



INITIATIVE 791: A Proposal That Undermines the Ability of Government to Serve the People

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Introduction and Summary Arguments

Initiative 791 (I-791) would limit nearly all state spending based on a formula that accounts only for general population growth and inflation. This “one size fits all” approach would severely restrict the ability of the state to respond to the needs and demands of Washington citizens by disregarding demographic and social changes and disallowing implementation of previous voter-approved initiatives. This proposal would potentially threaten vital services in health care, public safety, and education. This initiative would establish a fiscal limit so universal in application that it would engender chaos in its implementation and unintended negative consequences in its operation.

Changes to the Fiscal Growth Factor

The analysis contained below demonstrates that I-791 proceeds from a flawed fundamental premise, i.e. that the cost of services purchased by state government or provided by state government at the request of and for its citizens should never grow at a pace faster than the growth rate of general inflation and overall population growth. I-791 would then extend this flawed premise to apply to virtually the whole of state government. No area of state services, no matter the need, demand, or available revenue, would be allowed to grow in cost faster than the rate of general population and inflation.

The establishment of the new fiscal growth factor in proposed I-791 would subject most areas of state service to severe swings. As a rolling, three-year average, the fiscal growth factor in current law for the General Fund smoothes the effect of any particular good or bad year. The elimination of this “smoothing” influence would cause drastic shifts in expenditures from both the General Fund and all limited accounts immediately upon the pronouncement of a change in forecast for the fiscal growth factor.

Inability to Phase In Spending

The extension of these fiscal curbs to most state dedicated funds and accounts would eliminate the ability for the state to do any significant phasing in of projects or programs. Such ramped spending, up or down, would not be allowed by I-791's spending limit.

The inability to rationally phase increased spending under I-791 would likely extend to many accounts which fund construction projects or are used to provide the implementation costs for allowed trust fund expenditures. The inclusion of *solely for* language in the exceptions to the I-791 limits will require limits in many areas of spending which the initiative's authors probably did not intend to cover.

Sweeping Unobligated Balances

The sweeping of unobligated balances provision would result in severe cash flow difficulties in service areas for which the revenue flow does not neatly match up with state fiscal years. Similarly, the sweeping of the unobligated General Fund reserve to the Emergency Reserve Fund within each biennium would turbulently alter the budget process, making it increasingly susceptible to special legislative sessions and across-the-board cuts imposed by the Governor between sessions of the legislature.

Restricting Public Education Funding

I-791 would destroy several significant provisions of Initiative 728 (I-728). It would eliminate the use of Emergency Reserve Fund dollars for provision to school districts to improve class size within the K-12 system. It would also eliminate the ninety percent of average national per-pupil benchmark for triggering funds to K-12 to implement the provisions of I-728.

Causing Immediate Chaos with Effective Date

Finally, if adopted, I-791 would force a chaotic transition of uncertainty and emergency actions as the state attempted to implement it. Its retroactive application to the current fiscal year would force immediate reductions in state programs. The clearly unconstitutional provisions would produce lawsuits and uncertainty until the State Supreme Court resolved the issues raised by the initiative containing multiple subjects, amending statutes without setting them forth, and attempting to restrict legislative power without amending the State Constitution.

I-791 Ballot Title and Summary

The A.G. has given I-791 the following title and summary:

Ballot Title

Measure No. 791 concerns the state expenditure limit. This measure would extend state expenditure limits to additional accounts and re-enact and expand the two-thirds legislative vote requirement to raise revenue. Reserve levels would be increased and excess amounts would be redistributed.

Ballot Measure Summary

This measure would extend state expenditure limits to certain funds and accounts outside the General Fund. The limit for each fund would be the previous year's limit adjusted for inflation and population growth. The Emergency Reserve Fund would be five percent of biennial expenditures with excess revenue distributed as specified. Each revenue increase would require a two-thirds majority legislative vote. Spending in excess of the limit would be subject to a vote of the people.

Changes in Funds Subject to the Limit

Under Initiative 601 (I-601), the fiscal growth factor limited the annual growth of only expenditures from the state General Fund.

