Operating Budget Briefing Book

November 2016

Senate Ways & Means Committee

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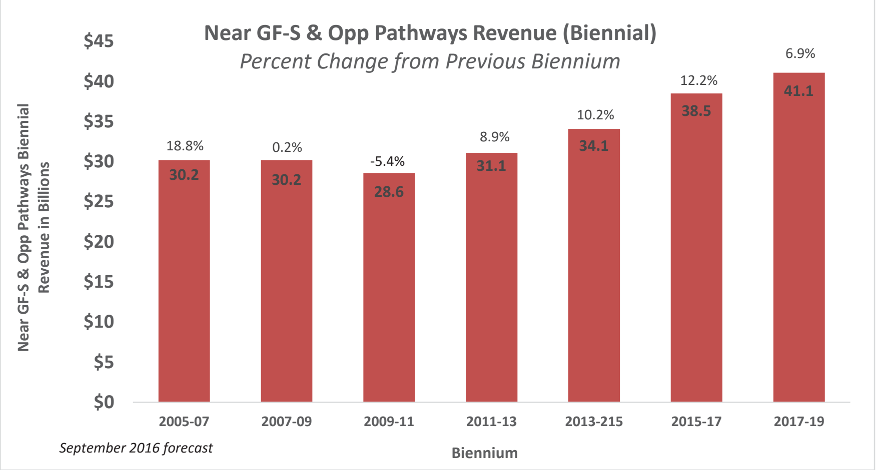
Revenue

Key Facts

- The most prominent streams of revenue to the state general fund are the sales and use tax (51%), the business and occupation tax (19%) and the property tax (11%).
- Near GF-S and Opportunity Pathways revenues are expected to increase from $38.5 billion in the 2015-17 biennium to $41.1 billion in the 2017-19 biennium.
- In 2013 (the latest data available), Washington ranks 22nd in state and local taxes per capita, and ranks 35th in state and local taxes per $1,000 of personal income. Washington has been trending down (less taxation in comparison to other states) over the last several years.

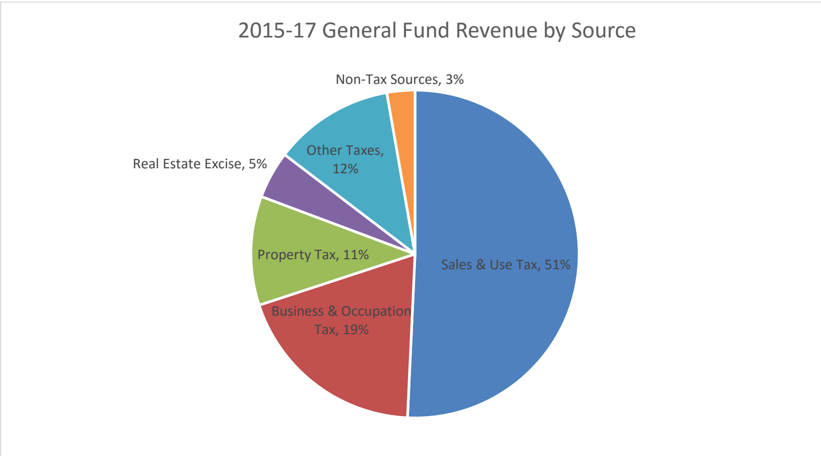
Trend/Overview Information

The graph below provides a biennial look at Near GF-S and Opportunity Pathways revenue over the past several biennia:



The chart below breaks out state general fund revenues by source expected for the 15-17 biennium based on the September 2016 forecast:

Tax Revenue to the General Fund



Current Revenue Issues and Updates

Streamline Sales Tax:

Since 1992, states have been unable to enforce their sales and use tax laws with respect to catalog and online sellers that lack physical presence in Washington (remote sellers). In 2013, a bipartisan group of U.S. Senators introduced and passed The Marketplace Fairness Act (Act), however the bill did not become law. Since the Marketplace Fairness Act, several other bills have been either discussed or introduced at the federal level to allow states to collect sales taxes from remote sellers but none have yet to pass. In addition, there are court cases that have been started that could result in the court overturning their 1992 decision requiring physical presence for sales tax collection. It would take at least two years for the cases to make it through the court system. If either federal legislation occurs or the courts overturn their previous decision regarding sales tax collection by remote sellers, the state would receive $123 million in the 17-19 biennium and $492 million in the 19-21 biennium.

Marijuana Revenue

Initiative 502, passed in November 2012, legalized the recreational use of marijuana and established a regulatory regime, including taxation; the retail sale of marijuana began in July 2014. The initiative imposed a 25% excise tax on marijuana production, processing, and sales. The initiative specified the distribution and purpose of revenue generated. During the 2015 session several changes were made to the marijuana laws. Most notably, beginning July 1, 2016, the medical marijuana market was merged with the recreational market both for sales and regulations. Other changes include collapsing the taxation to just the point of sale at a rate of 37.5% (the revenue neutral rate) as well as changes to the distribution of the revenues. Distributions to cities and counties were also adopted. Local governments

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will receive $6 million per year during the 2015-17 biennium, $15 million per year during the 2017-19 biennium, and $20 million per year each year thereafter. The chart below shows the amount of revenues from the marijuana excise tax and the distributions of the funds as estimated by the September 2016 economic and revenue forecast.

Marijuana Revenue Appropriations

Projected revenue from the **September 2016** Forecast as adopted by the Economic and Revenue Forecast Council
2013-15: Actuals
2015-17: Current appropriations and set percentages
2017-19: Set percentages and minimum appropriations or FY 2017 amount, if larger
(In Dollars)

	2015-17		2017-19	
	FY 16	**FY17**	**FY 18**	**FY 19**
Projected Revenue				
Taxes	$165,122,424	$295,542,544	$346,269,111	$372,313,698
Licenses	2,928,476	2,420,375	2,410,108	2,410,096
Total Revenue-Dedicated Marijuana Account	**168,050,900**	**297,962,919**	**348,679,219**	**374,723,794**
Appropriations with Set Amounts				
DSHS-Youth Survey*[1]	(500,000)	(500,000)	(500,000)	(500,000)
DSHS/WSIPP*[2]	(200,000)	(200,000)	(200,000)	(200,000)
UW-Public Education Materials*[3]	(20,000)	(20,000)	(20,000)	(20,000)
DES/Building Council*[4]	(95,000)			
LCB Appropriation*	(7,736,000)	(8,481,000)	(8,481,000)	(8,481,000)
Net to Distribute	**159,499,900**	**288,761,919**	**339,478,219**	**365,522,794**
Distribution of Net Above (using minimums in statute or set %)				
DSHS-Appropriation*[5]	12,814,000	27,786,000	27,786,000	27,786,000
DOH-Appropriation*[6]	7,500,000	7,500,000	9,750,000	9,750,000
UW-Appropriation*[7]	207,000	207,000	1,021,000	1,021,000
WSU-Appropriation*[8]	138,000	138,000	681,000	681,000
Basic Health Plan Trust Account-Trsfer**[9]	79,750,000	144,381,000	169,739,000	182,761,000
OSPI-Appropriation*[10]	251,000	511,000	511,000	511,000
HCA-Appropriation***[11]	7,791,000	12,979,000	16,974,000	18,276,000
Total Distributions before GFS	**108,451,000**	**193,502,000**	**226,462,000**	**240,786,000**
Net - GFS Transfer******	**$51,048,900**	**$95,259,919**	**$113,016,219**	**$124,736,794**
One-time Transfer to the Basic Health Plan Trust Account**[9]	$14,000,000			
GFS distribution to locals	$6,000,000	$6,000,000	$15,000,000	$15,000,000

* 2015-17: Amounts are appropriations from 2ESHB 2376.

* 2017-19: LCB appropriations are the same as FY 2017; the other amounts are the set amounts or minimums in RCW 69.50.540, except where the FY 2017 amount is larger than the minimum. In this case, the FY 2017 amount is carried forward to 2017-19.

**Amount of the transfer to Basic Health Plan Trust Account is 50% of the "net to distribute" per RCW 69.50.540, plus $14,000,000 (E2SHB 2376, Sec. 8

*** 2015-17: Amounts are the appropriations from 2ESHB 2376. 2017-19: Amount is 5% of the "net to distribute."

**** Amount to GFS is the residual of current revenues less all other appropriations and transfers. Differences from June 2016 forecast are due to rounding.

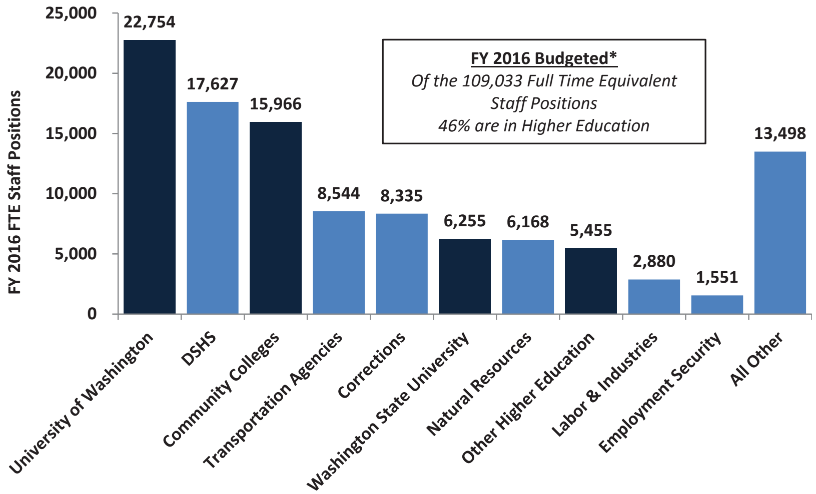
1. DSHS-Youth Survey: The Department of Social and Health Services is directed to design and administer the Washington State Health Youth Survey at least every two years. The survey must include questions on, but not limited to, academic achievement and age at time of substance use initiation.
2. DSHS/WSIPP: DSHS is directed to contract with the Washington State Institute for Public Policy to conduct the cost-benefit evaluation and produce the reports described in RCW 69.50.550.
3. UW-Public Education Materials: University of Washington Alcohol and Drug Abuse Institute for the creation, maintenance and timely updating of Web-based public education materials providing medically and scientifically accurate information about the health and safety risks posed by marijuana
4. DES/Building Council: Funding for the Department of Enterprise Services to develop and adopt fire and building code provisions related to marijuana processing and extraction facilities.
5. DSHS-Appropriation: Funding for the development, implementation, maintenance and evaluation of programs and practices aimed at the prevention or reduction of maladaptive substance use, substance-use disorders, substance abuse or substance dependence. Also, funding for mental health services for children and youth, and services for pregnant and parenting women.
6. DOH-Appropriation: Funding for the creation, implementation, operation and management of a marijuana education and public health program that includes a public health hotline that provides referrals to substance abuse treatment providers. Also, funding for a grant program to local health departments for intervention strategies for the prevention and reduction of marijuana use by youth.
7. UW-Appropriation: Funding for research on the short- and long-term effects of marijuana use and to assess if other states or private entities are conducting marijuana research in areas that might be useful to the state.
8. WSU-Appropriation: Funding for research on the short- and long-term effects of marijuana use and to assess if other states or private entities are conducting marijuana research in areas that might be useful to the state.
9. Basic Health Plan: Funding for health care services.
10. OSPI-Appropriation: Funding for grants to support the Building Bridges programs.
11. HCA-Appropriation: Funding for community health centers to provide primary health and dental care services.

Employee Compensation and Benefits

Salaries and Health Care

Key Facts

- 2015-17 Salary and Benefits – all agencies and higher education:
  - Near GF-S and Opportunity Pathways: $6.2 billion (16% of total expenditures)
  - Total Funds: $18.9 billion
- PEBB Subscribers, including retirees and local government: 362,000
- State employees including higher education (FTEs): 109,000



Reflects operating omnibus and transportation budgets, excluding the approximately 2,750 positions funded in the capital budget.

General Government

Generally, salaries and health care costs for general government employees that are represented are established and modified in labor contracts that are collectively bargained biennially. Salaries and health care costs for non-represented employees are generally set based on policy guidelines and practical restrictions on implementation. Historically across-the-board salary increases and health care provisions that have been applied to represented employees have been extended to non-represented employees.

Higher Education

Higher education institutions have a mix of represented and non-represented employees. Higher education institutions have greater flexibility than state agencies in establishing salary levels for most of their employees, including faculty and exempt staff.

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Collective Bargaining

The Labor Relations division of the Office of Financial Management (OFM) negotiates contracts with unions representing general government and transportation employees.

Four-year state colleges and universities generally negotiate collective bargaining agreements directly with the labor organizations that represent their employees rather than having OFM conduct the negotiations.

Washington Management Service and exempt employees of certain agencies (such as OFM, the Department of Personnel, and legislative and judicial agencies) are all precluded from forming bargaining units.

In addition to agreements with unions representing state and higher education employees, OFM also negotiates agreements for certain groups of non-state employees pursuant to separate collective bargaining statutes.

State Employee Labor Unions	
General Government	
Teamsters Local Union 117	6,000
Washington Federation of State Employees - DOC unique classification only	1,040
Washington Federation of State Employees	30,000
Washington Public Employees Association	2,300
Professional and Technical Employees Local 17	2,300
SEIU Local 1199NW	800
Coalition of Unions	600
WAFWP	500
Higher Education Community College Coalitions	
WFSE Higher Education CCC	3,300
WPEA Higher Education CCC	1,900

Excludes WSP and WA State Ferry Unions

Non-State Employee Group Unions	
SEIU 925 - Child Care Providers	8,000
SEIU 775 - Individual Home Care Providers	30,000
WFSE - Language Access Providers	900
Adult Family Home Council - Home Owners	2,600

Legislative Approval Process

If the Governor deems the agreements to be financially feasible the Legislature may either approve or reject the request for funds to implement agreements as a whole. It may not reject parts of an agreement selectively. The approval or rejection may be made in the budget bill or through separate legislation. If the contracts are rejected, either the bargaining unit or OFM may reopen negotiations.

If the legislature does not approve a tentative agreement, the terms and conditions in the current agreement remains in effect for up to one additional year unless a new agreement is reached and approved by the legislature before that date. This is known as the "tail."

