



State of the States and State Budget Crises

Northeastern States Tax Officers Association

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About The Task Force

- ▣ Co-chairs Richard Ravitch, Paul Volcker
- ▣ Three goals:
 - ⌘ Analyze fiscal condition and structural budget gaps in six states (CA, IL, NJ, NY, TX, VA)
 - ⌘ Analyze fiscal decision-making environment
 - ⌘ Engage state and federal policymakers
- ▣ Initial report in July (www.statebudgetcrisis.org). Outreach and engagement.

Unsustainable Path

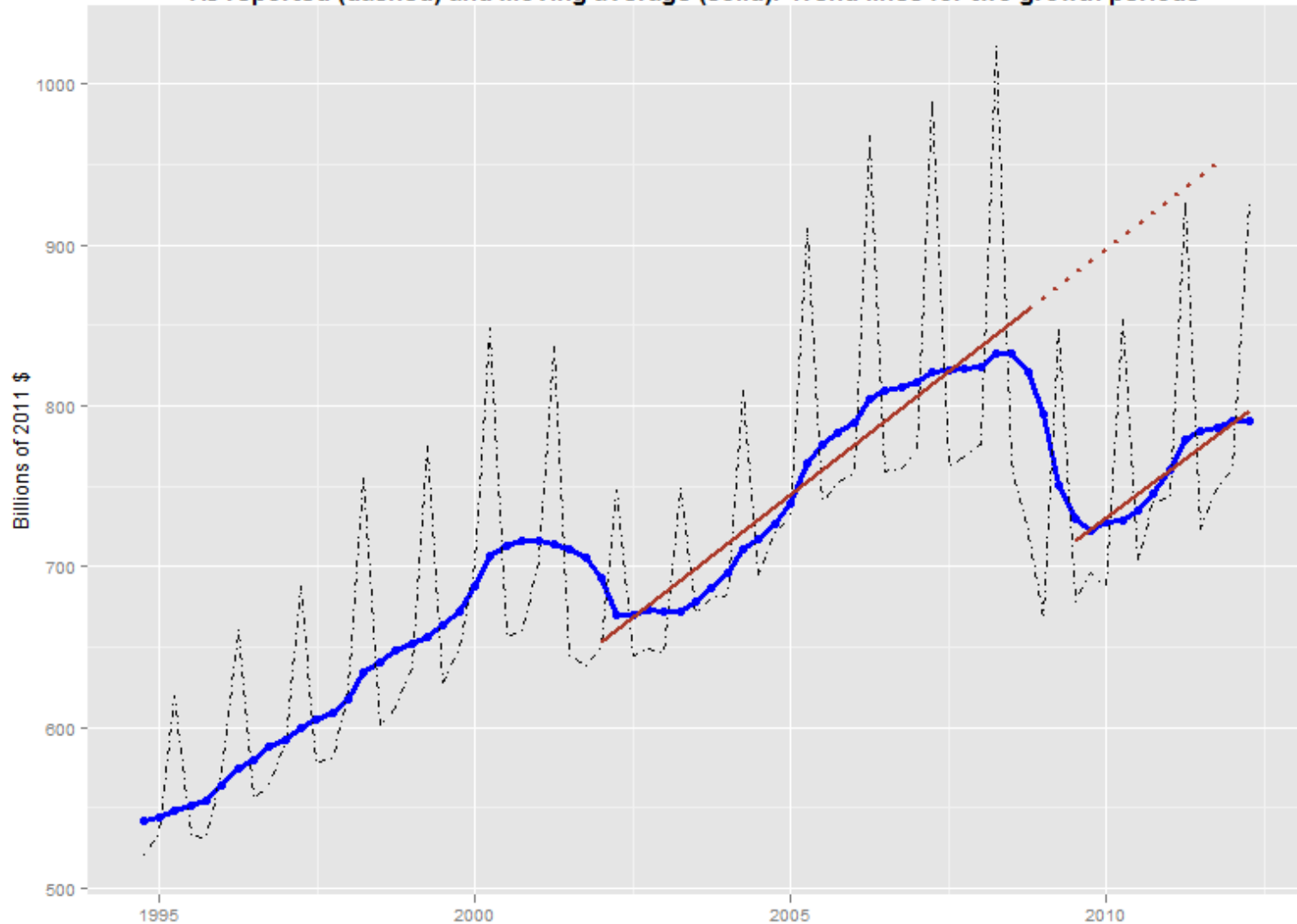
- ▣ Rapid Medicaid growth
- ▣ Federal deficit reduction
- ▣ Underfunded retirement promises
- ▣ Narrow tax bases, volatile revenue
- ▣ Local government fiscal stress
- ▣ Inadequate state budget laws and practices



Prelude: Where we are now

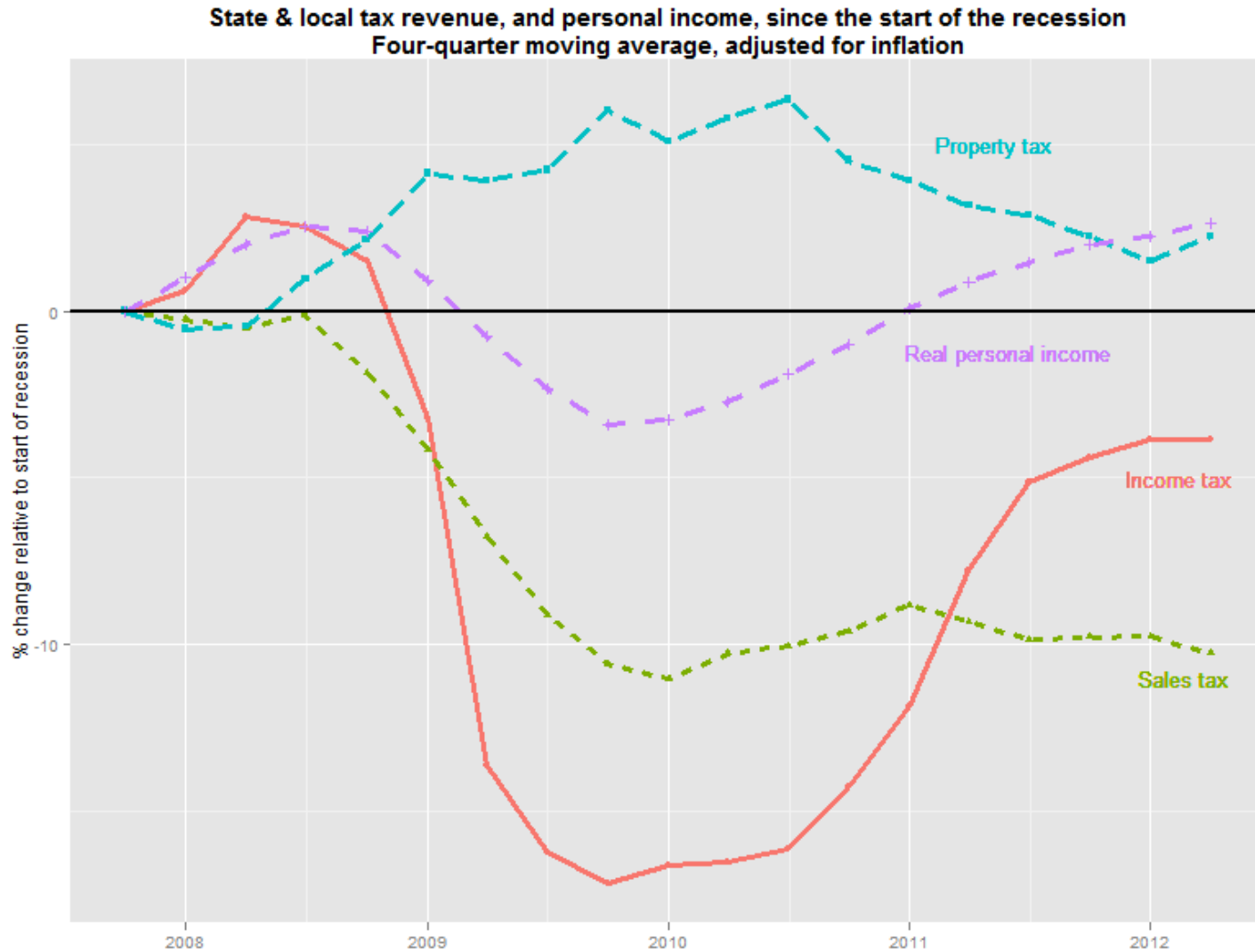
Limping up from the bottom of the cliff

State government real tax revenue at annual rates
As reported (dashed) and moving average (solid). Trend lines for two growth periods



