

FLORIDA IS FACING LARGE BUDGET SHORTFALLS

FEDERAL AID HAS ALLOWED THE STATE TO AVOID A DEFICIT SO FAR, BUT THE 2021 LEGISLATURE WILL HAVE TO ACT

The severe economic contraction brought on by COVID-19 has reduced state revenues significantly. The pandemic is also increasing government costs such as virus response/recovery and assistance to those harmed economically by the public health emergency. This spells trouble for the current and future state budgets.

The legislative *Long-Range Financial Outlook* is a constitutionally required annual report that compares estimated revenues to 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). It is a valuable tool that also looks ahead, giving a sense of what past budgetary actions mean for the state's financial *Outlook* over the next three years.

The latest edition of the *Outlook*,¹ recently adopted by the Joint Legislative Budget Commission, estimates that the FY2020-21 state budget passed by the Legislature last March will have a General Revenue (GR) budget shortfall of \$2.750 billion after funding the base budget plus "critical needs" and "high priority needs." This is considered a conservative continuation budget. Shortfalls of \$1.883 billion and \$0.928 billion are forecast for the next two budgets (see *What Are the \$2.653 Billion in Estimated GR Needs for FY2021-22?* On page 9 for detail on these spending needs).

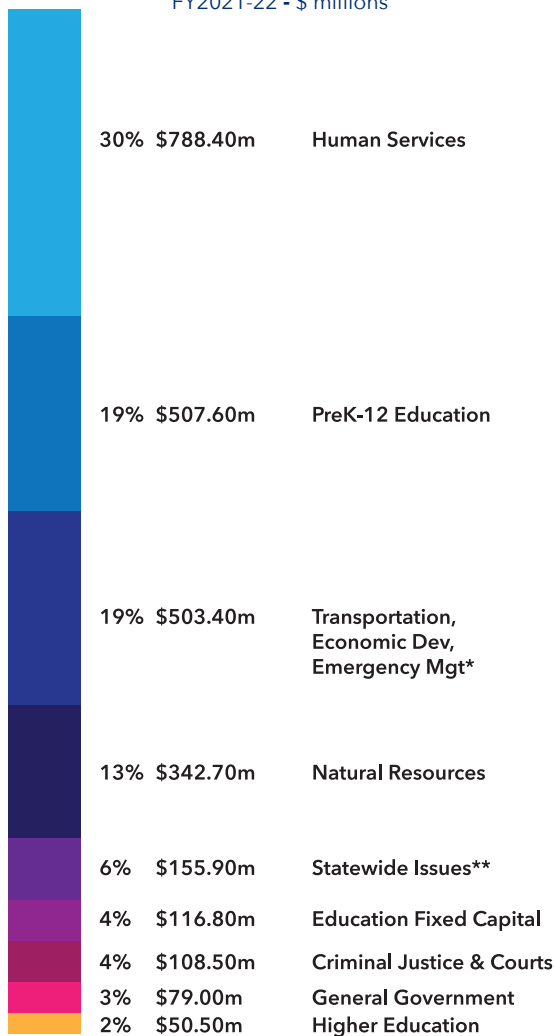
Actual GR collections in FY2019-20 came in \$1.883 billion below estimate as the pandemic severely impacted the last three months (April-June) of the fiscal year. In August 2020, the state's Revenue Estimating Conference reduced the GR estimate for FY2020-21 (the current budget year) by \$3.459 billion (10.0 percent) and by \$1.996 billion in FY2021-22. The previous estimates (January 2020) were the ones the current budget was built on. Huge sales tax losses—especially in the tourism and hospitality sector—and reduced corporate income tax collections were the main culprits.

¹ Florida Legislature, Long-Range Financial Outlook, Fiscal Years 2021-22 through FY2023-24, September 10, 2020. Available at http://www.edr.state.fl.us/Content/long-range-financial-outlook/3-Year-Plan_Fall-2020_2022-2224.pdf

The federal government—though the CARES Act—provided Florida governments \$8.328 billion in aid to respond to the pandemic. Of that amount, \$2.472 billion was sent directly to the state’s larger local governments. The remaining \$5.856 billion was deposited into the state’s GR Fund late in FY2019-20. This has allowed Florida to avoid a budget deficit—so far.

