



FISCAL FOCUS  
**KEEPING  
 THE PROMISE:**

*Children's Initiatives Fund/  
 Kansas Endowment for Youth*



# Creation of the System

The CIF and KEY Fund were created as a result of nationwide tobacco litigation in the late 1990s and the ensuing settlement that promised to provide \$206 billion to states, .83 percent (\$1.6 billion) of which would go to Kansas over a 25 year period.<sup>i</sup>

## The Tobacco Settlement

Kansas was one of a number of states that filed suit against the big tobacco companies in the 1990s to recoup money lost because of smoking-related Medicaid spending. After Florida, Minnesota, Mississippi and Texas individually settled their cases out of court, the tobacco companies and remaining states reached a settlement called the Master Settlement Agreement (MSA). The agreement was signed on November 23, 1998, by 46 states, including Kansas.<sup>ii</sup>

The agreement imposed a number of restrictions on the participating tobacco companies and required them to make \$206 billion in payments to the states over 25 years. A schedule for the payments was included in the agreement along with provisions for adjustment, reduction and offset. The agreement also compelled states to adopt and enforce legislation aimed at protecting participating tobacco companies from losing market share to non-participating companies.<sup>iii</sup>

## New Futures Task Force

Once the Master Settlement Agreement was reached, Kansas lawmakers set out to determine how the Kansas share of tobacco dollars would be spent. In January 1999, legislative leadership appointed a special task force for this purpose called the “New Futures Task Force.”<sup>iv</sup> The resulting legislation created the KEY Fund and CIF and assigned the Kansas Children’s Cabinet to oversee them.

## KEY Fund and CIF Laws

Under the system created by this legislation, tobacco dollars received by the state go directly to the KEY Fund. The KEY Fund serves as an endowment for the long-term benefit of funding children’s programs. The KEY Fund is invested and managed by the Kansas Public Employees Retirement System. Each year, a transfer is made to the CIF to support children’s programs. Transfers from the KEY Fund to the CIF are capped at \$45 million, plus a 2.5 percent annual inflation factor.<sup>v</sup>

### THE FLOW OF TOBACCO MONEY TO CHILDREN’S PROGRAMS



# Legislation highlights

## Kansas Endowment for Youth Fund (K.S.A. 38-2101)

- All revenues resulting from the Master Settlement Agreement must be credited to the KEY Fund.
- All revenues deposited in the KEY Fund should remain in the fund and serve as an endowment unless they are transferred to the CIF or used to support operating expenses of the Kansas Children’s Cabinet or the cost of investing the KEY Fund dollars.
- KEY Fund transfers are subject to appropriation.

## Children’s Initiatives Fund (K.S.A. 38-2102)

- The CIF must be used to provide additional funding for programs to benefit the physical and mental health, welfare, safety and overall well-being of Kansas children.
- CIF money may not be used to replace or substitute moneys appropriated from the State General Fund (SGF) in the previous year.
- An emphasis is to be placed on data-driven and outcomes-based programs when determining which programs are funded by the CIF.
- CIF payments are subject to appropriation.

## Transfers (K.S.A. 38-2102)

- On July 1, 2000, the first \$70.74 million from the KEY Fund is transferred to the State General Fund and \$30 million from the KEY Fund is transferred to the CIF.
- On July 1, 2001, \$40 million is transferred from the KEY Fund to the CIF and \$10 million is transferred from the KEY Fund to the State General Fund.
- On July 1, 2002, \$45 million is transferred from the KEY fund to the CIF.
- On July 1 of each succeeding fiscal year, 102.5 percent of the amount transferred to the CIF in the previous year is to be transferred from the KEY Fund to the CIF.
- The Legislature has the ability to increase or reduce the amount of these transfers based on higher or lower tobacco revenues for the year.

## Children’s Cabinet (K.S.A. 38-2103)

- The Children’s Cabinet must review, assess and evaluate all uses of CIF moneys.
- The Legislative Post Auditor will conduct performance audits of programs receiving CIF moneys at the request of the Kansas Children’s Cabinet.
- The Children’s Initiatives Accountability Fund is created to support the cost of evaluating and auditing the use of CIF moneys.

