Policy Playbook
for 2016

Headway and Headwinds

13th Annual
Leadership Summit

December 14, 2015

Oregon Business Plan.org

OREGON BUSINESS PLAN FRAMEWORK

Goal

Quality Jobs in Every Corner of Oregon

- 25,000 net new jobs per year through 2020
- Per capita income above the national average by 2020
- Reduction of poverty below 10 percent by 2020

Vision

Clusters of Innovative, Globally Competitive Industries

Traded-sector businesses drive the Oregon economy. They export products and services outside of Oregon, bringing in fresh dollars that re-circulate through payrolls, employee spending in the local economy, purchases from vendors, and tax revenues that fund critical public services like education. Industries that sell globally are both big and small. These industries tend to cluster based on access to shared resources, talent, suppliers, and other factors. The diversity of our traded-sector clusters is illustrated below.

Advanced Manufacturing
- Metals (Primary and Secondary)
- Machinery + Transportation Equip.
- Food Processing
- Defense

High Tech
- Computer and Electronics Equipment
- Software
- Education Technology + Services
- Biotechnology

Natural Resources
- Forestry and Wood Products
- Agriculture Products
- Wine/Winemaking
- Beer/Brewing
- Nursery Products
- Tourism and Hospitality

Aviation
- Heavy Lift Helicopters
- Unmanned Aerial Systems
- General Aviation

Clean Technology
- Green Building and Design
- Energy Efficiency
- Solar Manufacturing
- Wind Energy Development
- Wave Energy Development
- Environmental Technology + Services
- Electric Vehicles + Green Transportation

Footwear, Apparel and Outdoor Gear

Creative Industries

Strategy

4Ps for Prosperity – Conditions Essential to Promote High-Wage Job Growth in Oregon

People: A talented workforce.
Productivity: Quality infrastructure, resource utilization, competitive regulations and business costs.
Place: A high quality of life that attracts and retains talented people.
Pioneering Innovation: A culture of research, commercialization and innovation in product and process design.

Long-Term Policy Agenda to Improve the 4Ps

Public Services Redesign
- Tie state budget to key outcomes.
- Redesign education and workforce delivery.
- Redesign health care delivery.
- Reform public safety.
- Reform public employee compensation.
- Overhaul revenue system.

Jobs Agenda
- Boost innovation and entrepreneurship.
- Expand capital availability.
- Streamline regulation and permitting.
- Ensure industrial land supply and readiness.
- Invest in transportation.
- Secure affordable, reliable energy supply.
- Secure water for agriculture and other uses.
- Increase forest health and timber supplies.

Headway
- More jobs
- More and smarter money for schools
- Rural Oregon Investments

Headwinds
- Damaging, Costly Ballot Measures
- Transportation Gridlock
- Exploding PERS Costs

WELCOME

Fellow Oregonians,

Welcome to the 13th Annual Leadership Summit. Our theme, *Headway and Headwinds*, reflects both our optimism and concerns for the coming year.

On the headway side of things, Oregon carries great momentum into 2016. The past few years we've far exceeded the Business Plan goal in annual job growth, and incomes are starting to climb. It's essential to keep that momentum going so more families can share in the prosperity, especially in our rural communities.

We can do that by boosting international trade, continuing our efforts to support our rural natural resource economy, pressing smarter investments in education, and winning passage of the transportation package that we so desperately need.

With the growing state budget produced by the economic rebound, Oregon can also build on successes in public sector productivity that make it possible to move state dollars to priority needs.

Policies to control health care and corrections costs enabled exactly that in our current biennium, resulting in historically greater investments in early learning, K-12, and higher education. Oregon has the opportunity and imperative now to apply those resources to raise our education outcomes, in particular high school and postsecondary completion rates.

But there are headwinds that could stall or derail our economic and fiscal progress. A damaging and costly $5 billion tax on Oregon sales appears to be heading to the ballot. It would increase prices for almost everything Oregon consumers and business buy, hurting our families and undermining the competitiveness of Oregon businesses.

And our budgets for public services are still vulnerable to inherent flaws in the Public Employees Retirement System. Public employer PERS costs are expected to skyrocket, threatening to reduce services for education, police, fire, and other public needs.

These issues and how to address them are explored in this Leadership Summit and in the main section of this playbook. The playbook also contains deeper issue papers on rural development, education, health care, and public employee compensation and the PERS problem.

Thank you for joining the conversation and for all that you do for Oregon.

Sincerely,

Malia H. Wasson

Malia H. Wasson, Chair
Oregon Business Plan Steering Committee

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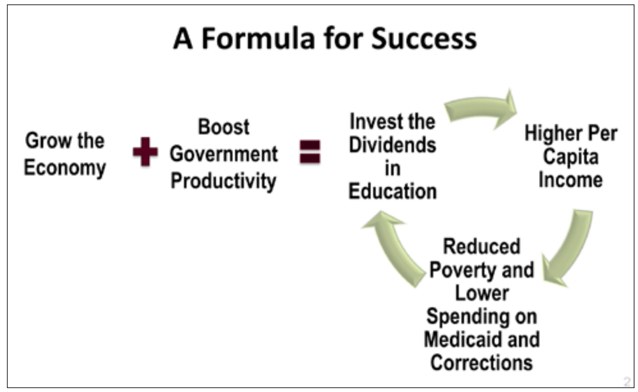
HEADWAY AND HEADWINDS

HEADWAY

Oregon is outperforming the nation as the U.S. economy enters its seventh year of expansion. Job creation has exceeded Business Plan goals, per capita personal income has ticked up relative to the U.S. average, and in-migration is strong.

Fiscal Dividend. Economic growth, in turn, has generated a fiscal dividend. The last two legislative sessions have seen the return of investment budgets, and the money has been well spent. Oregon schools now deliver full-day kindergarten, community college tuition will soon be free for qualified recent high school students, and universities have curbed tuition growth and are investing more in practices that encourage college completion, especially for first generation college students. The Legislature has increased investment in career-technical and STEM education – a critical Business Plan priority – and has set the stage for more. The share of Oregonians without health insurance has fallen to unprecedented lows, and smart reforms have strengthened the safety net and improved incentives to work.

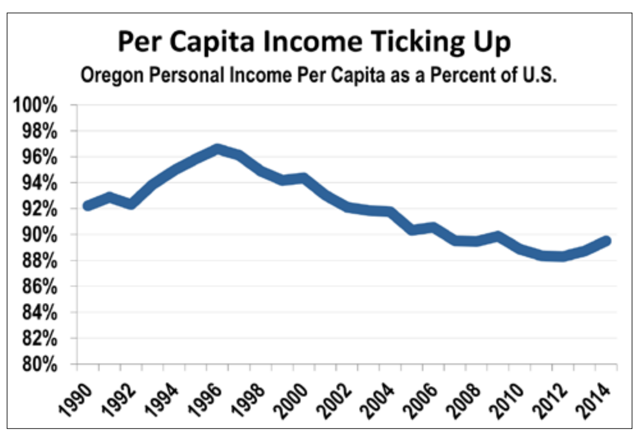


These are remarkable accomplishments given the conditions just five years ago when Oregon and the nation were facing economic challenges unseen since the 1930s. In response, the Business Plan in 2010 proposed a three-part turnaround strategy: 1) grow the economy, 2) boost government productivity, and 3) invest the fiscal dividends in education. (See top figure at right.)

Policy makers responded. And although the turnaround has been slow, difficult, and still unfinished, it has largely worked. In five years, Oregon has transitioned from crisis to opportunity. Oregon's recovery and fiscal stewardship deserve high marks.

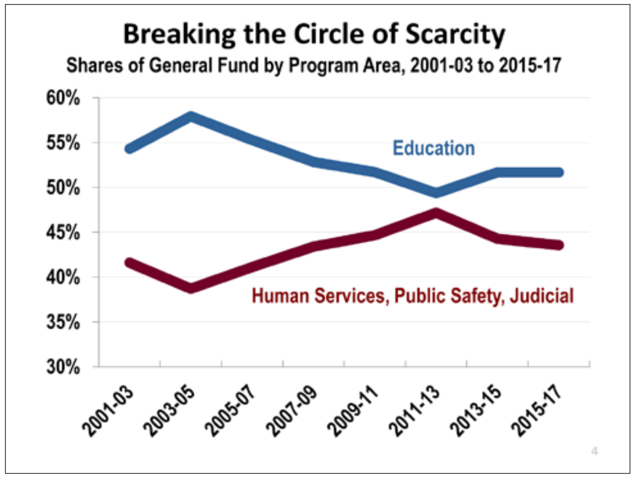
Jobs and the Economy. Statewide, jobs returned to their pre-recession peak late last year, and growth has marched on in 2015. (See middle figure at right.) The state has blown past the Business Plan's goal of adding 25,000 jobs per year.

In addition, the state made some progress on the Plan's goal to raise per capita personal income to the national average. Oregon's PCPI edged up relative to the U.S. average between 2013 and 2014. While we have a long way to go to reach the goal (see adjacent figure), our state economist forecasts Oregon's per capita income to grow at an average of 5 percent annually through the remainder of the decade, compared to only 4 percent for the nation. If this projection proves true, Oregon will significantly reduce the gap with the U.S. average.



Public Service Productivity. Along with more resources from a growing economy, smart reforms in healthcare and corrections helped to pave the way for needed education investments. New coordinated care organizations (CCOs) have reduced emergency room visits, increased preventive care, and slowed per capita growth in Medicaid spending to less than 3.4 percent annually. In corrections, sentencing reforms passed in the 2013 Legislature have stabilized the incarceration rate.

Breaking the Circle of Scarcity. The economic expansion has restarted a "circle of prosperity" in which a robust economy creates revenue for investment in education and other services, which, in turn, fuels business success and higher incomes. With higher tax receipts state lawmakers have had sizable revenue increases at their disposal in each of the last two sessions.



Breaking a trend of stagnant investment, budget writers steered large shares of the increases into education (see chart at right). For K-12 education, the additional revenue funded full-day kindergarten, restored school days, and allowed principals to rebuild programs lost during the recession. Universities and colleges received a 24 percent increase in the most recent legislative budget.

The current education budget counters a decade of stagnant funding in the face of surging enrollments. With the funding increase, universities have initiated a transition to outcome-based funding, which will tie state investments to degree progress and completion rather than enrollment. And, community colleges will be free of charge to Oregon residents within six months of high school completion who apply for available federal aid and maintain a 2.5 grade point average or better.

Unfinished Business. While there is much to celebrate, much remains unfinished. Oregon's poverty rate hasn't budged in recent years and stands a full percentage point above the U.S. average. Unemployment rates are high for adults with low levels of education attainment. And parts of the state – the Eugene and Medford regions and rural counties – have yet to return to pre-recession job levels. For too many, the recovery is incomplete. As we plan for the next stage, it is important to keep these challenges in mind.

Progress on Specific Business Plan Initiatives. This past year, the Business Plan called out three priorities that the Steering Committee believed were ripe for immediate attention.

- *Connect Education to Careers,*
- *Put Our Natural Resources to Work*
- *Modernize Our Infrastructure*

In addition, at the federal level the Business Plan highlighted the vital importance of U.S. adoption of the Trans-Pacific Partnership (TPP) agreement. Also, we laid out initiatives to improve the safety net for low-income, working Oregonians.

Oregon made good progress on all these issues this past year, with one exception: transportation funding. The Legislature was unable to agree on a package to support badly needed improvements. This is part of unfinished work that we want to pursue in 2016 and beyond.

HEADWINDS

As we plan ahead we see headwinds that could impede Oregon's progress. The state will need to address these challenges in the year ahead.

Initiative Petition 28 – The $5 Billion Tax on Oregon Sales. Growing businesses in order to grow jobs, incomes, and revenue for schools is at the core of the Oregon Business Plan. Over the past four years, business growth has led to over 150,000 new jobs and has provided $4 billion in additional revenue for public services. During that time, as a result of a growing economy and smarter spending, Oregon has moved from 37th among the states in K-12 per student spending up to 22.nd

Despite this progress, petitioners are circulating an initiative to impose a new $5 billion tax on Oregon sales – including the sale of many goods and services that Oregon consumers and small businesses purchase every day: food, electricity, gasoline, medicine, and other necessities.

The way the measure is structured, for many Oregon products the new tax could be applied at every step in the production process, as the product goes from manufacturer to distributor to retailer before finally reaching the consumer. This type of "tax on a tax" would make Oregon products more expensive, and Oregon companies less competitive.

IP 28 could impose – at every stage of the supply chain – a 2.5 percent tax on the sale of food, electricity, gasoline, medicine and other products and services that Oregon consumers and small businesses purchase every day.

And, because this would be a tax on sales – not profits – businesses will be forced to pay the tax whether they make a large profit, a small profit, or no profit at all. This means that the burden of paying this huge new tax will ultimately fall on Oregon consumers and small businesses through higher prices on everything from insurance to utilities to health care. Research has shown that this type of tax unfairly hurts those who can least afford to pay higher prices for essential goods and services such as groceries, utilities, and medicine. Seniors and families on fixed incomes would be hit especially hard.

The measure is particularly harsh to Oregon-based service companies, who will pay the tax on their global sales just because they are based in Oregon, dealing a severe blow to the competitiveness of Oregon's burgeoning software, engineering, and architecture industries.

PERS. One of the key Oregon Business Plan priorities in 2011 was to fix significant flaws in Oregon's Public Employees Retirement System or PERS. Our Governor and Legislature responded, making sensible adjustments to imprudent, excessively expensive retirement benefits. Unfortunately, the Oregon Supreme Court overturned those reforms, leaving Oregon with an $18 billion liability. If that isn't addressed, it will raise retirement costs and reduce service capabilities among public employers to punishing levels for the next two decades.

Fortunately, the court suggested steps that can be taken to tame future PERS costs. We should return to this issue with an aim to reduce the liability. We discuss this in greater detail below and in a separate policy paper on public employee compensation that follows in this playbook.

Housing Affordability. As the economy has recovered, individuals and families across the nation are seeking out new places to find opportunity and call home. Oregon is a top destination. West Coast technology firms, repelled by the Bay Area's housing prices and Seattle's traffic, are setting roots in Oregon.

In-migration, which adds knowledge and skills to our workforce, is generally good news. But the resulting rise in population is outstripping housing supply, especially in Portland and Bend. The two regions are in the top tier for house price appreciation nationally, and public policy has been slow to respond. Proposed remedies have ranged from low-income housing subsidies and eviction regulations to rent control and tiny houses. But a growing chorus of economists, including the President's chief economic adviser, points to land use restrictions as the main culprit. State and local governments need to develop a clearer, realistic understanding of Oregon's population future and design a comprehensive housing supply response that ensures inward migration doesn't drive out existing residents.

Minimum wage. Oregon has the second highest statewide minimum wage in the U.S. and proposals are circulating to push it even higher. Such increases risk making businesses less competitive and increasing unemployment among entry level workers. A 2014 report issued by the Brookings Institution suggested that states peg the minimum wage to one-half the median wage for full-time workers in the state. Oregon's current minimum wage, at $9.25 per hour, indexed to inflation, is roughly in line with the Brookings recommendation. And Oregon sets rate policy at the state level, which is critical for avoiding confusing and unfair differences among local jurisdictions. Any changes to current law need to be done with great care.

AN AGENDA FOR 2016

Our agenda for 2016 has two components. The first is to continue the work set out last year on CTE-STEM, natural resources, transportation, the Trans-Pacific Partnership agreement, and poverty reduction. The second is to work with our partners to comprehensively review the Business Plan to shape a fresh agenda in the next year.

As we organize our work, we continue to use the three-part formula for success described and illustrated on the opening page of this section: 1) grow the economy, 2) boost public sector productivity and 3) accelerate the circle of prosperity to invest more in key education outcomes. It has largely worked well over the past five years. We want to use it as a guide for the years immediately ahead.

1. Grow the Economy

Nearly every challenge facing Oregon is easier to address when the economy is flourishing. More people find work, incomes rise, and more dollars become available for public and non-profit services. The progress made over the past five years is a powerful illustration of this point.

Our overriding vision for growing jobs and incomes is suggested on the cover of this playbook. Oregon will prosper by supporting leading-edge firms that sell innovative products and services outside our borders and around the world. The Business Plan recognizes that places tend to specialize in terms of the products and services that they produce. Industries cluster together to take advantage of common suppliers, specialty workforce, and inherent regional advantages, such as availability of particular natural resources.

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The Business Plan has identified key Oregon clusters and promoted them. Looking at Oregon's clusters, there is good news. A snapshot of our performance is provided under Traded Sector Strength Indicators and Performance of Select Industries on the following table. In nearly all the clusters identified in the Business Plan, Oregon firms are gaining market share over other places, as illustrated by the location quotient data in the table (a quotient of 1.0 means Oregon has the same proportion of jobs in that sector as the average state; a higher quotient means more jobs). Two other signs bode well for Oregon: our exports have doubled in ten years and we have a high rate of patent creation.

