THE VOLCKER ALLIANCE
Working for Effective Government

Beyond the Basics

BEST PRACTICES IN STATE BUDGET TRANSPARENCY

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WORKING PAPER

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EXECUTIVE SUMMARY

While many US states have tried to encourage transparency in their annual or biennial budgets, all fifty still lack a full range of disclosures about the use of one-time revenue to cover recurring expenditures, the deferral of spending, and the underfunding of infrastructure maintenance and retirement obligations for public workers. This lack hinders debate over spending priorities and encourages the use of budget gimmicks that can lead to poorly informed policymaking.

The following working paper explains the basic principles of sound budgeting and provides recommendations for improving budgetary transparency, based on a review of literature and interviews with numerous current and former state budget directors, finance officials, and public administration professors specializing in state and local government budgeting. The principles and recommendations build on a set of recommendations made in a Volcker Alliance report, *Truth and Integrity in State Budgeting: Lessons from Three States,*[1] which focused on the fiscal practices of California, New Jersey, and Virginia. The recommendations in this working paper will be used to inform the Volcker Alliance's further scrutiny of state budgets and budget practices in all fifty states.

I. Introduction

While many US states have tried to encourage transparency in their annual or biennial budgets, all fifty still lack a full range of disclosures about the use of one-time revenue sources to cover recurring expenditures, deferrals of spending, and underfunding of infrastructure maintenance and public-worker retirement obligations. This lack hinders debate over spending priorities and encourages the use of budget gimmicks that can lead to poorly informed policymaking and improperly shift current spending obligations to future generations, as the Volcker Alliance concluded in a previous study, *Truth and Integrity in State Budgeting: Lessons from Three States*.[2] The budget crises that beset Illinois and Pennsylvania in 2015—and numerous other states in recent years—show the result of fiscal decisions that are often made with incomplete public disclosure.

The following working paper explains the basic principles of good budgeting and offers ten recommendations for improving budgetary transparency. In most cases, we refer to the general fund budget, which the National Association of State Budget Officers defines as the main fund for financing a state or locality's operations.[3]

The principles and recommendations have been developed by reviewing published literature on the subject and through extensive interviews with 25 fiscal experts. They include current and former state budget directors and finance officials as well as public administration professors specializing in state and local government budgeting. The principles and recommendations build on *Truth and Integrity in State Budgeting*, which focused on the fiscal practices of California, New Jersey, and Virginia. The recommendations in this working paper will be used to further inform the Volcker Alliance's scrutiny of state budgets and budget practices in all fifty states.

II. When Transparency Falls Short

A budget should contain information that allows citizens to see that it is balanced using current resources and to understand how any action taken one year will affect revenues and expenditures in future years. But fiscal experts point out that those putting together budgets can play games with figures.[4]

That is unfortunate, as the budget is "the mechanism for how a state decides to spend its money," says Marc V. Shaw, chair of the City University of New York's Institute for State and Local Governance and senior adviser to former New York Governor David Paterson.[5]

The budget process is most problematic during difficult fiscal times, especially recessions. When a state resorts to such gimmicks as shifting payments from one year to the next, underestimating expenditures, or using inflated revenue estimates, it may be doing so both to cope and to preserve the illusion of budgetary balance without raising taxes or cutting programs.[6] But ensuring that budgets are realistic and that one-time actions are clearly described will help guarantee those actions are used only when necessary and kept to a minimum.

Some states may lack the resources to provide greater transparency, says Scott Pattison, executive director of the National Governors Association and former executive director of the National Association of State Budget Officers (NASBO).[7] Still, effective financial management of a state relies on clear and easily accessible information about budgetary balance, service outcomes, future liabilities, and spending and revenue trends.

III. General Principles of Good Budgeting

As documents from all fifty states demonstrate, there is no single way to prepare and present a budget, according to Pattison, who also served as the budget director for the Commonwealth of Virginia.[8] The sentiment is echoed by many current and former budget directors. But however a budget is presented, it should contain consistent presentations of both revenue and spending.

"The principle is to present the information in as clear a way as possible," says Duane

Goossen, senior fellow at the Kansas Center for Economic Growth and the state's budget director from 1998 to 2010.[9]

Literature on budgeting and the authors' interviews with fiscal experts suggest that the state budget process should include these features:

- Policies that govern budget processes and presentation should be clearly stated, including policies for the use of reserves, such as rainy day funds, that feature explanations of how money should be added or taken from the fund;
- The budget document should communicate key fiscal and policy decisions, issues, and tradeoffs;
- Revenue and expenditure information should be presented consistently to facilitate comparison between fiscal years;
- Budgets should provide trend data to illustrate how the state's demographics, economy, and finances—including revenues and expenditures—change over time;
- Budget items should be defined consistently. For example, any capital budgets should clarify the difference between maintenance and major modification or construction; and
- The budget should provide information on the accuracy of past revenue and spending forecasts.

