

II. REVENUE FORECAST

A. 2007-09 General Fund Revenues

The forecast for General Fund revenues for the 2007-09 biennium is \$12,731.6 million, a decrease of \$165.9 million from the September 2008 forecast. The decrease is concentrated in personal income taxes and is the result of the expectation of the current economic slowdown being more severe than previously anticipated. Corporate income tax receipts have weathered the storm a little longer than expected and corporate balance sheets are expected to remain relatively strong, though a decrease in corporate income tax collections is still expected. The protracted slowdown will push receipts sharply downward relative to the September forecast in the 2009-11 biennium. Including the beginning balance of \$1,436.7 million, total available resources amount to \$13,806.8 million, a decline of \$166.1 million from the Close of Session forecast.

The December projections result in a negative ending balance of \$142.1 million for the 2007-09 biennium. Table B.1 in Appendix B presents detailed revenue information for the 2007-09 biennium.

The latest revenue forecast for the current biennium represents the most probable outcome given available information. OEA feels that it is important that anyone using this forecast for decision-making purposes recognize the potential for actual revenues to depart significantly from this projection. Actual revenues are likely to fall within 2.1 percent of the forecast produced at this point in the biennium, and are highly unlikely to deviate more than 4.2 percent. Table R.1 presents the December forecast for the 2007-09 biennium, including guidelines for budgetary purposes. Section D discusses explicit risks that might cause actual revenues to differ substantially from the forecast.

Table R.1

2007-09 General Fund Forecast Summary

(Millions)	2007 COS Forecast	September 2008 Forecast	December 2008 Forecast	Change from Prior Forecast	Change from COS Forecast
Beginning Balance	\$1,513.0	\$1,436.7	\$1,436.7	\$0.0	-\$76.3
Structural Revenues					
Personal Income Tax	\$12,347.9	\$12,227.3	\$12,066.7	-\$160.6	-\$281.2
Corporate Income Tax	\$920.9	\$857.3	\$857.3	\$0.0	-\$63.6
All Other Revenues	\$888.5	\$897.1	\$891.8	-\$5.3	\$3.2
Gross GF Revenues	\$14,157.3	\$13,981.7	\$13,815.8	-\$165.9	-\$341.6
Total Kicker Refunds/Credits	-\$1,164.7	-\$1,084.2	-\$1,084.2	\$0.0	\$80.5
Net GF Revenues	\$12,992.6	\$12,897.5	\$12,731.6	-\$165.9	-\$261.1
Administrative Actions ¹	-\$57.3	-\$42.1	-\$42.1	\$0.0	\$15.2
Legislative Actions ²	-\$309.4	-\$319.3	-\$319.3	\$0.0	-\$9.9
Net Available Resources	\$14,138.9	\$13,972.8	\$13,806.8	-\$165.9	-\$332.1
Confidence Intervals					
67% Confidence	+/- 2.1%		\$267.4	\$12.46B to \$13.00B	
95% Confidence	+/- 4.2%		\$534.7	\$12.20B to \$13.27B	

1 Reflects cost of cashflow management actions, exclusive of internal borrowing.

2. Equals portion of 2005-07 corporate surplus designated for Rainy Day Fund.

Personal Income Tax

Personal income tax collections totaled \$1,222.5 million for the first quarter of fiscal year 2009, \$23.4 million below the latest forecast. Withholding receipts of \$979.8 million came in ahead of forecast by \$4.3 million. Withholding receipts are expected to wane through the end of 2009 as the recession dampens wage pressures and reduces employment.

Estimated payments equal to \$264.4 million were \$9.4 million below forecast. Compared to the year-ago level, estimated payments were up 5.5 percent. Final payments fell \$14.8 million short of expectations, though more than 22 percent higher than a year ago. Though the quarter is a relatively slow quarter in terms of total revenue collections, refunds bounced back, rising 29 percent from a year ago. Table B.8 in Appendix B presents a comparison of actual and projected personal income tax revenues for the fourth quarter of fiscal year 2008.

