MINUTES OF THE
EXECUTIVE APPROPRIATIONS COMMITTEE
Tuesday, December 13, 2011 - 2:00 p.m. - Room 445 State Capitol

Members Present:
Sen. Lyle W. Hillyard, Co-Chair
Rep. Melvin R. Brown, Co-Chair
Sen. Kevin T. Van Tassell, Vice Chair
Rep. John Dougall, Vice Chair
Sen. Scott K. Jenkins
Sen. Patricia W. Jones
Sen. Peter C. Knudson
Sen. Benjamin M. McAdams
Sen. Karen W. Morgan
Sen. Wayne L. Niederhauser
Sen. Ross I. Romero
President Michael G. Waddoups
Rep. Brad L. Dee
Rep. Gregory H. Hughes
Rep. David Litvack
Speaker Rebecca D. Lockhart
Rep. Ronda Rudd Menlove
Rep. Jennifer M. Seelig
Rep. Christine F. Watkins

Members Excused:
Rep. Brian S. King

Staff Present:
Jonathan Ball, Legislative Fiscal Analyst
Steven Allred, Deputy Director
Greta Rodebush, Legislative Secretary

Note: A copy of related materials and an audio recording of the meeting can be found at www.le.utah.gov.

1. Call to Order/Approval of Minutes

Co-Chair Hillyard called the meeting to order at 2:38 p.m.

MOTION: Rep. Brown moved to approve the minutes of November 15, 2011. The motion passed unanimously with Sen. Van Tassell and Rep. Menlove absent for the vote.

2. Report of State Agency Federal Funds Receipts and Plans

John Reidhead, Director, Division of Finance, presented "Federal Receipts Reporting." Marcie Handy, Assistant Comptroller, Division of Finance, provided assistance.

Mr. Reidhead stated that the 240-page document fulfills requirements set forth in House Bill 138, "Federal Receipts Reporting Requirements," 2011 General Session. The report contains schedules of federal receipts reporting for state agencies, institutions of higher education, and local education agencies for the fiscal year ending June 30, 2011. The report also includes state agency plans to operate their agency in the event federal receipts are reduced by 5 percent and 25 percent.

Mr. Reidhead stated that for practical purposes, the division asked state agencies to report on programs $1 million and greater. In addition, the division did not ask for plans on ARRA programs because they would be ending in FY 2012.

Co-Chair Hillyard commented that Utah is not as dependent on federal money as other states.

Sen. Niederhauser asked clarifying questions pertaining to the schedule of federal receipts reporting for state agencies and the plans of potential 5 percent and 25 percent federal receipts reductions.

Mr. Reidhead explained that H..B. 138 designates which state agencies are required to report on federal receipts. He noted that the bill lists three agencies that did not receive any federal money, the departments of Alcoholic Beverage Control, Financial Institutions, and Human Resource Management. For a detailed listing of every grant within the state's reporting entity, Mr. Reidhead referred the Committee to the State Auditor's Fiscal Year 2011 Single Audit Report.

Sen. Morgan asked why the appropriated federal funds for transportation and public education were less than the federal funds receipts. Mr. Reidhead explained that most federal grants are based on the expenditure already occurring before the money is drawn from the federal government. By definition, then, receipts equal actual expenditure.

Co-Chair Hillyard commented that the division's report is sobering and yet helpful.

3. Revenue Volatility Report

Dr. Thomas Young, Economist, Office of the Legislative Fiscal Analyst (LFA), and David Stringfellow, Budget Analyst, Governor's Office of Planning and Budget (GOPB), presented the "Joint Revenue Volatility Report" along with two independent analyses, "Revenue Volatility Report - LFA View" and "Joint Revenue Volatility Report - The Governor's Office of Planning and Budget."

The Joint Revenue Volatility Report addresses the following topics: 1) the volatility tax bases and tax revenue streams that fund the state budget; 2) the balances in the General Fund Budget Reserve Account (GFBRA) and the Education Fund Budget Reserve Account (EFBRA); 3) the adequacy of the balances in these rainy day funds relative to the volatility of the revenue streams.

Dr. Young discussed the automatic transfer of revenue surpluses to the budget reserve accounts. In 2008, policymakers set the automatic transfer threshold for the General Fund at 6 percent and for the Education Fund at 8 percent. Since 2008, General and Education Fund revenue volatility and associated forecast error has increased. Dr. Young indicated that the current caps would cover about 75 percent of any potential forecast error. To cover updated error rates for 18 month revenue estimates, transfer caps would need to be 8 percent for the General Fund and 9 percent for the Education Fund.

Dr. Young discussed the volatility of the tax bases and revenue streams for the General Fund and Education Fund in greater detail. When comparing the volatility of the two funds, the Education Fund is more volatile by between 20 percent and 60 percent. This may be generally due to the fact that individuals' and corporations' income is less stable than individuals' and businesses' spending patterns.

