

OVERVIEW OF GOVERNOR GREGOIRE'S 2009-11 BIENNIAL OPERATING BUDGET (INCLUDING THE 2009 SUPPLEMENTAL) AND 2009-11 CAPITAL BUDGET PROPOSALS



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Governor Gregoire's Proposed 2009-11 Biennial Operating Budget (including the 2009 Supplemental)

Introduction¹

Since the last legislative session, there has been a significant economic downturn and dramatic declines in projected General Fund-State revenues which worsened what was expected to be a significant budget problem for the 2009-11 biennium.

Before the actions taken in Governor Gregoire's proposed 2009 supplemental and 2009-11 biennial budgets, the Near General Fund operating budget was projected to have a deficit of approximately \$504 million for the remaining part of the 2007-09 biennium and an additional \$5.2 billion deficit for the 2009-11 biennium, not including leaving an unrestricted ending fund balance.

Based on the assumptions used in the development of Governor Gregoire's budget, these deficits were projected based upon anticipated spending needs which included the costs of maintaining current programs and services, as well as providing cost of living adjustments (COLA's), collective bargaining agreements, health benefit cost increases for all public employees, and some selected policy level increases which were included in the Governor's proposal.

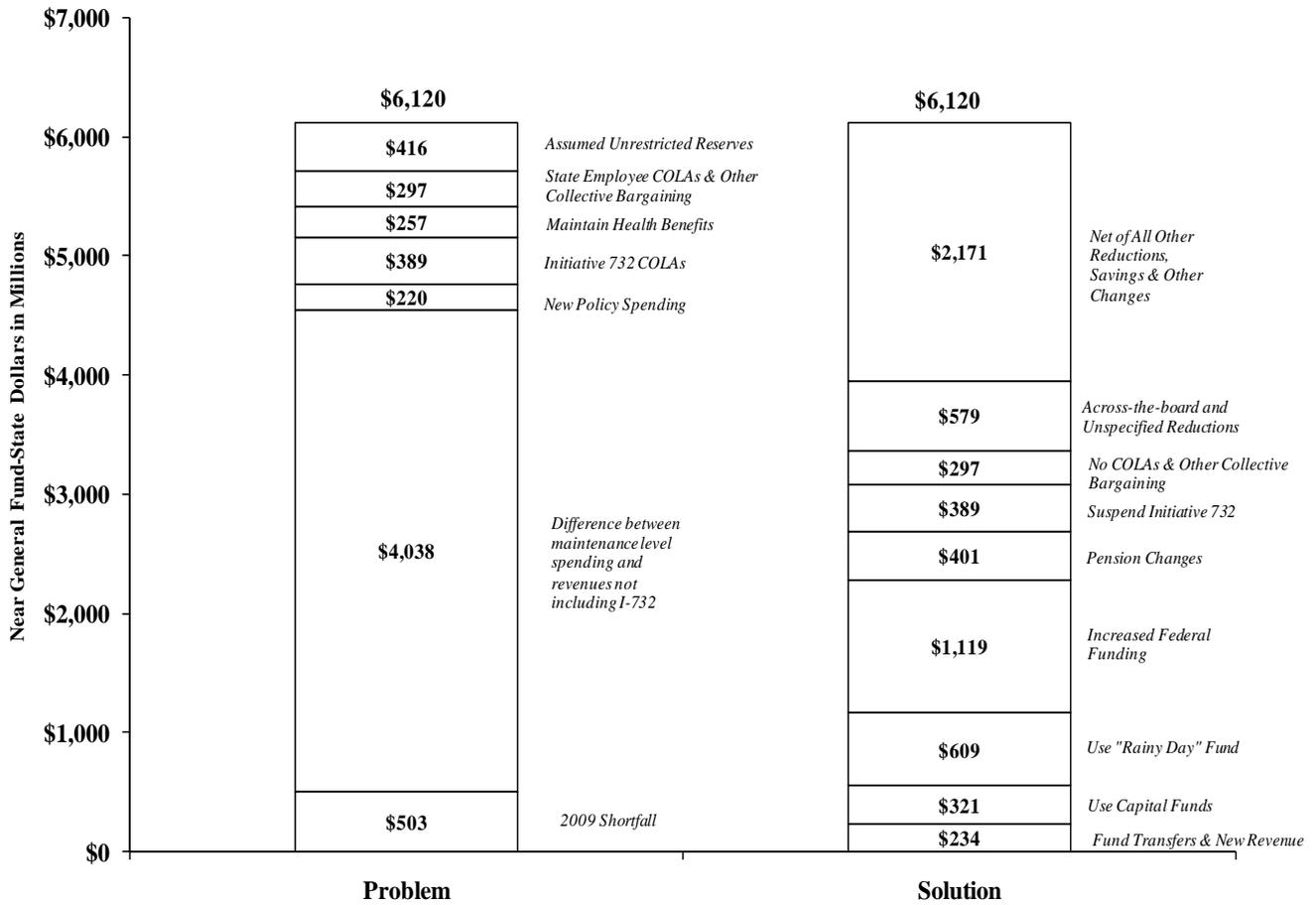
In summary, the difference between projected current services expenditures (plus COLA's and health care benefits, and other policy increases) and forecasted revenues was anticipated to total approximately \$6 billion for fiscal years 2009, 2010, and 2011, including the \$416 million projected to be left in unrestricted reserves.

