GUIDELINES FOR FY18
LFC APPROPRIATION
RECOMMENDATION

I. PURPOSE

The Legislative Finance Committee (LFC) budget guidelines provide analysts with direction on performance-based budgeting, the preparation of the budget narrative, and the development of FY18 recommendations on recurring appropriations, priority capital spending, and other one-time investments. The guidelines also serve to inform state agencies and the general public about the LFC priorities and the committee's approach to budget recommendations for FY18.

II. REVENUE OUTLOOK

The August 2016 consensus revenue estimate projects FY17 recurring general fund revenue will be $5.7 billion, and FY18 recurring revenue will be $6 billion. Preliminary FY16 ending reserve balances are estimated at $130.3 million, or 2.1 percent of recurring appropriations, prior to any current-year adjustments made by the Legislature. Preliminary estimates for FY17 ending reserve balances are negative $333.2 million, or -5.3 percent of recurring appropriations. There will be no "new money" in FY18, defined as FY18 projected recurring revenue less FY17 recurring appropriations, because the difference is projected to be a decline of $210.9 million, or 3.4 percent, from FY17 appropriations.

III. FY18 PRIORITY AND APPROACH

No one could foresee with any certainty the extent to which oil and gas prices and production would fall and the consequent decline in gross receipts and corporate incomes taxes in the months after the Legislature adopted the current year budget. Even though legislators reduced general fund spending for FY17, appropriated levels were higher than revenue collections, resulting in a projected spend down of general fund reserves into negative territory. Actions taken in a special legislative session to rebalance the FY17 budget did not leave much room for operating budget growth in FY18.

Overall, the committee will emphasize flat general fund appropriation levels in most state agency budgets and depending on the outcome of consensus revenue estimates, may consider further reducing general fund appropriation levels. Growth in base general fund appropriations will be considered on a case-by-case basis to address public safety and changes in program caseload, workload, waiting lists, and medical and per diem inflationary costs. In order to fund prioritized programs, the committee will consider targeted cost savings, focusing on duplicated services, non-critical or ineffective initiatives, areas where efficiencies have been created, or where there is no evidence a program is working.

Further, LFC analysts shall:

- Identify opportunities for consolidating or streamlining duplicate or unnecessary programs and activities, eliminating earmarks, and enhancing efficiency;
- Identify agencies or programs that exhibit mission drift, have demonstrated limited success in fulfilling their mission, are unfocused, ineffective, high cost, are not cost beneficial, could be funded by user fees or alternative sources, or are no longer needed because goals or other conditions have been met or changed, so that funding can be utilized elsewhere;
- Use cost-saving opportunities and evidence-based analysis to prioritize agency funding and improve performance outcomes; and
- Consider whether funding supports existing service levels and caseloads.

IV. PERFORMANCE ANDACOUNTABILITY

Updated key agency report cards, newly introduced cross-agency reporting, use of a statewide performance dashboard, and an updated web-based reporting system will improve access to performance information for the Legislature and the public. Key interim Accountability in Government Act (AGA) changes focused on improving the quality of performance measures, eliminating less-useful measures and reducing the frequency of reporting for other measures. The list of key agencies was updated to match the availability of data with some agencies switched from quarterly to semi-annual or annual performance reporting.

In a few instances, LFC and DFA did not reach consensus on AGA measures. In these agencies LFC analysts will consider returning to pre-AGA budget categories and restricted BAR authority, providing the Legislature with adequate appropriation and expenditure oversight.

Analysts shall integrate agency performance results into their budget analysis and, whenever possible, align budget recommendations with program achievement. Consideration for continued base funding should be given to those programs that demonstrate results, effective design, and strong planning and management. Analysts should follow these guidelines in reviewing agency performance:

- Agency strategic plans should ensure: 1) the stated mission, goals, and objectives are consistent with statute and state policies; 2) overarching programs are coordinated among divisions and, where applicable, across agencies; 3) programs are consistent with current resources and conditions; and 4) resources are aligned with the agency's strategic direction and performance results.
- Performance targets should be benchmarked for priority programs whenever possible. Suggested resources for benchmarking include federal standards, best practice standards set by other agencies and states, historical data, and desired results. Analysts should recommend new or alternative performance measures that better gauge program outcomes as necessary.
- Performance data and results from recent LFC program evaluations should be used to identify programs that are ineffective or producing marginal results or, conversely, are achieving desired outcomes.

Analysts shall use Results First cost benefit analysis where available, notably in the areas of public safety, early childhood, child welfare, and behavioral health programs.

In select cases, analysts may recommend additional performance measures from what DFA approved during the interim for agencies to include in their FY18 budget request to hold agencies accountable for achieving program results.

V. BUDGET GUIDELINES

The following budget guidelines apply to all agencies.

Compensation, FTE, and Vacancy Rates. Even though state employment in New Mexico remains significantly below peak employment levels seen prior to the Great Recession of 2008, out-of-cycle increases, targeted salary adjustments, and increased benefit costs have increased personal services and employee benefits (PS&EB) spending. Also, elevated vacancy rates have resulted in large amounts of PS&EB funding being transferred to other areas of the budget.

