

Governor Terry McAuliffe Unveils Biennial Budget for FY 2019-2020 to the Joint Money Committees

~As prepared for delivery~

The Governor's Address to the Joint General Assembly Money Committees

December 18, 2017

Chairman Jones, Chairman Norment, Chairman Hanger, Chairman Ware, members of the General Assembly: Good morning.

I'm joined today by my wife, First Lady Dorothy McAuliffe, members of my Cabinet, and staff.

Also joining us are Governor-elect Ralph Northam, Lieutenant Governor-elect Justin Fairfax, and Attorney General Mark Herring. I thank them for being here today and for their service to the Commonwealth.

This is the last budget that I will present to you.

To be honest, I feel some sadness that our time together is coming to an end, but I do take heart knowing that all of you are even sadder to see me go. Yet, I know you will be in very capable hands with the Governor-elect and Secretary Layne.

Unfortunately, it's not just my final budget.

This will be Finance Secretary Ric Brown's final budget, too. Ric has been at the heart of this work for 47 years, serving governors of both parties and keeping the Commonwealth running in good times and in bad.

Ric, we're very sorry to see you go, but you've more than earned your retirement.

Dorothy and I wish you all the best in your next career as a semi-pro fisherman!

We wouldn't be here today if it weren't for the tireless work of Dan Timberlake and his entire team of financial experts.

I can't count the number of hours we've spent poring over budgets these past four years.

It's a grueling process, but one that they've taken on happily, and with great pride for the positive impact it can have on Virginia families.

We've certainly had our financial ups and downs in recent years, but today I am proud to be here to tell Virginia's comeback story.

When I took office in January 2014, we were facing a revenue shortfall of \$438 million, which led to a \$2.4 billion cut in the 2015–2016 biennial budget.

Most of the shortfall was caused by federal tax changes on capital gains and non-wage income, but it was also clear that Virginia's economy was struggling as a result of sequestration.

We needed to diversify – and fast. We needed to build a new Virginia economy that worked for everyone, and that could insulate us from the whims of Washington politicians.

There is no question the biggest drag on our economy was created by disastrous federal spending decisions, notably the sequester cuts which continue today.

Those arbitrary cuts reduced military contracts in Virginia by \$9.8 billion between 2011 and 2013, and wiped out a significant number of high-paying jobs.

Since that difficult budget, my team and I have worked hard to reduce Virginia's reliance on federal spending, which has resulted in both big surpluses and big deficits over the past few years.

Through all of these highs and lows of economic gains and losses, I have remained committed to two important goals.

First, I pledged to work with you to pass balanced budgets that invest in priorities that are essential to economic growth and opportunity for all Virginians. I'm proud to say that we've kept that promise.

Together, we have:

- Invested a record amount in our education system to build a more talented and skilled workforce;
- Increased access to both physical and mental healthcare, especially for our most vulnerable citizens;
- Put our transportation dollars to much better use for taxpayers; and,
- Acted responsibly to protect Virginia's environment and natural beauty, to better maintain clean air and water for our citizens.

The bottom line is that by working together we have taken significant action to improve the lives of Virginians and regain solid financial footing.

The second commitment I made was to build a new, diversified Virginia economy, so that we could get in front of the challenges facing Virginia.

This new economy would focus on growing industries that are less reliant on federal decision-making, such as cybersecurity, bioscience, data analytics, communications, and unmanned systems.

Moreover, we would view the entire world as our marketplace.

With more than 95 percent of the world's customers located outside the United States, competing beyond our borders is now an economic imperative.

I am proud that I have kept these promises. For four years, I have worked tirelessly to promote our existing businesses, attract new investment, and increase trade.

I have made thousands of economic development calls on prospective clients and undertaken more economic development trade missions to other nations than any other Virginia governor in history.

And the numbers speak for themselves.

To date, my administration has announced more than 1,078 economic projects that will bring in more than \$19.4 billion in capital investment. That's billions more than any administration in Virginia history. Two-thirds of that investment is still in the permitting stage and will create more opportunity for years to come.

In addition, I recently announced the economic impact of our agriculture and forestry industries has reached \$91 billion annually. That's a 30 percent increase from when we took office.