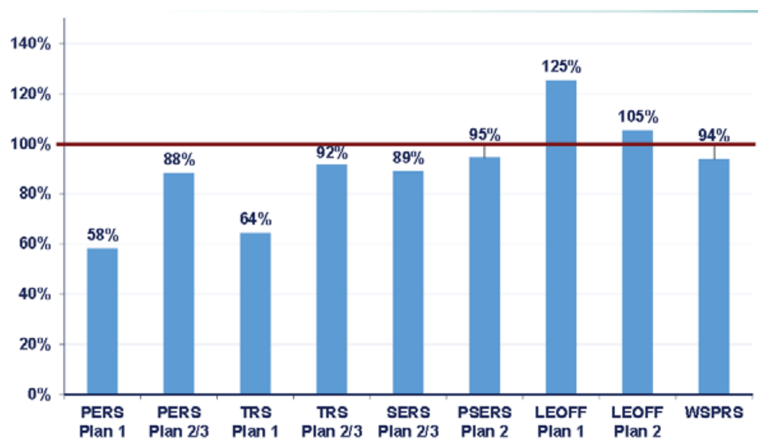
Size and composition of the state workforce is not subject to collective bargaining under RCW 41.80.040, so the Legislature may implement permanent reductions. Certain elements of the implementation, such as which employees are laid off first, would be governed by the labor agreements. Within the terms of the labor contracts, the Legislature may also mandate either temporary layoffs of up to 30 calendar days or a temporary reduction in hours to no less than 20 hours per week for no more than 120 calendar days in a year.

Pensions

Key Facts

- $1.7 billion 2015-17 Near GF-S and Opportunity Pathways in employer contributions
  - $4.3 billion 2015-17 total state funds
- $260 million 2017-19 Near GF-S and Opportunity Pathways contribution increase
  - $359 million 2017-19 increase all state funds
- 15 plans in 8 systems
- 309,565 active members – working and contributing to the plans
- 171,587 annuitants – retirees, beneficiaries and others who receive monthly payments

Funded Status by Plan – June 2015



Note: Liabilities valued using Entry Age Normal Cost method. This is not used to determine contribution rates.

2015-2017 Budget Recap

Salary increases for represented and non-represented employees – summary of key provisions:

General Government

- Wage increases (including non-represented employees):
  - 3.0 percent, effective July 1, 2015, and
  - 1.8 percent for employees who earn > $2,500/month or 1% plus $20/month for all employees who earn <$2,500/month, effective July 1, 2016
- Salary adjustments for targeted classifications and shift premiums

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DOC Wage Increase

- 5.5 percent, effective July 1, 2015 and
- 4.3 percent, effective July 1, 2016

Employee Health Benefits Agreement

- State to fund an average of 85% of health care premium costs
- Employee wellness program incentive of at least $125 per year.

Collective bargaining agreements and arbitration awards for non-state employees:

- Home care individual providers:
  - Wage scale increases to include a starting wage of $12 per hour and a top wage of $15.40 per hour
  - Increase of $0.66 per hour over two years for health care contributions
  - New retirement benefit contribution of $.23 per hour.
- Language access providers:
  - Hourly rate increases of $1.10 per hour in FY 2016 and $.90 in FY 2017
- Adult family home providers:
  - 5% increases in both the daily rate and in the expanded community service daily rate, in each fiscal year;
- Child care providers:
  - 2% increases in both the base rate and the base hourly rate for unlicensed providers, effective July 1, 2016.

State pension contributions:

State pension contributions were fully funded for state, school district, and local government law enforcement and firefighter employees at the levels recommended by the State Actuary and the Pension Funding Council. The rates reflected higher costs due to four primary factors:

1. An increase in required contributions for Plan 1 unfunded liabilities
2. Delayed recognition of past investment losses
3. Reduction in the long-term investment return assumption from 7.9% to 7.8%
4. Adoption of new mortality tables to recognize improvements in life expectancy

Current Budget Issues

2017-19 collective bargaining tentative agreements and awards – summary of key provisions:

General Government

- Wage increases (except DOC):
  - 2.0 percent, effective July 1, 2017
  - 2.0 percent, effective July 1, 2018
  - 2.0 percent, effective January 1, 2019
- Salary adjustments for targeted classifications
- $12 minimum wage (nominal impact)
- $1 Shift Premium – Nights and Evenings
- Health Care - 85% Employer / 15% Employee

- Changes to annual vacation leave accrual rates:
  - 0 - 24 hours per year depending on years of service
  - New schedule maxes out at 25 years instead of 16

DOC Wage Increase (arbitration):
  - 4.5 percent, effective July 1, 2017
  - 3.0 percent, effective July 1, 2018
  - 3.0 percent, effective January 1, 2019

Employee CBA & Award Cost Estimates ($ in thousands)	NGFS-P 2017-19 Total	Total Funds 2017-19 Total	NGFS-P 4-Year Outlook	Total Funds 4-Year Outlook
Total Represented Employees	$352,158	$709,524	$822,336	$1,632,769
Non-Represented Employees (aka parity)*	$205,946	$440,899	$542,503	$1,161,849
Total:	**$558,104**	$1,150,423	**$1,364,839**	$2,794,618

All figures are early rough estimates calculated by OFM HR for the purposes of bargaining and include wages, health care, other economic benefits, and back fill for added vacation leave accruals. Totals may differ from what is submitted with the Governor's budget.

**Non-represented employee parity assumes the three 2% wage increases and health care cost provisions.*

Non-State Employee Union Agreements

Home Care Individual Providers (SEIU 775)
- Increases to hourly wages and
- Additional wage step for those at the top of the wage scale
- Increased contributions to the retirement, health care and training trusts.

Language Access Providers (WFSE).
- Rate increases:
  - $0.50/hour for fiscal year 2018
  - $1.26/hour for fiscal year 2019.

Family Child Care Providers (SEIU 925)
- 2.0 percent rate increase for licensed providers
- $2.50/hour/child increase for licensed-exempt providers
- Increased funding for health care for licensed providers; increases in professional development days, licensing incentives and need-based grants; and establishment of a family child care career development fund.

Adult Family Home Providers (Adult Family Home Council)
- Increases in the daily rates.
- Payments to providers for providing meaningful home-based activities
- Payments to providers supporting clients in accessing and participating in the community integration program
- Mileage reimbursement

Non-Employee CBA Cost Estimates ($ in thousands)	NGFS-P 2017-19 Total	Total Funds 2017-19 Total	NGFS-P 4-Year Outlook	Total Funds 4-Year Outlook
Total:	**$145,355**	$296,722	**$359,969**	$738,349

All figures are early rough estimates calculated by OFM HR for the purposes of bargaining and include wages, health care, other economic benefits, and back fill for added vacation leave accruals. Totals may differ from what is submitted with the Governor's budget.

2017-19 pension rate increases:

Increases to the state retirement plan rates for 2017-19, as adopted by the Pension Funding Council, are based primarily on two factors:

1. Reduction in the long-term investment return assumption from 7.8% to 7.7%, and
2. Adoption of the second phase of the new mortality tables to recognize improvements in life expectancy.

Contribution Rates

	Employee 15-17	Total Employer 15-17	Employee 17-19	Employer Normal 17-19	Employer UAAL 17-19	Total Employer 17-19
PERS 1	6.00%	11.00%	6.00%	7.49%	5.03%	12.52%
PERS 2	6.12%	11.00%	7.38%	7.49%	5.03%	12.52%
TRS 1	6.00%	12.95%	6.00%	7.83%	7.19%	15.02%
TRS 2	5.95%	12.95%	7.06%	7.83%	7.19%	15.02%
SERS 2	5.63%	11.40%	7.27%	8.27%	5.03%	13.30%
PSERS	6.59%	11.36%	6.73%	6.73%	5.03%	11.76%
LEOFF 1	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
LEOFF 2	8.75%	8.75%	8.75%	8.75%	0.00%	8.75%
WSPRS 1/2	6.69%	8.01%	7.34%	12.81%	0.00%	12.81%

Employer rates exclude the 0.18% administrative expense rate collected by the Department of Retirement Systems.

Rates shown for 2017-19 are based on the 2015 Actuarial Valuation. The LEOFF Plan 2 rates were adopted by the LEOFF Plan 2 Retirement Board. All other rates were adopted by the Pension Funding Council and include lowering interest rate assumption from 7.8 to 7.7% and the second step of mortality improvements. All rates are subject to change by the Washington State Legislature.

Plan 1 members' contribution rate is statutorily set at 6.0%. Members in Plan 3 do not make contributions to their defined benefit.

In the LEOFF plans only, the state pays a percent of the total cost of benefits.

2017-19 cost increase of contributions to higher education supplemental retirement benefits:

The estimated benefit payments and benefit fund contributions to higher education supplemental retirement benefits will total about $39 million for the 2015-17 biennium. Early projections, based on key economic assumptions, indicate that costs could increase to $52 million for the 2017-19 biennium, and to over $118 million in the next five biennia.

K-12 Education

Washington State provides funding for basic and non-basic education through appropriations to the Office of the Superintendent of Public Instruction (OSPI). Funding for the nine regional Educational Service Districts (ESDs) is also provided through OSPI's budget. Of the total appropriated to OSPI, over 99 percent is subsequently distributed to school districts across the state. Less than one percent is for OSPI itself, the ESDs, and statewide programs (i.e. grants that are managed centrally).

Key Facts

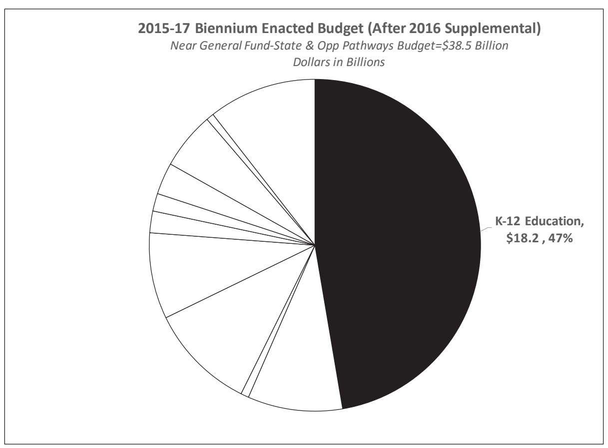
- K-12 Public School appropriations, 2015-17 Biennial Budget: $18.2 billion, Near GF-S and Opportunity Pathways
- School districts' operating fund sources for school year 2014: State funds (69%), Federal (8%), Local Taxes (19%), Other (4%)
- Number of K-12 students: 1,029,018*
- Number of schools: 2,300
- Number of school districts: 295; Tribal Compacts: 3; and Charter Schools: 9.
- K-12 staff in school year 2015, all fund sources: 110,611 (66,223 teachers and other certificated staff; 4,513 administrators; and 39,874 support staff)

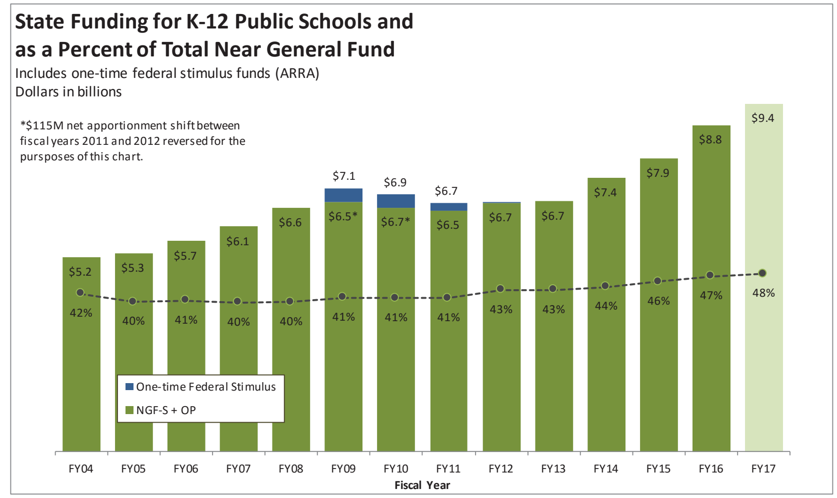
* Projected full-time-equivalent students for school year 2016

More detailed descriptions of the organization and funding of the state's public schools can be found in the Senate Ways & Means publication, "A Citizen's Guide to Washington State K-12 Finance." It can be found online at: http://www.leg.wa.gov/SENATE/COMMITTEES/WM/Pages/default.aspx.

Trend/Overview Information

K-12 education is the largest single part of the Near GF-S and Opportunity Pathways budget, making up 48 percent of the total. The following charts display the history of K-12 appropriations, as well as the percentage of the Near-General Fund State budget allocated to K-12.





Recent Basic Education Legislation Affecting K-12 Funding

In the 2009-11 biennium, two major pieces of legislation were enacted to redefine the program of basic education and restructure K-12 funding formulas. The first was ESHB 2261 (Chapter 548, Laws of 2009) which added programs to the definition of basic education — including the program for highly capable students and phasing in all-day kindergarten. It increased the number of instructional hours, increased the minimum number of credits for high school graduation, and changed the system for funding student transportation. The bill also created the framework for a new K-12 funding allocation formula based on prototypical schools. Changes took effect September 1, 2011 and most enhancements are to be phased in by 2018 on a schedule set by the Legislature. The second bill, SHB 2776 (Chapter 236, Laws of 2010), enacted in statute the funding formulas for the new prototypical schools format at levels that represented what the state was spending on basic education at the time. It set targets for class-size reduction in the lower grades and established a timeline for phasing in certain enhancements to the program of basic education and the new funding levels. The new funding model is intended to provide greater understanding about how state funds for K-12 are allocated to school districts, and to improve accountability. The bills require school-district reporting of actual staffing and expenditures, compared to the funding provided in the prototypical model. The comparisons are to be available on a public website of the Office of the Superintendent of Public Instruction, and can be found at this link: http://www.k12.wa.us/SAFS/INS/2776/Portal.asp.

2015-17 Budget Recap

As reflected in the table below, the enacted 2015-17 budget (after the 2016 supplemental) provided $18.2 billion for K-12 public schools. This represents a $2.9 billion or 19 percent increase from the estimated expenditures for the 2013-15 biennium.

2015-17 State Funding for K-12 Public Schools (After 2016 Supp) *Near GF-S & Opp Pathways in Millions*	
Estimated 2013-15 Expenditures for K-12 Public Schools	***15,261.9***
Compensation & General K-12 Items	
Continuation of 2013-15 Education Increases*	621.9
Enrollment & Workload changes	276.7
I-732 Cost of Living Adjustment	231.0
Pension Increases	210.2
Additional Salary Increase	152.3
All Other K-12 Increases	163.9
Increased Health Benefit Allocation	24.4
Compensation & General K-12 Items	***1,680.4***
New SHB 2776/Basic Education Items	
Completed Phase-in of Materials, Supplies, and Operating Costs	741.5
Continued Phase-in of K-3 Class Size Reductions	332.8
Completed Phase-in of All-Day Kindergarten	179.8
New SHB 2776/Basic Education Items	***1,254.1***
2015-17 Appropriations for K-12 Public Schools	**18,196.4**
Dollar Increases Above 2013-15	*2,934.5*
Percentage Increase Above 2013-15	*19.2%*

** Includes continued funding for basic education increases from the prior biennium, including: full funding of the pupil transportation funding formula; full funding of the increased high school instructional hours and graduation requirements; and continued phase-in of all-day Kindergarten, K-3 class size reductions, and Materials, Supplies, and Operating Costs.*

A total of $1.3 billion was provided for the implementation of basic education requirements of SHB 2776 (Chapter 236, Laws of 2010). This includes: (1) $741.5 million to complete implementation the materials, supplies, and operating costs (MSOC) component of the prototypical school funding formula; (2) $332.8 million to reduce class sizes in grades kindergarten through third grade with priority given to the earliest grades and high-poverty elementary schools; and (3) $179.8 million to complete implementation of state-funded all-day kindergarten by school year 2016-17, one year ahead of the statutory deadline.

