OBM

Ted Strickland
Governor

J. Pari Sabety
Director

September 10, 2008

MEMORANDUM TO:	The Honorable Ted Strickland, Governor The Honorable Lee Fisher, Lt. Governor
FROM:	J. Pari Sabety, Director
SUBJECT:	Monthly Financial Report

This report contains information regarding Ohio's financial position through August 31, 2008 as well as highlights of regional and national economic indicators.

As was the case last month, Ohio's economic indicators continue to be driven by the national economic downturn. As a result, July had significant underperformance in GRF revenues. August performance has confirmed that while part of the July performance was an aberration, it presages a disquieting downward trend.

From a monitoring perspective, two of the most effective real-time indicators of state economic performance are the state income tax (particularly withholding) and the state sales tax. These taxes act as a measure of economic activity from the current and previous month in terms of how much Ohioans are earning and how much they are spending for discretionary purposes.

Observing two months of FY 2009 revenue experience, the income and the sales tax account for $160 million of the $167 million GRF tax receipt shortfall (as later material will show, the withholding shortfall is even larger than the total income tax shortfall.) While the total August tax receipt variance of $27 million is significantly less than the July variance of $140 million, the cumulative effects of the under-performance in income, sales and other taxes have caused OBM to reforecast tax revenues for the balance of FY 2009.

As a result, FY 2009 GRF revenue projections will be modified to reflect a total that is $540 million below previous estimates. This new forecast is consistent with the "No Growth Scenario" that OBM projected could occur when revenues were revised downward early in CY 2008. Specific revenue, disbursement and fund balance estimates will be made available under separate cover and will be incorporated into the October Financial Report for use in future months.

This month's special feature outlines the impact of state payroll costs on the General Revenue Fund.

MONTHLY FINANCIAL REPORT CONTENTS

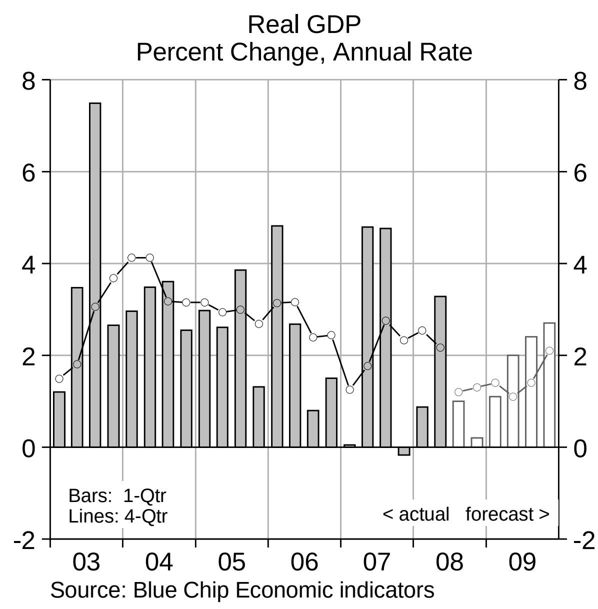
ECONOMIC SUMMARY

Labor markets weakened notably through August, even as some measures of manufacturing activity stabilized or improved. Total U.S. employment decreased for the eighth straight month in August. Ohio employment is down marginally for the year. Both the U.S. and Ohio unemployment rates hit new long-time highs. At the same time, however, industrial production increased for the second consecutive month in July and purchasing managers in manufacturing report sluggish, but stable conditions. Leading economic indicators still point toward weakness and economists have lowered forecasts of economic growth.

Highlights of Economic Performance

- The consensus among forecasters is that economic growth will remain at the recent weak pace for several more quarters.
- National employment fell by 84,000 in August, which was the eighth straight month of decline. Prior month employment declines were also revised to be larger. Ohio employment is down by 10,400 jobs since December.
- Excluding the federal stimulus rebates, disposable personal income increased 0.5% in July after rising 0.3% in June and 0.4% in May.
- The manufacturing purchasing managers' index remained near neutral for a fourth straight month, indicating neither growth nor decline in manufacturing activity.
- New housing starts and permits were both down by about 30% from a year ago based on a three-month moving average.

Economic Growth



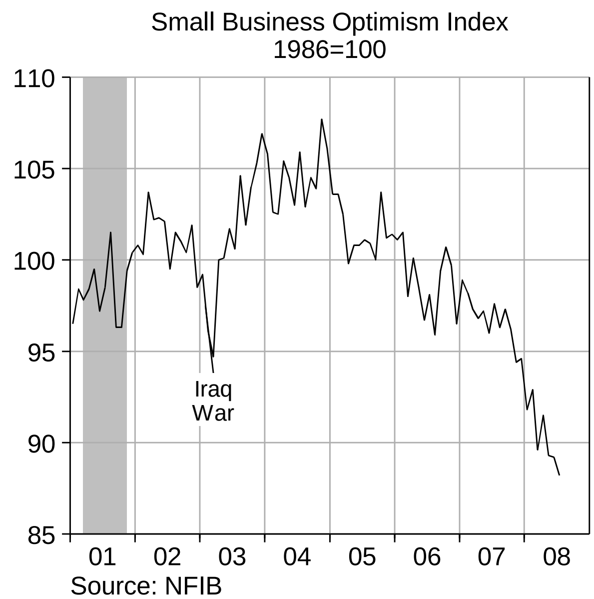
Real GDP growth was revised up to 3.3% in the second quarter from the initial report of 1.9%. The strong growth rate during the second quarter does not by itself rule out recession, considering that quarterly growth has been even stronger on three occasions in previous recessions. In addition, gross domestic income – an alternative measure of economic activity also compiled by the government – advanced by a less-rapid 1.9%, calling into some question the accuracy of the stronger real GDP growth rate.

The upward revision to second quarter real GDP growth reflected much stronger foreign trade than originally estimated and a smaller decrease in business inventories. The increase in exports and decrease in imports accounted for almost all of the growth in real GDP during the quarter. Excluding net exports, real GDP edged up by only 0.2%, following a small rise of 0.1% in the first quarter and a decrease of 1.0% in the fourth quarter of 2007. On this basis, growth has been weaker in the past only during or just prior to periods of recession.

The major drivers of second quarter growth remained net exports, personal consumption expenditures, government spending, and investment in nonresidential structures. Factors subtracting from growth included the change in business inventories, investment in residential structures and investment in equipment and software.

Looking ahead, the **Weekly Leading Index** from the Economic Cycle Research Institute (ECRI) sank to a new cycle-low in late August. The composite **Leading Economic Index** compiled by the Conference Board fell by 3.3% from a year earlier in July, a new low for this cycle. Neither business cycle gauge provides a sign that the economy is about to rebound in the near-term.

Owners of small businesses have a similar outlook. The **Index of Small Business Optimism**, compiled by the National Federation of Independent Business, fell further into recession territory in July, largely reflecting weak capital spending plans. Owners of small businesses reported that credit remains available, job creation is weak but not crashing, and that inflation is a widespread problem.

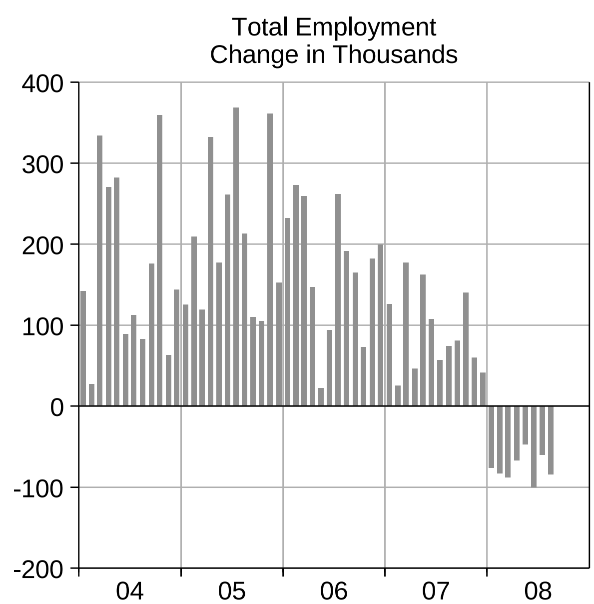


The consensus among forecasters is that economic growth will remain at the recent weak pace for several more quarters. The *Blue Chip Economic Indicators* consensus of approximately 50 forecasters is for real GDP growth of 1.0% in the third quarter, 0.2% in the fourth quarter, and 2.1% growth from the fourth quarter of 2008 to the fourth quarter of 2009. Global Insight predicts that real GDP will decrease in both the fourth quarter of 2008 and first quarter of 2009 and grow by only 1.5% during the four quarters of 2009.