We've also overseen the creation of 207,000 new jobs.

I'd remind you as well that unemployment is down to 3.6 percent – from 5.4 when I took office – and marks the lowest rate we've seen nearly a decade.

Every single city and county in Virginia has seen a drop in their unemployment rate. And our initial unemployment insurance claims have reached a 44-year low.

However, there's still more work to do, but there is no question that by working together, we are leaving Virginia's economy better off than we found it.

We can continue to build on this progress by finding common ground on the issues that we all care deeply about and that directly impact our economic future.

That means: investing further in public education, workforce training, infrastructure, and healthcare.

It means using our limited resources wisely to secure the things we'll continue to need in the future, including a highly skilled workforce and a high quality of living.

In this balanced budget, I am giving you a roadmap to take our achievements to the next level.

And because we've gained ground economically, I am optimistic that we have the resources to do so.

When I last spoke with you in August, I announced a surplus in our general fund revenue collections and told you the Virginia economy had continued to expand, especially among higher-paying jobs.

At that time, I also gave a very stern warning about the budget I initially had expected to unveil today.

However, I am happy to report that our outlook – and this budget – are far more positive than they were just a few months ago.

For fiscal year 2017, general fund collections exceeded the official forecast by more than \$134 million.

This was seven-tenths of a percent within the forecast – the smallest forecast error in 10 years.

After we factor in transfers to the general fund from other sources, we ended the fiscal year with an additional \$2.5 million, bringing the total to \$137 million above our budget assumptions for the general fund.

That was driven by strong growth in payroll withholding and corporate income-tax collections.

Now, before you start planning that rooftop swimming pool on the new General Assembly building, remember: the entire surplus is already committed.

As I explained in August, it will go toward the Water Quality Improvement Fund and our cash reserve, in addition to offsetting debt for capital projects.

The Appropriations Act also called for an additional deposit of \$35 million from the general fund in FY 2018.

Roughly \$31 million of this appropriation was expected from the Virginia Tax Amnesty Program.

The estimated revenues from the program fell short of expectations.

During budget deliberations, unfortunately, the General Assembly revised the estimate of general fund revenue from the program upward from \$31 million to \$89 million.

However, only \$42 million is estimated to be collected, creating a hole of \$47 million. That leaves no additional money for the reserve.

As a result, the current amount required to be deposited to the reserve is \$60.4 million. But given the significant uncertainty we still expect at the federal level, I believe it's wise to put every available dime we have into this rainy-day fund.

Let's not forget why we created this cash reserve in the first place.

Earlier this year, S&P Global Ratings affirmed our AAA bond rating, but they changed our rating outlook from "stable" to "negative."

They did that for two reasons.

First, they believed that Virginia could face economic headwinds in the future due to continued uncertainty in Washington.

Second, and in light of the first issue, S&P is concerned about our budgeted withdrawals from the Revenue Stabilization Fund during the current biennium.

To address these concerns, we must build reserves to protect us against the risks associated with the federal government and national economic uncertainty.

And even though we are taking a conservative approach that will help insulate us from potential future shocks, we are still delivering a structurally balanced spending plan that invests new money in key priorities.

As you know, my team began the process of reforecasting general fund revenues shortly after the close of fiscal year 2017, which involved a review by our two advisory boards.

The forecast calls for our nation's GDP to continue to grow at an average of 2.3 percent over the next three fiscal-year period, with no recession.

Both employment and personal income are forecast to continue to grow at moderate rates through fiscal year 2020.

In addition, inflation is expected to remain at, or below, 2.5 percent after posting a 1.9 percent increase in FY 2017.

The impact of federal tax reform is still largely unknown, and will remain so until a final bill is enacted, if at all.

At the state level, personal income is forecast to grow by 3.3 percent in FY 2018, up from 2.4 percent the year before, and job growth is expected to increase at a similar rate this year, too.

That means more Virginians will secure good-paying jobs and will in turn help us make the investments we need to provide quality education, affordable healthcare, and workforce training for 21st century jobs.

All of these projections give us a reason to be very optimistic, but due to ongoing national economic uncertainty, we are still using a conservative revenue forecast.

