League of Women Voters of Oklahoma
Fiscal Policy Restudy

Oklahoma State Spending and the Budget Process

In December 2015, the ***Office of Management and Enterprise Services*** (OMES) declared a ***revenue failure*** for FY 2016. In February 2016, a second revenue failure was declared. Although the first revenue failure resulted in across-the-board cuts of 3% to state agencies and the second resulted in 7% cuts, the fact that the cuts came so late in the fiscal year, meant that state agencies were actually left with 18% fewer dollars to work with through the end of June 2016. [1]

What is revenue failure and what causes this serious problem? In order to answer these questions, the process of developing the state budget must be unraveled. This section of the study will describe how the Oklahoma state budget is developed each year and what the expenditures are.

How the Budget is Determined:

The budget for the state of Oklahoma is prepared by the Governor, then submitted to the Legislature for consideration, returned to the governor for approval, veto or line-item veto, and finally enacted. Many groups and individuals contribute to the final document at various stages each year. The budget is prepared for one fiscal year from July 1-June 30.

The Oklahoma Tax Commission (OTC) and OMES collect and report data to help the governor prepare the Executive Budget. Before the governor can prepare the Executive Budget, the OMES solicits budget requests from all state agencies. OMES also collects the revenue forecast data from all agencies that collect revenue. OMES presents this information to the ***Board of Equalization*** (BOE) which is the group that must certify the amount of revenue available each year for ***appropriation***. The constitution mandates that the budget be balanced, so a vital piece of information is an accurate estimate of the revenue that will be collected each year. The state constitution specifies how this independent ***revenue estimate*** will be established. This revenue forecast is not a multi-year forecast. In-house and outside economists, analysts, and research firms evaluate and prepare the data used in the forecast. Resources at Oklahoma State University are involved in the process.

The BOE will certify an amount of revenue available that is 95% of the total revenue collection that is forecast for the year in order to ensure a balanced budget. The BOE certifies the amount based on information available in December. This is the figure the governor uses to prepare the Executive Budget. The BOE re-certifies the amount of revenue in February after the Governor presents the Executive Budget to the Legislature. The February figure reflects actual collections and updated forecasts. The Legislature and Governor work together towards enacting a budget that does not exceed the February certified revenue figure. The BOE will re-certify this amount again in June to reflect any changes in law. Sen. Clark Jolley called the

Red numbers indicate citations to be found in the endnotes after each section of this paper.

Words or phrases in ***bold italics*** are defined in the glossary

Executive Budget “irrelevant” because it is not based on the most accurate estimate of revenue from the BOE which comes three weeks after the Governor presents the Executive Budget.[2] Jolley proposed that a possible solution to this problem is unifying the certification dates used for both the Legislative and Executive Budget.

Some important factors that can affect the accuracy of the forecast are off-the-top funds and volatility in sources of revenue. A report prepared by the OTC in 2014, Report to the State Board of Equalization on Revenue Forecasting [3] includes an example of how off-the-top funds can affect the accuracy of the revenue forecast. Dedicated funds are not appropriated by the Legislature from the General Revenue Fund (GRF). Problems occur when these dedicated funds are subtracted from the total revenue collection leaving the GRF, which is then apportioned by the Governor and Legislature. Agencies that receive funding from the GRF are the only ones affected by mandated spending cuts when revenue falls short of the forecast. In addition, there will always be some revenue volatility related to the changing price of our oil and natural gas resources because Oklahoma is an energy producing state. Other states have to work with these fluctuations as well.

When revenues have not met the forecast in the past, the shortfalls have been addressed in part with non-recurring revenue sources like the ***rainy-day fund*** and federal stimulus funds such as the ***American Recovery and Reinvestment Act*** of 2009 (ARRA) which ended in 2013. Continuing to build budgets based on previous agency funding levels that have been dependent on these non-recurring sources also leads to unrealistic estimates of funding needs.

