Summary: Fall 2021 Fiscal Survey of States

December 17, 2021

State Budget Growth Reflects Improved Fiscal Conditions and One-Time Factors

Budgets for fiscal 2022 were enacted in most states in the spring of 2021, when state revenue forecasts were continuing to improve and many states were projecting considerable end-of-year surpluses for fiscal 2021. In this environment, states adopted budgets calling for the largest annual percentage increase in general fund spending since fiscal 2007. This increase follows moderate general fund spending growth and a sharp increase in revenues for fiscal 2021.

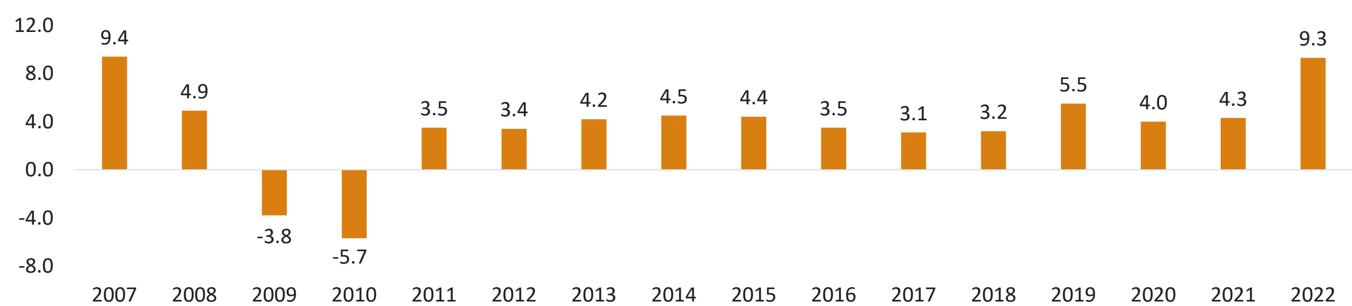
A number of unique, one-time factors contributed to the large projected general fund spending increase in states' fiscal 2022 enacted budgets. Similarly, the sharp uptick in general fund revenues in fiscal 2021 is partially attributable to the impact of the tax deadline shift on when revenues in some states were recognized, a lower baseline in fiscal 2020 due to the pandemic's economic effects on revenues in that year, and the inclusion of federal funds, borrowing and other sources in at least a few states.

One-time factors aside, this survey shows a marked improvement in state fiscal conditions compared to expectations when states enacted their original budgets for fiscal 2021, which projected general fund spending and revenue to decline year-over-year. State budgets did not fare as badly as was expected earlier in the pandemic for several reasons. Federal stimulus measures and the fact that higher-income earners were relatively insulated from the pandemic's impacts helped mitigate state income tax losses. Meanwhile, sales tax collections during the pandemic were helped by the recent enabling of expanded online sales tax collections along with the fact that the pandemic mostly curtailed consumption of services – which are less often included in states' sales tax bases.

Examining changes in balance levels provides another look at how much the state fiscal outlook has improved over the last year. In fiscal 2020, some states turned to their rainy day funds to close pandemic-related budget shortfalls, and reserves recorded a decline. However, stronger than anticipated revenue growth in fiscal 2021 led rainy day funds to rise to a new record

Figure 1.

Annual General Fund Spending Changes, Fiscal 2007 To Fiscal 2022 (Percentage Change)



Note: Fiscal 2022 figure is based on states' enacted budgets.

level by year-end. Similarly, total balance levels – rainy day funds combined with general fund ending balances – saw a sharp uptick in fiscal 2021, nearly doubling from fiscal 2020 levels, due mostly to revenues exceeding expectations when spending levels were first adopted. States are expected to spend down a portion of these unanticipated budget surpluses in fiscal 2022.

Fiscal 2022 Enacted Budgets Show Largest Spending Increase Since Fiscal 2007

General fund spending is projected to total $1.018 trillion in fiscal 2022 enacted budgets, a 9.3 percent increase over fiscal 2021 levels – the highest annual growth rate since fiscal 2007. This increase is driven by a number of factors, including one-time spending from surplus funds, a shift in reliance on federal funds to general funds in some program areas, a lower baseline in fiscal 2021 due to spending reductions in some states (that in some cases were restored in fiscal 2022), state funding for pandemic response efforts, and the inclusion of COVID-related federal aid in limited instances. General fund spending growth rates also vary considerably by state, reflecting the uneven impacts of COVID-19 on state economies and budgets, differences in timing of state expenditures within a given fiscal year, and states' varying use of federal funds. The high growth rate is also driven by significant increases in a few large states; for this reason, the median general fund spending growth rate for fiscal 2022, at 6.1 percent, is considerably lower than the total.

