Summary: 2021 State Expenditure Report

November 19, 2021

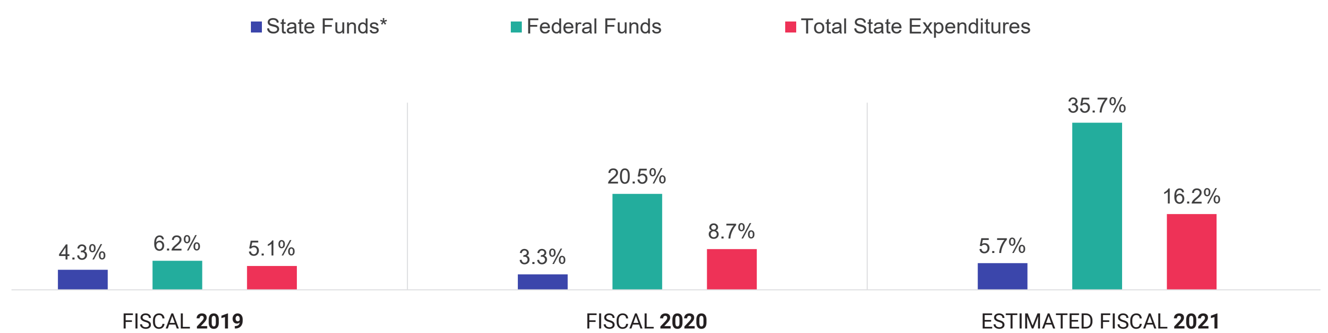
Overview: Total State Spending Grows at Highest Rate in Fiscal 2021, Largely Due to Additional Federal COVID-19 Aid

Total state spending reached $2.65 trillion in fiscal 2021, rising from $2.28 trillion in fiscal 2020. In fiscal 2021 it is estimated that total state spending grew 16.2 percent; the median rate was lower at 12.5 percent. Spending from states' own funds (general funds and other state funds combined, excluding bonds) rose 5.7 percent in fiscal 2021, while federal funds sharply increased 35.7 percent. The large increases in total state spending, led by strong gains from federal funds to states, is directly related to COVID-19 pandemic response and recovery efforts.

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 and continued to spend in fiscal 2021. Additionally, in March 2021, the *American Rescue Plan Act of 2021 (ARPA)* was signed into law, allocating $195.3 billion for states and the District of Columbia, and $4.5 billion for territories, through the Coronavirus State and Local Fiscal Recovery Fund (CSLFRF), in addition to multiple other funding allocations. While states have until the end of calendar year 2024 to allocate funds for CSLFRF, some states began allocating the funds towards the end of fiscal 2021. Over the past two fiscal years, states reported spending $427.9 billion in overall federal COVID-19 aid ($106.3 billion in fiscal 2020 and an estimated $321.6 billion in fiscal 2021). In fiscal 2021, both total state expenditures and federal funds to states are estimated to have grown at their highest rates in the 35-year history of the *State Expenditure Report*.

Total state spending grew by 8.7 percent in fiscal 2020, while the median rate was slightly lower at 7.0 percent. Spending from state funds rose 3.3 percent while federal funds once again sharply increased by 20.5 percent due to pandemic response efforts.

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.

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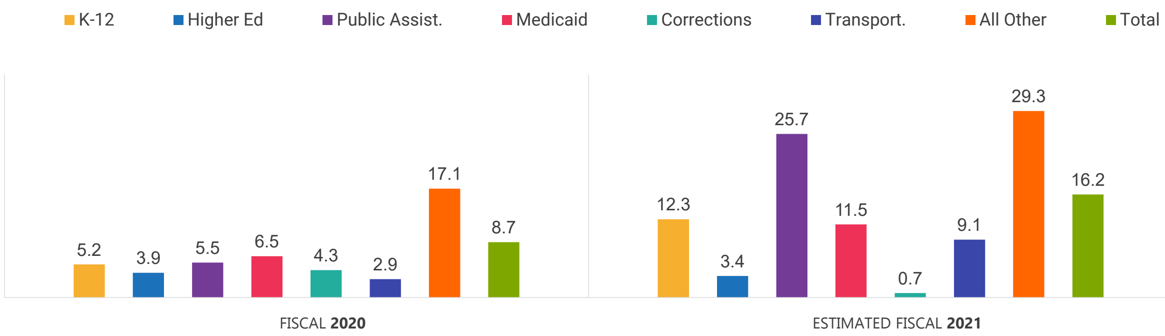
Total State Expenditures Percentage Spending Growth By Program Area



