

*CB 09-03 April 10, 2009***THE BOTTOM LINE**

Both the senate and the house budget proposals rely extensively on one time sources of funds to balance the 2007–09 and 2009–11 budgets. Under either plan, the state would likely face a significant budget gap for 2011–13.

The Near General Fund State (NGFS) is a collection of eight accounts from which the state funds general government services. The NGFS includes the General Fund–State, the Student Achievement Fund, the Health Services Account, the Public Safety and Education Account including the Equal Justice Subaccount, the Violence Reduction and Drug Enforcement Account, the Water Quality Account, the Pension Funding Stabilization Account, and the Education Legacy Trust Account.

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SENATE AND HOUSE BUDGET PROPOSALS KICK THE GAP FORWARD TO 2011–13

Senate Ways and Means Committee Chair Margarita Prentice released her proposed budget for the 2009–11 biennium on Monday, March 30. House Ways and Means Committee Chair Kelli Linville followed the next day with her proposed budget. Under either of these proposals, the state would end the biennium with about \$850 million in reserves, about \$600 million in the Near General Fund State (NGFS) accounts and \$250 million in the budget stabilization account (the constitutionally mandated rainy day fund). The SWM Chair's budget would spend \$31.3 billion from the NGFS accounts for 2009–11, while the HWM Chair's budget would spend \$31.4 billion. In addition, both proposals spend \$1.9 billion in federal stimulus funds on programs traditionally funded from the NGFS.

The bottom lines of the two proposals are fairly close. There are, however, some differences in spending priorities: The HWM Chair spends \$123 million more than the SWM Chair on K–12 education (all-budgeted-funds), while the SWM Chair spends \$279 million more than the HWM Chair on higher education.

Budget writers from the two chambers will negotiate a compromise, which they are planning to have to the governor's desk by the scheduled April 26 adjournment of the regular legislative session.

Federal stimulus funds and other one time resources like fund transfers and reduced pension contributions mean that there is likely to be a significant budget gap facing legislators in two years, when they write a budget for the 2011–13 biennium.

FEDERAL STIMULUS FUNDS

A March presentation by legislative fiscal staff identifies nearly \$3 billion in federal funding that is available to directly offset NGFS spending reductions in the 2007–09 and 2009–11 biennia, most of which is provided by the federal stimulus bill enacted in February (LFCS 2009). The two largest items are \$1.7 billion for Medicaid provided through a temporary (27 month) increase in the federal matching rate for Medicaid eligible services and \$1 billion from the State Fiscal Stabilization Fund. Eighty-two percent of the state's allocation from the fiscal stabilization fund is

Senate W&M Chair's Budget Proposal Two-Biennia Balance Sheet

Near General Fund in Millions

	2007-09	2009-11
Beginning Balance	2,105	562
Revenue		
March Revenue Forecast	30,437	30,503
2011-13 Revenues (Assumes 6% Annual Growth)	-	-
Transfer to Budget Stabilization Account	(125)	(268)
Revenue Changes	-	138
Total Revenue	30,312	30,373
Other Resource Changes		
Prior Fund Transfers (2007 & 2008)	117	-
ESHB 1694 Fund Transfers	91	-
Use Budget Stabilization Account	400	49
Use Capital Budget Resources	76	667
Other Fund Transfers	29	122
Budget Driven Revenue	(1)	94
Other Adjustments	12	6
Total Other Resource Changes	724	938
Total Resources	33,143	31,874
Spending		
Enacted 2007-09 Budget	33,655	
2009-11 Maintenance Level		37,012
Use Federal Stimulus Funds	(939)	(1,930)
2008 Actual Spending Adjustment	(16)	-
ESHB 1694 (Early Action, Excludes Stimulus Funds)	(297)	-
2009 Supplemental (Excludes Stimulus Funds)	177	-
2009-11 Net Policy Level Changes	-	(3,812)
Total NGFS Spending	32,581	31,270
Ending Balance & Reserves		
Unrestricted Ending Fund Balance	562	604
Budget Stabilization Account Balance	31	250
Total Reserves	593	854
Addendum:		
NGFS Spending + Spending from Federal Stimulus Funds	33,520	33,200

Source: SWM; WashACE

targeted at K-12 and higher education.

In addition to the \$3 billion in direct operating budget impact, fiscal staff identified \$700 million in federal stimulus funds that potentially offset reductions in the operating budget. The largest items in this area are grants to school districts for special education and remedial education.

