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16 N. Carroll Street • Suite 600 • Madison, WI 53703 • (608) 284-0580 • FAX (608) 284-0583
1442 N. Farwell • Suite 508 • Milwaukee, WI 53202 • (414) 831-8880 • FAX (414) 298-9127
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FEDERAL POLICIES ARE WORSENING WISCONSIN'S STATE AND LOCAL BUDGET PROBLEMS

John Keckhaver, Jon Peacock, and Iris Lav[i]

October 6, 2004

Executive Summary

At a time when state and local governments around the country struggle to overcome continuing budget shortfalls, the federal government is only making their jobs harder. Federal policies have contributed significantly to the fiscal crises in many states, including Wisconsin, by reducing state revenues and imposing additional costs. These policies – primarily unfunded mandates and federal health care and tax policies – have cost Wisconsin $2.4 billion since fiscal year 2002, according to a recent report by the Center on Budget and Policy Priorities (CBPP) in Washington, D.C.[ii]

The additional costs and lost revenue have significantly hampered state and local governments' ability to recover from the recent economic downturn. Elected officials throughout Wisconsin have been forced to deal with these costs and the slow pace of the economic recovery by making budget cuts and raising other revenue sources. The resulting impact on families throughout the state is just beginning to be felt in the form of higher costs and reduced public services. What's worse, the cost to Wisconsin from these federal policies is rising, with little relief in sight.

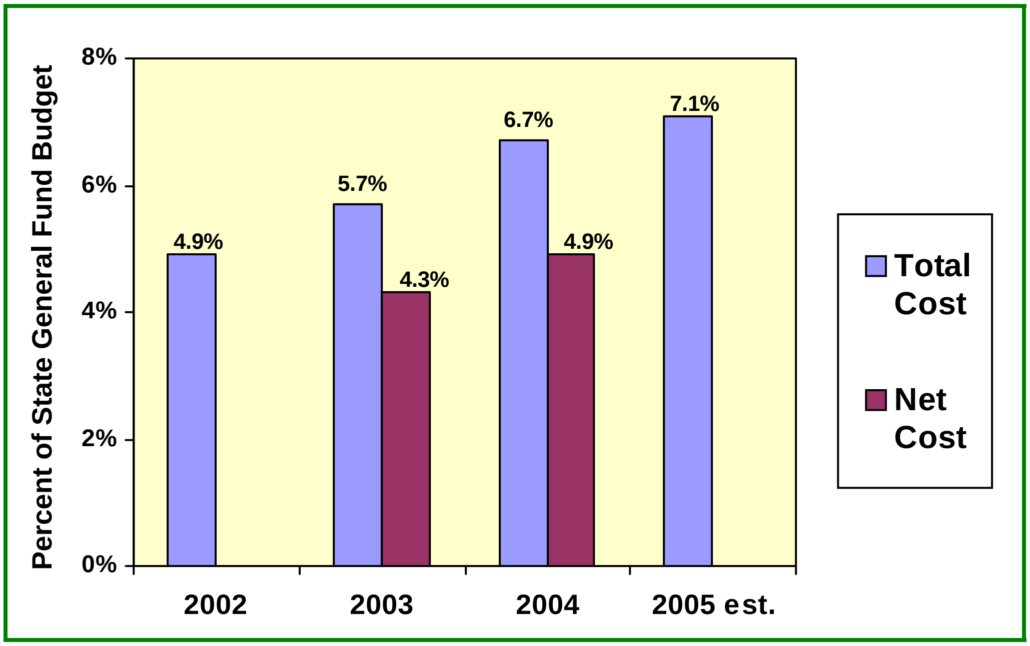
The federal policies noted by the Center on Budget and Policy Priorities that have significantly impacted Wisconsin since fiscal year 2002 and the corresponding cost or benefit are:

- **Unfunded Mandates –** Unfunded federal mandates have cost Wisconsin $1.2 billion between fiscal years 2002 and 2005, most significantly in the areas of education and election reform.
- **Medicare/Medicaid Dual Eligibles –** The increased use of prescription drugs shifts costs of health care for low-income elderly from the federal Medicare program to state Medicaid programs, and has cost Wisconsin $564 million during this time.
- **Remote Sales –** States cannot collect sales taxes on goods and services purchased over the Internet from a firm outside the state due to federal restrictions, costing Wisconsin $975 million from 2002 to 2005.

- **Federal Fiscal Relief** – Congress approved temporary grants in 2003 totaling $20 billion. Wisconsin's share of this aid was $352 million.

Figure 1 shows the costs of federal policy relative to Wisconsin's total general fund budget. The net cost figures for fiscal years 2003 and 2004 include the short-term fiscal relief that was provided to the states in those two years.

Figure 1. Net Costs of Federal Policy to Wisconsin
(as % of General Fund Budget)



Source: Center on Budget and Policy Priorities

To be sure, Wisconsin has not been the hardest hit state. The net cost of $2.4 billion from 2002-2005 amounts to 5.3 percent of Wisconsin's general fund budgets during that time (40th nationally). By comparison, the costs to Florida – the hardest hit – total $11.2 billion and amount to 13.3 percent of its general fund budget for the same time period. Wisconsin, because it is not heavily dependent on federal funding, not one of the poorest states, and because it decoupled from federal tax changes to the estate tax and bonus depreciation provisions, avoided even higher costs.

Nevertheless, federal policies have had a significant effect on Wisconsin state and local budgets. Unlike the federal government, state and local governments cannot run deficits even in difficult financial times. Wisconsin has had to make numerous cuts that are adversely affecting access to government services, the quality of those services, and the costs borne by state residents. For example:

- Students at the two largest University campuses must now pay $1,400 per year more than they did in 2002-03, and resident tuition at the other campuses has increased by $1,000 per year.

- Total state fee changes enacted from fiscal years 2002 through 2005 are costing Wisconsin residents an additional $252 million this year and $533 million over the four-year period. In addition to higher tuition, other examples include increases in vehicle registration fees and in the SeniorCare program, which subsidizes the cost of drugs for the elderly.
- Premiums in the BadgerCare program, which provides health insurance to low-income families were boosted by 60 percent – from 3 percent of income to 5 percent – causing an increase in the range of $480 to $720 per year for a family of four.
- Policy changes to BadgerCare (including the premium increases) reduced enrollment by more than 17,000 people (15 percent) in the first 9 months of 2004 — likely boosting the number of children in the state that lack health insurance.
- The state repealed its commitment to pay two-thirds of school costs and has reduced state aid to schools by about $375 million in 2004-05, relative to the amount required under prior law.
- State aid to counties and municipal governments under Shared Revenue and related programs, which had been effectively frozen since 1995, was cut by $40 million in 2004.

Local governments have also had to cut programs deeply and raise revenues. The reductions in Shared Revenue payments and other state aid are particularly ill-timed because local governments' budgets are being hit with significantly increasing costs in several areas. Health insurance coverage for employees, fuel, pension fund contribution increases, and other costs have risen dramatically in recent years. In response, local governments have had to trim back basic services, lay off employees, increase property taxes, increase existing fees and implement new ones.

We examined the local budget choices made in four areas of the state: Eau Claire, Kenosha, La Crosse, and Milwaukee. The following are just a few of the local impacts:

- School districts, caught between declining state revenue and unfunded federal mandates, have been raising fees, reducing instructional staff, and cutting summer and extracurricular programming. As a result, class sizes are increasing in many schools, access to extracurricular activities is diminished, and the quality of education for Wisconsin's children is likely to suffer.
- Reduced aid for counties and municipalities is diminishing access to services and the quality of local services. For example, there are long and growing waiting lists for services needed by people with disabilities; many municipalities have cut back on snow plowing, law enforcement and fire protection; and counties have fewer staff to handle child abuse and neglect cases.
- In Milwaukee County, a recent report found that an under-funded mental health system has resulted in people with acute mental illness being warehoused in jail cells or left unattended in hospital emergency rooms.
- Even as local governments are cutting staff and services, they have had to increase property taxes, in some instances quite substantially. For example, Milwaukee

Public Schools is increasing its property tax levy by 15.4 percent in 2004-05, notwithstanding the elimination of more than 600 teachers and 400 other positions over a two-year period.

