

In the 2018 Supplemental, the School Salary Increase is Fully Funded, But the Rainy Day Fund is Shortchanged

Briefly

As passed by the Legislature, the 2018 supplemental operating budget increases near general fund–state plus opportunity pathways spending by \$941.0 million. Appropriations for 2017–19 now total \$44.649 billion. The supplemental does not levy new taxes, and it reduces property taxes in 2019. It also fully funds the increase in school salaries in SY 2018–19, as ordered by the state Supreme Court.

The boost in anticipated revenues provided by the February forecast allowed for the substantial increase in spending while leaving reserves in the budget stabilization account (BSA, or rainy day fund) only slightly lower than anticipated when the biennial budget was enacted last year. Lawmakers, however, redirected funds that are otherwise constitutionally required to be deposited in the BSA.

On the last day of the regular session, the Legislature passed a 2018 supplemental to the 2017–19 operating budget. It increases near general fund–state plus opportunity pathways (NGFS+) appropriations by \$941.0 million, bringing 2017–19 NGFS+ appropriations to \$44.649 billion (a 16.9 percent increase over 2015–17 appropriations).

The supplemental reduces property taxes in 2019 and does not levy any new taxes. It also redirects funds that ought to have gone to the budget stabilization account (BSA, or rainy day fund).

Balance Sheet

Revenues. The supplemental reduces the state property tax rate in CY 2019, which is estimated to reduce revenues by \$206.2 million in 2017–19. Other revenue legislation includes HB 2437 (authorizing local sales taxes for affordable housing), which would reduce state revenues by \$11.0 million in 2017–19, and HB 2998 (authorizing a business and occupation tax exemption for certain Medicaid funds), which would reduce revenues by \$8.3 million in 2017–19.

Other Resources. The supplemental transfers \$105.2 million from the general fund–state (GFS) to the new dedicated McCleary penalty account. This account is established to keep the fines the state has been accruing in the McCleary case on school funding. (The entire amount in the account is then appropriated, on top of the NGFS+ spending in the balance sheet.) The supplemental also transfers \$58.5 million from the GFS to the disaster response account.

Spending. The supplemental would increase NGFS+ spending by \$941.0 million over enacted 2017–19 appropriations. Maintenance level changes (the cost of continuing current services) reduce spending by \$146.3 million, while policy changes increase spending by \$1.087 billion.

Reserves. The unrestricted NGFS+ ending balance is estimated to be \$1.227 billion in 2017–19. The supplemental appropriates \$22.5 million from the BSA for fire suppression costs (SHB 3002). The BSA ending balance is estimated to be \$1.139 billion. (When the Legislature

adjourned last year, the BSA ending balance was expected to be \$1.158 billion.)

Revenue Details

The Economic and Revenue Forecast Council estimates that the state will collect \$1.212 billion more in NGFS+ revenues for 2017–19 than expected in June 2017, thanks to economic growth. Alt-

hough carbon and capital gains taxes were proposed during the session, the substantial boost in anticipated revenues allowed legislators to fund their priorities, including property tax relief, without new taxes.

The property tax reduction stemmed from action taken last year to comply with the state Supreme Court's school funding mandate. In 2017, to increase state education funding, the Legislature added a new state property tax and increased the combined state property tax rate by \$0.81 per \$1,000 of assessed value, to \$2.70/\$1,000 beginning in CY 2018.

This session, the Legislature opted to reduce the state property tax rate by \$0.30/\$1,000 in CY 2019, to \$2.40/\$1,000 (ESSB 6614). This is estimated to reduce revenues by \$390.2 million, of which \$206.2 million will occur in 2017–19 and \$184.0 million will occur in 2019–21.

Spending Details

Public Schools. Last year, the Legislature partially funded the increase in school staff salaries that is required under the McCleary decision in SY 2018–19 and fully funded it in SY 2019–20. Subsequently, the state Supreme Court ordered the Legislature to fully fund the increase in SY 2018–19. The supplemental does so; this increases spending by a total of \$970.4 million. Of that, \$776.4 million occurs in 2017–19 and \$194.0 million occurs in 2019–21. This is mostly NGFS+, but \$74.0 million of the 2017–19 amount comes from the dedicated McCleary penalty account.

The supplemental increases the special education cost multiplier from 0.9309 to 0.9609 percent. This increases NGFS+ spending by \$86,000. Another \$26.8 million would be appropriated for this purpose from the dedicated McCleary penalty account.

The Legislature was supposed to begin phasing in funding of professional learning days in SY 2018–19; instead, the supplemental delays that until SY 2019–20.