The placement of Fannie Mae and Freddie Mac into conservatorship by the federal government potentially alters the outlook for the economy. The move might help to stabilize the faltering credit and housing markets and keep mortgage loan defaults and home foreclosures below levels that would have otherwise prevailed.

Employment

Total employment decreased for the eighth straight month in August, and the June and July losses were revised downward. The unemployment rate jumped to a new high for this cycle, removing any lingering questions about the severity and likely duration of the economic slump.



Employment fell by 84,000 in August. Losses in the prior two months were revised up by a total of 58,000 jobs. Total employment has decreased by a total of 605,000 jobs or 76,000 jobs per month since its peak last December.

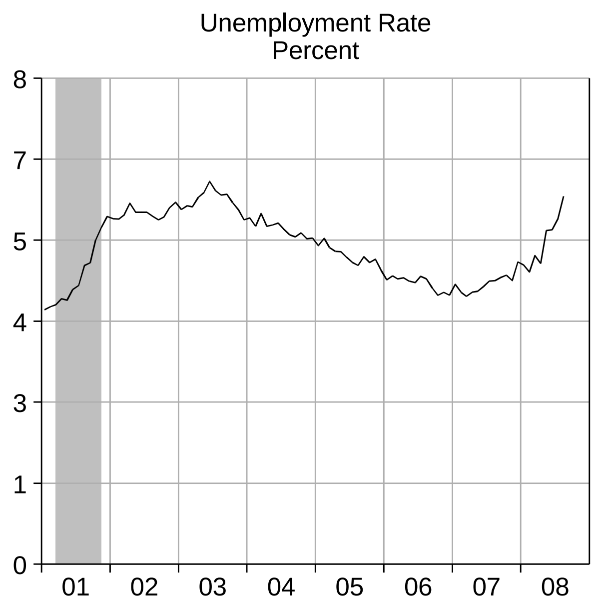
Private sector employment has decreased for nine straight months by a total of 772,000 jobs. Private sector employment has decreased for nine consecutive months during the post-war period only in conjunction with recessions.

The rate of job loss in construction moderated to 8,000 in August, compared with an average decline of 38,000 during the preceding twelve months. But the loss of manufacturing jobs intensified to 71,000 – the largest one-month loss since July 2003. Professional and business services shed 53,000 jobs. The only major sector to post a sizable employment gain was education and health services, where the job count increased by 55,000. Employment in temporary help services decreased for the twentieth consecutive month by the largest amount since the 2001 recession. Temporary help employment has led other measures of economic activity in the past, because of the ease which with temporary staff can be added or reduced.

Ohio employment decreased by 11,600 jobs in July, reversing the gains made during May and June. Ohio employment is down by 10,400 jobs since December and by 13,300 jobs since July 2007. The Ohio unemployment rate increased to 7.2% in July, up from 5.5% at the start of the year to the highest level since 1992.

Employment was weak across all major sectors during July, with none posting an increase. Leisure and hospitality (-3,000) and trade, transportation and utilities (-2,500) registered the largest declines, followed by construction (-1,500), government (-1,300), and manufacturing (-900).

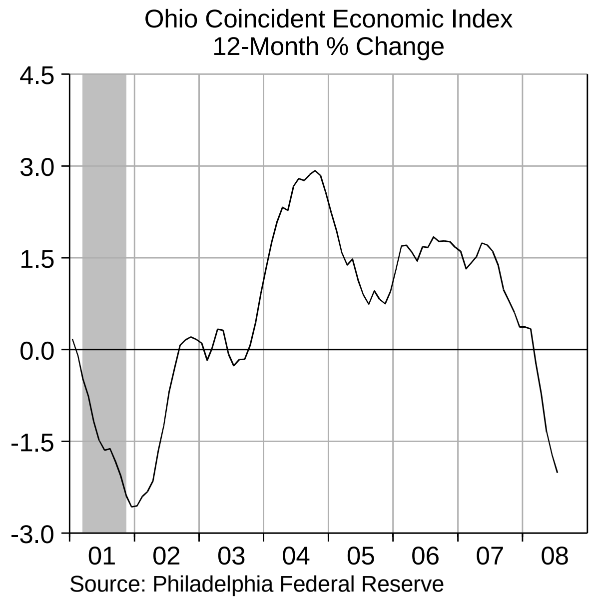
In and around Ohio, employment levels were largely unchanged through mid-August, according to a survey by the Federal Reserve Bank of Cleveland. Staffing firms reported a small increase in the number of job openings and applicants. Job vacancies were most prevalent in health care and high-skilled manufacturing.



The **national unemployment rate** increased by 0.4 percentage points to 6.1% in August to 1.7 percentage points above the cycle low of 4.4% in March 2007. The rate is also 1.3 percentage points above the preceding twelve-month low, a development that has occurred in the past only during periods of recession.

The **length of the workweek** for all production and nonsupervisory workers was unchanged at 33.7 hours – a notch above the all-time low of 33.6 hours. The manufacturing workweek slipped to 40.9 hours, and overtime fell to a weekly average of 3.7 hours. The index of aggregate weekly hours decreased for the fifth straight month. The July-August average is below the second quarter average by 1.3% at an annualized rate.

The **Ohio coincident index** compiled by the Philadelphia Federal Reserve fell for the fifth straight month in July, pulling the year-over-year percent change down to -2.0% – the weakest since just after the 2001 recession. The **Ohio leading economic index** fell 0.1% in July, continuing the negative see-saw pattern in place all year. Compared with a year earlier, the leading index is lower by 0.6%.



Among the eleven **Ohio Metropolitan Statistical Areas**, Columbus (+7,100) and Lima (+1,400) added the most jobs during the twelve months ended in July. Akron and Canton added 600 and 500 jobs, respectively. Employment fell in Dayton (-2,300), Cleveland (-2,100) and Toledo (-1,600).

Kentucky and West Virginia led the way in employment growth among **contiguous states** during the twelve months ending in July with gains of 1.0% and 0.5%, respectively. Employment in Michigan decreased 1.1% from a year ago. Employment fell by 0.6% in Indiana and 0.2% in Ohio and was little changed in Pennsylvania. In comparison, U.S. employment decreased 0.1% during the twelve months ending in July and 0.2% during the twelve months ending in August.

Consumer Income and Consumption

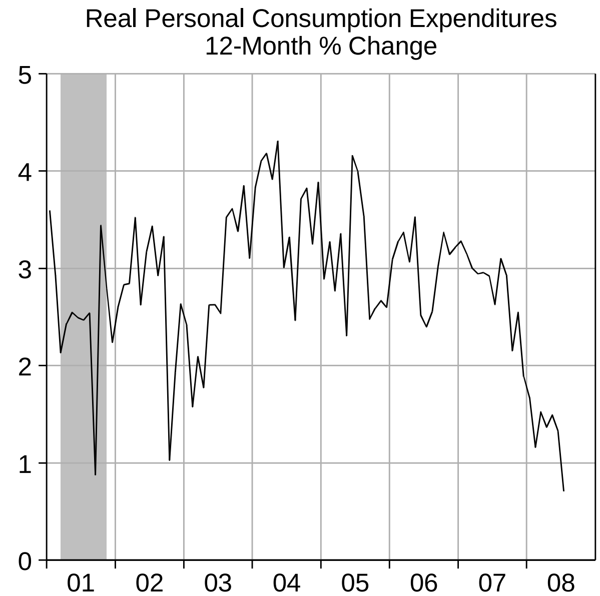
The timing of tax rebate checks continued to affect consumer income and spending through July. **Disposable personal income** decreased 1.1% in July after falling 1.9% in June and rising 5.7% in May. Excluding the rebates, disposable personal income increased 0.5% in July after rising 0.3% in June and 0.4% in May. Rebate checks amounted to $91.6 billion during April-July and are expected to total $106.7 billion through September.

