2011 State Budget Forecast

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Web Seminar
Abridged Transcript

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Introduction

Eric: Hello everyone, I'm Eric Giles, NASAA's learning services manager, and it's my pleasure to welcome you to today's web seminar. I'm glad that you could tune in for this session on fiscal forecasts and how state budget conditions will affect the arts in the years ahead.

NASAA's web seminars always draw many state arts agency staff and council members, so welcome back to all of you who have been taking advantage of our virtual learning services over the last year.

We also have some special guests logged in today. NASAA invited all of the statewide arts advocacy groups across the country to join us for this session. I want to extend a special welcome to all of you advocates and to thank you for your hard work. Citizen advocacy has made a critical difference for the arts during this recession, so I commend all of you who have been working overtime to make the case.

I also want to thank the National Conference of State Legislatures for participating in this session. We've enjoyed a long and fruitful relationship with NCSL, and are grateful that they will be sharing their latest research with us.

I'll now pass the conductor's baton to Sue Struve, NASAA's communications manager, who will be the moderator for today's session.

Sue: Thanks, Eric, and thank you for joining, everyone. I see that we have a good crowd on-line today. We all know from daily headlines that America's economy continues to be in turmoil. The recession hit state budgets particularly hard, causing some of the biggest state revenue gaps in history.

How bad is it? How long will it last? And how is it affecting the arts? Many people are asking these kinds of questions of state arts agencies and state advocacy groups as well. The next 60 minutes will help answer these questions and give you a sense of what is in store for the arts in the year ahead.

Before we turn it over to our first presenter, Todd Haggerty from the National Conference of State Legislatures (NCSL), I wanted to extend a special thanks to him. As many of you know, NASAA and NCSL have a long history of collaboration. We share information, have
had NCSL members on our board and have collaborated on joint research together in the past. So, many thanks to Todd and his colleagues at NCSL, who have continued the tradition of collaboration with this seminar.

We are extra grateful for Todd, because NCSL’s largest gathering of the year just occurred this past week and he managed to make time on his calendar to share his latest research while it is still hot off the press.

**State Fiscal Conditions in 2011**

**Todd:** Thank you very much. This is a great opportunity for us to share some brand-new information that, as Sue mentioned, was just released this past Tuesday. Hopefully, this information will give you a little bit more insight into what states can look forward to in FY2011 and looking ahead possibly to fiscal years 2012 and 2013. NCSL regularly surveys legislative fiscal directors and uses this information to compile 50 state reports on the fiscal situation.

So, let's go over some of the points that have come out of this most recent survey. I am going to provide a bit of good news today; usually when I give these presentations all I get to deliver is the bad. Although revenue challenges are going to remain with states for awhile, there has been a slight uptick lately in state revenue collections. This has many people saying that they have finally hit rock bottom and are starting to turn the corner.

Despite this good news, states are continuing to face sizable budget gaps into the near future. To put this into context, states have reported an estimated total budget gap through 2013 in excess of $500 billion, a truly staggering figure.
This chart, courtesy of the National Bureau of Economic Research, the official body determining recessionary periods, illustrates the difficult time that states are facing. Measuring the number of months, this chart shows the length of economic downturns, and as you can see at 21 months, this recession stands as the longest downturn since the Great Depression. Now, many economists have forecast that this recession in fact ended in the second quarter of 2009, but there has not been any official word on this. The fact remains that it has continued to put really tough pressures on state budgets as we look ahead.

Here, the line shows year-end balances while the gray bars show recessionary periods. The year-end balances are measured as a percentage of general fund budgets—what is left over compared to how much the state is spending. These are an important indicator of fiscal conditions. Budget pressures reduced year-end balances in most states, although legally required balances and rainy day funds have helped preserve them in some.

It is very difficult to evaluate these year-end balances since the onset of federal stimulus funds. We are aware that these balances would have fallen even further without the onset of these funds. Further complicating the matter have been Florida and Texas, which have rather large reserve funds from their oil revenues—and these account for half of their state revenue funds. If you were to exclude these states from the year-end balances, it would stand just around 1.8% for FY2011, a pretty significant drop.