- In response to the rising costs and the fiscal squeeze caused by federal policies and state aid cuts, total residential property taxes payable in 2004 are $838 million higher across Wisconsin than in 2001[iii], an average increase of $322 per household, or 16.5 percent. In inflation-adjusted terms, the increase over the last three years has been $185 per household, or 8.8 percent.

At a time when the federal government could have been ameliorating states' fiscal problems, it instead has been cutting federal income taxes, with most of the tax cuts targeted to high-income households. For a small number of very-high-income Wisconsin residents, the benefits of the federal tax cuts have probably outweighed the direct costs of state and local budget difficulties. For a large number of lower- and middle-income Wisconsinites, however, the benefit of the tax cuts is likely to be outweighed by the harm done by state and local budget cuts. For instance:

- In 2004, the average federal tax cut for a Wisconsin taxpayer in the middle fifth of the income spectrum is $971.[iv] That is nearly one-third less than the increase in annual tuition costs over the last two years for students at UW-Madison and UW-Milwaukee, and slightly less than the tuition increases at the other UW campuses.
- In 2004, the average federal tax cut for Wisconsin taxpayers in the poorest 60 percent of households is $529. That is less than the premium increase for many of the families participating in BadgerCare.

The end result of the federal policies affecting state budgets is becoming clearer as families throughout Wisconsin are now paying more for everything from car registration to college tuition, from health insurance premiums to school fees. These costs, along with the reduction in services offered, while individually manageable for most, add up to a higher cost of living and a decreased quality of life in Wisconsin.

Unfunded mandates from the federal government to state and local governments are nothing new. Indeed, this "devolution without support" has been going on for several years. What is different about the recent past is the level of the costs associated with these policies combined with their timing. In other words, just when state and local governments find themselves in significant fiscal distress – from the recent recession, the stock market declines, and rising costs associated with health care and other areas of public expenditure – the federal government is making it more difficult for them to work their way out.

Even greater impacts lie ahead. Wisconsin's budget writers have employed many short-term solutions and accounting gimmicks that have delayed the necessity of making hard choices between cutting services or raising taxes. As a result of that approach, the state must still grapple with a substantial Medicaid deficit (estimated at $224 million) in the current biennium, and with a projected "structural imbalance" of nearly $1.6 billion in the 2005-07 biennial budget. Since the state has already employed so many one-time remedies and has made several rounds of cuts, even harder choices await in the next budget – exacerbated by the continuing cost of the federal policies enumerated in this report.

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Introduction

Federal policies are inexorably linked to state and local budgeting. Decisions made inside the Capital Beltway are bound to affect – either directly or indirectly – state and local revenue and spending measures. For example, if a state's tax code is tied to federal law, a federal tax cut may result in decreased state tax revenue. This will force the state to cut expenditures or raise revenue, or some combination of the two in order to balance its budget. The expenditures cut, if that's the route taken, may come in the form of decreased access to health care for the poor, or in less funding for district attorneys, or in the form of less aid to local governments. Local governments, operating with less revenue from the state, are forced to cut the services they offer, or to raise property taxes or fee levels – all unpopular options.

Because the federal government often seems quite distant from daily life in local communities (and from the decisions made by local representatives regarding street repair, trash pickup, school fees, property taxes and the like), the role played by federal policy in state and local budgets is often ignored. But the impact, sometimes easily quantifiable and sometimes not, is undeniable.

The connection between recent federal policies and state and local budgets in Wisconsin and the resulting impacts on Wisconsin residents are examined in this report. We begin by looking at specific federal policies that have impacted Wisconsin since fiscal year 2002 – roughly the start of the state fiscal crisis – and document the level of that impact. We then turn to what the state and local governments have faced in recent years, and how they have responded. We look at four counties in particular, Eau Claire, Kenosha, La Crosse, and Milwaukee for examples of local budget pressures and responses. These have been chosen because they include both rural and urban communities, significant population bases, varied political leadership, and were especially forthcoming regarding recent budget actions. Finally, we look ahead and consider the various budget and policy pressures the state of Wisconsin and its local governments are likely to face in coming years.

The Costs and Benefits of Recent Federal Policy in Wisconsin

The following five areas of federal policy have significantly affected state and local budgets across the country since 2002: (1) federal tax policy, (2) federal preemption of state and local taxing authority, (3) the failure of Congress to address Supreme Court rulings that prevent states and localities from collecting taxes owed to them, (4) mandates that require states to spend funds for particular purposes, and (5) federal Medicare and Medicaid policies that have become expensive for states. States around the country have been affected in different ways by these federal policies. Table 1 shows the impact of these federal policies on Wisconsin from 2002 through 2005. A brief description of each then follows.

Table 1: Costs to WI of Federal Policy, 2002-2005 (in Millions of Dollars)

Federal Policy	Cost or Benefit
Internet Sales	- $975
Special Education	- $784
"No Child Left Behind"	- $404
Election Reform	- $12
Prescription Drugs	- $564
Total Costs	***- $2,738***
Fiscal Relief	+ 352
Net Costs	***- $2,385***

Source: Center on Budget and Policy Priorities

Tax Policy

Remote Sales – Congress has the authority, as described by recent Supreme Court case law, to allow state and local governments to enforce sales tax collection on most items purchased through catalogues or over the Internet from firms that otherwise do not have the required "nexus" – that is, a sufficient business connection – within the state. These are items that are taxed when bought in retail stores. Despite the efforts of some in Congress, enabling legislation has yet to be passed to allow such tax enforcement. Because of this inaction, state and local governments have lost at least $61 billion during this four-year period – with Wisconsin's share estimated to be $975 million.[v]

Estate Tax and Depreciation Provisions – A series of federal tax cuts were enacted in 2001 through 2003. Included in these were changes to the federal estate tax and depreciation provisions. (The latter is an issue when computing business income taxes.) States that have tax codes tied to the federal tax laws have been affected significantly by these changes. Some states chose to "decouple" from the federal tax code with regard to some or all of these measures and have thereby saved themselves millions of dollars in what would have been lost revenue. Those that did not decouple lost $9 billion from 2002 through 2005.

Wisconsin was one of 14 states (and the District of Columbia) that decoupled from both the estate tax change and the "bonus depreciation" provisions. However, the law decoupling Wisconsin with respect to the estate tax changes is scheduled to expire at the end of 2007, and Wisconsin will start losing about $86 million per year in 2008 if that law is not amended.[vi]

Internet Access Fees – The Internet Tax Freedom Act, passed in 1998 and extended in November of 2001, is a federal law barring states from taxing Internet access fees. This preemption does not apply to Wisconsin, which was one of nine states "grandfathered" out of its provisions, but has cost other states over $4 billion since 2002. Legislation pending in

Congress could remove Wisconsin's "grandfathered" status and cause a future state revenue loss.

Unfunded Mandates

A collection of federal mandates placed on state and local governments and school districts are having significant impacts in most states, including Wisconsin. The most critical of these have come in the areas of education and electoral reform.[vii]

Education Mandates

In 1997, Congress amended the Individuals with Disabilities Education Act (IDEA). The law requires that each disabled child receive an assessment and an individual education plan.[viii] The federal contribution toward meeting this mandate was to be 40 percent of costs. Over the last four years the federal government has fallen about $40 billion short of this mark.

A more recent education measure, and one that includes far-reaching mandates for both state and local governments is the Elementary and Secondary Education Act – often called the No Child Left Behind law. Under the Act, schools are required to meet new teacher qualification standards and implement comprehensive testing and reporting systems by specified dates.[ix] Federal funding meant to help pay for such changes has been, under a conservative estimate, $32 billion below the level authorized in the law. The total funding gap for Wisconsin from these two mandates alone totals $1.188 billion from 2002 to 2005.

Election Reform

Another area of recent federal action is election reform. Following the electoral debacle of 2000, Congress passed the Help America Vote Act (HAVA), a measure that provides federal guidelines and, ostensibly, resources that would allow local governments to update voting equipment.[x] The funding shortfall over the past four years has been over $1 billion nationwide and $12 million in Wisconsin.

Medicaid/Medicare Dual Eligibles

Many low-income elderly and disabled individuals are eligible both for Medicare, a federal program, and for Medicaid, a program for which states share the responsibility. Medicare is the primary payer for most services covered by both programs. The federal government has failed until just recently to include a prescription drug benefit under Medicare, so states, which pay an average of 43 percent of the costs of Medicaid, have born the brunt of significant prescription drug costs. This fact is made more significant given the increased importance of drug therapy in medical practice in recent years, as compared to prolonged hospital stays. The result of this federal inaction has cost Wisconsin $564 million over the last four years (and all states a total of $28 billion).

