

COMMONWEALTH OF PENNSYLVANIA



2009-10

BUDGET IN BRIEF

Edward G. Rendell
Governor





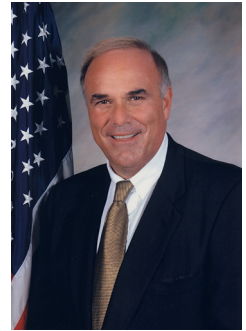
COMMONWEALTH OF PENNSYLVANIA
OFFICE OF THE GOVERNOR
HARRISBURG

THE GOVERNOR

February 4, 2009

To the People of Pennsylvania:

Over the past six years, we have worked together to make Pennsylvania stronger by growing our economy, improving our schools, revitalizing our communities and restoring our environment. Now we are faced with a national recession the likes of which have not been seen since the 1930s. While the economic challenges we face are considerable and require painful decisions, the only prudent course of action is to protect our progress while making the essential investments that will position the commonwealth for our recovery.



The nation's economic crisis is having a terrible impact on many Pennsylvanians, and indeed our state budget reflects the fact that the United States economy has contracted. Yet the fact is that Pennsylvania has not been hurt as badly as many other states, and our relative standing is due in large measure to the decisions that we have made since 2003: We established a solid foundation of fiscal responsibility, we improved government efficiency to cut waste and save more than \$1.5 billion a year, and we made wise investments that have made Pennsylvania a better place to grow up, live and do business.

In just the past year, we established Pennsylvania as a national leader in the emerging "green" economy, enacted a blueprint for providing adequate resources in all of our classrooms, and set in motion more than \$1.5 billion worth of job-creating improvements in critical infrastructure.

We cannot afford to lose that momentum now.

The 2009-10 budget that I share with you today is both a reflection of our economically distressing times and a plan for getting back to prosperity. It avoids any increases in broad-based taxes and includes many difficult cuts to programs and services that I care about deeply, for the simple reason that there is absolutely no alternative.

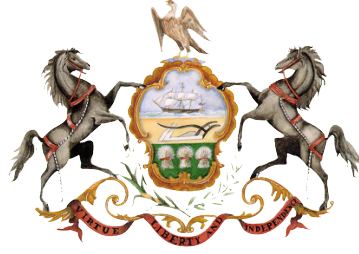
Even as it establishes fiscal stability, this budget moves Pennsylvania forward – and that is essential. We must enact our own economic stimulus to help companies create new jobs. We must continue to invest in increasing student achievement in our schools. We must make college more affordable to produce the next generation of leaders in the workforce. And we must provide more working adults with access to health insurance at a reasonable cost.

As the recession takes its toll on Pennsylvania families, the cost of doing nothing far exceeds the price of these vital investments. Together, we can and must meet our economic challenges while improving the quality of life for our citizens and setting our sights on our long-term vitality.

Pursuant to Article VIII, Section 12 of the Constitution of Pennsylvania, and Section 613 of the Administrative Code of 1929 (71 P.S. Section 233), I am transmitting to your representatives in the General Assembly my proposed budget for Fiscal Year 2009-10.

Sincerely,

Edward G. Rendell



Commonwealth of Pennsylvania

2009-10 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:

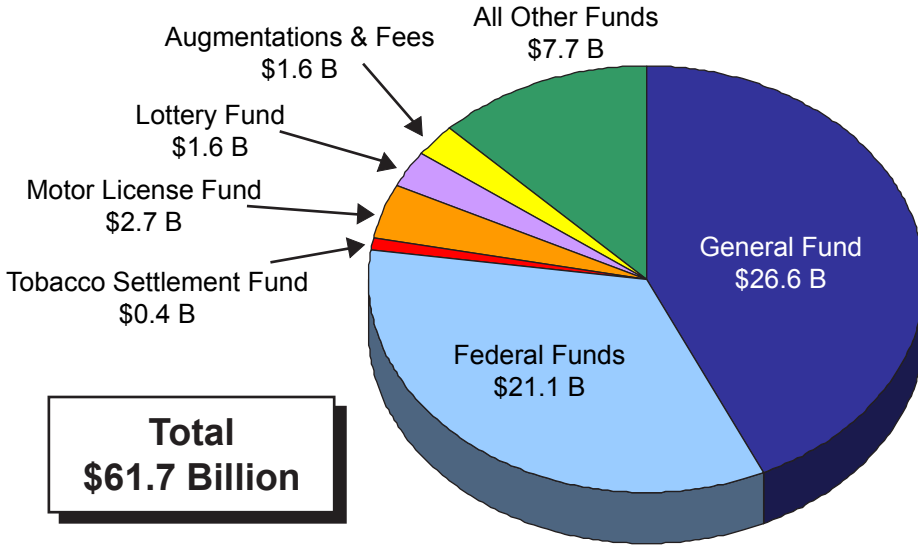
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–click on Current and Proposed Commonwealth Budgets–

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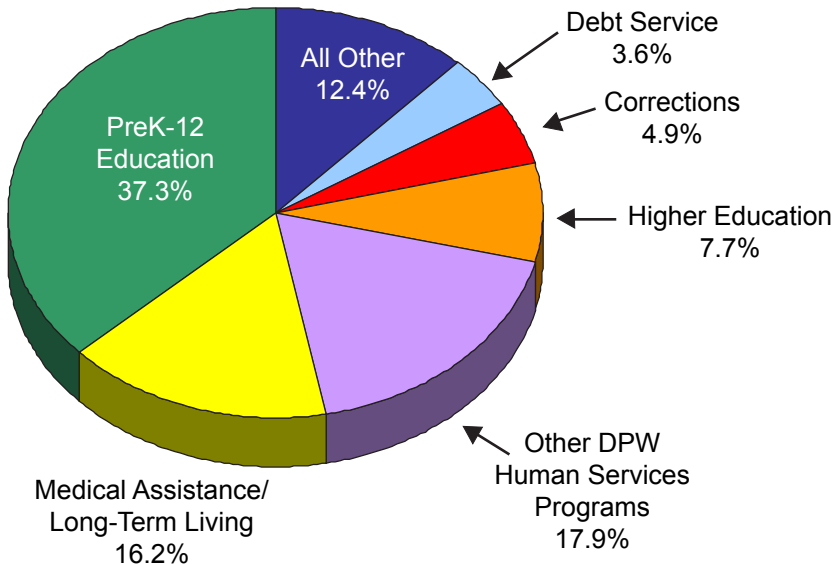
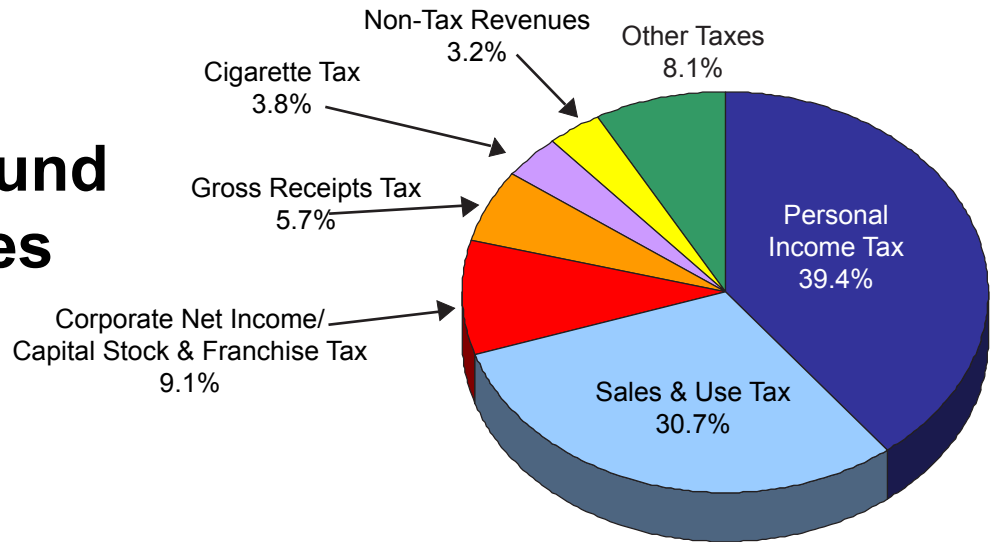
2009-10 Budget Overview



Total Operating Budget

The total Fiscal Year 2009-10 operating budget, including all commonwealth funds, is \$61.7 billion. The General Fund represents 43 percent of this amount.

General Fund Revenues



General Fund Expenditures

\$26.6 Billion

Shaping the 2009-10 Budget

The economy officially entered a recession in December 2007, but Pennsylvania began to feel the effects of the slowing national economy only in late spring of 2008. As the economy worsened and revenues began to fall short of estimates early in the 2008-09 fiscal year, Governor Rendell took decisive action by implementing a general hiring freeze, restricting out-of-state travel, banning the purchase of new vehicles, freezing cabinet and non-union salaries, and halting nearly \$500 million of planned spending.

The 2008-09 budget shortfall is now expected to reach \$2.3 billion by the end of the fiscal year. Federal fiscal relief will provide a major source of revenue to keep the commonwealth's budget in balance. Options to balance the current-year budget were selected with the goal of retaining some funding in the commonwealth's Rainy Day Fund for use in future years.

Based on current projections, 2009-10 revenues are expected to be the same as 2008-09 revenues – an illustration of the impact the economic downturn has had on state finances. The 2009-10 budget assumes that more than \$2.4 billion in federal fiscal relief will be used to prevent even deeper cuts throughout the budget and continue to provide critical funding for programs millions of Pennsylvanians rely on every day.

States are fortunate to receive federal fiscal relief during this period of great economic uncertainty, but that relief will be available only for a limited period of time. While it will be difficult, Pennsylvania must also take action to ensure its budget will remain in balance when federal fiscal relief is no longer available. To that end, the 2009-10 budget proposes to reduce or eliminate funding in 447 appropriations, lowering spending by nearly \$1 billion.

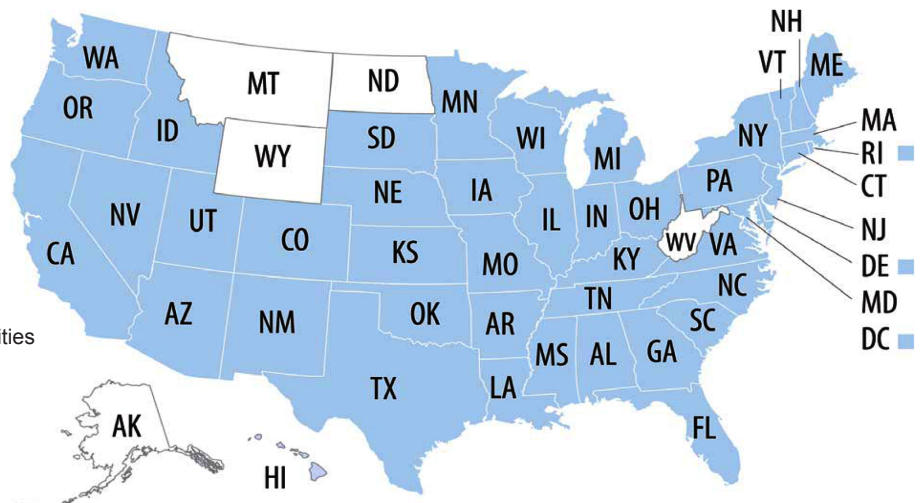
At the same time, Pennsylvania must continue to protect the progress that has been made over the last six years and prepare for recovery. To achieve this, the 2009-10 budget is built to:

- put more Pennsylvanians to work and keep those who are working in their jobs;
- relieve the impact of the recession on hard-working families; and
- keep the cost of state government down and manageable in the long run.

The following pages provide additional detail on Pennsylvania's comprehensive and prudent plan to weather the national economic storm while continuing to make critical investments so Pennsylvania can emerge from this national economic slowdown stronger and even more competitive.

Plan to Balance the 2008-09 Budget (dollars in millions)	
Potential Shortfall	\$ 2,300
Federal Fiscal Relief	\$ 1,083
Current Year Lapses (Including Budgetary Freezes)	\$ 521
Rainy Day Fund	\$ 250
Legislative Lapses	\$ 175
Transfer of Marcellus Shale Revenues	\$ 174
Prior Year Lapses	\$ 91
Current Year Lapses (Independent Agencies)	\$ 36

45 States Face Budget Shortfalls*



Source: Center on Budget and Policy Priorities
"State Budget Troubles Worsen"
January 14, 2009

* Includes states with shortfalls in fiscal year 2009 or projected shortfalls for fiscal year 2010

2009-10 Budget Highlights

- The 2009-10 budget is built to:
 - put more Pennsylvanians to work and keep those who are working in their jobs;
 - relieve the impact of the recession on hard-working families; and
 - keep the cost of state government down and manageable in the long run.
- The 2009-10 General Fund budget does not propose any broad-based tax increases.
- The 2009-10 General Fund budget is \$26.6 billion – a decrease of \$64.5 million, or 0.2 percent less than 2008-09, after accounting for the use of anticipated federal fiscal relief funds of nearly \$1.1 billion in 2008-09 and \$2.4 billion in 2009-10, which will offset state costs.
- In light of the national recession and the forecast for continued economic contraction at the outset of 2009, base General Fund revenues are not expected to grow over the current fiscal year.
- The 2009-10 budget proposes to reduce or eliminate funding for programs in nearly every commonwealth agency. This budget reduces funding for 346 programs and eliminates funding for 101 programs, lowering spending by nearly \$1 billion.
- The 2009-10 budget continues to re-invest savings realized through innovation and increased efficiency. By eliminating waste and improving government operations, the commonwealth expects to achieve \$1.75 billion in annual recurring savings in the 2008-09 fiscal year.
- The 2009-10 budget includes a reduction of 2,995 positions in the commonwealth's current authorized complement, for a total reduction of 4,767 positions since January 2003.
- In the 2009-10 General Fund budget, \$12.1 billion, or 45 percent, is for Education.
- The 2009-10 General Fund budget reduces spending by 8.8 percent in all areas other than Education, Public Welfare, Corrections, and Probation and Parole.
- The 2009-10 budget proposes to expand the adultBasic insurance program to provide affordable basic healthcare for an additional 50,000 uninsured adults.

Protecting Our Progress

Property Tax Relief – Provide nearly \$787 million in property tax relief in 2009.

Governor's Rebuild Pennsylvania Infrastructure Initiative – Invest more than \$537 million in our public infrastructure, including bridges, rail freight lines, small airports, high-hazard dams and flood-related projects, in addition to \$1.9 billion in base Motor License Fund bridge and highway funding.

Attracting More Businesses and Job Growth to Pennsylvania – Invest \$100 million to get Pennsylvania sites shovel-ready for use by businesses moving into the commonwealth or expanding their operations. Includes \$60 million to reinvigorate the successful Business in Our Sites Program that provides loans and grants for site acquisition and development for future use by businesses and \$40 million for water and wastewater infrastructure projects related to economic development.

Responding to Companies' Needs for Working Capital – Reallocate \$100 million in under-utilized Second Stage Loan Program resources that provides working capital to manufacturing, biotech and technology-related companies that are 2 to 7 years old.

Infrastructure Facilities Improvement Grant Program – Every \$1 million of funding for this program creates approximately 2,000 new jobs, but the current pipeline of eligible projects is far greater than the supply of available resources. The 2009-10 budget includes a \$10 million initiative for new infrastructure and facility improvement projects for this valuable engine of economic growth.

Energy Independence Strategy – Continue to invest \$650 million to help Pennsylvania companies and consumers lower their energy costs, reduce their dependence on foreign oil and develop renewable energy industries.

2009-10 Budget Highlights

Education – Investing in Our Children, Preparing for the Future

PreK-12 Education – More than \$9.9 billion in total funding for basic education, a \$262.5 million, or 2.7 percent, increase.

Basic Education Subsidy - \$5.5 billion, a \$300 million, or 5.7 percent, increase to support PreK-12 education and to continue phasing in a research-based funding approach to assist districts to advance student achievement.

Accountability Block Grant – \$271.4 million to fund proven educational programs. Includes earmarked funds for quality pre-kindergarten and full-day kindergarten.

Education Assistance Program - \$65.1 million to fund tutoring for 172,000 struggling students in 175 school districts.

Special Education – \$1.05 billion in total funding, a \$20.5 million, or 2 percent, increase, including federal fiscal relief directed towards special education.

Project 720 – \$10.7 million to transform Pennsylvania high schools by increasing the rigor of academic programs. More than 160 high schools are already participating.

Pennsylvania Pre-K Counts – \$95.1 million for pre-kindergarten, an \$8.6 million, or 10 percent, increase.

Science: It's Elementary – \$13.6 million to help at least 65,000 students become active science explorers.

Dual Enrollment – \$10 million to help students earn college credit. High school students are taking nearly 25,341 college courses this year as a result of our current investment of \$10 million.

Classrooms for the Future – \$22 million to improve the way teachers teach and students learn by putting a laptop on each student's desk for more effective learning.

Higher Education Programs – More than \$2 billion in total, including \$519 million for the State System of Higher Education and \$287.6 million, a \$6.8 million, or 2.4 percent, increase for community colleges.

Grants to Students – \$45 million increase in Pennsylvania Higher Education Assistance Agency tuition grants, including \$10 million to provide grants to nearly 10,000 additional community college students.

