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Briefing Report to the Chairman, Committee on the Budget, House of Representatives

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BALANCED BUDGET REQUIREMENTS

State Experiences and Implications for the Federal Government

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The Honorable Martin Olav Sabo
Chairman, Committee on the Budget
House of Representatives

Dear Mr. Chairman:

This briefing report responds to your request for information on state balanced budget laws and practices. You asked that we provide current data on state balanced budget requirements, states' experience in meeting those requirements, and implications of that experience for federal efforts to balance the budget. This report updates and expands on our earlier work in this area.[1]

BACKGROUND

Since 1975, 32 states have passed resolutions calling for a convention to consider amending the U.S. Constitution to mandate a balanced federal budget.[2] Although resolutions from 34 states are needed to convene a constitutional convention, these actions have helped to propel the balanced budget amendment into public debate.

The Congress has also considered a federal balanced budget amendment on many occasions. Although all of these amendments were rejected, the issues they raise continue to attract attention as the nation considers how best to address the large and growing federal budget deficit.

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[1]In our earlier report, Budget Issues: State Balanced Budget Practices (GAO/AFMD-86-22BR, December 10, 1985), we documented the state balanced budget requirements in effect in 1985 and assessed the relevance of state experience to the federal government.

[2]Three of the 32 states have subsequently rescinded their resolutions; it is currently unclear whether the rescissions or the original resolutions hold force.

Because many states have balanced budget requirements, their budget experiences are seen as relevant to proposals for a federal balanced budget amendment. Proponents of a federal mandate have suggested that the state requirements have prompted serious and responsible state efforts to budget within resource constraints. Opponents have suggested, however, that many states are meeting the letter, not the spirit, of their requirements, focusing their efforts on only a portion of their operations, and often relying upon gimmickry to create the appearance that their budgets are balanced.

Supporters and opponents of the federal balanced budget amendment have also focused on several other key issues. Opponents question the economic effects of such requirements, pointing to the federal budget's role in pursuing national economic goals. According to these opponents, strict constraints would hamper the federal government's ability to respond to economic downturns and might, in fact, exacerbate them. They also believe that the amendment would undesirably alter the balance of power between the President and the Congress by shifting additional power to the executive branch. Finally, the opponents question how the judiciary would interpret such a constitutional provision and what sorts of court interventions in federal budgeting might ensue.

Amendment supporters point to the federal record of rising budget deficits to underline the need to compel deficit reduction. They argue that the statutory approach to controlling federal deficits has failed, leaving only the constitutional requirement as an effective alternative.

RESULTS IN BRIEF

Although 48 of the 50 states have balanced budget requirements, not all states balance every year, even by the relatively flexible state definitions of balance. Nonetheless, many states have raised taxes and cut spending substantially in their attempts to live within resource constraints. State balanced budget requirements, however, do not appear to be the only motivators of these budget actions; thus, relying on such a requirement alone to balance the federal budget may not necessarily achieve that goal.

BALANCED BUDGET REQUIREMENTS

Forty-eight states have balanced budget requirements.[3] In most states, the balanced budget mandates apply to enacted budgets or to the governors' proposed budgets. Few balanced budget requirements specifically mandate year-end balance.

States focus primarily on balancing the "general fund," which includes general tax receipts and discretionary appropriations. General fund spending ranged from 21 to 74 percent of total state spending in fiscal year 1990, as reported by the Congressional Research Service. States measure general fund surplus or deficit cumulatively, carrying over surplus or deficit amounts from the prior year into current year results. Other state funds (such as capital, enterprise, and trust funds) are often expected to balance, although they may not explicitly be covered by balanced budget requirements and some (such as the capital improvements funds) are financed primarily by borrowing, rather than by current revenue. In contrast, the federal government measures deficit or surplus by annually comparing total current year receipts with total current year outlays, including capital. Thus, prior year deficits or surpluses in the federal government are not carried over into current year results as they are in the states. (See appendix I for a description of state balanced budget requirements and their coverage.)

State mechanisms to enforce balanced conditions differ from those that have been considered under a federal balanced budget amendment. State officials told us that unlike the federal government, they do not have provisions for sequestration--automatic spending cuts--or other formula-based processes to implement their requirements. Also, the officials told us that court involvement has not proven significant in compelling state budget reductions, as some fear will occur at the federal level. However, many states give governors the authority to enforce balanced budget requirements throughout the fiscal year by unilaterally

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[3]Vermont and Wyoming are the two exceptions. Although Wyoming has no constitutional or statutory requirements for a balanced budget, budget officials told us that the budget is required to balance in practice. For this reason, it is often included in reports and discussions as the 49th state with a requirement.

reducing state spending. (Appendix II discusses enforcement issues in more detail.)

RECENT STATE EXPERIENCES

Even though most states have balanced budget requirements, their year-end budget results have been mixed. States have made difficult policy decisions to balance their general funds. State tax and fee increases and spending cuts outweighed one-time strategies as budget-balancing measures in the recent experience of the 49 states providing information. Furthermore, although most balanced budget requirements are not explicit regarding balance at year-end, officials from 39 states told us their state budgets had been balanced or in surplus at the end of the budget period every year since 1990. However, according to budget officials, 10 states have carried over or financed deficits at least once in the past 3 years. Furthermore, some states reported balanced budgets at year-end, at least in part, through the use of one-time budget strategies. The one-time measures include use of cash reserves, accounting changes, and deferring current year payments until the following year. (See appendix III for details of state actions and results.)

IMPLICATIONS FOR THE FEDERAL GOVERNMENT

State officials credit a combination of factors with motivating balanced budget actions. In addition to a balanced budget requirement, these factors include the expectation and tradition of balanced budgets and the concern that state bond ratings may be lowered if the state's budget does not balance. A balanced budget requirement in isolation from these other factors may therefore not result in a state--or federal--balanced budget. (Appendix IV discusses factors motivating states to balance their budgets.)

Fundamental differences in state and federal budgeting environments could also preclude the use of state-style requirements at the federal level. The federal budget's unique macroeconomic role could be compromised by a strict balanced budget mandate. For example, the federal budget acts as an automatic stabilizer during economic downturns primarily because spending is maintained as revenue declines, but also because spending for unemployment assistance and other forms of aid rises. However, it could be turned into a destabilizing influence if the mandated response to a recession were an automatic spending cut or tax increase that could only be overridden by a three-fifths majority vote, as proposed in recent amendments. In addition, many governors have authority to make significant budget adjustments during the fiscal year without legislative approval. Although this executive branch authority helps states achieve balance, it would significantly shift budgeting power away from the Congress if applied to the federal government.

Although state budgets are structured differently than the federal budget, this may have less effect than is widely believed. Because the states focus primarily on balancing their general funds, some have questioned whether state budgets would be in balance if they were reported on the federal budget's unified basis. The answer to this question is unclear. A 1979 study suggested that the opposite could be true, that including all funds might increase some state surpluses.[4] Whether this is still the case today and whether all state budgets would show surpluses is not known. (Appendix V provides more detailed discussion of the implications for the federal budget.)

OBJECTIVES, SCOPE, AND METHODOLOGY

In response to your request, we (1) identified state balanced budget provisions, including the type of requirement (constitutional or statutory), the scope of the budget covered, when the budgets must balance, and the presence or absence of any enforcement mechanisms, (2) determined the types of actions state governments have taken to balance recent budgets and the results they have achieved, and (3) addressed implications of state experience for a federal balanced budget amendment.

