



BRIEFLY

Both the house and the senate have passed 2007-09 budgets that spend more than \$33.3 billion.

Both budgets spend \$1.3 billion more than expected revenue and make spending commitments that are not sustainable beyond the 2007-09 biennium

In addition, both budgets leave too little in reserve for this point in the revenue cycle.

SENATE AND HOUSE HEAD TOWARDS A COMPROMISE BUDGET

The 2007 session of the Washington Legislature is scheduled to end this week. The largest piece of unfinished business is the budget for the 2007-09 biennium, which begins July 1. The house passed a budget on March 26. The Senate passed its own version on March 31. Negotiators from the two chambers are at work ironing out the differences. Compromise should not be difficult.

On the macro level the difference is small, only about \$50 million on Near General Fund-State spending plans that exceed \$33.3 billion. Under either plan, spending would grow 15 percent from 2005-07 levels.

In January we criticized Governor Gregoire's budget proposal for leaving too little money in reserve against an unforeseen downturn in the economy and for charting an unsustainable course for spending (WRC 2007a). The House and Senate budgets are little better.

Both the house and the senate budgets spend \$1.3 billion more than they take in in revenue, drawing down reserves to an extent that is inappropriate at this point in the economic cycle.

In recent years, legislators have routed an increasing share of spending for general government purposes through accounts other than the general fund (WashAce 2006, WRC 2007a). In recognition of this, the Legislative Evaluation and Accountability Program Committee tracks spending for a constellation of accounts dubbed the *near general fund-state* (NGFS). NGFS includes the general fund-state (GFS), 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.

It is particularly important to look at the broader NGFS when evaluating the 2007-09 budget because most of the deficit occurs in accounts outside of GFS. Those accounts have built up substantial reserves during the 2005-07 biennium, it is spending down these reserves that accounts for the deficit in 2007-09.

We begin with a look at the 2005-07 budget, because decisions made there have laid the foundation for the deficits in 2007-09.



2005–07 BALANCE SHEETS

The GFS began the 2005–07 biennium with a balance of \$869 million. Following the March forecast update, expected revenue for the biennium is now \$27.5 billion. Various transfers enacted in 2005 and 2006, interest earnings and other adjustments provide an additional \$200 million in re-

sources. (See Chart 1.) It is currently expected that \$24.7 million will spill into the emergency reserve fund.

Entering the session, appropriations for the biennium stood at \$27,298 million. The original 2005–07 budget, enacted in 2005, set GFS spending at \$25,952 million. The 2006 supplemental budget added \$1,346 million. However, \$825 million of this was not really spent but rather was appropriated to three other NGFS accounts (the pension funding stabilization, student achievement and health services accounts).

The house's proposed 2007 supplemental budget would raise 2005–07 GFS spending by \$459.4 million, while the senate's proposal would raise spending by \$458.5 million. In each case, appropriations to other NGFS accounts or to the emergency reserve fund account for most of the net spending: The house appropriates \$4.5 million to the equal justice account, \$215 million to the Education Legacy Trust Account, \$45 million to the health services account and \$119.3 million to the emergency reserve fund. The senate appropriates \$3 million to the public safety and education account, \$3 million to the equal justice sub account, \$215 million to the education legacy trust account, \$155 million to the pension funding stabilization account and \$40 million to the health services account.

Both supplemental budgets appropriate \$50 million to the tobacco prevention and control account. The house appropriates \$30 million to the education construction account.

Chart 1: 2005-07 Balance Sheets

(millions of dollars)

