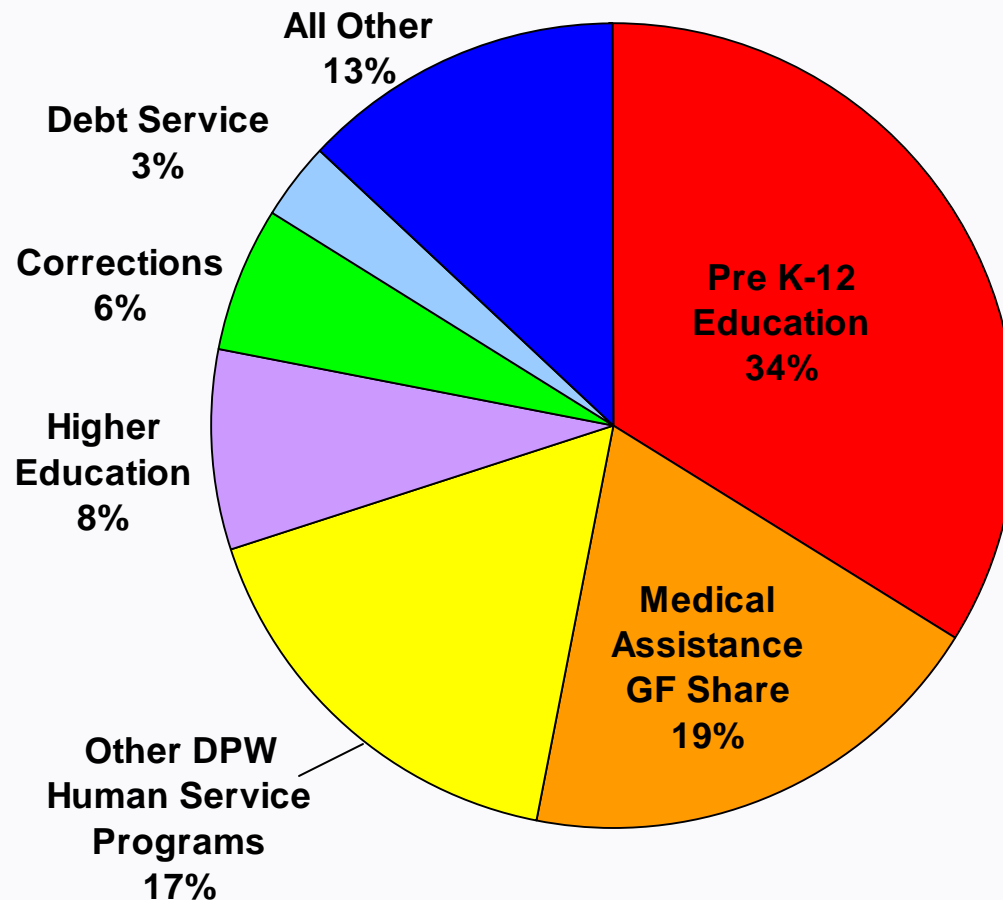
*The total 2008-09 operating budget, including all commonwealth funds, is \$61.6 billion. The General Fund represents 46 percent of this amount.*

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## 2008-09 General Fund Expenditures

*The 2008-09 enacted General Fund budget is \$28.3 billion, an increase of \$1.1 billion, or 3.98 percent, over 2007-08.*



*Spending on Education, Medical Assistance, other Department of Public Welfare programs, Corrections and Debt Service comprises 87 percent of total General Fund expenditures.*

