
Budgeting: Federal and State Issues

June 19, 2013

Objectives

- ▶ Discuss Budget Importance
- ▶ Fiscal Cliff/State of Economy
- ▶ CBO Estimates /Long-Term Outlook
- ▶ State Outlook: Tennessee and Virginia

Budgeting (continued)

Where are you going???????

How can you get there???????



Fiscal cliff???



Budgeting (continued)

Why so important in government and not for profits?



Budgeting (continued)

- Generally, no direct revenue/expense relationships (supply & demand)
- No excess capital/stockholders' equity to depend on
- Limits on borrowing
- Requirements for appropriation of expenses

Budgeting (continued)

- Budgeting Needed to**
- **Control Limited Resources**
 - **Provide Means to Achieve Goals**
 - **Evaluate Performance**
 - **Communicate plans to various responsibility centers / department managers**

Congressional Budget Office (CBO)

- ▶ The Budget and Economic Outlook: Fiscal Years 2013 to 2023.

Congressional Budget Office

- ▶ CBO anticipates a gradual improvement in many of the forces that drive the economy is offset by the effects of budgetary changes that are scheduled to occur under current law.
- ▶ After this year, economic growth will speed up, causing employment rate to decline and inflation & interest rates to rise.

Congressional Budget Office:

- ▶ Unemployment rate is expected to remain above 7 ½ percent through next year.
- ▶ CBO's baseline:
 - Deficits continue to shrink over the next few years
 - Deficits are projected to increase later in the coming decade (because of pressures of an aging population, rising health care costs, expansion of federal subsidies for health insurance and growing interest payments on federal debt.)

Congressional Budget Office

- ▶ CBO's baseline:
 - ▶ As a result, federal debt held by the public is projected to remain historically high relative to the size of the economy for the next decade.

Congressional Budget Office

▶ Revenues

- Federal revenues will increase roughly 25% between 2013 and 2015
 - Rise in income because of growing economy, from policy changes that are scheduled to take effect and from policy changes in effect but whose full impact on revenues will not be felt until after this year (recent increase in tax rates on income above certain thresholds).
 - Revenues projected to grow from 15.8% of GDP in 2012 to 19.1% of GDP in 2015 (compared with an average of 17.9% of GDP over the past 40 years).

Congressional Budget Office

▶ Outlays

- Federal spending rises over the next few years in dollar terms but falls relative to the size of the economy
- Growth of spending will be restrained by the strengthening of economy (as spending for programs such as unemployment compensation drops) and by provisions of the Budget Control Act of 2011.

Congressional Budget Office

- ▶ Outlays are projected to decline from 22.8% of GDP in 2012 to 21.5% by 2017
- ▶ After 2017, if current law remains in place, outlays will start growing again as a percentage of GDP because...

Congressional Budget Office

- Aging population
- Increasing health care costs
- Expansion of eligibility for federal subsidies for health insurance will boost spending for SS & major health care programs
- Increasing interest rates

Congressional Budget Office

- ▶ CBO expects that economic activity will expand slowly this year with real GDP growing just 1.4%
 - Fiscal tightening
 - Expiration of the 2% point cut in SS payroll tax
 - Increase in tax rates on income above certain \$
 - Automatic reductions in spending

Congressional Budget Office

- ▶ That subdued growth will:
 - Limit business' need to hire additional workers, thereby causing unemployment rate to stay near 8%

Congressional Budget Office

- ▶ Economic Outlook for 2014 to 2018
- ▶ CBO projects 3.4% growth in 2014 and an average of 3.6% a year from 2015 through 2018 based upon...

Congressional Budget Office

- ▶ CBO expects that the effects of the housing & financial crisis will continue to fade and that an upswing in housing construction, rising real estate, and stock prices and increasing availability of credit will help spur a cycle of faster growth in employment, income, consumer spending and business investment.

Congressional Budget Office

- ▶ Economic Outlook: 2019 to 2023
- ▶ Assumptions:
 - Growth of labor force will slow down (retirement of baby boomers)
 - Projects unemployment rate will fall to 5.2% by 2023 and that inflation & interest rates will stay at about their 2018 levels.

Congressional Budget Office

- ▶ Economic Outlook: 2019 to 2023
- ▶ CBO does not attempt to predict the ups & downs of the economy
- ▶ Assumptions:
 - GDP will stay at its max sustainable level – CBO projects that both actual & potential real GDP will grow at average rate of 2 ¼ % a year between 2019 and 2023

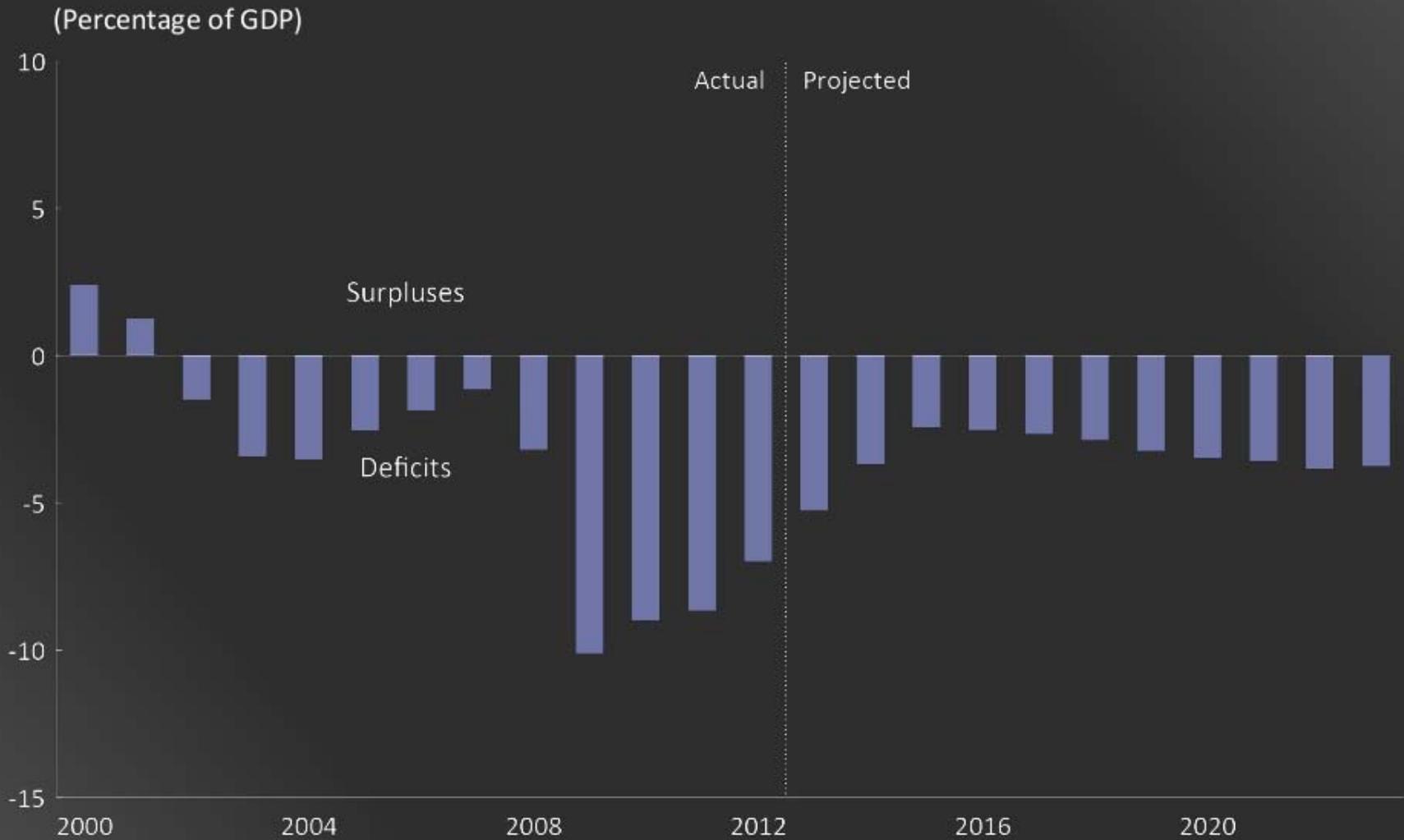
Congressional Budget Office

- ▶ CBO estimates the federal budget deficit will total \$845 billion in fiscal year 2013.
- ▶ First time since 2008 that the budget shortfall would be less than \$1 trillion

