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Budget Footnotes

A NEWSLETTER OF THE OHIO LEGISLATIVE SERVICE COMMISSION SEPTEMBER, 2001

FISCAL OVERVIEW

— *Doris Mahaffey*

On June 25, the state budget climbed into the black for the first time since July 14, 2000. After 6 years of $600 million plus budget surpluses, arising from below estimate Medicaid spending and above estimate tax revenues, the state's fortunes reversed in FY 2001. Medicaid finished the year $625 million *over* estimate and tax revenues came in $329 million *under* (based on July 2000 revenue estimates). The state ended the year with an unencumbered cash balance of $219.4 million, $206 million of which was needed as a carry over balance to FY 2002. For comparison, the unobligated balance at this time last year was $855.8 million – of which $196.4 million was needed as carryover to FY 2001.

The $219 million unencumbered balance exceeded the $188.2 million balance assumed for the start of FY 2000. Thus, no transfer *from* the Budget Stabilization Fund (BSF) was needed. Am. Sub. H.B. 94 – the FY 2002-2003 biennial appropriations bill – called for a transfer from the BSF at the end of FY 2001 in order to bring the fund balance to that level if necessary. In fact, the ending balance allowed for a $13 million transfer to the BSF – not nearly enough to lift the BSF to the target 5 percent of prior year revenue. That would have required a transfer of $63 million.

The contrast between the end of FY 2001 and the end of FY 2000 was striking. A year ago, a buoyant economy and plentiful tax revenues provided smooth sailing for the Ohio economy and state budget in FY 2000. But in the past year the twin problems of a slowing national economy and growing health care costs have cut into anticipated revenue for state budgets. Ohio was no exception. The growth of state tax revenues has stalled (increasing by only 0.2 percent in the last year). At the same time, Medicaid expenditure growth has accelerated. In FY 2001, Ohio's Medicaid expenditures increased by 17.8 percent over FY 2000. In contrast, Medicaid expenditures grew at an average annual growth rate of 4.3 percent between FY 1992 and FY 2000.

If anything, Ohio was particularly vulnerable, since the core of the economic slowdown was in the manufacturing sector; Ohio relies more heavily on manufacturing than all but a few other states. The first indications of the slow down were in retail sales. After growing at an average monthly rate of 9.5 percent throughout FY 2000, retail growth began to falter in the summer of 2000 – slowing to a rate of 6.1 percent in the second half of calendar year 2000 and a 3.2 percent growth rate in the

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Budget Footnotes is issued periodically by the fiscal staff of the Legislative Service Commission (LSC), a non-partisan agency serving the Ohio General Assembly.

Budget Footnotes examines the fiscal position of the state GRF on a periodic basis.

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TABLE 1
General Revenue Fund
Simplified Cash Statement
($ in millions)

	Month of June	Fiscal Year 2001 to Date	Last Year	Difference
Beginning Cash Balance	$331.3	$1,506.2		
Revenue + Transfers	$1,997.1	$21,309.2		
Available Resources	$2,328.4	$22,815.5		
Disbursements + Transfers	$1,511.3	$21,998.4		
Ending Cash Balances	$817.1	$817.1	$1,506.2	($689.1)
Encumbrances and Accts. Payable		$597.7	$650.4	($52.7)
Unobligated Balance		**$219.4**	**$855.8**	**($636.4)**
BSF Balance		$1,002.5	$953.3	$49.2
Combined GRF and BSF Balance		**$1,221.9**	**$1,809.1**	**($587.2)**

first half of 2001.[1] The slowdown in retail sales included a move toward necessities and away from fashion and gadgets. The rather narrow base of Ohio's sales tax (excluding food and many services) turned this retrenchment into a reduction, which it then amplified (just as it may have amplified the spending surge of a year ago when total sales tax revenues grew at a rate of 10.9 percent during the January to March 2000 period). Ohio was one of six states whose first quarter 2001 sales tax revenues (that is, January to March 2001) fell short of the same revenues from the first quarter of 2000.[2]

Ohio's income tax also reacted to the economic slowdown. The reduction in number of workers and hours worked took their toll on wages and subsequently on withholding. And the swift decline of the stock market in the fourth quarter of 2000 led to sharply revised estimates of non-wage income leading to lower quarterly estimated payments. Add to this, was the substantial tax cut on tax year 2000 income funded by the state's $610.4 million surplus at the end of FY 2000. The tax cut for 2000 of 6.96 percent cost the state $317.2 million more than the $293.2 million (or 3.63 percent) tax cut for tax year 1999. Thus, the tax cut exacerbated the impact of the economic slowdown on the state's tax receipts.

With the exception of the public utility excise tax, all the major taxes came in under estimate for the year. The sales and use tax was $239 million under estimate (of which $221 million was non-auto) and the personal income tax was $117 million under.

Total revenues were $438 million over estimate – largely due to a $599 million overage in federal reimbursements. Transfers contributed $115 million to the overage.

Tax revenues were basically flat compared to FY 2000 (up only 0.2 percent). Total GRF income was up 6.28 percent – largely due to a 21 percent increase in federal reimbursements. (The ITRF mechanism also served to increase "other revenues" while dampening tax receipts. Had the year's tax cut remained the same as last year's, tax revenues would have increased by 2.2 percent. Total revenue growth would have remained unchanged.)

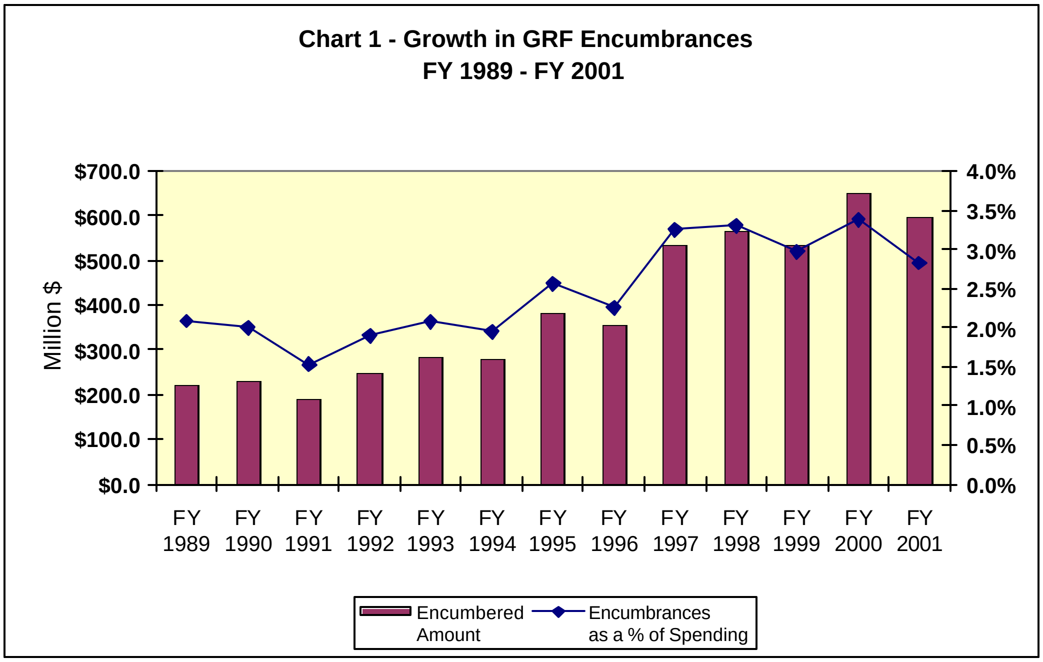
The growth in federal reimbursements was accompanied by an 18 percent growth in Health Care/Medicaid disbursements (along with a 20 percent growth in disability assistance [DA]). Growth in most other spending categories was more modest.

Ohio was one of 31 states that needed to make supplemental appropriations in FY 2001 to deal with growing Medicaid costs. The emerging Medicaid problems were reminiscent of the early 1990s when Ohio, as well as many other states, experienced double-digit spending growth rates. In the latter half of the 1990s, the Medicaid cost pressures were eased by reforms, low medical cost inflation, and a robust economy. But in the last 18 months the costs have begun to escalate with greater than expected caseload growth across all eligibility classes, coupled with higher than expected health care cost growth contributing to the cost pressures.

With faltering tax revenues and expanding Medicaid expenditures, in order to end the year with a positive fund balance, the state undertook two rounds of across-the-board budget cuts.

The first was implemented as a result of Sub. S.B. 346 enacted in December 2000. It increased Medicaid and DA appropriations by $645 million. Part of this increase was to be financed by an increase in federal reimbursements. The state share was to be funded by a $125 million increase in state revenues and $125 million in appropriations reductions. When the additional revenues failed to materialize and, in fact, decreased, the Governor called for and implemented an additional round of appropriations reductions in late March of 2001.

At the year's end, the GRF cash balance was $817.1 million. (See Table 1.) Subtracting the $597.7 million in encumbrances, FY 2001s unobligated balance was $219.4 million. Encumbrances were down $53 million or 8 percent from last year. As Chart 1 illustrates, as a portion of prior year spending, year-end encumbrances are lower than any fiscal year since 1996.



At the end of FY 2000, $650 million was encumbered. Table 1a shows the disposition of these funds at the end of FY 2001 by year encumbered. At the end of FY 2001, just $78 million of these funds remained encumbered. (One tactic for dealing with the mandated appropriations reductions was canceling encumbrances.)

Additional encumbrances of $519 million from FY 2001 appropriations were added to the remaining $78 million. Seven agencies accounted for 86 percent of these encumbrances. Ten line items in these agencies accounted for over half of these encumbrances. These are listed in Table 1b. By far the largest FY 2001 encumbrance was in the Department of Education's line item 200-501, Base Cost Funding, followed by Education's 200-534, Desegregation Cost. These encumbrances are discussed in the Disbursements section below. The next largest were in the Department of Job and Family Services 600-525, Medicaid, and 600-411, TANF Federal Block Grant lines. They also are discussed below.

Table 1a – Disposition of Prior Year Encumbrances in FY 2001

	Disbursements	Cancelled Encumbrances	Remaining Encumbrances
1993	488.23	49,662.12	0.00
1994	34,746.25	158,014.83	0.00
1995	101,182.75	276,953.54	0.00
1996	853,029.50	1,170,051.12	252,127.32
1997	4,048,321.50	10,378,936.23	3,728,278.56
1998	5,216,739.50	9,122,107.77	7,224,028.09
1999	25,694,118.24	28,753,408.67	9,955,445.45
2000	340,271,770.48	200,775,680.65	57,119,584.96
Total	$376,220,396.45	$250,684,814.93	$78,279,464.38

Table 1b - FY 2001 Encumbrances
$ In millions

Agency	Total		Major line items	Amount
Job and Family Services	$131.9	600-411	TANF Federal Block Grant	$28.4
		600-525	Medicaid	$31.2
Education	$127.0	200-501	Base cost funding	$36.4
		200-534	Desegregation cost	$32.5
Development	$50.2	195-422	Technology Action	$14.3
		195-434	Industrial Training Grants	$16.5
Rehabilitation and Corrections	$46.0	501-321	Institutional Operations	$24.8
Board of Regents	$34.3	235-590	12TH Grade Proficiency Stipend	$19.2
Transportation	$33.6	775-451	Public Transportation - State	$24.0
Mental Retardation & Developmental Disabilities	$23.0	322-413	Residential and Support Services	$22.9

Ohio's unobligated general revenue fund balance of $219.4 million and budget stabilization fund (BSF) balance of $1,002.5 million yielded a combined year-end balance of $1,221.9 million. This amounted to 5.6 percent of the state's FY 2001 expenditures (excluding federal grants but including encumbrances) – half of the 11.2 percent in FY 2000.

The $219 million fund balance was not sufficient to generate a tax cut for FY 2002. The bulk of the fund balance is to remain in the GRF in order to fulfill certain obligations. As prescribed in section 131.44 of the Revised Code, before transferring any money to the Income Tax Reduction Fund (ITRF), the following obligations must be met:

1. The maintenance of a cash-flow balance in the GRF equal to 0.5 percent of prior year (in this case, FY 2001) revenues;
2. The transfer of sufficient funds to the Budget Stabilization Fund (BSF) to bring the balance of the fund up to 5 percent of prior year revenues;
3. The maintenance of sufficient funds in the GRF to meet capital obligations; and
4. The maintenance of sufficient funds in the GRF to cover the delayed impact of the prior year's tax cut.

After meeting obligation numbers 1, 3, and 4 – which entailed a cash-flow balance of $106.5 million, a capital appropriation reserve of $17.9 million, and an income tax reduction impact reserve of $81.9 million – only $13 million was available for transfer to the BSF. That was $50 million short of the amount needed to bring the BSF up to 5 percent of FY 2001 revenues.

Throughout this publication, the actual FY 2001 revenues and disbursements are compared to the OBM estimates made in July 2000 (for revenues) and September 2000 (for disbursements).

This approach is consistent with *Budget Footnote's* long-established practice. OBM makes its monthly revenue and disbursement estimates based on these overall estimates, which LSC uses in setting up Tables 2 through 4 regarding monthly and year-to-date revenues and monthly and year-to-date disbursements.

Thus, the estimates used do not reflect the significant appropriation changes that were made in December 2000. Nor do they reflect the new revenue estimates that were made in December, as well as March and May of 2001.

In fact, the July 2000 revenue estimates themselves were revisions of the estimates made in June 1999, upon which the original FY 2001 appropriations were based. Actual FY 2001 revenues exceeded the original FY 2001 estimates by $1,005 million ($599 million of which, again, were from federal grants due to higher Medicaid and welfare spending). Based on those original estimates, had the original June 1999 estimates been retained, the budget picture throughout the second half of FY 2001 would have unfolded differently.

Looking Back on FY 2001

The initial budget projections for FYs 2000-2001 (utilized by the Conference Committee in finalizing Am. Sub. H.B. 282 and Am. Sub. H.B. 283 of the 123rd General Assembly) assumed that FY 2001 revenue would fall short of FY 2001 appropriations by $160.1 million. Thus, the planned ending fund balance for FY 2000 included $160.1 million to cover this planned deficit. Also, included in the ending fund balance estimates were a $37.7 million transfer to the BSF, $39.4 million for the ITRF impact reserve, $56.7 million for the capital appropriation reserve, and $101.5 million for the cash flow balance requirement.

When the revenue estimates were increased for FY 2001 at the end of FY 2000, it was thought that the excess was not needed for FY 2001 – that FY 2001 revenues would exceed the appropriations for FY 2001 – so that the $160.1 million originally planned to cover the deficit was transferred to the ITRF along with the other surplus revenue.

The estimated increased revenue for FY 2001 was to have covered not only the original $160.1 million deficit, but also the additional spending and transfers due (largely) to H.B. 640 (the capital appropriations bill) and other Controlling Board actions. Original transfers provided for in H.B. 283 included the $37.7 million to the BSF plus $23.4 million to disaster assistance and distance learning. H.B. 640 provided for additional transfers of $120 million to the public school building fund and $10 million to the state infrastructure bank fund. Plus, the transfer to the BSF was increased to $49.2 million due to the increase in FY 2000 revenues.

At the beginning of FY 2001, estimated program expenditures for FY 2001 exceeded original appropriations by $24 million while estimated transfers exceeded original transfer estimates by an additional $749.8 million. (This includes the transfer of $610.4 million to the ITRF. Excluding the transfer to the ITRF, the increase was $139.4 million.)

In July 2000, OBM increased its FY 2001 revenue estimates (over original Conference Committee estimates) by $567.3 million. The problem was that these revised revenue estimates were made when the growth rates of both economic indicators and state tax revenues had essentially peaked. At the end of FY 2000, the outlook for FY 2001 was optimistic.[3] Both personal income and retail sales had been growing strongly. Moreover, Ohio tax revenues had grown by more than 7 percent in FY 2000. In retrospect, the economic indicators generally pointed gently downhill from there.

Nevertheless, FY 2001 revenue estimates were further increased in December 2001 by an additional $680.3 million (largely due to an increase in federal grants related to the increased Medicaid appropriations noted above). The total increase was $1,247.6 million over original Conference Committee estimates for FY 2001.

In March 2001, OBM reduced its revenue estimates vis-à-vis July 2000 by $305 million. This is still greater than the original Conference Committee estimates by $942.6 million. Excluding federal funds, the net increase amounted to $325.3 million. This increase in state revenues would take care of much of the increase in appropriations and transfers – *but for* the increase in Medicaid costs.