*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 2021

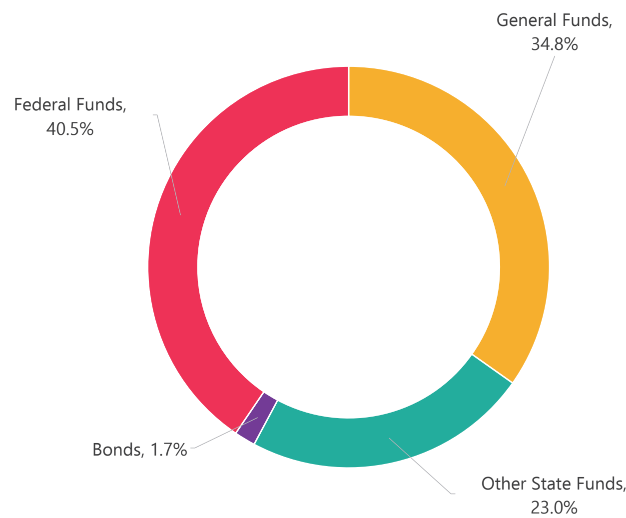
All eight program areas experienced an increase in total state spending in fiscal 2021, with the "all other" category seeing by far the largest gain, followed by public assistance, elementary and secondary education, and Medicaid. Many of the top expenditure areas for CARES Act funds fall under the "all 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. Additionally, states' initial plans for using Fiscal Recovery Funds under ARPA include many areas that fall under the "all other" category, such as: COVID-19 vaccination, testing, and other response costs; prevention in congregate settings; mental health services; other public health services; household assistance; unemployment benefits; contributions to unemployment insurance trust funds; job training assistance; small business economic assistance; aid to tourism, travel or hospitality; aid to other impacted industries; and broadband.

Federal Funds Represent Increased Share of Total State Spending

In fiscal 2021, federal funds represented 40.5 percent of total state spending, with general funds at 34.8 percent, other state funds at 23.0 percent, and bonds at 1.7 percent. This marks the first time in the history of the State Expenditure Report that federal funds have surpassed general funds as a share of total state spending. Federal funds have gone from representing 31.3 percent in fiscal 2019, to 34.7 percent in fiscal 2020, to an estimated 40.5 percent in fiscal 2021. Meanwhile, general funds have gone from representing 40.8 percent in fiscal 2019, to 38.8 percent in fiscal 2020, to an estimated 34.8 percent in fiscal 2021. However, state funds (general funds and other state funds combined) still make up a greater share of total state spending than federal funds, 57.8 percent compared to 40.5 percent.