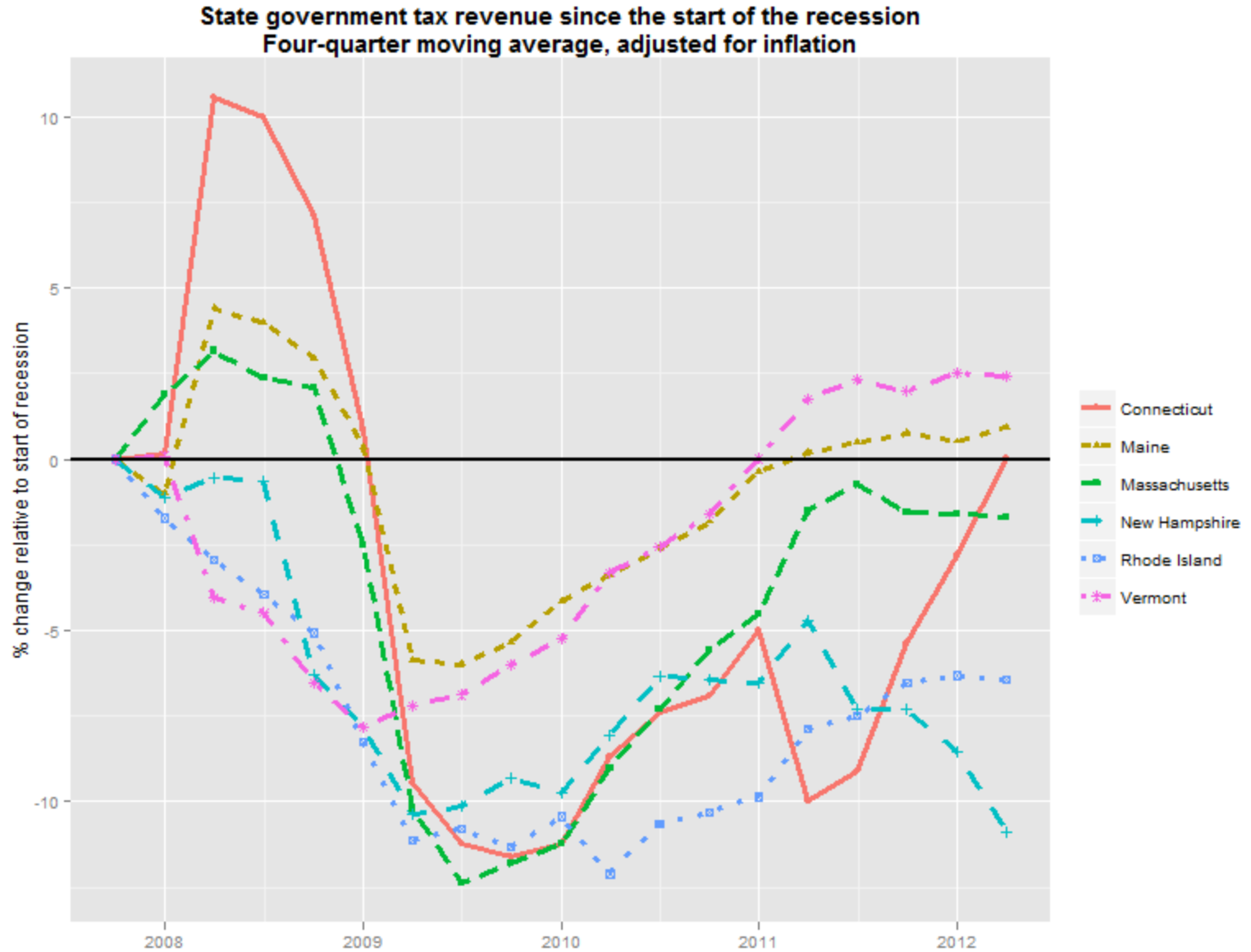
Source: U.S. Bureau of the Census (tax revenue)
and Bureau of Economic Analysis (GDP price index)

Income & sales tax recovery far weaker than (tepid) economic recovery. Property tax weakening



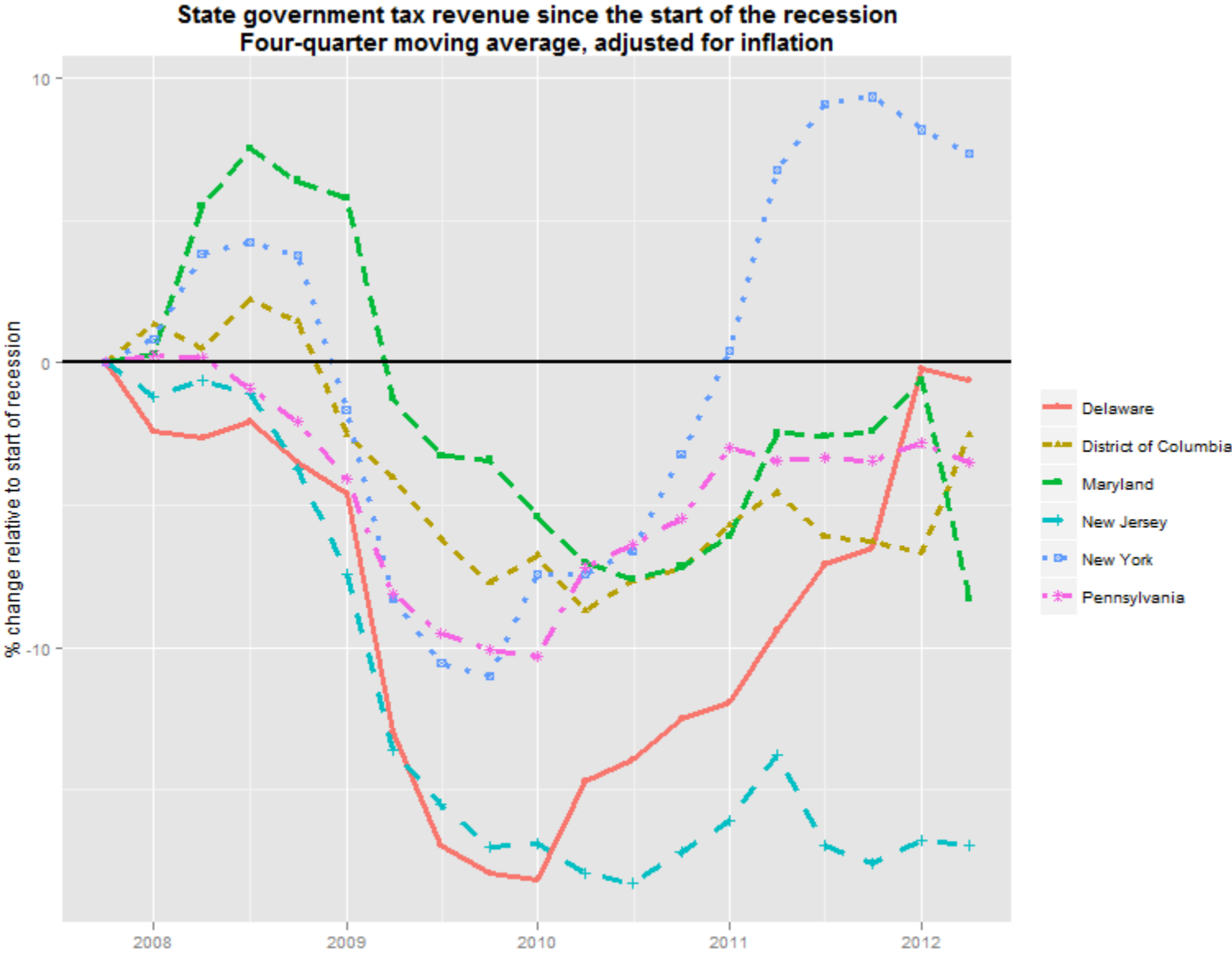
Source: U.S. Bureau of the Census (tax revenue)
and Bureau of Economic Analysis (GDP price index)