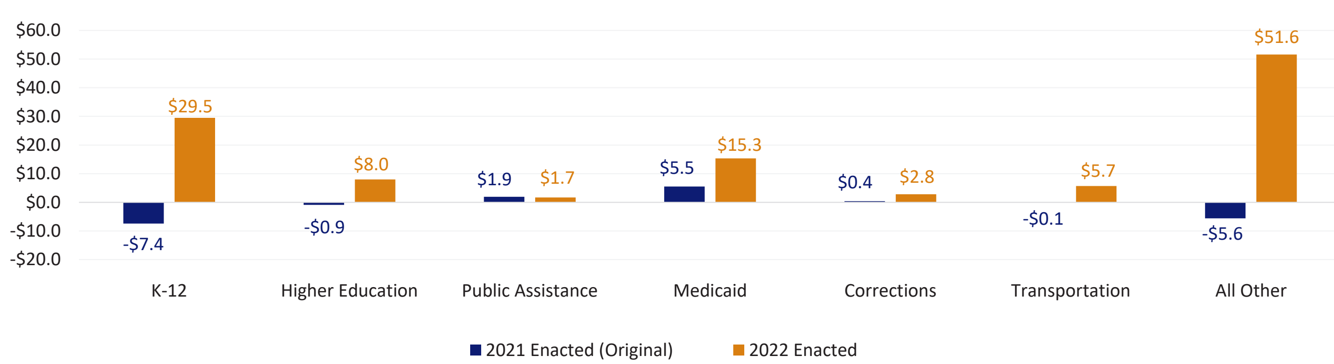
Meanwhile, this report shows that general fund spending grew moderately by 4.3 percent in fiscal 2021 to total $931.7 billion. This contrasts with states' originally enacted budgets for fiscal 2021, which called for aggregate general fund spending to decline for the first time since fiscal 2010, based on data reported one year ago in NASBO's *Fall 2020 Fiscal Survey*. While state budgets have not fared as badly as was expected earlier on in the pandemic, most states still reported general fund spending levels in fiscal 2021 below what governors proposed to spend prior to the onset of the COVID-19 crisis. Once again, the median spending growth rate for fiscal 2021 is lower, at 2.0 percent.

Enacted Budgets for Fiscal 2022 Call for Net Increases in All Program Areas Following Budget Cuts in Fiscal 2021

Enacted general fund budgets for fiscal 2022 call for $114.5 billion in increases over fiscal 2021 enacted appropriation levels. While this figure is larger than typically observed, it is also a reflection that some states' enacted budgets for fiscal 2021 (the baseline year used here) were considerably reduced. (See **Figure 2.**) Moreover, appropriation increases for fiscal 2022 also reflect a shift from reliance on federal funds for certain expenditures to a greater reliance on general funds. It should also be noted

Figure 2.

General Fund Appropriation Changes By Program Area (In Billions)*



*Fiscal 2022 enacted spending changes are compared to enacted appropriation levels for fiscal 2021. Spending changes for fiscal 2021 are compared to enacted levels for fiscal 2020.

that sizeable appropriation increases in one large state make up a little more than half of the total net spending change reported. Compared to governors' budget proposals for fiscal 2022, enacted budgets plan for significantly more new general fund money. This is attributable largely to upward revisions in revenue forecasts from the time governors proposed budgets to when states enacted appropriations for fiscal 2022. This is especially evident in the "All Other" category, which is slated for new expenditures more than double what was proposed in governors' budgets. Much of the additional funds in this category represent spending for one-time uses supported by prior-year surpluses, including deposits into rainy day funds.

States Turn to Budget Management Strategies to Lesser Extent in Fiscal 2022

In order to manage their budgets, states employ a variety of strategies and tools, including spending reductions (across-the-board or targeted), revenue changes, personnel actions, efficiency savings, and one-time measures. While state fiscal conditions and budget outlooks have improved considerably compared to one year ago, states are still taking steps to manage their budgets and control spending levels.

