

II. REVENUE FORECAST

A. 2007-09 General Fund Revenues

The forecast for General Fund revenues for the 2007-09 biennium is \$12,897.5 million, a decrease of \$119.2 million from the June 2008 forecast. The relatively small decrease (approximately one percent) is the result of the expectation of the current economic slowdown extending well into 2009, rather than turning around earlier in the year. Corporate income tax receipts have weathered the storm a little longer than expected and thus will be higher in the current biennium than previously forecast. However, the protracted slowdown will push receipts lower than the June forecast in the 2009-11 biennium. Including the beginning balance of \$1,436.7 million, total available resources amount to \$13,972.8 million, a decline of \$166.1 million from the Close of Session forecast.

The projected ending balance for 2007-09 equals \$23.8 million, \$119.2 million below the June 2008 forecast. 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 2.4 percent of the forecast produced at this point in the biennium, and are highly unlikely to deviate more than 4.8 percent.

Table R.1

2007-09 General Fund Forecast Summary

(Millions)	2007 COS Forecast	June 2008 Forecast	September 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	\$12,388.8	\$12,227.3	-\$161.5	-\$120.6
Corporate Income Tax	\$920.9	\$808.3	\$857.3	\$49.0	-\$63.6
All Other Revenues	\$888.5	\$903.8	\$897.1	-\$6.7	\$8.6
Gross GF Revenues	\$14,157.3	\$14,100.9	\$13,981.7	-\$119.2	-\$175.7
Total Kicker Refunds/Credits	-\$1,164.7	-\$1,084.2	-\$1,084.2	\$0.0	\$80.5
Net GF Revenues	\$12,992.6	\$13,016.7	\$12,897.5	-\$119.2	-\$95.2
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	\$14,091.9	\$13,972.8	-\$119.2	-\$166.1
Confidence Intervals					
67% Confidence	+/- 2.4%		\$309.5	\$12.59B to \$13.21B	
95% Confidence	+/- 4.8%		\$619.1	\$12.28B to \$13.52B	

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

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

Table R.1 presents the September 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.

Personal Income Tax

Personal income tax collections totaled \$2,473.6 million for the fourth quarter of fiscal year 2008, \$35.5 million below the latest forecast. Withholding receipts of \$1,300.7 million fell short of forecast by \$8.6 million. Withholding receipts are expected to wane during the remainder of 2008 and into 2009, though not nearly as dramatically as was experienced in 2002 and 2003.

Estimated payments equal to \$399.5 million were \$17.4 million above forecast. Compared to the year-ago level, estimated payments were up 10 percent. Final payments fell \$27.1 million short of expectations, though are nearly 25 percent higher than a year ago. Refunds were projected to come in lower due to changes in the withholding tables. Although refunds were down 12.3 percent compared to the prior year level, the quarterly refunds were \$25 million more than expected. 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 \$12,227.3 million, a decrease of \$161.5 million from the prior forecast. The revision reflects the expectation that the current weak economic conditions will extend into 2009. Furthermore, this forecast assumes a slower immediate recovery with faster growth in the out-years of the forecast. The result is a decrease in receipts relative to the June forecast in both the current and 2009-11 biennia.

Corporate Income Tax

Corporate income taxes equaled \$168 million for the fourth quarter of fiscal year 2008, \$7.8 million above the June forecast. Quarterly advanced payments were \$155.3 million for the quarter, \$4.4 million below forecast. Payments accompanying a filed tax return totaled \$52.1 million, exceeding the latest forecast by \$11 million. Refunds tracked very close to expectations with \$39.4 million, \$1.2 million less than forecasted. On a year-over-year basis, corporate receipts were off 5.7 percent. Table B.8 in Appendix B presents a comparison of actual and projected corporate income tax revenues for the third quarter of fiscal year 2008.

The forecast for corporate tax collections for the 2007-09 biennium is \$857.3 million, a increase of \$49 million from the June 2008 forecast. The increase is the result of several factors, most notably the strong market for exports. It should also be noted that the forecast for the subsequent 2009-11 biennium was reduced significantly to reflect differing expectations with respect to the timing of the impact of the economic downturn on corporate income tax receipts. Corporate income taxes are \$63.6 million below the Close of Session forecast.

Non-income Tax Sources of Revenue

All other revenues will total \$897.1 million for the biennium, a decrease of \$6.7 million from the prior forecast. Estate taxes continue to exceed historical trends, although this source exhibits considerable volatility. This was offset by reductions in the forecast for cigarette taxes and insurance taxes. 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 General Fund revenues will increase 19.9 percent to \$15,467.8 million in 2009-11. Personal income tax growth of 24 percent, which will raise collections to 13,815.8 million, is due in part 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 \$856.8 million, mildly below the prior biennium's level.

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%	11,143.1	0.9%	13,815.8	24.0%	15,908.5	15.1%	18,122.5	13.9%
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%	897.1	4.6%	856.8	-4.5%	878.4	2.5%	905.7	3.1%
Total General Fund	12,742.0	22.1%	12,897.5	1.2%	15,467.8	19.9%	17,768.0	14.9%	20,056.1	12.9%

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

General Fund revenues will total \$17,768.0 million in 2011-13, an increase of 14.9 percent from the prior period. The growth is fueled primarily by a 15.1 percent increase in personal income tax collections to \$15,908.5 million. Corporate income taxes will reach \$981.1 million, while all other revenues will total \$878.4 million.