IV. Developing Budget Standards

As the Volcker Alliance pointed out in *Truth and Integrity in State Budgeting,* there is no common definition of a balanced budget.[10] This is not for a lack of trying to come up with one. In 1842, Rhode Island became the first state to pass a constitutional requirement for a balanced budget. By the end of the nineteenth century, thirty-six other states had adopted balanced-budget rules.[11] Today, forty-six states require balanced budgets, while three others have limits on borrowing and deficits that effectively accomplish the same thing. Vermont follows those states' practices but lacks a statute for a balanced budget.[12]

There is strong consensus about the elements needed in a budget. Many were spelled out in the 1990s, when the National Advisory Council on State and Local Budgeting was established by seven state and local government groups and the Government Finance Officers Association (GFOA), a professional organization that includes state and local finance officers in the United States and Canada. The council was given the task of establishing a blueprint of good budgeting practices within three years of its inception.[13]

The key points of the council's final report included the need to tap stakeholders; set goals and priorities; and assess programs, requirements, and challenges in developing budgets. The recommendations also focused on adopting policies to guide financial practices—for example, developing policies on reserve funds, debt issuance, and the use of one-time and windfall revenues.[14] The recommendations made at that time remain relevant and applicable today.

Various organizations have produced other recommendations for good budgeting and disclosure practices, as well as evaluations of how well states are complying with them. They include the State Budget Process Quality Index, published by State Policy Reports[15]; the Pew Government Performance Project[16]; studies on long-term planning by the Center on Budget and Policy Priorities[17]; *Transparency in State Budgets: A Search for Best Practices,* by experts at the University of Illinois Institute of Government and Public Affairs[18]; and the Volcker Alliance's *Truth and Integrity in State Budgeting*.[19] NASBO's periodic report Budget Processes in the States contains a wide range of information on budgeting policies and practices, although it does not evaluate them.[20]

V. The Budget Process

According to NASBO, thirty states use budgets covering only one fiscal year. The remaining twenty span two fiscal years, often called a biennium.[21]

All but four states have a fiscal year that begins on July 1. For those with annual budgets, the process begins during the summer, when agencies receive guidance on expenditures from the governor's budget office. The agencies, in turn, submit budget requests to the governor in the fall. The budget office reviews the requests in light of revenue projections that are developed for that purpose, sometimes in conjunction with the legislature. The next step is developing a proposed budget that is produced by the governor's budget office and given to the legislature for its input and approval, usually in early winter.

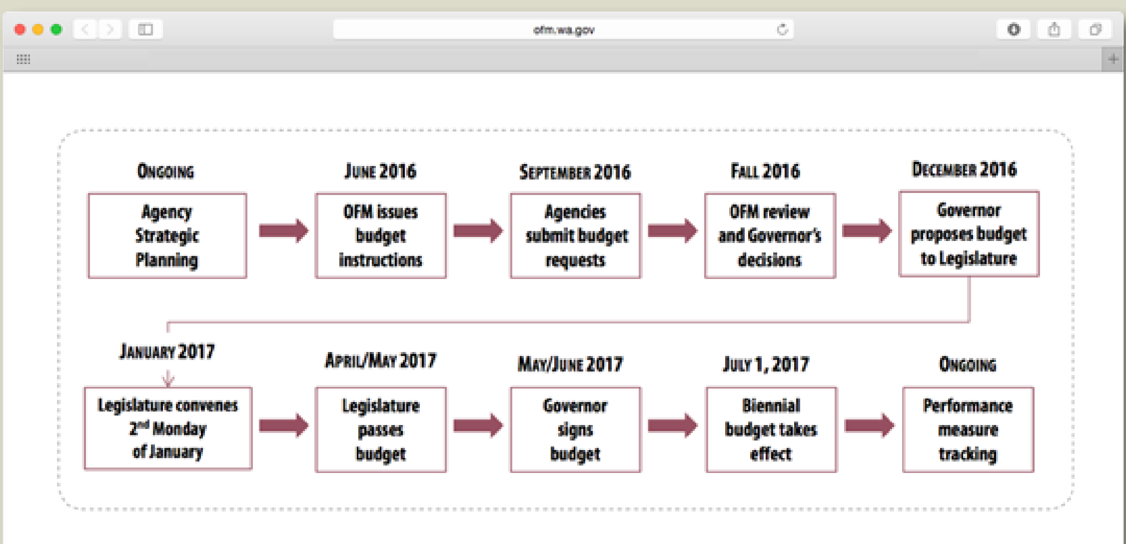
Once the legislature passes the measure, it is sent back to the governor, who may sign it or—depending on state law—veto individual items or the entire budget and return it to the legislature for further consideration. If discord within legislative bodies—or between them and the governor—is significant, passage of a budget may be delayed beyond the start of the new fiscal year or biennium. That can leave municipalities and agencies in a state of limbo until a budget is enacted. Both Illinois and Pennsylvania found themselves in such a situation in 2015, with neither enacting budgets for fiscal 2016 as of November 30, 2015.