Congressional Budget Office

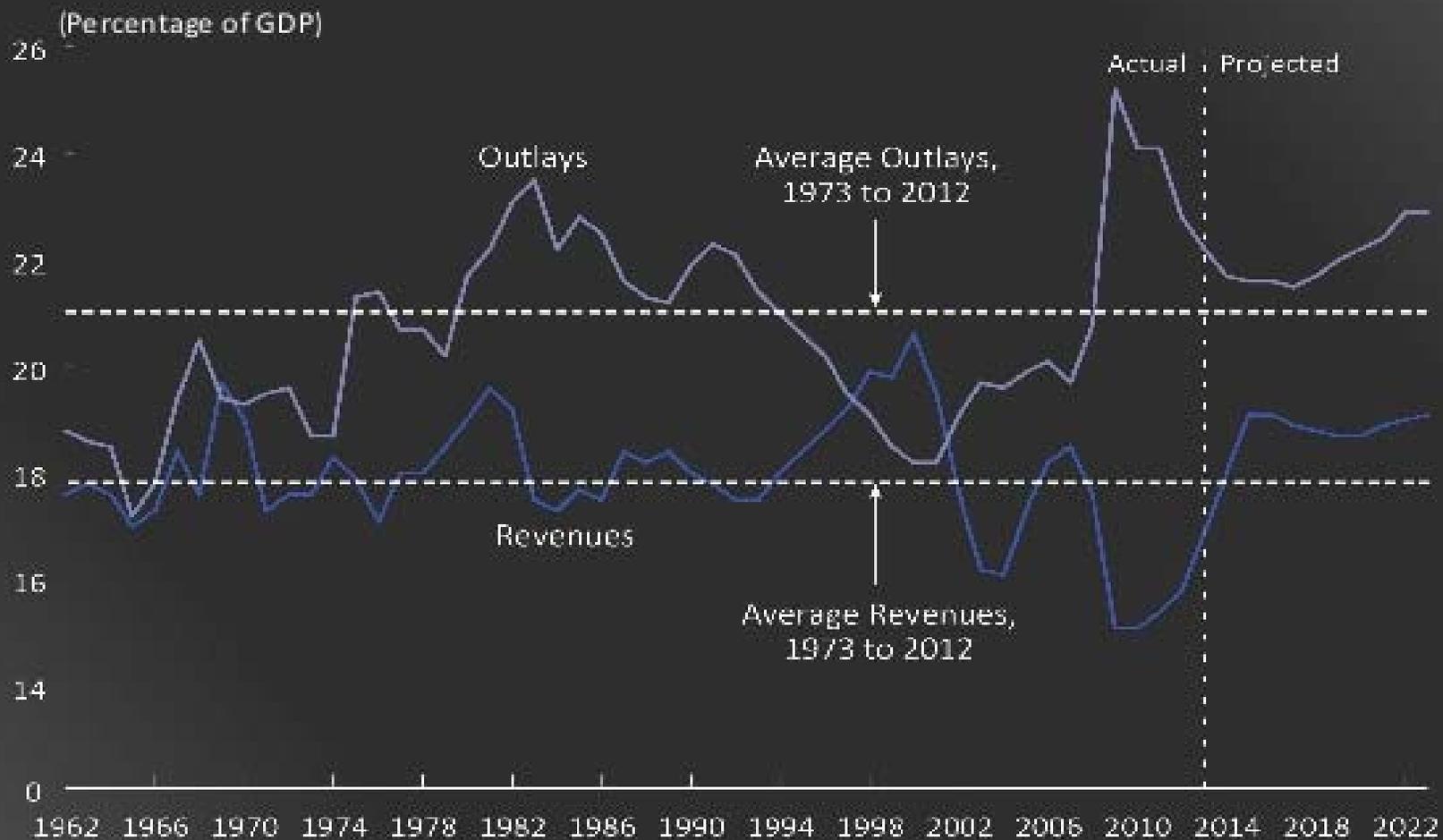
- ▶ At 5.3% of GDP, that deficit will be well below the peak of 10.1% in 2009.
- ▶ Debt held by the public is estimated to increase to 76% of GDP by the end of 2013, the largest ratio since 1950.

Total Federal Deficits or Surpluses



Estimates from *The Budget and Economic Outlook: Fiscal Years 2013 to 2023* (February 2013).

Total Federal Revenues and Outlays

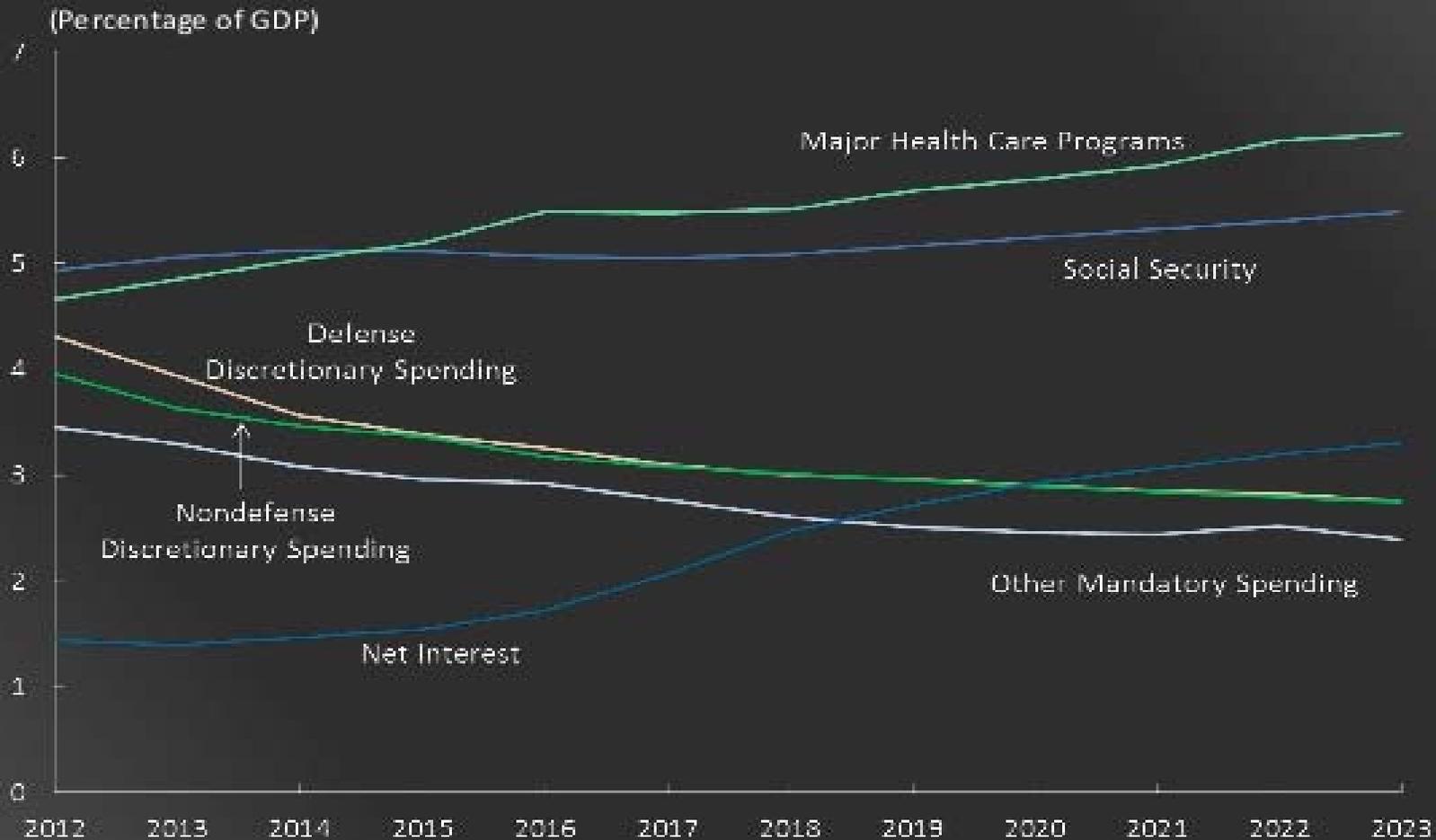


Estimates from *The Budget and Economic Outlook: Fiscal Years 2013 to 2023* (February 2013).