For the 2013-15 biennium, General Fund revenues will equal \$20,056.1 million, a 12.9 percent increase from the prior biennium. Personal income tax collections rise 13.9 percent to \$18,122.5 million, driven by broad-based gains in both wage and non-wage incomes. 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 \$905.7 million, a 3.1 percent increase over the prior biennium. Table B.2 in Appendix 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.

Beginning with the May 2003 forecast, OEA altered the manner in which it factors tax law changes into the revenue forecast. In the past, legislative impact estimates were characterized at the point of collections. However, tax laws are directly related to tax liability for given tax years. In fact, the original tax law impacts developed by the Legislative Revenue Office are characterized at the point of liability and irrespective of the timing of receipt. Given the focus on taxable income and liability in the personal and corporate income tax models, incorporating tax law changes as adjustments to the liability forecast proved far easier to administer and more intuitively accessible.

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.
- *Measure 59.* Ballot measure 59 would make federal income taxes fully deductible for Oregon personal income taxes. Passage and implementation of this measure would significantly reduce personal income tax receipts for the state relative to the 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 \$1,341.7 million, an increase of \$2.3 million from the prior forecast. The gain was driven entirely by increased expectations for administrative savings, which offset a slight structural decrease, as well as a downward adjustment related to smoking restrictions which go into effect January 1, 2009. Including the beginning balance and other earnings, total available resources equal \$1,419.9 million. Total projected resources have increased \$27.6 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 \$13.9 million.

An addition to the September forecast is the impact of smoking restrictions that go into effect 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

Table R.3

2007-09 Lottery Fund Forecast Summary

	Close of 2007 Session	June 2008 Forecast	September 2008 Forecast	Changes from:	
				June 2008 Forecast	Close of 2007 Session
Transfers of Lottery Earnings					
Traditional Games	\$129.3	\$134.9	\$133.5	-\$1.3	\$4.2
Video Lottery	\$1,151.9	\$1,143.6	\$1,133.5	-\$10.1	-\$18.4
Administrative Savings	\$35.0	\$60.9	\$74.7	\$13.8	\$39.7
Total Transfers	\$1,316.1	\$1,339.3	\$1,341.7	\$2.3	\$25.5
Economic Development Fund					
Beginning Balance	\$66.3	\$64.1	\$64.1	\$0.0	-\$2.2
Transfers from Lottery	\$1,316.1	\$1,339.3	\$1,341.7	\$2.3	\$25.5
Other earnings ¹	\$9.8	\$14.1	\$14.1	\$0.0	\$4.3
Total Available Resources	\$1,392.2	\$1,417.5	\$1,419.9	\$2.3	\$27.6
Dedicated Distributions ²	\$675.4	\$682.2	\$682.3	\$0.1	\$6.9
Other Legislatively Adopted Allocations	\$703.7	\$723.7	\$723.7	\$0.0	\$20.0
Total Distributions	\$1,379.0	\$1,405.8	\$1,406.0	\$0.1	\$26.9
Ending Balance	\$13.2	\$11.7	\$13.9	\$2.2	\$0.7

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.

impacts of smoking restrictions on gaming sales. OEA will continue to have ongoing discussions with LRO and the Lottery as to the appropriate level of decrease that is included in the forecast.

Based on existing research, as well as discussions with the LRO and the Lottery, OEA feels that a six percent decline in video lottery sales from what would otherwise be forecasted can be expected during the first quarter of 2009, with lesser declines beginning in the second quarter as retailers adjust to the new restrictions. Finally, we expect that video lottery sales will return largely to the historical trend by the second half of 2009 at a level one percent below the expected level of sales absent the smoking restrictions. This results in a relative decrease in earnings of approximately \$9 million for the 2007-09 biennium, and \$15 million in the 2009-11 biennium.

The extended outlook for lottery earnings can be found in Table B.9 in Appendix B. Lottery earnings are expected to grow 0.1 percent to \$1,342.4 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 \$74.7 million in the current

biennium. Video lottery earnings will increase 7 percent, while traditional products will decline slightly. Total available resources will amount to \$1,360.8 million.

Lottery earnings will amount to \$1,516.1 million in 2011-13, a 12.9 percent increase over the previous biennium. Including interest earnings, available resources will total \$1,522.1 million. For the 2013-15 biennium, lottery earnings will climb to \$1,691.9 million while available resources will equal \$1,697.9 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 \$340.6 million by the end of 2007-09, and to total \$391.8 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 \$396.2 million. By the end of the 2009-11 biennium, available ESF

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.

funds will total \$556.3 million. Table B.10 in Appendix B provides detailed information for Oregon's budgetary reserves.

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	\$340.6
Deposits	\$319.3	\$319.3	\$23.8
Interest	\$11.4	\$21.3	\$27.4
Triggered Withdrawals	\$0.0	\$0.0	\$0.0
Ending Balance¹	\$330.7	\$340.6	\$391.8
Education Stability Fund			
Beginning Balance	\$178.9	\$178.9	\$396.2
Deposits	\$112.1	\$217.4	\$160.1
Interest ²	\$10.3	\$24.7	\$51.7
Triggered Withdrawals	-\$9.6	-\$24.7	-\$51.7
Ending Balance	\$291.7	\$396.2	\$556.3
Total Reserves	\$622.4	\$736.9	\$948.1

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%).