



Summary: 2020 State Expenditure Report

November 20, 2020

Overview: Total State Spending Grows in Fiscal 2020, Largely Due to Additional Federal Aid Related to COVID-19 Pandemic

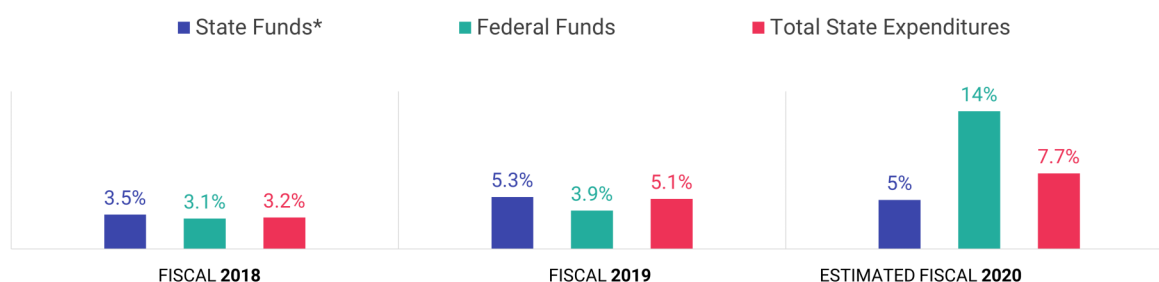
Total state spending reached \$2.26 trillion in fiscal 2020, rising from \$2.10 trillion in fiscal 2019. In fiscal 2020 it is estimated that total state spending grew 7.7 percent; the median rate was slightly lower at 7.5 percent. Spending from states' own funds (general funds and other state funds combined, excluding bonds) rose 5.0 percent in fiscal 2020 while federal funds to states grew 14.0 percent. One reason that estimated spending from state funds grew in fiscal 2020 despite the coronavirus outbreak is that when the COVID-19 crisis hit – leading to lockdowns and a dramatic fall in economic activity across the country – most states were entering the fourth quarter of fiscal 2020. This meant that states were limited in how much they could turn to spending cuts to close fiscal 2020 budget shortfalls, since it can be challenging to balance a budget with cuts late in the fiscal year. Many states utilized one-time measures including tapping reserves and fund transfers, as well as leveraging federal stimulus dollars, to close gaps in fiscal 2020. States also faced increased spending demands related to the pandemic and resulting economic decline.

Federal funds are estimated to have increased 14.0 percent in fiscal 2020, the highest annual growth rate since the Great Recession following the passage of the *American Recovery and Reinvestment Act* (ARRA) in 2009. The sizeable increase in federal funds spending in fiscal 2020 is largely due to additional federal aid states received in response to the COVID-19 pandemic. In Spring 2020, the United States Congress passed a series of bills, responding to the crisis, with the largest bill being the *Coronavirus Aid, Relief, and Economic Security (CARES) Act*. The CARES Act provided significant funding to states, which they began to spend in fiscal 2020. Congress also passed the *Families First Coronavirus Response Act* to address the rise in Medicaid spending and provide some state fiscal relief; the bill included a 6.2 percentage point increase in Federal Medical Assistance Percentage (FMAP) spending during the public health emergency.

Total state spending grew by 5.1 percent in fiscal 2019, slightly below the 34-year NASBO survey historical average of 5.4 percent (not adjusted for inflation). The median rate was slower at 4.0 percent.