Overview of Governor Gregoire's Proposed Budget Solution

The Governor's 2009-11 Near General Fund operating budget includes \$219 million in new non-compensation related spending, which increases the size of the deficit the Governor needs to close to about \$6 billion. The Governor's budget addresses this deficit by achieving approximately \$4 billion in savings by making spending reductions, pension changes, and not funding various compensation and collective bargaining increases. Her proposal also makes a number of fund transfers totaling \$184 million, and increases bond capacity by expanding general revenue which allows the utilization of approximately \$321 million cash from various capital accounts to assist the operating budget for the 2009-11 biennium. Approximately \$50 million in new revenue is assumed in the Governor's proposal by improvements to the Department of Revenue auditing function and opening 10 new liquor stores. Finally, the Governor's proposal assumes that \$609 million in the Budget Stabilization Account ("Rainy Day Fund" will be transferred to the General Fund in the 2009-11 biennium).

¹ **IMPORTANT NOTE: For ease of discussing the budget problem and solution, this document is based on the seven accounts or funds considered part of the Near General Fund rather than just the State General Fund. This is done because ultimately this is the best reflection of the entire budget situation that needs to be considered by the Legislature.**

The Governor's Proposed 2009-11 Near General Fund Budget



Near General Fund Budget Changes

Compensation and Collective Bargaining -- \$1 Billion Savings

State and K-12 Employee Compensation:

- Cost-of-living adjustments mandated by Initiative 732 are canceled for the 2009-11 fiscal biennium. Current forecasts of inflation predict that an increase of 4.1 percent would have been called for in the 2009-10 School Year -- \$389.0 million savings.
- Collective bargaining agreements negotiated by the Governor's Labor Relations Office and several institutions of higher learning with labor unions will not be funded, canceling salary increases of varying amounts (typically about 2 percent per fiscal year) -- \$104.0 million savings.
- Salary increases for non-represented employees to match the provisions of the collective bargaining agreements for represented employees would have required additional funding -- \$92.0 million savings.

Contributions to Retirement Systems:

The funds that the state, schools, local governments and employees must contribute to the state retirement systems in the 2009-11 biennium are reduced due to:

- the adoption of the projected unit credit method of actuarial valuation for the state pension systems in place of the current aggregate method of valuation;
- the delay of recognition of the increased longevity of plan members;
- changes to the salary growth assumptions used in calculating future benefit payments and plan revenues; and
- the suspension of the minimum contribution rates for employers that were established in 2006. Total impact from all changes to actuarial methods and assumptions -- \$401.0 million savings.

