



## BRIEFLY

Although some members of the legislature have declared Initiative 601 dead, the announcement is premature. Last year's amendment of the voter-approved tax and expenditure limitation has opened the door to mischief, particularly in the arcane area of fund transfers. Nothing, however, requires lawmakers to cross the threshold.

# I-601 Not Dead Until Legislature Declares It So

Examining the governor's proposed 2001-2003 budget, some Republican lawmakers seem poised for premature capitulation. They say they now consider last year's amendment of Initiative 601 a mistake. Changes in the law, they say, created a "loophole" that allowed the governor to raise the spending limit by some \$300 million. As a result, they contend, I-601 is dead.

Before internment, let's consider two points.

**First, the legislature writes the final budget.** The governor has previously proposed budget provisions that lawmakers have rejected. Sometimes they have disagreed with the governor's interpretation of I-601, as when they chose not to go along with his property tax credit for education last session. Sometimes, they have just chosen a different course, as when they've adopted budgets at a level lower than that proposed by the executive. And, occasionally, they've gone along with an interpretation of I-601 that they later regretted, as with the sports stadia tax credits. In the end, though, the survival and interpretation of I-601 has more to do with the legislature than it does with the governor, more to do with whether loopholes are exploited than with their existence.

**Second, amending I-601 to allow the limit to be raised for fund transfers made sound fiscal policy sense,** although lawmakers must exercise caution.

As adopted by the voters in 1993, Initiative 601 set out the justifications for raising or lowering the expenditure limit. Among them: "If the cost of any state program or function is shifted from the state general fund on or after January 1, 1993, to another source of funding, or if moneys are transferred from the state general fund to another fund or account, the office of financial management shall lower the state expenditure limit to reflect the shift." (RCW 43.135.035.4)

This provision established a one-way street; transfers from the general fund to other accounts lowered the limit, but transfers to the general fund did not increase the limit. For opponents of dedicated funds, earmarked accounts, and the like, this provision made it more difficult to eliminate the plethora of funds outside the general fund and not covered by I-601, which limits the general fund only. They wanted to see symmetry, a "two-way street."

So, I-601 was amended last year to add a new section creating the two-way street: "If the cost of any state program or function is shifted to the state general fund on or after January 1, 2000, from another source of funding, or if moneys are transferred to the state general fund from another fund or account, the state expenditure limit committee, acting pursuant to RCW 43.135.025(5), shall increase the state expenditure limit to reflect the shift." (RCW 43.135.035.5)

*Notice: the decision to increase the limit is the province of the state expenditure limit committee, also created last year in HB 3169, the bill*

108 S. Washington St., Suite 406

Seattle WA 98104-3408

PH 206-467-7088

FX 206-467-6957

[www.researchcouncil.org](http://www.researchcouncil.org)



*containing the amendments to I-601. (See Final Legislative Budget Good Enough, ePB 00-22, June 20, 2000)*

Now there's concern the two-way street may be a fast track to killing I-601. Again, that is simply not the case, although there is a problem with the language adopted last session.

## Legitimate Concerns

**Legislators are right to be skeptical of the transfers, and should exercise independent judgment before accepting the governor's proposal.** The governor cannot unilaterally shift funds from one account to another. If the shift does not occur, the limit will not be raised and the so-called "loophole" will not be exercised. So the decision remains with the legislature.

There are three fundamental concerns with the governor's approach.

**First, he creates new discretionary spending capacity.** By establishing a two-way street for program transfers, lawmakers hoped to create an incentive for the sound fiscal practice of reducing the state's reliance on earmarked taxes and dedicated accounts. (See *Too Much Earmarking, Dedicating Funds*, Special Report, July 31, 1996.)

One may contend that the transfer of a program or activity under this provision should not increase discretionary spending capacity. (For example, when the costs of Program X are transferred from the X Fund to the general fund, the general fund limit is increased to accommodate the new expenditure. No more or less should be spent on Program X than had been previously spent from the X Fund. Therefore, the higher spending capacity provides no additional discretion – it's only used for Program X.)

If that line of reasoning is followed, however, it simply preserves the dedication within the general fund. It's self-defeating, in that it fails to advance the goal of having the general fund serve as the legislature's basic discretionary fund. Over time, the dedication should be lost. In the transition, however, fund transfers that immediately create an opportunity to increase spending should receive extraordinary scrutiny.

**Second, revenues are transferred without program costs.** Where a drafting glitch clearly occurred is in the second part of the new section referenced above, i.e., "*if moneys are transferred to the state general fund from another fund or account.*" When revenues are brought into the general fund without a corresponding expenditure requirement, the limit is raised and the money can be spent freely. That was not the intent of the "two-way street" language.