Total State Expenditures By Fund Source

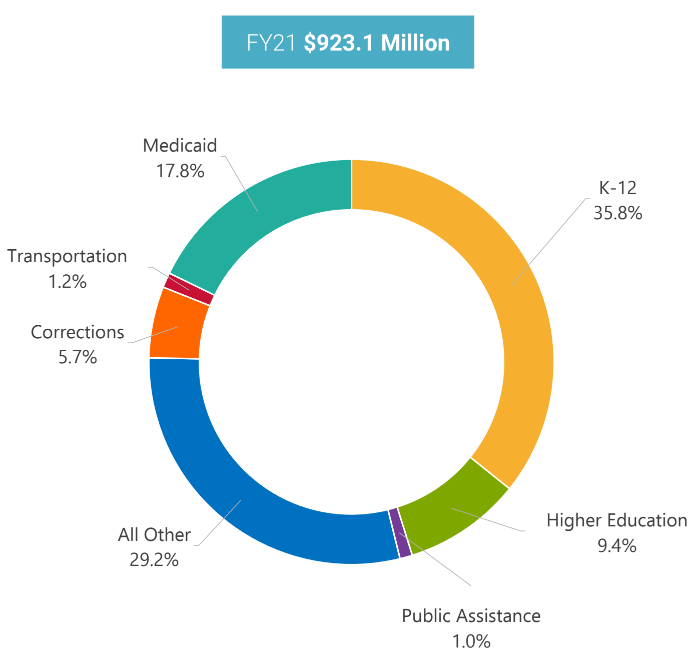
Estimated **Fiscal 2021**



General Fund Spending Grew Less than the Historical Average in Fiscal 2021

General fund spending grew an estimated 4.1 percent in fiscal 2021, less than the 43-year historical average for general fund spending reported in NASBO's *Fiscal Survey of States* of 5.3 percent. In fiscal 2020, general fund spending grew at a slightly slower rate of 3.4 percent. In both years, the median rate was lower at 2.0 percent in fiscal 2021 and 2.9 percent in fiscal 2020. In fiscal 2021, transportation and public assistance had the highest percentage growth at 32.3 percent and 21.7 percent respectively, while corrections spending declined 6.3 percent (federal funds for corrections, on the other hand, rose sharply). In fiscal 2020, the "all other" category had the highest growth rate at 8.5 percent, while transportation had the lowest rate, declining 9.9 percent. For transportation, general funds make up a very small percentage of overall transportation spending. Elementary and secondary education continued to represent the largest share of general fund spending in fiscal 2021.

General Funds Expenditures By Function



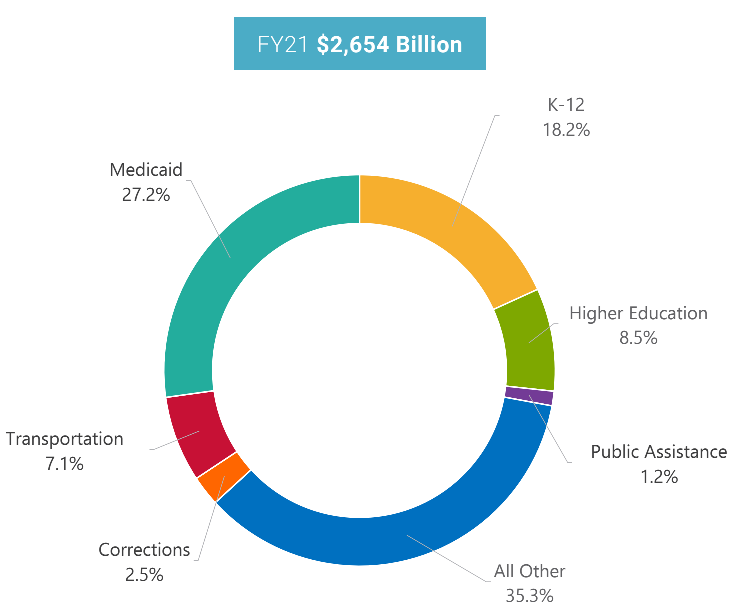
Additional state expenditure details and trends include:

- **Elementary and secondary education** total expenditures increased 12.3 percent in estimated fiscal 2021 and 5.2 percent in fiscal 2020. State funds for K-12 increased 3.9 percent in fiscal 2021 and 4.4 percent in fiscal 2020, while federal funds grew 63.6 percent in fiscal 2021 and 8.2 percent in fiscal 2020. State expenditures on K-12 education have been considerably impacted by the changing needs brought by the pandemic as well as the influx of additional federal aid in response to COVID-19. Early in the pandemic, some states enacted cuts to K-12 funding when they were forecasting considerable revenue declines. Overall, state spending reductions to K-12 education have been minimal during the pandemic, and those that did occur in some cases have since been restored as state fiscal conditions have improved. Also, in some instances, especially in fiscal 2021, spending decreases on K-12 education are connected to declining enrollment related to the pandemic, as much of state funding for schools is calculated on a per pupil basis. Meanwhile, state K-12 education expenditures have been affected by a significant increase in federal funding driven by federal aid to cover pandemic-related expenditure needs for K-12 education. States reported spending federal COVID-19 aid totaling at least $44 billion on K-12 education so far ($8.2 billion in fiscal 2020 and $36.3 billion in fiscal 2021).