To meet our objectives we contacted executive branch budget officials in the 50 states and conducted structured interviews with them or their designees in the 49 states from which we received responses. In 3 states, we conducted face-to-face interviews to test the questions and to gather detailed information on budget balancing actions; in 46 states, we conducted telephone interviews.

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[4]Peat, Marwick, Mitchell & Co. draft report, entitled: A Comparative Analysis of Federal and Selected State Financial Data, April 1979.

In general, we did not verify the information state officials provided. We did, however, review constitutions and statutes for all 50 states to determine the nature of state balanced budget requirements as well as to determine when state budgets are legally required to balance. (Appendix VI lists the balanced budget requirements for each state.) We reviewed prior reports on state requirements, including those by the National Association of State Budget Officers, the National Conference of State Legislatures, and the Advisory Commission on Intergovernmental Relations. We also reviewed articles and testimony from previous debates on balanced budget amendments.

We performed this work from August 1992 through February 1993.

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We are sending copies of this report to interested Members of Congress and the Director of the Office of Management and Budget. We will also make copies available to others upon request.

Please contact me at (202) 512-9573 if you or your staff have any questions. Major contributors to this briefing report are listed in appendix VII.

Sincerely yours,

Paul L. Posner

Paul L. Posner
Director, Budget Issues

C O N T E N T S

TYPES OF STATE BALANCED BUDGET REQUIREMENTS

Based on our review of state constitutions and statutes from the 50 states,

- 48 states have balanced budget requirements:
  - 35 states have constitutional requirements
  - 13 states have only statutory requirements
- 2 states have no explicit requirement, but balance is still considered important

Responses of budget officials from 49 states revealed the following:

- In some states, budget officials cited constitutional debt limits as the balanced budget requirement.
- Many states have other requirements, such as expenditure and revenue limits, that affect budget decisions.

TYPES OF STATE BALANCED BUDGET REQUIREMENTS

This appendix discusses types of state balanced budget requirements (constitutional or statutory), the points in the budget cycle when budgets must balance, and kinds of funds covered by the requirements. It also identifies some other legal requirements that can affect state budgeting.

TYPES OF REQUIREMENTS

All states, with the exception of Vermont and Wyoming, have balanced budget requirements. As shown in table I.1, 35 states have a constitutional balanced budget requirement and 13 states have only a statutory one. Wyoming has no constitutional or statutory requirements for a balanced budget, but its budget officials told us that the budget is expected to balance and that it is sometimes considered to be the 49th state with a requirement.

In some states, officials cited constitutional limits on debt as their state's balanced budget requirement. This response confirms findings in our earlier report[5] that some balanced budget requirements are based on interpretations of state constitutions and statutes rather than on an explicit statement that the state must have a balanced budget. This interpretive element makes it difficult to classify requirements as either constitutional or only statutory. For this report, we based our results on a thorough review of state constitutions and statutes in which we looked for explicit language requiring a balanced budget. We did not consider debt limitations to constitute balanced budget requirements because such limitations often allow for voter approved debt and/or do not restrict the use of nonguaranteed debt.[6] However, we found statutory balanced budget requirements for every state in which officials cited debt limits as requirements.

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[5]See Budget Issues: State Balanced Budget Practices (GAO/AFMD-86-22BR, December 10, 1985), p. 27.

[6]Nonguaranteed debt is generally defined as long-term debt payable solely from pledged specific sources rather than from general tax revenues.

Table I.1: Types of State Balanced Budget Requirements

States with constitutional requirements		
Alabama	Kansas	Ohio
Arizona	Kentucky	Oklahoma
California	Louisiana	Oregon
Colorado	Maryland	Pennsylvania
Connecticut	Massachusetts	South Carolina
Delaware	Michigan	South Dakota
Florida	Missouri	Tennessee
Georgia	Montana	Texas
Hawaii	Nevada	Utah
Idaho	New Jersey	Virginia
Illinois	New York	West Virginia
	North Carolina	Wisconsin
Total: 35		
States with statutory requirements		
Alaska[a]	Maine[a]	New Mexico[a]
Arkansas	Minnesota[a]	North Dakota[a]
Indiana[a]	Mississippi	Rhode Island[a]
Iowa[a]	Nebraska[a]	Washington
	New Hampshire	
Total: 13		
States with no constitutional or statutory requirement		
Vermont[b]		
Wyoming[c]		
Total: 2		

[a]These states also have constitutional debt limits that have been cited as balanced budget requirements.

[b]Vermont's statutory provisions indicate that budget balance is a goal.

[c]Wyoming's existing consitutional debt limit was not cited as a requirement. However, a strong expectation for a balanced budget was cited as a requirement in practice.

Source: Our analysis of state constitutions and statutes.

OTHER REQUIREMENTS

Many states have other legislative requirements that can affect state budget decisions and actions. These requirements include limits on expenditures and revenues and large portions of revenue earmarked for special purposes. According to state budget officials, 21 states have spending limits, 7 have revenue limits, and 3 have both. While most states have earmarked revenues, only two officials said that they significantly affected decisions about balancing the budget.

Expenditure and revenue limits take several forms. In some states, the growth in state personal income for a previous or base year limits appropriations or tax revenues. Some expenditure limits stipulate that growth in appropriations shall not exceed increases in population and inflation. Other expenditure controls limit appropriations to a fixed percentage of estimated revenue. For example, in Delaware the limit is 98 percent of estimated general fund revenue.

In many states with such requirements, budget officials said that the requirements were not particularly restrictive and did not necessarily make balancing the budget more difficult. In some states, however, officials perceived that these additional requirements limited potential budget balancing actions. In Colorado, for example, voters recently amended the state constitution to require voter approval of any tax increase and limit spending to the prior year's level plus inflation and the percentage increase in the population. Colorado budget officials were concerned that this new requirement might make balancing the budget more difficult. Budget officials in California said that roughly 40 percent of budget revenue is earmarked for education, making it more difficult to balance the state budget. In Alabama, a budget official said the large proportion of earmarked revenue (approximately 89 percent) somewhat constrained budgetary decisions.

WHEN STATE BUDGETS MUST BALANCE

Based on our review, most state budgets must balance at least through the formulation and enactment phases.

- **In 43 states, the budget proposed by the governor or the state budget board must balance.**
- **In 36 states, the budget that the legislature enacts must balance.**
- **Few requirements refer explicitly to year-end balance.**
- **In 39 states, officials said that budgets were required to balance at year-end; however, in 11 of these states, they said that deficits could be carried over if necessary.**

WHEN BUDGETS MUST BALANCE

Most state budgets must balance through formulation and enactment. In 43 states, the governor or the budget board must propose a balanced budget. In 36 states, the budget as enacted by the legislature must balance. Table I.2 provides information on the stages at which each state budget must balance.

Table I.2: When State Budgets Must Balance

State	Governor or budget board proposal	Legislative enactment
Alabama	X	X
Alaska	X	X
Arizona	X	X
Arkansas	X	X
California	X	X
Colorado	X	X
Connecticut	X	X
Delaware	X	X
Florida	X	X
Georgia	X	X
Hawaii	X	X
Idaho		X
Illinois	X	X
Indiana[a]		
Iowa	X	
Kansas	X	X
Kentucky	X	X
Louisiana	X	X
Maine	X	
Maryland	X	X
Massachusetts	X	X
Michigan	X	X
Minnesota	X	
Mississippi	X	
Missouri	X	
Montana	X	X
Nebraska	X	X
Nevada	X	X
New Hampshire	X	
New Jersey	X	X
New Mexico	X	
New York	X	
North Carolina	X	X
North Dakota	X	
Ohio	X	X
Oklahoma	X	X
Oregon	X	X
Pennsylvania	X	X
Rhode Island	X	X
South Carolina	X	X
South Dakota	X	X
Tennessee	X	X
Texas		X
Utah	X	X
Vermont		
Virginia[b]		
Washington	X	
West Virginia		X
Wisconsin	X	X
Wyoming		
Total	43	36

[a]Indiana's requirement does not explicitly state whether the budget must balance at the beginning of the year.