During fiscal 2021 (after budget enactment), 19 states reported making targeted spending cuts, seven states reported making across-the-board cuts, 17 states imposed hiring freezes and/or eliminated vacant positions, four states imposed furloughs, two states reported salary reductions, and one state offered employees early retirement. Some states also utilized one-time measures to manage their budgets in the middle of the year, including tapping rainy day funds (12 states), other fund transfers (13 states), using prior-year fund balances (9 states), and deferring payments (4 states). Some states also reported using federal assistance to offset some eligible general fund costs related to pandemic response and relief. Overall, budget management strategies were used to a lesser extent in fiscal 2022 enacted budgets given improved state fiscal conditions. States that reported use of budget management strategies were somewhat more likely to report strategic and/or longer-term actions, such as targeted cuts (14 states), reorganizing agencies (5 states) and revenue increases (6 states). Additionally, two states reported across-the-board cuts for fiscal 2022, and ten states reported continuing hiring freezes and/or eliminating vacant positions into fiscal 2022. Outside of hiring freezes, enacted personnel actions were minimal. Only a few states turned to other, largely one-time measures to manage their budgets. (See **Figure 3.**)

In addition to reporting on which budget management strategies were used, states also reported on mid-year spending actions for fiscal 2021 in quantitative terms. Overall, 18 states reported net mid-year decreases in general fund spending for fiscal 2021, while 17 states reported increases compared to their enacted budgets. Among the 18 states that reported net mid-year cuts, just seven of these states reported these cuts were made in response to a revenue shortfall, with spending

Figure 3.

State Budget Management Strategies, Fiscal 2021 and Fiscal 2022

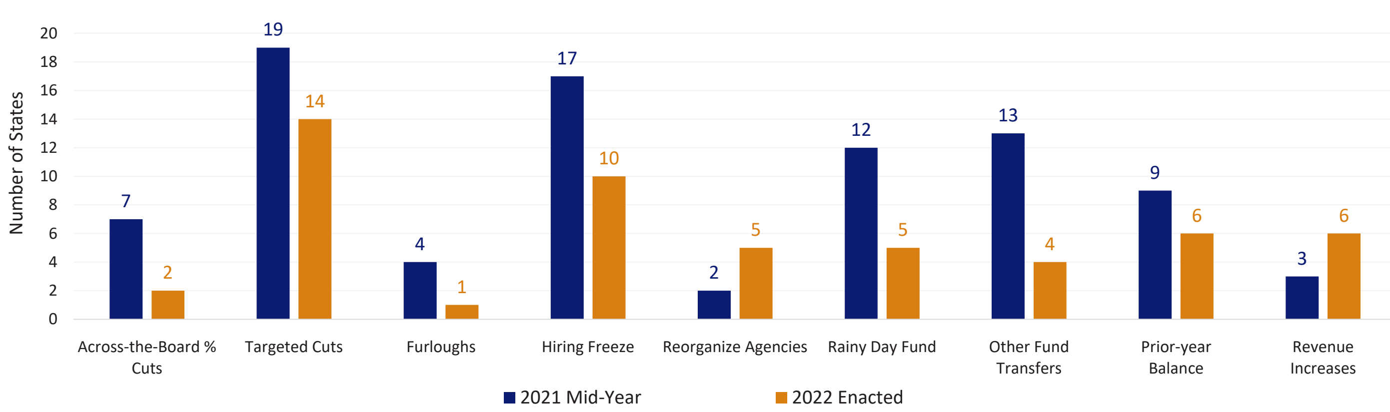
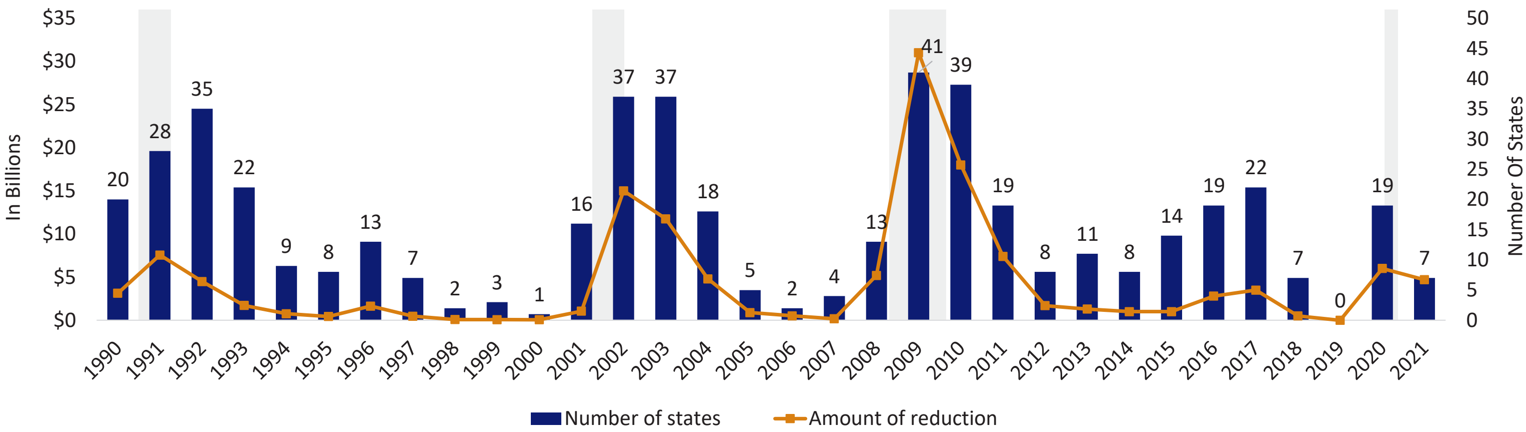


