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Oklahoma Economic Report™

News and analysis of Oklahoma's economy

A publication of the Office of the State Treasurer • Treasurer Ken Miller, Ph.D.

Raiders of the Lost Assets

Private property has become an important source of revenue for many states, perhaps too important. Unclaimed property laws, which exist in every state, are considered among the first consumer protection programs in the nation. They were established to protect abandoned or forgotten funds or property on behalf of the consumer instead of letting the funds revert back to the business or company.

The most common types of unclaimed property are accounts with financial institutions or companies that have no activity or contact with an owner for one or more years. The state is considered a safe-keeper of the value of the property, and there is no expiration date for the funds to be claimed by the owner or heirs. However, states receive far more property or funds than what is returned to owners, a fact that has not gone unnoticed by cash-poor states.

> *"Some states seem more interested in using the assets than in locating property owners."*

A majority of states direct proceeds from receipt of unclaimed property to the state's general fund, less a predetermined amount set aside to pay claims. The amount, which is typically based on the state's experience in paying actual claims, usually represents a fraction of what is actually held by the state on behalf of owners. Some of these states require additional funds to be appropriated in the event the amount set aside is insufficient to pay claims.

Several of the states siphon off funds in excess of actual claims to dedicated

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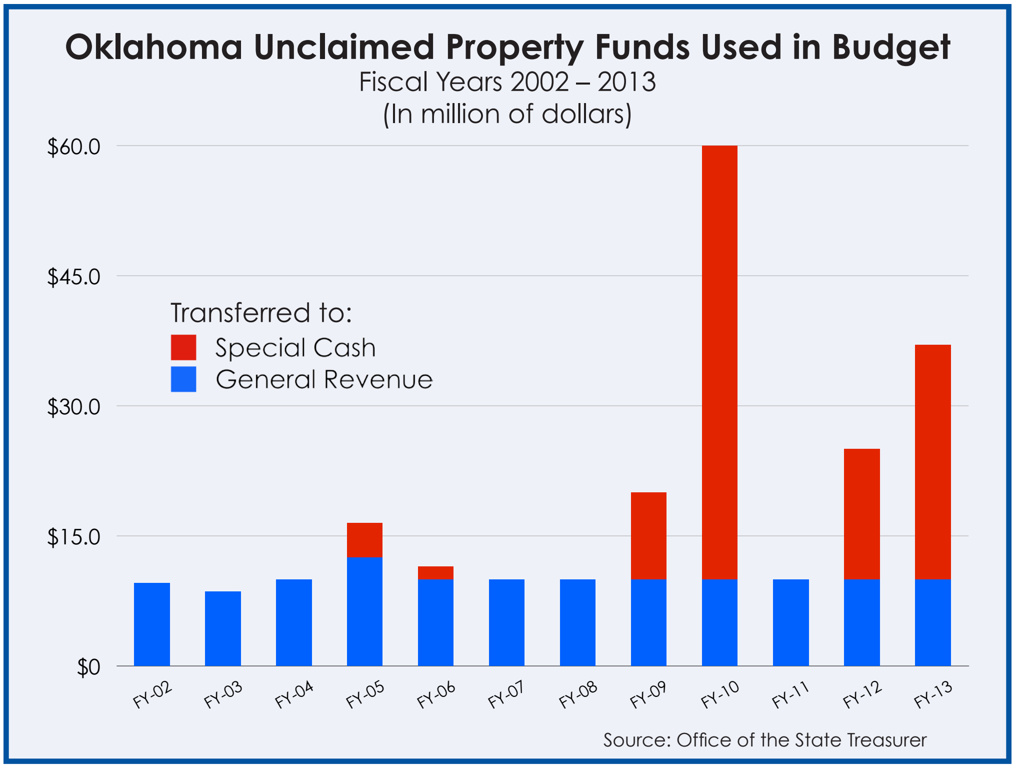

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Treasurer's Commentary

By Ken Miller, Ph.D.

Stop the madness

It is said the definition of insanity is doing the same thing over and over again and expecting different results.

In the context of the state budgeting process, it could be said the definition of insanity is continuing to plug budget holes with hundreds of millions of dollars in non-recurring revenues while at the same time working to eliminate the recurring ones.