NESTOA States: New England half



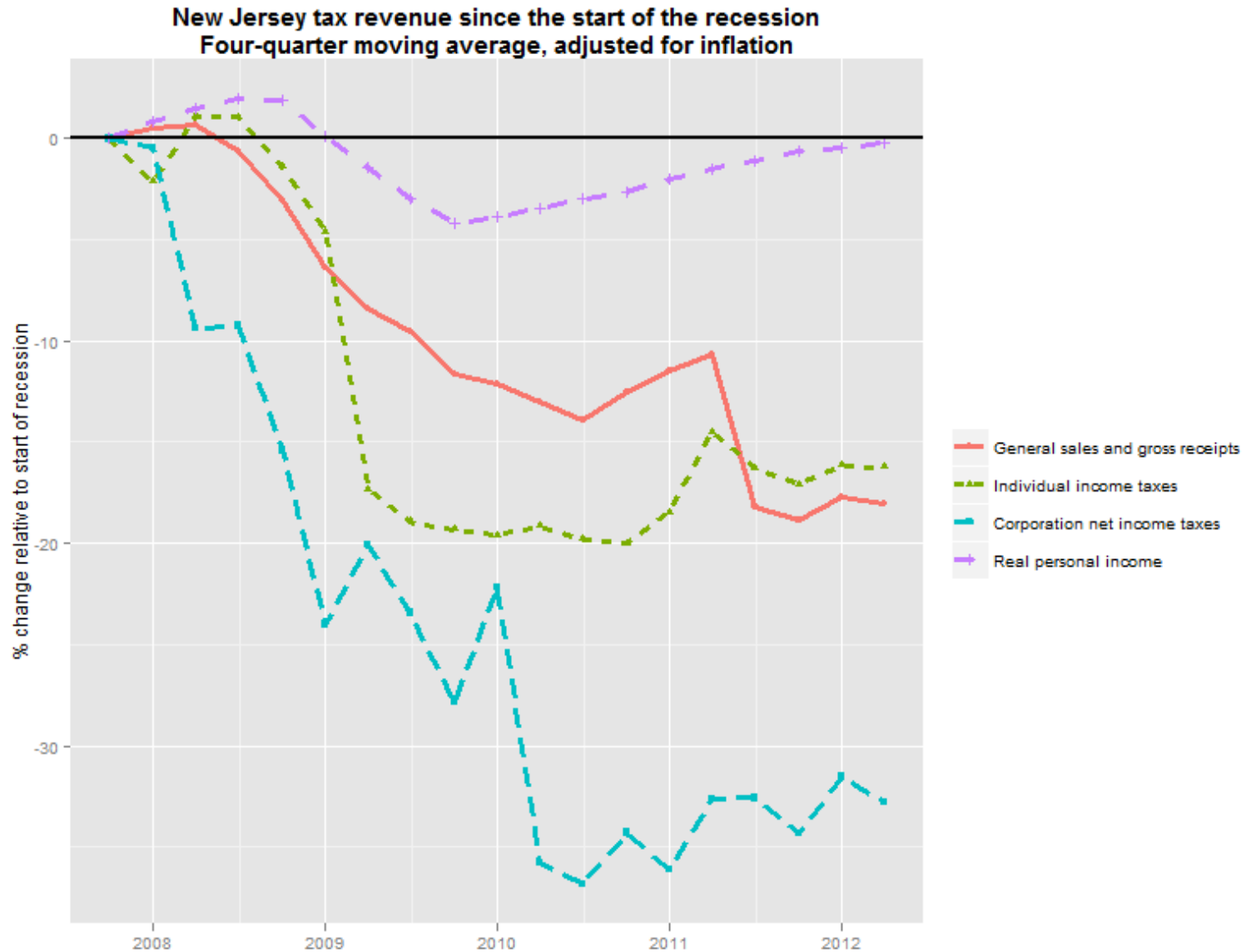
Source: U.S. Bureau of the Census (tax revenue)
and Bureau of Economic Analysis (GDP price index)

NESTOA States: Non-New England half



Source: U.S. Bureau of the Census (tax revenue) and Bureau of Economic Analysis (GDP price index)

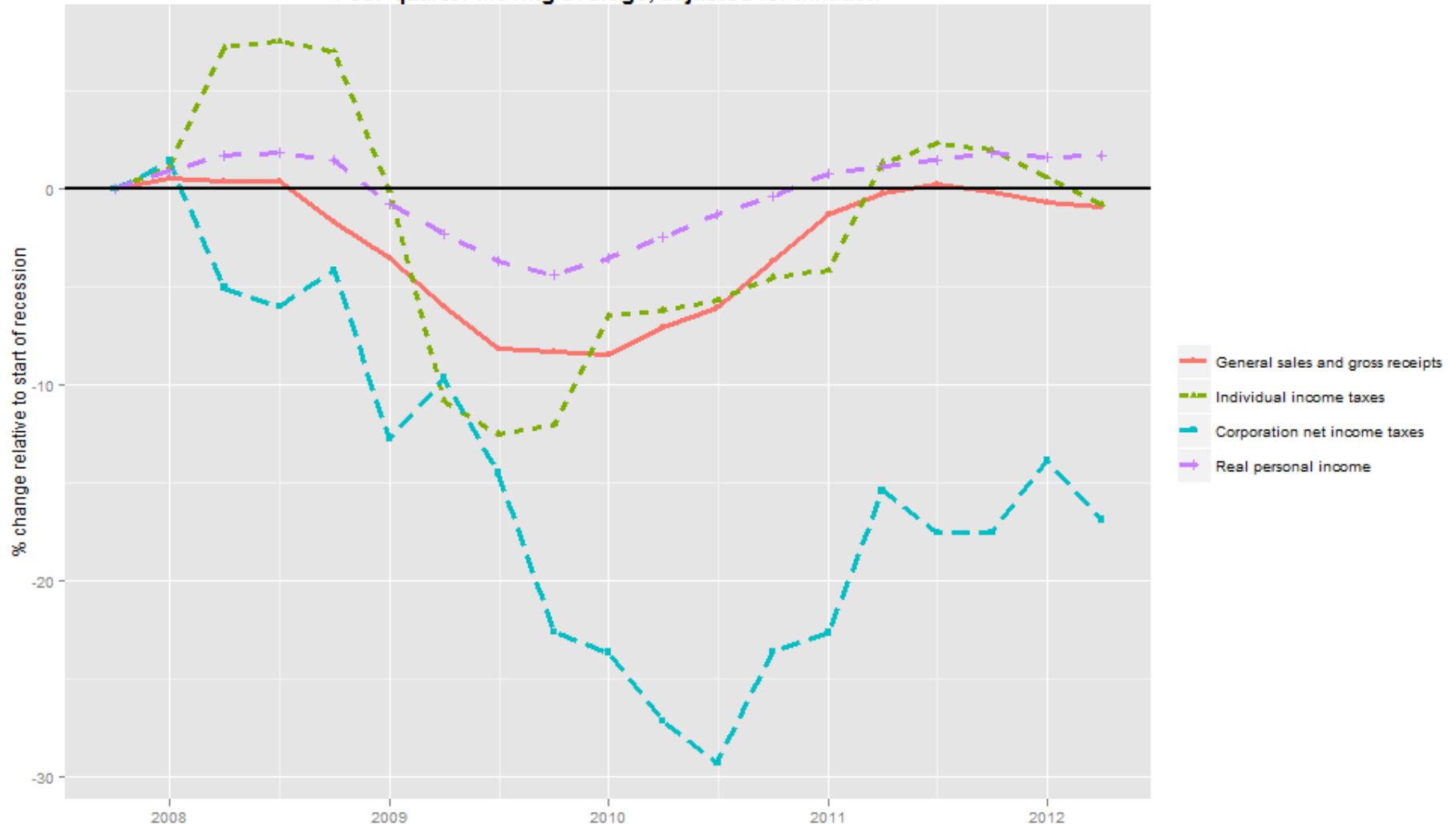
Weakness in New Jersey (a study state)



