Sen. Fumo: Senate Democratic Appropriations Committee mid-year analysis of the state budget.
Text of Dec. 21 report.
2004-05 Fiscal year mid-year analysis

Economic Outlook: The Governor in his mid year briefing accentuated the negatives of the economic situation in the Commonwealth and clearly things are sluggish compared to the booming 1990's. Employment has been slow to recover from the job losses of the recession in 2001. Business profits were better last year than they are now. High oil prices have increased costs for both individual and businesses. The Christmas season seems to be sluggish so far. But all in all the economy is reasonably strong.

Employment was up strongly in October as 337,000 new jobs were added in this country. The November job creation numbers were not as good, as only 112,000 jobs were created. The experts had expected 200,000 new jobs in November so the disappointment was heightened by the lower number, but after the huge October numbers, one month is nothing to be concerned about. Still it is typical of this recovery - growth is in spurts and the economy can't seem to get into a rhythm. But even with the lower November growth there are 2 million more people employed this November than there were last November in this country. The retail sector was down in the November numbers. That isn't supposed to happen just prior to Christmas. Manufacturing was another sector that slipped in November, even after all the good news surrounding the decline of the dollar and that new order numbers were up.

Real GDP is predicted by Global Insight, the economic forecasting firm of the Commonwealth, to grow by 3.37% over the course of the 2004-05 fiscal year. That is solid, sustainable growth. However, in June, when the revenue projections and the budget were implemented, Global Insight was projecting 4.175%. Expectations have decreased 19% since June. When the Governor expresses caution for the economic future, it is understandable.

High oil prices were a major threat to the economy for several months but prices have come down considerably within the last three weeks. In fact it was higher oil prices that removed a full .2% from Global Insight's prediction of GDP. But the threat has receded somewhat as the price per barrel fell from $55 to a much more manageable $48. Global Insight decreased their estimate based on oil at more than $50 per barrel in both the last quarter of 04 and the first quarter of 05. Global Insight feels that they may have over-estimated the concern.

The health of the economy currently is clearly a delicate matter but the threats that the Governor's office are touting are factored into Global Insights estimate of 3.37% real GDP growth. They estimate the chances of the economy doing much worse but not slipping into a recession at only 20%. Global Insight does not even view another recession in the next year and a half as a reasonable possibility.

Current Revenue Surplus: The current amount of revenue collected above the Governor's official revenue estimate is $176 million which is 2.1% above the official estimate. This overage is primarily from four sources as shown on the table.

Revenue Collections as of November 30, 2004
(In Thousands of Dollars)

Revenue Sources	Actual	Estimated	Difference	% Diff.	% Growth from 03-03
Total Business Taxes	853,910	800,300	53,610	6.7%	25.0%
Sales	3,369,354	3,353,000	16,354	0.5%	27.4%
Cigarette	329,736	353,700	(23,964)	-6.8%	19.3%
Malt Beverage	10,992	10,500	492	4.7%	20.0%
Liquor	76,647	73,600	3,047	4.1%	37.4%
Personal Income	3,078,015	3,030,600	47,415	1.6%	42.4%
Realty Transfer	210,563	178,500	32,063	18.0%	42.5%
Inheritance	292,581	319,600	(27,019)	-8.5%	11.9%
Minor & Repealed	(1,569)	(1,900)	331	-17.4%	-160.9%
Total Tax Revenue	8,220,229	8,117,900	102,329	1.3%	31.7%
Liquor Store	-	-	-	0.0%	0.0%
Licenses. Fees & Misc.	217,087	140,500	76,587	54.5%	110.3%
Fines, Pen. & Interest	8,513	11,500	(2,987)	-26.0%	-14.9%
Total Non-Tax Rev.	225,600	152,000	73,600	48.4%	99.2%
Total General Fund Rev.	8,445,829	8,269,900	175,929	2.1%	32.9%

As the table shows, the largest component of the overage is licenses, fees and miscellaneous income. A large influx of escheated property in October is responsible for this overage. There is probably not more money from escheated property and this surplus is unlikely to grow any further this fiscal year.

