

STATE
POLICY
REPORTS

In This Issue

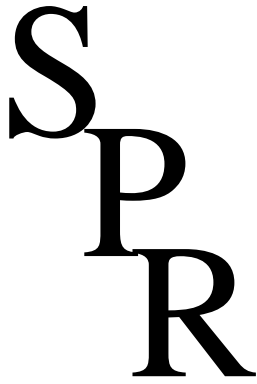
A Solution in Search of a Problem 2

In recent months, a narrative has emerged that puts some states on the brink of bankruptcy. To a large degree, that narrative confuses short- and long-term fiscal challenges, and overlooks the relatively strong financial positions of most states. Two recent analyses address this confusion, put these issues into historical context, and shed light on the actual liabilities states face in funding both their debt and pension requirements.

Tobacco Wars 8

When it was announced in 1998, the Master Settlement Agreement between 46 states and the tobacco industry looked like a guaranteed revenue flow that states could use to bolster other sources of state revenue. Several years on, it turns out that a certain provision of the settlement could put a portion of that stream of payments at risk.

Technical Notes 11



In This Issue

How Not to Balance a Budget 2

Federal lawmakers are trying to do something states do all the time: balance the budget. But they are having a difficult time, in part because they have excluded the lion's share of viable solutions from the debate, leaving only a small portion of federal spending to absorb outsized hits. They would probably make more progress if they took a page from the states' playbook and put everything on the table.

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ISSUE 3

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State and Local Finances in FY 2008 2

The Census Bureau has released its state and local finance series for fiscal year (FY) 2008. The combined state-local data allow meaningful comparisons of tax structures and burdens among the states. This issue focuses on the revenue highlights of the newly released data.

Defining Revenue 2

General Revenue 3

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The Much-Maligned Public Worker 2

Depending on which study you look at, you will be told that state and local government workers are paid better or worse than their private sector counterparts. So which is it? Both!

Cigarette Taxes and the Sore Thumb 4

A recent report finds that states with the highest cigarette tax rates are losing some of their prospective tax revenue because consumers are opting for smuggled—and therefore untaxed—cigarettes instead.

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ISSUE 5

In This Issue

Index of State Economic Momentum **2**

State results on the measures that make up the Index of State Economic Momentum continue their upward climb: personal income growth has improved since the last update, as have employment growth and the unemployment rate. The issue now is sustainability. Because most state economies fell into such a deep hole, it will take many more quarters of sustained improvement before they return to their pre-recession performance.

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In This Issue

The 2011 Camelot Index 2

The Camelot Index was developed by *Reports* founding editor Hal Hovey. It is based on the premise that most people share a common set of preferences: fewer taxes are better than more, small class sizes are better than large, low death rates are better than high, less crime is better than more and so on.

Many studies incorporate such preferences, but they often focus on just one area. For example, a study may attempt to identify the “healthiest” state but ignore the fact that health care isn’t delivered in a vacuum; it may be traded off with something else.

The Camelot Index brings together measures of economic vitality, health, education, crime, society and government. In the current Index, many states rank consistently across measures, while others do quite well on some measures but not on others. The historic dominance of the Plains continues, with four states ranking among the top five (but once again, not at the very top).

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STATE POLICY REPORTS

In This Issue

The Curious Case of the FY 2012 Census Budget 2

The U.S. Census Bureau wants to get out of the business of reporting on the flow of federal funds to states, and get into the business of reporting on state and local pension obligations. On its face, this appears to be a move that would eliminate the sole source of comprehensive state-by-state data on federal spending trends, while adding yet another voice to the already crowded field of pension reporting.

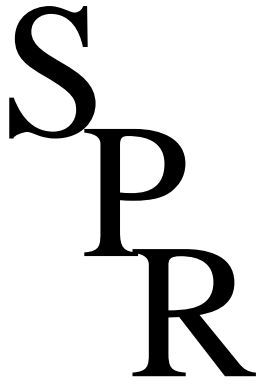
State Revenue Trends by Component 4

According to the latest budget survey from the National Conference of State Legislatures, most states are collecting more from their major state taxes than they anticipated when they adopted their budgets.

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In This Issue

State Government Finances in 2009 **2**

Typically, *Reports* ignores the annual Census Bureau report on state government finances, believing that a more complete understanding can be had by focusing on combined state and local finances. However, the release of the 2009 state finance series highlights the big changes that took place in response to the last recession, and the important role federal aid played in both state revenue and spending.

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In This Issue

50^o of Freedom 2

A market-based think tank has developed a freedom index that ranks the 50 states. It measures economic freedom and personal freedom, and its most recent results underscore the fitting state motto for **New Hampshire**: live free or die.