The recently enacted Medicare drug bill, set to take effect in 2006, will cover under Medicare some of the drugs for all Medicare beneficiaries. In the end, states will still be responsible for the bulk of drug costs, however, as they will be required to reimburse the federal government – through what is called a “clawback” provision – for most of the cost of prescription drug coverage for individuals who are eligible for Medicaid as well as Medicare. The amount the states will have to reimburse will be 90 percent of their savings in the first year, 2006, and will gradually be reduced to 75 percent by 2015.[xi]

Aid to the States

In spring 2003, the federal government committed $10 billion in direct grants to the states and another $10 billion in additional Medicaid funds, to be distributed over roughly a 15-month period. This aid, of which Wisconsin’s share was $352 million, alleviated some of the budget strain felt by state governments. At the time, however, many were calling for significantly larger grants from the federal government – the only unit of government that can carry a deficit. Despite the grants, states have had to primarily balance their budgets with revenue increases and service cuts, both of which take money out of their economies at the time it’s most needed – when trying to recover from a recession.

The State Fiscal Crisis

The prolonged state fiscal crisis was caused by several factors including the recession of 2001, decreased revenues stemming from significant tax cuts enacted throughout the late 1990s, the stock market decline, slow job growth during the early stages of the recovery, and the costs associated with the federal policies described above. Between fiscal years 2002 and 2004, the states faced a total budget deficit of $190 billion with additional deficits in fiscal year 2005 of $40 billion.[xii]

While there are two sides to every budget equation – revenues and expenditures – state spending is often blamed as the sole or primary cause of these recent and ongoing state deficits. As has been pointed out by the Center on Budget and Policy Priorities, state spending growth during the 1990s was actually low by historical standards when adjusting for inflation and population growth. In fact, it was lower than or equal to the spending growth in every other decade since World War II.[xiii] Spending, then, is only part of the picture. In order to solve continuing budget problems, states must understand the significant role recent tax cuts and federal policies have played.

Around the country, the state spending increases that did occur primarily came in the areas of health care, education, and corrections. The same is true in Wisconsin, and it is not difficult to see why. Health care costs have risen dramatically, the state took on a commitment to pay two thirds of the cost of K-12 education in 1995, and the state’s inmate population ballooned as a result of significant “tough on crime” reforms to the state’s criminal code. Wisconsin’s budget has been severely pinched by the combination of those spending increases, a series of tax cuts enacted when revenue collections were strong in the late 1990s, the effects of the subsequent recession, and the fiscal impact of federal policies.

Closing Budget Shortfalls in Wisconsin, 2002-2005

One-Time Sources of Revenue

By January of 2002, it was clear that Wisconsin lawmakers would have to pass a budget adjustment bill to close the widening budget gap – at the time $1.1 billion – by the end of the 2001-03 biennium. They did so and balanced the budget with across-the-board state agency cuts, delayed correctional facility openings, debt restructuring, the elimination of several minor program items, and, primarily, through the use of a significant one-time revenue source – the securitization of the state's tobacco settlement payments.

Wisconsin, as part of the lawsuit against the tobacco companies, was scheduled to receive about $5.9 billion over the next 25 years. Instead, state leaders chose to sell the rights to that revenue stream – "securitization" – for a one-time payment of about $1.6 billion, over half of which was immediately used to help close the 2001-03 budget shortfall.

Because revenue collections continued to disappoint and because the 2002 budget adjustment bill included several one-time sources of revenue along with delayed payments, the budget deficit heading into the 2003-05 biennium was even more significant at $3.2 billion. Wisconsin had the dubious distinction at the time of facing one of the highest deficits in the nation as a percent of its total general fund budget.

Within a self-imposed "no-tax-increase" framework, state leaders had very few options for dealing with the state's continuing fiscal crisis. Again, use of one-time sources of revenue would play a major role in balancing the 2003-05 budget. This allowed lawmakers to avoid deeper program cuts and tax increases, and in effect pushed off the remaining structural imbalance (between revenue collections and expenditures) to be dealt with at a later date. About $1 billion in one-timers were used to close the budget gap (see Appendix 1), and others were adopted later in the session to close a severe shortfall in the Medicaid budget.

Spending Cuts and Increased Fees

Even with the many short-term fixes, significant program cuts were necessary to balance the budget since lawmakers were adamant about avoiding tax increases. In the end, program cuts totaled $480 million. State jobs were also targeted, with 2,300 positions to be shed over the biennium. The biggest cut was a $250 million reduction in state support for the University System, approximately $150 million of that to be offset by higher tuition rates. The net cut of $100 million represents the largest single cut in the history of the UW System. Other agencies also suffered cuts, with about $325 million coming from agency budgets overall.

Most of the cuts outside the UW System have been in agency "operating budgets" – the funding for staff, supplies and other administrative expenses. Those budgets have been reduced steadily and substantially over the last four years, and the 2003-05 budget took the unusual step of prospectively requiring an additional $100 million per year to be cut from agency operating budgets in the 2005-07 biennium. The impact of the cuts in operating budgets is extremely difficult to quantify, but over time they are likely to cause erosion in the infrastructure needed to manage state programs effectively and provide critical services to the people of Wisconsin. Cuts in Department of Revenue staffing levels could also reduce state tax collections.

Fee increases have also played a significant role in balancing the state budget. The $150 million in tuition increases referenced above has raised tuition costs over a two-year period (2002-03 to 2004-05) by 18.7 percent for UW-Milwaukee students, 18.2 percent for UW-Madison students, and 16.7 percent for those at the other 4-year campuses.

Examples of other state fees increased recently are: the land record fee, court support services fees, various filing fees, and the motor vehicle registration fee. Also raised were several health care related fees such as the SeniorCare enrollment fee and BadgerCare premiums (described in more detail below). In all, over $22 million in general purpose revenue, $200 million in program revenue, and $190 million in segregated revenue is expected to be generated over the biennium from increased fees.

Table 2 below shows the fiscal effect of all fee changes implemented from fiscal years 2002 through 2005 according to the state's Legislative Fiscal Bureau.

Table 2: Revenue Impact of Wisconsin State Fee Changes, 2002-05

Fiscal Year	Fees
2001-02	43,270,900
2002-03	75,523,000
2003-04	161,795,000
2004-05	252,346,300
Totals	**$532,935,200**

Source: Wisconsin Legislative Fiscal Bureau

Health Care Budget Cuts

The 2003-05 budget bill contains cuts in a number of health care programs. The most significant of those with respect to health care coverage are two changes designed to reduce the cost of the BadgerCare program. BadgerCare provides health care coverage to uninsured children and parents with incomes below 185 percent of the federal poverty level ($28,992 for a family of three), but with too much income to be eligible for Family Medicaid (also know as AFDC-MA). Once in the BadgerCare program, families remain eligible until their income reaches 200 percent of the poverty level. The two changes and projected savings are:

- **A 60 percent increase in BadgerCare premiums –** The bill raised premiums from 3 percent to 5 percent of family income, for families with incomes above 150 percent of the federal poverty level. For a family with an annual income of $25,000, the increase is $480 per year. This change, which took effect on January 1, 2004, was projected to save $8.8 million in state and federal funds during the 2003-05 biennium ($2.5 million state general purpose revenue and $6.3 million in federal funds). Nearly $4 million of that total stems from the slower growth in BadgerCare enrollment that was expected to result because some families are unable or unwilling to pay the higher premiums.

- **More stringent requirements for verifying income and insurance –** The budget act also contained provisions imposing new requirements for BadgerCare applicants and participants to provide verification of their income and insurance status, prior to approval of their application or continuation of their coverage after an annual review. Under the previous statutes, an applicant could be found eligible while income verification and insurance status were still pending. The new verification requirements were projected to reduce spending growth by $9.3 million in the biennium ($2.7 million state GPR and $6.6 million in federal funds).[xiv] The new requirements will help ensure that BadgerCare funding is targeted to people who meet all the program eligibility standards; however, as described below, the additional red tape also appears to be turning away low-income families who do meet those standards.

