II. REVENUE FORECAST

A. 2009-11 General Fund Revenues

The forecast for General Fund revenues for 2009-11 is $13,210.3 million. This represents a decrease of $182.8 million from the December 2009 forecast. The forecast for the 2009-11 biennium is now $365.4 below the Close of Session forecast. On net, nearly all of the decrease for the March forecast is associated with lower expectations for personal income taxes, particularly in the remainder of the current fiscal year. In spite of increased expectations for corporate income taxes, the remainder of the changes to the forecast were offset by increases in the expectations for the amount of income tax credits to be claimed under the Business Energy Tax Credit (BETC) program. The expected ending balance is now a negative $106.3 million. Total available resources amount to $13,194.6 million. Table B.1 in Appendix B presents detailed revenue information for the 2009-11 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. Table R.1 presents the March forecast for the 2009-11 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

2009-11 General Fund Forecast Summary

(Millions)	2009 COS Forecast	December 2009 Forecast	March 2010 Forecast	Change from Prior Forecast	Change from COS Forecast
Structural Revenues					
Personal Income Tax	$11,545.7	$11,403.6	$11,219.9	-$183.7	-$325.8
Corporate Income Tax	$831.6	$822.4	$837.1	$14.7	$5.5
All Other Revenues	$1,198.4	$1,167.0	$1,153.2	-$13.8	-$45.1
Gross GF Revenues	$13,575.7	$13,393.1	$13,210.3	-$182.8	-$365.4
Administrative Actions[1]	-$43.7	-$15.7	-$15.7	$0.0	$28.0
Legislative Actions	$0.0	$0.0	$0.0	$0.0	$0.0
Net Available Resources	$13,532.0	$13,377.4	$13,194.6	-$182.8	-$337.4
Confidence Intervals					
67% Confidence	**+/- 6.1%**		**$805.8**	**$12.40B to $14.02B**	
95% Confidence	**+/- 12.2%**		**$1,611.7**	**$11.60B to $14.82B**	

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

Appendix Table B.8 compares the past quarter receipts with what was forecasted, as well as with what happened a year prior. *It is critical to note that the December forecast contained expected receipts from the tax measures passed in the 2009 Legislative Session and subsequently referred to, and affirmed by, voters. Therefore, the result of the election merely served to avoid a removal of $727 million relative to December.*

Personal Income Tax

Personal income tax collections totaled $1,201.7 million for the second quarter of fiscal year 2010, $23.4 million below the latest forecast. Withholding receipts of $1,151.7 million came in ahead of forecast by $8.4 million. Estimated payments equal to $161.8 million were $45 million below forecast. Compared to the year-ago level, estimated payments were down 7.5 percent.

Final payments exceeded forecast by $2.6 million, while refunds were $10.6 million less than expected. The second quarter declines relative to year ago figures were relatively mild compared to the previous several quarters – though this is largely due to the weakness that began in the second quarter of fiscal year 2009. Table B.8 in Appendix B presents a comparison of actual and projected personal income tax revenues for the second quarter of fiscal year 2010.

The forecast for total personal income tax receipts during the current biennium was decreased $183.7 million from the December forecast. This reflects an adjustment resulting from the especially weak estimated payments seen in December and January. It is important to note the relative magnitude of the change may appear larger because we are still very early in the biennium. Also, contributing to the downturn in the forecast for personal income taxes were increased estimates for the amount of credits that will be claimed under the BETC program. As a result, relatively minor changes can grow as the change flows through the expectations for the next 17 months.

Corporate Income Tax

Corporate income taxes equaled $50.6 million for the second quarter of fiscal year 2010, $7.5 million higher than December forecast. On a year-over-year basis, corporate receipts were up for the first time since March 2008. Also, of note, preliminary receipts in January far outpaced expectations. Table B.8 in Appendix B presents a comparison of actual and projected corporate income tax revenues for the second quarter of fiscal year 2010.

Over the last several months, the expectation for corporate income taxes, particularly in the near-term, has slowly been increasing. Similarly, the earnings and profitability announcements from large corporations have been more balanced. Though we do not believe that the increases seen over the last four months are indicative of a boom in corporate income tax collections, it is significant enough to raise our expectations for collections over the near term. More than offsetting the increased estimates for credits claimed under the BETC program, the forecast for corporate income tax collections was increased $14.7 million for the current biennium.