Much more promising for further surplus-building are the total business taxes collections. The majority of corporate taxes are received in September, December, March, April and June. It was collections in October, however, that were most instrumental in building the current overage as collections were $42 million over official estimates. According to the mid-year briefing the majority of that was due to a $35 million settlement of prior year taxes, not from collections from this year. Regardless, there is still a $19 million overage in September. If collections are good in the remaining months like they were in September, business taxes will be a solid contributor to the ending surplus.

Personal income tax collections are currently $47 million over estimates but that is only 1.6% above estimates. Unless job growth picks up substantially it doesn’t appear that PIT collections will be a huge contributor to the final surplus. Realty transfer tax collections are $32 million over estimates, which is 18% more than expected. It is expected that the housing market will cool over the next few months but experts have been predicting a cooling of the housing market for the last 6 years and it hasn't occurred yet.

Three revenue sources are reductions or non-factors to the year to date surplus. While there is an overage of $16 million in sales tax collections in all reality sales tax collections are even with estimates since $16 million is equal to on ½ of one percent above estimates. If, as predicted, the Christmas season is slow sales tax collections could turn into a deficit. Cigarette tax collections are $24 million below estimates. The shortage is probably due to loss of tax revenue from cross boarder and internet sales. Inheritance tax collections are $27 million below estimates. It isn't clear whether this shortfall is due to a greater loss of revenue from the state's acceptance of federal inheritance tax changes or a temporary shortfall because the timing of inheritance tax receipts is notoriously difficult.

In the mid-year budget briefing the Governor acknowledged the burgeoning revenue surplus but refused to say what he anticipates the final surplus to be. It is safe to say that the ending surplus is going to be between $300 and $650 million. At this point the best guess is somewhere in the higher portion of that range. A surplus of $500 million is most likely at this point. Christmas sales tax and employment numbers will be crucial to the final amount of the surplus.

The following chart shows the percentage of surplus or deficit collected by November compared to the percentage for the full fiscal year. Except for fiscal years 2000-01 and 2003-04, the percentage of overage collected by November averaged 56% of the percent of the of the final budget surplus. If the percent of surplus for this November were to be 56% of the final surplus then the final 2004-05 surplus would be $871 million. For the reasons discussed in the Economic Outlook section of this report the surplus won't be that high.

If the year-ending surplus is double the November surplus or $350 million it would be only 1.47% above official estimates. That would be lower than the current November surplus of 2.1%. The chart above suggests that it is unlikely to have the final percentage of surplus be less than what has been achieved in November. In the two years in the last decade that the final percentage of surplus was lower than the November percentage, as shown in the chart, there were extenuating circumstances. In fiscal year 2000-01 the country went into a recession in March that dragged down the final surplus dramatically. In 2003-04 the General Assembly raised taxes in December and so the final surplus was based not on the original estimate but on a new estimate made 6 months into the fiscal year. The bases of the percentages changed and therefore no real comparison is possible.

Outlook for General Fund: The condition of the economy determines the revenue picture, which in turn is the major determinate of the balance sheet of the Commonwealth. In July the Governor anticipated having $22.883 billion in funds to spend in the 2004-05 fiscal year. Expenditures were appropriated at $22.876 billion leaving about a $6 million balance expected at the end of the fiscal year. Six months later revenue collections look to be $500 million higher than was anticipated which would bolster the ending balance substantially

The Governor proposed supplemental appropriations of $164 million in his mid year briefing. So the final ending balance will be in the neighborhood of $340 million. That would be partially distributed to the new rainy day fund as part of the 25% automatic transfer of each ending year surplus to that fund. The remaining $255 million would roll over into the next fiscal year.

The Governor's proposed supplemental appropriations are explained in further detail throughout this report. While the Governor was not specific about how these supplementals would be funded, it appears that there will be significant lapses through the use of cost savings proposals already put in place by this administration.