For example, we have continued to place a collar on the projections of non-withholding income tax receipts.

This acts as a hedge against the natural volatility of these non-withholding receipts. In fact, our revenue surplus in fiscal year 2017 would have been a revenue shortfall had this collar not been in place.

In total, the final general fund forecast for the next biennium is just over \$42 billion.

This is based on total general fund resources growing at 3.8 percent for FY 2019, and 3.9 percent for FY 2020.

Given this forecast, today I am proposing a total of \$156 million from the general fund be deposited into the reserve in FY18.

Another \$50 million in FY19 and \$221 million in FY20 will be deposited to the reserve – well above my stated goal in August of \$121 million.

Over that three-year period, my recommendations will grow the cash reserve to \$427 million, or a full two-percent of the total of my general fund operating appropriations in fiscal year 2020.

This will be welcome news for our rating agencies.

With the new resources provided by our revised forecast, many of my spending recommendations will fund vital public services like the Standards of Quality for public education and the existing Medicaid program. These are two of my top priorities in this budget.

Our public schools are among the best in the nation and they serve as the foundation for our future workforce and economic vitality.

My team and I have worked hard to transform how we educate our children and prepare them for the new Virginia economy.

We've secured historic funding for public education, redesigned the high school experience, and helped expand access and affordability for higher education.

But we do still face some headwinds.

One of the toughest obstacles to providing that quality education is our ability to attract and retain our teachers, particularly at our most at-risk schools.

I announced last week that my budget funds several initiatives to address this growing crisis.

These proposals include funding to automate the teacher license application system and to support principal recruitment and retention in our hardest-hit school divisions.

In addition to addressing that urgent problem, my budget fully funds re-benchmarking of the Standards of Quality, which equates to \$436 million over the biennium.

We're also providing an additional \$7 million to support programming for our at-risk students and \$7.6 million to provide state support for a full-time principal – for the first time – in every elementary school.

I've also included \$1 million in new funding for two-week cybersecurity camps dedicated to exposing high school students to careers in this rapidly growing industry.

In total, this budget provides more than half a billion (\$516M) in additional funds for public education.

I'm proud of the work we've done to expand opportunity in the classroom, but we also know that our kids can't be hungry to learn if they're just plain hungry.

On that point, I want to recognize the First Lady for her work to connect our students with nutritious meals.

Thanks to her leadership, and the many partners she's brought in to help, we served more than 10 million more school breakfasts this year than in my first year in office, bringing an additional \$22 million in federal funding back to Virginia schools each year.

But we're not stopping there.

That's why I've included \$2 million over the biennium to support our breakfast incentive funding, which has dramatically improved participation in our high-need elementary schools.

It's time that we extend that funding for our middle and high schools as well so we can end childhood hunger in Virginia once and for all.

I've also included more than \$7 million for the Virginia Grocery Investment Fund, which will bring much-needed capital to our food deserts to expand food access and spark economic development.

Higher education is also critical to maintaining and strengthening Virginia's workforce of the future.

We've leaned in to provide new opportunities for Virginians to access a four-year education, but also for those who want to earn high-demand workforce credentials in less time, and for less money.

To help keep higher education affordable and accessible for all students, I am proposing an additional \$48 million for financial aid.

To support institutions with the least resources and those with the greatest growth, I've provided an additional \$35 million.

Through this funding, schools will be under less pressure to raise future tuition and fees, protecting the pocketbooks of our students and their families.

To help keep equipment at the institutions of higher education up-to-date, \$166 million in debt for the biennium is included for the Higher Education Equipment Trust Fund.

I'm also increasing funding for the New Economy Workforce Credential tuition assistance program by \$4 million to address the high demand of students wishing to participate in the program.

During FY 2017, the program served 5,050 students, with over 90 percent completing the academic portion of the program.

And it has nearly tripled the number of people who earned credentials at Virginia's community colleges and higher education centers.

Those are the graduates who are going to fill the high-skilled jobs that we're creating in 21st century industries.

By supporting that successful new program, we are putting more Virginians to work in good jobs with little to no student debt.

It's a small investment from the Commonwealth, with a big pay-off for Virginia's workers.