Texas is a notable exception to most states' procedures. Its Legislative Budget Board, a permanent joint committee of the Texas House and Senate, sends instructions to agencies in the spring of even-numbered years for preparing the biennial budget to take effect the following year. The board and the governor's office hold joint hearings, and each develops budget recommendations. Appropriations bills are passed by both legislative chambers. A conference committee then resolves any differences and sends a general appropriations act to the governor, who can veto individual items.[22]

The governor's power in the budget process differs considerably from state to state. This includes the chief executive's veto power and ability to act without legislative approval after a budget is passed. For example, if additional federal funds become available after the state enacts a budget, some governors can spend the money without consulting their legislature. Thirty-one governors—including those of California, Florida, and New Jersey—can spend funds that weren't anticipated when the budget was passed. The other nineteen, including the governor of Texas, cannot.[23]

When a budget underestimates the amount a program needs, the legislature may approve a supplemental appropriation. While a supplement might be necessary in emergencies, it can displace planned expenditures in other areas. It may also add complexity and inefficiency

BEST PRACTICE Present How the State Budget Is Assembled
States should explain clearly how the budget cycle works, including when planning for the next fiscal year starts, when the budget takes effect, and what follow-up moves may be taken. Washington's flowchart provides a model for others to emulate.



SOURCE: http://www.ofm.wa.gov/reports/budgetprocess.pdf to the budget if it's used to bypass scrutiny of program spending, according to Arwiphawee Srithongrung, associate professor of public administration at Wichita State University's Hugo Wall School of Public Affairs.[24]

VI. Budgetary Building Blocks

One of the basic steps that states must take in developing a budget is deciding how much money they have available to spend in the coming year. They accomplish this through a revenue-estimating process that varies among states. According to the Pew Charitable Trusts, about two-thirds of the states use consensus revenue estimates, which rely on multiple sources and are bipartisan.[25] Consensus revenue estimates aren't necessarily more accurate than those arrived at by other methods. But they do attempt to remove politics as much as possible from the consideration of how much a state has to spend in the coming fiscal period, allowing policymakers to focus on how to allocate resources.[26]

For example, Virginia uses consensus revenue forecasts. The estimates are based on input from the Joint Advisory Board of Economists. That panel, established by statute, includes the state finance secretary, representatives of both legislative houses, outside economists, and the Governor's Advisory Council on Revenue Estimates, which is composed of the governor, and legislative and business leaders. The revenue assumptions and methodologies used in the estimates are subject to periodic review by a volunteer state board of professional economists.[27]

Estimates of expenditures are also critical, as are the reasoning behind them. "There's a lot of misunderstanding about state government and a naive hope that costs can remain the same forever when they can't," says Goossen, the former Kansas budget director. "They go up every year. Understanding how much they're going up and the forces that are pushing them up is important," he says.[28]

As was the case in Virginia in fiscal 2014, states sometimes miss on their estimates and are left with lower revenues (or higher expenditures) than anticipated.[29] That's why budgets should be thorough and clear about the types of budget reserves the state may be able to tap and the policies that establish how to use and replenish them.[30]

Also critical is an analysis that provides context for the budget, describing the forces that underlie the revenue and spending projections including historical demographic changes, the state's economy and industries, and anticipated changes in federal outlays. For instance, Minnesota posts a variety of information, including an annual economic forecast that contains data on factors that will affect spending in the coming budget.[31]

Many states also include performance measurement data in the budget or collect them during the budgeting process. According to NASBO, thirty-nine states use performance measures to develop executive budgeting recommendations.[32]

BEST PRACTICE Use Consensus Revenue Forecasting
States should use multiple inputs, including forecasts from the executive and legislative branches as well as from independent economists and business groups, to estimate revenue and, as much as possible, insulate the process from politics. In this map, the Center on Budget and Policy Priorities has tracked which states use consensus forecasts.

SOURCE: http://www.cbpp.org/sites/default/files/atoms/files/10-15-15sfplookingahead.pdf

VII. Recommendations for Increased Transparency

Virtually all state budgets contain disclosures such as charts showing where revenue originates and goes, along with estimates of expenditures in the coming year. The budget and accompanying documents typically provide some basic financial information, a fiscal message from the governor, a glossary of terms, and a description of the budget process.

That may not disclose enough for citizens and legislators to make informed judgments about the future stability of state finances. The authors' interviews with former or current state budget officers, public finance professors, and investment analysts—along with a search of relevant literature—resulted in the following ten recommendations:

1. **Clearly present one-time revenues and their impact on future budgets.** States may generate one-time revenue but not note them as such. Examples include transferring money from special-fund accounts and accelerating estimated personal and corporate income taxes into the current year from future years. The risk in using one-time revenue to cover recurring expenditures is that similar solutions might be needed in subsequent years if more durable sources of revenue are not found.

