

# **Senate Finance Committee**

**2011 Session  
Budget Outlook**

**November 18-19, 2010  
Staunton, Virginia**

# 2011 Session Budget Outlook

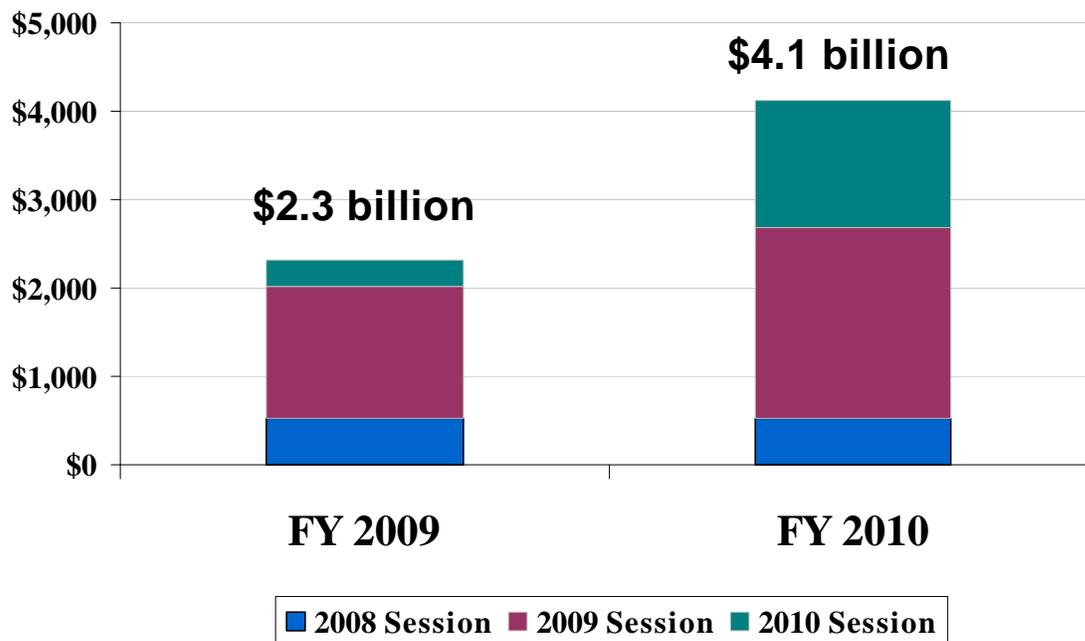
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- **Virginia's budget outlook has not improved dramatically (not a traditional V-shaped recovery), but you will not be trimming billions from the budget as in recent sessions.**
  
- **Based on projected revenues and a preliminary estimate of budget pressures, a general fund budget shortfall of under \$200 million is likely for the amended 2010-12 budget.**
  - SFC Staff estimates upward revenue adjustments of less than \$300 million on a base of about \$30 billion.
  
  - Budget pressures total about \$434 million, dominated by increased Medicaid utilization. Many of the typical discretionary funding items remain off the table (K-12, higher education, employee salaries, etc.)
  
- **Closing the \$4.5 billion budget gap last session required a combination of strategies, including reductions to core programs and the use of one-time savings and revenues.**
  
- **Looking ahead to the 2012-14 biennium.**
  - One-time savings and resources supporting the current budget contribute to "structural imbalance" for the next two-year budget.
  
  - Typical budget drivers – Medicaid, K-12 education, debt service -- may likely exceed available revenues, unless economic recovery accelerates.

## A look back at the previous biennium: revenue actions through the 2010 Session

- Over three legislative sessions, more than \$6.4 billion in revenue was cut from the 2008-10 biennial budget.
  - The magnitude of the revenue reductions, and the actions taken to address the shortfalls, directly impacted the decisions made to balance the 2010-12 biennial budget.