Year-Over-Year Percentage Spending Growth

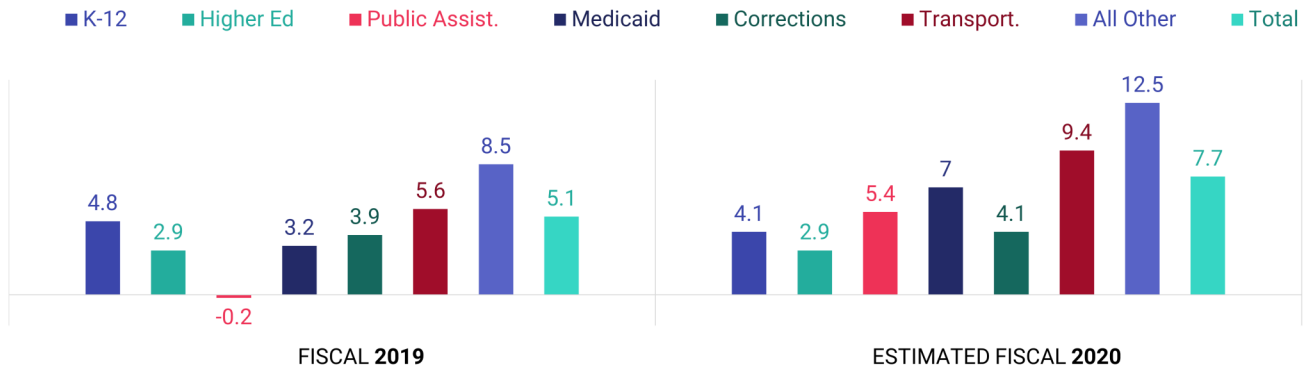
By Fund Source



*State funds are general funds and other state funds combined, excluding bonds. Total state expenditures are all federal and state funds.

Total State Expenditures Percentage Spending Growth

By Program Area



*Total state expenditures include spending from general funds, other state funds, bonds, and federal funds to states.

The “All Other” Category Saw the Largest Gains in Fiscal 2020

All eight program areas experienced an increase in total state spending in fiscal 2020, with the “all other” category seeing the largest gain. Many of the top expenditure areas for CARES Act funds fall under the “all other” category in the *State Expenditure Report* including unemployment insurance, public health programs, housing assistance, emergency management, economic relief, aid to local governments, and broadband and other technology upgrades. In fiscal 2019, nearly all program areas experienced an increase in total state spending, with the “all other” category once again seeing the highest growth rate and public assistance experiencing a

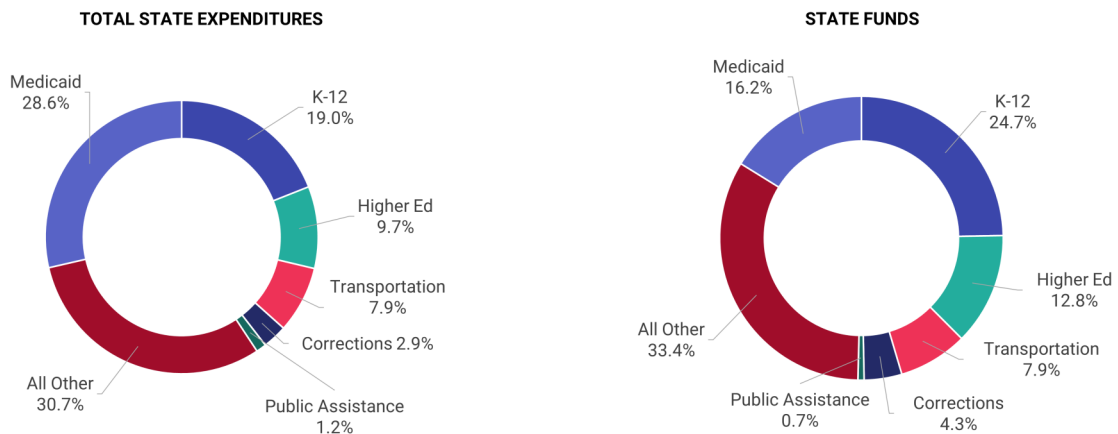
decline. In both years, the transportation category had the second highest percentage growth. The increase in transportation spending reflects the devotion of additional state resources to address the need for maintenance and infrastructure demands.

Medicaid Declines as a Share of Total State Spending in Fiscal 2020; K-12 Remained the Largest Category from State Funds

Since the beginning of the Great Recession and continuing through the enactment of the Affordable Care Act, Medicaid had risen as a percentage of total state spending, growing from 20.5 percent in fiscal 2008 to 29.3 percent in fiscal 2018.

Expenditures By Function

Estimated Fiscal 2020



Total state expenditures are all federal and state funds. State funds are general funds and other state funds combined, excluding bonds.

However, in the last two years Medicaid slightly declined as a share of total state spending, falling to 28.7 percent in fiscal 2019 and 28.6 percent in estimated fiscal 2020. Elementary and secondary education remained the second largest area of total state spending in fiscal 2020, representing 19.0 percent. When looking at state funds only, elementary and secondary education remained the largest category in fiscal 2020 at 24.7 percent, while Medicaid was second at 16.2 percent.

