



**REPORT ON KEY ISSUES FROM THE
HOUSE APPROPRIATIONS COMMITTEE**

BUDGET DAY BRIEFING

DWIGHT EVANS, DEMOCRATIC CHAIRMAN

February 16, 2007

The Commonwealth Checkbook

Governor Rendell's proposed 2007/08 operating budget for the Commonwealth totals \$59.09 billion. This includes the State General Fund, Federal Funds, the Motor License Fund, and other Special Funds, such as the Lottery Fund and Tobacco Settlement Fund and other non-state revenues.

The state General Fund is the focus of this briefing. A separate briefing will address the Tobacco Settlement Fund.

The 2007/08 state General Fund budget reflects:

- \$27.28 billion in total state money available to spend in 2007/08, an increase of nearly \$913 million or 3.5% from the \$26.37 million available in 2006/07.
- \$27.27 billion in total state spending in 2007/08, an increase of nearly \$948 million or 3.6% from the \$26.32 billion in 2006/07.

At the close of the 2006/07 budget year, the Governor's budget estimates that nearly \$12.5 million will be transferred to the Rainy Day Fund bringing the 2007/08 balance to \$563 million.

General Fund State Deposits

The total amount of state money available to spend each fiscal year includes deposits received in the current year, plus the balance carried over from the immediate prior year and unspent money from previous budgets. The bulk of deposits is the state taxes collected by the Commonwealth during the fiscal year, with fees and other non-tax revenue (such as Liquor Store profits) comprising the remainder of annual deposits. Each year the Commonwealth sets aside a portion of current deposits to cover refunds owed to taxpayers for overpayment of state taxes. This so-called, "refund reserve" reduces the amount of deposits that are available for the Commonwealth to spend.

For 2007/08, total state money available to spend in the General fund budget is \$27.28 billion. Deposits collected by the Commonwealth are expected to total \$28.39 billion. Approximately \$1.15 billion will be reserved to cover any tax refunds.

The Rendell Administration has revised the official estimate for 2006/07 annual deposits by \$66.7 million. This is a modest revision considering that the year-to-date overage through January stands at nearly \$100 million. The Administration's revision leaves room for further upward adjustment after receipts are tallied for March and April, the two most important (and largest) months for tax collections. If General Fund revenues – especially Personal Income and Corporation Tax collections – continue to perform as they have in recent months, 2006/07 could end with a larger surplus which, in turn, will translate into a higher revenue estimate for 2007/08. While we anticipate a larger surplus, we do not expect the good fortune experienced last year when the revenue surplus exceeded \$800 million.

For 2007/08, the Administration projects revenue growth of \$1.526 billion over the revised 2006/07 projections, representing 5.7% growth. As detailed below, 2007/08 revenues reflect nearly \$922 million in revenue modifications. These modifications include a change in the Sales and Use tax rate, an increase in the Cigarette tax and the creation of a new tax on other tobacco products.

Modifications that effect current programs:

- A proposal to increase the current Sales and Use Tax rate by one percentage point, from six to seven percent. This proposal, excluding the \$420 million dedicated to Property Tax Relief, is expected to generate approximately \$826 million in 2007/08.
- A proposal to increase various fees within the Department of Environmental Protection,

effective July 1, 2007. This proposal is estimated to generate \$9.156 million.

- A proposal to increase the Educational Improvement Tax Credit by \$1.4 million, which would take effect July 1, 2007. Currently, the maximum amount of the credit is \$54 million; the Governor's proposal would take the total amount of credits awarded to \$55.4 million.
- The Capital Stock and Franchise Tax rate continues to decline. Effective January 1, 2007 the rate decreased one mill to 3.89 mills. This decrease translates to nearly \$190 million in unavailable revenue for 2007/08.¹
- The Solid Waste disposal fee increases by \$2.75 to \$7.00. \$2.25 of the \$2.75 is dedicated to the Hazardous Sites Cleanup Fund generating \$37.7 million. Fifty cents of the \$2.75 is directed to the Environmental Stewardship Fund, generating \$8.4 million to help pay Growing Greener II debt service. The current amount of \$4.25 supports Environmental Stewardship Fund activities. The above amounts do not include the Act 101 \$2 recycling fee, which is not included in the 2007/08 proposal.
- A proposed compliance initiative designed to focus on the use of abusive tax shelters. This initiative is expected to generate \$10 million.

Modifications that effect new programs:

- The Systems Benefit Charge is a new 1/20th of a cent charge per kilowatt hour on electric power sold to residential, commercial and industrial customers. This revenue stream will be securitized to pay the debt service on bonds issued by the Pennsylvania Energy Development Authority (PEDA). The bond proceeds will pay for the proposed Energy Independence Fund programs.

Modifications that effect Rx/Prescription for PA:

- A proposal to increase the Cigarette tax by ten cents that will help pay for some of the cost associated with the proposed health care plan. Currently, the tax rate is \$1.35 per

pack; this increase is estimated to generate \$49.7 million.

- The creation of a new tax on other tobacco products, namely smokeless tobacco, cigars and cigarillos, and loose tobacco. The rate would equal 36 cents per ounce for smokeless and loose tobacco and the equivalent of 36 cents per ten sticks of cigars and cigarillos. The proposed tax would be effective August 1, 2007 and is expected to generate \$27.8 million in 2007/08.

