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To: CAS DeanStaff; CAS Unit Leaders; Salem Update Listserv
Subject: [Salem Update] Budget cuts and musical chairs
Date: Friday, May 02, 2008 1:11:14 PM
Attachments: ATT1867027.txt

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Revenue forecast puts salary pool at risk.

Legislators are beginning to hear concerns regarding possible cuts to state agencies that could stem from a Joint Legislative Emergency Board (E-Board) decision scheduled for June regarding the release of $125 million in funds designated for state agency salary increases.

The Legislature established the salary pool last session to enable state agencies to cover salary increases over the 2007-09 biennium. Since then, the Governor approved increases for state agency executives and classified workers, including classified staff at OSU. OSU followed suit and provided a modest average 4% increase for faculty with an expectation of further increases next year.

When the February 2008 revenue forecast showed a $150 million loss in revenues, legislative budget leaders decided to delay releasing the salary pool until after the next revenue forecast, scheduled for May 29th. The Emergency Board decision to consider the matter is scheduled for June 25-26.

Legislators currently are sitting on a $36.5 million "ending fund balance," down from the $184.2 ending fund balance they had at the beginning of the biennium. If the May 29th forecast shows further declines, the $36.5 million could disappear. A forecast that shows a loss of funds greater than $36.5 million would leave legislators with no alternative but to reduce the salary pool, unless they opt to go into a special session.

Regardless of the forecast, the E-Board can choose to release some, none, or all of the $125 million. OUS has claim to $28.5 million of these funds, with $12 million destined for OSU. If the E-Board holds onto some of the money, it can choose to apportion the reductions proportionately across all state agencies, or to release the funds to some, but not to others. No matter the decision, salaries will stay in place, but for every dollar legislators withhold, state agencies will be forced to make cuts elsewhere during the remainder of the biennium.

Some state agencies have more pressing problems than others. For example, if the E-Board withholds the more than $30 million in the pool designated for the State Department of Corrections, that agency may be forced to release prisoners – not a popular step, especially at a time when voters will be considering two ballot measures

calling for mandatory prison sentences.

The E-Board could also instruct or enable some agencies to use other funds, such as fees or tuition revenues to fill in for lost general funds. Tuition increases are problematic for a number of reasons. First, in a budget note that accompanied the OUS appropriation last session, the legislature sought to gear tuition increases to stay in synch with increases in the "median family income." That enabled tuition increases at around 3% per year. While the E-Board may approve actions that run counter to the budget note, any additional increase in tuition would diminish the effectiveness of funds the legislature devoted to financial aid in the Shared Responsibility Model.

Additionally, across OUS institutions, tuition would have to increase on average around 6 to 7% on top of the 3% in order to make up for the complete loss of the $28.5 million in salary pool funds. Several campuses have little or no flexibility in raising tuition due to potential decreases in enrollment or due to promises to hold tuition flat for students as they matriculate through their four yeas on campus – the Western Oregon University promise, for example. Further, deciding to increase tuition in July for students who have already made attendance and financial aid decisions based on a significantly lower number will surely have a disastrous effect, not only on enrollments and financial aid, but also on a university's credibility.

If the June forecast is significantly below the February forecast, the E-Board still may release the entire salary package even if doing so would result in the state's budget becoming "un-balanced". Although deliberate legislative actions that result in budget deficits may cause some to worry about the state's bond rating, in releasing the funds the legislature could commit to a special session later to rebalance the budget if the revenue picture does not improve.

But the Governor and Legislators are not favorably disposed to a special session. It is an election year, and cutting budgets or "raiding" the various reserve funds available to them may not be viewed favorably by Oregon voters. "Times are tough -- we're cutting our budgets, so should state agencies." Nevertheless, choosing to hold onto the salary pool in June already creates a budget cutting exercise – one made by a small number of legislators, to a limited number of agencies.

Some contend that releasing the salary funds in June regardless of the forecast would give the Legislature time to rationally and equitably address the problem of future revenue declines. If future forecasts increase, there may be no need for a special session. If the forecasts continue to decline, then a special session would have been inevitable anyway. Unless it goes into a special session, the Legislature will not be able to address the problem of falling revenues with the biggest player in the state budget: K-12. Because teachers are not state employees, K-12 and community colleges are not affected by a decision to withhold the salary pool.

It is possible that the matter of the salary pool may not even make it to the E-Board in June. If the Governor does not request the funds, the legislature is not obligated to put the issue on the agenda. But this course of action would automatically cause agencies to start cutting budgets, including the Department of Corrections. OUS

institutions, which must plan for the next academic term, would have no alternative but to start cutting budgets July 1st, the beginning of the second fiscal year of the biennium.

What are the alternatives?

If legislators eventually decide to resolve the matter in a special session, they have the choice of cutting budgets and/or making use of two reserve funds – the Education Stability Fund established by voters in 2002, and the Rainy Day Fund established by the legislature last session when it withheld some $300 million in corporate kicker refunds from Oregon businesses.

The Rainy Day Fund. Most legislators dismiss the Rainy Day Fund as an alternative. As prescribed by statute the rainy day fund has no available balances in the current biennium. The current statute requires the funds be available at the *beginning* of the biennium in which withdrawals occur. Since the corporate kicker was not transferred into the new fund until *after* the biennium began, those funds are not available in the current biennium. However, the statute can be modified with a simple majority vote (16 votes in the Senate, 31 votes in the House).

The political optics of raiding a fund they just created may be difficult. But if faced with disastrous revenue declines legislators might be convinced that, indeed, it is raining. Further using it, does not necessarily require a 3/5's super majority.