I-791 would expand the expenditure limit to apply to *all* funds subject to the allotment process under the state Budget and Accounting Act (RCW 43.88). An allotment of appropriations is an agency's statement of proposed expenditures, i.e., a plan prepared by each agency that breaks each appropriation out in detail with respect to its estimate of how each appropriation will be spent. Therefore, each appropriated fund in state government would be subject to a specific individual expenditure limit under I-791 unless categorically excluded. The only exceptions to these I-791 expenditure limits would be the following:

- Debt service funds from which the resources are used *solely* for the payment of debt.
- Capital project funds with resources used *solely* for acquisition, construction, or improvement of major capital facilities.
- Enterprise funds which provide goods or services to the public on a cost-reimbursable basis.
- Internal service funds which are revolving funds used *solely* for provision of goods & services to agencies on a cost-reimbursement basis.

- Expendable and non-expendable trust funds which are *solely* used to account for assets.
- Pension and investment trust funds that *solely* account for transactions, assets, liabilities, and net assets available for plan benefits.
- Accounts used to distribute taxes to local governments.
- Accounts which *solely* contain constitutionally dedicated funds.
- Revolving loan funds *solely* used to fund major infrastructure projects for local governments.

With these limited exceptions I-791, if adopted, would apply to approximately 250 accounts of state government.

The use of “**solely for**” language in this exception criteria section is problematic. Its inclusion likely has the effect of further limiting the exception even within each exempted category. A few examples will suffice to illustrate this problem.

For example, capital project funds are excepted from the new I-791 limits but only if the funds are used for major capital facilities. Capital funds that are used to acquire wildlife and recreational lands simply to set them aside from development but would not require capital construction projects would likely be subject to these stringent new limits.

Further, expendable and unexpendable trust funds are exempt from the I-791 limits for transactions and the payment of benefits. However, the separate funds which pay for the operating expenses for managing the unemployment trust funds benefit payments, eligibility determinations and job search requirement enforcement are likely subject to the limits and could not be increased to meet a swelling of demand for management of the unemployment benefit system during a recession.

Similarly, the Student Achievement Fund set up in Initiative 728 (I-728) to distribute additional per pupil funding to K-12 school districts to be used in reducing class sizes would be affected. The Student Achievement Fund would be subject to the I-791 limits for as long as the state lottery funds are transferred to the fund. When that diversion ends, the fund would be protected because the funds *solely* remaining would be state property taxes dedicated by the state Constitution to the support of the common schools.

Fundamental Flaw in Limiting Growth in All State Expenditures to the Growth in General Inflation and Population

I-791 adopts the fundamental premise contained in I-601 and dramatically extends its application. The premise of I-601 is that the growth in state General Fund expenditures can reasonably be limited to a combination of the growth in general inflation and general

population growth. The assumption presumes that the need or demand for state services is reasonably measured by the growth in these two factors.

However, this presumption often is incorrect. The demand for state government spending is more accurately determined by the growth rates for specific subsets of the population which are served by state programs and by the specific inflation rates in the cost of services which the state purchases.

For example, the state funds the costs of providing higher education services to a portion of the population demanding those services. The portion of the population seeking entrance into higher educational institutions ebbs and flows as demographic groups age into the portion of the population needing services. Currently, the baby boom echo cohort of the population is becoming old enough to enter the higher education system. The demand for higher education services will continue to grow as this huge population cohort ages its way through the need to demand higher education services. This growth in demand is difficult to accommodate within a fiscal growth limit which only reflects general population growth.

Similarly, the cost of services the state purchases for provision in programs may increase at a rate faster than the general rate of inflation. For example, the trend growth rate for health care costs for all public and private health care purchasers over the next several biennia is projected to be at or near twelve percent per year. The general inflation rate, for the same period, as measured by the implicit price deflator, is projected to be closer to two percent. Again, this rate of growth is difficult to accommodate within a fiscal growth limit that only reflects the general rate of inflation.

In fact, the premise that state expenditures should be able to be accommodated within the I-791 growth limit would only be true when there were present enough countervailing factors to compensate for areas which required a growth rate in excess of the fiscal growth factor. Defendants of I-601 and similar limits argue that while some areas of legitimate state expenditure growth exceed the general rates of inflation and population growth other areas will or should grow more slowly to compensate. Such is not always the case, however.

When the totality of state General Fund expenditures is considered, it is clear that many program areas often exceed this general rate of growth. The largest area of state General Fund expenditure is for K-12 schools. While one would expect that the rate of growth in K-12 eligible students would be slowing significantly as the baby boom echo population group aged into the higher education demand group, in fact, such slowing has previously been offset by the growth in K-12 age students generated during periods of high net population migration into the state.