Source: U.S. Bureau of the Census (tax revenue)
and Bureau of Economic Analysis (GDP price index)

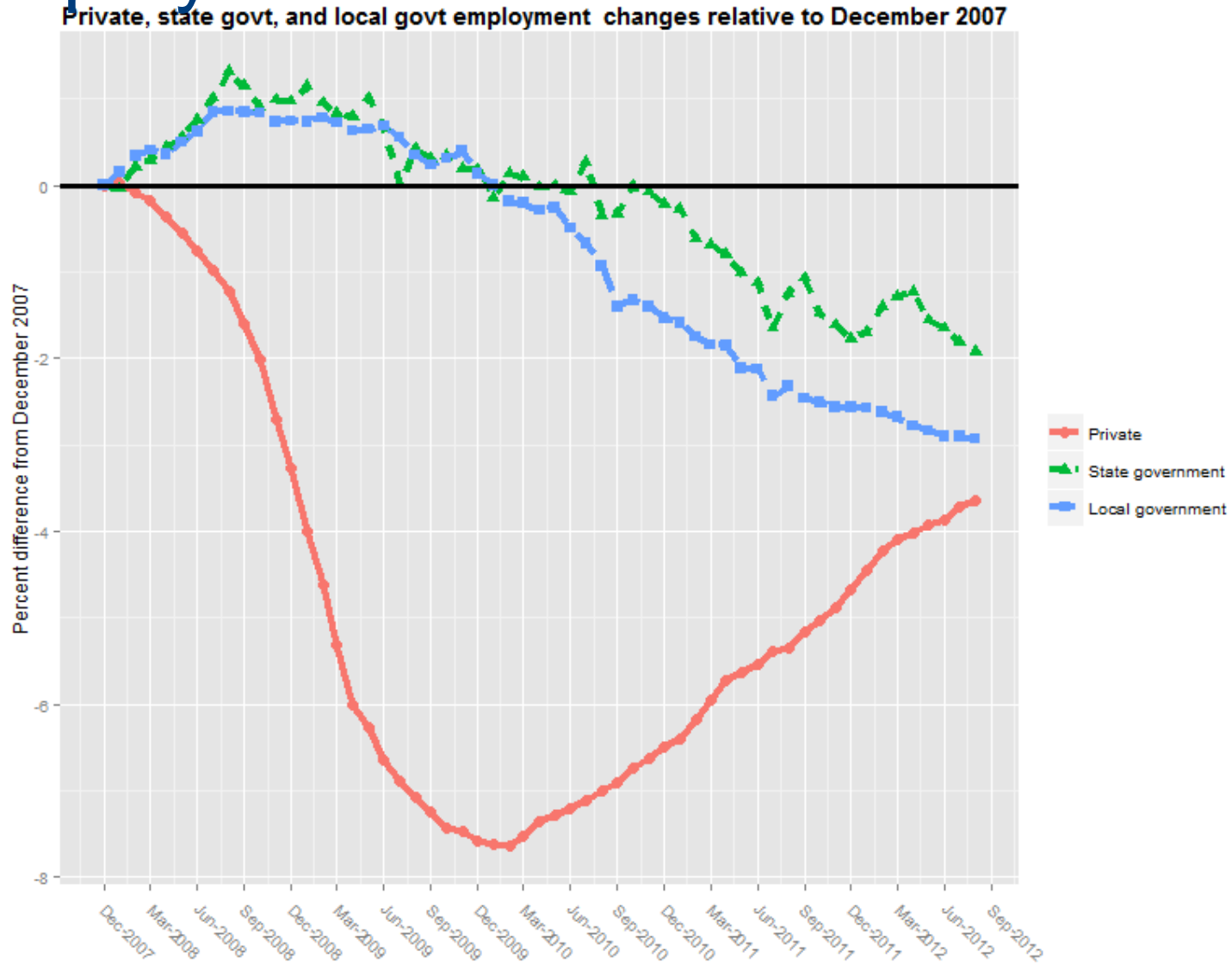
Tax increases & modest economic growth in New York (a study state) spurred revenue, but now flagging

New York tax revenue since the start of the recession
Four-quarter moving average, adjusted for inflation