Wage and salary disbursements, which were unaffected by rebate checks, increased 0.3% in July and 4.1% from July 2007. The price index for personal consumption expenditures increased 0.6% in July and 4.5% from a year earlier.

Personal consumption expenditures increased 0.2% in July. Inflation-adjusted consumption decreased by 0.4% after slipping by 0.1% in June. Compared with a year earlier, consumption increased 5.3% and was up 0.7% after adjustment for inflation – the weakest year-over-year change since 1991.

Midwest retail sales decreased 0.3% in July and were up just 2.3% from a year earlier. U.S. retail sales fell 0.1% nationally and were up 2.6% from July 2007.

Personal consumption expenditures are likely to decrease in the third quarter for the first time since the 1990-91 recession. Real spending ended the second quarter on a weak note and started the third quarter on a weaker one. To avoid a third-quarter contraction, real consumer spending would have to increase at an annualized pace in excess of about 4% in August and September – a pace not observed in back-to-back months since January-February 2007.



Light motor vehicle sales rebounded to 13.7 million units at a seasonally adjusted pace in August, up from 12.5 million units in July but still well below the 16.2 million unit pace of August 2007. Richer sales incentives and lower gasoline prices are believed to have helped boost sales. The ongoing credit crunch continues to hobble sales, as manufacturers have scaled back leasing and lenders maintain tighter credit standards.

Consumer expectations improved modestly during July and August, but remained at historically low levels. Assessments of the present situation deteriorated slightly in August.

<u>Manufacturing</u>

The industrial sector continues to tread water. **Industrial production** increased 0.2% in July for the second straight increase after four declines in a row. Manufacturing production increased 0.4%, mining rose 0.9% and utility output fell 1.9%. Compared with a year earlier, industrial production was down by 0.1%. Manufacturing production remained 1.1% below its year earlier level.

The recent upturn in production is a positive sign, as recessions have typically started when employment peaked and ended when industrial production reached a trough.

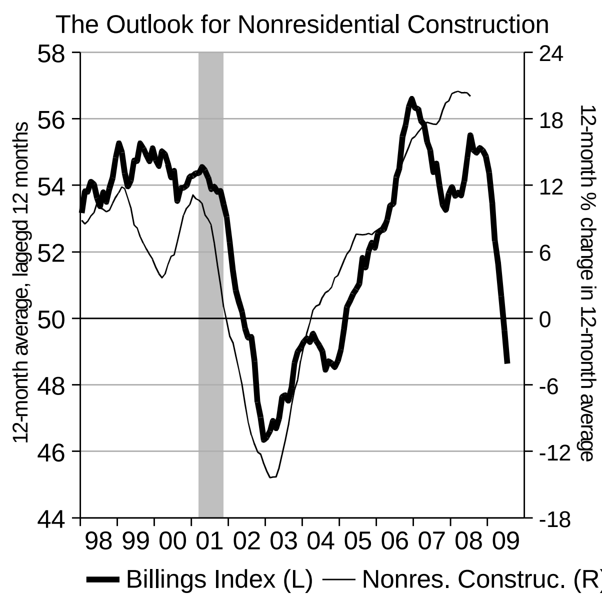
Capacity utilization increased to 79.9%, up from a low for the cycle of 79.6% in May. Utilization reached a high of 81.4% in July 2007. Despite the improvement, recent rates of capacity utilization remain consistent with below normal capital spending. Nonetheless, about one-half of manufacturers in and around Ohio said in mid-August that they plan to increase capital spending, according to the Cleveland Fed.

Midwest industrial production increased 0.4% in July, according to the Federal Reserve Bank of Chicago. Regional auto sector production and machinery sector production increased, while resource sector output and steel sector output both declined. The Cleveland Fed reported that output at factories in and around Ohio was largely stable during the six weeks ending in mid-August. Industrial activity improved modestly in the New York and Philadelphia Federal Reserve Bank Districts during August, according to surveys.

Factory orders and shipments remained solid. **New orders** from factories increased 1.3% in July and **factory shipments** increased 2.1%. Orders and shipments were not pushed higher by oil process as in recent months, but did reflect mid-year price increases for a range of items. Revisions to previous months were largely positive.

Reports from **purchasing managers** in manufacturing across the country were stable again in August. The purchasing managers index remained near neutral for a fourth straight month, indicating neither growth nor decline in manufacturing activity. The index for production slipped after four straight increases, but remained convincingly above neutral. The index for new orders rebounded, but remained convincingly in negative territory. In addition, the backlog of orders remained very weak.

Construction



Construction put-in-place fell 0.6% in July as the 2.1% decline in residential construction more than offset the 0.2% increase in nonresidential construction. Activity levels for May and June were revised significantly higher, especially for private nonresidential, multi-family, and state and local, with could add another quarter percentage point to second quarter real GDP growth in the next revision.

The **Architecture Billings Index** (ABI) edged higher in July, but the message of its recent pattern remains unequivocally negative. As shown in the nearby chart, the 12-month average of the index has a strong correlation with the rate of change in nonresidential construction put-in-place during the subsequent year. The last time that the 12-month average of the billings index was at the current level, nonresidential construction fell by about 5% during the next year. The history of the billings index includes only one previous recession, but sounds a warning worthy of note.

Housing starts fell sharply in July after a temporary rebound in June. Permits were also down substantially to near the March low. Starts and permits were both down by about 30% from year ago levels on a 3-month moving average basis. Recent trends are not inconsistent with a near-term trough in housing construction, but the July declines indicate that the onset of a durable recovery in housing construction could lie well into the future.

Existing home sales increased 3.1% in July. In the Midwest, existing home sales increased 0.9% to an annual rate of 1.12 million units. The number of homes for sale across the country increased to 4.67 million units, which translates into 11.2 months at the July pace of sales – the same as in April.

New home sales increased 2.4% in July to roughly the same level as in March and May. Sales in the Midwest fell by 8.2% – the third consecutive monthly decline. More importantly, the supply of newly built unsold homes decreased for the fifteenth straight month by the largest amount in any one of those months. The inventory of unsold new homes represented a 10.1-month supply at the July pace of sales, down from a peak for this cycle of 11.2 months in March.

GENERAL REVENUE FUND RECEIPTS

Across all sources, total year-to-date GRF receipts are $4,049.7 million, which is below estimate by $192.0 million. The table below illustrates the variances by category of revenue source.

Category	Includes:	YTD Variance	% Variance
Tax receipts	Sales & use, personal income, corporate franchise, public utility, kilowatt hour, foreign & domestic insurance, other business & property taxes, cigarette, alcoholic beverage, liquor gallonage & estate	($167.3 million)	(6.0%)
Non-tax receipts	Federal grants, earnings on investments, licenses & fees, other income, intrastate transfers	($12.8 million)	(0.9%)
Transfers	Budget stabilization, liquor transfers, capital reserve, other	($11.8 million)	(37.1%)
TOTAL REVENUE VARIANCE:		($192.0 million)	(4.5%)

Similar to July, but on a smaller scale, the negative performance of state tax receipts for the month of August was driven by shortfalls in the two largest GRF tax sources (non-auto sales and use and personal income). Together these two tax sources fell short of the monthly estimate by a combined $38.4 million. Helping offset this performance in August however was slightly stronger than anticipated performance by a number of smaller tax sources. While relatively better than July, the variance in tax receipts for the month of August increased the year to date shortfall to $167.3 million or 6.0% below estimate.

Also troubling in terms of individual monthly and year-to-date performance is a comparison of this year’s tax receipts with receipts at the same point in FY 2008. Not only have tax revenues failed to meet estimates for the first two months of the year, but they have also experienced a decrease when compared to the first two months of FY 2008. Total tax receipts are now $110.5 million (4.0%) below those at the same point a year ago. While some of this year-over-year decline can be attributed to the continued implementation of tax reform, the scope of the reductions and the taxes affected are greater and more widespread than would be anticipated when accounting for the impact of tax reform alone.