Preserving the Safety Net – Helping Pennsylvanians in Need

adultBasic Expansion – \$251.7 million in state, federal and other funds to provide an affordable basic health care plan for up to 50,000 additional uninsured adults.

Prescription for Pennsylvania – \$14.5 million in state and federal funds to implement a series of initiatives to improve the coordination and quality of health care.

Cover All Kids – \$407 million in state and federal funds to provide affordable health care for 206,836 children, an increase of 13 percent.

Expanding Services for the Disabled – \$429.5 million in state and federal funds, an increase of \$33.9 million, or 9 percent, including funds to enable 1,600 more individuals to receive home and community-based care.

Autism – \$56.6 million in state and federal funds, an increase of \$10.2 million, or 22 percent, to provide home and community-based services for adults with autism.

Child Care – \$793.1 million in state and federal funds, which includes funds for an additional 6,477 children.

Early Intervention – \$323.8 million in state funds, an increase of \$20 million, or 7 percent, to serve 2,980 additional developmentally delayed children.

PACE/PACENET – \$251.8 million for the state pharmaceutical program. An additional 15,000 seniors will be served by PACE, for a total of 375,000 seniors served.

Community-Based Mental Retardation Services – \$1.9 billion in state and federal funds, an increase of \$102.3 million, or 6 percent, including funds to provide home and community-based services to 793 more people.

Long-Term Living – \$3.9 billion in total funds for home and community-based services and nursing facility care. Funding will enable 2,000 additional seniors to remain in their homes as an alternative to nursing facility care.

Making Pennsylvania Safer

Department of Emergency Management and Homeland Security – Creation of a cabinet-level agency to coordinate emergency response efforts.

State Prison Capacity Expansion – \$19.6 million for housing units and cell blocks at existing institutions to add 1,600 additional beds.

Community Corrections – \$11.9 million for an additional 800 community corrections beds.

Probation and Parole – \$2 million for additional parole agents to enhance case-processing capabilities.

State Police – The number of troopers is projected to exceed 4,500 in 2009-10.

Federal Fiscal Relief

The nation is currently facing the most severe economic crisis in decades. The financial system is in turmoil, credit for private investment and consumer purchases has been frozen, and an extended period of employment growth has come to an abrupt end, replaced by dramatic job losses across all sectors of the economy.

Congress is deliberating the American Recovery and Reinvestment Act of 2009. Passage of this comprehensive economic stimulus measure will mean a significant injection of federal funds for key state and local services in Pennsylvania.

The 2009-10 budget anticipates at least two major new funding streams from this fiscal stimulus: budget stabilization funds for the states to prevent cuts in education, public safety and other critical government programs; and increases in the federal government's matching funds for the Medical Assistance program. The budget also incorporates two additional anticipated federal funding increases for special education and child care.

State Fiscal Stabilization: Education and Public Safety

As a key component of the American Recovery and Reinvestment Act, \$79 billion will be made available for states and school districts to stabilize budgets and maintain critical programs. Pennsylvania currently anticipates a total allocation of \$1.26 billion in federal funds in 2009-10 and an additional \$1.26 billion in 2010-11.

Approximately 61 percent of Pennsylvania's total allocation, or \$771 million per year, must be used to support elementary, secondary and higher education.

The remaining 39 percent, or \$493 million per year, will be used to offset state funding in the Department of Corrections. These federal funds will help prevent significant cuts in state funding for educational institutions, local government programs and other important services. The commonwealth's allocation of \$986 million over two years from this second funding stream is included in the 2009-10 budget.

Medicaid Funding

The federal government and the states share the cost of Medicaid – the joint state-federal health insurance program for low-income people and others in need. In previous times of economic hardship, the federal government increased its share of the costs, recognizing that vulnerable Americans needed more assistance. To offset cuts to health benefits or eligibility in this economic downturn, the stimulus measure includes a separate allocation of \$87 billion for state Medicaid programs.

The federal government currently pays approximately 54 percent of Pennsylvania's Medical Assistance costs; this share is expected to increase to between 62 percent and 66 percent, depending on state unemployment rates over the next two years. Federal Medical Assistance Percentage increases are also expected to provide additional support for Title IV-E foster care and adoption assistance programs. These enhancements are projected to increase federal reimbursements by approximately \$4 billion over the 27-month adjustment period between October 2008 and December 2010.

Special Education

The federal stimulus measure is expected to provide significant additional grant funds for states under the Individuals with Disabilities Education Act to prevent cuts to other critical education programs and services. The 2009-10 budget includes approximately \$20.5 million in federal funds from this special education stimulus measure.

Child Care

Additional federal funds are expected to be made available to the states under the Child Care Development Block Grant to provide child care services for children in low-income families while their parents go to work. The 2009-10 budget provides \$5.7 million in federal funds for child care services.

Federal Fiscal Relief in the 2009-10 Executive Budget	Dollar Amounts in Thousands		
	2008-09 Estimated	2009-10 Estimated	2010-11 Estimated
State Fiscal Stabilization For Department of Corrections (39% of Pennsylvania's allocation from State Fiscal Stabilization Fund)		\$493,000	\$493,000
Medical Assistance Aid Temporary increase in the Federal Medical Assistance Percentage (FMAP)	\$1,083,000	\$1,917,000	\$1,000,000
Special Education Increase in federal share of special education costs (IDEA grants)		\$20,500	\$20,500
Child Care Services Additional child care support for low-income working families		\$5,700	\$5,700
TOTAL	\$1,083,000	\$2,436,200	\$1,519,200

Making Government Work Smarter

One of Governor Rendell's highest priorities has been to significantly improve the quality of state services provided to Pennsylvania's residents while restraining the growth of administrative spending by state government. This approach allows the commonwealth to invest more resources in programs that directly benefit our citizens.

During his first term, Governor Rendell made good on his pledge to cut the cost of government by achieving annual recurring savings of \$1 billion. Building on this milestone, the Governor has instructed commonwealth agencies and the Governor's Office of Strategic Services to save an additional \$500 million annually over the next four years. In 2008-09 it is estimated the annual recurring savings will be \$1.75 billion.



The Rendell administration's response to the fallout from the global financial crisis has been swift and decisive. As soon as the state's revenues exhibited signs of weakness, the Governor took action to:

- Cut spending by \$500 million;
- Order a hiring freeze, leaving more than 4,500 positions unfilled;
- Freeze wages for 13,600 managers and other non-union employees, saving \$13.4 million;
- Prohibit the purchase of new vehicles, saving an estimated \$40 million;
- Restrict out-of-state travel; and
- Reduce state vehicle fleet by 1,000.

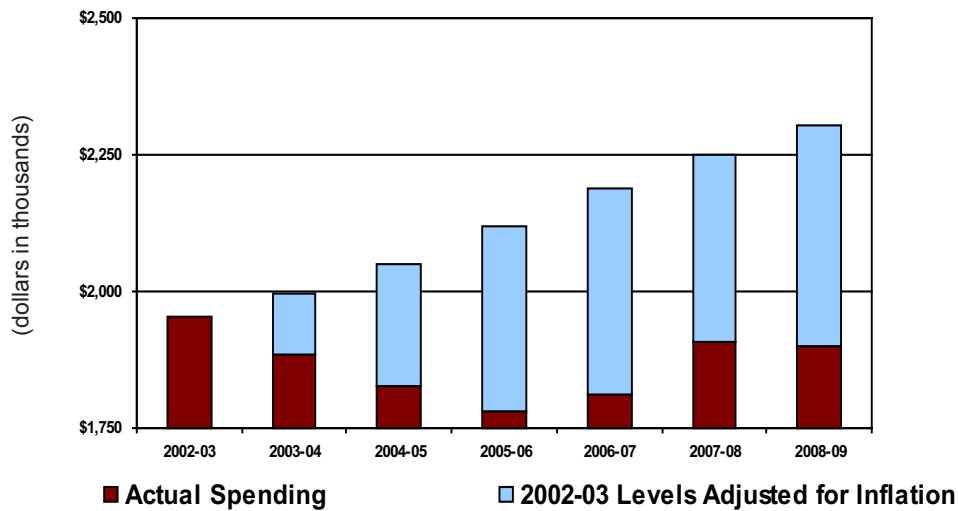
As revenues continue to decline, agencies are being forced to make increasingly difficult choices regarding their needs and priorities. To help these agencies develop creative and innovative solutions to the complex problems they face, Governor Rendell established the Office of Strategic Services to coordinate enterprise-wide initiatives to reduce

costs, identify new sources of revenues and enhance service levels. Formed from the merger of the Office of Management and Productivity and the Bureau of Management Consulting, this office has been tasked with taking a holistic view of the challenges faced by Pennsylvania state government and resolving issues.

The role and responsibilities of the Office of Strategic Services vary widely from one project to the next. Office staff have drafted solicitations, evaluated bids, negotiated contracts and analyzed a wide range of financial and operational data in order to help agencies drive down costs. They have also been called upon to draft new policies when necessary. Office of Strategic Services personnel have also had a crucial role in redesigning and streamlining processes to improve efficiency and enhance customer service. Through the efforts of the Office of Strategic Services and thousands of other dedicated state employees, the Governor was able to honor the commitment he made in 2003 – to dramatically reduce the cost of government by achieving \$1 billion in annual recurring savings during his first term.

Making Government Work Smarter

Inflation-Adjusted Administrative Spending versus Actual Spending



Having achieved this goal, the Governor challenged his cabinet in early 2007 to identify an additional \$500 million worth of efficiencies during his final four years in office. The Rendell administration responded by finding the necessary savings in 2007 and 2008 and is now on track to significantly exceed the revised target by the end of the Governor's second term. These efforts are helping to ensure that the state's revenues can be targeted to where they are most needed – to programs that provide educational opportunities or that benefit the commonwealth's residents most in need of assistance.

Negotiating Stronger Contracts

In the past, state agencies made uncoordinated purchasing decisions, wasting millions of taxpayer dollars. Governor Rendell's Strategic Sourcing Initiative has coordinated commonwealth purchasing, enabling agencies to jointly leverage their purchasing power in order to negotiate better prices and contract terms. This program is not only generating savings, but has also resulted in a significant increase in opportunities for Pennsylvania's minority and women-owned businesses. Furthermore, many of the contracts that have arisen from this initiative are performance-based, which means that in addition to saving money, they force vendors to meet quality or timeliness standards. The Rendell administration's procurement reforms are saving money by:

- Helping agencies buy together through the Strategic Sourcing Initiative (\$271.8 million);
- Striking a three-year licensing deal that integrates and streamlines the sign-on process for the employees, residents and business partners who use the state's Web site and computer systems (\$15.3 million); and
- Replacing expensive contractors with state employees who possess the same essential skills (\$1.7 million).

Improving Processes and Streamlining Operations

As revenues decline, it becomes increasingly important to ensure that every available cent be devoted to critical programs focused on residents, as opposed to the administrative aspects of government. By implementing common-sense initiatives and putting funds in budgetary reserve, commonwealth agencies will spend the same amount on administrative expenses in 2009-10 as they did in 2002-03. Had administrative expenses increased at the rate of inflation, taxpayers would pay 18 percent more in 2009-10 for operating state government.

Successful efforts to improve processes include:

- Overhauling our Retired Employees Health Program (\$94 million);
- Issuing Supplemental Security Income checks by state employees (\$30.5 million); and
- Avoiding change orders on major construction projects (\$13.3 million).

Implementing Technological Solutions

Although many of the projects launched through the Governor's management and productivity initiative were completed in pursuit of additional cost savings, others were chosen primarily for their ability to improve the customer service experience for those obtaining services from state government. Examples of recent technology projects include:

- Establishing an online portal through which insurance companies can obtain or renew licenses and also submit policy forms and rate filings for the Insurance Department's review and approval. These and other business and consumer-directed enhancements are saving more than \$340,000 per year.

Making Government Work Smarter

- Installing data encryption software on state laptops as part of a comprehensive strategy to protect sensitive information regarding our citizens, employees and contractors. If equipment is lost or stolen, this technology will prevent unauthorized users from accessing the data.
- Enhancing and promoting the use of the Department of Revenue's electronic filing option for Pennsylvanians to submit their personal income tax returns. Electronic filing by taxpayers has increased by 40 percent since 2004, saving \$960,000 in processing costs.

Saving Green

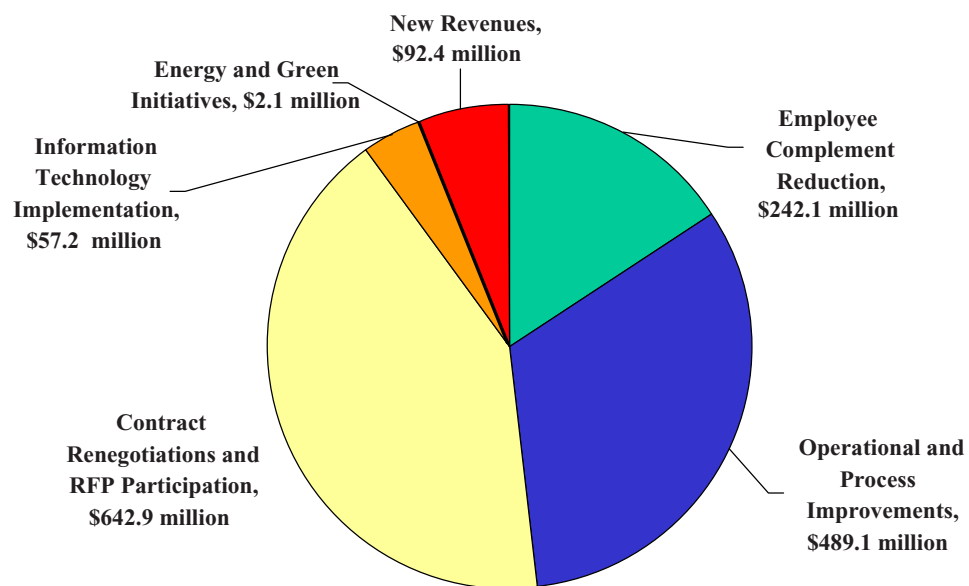
Management initiatives have shown that fiscal and environmental responsibility can go hand-in-hand. Pennsylvania's Procurement Code authorizes state and local governments to enter into guaranteed energy savings agreements, under which contractors make improvements to government facilities (typically lighting and climate control systems), and are paid out of the resulting savings in energy costs over as many as 15 years. The taxpayers are protected, because these agreements are structured in such a way that if the projected savings fail to materialize, the loss will be borne by the contractor. The 45 such projects that are now under way are estimated to yield \$50 million in

net savings over the life of the projects. To save both money and the environment, the Rendell administration is:

- Signing guaranteed energy-savings agreements to improve the energy utilization of state-owned buildings, saving \$1.9 million to date.
- Installing energy-saving controllers on a variety of pieces of heating, cooling and refrigerating equipment.
- Supplementing the improvements made through guaranteed energy-savings agreements by making other enhancements to state facilities. For instance, the State Police cut energy costs by more than \$211,000 by installing more efficient lighting, roofing and climate-control systems at various locations.

The Rendell administration is on track to achieve \$1.75 billion in annual recurring savings. These efforts have fundamentally changed the way the commonwealth provides services to its citizens. Building on that success, the administration has renewed its efforts to provide Pennsylvania taxpayers with additional savings and more efficient services so resources are directed to programs that can better serve Pennsylvanians and improve our quality of life.

Components of the \$1.5 Billion in Management and Productivity Savings for 2007-08

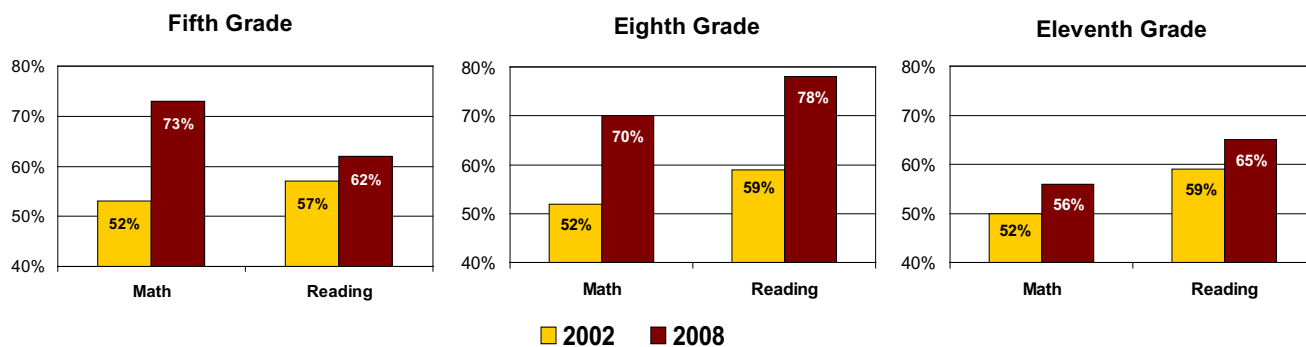


Education - Investing in Our Children, Preparing for the Future

Governor Rendell has made education a top priority for Pennsylvania – championing new investment and greater accountability as critical to the commonwealth’s economic development strategy and in fulfillment of our moral imperative to ensure that today’s students have the opportunity to succeed in the competitive, high-skills knowledge economy of the future.

