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Governor Romney's FY04 Budget: Does it Keep the Promise?

Despite the fanfare that accompanied Governor Romney's release of his proposed FY04 budget (commonly known as "House One"), a close look at the document suggests that there is little cause for celebration. While some of the proposals to reorganize government agencies and streamline the delivery of services are admirable, the budget ultimately does not deliver on Governor Romney's campaign promise to provide an FY04 spending plan that preserves essential services without raising taxes. In fact, the budget does rely on new revenue, includes severe cuts to a variety of important programs, and passes on the responsibility for making hard choices to local governments, which will be forced to cut education and public safety programs.

Equally troubling is the plan's reliance on one-time revenue and questionable assumptions (e.g., a plan to raise $75 million in exchange for a promise that the state will not open casinos). Because this budget does not seriously address the root cause of the state's fiscal woes — the loss of a significant portion of the tax revenue base through the passage of unaffordable tax cuts during the 1990s — it merely prolongs the fiscal crisis, affecting in particular children, the elderly, and other vulnerable populations.

Also problematic is the lack of information in the budget document. For instance, although we are informed that administrative restructuring will save $233 million, there is no data detailing prior year expenses that would back up this claim. Likewise, while it may well be desirable to remove earmarking language from appropriations, the Governor has gone further, eliminating nearly all language from each line item. This makes it difficult, if not impossible, for the ordinary citizen to understand the purpose of individual expenditures.

Similarly, although the Governor's proposed reorganization of agencies is not as sweeping a change as has been suggested (most agencies persist in their original form, but with new names and organized into new clusters), the consolidation and transfer of budget accounts

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makes it difficult to compare this proposal to the FY03 budget. In what follows, we take a look at the numbers underlying House One, describe the reorganization of programs, and provide a preliminary overview of spending changes in each budget area. Subsequent issues of the MBPC Budget Monitor will address the effect of the Governor's spending proposal on particular spending areas such as education and health care.

Table 1

FY04 Projected Revenue

FY03 tax revenue (proj)	**14,648.0**
FY04 revenue growth	175.8
One-time FY03 revenue	-145.0
Transfer to MBTA	-683.0
Projected FY04 tax revenue	**13,995.8**
Other revenue	8,123.8
Total FY04 revenue	**22,119.6**

A Closer Look at the Numbers

Governor Romney has pegged the FY04 budget deficit at over $3 billion dollars, and that figure has been echoed in press reports of the fiscal crisis, although the assumptions underlying the projection have never been made clear. However, since the current FY03 budget incorporates cuts that were made during FY02, nearly $1 billion in cuts made in the course of writing the initial FY03 budget, and additional cuts implemented by the Governor during the fiscal year, there is little doubt that the gap between expected revenue and historic spending trends will be $3 billion in FY04.

Revenue

Table 1 shows the Massachusetts Budget and Policy Center's estimate of FY04 revenue. This estimate starts with the current projected FY03 tax revenue total of $14.65 billion and uses the administration's conservative assumption that FY04 baseline tax revenue growth (increases in revenue before adjusting for changes in law) will be 1.2 percent. After adjusting for the fact that a portion of the revenue raised by last year's tax package was non-recurring, as well as the transfer of a portion of sales tax revenue to the MBTA, projected FY04 tax revenue totals $14 billion.

Other forms of revenue, chiefly federal reimbursements for Medicaid, as well as fee and lottery revenue add $8.12 billion, bringing total projected revenue available for use in the budget to $22.12 billion.

Projected Deficit

Given this projected revenue figure, the size of the deficit depends on assumptions concerning spending in FY04. Table 2 uses two sets of assumptions to delineate the parameters of the FY04 problem. The first spending projection is an austere one that starts from current FY03 spending projections, a level that incorporates some $2 billion in cuts made over the past year and a half. It then uses current estimates for mandatory expenditures that are driven by external forces, such as the rate of medical inflation or formulas that determine spending, as in the case of payments to the pension fund or debt service. It assumes that all other areas of the budget grow at a rate necessary to maintain current levels of service without any expansion of programs. Under this set of assumptions the deficit is $2.4 billion.

The second projection starts from the above total, but also assumes the restoration of about $650 million of the cuts included in the FY02 and FY03 budgets or implemented by the Governor during the course of the fiscal year. This figure represents only about one-third of the entire amount cut during the past year and a half, but it would allow restoration of health benefits to long-term unemployed individuals scheduled to lose them next month, as well as restoration of AIDS and other disease prevention programs, and food stamps for immigrants. Under these assumptions, the projected FY04 deficit would rise to $3.1 billion.

