

# Overview of the Methodology for the State Budget Outlook (January 2022)

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## Introduction

The purpose of this document is to provide an overview of the methodology used to develop the four-year budget projections pursuant to Chapter 8, Laws of 2012, 1st sp. sess. (SSB 6636). This document summarizes the major components of the projection, the overall approach, as well as the assumptions used in the State Budget Outlook (Outlook) document.

The amounts reflected in the Outlook are the sum of the state General Fund (GF-S), the Education Legacy Trust Account (ELTA), the Opportunity Pathways Account (OPA), and the Workforce Education Investment Account (WEIA). These funds are sometimes referred to as the Near General Fund Outlook (NGF-O) funds. For more information about the July 1, 2020 addition of the WEIA to the NGF-O funds, see Chapter 218, Laws of 2020 (SSB 6660) located here:

<https://app.leg.wa.gov/billsummary?BillNumber=6660&Initiative=false&Year=2019>. During the 2021 legislative session the Fair Start for Kids Account (FSKA), was added to the NGF-O definition (Chapter 199, Laws of 2021). The Governor's 2022 supplemental operating proposal does not propose any resources or expenditures into or out of the account and, as such, it is not reflected in the Outlook.

## Resources

Pursuant to Chapter 8, Laws of 2012, 1st sp. sess. (SSB 6636), the amounts depicted include the actual/projected revenue and other resources. Some of the largest components include:

### Beginning Fund Balance

The Outlook uses the certified fund balance in accordance with generally accepted accounting principles for the most recently closed biennium as the starting point. The beginning fund balance for subsequent Fiscal Years (FY) is equal to the projected ending balance for the previous FY.

### Revenue Forecast

The amounts for the 2021-23 and the 2023-25 biennia reflect the adopted November 2021 quarterly revenue forecast by the Economic and Revenue Forecast Council (ERFC). The provisions of Chapter 8, Laws of 2012, 1st sp. sess. (SSB 6636) call for the ensuing biennium revenue (in this instance, the 2023-25 biennium) to be based on the greater of:

- (1) the official revenue forecast for the ensuing biennium; or
- (2) an assumed revenue increase of 4.5 percent per year for that ensuing biennium.

Because the November 2021 forecast projects revenue growth of less than 4.5 percent per year in the 2023-25 biennium, this Outlook uses the 4.5 percent growth rate.

### Transfers to Budget Stabilization Account (BSA)

Pursuant to a constitutional amendment approved by the voters in 2007 (Article VII, section 12(1), of the Constitution), this reflects the transfer of one percent of general state revenues (GSR) for each FY to the Budget Stabilization Account (BSA). The estimated transfer amounts are based on the calculation of estimated general state revenues as defined in Article VIII, section 1, of the Constitution. The calculation of estimated GSR is based on the November 2021 revenue forecast adjusted for the estimated revenue impacts of the Governor's proposed revenue changes.

In addition to constitutionally required GFS transfer to BSA, the Governor proposes an additional transfer of \$600 million from the GFS to the BSA in FY 2022.

## Overview of the Methodology for the State Budget Outlook (January 2022)

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### Extraordinary Revenue Growth

Pursuant to a constitutional amendment approved by the voters in 2011 (Article VII, section 12 of the constitution), this reflects the transfer of three-quarters of extraordinary revenue growth (ERG) into the BSA. ERG is defined in the state Constitution as growth in general state revenues for the fiscal biennium that exceeds the average biennial percentage growth of the prior five fiscal biennia by one-third. The state Constitution also provides that the transfer only occurs to the extent that it exceeds the normal transfer amount into the BSA. The adopted November 2021 revenue forecast does not project ERG for the 2021-23 or the 2023-25 biennia so no additional BSA transfer is assumed in this Outlook.

### Enacted Fund Transfers

This category reflects all enacted NGF-O fund transfers made through the 2021 legislative session (including special sessions) after accounting for vetoes. For more information, see the 2021 Legislative Budget Notes at: <http://leap.leg.wa.gov/leap/budget/lbns/2021LBN.pdf>.