   Kansas, for one, provides charts showing transfers in and out of the general fund, such as paying transportation services from a special fund rather than the general fund.[33]

   Publishing this kind of data may discourage states from using one-time revenue inappropriately, according to Philip Joyce, senior associate dean and a professor of public policy at the University of Maryland's School of Public Policy.[34] The Volcker Alliance has said that a way to protect against the use of one-time solutions is to

BEST PRACTICE Disclose One-Time Transfers into the General Fund
States should clearly report how much cash is transferred into the general fund from special funds that may not be available in future years. Nebraska's Legislative Fiscal Office discloses this at the end of the state's fiscal biennium.

nebraskalegislature.gov

General Fund Transfers-In

	Current Yr	Biennial Budget		Following Biennium	
	FY2014-15	FY2015-16	FY2016-17	FY2017-18	FY2018-19
Securities Act Cash Fund	21,000,000	24,000,000	24,000,000	0	0
Tobacco Products Admin Cash Fund	10,000,000	13,000,000	10,000,000	0	0
Dept of Insurance Cash Fund	6,000,000	6,250,000	6,250,000	0	0
Charitable Gaming Oper Fund	0	2,000,000	0	0	0
Dept of Motor Vehicles Ignition Interlock Fund	200,000	200,000	200,000	0	0
Collection Agency Cash Fund	0	200,000	0	0	0
Waste Reduction and /Recycling Incentive Fund	0	1,000,000	0	0	0
Resource Recovery Cash Fund	0	200,000	0	0	0
Metropolitan Class Development Fund	0	147,000	0	0	0
Primary Class Development Fund	0	98,000	0	0	0
Convention Center Support Fund	0	150,000	0	0	0
Severance Tax Admin Cash Fund	0	150,000	150,000	0	0
Job Training Cash Fund	0	250,000	250,000	0	0
Medicaid False Claims Cash Fund	6,800,000	0	0	0	0
Total General Fund Transfers-In	44,000,000	47,645,000	40,850,000	0	0

SOURCE: http://nebraskalegislature.gov/pdf/reports/fiscal/2015budgetbrief.pdf move away from cash-based budgeting and adopt the type of accounting, used in comprehensive annual financial reports, that shows the true present value of future spending obligations.[35] "That would provide comparability not just between states, but in individual states from year to year," says Justin Marlowe, professor of public finance and civic engagement at the University of Washington's Daniel J. Evans School of Public Affairs.[36]

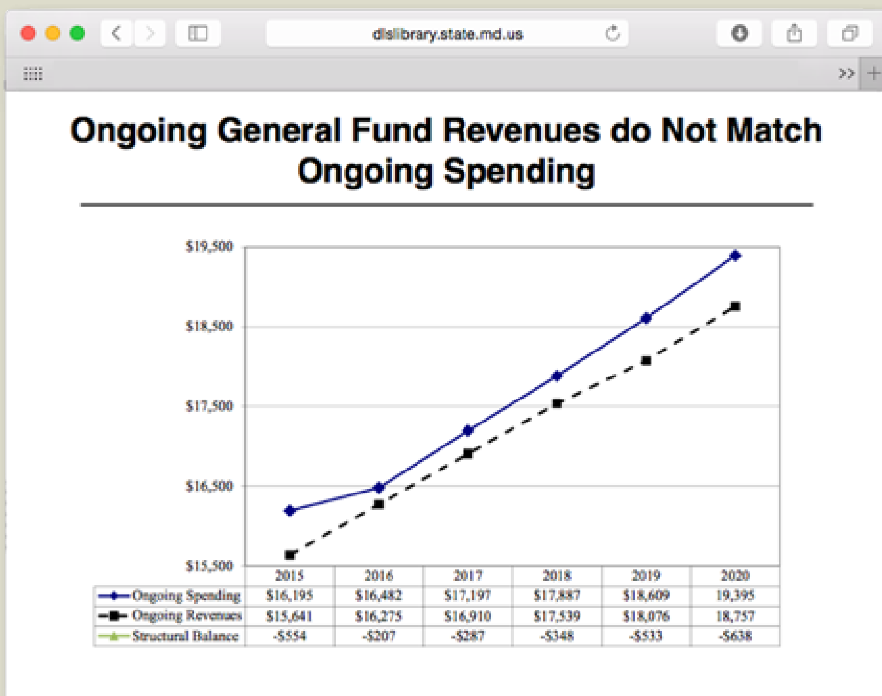
2. **Provide multiyear projections for growth of recurring revenues and expenditures.** Long-term estimates can reveal spending that has been deferred into the future, rev-

BEST PRACTICE Provide Long-Term Revenue and Spending Forecasts
Long-term revenue and expenditure forecasts are vital for policymakers' planning and to better inform the debate over the allocation of scarce resources. But while half of US states publish long-term projections either for revenues or spending for current services, only Alaska, New York, and Washington provide estimates for both. This map from the Center on Budget and Policy Priorities shows which states use forecasting policies that more should emulate.

SOURCE: http://www.cbpp.org/sites/default/files/atoms/files/10-15-15sfplookingahead.pdf enue sources that may cease to exist in coming years, and other temporary budgetary measures that cause long-term structural imbalance.