Maintenance of effort requirements and other strings attached to the federal funds complicate the budget writing task.

BALANCE SHEETS

A balance sheet for the SWM Chair's budget proposal appears to the left; a balance sheet for the HWM Chair's proposal appears on page 3. The first column on each balance sheet shows the 2007-09 biennium; the second column, the 2009-11 biennium. These columns essentially reproduce the balance sheets included with the two proposals. The only significant changes we have made are to separate reductions in NGFS spending that are due to replacement of state funds with federal stimulus funds from reductions in NGFS spending that represent true cuts in state services.

On page 4 we present pro forma "outlooks" for the 2011-13 biennium based on the respective budget proposals and a range of possible revenue growth rates. Our methodology for projecting maintenance level spending is admittedly crude. The results should be considered

illustrative of the problems budget writers will face in 2011 under either proposal rather than definitive estimates of the 2011-13 budget gap.

2007-09

The NGFS accounts began the 2007-09 biennium with \$2.1 billion in reserves. As of the March forecast, expected NGFS revenues total \$30.4 billion, of which \$124 million is to be transferred to the budget stabilization account. Coming into the session, budgeted NGFS spending for the biennium stood at just under \$33.7 billion. Together these three numbers imply a gap between resources and spending exceeding \$1.2 billion. Both budgets close the gap using a combination of fund transfers, federal stimulus funds and true spending cuts.

Fund transfers. During the 2007 and 2008 sessions legislators transferred \$113 million net to the NGFS accounts from other state accounts. The February "early action" supplemental budget (ESHB 1694) transferred an additional \$91 million to the NGFS accounts. The SWM Chair's and HWM Chair's supplemental budget proposals both use \$400 million from the budget stabilization account. The SWM Chair's supplemental taps "capital budget resources" for \$76 million. (This is accomplished by transferring funds from various state accounts and then back-filling the accounts through the capital budget.) Various additional transfers provide \$29 million for the SWM Chair and \$12 million for the HWM Chair.

Federal stimulus funds. ESHB 1694 used \$338 million in federal stimulus funds to reduce 2007-09 NGFS appropriations without actually cut-

HOUSE WAYS & MEANS ACTION

On April 7, after our analysis was substantially completed, the House Ways and Means Committee passed an amended version of the Chair's budget. As passed out by the committee, the house budget spend \$3 million less than the Chair had proposed.

Our comparison of balance sheets is based upon the HWM Chair's proposal.

The comparison of spending priorities on pages 5 and 6 of the brief has been updated to reflect the budget as passed out of committee.

House W&M Chair's Budget Proposal Two-Biennia Balance Sheet		
Near General Fund in Millions		
	2007-09	2009-11
Beginning Balance	2,105	618
Revenue	-	-
March Revenue Forecast	30,437	30,503
2011-13 Revenues (Assumes 6% Annual Growth)	-	-
Transfer to Budget Stabilization Account	(125)	(263)
Revenue Changes	-	(12)
Total Revenue	30,312	30,228
Other Resource Changes		
Prior Fund Transfers (2007 & 2008)	117	-
ESHB 1694 Fund Transfers	91	-
Use Budget Stabilization Account	400	45
Use Capital Budget Resources	-	780
Other Fund Transfers	12	149
Budget Driven Revenue	(2)	128
Other Changes	10	66
Other Resource Changes	628	1,168
Total Resources	33,046	32,014
Spending		
Enacted 2007-09 Budget	33,655	-
2009-11 Maintenance Level	-	36,997
Use Federal Stimulus Funds	(1,109)	(1,928)
2008 Actual Spending Adjustment	(16)	-
ESHB 1694 (Early Action, Excludes Stimulus Funds)	(297)	-
2009 Supplemental (Excludes Stimulus Funds)	194	-
2009-11 Net Policy Level Changes	-	(3,658)
Total NGFS Spending	32,428	31,411
Ending Balance & Reserves		
Unrestricted Ending Fund Balance	618	602
Budget Stabilization Account Balance	32	250
Total Reserves	649	852
Addendum:		
NGFS Spending + Spending from Federal Stimulus Funds	33,537	33,339

Source: OPR, WashACE

ting state services. The SWM Chair’s supplemental budget applies an additional \$611 million in federal stimulus funds to 2007–09. The HWM Chair’s supplemental budget replaces \$771 million in NGFS funds with stimulus funds.

