
Financial Outlook Report

Interim Joint Committee on Appropriations and Revenue

June 27, 2013

Jane C. Driskell, State Budget Director

John Hicks, Deputy State Budget Director

Greg Harkenrider, Deputy Exec. Director,
Governor's Office of Economic Analysis

Overview

- Introduction
- Current 2012-14 Status
- Next Biennium Outlook
- Planning for next Biennial Budget Process
- Q & A

Current 2012-14 Status

- Tight fiscal conditions lie ahead
- General Fund Receipts have been flat or declining for three of the last four months
- On watch list:
 - Sales and Use Tax
 - Likely to end FY13 lower than FY12
 - Only 3 such nominal declines since 1980
 - Severance Taxes
 - Coal production and demand declining
 - Natural Gas prices remain subdued

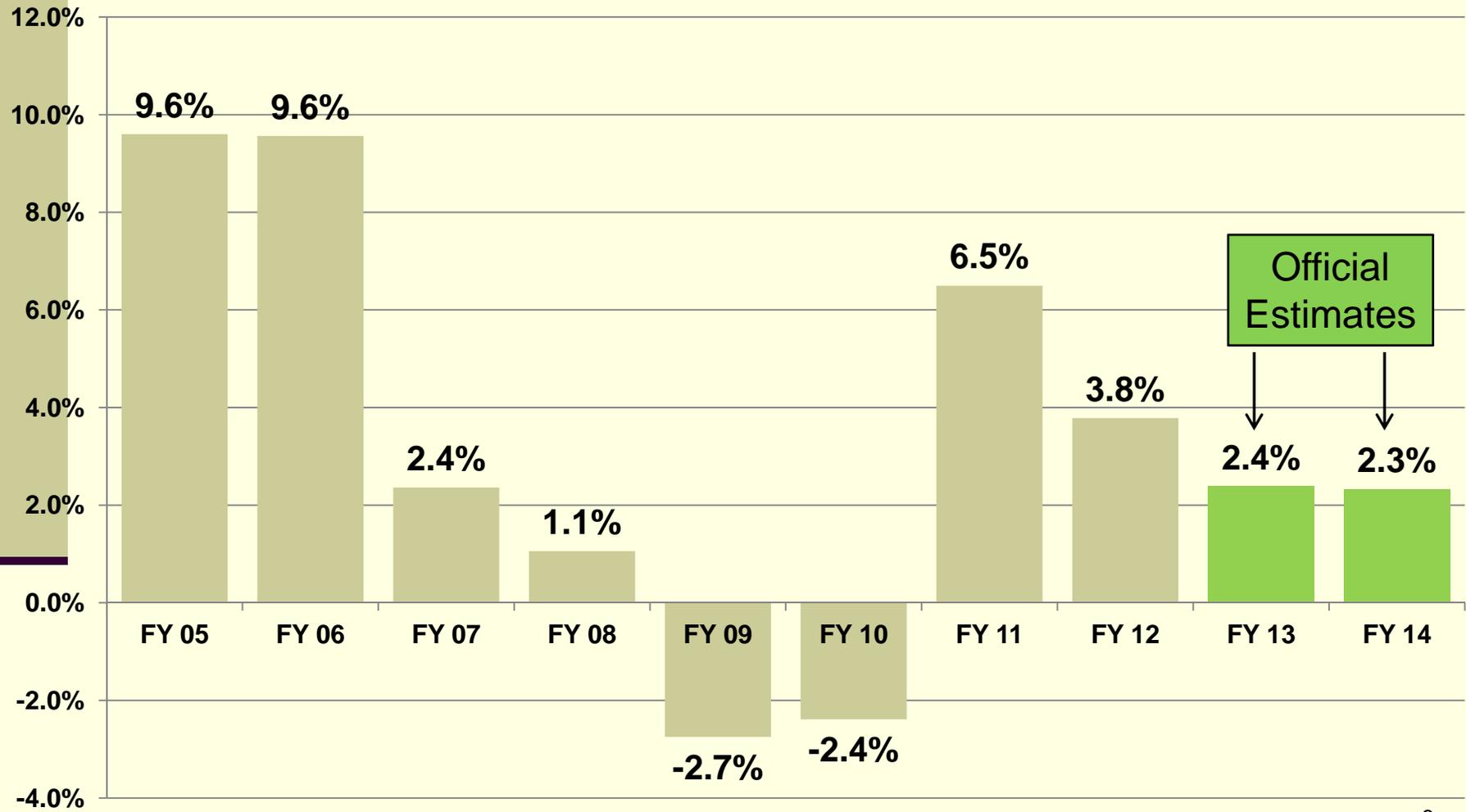
That Stubborn Economy

- When will “next year” finally get here?
 - We are now approaching the fifth year of a recovery but aggregate nominal growth rates have yet to hit robust levels
 - The newest explanation for tepid growth:
 - Expiration of payroll tax cut
 - Federal government sequestration