Critical and High Priority Needs by Program Area

FY2021-22 - \$ millions



HIGHLIGHTS

- The state’s *Long-Range Financial Outlook* estimates that as the 2021 Legislature develops the next state budget, it will be facing a GR budget shortfall of \$2.750 billion after funding the base budget plus “critical needs” and “high priority needs”—a conservative continuation budget. Shortfalls of \$1.883 billion and \$0.928 billion are forecast for the next two budgets.
- The COVID-19 pandemic battered Florida’s economy and left 1.4 million people without jobs. Huge sales tax losses in the tourism and hospitality sector and reduced corporate income tax collections resulted in total GR collections coming in \$1.899 billion below estimate for FY2019-20. In August 2020, the Revenue Estimating Conference reduced the GR estimate by \$3.459 billion for FY2020-21 and by \$1.996 billion in FY2021-22. This is compared to the last estimate (January 2020) on which the FY2020-21 budget was built.

* Transportation is funded entirely by trust funds, so the Outlook includes no additional costs for transportation. \$376.3 million of this amount is the required state match for FEMA disaster funding.

** Includes state employee salary and benefit increases, capital improvements, statewide technology issues, etc.

Source: Florida TaxWatch from data in the 2020 Long-Range Financial Outlook.

- Florida's constitution requires the budget to be balanced and, thanks to \$5.856 billion in federal aid, the Legislature was able to avoid a budget deficit in FY2019-20 and may be able to avoid one for the current budget. Despite this good news, the *Outlook* makes it clear the 2021 Legislature will have to take significant steps to balance the budgets for next year and beyond.
- It is estimated that the current budget year will have a surplus of \$1.322 billion and this is the starting point for *Outlook's* estimates; however, the estimate could be overstated.
- The federal CARES Act funds that the state deposited into the General Revenue Fund included \$1.275 billion that Congress earmarked for local governments. The state has only made one payment of \$318.8 million, meaning more than \$950 million still needs to be paid to local governments.
- In addition, the estimated surplus in FY2020-21 assumes all the CARES Act money can be used for existing appropriations that qualify or that Congress will allow states to use the aid to replace lost revenue, both of which are far from certain. Since all the money is already allocated, any significant new virus response expenses that may arise will also reduce the current surplus and increase the shortfalls estimated by the *Outlook*.
- The *Outlook* estimates "critical needs" will require an additional \$1.481 billion over the recurring GR base budget in FY2021-22. If the Legislature were to only fund these needs next year, a shortfall of \$1.806 million would result. "High priority needs" will require an additional \$1.172 billion.
- The *Outlook* also assumes that lawmakers will "sweep" \$312.4 million from trust funds (transferring it to GR) and pass \$84.9 million in tax cuts.
- The largest critical need in the *Outlook* for FY2021-22 is an additional \$546.6 million in GR (as well as \$1.330 billion from state trust funds) to fund Florida's \$31 billion Medicaid program. The number of beneficiaries has swelled due to the pandemic. These state costs are increasing despite the federal government paying a larger share of costs.
- The next largest need is funding to pay for 30,481 new public school students and increasing per-student funding by 2.4 percent. This will cost \$608.0 million in GR but \$124.0 million can be offset by increased lottery revenue in the Educational Enhancement Trust Fund. The state will also need \$376.3 million for its share of federal emergency management disaster funding for COVID-19 and hurricane recovery.

- The *Outlook* assumes a GR reserve (unobligated cash) of \$1.0 billion, as it does every year. This has been a conservative (lower than actual) estimate—the Legislature has left a larger planned reserve than that in each of the last ten years, including \$1.7 billion last session; however, the previous two recessions have left planned cash reserves below \$1.0 billion. While the Legislature would like to leave a larger reserve due to economic uncertainty (which would increase the shortfall), it is doubtful it will be much more than \$1.0 billion—and could be less.

BUDGET OUTLOOK

At the time of the last estimates in January 2020, a positive GR balance of \$1.9 billion was expected at the end of FY2019-20; however, actual revenues for the year came in \$1.9 billion under estimate, basically wiping out the reserves. Further, other events affecting both revenues and net appropriations occurred post-2020 session that affected the bottom line.

Some additional GR spending occurred, including \$460.8 million for COVID-19 response and \$69.8 million for hurricane response.

Florida deposited \$5.856 billion in CARES Act aid into the General Revenue Fund, assuring FY2019-20 would finish in the black. Additional federal aid arrived in the form of an increased Federal Medical Assistance Percentage (FMAP), which means the federal government will pay a higher share of Florida’s Medicaid costs. In addition to paying for some of the increased cost of rising Medicaid enrollment this year and next, the FMAP allowed \$592.4 million that was appropriated for Medicaid in FY2019-20 to revert, adding it to reserves. The state also took action to increase reserves by reverting an additional \$196.8 million in unbudgeted funds at the end of the fiscal year. The end result of all this was the state ended FY2019-20 with \$5.822 in GR in the bank.