While that may be the primary "loophole" created in last year's amendment to I-601, there is another concern. Spending capacity outside the general fund can be increased when program costs from a dedicated account are brought into the general fund unaccompanied by the associated revenue source. When this is done, new spending (i.e., spending outside the general fund) can be initiated with the dollars remaining in the dedicated fund that has been relieved of the spending obligation.

**Third, some earmarks and dedications should not be transferred.** Some accounts, like the Health Services Account, have been funded by taxes that are



effectively general fund revenue sources. Further, the activities paid for from these accounts are typically provided from the general fund. Although these dedicated accounts were set outside the general fund by the legislature, they ought to be returned. The programs they fund should vie with all other general fund programs in the traditional budget process.

Other accounts, though, like the state toxics accounts are tied to particular services and funded from taxes imposed on business presumed to contribute to actual or potential environmental hazards. The toxics account originated with a voter initiative. Transferring the account to the general fund, as proposed by the governor, eliminates the explicit link between the funding source and the service provided, one of the better arguments for tax dedication.

Because of situations like this, the legislature ought to carefully examine each proposed fund transfer to assure that the transfer represents good fiscal policy, matches the intent of the “two-way street,” and does not increase the spending limit without providing adequate ongoing resources to sustain the higher spending level.

**Examining the transfers.** In the following paragraphs, we attempt to track some of the changes proposed by the governor. Analysts disagree on how some of the transfers should be interpreted, so these figures may vary from those reported elsewhere. Nonetheless, they serve to illustrate the complexities of fund shifts in the governor’s proposed budget.

The governor’s 2001-2003 budget anticipated a total of \$479.6 million in increased I-601 spending capacity (see *Governor’s Proposed Budget Pushes the Limit*, ePB 00-38, December 21, 2000). Of that, \$165.1 million came from transfers into the general fund, an additional \$187.2 million from the effect of increased spending in the 1999-2001 supplemental budget (including spending made possible by fund transfers), and \$324.7 million from his proposed interpretation of what the voters intended by approving I-732. Partially offsetting these increases is a downward adjustment of \$197.4 million, primarily because transit funding would be transferred from the state to local government.

Only some of these changes are related to last year’s amendment of I-601, and not all of them violate the sensible intent to create a two-way street.

Consider first the 1999-2001 supplemental. Initiative 601 requires that the spending limit be based on actual expenditures. Any increase in a supplemental budget has always resulted in an elevation of spending capacity in the out years. The governor’s supplemental budget boosts spending \$156 million, translating to increased capacity in 2001-2003 of \$165.1 million (the new spending increased by the I-601 growth factor). To accommodate the new spending, the spending cap must be lifted. The governor proposes an increase of \$89.6 million in the 1999-2001 spending limit. Of that, about \$43.5 million is due to the transfer of Health Services Account revenues into the budget. The revenue transfer adds expenditure capacity not matched by program responsibility. Other program transfers amount to less than \$45 million, including a shift resulting from the loss of federal funds, an adjustment always legitimate under I-601.

The \$165.1 million in transfers in the 2001-2003 budget proposal are primarily program transfers.

To receive advance notice of  
Washington Research Council  
publications by e-mail send your  
e-mail address to  
wrc@researchcouncil.org



In total, it would appear that of the \$479.6 million in new spending capacity proposed in the governor's 2001-2003 budget and \$89.6 million in the 1999-2001 supplemental, less than \$100 million can be attributed to the loophole left in the drafting of last year's amendment.

More important, lawmakers have choices. For example, a) they can revisit the statute to require that when programs and revenues are transferred into the general fund, the expenses and revenues must match, b) the state expenditure limit committee can assure that any upward revision in the limit resulting from a transfer of one-time revenues (e.g., cash balances rather than earmarked taxes) to the general fund only increases the limit for that year, on the basis that such transfers, unlike expenditure obligations, are not ongoing.

**In sum, Initiative 601 has not been irreparably damaged by either the governor's proposed budget or last year's amendment.** Citizen initiatives are not exempt from the routine need for legislative modification. I-601 was one of a pair of tax and expenditure limitation measures on the 1993 ballot; each had strengths and weaknesses. The voters preferred I-601 and defeated the other. Since then, the limit has improved fiscal discipline on the part of the legislature and the governor. Whether it continues to do so will be for the 2001 legislature to decide.

As has been said before, no spending limit – however artfully drafted – can constrain a legislature determined to violate it. Correspondingly, lawmakers dedicated to fiscal responsibility can work within the confines of the limitation even when the existence of a technical loophole provides them a way out.

I-601 will only be dead when the legislature acts decisively to abandon it. Until then, the initiative continues to provide the framework within which the state budget must be written.

