



PB 09-05  
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## GOVERNOR GREGOIRE PRESENTS CURRENT REVENUE SUPPLEMENTAL BUDGET

### BRIEFLY

The Governor's current revenue budget proposal uses \$1.6 billion in program cuts and \$1 billion in reserves to close the state's \$2.6 billion gap for 2009-11.

Even with these cuts, a \$2.8 billion gap looms for 2011-13.

Since the legislature adjourned last April, declining revenue forecasts, increasing K-12 enrollment and human service program caseload forecasts, and other factors have opened a \$2.6 billion gap in the enacted budget for the 2009-11 biennium. Legislators are scheduled to come back into session on January 11. State law requires Governor Chris Gregoire to prepare a supplemental spending plan for legislative consideration that is balanced under the current revenue forecast. She released this supplemental budget at a press conference Wednesday in Olympia. The plan includes \$1.6 billion in programmatic cuts. The remainder of the \$2.6 gap is funded from reserves drawn from various state accounts, including the constitutionally established rainy day fund (the budget stabilization account). Even with these cuts, a \$2.8 billion gap looms for 2011-13.

Governor Gregoire described her proposed budget as "balanced but unjust" and stated that she would offer an alternative proposal next month that will identify sources for additional revenue and restore some of the programs cut in the initial proposal.

### PAST TRENDS

We start with a review of recent history to provide context for our discussion of the state's current fiscal situation.

Chart 1: Near General Fund-State Revenue and Spending Since 1999-01 (Billions of Dollars)

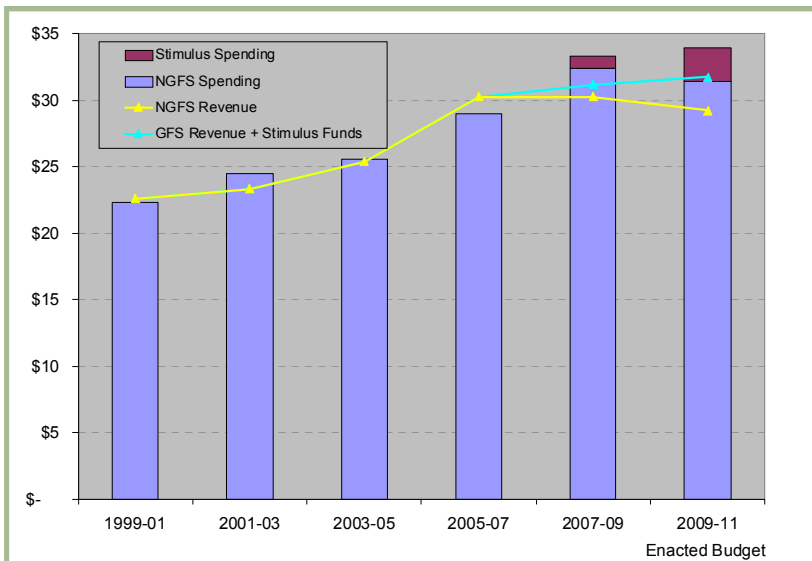


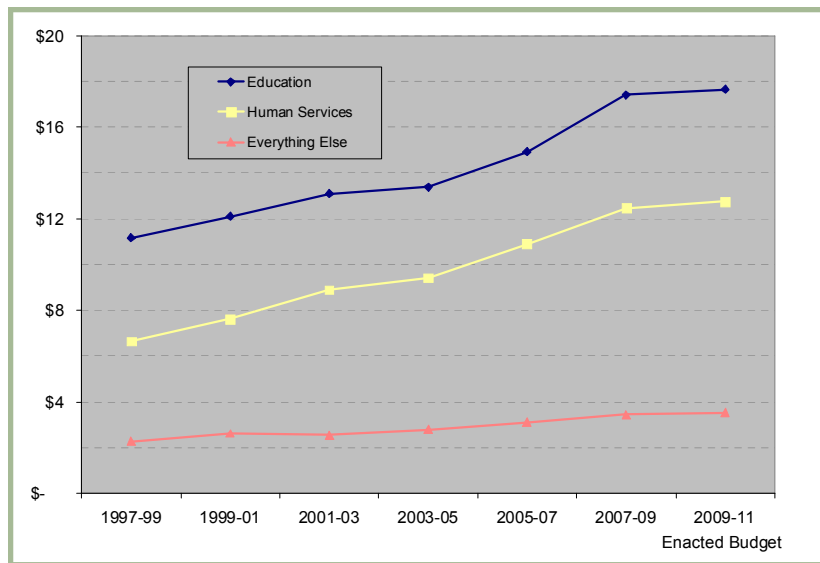
Chart 1 shows the trends in overall near general fund-state (NGFS) spending and revenue from the 1999-01 biennium through the enacted budget for 2009-11. (NGFS is our preferred measure of state spending. See the box on page 5.) Between the 1999-01 and 2007-09 biennia, NGFS spending grew by 45 percent, with large growth increments in both 2005-07 and 2007-09. Strong sales tax collections fueled by the real estate bubble drove spending growth in these two biennia. NGFS revenue in 2005-07 was 19 percent greater than 2003-05. During 2005-07 the state actually spent \$1.3 billion less than it took in. When legislators sat down to write the initial 2007-09 budget, the forecast was that revenue would grow a further 6 percent in 2007-09. The budget that they wrote spent all of this projected growth and drew down the substantial reserves built up in 2005-07.