Table 1: 2017–19 NGFS+ Balance Sheet (Millions of Dollars)

	<i>2017-19</i>
Beginning Balance	1,149
Revenue	
Feb. 2018 Revenue Forecast	44,990
2018 Supplemental	
Property Tax Reduction	(206)
Other Revenue Legislation	(45)
<i>Total Revenue</i>	<i>44,739</i>
Other Resource Changes	
Transfer to Budget Stabilization Account	(430)
Transfer to BSA (Extraordinary Revenue Growth)	(915)
Transfer from BSA (Extraordinary Revenue Growth)	915
Other Enacted Fund Transfers	328
Prior Period & CAFR Adjustments	41
2018 Supplemental	
Transfer to Dedicated McCleary Penalty Account	(105)
Other Fund Transfers	(61)
<i>Total Other Resource Changes</i>	<i>(227)</i>
<i>Total Resources</i>	<i>45,661</i>
Spending	
Enacted Budget	43,708
Reversions	(215)
2018 Supplemental	
Maintenance Level Changes	(146)
Policy Changes	1,087
<i>Total Spending</i>	<i>44,434</i>
Unrestricted Ending Fund Balance	1,227
Budget Stabilization Account Balance	1,638
Transfers from GFS and Interest Earnings	1,383
Transfers to the GFS	(915)
Transfers to Other Accounts	(925)
Appropriations from BSA	(19)
2018 Supplemental	
Appropriations from BSA	(22)
Projected BSA Ending Fund Balance	1,139
<i>Total Reserves</i>	<i>2,366</i>

This saves \$27.1 million in 2017–19.

Also, the Legislature established regionalization factors last year. These provide additional salary allocations in districts with home values higher than the state median. Such districts are grouped in terciles; the allocations for the first are increased by 6 percent; for the second, 12 percent; and for the third, 18 percent. The supplemental adds a 6 percent adjustment for districts bordering districts with regionalization factors that are more than one tercile higher. This increases spending in 2017–19 by \$13,000 from the NGFS+ and \$4.4 million from the dedicated McCleary penalty account.

By fully funding the increase in school salaries in SY 2018–19, the Legislature has likely avoided additional sanctions in the McCleary case. (Note, though, that footnote 17 of the state Supreme Court’s Nov. 2017 order faults the Legislature for not having a separate account for the McCleary fines and specifies, “the State may not expend the funds in that account without the court’s authorization.”) The Court will determine if the Legisla-

ture is finally compliant at some point after the state makes its report on action taken this session, which is due to the Court in April.

Higher Education. Maintenance level reductions of \$161.2 million in higher education cause the net change from the supplemental to be negative. However, the supplemental increases spending by \$18.5 million to reduce the wait list for the state need grant in FY 2019.

Other. Many budget areas have spending reduced on net due to maintenance level reductions. Appropriations for the Department of Social and Health Services (DSHS) are also reduced at the policy level due to a transfer of \$540.9 million to the Health Care Authority (HCA) related to continuing the integration of physical and behavioral health care services for Medicaid clients.

The supplemental increases spending by \$41.7 million to restore unrealized savings from the Healthier Washington and single Medicaid preferred drug list programs. Also, \$34.6 million is appropriated to cover overspending at the state

Table 2: NGFS+ and All Funds Appropriations (Thousands of Dollars)

	Original 2017-19 Appropriations		2018 Supplemental		Revised 2017-19 Appropriations	
	NGFS+	All Funds	NGFS+	All Funds	NGFS+	All Funds
Legislative	173,344	196,166	(6,752)	(1,369)	166,592	194,797
Judicial	290,429	364,011	(1,211)	8,702	289,218	372,713
Governmental Operations	543,005	4,052,647	357	124,461	543,362	4,177,108
DSHS	6,990,590	15,374,920	(572,585)	(1,226,886)	6,418,005	14,148,034
HCA	4,191,058	17,343,844	471,289	1,816,177	4,662,347	19,160,021
Other Human Services	2,898,723	6,110,156	(45,403)	53,451	2,853,320	6,163,607
Natural Resources	315,433	1,848,973	25,210	70,296	340,643	1,919,269
Transportation	93,970	210,379	325	15,429	94,295	225,808
Public Schools	21,968,576	23,905,236	723,451	882,000	22,692,027	24,787,236
Higher Education	3,832,786	14,544,483	(119,130)	(37,506)	3,713,656	14,506,977
Other Education	225,823	480,679	(2,415)	572	223,408	481,251
Other Appropriations	2,184,644	3,842,919	467,876	(949,644)	2,652,520	2,893,275
Total	43,708,381	88,274,413	941,012	755,683	44,649,393	89,030,096

hospitals in FY 2018. The supplemental appropriates \$46.4 million to pay fines related to the Trueblood lawsuit (on the timeliness of competency evaluations).

For fire suppression costs, NGFS+ appropriations for the Department of Natural Resources are increased by \$27.9 million.

Budget Stabilization Account

The supplemental budgets originally proposed in both the House and Senate had assumed that the reduction in property tax revenues would be offset by transfers from the BSA. But such transfers would have required approval by three-fifths of the Legislature.

