

## BUDGET OUTLOOK ASSUMES 2019 LEGISLATURE WILL SWEEP TRUST FUNDS TO AVOID A SHORTFALL

Florida’s state forecasters estimate that the 2019 Legislature will have a \$223.4 million budget surplus when it puts together the state’s new spending plan for FY 2019-20. However, this assumes the Legislature will transfer nearly \$400 million from trust funds—money earmarked by law for specific uses—into the General Revenue (GR) Fund. Without the trust fund sweeps, an estimated shortfall of \$78.9 million exists, climbing to \$169.1 million if the Legislature passes tax cuts.<sup>1</sup>

This information is contained in the new *Long-Range Financial Outlook*, recently adopted by the Joint Legislative Budget Commission. This constitutionally required annual report compares estimated revenues and expenditures to give the Legislature a sense of the state’s budget position going into session and whether lawmakers can expect a budget shortfall or surplus (for more description of the *Outlook*, see Appendix).

The *Outlook* further estimates the state will be facing shortfalls of \$47.8 million in FY 2020-21 and \$456.7 million in FY 2021-22, even with trust fund sweeps. This is due to the continuing “structural imbalance,” where the growth of the state’s recurring expenditures exceeds the growth of recurring revenues.

The *Outlook* recommends the Legislature adopt a “fiscal strategy” to address the imbalance and clear the shortfall in FY 2021-22. There are many ways to get there, but in the simplest terms, it would take a reduction in recurring expenditures of \$199 million to eliminate the future shortfall.

### Largest FY2019-20 General Revenue Spending Increases Included in the Outlook

\$ in millions

State Employees - Pay issues, health insurance, and retirement benefits	\$202.6
Medicaid - Caseloads, less federal and state TF funding, increased waivers and provider payments	\$188.4
Universities - Workload increases and restoring non-recurring funding	\$171.2
State match for Federal Emergency Management Disaster Funding	\$152.2
Water and Land Conservation	\$121.2
Education Fixed Capital Outlay	\$118.0
State Buildings - Repair, maintenance, and capital Improvements	\$104.1
Corrections - Inmate Health Services	\$100.2
PreK-12 Education - Enrollment growth and a 1.16% per-student funding increase	\$76.9
Job Growth Grant Fund	\$65.0
Local Water Projects	\$56.1
Kidcare - Enrollment growth and reduced federal funding (FMAP)	\$50.3

<sup>1</sup> The \$223 million estimated surplus also assumes \$90.2 million in tax cuts, the average size of the cuts the Legislature has passed over the last three years.

## HIGHLIGHTS

- State economists estimate that there will be insufficient General Revenue (GR) available to the 2019 Legislature to fund the base budget plus “critical needs” and “high priority needs”—basically a continuation budget. There is a shortfall of \$78.9 million without the Legislature making revenue adjustments.
- However, the *Outlook* assumes the Legislature will sweep \$392.5 from trust funds each year to accumulate sufficient GR. It also assumes there will be tax cuts of \$90.2 million<sup>2</sup> in each of the three years. When these revenue adjustments are included, the \$78.9 million shortfall becomes a \$223.4 surplus in FY2019-20.
- These two items have a combined positive effect of \$302.3 million on the next budget, but because about half of the tax cuts are assumed to be recurring and trust fund sweeps provide non-recurring revenue, the combination results in a \$92.7 million increase in the estimated deficit in FY2021-22.
- A budget shortfall is forecast in each of the following two years, totaling \$47.8 million and \$456.7 million, respectively.
- “Critical needs” will only require a net additional \$35.5 million over the recurring GR base budget in FY 2019-20 but “high priority needs” will require an additional \$1.83 billion.
- The “critical needs” estimate is so low because it assumes the Required Local Effort (RLE) school property tax millage rate will not change, which would produce an additional \$480.0 million from rising property values, reducing the need for state revenue. However, the “high priority needs” estimate assumes the Legislature will adopt a rolled-back millage rate, as it did last year, which allows school property taxes to grow by the value of new construction only. This would result in \$289.2 million less in local school property taxes and require \$536.1 million in additional state money to fund increased enrollment and a 1.16 percent increase in per student funding.
- The *Outlook* assumes a GR reserve (unobligated cash) of only \$1.0 billion. The Legislature has left a larger reserve than that in each of the last eight years, ranging as high as \$1.6 billion. Any reserve larger than \$1.0 billion would reduce the surplus.
- It will take a net reduction in recurring expenditures (budget cuts minus new initiatives) of \$199.0 million to erase the projected shortfall in FY2021-22.