The dash for cash typically occurs twice during the legislative session.

It happens at the start of session to fund supplementals for agencies that didn't receive sufficient funding for a full year. The Department of Corrections is a perennial recipient. And it happens again at the end of session when budget writers scramble to pull together enough resources to fund the General Appropriations bill.

Such suboptimal resource planning is understandable during times of extreme fiscal distress. Most would not fault the use of reserve funds or creative finance during the three budget cycles that spanned the Great Recession.

But such tactics should be rare, not business as usual.

> ***"Oklahoma has become dependent on the use of one-time funds in both good times and bad."***

State government funding in Oklahoma has become dependent on the use of one-time funds in both good times and bad. Revenue growth in the Sooner State was strong last year, yet legislators spent almost $400 million in non-recurring funds to increase the budget bill by five percent over the prior year.

Nearly $298 million in one-time money was employed in the FY'13 budget from such sources as the insurance premium assistance fund, various revolving funds and the unclaimed property fund, which has become such a favorite grab bag that budget writers often forget to seek the statutorily required authorization.

Last session, about $93 million originally destined for the Rainy Day Fund was intercepted by legislators to fund supplementals for education and public safety. In the previous session, $21.4 million was diverted in the same manner.

Even though the money was earmarked for legitimate needs, the ends did not justify the means.

In both diversions, simple changes to codified tax law allowed the Legislature to reapportion current year collections after the Equalization Board approved the final estimate.

The action effectually allowed the Legislature to spend more money than authorized.

Such action violates at least the spirit of the constitutional balanced budget provision and establishes a dangerous precedent which allows the Legislature to circumvent Rainy Day Fund laws at will.

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Commentary

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Now that state revenues have returned to pre-recession levels, it is time to inject common sense into our revenue structure.

Only when one-time revenues are reserved for one-time expenditures can eliminating recurring revenue sources be responsibly accomplished.

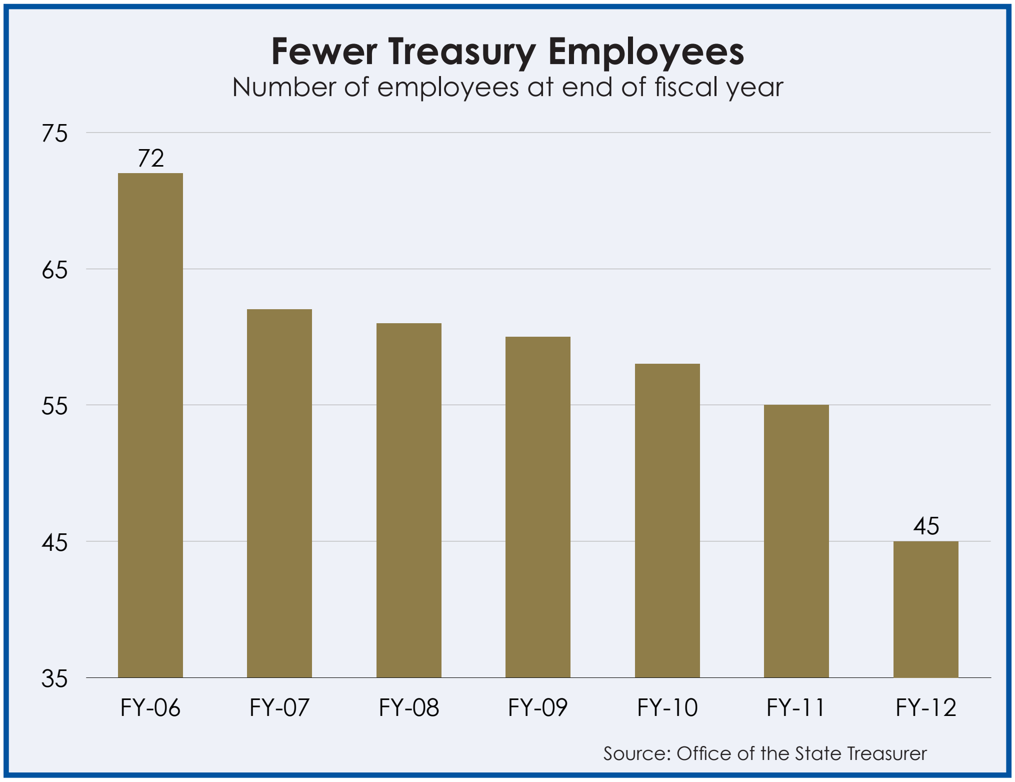
To get better budgeting results, policymakers must continually learn from past mistakes.