We need to build on this momentum and continue to concentrate on growing the economy. Sadly, Oregon has a history of losing focus as the economy improves. In the booming late 1990s, for example, elected officials signaled in ways big and small a lack of interest in growing jobs in the Portland region and the Willamette Valley. Industry leaders quietly listened and made decisions to invest elsewhere, to the regret of many when the recession hit soon thereafter.

To sustain economic growth and raise incomes, business leaders need to know that they are supported *throughout* the economic cycle, especially in good times. Every state woos business in recessions, a time when business expansion opportunities typically are limited. Smart states encourage businesses during the best of times.

In the year ahead we will be working in depth with industry leaders from around the state to gather fresh insight into what Oregon needs to do support the growth of its business. Drawing on our earlier work, below are four priorities for economic growth to work on right away.

KEY GOALS							
Fundamental Outcomes	Base Yr.	Base Value	Goal	Current	U.S.	Yr.	Rank
25,000 net new jobs /yr	N/A	N/A	25,000 net new jobs	30,520 (5 yr ave)	N/A	2010-14	N/A
Per Capita Income Above National Average (by 2020)	2010	89.4%	100%	90.4% (of national)	N/A	2014	N/A
Poverty Rate Below 10% (by 2020)	2010	15.8%	10% (by 2020)	16.6%	15.5%	2014	36
Traded Sector Strength Indicators							
Total Job Growth in Traded	2003	498,427	N/A	481,633	N/A	2013	N/A
Real Exports[1]	2003	$14.7 bn	N/A	$37 bn	N/A	2014	18
Patents Awarded per 10,000 employees	2003	12.44	N/A	15.5	8.94% (average)	2013	7

Performance of Select Industries	Location Quotient (2003)	Location Quotient (2013)	Oregon % Change Employment, (2003-13)	National % Change Employment, (2003-13)	Performance relative to Nation	Oregon Change in Employment share, (2003-13)
Manufacturing	1.09	1.17	-10.2%	-17.0%	6.9%	0.11%
Distribution and Electronic Commerce	1.03	1.08	11.7%	6.3%	5.4%	0.06%
Business Services	0.84	0.79	13.5%	19.9%	-6.3%	-0.05%
Forestry	10.81	11.78	-21.40%	-27.90%	6.50%	1.16%
Semiconductors	3.59	5.95	-2.80%	-41.50%	38.70%	2.81%
Wood Products	5.04	5.06	-32.00%	-32.30%	0.30%	0.03%
Information Technology and Analytical Instruments	2.17	2.2	-14.70%	-16.00%	1.30%	0.04%
Footwear	0.84	1.93	31.70%	-42.60%	74.30%	1.29%
Food Processing & Manufacturing	1.62	1.79	13.20%	2.10%	11.10%	0.21%
Software Publishers	1.32	1.58	48.20%	24.30%	23.80%	0.30%
Hospitality and Tourism	0.97	0.98	8.40%	7.20%	1.30%	0.01%
Apparel	0.45	0.70	-31.60%	-55.80%	24.20%	0.30%
Financial Services	0.74	0.53	-41.3%	-17.0%	-41.3%	-24.3%

Support the Trans-Pacific Partnership Trade Agreement. It's no accident that President Obama chose Oregon to showcase the TPP last May. Our region was built on a foundation of trade that predates the state's founding. And today's economy – from semiconductors and software to innovative wood products and sustainable architecture – leans into the future. We sit across the Pacific Ocean from rapidly growing economies. Projections show that Asia's middle class consumers could increase from 500 milion in 2009 to 3.2 *billion* by 2030.

Opportunities abound for Oregon businesses as populations fill expanding Asian cities. Regions will encounter growth challenges that we addressed long-ago. Our urban planners can help design ecodistricts that keep people and commerce flowing while using fewer resources. Our architects can collaborate on energy-efficient buildings. And infrastructure consultants can point to innovative solutions on storm and wastewater management. Along these lines, Portland's *We Build Green Cities* initiative is an important reminder that trade isn't limited to goods that can be shipped in a container.

That said, the demand for goods is on the rise too, and Oregon brands are strong. The state's food and beverage manufacturing sector barely paused during the recession and is developing a reputation for wholesome quality that sells well overseas and across the United States. And our footwear and athletic apparel sector has connected with a growing global consumer class.

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Last summer a majority of Oregon's congressional delegation supported trade promotion authority legislation which gave the President the authority to bring the TPP to Congress for an up or down vote. The agreement has now been reached. It reduces tariffs, strengthens protection for intellectual property, and includes other provisions to make Oregon products more competitive in this growing region of the world. Oregon's business leaders stand with TPP's supporters throughout the approval process. The agreement's passage will be a big win for Oregon.

Connect Education to Careers Through CTE and STEM. As outlined later in the playbook paper Students at the Center, the Oregon Business Plan has an ambitious agenda to transform learning and student outcomes. A vital part of that vision is better connecting our education system to well-paying careers through career technical education (CTE) and science, technology, engineering, and math (STEM) education.

This work took a big step forward last session as the Legislature more than doubled investments in CTE and STEM from $17 million to $35 million. These CTE and STEM investments – coupled with an Oregon Talent Council investment of $6.1 million – will help address high-demand workforce needs and improve the prosperity of individuals and communities across the state.

CTE and STEM education equips Oregon students with the knowledge, skills, and mindsets that will prepare them to thrive in a rapidly-changing, technologically rich, global society. The applied learning of CTE and STEM engages and motivates students, ignites curiosity and creativity, encourages problem solving, and instills strong work habits.

Oregon must redouble efforts to expand CTE and STEM education to all students through investments and policies that connect education to careers. The first step in in this process is the completion of a STEM Strategic Plan, which will outline a clear vision for STEM education in Oregon, identify goals and supporting strategies, and present the benefits that are certain to follow if Oregon fully implements its STEM, CTE, and workforce strategies.

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Put Our Sustainable Natural Resources to Work. Oregon should build on the success of the Umatilla Basin project for storing Columbia River water and continue to put our sustainable natural resources to work. As discussed later in this playbook, in the paper on Revitalizing Rural Oregon, the clear first step is sensible forest policy. Forest mismanagement, together with climate change, has extended the length of fire seasons and generated larger, more expensive fires. In August, fires affected 465,520 acres in Oregon and – and an average suppression cost of $201 per acre – costing $93.6 million. But the economic impact goes well beyond the costs of fighting fires. Wildfires push more carbon into the atmosphere, diminish air quality, and damage water supplies.

Improved managment requires action on multiple levels. Top priorities include reform of the federal Wildfire Funding Disaster Act and full implementation of the Oregon Department of Forestry's Federal Forest Health Program.

Along with better forest management, innovation in the sector will spur demand for wood products and create rural jobs. This September Oregon's D.R. Johnson became the first U.S. company certified to make cross-laminated timber panels. As demand for the product takes off across the world, Oregon—with its rich and diverse timberlands—holds a strong competitive advantage.

Maintain and Expand Infrastructure. In addition to favorable trade policy, a vibrant traded sector requires modern, well-maintained infrastructure. Oregon businesses are paying a high price for deterioriating roads and bridges. They pay through higher maintenance costs on their vehicles and in lost productivity from congestion.

The time to invest couldn't be better. Construction labor is available, material costs are down, and capital costs are at historic lows. This past June lawmakers in Washington State saw the opportunity and passed a $16 billion transportation package. It creates 200,000 jobs, eliminates a major I-5 bottleneck, restores bridges, and insures proper road maintenance across the state for the next 16 years. Meanwhile, in Salem, a much smaller transportation package was a near-miss. Getting that back on track is a key priority for 2016.

2. Boost Government Productivity

Public services are vital to Oregon's quality of life and to the performance of the economy. Many of the features included in the Business Plan strategy framework, including schools, transportation, health care, and human services involve the public sector. How well we provide those services impacts economic performance as well as to the general quality of life in our state.

For public services, just as for the private sector, there are always opportunities to innovate and improve service delivery. It is important to constantly seek improvements in order to provide value to taxpayers and states that do will also have an advantage in attracting and retaining businesses over those who do not.

Over the past five years the state has focused on making improvements in four large state systems, education, health care, human services and corrections. In addition, it has tried to stem the growing costs of the Public Employee Retirement System (PERS) and employee health care costs. Many of the results to date are promising, but there is much more to do.

Education and Health Care. In addition to the paper on transforming education, this playbook later addresses health and healthcare issues in the paper Health Care Strategy Reset. In education and health care, the aim is to encourage change in the way services are delivered to provide better results for students and for patients. The framework is similar in both cases. We need to be clear on the outcomes we want and measure how well we are achieving them. We need to design funding streams that encourage education and health care professionals to innovate to achieve the outcomes Oregon desires. We need to spotlight practices that are working and encourage replication. And we need to invest where we can make the greatest difference, which in the case of both education and health care is often early in life.

As both education and health care leaders rethink their models, there is a growing opportunity to align the work. Good health is critical for education and education is key to good health. Our policy papers suggest that by aligning efforts, schools and health care providers can be more effective at both. The Business Plan intends to explore this opportunity in greater depth in the year ahead.

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Human Services. In this area the Oregon Business Plan's Poverty Taskforce has focused on strengthening the safety net and improving work incentives. In 2015, the Legislature reformed the Temporary Assistance to Needy Families (TANF) program, expanded childcare subsidies, improved childcare tax credits, and extended a critical program that helps families build financial assets. These were big wins for low-income working families.

Going forward, the taskforce has two areas of focus. The first is a focused strategy on preventing poverty for teens and young adults (14-25 years). This population represents a critical leverage point in the overall poverty reduction strategy. Too many Oregon teens are dropping out of high school and entering young adulthood with bleak economic prospets. Moreover, many form families before they have the resources to support them. The taskforce will look across the education, safety net, and economic policy landscape and advocate the expansion of evidence-based programs that can fundamently improve how teens transition into adulthood.

Second, the taskforce will advocate expansion of and better outreach for the Earned Income Tax Credit (EITC). This wage subsidy program is perhaps the best intervention in U.S. labor market history. Oregon's program is underused and too small. Business leaders support expansion of the credit – especially for parents of pre-school-age children who have elevated costs and rates of poverty.

Corrections. Sentencing reforms have stabilized the growth in corrections populations. That said, Oregon needs to take reforms further. Rates of incarceration in Oregon and the U.S, are well above international norms. Costly prison beds should be reserved for violent offenders and those convicted of person-to-person crimes. We need to find cost-effective alternatives to incarceration for non-violent criminals.

Public Employee Compensation, PERS, the Cadillac Tax. Quality employees are critical for any organization, and public services are no exception. We need to provide pay that attracts the talent Oregon needs to deliver quality services. At the same time, we should recognize that when total compensation becomes excessive, it comes at the price of the public services themselves.

Later in this playbook the paper Overhauling Public Employee Compensation explores our public compensation headwind in greater depth. Briefly, however,– a federal surcharge on overly generous health plans.

These developments force a comprehensive review of compensation, and as it proceeds, it should follow a principle first advanced by Governor Ted Kulongoski's *Reset Report*: public employee compensation should advance in step with, but not outpace, the compensation increases experienced in the private sector workforce.

PERS poses by far the biggest challege. Oregon's Supreme Court has made clear that those who benefited from windfall pension gains—mostly those hired between the early 1970s and late 1980s—cannot be asked to share in the problems created by their good fortune. The decision, while misguided, nonetheless brings a new focus to the task at hand. The Supreme Court decision did provide guidance on specific steps that can be taken to tame Oregon's pension liability, which now is estimated to be in the range of 18 to 20 *billion* dollars. We explore those option in the accompanying policy briefing.

Public employers face two major challenges -- reversal of 2013 PERS reforms that will trigger unprecedented increases in contributions to the pension system, and navigating the Affordable Care Act's "Cadillac tax."

Public employee health plans also require attention. The Cadillac tax surcharge will assess a 40 percent luxury tax on plan costs that exceed $10,200 for individual coverage and $27,500 for families. A feature of the ACA, the tax draws support among economists who view it as an important tool to slow healthcare spending and bring wage and benefit compensation into better balance. The good news is that the Legislature, the Public Employee Benefits Board and the Oregon Educators Benefit Board are taking steps to address this challenge.

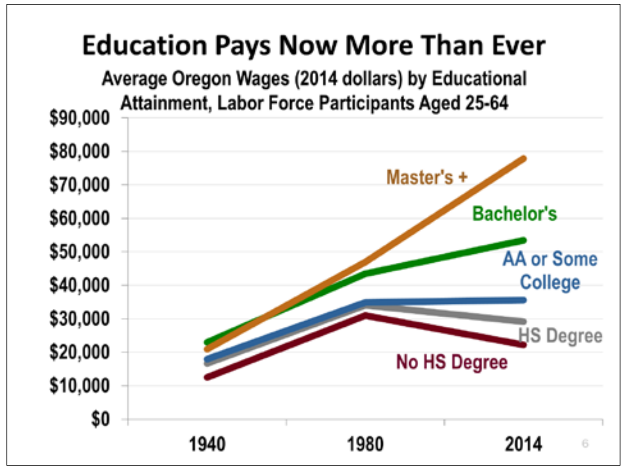
Competently navigating these two compensation issues would go a long way to strengthen the state's provision of public services.

3. Accelerate the Circle of Prosperity

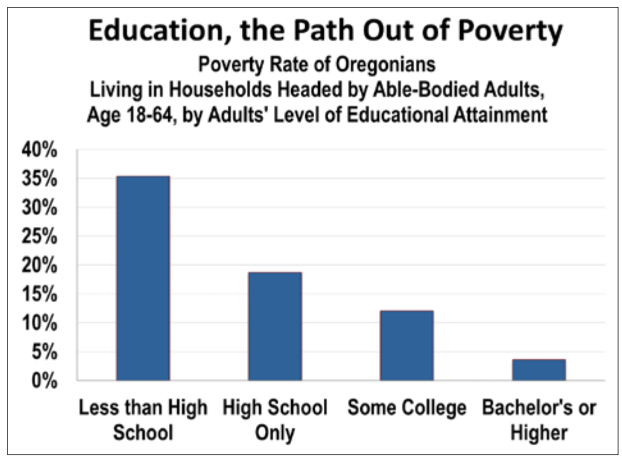
Oregon has created more jobs, which in turn has generated more public sector revenue – roughly $4 billion more in this current biennium – than was available four years ago. Through public service redesign, we have tamed the rates of growth for health care and corrections even while increasing dramatically the number of Oregonians with health insurance. We have invested more in education at every stage – and aimed those dollars toward greater rates of achievement and degree attainment.

We are moving in the right direction. To accelerate this progress in a way that generates not just more jobs but higher incomes and reduced poverty, we need to address the final pillar of our three part framework, the Circle of Prosperity.

The key idea behind the circle is the strong connection among education attainment, earnings, and employment security. As illustrated in the adjacent figure, now more than ever, education drives earnings. By the same token, the figure that follows illustrates a strong correlation between poverty and lower levels of education. And we know that individuals with career technical and STEM degrees typically gain an income premium. To raise incomes and reduce poverty, it is essential to provide Oregonians the education they need to thrive in a growing economy..



Income growth and lower poverty rates have two important impacts on public budgets. First, growing incomes result in significantly more public revenue. For example, we estimate that achieving our goals for CTE and STEM education alone could result in over $800 million per biennium in general fund revenue by substantially raising the personal income of the state as businesses demand for skilled employees is fulfilled. Raising attainment across the board could generate far more revenue. Second, we know that Medicaid and other social services disportionately go to those with high school diplomas or less. Those costs would be reduced by improving high school and college completion rates. The savings could then be channelled into more funding for schools and other public purposes.



It's a virtuous circle: economic growth yields stronger budgets and education investments which boosts incomes, lowers demand for social services, and – in turn – creates more opportunity for further education investments.

We have the opportunity to accelerate this progress through disciplined additional investments in accountable education. The first step is to adopt the recommendations to boost education productivity, as suggested above. We have set ambitious goals for education attainment in Oregon. That requires investing more dollars wisely translate in better outcomes for students and for Oregon. The key to such investment is 1) managing the state budget in a way that delivers more dollars per student and 2) invests those dollars in a way that enchances the educational experience, accelerates time to degree completion, and, in the case of post-secondary education, makes the experience more affordable, especially for low- and middle-income Oregonians.

A Hopeful Outlook. The Business Plan has examined the likelihood that Oregon will be able to increase education funding in the years ahead. There are positive and contervailing factors at play, but generally, the odds are favorable.