Table 2

FY04 Deficit Range	
Total FY04 revenue	22,119.6
FY04 Baseline budget (after all cuts)	24,554.9
FY04 historic baseline budget	25,204.9
FY04 Deficit Range	-2,435.3 -3,085.3

Filling the Gap

The Governor's budget proposal relies on a mixture of revenue solutions, cuts, and one-time fixes intended to save money. On the revenue side, the proposed solutions break down into a few basic categories:

New Revenue Sources ($664 million)

- **Closing Loopholes:** The budget assumes an increase in tax revenue of $166 million. The bulk of that figure – $128 million – is attributable to legislation designed to close a variety of corporate tax loopholes that the Governor initially proposed in January, and the legislature approved in the last week of February, to address the FY03 budget shortfall. The legislation would deny corporations a tax deduction for any royalty payments they make to related subsidiaries and thus would curb the use of passive investment corporations for tax avoidance purposes. In addition, the legislation would clarify current law to ensure that financial institutions and other corporations pay taxes on dividends they receive from real estate investment trusts, and that businesses organized as Subchapter S corporations continue to pay a tax surcharge on receipts that exceed $6 million.
- **Fees:** House One also assumes $339 in new fee revenue, the result of a wide range of fee increases. The bulk of this amount ($230 million) would come from fee increases at the Registry of Deeds, while an additional $59 million would be collected by a wide variety of state agencies (e.g., a $10 dollar fee for a certificate of blindness would be imposed at the Commission for the Blind). Finally, higher education fee increases would produce an additional $50 million in new revenue.
- **Federal Revenue Maximization:** The budget assumes that $159 million will be gained via a plans to bring in additional federal Medicaid reimbursements.

One-time Accounting Changes ($647 million)

- The budget proposes the transfer of state property worth $180 million to make up for a proposed reduction in pension funding of the same amount. The plan also assumes that $30 million will be raised from the sale of other state property.
- In addition, the plan relies on the one-time use of turnpike reserves and refinancing of turnpike debt for $191 million.
- The budget plan taps reserves and other funds that would otherwise be set aside (mainly tobacco settlement revenue). While use of some of these funds may be

appropriate in a time of fiscal crisis, they do not provide a solution to the state's long-term structural problem.

Other Solutions ($116 million)

Finally, the budget relies on two other techniques designed to produce new revenue, although it is unclear whether they will actually do so.

- A plan to get new revenue from neighboring states in exchange for a promise not to open casinos in Massachusetts would produce an estimated $75 million.
- Collecting fees for legal representation by public defenders would, according to budget estimates, raise $41 million.

It is important to recognize that even if all these solutions produced revenue in accordance with the estimates, they would still fail to fill the projected deficit. Moreover, to the extent that these solutions rely on one-time solutions instead of restoring a stable tax base, they fail to address the root causes of the fiscal crisis. If this budget should pass, we will continue to face new deficits in coming years.

A Closer Look at Spending

The solutions discussed above fail to close the FY04 deficit, leaving a gap of at least $1 billion (measured against an FY04 baseline budget that does not restore previous cuts). Thus, to achieve balance the Governor's budget plan must also rely on substantial spending cuts, on top of the $2 billion in cuts over the past two years. While the administration believes that it can reduce the impact of new cuts by achieving some $233 million in savings through reorganization of state agencies, other analysts, including the chairman of the House Ways and Means Committee, estimate such savings at closer to $100 million, leaving at least $900 million in actual program cuts. The budget also identifies about $540 million in health care and management "reforms" that will reduce state costs. For the most part, these proposals, including tighter eligibility and co-pays for Medicaid and reductions in compensation for state employees, are simply cuts under another name.

Table 3

Filling the FY04 Gap

Total FY04 revenue	**22,119.6**
FY04 Baseline budget (after cuts)	**24,554.9**
FY04 Deficit	**-2,435.3**
New revenue sources	664.0
One-time fixes	647.0
Other solutions	116.0
Proposed restructuring	100.0
Remaining Cuts	**-908.3**

Looking at the spending proposals contained in House One points to the gravity of the state's fiscal problems. With appropriations totaling $22.89 million, the FY04 budget barely increases, rising by less than half a percent over projected final FY03 spending (including supplemental appropriations that will be necessary to pay for additional Medicaid costs and snow and ice removal bills). Because projected Medicaid costs and required spending on the state debt will require new spending of $700 million in FY04, other programs are cut proportionately. The chart on page five shows proposed spending on state agencies (as they have been restructured), comparing the recommendations to expenditures on equivalent budget accounts in the FY03 budget

