Overview of the Methodology for the State Budget Outlook (January 2015)

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, and 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.

The Governor is required to submit a budget to the Legislature that is based on current law in terms of revenues, commonly referred to as Book 1. The Governor submitted an additional proposal to the Legislature that includes proposed new revenues, this is commonly referred to as Book 2. An Outlook has been completed for both Book 1 and Book 2.

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 2013-15, 2015-17, and 2017-19 reflect the November 2014 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 2017-19 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 2014 forecast projects revenue growth of less than 4.5 percent per year in the 2017-19 biennium, the November 2014 Outlook uses the 4.5 percent growth rate.

<u>Other Revenue Legislation</u>

The Book 2 budget assumes passage of legislation generating revenue totaling $1,557 million in 2015-17 and $3,157 million in 2017-19. Included in these amounts are, in millions:

	2015-17	2017-19
7% Capital Gains Tax	$798.0	$1,778.0
Carbon Pollution Accountability Tax	$380.0	$791.7
Cigarette Tax/E-Cigarettes	$54.1	$107.7
Sales Tax Exemption for Trade-Ins	$105.4	$128.0
Use Tax Exemption for Extracted Fuel	$51.1	$54.4
Non-resident Sales Tax Exemption	$51.5	$57.9
Sales Tax Exemption on Bottled Water	$44.4	$44.8
Preferential B&O Tax Rate for Royalties	$29.6	$33.7
Electronic Commerce	$8.7	$8.3

Revenue Reductions	($93.6)	($104.0)
Other Carbon Pollution Accountability Act	$128.0	$256.0

The Governor's Book 2 budget assumes a new revenue transportation budget. Under current law sales tax revenue from transportation projects flows to the state general fund. The Governor's transportation proposal directs revenue from the sales tax on new projects to the Motor Vehicle Fund. The November revenue forecast does not assume enactment of a new revenue transportation budget and does not include sales tax revenue attributable to new construction activity. The interplay between the operating and transportation budgets is not quantified in the Book 2 Outlook.

Other Enacted Fund Transfers

This category reflects all enacted fund transfers made in the 2013 and 2014 legislative sessions (including special sessions). For more information, see the 2013 and 2014 Legislative Budget Notes at http://leap.leg.wa.gov/leap/budget/lbns/2014Operating.pdf

Current Law (Book 1) Proposed Fund Transfers and Resource Redirections

The Governor's proposed transfers total $203.8 million for 2015-17, including $51.4 million from the Life Sciences Discovery Fund and $92.1 million from the Public Works Assistance Account. In 2017-19 a total of $180.6 million is transferred from the Public Works Assistance Account. Book 1 includes a net of $310.8 million in resource redirections. A net of $83 million is from I-502 taxes that are directed to the GF-S rather than to the Basic Health Plan Account and a distribution from I-502 taxes to local governments. Additionally in Book 1, there are local government distributions that are redirected to the GF-S totaling $244 million in 2015-17 and $245.8 million in 2017-19.

The Book 1 budget transfers a total of $847.5 million from the Budget Stabilization Account: $87.5 million in FY 2015 and $760 million in FY 2017.

New Law (Book 2) Proposed Fund Transfers and Resource Redirections

The Governor's proposed budget transfers total $91.3 million in 2015-17 including $31.4 million from the Life Sciences Discovery Fund; no fund transfers are assumed in 2017-19. Book 2 includes a net of $66.8 million in resource redirections. A net of $83 million is from I-502 taxes that are directed to the GF-S rather than to the Basic Health Plan Account and a distribution from I-502 taxes to local governments. There are also resources directed from the GF-S to a new dedicated L&I account.

The Book 2 budget transfers a total of $537.5 million from the Budget Stabilization Account: $87.5 million in FY 2015 and $450 million in FY 2016.

Transfers to Budget Stabilization Account

Pursuant to a constitutional amendment approved by the voters in 2007, this reflects the transfer of 1 percent of general state revenues for each fiscal year (FY) to the Budget Stabilization Account. This transfer is legally required and estimated transfer amounts are based on the November revenue forecast.

Extraordinary Revenue Growth

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 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 onethird. The state Constitution also provides that the transfer only occur to the extent that it exceeds the normal transfer amount into the budget stabilization account.