Fiscal Survey of States

- According to the Survey of Fiscal Conditions issued earlier this month our environment is consistent with a number of states:
 - State budgets are not growing fast enough to make up for recession impacts and inflation.
 - States continue to be challenged with providing resources in critical areas despite “fiscal distress” beginning to subside.
 - One-third of states expect FY13 General Fund spending growth to be less than 2%.

Modest Revenue Growth Predicted (percent change from prior fiscal year)



General Fund Update

- The latest completed quarter of revenue data showed revenues flattening to 0.2 percent growth (comparing the 3rd quarter of FY13 to the 3rd quarter of FY12).
- Statutorily-required internal projections from OSBD predicted that FY13 would close \$23.4 million short of the enacted estimates, an error of 0.2% compared to budgeted estimates.

Since the Last Quarterly Report...

- General Fund receipts fell 2.0 percent in April
 - April and June are typically the largest GF receipt months of the year
 - The fourth quarter of the fiscal year is always heavily weighted due to timing on income taxes
- Receipts climbed 8.3 percent in May
- June collections need to equal \$917.2 million to hit the enacted revenue estimates

June Receipts, Previous Years

(Comparing Needs for FY13 to Prior Year Actual Collections)



Road Fund Update

- The latest completed quarter of Road Fund data showed flattening to 3.4 percent growth (comparing the 3rd quarter of FY13 to the 3rd quarter of FY12).
- Statutorily-required internal projections from OSBD predicted that FY13 would close \$36.5 million short of the enacted estimates (compared to a total Road Fund base of \$1.5 billion).

Since the Last Quarterly Report ...

- Road Fund receipts soared 18.3 percent in April
- Road Fund receipts were flat in May due to timing, but fuels taxes grew sharply
- Both Motor Vehicle Usage and Motor Fuels taxes have shown considerable growth in the 4th quarter
- Road Fund will need to grow 5.2 percent in June to equal the official estimate

Road Fund Revenue Trends

- Positive

- Starting in July, motor fuels taxes will benefit from the statutory adjustment to the average wholesale price of fuel

- Areas of Concern

- Falling fuel prices could destabilize Road Fund
 - AWP floor is \$1.786 (16.1 cents per gallon)
 - Current AWP is \$2.878 (25.9 cents per gallon). The statutory AWP of \$2.878 has now caught the market price of \$2.884
 - Current state total fuels rate on gasoline is 32.3 cents per gallon
 - Federal rate is an additional 18.4 cents per gallon on gasoline and 24.4 cents per gallon on diesel fuel

Budget Balancing Measures During Beshear Administration

				Amount (millions)	Most Common % Cut
	Fiscal Year	Description			
1	2008	Budget Reduction		\$ 76	3.0%
2	2009	Enacted Reduction		\$ 176	12.0%
3		Mandated Budget Gap		\$ 180	4.5%
4		Budget Reduction		\$ 147	4.0%
5	2010	Budget Reduction - Round 1		\$ 273	4.0%
6		Budget Reduction - Round 2		\$ 49	3.0%
7	2011	Enacted Reduction		\$ 61	3.5%
8		Mandated Budget Gap		\$ 131	1.5%
9	2012	Enacted Reduction		\$ 81	1.0%
10		Mandated Budget Gap		\$ 169	2.0%
11	2013	Enacted Reduction		\$ 140	8.4%
12		Mandated Budget Gap		\$ 40	TBD
13	2014	Enacted Reduction		\$ 6	NA
Total				\$1.6 billion	38.4%

Most State Agencies Cut 8.4%

- 8.4% Cuts to Most State Agencies in FY 13 and no increases to that in FY 14
 - 6.4% Cuts to Universities and KCTCS
 - 4.2% Cuts to Education and Workforce agencies
 - 2.2% Cuts to most Justice and Public Safety agencies
- Critical Areas Exempt from Cuts
 - SEEK and Preschool;
 - Medicaid;
 - Corrections;
 - Debt Service;
 - Health Insurance and Retirement;
 - Teacher's Retirement;
 - Student Financial Aid;
 - Coal Severance Funds;
 - Community Based Services;
 - Behavioral Health;
 - Public Advocacy;
 - Revenue Operations;
 - Tourism-Fair Board, Horse Park;
 - Mine Permitting, Reclamation & Enforcement;
 - Veterans' Affairs.

