2006-2008 Executive

Budget Overview

For the Senate Appropriations and Revenue Committee

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State Budget Director
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Welcome to our web site.

Our goal is to help you access information about Kentucky's Budget office and the documents we prepare. This site contains both past and present Budgets of the Commonwealth, Executive Budget Recommendations and much more budget-related material. Please follow the Publications link on the left to find current information or select the Archives link to find past budget information. Use the Contact Us link to let us know what you think of this site.

Recent Publications

Governor Fletcher's 2006-2008 Biennial Executive Budget recommendation presented January 17, 2006

Study on Impact of Right-To-Work Legislation

Quarterly Economic and Revenue Report Second Quarter - Budget Year 2006

Official Revenue Estimate - December 2005 (PDF Format: 516 KB)

Economic Briefs for the week of January 27, 2006
(PDF Format: 48 KB)

Tax Receipts for December 2005
(PDF Format: 27 KB)

Most Recent Economic Indicators November 2005
(PDF Format: 74 KB)

Interim Joint Committee on Appropriations and Revenue Meeting - 9-22-2005 - Presentations

- Status of Capital Projects and Bonding (PDF Format: 28 KB)
- Impact of Gasoline on Revenues and Expenditures (PDF Format: 23 KB)

2006-2008 Branch Budget Request Manual (PDF Format: 4,551 KB)

SCOPE Presentation - September 18 2005 (PDF Format: 3,176 KB)
A good budget is . . .

. . . an efficient budget
✓ Builds on work of the Budget Stability Initiative and creates new resources by reductions to base budgets within the biennium
✓ Lives within our means; makes no promises it can’t keep; imposes no new or higher taxes; doesn’t drain the rainy date fund; preserves the traditional policy on debt capacity

. . . a progressive budget
✓ Funds progressive education and economic development initiatives as main engines of progress
✓ Provides major new funding for teacher compensation, early learning and technology; makes major investments in new economy and global outreach initiatives; funds programs and tax relief for small business

. . . a responsible budget
✓ Fulfills the state’s commitments in Medicaid, pension plans and state health insurance
Competing priorities: have to’s and want to’s

Commitments and obligations are costly to fulfill

✓ Healthcare costs are the root of the problem with Medicaid, state health insurance and pension plans
✓ Commitments must be fulfilled, even when the cost is unexpectedly high
✓ These are national problems; Kentucky is not unique

Policy initiatives are essential to state’s progress

✓ Education and economic development are the main engines of the state’s progress
✓ Improvements in P12 and higher education require funding
✓ Selection of capital projects requires tough choices
We can fulfill both objectives because . . .

- We saved money in FY05, contributing to $214 million surplus that we haven’t spent.
- We recognized the cost pressures early and began a $142 savings initiative.
- We are controlling Medicaid costs by reducing utilization and tailoring benefits to specific eligible populations.
- We have streamlined our health insurance program through self-insurance.
- We have been strengthening the Kentucky economy.
Where will new money ($1.4 billion) be used?

Commitments
- Medicaid
- Employee benefits
- Others

$995 million (70%)

Policy initiatives
- Education
- Economic Dev
- Others

$420 million (30%)

Where is the $1.4 billion coming from?

Growth revenue
- New FY07 - FY08 rev
- Increased FY06 rev
- Transfers, other rev

$978 million (69%)

Efficiency savings
- Saved FY05 surplus
- Budget stability
- Cuts to base funding

$436 million (31%)
Excess of new FY06 revenue over current year appropriations $273 ($392 m - $118 m)

New FY07 revenue $125 m

New FY08 revenue $335 m

FY07/08 restricted fund transfers $169 m
FY07/08 other resources $77 m

Growth revenue
✓ New FY07 - FY08 rev
✓ Increased FY06 rev
✓ Transfers, other rev

$978 million (69%)
Commitments
✓ Medicaid
✓ Employee benefits
✓ Others

$995 million (70%)

Other $31 m
Increase in student ADA $24 m
MHMR/Comm Based Svc $66 m
Corrections $60 m
Dedicated revenues $60 m
State employee increment $32 m