## BUDGET OUTLOOK IS IMPROVED FROM LAST YEAR

Last year’s *Outlook* estimated a \$1.1 billion budget shortfall for FY 2019-20. The new estimate of a \$223.4 million shortfall is evidence that there are some positive revenue and expenditures developments in FY 2018-19. In addition, last year’s estimate of a \$1.6 billion shortfall for FY 2020-21 was reduced to a \$456.7 million shortfall in this year’s *Outlook*. The 2018 Legislature deserves credit for reducing recurring expenditures. Lawmakers appropriated \$800 million less in GR than was forecast, including \$300 million less in recurring revenues. The base GR budget before the 2019 Legislature is now \$266 million less than anticipated. But the Legislature also swept more from trust funds and enacted fewer tax cuts than assumed in the *Outlook*, both improving the forecast by increasing available revenue.

<sup>2</sup> This is the first-year impact of the tax cuts. The annualized amount is \$148.7 million but it is assumed the effective dates of some of the cuts will be delayed until later in the fiscal year, reducing the first-year impact.

The biggest appropriation change was the Legislature’s decision to allow Required Local Effort (RLE) school property taxes to grow by the value of new construction. Last year’s *Outlook* assumed it would not increase the dollar amount of RLE, as it had done the two prior sessions. While this reduced the state revenue needed to fund the increase in per-student spending, it did cost local property taxpayers \$107 million.

**Budget Outlook - FY 2019-20 through FY 2021-22**

General Revenue - \$ in millions

<b>Revenues</b>	<b>FY18-19</b>	<b>FY19-20</b>	<b>FY20-21</b>
Unspent GR from Prior Year	\$1,224.3	\$1,223.4	\$1,000.0
Estimated Revenues	\$3,334.7	\$34,544.2	\$35,827.4
BP Settlement	\$26.7	\$26.7	\$26.7
Non-Op Funds and Transfers	\$99.3	\$99.3	\$99.2
<i>Total GR Available for Appropriation</i>	<i>\$34,685.0</i>	<i>\$35,893.6</i>	<i>\$36,953.3</i>
<b>Expenditures</b>			
Base Budget	\$31,809.4	\$32,786.3	\$34,229.1
Increase - Critical Needs	\$35.5	\$609.9	\$283.3
Increase - High Priority Needs	\$1,829.7	\$1,701.5	\$1,630.9
Transfer - Budget Stabilization Fund	\$89.3	\$41.2	\$54.6
Transfer - Lawton Chiles Endowment			\$304.7
<b>Total Estimated Expenditures</b>	<b>\$33,763.9</b>	<b>\$35,138.9</b>	<b>\$36,502.7</b>
Cash Reserves	\$1,000.0	\$1,000.0	\$1,000.0
<b>Surplus/(Shortfall)</b>	<b>(\$78.9)</b>	<b>(\$245.3)</b>	<b>(\$549.4)</b>
Tax Cuts (see note)	(\$90.2)	(\$195.0)	(\$299.8)
Trust Fund Sweeps	\$392.5	\$392.5	\$392.5
<b>Surplus/(Shortfall)</b>	<b>\$223.4</b>	<b>(\$47.8)</b>	<b>(\$456.7)</b>
<i>Note: Assumes the same amount of tax cuts are adopted each year (\$148.7 million annualized, \$90.2 million in first year). The annualization and recurring portion of the cuts compounds the amount in subsequent years. Source: Florida TaxWatch from data in the 2018 Long Range Financial Outlook</i>			

## REVENUE ADJUSTMENTS

### Should Trust Funds Sweeps Be Considered Standard Operating Procedure?

In 2015, the *Outlook* began assuming that the Legislature will cut taxes (reducing GR) and sweep trust funds<sup>3</sup> (increasing GR). Before 2015, the size of any estimated surplus was used by some as a gauge of the likelihood that there would be tax reductions. Now, tax cuts are built in. This year, it is assumed the Legislature will enact \$90.2 million<sup>4</sup> in net tax and fee reductions that reduce GR in each of the three years. This is the average of the last three years' worth of tax relief. This includes \$46.3 million in recurring cuts (such as permanent tax rate decreases or new exemptions) and \$43.9 million of non-recurring cuts (one-time reductions such as sales tax holidays.)