Other major increases included: (1) $621.9 million for the continuation of 2013-15 education increases, including the previous installments of the SHB 2776 (Chapter 236, Laws of 2010) enhancements; (2) $276.7 million for more technical enrollment and workload changes; (3) $231.0 million for the Initiative 732 Cost of Living Adjustment; (4) $210.2 million for the K-12 related costs associated with higher pension contribution rates; (5) $152.3 million for a one-biennium salary increase beyond the amounts

specified in Initiative 732; and (6) $24.4 million to increase health benefit allocations for certificated instructional, certificated administrative and classified staff while maintaining the classified health benefit factor.

Generally, cost-of-living adjustments (COLAs) for K-12 employee salaries are governed by the provisions of Initiative 732, state salary conditions and local collective bargaining. With respect to health benefits, K-12 school districts have broad authority to determine health plan benefits and premiums for their employees. A few districts provide benefits through the Public Employee Benefits Board (PEBB) of the Health Care Authority (HCA). Most districts adopt benefits through collective bargaining. Additionally, all school district retirees have the same opportunity to purchase continuing coverage through PEBB that is provided to retired state employees.

The largest reduction from the K-12 maintenance level was associated with the suspension of Initiative 1351 (I-1351). The fiscal impact of the phase-in requirements of Initiative 1351, which changed the state's funding requirements for class size and staffing formulas, was estimated at $2 billion for the 2015-17 biennium. Chapter 38, Laws of 2015, 3rd sp.s. (EHB 2266) delayed the phase-in dates for I-1351 by four years, resulting in savings in the 2015-17 biennium.

Current Budget Issues

McCleary v. Washington State: In January, 2012, the Washington Supreme Court held that the state had not complied with its Article IX, section 1 constitutional duty to make ample provision for the basic education of all children in Washington. The court did acknowledge the recent enactment of sweeping reforms under Chapter 548, Laws of 2009 (ESHB 2261), and acknowledged the current progress toward implementing those reforms. The Court also noted that, if fully funded, the reform package will remedy deficiencies in the K-12 funding system. The Court retained jurisdiction to help "facilitate progress" in the State's plan to fully implement the reforms by 2018.

In August 2015, the Washington State Supreme Court issued contempt sanctions of $100,000 per day until the Legislature submits a plan for fully funding its obligations in the McCleary v. State of Washington lawsuit. The Court requested that the Legislature keep this fine in a separate account and to use the funds for the benefit of basic education. Beyond the four budgeted funding enhancements of SHB 2776 (Chapter 236, Laws of 2010) – pupil transportation, MSOC, full-day kindergarten, and K-3 class size funding, the Court made specific references to the adequacy of K-12 funding for K-12 employee salaries and capital space needs.

In October 2016, the Court released its latest order addressing the state's progress in achieving full compliance under the McCleary decision. The order maintains the monetary sanction of $100,000 per day and requires the state to file its post-session report and a brief addressing the adequacy of the state's compliance within 30 days after the governor signs the final biennial operating budget after the 2017 session. The order also states that based on the relevant legislation, the state has until September 1, 2018, to fully implement its program, and that the remaining details of the program, including funding sources and appropriations, must be in place by the final adjournment of the 2017 session.

Education Funding Task Force: Chapter 3, Laws of 2016 (E2SSB 6195) established an Education Funding Task Force (EFTF) to review the data and analysis provided by an independent professional consultant regarding K-12 public school staff compensation. The EFTF must, at a minimum, make recommendations and provide any supporting legislation by January 9, 2017, regarding: possible compensation adjustments sufficient to hire and retain staff and whether future salary adjustments, a local labor market adjustment, or both, should be incorporated into the salary allocation model, and if so, the method in which such adjustments should be made.

Initiative Measure No. 1351 (I-1351): Approved by the voters in November 2014, I-1351 reduced class sizes and increased staffing formulas. Chapter 38, Laws of 2015, 3rd sp.s. (EHB 2266) suspended I-1351. Originally, the initiative was scheduled to be phased in over two biennia beginning with the 2015-17 biennium. The 2015 changes delay the implementation of the initiative by four years. I-1351 will now be partially phased in during the 2019-21 biennium and fully implemented in the 2021-23 biennium. The estimated fiscal impact is approximately $2 billion in the 2019-21 biennium depending on implementation decisions.

Capital Space Needs: As basic education is redefined and enhanced by the Legislature, school districts have expressed capacity issues within their current capital facilities to accommodate these changes. Since 2003, capital budget appropriations have directed OSPI to count kindergarten students as full-time for the state's school construction assistance funding formula. In 2012, this change was adopted into statute. While no changes have been made to the school construction assistance program (SCAP) to account for the lowering of K-3 class size requirements, the Legislature appropriated $200 million for the 2015-17 biennium for a pilot program of competitive grants for state funded class reduction efforts and all-day kindergarten requirements. The Legislature is continuing to explore ways to determine the actual capacity needs associated with the K-3 class size provided in Chapter 236, Laws of 2010 (SHB 2776). The biennial budget included funding and direction to OSPI and Washington State University to increase data collection efforts about school construction inventory and costs for the Legislature to consider during future budget development.

Charter Schools: Voters approved Initiative 1240 in 2012, the initiative allowed for the phased establishment of up to 40 charter schools in the state of Washington. As of the fall of 2016, 9 charter schools with approximately 1,300 students are operating in the state.

In September, 2015, the Washington Supreme Court ruled the charter school law unconstitutional. The Court found that charter schools are not common schools because they are not subject to and under the complete control of the qualified voters of the school district. The Court also found that since charter schools are not common schools, they cannot receive funds from the common school construction fund or be funded by the common school state property tax because the state constitution requires both to be used exclusively for common schools. The Court declared that because the charter school law could not be implemented without the impermissible funds the law in its entirety was unconstitutional and void.

Chapter 241, Laws of 2016 (E2SSB 6194) reenacted and amended Initiative 1240 to designate charter schools as public schools that are not common schools operating separately from the common school system. Charter schools are now funded through the Washington Opportunity Pathways Account.

Higher Education

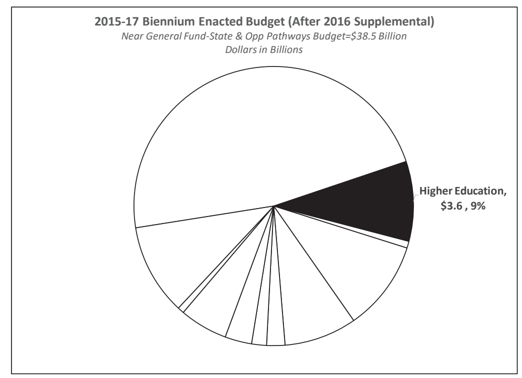
Public higher education is comprised of two research universities, four regional universities, and 34 community and technical colleges. Budgeted enrollment, tuition, and financial aid are interconnected levers that drive the higher education budget. State dollars[1] fund financial aid and, along with tuition, the core academic functions[2] delivered by higher education institutions.

Key Facts

- 2015-17 Biennium (2016 Supplemental) Enacted Budget: $13.9 billion total funds; $3.6 billion state funds; $2.9 billion tuition
- Portion of core academic functions funded with state funds (four-year institutions): 42.1%
- Portion of core academic functions funded with state funds (two-year institutions): 67.6%
- State-Funded FTE Enrollment 2014-15 academic year (most current data available): 233,441 (budgeted); 246,660 (actual)
- Four-Year School Degree production, 2014-15 academic year (most current data available):
  - 24,885 undergraduate degrees
  - 7,813 graduate degrees
- Two-Year Degree/Certificate production, 2014-15 academic year (most current data available):
  - 10,222 applied associate degrees
  - 286 applied baccalaureate degrees
  - 15,822 certificates
  - 18,491 academic transfer degrees

Overview/Trend Information

Of the $38 billion state budget, higher education represents 9% of the state budget (which increases to 11% if you include higher education's portion of debt service).



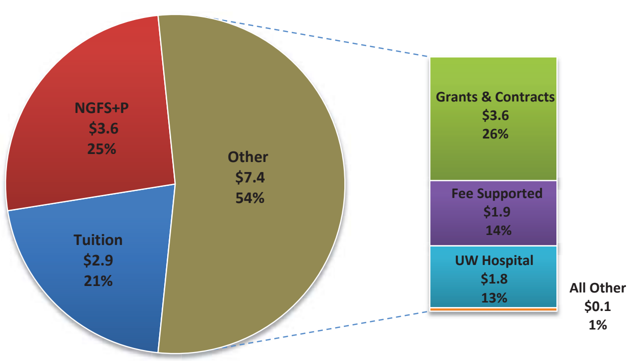
[1] State funds include the Near General Fund, Opportunity Pathways Account, Opportunity Express Account, Education Legacy Trust Account, and select expenditures from building accounts.

[2] Core academic functions include the cost of instruction, state sponsored research, and public service activities.

Higher Education Funding

Higher education funding, like most areas of the state budget, is comprised of more than Near GF-S and Opportunity Pathways. For the 2015-17 biennium, the total budget for higher education is approximately $13.9 billion (representing about 17% of the overall state budget). About 25% of this amount comes from Near GF-S and Opportunity Pathways ($3.6 billion).

2015-17 (After 2016 Supplemental) Biennium
Total Higher Education Operating Budget by Fund Sources
Dollars in Billions

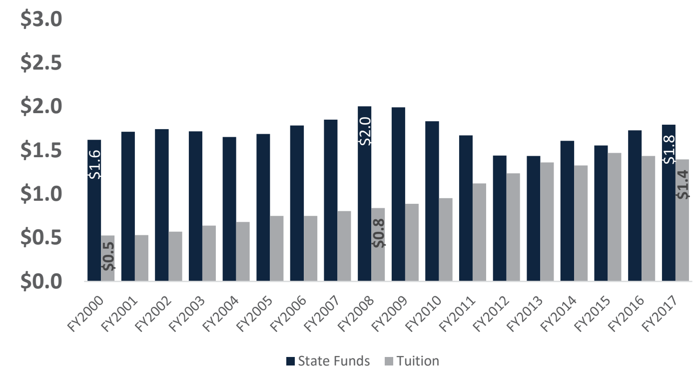


State Share of Core Academic Functions

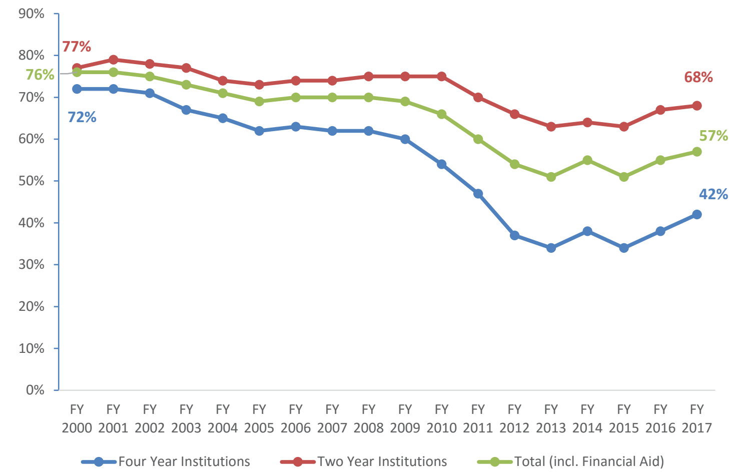
After adjusting for inflation, funding for core academic functions has increased by approximately 2.5% per year since FY 2000. The portion of core academic functions paid for with state funds versus tuition[3] has also changed over time. The average annual growth rate since FY 2000 for state funds increased by 1.0% while tuition increased by 6.1%. As a result, state funding has declined relative to tuition and now represents 68% in the community and technical college system and 42% in the four-year institutions, even after accounting for the increases in state appropriations provided for the 2013-15 and 2015-17 biennia and the reductions in resident undergraduate tuition in the 2015-17 biennium. See charts on the following page.

[3] Tuition includes all student categories and not just resident undergraduate.

State Funds and Tuition Portions of Core Academic Functions
2016 Constant Dollars in Billions



State Funds Share by Institution Type



Enrollment and Completion

Since the 2009-10 academic year, the four-year institutions have been increasing their enrollments by an average of 1,874 per year and their degrees awarded by an average of 601 per year. Enrollments for the community and technical colleges have been dropping by an average of 12,483 per year since 2009-10. The CTCs have continued to produce annual increases in degrees and transfers, but have experienced negative annual growth in certificates since 2013-14.

PUBLIC FOUR YEAR INSTITUTIONS	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
State-Funded Enrollments (Headcount)						
Undergraduate	100,196	102,014	104,810	105,798	106,821	108,795
Graduate	25,052	25,358	24,668	24,775	24,961	25,821
Total	125,248	127,372	129,478	130,573	131,782	134,616
Degrees Awarded						
Undergraduate	22,829	23,487	24,363	24,417	24,100	24,885
Graduate	6,864	7,211	7,423	7,590	7,581	7,813
Total	29,693	30,698	31,786	32,007	31,681	32,698
Annual Percent Change						
Headcount Enrollments		1.7%	1.7%	0.8%	0.9%	2.2%
Degrees Awarded		3.4%	3.5%	0.7%	-1.0%	3.2%

STATE BOARD OF COMMUNITY AND TECHNICAL COLLEGES	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
State-Funded Enrollments (Headcount)	338,109	330,608	305,709	292,119	283,408	275,695
Degrees/Academic Transfer						
Applied Associate Degree	8,064	9,875	10,689	10,298	10,403	10,222
Applied Baccalaureate Degree	51	138	155	192	244	286
Academic Transfers	13,973	16,183	16,747	17,492	17,439	18,491
General Studies (non-transfers)	331	376	410	401	379	425
Total	22,419	26,572	28,001	28,383	28,465	29,424
Certificates (Workforce Training)	20,851	22,521	22,697	24,624	21,352	15,822
High School Completion	6,224	6,274	6,082	5,924	5,751	3,553
Annual Percent Change						
Headcount Enrollments		-2.2%	-7.5%	-4.4%	-3.0%	-2.7%
Degree/Academic Transfers		18.5%	5.4%	1.4%	0.3%	3.4%
Certificates (Workforce Training)		8.0%	0.8%	8.5%	-13.3%	-25.9%

2015-17 Budget Recap

For the 2015-17 biennium, a total of $3.6 billion in state funds was provided in support of the higher education system (including financial aid); $2.8 billion (79%) of which is appropriated to the public colleges and universities. Compared to the 2013-15 biennium, this represents a $474 million (20%) increase in state funds to the institutions of higher education and a $480 million (15%) increase in state funds to the higher education system overall.