The GFOA recommends that forecasts extend beyond one year and that they be repeated as regularly as possible as the state's economy changes.[37] But Joyce at the University of Maryland suggests a better approach is "a three-year baseline or current-services projection that shows what you are anticipating and what will come up in the future." The projection should include estimates of demands for state-funded programs, such as Medicaid, as well as estimated inflation, he says.[38] Maryland Budget Highlights FY2016, which was transmitted by the governor to the General Assembly in January 2015 for fiscal 2016, contains an appendix that projects spending and revenue to 2020.[39]

BEST PRACTICE Disclose Long-Term Structural Budget Imbalances
Continuing gaps between a state's general fund revenues and expenditures may prompt governors and legislators to enact expedient one-time solutions to close deficits instead of considering more fundamental reforms of tax and spending policies. States should estimate and clearly disclose such gaps to better inform the debate over fiscal policy and allocation of resources. Maryland is one such state making this disclosure.



	2015	2016	2017	2018	2019	2020
Ongoing Spending	$16,195	$16,482	$17,197	$17,887	$18,609	19,395
Ongoing Revenues	$15,641	$16,275	$16,910	$17,539	$18,076	18,757
Structural Balance	-$554	-$207	-$287	-$348	-$533	-$638

SOURCE: http://dlslibrary.state.md.us/publications/OPA/P/MBO_2015.pdf

BEST PRACTICE Show the Cost of Underfunding or Borrowing to Make Pension Contributions

States should reveal how shortfalls in their annual pension contributions, or any borrowings to finance them, will affect future contributions. In 2010, New York adopted a rule allowing the state and local governments to defer a portion of their annual pension contributions, as required by actuaries, repaying them within 10 years with interest. This table, from the New York State Division of the Budget's midyear update for fiscal 2016, projects the cost of state government deferrals to 2029. The "Normal Costs" column shows actuaries' recommended annual pension contributions. The following columns show the amounts deferred, their cost, with interest, and the resulting total contributions, respectively.

publications.budget.ny.gov

EMPLOYEE RETIREMENT SYSTEM AND POLICE AND FIRE RETIREMENT SYSTEM[1]
PENSION CONTRIBUTIONS AND OUTYEAR PROJECTIONS
(millions of dollars)

Fiscal Year	Normal Costs[2]	(Amortized)/Excess Contributions	Amortization Payments	Total
Results:				
2011	1,543.2	(249.6)	0.0	1,293.6
2012	2,037.5	(562.8)	32.3	1,507.0
2013	2,076.1	(778.5)	100.9	1,398.5
2014	2,633.8	(937.0)	192.1	1,888.9
2015	2,325.6	(713.1)	305.8	1,918.3
Projections:				
2016	1,959.7	(350.4)	389.9	1,999.2
2017	1,768.0	0.0	431.5	2,199.5
2018	1,822.0	0.0	431.5	2,253.5
2019	1,825.6	0.0	431.5	2,257.1
2020	1,878.2	0.0	431.5	2,309.7
2021	1,911.4	0.0	431.5	2,342.9
2022	1,977.8	0.0	399.2	2,377.0
2023	1,993.5	0.0	330.7	2,324.2
2024	2,009.1	0.0	239.4	2,248.5
2025	2,024.4	0.0	125.8	2,150.2
2026	2,039.6	0.0	41.5	2,081.1
2027	2,054.3	0.0	0.0	2,054.3
2028	2,068.9	0.0	0.0	2,068.9
2029	2,107.7	0.0	0.0	2,107.7

[1] Pension contribution values in this table do not include pension costs related to the Optional Retirement Program and Teachers' Retirement System for SUNY and SED, whereas the projected pension costs in other Financial Plan tables include such pension disbursements.

[2] Normal costs include payments from amortizations prior to FY 2011, which will end in FY 2016 as a result of early repayments.

SOURCE: http://publications.budget.ny.gov/budgetFP/FY2016FPMidYear.pdf

Any multiyear projections should also show changes in the state's tax code, which may signal increases or decreases in revenue over a number of years, says North Carolina Budget Director Lee Roberts. Without that focus, he says, the true dollar impact of scheduled changes in tax policy over four, five, or six years may not be adequately taken into account.[40]

3. Disclose and explain the impact of delayed spending.

In *Truth and Integrity in State Budgeting*, the Volcker Alliance evaluated whether states fully funded prior long-term commitments for public worker pensions and health care, in line with actuaries' recommendations.[41] If the payments aren't made in line with actuaries' recommendations, the amounts required to cover the underfunding in future budgets grow ever larger. The amount of any underfunding and its cost in future years should be clearly disclosed in budget documents. So should the cost of any borrowing to finance states' pension contributions.

New York provides an example of such disclosure. In the years after the recession, annual recommended pension contributions rose dramatically in many states because of investment losses and pressure on governments to maintain essential services. To avoid paying the full amount of contribution at a time when revenues had dipped, New York passed a law in 2010 permitting part of each year's pension contribution for the state and for local governments outside New York City to be deferred and spread out over the following 10 years.[42]

New York State discloses the deferrals and their cost to taxpayers in a supplement to its budget. It shows that, over the course of six years beginning in 2011, the state deferred payments of about $3.6 billion, although it started to repay a portion of each year's deferred payment annually, with interest, as the law required. The supplement projects the costs this added to the program through 2026. In 2017, for instance, the state will be obligated to make a pension contribution of $2.2 billion, rather than the $1.8 billion it would have been without earlier deferrals.[43]

4. Determine and disclose deferred infrastructure maintenance.

Deferred maintenance–what needs to be spent to keep a state's physical assets in good order—is as much an obligation as pension underfunding or debt. But few states document as part of the budget process accrued deferred maintenance on roads and bridges, buildings, and other assets.