Collective Bargaining Agreements

- Collective bargaining and arbitration agreements for health care workers, including individual providers, adult family home workers and related agreements for agency providers are not funded. The agreements cover wages, benefits, training contributions, and other items. The savings shown here include the related impacts of Initiative 1029 -- \$80.0 million savings.
- Collective bargaining and arbitration agreements for child care workers are not funded -- \$21.0 million savings.

Compensation -- \$257 Million Increase

Additional funding for employee health benefits reflects assumed employer contributions of \$774 per employee per month in Fiscal Year 2010 and \$831 per employee per month in Fiscal Year 2011 and is expected to allow for the continuation of the current 88 percent employer share of medical insurance premium costs -- \$257.0 million increase.

Increased Federal Funding -- \$1 Billion Savings

Combined, the Governor's proposed 2009 supplemental and 2009-11 operating budget incorporates an assumption that approximately \$1.1 billion in federal funding will be available to reduce state obligations. Specifically, this includes:

- An increase in the state's Federal Medicaid Assistance Percentage (FMAP) used for calculating the federal share of Medicaid related costs based on passage of the federal stimulus package by Congress —\$780.0 million savings.
- A change in federal law allowing Washington to receive an enhanced match for the State Children's Health Insurance Program (SCHIP) funding— \$54.0 million savings.
- The ability to utilize Temporary Assistance for Needy Families (TANF) contingency funds to decrease state-funded support - \$285.0 million savings.

Across-the-Board Reductions -- \$579 Million Savings

In response to the decline in projected revenues, several times during the fall of 2008, the Governor announced various across-the-board reductions, such as freezes on new hiring, out-of-state travel, personal service contracts, and equipment that she was either directing or requesting agencies to make. The Governor's proposed 2009 supplemental budget incorporates some of those assumed reductions and savings for the remainder of this biennium. Additionally, the Governor's proposal for 2009-11 biennium assumes that some of those as of yet unidentified savings will continue on an on-going basis. Over the three years, the assumed level of savings is approximately \$579 million. The savings are reflected in all areas of state government and could result in both administrative and programmatic reductions.

Department of Social and Health Services & Health Care -- \$1 Billion Savings

Low Income Health Care

- Reduce Basic Health Plan (BHP) expenditures by 42 percent beginning July 2009, directing the agency to re-structure benefits, cost-sharing, and enrollment in order to achieve -- \$251.9 million savings.
- Eliminate the General Assistance-Unemployable (GA-U) and Alcohol and Drug Treatment Support Act (ADATSA) medical programs, which provide health care coverage for adults who are temporarily unemployable due to a physical or mental incapacity or are in need of chemical dependency treatment -- \$254.7 million savings.

Provider Reimbursement Reductions and Efficiencies -- \$110.9 million savings

- Reduce hospital inpatient and outpatient reimbursement by 4 percent -- \$42.0 million
- Reduce managed care premium growth rate from no growth to a 1 percent reduction for CY 2009 and from 2.5 percent annually to no growth for CY 2010 and CY 2011 -- \$37.7 million savings.
- Adjust methodology for some inpatient and outpatient rates to improve cost-containment, and to managed care enhanced payments to FQHCs and RHCs to be compliant with a recent federal audit -- \$28.2 million savings.
- Roll back part (7 percent) of the recent rate increase for pediatric office visits and equalize rates for natural and Caesarian section births -- \$3.0 million savings.

Other Eligibility and Benefit Changes -- \$87.6 Million Savings

- Discontinue state reimbursement for non-emergent expenditures under the Alien Emergency Medical (AEM) program -- \$34.8 million savings.
- Reduce maternity support services by 5 percent and durable medical equipment (DME) by 10 percent -- \$20.6 million savings.
- Reduce transportation expenditures as a result of eliminating Adult Day Health program in the Aging and Adult Services (ADSA) budget -- \$10.7 million savings.
- Suspend implementation in January 2009 of the Health Insurance Partnership (HIP) and children's health care coverage expansion from 250 to 300 percent FPL -- \$17.8 million savings.
- Terminate Dental Residency grant, Medicare Part C premium coverage, and Foster Care Health Pilot -- \$3.7 million savings.