The Governor's briefing did not include a list of court cases that might have fiscal impact on this fiscal year. It was helpful to gauge the risks that might have to be dealt with to keep the budget balanced.

Community and Economic Development: Following a bumpy ride that has included continued dips in commonwealth employment for the past several years, the employment picture has finally begun to brighten. Total payroll employment in Pennsylvania has increased by nearly 70,000 jobs since December of 2003. More significantly, a growth rate of more than 1%, tracking national averages, signals the first time the commonwealth has matched national employment trends in more than a decade.

The commonwealth continues to invest significant state dollars in an array of loan and grant incentive programs to attract jobs. These programs will now be bolstered by the General Assembly's approval of the Governor's $2 billion economic stimulus program. The newly formed Commonwealth Financing Authority (CFA) will be responsible for administering $1.3 billion of these programs for infrastructure, venture capital, tourism and agriculture promotion, community revitalization, and business assistance. The Governor will directly control additional capital investments of $700 million through the Redevelopment Assistance Capital Program, while the Pennvest program will invest up to $150 million for water and sewer infrastructure improvements.

Corrections: Budgeted spending for the Department of Corrections will rise above $1.3 billion, an increase of more than $39.3 million, or a 3% increase from the 2003-2004 fiscal year. The inmate population is the single most important factor that affects cost in the correctional system. The offender population was 40,674 by the end of November 2004. In comparison with the prior year this shows a gradual decline in population. It was forecast that the inmate population would continue to grow in 2004 and reach 42,409 when in fact there has been a decrease of 1.4% (605 inmates.) When factoring the cost of inmate health care, education and training expenses the average cost per inmate is anticipated to be $32,000 annually.

The Commonwealth's current budgeted corrections system includes 28 institutions and 14 community corrections facilities. SCI Pittsburgh has continued to downsize and will be "moth-balled" at the end of this year. This means that a limited number of personnel will be maintained at the facility until the exact closing date is determined by the Commonwealth. SCI Forest, a new institution, opened this year and has a capacity for 2,000 inmates.

New legislation passed this year is anticipated to assist in reducing the inmate population. The State Intermediate Punishment Program (SIP) involves placing appropriate, non-violent offenders in a structured AOD (Alcohol or other drugs) treatment program. The offender would serve seven months in a correctional facility and then be placed in either a Community Corrections Center or a contracted group home within the community. The Department is anticipating an overall savings of approximately $28,000 per participant with the goal of having 1500 inmates participate each year. Research indicates that treatment for addicted offenders can be effective in reducing recidivism rates by 25% or more.

Education: Federal No Child Left Behind requirements continue to require states to adopt comprehensive testing programs to measure student classroom performance, with expectations that all children will eventually be able to achieve certain levels of proficiency by the year 2014. The commonwealth's unprecedented new investment in basic education programs will likely focus more interest on how to measure the impact of these efforts to enable school districts to meet state academic standards.

The new $200 million Accountability Block Grant program, $46 million for new tutoring programs, a $15 million state supplement for federal Head Start programs, and a $175 million increase in Basic and Special Education subsidies for local school districts are the major components of more than $500 million in increased basic education spending during the 2004-05 fiscal year.

The Governor's proposed budget for the coming fiscal year is likely to advocate for further increases in several of these programs. However, a commitment was made by the Governor not to seek an increase in the $200 million Accountability Block Grant for the 2005-06 fiscal year. While the new spending targeted funding for early learning programs, and initiatives to help students not currently meeting established state academic standards, it will be far too early during the coming fiscal year to assess the ultimate effectiveness of these efforts.

Meanwhile, public education advocates will continue to call for greater efforts to provide a more equitable state subsidy system for local school districts. Per pupil spending continues to vary dramatically within a system predominantly funded through local revenue sources.

The enactment of a long sought property tax relief program, primarily funded with slots generated income from newly legalized gaming facilities, is expected to fund significant tax relief among all school districts. Unfortunately, the potential delay in establishing the gaming oversight board, and the licensing of gaming facilities, may delay meaningful tax relief for several more years. When the legislation was enacted it was hoped that tax payers would receive their initial homestead tax relief during the 2006-07 fiscal year. That possibility now appears highly remote.