In the short-term, this reduction is more than offset by the inclusion of trust fund sweeps, which are estimated at \$392.5 million each year. Including these two revenue adjustments results in a positive impact on available GR for next year of \$302.3 million; however, over the next years of the *Outlook's* forecast horizon, the net impact of the tax cuts increases significantly. The recurring portion of the tax cuts compounds each year, while trust fund sweeps are non-recurring, resulting in a net reduction from tax cuts and trust fund sweeps of \$92.7 million in FY2021-22, pushing the estimated shortfall to \$456.7 million.

Trust funds are created by law, specifying the revenue source and dedicating that revenue for specific uses. By contrast, General Revenue can be spent on virtually anything. Trust fund sweeps have become a significant source of GR, used by legislators not only to address shortfalls, but also to fund new initiatives and tax cuts. The Legislature swept \$404 million last year, and sweeps have exceeded half a billion dollars in five of the last ten years.<sup>5</sup>

Trust fund transfers have their place in budgeting, especially in times of a shortfall, when education and human services (which comprise the majority of general revenue spending) typically bear the brunt of budget cuts. Transferring funds from trust funds to general revenue can help share the pain. However, care should be taken that the lawfully-created relationship between trust fund revenues and their uses is considered and the impact of the sweeps should be quantified and evaluated. The authority for trust fund transfers is placed in the General Appropriations Act and can change significantly in the budget conference process, often without a thorough vetting.

If a trust fund continually carries a significant unobligated balance, the amount of the tax or fee that funds it should be reconsidered, it may be too high. This is especially true if there is a direct relationship between the revenue source and the specified use of funds. For example, if a taxpayer pays a fee to fund regulation of an activity they undertake or to pay for a service or benefit they receive, it would be unfair—a violation of a social contract—to use that money for other purposes.

3 The Legislature often transfers money from trust funds, which has specified uses, to GR, which may be used for anything. For more information see Florida TaxWatch, Putting the Trust Back in Trust Funds, March 2014.

4 This is the first year impact of the tax cut. Because recurring tax cuts usually have delayed effective dates, the first year impact is less than the annualized amount. The annualized amount (plus the non-recurring cuts) is \$230.6 million.

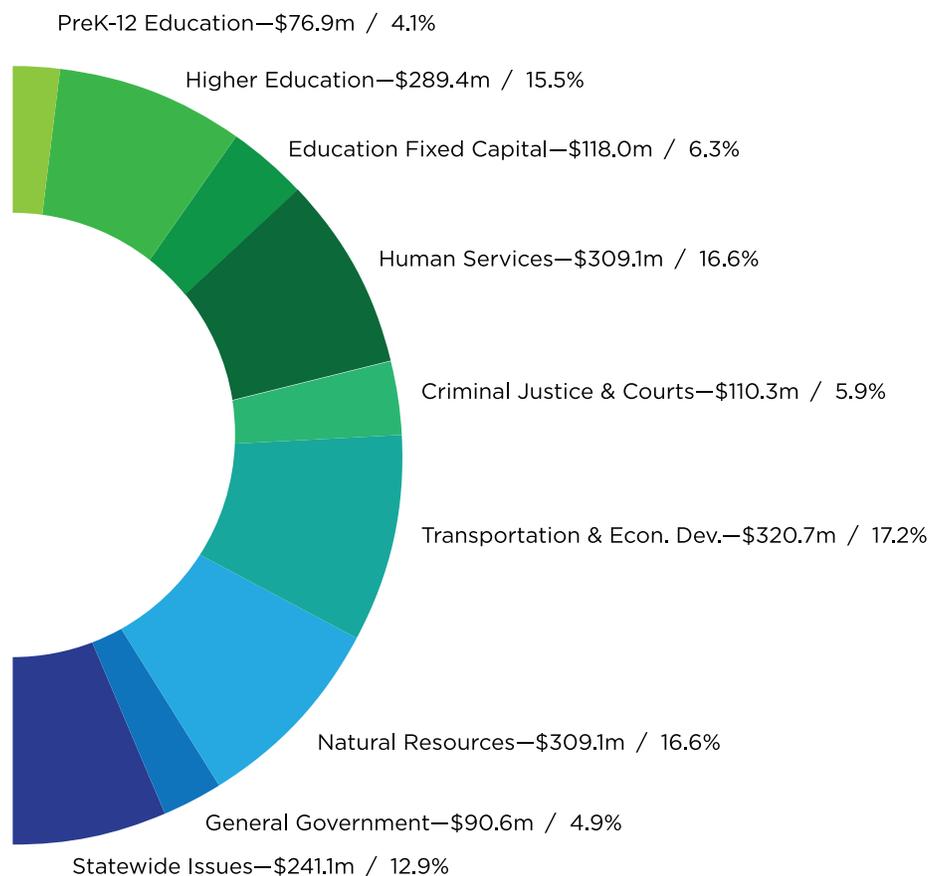
5 The Governor vetoed \$12.5 million of the sweeps last year and governors have vetoed \$382 million over the previous ten years.