Carrying that reserve forward into the current budget year allows the state to offset the \$3.459 billion in reduced revenue caused by the pandemic, as well as new budget amendments totaling \$896.2 million in additional spending for COVID-19 response. It is now estimated that the current budget year (FY2020-21) will have ending cash reserves of \$1.322 billion. This balance is the starting point for the new *Long-Range Financial Outlook*.

The Budget *Outlook* table on page 5 shows all three “tiers” of budget estimates. Tier 1 includes funding of the base budget and “critical needs,” which are defined as the minimum cost to fund the budget without significant law or programmatic changes. Tier 2 adds “high priority needs” which are historically funded issues that are typically viewed as “must fund” in normal

Budget Outlook - FY2021-22 through FY2023-24

General Revenue - \$ in millions

	FY21-22	FY22-23	FY23-24
Revenues			
Unspent GR from Prior Year	\$1,322.5	\$1,000.0	\$1,000.0
Estimated Revenues	\$33,691.2	\$35,279.3	\$36,800.7
BP Settlement	\$26.7	\$26.7	\$26.7
Non-Op Funds and Transfers	\$98.3	\$97.6	\$97.2
Total GR Available for Appropriation	\$35,138.7	\$36,403.6	\$37,924.6
Expenditures			
Base Budget	\$34,158.5	\$35,308.3	\$35,807.2
Increase - Critical Needs	\$1,481.0	\$773.3	\$392.0
Transfer - Budget Stabilization Fund			\$11.7
Transfer - Lawton Chiles Endowment	\$304.7		
Total Estimated Expenditures	\$35,944.2	\$36,081.6	\$36,210.9
Cash Reserves	\$1,000.0	\$1,000.0	\$1,000.0
Surplus/(Shortfall) - Fund Critical Needs Only	(\$1,805.5)	(\$677.9)	\$713.7
Recurring Impact of Critical Needs		(\$378.7)	(\$740.0)
Increase - High Priority Needs	(\$1,171.9)	(\$1,001.4)	(\$991.0)
Surplus/(Shortfall) - Critical & High Priority Needs	(\$2,977.4)	(\$2,058.1)	(\$1,017.3)
Revenue Adjustments			
Tax Cuts (see note)	(\$84.9)	(\$153.4)	(\$221.9)
Trust Fund Sweeps	\$312.4	\$312.4	\$312.4
Surplus/(Shortfall) - Critical & High Priority Needs & Revenue Adjustments	(\$2,749.9)	(\$1,899.1)	(\$926.8)

Note: Assumes the same amount of tax cuts are adopted each year--\$68.5 million in recurring cuts (\$41.5 million in first year) and \$43.4 million in one-time cuts. The annualization and recurring portion of the cuts compounds the amount in subsequent years.

Source: Florida TaxWatch from data in the 2020 Long-Range Financial Outlook

FY2021-22 General Revenue Spending Increases Included in the Outlook

\$ millions

Medicaid - Increased caseloads, waivers and provider payments	\$584.0
K-12 Education (FEFP) - Enrollment growth and a 2.44% per-student funding increase	\$513.9
State Match for Federal Emergency Management Disaster Funding	\$376.3
Water and Land Conservation - Everglades, Florida Forever, lake restoration, etc.	\$170.7
State Employees - Pay issues, health insurance, and retirement benefits	\$130.1
Other Agricultural and Environmental Programs	\$119.8
Higher Education	\$50.6
Education Fixed Capital Outlay	\$116.8
Developmental Services	\$72.0
Corrections - Inmate Health Services	\$67.7
Children & Family Services	\$67.6
State Buildings - Repair, maintenance, and capital Improvements	\$65.3
Local Water Projects	\$52.2
Job Growth Grant Fund	\$48.3
Other Criminal Justice & Courts	\$40.8
Economic Development Incentive Programs	\$40.0
Dept. of State - Cultural, Historic Preservation, Elections, and Library Grants	\$34.2
Temporary Assistance to Needy Families (TANF)	\$33.8
Fiscally Constrained Counties - Reimburse property tax losses from constitutional amendments	\$31.5
Other Health & Human Services	\$23.7
Other General Government	\$12.5
Kidcare - Enrollment growth and reduced federal funding (FMAP)	\$7.1
Voluntary PreK (reduced enrollment)	(\$6.3)
TOTAL	\$2,652.6

budget years. Tier 3 also includes “revenue adjustments” which are the three-year averages of trust funds sweeps (which reduce the shortfall) and tax cuts (which increase the shortfall).

