



## Budget Tidbits... just the facts

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### Budget Brief #10: (4/1/10)

#### **The \$8 Billion 'Bow Wave': How the Legislature's decisions have worsened Washington's budget situation**

*Even when revenue growth returns to normal, the state budget will not be able to fund anywhere near the promises made during the 2009-10 legislative sessions.*

While much of the attention this session has been on tax increases, an equally important story has gone untold: the extent to which the Legislature, by decisions made this session and last, has worsened the state's budget situation by billions of dollars in upcoming budget cycles.

This has occurred in three ways:

1. "Kicking the can forward" – These are the Legislature's actions that merely moved the cost of items forward into future biennia.
2. "Obligated to new policy spending in future" – These are legislative decisions that created a new program and either punted its cost into the future or funded only a fraction of the eventual cost.
3. "Temporary reforms" – These consist of changes in the law or policy that are temporary, resulting in costs returning to the budget in the future.

**A. The Chart: \$8 billion in future costs attributable to decisions made this biennium**

The following chart depicts future costs of decisions made by the Legislature during the 2009 and 2010 sessions. Figures are supplied by non-partisan Senate Ways and Means staff.

**Estimated Future Cost of Selected Budget Items**

*(Dollars in Millions)*

<b><u>Kicking the can forward</u></b>	<b><u>2011-13</u></b>	<b><u>2013-15</u></b>
I-728 (returns with interest)	871	1,045
Additional pension costs	703	1,298
I-732 suspension (promise to buy back skipped COLA)	174	387
I-1029 homecare worker training	43	49
<b><i>Total</i></b>	<b>1,790</b>	<b>2,780</b>
<b><u>Obligated to new policy spending in future</u></b>		
SHB 2776 - K-12 funding distribution formula	765	1,852
Enhanced levy equalization	113	111
PEBB & K-12 health benefit issue	199	-
Hospital assessment post-2013	-	429
2SHB 2731 - Early learning	-	27
<b><i>Total</i></b>	<b>1,077</b>	<b>2,419</b>
<b><u>“Temporary” reforms</u></b>		
Temporary tax increases (sales, B&O, bottled water)	-	967
Enhanced federal medicaid	901	946
Capital budget transfers	960	960
GAU time limit	-	40
<b><i>Total</i></b>	<b>1,861</b>	<b>2,914</b>
 <b>TOTAL</b>	 <b>4,729</b>	 <b>8,113</b>

## **B. A Closer Look at the Items**

### **1. "Kicking the can forward"**

- Initiative 728 (returns plus interest) – The Legislature suspended the "lower class size" initiative for the 2009-11 biennium, reducing proposed funding to \$0 in the supplemental budget. However, beginning in the first year of the next biennium, [Substitute House Bill 2356](#) requires the Legislature to fully fund the initiative, plus interest, as if the suspension had not occurred.<sup>1</sup>
- Additional Pension Costs – In 2009 the Legislature "saved" \$449 million in pension costs by funding only 36% of the state actuary's recommended level for the Teachers Retirement System/Public Employees Retirement System Plan 1 unfunded liability, plus ignoring the actuary's recommendation for additional funding due to longer employee life spans.<sup>2</sup> Pension costs are a "pay now or pay more later" proposition, as they are a contractual liability of the state. By deferring payments, the Legislature significantly increases the cost to future budget writers and taxpayers. The state actuary's latest valuation concluded it will take "extraordinary efforts" -- in the form of dramatically higher state/taxpayer contributions -- to address the financial health of the system after years of underfunding and inadequate returns.<sup>3</sup>
- I-732 (promise to buy back skipped COLA) – Initiative 732, passed by voters in November 2000, required annual cost-of-living increases for K-12 staff. Legislators suspended scheduled increases in K-12 pay during the 2009-11 biennium, saving hundreds of millions. But the bill that suspended the increases required future legislatures to "make up" the skipped payments over the next four years.<sup>4</sup>
- I-1029 Homecare Worker Training – Initiative 1029 requires additional training for workers who care for elderly/disabled clients in the clients' home. (*Keep in mind more than half of caregivers care for a family member, and they receive health benefits of over \$600 per month, plus a salary.*) The Legislature delayed training requirements this biennium, although they come into full effect next biennium.