Oklahoma would certainly benefit from comprehensive tax reform that lowers rates by broadening the base and better prioritizing the spend. But until the annual mad dash for cash comes to an end, the quest for fiscal sanity will remain elusive.

Miller slashes own budget

One of Ronald Reagan's more famous quotes was delivered in a speech in 1964, when he said, "No government ever voluntarily reduced itself in size."

While that might be true of most government agencies, such is not the case with the Oklahoma State Treasurer's Office.



Cutting the budget

When the Great Recession hit Oklahoma and state revenue collections plummeted, appropriations to the treasurer's office were cut by 17 percent. Now that the economy is growing and more money is flowing into state coffers, many agencies are seeking to expand to make up what was lost. Not so in the treasurer's office.

Treasurer Ken Miller has asked the Legislature to cut appropriations to the treasurer's office by an additional five percent next fiscal year. That means a further reduction of $190,000 of taxpayer money to fund the office.

A few years ago, the State Treasurer's Office had 72 employees working at three different locations around Oklahoma City.

Soon, the staff will be 40 percent smaller and every treasury employee will be working in one location – along the northeast corridor of the State Capitol's second floor.

Those employees will still oversee banking and treasury services for some $23 billion deposited each year, the daily investment of more than $6 billion, and the return of unclaimed property to Oklahomans.

It just won't cost the taxpayers near as much money to make it all happen.

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Slashing
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Redefining business as usual

In the treasurer's office, business as usual has come to mean finding ways to do more with less.

The first phase of consolidation of the treasurer's office increased usable square footage in the State Capitol Building by 32 percent.

The second and final phase of consolidation will allow 15 employees now working in Shepherd Mall to move to 23rd and Lincoln. It will eliminate the need for leased office space and will result in total annual savings of $64,000.

It will also create a more cohesive and synergistic work environment by uniting for the first time all treasury employees in one workplace.

Thanks to savings garnered through numerous efficiency projects, the treasurer's office is in the final steps of implementing a $2 million replacement of obsolete financial software – all done without any additional appropriations.

To a large degree, efficiencies have been accomplished through enhanced technology, which has streamlined banking functions. Personnel efficiencies have been realized through outsourcing general functions, such as information services and accounts payable, and from reductions in force with remaining employees assuming additional responsibilities.

What Ronald Reagan thought to be impossible 48 years ago is now happening at the Oklahoma State Treasurer's Office as it voluntarily reduces its size.

First quarter General Revenue allocations top estimate

Allocations to the state's General Revenue Fund (GRF) exceeded the estimate by less than two percent in the first quarter of Fiscal Year 2013, according to the Office of Management and Enterprise Services.

Collections funneled to the GRF during the first three months of the fiscal year total $1.317 billion, topping the estimate by $22.3 million or 1.7 percent.

Most of the excess came from corporate allocations, which total $94.4 million. That is $42.6 million or 82.3 percent above the estimate.

Personal income tax allocations to the GRF total $504.3 million for the quarter, topping the estimate by $30 million or 6.3 percent.

Sales tax allocations for the first quarter are $486.8 million, above the estimate by $19.9 million or 4.3 percent.