It is now estimated the 2021 Legislature will have \$35.139 billion in GR available for the FY2021-22 budget, enough to cover the recurring base budget of \$34.158 billion. But when spending is added to cover “critical needs”—a shortfall of \$1.805 billion results. The “high priority needs” increase the shortfall to \$2.977 billion and the revenue adjustments decrease to shortfall to \$2.750 billion.

Shortfalls are estimated for FY2022-23 and FY2023-24 as well: \$1.899 billion and \$0.927 billion, respectively. They are smaller because revenues, while still well below previous estimates, are expected to begin rising again on a year-to-year basis. Also, critical needs in FY2021-22 are higher due in large part to increasing costs in human services, especially Medicaid.

The *Outlook* assumes the Legislature will address any shortfall (as it must) and leave \$1.0 billion in reserves, so the shortfalls in the *Outlook* are not cumulative. Each year starts with \$1.0 billion in the bank.

While the *Outlook* predicts there will not be a deficit this year (FY2020-21), there are factors that make one a distinct possibility.

The more than \$5 billion from the CARES Act that is being counted as available GR includes funds that still need to be distributed to local governments. Of the \$1.275 billion in CARES Act funds that Congress earmarked for local governments, the state has only disbursed \$318.8 billion, meaning more than \$950 million still needs to be distributed to cities and counties. This will reduce the estimated \$1.322 billion surplus to less than \$400 million. Any event that lowers the estimated surplus for this year will also impact the years covered in the *Outlook*, since less money will be carried forward.

Further, as Florida TaxWatch has been pointing out,² there are no assurances Florida will be able to use all the CARES Act relief funding that we now have in the bank. The Act limits funding to “necessary state and local government expenditures incurred due to the COVID-19 public health emergency.” The costs can’t be in the state’s budget most recently approved as of March 27, 2020. Florida’s budget was not signed until June 29 so its expenses could qualify; however, the budget was developed largely without COVID-19 in mind.

2 Florida TaxWatch, Budget Watch, COVID-19 Impact, July 29, 2020.

CARES Act funds may not be used directly for revenue replacement or to cover shortfalls. In addition to direct virus response expenditures, funds may be used for second-order effects of the emergency, such as economic support to those suffering from employment or business interruptions.³ Florida will be able to find appropriations in the budget that, while not originally envisioned to respond to COVID-19, would qualify for CARES Act fund. For example, payroll expenses for public safety, health care, human services, and similar government employees whose services are substantially dedicated to mitigating or responding to the COVID-19 public health emergency.

The *Outlook* includes a note that the GR Estimating Conference used to qualify the estimate of a surplus in the current year:

“However, there is a very high degree of uncertainty surrounding the future allowable uses of these dollars by states and local governments. To the extent that the funds cannot be used to fill revenue shortfalls or offset current appropriations when they are used for pandemic-related purposes, or if additional COVID-19 expenditures are required, the Fiscal Year 2020-21 ending balance shown in this Outlook will be lower, potentially becoming negative.”⁴

WHAT ARE THE \$2.653 BILLION IN ESTIMATED GR NEEDS FOR FY2021-22?

This detailing of the \$1.481 billion in Critical Needs and \$1.172 billion in High Priority Needs focuses on General Revenue (as does the *Outlook*). Many of these issues will require additional trust fund revenue as well.

PreK-12 Education (Total Need - \$507.6 million GR)

Critical Needs (\$477.7 million GR) - Historically, the *Outlook* has considered the GR needed to fund enrollment growth (at the current per-student funding amount) a Critical Need and any increase to the per-student funding to be a High Priority Need. Starting with last year, both are now considered Critical Needs. Enrollment growth of 30,481 students (1.1 percent) and increasing per-student funding for all students by 2.4 percent (the average of the last three years) will require \$797.6 million in additional funding.

However, the *Outlook* makes two assumptions that will reduce the need to use GR for this additional education funding. It is estimated there will be enough unspent revenue in two education trust funds⁵ to reduce the need for GR by \$124.0 million. It is also assumed the Legislature will adopt the rolled-back school property tax millage rate for RLE⁶, meaning there will be additional revenue from new construction. This will result in an increase of \$158.4 million in local school property tax revenue for RLE. Additionally, it is assumed the Non-Voted Discretionary Millage rate (levied by all districts) will remain at 0.748 mills, producing an additional \$31.2 million from increasing property values. The result is that only \$484.0 million of the \$797.6 million needed to fund enrollment growth and increase per-student spending by 2.4 percent will need to come from GR.

The other Critical Need in education will help the budget's bottom line. A projected enrollment drop of 2,408 more students in the Voluntary Pre-Kindergarten Program will reduce GR funding by \$6.3 million (at the current per-student level).