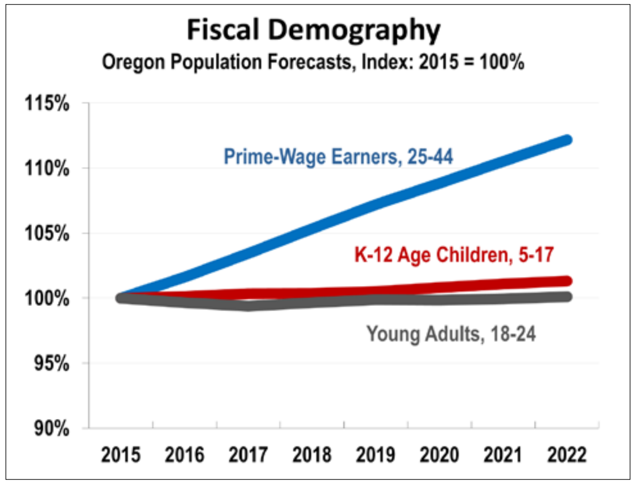
The state economist projects the economy – and the General Fund – to grow a little faster than 5 percent annually over the decade. That, in turn, generates an additional $2 billion in each biennium during the forecast period.

Countering that trend, Medicaid, state employee health care, and PERS could grow faster than the economy and General Fund. Medicaid costs will be driven by long-term care for aging boomers, the gradual phase-in of a state match rate for the Affordable Care Act, and the ever-present threat of cost inflation. The cost pressures on state employee health care and PERS have been discussed previously. The state's share of

Medicaid could grow 7 percent annually; employee benefits – if unreformed – could grow 6 percent annually. Our proposals intend to curb both of these rates.

Yet even if the most pessimistic scenario occurs, education spending – net of employee benefit increases – would grow at about 4 percent annually overall and *per student*.

This increase in funding per student is due to some welcome demographic news. After a couple of decades of exerting pressure on education funding, the children of Baby Boomers (the big cohort sometimes called the Baby Boom echo), has left school and is aging into its prime earning – and taxpaying -- years. From 2015 to 2022, the state will add nearly 131,000 prime-age earners (25-44) compared with just under 9,000 school-aged children and young adults. In other words, the state will add about 15 new potential taxpayers for every new student. The slow – .1 percent – growth in the age 5-24 population implies that per-student spending will increase at about the same rate as overall spending.



Four percent growth would increase Oregon's $11,100 K12 per-student spending – ranked 22nd in U.S. in 2015 – by $400 to $500 per year. We see opportunities for this investment to grow even faster. First, we could beat the state economist's expectations and add a percentage point or two to economic growth. Oregon has done this before; the state grew at a 6.7 percent annual clip in the 1990s. We should not let up on our current momentum. Second, we can do the hard work to keep Medicaid and public employee benefit costs in line, as suggested in the two policy papers included in this Playbook. Taken together, those two steps would take our education investment from good to great.

The Governor and legislative leaders have the opportunity to create a long-term fiscal plan that drives stronger education outcomes that in turn will help to bolster our economy, grow incomes, and reduce poverty. The plan should recognize the dynamic between education attainment and incomes. It should also consider the demographic trends that will shape funding requirements. During the next year the Governor will be preparing a budget for 2017-19. As she prepares that budget, we encourage her to take the long view and bring forward a plan that steadily increases investments in accountable education over the years ahead.

> *We need a revenue system that pays for vital services throughout economic cycles, is predictable, creates strong incentives for economic growth, and is equitable. The Legislature is the best place to pursue such a system.*

Tax Structure and Revenue Adequacy. While the forecast above suggest that student funding will increase in the years ahead, our current tax structure and revenue policy could throw Oregon off course. The current revenue system, with extraordinary reliance on the personal income tax, suffers from two big flaws.

First, it is unstable, swinging wildly with economic cycles. This roller coaster effect harms vital services, especially schools, which inevitably suffer budget cuts during downturns. This volatility is exacerbated by the kicker law, which refunds revenue that exceeds forecasts rather than building up a reserve fund. Policymakers deserve credit for improving the reserve policy over the past decade. Reserves currently stand at about 5 percent of the General Fund, which is much better than levels during our two most recent recessions. But our reserves won't reach an adequate level – 7.5 percent of the General Fund – until the end of the 2017-19 fiscal year, so we are left hoping this economic expansion continues its run.

Second, because our incomes and capital gains tax rates are among the highest in the nation (in sharp contrast to Washington state, which has none at all), we discourage entrepreneurs and businesses with high salaries from locating here. Indeed, our tax system could explain much of the reason that Washington state enjoys much higher incomes and rates of capital formation.

This is a long-standing problem that many business leaders want to address. We need a system that pays for vital services throughout economic cycles, is predictable, creates strong incentives for economic growth, and is equitable.

Whatever the tax structure, a second issue relates to the adequacy of the revenue system to pay for the services that Oregonians want. Assessing adequacy of services is always a matter of judgement, but we suggest the following three pillars guide any such discussion.

- The best source of increased revenue for public services is a strong healthy economy. Tax policy that impedes economic growth is counterproductive.
- The public sector should be continuously improving productivity.
- Any revenue increase must be tied to clear, demonstrable outcomes that make Oregon a better place to live and work.

By far the best place to address tax structure and revenue adequacy is in the Legislature, not through initiative measures. The Legislature is a far better venue for weighing different perspectives, addressing critical details, and forging good public policy.

FOUR ISSUE PAPERS

REVITALIZING RURAL OREGON

Draft for Discussion at the Leadership Summit

Summary Recommendations

- Improve national forest health and resiliency by enacting federal legislation to address the wildfire-funding crisis and create legally sufficient opportunities to increase active, sustainable forest management.
- Fully implement the Oregon Department of Forestry's Federal Forest Health Program to strengthen the capacity of collaboratives statewide and provide funds to ODF to augment the U.S. Forest Service's restoration efforts.
- Fully implement HB 3549, enacted by the 2015 Legislature, to ensure safe and appropriate use of forest herbicides in Oregon.
- Develop and approve a plan by the end of 2016 for Oregon's state-owned forests to set aside 70 percent of the forests for active timber management and 30 percent for conservation values, while guaranteeing that harvest will not exceed annual growth.
- Support private and public initiatives that advance the use of traditional and innovative wood products in commercial construction, including the use of mass timber in tall wood buildings.
- Continue support for investments in water supply, storage, and reuse in rural Oregon. Help build political support for environmentally sound water supply policy.
- Expand the commitment to better quantify water supply and demand, and improve conservation and wildlife protection to drought-prone regions of the state.
- Continue to support innovative place based planning and regional implementation of programs and projects to fix water supply challenges and susceptibility to drought impacts.
- Continue to support efforts to manufacture and market sustainably harvested Western Juniper.
- Support working farms, forests, and rangelands in Oregon that balance both production and conservation needs.
- Expand access to capital to rural enterprises and infrastructure. Funds should be prioritized for projects that balance production needs and conservation benefits related to forest, water, farm, or rangeland management. Streamline access to these funds through partnerships with third party providers.

Overview

Rural Oregon enjoyed important natural resource policy victories in 2015, including expansions in state support for federal forest management, funds to help plan, design and build new water supply infrastructure, and investments in the marketing and manufacturing of sustainably harvested Western Juniper. But to overcome rural Oregon's economic prosperity shortfall, independent actions are not enough. Thoughtful natural resource use, improvements in land stewardship, and community conservation strategies will help unleash the potential for sustainable use of Oregon's natural resources. From expanding into new manufactured wood products to developing more valuable agricultural products, Oregon's natural resource-dependent rural communities could double their economic output in ten years.

In 2016 the Oregon Business Plan will reaffirm its commitment to 1) promote working forest landscapes and water development and storage, 2) advocate for expanded use of manufactured wood products and increases in investments in value-added agriculture products, and 3) build markets for Western Juniper wood products. Top priorities will include pressing the federal government to accelerate the pace and scale of forest restoration, securing federal funding that places forest fire response on par with other natural disasters, and building public support for water development and storage. Working closely with our rural community partners, in 2016 we will revise and update the rural agenda of the Business Plan, building on the sustainable use and protection of natural resources, diversifying economic opportunities to add more value to products, and develop effective linkages between rural economic health, education and workforce training, and public health.

While much of Oregon has recovered from the Great Recession of 2008, when compared to the rest of the state, unemployment, poverty, and incomes in rural Oregon remain unacceptably high.

The Challenge

While much of Oregon has recovered from the Great Recession of 2008, when compared to the rest of the state, unemployment, poverty, and incomes in rural Oregon remain unacceptably high. Employment throughout rural Oregon is still 7 percent below the 2008 peak, while employment in urban areas is now higher than it was in 2008[1]. For every $3 earned by families in Umatilla, Jefferson, and Malheur counties, families in Multnomah, Washington, and Clackamas counties earn $4.[2]

One important explanation for this trend lies in the inadequate use, management, and conservation of Oregon's natural resources. Nowhere is this more prevalent than public land management.

Unrealized Commercial and Conservation Opportunities in Oregon's Forests. Timber harvest serves as a good indicator of forest and forest community health. In 2014, timber harvest in Oregon remained steady at just above 4 million board feet. Timber harvest from federal land increased roughly 7 percent, due largely to post-fire timber harvest and increases in harvests in Lake, Grant, and Harney counties. Nearly 400 million board feet (mmbf) was harvested in 2014; Oregon's 11.6 million acres of USFS timberlands produced roughly 33 bf/acre per year. This compares to 3,185 mmbf harvested on 10.3 million acres of private timberland, producing an average of 309 bf/ac/year.

Lack of intensive management practices is a major cause of the catastrophic forest fires we endure every fire season. Fires burned nearly 640,000 acres across Oregon in 2015, costing nearly $80 million to fight, and resulted in an estimated cost of over $200 million in lost timber volume.[3] The impact on the environment is arguably even more costly. While no estimates exist for the impact of Oregon's wildfires, the Washington Department of Natural Resources estimates that the 2015 fire season produced an estimated 15.8 million metric tons of CO2e emission – second only to transportation as the worst GHG emitter in the state.[4]

Our forest fires impact a range of costs affecting the state. In 2015 the Oregon Department of Forestry (ODF) paid Lloyds of London $3.75 million to insure against forest fire costs – nearly double the amount from 2014-15.[5] Fire-prone areas in California have seen annual homeowner insurance premiums jump by more than $4,000. Many major carriers have stopped offering coverage in fire-prone, forested areas.

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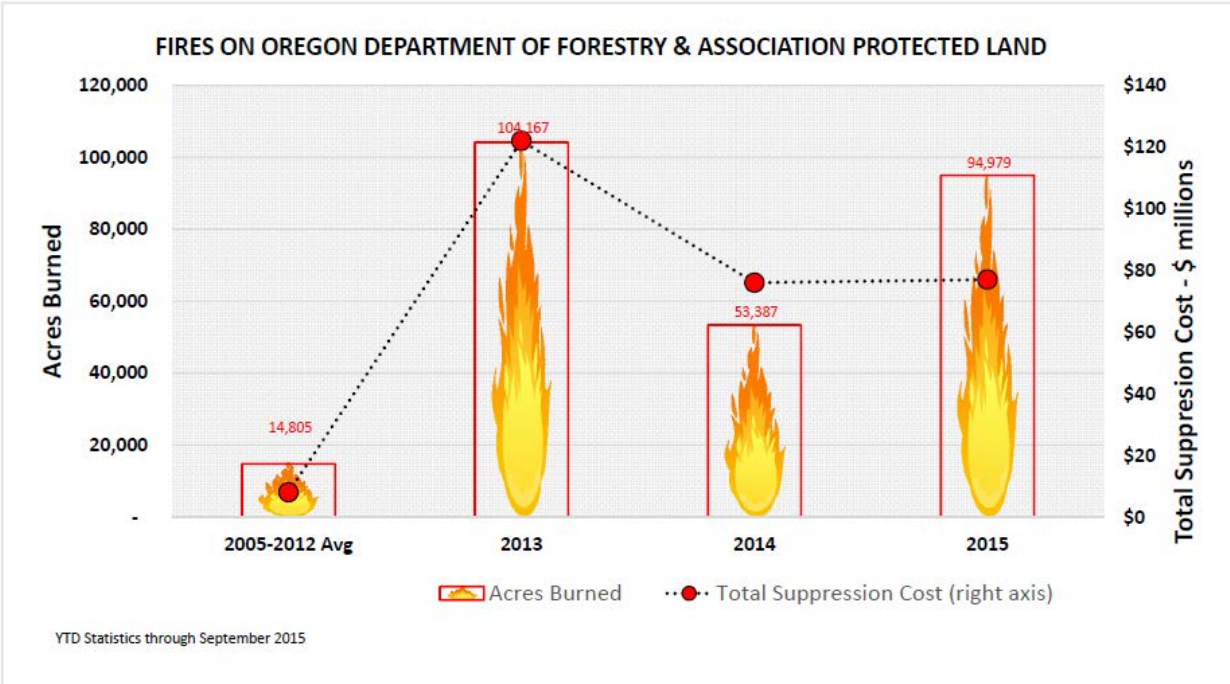
[1] Mark McMullen and Josh Lehner, *Rural Oregon: Analyzing Demographic and Economic Trends Across Rural Oregon, and a Look Ahead*. Oregon Department of Economic Analysis. September 2015.

[2] Oregon Department of Economic Analysis, http://www.oregon.gov/DAS/OEA/docs/economic/oregon.p

[3] Data on acres burned received from the Oregon Department of Forestry. Data on total cost of fires was received from AFRC.

[4] From the Office of the Commissioner of Natural Resources: Total acres burned (as of October 7, 2015) was 1,090,765. Estimated CO2e emissions from wildfire: 15.8 million metric tons

[5] http://www.oregonlive.com/pacific-northwest-news/index.ssf/2015/04/lloyds_of_london_offers_oregon.html. The Lloyds of London policy was originally designed to protect the General Fund from emergency forest fire suppression costs that exceeded the local forest protection district fire fighting resources. It does not protect landowners from resource loss. Historically, through the Oregon Forestland Protection Fund landowners and General Fund shared the cost of the insurance premium and deductible, then the insurance policy kicked in for suppression costs exceeding the deductible.



(EFCC from ODF data)

While we are making important progress to restore federal forests and rebuild timber jobs, the pace is too slow, the scale too small, and the costs difficult to sustain. Oregon's most successful forest restoration efforts are underway in the Blue Mountain area, comprised of nearly six million acres across the Wallowa Whitman, Umatilla, Ochoco, and Malheur National Forests. $1.8 million in state and federal funds were spent on Blue Mountain forests between 2013-15, resulting in 140,000 acres of forest lands treated, 157 million board feet of timber produced, and nearly 500,000 acres moving towards consensus on management.[6] If we double the annual rate of acres treated in 2014 (300,000), we estimate it will require at least 14 years and $20 million dollars to complete restoration in the Blue Mountains region alone.[7] Given the damage to natural systems and communities caused by forest fires, and its contribution to climate change, we simply don't have twenty years to play forest health catch up.

While we are making important progress to restore federal forests and rebuild timber jobs, the pace is too slow, the scale too small, and the costs difficult to sustain.

Water. Two out of three Oregon counties declared drought emergencies in 2015, including west-side counties where water is normally thought to be in abundance. Drought conditions forced farmers to change their irrigation patterns, risking water supply towards the end of the growing season. Large portions of land in north central and southeastern Oregon, and in the Klamath Basin saw only one cutting of hay crops due to the lack of water for irrigation. Drought conditions in 2015 have long-term implications for growing next season's crops, and farmers already anticipate low water and snow pack in 2016.[8] Based on current consumption and storage practices, Oregon can no longer claim to have plenty of water to go around.

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[6] Eric M. White, Emily Jane Davis, Drew E. Bennett, and Cassandra Moseley, *Monitoring of Outcomes From Oregon's Federal Forest Health Program*. University of Oregon Ecosystem Workforce Program Working Paper Number 57, Summer 2015.

[7] Estimate based on treating .73 percent of the 6 million total acres for eligible for treatment, divided by 300,000 acres treated per year, multiplied by $1 million in annual treatment costs.

[8] http://www.ktvz.com/news/twothirds-of-oregon-counties-now-in-drought-emergency/34282672.