The forecast for total personal income tax receipts during the current biennium is \$12,006.7 million, a decrease of \$160.6 million from the prior forecast. The revision reflects the expectation that the current weak economic conditions will be both deeper and longer than previously anticipated. The result is a sharp decrease in receipts – \$711 million – relative to the September forecast in the 2009-11 biennium.

Corporate Income Tax

Corporate income taxes equaled \$96 million for the first quarter of fiscal year 2009, \$17.9 million below the September forecast. Quarterly advanced payments were \$100.6 million for the quarter, \$12 million below forecast. Payments accompanying a filed tax return totaled \$23.5 million, exceeding the latest forecast by \$0.3 million. Refunds totaled \$28.1 million, \$6.2 million more than forecasted. On a year-over-year basis, corporate receipts were off 18.3 percent. Table B.8 in Appendix B presents a comparison of actual and projected corporate income tax revenues for the first quarter of fiscal year 2009.

The forecast for corporate tax collections has not materially changed from September. In spite of the recent economic troubles, the expectations for corporate profits on a national level has not changed. The forecast for the 2007-09 biennium is \$857.3 million. It should also be noted that the forecast for the subsequent 2009-11 biennium is \$62.1 million lower than that for 2007-09 reflecting the overall weakening in the economy. Corporate income taxes are \$63.6 million below the Close of Session forecast.

Non-income Tax Sources of Revenue

All other revenues will total \$891.8 million for the biennium, a decrease of \$5.3 million from the prior forecast. The only significant changes were slight reductions in the forecasts for insurance taxes and criminal fines and assessments. All other revisions are negligible.

B. Extended General Fund Revenue Outlook

Table R.2 exhibits the long-run forecast for General Fund revenues through the 2013-15 biennium. Total structural General Fund revenues will increase 6.8 percent to \$14,749.4 million in 2009-11. Personal income tax growth of 19.3 percent, which will raise collections to \$13,104.8 million, is due largely to the \$1.084 billion kicker rebate distributed in the prior biennium. In addition, the sunset of the Bush tax cuts in 2011 are expected to have a short-run positive impact on personal income taxes, particularly through capital gains realizations. Corporate income taxes will decline 7.2 percent to \$795.2 million, as the economic slowdown in 2008 and 2009 filters through to corporate income tax receipts. All other revenues will reach \$849.4 million, mildly below the prior biennium's level.

General Fund revenues will total \$16,955.7 million in 2011-13, an increase of 15 percent from the prior period. The growth is fueled primarily by a 15.2 percent increase in personal income tax collections to \$15,099.8 million. Corporate income taxes will reach \$981.1 million, while all other revenues will total \$874.7 million.

Table R.2

General Fund Revenue Forecast Summary (Millions of Dollars, Current Law)

Revenue Source	Forecast 2005-07		Forecast 2007-09		Forecast 2009-11		Forecast 2011-13		Forecast 2013-15	
	Biennium	% Chg	Biennium	% Chg	Biennium	% Chg	Biennium	% Chg	Biennium	% Chg
Personal Income Taxes	11,040.3	22.8%	10,982.5	-0.5%	13,104.8	19.3%	15,099.8	15.2%	17,437.0	15.5%
Corporate Income Taxes	844.1	31.7%	857.3	1.6%	795.2	-7.2%	981.1	23.4%	1,027.9	4.8%
All Others	857.6	6.4%	891.8	4.0%	849.4	-4.8%	874.7	3.0%	901.0	3.0%
Total General Fund	12,742.0	22.1%	12,731.6	-0.1%	14,749.4	15.8%	16,955.7	15.0%	19,365.8	14.2%
<i>Kicker Distributions</i>	-		1,084.2		-		-		-	
Total Revenue	12,742.0	22.1%	13,815.8	8.4%	14,749.4	6.8%	16,955.7	15.0%	19,365.8	14.2%

