

June 25, 2020 | ISSUE BRIEF

Summary:

Spring 2020 Fiscal Survey of States

Every spring, NASBO conducts the Fiscal Survey of States to assess the fiscal health of states based on governors' budget recommendations. However, as this report reflects state fiscal conditions before the effects of COVID-19 and its economic fallout, it does not capture the current state of the states. Most governors proposed their budgets in December or January, with the earliest coming out in November and the latest released in early March. These budget proposals reflect another era, before "coronavirus" and "COVID-19" were household words, when unemployment was at a 50-year low of 3.5 percent, and state revenues were on track to grow for a 10th consecutive year. Just a few months later, national unemployment stood at 13.3 percent, retail sales were plummeting, and state and local governments had already shed 1.5 million jobs.

The data cited in this summary, and published in the full [Spring 2020 Fiscal Survey of States report](#), reflect state general fund spending, revenue, and balance estimates for fiscal 2020 and projections for fiscal 2021 before the impact of the COVID-19 crisis. NASBO expects the data in this report will serve as a historical baseline for comparison to post-COVID fiscal conditions, as states release revised [revenue forecasts](#), and make [budget adjustments](#) for fiscal 2020 and fiscal 2021.

Governors' Fiscal 2021 Budgets Reflect Strong State Fiscal Conditions Before COVID-19 Crisis

Before the COVID-19 pandemic and its economic fallout upended state budgets, state fiscal conditions were strong overall following a decade of revenue growth and strengthening reserves. Most states experienced multiple consecutive years of faster-than-expected revenue growth coming into the crisis, leading to sizeable budget surpluses in some cases. States were focused on investing in key priorities while at the same time being cautious about taking on too many new ongoing spending commitments. At the time governors proposed their budgets, a majority of states were seeing revenues coming in above budget projections for fiscal 2020, with modest revenue growth forecasted for fiscal 2021. Rainy day fund balances were at an all-time high as well, as states focused on preparing for the next recession – though no state could have prepared for the present public health and economic crisis.

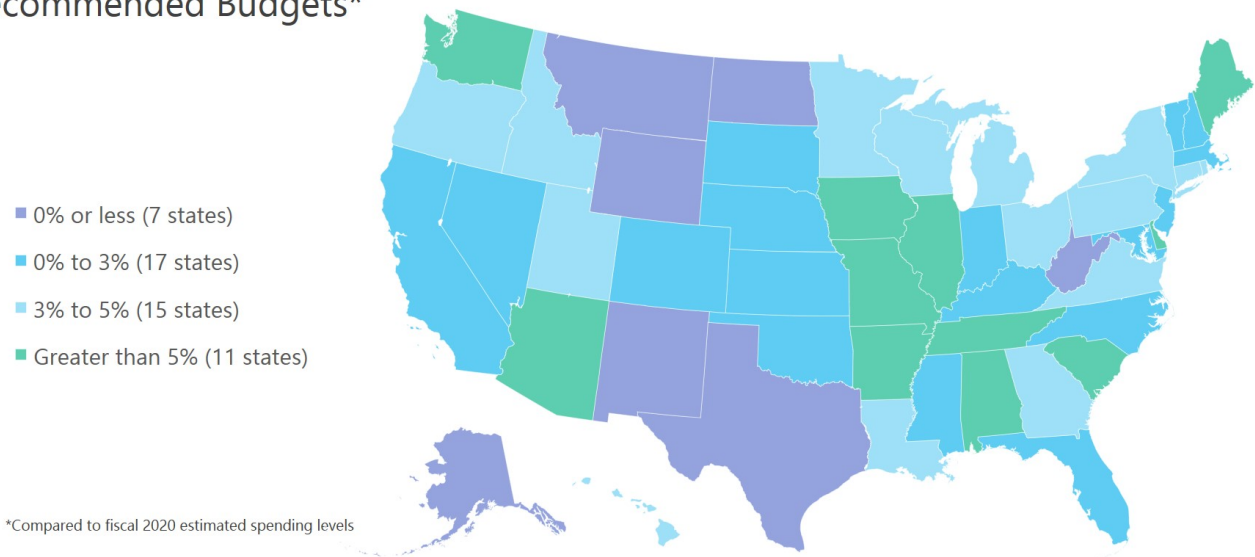
Modest State Spending Growth Was Expected in Fiscal 2021 Pre-COVID

Governors' budget proposals were introduced following nine consecutive years of growth in both state general fund spending and revenue (fiscal 2011-2019), with most states expecting fiscal 2020 to mark a tenth straight year. Most states were planning for another year of spending growth in fiscal 2021, though at a slower rate compared to the past couple of years. More modest projected revenue growth and governors' emphasis on fiscal discipline contributed to this slower growth rate.