Local school districts will have to decide by May of 2005 if they want to participate in the state funded property tax relief plan. If they choose to do so, districts will become subject to new limitations on their future ability to adopt local tax increases above annual rates of inflation. The limitations will require voter referendum approval for increases above the inflation rate. These limitations will become effective for school budgets enacted for the 2006-07 fiscal year, regardless of when initial distributions are made for state funded property tax relief. School districts will also have the option of placing referendum questions on the Fall 2005 ballot giving tax payers the local option of increasing local wage taxes in exchange for funding additional property tax relief.

Growing Greener I and II: In his FY 2004-05 budget proposal, the Governor cited the depletion of the Environmental Stewardship Fund (Growing Greener I) and the Hazardous Sites Cleanup Fund balances as reasons to enact his Growing Greener II initiative. To date, the General Assembly has not acted upon this plan.

Environmental Stewardship Fund

As a result, the Environmental Stewardship Fund (ESF) is not only reducing expenditures, but drawing down what little remains of the fund balance, as well. In the current year, the problem is exacerbated by a one-time $16.5 million transfer from the ESF to the Agricultural Conservation Easement Purchase Fund, which was mandated under Act 233 of 2002.

Environmental Stewardship Fund – Expenditures and Closing Balances

($ Thousands)	**FY 2003-04**	**FY 2004-05**	**FY 2005-06**
Expenditures	$108,572	$95,898	$92,257
Closing Balance	$5,427	$1,447	-$0-

The Department of Environmental Protection’s hands are further constrained by the fact that the Ridge and Schweiker Administrations committed Growing Greener funds well beyond the expiration of their terms in office. Furthermore, as the Growing Greener program matures, an increasing share of the program’s resources must be spent in order to maintain those projects that have already been completed. As a result, available resources will continue to diminish in the upcoming years.

The Governor’s Growing Greener II proposal included a $5 per ton tipping fee increase, of which 20 percent (about $21 million annually) would have been dedicated to the Environmental Stewardship Fund. Those additional resources would have generated more than enough to offset an ongoing transfer to the Agricultural Conservation Easement Purchase Fund. Without those new revenues, such transfers would severely impair the DCNR, DEP, and PennVEST components of the Growing Greener program, should the General Assembly choose to extend the annual ACEP transfers.

Hazardous Sites Cleanup Fund

The Governor’s Growing Greener II proposal also called for additional revenues for the Hazardous Sites Cleanup Fund (HSCF). A new fee of $0.15 per pound on those materials reported under the EPA’s Toxic Release Inventory would have generated an estimated $20.4 million annually for HSCF. The plan also called for transfers from the General Fund to HSCF in FY 2004-05 and the three successive years, to be paid for through a portion of the $4 per ton of the tipping fee increase that was not to be dedicated to ESF. Since this plan was not adopted, the HSCF now faces an anticipated FY 2004-05 year-end deficit of approximately $14 million. Without a significant new revenue source, expenditures from this fund would drop from $61.8 million in FY 2003-04 to approximately $10 million per year in FY 2006-07 and beyond.

The administration notes that the failure to identify a new revenue source for this fund would eliminate DEP’s ability to cleanup 25 hazardous waste sites (at a total cost of

$22 million) per year, while also severely hampering the Commonwealth's land recycling and brownsfield remediation efforts.

What the administration fails to mention is Section 602.3 of the Tax Reform Code, which states that in presenting his proposed budget for the upcoming year, if the Governor expects the current year's closing balance for the Hazardous Sites Cleanup Fund to fall below $5 million, then he "shall authorize" the Budget Secretary to transfer an amount equivalent to 0.25 mills of the Capital Stock and Franchise Tax from the General Fund to HSCF in the upcoming fiscal year.