Pennsylvania’s investment in education is paying off with greater student achievement across the state in every grade and subject.

Math and Reading Achievement on the Rise, 2002 vs. 2008
Percentage of Students On Grade Level



In addition, many of the most academically challenged school districts and student populations are making strong progress:

- 479 school districts have a majority of students on grade level compared to 375 districts in 2002.
- 72 districts have increased the number of students on grade level by at least 40 percent since 2002.
- 36,000 fewer students are “below basic” in math and 13,000 fewer students are scoring in the lowest level in reading in 2008 compared to 2002.

Pennsylvania is one of only nine states in the nation that made progress in elementary school math and reading achievement from 2003 to 2008, according to the National Assessment of Educational Progress, also known as “The Nation’s Report Card.”

We cannot afford to lose momentum now. The national economic crisis has put enormous pressure on state budgets, and Pennsylvania is no exception. But the commonwealth also has the opportunity to recognize educational investment as a core component of our economic recovery strategy.

The better prepared Pennsylvania students are when they graduate from high school, the more likely they are to be employed, the more they will earn and generate in tax revenue, and the less the government will have to spend to support them.

Education translates into a far stronger workforce. An adult with a high school diploma was nearly 30 percent more likely to be employed in 2006 than a high school dropout. A Pennsylvanian with a four-year college degree had even better odds of having a job: a 12 percent greater likelihood than the high school graduate and a stunning 45 percent better chance than the high school dropout. Over a lifetime, a college graduate will earn over \$1 million more than his or her peer with only a high school diploma.

In addition, improving education strengthens communities and saves taxpayers money:

- 77 percent of Pennsylvanians with a bachelor’s degree own their own home – and they are 13 percent more likely to be a homeowner than high school graduates with no or some college education.
- For every \$1 in taxes paid by a Pennsylvania high school dropout, a high school graduate pays \$1.42 and a worker with a four-year degree pays \$2.55. The better educated Pennsylvania’s workforce becomes, the less the tax burden will be on each individual worker.
- Only 4 percent of Pennsylvanians with a bachelor’s degree received food stamps, Medicaid, housing subsidies, free or reduced-price school lunches, or similar government support – compared to 17 percent of high school graduates who do not go to college and 35 percent of high school dropouts.

Education - Investing in Our Children, Preparing for the Future

Growing Pennsylvania's economy by developing a world-class education system starts with the first day of pre-kindergarten and lasts through the final day of high school and a student's transition to college or the workforce. Pennsylvania faces four essential challenges that it must meet in order to ensure that our students are prepared to compete in the global economy:

First, every student needs to attend a school that has adequate resources to get the student achievement results we demand. The commonwealth must ensure that schools have sufficient resources to meet this challenge and that taxpayer dollars are invested in the programs most likely to boost student learning.

Second, our schools need to continue transforming with the times so that when Pennsylvania students graduate from high school, they are ready for the high-tech, high-skills economy that will await them. The commonwealth must provide the accountability, leadership and resources needed to ensure that a Pennsylvania high school diploma is a ticket to post-secondary opportunity.

Third, Pennsylvania schools need to modernize the way they do business by increasing efficiency and accountability. School districts should streamline and consolidate their operations in order to get more resources into the classroom instead of the bureaucracy. Also, Pennsylvania should learn from its successful charter schools while enhancing the public's confidence in charter school funding and accountability.

Fourth, Pennsylvania needs to ensure that family finances never prevent a student from earning a college degree. Nearly three out of four Pennsylvania public four-year university students leave school with student loan debt – far more than in comparable states – and the average student's debt totals nearly \$20,000 by the time they graduate. The commonwealth can make college affordable for every family – without raising taxes.

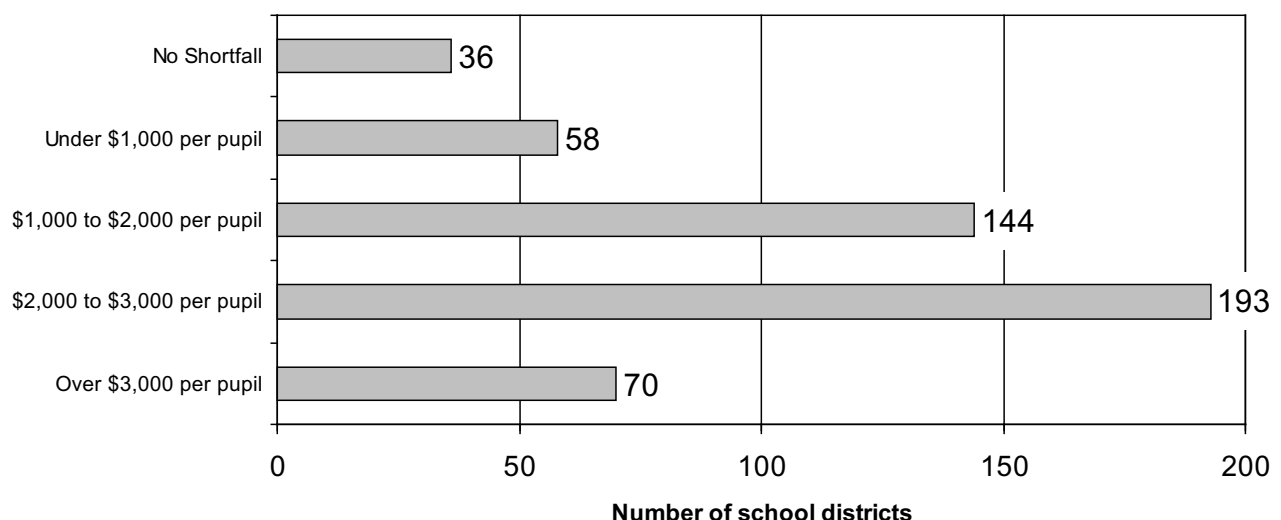
Investing in Student Success

In 2006, the Pennsylvania Legislature commissioned the commonwealth's first-ever study to determine the actual level of resources schools need in order to get students to achieve on grade level. The report concluded that Pennsylvania faced a \$4 billion regular education funding shortfall.

With the 2013-14 federal mandate of getting all students to grade level just five years away, closing this shortfall must be an urgent priority. Pennsylvania has just two more years until the next increase in statewide academic targets that all schools are required to meet: 72 percent of all students on grade level in reading and 67 percent of students on grade level in math. If that standard were in place today, more than 1,500 schools and nearly half of school districts would receive a failing grade.

The evidence from the legislature's report shows that the vast majority of Pennsylvania school districts need additional funding in order to close their achievement gaps.

More Than Half of Pennsylvania School Districts Need \$2,000 or More per Pupil to Close Their Achievement Gaps



Education - Investing in Our Children, Preparing for the Future

To meet the state commitment to close this funding gap, in February 2008 Governor Rendell proposed a \$2.6 billion, six-year plan. In July 2008, the legislature enacted a new school funding law that set an “adequacy target” for each school district based on the formula set forth in the legislature’s report; delivered the first-year installment of the state’s contribution; and stated in law that “...in order to enable students to attain applicable Federal and State academic standards, it is the goal of this Commonwealth to review and meet State funding targets by fiscal year 2013-2014.”

With the academic pressures faced by school districts, it is clear that if the state does not do its part to close this gap, local property tax hikes will be the result.

In these difficult economic times, it is more important than ever to prioritize the use of state resources to have the greatest possible impact. One of the key features of Pennsylvania’s new school funding formula is that the law requires school districts to invest their new resources in a menu of proven academic programs and it gives the Department of Education the authority to reject the investment plans of academically-challenged school districts.

The **2009-10 basic education subsidy includes a \$300 million (5.7 percent) increase** to demonstrate the commonwealth is serious about meeting its commitment to provide adequate resources using the new funding formula, even during an extraordinarily difficult budget year.

In addition to a substantial increase in the basic education subsidy, the 2009-10 budget sustains Pennsylvania’s progress by continuing to support other successful academic programs:

- **High-quality early childhood education.**
 - **\$95.1 million for Pennsylvania Pre-K Counts.** School districts, Head Start programs and other community providers with proven track records of success are eligible to apply for these resources. Nearly 13,000 children from every part of the commonwealth will have new opportunities for early learning as a result of this investment – with the greatest focus on children who are at risk of future academic failure.
 - **\$39.5 million for the Head Start Supplemental Assistance program.** For the last four years, Pennsylvania has supplemented federal Head Start funding so the successful program can reach more families. The 2009-10 funding will make it possible to enroll 5,620 children ages 3 and 4.
 - **\$189 million for Early Intervention.** This \$3.9 million increase will serve an additional 1,107 children ages 3 through 5.

- **\$271.4 million for the Accountability Block Grant.** This initiative funds pre-kindergarten, full-day kindergarten, elementary school class-size reduction and other proven educational programs. Beginning in 2009-10, Accountability Block Grant funding will be folded into each school district’s basic education subsidy.
- **\$65.1 million for the Education Assistance Program.** Pennsylvania’s hallmark tutoring program provides extra help to 172,000 struggling students in 175 school districts and Career and Technical Centers. Beginning in 2009-10, Education Assistance Program funding will be folded into school districts’ basic education subsidies or, for vocational schools, the Career and Technical Education appropriation.
- **\$13.6 million for Science: It’s Elementary.** This budget will enable at least 65,000 students in 141 schools to become active science explorers.

Making the High School Diploma Count

Pennsylvania has made enormous progress in increasing student achievement over the last six years, and has enacted a long-term school funding plan to ensure that students have adequate resources in the classroom for years to come. The commonwealth still faces a significant challenge: How do we make sure families, employers and college admissions officers can have confidence that a Pennsylvania high school diploma means our students are ready for the real world?

The truth is that right now, they can’t. In fact, nearly 44 percent of Pennsylvania’s high school seniors received diplomas in 2007 after failing the state’s 11th-grade-level reading and math tests a year earlier. And one in three Pennsylvania high school graduates who enroll in a state-owned university or community college are not prepared for a first-year college math or English course. Pennsylvania is taking action to give the high school diploma meaning by ensuring that all students demonstrate essential skills in English, math, science and social studies in order to graduate.

Under Pennsylvania’s plan, students would be able to earn their diploma by passing six standardized final exams as soon as they finish key high school courses – while the material is still fresh in their minds. Students who don’t pass the first time would get extra help and have the chance to retake the tests as many times as necessary. Or school districts could use their own local assessments, as long as they are at least as rigorous as the state’s assessment – among a number of other options on the proposed high school graduation menu.

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Pennsylvania's Plan for Ensuring that Every High School Diploma Counts

The State Board of Education proposed a menu of ways for students to show they are ready to graduate. The new requirements would start with the class of 2014 – this year's seventh graders.

Students could earn their high school diploma in any of four ways:

- By scoring Proficient or Advanced on the Pennsylvania System of School Assessment (PSSA) given in 11th grade; OR
- By passing six of 10 standardized final exams, called Graduation Competency Assessments; OR
- By passing local assessments of equal rigor; OR
- By taking Advanced Placement or International Baccalaureate exams.

To ensure that all high school students stay in school and are ready and able to graduate, Pennsylvania is providing more resources and support than ever before:

- **\$22 million for Classrooms for the Future.** This program changes the way teachers teach and students learn in Pennsylvania high schools by putting a laptop on every student's desk and providing teachers with intensive training so they can effectively use the power of the Internet to engage the technology generation and enhance student achievement.
- **\$10 million for Dual Enrollment to Help More High School Students Earn College Credit.** A portion of this funding is directed toward low-income students – who otherwise might never even visit a college campus – to ensure that these students are not “priced out” of an experience that can change their lives.
- **Resources To Help Every Student Succeed.** This budget will offer school districts new resources, including the beginning of a voluntary curriculum for English, math, science and social studies courses; strategies for identifying students who need help and ways to effectively boost their academic skills; and improved teacher training.

Government Reform: Increasing Efficiency and Accountability in Public Education

Bringing government reform to public education means taking the following steps in enacting the commonwealth's 2009-10 budget:

- **Reducing bureaucracy while preserving community schools.** This budget launches a process to investigate options for consolidation and alternative solutions.
- **Using the purchasing power of school districts to cut health care costs.** Pennsylvania can address this issue by creating a statewide school employee health benefit system that will leverage the purchasing power

of all our school districts and potentially 250,000 school employees in a way that is fair to taxpayers, students and teachers.

- **Eliminating excuses when it comes to turning around failing schools.** Existing state laws effectively block major overhauls – leaving students in failing schools for even longer. It is time to increase support to turn around these schools, while also ensuring that schools and school districts that still continue to fail are actually restructured – given new staff while protecting the rights of current teachers, provided a new curriculum, led by new leaders or converted to charter schools – as the federal law envisions.
- **Improving public confidence in charter schools.** With more than a decade of experience in charter education, the state now has the perspective to improve the charter law without threatening the innovative spirit that charter schools were designed to foster.

Making College Affordable for Working Families

Far too often in Pennsylvania, students do not pursue a college degree because their families can't afford it, they leave school mid-way through because college becomes too expensive, or they graduate with so much debt that it is difficult to pursue a career while paying their bills. Meanwhile, Pennsylvania's future economic vitality depends on having a college-educated workforce prepared to lead in the high-skills global economy.

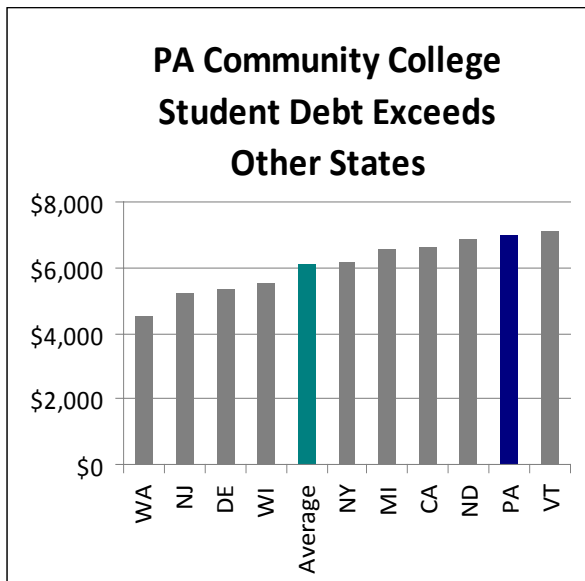
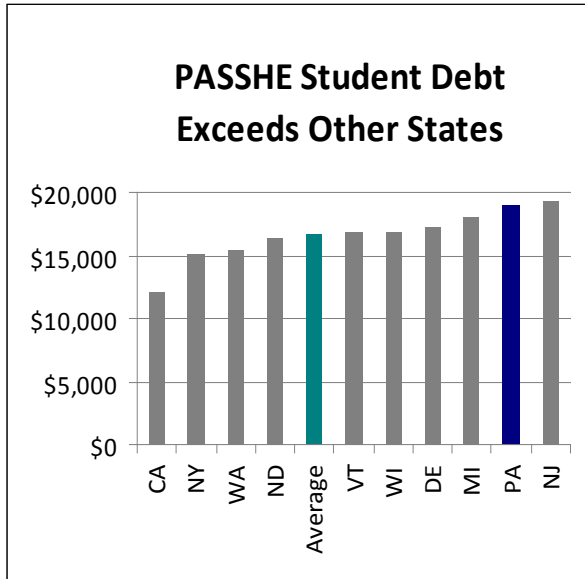
The State System of Higher Education, in partnership with the Rendell administration, has worked hard over the last six years to keep tuition increases to a bare minimum. The last four tuition increases have been below the rate of inflation, and three of the last six have been lower than 3 percent. State System of Higher Education and community college students face significant financial hurdles: 74 percent of SSHE students and one third of community college students leave school with significant student loan debt.

Education - Investing in Our Children, Preparing for the Future

Students in comparative and competitor states do not have the same cost barriers.

In addition, this budget includes a \$45 million increase in Pennsylvania Higher Education Assistance Agency (PHEAA) tuition grants. This increase will dedicate \$10 million to provide grants to nearly 10,000 additional community college students while ensuring that other college and university students do not lose their grants as a result of a reduction in contributions to student grants by PHEAA.

The 2009-10 budget also doubles capital funding for the Pennsylvania State System of Higher Education to \$130 million – ensuring that college students will learn in facilities that prepare them for the high-tech world, while creating jobs across the commonwealth.



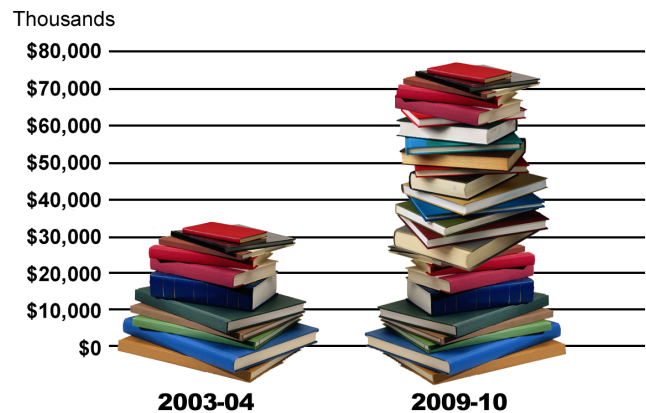
Total Higher Education Funding is Over \$2 Billion

Key Higher Education Funding:	(In Millions)
TOTAL FUNDING	
Community Colleges	\$287.6
State System of Higher Education	\$519.2
State-Related Universities:	
Pennsylvania State University	\$318.1
University of Pittsburgh	160.5
Temple University	165.0
Lincoln University	13.6
Total – State-Related Universities	\$657.2
Non-State-Related Universities and Colleges	\$ 54.9
PA Higher Education Assistance Agency	\$513.7

Tuition Relief

The administration proposes a dramatic increase in state grants for students at Pennsylvania’s core public institutions – the 14 State System of Higher Education campuses and the 14 community colleges. To ensure the long-term affordability of higher education, the commonwealth will establish a dedicated revenue stream by legalizing a limited number of video poker machines at private clubs, taverns and other establishments.