In addition, there is a question as to whether some of these trust funds have “unnecessary” revenue in them. It is widely thought that Florida has a significant unmet need in affordable housing, yet the Sadowski funds have been by far the biggest source of sweeps, including providing almost half (\$182 million) of last year’s total. In fact, over the previous 10 years, the Legislature has swept \$1.5 billion from the State Housing and Local Government Housing trust funds, more than the \$1.1 billion appropriated from the funds for affordable housing.

The second largest sweep was \$54.8 million from the Inland Protection Trust Fund (IPTF). The IPTF is funded by a tax levied on those licensed to produce or import motor fuel, diesel fuel, aviation fuel, or other pollutants. Funds are dedicated to cleanup leaking underground petroleum tanks, a very important environmental and public safety issue. The state has been closing approximately 400 sites per year. However, there is a backlog 3,000 sites awaiting remediation and another 6,500 that are not yet finished.<sup>6</sup> Furthermore, the tax rate is based on the balance in the IPTF—the higher the balance the lower the tax. Sweeping the fund puts upward pressure on the tax rate.

### Critical and High Priority Needs by Program Area

\$ in millions



\* Includes state employee salary and benefit increases, capital improvements, statewide technology issues, etc.  
 Source: Florida TaxWatch from data in the 2018 Long Range Financial Outlook

6 Tampa Bay Times, “Florida should spend more to clean up leaking tanks,” January 11, 2018.

## WHAT ARE THE \$1.865 BILLION IN ESTIMATED INCREASED NEEDS FOR FY 2019-20?

“Critical needs” will only require an additional \$35.5 million over the recurring GR base budget in FY 2019-20, but “high priority needs” will require an additional \$1.83 billion. The “critical needs” estimate is so low because it assumes the Required Local Effort (RLE) school property tax millage rate will not change, which would produce an additional \$480.0 million from rising property values, reducing the need for state funds. However, the “high priority needs” estimate assumes the Legislature will adopt a rolled-back millage rate, as it did last year, which allows school property taxes to grow by the value of new construction only. This would result in \$289.2 million less in local school property taxes and require \$536.1 million in additional state money to fund increased enrollment and a 1.16 percent increase in per student funding.

### **PreK-12 Education (Total Need - \$76.9 million)**

**Critical Needs (-\$478.6 million)** – Maintaining the current PreK-12 budget and funding new students at current per-student level will require an additional \$101.8 million. This includes \$94.2 million for 13,680 new K-12 students and \$7.6 million for 3,010 more students in the Voluntary Pre-Kindergarten Program. However, the *Outlook* makes two revenue assumptions that reduce the need for GR to fund education. There is enough unspent revenue in two education trust funds<sup>7</sup> to use \$103.9 million to replace GR funds. It is also assumed the Legislature will keep the same school property tax millage rate for RLE<sup>8</sup>, resulting in \$480.0 million in additional revenue from increasing property values. This may not happen (see the High Priority Needs section). These increased non-GR revenue sources means that \$478.6 million less in GR would be needed to maintain the current PreK-12 budget and fund enrollment growth.

**High Priority Needs (\$555.5 million)** – In addition to maintaining per student funding (a critical need), the *Outlook* includes an increase in per student funding equal to the average of the last three years. This would be a 1.16 percent increase for the Florida Education Finance Program (FEFP), costing \$237.2 million next year. This would add approximately \$86 to the current per-student funding of \$7,408.

