



BRIEFLY

While talk of a 'crisis' is premature, budget deliberations in Olympia will severely test lawmakers. The task is complicated by four factors: passage of two education initiatives, the small increase in spending permitted by I-601, the partisan balance of the legislature and the increased cost of maintaining current service levels

Spending requests significantly exceed the spending limit. Moreover, for the first time since 1993, desired spending exceeds available revenues.

Expenditure reductions will be required and legislators will be tempted to amend or scrap the spending limit.

Lawmakers Face Toughest Budget Challenge Since 1993

Just days before Gov. Locke releases his proposed budget for the 2001-2003 biennium, there's talk of an impending budget "crisis."

With the economy still strong, but slowing, and reserves of about \$1 billion, the state's fiscal health is solid. Nonetheless, budget writers will be severely tested next year.

Several factors come together to complicate the crafting of the biennial general fund state budget.

First, the passage of Initiative 728 and Initiative 732 significantly limited legislative discretion. The former shifted lottery and property tax money from the general fund, reducing reserves; the latter mandated salary increases for school personnel.

Second, the spending limit established by Initiative 601 (passed in 1993) will grow at the lowest rate (5.9 percent for the biennium) since I-601 was approved.

Third, the partisan balance of the legislature – a one-vote Democratic majority in the Senate and a 49-49 tie in the House – means another session of extended bipartisan negotiation before budget agreement is reached.

Fourth, the cost of extending current services pushes state spending above the I-601 spending limit, even before the effect of the I-732 cost-of-living allowance for most school employees. (With passage of the initiative, the COLA should now be considered part of the current services budget.)

First let's look at the balance sheet.

Balance sheet. The 2001-2003 picture starts out looking reasonably good (see Figure 1). With about a billion dollars in reserves, half in the

emergency reserve fund (ERF), the state appears to have ample cash. Revenues are forecast to exceed the spending limit for 2001-2003 by about \$100 million. The loss of about \$470 million in general fund revenues is incorporated as a result of the transfer of lottery and property tax funds to a new dedicated account created when the voters adopted Initiative 728.

Preliminary General Fund Balance Sheet

General Fund - State (Dollars in Millions)

	<u>1999-01</u>	<u>2001-03</u>
Beginning Fund Balance	\$ 462	\$ 546
Revenues (November forecast, including initiatives)	\$ 21,169	\$ 22,326
Expenditures		
Original 1999-01 Appropriation	\$ 20,573	
2000 Supplemental Budget	\$ 277	
Revised 1999-01 Expenditure Authority	\$ 20,851	
I-601 Limit	\$ 20,935	\$ 22,223
Unrestricted Ending GFS Balance	\$ 550	\$ 539
Emergency Reserve Fund Balance	\$ 537	\$ 570

Source: Office of Financial Management, November 2000

FIGURE 1

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Maintenance level budget. But the budget begins to tighten immediately when the continuing costs of current programs and services are included.

In writing the state’s spending plan, fiscal staff generally begin with something called the “maintenance level” budget. That’s the budget that incorporates the costs of extending current services – including growth in entitlement caseloads and school enrollments – forward into the next biennium.

State budget analysts estimate a maintenance level budget for 2001-2003 of up to \$22.5 billion – about \$300 million above the I-601 spending limit of \$22.2 billion. More conservative estimates of the maintenance level place it right at the I-601 limit. As always, there will be some dispute over what constitutes an extension of current programming and what is actually new or augmented spending. However you slice it, it’s thin.

A recent Senate Ways and Means Committee analysis breaks out a possible \$1.6 billion increase in maintenance level costs along the lines shown in Figure 2. (The committee’s analysis is similar to the projections made by the state Office of Financial Management.) Nearly half the increase is associated with the Department of Social and Health Services (DSHS) - \$466 million for medical assistance and \$336 for “other,” principally caseload growth. Corrections’ spending increases about \$100 million. The I-732 cost-of-living allowance approved for school employees adds nearly \$350 million and school enrollment

growth increases K-12 spending by more than \$225 million. Required debt service payments will take an additional \$88 million.

New spending. Beyond the maintenance budget, there are a number of items legislators are likely to consider. Among those identified by the Senate Ways and Means Committee are these: maintaining current health benefits for state and K-12 employees (about \$230 million), funding increased higher education enrollments and financial aid (\$100 million), and providing all employees and vendors the COLA benefit school employees received under I-732 (\$320 million).

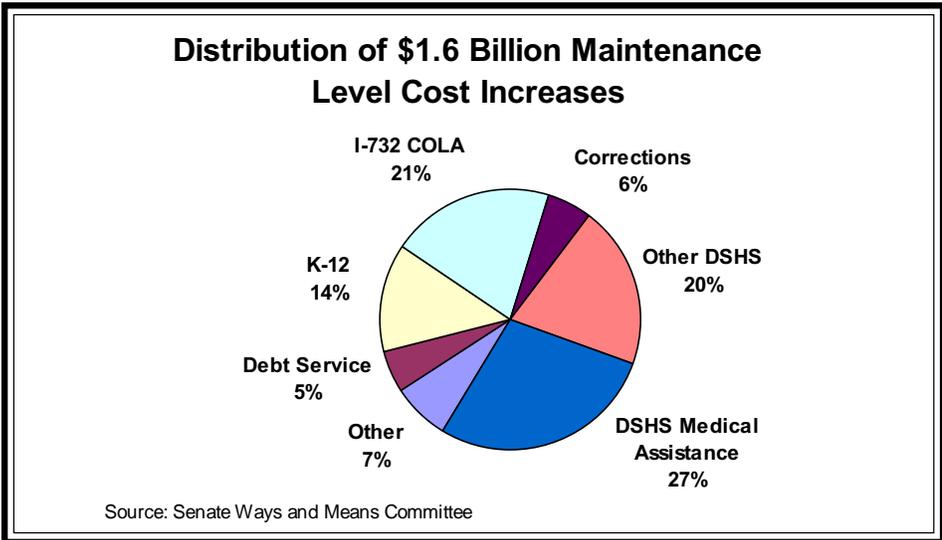


FIGURE 2

With these \$650 million in policy additions, total GFS spending reaches nearly \$23.3 billion, or about \$1.1 billion over the spending limit. Further, the \$23.3 billion exceeds forecast revenues for the biennium by \$1 billion, nearly the combined reserve total (the unrestricted balance plus the emergency reserves).

Discussion. Pre-session budget projections often focus on the gap between desired spending and the spending cap. This year is different. Spending requests also exceed available revenues. At no time since passage of I-601 in November 1993 have lawmakers faced a budget challenge of this severity.



The governor's budget office asked agencies to propose expenditure reductions of six percent. And while savings through efficiencies can create additional maintenance level expenditure capacity, some actual program reductions will surely be required under any likely budget resolution.

As well, the I-601 spending limit will be tested. With an evenly divided House of Representatives and the one-vote Democratic majority in the Senate, the pressure to forge the typical budget compromise – add a bit here, cut a bit there, and try to work with available revenues – will be intense. To the extent the spending cap reduces negotiating flexibility, there will surely be efforts either to amend it or, even, to scrap it entirely.

The governor will release his budget soon. His initial spending plan, and legislative reactions to it, will set the tone for what promises to be a long and tense budget session.



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