Pension funds $93 m
State health insurance $165 m

2% Salaries, school district $205 m

Medicaid $259 m
FY07/08 reductions to base $170 m

FY06 Budget Stability Initiative $142 m

Remaining FY05 Surplus $124 m

FY06 Budget Stability Initiative $142 m

FY07/08 reductions to base $170 m

Efficiency savings
✓ Saved FY05 surplus
✓ Budget stability
✓ Cuts to base funding

$436 million (31%)
Policy initiatives

- Education
- Economic Dev
- Others

$420 million (30%)

P-12 initiatives $171 m

Including teacher compensation
(excluding 2% base increase)

Postsecondary education $140 m

Public Advocacy $6 m
State Police $12 m
New debt serv (ex SFC) $33 m
Small business AMC relief $13 m
Small business health ins $20 m
Economic Development $25 m
Budget stability initiative

- Began planning after last budget adopted, anticipating increased costs of commitments
- Generates $142.5 m in FY06, with schools, universities and Medicaid exempted
- $83.2 m will result from General Fund lapse (including debt service lapse)
- $59.3 m will result from restricted fund transfers
Advice from the rating agencies

- Enact a biennial budget
- Minimize structural imbalance
- Don’t exceed our traditional debt capacity
- Strengthen the Kentucky economy
- Maintain and build the rainy day fund
Structural imbalance points

✓ We are carrying forward a large cash balance
✓ We will be transferring a lot of money from restricted funds to the General Fund
✓ Healthcare expenses are rising faster than the revenue base
Structural imbalance points

But . . .

✓ Tax modernization will be fully implemented within the budgeted biennium
✓ A portion of the restricted fund transfers are recurring
✓ We are bringing healthcare costs under control
Don’t drain the rainy day fund

- We have a significant structural imbalance
- Our bond rating has been on a negative watch
- We are routinely borrowing to the limit of our debt capacity
- Incremental shifts in bond rating result in higher interest rates and millions of dollars in additional expense
- Current balance ($119 million) is inadequate
- $77 million needed to achieve national average
A progressive budget: top view numbers

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Appropriations</th>
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<tbody>
<tr>
<td>2006 (Revised)</td>
<td>$8,401,719,400</td>
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<tr>
<td>2007</td>
<td>$8,770,400,200</td>
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<tr>
<td>2008</td>
<td>$9,190,502,400</td>
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</table>

Recommended Bond Projects $939.2 million
Themes of funded P12 initiatives

- It’s about the kids: higher test scores and student achievement
- Not how much we spent but how much we bought
- Focus on teacher compensation, not just salaries
- Remarkable disparities in teacher compensation
Variation in teacher salaries is remarkable

Salary variation 2004 (standard deviation in salaries divided by mean salary)

- 0.126 - 0.157
- 0.157 - 0.18
- 0.18 - 0.202
- 0.202 - 0.226
- 0.226 - 0.279
Teacher compensation: $232.8 million new funding

Additional days in the school calendar

- One professional development day in FY07
- Two instructional days in FY08 (current Kentucky average is 175; national average is 180)

Base increase of 2% each year

Enhanced professional compensation ($20m)

- Addresses critical needs and shortages
- Creates opportunities for professional advancement
Instructional days in neighboring states
Criteria for differentiated compensation plans

- Address critical shortage areas
- Emergency certified teachers
- Difficult assignments and hard-to-fill positions;
- Voluntary career advancement opportunities for classroom teachers who voluntarily wish to participate to reward teachers for increasing their skills and knowledge;
- Instructional leadership
Other education initiatives

- Preschool program - $46m
- Kentucky Education Network - $37m
- Ready, Set Success - $1m additional
- Read to Achieve - $8m additional
- Technology in coal counties - $10m
- Opening vocational and technical schools - $4.6m
- School Construction - $100m
Funding for higher education

- Funding moved strongly in the last budget; many achievements in recent years; study shows college education is generally affordable, but there are gaps.
- Base funding increases through benchmark process - $50m; this is affordable and sustainable.
- Respectful of CPE’s jurisdiction re: distribution of operating funds through benchmark formula.
- No funds will be taken from the institutions for the BSI.
Postsecondary education