The Far West and Southeast Lead All Regions in Spending Growth in Fiscal 2020

All geographic regions experienced increased spending from state funds, federal funds, and total funds in both fiscal 2020 and fiscal 2019. In estimated fiscal 2020, the Far West and Southeast regions experienced the highest growth in total spending at 11.6 percent and 10.4 percent respectively, likely due to population growth and increased spending demands, while the Mid-Atlantic region had the slowest growth at 3.5 percent. In fiscal 2019, the Far West region had the largest increase in total spending at 10.0 percent, while the Great Lakes and Plains regions had the slowest growth at 2.1 percent and 2.3 percent respectively.

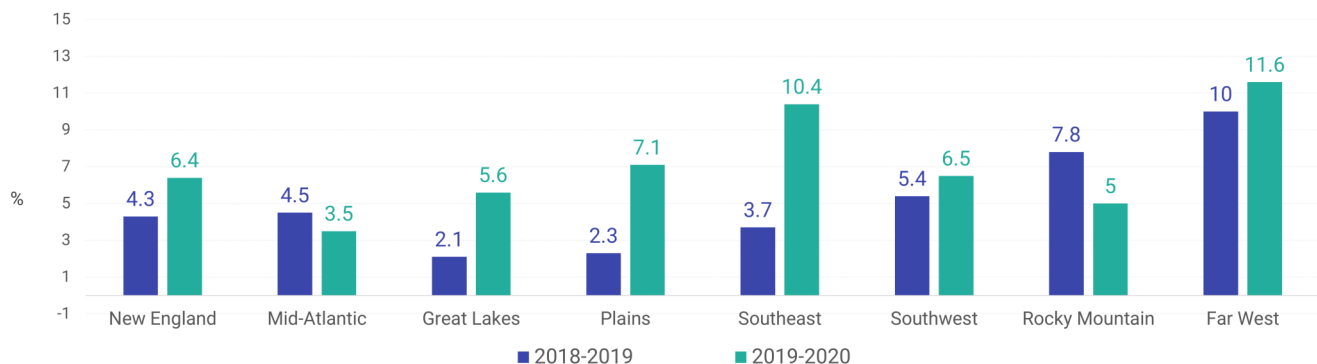
Additional state expenditure details and trends include:

- Elementary and secondary education** total expenditures increased 4.1 percent in estimated fiscal 2020 and 4.8 percent in fiscal 2019. State funds for K-12 increased 3.7 percent in fiscal 2020 and 4.9 percent in fiscal 2019, while federal funds grew 4.5 percent in fiscal 2020 and 5.0 percent in fiscal 2019. Before the onset of the COVID-19 pandemic and ensuing economic downturn, some states

took targeted steps to increase teacher compensation and improve teacher recruitment and retention. Other states increased or reformed their school funding formulas, including adding more funding for at-risk students and special education. Early education, school safety, and student counseling are other areas where states invested greater resources. K-12 education saw limited spending cuts in fiscal 2020, partly due to the fact that most states were entering the fourth quarter of fiscal 2020 when the COVID-19 crisis hit and were limited in how much they could cut spending to close fiscal 2020 budget shortfalls that late in the fiscal year.

- Total expenditures for **higher education** increased 2.9 percent in estimated fiscal 2020 and 2.9 percent in fiscal 2019. State funds for higher education are estimated to have increased 2.5 percent in fiscal 2020 and 2.6 percent in fiscal 2019, while federal funds rose 2.8 percent in fiscal 2020 and 3.9 percent in fiscal 2019. Before the onset of the COVID-19 crisis, states targeted additional funds to increase operating support for higher education institutions and to restrict tuition increases or freeze tuition rates. States also directed more resources toward postsecondary student financial aid, including through creating or expanding state-level “Promise” programs, last-dollar scholarship programs that guarantee free tuition, typically for in-state residents only. Additionally, states made targeted investments in career and technical education to better align their education systems with workforce demands. Due to the impacts of COVID-19 on state fiscal conditions, states have started to pull back on some of these investments.

Regional Percentage Change In Total Expenditures*



*Total state expenditures include spending from general funds, other state funds, bonds, and federal funds to states.