Resident undergraduate tuition (RUG) was reduced under the College Affordability Program (2ESSB 5954). Starting in the 2015-16 academic year, the tuition operating fee is reduced by 5 percent from the 2014-15 academic year level for all institutions of higher education. In 2016-17, the tuition operating fee is reduced another 10 percent from the 2015-16 academic year for the research institutions and another 15 percent for the regional institutions.

Major Increases:

2015-17 Biennium Enacted Budget. As required under the College Affordability Program, the legislature appropriated $113 million in state funds for the estimated reduction in net revenues from the tuition reductions. This amount included $158 million to the institutions of higher education for net tuition reductions and a $45 million offset to financial programs due to lower tuition award amounts.

The legislature also increased funding by $41 million for the Opportunity Scholarship Program; $11.5 million for a new Washington State University medical school ($2.5 million) and to continue the University of Washington's current medical school in Spokane ($9 million); and $16 million for increased computer and engineering enrollments.

2016 Supplemental Enacted Budget. The legislature appropriated an additional $7.8 million in state funds, above the amount provided in the 2015-17 Biennium Enacted Budget, to the institutions of higher education to replace the loss of tuition revenue resulting from the reductions specified in the College Affordability Program.

The legislature also shifted $18 million in one-time caseload savings from the College Bound Scholarship (CBS) Program to the State Need Grant (SNG) Program to maintain FY 2015 service levels for FY 2016 and FY 2017; and provided $3 million to Bellingham Technical College for on-site worker training and skills enhancement training for Alcoa Intalco aluminum smelter workers whose jobs have been impacted by foreign trade and $1.1 million to the Washington Student Achievement Council for the Teacher Shortage Conditional Scholarship and Residency Grant Programs.

Current Budget Issues

State Need Grant. The SNG 2017-19 biennium base budget does not include the $18 million in one-time CBS savings that was shifted to the SNG in the 2016 Supplemental Enacted Budget. This shortfall could impact the program's ability to maintain the FY 2015 service level. In its 2017-19 agency submittal, the Washington Student Achievement Council is requesting additional funding to continue maintaining the SNG service level.

Medical School. Both the University of Washington (UW) and Washington State University (WSU) are requesting additional funding for medical education in their 2017-19 agency submittals. The UW requests $15 million in state funds for the continuation ($5.7 million) and expansion ($9.3 million) of operations at the Washington, Wyoming, Alaska, Montana, and Idaho (WWAMI) Medical School. Having achieved preliminary accreditation in October 2016, WSU requests $10.8 million in state funds for the continued implementation of the medical education program at the Elson S. Floyd College of Medicine.

Higher Education Supplemental Retirement Plans. The institutions of higher education have the ability to offer supplemental retirement plans. The estimated benefit payments and benefit fund contributions (to the higher education supplemental retirement fund) will total about $39 million for the 2015-17 biennium. Early projections, based on key economic assumptions, indicate that costs could increase to $52 million for the 2017-19 biennium, and to over $118 million in the next five biennia.

Tuition. Under the College Affordability Program, RUG tuition operating fees, for all institutions of higher education, may be adjusted for inflation, beginning in the 2017-18 academic year.

State Funding to Replace Tuition Reductions. In the 2016 Supplemental Enacted Budget, the legislature capped the RUG enrollment growth rate used to adjust the FY 2016-17 state backfill funding for the tuition reductions. If annual enrollment at an institution of higher education increases by more than 1% for the 2016-17 academic year, then a 1% growth rate or the institution's preceding five-year average enrollment percentage change may be used – whichever is greater. Also, under the College Affordability Program, the state funding appropriated in the 2015-17 biennium for the tuition reductions will be adjusted for inflation, beginning in the 2017-19 biennium.

Department of Early Learning

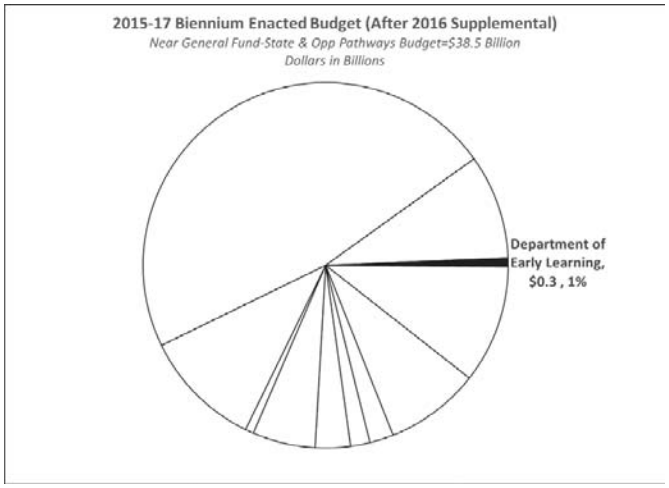
The Department of Early Learning (DEL) was created in 2006 via Chapter 265, Laws of 2006 (2SHB 2964) and is responsible for implementing early learning policy and the coordination of child care and early learning programs. DEL partners with several non-governmental organizations for service delivery and to leverage private funds.

Programs and services include the following:
- Licensure and oversight of licensed child care centers and unlicensed family home child care programs;
- Manage delivery of the Early Childhood Education and Assistance Program (ECEAP);
- Coordinate the Early Achievers, Quality Rating Information System for licensed child care and early learning providers;
- Assist early learning professionals in obtaining education/professional development;
- Contract for evidence-based Home Visiting services through a partnership with Thrive Washington;
- Contract with therapeutic providers who offer child care and treatment to children exposed to environmental, familial, and biological risk factors;
- Establish policy for child care subsidy programs that are funded within the Department of Social and Health Services (DSHS), including the Working Connections Child Care (WCCC) and Seasonal and Homeless Child Care subsidy programs; and
- Coordinate services for infants and toddlers with disabilities or developmental delays through the Early Support for Infants and Toddlers program (ESIT).

Key Facts
- 2015-17 biennial budget, including the 2016 supplemental: $632.0 million total funds; $301.6 million Near GF-S and Opportunity Pathways
- ECEAP, FY 2016:
  - 11,691 funded slots
    - Partial Day ($7,578 per slot): 9,758 slots (83%)
    - Full Day ($10,312 per slot): 1,439 slots (12%)
    - Extended Day ($15,961 per slot): 494 slots (4%)
- Child Care, FY 2015: 54,279 children served
  - WCCC: 49,910 children served
  - Seasonal: 3,740 children served
  - Homeless: 629 children served
- Home Visitation, FY 2015: 8,500 slots
  - 2,100 slots (25%) funded via the Home Visiting Services Account (HVSA)
- Early Support for Infants and Toddlers (ESIT), FY 2016:
  - 7,408 infants and toddlers served

Trend/Overview Information

For the 2015-17 biennium state appropriations to DEL total $301.6 million, which represents 0.8 percent of the $38.5 billion state budget.



The largest driver of the DEL budget is ECEAP, which accounts for 31 percent of the overall budget. ECEAP provides nutrition, health, education, and family support services to children aged 3 and 4 years old from households with income below 110 percent of the federal poverty level and those who are eligible for special education due to a disability. Enrollment is prioritized to children from families with the lowest income, children in foster care, and children from families with multiple needs.

Statute directs that ECEAP will become an entitlement in the 2020-21 school year and the number of slots are to be phased in incrementally each year until full implementation is achieved. Over the last three fiscal years, the legislature has funded an additional 3,300 slots; 350 in Fiscal Year 2014, 1,350 in Fiscal Year 2015, and 1,600 in Fiscal Year 2016.

2015-17 Budget Recap

For the 2015-17 biennium, a total of $301.6 million Near GF-S and Opportunity Pathways was provided to DEL. Compared to the 2011-13 biennium, this represents a $141 million (88%) increase in state funds.

ECEAP

An additional $40.9 million Near GF-S and Opportunity Pathways was provided for ECEAP. These funds were provided to support an additional 1,600 partial day (2.5 hour) slots and to maintain the 1,359 full day (5.5 to 6 hour) and 567 extended day (10 hour) slots added in Fiscal Year 2015.

Chapter 7, Laws of 2015, 3rd Special Session (2E2SHB 1491) delayed full statewide implementation of ECEAP from the 2018-19 school year to the 2020-21 school year and Chapter 128, Laws of 2015 (SSB 5999) directed the Caseload Forecast Council (CFC) to forecast the number of children eligible for and served by ECEAP.

Child Care

Chapter 7, Laws of 2015, 3rd Special Session (2E2SHB 1491) expanded the Early Achievers program and required child care facilities and early learning programs receiving state funds to participate in the Early Achievers program. To implement this legislation, the 2015-17 biennial operating budget provided $91.8 million in state funds, which included $22 million from Near GF-S and Opportunity Pathways for WCCC subsidies to support the twelve month WCCC eligibility provisions required in the Early Start Act, which began on July 1, 2016.

An increase of $10.3 million Near GF-S and Opportunity Pathways was provided for a 2 percent base vendor rate increase for seasonal and homeless child care providers beginning on July 1, 2016; selected base rate increases and tiered reimbursement awards in Fiscal Year 2016 for child care providers participating in the Early Achievers Program; and other items negotiated as part of the Service Employees International Union (SEIU), Local 925 collective bargaining agreement and the corresponding reopener. The funds appropriated to DEL represent approximately 34 percent of the total $30.1 million Near GF-S and Opportunity Pathways provided in the 2015-17 operating budget for these purposes. The remaining funds were provided to Children and Family Services and the Economic Services Administration both housed within the Department of Social and Health Services.

Current Budget Issues

ECEAP Expansion: Chapter 7, Laws of 2015, 3rd Special Session (2E2SHB 1491) delayed statewide implementation of ECEAP until the 2020-21 school year, required child care facilities and early learning programs receiving state funds to participate in the Early Achievers program, and made other early learning changes. ECEAP expansion, child care and ECEAP vendor rates, and early learning quality requirements will likely continue to be in the forefront of fiscal and policy considerations over the next several years. The estimated cost for full implementation in Fiscal Year 2021 is $56 million.

WCCC Wait List: Chapter 7, Laws of 2015, 3rd Special Session (2E2SHB 1491) established a full 12 months of eligibility for WCCC once an individual is approved for the program. As a result, the rate of exit from the program is likely to slow which will produce an increase in the caseload. Current legislative policy is to cap enrollment in the program at 33,000 households and to implement a wait list. It is presently anticipated that the wait list will begin sometime in Fiscal Year 2017. The DEL is requesting an additional $77 million of General Fund-State to eliminate the need for the wait list.

Child Care Collective Bargaining Agreement: The DEL and the Service Employees International Union Local 925 (SEIU 925) have negotiated a new collective bargaining agreement that includes a 2 percent subsidy rate increase for licensed family child care providers; a $2.50 per hour increase to the rate paid to license-exempt family, friends, and neighbors (FFN) providers; and additional funds for professional development. Estimated costs of this agreement are $14 million for the 2017-19 biennium.

Child Care Center Vendor Rate Parity: Prior to the 2016 legislative session, vendor rates for licensed child care centers were on par with family child care providers. In the 2016 supplemental budget, the Legislature, via a collective bargaining agreement reopener, funded an increase in base subsidy rates for family child care providers but did not provide funds for a similar rate increase for child care centers. The DEL is requesting $80 million in the 2017-19 biennium to bring parity to the subsidy rates for child care centers.

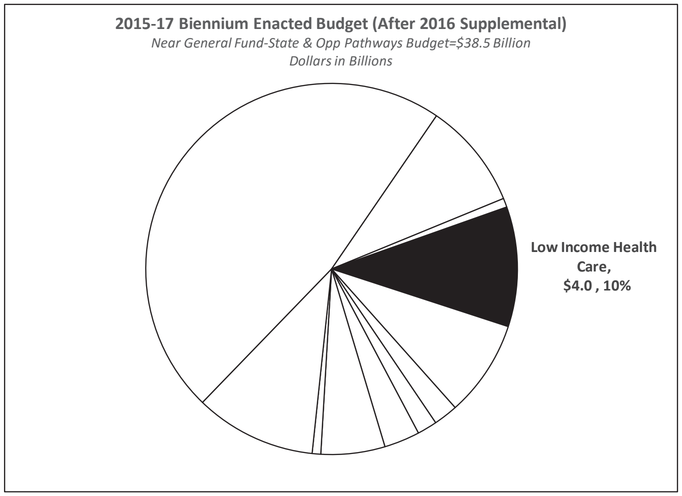
Federal Grant Activities: The federal government recently reauthorized Child Care and Development Block Grant (CCDBG). The DEL is requesting $10.7 million from Near GF-S and Opportunity Pathways to comply with additional requirements placed upon them by the CCDBG, including: (1) yearly monitoring of providers; (2) background checks; (3) additional training services to providers; and (5) data collection.

Low-Income Health Care

Washington is budgeted to spend $16.3 billion during the 2015-17 biennium to cover all or part of the physical health cost of medical and dental care for an average of 1.8 million low-income children and adults. These expenditures are administered by the Health Care Authority, which contracts with managed care insurance plans and directly with hospitals, physicians, dentists, pharmacies, and other medical providers to deliver services under Medicaid.

Key Facts

- Total 2015-17 biennial budget: $4.7 billion Near-General Fund State + Hospital Safety Net, $11.2 billion Federal (primarily Medicaid), and $0.4 billion other state and local funds
- Estimated Lives Covered in FY 2017: 1.8 million or 1 of every 4 Washingtonians, including:
  - ✓ 1 of every 2 children in the state
  - ✓ 1 of every 2 pregnant women
  - ✓ 1 of every 5 adults (non-pregnant, non-elderly)
  - ✓ 1 of every 10 elderly adults
- Average Annual Cost Per Person Covered: $3,781, ranging from $1,645 per year for State Children's Health Insurance Program (SCHIP) to $15,241 per year for non-citizen pregnant women
- Total State Staff: 1,1100 FTE's



Trend/Overview Information

Publicly-funded medical care for low-income people is the third largest component of the state-funds operating budget, after K-12 education and human services programs.

State dollars are only part of how low-income medical spending is financed. Total low-income medical care spending is financed through the Medicaid program - which is a jointly federal-state funded entitlement program. Additional funds for the program come in through the Hospital Assessment program and are used in lieu of state funds for Medicaid hospital services. The total of all funds through the Hospital Assessment program for the 2015-17 biennium total an additional $1.3 billion dollars. The following table shows how the federal and state shares of Medicaid financing have changed and are expected to change. For example, in 2008 the federal and state shares of total costs were roughly the same - 47% and 51% respectively. Ten years later, nearly seven out of every ten Medicaid dollars will be federal. This is largely a result of four factors: Medicaid expansion under the Affordable Care Act, the renewal of the Hospital Safety Net Assessment, Initiative 502 funding, and improved federal match for the Children's Health Insurance Program (CHIP).

