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*Economic woes hit state budgets*

*Soaring inflation and shrinking tax revenues will make it tougher for at least 25 states to fund public services.*

*By Peter Grier*

Washington - In Nevada, Gov. Jim Gibbons told legislators on March 31 that the state's budget shortfall could reach \$900 million by the middle of next year – and that he wants spending cuts beyond the 4.5 percent cutbacks he ordered in January.

In Florida, state leaders say they are facing a series of budget shortfalls unprecedented in modern history. They're considering using up as much as \$1.7 billion in revenue reserves to plug spending gaps in coming months.

In Maryland, the General Assembly last fall raised taxes by \$1.4 billion a year at Governor Martin O'Malley's urging. His job approval rating has now fallen below 40 percent.

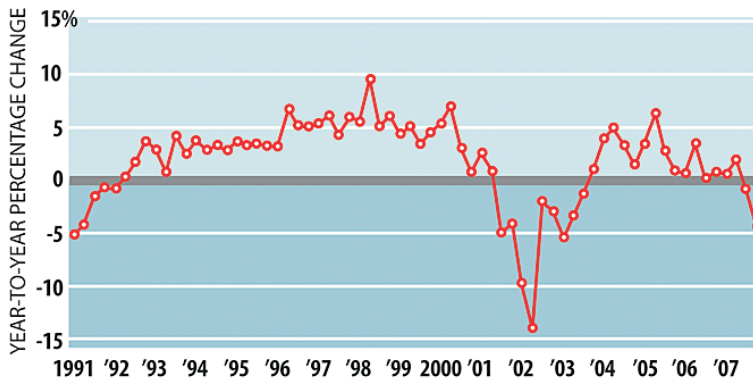
Across the United States, soaring inflation and shrinking tax revenues have combined to place state budgets under severe stress.

This fiscal year is tight, and the next one promises to be even tighter. At least 25 states will be in the red for fiscal 2009, which begins this coming July for many. The combined shortfall is expected to total at least \$39 billion, according to figures compiled by the Center on Budget and Policy Priorities.

**“The result may be a squeeze on states’ ability to fund services,” said Robert Ward, deputy director of the State University of New York’s Rockefeller Institute of Government in a report on state budgets released March 31.**

**The ups and downs of state tax revenues**

In the last quarter of 2007, tax revenues collected by states (adjusted for tax cuts and inflation) decreased by 4.3 percent, the lowest rate since January-March 2003.



*SOURCE: Individual state data analysis from the Rockefeller Institute of Government with legislated tax changes by the National Conference of State Legislatures and inflation data from the US Bureau of Labor Statistics.*

The causes of state budget problems are easy to spot with even a cursory glance at the business section of a newspaper.

Falling home prices are causing consumers to curb spending, which in turn reduces state sales tax revenues. Unemployment is rising, and income is flat or declining – resulting in state income tax revenues that are not as high as once projected.

**With the effects of inflation and enacted tax changes added to this mix, combined state tax revenues decreased by 4.3 percent in the fourth quarter of fiscal 2007, according to figures compiled by the Rockefeller Institute.**

Meanwhile, the cost of the items states spend their money on is rising at a rate greater than that of overall national inflation. State and local government inflation rose 6.2 percent for fiscal 2007, with jumps in fuel and healthcare and pension costs big contributors.

**“States are experiencing a classic nutcracker effect: costs are rising sharply just as revenues falter,” said Mr. Ward.**

Among the states where revenues dropped significantly were Oregon, Florida, West Virginia, Mississippi, Arizona, and Nevada, according to the Rockefeller survey.

Kentucky, Oklahoma, Tennessee, North Carolina, Wyoming, Delaware, and Wisconsin showed smaller declines.

Meanwhile, some mineral and petroleum-rich states showed revenue increases. These included Alaska, Colorado, and Texas.

Given the unpredictable nature of the course of the national economy and the course of action Washington may pursue in attempting to jump-start it, predicting the status of future state budgets is fraught with uncertainty, notes the Rockefeller Institute report.

“One apparently safe prediction: [It will be] a very difficult year for state budget makers,” it concludes.

Of course, those budget makers may be used to trouble by now. Though a booming economy eased

some of their problems in recent years, overall, many states have never recovered from the fiscal crisis of the early part of the decade.

The recession of 2001 was a difficult one in many state capitals. State expenditures fell sharply – and for all states combined, today they remain below the level of 2001, when inflation is taken into account, according to a report by the Center on Budget and Policy Priorities (CBPP).

And budget problems can be more severe for states than the federal government. By law many cannot run a deficit as Washington can.

Among the budget cuts that have been made or proposed, according to a roundup compiled by CBPP, are reductions in public health programs. In California, for instance, Gov. Arnold Schwarzenegger has proposed making some families pay more for the State Children’s Health Insurance Program.

At least eight states are proposing to cut K-12 education, according to the CBPP roundup. Arizona may eliminate childcare subsidies for some low-income working families.

Meanwhile, eight states – including Florida, Kentucky, and Virginia – either have already reduced or may soon reduce funds for public higher education.

Tax hikes are another means of dealing with red ink. But as the experience of Governor O’Malley shows, they can be very unpopular.

The \$1.37 billion in tax increases approved by Maryland’s General Assembly last year is already facing a significant alteration: Fierce industry reaction to a surcharge on computer services has led to the consideration of a proposed tax on millionaires to replace the computer levy.

Michigan also passed a broad tax increase in late 2007. Other states considering revenue enhancements include Kentucky, where the governor has proposed raising the tobacco tax.

*Material from the Associated Press was used in this report.*