[b]In Virginia, the governor is required to ensure that expenditures do not exceed revenues during budget execution.

Source: Our analysis of state constitutions and statutes.

As with the balanced budget requirement itself, the question of when a budget has to balance is open to interpretation. We based our calculations on a reading of constitutions and statutes. However, when we asked budget officials about when budgets had to balance, 48 responded that the budget had to be balanced when the governor proposed it and 46 said it had to be balanced when the legislature passed it.

It is even less clear how many state budgets must balance at the end of the budget period. While only a few states have balanced budget requirements that explicitly refer to year-end balance, officials in 39 states said their state budget was required to balance at the end of the budget period. However, 11 of these 39 officials also said that their state could carry over a deficit from one budget period to the next if necessary.

The requirement to be in balance at the end of the budget period appears to be more of a perception than an explicitly stated legal requirement. As shown in table I.3, 21 states can carry over deficits if necessary (the 10 states that do not require year-end balances plus the 11 that require balance but allow carryover and/or borrowing if necessary). We found, however, that the language of the balanced budget requirements did not always clearly differentiate this group of states from those in which budget officials said a deficit could never be carried over from one budget period to the next.

Table I.3: Reported State Requirements for Year-end Budget Balance

Year-end budget balance not required		
California	Illinois	Pennsylvania
Connecticut	Iowa	Texas
Delaware	Nebraska	Vermont
	New Hampshire	
Total: 10		
Year-end budget balance required		
Alabama	Maine	Ohio
Alaska	Maryland[a]	Oklahoma
Arizona[a]	Massachusetts[a]	Oregon
Arkansas	Michigan[a]	Rhode Island
Colorado	Minnesota	South Carolina
Florida	Mississippi	South Dakota
Georgia[a]	Missouri	Tennessee
Hawaii	Montana	Utah[a]
Idaho	New Jersey	Virginia[a]
Indiana	New Mexico	Washington[a]
Kansas	New York[a]	West Virginia
Kentucky	North Carolina	Wisconsin[a]
Louisiana[a]	North Dakota	Wyoming[b]
Total: 39		

Note: States total 49 because no response was received from Nevada.

[a]Although these states require year-end budget balance, carryover and/or borrowing to finance a deficit are allowed if necessary.

[b]Although Wyoming has no legal requirement to balance the budget, officials cited a strong expectation for a balanced budget as a requirement in practice.

Source: Interviews with state budget officials.

APPENDIX I

KINDS OF FUNDS COVERED BY BALANCED BUDGET REQUIREMENTS

- Requirements do not always specify which funds must balance.
- States focus on balancing operating (general) funds.
- According to Congressional Research Service calculations, general fund spending was 54 percent of total state spending for fiscal year 1990.
- Other funds, such as capital funds, may be required to balance, but states use borrowing to finance them.
- According to budget officials in 25 states, capital funds are covered under balanced budget requirements; however, these states issue long-term debt to finance capital projects.

FUNDS COVERED BY REQUIREMENTS

State constitutions and statutes do not always specify which funds are subject to balancing requirements. In practice, however, state governments focus primarily on balancing general fund budgets and not on the other major state fund groups, such as capital, enterprise, and trust funds. According to budget officials from all 49 states responding, their states had general funds, defined as the funds into which general tax receipts are credited for discretionary appropriation. For the states with balanced budget requirements, officials said that the general fund is required to balance. While other funds, such as capital or bond funds, may be required to balance, states include bond proceeds when determining if the funds are balanced. In other words, these funds may use borrowed amounts to balance--a convention which is not followed at the federal level where borrowing is not counted as receipts for purposes of calculating surpluses or deficits.

According to Congressional Research Service calculations, general fund spending was 54 percent of total state spending for fiscal year 1990. This percentage was estimated by dividing general fund expenditures for each state (as reported by the National Association of State Budget Officers) by total spending per state (as reported by the Census Bureau) for fiscal year 1990. The Congressional Research Service reported that general fund spending ranged from 21 percent of total state spending in Wyoming to 74 percent in Hawaii.

Budget officials from 25 of 49 states told us that capital funds were covered under their state's balanced budget requirement. However, all of these states finance major capital projects by issuing long-term debt. Using the federal approach to measuring deficit or surplus (that is, matching current year receipts to current year expenditures), these states do not balance their capital funds. State officials explained that when including capital funds under balanced budget requirements, their states cannot spend more than they borrow or, in most cases, that debt service payments are included under balanced budget requirements. According to Census figures, state spending for capital was 9 percent of total state general spending in fiscal year 1990.[7]

[7]The Census Bureau defines "general expenditure" as all state government expenditure other than that classified under utility expenditure, liquor stores expenditure, and employee-retirement or other insurance trust expenditure.

ENFORCEMENT PROVISIONS AND IMPLEMENTATION ISSUES

- Very few states have provisions for automatic spending reductions or revenue increases.
- Governors have broad powers to cut budgets during the year.
- Some states have legislative supermajority voting requirements to increase revenue.
- State officials said that generally court decisions were not a factor enforcing balanced budget requirements; however, court decisions were cited in cases where spending cuts were questioned.
- Very few states have legal sanctions or penalties for not balancing the budget.

ENFORCEMENT PROVISIONS AND IMPLEMENTATION ISSUES

Federal legislators have felt it necessary to develop formula-based budget rules and structures, including automatic sequestration provisions, to guide and discipline deficit reduction in the complex world of federal budgeting. Observers have noted that a federal balanced budget requirement is likely to depend on such enforcement provisions and on the courts to resolve disagreements over interpretation and application of the requirement.

By contrast, state governments do not rely extensively on formula-based provisions to implement their balanced budget requirements. Most states also do not rely on formal legal sanctions to motivate balancing, and the courts have played a minimal role in interpreting and applying state requirements. Unlike the President, many state governors can enforce budget balance through unilateral actions to reduce expenditures during the budget period.

VERY FEW STATES HAVE FORMULA-BASED ENFORCEMENT PROVISIONS

Federal statutes aimed at balancing the budget, such as the Balanced Budget and Emergency Deficit Control Act of 1985 (Gramm-Rudman-Hollings) and the Budget Enforcement Act of 1990, prescribe specific formulas for bringing down deficits that exceed legislatively established thresholds. However, at the state level, automatic enforcement mechanisms, such as sequesters or "trigger taxes," are rare. Most state officials told us that there were no such automatic mechanisms in their states. In California, we found that a mechanism exists which automatically reduces budget year appropriations when forecasted general fund revenues are insufficient to fund the state's general fund workload budget.[8] This mechanism reduced the 1991-1992 budget by about $800 million, but the state suspended the mechanism for

[8]The general fund workload budget is defined as existing programs adjusted for factors such as inflation; federal or court ordered mandates; and changes in enrollment, caseload, or population.

budget year 1992-1993 and has proposed suspension for the 1993-1994 budget. No state officials we spoke to said that their state had trigger taxes; that is, tax increases that automatically take effect under certain specified economic conditions, though the concept received some attention during the 1980s.[9]

GOVERNORS HAVE POWER TO CUT BUDGETS

Many governors can enforce balanced budget requirements by reducing spending during the budget year. Budget reduction authority available to state governors was characterized in a recent National Conference of State Legislatures report[10] as ranging from no restrictions on the governor's authority to reduce spending, to cutting across-the-board only, to having a maximum percent reduction, to having to consult with the legislature before making any cuts.