As discussed above, the estimate of critical needs assumes the Legislature would keep the same RLE millage rate. However, the 2016 and 2017 Legislature opted to maintain total RLE dollars at the previous level, using state funds to pay for increased costs. Last year, the Legislature used the rolled-back millage rate, which allows property tax revenue to increase by the value of new construction only. The High Priority Needs estimate anticipates the Legislature doing this again, which would require \$289.2 million in extra state funding for the FEFP. This would basically buy-back a portion of the \$480 million in increased RLE that was assumed in Critical Needs. Since this approach to RLE would increase the state’s share of increased FEFP costs, the *Outlook* adds an additional \$9.7 million to the High Priority Needs.

The *Outlook* also includes a funding increase of \$18.9 million for the Florida Best and Brightest Teacher and Principal Scholarship Program and \$0.5 million for the operations of the Florida School for the Deaf and Blind.

<sup>7</sup> The Educational Enhancement Trust Fund (funded by the lottery and slot machines) and the State School Trust Fund (funded by unclaimed property).  
<sup>8</sup> Required Local Effort is the amount of property taxes school districts must levy in order to participate in the state’s school funding formula—the Florida Education Finance Program. The Legislature sets the amount of RLE—currently \$7.7 billion-- in the General Appropriations Act each year, although it is not counted as a state appropriation. The current RLE millage rate is 4.075 mills statewide. School districts may also levy a non-voted local discretionary millage of 0.748 mills, that produces an additional \$1.5 billion.

### **Higher Education (Total Need – \$289.4 million)**

**Critical Needs (\$1.4 million)** – An additional \$10.4 million will be needed to fund more eligible students for the Bright Futures and the Children and Spouses of Deceased/Disabled Veterans scholarship programs. The Educational Enhancement Trust Fund (Lottery) will provide \$9.0 million, with the remaining \$1.4 million coming from GR.

**High Priority Needs (\$288.0 million)** – To maintain the current budget for colleges and universities, \$64.8 million is included to restore non-recurring appropriations. This includes \$52.7 million in performance incentive funding, \$2.5 million in equity-based allocations for state college operations, and \$9.6 million to restore student award amounts for the EASE and ABLE grant programs.

Workload increases are included for universities (\$158.5 million), colleges (\$14.1 million), and workforce education (\$0.5 million). Another \$50.1 million is included for increased funding for student financial assistance programs, most of which (\$40.2 million) goes to Florida Student Access Grants

### **Education Capital Outlay (Total Need – \$118.0 million)**

**High Priority Needs (\$118.0 million)** – Public Education Capital Outlay (PECO) funding has historically come from a mix of bonding and gross receipts tax collections in the PECO Trust Fund, plus supplemental GR and EETF funds. Due to the state’s recent policy of not bonding for PECO, the *Outlook* assumes GR will be used to maintain current spending levels. To maintain the three-year average (excluding any member projects), \$118.0 million in GR would be needed. This would be in addition to the \$347.7 million available in the PECO fund for construction, renovation, maintenance and repair of educational facilities.

### **Health & Human Services (Total Need – \$309.1 million)**

**Critical Needs (\$182.9 million)** – Medicaid is a \$27.5 billion federal and state program, the largest single program in the state budget. Not surprisingly, its growth creates the largest need for additional funding in a continuation budget. Total Medicaid beneficiaries are estimated at just under 4.0 million. After decreasing the last two years, the number of beneficiaries is expected to start rising again in FY 2019-20. An additional 28,000 cases are expected in each of the next three years—growth of less than one percent. Total program expenditures are expected to increase by \$591.2 million over the base budget next year. Medicaid is funded through GR, various state trust funds and federal funds. The GR portion of this increase is \$143.1 million. A slight decrease in the Federal Medical Assistance Percentage (FMAP) will result in the need for more GR. Lower than anticipated revenues from the Tobacco Surcharge—which go into Medicaid trust funds—and the Tobacco Settlement Trust Fund also boost the GR requirement.

The Patient Protection and Affordable Care Act has increased the federal share of funding for Florida’s Kidcare program to 96 percent. Florida’s share will begin rising next year, when the Kidcare FMAP falls to 87 percent. It is expected to reach 73 percent by FY 2021-22. With the lower FMAP, an expected increase of 12,543 beneficiaries (5.0 percent) will require an additional \$50.3 million in GR.

