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**2010-2012 Budget Address
Jan. 19, 2010
Governor Steve Beshear**

Mr. President, Mr. Speaker, distinguished members of the Kentucky General Assembly, Lt. Governor Mongiardo, other Constitutional officers, honorable members of the Court of Justice, honored guests, including Kentucky's First Lady and my fellow Kentuckians ...

As your governor I come tonight during a time of unprecedented financial hardship in our country to present my plan for funding state government over the next two years.

This financial crisis was created by forces beyond our control, but it has been my job to lead our people through it.

Six times since I became governor in December 2007 the General Assembly and I have acted together to fill budget shortfalls ranging from \$100 million to nearly a billion dollars.

This budget I unveil tonight fills a seventh gap between expected revenues and critical needs, the largest shortfall in the history of the Commonwealth.

And it does so by continuing the same strategic approach that I have used to guide Kentucky through these last two years of economic turmoil, an approach that has strengthened, day by day, how we serve our people.

My approach has been a steady, pragmatic one that addresses short-term challenges with an eye toward the future, and that has allowed us to make progress – not as much progress as we all want to make – but tangible and measurable advances on persistent challenges facing Kentucky.

Thus this budget ...

- ... is responsibly balanced.
- This budget says "no" to raising taxes on our struggling families and businesses.
- This budget creates and retains jobs.
- This budget guides state spending through the next two years, as required by law and as needed by agencies, universities and schools so they can plan for expenses and personnel.

Some say we should pass a one-year budget and pray that things get better before the second year. I say we must not hide from difficult decisions, and we must not sidestep our duty.

This budget protects core priorities, such as the basic funding formula for our classrooms and children, public safety, and health care for our most vulnerable populations, while minimizing cuts to other critical areas, such as higher education and environmental protection.

This budget continues to reduce costs – in the last two years we've already cut about a billion dollars in spending by eliminating unnecessary expenses, increasing efficiencies, trimming staff and rethinking how government operates.

It requires additional 2 percent cuts in many agencies, a figure that comes on top of 20 percent to 25 percent cuts over the previous two years.

It also contains savings from a new Smart Government Initiative I announced last week, which includes reviews of property management, information technology, the transportation fleet, contracts and procurement.

We expect to reap savings of \$77 million over the biennium, including \$33 million in the General Fund.

This budget features the same flexibility and maneuverability that has allowed us to fight this recession one step at a time, leaving Kentucky in better financial condition than most other states.

And finally, this budget contains a new source of recurring revenue, revenue that currently is being carried across our borders to fund schools, roads, health care and other needs in our neighboring states ... revenue that would begin moving us away from the habit of using one-time monies to fund recurring expenses.

Numerous times over the past month, people have asked whether my budget plan would include money from an expansion of gaming.

My answer – each of those times -- was the same: Everything is on the table for discussion.

In fact, up until the very last minute we have been investigating every option of funding Kentucky's priorities ... every option, that is, *except* for a broad-based increase of the tax burden on Kentucky families and businesses – an approach that would be counter-productive to our economic recovery.

My friends, the analysis is now over, and the conclusion is clear: Gaming revenue is the only practical option to begin funding long-term priorities with recurring revenue.

For too long, state government has been relying on one-time solutions to balance its budgets, all the while increasing what's called a structural deficit, meaning our expenditures each year exceed our recurring revenues.

Revenue from a limited expansion of gaming will help us begin to reverse that trend.

It will provide a reliable source of income we can use year after year after year to make investments in the institutions and people of this state, to strengthen our efforts to emerge from this recession not shell-shocked and shattered, but ambitious and able.

Now, what sorts of investments are we making?

Let me tell you what this budget proposes:

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In the area of education, which must be our highest priority:

- This budget maintains the General Fund appropriation for SEEK, the basic funding formula for teaching in the classroom which represents some 77 percent of our K-12 spending.
- It authorizes \$150 million in bonds for building and renovating school facilities.
- This budget repays the teachers' pension fund the \$476 million the state borrowed to pay teacher retiree health insurance and realizes \$96 million in savings by financing at a cheaper rate.
- It partially funds the standards, assessment, accountability and professional development for both K-12 and Postsecondary Education required by Senate Bill 1 from the 2009 session.

