II. REVENUE FORECAST

A. 2007-09 General Fund Revenues

The forecast for General Fund revenues for the 2007-09 biennium is $11,757.9 million, a decrease of $260.6 million from the March 2009 forecast. The decrease is concentrated in personal income taxes, as expectations for income tax receipts related to both capital gains and business income continued to slide rapidly through April. Corporate income tax receipts have exhibited similar weakness. Including the beginning balance of $1,436.7 million, total available resources amount to $12,833.2 million, a decline of $1,305.7 million from the Close of Session forecast.

After adjustments for several new laws related to expenditure cuts and revenue increases, the May projections result in a negative ending balance of $351.3 million for the 2007-09 biennium. Table B.1 in Appendix B presents detailed revenue information for the 2007-09 biennium.

The protracted slowdown will push still further downward relative to the March forecast in the 2009-11 biennium. The forecast for total General Fund revenue during 2009-11 was reduced by $532.5 million relative to March.

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

Table R.1

2007-09 General Fund Forecast Summary

(Millions)	2007 COS Forecast	March 2009 Forecast	May 2009 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	$11,456.4	$11,190.1	-$266.3	-$1,157.8
Corporate Income Tax	$920.9	$748.8	$686.7	-$62.1	-$234.2
All Other Revenues	$888.5	$897.5	$965.3	$67.8	$76.8
Gross GF Revenues	$14,157.3	$13,102.7	$12,842.1	-$260.6	-$1,315.2
Total Kicker Refunds/Credits	-$1,164.7	-$1,084.2	-$1,084.2	$0.0	$80.5
Net GF Revenues	$12,992.6	$12,018.5	$11,757.9	-$260.6	-$1,234.7
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	$13,093.8	$12,833.2	-$260.6	-$1,305.7
Confidence Intervals					
67% Confidence	+/- **1.5%**		**$176.4**	**$11.58B to $11.93B**	
95% Confidence	+/- **3.0%**		**$352.7**	**$11.41B to $12.11B**	

1 Reflects cost of cashflow management actions, exclusive of internal borrowing.
2. Equals portion of 2005-07 corporate surplus designated for Rainy Day Fund.

projection. Tables R.1 present the May forecast for the 2007-09 and 2009-11 biennia, 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 $1,002.7 million for the third quarter of fiscal year 2009, $59.8 million below the latest forecast. Withholding receipts of $1,129 million fell short of forecast by $65 million. Estimated payments equal to $217.3 million were $30.3 million above forecast. Compared to the year-ago level, estimated payments were down 22.8 percent. For both withholding and estimated payments, these rates of decline are the largest quarterly year-over-year decreases since at least 1993 (records reflect data from 1994 forward).

Final payments exceeded forecast by $9.7 million, while refunds were $34.8 million more than expected. Refunds were up 14.8 percent over the prior year level, in part a product of processing efficiencies at the Department of Revenue accelerating the paying of refunds through the tax season.

The forecast for total personal income tax receipts during the current biennium is $11,190 million, a decrease of $266.3 million from the prior forecast. This reflects an adjustment for the weaker-than-expected final payments in April, as well as the lower expectations for withholding receipts due to the severe job losses that have characterized early 2009. We further expect that the current weak economic conditions will be both deeper and longer than previously anticipated. The effect on tax receipts will be exacerbated by somewhat limited growth in FY 2011 as the economy slowly recovers. The result is a decrease in receipts – $406.9 million – relative to the March forecast in the 2009-11 biennium.

Corporate Income Tax

Corporate income taxes equaled $18.6 million for the third quarter of fiscal year 2009, a shortfall of $0.5 million relative to the March forecast. The third fiscal quarter is a low volume quarter in terms of collections, and is thus subject to significant fluctuations in percentage terms. On a year-over-year basis, corporate receipts were down 70.4 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 2009.

Following expectations that corporate profits will be severely limited in the near future, the forecast for corporate tax collections has been decreased significantly in the near term. The forecast for the 2007-09 biennium is $686.7 million, a decrease of $62.1 million from the March forecast. Meanwhile, the forecast for the subsequent 2009-11 biennium is $117.4 million lower than was anticipated in March.

Non-income Tax Sources of Revenue

All other revenues will total $965.3 million for the biennium, an increase of $70 million from the prior forecast. Other than a significant increase due to one-time transfers associated with the passage of Senate Bill 581, the only significant changes were slight decreases in the forecasts for interest earnings and miscellaneous revenues.