Investing in Libraries. Building a knowledge society demands a strong investment in our public libraries. The 2009-10 budget continues to fund local libraries through \$74 million in state subsidy.

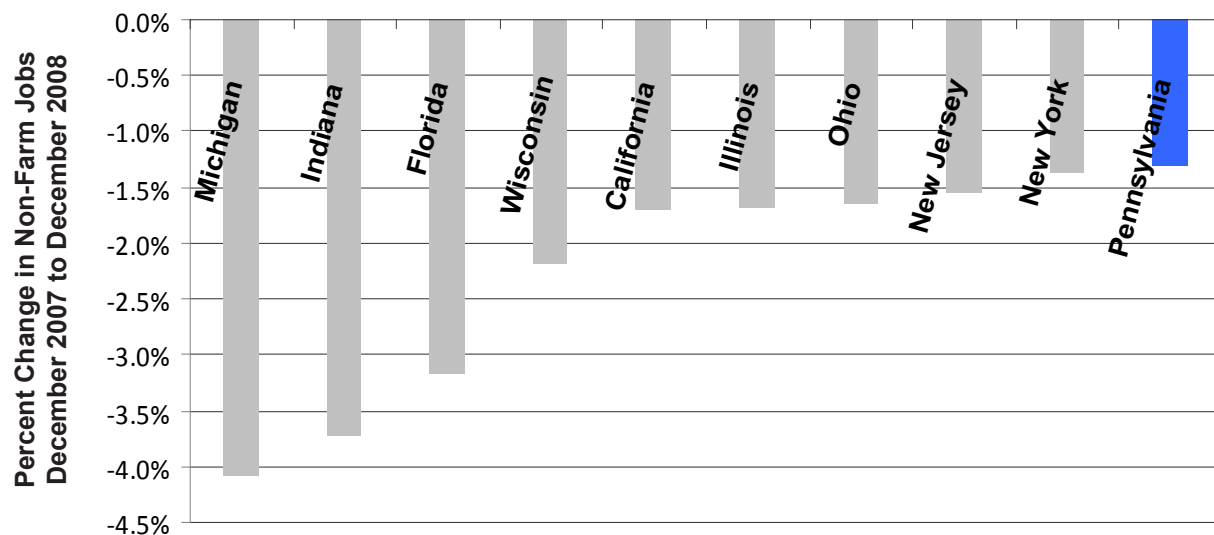


Pennsylvania's Economic Stimulus

Strategic investments in job growth, coordinated economic and community development initiatives, and targeted business tax cuts have strengthened Pennsylvania's economy in the past six years. Although Pennsylvanians are now feeling the impact of the national economic crisis in their daily lives, the crisis is less dire here than in many other states – in part because of the impact of these pro-growth policies.

Despite recent job losses, Pennsylvania still has over 100,000 more jobs today than it did when Governor Rendell took office in January 2003. The commonwealth's unemployment rate has been at or below the national level for 70 of the past 72 months. Since the national recession began in December 2007, Pennsylvania has held onto jobs better than many other large, competitor or neighboring states.

Pennsylvania is Withstanding the National Recession Better Than Other States



Just as Pennsylvania's success over the last six years and during the current economic uncertainty is no accident, so too must the state continue to make smart investment choices to keep our economy moving. With a strong track record of investments in business growth, alternative energy and infrastructure, Pennsylvania is well-poised to stimulate the economy further during this crucial time. While the federal government will be a valuable partner, Pennsylvania cannot afford to simply follow federal leadership or depend on others for our economic growth strategies.

Protecting Our Progress

Since it was approved by the General Assembly in 2004, Pennsylvania's Economic Stimulus program has invested \$3.2 billion and created new opportunities for economic success across the commonwealth. More than 2,800 projects have already been funded with Economic Stimulus program resources – helping Pennsylvania businesses to create and maintain a projected 288,000 new jobs. The rapid pace of investment through the Economic Stimulus program has had a significant impact on Pennsylvania's economy, leveraging more than \$8.6 billion in additional economic activity.

The 2009-10 budget provides additional funding and important changes for several critical components of the Economic Stimulus program as part of Pennsylvania's efforts to respond to the national economic crisis:

- **Attracting More Businesses and Job Growth to Pennsylvania.** The 2009-10 budget includes an additional \$100 million to get Pennsylvania sites shovel-ready for use by businesses moving into the commonwealth or expanding their operations. Of that, \$60 million will be used to reinvigorate the successful Business in Our Sites Program that provides loans and grants for site acquisition and development for future use by businesses, and \$40 million will be invested in water and wastewater infrastructure projects related to economic development. No new funds are needed to make these important investments; instead, the Commonwealth Financing Authority will be asked to leverage existing assets to generate the necessary additional capital.

Pennsylvania's Economic Stimulus

- **Responding to Companies' Needs for Working Capital.** Since 2004, Pennsylvania's Second Stage Loan Program has provided working capital to manufacturing, biotech and technology-related companies that are between 2 and 7 years old. Recognizing the need for more flexibility to help additional Pennsylvania companies in this challenging economic environment, the 2009-10 budget will reallocate under-utilized existing resources to dedicate an additional \$100 million to the loan guarantee program while expanding it to reach companies in other fields and eliminating the time limitations.
- **Infrastructure Facilities Improvement Grant Program.** Every \$1 million of funding for this program creates approximately 2,000 new jobs, but the current pipeline of eligible projects is far greater than the supply of available resources. The 2009-10 budget includes a \$10 million initiative for new infrastructure and facility improvement projects for this valuable engine of economic growth.

In addition, the 2009-10 budget **doubles capital funding for the commonwealth's public universities.** Doubling the State System of Higher Education's \$65 million capital allocation to a total of \$130 million will put Pennsylvanians to work while improving educational facilities that will train the next generation of workers and entrepreneurs.

Rebuilding Pennsylvania

Across the nation, states face \$2.2 trillion in costs to repair aging infrastructure and make essential upgrades. No state can meet this burden alone, but Pennsylvania is doing its part to keep the commonwealth competitive and ensure the public's safety by investing in infrastructure. The 2008-09 budget launched Governor Rendell's Rebuild Pennsylvania initiative with the approval of more than \$1.5 billion to begin addressing overdue repairs to dangerous bridges and dams, as well as investing in necessary improvements to critical aviation and rail freight facilities. In the process, these investments will create tens of thousands of jobs for Pennsylvania workers. Rebuild PA resources approved last year include:

- \$350 million for the accelerated repair of structurally deficient bridges;
- The H2O Fund, implemented through the Commonwealth Financing Authority, that will provide \$800 million over the next 10 years for critical water, sewer and flood-control projects, and repairs to unsafe high-hazard dams; and
- Voter authorization of a \$400 million bond issue to provide funds for PENNVEST to invest in public drinking water and wastewater systems, including innovative, cost-effective strategies such as nutrient trading.

The 2009-10 budget continues Pennsylvania's job-creating infrastructure investments with an additional \$537 million for Rebuild PA projects. This includes \$200 million for bridge repairs, an estimated \$190 million for water, sewer, flood-control and dam projects, \$100 million for PENNVEST water and wastewater projects, \$27.5 million for rail and aviation projects, \$15 million for rail freight assistance, and \$4.5 million for flood-control projects and program support.

These additional resources in the 2009-10 budget mean more jobs and more necessary infrastructure improvements.

Accelerating Needed Bridge Repairs

The 2008-09 budget included \$350 million to supplement the existing bridge program funding. This allowed the Department of Transportation to speed the rebuilding of 411 structurally deficient bridges statewide. As of the end of December, the work is ahead of schedule and these projects are well on their way to generating more than \$300 million in economic activity for construction and supporting 9,000 Pennsylvania jobs.

In addition to targeting funds to the bridges most in need of rebuilding, the Governor directed the Department of Transportation to accelerate the way government does business in order to start as quickly as possible. The department has employed two innovative contracting strategies to achieve this goal:

- Design-build contracts save months of design time by combining the design services of a consultant with the work of a contractor in a single contract. A projected 83 of the 411 bridges funded in the 2008-09 Rebuild PA initiative will be design-build contracts.
- Group contracts combine a number of bridges into a single contract to cut administrative costs and achieve greater economies of scale – saving taxpayers money so that more infrastructure needs can be addressed with limited funds. A projected 187 bridges will be rebuilt through 54 group contracts this fiscal year.

The 2009-10 budget moves forward with the second year of bridge program acceleration with \$200 million of additional resources. These funds will enable 367 structurally deficient bridges to be addressed – supporting 6,600 Pennsylvania jobs. In addition to the \$200 million provided by Rebuild PA, the 2009-10 budget includes \$1.9 billion in base Motor License funds for bridge and highway repair.

Pennsylvania's Economic Stimulus

Rail and Aviation Infrastructure Support

Pennsylvania's infrastructure investment is making businesses and communities more competitive through expanded rail and air projects – work that makes companies more efficient and municipalities more attractive to economic growth.

Pennsylvania has a strong record of making successful investments in rail freight programs that have enabled companies to locate or expand operations in the commonwealth. Rebuild PA increased the Rail Transportation Assistance Program by \$10 million to \$30 million in 2008-09, including \$3 million for the preservation of railroad bridges. The remaining funds will be used to construct and re-establish rail lines, preserve existing rail lines, improve safety and add new capacity.



Rebuild PA will provide \$22.5 million in 2009-10 for additional rail freight projects, bringing the total two-year funding increase to \$32.5 million. In addition, the 2009-10 budget includes \$15 million in additional rail freight assistance funding.

The 2008-09 Rebuild PA budget also doubled the aviation grant program from \$5 million to \$10 million. The economic potential of Pennsylvania's small to medium-sized cities is increasingly being held back by a lack of passenger and freight airport capacity. State funding supports key projects that will be economic generators for both airports and the local communities they serve. New or updated aviation facilities, such as hangars and terminals, make airports attractive to commercial and corporate users looking to base or expand their operations.

The 2009-10 budget provides a total of \$10 million for new aviation facility projects.

Pennsylvania Infrastructure Bank

The Pennsylvania Infrastructure Bank is a loan program that provides low-interest financing for highway, bridge, aviation, rail freight and public transportation projects. Since inception, the Infrastructure Bank has approved 150 loans worth \$84.8 million to municipalities and local authorities, among other recipients. These loans have leveraged an additional \$277.2 million of federal, state, local and private funds. As part of the Rebuild PA infrastructure initiative, the Infrastructure Bank has approved 20 loans for \$10.6 million in the first half of the 2008-09 fiscal year.

Meeting Pennsylvania's Critical Water and Sewer Infrastructure Needs

Since enactment of the \$800 million H2O program in July, guidelines have been developed and the program is accepting applications for all three categories of authorized water projects:

- \$650 million for acquisition, construction, improvement, expansion or rehabilitation of water supply, sewage disposal or storm water management systems or combinations of systems. Funds can also be used for regionalization of two or more systems.
- \$100 million for municipal flood-control projects, including channel improvements, compacted earth levees, concrete channels, concrete floodwalls, detention dams, and non-structural measures.
- \$35 million for repair of high-hazard dams identified by the Pennsylvania Department of Environmental Protection as having deficiencies that if not corrected could cause a failure of the dam, with subsequent loss of lives or substantial property damage.

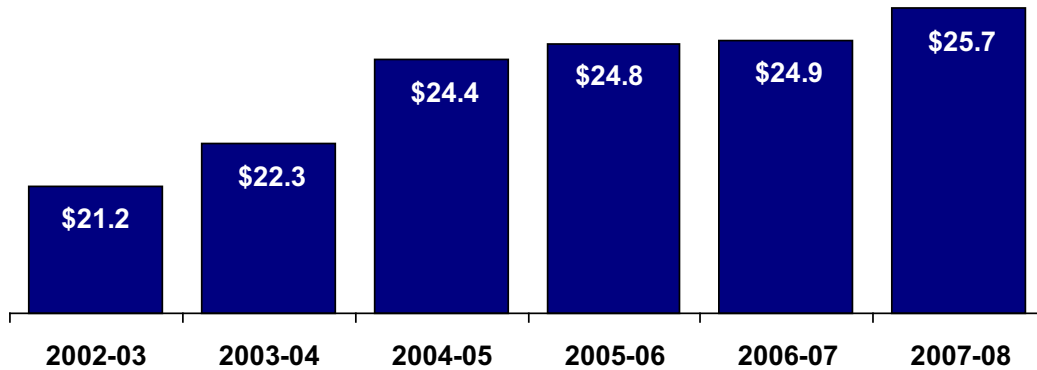
In addition, PENNVEST has been actively advertising and recruiting projects across the state for the \$400 million authorized by the voters in November for water, sewer, storm water and nutrient-trading projects.

Protecting Homeowners – Pennsylvania's Flood-Prevention Program

Flooding has been a consistent problem in Pennsylvania because of the state's 82,000 miles of inland waterways and increased development of land along these waterways. Over the last 10 years, Pennsylvania received more than \$500 million in claims payouts from the National Flood Insurance Program, the second-highest total in the nation prior to the Hurricane Katrina losses. While federal payments are welcome to help repair homes and businesses after a severe flood, more must be done to make our communities more flood-resistant. The Rebuild PA initiative is making flood-prone communities safer with an additional \$3 million in flood-control funds.

Pennsylvania's Economic Stimulus

Total Spending by U.S. Travelers in Pennsylvania
(dollars in billions)



Based on data from D.K. Shifflet & Associates, Ltd.

Pennsylvania Grows Its Tourism Industry

The citizens of Pennsylvania have long been blessed with a commonwealth rich in abundant natural resources, filled with scenic beauty and home to world-class metropolitan areas. Increasingly, people outside of Pennsylvania are taking notice and making the commonwealth a prime destination. Pennsylvania's burgeoning tourism industry is becoming a major economic driver for the commonwealth, with travelers from throughout the United States spending nearly \$26 billion in Pennsylvania – an increase of 21 percent since 2002-03. International visitors contribute an additional \$2 billion each year.

Spending by tourists on a variety of travel-related goods and services supports 610,000 Pennsylvania jobs in businesses that directly serve the traveling public, supply the goods and services used by travelers or benefit from the spending of tourism-related wages by employees of such companies. The commonwealth's tourism industry also generates more than \$2.8 billion annually in state and local tax revenue that is then used for services that benefit all Pennsylvanians.

The Rendell administration has taken a regional approach to investing in and marketing Pennsylvania's tourism assets. These efforts are delivering results:

- Governor Rendell launched a new marketing plan for the 12-county **Pennsylvania Wilds** region of North-central Pennsylvania in 2003 and the results have been dramatic. Visitation to the Pennsylvania Wilds region increased from 3.5 million to 4.1 million people between 2004 and 2007, an 18 percent increase. This increase in visitors has helped fuel demand for hotel

rooms in the region, up 8.8 percent since 2003, and has also helped to drive up the state's hotel tax revenues by more than \$1 million over the same time period. A recent economic study of the Pine Creek Rail Trail revealed that it generates about \$5.5 million annually for the local economy.

- Southwestern Pennsylvania's **Laurel Highlands** region is home to a large section of the 150-mile Great Allegheny Passage, part of a trail system that extends from Pittsburgh to Washington, D.C. The Great Allegheny Passage receives an estimated 350,000 visitors per year who contribute \$10 million to the economies of trail towns located along its span. Administration investments continue to support trail town revitalization and projections are for more than \$12 million to \$15 million in economic impact for 2008.
- The **Schuylkill Highlands** region in the Southeast is home to a large segment of the Schuylkill River Trail, which will eventually span 130 miles from Schuylkill Haven to Philadelphia. Trail and riverboat concession use in the tidal Philadelphia-area Schuylkill River segment is estimated to have had a direct tourism impact of \$1.3 million on the local economy in 2007.
- For the first time, the ten counties of **Northeast Pennsylvania** will be pooling their resources and collaborating in a joint marketing effort. This will enable this region to develop road trips and create itineraries united under one brand that can compete with other destinations in key markets such as New York. This campaign will begin in 2009.

Energy Independence

Leading the Way in the Renewable Energy Economy

Pennsylvania's economy is growing "green." Strategic investments in the alternative energy sector over the last six years have helped the commonwealth become a leader in renewable energy production. Governor Rendell and the legislature have taken steps to invest nearly \$915 million to spur on Pennsylvania's alternative energy economy, both in funds distributed since 2003 and by passing laws to ensure that the commonwealth will be a national leader for years to come.