The rest of the funding would come from Kentucky's Race to the Top application for additional federal funds, which was enabled by the passage of House Bill 176 just last week.

- And this budget identifies teacher raises as the No. 1 priority should we get another round of federal stimulus funding.

In the area of higher education:

- This budget protects our institutions from cuts in the first year of the biennium and limits them to a 2 percent cut in the second year, when the current federal stimulus is exhausted.
- It uses \$584 million in General Fund bonds to fund the highest priority capital construction project at each of our eight public universities, plus two buildings on our community and technical college campuses.
 - I'm talking about constructing phase II of the Eastern Kentucky University science building.
 - At Kentucky State University, expanding and renovating the Betty White Nursing Building.
 - At Morehead State University, renovating and expanding the Student Center.
 - At Murray State University, constructing the final phase of the New Science Center Complex.
 - At Northern Kentucky University, constructing the Health Innovations Center and renovating the old science building.
 - At the University of Kentucky, building a Science Research facility to further UK's efforts to be a Top 20 research institution.
 - At the University of Louisville, constructing a classroom building.
 - At Western Kentucky University, renovating the Science complex.
 - At Jefferson Community and Technical College, constructing a building that will become the Carrollton campus.
 - And at Owensboro Community and Technical College, constructing phase II of the Owensboro Advanced Technology Center.
- This Budget recommends \$323 million in agency bonds, bonds that you and I know require no debt service from the state, to construct buildings and renovations that the universities have requested and expressed the ability to pay for.
- And it uses 100 percent of lottery revenues for student financial aid, fully funding the KEES scholarship program, increasing funding for need-based scholarships by 27 percent and fully funding the National Guard Tuition Assistance Program.

In the area of health care:

- In the Medicaid program, we are instituting a range of initiatives to contain costs in utilization and benefit management as well as improving program integrity and increasing revenue collections. We estimate savings from those efficiencies of \$244 million in the first year and \$117 million in the second year, including 75 million in General Fund dollars in year one and \$33 million in year two.

However, Medicaid costs will continue to increase because of higher health care costs; the loss of the increased federal match rate; and eligibility rolls that are expanding by 3,400 Kentuckians a month because of the recession.

That number – 3,400 per month – shows in a dramatic way the impact of this recession. In the previous biennium, the increase to our Medicaid rolls was 930 a month.

We now have over 789,000 Kentuckians in the Medicaid program. That's nearly one in five of our citizens depending on us for their health care. We're talking about Kentucky's most vulnerable citizens – the blind, the disabled, pregnant women and children in our lowest-income families.

This budget also requires an additional \$50 million in General Fund savings from the Medicaid program each year of the biennium. We will be reviewing that program from top to bottom to identify areas of additional cost savings.

- This budget for the first time funds smoking cessation programs in the Medicaid budget in an attempt to drive down Kentucky's historically high smoking rates, a major drain on our health care budget. This step alone could have significant, long-term payoffs in reduced health care costs, fewer chronic problems for our children, increased worker productivity and an improved image for our state.
- This budget also removes a barrier to KCHIP, the health insurance program for low-income children, by eliminating the requirement that our poorest families pay a premium. It's estimated that this requirement denies health insurance to 700 children a month. For only about \$370,000 a year, we can provide health insurance to thousands of additional Kentucky children who need it.

Already we've brought health care to 35,000 previously uninsured children. This is both a moral obligation and a strategic one, because it will pay off in lower long-term health care costs and children better prepared for school and life.

- This budget authorizes \$129 million in General Fund bonds to build a new Eastern State Hospital mental health facility to replace a complex in Lexington whose buildings pre-date the Civil War.
- And it replaces the Glasgow State Nursing Facility, a long-term care nursing facility for seniors with mental illness or mental retardation. This building has structural problems and must be replaced, and this budget funds construction.