Before the COVID-19 crisis hit, governors proposed general fund spending in the amount of \$944.6 billion in fiscal 2021 according to recommended budgets. This represented a modest 2.8 percent increase compared to estimated spending levels for fiscal 2020. Overall, 43 states were expecting general fund spending to grow in fiscal 2021 based on governors' budgets, with most states calling for increases of less than 5 percent. (See **Figure 1.**)

Figure 1.

General Fund Spending Percentage Change In Fiscal 2021 Recommended Budgets*

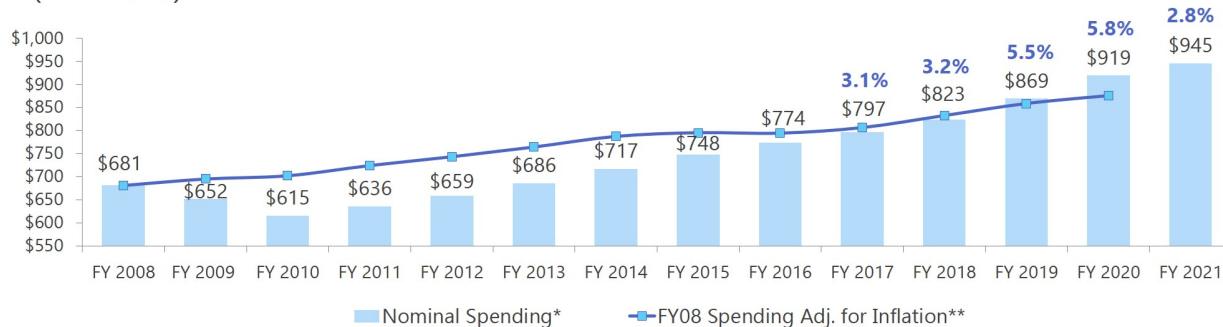


Based on pre-COVID estimates, general fund spending was on track to total \$919.1 billion in fiscal 2020, a 5.8 percent increase, with this growth partially driven by one-time investments and rainy day fund deposits made with surplus funds. After steep declines during the Great Recession, state general fund spending just barely returned to inflation-adjusted pre-recession fiscal 2008 levels in fiscal 2019. (See **Figure 2.**) Even in fiscal 2020, according to pre-COVID estimated spending levels, 24 states were expecting to spend less from their general funds than they did in fiscal 2008, after adjusting for inflation.¹

¹ The state and local government implicit price deflator cited by the Bureau of Economic Analysis National Income and Product Account Tables, Table 3.9.4., Line 33 (last updated on May 28, 2020), is used for inflation adjustments. Quarterly averages are used to calculate fiscal year inflation rates.

Figure 2.

General Fund Spending, Fiscal 2008 To Fiscal 2021 (In Billions)



Fiscal 2020 figure is estimated (pre-COVID-19). Fiscal 2021 figure is based on governors' recommended budgets (pre-COVID-19).

Percentages shown represent total annual general fund spending growth.

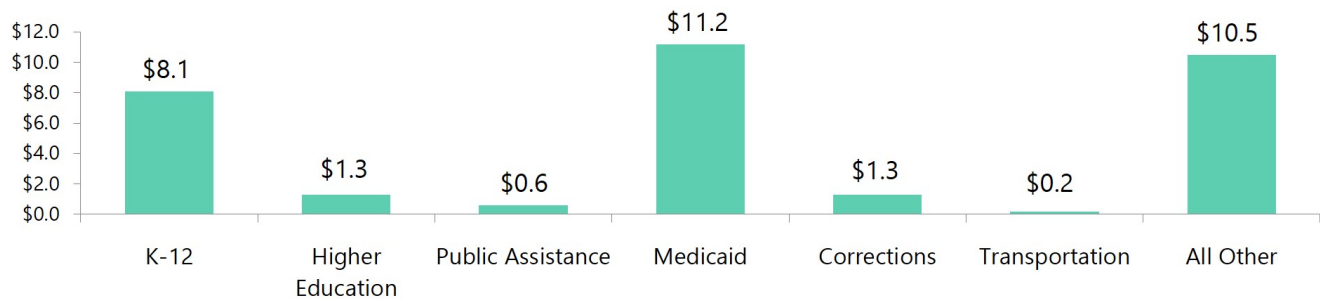
*Beginning with the Fall 2019 Fiscal Survey edition, Massachusetts now excludes federal reimbursements in its general fund spending and revenue totals. NASBO has adjusted prior 50-state totals from the Fiscal Survey to remove Massachusetts' federal reimbursement amounts (as reported in the state's Comprehensive Annual Financial Report, or CAFR) for comparison purposes.