Growing the Green Economy

State investments since 2003 have funded 564 projects, which have created and retained more than 8,300 jobs. As a result, Pennsylvania is now home to some of the world's leading renewable energy companies and is on track to produce 18 percent of all energy sold in the state from clean renewable sources by 2021. On July 9, 2008, Governor Rendell signed the Alternative Energy Investment Act into law. The law provides \$650 million in funding and tax credits over the next several years for alternative energy projects, companies and technologies that will help make Pennsylvania a leading destination for green jobs and clean energy. Key investments include:

- \$270 million in economic development support for energy projects and companies through the Commonwealth Financing Authority,
- \$220 million for consumers and small businesses for energy efficiency, solar and green building projects,
- \$50 million in tax credits for developing and building alternative energy projects,
- \$40 million to provide heating assistance to low-income customers,
- \$40 million to foster the development of early stage energy technology companies,
- \$25 million for pollution-control technology, and
- \$5 million for the Home Energy Efficiency Loan Fund.

Over the past four years the programs and partners with the Technology Investment Office in the Department of Community and Economic Development have invested approximately \$37.8 million in more than 140 alternative energy and related projects. This funding leveraged \$69.1 million in additional investment to enhance the commonwealth's alternative energy capabilities.

Moving Towards Independence From Foreign Oil

The PennSecurity Fuels Initiative is fostering economic development, energy independence and environmental protection through the use of alternative fuels by requiring all diesel fuel and gasoline sold in Pennsylvania to contain ethanol or biodiesel. By 2017, 1 billion gallons of home-grown biofuels will be produced and consumed in Pennsylvania – an amount equal to what the state will import from the Persian Gulf by that time.

Pennsylvania is already well on its way to increasing production of home-grown alternative fuels. In January, the commonwealth announced that Pennsylvania businesses are now producing 40 million gallons of biodiesel a year – the first key threshold under the law. Every gallon of on-road diesel fuel sold in Pennsylvania must contain 2 percent biodiesel fuel within one year. At the law's full potential of 20 percent biodiesel and 10 percent ethanol, Pennsylvania will cut oil imports by billions of dollars a year.

To help build the market for alternative fuels, Pennsylvania launched the Biodiesel Production Incentive – which provides 75 cents per gallon for biodiesel produced and sold in Pennsylvania. The commonwealth has awarded \$2.29 million in production incentives since July 1. By 2011, Pennsylvania will reach \$15.9 million in biodiesel production incentives.

Diversifying Our Energy Supply

Pennsylvania adopted the Alternative Energy Portfolio Standards Act that requires companies that generate and distribute electricity to fill a portion of the commonwealth's energy needs using alternative energy sources.

By 2021, Pennsylvania's electric generation and distribution companies will be expected to generate 18 percent of their retail electricity from alternative energy sources. In the year that ended on May 31, 2008 – the second year of the program's implementation:



- Six Pennsylvania electric distribution companies met their alternative energy requirements, and
- 11 electric generation suppliers met their alternative energy targets.

The companies that do not reach their targets contribute to a special fund used for projects that will increase the amount of electric energy from alternative energy resources.

Prescription for Pennsylvania

Making Quality Health Care Affordable and Accessible in Pennsylvania

Launched by Governor Rendell in January 2007, **Prescription for Pennsylvania** is the commonwealth's plan to ensure access to affordable health insurance for all Pennsylvanians, expand the availability of health care, improve the quality of care and help bring health care costs under control for employers and workers.

Many components of **Prescription for Pennsylvania** have already been successfully implemented and Pennsylvania has made strides in improving quality, expanding access to care and reducing costs by reducing avoidable health-care-associated infections and avoidable hospitalizations. Yet the commonwealth has failed to adopt some of the most crucial elements of this plan. In these tough economic times, it is even more important to implement the critical remaining components of Prescription for Pennsylvania.

Pennsylvania Has Taken Several Essential First Steps in Health Care Reform

- **Pennsylvania is “Covering All Kids” to provide universal health insurance for the commonwealth’s children.**

In 2006, the General Assembly passed Governor Rendell’s Cover All Kids initiative, making Pennsylvania one of six states in the nation to ensure that all children have access to health care coverage. As a result, the number of children in Pennsylvania’s Children’s Health Insurance Program has risen by one-third – from 125,983 in January 2003 to 183,891 in January 2009.

Cover All Kids:

- Provides comprehensive health care coverage, including visits to doctors, hospitalization, prescription drugs, mental health and substance abuse services, vision, dental and home health care.
- Subsidizes coverage for children in families whose annual income is up to 300 percent of the federal poverty level (\$66,150 for a family of four in 2009). Family premiums range, on average, from between \$43 and \$69 per month per child.
- Offers at-cost coverage for children in families whose income exceeds 300 percent of the federal poverty level (on average, \$172 per month per child).
- **Pennsylvania is ensuring that older adults have access to affordable prescription drugs.**

In November 2003, Governor Rendell signed into law a historic expansion of Pennsylvania’s PACE and PACENET programs that provide affordable prescription medication for senior citizens.

- In response to the federal government’s implementation of Medicare Part D, Pennsylvania established “PACE Plus Medicare,” which

guarantees that eligible seniors will not incur more costs than they otherwise would have paid when their prescriptions were covered by PACE and PACENET.

- **Pennsylvania has adopted the most comprehensive plan in the nation for eliminating health-care-associated infections.**

- Act 52 of 2007 is Pennsylvania’s first-ever law requiring that health care facilities report all incidents of health-care-associated infections and adopt plans to reduce them. The Pennsylvania Health Care Cost Containment Council reported that for 2007, health-care-associated infections were 7.8 percent lower than in 2006, with 300 fewer deaths than in the previous year. This budget recommends \$2.6 million for health-care-associated infection-reduction initiatives in 2009-10.

- **Pennsylvania is improving prevention and treatment of chronic diseases such as heart disease, diabetes and asthma.**

- Approximately 78 percent of all health care costs in Pennsylvania can be traced to the 20 percent of patients with chronic diseases. In February 2008, the Governor approved the Chronic Care Management, Reimbursement and Cost Containment Commission’s strategic plan to improve the delivery of health care to Pennsylvanians with chronic diseases. The plan calls for the design of the informational, technological and reimbursement infrastructure needed to support implementation of the chronic care model throughout the state.
- This budget recommends \$1.5 million for chronic care management in 2009-10. With this investment, the commonwealth expects to leverage \$35 million from private insurers over three years.

- **Pennsylvania is taking the lead in developing a statewide health information exchange to reduce medical errors and improve the quality of care for patients.**

- A health information exchange will enable clinicians to have access to important medical details about the patients they treat and, with their patients’ consent, share that information with other health care providers for treatment purposes.

Prescription for Pennsylvania

- In 2008, the Pennsylvania Health Information Exchange was established to provide the information technology architecture to support statewide interoperable electronic health records. This budget includes \$3 million to develop and begin implementation of a statewide information technology system.

Pennsylvania's Medical Malpractice Reforms are Working

The success of Pennsylvania's health care system depends on a continuing ability to recruit and retain world-class doctors and other medical professionals. When Governor Rendell took office in January 2003, medical malpractice posed a major threat to the well-being of health care in the commonwealth.

The tide has turned. Initiatives implemented by the current and prior administrations, the General Assembly and the Supreme Court have had a substantial impact on the medical malpractice climate.

- There is not an exodus of doctors from Pennsylvania. In fact, Pennsylvania has about 2,000 more doctors today than it had in 2003.
- In the last four years, doctors in Pennsylvania have seen their malpractice premiums drop by \$14,100 on average.
- Insurance rates are decreasing for the first layer of medical malpractice insurance that doctors are required to carry – the coverage administered by private insurance companies. In 2008, one insurer reduced base premiums by an average of 11 percent as compared to 2007 and the other insurer reduced rates by 6 percent.
- Assessments are decreasing for medical malpractice insurance provided through the state's Medical Care Availability and Reduction

of Error (Mcare) Fund. The amount and number of claims payouts decreased for the fifth straight year. In fact, in 2008, Mcare paid less than half of what was paid in 2003.

- The number of statewide medical malpractice claims was 41 percent lower in 2007 than the base period of 2000 to 2002, before medical malpractice reforms were implemented.

Unfinished Business: Filling the Prescription for Pennsylvania

Hundreds of thousands of uninsured Pennsylvania adults face the very real fear that a sudden job loss or illness could lead to unnecessary personal suffering and possibly even bankruptcy.

- **An expanded adultBasic program will provide affordable basic health insurance for uninsured individuals.**

The vast majority of Pennsylvania's uninsured adults are employed: Most of the working uninsured have full-time jobs and many are employed by small businesses. Most earn low wages and do not have access to health insurance because of the high cost of premiums for both businesses and individuals. An expanded adultBasic program will begin to address these problems.

Health care coverage under the expanded adultBasic program will be offered through private insurance companies and will include coverage for prescription drugs. The proposal will increase the number of low-income Pennsylvanians with state-supported health care insurance by 50,000 – from approximately 40,000 at the end of 2008-09 to an estimated 90,000 by the end of 2009-10.

The total state and federal cost for the expanded adultBasic program is projected to be \$251.7 million in 2009-10. State funding for the program is derived from

Expansion of Pennsylvania's adultBasic Program

	(Dollar Amounts in Thousands)			
	2009-10 Estimated	2010-11 Estimated	2011-12 Estimated	2012-13 Estimated
State Funds				
adultBasic Tobacco Funds	\$29,949	\$28,044	\$24,044	\$19,608
Community Health Reinvestment	83,224	129,947	122,802	108,763
Transfer from HCPRA	<u>0</u>	<u>0</u>	<u>19,323</u>	<u>47,085</u>
Subtotal State Funds	113,173	157,991	166,169	175,456
Federal Funds	132,855	185,467	195,067	205,970
Individual Enrollee Share	5,683	8,264	8,674	9,111
TOTAL	\$251,711	\$351,722	\$369,910	\$390,537

Prescription for Pennsylvania

existing tobacco and community health reinvestment funds used to support the more-limited current adultBasic program, and \$66.4 million from the Health Care Provider Retention Account by the end of four years.

The program will also be funded with new federal matching funds and enrollee premiums.

The expanded program will begin providing health care coverage to new enrollees on July 1, 2009, assuming timely passage of state legislation and approval by the federal government for the use of federal matching funds. The expansion will sunset on June 30, 2013.

- **Pennsylvania will pay down Mcare’s Unfunded Liability – the “Claims Tail.”**

To protect the substantial progress that has been seen in the medical malpractice climate, the 2009-10 budget proposes to “pre-pay” the unfunded liability of the Mcare Fund, with contributions derived from the following sources:

- A \$280 million down payment from the Health Care Provider Retention Account;
- Continued redirection of \$44 million per year in moving violation surcharge revenues from the Catastrophic Loss Benefits Continuation Fund to the Mcare Fund through December 2023, providing a total of \$638 million in revenues;
- The current balance of the Mcare Fund, which was approximately \$104 million in December 2008; and
- Interest earnings on these contributions for the duration of the Mcare claims tail.

These sources will pay off Mcare’s unfunded liability over the long term, allowing Mcare to terminate health care provider assessments once the fund is no longer providing prospective coverage.

A Continuing Commitment to Health Care Reform

In addition to an expanded adultBasic program and paying down the unfunded liability of the Mcare Fund, the commonwealth needs to enact other important efforts to achieve comprehensive health care reform:

- **Protect individuals and small businesses from extraordinary spikes in health care premium costs through more effective regulation of the individual and small-group insurance market.** The **Prescription for Pennsylvania** calls for the

strengthening of state oversight of health insurance companies and health maintenance organizations. This strengthened oversight will protect individuals and small employers from volatile premium increases, require insurers to establish a standard basic health care package for individuals and small businesses, and prohibit insurers from driving up the cost of insurance based on narrowly defined demographic characteristics.

- **Eliminate duplicative and unnecessary capital expenditures for new technology, equipment and facilities.** The **Prescription for Pennsylvania** calls for the development of a strategy to effectively control expensive health care expenditures and the establishment of criteria that ensure that future expensive capital expenditures will strategically address health care needs.
- **Modernize hospital regulations.** The **Prescription for Pennsylvania** calls for updating Pennsylvania’s hospital regulations to reflect quality improvement practices, standardized admission and billing criteria, improved charity care transparency, elimination of avoidable emergency room use, and improved patients’ rights and responsibilities and discharge planning.
- **Modify PACE reimbursement rates and pharmaceutical dispensing fees.** Since the inception of the PACE program, the Average Wholesale Price (AWP) has been the primary component of the reimbursement formula for participating pharmacies. Because recent studies have indicated that AWP bears little relationship to the actual cost of the drug paid by the retailer, this budget proposes to add Actual Acquisition Costs as the primary component, which is the final cost paid by the pharmacy after all discounts, rebates and charge-backs are subtracted.

The 2009-10 budget also proposes increased dispensing fees that will offer incentives for pharmacists to consult with prescribing physicians about substituting equivalent generic drugs for brand-name drugs. The proposed dispensing fees are \$5 for brand-name drugs and \$10 for generic drugs. This initiative will generate approximately \$41.6 million in savings in the first year of implementation.

Implementation of the remaining elements of Prescription for Pennsylvania will make Pennsylvania a national leader in addressing the issues of health care cost, funding and quality.

Preserving the Safety Net – Helping Pennsylvanians in Need

Helping Our Families and Our Neighbors to Find Work, Regain Independence and Live in Dignity

Although Pennsylvania's economy has fared better than the economies of many other states, the onset of the recession means that more Pennsylvanians need help putting food on the table, heating their homes and caring for their families. The commonwealth's social safety net needs to be there to help Pennsylvania's children, families, seniors and other vulnerable adults survive tough economic times.

Protecting Pennsylvania's Most Vulnerable Citizens

To meet these continuing commitments, the 2009-10 Department of Public Welfare budget provides an increase of \$474.8 million in General Fund resources to expand programs for Pennsylvanians in need — a 5.2 percent increase from the previous year.

The Commonwealth Provides Vital Services to Children, Seniors and Other Pennsylvanians in Need		
PROGRAM	People Served 2008-09	People Served 2009-10
Medical Assistance – Health Care for Low-Income Elderly, Disabled, Children, Adults and Chronically Ill Adults	1,960,514	2,022,490
Pharmaceutical Assistance Contract for Elderly (PACE)/ PACENET	360,000	375,000
Protection for Children at Risk due to Abuse, Neglect and Delinquency	283,745	286,983
Cash Assistance (TANF, General Assistance and State Blind Pension)	219,414	225,240
Child Care for Low-Income Families	246,579	253,054
Children's Health Insurance Program	183,356	206,836
Community Mental Retardation and Autism Services	48,991	50,051
adultBasic (year-end)	40,052	90,000

Note: Some people may receive services in more than one category.

Medical Assistance: Continuing Services Through Cost-Containment

The 2009-10 budget for Medical Assistance will provide health care and long-term care services to more than 2 million Pennsylvanians, a 3.2 percent increase over the prior year. This budget includes broad-based cost-containment reforms and revenue replacement initiatives to fund needed services in critical programs. The commonwealth developed the cost-containment package with three guiding principles in mind:

- 1) Minimize the impact on seniors, children, families and other vulnerable individuals.
- 2) Apply cost reductions across all program areas.
- 3) Avoid program changes that could result in costly placements in institutional settings.

The cost-containment initiatives for the Medical Assistance program total \$329.1 million and include the following:

- Implement a 2 percent assessment on all managed care organizations in the state beginning January 1, 2010, saving \$200 million. (generates revenue as opposed to savings)
- Assume responsibility for managing the pharmacy benefits currently managed by HealthChoices providers, saving \$54 million.
- Modify the Behavioral Health HealthChoices program, saving \$35 million.
- Reduce supplemental payments to hospitals, saving \$20 million.
- Implement additional fraud and abuse initiatives, saving \$15.7 million.
- Increase efficiencies in the Access Plus program, saving \$4.4 million.

Preserving the Safety Net – Helping Pennsylvanians in Need

Cost-Containment Initiatives	Dollar Amounts in Millions	
	2009-10	2010-11
Replace Managed Care Assessment – The department proposes to implement a 2 percent assessment on all managed care organizations in the state beginning January 1, 2010. This will replace the existing Medicaid MCO assessment, which the federal government will discontinue October 1, 2009.	\$200.0	\$400.0
Implement Smart Pharmacy Program – The department will assume responsibility for administering the pharmacy benefits currently managed by HealthChoices providers. This will simplify prescribing, dispensing and claims submission for providers, maintain consumer access to quality health care and enable the department to receive federal drug rebates, resulting in substantial savings in taxpayer dollars.	\$54.0	\$146.0
Increase Behavioral Health Managed Care Efficiencies – The department completed the statewide implementation of its behavioral health managed care program in 2008. Program modifications, including adjusting the level of county risk and contingency funds and tightening the treatment of reinvestment funds, will be implemented in		
Reduce Hospital Supplemental Payments – The department will reduce supplemental payments to hospitals through across-the-board reductions in inpatient, outpatient, medical education and community access funds.	\$20.0	\$20.0
Reduce Fraud and Abuse and Expand Third-Party Liability – The department will implement a Medical Assistance false claims act, enhance the recipient restriction program, limit attorney fees, place a cap on past medical expenses that can be included in determining Medical Assistance eligibility and implement other initiatives.	\$15.7	\$28.1
Increase Access Plus Efficiencies – The department will continue to enhance disease management by covering an additional 21 conditions, including stroke, hypertension, gastrointestinal diseases and neurological disorders. It will also implement a package of pharmacy management initiatives to reduce costs and improve therapeutic outcomes, including expanding the specialty pharmacy program, strengthening utilization management and creating a mail-order delivery system.	\$4.4	\$11.5
TOTAL	\$329.1	\$615.6

Reforming the Long-Term Living System

The 2009-10 budget proposes to further integrate the long-term living programs that are administered by the Departments of Aging and Public Welfare by consolidating these programs into the Department of Aging and Long Term Living. Establishing a single state entity for the administration of long-term living services will result in rebalancing long-term living resources by consolidating policy, financing, quality management and administration into one department. This consolidated department will enhance the ability of persons with disabilities and older persons to live with dignity and independence in the setting they prefer.