Finally, higher-ed will also receive \$217 million in maintenance reserve funding to help maintain existing institutional facilities, and to help address a variety of infrastructure and security-related needs.

This is the largest amount of maintenance reserve funding ever provided to our higher education system.

Once our students graduate – whether it's with a four-year degree or a 10-week credential – we want them to find a good job right here in the Commonwealth.

That's why we are continuing to invest in initiatives that will boost our efforts to grow and diversify our economy.

I am proposing \$7.5 million to launch a customized, turnkey workforce recruitment and training incentive program to secure high-impact, high-quality economic development projects. This will be modeled after other nationally recognized workforce programs.

Through this initiative, workforce experts at the Virginia Economic Development Partnership and the Virginia Community College System will collaborate to improve recruitment, screening, and development and delivery of customized training – all at no cost to participating companies.

This new incentive will be available exclusively to projects that include a new location, or a substantial expansion of an existing location, and will create high-wage jobs.

By doing so, we will extend the reach of these dollars to provide opportunities in communities that need it.

My budget also provides \$4 million for the grant program that incentivizes companies to locate new maritime-related employment centers, or expand existing centers statewide, in order to encourage the growth of the Port of Virginia.

In addition, my budget will help the Port of Virginia plan for the deepening of the Norfolk Harbor and Elizabeth River channels.

This planning is necessary to gain access to federal funds to dredge these channels.

With deeper channels, the Port of Virginia will be able to accommodate the largest container ships and maintain its competitive edge against other ports on the east coast.

As you know, the Port was unwisely put up for sale during in 2012 after experiencing five straight years of losses.

Following a \$670 million state investment, today it's one of the busiest container ports on the East Coast, has made money for the past three years, and is well-positioned for future growth.

The Port is just one of the success stories we've seen during our transformation of the Commonwealth's transportation system.

I hope we can someday soon tell that same story about WMATA. The Metro system is a lifeline for the Northern Virginia economy, and it remains critical to our economic competitiveness.

Along with VRE, it supports 130,000 jobs and 85,000 families in Northern Virginia.

But we all know that system is just plain broken. And it represents a significant threat to our economy if we don't fix it, and quickly.

Instead of agreeing to a regional general sales tax, which would disproportionately burden Virginians, I have instead included dedicated, ongoing funding to provide Virginia's \$150 million share of the \$500 million needed to keep the system running.

This shouldn't be a tough call, given that the General Assembly has previously voted to approve that funding.

And of course, our funding is contingent on DC and Maryland paying their share, too.

Without that funding, Metro's General Manager has said he will need to cut service as of July 1 next year. I've said it time and again: if you cut service, it will be a death spiral for Metro. People won't ride if it's not reliable.

Its problems didn't happen overnight, and any solutions will take time to work, too, but we cannot delay action any longer.

That's why I support the temporary reform board recommended by former Transportation Secretary Ray LaHood, who did an objective top-to-bottom review of Metro this year.

With a more streamlined governance structure, it will be able to make the tough decisions needed to get this vital system back on track.

In addition to Northern Virginia, we need to support mass transit across the Commonwealth.

These systems help reduce the need for road construction, cut the number of vehicles on the roads, and provide more options to commuters and visitors.

The state funding we've been using to support the capital needs of our transit systems will no longer be available come fiscal year 2020.

Given this reality, my budget includes the authorization to issue \$110 million in Commonwealth Transportation Capital Projects Revenue Bonds for mass transit projects in FY 2020 to maintain the state's commitments to these services.

We need robust, sustainable public-transit systems to support the growth and diversification of our economy.

They also help us reduce our carbon footprint and car culture, which drive other costly investments we must continually make – which is everything from road maintenance to climate change mitigation.

As we shift toward a 21st century model for economic growth and transportation, we remain laser-focused on developing a renewables industry that can support our rising energy demands.

Solar energy, in particular, is an essential part of our efforts to diversify our energy mix.

To that end, my budget includes \$2 million to support the development of the solar industry in Virginia. Through a revolving loan program and a loan loss reserve program, financing for solar projects will become more accessible.