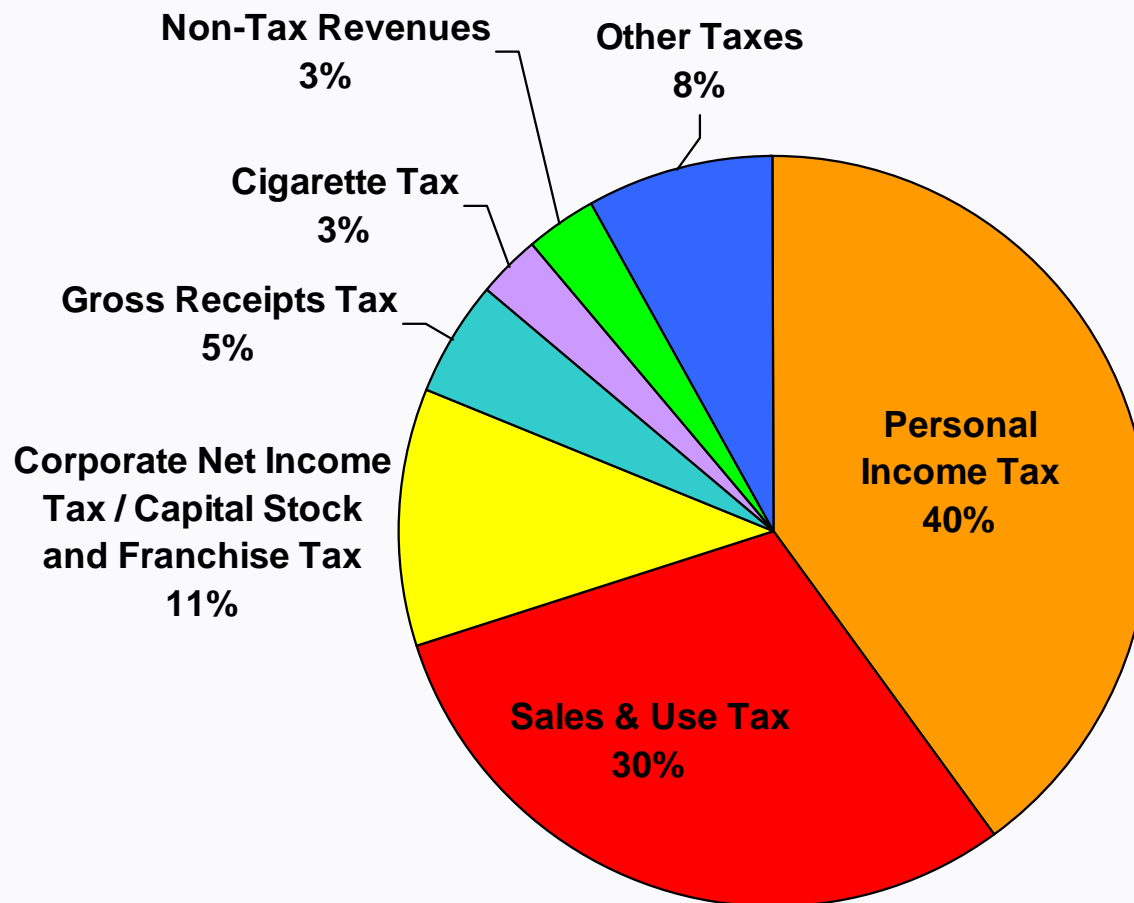
**Total GF Expenditures:  
\$28.3 Billion**



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## 2008-09 General Fund Revenue Sources



*More than two-thirds (70 percent) of General Fund revenues are derived from the Personal Income Tax and the Sales & Use Tax.*