Additionally, resource changes proposed in the Governor's budget both in Book 1 and in Book 2 impact the amount of anticipated transfer due to extraordinary revenue growth. The impacts of the proposed resource changes are captured in each version.

Expenditures

As the starting point for the expenditure projection, the Outlook utilizes the most recently enacted budget. In this case, this is based on the 2014 supplemental budget appropriation levels, and then reflects adjustments for carryforward level (CFL) and preliminary maintenance level (ML). For more information on the 2014 supplemental Budget, please see http://leap.leg.wa.gov/leap/budget/index_lbns.asp

Assumed Reversions

In Book 1, reversions are assumed to continue at $70 million per year and in Book 2, the proposal does not continue to assume reversions in FY 2016 and beyond.

Carryforward Level Revisions

The Outlook then adjusts the most recently enacted spending level to the CFL. In short, the CFL is a relatively mechanical calculation based on the removal of any one-time items and adjusting for the bow wave impact of items assumed in existing appropriations (costs or savings). In many instances, this means simply biennializing to the second year enacted funding levels. CFL adjustments total $1.35 billion in 2015-17 and $702 million in 2017-19 reflecting the increasing the base budget by the growth factors adopted by the ERFC. For more information on the CFL adjustments, please see: http://www.erfc.wa.gov/forecast/documents/bo_201501_NovemberOutlookCorrected.pdf

Maintenance Level Revisions

In this section, additional adjustments are made to reflect the expenditure level based on the estimated cost of providing currently authorized services in the ensuing biennium. It is calculated by using the CFL as a starting point and making adjustments for the forecasted changes in the entitlement caseload/enrollment and other mandatory expenses.

The distinction is that this reflects the costs of continuing to comply with current law provisions. This is often referred to as 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, costs of any adverse court rulings within 90 days of each respective legislative session, and the phase-in of K-12 McCleary-related funding.

K-12 Education

This is based on the most recent enrollment forecast and budget driver information for required K-12 entitlement changes. This estimate will continue to be updated as more information like staff-mix is received from local school districts. The K-12 funding will be adjusted 0.66 percent from FY 2017 each year of the ensuing biennium. The Materials, Supplies, and Operating Costs (MSOC) amount is adjusted by both enrollment and the implicit price deflator (IPD).

Larger adjustments in the 2015-17 ML include: enrollment/workload adjustments ($244.7 million), Local Effort Assistance ($7.1 million), K-12 staff mix ($31.7 million), assessment system costs ($22.5 million), and MSOC ($751.8 million).

The larger 2015 supplemental items include: student assessment costs ($16.8 million), enrollment and workload adjustments ($16.4 million), prior school year adjustments ($7.0 million), and local effort assistance ($4.0 million).

Local Effort Assistance
Funding for Local Effort Assistance is adjusted at both at ML to reflect statutory changes that decrease the state funding beginning in FY 2018. This change reduces LEA by $129 million in 2017-19.

Initiative 732 K-12 and Community College Staff Increases
Funding is provided for costs associated with cost of living increases to K-12 and certain community college staff pursuant to Initiative 732. The costs are generally based on the November 2014 Seattle consumer price index (CPI) forecast with projections for a 1.9 percent increase in FY 2016, 1.3 percent increase in FY 2017, 1.8 percent increase in FY 2018, and 2.0 percent increase in FY 2019; these costs total $248 million.

Higher Education
The largest adjustment is related to the College Bound Scholarship program and is based on the most recent caseload information. Other Higher Education items are related to maintenance and operations and lease adjustments. The cost of College Bound is displayed separately. The remaining Higher Education items are adjusted by 0.3 percent per year from FY 2017.

The larger adjustment in the 2015-17 ML is related to College Bound ($25.6 million).

Low-Income Health Care
The amounts depicted reflect the 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 medical inflation. Assumed future growth is estimated at 3.22 percent per year from FY 2017.

Larger adjustments in the 2015-17 ML are related to caseload and utilization changes (-$86.2 million). Other adjustments are related to managed care rates ($109.4) and expansion state Federal Medical Assistance Percentage (FMAP) changes ($47.9 million).