Modifications that effect Transportation:

- The proposal creates the Oil Company Gross Profits Tax. The proposed tax uses a combined reporting method, in which each firm's total profits are examined, and the portion of those profits that can be attributed to activity in Pennsylvania are subject to Pennsylvania tax. The new tax would be taxing gross profits instead of net income. If enacted, the tax rate would be 6.17%, and corporations subject to this tax would not be subject to the 9.99% Corporate Net Income tax (CNI). This proposal is expected to generate a net revenue increase of \$760 million.²

General Fund State Expenditures

The 2007/08 state General Fund budget request is \$27.27 billion, nearly \$948 million or 3.6% above the current year budget which includes a proposed supplemental appropriation of \$211.6 million. This \$948 million includes \$21.3 million of spending for the new **Prescription for Pennsylvania** initiative. Not including the Corrections department, the total complement for all agencies declined by 395 positions. Most of the \$211.6 million supplemental request for 2006/07 is for the Department of Public Welfare (\$201 million) and the Department of Education (\$4.5 million). The Governor is requesting supplemental state funds for DPW so that the Department can make all payments owed to Medical Assistance providers in 2006/07, including June 2007 payments. By using current year revenue to pay the providers, the Governor is preserving the Rainy Day Fund.

For 2007/08, the agencies slated to receive additional state funds are led by the Department of Education (\$544 million), followed by the Department of Public Welfare (\$367 million) and Corrections (\$185 million).

¹ This \$190 million is not included in the Governor's total proposed General Fund tax and revenue modifications number.

² This \$760 million is not included in the Governor's total proposed General Fund tax and revenue modifications number.

PENNSYLVANIA'S GENERAL FUND CHECKBOOK		
<i>(\$ Millions)</i>		
	2006/07	2007/08
BEGINNING BALANCE	\$514.1	\$37.5
STATE DEPOSITS:		
Total Deposits	26,951.2	28,392.4
Less: Refund Reserves	(1,100.0)	(1,150.0)
Total State Money Available	\$26,366.8	\$27,279.8
STATE EXPENSES:		
Anticipated Expenses	(26,115.2)	27,274.7
Unanticipated Expenses	(211.6)	0.0
Less: Spending Freezes	10.0	0.0
Total State Expenses	(\$26,316.8)	(\$27,274.7)
Preliminary Balance	50.0	5.1
Less: Transfer to Rainy Day	(12.5)	(1.3)
ENDING BALANCE	\$37.5	\$3.8

Part of the Department of Education's budget reflects an increase of \$80 million because the employer contribution rate for the PA School Employee Retirement System increased for 2007/08 to 7.13% from 6.46% of payroll. There is also a \$23.8 million increase in the Treasury department. The increase in Treasury is driven by a \$24.5 million increase in General Obligation Debt Service.

The 2007/08 DPW budget includes \$155 million additional state spending for disability programs, including mental retardation programs (\$91 million), mental health services (\$30 million), and services for persons with physical disabilities (\$34 million). Other DPW program areas budgeted to receive significant increases are child care support for the children of TANF and former TANF recipients (\$53 million), early intervention programs (\$14 million), child care services for non-TANF low-income families (\$43 million), and child welfare services (\$64 million). State spending for the Medical Assistance (MA) program increases by only \$50 million. This is because the Governor is proposing savings initiatives and alternative funding sources as a means to reduce the state General Funds that otherwise would be needed for the MA program. Without these budgetary measures, our preliminary estimate for state MA funding would have to increase by an additional \$774 million above the Governor's 2007/08 request. More detail on DPW's budget will be forthcoming in other **Budget Briefings**.

The Governor's budget has proposed a substantial increase to the basic education subsidy for 2007/08, increasing by 3.5% or \$166.7 million, for a total of

\$4.95 billion. The appropriation for special education increases by three percent for a total of \$1.01 billion. For the 2007/08 budget, the Governor requested an increase of \$100 million for a total of \$350 million for the Accountability Block Grants program. Early Intervention, designed for children aged three to five, would receive an increase of \$29 million for a total of \$173.1 million, under the Governor's proposal. *Science: It's Elementary* program, would receive a \$5 million increase for a total of \$15 million. *Classrooms for the Future* is set to receive a \$70 million increase for a total of \$90 million in 2007/08.

Higher Education funding breaks down this way: a 3.5% increase for community colleges and the State System of Higher Education; a two percent increase for the four state-related universities: Penn State, Pitt, Temple and Lincoln. Total funding for higher education in the Governor's proposal is \$1.55 billion.

The Department of Corrections is budgeted to receive an increase of \$185 million to address the continued growth in the offender population. This population has risen 13 percent since 2003/2004, from 40,187 to 45,596. In just one year, between December 2005 and December 2006, the state prison population rose by five percent.

To address this overpopulation, the Governor is proposing to reopen State Correctional Institution (SCI) Pittsburgh at a cost of \$32 million. SCI Pittsburgh closed in January 2005. The reopening would allow the Department of Corrections to house an additional 750 inmates, and would provide the capacity for as many as 1,500 inmates. Three hundred seventy four additional jobs will be created to staff the reopened institution. In addition to the reopening of SCI Pittsburgh, the proposed budget would add beds at several other institutions, providing the capacity to accommodate an additional 1,500 inmates.

QUESTIONS AND COMMENTS
717-783-1540

Miriam A. Fox, Executive Director
mfox@hacd.net
Stephanie Puglia, Budget Analyst
Barbara Fellencer, Communications Director
<http://www.hacd.net>