Dr. Young stated the GFBRA balance is 5.9 percent of FY 2011 appropriations. If FY 2012 revenue comes in above target, the amount that could be transferred from the General Fund to the GFBRA is $317,100. The EFBRA balance is 4.2 percent of FY 2011 appropriations. Likewise, if FY 2012 revenue comes in above target, the amount that could be transferred to the EFBRA is $82.2 million. The current combined balance in the Rainy Day Fund is $232.5 million.

Mr. Stringfellow stated that LFA and GOPB's conclusions are broadly similar. He said that revenues are volatile because the economy is volatile. Forecasting volatility and forecasting revenue is difficult largely due to economic movements. However, in a small measure, volatility is also associated with tax structure and tax system changes.

Mr. Stringfellow's report findings indicate that if the purpose of the rainy day funds is to cover losses from revenue forecast errors for the current budget, then the existing reserve caps for the General Fund and the Education Fund are more than adequate. If the intent of the rainy day funds is to reduce the severity of budget cuts over multiple years, then the optimal reserve size depends on the extent to which policymakers want to insulate spending priorities from economic downturns.

Mr. Stringfellow listed other mechanisms that could dampen revenue volatility, such as, cutting or delaying expenditures, changing bonding positions or debt levels, or using other reserve funds.

Dr. Young and Mr. Stringfellow responded to committee member questions regarding possible changes in the tax laws to correct revenue volatility, forecast adjustments and budget adjustments when economic conditions change, rainy day funds from a multi year perspective, adequacy of the transfer caps, the impact of recent tax rate cuts on volatility, and how broadening the tax base impacts overall revenue volatility.

Sen. Jones asked for a summary of the options for mitigating revenue volatility. Mr. Stringfellow outlined the following options: 1) design a robust system of taxation; 2) forecast revenue more conservatively; 3) save excess funds in the rainy day funds; 4) shift when you spend money or when you collect revenue; 5) restructure or expand debt; 6) provide different levels of public goods and services; 7) raise or lower taxes; 8) transfer volatility to other units of government.

Mr. Ball suggested using a five-year rolling average for corporate income tax as another way of managing volatility.

4. Revenue Estimates

Dr. Andrea Wilko, Chief Economist, LFA, presented "Revenue Estimates - November 2011."

Dr.Wilko explained that the adopted consensus revenue estimates set the baseline for beginning budget deliberations. She stated that the final revenue estimates will be available in February.

Dr. Wilko reported that the state ended FY 2011 with a surplus of about $60.2 million. Revised revenue estimates for FY 2012 show a surplus of $68 million, which brings the total of available one-time money to $128 million. Dr. Wilko also stated that forecast revenues for FY 2013 grew by $275 million. She noted that a reduction in the required set-aside for Economic Development Tax Increment Financing from $7.2 million in FY 2012 to $3.1 million in FY 2013 will effectively add $4.1 million to available ongoing General Fund revenue. This brings the total to about $280 million.

Co-Chair Hillyard asked why the Mineral Lease Fund is down. Dr. Wilko stated that the Mineral Lease Fund has been growing exponentially for about eight years. However, based on collection patterns she expects those funds to start coming down to historical levels.

MOTION: Rep. Brown moved to adopt the revised revenue estimates for Fiscal Year 2012 and the revenue estimates for Fiscal Year 2013 as indicated on page 1of the sheet entitled, "Revenue Estimates - November 2011" and dated today, December 13, 2011. The motion passed unanimously with President Waddoups and Sen. Van Tassell absent for the vote.

5. Appropriations Limit Estimates

Angela Oh, Economist, LFA, presented the "Appropriations Limit" dated December 13, 2011.

Ms. Oh explained that the Legislature adopted the *State Appropriations and Tax Limitation Act* in 1989 to limit state government spending. The Act restricts non-exempt General Fund and non-exempt Education Fund appropriations to a formula amount that is determined on a per-person basis. The appropriations limit changes as a certain measure of inflation and population estimates change.

Ms. Oh reported that the base budget non-exempt appropriations are well below the appropriations limit. The estimated appropriations limit is approximately $3 billion for FY 2012 and $3.2 billion for FY 2013. She stated that when those numbers are offset against current non-exempt appropriations, the difference or "Cap Gap," is approximately $800 million for FY 2012 and $1 billion for FY 2013.

Ms. Oh noted that these numbers are only estimates and will be finalized in February once the Bureau of Economic Analysis publishes inflation and population numbers.

Co-Chair Hillyard asked if the appropriations limit would change much with those final inflation and population numbers. Ms. Oh stated that those numbers would not change significantly.