Non-income Tax Sources of Revenue

All other revenues will total $1,153.2 million for the biennium, a decrease of $13.8 million from the prior forecast. Generally, changes to forecasts from these revenue sources in this category served to offset each other, with the most significant changes between increases in cigarette taxes and declines in miscellaneous revenue, interest income, and insurance taxes.

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 13.8 percent to $15,036 million in 2011-13. Lower expectations for wage growth and increased expectations for credits claimed through the BETC program led to a decrease of $412.3 million relative to the December forecast. Personal income tax growth of 17.2 percent will raise collections to $13,151.4 million. The full realization of the corporate income tax changes passed during the 2009 legislative session and subsequently passed by voters will push corporate income tax collections up 12.5 percent to $1,058.4 million. All other revenues will reach $942.5 million.

General Fund revenues will total $17,476.5 million in 2013-15, an increase of 16.2 percent from the prior period, and a $521.9 million below the December forecast, as changes made to the forecast for 2011-13 proliferate through the forecast period. The growth is fueled primarily by a 17.1 percent increase in personal income tax collections to $15,405.4 million. Corporate income taxes will reach $1,085.4 million, while all other revenues will total $985.7 million. Table B.2 in Appendix presents a more detailed look at the long-term General Fund revenue forecast.

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%	10,090.6	-8.6%	11,219.9	11.2%	13,151.4	17.2%	15,405.4	17.1%
Corporate Income Taxes	844.1	31.7%	684.5	-18.9%	837.1	22.3%	942.1	12.5%	1,085.4	15.2%
All Others	857.6	6.4%	948.6	10.6%	1,153.2	21.6%	942.5	-18.3%	985.7	4.6%
Total General Fund	12,742.0	22.1%	11,723.6	-8.0%	13,210.3	12.7%	15,036.0	13.8%	17,476.5	16.2%
Kicker Distributions	-		*1,084.2*		-		-		-	
Total Revenue	12,742.0	22.1%	12,807.9	0.5%	13,210.3	3.1%	15,036.0	13.8%	17,476.5	16.2%

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

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.

In addition, Appendix B Table B.3A summarizes revenue changes associated with actions taken during the 2009 Legislative Session. The totals presented in the table were added to the forecast for structural revenue growth in order to arrive at the total revenue numbers presented in this document.

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:

- *Increased Volatility.* With the passage of Measure 66, the state has increased the volatility of its personal income tax revenue stream. In past years, the relatively small number of taxpayers impacted by the measure – two to three percent – regularly accounted for two-thirds of the change in tax revenues from one year to the next. By increasing the dependence on this small group, relatively small changes in the economy can yield large changes in income tax collections. Essentially, the state can expect to experience greater positive revenue changes in good years and greater losses in revenue in bad years relative to the past.

- *Magnitude and Effectiveness of Federal Government Policy.* Throughout the last year, the federal government has increased their role in injecting stimulus into the economy at unprecedented levels. To the extent that impacts of these, or any new, policies deviate from expectation pose a risk to a variety of Oregon's revenue streams.

- *Taxpayer response to tax policy.* While we do not expect a sharp deviation from prior behavior related to the passage of Measure 66 and 67, there are several outstanding tax policy issues that increase risk in the forecast in both directions. For tax year 2010, the federal government has eliminated the income restriction on converting conventional Individual Retirement Accounts (IRA) to Roth IRAs. If taxpayers choose to convert these accounts, they can choose to pay taxes for tax year 2010 or spread the liability to 2011 and 2012. The extent that wealthier taxpayers take advantage of this opportunity represents an upside risk to the forecast, in particular because they could choose to pay all of the income taxes based on 2010 income in order to avoid expected marginal tax rate increases in 2011.

  The popularity of Oregon's Business Energy Tax Credit has left the state with a substantial amount of credits that will serve to reduce revenues into the future. Because the credits can be redeemed, sold, or held, it is somewhat unclear when the credits will be claimed. The risk relates to the extent that the actual accumulation and redemption of credits deviates from what is expected.

  Finally, the federal government may raise marginal tax rates for high income taxpayers beginning in 2011. We are expecting some increase in collections related to people taking capital gains in 2010 to avoid paying on the higher tax rate. However, it is unclear how widespread this will be. We believe that this is generally an upside risk to the forecast for 2011.

- *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. For example, in tax year 2008, capital gains were over 60 percent *less* than 2007.

- *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.