Nowhere are the consequences of limited water supply to conservation and agriculture more apparent than in north central Oregon. Through the adoption of state-of-the art water use and conservation technologies, over the past decade Oregon's agriculture belt has diversified its crops to include higher value and value added crops like carrots, sweet corn, and asparagus as well as a growing dairy and beef industry. In turn, the growth in agriculture output has fueled explosive investments in manufacturing and food processing. Responding to this opportunity to add value to Oregon's food crops, by 2013 the Port of Morrow has grown to become Oregon's second largest port. It is the primary export port for value-added agricultural products, serving farmers and ranchers in a five-state area. Total employment exceeds 7,000 people, $266 million in salaries paid, and $1.6 billion in annual total output.[9]

But the potential to grow more agricultural products and create more jobs is constrained by the lack of additional water. As the box below shows for carrot production, if we can develop enough water for just one standard sized irrigation circle (125 acres or 375 acre-feet of water), we could add $475,000 of revenues to the farm, but generate a total of $8.6 million in value-added economic impact to Oregon's economy.[10] That is just one example of one crop. The Umatilla Basin grows over 280 crop varieties and is working to develop over 150,000 acre-feet of sustainable Columbia River water in the years to come.

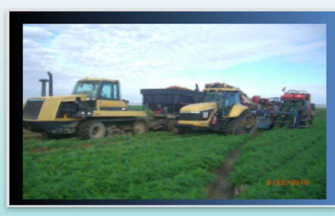
RAW PRODUCT - CARROTS

OREGON'S OTHER ORANGE POWERHOUSE

125 ACRES = $475,000 = $8.6 MILLION

CARROTS

						PER ACRE				TOTAL			
#	SUPPLY CHAIN	PRICE UNIT	PRICE UNIT	$/UNIT	%	TONS	POUNDS	OUNCES	$	TONS	POUNDS	OUNCES	$
1	Farm	Harvested Carrots	Ton	$ 95.00		40.00	80,000	1,280,000		5,000.00	10,000,000	160,000,000	
2	Farm	Usable Carrots	Ton	$105.56	90%	36.00	72,000	1,152,000	$ 3,800	4,500.00	9,000,000	144,000,000	$ 475,000
3	Processor	Finished Product	Pound	$ 0.35	60%	21.60	43,200	691,200	$ 15,120	2,700.00	5,400,000	86,400,000	$ 1,890,000
4	Repackage Facility	Packaged Finished	Pound	$ 0.10	100%	21.60	43,200	691,200	$ 4,320	2,700.00	5,400,000	86,400,000	$ 540,000
5	Retail	Store Sales	Ounce	$ 0.10	100%	21.60	43,200	691,200	$ 69,120	2,700.00	5,400,000	86,400,000	$ 8,640,000



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While water in the West is usually the heart of many a disagreement, accessing additional water was recently made possible due to thoughtful agreements among land owners, community leaders, Native American tribes, and conservationists over the collection and storage of additional water drawn from the Columbia River.[11] Stakeholders to this agreement believe that there are ways in which additional water withdrawals from the Columbia River can be done to benefit both fish and farms, and provide economic development opportunities in the agricultural sector in this part of Oregon. Additional ecological benefits may include

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[9] Economic Impact Analysis, Port of Morrow. June 11, 2013. http://www.portofmorrow.com/documents/PortEcononomicImpactReport.pdf

[10] Data and inserted slide provided by the Northeast Oregon Water Users Association.

[11] "Task Force Signs Cooperative Agreement on E. Oregon Water" http://www.capitalpress.com/content/ml-columbia-agreement-021513. For information regarding this agreement, see http://orsolutions.org/osproject/crustaskforce

projects to supplement tributary flows and groundwater supplies. The next step is drawing and storing the water in a manner that meets both agriculture and conservation goals, something Oregon legislators are willing to support.

Oregon Legislature Responds: Job Creation and Conservation Working Hand in Hand

In response to many of these challenges, during the 2015 session the Legislature responded with some important natural resource sector policy victories. It increased investments in water storage, expanded state support for accelerating forest restoration and associated job creation and economic development, and made important investments in manufactured wood products, as well as the emerging market and manufacturing of sustainably harvested Western Juniper. These actions reflect Oregon's steadfast faith in the power of solutions that benefit both people and the natural systems on which they depend. Add to these victories the decision by the U.S. Fish and Wildlife Service not to list the Greater Sage Grouse, and 2015 can be regarded as a year of solid wins for Oregon's rural economies.

A GOOD YEAR FOR RURAL NATURAL RESOURCE LEGISLATION

Initiative	Description
State Support for Fed Forest Collaboration	$5 million dollars to support federal forest collaboration. These funds will enable ODF to provide the USFS with additional technical assistance, and fund collaborative processes throughout the state.
State Support for Water Development and Storage Projects	$50 million dollars to help design and build new water development and storage projects throughout the state
State Support for manufacturing and marketing of Western Juniper	$1.2 million dollars to help build the capacity to manufacture and market Western Juniper
Greater Sage Grouse	United States Fish and Wildlife Service decided not to list the Greater Sage Grouse under the Endangered Species Act.
OSU Extension Services	$6 million for OSU's Oregon Agricultural Experiment Station; $4.5 million to the OSU Extension Service; and $3.5 million to OSU's Oregon Forest Research Laboratory. Total funding for extension services is $118 million for the biennium.
Manufactured Wood Products design and use	$2.5 million to support OSU School of Forestry/U of O National Center of Excellence for Advanced Manufactured Wood Products and Design

Three important themes arise from these rural victories. First, progress on natural resource use and management issues is the product of successful collaborations between diverse stakeholders. Sustainable solutions require firm grounding in both natural and social science; both communities and nature must benefit. But collaboration takes a great deal of time and money, and at the current rate is too slow to accelerate Oregon's rural, natural resource economy.

The second important point is that, when viewed as a whole, these natural resource victories look more like 'random acts of kindness' than they reflect a comprehensive plan forward to rebuild rural economies. To be more effective, we must develop and implement a comprehensive vision for rural Oregon's future.

Lastly, given Oregon's size and diverse geography, solutions must be tailored to meet the needs of respective regions. As we work to expand the Oregon's Business Plans focus on rural economic development, we must be sensitive to these differences by listening carefully to the needs articulated by the communities we wish to serve. As we look forward, we must redouble our efforts to solutions designed to expand Oregon's natural resource economy. Expansion must occur in both an economically and environmentally responsible manner; the effects of climate change are already with us. But rural Oregonians understand these pressures better than anyone else, and they are committed to finding solutions that benefit both people and nature.

Broadening Opportunities for Rural Oregon

To help expand its focus on rural economic development priorities, in 2014 the Oregon Business Plan partnered with Business Oregon and Regional Solutions Centers to host twelve regional economic development forums across the state.[12] The forums were attended by people representing economic development organizations, local government, businesses, business groups, and education and workforce development. Our goal was to listen to economic partners and businesses to understand the challenges and opportunities in each region in order to help shape Business Oregon's new economic strategy in support of regional opportunities and priorities; inform the policy agenda of the Oregon Business Plan, and; strengthen the state and regional economic partnerships.[13]

"Participants strongly agreed with a 'grow your own' economic framework; and with most aspects of the new Business Oregon economic framework, especially:

- A focus on supporting regions and their economic priorities,
- More focus on retention, growth, and expansion efforts of existing businesses,
- Enhanced coordination of infrastructure support and financing
- Greater exposure and coordination of innovation & entrepreneurial resources.[14]

Beyond the short legislative session, much of the work ahead in 2016 will be designed to build off this information and prepare a more comprehensive rural economic development agenda for 2016. How do we ensure that workforce-training programs prepare people to take advantage of jobs created by increased investments in juniper harvest and manufacturing? Are mid-sized agriculture producers able to capture more of the value of their Oregon products? What steps can we take to promote sufficient affordable and available housing for Oregon's rural workforce? Do rural communities have sufficient access to high-speed Internet to respond to market signals and get the most from their products? With the average age of the principal farm or ranch operator approaching 60, are we doing enough to encourage a new generation to live and work on the land? To be successful in rebuilding rural Oregon's economies we must develop and deliver a comprehensive, broadly supported rural economic agenda.

While rural Oregon continues to develop the housing, education, and transportation and communication necessary to help diversify its economy, for the next decade we believe that natural resource use and restoration will continue to drive Oregon's rural economy. We need to accelerate the sustainable use of Oregon's natural resources by finding new ways to manage and protect federal lands, sustainably store water for agricultural production and groundwater recharge, and increase the value of agricultural output. Achieving these goals is possible only if we are able to bridge the gap between rural and urban created by misunderstanding and mistrust of one another's intentions and actions. All Oregonians benefit from strong local economies, healthier environments, and education and workforce training that helps us achieve both.

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[12] Regional Economic Development Forums, http://www.oregon4biz.com/dev/www/BOR/Economic-Forums/

[13] A portion of the Executive Summary has been included in this written testimony.

[14] Regional Economic Development Forums, executive summary

STUDENTS AT THE CENTER
Moving Toward Oregon's Vision for Education

Draft for Discussion at the Leadership Summit

Summary Recommendations

- Scale-up student-centered education, including classroom practices to engage and motivate learners, new models of learner-centered assessments, greater supports for students and families, and alignment of standards and curriculum across all levels of education.
- Complete the longitudinal education database to provide solid information on system performance disaggregated by race, income and region to: 1) spotlight key needs, 2) identify and share best practices, and 3) track progress towards goals.
- Increase outcome-based funding for education at all levels.
- Support and strengthen teaching in Oregon.
- Better connect education to careers through Career Technical Education (CTE) and Science Technology, Engineering, and Math (STEM) education.
- Substantially improve high school and postsecondary completion.
- Invest in early learning to ensure student readiness and close the 3rd grade reading and math gaps.

Oregon's Vision for Education

- Oregonians attain higher levels of education than ever before, in particular this includes student populations traditionally left out or behind. This elevates the life prospects of individuals and meets the competitive needs of the Oregon economy.
- All students (not just most) learn, advance, and attain the knowledge, skills, and credentials they desire.
- We accomplish this by focusing policies and systems to 1) address education gaps and disparities before kindergarten, 2) support and scale best practices in teaching and learning that are achieving desirable, equitable student outcomes and 3) connect education more closely to careers and good paying jobs in demand.

What's At Stake

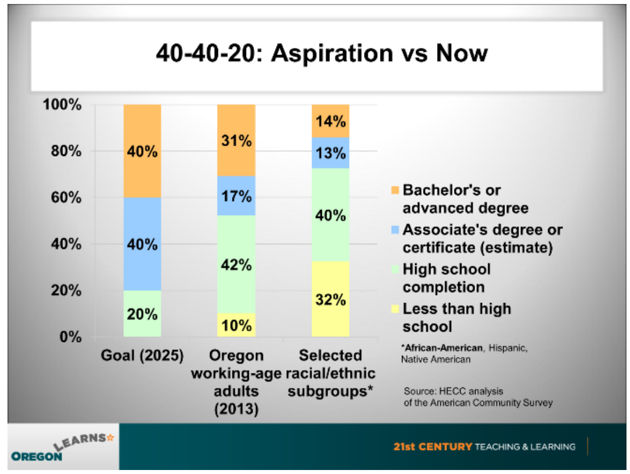
Stronger education outcomes directly determine Oregon's prospects for achieving the three key goals of the Oregon Business Plan – to grow jobs, raise incomes, and reduce poverty.

Transforming education outcomes and equity are critical to the Oregon economy and to the life prospects of Oregonians and their communities. Economic competition has increased in other states and countries, and there is a premium on education for state and regional economies, for employers, and for individuals. Education is vital to individual aspirations, stable families, civic engagement, and strong communities. Conversely, lack of education dims the prospects of individuals and increases community instability and social costs. There is a high correlation between lack of education and poverty.

Oregon's 40-40-20 Attainment Goal

Forty percent of Oregon adults should have a bachelor's degree or higher, another 40 percent should have at least an associate's degree or other technical credential, and the remaining 20 percent should have at least a high school diploma that represents a high level of academic and work readiness skills.

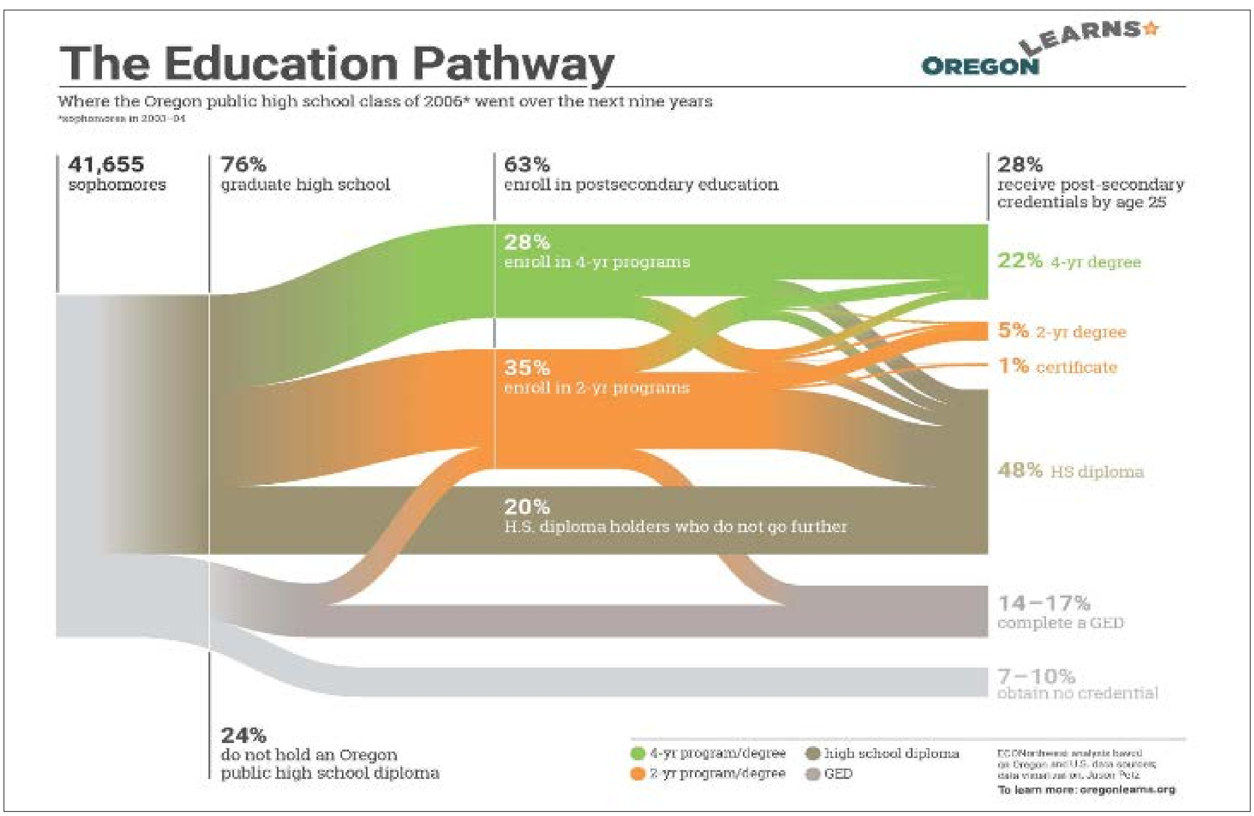
In addition to these broad goals, Oregon can achieve near-term wins by connecting education more closely to career and job opportunities in demand. Degrees and certificates associated with career technical and STEM education are in demand throughout the Oregon economy. Preparing more Oregonians for high-demand jobs that pay good wages will expand the personal prospects of individuals, keep Oregon's companies and economy more competitive, raise family incomes, strengthen the middle class, promote equity, and reduce poverty.