This Budget Recommends:

- \$4.4 billion in total funds from the Department of Public Welfare to the Department of Aging and Long Term Living.
- \$9.6 million to provide home and community-based services to 2,000 additional older Pennsylvanians.
- \$16.5 million to provide home and community-based services to 1,600 additional persons with disabilities.

Expanding the Availability of Quality Early Childhood Services

Quality early childhood programs not only support families in their quest for self-sufficiency, they also support the development of children and their preparation for school and life success. In 2009-10, quality child care services will be provided to 6,477 additional children.

This Budget Recommends:

- \$20.6 million in state funds to provide quality child care services to an additional 6,477 children of low-income families and for Keystone STARS providers to continue to improve service quality.
- \$20 million in state funds for Early Intervention to serve nearly 2,980 additional infants, toddlers and preschoolers who are experiencing developmental delays.
- \$3 million for the Early Learning Network, an integrated information technology system that captures assessment data.

Preserving the Safety Net – Helping Pennsylvanians in Need

Protecting Children and Preserving Families

This budget includes an increase of \$6.3 million to allow more children to be adopted and to continue to provide financial assistance to those who have already been adopted.

Expanding Services for Individuals with Developmental Disabilities

The 2009-10 budget continues to support independence for people with mental retardation and mental illness.

This Budget Recommends:

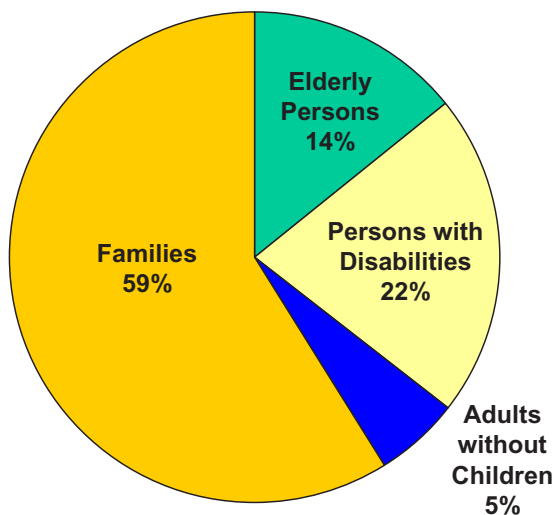
- \$15.1 million to provide home and community-based services for 793 additional individuals with mental retardation, including 500 young people leaving the special education system.
- \$7.7 million in additional funds to continue to provide home and community-based services for adults with autism.

- \$4.2 million in additional funds to support community-based mental health programs for persons discharged from state hospitals.
- \$1.4 million to provide home and community-based start-up funding for 32 additional people currently living in intermediate care facilities for the mentally retarded to move into the community in 2009-10.

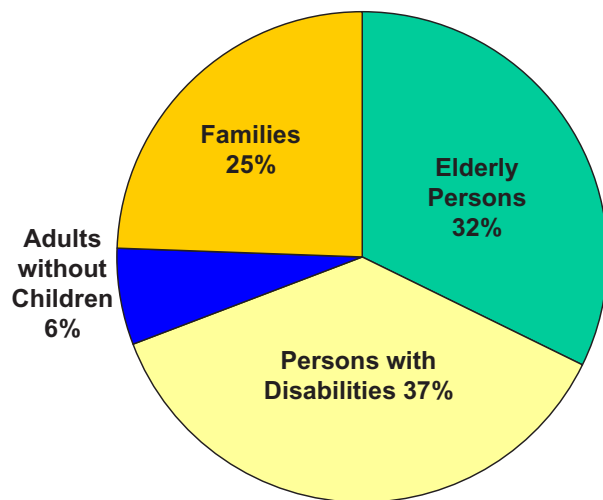
Expanding Health Services for Pennsylvanians

- \$774,000 in additional funds to expand the newborn screening program to provide for additional confirmatory tests and follow-up services as mandated by Act 38 of 2008.
- \$1.2 million in additional funds to provide increased utilization for current enrollees with chronic renal failure.

Seniors and People with Disabilities Use the Greatest Share of Medical Assistance Resources



**Total People
2 Million**



**Total Expenditures
\$14.3 Billion**

Elderly and disabled persons make up only 36 percent of the total Medical Assistance population, but they account for 69 percent of the Medical Assistance expenditures. Families comprise 59 percent of the Medical Assistance population but account for just 25 percent of the expenditures.

Making Pennsylvania Safer

The commonwealth continues to take a comprehensive and proactive approach to creating stronger communities by making Pennsylvania safer.

Even in these difficult and challenging economic times, the commonwealth is committed to ensuring a comprehensive and proactive approach to keeping Pennsylvanians safe. This budget illustrates that commitment by continuing to fund State Police troopers at a high level, fortifying our emergency preparedness functions, and providing the Department of Corrections and the Board of Probation and Parole with the tools necessary to reduce victimization and increase public safety.

Continuing Record Number of State Police Troopers

Governor Rendell has consistently recognized the vital services Pennsylvania's state troopers provide; under his leadership, the number of state troopers has reached levels historically higher than those in all previous administrations. The number of troopers is projected to exceed 4,500 in 2009-10. This budget provides an effective level of state troopers to keep communities safe, patrol the commonwealth's interstates, investigate firearm-related and drug crimes, and ensure that sex offenders comply with their registration requirements under Pennsylvania's Megan's Law.

Expanding Capacity to Safely House Prisoners

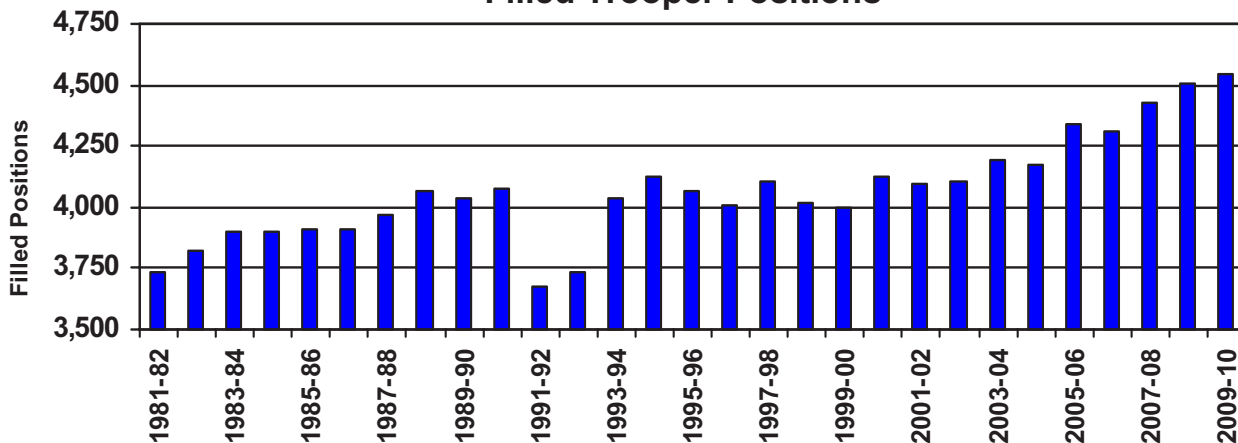
Pennsylvania's offender population continues to increase. In light of the increases in Pennsylvania's prison population and to ensure continued compliance with national standards, this budget provides \$19.6 million in funding to the Department of Corrections for more than 1,600 additional beds at 10 different institutions and \$11.9 million for an additional 800 community corrections beds. This budget also provides \$2 million for additional parole officers to effectively supervise parolees and to avoid repeat victimization after release on parole.

Providing Programs for Less-Violent Offenders to Successfully Re-enter Society and Ensuring that Violent Offenders Serve Longer Prison Terms

In September 2008, Governor Rendell signed comprehensive legislation that will reduce the recidivism rate, reduce crime and help to control the prison population by increasing access to drug treatment programs and providing incentives for less-serious offenders to complete programs that offer the tools they need to live crime-free in society. This legislation projects a total five-year cost savings of \$84.5 million. In addition, the legislation helps to address the needs of less-serious offenders, whose admission rates have increased at a far greater pace over the last eight years than the admission rate of violent offenders. In 2000, less-violent offenders made up 28 percent of the prison population, while today that figure is nearly 40 percent.

In contrast to the majority of offenders, some offenders will continue to pose a threat to public safety if they are paroled before they possess the skills and competencies necessary to reintegrate into society. The Governor has proposed legislation that would change the sentencing structure for repeat violent offenders who use a deadly weapon in the commission of a crime by instituting certainty in sentencing. This proposed legislation will ensure a longer prison term and end the possibility of parole for these offenders. Specifically, the Governor's proposal would establish flat, determinate sentences for repeat violent offenders who use deadly weapons, to be followed by a five-year period of post-release supervision. Nearly 25 other states and the federal government have either eliminated or limited parole for certain classes of offenders.

Filled Trooper Positions



Making Pennsylvania Safer

Improving the Commonwealth's Preparedness for Disasters and Emergencies

Emergency Preparedness. An ongoing priority for the commonwealth has been executing an all-hazards emergency preparedness strategy comprised of the four essential mission areas of prevention, protection, response and recovery. A comprehensive analysis of the commonwealth's preparedness capabilities has led to a continued effort to restructure emergency preparedness efforts in Pennsylvania. This restructuring includes:

- Transitioning the Pennsylvania Emergency Management Agency into the Department of Emergency Management and Homeland Security – a Cabinet-level agency.
- Bolstering the Governor's Emergency Management Council with additional members and new responsibilities.
- Requiring the new Department of Emergency Management and Homeland Security to develop and implement a comprehensive Commonwealth Preparedness Strategic Plan.
- Requiring the Department of Emergency Management and Homeland Security to coordinate emergency management and response efforts across all state agencies.
- Implementing a more aggressive and fiscally responsible model for distributing federal and state funds.
- Continuing successful partnerships with local governments, the private sector and the federal government.
- Continuing the ReadyPA Citizen Preparedness Campaign and launching a statewide, multi-technology emergency alerting and notification system.
- Pursuing an update to the Pennsylvania Emergency Management Services Code. These statutory provisions must be amended to reflect national changes in emergency management and homeland security enacted since the attacks of September 11, 2001 and Hurricane Katrina in 2005.
- Continuing to institutionalize the National Incident Management System to enable all jurisdictions and disciplines providing public safety services across the commonwealth to work together to better respond to disasters and emergencies.

Pandemic Preparedness. The Department of Health, the Department of Emergency Management and Homeland Security and the Office of Administration will continue to monitor and prepare for the possible threat of a pandemic event caused by the H5N1 strain of avian influenza and any other emerging disease threat. The commonwealth's efforts on this subject are focused on three main activities:

- Preparing state employees and establishing necessary continuity of operations plans and policies and testing those plans;
- Ensuring that the commonwealth's health care, emergency management and other response partners are prepared by developing and testing more robust plans to address the issues of vaccine and antiviral distribution, community disease containment, health care system capacity, local government response, workforce planning, and citizen education and preparedness; and
- Working with critical industry partners to ensure that essential industry functions are sustained if a pandemic occurs.

Public safety is integral to a high quality of life and continues to be a priority for Governor Rendell. By maintaining a historic level of law enforcement personnel, offering offenders the treatment and supervision necessary to prevent a return to prison, and enhancing the commonwealth's emergency preparedness and response capability, Pennsylvania continues to take proactive measures to improve the safety and security of its citizens.



Property Tax Relief for Pennsylvania

The 2009-10 Budget Will Provide Nearly \$787 Million in Continued Property Tax Relief

Pennsylvania will become even more competitive in 2009-10 through the continuation of last year's historic reduction in the amount of property tax paid by each Pennsylvania homeowner. This budget marks the second year of long-anticipated property tax relief, which is designed to provide the greatest benefit for those communities with weak tax bases and high tax burdens, so they can increase their competitive edge.

Continuing Property Tax Relief for All Pennsylvania Homeowners

The 2009-10 budget marks the second year of historic property tax relief for all Pennsylvania homeowners. The Taxpayer Relief Act – signed into law in 2006 – has already eliminated school property taxes for more than 113,000 senior citizens. In the coming year, Pennsylvania homeowners, on average, will continue to receive nearly \$200 in state-funded property tax relief – with even more savings for older adults who have the most urgent need.

The 2009-10 budget provides nearly \$787 million in property tax relief, including \$612.9 million in broad-based property tax relief and \$143.4 million in property tax and rent rebates for Pennsylvania's senior citizens. When fully in place, this tax reform will cut property taxes by more than \$1 billion each year.

- In 2009-10, the \$612.9 million in **broad-based property tax cuts** will translate to an average of nearly \$200 for every Pennsylvania household. Instead of reducing property taxes, Philadelphia's share of funding for broad-based tax relief will be used to reduce the city's wage tax, which is a greater barrier to economic growth in Philadelphia. The Taxpayer Relief Act also

allows Scranton to use a portion of its tax relief funds to cut that school district's wage tax, the highest of all Pennsylvania school districts.

- The **Property Tax/Rent Rebate program** will provide \$143.4 million in property tax and rent rebates for 624,000 of Pennsylvania's senior citizens earning less than \$35,000 a year. This program funds tax relief for 412,000 homeowners and 212,000 renters. These older Pennsylvanians will receive additional property tax relief through the broad-based property tax relief eligible to all homeowners.
- In addition, **senior citizens who pay a significant portion of their income in property taxes or who live in high property-tax areas** will receive additional targeted property tax relief totaling \$30.6 million in 2009-10.

Pennsylvania's favorable business and tax climate, along with property tax reductions that are the direct result of the successful implementation of expanded legalized gaming, puts the commonwealth in a strong position to attract and retain jobs. And the Governor's plan for Protecting Our Progress ensures that the economic gains Pennsylvania has made over the last six years will not be lost in the face of the current national economic challenges.

Estimated Property Tax Relief Funded by Expanded Gaming in Pennsylvania

Type of Tax Relief	Amount of Tax Relief in 2009-10
Property tax relief for all homeowners from gaming revenue (wage tax relief in Philadelphia)	\$612.9 million
Enhanced property tax rebates of up to \$650 for senior citizens earning up to \$35,000 a year	\$143.4 million
Higher rebates for senior citizens with a high tax burden or those living in cities with a high tax burden	\$30.6 million
TOTAL	\$786.9 million

Pennsylvania's Tax Structure

Works for Businesses and Families

Over the last six years, businesses and families have saved \$5.9 billion through tax cuts and other policies that reduce the cost of doing business in Pennsylvania – including more than \$4.2 billion in cumulative savings for businesses that create jobs and \$1.7 billion in savings for Pennsylvania families. Despite the national recession, Governor Rendell has proposed a balanced budget for 2009-10 without any broad-based tax increases while keeping Pennsylvania's tax structure competitive with neighboring and other large states.

Total Savings Through Tax Cuts (dollars in millions)

	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Business Tax Cuts	\$20.3	\$181.3	\$386.9	\$712.4	\$1,239.4	\$1,624.4	\$1,977.9
Non-Business Tax Cuts	\$60.1	\$133.7	\$154.3	\$190.2	\$205.5	\$1,009.3	\$1,009.7
TOTAL	\$80.4	\$315.0	\$541.2	\$902.6	\$1,444.9	\$2,633.7	\$2,987.6

Business Tax Cuts – Includes capital stock and franchise tax; sales, research and development, educational improvement, keystone innovation zone and other tax credits; and net operating loss expansion.

Non-business Tax Cuts – Includes special poverty exemption, inheritance tax recouple to federal estate tax, 529 deductions and all property tax relief.

Pennsylvania's Tax Structure is Competitive

By virtually any measure, the level of taxes in Pennsylvania is in line with – and in many cases is better than – the tax climate in neighboring and competitor states:

- The non-partisan, business-funded Tax Foundation rates the commonwealth's business tax climate as more favorable than that of five of our six neighboring states – New York, New Jersey, Maryland, Ohio and West Virginia – and Pennsylvania's 2009 ranking is near the middle of the pack nationally, at 28th best out of 50 states. The Tax Foundation also says that the total state-local tax burden in Pennsylvania is lower than in New Jersey, New York, Maryland and Ohio – all of our neighboring states except Delaware and West Virginia.
- In 2007, Pennsylvania ranked 24th in the nation in annual per capita state taxes – with a lower burden of total state taxes than the national average. The commonwealth's per capita total tax burden is lower than Delaware, New Jersey, New York, Maryland and West Virginia.
- In 2007, Pennsylvania ranked 32nd in total state taxes as a percent of personal income – better than West Virginia, Delaware, New York and New Jersey.
- A 2007 study by the financial services firm Ernst & Young, in conjunction with the Council on State Taxation, showed that Pennsylvania businesses pay a smaller share of total state and local taxes than the national average and pay lower taxes than businesses in three of our six neighboring states.