True spending cuts. ESHB 1694 provided real cuts in NGFS appropriations totaling \$297 million. For the most part, these appropriations cuts simply ratified spending reductions imposed administratively by Gov. Gregoire during the last half of 2008. The SWM Chair’s supplemental budget adds back \$177 million largely reflecting caseload increases and fire-related costs. The HWM Chair’s supplemental adds back \$194 million.

Bottom line. The SWM Chair’s budget proposal spends \$32,581 million directly from the NGFS accounts. Adding in the \$939 million in federal stimulus funds that her budget provides for NGFS programs brings the spending total to \$33,520. The HWM Chair’s proposal spends \$32,428 million directly from the NGFS accounts and \$1,109 of federal stimulus funds, for a total of \$33,537 million.

2009–11.

Under the SWM Chair’s proposal, the NGFS accounts are expected to begin the 2009–11 biennium with \$562 million in reserves. Under the HWM Chair’s proposal, the NGFS beginning balances are expected to total \$618 million. Forecast revenues for the biennium are

\$30.5 billion, of which about \$265 million must be transferred to the budget stabilization account. Maintenance level spending (the cost of continuing in 2009–11 the programs funded in the 2007-09 budget) is estimated to be \$37.0 billion. The two supplemental budgets close the gap with a combination of revenue enhancements, fund transfers, federal stimulus funds and spending cuts.

Revenue enhancements. The SWM Chair’s proposal adds \$138 million net to state revenue through a number of changes, including the elimination of several tax exemptions. The largest increases come from: elimination of the real estate excise tax exemption on the sale of foreclosed property; elimination of the discount on the purchase from the state by licensees of liquor for resale; repeal of the sales tax exemption for hybrid vehicles; and repeal of the 2 percent credit against the sales tax on lodging sales in Seattle, which is distributed to the convention center. HWM Chair’s budget does not end any exemptions.

The SWM Chair’s proposal includes \$94 million in “budget driven revenue.” Sources include increased audit activities at the department of revenue, opening new retail stores, opening liquor stores on seven holidays, and increasing the profitability of state liquor stores through price increases or operational efficiencies. The HWM Chair’s proposal assumes \$128 million in budget driven revenue from the same sources.

Fund transfers. The SWM Chair uses \$49 million from the budget stabilization account; the HWM Chair uses \$45 million. The SWM Chair uses \$667 million in capital budget resources; the HWM Chair, \$780 million.

The SWM Chair gets an additional \$122 million from other fund transfers; the HWM Chair gets \$149 million.

Federal stimulus funds. The SWM Chair uses \$1,930 million and the HWM Chair uses \$1,928 million in federal stimulus funds to fund items included in the NGFS maintenance level.

True spending cuts. For the SWM Chair’s proposal, net policy level changes reduce spending NGFS by \$3,812 million from the maintenance level. For the HWM Chair’s proposal, net policy level savings are \$3,658 million.

Bottom line. For 2009–11, the SWM Chair’s budget proposal spends \$31,270 million directly from the NGFS accounts and \$1,930 million in federal stimulus, for a total of \$33,520 million on NGFS programs. The HWM Chair’s proposal spends \$31,441 million directly from the NGFS accounts and \$1,928 of federal stimulus funds, for a total of \$33,339 million.

2011–13.

The balance sheet below presents six pro forma outlooks for the 2011–13 biennium. Three of these are based on the SWM Chair’s 2009–11 budget proposal; three are based on the HWM Chair’s 2009–11 budget. We include three revenue growth scenarios, under which the annual growth rates for both years of the biennium are respectively 4, 5 and 6 percent. (The long-run average rate of revenue growth is roughly 5 percent.) For the three cases based on the SWM Chair’s budget, revenue available after the required transfer to the budget stabilization account ranges from \$33.80 billion to \$34.77 billion. For the cases based on the HWM Chair’s budget,

available revenue ranges from \$33.64 billion to \$34.60 billion.

We begin the calculation of 2011–13 maintenance level spending by scaling up total spending for 2009–11 (\$31,270 million with the SWM Chair’s budget, \$31,411 million with the HWM Chair’s budget) by the growth in the 2009–11 maintenance level over the 2007–09 enacted budget (9.975 percent). This gives basic 2011–13 maintenance levels of \$34,389 million for the SWM Chair’s budget and \$34,544 million for the HWM Chair’s budget.