### Cumulative Revenue Forecast Reductions



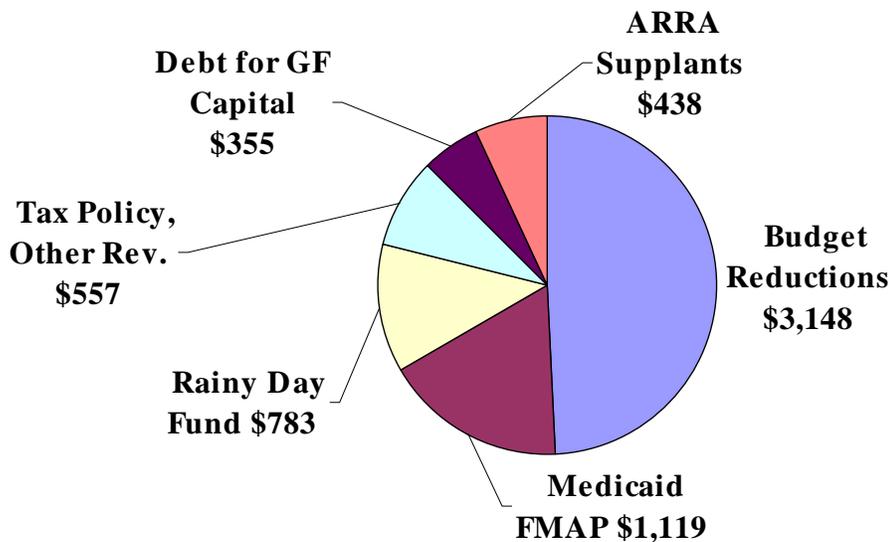
<u>Revenue Re-forecasts</u>	<u>FY 2009</u>	<u>FY 2010</u>
	<i>(\$ in millions)</i>	
2008 Session (Dec/Feb)	(\$ 520.1)	(\$ 532.2)
2009 Session (Oct/Dec/Feb)	( 1,495.0)	( 2,160.0)
2010 Session (Aug/Dec/Feb)	( 298.8)	( 1,436.5)
<b>Total</b>	<b>(\$2,313.9)</b>	<b>(\$4,128.7)</b>

# Closing the budget gap: 2008-10 biennium

- About **one-half** of the balancing actions were one-time in nature – Rainy Day fund withdrawals, tax amnesty, bonded debt for general fund cash, and the use of ARRA funds to supplant general funds.

## Actions to Close the 2008-10 Budget Shortfalls

**\$6.4 billion**  
(\$ in millions)



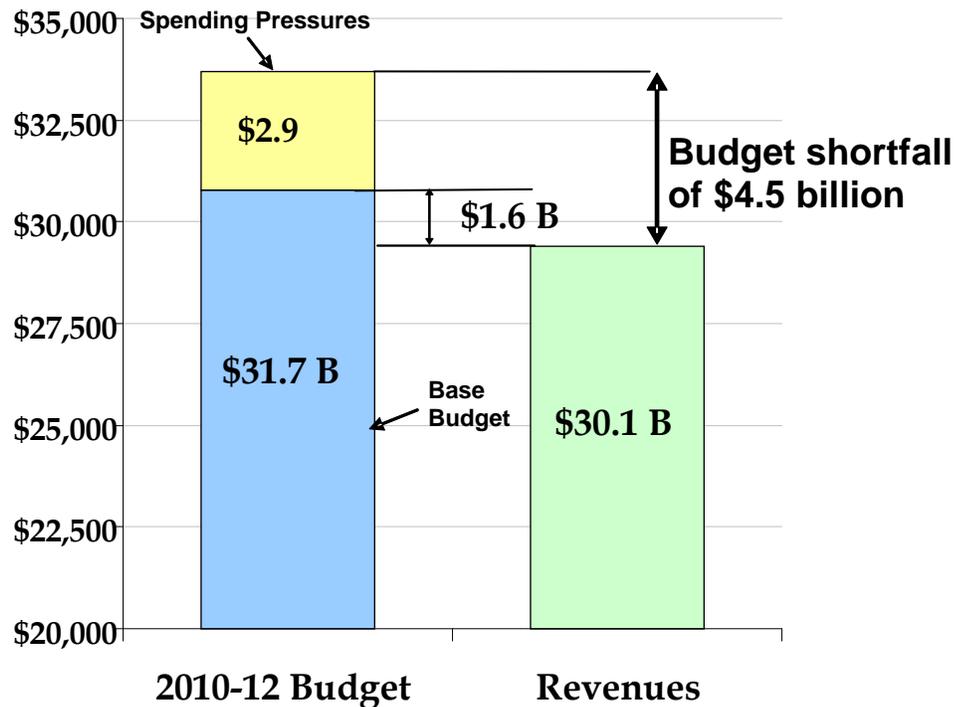
## ARRA Funds in 2008-10 Budget

(\$ in millions)

