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Deficit Reduction Step Two Bringing Other Voices Into the Planning Process

Update 8/11/08

FY 2009 Budget Outlook

On August 1st the Governor announced that the state faces a potential budget deficit of **\$1.6 billion in FY 2009**. The Governor has ordered state agencies to immediately reduce their budgets by 6 percent. The only exceptions are the Medicaid and PeachCare programs, which will face a 5 percent reduction, and the funding for the Board of Education, which will face a 2 percent reduction. In addition, the Governor announced a delay and possible elimination of the distribution of the Homeowners Tax Relief Grant and the state employee salary increase scheduled to go into effect January 1, 2009. Savings from these actions total \$1.2 billion. An additional \$400 million will come from State Health Benefit Plan reserves, the suspension of OPEB contributions, use of tobacco fund reserves, and unexpended funds appropriated in FY 2008 for reservoirs (Table 1). The Governor's deficit reduction plan does not include use of the Revenue Shortfall Reserve (RSR) at this time.

Table 1
Governor's FY 2009 Deficit Reduction Plan

6% Reduction – Non-Exempt State Agencies	\$443 million
2% Reduction – Board of Education	\$164 million
5% Reduction – Medicaid/PeachCare	\$108 million
State Employee Salary Increase	\$73 million
Reduce State Health Benefit Plan Reserves	\$225 million
Suspend OPEB Contributions	\$100 million
Homeowners Tax Relief Grant	\$429 million
OneGeorgia Authority (Tobacco Reserves)	\$47 million
FY 2008 Amended Budget Unexpended Reservoir Funds	\$40 million
Total Deficit Reduction Plan	\$1.63 billion

The Office of Planning and Budget has informed state agencies that their budget allotments (distribution to state agencies of appropriated funds every 6 weeks) are being immediately reduced by 6 percent. In addition the state has suspended or eliminated the hiring of new and replacement positions, all out-of-state and non-essential travel, all purchases of motor vehicles, and the purchase of supplies, materials, equipment, and printing.

The Governor also asked state agencies to develop proposals for the amended FY 2009 and the FY 2010 budgets that will include options for cuts of 6 percent, 8 percent, and 10 percent of their budgets (Table 2).

Table 2
State Agency FY 2009 and FY 2010 Reduction Targets¹

	FY 2009 Budget	6% Cut	8% Cut	10% Cut
Legislative Branch	\$77,084,764	\$4,625,086	\$6,166,781	\$7,708,476
Judicial Branch	\$169,523,185	\$10,171,391	\$13,561,855	\$16,952,319
Accounting Office	\$5,456,173	\$327,370	\$436,494	\$545,617
Administrative Services	\$13,792,429	\$827,546	\$1,103,394	\$1,379,243
Agriculture	\$46,719,425	\$2,803,166	\$3,737,554	\$4,671,943
Banking and Finance	\$12,898,273	\$773,896	\$1,031,862	\$1,289,827
Community Affairs	\$53,426,544	\$3,205,593	\$4,274,124	\$5,342,654
Community Health (non Medicaid and PeachCare)	\$177,546,411	\$10,652,785	\$14,203,713	\$17,754,641
Corrections	\$1,157,668,132	\$69,460,088	\$92,613,451	\$115,766,813
Defense	\$11,716,641	\$702,998	\$937,331	\$1,171,664
Driver Services	\$62,791,511	\$3,767,491	\$5,023,321	\$6,279,151
Early Care and Learning	\$4,574,106	\$274,446	\$365,928	\$457,411
Economic Development	\$39,581,672	\$2,374,900	\$3,166,534	\$3,958,167
Employees Retirement System	\$7,151,826	\$429,110	\$572,146	\$715,183
Forestry	\$39,265,053	\$2,355,903	\$3,141,204	\$3,926,505
Governor's Office	\$47,774,172	\$2,866,450	\$3,821,934	\$4,777,417
Department of Human Resources	\$1,638,874,663	\$98,332,480	\$131,109,973	\$163,887,466
Insurance	\$19,230,125	\$1,153,808	\$1,538,410	\$1,923,013
Georgia Bureau of Investigation	\$77,283,568	\$4,637,014	\$6,182,685	\$7,728,357
Juvenile Justice	\$345,129,544	\$20,707,773	\$27,610,364	\$34,512,954
Labor	\$55,769,092	\$3,346,146	\$4,461,527	\$5,576,909
Law	\$19,650,981	\$1,179,059	\$1,572,078	\$1,965,098
Natural Resources	\$130,877,057	\$7,852,623	\$10,470,165	\$13,087,706
Pardons and Parole	\$58,439,590	\$3,506,375	\$4,675,167	\$5,843,959
Public Defenders Standards Council	\$40,439,957	\$2,426,397	\$3,235,197	\$4,043,996
Public Safety	\$135,260,351	\$8,115,621	\$10,820,828	\$13,526,035
Public Service Commission	\$10,348,009	\$620,881	\$827,841	\$1,034,801
Board of Regents	\$2,278,680,052	\$136,720,803	\$182,294,404	\$227,868,005
Revenue	\$129,207,540	\$7,752,452	\$10,336,603	\$12,920,754
Secretary of State	\$40,504,390	\$2,430,263	\$3,240,351	\$4,050,439
Soil and Water Conservation Comm.	\$3,572,839	\$214,370	\$285,827	\$357,284
Student Finance Commission	\$31,553,893	\$1,893,234	\$2,524,311	\$3,155,389
Teachers Retirement System	\$1,523,000	\$91,380	\$121,840	\$152,300
Technical College System of Georgia	\$370,975,007	\$22,258,500	\$29,678,001	\$37,097,501
Transportation (State General Funds)	\$29,659,047	\$1,779,543	\$2,372,724	\$2,965,905
Veterans Service	\$25,701,669	\$1,542,100	\$2,056,134	\$2,570,167
Workers Compensation	\$17,720,194	\$1,063,212	\$1,417,616	\$1,772,019
Board of Education (2% Cut)	\$8,196,497,771	\$163,929,955	\$163,929,955	\$163,929,955
Medicaid Benefits (5% Cut)	\$2,055,692,866	\$102,784,643	\$102,784,643	\$102,784,643
PeachCare (5% Cut)	\$98,672,929	\$4,933,646	\$4,933,646	\$4,933,646
Total Agencies	\$17,738,234,451	\$714,890,498	\$862,637,916	\$1,010,385,334