High Priority Needs (\$29.9 million) - With the cost of increasing per-student spending now considered a Critical Need, the only High Priority Needs in the *Outlook* are an increase of \$28.9 million for the Gardiner Scholarship Program, a \$0.845 million increase for the operations of the Florida School for the Deaf and Blind, \$0.189 million to restore nonrecurring funds for the teacher salary increase passed last year.

Higher Education (Total Need - \$50.5 million GR)

Critical Needs (-\$66.4 million) - An additional \$1.9 million in GR will be needed to fund

more eligible students for the Children and Spouses of Deceased/ Disabled Veterans scholarship program. Bright Futures Scholarships are funded by the Educational Enhancement Trust Fund (Lottery) and 3,820 fewer eligible students will reduce needed lottery funds by \$19.6 million in FY2021-22.

In addition, growth in lottery revenues provides an additional \$68.3 million from the Educational Enhancement Trust Fund to be used in higher education instead of GR. This reduces the total cost of the Critical Needs.

High Priority Needs (\$117.0 million GR) - Workload increases are included for universities (\$77.7 million), colleges (\$22.7 million), and workforce education (\$8.0 million). These increases are the three-year average increase provided, not including member projects. Another \$7.8 million is needed for increased funding for student financial assistance programs—Effective Access to Student Education (EASE) and Access to Better Learning (ABLE) grants and the Benacquisto Scholarship Program.

Another \$0.8 million is provided to restore a nonrecurring appropriation for Workforce Development programs at school district technical centers using a statewide equity-based funding model.

Education Capital Outlay (Total Need - \$116.8 million GR)

High Priority Needs (\$116.8 million GR) - 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; however, since the Legislature has authorized bonding for PECO only once in the last ten years, the *Outlook* assumes GR will be used to maintain current spending levels. To maintain the three-year average (excluding any member projects), \$116.8 million in GR would be needed. This would be in addition to the \$242.3 million available in the PECO fund for construction, renovation, maintenance and repair of educational facilities, including both traditional public and charter schools.

Health & Human Services (Total Need - \$788.4 million GR)

The COVID-19 pandemic and the attendant economic slowdown and massive unemployment resulted in a large increase in Floridians in need. Not surprisingly, the cost of providing assistance to these families results in this budget area requiring the most additional funding. In addition to \$788.4 million in GR, another \$1.676 billion from state trust funds is expected to be needed.

Critical Needs (\$587.5 million) - Medicaid is a \$31.3 billion federal and state program

and the largest single program in the state budget, accounting for 32.1 percent of the state budget. After Medicaid enrollment declined and stayed below the FY2016-17 level for three years, the COVID-19 pandemic and the attendant economic slowdown and massive unemployment is expected to add more than half a million beneficiaries to the program. The program will serve 4.4 million Floridians, up from 3.8 million last year. Caseloads are expected to decrease very slightly in FY2021-22 and stay at an elevated level through at least FY2023-24. Total program expenditures are expected to increase by \$3.0 billion in the current year and rise slightly in FY2021-22. Medicaid is funded through GR, various state trust funds and federal funds. The GR portion of the FY2021-22 increase is \$553.7 million and another \$1.330 billion from state trust funds will be needed. An increased Federal Medical Assistance Percentage (FMAP) will help limit the state's additional funding need.

Florida's Kidcare Program—which implements the federal Children's Health Insurance Program (CHIP)—provides health insurance to uninsured low-income children. The federal government pays roughly three-quarters of the cost of the program. Enrollment has been increasing significantly and will continue to do so through the *Outlook's* forecast horizon, increasing from 244,874 in FY2019-20 to 302,332 in FY2023-24—growth of 23.5 percent. The 25,000 additional children in FY2021-22 will cost the state \$7.1 million in GR.

Caseloads and expenditures are also rising in the Temporary Assistance for Needy Families (TANF) program—another federal/state program. TANF provides assistance (including cash payment) and work opportunities to families in need. An additional \$33.8 million in GR will be needed in FY2021-22 to cover enrollment growth of 5.0 percent.

High Priority Needs (\$200.7 million) - Increases in GR funding for the following programs are assumed in the *Outlook*:

- **Medicaid** - \$37.4 million to the Agency for Health Care Administration and the Department of Elder Affairs for provider rate increases and additional waiver slots for the elderly.
- **Children and Families** - \$67.6 million to fund 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** - \$8.2 million to fund increases are provided for Early Steps, newborn screening, Child Protection Teams, Medical Quality Assurance, HIV/AIDS programs, epidemiology programs, three Florida Poison Control Centers, and the Office of Medical Marijuana Use.