CONGRESSIONAL BUDGET OFFICE

Projected Growth in Major Federal Spending Categories



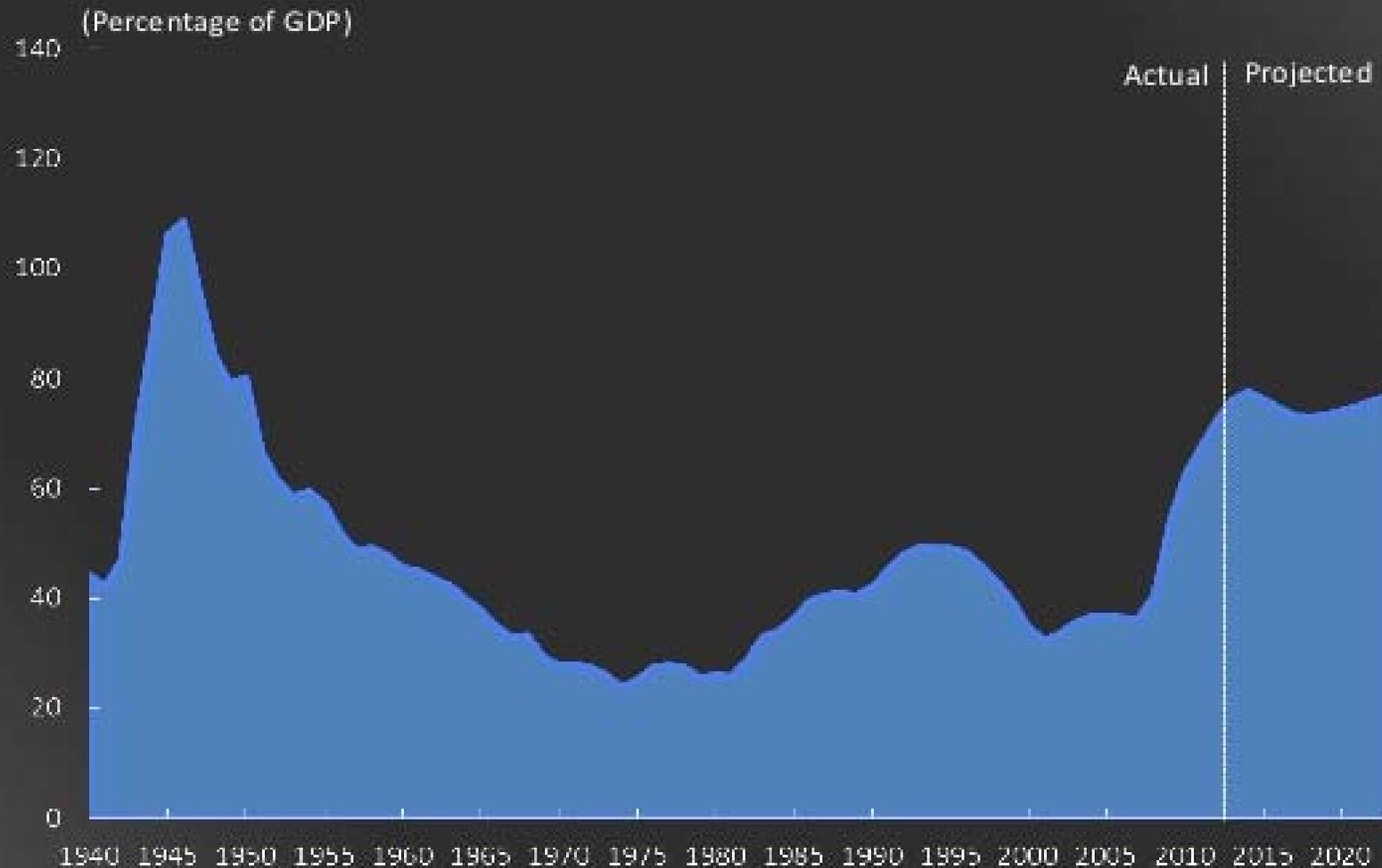
Estimates from *The Budget and Economic Outlook: Fiscal Years 2013 to 2023* (February 2013).



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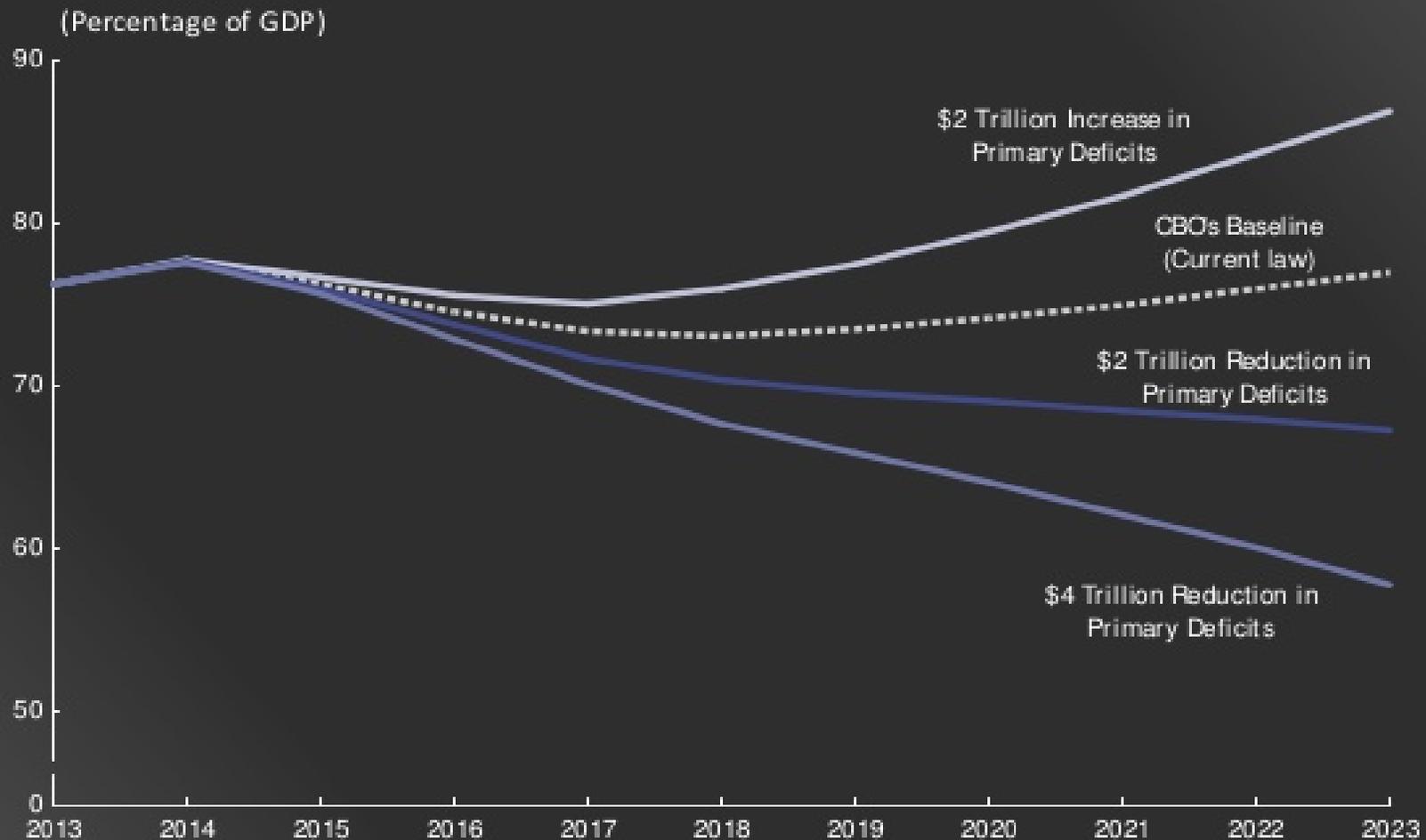
Federal Debt Held by the Public



Estimates from *The Budget and Economic Outlook: Fiscal Years 2013 to 2023* (February 2013).



Debt Held by the Public Under Current Law and Alternative Budgetary Paths



Estimates from *Macroeconomic Effects of Alternative Budgetary Paths* (February 2013).