These initiatives build on important investments in the solar industry across Virginia.

When I came into office, it's fair to say that Virginia was behind the curve on solar. We had only 17 megawatts in 2014. Today, we have over 2,600 megawatts installed or under development today.

This isn't just good for the environment – it sends a message to job-creators, too.

These kinds of investments in clean energy have helped us attract big-name companies like Facebook, Google, and Amazon.

These actions clear the way for us to attract new businesses and create high-paying jobs.

But as I've heard from job-creators around the globe, they want to go where they'll have access to a healthy workforce, too.

If we're going to continue to bring in these companies, we will need to strengthen our healthcare system and expand access to it.

Sadly, there are still nearly 400,000 Virginians who lack access to basic healthcare because they fall in the coverage gap.

Each year during my term, I've gone out to the RAM clinic in Southwest Virginia and I meet many of these folks.

That once-a-year clinic provides life-saving care, but in America, our citizens should be able to access healthcare wherever and whenever they need it – without facing the prospect of financial ruin.

I've fought to expand coverage to these Virginians every year for four straight years.

As you know, that effort has repeatedly failed in the General Assembly, leaving hundreds of thousands of our friends and neighbors without access to basic care.

We've filled that gap the best we could through my Governor's Access Program and other measures to meet these needs. But we can – and should – be doing more.

That's why my budget will expand Medicaid for the Commonwealth of Virginia.

Since the Affordable Care Act became the law of the land, Virginia has left more than \$10.5 billion of our own tax dollars on the table, rather than bring them back to Virginia to benefit those who need it most.

Through Medicaid expansion, we will be able to offer coverage to the nearly 400,000 Virginians who not only desperately need it, but they are entitled to it and we've already paid for it.

The cost of providing these additional services will be funded through an assessment on private acute care hospitals.

In return, hospitals will see reduced costs for indigent and uncompensated care, since more of their patients will now be covered.

It makes sense that they will be expected to help cover a portion of the state's cost to serve a population that will now be the source of significant revenue for these hospitals.

This expansion of Medicaid will allow Virginia to achieve substantial savings, because the new federal funding will replace state-supported indigent care costs, services provided by Community Services Boards, and inpatient hospital costs for incarcerated individuals.

From a budgetary perspective, across the executive branch there is a modest general fund cost of about \$612,000 in fiscal year 2018, which will result in a savings of \$421.7 million over the upcoming biennium.

In addition, this will unlock over \$3.2 billion in federal funds over the biennium, which will run through our economy.

It's long past time to take this commonsense, fiscally responsible step.

Without bringing these dollars back to Virginia, it makes it impossible to fund all of our shared priorities, like the SOQs and our cash reserve.

Unfortunately, while our Medicaid expansion proposals have languished, we've continued to see growing costs in physical and mental health care.

This budget fully funds mandated services, including the revised Medicaid forecast, foster care and adoption programs, and Children's Services Act caseloads.

In total, the increased cost for these services is \$743 million over the biennium.

Consistent with the 2012 agreement with the U.S. Department of Justice, this budget includes funding to support 825 additional Medicaid waiver slots over the course of the biennium for individuals with intellectual disabilities, including 70 slots set aside to transition people back to their communities.

We've budgeted \$14.5 million in FY 2019 and \$30.5 million in FY 2020 for these slots. An additional 50 emergency slots are also funded to provide flexibility during crises.

The children's insurance programs, known as FAMIS and M-CHIP, will soon run out of funds due to federal inaction.

Last week, that forced me to notify 68,495 Virginia children and 1,114 pregnant women who stand to lose coverage if Congress fails to reauthorize funding for CHIP.

Just imagine – two weeks before the Christmas holidays — thousands of low-income Virginians getting a notice in the mail that their children's healthcare is at risk.

To me, this is absolutely unconscionable. It's nothing short of malpractice on the part of Congress.

However, given the immense pressure Congress is under to act, and its history of doing so only under the threat of a deadline, our projections assume it will be reauthorized before Virginia runs out of its portion of federal funding on January 31st.

That includes \$49 million from the general fund and \$91 million in nongeneral funds over the three-year period.