Individual Sources Above Estimate		Individual Sources Below Estimate	
Auto Sales Tax	$1.4	Non-Auto Sales Tax	($18.2)
Public Utility Tax	$4.8	Personal Income Tax	($20.2)
Kilowatt Hour Tax	$2.1	Federal Grants	($10.9)
Cigarette Tax	$1.3	Liquor Transfers	($12.0)
Licenses and Fees	$1.1	Other Sources Below Estimate	($2.7)
Other Sources Above Estimate	$1.3		
Totalabove	**$12.1**	**Total below**	**($64.0)**

Non-Auto Sales and Use Tax

As previously mentioned, contributing significantly to the overall shortfall in monthly tax revenue was the performance of the non-auto sales tax. August collections were $545.5 million, resulting in a negative variance of $18.2 million (3.2%). On a year-over-year basis, the non-auto sales tax experienced an increase of $7.7 million, an amount that effectively reflects zero growth when factoring out decreased deposits to the local government funds. With the failure of this tax source to meet estimates during the first two months of FY 2008, the non-auto sales tax has failed to meet its targets in five of the previous seven months.

Auto Sales Tax

One relative bright spot during the month of August which partically offset the performance of the non-auto sales and personal income taxes was the auto sales tax. Specifically, this tax reversed its performance in July by bringing in $87.3 million during the month of August and exceeding estimates by $1.4 million (1.7%). While this positive performance is a modest but distinct improvement over June and July, it marks only second time in the last six months that this tax source has met the estimates. As a result, OBM will continue to closely monitor the performance of this tax source in light of the potential impact on auto sales brought about by a tightening of credit, high oil prices and gasoline prices, and an uncertain labor market with rising unemployment claims, and sliding consumer confidence.

Personal Income Tax

As with the non-auto sales tax, the personal income tax again struggled during the month of August as receipts were $543.9 million or $20.2 million (3.6%) below estimate. While income tax receipts failed to meet estimates several times during FY 2008, those variances were more often than not the result of greater than anticipated refunds. This was certainly not the situation in August as refunds were actually lower than anticipated with the primary factor in the negative variance being a weakness in withholding. In fact, had it not been for the $19.0 million variance in refunds, the monthly variance for the income tax would have been nearly double as withholding alone was below estimate by $49.2 million. On a year-over-year basis, total personal income tax receipts decreased by $36.0 million, an amount that accounts for most of the August year-over-year reduction in tax revenue of $45.7 million.

The real concern in the income tax is the very weak performance of employer withholding for the first two months of FY 2009. The $49 million August shortfall followed a July shortfall of almost $63 million. Over just two months, withholding is almost $112 million below estimates. Although one cannot compare this year's collections with last year's collections without adjusting for the fact that tax rates are lower in FY 2009, the number of business days are fewer this July and August than last year, and for other timing factors, even after making those adjustments withholding so far this year is very weak. Withholding this fiscal year has shown essentially no growth from last year.

FY 2009 PERSONAL INCOME TAX RECEIPTS BY COMPONENT ($ in millions)

	ESTIMATE AUGUST	ACTUAL AUGUST	$ VAR AUGUST	ESTIMATE Y-T-D	ACTUAL Y-T-D	$ VAR Y-T-D
Withholding	$634.7	$585.5	($49.2)	$1,321.4	$1,209.6	($111.8)
Quarterly Est.	$14.6	$13.6	($1.0)	$33.3	$31.3	($2.0)
Trust Payments	$0.7	$0.3	($0.4)	$4.3	$1.2	($3.1)
Annual Returns & 40 P	$10.1	$12.7	$2.6	$19.6	$23.7	$4.1
Other	$3.0	$7.3	$4.3	$8.0	$13.1	$5.1
Less: Refunds	($42.0)	($23.0)	$19.0	($68.3)	($66.7)	$1.6
Local Distr.	($57.0)	($52.5)	$4.5	($129.6)	($125.1)	$4.5
Net to GRF	**$564.1**	**$543.9**	**($20.2)**	**$1,188.6**	**$1,087.1**	**($101.6)**

Corporate Franchise Tax

With $3.1 million in receipts, the corporate franchise tax was slightly above estimate during the month of August, exceeding the estimate of $2.5 million by just over $600,000. On a year-over-year basis, receipts for FY 2009 to date are $36.4 million greater than in FY 2008, although one large settlement payment of over $40 million accounts for all of the growth, and then some.

Commercial Activity Tax

In FY 2009, receipts from the commercial activity tax (CAT) are distributed to non-GRF funds to reimburse school districts and local governments as the tangible personal property tax is phased out. During the month of August, CAT receipts totaled $281.0 million and were $16.7 million above estimates (6.3%). As was the situation in July, this positive variance was unexpected given the weaker than expected performance of the CAT during FY 2008 and has created a positive variance of $22.9 million for the year to date. Given the relatively short history of this tax source, OBM will continue to closely monitor this tax as we move toward the next payment date in November.

Public Utility Tax

A majority of tax payments due on the public utility tax in August were on gross receipts of public utility companies during the period of April to June and primarily reflect the payments made by natural gas companies. During the month, public utility tax receipts totaled $47.4 million and exceeded estimates by $4.8 million (11.3%). As there were no payments or estimates for the month of July, the year to date variance for this tax equals the variance for the month.

Cigarette Tax

The August performance of the cigarette tax showed a modest reversal of the prior downward trend. August collections were $86.3 million or $1.3 million (1.6%) above estimates. This performance followed an exceptionally bad July where this source experienced a shortfall of $6.0 million (24.9%). As discussed in last month's report, OBM believed that part of the problem with July may have been the timing of payments that might be made in early August. In monitoring this, it appears that this may have well been the situation as $9.4 million in receipts were posted the first day of August. Without one of the two relatively large payments posted at the beginning of the month, this tax would have recorded another negative variance for the month in the range of $2.7 to $4.0 million. As it is, the cigarette tax has experienced a year-to-date shortfall of $4.7 million (11.3%.)

GRF non-tax receipts totaled $561.7 million in August and were $12.0 million below estimate (2.0%). This variance that existed for the month was primarily due to receiving slightly less in federal grants, ISTV's and "other income" than was estimated. On a year over year basis, non-tax receipts for this August were $198.1 million (26.1%) lower than in August 2007 primarily as a result of receiving $197.7 million less in federal grants. The receipt of these federal grants and may be attributable in large part to the number Medicaid reimbursements received in FY 2008.

Table 1*

GENERAL REVENUE FUND RECEIPTS
ACTUAL FY 2009 VS ESTIMATE FY 2009
($ in thousands)