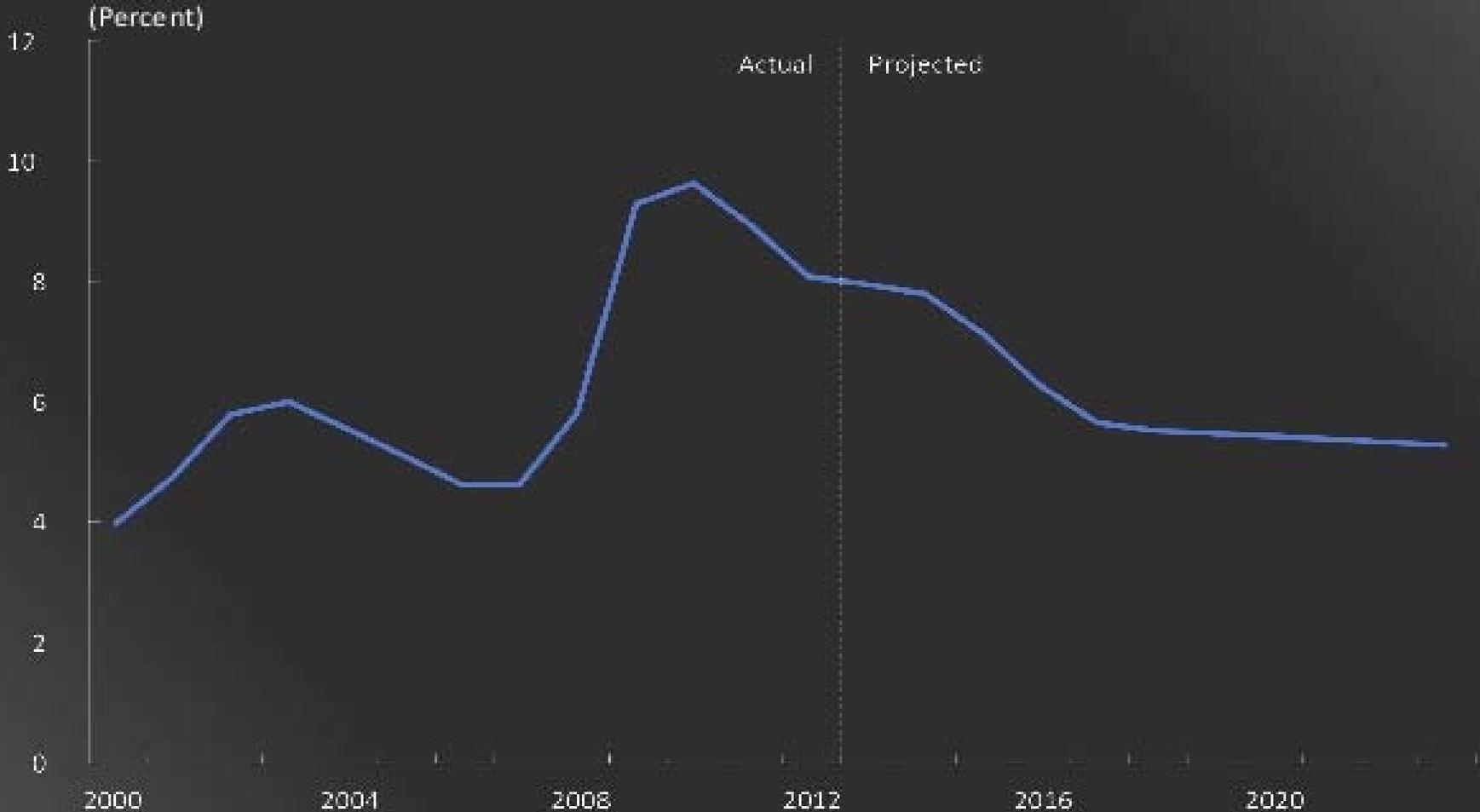
Consequences of High & Rising Debt

- ▶ Crowding out of capital investment will be greater
 - ▶ Lawmakers will have less flexibility to respond to unexpected challenges
 - ▶ Heightened risk of a fiscal crisis.
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- ▶ Source: CBO: *The Budget Outlook: Presentation to the National Association for Business Economics*. Douglas W. Elmendorf: March 4, 2013.

Criteria for Evaluating Proposed Policy Changes

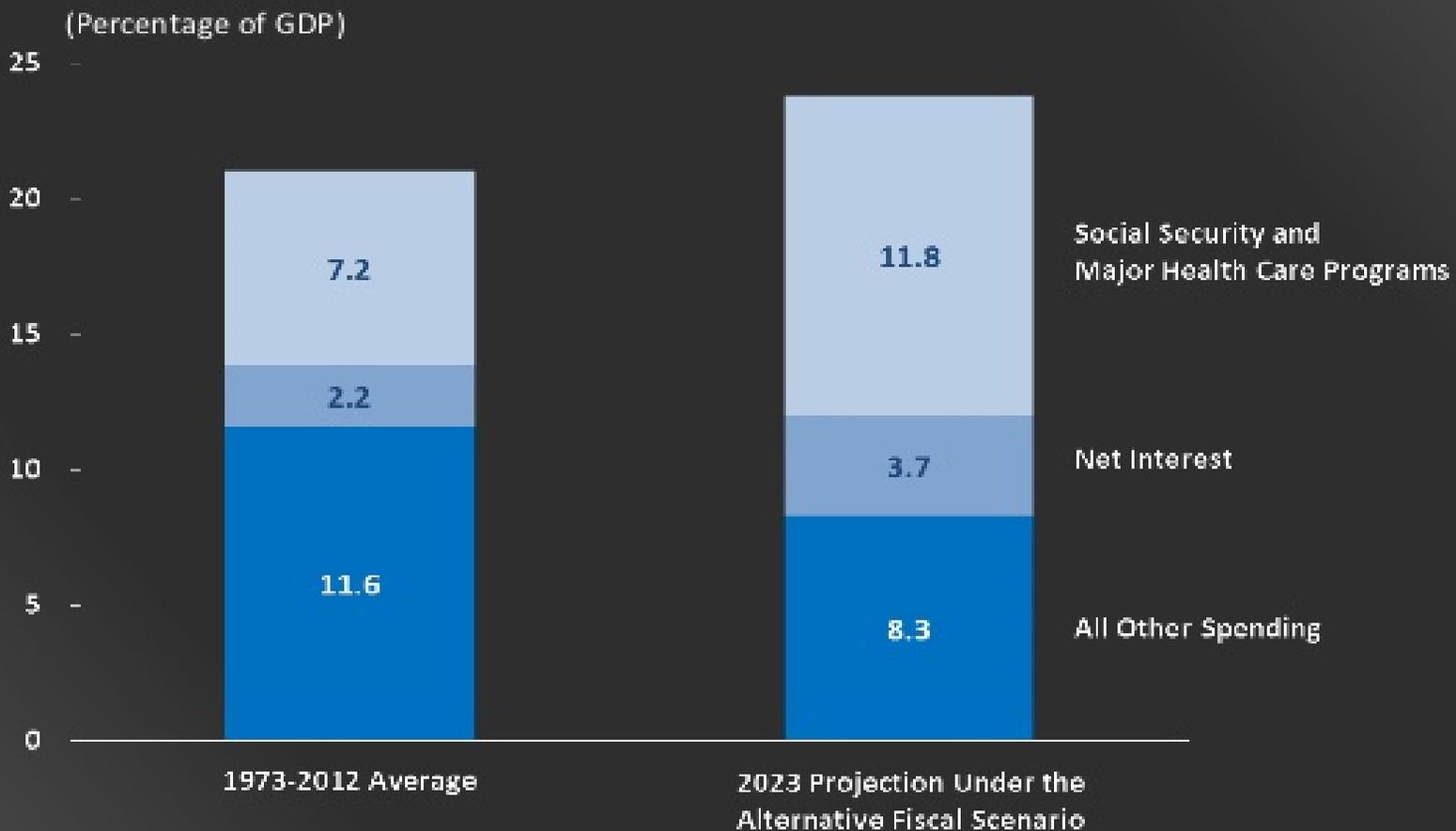
- ▶ The more that debt is reduced, the more that the harms caused by high debt would be avoided --- but--- also the greater the loss of government benefits and services or the burdens on individuals and businesses of higher taxes.
- ▶ Source: CBO: *The Budget Outlook: Presentation to the National Association for Business Economics*. Douglas W. Elmendorf: March 4, 2013.

Unemployment Rate



Estimates from *The Budget and Economic Outlook: Fiscal Years 2013 to 2023* (February 2013).

Criterion 3: How Would the Government's Resources Be Allocated?



Estimates from *The Budget and Economic Outlook: Fiscal Years 2013 to 2023* (February 2013).



