

To: Economic and Revenue Forecast Council

From: State Budget Outlook Work Group

Date: September 13, 2024

Subject: Accuracy of projections for ensuing biennium expenditures.

Chapter 82.33.060 RCW requires the state budget outlook work group to analyze the reliability of the methodology for projecting ensuing fiscal biennia and to make recommendations to change the outlook process to increase reliability and accuracy. The language from the statute is as follows:

"The state budget outlook work group, in consultation with the economic and revenue forecast work group and outside experts if necessary, must analyze the extent to which the proposed methodology for projecting expenditures for the ensuing fiscal biennia may be reliably used to determine the future impact of appropriations and make recommendations to change the outlook process to increase reliability and accuracy. The recommendations are due by December 1, 2013, and every five years thereafter."

The following memo provides an update from the state budget outlook workgroup. This analysis was last completed in 2019.

Background:

Chapter 8, Laws of 2012 (SSB 6636) requires that beginning with the 2013-2015 fiscal biennium, the Legislature must enact a budget bill that leaves a positive ending fund balance in the state General Fund and related funds and that the projected maintenance level (ML) for the budget in the ensuing biennium may not exceed available fiscal resources. Related funds for purposes of this requirement are defined as the Washington Opportunity Pathways Account, the Education Legacy Trust Account, the Workforce Education Investment Account, and the Fair Start for Kids Account¹. The act directed that the estimate of ensuing biennium expenditures must include ML items including, but not limited to:

- Continuation of current programs.
- Forecasted growth of current entitlement programs.
- Actions required by law, including legislation with a future implementation date.

¹ There are currently no revenues to or appropriations from the Fair Start for Kids Account.

The act also directed that estimates of ensuing biennium expenditures must exclude policy items including, but not limited to:

- Legislation not yet enacted by the Legislature.
- Collective bargaining agreements (CBAs) not yet approved by the Legislature.
- Changes to levels of funding for employee salaries and benefits unless those changes are required by statute.
- Costs of court rulings issued during or within fewer than ninety days before the beginning of the current legislative session.

Summary of the Methodology Used to Project Ensuing Biennium Expenditures

The current methodology for estimating expenditures for the ensuing biennium has been developed by the technical work group and approved by the Economic and Revenue Forecast Council (ERFC). The general approach to estimating ensuing biennia costs for current programs and growth in entitlement programs is by applying a historical growth factor to the second fiscal year (FY) for agency base budgets and for the cost or savings associated with each budget item to derive the ensuing biennia by FY. The historical growth factors used to estimate increased costs in the subsequent fiscal biennium are updated each biennium by the technical work group and adopted by the ERFC. For the 2022 growth factor update cycle, the ERFC moved to not update the prior growth factors due to variations in growth factor data caused by the COVID-19 pandemic.

There are some cases where an approach other than simply applying the growth factor to the cost or savings of a budget item is used. These include the following situations:

- **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 not yet approved by the Legislature, or salaries and benefits, no growth factor is applied to most 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. In addition, adjustments for compensation increases that are

required under current law such as cost of living adjustments for community & technical colleges (in accordance with Initiative 732) and K-12 education are included. Also included is the impact of estimated pension rate changes (assuming no change to pension funding methodologies or benefits).

- **K-12.** Beginning with the 2017 legislative session, K-12 calculations for the ensuing biennium shifted from a growth factor approach to utilization of a K-12 model. The K-12 model updates caseload and inflationary factors with each forecast and is continually updated for other factors such as levy equalization, enrollment, student transportation, and staff mix. The K-12 model is also used for fiscal notes and legislative policy proposals.
- **Debt Service.** Beginning with the 2018 legislative session, debt service calculations for the ensuing biennium shifted from a growth factor approach to utilization of the debt service model.

Challenges in Assessing the Reliability of Outlook Projections

There are a variety of challenges in assessing the reliability of the methodology that is used to estimate ensuing biennium expenditures. These include:

- **Supplemental budget policy changes.** The original biennial budget provides an estimate of the projected ML of the ensuing biennium including the policy changes made during that legislative session. However, policy changes made in the supplemental budget continue to revise the budget and ensuing biennium projections. Data available to staff do not provide sufficient detail to know what portion of actual ML costs in the following biennium are specifically related to policy changes made in the supplemental budget. As there is no way to identify what the ML in the following biennium would be without policy level changes in the supplemental budget, the most accurate comparison for the accuracy of the Outlook projections is the comparison of the estimated expenditures in the supplemental budget sessions with the following biennium's enacted ML biennial operating budget. Because of this, recommendations for the Outlook accuracy utilize supplemental budgets only.
- **Initiatives, court rulings, and changes in federal law.** Initiatives, court rulings, and changes in federal law which come after a budget is enacted and an Outlook is adopted can drive significant changes in ML expenditures. An example of this is Initiative 1351 (K-12 class size funding), approved by voters in November 2014 (after the 2014 supplemental budget and related outlook was adopted). The ML adjustment for I-1351 was an increase of \$2 billion dollars NGF-O in the 2015-17 biennium. Ultimately, the 2015-17 budget suspended the initiative in policy level but the maintenance level shows these increased costs. These costs were not (and could not) have been included in the outlook adopted in May 2014 for the enacted 2014 supplemental operating budget as the initiative had yet to be considered by the voters.