Pharmaceutical Savings Initiatives -- \$108.6 Million Savings

- Increase generic drug utilization by 20 percent -- \$43.9 million savings
- Reduce payment for brand-name single-source drugs from 86 percent to 82 percent of the Average Wholesale Price (AWP) beginning January 2009 -- \$13.5 million savings
- Discontinue payment for over-the-counter (OTC) drugs -- \$18.5 million savings
- Increase cost-effectiveness by requiring 90-day supply dispensing for low-risk pharmaceuticals and by changing purchasing strategies related to a number of specific drugs -- \$32.7 million savings

DSHS Long Term Care

The following three components make up a single item reduction in the Governor's Budget -- \$60.2 million savings:

- Reduce nursing facility rates by 7.5 percent -- \$46.2 million savings
- Require certain LTC clients currently using agency provider (AP) services to use individual provider services. This will impact approximately one-third of the clients currently utilizing AP clients -- \$10.6 million savings.
- The homecare worker training enhancements enacted in the 2007 legislative session for increased advanced training (2SHB 2284) scheduled to start January 1, 2010, are suspended this biennium --\$3.4 million savings.

DSHS Economic Services

- WorkFirst savings are estimated by reducing the caseload by 5 percent, reducing education funding to non-TANF and low income clients, and reducing employment and training funding for the Department of Employment Security, State Board for Community and Technical Colleges, and Community, Trade and Economic Development -- \$68.7 million savings.
- The General Assistance – Unemployable (GA-U) program, which provides public assistance payments for disabled, low-income adults not eligible for federal Supplemental Security Income (SSI) benefits, is eliminated. This elimination does not include aged, blind, or disabled programs. The reduction is expected to affect 21,000 recipients a month -- \$156.2 million savings for cash benefits only.

DSHS Children's Administration

- Eliminates state funding for several pilots and programs (secure crisis residential centers, intensive resource foster homes, trauma mitigation pilot, foster care to age 21 pilot, sex abuse recognition training, continuum of care services, and parent education support) -- \$11.5 million estimated state savings.
- Family support services for crisis family intervention and contracts with dependency professionals are reduced - \$3.6 million savings in state funding.

DSHS Mental Health

- "Non-Medicaid" community mental health services are to be reduced by 7.4 percent through unspecified efficiencies and reductions -- \$19.4 million savings.
- Medicaid community mental health payment rates are to be reduced by 3.2 percent -- \$11.2 million savings.
- Three temporary wards (90 beds) at Eastern and Western State Hospitals are to close during 2009, as directed in the 2005-07 and 2007-09 biennial budgets -- \$27.0 million savings already in base budget.
- Children's pilot projects, special grants for adult clubhouses and other innovative services, and performance measurement studies are eliminated -- \$4.9 million savings.

DSHS Juvenile Rehabilitation

- Naselle Youth Camp, in Pacific County, to be closed -- \$12.8 million savings.
- The expansion of evidence-based programs from 2007 are reversed -- \$10.1 million savings.
- Griffin and Touchstone community transition facilities to be closed -- \$2.3 million savings.

DHSH Developmental Disabilities

- Transition approximately 2,400 - 2,500 clients currently receiving state-only funded employment and day services to the Basic waiver program and transition approximately 263 clients currently receiving state-only residential services to the Core waiver. Both moves leverage Medicaid cost sharing -- \$19.0 million savings.
- The Governor proposes to close Yakima Valley School Residential Habilitation Center (RHC) by June 2011. Additionally, the Governor proposes to close Fircrest and Rainier RHCs swimming pools and phase out subsidies to medical and dental staff providing services to community clients. Delay in implementing worker training provisions from 2SHB2284 (Chapter 361, Laws of 2007) -- \$7.7 million savings.

