



Four State Budget Plans Show Disparate Fiscal Pictures

Patricia L. Billen and Brian T. Stenson

Nelson A. Rockefeller Institute of Government

March 2006

This is the third in a series of reviews of fiscal year 2006-07 budget proposals advanced by the governors of major states. The Rockefeller Institute previously released summaries of the executive budgets in Arizona, California, Connecticut, Maryland, Massachusetts, and New York. Themes across these early submittals include strong revenue growth, tax reductions, and, to a certain extent, education funding and replenishing budget reserves.

This brief describes the recommendations advanced by governors Bush (R-Florida), Blagojevich (D-Illinois), Granholm (D-Michigan), and Rendell (D-Pennsylvania). All are running for re-election in November 2006 with the exception of Governor Bush, who has reached Florida's gubernatorial term limit. These four budget proposals represent disparate states — some with surging revenue and new money and some still struggling with stagnant revenue growth and structural deficits. As a result, the governors' budget recommendations show marked differences in the extent to which they advance costly initiatives.

Florida

Governor Bush released his fiscal year 2006-07 executive budget recommendation February 1. The proposal totals over \$70 billion, reflecting a 4.4 percent increase compared to 2005-06, with an operating budget of approximately \$56 billion and over \$14 billion in capital outlays.

Overall Structure: Florida's state constitution prohibits the enactment of a personal income tax, making it one of nine states without this broad-based revenue source. Approximately three-quarters of Florida's General Revenue is from the sales tax, and the corporate income tax accounts for another nine percent. After adjusting for proposed changes, revenue from these taxes is expected to grow 2.83 percent and 2.85 percent, respectively, in 2006-07.

The governor's budget assumes \$5.8 billion in General Revenue funds above the fiscal year 2005-06 continuing spending base; \$4.1 billion of this additional revenue is nonrecurring. This "new" money will be used to increase the state's reserves as well as fund tax cuts and tax relief; education; hurricane preparedness and recovery; health and human services; public safety; land acquisition; and Everglades restoration.

Tax Reductions: The proposed tax relief is expected to reduce 2006-07 General Revenue by approximately \$342 million. These measures include eliminating the state's intangibles tax on savings and investments; sales tax holidays for back-to-school and hurricane preparedness spending; sales tax exemptions for machinery and equipment used for manufacturing, research and development, and space and defense activities; repealing the state's "by-the-drink" tax; and various sales tax exemptions and corporate income tax credits to encourage development and the use of alternative energy sources.

Education: The budget would provide \$17.7 billion for the Florida Education Finance Program (FEFP), the state's public K-12 education formula. This includes approximately \$9.96 billion in state funds, representing a 9.4 percent increase when compared to 2005-06, and approximately \$7.7 billion in local funds, or an 8.3 percent increase. The proposal assumes an increase of 47,995 in full-time equivalent students (1.8 percent), and provides an additional \$348 in funding per student.

The governor's budget recommends \$1.7 billion for Florida's community colleges, which includes \$1.2 billion in state appropriations (up 8 percent from 2005-06), and \$497 million in student fees (a 5 percent increase.) It also provides \$3.4 billion for Florida's universities including \$2.3 billion in state appropriations, reflecting a 2 percent increase from 2005-06, and \$972 million in student fees (a 10 percent increase). The increase in student fees is derived from tuition increases — 5 percent for in-state undergraduate students and 7.5 percent for out-of-state, graduate, and professional students — and higher enrollments. However, the governor's 2006-07 supplemental budget released March 2 recommends an additional \$26.4 million to scale back the proposed tuition increases from 5 percent to 3 percent for undergraduate students and from 7.5 percent to 5 percent for out-of-state, graduate, and professional students.

Medicaid: Proposed All Funds spending for Medicaid totals \$15.9 billion, an \$845 million, or 5.6 percent, increase from 2005-06. This includes approximately \$5 billion in General Fund revenue, reflecting an increase of \$560 million, or approximately 12 percent. The governor's March 2 supplemental 2006-07 budget also includes \$124.8 million for Medicaid rate increases for healthcare providers.