	<u>FY 2009</u>	<u>FY 2010</u>	<u>2008-10</u>
<b>GF Supplants:</b>			
Medicaid Enhanced Match	\$372.5	\$746.4	\$1,118.9
GF Supplant – Flexible Spending	109.5	109.5	219.0
K-12 Public Educ.– Supplanting	0.0	219.0	219.0
<b>Other:</b>			
K-12 Public Educ.– Restore Cuts	0.0	365.2	365.2
Higher Education – Restore Cuts	0.0	75.0	75.0
Byrne JAG – Restore Cut to Sheriffs	0.0	23.3	23.3
	<u>\$482.0</u>	<u>\$1,538.4</u>	<u>\$2,020.4</u>

## 2010-12 Biennium: \$4.5 billion budget gap

- Due to the one-time nature of certain prior year actions, projected revenues for the two-year period fell short of the biennial “base budget” by **\$1.6 billion**. Required spending totaled almost **\$2.9 billion**, exacerbating the budget shortfall.



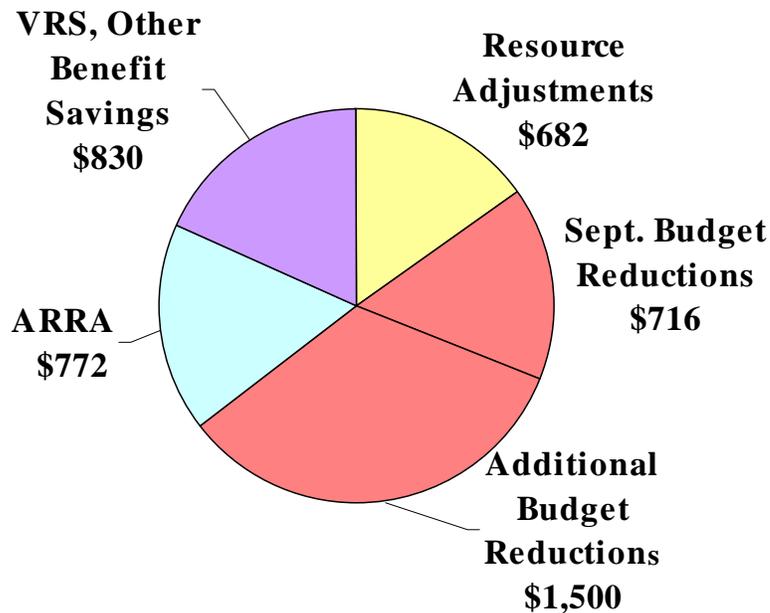
2010-12 Required Spending (\$ in millions)	
	<u>FY 2010-12</u>
Replace Medicaid Enhanced Match Funds	\$1,191.5
Fund Medicaid Utilization and Inflation	777.7
Fund Debt Service	165.7
Re-benchmark SOQ	182.8
VRS payments/Health Insurance (inc. SOQ)	174.1
Other	<u>386.8</u>
Total	<b>\$2,878.6</b>

# Closing the budget gap: 2010-12 Biennium

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- The task of closing an additional \$4.5 billion shortfall was more difficult because many one-time strategies had already been used. As a result, balancing the 2010-12 budget relied largely on budget reductions and one-time savings on benefit rates.

## Actions to Close the 2010-12 Budget Shortfall (\$ in millions)



- The proposal to eliminate state support for the Car Tax (\$1.9 billion) was not adopted; as a result, additional reductions to general fund-supported programs were adopted.
- **K-12 Public Education:** Net reductions in the budget as introduced totaled almost \$400 million; actions taken by the General Assembly reduced funding another net \$605 million (including \$346 million from reduced benefit contribution rates for VRS and other benefit programs).