The demand for social service expenditures is also more accurately determined by factors other than general inflation and population growth. Corrections and prison expenditure trends most closely track the growth rate in the male population group 18-32 years in age. Welfare expenditures most closely follow the trend growth rate in the population group

of single mothers of child-bearing age and the change in the rate of poverty. And so on. Of course, the growth rate of state expenditures in these programs are also modified by policy changes to expand or contract the portion of the population which are eligible to be served in each program area.

I-791 takes this premise of I-601, extends it globally to most state expenditures, and applies the limit to each **individual** fund. Therefore, the proposed initiative would severely restrict what limited flexibility the state has retained under the I-601 limitation. The proposed initiative would eliminate the ability to utilize the benefits of compensating changes in program areas supported by other accounts. Any offsetting flexibility from slower growing expenditure areas or faster growing revenue sources would in the future have to occur within each limited account. For example, the state over recent biennia has been able to accommodate double digit increases in the cost of health care by dramatically increasing expenditures from the Health Services Account (HSA). That practice has partially relieved the burden of providing these increases exclusively from the state General Fund. The passage of I-791 would dramatically limit the growth in expenditures from the HSA and close off this relief option for the state General Fund. The same would be true for other funds which have provided sources of expenditure which would otherwise have had to come from the General Fund, such as the Public Safety and Education Account and the Violence Reduction and Drug Education Account.

Changes in the Fiscal Growth Factor

Under Initiative 601 the fiscal growth factor is a three-year rolling average of general inflation (as measured by the implicit price deflator) and general population growth. The fiscal growth factor which is contained in I-791 changes this to an annual figure based on a projection of general inflation and general population growth.

This change eliminates the “smoothing” benefit of the I-601 fiscal growth factor. The I-601 rolling average fiscal growth factor allows for the General Fund state expenditure limit to accommodate a phased reduction or expansion of expenditures as the growth rates for population and inflation fall or rise. I-791 would require expenditures to immediately change as drastically as the projection for inflation and population growth.

The application of expenditure limits to most state accounts and the immediate reaction of the fiscal growth factor under I-791 to a forecasted change in general inflation or population growth would circumscribe any ability of the state to phase in significantly increased or decreased spending for programs provided by funds from a limited account. Such ramped spending increases or decreases cannot be accommodated under the I-791 growth limits. Rational phasing of expenditure increases above the limit are impossible under the strictures of I-791. Similarly, a rational ratcheting down of expenditures from limited accounts over the prescribed expenditure limit are not to be accommodated under I-791. The limits are rigid and unalterable without a vote to amend the initiative.

The Impact of Transferring Funds Between Accounts

Under Initiative 601 the General Fund state expenditure limit is adjusted up or down for shifts of programs or revenues into or out of the General Fund. For example, shifts of program costs from another account or transfers of money from another account to the state General Fund each have the effect of raising the General Fund expenditure limit. This gives the Legislature access to spend additional General Fund dollars which would otherwise be transferred as excess funds to the Emergency Reserve Fund. The ability to spend in the future from the accounts from which the costs were shifted or the funds transferred is unaltered under I-601. Such spending remains limited only by the revenues accruing to those funds.

Further, under I-601 the actual spending level in one fiscal year becomes the base for the level in the following year. Thus, raising the limit in one year has the effect of raising the limit in future years. Conversely, spending below the limit one year constricts the limit in future years.

The proposed initiative would restrict this ability to raise the expenditure limit. It would impose the fiscal growth factor limits on most accounts and funds and circumscribe the ability to raise overall state spending limits by restricting the transfers of costs and dollars between these funds. Under I-791, when money is transferred or program costs or revenue shifted from a limited account to another limited account, the expenditure limit of the former account would be reduced and the latter limit increased. Future spending from the first limited account would only be possible at the reduced level, not at the previous level. Transfers to limited accounts from unlimited accounts under I-791 would only serve to bring more and more of total spending under the limitation of the initiative.

The aforementioned transfer provisions of the current expenditure limit law are known in budget parlance as the “two-way street” transfer provisions. The “two-way street” mechanism was created in a subsequent legislative amendment to I-601. Opponents of this change to I-601 roundly criticize this aspect of current law because of the ability to increase the General Fund state expenditure limit by some moderate measure when the revenues are available to sustain additional spending.

The drafters of I-791 want to eliminate “two-way street” transfers. I-791 allows some ability to raise the General Fund state limit but only at the expense of dedicated fund programs. Any transfer comes with the price of shifting more and more of state government spending into the fiscal strait-jacket of the initiative’s limitation.