According to the State Personnel office, the state's salary structure is 18 percent below market. The committee may consider the need for targeted compensation increases to address poor recruitment and retention impacting public safety, health care, and vulnerable citizens. Additionally, the committee may consider general salary increases for state employees to offset inflation and health insurance premium increases.

Expenditures and Contractual Services. Analysts are directed to analyze requested expenditures for professional services contracts to ensure contracts address agency priorities, adhere to performance criteria, and are monitored for performance. Analysts shall use the monthly Contracts Report provided by DFA and information in the New Mexico Sunshine Portal to analyze an agency's historical use of contractual services. Analysts should note shifts of workload from FTE to contractors and ensure the cost of performing the work is not double funded.

Revenues and Cash Balances. Use of other state funds and federal funds shall be maximized based on grants, awards, agreements, budget adjustment request (BAR) activity, and program history. To reduce the need for revenue from the general fund, cash balances shall be used in the FY18 budget recommendation. Governing statutes shall be reviewed to determine if funds are budgeted appropriately and if they can be used for other purposes. Analysts shall scrutinize expenditures where an earmarked revenue is in decline or unavailable.

Federal Funds. Federal funds should be leveraged to the extent possible in keeping with the committee's policy priorities to ensure these funds are accurately reflected in the budget recommendation. Analysts are directed to compare information on revenue forms provided in the budget requests with deviations from appropriations, the database provided by the Federal Funds Information for States (FFIS) service, and other sources of information on federal funds. Analysts shall also use historical budget adjustment request (BAR) information to determine if the level of federal funds is accurately reflected in the agency request.

Expansion. Given weak revenue projections, expansions will be limited to committee priorities that are evidence-based or tied to enhanced service delivery. Workload growth is not considered an expansion. Analysts shall avoid financing expansions with nonrecurring revenue. Generally, expansions not identified as a committee priority must be financed within current appropriation levels through reprioritization. All expansions must be tied to enhanced performance and explained in the budget document accordingly. Expansion FTE should be budgeted for a partial year if it is unlikely they will be filled by July 1, 2016.

Capital Outlay, Building Use Costs, and Space Allocation. To achieve greater efficiency with the state's limited resources, analysts should evaluate capital projects based on critical public health and safety, other initiatives in progress, and state and federal code compliance. Analysts shall evaluate the effectiveness of agency owned and leased space and operating budget implications, including maintenance and renewal costs in future years, space utilization standards adopted by the Capitol Buildings Planning Commission, lease costs, and square feet per employee, when reviewing requests for new facility construction, renovation, expansion, demolition, or leased space. Analysts shall review agency Infrastructure Capital Improvement Plans (ICIP), agency compliance with Executive Order 2012-023 (Facility Master Planning Guidelines) and Executive Order 2013-006 (Uniform Funding Criteria, Grant Management, and Oversight), LFC quarterly reports, and the progress and project outcome of significant capital appropriations included in the $1 Million or Greater Report authorized in previous years and progress toward completion of local projects funded between $300,000 to $999,999.

Information Technology Request. Given weak revenue projections, a limited number of the state's most critical IT projects will be considered for funding. Funding recommendations will be based on conformance with stated agency priorities, agency and statewide IT plans, the quality of the specific business case, and available funding. Analysts shall consider operating budget implications, such as ongoing maintenance, training, and impacts on operations, when reviewing requests for new or extended information technology (IT) projects. Staff shall review IT appropriations from previous years and monitor the progress and outcome of ongoing IT projects. Analysts must ensure all IT funding requests are submitted through established protocol (whereby requests are submitted directly to DFA, LFC, and DoIT using the "C2" request form separate from the agency's annual budget request) to ensure these requests receive the appropriate level of analysis prior to approval.

Agency Audit Reports. Analysts shall use the agency's financial audit reports in preparing the FY18 budget recommendation paying close attention to general fund reversions, unreserved/undesignated fund balances, and any long-term outstanding debt. Significant deficiencies and material weaknesses identified in the audit shall be reported to the LFC. Additionally, analysts shall identify significant, long-existing fund balances, barriers to expenditure, and potential reprioritization of accumulated balances.

VI. TAX EXPENDITURES

The committee shall review tax expenditures and earmarked revenues to identify uses of state funds that do not meet the intended purpose, are not cost effective, or are no longer necessary and can be redirected to higher priority uses. In particular, the committee will review health care tax expenditures in light of the changed health care landscape after the implementation of the Affordable Care Act and the expansion of Medicaid. In the 2016 legislative session, the state faced significant challenges crafting a budget due to declining revenue projections, and these challenges will likely continue in the 2017 legislative session. These budget affordability issues are prominent in health care, including the state's share of the cost of Medicaid expansion. Making the budget situation more difficult is the magnitude of the state's tax expenditures, many of which have not been reviewed for efficacy or efficiency, and some of which appear no longer necessary.