Under the state constitution (article VII, section 12), 1 percent of general state revenues must be deposited in the BSA each year. Additionally, three-quarters of any extraordinary revenue growth (EORG) must be deposited in the BSA each biennium. General state revenues, as defined in article VIII, section 1 of the state constitution, are essentially general fund revenues—they don't include dedicated funds.

State property tax collections are dedicated to the support of common schools (RCW 84.52.065), and collections must be paid into the GFS (RCW 84.52.067). Last year, as noted above, the Legislature enacted an additional state property tax that is also dedicated to the support of common schools. The collections from this additional tax were also directed to the GFS.

With a striking amendment offered by the Senate Ways and Means chair in the closing days of the session, ESSB 6614 specifies that \$935 million of the additional property tax must be deposited in the education legacy trust account (ELTA) in FY 2019. The diversion of this revenue allowed lawmakers to spend the money without having to muster the supermajority vote required to tap the BSA. While the diversion had no impact on NGFS+ revenues (because the ELTA is part of the NGFS+), it reduced general state revenues. Consequently, the amounts to be

deposited in the BSA are reduced by about \$700 million (three-quarters of the \$935 million).

Even with this change, there is expected to be an EORG deposit in 2017–19 of \$915 million. Under legislation enacted last year (EHB 2190), the full amount will be transferred back to the GFS.

Additionally, the Legislature passed SHB 3002. It appropriates \$22.5 million from the BSA for fire suppression costs. Although it was passed unanimously by the Senate, it received just a simple majority in the House. Because Gov. Inslee declared a state of emergency on Sept. 2, 2017 due to wildfires, the bill did not require a three-fifths majority.

Outlook

The unrestricted NGFS+ ending balance is estimated to be \$103 million in 2019–21, and the BSA is expected to have an ending balance of \$1.691 billion. (The BSA balance was expected to be just slightly higher—\$1.701 billion—when the Legislature adjourned last year.)

Policy changes in the supplemental that will have significant impacts in 2019–21 include:

- The fiscal impact of the special education cost multiplier increases to \$97.2 million in 2019–21.
- In addition to the new regionalization factor, the supplemental also adds a 4 percent experience factor for districts with median teacher experience above the state average (and a higher ratio of advanced to bachelor's degrees). This experience factor won't kick in until SY 2019–20. Combined, the new regionalization and experience factors will increase spending by \$50.9 million in 2019–21.
- The professional learning day delay will reduce spending by \$75.8 million in 2019–21.
- The Legislature intends to continue to reduce the state need grant wait list until it is eliminated in FY 2022. This

will increase spending by \$97.6 million in 2019–21.

- Transfers must be made from the GFS to the local public safety enhancement account (RCW 41.26.800) in odd-numbered years if general state revenues have increased by more than 5 percent. The transfers for 2013, 2015, and 2017 were suspended by the Legislature. The 2018 supplemental states that it is the intent of the Legislature to fund any distributions in 2019 and 2021 “through alternate means, which may include transfers from the law enforcement officers’ and firefighters’ plan 2 retirement fund.” This policy saves \$50.0 million in 2019–21. However, Gov. Inslee vetoed identical language in the 2017–19 biennial budget last year.

Comment

The supplemental abides by the four-year balanced budget requirement, which is meant to encourage sustainability by balancing the future costs of current policy decisions. Similarly, the constitutional requirement that three-quarters of EORG go to the BSA is meant to hedge against revenue swings by saving during exceptional times. This could help to avoid painful cuts to services during bad times. We have expressed our support for the four-year balanced budget requirement and the constitutional rainy day fund many times.

While the Legislature has spent nearly all the extraordinary revenue growth the state has experienced since 2013–15 (WRC 2018), it has done so by following the rules established in the constitution. Not so this year. As the News Tribune reports,

[Ways and Means chair Christine Rolfes told the two news outlets on Tuesday the plan is necessary because the GOP “indicated” they didn’t support an earlier proposal to pay for the property tax cuts with money from the rainy day fund.

“We can give that money back directly

to the people before it goes to the rainy day fund,” Rolfes said.

The strategy “allows it to be a simple majority vote so we don’t have to fight about it,” she said. (Orenstein 2018)

By avoiding that “fight,” this year’s redirection of funds establishes a precedent that seriously weakens the constitutional provisions.

References

- McCleary et al. v. State of Washington. 2017. [Order in Supreme Court No. 84362-7](#). Nov. 15.
- Orenstein, Walker. 2018. [“The Legislature may give you a property tax cut — but not until 2019.”](#) The News Tribune. March 7.
- Washington Research Council (WRC). 2018. [“Legislature Has Used Rainy Day Fund Each Biennium Except 2011–13.”](#) PB 18–02. Jan. 12.