

27r1

# Budget and Compensation Reserves

(LFB Budget Summary Document: Page 117)

## LFB Summary Item for Which an Issue Paper Has Been Prepared

Item #

Title

1

Required General Fund Statutory Balance (Paper #240)

**Gov Agency:** Budget & Compensation Reserves - Required General Fund  
Statutory Balance

**Recommendation:**

**Paper No.** 240      **Alternative:** 2

**Comments:**

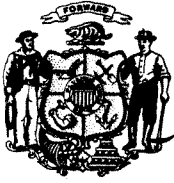
Approves the Governor's recommendation to increase the statutory balance to 1.1% in 2000-01 but deletes reference to future increases in the percentage.

The current 1% balance is inadequate as a reserve to guard against possible economic downturns. Most states have a budget balance far larger than Wisconsin's and bond rating agencies look at the state's budget reserves as a key point in rating state bonds. Increasing the reserve also helps to limit any short-term borrowing that must be done to meet cash demands.

This alternative gives future legislatures the flexibility to determine the appropriate compensation reserve percentage appropriate for that biennium.

**Prepared by:** Deb

A1 + 4uf  
Gard - ~~assent~~ 2 fails  
~~assent~~



## Legislative Fiscal Bureau

One East Main, Suite 301 • Madison, WI 53703 • (608) 266-3847 • Fax: (608) 267-6873

June 7, 1999

Joint Committee on Finance

Paper #240

### Required General Fund Statutory Balance (Budget and Compensation Reserves)

[LFB 1999-01 Budget Summary: Page 117, #1]

#### CURRENT LAW

Under s. 20.003(4) of the statutes, "No bill directly or indirectly affecting general purpose revenues ... may be enacted by the Legislature if the bill would come cause the estimated general fund balance on June 30 of any fiscal year...to be an amount equal to less than one percent of the total general purpose revenue appropriations for that fiscal year plus any amount designated as "Compensation Reserves" for that fiscal year..."

#### GOVERNOR

Beginning with the 2000-01 fiscal year, increase the 1% statutory reserve requirement as follows:

<u>Fiscal Year</u>	<u>Percent</u>
2000-01	1.1%
2001-02	1.2
2002-03	1.4
2003-04	1.6
2004-05	1.8
2005-06 (and thereafter)	2.0

## DISCUSSION POINTS

1. The 1% statutory balance was enacted in Chapter 1, Laws of 1981, and became effective in the 1983-85 biennium. The provision was enacted in response to the recession of the early 1980s and was an effort to ensure that some cushion was available in the general fund in times of economic downturn or fiscal uncertainty.

2. As originally enacted, the 1% applied to total GPR appropriations for the biennium (rather than annually as under current law). The provision was applied to the second fiscal year of the biennium. Since its original adoption, three changes have been made to the provision.

- Due to a projected budget shortfall in 1986-87, a session law provision of 1985 Act 120 waived the 1% requirement for the 1985-87 biennium and set the statutory balance at a specific dollar amount (\$26.5 million below what would have been required had the 1% been in effect).

- In his 1987-89 budget submission, Governor Thompson recommended that the provision be modified to set the statutory balance at 1% of appropriations in each fiscal year rather than for the biennium. This was adopted by the Legislature and enacted in 1987 Act 27. Under this change, the required balance for 1987-88 was \$53 million and for 1988-89 was \$55 million. Had the change not been made, the statutory balance at the end of the biennium (1988-89) would have been \$108 million -- 1% of biennial (rather than annual) appropriations. Thus, the change contained in 1987 Act 27 reduced the required balance for the biennium by one-half.

- In the 1995-97 budget (1995 Act 27) the 1% requirement was expanded to apply to compensation reserves, in addition to gross appropriations. In that biennium, this modification increased the required balance by \$0.2 million in 1995-96 and \$0.5 million in 1996-97.

3. Given the GPR appropriations of AB 133, the general fund condition statement of the bill reflects required statutory balances of \$105.5 million (1%) in 1999-00 and \$121.5 million (1.1%) in 2000-01. If the 1% requirement were to be retained in 2000-01, the balance amount for that year would be \$110.4 million, \$11.1 million less than the Governor's recommendation.

4. The following table shows the effect of the Governor's proposal (in millions) in 2000-01, if the recommended percentage increases were in effect for that year.