## Closing the budget gap: 2010-12 Biennium

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- **Health and Human Resources:** Reductions totaling more than \$1.0 billion were adopted, in part to off-set growth in programs such as Medicaid.
  - Although additional ARRA funds were under consideration during the 2010 Session, the General Assembly did not include these funds in the budget, instead making the restoration of about \$400 million in general fund reductions contingent on the receipt of the additional federal funds.
  
- **Employee Benefit Savings:** Deferred approximately \$620 million of the usual VRS retirement contributions for the biennium. Contributions were based on the actuarial “normal” cost of providing retirement benefits, rather than the “normal” rate PLUS a portion of the unfunded liability.
  - Savings from other employee benefits and retirement program changes totaled about \$210 million.
  
- ARRA funds play less of a role in the current budget than they did in the 2008-10 budget. (*Funding in italics provided after budget was adopted.*)

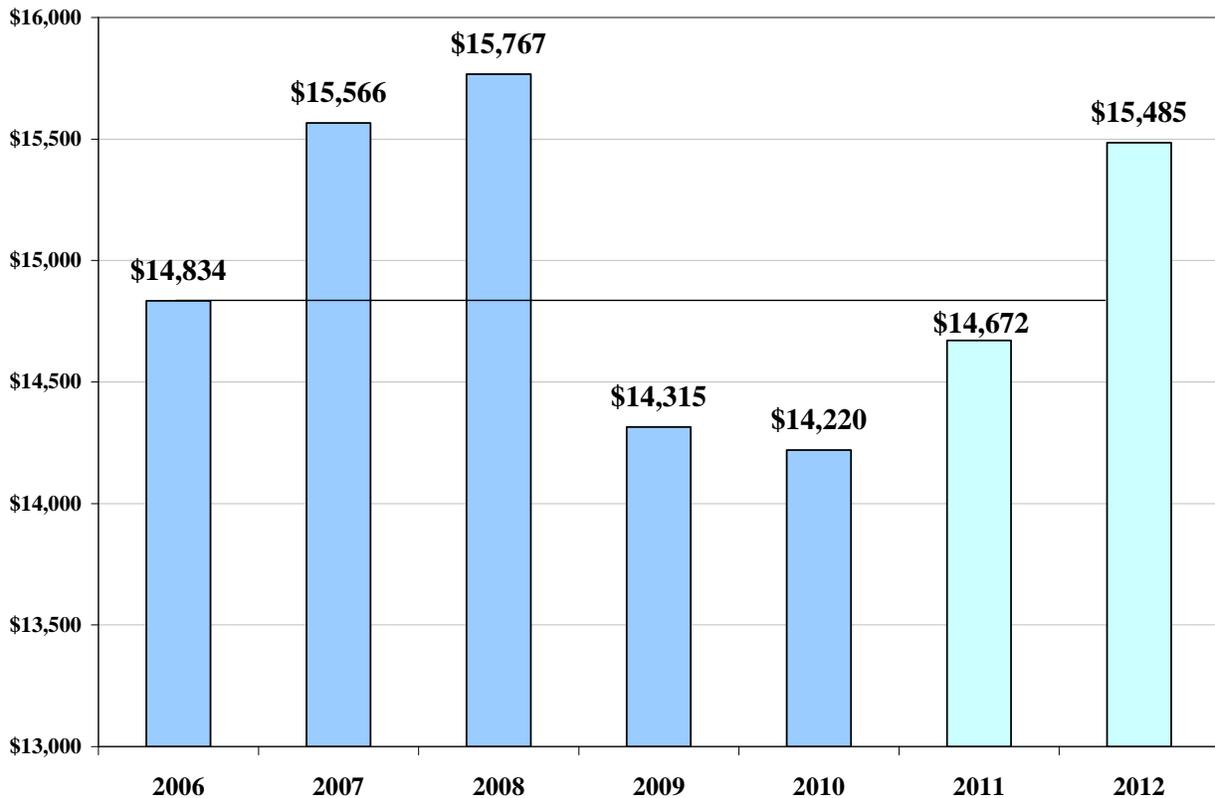
<b>ARRA Funds in 2010-12 Budget</b>			
<i>(\$ in millions)</i>			
	<u>FY 2011</u>	<u>FY 2012</u>	<u>2010-12</u>
Medicaid Enhanced Match	\$448.0	\$0	\$448.0
K-12 Public Education	122.9	0	122.9
Higher Education	<u>201.7</u>	<u>0</u>	<u>201.7</u>
Total	\$772.6	\$0	\$772.6
<i>Six-month FMAP Extension</i>	\$265.6	\$0	\$265.6
<i>K-12 EduJobs</i>	\$249.5	\$0	\$249.5