Total funding for low-income medical grew by 8.2% from to 2008 to 2017 - with federal funding growing at 12.1% compared to the state share decreasing by 1%. When Near GF-S and Opportunity Pathways is combined with the Hospital Assessment, there is growth of .7%.

Medicaid Enrollment and Funding Changes Over Ten Years
FY 2008 to FY 2017

Population/Funds	Totals 2008	Totals 2017	Percent Share of Total 2008	Percent Share of Total 2017	Avg Annual Growth 2008 to 2017
WA State Population	6,566,666	7,201,457	100%	100%	1.0%
Medicaid Pop.	1,027,493	1,906,535	16%	26%	7.1%
Non-Medicaid Pop.	5,539,173	5,294,922	84%	74%	-0.5%
Fund Source	**$ in millions 2008**	**$ in millions 2017**	**Percent Share of Total 2008**	**Percent Share of Total 2017**	**Avg Annual Growth 2008 to 2017**
Total Funds	**$ 4,436.4**	**$ 8,487.1**	**100%**	**100%**	**8.2%**
NGF-S*	$ 2,263.9	$ 2,059.3	51%	24%	-1.0%
Hospital Safety Net**	$ -	$ 345.0	0%	4%	22.5%
Federal	$ 2,072.0	$ 5,782.4	47%	68%	12.1%
Other Funds	$ 100.5	$ 300.4	2%	4%	12.9%

*NGF-S includes GF-S and Opportunities Pathways
**Hospital Safety Net began in 2010

2015-17 Budget Recap

The 2015-17 all-funds appropriation of $16.6 billion for low-income medical care is a net $2 billion (13.7 percent) increase from the 2013-15 biennium appropriations, and includes a net $181.7 million (4.3 percent) decrease in state-fund appropriations (Near GF-S + Opportunities Pathways).

The majority of the total fund increases ($2 billion) are almost entirely due to Medicaid Expansion under the Affordable Care Act (ACA) continuing, increasing hospital rates under the Hospital Safety Net, Hepatitis C funding, and increased managed care rates. Of the net $2 billion in increases, $1.8 billion is from federal sources. This is offset by reductions in state-fund appropriations ($181.7 million) which are realized primarily through forecast adjustments for all populations, improved federal matching rates for the Children's Health Insurance Program (CHIP), Initiative 502 funding, and the continued funding of the Hospital Safety Net program.

Under the Hospital Safety Net, the state is able to use Hospital Safety Net funds in lieu of Near GF-S and Opportunity Pathways for Medicaid hospital services. This fund shift achieves a net $397 million increase

in state funds by increasing the Hospital Safety Net Account $689 million while offsetting $292 million in Near GF-S and Opportunity Pathways spending. During the 2015-17 biennium this program was expanded to purchase primary care and psychiatric residency slots.

Current Budget Issues

The 2015 supplemental budget contained a veto of the Near GF-S and Opportunity Pathways appropriation assumed for FY 2015 based on three forecast items. These three items resulted in unrealized savings. Two carried into the 2016 supplemental budget. One will be discussed in greater detail below.

- Unachieved LEAN Savings 2015 veto only, no assumptions in 2015-17
- Reimbursement Methods Waiver:
  - 2015-17 - $35.2 million ($16.8 million Near GF-S and Opportunity Pathways)
- Healthier Washington (State Health Care Innovation):
  - 2016 only - $25.9 million ($11.4 million Near GF-S and Opportunity Pathways)

State Health Care Innovation: In December 2014, Washington State received approximately $65 million from the Centers for Medicare and Medicaid Services (CMS) Innovations Fund to implement its State Health Care Innovation Plan. Implementation is expected to slow the growth of state health care costs. This bill also required the creation of an All Payer Claims Database (APCD), collaboration with Department of Social and Health Services to integrate physical and behavioral health rates, and savings attributable to the innovation plan beginning in State Fiscal Year 2016. The Office of Financial Management has selected a vendor for the APCD.

During FY 2015, there were no savings attributable to Healthcare Innovation (Healthier Washington). HCA made a request to restore savings in FY 16 and FY 17 based on lack of Early Adopters for fully integrated behavioral and physical health plans. In 2016, Health Care Authority anticipated saving $1.7 million in Near GF-S and Opportunity Pathways integrating physical and behavioral health in Southwest Washington ($26 million total funds ($11.4 million Near GF-S and Opportunity Pathways) in savings was restored). An additional request has been made by HCA to restore savings in FY17-21 in anticipation of no other integration of behavioral and physical health plans. The requested restoration of savings is $68.5 million ($30.5 million Near GF-S and Opportunity Pathways) per year beginning FY17.

The HCA has received approval for a second waiver from CMS for an additional $2 billion in federal spending authority for parallel innovation strategies. These strategies would require HCA to leverage existing state funds and secure new local funds as the matching dollars. This waiver would be used for Accountable Communities of Health, Long Term Support Services, and Supportive Housing and Employment. There are no Near GF-S and Opportunity Pathways in this budget item.

Hepatitis C: In January 2014, the Food and Drug Administration (FDA) approved Sovaldi as a treatment for Hepatitis C. This drug, in combination with Interferon, is a cure for this condition. Several additional drugs have since been approved. Clinical policy created by Health Care Authority. This policy is followed within Health Care Authority for both Medicaid and Public Employee Benefits (PEB). It is also followed by Department of Health and Department of Social and Health Services (Mental Health and Special Commitment Center). Department of Corrections follows a similar policy.

Both Medicaid and PEB were sued in 2015 and 2016, respectively, resulting in an expanded treatment policy for clients with a lower fibrosis score. Additional competition between available drugs has resulted in lower costs for treatment. Current estimates to treat patients across all fibrosis scores results in additional anticipated costs of approximately $89 million ($13 million Near GF-S and Opportunity Pathways) for the 2015-17 biennium.

Managed Care and Prescription Drug Costs: Increases in managed care rates were the primary driver for Near GF-S and Opportunity Pathways increases during the 2016 legislative session in Low Income Health. This appears to be primarily attributable to prescription drug costs within the managed care population. All populations are seeing increases in drug costs for generic, brand name, and specialty drugs. HCA also saw increasing claims costs for the State Children's Health Insurance Program (SCHIP) and the Blind Disabled populations.

Hospital Safety Net: Under the Hospital Safety Net, the state is able to use Hospital Safety Net funds in lieu of state general fund for Medicaid hospital services. The hospital safety net is set to expire in the 2019-21 biennium. The fiscal impact associated with this expiration is estimated at approximately $300 million per biennium.

Long Term Care and Developmental Disabilities

The Developmental Disabilities Administration (DDA) and Aging and Long Term Support Administration (ALTSA) are administered by the Department of Social and Health Services (DSHS).

Washington is budgeted to spend $3.2 billion Near GF-S and Opportunity Pathways ($7.1 billion total funds) during the 2015-17 biennium to provide aging and long-term support services, which are primarily Medicaid-funded (i.e. state and federal matching funds). Both ALTSA and DDA operate an institutional-based Medicaid entitlement program. The entitlement setting in ALTSA is nursing homes and the entitlement service setting in DDA is Residential Habilitation Centers (RHCs). Both ALTSA and DDA offer Medicaid waiver programs. These programs waive the Medicaid entitlement and offer alternative services to clients in their own homes or community residential settings (i.e. adult family homes and assisted living homes).

Since both ALTSA and DDA primarily provide Medicaid funded services, the Medicaid rules guide the structure and operation of the programs. These rules, and associated case law, significantly limit the state's ability to manage expenditures through program or client eligibility changes.

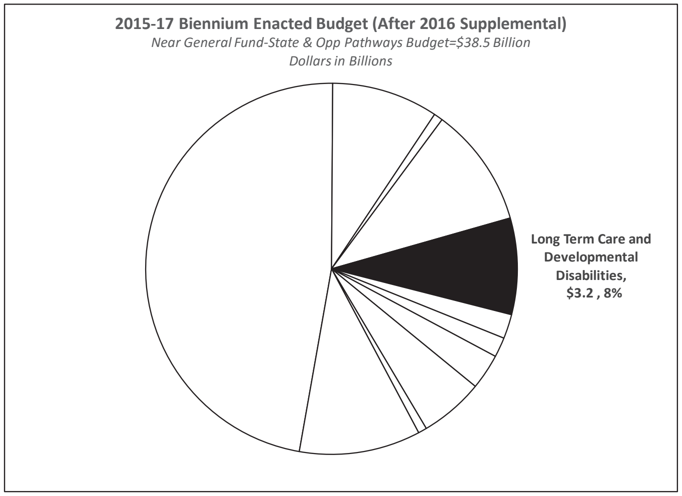
Key Facts

- 2015-17 budget by program:
    - ALTSA: $1.9 billion Near GF-S and Opportunity Pathways ($4.5 billion total funds) and 1,690 FTEs
    - DDA: $1.3 billion Near GF-S and Opportunity Pathways ($2.6 billion total funds) and 3,430 FTEs
- Percent of the program budget that comes from the state: 46%
- Number served and Average Monthly Cost per Client:

Service Setting	Numbers Served	Average Monthly Cost/Client
Nursing Homes	9,700	$ 5,200
ALTSA Community Residential	12,600	$ 1,700
ALTSA In-Home	41,100	$ 2,000
Residential Habilitation Centers	800	$20,300
DDA Community Residential	4,600	$ 8,600
DDA In-Home	11,900	$ 2,300

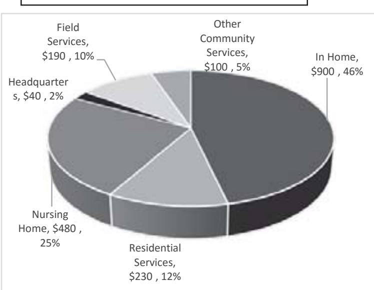
Trend/Overview Information

ALTSA and DDA programs and services account for just over eight percent of the statewide total Near GF-S and Opportunity Pathways for the 2015-17 biennium and roughly 26 percent of total human services budget.

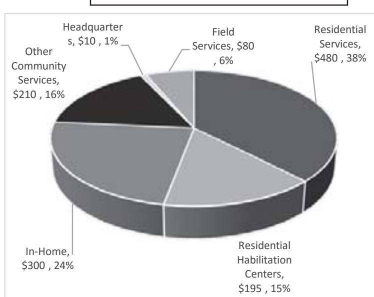


Within ALTSA and DDA, the bulk of Near GF-S and Opportunity Pathways dollars are budgeted for home and community based services.

2015-17 ALTSA Budget
NEAR GF-S Total: $1.9 Billion



2015-17 DDA Budget
NEAR GF-S Total: $1.3 Billion



Over 90 percent of ALTSA and about 30 percent of DDA are forecasted caseload programs. Client caseloads for in-home and residential personal care (both DDA and ALTSA), ALTSA waiver services, and ALTSA entitlement services are modeled and adjusted by the Caseload Forecast Council. These costs are funded in the maintenance level budget. Per capita expenditures for these service areas are modeled and adjusted by joint legislative and executive staff workgroups, and are also adjusted in the maintenance level budget. Unlike ALTSA, DDA residential services beyond personal care are capped. Per capita expenditures for the existing capped client caseload are adjusted in maintenance level. Increases in caseload are explicitly funded by the Legislature at policy level.

Caseload increases are primarily driven by demographic changes, particularly due to the impact of an increasingly aging population. The overall state population is projected to grow at about 1 percent per year, however, the 65 and older population is growing at four times that rate. This impacts growth in the elderly population receiving services, but also impacts adults with developmental disabilities. Roughly 70 percent of the caregivers for adults with developmental disabilities are parents and relatives who are themselves aging and incurring more difficulties in providing care. Per capita cost increases have occurred across both the ALTSA and DDA populations. These costs are typically driven by worker wages and benefits--primarily the impact of collective bargaining agreements for home care workers. However, a portion of the cost increases are driven by increases in client acuity which correspondingly increase required levels of care.

2015-17 Budget Recap

The 2015-17 Biennium Enacted Budget and 2016 Supplemental Enacted Budget increased funding for ALTSA and DDD by $400 million Near GF-S and Opportunity Pathways ($1.3 billion total funds), or about a twenty percent increase over the 2013-15 Biennium. Maintenance level adjustments, such as increased caseload and annual per capita costs, accounted for about one third of the increase in funding. The remainder is due to other policy level changes, including the following highlights:

- $116 million Near GF-S and Opportunity Pathways ($260 million total funds) was provided to fully fund the 2015-17 collective bargaining agreement for individual providers. This included phased-in changes and increases to the wage scale, increases in health care contributions, increases in the training contribution, an increase in personal time, and a retirement benefit contribution. This included funds to meet statutory parity requirements for homecare agencies.
- $32 million Near GF-S and Opportunity Pathways ($73 million total funds) was provided to comply with a recent U.S. Department of Labor rule that applies provisions of the Fair Labor Standards Act (FLSA), including a requirement for overtime pay, to Individual Provider (IP) home care workers.
- $20 million Near GF-S and Opportunity Pathways ($40 million total funds) was provided to increase the benchmark vendor rate for supported living providers, group homes, and licensed staff residential providers. Beginning July 1, 2015, the vendor rate was increased by 4 percent. Beginning July 1, 2016, the vendor rate was increased by 8 percent.
- $17 million Near GF-S and Opportunity Pathways ($40 million total funds) was provided to fully fund the 2015-17 arbitration award for adult family homes. Beginning July 1, 2015, the vendor rate was increased by 5 percent. Beginning July 1, 2016, the vendor rate was increased by 10 percent.
- $16 million Near GF-S and Opportunity Pathways was provided to fully restore the portion of Lean management savings distributed to LTC and DD.
- $7 million Near GF-S and Opportunity Pathways ($14 million total funds) was provided for additional staff to address compliance with Centers for Medicare and Medicaid Services (CMS)

requirements for habilitation, nursing care, staff safety, and client safety at the Residential Habilitation Centers.

- $5 million Near GF-S and Opportunity Pathways ($10 million total funds) was provided to lower the ratio of case carrying staff to clients at the Area Agencies on Aging from 1-to-75 to 1-to-70 during the 2015-17 biennium.
- $4 million Near GF-S and Opportunity Pathways ($8 million total funds) was provided to increase the vendor rate for assisted living providers by 2.5 percent, beginning July 1, 2015.
- $2 million Near GF-S and Opportunity Pathways ($4 million total funds) was provided to develop short-term community-based respite services across the state for individuals with developmental disabilities as an alternative to using respite services in an institutional setting.
- $1 million Near GF-S and Opportunity Pathways ($2 million total funds) was provided for eight additional planned respite beds at Yakima Valley School. The beds are intended to give families a break in caregiving, which may help individuals with a developmental disability maintain residence in community settings.
- $1 million Near GF-S and Opportunity Pathways ($2 million total funds) was provided to increase home visits for individuals at the highest risk of abuse or neglect and expand Adult Protective Services fatality review responsibilities.