- **Health benefits and compensation.** As noted above, the outlook statute requires that, changes to levels of funding for employee salaries and benefits be excluded from ensuing biennium estimates unless those changes are required by statute. Budgeted funds for health benefit employer contribution rates in some sessions are adjusted for surplus balances that may not be available the following year when the biennial budget for the ensuing biennium is being written.

Analysis of Outlook Reliability for the 2015-2023 Time Period

Since the Outlook requirements were adopted, there are five budgets that provide an opportunity to compare an enacted ML to the estimates that were projected in prior supplemental budget Outlooks. The following table provides the estimated and actual ML expenditures for these budgets.

Session	Outlook Estimated ML	Ensuing Biennium Actual ML	Difference	Difference Percent
2014 ²	\$ 36,576	\$ 37,111	\$ 535	1.5%
2016	\$ 41,728	\$ 41,636	\$ (92)	-0.2%
2018	\$ 50,485	\$ 50,485	\$ -	0.0%
2020 ³	\$ 57,126	\$ 55,980	\$ (1,146)	-2.0%
2022	\$ 64,834	\$ 65,060	\$ 226	0.3%

As noted in the prior section, the most accurate comparison for the purposes of assessing outlook accuracy are the supplemental budget (even year) sessions, as there is no way to identify what the ML for ensuing biennia would have been without the policy changes adopted in those supplemental sessions. Outlook projections for biennial budget (odd year) sessions are included in Appendix A for informational purposes only.

There have been two comparison periods (2020 and 2022) since this report was last updated in 2019. The 2020 supplemental budget over-estimated 2021 ML expenditures by 2%. This is a significant margin compared to historical figures. However, this can be largely attributed to impacts from the COVID-19 pandemic. The pandemic reduced the 2021 session ML relative to prior projections due to caseload decreases in areas like K-12

² To improve comparability, an adjustment was made for the 2015-17 biennium to remove the \$2 billion in ML expenditures that were associated with Initiative 1351, which was adopted after the 2014 budget and Outlook were adopted.

³ The WEIA was added as an Outlook fund in the 2021-23 biennium. WEIA expenditures are included in the 2020 session Outlook projections to provide an accurate comparison.

Education, Corrections, and Social and Health Services. Post-pandemic, the 2022 supplemental budget projection underestimated the enacted 2023 session ML by 0.3%.

Recommendations

As noted above, the original methodology has evolved to utilize the K-12 model and debt service model for more accurate projections in these areas. Fiscal growth factors have been reviewed and updated each biennium.

The workgroup believes that the fiscal growth factors should continue to be updated in the fall of even numbered years, and the approach of using the K-12 model and debt service model should be continued. The workgroup is recommending updated growth factors for the 2025-27 budget cycle. Based on the above analysis, the workgroup has no further recommendations for changes to the methodology for projecting ensuing biennium expenditures.

Appendix A

(dollars in millions)

2013-15 Biennial and 2014 Supplemental Projections of Enacted 2015-17 ML

Session	Outlook Estimated	Enacted 2015 Session Adj. For I-1351	Difference	Difference Percent
2013	\$ 36,052	\$ 37,111	\$ 1,059	2.9%
2014	\$ 36,576	\$ 37,111	\$ 535	1.5%

2015-17 Biennial and 2016 Supplemental Projections of Enacted 2017-19 ML

Session	Outlook Estimated	Enacted 2017 Session	Difference	Difference Percent
2015	\$ 41,575	\$ 41,636	\$ 61	0.1%
2016	\$ 41,728	\$ 41,636	\$ (92)	-0.2%

2017-19 Biennial and 2018 Supplemental Projections of Enacted 2019-21 ML

Session	Outlook Estimated	Enacted 2019 Session	Difference	Difference Percent
2017	\$ 49,890	\$ 50,485	\$ 595	1.2%
2018	\$ 50,485	\$ 50,485	\$ -	0.0%

2019-21 Biennial and 2020 Supplemental Projections of Enacted 2021-23 ML

Session	Outlook Estimated Adj. for WEIA*	Enacted 2021 Session	Difference	Difference Percent
2019	\$ 56,834	\$ 55,980	\$ (854)	-1.5%
2020	\$ 57,126	\$ 55,980	\$ (1,146)	-2.0%

2021-23 Biennial and 2022 Supplemental Projections of Enacted 2023-25 ML

Session	Outlook Estimated	Enacted 2023 Session	Difference	Difference Percent
2021	\$ 61,181	\$ 65,060	\$ 3,880	6.0%
2022	\$ 64,834	\$ 65,060	\$ 226	0.3%