Congressional Budget Office

- ▶ Source: Federal Grants to State and Local Governments – March 2013
- ▶ In Fiscal Year 2011, the federal government provided \$607 billion in grants to state and local governments.
- ▶ 17% of federal outlays
- ▶ 4% of GDP
- ▶ 25% of spending by state and local governments

Congressional Budget Office

- ▶ In total, the federal government reported outlays in 2011 for more than 200 intergovernmental grant programs, which were administered by 30 federal departments and independent agencies.

Congressional Budget Office

- ▶ In 1960, grants accounted for 7.6% of all federal outlays and 1.4% of GDP
- ▶ In 2011, grants accounted for 16.8% of all federal outlays and 4.1% of GDP.
- ▶ In the 1960s and 1970s, spending on grants generally increased after the creation of Medicaid and the introduction of other grant programs for low-income households during that period.

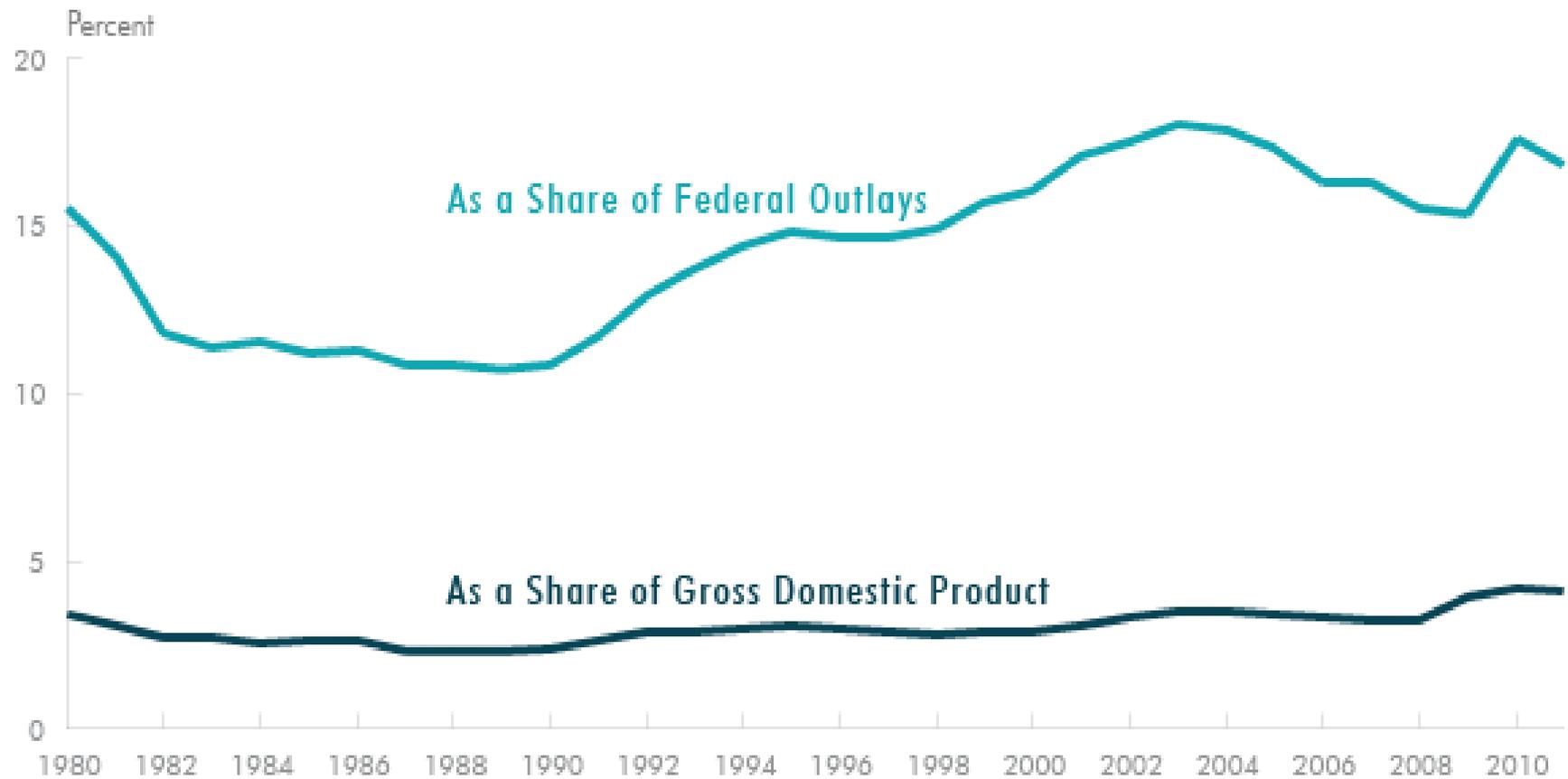
Congressional Budget Office

- ▶ Much of the increase in outlays as a share of GDP over the past several years can be attributed, in part, to grants provided to state and local governments under ARRA and subsequent extensions of some provision of that legislation.

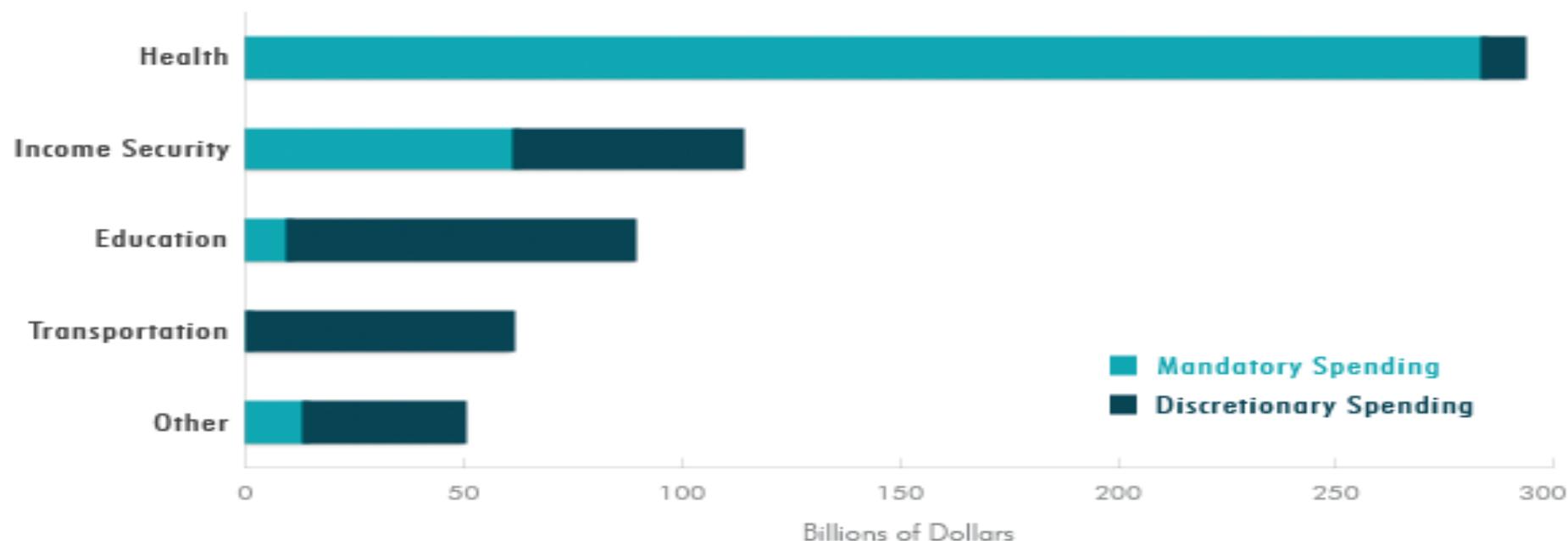
Congressional Budget Office

- ▶ GAO: \$264 billion in ARRA funds was paid out to states and local governments as of January 18, 2013.