HOUSE ONE: PROPOSED FY04 SPENDING

	FY03 initial	FY03 current	FY04 prop	Change from initial FY03	
Judiciary					
Judiciary	545,483,056	545,483,056	543,970,266	-1,512,790	-0.3%
Attorny Gen, DAs	108,517,996	108,517,996	111,131,577	2,613,581	2.4%
Administrative Costs					
Pensions	814,048,766	814,048,766	668,835,000	-145,213,766	-17.8%
Debt Service	1,492,517,156	1,492,517,156	1,593,393,156	100,876,000	6.8%
Contract Asst	108,517,751	108,377,751	261,140,270	152,622,519	140.6%
Employee Hlth Ins	794,862,213	766,037,990	765,880,743	-28,981,470	-3.6%
Other Admin	528,874,474	479,405,394	512,824,552	-16,049,922	-3.0%
Unrestricted Local Aid					
Local Aid (non-ed)	1,236,358,431	1,121,969,856	886,940,966	-349,417,465	-28.3%
Exec. Office for Commonwealth Development					
Executive	497,715	197,715	882,986	385,271	77.4%
Housing	95,695,874	82,429,439	74,069,597	-21,626,277	-22.6%
Environment	200,325,116	183,772,042	180,538,084	-19,787,032	-9.9%
Transportation	109,940,311	106,264,715	158,339,527	48,399,216	44.0%
Executive Office for Health & Human Services					
Executive	507,123,504	504,694,407	567,709,162	60,585,658	11.9%
Veterans	23,002,434	22,090,505	20,421,264	-2,581,170	-11.2%
Elder Affairs	192,215,581	191,920,612	185,004,989	-7,210,592	-3.8%
Medical Asst.	5,692,807,023	5,608,822,472	6,211,520,000	518,712,977	9.1%
Public Health	409,819,792	381,211,231	364,443,159	-45,376,633	-11.1%
Mental Health	567,010,968	564,547,513	551,186,027	-15,824,941	-2.8%
Disabilities	1,076,363,824	1,065,378,567	1,108,505,235	32,141,411	3.0%
Social Services	608,400,862	594,666,895	624,112,633	15,711,771	2.6%
Juv. Delinquency	114,184,743	114,184,743	122,325,964	8,141,221	7.1%
Child Care	464,720,801	445,620,801	420,007,732	-44,713,069	-9.6%
Emergency Fin. Asst.	761,227,445	737,981,303	754,785,040	-6,442,405	-0.8%
Senior Pharmacy	97,609,000	85,609,000	0	-97,609,000	-100.0%
Executive Office of Economic Affairs					
All Programs	116,849,823	114,162,577	116,003,491	-846,332	-0.7%
Executive Office for Education					
Executive	46,547,092	46,451,798	45,406,710	-1,140,382	-2.4%
Education Local Aid	3,258,969,179	3,258,969,179	3,331,892,681	72,923,502	2.2%
K-12 Education	375,589,646	357,208,106	311,547,296	-64,042,350	-17.1%
SBAB Debt Service	$361,596,898	361,596,898	388,418,282	26,821,384	7.4%
Higher Education	1,019,577,697	997,676,969	734,803,991	-284,773,706	-27.9%
Executive Office for Public Safety					
All Public Saf. Prog.	1,217,755,918	1,213,321,676	1,255,930,591	38,174,673	3.1%
Other Expenditures					
Capital Projects	23,000,000	15,500,000	0	-23,000,000	-100.0%
Uncomp Care Pool	72,000,000	72,000,000	30,000,000	-42,000,000	-58.3%

(the chart provides both initial FY03 spending data and figures adjusted to reflect cuts implemented so far this year).

Highlights of the spending proposal include:

Local Aid

Currently, the main components of local aid are Chapter 70 education aid, lottery aid, and, in the case of some cities and towns, a category of aid known as Additional Assistance. While there are some other forms of aid to cities and towns that are restricted to specific uses, such as School Building Assistance payments, these three account for almost 90 percent of all local aid distributed by the state. Excluding education aid, which is discussed below, Additional Assistance and Lottery distributions were set at $1.24 billion in the initial FY03 budget.

In January, Governor Romney cut Additional Assistance by about nine percent from its level of $446.6 million in the FY03 budget, and now his budget proposal simply eliminates this form of local aid. The budget would cut lottery distributions from $778.1 million in the initial FY03 budget to $419.0 million, repeating a technique employed during the last fiscal crisis, when aid distributions from the lottery (which was originally set up as a source of local aid) were capped and revenue was diverted into state coffers.