Continuing declining enrollment in Temporary Assistance for Needy Families (TANF) will reduce the total critical needs in Health & Human Services. Expected TANF expenditures in the current year are \$10.1 million below the amount appropriated. Coupled with another small decrease in enrollment next year, the *Outlook* estimates a \$10.5 million reduction in GR spending.

**High Priority Needs (\$126.2 million)** – In Medicaid, the *Outlook* includes \$45.3 million for additional waiver slots for the elderly and provider rate increases. Increases in GR funding for the following agency programs are also provided:

- *Children and Families* (\$54.7 million) – This includes increases for adoption subsidies, community-based care lead agencies, child abuse investigations by sheriffs, foster care, homeless coalitions, claims bills, domestic violence prevention and services, child welfare legal services, and mental health and substance abuse initiatives.
- *Health* (\$3.4 million) – Funding increases are provided for Early Steps, cancer screening, biomedical research, newborn screening, and the Office of Medical Marijuana Use.
- *Persons with Disabilities* (\$11.6 million) – These dollars are for reducing the waitlist for the developmental disability waiver, supported employee and internship programs, and Medicaid Waiver provider rate increases.
- *Veterans Affairs* (\$1.3 million) – Increases are provided for the Entrepreneurship Program and the Veterans Training Grants Program.
- *Elder Affairs* (\$5.4 million) – Additional funding is included for reducing the Community Care for the elderly waitlist, Alzheimer’s disease respite services, Public Guardianship services, and Aging Resource Centers.

The *Outlook* also includes \$4.5 million in GR (along with \$23.9 million in trust funds) for human services information technology costs. This includes the completion of the Agency for Persons with Disabilities’ Client Data Management System, the Florida Medicaid Management Information System transition, and cloud conversion for the Department of Children and Families’ Florida Safe Families Network.

### ***Economic Development and Transportation (Total Need - \$320.7 million)***

**Critical Needs (\$152.2 million)**– The Department of Transportation’s work program is not funded with GR, so transportation system needs are not reflected here. One critical needs item is included: \$152.0 million for the state match for federal FEMA disaster funding. All damage assessments and claims processing, which can span several years, may not be complete and could increase this match requirement.

**High Priority Needs (\$168.5 million)** –\$116.0 million in GR is included for economic development and workforce programs, including \$65.0 million for the Job Growth Grant Fund. Funding is included for maintenance and security enhancement of National Guard armories and other military affairs priorities (\$5.2 million). Funding for the Department of State’s library, cultural, historical, and election priorities (\$47.3 million) is also included, down from \$70.3 million, reflecting the Legislature’s reduced spending in these areas after significantly increasing funding for these programs in 2014.

### ***Criminal Justice & Courts (Total Need - \$110.3 million)***

**Critical Needs (-\$13.4 million)** – Florida’s prison population continues to decline. It is predicted that FY2019-20 will mark the sixth straight year that the year-end population will decrease. In FY2013-14, the year-end population was 100,942 inmates, the next budget year will see an estimated 95,878 inmates (a decrease of 5.0 percent). The *Outlook* estimates a \$13.4 million reduction in costs for the next budget.

**High Priority Needs (\$123.7 million)** – In recent years, expenditures for due process and conflict cases have exceeded appropriations and the Legislature has consistently funded the deficits. The *Outlook* includes an increase of \$17.8 million for these costs. In corrections, increased costs were included for

inmate health services and pharmaceuticals (\$43.5 million), and the settlement of lawsuits relating to the accommodations of inmates with mental health treatment needs (\$54.9 million) and for those with disabilities (\$1.7 million).

There are 278 youths adjudicated to residential commitment programs but waiting for an actual assignment to a residential facility. The average length of time between adjudication and commitment is 53 days. GR of \$5.7 million is included for additional residential commitment beds.

### **Natural Resources (Total Need - \$309.1 million)**

**Critical Needs** – None.

**High Priority Needs (\$309.1 million)** – Although there are no additional critical needs identified in Natural Resources in the *Outlook*, significant high priority needs are included, highlighting the Legislature's increased environmental funding in recent years. Funding of \$121.2 million GR (along with \$162.7 million in trust funds) is provided for water and land conservation. This includes additional GR Florida Forever (\$39.6 million), Everglades restoration projects (\$8.3 million<sup>9</sup>), land management (\$40.7 million), St. Johns River/Keystone Heights restoration (\$8.7 million), and Lake Apopka (\$5.0) million.