Governors Proposed Spending Increases for K-12 and Medicaid

In their budgets, governors recommended most new money go towards K-12 education and Medicaid, the two largest categories of state general fund budgets, with the "all other" category receiving sizeable proposed increases as well, including for one-time investments and reserve deposits. Governors recommended \$33.2 billion in general fund appropriation increases in their fiscal 2021 budgets, with Medicaid as the largest recipient of new money in fiscal 2021, receiving an \$11.2 billion funding boost, after smaller increases in recent years. Elementary and secondary education, by far the largest recipient of new money in fiscal 2020, received an additional \$8.1 billion in governors' fiscal 2021 budgets to build upon recent funding increases. Every other program area received net increases in governors' fiscal 2021 budgets as well. (See **Figure 3.**)

Figure 3.

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

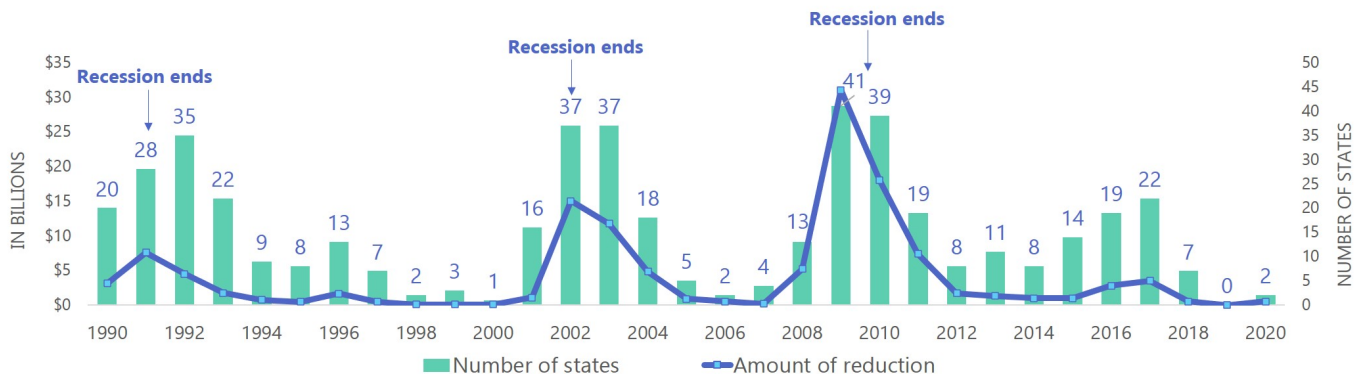


*Appropriation increases are compared to enacted appropriation levels for fiscal 2020.

Nineteen states reported making mid-year spending increases in fiscal 2020, while just four states reported net mid-year spending reductions, for a net increase of \$4.1 billion. Among those states reporting net decreases in spending, only two states reported that the mid-year reductions were made in response to revenue shortfalls. (See **Figure 4.**) One of those two states, Arkansas, is the only state that completed the full survey based on the state's post-COVID-19 spending and revenue data.

Figure 4.

Budget Cuts Made After The Budget Passed



Note: Beginning in Fiscal 2018, NASBO asked states reporting net mid-year budget reductions as to whether the reductions were made due, at least in part, to a revenue shortfall. Effective in Fiscal 2018 going forward, only states reporting mid-year budget cuts due to a shortfall are included in the totals reported in this figure. Prior to Fiscal 2018, 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.