The main factor has been the performance of revenues. The recession has really battered state revenues. In November when we surveyed fiscal officers, we asked them how FY2010 revenues looked in comparison to FY2009 collections. As I mentioned, FY2009 was in the middle of the recessionary period which carried on into 2010. Despite the recession beginning earlier, 2010 was one of the worst years and will not be
remembered fondly by state officials. As you can see, 40 states were projecting that their FY2010 revenues would be lower than their 2009 collections. We are still waiting for official data stating that this was indeed the case, but as you can see, state revenues continued to plummet in FY2010. It is important to note that states enacted tax increases of $28.6 billion. In 24 of these states, taxes were increased by more than 1%. These effects are included in this forecast, just to show how far revenues plummeted.

These next two slides will show the components of state revenue, personal income tax and general sales tax, as compared to the forecast. These are important because they account for two out of every three state general fund dollars. For personal income tax, as you can see on this chart, 20 states are still coming in below forecast through May for collections. This is still a very high number of states that are performing below estimate. It is actually an increase from our previous surveys; in March, over 25 states had reported that they were coming in below estimate, and in November over 30. You can also see that 14 states are on target and 5 above, also an increase from previous surveys.

Looking at sales tax collections, the news gets a little bit better, with 28 states either on target or above target. Thirteen states are still below target. But this does show that there has been some renewed consumer confidence and consumers are out making additional purchases.
If we look ahead, this apparent increase in consumer confidence has many states in 2011 expecting their revenue to get better. Forty-two states, shown here in dark green, are expecting their revenues to be better than they were in 2010. While this is good news, it must be tempered by the fact that revenues fell so far in 2009 and 2010. Many states are saying that they have hit rock bottom and are seeing a slight rebound, but these are modest increases for a majority of states. Any blip in the economy or mistimed forecast could put these states out of balance. But it goes to show that many states are seeing FY2011 as the beginning of climbing out of the recession.

Because revenues fell so far, when can they return to their former peak? FY2008 represented the peak for many states, but because of the steep drop-off through 2010, it will take quite a while to approach that peak again. As you can see, a majority of states are looking at FY2012 or beyond before they can return to that peak. Additionally, you may notice that it is not even on the current forecast horizon for 19 states. That means that either they do not have a long-term forecast to predict when it will return or it is beyond 2015. So, while things are beginning to improve, it is going to be slow.

Here we see the manifestation of what the loss of state revenues cost, especially as states crafted their FY2011 budgets. Forty-one states addressed budget gaps while crafting their FY2011 budgets; 24 of these states closed gaps in excess of 10% of the general fund budgets. Cumulatively, this totaled an $83 billion gap that states had to address. This is coming on the heels of fiscal years 2009 and 2010, where states closed gaps of $117 billion and $174 billion, respectively. This does not take into account any unresolved budget gaps that states already have looming as we are now only just about a month into FY2011.
This chart shows budget gaps in cumulative total by year for the last 10 years, including the last two recessionary periods that have had an impact on state budgets. In 2001, there was an eight-month-long recession, and you can see that it took states until FY2006 to fully recover—with budget gap amounts that we thought, at the time, were extreme and unheard of. There was a brief respite in FY2007, and then the beginning of this recession in FY2008. This current recession, as we can see, has produced some jaw dropping numbers, such as the $117 billion in 2009 and the $174 billion in 2010. Looking forward, we even have states forecast budget gaps as far as 2012 and 2013.

Revenues have been a key driver in state budget gaps, with the recession putting enormous pressure on state finances. However, this has now been coupled with spending pressures in programs like Medicaid, which have been driving up gaps in FY2011. Fiscal years 2012 and 2013 are being compounded by the absence of federal stimulus funds. States are not predicting the return of peak revenue funds prior to federal stimulus funds running out, thus creating a very difficult situation for lawmakers looking ahead.

