

# Reality Check

## Governor's 2012-2014 Budget Ignores Current Needs

By Sara Okos and Michael J. Cassidy

In his effort to balance the state's budget and close major funding gaps, Governor McDonnell has presented legislators with a budget that ignores the reality of growing need, shifts obligations to others, hides real cuts in education funding and will cost Virginia jobs.

Instead of reforming, reallocating and reinvesting in the programs that make government more efficient, effective and accountable, the Governor's proposal strikes at – and cuts – the core services that Virginians rely on every day while at the same time widening tax loopholes that drain yet more resources from the state.

- The Governor's budget proposes over \$880 million in cuts to services in order to close the budget shortfall he faced and to make room for his new initiatives.
- Over 90% of the cuts in the proposed budget are in the areas of education and health care.
- The Governor's budget shifts the state's growing cost of providing services like education and health care to localities, health care providers, and consumers.
- The Governor's budget substantially underfunds K-12 education with a real new increase in education funding of less than 1 percent.
- The Governor's budget widens unproven loopholes in the state's tax code by expanding existing tax preferences and creating new ones with little to no evidence of their effectiveness.

In order to improve his proposal, lawmakers and advocates need to give the Governor's proposal a reality check.

### Reality Check: Declining Revenue, Declining Spending

**General Fund Resources:** Despite a nominal uptick in state general fund revenue levels, state revenue collections as a share of personal income are projected to remain well below pre-recession levels through the next biennium. Between FY2003 and FY2007, the period of economic expansion following the previous recession, Virginia's general fund revenues as a share of state personal income averaged roughly 4.65 percent. Yet looking at FY2013 and FY2014, general fund revenues are expected to represent just 4.16 percent of state personal income (see Figure 1). Since the onset of the downturn in 2007, state personal income has increased roughly three times as fast as general fund revenues.

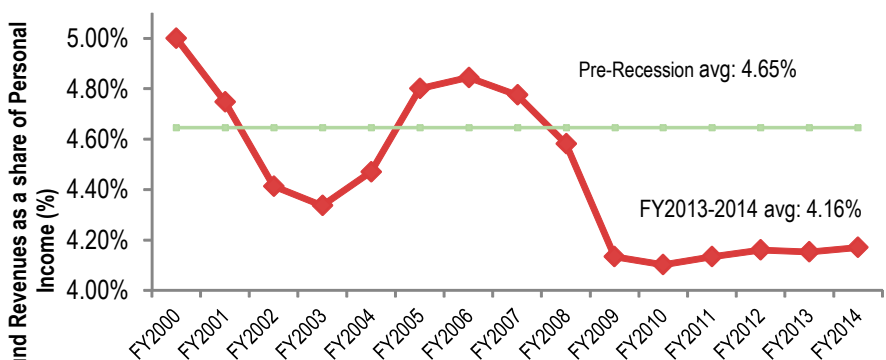
**General Fund Spending:** While the Governor asserts state spending has increased by 23 percent in recent years, his explanation is incomplete. Virginia's general fund spending actually declined by five percent over the past

decade, adjusting for inflation and population growth. It is only when we factor in growth from the other piece of Virginia's budget – the state's non-general fund – that we see positive total budget growth of about 23 percent over the past decade. But the revenues that drive these two parts of the budget are very different, and understanding the difference is important to unpacking what these trends in the state budget actually reveal about our priorities.

General fund revenues are made up largely by sales tax, and individual and corporate income taxes. Non-general fund revenues are made up of items such as money from the federal government and college tuition payments from students and parents. Over 30 percent of the recent growth in non-general funds was driven by increases in federal funds to the state. Federal Recovery Act funds, for example, helped Virginia cope with the Great Recession and its effect on state revenues. Federal matching funds for our state's Medicaid program, which has seen significant increases in enrollment due to the recession, are

### Revenues Remain Below Pre-Recession Levels

Figure 1: General Fund Revenues as a Share of State Personal Income, FY2000-FY2014



Note: General fund revenues exclude transfers. FY2012-2014 revenues and personal income growth projections come from GACRE November 2011 forecast.