Other taxes include General Fund portions of the Eastern Oregon Severance Tax, Western Oregon Severance Tax and Amusement Device Tax. Commercial Fish Licenses & Fees and Pari-mutual Receipts are included in Other Revenues

For the 2013-15 biennium, General Fund revenues will equal \$19,365.8 million, a 14.2 percent increase from the prior biennium. Personal income tax collections rise 15.5 percent to \$17,437 million, as income growth returns to long-term trends. Corporate income taxes will experience modest 4.8 percent growth, just eclipsing the billion dollar mark for the first time. Remaining sources of revenue will equal \$901 million, a three percent increase over the prior biennium. Table B.2 in Appendix B presents a more detailed look at the long-term General Fund revenue forecast.

C. Tax Law Assumptions

The revenue forecast is based on existing law, including actions signed into law during the 2007 Oregon Legislative Session and recent federal legislation. OEA makes routine adjustments to the forecast to account for legislative and other actions not factored into the personal and corporate income tax models. These adjustments can include expected kicker refunds, when applicable, as well as any tax law changes not yet present in the historical data. A summary of these items can be found in Appendix B Table B.3b.

A rough rule of thumb for personal income tax is that nearly all collections activity on a given tax year occurs between the start of the tax year and June of the following year. Modest payment and refund activity continues for years thereafter, but with only a marginal net impact on revenues. Therefore, when interpreting the timing of personal income tax impacts presented in Appendix B Table B.3, this 18-month window is suitable for all but the most technical purposes.

Corporate income tax is more difficult in that corporations do not have a standardized tax year. A corporate tax year is signified by the calendar year in which the corporation's fiscal year begins. The rule of thumb is that the majority of corporate collections on a given tax year will be received in the State fiscal year that begins July 1 of that year, i.e. the corporate tax impact specified in Appendix B Table B.3 for tax year 2007 will be realized primarily in state fiscal year 2007-08. Contact the Office of Economic Analysis at (503) 378-3455 with questions regarding tax law impacts.

D. Forecast Risks

The revenue forecast presented herein constitutes a guideline for budgetary purposes. Variation above or below this forecast is to be expected, although OEA strives to minimize the magnitude of this variation by investigating new data resources and methodological approaches, as well as regularly consulting with experts from the economics, financial, and accounting communities.

The following are major factors that could cause actual revenues to deviate from this forecast by a significant degree:

- *Personal income tax is expected to account for nearly ninety percent of General Fund revenues in the 2007-09 biennium and beyond.* The income tax forecast is based on OEA's outlook regarding general economic conditions. To the extent that actual economic performance departs from this outlook, particularly with respect to factors that influence more volatile forms of non-wage income, so too will the personal income tax, and thus the General Fund forecast. It should also be noted that current conditions will manifest themselves over the next 12 months as taxpayers reconcile differences in withholding and estimated payments compared to taxes owed through final payments and refunds.
- *Capital gains income is highly volatile.* Large swings in the markets on nearly a daily basis make it difficult to gauge an already volatile income source. This is pertinent to Oregon because of its impact on personal income taxes which amounts to a significant

driver in terms of the fluctuation of income tax receipts. Furthermore, financial decisions on the part of a few individuals can have a significant impact on the aggregate levels. The concentration of gains at the high end of the income distribution exacerbates the inherent volatility in this source of income.

- *Numerous changes have been made to Oregon's corporate income tax code in recent years.* The most significant is in how multi-state corporations apportion federal taxable income to compute income taxable in Oregon. As of tax year 2006, apportionment is based solely of the fraction of a corporation's sales that occur in Oregon. While payment and refund activity related to tax year 2006 continues, the approximate impact of the change is evident. More recently, the weak dollar has allowed for strong export growth in the face of tough economic time domestically.
- *Growth in revenues is partly due to inflation.* Wage inflation contributes to rising wage and salary income, and consequently personal income tax collections. Price inflation raises gross corporate revenues and, potentially, corporate income tax revenue. Rental and small business income exhibit similar growth factors. The magnitude of actual revenue growth will depend on actual inflation rates. Currently, OEA expects inflation to come down from its current levels for the coming years, contributing to slower than expected revenue growth compared to that experienced in the previous two decades. Should inflation be stronger than expected, revenue growth could also exceed forecast.
- *Unexpected changes in the impact of tax expenditures.* Tax expenditures such as credits and deductions reduce tax revenue. In some cases, estimates of the usage and tax impact vary widely, thus making it is difficult to know the amount of tax reduction. Increased usage of such provisions would reduce revenues relative to this forecast.