Federal Grants to State and Local Governments



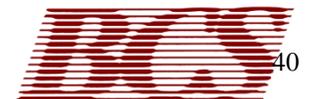
Outlays for Federal Grants to State and Local Governments, by Budget Function and Type of Spending, 2011



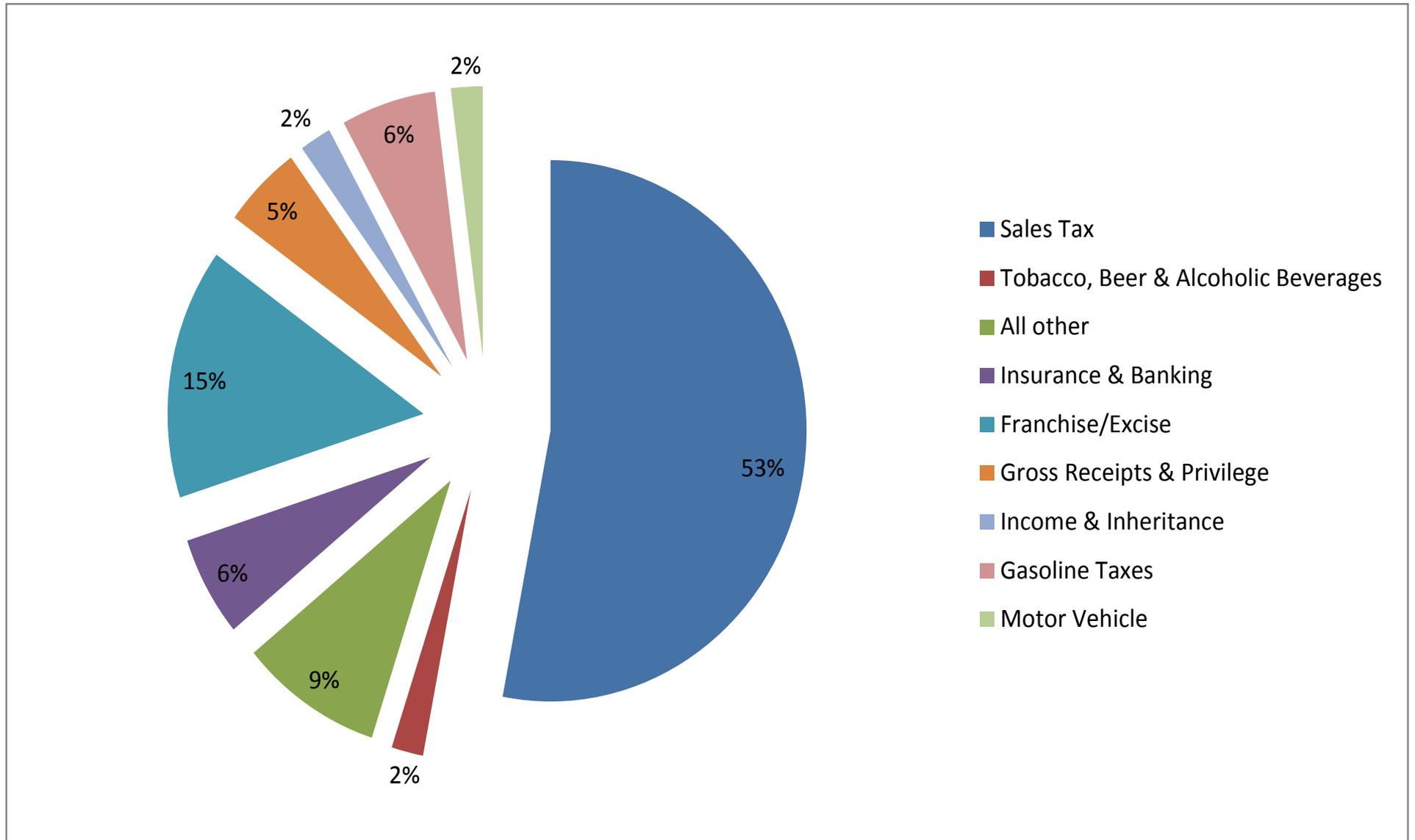
Notes: For the purposes of organizing the budget, federal resources are grouped into 20 general-subject categories—referred to as budget functions—so that all budget authority and outlays can be presented according to the national interests being addressed.

“Other” includes the following budget functions: national defense, international affairs, energy, natural resources and environment, agriculture, commerce and housing credit, community and regional development, Social Security, veterans benefits and services, administration of justice, and general government.

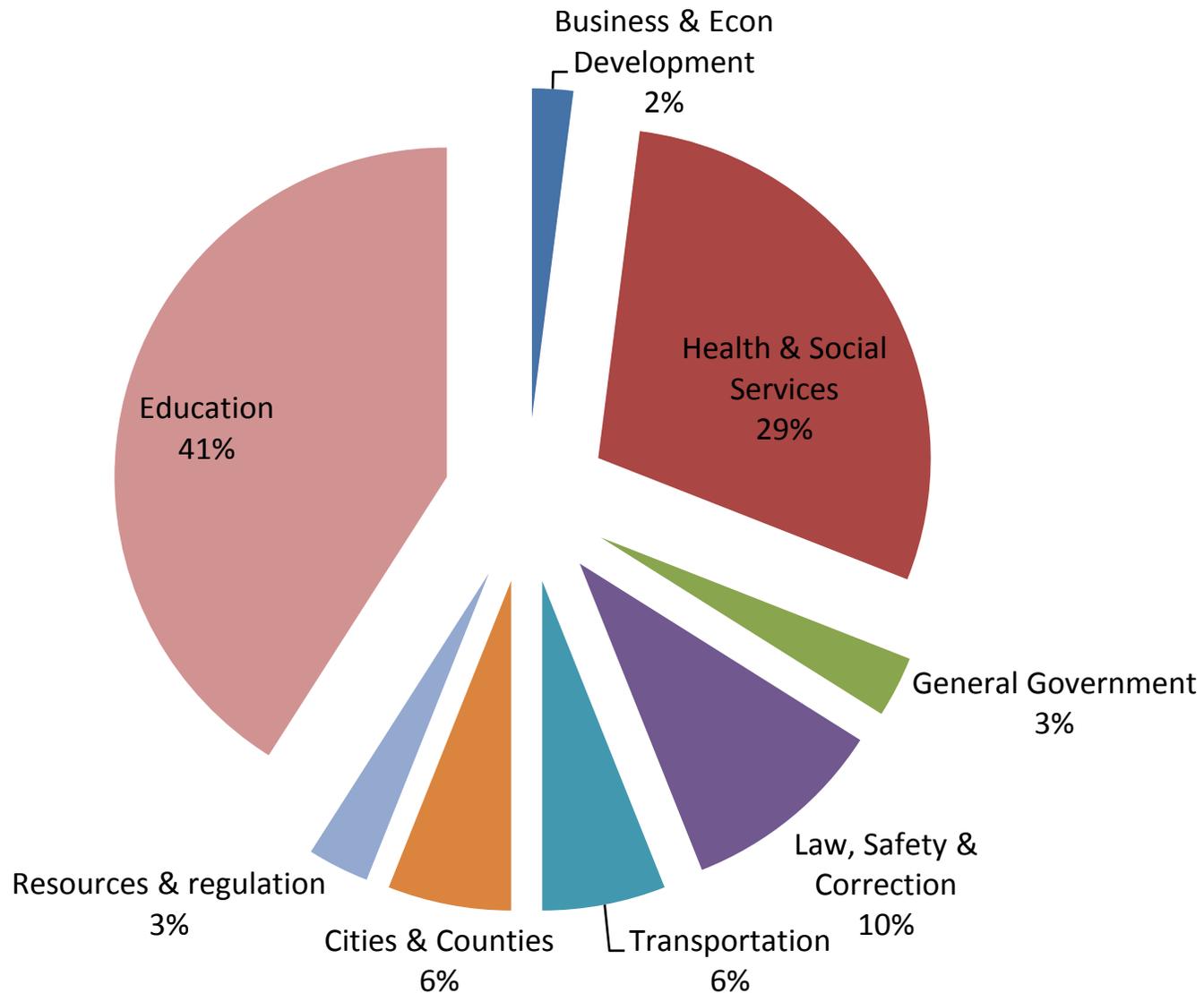
State of Tennessee



State of Tennessee: Where your state tax dollar comes from...



State of Tennessee: where does your state tax dollar go



State of Tennessee:

- ▶ SOURCE: Comptroller of the Treasury: Quarterly Fiscal Affairs Report (volume 2, Number 1, February 2013)
- ▶ State law directs the Comptroller to make quarterly reports concerning the state's fiscal affairs

State of TN: Fiscal Affairs

- ▶ First Five Months of the current FY: General Fund Collections increased 3.63% over collections from the same period during the previous year
- ▶ Current State debt is not excessive

State of TN: Fiscal Affairs

- ▶ Budgeted for payment of principal and interest on state-issued bonds.
- ▶ State's retirement plan is sound
- ▶ Post-employment benefit obligation for retirees is manageable
- ▶ State's unemployment trust fund is solvent

State of TN: Revenue Projections

- ▶ General Fund revenue growth: 1.98% to 2.85% for FYE June 30, 2013 and from 2.74% to 3.89% for FYE June 30, 2014
- ▶ As of June 30, 2012, the Reserve for Revenue Fluctuations (Rainy Day Fund) had a balance of \$306 million.