### Governor's Proposed Resource Changes

#### *Fund Transfers*

In addition to the \$600 million transfer from the general fund to the BSA noted above, the Governor's budget proposes the following NGF-O transfers.

| <b>Transfers Proposed in the Governor's FY 2022 Supplemental Budget (\$'s in 1,000's)</b> |                    |                    |
|---|--------------------|--------------------|
|   | <b>2021-23</b>     | <b>2023-25</b>     |
| From the GFS to the Municipal Criminal Justice Assistance Account                         | \$(761)            | \$0                |
| From the GFS to the State Drought Preparedness Response Account                           | \$(9,000)          | \$0                |
| From the GFS to the Home Security Fund Account  | \$0                | \$(9,000)          |
| From the GFS to the Wildfire Response, Forest Restoration, & Community Resilience Account | \$(87,107)         | \$(94,800)         |
| From the GFS to the Derelict Vessel Removal Account                                       | \$(2,500)          | \$(5,000)          |
| From the GFS to the Clean Energy Transition Workforce Account                             | \$(24,780)         | \$0                |
| From the Streamlined Sales & Use Tax Mitigation Account to the GFS                        | \$3,186            | \$0                |
| From the School Employees Insurance Account to the GFS                                    | \$(972)            | \$0                |
| <b>Total</b>  | <b>\$(121,934)</b> | <b>\$(108,800)</b> |

#### *Proposed Revenue Changes*

The Governor is proposing several pieces of legislation that will affect NGF-O revenues if enacted:

| <b>Governor Inslee's Revenue Proposals (\$'s in 1,000's)</b>       |                  |                   |
|--|------------------|-------------------|
| Capital Gains Tax Modifications (HB XXXX/SB XXXX)                  | \$0              | \$(1,000)         |
| Clean Energy Manufacturing Sale/Use Tax Deferral (HB 1988/SB 5744) | \$(3,115)        | \$(7,188)         |
| HBE – B&O Tax Exemption Extension (HB 1765/SB 5654)                | \$0              | \$(2,110)         |
| I-405/SR 167 Sales/Use Tax Deferral (HB 1990/SB 5705)              | \$(400)          | \$(14,080)        |
| Penalties & Interest (HB XXXX/SB XXXX)                             | \$(800)          | \$(3,200)         |
| <b>Total</b>   | <b>\$(4,315)</b> | <b>\$(27,578)</b> |

## Overview of the Methodology for the State Budget Outlook (January 2022)

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### *Budget Driven Revenue Adjustments*

Adjustments are made to reflect the difference between assumed transfers of cannabis, liquor, and lottery revenue to the General Fund in the November forecast and what is estimated to be available after adjusting for the Governor's proposed spending levels.

| <b>Governor Inslee's Budget Driven Revenue (\$'s in 1,000's)</b> |                   |                    |
|--|-------------------|--------------------|
|  | <b>2021-23</b>    | <b>2023-25</b>     |
| Liquor & Cannabis Board (Marijuana)                              | \$(62,468)        | \$(120,418)        |
| Liquor & Cannabis Board (Liquor)                                 | \$(15,671)        | \$2,791            |
| Lottery  | \$(752)           | \$(1,191)          |
| <b>Total</b>   | <b>\$(78,891)</b> | <b>\$(118,818)</b> |

The marijuana revenue adjustment is larger than usual and reflects a reduction in the estimated amount of Dedicated Marijuana Account (DMA) revenues that would be transferred to GFS as a result of Governor proposed transfers from the Dedicated Marijuana Account (DMA) to the Community Reinvestment Account for a new program in the Department of Commerce.

### **Expenditures**

As the starting point for the expenditure projection, the Outlook utilizes the most recently enacted budget (the 2021-23 Biennial budget). It is based on these 2021-23 budget appropriation levels. Adjustments are then made for the Governor's Maintenance Level (ML) and the Governor's Policy Level (PL) changes. For more information on the 2021-23 biennial budget, please see: [http://leap.leg.wa.gov/leap/budget/index\\_lbns.asp](http://leap.leg.wa.gov/leap/budget/index_lbns.asp).

### Estimating Costs for the 2021-23 and 2023-25 Fiscal Biennia

Per statute, the estimated expenditures in the Outlook reflect the cost to continue current programs, entitlement program growth, and actions required by law in the subsequent fiscal biennium (i.e. the 2023-25 biennium). The general approach to estimating the cost to continue current programs and growth in entitlement programs is by applying a historical growth factor to the FY cost or savings associated with a budget item.