The two BadgerCare changes were not expected to cause a net decrease in the program's enrollment, but were intended to substantially slow its growth. However, it appears that their actual effect will be far greater than anticipated. BadgerCare enrollment dropped by more than 17,000 people, or 15 percent, in the first nine months of 2004, even as the Family Medicaid enrollment of low-income families grew by more than 23,000 people (10.5 percent) during that same period. Typically, BadgerCare enrollment grows at a rate similar to the Family Medicaid participation, because trends in employment and private sector health coverage have similar effects for both programs. However, enrollment trends in those programs have gone in opposite directions since the BadgerCare policy changes were made.[xv] The changes in the enrollment procedures are likely to continue to reduce program participation in the coming months, though probably at a slower rate of decrease.

Appendix 2 shows some of the other significant cuts in health care spending made in fiscal year 2004 by the biennial budget bill.

TANF and W-2 Related Cuts

Many of the cuts made in the 2003-05 budget are in programs financed primarily with the child care and welfare reform block grants. (The latter block grant is known as Temporary Assistance to Needy Families, or TANF.) Thanks in part to steady growth in child care spending and a recession-induced increase in W-2 enrollment in 2001-03, the state had a $100 million per year TANF structural deficit as it approached the 2003-05 biennium.

Appendix 2 shows the many deep cuts made to reduce that structural deficit, which have substantially diminished the range of W-2 related services, as the remaining funding was focused on child care subsides and cash benefits for W-2 work. Among the most significant cuts in the TANF-funded programs are:

- The reduction of almost $14.8 million per year in “pass-through” grants to local governments to help them improve the quality of and access to child care services.
- A $21.3 million per year cut in W-2 “ancillary services” provided by the local agencies, such as training, job readiness, motivation, and social services for W-2 participants.
- Elimination of funding for the Workforce Attachment and Advancement program, which provided employment services to more than 4,500 individuals in 2001-02.

Notwithstanding the $70 million of cuts in FY 2004 shown in Appendix 2, Wisconsin still faces a $50 million per year TANF structural deficit at the end of the 2003-05 biennium. Barring any increase in federal or state revenue to support child care and W-2 related programs, the state will have to cut at least $50 million per year from TANF-funded programs in the 2005-07 biennium.[xvi]

Cuts in State Aid to Local Governments

A significant portion of the state’s resources (roughly seven percent of 2004-05 general fund appropriations) is spent every year on aid to local governments through the Shared Revenue program. Shared Revenue payments amount to the fifth largest state expenditure, behind general elementary and secondary school aids, medical assistance, corrections, and the University System.

Funding for state aids had been effectively frozen since 1995. In 2001, then-Governor Scott McCallum shocked many in the state when he proposed gutting the Shared Revenue program. While that proposal was quickly and decisively defeated, cuts in state aid to local governments have been part of the budget balancing equation in Wisconsin ever since. In 2004, Shared Revenue payments were cut by $40 million. The impact of this cut on individual local governments is discussed in more detail below.

County and Municipal Budget Pressures and Responses

Less Aid

The shared revenue program has a long history, dating back to 1911 and the implementation of the state’s individual income tax. A portion of that tax revenue was earmarked for local governments to compensate them for property tax exemptions implemented at the state level. The program has evolved since then, and its core function is one of tax base equalization. The program is credited with minimizing what would otherwise be much larger revenue disparities from one community to the next in the state.

Shared revenue accounts for a significant portion of many local governments’ total revenue. The program accounted, for instance, for 42 percent of the City of Milwaukee’s general purpose revenue in 2003 – the single largest source of general revenue for the City. Shared revenue payments accounted for 22 percent of the general revenue in La Crosse, 28 percent in Kenosha, and 19 percent in Eau Claire (all in 2003).

The $40 million cut referenced above has had a profound impact on the budgets of local governments around the state. Table 5 shows the recent shared revenue aid amounts for four counties and for the largest municipalities within those counties. Shared revenue payments for 2005 are slated to remain frozen at the 2004 levels.

Table 5: Shared Revenue and Related State Aid Payments to Local Governments, 2002-04 (Calendar Year)[xvii]

Local Government	2002	01-02 % change	2003	02-03 % change	2004	03-04 % change
Counties						
Milwaukee	59,096,439	2.0	60,681,942	2.7	57,230,975	-5.7
Kenosha	3,935,416	-1.5	3,834,341	-2.6	3,262,686	-14.9
Eau Claire	3,669,490	-4.1	3,507,724	-4.4	3,159,841	-9.9
La Crosse	5,098,833	1.9	5,230,141	2.6	4,834,356	-7.6
Cities						
Milwaukee	248,163,780	1.8	249,988,564	0.7	240,427,176	-3.8
Kenosha	17,439,011	1.5	17,872,408	2.5	16,256,575	-9.0
Eau Claire	9,375,288	0.4	9,586,381	2.3	8,593,336	-10.4
La Crosse	12,469,815	-0.1	12,660,563	1.5	11,868,618	-6.2

Source: Wisconsin Department of Revenue

In addition to the cut in Shared Revenue payments to local governments, many have had to deal with decreased funding for state or federal-mandated services run by the local governments, in particular, counties. The following are some examples of such state cuts and their impact on county governments in the state.

- **Community Aids –** The Community Aids program is a block grant to counties to assist them with the cost of mandated human services. The state GPR funding in 2003-05 for Community Aids was maintained at the 2002-03 level, but federal funding was reduced by a little over $1 million per year. Although that only cuts Community Aids by 0.4 percent, it comes on top of a long erosion of this critical source of support for county human service programs. Some of the consequences of that erosion include long waiting lists for services to people with disabilities, staffing cuts in the child welfare programs that handle child abuse and neglect cases, and insufficient programs for people with mental illness. An August 2004 study by the Milwaukee Mental Health Task Force reported that hundreds of people in the county who suffer from acute mental illness are not getting the help they need and instead have been warehoused in jail cells or left unattended to wander away from hospital emergency rooms.
- **County IGT Funds –** The 2003-05 budget eliminated the $40 million per year in federal Medicaid funding that many counties were receiving from inter-governmental transfers (IGTs). Although that funding was intended for county-operated nursing homes, the large hole created by the cut also drained money from other parts of counties' budgets.

- **Income Maintenance Administration –** Funding for county administration of income maintenance programs was cut by almost $3.5 million in 2003-04, or 6 percent.
- **Reduced W-2 Funding –** The counties that administer the Wisconsin Works (W-2) program were affected by a 5 percent cut in funding for local administration of W-2 and a cut of almost 28 percent for "ancillary services," such as training and job readiness services, provided by the local agencies to W-2 participants (see Table 2 in Appendix 2).

Increasing Costs

Along with decreased aid from the state, local governments have had to deal with rising costs. Local officials contacted for this report specifically noted rising health and dental insurance costs for their employees, pension fund contribution increases, fuel and utility costs, and wage pressures.

For example, officials in Eau Claire County expressed concern about the cost of health insurance for its employees, a cost which increased by 45 percent in 2002, 10 percent in 2003 and 13 percent in 2004 – about an 80 percent increase over three years. The County's required pension fund contributions also have increased recently, and though the stock market has rebounded to some extent in the past year, the County sees those required contributions continuing to increase over the next three to four years.

The City of Glendale, a relatively wealthy suburban city north of Milwaukee, is experiencing many of the same serious budget issues as other municipalities around the state. Revenues coming into the city decreased by over $364,000 from 2003 to 2004, because of shared revenue cuts and declining revenue form the hotel/motel room tax and various fees. On the cost side, health and dental insurance for city employees increased 24 percent in 2002, 22 percent in 2003, and 18 percent in 2004, for a total increase of 78 percent from 2002 to 2004. The increase in 2004 alone amounted to over $280,000, and other costs have been increasing as well. City officials pointed out increases in electrical, natural gas, fuel, liability insurance, and telephone services.

As local governments around Wisconsin face rising costs and decreased state aid, as well as continuing state and federal mandates, they have struggled to balance their budgets. Local governments, like the state government, cannot run deficits, and have only a handful of options available for increasing revenues or decreasing their expenditures. Were the state budget on sounder footing, state aid could have remained level or even risen to assist localities with their increased cost pressures.