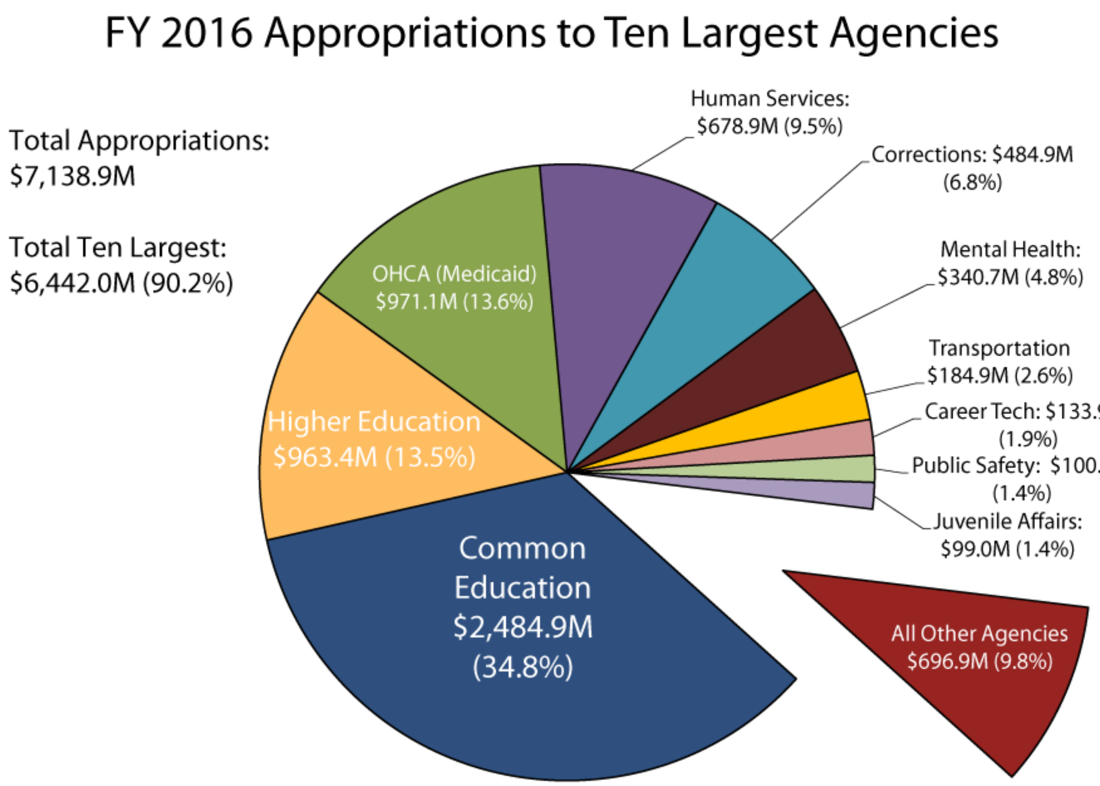
Where Does the Revenue Go?

State revenue is spent by legislative appropriation from the GRF, by tax expenditures, and by dedicated revenue sources.

For example, the budget enacted for FY2016 appropriated more than $7 billion from the GRF. Most of the funds, 90.2%, were directed to these top ten agencies:

Common Education	34.8%
Higher Education	13.5%
Medicaid	13.6%
Human Services	9.5%
Corrections	6.8%
Mental Health	4.8%
Transportation	2.6%
Career Tech	1.9%
Public Safety	1.4%
Juvenile Affairs	1.4%
Other	9.8%

Figure 1 below illustrates appropriations to the ten largest agencies in Oklahoma. [4]



Tax expenditures, a collective term for tax credits, incentives, exemptions, subsidies, and deduction, are another kind of expense. “There are more than 400 tax credits, deductions, and exemptions on the books in Oklahoma, with costs ranging from zero to hundreds of millions of dollars every year. Some of these benefit large swaths of the state — such as the personal exemption that all Oklahoma households can claim on their tax return. Others subsidize very specific activities or industries.” [5] The Tax Expenditure Report for 2013-14, for example, reported on fifty four ***tax credits***, thirty four ***exemptions*** and ***deductions,*** eighteen tax exempt entities, four miscellaneous income tax expenditures and twenty seven exemptions on interest and other income earned on certain bonds, notes, and obligations. The report stated that this was only an incomplete list of tax expenditures for that year. [6] There can be good reasons for these tax expenditures, but they divert funds from the total revenue collected by the state. They are not appropriated like incoming funds, and they seem to be an almost invisible state expenditure. Many continue indefinitely without any planned review or cap. Whether they accomplish their objectives is not often evaluated.