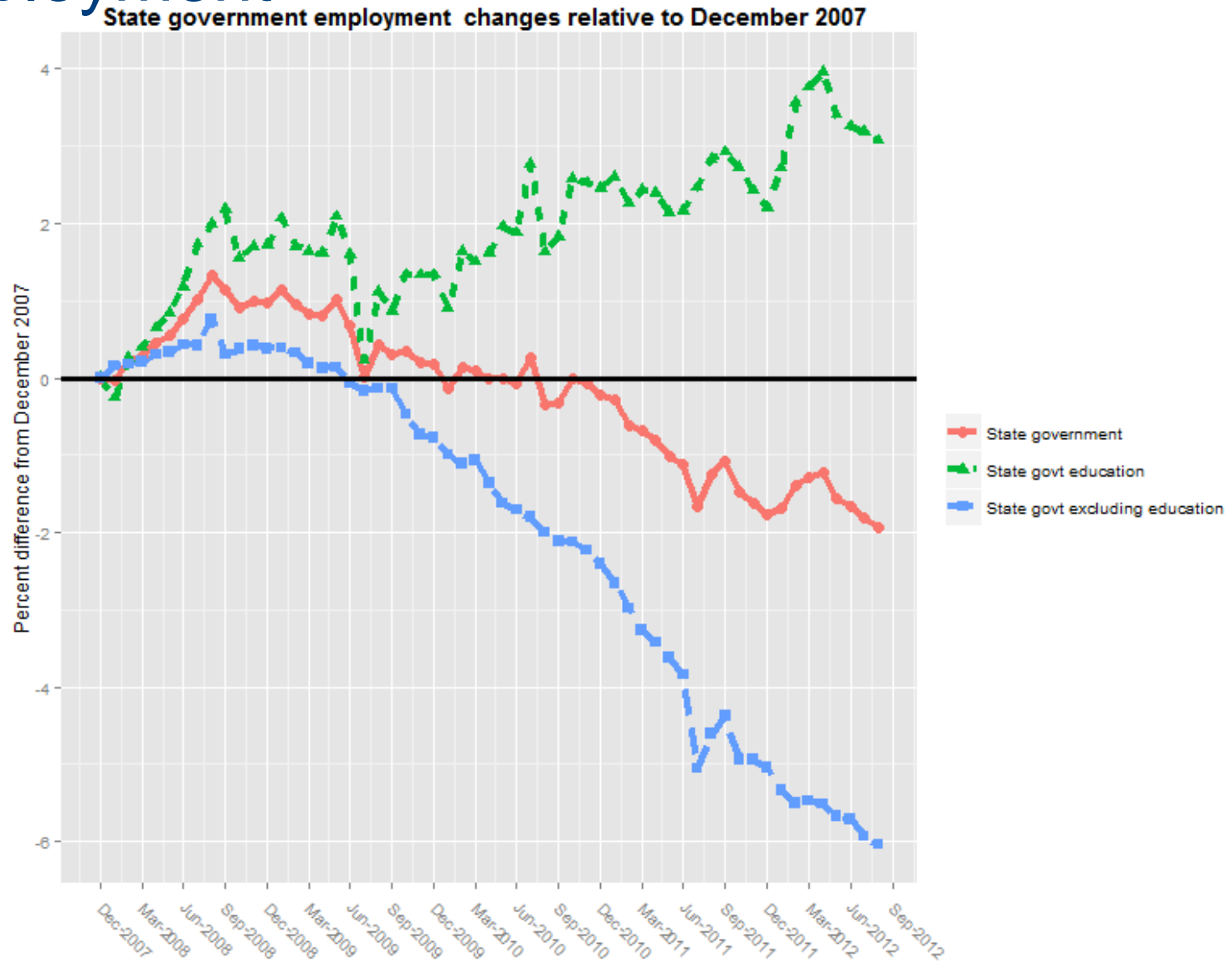
Source: U.S. Bureau of the Census (tax revenue)
and Bureau of Economic Analysis (GDP price index)

Governments are cutting employment



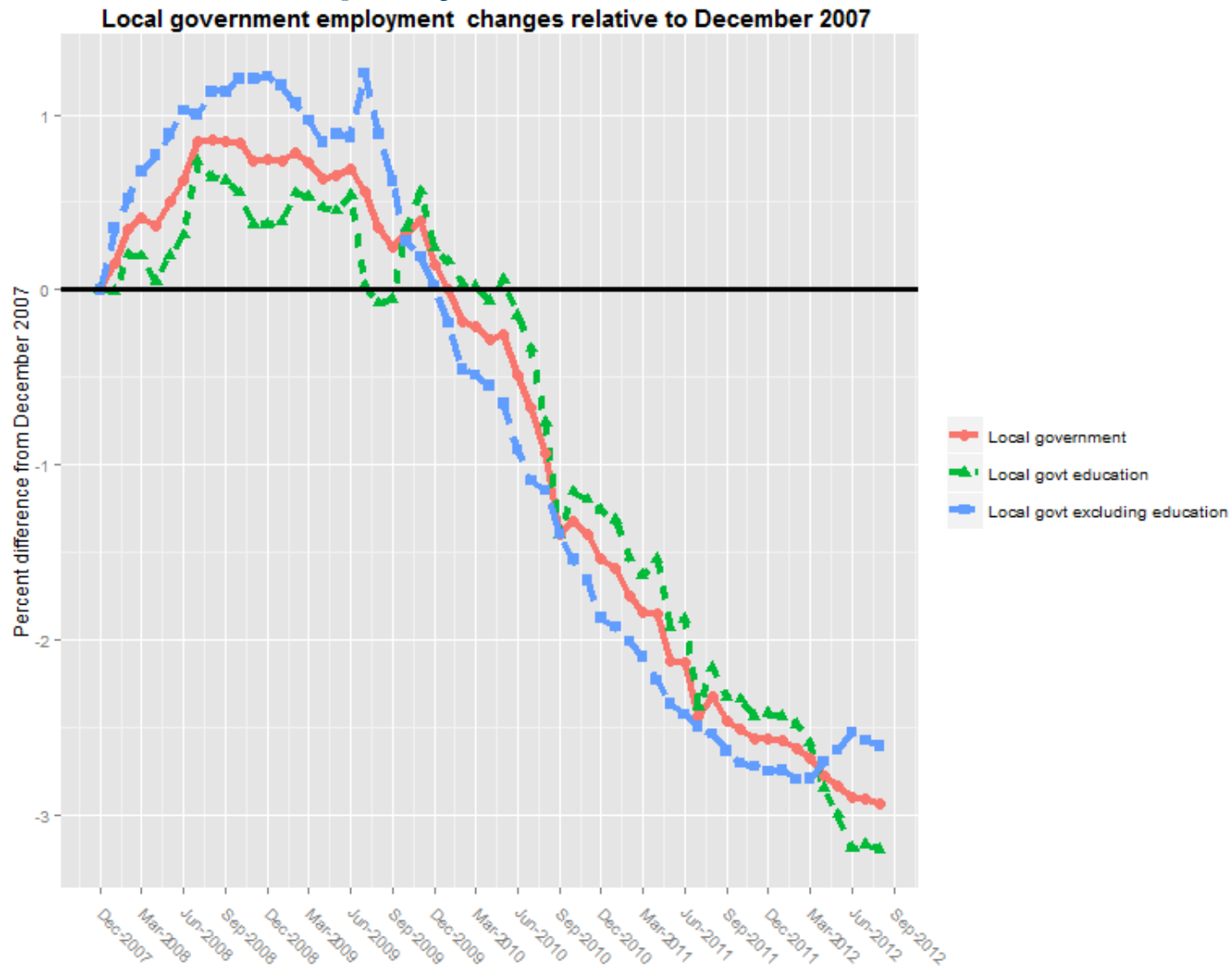
Source: Bureau of Labor Statistics, Current Employment Statistics