The historical growth factors used to estimate increased costs in the subsequent fiscal biennium are updated each biennium through a joint effort by legislative and executive branch staff and ultimately adopted by the ERFC. The growth factors were adopted by the ERFC on November 18, 2020. Additional information on the calculation of the historical growth factors adopted by the ERFC for the current outlook can be found in the following document available on the ERFC website: <https://erfc.wa.gov/sites/default/files/public/documents/forecasts/rev20201118.pdf>

The current ERFC adopted growth rates are shown below:

| <b>2020 Outlook Growth Rates Summary Table</b>       |                                    |
|--|------------------------------------|
| <b>Default Growth Rate Category</b>                  | <b>Adopted 2020 Growth Factors</b> |
| All Other  | 0.00%                              |
| Corrections  | 1.53%                              |
| Debt Service   | Use Bond Model                     |
| Department of Social and Health Services             | 3.31%                              |
| Higher Education                                     | 0.69%                              |
| K-12 Education                                       | Use K-12 Model                     |
| Low Income Health Care & Community Behavioral Health | 2.86%                              |

## Overview of the Methodology for the State Budget Outlook (January 2022)

---

There are some cases whereby simply applying the growth factor to the cost or savings of a budget item is not used to estimate costs in the subsequent fiscal biennium. These include the following situations:

- **K-12 Education.** K-12 Outlook calculations are derived from the K-12 model, which is updated quarterly based on the caseload forecast for growth and inflationary factors. The K-12 model is periodically updated for other factors such as levy equalization and student transportation.
- **Debt Service.** Debt service calculations are derived from the debt service model. The Outlook statute specifies that "estimates of ensuing biennium expenditures must exclude policy items including, but not limited to, legislation not yet enacted by the legislature." Pursuant to ERFC guidance on June 6, 2019, the model used for the Outlook continues to assume enactment of a bond bill and capital budget for the ensuing 2023-25 biennium.
- **Custom adjustments.** Custom adjustments are used when the estimated annual costs in the subsequent fiscal biennium are expected to be significantly different from the second FY of the current biennium. This occurs primarily when a policy is being phased in during the second FY of a biennium or may be delayed until the subsequent fiscal biennium. In most cases, the growth factor is applied after a custom adjustment is made to reflect the phase in for the policy item. In a small number of cases, the custom adjustment already accounts for the types of growth captured by the growth factor and so the growth factor is not applied.
- **One-Time costs.** Certain items in the budget are one-time for the current biennium and therefore the related costs or savings are not carried forward into the subsequent biennium.
- **Compensation items.** Because the Outlook statute specifically excludes any additional future costs related to collective bargaining agreements (CBAs) not approved by the Legislature, or salaries and benefits, no growth factor is applied to compensation related items. However, a custom adjustment is applied to items that are not fully implemented in the second year of the biennium to capture the full cost in the subsequent fiscal biennium.

### **Maintenance Level Revisions**

In this section, additional adjustments are made to reflect the NGF-O costs of continuing to comply with current law provisions. This is often referred to as ML. Pursuant to the provisions of Chapter 8, Laws of 2012, 1st sp.s. (SSB 6636), this excludes the costs of policy enhancements, including new CBAs not approved by the Legislature, other proposed compensation increases, and costs of any adverse court rulings within 90 days of each respective legislative session.

The Governor's total statewide ML changes estimate, by biennial period:

- ❖ 2021-23 biennial estimate: \$1.144 billion savings, and
- ❖ 2023-25 biennial estimate: \$1.244 billion savings.

These estimates are total impacts. These amounts are based on the Governor's budget and will change prior to the enacted FY 2022 Supplemental budget.

### **Kindergarten – Grade 12 (K-12) Education**

The amounts depicted reflect the November 2021 caseload and K-12 entitlement changes. The K-12 funding is adjusted each year of the ensuing biennium using the K-12 model, which updates the growth and inflationary factors with each forecast. The K-12 model is also periodically updated for other factors such as levy equalization and student transportation.

- ❖ ML adjustments total \$928 million savings in the 2021-23 biennium and \$1.110 billion savings in the 2023-25 biennium.

## Overview of the Methodology for the State Budget Outlook (January 2022)

---

The larger increases are related primarily to salary inflation. The largest savings in this category are related primarily to enrollment and workload adjustments.