Residents Face Increased Fees

In response to the loss of state aid and rising costs, local elected officials have cut staff, raised fees, pared back basic services, reorganized and restructured departments, and in some cases increased their property tax levies.

Nearly half of the local governments surveyed by the Legislative Audit Bureau implemented new fees between 2001 and 2003 — 275 new fees altogether.[xviii] And nearly 40 percent of those surveyed plan to establish new fees in the next three years, with 12 percent more considering such fees. Some of these enacted fees are:

- County jail room and board fees
- Cremation fee
- Park shelter reservation fees
- Garbage and recycling fees
- Stormwater management fees

A brief look into our four-county areas of examination reveals the extent to which local governments have relied recently on increased fees. Eau Claire County, for example, managed to generate close to $200,000 in new revenue in 2004 from fee increases. In Glendale, fee increases raised the costs for various permits, licenses and other applications. Others fee increases – including new fees for businesses, recycling and refuse collection – were proposed but eventually cut from the budget, and those options loom large as the city faces continued tough fiscal times.

Positions Cut and Services Pared Back

Nearly every local government in the four areas contacted for this report reported position cuts and pared-back basic services. The size of the cuts ranged from a couple of administrative support positions to, in the case of the City of Milwaukee, over two thousand positions eliminated between 2001 and 2004. Other examples of local government cuts abound.

Since 2001, Kenosha County has eliminated 35 levy-funded positions. These include eleven human services positions, seven from the Sheriff's Department, and ten public works positions, among others. Twenty of the position cuts came in 2004. The 2004 cuts helped the county reduce its levy by $900,000 in that year alone. Waiting lists have been increased in many human services programs according to county personnel. One example cited by several staff is its intensive in-home program for juveniles, which provides a positive alternative to placing juveniles in a county facility, away from family and with other individuals who can lend needed support. Staff reported that waiting lists for this program have increased from a week to over a month.

Due to the costs mentioned earlier, in 2004 Eau Claire County found that in order to continue providing services at the previous year's level, it would have to increase its property tax levy by over 29 percent. County officials worked hard to reduce that increase by cutting operational costs in all departments, reducing county staff by 25 positions, reducing funding of community agencies by 10 percent in most cases – resulting in a spending reduction of over $2.5 million – and, as mentioned earlier, increasing fees. The positions cut were from several departments including sheriffs, highway laborers, and human services personnel. The county also closed its Anne Street facility, a group home, and began contracting out for such services. In the end, county officials managed to reduce county spending, but still needed to increase their levy by 8.8 percent.

Cultural and recreation expenditures have been cut in most of the county and municipal budgets looked at for this report as well. In Eau Claire County, the Kemper Center levy funding was eliminated, but the county began using money from its reserve fund to pay for operations of the facility. While the facility remains open and operational, funding it from the county reserves is an unsustainable practice. The Kenosha History Center, which had received $138,500 in 2003 from the county saw that amount drop down to $100,000 in 2004, a cut of 28 percent. Interestingly, the county was only able to fund the Center at that level because it eliminated a disaster preparedness program intended to screen mail for foreign substances.

Milwaukee County Executive Scott Walker has made dramatic cuts to a variety of county programs that directly affect residents there. In order to meet a self-imposed pledge to hold the line on property taxes, county officials have recently made substantial cuts in funding for AIDS prevention, homeless shelters, youth employment, University of Wisconsin Extension programs, and county-run mental health case management.

A wide range of other cuts have also been made in Milwaukee County, including reduced funds for mass transit, the parks system, and a county-funded snow-shoveling service for the elderly. These cuts, while significant to those who utilize these services and county amenities, pale in comparison to those that directly affect the health and well being of the county's neediest.

For example, staff and funding cuts in the area of mental health are specifically being blamed for a near-crisis situation at the County's Mental Health Complex. Given the nature of the illnesses and issues dealt with there, understaffing the Complex is particularly dangerous, both to staff and the patients themselves. An investigation by Milwaukee Journal Sentinel staff revealed that from late April to late June of 2004, 62 mentally ill patients waited in emergency rooms between two and 60 hours before being taken to the Mental Health Complex for treatment.[xix]

La Crosse County officials note that the area hit the hardest there has been the provision of basic human services. Over $1 million in spending was cut in the Family and Children Services area in 2004, a move which staff describe as "coming back to haunt them" because of sharply increased demand for services, a reality brought about at least in part by the continued sluggishness of the economy.

In the City of La Crosse, 13 positions were cut in 2004 including three in the police department and four in the fire department. Several services were pared back as well, for instance, instead of sending road plowing crews out at night after a storm – and thereby having to pay overtime – the city waits until the next morning so the work can be done during regular hours. This example is only one of many such parebacks discussed by local officials.

Large and small municipalities alike have found themselves with tight budgets in recent years, but the scale of the cuts is much more dramatic in larger cities, especially Milwaukee. It has cut city positions by nearly 18 percent since 2001; from 11,748 in 2001 to 10,526 in 2002, 10,340 in 2004, and 9,675 in 2004. It also reorganized several departments to reduce costs and implemented a long list of other cost-saving moves. For example, libraries cut their hours and decreased equipment and material purchases. In the fire department, staff on single engine companies was reduced from five personnel to four, and overtime pay was reduced. Various public works services were pared back, including reducing snow plowing and salting, reducing the frequency of tree pruning, purchasing fewer vehicles, and reducing facility upkeep.

Higher Property Tax Bills

The picture that develops is one of many local governments dealing with their budget gaps by cutting personnel, implementing and increasing fees, increasing waiting lists for some programs and paring back basic local services. While many local governments have sought to limit the increase in their portion of the property tax levy, Wisconsin residents in some locations have been faced with significantly higher property taxes recently.[xx]

The table below shows the average property taxes paid by homeowners over the last few years in the major cities in each of the four counties that we looked at for this report. Although the cities do not all use the same method of tracking the typical tax rate for residential property, which makes comparisons between cities problematic, the statistics illustrate the average changes in residential property taxes for each city.

Table 6: Average Residential Property Taxes Paid in Several Wisconsin Municipalities, 2001-03[xxi]

Municipality	2001	2002	2003	% Change, 01-03
Eau Claire	$2,038	$2,247	$2,230	9.42%
Kenosha	$2,880	$3,018	$3,092	7.36%
La Crosse	$2,365	$2,275	$2,419	2.28%
Milwaukee	$2,029	$2,444	$2,513	23.85%

Source: Municipal finance directors in each locality.

Table 6 shows that property tax increases have varied greatly from one community to another, thanks in part to differences in state aids cuts. Nevertheless, almost all local governments have been in a similar bind. Notwithstanding substantial cost cutting at the local level, the state reductions in local aids and erosion of those aids by inflation have put upward pressure on local property taxes.

Wisconsin communities are not alone in seeing the trickle-down effect of reduced state and federal funding. A recent analysis prepared for the Wall Street Journal by the Federal Reserve Bank of Boston showed that nationwide, local governments have been turning to the property tax to make up for state and federal funding shortfalls.[xxii] As a share of state and local revenue, the local property tax has risen significantly – from 25.5 percent in the first quarter of 2001 to 28.2 percent in the first quarter of 2004. Meanwhile, income taxes as a percentage of state and local revenue fell, and sales taxes rose only slightly. Property taxes represent the one significant revenue source over which local governments retain some discretion.

Schools are Hit Hard and are Under Increasing Pressure

The news today is filled with stories of school program cuts, teacher layoffs, and school construction and maintenance delays. By all accounts, public schools in Wisconsin are experiencing a funding crisis. The best response to this crisis is a matter of heated debate, and state and local education officials are currently considering various school finance reform options. There is little doubt, however, that the significant and costly reforms associated with the No Child Left Behind law as well as the continued underfunding of the Individuals with Disabilities Education Act, are contributing to this crisis, with perhaps the worst to come.

Underfunded Federal Mandates on Schools

The federal government's education policies have a direct and significant impact on local schools. Recently, mandates in the areas of special education and student testing have added to the responsibilities of school districts and individual teachers alike. As mentioned earlier, both the Individuals with Disabilities Education Act, and the No Child Left Behind law have brought significant costs to Wisconsin schools over the last few years. The total cost from these measures for Wisconsin has been identified by the Center on Budget and Policy Priorities as over $1.1 billion. Others have given estimates for these costs as well, and offer support to the contention that federal education policies are seriously exacerbating the fiscal duress of local schools and school districts.[xxiii]

The Individuals with Disabilities Education Act, or "IDEA," is the federal law designed to provide special education for children with disabilities. For qualifying disabled students, school districts must provide free appropriate public education in the least restrictive environment as specified in a child's annual individual education plan. The federal government promised to pay 40 percent of the costs associated with providing the special education services mandated by the law.