	Based on Senate Proposal			Based on House Proposal		
	4%	5%	6%	4%	5%	6%
Beginning Balance	604	604	604	604	604	604
Revenue						
2011-13 Revenues	-	-	-	-	-	-
4% Annual Growth	33,489			33,325		
5% Annual Growth		33,977			33,810	
6% Annual Growth			34,468			34,299
Transfer to Budget Stabilization Account	(294)	(299)	(303)	(293)	(297)	(301)
Total Revenue	33,195	33,678	34,165	33,032	33,513	33,997
Total Resources	33,799	34,282	34,769	33,636	34,117	34,601
Spending						
Basic 2011-13 Maintenance Level	34,389	34,389	34,389	34,544	34,544	34,544
Backfill Federal-to-State Stimulus Funds	2,123	2,123	2,123	2,120	2,120	2,120
Backfill Federal-to-School-District Stimulus Funds	410	410	410	410	410	410
Pensions	342	342	342	361	361	361
Total Spending	37,264	37,264	37,264	37,435	37,435	37,435
Ending Balance & Reserves						
Unrestricted Ending Fund Balance	(3,465)	(2,982)	(2,495)	(3,799)	(3,318)	(2,834)
Budget Stabilization Account Balance	544	549	553	537	542	546
Total Reserves	(2,921)	(2,433)	(1,942)	(3,262)	(2,777)	(2,288)

Source: WashACE

But this is not the end of the calculation. The projected 2011–13 maintenance level should be adjusted to reflect instances where “one-time money” has been used to balance the 2009-11 budget. Our analysis adjusts for three uses of one time money.

First, the activities that are paid for with federal stimulus funds in 2009–11 will revert back to the NGFS in 2011-13, and this must be backfilled. Assuming the same 9.975 growth we used in calculating the basic mainte-

nance level, this adds \$2,120 million to 2011–13 maintenance spending.

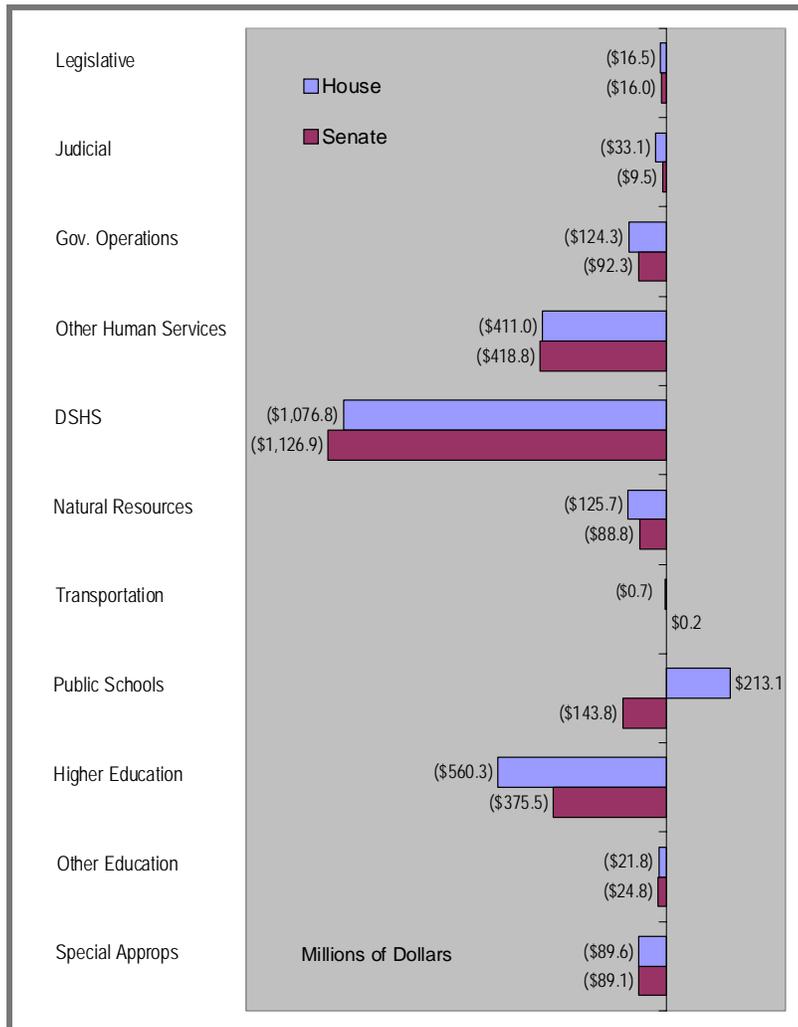
Second, as the SWM Chair’s budget overview notes, the state is counting on stimulus funds that the federal government provides directly to school districts to offset some of the cutbacks in NGFS funding to the districts:

Additionally, it is estimated that the K-12 school districts in Washington state will receive \$410 million in enhanced funding for special education, remedial education, school improvement, and technology that will offset some of the state budget reductions. The Senate budget incorporates these various streams of resources in order to equalize the impacts of the various budget reductions among school districts. (SWM 2009, p. 13)

This \$410 million must be backfilled.

Finally, both the SWM Chair’s and the HWM Chair’s budgets hold down spending by underfunding pensions in the 2009–11 biennium. Returning pension funding to the appropriate level will add an estimated \$342 million in the case of the SWM Chair and \$342 million in the case of the HWM Chair.

Chart 1: Difference Between 2009–11 Proposed NGFS Spending and Enacted 2007–09 Budget



These considerations raise 2011–13 maintenance level spending to \$37,264 million with the SWM Chair’s budget and \$37,435 million with the HWM Chair’s budget.

The 2011-13 gap between available NGFS resources and spending ranges from \$2.5 to \$3.5 billion with the SWM Chair’s budget proposal and \$2.8 to \$3.8 billion with the HWM Chair’s proposal.

SPENDING PRIORITIES.

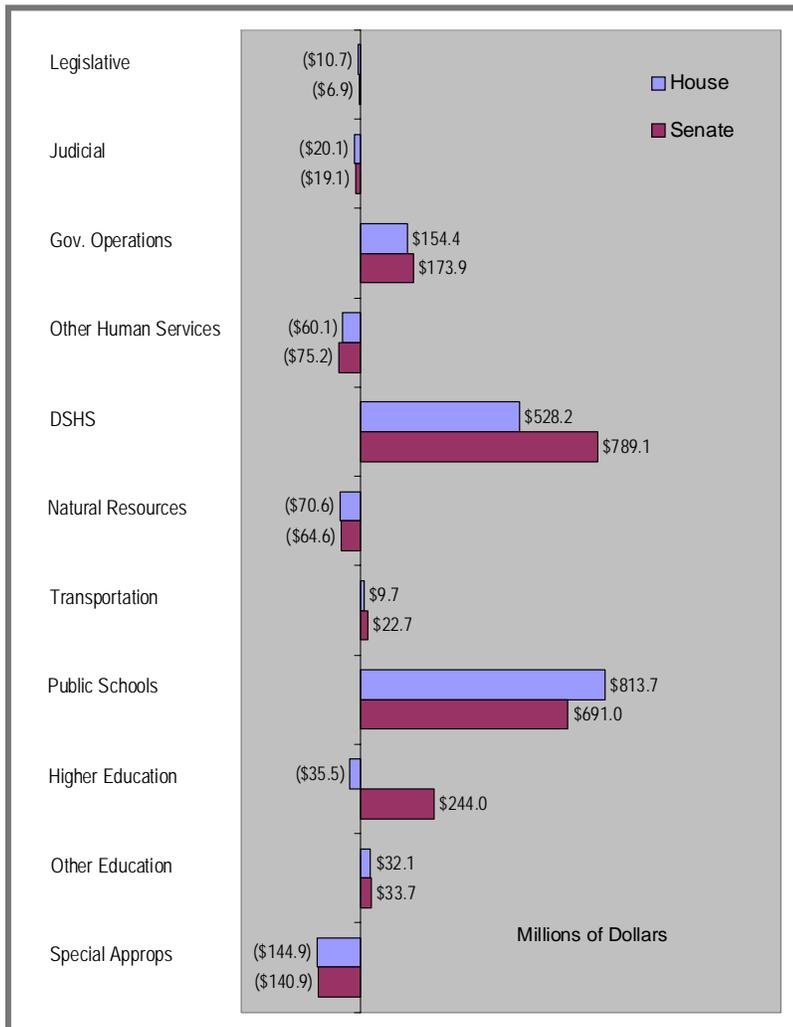
Charts 1 and 2 compare the broad spending priorities of the budget proposed by the SWM chair and the budget passed out by the HWM Committee on April 7th.