In English, if the administration anticipates that the FY 2004-05 closing balance for HSCF will fall below $5 million (which appears to be a foregone conclusion), then it appears that they will be forced to transfer approximately $35 million from the General Fund to HSCF in FY 2005-06. Although this trigger will not affect HSCF's current year fund balance, it may help the program limp along until the Capital Stock and Franchise Tax is phased out at the end of 2010. This is especially true if the trigger is activated each year between now and then.

Recycling Fund

The Recycling Fund is the last of the three funds for which the Growing Greener II proposal sought to raise revenue. That it is in the least precarious condition of these three funds is evidenced by the fact that the mid-year briefing fails to mention it.

The Growing Greener II proposal called for a $25 million annual transfer from the General Fund to the Recycling Fund, which would have been paid for through the undedicated share of the tipping fee increase. When added to preexisting dedicated revenues for this fund, this would allow for nearly $74 million in annual Recycling Fund expenditures.

Without the tipping fee increase (and the associated General Fund transfer), the Recycling Fund only has $49 million per year to work with in the foreseeable future. Although this appears to be substantially less than the fund expended in FY 2002-03 ($78.8 million) and FY 2003-04 ($88.5 million), one must bear in mind that those figures include transfers to the Environmental Stewardship Fund of $25 million and $15 million, respectively. Once those transfers are backed out, the Recycling Fund's structural fund deficit appears in a far less apocalyptic light.

Insurance: The current enrollment in the CHIP program is 133,712. Over the last six months, it has ranged from 133,550 to 134,426. The problem is in the Adult Basic Insurance Program, where enrollment is 37,793, down from 41,237 in June. The program has a waiting list of 92,140. Adult Basic is funded exclusively from the Tobacco Settlement Fund whose revenues decline each year.

Adult Basic

County	Waiting List
Allegheny	8,629
Beaver	1,370
Berks	2,096
Cambria	1,595
Lackawanna	1,193
Luzerne	2,177
Montgomery	2,001
Philadelphia	13,848
Washington	1,683

Mass Transit: The mid-year review indicates that between 1991 and 2003, transit support allocated through the Mass Transportation Assistance line item increased by only 20 percent, or barely half the rate of inflation as measured by the CPI-U. The administration blames slow growth in the Mass Transportation Assistance line item for this gap, along with the sub-par performance of the Public Transportation Assistance Fund (or more particularly, PURTA).

The review notes that if the MTA appropriation had increased at the rate of inflation since 1991, then it would be nearly $42 million higher this year than the almost $288 million that was ultimately provided. The contrast between the growth rate of the MTA appropriation and overall General Fund expenditures is much starker, however. While the line item grew by approximately 23 percent between FY 1990-91 and the current fiscal year, General Fund expenditures during the same period increased by an astounding 80 percent.

Touted in 1991 as a $200 million per year package for mass transit, the Public Transportation Assistance Fund has yet to reach that goal. The worst-performing component of PTAF had been PURTA, which was completely undermined as a revenue source by the electric deregulation statute. Although PURTA slipped into a tailspin after deregulation was enacted in 1996, it was only in December 2003 that the hemorrhaging stopped, when Act 46 allowed PTAF to exchange its deteriorating PURTA revenues for an equivalent amount of dedicated sales tax receipts. While Act 46 will prevent any further damage, no action has been taken to compensate transit entities for the revenues they lost as a result of the poor performance of the various PTAF revenue components through the years, or to cover their losses due to electric deregulation.

At present, the Commonwealth's mass transit entities are facing a combined current year operating deficit of approximately $100 million. This includes $62 million for SEPTA and $30 million for the Port Authority of Allegheny County. The mid-year review makes no mention of these deficits.

The review does, however, refer to the increase in the Oil Company Franchise Tax that will take effect in January 2005 (although it does not place a specific value upon this increase). According to PennDOT, this would raise an additional $55 million for highway capital and bridge projects in the second half of the 2004-05 fiscal year. It has been proposed that an equivalent amount of federal funds could be diverted from highway capital and bridge projects to mass transit, in order to help address their deficits. The unanticipated OCFT revenues could then be used in order to plug the hole that this would create. The legality of such action is currently being investigated by the administration.