For Lawyers, Supply > Demand 6

A recent article lists the number of new lawyers in each state compared to the number of jobs available to them. The picture is not pretty.

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In This Issue

The Idiosyncrasies of Federal Funding **2**

A recent report that ranks states based on their per capita receipt of federal funds shows some surprising results: in contrast to conventional wisdom, not all grants redistribute funding from wealthier to poorer states. In fact, a few wealthy states do quite well on a per capita basis.

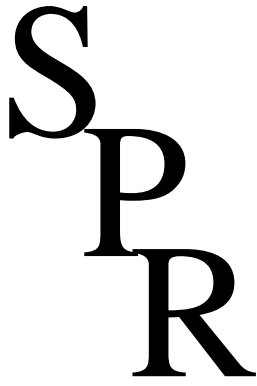
While No One Was Watching **6**

During the past three years, the federal government has provided states with more than \$100 billion in fiscal relief through a temporary increase in federal Medicaid matching rates. The matching rates return to their regular levels on July 1, 2011. Some states will see larger reductions than others, in part because the temporary aid masked trends that were occurring in the underlying rates.

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Continuum of State Fiscal Stress 2

In fiscal year (FY) 2006, 47 states ranked in one of the two most desirable categories of the Continuum of State Fiscal Stress. By FY 2009, that number had slipped to six. Now, 19 states have reached these top ranks, providing evidence that states are continuing the long, slow climb out of a recession unlike any they had seen for many business cycles.

Potentially large reductions in federal aid loom on the horizon and will almost certainly slow down states' recovery. But will they halt the recovery entirely, or even reverse it? That question remains.

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Index of State Economic Momentum 2

This update of the Index of State Economic Momentum is full of “buts,” which makes it worrying. Personal income is growing in every state, but mostly due to a federal tax cut. Job growth is positive, but less so than in the last update, with more states reporting job losses. The unemployment rate is climbing, and house prices have increased in only three states in the past year. More than anything, the update emphasizes what a long way to go most states have, with the notable exception of **North Dakota**, which left every other state in the dust this time around.

Unemployment Rates 6

Spotlight on Housing 8

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Good News, Tempered 2

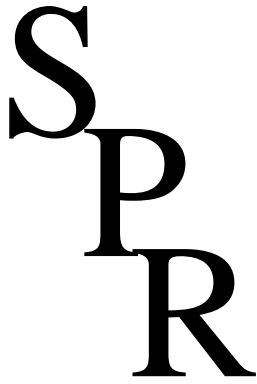
The most recent report on state tax revenues includes encouraging figures for most states in the first quarter of 2011. That said, states have yet to recover to their pre-recession revenue levels, and the prospect for future collections is uncertain.

Not Cool 5

Facing both a cut in federal funding and a hotter-than-usual summer, many states are finding they cannot meet the demand for summer cooling assistance. The problem is likely to get worse, as the federal program that provides such assistance is facing an even bigger potential cut next year.

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In This Issue

State Reliance on Federal Spending 2

With the recent downgrade in U.S. government debt by one of the three major bond rating agencies, state reliance on federal funding has moved into the spotlight. Now, instead of seeking to maximize their receipt of federal funds, states have a reason to tout their lack of reliance on such funding.

Curious State Rankings, Cont'd. 8

If you saw that your state was losing more white-collar jobs than other states, would you be concerned? A recent article reported such data, but its list of states included a few that are widely viewed as having above-average economies. So maybe it's not such a bad thing.

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In This Issue

State Solvency Slippage

2

If a state went out of business today, would it be able to pay all of its debts and have money left over? Or would it have to levy an assessment on its residents to meet its financial obligations? To help understand these questions, this issue includes the most recent State Solvency Index.

A Silver Lining?

10

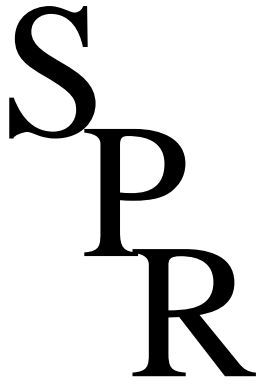
A new federal budget law sets spending targets to achieve federal budget deficit reduction and creates a special committee to dig even deeper for additional cuts or new revenues. Should that committee fail in its mission, the law would impose across-the-board cuts on many federal spending programs, but would spare the preponderance of funding that flows to states.