Cumulative business tax cuts since 2003 include:

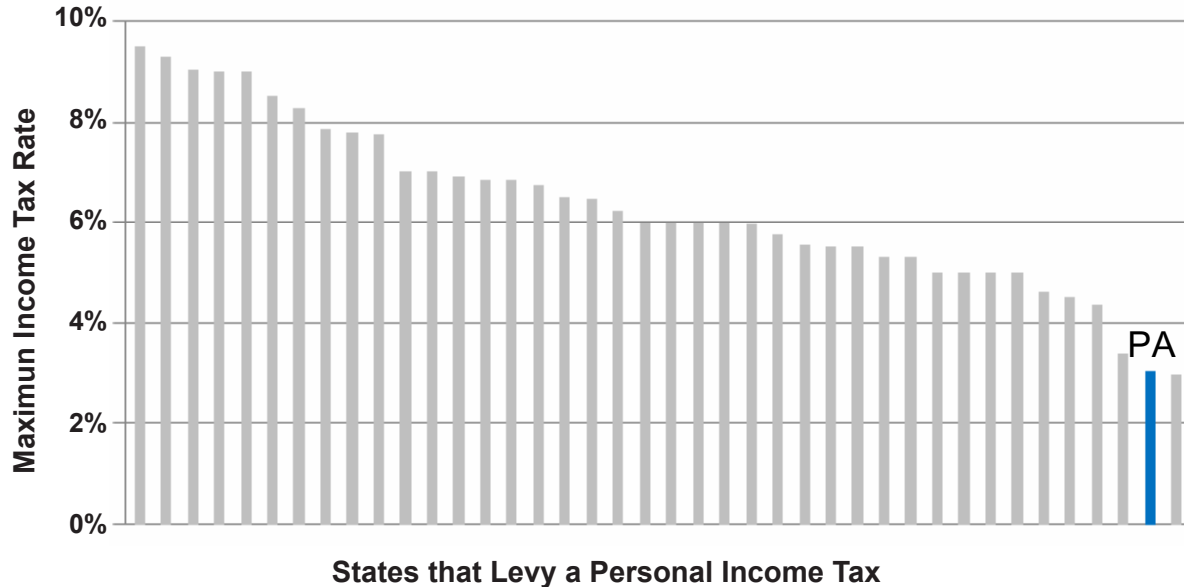
- Successive annual reductions in the Capital Stock and Franchise Tax, saving businesses \$2.9 billion. Businesses will receive an additional \$1.5 billion in Capital Stock and Franchise Tax savings in 2009-10.
- Expanding the cap on Net Operating Losses and increasing the sales factor for Corporate Net Income Tax apportionment, saving businesses \$257 million.
- Expanding Research and Development Tax Credits, saving businesses \$120 million. An additional \$40 million will be saved in 2009-10.
- Expanding the Educational Improvement Tax Credit program, saving businesses \$163 million and promoting expanded educational opportunities for students in the commonwealth. An additional \$45 million will be saved in 2009-10.
- Creating the Keystone Innovation Zone Tax Credits, saving businesses \$56 million. An additional \$25 million will be saved in 2009-10.

Pennsylvania's Personal Income Tax is "One of the Best in the Nation"

With one of the lowest personal income tax rates in the nation – paid both by residents and by more than half of Pennsylvania's businesses – the commonwealth has been able to attract companies and provide state services at a relatively low cost to the taxpayer. At 3.07 percent, the commonwealth's personal income tax rate is the second lowest of the 40 states that levy this tax. Pennsylvania residents pay 11 percent less in per capita

Pennsylvania's Tax Structure

PA's Income Tax is the 2nd Lowest of the 40 States that Levy this Tax



state income taxes than the national average, and less than all of our neighboring states except West Virginia. The commonwealth's low rate led the business-backed Tax Foundation to call Pennsylvania's income tax "one of the best in the nation." In fact, Pennsylvania has the lowest tax rate in the nation of the 42 states that tax pass-through entities. In 2008-09, this equates to \$1.1 billion in savings for these businesses.

Protecting Our Progress

The national recession is hitting Pennsylvania and all other states – requiring difficult budget cuts as well as strategies to enhance revenue. From the time Governor Rendell signed the 2008-09 budget into law in July, he has already made nearly half a billion dollars in budget cuts.

Even with additional cuts to contain the natural growth in the 2009-10 budget, the commonwealth still faces a budget shortfall for the coming fiscal year. While several other states are turning to increases in broad-based taxes to close their budget gaps, Governor Rendell has balanced the budget without such measures. Instead, the 2009-10 budget features a number of new revenue sources in order to avoid draconian service cuts while still keeping the commonwealth competitive, including:

- **Increasing the cigarette tax by 10 cents per pack.** Pennsylvania would join at least four other states in proposing cigarette tax increases. With this change, the commonwealth's cigarette tax would remain in the middle compared to the cigarette tax in our six neighboring states, and Pennsylvania's national ranking among all state cigarette taxes would increase just two spots, surpassing Iowa and Texas.
- **Levying a tax on other tobacco products.** Pennsylvania remains the only state in the nation that does not tax tobacco products such as smokeless tobacco and cigars. The 2009-10 budget would eliminate that anomaly.
- **Ensuring the public benefits from unprecedented natural gas production.** Pennsylvania has immense natural gas reserves – in an area known as the Marcellus Shale – that are now being tapped by private companies. These companies will extract an estimated 57 trillion cubic feet of gas from the Marcellus Shale over the next 25 years, and in the 2009-10 budget Pennsylvania joins the 28 other states that ensure that the public receives a share of the proceeds from the use of these resources.

Pennsylvania's Tax Structure

Tax cuts will save Pennsylvania's businesses and families more than \$8.5 billion from 2005-06 through 2009-10.

Major Tax-Saving Initiatives

Dollars in Millions	<u>2005-06</u>	<u>2006-07</u>	<u>2007-08</u>	<u>2008-09</u>	<u>2009-10</u>
Continued CSFT Phase Out.....	\$ 266.2	\$ 523.4	\$ 868.2	\$1,192.0	\$1,540.2
Special Poverty Expansion (\$500 per dependent).....	13.6	13.3	13.0	12.7	12.4
Research and Development Tax Credit Expansion	15.0	25.0	25.0	40.0	40.0
Sales tax credits (Call Centers).....	30.0	30.0	30.0	30.0	30.0
Sales tax credits (Telecommunications).....	42.6	45.3	48.8	52.6	56.6
Inheritance Tax (recouple to federal return basis).....	140.7	160.7	173.8	186.4	189.6
Educational Improvement Tax Credits.....	19.0	29.0	29.0	29.0	29.0
Keystone Innovation Zone Tax Credits.....	-	6.0	25.0	25.0	25.0
Film Production Tax Credit	10.0	-	40.8	75.0	75.0
Keystone Opportunity Zones	2.9	0.9	0.9	0.9	0.9
Malt Beverage Investment Tax Credit.....	1.2	1.0	1.1	1.1	-
Expansion of Net Operating Loss Cap and Increase Sales Factor	-	35.7	109.1	111.9	110.8
TAP & 529 Plan Contribution Deductions.....	-	16.2	18.7	19.7	20.8
Health Savings Accounts.....	-	2.0	2.5	2.8	2.9
CSFT Exemption for certain Restricted Professional Corporations	-	7.2	6.6	6.0	5.1
SUT Exemption for investment in metal bullion..	-	2.1	2.2	2.4	2.7
CSFT Exclusion increase to \$150,000	-	1.7	5.1	4.5	3.3
Life Valuation Fees	-	1.9	1.9	1.9	1.9
Sub-Chapter S Elections	-	1.1	1.2	1.4	1.6
Agricultural Easement Valuation Reductions.....	-	0.1	0.2	0.2	0.3
Educational Improvement Tax Credits.....	-	-	16.0	16.0	16.0
Bank Shares Tax-Goodwill Deduction	-	-	12.6	14.9	18.5
Resource Enhancement and Protection Tax Credit	-	-	10.0	10.0	10.0
Powdered Metals Exemption.....	-	-	1.9	0.3	0.4
Remanufactured Locomotives Exemption.....	-	-	1.2	1.1	1.1
Alternative Energy Production Credit	-	-	-	5.0	5.0
Volunteer Responder Retention and Recruitment Tax Credit	-	-	-	4.5	-
KOZ Expansion (SUT building exemption/apportionment CNIT/CSFT).....	-	-	-	0.3	1.6
Property Tax Relief	-	-	-	786.0	786.9
Annual Total.....	<u>\$ 541.2</u>	<u>\$ 902.6</u>	<u>\$1,444.9</u>	<u>\$2,633.7</u>	<u>\$2,987.6</u>
Cumulative Total.....	\$ 541.2	\$1,443.8	\$2,888.7	\$5,522.4	\$8,510.0

2009-10 General Fund Revenues

PA Revenue Sources

Dollars in Millions	Actual Collections 2007-08	Estimated Collections 2008-09	Estimated Collections 2009-10
Personal Income Tax	\$10,907.7	\$10,755.8	\$10,754.7
Sales and Use Tax ¹	\$8,496.6	\$8,274.5	\$8,389.6
Corporate Net Income Tax	\$2,417.7	\$2,037.2	\$1,918.8
Capital Stock and Franchise Tax	\$1,019.9	\$801.3	\$578.4
Gross Receipts Tax	\$1,348.9	\$1,444.3	\$1,562.3
Cigarette Tax ²	\$784.1	\$782.1	\$1,035.5
Other Taxes ³	\$2,318.3	\$2,106.9	\$2,213.2
Non-Tax Revenues ⁴	\$634.9	\$456.3	\$861.6
Total	\$27,928.1	\$26,658.4	\$27,314.1
Difference from prior year	\$478.7	\$(1,269.7)	\$655.7
Percentage Difference	1.7%	-4.5%	2.5%

¹ Effective July 1, 2009, the one percent discount for the timely remittance of sales tax collected by licensed vendors is proposed to be eliminated.

² Effective August 1, 2009, an increase in the cigarette tax rate equivalent to \$0.10 per pack of 20 cigarettes is proposed. Additionally, effective July 1, 2009, the 18.52 percent transfer of the cigarette tax to the Health Care Provider Retention Account is proposed to be eliminated.

³ Effective October 1, 2009, a new 5 percent tax on the severance of natural gas within the commonwealth is proposed.

⁴ A transfer of \$174 million from the Oil and Gas Lease Fund is proposed in 2008-09. A transfer of \$350 million from the Health Care Provider Retention Account is proposed in 2009-10.

2009-10 Motor License Fund

INCOME

(Dollars in Millions)



Liquid Fuels Tax — \$1,216

Licenses and Fees — \$877

Turnpike Commission Payment — \$500

Other — \$95

Total Income	\$2,688
Beginning Balance....	52
TOTAL	\$2,740

OUTGO

(Dollars in Millions)



Highways & Bridges — \$1,669

State Police — \$524

Local Subsidy — \$235

Other — \$141

Total Outgo	\$2,722
Ending Balance	18
TOTAL	\$2,740

Licensing & Safety — \$128

Debt Service — \$25

2009-10 General Fund Expenditures

(dollar amounts in thousands)

<u>Department</u>	<u>2007-08 Actual</u>	<u>2008-09 Available</u>	<u>2009-10 Budget</u>
Aging and Long Term Living.....	\$ 850,578 ¹	\$ 1,097,307 ¹	\$ 1,329,733
Agriculture.....	81,206	82,154	68,197
Attorney General.....	93,836	94,509	92,557
Auditor General.....	54,018	54,520	50,996
Civil Service Commission.....	1	1	1
Community & Economic Development.....	623,260	630,017	412,041
Conservation and Natural Resources.....	116,486	120,390	113,482
Corrections.....	1,600,181	1,639,655	1,803,355
Education.....	11,059,668	11,399,759	11,569,037
<i>Basic Education (Pre K-12)</i>	9,327,534	9,645,969	9,911,276
<i>Higher Education</i>	1,604,055 ²	1,624,792 ²	1,536,374 ²
<i>Public Library Subsidy</i>	75,750	75,750	74,000
<i>All Other</i>	52,329	53,248	47,387
Emergency Management and Homeland Security.....	30,776	28,792	15,316
<i>Disaster-Related Funding</i>	12,400	5,950	700
<i>All Other</i>	18,376	22,842	14,616
Environmental Protection.....	222,459	231,046	212,813
Executive Offices.....	258,747	264,123	233,800
Fish and Boat Commission.....	16	17	17
General Services.....	120,515	125,729	127,294
Governor's Office.....	7,559	7,336	7,274
Health.....	297,847	291,892	253,398
Higher Education Assistance Agency.....	451,968	472,873	513,672
Historical & Museum Commission.....	33,865	33,768	26,439
Insurance.....	101,290	124,346	122,944
<i>Children's Health Insurance</i>	65,931	86,900	94,600
<i>All Other</i>	35,359	37,446	28,344
Judiciary.....	299,657	307,141	288,716
Labor & Industry.....	122,775	128,320	105,094
Legislature.....	334,129	332,233	309,293
Lt. Governor's Office.....	1,523	1,579	1,500
Military & Veterans Affairs.....	135,804	130,629	110,381
Probation & Parole Board.....	109,382	114,756	122,714
Public Television Network.....	13,498	12,329	0 ³
Public Welfare.....	8,616,884	9,171,145	9,645,909
<i>Medical Assistance</i>	4,261,598 ⁴	4,550,692 ⁴	4,883,898 ⁴
<i>Mental Health</i>	757,968	781,329	800,436
<i>Mental Retardation</i>	1,105,616	1,180,602	1,253,868
<i>County Child Welfare</i>	994,762	1,053,890	1,062,919
<i>Cash Grants</i>	254,459	266,079	268,579
<i>Child Development</i>	473,989	530,808	537,517
<i>All Other</i>	768,492	807,745	838,692
Revenue.....	187,838	195,877	205,835
Securities Commission.....	2,354	2,265	1,713
State.....	20,571	14,091	11,959
State Employees Retirement System.....	4	4	4
State Police.....	180,882	186,434	194,730
Tax Equalization Board.....	1,519	1,484	1,298
Transportation.....	13,862	13,557	27,941
Treasury.....	923,352	956,452	993,190
<i>General Obligation Debt Service</i>	870,561	904,510	942,939
<i>All Other</i>	52,791	51,942	50,251
TOTAL	\$ 26,968,310	\$ 28,266,930	\$ 28,972,643
Less Projected Current Year Lapses.....		\$ (556,809)	
Less Projected Federal Fiscal Relief Funds:			
Increased Medical Assistance Percentage.....		\$ (1,083,000)	\$ (1,917,000)
State Fiscal Stabilization Fund.....			\$ (493,000)
PROJECTED STATE EXPENDITURES	\$ 26,968,310	\$ 26,627,121	\$ 26,562,643

¹ 2007-08 Actual and 2008-09 Available amounts were appropriated in the Department of Public Welfare. This budget proposes to reorganize the commonwealth's long-term living services within the Department of Aging and Long Term Living.

² Includes the State System of Higher Education.

³ This budget proposes the elimination of the Public Television Network and transfers network infrastructure responsibilities to the Office of Administration.

⁴ Medical Assistance is funded by a variety of state sources and federal funds.

2009-10 General Fund Financial Statement

	Dollars in Millions		
	2007-08 Actual	2008-09 Available	2009-10 Budget
Beginning Balance	\$ 531	\$ 583	\$ 8
Revenues:			
Receipts	\$ 26,878	\$ 27,660	\$ 25,354
Revenue Shortfall .....	.....	- 2,300	.....
Additional Projected Revenue .....	.....	.....	830
Transfer from Oil & Gas Lease Fund .....	.....	174	.....
Prior Year Lapses	142	266 ¹	.....
Funds Available	\$ 27,551	\$ 26,385	\$ 26,192
Expenditures:			
Appropriations	\$ 26,968	\$ 28,267	\$ 28,973
Federal Fiscal Relief .....	.....	- 1,083 ²	- 2,410 ²
Current Year Lapses .....	.....	- 557 ³	.....
Total Expenditures	\$ 26,968	\$ 26,627	\$ 26,563
Preliminary Balance	\$ 583	\$ - 242	\$ - 371
Transfer from Rainy Day Fund .....	.....	250	375
Ending Balance	<u>\$ 583</u>	<u>\$ 8</u>	<u>\$ 4</u>

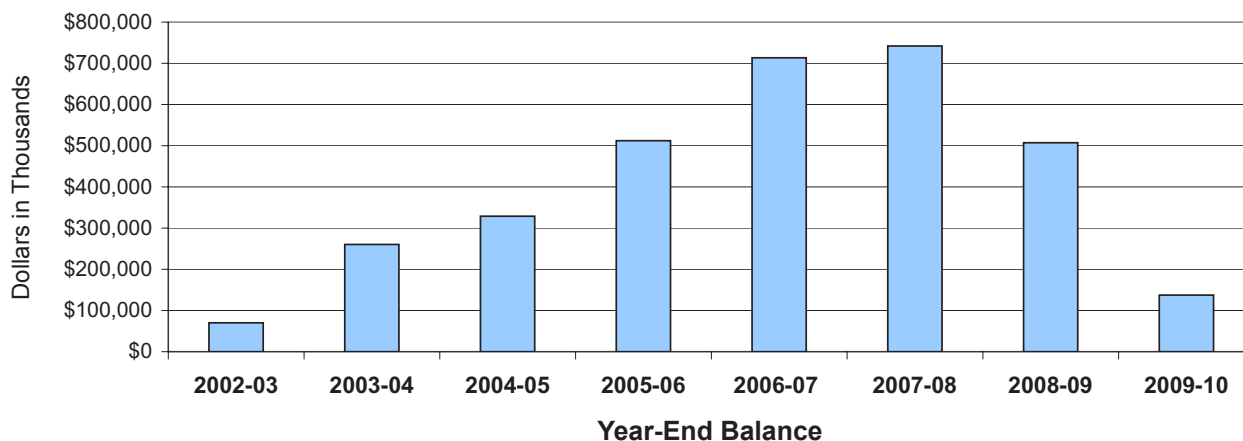
¹ Includes the proposed lapse of \$175 million from prior year appropriations to the Legislature.

