McAuliffe Budget Analysis

2018 Session

In his December 18 farewell address (https://governor.virginia.gov/newsroom/newsarticle?articleId=21995) to the senators and delegates who serve on the Senate Finance Committee, the House Finance Committee, and the House Appropriations Committee, Gov. Terry McAuliffe recounted the highlights of his four-year administration.

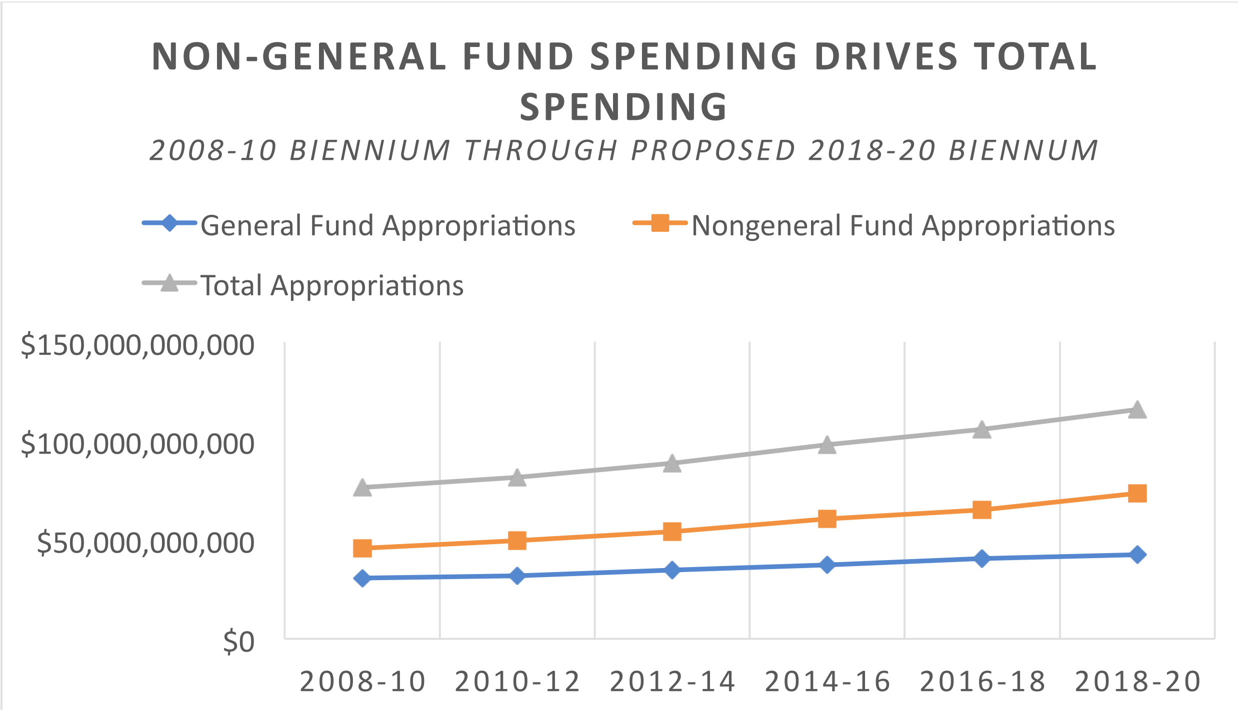
He boasted about the more than 1,078 economic development projects that will bring in more than $19.4 billion in capital investment, although he admitted that two-thirds of the investment will not mature for years to come.

He reminded the legislators that unemployment has shrunk to 3.6 percent, that initial unemployment insurance claims are at a 44-year low, and that his Administration oversaw the creation of 207,000 jobs. And, all of this was accomplished in an economy that was reeling when he first took office from the impacts of federal budget sequestration.

But, it was the unveiling of McAuliffe's budget proposals that drove the General Assembly members' interest.

The governor's budget for the next biennium includes $73.5 billion in non-general fund revenues or 63.4 percent of the entire budget. Non-general funds are made up of federal grants and contract, motor fuel taxes, college tuition, ABC sales, and special licenses and fees. As the graph below shows, the state's increasing reliance on non-general funds serves as the fuel for the overall spending. While total appropriations will rise by 51 percent from the 2008-10 biennium through 2018-20, non-general fund spending jumps by 60 percent.

In contrast, general fund spending increases by 38 percent over this same time period. It is the general fund that interests most taxpayers, politicians and local governments because the general fund relies on income and sales taxes. General fund appropriations help localities pay for K-12 education, public safety, economic development, and health and human services programs.



2016-18 Biennium Will Finish Strong

For Fiscal Year 2017, general fund collections and non-general transfers to the general fund exceeded the official forecast, resulting in $137.0 million more than the amounts anticipated. Most of the growth came from tax collections, specifically payroll withholding and corporate income taxes.

In Fiscal Year 2018 the official forecast calls for 2.7 percent growth in the general fund over the FY17 collections. Total general fund revenues have increased by 4.9 percent from July through November. Roughly two-thirds of the growth is from payroll withholding and sales tax.

The "caboose bill" which addresses the final months of FY18 focuses on both tax and spending issues. According to Secretary of Finance Ric Brown, HB/SB 29 fine tunes the official revenue forecast to take into account federal tax conformity, tax enforcement and compliance, and an over-estimate of tax amnesty collections. (Neither HB/SB 29 nor HB/SB 30 reflect recent congressional action on federal tax policy. At the request of the McAuliffe Administration, HB 154 has been introduced to conform with federal tax law as the law existed on December *1*, 2017.)