Before COVID, Most States Saw Revenues Exceeding Projections for Fiscal 2020

As governors were introducing their budget proposals for fiscal 2021, most states were seeing tax collections coming in above budget projections in fiscal 2020 and forecasting modest revenue growth for fiscal 2021. The onset of the COVID-19 public health crisis and ensuing recession have dramatically altered revenue projections for the remainder of fiscal 2020 and fiscal 2021, which begins on July 1, 2020 for the vast majority of states.² States rely on personal income taxes and sales taxes combined for roughly 75 percent of their general fund revenue. These sources have been hit hard in light of stay-at-home orders, business closures, and rising unemployment claims that have resulted in likely the worst economic situation this country has faced since the Great Depression. As this report went to print, states had begun to release updated [revenue forecasts](#) that account for the impacts of COVID on their economies and tax collections.

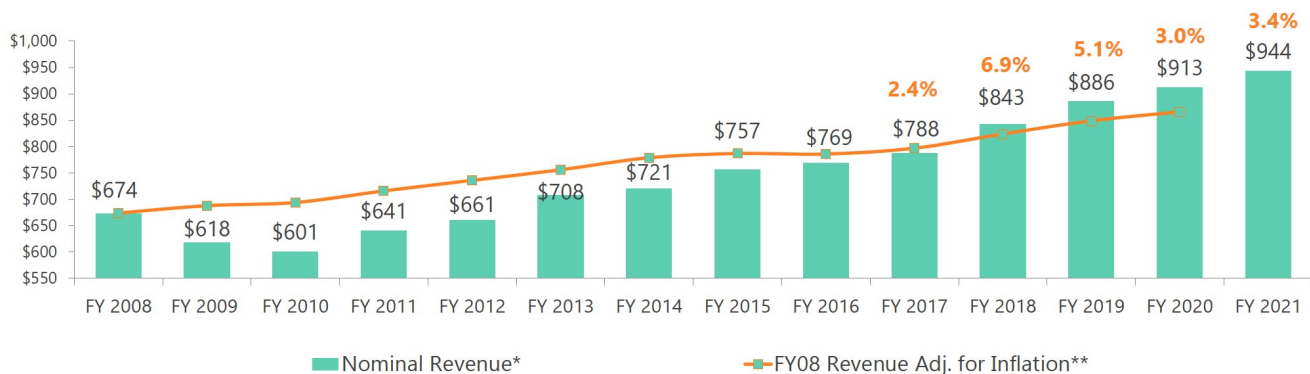
Before COVID-19 hit, revenues were on track to increase 3.0 percent in fiscal 2020 over fiscal 2019, slower than the level of growth observed over the past couple of years. General fund collections from sales taxes were on track to grow 5.0 percent in fiscal 2020, personal income taxes were set to increase by an estimated 2.7 percent, and corporate income taxes, a more volatile revenue source, were estimated to increase by 1.0 percent in fiscal 2020. Gaming and lottery revenues, a modest source of general fund revenue for states, was estimated to decline 3.6 percent (mostly due to the elimination of this as a revenue source in one state), and all other general fund revenue was estimated to grow by 0.7 percent. According to governors' pre-COVID recommended budgets, general fund revenue collections were forecasted to grow 3.4 percent in fiscal 2021 to total \$943.9 billion. Broken

² Typically, 46 states begin their fiscal years in July and end them in June. The exceptions are New York, which starts its fiscal year on April 1; Texas, with a September 1 start date; and Alabama and Michigan, which start their fiscal years on October 1. [For fiscal 2020 only, New Jersey extended its fiscal year so that fiscal 2021 will begin on October 1, 2020 and end on June 30, 2021; however, New Jersey's survey data in this report predate this change and do not reflect that adjustment.]

down by tax type, general fund collections from sales taxes were forecasted to grow 3.3 percent, personal income taxes by 3.7 percent, corporate income taxes by 2.7 percent, gaming and lottery revenues by 2.5 percent, and all other revenues by 0.9 percent in fiscal 2021. (See **Figure 5.**)

Figure 5.

General Fund Revenue, Fiscal 2008 To Fiscal 2021 (In Billions)



Fiscal 2020 figure is estimated (pre-COVID-19). Fiscal 2021 figure is based on governors' recommended budgets (pre-COVID-19).