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 decrease 2.5 percent to $12,517.5 million in 2009-11. This represents a $532.5 million decrease relative to the March forecast. Personal income tax growth of 9.1 percent, which will raise collections to $11,022.9 million, is due entirely to the $1.084 billion kicker rebate distributed in the prior biennium – factoring the kicker out results in a modest decline in personal income tax revenue in 2009-11 relative to 2007-09. Corporate income taxes will decline 11.2 percent to $609.7 million, as the economic slowdown in 2008 and 2009 filters through to corporate income tax receipts. All other revenues will reach $884.9 million, mildly below the prior biennium's level. It should be noted that these figures include $62 million in positive indirect impacts resulting from the federal stimulus package enacted on February 18, 2009.

General Fund revenues will total $15,028.8 million in 2011-13, an increase of 20.1 percent from the prior period. The growth is fueled primarily by a 21.1 percent increase in personal income

Table R.2

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

Revenue Source	Forecast 2005-07 Biennium	% Chg	Forecast 2007-09 Biennium	% Chg	Forecast 2009-11 Biennium	% Chg	Forecast 2011-13 Biennium	% Chg	Forecast 2013-15 Biennium	% Chg
Personal Income Taxes	11,040.3	22.8%	10,105.9	-8.5%	11,022.9	9.1%	13,349.5	21.1%	15,876.9	18.9%
Corporate Income Taxes	844.1	31.7%	686.7	-18.6%	609.7	-11.2%	804.9	32.0%	904.6	12.4%
All Others	857.6	6.4%	965.3	12.6%	884.9	-8.3%	874.4	-1.2%	915.6	4.7%
Total General Fund	12,742.0	22.1%	11,757.9	-7.7%	12,517.5	6.5%	15,028.8	20.1%	17,697.2	17.8%
Kicker Distributions	-		*1,084.2*		-		-		-	
Total Revenue	12,742.0	22.1%	12,842.1	0.8%	12,517.5	-2.5%	15,028.8	20.1%	17,697.2	17.8%

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

tax collections to $13,349.5 million. Corporate income taxes will reach $804.9 million, while all other revenues will total $884.9 million.

For the 2013-15 biennium, General Fund revenues will equal $17,697.2 million, a 17.8 percent increase from the prior biennium. Personal income tax collections will rise 18.9 percent to

$15,876.9 million, as income growth returns to long-term trends. Corporate income taxes will experience modest 12.4 percent growth to $904.6 million. Remaining sources of revenue will equal $915.6 million, a 4.7 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 2009 Oregon Legislative Session and indirect impacts resulting from 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.3.

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 and business-related income are highly volatile*. Capital gains income exceeded 10 percent of income for the first time in the 2007 tax year. This exposure contributes to the volatility in personal income taxes because the financial decisions on the part of a relatively 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.

- *The timing and nature of an economic recovery.* Historically, economic recoveries would suggest that there will be significant increases in income tax revenue beginning in either FY 2011 or FY 2012. This forecast assumes that the vast majority of any recovery would occur in the 2011-13 biennium. However, should the recovery come earlier, or be significantly weaker than previous upturns, the forecast errors could be significant.

- *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 $1,326.9 million, an increase of $9.7 million from the prior forecast. Though coming in slightly ahead of the March forecast, the dramatic decline in lottery sales through the winter has continued, with weekly video lottery sales down more than 20 percent on a year-over-year basis. Including the beginning balance and other earnings, total available resources equal $1,400.2 million. Total projected resources have increased $8 million from the Close of 2007 Session.

Despite a historic decline in sales, the current forecast for the ending balance in the Economic Development Fund is $0.4 million. This occurs because the Lottery has transferred an additional $102.7 million in administrative savings during the biennium. Furthermore, the implementation of the Raffle added roughly $800,000 to the last transfer for this biennium.