Figure 4.

Budget Cuts Made After The Budget Passed



Gray boxes denote recessionary periods, based on a July-June fiscal year calendar that most states follow. Recession dates are as follows: Early 1990s recession (July 1990 to March 1991); Early 2000s recession (March 2001 to November 2001); Great Recession (December 2007 to June 2009); COVID-19 Recession (February 2020 – April 2020).

Note: Beginning in Fiscal 2018, NASBO asked states reporting net mid-year budget reductions whether the reductions were made due, at least in part, to a revenue shortfall. Effective in FY2018 going forward, only states reporting mid-year budget cuts due to a revenue shortfall are included in the totals reported in this figure. Prior to FY2018, particularly in non-recessionary periods, states that reported mid-year cuts that were due to other reasons, such as a reduction in caseload, would have been included in the counts above.

reductions due to a shortfall totaling $4.7 billion. (See **Figure 4.**) The other states reported the reductions were attributed mostly to lower spending needs or in areas where federal assistance was able to be used in place of general funds. For the states that reported net mid-year increases in general fund spending, these incorporate enacted supplemental appropriations for fiscal 2021 – including for pandemic response – and restoration of spending cuts included in originally enacted budgets.

47 States Saw Revenue Collections Outperform Budget Projections in Fiscal 2021

General fund collections for fiscal 2021 from all revenue sources came in above original projections used to adopt budgets in 47 states and lower in just 3 states. (See **Figure 5.**) State revenues in fiscal 2021 performed considerably better than was expected earlier in the pandemic, when most states originally adopted their budgets, for several reasons. First, federal stimulus measures put a lot of additional money into the economy and directly boosted personal income, helping to lessen state revenue losses. Second, personal income taxes were not as impacted due to the recession disproportionately affecting low-income workers while high-income earners have been relatively insulated. Third, the pandemic's effects on economic activity largely curtailed consumption of services that most states do not tax, while consumption of goods, which are taxed, was less affected. Fourth, the expanded ability to collect online sales taxes following the U.S. Supreme Court decision in *Wayfair v. South Dakota* helped mitigate sales tax losses.

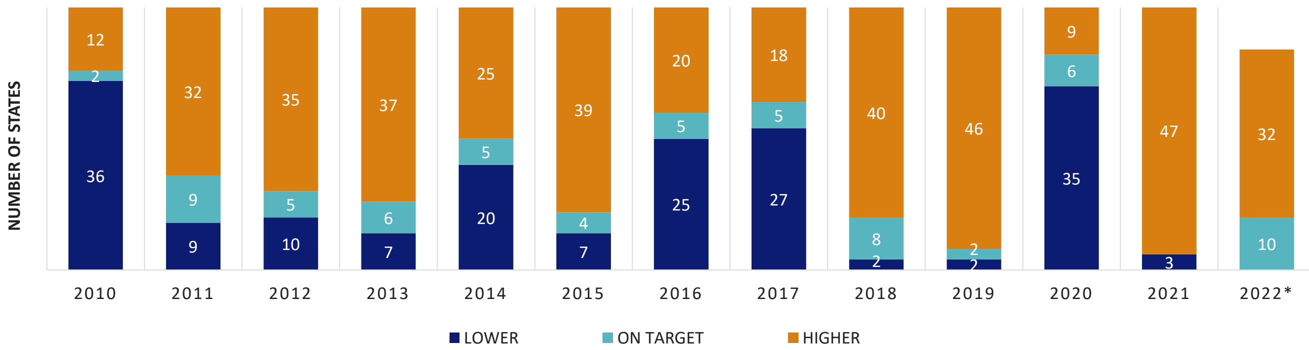
States Saw Sharp Revenue Increase in FY 2021, Due in Part to One-Time Factors