The budget also provides \$38 million in general fund dollars, and nearly \$4 million in nongeneral fund dollars over the biennium to cover increased medical costs for inmates, and \$5 million in FY 2018.

We also recognize that there is significant work yet to be done to address crises related to mental health and opioids, despite great advancements that we've made in the past four years.

As such, my budget builds on our recent achievements by expanding same-day access to all 40 of our Community Services Boards.

As I heard from the leadership at the Giles County clinic last week, that option can be a life-saver for someone who has finally worked up the courage to seek help.

If they are told to come back another day, unfortunately we know that there might not be another day.

We also provide funding for two assisted-living facilities and for supportive housing for people currently in our mental health hospitals who can function in less restrictive settings.

We fund the operating costs for the new expansion of Western State Hospital.

And we provide \$11 million in funding to begin primary care screening and monitoring at the Community Service Boards, in keeping with last year's legislation.

Beyond direct treatment, this budget also provides \$1 million for the creation and expansion of mental health dockets in jurisdictions with high caseloads.

These resources will allow courts to identify individuals with mental illness who can be safely supervised and treated in the community.

The budget also provides \$2.9 million to establish special units and programs for seriously mentally ill inmates.

Too often, people with mental health issues wind up in jail, the emergency room, or homeless. These Virginians shouldn't face that dangerous and costly cycle when we have the knowledge and tools to help them.

As we all know, the opioid epidemic has reached crisis proportions in virtually every region of the country and this commonwealth.

Additional resources are absolutely necessary if we hope to turn the tide on this issue.

My budget increases our resources to combat this problem in several ways.

It provides:

- \$10 million to support medication-assisted treatment for individuals who seek help with opioid addiction, through our Community Service Boards;
- Nearly \$2.5 million for supportive housing for pregnant women and mothers dealing with addiction and residential opioid treatment programs for nonviolent offenders;
- \$1.2 million to increase staffing at the Department of Forensic Science to reduce its opioid-related backlog; and,
- Funding to expand drug courts.

All told, this budget increases our resources to combat the opioid epidemic by \$17.8 million from the general fund and \$350,000 from nongeneral fund sources.

Our hearts break for the 1,100 Virginians who died of an opioid-related overdose last year and their families.

We must take these smart additional steps to save lives today and get folks clean, healthy, and back to work.

In addition to Medicaid and behavioral health care, the Commonwealth also operates our veterans care centers and health departments, and we provide funds for private and nonprofit organizations to offer rehabilitative and safety-net services.

My budget includes \$45 million from the general fund and \$47 million in federal and special funds for these purposes.

These funds will ensure adequate training and pay for personal care attendants, help to implement electronic health records, and support the construction of two new veterans care centers that I broke ground on this fall.

This isn't just the right thing to do for our veterans, but it's a necessity if we're going to remain the best state in the nation for our veterans, military service members, and their families.

While I am very proud of all of the many priorities we've taken care of in my final budget, this document is only as good as the 110,000 state workers that carry out its vision.

That's why I am so proud to give them one parting gift this holiday season, in recognition of their work and dedication to our Commonwealth.

My budget funds a two-percent raise in compensation and offsets health premiums for our hard-working state workforce. This will be the third pay raise for state employees during my term, and reflects my commitment to building a strong and sustainable workforce.

This pay raise also means that our teachers, law enforcement, state agency workers, and more will not have to choose between serving their communities and sufficiently providing for their families.

And we've been able to make this investment while still fully funding the retirement fund and other post-employment benefit programs.

This raise, and the many other new investments we make, are only possible because we've worked together to put our state finances back on solid footing.

When I took office, I inherited a \$2.4 billion shortfall and an economy that was too reliant on federal funding.

Today, I am proud to leave you with a structurally sound budget that prepares us for inevitable future storms, meets every single one of our commitments, and builds on the work we have done together to create a diversified economy with a well-educated and healthy workforce.

With your partnership, we have built the new Virginia economy. I hope you will use my final budget as a roadmap for continued economic success.

It has been a tremendous privilege to serve as your Governor.

I wish you all the best of luck in the upcoming legislative session and a happy holiday season.

May God bless you and our great Commonwealth.

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