- Total expenditures for **higher education** increased 3.4 percent in estimated fiscal 2021 and 3.9 percent in fiscal 2020. State funds for higher education are estimated to have increased 2.3 percent in fiscal 2021 and 2.6 percent in fiscal 2020, while federal funds rose 12.6 percent in fiscal 2021 and 13.3 percent in fiscal 2020. Regarding state funds, due to the early impacts of COVID-19 on revenue forecasts, some states had started to pull back on some recent investments in higher education. Nine states reported general fund spending decreases in fiscal 2020, though not all reductions may be related to the effects of the pandemic. In fiscal 2021, 20 states reported estimated general fund expenditure reductions for higher education compared to fiscal 2020, though most of these decreases were small and possibly in part due to reduced enrollment. Meanwhile, 20 states in fiscal 2020 and 21 states in fiscal 2021 reported reductions in other state fund expenditures for higher education. These reductions likely reflect in large part lower revenues from tuition and fees and auxiliary services due to the impacts of the pandemic; most but not all states include spending from tuition and fees in their other state funds expenditure data. The large increases in state higher education expenditures from federal funds over the past two years are driven by COVID-19 relief funding. States reported higher education expenditures from federal COVID-19 aid totaling $11.1 billion so far ($2.7 billion in fiscal 2020 and $8.4 billion in fiscal 2021).

- Total **public assistance** increased 25.7 percent in estimated fiscal 2021, after increasing 5.5 percent in fiscal 2020. State funds for public assistance are estimated to have increased 22.5 percent in fiscal 2021 and 0.7 percent in fiscal 2020, while federal funds rose 27.9 percent in fiscal 2021 and 9.0 percent in fiscal 2020. Increases in public assistance spending in both fiscal 2020 and fiscal 2021 were heavily driven by additional federal COVID-19 aid, with states reporting $4.8 billion in federal COVID-19 aid for public assistance in fiscal 2020, and an estimated $11.0 billion in fiscal 2021. Public assistance represented 1.2 percent of total state expenditures in fiscal 2021. 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 State Expenditures
By Function



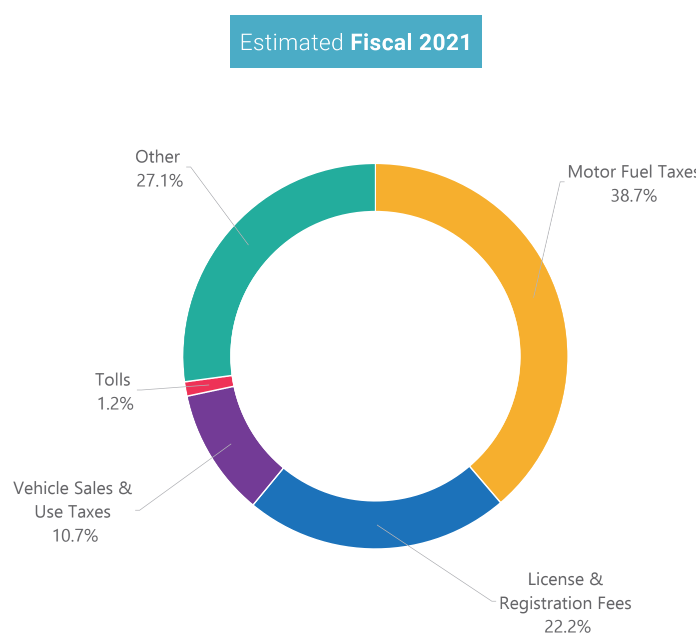
- Total **Medicaid** spending increased 11.5 percent in fiscal 2021, with state funds increasing 3.3 percent, and federal funds increasing 15.9 percent. In fiscal 2020, total Medicaid spending increased 6.5 percent with state funds increasing 0.5 percent and federal funds increasing 10.0 percent. Medicaid spending in fiscal 2020 and fiscal 2021 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, provides a 6.2 percentage point increase in Federal Medical Assistance Percentage (FMAP) spending during the public health emergency. The increase is conditioned on states meeting certain maintenance of effort requirements including continuous coverage for current enrollees. The increase in the FMAP is retroactive to January 2020 and is reflected in half of fiscal 2020 and in all of fiscal 2021 for most states. States reported $13.4 billion in fiscal 2020 and $26.5 billion in fiscal 2021 for COVID-19 federal relief aid from the increased Medicaid FMAP.