The administration has also asked the PennDOT district executives to submit a list of $35 million worth of projects that could be cut from the Transportation Improvement Plan in the remaining months of the current fiscal year in order to cover the costs of additional transfers to mass transit. Such cuts would require the approval of the affected Metropolitan Planning Organizations.

It appears at present that the flexing of these federal funds could only take place within individual MPOs, and that any funds flexed for transit would have to be dedicated to capital projects. This being the case, SEPTA could only receive money that is currently slated for the Delaware Valley Regional Planning Commission. According to a PennDOT projection, this means that only $14.5 million would be available for SEPTA through the OCFT windfall in what remains of the 2004-05 fiscal year, plus another $9.2 million that SEPTA could receive if the statewide cut list of $35 million in TIP projects is adopted. Together, this would only address about 38 percent of SEPTA's $62 million deficit. With half of the 2004-05 fiscal year now on the books, and given the substantial operating deficits that the Commonwealth's mass transit entities are facing, the outlook for the next six months is exceedingly grim.

Motor License Fund: The Motor License Fund is revenue collected from a number of taxes such as the: Liquid Fuels and Fuel Tax, Motor Carrier Road Tax, Oil Company Franchise Tax. Some of these taxes are restricted, meaning that they are dedicated to certain types of transportation projects which are many times local projects, such as local county bridges. However some are categorical state projects. Other revenue from the Motor License Fund is unrestricted funds which can be used for many state highway and bridge projects. All of the Motor License Funds are based upon formulae.

The Governor in his 2004-2005 budget projected there will be $2.051 billion in revenues for the entire Motor License Fund. The Governor in his mid-year budget brief indicated that through November, the Fund is $13.5 million above estimate or 1.53%. Generally, Motor License revenues have been relatively flat since 1998-1999. Flat revenues may jeopardize future highway and bridge construction and maintenance projects.

The Oil Company Franchise Tax uses a formula based upon the price of the wholesale gallon of gas; which was 91.9 cents per gallon. However, recently the price of the wholesale gallon of gas went from 91.9 cents to $1.17 per gallon. The Department of Transportation along with the Department of Revenue estimates that this change will increase unrestricted and restricted revenues of the Oil Company Franchise Tax, (OCFT) by $281 million for the last six months in the 2004-2005 and first six months in the 2005-2006. The breakdown in funds are as follows: $85 million – used for unrestricted purposes (highways, bridges); the remaining amounts are for restricted purposes: highway maintenance $97 million, bridges $32 million, municipal government transportation projects $31 million, capital projects $16 million, turnpike $13 million, Highway Transfer program $5, Forestry Bridges $2 million.

PEMA: Disaster Assistance: The September tropical storms of Frances, Ivan and Jeanne created $264 million in damages. The disaster recovery grants and disaster loans totaled at this point $96.5 million. More than 35,499 Pennsylvanians have registered for assistance. Individual and Household grants have totaled approximately $71.7 million. The Small Business Administration has approved over $24.8 million in loans for small businesses.

This Administration has proposed that Pennsylvania provide the full 25% non-federal match required for Federal disaster assistance. The total funding needed to match Federal disaster assistance is $38 million.

Public School Employees Retirement System Employer Contribution Rate: On December 9, 2004, the Public School Employees Retirement Board certified the employer contribution rate for the 2005-06 fiscal year. The 4.69% rate is composed of a .69% rate for health insurance premium assistance and a pension rate of 4%. Next year's rate is higher than the 4.23% rate of the current year but slightly less than the rate that had been forecasted for next year: 4.82%.

However, the contribution rate is being held down artificially by Act 40 of 2003 which provided for a ten year amortization of then-accrued gains and a 30 year amortization of then-accrued losses. The impact of that legislation begins to lessen in 2006-07.

Past and Future Employer Contribution Rates

2004-05: 4.23%
2005-06: 4.69%
2006-07: 6.38%
2007-08: 7.49%

Based on a state-wide payroll of approximately $11 billion, and an approximate 55%-45% split in state-school district responsibility, the increased rate will cost the General Fund approximately $28 million in 2005-06 and an additional $104 million in 2006-07.