	House	Senate
Beginning GFS Balance	869.7	869.7
November Revenue Forecast	27,365.8	27,365.8
March Update	144.3	144.3
Total Revenue	27,510.1	27,510.1
Emergency Reserve Spillover	(24.7)	(24.7)
Other Transfers and Adjustments	200.2	200.2
Total Transfers and Adjustments	175.5	175.5
Total Revenues and Resources	28,555.2	28,555.2
Prior 2005-07 Appropriations	27,297.9	27,297.9
2007 Supplemental Budget		
Public Safety and Education Account		3.0
Equal Justice Account	4.5	3.0
Education Legacy Trust Account	215.0	215.0
Pension Funding Stabilization Account		155.0
Health Services Account	45.0	40.0
Emergency Reserve Fund	119.3	
Total Appropriations to NGFS Reserves	383.8	416.0
Tobacco Prevention and Control Account	50.0	50.0
Education Construction Account	30.0	
Maintenance Changes	(61.7)	(61.7)
Other Supplemental Appropriations (net)	57.3	54.2
Total Supplemental	459.4	458.5
Total Spending	27,757.3	27,756.4
Ending GFS Balance	797.9	798.8
Emergency Reserve Fund Balance	144.0	24.7
Total GFS Reserves	941.9	823.5
Addendum:		
NGFS Supplemental	441.4	442.0
GFS Spending Excluding Appropriations to NGFS Reserves	26,548.5	26,515.4
NGFS Spending Excluding Appropriations to NGFS Reserves	28,954.5	28,922.9

Source: Senate Ways and Means Committee, House Appropriations Committee, WRC Calculations

Maintenance changes to the 2005–07 budget (due to revised forecasts of public school enrollment and medical assistant caseloads, for example) reduce spending by \$62 million, net. Other supplemental appropriations add \$57 million to the house budget and \$54 million to the senate.



Looking at the larger NGFS, the house supplemental adds \$441 million, while the senate supplemental adds \$442 million.

As noted, the 2006 supplemental and both 2007 supplemental proposals make large appropriations from GFS into other NGFS accounts and to the emergency reserve fund (\$1,209 million with the house supplemental, \$1,241 million with the senate). Netting out these appropriations to reserves gives true spending under the house supplemental as \$26,549 million GFS and \$28,955 million NGFS. Similarly, true spending under the senate supplemental is \$26,515 million GFS and \$28,923 million NGFS.

2007-09 BALANCE SHEETS

The balance sheets shown on Chart 2 summarize the house and senate budgets for the 2007-09 biennium.

The March update from the Forecast Council pegs GFS revenues for the biennium at \$29,516 million. In the house budget, revenue legislation re-

duces expected revenue by \$37.1 million, while other legislation is expected to raise \$700 thousand. In the senate budget, revenue legislation reduces expected revenue by \$56.4 million, while other legislation adds \$7.5 million.

Both budgets reduce the scheduled transfer of revenue from the GFS to the water quality account by \$12.4 million, and both budgets transfer \$20 million to the GFS from the treasurer's account.

The senate budget presumes enactment of the proposed constitutional amendment to establish a rainy day fund (the budget stabilization account, WRC 2007b). Thus the budget stabilization account receives a \$134 million transfer from the GFS and a \$24.7 million rollover from the emergency reserve fund, which it supplants.

The house spends \$29,788 million GFS, \$232 million more than the \$29,556 million that the senate spends, growth of 12.2 and 11.5 percent respectively from 2005-07 levels (excluding appropriations to reserves). Much of the senate's lower GFS spending, however, is offset by greater spending from other accounts included in the broader NGFS. (The senate 2007 supplemental transfers \$151.5 million more from the GFS to other NGFS accounts than the house supplemental does.)

House NGFS spending for 2007-09 is \$33,388 million, while senate NGFS spending is only \$53 million less, \$33,335 million. Growth rates from 2005-07 are 14.8 and 15.3 percent respectively.

The 2007-09 house GFS budget has a deficit (spending in excess of revenues) of \$310.4 million. The senate GFS deficit is \$89.7 million. Looking

Chart 2: 2007-09 Balance Sheets
(millions of dollars)

	House	Senate
Beginning GFS Balance	797.9	798.8
November Revenue Forecast	29,533.3	29,533.4
March Update	(17.8)	(17.8)
Revenue Legislation	(37.1)	(56.4)
Budget Driven Revenue	(0.7)	7.5
Total Revenue	29,477.7	29,466.7
Water Quality Transfer	12.4	12.4
Treasurer's Account Transfer	20.0	20.0
Budget Stabilization Account Transfer		(134.0)
Total Transfers	32.4	(101.6)
Total Revenues and Resources	30,308.0	30,163.9
2007-09 GFS Spending	29,788.3	29,556.4
Ending GFS Balance	519.8	607.6
Emergency Reserve Fund Balance	144.0	
Budget Stabilization Account Balance		158.7
Total GFS Reserves	663.8	766.3
Addendum:		
GFS Deficit (revenues minus spending)	(310.6)	(89.7)
NGFS Spending	33,388.4	33,335.5
Estimated NGFS Deficit	(1,323.6)	(1,270.7)

