

# Report of the Legislative Budget Committee to the 2017 Kansas Legislature

**CHAIRPERSON:** Senator Ty Masterson

**VICE-CHAIRPERSON:** Representative Ron Ryckman, Jr.

**OTHER MEMBERS:** Senators Jim Denning and Laura Kelly; and Representatives Jerry Henry, Marvin Kleeb, and Sharon Schwartz

## **CHARGE**

The Legislative Budget Committee is statutorily directed to compile fiscal information and to study and make recommendations on the state budget, revenues, and expenditures and the organization and functions of the State, its departments, subdivisions, and agencies with a view of reducing the cost of state government and increasing efficiency and economy.

HB 2739 (2016) established the Budget Stabilization Fund within the State Treasury as of July 1, 2017, and directed the Legislative Budget Committee to meet for up to ten days between the 2016 and 2017 Legislative Sessions to study and review policies concerning transfers to and expenditures from the Budget Stabilization Fund. The review by the Legislative Budget Committee was to include, but not be limited to:

- Analyzing risk-based budget stabilization practices in other states;
- The appropriate time period over which to analyze State General Fund revenues and expenditures;
- Which entity should certify the reserve amount necessary in the Budget Stabilization Fund;
- Sources of funding for the Budget Stabilization Fund;
- The appropriate level of risk of exhausting the balance within the Budget Stabilization Fund during an economic downturn; and
- The circumstances under which money could be withdrawn from the Budget Stabilization Fund.

# Legislative Budget Committee

## ANNUAL REPORT

### Conclusions and Recommendations

Following its review and discussion, the Committee made no recommendations.

- *Proposed Legislation:* None

### BACKGROUND

The Legislative Budget Committee is statutorily directed in KSA 46-1208 to compile fiscal information. It also is directed to study and make recommendations on the state budget, revenues, expenditures, and on the organization and functions of the State, its departments, subdivisions, and agencies with a view of reducing the cost of state government and increasing efficiency and economy.

### COMMITTEE ACTIVITIES

The Committee met December 16, 2016, to review fiscal information regarding revenues and expenditures and to specifically discuss the revenue estimates and what components comprise the state tax revenue and human services caseloads estimates; receive an update on Kansas Public Employees Retirement System (KPERS) valuation; review the Kansas Efficiency Study recommendations progress; review the Department of Corrections facility closure; receive an update on performance-based budgeting; and review information related to the establishment of a Budget Stabilization Fund in accordance with 2016 HB 2739 (KSA 2016 Supp. 75-6706).

#### State Budget, Revenues, and Expenditures

#### Consensus Revenue Estimates for FY 2017, FY 2018, and FY 2019

Kansas Legislative Research Department (KLRD) staff presented an overview of the

projection of State General Fund (SGF) receipts for fiscal year (FY) 2017, FY 2018, and FY 2019. Staff noted most major economic variables and indicators have been adjusted downward since the Consensus Group had last convened in April 2016. For FY 2017, the revised estimate is 5.5 percent below the previous forecast; the revised estimate for FY 2018 is 7.4 percent below the revised forecast for FY 2017. Staff noted Kansas personal income has been growing more slowly than U.S. personal income since the first quarter of 2014 and that trend is expected to continue. The Kansas Department of Labor reports job growth has been stagnant since early 2015. Staff noted a great deal of uncertainty about the future of U.S. foreign policy, trade policy, health policy, immigration policy, and tax policy has already shown signs of increasing volatility in global and domestic markets. The impact of any such increased volatility on confidence, as well as consumption and investment decisions by consumers and businesses alike, will be monitored by the Consensus Group over the winter prior to the next meeting in April.

Staff stated the consensus revenue estimates will be further adjusted in mid-April prior to the conclusion of the 2017 Legislative Session.

#### Human Services Caseloads

KLRD staff explained the human services caseload impacts detailed in the Fall 2016 Human Services Consensus Caseload Estimates for FY 2017, FY 2018, and FY 2019.

The estimate for FY 2017 is an increase of \$147.0 million from all funding sources and \$1.9 million from the SGF as compared to the budget approved by the 2016 Legislature. (The approved amount reflects the Governor's May 2016 allotments.) The estimate for FY 2018 is a decrease of \$120.4 million from all funding sources and an increase of \$35.3 million from the SGF above the FY 2017 revised estimate. The estimate for FY 2019 is an increase of \$48.4 million from all funding sources and \$165.8 million from the SGF above the FY 2018 estimate.

#### ***FY 2017***

For FY 2017, the revised estimate for all human services caseloads is an all funds increase of \$147.0 million and an increase in SGF expenditures of \$1.9 million above the budget approved by the 2016 Legislature.