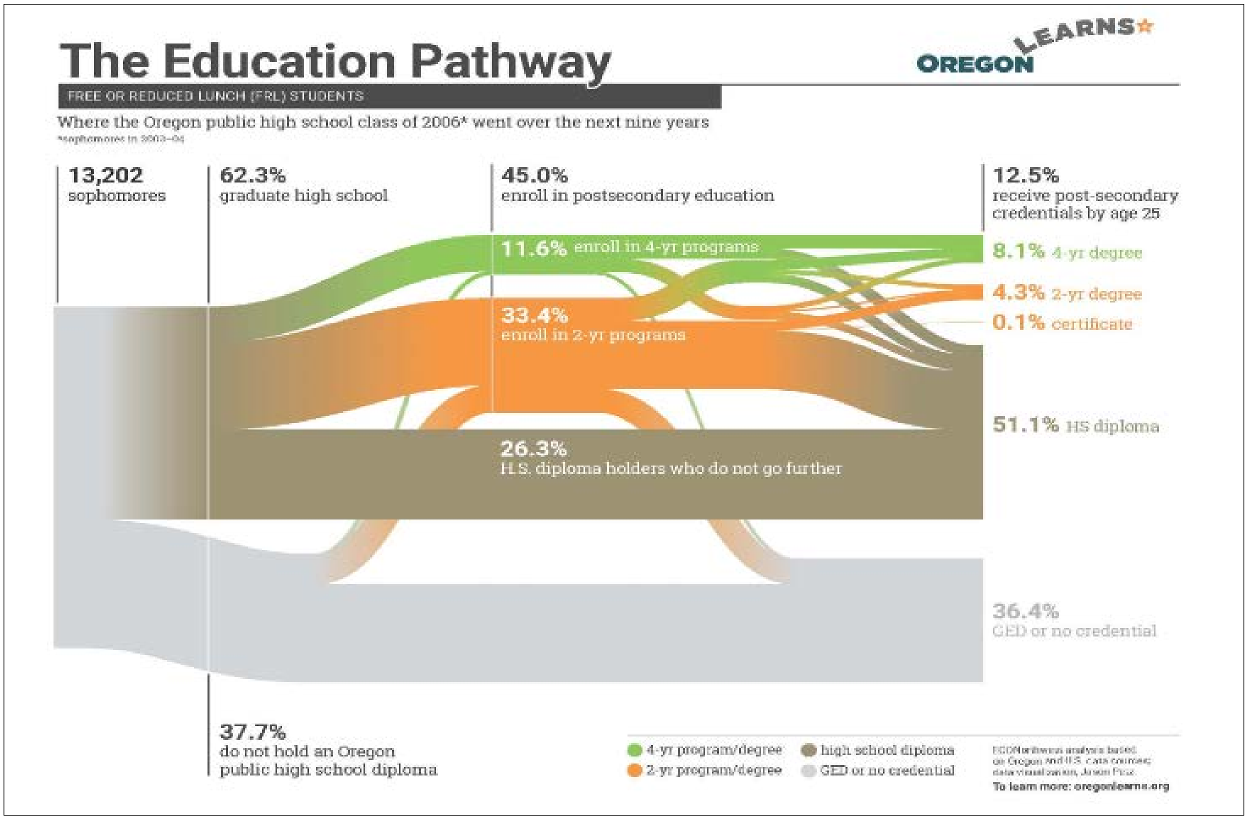


CTE and STEM education also have other benefits. They engage students, instill in them good work habits, and motivate them to stay the course. They also support fundamental skills development, including critical inquiry, logical reasoning, and creative problem solving.

Oregon's Challenge

Increasing Oregon's attainment output is a tremendous lift, and by any number of indicators we have a lot of work at hand to reach our goals. Troubling indicators include middling NAEP reading and math scores, a 69 percent high school graduation rate in four years, low postsecondary enrollment, and underwhelming postsecondary attainment rates. The figure above right illustrates the gaps between our aspirations for education attainment and the current reality, especially for student populations of color. The next figure below illustrates the pathways and attainment rates of a representative cohort of more than 41,000 Oregon students who were sophomores in 2003-04 through age 25 nine years later. Only 22 percent received a four-year credential, and only 6 percent a two-year degree or certificate. The figure on the following page shows even lower attainment for students eligible for free and reduced cost lunch at school, a marker for poverty.





The Need for New Design

Our current outcomes stem from an education system that was designed in and for an earlier time. It's still largely a time-based system that moves students along in batches with too little variation in learning pace and learning experiences suited to their individual differences. In a time-based system, too many students fall behind and drop out or move on even when they haven't mastered the material. Worse, the system often sorts students rather than challenging all of them and supporting them to meet the high standards of knowledge and skills now required of 21st century employment and life.

In this system, too many children get off to a weak start and then struggle to grow and advance, especially students from low-income backgrounds and communities of color. At-risk children who don't access high-quality early learning experiences are 25 percent more likely to drop out of school, 50 percent more likely to need special education, and 60 percent less likely to attend college.

Also, the new design that we envision eliminates the walls between academic and applied learning, between in-school and out-of-school learning, between schools at all levels, and between educators and employers. A number of community based organizations have demonstrated that they can support or achieve impressive outcomes with learners from preschool through high school, especially children from low-income homes or communities of color.

Effective community models should be included in the mix of resources funded to produce better outcomes. By the same token, employers and community organizations should be included as venues where students acquire competencies and credit for learning.

Successes to Build On

The past decade schools and teachers at various locations throughout the state have been applying and refining best practices in student-centered teaching and learning that help students excel and move forward. These practices have the potential to be scaled statewide. More recently, Oregon has built a policy, governance, and budgeting framework to support such practices, and better learning, achievement, and attainment in general from PreK through 20. As it recovers from the Great Recession, Oregon is directing more funding to education. All of these factors form a foundation for adopting and scaling a new education design that helps more students excel.

Scalable Best Practices. At the grass roots, individual schools at various locations around Oregon are breaking the old mold and employing practices that are engaging and motivating students to achieve and advance.

- At Earl Boyles Elementary in the David Douglas district, some 90 preschoolers are part of a program that brings parents, educators and the community together to help ensure students are ready for kindergarten and for success in third grade and beyond.
- At high schools from Scappoose to Medford to Madras teachers are engaging students in student-centered learning focused on high, clearly defined standards that they achieve at their own pace and in a variety of ways.
- Sherwood High School's Bowmen Fab Lab students are absorbed in hands-on learning of computer controlled manufacturing, 3D printing, and other technologies that involve job and career capabilities that pay well and are in demand.
- At Woodburn the school district is achieving some of the best high school completion rates in the state through a combination of strong community involvement, dual language learning, and student-centered teaching and learning.
- In Eastern Oregon three community colleges and Eastern Oregon University are partnering with local high schools in the Eastern Promise program, which affords high school students early college courses and credit through dual enrollment. Other regions are adopting this model.
- At Oregon Health and Sciences University the School of Medicine is shifting the bulk of medical student learning away from a traditional model based on seat time and lectures to one based on clinical simulations and other hands-on experience to achieve 43 essential competencies.

Policy, Governance, and Budgeting Framework. Since 2011 state legislators and education officials have assembled an impressive array of legislation, policies, and investments to prompt system changes and better outcomes for learners. A Chief Education Officer is now charged to oversee the formulation of education policy and investment, break down barriers to a seamless PreK through 20 system, and assure system performance and accountability. The state's investments and interests in state universities, community colleges, and student financial aid are managed by a Higher Education Coordinating Commission (HECC).

Oregon has also made real progress in shifting to outcome-based budgeting in education. This form of budgeting tailors state investments to long-term strategies and specific desired outcomes. The 2015-17 budget, for example, prioritized 1) preparing early learners for the pathway from kindergarten to third grade reading, 2) higher rates of high school and postsecondary completion, and 3) a stronger connection between education and well-paying jobs and careers. The budget that was crafted in 2015 increases base funding for public schools, funds all-day kindergarten, and targets specific outcomes. Particular targeted outcomes include 1) changes in funding formulas for higher education completion and career technical education (CTE), 2) system investments in a variety of special efforts such as collective impact hubs, data systems, culturally responsive teaching, and mentoring, and 3) short-term strategic investments such as CTE and STEM grants.

HECC adoption of a new funding formula for state universities this past April marked a significant breakthrough in outcome-based budgeting in Oregon. The Student Success and Completion Model, as it is called, shifts the basis for state university funding from enrollment—seats in a class— to better access and successful completion of degrees for resident students. The new formula directs more resources to support students and promote the timely completion of programs and degrees, with extra attention to the needs of historically under-served students. Moreover, the formula contains significant additional weights for completion of degrees in high-priority fields for the state, such as STEM, health care, and the preparation of teachers for bilingual classrooms.

A New Support Framework for Early Learners and their Families. The 2015 Legislature created a blueprint for vastly increasing the quality and capacity of publicly funded preschool programs for children from low-income families. This framework envisions higher credentials and pay among preschool staff, instructional time aligned with full-day kindergarten, and high scores on a state quality rating and improvement system for preschool programs. Funding was secured to add approximately 1,400 additional children to the program in 2016-17 with a vision of ultimately serving all of the 30,000 low-income children (under 200 percent of the federal poverty line) in Oregon who currently don't have access to a high-quality state-funded preschool program.

Dedicated Investment in Quality Teaching. Recognizing the central role of teachers in student success, Oregon created the Network for Quality Teaching and Learning in 2013 to strategically invest in activities such as mentoring, collaboration, Common Core implementation, and professional development models. The Legislature provided for continuous funding for this network indexed to the State School Fund and it authorized additional positions at the Department of Education to support educators in identifying best practices and closing the achievement gap.

Education Funding Increases. The 2015 Legislature increased Oregon's education funding significantly within the state's revenue constraints. It passed a $7.4 billion biennial funding package for K-12 education, a 9 percent increase over the previous biennium. This included a $220 million investment in full- day kindergarten.

As a down payment on the larger, longer-term funding requirements, the Legislature invested over $100 million in strengthening early childhood programs – including $27 million to expand and improve preschool, $9.5 million for home visiting services for children birth to three years old and their families, $47 million for childcare quality and access, and $9.5 million to continue the strategic investment in aligning early childhood programs and elementary school.

The session also made important new investments in postsecondary education. It gave Oregon's universities and community colleges a 24 percent increase over the previous biennium, marking a departure from a decade of stagnant state investment that has shifted significant costs to students in the form of successive tuition increases.

Student aid was significantly increased. Legislators allocated nearly $141 million for Oregon Opportunity Grants, a 23.6 percent increase over the previous biennium, to improve affordability for Oregon's highest-need students. Approximately 16,000 additional students will be served through this new investment. The session also adopted The Oregon Promise, allocating $10 million to the HECC to make community college tuition virtually free for recent Oregon high school graduates who maintain at least a 2.5 grade average. That program will start in the 2016-17 school year.

The session was good as well to the Oregon Business Plan's recommendations to better connect education to well-paying careers and jobs in demand. It more than doubled funding for CTE and STEM education (from $17 million to $35 million), and it allocated $6 million for the Oregon Talent Council, successor to ETIC, the Engineering & Technology Industry Council. Included in the package is a new funding model to award additional dollars to high schools for students completing a sequence of career technical education courses, with special emphasis on under-represented students.

The Path Ahead

At this juncture and with the framework it has in place to transform education, Oregon should shift its focus to statewide scaling of student-centered teaching and learning, as defined below, preschool through college. Elements of this effort should include 1) expanding exemplary student-centered teaching and learning where it is already established in various Oregon classrooms and schools, 2) encouraging its adoption in other schools where it is not now practiced, and 3) making it the core of study for teacher candidates in college and university teacher training programs. In addition, the scaling of student-centered teaching and learning should closely tie in CTE and STEM education as a way to better motivate and inspire students and to connect more of them to well-paying jobs and careers.

Student-Centered Teaching and Learning. This approach to pedagogy is based on the proposition that students have powerful capacity to learn wherever they are and by a variety of experience. Such learning engages and motivates students far more than passive listening. The best teachers unleash that learning capacity and motivation rather than attempting to be a conduit that "delivers" knowledge or skills. In this approach, learning is the constant and time is the variable, rather than the other way around. In this context, these are the main characteristics of student-centered teaching and learning:

- Students advance on mastery of well-defined, high standards, demonstrating at each stage that they are ready for the next.
- Learning objectives and how they are assessed are explicit and clearly understood by students.
- Students have ownership and partner in achieving them.
- Assessment – whether diagnostic, formative, or summative – is meaningful and an ongoing part of the student's learning experience.
- Grading for credit and advancement is based on demonstrated student mastery of standards.
- Students receive rapid differentiated supports based on individual needs, which include culturally responsive approaches to teaching and learning.
- Learning outcomes emphasize application and creation of knowledge plus development of important skills and dispositions.

Such teaching and learning can't flourish in isolation. Teachers, in particular, are central to this effort and should be accorded every support possible. At the K-12 level, for example, key support elements include district-level commitment, building-level leadership in instructional improvement, and teacher collaboration on standards and practices. This requires that principals and teachers themselves be part of a professional learning community and that they be afforded time in the school day for collaboration to grow in their understanding and skills and to improve practice. These support elements are equally needed at the postsecondary level.

Recommendations for 2016 and Beyond

Our recommendations are organized in two broad categories. First, we propose that the Chief Education Officer build the system-wide capacity to achieve Oregon's ambitious agenda for transformation. We envision a broad array of stakeholders joining in the effort. Second, we support three specific education investments that have been adopted as priorities by the Governor and Legislature this past year. Our recommendations here are to encourage all stakeholders to roll up their sleeves and make significant, measurable progress.

Four Recommendations to Improve System-wide Capacity

1. **Scale-up student-centered education**, including classroom practices to engage and motivate learners, new models of learner-centered assessments, greater supports for students and families, and alignment of standards and curriculum across all levels of education. For Oregon to advance at scale, we need widespread buy-in among teachers, administrators, students, parents and policy-makers about the kind of education practices we want for Oregon in the future. While there is no simple, cookie cutter approach to quality teaching and learning, some important common elements are emerging, including those identified above. We propose a broad and deep discussion be held in communities throughout Oregon.
    - Expand the conversation statewide about student-centered teaching and learning.
    - Highlight exemplars of student-centered learning already in place in Oregon. Celebrate and support principals and teachers who are leading the charge.

- Establish a coalition of educators and stakeholders to champion and accelerate statewide adoption and growth of student-centered models.

- Adopt and support implementation of a new assessment system based on the principles and recommendations advocated in *A New Path for Oregon: System of Assessment to Empower Meaningful Student Learning.* This plan, developed by state education leaders and the Oregon Education Association, contains recommendations and timelines for implementing new assessment policies and practices that would have a powerful influence in scaling student-centered teaching and learning.

2. **Complete the longitudinal data system.** We will not be able to know whether and where we are improving without a high quality system to measure learning outcomes. Oregon has made great progress in recent years, but the work is unfinished. We need a system to measure the progress of students by geography, race and socio-economic characteristics at every stage – including employment after school completion. The data system should be used to track our goals, identify promising practices, and highlight areas where we need to improve.

3. **Increase outcome-based funding for education at all levels.**

    - Develop budgets for 2017-19 to focus on 1) early learning and all-day kindergarten to assure school readiness and close the 3rd grade reading and math gaps, 2) CTE-STEM education throughout the P-20 continuum, and 3) high school and postsecondary completion.

    - Expand the application of outcome-based funding formulas to accomplish goals in high school completion, CTE-STEM degrees and credentials, and community college completion.

4. Support and strengthen teaching in Oregon.

- Increase the pre-service preparation of teachers, and also administrators, in the principles and practices of student-centered teaching, learning, and assessment.

- Support new teachers and administrators in applying these principles and practices, and other best practices, through mentoring.

- Provide educators with professional learning and leadership development opportunities.

- Encourage professional collaboration among teachers and between teachers and administrators to improve practices and student outcomes, and provide ample time in the work day for such collaboration.

- Support efforts to improve recruitment, preparation, induction, career advancement opportunities, and retention of educators.

Three Recommendations to Achieve Priority Objectives in the Next Several Years

1. **Connect education to careers through Career Technical Education (CTE) and Science, Technology, Engineering and Math (STEM).**

    - Complete Oregon's strategic plan for CTE and STEM education.

    - Build dedicated, sustained funding for CTE and STEM education at all levels of the PreK-20 continuum to expand access to all students throughout the state.

    - Focus strategic grants on innovative models using student-centered design principles.

    - Implement the Career Pathway Fund formula change for high schools to encourage completion of CTE-STEM pathways and to cover the higher costs of programs.

    - Provide support to increase access to out-of-school programs, such as internships, that motivate and prepare students for CTE-STEM fields.

- Dramatically improve math proficiency by aligning math standards and assessment across the P-20 continuum.
- Weight community college funding in the HECC allocation of state resources to promote more CTE-STEM subject enrollments and completions at community colleges. (Today, the community college enrollment based formula treats every credit-enrollment identically, regardless of whether for a high-cost CTE course or a low-cost general education course.)
- Continue to fund and build out regional STEM hubs to coordinate connections between regional partners to promote high-quality professional development, internships, and out-of-school learning programs.
- Expand the size and capacity of our CTE-STEM teacher corps at both the K-12 and postsecondary levels.
- Support the new Oregon Talent Council in its charge to highlight key career opportunities, document skill requirements to fill them, and invest in creation or expansion of degrees and credentials that address critical talent needs.
- Establish and measure clear outcomes for CTE-STEM. Tie metrics to employment in CTE-STEM jobs in Oregon. (Use 2X attainment goals in STEM statute as a starting point.)
- Implement a coordinated communications campaign to change student perceptions of CTE-STEM careers and to increase awareness of opportunities and pathways, in particular for girls and students of color.
- Continue to build the connection of CTE and STEM education to the workplace through greater engagement of employers in providing contextual learning and mentoring.