Fiscal 2021 general fund revenues totaled $1.002 trillion, representing a sharp 14.5 percent increase over fiscal 2020 actual collections of $875.1 billion. In addition to the reasons cited above for why revenues performed better than expected, there are several one-time factors helping to drive this high growth rate. These include the impact of the tax deadline shift on when revenues in some states were recognized, a low baseline in fiscal 2020 due to the impact of the pandemic on state revenues that year, and the inclusion of federal funds, borrowing and other sources in at least a few states.

States' enacted budgets for fiscal 2022 are based on general fund revenues totaling $975.3 billion, 2.6 percent below preliminary actual revenue levels for fiscal 2021. This year-over-

Figure 5.

General Fund Revenue Collections Compared To Original Budget Projections (By Fiscal Year)



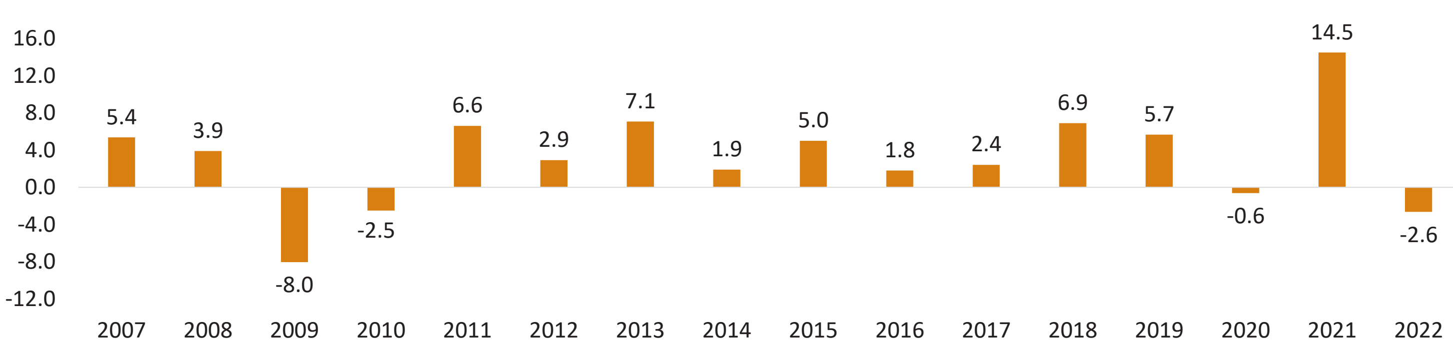
Fiscal 2022 is ongoing; figures are subject to change, and not all states were able to report this early in the fiscal year.

year decline is driven in part by two factors. First, the shift in the tax filing deadline from April 2020 to July 2020 resulted in some states recognizing a portion of their revenues (mainly from income taxes) in fiscal 2021 instead of fiscal 2020, causing a one-time bump in fiscal 2021. Second, for most states, their fiscal 2021 and fiscal 2022 figures were determined at two different points in time. Preliminary actual data for fiscal 2021 are based on final revenue collections data after the fiscal year (which ended on June 30, 2021 for most states). Enacted revenue forecasts for fiscal 2022 for many states were developed early in the 2021 calendar year, before the most recent uptick in collections. Thus, state revenues assumed in general fund budgets for fiscal 2022 are likely to be lower compared to more recently revised forecasts that take into account actual revenue collections for fiscal 2021. (See **Figure 6.**)

In this survey, 14 states separately reported more current revenue estimates for fiscal 2022. Among those states, nearly all reported upward revisions to their fiscal 2022 revenue projections compared to their enacted budget forecasts, with a median increase of 4.9 percent from enacted to most current. Furthermore, at the time of data collection, 32 states reported collections were coming in ahead of budget projections and 10 states were on target for fiscal 2022 (not all states were able to report this early in the fiscal year).

Figure 6.

Annual General Fund Revenue Changes, Fiscal 2007 To Fiscal 2022 (Percentage Change)



Note: Fiscal 2022 figure is based on states' enacted budgets.