DSHS Alcohol and Substance Abuse

- Various treatment program reductions including eliminating ADATSA stipends and reducing treatment services for adult drug court offenders. In total these reductions impact approximately 22,000 - 23,000 clients -- \$17.8 million savings.

DSHS Special Commitment

- Savings are made by reducing the number of residential rehabilitation counselors – \$5.0 million.

Department of Health -- \$67 Million Savings

- Transition from Universal to Non-Universal vaccine status by July 2010 and eliminate funding for Human Papilloma Virus (HPV) vaccine by July 2009. Federal funding through the Vaccines for Children (VFC) program will still cover Medicaid eligible children and the cost of vaccines for non-Medicaid children will be shifted to other providers consumers -- \$49.6 million savings.
- Other Reductions totaling \$17.5 million in areas such as colorectal cancer screening, digital mammography rates, family planning, HIV Early Intervention program, Women, Infant and Children (WIC) program, the Poison Control Center, and the AIDSNET grant.

K-12 Education -- \$406 Million Savings

- Initiative-728 expenditures would be reduced by 21 percent. I-728, enacted by voters in 2000, provides certain state revenues for classroom-size reduction, extended-learning opportunities for students needing additional time in school, and teacher professional development. -- \$178.0 million savings.
- The Governor's budget reduces levy equalization payments by 33 percent. -- \$125.4 million savings
- Funding for a number of K-12 programs is suspended, reduced, or eliminated. -- \$48.3 million savings
- Math and science professional-development funding that was increased in the 2007-09 biennium is eliminated for 2009-11. The Governor's proposal continues funding through the general apportionment allocations to districts for learning-improvement days to be prioritized for professional development in math and science. -- \$39.7 million savings

Higher Education -- \$370 Million Savings

- After accounting for the higher education share of the across-the-board reductions described previously, state appropriations are reduced by an average of 13 percent at the public four-year colleges and universities, and by 6 percent at the community & technical colleges -- \$343.9 million savings.
- The Governor proposes resident undergraduate tuition increases of up to 7 percent each year at the public four-year institutions, and up to 5% at the community & technical colleges. This will generate an estimated \$163.0 million of additional revenue if the same percentage increases are applied to graduate and non-resident students.
- Maximum income eligibility for the State Need Grant is reduced, basic grant levels are reduced by 5 percent for higher income students, grants are not increased to offset tuition increases at private institutions, and Washington Scholars awards are reduced by 10 percent -- \$26.0 million savings.
- Higher Education Coordinating Board planning and administration are reduced by approximately 8 percent -- \$1.4 million savings.
- Workforce Education and Training Board planning and programs are reduced by approximately 10 percent -- \$0.4 million savings.
- No funding is provided to increase enrollments at the public colleges and universities over the current budgeted (235,000 FTE student) or actual (245,000 FTE student) levels.

Department of Corrections -- \$124 Million Savings

Savings are made by:

- Deporting all non-citizen drug and property offenders -- \$9.0 million savings
- Eliminating 50 percent of the offender re-entry investments made in 2007 -- \$15.0 million savings
- Implementing early release of aged and infirm offenders -- \$1.5 million savings
- Enabling home detention instead of jail for community custody violators -- \$7.5 million savings
- Reducing the sentence lengths by 25 percent on the lowest two levels of the drug grid -- \$5.2 million savings
- Discontinuing supervision of lower risk offenders (Cs and Ds) and misdemeanants -- \$41.6 million savings
- Reducing community custody lengths to 12 months for all except sex offenders, which remain at 36 months -- \$27.2 million savings

The prison savings total \$45 million and the community supervision savings total \$77 million.

