



Commonwealth of Virginia
Office of Governor Bob McDonnell

October 1, 2013

MEMORANDUM

TO: Executive Branch Agency Heads

CC: Cabinet Secretaries

FROM: Martin L. Kent, Chief of Staff

SUBJECT: Budget Savings

Once again, let me thank you on behalf of the Governor, for all of your effort and diligence to make Virginia an effectively and efficiently managed state. Your success continues to be borne out by the surplus balances you generate each year and by recognition from external groups such as Forbes.com selecting Virginia as the “Best State for Business.”

As we have begun to review the budget requests submitted by agencies, it has become increasingly apparent that the many critical needs of our state will have to be met with what may be increasingly limited resources. The first quarter’s revenue collections lack the certainty that we are headed toward a solid economic recovery. In fact, the signals are mixed as we see the effects of federal sequestration.

Adding to that uncertainty, we have yet to see what action the federal government will take in order to control spending and balance its budget. This lack of leadership and responsibility in Washington has gone on for so long now that Congress and the President have allowed the beginning of the new federal fiscal year to come without the passage of a budget or a continuing resolution from which appropriations would be authorized to continue federal programs.

Impact on Federal Programs

Effective today, there is no new federal appropriation authority [for federal fiscal year (FFY) 2014] to continue spending for federal programs and there will be none until Congress and the President approve a new budget or another continuing resolution. This failure by the federal government has two levels of impact. The first is on mandatory federal programs and the second is on discretionary federal programs. It is our understanding that mandatory programs are authorized to continue to operate without an appropriation; however, the lack of an FFY 2014 budget results in a lack of knowledge about what level of spending will ultimately be authorized.

It is also our understanding that discretionary programs are not allowed to continue spending or incurring new obligations. These provisions deal with new FFY 2014 spending authority and not with continued spending that is allowed against unspent prior year authorizations. I have previously issued guidance on how to deal with these issues and I have asked the Department of Planning and Budget (DPB) to survey you for the impact they have on your respective agencies relative to the lack of new spending authority and a partial government shutdown. It is vitally important that you contact your federal cognizant agency to obtain specific information about how your programs will be impacted.

Impact on State Programs

It is our responsibility as leaders of state government to react and plan accordingly for how the continued federal budget actions or inactions will impact state general fund revenue and thus state funded programs. Even though we have reported surpluses for FY 2013, there are a number of standing commitments against those balances. Moreover, experience has taught us that we cannot assume that future revenue growth will be sufficient to meet the increase in program costs required by federal mandates and other budgetary pressures over the next biennium, given the present economic uncertainty.

There are several examples that help illustrate this point. First, state obligations for key programs such as public education and increased payments to the state's retirement system must be addressed. To give you a sense of the challenge ahead, the Board of Education has just approved a rebased budget for the Standards of Quality and other public education programs at a price tag that exceeds \$350 million in the next biennium. Further, the next phase of rate increases aimed at addressing the unfunded liabilities in the Virginia Retirement System for state employees and teachers will exceed \$330 million in general fund cost in the next biennium.

Also, because of the federal government's actions and just as a matter of experience, we expect to see large increases in general fund cost in the Medicaid program. The uncertain advance of healthcare reform and the possibility of a sluggish economy likely will result in significant growth in this program area. Other spending needs, including mental health issues, economic development to foster job creation, higher education, and public safety, will also require attention in the introduced budget.

Accordingly, as we face these uncertain times, we must prudently prepare for the future. To that end, the Governor is directing two courses of action to identify potential savings in the state's

budget. First, he is assembling work groups to develop proposals for targeted savings strategies in selected programs such as higher education, public education, and Medicaid. For all other programs in the Executive Branch, he is asking each agency to prepare savings strategies for FY 2014 equivalent to two (2) percent of its FY 2014 adjusted general fund appropriation. Likewise, the Governor is asking each executive branch agency to prepare savings strategies for FY 2015 and FY 2016 equivalent to four (4) percent of its adjusted general fund base appropriation for the 2014-2016 biennium. DPB will issue specific guidance relative to these adjustments, any exemptions that might be permitted, and the final specific savings targets for each agency later this week.

Just as you have been requested in the past, these savings plans should focus on identifying the lowest priority activities in your respective agency. You should also focus on savings you anticipate obtaining through your ongoing efforts to restructure internally to drive down administrative costs and to deliver programs more efficiently. You should examine statutory mandates that are outdated and should be eliminated.

You should specifically look at service and program areas where we spend state funds that match federal funds or other nongeneral funds. You need to ask if the use of these funds, state and federal, is achieving outcomes that are of the highest priority for use of the general fund match. You should not exclude these programs from savings and efficiency strategies just because they may result in the loss of matching funds. As we have seen, there is no guarantee that these matching funds can be continued in the future.

Please be certain to look at the actions taken last fiscal year that may have allowed you to end the year with a significant general fund balance. Whenever possible, you should continue those positive savings actions.

Please do not count savings actions that will reduce payments to other state agencies or have a negative financial impact on other state programs; however, we are very interested in any ideas you may have that could reduce statewide costs, so please communicate these to your DPB analyst. For instance, if you are a recipient of state funds from another agency and believe that the program being funded is not efficient or productive, that would be helpful to know.

Do not hesitate to suggest program or service eliminations even if they are required by current state law. Any required changes to state law will be proposed if the reduction plan is adopted. The Governor expects your very best input and he knows that this is not going to be easy to accomplish given the previous rounds of savings actions that already have been taken. Keep in mind, however, that he will consider every strategy suggested and he does not want strategies that are unworkable or unachievable.

While I recognize that it may be necessary to employ some one-time savings strategies, please try to limit these to FY 2014. Savings strategies for FY 2015 and FY 2016 should reflect more permanent savings. It is important to remember that all one-time savings strategies will have to be replaced with ongoing savings in future years including the next biennium. You should not assume that one-time savings will be replaced at any point in the future. It will be assumed that if you propose a one-time strategy in FY 2016, you know that your base appropriation going

forward will be permanently reduced so you will be required to find additional savings from other actions going forward.

Finally, please ensure that your recommendations are both practical and consistent with known priorities or directives of the Governor. If you have questions about this requirement, please discuss them with your respective Cabinet Secretary. To the extent an agency submits a savings strategy that does not meet these criteria, the Governor may reduce that agency's base appropriation after consultation with the DPB and your respective Secretary.

Please note institutions of higher education are exempt from submission of savings plans outlined in this memo. A separate analysis and approach will be developed for them and addressed in a separate communication should it be necessary.

Your specific agency targets for the savings plans will be available in the DPB performance budgeting system later this week. Your final plans must be submitted in DPB's performance budgeting system and are due no later than Monday, October 21, 2013*. This timeframe is necessary so that the Governor has sufficient time to appropriately evaluate these strategies for inclusion in his budget to be submitted in December, should such savings become necessary. (NOTE: These plans will be considered official budget submissions and, as such, will be sent to the General Assembly within five (5) days of receipt by DPB. They will also be available to the public and media.)

Thank you very much for your continued efforts in governing the Commonwealth through these most difficult economic times. Your previous actions have enabled us to live within our means and to ensure funding for the continued operation of state government. The Governor and I appreciate your service to the public and your continued support to make Virginia the best place to live and work. You make the difference and the Commonwealth is blessed to have you on its management team.

*note: date corrected from original