Source: BEA and Virginia Secretary of Finance.



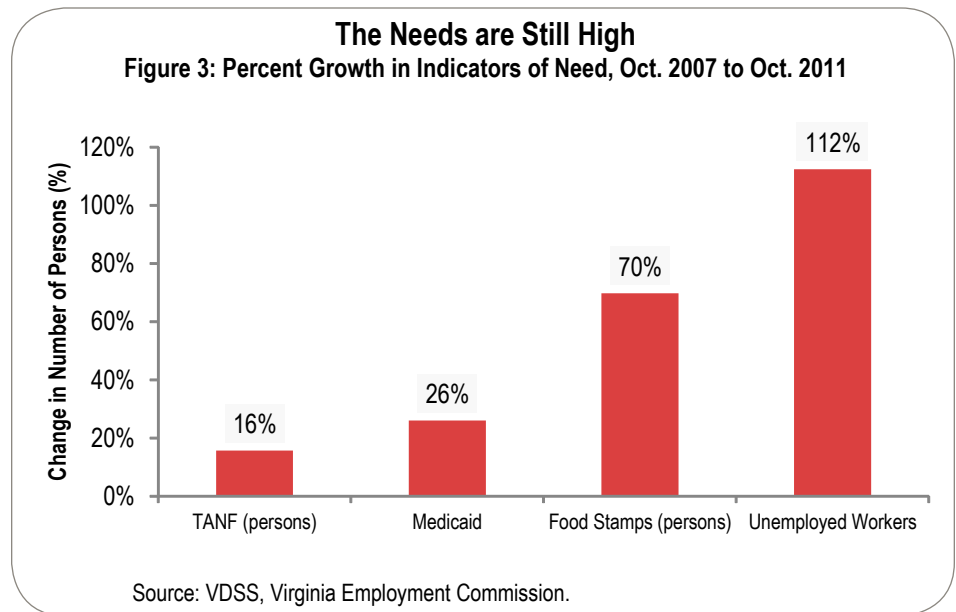
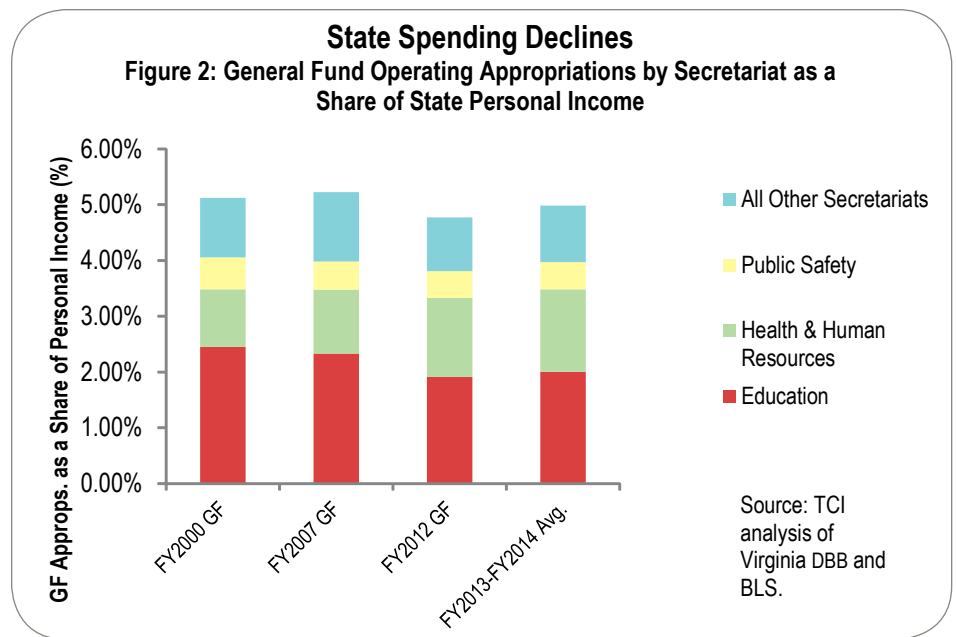
also included in this category. Another key piece of the growth in non-general funds is the result of increases in tuition payments to our state's colleges and universities. Tuition to state colleges and universities is counted as non-general fund revenue in our state's budget. Requiring our students to pay more for college does not signify any meaningful increase in public investment.