2. Substantially improve the high school and postsecondary completion rates of young adults.

High School. Elevate and prioritize improvement of Oregon's high school graduation rate. Oregon should support and scale all, or any combination, of the following:

- *Transitional intensives*. Students are at the highest risk of dropping out of high school in the first two years, especially if they start academically behind. A number of Oregon school districts have adopted proven practices (also employed nationally) in 1) identifying students not academically ready for high school, 2) providing them intensive academic support in the summer before ninth grade or in concentrated blocks of time during or after school, and 3) employing ninth grade academies which focus on the particular needs of students at that age level.
- *Engaging learning*. Student centered learning, which, by definition, engages and motivates both struggling students and adept learners, is a powerful incentive in both achievement and completion. Approaches here include 1) *active learning*, i.e., engaging students as partners in clearly understanding their learning targets and in plotting and monitoring their own learning path, 2) *varied learning activities and settings*, ranging from individual studies to group projects to service learning in the classroom, in work settings, and in the community, and 3) *use of technology and development of technology skills*, particularly in career technical education subjects, even for college-bound students.
- *Student-centered teaching.* The best teaching is not telling, but rather unlocking the power of learning (constructing knowledge) inherent in each individual through the learning formats described above. This pedagogy is emerging increasingly through research, professional collaboration among teachers and principals in schools, in-service professional development, and, to a smaller extent, pre-service teacher education.
- *Specific dropout prevention efforts*. These include mentoring and tutoring, alternative schooling, and after-school and summer programs tailored to individual student needs.

- *Accelerated learning.* Continue to support and expand accelerated learning and credit options for high school students as a way to help them achieve high standards, stay in school, smooth the transition from high school to postsecondary studies, and reduce the costs of postsecondary studies. Successful programs in place range from Advanced Placement and International Baccalaureate to concurrent enrollment and credit arrangements with community colleges and state universities, most notably dual credit and tech prep (career technical education) programs. In addition, the state supports expansion of the Eastern Promise model of early college experience for high school students through Regional Promise grants to five regional secondary-postsecondary consortia that each serve at least 10,000 students.

Postsecondary Education. Postsecondary institutions and personnel have historically focused their energies on enrollment far more than completion. That needs to change.

- *Shift of focus*. Encourage postsecondary institutions through funding formulas and moral suasion to focus on completion as much as, or more than, enrollment.
- *First-year focus*. Through increased application of counseling, mentoring, and other student services, provide intensive support to students in the difficult first-year transition into postsecondary studies.
- *Guided pathways*. As described in current literature, leading-edge community colleges are raising student completion through a "guided pathways" approach. This moves students away from fragmented or cafeteria-style course taking toward a more purposeful academic path. It includes development of a clear academic plan, a defined learning sequence, built-in advising and other student support, integrated hands-on learning and practicums, and a clear route to transfer and/or employment.
- *Voluntary Framework for Accountability*. Oregon's community college system should sign on to the VFA system, in which schools measure and improve their performance based on such indicators as student access, academic engagement, achievement, and completion.
- *Financial affordability.* For Oregon residents, hold the line on tuition increases and expand student financial aid such as Oregon Opportunity Grants and The Oregon Promise (free community college tuition) as much as possible.

3. Invest in early learning to ensure student readiness and close 3rd grade reading and math gaps.

- Align health care and education system services for learners to better meet their physical, mental, oral health and learning needs.
- In 2016, develop the case for the 2017-19 state budget to fund higher quality and capacity in preschool programs for at-risk children, as envisioned in HB 3380. This legislation envisions higher credentials and pay among preschool staff, instructional time aligned with full-day kindergarten, and high scores on a state quality rating and improvement system for preschool programs. It also envisions adding about 5,500 preschool slots to serve all 3- and 4-year-olds who live in families with incomes below 100 percent of the federal poverty line.
- Thereafter, the state should develop an investment plan—over biennia—to fully implement the state's vision to serve all children below 200 percent of the federal poverty line in higher quality, mixed-delivery programs.
- Invest in culturally responsive approaches and partnerships in the effort to close 3rd grade reading and math gaps.
- Document, replicate, and scale practices from a number of school districts in Oregon (for example, targeted interventions, dual language instruction) that have been successful in raising students' numeracy and literacy through third grade.

HEALTH CARE STRATEGY RESET

Draft for Discussion at the Leadership Summit

Summary Recommendations

- Maintain the momentum for health system reform, including the continued integration of physical, behavioral, and dental care through Oregon's Medicaid Coordinated Care Organizations, as well as the cost and quality initiatives spearheaded by the Oregon Health Leadership Council.
- Work across sectors to find sustainable short- and long-term funding strategies to support Oregon's Medicaid program and other essential state services.
- Evaluate the impact of the Affordable Care Act on insurance coverage options and affordability, and develop targeted initiatives and policies to further Oregon's health reform progress, including a high-value small business health insurance exchange in 2017.
- Engage employers, schools, civic organizations, health care entities, and other partners in community level collaborative efforts across Oregon to maximize resources targeting the underlying causes of poor health and health disparities among Oregonians.
- Maximize collaborative efforts between Oregon's health care and education systems to improve the health of our children and their readiness to learn.

Background

Health care reform was first introduced as an Oregon Business Plan initiative at the 2004 Oregon Leadership Summit. Oregon's employers recognized that our health care system was not delivering sufficient value. The U.S. and Oregon were spending a much higher share of GDP on health care than other developed nations, with health insurance premiums growing at an unsustainable rate. Quality of care was inconsistent, and many were left out. Seventeen percent of Oregonians were uninsured at the time.

Oregon has made substantial strides in health care reform in the last decade. Our public and private sectors have worked together to improve access to high quality health care while curbing the growth of costs. Under federal and state reforms, approximately 95 percent of Oregonians are insured today, an increase of 10 percent from a decade ago. Oregon has some of the lowest rates of avoidable hospitalizations in the country and is outperforming national averages on a notable number of widely used health care quality measures such as breast cancer screening and appropriate use of imaging for lower back pain. Collaborative work between the health care industry and the Oregon Health Authority has yielded notable improvements in how health data is used to improve health care decision making.

Almost all of our Medicaid enrollees are now receiving their health care through Coordinated Care Organizations (CCOs), where the funding for physical, mental, and dental health has been aligned to provide integrated and improved care. Over half of all Oregonians are having their care coordinated through patient-centered primary care homes, which perform highly on quality-of-care measures. Data have indicated a reduction in per capita emergency room visits in recent years while primary care visits have been increasing, indicating that Oregonians are starting to receive better and less costly preventive care and care management services.

Emergency Department Information Exchange (EDIE) and PreManage

Emergency Department (ED) visits, with high overhead costs and reliance on advanced technology, are a significant driver of health care costs in Oregon. Another associated cost driver is the lack of care coordination across health care settings, especially for patients who are high utilizers of care, leading to higher use of the emergency department.

Recognizing the cost implications of ED use, Oregon built off recent successes in Washington state and began its own efforts to promote the statewide adoption of EDIE, or Electronic Department Information Exchange, to address several aims, including:

- Building consensus for all hospitals to perform ED notifications;
- Minimizing high ED utilization costs;
- Improving care coordination and management; and,
- Abetting anticipated rises in ED utilization for primary care by the new Medicaid expansion.

The OHLC and the Oregon Health Authority (OHA), and the Oregon Association of Hospitals and Health Systems (OAHHS) worked with the vendor Collective Medicaid Technologies (CMT) to implement electronic notifications to all hospitals across the state through EDIE. Immediate benefit has been realized through sharing real-time ED alerts and notifications across health systems. To enhance the the "EDIE Utility", OHLC and CMT worked with hospitals to expand the notifications to include inpatient visits along with ED events. Today, all 59 hospitals in Oregon are receiving EDIE notifications which include all Emergency Department visits and Inpatient Admissions in Oregon and Washington. ED physicians report significant value in seeing a broader picture of patients' utilization.

The EDIE Utility also has provided a foundation for a complimentary product, PreManage,that allows hospital visit data to be pushed to health plans, CCOs and provider groups on a real-time basis for specified member or patient populations. Early adopters have reported that PreManage has facilitated their ability to implement and strengthen care coordination processes and ED utilization in their high needs, high utilizing population. One primary care practice has reported a significant reduction in readmissions by knowing "real time" when a patient has been discharged from the hospital and subsequently following up the same day with the patient.

EDIE Goals

- Continue trend of decline in ED utilization by 1 percent from visits in 2013 ($12 million savings).
- Match State of Washington ED utilization rates per 1,000 population (2011 data) by the end of 2016. This would represent a 6.3 percent improvement ($76 million savings).
- Meet the Oregon Health System Transformation ED visit benchmark (ED admissions per 1,000 member months) by the end of 2016 for the Oregon Health Plan patient population. This would represent a 12 percent decrease in ED utilization from 2013.

But there is more to do. In comparison to other states, Oregon is in the middle of the pack on health outcomes and below the national average on some commonly cited quality-of-care measures, such as well care visits for children ages 3 to 6 and for adolescents. There are wide disparities in health outcomes between non-Hispanic whites and other racial and ethnic groups, and between rural and urban residents. Costs of care in Oregon vary significantly, with some clinics incurring costs 75 percent higher than others in the state.

Providers and insurers are reporting an uptick in emergency room visits following the expansion of health insurance coverage. And while we saw health care insurance premiums leveling out in recent years, rate increases last year indicate that the full impact of federal insurance reforms on Oregon's market are still unclear. Insurers report that prescription drugs are increasingly absorbing available resources and threaten the sustainability of health care cost growth. And we have much work ahead of us to to improve and align the dashboards and metrics we use to evaluate progress and guide improvement efforts.

We must stay the course. Improving the effectiveness of our health care system and reducing the cost burden is crucial to the health and productivity of Oregonians and our state's economic growth. In order to realize the full potential of current collaborative efforts, we have to maintain focus and momentum on reforms already underway, including the full integration of services under the Medicaid CCOs and the health system reforms spearheaded by the Oregon Health Leadership Council.

Additionally, we need to focus our collective efforts – health care industry and employers included – to change the underlying determinants of poor health. Oregon's communities are developing local collaborative efforts through which employers, insurers, health care providers, school systems, civic groups, and public sector agencies are investing resources to improve the health and well-being of their communities. In the coming years, Oregon's business and health care communities can be key leaders in this work, as well as in emerging efforts to align early childhood learning with health reform to give Oregon's children a healthy, well-prepared start in life.

Progress on Oregon Business Plan 2014 Goals

Goal	OR	US	Year	State Rank
Uninsured rate of 5% by 2017	9.7%	11.7%	2014	21
Per capita expenditures on personal health care in lowest 10% in the U.S	$5,842	$5,973	2012	23
Total average contribution for private, single person coverage in lowest 10% in U.S.	$5,340	$5,500	2014	19
Healthiest citizens in the U.S. by 2020	27th	-	2014	27

Note: Recent estimates based on additional state data indicate Oregon uninsured rate is 5.6%.

State Rank scale: 51 Worst State – 41 – 31 – 21 – 11 – 1 Best State

Source: ECONorthwest; Additional sources

Proposed Oregon Business Plan Health Vision

- The people of Oregon and our communities will be the healthiest in the nation because we view health and well-being as a core value, committing energy and investments to that end.
- We will have an efficient, competitive, and financially sustainable health care market that supports the health of all Oregonians and delivers high quality health care at an affordable price.

- The Oregon business climate is enhanced and more competitive because we all are healthier; employees are more productive; and the per capita cost of health care in the state is one of the lowest in the nation and most financially sustainable over time.

Goals to Achieve our Vision

1. Affordable insurance coverage options are available to all Oregonians through innovative market solutions that align incentives for improved health, high quality care, and sustainable cost growth.
2. All Oregonians have access to appropriate, high quality, coordinated care that supports their physical health, as well as mental health and social well-being.
3. Consumers, employers, providers, and insurers have easy access to the right tools and information to make the best health, purchasing, clinical, and coverage decisions.
4. Employers and the health care industry work collaboratively with partners throughout the state to create healthy communities.

Health Care and the Oregon Business Plan: 10 Years of Reform

Both the cost of health care as well as the quality of the health care delivered are important for business and all Oregonians. Unchecked benefit cost growth can hurt Oregon's competitiveness in a global market, reduce funds for business investment, and dampen economic growth. Inadequate insurance coverage and low quality health care can contribute to poor employee and dependent health and wellness, hurting productivity. In addition, the high cost of publicly financed health care diverts public resources needed for investment in education and transportation.

As Oregon's employers and their employees pay the bill for the cost of health care both directly and through their tax dollars, the business community is uniquely positioned to provide leadership and a strong point of accountability for health care reform.

***Successes*.** Since health care was added to the Oregon Business Plan agenda, the state's business community has partnered with health care providers and insurers, state and local government, and civic leaders on many innovative reforms. Employers were at the table when major reform policies were developed through the Oregon Health Fund Board, the Oregon Health Policy Board, and numerous committees. They created the Oregon Health Leadership Council (OHLC) to champion collaborative reform efforts across employers, insurers, providers, and the state. These reforms have focused on increasing the availability of affordable coverage options, improving the quality of care delivered, and curbing cost growth. Some highlights of Oregon's reform achievements include:

- **Supporting affordable insurance coverage.** Oregon's rate of uninsured has dropped from 17 percent to less than 6 percent in the last 10 years. This is partially due to successful collaborative efforts that sustained funding for the Oregon Health Plan during economic recession and expanded coverage to children under the Healthy Kids program. Most recently, state and federal reform efforts under the Affordable Care Act produced the greatest increase in insurance coverage in decades. Oregon's employer community was an active supporter of many of the policies that led to the reduction in the uninsured, including Oregon's most recent Medicaid expansion and the creation of a health insurance exchange.
- **Making the most of our public investment in health care by improving quality while slowing cost growth.** The business community and the Oregon Health Leadership Council supported the implementation of the coordinated care model through Medicaid Coordinated Care Organizations (CCOs) and our Public Employees Benefit Board (PEBB). Early indicators pointed to decreased emergency room visits per enrollee and increased primary care visits while holding down costs to the approved 3.4 percent annual growth negotiated under the state's federal Medicaid waiver. PEBB is demonstrating similar promising trends.
- **Using innovative health care purchasing and delivery system redesign to create incentives for high quality care while holding down costs.** Private employers are increasingly driving reform through

benefit offerings that create greater aligned incentives among consumers, providers and payers (e.g., value-based benefit design, defined contribution for employee insurance, and greater choice of health plan packages.) We are seeing improvements in quality-of-care measures over time in our commercial insurance market. Initiatives championed by the Oregon Health Leadership Council, insurance carriers, providers, and the Oregon Health Authority have tested new payment and care coordination models with promising quality and cost outcomes.

- **Making every health-related decision an educated decision.** Insurers, providers, state agencies, and others have engaged in numerous collaborative efforts to align performance metrics across the system and provide meaningful cost and quality information to consumers, purchasers, and providers. Some strategies have focused on improving consumer health literacy and supporting more informed decision making (e.g. Advance Care Planning, palliative care). Additionally, the health care industry, in collaboration with the Oregon Health Authority, has facilitated considerable progress in streamlining the administrative data that support care delivery (e.g., billing, payment, benefit eligibility) with the goals of reducing costs and improving the efficiency of care.

See the following timeline of Oregon's private and public health reform initiatives over the past decade. For additional information on Oregon's health reform efforts, please see the readings at the end of this document.

Challenges

While we have made some clear advances in coverage, cost, and quality, there is still much to do. Health care expenditures equate to 17 percent of our gross state product. On many health outcome indicators, we are not leading the nation. We need to maintain focus on work that we've begun, building on successful collaborations and expanding the impact of our system improvement efforts.

Key challenges for our state:

- **Oregon is not as healthy as we think**. Over 17 percent of Oregonians smoke and 1 in 4 is obese. Tobacco and obesity are the two most preventable causes of death and disease, costing Oregonians billions of dollars a year in medical expenditures and lost productivity. Oregon is ranked 23rd and 28th on binge drinking and drug poisoning deaths respectively. Oregon also has the highest rate in the country of adults reporting poor mental health.
- **The full impact of federal reform is still unclear.** The federal Affordable Care Act changed many aspects of both public and private health insurance. The full effect of those changes on Oregon's insurance market is still unknown. While rates have increased more slowly in recent years, insurance premium rates in the individual market have increased substantially this year. Oregon's health insurance exchange launch was tumultuous, leading to the transfer of operations from Cover Oregon to the Department of Consumer and Business Services (DCBS).

Over a Decade of Health Care Transformation

STATE AND FEDERAL POLICY

OHP Standard benefit package with reduced benefits is created with higher copayments and requires premiums.

Legislature establishes Medicaid managed care and hospital provider taxes (HB 2747) to begin in 2004.