By the end of November 2000, Medicaid expenditures were already $188 million over estimate. By the end of February, they were $486 million over estimate. This Medicaid problem was not entirely unexpected. It was developing in FY 2000, but the funding shortfall was largely taken care of by non-GRF sources. FY 2000 GRF Medicaid appropriations were increased from $5,517.8 million to $5,530 million of which $5,525 million was spent and the remainder was encumbered.

To take care of the anticipated FY 2001 spending overage, S.B. 346 (which was effective December 8, 2000) increased appropriations to Medicaid and disability assistance by a total of $645.5 million in FY 2001. Of this, nearly $400 million was to come from increased federal assistance and the remaining $250 million was to come from state sources – half from additional revenue and half from executive budget cuts.

In accordance with S.B. 346, OBM authorized a total of $126.3 million in spending reductions. However, in January, the weakness of the economy became widely recognized.[4] The tumbling stock market, the increase in mass layoff announcements, and the slow holiday shopping season provided convincing evidence that a slowdown – if not an actual downturn – was indeed in progress. (Economists have avoided using the term "recession" to describe the economy, although the word has been applied to the manufacturing sector since early January. The terms "dip," "double-dip," and "swoosh" have been offered to depict what a graphical view of the economy might portray.)

By March it seemed apparent that the additional revenue was not forthcoming; thus the remedies called for in S.B. 346 were not enough. The $325.3 million net increase in state revenues over Conference Committee estimates was needed to fund the increase in net transfers – i.e., $184.5 million ($120 million to the Public School Building fund, plus $10 million to the State Infrastructure Bank fund, plus $54.5 million [the local government's part of the FY 2001 tax cut incurred in FY 2001[5]]) – plus the $160.1 million revenue surplus from FY 2000 that was originally going to cover the "planned" FY 2001 deficit, but that was transferred to the ITRF when it was thought that it would no longer be needed. Thus the increase in net revenues ($325.3 million) was not even enough to cover the transfers ($344.6 million). Additional measures – i.e., more budget cuts – were required to deal with the Medicaid problem. ❑

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[1] Based on seasonally adjusted year-over-year monthly data issued by the Monthly Retail Services Branch of the U.S. Census Bureau.

[2] Nicholas W. Jenny and Donald J. Boyd, "A Second Quarter of Slow State Tax Revenue Growth," *State Revenue Report*, No. 44, June 2001.

[3] For example, the Standard & Poor's DRI forecast of the U.S. economy for July 2000 begins its synopsis as follows:

> The current expansion continues to roll through its 10th year. The expansion is already a record length, and there are few signs that the streak will end soon. The boom is beginning to attenuate, however, which should extend its life. (Standard & Poor's DRI, *The U.S. Economy*, July 2000, p. 10)

The August 2000 forecast summary, entitled, "What Happened to the Slowdown?" begins:

> Rumors of an economic slowdown have apparently been exaggerated. The 5.2% growth of real GDP in the second quarter suggests that the U.S. economy is not downshifting, and that the Fed may have to hit the monetary brakes again.
>
> But the GDP data are misleading, distorted by government spending and inventory accumulation. The slowdown in private demand will eventually dampen economic growth, but perhaps not as much as we had expected. (Standard & Poor's DRI, *The U.S. Economy*, August 2000, p. 1)

In hindsight, the boom did not attenuate so much as dissipate; and the slowdown was much more than we expected.

[4] As WEFA observed in its forecast overview for January 2001:

> It looks like a good year in 2001 – for economists. We have clearly moved to a contractionary stage of the business cycle. A year ago, some had concluded that there were no more significant US business cycles. Now, all attention is focused on how low and how long the slowdown will be, and whether there could be an outright recession. (WEFA, *U.S. Economic Outlook 2000-2006*, January 2001, p. 5)

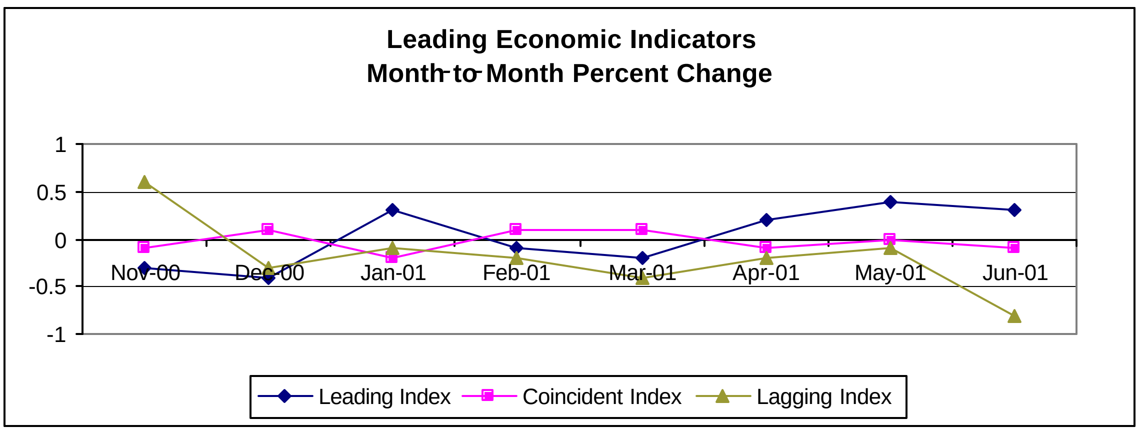
[5] Of the $610.4 million transferred to the ITRF, the bulk of the money – $546.3 million – is transferred back into the GRF to pay for the tax cut.

TRACKING THE ECONOMY

— Jean J. Botomogno

Is the economy just treading water before a rebound or are we at the brink of a recession? It just is not clear which way the economy is turning. One scenario has the second quarter being the worst of the year with the economy getting better afterwards. Another scenario has the economy being in the middle of a protracted slump. Six interest rate cuts this year by the Federal Reserve Board are yet to kick the economy into higher gear, due to the considerable time lag between interest rate cuts and their positive impact on economic activity. Disappointing corporate profits and a dismal outlook are restraining capital investments and increasing layoff announcements. In the words of Alan Greenspan testifying before the U.S. Congress on July 24, 2001, "uncertainties surrounding the current economic situation are considerable, . . .we are not out of the woods."

The U.S. index of leading economic indicators rose 0.3 percent in June. This was the third consecutive increase in the leading index. While the leading index rose strongly, the coincident index, a barometer of the current state of the economy, fell slightly. The lagging index, a barometer of where the economy has already been, fell 0.8 percent in June. The slight drop in the coincident index combined with the sharp drop in the lagging index suggests that the worst may be over for the economy, barring an unforeseen shock. The indicators' behavior suggests that economic conditions are beginning to firm and may be setting the stage for a bottoming out, but this is by no means a certainty.

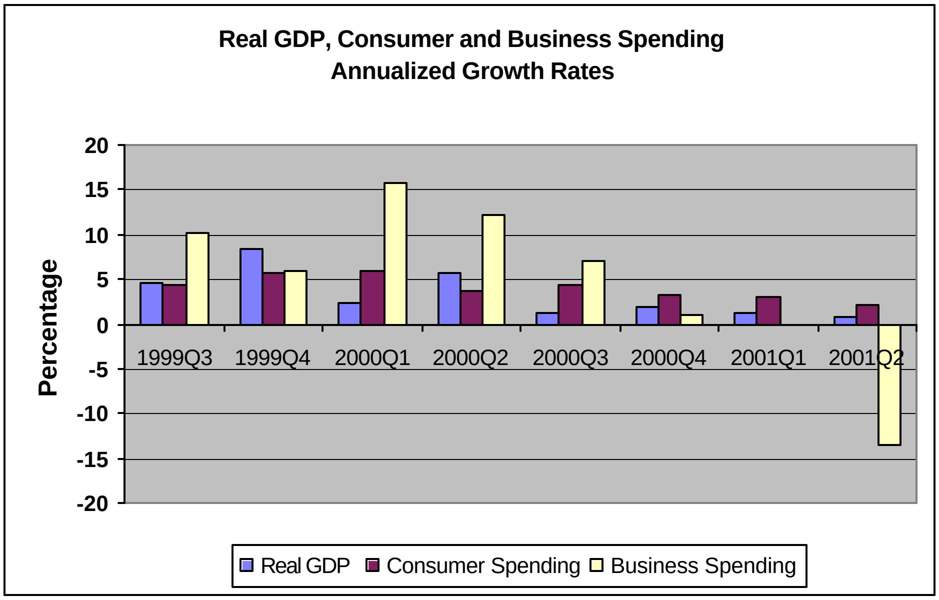


Gross Domestic Product

The economy has experienced little growth since the fall quarter of 2000. In the final revision to first quarter real Gross Domestic Product (GDP) – the country's total output of goods and services – the economy expanded by just 1.2 percent when compared to the fourth quarter of 2000. The weakest performance in 8 years was recorded in the second quarter of 2001 as advance real GDP grew by an anemic 0.7 percent. Any subsequent downward GDP revision may result in no economic growth in the second quarter.

Consumer spending that rose 2.1 percent and government spending that grew at 5.5 percent kept real GDP in positive territory. Consumer spending, which accounts for two-thirds of total economic activity, had the slowest increase in four years, but it was enough to offset weaknesses in other GDP categories, most of which declined in the second quarter.

Business spending fell 13.6 percent. Construction expenditures and equipment sales were down sharply. Exports dropped by 9.9 percent as overseas economies also showed weakness. Imports declined by 6.7 percent. Inventories were cut in the second quarter, but by a smaller amount than in the first quarter. The decrease in inventories was $26.9 billion in the second quarter, following a drop of $27.1 billion in the first quarter. Inflationary pressures weakened. The implicit GDP price deflator declined from 3.3 percent in the first quarter to 2.3 percent in the second quarter of 2001. A large part of the decline was due to the fall in fuel and energy costs.



Ohio Gross State Product (GSP) – a measure of state economic activity – barely changed in the first six months of 2001. Ohio GSP likely grew 0.1 percent in the second quarter, following a 0.1 percent decline in the first quarter. Ohio mining and manufacturing industries continued their contraction in the second quarter. Ohio construction declined slightly in the second quarter after posting a 4.8 percent growth in the first quarter, due primarily to a drop in business construction. Most other sectors showed little or no growth in the second quarter.

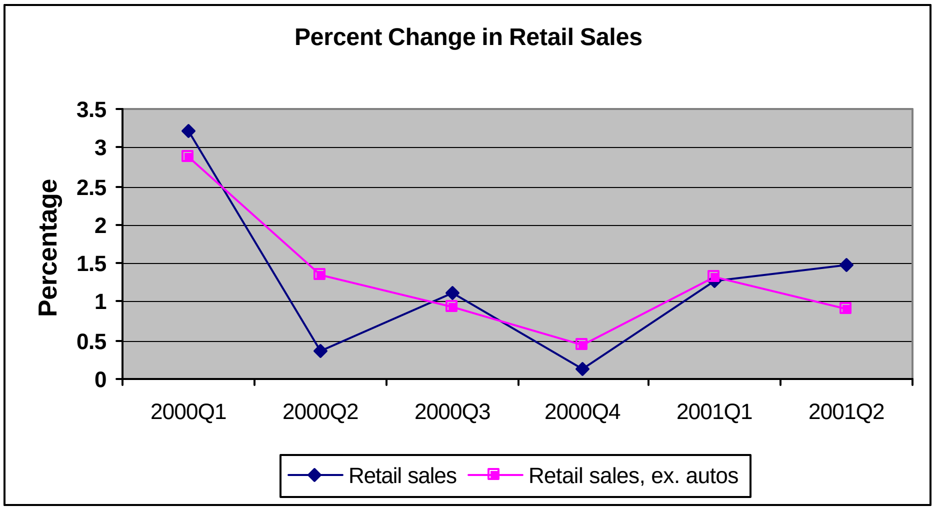
Consumers

The slowing economy has resulted in a slowdown in personal income growth. Personal income rose by a slight 0.2 percent in May, following a similar rise in April. This growth is smaller than the 0.5 percent growth registered for the first quarter of 2001. Conversely, consumer spending has risen each month of this year. The personal savings rate therefore turned downward to a negative 1.1 percent in May, its lowest since January when it stood at 1.3 percent. Consumers continue to spend out of savings and borrowing. Personal consumption expenditures grew at a seasonally adjusted annual rate of 3.4 percent in the first quarter of 2001, after a growth rate of 2.8 percent in the fourth quarter in 2000. Wages and salaries growth declined from 0.8 percent in January to 0.2 percent in May.

Retail sales posted a weak 0.2 percent gain in June. The weakening labor market and high household debt are increasingly weighing on the ability or willingness of consumers to boost the retail sector. Pockets of weakness in retail sales included clothing and accessories, food and beverage stores. Excluding autos, retail sales actually declined by 0.2 percent during the month of June. On a quarterly basis, retail sales grew 1.3 percent and 1.5 percent in the first and second quarters, respectively. Excluding autos, the percent change in retail sales was 1.3 percent in the first quarter and 0.9 percent in the second quarter. Some of the tax rebate that starts trickling to consumers in the third quarter of 2001 will help consumer spending and retail sales. The full extent of its impact in the economy will not be known for some time.

Sales at motor vehicle and parts dealers grew 1.5 percent in June 2001. At a 17.1 million seasonally adjusted annualized rate, June auto unit sales were about even with the year-ago pace. Consumers were lured to show-rooms by generous incentives and cutthroat market share competition between domestic manufacturers and international manufacturers. International manufacturers have assaulted the lucrative light truck market, help-ing to reduce overall corporate profits in this sector. A spate of new light truck models has helped maintain consumer interest and sales, but incentives have hurt profits.

Consumer confidence ticked up slightly in June propelled by more optimistic future economic conditions. The Conference Board's composite index increased from 116.1 in May to 117.9 in June. It has improved for a

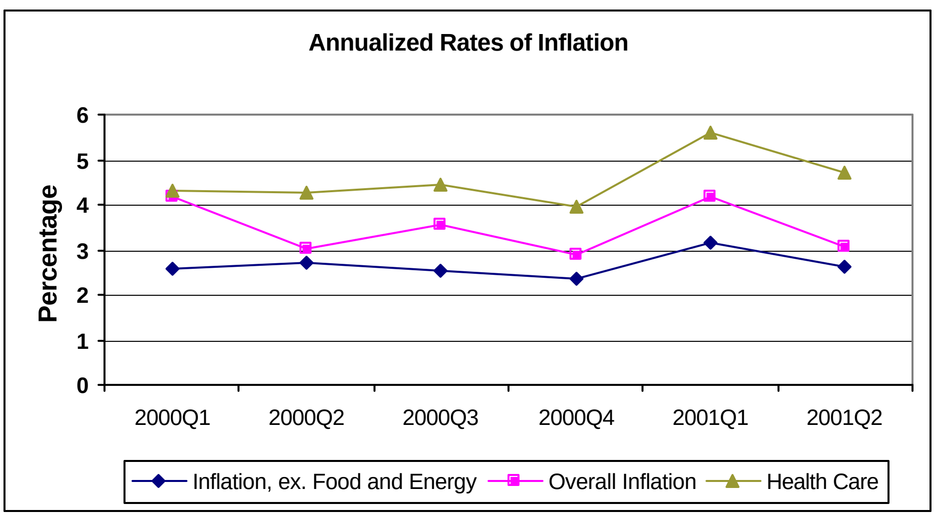


second consecutive month after dropping in April 2001. However, consumer assessment about present conditions continues to fall. The weakening labor market, stock market waffling, poor corporate earnings, and announced layoffs continue to weigh on consumer confidence. The Michigan Consumer Confidence Index fell 0.2 in July to 92.4. However, this index is still above the February level of 90.6.

Housing activity has been very resilient despite the sluggish economy. Existing and new home sales nationwide have been robust this year, helped by cuts in short-term interest rates and refinancing of mortgage debt by consumers. Existing home sales fell 0.6 percent to an annual rate of about 5.33 million units in June, from a rate of 5.37 million in May. Housing starts increased about 3 percent in June. Sales of new homes at 922,000 in June were 1.7 percent higher than May and 16.3 percent higher than June a year ago.