As we all know, states are bound by budget balance requirements, meaning that they must try anything and everything to bring those budgets into balance. As I mentioned, in FY2010 many states enacted tax changes generating $28 billion. There are other revenue increases, like fees, that states have looked at as well. In addition, there were federal stimulus funds, which state lawmakers have told us prevented possibly more severe budget gaps and cuts. States also used a wide array of other actions, like tapping rainy day funds, fund sweeps and transferring funds from other programs. Behind all of this we have also seen states looking at streamlining and government efficiency.
Let's take a look at spending cuts in just a little more detail. On our latest survey, we had a list of actions that states had used to bring their budgets into balance. We then asked them to list the percentage that each action accounted for. Most states used spending cuts to bring their budgets into balance—at least 33 as shown on this map—although we did not have final data from 4 states. You can see they range from Maryland, where spending cuts accounted for 9% of the solution, to New Jersey, where spending cuts accounted for 93% of the budget gap closing solution. If you look at FY2010 and into FY2011, spending cuts have been one of the primary ways that states have brought their budgets into balance.

Last year, states enacted tax increases generating $28 billion that went in to effect in FY2010. While this was the largest tax increase dollarwise in some time, as a percent of total tax collection it was actually less than in 1991, when states enacted tax increases of 5.4%. Despite that, this was definitely a tool that was used strongly by most states. Now, looking at our preliminary information, states have only enacted tax changes worth $3 billion. This has been compounded by the election year coming up, with many officials not wanting to go down the tax route, especially with a large increase last year. So while tax increases are still being used, it is definitely not being done in the way that it was last year. Additionally, California and New York were the primary drivers last year with their tax changes, which accounted for a vast majority of those in 2010.

Let's talk about some of the concerns states have looking ahead. One of the main things that states will have to face in the foreseeable future is finding a replacement for these federal stimulus funds. As I mentioned previously, the budget gaps in fiscal years 2012 and 2013 are being driven primarily by the absence of these funds. Unfortunately, revenues are not expected to rebound in
time to replace these funds, which have had a tremendous impact. This is definitely presenting a challenge and raising the feasibility of further state budget cuts. As you know, states have been looking at 5% or 10% or even 15% across-the-board cuts, which have had significant impacts. With states now entering their third, fourth or fifth year of these entrenched budget gaps, they are facing the possibility of making more cuts or even possible program eliminations as well. States again have not raised taxes as much as they had in the previous year, so what is the possibility of raising more revenue? We have seen a continuation of some fee increases, but tax increases are definitely not as common as in the previous year.

Another significant issue that I haven't touched on, but that looms ahead for state budgets, is unfunded pension liabilities. The Pew Center on the States released a report a little while ago that was called \textit{The Trillion Dollar Gap}, noting that states have over a trillion dollars in unfunded pension liabilities. Many states, in response to the current economic downturn, have either delayed pension payments or borrowed against pension payments in order to bring their budgets into balance. This creates a significant problem as, moving ahead, states are going to have to make those payments. And what this shows us is that there is a deeper, more structural budget gap that needs to be addressed.

In conclusion, there is some good news. State revenues are starting to show some growth, albeit very modest. Also, if there is another blip in the economy or if the estimates are off, it could cause a rather large problem. Looking ahead, states are going to face budget gaps for at least another two years, and few states have plans to address the end of federal stimulus funds. These are some of the main issues that states will be grappling with as they look to balance their budgets.

**Q&A**

\textbf{Sue:} Thank you Todd, it looks like we have a number of questions in the queue. To start, you mentioned that there were a lot of tax increases enacted to address budget gaps. How were those states able to push those increases through? And then a piggy-back on to that, what other revenue increasing tactics are states looking at currently?

\textbf{Todd:} In many cases, the tax increases that were looked at in 2009 and went into effect in 2010 were those broad based taxes—personal income, sales and use. Those were, in general, aimed at high-income users, so that made them, in a way, more palatable to go through. In addition, states like Arizona and Oregon have put tax increases on the ballot and let the citizens decide between
budget cuts and the raising of taxes to maintain programs and funding levels. You have also seen an increase in use fees, where if the consumer is willing to pay the fee for that activity, they can increase the fees for extra cash flow without making a broad based tax increase.

**Sue:** We have another question from our queue. How are legislators making choices about cuts? What factors are taken into consideration when elected officials are making these choices?

**Todd:** Well, many things go into that. Requirements from federal stimulus funds in some ways can dictate what cuts can be made, for instance in K-12 and higher education. In other states it revolves around what political options are available in that state. Some states have gone as far as to identify what their priorities are to determine which areas are the last that they will make budget cuts to. So, states have used a broad range of methods to determine which programs and funds are going to be cut. And I'm sure that everyone out there can attest to this: there is not a one-size-fits-all solution to this issue. But those are some of the ways that states have gone about it.