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## Motor License Fund

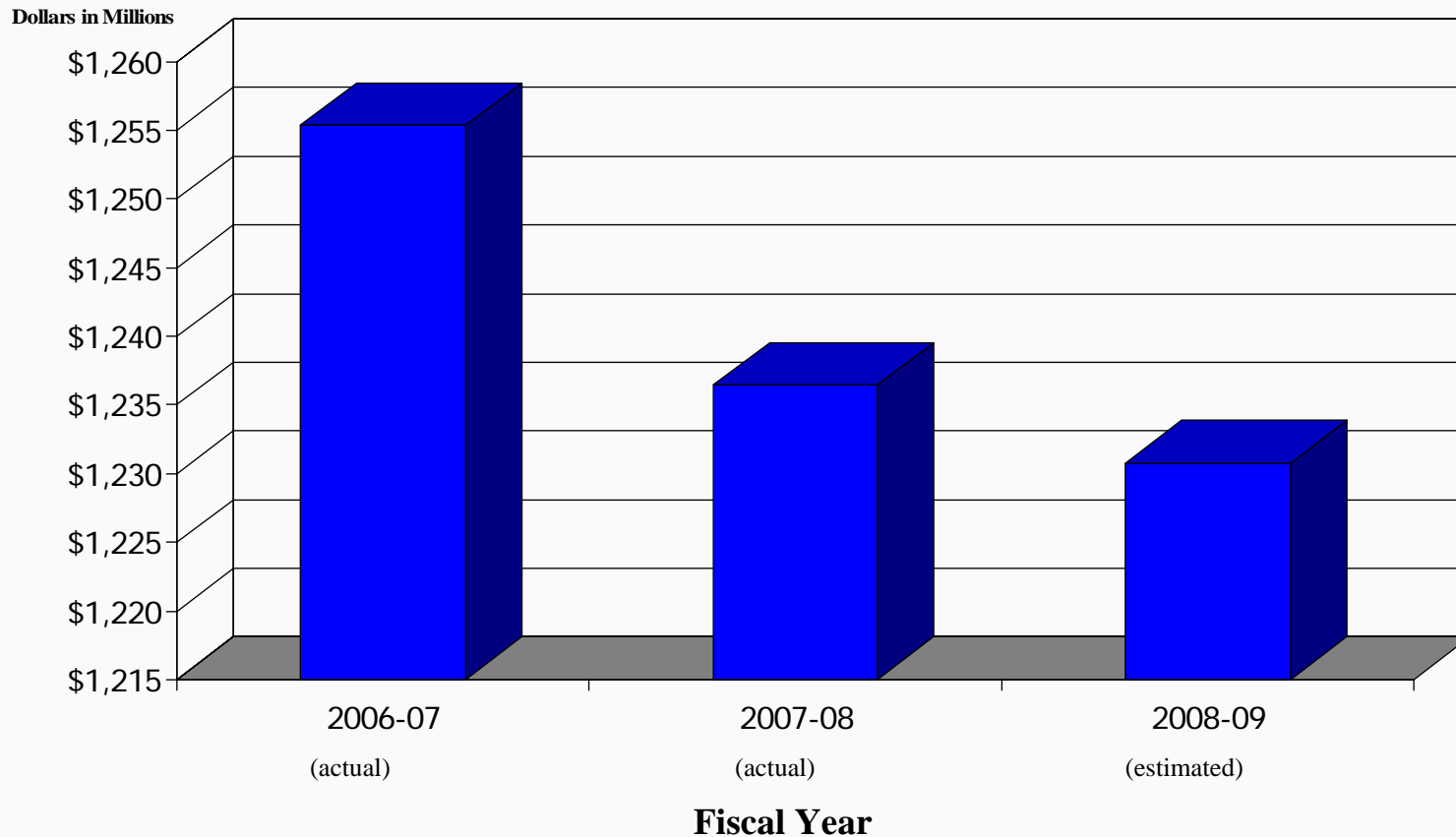
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## Revenue Decline in Liquid Fuels Taxes

*Due to rising gas prices, revenue to the Motor License Fund from the Liquid Fuels Tax has decreased in recent years.*

### Liquid Fuels Tax Revenue



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## Selected 2008-09 Motor License Fund Spending Cuts

*The 2008-09 enacted budget made numerous cuts to the amounts the Governor recommended in his February budget.*

<u>Department</u>	<u>Appropriation</u>	<u>Dollars</u> <u>(in millions)</u>
Transportation	<i>Highway Systems Technology</i>	- \$7
	<i>Highway Capital Projects</i>	- \$5
	<i>Highway &amp; Safety Improvements</i>	- \$15
	<i>Security Walls Pilot Program</i>	- \$5
	<i>Reinvestment - Facilities</i>	- \$2
State Police	<i>General Government Operations</i>	- \$11.8
	<i>Other State Police appropriations</i>	- \$0.4

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## 2008-09 Enacted Motor License Fund Budget

Dollars in Millions

	<u>2007-08</u> Actual	<u>2008-09</u> Enacted
Beginning Balance .....	\$97	\$111
Receipts .....	2,668	2,732
Prior-Year Lapses .....	97	
Funds Available .....	<hr/> \$2,862	<hr/> \$2,843
Expenditures .....	- 2,804	- 2,828
Current-Year Lapses .....	53	
Total Expenditures .....	<hr/> - \$2,751	<hr/> - \$2,828
Ending Balance .....	<hr/> <hr/> \$111	<hr/> <hr/> \$15

## Economic Overview 2008-09

*Recent headlines highlight the deteriorating global economic conditions. Due to the collapse of the credit markets and rising commodity prices, economic conditions have worsened nationwide.*

### ***Global Economic Picture Darkens - World Economy Shows New Strain***

*Wall Street Journal, August 15, 2008*

### ***Drivers Spent More on Fuel Than Cars for First Time Since 1982***

*Bloomberg, August 15, 2008*

### ***Foreclosure Filings Rise in July as Credit Woes Continue***

*Wall Street Journal, August 14, 2008*

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## 2008-09 General Fund Revenues

*Revenues were \$117 million under estimate,  
but there were a few positive signs in August.*