"There is no single unreported or underreported number on the balance sheets of state and local governments greater than the value of deferred maintenance of infrastructure," says Edward Mazur, senior adviser to the accounting firm Clifton-LarsonAllen and former member of the Governmental Accounting Standards Board.[44]

This is largely because many states lack the means to perform condition assessments on infrastructure that could be used in an asset management system, according to Roberts in North Carolina.[45]

California is one of the states making this disclosure. Its most recent five-year

BEST PRACTICE Disclose Deferred Infrastructure Maintenance Costs

Like unfunded pension obligations that eventually will need to be addressed, the cost of deferred maintenance on highways, bridges, and other state infrastructure represents a burden on future taxpayers. It should be disclosed as part of the budget process so informed decisions about allocation of resources can be made. California provides an excellent guide to deferred maintenance in its five-year plans (the most recent estimate was $66.1 billion for 2015).

ebudget.ca.gov

Figure INO-02

Identified Statewide Deferred Maintenance

(Dollars in Millions)

Department of Transportation	$59,000
Judicial Branch	$1,930
Department of Parks and Recreation	$1,420
California Community Colleges	$1,034
Department of Corrections and Rehabilitation	$996
California State University	$692
Department of Developmental Services	$387
Department of General Services	$138
Department of Forestry and Fire Protection	$126
California Military Department	$109
University of California	$100
Network of California Fairs	$57
Department of State Hospitals	$54
State Special Schools	$25
Department of Fish and Wildlife	$21
Department of Veterans Affairs	$21
California Highway Patrol	$17
California Science Center	$6
Department of Motor Vehicles	$5
Office of Emergency Services	$4
Department of Food and Agriculture	$3
California Conservation Corps	$0.3
Total	**$66,145**

SOURCE: http://www.ebudget.ca.gov/2015-Infrastructure-Plan.pdf infrastructure plan, included as part of the governor's proposed 2016 budget, provides estimates of $66 billion in total deferred maintenance in the state. "Deferred maintenance can be costly and a threat to public safety if facilities become unsafe," the document states.[46]

5. **Provide tax-expenditure information.**

   At least forty-six states produce reports on tax expenditures, according to the Institute on Taxation and Economic Policy.[47] While the reports calculate the amount of taxes given up through exclusions, exemptions, deductions, and credits to individuals and businesses, they vary in their level of detail and are often not a visible part

BEST PRACTICE Present the Cost of Tax Breaks

States should disclose as part of their budget documents the amount of revenue they have given up via tax exemptions and credits offered to businesses and individuals. This brings budgets more in sync with a Government Accounting Standards Board rule for states and municipalities to disclose such tax breaks in their comprehensive annual financial reports, beginning in December 2015. Louisiana makes such a disclosure in its budget.

doa.la.gov

REVENUE LOSS SUMMARY

	Tax type (Listed in order of magnitude)	FYE 6-11	FYE 6-12	FYE 6-13	FYE 6-14 (projected)	FYE 6-15 (projected)
1	Income tax - corporation	$1,394,651,120	$1,507,243,105	$1,502,155,325	$1,532,064,382	$1,559,318,002
2	Income tax - individual	$1,822,494,862	$1,934,546,190	$1,961,388,192	$1,975,223,996	$2,014,728,476
3	Sales tax	$2,516,791,839	$2,481,945,738	$2,663,450,562	$2,708,644,784	$2,762,795,080
4	Natural Resources - severance	$431,575,500	$527,153,045	$462,887,099	$472,144,841	$481,587,738
5	Tax incentives and exemption contracts	$345,194,562	$380,614,581	$319,403,814	$325,791,890	$332,307,728
6	Petroleum products tax	$91,260,450	$177,268,900	$73,337,375	$112,740,000	$112,740,000
7	Corporation franchise tax	$7,077,824	$5,116,549	$19,812,262	$20,208,507	$20,612,677
8	Tobacco tax	$66,764,695	$70,815,180	$75,997,300	$76,950,000	$76,950,000
9	Public utilities and carriers taxes (Note 1)	$2,693,400	$3,012,800	$3,196,000	$3,200,000	$3,200,000
10	Liquors - alcoholic beverage taxes	$2,305,900	$2,522,625	$2,776,055	$2,835,000	$2,835,000
11	Telecommunications tax (Note 1)	$19,800	$18,600	$16,800	$18,000	$18,000
12	Hazardous waste disposal tax (Note 1)	$17,000	$15,980	$13,700	$16,000	$16,000
13	Inheritance tax	$80,000	Negligible	Negligible	$0	$0
14	Gift tax	$26,000	Negligible	Negligible	Negligible	Negligible
	Total tax revenue loss	**$6,680,952,952**	**$7,090,273,293**	**$7,084,434,484**	**$7,229,837,400**	**$7,367,108,701**

Notes:
1 Included on the miscellaneous tax table.