Public Welfare: According to the Governor, Public Welfare supplemental appropriations will approximate $126 million. Nearly all of that amount will be in medical assistance.

The Department of Public Welfare will be facing three critical issues this year and in next year's budget: Medical Assistance, Child Welfare and TANF. To some extent they are interrelated.

Over the last year the number of unduplicated persons per month eligible for medical assistance has increased by approximately 120,000 persons. At the same time, the cost of health care inflation affects the medical assistance program in a manner similar to its impact on the general economy.

Next fiscal year, the medical assistance program will lose the benefit of the federal fiscal relief provided in 2003-04 and 2004-05 amounting to approximately $375 million. In addition IGT funding which has been the mainstay of medical assistance program for the last 15 years will be reduced by at least $100 million.

Furthermore, as of this date, neither the nursing home provider assessment nor the managed care provider assessment has been approved by the federal government. While, it is clear that a nursing home provider assessment plan is approvable, the department is attempting to minimize the number of facilities who will become losers under the scheme.

While the medical assistance caseload and costs are up and federal revenues are down, MA is being asked to support the fiscally strapped Child Welfare program. Child Welfare suffers from a current fiscal year problem of miscalculating its ability to earn current and retroactive federal IV-E foster care funds. The department hired Maximus which project earnings based on unrealistic assumptions and bad calculations. It had the effect of greatly reducing the state Act 148 funding to the counties. The department now acknowledges the error and has recomputed each county's entitlement. It is working strenuously to shift some behavioral medical costs from state and county expenditures to medical assistance where they really belonged. Without the shift of expenditures the Child Welfare deficit would be in excess of $40 million. The department expects to reduce that amount to approximately $20 million. Since those funds will not be necessary until the 1st quarter of next fiscal year, funding can be delayed until the 2005-06 fiscal year.

The Child Welfare problem for next year will be due to the reduction in available TANF funding. The federal block grant is a stable $760 million per year. In the years immediately after its enactment in 1996 the Commonwealth spent less than the grant, creating substantial reserves. Beginning in 2001-02, expenditures exceeded the grant as the block grant funds were legally used to support child care and child welfare programs. The consequence of these expenditures is that at the end of the current fiscal year, the reserve will have nearly disappeared.

In 2004-05, expenditures exceeded the current grant level by more than $200 million. Of that amount, $162 million was transferred to the federal Child Care Development Fund block grant to support day care programs and $300 million was allocated to support the County Child Welfare program. Child Welfare costs will rise, not fall. To the extent that TANF funding is removed from Child Welfare, it will have to be replaced by state and county funding, with approximately 75% coming from the state. If the TANF funding is taken from the Day Care appropriation, either the amount of daycare will be reduced or it will be funded totally with state funds.

The TANF problem is further exacerbated by an increase in TANF caseload. From 2001 to 2003, the number of non-employed single parents in Pennsylvania rose from 98,000 to 140,000. This is similar to a trend throughout the country. The number of persons receiving TANF has increased over the past year from 202,417 to 228,548, an increase of 12.9%.

Strategic Sourcing Initiative: Governor Rendell promised to save $100 million this year through his Strategic Sourcing Initiative, which seeks to bring private sector procurement practices to state government. To date, 13 contracts have been awarded under this program, yielding an annual estimated savings of $118.7 million.

For example, DGS awarded an IT staff augmentation contract to Computer Aid of Allentown, which will not only save taxpayers $19.8 million, but also includes a broad network of over 50 subcontractors. Furthermore, the contract has a minority and women-owned business participation level of 49.5 percent.

Another example would be the Commonwealth’s new contract with W.S. Lee and Sons of Altoona, who will supply food to state correctional institutions, state hospitals, and other state agencies at a taxpayer savings of $13.8 million. The firm expects to create about 100 new jobs in Pennsylvania as a result of this deal.