The larger adjustments in the 2015 supplemental budget is related to caseload and utilization -$149.2 million).

Hepatitis C
This item reflects costs identified in Health Care Authority, Department of Corrections, Mental Health, and the Special Commitment Center associated with the new Hepatitis C drug treatment and include $73.9 million in the 2015 supplemental budget and $104.2 million in 2015-17.

Expiration of Hospital Safety Net GF-S Offset
This reflects the GF-S required to cover the rate increases that were allowed as a result of the establishment of a hospital safety net assessment (HSNA). The HSNA phases down during FY 16 and

FY 17 and is set to expire June 30, 2017. Based on legislative expectations, funding is adjusted assuming the replacement of a portion of the hospital safety net assessment revenue with state funds (consistent with statute); these costs are $60.2 million in 2015-17 and $199.8 million in 2017-19.

DSHS Mental Health, Long-Term Care, and Developmental Disabilities
The amounts depicted reflect the most recent caseload and per capita cost information prepared through joint effort by legislative and executive branch staff, 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 3.42 percent per year from FY 2017.

Larger adjustments in the 2015-17 ML include: implementation of community first choice (-$58.4 million), caseload and utilization changes ($ $95.5 million), continued implementation of the children's mental health settlement ($16.6 million) and workload adjustments ($9.1 million).

Larger adjustments in the 2015 Supplemental ML include funding for the Rekhter decision ($43.9 million),

DSHS Children's Services and Economic Services
The amounts depicted reflect the most recent caseload and per capita cost information prepared through joint effort by legislative and executive branch staff, as well as other mandatory maintenance level changes. Some of the major cost components include foster care and adoption support caseload, eligibility experience and revised growth trends. Assumed future growth is estimated at 1.93 percent per year from FY 2017.

Larger adjustments in the 2015-17 ML are related to caseload adjustments (-$27.9 million) and funding for a new SNAP EBT vendor ($3.1 million).

Larger adjustment in the 2015 supplemental budget is related to caseload ($6.3 million).

Department of Corrections, DSHS Juvenile Rehabilitation and Special Commitment Center
The amounts depicted reflect the most recent caseload and per capita cost information prepared through joint effort by legislative and executive branch staff, 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 3.19 percent per year from FY 2017.

Larger adjustments in the 2015-17 ML include: mandatory caseload adjustment ($27.7 million), community violator funding ($2.3 million), and utility rate adjustments ($2.2 million).

Larger adjustments in the 2015 supplemental ML include: mandatory caseload adjustment ($4.9 million, community violator funding ($3.0) and medical inflation ($1.6 million).

Other
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. Assumed future growth is estimated at 0.53 percent per year from FY 2017.

Larger adjustments in the 2015-17 ML include: funding for the presidential primary and voter pamphlet ($11.5 million) and implementing 2SSB 6312 regarding behavioral and medical care purchasing ($33.8 million).

Larger items in the 2015 supplemental ML include: cost allocation adjustments ($1.6 million) and workload adjustments ($1.1 million).

Special Appropriation Items (Part of Other in the Outlook)

This category reflects the typical special appropriation items that are removed in the development of the CFL, but have historically been restored in the ML. It also includes a few new items associated with recent legislation or budgetary actions. An itemization is listed in the table below:

Dollars in Millions

Detail of Items in Special Appropriations	**2015-17**	**2017-19**
Governor's Emergency Fund	$ 1.7	$ 1.7
K-20 Network	$ 16.0	$ 16.0
County Public Health Assistance	$ 72.8	$ 72.8
Fire Contingency	$ 8.0	$ 8.0
O'Brien Building COP Payment	$ 5.9	$ 5.9
SERA Account Repayment	$ 10.2	$ 10.2
Common School Construction Account	$1.2	$1.2
Real Property Replacement Account	$0.6	$0.6
Impaired Driving	$0.7	$0.7
Local Public Safety Enhancement Account RCW 41.26.802	$ 20.0	$ 50.0
Auto Theft Prevention Authority Account	$1.8	$1.8
Total	**$ 148.9**	**$ 178.9**

Policy Items reflected in 2015

The Outlook includes items that are in policy in the 2015 supplemental budget totaling $150 million. The larger items are fire suppression and mobilization and disaster response account funding ($98.5 million).