**Sue:** Another participant has asked, What differences in impact are you seeing in different regions of the country?

**Todd:** That is one of the very interesting things we've seen from this recession. Really no one region or area has been unaffected by this recession. If you look at FY2010 48 of the states had budget gaps; it was only the really strong agricultural states and those with oil or gas that were relatively immune. And the responses that we saw, although every state had their own political things they had to address, for the most part it was this mixture of tax increases, budget cuts, federal stimulus funds and their rainy day funds that they used to bring their budgets into balance. There really was no difference between regions; the times called for a broad based number of actions.

**Sue:** The Florida Division of Cultural Affairs has a question for you, Todd. Are the states that have no income tax in worse shape than the ones that do?

**Todd:** That is an interesting question, because you can also have the inverse, where states that only have only sales tax and no income tax are worse off. You can look at Oregon and Washington, where despite their different taxing situations their budgets are really running in parallel with each other. So despite the fact that one has no sales tax and one no income tax, they are really about the same.

**Sue:** The Nebraska Arts Council has asked, Are you gathering any data that compares term-limited legislatures to legislatures that are not term limited?

**Todd:** No, we have not. But that is an interesting question that I will have to bring up to our elections folks here.

**Sue:** One last question. We know that you have been giving primarily the headlines here. If someone wants to learn more, or to access a report or summary, where could they find it?

**Todd:** Our report is found on the NCSL website under the issues tab ([http://www.ncsl.org/?TabId=20890](http://www.ncsl.org/?TabId=20890)). We also have a fantastic collection of tables on 13 different measures that states are taking to close their budget gaps ([http://www.ncsl.org/?tabid=19650](http://www.ncsl.org/?tabid=19650)).
And these provide a lot of detailed information, including specific examples and dollar amounts. If you combine those two documents, you will have a lot of information at your fingertips.

**Forecast for the Arts**

**Sue:** Thank you, Todd. The information you provided today really helps us understand the forces that are creating some of the difficulties that state arts agencies are facing during this recession.

Now, I would like to introduce Angela Han, NASAA’s director of research, who will bring us up to speed on what this means for the arts. NASAA tracks state arts agency budget information year-round, and Angela and her team recently completed a survey of their own to gauge what is happening with state arts agencies right now. So Angela, what’s the news?

**Angela:** You have just had a chance to learn what is going with state budgets overall. What I’d like to do over the next few minutes is zero in on what is going on with state arts budgets. I want to talk about what is going on now and then give a little historical context, that way you’ll get both a national and historical frame for what is going on in your state during this recession.

As you probably know, state arts agencies receive revenue from a variety of different sources. Today we are going to focus on one source, legislative appropriations, and that constitutes the bulk of state arts agency funding. In aggregate, appropriations constitute over 80% of SAA budgets. The information I am going to talk about today is based on the survey that Sue just mentioned. It is the survey that NASAA conducted in May and June of this year, where we asked SAAs to estimate their appropriations for FY2011. FY2011 actually began on July 1 for most states. Please bear in mind that the figures we are discussing today are preliminary and are subject to change as legislatures submit budgets throughout the year. Of course, we will survey agencies again in the fall, so make sure to look out for that survey.
Our first big-picture headline is that for FY2011, state and jurisdictional agencies are projected to be appropriated $268 million in funds from their legislatures. This is a decrease compared to last year—a 13% decline compared to 2010. As you can see by this graph, this is the third year in a row that appropriations have declined. If you compare it to 10 years ago, back in 2001, appropriations have declined 41%, and you can see that it hasn’t been a straight decline over those 10 years. I should also point out that 2001 was an all-time high in state arts appropriations, at $451 million.

While appropriations declined overall going into 2011, that was not the case in every state. Out of the 56 state and jurisdictional arts agencies, 15 responded that they are anticipating flat funding. The way we define flat funding is either no change or a change of less than one-half of one percent. Another 10 agencies are reporting that they are expecting a funding increase. In a number of those states increases represent a partial restoration of funding they lost in FY2010. Decreases were reported from 31 states, and that comes out to a little bit more than half of all state arts agencies. Compared to last year, the number of states receiving decreases is slightly smaller. In FY2010, the last time we surveyed, 37 states were reporting that they had received decreases. Also, the number of states expecting large cuts has decreased by over a third.

