STATE BUDGET UPDATE: FALL 2013

NATIONAL CONFERENCE of STATE LEGISLATURES

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Fiscal Affairs Program
National Conference of State Legislatures
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The National Conference of State Legislatures is the bipartisan organization that serves the legislators and staffs of the states, commonwealths and territories.

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- To improve the quality and effectiveness of state legislatures.
- To promote policy innovation and communication among state legislatures.
- To ensure state legislatures a strong, cohesive voice in the federal system.

The Conference operates from offices in Denver, Colorado, and Washington, D.C.

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State Budget Update: Fall 2013

Four and half years after the end of the Great Recession, state budget recovery remains a work in progress. Although fiscal conditions have improved and revenue collections are meeting projections, the recovery has been painfully slow. According to a recent report from Standard & Poor's, the U.S. annual growth rate has averaged just 2.3 percent over the past four years, which is half the historic average annual growth over the past 50 years.[1]

> This report is based on data collected in the fall of 2013 from legislative fiscal officers in all 50 states and the District of Columbia. It includes information on:
>
> - State revenue performance;
> - Areas of spending over budget; and
> - A summary of state fiscal situations.

These economic doldrums have led to modest state revenue recovery in most areas of the country. This situation—and expectations for more of the same—has important implications for state finances. Although budget gaps are rare and policymakers may have some added flexibility to deal with spending overruns or other unexpected developments, there appears to be little room for major new policy initiatives.

Overall, state budgets appear to be stabilizing and settling into a period of modest growth.

FY 2014 Revenue Performance

To date, revenue collections have met or exceeded expectations in most states. Nearly all states are optimistic that they will meet their revenue targets for the rest of the fiscal year.

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[1] *Economic Research: U.S. Economic Forecast: Two Economies Diverged In A Wood.* Standard & Poor's. Dec. 5, 2013.

[2] Performance information for all tax categories in Nebraska is not available because the forecast

Through October in most states, personal income tax collections were relatively strong, with only a handful of states missing their targets. Both sales and corporate income taxes showed more volatility—about a dozen or states failed to hit their projections for these taxes. The real test for sales tax collections, however, will occur in December after officials can assess the strength of holiday sales.

Thirty-seven states and the District of Columbia levy all of the "big 3" taxes (personal income, general sales and corporate income). Of these, four states—Massachusetts, North Dakota, Pennsylvania and Wisconsin—reported higher-than-expected collections for all three categories. Only West Virginia reported collections below estimate for all three taxes. Officials there reported that collections through October were $42 million below forecast, largely due to weakness in the personal income tax. Other notable revenue developments include the strong performance of real estate transfer taxes, signaling a continued rebound in the housing market.

The rest of this section provides a snapshot of recent performance for state personal income, sales, and corporate income taxes. Information on the performance of other taxes is included for those states that provided it.[2]

Revenue Outlook for the Remainder of FY 2014

Revenue performance is a key indicator of the state fiscal situation, so it is also important to get a sense of future revenue expectations. For the remainder of the fiscal year, the majority of state officials expect general fund revenues to meet the FY 2014 forecast. Only a handful of states anticipate that revenues will "likely exceed" or "unlikely meet" their projected targets by the end of FY 2014.

- Thirty-eight states and the District of Columbia reported that revenues are expected to meet FY 2014 revenue estimates.
- Fiscal directors in eight states indicated that revenues are likely to exceed projections.
- Revenues are unlikely to meet their forecasts in four states—Alaska, Indiana, Tennessee and West Virginia.

Table 7 provides further details on state general fund revenue outlooks for the remainder of the fiscal year.

Personal Income Taxes

Personal income tax collections account for nearly 34 percent of state own-source revenues. Nine states do not levy a broad-based personal income tax, though two of these states--New Hampshire and Tennessee—do tax interest income and dividends.

- Sixteen states reported that personal income tax collections exceeded the latest estimate. Four of these states (Arizona, Maine, Maryland and Utah) saw collections surpass an estimate that had been revised upward. In Arizona, personal income tax collections through October were 7.2 percent above prior year collections.

[2] Performance information for all tax categories in Nebraska is not available because the forecast recently was revised. Performance information for the corporate income tax in Illinois is not available.

- Eighteen states and the District of Columbia saw personal income tax collections come in on target (see Figure 1). California, Oregon, Rhode Island, South Carolina and the District of Columbia had raised their estimates while Idaho had reduced its forecast.

- Georgia, Indiana, Mississippi, Missouri, New Jersey and West Virginia reported personal income tax revenues below the latest target. Officials in New Jersey noted that high refund payments are holding down net growth.

Table 1 contains more information on personal income tax performance.

Figure 1. State Performance of Major Taxes, Personal Income

Source: NCSL Survey of Legislative Fiscal Offices, fall 2013.

General Sales Taxes

General sales and use taxes represent about 32 percent of state own-source revenues. Five states—Alaska, Delaware, Montana, New Hampshire and Oregon—do not levy a state sales tax.

- Eleven states reported sales tax collections coming in over the latest estimate (see Figure 2). In Florida, preliminary collections through October exceeded a forecast that was revised upward in August.

- Twenty-one states and the District of Columbia reported sales tax revenue coming in on target. However, seven of those states (California, Connecticut, Illinois, Kansas, Rhode Island, South Carolina and Washington) were meeting targets that had been raised. Four states—Arkansas, Minnesota, Utah and Wyoming—and the District of Columbia were meeting targets that had been reduced.