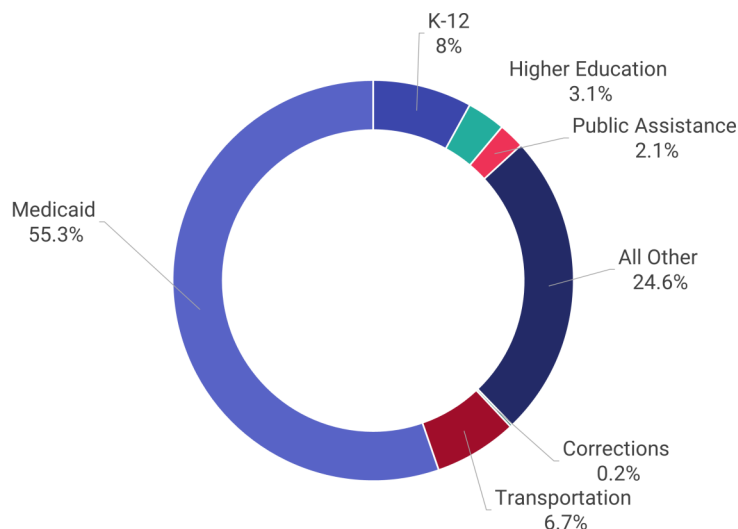
- Total **public assistance** increased 5.4 percent in estimated fiscal 2020, after declining 0.2 percent in fiscal 2019. The timing of expenditures may vary from year-to-year and may not reflect underlying program activity in a given year; large swings in some states often due in part to timing and reporting issues can substantially affect average spending growth rates. Public assistance represented 1.2 percent of total state expenditures in fiscal 2020. Public assistance data in this report is narrowly defined as spending on the Temporary Assistance for Needy Families (TANF) program and other cash assistance programs. Programs in the “other cash assistance” category, which includes optional state programs for Supplemental Security Income (SSI) and General Assistance, are not funded in all states, and when funded, are relatively small programs. Other human and social services program spending is captured in the “all other” category.
- Total **Medicaid** spending of \$646.5 billion for fiscal 2020 reflected an increase of \$42.4 billion over the \$604.1 billion spent in fiscal 2019, a 7.0 percent increase. Spending from state funds increased 4.1 percent and federal fund spending grew 8.8 percent in fiscal 2020. Medicaid spending in fiscal 2020 reflects the impact of the COVID-19 pandemic and ensuing economic fallout, with the resulting rise in unemployment affecting Medicaid enrollment and spending. To address the rise in Medicaid spending and provide state fiscal relief, the *Families First Coronavirus Response Act*, enacted in March

2020, provided a 6.2 percentage point increase in the Federal Medical Assistance Percentage (FMAP) spending during the public health emergency conditioned on states meeting certain maintenance of effort requirements including continuous coverage for current enrollees. The overall spending growth rate for total Medicaid expenditures in fiscal 2019 was considerably lower at 3.2 percent, with state funds growing 1.7 percent and federal funds increasing 4.1 percent. Federal funds comprised 62.7 percent of total Medicaid spending, general funds 27.3 percent, and other state funds 10.0 percent, in fiscal 2020.

- Total **corrections** expenditures increased 4.1 percent in estimated fiscal 2020 and 4.1 percent in fiscal 2019. Corrections accounted for 2.9 percent of total state expenditures in fiscal 2020 and 6.5 percent of general funds. Increased state spending on corrections can be attributed to several factors. First, several states have included additional funds to raise the compensation for existing and new correctional officers in recent budgets, to improve the recruitment and retention of these vital security positions. Prior to the economic downturn caused by the COVID-19 pandemic, there was a growing economy and tight labor market in which states were having to increase salaries to attract applicants and retain employees. Second, states continue to invest in criminal justice reforms to reduce correctional populations and improve outcomes; these reforms include alternatives to incarceration, earning sentence credits for good behavior,

Federal Funds Expenditures By Function

Estimated Fiscal 2020



parole reforms, and increased treatment to address mental health and substance abuse disorders. State funds (general funds and other state funds combined but excluding bonds) accounted for 96.8 percent of total state corrections spending in fiscal 2020. Federal funds accounted for 1.7 percent and bonds accounted for 1.5 percent.