In the area of public safety:

- This budget maintains the safety and security of the public by providing funding for growing prison populations, but it also holds down costs with a variety of measures: Continued use of the parole credit for certain offenders; expanded use of home incarceration; the switch that moves female inmates out of Otter Creek; and increased use of community-based substance abuse programs like halfway houses and the Recovery Kentucky Centers.

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- This budget maintains funding for the Kentucky State Police, allowing them to fund another cadet class so that Kentuckians can continue to feel safe in their homes and on the streets. Our number of sworn officers is at its lowest since 1995 due to retirements and lack of additional funding.
- And it provides funding to keep our justice system operating by addressing part of the shortfall in state court operations and maintaining funding for our prosecutors and public advocates.

In the areas of economic development and transportation:

- It reinvests in programs to create and retain jobs, including \$50 million in KEDFA and economic development bond funds and \$10 million in grants and loans to high-tech companies.
- It includes \$38 million in General Fund Economic Development bonds to fund infrastructure needs related to the military base realignment at Fort Knox to prepare for 5,000 new jobs.
- And it proposes \$112 million in Road Fund bonds to finish projects initiated in the last budget cycle related to BRAC.
- This budget also proposes the authorization of \$300 million in bonds to fund critical state highway projects.
- And it dedicates an additional \$50 million in federal highway funds each year for the Louisville bridges project. This is on top of the \$231 million in GARVEE bonds already authorized.

Maintaining existing jobs and creating new jobs is the fastest way for Kentucky to emerge from this recession, and this budget helps accomplish that.

In the area of public employees and retirees:

- In 2008 the General Assembly and I came together in a special session to save the retirements of our state police and state employees. This budget honors that commitment by fully funding the promised increase in employer contribution rates over the next two years for both current and future retirees.
- This budget also funds health insurance for our teachers, school employees and other state employees, even as we continue efforts to control costs by promoting wellness programs.
- And if we get another round of federal stimulus funding, I propose we fund 1 percent raises for state employees.

And finally, unlike other states this budget keeps our parks system open. But we believe we can manage them better. We've conducted a comprehensive review of our system and will be implementing cost savings and management improvements to serve our customers better with fewer tax dollars.

My friends, these investments in our future are ours to make.

We just need the courage and commitment to make them happen.

I'm confident that everyone in this chamber shares most if not all of the priorities we propose to fund in this budget.

But I also understand that some of you disagree with my proposal to fund these priorities and balance this budget using recurring gaming revenues.

Unfortunately, our options are limited. In fact, there are only four possibilities or some combination thereof.

First, we could make cuts sufficient to balance our budget without any additional revenue.

But to those of you who think we can simply cut our way to prosperity, a word of caution:

If you take this approach but want to maintain the priorities set forth in this budget, the cuts to the rest of government would not be 2 percent over the biennium – instead those cuts would be over 12 percent in the first year of the biennium and 34 percent in the second year, compared to the current year.

And that's on top of the 20 percent to 25 percent in cuts that many of these agencies have already experienced in the last two years.

Cuts of this magnitude would undoubtedly lead to mass layoffs and would inflict devastating damage on literally hundreds of critical services to communities and individuals around the Commonwealth, such as prenatal care, water permits, air quality inspections, social workers and fire inspections of public facilities like day-care centers and schools.

A second option for balancing our budget is the possibility of an additional round of stimulus funding from Washington.

We've all been watching as Congress debates whether to provide additional stimulus help for states in the form of more stabilization funds, an extended higher Medicaid match and highway project funding.

My budget office is monitoring that situation closely.

But the bottom line is we cannot control what happens in Washington, and thus my budget does not count on that money.

Attached to my budget is a contingency plan that suggests strategic use of that money over the next two years should we get it.

But if we do get it, it is absolutely imperative that we do not squander those funds in the first year of this biennium by front-loading this budget with projects.

During the last round of stimulus funding, many states were forced to use all of their State Fiscal Stabilization Funds right away.