(dollars in thousands)

<b>REVENUE SOURCE:</b>	<b>August 2007</b>	<b>August 2008</b>	<b>Dollar Change</b>	<b>Percent Change</b>
Sales Tax – Motor Vehicle Sales	\$ 111,256	\$ 84,058	\$ (27,198)	-24.4%
Sales Tax – Non-Motor Vehicles	582,453	608,947	26,494	4.5%
Personal Income Tax	651,417	737,188	85,771	13.2%
Business/Corporate Taxes	61,203	48,846	(12,357)	-20.2%

## Budgetary Freeze

*On September 16<sup>th</sup> the Governor directed commonwealth agencies to freeze portions of their discretionary budgets in order to put \$200 million of General Funds and \$40 million of Motor License Funds in budgetary reserve. The announcement also included a hiring freeze and elimination of out-of-state travel for commonwealth employees.*

- 4.25 percent across-the-board cuts
- 2 percent cuts for public safety agencies
- Specific cuts for agencies with nondiscretionary programs



## Economic Downturn

- The financial markets are in historic turmoil due to write-offs of sub-prime mortgage-backed securities and related credit failures
  - Major financial companies such as Bear Stearns, Merrill Lynch, Washington Mutual, Wachovia and Lehman Brothers are gone
  - On October 3, President Bush signed into law an unprecedented \$700 billion federal bailout approved by Congress after a tumultuous week
  - Economic uncertainty and anxiety remain high

### THE WALL STREET JOURNAL

SEPTEMBER 18, 2008

#### **Worst Crisis Since '30s, With No End Yet in Sight**

**By JON HILSEN RATH, SERENA NG and DAMIAN PALETTA**

The financial crisis that began 13 months ago has entered a new, far more serious phase...

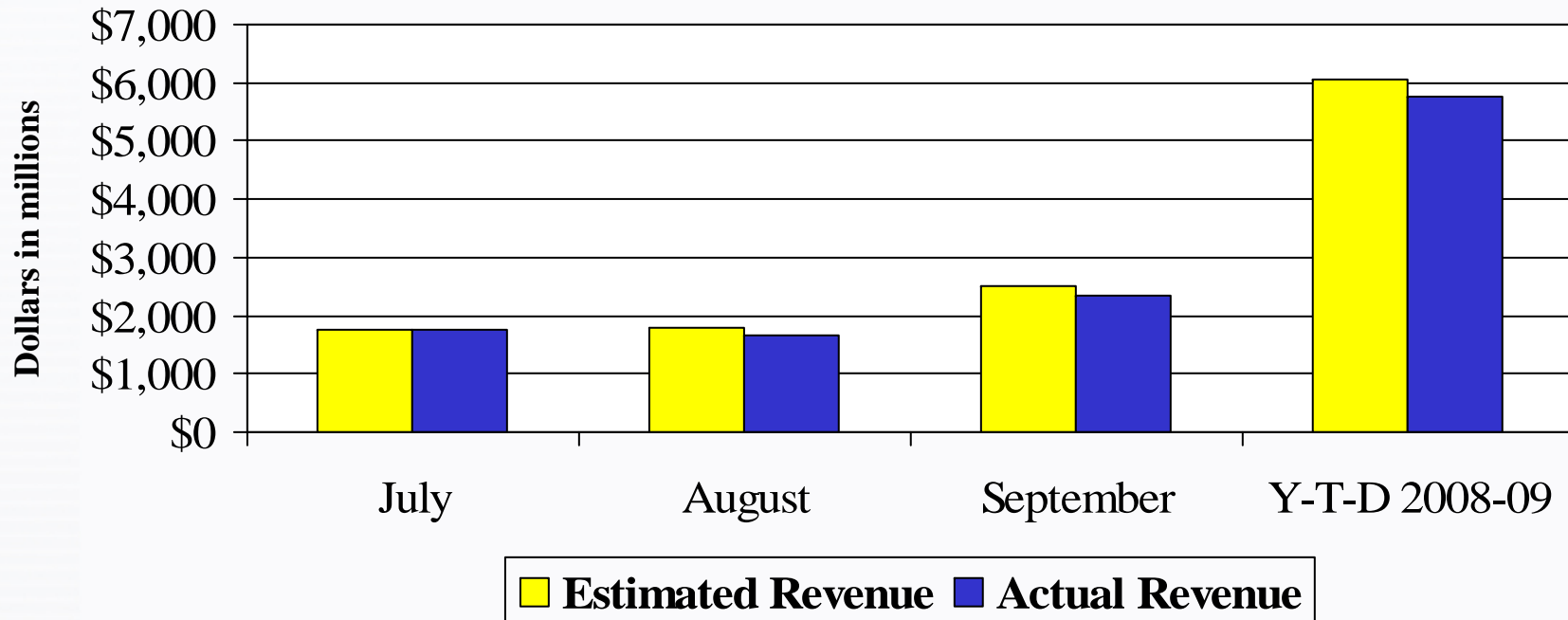
The U.S. financial system resembles a patient in intensive care. The body is trying to fight off a disease that is spreading, and as it does so, the body convulses, settles for a time and then convulses again. The illness seems to be overwhelming the self-healing tendencies of markets. The doctors in charge are resorting to ever-more invasive treatment, and are now experimenting with remedies that have never before been applied.