Subsequent Events

- **Pension**-Full Funding for ARC
- **Corrections** - Higher Inmate Population than Budgeted
- **Sequestration**-Current impact estimated approximately 5% (\$62 million) total in cuts to Nondefense discretionary programs
- **Settlements**-Online gambling suit
- **Medicaid**-Woodwork Effect
- **Marketplace Fairness Act (MFA)**-Internet sales tax bill is stalled in the House Judiciary Committee of Congress
- **Lottery**-KENO

Necessary Government Expense (millions)

FY 13 Estimate \$53.6

\$7.9 million more than the FY 12 General Fund Surplus

Notes on Largest Amounts:

Corrections \$25.0

Guardian Ad Litem \$9.2

Military Affairs-Disasters and Planned Events \$6.5

Forest Fire Suppression \$5.0

County Costs-Example: Courthouse Security \$3.7

What to do if short?

- **General Fund:** If actual General Fund receipts are short by the estimated \$23 million from the April Quarterly Report: Actual expenditures less than appropriated will be sufficient to cover the \$23 million revenue shortfall.
- **Road Fund:** For a revenue shortfall at the end of the fiscal year, unexpended Road Fund appropriations in the areas of debt service and personnel/operating areas are first used to balance.

What to do if surplus?

- **General Fund:** Surplus Expenditure Plan places Necessary Government Expenses as the first call. The second use is a deposit into the Rainy Day Fund.
- **Road Fund:** Surplus funds go to the State Construction Account for the 2012-14 Biennial Hwy Construction program.

LGEAF and LGEDF

	FY 13 Enacted	FY 13 Actual	FY 13 Variance
Local Government Economic Assistance Fund	\$73.8	\$55.1	(\$18.7)
Local Government Economic Development Fund	\$75.3	\$43.0	(\$32.3)
Single County Funds	\$50.2	\$28.7	(\$21.5)
Multi-County Funds	\$25.1	\$14.3	(\$10.8)

What Does the Future Hold?

- Short Term and Long Term Budget Challenges
 - Need to increase funding for education
 - Demand for government services goes up when the economy is down; the effects of the recession continue to elevate demand for services
 - Adequately fund pension obligations
 - Address infrastructure needs – education, water & sewer, parks, other
 - Impact of Federal budget cuts on K-12 Schools
 - Need to increase the Rainy Day Fund
 - Health care and justice system costs continue to increase faster than revenues
 - Aging population will require additional services

Early Look at Next Biennial Budget

Structural Imbalance of 2012-14 General Fund Budget

FY 14 Beginning Balance	\$52.1
Use of Rainy Day Fund	\$49.0
Fund Transfers in excess of \$40 million	<u>\$56.3</u>
Total	\$157.5
FY 14 Percent of General Fund Revenue	1.6%
FY 12 Percent of General Fund Revenue	4.6%

Early Look at Next Biennial Budget (con't)

	FY 15 <u>(millions)</u>
Revenues	
Revenue Growth of 2.5% to 3%	\$238 - \$286
Funding Plan for SB2	\$100
Budgetary Requirements	
Fund Recurring Expenses Supported by One-time Money	\$157
Pension Contributions for Teachers and State Employees- Under Current Schedule	\$28
Full Funding for the ARC for Kentucky Retirement Systems	\$100-\$120
Medical Inflation in Medicaid (5%)	\$75
Medical Inflation in Health Insurance for Teachers and Public Employees (5%)	\$40
Total	<u>\$400 - \$420</u>

Early Look at Next Biennial Budget (con't)