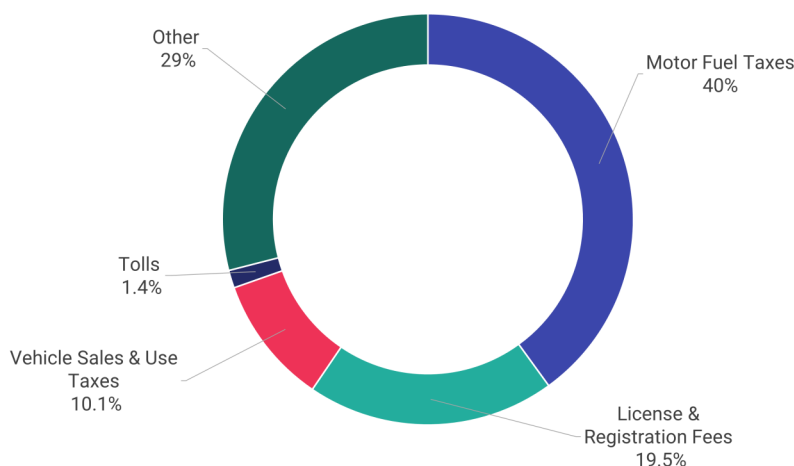
- Total **transportation** spending, representing 7.9 percent of total state expenditures, increased 9.4 percent in estimated fiscal 2020 and 5.6 percent in fiscal 2019. In fiscal 2020, it is estimated that state funds spending rose 10.4 percent and federal funds 11.9 percent, while spending from bonds declined 6.2 percent. Twenty states experienced growth of 10 percent or higher in total transportation spending in fiscal 2020. Other state funds, which are typically earmarked revenue sources such as fuel taxes, comprised 62.2 percent of total transportation spending in estimated fiscal 2020, with federal funds at 27.2 percent, bonds at 7.3 percent, and general funds only accounting for 3.3 percent. States are concerned that in the long term, the current structure of state and federal fuel tax revenue will not be able to meet transportation needs as most gas taxes are set at fixed rates and do not rise with inflation (22 states have indexed or variable-rate gas taxes), new vehicle fuel economy continues to increase, and the growth in vehicle miles traveled has leveled off. Since 2013, 33 states have taken actions to raise their fuel tax revenues. Many of the actions were the result of multi-year transportation plans and were

combined with other revenue-raising actions. One of the more notable recent actions has been the institution of registration fees on electric and hybrid vehicles to ensure that all vehicles pay a share of transportation system costs, as 27 states now have fees on electric vehicles. Additionally, states continue to explore road usage charges, or mileage-based user fees, with a growing number conducting pilot programs. State transportation funding has also been impacted by the COVID-19 pandemic. The outbreak of the coronavirus in mid-March caused a sharp decline in vehicle miles traveled, although the amount of travel has now begun to rebound somewhat. States continue to update their revenue forecasts to determine the amount of lost revenue and their ability to maintain transportation systems and current operations.

- States were also asked to detail **transportation fund revenue** sources. Forty-seven states reported having a separate transportation fund. Motor fuel taxes represented the largest revenue source for transportation funds at 40.0 percent, followed by license and registration fees (19.5 percent), vehicle sales and use taxes (10.1 percent), tolls (1.4 percent), and all other (29.0 percent). Transportation fund revenue sources totaled \$102.1 billion in fiscal 2018, \$108.8 billion in fiscal 2019, and \$106.7 billion in estimated fiscal 2020.
- The “**all other**” category of state spending increased 12.5 percent in estimated fiscal 2020, with state funds

Transportation Fund Revenue Sources

Estimated Fiscal 2020



(excluding bonds) rising 6.4 percent and federal funds increasing 35.8 percent. In fiscal 2020, total state spending for the “all other” category had the highest growth rate among all spending categories. The sizeable increase in “all other” spending in fiscal 2020 is largely due to additional federal aid states received in response to the COVID-19 pandemic. In Spring 2020, the United States Congress passed a series of bills responding to the coronavirus outbreak with the largest bill being the *Coronavirus Aid, Relief, and Economic Security (CARES) Act*. The CARES Act provided significant funding to states, which they began to spend in fiscal 2020. Many of the top expenditure areas for CARES Act funds fall under the “all other” category in this report including unemployment insurance, public health programs, housing assistance, emergency management, economic relief, aid to local governments, and broadband and other technology upgrades. In fiscal 2019, “all other” spending rose 8.5 percent as state funds increased 9.3 percent and federal funds increased 4.2 percent. “All other” represented 30.7 percent of total state expenditures in estimated fiscal 2020 and 27.3 percent of general fund expenditures. “All other” spending in states includes the Children’s Health Insurance Program (CHIP), care for the mentally ill and developmentally disabled, public health programs, child welfare and family services, constitutional officers, the legislative and judicial branches, some employer contributions to pensions and health benefits, economic development, state police, environmental protection, parks and recreation, other natural resources programs, unemployment insurance, housing, general aid to local governments, and debt service.