# Trends

## KEY Fund & CIF

### Tobacco Dollars Received by Kansas

The complex nature of the Master Settlement Agreement payment schedule and adjustments, reduction and offset has left state officials uncertain of the amount of tobacco payments each year. The combined average annual tobacco receipts and interest earnings since 1999 is \$56.3 million. However, this amount has fluctuated between a low of \$46.9 million in FY 2007 and a high of \$72.2 million in FY 2009.<sup>vi</sup>

### KANSAS TOBACCO REVENUE AND INTEREST EARNINGS



### Funds Diverted from the CIF

Despite the fact the state made a commitment to fund early childhood programs, on several occasions since the inception of the KEY Fund and CIF, tobacco dollars have been transferred to the State General Fund instead. Although some of these transfers were a part of the original plan for the tobacco dollars, the majority of transfers were a departure from the statutory charge for the state's settlement agreement revenues. In fact, over the first 10 years of state payments under the Master Settlement Agreement, \$137.3 million were diverted away from the KEY Fund to the State General Fund. In real dollars this would have been closer to \$216 million if the tobacco money had been allowed to remain in the KEY Fund and earn interest.<sup>vii</sup> This left the KEY Fund with minimal balances over the years and undermined the original concept of an endowment for children's initiatives.

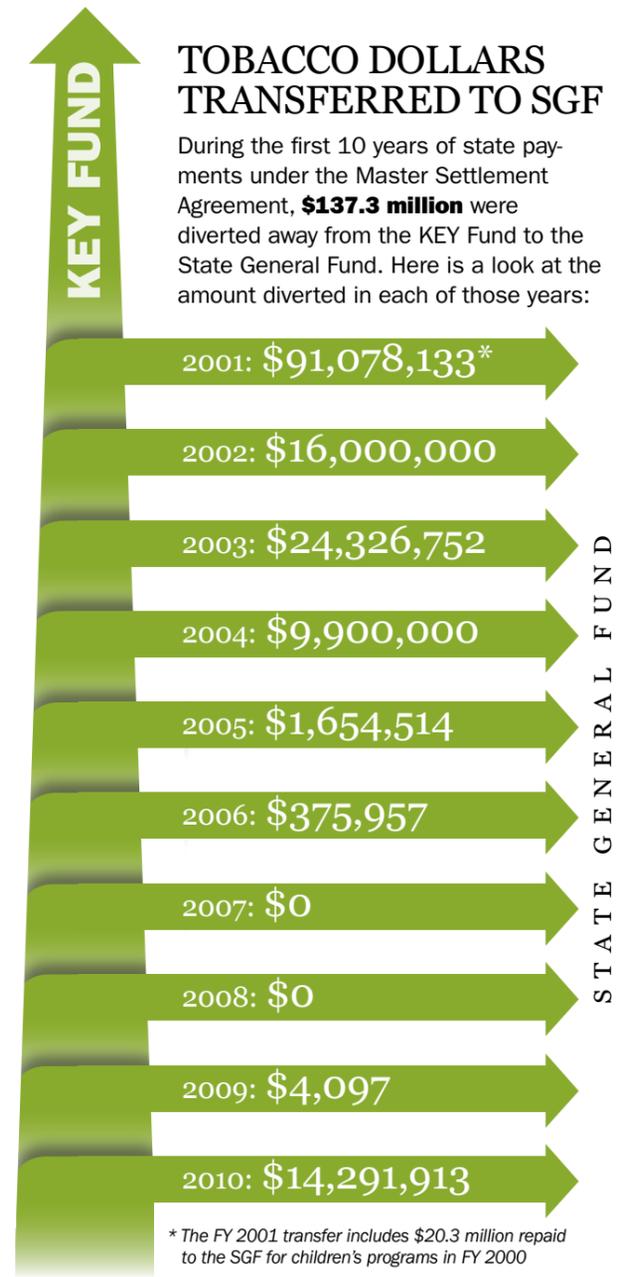
# Trends

## KEY Fund & CIF

The CIF provides funding for a wide range of services for young children. Approximately 200,000 – roughly one-third of the state's children – were served in Fiscal Year 2011 by programs that rely on CIF dollars.

Since the inception of the system, the number and type of programs funded through the CIF have varied from a low of 16 programs in FY 2000 to a high of 26 programs in FY 2009. Most recently, lawmakers appropriated CIF funding for 19 programs administered by three state agencies: the Kansas Department of Health and Environment, the Kansas Department of Social and Rehabilitation Services and the Kansas Department of Education.<sup>viii</sup>

While most of these programs fit the legislative mandate to provide additional funding for programs benefitting children, others appear to conflict with the prohibition against supplanting current State General Fund dollars with CIF dollars. For example, the Parents as Teachers (PAT) program began as a program entirely funded by the State General Fund. Since the CIF was created, Parents as Teachers has received varying levels of support from the CIF. However, under the approved FY 2012 budget, the program will receive all of its state funding from the CIF, essentially supplanting its State General Fund money with CIF funds.



