Introduction
The purpose of this document is to provide an overview of the methodology used to develop the four-year budget projections pursuant to Chapter 8, Laws of 2012, 1st sp. sess. (SSB 6636). This document summarizes the major components of the projection, the overall approach, as well as the assumptions used in the State Budget Outlook (Outlook) document.

The amounts reflected in the Outlook are the sum of the state General Fund, the Education Legacy Trust Account, and the Opportunity Pathways Account.

Resources
Pursuant to Chapter 8, Laws of 2012, 1st sp. sess. (SSB 6636), the amounts depicted include the actual/projected revenue and other resources. Some of the largest components include:

<u>Beginning Fund Balance</u>
The Outlook uses the certified fund balance in accordance with generally accepted accounting principles for the most recently closed biennium as the starting point.

The beginning fund balance for subsequent years is equal to the projected ending balance for the previous year.

<u>Revenue Forecast</u>
The amounts for 2017-19 and 2019-21 reflect the November 2017 quarterly revenue forecast by the Economic and Revenue Forecast Council (ERFC). The provisions of Chapter 8, Laws of 2012, 1st sp. sess. (SSB 6636) call for the ensuing biennium (in this instance, the 2019-21 biennium) to be balanced based on the greater of: (1) the official revenue forecast for the ensuing biennium; or (2) an assumed revenue increase of 4.5 percent per year for that ensuing biennium. Because the November 2017 forecast projects revenue growth of less than 4.5 percent per year in the 2019-21 biennium, the this Outlook uses the 4.5 percent growth rate.

<u>Transfers to Budget Stabilization Account</u>
Pursuant to a constitutional amendment approved by the voters in 2007, this reflects the transfer of one percent of general state revenues for each fiscal year (FY) to the Budget Stabilization Account. The estimated transfer amounts are based on the calculation of estimated general state revenues as defined in Article VIII, section 1, of the Constitution. The calculation of estimated general state revenues based on the November 2017 revenue forecast is not yet complete so this outlook uses the estimates based on the September 2017 revenue forecast.

<u>Extraordinary Revenue Growth</u>
Pursuant to a constitutional amendment approved by the voters in 2011, this reflects the transfer of three-quarters of extraordinary revenue growth into the budget stabilization account. Extraordinary revenue growth (ERG) is defined in the state Constitution as growth in general state revenues for the fiscal biennium that exceeds the average biennial

percentage growth of the prior five fiscal biennia by one-third. The state Constitution also provides that the transfer only occurs to the extent that it exceeds the normal transfer amount into the budget stabilization account. A transfer of $1.096 billion in 2017-19 is reflected from the GF-S into the BSA. The calculation of estimated general state revenues based on the November 2017 revenue forecast is not yet complete so this outlook uses the estimates based on the September 2017 revenue forecast for purposes of calculating the estimated ERG required transfer.

Chapter 2, Laws of 2015, 3rd sp. sess. (EHB 2286) directs the State Treasurer to transfer amounts attributable to extraordinary revenue growth that were deposited into the BSA to the GF-S. The transfer amount was capped at $550 million for 2017-19. Chapter 29, Laws of 2017, 3rd Special Session (EHB 2190) increased the amount that the State Treasurer must transfer from the BSA to GF-S from $550 million to $1.078 billion.

Enacted Fund Transfers

This category reflects all enacted fund transfers made in the 2015 and 2016 legislative sessions (including special sessions) after accounting for vetoes. For more information, see the 2017 Legislative Budget Notes at: http://fiscal.wa.gov/BudgetOBillsLBNs.aspx.

Transfers for the FY 2019-21 biennia are only included to the extent they are either statutorily required or there was intent language adopted to maintain the transfers in the FY 2019-21 biennium. In accordance with prior ERFC guidance, transfers are not assumed in cases in which the Governor vetoed a transfer or the intent language to continue the transfer in the FY 2017-19 biennium.