Another way of looking at state spending is to compare it to total state personal income over time. As shown in Figure 2, the state general fund operating budget as a share of personal income has fallen both since the start of the past decade (FY2000) and the start of the recession (FY2007). In FY2007, general fund spending represented about 5.23 percent of total state personal income. The spending levels included in the Governor's 2012-2014 budget proposal make up about 4.98 percent of projected personal income levels over the next biennium.

When we break down that 4.98 percent of personal income by spending area, we see that education has been the hardest hit. Investment in education has fallen from 2.33 percent of personal income in FY2007 to roughly 2 percent of personal income across the 2012-2014 biennium. Investment in public safety, another key general fund budget driver, also declined slightly since the start of the recession.

### Reality Check: Increasing Need

On top of declining revenue and declining funding, Virginia faces increasing costs of providing services to a growing population. Since 2007, we have seen unemployment levels rise by nearly 130,000 Virginians. Medicaid enrollment in 2014 is projected to come in about 40 percent higher than in 2006-2007. Student enrollment in K-12 education will continue to increase so that over the 2006-2014 period, the number of Virginia students in our schools will grow over 3 percent.



In addition, the ongoing sluggishness of Virginia's economic recovery means we also will face continued high demand for programs designed to keep struggling families afloat. And despite modest upticks in revenue collections, we cannot ignore the fact that revenues are not bouncing back to the level required to support Virginian's ongoing high needs. Food stamp participation and Medicaid enrollment are hovering near their highest levels since the recession began, up roughly 70 percent and 26 percent, respectively. And, as shown in Figure 3, the number

of unemployed workers in the state is still up 112 percent since the start of the recession, and TANF reciprocity is up 16 percent. Until Virginia can make substantial progress in reducing the unemployment rate, Virginians are going to continue to look to these and other public programs to help make ends meet and stay afloat.