Measure 30 intended to help fund state budget fails. OHP Standard closes to new enrollment July 1, 2004 and benefits are reduced and partially restored.

Oregon Health Fund Board created by SB 329 with support from the business community. Introduces Oregon Health Authority and a health exchange concepts.

OHP Standard lottery opens to maintain enrollment within available funding.

The Oregon Legislature also enacts HB 2116 creating the Healthy Kids program, covering children up to 300% FPL.

Oregon Legislature passes HB 2009, creating the **Oregon Health Authority, the Oregon Health Policy Board**, an enhanced rate review process overseen by DCBS and direction on an array of cost and quality initiatives.

Federal Affordable Care Act is signed into law.

2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010

The **Oregon Business Plan Health Care Initiative** was introduced at the 2004 Leadership Summit.

Oregon Health Policy Commission recommends **electronic health records and data exchange** in Oregon, community health collaboratives, and an **Oregon Health Insurance Exchange.**

OAHHS and OHPR develop websites to provide comparative information on **hospital prices and quality.**

The **Oregon Coalition of Health Care Purchasers** started to use Evalue8, which collects health plan process and outcome measure data.

The **Oregon Health Care Quality Corporation** begins its quality measurement and reporting work.

The Oregon Health Leadership Council (OHLC) formed at the request of four major business groups.

The OHLC's **High Value Patient Centered Care Demonstration** begins, a two year multi-payer medical home effort: 14 medical groups and 3,600 high-risk patients.

OHLC collaborative launches effort on **administrative simplification** with insurers, providers, and the Oregon Health Authority.

OHA develops the **Patient Centered Primary Care Model** in collaboration with the provider and insurer community. Over half of Oregonians will be receiving care through a certified medical home by 2015.

PEBB, OEBB, EVRAZ, Moda Health, and Legacy Health develop **value-based benefit plans.**

KEY PRIVATE AND PUBLIC COLLABORATIVE EFFORTS

STATE AND FEDERAL POLICY

2011

The Health Care Transformation Act (HB 3650) passes authorizing the development of **Medicaid Coordinated Care Organizations (CCOs)** and SB 99 authorizing Oregon's health insurance exchange.

2012

Oregon's federal waiver to implement the CCOs approved providing **$1.9 billion in transformation funding** over five years.

2013

Initial implementation of CCOs begins.

2014

ACA Medicaid expansion and coverage through Cover Oregon begins; The Oregon Medical Insurance Pool ends.

2015

The operations of **Cover Oregon** are transitioned to the Department of Consumer and Business Services.

2016

2017

DCBS to begin Oregon's Small Business Health Options Program (SHOP).

Oregon's waiver to expire; initial negotiations starting currently.

KEY PRIVATE AND PUBLIC COLLABORATIVE EFFORTS

2011

Working with American Specialty Health, the OHLC worked to find opportunities to improve quality of care, avoid the use of **unnecessary imaging tests.**

2012

Health plans provide access to **OneHealthPort** providing one secure sign-on to health plan websites for administrative transactions.

OHLC launches a two-year pilot initiative to offer direct access to physical therapists for patients with **acute low back pain.**

OHLC, March of Dimes, and OAHHS champions "Hard Stop" Initiative championed: 90% of Oregon's birthing hospitals have adopted a policy on early elective, non-medically necessary deliveries before 39 weeks gestation.

2013

OHLC, OHA, and the Governor's Office develop a **Medicaid funding strategy** to fully fund the Medicaid budget for 2013 to 2015.

2014

Implementation of **Emergency Department Information Exchange (EDIE) and PreManage** allows the exchange of emergency department and inpatient hospital data for high utilizers of ER services.

Oregon Healthiest State Initiative kicked off with broad support by business, nonprofit, and the state leadership.

2015

OHLC **Advanced Care Planning** pilot to build sustainable financing for advanced care consulting to patients with terminal illness.

In the upcoming year, DCBS will be developing a small business exchange (Small Business Health Options Program or SHOP) for 2017 that ideally will provide new value to Oregon's small employers looking for quality insurance choices for their employees. Additionally, the federal "Cadillac Tax", an excise tax on higher cost employer-sponsored health coverage scheduled to take effect in 2018, has the potential to increase public and private employer insurance costs.

- **A state budget deficit looms ahead.** We are faced with a Medicaid structural budget deficit in future years due to a number of reasons. The Affordable Care Act authorized 100 percent federal funding initially for the 2014 Medicaid expansion to low-income adults, but this funding decreases to 90 percent by 2020. In addition, Oregon's federal waiver that expires in 2017 provided one-time funding. And lastly, a hospital tax that has been in place in various forms since 2003 is next set to expire in 2019. Assuming no intervening change in the course of these three dynamics, the Oregon Health Authority projects a $500+ million budget gap in the 2017-2019 biennium that will increase in future biennia.
- **We continue to need innovative approaches to address the root causes of poor health and high costs.** We recognize that there are wide ranging disparities in many health indicators for some groups of Oregonians, based on race, ethnicity, poverty, age, and other factors. More providers in rural regions of Oregon are seeing notably lower quality of care scores than those in the Portland metropolitan area. There is strong support for additional investment and experimentation around new integrated models of care that target these inequities in medical care, behavioral health, social well-being, and environmental factors.
- **We need to truly align health system metrics.** Although not for a lack of effort, Oregon lacks alignment across public and private payers in dashboards and quality metrics that should be valuable resources for evaluating systems, targeting reform efforts, and rewarding successes. And in many cases, consumers do not have clear and useful data on which to base health care decisions.

Proposed Health Reform Priorities

Oregon's employer community believes the accomplishments of the last decade and work currently underway is on the right course. We have witnessed an extraordinary level of collaboration between public and private sectors at the state and local level. To continue the momentum in 2016 and beyond, we propose a two-prong strategy.

1. ***We must stay the course***. Improving the effectiveness of our health care system and reducing the cost burden is crucial to the health, productivity, and financial stability of Oregonians. This focus should continue to be a priority for collaborative efforts among employers, the health care industry, state policymakers and others. This work includes:

   - The integration of physical, mental, and dental health services under CCOs to fully realize the promise of high quality care at a sustainable cost to Oregon taxpayers. The focus of the CCO initiative on improved quality measurement and aligning incentives should be maintained.
   - Cost and quality initiatives spearheaded by the OHLC and others, including continued efforts to improve the use of electronic health information, targeting areas of high cost and low value, and truly aligning outcome metrics and dashboards across stakeholders.

   We will need to define key policies to build on and sustain our progress and address upcoming challenges. Such efforts include working across sectors to address state funding challenges for Oregon's Medicaid program and other essential services. Additionally, we need to evaluate the impact of federal reform on Oregon's insurance market and identify areas of concern and further development. In particular, there will be work needed to shape a small business insurance exchange that will add value and reduce costs for small employers and their employees.

2. ***We need to focus on supporting health and wellness, the underlying determinants of health, and health disparities***. In order to build a healthy Oregon for today and future generations, we need to do this with the same focus and attention we give health care delivery reform***.*** We can do this in two ways.

   First, the business community and the health care industry should embrace the Oregon Healthiest State initiative, Blue Zones Initiative, and other similar efforts. Communities need to come together and rally around key local health goals, identify disparities, and focus on clear strategies to improve the health and well-being for all community members. Employers and the health care industry are strong community leaders that can make a difference “upstream” in order to improve health and ultimately reduce health care costs.

   Second, we can collectively advance the health and well-being of Oregon’s children and their families by leveraging the hard work that created Oregon’s Medicaid Coordinated Care Organizations and Early Learning Hubs. New alignment efforts between early childhood learning, K-12 education, and health care communities have surfaced with the goal of giving Oregon’s children a healthy, well prepared start in life. It makes sense for the employer and health care communities to actively support this work as healthy children learn better and will be Oregon’s entrepreneurs, policymakers, workforce, and parents of tomorrow. Through innovative approaches that align funding and integrate services, our medical and early education systems can identify children’s health, learning, and social needs early, connecting them to services before and beyond the first day of kindergarten.

Please see fact sheets that follow on promising community approaches to health and well-being in Oregon. These are followed by references for further reading on health care reform.

Umatilla County Wellness HUBs

MISSION

Empowering students to be healthy and ready to learn by ensuring they have access to high quality healthcare services and education.

GOALS

- Increased collaboration between community agencies that serve schools
- Decrease in unmet healthcare needs of students in Wellness HUB regions
- Promotion of healthy lifestyle choices that will last a lifetime through comprehensive health education
- Increased school attendance, increased 3rd Grade Reading rate, increased high school graduation rate

WHY

If students are healthy and receiving high quality care and health education, they are more likely to attend school and perform better academically.

WHAT

Wellness HUBs are a network of educational and healthcare services including physical (primary/urgent care), oral (dental screenings and sealants), mental (counseling and preventative services) and the CARE program. Each school within the HUB will have a dedicated space for HUB staff & partners to provide on-site care & services to students, staff, and, if the school so chooses, community members.

Services may include: sports physicals, immunizations, urgent care for benign, acute ailments such as strep throat or pink eye, primary care if needed, referrals to specialists including dentists, mental health counseling and substance abuse and addictions counseling as needed.

Wellness HUBS integrate neighboring school districts, the local public health department and community healthcare partner agencies to meet student healthcare needs by bringing services to them, AT THE SCHOOL.

WHO

The Wellness HUBs are a partnership between Umatilla County Health Department, the InterMountain Education Service District, Greater Oregon Behavioral Health, Lifeways, and school districts.

Each Wellness HUB will be staffed and coordinated by a Nurse Coordinator employed by IMESD, supervised by Umatilla County Public Health and who works closely with schools and community partners. The Nurse Coordinator will be responsible for coordinating healthcare service providers, providing direct nursing care and in-class health education and working with community partners to identify needs and ensure success of Wellness HUB efforts.

WHERE

There are THREE proposed Wellness HUBs within this partnership:

NorthEast: Athena-Weston, Helix, Milton-Freewater

Central: Mission, Pendleton, Pilot Rock, Ukiah

NorthWest: Stanfield, Umatilla, Echo

WHEN

To build capacity and develop relationships in the communities we serve, the first Nurse Coordinator is being hired. This first year will focus on working with community partners and the school districts to identify needs and strategize how to work together to best meet those needs.

BLUE ZONES PROJECT®
by HEALTHWAYS

Helping Oregonians Live Longer, Better: The Blue Zones Project® in Oregon

On the Gallup-Healthways Well-Being Index®, Oregon's well-being ranks No. 27 among all 50 states. That puts us in the middle of the pack, but the promise of a growing economy and a good quality of life for all Oregonians requires that we do better. Cross-sector statewide initiative Oregon Healthiest State was founded to ignite a movement that helps do just that by identifying and expanding what's working to improve health in Oregon.

As part of this effort, the initiative inspires partners across Oregon -- employers, schools, public officials and community members -- to create and sustain healthy environments to support healthy lifestyles. Lead funder, Cambia Health Foundation brought Blue Zones Project to Oregon in collaboration with Healthways, Inc. and Blue Zones, LLC to support Oregon Healthiest State at the grassroots level.

Blue Zones Project is a community-by-community well-being improvement initiative that aims to lower community health care costs, boost civic engagement and increase employee engagement through lower absenteeism and higher productivity. Blue Zones Project is based on principles developed by Dan Buettner, National Geographic Fellow and New York Times best-selling author of "The Blue Zones" and "The Blue Zones Solution." Blue Zones are places in the world where the environment surrounds residents with healthy options and supports inspiring them to live longer, better.

The project differs from diet and exercise programs, which narrowly focus on physical health and require participants to consciously change their behavior. Instead, the project works to optimize where we spend time -- our homes, schools, worksites, communities and peer groups -- to nudge people to improved well-being.

To date, 28 communities in the United States have utilized the approaches and support offered by the Blue Zones Project. Here in Oregon, Klamath Falls is the first Blue Zones Project Demonstration Community. Sky Lakes Medical Center, a community champion, answered Cambia's funding match to support the local initiative. Guided by a comprehensive community-wide assessment conducted in the spring, Klamath Falls based Blue Zones Project staff are already working with more than 120 volunteers from businesses, schools, government, healthcare, faith-based, and non-profit sectors to develop and implement a blueprint for increasing community-wide well-being. While early sector engagement work is already taking place, a kickoff next spring will launch the initiative and encourage individuals, families and organizations to get involved.

Soon, a Blue Zones Project team dedicated to statewide efforts will announce the selection of a second Demonstration Community in Oregon. In addition to this community focused work, the state team is conducting outreach to worksites and schools throughout Oregon, providing tools and support to remake environments for better well-being.

While the work is just getting underway, excitement is building. Join the movement to make Oregon the healthiest state in the nation! For more information on how Blue Zones Project in Oregon can help you transform the well-being of your worksite, school, restaurant, grocery store or community, visit bluezonesproject.com.

Brought to Oregon by CAMBIA™ health foundation

Further Reading on Health Reform

Insurance Premium Growth
Between 2003 and 2010, employer sponsored health plans for individuals and families rose 5 percent to 6.5 percent on average a year in Oregon and nationally. C. Schoen, D. C. Radley, and S. R. Collins, *State Trends in the Cost of Employer Health Insurance Coverage, 2003–2013,* The Commonwealth Fund, January 2015. http://www.commonwealthfund.org/~/media/files/publications/issue-brief/2015/jan/1798_schoen_state_trends_2003_2013.pdf?la=en

Insurance Coverage
In 2004, 17 percent of Oregonians were estimated to be uninsured. Most recent estimates of the uninsured are as low as 5.6 percent. *Trends in Oregon's Health Care Marketplace and the Oregon Health Plan*, Oregon Health Policy and Research, January 2005, and Oregon Health Authority and OHSU, Impacts of the Affordable Care Act on Health Insurance Coverage in Oregon, Feb. 2015. http://www.ohsu.edu/xd/research/centers-institutes/center-for-health-systems-effectiveness/upload/Health-Insurance-Coverage-in-Oregon-County-Results.pdf

Health Care Quality Metrics
For Oregon Health Care Quality Corporation reports, see: http://q-corp.org Selected Qcorp data points used in this paper include:

- Cost of care in Oregon varies significantly by clinic, with some clinics incurring costs 75 percent higher than others in the state, after controlling for differences in age, gender, and acuity.
- Our more rural sections of Oregon are seeing notably lower quality of care scores than the Portland metropolitan area. Portland is outperforming on 21/21 (or 100 percent) of the quality measures reviewed compared to the more rural areas of the state.
- Patient Centered Primary Home Clinics (PCPCHs) are generally showing higher rates on quality of care measures. In Q Corp's annual Statewide Report, PCPCHs had higher rates in 9 out of 11 measures studies, and in seven of those cases PCPCHs had statistically significant higher results.
- The Commercial market is generally seeing improvements in quality of care metrics over time. Twenty out of twenty-nine measures saw improvements year-over-year. (statistician note: this is comparing July 2012 – June 2013 to July 2013 – June 2014)
- Oregon is outperforming national averages (using the HEDIS national mean to compare) on 8 out of 14 measures. Most notably, the state of Oregon is underperforming (compared to HEDIS averages) on two measures focused on LDL screening, well care visits for adolescents and children ages 3 – 6, and on chlamydia screenings.

System Reform Resources

- For Oregon Health Leadership Council initiatives, see www.oregonhealthleadership.org
- For Oregon Health Authority Coordinated Care Progress reports, see: http://www.oregon.gov/oha/Metrics/Pages/HST-Reports.aspx
- For state comparisons of health system reform metrics, see The Commonwealth Fund's, *Aiming Higher: Results from a Scorecard on State Health System Performance, 2014.* http://www.commonwealthfund.org/publications/fund-reports/2014/apr/2014-state-scorecard

Oregon Healthiest State Initiative: *The State of Health in Oregon: Progress and Opportunities*, November 2015. http://orhealthieststate.org/wp-content/uploads/2014/10/2015-State-of-Health-in-Oregon_Progress-and-Opportunities_FINAL.pdf

OVERHAULING PUBLIC EMPLOYEE COMPENSATION

Draft for Discussion at the Leadership Summit

Summary Recommendations

- **Advance the principle that increases in public employee compensation should keep pace with, but not exceed, the rate of compensation increases in the private sector workforce**. This principle will ensure that revenue dividends from an expanding economy are not consumed by extraordinary public sector payroll costs and will enable the state, schools and local governments in Oregon to invest in programs that expand opportunity and promote prosperity.
- **Renew efforts to moderate future cost increases for the Public Employees Retirement System (PERS)**. Follow the prevailing practice in other states by which public employees share the responsibility for supporting their pension benefits. Consider proposals for employees to share in the cost of restoring the system's fully funded status.
- **Monitor progress toward controlling employee health care costs to avoid triggering the pending "Cadillac tax."** Consider alternatives if government plans fail to control costs and face the imposition of the tax in 2018.
- **Promote transparency and accountability in collective bargaining and managerial pay practices**. Establish mechanisms to require consideration of the effects of salary and benefit commitments on the ability of governments to improve and expand public services and investments.