Prices

The Consumer Price Index (CPI), the overall rate of inflation, grew 0.2 percent in June. The core rate of inflation (CPI, excluding food and energy) in June posted its strongest advance in three months at 0.3 percent. However, energy prices, including household fuels and utilities, reversed in June. The CPI posted a seasonally adjusted annual rate of 3.7 percent in the second quarter, lower than the 4.0 percent pace of the first quarter. The core rate of inflation posted a 2.6 percent increase during the second quarter following a jump of 3.5 percent in the first quarter. Year-to-date, the CPI is advancing at a rate of 3.8 percent, which is a small increase over the year-ago rate. The Consumer Price Index posted a 3.1 percent increase in 2000.

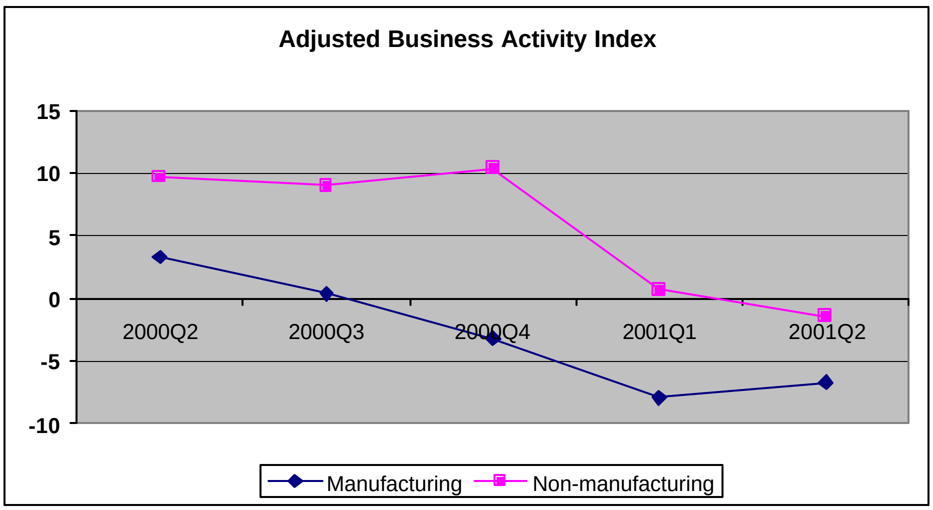


Energy prices grew at an annual rate of 8.4 percent in the second quarter, down from an annual rate of 13.7 percent in the first quarter. Health care costs increased at a 4.7 percent annual rate down from 5.6 percent in the first quarter. Food prices grew 3.1 percent in the second quarter, following an increase of 3.7 percent in the first quarter of 2001.

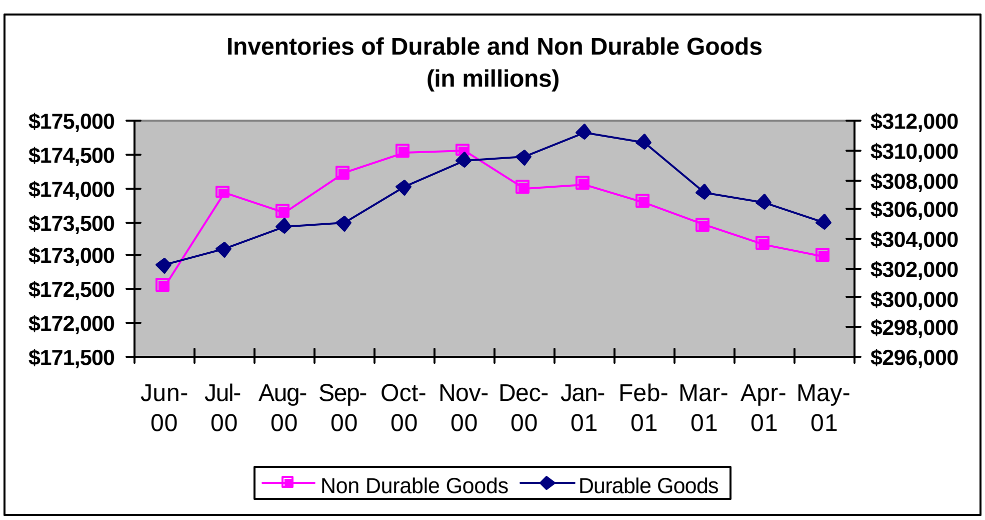
The Producer Price Index (PPI) for finished goods declined by 0.4 percent in June compared to May. This is largely due to a drop in energy prices that decreased by 2.5 percent. Inflation remains subdued, as the core index (PPI, excluding food and energy) increased only by 0.1 percent. In the second quarter, PPI's growth slowed to 0.2 percent from 1.3 percent in the first quarter. Excluding more volatile food and energy production, PPI increased only at the same rate of 0.4 percent in the first and second quarters.

Production

According to the National Association of Purchasing Management (NAPM), the non-manufacturing business activity index declined 16 percent in the first quarter and 4 percent in the second quarter. The NAPM manufacturing business activity index increased 3 percent in the second quarter, following a 10 percent decrease in the first quarter. Although its decline has slowed in the second quarter, manufacturing has been on a



down slope for 11 straight months. The adjusted NAPM activity indexes show that manufacturing has continued in 2001 its contraction started in the third quarter of 2000, and that non-manufacturing business activity while positive in the first quarter of 2001, also turned negative in the second quarter.



Industrial capacity utilization decreased in the second quarter. The capacity utilization index fell to 77.5 in the second quarter from 79.1 in the first quarter of 2001. Businesses have continued to cut inventories to adjust to slackening demand. During this adjustment, businesses also have sharply reduced capital and information technology spending. Most industries, except information technology and telecommunications, have returned to desirable levels of inventory. The sharp pull back in demand for information technology and communications services is hurting the draw down of inventories in this sector.

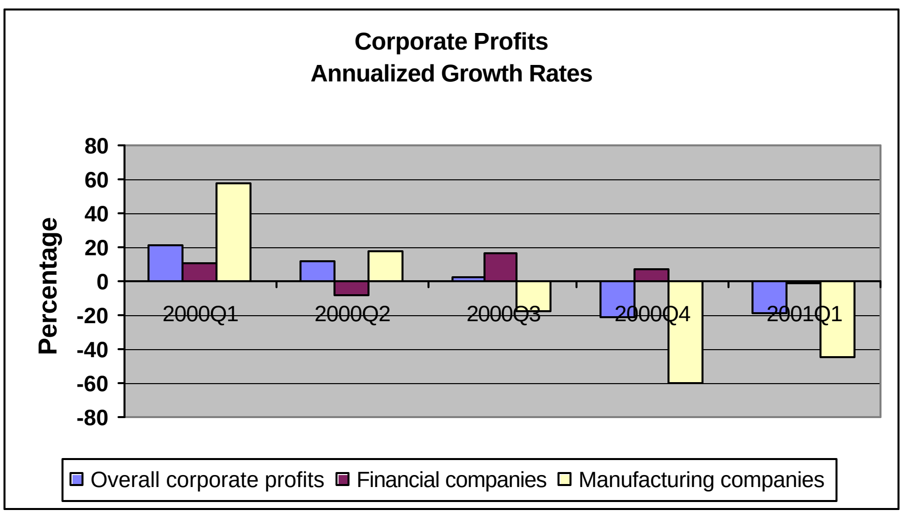
Employment

Ohio's unemployment rate (seasonally adjusted) was 4.2 percent in June, up from 4.0 percent in May and 3.9 percent in April. The unemployment rate in the second quarter of 2001 averaged 4.0 percent while the first quarter unemployment rate was 3.9 percent. Overall, Ohio has lost about 4,800 jobs since the beginning of the year 2001. While most sectors had positive or no employment growth, the serious downturn in manufacturing has cost about 15,000 jobs since the start of 2001. Over the last 12 months, Ohio nonagricultural wage and salary employment expanded by 11,400 jobs, with services primarily responsible for the change. In contrast, Ohio manufacturing has lost about 30,800 jobs, about 3 percent of manufacturing jobs as producers have aggressively reduced their labor costs during the economic slump.

Nationally, unemployment stood at 4.5 percent in the second quarter, up from 4.2 percent in the first quarter. Despite the increase in unemployment, average hourly earnings increased from $14.10 to $14.25 in the second quarter. Hourly earnings averaged $15.92 for goods-producing activities. Mining paid $17.82 per hour. Manufacturing paid an hourly wage of $17.22, Construction $18.30, Transportation $16.86, and Retail Trade $9.83.

Corporate Profits

Corporate profits have reflected the economic slowdown. All sectors, except utilities, registered declining corporate profitability in the first quarter of 2001. Corporate profits declined 18.5 percent in the first quarter, following a decrease of 21 percent in the fall of 2000. Financial companies saw no profit growth in the first



quarter of 2001. Transportation companies' profitability worsened, declining 64.2 percent following a drop of 53 percent in the fall quarter of 2000, mainly due to high energy prices. Manufacturing profits declined 44.4 percent, after 60 percent slide in the fall of 2000. Conversely, energy companies' profits increased 84.5 percent in the first quarter of 2001. ❑

Status of the General Revenue Fund

REVENUES

— Doris Mahaffey

The good news at the end of FY 2001 was that the state did not need to dip into the Budget Stabilization Fund to make it through the year. Revenues ended the year $438 million over estimate. The bulk of this was due to the $599 million overage in federal reimbursements. Most other non-tax revenue sources also came in over estimate.

Taxes were a different matter. Total tax revenue ended the year $329 million under estimate (based on the July 2000 OBM estimates). The sales tax was the greatest disappointment – coming in $239 million – nearly 4 percent – under estimate. The personal income tax also contributed to the disappointment: it was $117 million – or 2 percent – under estimate. The corporate franchise tax and the foreign insurance tax were another $35 million (4 percent) and $29 million (12 percent) under estimate, respectively. Finally, the kilowatt-hour tax debuted at $2 million under estimate. (The first payments of this tax, created by S.B. 3 of the 123rd General Assembly, in part, to replace the gross receipts tax on electric companies, were due in June of this year.)

Table 2
General Revenue Fund Income
Actual vs. Estimate
Month of June, 2001
($ in thousands)

REVENUE SOURCE			
TAX INCOME	**Actual**	**Estimate***	**Variance**
Auto Sales	$77,557	$74,700	$2,857
Non-Auto Sales & Use	$424,856	$481,050	($56,194)
Total Sales	$502,413	$555,750	($53,337)
Personal Income	$621,363	$670,889	($49,526)
Corporate Franchise	$50,281	$76,000	($25,719)
Public Utility	$151,347	$186,875	($35,528)
Kilowatt Hour Excise Tax	$22,794	$25,000	($2,206)
Total Major Taxes	**$1,348,198**	**$1,514,514**	**($166,316)**
Foreign Insurance	$1,033	$563	$470
Domestic Insurance	$228	$7,360	($7,132)
Business & Property	$509	$338	$171
Cigarette	$26,518	$25,200	$1,318
Soft Drink	$0	$0	$0
Alcoholic Beverage	$5,312	$5,225	$87
Liquor Gallonage	$2,448	$2,380	$68
Estate	$21,831	$1,600	$20,231
Racing	$0	$0	$0
Total Other Taxes	$57,879	$42,666	$15,213
Total Taxes	**$1,406,077**	**$1,557,180**	**($151,103)**
NON-TAX INCOME			
Earnings on Investments	$34,798	$32,200	$2,598
Licenses and Fees	$1,031	$1,400	($369)
Other Income	$44,326	$39,525	$4,801
Non-Tax Receipts	$80,155	$73,125	$7,030
TRANSFERS			
Liquor Transfers	$11,000	$10,000	$1,000
Budget Stabilization	$0	$0	$0
Other Transfers In	$13,463	$10,000	$3,463
Total Transfers In	$24,463	$20,000	$4,463
TOTAL INCOME less Federal Grants	**$1,510,695**	**$1,650,305**	**($139,610)**
Federal Grants	$486,384	$322,170	$164,214
TOTAL GRF INCOME	**$1,997,079**	**$1,972,475**	**$24,604**

* July, 2000 estimates of the Office of Budget and Management.
Detail may not add to total due to rounding.

The remaining taxes were over estimate by a total of $94.3 million, somewhat mitigating the tax revenue shortfall. The public utility excise tax provided the biggest boost – $65.5 million over estimate. The domestic insurance tax contributed another $17.3 million overage – partially making up for the shortfall in the foreign insurance tax. Table 3 shows how each of the state taxes and other categories fared for the year.

Personal Income Tax

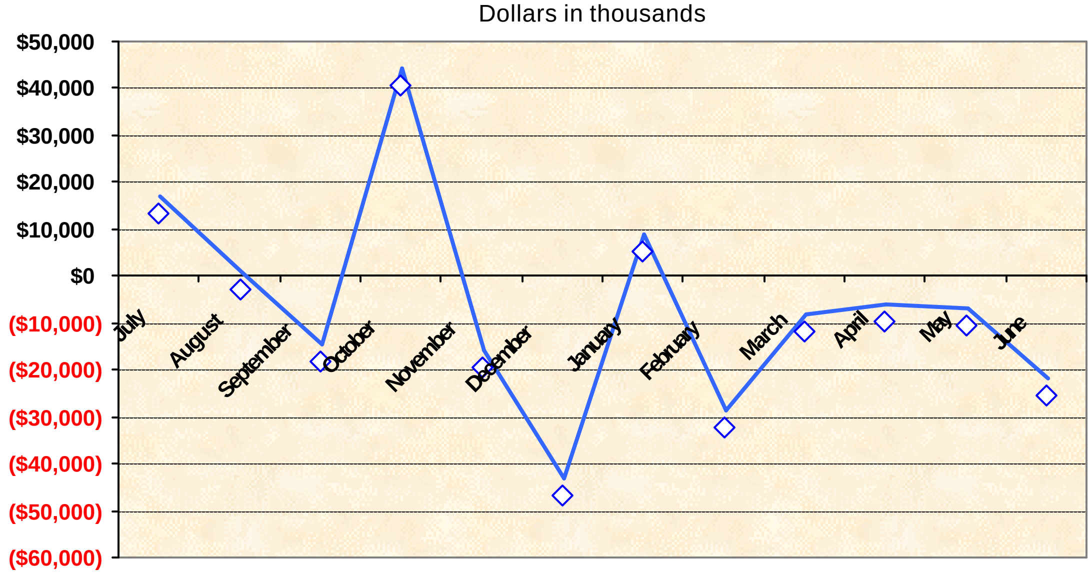
The personal income tax was under by $117 million for the year. Income tax revenues were adequate in the beginning of FY 2001 but then tumbled in November, December, and January. After coming in over estimate for the first four months, it has come in under estimate in every subsequent month except May. The May overage nearly offset the April shortfall (which was substantial) and can largely be attributed to the late processing of April returns.

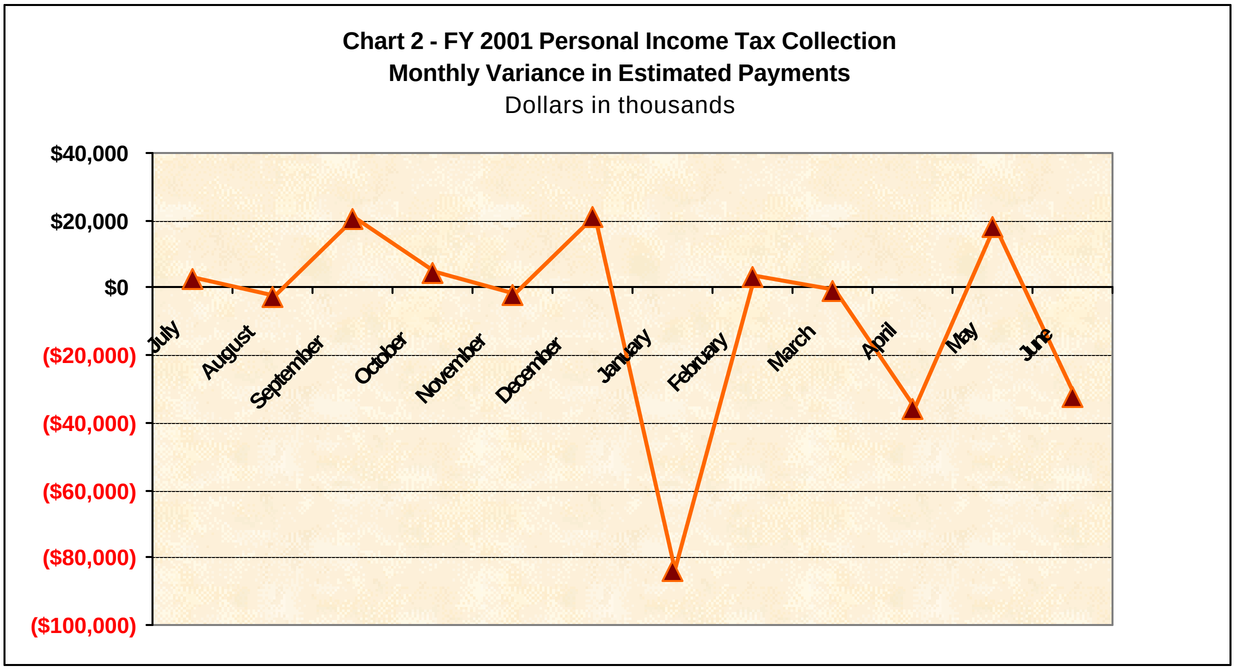
Withholding and quarterly estimated payments both contributed to the revenue shortfall. Total withholding (including revenue going to the local government funds as well as the GRF) was under estimate by $123.6 million or 1.7 percent for the year. Quarterly estimated payments were under by $87.4 million or 5 percent. Refunds were also less than anticipated ($64 million under estimate), offsetting some of the underage in withholding and quarterly estimated payments.