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## 2008-09 General Fund Revenues *Estimated versus Actual Revenue Collections*

*In the first three months of 2008-09, revenue collections were \$281.4 million, or 4.7 percent, lower than estimated.*



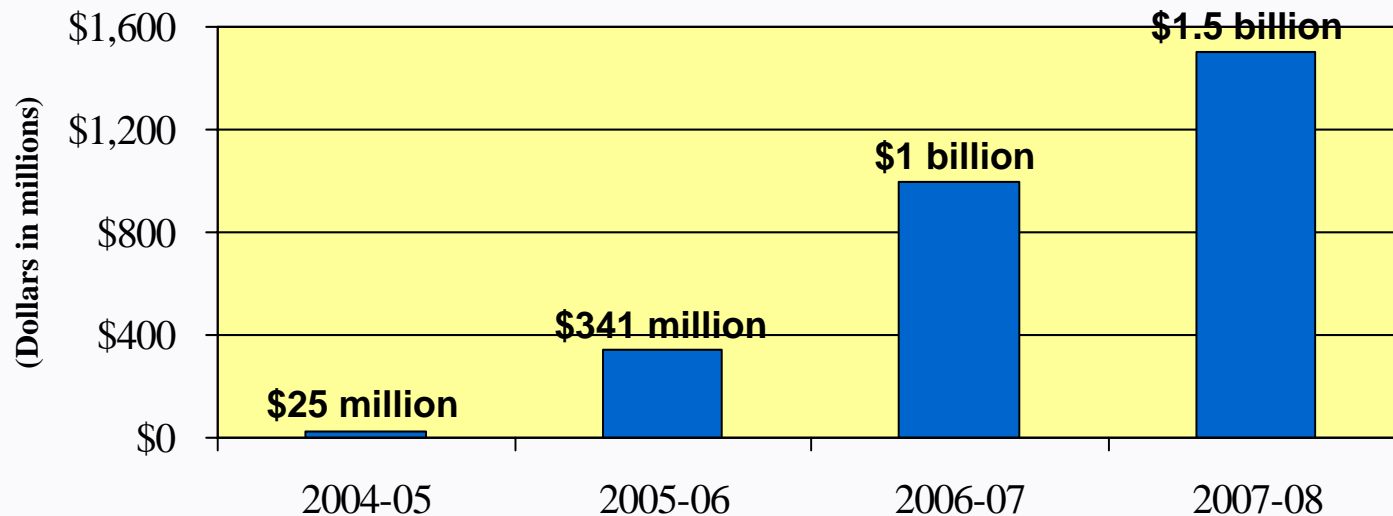
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## Pennsylvania Achieves \$1.5 Billion in Annual Cost-Cutting Management & Productivity Improvements

*Governor Rendell pledged to cut the cost of government and improve the way the commonwealth works. In five years, by developing new business practices and focusing on innovation and efficiency throughout the government, the administration exceeded projections to reach annual recurring savings of at least \$1.5 billion by the end of 2007-08.*