The law was a significant step forward for those students who would benefit from its provisions. The problem has come with the lack of federal financial support for it. Currently, nationwide, federal funding amounts to 19 percent of the costs associated with the law. In Wisconsin, the funding shortfall from 2002 to 2005 equals $784 million. School districts throughout Wisconsin have been forced to reduce the general education services they offer due to the greater share of the law's cost that they're required to pay.

Much has been written about the No Child Left Behind law. The significant new standardized testing and reporting requirements and teacher qualification standards placed on schools and students have been a controversial development to say the least. This substantive development will continue to be debated. The budget impact on school districts is another controversial aspect of this law, and is one that is only beginning to be felt. Many of the law's testing deadlines arrive over the next couple of years, and school district administrators around the state have told us of the likely need to reallocate significant amounts of revenue from their general education efforts in order to meet these testing requirements.

State Aid Commitment to Schools

The impacts of underfunded and unfunded federal mandates are only adding to an already difficult situation for Wisconsin's public schools. School districts have just taken a significant budget hit from the state. In 1995, the state took on a commitment to pay two-thirds the cost of K-12 education not funded by the federal government. This change was meant not as an increase in the amount of funds going to schools in the state, but as a property tax relief measure, as schools had primarily been funded by the local property tax.

In the recent 2003-05 state budget, the Governor and Legislature repealed the two-thirds commitment and reduced state support for public education. State support fell from 66.35 percent in 2002-03 to 65.16 percent in 2003-04. The Legislative Fiscal Bureau estimates that state support will fall further in 2004-05 – down to 63.75 percent. While the actual dollar amount going to public school districts increased by $113 million during the biennium, if the state had maintained its commitment at the two-thirds level, schools would have received about $375 million more – in addition to the $113 – during this two-year period.

Examples of School District Budget Pressures

Public school officials in Wisconsin are facing serious budget pressures. Some of these are identical to those faced by other local governmental bodies throughout the state, such as increased health insurance[xxiv], utility, and fuel costs. Others, such as the effect of declining enrollment on state aid, are unique to the schools.[xxv] Also, the continued underfunding of IDEA and the increasing impact of underfunding the No Child Left Behind law add further stress to their budgets.

Cumulatively, these factors are causing teacher and support staff losses, larger class sizes, capital project delays, elimination of many sporting and cultural opportunities, as well as summer programming, and increased fees for a variety of school activities. As a result, the quality of education for Wisconsin children is diminished, families have to cope with many fee increases, and those fees put extracurricular activities out of the reach of some students.

We examined the budget choices made by the school districts in the four counties mentioned earlier. What we found is that both large and small school districts are experiencing serious budget difficulties and expect to continue facing them over the next few years.

The Milwaukee Public School District faces many of the same budget pressures as other school districts, but offers a particularly dramatic illustration of the fiscal bind experienced by districts across the state. It adopted a 2004-05 school year budget that contains a property tax increase of 15.4 percent (the largest increase in 20 years) and 450 job cuts, including 300 teaching positions. These cuts come on top of more than 660 positions eliminated the previous year – 307 of which were teaching positions.

Summer program funds have been cut in Milwaukee, and capital improvements have been delayed. School district officials made a point of expressing deep concern about the impending No Child Left Behind testing deadlines and talked of the significant amount of funds that will have to be reallocated from general education purposes to meet those deadlines.

In the La Crosse School District, the school portion of the property tax is going up this year for the first time in six years, despite a cut of over $3 million in spending from the previous year's budget. Some of the savings came from cutting 42 positions, including 26 teachers and two administrators. Class sizes are to increase, and extra-curricular offerings have been pared down.

School district officials there specifically pointed out the decreased state aid and underfunded federal mandates and the negative impact those have had on its recent budgets. In addition to the cut positions and the increased taxes, the district will close at least one school (and one *or more* additional schools are likely to be closed if an upcoming referendum on school spending is not approved by voters).

In the Bristol school district (in Kenosha County) officials expressed concern about the approaching deadlines associated with the No Child Left Behind law. The costs associated with increasing their testing of students come at a time when they are already having particular trouble providing ESL – English as a second language – services for a growing population of non-English speakers.

Wheatland Center officials (in Kenosha County) talked of having to lay off employees for the first time ever. They cited the impact of declining enrollment in their schools, and how the state funding formula decreases their aid by more than the amount that their costs actually fall from having fewer students. Interestingly, other districts that are experiencing enrollment growth and are adding staff – such as the Kenosha Unified District and the Holmen School District in La Crosse County – note that the costs of health insurance and other benefits offered to an expanding workforce are rising much faster than revenue limits allow, thereby putting more pressure on each districts' overall budget.

Wauwatosa (in Milwaukee County) has also had to deal with how the funding formula addresses declining enrollments. They have had to downsize offices, eliminate some school aids, and reduce teaching staff. Future budgets, we are told, will likely include closing buildings, increasing class sizes, and selling off district assets.

Continuing Fiscal Challenges

Federal Policy – Increasing Costs and Less Aid

Since 2002 most states, including Wisconsin, have had trouble coming up with enough revenue to continue existing spending commitments, much less meet the increased responsibilities associated with unfunded mandates and other federal policy changes. This state fiscal crisis has been well documented. What may come as a surprise to some is that even as our economy recovers and jobs are created, the states will continue to face significant budget gaps in the coming years, partially due to the federal policies enumerated in this report. In Wisconsin, the cost of these federal policies is growing, as seen in Figure 1 in the Executive Summary.

The types of fiscal problems described in this report are likely to be exacerbated by future federal budget cuts. A White House Office of Management and Budget memo that was obtained earlier this year by the Washington Post directs federal agencies to prepare budgets that include significant spending reductions in 2006. For example, it calls for a cut of $177 million to the Women, Infants and Children (WIC) nutrition program, a $177 million cut to Head Start, $1.5 billion less for discretionary spending by the Department of Education, and over $900 million cut from the Veterans Administration.

The White House has described that memo as merely a starting point, and it is too early to tell if the federal government will be further reducing its funding for basic human services and the mandates it places on the states and local governments, as many now fear.

State Budget Deficits and Program Shortfalls

Although the state and local effects of the federal policies have been broad, and in some cases significant, greater problems lie ahead. Wisconsin's budget writers have employed numerous short-term solutions and accounting gimmicks that have delayed the necessity of making hard choices between cutting services or raising taxes. For example, the level of general obligation and revenue bonding increased by about 77 percent in the 2003-05 biennial budget, growing to $3.57 billion, from $2.03 billion in 2001-03, which will mean higher debt repayment levels in the future.

The Legislative Fiscal Bureau (LFB) estimated in June 2004 that Wisconsin faces a general fund "structural imbalance" of nearly $1.6 billion in the 2005-07 biennial budget ($742 million in 2005-06 and $849 million in 2006-07). The "structural imbalance" is the amount of revenue growth that is needed in coming years simply to maintain programs at current funding levels – without factoring in any inflationary increases or caseload growth.

Although the LFB figures are very sobering, they do not fully capture the extent of the state's fiscal challenges. As noted previously, the Legislature added an amendment to the 2003-05 budget bill directing $100 million to be cut from agency operations in each year of the 2005-07 biennium. On paper, that amendment reduced the "structural imbalance" by $200 million, but it also means that if the next biennial budget were balanced by cuts alone, those cuts would have to total $1.8 billion. Also, the Fiscal Bureau's calculations do not factor in the current Medicaid deficit, which they estimate to be $224 millionin state dollars in the current biennium.

Another potential problem stems from the fact that last budget included additional revenue of $157 million over the biennium stemming from renegotiated gaming compacts with the state's Indian tribes. Since that time, the Wisconsin Supreme Court invalidated those compacts, and it remains to be seen whether the original estimate for additional revenue is realized. Any amount short of this estimate will have to be made up elsewhere.