Revisiting some of the more costly tax expenditures and reducing or eliminating ones that do not offer significant benefits could free up funds to pay for essential state services. The healthcare industry is the fastest growing industry in New Mexico, but it is largely untaxed, impacting state revenues and tying up funds that could be better used elsewhere, including for state-supported health care services. Health care tax expenditures cost the state $344 million in FY15 and represent 28 percent of all revenues lost through tax expenditures.

VII. OTHER FINANCIAL ISSUES

In addition to agency operating budgets and revenues, analysts should consider other financial issues.

Medicaid. By the end of FY17, an estimated 925,000 New Mexicans will be enrolled in Medicaid, 263,000 of whom became eligible pursuant to the federal Patient Protection and Affordable Care Act (ACA), which expanded Medicaid eligibility for adults with incomes up to 138 percent of the federal poverty level beginning January 1, 2014. While early projected shortfalls for FY17 were largely avoided due to initial cost containment efforts and a moratorium on a federal insurers' tax, the outlook for FY18 remains a significant concern. In May the Human Services Department estimated an additional $60 million to $80 million in new appropriations from the general fund will be needed in FY18 for enrollment, utilization, and reduced federal support for the expansion population, which is decreasing to a maximum of 90 percent by calendar year 2020.

Analysts should evaluate cost-saving initiatives such as payment and delivery system improvement initiatives, appropriateness of various rate structures, changes in federal requirements, and consider ways the state can leverage Medicaid dollars for services that improve outcomes, such as Medicaid financed home visiting. Additionally, analysts should evaluate programs initiated or expanded with ACA such as care coordination, pay-for-performance and Centennial Rewards to ensure cost effectiveness and expected performance outcomes.

Public School Funding Issues. The more than $2.7 billion investment in public education continues to show slow progress in improving student achievement. Certain components of the formula are not aligned with improving student achievement, accountability for both formula funding and PED flow-through grant funding continues to be of concern, and districts are not able to compete with neighboring states when it comes to teacher pay. Priorities of the committee include alignment of the funding formula in a way that supports improved student achievement and closing the achievement gap, ensuring accountability for appropriations made for public education, and increasing compensation for school employees through broad-based, targeted, and performance-based compensation initiatives that will assist districts in recruiting and retaining the highest quality employees. Continued focus will be placed on the two education sufficiency lawsuits and federal special education maintenance of efforts requirements. Additionally, early childhood programs that promote literacy will again be prioritized, including Prekindergarten and K-3 Plus – both of which have demonstrated increased learning for participants.

Economic Growth and Workforce Development. New Mexico's economy has not yet recovered from the Great Recession and has not grown much for most of the past year. The state's workforce training and development programs are coming under increasing pressure to prepare and retrain citizens for current and prospective job opportunities, especially in light of underemployment and regional unemployment levels in New Mexico. However, these programs often overlap, duplicate administrative costs, are fragmented, and do not report on outcomes. Many other economic development programs and tax incentives focus on short-term results, ignoring long-term structural issues such as infrastructure and workforce education and readiness. However, nearly every survey of business executives and site selection consultants ranks these two issues as the most important for expanding and relocating businesses. Analysts shall review existing and proposed programs related to economic development and workforce training to address these concerns, improve accountability for recently approved funding, calculate the cost per job created when possible, and identify evidence based investments to improve agency coordination and reporting, reduce fragmentation, improve labor force quality, assist job growth, and promote increasing personal income levels.

Child Welfare. Although funding for early childhood initiatives increased over the last three years, early childhood programs are under increasing pressure to improve statewide quality standards which typically increase costs. Priorities for FY18 include targeting existing services to children birth to age 3. LFC analysis indicates children from birth to age 3 are most in need of continued growth of services. Additionally, funding must be invested in a deliberate manner so that communities can grow local capacity and infrastructure responsibly. Given the weak revenue projections, early childhood funding may need to be reprioritized to programs with the strongest outcomes. Other child welfare programs, such as child Protective Services, may benefit from second look at what is working in other states.

New Mexico continues to struggle to meet quality childhood program standards, such as the providers' level of technical skills, education, and stability among caregivers; workforce development for providers will be crucial to improving child welfare.

Behavioral Health. Concerns remain that the state has not fully recovered from disruptions to the behavioral health system which exacerbated the already existing challenges to access and quality care. Over the interim, the state's Legislative Finance Committee (LFC) and the Legislative Health and Human Services Interim Committee (LHHS) jointly requested additional information about the Human Services Department's efforts to ensure the behavioral health network is sufficient to meet the needs of the state's most vulnerable populations. Working together with HSD, analysts will analyze access, costs and expenditures, outcomes, and services available to best address gaps and improve outcomes with limited resources.

For non-Medicaid behavioral health administered by HSD’s Behavioral Health Services Division, analysts will assess changes as clients move from state-funded services to Medicaid-funded services and determine the best use for any additional savings realized. Additionally, analysts should assess the department’s plan for and anticipated costs and savings for the department to assume the administrative services functions from OptumHealth.