

SEVERE STATE FISCAL CRISIS MAY BE WORSENING

States have closed, or are closing, about \$80 billion in budget shortfalls for the current fiscal year (which ends June 30 in most states) and another \$79 billion in shortfalls for FY 2004, according to the National Conference of State Legislatures. Forced by balanced budget requirements to close these deficits, states have been cutting important programs and services, including education, health care, and public safety.

Now the crisis appears to be worsening. New data show that in a number of states, including California, Colorado, Connecticut, Idaho, New York, North Carolina, and Pennsylvania, revenues for April fell short of expectations, so these states are raising their deficit forecasts. Clearly, states are unlikely to pull out of the fiscal crisis by themselves anytime soon. Without new revenues, states are likely to enact increasingly painful budget cuts.

What Public Services Are Being Cut?

States spend most of their money on education, health care, public safety, and human services. All of those areas have been subject to sharp reductions in recent months, and more cuts lie ahead.

- *Health care.* Hundreds of thousands of people nationwide have already lost Medicaid coverage due to state budget cuts. That number will climb to 1.7 million people if the cuts proposed by governors in 22 states for which we have detailed information are approved.
- *Elementary and secondary education.* States such as California, Missouri, Oklahoma, and Oregon cut public school spending midway through the current school year. For the upcoming year, at least 18 states are planning or considering cuts, according to NCSL. The likely consequences include teacher layoffs, school closures, and shortened school years.
- *Higher education.* Most states have cut aid to colleges and universities over the past year. This has resulted in faculty layoffs, cancelled classes, and large tuition increases, among other measures. Sixteen states raised tuition by more than 10 percent for the current school year, and six states took the unusual step of enacting mid-year tuition hikes for the spring 2003 semester. Also, seven states have already raised tuition for the 2003-04 school year by anywhere from 10 percent to 39 percent; large tuition hikes are on the table in about 16 other states.

Examples of Cuts in Services

- **Oregon** — Some 50 school districts are shortening the school year.
- **Ohio** — Some 17,000 children are losing child care subsidies.
- **Kentucky** — almost 900 non-violent offenders were released early from prison.

- *Public safety.* Some 19 states are implementing or considering cuts in corrections spending, according to NCSL. The likely consequences include paroling nonviolent offenders, moving prisoners to cheaper out-of-state facilities, or closing prisons.
- *Aid to local governments.* Local governments in most states are responsible for police, fire, and many other services. A number of states support local governments through revenue-sharing, but a dozen or more of these states are scaling those programs back.
- *Child care and other human services.* Many states are cutting human services spending substantially. For instance, a large number of states are cutting child care subsidies for poor and near-poor working families, making it difficult for parents to remain in the workforce. A General Accounting Office survey issued this week found that 23 states have reduced access to affordable child care since 2001 through tightened eligibility, increased co-payments, or other measures. In addition, ten states plus the District of Columbia are proposing more child care cuts for 2004.
- *Tax increases.* A number of state constitutions impose major barriers to tax increases, such as supermajority or voter-approval requirements. Nonetheless, some 17 states raised taxes significantly in the current fiscal year, and some 25 governors have proposed raising taxes for the coming year. Among the enacted increases are major hikes in income, sales, or business taxes in Connecticut, Idaho, and Massachusetts.

State Budget Shortfalls May Be Growing

Though significant, the spending cuts states have already enacted are far from sufficient to solve their budget crisis. As of late April, states still faced about \$22 billion in shortfalls for 2003 and another \$54 billion for 2004, according to NCSL. With rainy day funds and other reserves largely drained, and with very limited ability to borrow funds to cover operating costs, states are likely to close these shortfalls through large spending cuts and perhaps tax increases.

Ultimately, the amount of spending cuts may well exceed what anyone has acknowledged to date. In the last few days, states such as California, Colorado, Connecticut, Idaho, New York, North Carolina, and Pennsylvania have reported lower-than-expected revenues for April. Because April marks the end of the income tax filing season, states pay close attention to April receipts in developing revenue projections, and often revise forecasts as a result.

The national scope of the revenue problem is confirmed by U.S. Treasury reports, which show federal taxes coming in below last year's levels and lower than expectations. Since state income taxes use essentially the same tax base as federal income taxes, the Treasury reports — combined with initial state reports for April — suggest that the state fiscal crisis may be getting worse and that even more painful measures may lie ahead.