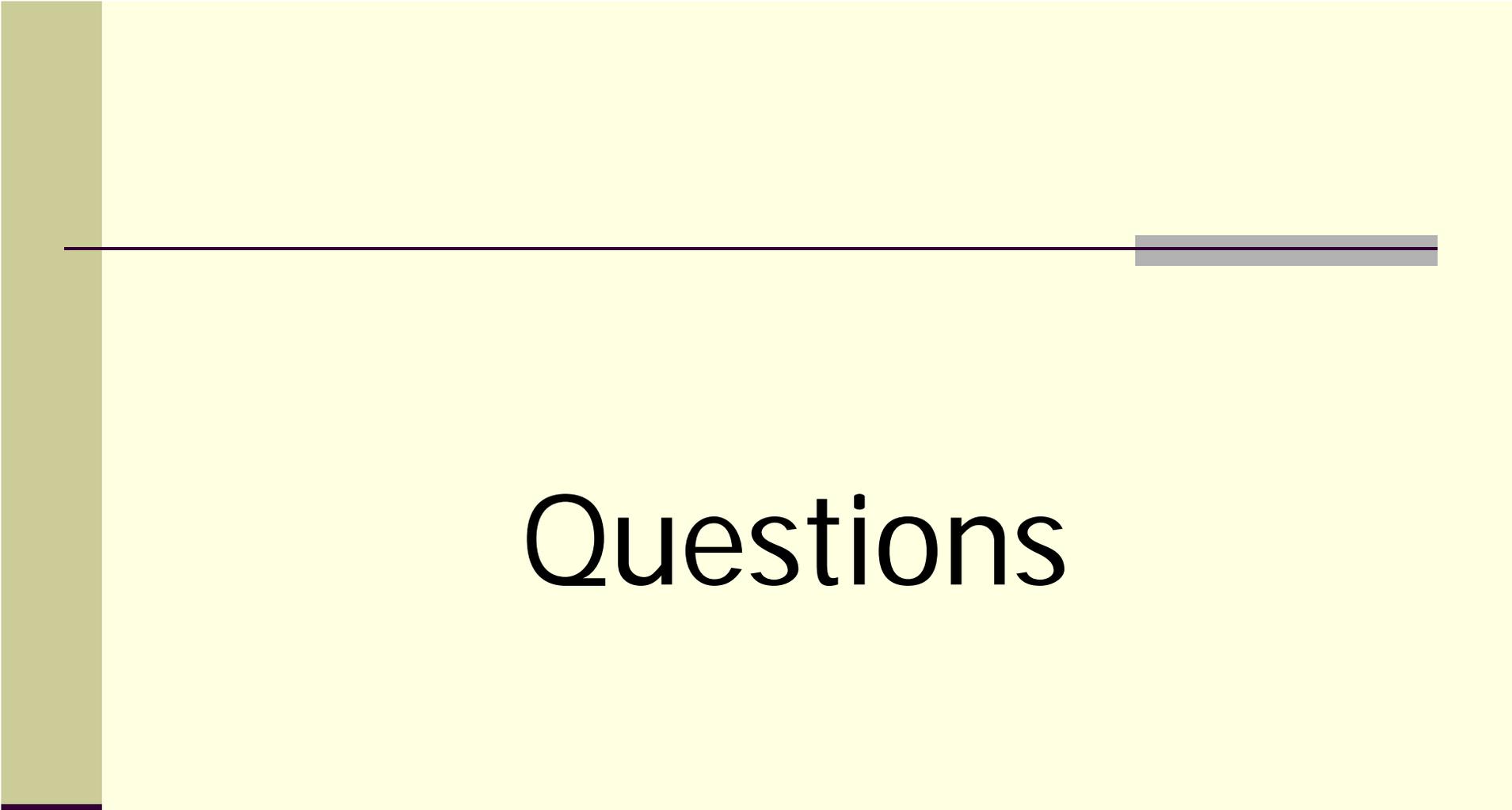
	FY 15 (millions)
Other Critical Needs	
SEEK Funding (every 1% increase)	\$29
Teacher Raises (every 1%)	\$23
Restore Cuts to K-12 Programs like Textbooks, Professional Dev.	\$64
Increase Funding for School Safety	?
Increase Postsecondary Education Funding (every 1% increase)	\$9
Restore Cuts for DCBS - Protective Services, Child Care Assistance	\$87
Debt Service for Any New Capital Projects	?
Salary Increment for State Employees (every 1% increase)	\$8
Relieve Caseload levels for Public Advocates and Prosecutors	?
Other Priorities	?

Planning for next Biennial Budget Process

- Budget Instructions
- Capital Planning
- Budget Requests

Upcoming Forecasts

- Pursuant to KRS 48.120, economic and revenue forecasts will be prepared in the upcoming months
 - August 15th – Planning Estimates
 - October 15th – Preliminary Estimates
 - Dec/Jan – Official Estimates



Questions

Financial Outlook Report

Interim Joint Committee on
Appropriations and Revenue

June 27, 2013

Jane C. Driskell, State Budget Director
John Hicks, Deputy State Budget Director
Greg Harkenrider, Deputy Exec. Director,
Governor's Office of Economic Analysis