The underage in withholding should not come as a great surprise, given the recent weakness of the manufacturing sector and its importance to the state economy. Although Ohio data show only slight deterioration in the unemployment rate between June 2000 and 2001 (it increased from 4.1 to 4.2 percent over the same time period), the problem is the mix. While overall employment increased from 5,639,200 to 5,650,400 over this time period, manufacturing employment has fallen considerably (from 1,088,200 to 1,057,400). Slight gains were made in construction, trade, finance, insurance and real estate, and government sectors; and the service sector made substantial gains (employment increased from 1,592,800 to 1,617,700). But hours worked and the associated wage and salary make a difference.

According to the Cleveland Fed *Beige Book* (for March, May and June), economic activity was weak in the fourth district throughout the first half of 2001. The slowdown in manufacturing has persisted with no real end in sight. Hiring has eased (especially of temporary workers). Layoffs have continued and wage growth has slowed. Although labor markets continued to soften through the period, companies have been hanging on to highly skilled workers: offering time off and reduced hours. After struggling to find qualified workers during the tight labor market of the nineties and spending heavily to upgrade the education and skill levels of the more marginal workers, businesses are in no hurry to cut their workforce. So the deterioration in Ohio personal in-

Chart 1 - FY 2001 Personal Income Tax Collection
Monthly Variance in Withholding
Dollars in thousands





come and personal income tax collections is not as bad as it could have been. On the other hand, with excess capacity, employers have been unwilling to invest, which prolongs the slowdown.

Charts 1 and 2 show the monthly variances in withholding and quarterly estimated payments for FY 2001. For most of the first half of the year, withholding was over estimate. December cutbacks in employment, however, particularly in manufacturing, resulted in a negative variance that month. As employment continued to falter, the underage basically grew for the rest of the year.

With fewer employed and fewer hours worked, withholding fell short of the estimate. At the same time, the falling stock market led to a reduction in quarterly estimated payments. Quarterly estimated payments had been over estimate for most of the year until January's $83 million underage wiped that out. Up until that time, the vacillations of the stock market were generally taken in stride, and taxpayers were apparently betting on a year-end rebound. When no such rebound materialized, January's quarterly estimated payments dissipated, as well, coming in $83 million (15 percent) short of the estimate. Again, the overage in May was more than offset by shortfalls in April and June.

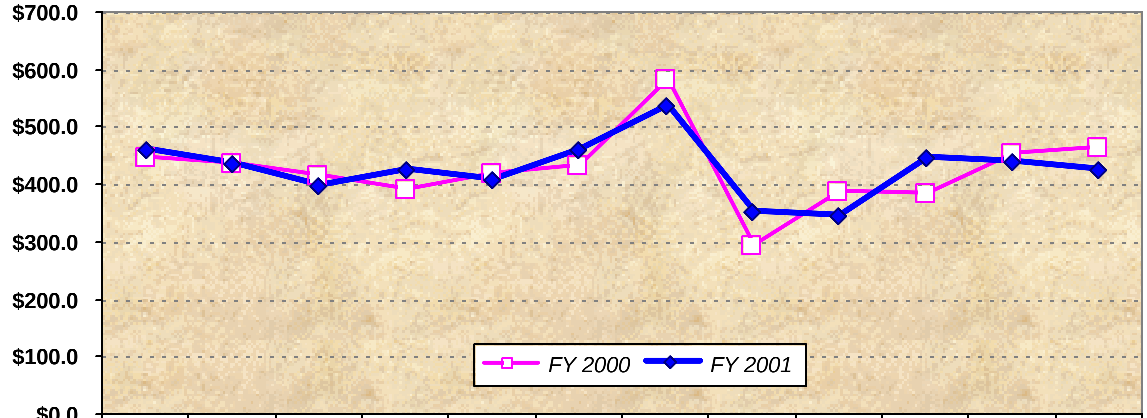
Nevertheless, in spite of the poor performance of the personal income tax, it was up 0.43 percent from a year ago. Withholding was up 4 percent; and quarterly estimated payments were up 2 percent. On the other hand, annual returns were down 7 percent. This may be accounted for by the 6.96 percent tax cut that Ohioans received as a result of the budget surplus at the end of FY 2000. Taking the tax cut into consideration, annual returns were virtually on target for the year ($4.8 million over estimate.)

Sales and Use Tax

After a surplus of nearly $210 million during FY 2000, the sales tax simply deflated in FY 2001, ending the year with a shortfall of $239 million. The faltering economy, the worrisome stock market, and later in the year, mass layoff announcements made consumers more cautious. High fuel prices also entered the equation – high gasoline prices in the summer and high natural gas prices in the winter made sizeable dents in consumer wallets, but these are generally not taxable under the sales tax. To the extent that households were willing to spend money, their money went to buy different things in FY 2001 than in FY 2000. And more of those FY 2001 things were not in the Ohio sales tax base.

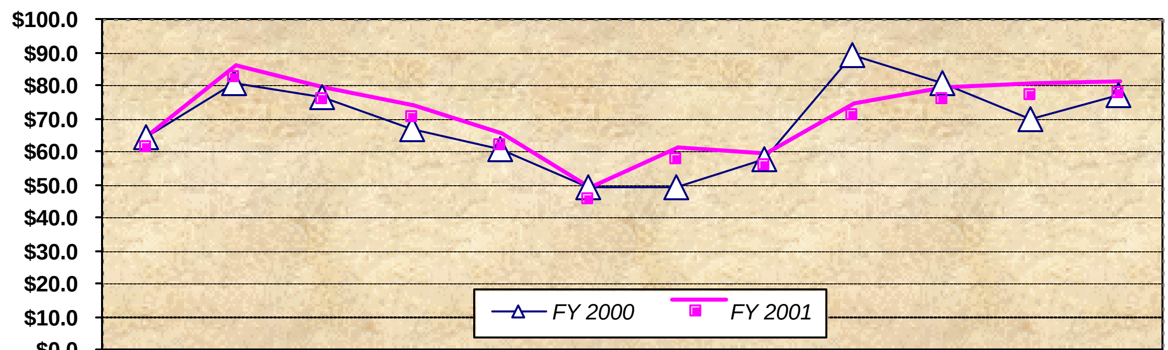
On a year-over-year basis, sales tax revenues grew by only 0.4 percent in FY 2001. (Between FY 1995 and FY 1999 the average growth rate was 5.3 percent. In FY 2000, it reached 6.6 percent.) The non-auto portion grew by 0.6 percent; while the auto portion fell by 1.2 percent coming off of FY 2000's 8.1 percent growth rate. Charts 3 and 4 compare monthly sales tax receipts for both non-auto and auto for fiscal years 2000 and 2001.

Chart 3
Non-Auto Sales and Use Tax Revenue
Monthly Receipts
Dollars in Million



	July	Aug.	Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	March	April	May	June
FY 2000	$444.4	$435.6	$413.0	$390.4	$419.4	$430.4	$581.4	$291.3	$387.6	$384.0	$451.4	$463.1
FY 2001	$458.0	$434.6	$396.7	$423.8	$409.0	$459.3	$537.5	$350.3	$344.6	$447.0	$438.4	$424.9

Chart 4
Auto Sales and Use Tax Revenue
Monthly Receipts
Dollars in Million



	July	Aug.	Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	March	April	May	June
FY 2000	$64.3	$80.8	$76.5	$66.9	$60.5	$48.9	$49.3	$57.8	$89.1	$80.8	$69.8	$77.0
FY 2001	$61.0	$82.3	$75.6	$70.1	$61.6	$45.7	$57.7	$55.9	$71.1	$75.9	$77.0	$77.6

Non-auto sales. The non-auto sales tax had a particularly disappointing year. It ended FY 2001 almost $221 million under estimate. It was under estimate every month of the year except December, February, and April (generally reflecting retail sales in November, January, and March). Particularly large shortfalls came in January and June. January receipts were $77 million under estimate, underscoring just how dismal the holiday shopping season was for retailers. The unusually cold December weather did not help either. Bad weather was also a factor in June's $56 million underage. May was an exceptionally cold and rainy month, which put a damper on apparel shopping, in particular.

December's overage may reflect the impact of the relatively long post-Thanksgiving shopping season in November. February's reflects the stronger than expected retail sales in January. Deep discounting along with milder weather after the holidays induced

Table 3
General Revenue Fund Income
Actual vs. Estimate
Month of June, 2001/Fiscal Year-to-Date 2001
($ in thousands)

REVENUE SOURCE					
TAX INCOME	**Actual**	**Estimate***	**Variance**	**FY 2000**	**Percent Change**
Auto Sales	$811,468	$830,000	($18,532)	$821,654	-1.24%
Non-Auto Sales & Use	$5,124,113	$5,345,001	($220,888)	$5,092,029	0.63%
Total Sales	$5,935,581	$6,175,001	($239,420)	$5,913,683	0.37%
Personal Income	$7,263,434	$7,380,660	($117,226)	$7,231,994	0.43%
Corporate Franchise	$915,259	$950,000	($34,741)	$969,398	-5.58%
Public Utility	$640,547	$575,001	$65,546	$642,112	-0.24%
Kilowatt Hour Excise Tax	$22,806	$25,000	($2,194)	$0	—
Total Major Taxes	**$14,777,627**	**$15,105,662**	**($328,035)**	**$14,757,187**	**0.14%**
Foreign Insurance	$220,563	$250,001	($29,438)	$252,316	-12.58%
Domestic Insurance	$109,292	$92,000	$17,292	$88,161	23.97%
Business & Property	$9,498	$7,503	$1,995	$8,673	9.51%
Cigarette	$282,481	$280,000	$2,481	$287,709	-1.82%
Soft Drink	$0	$0	$0	$0	-100.00%
Alcoholic Beverage	$55,032	$55,002	$30	$55,276	-0.44%
Liquor Gallonage	$28,999	$28,000	$999	$28,500	1.75%
Estate	$166,005	$160,000	$6,005	$139,953	18.61%
Racing	$0	$0	$0	$0	—
Total Other Taxes	$871,870	$872,506	($636)	$860,588	1.31%
Total Taxes	**$15,649,497**	**$15,978,168**	**($328,671)**	**$15,617,776**	**0.20%**
NON-TAX INCOME					
Earnings on Investments	$153,339	$115,000	$38,339	$122,516	25.16%
Licenses and Fees	$32,910	$35,000	($2,090)	$33,673	-2.26%
Other Income	$181,737	$165,002	$16,735	$110,963	63.78%
Non-Tax Receipts	$367,986	$315,002	$52,984	$267,151	37.74%
TRANSFERS					
Liquor Transfers	$102,000	$93,000	$9,000	$95,000	7.37%
Budget Stabilization	$0	$0	$0	$0	—
Other Transfers In	$661,927	$556,300	$105,627	$341,185	94.01%
Total Transfers In	$763,927	$649,300	$114,627	$436,185	75.14%
TOTAL INCOME less Federal Grants	**$16,781,409**	**$16,942,470**	**($161,061)**	**$16,321,113**	**2.82%**
Federal Grants	$4,527,831	$3,928,903	$598,928	$3,729,547	21.40%
TOTAL GRF INCOME	**$21,309,240**	**$20,871,373**	**$437,867**	**$20,050,659**	**6.28%**

* July, 2000 estimates of the Office of Budget and Management.
Detail may not add to total due to rounding.

shoppers to return to the stores in January. The growing use of gift certificates and gift cards has likely moved some retail sales from December to January. Finally, household refinancing due to interest rate cuts reached its peak in Ohio in late February and early March. This freed up cash for some large-ticket items and home improvements; the sales of which in March may help explain the April sales tax overage.

For the first half of the fiscal year, retail sales were on a slow but even keel – with chain store sales growing at a little over 4 percent on a year over year basis. However, December sales fell to just 0.7 percent over last December's level, and performance has been pretty erratic since then with May sales (the basis for June sales tax receipts) ending at just 1.5 percent over last year.

The same slowdown in personal income growth in October and November that led to underages in withholding in November has been blamed for December's weak consumption figures. The stock market dive of the fourth quarter of 2000 has also been blamed for the declining retail sales, as people who feel poorer are not likely to spend as much or to commit to large purchases. This has become known as the negative wealth effect. It is not clear to what extent it has been a factor in the slow down in retail sales, since the declining personal income level does a perfectly good job of explaining the phenomenon.

Sales of clothing and accessories, shoes, and general merchandise items were especially weak this spring. Higher end apparel stores were particularly hard hit, along with department stores. On the other hand, drug stores and wholesale clubs did well, with chain store sales posting average monthly year-over-year growth rates of 10.1 percent and 5.6 percent, respectively, for the January through June 2000 period. The average growth rate for the index of chain store sales activity was 3 percent. Apparel stores fell by 2.8 percent.[1]

Other than necessities and value-priced items, households have been putting more of their money into residential homes – particularly new homes. In fact, FY 2001 is likely to be a record year for new home sales, which will ultimately bode well for the furniture market.

Ordinarily, declining levels of consumer confidence would undermine the residential housing market, not bolster it. But with both interest rates and stock prices falling, houses are not only more affordable; they are also a reliable, low-risk refuge for individual wealth.

Auto sales. The auto sales tax finished the year $18.5 million under estimate. It was down by 1.24 percent off the heights of FY 2000.

Nationwide, vehicle sales have beaten all expectations. Except for December's poor performance (due largely to extremely cold weather), monthly sales have surpassed a seasonally adjusted annualized rate of 16.5 million all year long – coming in in June at a rate of 17.1 million vehicles. While sales are unlikely to meet the record sales level of 2000 or the near-record level of 1999, calendar year 2001 may still result in the third highest sales level in history.[2] Falling fuel prices and generous incentives peppered with new models to keep interest up have helped maintain this level of sales.

The situation in Ohio is a little less sanguine. While lower interest rates have generally increased borrowing, in areas experiencing significant layoffs from local steel manufacturers and other employers, the demand for new loans is a lot weaker. Also, the high gasoline prices of the first part of FY 2001 dampened sales. However, auto sales have been improving compared to the start of year – most likely due to the lower gas prices. Not coincidentally, the auto sales tax came in over estimate in both May and June.

Public Utility Excise Tax

The public utility excise tax ended the year $65.5 million over estimate. At the same time, FY 2001 revenues were 0.2 percent lower than FY 2000 revenues. The reason for the anomaly is that last biennium major changes were made in the public utility taxes. The changes began to take effect during FY 2001.

Among other changes, Am. Sub. S.B. 3 of the 123rd G.A. removed electric companies from the public utility excise tax and imposed a kilowatt-hour tax to replace the revenue. Electric companies made their last excise tax payment in May 2001 (a short payment: 75 percent of what it otherwise would have been) and their first payment of the kilowatt-hour tax in June. (The GRF portion of the first payment of the kilowatt-hour tax was $2.2 million under estimate.) Comparing FY 2001 excise tax plus kilowatt-hour tax receipts with FY 2000 excise tax receipts, the public utility taxes grew 3.3 percent in FY 2001.

Am. Sub. H.B. 283 of the 123rd G.A. made another change to the public utility excise tax. It took natural gas utilities off of the annual basis of the tax and put them on a quarterly basis. At the time that the change was made, it was assumed that the shift would result in a loss of revenue to the GRF. This was because the change in tax base also shifted the base forward. On top of that, the natural gas excise tax base was declining. Due to the choice program, some households and businesses were purchasing natural gas from dealers rather than utilities. These purchases were subject to the sales tax rather than the excise tax. Also, at the time, the price of natural gas was low and was expected to stay low. So much for expectations.