Budget officials we spoke to also confirmed that the reduction powers of the governors varied. For example, the governor's maximum reduction authority ranged from 3 percent of a fund or 5 percent of an appropriation in Connecticut to 10 percent in Louisiana and to 25 percent of most executive-branch appropriations in Maryland. In Kentucky, the governor can cut up to 2.5 percent of agency budgets but must implement a budget reduction plan that has been preapproved by the legislature for reductions between 2.5 and 5 percent.

SUPERMAJORITY VOTING REQUIREMENTS

According to budget officials, eight states have legislative supermajority (that is, 60 percent or greater) voting requirements for revenue increases. These requirements make it more difficult for states to increase taxes in order to balance the budget and thus serve as a procedural, rather than explicit, spending limit.

[9]See National Conference of State Legislatures, Legislative Finance Paper #60, State Deficit Management Strategies, November 1987, pp. 55-56.

[10]See National Conference of State Legislatures, Legislative Authority Over The Enacted Budget, July 1992, table 6.

FEW COURT CASES ENFORCING CUTS

In 16 of 49 responses, state budget officials said that there had been court decisions or attorney general opinions that affected balanced budget requirement interpretation. None of these cases involved a party suing the state to enforce balanced budget requirements. In reviewing these and other cases, we found that legal cases often centered on the governor or budget board's authority to reduce expenditures and were brought by parties that either claimed to be harmed by the spending reductions or contested their validity.

Budget officials from only 3 of the 49 states said that their state legally sanctioned or penalized officials if the state budget was not balanced. These states were New Mexico, South Dakota, and Virginia. According to budget officials, possible sanctions included removal from office, fines, and jail terms for responsible state officials. However, these officials said that they knew of no use of the sanctions.

RECENT STATE EXPERIENCE

- Budget officials in 41 states reported budgetary stress (that is, fiscal pressure) since 1990.

- In response, states have increased revenues, reduced expenditures, and taken one-time budget balancing actions.

- Although many states acted to close midyear budget gaps, some still reported deficits at the end of the most recent budget period.

- Officials in 10 states reported either ending with a deficit or financing one since 1990.

RECENT STATE EXPERIENCE

According to state budget officials, most states have experienced budgetary stress since 1990. In response, state governments have increased revenues, reduced expenditures, and taken other one-time budget balancing actions.

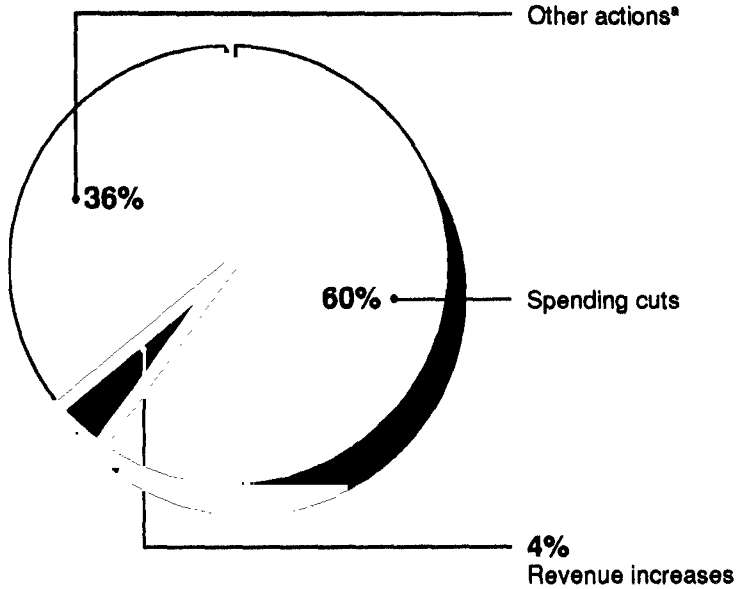
BUDGET STRESS

Budget officials from 41 of 49 states told us that their state had experienced significant budgetary stress over the past several years. Officials attributed increases in Medicaid spending, the recent recession, increases in federally mandated programs, and growth in spending for education and corrections with causing the greatest amount of budgetary stress. Officials in several states also said population growth was a major contributor. State associations have documented the fiscal stress which has characterized states' general environment since 1990.

BUDGET GAP-CLOSING ACTIONS BY STATES

We asked budget officials if their states had acted to close budget gaps midyear during the prior budget period and/or during enactment of the current budget. Budget officials in 38 of 49 states reported that their states had taken steps to close midyear gaps during the last budget period, and 32 of them provided the amount of the gap and how it was closed. The total amount of midyear gaps closed was $9.3 billion, which represented an average of about 4 percent of general fund spending. In 33 of 49 states, officials reported closing budget gaps as part of the enactment of the current year's budget, and 25 of them provided the amount of the gap and how it was closed. The total amount of gaps closed during enactment was $28.3 billion. See figures III.1 through III.6 for information on how gaps were closed in terms of total dollars and the number of states taking one-time actions. See tables III.1 and III.2 for the number of states using each of the three gap-closing options (that is, revenue increases, spending reductions, one-time actions). Table III.3 provides information on budget and legislative cycles for each state.

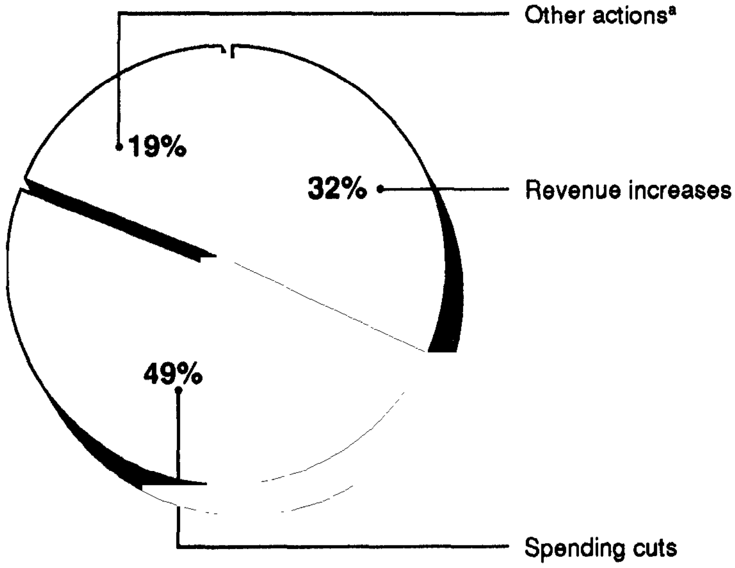
Figure III.1: Dollar Value of Budget Balancing Actions 32 States Took to Close Midyear Gaps for Most Recently Completed Budget Periods



Note: Thirty-eight of 49 states reported midyear gaps, but only 32 provided the amount of the gap and how it was addressed. The total midyear gap the 32 states closed was $9.3 billion. Budget periods were 1991-1992, 1990-1992, or 1989-1991. Three of the states reporting midyear gap-closing actions during the 1991-1992 budget year also reported deficits at year-end.

[a]Other actions included use of rainy day funds, interfund transfers, deferred payments, and short-term borrowing.