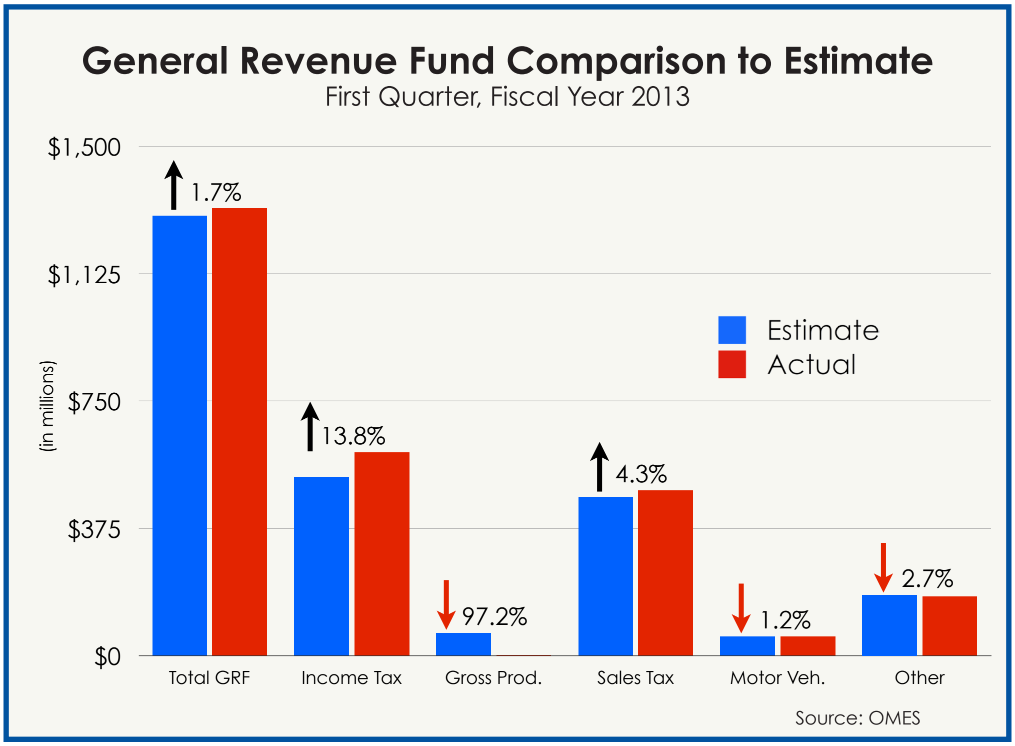
All other revenue sources for the GRF failed to meet the estimate.

The gross production tax on natural gas fell far below the estimate with GRF allocations for the quarter of $1.9 million. With allocations estimated to be $66.7 million, the mark was missed by $64.8 million or 97.2 percent.

First quarter motor vehicle collections to the GRF are $55.7 million, missing the estimate by $0.7 million or 1.2 percent.

Other sources total $174.3 million for the quarter, falling below the estimate by $4.8 million or 2.7 percent.

During the quarter, the GRF received 49.9 percent of gross collections.



Raiders

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accounts, while others commingle unclaimed property funds with taxpayer money.

Oklahoma's status as a strong property-rights state has led to it being one of the few states whose statutes specify that cash holdings of the unclaimed property program are designated for payment of claims and administration of the program and does not direct diversion of the funds elsewhere. Even so, Oklahoma's relatively strong statutory protections have not prevented the funds from being used for other purposes. Over the past 12 years, more than $228 million in unclaimed property funds have been transferred for use in the state budget.

Colorado was once among the states with better protections of its fund. However, the economic downturn that began in 2001 resulted in a 16-percent decline in revenue to the state's general fund over a two-year period. As Colorado found it hard to climb back due to the state's mandatory spending and revenue limitations, statutes were amended to direct large sums of unclaimed property funds to fill budget holes. Statutes were later amended to direct excess funds to the state's health insurance program.

Delaware is often the poster state for aggressiveness in obtaining and using unclaimed property funds. The program is the third-largest source of revenue for the state, after personal income and franchise taxes. Its unclaimed property program is located in the state department of revenue, lending to the appearance that the state views the program more as a revenue generator than a consumer protector.

With unclaimed property becoming an increasingly important part in state budgets, some are looking for ways to collect even more unclaimed property, and more quickly. Several states shortened dormancy periods required before property can be transferred to the state. Others have taken a more aggressive position, seizing property or seeking to categorize additional types of property.

According to The Council on State Taxation (COST), some states have even gone so far as to charge beverage wholesalers for the value of unreturned bottle deposits and require publishers of returned magazine subscriptions to convert the value of the subscription to cash. And states have increased audit activity to ensure businesses and other property holders are complying with reporting requirements.

