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Policy Brief

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Assumptions Gap Divides Legislative Budget Proposals

Briefly

*The House– and Senate– passed 2013–*15 operating budgets each rely on shaky assumptions on revenues, savings, transfers from the capital budget, and reserves. Legislators' special session goal must be a budget that doesn't rely on one-time transfers, increased business costs, unrealizable savings, or drained reserves.

The regular session of the legislature ended April 28 with no agreement reached on an operating budget for 2013–15. Gov. Inslee has called for a special session to begin May 13. As he said, "The parties are not miles apart at the moment, they are light years apart at the moment" (La Corte).

While both the House- and Senate-passed budgets would significantly increase education spending, the House generally pays for it by increasing taxes, and the Senate generally reduces other spending. Each does, however, make various assumptions about savings or revenues that are unlikely to hold up in the end. (The House has already seen some assumptions go awry, with the passage of fewer tax increases than proposed.)

In a letter to House and Senate leadership, state Treasurer Jim McIntire flags issues with both budgets that "may negatively affect our credit rating" (McIntire). These include low ending fund balances, swapping debt for cash, overly optimistic revenue assumptions, unspecified savings, and questionable lean management savings. In this brief, we'll discuss those and other shaky revenue and savings assumptions.

Revenue Assumptions

The House budget assumed passage of $1.068 billion in new and extended taxes and changes in tax preferences. These proposals (including making a 0.3 percent business and occupation tax surcharge on service business permanent) were dealt with separately from the main budget bill, in ESHB 2038. As passed, ESHB 2038 is estimated to increase revenues by only $885.6 million in 2013–15. (For more information, see "House Finance Committee Considers Tax Increases" and "Tax bill passes House.")

The House has also passed E2SHB 1971 (communications services reform) and EHB 1920 (estate tax clarification); revenues from these bills are assumed in the House budget, but neither has been acted on by the Senate. E2SHB 1971 would make all residential telephone service subject to sales tax (currently, residential landline service is not subject to the tax, but cell phone service is). The telecommunications industry supports the bill. EHB 1920 is a response to the "Bracken decision," in which the state Supreme Court held that the state estate tax does not apply to property going to heirs through a qualified terminable interest trust. Essentially, this opened up an estate planning strategy through which married couples could avoid the state estate tax. EHB 1920 would make these transfers subject to the state estate tax, as they are to the federal estate tax.

The Senate budget assumes a revenue increase of $40 million from collecting use taxes that are currently due. Summary documents about the Senate proposal say that "the Senate is working with the Department of Revenue and industry to develop a way through compliance of existing laws or through legislation to collect a portion of the unpaid taxes" (Senate Chair 2013a). But, as the treasurer notes, there is "no additional collection capacity provided to make this happen" (McIntire).

Savings Assumptions

Both the House and Senate count savings that may not materialize. Critics of each budget have pointed particularly to $151 million in the Senate budget and $20 million in the House budget.

The Senate budget includes savings from $85.9 million in administrative efficiencies, described as

> . . administrative efficiencies and other actions that agencies will take to lower costs. Agencies are directed to achieve these reductions through strategies that minimize negative impacts on the short- and long-term accomplishment of the agency's mission. To the extent possible, agencies are encouraged to use LEAN management principles and employee-driven input to improve agency operational efficiency and to have a measureable impact on services delivered to the public. (Senate Chair 2013b)

It also includes $50.0 million in consolidated savings efficiencies, through which "appropriations are reduced to reflect (1) available fund balances in dedicated revolving funds used for central services to state agencies, and (2) more efficient delivery of consolidated central services to state agencies" (Senate Chair 2013b).

The Senate also books $15.0 million from "efficiencies in information technology expenditures statewide" (Senate Chair 2013b).

LEAN management. The House assumes $20.0 million in savings from LEAN management.

After Gov. Inslee introduced his "budget priorities for a working Washington," David Schumacher, director of the Office of Financial Management, said, "We figured booking savings from LEAN was premature, that when we get to the end of this fiscal year and the next fiscal year, we will hopefully be able to show them, but it seemed like an artificial way of making our balance sheet look better" (Schumacher).

McIntire notes that the LEAN assumptions "stretch the bounds of credibility after so many years of cuts, consolidations, and program eliminations that have already been made" (McIntire). While no one doubts that state government, like any large enterprise, can be made to operate more efficiently, booking the savings represents an aspirational approach to budgeting that may result in disappointing fiscal results in the next biennium.

Workers' compensation and health care. Additionally, the Senate books savings from expanding workers' compensation voluntary settlement agreements to more workers ($10 million) and from reducing health insurance allocations for certain part-time state, higher education and K-12 employees who will be eligible for insurance through the health benefit exchange ($127 million). Under the Affordable Care Act, employers with more than 50 full time employees must provide health coverage, and "full time" is defined as being at least 30 hours a week.