The Legislature is expected to continue to fund scores of local water projects, so the *Outlook* includes \$56.1 million for these. Florida TaxWatch reiterates its recommendation to develop a formal, comprehensive competitive selection process for these projects.<sup>10</sup>

Another \$138.1 million is included for a myriad of environmental and agricultural programs including drinking water and wastewater loans, Florida Keys protection, the Herbert Hoover Dike, payments due from citrus canker eradication litigation, agriculture promotion, citrus research, and Fish & Wildlife Commission programs. Funding is based on the average of the last three years of appropriations.

### **General Government (Total Need - \$90.6 million)**

**Critical Needs (\$23.9 million)** - State law requires the Legislature to provide money to fiscally constrained counties to offset property tax reductions arising from two constitutional amendments. While paid annually, this money is considered non-recurring and is not part of the budget base, so the entire payment is included in Critical Needs. This will cost \$23.6 in the next budget. **This does not include \$10.5 million that will be needed to reimburse the counties should the voters approve a new homestead exemption this November.**

A small increase (\$0.3 million) is expected in Non-Florida Retirement System Pensions and Benefits (such as for the Florida Natural Guard and disabled justices and judges).

Due in large part to Hurricane Irma, there is a projected deficit for FY 2019-20 in the state's self-insurance fund, which provides workers' compensation, general liability, federal civil rights, auto liability, off-duty law enforcement vehicle property damage, and property insurance coverage to state agencies. The next budget will need \$9.4 million in GR to close that deficit.

<sup>9</sup> \$117.3 million in additional trust fund spending on Everglades restoration is assumed.

<sup>10</sup> Florida TaxWatch, The 2018 Budget Turkey Watch Report: An analysis of the transparency and accountability of the budget process, April 2018.

**High Priority Needs (\$66.7 million)** – GR of \$17.0 million is included for general repair and maintenance of the state building pool, \$11.6 million for the replacement of the state’s accounting system (FLAIR) and \$3.6 million is provided for other general government activities.

### **Statewide Issues (Total Need – \$241.1 million)**

**Critical Needs (\$167.1 million)** – State contributions for state employee health insurance are expected to increase by \$272.6 million next year, which will lead to a mid-fiscal year premium increase of 11 percent. This will require \$86.4 million from the General Revenue Fund and \$55.7 million from trust funds.

The *Outlook* assumes the Legislature will continue providing full funding to amortize any unfunded liability in the Florida Retirement System. The state has lowered the expected investment rate of return (currently 7.5 percent) in three of the last four years. Further reductions are very possible. Based on a three-year average, the *Outlook* an increase of \$71.6 million in GR and \$10.1 million from trust funds.

A reduction of 0.3 percent for operations of the Division of Administrative Hearings is projected, based on reduced hearing hours in FY 2017-18.

**High Priority Needs (\$74.0 million)** - GR of \$44.6 million is provided for state employee bonuses and competitive, merit and retention pay adjustments and \$29.4 million is provided for critical capital improvements of state buildings.

## **CONCLUSION**

The *Outlook* is a very useful tool, but it is not meant as a blueprint for the next state budget and its estimate of any surplus or shortfall is debatable. There are many, many factors that impact these forecasts. There will be another round of estimating conferences before the next legislative session begins in March (or soon after it starts) that could significantly change—either up or down--the estimate of available revenue, as well as estimates for budget drivers such as school enrollment and Medicaid caseloads.

There are also significant risks to state’s forecasts. The impact of hurricanes and other natural disasters, pending litigation against the state, the possible loss of federal Medicaid funds for hospitals, and the state’s current \$732 million unfunded obligation for unfinished education capital outlay projects that were funded in prior years are all cited as potential needs for increased expenditures. Threats to our economy, including events reducing tourism (such as red tide) and the potential for a full-scale trade war could negatively impact tax collections.

The Legislature is to be commended for taking steps to mitigate looming budget shortfalls. However, its work is not done. It is still clear that the 2019 Legislature will have to cut some current spending (or increase revenues) if it wants to fund any new initiatives. The new Governor will likely have some new spending priorities of his own.

The next budget can be balanced without too much trouble, but changes are needed to avoid future, larger problems. Simply, the problem is that recurring GR spending is growing faster than available recurring GR, and the longer it takes to address the problem, the more expensive corrective action will become. It will take a net reduction in recurring expenditures (budget cuts minus new initiatives) of \$199.0 million to erase the projected shortfall in FY2021-22.