As it was, any anticipated decline in the base was more than offset by the colder than normal November and December that we experienced this past year along with the much higher price of natural gas.

While natural gas sales contributed to the overage in the excise tax, they were not the only reason. Excise tax revenues from electric companies and telephone companies remained on the annual basis, and thus reflected economic activity from the May 1999 to April 2000 period. The high level of industrial activity increased electric usage; and the expanding telecommunications industry increased receipts from local telephone companies.

Due to the anticipated decline in natural gas tax revenues, H.B. 283 called for an advanced payment of the public utility tax in June 2001 by any natural gas utility that had more than 30,000 open access customers by July 1, 1999. One utility qualified: Columbia Gas of Ohio. As a result, on the last day of FY 2001, the GRF received an additional $9.8 million in public utility tax revenue. Removing this extra payment from the FY 2001 receipts, public utility receipts grew by only 1.8 percent over FY 2000. (Columbia – now NiSource – will be reimbursed over time for its "advanced payment" in the form of a tax credit.)

FY 2001 was a transition year for the public utility excise tax. Revenues from the tax will be much lower in subsequent years. The electric companies, which previously constituted 64 percent of the tax base, have been removed from the base. Local telephone companies are the largest segment that will continue to pay the tax on an annual basis. Natural gas companies will remain subject to the tax but will continue to experience base erosion. As a result of the higher natural gas prices this winter, more households signed up for the natural gas "choice" program, hoping to purchase natural gas from a non-utility at a lower price. At whatever price, this gas will be subject to the sales tax not the public utility excise tax. (Although utilities will still provide transportation of natural gas and that will still be subject to the excise tax.) Consequently, natural gas public utility excise tax revenues will most likely decline.

Non-tax Revenue

Federal reimbursements were the largest source of non-tax revenues, providing 21 percent of FY 2001 revenues. That was larger than any other source except for the personal income tax and the sales tax. The $599 million overage was linked to the overage in Medicaid and TANF spending, as discussed in the Fiscal Overview.

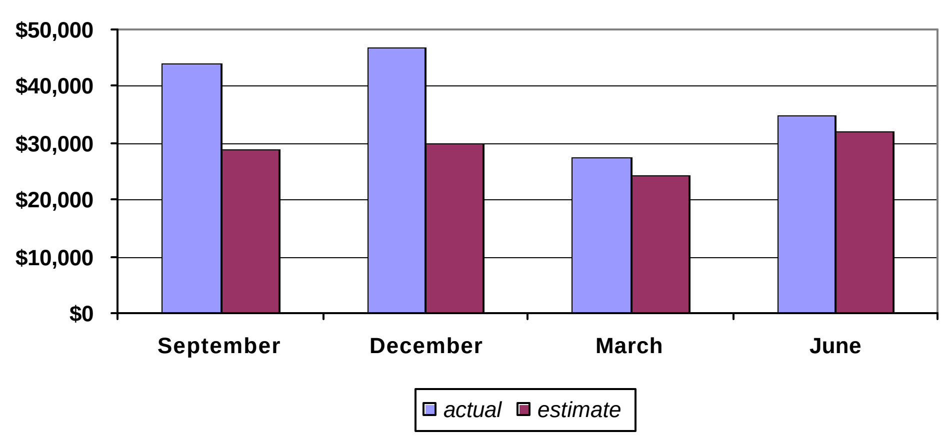
"Other transfers in" was the next largest source of non-tax revenue. The largest component of this was the big transfer from the income tax reduction fund (ITRF). The GRF received $546.3 million in January to help fund its share of the $610.4 million tax cut. The remainder was transferred to the local government funds. The transfer had no impact on the variance, since it was fully anticipated. However, it did help to prop up the fund balance.

Earnings on investments provided $38.3 million dollars over estimate to the GRF. The GRF receives revenue from investments four times throughout the fiscal year. Table 5 shows the revenues from this source in FY 2001. The high interest rates in the first

Earnings on Investments

	Actual	Estimate
September	$44,189	$28,750
December	$47,005	$29,900
March	$27,347	$24,150
June	$34,798	$32,200

Chart 5 - Earnings on Investments in FY 2001
Dollars in thousands



half of the fiscal year produced significant earnings overages in September and December. In March, the lower interest rate, along with the lower fund balance in the third quarter, brought down actual revenues and reduced the variance (although it was still positive). As the fund balance grew, so did June receipts, but the now lower interest rates continued to keep earnings closer to the estimate. ❑

[1] The "Chain Store Sales Index" tracks the trends among different categories of retailers. LSC obtained the index information from Economy.com's *The Dismal Scientist* website.

[2] Sophia Koropeckyj, "Vehicle Sales," *The Dismal Scientist*, www.dismal.com, July 5, 2001 (accessed July 17, 2001).

DISBURSEMENTS

*— Jeffrey E. Golon**

The state's finances during the latter half of FY 2001 experienced two contrasting pressures. The first, and most obvious pressure, was exerted by the state's Health Care/Medicaid program, which due to rising caseloads and health care costs, required considerably more in GRF funding than originally forecast and thus drove spending higher. The second, and contrary, pressure was the requirement that certain state agencies and programs cut their authorized FY 2001 expenditures, not only in order to help fund the ongoing escalation of Health Care/Medicaid costs, but also as a more general response to softening economic conditions and lower than forecast state revenues.

Two important points need to be emphasized. First, temporary law contained in Sub. S.B. 346 passed by the 123rd General Assembly last fall required the Office of Budget and Management (OBM) to take action that would reduce authorized FY 2001 expenditures by at least $125.0 million as part of the plan to provide supplemental funding to the Medicaid program. By the close of February 2001, OBM had taken that action and in fact managed to reduce authorized FY 2001 expenditures by $126.6 million, or $1.6 million more than the temporary law provision required. And then in April, state agencies experienced another round of mandatory expenditure reductions ordered by the Governor in response to state revenue collections that continued to track lower than forecast. Thus, by the end of FY 2001, many state agencies and programs generated underages that, at least in part, represented their required contribution to reducing overall expenditures.

Second, as of January 2001, OBM revised all of its original FY 2001 disbursement estimates for the Department of Job and Family Services (JFS), which includes the following four functional reporting or program categories: (1) Health Care/Medicaid, (2) Temporary Assistance to Needy Families (TANF), (3) General/Disability Assistance (GA/DA), and (4) Other Welfare. We opted not to follow suit, but, as has been this publication's practice for many years, continued to use the original FY 2001 disbursement estimates as our base of comparison to actual disbursements. As a result, with regard to discussing JFS year-end disbursements, this publication and OBM's Monthly Financial Report were written from different perspectives, and for the readers of both, finding common points of reference will no doubt be somewhat problematic.

This article takes two different looks at the state's FY 2001 disbursement activity. First, we examine the most notable state agency budgets and programs that came to bear on the year-end disbursement variance. Second, we close with a brief outline of the state's disbursement dynamics as they unfolded over the twelve months of FY 2001 (July 2000 through June 2001).

I. Year-End Disbursement Variance

At the close of FY 2001, excluding transfers, the state was holding a $506.2 million positive year-end disbursement variance, over the $20.64 billion spending estimate by 2.5 percent. The overage was principally the work of the Health Care/Medicaid program, where caseloads and related costs were rising, monthly overages had become the norm, and a looming budgetary shortfall had been staved off by a rather substantial infusion of supplemental state and federal funding. More distant secondary factors in the year-end overage included: (1) several appropriation increases in the Department of Job and Family Services' GRF budget that were unrelated to fixing the Health Care/Medicaid shortfall and spiked spending over the original FY 2001 disbursement forecast, and (2) the timing of the release of $30-plus million in capital funding earmarked for various rural and urban community assistance projects.

Our discussion of the state agency budgets and programs that contributed to the state's year-end overage, arranged in order of the magnitude of their contribution, appears immediately below. It is followed by a discussion of ten notable year-end underages. The reader's attention is also directed to Table 4, which provides a more detailed picture of the year-end disbursement variances by program category.

Health Care/Medicaid. For the year, the Health Care/Medicaid program, which includes the Children's Health Insurance Plan (CHIP-II) program,

Table 4
General Revenue Fund Disbursements
Actual vs. Estimate
Fiscal Year-End 2001
($ in thousands)

USE OF FUNDS PROGRAM	Actual	Estimate*	Variance	FY 2000	Percent Change
Primary & Secondary Education (1)	$5,554,127	$5,562,612	($8,485)	$5,132,187	8.22%
Higher Education	$2,518,790	$2,556,103	($37,313)	$2,432,758	3.54%
Total Education	$8,072,917	$8,118,715	($45,798)	$7,564,945	6.71%
Health Care/Medicaid	$6,505,689	$5,879,983	$625,706	$5,525,570	17.74%
Temporary Assistance to Needy Families (TANF)	$928,871	$837,571	$91,301	$863,735	7.54%
General/Disability Assistance	$71,442	$64,250	$7,191	$59,676	19.71%
Other Welfare (2)	$527,069	$516,977	$10,092	$449,245	17.32%
Human Services (3)	$1,114,126	$1,150,073	($35,947)	$1,130,086	-1.41%
Total Welfare & Human Services	$9,147,196	$8,448,854	$698,343	$8,028,311	13.94%
Justice & Corrections	$1,814,004	$1,852,624	($38,619)	$1,750,784	3.61%
Environment & Natural Resources	$129,593	$131,109	($1,516)	$135,976	-4.69%
Transportation	$39,799	$43,039	($3,240)	$41,540	-4.19%
Development	$180,591	$188,696	($8,105)	$133,864	34.91%
Other Government (4)	$379,413	$466,091	($86,678)	$368,959	2.83%
Capital	$50,759	$21,117	$29,642	$17,427	191.27%
Total Government Operations	$2,594,159	$2,702,675	($108,516)	$2,448,551	5.95%
Property Tax Relief (5)	$1,119,191	$1,151,406	($32,214)	$1,055,427	6.04%
Debt Service	$210,700	$216,333	($5,633)	$146,385	43.94%
Total Program Payments	**$21,144,164**	**$20,637,982**	**$506,182**	**$19,243,619**	**9.88%**
TRANSFERS					
Local Govt Distribution	$0	$0	$0	$0	——
Budget Stabilization	$49,200	$49,200	$0	$46,400	6.03%
Other Transfers Out	$805,025	$621,692	$183,333	$766,956	4.96%
Total Transfers Out	$854,225	$670,892	$183,333	$813,356	5.02%
TOTAL GRF USES	**$21,998,389**	**$21,308,874**	**$689,515**	**$20,056,975**	**9.68%**

(1) Includes Primary, Secondary, and Other Education.
(2) Includes the Department of Job & Family Services, exclusive of Medicaid, TANF, and General/Disability Assistance.
(3) Includes Mental Health, Mental Retardation and Developmental Disabilities, and Other Human Services.
(4) Includes Regulatory and Nonregulatory agencies, Pension Subsidies, and Reissued Warrants.
(5) Includes property tax rollbacks, homestead exemption, and tangible property tax exemption.

* August, 2000 estimates of the Office of Budget and Management.

Detail may not add to total due to rounding.

posted disbursements that were $625.7 million, or 10.6 percent, above estimated spending of $5.88 billion. All of the Health Care/Medicaid service categories contributed to pushing the program's FY 2001 disbursements above the estimate. In order of magnitude, the most important service category contributors were as follows: (1) Nursing Homes ($126.7 million), (2) Hospitals ($126.4 million), (3) Prescription Drugs ($95.4 million), and (4) All Other ($94.3 million). The overages in the program's various service categories largely reflected the combination of two factors: (1) higher than anticipated caseloads across all eligibility categories, in particular Covered Families and Children, and (2) higher than expected health care cost growth, in particular for prescription drugs. (A more detailed visual picture of FY 2001 Health Care/Medicaid disbursement activity, as well as a spending comparison with FY 2000, is contained in Table 5.)

Of particular note was the overage posted by the CHIP-II program, which provides medical coverage for uninsured children under age 19 in families with incomes between 150 percent and 200 percent of the

Table 5

Health Care Spending in FY 2001

Medicaid (600-525)*

Service Category	FY 2001 Actual** July 00 - June 01	FY 2001 Estimate** July 00 - June 01	Variance	Percent Variance	FY 2001[3] Actual** July 00 - June 01	FY 2000[3] Actual** July 99 - June 00	Variance	Percent Variance
Nursing Homes	$2,265,633,923	$2,138,944,136	$126,689,787	5.9%	$2,265,633,923	$2,110,779,043	$154,854,880	7.3%
ICF/MR	$383,170,575	$352,776,921	$30,393,654	8.6%	$383,170,575	$352,235,439	$30,935,137	8.8%
Hospitals	$1,481,721,718	$1,355,335,040	$126,386,678	9.3%	$1,481,721,718	$1,261,297,915	$220,423,804	17.5%
Inpatient Hospitals	$1,070,106,273	$992,103,914	$78,002,359	7.9%	$1,070,106,273	$938,775,777	$131,330,496	14.0%
Outpatient Hospitals	$411,615,445	$363,231,126	$48,384,319	13.3%	$411,615,445	$322,522,137	$89,093,308	27.6%
Physicians	$419,449,250	$353,965,393	$65,483,857	18.5%	$419,449,250	$323,345,086	$96,104,164	29.7%
Prescription Drugs	$860,560,524	$765,146,194	$95,414,330	12.5%	$860,560,524	$669,107,626	$191,452,898	28.6%
Payments	$1,053,849,198	$943,242,939	$110,606,259	11.7%	$1,053,849,198	$840,075,404	$213,773,794	25.4%
Rebates	($193,288,675)	($178,096,745)	($15,191,930)	8.5%	($193,288,675)	($170,967,778)	($22,320,896)	13.1%
Waiver[1]	$141,359,520	$124,059,447	$17,300,073	13.9%	$141,359,520	$121,941,312	$19,418,208	15.9%
HMO	$422,565,428	$381,307,737	$41,257,691	10.8%	$422,565,428	$360,397,168	$62,168,260	17.2%
Medicare Buy-In	$120,370,318	$115,538,650	$4,831,668	4.2%	$120,370,318	$121,342,841	($972,523)	-0.8%
All Other***	$537,791,329	$443,469,503	$94,321,826	21.3%	$537,791,329	$405,008,166	$132,783,163	32.8%
DSH offset	($156,886,651)	($159,316,221)	$2,429,570	-1.5%	($156,886,651)	($199,884,845)	$42,998,194	-21.5%
Total (525) w/o CHIP-II payment	**$6,475,735,935**	**$5,871,226,800**	**$604,509,135**	10.3%	**$6,475,735,935**	**$5,525,569,750**	**$950,166,185**	17.2%
CAS	$6,481,100,337							
Est. Federal Share	$3,807,085,156	$3,451,694,236	$355,390,921		$3,807,085,156	$3,228,590,405	$578,494,751	17.9%
Est. State Share	$2,668,650,779	$2,419,532,564	$249,118,215		$2,668,650,779	$2,296,979,345	$371,671,434	16.2%
CHIP-II Payment	$5,703,558				$5,703,558			
Total (525) w/ CHIP-II payment	**$6,481,439,493**	**$5,871,226,800**	**$610,212,693**	10.4%	**$6,481,439,493**	**$5,525,569,750**	**$955,869,743**	17.3%
CAS	$6,481,100,337				$6,481,100,337			
Est. Federal Share	$3,811,139,245	$3,451,694,236	$359,445,010		$3,811,139,245	$3,248,482,456	$562,656,789	
Est. State Share	$2,670,300,248	$2,419,532,564	$250,767,684		$2,670,300,248	$2,277,087,294	$393,212,954	

Children's Health Insurance Plan (CHIP-II), (600-426)*[2]

Total (426)	$23,935,737	$8,756,229	$15,179,508	173.4%
Est. Federal Share	$17,013,522	$6,223,928	$10,789,594	
Est. State Share	$6,922,215	$2,532,301	$4,389,914	
TOTAL Health Care	***$6,505,375,230***	***$5,879,983,029***	***$625,392,201***	***10.6%***

* This portion of the table only includes Medicaid spending through Job & Family Services' line item 600-525 and the former HUM line item 400-525.