FY 2009 Revenue Outlook

General Fund revenues would need to increase by \$1.48 billion, or 8.4 percent, to meet the FY 2009 revenue estimate (Table 3). This revenue growth estimate does not account for tax cut legislation that was passed during the 2008 legislative session, which could cost an additional \$155 million to \$165 million in FY 2009.

Table 3
Revenue Growth Needed for FY 2009 Budget

	FY 2008 Revenues	FY 2009 Revenue Estimate	Revenues Needed to Make Estimate	Growth Needed to Make Estimate
General Funds	\$17,605,971,713	\$19,089,687,167	\$1,483,715,454	8.4%
Motor Fuel Funds	\$994,790,336	\$1,042,158,859	\$47,368,523	4.8%
Total	\$18,600,762,049	\$20,131,846,026	\$1,531,083,097	8.2%

For the first month of FY 2009 (July 2008), revenues declined by 6.6 percent (\$86.4 million), as compared to July 2007. Thus, revenues would need to grow by \$1.57 billion over the next 11 months to meet the FY 2009 revenue estimate.

Revenue Shortfall Reserve

The RSR totaled \$1.54 billion heading into the end of FY 2008. Accounting for use of the reserves in FY 2008 and expected end of year lapse of state agency funds to be added back into the Revenue Shortfall Reserve, the RSR is expected to total between \$873 million and \$973 million heading into FY 2009. To fund the Education Midterm Adjustment Reserve, approximately \$186 million would need to be appropriated from the RSR in the FY 2009 Amended Budget, leaving the RSR with between \$687 million and \$787 million.

Table 4
Revenue Shortfall Reserve

FY 2008 Revenue Shortfall Reserve	\$1.5 billion
FY 2008 Revenue Deficit	(-\$771 million)
FY 2008 Estimated State Agency Lapse Funds	\$100 - \$200 million
FY 2009 Education Midterm Adjustment Reserve	(-\$186 million)
FY 2009 Estimated Revenue Shortfall Reserve	\$687 – \$787 million

Revenue Options

Although the Governor did not recommend revenue enhancements as part of his deficit reduction package, a well balanced deficit reduction plan would include such options. It would take action by the General Assembly to rescind, delay or implement tax legislation, such as:

- Eliminating or delaying special interest tax breaks passed during the 2008 legislative session could save the state over \$100 million. Such tax breaks include:
 - Income tax credit for donations to student scholarship organizations (\$50 million cap). Although this tax credit already went into effect, legislators could minimize the revenue loss by lowering the \$50 million cap to a more reasonable level. This savings could be used to reduce the cut to the QBE education funding formula.
 - Tax incentive to insurance companies for high deductible health plans (\$11.5 million in FY 2009 and \$24.9 million in FY 2010). The primary tax cuts within this legislation do not take effect until January 1, 2009. Legislators could eliminate or delay the implementation of these special interest tax breaks until 2010 or 2011. These funds could be used to reduce the cuts to Medicaid and PeachCare programs.