Initiative 1351

The Governor's budgets, both Book 1 and Book 2, assume the passage of legislation that exempts I-1351 (class size reduction) from the preparation of the Outlook. The Outlooks include a footnote that references this exclusion. The Office of Financial Management prepared a fiscal impact statement on I-1351 for inclusion in the voter's pamphlet. According to that fiscal impact statement and absent the exclusion assumed in the Governor's budget, the cost of I-1351 would be $2.042 billion in 2015-17 and $2.755 billion in 2017-19.

Policy Level Revisions in 2015-17

In this section, adjustments are made to reflect the policy level expenditures included in the Governor's proposed budget. In general, the enhancements are similar in both Book 1 and Book 2 budget; Book 1 also includes reductions. The Book 1 expenditures total $411.8 million in 2015-17 and $1,379 million in 2017-19; the Book 2 expenditures total $1,733 million in 2015-17 and $2,931 million in 2017-19, excluding costs associated with I-1351.

K-12 Education

Enhancements include Full Day Kindergarten ($107.6 million) and K-3 Class Size Reduction ($448.1 million). Statute requires fully funding these items by FY 2018; the Governor's budget fully funds these in FY 2017. The amounts in 2017-19 reflect the projected cost of continuing these policies, including adjustments for the school-year to fiscal-year conversion.

For Book 1, Local Effort Assistance is reduced by 50 percent (-$261.7 million).

Higher Education

Funding for the Opportunity Scholarship is $70 million in Book 1 and $100 million in Book 2. In Book 1, state funding for higher education institutions is reduced by 10% ($141.4 million) and funding for the State Need Grant is reduced by $256 million.

Early Learning

Both Book 1 and Book 2 provide funding for Early Achievers ($70.5 million) and ECEAP Expansion ($79.9 million).

Book 1 reduces funding by $20.9 million to reflect the elimination of 1,391 ECEAP slots.

DSHS Mental Health, Developmental Disabilities and Long Term Care

Both Book 1 and Book 2 fund Mental Health Single Bed Certification ($24.7 million), and a variety of rate adjustments ($30.8 million).

Book 1 delays the Nursing Home Rebase (-$58.7 million).

Department of Corrections, DSHS Juvenile Rehabilitation Administration and Special Commitment Center

Book 1 reduces funding in the Department of Corrections by a total of $261.3 million including: Weapon Enhancement Concurrency ($32.7 million), Prison Swift and Certain Sanctioning ($5.1 million), no longer supervising misdemeanants ($2.5 million), Increasing Earned Time Credits to 50 Percent ($18.4 million), Eliminating supervision for Jailed drug offenders ($16.6 million), Changing the Jail Demarcation Line 22 months ($69.6 million) and 150 Days Early Release ($115.4 million)

DSHS Children's Administration and Economic Services

Both Book 1 and Book 2 provide funding for the FPAWS litigation ($14 million), child protective service staffing, ($6.3 million), Braam compliance ($5.4 million), and Eligibility Services and ACES Remediation (ESAR) IT project ($8.9 million).

Book 1 eliminates funding for Extended Foster Care ($16.2 million) and reduces funding for a variety of programs related to WorkFirst (-$32.1 million).

Hospital Safety Net

Both Book 1 and Book 2 assume savings of $142.6 million attributable to extending and increasing the amount collected under the Hospital Safety Net Assessment by 5.5 percent.

All Other

In Book 2, there is $106.4 million for the Working Families Tax Exemption and $20 million in Department of Commerce for Forest Products.

Collective Bargaining Agreements

Both Book 1 and Book 2 budgets provide funding for collective bargaining agreements for represented employees and comparable salary increases for non-represented employees. Additionally, funding is provided for agreements for non-employees which include home care providers and agency parity, licensed family child care providers and exempt-providers. Total costs for agreements and parity are $424.1 million.

Additional K-12 Cost of Living Adjustment

Both Book 1 and Book 2 budgets provide funding for an additional cost of living adjustments for K-12 employees; the increase makes the K-12 employee COLA comparable to COLA included in the bargained agreements for the represented state employees ($150 million).