Department of Community, Trade and Economic Development (CTED) -- \$31 Million Savings

The Governor proposes to reduce or eliminate various CTED programs, including:

- Transitional Housing and Operating Rents (THOR) -- \$3.0 million savings,
- Dispute Resolution Centers -- \$1.8 million savings,
- Grants to public broadcasters -- \$3.2 million savings,
- Offender re-entry housing pilot project -- \$3.9 million savings,
- Reduce pass-through to Associate Development Organizations -- \$2.0 million savings and
- Reduce the WA Technology Center -- \$1.7 million savings.

Natural Resources -- \$44 Million Savings

The Governor's Budget proposes the following savings:

- Reduction of fish production and closure of the Palmer Ponds and Bellingham hatcheries (\$8.1 million General Fund-State) and closure of the Colville, Omak, Arlington, Mossyrock, and McKernan hatcheries to align expenditures with revenue – \$155,000 Warm Water Game Fish Account, \$7.5 million State Wildlife Account.
- Reductions in water resource-related data collection, grants and technical assistance for watershed plan implementation, and water rights processing activities – \$7.4 million savings.
- Seasonal closure of some state parks and permanent closure of 13 parks and one interpretive learning center --\$5.3 million savings.
- Reductions in land and species management and conservation and habitat protection activities, including funding reductions for local entities -- \$12.6 million savings.
- A variety of other reductions including elimination of seven Department of Fish and Wildlife enforcement officers and other management efficiencies -- \$10.6 million savings.

Selected Other Reductions

- Funding for the Washington State Child Care Resource and Referral Network, child care career and wage ladder, and parent, family, and caregiver support program have been eliminated for 2009-11 -- \$6.7 million savings.
- The Governor proposes the re-organizing of three agencies. The Washington State Historical Society and the Eastern Washington Historical Society are to be merged into one organization. This merger eliminates 6 FTE's and \$1 million from the Eastern Washington Historical Society. Both Historical Societies are also taking a 10 percent reduction in their budgets. The Department of Archeology and Historic Preservation are to be merged with the Parks Department but no budget reductions are assumed with this transfer. The Historic Barn and Courthouse grant program is being moved to the new joint Historic Society.

New Spending -- \$219 Million Increase

- Funding is provided for the debt service associated with the Governor's proposed 2009-11 capital budget -- \$53.0 million
- In order to partially mitigate the effects of eliminating the General Assistance – Unemployable (GA-U) program and reducing the Basic Health Plan (BHP) funding is added to the Health Care Authority's Community Health Clinic grant program -- \$40.0 million.
- Ongoing funding is provided for emergency housing in areas with a high incidence of homelessness -- \$20.0 million.
- Funding is provided for enhanced K-12 pupil transportation allocations to school districts--\$25 million.
- Funding is provided to offset the impact of proposed tuition increases for students receiving state financial aid -- \$19.0 million.
- Additional residential and support services for 92 clients, as detailed below -- \$5.9 million additional:
 - 32 slots for youth aging out of Children's Administration or Juvenile Rehabilitation Administration; and
 - 60 slots for clients who are currently residents of DDD institutions and patients being diverted or discharged from state psychiatric hospitals and participants in the Dangerous Mentally Ill Offender program.
- Funding is provided for water quality and resource-related activities including water adjudication in the Spokane area; completion of the Kittitas groundwater study; research of Puget Sound ecosystem change; and implementation of a statewide watershed health monitoring system in support of the Puget Sound recovery plan -- \$1.1 million Near General Fund-State, \$500,000 other funds.

- Funding is provided to implement greenhouse gas reporting and a regional cap and trade system -- \$1.8 million Other Funds.
- Funding is provided for a variety of other investments including posting a standby emergency rescue tug in Neah Bay; maintaining and increasing recreational shellfish harvest opportunities; removing derelict vessels; implementation of hatchery reform actions; and eradication of spartina in Willapa Bay -- \$726,000 General Fund-State, \$21.2 million Other Funds.