** Includes spending from prior year encumbrances in the "All Other" category.

*** "All Other," includes all other health services funded by line item 600-525.

1. Waivers provide home care alternatives to consumers whose medical conditions/functional abilities would otherwise require Long Term Care facility residence. Prior to FY 2001, reported in "All Other" category.

*2 This portion of the table only includes CHIP-II spending through Job & Family Services' line item 600-426. CHIP-II, effective 7/1/2000, provides health care coverage for children under age 19, with family incomes between 150-200% of FPL.

3. CHIP/HS Phase I service payments are rolled into line item 600-525 for FY 2001. For FY 2000, total CHIP/HS-1 spending of $66.6 million occurred through HUM line items 400-671 and 400-623.

Note: In the comparison of FY 2001 to FY 2000 actuals, this table does not include CHIP-II since it was implemented in FY 2001.

Source: BOMC8300-R001, BOMC8350-R001&R002 Reports, Ohio Department of Job & Family Services.

federal poverty level (FPL). CHIP-II not only exhausted all of its FY 2001 GRF appropriation of $23.9 million (line item 600-426); it did so with just under two months of the fiscal year still left to go. For the remainder of the fiscal year, the Department of Job and Family Services covered CHIP-II's obligations by tapping into its Medicaid funding (line item 600-525), payments that totaled $5.7 million. Thus, the true CHIP-II year-end overage was $20.9 million ($15.2 million CHIP-II funding + $5.7 million Medicaid funding), in excess of the estimate by 238.5 percent. (Even though the federal reimbursement rate (FMAP) for Medicaid is lower than CHIP-II's (Enhanced FMAP), the department does not expect that the need to supplement CHIP-II's budget by using $5.7 million in Medicaid funding will result in a reduction in federal reimbursement revenue. The expectation is that the federal government will reimburse the state on that expenditure of $5.7 million in Medicaid funding at the higher CHIP-II rate since the money was spent on CHIP-II activity.)

The program's FY 2001 disbursement story also featured a large and important planned accounting twist. The Department of Job & Family Services' original FY 2001 disbursement plan called for it to credit $159.3 million in non-GRF funding from its Institutions for Mental Diseases/Disproportionate Share Hospital (IMD/DSH) program against the Medicaid program's total spending for the month of February; it actually did not take place until May and was for a slightly lesser amount – $156.9 million.

In prior issues of this publication, we noted that the significance of the Health Care/Medicaid program's ongoing pattern of monthly overages that eventually led to the sizeable year-end overage was not lost on the executive and legislative branches of state government last fall, as it seemed to be sailing unwaveringly towards a fiscal crisis. In light of that fact, Sub. S.B. 346 was passed by the 123rd General Assembly, which, among other things, included supplemental funding designed to fix the Health Care/Medicaid program's projected budgetary shortfall. The financial fix totaled $634.8 million in additional FY 2001 GRF appropriation authority. The state share of that total was $236.9 million, with the remainder, or $397.9 million, being covered by federal reimbursement.

As a closing remark, it is important to note the larger context of our discussion of the Health Care/Medicaid program's year-end $625-plus million overage. The overage reflects a comparison to the program's original FY 2001 disbursement estimates that were in turn based on the program's available funding as of the start of the fiscal year (July 1, 2000). Thus, the program, as expected, prematurely exhausted its original available funding and what got it through the remainder of the fiscal year was the $634.8 million in supplemental GRF funding (state share plus federal share) provided last fall.

TANF. The Temporary Assistance to Needy Families (TANF) program closed with a year-end overage of $91.3 million, in excess of the $837.6 million spending estimate by 10.9 percent. This development was the direct result of FY 2001 appropriation increases in two of TANF's GRF components – line items 600-411, TANF Federal Block Grant ($161.1 million), and 600-413, Day Care Match/MOE ($12.7 million). As a result, the two line items were able to overshoot their year-end disbursement estimate by $81.5 million and $12.7 million, respectively. These increased appropriations were made to provide additional funding for consolidated county funding, supplemental Early Start and Workforce Investment activities, and day care.

What was the source of revenue for these appropriation increases? The $161.1 million increase in the TANF Federal Block Grant line item's appropriation was made up entirely of unappropriated federal TANF Block Grant funds. The $12.7 million increase in the Day Care Match/MOE line item's appropriation, however, had a less straightforward source, as it was drawn from money labeled "earned federal" that had resulted from the transfer of federal TANF Block Grant funds for use in the state's Social Services Block Grant. These funds were "earned federal" because they matched state expenditures that had already occurred. With their status of "earned federal," these funds became state money and could then be used in programs that match other federal dollars, in this case they were claimed as part of Ohio's maintenance of effort (MOE) requirement in the TANF program.

Although in this publication we typically stay focused on the variance from the executive branch's original disbursement estimates, it should be noted that TANF's FY 2001 disbursement estimates were revised for the second half of the fiscal year so as to reflect the substantial spending jump that would come from the TANF Federal Block Grant line item's $160-

plus million appropriation increase. If, rather than using the original FY 2001 disbursement estimates as a referent point, one were to examine TANF's actual FY 2001 GRF expenditures against these revised disbursement estimates, then the program closed not with a year-end $91.3 million overage, but with a year-end underage of $69.1 million. The program's year-end underage that results from using the revised FY 2001 disbursement estimates was almost entirely a function of two distinct parts of the TANF Federal Block Grant line item: (1) current year funding ($30-plus million), and (2) encumbered prior year appropriations ($40-plus million). Most of the unspent current (or FY 2001) funding was encumbered presumably for disbursement sometime during FY 2002, while virtually all of the unspent prior years' appropriations resulted from the cancellation of encumbrances, which essentially freed up previously obligated TANF Federal Block Grant money for other purposes.

Our review of TANF's year-end disbursement picture would not be complete without at least some mention of the program's cash assistance component known as Ohio Works First (OWF). At the close of FY 2001, the program's cash assistance caseload stood at 196,600 recipients, or 84,400 cash assistance groups. In comparison to the same point in time last year, the OWF caseload had declined by 50,000 cash assistance recipients, or nearly 14,000 cash assistance groups. These OWF caseload changes represented reductions of 20.3 percent in the number of cash assistance recipients and 14.2 percent in the number of cash assistance groups. While the overall number of cash assistance groups has declined, the number of children in "child only" cases has increased to the point that the latter constituted in excess of 45 percent of the total number of cash assistance groups. These are cases in which children are typically living with a relative other than a parent. Some "child only" cases may also occur when the parent is receiving assistance from another program and thus is not eligible for a TANF cash benefit.

Capital. For the year, the state's Capital program category posted disbursements that were in excess of the estimate by $29.6 million. The estimate assumed that $21.1 million in GRF capital appropriations would be disbursed in FY 2001, while the actual amount disbursed was noticeably larger at $50.7 million. As reported in prior issues of this publication, over the course of FY 2001, a rather sizeable chunk of capital funding earmarked for various rural and urban community assistance projects was released earlier than expected by the Controlling Board. Presumably, many of these capital earmarks were not anticipated to be released until FY 2002.

Job & Family Services. For FY 2001, disbursements for the Department of Job and Family Services' operating expenses and subsidy programs – exclusive of Medicaid, TANF, and General/Disability Assistance, which are tracked under separate components of the Welfare & Human Services program category, and inclusive of former Bureau of Employment Services programs – landed $10.1 million, or 2.0 percent, over the estimate. At the center of the disbursement variance were line items 600-416, Computer Projects, and 600-437, Temporary Heating Assistance for Warmth, with overages of $19.8 million and $13.2 million, respectively. The Computer Projects overage was not surprising given the fact that, last October, the department exercised permissive authority granted under the biennial budget to increase the available FY 2001 appropriation for computer projects from $104.0 million to $154.6 million, a bump of $50.6 million. This rather healthy appropriation increase came a few months after the original FY 2001 disbursement estimates were assembled. Thus, the department had considerably more money on hand for computer projects spending than had been assumed would be the case at the start of the fiscal year.

The Temporary Heating Assistance for Warmth overage was also tied to events that occurred after the original FY 2001 disbursement estimates had been assembled; in this instance it was Sub. H.B. 9 of the 124th General Assembly, which enacted a program effective March 2001 to provide assistance with the payment of winter heating expenses for persons not eligible for assistance under Title IV-A of the Social Security Act, and whose gross monthly income did not exceed 200 percent of federal poverty guidelines. House Bill 9 appropriated $20.0 million to the department's budget for this purpose. By year-end, $13.2 million of that total appropriation had been disbursed, and the remainder, $6.8 million, was encumbered and carried into FY 2002.

Two more distant contributors to the department's year-end overage were related to personal services ($3.1 million) and food banks ($2.5 million), reflecting yet again appropriation changes that were not built into the original FY 2001 disbursement estimates. The personal services overage involved a $15.0 million increase in the department's Personal Services line item, principally reflecting a change in how vendors who render Medicaid third-party liability recovery services are paid. The food banks overage was traceable to a $2.5 million lump sum distribution to the Ohio Association of Second Harvest Food Banks that was not built into the FY 2001 disbursement estimates.

The size of the department's year-end overage was in turn considerably muted by a collection of line item underages totaling $27.1 million, that included, in order of magnitude: electronic benefits transfer ($5.4 million), child support administration ($5.2 million), adoption services ($3.7 million), child and family services ($2.5 million), child protective services ($2.3 million), burial claims ($1.9 million), state refugee services ($1.8 million), non-TANF county administration ($1.7 million), maintenance ($1.4 million), and adult protective services ($1.2 million). Roughly one-half of this collection of underages, around $13.6 million, was traceable to the cancellation of prior years' encumbrances, which meant that the associated funding lapsed and became part of the state's GRF cash balance. Most of the remainder of these underages, approximately $11.2 million, was primarily tied to current year funding that was not disbursed as planned and had been encumbered for future disbursement.

GA/DA. At the close of FY 2001, the state's General Assistance/Disability Assistance program component was holding a $7.2 million positive year-end disbursement variance, over the estimate by 11.2 percent. The driving force in the disbursement variance was the Department of Job & Family Services' $74-plus million Disability Assistance (DA) program, a state- and county-funded effort that provides cash and/or medical assistance to persons ineligible for public assistance programs that are supported in whole or in part by federal funds.

The DA program overage was a function of two factors: (1) monthly cash assistance caseloads that consistently exceeded the forecast on which the biennial budget for the DA program was based, and (2) medical cost inflation that was higher than originally forecast, most notably in the area of prescription drugs. The majority of the DA program overage was traceable to this second factor: higher than expected medical costs.

After the first quarter of FY 2001 had passed, it was fairly clear to many budget watchers that the DA program was headed for a budgetary shortfall, a fate that the program also faced in FY 2000. That FY 2000 shortfall was addressed by a $2.1 million cash infusion, as well as by postponing some program expenditures until the start of FY 2001. The projected shortfall for FY 2001 was addressed last fall through Sub. S.B. 346 of the 123rd General Assembly, which, among other things, included $10.7 million in supplemental GRF funding for the DA program.

So as to not mislead the reader, an important part of the larger context of our discussion of the DA program's year-end overage needs to be clearly understood. The overage reflects a comparison to the program's original FY 2001 monthly disbursement estimates that were in turn based on its original annual appropriation of $63.7 million. Thus, although the program did prematurely exhaust its original FY 2001 appropriation, it managed to avoid a funding shortfall because of the $10.7 million in supplemental GRF funding provided last fall.

Of the revised FY 2001 appropriation totaling $74.4 million, the DA program disbursed $71.4 million, which was $7.7 million higher than its original appropriation. The remainder of the revised FY 2001 appropriation, roughly $3.0 million, was encumbered, presumably for disbursement sometime in early FY 2002.

Notable Underages. There were ten notable state agency and program underages totaling $221.0 million in the year-end disbursement picture, all of which are discussed below. As a group, these underages were driven, in order of magnitude, by: (1) excess funding, which represented appropriation authority that was not needed and had lapsed back into the FY 2001 GRF cash balance, (2) mandated reductions in authorized FY 2001 expenditures that were imposed on most state agencies in the latter half of the fiscal year, (3) timing-based delays in planned spending that led to the encumbrance of funding for disbursement sometime in FY 2002, and (4) a relatively sizeable, but essentially insignificant, accounting maneuver associated with the Controlling Board's appropriations.

Controlling Board. The Controlling Board's budget, which is buried within the catchall Other Government component of the Government Operations program category, chipped in a year-end underage totaling $51.9 million, all of which showed up in the month of June. While it looked relatively large, the year-end underage was in fact not very significant at all. It simply reflected the results of a device – built into the original disbursement estimates assembled last August by the Office of Budget and Management (OBM) – intended to account for the portion of the Controlling Board's total FY 2001 GRF appropriation that was expected to be transferred to other state agency budgets. As the reader may be aware, Controlling Board appropriations are not disbursed per se, but are transferred to, and then disbursed from, other state agency budgets.

Regents. The Board of Regents closed with a negative year-end disbursement variance of $37.3 million, an underage of only 1.5 percent in the context of a $2.56 billion spending estimate. The underage arose primarily from two line items: (1) 235-501, Instructional Subsidy ($20.0 million), and (2) 235-401, Lease Rental Payments ($11.3 million). Disbursements from the Instructional Subsidy line item, which contained $1.6 billion that funds a formula-based subsidy partially offsetting the costs of a college education, were lower than expected because of mandated reductions in FY 2001 expenditures ($16.5 million) in combination with the encumbrance of $3.5 million of reallocated doctoral reserve funding that will be distributed among state-assisted universities in early FY 2002. As of this writing, the reasons behind the underspending in the Lease Rental Payment line item were less clear, but could have been related to the restructuring of education-related debt service between general and special obligation bonds.

Also in the mix of year-end underages was the Ohio Instructional Grant (OIG) program (line item 235-503) with $6.5 million, a function of mandated reductions in FY 2001 expenditures in combination with fewer than expected eligible students. Further in the background were the National Guard Scholarship program (line item 235-599) and Student Workforce Development Grants (line item 235-534) with underages of $1.2 million and $1.0 million, respectively, as the FY 2001 amounts appropriated for each exceeded the need.

The effect of these underages on the Regents' negative year-end disbursement variance was in turn somewhat diluted by higher than expected spending in the Eminent Scholars program ($5.2 million) as well as the Student Choice Grant program ($2.8 million). In the case of the former, the program's entire FY 2001 appropriation of $5.2 million for endowing chairs at Ohio universities was disbursed earlier than anticipated and not encumbered for disbursement in FY 2002 as originally planned. In the case of the latter, a $2-plus million bump in the Student Choice Grant program's FY 2001 appropriation allowed it to overspend, as the growth in the number of private college enrollments, and thus the number of students eligible for tuition grant awards, was higher than expected.

Property Tax. For the year, the Property Tax Relief program landed with a $32.2 million underage, an amount that included $22.0 million in real property tax credits/exemptions funding and $10.2 million in tangible credits/exemptions funding. All of the underage represented a mix of unused and unneeded appropriation authority from FYs 2000 and 2001 that was left unencumbered at the close of the fiscal year and simply allowed to lapse back into the state treasury and become part of the GRF's cash balance.

Over the course of FY 2001, the departments of Education and Taxation disbursed $1.12 billion back to school districts, counties, municipalities, townships, and other special taxing districts as compensation for credits or exemptions provided to taxpayers under existing state law. The timing of these distributions depended heavily on how quickly the settlement process went at the local level and when county auditors applied to the state for relief payments. Not unexpectedly during FY 2001 that timing was off, and as a result, we witnessed large negative and positive disbursement variances in the Property Tax Relief program from one month to the next.

Rehabilitation & Correction. For the year, the Department of Rehabilitation & Correction's disbursements registered $24.4 million, or 1.8 percent, lower than originally forecast. The most notable contributor to the disbursement variance was a collection of $20.1 million in underages related to day-to-day prison operations and programs (personal services, maintenance, and equipment). The key factor in the departmental underage was the imposition of mandated reductions in authorized expenditures, a reality that most state agencies experienced during the latter half of FY 2001.

Administrative Services. At the close of FY 2001, the Department of Administrative Services held a negative year-end disbursement variance of $23.2 million, 15.1 percent below the estimate. The department's FY 2001 disbursement storyline itself tracked fairly close to our three previous year-end reports, as two components of its budget accounted for a huge portion of the underage (92.6 percent).