Significant investment in capital projects - $465m
Heavy investment in research; infrastructure investments
Research support at UK & UL - $10.5m
Regional stewardship - $4.8m
Adult education and literacy - $4m
Workforce development through KCTCS - $1.5m
Performance funding - $1m
Principal leadership - $1m
Student financial aid

Need and merit-based programs - $22.2m
Additional need–based aid in coal counties - $10m
National Guard Tuition Assistance – full funding
Mining engineering scholarships - $.4m
Postsecondary education capital investments

UK – Biological/Pharmaceutical; Hospital
UL – Health Sciences Research; Center for Predictive Medicine
KCTCS
- Advanced manufacturing – Gateway
- Emerging Technology – West Kentucky
- Allied Health / Technical Ed. – Somerset @ Laurel Campus
Postsecondary education capital investments

WKU: Academic/Athletic Complex renovation; Materials Characterization Center; Science campus renovation
KSU: Hathaway Hall renovation
NKU: Student union and Science building renovations
Murray: New student housing project
EKU: New student housing project; Dairy research facility
Morehead: Center for Health, Education and Research
System-wide: capital renewal pool
Capital projects

- Preserving traditional 6% debt capacity policy
- Heavily invested in education – 64%
- Investments in infrastructure and technology
- Detailed analysis performed showed $39m in reduced construction costs on new projects through repeal of prevailing wage law
- Savings permits additional construction within existing bond capacity
% construction cost savings for listed projects

A  Data Center Readiness
B  Renovate Lonnie Watson Building-Ky Correctional Inst for Women
C  Capital Renewal & Maintenance Pool
D  New Student Housing
E  EKU-UK Dairy Research Project (Meadowbrook Farm)
F  Renovate Ky State Office Building
G  New Indoor Arena
H  Emerging Technology Center, West Ky Community & Technical College
I  Advanced Manufacturing Technology Facility-Gateway Community & Tech. College
J  Allied Health/Technology Education Building-Laurel Campus of Somerset CC
K  Replace Pavilion Roof
L  Renovate Hathaway Hall Phase III
M  Oakwood Mental Retardation Facility-Replace Chillers, Heating & Cooling Lines
N  New Residential College, Murray State University
O  Renovate Old Science Building
P  Patient Care Facility Phase II - Hospital
Q  Biological/Pharmaceutical Complex - Phase II
R  Health Sciences Center Research Facility-Phase IV
S  Renovate Academic/Athletic #2 Complex
T  Renovate Science Campus Phase III
U  Construct Materials Characterization/ICSET Phase II
Economic development initiatives

- Small and minority business development - $.6m
- New economy capital investments - $20m
- Economic development bond pool - $10m
- Wildlife Elk Interpretive Center - $3m
- Downtown Louisville arena - $75m
- Opening of China office - $.2m
- New economy initiatives - $20m
- Parks renovations - $8m
Funding for business programs

- Large investment in new economy initiatives
- ICARE: Insurance Coverage Affordability and Relief to Employers
  - $20m pilot program
  - Provides monthly subsidies to small employers with less than 25 employees
  - Provides access to the previously uninsured and those with high cost conditions
- AMC tax relief for small businesses
Developing our economy

- Expanding global connections
- Showcasing Kentucky worldwide
- New economy investments
- Tax relief for small businesses
AMC Objectives

- Fairness to Ky-only companies by ensuring payments by multi-state nonresident companies
- Increase stability of revenue stream
- Offset repealed taxes and rate reductions
- Fairness to profitable companies

Incidence of taxation is highly concentrated
AMC tax relief for small businesses

- No business with gross receipts of $2 million or less will pay AMC on its gross receipts.
- Businesses with gross receipts between $2 million and $10 million will get a proportionate credit against AMC calculation on gross receipts.
- Retains the stabilizing effect of AMC while reducing tax burden on small business.
- Friendly to start-up businesses that are not yet profitable but have gross receipts under $10 million.
- All companies will still pay the greater of the income factor, the AMC, or the minimum tax of $175.
AMC tax relief for small businesses

- 60,000 businesses (mostly LLE’s) will pay no AMC
- An additional 10,000 businesses (with gross receipts between $2 million and $10 million) will receive reduction of AMC obligation
- Fiscal impact:
  - FY07: $3.2 million
  - FY08: $9.7 million
Depiction of AMC relief for small business