Revenue actually declined slightly in 2007-09, and budget writers were forced to cut back NGFS spending in the 2009 supplemental budget. Pro-

grammatic cuts were avoided, however, by replacing NGFS funding with federal monies provided to the state through the American Recovery and Reinvestment Act (stimulus funds).

For 2009-11, NGFS revenues are currently forecast to be 3 percent less than 2007-09 revenues. The enacted 2009-11 NGFS budget spends 3 percent less

Chart 2: Near General Fund-State and Stimulus Spending Since 1999–01 (Billions of Dollars)



than actual 2007–09 NGFS spending. Including stimulus funds, however, the enacted 2009–11 budget spends 1.8 percent more than was spent in 2007–09. With Governor Gregoire’s proposed budget cuts, the total would be 0.8 percent less in 2009–11 than in 2007–09.

Chart 2 breaks NGFS plus stimulus spending into three broad categories, education, human services, and everything else. Education accounts for 52 percent of spending in the enacted budget, human services accounts for a bit less than 38 percent; and everything else, a bit more than 10 percent. Human services has been the fastest growing category of spending over the last dozen years, up 92 percent from 1997–99 to the enacted 2009–11 budget, compared to 58 percent for education and 55 percent for everything else. This growth in human services spending was to a great extent driven by health care. For more see WashACE 2008.

**2009–11 BALANCE SHEET**

The table on page 3 presents a near general fund-state balance sheet for the 2009–11 and 2011–13 biennia that incorporates Governor Gregoire’s proposal. We have constructed this balance sheet based on the general fund balance sheet that accompanied Governor Gregoire’s budget proposal and general fund “outlook” provided to us by the Office of Financial Management (Governor 2009, OFM 2009).

The left column of the table shows the 2009-11 situation. The NGFS began the current biennium with a balance of around \$400 million. The November forecast pegs NGFS revenue for the biennium at \$29.2 billion; the state constitution requires that \$252 million of this be transferred to the rainy day fund. The 2009–11 budget enacted last spring transferred \$919 million to the NGFS from other state accounts. Of this amount, \$45 million came from the rainy day fund. The Governor’s supplemental proposal transfers to the NGFS another \$229 million from the rainy day fund as well as \$356 million from other state accounts. This brings total transfers for the biennium to \$1.5 billion. Revenue and transfers to the NGFS thus total just under \$30.5 billion.

The enacted budget appropriates \$31.4 billion for the biennium. OFM has identified an additional \$760 million in spending needed to maintain existing programs. Of this, about \$300 is due to increased forecasts for K–12 enrollments and various human service program caseloads. Funding these maintenance level changes would raise spending for the biennium to more than \$32.1 billion. Governor Gregoire proposes program reductions of \$1.6 billion to hold spending to \$30.5 billion.

Under the Governor’s proposal, the projected NGFS ending balance is \$347 million and the rainy day fund’s ending balance is zero.

While the Governor’s proposed supplemental budget puts the 2009–11 budget technically into balance, expenditures exceed revenues by \$1.5 billion dollars. This difference is covered by transfers to the NGFS from other state accounts. The imbalance between revenues and expenditures sets the stage for a gap to reappear in the 2011–13 biennium.

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**Approximate 2009–11 Balance Sheet and 2011–13 Outlook  
Near General Fund-State (NGFS)**  
(Dollars in Millions)