The first underage component contained $12.8 million tied to three line items that support the provision of computing and communications services to various state agencies. That mix of underspending included, in order of magnitude, line items: (1) 100-417, Multi-Agency Radio Communication System (MARCS), (2) 100-416, Strategic Technology Development Programs, and (3) 100-419, State of Ohio Synchronous Optical Network/Ohio SONET. With regard to each of these line item underages, the following factors appeared to come into play: (1) contractor disputes and difficulties in finding acceptable tower locations and arranging leases for those sites that hampered the initial roll-out of MARCS, (2) technology project delays that are to be expected but are also difficult to build into a timeline for completion, and (3) invoice reconciliations for fiber optic services provided by Ameritech that slowed Ohio SONET spending.

The second underage component contained three building rent and operating payment line items (100-433, 100-447, and 100-449) that chipped in $8.1 million. Factors behind the component's underage included smaller than anticipated debt service payments to the Ohio Building Authority, and lower than expected operating, renovation, and relocation expenditures in various state office buildings.

Mental Retardation. The Department of Mental Retardation & Developmental Disabilities closed FY 2001 with a negative year-end disbursement variance of $18.5 million, under estimated spending of $353.9 million by 5.2 percent. At the center of the underage was line item 322-413, Residential and Support Services, which largely dominated the department's FY 2001 disbursement picture. The line item, which carries funding to pay for services delivered to individuals with mental retardation or developmental disabilities, ended FY 2001 with a $14.9 million underage. The underspending was related to the difficulty in precisely predicting how long it will take the department to review and settle service provider payment requests, a process that in some instances can take up to three years. At year-end, most of this unspent Residential and Support Services funding had been encumbered by the department for disbursement in FY 2002.

The remainder of the department's year-end underage was traceable to: (1) line item 323-321, Residential Facilities Operations ($1.6 million), and (2) line item 322-414, Sermak Class Services (just shy of $1.0 million). The first of these line item underages was tied to the operating expenses of the department's 12 developmental centers, where in response to mandated reductions in authorized expenditures vacant staff positions went unfilled. The second of these line item underages involved unspent prior year funding related to the Sermak legal matter, a class action lawsuit that contested the appropriateness of placing certain individuals in nursing facilities. As a majority of those affected individuals have either been moved into one of the department's waiver programs or passed away, most of the remaining Sermak funding was not needed and thus allowed to lapse.

Youth Services. At year-end, the Department of Youth Services was holding a negative disbursement variance of $9.4 million, under the estimate by 3.9 percent. One key factor in the underage was the imposition of mandated reductions in authorized expenditures, a reality that affected most state agencies in the second half of FY 2001. Timing also seemed to play a role in the underage, as was evidenced by the fact that the department was carrying roughly $4.0 million more than was anticipated in funds encumbered for disbursement in the future. This meant that some of the department's existing FY 2001 financial obligations would not be paid for until FY 2002. The effect of these two factors was most noticeable on the department's expenditure of RECLAIM Ohio funding, a pool of money that is used to provide subsidies to juvenile courts and finance state-operated institutions.

Development. Timing was the key influence on the Department of Development's negative year-end disbursement variance of $8.9 million, an amount that was 6.4 percent shy of the estimate. The primary element in the underage was the department's Technology Action Grant program ($14.9 million), with a very distant secondary contribution from its Urban & Rural Initiative Grant program ($1.1 million). Exerting somewhat of a braking effect on the overall size of the underage were three areas of the department's budget that posted timing-based overages: (1) Business Development grants ($5.2 million), (2) Ohio Industrial Training grants ($1.3 million), and (3) Project 100 matching funds ($1.0 million).

Health. Several forces coalesced to constrain the Department of Health's expenditures and produce the resulting $8.4 million negative year-end disbursement variance, which was under the $95.2 million spending estimate by 8.8 percent. There were numerous underages littered throughout the department's budget, the most noticeable of which involved: (1) local health districts ($2.1 million), (2) health care policy and data ($1.2 million), (3) AIDS prevention and treatment ($970,000), (4) community-based child and family health services ($913,000), (5) quality assurance ($614,000), (6) public health prevention ($522,000), (7) immunizations ($470,000), (8) Ohio Early Start/Help Me Grow ($460,000), and (9) nursing home survey and certification ($448,000). In order of magnitude, the development of these underages was tied to: (1) the timing of various grants, contractor payments, and drug purchases, (2) a drop in operating costs largely the result of vacant staff positions, and (3) the mandated reduction in authorized expenditures that many state agencies experienced in the latter half of FY 2001.

Education. The Department of Education closed FY 2001 with a negative year-end disbursement variance of $6.8 million, or 0.1 percent, a microscopic underage when compared to the spending estimate of $5.42 billion. More than 20 line items in the department's GRF budget contributed to the underage, the most notable being the Disadvantaged Pupil Impact Aid/DPIA program ($27.8 million).

The $27.8 million underage in the DPIA Program was in large part tied to the fact that the level of participation in all-day, everyday kindergarten was less than what was projected would be the case in building the program's FY 2001 appropriation. Eligible school districts need to actually provide all-day, everyday kindergarten in order to receive state funding. The program's original appropriation assumed that all eligible school districts would provide this service to all of their kindergarten students, and that was not the case.

There were also two notable overages in the department's year-end disbursement picture: (1) the School Foundation Basic Allowance/Base Cost Funding program ($16.7 million), and (2) the Pupil Transportation program ($15.6 million).

The overage in the School Foundation Basic Allowance/Base Cost Funding program was largely a result of the department's response to a shortfall in lottery profits. The shortfall meant that $53.1 million less than had been projected would be available for transfer into the Lottery Profits Education Fund to be used as part of the Base Cost Funding program in FY 2001. To cover that funding shortfall, the department: (1) received Controlling Board approval in June to transfer $22.4 million from various departmental GRF line items into the Base Cost Funding line item (200-501) and $18.0 million from the Lottery Profits Education Reserve Fund into the Lottery Profits Education Fund's Base Cost Funding line item (200-612), and (2) tapped into a surplus in the GRF Base Cost Funding line item earmark for additional special education cost reimbursements. In FY 2001, $14.0 million was set-aside within the GRF Base Cost Funding line item to provide additional state subsidies for the cost of certain eligible special education students that exceeded $25,000 per pupil. The department estimated that $12.5 million of that earmark would not be needed for special education cost reimbursements, and was thus available to help in alleviating the fiscal problem created by the lottery profits shortfall.

In FY 2001, the purpose of the two Base Cost Funding line items was to create a pool of funding that would equalize state subsidies to school districts (including joint vocational school districts), and among other things, guarantee $4,294 in per pupil base cost funding with the cost of doing business factor adjustment in combined state and local revenues at 23 mills (the local charge-off millage rate is 0.5 mills for joint vocational school districts), and fund the state share of special and vocational education weight costs.

The overage in the Pupil Transportation program was largely due to the fact that school districts reported higher than expected student transportation expenditures, which in turn meant that the state would need more funding than had been appropriated ($290-plus million) to reimburse school districts for a portion of their operating costs associated with transporting students. To cover what would otherwise have been a funding shortfall in the last month of the fiscal year, the Controlling Board approved a

June transfer of $15.9 million from various departmental GRF line items into the Pupil Transportation program.

Prior Years' Funding. The department entered FY 2001 carrying $166.3 million in GRF funds that had either been encumbered or were part of an available appropriation balance from prior fiscal years, some of which dated back to FY 1996. At year-end, of that total, $60.8 million, or 36.5 percent, had been disbursed, $58.3 million, or 35.0 percent, had been transferred into FY 2001, $15.7 million, or 9.5 percent, was still encumbered for future disbursement, and $31.5 million, or 19.0 percent, had been cancelled and allowed to lapse back into the state treasury to become part of the GRF cash balance.

The GRF fund transfers included: (1) pursuant to Controlling Board approval last December, the movement of $30.0 million in unneeded FY 2000 Base Cost Funding into FY 2001 for the department's Desegregation program in order to cover the state's full and final payment to the Dayton City School District as part of tentative agreement to settle the case of *Brinkman v. Gilligan*, (2) pursuant to Am. H.B. 181 of the 124th General Assembly and Controlling Board approval, the movement of $17.5 million in obligated but unexpended GRF appropriations from prior fiscal years into the 12th Grade Proficiency Stipend program, (3) pursuant to temporary law in Am. Sub. H.B. 282 of the 123rd General Assembly, the movement of $4.0 million of the Maintenance and Equipment line item's unencumbered FY 2000 balance into FY 2001 to pay the cost of the department's move from the Ohio Departments Building, and (4) pursuant to Am. Sub. H.B. 640 of the 123rd General Assembly, the movement of $4.9 million of the Teacher Incentive Grants line item's unexpended and unencumbered balance to supplement available FY 2001 appropriations used to provide one-time incentive grants to qualified reading, mathematics, and science teachers.

Current Year Encumbrances. In addition to the previously mentioned $15.7 million in prior years' encumbrances that the department was still holding at the close of the fiscal year, it had also encumbered $127.0 million in FY 2001 appropriations for future disbursement. This total included: (1) Base Cost Funding ($36.4 million), (2) Desegregation Costs ($32.5 million), (3) Disadvantaged Pupil Impact Aid/DPIA ($9.1 million), and (4) Bus Purchase Allowance ($9.1 million).

The encumbered FY 2001 Base Cost Funding contained $16.2 million to cover outstanding set asides and to make final school foundation basic allowance payment adjustments, $10.1 million to make payments for students that are enrolled in post-secondary programs, $8.6 million for community school payment adjustments to reimburse school districts that may have had too much state aid deducted relative to the number of students that actually attended community schools, and $1.5 million for the special education "catastrophic" cost set aside.

The encumbered FY 2001 Desegregation Costs funding was for the state's portion of settling the Dayton City School District's desegregation case, which was still awaiting approval of the federal court with jurisdiction over the legal matter.

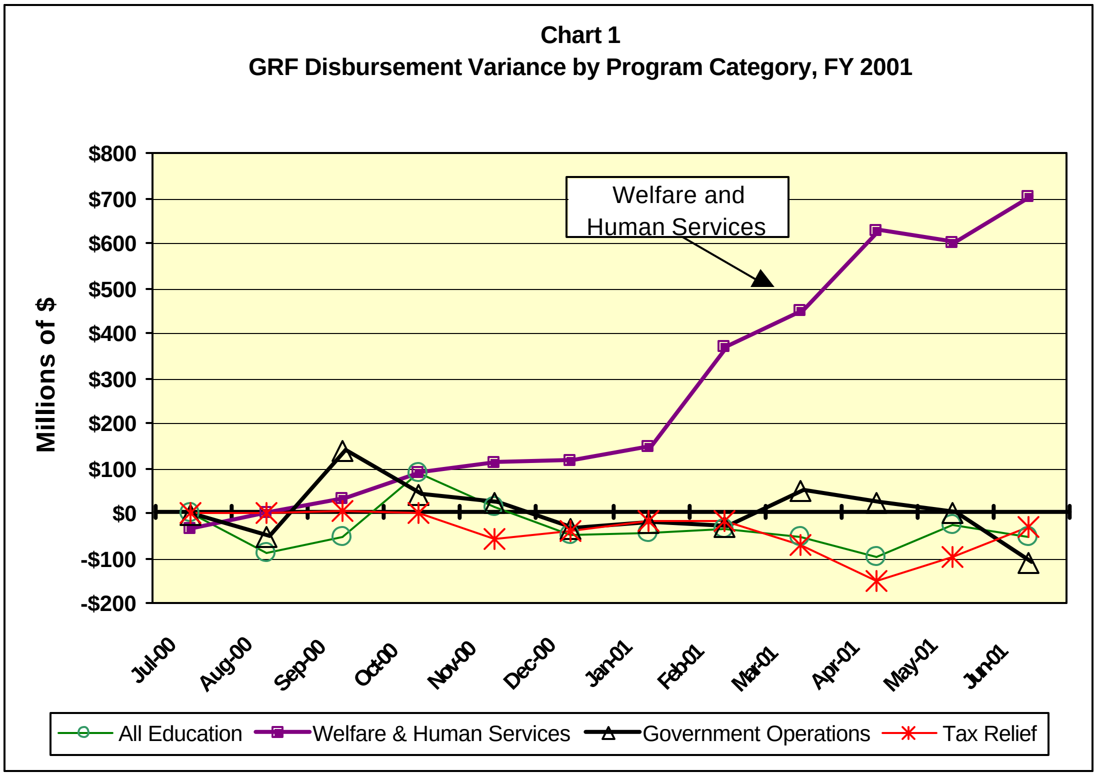
The encumbered FY 2001 DPIA funding represented the unneeded portion of the $13.9 million that was earmarked to operate the pilot school choice program in the Cleveland City School District and would eventually be returned to the school district.

The encumbered FY 2001 Bus Purchase Allowance funding was being held to reimburse school districts for the full cost of purchasing buses used to transport special education and non-public school students. Those reimbursements will not be made until the school districts actually take delivery of their buses.

II. Program Category Variances

In Chart 1, we've visually mapped from July 2000 through June 2001 the trajectory of the year-end disbursement variances of four of the state's major GRF program categories. This is intended to help the reader see how the state came to be holding a $506.2 million year-end overage. In the narrative below, we've distilled the essence of the twelve-month disbursement patterns exhibited by those four major program categories.

Welfare/Human Services (+$698.3 million). The storyline in the Welfare & Human Services program category's disbursements was dominated by one area of spending handled by the Department of Job & Family Services – the Health Care/Medicaid program. The Health Care/Medicaid program featured an ever mounting year-to-date overage that showed no signs of abating, and as a result, required a sig-



nificant infusion of supplemental GRF funding last fall in order to stave off a certain budgetary shortfall.

Potentially less noticeable elements in the program category's FY 2001 disbursement picture included: (1) the Temporary Assistance to Needy Families program, which posted roughly nine months of underspending attributable to a flexible revenue stream and then closed the fiscal year by registering three sizeable monthly overages propelled by a $160-plus million appropriation increase, and (2) the distribution of subsidy funding and service provider payments by the departments of Mental Retardation & Developmental Disabilities, Mental Health, and Alcohol & Drug Addiction Services, which posted timing-based underages and overages throughout the year.

Government Operations (-$108.5 million). Timing played a key role in the Government Operations program category's FY 2001 disbursement variances. It first constrained corrections and pension subsidy spending last August and then facilitated the early disbursement of close to $180 million in debt service payments that were originally forecast to hit in October. As expected, the program then self-corrected in October by posting several large debt-service driven underages. November 2000 through March 2001 followed with a largely mixed bag of timing-based underages and overages. In April, May, and June, a wider mix of forces that included mandated expenditure reductions, a Controlling Board accounting adjustment, and more timing issues combined to produce a series of underages to close the fiscal year.

Education (-$45.8 million). The Education program category cycled under and then over the estimate last August and September, respectively, led by timing-based disbursement variances posted in various subsidy programs administered by the Department of Education. In October and November, the program category's disbursement variance was dominated by the Board of Regents, essentially due to the timing of a $100-plus million debt service payment. In the last seven months covering December 2000 through June 2001, the program category once again swung over and under the estimate, as timing influenced the distribution of funding for various subsidy and student financial assistance programs.

Tax Relief (-$32.2 million). Prior to November, the state's Property Tax Relief program played virtually no role in the year-to-date disbursement picture. Starting with November and running through the remainder of the fiscal year, the pro-

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gram featured its historically typical series of relatively large timing-based monthly overages and underages. The program's year-end underage reflected property tax relief funding that was not needed and then allowed to lapse back into the state treasury to become part of the GRF's available cash balance. ❑

LSC colleagues who contributed to the development of this disbursements article included, in alphabetical order, Ivy Chen, Nelson Fox, Steve Mansfield, Ross Miller, Laura Potts, David Price, Nicole Ringer, Joseph W. Rogers, Jeffrey M. Rosa, Maria Seaman, Allison Thomas, and Wendy Zhan.

Lottery Profits Quarterly Report

LOTTERY TICKET SALES AND PROFITS TRANSFERS FOURTH QUARTER, FY 2001

— *Jean J. Botomogno*

Ticket sales

Table 1 summarizes fiscal year 2001 Lottery ticket sales per game and per quarter. It shows total ticket sales were $1,920.1 million, and Instant tickets sales were $988.5 million. Instant ticket sales totaled 6.1 percent higher than on-line sales at the end of June 2001. Total ticket sales for the fourth quarter of fiscal year 2001 were $473.0 million, 5.4 percent lower than third quarter sales, and 1.9 percent lower than second quarter sales. Fourth quarter sales were $8.3 million or 1.8 percent higher than first quarter sales in FY 2001.