Fund Transfers & New Revenue Changes -- \$234 Million

Fund Transfers

A number of fund related actions and one-time fund transfers are made in both the Governor's proposed 2009 supplemental and 2009-11 budgets to increase reserves. Some of largest include: transferring \$60.0 million in FY 2008 reversions that would have gone to the Education Savings Account; eliminating the \$53.0 million transfer from the General Fund to the Health Services Account; \$30.0 million in State Treasurer's Service Account; and \$11.0 million from the Education Legacy Trust Account --\$185.0 million in total

Liquor Control Board

Several revenue enhancing strategies have been proposed including: opening 10 new stores, expanding lottery sales at liquor stores, and the sale of some non-liquor merchandise. These changes are expected to increase revenues by \$12.9 million but will cost \$1.5 million to implement -- \$11.4 million savings.

Department of Revenue

Funding is provided for the Department to invest in new resources that will improve data analysis and increase efficiency in audit selections and collection. In addition, the funding includes an enhanced focus on out-of-state taxpayers including audit assessments and tax recovery on registered accounts that are under-reporting -- \$38.2 million increase.

Reserves

The Governor's proposed budget leaves an unrestricted ending fund balance in the Near General Fund of approximately \$416 million, with about \$408 million of this amount in the state General Fund. Additionally, after the \$609 million transfer, the projected balance in the Budget Stabilization is projected to be \$100 million.

2009 Supplemental Budget

The Governor's proposed 2009 supplemental operating budget reflects a net reduction in spending of \$467.8 million from the enacted level. The typical caseload and other more usual supplemental adjustments as well as wildlife-related costs total approximately \$182 million. As discussed in previous sections, this increase is more than offset by the assumption that approximately \$338 million in increased federal funds will be available to reduce state obligations for the remainder of the biennium and the assumed implementation of approximately of \$312 million in savings, primarily from across-the-board reductions.

Summary of Governor Gregoire's Proposed 2009-11 Biennial Capital Budget

Background

The Governor's capital budget proposes to spend \$3.4 billion in total funds. Spending from bonds is about \$2.2 billion. The Governor increases bond capacity by expanding general revenue by eliminating the following accounts: Health Services Account, Violence Reduction and Drug Enforcement Account and the Water Quality Account. Revenue that would have flowed to these accounts goes into the General Fund. The added bond capacity is used, in part, to fund about \$321 million in projects typically funded with cash accounts (such as the Water Quality Account, State and Local Toxics Accounts, the Education Construction Account and the Common School Construction Account); the cash from these accounts is transferred to the General Fund for the 2009-11 biennium only.

The budget is distributed among the functional areas as follows:

	Bonds	Total
NEW PROJECTS (\$1,000s)		
Governmental Operations	289,521	779,673
Human Services	145,536	179,513
Natural Resources	430,298	779,530
Higher Education	701,100	831,941
Public Schools	583,694	838,031
Other Education	21,509	21,509
Projects Total	\$2,171,658	\$3,430,197

Proposal

The Governor's proposed capital budget provides:

- \$832 million for higher education facilities, of which \$390 million is for community and technical college facilities and \$442 million is for four year institutions. In addition, the Governor's capital budget authorizes alternative financing for projects totaling \$201 million for the community and technical colleges and \$116 million for the 4-year institutions; this certificate of participation authority will be paid by tuition building fees.
- \$827 million in state matching funds for K-12 school construction.
- \$69 million for correctional facilities, including \$14 million to construct 594 close custody beds at the Washington State Penitentiary. In addition, \$10 million in solar power investments (Alternative Energy Investments through CTED) are made at the Penitentiary and Coyote Ridge and Airway Heights correctional centers.
- \$100 million for housing assistance, weatherization, and affordable housing.
- \$267 million to protect and clean up Puget Sound, including \$138 million in the Department of Ecology and \$83 million in the Recreation and Conservation Office.

- \$78 million in grants to local communities, including \$16 million for local projects, \$32 million for the Building Communities Fund projects, \$10 million for Heritage Projects and \$12 million for Building for the Arts.
- \$50 million for the Washington Wildlife and Recreation Program to preserve habitat and support local and state parks.
- \$97 million for Trust Land Transfers.