State of TN: Revenue Projections

- ▶ “The rainy day fund has not been adequately restored. This office believes the reserve amount should be increased.” – State of TN Comptroller of the Treasury, Quarterly Fiscal Affairs Report (volume 2, Number 1, Feb. 2013).

State of TN: Federal Cuts & Funds

- ▶ TN's budget is approximately \$32.6 billion, of which slightly more than \$12 billion is attributable to state taxes, and about \$12.3 billion is from federal funds.
- ▶ “If federal funds were to be reduced, services the state is able to deliver could be significantly impacted.”

State of TN: Fiscal Affairs – TCRS

- ▶ “Superb management has put TCRS in a very good position in comparison to the plans of other states.”
- ▶ “It is essential that the TCRS and the General Assembly continuously review the plan to provide reasonable benefits while containing costs.”

State of TN: Fiscal Affairs – Education

- ▶ Basic Education Program (BEP) – state’s funding formula for K–12 education.
- ▶ BEP consumes \$4 billion or 40% of the taxes in the general and education funds.

State of TN: Fiscal Affairs – Education

- ▶ “The formula for determining BEP funding should be transparent, verifiable and understandable. Our review shows this complicated formula is none of these.”

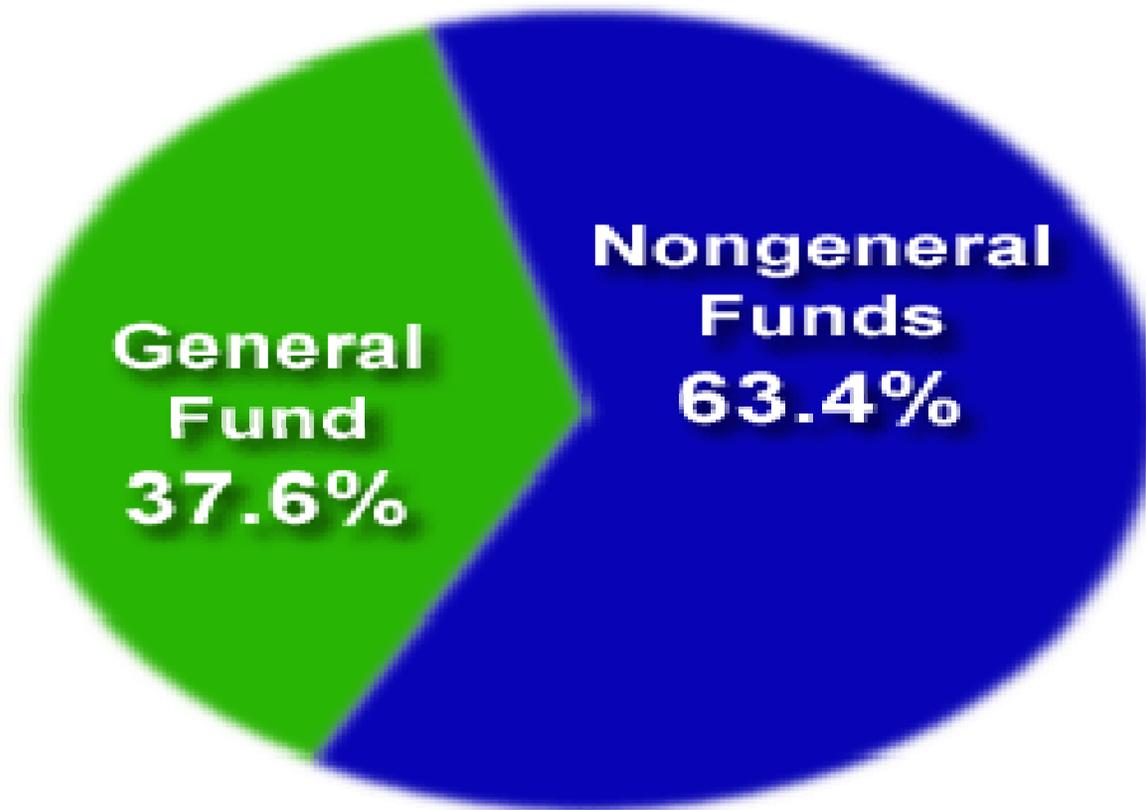
State of TN

- ▶ SOURCE: Comptroller of the Treasury: Quarterly Fiscal Affairs Report (volume 2, Number 1, February 2013)