Source: Senate Ways and Means Committee, House Appropriations Committee, WRC Calculations

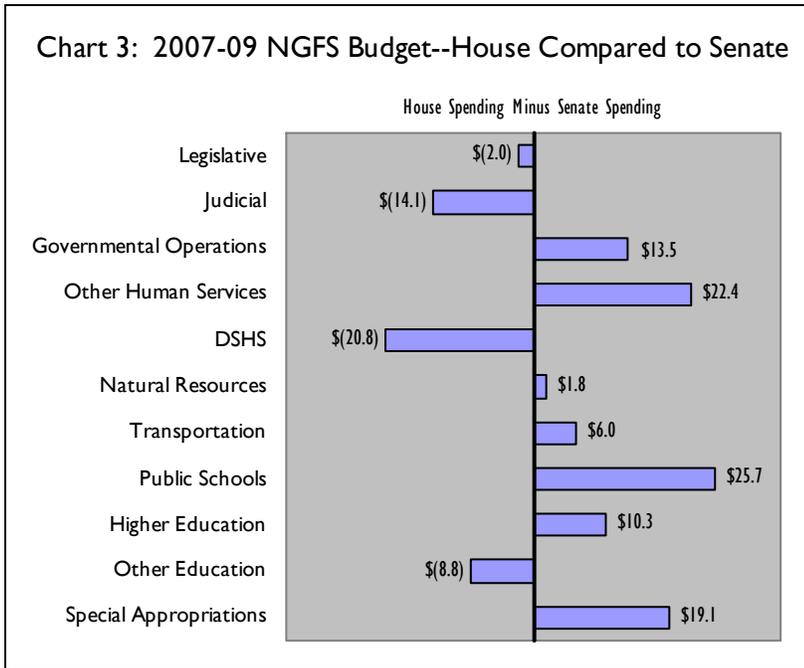


at the broader NGFS, we estimate the house deficit to be about \$1,320 million and the senate deficit to be about \$1,270 million.

The house leaves an ending balance of \$519.8 million in the GFS and \$144 million in the emergency reserve fund. The senate leaves \$607.9 million in the NGFS and \$158.7 million in the budget stabilization account.

SPENDING PRIORITIES

The two budgets differ by more than the overall spending level. They embody somewhat different priorities. The bars on Chart 3, which show differences in NGFS spending levels for the two budgets across 11 broad categories, give an indication of those priorities.



The house spends less on the legislative and judicial branches than does the senate, but more on government operations; less on the programs of the department of social and health services, but more on other human services; more on natural resources and transportation; more on public schools and higher education, but less on other education. Still, these differences are small as a percentage of spending in the categories.

Underneath these broad summaries there are further differences, and it is sorting through these differences that is occupying the time of house and senate negotiators. To stakeholders, every dollar difference between the house and senate is large. Still, with spending up 15 percent overall, it

should not be that difficult to strike a bargain.

DISCUSSION

Both the house and the senate budgets save too little and spend too much.

In the near term, the house and senate budgets leave \$664 million and \$766 million in GFS reserves, respectively. Other NGFS accounts are almost completely drained of reserves. At this stage of the economic cycle, a 5 percent reserve, \$1,670 million, would be prudent.

The national economy has entered a period of low economic growth, and many economists worry that weakness in construction will tip it into recession. It is conventional wisdom that Washington's economy will be stronger than that of the nation as a whole. But, of course, that was also the conventional wisdom in the summer of 2001.

Longer term, the spending commitments contained in the budget are not sustainable. Under both the house and senate budgets the NGFS deficit is \$1.3 billion. A deficit like this at the peak of the economic cycle is inherently structural. Washington state tax revenues are highly sensitive to the level of construction activity and construction is at a 25-year high as a share of economic activity in the state (WRC 2007b). As the construction boom inevitably winds down, state government faces three or four years of below average growth in revenue. And the job of budget writers in 2009 will be much less pleasant than it has been in 2007.



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