States are slashing non-education employment




Source: Bureau of Labor Statistics, Current Employment Statistics

Locals are cutting education and non-education employment



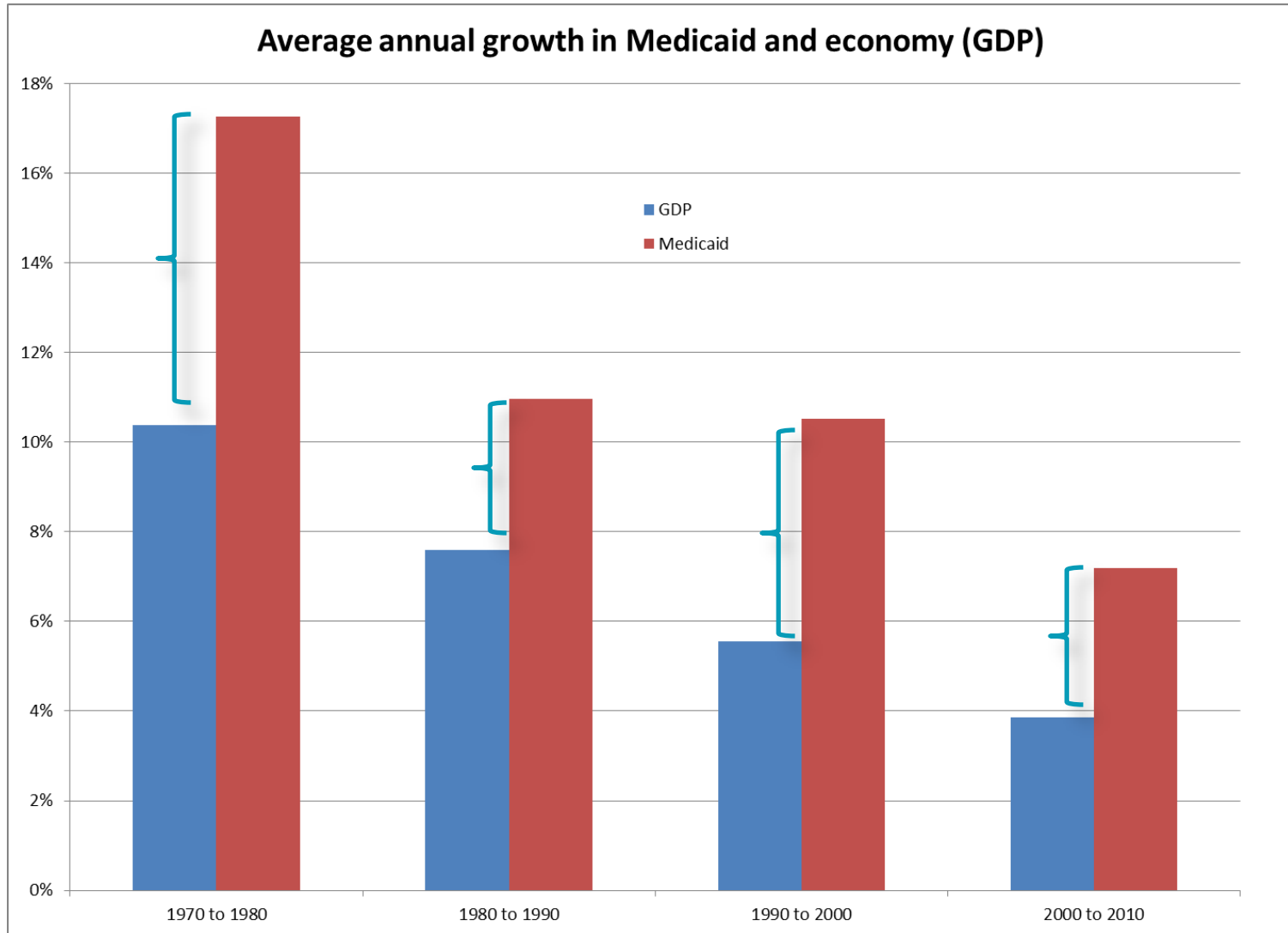
Source: Bureau of Labor Statistics, Current Employment Statistics



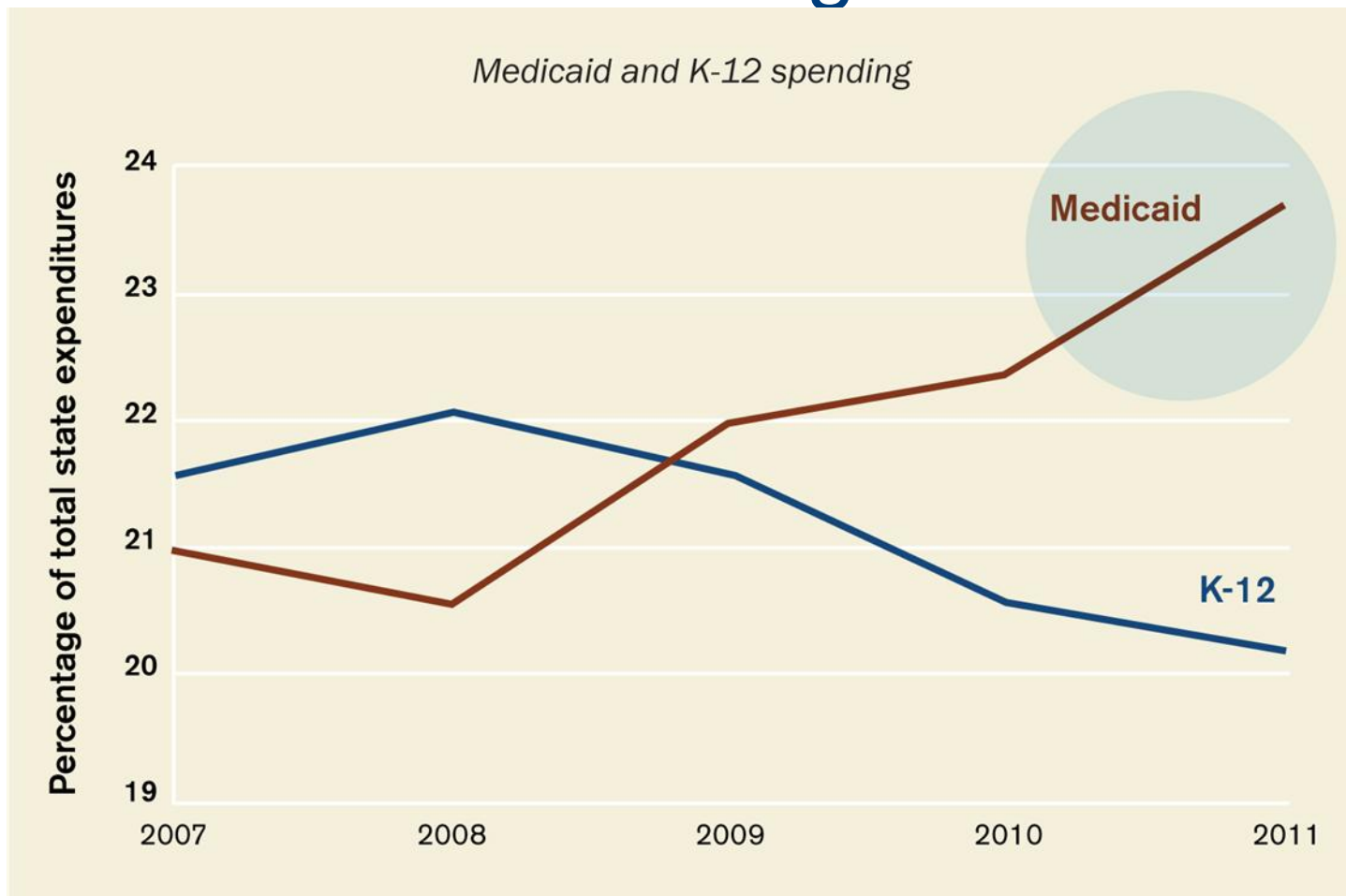
Six Major Threats The Task Force Examined



Decade after decade, Medicaid grows faster than states' capacity to pay for it



Medicaid Has Surpassed K-12 Education in State Budgets



Source: National Association of State Budget Officers (NASBO), State Expenditure Report

Note: Figures are for total state expenditures, including both general fund spending and federal funds

Federal Deficit Reduction Threatens State Finances

- ▣ Federal grants: \$600+ billion, 32% of state revenue
- ▣ Other federal spending – impact on state economies
- ▣ Federal tax changes - municipal bond interest, tax deductibility
- ▣ Impact on states should be a major consideration in federal decision-making

Federal Deficit Reduction Could Hit States Hard

Potential impact of 10-percent cut in federal grants

	Total (\$ millions)	Per capita (\$)
United States	\$62,074	\$201
California	6,657	179
Illinois	2,319	181
New Jersey	1,631	186
New York	6,134	317
Texas	4,373	174
Virginia	1,065	133

Source: Task Force analysis of data from U.S. Bureau of the Census, *Federal Aid to States 2010*.