Current Budget Issues

State Hospital Waitlist Reduction.
The DSHS, in coordination with the Office of Financial Management, has taken action to address recent contempt orders at the state psychiatric hospitals. Additional recommended resources for ALTSA include additional capacity for Enhanced Service Facilities, Specialized Behavior Support, Permanent Supportive Housing, and Specialized Nursing Facilities. Additional recommended resources for DDA include expanded capacity for State Operated Living Alternatives.

Habilitation Requirements at the DD Institutions.
The DSHS operates four institutions for the developmentally disabled, and is currently able to claim federal match for all clients living at three institutions - Fircrest, Yakima Valley, and Lakeland Village. At Rainier, due to citations from the Centers for Medicare & Medicaid Services, the DSHS can only claim federal match for a portion of campus. The DSHS has implemented a corrective action plan. If the changes at Rainier are not deemed sufficient, and a portion of campus is decertified, then Rainier could lose about $800,000 per month in federal funds. The DSHS expects resolution prior to the 2017 session.

Medicaid Transformation Waiver.
The Centers for Medicare and Medicaid Services has approved a five-year demonstration waiver for Washington. The waiver does not require additional state expenditures. New federal funds would fall under three initiatives: (1) incentive-based payments for transformation projects designed to improve care and lower cost for Medicaid clients, (2) services for family caregivers, and (3) supportive housing and employment services for adults with complex care needs. The Health Care Authority is requesting expenditure authority for the first initiative. The second and third initiatives impact the ALTSA budget.

Economic Services Administration

The Economic Services Administration (ESA) administers public assistance programs that provide low-income Washington residents with cash assistance, food assistance, some eligibility determinations for medical assistance, child support enforcement and collections, eligibility for child care subsidy, disability determinations, employment services, and other services within the Department of Social and Health Services (DSHS). ESA's Community Service Offices serve as the "front door" for cash and food benefits and referrals to other programs and services for low-income families. ESA clients include low-income individuals, families, and children; pregnant women; individuals with disabilities; older adults; refugees; and immigrants.

Major assistance programs administered by ESA include:

- ***Temporary Assistance for Needy Families (TANF):*** Cash grants for low-income individuals with children (lifetime limit of 60 months) and children whose parents are ineligible or who are being cared for by non-parent caregivers. Clients must participate in approved WorkFirst activities to receive the full TANF grant. Failure to participate results in a reduced grant and continued lack of participation may result in benefit termination.
- ***State Family Assistance (SFA):*** Cash assistance to legal immigrants who are ineligible for TANF due to legal immigration status of less than 5 years, students aged 19-20, and certain pregnant women.
- ***WorkFirst program:*** Support services focused on obtaining paid, unsubsidized employment for low-income families who receive TANF cash welfare.
- ***Working Connections Child Care (WCCC):*** Child care subsidies for low-income parents who are working, participating in an approved work activity, or receiving TANF cash assistance.
- ***Additional Requirements for Emergent Needs (AREN):*** Emergency cash payments to prevent eviction, utility shut-off, and other emergency payments related to health and safety for TANF, State Family Assistance (SFA), and Refugee program clients.
- ***Aged, Blind and Disabled (ABD):*** Cash assistance to low-income clients, without dependents, who cannot work due to a disability and are likely to meet federal Supplemental Security Insurance (SSI) standard; and for legal immigrants and refugees who cannot obtain SSI, but meet the disability criteria.
- ***Basic Food/Supplemental Nutrition Assistance Program (SNAP):*** Federally funded food assistance program for Washington residents, refugees, and legal immigrants (with legal status of 5 years or more).
- ***State Food Assistance (FAP):*** Food assistance to legal immigrants who are ineligible for federal SNAP due to immigration status of less than 5 years.
- ***Diversion Cash Assistance (DCA):*** Short term, emergency cash assistance to TANF/SFA-eligible households, who do not need ongoing monthly cash assistance. If family ends up on TANF/SFA within 12 months, the household repays the DCA benefit.
- ***Refugee and Immigrant Services (RCA):*** Cash assistance and medical assistance for newly arrived refugees.

Key Facts

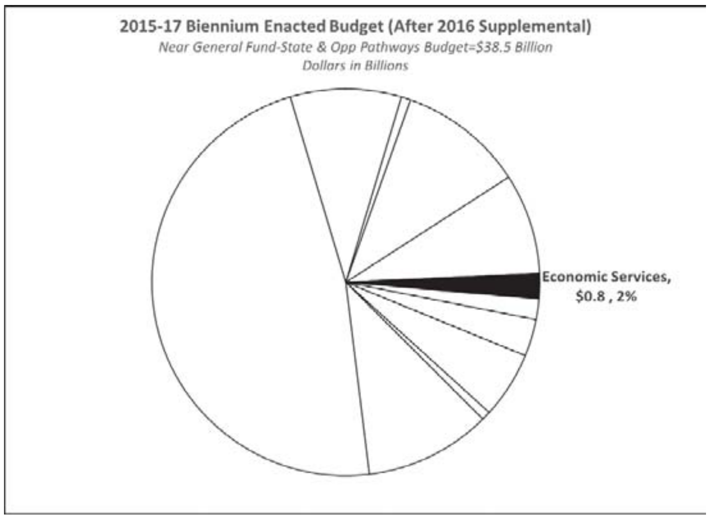
- Total 2015-17 Enacted Budget: $2.1 billion total funds ($814 million Near GF-S and Opportunity Pathways)
- Percent of budget that comes from state funds: 38 percent
- TANF/WorkFirst as a percent of budget: 14 percent state/37 percent total
- Child Care as a percent of budget: 22 percent state/21 percent total

- Basic Food Program as a percent of budget: 11 percent state/4 percent total
- Numbers served and average monthly cost:

Major Public Assistance Programs, Fiscal Year 2015			
Type	Programs	Households	Avg. Monthly Cost/Client
Food Assistance	Supplemental Nutritional Assistance Program	578,461	$223
Cash Grant	TANF Cash Assistance	35,158	$373
Child Care Subsidy	Working Connections Child Care	29,111	$757
Cash Grant	Aged, Blind and Disabled	21,904	$172
Food Assistance	State Food Assistance	11,168	$111

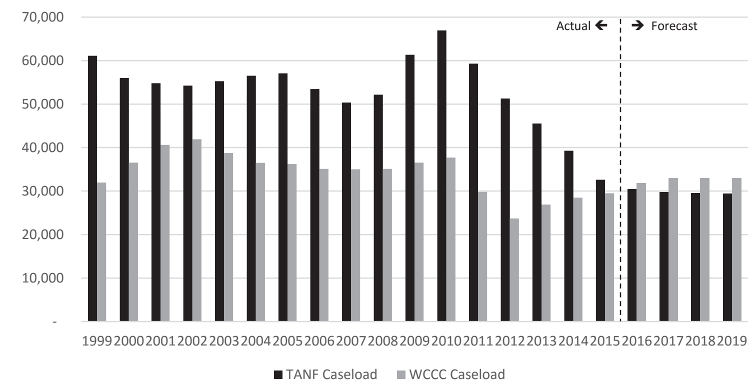
Trend/Overview Information

ESA accounts for two percent of the statewide total Near GF-S budget for the 2015-17 biennium and represents 15 percent of the total budget for DSHS.



A significant portion of ESA's budget is driven by forecasted caseloads for the TANF/Workfirst and Working Connections Child Care program (WCCC). These programs are forecasted, as a courtesy, by the Caseload Forecast Council (CFC) and per capita expenditures are estimated and adjusted by the joint legislative and executive staff workgroups for these programs. TANF/WorkFirst and WCCC are not entitlements and, as a result, the Legislature has significant flexibility to make policy choices that impact these caseloads or benefit levels.

Operating Budget Briefing Book 2017 Session



- TANF caseloads significantly declined after the 1998 welfare reforms and then were fairly stable until the Great Recession produced an increase from 2008 through 2010. Reductions in grants and a five-year lifetime limit resulted in significant caseload declines beginning in 2012. Caseloads are estimated to continue to decline slightly through Fiscal Year 2019.
- Program changes in WCCC, such as income eligibility and a child support enforcement requirement, created a significant decline in utilization in 2011 and 2012, although these policies were largely removed in 2012. The caseload has since been growing, but enrollment is planned to be capped at 33,000 households at which point a waiting list will be implemented. The current forecast predicts this will occur in Fiscal Year 2017.

2015-17 Budget Recap

For the 2015-17 biennium, including the 2016 supplemental budget, a total of $814 million in state funds (Near General Fund-State plus Washington Opportunity Pathways Account) was provided to ESA. Compared to the 2011-13 biennium, this represents a $82 million (11%) increase in state funds.

Savings

- Near GF-S and Opportunity Pathways savings of $80.6 million were achieved through forecasted caseload reductions in the TANF Program and the Working Connections Child Care (WCCC) Program, reductions in funding for work activities to reflect under-expenditures in those programs, and the use of unexpended federal grant and contingency funds to offset state expenditures.

Major Enhancements

- $30.6 million to increase the monthly TANF grant by 9 percent
- $22.2 million to implement 12 month authorizations for the WCCC program
- $17.7 million to increase base rates and tiered reimbursement provided to WCCC providers
    - $9.7 million for a 2 percent increase in the base rate for all WCCC providers effective July 1, 2015
    - $8.0 million for a market rate adjustment in the base rate and an increase in tiered

reimbursement for family child care providers effective July 1, 2016
- $9.6 million to increase the monthly benefit for the State Food Assistance Program to 100 percent of the federal SNAP benefit level

Current Budget Issues

TANF Two-Parent Work Participation Penalty: Federal TANF law sets minimum work participation standards that a state must meet and any state that fails to meet those standards are penalized by a reduction in its block grant. The work participation standards are 50 percent of all families and 90 percent of two-parent families. Washington did not meet the two-parent family standard and, as a result, could face a $67.9 million penalty unless Washington can demonstrate that they will meet the targets for a Federal Fiscal Year 2016. ESA is requesting $1.2 million in state funds to continue the Working Family Support (WFS) program, which provides a monthly $10 payment to eligible clients and allows their work participation to be counted toward meeting the federal requirement.

Medicaid Cost Allocation: Chapter 4, Laws of 2015, 3rd sp.s., Partial Veto (ESSB 6052) directed the ESA to assist clients with Medicaid applications through the Healthplanfinder (HPF) online Medicaid application. The carryforward level budget assumed ESA would receive a total of $72.4 million of federal funding for this work; however, it is anticipated that only $25.4 million can be claimed due to the limited amount of Medicaid eligibility determinations ESA now makes. To address the gap, ESA eligibility staff now have access to HPF and additional work has been conducted to time sample staff work in order to maximize the ability to claim these federal dollars. With these strategies, an additional $22.4 million can be paid for with federal dollars, leaving a shortfall of $24.6 million. ESA is requesting Near GF-S and Opportunity Pathways to address the shortfall.

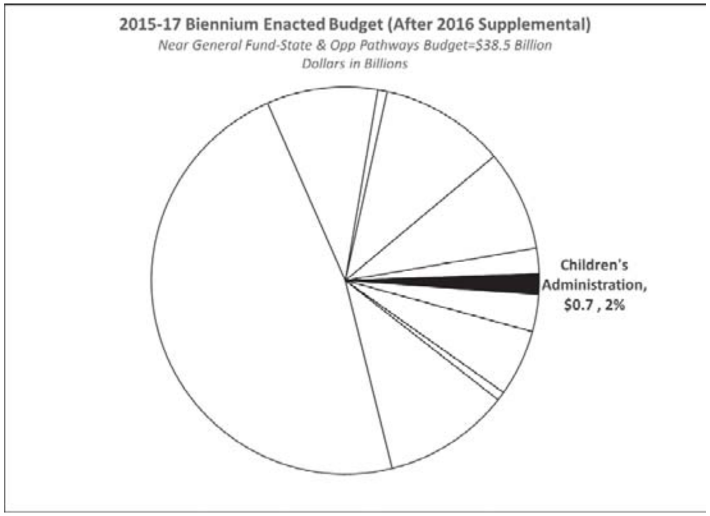
Aging Computer Systems and Infrastructure: A total of $15.7 million is being requested to update aging technology systems and infrastructure, including the following:
- **Maintenance and Operation of the Mainframe System:** $922,000 in state funds and $1.7 million in federal funds are being requested to fund ongoing maintenance and operation of the existing Unisys mainframe system, which includes support for the computer systems for child support payments and child care subsidy payments.
- **Modernization of Client Eligibility System:** $3.3 million in state funds and $24.7 million federal funds are being requested for modernization of the Automated Client Eligibility System (ACES) including migration of the 20-year old mainframe system to a modern platform, and development of web-based systems focused on customer and social worker access and functionality.
- **Replacing Antiquated Payment System:** $8.3 million in state funds is being requested to replace the 40-year old mainframe Social Services Payment System (SSPS) with a cloud-based system that includes the ability for more rigorous reporting and enhanced analytics.
- **Upgrade Child Support System:** $3.2 million in state funds and $6.2 million in federal funds are being requested to modernize the Support Enforcement Management System (SEMS) to include more rapid response time, the ability to more heavily utilize electronic form delivery, and incorporation of data analytics.

Children's Administration

Children's Administration (CA) is responsible for protecting abused and neglected children, supporting the efforts of families to care for and parent their own children safely, and providing quality care and permanent families for children. CA relies on outside (non-employee) providers for most services to families and children while CA staff focus on child protective services and foster care casework.

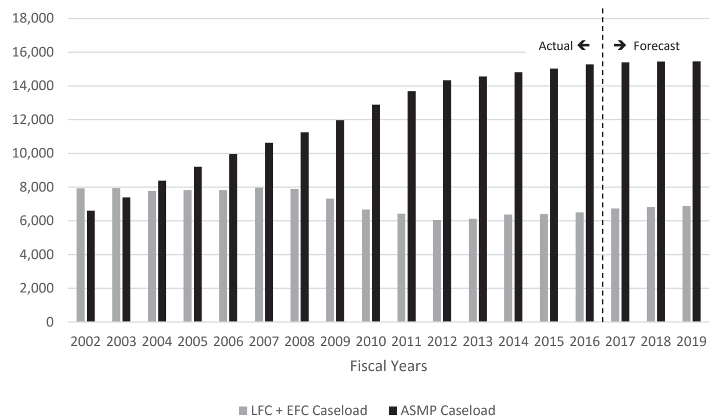
Key Facts
- Total 2015-17 budget: $1.2 billion total funds ($662 million Near General Fund-State)
- Percent of budget that comes from the state: 56 percent
- Child Welfare referrals (FY 2016): 9,250 monthly average
  - Child Protective Services (CPS): 8,177 monthly average
  - Family Assessment Response (FAR): 358 monthly average
- Foster Care FTE caseload, FY 2016: 9,725
  - Licensed Foster Care: 5,540
  - Extended Foster Care: 466
  - Unlicensed Foster Care: 4,121
- Adoption FTE caseload, FY 2016: 15,277

Trend/Overview Information
CA accounts for two percent of the statewide total Near GF-S and Opportunity Pathways budget for the 2015-17 biennium and represents 10 percent of the total budget for DSHS.