- Total **corrections** expenditures increased 0.7 percent in estimated fiscal 2021 and 4.3 percent in fiscal 2020. State funds for corrections are estimated to have declined 5.5 percent in fiscal 2021 and increased 0.8 percent in fiscal 2020, while federal funds rose 183.3 percent in fiscal 2021 and 348.8 percent in fiscal 2020. The large percentage increases in federal funds are related to the small amount of federal funds for corrections prior to COVID-19; for example, in fiscal 2019 federal funds only comprised $531 million out of $63.2 billion in total spending on corrections. The increase in federal funding is the result of several COVID-19 relief bills, including the CARES Act which permitted states to use federal funds to cover public safety payroll costs, including for correctional officers. States also received federal pandemic funds for specific purposes, such as $563.1 million from the U.S. Department of Justice for the Coronavirus Emergency Supplemental Program, allocated through the CARES Act. State funds (general funds and other state funds combined but excluding bonds) accounted for 88.9 percent of total state corrections spending in fiscal 2021, with federal funds accounting for 10.2 percent and bonds 0.9 percent. Corrections represented 2.5 percent of total state expenditures in fiscal 2021 and 5.7 percent of general funds.

- Total **transportation** spending, representing 7.1 percent of total state expenditures, increased 9.1 percent in estimated fiscal 2021 and 2.9 percent in fiscal 2020. In fiscal 2021, it is estimated that state funds spending rose 6.2 percent and federal funds 13.3 percent, while spending from bonds increased 17.7 percent. Other state funds, which are typically earmarked revenue sources such as fuel taxes, comprised 57.5 percent of total transportation spending in estimated fiscal 2021, with federal funds at 28.3 percent, bonds at 8.5 percent, and general funds only accounting for 5.7 percent. States estimate in fiscal 2020 they expended $1.1 billion in federal COVID-19 aid for transportation, while in fiscal 2021, federal COVID-19 aid for transportation purposes is estimated at $4.8 billion. In recent years states have been responding to the diminishing buying power of fuel tax revenues resulting from more fuel-efficient vehicles. 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, approximately two-thirds of 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. Additionally, states continue to explore road usage charges, or mileage-based user fees, with a growing number conducting pilot programs.

- 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 (38.7 percent), followed by license and registration fees (22.2 percent), vehicle sales and use taxes (10.7 percent), tolls (1.2 percent), and all other (27.1 percent). Transportation fund revenue sources totaled $107.4 billion in fiscal 2019, $105.4 billion in fiscal 2020, and $110.1 billion in estimated fiscal 2021.