REVENUE SOURCE	Month: ACTUAL AUGUST	Month: ESTIMATE AUGUST	Month: $ VAR	Month: % VAR	Year-to-Date: ACTUAL Y-T-D	Year-to-Date: ESTIMATE Y-T-D	Year-to-Date: $ VAR	Year-to-Date: % VAR
TAX RECEIPTS								
Non-Auto Sales & Use	545,469	563,691	(18,221)	-3.2%	1,148,835	1,206,846	(58,011)	-4.8%
Auto Sales & Use	87,317	85,888	1,430	1.7%	175,091	178,973	(3,881)	-2.2%
Subtotal Sales & Use	632,786	649,578	(16,792)	-2.6%	1,323,927	1,385,819	(61,892)	-4.5%
Personal Income	543,866	564,081	(20,215)	-3.6%	1,087,027	1,188,637	(101,610)	-8.5%
Corporate Franchise	3,083	2,481	602	24.2%	29,753	32,481	(2,728)	-8.4%
Commercial Activity Tax	0	0	0	N/A	0	0	0	N/A
Public Utility	47,387	42,575	4,812	11.3%	47,387	42,575	4,812	11.3%
Kilowatt Hour	16,534	14,399	2,135	14.8%	22,642	22,659	(17)	-0.1%
Foreign Insurance	(39)	0	(39)	N/A	(98)	0	(98)	N/A
Domestic Insurance	53	0	53	N/A	(558)	0	(558)	N/A
Other Business & Property Tax	293	220	73	32.9%	246	253	(6)	-2.6%
Cigarette	86,319	84,996	1,323	1.6%	104,362	109,025	(4,664)	-4.3%
Soft Drink	0	0	0	N/A	0	0	0	N/A
Alcoholic Beverage	5,216	4,985	231	4.6%	10,521	10,900	(379)	-3.5%
Liquor Gallonage	3,184	3,093	91	3.0%	6,069	6,234	(165)	-2.6%
Estate	1,040	800	240	30.0%	1,082	1,100	(18)	-1.7%
Horse Racing	0	0	0	N/A	0	0	0	N/A
Total Tax Receipts	1,339,722	1,367,208	(27,486)	-2.0%	2,632,360	2,799,684	(167,324)	-6.0%
NON-TAX RECEIPTS								
Federal Grants	550,731	561,621	(10,891)	-1.9%	1,374,399	1,388,299	(13,900)	-1.0%
Earnings on Investments	0	0	0	N/A	0	0	0	N/A
License & Fees	6,481	5,347	1,134	21.2%	12,452	11,450	1,002	8.7%
Other Income	4,423	4,600	(177)	-3.9%	10,400	8,294	2,106	25.4%
ISTV'S	36	2,100	(2,064)	-98.3%	66	2,110	(2,044)	-96.9%
Total Non-Tax Receipts	561,670	573,668	(11,998)	-2.1%	1,397,317	1,410,153	(12,836)	-0.9%
TOTAL REVENUES	1,901,392	1,940,876	(39,484)	-2.0%	4,029,677	4,209,837	(180,160)	-4.3%
TRANSFERS								
Budget Stabilization	0	0	0	N/A	0	0	0	N/A
Liquor Transfers	0	12,000	(12,000)	-100.0%	15,000	24,000	(9,000)	-37.5%
Transfers In - Capital Reserve	0	0	0	N/A	0	0	0	N/A
Transfers In - Other	0	400	(400)	-100.0%	5,065	7,900	(2,835)	-35.9%
Temporary Transfers In	0	0	0	N/A	0	0	0	N/A
Total Transfers	0	12,400	(12,400)	-100.0%	20,065	31,900	(11,835)	-37.1%
TOTAL SOURCES	1,901,392	1,953,276	(51,884)	-2.7%	4,049,742	4,241,737	(191,996)	-4.5%

Table 2*
GENERAL REVENUE FUND RECEIPTS
ACTUAL - FY 2009 VERSUS FY 2008
($ in thousands)

REVENUE SOURCE	Month ACTUAL 2009	Month ACTUAL 2008	Month $ VAR	Month % VAR	Year-to-Date ACTUAL 2009	Year-to-Date ACTUAL 2008	Year-to-Date $ VAR	Year-to-Date % VAR
TAX RECEIPTS								
Non-Auto Sales & Use	545,469	537,767	7,702	1.4%	1,148,835	1,152,953	(4,118)	-0.4%
Auto Sales & Use	87,317	89,848	(2,531)	-2.8%	175,091	175,985	(893)	-0.5%
Subtotal Sales & Use	632,786	627,615	5,172	0.8%	1,323,927	1,328,938	(5,011)	-0.4%
Personal Income	543,866	579,844	(35,979)	-6.2%	1,087,027	1,187,344	(100,318)	-8.4%
Corporate Franchise	3,083	4,761	(1,678)	-35.2%	29,753	(6,648)	36,401	-547.5%
Commercial Activity Tax	0	0	0	N/A	0	0	0	N/A
Public Utility	47,387	41,641	5,746	13.8%	47,387	41,642	5,746	13.8%
Kilowatt Hour	16,534	31,435	(14,901)	-47.4%	22,642	61,444	(38,802)	-63.1%
Foreign Insurance	(39)	1	(40)	-4999.3%	(98)	16	(114)	-704.7%
Domestic Insurance	53	40	13	31.8%	(558)	41	(599)	-1461.7%
Other Business & Property Tax	293	245	48	19.5%	246	281	(35)	-12.4%
Cigarette	86,319	91,894	(5,575)	-6.1%	104,362	113,130	(8,769)	-7.8%
Soft Drink	0	0	0	N/A	0	0	0	N/A
Alcoholic Beverage	5,216	4,842	374	7.7%	10,521	10,588	(67)	-0.6%
Liquor Gallonage	3,184	2,946	238	8.1%	6,069	5,939	131	2.2%
Estate	1,040	130	910	698.9%	1,082	160	922	576.1%
Horse Racing	0	0	0	N/A	0	0	0	N/A
Total Tax Receipts	1,339,722	1,385,393	(45,672)	-3.3%	2,632,360	2,742,874	(110,514)	-4.0%
NON-TAX RECEIPTS								
Federal Grants	550,731	748,472	(197,742)	-26.4%	1,374,399	1,075,719	298,680	27.8%
Earnings on Investments	0	0	0	N/A	0	0	0	N/A
License & Fee	6,481	7,096	(615)	-8.7%	12,452	13,176	(724)	-5.5%
Other Income	4,423	4,182	241	5.8%	10,400	7,942	2,458	31.0%
ISTV'S	36	29	7	24.1%	66	39	27	69.1%
Total Non-Tax Receipts	561,670	759,780	(198,109)	-26.1%	1,397,317	1,096,875	300,442	27.4%
TOTAL REVENUES	1,901,392	2,145,173	(243,781)	-11.4%	4,029,677	3,839,749	189,928	4.9%
TRANSFERS								
Budget Stabilization	0	0	0	N/A	0	0	0	N/A
Liquor Transfers	0	14,000	(14,000)	-100.0%	15,000	39,000	(24,000)	-61.5%
Transfers In - Capital Reserve	0	0	0	N/A	0	0	0	N/A
Transfers In - Other	0	5,402	(5,402)	-100.0%	5,065	15,386	(10,321)	-67.1%
Temporary Transfers In	0	0	0	N/A	0	0	0	N/A
Total Transfers	0	19,402	(19,402)	-100.0%	20,065	54,386	(34,321)	-63.1%
TOTAL SOURCES	1,901,392	2,164,575	(263,182)	-12.2%	4,049,742	3,894,135	155,607	4.0%

GENERAL REVENUE FUND DISBURSEMENTS

Across all fund uses, total year-to-date GRF disbursements are $5,587.4 million.

Fund Use	Includes:	YTD Disbursements
Expenditures and transfers between agencies (ISTVs)	State agency operations, subsidies, tax relief, debt service payments, and pending payroll (if applicable)	$5,198.4 million
Transfers	Temporary or permanent transfers out of the GRF that are not agency expenditures	$389.0 million
TOTAL GRF DISBURSEMENTS:		$5,587.4 million

Year-to-date expenditures and interagency transfers are 1.6% less than the estimates. See table 3 for additional information. Please note that disbursement estimates will be revised for the October financial report in accordance with the additional FY 2009 GRF budget reductions that were announced earlier today.

GRF disbursements are reported according to functional reporting categories, and this section contains information regarding each category. Variance information is included on an agency-specific basis as a component of the category summaries. In the event that an agency spent its GRF appropriation according to plan during the month, a variance would not exist to be explained.

Primary, Secondary, and Other Education

This category includes expenditures made by the School for the Blind, the School for the Deaf, E-Tech and the Department of Education. August expenditures in this category were $631.2 million.

- August disbursements by the Department of Education totaled $624.3 million. Compared with the estimate for August, The department's spending was below estimate by $25.1 million or 3.9%. Higher than anticipated spending is exhibited in line items for the Ohio Educational Computer Network, Student Assessment and the Education Management Information System, while spending for Foundation Funding is $58 million (10.7%) lower than projected.