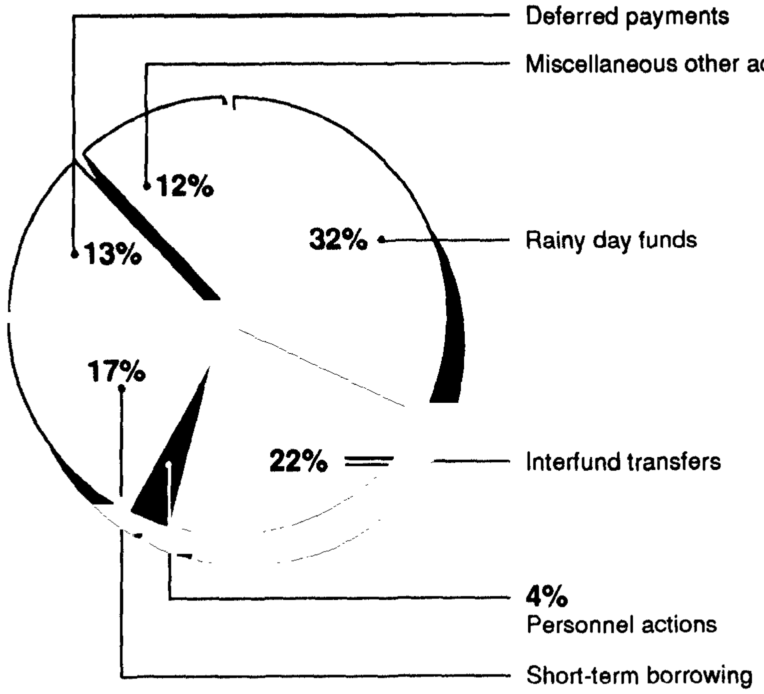
Figure III.2: Dollar Value of Budget Balancing Actions 25 States Took to Close Gaps During Enactment of Current Budgets



Note: Thirty-three of 49 states reported gaps during budget enactment, but only 25 provided the amount of the gap and how it was addressed. The total gap the 25 states closed was $28.3 billion. Budget periods were 1992-1993, 1992-1994, or 1991-1993. One state reported closing only 90 percent of the gap during enactment.

[a]Other actions included use of rainy day funds, interfund transfers, deferred payments, and reduced pension contributions.

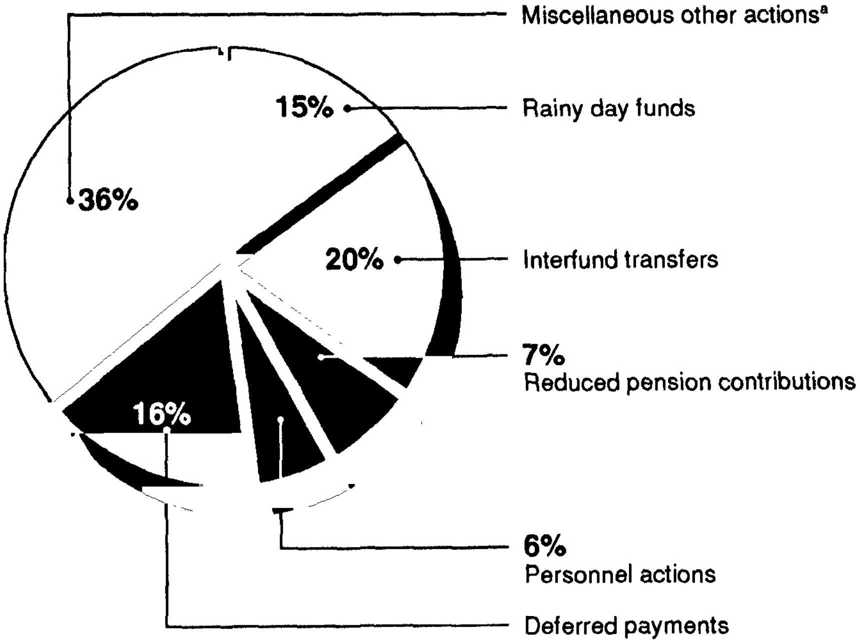
Figure III.3: Dollar Value of Other Actions Used to Close Midyear Budget Gaps for Most Recently Completed Budget Periods



Note: Twenty-four of 32 states providing details on how midyear gaps were closed used one or more of these other actions to close over $3 billion in gaps.

[a]Miscellaneous other actions included an accounting change and the use of a pension surplus.

Figure III.4: Dollar Value of Other Actions Used to Close Budget Gaps During Enactment for Most Recently Enacted Budgets

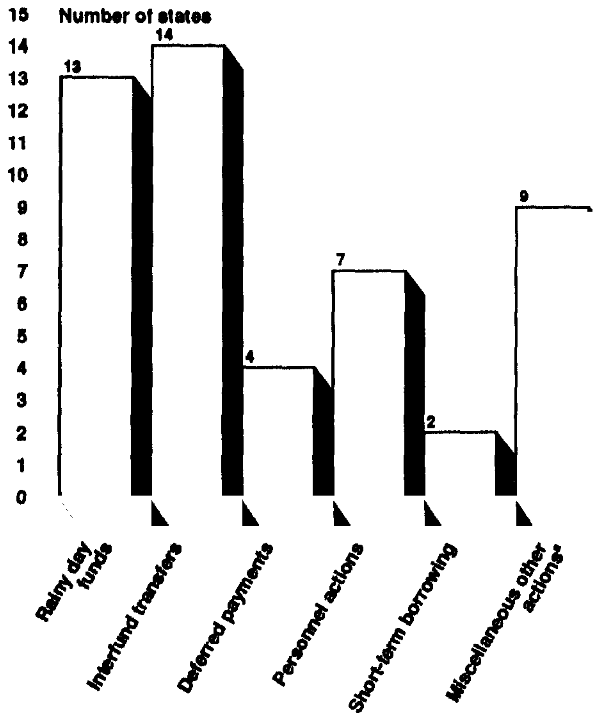


Note: Eighteen of 25 states providing details on how gaps were closed during budget enactment used one or more of these other actions to close over $5 billion in gaps.

[a]Miscellaneous other actions include two uses of pension surpluses. They also include a $1.3 billion cost shift from the California state general fund to cities and counties for education funding. If this action was reported separately, the total for miscellaneous other actions would be 9 percent.

APPENDIX III

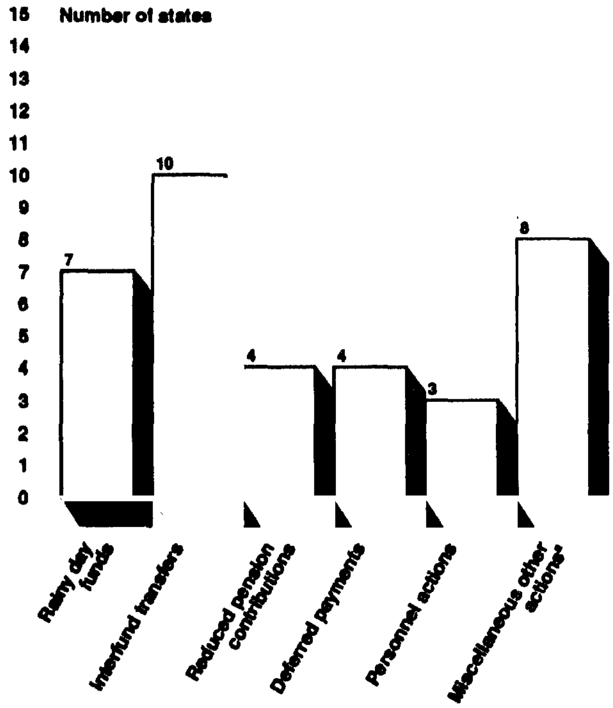
Figure III.5: Number of States Using Other Actions to Close Midyear Budget Gaps In Most Recently Completed Budget Periods



Note: Twenty-four of 32 states providing details on how midyear gaps were closed used one or more of these other actions.