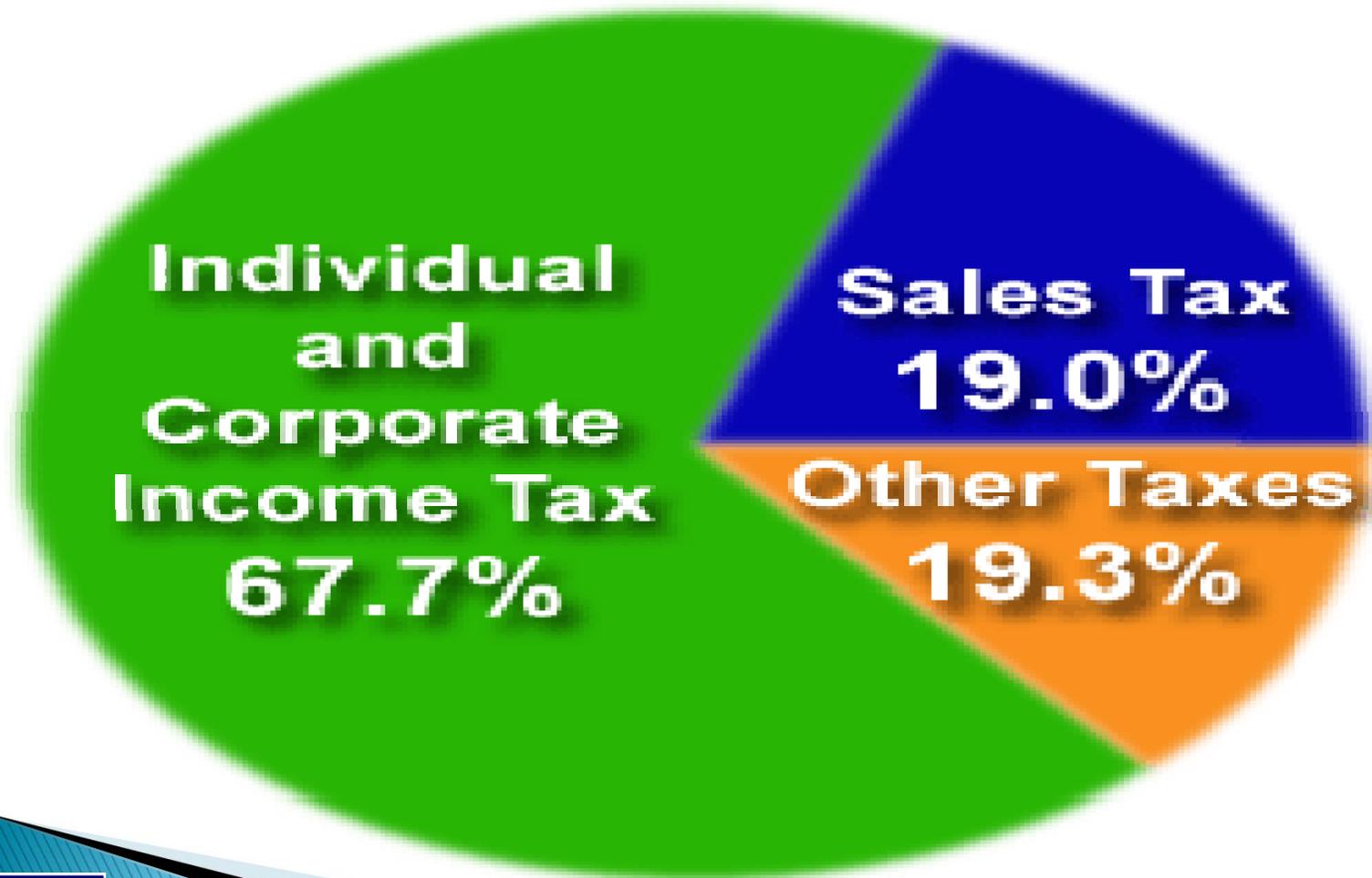
Commonwealth of Virginia



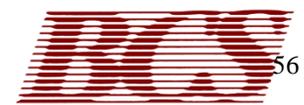
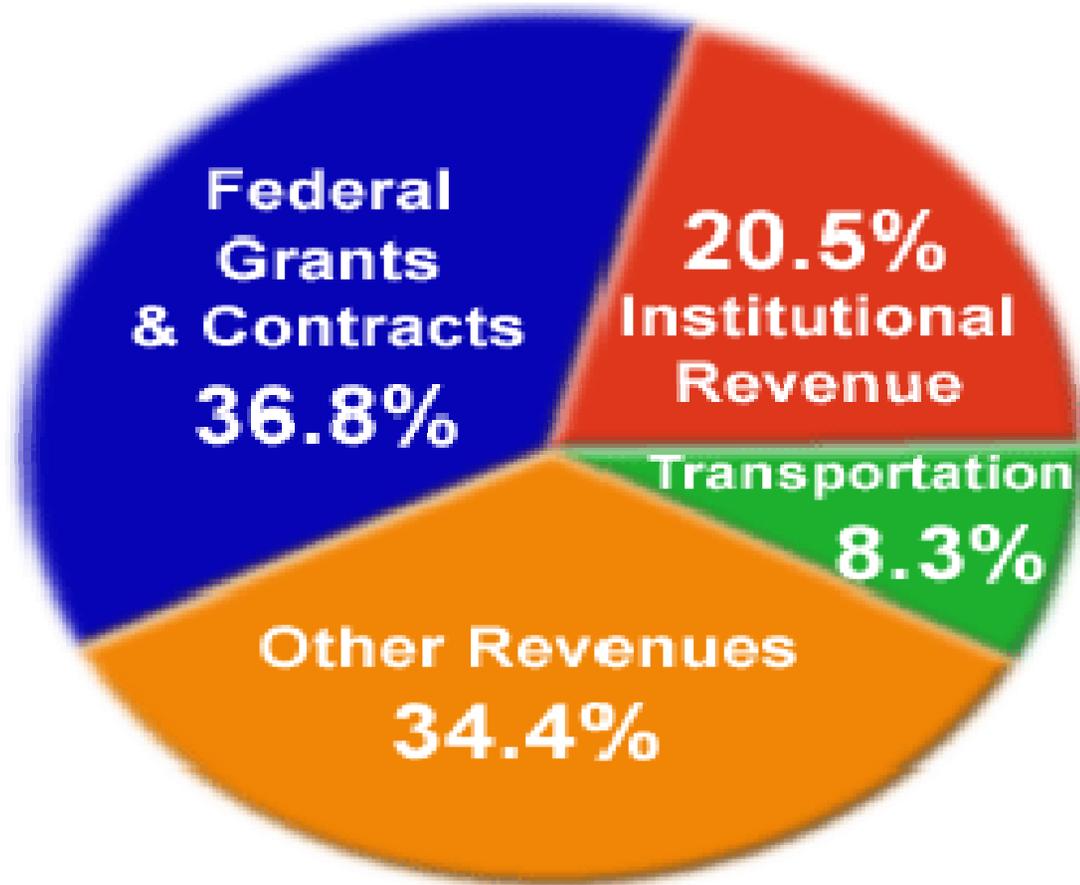
Virginia: Where does the money come from...



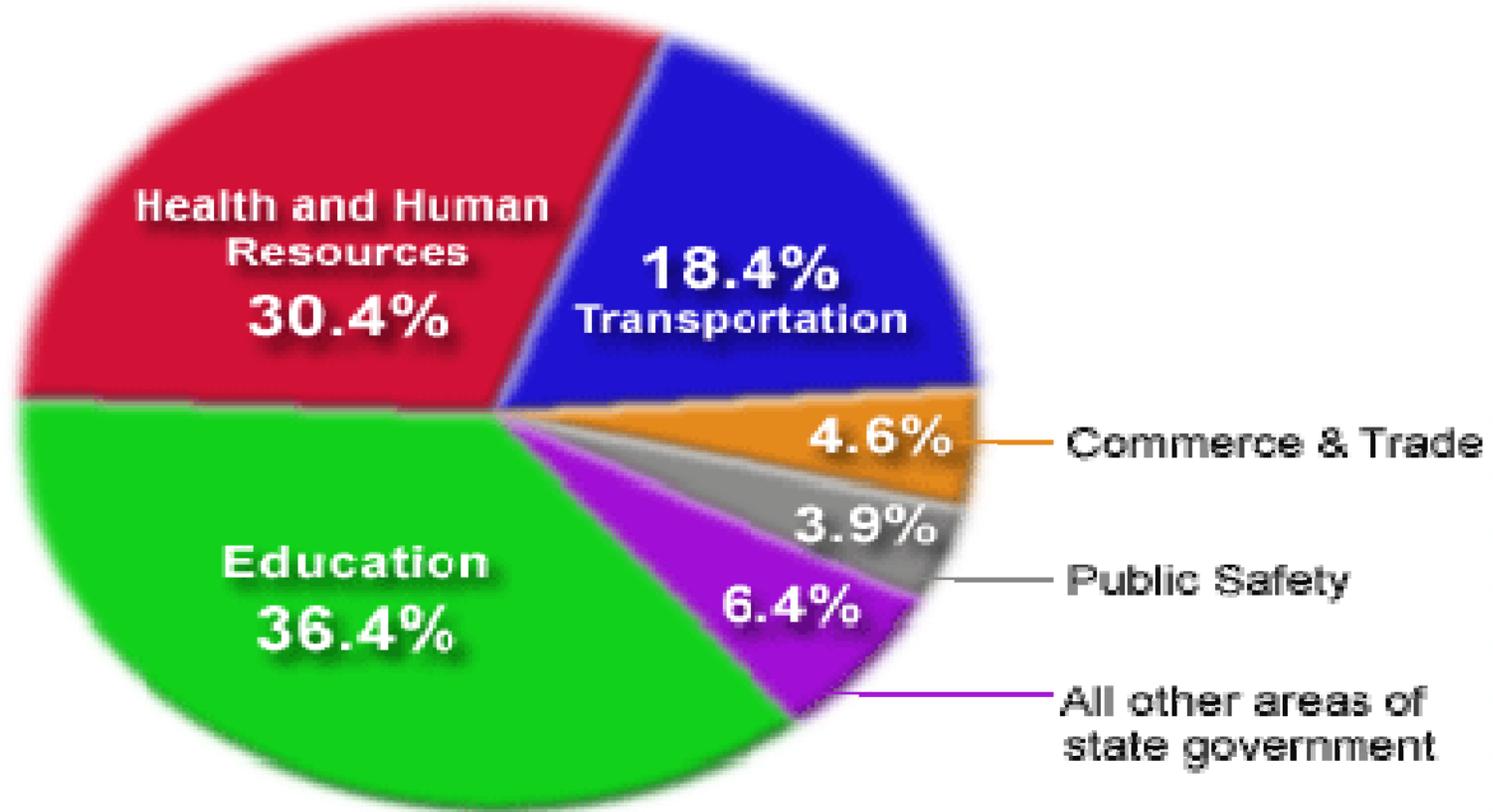
Virginia: General Fund Sources



Virginia: Nongeneral fund revenues



Virginia: Where does the money go?



Virginia

- ▶ Virginia economy was expected to grow at a pace similar to that of FY 2012
- ▶ Total personal income increased 4%
- ▶ Income from wages & salaries grew 2.6% (lagging the forecast of 3.3%)
- ▶ In FY 2012: total general fund revenues grew 5.4% (exceeding the official forecast of 4.5%)

Virginia – Forecasts

- ▶ Personal income expected to grow 3.4% in FY 2013 and 4% in FY 2014.
- ▶ Wages & salaries expected to grow 3.5% in FY 2013 and 3.8% in FY 2014
- ▶ Employment expected to increase by 1% and 1.3% in FY 2013 & FY 2014, respectively

Virginia

- ▶ Source: *Commonwealth of Virginia 2012–2014 Biennial Budget Part A–Overview Economic Forecast.*

Where are we going?