Higher Education

August disbursements for Higher Education were $243.3 million, representing a variance of $12.4 million (5.4%) above the estimate for the month. Year-to-date disbursements were $423.3 million, representing a variance totaling $12.4 million (3.0%) above the estimate. Disbursements for the Ohio College Opportunity Grant (OCOG) program and the Ohio Instructional Grant (OIG) program were $22.2 million more than anticipated for the month. August is the final month for campuses to request reimbursement for the summer term, so an increase in payments was noted. This variance was offset by the Choose Ohio First scholarship, for which distributions in the month were $2.5 million less than estimated. Grant agreements for the program have not yet been processed; however, disbursements will begin in the fall.

Public Assistance and Medicaid

August expenditures in this category, which includes all GRF expenditures by the Department of Job & Family Services, were $959.4 million.

<u>Public Assistance and Non-Medicaid</u>
This sub-category includes, but is not limited to, the following types of expenditures: social services such as adoption assistance and disability financial assistance; state match for federal child care and TANF grants; administrative support expenses including payroll and equipment; and county administration for public assistance programs.

- For the month of August, ODJFS non-Medicaid General Revenue Fund disbursements total $51.4 million.

- When compared to August FY 2009 disbursement estimates, in aggregate, actual disbursements were $7.9 million (14.5%) under estimate. This is primarily attributable to the following:
  - Approximately $1.8 million in underspending was in the support services line item. Lower than anticipated disbursements are attributable to billings for central administration, maintenance, and the early retirement incentive plan not arriving in August as originally anticipated.
  - Approximately $1.8 million in underspending was in the county child support administration line item. The underspending occurred due to lower than anticipated requests for funding advances.
  - Approximately $2.5 million in underspending was in the computer projects line item (600-416). The underspending occurred due to lower than anticipated prior year invoices.

<u>Medicaid</u>
This category includes expenditures by the Department of Job & Family Services for Medicaid services. Please note that administrative costs related to the ODJFS Medicaid program are included in the previous sub-category.

Expenditures
August disbursements for Medicaid totaled $907.7 million in GRF, and $907.8 million for all funds. Year-to-date disbursements total $2,270.6 million in GRF, and $2,270.8 million for all funds. The major categories of spending for the month August included $349.3 million in Managed Care payments ($251.3 million for the CFC program and $98 million for the ABD plans), $218 million in Nursing Home expenditures, and $64.5 million for Inpatient Hospitals.

Caseload
The Medicaid caseload assumptions for FY 2009 match the corrective appropriations in H.B. 562. In July, the most recent caseload data available, there was no variance compared to what was projected in the corrective bill and actual enrollment for the overall program. In July 42,000

more consumers enrolled onto the program, of which 35,300 can be attributed to the CFC eligibility category and 6,700 can be attributed to the ABD eligibility category.

Program Highlights
House Bill 119 created a new eligibility category for Medicaid that provides health coverage to working Ohioans with disabilities. Medicaid Buy-In for Workers with Disabilities (MBIWD) was created to encourage Ohioans with disabilities to work and still keep their health care coverage. Enrollment in the MBIWD began on April 1, 2008. Four months after implementation nearly 770 disabled Ohioans have enrolled in the program. Consumers wishing to enroll in this program must meet certain financial eligibility criteria and are required to pay a premium if they have an annual gross income greater than $15,600 (150% of the Federal Poverty Limit).

Health and Human Services

This category includes GRF expenditures for the following state agencies: Aging, Mental Health, MR/DD, ODADAS and Health. Examples of expenditures in this category include: administration of the state's psychiatric hospitals; operating subsidies to county boards of MR/DD; various immunization programs; and Ohio's long term care ombudsman program. To the extent that these agencies spend GRF to support Medicaid services, that spending is reflected in this category instead of the previous category.

August expenditures in this category were $93.3 million. Significant notes include:

- The Department of Health disbursed $5.0 million in the month of August, or 23% below the plan of $6.45 million. A majority of the under spending ($1.65 million) was due to Child and Family Health Services, which was less because of expenses having been paid in July instead of August. Additional underspending occurred in Immunizations ($900K), and AIDS Prevention ($885K). Immunization was under due to fewer prior year payments being made than planned; AIDS was less due to timing. One significant overrun ($1.7 million) was in the line item for Medically Handicapped Children. This was due to expenses being paid early and the Department using more GRF funds than federal funds. (There were no planned expenditures in July and August.) Spending on this program should be back on plan by the end of the quarter. The Department was 71% above plan ($4.1 million) in the month of July.

- The Department of Aging disbursed $16.9 million in GRF in the month of August, or 1% under plan. Within this there were two significant variances. Expenditures in the Residential State Supplement program were $829K above plan due to timing of the department's transfers to JFS. This should be back on schedule by the end of the quarter. Assisted Living was under plan due to the GRF payment for August being reduced since the GRF payment was over plan in July.

- The Department of Mental Health disbursed $41.9 million in the month of August, which was $5.1 million, or 13.8%, greater than the estimate. The overage occurred within the Department's subsidy lines, ALI 334408, Community and Hospital Mental Health Services and ALI 335505, Local Mental Health Systems of Care and is attributable to the timing of transfers requested by County Boards.

- The Department of Mental Retardation and Developmental Disabilities disbursed $24.4 million in the month of August, which is $4.3 million, or 21.0%, greater than the estimate. The variance can be attributed to spending exceeding the estimates in the Medicaid Waiver- State Match line item, 322416. These funds are disbursed to the County Boards of MR/DD to pay waiver service costs. Variances between actual expenditures and estimated disbursements occur because providers have 365 days to submit bills for services they have provided.

Justice and Public Protection

This category includes GRF expenditures by the following state agencies: Department of Rehabilitation & Corrections, the Department of Youth Services and the Department of Public Safety. In the aggregate, August expenditures in this category were $131.1 million.

- The Department of Rehabilitation and Correction (DRC) disbursed $95.8 million in the month of August, which was $29.9 million (23.8%) less than the $125.7 million estimate for the month. This variance occurred because DRC was not invoiced as expected by the Office of Support Services (Department of Mental Health) for medical supplies and other goods.

- The Department of Youth Services (DYS) disbursed $14.0 million in the month of August, or $0.2 million (1.5%) less than the $14.2 million estimate for the month.

- In last month's report, a variance for DYS existed due to the timing of a number of July transactions not having been posted to the OAKS general ledger at the time of the report being published. All DYS transactions for the month of July now have been posted to the general ledger. The final DYS disbursement number for July was $59.4 million, which was $2.1 million (3.7%) more than the $57.3 million disbursed in July of fiscal year 2008.

Environmental Protection & Natural Resources

August expenditures in this category were $7.9 million, which was $900,000 above estimate.

Transportation

August expenditures in this category were $941,000, which was $506,000 below estimate for the month.

General Government

August expenditures in this category were $19.2 million, which was $2.2 million below estimate for the month.

Community & Economic Development

August expenditures in this category were $8.2 million.

- During the month of August the Department of Development disbursed $6.7 million in GRF, which is $1.5 million below the August estimate. This variance was due to the unpredictable grant subsidy payments from current and prior years.

- The primary lines accounting for the variance where grantees did not request their expected reimbursements were primarily from the Regional Offices & Economic Development, Third Frontier Action Fund, Appalachian Local Development District, and the Travel & Tourism Grants appropriation line items.

Tax Relief & Other

August tax relief disbursements totaled $136.1 million, which exceeds the monthly estimate by $78.7 million (137%). Both the month and year over year variance are due to requests for payments related to the 10 percent and 2.5 percent rollback on non-homestead eligible properties being received earlier than anticipated. As was the situation in FY 2008, the additional tax relief appropriations attributable to the expansion of the homestead exemption authorized in HB 119 will not be included in the OBM estimates for FY 2009, as HB 119 sets forth a Controlling Board process for increasing appropriations and funding the increase through lapses in debt service and the transfer of excess interest earnings on tobacco securitization proceeds.

The tax relief disbursements are divided between two recipients – school districts and local governments. The $49.5 million in disbursements for school district tax relief during the month of August was identical to the monthly estimate, and the resulting year-to-date spending is $49.5 million. The $86.6 million in disbursements for local government tax relief during the month of August was $78.7 million above estimates for month and also considerably above the $22.2 million disbursed during the same month a year ago

Debt Service

August expenditures in this category were $38.7 million.