Property holders in more aggressive states are seeking reform of unclaimed property laws, alleging the intense scrutiny they are receiving regarding compliance is overreach. The holder's perspective, as summarized by COST, is that a significant disconnect exists between efforts to identify new types of property and the premise upon which unclaimed property law is based – that is, "the state stands in the shoes of the lost owner and holds their unclaimed property in trust until the lost owner is found."

A concern is that some states are putting less emphasis on locating property owners than they are in using the assets to replace or enhance state revenues.

Earlier this decade, California was routinely criticized for its lackluster efforts in trying to reunite property with owners; after all, known celebrities were listed among those with property.

Numerous lawsuits were filed by property owners who claimed good faith efforts to inform them were not made and they subsequently lost value or interest earnings from the state's liquidation of their assets. A 2007 lawsuit that led to a federal injunction against the state determined that California had violated its own notification laws.

Soon after, legislation was enacted authorizing California's unclaimed property division to notify owners before the property is sent to the state in an attempt to prompt owners to reclaim the property directly from the business. The department has also ramped up publishing notices in recent years to demonstrate a willingness to return property to its owners. Despite these efforts, in March a Sacramento news outlet reported that actress Lindsay Lohan and reality star Kim Kardashian were included among those with unclaimed property being held by the state.

In contrast, Oklahoma's program has dedicated increasingly more time and resources to notifying the public since its relocation from the state tax commission to the State Treasurer's Office in 2000. In fiscal year 2012, Oklahoma reunited owners with nearly $18.5 million in property. Other property with great sentimental value has been returned intact, such as a baseball autographed by Mickey Mantle, a collectible Rolling Stone magazine, and staff is currently working on returning lost military medals.

Unclaimed property programs, operated as intended, are a true public service. When states become dependent on unclaimed property as a revenue stream, that service risks being compromised.

Gross receipts & General Revenue compared

The Treasurer's October 1 Gross Revenue report and the Office of Management and Enterprise Services' October 9 General Revenue Fund (GRF) report contain key differences.

September gross receipts totaled $988.02 million, while the GRF received $541.9 million or 54.9% of the total.

The percentage of monthly gross revenue going to the GRF varied from 34.9% to 56.4% during the past 12 months.

From September gross receipts, the GRF received:

- **Personal income tax: 73.2%**
- **Corporate income tax: 72.3%**
- **Sales tax: 45.4%**
- **Gross production-Gas: 9.8%**
- **Gross production-Oil: None**
- **Motor vehicle tax: 32.1%**
- **Other sources: 55.7%**

September GRF allocations topped the estimate by $19.3 million or 3.7 percent. In August, collections were below the estimate by $17 million or 4.2 percent.

For the month, insurance premium taxes totaled $37.8 million.

Tribal gaming fees generated $10.6 million during September.

Thanks to strong income tax receipts, September collections resume rise

Revenue collections ticked up in September, pushed by strong income tax remittances, State Treasurer Ken Miller announced as he released the monthly gross receipts to the treasury report.

Total collections were almost three percent higher than in September of last year.

Three of the four major tax categories were positive, with income tax leading the way up almost 16 percent. Sales tax and motor vehicle receipts also showed growth.

> *"Oklahoma's economy continues to climb up the expansion side of the business cycle . . ."*

Collections from the gross production tax on oil and natural gas remained well below prior year totals, down almost 40 percent, but off their low of 54 percent below the prior year in August, indicating we may have turned a corner, Miller said.

"Oklahoma's economy continues to climb up the expansion side of the business cycle in spite of low prices for natural gas," Miller said.

