

**GEORGIA STATE SENATE
BUDGET AND EVALUATION OFFICE**

Chairman's Column

December 18, 2009

Basic Budget Math

In the news, we all hear about the gravity of the state budget situation, a brief review of the basic budget math illustrates why budget writers are so concerned.

Fiscal Year (FY) 2010 Revenue Situation

November revenues put the state -15.4% below FY09 revenues year to date, while the executive revenue estimate reported in recent state bond documents is -6.2%. We do expect some "recovery" in the coming months simply because we measure revenues over the prior year, and the state did not fully feel the impact of the downturn until January of 2009. However, the Governor's revised revenue estimate assumes that the state will bring in the same amount or increased revenues over comparable FY09 revenues in the coming months. This is possible but risky given the fact that state reserves are depleted. The current estimate would mean a FY10 shortfall of \$1.26 billion. Or, the state has budgeted \$1.26 billion more than we expect to raise in taxes and fees.

Fiscal Year (FY) 2011 Revenue Situation

Currently, the bond documents suggest that the Governor is expecting 3.9% growth in FY11 over the FY10 revenues, a percentage that seems a little high given that most economists are expecting a slow recovery. If we follow Georgia State's forecaster, Dr. Rajiv Daiwan, we would project around 2% growth, which means around \$300 million in new revenues in FY11.

Shortfalls

One way of thinking about our budget is that in FY09, we based our budget on \$20.1 billion in tax and fee revenues. In FY10, the Governor is estimating we will bring in around \$15.7 billion in tax and fee revenues. This is a \$4.4 billion drop or 22%. However, because of stimulus and reserves, we are spending around \$2 billion more than what our tax revenues can support. Over FY11 and FY12, these one-time funds will be phased out at a rate of roughly \$900 million to \$1 billion a year.

In FY11, the net effect of losing \$900 million in reserves and stimulus less \$300 million in growth means that the state will need to find \$600 million in additional cuts on top of the \$1.26 billion in cuts in FY10 or the state will face at least a \$1.8 billion hole in the budget. Because the state also used one-time funds to balance the budget, the reduction will actually be closer to \$2 billion.

Table 1: Revenue Estimates for FY10 and FY11

	FY10 Budget As Passed	FY10 Amended (Current Rev Est)	FY11 General (2% Growth)
State Tax and Fee Revenues	\$16.99 billion	\$15.73 billion	\$16.05 billion
Reserves	\$.324 billion	\$.324 billion	
Tobacco Reserves	\$.151 billion	\$.151 billion	
Regular Tobacco Funds	\$.159 billion	\$.159 billion	\$.159 billion
Lottery Funds	\$.938 billion	\$.938 billion	\$.938 billion
Stimulus	\$1.4 billion	\$1.4 billion	\$1 billion
TOTAL Spending	\$19.96 billion	\$18.7 billion	\$18.1 billion
Difference from FY10 As Passed		-1.26 billion	-\$1.8 billion

Balancing the Budget - FY2010 & 2011

As reported in earlier columns, in July, the Governor identified around \$900 million in reductions and reserves in FY10 and has been withholding agency allotments accordingly. If the current revenue estimate holds, the Governor's January budget proposal will need to identify around \$360 million in additional reductions, reserves, or one-time funds.

The FY11 budget will prove trickier. Not only are more cuts required, but the state typically budgets for growth in the K-12 and higher education funding formulas, as well as growth in Medicaid. This year, the state also needs to budget additional funds for its mental health system. The net impact will be around \$450-\$500 million in additional demand for funding.

When looking at how to cut the budget, there are several different ways to categorize spending. The following is one way of looking at the budget:

Starting with the \$19.96 billion in the table above (which includes stimulus), first subtract off all funds that either cannot be cut, or are so restricted that they cannot be moved to cover shortfalls in any other part of the budget. Funds that are restricted include Lottery funds, Motor Fuel, and Debt Service. Once these are subtracted out, \$17.2 billion remains. Assuming the Governor does not cut Behavioral Health, this reduces the funding that can be cut to \$16.5 billion. Just looking at the \$16.5 billion, of this amount around 48% or half is K-12 education, and of this, approximately 80% is teacher salaries. Approximately, 16% is Medicaid, 13% is the University System of Georgia, and 6% is the state correctional system.

Eighty-four percent of the state budget that is available to be cut to balance the budget, then, is made up of four agencies. The remaining 16% spans every other agency from all the state's public safety agencies, parks, natural resources, the courts, to the General Assembly and Governor's Office.

In the FY09 and FY10 initial rounds of budget cuts, the state protected the larger agencies, such as K-12 and Medicaid. Each of these agencies' budgets actually grew slightly from FY08 to FY10, while the

16% of "all other agencies" in total were cut around 10-12%. Although we continue to try to protect K-12 and Medicaid, if we have to cut more, we cannot hold them harmless.

The state may be helped by stimulus funding. The U.S. House recently passed legislation assisting states by extending fiscal assistance through the Medicaid program. Initial estimates suggest this funding could help the state cover \$400 million of its FY11 shortfall.

There are difficult decisions ahead, but opportunities as well. It will take creative, out of the box thinking from the leadership of this state to navigate the crisis.