The governor's proposal assumes \$26 million in cost savings in Medicaid fee for services categories. This is equal to the infrastructure costs associated with Florida's Medicaid reform effort that the state will begin implementing in two counties in the upcoming fiscal year. Florida's reform plan was approved by the federal Centers for Medicare and Medicaid Services in October 2005 and is scheduled to be operational statewide by 2011. Major elements of the plan include premiums that Medicaid enrollees will access to

choose a managed care plan; enhanced benefits accounts that enrollees will earn through healthy behaviors to purchase noncovered healthcare related items; and the option for enrollees to use their Medicaid premium to purchase employer-sponsored insurance.

Information on the Florida Executive Budget is available online at www.ebudget.state.fl.us.

Illinois

Governor Blagojevich released his fiscal year 2006-07 executive budget recommendation on February 15. The proposal totals \$45.4 billion in operating appropriations, reflecting a \$2.1 billion, or 4.9 percent, increase when compared to fiscal year 2005-06. Of this total, \$25.7 billion, or 57 percent, is from the state's General Fund.

Overall Structure: Improving revenue trends are helping Illinois battle its way out of structural deficit — 2006-07 is the first year in four years that the state's base revenue should fund all spending. The governor's proposal assumes that revenue from individual and corporate income taxes (50 percent of the General Fund) and sales tax (34 percent of the General Fund) will grow 6.5 percent and 4.7 percent, respectively, when compared to current year estimates.

The 2006-07 executive budget reflects the governor's continued efforts to rein in the Illinois pension system, one of the state's "structural deficit-drivers." Previous efforts to reform the pension system included issuing bonds to reduce pension debt, capping state participation in end-of-career pay increases, eliminating lump sum awards for unearned sick leave, and identifying a funding source for new benefits, among others. The executive budget recommends earmarking one-time proceeds from the sale of a riverboat gaming license and recurring proceeds from the sales of surplus state-owned property for the pension system.

Cost containment measures continue for Medicaid, another program the governor has identified as a deficit driver. These measures include implementing new systems for statewide primary care case management and disease control, and interagency collaboration to maximize federal revenue.

Tax Changes: Several revenue enhancements have been recommended to support increased funding for K-12 education, including completing the phase-out of a tax credit for landfill-generated electricity, broadening the environmental impact tax base, and increasing the tax on noncigarette tobacco, among others. It also includes a \$1,000 tax credit for higher education tuition.

Education: The governor's budget recommends \$6.5 billion in General Fund support for the state's 800 school districts, reflecting a \$429 million, or 7 percent, increase from the previous year's enacted budget. New funding of \$400 million would be programmed at a later date in conjunction with the state's General Assembly for efforts such as increasing

general state aid for education; funding early childhood/preschool education; reducing class size; funding state mandated services; and other initiatives.

Information on the Illinois Executive Budget is available online at www.state.il.us/budget/FY07%20Budget%20Book.pdf.

Michigan

Governor Granholm released her fiscal year 2006-07 executive budget recommendation in early February. The \$42.6 billion proposal reflects a \$1.1 billion, or 2.5 percent, increase in spending when compared to current law. Over 65 percent of estimated revenue is from state sources with the majority from the General Fund/General Purpose (\$9 billion) and the State Education Fund (\$13 billion).

Overall Structure: Michigan continues to be plagued by a structural budget deficit. State officials attribute this situation largely to the inability of General Fund/General Purpose revenue growth to recover ground it lost during the period 1999-2000 through 2003-04. The governor's budget assumes a funding gap of approximately \$408 million, down from \$1.9 billion in the 2003-04 budget. The gap reflects General Fund net revenue growth of \$60 million and baseline spending increases of \$468 million. Over 61 percent of the spending increase is attributable to increasing Medicaid costs, supporting programs previously funded by federal Temporary Assistance to Needy Families (TANF) reserves, and increasing pension costs, as well as costs associated with retiree health benefits. The governor proposes to close the shortfall and support enhanced funding for select efforts with spending reductions, modifications to select tax expenditures (discussed below), increased liquor license fees, funding shifts, prior year available revenue, and Medicaid provider taxes.