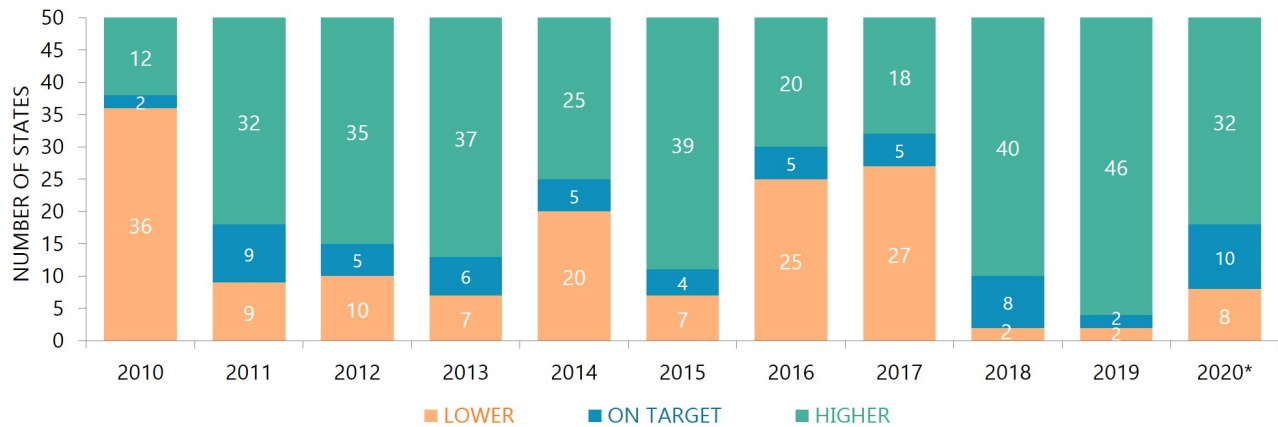
Percentages shown represent total annual general fund revenue growth.

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Despite more modest growth, 32 states were seeing revenue collections exceeding original budget projections, with 10 states reporting collections as on target and only eight states reporting collections coming in lower than their original budget forecasts. (See **Figure 6.**) A few states with collections coming in below projections reported that some early impacts of COVID-19 were observed in their collections and incorporated into their responses, based on when they reported. Additionally, several states that reported collections coming in lower than projections are especially reliant on the energy industry for revenues, which have been hard hit by collapsing oil prices.

Figure 6.

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













*Fiscal 2020 figures were estimated based predominantly on pre-COVID-19 data. A few states that reported collections coming in lower than projections incorporated some early COVID-19 impacts on their tax collections.

Governors Propose Mostly Modest Tax Changes for Fiscal 2021

When governors proposed their fiscal 2021 budgets, fiscal conditions were stable in the vast majority of states, and recommended revenue actions were for the most part limited and modest in size. According to executive budgets, 14 states proposed net increases in taxes and fees while 15 states proposed net decreases, resulting in a projected net positive revenue impact in fiscal 2021 of \$2.4 billion. Most of the additional revenue that would be generated by these proposals would go towards non-general fund sources for dedicated purposes such as transportation and health care. In fact, looking at general fund revenue impacts only, governors proposed changes with a net decrease in general fund revenue of \$588 million. (See **Figure 7.**) Additionally, 13 states enacted changes in taxes and fees in the middle of fiscal 2020, with four states enacting increases and nine states enacting decreases, for a total net revenue decrease of \$123 million.

Figure 7.

Summary of Recommended State Revenue Changes, Fiscal 2021

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 Recommending Increases	7	3	4	6	2	0	6	7	7	14
# of States Recommending Decreases	2	14	6	2	0	1	0	6	0	15
Net Change (\$ In Millions)	+\$767	-\$1,079	+\$47	+\$195	+\$1,070	-\$5	+\$85	+\$843	+\$519	+\$2,431
Net Change – General Fund Only (\$ in Millions)	+\$714	-\$1,607	+\$39	+\$177	\$0	-\$5	+\$53	-\$86	+\$127	-\$588