Expenditures

As the starting point for the expenditure projection, the Outlook utilizes the most recently enacted budget. It is based on the 2017-19 budget appropriation levels, and then reflects adjustments for preliminary maintenance level (ML) estimates. For more information on the 2017-19 Budget, please see: http://leap.leg.wa.gov/leap/budget/index_lbns.asp.

Assumed Reversions

Reversions for fiscal year 2017 have been updated to reflect actuals. Reversion assumptions for other years are the same as what was included in the Outlook adopted for the enacted budget.

Estimating Costs for the Subsequent Fiscal Biennium

Per statute, the estimated expenditures in the Outlook are to reflect the cost to continue current programs, entitlement program growth, and actions required by law in the subsequent fiscal biennium (e.g. FY 2019-21). The general approach to estimating the cost to continue current programs and growth in entitlement programs is by applying a historical growth factor to the fiscal year cost or savings associated with a budget item. The historical growth factors used to estimate increased costs in the subsequent fiscal biennium are updated each biennium through a joint effort by legislative and executive branch staff and ultimately adopted by the ERFC. Additional information on the calculation of the historical growth factors adopted by the ERFC for the current outlook can be found in the following document available on the ERFC website:

http://erfc.wa.gov/sites/default/files/public/documents/budget/20160921_BudgetOutlook.pdf

There are some cases in which simply applying the growth factor to the cost or savings of a budget item is not used to estimate costs in the subsequent fiscal biennium. These include the following situations.

- K-12 Education. K-12 Outlook calculations utilize the K-12 model, which updates the growth and inflationary factors with each forecast. The K-12 model is continually updated for other factors such as levy equalization, student transportation, and staff mix. The calculations derived from the K-12 model are the same that are used for fiscal notes and legislative policy proposals.
- Custom adjustments. Custom adjustments are used when the estimated annual costs in the subsequent fiscal biennium are expected to be significantly different from the 2nd fiscal year of the current biennium. This occurs primarily when a policy is being phased in during the second year of a biennium or may be delayed until the subsequent fiscal biennium. In most cases, the growth factor is applied after a custom adjustment is made to reflect the phase in for the policy item. In a small number of cases, the custom adjustment already accounts for the types of growth captured by the growth factor and so the growth factor is not applied.
- One-Time costs. Certain items in the budget are one-time for the current biennium and therefore the related costs or savings are not carried forward into the subsequent biennium.
- Compensation items. Because the Outlook statute specifically excludes any additional future costs related to collective bargaining agreements not approved by the Legislature, or salaries and benefits, no growth factor is applied to compensation related items. However, a custom adjustment is applied to items that are not fully implemented in the second year of the biennium to capture the full cost in the subsequent fiscal biennium.

Maintenance Level Revisions

In this section, additional adjustments are made to reflect the costs of continuing to comply with current law provisions. This is often referred to as Maintenance Level (ML). Pursuant to the provisions of Chapter 8, Laws of 2012, 1st sp.s. (SSB 6636), this excludes the costs of policy enhancements, including new collective bargaining agreements not approved by the Legislature, other proposed compensation increases, and costs of any adverse court rulings within 90 days of each respective legislative session. The preliminary estimate of maintenance level adjustments total $313 million in 2017-19 and $174 million in 2019-21.

Kindergarten – Grade 12 (K-12) Schools

The updates are based on the most recent enrollment forecast and budget driver information for required K-12 entitlement changes. The K-12 funding is adjusted each year of the ensuing biennium using the K-12 model which updates the growth and inflationary factors with each forecast. The K-12 model is also continually updated for other factors such as levy equalization, student transportation, and staff mix.

Preliminary ML adjustments total -$34 million in 2017-19 and -$164 million in 2019-21. The larger adjustments are related primarily to enrollment and workload changes, K-3 class size reductions, and prior school year adjustments.

Low-Income Health Care & the Children's Health Insurance Program (CHIP)

The amounts depicted reflect the most recent caseload and per capita cost information prepared as part of the agencies budget submittal, as well as other mandatory maintenance level changes. Some of the major cost components include utilization, caseload, and medical inflation. The growth factor for 2019-21 is estimated at 3.04 percent per year from FY 2019 levels.