Table 3*
GENERAL REVENUE FUND DISBURSEMENTS
ACTUAL FY 2009 VS ESTIMATE FY 2009
($ in thousands)

Functional Reporting Categories Description	MONTH ACTUAL AUGUST	MONTH ESTIMATED AUGUST	MONTH $ VAR	MONTH % VAR	YEAR-TO-DATE YTD ACTUAL	YEAR-TO-DATE YTD ESTIMATE	YEAR-TO-DATE $ VAR	YEAR-TO-DATE % VAR
Primary, Secondary and Other Education	631,153	654,279	(23,126)	-3.5%	1,287,837	1,310,963	(23,126)	-1.8%
Higher Education	243,357	230,949	12,408	5.4%	423,303	410,895	12,408	3.0%
Public Assistance and Medicaid	959,409	985,635	(26,225)	-2.7%	2,398,893	2,425,119	(26,225)	-1.1%
Health and Human Services	93,301	85,220	8,081	9.5%	266,801	258,719	8,081	3.1%
Justice and Public Protection	131,124	161,655	(30,531)	-18.9%	412,853	443,384	(30,531)	-6.9%
Environmental Protection and Natural Resources	7,878	6,978	900	12.9%	19,101	18,201	900	4.9%
Transportation	941	1,447	(506)	-35.0%	2,135	2,641	(506)	-19.2%
General Government	19,167	21,383	(2,216)	-10.4%	61,925	64,140	(2,216)	-3.5%
Community and Economic Development	8,227	11,482	(3,255)	-28.3%	16,635	19,890	(3,255)	-16.4%
Tax Relief and Other	136,965	137,115	(151)	-0.1%	150,086	150,237	(151)	-0.1%
Capital Outlay	0	0	0	N/A	0	0	0	N/A
Debt Service	38,692	38,712	(20)	-0.1%	158,851	158,871	(20)	0.0%
Pending Payroll	0	0	0	N/A	0	0	0	N/A
Total Expenditures & ISTV's	**2,270,214**	**2,334,855**	**(64,641)**	**-2.8%**	**5,198,419**	**5,263,060**	**(64,641)**	**-1.2%**
Transfers Out:								
OPER TRF OUT-OTH	12,707	200	12,507	N/A	229,800	217,293	12,507	N/A
OPER TRF OUT-TEMPORARY	159,159	159,159	0	N/A	159,159	159,159	0	N/A
Total Transfers (Out)	**171,866**	**159,359**	**12,507**	**N/A**	**388,959**	**376,452**	**12,507**	**N/A**
Total Fund Uses	**2,442,080**	**2,494,214**	**(52,134)**	**N/A**	**5,587,378**	**5,639,512**	**(52,134)**	**N/A**

Table 4*
GENERAL REVENUE FUND DISBURSEMENTS
ACTUAL FY 2009 VS ACTUAL FY 2008
($ in thousands)

Functional Reporting Categories Description	MONTH ACTUAL 2009	MONTH ACTUAL 2008	MONTH $ VAR	MONTH % VAR	YEAR-TO-DATE ACTUAL 2009	YEAR-TO-DATE ACTUAL 2008	YEAR-TO-DATE $ VAR	YEAR-TO-DATE % VAR
Primary, Secondary and Other Education	631,153	842,471	(211,318)	-25.1%	1,287,837	1,447,990	(160,153)	-11.1%
Higher Education	243,357	177,692	65,665	37.0%	423,303	424,914	(1,611)	-0.4%
Public Assistance and Medicaid	959,409	958,634	775	0.1%	2,398,893	1,964,949	433,945	22.1%
Health and Human Services	93,301	124,341	(31,040)	-25.0%	266,801	263,559	3,242	1.2%
Justice and Public Protection	131,124	142,428	(11,304)	-7.9%	412,853	402,928	9,924	2.5%
Environmental Protection and Natural Resources	7,878	5,648	2,230	39.5%	19,101	20,597	(1,496)	-7.3%
Transportation	941	2,590	(1,650)	-63.7%	2,135	3,266	(1,131)	-34.6%
General Government	19,167	28,457	(9,290)	-32.6%	61,925	59,162	2,762	4.7%
Community and Economic Development	8,227	9,485	(1,259)	-13.3%	16,635	13,489	3,146	23.3%
Tax Relief and Other	136,965	91,417	45,548	49.8%	150,086	92,460	57,627	62.3%
Capital Outlay	0	0	0	N/A	0	0	0	N/A
Debt Service	38,692	28,825	9,867	34.2%	158,851	141,987	16,863	11.9%
Pending Payroll	0	0	0	N/A	0	0	0	N/A
Total Expenditures & ISTV's	**2,270,214**	**2,411,989**	**(141,775)**	**-5.9%**	**5,198,419**	**4,835,301**	**363,117**	**7.5%**
Transfers Out:								
OPER TRF OUT-BUD STABILIZATION	0	0	0	N/A	0	0	0	N/A
OPER TRF OUT-OTH	12,707	266,883	(254,176)	-95.2%	229,800	287,945	(58,145)	-20.2%
OPER TRF OUT-TEMPORARY	159,159	0	159,159	N/A	159,159	0	159,159	N/A
Total Transfers (Out)	**171,866**	**266,883**	**(95,017)**	**-35.6%**	**388,959**	**287,945**	**101,014**	**35.1%**
Total Fund Uses	**2,442,080**	**2,678,872**	**(236,792)**	**-8.8%**	**5,587,378**	**5,123,246**	**464,132**	**9.1%**

FUND BALANCE

Table 5 describes the General Revenue Fund (GRF) ending fund balance for FY 2009. Based on February 2008 estimates, FY 2009 revenue disbursements, transfers, and encumbrances would result in a GRF ending fund balance for FY 2009 of $269.4 million. However, OBM has revised expected revenues and spending for FY 2009 downward by $540 million. These updated estimates will be described in forthcoming budget directives and a revised ending fund balance will be presented in the October 10, 2008 financial report.

The GRF ending fund balance should not be considered as a balance available for expenditure in FY 2009 nor should it be considered as equivalent to the FY 2009 surplus calculation as defined in Section 131.44 of the Ohio Revised Code.

It is important to note that the GRF ending fund balance will be impacted by any GRF expenditures or transfers that may be authorized by the General Assembly or by the Controlling Board during the course of the fiscal year.

FUND BALANCE
GENERAL REVENUE FUND
FY 2009
($ in thousands)

July 1, 2008 Beginning Cash Balance	$ 1,682,002
Plus FY 2009Estimated Revenues	19,564,863
Plus FY 2009Estimated Federal Revenues	6,632,767
Plus FY 2009Estimated Transfers to GRF	1,521,105
Total Estimated Sources Available for Expenditure & Transfer	29,400,737
Less FY 2009Estimated Total Disbursements	27,587,947
Less FY 2009Estimated Total Encumbrances as of June 30, 2008	690,905
Less FY 2009Estimated Transfers Out	852,439
Total Estimated Uses	29,131,291
FY 2009 Estimated Ending Fund Balance	$ 269,446

FEATURED ANALYSIS

State Employee Payroll Costs

The cost of wages and benefits for state employees is a significant expense within Ohio's overall state budget. In State Fiscal Year 2008, total payroll expenses were approximately $4.4 billion. Each state agency funds payroll costs for its respective employees through its operating budget, which is appropriated by the General Assembly and implemented by the executive branch.

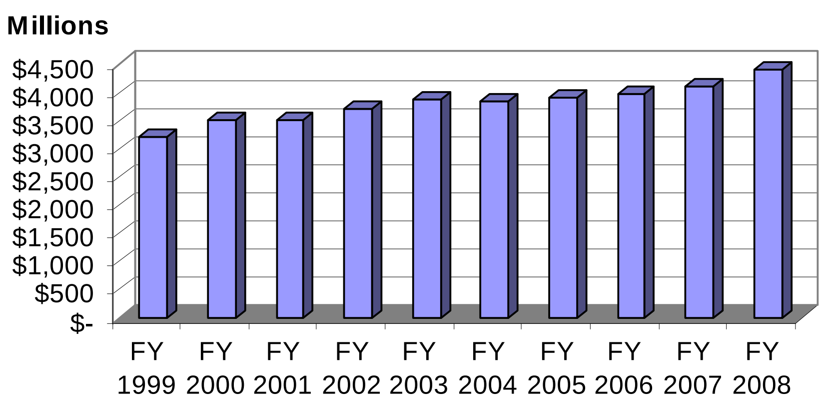
As of August 15, 2008 Ohio has 62,539 state employees. Their roles are numerous and diverse, including: juvenile corrections officers, insurance regulators, nurses, budget analysts, highway technicians, legislative aides, architects, Supreme Court justices, grants administrators to school districts, state troopers, economists and park rangers.