The "Revenue Loss Summary" is published by the Department of Revenue in the Tax Exemption Budget 2012-2013, and included in the State Budget per R.S. 39:56D.
(To See the complete "Tax Exemption Budget" document, please visit: http://revenue.louisiana.gov/sections/Publications/ep.aspx)

SOURCE: http://www.doa.la.gov/opb/pub/FY15/StateBudget_FY15.pdf of the budget process.

GASB has required that states begin disclosing information on tax abatements in their comprehensive annual financial reports beginning December 15, 2015.[48] Similar disclosures should be included in budgets to show how much revenue is foregone in each fiscal period.

Some states have begun to include basic information in budgets. Louisiana, which summarizes the cost of tax expenditures in its budget in a Revenue Loss Summary, calculated a $6.7 billion loss in fiscal 2011 and projects a $7.4 billion loss in fiscal 2015.[49] In Ohio, a full tax expenditure report is published in Book 2 of the three-volume operating budget, a requirement put into effect in 2000. The estimate of total foregone

BEST PRACTICE Forecast the Cost of Debt Service
To help policymakers and taxpayers understand the composition and cost of borrowings, states should clearly present information on current and estimated future expenditures for debt service on general obligation and other tax-supported bonds. Minnesota's Commissioner of Budget and Management reports on this to the legislature each February and November.

mn.gov

Actual Annual Debt Service Costs
($ in Thousands)

	General Obligation Bonds				
Fiscal Year	Various Purpose	Trunk Highway Fund	Subtotal	Other Tax Supported Bonds	Total
2006 actual	$353,728	$36,347	$390,075	$10,629	$400,705
2007 actual	$400,146	$53,752	$453,898	$14,695	$468,593
2008 actual	$409,426	$52,170	$461,596	$17,999	$479,595
2009 actual	$452,978	$59,542	$512,520	$24,259	$536,779
2010 actual	$429,123	$70,542	$499,665	$27,640	$527,305
2011 actual	$398,799	$45,225	$444,024	$30,393	$474,417
2012 actual	$190,799	$72,601	$263,400	$38,194	$301,594
2013 actual	$222,584	$120,305	$342,889	$49,236	$392,125
2014 actual	$619,935	$136,488	$756,423	$97,492	$853,915
2015 forecast	$623,060	$154,593	$777,653	$147,149	$924,802
2016 forecast	$632,991	$185,953	$818,944	$148,481	$967,425
2017 forecast	$638,247	$211,492	$849,739	$147,171	$996,910
2018 forecast	$592,101	$217,106	$809,207	$146,251	$955,458
2019 forecast	$621,471	$215,579	$837,050	$144,894	$981,944
2020 forecast	$601,867	$210,295	$812,162	$135,621	$947,784
2021 forecast	$629,305	$203,659	$832,964	$135,371	$968,336

*Totals may not add due to rounding.

SOURCE: http://www.mn.gov/mmb/images/DCF-February-2015.pdf revenue was $7.7 billion in fiscal 2014, rising to $8.8 billion in fiscal 2017.[50]

6. Include current, historical, and trend information for debt.

Debt ratios, which compare a state's outstanding debt to a variety of other items, such as revenues, should be easily available. In addition, states should provide information about their capacity to take on new debt without jeopardizing their credit rating, as well as current commitments, including details on the type and maturity of debt.

"This makes it more likely that states will use debt prudently and prioritize capital projects," says John Bartle, dean of the College of Public Affairs and Community Service at the University of Nebraska, Omaha.[51]

According to a GFOA proposal on budget guidance, policies "should identify debt limits and current commitments to provide available debt capacity for new projects."[52] The governor's budget in Georgia, for example, presents a 10-year chart that compares annual debt service to the state's constitutional cap for debt service (which totals 10 percent of the prior year's net treasury receipts). The chart provides a look at debt service costs annually starting in 2007, with projections for fiscal 2015 and 2016. It shows that debt service came closest to the cap in 2011, when it was 8.1 percent of net treasury receipts. In fiscal 2016, it was projected to be 6.2 percent, the lowest level since 2008.[53]

7. Disclose the impact of state fiscal actions on local governments.

The financial interplay between states and local governments is complex and varies widely from state to state. It is an important and often opaque part of budget decision-making.

Even after the last recession ended in 2009, many states reduced aid to local governments. In Ohio, state support for local governments dropped by about $1 billion between the 2010–2011 biennial budget and the 2014–2015 biennial budget.[54] In Maryland, fiscal 2015's $549.5 million in aid to counties and municipalities was 34 percent less than the $828.2 million in fiscal 2006.[55]

These numbers are large, but many states reveal changes in the flow of cash to localities only in the broadest terms. More details would help citizens understand the effect that cuts in state expenditure have on their localities, in the context of their own revenues and historical patterns.