Tax Changes: The executive budget recommends eliminating or modifying the following tax exemptions to generate revenue: international and some interstate communications; interstate truck and trailer exemption; tax liabilities of professional employee organizations and other employee leasing arrangements; collection of taxes from a single enterprise (affiliate nexus); gains and losses attributable to a business entity not taxable in Michigan; calculation of tax on inherited assets; penalties for delinquent taxes; insurance company out-of-state purchases; oil and gas double deductions; "flow-through" entity deductions; income limits for limited liability companies filing as a corporation; tax relief for small businesses owned by a similar business without ties to Michigan; commercial rental property taxation; sales in prison stores; and driver education vehicle purchases.

Education: The governor's 2006-07 budget proposes \$13.1 billion in school aid, reflecting a \$362 million, or 2.8 percent, increase compared to current law. The bulk of Michigan's K-12 funding is supported by the state's School Aid Fund. Over 75 percent of the fund's revenue comes from sales, use, income, and state education taxes.

The fund is projected to total approximately \$13 billion for fiscal year 2006-07, an increase of \$305 million, or 2.4 percent, compared to 2005-06.

Information on the Michigan Executive Budget is available online at www.michigan.gov/budget/0,1607,7-157-11460---,00.html.

Pennsylvania

Governor Rendell released his fiscal year 2006-07 executive budget recommendation on February 8. The proposal includes a \$54.2 billion operating budget, with \$25.4 billion, or 47 percent, from the state's General Fund.

Overall Structure: Current year tax collections are expected to exceed estimates certified at the beginning of fiscal year 2005-06 by \$381 million, or 1.5 percent. Newly projected increases in personal and corporate income tax collections make up \$297 million of this unanticipated revenue. The governor's executive proposal assumes the state will end the 2005-06 fiscal year with a \$204 million General Fund surplus and General Fund revenue will grow 3.9 percent in fiscal year 2006-07, with increases in personal income and consumption tax collections leading the way. The governor's budget recommendation includes a \$924 million, or 3.8 percent, increase in General Fund expenditures, including statutory transfers to the state's rainy day fund.

Tax Reductions: Proposed tax reductions total approximately \$221 million, and include an accelerated reduction in Pennsylvania's Capital Stock and Franchise Tax, an increase in the Research and Development Tax Credit, and an increase in the annual cap on deductions for Net Operating Loss Carry-Forward.

Education: The governor's 2006-07 budget proposal recommends \$8.6 billion in General Fund support for Pennsylvania's basic education program, the state's pre-K-12 education system. This reflects a \$517 million, or 6.4 percent, increase compared to the previous fiscal year, and assumes a small decline in enrollment (10,320, or less than 1 percent). Proposed adjustments include a \$225 million increase in basic education funding — reflecting a 5 percent increase in basic education funds to school districts and increased support to select school districts to increase their spending toward the statewide foundation level and a \$114 million increase to support the employer's portion of school employee's retirement, bringing the state's total payment to \$369 million.

Additionally, a \$47 million, or 3.2 percent, increase in General Fund support is recommended for Pennsylvania's higher education institutions including the State System of Higher Education (SSHE); state-related universities; community colleges; and private colleges and universities. Proposed increases include \$18 million for SSHE and \$23 million for state-related universities including Pennsylvania State University, the University of Pittsburgh, Temple University, and Lincoln University.

Health Care: Proposed Medical Assistance funding for 2006-07 includes \$4.9 billion from the General Fund, reflecting a \$109 million, or 2.3 percent, increase compared to 2005-06. Recommended adjustments to the 2005-06 funding level include a \$145 million increase for changes in caseload and utilization (the budget proposal assumes a 2.7 percent increase in monthly average participants); a \$184 million increase in payments to the federal government for the Medicare drug program (bringing the state's total payment to \$348 million); and \$227 million in savings from the federal Medicare Part D pharmacy benefit. The governor's proposal also includes program efficiency and integrity initiatives expected to generate approximately \$126 million in savings. These initiatives include selective contracting; increasing efforts to identify third-party coverage; and measures to address fraud, abuse, and waste.

Information on the Pennsylvania Executive Budget is available online at www.governor.state.pa.us/governor/cwp/view.asp?a=1101&q=445371.