One way to help achieve the needed budget fix is to implement the recommendations of the 2016 Government Efficiency Task Force (GETF). The 29 recommendations within the final GETF report range on issues from telehealth to criminal justice to efficiency in state contracting. The state could realize savings and cost avoidance upwards of \$2 billion if these recommendations were implemented.

Florida TaxWatch also urges considerable restraint by lawmakers in requesting local member projects. Despite new rules designed to limit and increase the transparency of member projects, the 2018 budget contained more than 500 projects worth more than \$560 million, a surprising amount given that it was pronounced “a tight budget year.” Some of the funding for these projects are included in the *Outlook’s* high priority needs, but most are not.

The Legislature should reconsider its use of trust fund sweeps to balance the budget. The *Outlook* should also not assume the Legislature will sweep trust funds, for it further legitimizes the practice as an integral part of the budget process, instead of one of the last resorts in tight budget years. Trust fund transfers have their place in budgeting, especially in times of a shortfall, when education and human services (which comprise the majority of general revenue spending) typically bear the brunt of budget cuts; however, care should be taken that the lawfully-created relationship between trust fund revenues and their uses is considered and the impact of the sweeps should be quantified and evaluated.

Florida TaxWatch reiterates its recommendation that if the Legislature wants to sweep a trust fund, it should be required to introduce a separate general bill for each trust fund sweep. Currently, a legislator cannot vote against a trust fund sweep without voting against the entire budget. Like other bills, a staff analysis would be developed that would compare what would be funded with and without the sweep and the associated costs and benefits. The analysis should also address the current tax or fee structure that funds the trust fund and determine if the current levels are appropriate.

## APPENDIX

### What is the Long-Range Financial Outlook?

The *Long-Range Financial Outlook* is a valuable, constitutionally required budget planning tool that looks ahead three years, comparing estimated revenues and expenditures. This summer's round of state estimating conferences was the basis for the *Outlook*, which is produced annually by the legislative Office of Economic and Demographic Research and the House and Senate Appropriations Committees. The *Outlook* focuses on General Revenue (GR)--the funds that can be spent by the Legislature on anything and that are major source of funding for education, human services and criminal justice. The *Outlook* also forecasts some trust funds that can affect the need for GR spending in certain areas of the budget, such as the Educational Enhancement Trust Fund, which provides lottery and slot machine revenue for education.

The *Outlook* first projects the amount of GR that will be available for the budget. That amount is then compared to the base budget (recurring appropriations in the current budget) plus an estimate of increased spending needed for a "continuation budget." The difference in projected revenues and expenditures is the projected surplus or shortfall.

The forecasted growth in expenditures is made up of two categories. **Critical Needs** are mandatory increases (based on estimating conferences and other essential items), representing the minimum cost to fund the budget without significant programmatic changes. New initiatives and funding increases above what is required are not included. For example, the cost of funding additional students is included as a critical need but an increase to per student funding is not. Historically, maintaining per-student Pre K-12 student funding levels and increased Medicaid costs make up the vast majority of these new "critical needs."

**High Priority Needs** are historically funded issues that are typically viewed as "must fund" in normal budget years. These can include the continued funding of programs paid for with non-recurring revenues, as well as non-mandatory increases for recurring programs. These are usually calculated by using the three-year average appropriations for that program. For example, while Critical Needs include only the cost of maintaining per-student funding, this year's High Priority Needs include a 1.16 percent increase in per-student funding (the average increase of the last three years).

Adding these two categories to the recurring expenditures in the current budget comprises what can be thought of as a continuation budget.

In 2015, the *Outlook* began assuming that the Legislature will cut taxes (reducing GR) and sweep trust funds<sup>11</sup> (increasing GR). These two changes (the average of the previous three years) are added to the estimate of available GR. So far, the estimate of trust fund sweeps has been larger than the tax cut estimate, so this has improved the budget outlook in the first year. However, since a portion of the tax cuts is considered recurring, while the sweeps are non-recurring, the impact of the tax cuts compounds over time and it reduces the surplus (or increases the shortfall) by the second or third year of the forecast.

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<sup>11</sup> The Legislature often transfers money from trust funds, which has specified uses, to GR, which may be used for anything. For more information see Florida TaxWatch, Putting the Trust Back in Trust Funds, March 2014.

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