Underfunded Retirement Promises - state & local -

- ▣ Pensions –\$1-3 trillion underfunded
- ▣ Retiree health benefits –more than \$1 trillion underfunded
- ▣ Reporting and disclosure is opaque. Contributions underpaid.

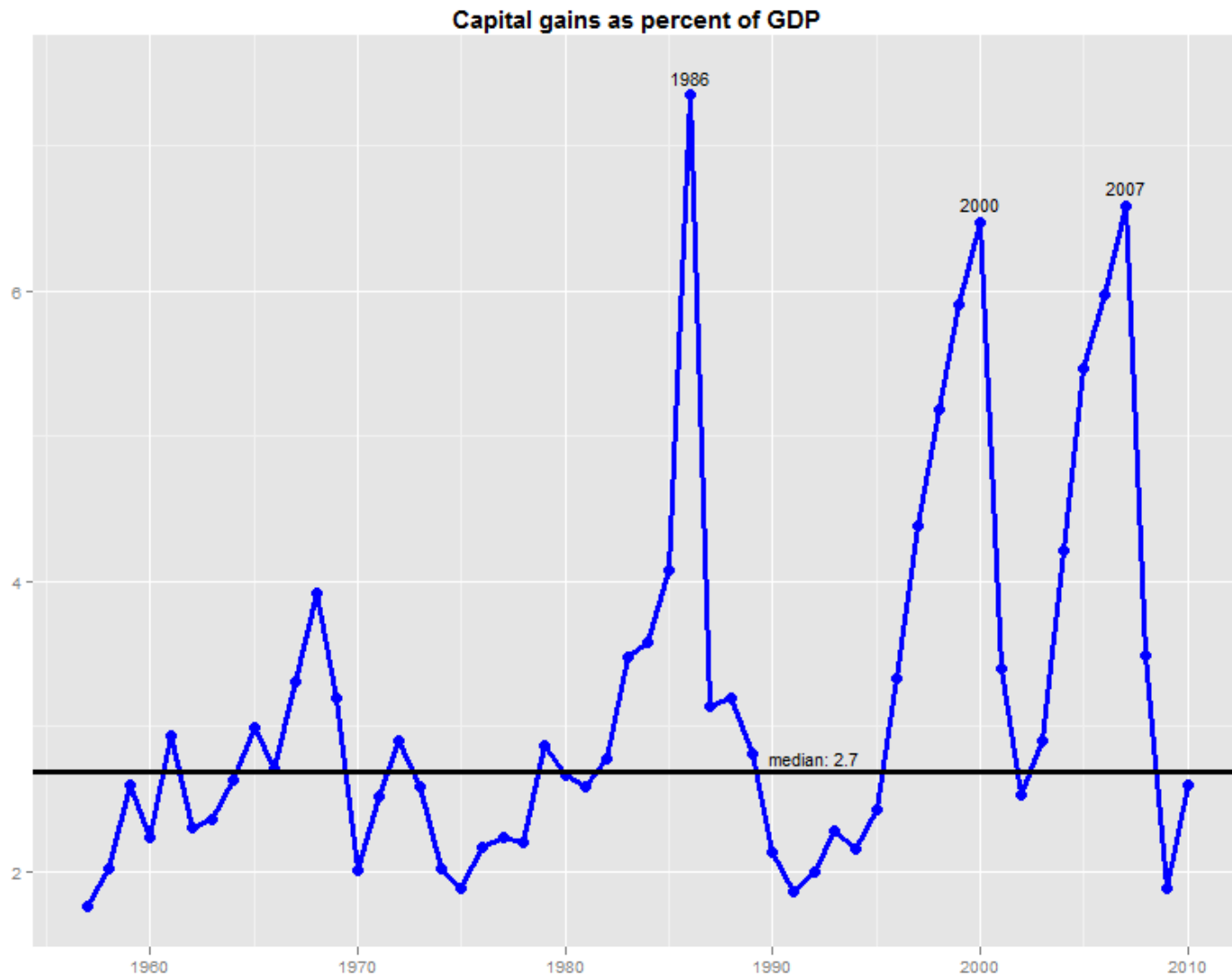
Underfunded Pensions In Study States

State and local government retirement system funded status					
Major state plans and major local plans					
<i>Amounts in \$ billions</i>					
Plan Name (asset value year)	Actuarial Liabilities	Market Value of Assets	Unfunded Liability (Surplus) Using Market Value of Assets	Funded Ratio Using Market Value of Assets (%)	Unfunded Liability Per Capita
United States totals, 126 plans	\$3,442.8	\$2,551.2	\$891.5	74.1	\$2,882.1
Totals for 6 study states	1,542.2	1,156.0	386.2	75.0	3,459.2
California	597.4	461.6	135.8	77.3	3,635.9
Illinois	187.6	95.0	92.5	50.7	7,205.7
New Jersey	120.2	77.6	42.6	64.6	4,838.6
New York	348.0	301.2	46.8	86.6	2,411.8
Texas	214.0	167.7	46.3	78.3	1,835.2
Virginia	75.1	52.9	22.2	70.4	2,770.1

Source: Public Fund Survey (www.publicfundsurvey.org) for actuarial liabilities, accessed June 19, 2012; market value of assets provided by National Association of State Retirement Administrators, June 19, 2012; Unfunded liabilities and funded ratios calculated by Task Force.