Minnesota has done this, publishing an annual Price of Government report that examines the cost of services statewide, including those delivered by the state, cities, counties, and school districts. Provided with supplementary budget documents, the report shows annual changes in revenues localities collect and the aid they get from the state, and helps explain how changes in state spending affect them.

8. **Compare actual education funding to goals set by legislatures, voters, or court decisions.**

Legislators may pass—and then ignore—statutes that require certain levels of educational funding. While state funding formulas for K-12 education vary widely, budgets should show whether spending is matching or falling short of any targets set by legislatures, voters, or courts, according to former Massachusetts Deputy Comptroller Eric Berman.[56]

For example, in 2008 the New Jersey Legislature set a new state formula for education funding in pre-K-12. But even though New Jersey is among the top five states in spending per pupil, its funding still fell short by about $1 billion of the required amount for fiscal 2015 under the State Funding Reform Act.[57]

A comparison of actual funding to past funding requirements is not commonly revealed in budgets, although some states provide parts of this information in supplementary documents, as the California Legislative Analyst's Office did in a February 2014 report.[58] It shows, for example, that from 2008–09 to 2011–12, the state deferred payments to schools and community colleges that were mandated by statute.[59] (Most of the deferrals have been repaid, according to the LAO.[60])

9. **Improve disclosure of the degree of volatility in tax revenues.**

In the recession that lasted from 2007 to 2009, tax revenues in states that depend on capital gain levies were hit unusually hard, especially with the 38 percent decline of the Standard & Poor's 500 stock index in 2008.[61] Disclosing how past revenues have gyrated would help governors and legislators design and use rainy day funds and other budget reserves to help governments cope with future volatility.[62]

Utah requires this kind of disclosure. According to its Legislative Fiscal Analyst's Office, "To manage long-term revenue fluctuations, avoid committing short-term gains to long-term obligations, and assure Utah has adequate and justifiable resources in reserve," the analyst's office and Governor's Office of Management and Budget must disclose revenue volatility in reports that are important to the budgetary process.

10. **Include targets for achieving financial goals.**
Budgets should clearly disclose where the government stands in relation to financial goals, such as retaining a certain portion of funds in a reserve or reducing unfunded pension liabilities by a targeted amount. Mac Taylor, the California legislative analyst, suggests that states should also explain how they intend to reach those goals.[63]

For example, California has a goal that its budgetary stabilization account, established as part of Proposition 2 approved by voters in 2014, should amount to 10 percent of revenues. But when the 2015–16 budget was passed, seven years into an economic recovery, the amount in that account was less than 3 percent.[64]

Some states do track their progress toward goals. For example, the governor's office in Michigan produces an online dashboard with a variety of performance measurements, including financial health. While the dashboard is not part of the state budget, it points out that a good practice is to keep at least 10 percent of annual operating expenditures in reserve. The dashboard also shows that the state is only at 4.04 percent.[65]

VIII. CONCLUSION

A budget is a planning document. It remains that way through the entire fiscal year or biennium, sometimes requiring supplemental spending and cuts in expenditures to stay in balance. If leaders can address unforeseen circumstances promptly, a state is more likely to maintain fiscal stability. However, better disclosure is also necessary to show the nature of a state's revenue streams as well as the true cost of long-term obligations and goals. Most budgets adhere to some basic transparency practices, disclosing policies that govern budget processes, key fiscal and policy decisions, and revenue and expenditure information. Yet many fail to achieve a level of transparency sufficient to communicate a full understanding of a state's fiscal stability.

More detailed information is still needed in fields such as revenue windfalls; multiple-year projections; delayed spending; deferred infrastructure maintenance; tax expenditures; debt; the impact of state fiscal actions on localities; education funding; volatility in tax revenues;

and strategies for achieving financial goals.

These recommendations will help guide further scrutiny of state budgetary practices and, it is hoped, act as catalysts for states themselves to improve the quantity and quality of their budget disclosures. Only when political leaders and citizens alike thoroughly understand the critical yet often hidden elements that underlie their states' budgets can they make well-informed decisions about the ways to allocate scarce resources in good times and bad.

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ABOUT THE ALLIANCE

THE VOLCKER ALLIANCE was launched in 2013 by former Federal Reserve Board Chairman Paul A. Volcker to address the challenge of effective execution of public policies and to help rebuild public trust in government. The nonpartisan Alliance works toward that broad objective by partnering with other organizations—academic, business, governmental, and public interest—to strengthen professional education for public service, conduct needed research on government performance, and improve the efficiency and accountability of governmental organization at the federal, state, and local levels.

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This paper is the product of the Volcker Alliance project on truth and integrity in government finance. It is an important goal of the Alliance to produce reports that contain ideas, proposals and recommendations for dealing in new ways with persistent governance problems based on independent research and analysis supporting constructive solutions. To stimulate this process and maintain project independence to make such conclusions and recommendations as they deem to be appropriate, these Alliance projects are commissioned to proceed without the requirement of approval of their conclusions and recommendations by the board of directors collectively or by individual members of the board of directors.

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