[a]Miscellaneous other actions include one accounting change and one use of a pension surplus.

Figure III.6: Number of States Using Other Actions to Close Budget Gaps During Enactment of Current Budgets



Note: Eighteen of 25 states providing details on how budget gaps were closed during enactment used one or more of these other actions.

[a]Miscellaneous other actions include two uses of pension surpluses.

Table III.1: Actions Taken Midyear to Close Gaps During Budget Execution

State	Fiscal period covered	Amount of gap (millions)	Increase revenue	Reduce spending	Take other actions
Alabama	1991-92	$115.3		X	
Alaska	1991-92	310.0			X
Arizona	1991-92	41.0	X	X	X
Arkansas					
California					
Colorado	1991-92	108.0		X	X
Connecticut					
Delaware	1991-92	11.0		X	
Florida	1991-92	720.5		X	X
Georgia	1991-92	510.0		X	X
Hawaii					
Idaho	1991-92	14.0		X	
Illinois	1991-92	350.0		X	X
Indiana	1989-91	91.8		X	X
Iowa	1991-92	253.9	X	X	X
Kansas	1991-92	24.8		X	
Kentucky	1991-92	177.0		X	X
Louisiana	1991-92	156.2		X	X
Maine	1991-92	148.6	X	X	X
Maryland	1991-92	727.6	X	X	X
Massachusetts					
Michigan	1991-92	783.7	X	X	X
Minnesota	1989-91	197.0	X	X	X
Mississippi	1991-92	75.6		X	
Missouri	1991-92	71.0		X	
Montana					
Nebraska					
Nevada					
New Hampshire					
New Jersey	1991-92	150.0			X
New Mexico					
New York	1991-92	875.0		X	X
North Carolina					
North Dakota	1989-91	59.0		X	
Ohio	1991-92	300.0	X	X	X
Oklahoma	1991-92	52.0		X	X
Oregon					
Pennsylvania					
Rhode Island					
South Carolina	1991-92	248.2		X	X
South Dakota					
Tennessee	1991-92	80.0		X	X
Texas	1989-91	400.0	X	X	
Utah					
Vermont	1991-92	21.0		X	X
Virginia	1990-92	2181.9	X	X	X
Washington					
West Virginia	1991-92	50.0		X	X
Wisconsin					
Wyoming	1990-92	45.0	X	X	X
Total		$9,349.1	10	30	24

Source: Unaudited figures from interviews with state budget officials.

Table III.2: Actions Taken During Enactment to Close Budget Gaps

State	Fiscal period covered	Amount of gap (millions)	Increase revenue	Reduce spending	Take other actions
Alabama	1992-93	$24.0		X	
Alaska	1992-93	167.7	X	X	X
Arizona					
Arkansas					
California	1992-93	7900.0	X	X	X
Colorado	1992-93	55.0	X		
Connecticut	1992-93	1085.0	X	X	
Delaware					
Florida	1992-93	1052.6	X	X	
Georgia					
Hawaii					
Idaho	1992-93	11.3		X	X
Illinois	1992-93	1459.0	X	X	X
Indiana	1991-93	829.5			X
Iowa	1992-93	220.0	X	X	
Kansas					
Kentucky					
Louisiana	1992-93	1206.0	X	X	X
Maine	1992-93	129.6	X	X	X
Maryland	1992-93	362.0	X	X	
Massachusetts					
Michigan					
Minnesota	1991-93	1657.0	X	X	X
Mississippi					
Missouri	1992-93	41.0		X	
Montana					
Nebraska					
Nevada					
New Hampshire					
New Jersey	1992-93	930.0		X	X
New Mexico	1992-93	20.0			X
New York	1992-93	4800.0	X	X	X
North Carolina					
North Dakota					
Ohio					
Oklahoma					
Oregon					
Pennsylvania	1992-93	105.0		X	X
Rhode Island					
South Carolina	1992-93	202.1		X	X
South Dakota					
Tennessee					
Texas	1991-93	4600.0	X	X	X
Utah					
Vermont	1992-93	20.0		X	X
Virginia	1992-94	648.5	X	X	X
Washington	1991-93	694.0	X	X	X
West Virginia					
Wisconsin					
Wyoming	1992-94	100.0		X	X
Total		$28,319.3	15	22	18

Source: Unaudited figures from interviews with state budget officials.

Table III.3: State Budget and Legislative Calendars

State	Fiscal year begins	Budget cycle		Legislative cycle	
		Annual	Biennial	Annual	Biennial
Alabama	October	X		X	
Alaska	July	X		X	
Arizona	July	X		X	
Arkansas	July		X		X
California	July	X		X	
Colorado	July	X		X	
Connecticut	July	X		X	
Delaware	July	X		X	
Florida	July	X		X	
Georgia	July	X		X	
Hawaii	July		X	X	
Idaho	July	X		X	
Illinois	July	X		X	
Indiana	July		X	X	
Iowa	July	X		X	
Kansas	July	X		X	
Kentucky	July		X		X
Louisiana	July	X		X	
Maine	July		X	X	
Maryland	July	X		X	
Massachusetts	July	X		X	
Michigan	October	X		X	
Minnesota	July		X	X	
Mississippi	July	X		X	
Missouri	July	X		X	
Montana	July		X		X
Nebraska	July		X	X	
Nevada	July		X		X
New Hampshire	July		X	X	
New Jersey	July	X		X	
New Mexico	July	X		X	
New York	April	X		X	
North Carolina	July		X		X
North Dakota	July		X		X
Ohio	July		X	X	
Oklahoma	July	X		X	
Oregon	July		X		X
Pennsylvania	July	X		X	
Rhode Island	July	X		X	
South Carolina	July	X		X	
South Dakota	July	X		X	
Tennessee	July	X		X	
Texas	September		X		X
Utah	July	X		X	
Vermont	July	X		X	
Virginia	July		X	X	
Washington	July		X	X	
West Virginia	July	X		X	
Wisconsin	July		X	X	
Wyoming	July		X	X	
Total		31	19	42	8

Source: Interviews with state budget officials and limited state reviews.

In general, state governments used spending cuts and one-time actions to close midyear budget gaps, and spending cuts and revenue increases to close gaps prior to budget enactment. According to budget officials, 60 percent of the $9.3 billion in total midyear gaps were closed using spending cuts, 36 percent using one-time actions, and 4 percent using revenue increases. Of the 32 states that closed midyear gaps, none used just revenue increases, 8 used just spending cuts (4.7 percent of total $9.3 billion gap), and 2 used just other actions (4.7 percent of total gap). The other 22 states used a combination of the three options.

Budget officials told us that during enactment of current year budgets, 49 percent of the $28.3 billion dollars in total budget gaps were closed with spending cuts, 32 percent with revenue increases, and 19 percent with one-time actions. Of the 25 states that provided information on closing gaps during enactment, 1 used only revenue increases (.2 percent of total $28.3 billion gap closed), 2 used only spending cuts (.2 percent of total gap), and 2 used only other actions (3 percent of total gap). The other 20 states used combinations of the options.