$2 million  $10 million
A responsible budget: fulfilling commitments

- Medicaid
- State health insurance
- Employee salary increment
- Pension plan funding
- Justice Cabinet initiatives
- Transportation programs
FY06 Medicaid shortfall

- Decreased leveraging opportunities as a result of federal policy / rule changes
- Increasing expenditures
- Actions to balance
- Current year appropriation of $85m
Change in Direction: KyHealth Choices

- 1115 Waiver request
- Stretch resources to most appropriately meet the needs of recipients
- Encourage Medicaid members to be personally responsible for their own healthcare
- Expect to begin phase-in January 2006
- Additional funding over biennium of $258.5m
Other Health and Families Services priorities

Community Based Services - $29.4m
Mental Health / Mental Retardation - $30.7m
Workers’ Information System (TWIST) - $6.2m
Aging Services - $1.5m
Governor’s Council on Wellness and Physical Activity - $2.5m
Public employee health insurance

- Maintains current program in 2007 with minor adjustments
- Ability to maintain due to savings from self-insurance state-wide
- Many Blue Ribbon Committee recommendations incorporated
- 9% increase in costs in FY 07
- Another 9% increase in costs in FY 08
State salary and compensation policy

✓ Graduated scale beginning at $1000 per year at lower salaries
✓ Reduced to $200 per year for employees over $60,000 per year
✓ Intended to reduce turnover among lower paid employees and to provide funds to address health needs
KY Pension Funding Levels are Close to National Averages (not including medical funds)

<table>
<thead>
<tr>
<th></th>
<th>FY 01</th>
<th>FY 02</th>
<th>FY 03</th>
<th>FY 04</th>
</tr>
</thead>
<tbody>
<tr>
<td>KERS (non-hazardous)</td>
<td>125.7%</td>
<td>110.4%</td>
<td>97.4%</td>
<td>85.1%</td>
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<tr>
<td>KTRS</td>
<td>90.8%</td>
<td>86.6%</td>
<td>83.5%</td>
<td>80.9%</td>
</tr>
<tr>
<td>National Average</td>
<td>100.8%</td>
<td>96.2%</td>
<td>91.2%</td>
<td>87.8%</td>
</tr>
</tbody>
</table>

Source: KERS and KTRS annual reports and NASRA September 2005 Report
Pensions

✓ Took a while to get here; will take a while to get out
✓ Our situation is not unlike other states
✓ Governor wants to make a good faith effort to address the problem; undertake a professional study of long term solutions
✓ Benefits to state employees are guaranteed under the inviolable contract doctrine
✓ KRS employer contribution for non-hazardous service is increased 24% in FY07 and 11% in FY08
✓ KTRS funding will permit continuation of health benefits to retirees
Transportation

GARVEE bonds for federal highway projects - $290m
Economic Development Highway bonds - $75m for local road aid projects
State Resurfacing program - $33m
Minority Scholarship program - $.4m
Justice, Public Safety and Drug Control

Department for Public Advocacy - $6.2m for decreasing caseloads and a pilot program with social workers

Kentucky State Police - $8.5m for overtime payments; additional funding for overtime results in the equivalent of 50 new troopers
K e n t u c k y P r i s o n P o p u l a t i o n
1 9 9 5 - 2 0 1 5

F i s c a l Y e a r E n d i n g
## Justice, Public Safety and Drug Control

### Department of Corrections
- $4.3m for additional parole and probation officers
- $15m for increased inmate medical costs
- $2m for additional beds at Otter Creek
- $16.7m for additional local jail payments
- $2m to expand home incarceration program
- $6.6m for additional half-way house beds
- $1.2m for new beds at Recovery Kentucky drug and substance abuse treatment centers
- $4m for regional drug courts in coal counties
- $2m for drug and substance abuse treatment in local jails
Payments by Kentucky smokers are subsidizing other states.

Time has come for a Kentucky assessment directly on tobacco manufacturers.

Manufacturer’s assessment would bring in additional $150 million each year.

Funds would be used for higher education, small business tax relief and strengthening pension programs.