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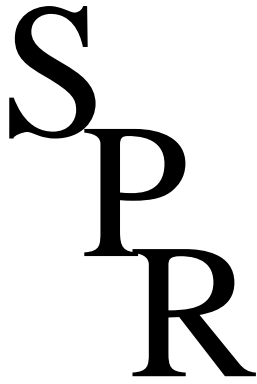
In This Issue

The Intersection of Sales Taxes and E-Commerce 2

Problems with the state sales tax are large and growing. It has been the victim of two accelerating trends: more consumption of services, which are scarcely taxed in most states, and more consumption via e-commerce and other types of remote sales, which can make tax collection difficult if not impossible. Meanwhile, the revenues states lose to these developments continue to mount. Developments in **California** could shift the e-commerce debate to Congress, where expanded state taxing authority might get a better reception than it has in recent years, in light of the prospect of declining federal aid for states.

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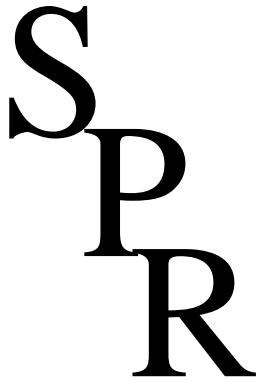
Index of State Economic Momentum 2

This update of the index shows state economies continuing their climb out of recession. Personal income and employment growth are both up since the last update, and the national unemployment rate is unchanged. New population estimates for 2001-2009 (derived from the 2010 decennial census) suggest that some interstate migration patterns have been affected by the economy.

Unemployment Rates 8

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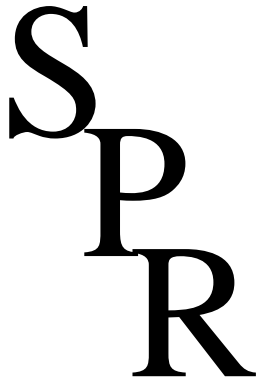
In This Issue

A Decade in Review: 2000-2010 **2**

The release of population and personal income data for 2010 allows an evaluation of how individual states fared over the decade from 2000 to 2010. Many sectors of the economy were in turmoil during the period, including manufacturing, housing, financial services, natural resources and agriculture. State population trends and income changes reflect the impact of these forces, with some states suffering from harsh economic realities while others enjoyed the fruits of more favorable developments.

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Federal Spending Traceable to States 2

The U.S. Census Bureau has released its report for fiscal year (FY) 2010 that tracks the flow of federal funds by state. States can use data in the report to assess how they fare in their fiscal relationship with the federal government, an especially relevant issue in an era of federal budget cutting. Sadly, this report may itself become the victim of federal budget cutting, making future analyses of federal spending in the states more difficult to conduct.

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In This Issue

Performance Measures in Booms and Busts **2**

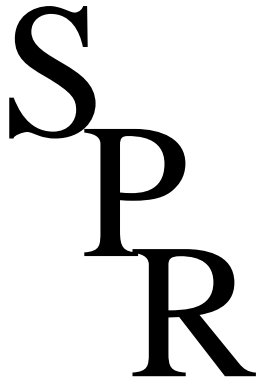
A recent analysis of states' use of performance-based budgeting finds that the system is more widely used by the executive branch, and more widely used when the economy is strong. Are those bad things?

Can States Learn from the Feds? **4**

The federal budget process is rife with complexities that are largely absent from state processes. A recent paper suggests that states might benefit from emulating the federal rules. While some states might benefit, the data suggest that most states currently implement the spirit—if not the letter—of the proposed policies.

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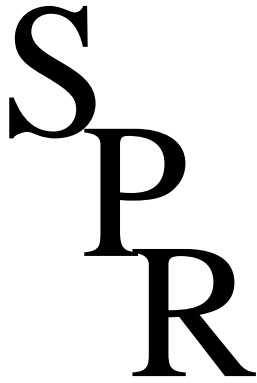
States, the Department of Defense and the BCA 2

In August 2011, the Budget Control Act of 2011 (BCA) was signed into law. It sets federal budget caps for both domestic discretionary and defense spending, and includes triggers for additional budget reductions. A good deal of attention has focused on the likely impact on states of cuts to domestic spending, while little attention has been focused on the impact on states from cuts in defense spending. For some states, the latter pose as much a threat as the former.

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A Recession in the Rear View Mirror

After modest improvement in fiscal year (FY) 2010, state economies and budgets continued to strengthen in FY 2011. As a result, it now appears that states have begun the long, slow process of recovering from the recession that devastated state budgets in FYs 2008-2009. One big question looms: will the national recovery be sustained at a level that allows states to replace the loss of federal fiscal assistance in FY 2012 and beyond?

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