## FY 2011 projected revenues below actual revenue collected in FY 2006

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- Most state programs and services operating this fiscal year on a revenue base of \$14.7 billion – an amount below that of five years ago.

**Actual and SFC Projected GF Revenues**  
**FY 2006 to FY 2012**  
(Excludes transfers; \$ in millions)



- Budget pressures in the 2011 Session will pale in comparison with recent sessions; however, options to deal with the pressures have diminished accordingly.

## 2010 Session: Budget Pressures

- **Medicaid:** About \$207.0 million to address the Medicaid forecast, FAMIS, and shortfall in tobacco revenues. Does not include \$137.3 million to cover the FY 2012 shortfall in anticipated enhanced FMAP funds.
- **VITA:** Roughly \$25 to \$30 million per year (GF only) to cover contract modifications and usage-based billing for IT services.
- Some savings from projected lower K-12 average daily membership (ADM). No assumptions about any budget restorations, salary adjustments for employee groups, new initiatives, etc.

<b>Preliminary 2010-12 GF Spending Pressures</b>			
(\$ in millions)			
	<u>FY 2011</u>	<u>FY 2012</u>	<u>2010-12</u>
Medicaid Forecast	(\$39.9)	\$205.1	\$165.2
FAMIS (Children's Health Care)	19.0	10.0	29.0
Va. Health Care Fund - MSA Payments	6.0	7.0	13.0
Other HHR (DSS, Health, ESH)	0.0	18.5	18.5
VITA (contract mods, billing basis)	25.0	25.0	50.0
K-12 Sales Tax Adjustment	16.1	18.2	34.3
K-12 Lower Avg. Daily Membership	(13.6)	(14.0)	(27.6)
Higher Educ. Restructuring Incentives	0.0	8.3	8.3
Sexually Violent Predator Program	8.7	16.6	25.3
Public Safety (inmate medical, HB 599)	0.9	45.0	45.9
Comp Board (per diems, jail expansion)	7.4	8.0	15.4
Judicial (crim. fund, judicial vacancies))	6.7	9.2	15.9
Debt Service (if capacity is available)	0.0	7.0	7.0
Fed. Tax Conformity (GF revenue loss)	<u>25.4</u>	<u>8.2</u>	<u>33.6</u>
<b>Total</b>	<b>\$61.7</b>	<b>\$372.1</b>	<b>\$433.8</b>
<b>Other issues:</b>			
Backfill for FMAP Shortfall	\$0.0	\$137.3	\$137.3
VEC - Repayment of fed. loan	0.0	10.0	10.0
HE - Unspecified reduction	0.0	10.0	10.0

## 2010-12 Amended budget shortfall may be less than \$200 million

- Based on SFC staff estimates of revenue and spending pressures, the budget shortfall may be about \$150 million.

<b>2010-12 Amended Budget Shortfall</b>			
<i>(\$ in millions)</i>			
	<u>FY 2011</u>	<u>FY 2012</u>	<u>2010-12</u>
Official Forecast (Ch. 874)*	\$14,583.5	\$15,303.1	\$29,886.6
Plus: SFC Adjustment	\$94.6	\$189.4	\$284.0
Less: Budget Pressures	<u>\$61.7</u>	<u>\$372.1</u>	<u>\$433.8</u>
<b>Budget Shortfall</b>	<b>\$32.9</b>	<b>(\$182.7)</b>	<b>(\$149.8)</b>

\*Includes transfers.