	2009-11	2011-13
<b>RESOURCES</b>		
<b>Beginning Fund Balance</b>	391	347
<b>Revenue</b>		
November Forecast	29,224	
Extended assuming 4.8% growth From FY 2011		32,809
Required Transfer to Budget Stabilization Account	(252)	(284)
<b>Total Revenue</b>	<b>28,972</b>	<b>32,525</b>
<b>Other Resource Changes</b>		
Enacted Transfer from Budget Stabilization Account	45	
Other Enacted 2009 Fund Transfers	874	
Proposed Additional Transfer from Budget Stabilization Account	229	
Other Proposed 2010 Fund Transfers	356	
<b>Total Other Resource Changes</b>	1,504	
<b>Total Revenues and Resources</b>	<b>30,476</b>	<b>32,525</b>
<b>EXPENDITURES</b>		
<b>Spending</b>		
Enacted 2009-11 Budget/Baseline 2011-13 Budget	31,389	34,449
Additional 2011-13 Expenses		
Replace Stimulus Funding/Other		974
Additional Pension Costs		702
Initiative 728 Catchup		667
Initiative 732 Catchup		172
Proposed 2009-11 Supplemental		
Maintenance Level Changes	760	1,018
Reductions and other changes	(1,629)	(2,288)
<b>Total Appropriations</b>	<b>30,519</b>	<b>35,694</b>
<b>RESERVES</b>		
<b>Ending Balance &amp; Reserves</b>		
Unrestricted Ending Fund Balance	347	(2,822)
Budget Stabilization Account Balance	-	284
<b>Total Reserves</b>	<b>347</b>	<b>(2,538)</b>
Addendum:		
Expenditures of Federal Stimulus Funds	2,528	-
<b>NGFS Appropriations + Expenditures of Stimulus Funds</b>	<b>33,048</b>	<b>35,694</b>

Sources: LEAP, ERFC, OFM; WRC calculations

**2011–13 OUTLOOK**

The right column in the table shows the outlook for 2011–13. The first official forecast of 2011–13 revenues will be made next February. The \$32.8 billion in revenue we show for 2011–13 is calculated assuming 4.8 percent annual growth from the official forecast for FY 2011. Subtracting the required transfer to the rainy day fund leaves \$32.5 billion available to spend.

The estimated cost of continuing in 2011–13 the programs funded in the enacted 2009–11 budget is \$34.5 billion. This estimate assumes that teachers and others covered by Initiative 732 will receive pay increases at the projected rate of CPI inflation (1.7 percent for FY 2012 and 2.2 percent for FY 2013) and that other employees will receive pay increases at the projected rate of increase of the implicit price deflator (1.8 percent and 1.6 percent). Per capita costs of employee health care and medical assistance are expected to grow by 6 percent per year. Per capita costs of other health related programs are expected to grow by 3.6 percent per year. Per capita costs for most other programs grow at the rate of increase in the implicit price deflator.

The analysis identifies \$2.5 billion in additional costs. Maintaining programs that are to be funded with federal stimulus funds in FY 2011 would add nearly \$1 billion to 2011–13 NGFS spending. Additional pension costs add \$702 million, while catching up with Initiatives 728 and 732 would add \$939 million.

The net reduction in spending in the Governor’s 2009-11 budget would carry forward to save \$1,280 in 2011–13. Summing it all up, the projected ending balance for the NGFS is *negative* \$2.8 billion.

**DETAILS OF THE CUTS**

Education accounted for 66 percent of the net reductions relative to the enacted budget in Governor Gregoire’s proposal. Human services’s share of the cuts is 24 percent, while everything else’s share is 10 percent. Here are some of the specific cuts:

*Education.* In early learning, funding is eliminated for 3-year-olds and preserved for 4-year-olds, saving \$10.5 million. (Approximately 1,500 3-year-olds would have been served by the eliminated funding.) Notable cuts in K-12 education include: elimination of funding K–4 class size reductions; suspension of levy equalization; suspension of the student achievement program; and suspension of the program that funds all-day kindergarten at schools with high poverty levels. Together, these four reductions save \$366 million.

In higher education, funding for the state need grant program is reduced, while the work-study program and three smaller scholarship programs are suspended. Total savings from these reductions in financial aid is \$181 million. Direct support for the two- and four-year institutions is reduced by \$86 million.

NGFS higher education spending is reduced by a further \$103 million by shifting responsibility for the bulk of operations and maintenance programs to the capital budget where expenses will be covered by each institutions local building fund. Projects that would have been funded from the local building funds will instead be funded by borrowing. This particular reduction is not a true cut in spending.

*Public Safety.* Twenty-five Washington State Patrol staff positions are eliminated (none of these are troopers) saving \$4 million. Reducing excess capacity in the prison system will save \$8.7 million.