Background

Five years ago, then Gov. Ted Kulongoski's Reset Cabinet warned of steep increases in public employee compensation costs, which were projected to exceed state revenue growth by three to four percentage points a year for the better part of the current decade. The effects of these increases, as the Rest Cabinet foresaw, would be to force the state, schools, and local governments to divert revenue gains from a recovering economy into sustaining existing payrolls – rather than expanding investments in education, infrastructure and other drivers of economic growth and prosperity. The imperative then was to address this challenge in ways that would allow the state and its school districts in particular to move beyond "budgets of necessity" to "budgets of opportunity."

The Reset Report identified three drivers of extraordinary public employee compensation costs: 1) the need to boost funding for PERS public employee retirement benefits, placing the full burden of financing those benefits on employers, 2) persistent hyper-inflation in employee health benefit costs, and 3) the practice of negotiating wage increases and longevity-based pay scales without fully accounting for rising benefit costs, the capacity of governments to afford such increases, or the impact of costs on the provision of public services.

Finally, the report offered solutions to mitigate these cost drivers without reducing total compensation or the take-home pay of public employees.

Five years later, we find that the state, our schools, and local governments have managed to avoid the most extreme impacts of previously predicted payroll cost increases by deferring their effects rather than addressing their causes. The bill for underfunded retirement benefits and rising health care costs is now coming due.

Public Employee Retirement System (PERS). In 2013, Gov. John Kitzhaber engineered a "grand bargain" that avoided the imposition of steep payroll cost increases for PERS. The centerpiece of his PERS reforms reduced future cost-of-living increases for retired and active employees. In 2015, the Oregon Supreme Court overturned this reduction in benefits (Moro v. State of Oregon). As a result, PERS officials now predict that the system's costs will add as much as three to four percent to the payroll costs of the state, schools and local governments in each of the next three biennial budget periods – for a total increase of nine to twelve percent of payroll over the next six years. Under the current system, these costs will be borne in full by public employers, unless employees begin contributing to their pension plans as is the prevailing practice in other states.

Health Care Benefits. State health plan administrators have made progress in controlling costs in recent years, but their counterparts in K-12 education have yet to show similar success. In both sectors, they will be hard pressed to keep cost increases in line with those of the Oregon Health Plan, which has become the state's benchmark for cost containment success. If they fail, the ACA's new Cadillac tax will compound the costs of maintaining current benefits.

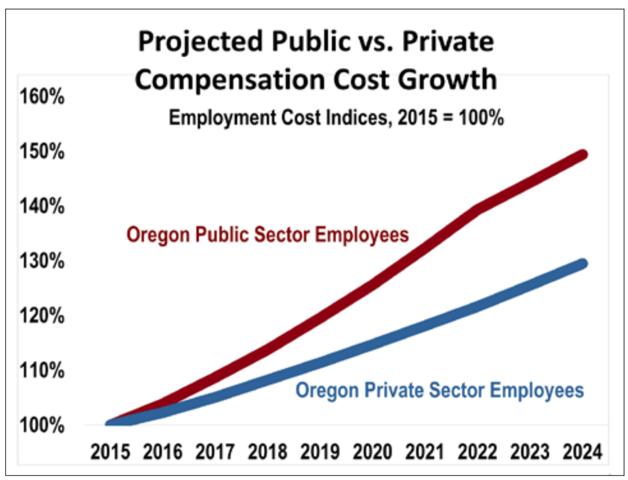
Public employee compensation should advance in step with, but not outpace, the rate of compensation increases in the private sector workforce.

Enabling continued investments in "budgets of opportunity" will require a renewed effort to control public employee payroll costs in an equitable and effective manner. To that end, a principle advanced in the 2010 Reset Report remains just as valid today: Public employee compensation should advance in step with, but not outpace, the rate of compensation increases in the private sector workforce.

Doing so will better align the cost of sustaining current service levels with the growth of public resources and thereby enable new investments in education and infrastructure that can promote opportunity, progress and prosperity.

The Challenge Now

Oregon's public employers face extraordinary payroll cost increases, beginning in 2017, when rate increases required to restore funding for existing PERS benefits are due to take effect. These increases, illustrated at right, will raise the average employer contribution rate for PERS from 18 percent of payroll to 27 to 30 percent, depending on the fund's investment performance from 2017-19 through 2021-23. For school districts, the rates will be even higher, because schools employ more career employees with longer longevity rates.

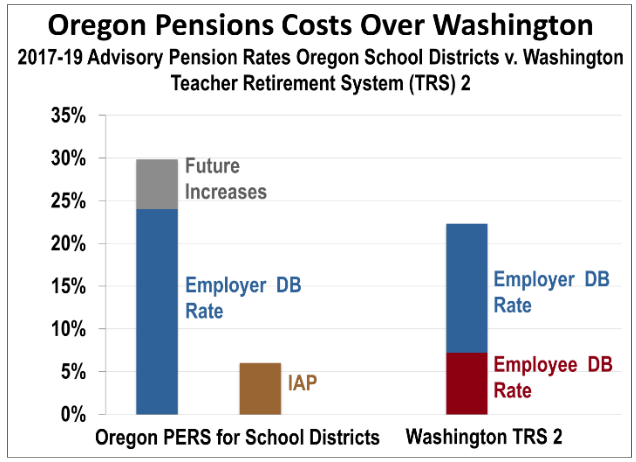


These retirement cost increases, combined with pay and benefit increases, will create an inflationary compensation spiral of 6.5 to 7.5 percent a year. (This prediction is based on the most recent projections from the PERS actuary of 3.5 percent annual wage growth and a legislatively-directed ceiling for state and school health plan rate increases of 3.4 percent a year.)

If these trends persist, payroll costs are likely to accelerate markedly faster in Oregon's public sector than in its private sector.

Further, there are longer-term, cumulative effects from these developments. One is that these same trends will widen disparities within government workforces, as younger employees are forced to share the legacy payroll costs of more senior employees without reaping the benefits they are supporting. Another is that the existing benefit structure of public sector employment is geared to and rewards career employees at the expense of younger workers, who are more likely to move from one employer to another and to retrain for different jobs in the course of their working lives. Pension plans that withhold benefits from workers who fail to meet a threshold of service time are not well suited to today's more mobile work force.

But the fiscal effects of extraordinary legacy costs, driven primarily by a pension system whose payouts far exceeded expectations and have yet to be accounted for, are our greatest and most immediate concern. These effects come into focus most clearly when we compare the magnitude of Oregon's unfunded liability for retirement benefits to that of Washington (see right).

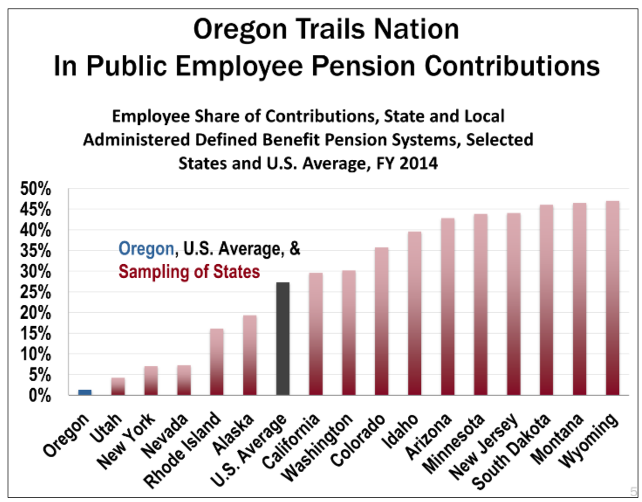


Recommendations for 2016 and Beyond

Compensation trends now in place will have dire consequences for the ability of Oregon's state and governments to improve public service and expand public investments. If unchecked, these trends will undermine the ability of government in Oregon to invest more resources in expanding opportunities for our people. However, these trends can be changed, and it need not require an exercise in austerity to do so.

1. **Address PERS costs in the wake of the Moro decision.** PERS' payroll cost increases are driven by the magnitude of the system's unfunded liability, a legacy cost that resulted from higher-than-expected payouts from the system's Money Match program beginning in the 1990s and the fund's investment losses in the 2008 financial crisis. But this unfunded liability will worsen if, as now seems likely for 2015 and later years, the PERS fund fails to meet its assumed earnings rate of 7.5 percent per year. In that case, benefits yet to be earned will come with unfunded liabilities as well.

Since 2003, PERS has been a non-contributory plan for public employees. Public retirement plans in other states require some level of contributions from employees, and many have required increased contributions from employees to make up for shortfalls in investment earnings. As a consequence (see right) every state in the nation has a higher level of public employee pension contribution than Oregon.



Also in 2003, legislation created a second, stand-alone defined contribution plan as part of PERS. This plan is known as the Individual Account Program (IAP). Public employees covered by PERS are required to contribute 6 percent of salary to the IAP, although, in many jurisdictions, their contributions are paid in full by their public employers. Notably, these contributions are segregated from the fund that supports the PERS pension plan and, under current law, cannot be used to support the pension plan or make up for losses in the PERS fund.

In the wake of the Supreme Court's *Moro v. State of Oregon* decision on PERS, what can be accomplished to avoid a crushing impact on public budgets from rising payroll costs has become more complicated. But it remains feasible, and just as compelling, to pursue solutions.

The court made clear that benefits already earned cannot be compromised. But it also made clear that benefits yet to be earned can be changed. This leaves open the possibility that current employees can become part of the solution to the PERS problem by contributing to their own retirement plans or by accepting lesser benefits in the future.

Policy Option 1: Establish employee cost sharing. Enact legislation to establish cost-sharing mechanisms for public employees to sustain adequate funding for their pension benefits. This could take the form of:

- Requiring employee contributions to support the PERS pension plan, or,
- Redirecting all or a portion of the 6 percent of salary that now supports the IAP to offset the cost of future pension benefits, or,
- Redirecting the 6 percent of salary that now supports the IAP for Tier 1 and 2 employees to restore funding for Tier 1 and 2 benefits.

The last of these alternatives was recommended by the Portland City Club in 2011 in a research report, entitled *Oregon PERS: Burdened by the Past, Poised for the Future*. In that report, the City Club concluded, "By redirecting the Tier 1 and Tier 2 mandatory employee contribution from the IAP to the general PERS fund, the money can be used to reduce the UAL while Tier 1 and Tier 2 employees continue to work, returning the fund to fully funded status faster and lowering the burden passed on to future generations."

The PERS Board should terminate the favored treatment of Money Match benefits by which benefits are annuitized by using the system's assumed rate of return of 7.5 percent per year rather than current market rates for annuities.

Policy Option 2: Reduce the favored treatment of Money Match benefits*.* The PERS Board should terminate the favored treatment of Money Match benefits by which benefits are annuitized by using the system's assumed rate of return of 7.5 percent per year rather than current market rates for annuities.

Currently, the PERS Board uses the system's assumed earnings rate of 7.5 percent to annuitize Money Match accounts. As noted in the 2011 Portland City Club report, this practice not only inflates Money Match pensions but compounds costs with subsequent cost-of-living benefits. In 2011, the system's assumed earnings rate was 8 percent. It has since been reduced to 7.5 percent. But today's market rates, depending on the age of the retiree, would still warrant a reduction of several percentage points, with the potential for savings to the system above $1 billion.

The goal of both policy options is to hold employer rates constant or, at a minimum, keep future employer rates below 20 percent of payroll.

2. ***Monitor progress toward cost containment targets for employee health benefits and be prepared to implement alternative strategies to avoid the impact of the "Cadillac Tax.*** Until recently, the costs of health benefits administered by the Public Employees Benefits Board (PEBB) for state employees and by the Oregon Educators Benefits Board (OEBB) for school employees had been increasing at 7 percent to 8 percent a year.

If those costs trends had continued, most plans offered by PEBB and OEBB would have triggered the Affordable Care Act's so-called Cadillac tax in 2018, a tax of 40 percent applied to the cost of benefits above specified thresholds. But PEBB has succeeded in cutting its rate of increase by half of the prior trend over the last two years. And, in response to a legislative directive to hold cost increases to no more than 3.4 percent a year, both PEBB and OEBB have recalculated their rate projections to reflect that cost cap going forward. By doing so, it appears that, with other changes related to the differential pricing of benefits for employees with dependents, PEBB will be able to avoid the Cadillac tax on all of its plan offerings.

Likewise, OEBB should be able to do the same for most of its plans, provided its participating school districts establish tiered pricing for employees with dependents. However, these cost containment projections remain more aspirational than real, especially since the Legislature's directive includes a caveat about not reducing benefits and shifting costs to employees. And school districts with supplemental Health Savings Accounts and other tax-sheltered benefit programs will have to recognize that such mechanisms apply to the Cadillac tax as well.

The next year will be critical for evaluating the progress of PEBB and OEBB in achieving their cost containment goals. Should they fail to do so, the Legislature may have to revise its directive regarding the maintenance of current benefits or take other actions to ensure that health care costs for public employees do not trigger the Cadillac tax in 2018 or succeeding years.

One such alternative has been proposed by Rep. Julie Parrish in HB 3564 (2015), which she will reintroduce in the 2016 legislative session. This approach would restructure payments and benefits for health coverage to avoid the tax and direct savings to a fund to meet critical health care needs and other services.

3. **Align bargaining and compensation practices with fiscal realities and policy goals**. In theory, benefit increases need not drive the total cost of employee compensation to disproportionate levels. Wage increases can be reduced or forgone to adjust for the higher cost of benefits. But, in practice, PERS costs are often treated as an obligation of employers to make good on promised benefits, and are thus seen as "off the table" for collective bargaining. The costs of maintaining health care benefits is a perennial challenge. And salaries are usually set, at least in part, without subjecting them to rebalancing on a total compensation scale. (One exception here is evident in recent state employee contract settlements, which provide for accelerated salary increases if PEBB achieves greater-than-targeted reductions in health care costs. If the relationship here is treated as a two-way street, then higher-than-expected increases in health care costs should be taken into account when setting wages.)

Governments in Oregon should establish policies that seek to align compensation increases with those experienced in the state's private sector labor market and better align bargaining with budgeting when it comes to determining impacts on levels of service.

Further, the ability of governments to meet compensation impacts on service levels and the impacts of those demands on levels of service are usually not evident in the collective bargaining process or when it comes to setting salaries for managers and other public employees who are not covered by bargaining agreements.

To address these problems, governments in Oregon should establish policies that seek to align compensation increases with those experienced in the state's private sector labor market and better align bargaining with budgeting when it comes to determining impacts on levels of service.

Among the options to consider:

- Change the terms and processes for collective bargaining for teachers and staff of the state's 197 school districts, e.g. requiring arbitration in lieu of strikes or converting to regional or statewide bargaining.
- Establish parameters for economic bargaining in school districts in line with state funding increases, so that local bargaining does not direct all new state resources to boosting existing payrolls.
- Increase the transparency of public employee negotiations, e.g. requiring timely disclosure and allowing public comment on terms and costs of proposed settlements.

Conclusion

A well-compensated public workforce is essential to the delivery of high-quality public services, which in turn provide the foundation for a vibrant private economy. This relationship is a two-way street, connecting the 17 percent of workers employed in the public sector and the 83 percent of workers in the private sector through their mutual interests and connections to the economy. When public sector compensation lags that of the larger private workforce, governments have difficulty recruiting and retaining qualified workers and suffer from a diminished capacity to innovate and deliver services efficiently. But, when public sector compensation outpaces that of the private workforce and is not supported by gains in productivity, an increasing share of government resources is directed to support existing payrolls and are unavailable for reinvestment in education, infrastructure, and other drivers of individual opportunity and societal progress.

Keeping public employee compensation in sync with private sector compensation is a necessary condition for doing more and better with the resources provided by taxpayers and to enable investment in the "budgets of choice" that create opportunity for society.

Keeping public employee compensation in sync with private sector compensation is a necessary condition for doing more and better with the resources provided by taxpayers

There has always been a tradition of public service in public employment, which seeks to make life better for the citizens that government protects, serves, and assists in achieving their full potential. Public employees and their unions can be re-engaged in this effort, with rewards for productivity gains in their workplaces and a shared commitment to revitalizing public services. Ultimately, a vibrant private sector generating revenue dividends for an improving public sector is the path to a better quality of life for participants in both sectors. It is this connection which must guide the work of updating and reorienting labor compensation policies in Oregon's state and local governments.

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