The Education Stability Fund. This fund was established in the Constitution by the voters in 2002 and is funded with 18% of lottery proceeds. It has been used in the past, and unlike the rainy day fund, it is automatically replenished with lottery funds. It is the more likely target, but the fund can only be used for "public education." (Nevertheless, in a special session, the legislature can always cut from public education, use the savings to help somebody else out, and re-fill the education hole with funds from the Education Stability Fund. When the legislature is in session, everything is "fungible.")

Currently some $350 million resides in the fund. Gaining access to it, however, requires a 3/5 vote in each chamber (18 votes in the Senate, 36 votes in the House) and meeting one of the following triggers:

a. The final revenue forecast for the current biennium indicates revenues in the next biennium will be at least 3% less than appropriations for the current biennium. (*It will not be possible for the legislature to meet this trigger for the current biennium in a special session because the final revenue forecast for the current biennium will not occur until the Legislature is in regular session in 2009.*)

b. Employment has dropped for two or more consecutive quarters in the last 12 months. *(In June, it will not be possible to determine if this trigger has been met. While seasonally adjusted employment has now dropped for one quarter, information for the next quarter will not be available until July.*) OR

c. A quarterly revenue forecast that projects general fund revenues in the current

biennium will be 2% below the forecast used for the current budget. (*In order to meet this trigger in the current biennium before September, the May2008 forecast would have to be down by another $129.4 million over the February 2008 forecast.*)

The Education Stability Fund may also be released if the Governor declares an emergency. In that case, the legislature must meet in a special session, and both chambers would still have to approve the release of the funds through a 3/5 vote.

Another alternative involves the Governor's power to cut budgets by 1% across-the-board. Higher education would be better off with a 1% reduction if provided the salary package, than no salary package at all. For public education, including K-12, any across-the-board reductions could be mitigated by the legislature in a special session with money from the Education Stability Fund.

What happens next?

1. The next Revenue Forecast is scheduled for Thursday, May 29th. Based on the forecast, we will know whether revenues are expected to continue to slide, level off, or improve.

2. Within a week of the forecast, the Governor must determine whether to request the Emergency Board to release the funds. If the Governor does not request the release, it is possible the issue may not come before the Emergency Board, although legislators could defy the Governor and put the issue on the agenda.

3. If the issue reaches the Emergency Board's June 25-26 Agenda, the Emergency Board may exercise discretion in releasing these funds. It may choose to make across-the-board reductions applied proportionately to state agencies, release the funds to some agencies but not others, or not to release any of the funds.

Those who are seeking release of the salary pool have made the following arguments:

- The Governor and the Legislature deserve credit for doing the right thing last session by significantly increasing funding both for Oregon's public universities and for financial aid to Oregon students under the Shared Responsibility Model.

- The investments are working. Due to the Shared Responsibility Model and increased funding to supply more classes and services, enrollments this fall are projected to increase. Applications from resident undergraduate students are up 15% across OUS. Oregon is providing opportunities for students who previously could only dream of attending college.
- Withholding funds now would immediately stop the progress and eliminate opportunities altogether. Universities would be forced to eliminate class offerings, services to ensure student success would be cut, and tuition could be increased.
- Long term residual impacts of "boom-bust" investments are well documented. In 1999 the Legislature significantly increased support for universities and capped tuition. Enrollments climbed. But in 2002 and 2003 the Legislature cut

funding and raised tuition. Enrollments declined, graduation rates fell, and Oregon lost ground.

- With classes due to start in September, Oregon's students cannot wait for a possible increase in the September forecast. If the Legislature does not release the funds in June, universities have no choice but to cut their budgets. Some universities are already struggling.
- Failing to release the funds disrupts the K-20 continuum. The cuts will fall only on Oregon's public universities.

More musical chairs – Bonamici moves to the Senate.

In March, Governor Kulongoski appointed Senator Brad Avakian (D-Washington/Multnomah Counties) to fill in as the Commissioner of Bureau of Labor and Industries, creating a vacancy in the Senate that was filled this week by the local county Commissioners who appointed State Representative Susan Bonamici, a first term Washington County Democrat.

Bonamici, who holds both an undergraduate and a law degree from the University of Oregon, worked with the Federal Trade Commission in Washington DC as well as a Portland law firm. She has been an active volunteer in the Beaverton school system. In the House she has served on the Judiciary, Consumer Protection, and Health Care Committees.

Washington County commissioners must now select a Democrat to fill Bonamici's vacancy in the House. The move also will create changes on the November ballot. Although Avakian was mid-term, Bonamici will be required to run for the seat in November -- for a two-year term. Since it's too late to put the race on the May 20th primary ballot, there will be no primary race. Rather, in November Bonamici could possibly face a host of Democratic and Republican candidates vying for the seat.

The story is a little different for whomever is appointed to replace Bonamici in the House. That vacancy must be filled by the local county Commissioners within 30 days of the vacancy. Although Bonamici appears on the May 20th primary for the House seat, votes for her won't count. The lone Republican candidate for that seat will appear on the November ballot -- the Republicans have no opportunity to switch to another candidate. Any Democrat, including the individual who will be appointed to fill the vacancy may file for the seat in the November election. August 26th is the deadline to file for both House and Senate seats in order to be on the November ballot.

Meanwhile, with Avakian's departure from the Senate, Senate President Peter Courtney has appointed Senator Alan Bates (D-Ashland) to chair the Senate Energy and Environment Committee.

Questions, comments or concerns about any of the above will be gladly received.

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