MOTION: Rep. Brown moved to adopt the Fiscal Year 2012 and 2013 appropriations limit estimates as indicated on the sheet entitled, "Appropriations Limit - December 13, 2011." The motion passed unanimously with President Waddoups and Sen. Van Tassell absent for the vote.

6. Subcommittee Allocations

Jonathan Ball, Director, LFA, presented the "Memo Re: Subcommittee Allocations" behind Tab 6.

Mr. Ball explained that Joint Rule 3-2-402 requires the Executive Appropriations Committee to meet in December to approve an appropriate amount (allocation) for each subcommittee to use in preparing its budget. Under that same rule, EAC can set aside a certain amount for various other purposes.

Based on requirements set forth in H.J.R. 45, "Joint Rules Amendments for Establishing Base Budgets," 2011 General Session, LFA calculated subcommittee allocations for FY 2013 at the same level as FY 2012. The calculations are attached to the memorandum and listed as "Subcommittee Allocations (General and Education Funds)." Mr. Ball stated that these initial allocations are subject to legislative action.

Mr. Ball pointed out that if the Committee chooses to allocate the ongoing base budget to the subcommittees, inherent in that amount is $52 million to cover the structural imbalance from FY 2012.

MOTION: Rep. Brown moved to allocate to appropriations subcommittees for Fiscal Year 2013 the General Fund and Education Fund totals listed on the sheet entitled, "Subcommittee Allocations (General and Education Funds)" and dated today, December 13, 2011.

Co-Chair Hillyard clarified that this motion gives each of the subcommittees the same amount of money they had with last year's budget. Because $52 million of last year's budget was one-time money, the motion replaces the $52 million with ongoing revenue.

Rep. Litvack asked if the $52 million has been allocated per subcommittee. Mr. Ball explained that the structural imbalance is a mathematic function and not an appropriation or allocation. The first $52 million in growth in revenue goes to cover the shortfall in ongoing revenue.

SUBSTITUTE MOTION: Sen. Morgan moved the entire previous motion plus an additional $41 million for enrollment growth to the public education base budget.

Sen. Jenkins asked for a clarification on the $41 million.

Mr. Ball clarified that the $41 million represents the consensus enrollment growth cost estimate between the Governor's Office, LFA, and the Utah State Office of Education. The $41 million includes $17.6 million for increased Weighted Pupil Units (WPUs) in the Basic School Program, $11.9 million in the Voted & Board Leeway growth, $10.6 million in increased Charter School Local Replacement costs, and $514,000 in Charter School Administrative Costs. Mr. Ball indicated that the $41 million does not include cost increases to the Educator Salary Adjustments.

Rep. Dougall asked if the substitute motion includes a cut to eliminate the double funding of students.

Sen. Morgan stated that her motion does not include an adjustment for double funding, which she believes is a separate issue. Sen. Morgan stated that the base budget needs to include the 12,500 new students that are enrolling in the fall of 2012.

Rep. Dougall asked for more information on the double funding of students.

Rep. Dee said that while he supports new student growth in education, he does not want to usurp the appropriations process of the subcommittees.

Sen. Niederhauser stated that building a larger base budget circumvents what legislators are elected to do, and that is, digging into the budgets.

Sen McAdams stated that it is philosophically appropriate to include this motion at this time. Student growth is part of the prior year's base budget. Passing the motion sends a message to the appropriations subcommittees that education funding is a priority to the EAC.

Rep. Litvack stated that while he respects the subcommittee process, he felt that the EAC should set the tone by making growth in education one of its top budget priorities.

Rep. Menlove stated that earmarking those funds circumvents the process that allows the public to voice their concerns and legislators to do their work as budget managers.

Sen. Romero spoke in support of the substitute motion. He stated that there is a cost associated with educating students and since there is a consensus number on what those costs will be, he did not think it would be useful to wait for a committee hearing.

Sen. Jones asked if the subcommittees would be able to vet some of the appropriations if the motion passed. She also asked if the public would still have an opportunity to express their desires in the subcommittees as well. Mr. Ball explained that this is an iterative process and that there will be many opportunities to change the budget.

President Waddoups encouraged the Committee to defeat the substitute motion because he felt that the subcommittees need to do their work in preparing a well-thought out budget.

Rep. Seelig spoke in support of the substitute motion and pointed out that including enrollment growth in the base budget has been a part of normal operating procedure prior to the recession.

Co-Chair Hillyard commented that while he supports funding the growth in education he also supports an increase in the WPU which affects all of the school districts.

Sen. Brown restated his position on the original motion. He felt that the legislative process should begin with the subcommittees and that it was premature to do it any other way.

Sen. Morgan summed that she didn't think it was premature to include the $41 million in the base budget. She stated that historically, enrollment growth has always been included in the base budget. Sen. Morgan clarified that the consensus enrollment growth cost is $40,624,100. This brings the total public education budget to $2,447,130,400.