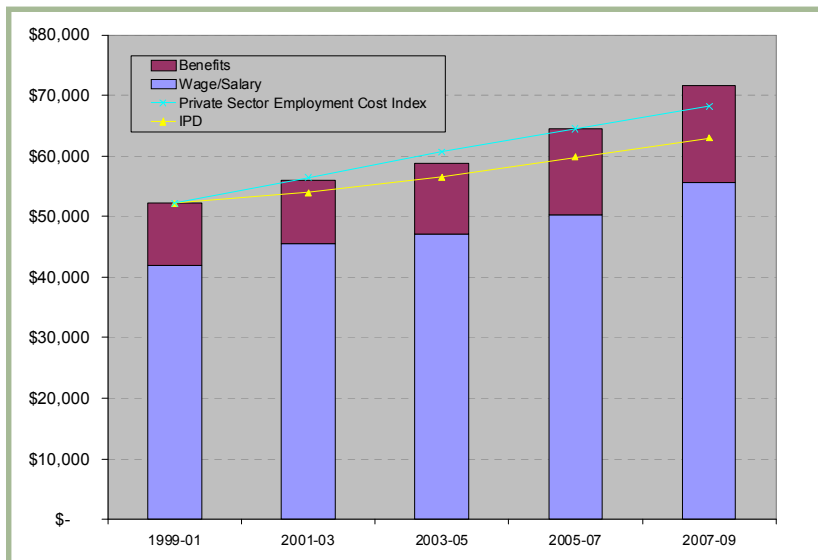
*Social Services.* Elimination of the General Assistance Unemployable grant program will save \$88.5 million. Limiting new subsidies for child care to 1,400 cases per month will save \$88.5 million. Eliminating house-keeping and off-site laundry services to 42,000 elderly or developmentally disabled clients will save \$18.3 million.

*Health care.* The governor’s proposal eliminates the basic health plan, saving \$161 million. Eliminating the General Assistance Unemployable Medical services program saves \$119 million. Suspending the non-medical maternity support program saves \$28 million. Suspending non-emergent adult dental services saves \$14 million. Reducing the eligibility threshold for the Apple Health program for low income children from 300 percent of the federal poverty level to 205 percent saves \$12 million. Suspending three optional Medicaid services for adults (physical, occupational and speech therapies; non-medical vision services; and podiatry services) saves \$7.2 million.

*Employee costs.* Averaged over the full biennium, the supplemental budget decreases full time equivalent state employment by 825, to 98,019, compared to the enacted budget.

As Chart 3 shows, average compensation per full-time-equivalent state employee grew by \$19,400, 37 percent, from 1999–01 to 2007–09. The

Chart 3: Compensation of the Average Full-Time State Employee



percentage by which average state compensation grew exceeded the 21 percent increase in the cost of living over the period as measured by implicit price deflator for personal consumption expenditures (IPD) and exceeded the 31 percent growth in average private sector compensation as measured by the Bureau of Labor Statistics’s employment cost index.

Governor Gregoire's proposal does not make any adjustments to state salary schedules. It does increase the amount of compensation going to state employees in the form of medical benefits. Employee medical costs are increasing more rapidly than anticipated in the enacted budget. The state will bear some of the increased cost and the remainder will be shifted on to employees. The state’s monthly contribution per employee will

increase from \$768 to \$830. For all employees, the annual deductible will increase to \$250. Currently, the deductible is \$200 for 65 percent of state employees, while the other 35 percent now face no deductible at all.

Compared to what is happening in the private sector, these deductibles still appear modest. For example, at the Washington Research Council the employee deductibles will increase from \$500 to \$1,000 on January 1.

#### **LOOKING AHEAD.**

While Governor Gregoire's supplemental proposal would put the 2009–11 budget back into balance, the heavy reliance on one-time resources sets the stage for another budget gap in 2011. The Governor has said that she will bring forward in January an alternative supplemental proposal that would tap additional sources of revenue to restore some programs cut in the supplemental proposal released on Wednesday. Simply swapping tax hikes for spending cuts, however, would leave the structural deficit in place and the state on course for crisis in 2011.

In the introduction to her proposal, Governor Gregoire said: "I invite a robust discussion about how we balance the budget." We look forward to that discussion.

#### **The Near General Fund**

Sound fiscal policy minimizes the amount of tax earmarking.

The Research Council has long lamented the proliferation of special accounts through which the legislature has funded general government programs (WRC 1995). In recent years, eight specific accounts (the "general fund related accounts") have functioned as adjuncts to the general fund: the health services account, the student achievement account, the education legacy trust account, the public safety and education account and its equal justice sub-account, the violence reduction and drug enforcement account, the water quality account, and the pension funding stabilization account. Monies have been freely transferred back and forth between these accounts and the general fund as needs arise. In 2006, the Washington Alliance for a Competitive Economy, of which we are a member, called for these accounts to be consolidated into the general fund (WashACE 2006).

For several years, legislative fiscal staffs have been reporting state spending in terms of a synthetic "account," the near general fund–state (NGFS), which aggregates the general fund and the eight related accounts. This has improved transparency and accountability, and we have generally chosen to use the NGFS in our discussions of the state budget (WRC 2007).

During the 2009 session, the legislature passed and the governor signed Senate Bill SB 5073, which consolidates six of the eight related accounts (all but the education legacy trust account and the pension funding stabilization account) into the general fund. We applaud this, but believe that the education legacy trust account should likewise be consolidated into the general fund. (As no taxes are dedicated to it, the pension funding stabilization account is effectively dead.)

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