State officials reported using over $3 billion in other actions to close midyear gaps during the previous budget period and over $5 billion in other actions to close gaps during enactment of the current budget. Other actions included use of rainy day funds or operating reserves, transfers from other funds into the general fund, drawing down of pension surpluses, reducing pension contributions, short-term borrowing, accounting changes, and deferring payments to the next fiscal period. Many of these actions could be considered one-time budget "fixes".

SOME STATES STILL REPORT DEFICITS

Although officials from 32 states reported state action to close midyear gaps, 3 reported that their state ended fiscal year 1992 with a deficit. These states were Illinois, Maryland, and Vermont.

Budget officials from 10 states reported that deficits had been carried over and/or the state had borrowed to finance deficits at some time during the past three budget periods. Budget officials from California, Connecticut, Illinois, Maryland, Michigan, New

Hampshire, Pennsylvania, and Vermont said that their state had carried over deficits. Budget officials from Connecticut, Massachusetts, New York, and Vermont said that their states had borrowed money to cover or consolidate budget deficits.[11]

[11]At the end of its fiscal year 1992, Connecticut converted 2 years worth of budget deficits ($808 million for 1991 plus $157 million for 1992 for a total of $965 million) into bonds payable over the next 5 years. Massachusetts borrowed $1.4 billion to finance its 1990 deficit. In its fiscal years 1990, 1991, and 1992, New York issued short-term deficit notes of $775 million, $1.081 billion, and $531 million, respectively. Vermont issued $65 million of general obligation notes in fiscal 1991 to finance its deficit.

APPENDIX III

FACTORS MOTIVATING STATES TO BALANCE THEIR BUDGETS

- Budget officials cited the following factors as significant motivators to balance the state budget:

  - the legal requirement (45)

  - tradition (42)

  - concern over bond ratings (32)

  - all three factors (28)

- States without year-end balance requirements took steps to close midyear gaps, demonstrating that factors other than balanced budget requirements motivate action.

FACTORS MOTIVATING STATES TO BALANCE THEIR BUDGETS

Budget officials in 49 states listed the factors that motivate their state government to try to enact and maintain a balanced budget. The full list of factors included the balanced budget requirement itself, enforcement provisions and sanctions, court decisions, the tradition or expectation of balance, bond ratings, and other motivators.

The results indicated that the balanced budget requirement, while important, was not the only factor that encouraged balanced budgets. Budget officials in 45 states identified the balanced budget requirement as an important motivating factor in state efforts to maintain balanced budgets. However, two other motivating factors, the tradition and expectation of balance and the concern over bond ratings, were cited almost as often. Factors such as enforcement provisions, sanctions, and court decisions were cited by only a few officials as being significant motivators.

The importance of factors other than the balanced budget requirements is evident because of the number of states that took steps to close midyear gaps that did not have year-end balance requirements. Of the 10 states that, according to budget officials, are not required to have a balanced budget at the end of the year, 4 states[12] took steps to close budget gaps that were identified during the execution of the 1992 budget. In these cases, the spirit, rather than the letter, of the balanced budget requirement significantly motivated action on the budget gaps.

[12]Delaware, Illinois, Iowa, and Vermont.

IMPLICATIONS FOR FEDERAL BUDGETING

- The state experience with balanced budget requirements may not transfer to the federal budget for the following reasons:

  - The role of the federal government (for example, stabilizing the economy) may not always be compatible with achieving a balanced budget.

  - The balance of powers is different at the state and federal levels. (For example, many governors can cut budgets during the year without legislative approval.)

  - Other factors motivating state efforts to balance budgets (for example, bond ratings) have not been strong enough at the federal level to maintain a balanced budget.

  - Some balanced budget requirements provide enough flexibility for states to carry over deficits if necessary.

- Although federal and state budget structures differ, results may not.

IMPLICATIONS FOR FEDERAL BUDGETING

While the state experience with balanced budget requirements has some positive aspects, it may not be directly transferrable to the federal government for a number of reasons, including the role of the federal government in the economy, the power of governors to unilaterally reduce budgets, and the differences in the two governmental budget structures. Given these differences, the other external motivating factors at the state level, and the flexibility afforded the states in meeting requirements, the state model may not be appropriate for a federal requirement.

FEDERAL BUDGET ROLE IN ECONOMY

Because the federal budget must address responsibilities that do not exist at the state level, state experience with balanced budget requirements may not entirely apply to the federal budget. Most importantly, the federal budget's unique macroeconomic role could be compromised by a strict balanced budget requirement. For example, the federal budget acts as an automatic stabilizer during economic downturns, primarily because spending is maintained. Also, additional spending is induced for unemployment assistance and other forms of aid. However, the federal budget could have a destabilizing influence if the mandated response to a recession were an automatic spending cut or tax increase that could only be overridden by a three-fifths majority vote, as proposed in recent amendments.

EXECUTIVE POWER TO UNILATERALLY CUT THE BUDGET

Unlike the President, many governors have the unilateral authority and responsibility to reduce expenditures during budget execution in order to avoid an end-of-period deficit. In contrast, the President's power to impound is subject to legislative control.

OTHER MOTIVATORS

State budget officials told us that in addition to the requirements themselves, the expectation or tradition of balanced budgets as well as concern over bond ratings were important motivating factors in their states' efforts to balance budgets. Without these other factors, balanced budget requirements may not be sufficient to ensure balanced state budgets. While present at the federal level, concerns over long-term budget balance and credit worthiness have not been historically strong enough to maintain a balanced federal budget.

FLEXIBILITY TO CARRY OVER DEFICITS

As discussed in appendix I, some states with balanced budget requirements also have the flexibility to carry over deficits if necessary. This allows states to deal with unanticipated deficits resulting from a variety of possible causes, including emergencies and unforeseen drops in state revenues. Although this flexibility means that states with requirements do not always have balanced budgets, it also means that state governments are not forced into automatic or sequester-like actions as the federal government would be under some balanced budget proposals.

BUDGET STRUCTURES DIFFER, BUT RESULTS MAY NOT

Some argue that the test of whether budgets are balanced would be more stringent under the federal approach, which counts the entire unified budget, whereas states normally only base the calculation on their general fund budgets.[13] However, it is not clear whether state budgets would or would not be in balance if they were reported on the federal budget's unified basis or, conversely, that the federal budget would be any easier to balance on a state basis.

While we have not assessed how states would fare using federal budgeting concepts, a 1979 study suggests that most state budgets might not fall into deficit on a unified basis.[14] Even though capital spending--which would be included on a unified basis--is typically debt financed, it comprised only 9 percent of total state general spending in 1990. A unified budget, moreover, would permit states to include trust funds, which are typically in surplus and, therefore, would offset deficits.

It is also unclear whether the federal budget would be easier to balance on a state basis. A variety of factors would have to be considered to convert the federal budget to a state basis, and our study was not designed to analyze these differences. The 1979 Peat-Marwick study cited above concluded that in 1978 the federal budget deficit would have been somewhat smaller if calculated in

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[13]See Louis Fisher, "The Effects of a Balanced Budget Amendment on Political Institutions," The Journal Of Law & Politics, Vol. IX, No. 1, Fall 1992.

[14]See Peat, Marwick, Mitchell & Co. draft report, entitled: A Comparative Analysis of Federal and Selected State Financial Data, prepared for the Congressional Budget Office, April 1979.

the same way states calculate their deficits. However, there have been changes since 1979, most particularly the dramatic growth in the federal trust fund surpluses which masks the general fund deficit. This would imply that the federal deficit might look larger on a state basis. However, states exclude capital and enterprise funds, and the impact of excluding these programs on the federal general fund deficit would depend on how they might be defined at the federal level.