The Committee voted on the substitute motion. The motion failed with Sen. Jones, Sen. McAdams, Sen. Morgan, Sen. Romero, Rep. Litvack, Rep. Seelig, and Rep. Watkins voting in favor of the motion.

A vote was taken on the original motion. The motion passed unanimously with Sen. Van Tassell absent for the vote.

7. Fiscal Year 2013 Base Budget Bills

Mr. Ball explained that the next motion directs legislative staff to prepare a base budget bill or bills to be introduced on the first day of the 2012 General Session.

MOTION: Rep. Brown moved to authorize legislative staff to prepare and number base budget bills for state agencies, higher education, and the Minimum School Program, as Executive Appropriations Committee bills to be introduced on the first day of the 2012 General Session. Staff shall include in these bills:

1. Ongoing General, Education and Uniform School Fund appropriations defined in the current year's appropriations acts;

2. Restricted fund reductions included in agency budget requests; and

3. Adjustments to dedicated credits, nonlapsing balances, and federal funds included in agency budget requests as allowed under the Budgetary Procedures Act.

In consultation with the Co-Chairs of the Executive Appropriations Committee, the Legislative Fiscal Analyst may make any technical changes necessary.

Speaker Lockhart asked if staff was going to prepare one base budget bill or separate base budget bills. She also asked about bill sponsorship. Mr. Ball indicated that staff was going to prepare a single bill that most likely would be sponsored by Sen. Hillyard, plus nine separate bills, one for each subcommittee. The sponsors would be the subcommittee co-chairs who did not sponsor last year's bills.

A vote was taken on the motion. The motion passed unanimously with Sen. Van Tassell absent for the vote.

8. Other Business (Agenda Item 9)

Co-Chair Hillyard called attention to the eight reports behind Tab 9. He asked committee members to read the reports and contact staff with questions. If committee members would like a report added to an EAC agenda, they were to contact the EAC chairs.

The reports included: 1) Federal grants approved by the Governor; 2) Elected Official and Judicial Compensation Commission Update; 3) Legislative Compensation Commission Report; 4) S-Corporation Taxation Report; 5) Cigarette Tax Restricted Account Issue Brief; 6) Tobacco Settlement Restricted Account Issue Brief; 7) Medicaid Inspector General Annual Report; 8) State Dept Update.

9. LFA In-depth Review: Public Education (Agenda Item 8)

Ben Leishman, Fiscal Analyst, LFA, and Dr. Thomas Young, Economist, LFA, presented the in-depth budget review, "Minimum School Program & The Utah State Office of Education."

Mr. Leishman thanked the LFA team of analysts for their contribution to the report and the Utah State Office of Education (USOE), which provided needed and requested information.

Mr. Leishman referenced the summaries and findings in the budget reviews, "The Minimum School Program & the Utah State Office of Education" and "Minimum School Program: Highlights."

The in-depth budget review is divided into six parts: Part 1 is a general structural overview of the public education system; Parts 2-5 provide the research, observations, and recommendations related to study questions on the Minimum School Program; Part 6 details an in-depth review of the Utah State Office of Education.

Mr. Leishman's presentation highlighted several areas for improvement along with the following recommendations: The Analyst recommends that the Legislature: 1) reinstate an independent review of USOE's application of statutory distribution formulas and allocations to school districts and charter schools; 2) implement a statewide financial management database for school districts and charter schools to report financial data; 3) develop program-level performance measures for each semi-restricted and restricted program.

Dr. Young reviewed four recommendations pertaining to the Utah State Office of Education. The full list of recommendations are listed in Part 6 of the report. The Analyst recommends the following:

- The Legislature work with USOE to align line items and appropriation units to match the current USOE organizational structure;

- The Legislature consider whether to allow a state entity to maintain an open Other Post Employment Benefit (OPEB) plan that allows individuals to accumulate health insurance benefits at retirement;

- The Utah State Board of Education work with the Analyst in developing job specific outcome based performance measures and report these measures by November 2012;

- The USOE work with the Analyst to perform cost-benefit analysis regarding program outputs for most of its programs.

MOTION: Rep. Brown moved to refer the Minimum School Program and the State Office of Education in-depth study to the Public Education Appropriations Subcommittee. The motion passed unanimously with Sen. Van Tassell and Rep. Hughes absent for the vote.

Co-Chair Hillyard suggested that the USOE meet with LFA staff to discuss the logistics of the report's recommendations and report to the co-chairs of the public education appropriations subcommittee.

MOTION: Rep. Brown moved to adjourn. The motion passed unanimously with Sen. Van Tassell and Rep. Hughes absent for the vote.

Co-Chair Hillyard adjourned the meeting at 4:13 p.m.