### Low-Income Health Care and Community Behavioral Health

The amounts depicted reflect the caseload and per capita cost information, as well as other mandatory maintenance level changes. Some of the major cost components include utilization, caseload, and medical inflation. The average growth factor for this grouping is 2.86 percent per FY from FY 2023 levels.

- ❖ ML adjustments total \$37 million savings in the 2021-23 biennium and \$10 million increased costs in the 2023-25 biennium.

The larger state costs are related primarily to changes in actuarially calculated Medicaid managed care rates, and mandatory caseload adjustments. Larger state savings are related to reductions in medical utilization across some populations.

### Social and Health Services

The amounts depicted reflect caseload and per capita cost information, as well as other mandatory maintenance level changes. Some of the major cost components include caseload, utilization, and severity of client needs. The average growth factor for this grouping is 3.31 percent per FY from FY 2023 levels.

- ❖ ML adjustments total \$47 million savings in the 2021-23 biennium and \$20 million savings in the 2023-25 biennium.

The larger increases are related to a technical correction to the consumer directed employer budget and a receivable adjustment related to the child support program. The larger savings are due to forecasted mandatory caseload adjustments and projected cost changes related to utilization of residential and personal care services.

### Higher Education

Higher Education adjustments are generally related to the Initiative 732 cost of living adjustments, the Washington College Grant program, and to maintenance, operations, and lease adjustments. The average growth factor for this grouping is 0.69 percent per FY from FY 2023 levels.

- ❖ ML adjustments total \$24 million savings in the 2021-23 biennium and \$62 million savings in the 2023-25 biennium.

The larger increases are related to Initiative 732 cost of living adjustments. The larger savings are due to caseload reductions in the Washington College Grant program.

### Corrections

The amounts depicted reflect caseload, as well as other mandatory maintenance level changes. The average growth factor for this grouping is 1.53 percent per FY from FY 2023 levels.

- ❖ ML adjustments total \$73 million savings in the 2021-23 biennium and \$85 million savings in the 2023-25 biennium.

The larger increases are related to the increased costs for nursing relief health services, and adjustments to the employer funding rate for public employee insurance benefits. The larger savings are due to changes in the community supervision caseload, community violator caseload, and male offender caseload forecasts.

## Overview of the Methodology for the State Budget Outlook (January 2022)

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### All Other

This area includes all other agencies not reflected in the preceding Outlook groups. Many are general government agencies, smaller human service agencies, the department of child youth and families (DCYF), natural resource agencies, legislative agencies, and judicial agencies. The average growth factor for this grouping is zero percent per FY from FY 2023 levels.

- ❖ ML adjustments total \$1 million savings in the 2021-23 biennium and \$54 million in the 2023-25 biennium.

The larger increases are related to forecasted cost increases for the Early Supports for Infants and Toddlers program. The larger savings are related to an update to the forecasted cost of the Working Families Tax Credit refund and workload and caseload adjustments.

### Debt Service

The amounts depicted reflect the cost of the debt on all capital budget bonds that were authorized through the 2021 session using the bond model to calculate estimated costs for the 2023-25 biennium.

- ❖ ML adjustments total \$34 million savings in the 2021-23 biennium and \$30 million savings in the 2023-25 biennium.

### **Policy Level Items**

In this section, referred to as PL, adjustments are made to reflect the PL expenditures included in the Governor's proposed budget.

The Governor's total statewide PL changes estimate, by biennial period:

- ❖ 2021-23 biennial estimate: \$4.185 billion, and
- ❖ 2023-25 biennial estimate: \$4.657 billion.

### Kindergarten – Grade 12 (K-12) Education

The Governor proposes to increase funding for K-12 Schools by \$1.023 billion in the 2021-23 biennium and by \$1.251 billion in the 2023-25 biennium. The major components of this increase are:

- ❖ Accelerated learning opportunities;
- ❖ Student support staffing to increase the number of school nurses, social workers, psychologists, and guidance counselors; and
- ❖ Residential outdoor school.

The Governor's proposed savings related to the School Employee Benefits Board (SEBB) health benefit funding rates is also included in this category. These rates are adjusted based on updated rates to incorporate new data from SEBB open enrollment regarding plan choice and demographic information.