Deposits into the Emergency Reserve Fund

Under the provisions of current law the State Treasurer transfers all state General Fund revenue in excess of the state expenditure limit for that fiscal year to the Emergency Reserve Fund (ERF). The provisions of I-791 would require that the Treasurer transfer the **unobligated fund balance** of *each* of the covered limited funds to the Emergency Reserve Fund.

Thus, every covered account or fund would have to begin each fiscal year with no balance. The operation of this mechanism would likely generate cash flow problems for service provision in programs funded from accounts which do not experience a perfect match-up between the annual revenues into the fund and the annual expenditures from the account or fund.

This “sweeping of balances” provision of I-791 would dramatically affect the state General Fund and the state legislative budget process. Under current law and budget practice any General Fund state money which is remaining under the expenditure limit, and not spent in the biennial budget, remains in the state General Fund as an **“unrestricted General Fund balance.”** These funds are available to compensate for declines in the quarterly revenue forecast both during the legislative session and in periods when the Legislature is not in session. This unobligated General Fund balance can also be carried over from one biennium to the next.

Initiative 791 would require that this unrestricted General Fund balance be transferred at the end of the first fiscal year of the biennium to the Emergency Reserve Fund. Therefore, from the end of the first fiscal year forward, within each biennium, the state would be exposed to the need for either emergency across-the-board cuts by the Governor under the authority granted in the Budget and Accounting Act or to an immediate special session of the Legislature. These actions would be required if the General Fund revenue forecast declined by any amount at any of the quarterly forecast revisions. This would occur because the state is prohibited by law from operating with a projected cash deficit.

The Uses of the Emergency Reserve Fund Balance

The Emergency Reserve Fund balance under current law can be expended after a two-thirds affirmative vote of the Legislature if such expenditures remain under the I-601 limit. However, because of a 2002 statutory amendment the Legislature can make appropriations from the Emergency Reserve Fund in the 2001-2003 biennium by a simple majority vote.

I-791 would eliminate the exception for the 2001-2003 biennium, reinstate the two-thirds affirmative vote requirement and add the requirement that the Governor declare an emergency before the ERF could be spent. The Legislature would be allowed to make appropriations from the ERF after the declaration of an emergency with a simple majority of each house, if General Fund state revenues for the biennium are forecast to be one percent less than for the preceding biennium. This exception has little practical effect as this magnitude of revenue decline has occurred rarely in recent history.

Under current law the ERF balance cannot exceed five percent of *annual* General Fund state revenues. Any excess balance of this amount is required to be transferred in the following proportions: seventy-five percent to the Student Achievement Fund and twenty-five percent to the unrestricted General Fund balance.

I-791 would first change the ceiling to any excess funds above five percent of *biennial* state expenditures from all limited accounts, essentially more than doubling the current requirement. Second, the initiative sets out the transfers from all limited accounts as follows: fifty percent to the Education Construction Fund (up to \$250 million per fiscal year), twenty-five percent to the Higher Education Capital Construction Fund (up to \$250 million per fiscal year) and any remaining balance to the Congestion Relief Fund established by the initiative. This newly created fund is required under the initiative to be appropriated exclusively for new highway and road construction, preservation and maintenance of highways and roads, and freight mobility projects. I-791 requires that moneys transferred to these funds can only be appropriated for *other* purposes with a two-thirds affirmative legislative vote *and* a vote of the people.

As can be seen from the above comparison I-791 would dramatically alter the provisions of I-728 that affected the Emergency Reserve Fund. I-728, as a provision of current law, requires the transferring of the overwhelming portion of “excess” ERF funds to the Student Achievement Fund to be appropriated to the Superintendent of Public Instruction and distributed to school districts on a per-student basis. Such transfers of excess ERF moneys must continue until per-student state funding reaches ninety percent of the national average of total per-pupil funding. Further transfers are required to maintain state per-pupil K-12 expenditures at the ninety percent benchmark level. All of these provisions of I-728 would be eliminated by I-791.

Limitations on Taxes and Fees

Under I-601, any action or combination of actions by the Legislature that raises state General Fund revenue or contains revenue-neutral tax shifts requires a two-thirds affirmative vote of each house of the Legislature, if the expenditures resulting from that revenue increase will not exceed the expenditure limit. For the 2001-2003 biennium such revenue raising measures can be taken if approved by a simple majority of each house, if the expenditures will remain under the spending limit.

I-601 also provides that no fee can be increased by an agency in any fiscal year by more than the fiscal growth factor without prior legislative approval, by a simple majority vote in both houses.