The figures cited above focus just on the state's general fund structural imbalance. It should be remembered that the state also has a $50 million per year structural deficit in the TANF budget for the Wisconsin Works program and related services.

The grim fiscal outlook for both the general fund and other parts of the budget caused Governor Doyle to issue 2005-07 budget instructions to state agencies requesting they cut their operating budgets by ten percent. Because of the cuts already made at the state level, as described earlier in this report, it will be increasingly difficult for state agency personnel to cut their budgets without continuing to have significant effects on those Wisconsin residents served by the respective state agencies.

Federal Tax Cuts Fail to Offset Other Federal Policies for Many in Wisconsin

Several federal tax cuts have been implemented in recent years. The cost of these cuts to the country has been significant. In fact, the tax cuts enacted since 2001 have been more costly than any of the other budgetary actions by the federal government – costlier than the *combined* impact of new spending for homeland security, the war in Iraq, operations in Afghanistan, expanded anti-terrorism efforts, and all domestic spending increases over the last three years.[xxvi]

These tax cuts have come at a time when the federal government could have been increasing its aid to the states, or more fully funding the mandates it has placed on state and local government around the country.

For a small number of very-high-income Wisconsin residents, the benefits of the federal tax cuts have probably outweighed the direct costs of state and local budget difficulties. For example, this year the wealthiest one percent of Wisconsin residents — a group with an average annual income of $754,000 — will receive an average benefit of $47,485 from the 2001-2003 tax cuts, according to the Institute on Taxation and Economic Policy.[xxvii]

For many lower- and middle-income Wisconsinites, however, the benefit of the tax cuts is likely to be outweighed by the harm done by state and local budget cuts. For instance:

- In 2004, the average federal tax cut for a Wisconsin taxpayer in the middle fifth of the income spectrum is $971. That is nearly one-third less than the increase in annual tuition costs over the last two years for students at UW-Madison and UW-Milwaukee, and slightly less than the tuition increases at the other UW campuses.
- The average federal tax cut in 2004 for Wisconsin taxpayers in the poorest 60 percent of households is $529. That is less than the premium increase for many of the families participating in BadgerCare.
- As federal policies restrict state revenue, and the state cuts local aid, property tax payers, homeowners and renters across the state are paying higher property taxes. Residential property taxes rose by an average of $322 per household from 2001 to 2004, or $185 in inflation-adjusted terms.

The federal tax cuts are also having a negative long-term impact on Wisconsin residents by contributing to the national debt. Most economists agree that the added debt eventually will have to be repaid, either through tax increases or in further reductions in public services.

Conclusion

Federal policies relating to taxes, health care, and unfunded or under-funded mandates have cost the state of Wisconsin $2.4 billion from 2002 through 2005 by conservative estimates. These costs have hit the state and local governments just as they have faced other fiscal distress, and have made it more difficult for them to balance their budgets. The resulting state and local budget cuts, fee increases and property tax hikes mean people in Wisconsin are now paying more for less.

Wisconsin has not seen the end of its fiscal troubles. The numerous temporary measures used to balance the last two biennial budgets have left the state in a deep fiscal hole. Some combination of deeper spending cuts and additional state and local tax and fee increases can be expected in 2005-07. Furthermore, even as our economy improves, the negative fiscal impact from federal policies is growing and will continue to hamper efforts by state and local officials to balance their budgets without severely impacting the quality of life in Wisconsin.

Appendix 1: Short-term Measures Used to Balance the 2003-05 Budget

In addition to the significant cuts made in the 2003-05 budget, the $3.2 billion deficit was closed with numerous measures that are very short-term fixes. Some of the more significant of those include the following:

- One-time transfers totaling $175 million from the Transportation Fund to the General Fund.
- Use of an additional $400 million from the Transportation Fund in for Shared Revenue.
- $352 million of one-time federal fiscal relief.
- Transferring about $46 million from the utility public benefits fund, mostly on a one-time basis.
- Roughly $145 million in other segregated or program revenue funds that are transferred or lapsed to the General Fund.
- A short-term savings of more than $140 million by using bonding to finance pension and sick-leave obligations.
- $28 million saved on a short-term basis by replacing the reserves in the Clean Water Fund with a surety bond.
- A reduction in the required statutory balance (from $235 million to $45 million), freeing up $190 million that will have to be restored in the 2005-07 budget.

After the 2003-05 budget bill was enacted, the state's fiscal situation continued to deteriorate, and the state did not receive some of the federal funding for Medicaid that legislators had included in the budget bill. As a result, the Legislative Fiscal Bureau estimated early in 2004 that the state's Medicaid budget had a general fund shortfall of about $400 million. The Legislature subsequently approved two more short-term remedies to narrow that deficit:

- Act 129 approved debt restructuring to cut interest payments by $175 million in FY 2004 and put $122.5 million of that amount into Medicaid.
- A special session bill approved in late May 2004 generates $52 million, on a one-time basis, by transferring Community Aids funds to the state Medicaid appropriation, and using them to draw down federal matching funds.

These two measures reduced the projected Medicaid shortfall to $224 million GPR. Although they helped state budget writers get through the 2003-05 legislative session, neither provides a long-term source of funding, and Act 129 actually reduces the revenue available in future years by increasing expenditures for bond principal and interest.

Appendix 2

Selected State Cuts in Health Care and Workforce Support Programs

The most significant cuts in health care spending, from the perspective of access to health insurance, were the premium increases and other policy changes made in the BadgerCare program, discussed in the text. However, there were also a number of other cuts in health care, which are shown in Table 1.

Table 1: Selected Health Care Cuts in 2003-04

Health Care Programs	2002-03 Base ($)	2003-04 Cut ($)	Percent Cut
WisconCare (GPR)	750,000	750,000	100%
Graduate medical education (GPR)	11,890,000	10,890,000	91.6%
County IGT funding	40,000,000	40,000,000	100%
Tobacco control and prevention (all funds)	15,345100	5,290,700	34.5%
Northern WI Center (all funds)	29,400,600	11,432,700	38.9%

The 2003-05 budget also made numerous cuts in programs financed primarily with federal funding from the child care and welfare reform block grants. (The latter block grant is known as Temporary Assistance to Needy Families, or TANF.) There are a number of reasons for these cuts, including:

- Frozen TANF Funding – The amount of federal funding for the TANF block grants has been frozen since the program began in FY 1997. If TANF funding had been adjusted for inflation since that time, Wisconsin's FY 2004 allocation would have been almost $58 million higher, and it would be about $64 million higher in FY 2005.
- Increased Child Care Spending – A little more than half of all TANF and other W-2 related funding is spent for child care. The number of children served by the Wisconsin Shares child care subsidy program grew by 63 percent from FY 2000 to FY 2004, and spending grew by a little over 80 percent during that four-year period. This has required reducing or eliminating spending for other TANF-funded programs.
- Diminished State Funding – In the early years of the W-2 program, spending for child care subsidies was significantly less than anticipated and enrollment in cash benefits dropped dramatically. As a result, the state built up a large TANF surplus, which it began to use in 1999 for a variety of new purposes – including replacing about $50 million per year of state funding for the earned income tax credit. Although that decision was not essential at the time, Wisconsin's current fiscal difficulties, and the federal policies that greatly exacerbate them, make it nearly impossible to restore the state funding that was cut in 1999.

With the steady growth in child care spending and the recession-induced increase in W-2 enrollment in 2001-03, the state had a $100 million per year TANF structural deficit as it approached the 2003-05 biennium. Table 2 shows the many deep cuts made to reduce that structural deficit and substantially diminish the range of W-2 related services, as the remaining funding was focused on child care subsides and cash benefits for W-2 work.