Preliminary ML adjustments total $289 million in 2017-19 and $190 million in 2019-21. This includes adjustments related to an increase in the state share of cost for clients receiving services under the Children's Health Insurance Program (CHIP) which has expired and has not yet been reauthorized by the federal government. This also includes an adjustment related to a premium tax established under the Affordable Care Tax that must be paid by most of the managed care plans serving Medicaid clients. This tax has previously been suspended at the federal level but is now scheduled to take effect in 2018. Other large adjustments are related primarily to caseload reductions, increased managed care rates, and an increase in the state's responsibility for the its share of costs for dually eligible clients.

Mental Health/Long Term Care/ Developmental Disability Services

The amounts depicted reflect the most recent caseload and per capita cost information prepared as part of the agencies budget submittal, as well as other mandatory maintenance level changes. Some of the major cost components include utilization and severity of client needs. Assumed future growth is estimated at 4.12 percent per year from FY 2019.

Preliminary ML adjustments total $5 million in 2017-19 and $51 million in 2019-21. The larger adjustments are related to caseload and workload changes, utilization changes, increased managed care rates for behavioral health organizations, and revised estimates for federal revenue available to support operations at the state hospitals.

Children’s/Economic Services

The amounts depicted reflect the most recent caseload and per capita cost information prepared as part of the agencies budget submittal, as well as other mandatory maintenance level changes. Some of the major cost components include caseload and per capita cost increases and revised growth trends. Assumed future growth is estimated at 1.20 percent per year from FY 2019.

Preliminary ML adjustments total $26 million in 2017-19 and $23 million in 2019-21. The larger adjustments are related to caseload changes and a reduction in the amount of federal funding available to support field staff and administrative costs.

<u>Department of Corrections/ Special Commitment/ Juvenile Rehabilitation</u>
The amounts depicted reflect the most recent caseload and per capita cost information prepared as part of the agencies budget submittal, as well as other mandatory maintenance level changes. A major cost component is the proportion of community and institution population. Assumed future growth is estimated at 1.58 percent per year from FY 2019.

Preliminary ML adjustments total $50 million in 2017-19 and $48 million in 2019-21. The larger adjustments are related to caseload changes and restoration of funding for savings included in the current operating budget that assumed new legislation which was never enacted.

<u>Debt Service</u>
The operating budget enacted in 2017 included funding for increased debt service related to assumed passage of a capital budget which has not yet been enacted. The amounts depicted reflect the removal of these funds. Assumed future growth is estimated at 4.35 percent per year from FY 2019 which is consistent with the growth assumed in the 2017 budget.

<u>Higher Education</u>
Higher Education adjustments are generally related to the College Bound Scholarship program and to maintenance and operations and lease adjustments. Higher Education items are adjusted by 0.07 percent per year from FY 2019.

Preliminary ML adjustments total -$9 million in 2017-19 and -$6 million in 2019-21. The larger adjustments are related to a correction in the amount of costs that are allocated to federal funds as well as increased operations and maintenance costs.

<u>Other</u>
This area includes all other agencies not reflected in the proceeding Outlook groups. Many are general government agencies, smaller human service agencies, natural resource agencies, legislative agencies and judicial agencies.

Preliminary ML adjustments total for remaining areas are $34 million in 2017-19 and $132 million in 2019-21. The larger adjustments are related to increased pension costs assumed for the 2019-21 biennium, adjustments for early learning tiered reimbursement programs, a technical adjustment, and an increase in the estimated costs for operating veterans institutions.

Other Outlook Items

These are items that are not in ML but which the ERFC has directed staff to include in the November 2017 outlook.

- Trueblood Fines: This adjustment reflects the estimated penalties the state will pay in FY 2018 related to delays in providing competency evaluation and restoration services in accordance with timelines mandated by a federal court order. The estimates are only calculated through the end of FY 2018. The preliminary cost is estimated at $48 million.
- Fire Suppression Costs: This adjustment reflects the estimated costs of the 2017 fire season which exceeds the amount built into agency base budgets for fire suppression. The preliminary cost estimate is $41 million for FY 2018.