- **Persons with Disabilities** - Reflecting the state's increased funding in this area, \$72.0 million is estimated to be needed to reduce the waitlist for the developmental disability waiver, supported employee and internship program enhancements, and Medicaid Waiver provider rate increases. Newly legislatively authorized additional services in the Home and Community Based Service category that are not included in the needs calculation may increase costs further.
- **Veterans Affairs** - \$1.3 million is included for the Entrepreneurship Program, the Veterans Training Grants Program, and veterans' home equipment.
- **Elder Affairs** - \$8.2 million in 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.
- **Information Technology** - \$5.6 million in GR (along with \$48.5 million in trust funds) to complete the Agency for Persons with Disabilities' Client Data Management System, the Department of Veterans' Affairs computer replacement program and security enhancements, the Florida Medicaid Management Information System transition, continuation of the Enterprise Client Information and Registration Tracking System (eCIRTS) Project in the Department of Elder Affairs, and cloud conversion for the Department of Children and Families' Florida Safe Families Network.

Economic Development and Transportation (Total Need - \$503.4 million GR)

Critical Needs (\$376.3 GR million) - One critical needs item is included: the state match for federal FEMA disaster funding for all open federally declared disasters. This state share of this hurricane recovery funding is expected be \$376.3 million in FY2021-22 and total \$755.7 million over the three years covered in the *Outlook*. Of the three-year total, \$381.4 million is due to COVID-19 and \$374.3 million is for hurricane recovery. The *Outlook* does not attempt to estimate costs for future disasters. Also, all damage assessments and claims processing, which can span several years, may not be complete and could increase this match requirement.

The Department of Transportation's work program is funded by the State Transportation Trust Fund, so transportation system needs are not reflected here. DOT's work program is estimated at \$9.1 billion in FY2021-22.

High Priority Needs (\$127.0 million) - \$88.3 million in GR is included for economic development and workforce programs, including \$48.3 million for the Job Growth Grant

Fund. The rest would go to traditional economic development programs such as the Qualified Target Industry Tax Refund, the High-Impact Performance Grant, and the Brownfield Redevelopment Tax Refund and Bonus Refund programs.

The *Outlook* assumes no new funding for any other economic development programs or additional funding for VISIT Florida.

Funding is also included for the Department of State's grant programs—libraries (\$3.2 million), cultural affairs (\$20.5 million), and historic preservation (\$7.6 million). This spending has been decreasing since the peak in 2014, despite the funding of many local member projects, which often supplant projects that were approved through the department's established grant programs⁷. The Department's election priorities (\$3.0 million) are also included.

Funding is included for maintenance and security enhancement of National Guard armories and other military affairs priorities (\$4.5 million).

Criminal Justice & Courts (Total Need - \$108.5 million)

Critical Needs (none) - Florida's prison population has been declining, falling by 13,148 inmates (13.0 percent) since FY2013-14, with declines every year. This culminated in a large drop of 7,006 inmates (8.3 percent) in FY2019-20 attributed to COVID-19. It is expected population will start increasing this year, but only minimally; however, the latest population estimates are below the estimate used to fund the current budget, so no prison workload increases are included in the *Outlook*.

High Priority Needs (\$108.5 million) - In Corrections, \$30.2 million is included for complying with a federal court order to test all inmates for Hepatitis C and treat those infected with a far more effective treatment (but also more expensive) treatment. In addition to the \$16,000 per inmate treatment cost, the number of those infected is also increasing. Also included are increased costs for pharmaceuticals (\$5.5 million), and the settlement of lawsuits relating to the accommodations of inmates with mental health treatment needs (\$29.1 million) and for those with disabilities (\$2.9 million).

In Juvenile Justice, there are 169 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 36 days and those awaiting commitment must be assigned to secure detention. GR of \$1.4 million is included for additional residential commitment

⁷ For more information on these and other projects that circumvent proper budgeting practices, see Florida TaxWatch's annual *Budget Turkey Watch Report*.

beds and evidence-based services for these juveniles. Another \$1.1 million is included for increased community supervision costs and \$4.7 million for prevention programs that target high-risk juveniles.

Another \$24.4 million in increased costs are included for rehabilitation programs, more cameras in corrections facilities, motor vehicles, and several information technology improvements, including a Sexual Predator database and a Data Transparency project in the Department of Law Enforcement and the Department of Legal Affairs agency-wide technology modernization project.

In Justice Administration, the *Outlook* includes an increase of \$3.1 million for due process and conflict case costs such as court reporting, interpreting, expert witnesses and medical/mental health evaluations. Another \$3.4 million is included to fund the expected growth in costs for the state's five Criminal Conflict and Civil Regional Counsels and Capital Collateral Regional Counsels.