As referenced earlier, it is important to note that annual percentage changes in general fund revenue in fiscal 2020, fiscal 2021 and fiscal 2022 were affected by the shift in the tax deadline from April 15, 2020 to July 15, 2020. Nineteen states reported that they recognized these revenues due to the deadline shift in fiscal 2021 instead of fiscal 2020 (most states end their fiscal year on June 30), while the other 31 states did not defer the delayed revenue, either because they recognized receipts on an accrual basis, they do not collect an income tax, or follow a different fiscal year. Deferring states were much more likely to report revenue declines in fiscal 2020 followed by large, double-digit percentage increases in fiscal 2021. Comparing the median general fund growth rates for fiscal 2020 and fiscal 2021 for states that deferred revenues to those that did not defer can help illuminate this. The median growth rates for all 50 states were -1.5 percent in fiscal 2020 and 12.5 percent in fiscal 2021. For the states that did not defer revenues due to the deadline change, median growth was 0.9 percent in fiscal 2020 and 10.9 percent in fiscal 2021. For those states that deferred revenue, median growth was -3.7 percent in fiscal 2020 and 20.6 percent in fiscal 2021. (See **Figure 7.**)

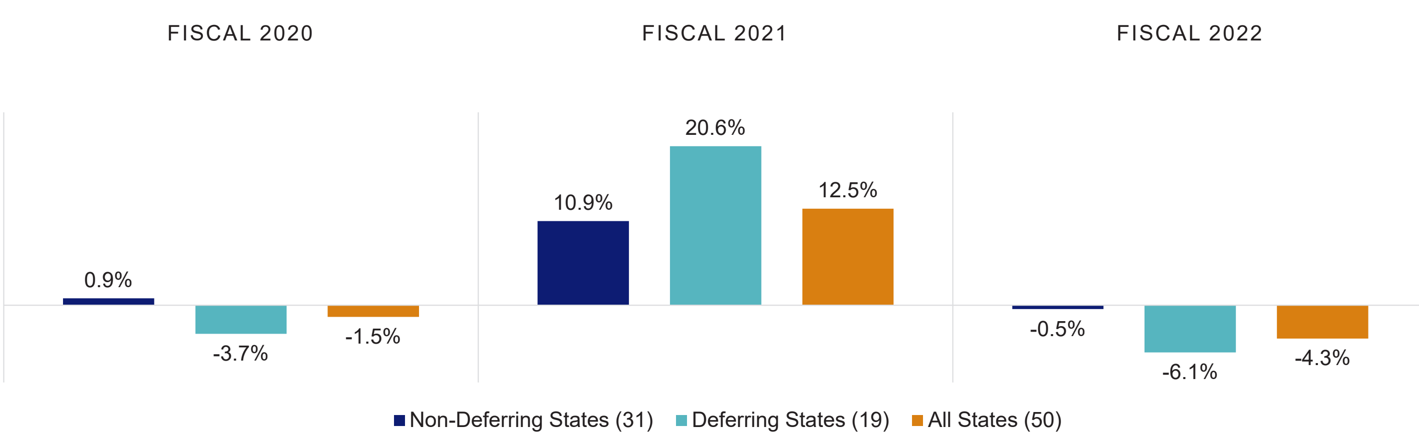
General Fund Revenue Estimates Have Improved Over Course of Pandemic

State revenues performed considerably better than was expected earlier in the pandemic for several reasons discussed above. This trajectory is evident in NASBO's *Fiscal Survey of States*. One year ago, state revenue estimates reported in the *Fall 2020 Fiscal Survey* predicted that general fund revenue would record an annual decline of 3.5 percent in fiscal 2021. In the *Spring 2021 Fiscal Survey*, revenue in fiscal 2021 was expected to grow 3.7 percent. In this survey, preliminary actual collections data show revenue increased by 14.5 percent. These large swings speak to the many difficulties of and tremendous uncertainty surrounding state revenue forecasts during the pandemic. Several factors made revenue forecasting especially challenging for states since the start of the COVID-19 crisis. Models for reliably projecting state revenues in unprecedented events such as a pandemic did not exist. Moreover, public health and economic conditions have evolved rapidly and unevenly across states over the course of the pandemic. A large influx of federal stimulus early on, coupled with uncertainty regarding additional federal aid last year, contributed to forecasting challenges as well. The tax deadline shift added further complexity to forecasting - and contributed to the higher revenue growth rate for fiscal 2021, as discussed above.