STATE BALANCED BUDGET CITATIONS

State	Type of requirement	Citations
Alabama	C	Ala. Const. art. XI, § 213, amend. no. 26 See also Ala. Code §§ 41-4-83, -90, 41-19-4, -7, -9 (1991)
Alaska	S	Alaska Stat. §§ 37.07.020, 37.07.030 (1988 & Supp. 1991)
Arizona	C	Ariz. Const. art. 9, § 3 See also Ariz. Rev. Stat. Ann. §§ 35-115.4, 35-144 (1990 & Supp. 1992)
Arkansas	S	Ark. Stat. Ann. tit. 19, ch. 4 (1987) See also Ark. Stat. Ann. § 19-1-212(4) (1987)
California	C	Cal. Const. art. IV, § 12(a) See also Cal. Gov't Code § 13337.5 (Deering 1991)
Colorado	C	Colo. Const. art. X, §§ 2, 16 See also Colo. Rev. Stat. §§ 24-37-301, -304(1)(a) (1988 & Supp. 1990)
Connecticut	C	Conn. Const. art. 3, § 18 See also Conn. Gen. Stat. Ann. §§ 2-35, 4-72 (West Supp. 1992)
Delaware	C	Del. Const. art. VIII, § 6 See also Del. Code Ann. tit. 29, §§ 6334(b)(3), 6337, 6339, 6533 (1991)
Florida	C	Fla. Const. art. 7, § 1 See also Fla. Stat. Ann. ch. 216 (West 1989 & Supp. 1993)
Georgia	C	Ga. Const. art. 3, § 9, ¶¶ 4, 5 See also Ga. Code Ann. § 45-12-75 (Michie 1990)
Hawaii	C	Haw. Const. art. 7, § 5 See also Haw. Const. art. 7, §§ 7, 8, 9, Haw. Rev. Stat. § 37-71(d)(1)(B) (Supp. 1991)
Idaho	C	Idaho Const. art. 7, § 11
Illinois	C	Ill. Const. art. 8, § 2
Indiana	S	Ind. Code Ann. §§ 4-10-18-1 to 4-10-18-9, 4-9.1-1-10, 4-13-2-18 (Burns 1990)
Iowa	S	Iowa Code Ann. ch. 8 (West 1989 & Supp. 1992)

Legend: C = Constitutional S = Statutory N/A = Not applicable

State	Type of requirement	Citations
Kansas	C	Kan. Const. art. 11, § 4 See also Kan. Stat. Ann. § 75-3721 (Supp. 1991)
Kentucky	C	Ky. Const. § 171 See also Ky. Rev. Stat. Ann. § 48.110(6) (Baldwin Supp. 1991)
Louisiana	C	La. Const. art. 7, §§ 10, 11 See also La. Const. art. 4, § 5(G)
Maine	S	Me. Rev. Stat. Ann. tit. 5, §§ 1663, 1664, 1666 (1989 & Supp. 1992)
Maryland	C	Md. Const. art. 3, § 52(5a)
Massachusetts	C	Mass. Const. amend. art. 63, secs. 2 [§ 197], 4 [§ 199] See also Mass. Ann. Laws ch. 29B (Law. Co-op. Supp. 1992)
Michigan	C	Mich. Const. art. IV, § 31, art. V, § 18 See also Mich. Const. art. V, § 20
Minnesota	S	Minn. Stat. Ann. § 16A.11.subd. 2 (West 1988) See also Minn. Stat. Ann. § 16A.15 (West 1988 & Supp. 1993)
Mississippi	S	Miss. Code Ann. tit. 27, ch. 103 (1990 & Supp. 1992)
Missouri	C	Mo. Const. art. 3, § 53, art. 4, §§ 24, 27, 27(a), Mo. Ann. Stat. § 33.270 (Vernon 1992)
Montana	C	Mont. Const. art. 8, § 9 See also Mont. Code Ann. § 17-7-123 (1991)
Nebraska	S	Neb. Rev. Stat. §§ 77-2715.01(1)(b), §81-125, 81-125.01 (1990 & Supp. 1992)
Nevada	C	Nev. Const. art. 9, § 2 See also Nev. Rev. Stat. §§ 353.205, 353.235 (1991)
New Hampshire	S	N.H. Rev. Stat. Ann. ch. 9 (1988 & Supp. 1990)
New Jersey	C	N.J. Const. art. 8, § 2, ¶ 2 See also N.J. Stat. Ann. § 52:27B-21, -22 (West 1986)
New Mexico	S	N.M. Stat. Ann. §§ 6-3-10, 6-3-11 (1992)
New York	C	N.Y. Const. art. 7, § 2

Legend: C = Constitutional S = Statutory N/A = Not applicable

State	Type of requirement	Citations
North Carolina	C	N.C. Const. art. 3, § 5 See also N.C. Gen. Stat. § 143-2, -12, -15 (1990)
North Dakota	S	N.D. Cent. Code § 54-44.1-06.6 (1989) See also N.D. Cent. Code §§ 54-27.2-01 to 54-27.2-03, 54-44.1-12 (1989 & Supp. 1991)
Ohio	C	Ohio Const. art. 12, § 4 See also Ohio Rev. Code Ann. §§ 107.03(A) (Anderson 1990)
Oklahoma	C	Okla. Const. art. 10, §§ 2, 3, 23 See also Okla. Stat. Ann. tit. 62, §§ 41.33, 41.34 (West 1989)
Oregon	C	Or. Const. art. 9, §§ 2, 6 See also Or. Rev. Stat. § 291.216(2) (1991)
Pennsylvania	C	Pa. Const. art. 8, §§ 12(a), 13(a)
Rhode Island	S	R.I. Gen. Laws tit. 35, ch. 3 (1990 & Supp. 1991)
South Carolina	C	S.C. Const. art. 10, § 7(a) See also S.C. Const. art. 3, § 36, S.C. Code Ann. §§ 11-11-70(B), 11-11-310 (Law. Co-op. Supp. 1992)
South Dakota	C	S.D. Const. art. XI, § 1 See also S.D. Codified Laws Ann. § 4-7-10 (1985)
Tennessee	C	Tenn. Const. art. 2, § 24 See also Tenn. Code Ann. §§ 9-6-101, 9-6-106 (1992)
Texas	C	Tex. Const. art. 3, §§ 49a, 49-g, art. 8, § 22
Utah	C	Utah Const. art. 13, §§ 2(11), 9 See also Utah Code Ann. § 63-38-2 (Supp. 1992)
Vermont	N/A	Vermont has no explicit balanced budget requirements although several statutory provisions indicate that a balanced budget is contemplated, see Vt. Stat. Ann. tit. 32, §§ 202, 307, 308 (1981 & Supp. 1991)
Virginia	C	Va. Const. art. 10, §§ 7, 8
Washington	S	Wash. Rev. Code Ann. ch. 43.88 (1983 & Supp. 1992)

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State	Type of requirement	Citations
West Virginia	C	W.Va. Const. art. 6, § 51, art. 10, § 5
Wisconsin	C	Wis. Const. art. 8, § 5 See also Wis. Stat. Ann. §§ 16.45, 16.46(4) (West 1986 & Supp. 1992)
Wyoming	N/A	Wyoming has no explicit balanced budget requirements but see Wyo. Stat. §§ 9-2-1005, 9-2-1012 (1991 & Supp. 1992)

Legend: C = Constitutional S = Statutory N/A = Not applicable

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