Geographically, neither increases nor decreases are concentrated in any one part of the country. As you can see, there is not a particular region that has been targeted.
Another way that we talk about arts appropriations is in per capita funding. Right now, national per capita funding stands at $0.86. And just a quick reminder about how we get that figure. We take total appropriations and divide it by the U.S. population. Compared to FY2010, this figure is a decrease of $0.13. The loss reflects not only a loss of funds and absolute dollars, but also a growing population. So, state arts agencies are being asked to extend their reach further with less public funding. Even though the national figure is $0.86, individual states vary pretty widely above and below this figure.

Most of you are aware that we do per capita figures for each state, and we do this the same way as the national number. We take the appropriations as reported by each state and divide it by their population for that year. What this map shows is which states are receiving above and below one dollar per capita in appropriations funding in FY2011. You can see that geographically speaking, higher per capita funding is slightly concentrated in the northeast.

When we report on per capita figures, we often talk about above or below a dollar. This year a lot of states have dropped below $.50 in per capita funding, so we wanted you to be aware of that going into FY2011. Actually, one-third of state arts agencies are reporting appropriations that work out to be less than $0.50 per person.
That is what we know about arts appropriations right now for FY2011. What I would like to do is switch gears a little bit now to discuss how the current funding situation compares to years past and give some historical context to what we are seeing. By far, the driver in state arts appropriations is overall state fiscal health, which is why it was important to hear from NCSL. As you heard Todd mention, this is the third year in a row that state budgets are being negatively affected by the recession. So it is little surprise that this is the third year in a row that arts appropriations have declined. This trend, where arts appropriations decline with overall state government, is actually one that we have seen before.

During the last recession, in the early 2000s, states also experienced fiscal distress, and between 2001 and 2004 arts appropriations also declined. You can see that the three-year decline from 2001 to 2004 was pretty significant: 38% of appropriations were lost during that period. That decline was even sharper than the one we have seen to date from 2008 to 2011. There was also a recession in the early 1990s where we saw arts appropriations decline at a similar rate, percentagewise, as we are seeing right now. I do want to point out a couple of differences between those two recessions and what we are experiencing right now. First, in both the 1990 and 2001 recessions, arts appropriations were at an all-time highs, and that was not the case in 2008. Also, as Todd mentioned, state budget gaps are expected to continue for the next few years, so the impact of this recession will be felt longer than those of the previous two.

All of the figures I have talked to you about so far have been in nominal dollars, exactly as they were reported to us when we asked. That does not take into account that inflation erodes the buying power of money over time. When you adjust for inflation, as we have done on this graph, over the last 25 years it looks a little bit different.
For example, I mentioned that arts appropriations have decreased 41% over the last 10 years; when you adjust for inflation, appropriations have actually declined by 51% over that same period. So, we’re at about half the funding level we were 10 years ago when we adjust for inflation.

Another aspect of appropriations is when we look at per capita funding. Again, when you look at inflation-adjusted dollars, the story is different. I mentioned that going into FY2011 we are looking at per capita funding of $0.86. When you adjust for inflation and look back over the last twenty-five years this is actually the lowest per capita funding during that period. In 1987 dollars it is $0.45, much, much lower than we have seen in years past.

Those are the major points that I wanted to make regarding appropriations headed into FY2011 as well as with regard to past recessions. Before we move on to Q&A, I wanted to leave you with a couple of final thoughts.

One, we’ve seen funding go through tough times in past recessions, but we have also seen upward trends when state government has recovered. In fact arts appropriations have always recovered.

I want to also remind you that legislators are finding ways to keep funding the arts, even if it is at reduced levels. We received surveys back from every single state and jurisdictional arts agency and every one said that they were receiving funding in FY2011. So, state legislators still value the arts and are looking to fund them.

Let me also remind you that advocacy makes a difference. Policymakers recognize the value and importance of the arts in and of themselves, as well as in terms of contributing to economic recovery, quality of life and education.
Q&A

Sue: Thank you, Angela. Here's our first question for you. Our state arts agency was nearly eliminated this past year. Is that happening all over the country?