CA's budget is largely driven by maintenance payments associated with the adoption support and foster care caseloads. When the department needs to remove a child from their home, the state has legal responsibility for that child until a long-term solution is developed. While the child is in state custody, the state must provide medical, dental, and mental health services; provide for the physical well-being of the child; and provide maintenance payments to licensed foster parents. Not all children who are on the foster care or adoption caseloads are eligible for federal matching funds under Title IV-E of the Social Security Act and, as result, for these cases the state pays the full cost. Eligibility for Title IV-E federal reimbursement is a complicated process based on many factors including income and asset determination, child's age, citizenship status, and licensure of the foster home placement.

Licensed foster care and adoption support are considered mandatory caseloads and are forecasted by the Caseload Forecast Council (CFC). Per capita expenditures are estimated and adjusted by the joint legislative and executive staff workgroups. Because both foster care and adoption support caseloads are federal and state entitlements the Legislature has limited flexibility to make policy changes that would result in less than full funding of these caseloads.



- Adoption support caseloads have been increasing since 2002, but the growth has slowed since 2012. The state pays adoption support payments to parents who adopt children from the state foster care system.

- Foster care caseloads decreased significantly from 2007 through 2012. Beginning in 2013, however, the caseloads began to increase slowly; a pattern that mimics the national trend.

2015-17 Enacted Budget Recap

For the 2015-17 biennium, including the 2016 supplemental budget, a total of $662 million Near GF-S and Opportunity Pathways was provided to CA. Compared to the 2011-13 biennium, this represents a $56.9 million (9%) increase in state funds.

Major Enhancements

- $12.5 million Near GF-S and Opportunity Pathways was provided to reimburse foster parents under a mediated agreement with the Foster Parents Association of Washington State (FPAWS). Under the agreement, CA will increase basic foster care maintenance rates from a monthly average of $500 per child to a monthly average of $649 per child. The new rates are based on the estimated costs of providing a child with food, clothing, personal incidentals, and shelter.
- $6.4 million Near GF-S and Opportunity Pathways was provided for CA to: 1) reduce the caseloads of social workers serving children in foster care to support compliance with the Braam Settlement and reduce lengths of stay in foster care; 2) support the safe closure of CPS investigations within 90 days of intake, when appropriate; and 3) progress towards statewide expansion of FAR.
- $3.9 million Near GF-S and Opportunity Pathways was provided for a 3 percent increase in Behavioral Rehabilitative Services (BRS) vendor payments.
- $3.4 million Near GF-S and Opportunity Pathways was provided to continue expansion of FAR and performance-based contracting of family support and related services; and to increase the vendor rate for child placing agencies by 18 percent.
- $2.7 million Near GF-S and Opportunity Pathways was provided for contracted vendors to conduct court-ordered supervised visits between children in out-of-home care and their parents and siblings.
- $2.5 million Near GF-S and Opportunity Pathways was provided to serve BRS youth enrolled in Extended Foster Care (EFC), and to fund the costs of other supportive services that are not currently funded through the foster care forecast.

Current Budget Issues

USDOL (Perez) v. DSHS: A settlement agreement has been reached in this class action suit involving the Fair Labor Standards Act and over 4,500 claimants over a 10-year period for uncompensated overtime to certain Social Workers. Total cost is $9.8 million -- $4.9 million in back wages and $4.9 million in damages – plus standard employer expenses associated with the $4.9 million awarded for wages.

Improving Foster Care Placement Continuum: CA is experiencing a declining supply of licensed foster care homes; increases in social worker caseloads; and a more recent increase in the number of children who are extremely difficult to place, which has produced an increase in hotel stays and other suboptimal placement settings. To address these issues, CA is requesting $15.6 million in state funds for the following:

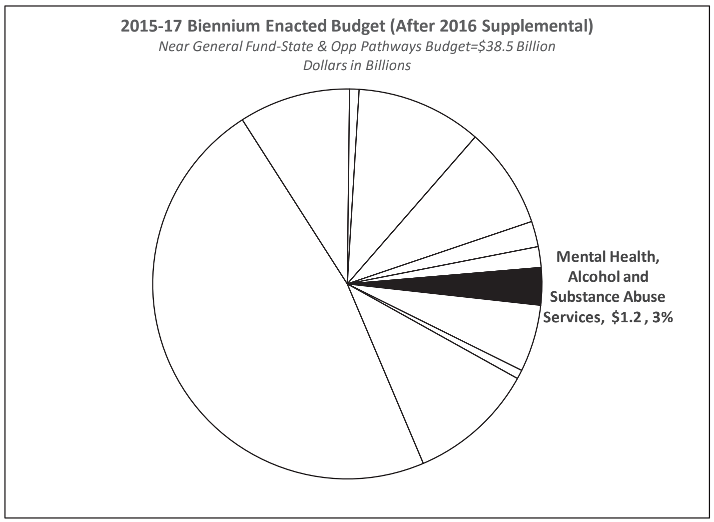
- $8.7 million in Near GF-S and Opportunity Pathways and 61 FTE to address the issue of high social worker caseloads, which can increase lengths of state on foster care;
- $5.0 million Near GF-S and Opportunity Pathways to expand the numbers of options that provide placement to children with the highest behavioral and mental health needs to help reduce the numbers of placements for these children; and
- $1.9 million Near GF-S and Opportunity Pathways and 10 FTE to reduce the length of time it takes to license foster care homes to expand the number of placement options available.

Division of Behavioral Health and Recovery (Mental Health and Alcohol and Substance Abuse Services)

The Division of Behavioral Health and Recovery (DBHR) in the Department of Social and Health Services combines Mental Health and Alcohol and Substance Abuse (ASA) programs.

Washington is budgeted to spend $3.1 billion total funds ($1.2 billion Near GF-S and Opportunity Pathways) during the 2015-17 biennium to provide mental health and substance abuse services for low-income Washingtonians. The majority of DBHR services are provided utilizing a network of community providers. DSHS directly operates three inpatient, psychiatric mental health facilities.

- Eastern and Western State Hospitals, state institutions for mental disease (IMD) that provide services to adults who have been either:
    - found not guilty by reason of insanity (forensic), or
    - committed involuntarily for treatment expected to last 90 days or longer (civil); and,
    - Child Study Treatment Center, which is a small facility for children and adolescents.



Key Facts

Mental Health

- Total: 2015-17 biennial budget: $2.3 billion in total funds and 2,999 FTEs
- Percent of budget that comes from state funds: 45%
- Number served (FY2015 unduplicated client counts):
    - Community Services/RSNs: 170,027 (148,697 are Medicaid)
        - Western State Hospital: 1,837
        - Eastern State Hospital: 843

- Child Study Treatment Center: 94

DASA

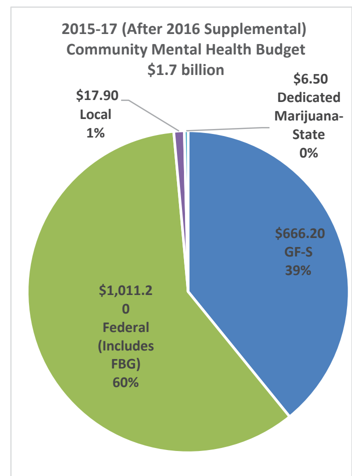
- Total: 2015-17 budget: $720 million in total funds and 85.3 FTEs
- Percent of budget that comes from state funds: 18.1%

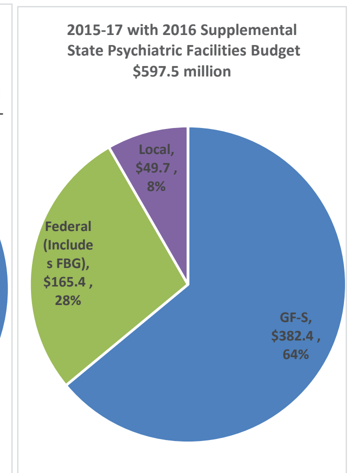
Trend and Overview Information

In terms of 2015-17 Near GF-S and Opportunity Pathways, the DBHR program comprises just under three percent of state-wide spending and nearly ten percent of state spending on health and human services programs.

Both the Mental Health and Alcohol and Substance Abuse (ASA) programs are adjusted at maintenance level for Medicaid caseload changes, similar to other Medicaid programs. This is a relatively new method for adjusting the ASA program as DSHS moved to integrated mental health and substance abuse rates provided by managed care run Behavioral Health Organizations. This integration of rates and services became effective April 1, 2016.

Of the total funds in the community mental health budget, 12 percent are used to pay for services and clients who are not Medicaid eligible. Under federal law, Medicaid funds may not be used to cover costs for investigation, detention, or court hearings under the Involuntary Treatment Act, or direct housing costs. State funding covers about 63 percent of the cost to operate the state psychiatric facilities.





2015-17 Budget Recap

Mental Health

The 2015-17 Enacted Budget and the 2016 Supplemental Enacted Budget included significant increases in both maintenance and policy level, with Near GF-S and Opportunity Pathways funds increasing by nearly thirteen percent from the 2013-15 funded level. Overall funding increased by $478.8 million ($120 million Near GF-S and Opportunity Pathways) or 26 percent from the 2013-15 funded level. This increase was primarily driven by expanded Medicaid eligibility ($328.2 million total funds), lawsuit settlements, state hospital safety improvements, and community mental health enhancements.

2015-17 biennium Enacted budget:

- $57.2 million ($39 million Near GF-S and Opportunity Pathways) was provided to meet the demands for expanded involuntary civil detention and commitment criteria in order to implement D.W. v. DSHS. These funds are available to each of the RSNs as they demonstrate increased community civil bed utilization and also to fund a 30-bed civil ward at Western State Hospital.
- A total of $40 million ($38.3 million Near GF-S and Opportunity Pathways) was provided for increased competency evaluation and restoration staff, state hospital wards, diversion from prosecution for nonviolent offenders, and the creation of an Office of Forensic Mental Health in order to implement the commitments in the Trueblood v. DSHS Settlement Agreement.
- A total of $23 million ($14.3 million Near GF-S and Opportunity Pathways) was provided to enhance community mental health services. The purpose of this funding is to implement the criteria in Chapters 250 and 258, Laws of 2015, which provide Assisted Outpatient Treatment and Detention Decision Review.
- A total of $9.4 million Near GF-S and Opportunity Pathways for state hospital safety enhancements including: (1) Psychiatric Intensive Care Units; (2) Psychiatric Emergency Response Teams; and backfilling of staff to complete training in compliance with an L&I settlement agreement.

2016 Supplemental Enacted Budget:

- A total of $35.8 million in total funds ($35.1 million Near GF-S and Opportunity Pathways) was provided to improve safety at state hospitals, address deficiencies identified by the Centers for Medicare and Medicaid Services (CMS) through site audits, and cover overspending.
- A total of $11.2 million in total funds ($4.4 million Near GF-S and Opportunity Pathways) was provided for community mental health service investments to expand mobile crisis teams, expand housing and recovery services, and a variety of other enhancements to include peer bridging programs and increased mental health referrals by law enforcement.
- A total of $37.8 million in total funds ($24.9 million Near GF-S and Opportunity Pathways) in one-time savings resulted from the return of state and federal reserves from Southwest Washington Regional Support Network as it transferred to a fully integrated managed care system. Other savings resulted from delayed implementation of various community and state hospital investments made in the 2015-17 operating budget.

Chemical Dependency

The 2015-17 Enacted Budget and the 2016 Supplemental Budget included significant increases mainly due to maintenance level increases based on Medicaid rate adjustments for moving to a managed care model on April 1, 2016 and Medicaid caseload. Overall funding increased by $269.7 million ($7.3 million decrease in Near GF-S and Opportunity Pathways).

2015-17 Enacted Budget:

- $35.5 million spent on prevention and treatment services from dedicated marijuana funds account, which included $16.5 million for services previously funded from Near GF-S and Opportunity Pathways.
- Increased Near GF-S and Opportunity Pathways by $2.2 million to fund an increase in Medicaid rates for certain statewide treatment services, to include: a) group treatment; b) opiate substitution treatment; and c) certain services target at pregnant and parenting women, filling the gap until April 1, 2016 when new integrated Medicaid rates for the managed care system responsible for providing both mental health and substance abuse services.
- Increased Near GF-S and Opportunity Pathways by $1.3 million to include outpatient substance abuse treatment as services available under the involuntary outpatient mental health treatment created by the passage of E2SHB 1450.

2016 Supplemental Enacted Budget:

- $2.0 million in General Fund-Federal was provided to increase access to medication assisted treatment for individuals with opioid addiction.
- $0.6 million in total funds ($0.4 million General Fund-State) was provided to implement Engrossed Third Substitute House Bill No. 1713 (mental health, chemical dependency) which begins to integrate the involuntary treatment systems for chemical dependency and mental health.

Current Budget issues

Mental Health

Competency to Stand Trial

In August 2014 a class action lawsuit, *Trueblood vs DSHS*, was filed in federal court addressing competency to stand trial evaluations and restorations performed at and by the state hospitals. The lawsuit contends that the DSHS is not providing timely competency evaluations and restoration treatments for persons suffering from mental illness. This lawsuit was settled in April 2015.

Under the terms of the court ruling, DSHS must complete competency evaluations within seven days of a defendant raising competency issues and must provide restoration services within seven days of a defendant being determined not competent to stand trial. The DSHS was given until January 2016 to fully comply with the ruling.

Funding was provided in the 2015 Early Action Supplemental and the 2015-17 biennial budget to address the requirements of this lawsuit and the time limits imposed by the court. Funding totaled $41.2 million and provided the following:

- Additional Competency Restoration Wards at Western State and Eastern State Hospitals
- Out-stationed forensic evaluators in areas with high referral rates
- Staffing for an Office of Forensic Mental Health
- Continuation of community competency evaluations

Since April 2015, DSHS has increased the capacity for competency services by adding 96 beds between the two state hospitals and two community sites for a 65 percent increase.

Currently, DSHS is still not meeting the timeframes required by the court and is in contempt of the order. Monetary sanctions of up to $1000 per day for each individual waiting longer than 7 days are being levied under the contempt order. The fines must be utilized for the benefit of the class members. To date, DSHS has been fined over $700,000 (through July 2016). DSHS intends to be in compliance by the end of 2016, and it is not clear how the fines will be utilized or funded.