Rainy Day Fund Balances at All-Time High Coming into COVID Crisis

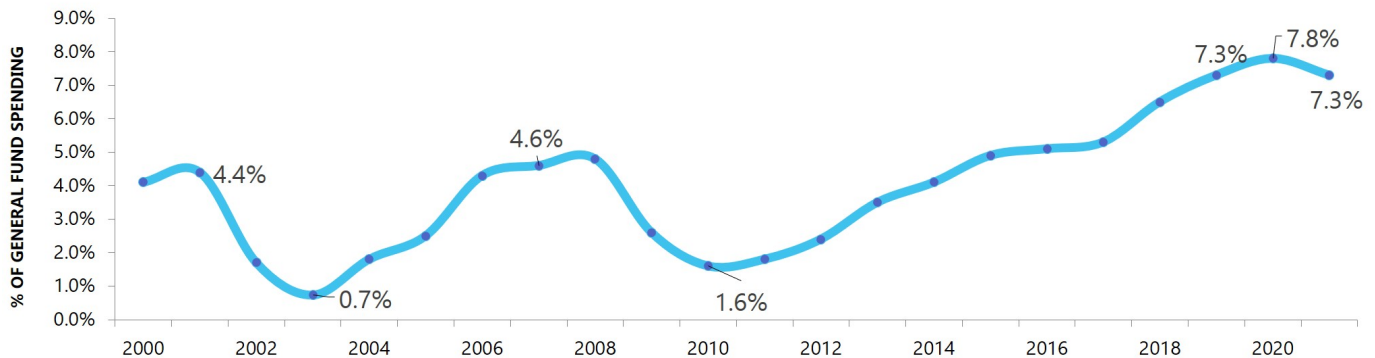
In recent years, states have focused on strengthening their reserves in preparation for the next economic downturn. When governors proposed their budgets for fiscal 2021, rainy day fund balances were at an all-time high in the aggregate, both in nominal dollars and as a percentage of state spending, following steady growth in the years since the Great Recession. Rainy day fund balances reached \$75.5 billion in fiscal 2019 (with a median balance of 7.3 percent as a share of general fund spending). Before the COVID-19 crisis, states were expecting to end fiscal 2020 with a median rainy day fund balance of 7.8 percent, a new all-time high.

Since fiscal 2010, the median rainy day fund balance level as a percentage of general fund spending had grown from 1.6 percent to an estimated 7.8 percent in fiscal 2020. Improved

revenue conditions coupled with deliberate policy choices contributed to this growth. By comparison, going into the last recession, the median rainy day fund balance in fiscal 2007 was 4.6 percent. (See **Figure 8.**)

Figure 8.

Median Rainy Day Fund Balance Over Time



Governors' pre-COVID-19 budget proposals for fiscal 2021 planned to continue prioritizing rainy day funds, with 28 states projecting increases in fiscal 2021 based on governors' budgets, following 36 states with estimated increases in fiscal 2020. Rainy day fund balance levels continue to vary by state, but most states have made significant progress in strengthening their reserves since the Great Recession, and in fiscal 2019, 35 states reported rainy day fund balances exceeding 5 percent of general fund spending.

Total balances include both general fund ending balances and the amounts in states' rainy day funds, and reflect the funds that states may use for cashflow liquidity, to respond to unforeseen circumstances and to help resolve revenue shortfalls, though in some states, part of the ending balance may already be reserved for expenditure in a subsequent year. In fiscal 2020, total balances (before the COVID crisis) were estimated to end the year totaling \$108.3 billion (excluding two states that were unable to provide comparable balance data for fiscal 2020 and fiscal 2021). For fiscal 2021, based on governors' budgets, states were forecasting total balances of \$102.2 billion.

As states cope with precipitous revenue declines and increased spending demands in the wake of the COVID-19 pandemic, these rainy day funds and other reserves will be a critical budget management tool for states, though they will not be enough to cover the massive budget shortfalls expected this year and in the years to come.

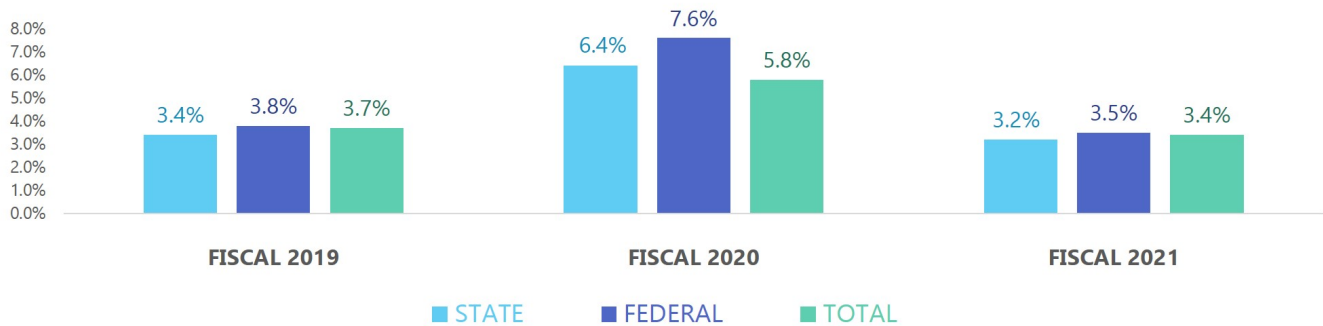
Medicaid Spending Was Expected to Slow in Fiscal 2021 Before COVID Crisis

The Spring Fiscal Survey also includes a special feature on the outlook of state Medicaid programs in terms of spending and programmatic changes. The numerical figures on Medicaid expenditures provided in this survey, as with other data in the report, do not reflect COVID-19 impacts.