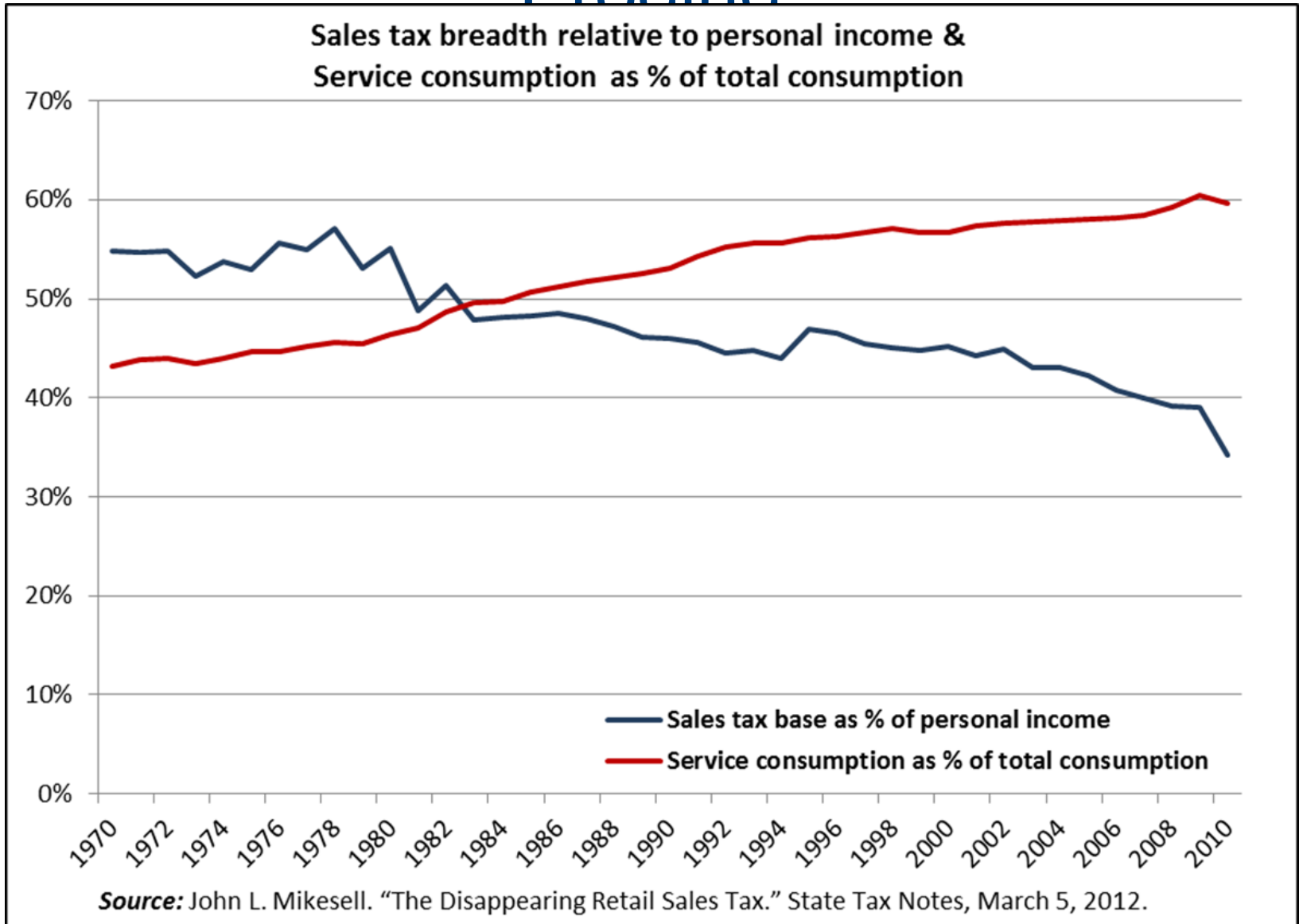
Source: Task Force analysis of data from U.S. Bureau of the Census, *Federal Aid to States 2010*.

Capital gains are a major cause of increased state tax volatility

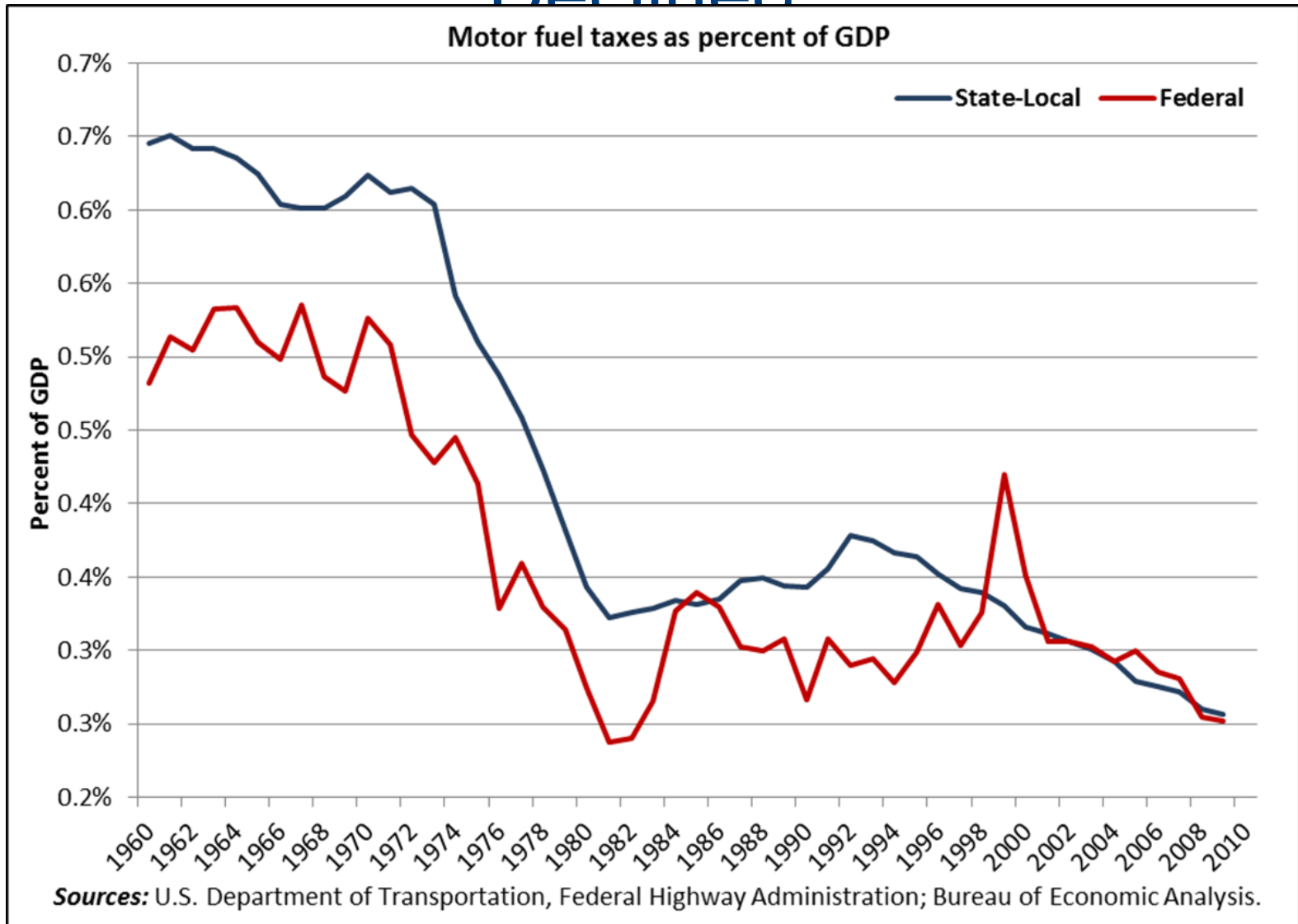


Sources: U.S. Department of the Treasury, Bureau of Economic Analysis

State Sales Tax Bases Have Been Eroding



Highway Funding Sources Have Declined



Local government fiscal stress requires monitoring

- ▣ Property tax (74% of local taxes, on average) under stress, falling in some areas (e.g., California)
- ▣ Rising contributions and payments for pensions and OPEB, in states where local gov'ts pay major share (e.g., CA, IL, NY)
- ▣ Property tax caps limiting ability to address spending pressures

State fiscal procedures mask and encourage gaps - Examples

California	Borrowing for operating purposes over many years created \$28 billion “wall of debt”
Illinois	\$10 billion pension obligation bonds in 2003
New Jersey	Securitized tobacco settlement revenue in 2003 and 2004
New York	Securitized tobacco settlement revenue
Texas	Delayed school aid moved \$2+ billion from one budget period to the next
Virginia	Underpaid pension contributions; accelerated sales tax payments

Needed: Better Ways To Analyze And Manage Fiscal Threats

- ▣ Better fiscal tools: multi-year planning, disclose full costs of services delivered
- ▣ Stronger rainy day funds
- ▣ Broad-based, stable, productive tax bases
- ▣ Federal entity to analyze impact of federal deficit reduction on states

Next steps for the Task Force

- ▣ Individual reports/outreach for study states
- ▣ Meetings in selected states
- ▣ “Dialogues” on major issues. Candidates:
 - ⌘ Federalism and federal deficit reduction
 - ⌘ Pensions
 - ⌘ Medicaid
 - ⌘ Infrastructure
- ▣ Follow-up report early next year