In the Judicial Branch, an increase of \$2.7 million is provided for problem-solving courts—such as drug, veterans, mental health, and early childhood courts. These are supported by Florida TaxWatch as a way to reduce recidivism and improve societal outcomes.

Natural Resources (Total Need - \$342.7 GR million)

Critical Needs - None.

High Priority Needs (\$342.7 million GR) - Although there are no additional critical needs identified in Natural Resources in the *Outlook*, significant high priority needs are included, highlighting the increased environmental funding in recent years. Funding of \$170.7 million GR (along with \$283.8 million in trust funds) is provided for water and land conservation. This includes additional GR for Florida Forever (\$10.2 million), Everglades restoration projects (\$25.6 million⁸), land management (\$3.5 million), and St. Johns River/Keystone Heights restoration (\$5.9 million).

Continuing the Governor and Legislature's commitment to funding our water resources, the *Outlook* includes \$109.6 million in each year for water quality improvements, including nutrient reduction, restoration of coral reefs, alternative water supply projects, and the Blue-Green Algae Task Force.⁹

⁸ \$134.8 million in additional trust fund spending on Everglades restoration is assumed.

⁹ Florida TaxWatch, *We Can't Wait on Water: The Restoration and Protection of Florida's Water Resources is an Essential Taxpayer Investment*, January 2020.

The Legislature is expected to continue to fund scores of local water projects, so the *Outlook* includes \$119.8 million for these. Florida TaxWatch reiterates its recommendation to develop a formal, comprehensive competitive selection process for these member projects.¹⁰

Another \$132.9 million is included for a myriad of environmental and agricultural programs including drinking water and wastewater loans, Florida Keys protection, the Florida Resilient Coastlines Program, payments due from citrus canker eradication litigation, agriculture promotion, citrus research, wildfire suppression, and Fish & Wildlife Commission programs. Funding is based on the average of the last three years of appropriations.

General Government (Total Need - \$79.0 million GR)

Critical Needs (\$31.7 million GR) - 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 \$31.5 in the next budget.

A small increase (\$0.2 million) is expected in Non-Florida Retirement System Pensions and Benefits (such as for the Florida Natural Guard and disabled justices and judges).

High Priority Needs (\$47.3 million GR) - GR of \$39.5 million and \$15.8 million in trust funds is included for general repair and maintenance of the state building pool and \$30.0 million (\$7.8 million GR) is provided for other general government activities.

Statewide Issues (Total Need - \$155.9 million)

Critical Needs (\$74.1 million) - State contributions for state employee health insurance are expected to increase by \$213.3 million next year, which will lead to a mid-fiscal year premium increase for agencies of 2.5 percent. This will require \$22.4 million from the General Revenue Fund and \$13.8 million from trust funds to keep the fund solvent. Even greater premium increases are expected to be needed in the next two years. Over the three-year *Outlook* horizon, an additional \$161.1 million will be needed to fund state employee health insurance.

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 from 7.75 percent in 2013 to 7.2 percent in 2019, which requires an increase in contributions. Further reductions are very possible. Based on a three-year average, the *Outlook* includes an increase of \$51.5 million in GR and \$19.5 million from trust funds. The 2020 Annual Actuarial Valuation is not yet available, so these numbers could change significantly.

¹⁰ Florida TaxWatch, *The 2020 Budget Turkey Watch Report: An analysis of the transparency and accountability of the budget process*, June 2020.

The Division of Administrative Hearings handles disputes between the state and others, such as contractors. Assessments are paid by agencies fund DOAH, and these vary. The mix of GR and trust funds used to pay these assessments also varies between agencies. While an additional \$0.2 million in GR funding spending is expected to be needed next year, trust fund spending for DOAH assessments is expected to decrease by \$0.2 million.

High Priority Needs (\$81.8 million GR) - A total of \$89.9 million (\$56.0 million GR) is provided for state employee bonuses and competitive, merit and retention pay adjustments and \$47.9 million (\$25.8 million GR) is provided for critical capital improvements of state buildings.

CONCLUSION

Federal aid has allowed Florida to avoid a budget deficit in FY2019-20 and possibly FY2020-21, but shortfalls in the next three years are anticipated. Moreover, a deficit in the current budget year—ending June 30, 2021—may still develop.

The *Outlook* is a very useful tool, but it is not meant as a blueprint for the next state budget and its estimates are subject to change. There are many factors that impact these forecasts. There will likely be two more rounds of estimating conferences before the 2021 Legislature puts the next state budget together in the Spring. These conferences could significantly change the estimate of available revenue in both directions, as well as estimates for budget drivers such as school enrollment and Medicaid caseloads.