Figure 2 below shows 15 of the major tax expenditures in Oklahoma

Name	Annual Cost	Type
Investment/New Jobs Tax Credit	$94,792,000	Income tax credit
Quality Jobs Program	$83,241,878	Tax refund or rebate
Insurance Premium Tax	$39,007,824	Insurance company credits
Five Year Ad Valorem Tax Exemption	$35,422,118	Reimbursement to local governments
Electricity Generated by Zero Emission Facilities	$18,181,000	Income tax credit
Economic Development Pooled Finance	$12,567,178	Other
Clean Burning Fuel Vehicle Credit	$10,674,000	Income tax credit
Oklahoma Film Enhancement Rebate Act	$8,909,205	Tax refund or rebate
Quality Jobs Leverage Program	$7,102,141	Other
Farm Vehicle Registration Benefits	$3,978,000	Other
Historic Rehabilitation Tax Credit	$3,869,000	Income tax credit
Energy Efficient Residential Construction	$3,714,000	Income tax credit
Aerospace Engineer Tax Credit	$2,497,000	Income tax credit
Aircraft Repairs and Modifications	$2,425,000	Sales tax exemption
Training for Industry Program	$2,195,180	Other
Total	**$334,575,524**	

Note: Annual cost figures above are based on the most recent available data from fiscal year 2014 or fiscal year 2015.[7].

The fifteen largest business incentives (shown in Figure 2 above) are among those slated for review by a new state commission. This commission, the Incentive Evaluation Commission, was established by a new law, HB2182. The IEC is an 8-member group that is supposed to provide information to the legislature. Speaker of the House, Jeff Hickman, reported that HB2182 is "a law requiring all tax credits to be reviewed every four years, starting with the costliest ones this year, to determine whether the benefit to the state is greater than the cost." [8] In 2016, the commission is planning to review at least 17 incentives and make recommendations to the legislature about which should be reconsidered. The effect of any action by the legislature based on the work of this commission won't be felt until 2017. Nevertheless, this legislation, which was proposed by Rep. David Dank, is one step towards tackling Oklahoma's chronic budget difficulties.

Finally, other expenditures are off-the-top funds, or dedicated revenue sources. These expenditures have been established over time by more than 15 legislative statutes. [9] Speaker Hickman asserted that "more than $3 billion is automatically taken out of the pot of revenue due to earmarks for 'off-the-top' funding passed by previous Legislatures. That 'off-the-top' amount grows annually leaving lawmakers with less money each year to appropriate – even as revenues have reached record levels in recent years. Just eight years ago, 55% of revenue went to the General Revenue Fund for the Legislature to appropriate. Today, just 45% of state revenue makes it to the Legislature for use in the annual budget." [10] Some of the large off-the-top funds are the Education Reform Fund (HB1017), Education Technology, ***Oklahoma Higher Learning Access Program* (*OHLAP*), *Rebuilding Oklahoma Access and Driver Safety* (*ROADS*)**, ***County Improvement for Roads and Bridges* (*CIRB*)**, retirement funds, and the Tobacco Settlement Fund. State Treasurer Ken Miller stated that eliminating off-the-top funds is not a "silver bullet" because "close to 90%" of these off-the-top funds would have to be spent anyway. [11].

ENDNOTES ON OKLAHOMA STATE SPENDING AND THE BUDGET PROCESS

1. http://www.koco.com/news/oklahoma-officials-order-235-million-cut-to-state-agencies-after-2nd-revenue-failure/38320388
2. Panel discussion at the Jan. 28, 2016 Oklahoma Policy Institute Budget Summit.
3. http://lwvok.org/files/OTC_Revenue_Forecast_Commission_Review_2014.pdf
4. http://okpolicy.org/issues/responsible-budget-taxes graph reprinted with permission
5. http://www.okacademy.org/PDFs/2015Research.pdf
6. https://www.ok.gov/tax/documents/Tax%20Expenditure%20Report%202013-2014.pdf
7. Oklahoma Tax Commission, Oklahoma Insurance Department, Oklahoma Watch research. http://oklahomawatch.org/2015/11/10/up-for-scrutiny-335m-a-year-in-business-incentives/
8. https://www.ok.gov/treasurer/documents/OER_12-31-15.pdf p. 2.
9. https://www.ok.gov/tax/Forms_&_Publications/Reports_&_Statistics/Apportionment_Charts_&_Formulas/index.html
10. https://www.ok.gov/treasurer/documents/OER_12-31-15.pdf p. 2.
11. Meeting with LWVOK Fiscal Policy Restudy Committee 1/27/2016.