"After two years of sharp growth in revenues, collections have leveled off

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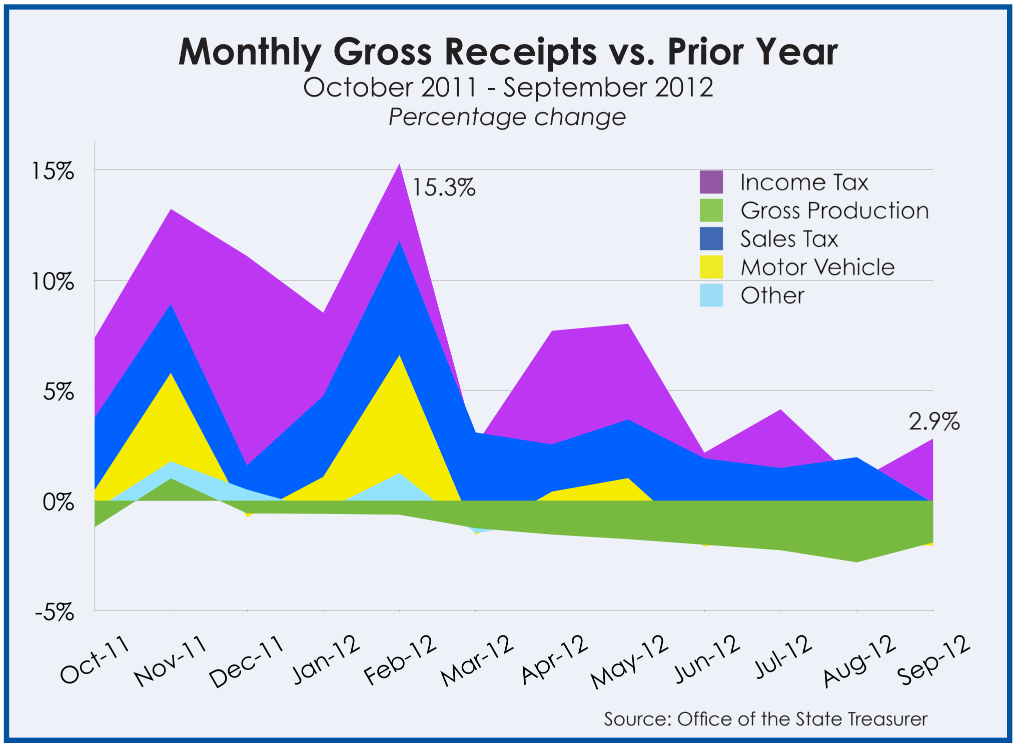

State unemployment rises for third consecutive month, but . . .

Oklahoma's seasonally-adjusted unemployment rate rose to 5.2 percent in September, according to the Oklahoma Employment Security Commission. The reason for the hike is that labor force participation increased by more than employment.

In spite of the rise, 10,920 jobs were added in the state during the month. The number of jobless Oklahomans went up by 2,720 from August.

The U.S. jobless rate fell to 7.8 percent for the month.

State Unemployment

OKLAHOMA	Unemp. rate*	Labor force*	Employment*	Unemployment*
Sep '12	**5.2%**	**1,812,950**	**1,718,770**	**94,180**
Aug '12	5.1%	1,799,250	1,707,850	91,400
Jul '12	4.9%	1,795,720	1,707,300	88,420
Jun '12	4.7%	1,794,260	1,709,300	84,960
May '12	4.8%	1,791,380	1,706,070	85,320
Apr '12	5.0%	1,789,150	1,699,870	89,280
Sep '11	6.3%	1,774,570	1,662,110	112,460