E. Lottery Earnings Forecast

Table R.3 presents a summary of lottery earnings and distribution for the 2007-09 biennium. Projected lottery earnings will total \$1,324 million, a decrease of \$17.7 million from the prior forecast. Overall consumer spending has stalled, driving down expectations for lottery sales through the remainder of this biennium. Including the beginning balance and other earnings, total available resources equal \$1,402.1 million. Total projected resources have increased \$9.9 million from the Close of 2007 Session.

During the Special Session in February 2008, the legislature increased the lottery fund allocation to the State School Fund by \$20.0 million. Increased earnings resulted in a \$3.0 million rise in dedicated distributions, including the Education Stability Fund and County Economic Development programs. The current forecast for the ending balance in the Economic Development Fund is \$3.3 million.

The December forecast continues to incorporate the expected impact from statewide smoking restrictions that was articulated in the September forecast. These restrictions go into effect

Table R.3**2007-09 Lottery Fund Forecast Summary**

	Close of 2007 Session	September 2008 Forecast	December 2008 Forecast	Changes from:	
				September 2008 Forecast	Close of 2007 Session
Transfers of Lottery Earnings					
Traditional Games	\$129.3	\$133.5	\$132.6	-\$0.9	\$3.3
Video Lottery	\$1,151.9	\$1,133.5	\$1,116.5	-\$17.0	-\$35.4
Administrative Savings	\$35.0	\$74.7	\$74.9	\$0.2	\$39.9
Total Transfers	\$1,316.1	\$1,341.7	\$1,324.0	-\$17.7	\$7.8
Economic Development Fund					
Beginning Balance	\$66.3	\$64.1	\$64.1	\$0.0	-\$2.2
Transfers from Lottery	\$1,316.1	\$1,341.7	\$1,324.0	-\$17.7	\$7.8
Other earnings ¹	\$9.8	\$14.1	\$14.1	\$0.0	\$4.3
Total Available Resources	\$1,392.2	\$1,419.9	\$1,402.1	-\$17.7	\$9.9
Dedicated Distributions ²	\$675.4	\$682.3	\$675.1	-\$7.1	-\$0.2
Other Legislatively Adopted Allocations	\$703.7	\$723.7	\$723.7	\$0.0	\$20.0
Total Distributions	\$1,379.0	\$1,406.0	\$1,398.8	-\$7.1	\$19.8
Ending Balance	\$13.2	\$13.9	\$3.3	-\$10.6	-\$9.9

Footnotes:

1. Includes interest earnings and reversions.

2. Includes the Education Stability Fund (18%), the Parks and Natural Resources Fund (15%), and Debt Service. See Table B.9 for more information.

January 1, 2009. While expectations regarding the magnitude of this impact range wildly, the Legislative Revenue Office (LRO) concluded that there would be at least a short-term loss in video lottery sales. This is consistent with various academic and economic studies regarding the impacts of smoking restrictions on gaming sales. OEA will evaluate the actual impact of the smoking restrictions as soon as data become available.

The extended outlook for lottery earnings can be found in Table B.9 in Appendix B. It is critical to note that the earnings reflected in Table B.9 include a transfer rate pertaining to video lottery of 65.1 percent as opposed to the 62.4 percent rate. The Lottery will apply this transfer rate on sales beginning July 1, 2009. Additionally, anticipated long term growth rates for lottery sales were reduced to reflect long-term expectations for consumption. Lottery earnings are expected to fall one percent to \$1,311 million for the 2009-11 biennium. In addition to the expected impact of the smoking restrictions, the weak growth is the result of an absence of administrative savings for the biennium, compared with \$74.9 million in the current biennium. Buoyed by the increased transfer rate, video lottery earnings will increase six percent, while traditional products will decline four percent. Total available resources will amount to \$1,317.1 million.