- About \$88 million from the FY 2010 \$228 million in collections above the forecast were unallocated and can be used to address the shortfall. (The majority is dedicated to the contingent 3 percent bonus for state employees, WQIF, and transportation.)
- On October 21st, the Governor requested agencies to prepare 2, 4, and 6 percent budget reduction plans with no program exclusions. Budget reduction guidance observed that previous exercises have exempted as much as two-thirds of the general fund budget from consideration.

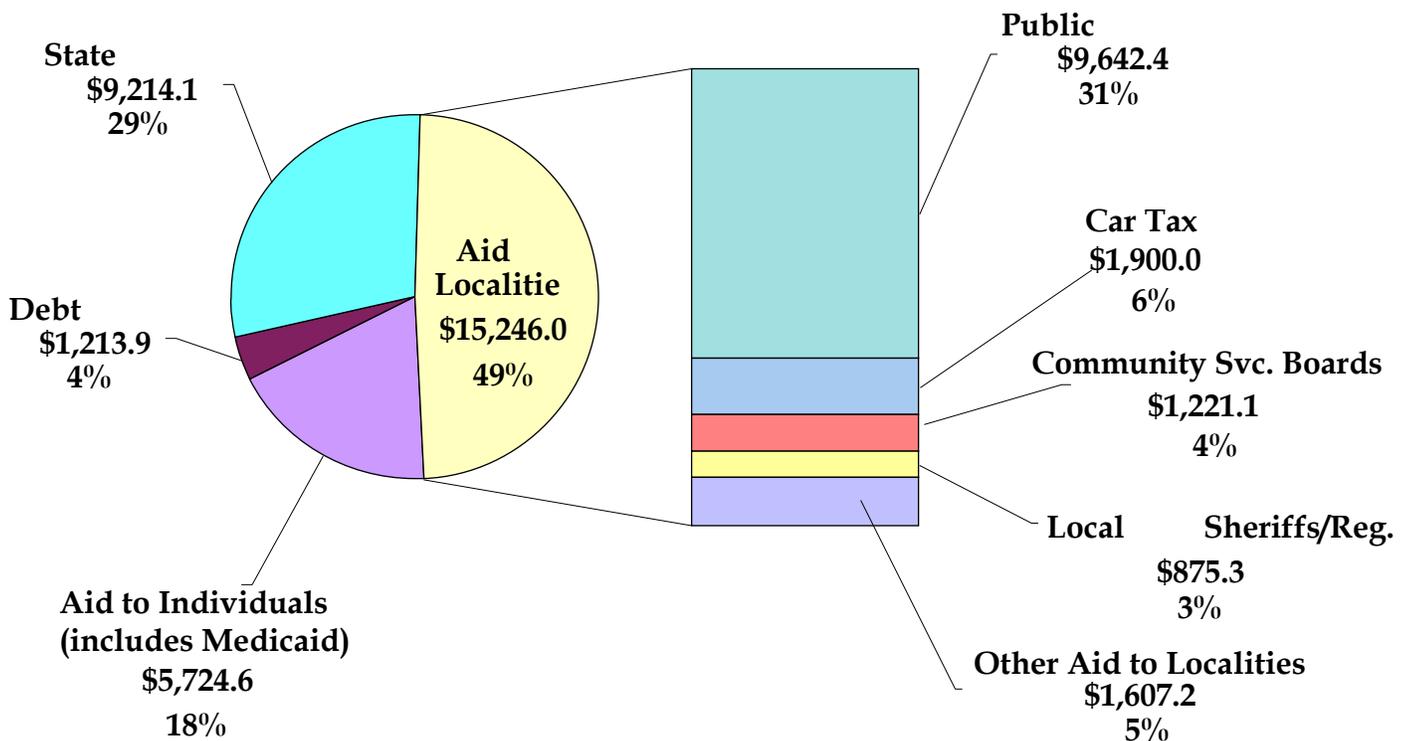
<u>Reduction</u>	<u>FY 2012</u>
2%	\$312.5 million
4%	\$624.9 million
6%	\$937.5 million

# General Fund Budget Drivers: where does the money go?

- Programs included in the reduction calculation on the previous page are detailed in the pie chart below.
- About half of the general fund budget is driven by several large state programs delivered at the local level, and local tax relief.