But in Kentucky, the General Assembly and I followed a strategic plan for using those funds that allowed us to carry over money not only to help balance the 2010 budget but also to use \$268 million for the coming fiscal year.

I urge you to join me in adopting a similar approach should those federal funds materialize again.

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My priorities for this money would be:

- Funding 1 percent pay increases for teachers and state employees.
- Restoring cuts to higher education.
- Restoring cuts to the Department for Community-based Services.
- Creating a buffer in case revenues do not materialize.
- And beginning to build a rainy day fund to return us to some semblance of solvency.

Some people might see the possibility of receiving that federal money as an excuse to avoid decisions on recurring revenue. That approach takes into account neither recent history nor the future, and it unbalances even further the spending versus revenues equation.

The fact is, one-time federal stimulus assistance doesn't change the reality that without a dependable recurring revenue stream it will be extremely difficult to protect our priorities.

In fact, to balance this budget – even with recurring gaming revenue – we are using a range of one-time budget solutions, including one-time fund transfers, debt restructuring and alternative financing.

The latter includes the use of bonds for certain long-term expenses, such as student financial aid and maintenance.

Now, the third option for balancing this budget is a broad-based tax increase, and that indeed would be a source of recurring revenue.

But that would accomplish the exact opposite of what we need during these difficult times by increasing the burden on the very people and the very businesses we are relying on to grow us out of this recession.

Our economy has begun to turn around, as seen by recent job announcements and the December revenue forecast that predicted revenue growth of 3.6 percent in the first year and 3.7 percent in the second.

A broad-based tax increase would throw cold water on those sparks of recovery.

Some people also think that it is time to talk about reinventing our tax system to make it more modern and make it more fair.

I am open to those conversations.

But we are not in this financial crisis because of our tax structure, and changing our tax structure isn't going to get us out of this financial crisis.

Look around the country.

Regardless of what tax system a state has, every state is in trouble – many of them in worse shape than we are.

And finally, our fourth option to balance our budget is the use of tax revenues and license fees from a limited expansion of gaming at our Kentucky horse tracks.

Some say it would be unprecedented for a governor to propose a budget that depends on revenue from other legislation.

That is simply not the case.

In fact, three previous governors – on four different occasions since 1984 – have done the same thing.

And people who may propose substantial tax increases to help balance this budget will be taking the same approach.

Now, my views on gaming have been clear for some time.

As I've said before, this is a recurring source of revenue that will help us begin to minimize the gap between the revenue we bring in this year and our expenditures.

The House passed a version of this bill in 2009.

A bill has been introduced today with language authorizing video lottery terminals at racetracks.

The appropriation and revenue language will be reflected in my proposed budget.

The only difference in the content of this year's bill and the House bill of 2009 is where the revenue is allocated.

I propose bringing the revenue into the General Fund to help balance the budget and fund our priorities.

Now, in 2009, the House proposed that we use this recurring revenue to replace dilapidated school buildings.

Ordinarily, that's a good use of state money, and I support that concept. But frankly I'm more concerned right now about keeping our existing classrooms open and our existing teachers on the job.

So there you have it.

I've put forth my plan – a conservative, responsible plan that would not only help the state survive but also help it move forward.

Now what's needed is honest, thoughtful and open discussion of how to make that happen.

We've worked together to solve budget shortfalls before.

Together we protected the pensions of teachers, firefighters, police officers and other public employees. Together we moved forward on bridges legislation.

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Together we revamped Kentucky's economic development tools. And together – just the other day – we took a stand toward helping our lowest-performing schools succeed.

I'm confident that – together -- we can get the job done once again.

In closing, let me share an anonymous note we recently received.

*“Kentucky has been good to me,” it read. “...
a pleasant place to live, a low cost of living, reasonable tax rates etc.*

I wish this could be more, but every little bit helps. Thank you Kentucky.”

Enclosed in the envelope with the note was a money order, payable to the state treasurer, for \$200.

My friends, that Kentuckian and many others across this state know what a special place Kentucky is. It's our job to keep it that way.

Thank you, God bless you and God bless this beloved commonwealth.

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