This article contains a brief overview of state payroll costs and four items that may impact these costs during the FY 10/11 biennium: employee health insurance premiums; the upcoming negotiation of collective bargaining agreements with state employee unions; agency budget request planning targets for FY 10/11 that are below FY 2009 appropriation; and the yet-evolving impact of early retirement incentive plans on specific agencies' payroll costs.

State Payroll Costs

Total state payroll costs have grown by approximately 37% in the last ten years—from $3.2 billion in FY 1999 to $4.4 billion in FY 2008. Wages and benefits paid by the General Revenue Fund represent 47%—that is, almost half—of all payroll costs incurred annually. In FY 2008, the GRF portion of payroll amounted to $2.1 billion.

Total State Payroll, FY 1999 - FY 2008

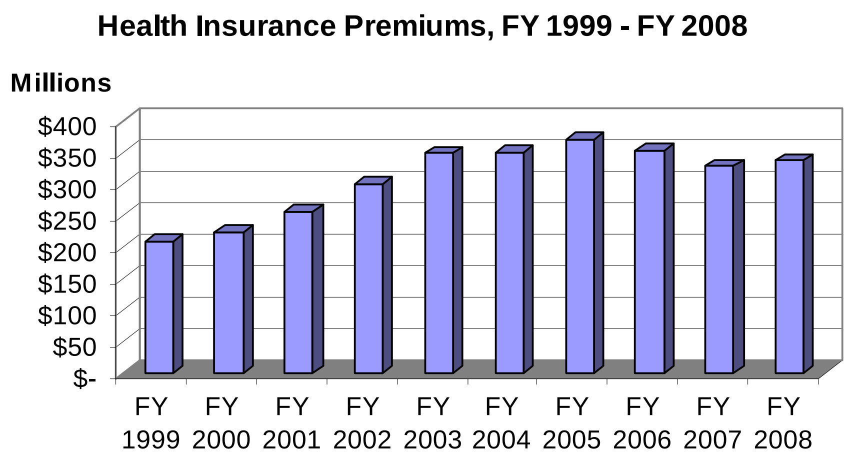


A majority of these costs—namely, wages for time worked, paid time off, overtime, wage-based benefit contributions like retirement, and various payroll charges that support state agencies like the Department of Administrative Services and OBM—are directly linked to hourly rates of pay.

Health Insurance Premiums

The most significant payroll item that is not linked to the hourly pay rate is health insurance premiums. The state shares health insurance costs with its employees. Agencies pay 85% of the premium for full-time employees (less for part-time depending on the number of hours worked), with employees responsible for the remaining 15% of the premium. As a result, state agencies now contribute well over $300 million per year toward their employees' health insurance.

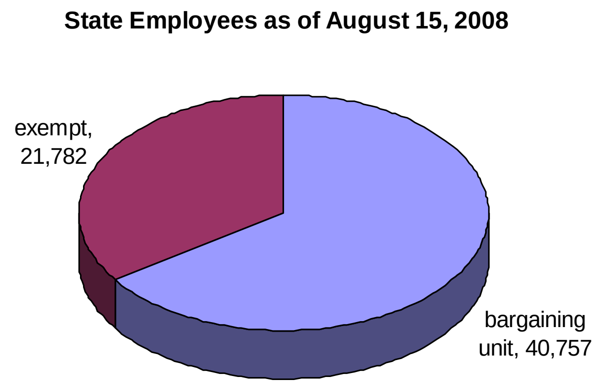
As noted above, the state pays a fixed percentage of whatever health insurance premiums are, as opposed to a fixed dollar amount. Consequently, the high rate of medical inflation in recent years has meant that agency costs for this benefit have grown faster than overall payroll costs. While total payroll costs grew by approximately 37% over the last ten years, agency health insurance contributions increased by more than 68% during the same period.



In FY 2007 and FY 2008, state agencies were able to skip a month's worth of health insurance premium contributions in each year to draw down accumulated assets. However, in FY 2009 agencies resume paying a full year of contributions. In OBM's budget guidance to agencies for FYs 2010-2011, agencies were instructed to assume that annual medical inflation will continue to be in the high single digits, outpacing the growth in other payroll costs.

Collective Bargaining

Approximately 65% of Ohio's state employees are members of a bargaining unit. Current collective bargaining agreements that govern wages and benefits for distinct groups of state employees expire by the end of the current biennium. As a result, the Administration will be negotiating with the unions that represent state employees for new contract agreements. The new contracts will impact agency budgets in the FY 10/11 operating biennium.



The Administration will engage in collective bargaining with the unions that represent many state employees at the same time as the budget process that will determine agency budgets for the FY 10/11 operating biennium. The administration first bargains with the Ohio Civil Service Employees Association (OCSEA), which is the largest of the state employee unions. This will begin in fall 2008. Once the provisions of this contract are determined, the state negotiates with the other employee unions beginning in spring 2009.

Agency Budget Request Targets for FYs 10/11

There are a number of important factors that impact wage and benefit costs in agency budgets. Even absent any cost-of-living pay raises, agency payroll costs will increase approximately 1% annually due to step and longevity increases that employees receive as additional compensation for their tenure and experience. Agency payroll costs also increase automatically due to higher health insurance premiums, since the state pays a fixed percentage of whatever premiums turn out to be.

In contrast to these "automated" increases in payroll costs, OBM's budget guidance to agencies limits their GRF budget requests for FYs 10/11 to 90% or 95% of their FY 2009 appropriations. Thus, GRF-supported agencies in particular will be squeezed to cover automated payroll increases let alone any additional wage or benefit items that might be negotiated.

As a specific example, each 1% pay raise in the next biennium would cost state agencies approximately $40 million ($19 million GRF) annually. Thus, 3% annual pay raises in both FY 2010 and FY 2011 would cost agencies with GRF-supported staff an extra $57 million in the first year of the biennium and an additional $59 million above that in FY 2011. Note that the total increase in the second year of the biennium compared to FY 2009 is the sum of each year's cost. In other words, GRF payroll would cost $114 million more in FY 2011 than in FY 2009.

Anticipated Early Retirement Incentive (ERI) Savings

To help agencies blunt the impact of increased payroll costs and a likely decrease in GRF funding for the FY10-11 budget, OBM issued a memorandum in January encouraging agencies to consider offering early retirement incentive (ERI) plans to their eligible employees if they could derive savings and achieve management goals, such as restructuring to improve efficiency. By offering an ERI, an agency essentially agrees to purchase service credit for an employee to allow them to either retire earlier or with greater benefits than normal. Savings are generated by the agency if it refills positions vacated due to the ERI at a sufficiently lower cost.

Thus far, ten agencies have moved forward to implement OBM-approved ERI plans, resulting in 379 state employees accepting early retirement as of August 14, 2008. This number will continue to increase through out this fiscal year since six of the agency plans have not yet closed.

While fewer employees have accepted ERIs than originally estimated by the agencies, agencies can still collectively anticipate realizing as much as $38 million in total savings through FY11. In the case of a mandatory ERI[1], an agency may still realize anticipated savings even if fewer than estimated employees accept an ERI. Frequently, an agency will design a plan with the hope of reducing the need for layoffs, so the number of employees laid off will increase if fewer employees accept the ERI. While not an ideal situation, in the case of agencies that offered mandatory ERIs this will likely result in anticipated savings being realized through layoffs instead of ERIs.

[1] An agency is required to offer a mandatory ERI if it implements layoffs or closes an institution.