The May forecast continues to incorporate the expected impact from statewide smoking restrictions that was articulated in the September forecast. These restrictions went 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

Table R.3

2007-09 Lottery Fund Forecast Summary

	Close of 2007 Session	March 2009 Forecast	May 2009 Forecast	Changes from: March 2009 Forecast	Changes from: Close of 2007 Session
Transfers of Lottery Earnings					
Traditional Games	$129.3	$132.7	$132.2	-$0.5	$2.9
Video Lottery	$1,151.9	$1,087.5	$1,091.2	$3.7	-$60.6
Administrative Savings[1]	$35.0	$97.0	$103.5	$6.5	$68.5
Total Transfers	$1,316.1	$1,317.2	$1,326.9	$9.7	$10.7
Economic Development Fund					
Beginning Balance	$66.3	$64.1	$64.1	$0.0	-$2.2
Transfers from Lottery	$1,316.1	$1,317.2	$1,326.9	$9.7	$10.7
Other earnings[2]	$9.8	$14.1	$9.3	-$4.8	-$0.5
Total Available Resources	$1,392.2	$1,395.3	$1,400.2	$4.9	$8.0
Dedicated Distributions[3]	$675.4	$671.3	$667.0	-$4.3	-$8.4
Other Legislatively Adopted Allocations	$703.7	$723.7	$732.9	$9.2	$29.2
Total Distributions	$1,379.0	$1,395.0	$1,399.9	$4.9	$20.8
Ending Balance	$13.2	$0.4	$0.4	$0.0	-$12.8

Footnotes:
1. Includes a transfer of $800,000 related to the Lottery Raffle. 2. Includes interest earnings and reversions.
3. Includes the Education Stability Fund (18%), the Parks and Natural Resources Fund (15%), and Debt Service. See Table B.9 for more information.

video lottery sales. Though there is only a limited amount of data, thus far it does appear as though the actual impact is perhaps slightly higher than expected. Furthermore, it should be noted that it is difficult to draw significant conclusions as to the magnitude of the smoking restriction impact compared to that from the economic recession. OEA will continue to evaluate the actual impact of the smoking restrictions as more 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. Lottery earnings are expected to fall 14.3 percent to $1,137.1 million for the 2009-11 biennium. In addition to the expected impact of the smoking restrictions and slow economic growth, the weak growth is the result of an absence of administrative savings for the biennium, compared with $102.7 million in the current biennium. In spite of the increased transfer rate, video lottery earnings will decrease 7.1 percent, while traditional products will decline 7 percent. Not including any administrative savings that may accrue during the biennium, total available resources will amount to $1,141.8 million.

Lottery earnings will amount to $1,253.8 million in 2011-13, a 10.3 percent increase over the previous biennium. Including interest earnings, available resources will total $1,259.8 million. For the 2013-15 biennium, lottery earnings will climb to $1,371.6 million while available resources will equal $1,377.6 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 May 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 earnings[4], 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. Should no withdrawals be made from the ESF, it is expected that the five percent cap would be reached late in the 2009-11 biennium. At that point, funding of the ESF stops and instead 15 percent of lottery earnings will flow to a school capital matching account.

Table R.4

Oregon's Budgetary Reserves

(Millions)	Actuals through 3/1/2009	2007-09 Biennium	2009-11 Biennium
Rainy Day Fund			
Beginning Balance	$0.0	$0.0	$337.9
Deposits	$319.3	$319.3	$0.0
Interest	$17.4	$18.6	$27.0
Triggered Withdrawals	$0.0	$0.0	$0.0
Ending Balance[1]	$336.7	$337.9	$364.9
Education Stability Fund			
Beginning Balance	$178.9	$178.9	$394.0
Deposits	$215.0	$215.0	$112.1
Interest[2]	$16.2	$17.4	$18.9
Triggered Withdrawals	-$16.0	-$17.3	-$18.9
Ending Balance	$394.0	$394.0	$506.1
Total Reserves	$730.7	$731.9	$871.0

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%).

Budgetary Reserve Outlook

Table R.4 presents current and projected balances for the ORDF and ESF. As of the third quarter of fiscal year 2009, the balance in the ORDF equaled $336.7 million. As indicated above, none of this balance is available this biennium without additional legislation. The ORDF is projected

[4] 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.

to reach $337.9 million by the end of 2007-09, and to total $364.9 million by the end of next biennium.

At the end of March 2009, the ESF balance stood at $394.0 million with the full amount available to the legislature if economic and fiscal conditions are met. Assuming no distributions are made during the next biennium, by the end of 2009-11, available ESF funds will total $506.1 million. Table B.10 in Appendix B provides detailed information for Oregon's budgetary reserves.