OVERVIEW

Governor Kaine's 2010-2012 introduced budget bill reflects a Commonwealth facing continued fiscal challenges. Although the national economy is beginning to show signs of emerging from the recession and Virginia unemployment numbers have dropped from their midyear peak, families across the Commonwealth still face uncertain economic times and worry about what the future holds.

Like families and businesses statewide, Virginia government is doing what it must in times like these – tightening its belt, examining every expenditure, and taking care of the basics.

This budget projects very modest growth over the next two years. It is built on a cautious, responsible forecast, yet one that is more hopeful than the two consecutive years of revenue contraction that occurred in FY 2009 and FY 2010.

While the 2008-2010 biennial budget proved challenging, the state's leadership rose to the occasion. A series of early, proactive steps to address potential shortfalls kept Virginia's budget in balance and won praise from bond rating agencies, who reaffirmed the Commonwealth's AAA status in 2009.

In the last biennium, Virginia benefited greatly from the American Recovery and Reinvestment Act of 2009 (ARRA) that was approved by Congress and the President.

ARRA funds helped the Commonwealth avoid even more painful cuts to education, health care, and public safety. Federal funds prevented layoffs of teachers and police officers while protecting the health care safety net.

In the 2010-2012 biennium, Virginia can no longer rely on the ARRA. This budget

proposal brings the Commonwealth's budget into balance in FY 2012 without using any stimulus funds, making Virginia the first state to reach that milestone.

It is not unusual for Virginia to be first, though. Standard and Poor's said that "the Commonwealth's strong financial management focus is evident in its early and active response."

Throughout the downturn, Virginia has remained one of only seven states to hold a AAA bond rating, and the Commonwealth has consistently been rated the Best State for Business, with CNBC describing Virginia as the state "most likely to emerge from an economy turned upside down."

Balancing the budget without stimulus funds in FY 2012 requires difficult cuts. Leading up to this budget proposal, the declining revenues of the past few years have already required strategies to cover more than $7 billion in shortfalls. In fact, the revenue forecast for FY 2012 is for fewer general fund dollars than in FY 2007.

<u>Making Education a Priority</u>

Education is one of the Commonwealth's highest priorities and most important responsibilities. As such, K-12 education has largely been spared in all the previous rounds of budget cuts, thanks in part to federal stimulus dollars. However, as stimulus funds run out, even K-12 will be affected by the worst economic crisis in a generation. This budget makes a series of strategic, targeted cuts to K-12 that are designed to create savings while having as little impact on the students in the classroom as possible.

The introduced budget continues a policy change suggested by the Governor and approved by the General Assembly last year. The budget supports a ratio for funding of administrative and support staff in local school divisions, consistent with a ratio for teachers and instructional staff that already exists. The Board of Education has announced that they intend to continue to study and refine the strategy in the future, creating different ratios for different categories of administrative and support staff.

The budget also amends the current approach of funding localities for health insurance for all school personnel, regardless of whether the insurance is provided. This budget proposes to only provide funds to localities for employee health insurance for those employees who actually are insured through the locality.

In addition, in order to give local school divisions more certainty in a challenging time, the budget proposes delaying the scheduled change in the composite index of local ability to pay for a year, until FY 2012.

Higher Education

The introduced budget spares higher education from the most challenging cuts in FY 2011 because of the availability of federal stimulus dollars, but by FY 2012, the budget provides fewer general fund dollars to higher education than in FY 2006.

Virginia's colleges and universities are reducing expenditures and making cuts, and recent budgeted increases in student financial aid will provide some protection to students from cost increases. However tuition costs will likely rise in this biennium.

Public Safety

Some of the most difficult cuts necessary to balance this budget come in public safety.

The Department of State Police will postpone new trooper schools, saving money but making it more difficult to fill vacancies as current troopers retire or leave the service.

Local sheriffs' departments will face cuts over sixteen percent, which may require layoffs on the local level to keep their own budgets in balance. Cuts to local Commonwealth's Attorney's offices also exceeds sixteen percent. Circuit Court Clerks have similar reductions.

Local police departments funded through the House Bill 599 formula will also receive a reduction similar in scale to sheriffs' deputies.

The Department of Corrections, now Virginia's largest state agency, will move forward with the closing of facilities in Botetourt and Brunswick.

Health Care

Among the greatest challenges in this budget is preserving the safety net for those citizens who are most vulnerable in these economic times. Yet the depth of the revenue shortfall requires cuts even to these programs.

One of the most important elements of the federal recovery package was increased funding for Medicaid. The current economic downturn has resulted in dramatic growth in the number of Virginians who are eligible for Medicaid, and the stimulus was critical in helping Virginia maintain services to a larger population. However, that money will not be available beginning in early FY 2011, and health care for needy Virginians will be affected.

Overall, Medicaid expenditures are projected to require an additional $778 million from the general fund in response to rising caseloads and costs in the weak economy. In an effort to control rising costs, this budget proposes offsetting reductions of $419 million from the general fund by limiting services to individuals and reimbursements to health care providers.

The introduced budget calls for the freezing of some waiver programs – Intellectual Disabilities, Developmental Disability, Day Support, Elderly and Disabled, and Alzheimer's waivers – which will leave many people on waiting lists until the programs can be reopened.