Under I-791 any action or combination of actions that raises revenue for *any limited account* would be allowed only if approved by a two-thirds vote of each house of the Legislature if such legislative spending in that account were to remain under the expenditure limit for that account. If such legislative revenue raising actions were to result in expenditures from the limited account in excess of the limit for that account those actions would also require an affirmative vote of the people. I-791 includes the raising of fees in the new definition of raising revenue and, therefore, extends the specific supermajority vote and voter approval requirements to all fee increases, no matter how trivial. The likely effect would be many public votes on small fee increases, often supported by those who would willingly pay the fees without a vote.

Effective Date and Implementation

If adopted by the voters in November, I-791 would take effect thirty days later. However, the initiative contains language which applies the new limits to the current fiscal year, which begins July 1, 2002. Imposing these new fiscal expenditure limits after the beginning of the fiscal year would require the immediate restricting of expenditures from the accounts which would have already exceeded the newly imposed limit for this fiscal year when the initiative took effect. The initiative would force immediate and drastic service reductions in programs funded by these newly limited accounts. Further, because the Legislature would not be able to make changes to the spending limit, any further spending from these accounts would require an amendment to the initiative by a two-thirds vote of each house of the Legislature.

Constitutional Problems with I-791

When the constitutional questions by the proposed initiative are considered, it appears that attempts to implement it will result in extensive and expensive court challenges. The state is required by law to use taxpayer money to defend any voter approved initiative, no matter how poorly drafted or clearly unconstitutional. The primary issue posed by the initiative is whether or not the drafters can, through the initiative process, restrict the legislative powers granted in the State Constitution. I-791 would require a supermajority vote of the Legislature to increase taxes and fees and require voter approval of taxes and fees under certain circumstances. The State Constitution is the only instrument which limits the legislative power by requiring legislation to be adopted by greater than a majority vote of the Legislature in a few particular cases. In every other case the state Constitution simply requires a simple majority of both houses to enact legislation. The state Supreme Court has said that initiatives will be considered to be amendments to the Constitution if they add conditions to those areas where the Constitution already contains the exclusive criteria [**Gerberding V. Munro**, (134 Wn.2d188)]. As such, these attempts to amend the Constitution via the initiative process would be unconstitutional and invalid. I-791 would appear to violate this constitutional condition by imposing additional supermajority and referendum requirements beyond those exclusively set out in the Constitution.

Further, I-791 is flawed in that it contains more than one subject. Article II, section 19 of the Constitution requires a single subject to “prevent Legislators, whether the people or the Legislature, from having to vote for a law they do not favor in order to obtain a law which they do.” The State Supreme Court has ruled twice in recent years on the issue of initiatives addressing more than one subject. The Court found Initiative 695 unconstitutional in its entirety in **Amalgamated Transit v. State** (142Wn.2d 183) because it contained more than one subject. The State Supreme Court also declared Initiative 722 void because it embodied two unrelated subjects in violation of Article II, section 19 in **Burien v. Kiga** (144 wn.2d 819).

A simple examination of proposed I-791 reveals that it contains multiple subjects, some of which are unrelated by any examination. It would establish a new expenditure limit as it applies to the General Fund, establish new limits for over two hundred dedicated funds, require supermajority votes in the Legislature for certain legislation, require voter approval of certain tax and fee increases, establish new uses for the Emergency Reserve Fund, set up a new Congestion Relief Fund, and establish a new prohibition on state and local governments in the taxation of intangible property.

I-791 is therefore flawed when judged in light of the requirements in Article II, section 19 of the Constitution.

I-791 is similarly flawed when considered in light of Article II, section 37 of the State Constitution which prohibits enactment of legislation that revises or amends other acts without setting those acts forth in full and showing the effects of the amendments on current statutes. As the state Supreme Court indicated in **Amalgamated Transit v State** (142 Wn.2d 183):

The purposes of this provision are to avoid confusion, ambiguity, and uncertainty in the law that would occur if the law existed in separate and disconnected legislative provisions, and to disclose the new law impact on existing law

I-791 would amend the enabling statute of every account and dedicated fund to which the new limits apply. Each of these funds and accounts has a statutory provision which establishes the taxes and fees which flow into the account and provides the purposes for which those funds may be expended. I-791 would purport to amend all of these statutes by providing specific limits for each and allowing the funds to be taken and spent on new purposes, after passing through the Emergency Reserve Fund. Yet, none of these statutes are set forth or explicitly amended in the text of the initiative. I-791 would appear to violate the most basic conditions required under Article II, section 37.