In addition to revenues outperforming projections from earlier in the pandemic and in enacted budgets, most states have seen general fund collections come in above their pre-COVID forecasts. Examining general fund revenue for fiscal 2020 and fiscal 2021 combined, aggregate collections came in 2.2 percent above states' (mostly) pre-COVID forecasts reported in NASBO's *Spring 2020 Fiscal Survey*. (See **Figure 8.**)

Figure 7.

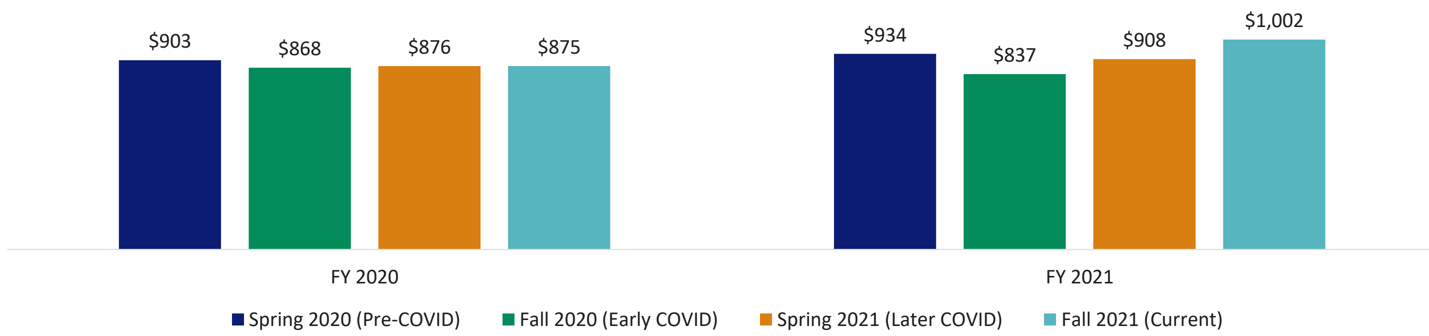
Median Annual Percentage Change in General Fund Revenue, Deferring and Non-Deferring States



Note: 19 "deferring" states recognized some revenue in fiscal 2021 instead of fiscal 2020 due to the tax deadline shift from April 15, 2020 to July 15, 2020.

Figure 8.

General Fund Revenue Estimates By Fiscal Year in Different Fiscal Survey Editions ($ in Billions)



**General fund revenue information reported in the Spring 2020 and Fall 2020 Fiscal Surveys was adjusted for this comparison to account for a change in Ohio's reporting methodology. Beginning in the Spring 2021 Fiscal Survey, Ohio began excluding federal Medicaid reimbursements from its general fund reporting.*

States Adopt Tax Changes in Fiscal 2022 Resulting in Modest Net Revenue Decrease

According to enacted budgets, 12 states adopted net increases in taxes and fees while 28 states made net decreases, resulting in a projected net revenue impact in fiscal 2022 of -$2.9 billion. This net reduction contrasts with proposed revenue actions in governors' budgets reported in the *Spring 2021 Fiscal Survey of States*, which called for a net increase in revenue of $6.5 billion. This difference is in part indicative of improving fiscal conditions from the time governors released their budget proposals to when states adopted budgets for fiscal 2022. While some states enacted income tax increases, including a temporary high income surcharge and limiting corporate tax breaks, others reported personal income tax decreases in the form of rate reductions or increasing certain deductions. Additionally, a number of states enacted income tax changes to conform with changes at the federal level that will result in net revenue decreases. General fund revenue will be reduced by an estimated $1.7 billion on net as a result of these changes, representing less than 0.2 percent of total general fund revenues forecasted in enacted budgets for fiscal 2022. (See **Figure 9.**)