State, higher education, and K-12 employees who work at least 20 hours are currently eligible for coverage. Under the proposal, employees who work between 20 and 30 hours would no longer be eligible for state coverage, but they would be able to get coverage through the exchange. It's important to note that many details about how the state health benefit exchange will work remain to be settled. Gov. Inslee said, "It's one of those ideas that's premature for us to launch this year, but I don't think we should take it off the table" (Baker). Unions are opposed. House Democrats have been critical of the voluntary settlements and the shift of part-time employees to the exchange. The workers' compensation reforms will continue to be a business priority in the special session. If they don't pass, the assumed savings will disappear, increasing pressure on the Senate budget.

Transfers from the Capital Budget

The House budget includes a $100 million transfer to the general fund–state

(GFS) from the public works assistance account. According to the treasurer, "Though not replaced with state bonds, this cash will likely be replaced with higher cost local government bonds to finance needed infrastructure projects" (McIntire). (The Senate transfers $15 million from this account to the GFS.)

The Senate budget permanently transfers $166 million of public trust land timber revenues to the GFS from the common school construction fund. The revenues would be replaced with state bond proceeds.

Common school construction fund. The common school construction fund is established in the constitution "to be used exclusively for the purpose of financing the construction of facilities for the common schools." Based on this, some critics have challenged the constitutionality of the transfer. Counsel for the Senate Ways and Means Committee argues that the following passage from Article IX, Section 3 of the constitution means that such a transfer would be constitutional:

> To the extent that the moneys in the common school construction fund are in excess of the amount necessary to allow fulfillment of the purpose of said fund, the excess shall be available for deposit to the credit of the permanent common school fund or available for the current use of the common schools, as the legislature may direct. (Jones)

Regardless, McIntire says, "In addition to legal concerns about this proposal, I have serious concerns about increasing reliance on debt to fund school construction particularly when general fund debt service costs will already be over $2 billion next biennium" (McIntire).

Table: Near General Fund–State plus Opportunity Pathways Balance Sheet (Dollars in Millions)

	House	*Senate*
Beginning Balance	220	194
Revenue		
March Revenue Forecast	32,865	32,865
Transfer to Child/Family Reinvestment Account	(5)	(6)
Estate Tax Clarification	160	
Tax Preference Repeals	352	
Extend B&O Tax Surcharge	534	
Communications Services Reform	110	
Various Unenacted Bills	(38)	(11)
Budget Driven Revenue	7	7
Collection of Existing Use Tax		40
Reduction of Local Share of Liquor Excise Tax		25
Total Revenue	*33,986*	*32,920*
Other Resource Changes		
Transfer to Budget Stabilization Acct.	(307)	(307)
Use of Budget Stabilization Acct.	575	
Public Works Assistance Acct. transfer	100	15
Foreign Student Surcharge (and transfer to GFS)		59
Other Transfers	87	105
Redirection from Common School Construction Fund		166
Other Capital Budget and Other Revenue Redirection		101
Total Other Resource Changes	*454*	*139*
Total Resources	***34,659***	***33,253***
Spending		
2013-15 Appropriations	34,512	33,349
Projected Reversions		(120)
Total Spending	***34,512***	***33,229***
Unrestricted Ending Fund Balance	*147*	*24*
Budget Stabilization Account Beginning Balance	*268*	*268*
Transfer from GFS	*307*	*307*
Transfer to GFS	*(575)*	-
Total Reserves	*147*	*599*

Reserves

As originally proposed, both the House and Senate budgets left a positive unrestricted ending fund balance: $35 million in the Senate and $337 million in the House. Those numbers have dropped based on the spending and revenue levels that were actually passed, to $24 million in the Senate and $147 million in the House. (Total reserves, including budget stabilization account (BSA) amounts, are $599 million in the Senate and $147 million in the House.) Even those reduced reserves are contingent on transfers that have not yet been passed by either body.

The Senate number includes a transfer of $59.2 million to the GFS from the higher education institutions–local account; the funds are from a proposed surcharge on foreign students (SB 5893), on which there has been no legislative action. Without those funds, the Senate's unrestricted ending balance drops to *negative* $35 million. (Total reserves would be

$540 million.)

The House number includes a transfer of $575 million from the BSA to the GFS. The legislature may tap the BSA by a simple majority vote when the governor declares an emergency resulting from a catastrophic event or when employment growth is forecast to be less than 1 percent. Since neither of these conditions applies, sweeping the BSA would require a vote of three-fifths of both the House and Senate. Without the BSA funds, the House's unrestricted ending balance would be *negative* $428 million. (Total reserves would be $147 million.)

Comment

It may not be a gap of light years, but budget negotiators clearly have their work cut out for them. McIntire concludes, "In a larger context, neither of these budgets is sustainable in the sense that they are fully responsive to the constitutional and statutory obligations of the state and they provide for a minimal unrestricted ending fund balance" (McIntire). We agree.

Ultimately, the special session goal must be a sustainable budget that doesn't rely on one-time transactions, increased business costs, unrealizable assumed savings or drained reserves. Whether legislators end up increasing revenues or cutting more spending, they should focus on avoiding a shakily-balanced budget that will set them up for a tough time if the economy should soften.

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