### Reality Check: Investments Lagging

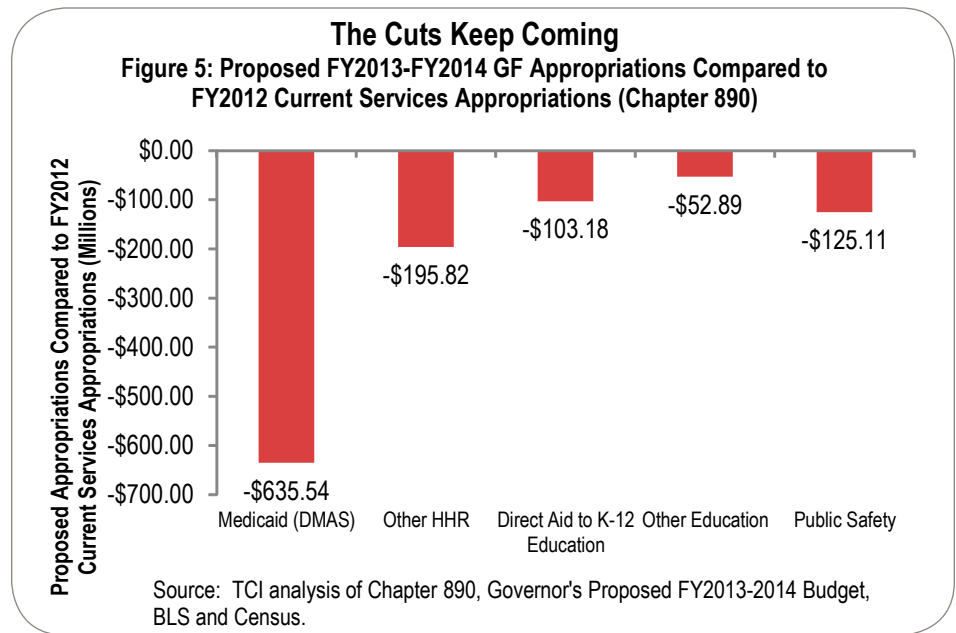
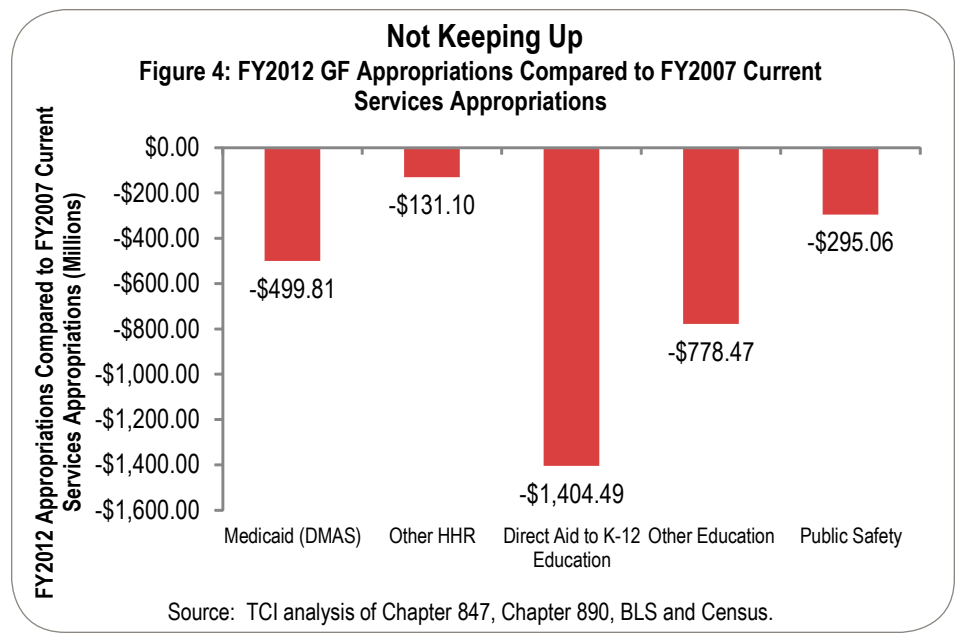
In order to make sense of the Governor's proposed spending levels going forward, it's important to understand Virginia's budget in the context of

“current services” spending, which adjusts spending for growth in inflation and population. Using this method to compare current spending to pre-recession spending shows that current spending is substantially lower than pre-recession spending. As shown in Figure 4, all of the state’s key general fund investments – health care, education, and public safety – have experienced cuts on this current services basis. That means if we had continued the pre-recession level of state investment in K-12 education, for example, current appropriation levels would fall over \$1.4 billion short, given rising costs and rising student enrollment. In terms of Medicaid, current investment falls almost \$500 million below FY2007 levels, adjusted for inflation and enrollment growth.

Yet when we reset the current services baseline spending from 2007 to 2012 and look ahead to the spending levels proposed by Governor McDonnell for FY2013 and FY2014, new cuts appear. Proposed general fund support for health care, education, and public safety fall even further behind FY2012 spending levels. Across the biennium, investment in Medicaid (DMAS) will fall over \$635 million below FY2012 levels, adjusted for rising enrollment and cost expectations. Figure 5 shows these adjusted cuts across the biennium by spending area and the years of systematic disinvestment and underfunding of the core functions of government as identified by Governor McDonnell.

## Conclusion

Though the Governor has proposed a budget that balances, suggesting that Virginia has reached some equilibrium between revenues and expenditures, the reality is more complex. Rather than take a balanced approach, one that includes new revenue, the Governor’s proposal cuts and disinvests in the core functions of government and in the



economic health and vitality of Virginia. In addition, rather than making gains in transparency and efficiency, Governor McDonnell’s budget hides important details, and as the cuts from his budget translate into layoffs and lost jobs, the economic impact will be felt broadly across the Commonwealth.

## Endnotes

1 See the 2011 update of the Joint Legislative Audit and Review Commission’s (JLARC) “Review of State Spending,” <http://jlarc.virginia.gov/meetings/October11/Spend11.pdf>.

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