* data adjusted for seasonal factors

Source: OESC

Revenue

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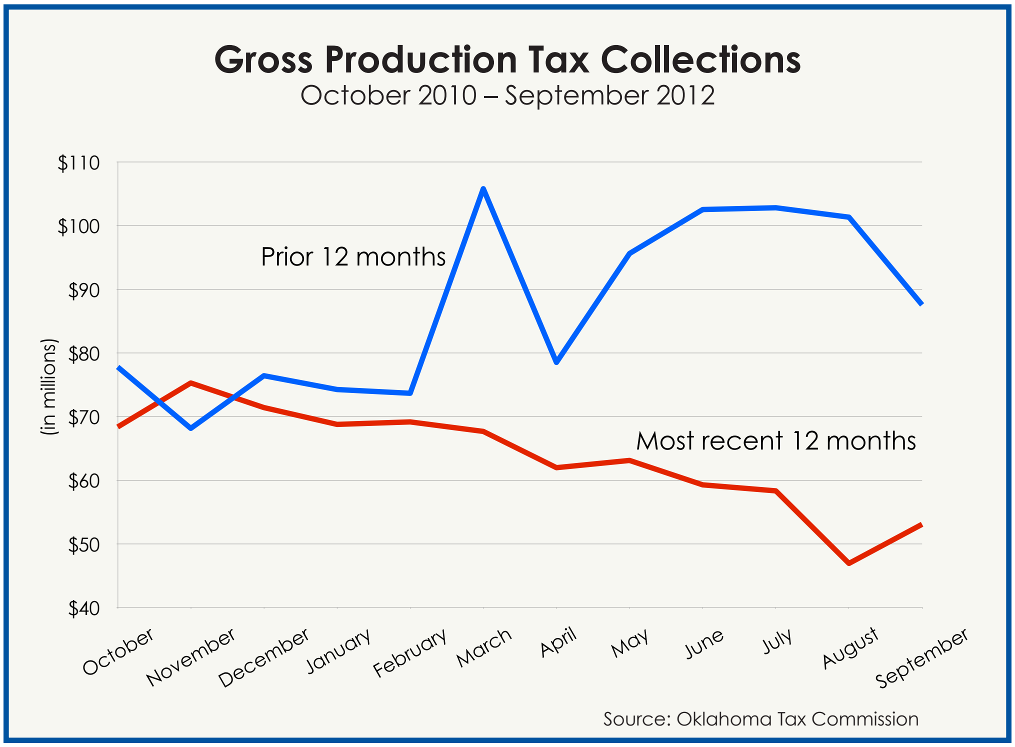
over the past half year as we close in our all time high from December 2008."

The positive turn on gross receipts comes after collections dropped below the prior year during three of the past seven months, including August.

However, oil and natural gas production collections have been consistently lower than the prior year for 10 months.

"Sales tax collections, generally viewed as a measure of consumer confidence, are up almost six percent in September," Miller said.

"This is obviously a good sign, even though sales tax has been growing by double digits for much of the past year."



Other positive indicators

The Business Conditions Index for Oklahoma improved in September. The leading economic indicator rose to 56.6 from 53.6 in August.

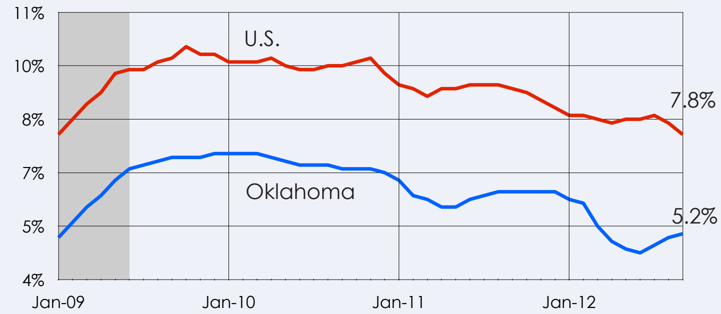
Numbers above 50 mean growth is expected. Over the past several months, surveys have shown solid business gains and an anticipated reduction in the state unemployment rate in the coming months.

The September unemployment rate increased by 0.1 percentage points from August to 5.2 percent, according to the Oklahoma Employment Security Commission.

However, analysts noted that seasonally-adjusted employment expanded by almost 11,000, while the number of jobless rose by less than 3,000.

Economic Indicators

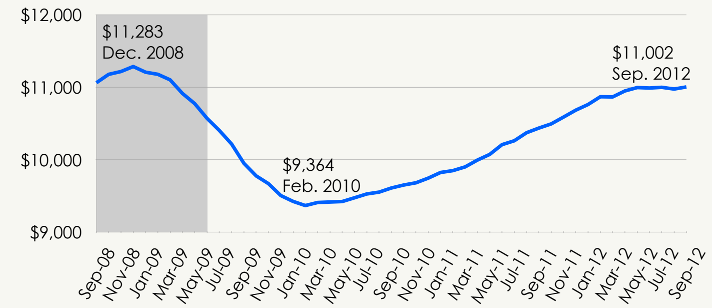
Unemployment Rate
January 2009 – September 2012