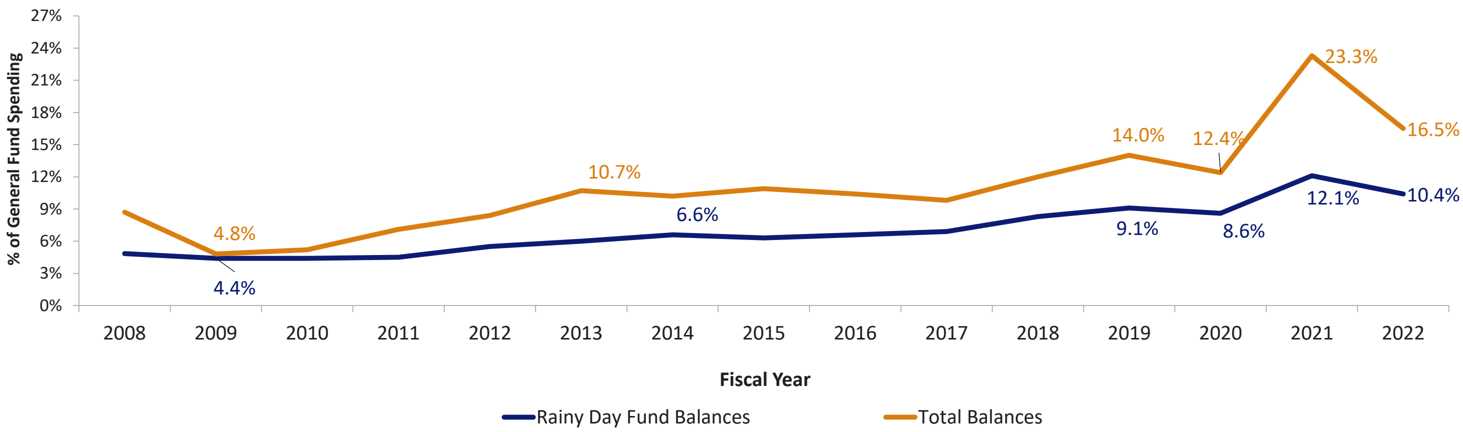
Figure 9.

Summary of Enacted State Revenue Changes, Fiscal 2022

Revenue Type	Sales Tax	Personal Income Tax	Corporate Income Tax	Cigarette/ Tobacco Tax	Motor Fuel Tax	Alcohol Tax	Gaming/ Lottery Revenue	Other Tax	Fees	All Revenue Changes
# of States Enacting Increases	4	5	6	2	2	1	3	11	5	**12**
# of States Enacting Decreases	15	24	16	1	2	1	0	9	3	**28**
Net Change ($ In Millions)	+$1,125	-$4,642	+$724	+$207	+$88	-$1	+$352	-$898	+$95	**-$2,950**
Net Change – General Fund Only ($ in Millions)	+$1,125	-$4,163	+$592	+$207	-$2	-$1	+$336	+$261	-$10	**-$1,655**

Figure 10.

Rainy Day Fund Balances and Total Balances as a Percentage of General Fund Expenditures



State Balances Reach All-Time High in Fiscal 2021 After Decline Early in Pandemic

Before the COVID-19 crisis hit, state rainy day funds and total balances were at an all-time high, after a decade of rebuilding reserves following the Great Recession. In fiscal 2019, rainy day fund balances reached 9.1 percent as a share of general fund spending and total balances were at 14.0 percent. As they coped with weakening revenue projections and increased spending demands early in the pandemic, some states turned to their rainy day funds, other reserves, and prior-year balances as a tool to help manage their budgets. This resulted in declines in both rainy day funds and total balances in fiscal 2020.

Due to revenues exceeding budget projections as well as other one-time factors, states reported substantial increases in balance levels in fiscal 2021, with both rainy day funds and total balances reaching new record levels. At the end of fiscal 2021, rainy day fund balances totaled $112.7 billion or 12.1 percent as a share of general fund spending and total balances (including rainy day funds) reached $217.1 billion or 23.3 percent of general fund spending. According to enacted budgets, states are planning to spend down some of their larger-than-expected ending balances, including for one-time investments, with 32 states reporting lower total balance levels for fiscal 2022. As a share of general fund spending, total rainy day fund balances are expected to dip slightly as well, though the median balance is projected to tick up to 11.9 percent. (See **Figure 10.**)

State Budget Outlook: Investing in Recovery and Resiliency

States are in a much stronger position today than was expected earlier in the pandemic, due in large part to significant federal economic stimulus and direct federal aid to states. Based on this survey, nearly all states saw general fund revenues outperform budget projections in fiscal 2021, and most states are seeing revenues coming in ahead of their forecasts for fiscal 2022 as well. Enacted budgets for fiscal 2022 – as well as more recent actions in some states – demonstrate states' planning efforts for how to spend available federal aid and state budget surpluses. States are directing this one-time money towards assistance for individuals, businesses, and communities that were most affected by the pandemic and other targeted one-time investments to support a robust economic recovery, as well as for ongoing COVID-19 response efforts. States are also taking steps to build financial resiliency and maintain their record high reserve levels. This activity is expected to carry into 2022 legislative sessions and presents both opportunities and challenges for state budgeting, especially in an environment where uncertainty about the future course of the pandemic and recovery remains.

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