Before COVID-19, Medicaid spending from all fund sources was estimated to grow by a median of 5.8 percent in fiscal 2020 compared to fiscal 2019 levels. In fiscal 2020, spending from state fund sources was estimated to grow by a median of 6.4 percent, with general fund spending growing 5.0 percent and spending from other state funds growing 9.9 percent. Federal fund spending on Medicaid was on track to grow 7.6 percent for fiscal 2020. Looking ahead, Medicaid spending growth was forecasted to slow somewhat in fiscal 2021, based on governors' proposed budgets. The median growth rate for total Medicaid spending was projected at 3.4 percent for fiscal 2021. State fund spending was forecasted to grow 3.2 percent for the average state, with general fund spending growth of 4.2 percent and other state funds staying flat, while federal fund spending was expected to increase 3.5 percent. (See **Figure 9**.)

Figure 9.

Median Percentage Change In Medicaid Spending (By Fund Source)



States that expanded Medicaid also reported on their expenditures for the new adult eligibility group (including both “newly eligible” and “not newly eligible”) by fund source. States began paying 5 percent of the costs for newly eligible adults in calendar year 2017, with the state share gradually set to increase to 10 percent by 2020. As states have begun to pick up a larger share of the cost, Medicaid expansion spending from state funds is estimated to increase by \$2.1 billion in fiscal 2020, and is projected to grow by another \$2.5 billion in fiscal 2021. These increases are also driven in part by more states adopting Medicaid expansion. In Idaho, Nebraska, and Utah, voters approved expansion in 2018 ballot initiatives with expansion implemented during fiscal 2020 and fiscal 2021. As of May 2020, 36 states and the District of Columbia have adopted Medicaid expansion. Additionally, governors in two states that have yet to expand, North Carolina and Oklahoma, included funding in fiscal 2021 for Medicaid expansion in their recommended budgets.

States reported on programmatic changes in Medicaid that they made in fiscal 2020 and recommended for fiscal 2021 for both enhancing programs and containing costs. The most common program enhancement actions for fiscal 2020 included increasing payments to providers (35 states), expanding access to behavioral health services (26 states), and expanding or restoring benefits (21 states). Similar numbers of states recommended these program enhancements in fiscal 2021 proposed budgets. States were also asked about

changes to contain costs and the most common responses were enhanced program integrity efforts in 16 states, changes to delivery systems in 14 states, and policies to cuts costs for prescription drugs in 13 states for fiscal 2020. Additionally, for fiscal 2020, 17 states have raised or plan to raise provider taxes or fees while 17 states have plans to raise provider taxes or fees in governors' recommended budgets for fiscal 2021.

Outlook for State Budgets & Impact of COVID-19

As this survey shows, before the COVID pandemic, state fiscal conditions were strong overall and rainy day funds were at an all-time high. Governors' budgets for fiscal 2021 were focused on investing in key priorities while calling for modest spending growth, with an emphasis on fiscal discipline and preparing for the next recession.

However, no states could have prepared for the economic fallout of COVID-19. In just a few months, state fiscal conditions have experienced a dramatic shift for the worse. States have begun to release updated revenue forecasts that project the impacts of COVID over the next one to two years, and early analyses suggest potential revenue losses double what states experienced during the Great Recession, when states saw a more than 11 percent decline in revenues over two years. A number of states have already announced multi-billion-dollar budget shortfalls and revenue losses, as others are preparing to release updated projections in the coming weeks and months.

In this new fiscal environment, states are facing tough decisions, looking at cutting spending, instituting layoffs, and weighing when to use the reserves they worked hard to build in recent years. As this report went to print, states were also waiting to see whether additional aid would come from the federal government. Though not expected to eliminate the need for spending reductions, additional federal aid will be necessary to avoid even more drastic and painful cuts that will hurt state residents and significantly dampen the nation's economic recovery.

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