Angela: Heading into FY2011 there were three state arts agencies that received elimination proposals at some point in their budget process. That is actually an improvement compared to 2010 when we saw six states that had elimination proposals as part of their budget process. That is not the norm. We still consider that to be too many. An important thing for you to say in your own state if this should come up is that elimination is an extreme tactic and no other state has accepted it. Don't let legislators think that elimination is standard operating procedure; it is not.

Sue: We have another question along the same lines: Are the arts being targeted for cuts?

Angela: We've been in pretty close contact with all our members since the recession began and in some places, yes, state arts agencies are being treated in a way that they feel is disproportionate to what is going on with other state agencies. But a large majority of the states have reported that their cuts are comparable in size to what's going on within state government. A lot of folks have told us that they are receiving the same across-the-board cuts that every other agency in state government has had to take. Other agencies have said that they are being treated similarly or maybe even protected a little bit compared to their peer agencies in their departments. And other agencies are being cut proportional to other agencies their budget size. So, it is much more the norm that state art agencies are being treated the same as their peers in state government and not being targeted.

Sue: I have a clarification question from Florida. Do the per capita figures include or exclude line items?

Angela: When I talked about legislative appropriations, we included line items in those dollar figures. Line items might be called earmarks or pass-through funds in your state. They are basically funds that pass through your state agencies but go to another entity through a different process than other agency funds. So all of our figures today include line items. But if you would like figures that exclude line items, we would be more than happy to get you those figures.

Sue: And another clarification question: Does the $268 million include NEA funds that are given to SAAs?

Angela: The $268 million only includes appropriations from state legislators, so it does not include other sources of funding that state arts agencies may receive, such as NEA funds or private funds or any other funds that don’t pass through the legislature.
Sue: Does NASAA collect information on regional arts organizations as well as state arts agencies?

Angela: We don't collect budget information from regional arts organizations. What we have available in terms of regionals is actually grant-making figures. And we experience about a year lag on those because of the nature of that reporting.

Sue: We have time for another question or two. We keep hearing from our legislature that there isn't enough money and that the arts just aren't as important as other services. Do you have any advice for that situation?

Angela: I want to comment from my perspective as a director of research. The size of funding that states make to the arts is not very large. On average, compared to general fund dollars, states spend 0.042% of the general fund on the arts. In other words, for every $1,000 spent in general fund dollars, less than $0.42 is spent on the arts. That is a really small percentage, so I am always fascinated when people make the argument that they need to balance their budget and that is why they are proposing to reduce or fully eliminate arts council funding. There is no way that eliminating an arts council will balance your budget, it is such a small amount of money. Also, the return on investment for those funds spent on the arts agencies is huge.

It is also important that you answer that question in a way that is tactical, rather than just fact based. You need to have influential spokespeople who can connect the arts to other things that are going on that are important to state policy—connecting them to the economy, to education, etcetera. There are a lot of advocacy tools that NASAA offers that I urge you all to consult, and, Sue, I believe you will mention them in just a minute, correct?

Sue: Yes. Angela, we have one last question. You have been talking about national trends, but if someone wants state-level statistics, where should they go for those?

Angela: First off, I'd like to say that if anyone participating today has a question about anything presented here, please feel free to contact us. We are always happy to put together information that is custom built for your state, so you are always welcome to contact us.

We also have information available on our website. On our funding page you can find the most recently available information that we have on state budgets. That will include all of the information that I discussed today. It is all available in the Legislative Appropriations Preview, the top link on our Funding page.
Sue: As you all know, NASAA offers a lot more than just numbers. For instance, check out the series of reports that NASAA helped the National Governors Association develop with the National Endowment for the Arts, *Arts and the Economy* being the most recent. These reports are a treasure trove of information on the economic impact of the arts. There is a new report in the pipeline due to be released in 2011, so keep an eye out.

NASAA also offers some applied advocacy tools to help make the case for arts funding. For instance, this spring we released *Why Should Government Support the Arts?* Check it out, because it gives answers to the top 10 questions that lawmakers most often ask about funding the arts when funds are scarce. All of these tools are located on the NASAA website.

Thank you all once again for participating and we hope to see you in Austin at Assembly 2010!