### **2. Obligated to new policy spending in future**

- Substitute House Bill 2776: K-12 funding distribution formula – This session the Legislature passed [SHB 2776](#), which established new policies with regard to state funding of school districts' transportation, maintenance/operations, K-3 class sizes, and all-day kindergarten. These policies are in large part to be phased in over the next five to seven years and, once in place, under the state Constitution cannot be eliminated for fiscal reasons. The figures from the chart come directly from the Office of the Superintendent of Public Instruction's fiscal note estimate of the additional funds needed to comply with the legislation (\$765 million in 2011-13 and \$1.85 billion in 2013-15).<sup>5</sup> The costs expand at a similar rapid rate in the 2015-17 biennium.

- Enhanced Levy Equalization – This session the Legislature authorized an increase in the amount of a school budget that can be financed with local levy dollars. To assist districts with lower property values in raising those funds, the Legislature increased state levy equalization support from 12% to 14%. While this costs an additional \$26 million in the proposed 2010 supplemental budget, the amount quadruples in the next biennium. And this merely represents the known costs from local levies already passed. If other levies are approved, which is a near certainty, the state's costs will rise even further.
- Public Employees Benefits Board and K-12 Health Benefit Issue – The state employees' health benefits account is more than \$200 million in the red, due in large part to a collective bargaining agreement signed between the governor and the state employees' unions after the 2009 session; the new contract guaranteed an employee premium share that was not sustainable given the budget appropriation.<sup>6</sup> Both the Senate and House budgets propose additional taxpayer funds to help bail out the account over the remaining six months of this biennium. (For instance, state funding per employee for health benefits would rise by \$27 per month under the Senate budget and \$95 per month under the House budget from last year's budgeted levels.) The figure on the chart represents the carry-forward cost of that new appropriation into the next biennium.
- Hospital Medicaid Rates/Provider Tax – The Legislature is in conference on Second Engrossed Substitute House Bill 2956, which would restore a rate cut for hospitals plus increase rates by as high as 36% depending on the type of hospital and service. This is financed via a "provider tax" mechanism that draws additional federal funds to finance the higher reimbursements. However, under 2ESHB 2956, the provider tax expires in 2013 and, with it, the revenues that leverage the federal funds. In the 9th Circuit Court of Appeals, no state has been successful yet in defending a Medicaid rate cut to providers. Thus, when the federal funds go away in 2013, the state will face a significant legal risk if it does not maintain and continue the higher Medicaid rates.
- Second Substitute House Bill 2731: Early Learning – This session the Legislature passed a program of early learning that, when fully implemented, will be an entitlement for eligible 3- and 4-year-old children. The legislation has no fiscal impact this biennium, but beginning in 2013-14 additional funding must be phased in until all children in households with incomes less than 110% of the federal poverty level are entitled to state-funded early learning services. The chart reflects that initial phase-in of one-third of unserved eligible children. Costs grow higher in subsequent biennia.

There has been a push, thus far resisted, to define "early learning" as part of constitutionally-protected basic education. This would have significant fiscal ramifications beyond those identified above. The attorney general has indicated that providing a component of basic education to some children, but not others, based solely on economic status would conflict with Article IX, Section 1 of the state constitution, meaning the scope of those entitled to taxpayer-funded early learning services would likely expand far beyond low-income children.<sup>7</sup>