State Hospital Safety

DSHS entered into a formal Systems Improvement Agreement with CMS. CMS required DSHS to enter the agreement after failing to create an acceptable plan to make Western State Hospital safe. DSHS has until July 2017, to fix the problems identified by CMS or lose approximately $67 million in federal funding per year. The Systems Improvement Agreement required DSHS to hire an independent consultant to review and provide a root cause analysis report for Western State Hospital and to help develop a corrective action plan based on the findings. Initial requests for funding from DSHS to reach compliance could reach $15-20 million for Fiscal Year 2017.

A Governor's Innovation fund was created and $6.77 million in one-time funding, provided to improve the functioning at the state hospital. Any programs built with the funding will carry forward as maintenance level costs, which results in approximately $20 million costs for 2017-19 biennium.

In addition, DSHS is predicting nearly $29 million in spending beyond its budget at the State Hospitals for Fiscal Year 2017.

Compensation

New Collective Bargaining Agreement MOUs have been signed for certain job classes at Western State Hospital and other institutions within DSHS to provide increased compensation through the end of Fiscal Year 2017. Salary increases of $24 million for Fiscal Year 2017 are approved through the MOUs in an effort to stabilize a workforce to increase safety and security.

IMD regulations

Prior to Fiscal Year 2016, all stays in Institutions for Mental Disease (IMD) for individuals ages 21-64 were ineligible for federal Medicaid match. Beginning in Fiscal Year 2016, Medicaid match was allowable for community stays less than 30 days in an IMD setting and substance abuse IMDs were allowed beginning April 2016.

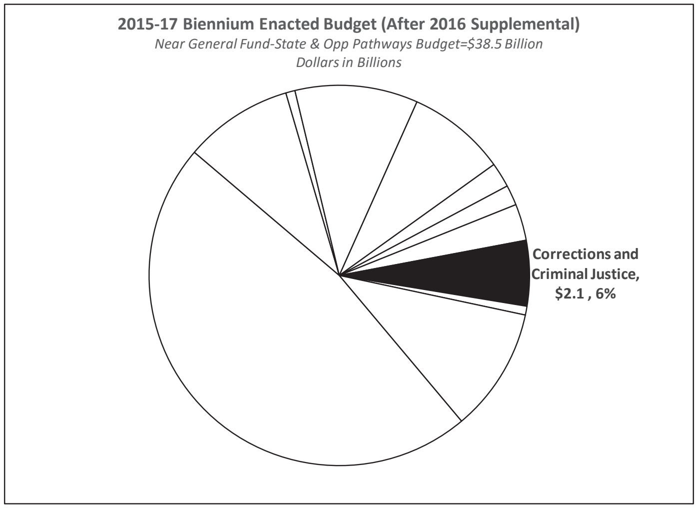
New federal regulations narrow the allowance to 15 days in a calendar month for stays in an IMD to receive federal Medicaid match. This will increase the amount of Near GFS necessary for these settings as federal funding will be limited. Actuarial work has not been fully completed but initial work indicates the lost federal revenue may exceed $20 million.

DSH

The federal Disproportionate Share Hospital (DSH) program allows qualifying hospitals to receive federal reimbursement for uninsured individuals. Approximately one-third of Washington's funding is utilized for the state hospitals. The Affordable Care Act requires a phased reduction of DSH beginning in 2018. By the end of Fiscal Year 2019, the state hospital portion of this funding will drop from $67 million down to approximately $50 million. By 2025, this funding is estimated to be near $22 million.

Department of Corrections and Other Criminal Justice

The 2015-17 Enacted Budget as updated by the 2016 Supplemental Enacted Budget provides $2.1billion in Near GF-S and Opportunity Pathways for the Department of Corrections (DOC), Juvenile Rehabilitation Administration (JRA), the Special Commitment Center (SCC) for sexually violent predators, and the Criminal Justice Training Commission.



Key Facts

- Adult offenders are housed in 8 major prisons (6 for men and 2 for women), 4 minimum custody work camps, 16 work release centers, and approximately 900 beds rented in county jails.
- Juvenile offenders reside in 3 state-run institutions and 8 contracted community facilities.
- Civilly committed sexually violent predators reside in 1 total confinement facility on McNeil Island and in 2 secure community transition facilities.

	2015-17 Budget	Number of Offenders/ Residents	FTE Staff	Annual Cost per Offender/Resident
DOC Prison	$1,246 million	17,404	6,172	$35,587
DOC Supervision	$312.7 million	17,236	1,266	$7,415
JRA	$191.7 million	477	768	$107,591
SCC	$80.3 million	286	403	$142,737

2015-17 Budget Recap

Increases

- $13 million to manage increased medical costs in prisons
- $3.5 million to improve safety and security at prisons and juvenile community facilities
- $3.0 million to provide treatment and rehabilitative care for high acuity residents at SCC
- $1.7 million to train law enforcement officers in crisis intervention

Reductions

- $1.7 million to close Juvenile Offender Basic Training Camp
- $1.7 million by reducing lost earned time by using more immediate sanctioning
- $1.7 million by utilizing Medicaid funding for treating chemical dependency in the community

Current Budget Issues

Work Release Capacity

DOC currently either contracts or operates 16 Work Release (WR) facilities totaling 679 minimum security offender population beds. One of DOC's contracted vendors, a non-profit agency holding contracts to run seven WR facilities has determined it cannot continue operating two of its facilities beginning January 1, 2017. DOC intends to take over operations of one of the two facilities. While prison population has remained at a slower increase over the last few years, the population need has shifted from higher security needs to a need for minimum security beds. DOC will request funding to maximize its current WR settings (90 bed increase) at a cost of nearly $4 million per biennium, and will also be looking for new WR solutions. It is not yet known what the cost of any new facilities might be.

Community Supervision and Violator Caseloads

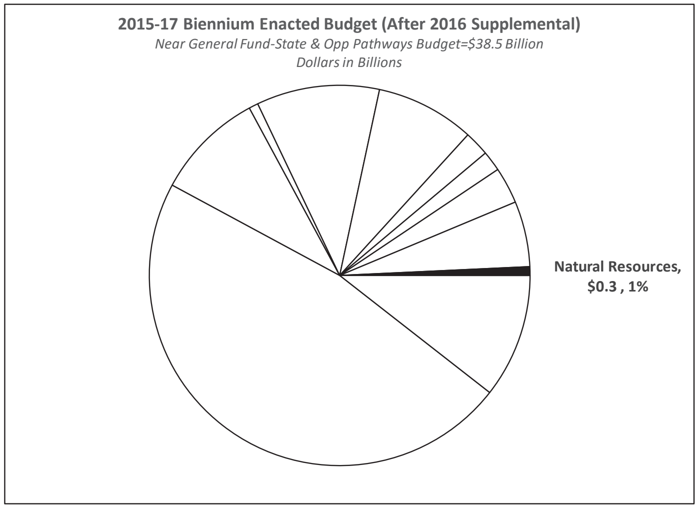
DOC Caseloads continue to grow for individuals released from prison but still subject to community supervision. During the 2017-19 biennium, the community supervision caseload is forecasted to grow from a daily population of 17,373 to 18,898 or by almost nine percent. In addition, the population of individuals spending time in local jails for violations of community supervision requirements continues to increase as well. The violator caseload is forecasted to increase from the currently funded daily population of 1,015 to near 1,400 by the end of the 2017-19 biennium.

Basic Law Enforcement Academy Classes

Under RCW 41.101, the Criminal Justice Training Commission is required to provide local law enforcement peace officers, basic training within six months of being hired. Currently, the Commission is funded to provide 10 academy classes per year or 300 training slots. The Commission estimates that it will receive approximately 500 applications annually during the 2017-19 biennium. Additional classes will likely be necessary to meet the statutory timelines for training over the next biennium. The Commission is requesting funding for eight additional classes per fiscal year at a cost of $4.9 million.

Natural Resources

As of the 2015-17 biennium, natural resource programs represent 0.75% of the Near GF-S and Opportunity Pathways budget ($287 million). The total budget, including various other funds, for natural resources is approximately $1.75 billion and represents 2.2% of the overall budget. The natural resources agencies budgets are funded primarily by dedicated funds.



Key Facts

Of the 11 agencies that are included in the natural resources budget, the three largest agencies (DNR, WDFW, and Ecology) account for 76% of both the total and NGF-S budget:

- Department of Ecology (DOE) regulates, inspects, and provides technical assistance for the environment; including air, land and water pollution and clean up. ($49 million NGF-P; $468 million total)
- Department of Natural Resources (DNR) manages 2.6 million acres of aquatic lands and 3 million acres of state trust lands for revenue to trust beneficiaries, such as school construction. NGF-S is used to fight forest fires, administer Forest Practices (regulations), provide geology services, and manage conservation areas. ($79.9 million NGF-P; $451 million total)
- Department of Fish and Wildlife (WDFW) provides protection to fish and wildlife and their habitats and sustainable fish and wildlife related recreational and commercial opportunities. ($77 million NGF-P; $414 million total)
- State Parks and Recreation Commission (State Parks) manages 120,000 acres with 117 developed parks, 35 heritage sites, 13 interpretive centers and more than 700 historic structures. ($21.7 million NGF-P; $172 million total)

- Department of Agriculture (Ag) provides support to the agricultural community and promotes consumer and environmental protection. ($34 million NGF-P; $175 million total)
- Washington State Conservation Commission (SCC) supports and guides the 45 conservation districts as a non-regulatory resource of information, guidance, and technical services for private landowners in dealing with land, water, and air quality conservation. ($13.6 million NGF-P; $32 million total)
- Recreation and Conservation Office (RCO) manages grant programs for outdoor recreation, wildlife habitat and farmland, and restoration of salmon habitat. ($1.7 million NGF-P; $10 million total)
- Puget Sound Partnership (PSP) coordinates the regional effort to clean up Puget Sound. ($4.7 million NGF-P; $17 million total)
- Environmental and Land Use Hearing Office (ELUHO) hears appeals and decides cases of certain land use and environmental decisions. ($4.3 million NGF-P; no other funds)
- Pollution Liability Insurance Program (PLIA) makes pollution liability insurance available and affordable to the owners and operators of regulated petroleum underground storage tanks and heating oil tanks by offering reinsurance services to the insurance industry. (No NGF-P; $1.9 million total)
- Columbia River Gorge Commission is a bi-state compact agency and funded equally by Oregon and Washington and works in partnership with the U.S. Forest Service, Tribes, and six counties within the National Scenic Area to adopt land use policy for the approximately 115,000 acres in the Scenic Area. (Washington's share is $0.9 million NGF-P; $1.8 million total)

2016 Supplemental Budget Recap

Wildfires

The Department of Natural Resources (DNR) was provided $155 million and the Department of Fish and Wildlife (WDFW) was provided $155,000 from the Budget Stabilization Account (BSA) for fire suppression costs resulting from the 2015 fire season.

A total of $6.1 million from the Disaster Response Account (DRA) was provided to DNR for additional firefighting resources and prevention activities. The Conservation Commission was provided $1.0 million from the DRA for the Firewise program, and $6.8 million from DRA to assist private landowners with re-seeding and infrastructure repair.

Forest Management

DNR was provided a total of $578,000 to increase staff capacity in the Forest Practices program, including additional screening of potentially unstable slopes, as well as a total of $236,000 for management activities at the Teanaway Community Forest.

Fish and Wildlife Management

WDFW was provided a total of $4.0 million in one-time funding for fish management, including hatchery maintenance, hatchery production, fishery monitoring and sampling, and activities related to securing Endangered Species Act permits. The WDFW was provided $475,000 of state general fund for increased stakeholder engagement on agency decisions and $300,000 of state general fund for Livestock Damage Prevention Cooperative agreements to reduce potential wolf-livestock conflict.

Outdoor Recreation

State Parks was provided $250,000 from the Recreation Access Pass Account to coordinate with WDFW and DNR on recommendations to improve access fee systems, and for a contract to facilitate this process. A report is due December 2017. Funding of $1.8 million from the Off-Road Vehicle and Non-Highway Vehicle

Account was provided to DNR to increase outreach and volunteer efforts, maintain recreational facilities and trails, and reduce the maintenance backlog for trails used by off-road vehicles.

Agriculture

A total of $4.8 million ($1.2 million in state general fund and $3.6 million in federal funds) was provided to the Department of Agriculture to design and implement an eradication program for the Asian gypsy moth to take place in the spring of 2016 and spring of 2017.

Model Toxics Control Act (MTCA) Savings

A total of $15.6 million of Department of Ecology operating expenditures from the Model Toxics Control Act (MTCA) accounts were reduced to address the decline in the Hazardous Substance Tax revenue.

General Fund-State Savings

In the Department of Ecology, $11.5 million of operating costs in the Water Resources Program were shifted on a onetime basis from state general fund to either the Reclamation Account or the Water Rights Tracking System Account. State general fund base budgets for fire suppression of $21.1 million for DNR and $344,000 for WDFW are reduced, as funding for fire suppression is provided from the BSA.

Current Budget Issues

Model Toxics Control Account (MTCA) revenue collections are approximately $72 million below the forecasted amounts used to build the enacted 2015-17 and 2016 supplemental operating and capital budget. The Department of Ecology has requested bond funds to offset the shortfall in MTCA revenue.

Department of Fish and Wildlife is requesting changes in their current fee authorities to help make up for budget shortfalls.

State Parks Revenue - The projection for revenue generated from Discover Pass, donations, and camping fees is to be $4.3 million higher than the current expenditure authority in the enacted 2015-17 biennial budget. State Parks is requesting to use this additional revenue to reduce the preventative maintenance backlog, upgrade law enforcement radios, support fire protection efforts, and promote parks.

Department of Agriculture

The department is requesting changes to their current fee authorities to help offset budget shortfalls. They are also requesting two policy bills and budget to assist the Liquor and Cannabis Board implement aspects of the new marijuana laws.

Department of Natural Resources will have underspent Budget Stabilization Account (BSA) funds for fire suppression costs in 2015 by approximately $24 million, but will have a 2017 supplemental request of $23.9 million for 2016 fire suppression costs.

Information Technology Investment Pool

The Information Technology Investment Pool (IT Pool) allows the Director of Financial Management to authorize funds from an appropriated pool for IT projects that meet certain criteria.

Chapter 33, Laws of 2013 (ESSB 5891) authorized OFM to establish an IT Pool and enter into contracts for IT purchases if the purchase replaces IT systems with more modern and efficient systems, improves the ability of an agency to recover from a major disaster, or future savings and efficiencies for an agency.

2016 Supplemental Enacted Budget Recap

The 2015-17 Biennium Enacted Budget appropriated $86.1 million for the IT Pool, including $25 million from the NGF-S. The 2016 Supplemental Enacted Budget increased the total appropriation to $93.2 million and the NGF-S appropriation to $26.7 million. OFM has allotted $66.7 million of the IT Pool appropriation as of October 28th, 2016.