- States were also asked to separately detail their **debt service** spending. States’ spending on debt service totaled \$50.1 billion in fiscal 2018, \$52.6 billion in fiscal 2019, and \$49.5 billion in estimated fiscal 2020. In estimated fiscal 2020, general funds represented 56.6 percent of total state spending on debt service, while other state funds comprised the remaining 43.4 percent. In fiscal year 2020, debt service represented 3.3 percent of spending from state funds (general funds and other state funds combined, excluding bonds), and 3.1 percent of spending from the general fund only. Some states reflect no general fund spending for debt service because they earmark certain tax revenue streams to support bond repayments and direct those resources to state funds other than the general fund.

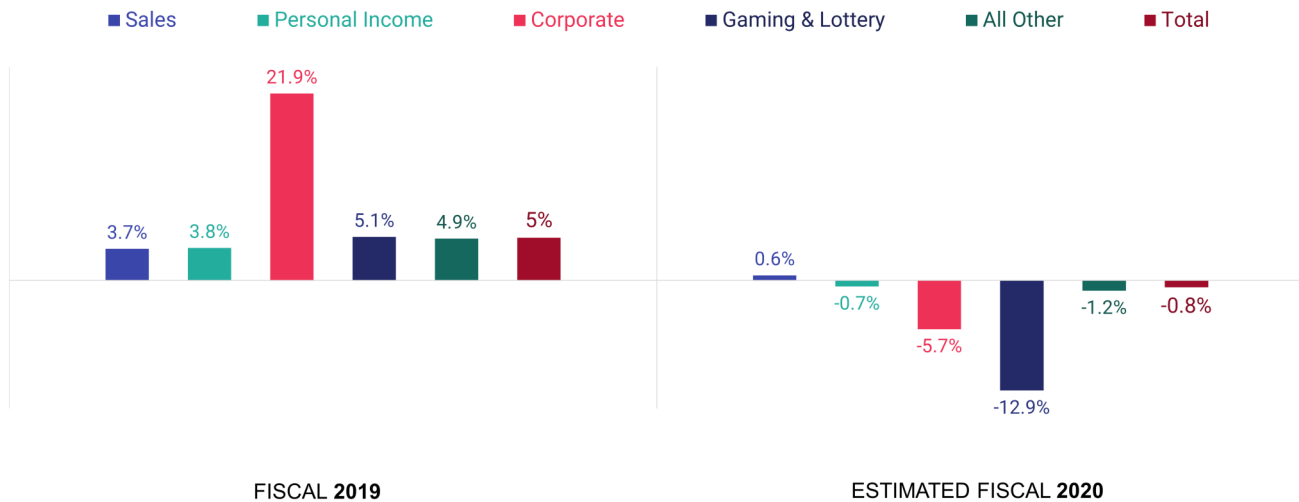
- **Capital** expenditures are made for new construction, infrastructure, major repairs and improvements, land purchases, and the acquisition of major equipment and existing structures. Capital spending increased an estimated 10.3 percent in fiscal 2020, 6.2 percent in fiscal 2019, and 1.0 percent in fiscal 2018. The fiscal 2020 growth rate of 10.3 percent is the highest annual figure over the last 20 years. The nature of capital spending often includes multi-year construction timetables and unforeseen or delayed project costs, which explains why state specific spending on capital projects can fluctuate from year-to-year. States primarily use dedicated sources to finance capital spending like the transportation fund, higher education tuition and fees, set-aside funding for capital projects, federal funds, and fund surpluses. State cash sources represent 48.2 percent of capital spending in fiscal 2020, federal funds are 25.8 percent, and bonds are 26.0 percent. The vast majority of federal funds spent for capital purposes is for transportation (94.6 percent in fiscal 2020).