<u>Percent</u>	<u>Amount</u>
1.0% (current law)	\$110.4
1.1	121.5
1.2	132.5
1.4	154.6
1.6	176.7
1.8	198.8
2.0	220.8

5. In essence, the Governor is proposing that the state's statutory balance revert to the original language that was enacted in 1981. His recommendation to move (over time) to 2% of annual appropriations is similar, in terms of amount, to 1% of total, biennial appropriations.

6. In addition to statutory balance requirements, the state has a budget stabilization fund. The fund, created in 1985 Act 120, was established to "provide state revenue stability during periods of below-normal economic activity when actual state revenues are lower than estimated revenues..." Act 120 also required that the Secretary of Administration recommend an amount of GPR to be transferred into the fund in the 1987-89 biennium. No recommendation was ever provided. And, although still in the statutes, the stabilization fund never had any monies directed to it until 1998. In that year, Representative Doris Hanson, and Mr. Nathan Henry donated \$10 and \$2, respectively, to the fund. Today, with accumulated interest on the Hanson/Henry donation, the fund has a total of approximately \$12.65.

7. A March, 1998, report of the National Conference of State Legislatures indicates that 45 states currently have some type of budget stabilization or rainy day fund. The only jurisdictions without such funds are Arkansas, the District of Columbia, Hawaii, Illinois, Montana and Oregon.

- Most of the funds are established by statute; however, in seven states (Alaska, Delaware, Louisiana, Oklahoma, South Carolina, Texas and Virginia), the fund is constitutional.

- The amount to be placed in the funds is usually expressed as a percentage of general fund appropriations, expenditures, prior year revenues or some other similar base.

- For fiscal year 1997, 24 states had stabilization funds below 3% of general fund appropriations, 11 states had funds between 3% and 5% and 10 states had stabilization accounts in excess of 5% of general fund appropriations. Eight states, including Wisconsin, had established funds but had not appropriated any monies to them.

8. The rationale for increasing the statutory balance beyond 1% (or appropriating monies to the budget stabilization fund) is to increase the amount of cushion available in case of revenue shortfalls. Suggestions have been advanced that, given the uncertainty of revenue projections, sufficient balances should be maintained. In its study on the subject of rainy day funds,

the National Conference of State Legislatures states, "Wall Street analysts recommend that states maintain budget stabilization funds equal to 3 percent to 5 percent of their general fund budgets." Wisconsin's stabilization fund was recommended by the Wisconsin Expenditure Commission in its report of December, 1986. The Commission, which was created by Governor Earl, suggested that, "To immediately establish the fund's credibility, the 1986-87 ending balance of state general purpose revenues should be deposited in the fund. Additional deposits should be required each fiscal year."

9. The "Budget in Brief" for the 1999-01 biennium identifies the Governor's rationale for recommending an increase in the required statutory balance. That document states, "A one percent balance is inadequate as a reserve to guard against possible economic downturns. Most states have a budget balance far larger than Wisconsin's and bond rating agencies look at the state's budget reserves as a key point in rating state bonds." The "Budget in Brief" also states, "Increasing this reserve also helps to limit any short-term borrowing that must be done to meet cash demands."

10. Increasing the balance beyond the current 1% level, although meritorious, may be difficult to achieve. The state's commitment to two-thirds funding of elementary and secondary school costs, an expanding corrections budget and an interest on the part of many to reduce general fund taxes places constraints on most other state programs. Using state revenues to increase the statutory balance will likely place greater fiscal pressure on those goals and programs.

11. If there is a desire to provide a larger cushion in the general fund, the following options are presented:

- The Governor's recommendation of AB 133. (Alternative 1)
- The Governor's recommendation for 2000-01 at 1.1%, but with no further commitment to increasing the percentage. This would allow the next Legislature to determine if the percentage should be adjusted. (Alternative 2)
- Make no change for this biennium, but increase the balance percentage to 1.2% beginning with the 2001-02 fiscal year. (Alternative 3)
- The Governor's recommendation but maintain the 2000-01 percentage at 1.0% and begin the phase-in at 1.2% in 2001-02. (Alternative 4)
- Eliminate the 1.1% in 2000-01 and begin the phase-in at 1.2% in 2000-01. (Alternative 5)
- Maintain the current statutory balance requirement and direct the Governor, when submitting the biennial budget to recommend an amount, if any, to be placed in the budget stabilization fund. Thus, rather than modifying the percentage of general fund appropriations for the statutory balance, a specific additional dollar amount could be recommended for transfer to the stabilization fund. (Alternative 6)

**ALTERNATIVES**

1. Approve the Governor's recommendation to increase the 1% statutory balance as follows:

<u>Fiscal Year</u>	<u>Percent</u>
2000-01	1.1%
2001-02	1.2
2002-03	1.4
2003-04	1.6
2004-05	1.8
2005-06 (and thereafter)	2.0

2. Approve the Governor's recommendation to increase the statutory balance to 1.1% in 2000-01 but delete reference to future increases in the percentage.