The proposed spending changes in the caboose bill deal with increases of $121.4 million for the Revenue Cash Reserve and $86.6 million for Medicaid utilization and inflation. The largest spending cuts target K-12 by $60.0 million due to enrollment and technical revisions and $40.5 million in Health Care Fund revenues that offset general fund Medicaid costs.

The net result of the 43 budget amendments is a $101.2 million *increase* over the amounts appropriated in the 2017 legislative session.

McAuliffe's budget wizards predict that after all the revenue, transfers, and spending changes are made in fiscal year 2018, the resulting unexpended balance of $201.6 million will roll forward to the 2018-20 biennium.

Budget Proposal in New Biennium Calls for Net Spending Increase of $1.8 Billion

According to the Director of the Department of Planning and Budget, the themes of the McAuliffe budget focus on expanding Medicaid coverage through "Obamacare", bringing the state budget into a structural balance, continuing economic development efforts to reduce dependence on federal spending, and addressing mandates and core services.

Net new spending for general fund programs would increase by $526.6 million in FY19 and by $1.2 billion in FY20. The proposed budget includes 251 amendments totaling almost $2.5 billion in new spending for the biennium. As a counterbalance, HB/SB 30 includes 35 amendments that reduce spending by $711.7 million.

Top 10 Policy Amendments Account for Almost 72% of New Spending

Agency	*Title*	*Biennial Total*
Dept of Medical Assistance Services	**Medicaid utilization & inflation**	**$583,872,606**
Direct Aid to Public Education*	Update costs of the Standards of Quality	$487,526,880
Dept of Accounts	Funding Revenue Cash Reserve	$270,700,000
Central Appropriations	State employer health insurance rates	$118,234,028
Direct Aid to Public Education*	Decrease Literary Fund support for school employee retirement	$80,000,000
Children's Services Act	Caseload & utilization	$54,228,358
Direct Aid to Public Education*	Two percent salary increase for SOQ funded school positions	$51,299,725
Central Appropriations	State agency information technology costs	$50,484,872
Central Appropriations*	Two percent salary increase for state employees and state-supported local employees	$49,428,113
Dept of Medical Assistance Services	Waiver slots required by settlement agreement with U.S. Department of Justice	$45,019,938

Top 10 Total		$1,206,921,914
Remaining Spending Amendments		$701,725,414
Grand Spending Total		$1,908,647,328
*Amendments of interest to localities		

As has been the case for several years, the state agencies receiving the most general fund dollars are Direct Aid to Public Education ($515.8 million) and the Department of Medical Assistance Services ($317.5 million).

The greatest budget savings are related to Medicaid expansion. In effect, expansion allows the state to use new federal dollars to pay for services currently financed by the general fund. The general fund savings of over $420.0 million show up in providing health care coverage to the uninsured, using federal dollars to pay a share of health care costs for state inmates, and employing federal resources in substance abuse and mental health services. The budget assumes that October 1, 2018 would be the effective date for implementing this major policy change.

Unlike previous attempts, the proposed budget's savings and costs are based on providing services for just over 300,000 Virginians and not the current estimate of 370,000 uninsured individuals. All eligible costs would be covered by a "provider assessment" estimated to generate some $80.8 million in FY19 and $226.1 million in FY20. (The special fund dollars would be deposited to the Health Care Fund to offset Medicaid expenses.) *Although no estimates are included in the McAuliffe budget, local and regional jails could see budget savings in their own operations from Medicaid expansion.*

As part of the effort to register eligible Virginians for the health insurance coverage, the budget includes $5.9 million for local social services departments.

Budget Turbulence:

Gov. McAuliffe's budget closely ties two of his most important budget themes – Medicaid expansion and the Cash Reserve Fund.

The reserve fund would help bring the state budget into structural balance, meaning dependence upon Rainy Day Fund withdrawals to pay for current government operations while the economy is growing would not be necessary. The Rainy Day Fund would be used as originally intended to address unexpected financial emergencies and economic distress. A cash reserve fund would provide the governor and General Assembly with greater budget flexibility than the Rainy Day Fund, and thus preserve Virginia's exceptional bond rating.

In the governor's own words over a three-year period, HB/SB 29 and HB/SB30 "will grow the cash reserve to *$427 million*, or a full two-percent of the total of my general fund operating appropriations in fiscal year 2020." As for Medicaid expansion, the governor told the money committees that his proposal "will result in savings of *$421.7* *million* over the upcoming biennium." The two numbers are too close to be coincidental. The questions to be answered are what happens if the General Assembly rejects Medicaid expansion? Which state program will be cut to make up the Cash Fund Reserve? And, so these programs assist local governments in carrying out state-mandates and state high-priority programs?

There are other issues that could rock the McAuliffe proposed budget. The budget bills do not include any money for local storm water management projects. The budget does not include a long-term solution for the upcoming transit capital funding crisis, although a FY20 authorization of $110.0 million in bonds is part of the budget package. The budget does not update state per diem support for either local-responsible or state-responsible inmates housed in local or regional jails. The budget reduces state support for maintenance of city- and town-owned roads. The budget does not fix the pro-ration of benefits owed to taxpayers for making capital investments or creating jobs in Enterprise Zones. The budget does not provide state funding (on a per pupil basis) beyond what was provided in FY 2009.

These and other budget items will be before the General Assembly in the upcoming weeks. VML will lobby hard for local interests. Please sign up for eNews (http://forms.aweber.com/form/91/874574591.htm) to stay up-to-date on state budget deliberations and other legislative issues in the 2018 session.

Budget Details:

Following this narrative is a spreadsheet detailing the various budget items of interest to localities.