Figure 2. State Performance of Major Taxes, General Sales

Source: NCSL Survey of Legislative Fiscal Offices, fall 2013.

- In 12 states, sales tax revenues were failing to meet forecasts. In Georgia, the sales tax was 7.2 percent below target and in Idaho collections were $6 million lower than forecast.

Table 2 contains more information on general sales tax performance.

Corporate Income Taxes

On average, corporate income taxes account for about 5 percent of state own-source revenues. Alaska, Delaware and New Hampshire, however, depend on them for more than 10 percent of collections. Six states—Nevada, Ohio, South Dakota, Texas, Washington and Wyoming—do not levy a traditional corporate income tax.

- Fourteen states reported corporate income tax receipts above estimates (see Figure 3). This includes Arkansas that had raised its forecast. Hawaii and Idaho saw revenues coming in over a lower estimate. Officials in Missouri noted that while the collections were above estimate, the corporate income tax is a highly volatile source of revenue.
- Fifteen states and the District of Columbia reported collections coming in on target. Of these, California, Connecticut, Minnesota, Oregon, South Carolina Utah and the District of Columbia had raised the forecast, while no state lowered the forecast.

Figure 3. State Performance of Major Taxes, Corporate Income

Source: NCSL Survey of Legislative Fiscal Offices, fall 2013.

- Corporate tax receipts were coming in below expectations in 13 states. The forecast had been revised up in Arizona and down in Maine and Maryland. In Maine, officials note that the downward revision was modest.

Table 3 contains more information on corporate income tax performance.

Other Taxes

States also rely on a variety of other taxes. These include taxes on oil and gas production, real estate transfers, tobacco, meals and rooms, insurance premiums, gambling, estates and others.

- Six states reported severance taxes performing above estimate. Eight states saw severance taxes coming in on target, and five states reported severance taxes below the latest forecast.
- Real estate transfer tax collections were on target for 17 states and the District of Columbia. Five states—Florida, New Hampshire, Pennsylvania, Virginia and Wisconsin—reported real estate transfer tax revenue above the latest target.

Only two states—New Jersey and Tennessee—reported real estate transfer taxes below the projected amount.

- Miscellaneous taxes were performing above estimate in four states. Another four states and the District of Columbia reported them coming in on target, and nine states reported miscellaneous taxes on items such as tobacco, gaming, inheritance and estates were coming in below estimates.

Tables 4, 5 and 6 contain more information on these other taxes.

Areas of Spending Over Budget

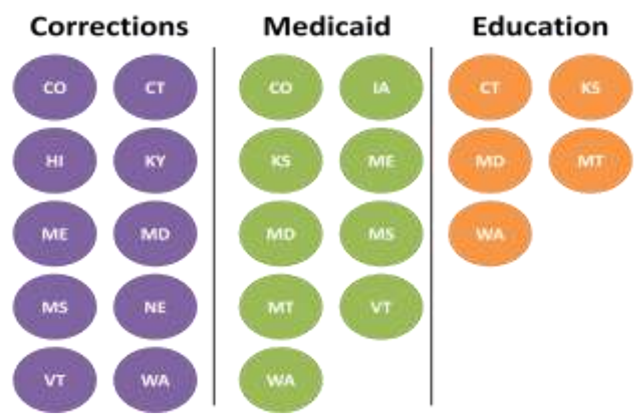
Seventeen states reported that at least one category of spending is significantly over budget for FY 2014. Some examples of areas over budget include:

- Ten states indicated corrections budgets are overspent through the first four months of FY 2014 (see Figure 4). In Colorado and Kentucky, higher than forecasted inmate populations are driving the overages. In Nebraska, inmate medical expenses and other per diem expenses may be higher than budgeted.

- Nine states reported that Medicaid is over budget. In Kansas, Maryland and Vermont, overspending is due to higher than anticipated caseloads. The Mississippi Division of Medicaid anticipates a deficit of $77.2 million.

- Five states noted that education spending was over budget. K-12 spending was exceeding budgeted levels in Connecticut, Kansas, Maryland and Montana. Kansas reported that school finance estimates were revised up by $31.8 million, or 1.3 percent in November. Maryland, as well as Washington, also reported overages in higher education spending.

Figure 4. Areas of Spending Over Budget in FY 2014



Source: NCSL survey of legislative fiscal offices, fall 2013.

- Other programs over budget include social services programs in Maryland, Vermont and Wisconsin; public defender systems in Maryland and Massachusetts; and emergency funds in Colorado as a result of recent flooding.

Table 8 contains more information on areas of spending over budget.

Summary of the State Fiscal Situation

More than two-thirds of legislative fiscal directors described their state fiscal situation as stable. Common terms were “stable with slow growth” and “moderately positive.” Some respondents used more upbeat descriptions such as “strong” and “exceeding projections.” At the same time, a few others described their situations as “weak” or noted a “structural shortfall.” Here are examples of state responses:

- California officials remarked that the state’s budget situation is stronger now than at any point in the last decade.
- Nebraska officials stated that the general fund budget appears to be sustainable for the next two to three years.
- Officials in Colorado noted that while revenue collections are on target, financial uncertainty and federal fiscal policies continue to dampen any robust economic growth.
- Officials in Tennessee and Virginia reported weak revenue collections. In Virginia, this is in due in part to the impacts of sequestration.
- Officials in Arizona and Rhode Island stated that while current year budgets are balanced, out-year structural shortfalls are expected.

Table 9 provides summary information on the current state fiscal situation.

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