- Increasing the cigarette tax by \$1 a pack, from 37 cents a pack to \$1.37 a pack. Georgia's cigarette tax ranks 43rd in the country, well below the average of \$1.11 per pack. A \$1 per pack increase would raise approximately \$442 million when implemented for an entire year.² Numerous studies have documented that cigarette price increases lead to significant reductions in smoking prevalence among smokers and to reductions in smoking initiation.³ Such funds could be used to mitigate cuts to the Medicaid and Peachcare programs, as well as the Division of Public Health.
- Implementing a temporary income tax surcharge on family income of over \$400,000 (less than 1 percent of taxpayers). A new 7 percent income tax rate on income above \$400,000 would raise \$225 million per year.⁴
- Reinstating the estate tax through decoupling from the federal tax code or implementing a separate estate tax modeled after the federal tax credit. An estate tax would raise approximately \$150 million and only affect those estates of greater than \$4 million (less than 1 percent of all estates).

Recommendations

The Governor's acknowledgement of the state's fiscal problems and his timely response is the first step in a balanced approach to deficit reduction. However, the second step – the prioritization of cuts and balancing of options – requires more than just executive branch actions. It requires legislative debate and public input that are made possible only through a special session.

Between \$714 million and \$1 billion in state agency budget cuts, as proposed by the Governor, would have a significant impact on the education, health, welfare, and public safety of a majority of Georgia citizens. Due to the size and potential impact of the proposed budget cuts, it is important that the General Assembly hold public hearings to hear testimony from the state agency heads as to the details of the planned budget cuts. It is also important that the General Assembly hear from the Georgia citizens who will be most affected by the proposed cuts.

In order to assure transparency, receive public input, and fully consider all deficit reduction options in a timely manner, a special session of the General Assembly should be called in September. The General Assembly should:

- Implement and prioritize targeted budget cuts after gathering public input. Medicaid, PeachCare, Department of Human Resources, Board of Education and public safety programs should be the highest priority for funding. A decision either to eliminate or reduce the Homeowners Tax Relief Grant needs to be made in a timely fashion to give counties, cities and school districts sufficient time to notify property owners;
- Redirect funding from low priority programs to high priority programs. For example some of the tobacco settlement funds that are currently appropriated for economic development programs in the OneGeorgia Authority could be redirected towards Medicaid, PeachCare and Public Health programs.
- Pass legislation that would increase revenues in order to avoid significant budget cuts to vital government services. Such legislation could include increasing the cigarette tax by \$1 a pack, eliminating some of the special interest tax breaks passed during the 2007 and 2008 sessions of the General Assembly, implementing an income tax surcharge on those earning more than \$400,000, and reinstating the estate tax; and
- Plan on using between 50 to 75 percent of the funds available in the Revenue Shortfall Reserve in order to avoid significant budget cuts to vital government services.

A balanced deficit reduction plan that consists of a combination of targeted budget cuts centered on lower priority government services, redirection of funding from low-priority to high-priority programs, Revenue Shortfall Reserve funds, and new revenues would put Georgia in the best position to meet our education, public safety, and healthcare obligations while maintaining the short-term fiscal health of the state. To assure the long-term fiscal health of the state, the Governor should appoint a blue ribbon commission to study ways to comprehensively reform

Georgia's tax system. For Georgia to successfully compete in the 21st century world economy it is important that a tax system be developed that fairly raises sufficient revenues to fund the education, healthcare, public safety, transportation and basic infrastructure needs of a modern and growing state.

¹ Calculations based on 6, 8 and 10 percent of total FY 2009 state funds appropriation. Actual reductions could be less depending on whether OPB exempts individual programs from reductions.

² Author's calculation using estimates from House Bill 1197 Fiscal Note.

³ For more information, see *Increasing Georgia's Low Cigarette Tax Would Yield Public Health Benefits*, GBPI, March 2008

⁴ Estimate by the Institute on Taxation and Economic Policy. August 2008.