Lottery earnings will amount to \$1,430.4 million in 2011-13, a 9.1 percent increase over the previous biennium. Including interest earnings, available resources will total \$1,436.4 million. For the 2013-15 biennium, lottery earnings will climb to \$1,564.9 million while available resources will equal \$1,570.9 million.

F. Overview of Budgetary Reserves

The state currently administers two general reserve accounts, the Oregon Rainy Day Fund (ORDF) and the Education Stability Fund (ESF). This section updates balances and the recalculates the outlook for these funds based on the September revenue forecast.

Oregon Rainy Day Fund

Established by the 2007 Legislature, the ORDF is funded from ending balances each biennium, up to one percent of appropriations. The Legislature can deposit additional funds, as it did in first populating the ORDF with surplus corporate income tax revenues from the 2005-07 biennium. The ORDF also retains interest earnings. Withdrawals from the ORDF require one of three triggers, including a decline in employment, a projected budgetary shortfall, or declaration of a state of emergency, plus a three-fifths vote. Withdrawals are capped at two-thirds of the balance as of the beginning of the biennium in question. Fund balances are capped at 7.5 percent of General Fund revenues in the prior biennium.

Education Stability Fund

The ESF gained its current reserve structure and mechanics via constitutional amendment in 2002. The ESF receives 18 percent of lottery earnings¹, deposited on a quarterly basis. The ESF does not retain interest earnings. The ESF has similar triggers as the ORDF (in fact, the ORDF was modeled on the ESF), but does not have the two-thirds cap on withdrawals. The ESF balance is capped at five percent of General Fund revenues collected in the prior biennium.

Budgetary Reserve Outlook

Table R.4 presents current and projected balances for the ORDF and ESF. As of the fourth quarter of fiscal year 2008, the balance in the ORDF equaled \$330.7 million. As indicated above, none of this balance is available this biennium without additional legislation. The ORDF is projected to reach \$340.5 million by the end of 2007-09, and to total \$366.2 million by the end of next biennium.

The ESF balance stood at \$291.7 million as of June 30th, with the full amount available to the legislature if economic and fiscal conditions are met. The projected ending balance in the ESF for the current biennium is \$393.4 million. By the end of the 2009-11 biennium, available ESF funds will total \$550.5 million. Table B.10 in Appendix B provides detailed information for Oregon's budgetary reserves.

¹ Ten percent of these transfers are deposited to the Oregon Growth sub-account. Due to the illiquid nature of this sub-account, only funds in the main account are included in the figures presented here.

Table R.4**Oregon's Budgetary Reserves**

(Millions)	Actuals through 6/31/2008	2007-09 Biennium	2009-11 Biennium
Rainy Day Fund			
Beginning Balance	\$0.0	\$0.0	\$340.5
Deposits	\$319.3	\$319.3	\$0.0
Interest	\$11.4	\$21.2	\$25.8
Triggered Withdrawals	\$0.0	\$0.0	\$0.0
Ending Balance¹	\$330.7	\$340.5	\$366.2
Education Stability Fund			
Beginning Balance	\$178.9	\$178.9	\$393.4
Deposits	\$112.1	\$214.5	\$157.1
Interest ²	\$10.3	\$17.9	\$35.9
Triggered Withdrawals	-\$9.6	-\$17.9	-\$35.9
Ending Balance	\$291.7	\$393.4	\$550.5
Total Reserves	\$622.4	\$733.9	\$916.7

Footnotes:

1. Under current law, only 2/3rds of the beginning balance is available for withdrawal. Withdrawal subject to economic and financial triggers.
2. Education Stability Fund interest is distributed to the Oregon Education Fund (75%) and the State Scholarship Commission (25%).