The estimate for the Temporary Assistance for Needy Families program is an increase of \$255,000, all from federal funds, above the approved amount. The number of individuals receiving cash assistance benefits is still expected to decrease compared to the number in the previous fiscal year, just not as quickly as had been anticipated in the spring estimate. Estimated expenditures for the Foster Care program were increased by \$4.9 million, including \$4.0 million from the SGF, above the approved amount. The number of children served is growing slower than anticipated, and the cost per child is expected to be higher than was anticipated in the spring.

The FY 2017 estimate for KanCare Medical is \$2.7 billion from all funding sources, including \$889.5 million from the SGF, reflecting an increase of \$130.1 million from all funding sources and a decrease of \$6.6 million from the SGF from the amount approved by the 2016 Legislature. The KanCare Medical estimate includes Kansas Department of Health and Environment, Kansas Department for Aging and Disability Services, and Kansas Department of Corrections KanCare medical expenditures. The estimate includes an all funds addition of \$93.5 million, including \$41.0 million from the nursing facility quality care assessment, due to the enactment of 2016 Senate Sub. for HB 2365.

#### ***FY 2018***

The FY 2018 estimate is \$2.8 billion from all funding sources, including \$1.0 billion from the SGF. The estimate is an all funds decrease of \$120.4 million and an increase in SGF expenditures of \$35.3 million above the FY 2017 revised estimate. The federal Medicaid matching rate determined by the federal Centers for Medicare and Medicaid Services increased the required state share (commonly referred to as FMAP [federal medical assistance percentages]) by 1.04 percent between FY 2017 and FY 2018, with an estimated impact of approximately \$27.0 million in additional SGF expenditures.

The estimate for the Temporary Assistance for Needy Families program is a decrease of \$814,289, including \$185,477 from the SGF, below the amount estimated for FY 2017. The number of individuals receiving cash assistance is expected to continue to decrease. Estimated expenditures for the Foster Care program were increased by \$4.1 million, including \$3.5 million from the SGF, above the FY 2017 estimate based on increased numbers of children served.

The FY 2018 estimate for KanCare Medical is \$2.6 billion from all funding sources, including \$925.0 million from the SGF. The estimate is an all funds decrease of \$114.9 million and an increase in SGF expenditures of \$35.5 million from the FY 2017 revised estimate.

The SGF increase is largely attributable to the state share (FMAP) increase and a scheduled increase in Medicare buy-in payments. The all funds decrease is due to a federal suspension of health insurance provider fee payments decreasing KanCare expenditures by \$53.9 million, including \$23.6 million from the SGF. A decrease is expected to be seen in the member population due to the elimination of the eligibility determination backlog and the managed care organization (MCO) privilege fee reduction from 3.31 percent to 2.0 percent, effective January 1, 2018.

#### ***FY 2019***

The FY 2019 estimate is \$2.9 billion from all funding sources, including \$1.2 billion from the SGF. The estimate is an all funds increase of \$48.4

million and an increase in SGF expenditures of \$165.8 million above the FY 2018 estimate.

The estimate for the Temporary Assistance for Needy Families program is a decrease of \$940,711, including \$12,581 from the SGF, below the amount estimated for FY 2018. The number of individuals receiving cash assistance is expected to continue to decrease. Estimated expenditures for the Foster Care program were increased by \$6.9 million, including \$5.8 million from the SGF, above the FY 2018 estimate. The number of children to be served in the foster care system is expected to continue to increase.

The FY 2019 estimate is higher than the FY 2018 estimate by \$42.4 million from all funding sources and \$160.0 million from the SGF. The increase is largely attributable to the MCO privilege fee continuing at the reduced 2.0 percent rate for the entire fiscal year. Under current law, the funds from the privilege fee move from being deposited in the Medical Assistance Fee Fund back to the SGF in FY 2019. In addition, health insurance provider fee payments suspended in FY 2018 will be reinstated in FY 2019, which will increase KanCare expenditures by \$72.4 million, including \$32.5 million from the SGF.

### **Expanded Lottery Act Revenue Fund**

KLRD staff presented an overview of the Expanded Lottery Act Revenue Fund (ELARF) for FY 2016 through FY 2019. Staff explained the reduction of expenditures in FY 2017 is attributable to a reduction in debt service. The FY 2017 estimate for ELARF gaming revenues was reduced downward by roughly \$2.3 million as a result of the Fall 2016 Gaming Revenue Consensus Estimate.

Staff further explained a balance of roughly \$10.9 million is projected to be carried forward from FY 2018, as there is no law governing the transfer of the ELARF ending balances beyond FY 2017.