² Anticipated Federal Fiscal Relief funds will be appropriated in lieu of state funds for selected programs in this budget.

³ Includes the proposed lapse of \$36 million from current year appropriations to independent agencies.

2009-10 Rainy Day Fund

The current balance in the commonwealth's Rainy Day Fund is \$753 million. This budget proposes transfers from the Rainy Day Fund to the General Fund of \$250 million in 2008-09 and \$375 million in 2009-10.



The Economic Outlook for 2009-10

The recession is expected to continue during 2009

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

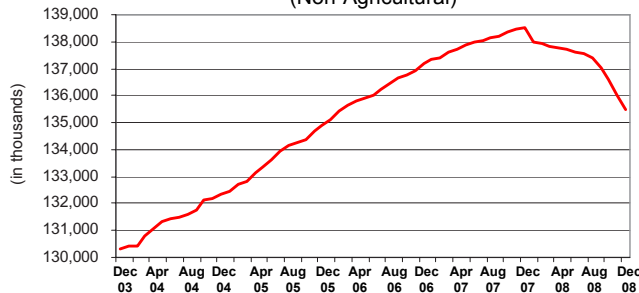
Recent Economic Trends

The U.S. economy entered the current recessionary period in December 2007. The economic slowdown was triggered by a nationwide crash in the housing market, which caused a dramatic tightening of credit. This credit crunch sapped consumer spending power, leading to a rapid decline in consumer consumption. The slowdown in spending and the lack of available credit affected the business community, which responded by laying off workers. At the same time, the crises in housing and credit were quickly reflected in the financial markets, with investors ranging from multi-billion-dollar municipal pension funds to individual workers saving for retirement suffering huge losses in their investment portfolios. This sharp decline in the value of investments further reduced consumer spending, leading to more business closings and more layoffs in many sectors of the economy.

Overall real GDP growth for 2008 is expected to finish just over 1 percent for the year, while real GDP, as measured on a quarterly basis, reveals the sharp reversal the U.S. economy has experienced since the fourth quarter of 2007. The 0.5 percent contraction in the third quarter of 2008 will likely be followed by a 5 percent to 6 percent contraction in the fourth quarter of 2008.

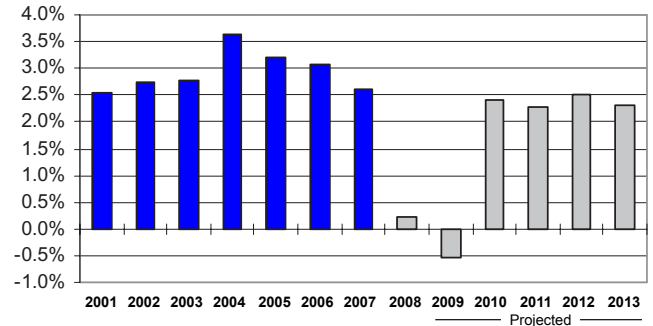
Employment in the United States peaked in December 2007 just as the recession was beginning. During all of 2008, U.S. employers eliminated 2.6 million jobs, cutting 1.9 million in the last four months of the year alone. These staggering job losses pushed the December 2008 U.S. unemployment figure to 7.2 percent, the highest figure since January 1993. Beyond job losses, hours worked are being reduced as well. During December, the average number of hours worked fell to 33.3 hours per week, down two-tenths of an hour to the lowest level since record-keeping for this data began in 1964.

U.S. EMPLOYMENT
(Non-Agricultural)



Job losses, declines in household wealth and tighter credit are just a few of the factors adversely impacting consumer spending. Widely regarded as the main engine of the U.S. economy and accounting for fully two-thirds of GDP, consumer spending has been in a tailspin since the recession deepened in the summer of 2008. It is estimated

REAL PERSONAL CONSUMPTION EXPENDITURES
(Annual Growth)



that households have lost more than \$8 trillion in net worth since the summer of 2007 due to falling home equity and stock prices. These stunning losses account for the large-scale retreat in consumer spending. Consumer spending is expected to be down for the fourth quarter of 2008 as well. December retail sales were down 7.5 percent from the prior year, a foreboding sign. Further, the December decline in retail sales marked the sixth consecutive month of slumping retail sales. Consumer spending has never declined for three consecutive quarters since records were first kept in 1947. Yet, economists now expect the decline in consumer spending to continue during the first quarter of 2009.

In response to this pullback in consumer spending, businesses began to cut back sharply on production. Automobile output is expected to have plunged 60 percent during the fourth quarter of 2008. Exports are also slumping; they are on a path to post their largest quarterly decline in 35 years. The World Bank expects global trade to decline by 2.1 percent in 2009, following a 27-year boom cycle. In fact, the current recession marks the first time in the postwar era that a recession has occurred simultaneously in the U.S., Europe and Japan.

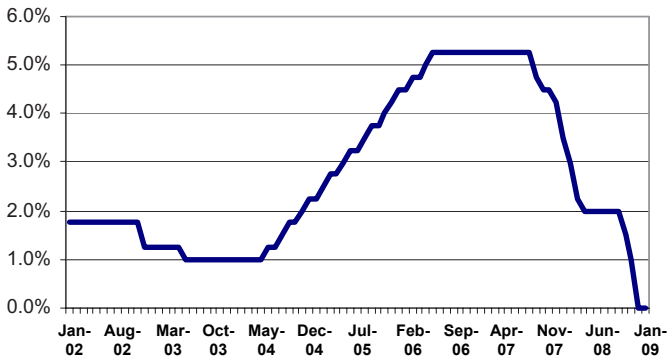
Early data from 2009 shows that the U.S. housing market continues to implode. U.S. Commerce Department data indicates that housing starts fell 16 percent last month to an annual rate of 550,000. This level is the lowest since statistics were first kept in 1945. With excess supply and very weak demand, it is likely that housing starts will remain depressed for several years. During all of 2008, housing starts were down 33 percent from 2007 to 904,300, also the fewest since 1945. Not only are fewer new homes being built, but more people in existing homes are losing their homes. Filings for foreclosures in December 2008 were

The Economic Outlook for 2009-10

41 percent higher than in December 2007. The National Association of Realtors reports that at least 40 percent of the sales of existing homes are attributable to the resale of foreclosed properties.

Monetary policy efforts by the Federal Reserve to date have been aimed at the financial markets generally and the mortgage industry in particular. Reductions to the federal funds rate have been extraordinary in scale and frequency.

FEDERAL FUNDS RATE



The Fed's December 16, 2008 announcement that it was lowering its target federal funds rate to a range of 0.0 percent to 0.25 percent is the lowest in the history of the Federal Reserve, which was founded in 1913. Additionally, the Fed has committed to buy large volumes of "tainted mortgages" in an effort to stabilize the mortgage industry. Such actions have dramatically driven up the Fed's balance sheet, which currently stands at \$2.2 trillion, up from \$900 billion in September 2008. Expectations are that the Fed's balance sheet could reach \$5 trillion by the end of 2009.

Forecast for 2009

Real GDP is expected to have grown at a very subdued rate of 1.2 percent in 2008 – the lowest level of growth since 2001. The economy contracted 0.5 percent in the third quarter of 2008 and expectations are that the fourth quarter contraction in real GDP could reach 5 percent to 6 percent. Similar economic contraction is forecast for the first and second quarters of 2009.

Annual growth in real GDP is projected to be -1.8 percent in 2009, with significant contraction during the first two quarters, followed by minimal positive growth in the last two quarters of 2009. The current forecast anticipates that the recession will deepen and that the economy will experience four straight quarters of negative growth from the fall of 2008 until summer 2009. Additionally, since all of the major economies of the world are simultaneously in a recession for the first time in the postwar period, there are no external forces to support growth. Economic forecasts now project the first decline in real world GDP in the postwar era. Modest

**Change in
Key US Economic Indicators
Annual Percentage Growth***

Indicator	2007	2008p	2009p	2010p
Nominal GDP	4.8	3.5	-0.3	3.4
Real GDP	2.0	1.2	-1.8	2.1
Real Personal Consumption	2.8	0.2	-0.5	2.4
Corporate Profits (After Tax)	2.2	-14.5	1.2	9.2
Unemployment Rate (Rate)	4.6	5.8	8.2	8.6
CPI	3.1	3.7	-1.5	2.4
Federal Funds (Rate)	5.0	2.0	0.1	1.2

* Assumptions in this chart, as well as other assumptions, are incorporated in the 2009-10 fiscal year revenue estimates.

p=projected

growth is forecast for 2010 and beyond, but the economy will strain to get through 2009. The current 13-month-long recession is expected to last up to 24 months, making it the longest recession since the Great Depression and the second longest since 1910.

Declines in housing construction and housing finance led the economy into recession. Until the housing markets stabilize, the depth of the current recession will remain unknown. The economic forecast is for continued weakness in new housing starts through the second quarter of 2009. Total housing starts are expected to bottom out at 604,000 units in 2009, a 33 percent decline from the 2008 level, which was already the worst on record. The rapid decline in housing starts reflects the combination of excess supply in the market, weak demand and a continuation of the credit crunch. The Federal Reserve's action to inject massive amounts of liquidity into the financial system has driven the average 30-year mortgage rate to below 5 percent, but most of the benefit has been attained by those refinancing existing debt rather than by those purchasing new homes. Overall housing prices are expected to continue to decline through the first quarter of 2010.

Real consumer spending is expected to decline for four straight quarters, starting with the third quarter of 2008. Real personal consumption is expected to decline 0.5 percent in 2009. A projected 2.3 percent peak-to-trough drop in real personal consumption is expected. This would be the largest such decline since the 1980 recession. According to economists, any turnaround in consumer spending in the spring of 2009 depends on the enactment of additional fiscal stimuli such as new tax cuts or rebates. In addition, personal income growth is expected to return in 2009, despite rising unemployment. Growth in real personal income is expected to reach 2.3 percent in 2009, up from just 0.6 percent growth in 2008.

The Economic Outlook for 2009-10

The U.S. economy is expected to continue to shed jobs in 2009. Job losses are expected to average around 500,000 monthly in early 2009 before slowing in the latter part of 2009. Total peak-to-trough job losses from December 2007 until 2010 are projected to be 5 million jobs. The U.S. unemployment rate in December 2008 was 7.2 percent; economists estimate it will reach close to 9.0 percent by the end of 2009 before job growth returns in 2010.

The Outlook for Pennsylvania

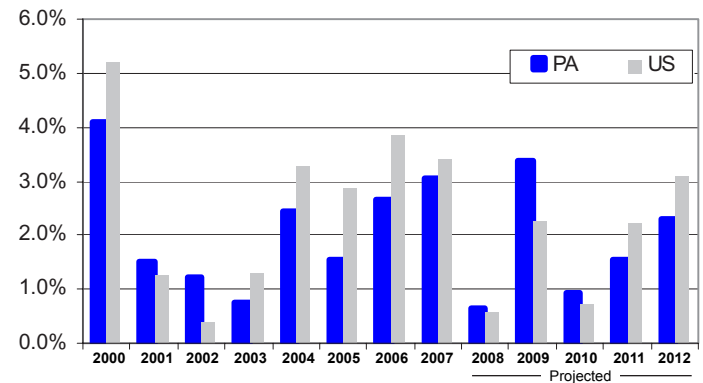
As the U.S. and state economies slowed in late 2007, employment in the commonwealth peaked in January 2008 at 5.811 million non-agricultural jobs. Since December 2007 and the start of the national recession, Pennsylvania has lost 76,200 jobs. Beginning in the fall of 2008, job losses began to accelerate, with 26,000 jobs lost in November and 28,000 jobs lost in December. This reduction in jobs is the largest 12-month drop since the 1991 recession. However, Pennsylvania's 12-month job loss rate of -1.3 percent is still better than the national average of -1.9 percent. In December 2008, the commonwealth's unemployment rate was 6.7 percent, its highest level since March 1994. The national unemployment for December 2008 was 7.2 percent. Pennsylvania's unemployment rate has now been equal to or below the national average for 70 of the past 72 months.

As job losses are expected to continue nationally through 2009, the slower rate of job losses in Pennsylvania is expected to push the commonwealth up to 14th among the 50 states in terms of annual job growth in 2009, according to estimates by IHS Global Insight. Annual employment growth in Pennsylvania is forecast at around -0.5 percent in 2009, while positive job growth is expected to return in 2010 at a rate of 0.6 percent annually. Slightly more robust job growth is forecast for the commonwealth after that, with growth of 1.1 percent in 2011 and 1.3 percent in 2012. As the national economy begins to recover in 2010, the rate of job growth in Pennsylvania is expected to again lag behind the national average from 2010 through 2012.

Housing construction continued to slow in Pennsylvania in 2008, down from a high of 45,000 new units in 2005 to just under 25,000 units in 2008. Economic forecasts project that housing starts will fall another 12 percent in 2009. Sales of new and existing homes also declined by 24 percent during 2008.

The inverse relationship of the national and the commonwealth's growth in personal income has re-emerged during the current recession. As the recession of 2008 took hold and deepened, the rate of growth in real personal income plunged for the nation as a whole, as it did for the commonwealth. However, the decline in the rate of growth was less severe for Pennsylvania than

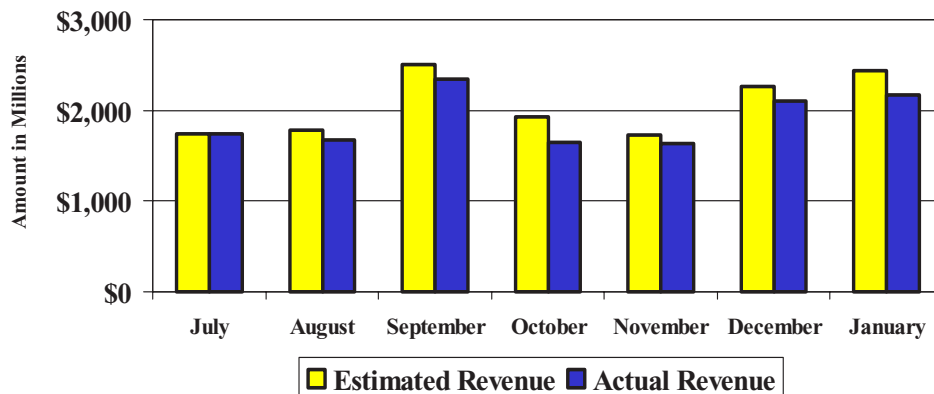
PA and U.S. Real Personal Income
(Annual Growth)



for the nation as a whole. Economists expect that the rate of growth in real personal income for Pennsylvanians will exceed the national average through 2010. This strong performance is partially the result of the diversification of the Pennsylvania economy and a stronger state labor market. Growth in less recession-prone industries such as health care, pharmaceuticals, education and government have aided the commonwealth.

2008-09 General Fund Revenues

Estimated versus Actual Revenue Collections



After the first seven months of the 2008-09 fiscal year, revenue collections were \$1.076 billion lower than estimated (down 7.5 percent).

2009-10 Capital Budget

	<u>Millions</u>
<u>From Bond Funds</u>	
Conservation and Natural Resources.....	\$ 102.3
Corrections	28.7
Education.....	108.5
General Services.....	58.2
Historical and Museum Commission	60.6
Military and Veterans Affairs	46.3
Public Welfare	25.0
State Police	13.9
Transportation-Local Transportation Assistance	123.7
Subtotal Bond Funds.....	<u>\$ 567.1</u>
<u>From Current Revenues</u>	
Conservation and Natural Resources.....	\$ 63.4
Subtotal Current Revenues	<u>\$ 63.4</u>
TOTAL CAPITAL PROJECTS TO BE AUTHORIZED	<u><u>\$ 630.7</u></u>

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

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.

General Services

Provides for the construction, renovation and improvements to state office buildings and facilities.

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.

Military and Veterans Affairs

Provides for land acquisition, renovations, additions and replacement at the state armories and veterans' homes. Also may include original furniture and equipment authorizations.

Public Welfare

Provides for construction and renovation of patient buildings, support facilities and utilities at the state institutions for individuals with mental illness and mental retardation, restoration centers and youth development centers.

State Police

Provides for renovation, expansion and construction of troop headquarters/station facilities and driver examination facilities.

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.