Transportation Fund Revenue Source



- The **"all other"** category of state spending increased 29.3 percent in estimated fiscal 2021, with state funds (excluding bonds) rising 10.4 percent and federal funds increasing 72.8 percent. In fiscal 2020, total spending in the "all other" category rose 17.1 percent, with state funds increasing 4.9 percent and federal funds rising 61.3 percent. In both fiscal 2020 and fiscal 2021, total state spending for the "all other" category had the highest growth rate among all spending categories. The sizeable increase in "all other" spending is largely due to additional federal aid states received in response to the COVID-19 pandemic. States estimate in fiscal 2020 they expended $73.2 billion in federal COVID-19 aid for "all other", while in fiscal 2021, federal COVID-19 aid for "all other" purposes is estimated at $226.4 billion. Many of the top expenditure categories 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. Additionally, states' initial plans for using Fiscal Recovery Funds under ARPA include many areas that fall under the "all other" category, such as: COVID-19 vaccination, testing, and other response costs; prevention in congregate settings; mental health services; other public health services; household assistance, unemployment benefits; contributions to unemployment insurance trust funds; job training assistance; small business economic assistance; aid to tourism, travel or hospitality; aid to other impacted industries; and broadband. Along with substantial increases in federal funds over the past two years, state funds in the "all other" category have also seen growth resulting from prior budget surpluses and continued revenue growth.

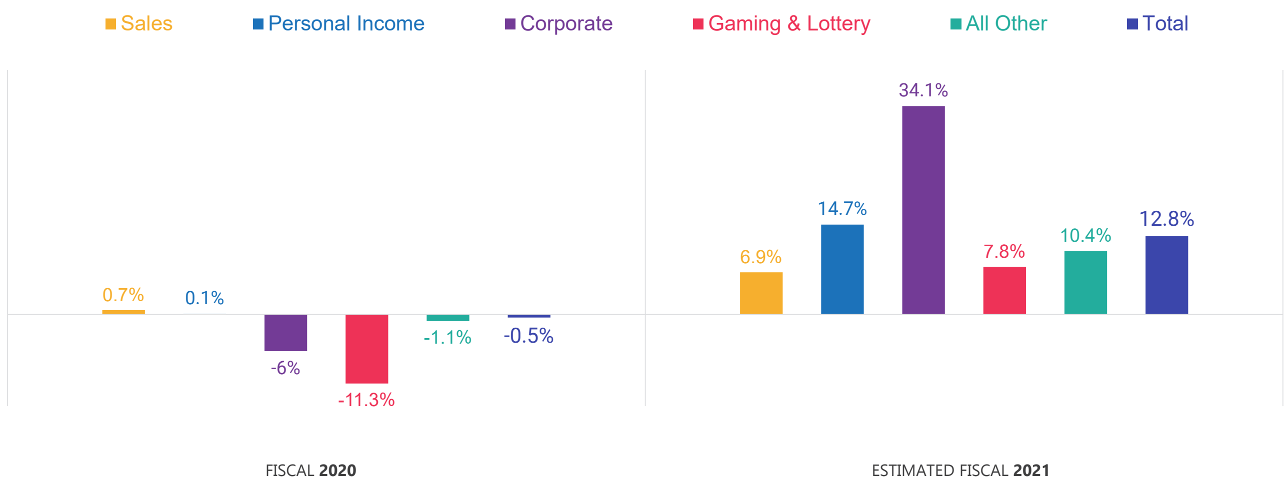
- States were also asked to separately detail their **debt service** spending. States' spending on debt service totaled $50.7 billion in fiscal 2019, $47.8 billion in fiscal 2020, and $55.9 billion in estimated fiscal 2021. In estimated fiscal 2021, general funds represented 76.0 percent of total state spending on debt service, while other state funds comprised the remaining 24.0 percent. In fiscal year 2021, debt service represented 3.6 percent of spending from state funds (general funds and other state funds combined, excluding bonds), and 4.6 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 by an estimated 9.1 percent in fiscal 2021, 4.7 percent in fiscal 2020, and 6.1 percent in fiscal 2019. The fiscal 2021 growth rate of 9.1 percent is the highest annual figure in the last 15 years. Capital spending will likely maintain high growth rates for the next several years as states allocate funding from ARPA. Under ARPA, states and localities are permitted to use federal funding for investments in infrastructure, including water, sewer, and broadband services. States primarily use dedicated sources like the transportation fund, higher education tuition and fees, set-aside funding for capital projects, federal funds, and fund surpluses to finance capital spending. State cash sources represent 45.3 percent of capital spending in fiscal 2021, federal funds are 26.4 percent, and bonds are 28.3 percent. The vast majority of federal funds spent for capital purposes is for transportation (91.6 percent in fiscal 2021).