### **State General Fund Profile**

KLRD staff provided an overview of the SGF Profile for FY 2015 through FY 2019. Staff noted the reduction in expenditures needed to maintain a zero ending balance on June 30, 2017, is \$349.1

million; on June 30, 2018, is \$582.6 million; and on June 30, 2019, is \$172.3 million.

### **Review of Kansas Efficiency Study**

Legislative Division of Post Audit staff provided an update on the August 2016 progress report on the Alvarez and Marsal efficiency recommendations prepared for the Legislature. Staff stated the Legislative Division of Post Audit is monitoring the State's progress in addressing and implementing the recommendations in the February 2016 Alvarez and Marsal efficiency study report. Staff also noted, in preparing the progress report, each agency was contacted and asked to provide information on the Alvarez and Marsal recommendations that affected the agency. The report characterized the 105 Alvarez and Marsal recommendations in five categories: 1) fully implemented; 2) partially implemented; 3) in progress; 4) not started; and 5) no action.

Staff indicated the agency plans to provide another follow-up on the recommendations and report back to the Legislature in February 2017. The Committee requested Post Audit provide an update at that time on total savings achieved by recommendation implementation.

### **Review of KPERS Valuation**

KPERS staff reviewed the 2015 actuarial valuation, which is a snapshot of the financial condition of the Retirement System as of December 31, 2015. The actuarial valuation of system assets, which includes the \$1.0 billion proceeds of the pension obligation bonds issued in 2015, was estimated to be \$17.409 billion. Staff reported the funding status has improved for four membership groups (KPERS state, school, and local groups and the Judges' Retirement System). The funded ratio for the Kansas Police and Firemen's Retirement System decreased by 10 basis points to 74.0 percent. The unfunded actuarial liability for the entire system decreased in 2015 by \$929 million, leaving \$8.539 billion remaining to be funded. The funded ratio increased from 62.3 percent in 2014 to 67.1 percent in 2015. Legislative reforms enacted in 2012, including increased employer and employee contributions, will continue to improve funding. Assuming all actuarial assumptions are met in the

future, KPERS will be fully funded at the end of the amortization period in calendar year 2033.

Staff also presented information on the revised actuarial assumptions adopted by the KPERS board. The Committee was informed the presumed rate of return for the System's investments has been revised down from 8.00 percent to 7.75 percent, in addition to other revised assumptions. Taken as a whole, the revised assumptions are projected to increase actuarial recommended employer contribution rates, above what otherwise would have been recommended, beginning in FY 2020. There was Committee discussion of the "layered amortization" the KPERS board has endorsed for the actuarial effects of the revised assumptions.

### **Review of Corrections Facility Closure**

Staff from the Department of Corrections presented a review of corrections facility closures. Staff explained the Department was in the process of moving inmates from the Larned Juvenile Correctional Facility to the Kansas Juvenile Correctional Complex in Topeka. Staff noted housing units are being closed as the population shrinks. In addition, no capital outlay improvements are being considered for the facility. Staff indicated current staff at Larned are being hired at other facilities if possible and additional training will be provided where necessary. Staff noted a workforce is being maintained at Larned Juvenile Correctional Facility, responsible for the security of the facility. In addition, utilities are being maintained at the level needed.

The Committee expressed concern that inmates are being moved away from their families or home area. Staff stated some families are being involved in the relocation process.

### **Performance-Based Budgets**

KLRD staff presented an update on the performance-based budget process established in

accordance with enacted 2016 HB 2739. Staff explained the Legislature retained the services of Alvarez and Marsal to examine several areas of state operations and spending, including a review of the state budget process. Staff noted HB 2739 requires the State to begin the implementation of performance-based budgeting (PBB). Staff indicated PBB differs from the current budget process in Kansas by emphasizing performance measures and, to the extent possible, creating correlations between dollars, outcomes, and objectives.

Staff noted Phase I of the performance-based budgets will be completed by January 9, 2017, and available to legislators to review along with other budget documents and the Governor's recommendation.

### **Rainy Day Fund**

KLRD staff provided an overview of a rainy day fund. Staff explained enacted 2016 HB 2739 created the Budget Stabilization Fund (KSA 2016 Supp. 75-6706) and called for the Legislative Budget Committee to identify and recommend deposit rules, withdrawal provisions, and policies to calculate the appropriate risk-based balance for the Fund.

Staff provided information concerning funding for the Budget Stabilization Fund, including how other states secure funding, how funds are expended from the budget stabilization fund, and how a risk-based balance is calculated.

Staff noted the Alvarez and Marsal 2016 report recommends such a fund and states Kansas would need to establish deposit rules, withdrawal rules, and the size of the fund.

## **CONCLUSIONS AND RECOMMENDATIONS**

The Committee made no recommendations to report to the 2017 Legislature.