3. Delete the Governor's recommendation and instead increase the statutory balance to 1.2% beginning in 2001-02.

<b>Alternative 3</b>	<b>GPR</b>
1999-01 BALANCE (Change to Bill)	- \$11,042,900

4. Modify the Governor's recommendation as follows:

<u>Fiscal Year</u>	<u>Percent</u>
2000-01	1.0%
2001-02	1.2
2002-03	1.4
2003-04	1.6
2004-05	1.8
2005-06 (and thereafter)	2.0

<b>Alternative 4</b>	<b>GPR</b>
1999-01 BALANCE (Change to Bill)	- \$11,042,900

5. Modify the Governor's recommendation as follows:

MO# Alt. 2

		<u>Y</u>	N	A
2	BURKE	<u>Y</u>	N	A
1	DECKER	<u>Y</u>	N	A
	JAUCH	<u>Y</u>	N	A
	MOORE	Y	<u>N</u>	A
	SHIBILSKI	Y	<u>N</u>	A
	PLACHE	Y	<u>N</u>	A
	COWLES	Y	<u>N</u>	A
	PANZER	Y	<u>N</u>	A
	GARD	Y	<u>N</u>	A
	PORTER	Y	<u>N</u>	A
	KAUFERT	Y	<u>N</u>	A
	ALBERS	Y	<u>N</u>	A
	DUFF	Y	<u>N</u>	A
	WARD	Y	<u>N</u>	A
	HUBER	<u>Y</u>	N	A
	RILEY	<u>Y</u>	N	A

AYE 5 NO 11 ABS

<u>Fiscal Year</u>	<u>Percent</u>
2000-01	1.2
2001-02	1.4
2002-03	1.6
2003-04	1.8
2004-05 (and thereafter)	2.0

<u>Alternative 5</u>	<u>GPR</u>
1999-01 BALANCE (Change to Bill)	\$11,042,900

6. Delete the Governor's recommendation and instead require that the Governor, when submitting the biennial budget to the Legislature to recommend an amount, if any, to be placed in the budget stabilization fund.

7. Maintain current law.

<u>Alternative 7</u>	<u>GPR</u>
1999-01 BALANCE (Change to Bill)	- \$11,042,900

Prepared by: Bob Lang

MO# Alt. 4

BURKE	Y	<u>N</u>	A
DECKER	Y	<u>N</u>	A
JAUCH	Y	<u>N</u>	A
MOORE	Y	<u>N</u>	A
SHIBILSKI	Y	<u>N</u>	A
PLACHE	Y	<u>N</u>	A
COWLES	Y	<u>N</u>	A
PANZER	Y	<u>N</u>	A
1 GARD	<u>Y</u>	N	A
2 PORTER	<u>Y</u>	N	A
KAUFERT	<u>Y</u>	N	A
ALBERS	<u>Y</u>	N	A
DUFF	<u>Y</u>	N	A
WARD	<u>Y</u>	N	A
HUBER	Y	<u>N</u>	A
RILEY	Y	<u>N</u>	A

AYE 6 NO 10 ABS

MO# Alt 4, as amended →

BURKE	Y	N	A
DECKER	Y	N	A
JAUCH	Y	N	A
MOORE	Y	N	A
SHIBILSKI	Y	N	A
PLACHE	Y	N	A
COWLES	Y	N	A
PANZER	Y	N	A
GARD	Y	N	A
PORTER	Y	N	A
KAUFERT	Y	N	A
ALBERS	Y	N	A
DUFF	Y	N	A
WARD	Y	N	A
HUBER	Y	N	A
RILEY	Y	N	A

2001-02 1.1  
2002-03 1.2  
2003-04 1.3

AYE \_\_\_ NO \_\_\_ ABS \_\_\_