**2010-2012 GF Operating Budget = \$31,398.1**

**Chapter  
(Biennial, \$ in millions)**

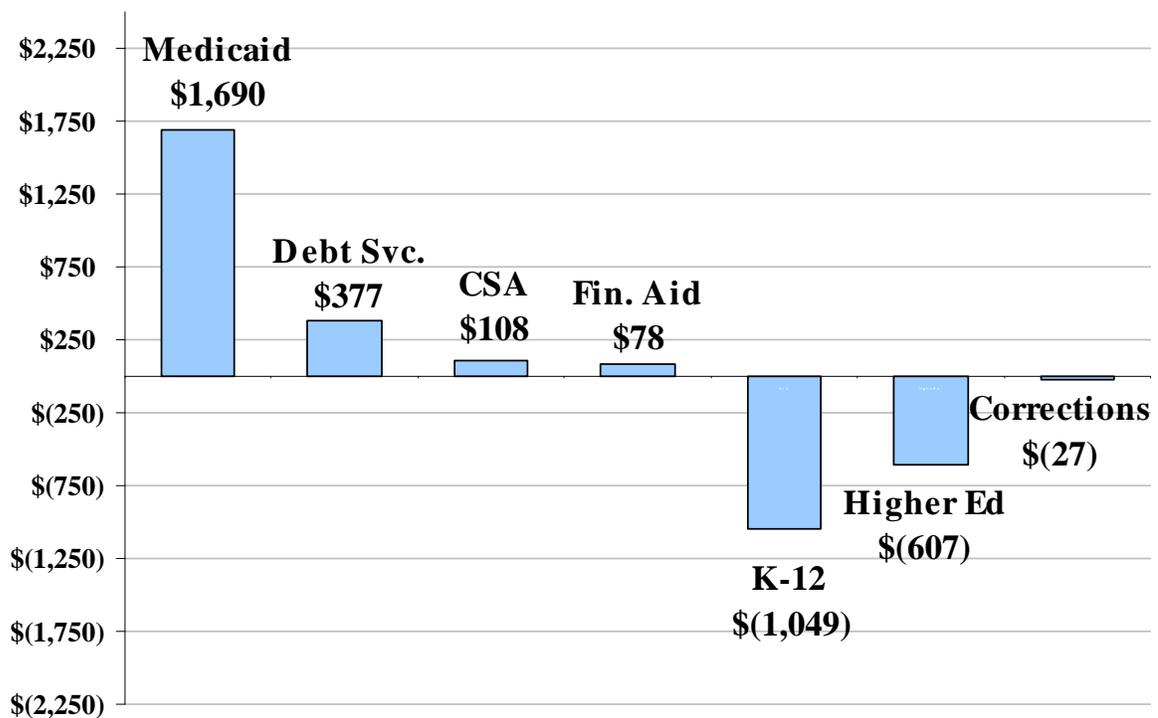


\* "State Agencies" includes institutions of higher education, corrections, natural resources, judicial, executive, and administrative agencies.

## Budget changes have varied across programs, agencies

- When current biennial budgets are compared to the 2006-08 budgets (pre-recession), some programs have seen increases in general fund spending, while others have been reduced to cover budget shortfalls.
  - Medicaid, Comprehensive Services Act, Debt Service, and Financial Aid are among those programs that have grown during this period.