The Outlook's estimates are based on an economic forecast where the bottom of the recession came in April—ending the shortest and deepest recession in U.S. history. A recovery has begun, and it is expected be a modest one through the end of the fiscal year, then pick up steam (with the assumption that a vaccine will be available by early 2021). It estimates that GR collections will be back to pre-pandemic levels in FY2021-22.

The *Outlook* notes that not all economists agree. Some are concerned about the availability of a vaccine being delayed and the possible lack of a future federal stimulus package. Others are predicting a “W” recovery—which would mean another economic contraction is coming—instead of a “V” recovery that assumes the recovery will continue.

There are other significant risks to state’s forecasts. The impact of hurricanes and other natural disasters is a major risk, and the state is currently assessing the impact of Hurricane Sally. Pending litigation against the state, the possible loss of federal Medicaid funds for hospitals, and the potential impact of numerous proposed constitutional amendments are all cited as potential needs for increased expenditures.

In addition, the estimated surplus in FY2020-21 assumes all the CARES Act money can be used for existing appropriations that qualify or that Congress will allow states to use the aid to replace lost revenue, both of which are far from certain. Since all the money is already allocated, any significant new virus response expenses that may arise will also reduce the current surplus and increase the shortfalls estimated by the *Outlook*. It must also be remembered that the state still owes local governments more than \$950 million in CARES Act funds.

The 2021 Legislature will have to take action to address the shortfalls and may have to act to avoid a deficit in the current year. Lawmakers have significant reserves at their disposal. The Budget Stabilization Fund (BSF) contains \$1.674 billion but funds can be withdrawn "... only for the purpose of covering revenue shortfalls of the General Revenue fund or for the purpose of providing funding for an emergency, as defined by general law".¹¹ It cannot be used to prospectively address a potential budget shortfall but could be used if an actual deficit develops in the current year. Withdrawals from the BSF are constitutionally required to be repaid, which would add strain to future budgets. It should be viewed as a last resort.

The Lawton Chiles Endowment, funded by tobacco settlement payments, is also considered part of state reserves. It currently has a balance of \$867.2 million which the Legislature may draw down. There is also a repayment to the Endowment of \$304.7 million scheduled for FY2021-22 which is included in the *Outlook* (see the *Budget Outlook* table on page 5). Repayment is statutorily—not constitutionally—required, so the Legislature could delay or eliminate it.

While Florida TaxWatch usually contends that the \$1.0 billion cash reserve assumed by the *Outlook* is too low, the level of these reserves following the last two recessions were lower than \$1.0 billion. Although cash reserves are even more important during times of economic uncertainty, the Legislature may choose to leave an amount less than \$1.0 billion unappropriated.

The *Outlook* does assume that the Legislature will transfer (sweep) \$312.4 million from trust funds to GR. The Legislature will certainly look closely for available trust fund surplus and could conceivably sweep a larger amount, but the *Outlook* warns surpluses of that magnitude may not be available.

Reserves and trust fund sweeps are possible tools for addressing the shortfalls, but they are nonrecurring fixes which do not help future budgets. The Legislature must focus on reducing the current recurring base budget.

¹¹ Article III, Section 19(g) of the Florida Constitution.

Next session will be even more budget-centric than usual. The Governor has already instituted a 6 percent holdback of agency operational spending (1.5 percent per quarter) to “curtail state agency spending during the upcoming fiscal year to allow for a review and potential reduction of non-essential state services and programs.”¹² This was one of the recommendations in the Florida TaxWatch report *Bringing Florida’s Budget Back from COVID-19*.¹³

Florida TaxWatch encourages the Governor and the Legislature to consider more recommendations from that report, including implementing E-Fairness legislation and negotiating a new gaming compact with the Seminole Tribe. These two actions could provide \$1 billion to \$1.5 billion in new revenue without raising taxes.

¹² Governor Ron DeSantis, HB 5001 Transmittal Letter to Florida Secretary of State, June 29, 2020.

¹³ Florida TaxWatch, “Roadmap for Recovery,” June 2020.

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 Medicaid enrollees is included as a critical need but added services or increased provider payments are not. Historically, maintaining per-student PreK-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. 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 the Legislature will cut taxes (reducing GR) and sweep trust funds¹⁴ (increasing GR). These are usually estimated using the average of the previous three years, although the amount of trust fund sweeps was done differently this year, resulting in smaller than usual number. These two changes 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.

¹⁴ 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 and *The Legislature Must Stop Diverting Affordable Housing Funding*, April 2019.

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