Fourth quarter Instant ticket sales decreased when compared to sales in the second and third quarters. Instant ticket sales fell 9.8 percent compared to third quarter sales, and decreased 11.6 percent when compared to second quarter sales. In contrast, Instant ticket sales in the fourth quarter were $6.5 million or 2.9 percent higher than first quarter sales.

Table 1: FY 2001 Lottery Ticket Sales by Games, millions of current dollars.								
	Pick 3	Pick 4	Buckeye 5	Kicker	Super Lotto	On-Line Tickets	Instant Tickets	Total Sales
Q1	$103.2	$36.1	$14.2	$11.6	$71.2	$236.3	$228.4	$464.7
Q2	$103.0	$37.4	$14.1	$9.3	$53.1	$216.8	$265.4	$482.2
Q3	$109.9	$39.4	$14.4	$10.8	$65.6	$240.1	$260.1	$500.2
Q4	$102.9	$37.8	$13.7	$11.3	$72.7	$238.4	$234.6	$473.0
Total	**$419.0**	**$150.7**	**$56.4**	**$42.9**	**$262.5**	**$931.6**	**$988.5**	**$1,920.1**

*Totals may not add up due to rounding

Compared to fourth quarter results a year ago in fiscal year 2000, ticket sales in the fourth quarter this year were down $47.8 million or 9.2 percent. On-line sales decreased $36.8 million or 13.4 percent. Instant ticket sales declined $11.0 million or 4.5 percent. Except for Pick 4 that had similar sales in the same period a year ago, on-line games experienced a decline. Pick 3 declined $8.9 million or 8.0 percent. The downturn was more severe for Super Lotto Plus ($23.8 million or 24.7 percent) and for Kicker ($3.1 million or 21.5 percent). Super Lotto Plus sales were lower this year in the fourth quarter as compared to the same period last year due to several larger jackpots in FY 2000. For example, in April and June 2000, the jackpot reached $32 million and generated high monthly sales. Due to the slower jackpot growth, most Super Lotto Plus jackpots in the fourth quarter of FY 2001 were not conducive to high levels of sales.

FY 2001 Results

A look at FY 2001 and FY 2000 shows a marked decline in total sales of $230.3 million or 10.7 percent. FY 2000 sales were about $8 million higher than FY 1999 sales. The decline in ticket sales is continuing, despite a momentary pause in FY 2000. FY 2001 sales were 17 percent lower than the record ticket sales of $2,314.7 million in FY 1996. Ticket sales had not reached such a low level since 1994 when they were $1,919.9 million.

Instant tickets

Instant tickets were higher than on-line sales by 6.1 percent in FY 2001 and 10 percent in FY 2000. Instant tickets declined by $1.6 million in FY 2000 when compared to FY 1999. This downturn in In-

Table 2: Lottery Ticket Sales by Games, FY 2001 and FY 2000								
	Pick 3	Pick 4	Buckeye 5	Kicker	Super Lotto	On-Line Tickets	Instant Tickets	Total Sales
FY2001	$419.0	$150.7	$56.4	$42.9	$262.5	$931.6	$988.5	$1,920.1
FY2000	$427.3	$144.7	$62.3	$52.8	$336.8	$1,023.9	$1,127.1	$2,151.0

*Totals may not add up due to rounding

stant tickets sales accelerated in FY 2001 as sales declined $138.6 million or 12.3 percent when compared to FY 2000. This marks the second time Instant tickets sales were lower compared to the previous year. The enacted budget for the FY 2002-2003 biennium removed a pre-existing provision requiring that a minimum of 30 percent of ticket sales must be transferred to the Lottery Profit Education Fund (LPEF). Instant tickets sales may benefit from these changes because the Ohio Lottery could offer Instant games with higher payout ratio than in previous years. Instant games percentage payout was about 63 percent in FY 2001, lower than non-Ohio Lottery products that may reach 75 to 90 percent payout. Increasing the payout ratio may in turn help the Ohio Lottery to better compete against other organizations' scratch-offs, pull-tabs, bingo and "charitable" instant games, and regain lost gaming dollars.

On-line sales

FY 2001 online sales, after a slight improvement in FY 2000, have resumed their decline. On-line sales declined $92.3 million or 9.0 percent in FY 2001. This was a slower rate of decline than for Instant tickets. A closer analysis of FY 2001 results points out the importance of Pick 3 to on-line sales and total sales. Pick 3 contributed 45 percent of on-line sales while Super Lotto Plus contributed only 28.2 percent. The increase, attributable to the Red Ball promotion and to mid-day drawings for Pick 3 and Pick 4 games introduced in FY 2000, have magnified the importance of Pick 3 and Pick 4 to yearly sales results.

In FY 2001, only the Pick 4 game showed an increase in sales over a year ago. Pick 4 sales increased $6.0 million or 4.1 percent in FY 2001, after an increase of 15 percent between FY 2000 and FY 1999. The remaining on-line games had lower results in FY 2001 when compared to FY 2000. Pick 3 sales declined $8.3 million or 1.9 percent. Given overall trends, this was a favorable result. Buckeye 5, Super Lotto and Kicker continue to experience difficulties. Buckeye 5 fell 9.4 percent, Kicker fell 18.7 percent, and the Super Lotto Plus declined 22.1 per-

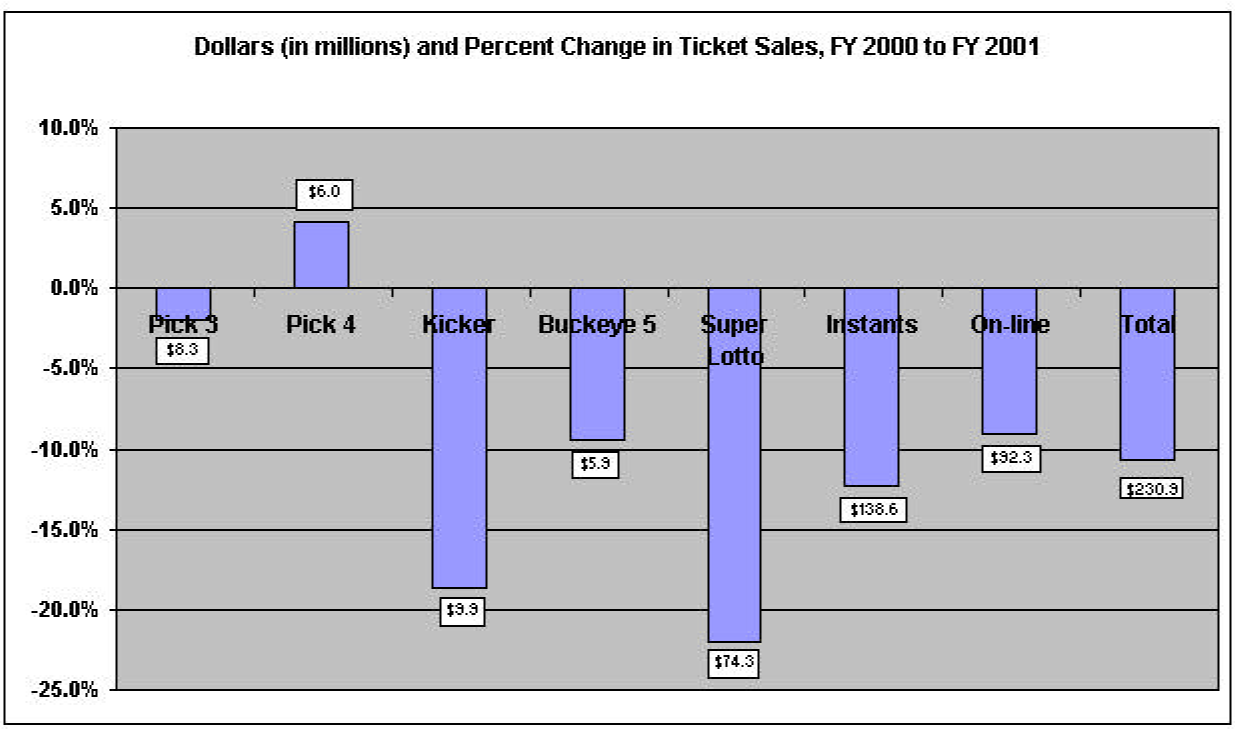

Table 3: FY 2001 Lottery Ticket Sales and Transfers to LPEF, millions of current dollars						
	Ticket Sales	Actual Transfers	Projected Transfers	Dollars Variance	Percentage Variance	Transfer As a Percentage of Sales
Q1	$464.7	$152.3	$161.6	-$9.3	-5.7%	32.8%
Q2	$482.2	$167.1	$171.5	-$3.9	-2.3%	34.6%
Q3	$500.2	$144.9	$167.5	-$22.6	-13.5%	29.0%
Q4	$473.0	$147.7	$165.1	-$17.4	-10.5%	31.2%
Total	**$1,920.1**	**$612.0**	**$665.2**	**-$53.2**	**-8.0%**	**31.9%**

cent. Super Lotto contributed 80 percent of the decline in on-line sales in FY 2001. Buckeye 5 has experienced a decline in sales every year since its introduction in FY 1993.

Super Lotto Plus

Perhaps because of the lack of mega jackpots in excess of $150 million for multi-state lotteries PowerBall and Big Game in neighboring states in FY 2001, Super Lotto Plus sales decreased considerably. Concerns over sagging Super Lotto sales had the Ohio Lottery introduce the Super Lotto Plus in July 2001. Super Lotto had the smallest profit margin of all Lottery games. The new game, Super Lotto Plus, promised players better odds of winning a prize and more winners by paying out smaller prizes. Super Lotto Plus slowed jackpot growth when there were no winners, from $4 million increments to $1 million or larger depending on ticket sales. It also increased the length of annual payments from 26 to 30 annual payments. The Ohio Lottery was hoping that these changes would increase overall sales while increasing profit margins for Super Lotto. Some improvement did occur. Payout percentage for Super Lotto Plus averaged about 60 percent in FY 2001, while the payout percentage was about 73 percent for Super Lotto in FY 2000. Jackpot "fatigue" is entrenched and with slowing the jackpot growth, the Ohio Lottery may have also delayed buying frenzies that accompany high jackpot levels. It appears that the Ohio Lottery may have improved profit margins on Super Lotto Plus at the expense of ticket sales. This may have produced a more stable game at the lower sales levels that are now the norm.

Transfers to the Lottery Profits Education Fund

Table 3 summarizes transfers to the Lottery Profits Education fund (LPEF). Fourth quarter transfers were $147.7 million, up 1.9 percent from $144.9 million in the third quarter and down 11.6 percent from $167.1 million in the second quarter (which had the highest transfer from operations). Compared to fourth quarter transfers a year ago, FY 2001 transfers were down $18.8 million or 11.3 percent.

Transfers to LPEF from operations in FY 2001 were $612.0 million, $49.0 million or 7.4 percent lower than in FY 2000. FY 2001 transfers were $53.2 million or 8.0 percent less than projected transfers. Total fiscal year 2001 transfers that include $25 million from non-operating sources were $637.0 million. Transfers to LPEF from operations have declined steadily since a high of $713.5 million in FY 1996. FY 2001 transfers from operations were down 14.2 percent from FY 1996 highs.

A permanent law change contained in the enacted budget for the FY 2002-2003 biennium removed the statutory transfer of at least 30 percent of ticket sales to LPEF. A transfer target to LPEF will be determined for each biennium during the legislative budget process. The FY 2002-2003 biennial budget requires The Ohio Lottery Commission to transfer an amount greater than or equal to $633.7 million in FY 2002 and $621.7 million in FY 2003 to LPEF. Transfers will be from net income from operations and may be supplemented by the Unclaimed Prizes Fund. In the last three fiscal years, transfers from the Unclaimed Prizes Fund have been $25.0 million. The change in the law gives the Ohio Lottery more flexibility in designing new Instant games and change the game mix. However as seen with Super Lotto Plus, changes in games do not necessarily guarantee improved sales or profits. ❑

LOTTERY PROFITS EDUCATION FUND DISBURSEMENTS DISBURSEMENTS OF FISCAL YEAR 2001 PROFITS

— *Wendy Zhan*

Table 1: FY 2001 LPEF (017) and LPERF (018) Appropriation/Disbursement Summary As of June 29, 2001							
Agency	**Fund**	**Line Item**	**Line Item Name**	**FY 2001 Appropriation**	**FY 2001 Disbursement**	**Appropriation Encumbrance**	**Appropriation Balance**
EDU	017	200-612	Base Cost Funding	$ 660,467,000	$ 628,967,000	$ 0	$ 31,500,000
EDU	017	200-682	Lease Rental	$ 29,733,000	$ 29,733,000	$ 0	$ 0
NET	017	228-690	SchoolNet Electrical Infrastructure	$ 13,492,663	$ 4,109,194	$ 0	$ 9,383,469*
			Total LPEF	***$ 703,692,663***	***$ 662,809,194***	***$ 0***	***$ 31,500,000***
SFC	018	230-649	Disability Access Project	$ 69,746	$ 63,966	$ 4, 480	$ 1,300

* The entire balance was reappropriated in FY 2002 per Am. Sub. H.B. 94 of the 124th General Assembly.

Lottery Profits Education Fund (LPEF) disbursements in fiscal year 2001 totaled $662.8 million. Of this amount, $629.0 million (or 94.9 percent) occurred in appropriation item 200-612, Base Cost Funding. Lottery Profits Education Reserve Fund (LPERF) disbursements were $0.6 million in fiscal year 2001. Table 1 shows the LPEF and LPERF appropriation and disbursement summary as of June 30, 2001.

Lottery profits transfers were $53.1 million below the estimate. The short fall is made up by transferred funds of $18.0 million from the LPERF, $4.5 million in interest earnings of the LPEF, and $30.6 million in existing General Revenue Fund (GRF) appropriations within various line items of the Department of Education.

*Base Cost Funding***.** The $629.0 million lottery profits spending blends with GRF base cost funding (line item 200-501) appropriation ($3,794.8 million) to fund the state foundation aid program. Among other things, the program provides equalized subsidies to school districts (including joint vocational school districts) to guarantee $4,294 in per pupil funding with the cost of doing business factor adjustment at the combination of state and local revenues at 23 mills (the charge-off millage rate is 0.5 mills for the joint vocational school district funding formula) and to fund the state's share of additional special and career-technical education costs. With the combination of GRF and LPEF moneys, base cost funding ($4,423.8 million), the biggest education subsidy item, represents about 64.7 percent of Department of Education's GRF and LPEF budget components.

*Lease Rental***.** The lease rental appropriation ($29.7 million) was transferred to GRF to support the GRF appropriation for line item 230-428, Lease Rental Payments, of the School Facilities Commission. Total appropriations for lease rental payments amounted to $57.5 million in fiscal year 2001, including $41.8 million for GRF item 230-438, Lease Rental Payments, and $15.7 million for GRF supported (Fund 078) item 155-900, Common School Capital Improvement Bond Service Fund, of the Commissioners of Sinking Fund. These moneys were used to pay bond service charges on obligations issued for the classroom facilities assistance programs.

SchoolNet Electrical Infrastructure – "Power-up For Technology." To help school districts implement SchoolNet and SchoolNet Plus initiatives, the 122nd General Assembly originally appropriated $27.0 million in LPEF moneys in fiscal year 1998 for electrical service upgrades. The SchoolNet Commission is to distribute the funding through a competitive grant application process. School districts with a valuation per pupil less than $200,000 are eligible for the funding. The maximum grant amount for a single district is $1.0 million. Approximately $13.6 million was disbursed by the end of fiscal year 2000. The remaining balance of $13.4 million was transferred into fiscal year 2001 per the Controlling Board's action. As of June 29, 2001, $4.1 million was disbursed. The remaining balance of $9.5 million was reappropriated in FY 2002 per Am. Sub. H.B. 94 of the 124th General Assembly.

The program's disbursement activities appear to be relatively slow on the surface. This is primarily due to the program's capital project nature. Eligible school districts first need to submit applications to the SchoolNet Commission. Once they are awarded initial grants, school districts have to go through the actual bidding process. The final grant awards are based on the actual bidding prices instead of initial estimated amounts made by school districts. According to the SchoolNet Commission's spokesperson, on average the final grant awards are 20 percent less than the initial award amounts. This allows more school districts to receive grants under the program. ❑