### 3. "Temporary" reforms

- Temporary tax increases – The Senate budget and revenue package relies on three tax increases set to expire on June 30, 2013 (0.2% sales tax, 0.25% B&O rate increase on service businesses, and applying the sales tax to bottled water). These items alone represent nearly \$1 billion in revenue to support the 2011-13 budget that is expected to be unavailable in the 2013-15 biennium.
- Enhanced federal Medicaid – The operating budgets adopted in 2009 and proposed in 2010 rely on a temporary influx of billions of dollars from the federal government. The largest component of this is temporarily higher support of Medicaid in terms of the federal share of the costs. This is scheduled to expire in December 2010, although budget writers have booked an additional \$483 million by assuming additional support continues through June 2011.<sup>8</sup> Either way, the state will be on the hook for a more traditional share of costs beginning in the 2011-13 biennium.
- Capital budget support of operating budget – Cash used to support capital budget construction efforts has been transferred to the operating budget to the tune of almost \$1 billion this biennium. The funds are scheduled to return to their typical uses next biennium. Here are the major items:
  - Public Works Trust Fund – Traditionally, a portion of the real estate excise tax goes to the Public Works Trust Fund to provide low-interest loans for local government infrastructure projects. For the 2009-11 biennium, the Legislature proposes transferring all of that revenue (\$509 million) to the operating budget.
  - Lottery – The state lottery proceeds traditionally go to fund K-12 school construction. For the 2009-11 biennium, the revenues (\$208 million) were transferred to the operating budget.
  - Other Transfers/State and Local Toxics – An additional \$243 million was transferred to the operating budget. The largest share of this was \$180 million in funding that was scheduled to be used for state and local toxic cleanup efforts.
- GA-U time limit (sunsets in 2013) – The General Assistance-Unemployable program has been one of the fastest growing areas of the state budget for years. This year the Legislature, to its credit, imposed a time limit on assistance. However, to its discredit, the Legislature allows those time limits to expire in 2013.<sup>9</sup> That is, the program will return to status quo – no time limits for assistance – in 2013. That is government reform circa 2010 in Olympia.

**C. "If lawmakers do not look beyond the current budget crisis, they will have invited future ones."**

"The biggest danger of this year's legislative session isn't what lawmakers will consider necessary to close the \$2.6 billion budget hole. It's what they will consider unnecessary. . . . [I]f lawmakers do not look beyond the current budget crisis, they will have invited future ones.

...  
The Legislature cannot simply cut-and-tax itself out of this problem. It must reform its way out."

-- "*Legislature must look beyond this year's hurdle,*" *News Tribune editorial (1/10/10)*

The [first Budget Tidbit of the 2010 session](#) began with this quote. And, as the chart demonstrates, this Legislature – by kicking the can forward, obligating future legislatures to billions more in new policy spending, and enacting "temporary" reforms -- has clearly invited future budget crises with its actions.

*The simple truth is this: Even when revenues return to normal growth, the state budget will not be able to fund all the promises made during the 2009-10 legislative sessions.*

**Bottom Line**

While legislators can point to a difficult revenue situation in the 2009-11 budget cycle, the blame for upcoming multibillion-dollar budget difficulties will rest on their shoulders. It will be a situation largely of legislators' own making, attributable to an inability to make necessary structural changes and a penchant for obligating future legislatures to costly endeavors.

The \$8 billion bow wave. That is the legacy of the 2009-10 Legislature.

And it is a sad one.

1. SHB 2356 (2009) <http://wsldocs/2009-10/Pdf/Bills/Session%20Law%202009/2356-S.SL.pdf>
2. <http://www.leg.wa.gov/Senate/Committees/WM/Documents/SenateBudget/2009/ConferenceCmte/Three%20Way%20Final%20Comparison.pdf>
3. See "Pensions in Peril" (9/22/09), <http://www.senaterepublicans.wa.gov/budgettidbits/2009/092209BudgetTBPensions.pdf>
4. SHB 2363 (2009) <http://wsldocs/2009-10/Pdf/Bills/Session%20Law%202009/2363-S.SL.pdf>
5. Fiscal note for 2776 SHB.PL (3/19/10) <https://fortress.wa.gov/ofm/fnspublic/legsearch.asp?BillNumber=2776&SessionNumber=61>
6. See "Governor's Collective Bargaining Fiasco" (12/7/09) <http://www.senaterepublicans.wa.gov/budgettidbits/2009/120809BudgetTidbit.pdf>
7. AGO no. 9 (2008).
8. See Senate & House 2010 supplemental operating budget proposals.
9. E2SHB 2782 (2010) <http://wsldocs/2009-10/Pdf/Bills/House%20Passed%20Legislature/2782-S2.PL.pdf>