To counter these cuts, the Governor proposes a substantial ($162.9 million) increase in payments that towns with state-owned land receive in lieu of property taxes (PILOT payments) and one-time "transitional local aid mitigation" payments that total $293.3 million. The end result is a total cut in non-education local aid of $349.4 million, the largest single cut in the budget. Different communities rely on local aid to varying extents, but it is safe to say that these cuts will have a substantial impact on local budgets, requiring either property tax increases, cuts in spending on schools and public safety, or both.

K-12 Education

The proposed reorganization of state government includes a plan to establish an Executive Office for Education, which would oversee both K-12 and higher education programs. The budget does not include an estimate of the cost savings resulting from this change; a comparison to equivalent accounts in the FY03 budget shows a slight cut ($1.1 million).

Local education aid (Chapter 70) comprises the bulk of spending on K-12 education, and is intended to ensure that cities and towns will have the resources to provide an adequate education to all children (defined as a "foundation budget"), regardless of a given town's wealth or other resources. The proposed budget would increase Chapter 70 aid by $73 million; an amount sufficent to cover the cost of projected enrollments and inflation.

Balancing this modest increase is a substantial cut to other K-12 education spending, including the elimination of early literacy, full-day kindergarten, and class size reduction programs, a steep cut in funding for regional school transportation, and the transfer (without adequate funding) of the state's early education program for three to five year olds. Combined with the cuts to non-education local aid discussed above, which will put heavy pressure on local government budgets, it is clear that the progress made since the passage of Education Reform in 1993 will be gravely threatened.

Higher Education

When it comes to spending on higher education, the budget assumes a fairly radical reorganization of higher education that will decentralize the state's university and college system and, it seems, require each institution to assume greater responsibility for its finances. The overall cut to higher education programs in the budget is $285 million, but this will be balanced by provisions allowing institutions to retain tuition, resulting in a net cut of $156 million.

Health and Human Services

The proposed reorganization plan would group human services programs into four departments, Elder and Veteran, Health Services (Medicaid, Public Health, Mental Health), Disabilities and Community Services (Mental Retardation and a variety of smaller programs serving blind, deaf,and physically disabled individuals), and Children, Youth and Family Services (the equivalent of the current Departments of Social Services, Youth Services, and Transitional Assistance, as well as the Office for Child Care Services). While it is not yet clear how much of the proposed cuts to health and human services can be accounted for by savings realized through reorganization, it is quite evident that the budget includes cuts to vital services. These include:

- The planned elimination of the model Senior Pharmacy program that provides drug benefits for the elderly. The administration says it will reinstate the program only if the state receives federal assistance in paying for it.

- Proposed co-pays and premiums for Medicaid patients, along with tighter eligibility standards, will lead to the loss of health coverage by low-income families and individuals. The Governor also fails to make good on his promise to restore coverage for long-term unemployed adults who are scheduled to lose health care next month.

- While funding for child care programs that serve welfare recipients and low-income families appears to rise, the increase is illusory. After accounting for the consolidation of an early education program for three to five year olds with these programs, total spending on child care drops by $44.7 million, nearly ten percent. At the same time, more stringent work requirements for welfare recipients will increase the demand on these programs.

- The budget appears to rely on savings that will be realized by requiring parents of two to five year olds who receive TAFDC to work. At the same time, funding for education and training programs is cut to just under $12 million, although this amount will be supplemented by the one-time use of $6 million in federal funds. Even so, these programs have been cut by about $18 million since FY02.

- Spending on a variety of prevention programs, including smoking cessation and a home visiting program for teenage mothers, is cut sharply.

The Environment

Overall funding for environmental programs declines by about $20 million compared to the initial FY03 level; among the programs affected, according to environmental advocates, is the state's Riverways program that helps protect state rivers and streams. Also problematic is the transfer of numerous environmental funds to the state's general budget fund; this change will make it difficult, if not impossible, to know whether funding streams dedicated to environmental uses (e.g. revenue from unclaimed bottle deposits) are being spent for their intended purpose.

Housing

After years of reductions there is not much left to cut in this area. Neverthless, the Governor cuts public housing subsidies by $4.5 million from the initial FY03 level; it appears that this cut will be at least partly balanced by an increase in minimum rents that must be paid by public housing tenants. The budget also eliminates funding for the Affordable Housing Trust fund.