Table 2: Cuts in 2003-04 in TANF-funded and W-2 Related Programs

Child care/early education	**2002-03 Base ($)**	**2003-04 Cut ($)**	**Percent Cut**
Child care grants to local governments	17,253,200	14,778,100	85.7%
Head Start (TANF & GPR)	7,425,000	212,500	2.9%
Scholarship & bonus funding	6,007,200	3,307,200	55%
Early Childhood Excellence Centers	2,750,000	250,000	9.1%
Child Care Resource & Referral agencies	1,355,300	135,500	10%
Racine demonstration project	1,000,000	1,000,000	100%
Technical assistance	995,300	995,300	100%
Safe Child program	580,000	580,000	100%
Other TANF and W-2 related programs			
W-2 agency services to participants	76,941,900	21,335,300	27.7%
Local agency administration	22,279,700	1,114,000	5.0%
Community reinvestment	5,539,700	5,539,700	100%
Kinship care	24,852,600	730,400	2.9%
Job access loans	600,000	400,000	66.7%
State administration	21,721,000	3,236,500	14.9%
Partnership for Full Employment	1,756,700	1,756,700	100%
Fraud & front-end verification	661,400	661,400	100%
W-2 financial oversight	554,100	554,100	100%
Transportation	900,000	900,000	100%
Legal services	100,000	100,000	100%
Workforce Attachment & Advancement	7,842,200	7,842,200	100%
Literacy programs (TANF)	800,000	800,000	100%
Aid to Milwaukee Public Schools (TANF)	1,410,000	1,410,000	100%
Badger Challenge	1,816,500	449,400	24.7%
Nutrition services (TANF)	1,000,000	1,000,000	100%
Immunization (TANF)	1,000,000	1,000,000	100%
Domestic violence services (TANF)	1,000,000	250,000	25%

Footnotes

i Iris J. Lav is Deputy Director of the Center on Budget and Policy Priorities (CBPP); John Keckhaver is a Policy Analyst at the Wisconsin Council on Children and Families; and Jon Peacock is Director of the Wisconsin Budget Project, which is part of WCCF. Nick Johnson, who is the Director of the State Fiscal Project at CBPP, also made numerous contributions to this report. The authors wish to thank numerous staff of local governments and the Legislative Fiscal Bureau who provided data and responded to inquiries. The authors are solely responsible for any errors.

[ii] See Andew Brecher and Iris J. Lav, *Passing Down the Deficit: Federal Policies Contribute to the Severity of the State Fiscal Crisis*, August 18, 2004, available on the Center on Budget and Policy Priorities website at http://www.cbpp.org/5-12-04sfp.htm.

[iii] The property tax growth is calculated from net figures (after subtracting state tax credits) produced by the Legislative Fiscal Bureau (LFB) in Information Paper #13 (January 2003) and in a September 20, 2004, memo to Senator Jon Erpenbach.

[iv] State-specific data on the distribution of the federal tax cut come from the microsimulation model developed by the Institute on Taxation and Economic Policy from U.S. Treasury tax data.

[v] The Wisconsin Department of Revenue recently estimated the lost revenue to the state in 2003 at between $86 and $141 million for internet sales and $115 for catalog and telephone remote sales, for a total loss of between $201 and $256 million for that one year, an amount similar to the CBPP estimate. For a more complete discussion of Wisconsin's sales tax provisions including those concerning electronic commerce and remote sales see the Wisconsin Legislative Reference Bureau's Information Paper #6, *Sales and Use Tax*, January 2003, available on their website at http://www.legis.state.wi.us/lfb/Informationalpapers/6.pdf.

[vi] Wisconsin's estate tax will remain decoupled from federal estate tax provisions until January 1, 2008 when it will re-couple with federal law. The state will therefore begin losing estate tax revenue in 2008 unless current state law is changed. Federal estate tax provisions, which included a gradual phase-out of the estate tax between 2002 and 2010, will sunset in the year 2010 unless current federal law is changed. Wisconsin's decoupling from federal depreciation provisions, on the other hand, is permanent barring any change in current state law.

[vii] The CBPP report, *Passing Down the Deficit: Federal Policies Contribute to the Severity of the State Fiscal Crisis*, and this report deal only with those mandates that have resulted in easily quantifiable impacts on the states. There are a number of other under- or un-funded federal mandates at work presently. The costs given of recent federal policies on the states, then, represent a conservative estimate. For another discussion of federal mandates on state and local governments, including a somewhat broader list of mandates analyzed, see the National Conference of State Legislatures, *The Mandate Monitor*, March 31, 2004.

[viii] For a more thorough discussion of the Individuals with Disabilities Education Act and other special education issues, see the National Education Association's website, http://www.nea.org/specialed/.

[ix] For a discussion from the Department of Education regarding the No Child Left Behind Act, see their desk reference to the legislation at http://www.ed.gov/admins/lead/account/nclbreference/index.html. See also the Learning First Alliance's report *Major Changes to ESEA in the No Child Left Behind Act*, available at the Alliance's website, http://www.learningfirst.org/.

[x] For more information on HAVA and other democracy-related issues and legislation see the Demos website at http://www.demos-usa.org/page14.cfm.

[xi] For a more thorough discuss of the new Medicare legislation, see the National Health Law Program website at http://www.healthlaw.org/medicare.shtml.

[xii] John Springer, *A Brief Overview of State Fiscal Conditions and the Effects of Federal Policies on State Budgets*, May 12, 2004, available on the Center on Budget and Policy Priorities website at http://www.cbpp.org/10-22-03sfp4.htm.

[xiii] Liz McNichol, *The State Fiscal Crisis: Extent, Causes, and Responses*, April 24, 2003, available at the Center on Budget and Policy Priorities website at http://www.cbpp.org/4-24-03sfp.htm.

[xiv] BadgerCare enrollment was expected to decline by 439 people per month – with a cumulative drop of nearly 8,000 people by the end of FY 2005. The changes in verification requirements are the chief cause of the projected decrease; but the estimate also includes the modest effect of a change making it easier for the state to help purchase employer coverage for certain employees eligible for BadgerCare.

[xv] An informal report by Jim Jones in the Department of Health and Family Services, "Analysis of BadgerCare Enrollment Trends, (Oct. 1, 2004) reveals that a portion of the decrease in BadgerCare enrollment since April, 2004 (perhaps as much as a third) can be accounted for by a decrease in 2004 in the number of family Medicaid recipients moving into BadgerCare.

[xvi] The initial 2005-07 budget proposal submitted by the Department of Workforce Development on Sept. 15, 2004, contains proposed TANF spending that exceeds available funding by $129.6 million.

[xvii] These amounts, provided by the Department of Revenue, include the following programs/payments (not all those listed were in place in each year or are applicable to each unit of government listed in the table): Utility Entitlement, County Mandate Entitlement, Aidable Revenues Entitlement, Minimum-Maximum Adjustment, 1% Increase Shared Revenues, County and Municipal Aid Payment, SMSR Entitlement, and Expenditure Restraint Entitlement.

[xviii] Wisconsin Legislative Audit Bureau, *Best Practices Review: Local Government User Fees*, April 2004, available at the Bureau's website at http://www.legis.state.wi.us/lab/reports/04-0UserFeesFull.pdf.

[xix] See the June 27, 2004, Milwaukee Journal Sentinel article, "Urgently needed mental care delayed," by Dave Umhoefer and Joe Manning, at http://www.jsonline.com/news/metro/aug04/253273.asp

[xx] In most localities, property tax rates have been decreasing, but total levies have been driven higher by growth in valuations.

[xxi] Municipalities often keep records of their property taxes and property values in different ways. For instance, in Eau Claire and Kenosha, the property taxes listed represent those paid on the average assessed value for all residential property. In La Crosse, the taxes listed represent those paid on residential properties of one to three dwelling units, and in Milwaukee, those paid on the single family median home.

[xxii] Downturn Made States and Cities More Dependent on Property Taxes, Ray A. Smith, The Wall Street Journal, August 24, 2004, p. A1.

[xxiii] See estimates of the costs to each state of federal education policies including IDEA and the No Child Left Behind Act at http://www.nea.org/lac/fy04edfunding/#charts.

[xxiv] A study released September 24, 2004, by the Wisconsin Taxpayers Alliance, *School Districts Challenged by Health Insurance Costs,* found that family health insurance premiums paid by Wisconsin school districts increase by an average of 40.7 percent from 2001-02 to 2003-04.

[xxv] Revenue caps that were placed on schools in 1993 essentially tie their annual budget growth to inflation and school enrollment. As a result, districts with declining enrollment have declining enrollment, as well as reduced school aid.

[xxvi] See *Deficits and the Mid-Session Review*, Center on Budget and Policy Priorities, revised August 2004.

[xxvii] State-specific data on the distribution of the federal tax cut come from the microsimulation model developed by the Institute on Taxation and Economic Policy from U.S. Treasury tax data.