Some Medicaid services have been reduced or eliminated in FY 2012, including limits on physical, occupational, and speech therapy, and new lower limits on hours for respite care.

And many health care providers will see freezes or even reductions in state payments for serving Medicaid patients.

The Virginia Department of Health will reduce support to their non-state partners in providing a health care safety net, such as the free clinics and the Virginia Health Care Foundation.

At the same time, programs supported by the Department of Social Services with Temporary Assistance for Needy Families (TANF) funds will be reduced and/or eliminated. Due to increased spending on mandated programs, optional TANF expenditures ranging from homelessness assistance to teen pregnancy prevention had to be cut.

State Employees

The introduced biennial budget does not propose a pay increase for state employees in either year. However, there are no additional furlough days proposed beyond the single day previously announced for FY 2010.

In addition to the 593 layoffs included in the Governor's September Reduction Plan for FY 2010, this budget proposes savings actions that will result in 664 layoffs in 2010-2012 biennium. Also, the introduced budget includes the elimination of nearly 1,900 vacant positions. The agencies impacted the most are the Departments of Transportation, Behavioral Health and Development Services, Corrections, and Juvenile Justice and the University of Virginia.

Another change to state employee compensation brings the Commonwealth more in line with other major employers. Currently, the Commonwealth pays both the employer share and the employee share of retirement contributions. Beginning in FY 2011, state employees will be required to pay one percent of salary as their share of the total contributions required for membership in the VRS defined benefit retirement program. This will increase to two percent of salary in FY 2012.

Transportation

Virginia's transportation budget is supported mostly by nongeneral fund revenue. The Governor's introduced budget reflects the continuing downward changes in the revenue forecast for transportation.

The Virginia Department of Transportation (VDOT) continues to reduce central office staff and streamline operations around the state to respond to the reduced revenue forecast. VDOT is in the process of reducing agency employment to 7,500 employees after having once had as many as 10,600.

The Commonwealth Transportation Board continues to revise the Six Year Plan to balance proposed construction and maintenance expenditures against proposed revenues. Because maintenance of current infrastructure takes priority, there is now almost no revenue for new construction in the six year plan.

Growing the Economy

The economic future for Virginia citizens depends on continuing to attract new businesses and new jobs to the Commonwealth. The Governor's budget proposal recommends continuing to invest in job creation through the Governor's Opportunity Fund, the Virginia Investment Partnership program, and the Major Eligible Employers grant fund.

The budget fulfills our commitments to major new investors in Virginia like Rolls Royce, SRI, and the IGNITE Institute.

Local Government

The budget proposal includes a structural reform in the area of local finance. Given that local Commissioners of Revenue and Treasurers administer local taxes, the budget proposes that the funding responsibility for these offices belongs to local rather than state government. A companion proposal to the budget bill will reduce the assessment workloads for Commissioners of Revenue and provide an additional funding source for local governments in the future.

Language in the introduced budget bill also encourages localities to consolidate functions and look for opportunities for savings.

Overall, state aid to localities is reduced by $2.6 billion, through cuts in education, public safety, and other programs.

Delivering on a Promise

The cuts that have been required in this budget proposal and in previous rounds of budget balancing have been painful. Virginia has gone well beyond finding efficiencies and doing more with less, and have had to make cuts in programs that directly affect Virginians' lives.

Even after taking actions to save $7 billion over the past three years, and making another $2.3 billion in difficult cuts to programs and services in the introduced budget, a significant shortfall would remain. Additional cuts to law enforcement, to schools, or to health care at this point are both untenable and against the interest of citizens of the Commonwealth.

Therefore, the introduced budget proposes ending the $950 million annual subsidy to local governments for personal property tax relief.

Since the subsidy was first proposed twelve years ago, the incomplete car tax relief program has been a point of contention among both legislators and local governments – and has remained a point of concern among budget writers and bond rating firms alike.

A companion bill to the budget bill proposes delivering on the unfilled promise of more than a decade ago by eliminating the car tax on personal vehicles once and for all.

The companion bill provides a new, dedicated source of local revenue through a 1 percent income tax surcharge, phased in over two years.

Together, the budget action and the companion bill provide structural stability for both state and local government budgets, remove the budget questions about the future of a promise half-kept, and finally eliminate the car tax in Virginia.

Fiscal Stability – A Virginia Tradition

The Governor's budget proposal provides a blueprint for a balanced budget that is not dependent on stimulus dollars or one-time items. It relies on difficult, but necessary and responsible decisions about prioritizing the services that the Commonwealth provides to its citizens. It adheres to Virginia's tradition of sound long-term fiscal policy, and it protects Virginia's AAA bond rating and reputation.

Throughout the past four years, Virginia's government has worked proactively to make the budget adjustments necessary during the recession. Because of that, Virginia is in a better position than most states as we come out of the recession and begin to grow again.

While other states wrestle with much greater shortfalls this year, and will spend years wrestling with the legacies of short-term strategies and one-time fixes, the Governor's 2010-2012 introduced budget gives Virginia a firm foundation on which to build for the future.