SOURCE: The Governor's Budget Report, FY 2004 – FY 2011

# The future of the KEY Fund & CIF

## Focus on Early Childhood

Investing in early childhood programs gives the state the most value for its dollar. In fact, according to an economist at the Federal Reserve Bank, every dollar invested in quality early care and education saves taxpayers up to \$7 in future costs for reduced grade retention, crime and other public assistance.<sup>ix</sup> Research shows that brain growth is most rapid during the first three years of a child's life. This is when a child acquires the ability to think, speak, learn and reason.<sup>x</sup> By providing quality early childhood education and health services, which are critical to strong child development, we will reduce the need for more costly remediation in the education and criminal justice systems in the future. Early childhood programs should take priority when faced with limited resources.

## Commitment to CIF Programs Regardless of Tobacco Revenues

In 2011, lawmakers restored a shortfall created by lower-than-anticipated tobacco revenues using State General Fund dollars. Before this time, tobacco money had been diverted to the State General Fund but the State General Fund

had never been diverted to the CIF. With a two-year tobacco shortfall of \$8.3 million, lawmakers faced eliminating funding for one or more programs under the CIF or imposing an across-the-board cut of 17.5 percent for programs receiving CIF dollars in FY 2012. By transferring State General Fund dollars to the CIF to cover the shortfall, lawmakers preserved funding for key children's programs. An ongoing commitment to children's programs is important regardless of tobacco revenues.

## Development of a True Endowment

While it is unlikely that the \$137.3 million diverted away from the KEY Fund over the past decade will ever be restored, it is not too late to develop a true endowment. In November 2011, Kansas was positioned to have a FY 2012 ending balance of \$318 million and a FY 2013 ending balance of \$388.9 million.<sup>xi</sup> A portion of this money can be set aside to seed the KEY Fund endowment without jeopardizing the state's fiscal health. This would provide the stability to ensure continued funding for important children's initiatives regardless of the instability of the tobacco settlement payments.

# Conclusion

*In the decade since the creation of the KEY Fund and CIF, the system for funding important children's programs has evolved from an endowment to provide long-term investments into a yearly system addressing immediate needs. The system created by Kansas lawmakers would have invested tobacco Master Settlement Agreement dollars in an endowment thereby stabilizing funding for children's programs and encouraging innovative new children's initiatives. In reality, the KEY Fund became a rainy day fund for the state during challenging economic times. This threatens to undermine the foundation Kansas has worked to build as well as the state's future workforce and long-term prosperity.*

## Sources

- <sup>i</sup> "State-by-State Tobacco Settlement 25-year Totals and Percent of Total," National Conference of State Legislators, [www.ncsl.org](http://www.ncsl.org).
- <sup>ii</sup> "Summary of the Attorneys General Master Tobacco Settlement Agreement," Joy Johnson Wilson, National Conference of State Legislators, March 1999, p. 4.
- <sup>iii</sup> *Ibid.*, p. 27.
- <sup>iv</sup> Roger Myers, *The Topeka Capital-Journal*, January 16, 1999.
- <sup>v</sup> Kansas Legislator Briefing Book 2011(E-1), Kansas Legislative Research Department, p. 2.
- <sup>vi</sup> Data from Kansas Legislator Briefing Book 2011, Kansas Legislative Research Department, p. 2.
- <sup>vii</sup> This calculation used the rate of return on the Kansas Unclaimed Property Fund, a parallel fund with a similar investment purpose managed by KPERS.
- <sup>viii</sup> Kansas Legislative Research Department, Children's Initiatives Fund spreadsheet reflecting Conference Committee Action on HB as of May 11, 2011.
- <sup>ix</sup> Art Rolnick and Rob Grunewald, *Early Childhood Development: Economic Development with a High Public Return*, Federal Reserve Bank of Minneapolis, [http://www.minneapolisfed.org/publications\\_papers/studies/earlychild/abc-part2.pdf](http://www.minneapolisfed.org/publications_papers/studies/earlychild/abc-part2.pdf).
- <sup>x</sup> "A Window to the World: Early Language and Literacy Development," Zero to Three Policy Center, February, 2011.
- <sup>xi</sup> Kansas Legislative Research Department and Kansas Division of the Budget Short Memorandum on State General Fund Revenue Estimates for FY 2012 and FY 2013.



720 SW Jackson, Suite 201  
Topeka, Kansas 66603  
785.232.0550  
[www.kac.org](http://www.kac.org)

*This report was written and published by Kansas Action for Children as part of its Fiscal Focus Initiative. The Fiscal Focus Initiative is funded, in part, by The Annie E. Casey Foundation and the United Methodist Health Ministry Fund. The findings and conclusions presented are those of Kansas Action for Children and do not necessarily reflect the opinions of the funders.*