State General Fund Revenue Declined in Fiscal 2020 for the First Time Since the Great Recession

General fund revenue, the largest source of state expenditures and the most discretionary, totaled an estimated \$882.5 billion in fiscal 2020, a 0.8 percent decline over fiscal 2019. States saw an overall decline in general fund tax collections in fiscal 2020 even though for three quarters of the fiscal year most states were seeing strong revenue growth and tax collections coming in above projections. Most states saw sharp revenue declines in the fourth quarter of fiscal 2020 (April-June) resulting from the impact of the COVID-19 pandemic. Personal income tax collections experienced a 0.7 percent decline despite the fact that withholding collections were buoyed by temporary stimulus measures provided by the federal government, including the enhanced unemployment insurance benefits. Additionally, the Paycheck Protection Program loans helped keep many individuals employed and paying income taxes. Sales tax collections are estimated to only grow 0.6 percent despite the strong start to the fiscal year and the impact of temporary federal stimulus measures on spending levels. Corporate income taxes are estimated to decline 5.7 percent even as stimulus measures such as the Paycheck Protection Program sought to keep companies operating. Gaming and lottery revenues experienced a 12.9 percent decline partly due to the closure of casinos and other

Revenue Growth By Percentage

State General Funds



gambling establishments during the pandemic. Finally, the “all other” category of general fund revenue declined 1.2 percent, with oil producing states seeing sharp drops in severance taxes. For most revenue sources, the median growth rate was lower than the year-over-year percentage change in estimated fiscal 2020. The median growth rate was lower for total general fund revenue collections (-2.4 percent), personal income taxes (-3.6 percent), corporate income taxes (-14.1 percent), gaming and lottery revenue (-16.7 percent), and “all other” general fund revenue (-2.0 percent), with only the median sales tax rate showing stronger growth compared to the total (1.6 percent). One reason for the difference is that states with differing fiscal years felt more or less of an impact from COVID-19 in fiscal 2020, and this tends to skew the total percentage change more than the median. Fiscal 2020 general fund revenue collections were also impacted by varying degrees from the shifting of the federal tax deadline from April 15 to July 15, 2020. Additionally, the revenue data in this report are based on estimates provided over the summer and are subject to change; NASBO’s *Fall Fiscal Survey of States*, to be released in December, will provide preliminary actual data on general fund revenues for fiscal 2020.

While state tax collections in fiscal 2020 saw an overall decline, tax collections in fiscal 2019 grew by 5.0 percent. All major sources of general fund revenue grew in fiscal 2019 including personal income taxes (3.8 percent), sales taxes (3.7 percent), corporate income taxes (21.9 percent), gaming and lottery revenue (5.1 percent), and “all other” general fund revenue

(4.9 percent). The gains in personal income taxes were largely driven by higher collections from non-wage income (capital gains, dividends, and bonuses), while the payroll withholding component also saw growth. The growth in sales tax collections has been led by gains in consumption with some states also attributing part of the fiscal 2019 growth to expanded online sales tax collections. Increases in corporate income taxes, typically a volatile revenue source for states, may in part be due to changes from the federal *Tax Cut and Jobs Act* (TCJA).

Outlook

Looking forward, state revenues are expected to see more severe declines in fiscal 2021 than they experienced in fiscal 2020 for several reasons, including: for the vast majority of states, only the last quarter of fiscal 2020 revenue collections were impacted by COVID-19, while the crisis will impact the entirety of fiscal 2021; federal stimulus measures that have helped to prop up the economy have now largely expired; state tax returns for fiscal 2020 reflected the strong economic activity of 2019 while returns in 2021 will reflect the weaker 2020 economy; and declines in state tax collections typically lag the start of national economic downturns. The declines in revenue will require states to take additional steps to ensure that their budgets remain in balance for fiscal 2021 and fiscal 2022, including spending cuts, personnel actions, examining tax increases, using rainy day funds and reserves, and the possibility of additional federal aid to states.

Since its inception in 1987, the State Expenditure Report has developed into a definitive baseline for the analysis of state spending. This edition of the report includes data from estimated fiscal 2020, actual fiscal 2019, and actual fiscal 2018. The report details by funding source the seven main functional categories of state spending: elementary and secondary education, higher education, public assistance, Medicaid, corrections, transportation, and "all other." In addition, the report separately breaks out capital spending by program area, as well as contains data on general fund revenue collections.

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