Shaded area denotes U.S. recession

Source: Bureau of Labor Statistics

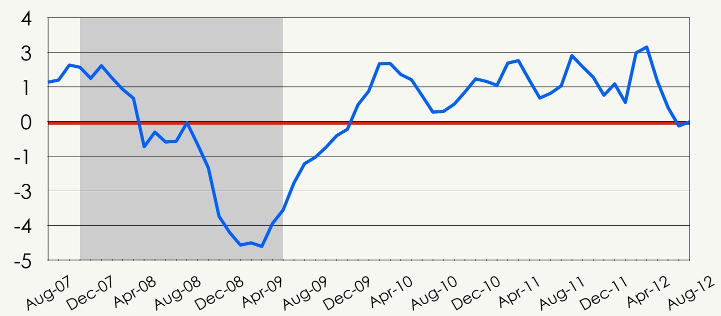
Oklahoma 12-Month Gross Receipts
September 2008 - September 2012
(in millions)



Shaded area denotes U.S. recession

Source: Office of the State Treasurer

Leading Index for Oklahoma

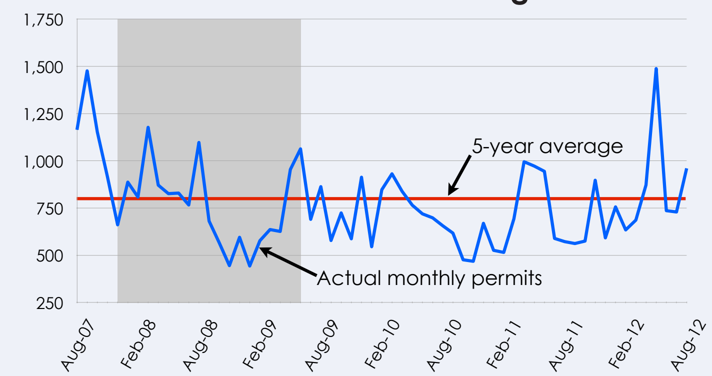


This graph predicts six-month growth by tracking leading indicators of the state economy including initial unemployment claims, interest rate spreads, manufacturing and earnings.

Shaded area denotes U.S. recession

Source: Federal Reserve

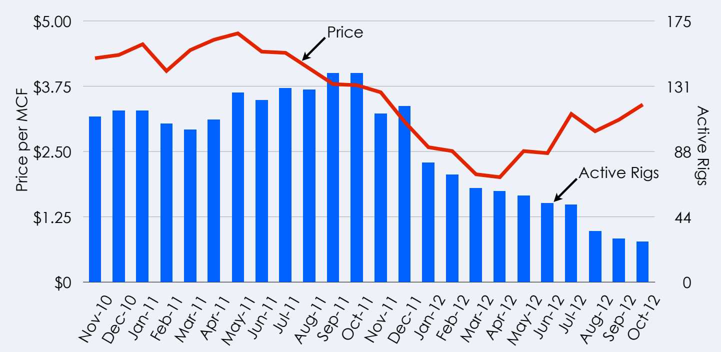
Oklahoma Residential Building Permits



Shaded area denotes U.S. recession

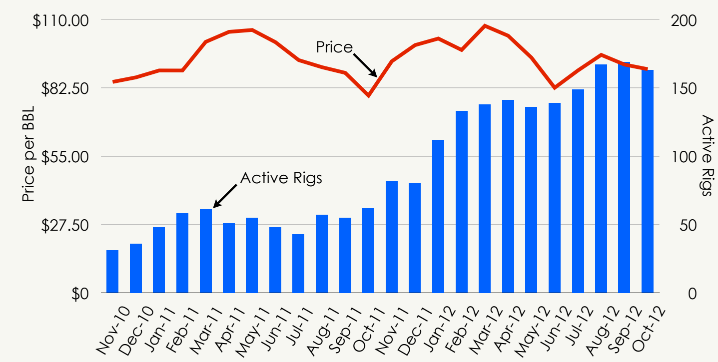
Source: U.S. Census Bureau

Oklahoma Natural Gas Prices & Active Rigs



Source: Baker Hughes & Bloomberg

Oklahoma Oil Prices & Active Rigs



Source: Baker Hughes & Bloomberg