Normally, when comparing spending priorities of two budget proposals, we would focus exclusively on spending from the NGFS accounts. We do this in Chart 1. For 2009–11 spending plans, however, the use of federal stimulus funds means that looking at NGFS spending alone may give an incomplete picture of priorities. Complicating matters is the fact that the Legislative Evaluation and Accountability Program/Office of Financial Management fiscal information website provides scant detail on the use of federal stimulus funds in the HWM Committee budget. (In contrast, the website provides extensive detail on the SWM Chair’s use of federal stimulus funds.) For both propos-

als, the website does present detailed spending totals from all budgeted funds. Comparing these totals does provide some insight as to how the stimulus funds are applied. We do this in Chart 2.

Focusing first on just the NGFS, the HWM Committee budget proposes spending for 2009–11 that is \$2.25 billion less than \$33.66 billion budg-

Chart 2: Difference Between 2009–11 Proposed All-Budgeted-Funds Spending and Enacted 2007–09 Budget



eted for 2007–09 coming into the current session (the enacted budget). The NGFS reduction in the SWM Chair’s budget is a bit larger, \$2.39 billion. Chart 1 on page 5 shows the difference between proposed 2009–11 NGFS

spending and the enacted 2007–09 budget in 11 broad spending categories for the two budget proposals. In all but two cases, proposed spending for 2009–11 is less than the 2007–09 budget: The HWM Committee proposes to spend \$213 million NGFS more for public schools than the amount budgeted for 2007–09, while the SWM Chair’s proposes to spend \$154,000 more for transportation. (The amount of transportation spending in the operating budget is relatively small, about \$86 million NGFS for 2007–09; most transportation spending flows through the separate transportation budget.)

The biggest differences in NGFS priorities are in education. The HWM Committee spends \$357 million more than the SWM Chair on public schools, while the SWM Chair spends \$185 million more than the HWM Committee on higher education.

Turning now to all-budgeted-funds spending, the HWM Committee proposal for 2009–11 spends \$58.4 billion from all budgeted funds, \$1.4 billion more than the 2007–09 enacted budget. The SWM Chair’s proposal spends \$58.8 billion, \$1.6 billion more than the enacted budget. Federal stimulus funds largely explain the ability of the two proposals to increase overall spending while cutting NGFS spending. Higher education tuition hikes also contribute.

Chart 2 shows differences from the 2007-09 enacted budgets in all-budgeted-funds for the two proposals. The SWM Chair’s 2009–11 budget proposal spends \$58.8 billion all-budgeted-funds, which is \$1.6 billion more than the enacted 2007–09 budget spends. The HWM Committee spends \$58.4 billion, up \$1.2 billion from 2007–09.

Both budgets show overall spending growth for governmental operations, the department of social and health services (DSHS), transportation, public schools and other education. Under the SWM Chair’s proposal, all-budgeted-funds spending for higher education also grows. The largest swings between the NGFS differences shown on Chart 1 and the all-budgeted-funds differences shown on Chart 2 occur for DSHS, whose Medicaid programs receive more than one-half of the state’s federal stimulus funds.

The SWM Chair spends \$261 million more than the HWM Committee on DSHS from all-budget-funds. The HWM Committee spends \$123 million more than the SWM Chair on K–12 education. The SWM Chair spends \$279 million more than the HWM Committee on higher education. The SWM Chair also provides for lower higher education tuition hikes than the HWM Committee (7 percent at the four-year institutions and 5 percent at the community and technical colleges versus 10 percent and 7 percent).

DISCUSSION

State revenues have been hammered by the “Great Recession.” Based on the 2009–11 budget proposals working their ways through the legislature, it appears that the state will spend \$2.2–\$2.4 billion less from the NGFS accounts in 2009–11 than will be spent in 2007–09. However, growth in revenues outside the NGFS accounts, including federal stimulus funds and higher education tuition hikes, will allow overall state spending to increase by about \$1.2 to \$1.6 billion.

The SWM Chair’s proposal and the HWM Committee’s proposal both rely extensively on one time sources of funds to balance the 2007–09 and 2009–11 budgets. Under either plan, the state would likely face a significant budget gap in 2011–13.

Our estimates put the gap in the \$2.5–\$3.8 billion range.

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Washington State Fiscal Information Website: <http://fiscal.wa.gov/>
