

REMARKS
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DEPARTMENT OF FINANCE AND ADMINISTRATION
STATE OF ARKANSAS
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Chairman Yarmuth, Members - Thank you for the opportunity to speak to you today. Thank you to Ranking Member Womack for the invitation.

I would like to share with you a brief overview of the budgeting and planning process in Arkansas.

To do this, we must go back to the late 1920s and early 1930s. Arkansas was experiencing the great flood of 1927, a significant amount of road debt that was transferred to the state from counties and the overall Great Depression.

As a result, Arkansas was struggling to maintain state services and defaulted on its debt.

A variety of new taxes were implemented around this time to address the state's budget needs.

However, this didn't solve the issue and the state needed a long-term solution. This was established through Amendment 20 to the state constitution.

Amendment 20 states: Except for the purpose of refunding the existing outstanding indebtedness of the State and for assuming and refunding valid outstanding road improvement district bonds, the State of Arkansas shall issue no bonds or other evidence of indebtedness pledging the faith and credit of the State or any of its revenues for any purpose whatsoever, except by and with the consent of the majority of the qualified electors of the State voting on the question at a general election or at a special election called for that purpose.

In simple terms, we are constitutionally barred from borrowing money without a vote of our citizens. Arkansas maintains a true balanced-budget approach to funding state programs. We do not commit state dollars until we have those dollars in hand and available to spend.

Under Arkansas law, it is my duty as Secretary of the Department of Finance and Administration to see that the funds on hand and estimated to become available to each state agency are sufficient to maintain state services on a sound financial basis **without incurring a deficit.**

As a consequence, we have developed programs and practices which build strength and financial reserves when times are good and safeguard our more important programs when times are bad. We must be prepared for whatever the future may bring.

Our annual budgeting process doesn't just allocate dollars to state programs – it also prioritizes spending. Agencies define spending priorities by applying an A, B,

C or D to each category to represent its importance. Through this process, agencies make tough decisions but also have a clear understanding of what will take place in all budget scenarios.

If the economy fails or revenues drop, we have a plan in place – in law actually – which will safeguard our most vital programs and cut those which can afford to be cut.

Our state's highest priority remains K-12 public education. It is funded first. That's why, during the Recession in 2008-2009, Arkansas not only did not cut state funding for public schools, we actually increased funding for our schools.

Lower priority programs – such as capital projects or major program expansions – are funded in Arkansas last and only if funding is available. If funds dry up, these programs are simply not funded.

Another consequence of being barred from taking on debt is our need to build fund balances in support of our most important programs. Today, Arkansas maintains trust funds to support public education, Medicaid, employee pay raises and other programs. These trust funds exist to delay or avoid the need to cut budgets to these programs if revenues fall short. They roll forward from year to year, growing when times are good to help mitigate damage when times are bad.

One concern that I would like to share with you is the increasing amount of federal funding for state programs being granted through a competitive process

with a limited number of grant awards. This approach to distribution of funds often places smaller states like Arkansas at a disadvantage as some formulas are based on population. Additionally, the time frame in which a response is required may limit ability to formulate a plan that truly reflects the needs of the state.

In order to safeguard state programs in the case of a recession and allow us to remain competitive when opportunities arise, Arkansas has recently invested in a series of reserve funds. Under Governor Asa Hutchinson, we maintain three such funds – the Restricted Reserve Fund, the Long-Term Reserve Fund, and the Rainy Day Fund. Each has a unique role to play.

Since Governor Asa Hutchinson took office in January 2015, three of the largest individual income tax cuts in the state's history have been implemented. This includes a middle-income tax cut in 2015, a cut for low income Arkansans in 2017 and an upper income cut that was effective January 1, 2020. These historic cuts, which reduced income taxes for each tax paying Arkansan, also reduced state revenue by hundreds of millions of dollars. Under Governor Hutchinson, income tax was also eliminated on military retirement and the grocery tax was reduced from 1.5 percent to slightly more than one tenth of a percent.

However, all these tax cuts were absorbed without any changes or reductions to state services due to responsible budgeting and an economy that continues to expand.

While the Arkansas economy remains in expansion, every year we are prepared for all scenarios in the economy. These scenarios consider reduced growth rates in key economic assumptions as we also check for model weaknesses in national forecasts.

Federal funds remain a significant component of the day to day operation of state services. In Fiscal Year 2019, which ended in June 2019, federal dollars accounted for 29% of our total expenditures. The largest portion, approximately \$6 billion, supports our Department of Human Services, which administers the state's Medicaid program.

While the largest portion of Federal funds are directed to Medicaid, the state Department of Education also receives a significant amount, approximately \$539 million in Fiscal 2019. The Arkansas Department of Transportation followed with \$506 million.

The Arkansas budget is presented each biennium. As we prioritize programs and projects, we do our best to anticipate any potential changes in Federal funding as this does account for almost one third of our overall budget. However, with the federal government operating on a continuing resolution, we do feel a responsibility to dedicate resources to the ongoing development of contingency plans. A shutdown can have an immediate impact on our budget and more importantly, the day to day services we provide to Arkansans. Federal funds are critical to the stability of our budget over both the short term and the long term.

We remain in close contact with our delegation and this is an issue we have shared with them.

Leaders of Arkansas' departments that administer our Federal funds report strong working relationships with Federal agencies.

From education to health to highways, we appreciate and value the positive impact of Federal funds throughout the state.

We must also acknowledge Federal Funds' crucial role in addressing natural disasters and emergencies. In 2019, Governor Hutchinson and President Trump declared an emergency in the state due to immense flooding of the Arkansas River. While Arkansas maintains both a balanced budget and several reserve funds that can significantly help in these scenarios, a disaster of this scale requires immediate support in the form of Federal funds. Due to President Trump's declaration and the work of FEMA, federal funds were made available at the time and remain available today for those recovering from the damage caused by this event. I believe the State-Federal partnership is at its best in these times of need. From Washington D.C. to those in Arkansas impacted by these events, it simply becomes people helping people. We are grateful for the decisions made here that allow for this partnership. It was Federal funding that allowed the establishment of the McClellan Kerr Navigation System in the early 1970s which has prevented a repeat of Arkansas' 1927 flood, the worst in the state's history and among the worst in the United States.

As a result of the 2019 flooding, Governor Hutchinson established a Levee Task Force to study the state's 92 levees and provide recommendations. Those recommendations were released in December. While several of the recommendations may be incorporated without outside assistance, we know Federal funds will be required to effectively maintain safe levees. Before making any request at the Federal level, it is up to the state to determine specifically what we hope to accomplish, and the amount needed to responsibly address this need. Understanding the importance of making this type of an ask of the Federal government, as a state we always carefully consider every need along with our own resources before bringing this before you.

Again, thank you for the honor of speaking to you today. I look forward to answering any questions.