State General Fund Revenues Rose Sharply in Fiscal 2021 After Declining in Fiscal 2020

General fund revenue, the largest source of state expenditures and the most discretionary, totaled an estimated $988.2 billion in fiscal 2021. Unlike fiscal 2020, when state revenues declined for the first time since fiscal 2010, state revenues rose sharply in fiscal 2021, increasing by an estimated 12.8 percent. Several factors help explain recent improvements in states' revenue outlooks, including: federal stimulus measures infused additional money into the economy, which helped to lessen state revenue losses; high-income earners have been relatively insulated from the COVID-19 pandemic's economic effects, which has limited impacts on personal income tax collections; the types of consumption most curtailed by the pandemic comprise a relatively small portion of states' sales tax bases; and the ability to tax online sales following the U.S. Supreme Court decision in Wayfair v. South Dakota. Fiscal 2021 revenue collections were also impacted by the shifting of the 2020 tax deadline from April 15 to July 15. . According to NASBO's Spring 2021 *Fiscal Survey of States*, 19 states reported they recognized these delayed revenues due to the deadline shift in fiscal 2021 instead of fiscal 2020, depressing fiscal 2020 revenues and leading to higher collections in fiscal 2021. The lower fiscal 2020 revenue totals also helped lead to higher year-over-year

Revenue Growth By Percentage
State General Funds



percentage growth for fiscal 2021. As a result of the preceding factors, most states saw strong year-over-year growth in overall tax collections for fiscal 2021, with 29 states reporting double digit increases. When looking at 50-state totals, all revenue sources tracked in this report experienced growth in fiscal 2021 including sales tax (6.9 percent), personal income tax (14.7 percent), corporate income tax (34.1 percent), gaming and lottery revenue (7.8 percent), and all other general fund revenue (10.4 percent).

In fiscal 2020, general fund tax collections declined 0.5 percent 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 had sharp revenue declines in the fourth quarter of fiscal 2020 (April-June) resulting from the impact of the COVID-19 pandemic. As previously noted, fiscal 2020 revenues – particularly personal income and corporate income tax collections - were also negatively impacted by the shifting of the federal tax deadline from April 15 to July 15, which caused some revenues to be shifted to fiscal 2021 in a number of states. Personal income tax collections only grew 0.1 percent in fiscal 2020 even though withholding collections were buoyed by temporary stimulus measures provided by the federal government, including enhanced unemployment insurance benefits. Additionally, the Paycheck Protection Program loans helped keep many individuals employed and paying income taxes. Sales tax collections only grew 0.7 percent despite the strong start to the fiscal year and the impact of temporary federal stimulus measures on spending levels. Corporate income taxes declined 6.0 percent even as stimulus measures such as the Paycheck Protection Program sought to keep companies operating. Gaming and lottery revenues experienced a 11.3 percent decline partly due to the closure of casinos and other gambling establishments during the pandemic. Finally, the "all other" category of general fund revenue declined 1.1 percent, with oil producing states seeing sharp drops in severance taxes.

Outlook

Looking forward, state revenue collections are expected to continue to grow in fiscal 2022, although at a lower rate than fiscal 2021 when states saw exceptionally strong year-over-year growth due to a unique set of circumstances, including the shifting of the federal tax deadline. States will also continue to carefully plan how best to spend federal aid to help the individuals and businesses most impacted by the pandemic, while also working to foster a strong economic recovery. Although state fiscal conditions are expected to remain stable in fiscal 2022, future state budgets will need to contend with the one-time nature of much of the additional federal aid and a shifting economic landscape brought on by the pandemic, as well as both new and ongoing spending pressures.

If you would like additional information, please contact Brian Sigritz (bsigritz@nasbo.org or 202-624-8439).

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 2021, actual fiscal 2020, and actual fiscal 2019. 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.