### Low-Income Health Care and Community Behavioral Health

The Governor proposes to increase funding for Low Income Health Care and Community Behavioral Health by \$394 million in the 2021-23 biennium and \$951 million in the 2023-25 biennium. The major components for Low Income Health Care and Community Behavioral Health are:

- ❖ Medicaid caseload adjustments from assuming a longer period to conduct dis-enrollments upon conclusion of the Public Health Emergency than assumed in the November forecast;
- ❖ Expansion of the Apple Health program eligibility in the ensuing biennium;

## Overview of the Methodology for the State Budget Outlook (January 2022)

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- ❖ A variety of behavioral health initiatives related to provider rates and relief, housing, and Opioid prevention and treatment services.

### Social and Health Services

The Governor proposes to increase funding for DSHS programs by \$315 million in the 2021-23 biennium and by \$567 million in the 2023-25 biennium. The major components for DSHS are:

- ❖ Continuation of Covid-19 rate enhancements;
- ❖ Increasing the aged, blind, or disabled (ABD) grant standard and in-home personal care needs allowance; and
- ❖ State hospital direct care staffing; and
- ❖ Savings associated with a longer period of enhanced FMAP resulting from extension of the public health emergency.

### Higher Education

The Governor proposes to increase funding for Higher Education by \$66 million in the 2021-23 biennium and by \$87 million in the 2023-25 biennium. The major components of these changes are:

- ❖ Health workforce grants;
- ❖ Cybersecurity degree programs;
- ❖ Financial aid access support at community and technical colleges;
- ❖ Healthcare simulation labs.

### Corrections

The Governor proposes to decrease funding for Department of Corrections (DOC) by \$101 million in the 2021-23 biennium and increase funding by \$158 million in the 2023-25 biennium. The major components for DOC are:

- ❖ Patient centered care;
- ❖ Tolling records staff;
- ❖ Custody relief factor; and
- ❖ Utilizing unspent Coronavirus response funds (CRF) (savings).

### All Other

This area includes all other agencies not reflected in the preceding Outlook groups. Many are general government agencies, smaller human service agencies, natural resource agencies, legislative agencies and judicial agencies. Other PL changes total \$2.174 billion in the 2021-23 biennium and \$1.115 billion in the 2023-25 biennium. The major components are:

- ❖ Appropriations to transportation accounts for ferry projects appropriated in the transportation budget;
- ❖ Liability Account funding;
- ❖ Department of Commerce: Solar Incentives;
- ❖ Department of Commerce: Electric Vehicle Rebates;
- ❖ Department of Health: COVID-19 funding; and
- ❖ Department of Natural Resources: Emergency Fire Suppression.

### Compensation Changes

The Governor's proposed spending reflects the impacts associated with CBAs that include one-time payments for select employees and a 3.25% general wage increase for most state employees effective July 1, 2022 as well as a similar general wage increase for non-represented state employees. Additional

## Overview of the Methodology for the State Budget Outlook (January 2022)

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funding is provided contingent upon the execution of future MOUs with the unions. PL adjustments total \$295 million in the 2021-23 biennium and \$477 million in the 2023-25 biennium.

### Employee Health and Benefits

PL changes reflect the cost projected for employer health and benefits. This includes updated employer funding rates for Public Employee Benefits. PL adjustments total \$19 million in the 2021-23 biennium and \$50 million in the 2023-25 biennium.

### Budget Stabilization Account (BSA)

The Governor proposes an additional transfer of \$600 million from the GFS to the BSA in FY 2022.

### Assumed Reversions

Reversions are the estimated appropriations that will be unspent and revert to the state for re-appropriation. Consistent with prior outlooks, reversions are estimated at approximately 0.5% of GF-S appropriations. Additional adjustments for reversions are made in accordance with prior direction from the ERFC.

The total reversions assumed are \$313 million savings in the 2021-23 biennium and \$306 million savings in the 2023-25 biennium; totaling \$619 million savings over the Outlook period.

These totals include:

- 0.5% of GF-S appropriation reversions of \$296 million savings in the 2021-23 biennium, and \$306 million savings in the 2023-25 biennia, totaling \$602 million savings over the Outlook period; and
- Additional K-3 reversion assumption of \$17 million savings in the 2021-23 biennium.