

Transcript Prepared By the Clerk of the Legislature
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Tax Rate Review Committee
November 19, 2008

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The Tax Rate Review Committee met at 10:30 a.m. on Wednesday, November 19, 2008, in Room 2102 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing. Members present: Senator Pat Engel; Senator Lavon Heidemann; Senator Mike Flood; Senator Ray Janssen; and State Tax Commissioner Doug Ewald. Members absent: None. Also present: Mike Calvert; Tom Bergquist; and Laurie Weber. []

SENATOR ENGEL: (Microphone malfunction) I think we're all here. (Inaudible) before or after July 15 or November 15 (inaudible) proposal. With that, I will turn it over to Michael Calvert to go over the situation. []

MIKE CALVERT: (Exhibit 1) Thank you, Senator. The report that you have before you was prepared by the Legislative Fiscal Office. It incorporates the most recent revenue forecast estimates done by the Forecasting Advisory Board, on October 31. And we also make some adjustments, I would point out, based on, I guess, some guidance that we'd like to provide with respect to the future prospects on expenditures. The simplest way, probably, to do this is to start on page 4, because that will give me an opportunity to go back in time a little bit. At the top of the page we have a chronology that lays out a viewpoint for the next budget biennium, the next two-year period ending June 30, 2011. When we adjourned at sine die 2008, based on long run projections of the cycling of revenues and methodology that we use and very preliminary estimates based on historical growth pattern of expenditures, a financial status that indicated at sine die 2008 that when you came back for your budget in this next session there would be a projected shortfall of about \$261.7 million to meeting your minimum reserve. In other words, we were starting to anticipate some budget distress going into this next budget cycle. Your last meeting in July that adjusted a little bit to \$267.1 million shortfall. So that was the outlook as of that point in time. Again, a period of developing budget stress or imbalance relative to meeting obligations in the current law concept. In other words, we're not adding or subtracting services, we're not adding or subtracting tax rates or bases. Needless to say, a great deal has changed since July. The revised revenue forecast, item 5 under the chronology, in comparison to our planning estimates, and keep in mind those planning estimates were ours, they were based on the cyclical nature of revenue patterns over the past 25 years. But a great deal economically has occurred since July. Growth rates of the forecast that were prepared by the Forecasting Board are 1.2 percent for '08 for the first fiscal year of the new budget biennium, and 1.4 percent for the second year of the budget biennium. So very, very low growth in comparison to the historical pattern of about 5.5 percent year over year growth. That largely is driven by the economy. Year to date receipt performance is actually pretty decent. The second thing that I would point out is if you just simply stopped there and adjusted for the forecast, the shortfall would be about \$690 million. However, since we are going into a new budget cycle we always take the time to try and assess, based on

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requests, what expenditures might also look like, and have made some judgments in summary, on line 7, that says based on requests for certain major categories of expenditure there might actually be somewhat lower cost obligations going into the next budget biennium to the tune of about \$318 million. Those cost obligations, those cost centers are itemized in the footnote at the bottom, under item 7, what we isolated on. So if those cost obligations do, in fact, prove to be a reasonable estimate, the shortfall might be something less than the \$690 million, it could be around \$377 million. Unfortunately, at this stage we've only just started going through budget requests. And I can't absolutely vouch for the reasonableness of those cost estimates. You know, a superficial look at it seems that in particular school aid might be a pretty reasonable estimate based on our understanding of the formula and its operation. It becomes more of a judgment call as we look at homestead exemption as requested, as we look at public assistance as requested, Medicaid as requested, children's health insurance as requested, those are based on request numbers. Some of these things might be economically sensitive, tend to be countercyclical such as Medicaid. So one of my concerns would be, as we go into the next legislative session, what kind of demand will occur, what kind of pressures will be generated on Medicaid that might cause upward cost pressures. Those items, other than TEEOSA, really appear to be driven by current year expenditures that are substantially below estimate. So if the baseline lowers then future cost estimates are somewhat lower than what we had originally projected. That is the outlook. There are, I'm sure as you are well aware, many, many risks. And we have attempted to try and disclose some of those items that we can see. On the bottom of page 2 there is a discussion of budget risks. Undoubtedly on the revenue side there are huge uncertainties, despite the moderate growth rate for the current year and next year that's just barely above 1 percent. Those of you that were here several years ago, you probably recall how the forecast nose-dived in kind of a series of iterations. And we'll have two more forecasts--we'll have one in February and we'll have one in April. The path of receipts and the path of the economy is a huge uncertainty. I suppose the safest statement you can make is that it looks pretty ugly. It's just a matter of degree now. On the expenditure side there are a number of things that we have not modeled into this status because of the uncertainty--potential loss of federal funds at Beatrice State Development Center in the range of, we understand, potentially \$25 million. We have had a longstanding concern about any liability for damages under Kansas v. Nebraska water litigation. The request document, one item that caught our attention in terms of provider rate increases, they were requested at a 1 percent provider rate increase and that has been the source of concern amongst the Legislature. And we just simply wanted to indicate that if something was different, something was preferred in terms of a provider rate increase, dollar magnitude is itemized there, a 3 percent versus 1 percent is shown in the status, costs roughly about \$50 million. One real uncertainty that has become very apparent here in the last couple of months, in large part because of the performance of the stock market, there is a lot of uncertainty as to how our defined benefit pension plan financing outlook is going to be coming into this next session and actually for the next several years. Shortfalls to meeting long run obligations are made

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up by the state General Fund for defined benefit plans. We may also have a situation where the state Cash Balance Plan might require an infusion of capital, I don't know at this point in time. The last actuarial report that was received was effective through June 30, 2008. And as you all well know, a lot has happened since then in terms of pensions as far as investment values and how that might affect the pension portfolio. I think the potential risk and the potential costs there, based on what I'm seeing other states experience, could be very dramatic, could be very large. So some thought might need be given to a supplemental actuarial review sometime during the next legislative session, and try and get a better handle as to the magnitude and timing of those pension impacts. So I've highly summarized the report. There's a lot of detail there. If you have questions, I'd be happy to answer them. This report, I mentioned to Senator Heidemann as he came in, we'll be sending that out. It's now at the printer, and we'll be sending it out to the members as soon as possible so that they have the same thing in front of them. []

SENATOR ENGEL: (Microphone malfunction) Any questions of Mike from anyone? Comments? (Inaudible) Mike do that. []

MIKE CALVERT: I'm sure you would. (Laughter) You just love it here, don't you. (Laugh) []

SENATOR ENGEL: (Microphone malfunction) So with that, (inaudible). []

MIKE CALVERT: Thank you. []

Chairperson

Committee Clerk