**2006-08 Biennial Budget  
Compared to 2010-12 Biennial Budget  
(GF \$ in millions)**

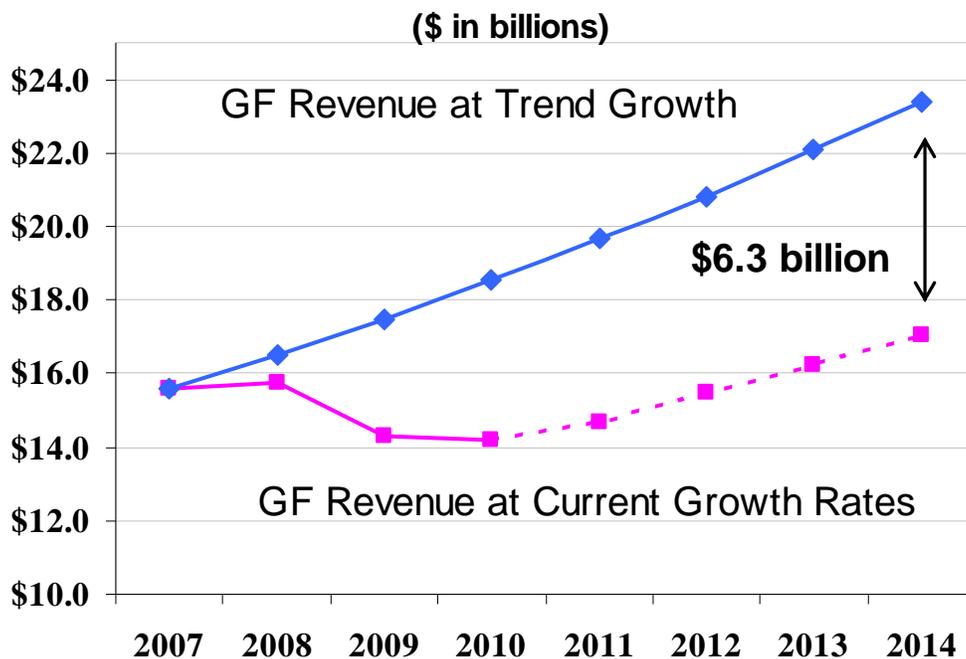


# Looking ahead to the 2012-14 Biennium

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## *Loss of five years of general fund revenue growth.*

- Virginia has seen 5 years of negative or low revenue growth. Even if revenue growth returns to historical levels of about 6 percent per year, the revenue base has been lowered.



- Will revenue growth in the 2012-14 biennium be sufficient to cover mandated or high-priority funding items?
  - Growth would need to be at least 6 percent per year to cover mandated/high priority funding items. However, growth may need to exceed that rate to cover extraordinary items such as the Rainy Day Fund deposit and VRS payback.

# Looking ahead to the 2012-14 Biennium: Budget Pressures

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- **Likely will be cutting budgets again in the 2012 session. Budget pressures include:**
  - Cover one-time revenue sources and one-time savings “propping up” current budget = \$400 to \$500 million for the biennium.
  - Medicaid will likely grow about 8 percent per year = \$880 million for the biennium.
  - K-12 public education rebenchmarking = likely not lower than \$250 to \$300 million. Return to traditional contribution rates for teachers would be an additional \$215 million per year (state share only).
  - VRS, other benefits: Required repayment of deferred VRS contributions = \$74 million per year. Return to traditional contribution rates for state employees would be an additional \$180 million per year.
  - Rainy Day Fund mandatory deposit of \$222 million in FY 2014 (\$50 million reserved in FY 2012 for this purpose.)
  - Other mandatory payments, such as debt service and VITA costs.
  - Employee compensation.
- **Little or no flexibility to restore funding reductions made in the current budget.**
- **Unable to make additional investments in existing programs, new programs, or human capital -- “growth by substitution”.**

## Challenges of the 2011 Session

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- Uncertainty surrounds the national economic outlook and the revenue forecast for Virginia for the remainder of FY 2011 and FY 2012.
  - At the state level, revenues are improving modestly.
  - Risks to the forecast, and there are several, are difficult to quantify.
  - Calls for cautionary approach.
- SFC staff estimates modest upward revenue adjustments of under \$300 million.
- Spending pressures total about \$434 million (assuming no new initiatives, or restoring cuts made last session).
- As a result, the total projected budget shortfall for the 2010-12 biennium may be less than \$200 million.
  - Balancing the budget should not require major additional budget cutting – unless new initiatives are proposed.
- The challenges of the 2012-14 biennium loom large.