• The purpose of this presentation is to share with you the latest on our state budget.
• I’ll start by sharing some basics about the State budget and detailing our recent challenges on the revenue side.
• I will then talk a bit about how and where demands for spending continue to rise.
• The combined effect of these two forces is less money for programs and projects that you might like.
• Our state is not as bad off as some but we face significant challenges, and those challenges will impact you directly.
• Finally I will review what we have been asked to do as we approach the 2011 general session.
• First, let’s talk about the “colors of money” in the state budget.
• Starting with the light purple color, we project that this year the state will get 17% of its money from the General Fund – that’s sales tax for the most part.
• Next in maroon is a little less than a quarter (23%) from income taxes – individual and corporate.
• Federal funds – regular and “stimulus” – make up the next 27%, followed by gas taxes at 4%, Dedicated Credits – the sale of services – at 7%, and “Other” – largely restricted revenue sources and fees – at 22%.
• That brings us back to General Fund.
• That slice of the pie is the only one that’s truly discretionary. All the rest are dedicated to something.
• Education and Transportation Funds Fund are self explanatory. They’re dedicated in our state constitution.
• Federal Funds go to whatever program the Feds say it’s for – largely Social Services.
• Dedicated Credits and “Other” go to the programs in which they are generated.
This next slide shows where we spend all that taxpayer money.
6% goes to our courts, prisons, and troopers. 38% to Education. 23% to social services like Medicaid. 12% to capital expenses (buildings, debt, and roads). 21% to General Government.
• It’s no secret that our economy has seen better days. And it will see better again in the future. But for now, that means less resources for government services.
• Between FY 2008 and last General Session, the “general tax” portion of that first pie I showed - the General and Education Funds - decreased by more than $1 billion – from $6 billion at its height in 2008 to $4.8 billion now.
• This chart shows the ongoing revenue feeding into those “state” funds.
• The good news is that for the first time since December 2007, we’ve had a revenue report from our economists that doesn’t included downgrades!
• They expect revenue will be as predicted in FY 2011 (+$6m over Feb. 2010 estimates) and grow by about $216 million from FY 2011 to FY 2012.
The bad news is that we’ve committed more than that amount of new revenue to ongoing programs in our current budget. $313 million of our current budget is coming from one-time sources like our Rainy Day funds and from sweeping balances in every corner we can find.

Because those revenues are one-time, and the commitments are ongoing, if nothing else changes, our budget will be $313 short on July 1 of next fiscal year. That’s before the cost of new growth – in areas like public education, medicaid, and retirement.
• You saw on the second slide that Public and Higher Education use 38% of all our resources. They use 100% of income tax, plus nearly $500 million from the General Fund.
• This year, Public and Higher Education will get 65% of our general tax revenue (sales and income taxes).
• Public Education alone will get 50% of General and Education funds.
• This graph shows that we keep having kids. No surprise there.
• We expect our public education rolls to continue rising by 3% per year. That’s 25-30% over the next ten years.
• In typical years, we fund this growth FIRST – in the Base Budget bill – without much debate or acknowledgement.
• Each year, this will cost us between $50 and $100 million depending upon the number of kids and the performance of local property taxes.
• As these kids enter our schools, because we fund them on a per-unit basis, the new costs will require increased general and education fund revenue.
•Next is Medicaid.
•13 years ago, Medicaid accounted for 6% of all of our General & Education Funds.
•This year, it’s 9%.
•By FY 2010 without federal health care reform, Medicaid is projected to use 13% of all General and Education Funds.
•And if we can’t bring medical costs down, Medicaid’s share of our budget will continue to grow exponentially.

•Notes
•Medicaid growth based on average annual growth of 8% based on experience of FY 1999 through FY 2010
•General and Education Fund growth based on a conservative (low range) estimate of revenue growth
• Then there’s retirement.
• This state has prided itself on covering its retirement commitments.
• Just a few years ago, we were 100% funded.
• Given recent market performance, without further reform, we will need to increase contribution rates to 22.4% of salary in order to be actuarially sound.
• That’s a cost increase of nearly 70% in the next four years. It will cost us $316 million more in that timeframe.
• It’s a nearly 16% increase next year.
The Hole Defined
in Millions

<table>
<thead>
<tr>
<th>Spending</th>
<th>Revenue</th>
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</thead>
<tbody>
<tr>
<td>Structural Deficit = $313</td>
<td>FY 2012 = $216</td>
</tr>
<tr>
<td>2012 School Kids = $80</td>
<td></td>
</tr>
<tr>
<td>2011 School Kids = $70</td>
<td></td>
</tr>
<tr>
<td>Medicaid/CHIP = $91</td>
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<tr>
<td>Retirement = $41</td>
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<tr>
<td>Health Insurance = $38</td>
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<tr>
<td>Bond Coverage = $15</td>
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<tr>
<td>Settlements = $5</td>
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<td><strong>TOTAL = $653</strong></td>
<td><strong>Difference</strong></td>
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• Add to those big ticket items health insurance, double coverage on build America bonds, and payment of lawsuit settlements, and you have $653 million in needs.

• Versus $216 million in revenue growth.

• Leaving $437 million to fill or go without.
• We have some money in our rainy day funds to help cover that $653 million.

• But, it’s not enough to cover the whole thing. We only have $210 million in reserve.

• And it’s one time – meaning that if we use it to cover ongoing costs in FY 2012, we’ll face the same problem in FY 2013.

• Dealing with these numbers will be one of the major decisions to be made by the Legislature in the 2011 session.
Where do we go from here?

EAC motion, 12/14/10:
“Prepare and number a base budget bill equal to ongoing state funds in the current year, adjusted to a level that eliminates the structural deficit.”
$313M structural deficit = 7%

• In its last meeting, the Executive Appropriations Committee adopted a motion to have staff prepare a base budget bill equal to ongoing state funds in the current year, adjusted to a level that eliminates the structural deficit.
• Eliminating the $313M structural deficit translates to an adjustment of 7%.
• The next two slides show how we plan to meet the requirements of legislative rules with the base budget bill.
• Rules require a base budget bill (or bills) on your desks by the morning of the first day of session.
• The introductory bill will simply reduce all budgets across the board by 7%.
• However, as the subcommittees do their work, the bill will change to include more surgical cuts.
Where do we go from here?
Timeline

JR4-5-201:
By noon on the tenth day, but not before the third day, the Legislature shall either pass or defeat each base budget bill.

Action:
Subcommittees discuss specific changes on Jan. 19, and 2 or 3 more meetings during session. Bill substituted with surgical changes by the tenth day.

• Rules require the base budget bill (or bills) to be acted upon by the 10th day of session.
• This gives subcommittees the meeting on the 19th, plus 2 or 3 more during the session, to replace the across-the-board cuts in the introductory bill with surgical cuts.
• This leaves the remaining meetings of the general session to discuss changes to the base budget, including potential add-backs, fees, intent language, projects, and so forth.