Recurring Annual Reductions



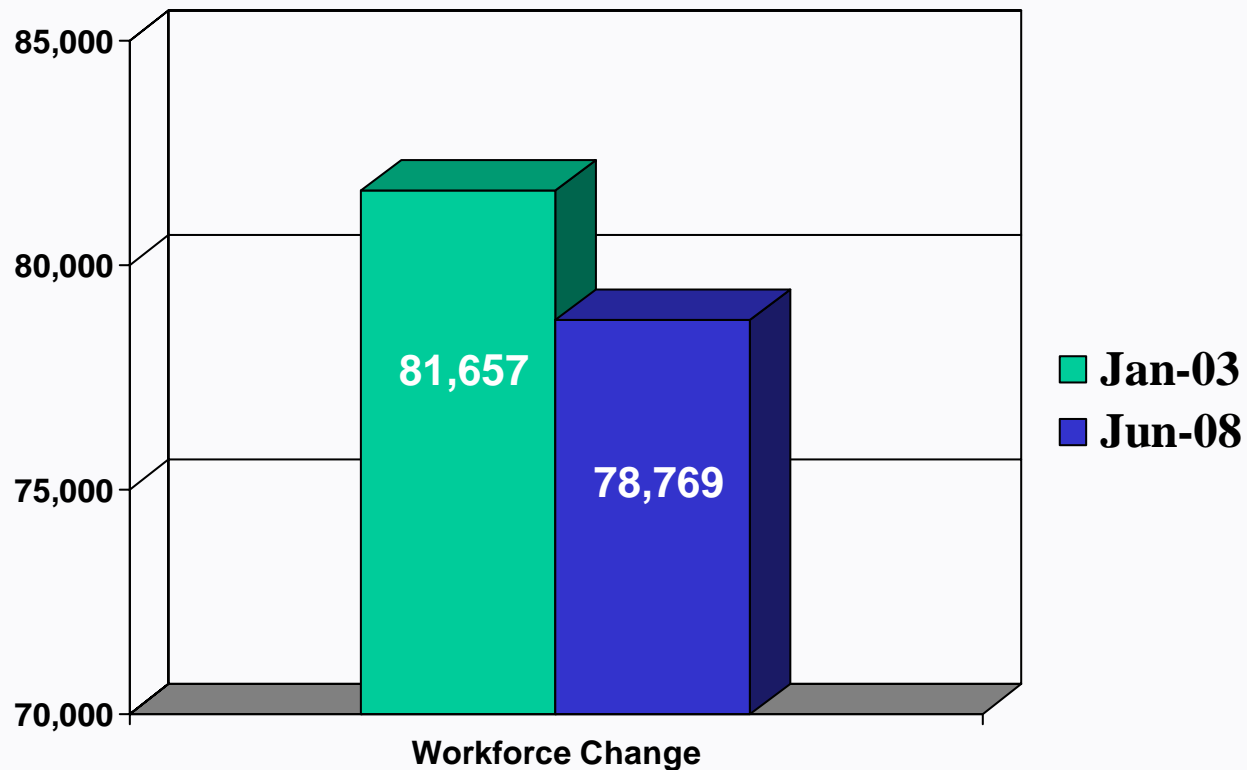
## Recent Management & Productivity Cost-Saving Initiatives

- 2007-08 recurring savings - **\$1.52 billion**
- 2008-09 recurring savings target - **\$1.75 billion**
- Significant projects in progress
  - Data Powerhouse consolidation and contract restructuring will result in **savings of \$13 million** in 2008-09.
  - The Department of General Services' strategic sourcing initiative remains a consistent source of savings, with anticipated **savings of \$313 million** in 2008-09.
  - Changes to the Retired Employees Health Program will save **\$68 million** in 2008-09.
  - The Department of Public Welfare's creation of two separate managed care contracts for federal and state-only recipients will generate **savings of \$61 million** in the upcoming fiscal year.
  - Tightened oversight of PennDOT construction projects will save **\$26 million** in 2008-09.
  - Changes to pharmacy reimbursements and the Department of Aging's preferred-drug list will result in **\$158 million** in federal funding that would otherwise be paid by the commonwealth.

Note: 2008-09 savings are based on estimates provided by the agencies.

## Percentage Change in Filled Complement *2002-03 versus 2007-08*

*Between January of 2003 and June of 2008, commonwealth agencies under the Governor's jurisdiction reduced the commonwealth's filled workforce by 3.5 percent or 2,888 positions.*



## Challenges in 2008-09 and Beyond

- Economic downturn
- Health care cost inflation
- Projected increase in pension costs in 2012-13
- An aging Pennsylvania that requires more costly services
- Pennsylvania's critical infrastructure needs

## Summary

- Pennsylvania has a long history of sound financial management, as evidenced by our double-A credit rating – the second-highest level of credit.
- Governor Rendell has led an effort to improve the way commonwealth government works while cutting unnecessary costs.
- The Governor is taking the steps necessary to maintain a balanced budget in this period of economic uncertainty.