- *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 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 2009-11 biennium. Projected lottery earnings will total $1,071.7 million, a decrease of $9.5 million from the prior forecast. The typical seasonal behavior of video lottery receipts (e.g., receipts in the winter months tend to be higher than in the summer) has not been seen in the current cycle, as January receipts closely resembled those seen last July. Including the beginning balance and other earnings, total available resources equal $1,073.8 million.

After adjusting for programs that receive a strict percentage of lottery transfers, the current forecast for the ending balance in the Economic Development Fund is a negative $33.6 million.

Table R.3

2009-11 Lottery Fund Forecast Summary

	December 2009 Forecast	March 2010 Forecast	Changes from: December 2009 Forecast
Transfers of Lottery Earnings			
Traditional Games	$125.5	$125.9	$0.5
Video Lottery	$950.4	$936.4	-$14.0
Administrative Savings	$5.4	$9.4	$4.0
Total Transfers	$1,081.2	$1,071.7	-$9.5
Economic Development Fund			
Beginning Balance	$1.4	$1.4	$0.0
Transfers from Lottery	$1,081.2	$1,071.7	-$9.5
Other earnings[1]	$1.2	$0.8	-$0.4
Total Available Resources	$1,083.8	$1,073.8	-$9.9
Dedicated Distributions[2]	$637.8	$633.9	-$3.9
Other Legislatively Adopted Allocations	$473.5	$473.5	$0.0
Total Distributions	$1,111.3	$1,107.4	-$3.9
Ending Balance	-$27.6	-$33.6	-$6.0

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.

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 has applied this transfer rate on sales since July 1, 2009. The effect of this action will serve to reduce the potential for additional administrative savings, as a larger percentage of revenue will be transferred through the normal quarterly process. In spite of this change, the Lottery expects some administrative savings to be realized over the course of the biennium. Included in this forecast is a $4 million transfer expected to be made this fall.

Following a decline of 19.2 percent for 2009-11 over 2007-09 figures, lottery earnings are expected to rise a modest 7.4 percent to $1,150.6 million for the 2011-13 biennium. In addition to the expected impact of the smoking restrictions and slow economic growth, the weak growth for 2009-11 is the result of an absence of significant administrative savings for the biennium, compared with $102.7 million in the 2007-09 biennium. Not including any administrative savings that may accrue during the biennium, total available resources for 2011-13 will amount to $1,151.7 million. For the 2013-15 biennium, lottery earnings will climb to $1,251.1 million, while available resources will equal $1,253.1 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 recalculates the outlook for these funds based on the March 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. The state budgeted a $225 million withdrawal for spending during 2009-11. As a result, the beginning balance of the fund was reduced commensurately for 2009-11.

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[2], 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. The balance of the ESF was withdrawn near the end of 2007-09 in order to fill the budget gap created by decreasing revenues late in the biennium. As a result, we do not expect that the fund will reach its cap during the forecast period.

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[2] Five 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.

Budgetary Reserve Outlook

Table R.4 presents projected balances for the ORDF and ESF. At the close of fiscal year 2009, the balance in the ORDF equaled $112.5 million. The ORDF is projected to reach $134.7 million by the end of 2009-11. Assuming no withdrawal is made to offset the negative ending balance in 2009-11, the balance would reach to $138.4 million by the end of 2011-13.

The ESF balance was completely withdrawn at the end of 2007-09 in order to fill the budget shortfall for 2007-09. Assuming no additional distributions are made during the next biennium, by the end of 2009-11, available ESF funds will total $183.3 million. Table B.10 in Appendix B provides detailed information for Oregon's budgetary reserves.

Table R.4

Oregon's Budgetary Reserves

(Millions)	2007-09 Biennium	2009-11 Biennium	2011-13 Biennium
Rainy Day Fund			
Beginning Balance	$0.0	$112.5	$134.7
Deposits	$94.3	$19.8	$0.0
Interest	$18.3	$2.3	$3.8
Triggered Withdrawals	$0.0	$0.0	$0.0
Ending Balance[1]	$112.5	$134.7	$138.4
Education Stability Fund			
Beginning Balance	$178.9	$0.1	$183.3
Deposits	-$178.9	$183.2	$201.7
Interest[2]	$17.2	$2.7	$22.2
Triggered Withdrawals	-$17.1	-$2.7	-$22.2
Ending Balance	$0.1	$183.3	$385.1
Total Reserves	$112.6	$318.0	$523.5

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%).