Trading Places

The Role of Taxes and Spending in the Fiscal Crisis

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EXECUTIVE SUMMARY

For the next 24 months and perhaps longer, the most difficult and controversial decisions state officials face will be the effort to balance the state budget. With significant challenges in balancing the current FY03 budget front and center today, the FY04 budget looms with a deficit of over $2 billion. In that context, a clear picture of the role that spending and tax policies have played in contributing to the fiscal crisis is vital.

This report examines spending trends in Massachusetts from a number of perspectives. It finds that contrary to the role spending played in the last fiscal crisis, spending growth in Massachusetts has been quite modest. Highlights of the report include the following.

Overall State Spending

- Massachusetts spends a smaller share of its total personal income on state and local services than most states; only five states spend less than Massachusetts in the overall measure. Moreover, the share of state resources dedicated to public services has fallen more here over the last two decades than in any state in the nation.

- While personal income rose at a rate of 2.6 percent annually from 1991 to 2002, after adjusting for inflation, the annual growth rate for state spending lagged behind, at 2.3 percent.

- The spending increase from 1991 to 2002 was just half the rate of growth experienced during the1980s, when inflation-adjusted spending grew at a rate of 4.7 percent. And while state spending grew *faster* than personal income during the 1980s, it grew more *slowly* than personal income during the 1990s.

- Massachusetts has fewer public employees than nearly any state in the nation and devotes a relatively small share of resources to paying their wages and benefits.

Only three states spend a smaller share of personal income on public employees than does Massachusetts.

- Of the limited number of state and local employees in Massachusetts, a far greater percentage than in other states are the front line teachers, fire fighters, and police officers most valued by the public. Ignoring these front line workers, Massachusetts has fewer state and local workers than all but two states, 16 percent below the national average.

Spending Priorities

- Education, health care, and corrections account for 99 percent of new state spending during the 1990s. All other areas of the budget — from the environment to human services to payments on the state debt — account, on net, for the remaining one percent.

- Notwithstanding the spending increases associated with education reform, state and local K-12 education spending in Massachusetts, as a percent of personal income, ranks 49th in the nation; in 1979, Massachusetts ranked 7th. Between 1979 and 2000, education spending in Massachusetts fell from 19 percent above the national average to 16 percent below the national average.

- In the case of higher education, the very small growth between 1991 and 2002 followed deep cuts in the immediately preceding years. Anticipated FY03 spending on higher education is 11 percent below the real level of FY89.

- While spending on Medicaid accounts for 40 percent of the total increase in state spending between 1991 and 2002, it is important to recognize that the federal government covered nearly half of this increase through the federal Medicaid match.

- The state cost of creating the senior pharmacy program and expanding health care services to low-income children and families amounted to less than $400 million in 2002. This hardly explains continuing multi-billion dollar budget deficits.

- Cash assistance programs and housing programs experienced by far the deepest budget reductions, having been cut by over 60 percent since 1991, after adjusting for inflation. Other program areas that experienced more modest cuts include environmental programs, non-education local aid, and mental health.

Tax Cuts in Perspective

- In contrast to these spending increases, the state enacted 42 tax cuts amounting to $5.0 billion between 1991 and 2002. Even after factoring in the tobacco tax increases approved during the 1990s and package of tax increases enacted in 2002, the net tax change during this period drains the state treasury of $3.7 billion annually.

- This figure exceeds the amount Massachusetts committed to any other priority during the same period. It is more than twice the amount the state increased Chapter 70 education aid, and over four times the state's share of the increased cost of Medicaid.

Based on this analysis, then, one can hardly assert that spending has been a significant factor in the state's fiscal crisis. Growth in even the highest priority spending items pales in comparison to the large tax cuts enacted during the 1990s, even after adding back in the tax increase of 2002. The deep cuts already made in the FY03 budget will reduce the already-modest spending growth rates yet further.

This suggests, then, that tax increases to compensate for the overly ambitious tax cuts of the 1990s must be part of any solution to the state's fiscal crisis. To propose that the budget should be balanced by cutting programs – few of which grew to any significant degree during the 1990s and many of which have already been cut substantially – without reconsidering what in retrospect are the clearly unaffordable tax cuts of the 1990s, ignores the reality of budget decisions and priorities of the last decade.

I. INTRODUCTION

Writing the fiscal year 2003 budget was a challenge for everyone involved in the process. From the point when Governor Swift proposed a $23.5 billion spending plan for the year until the final veto override votes were cast on a spending plan of $23.1 billion, questions of how to balance the budget were highly controversial. Facing a new round of cuts to bring the FY03 budget back into balance in light of continuing revenue shortfalls makes it clear that the controversy has not abated. Yet as we look forward to the FY04 budget, there is no indication the process will be any easier. Notwithstanding spending cuts and tax increases both in excess of $1 billion in the FY03 budget, it is likely that we will begin the FY04 process with a current-services deficit (the difference between the cost of maintaining current services and available revenue) of $2 billion or more.

Much of the debate about the deficit circles around the question of spending priorities. Specifically, opponents of a revenue solution to the budget deficit claim that the problem is that spending has simply grown too fast in Massachusetts. It is regularly asserted that spending has doubled in the last 10 years, a claim that is demonstrably untrue, yet used to assert that excessive spending has created our budget crisis.

These claims may make good sound bites, but they do not help illuminate the challenges Massachusetts faces in a time of recurring budget deficits. To look at spending over a decade or more without accounting for inflation is deceptive. Simply asserting that some arbitrary figure should be adequate, without articulating which priorities will be met and which foregone, is irresponsible. Under the best of circumstances, the budget process is likely to be somewhat opaque; the budget is a massive document with a wide array of programs, goals, and funding streams. Because budget documents do not typically contain data concerning prior year expenditures, and because the way budget items are organized can change from year to year, it is difficult for most people to know exactly how state resources are being used.

Yet understanding these issues is crucial in determining the proper course of action in fighting the state's continuing budget deficits. If the deficits are simply the result of an economic slowdown, perhaps we merely need to wait for the economy to turn around; in

that case temporary solutions and use of one-time revenue sources may be reasonable. If the problem is structural, with the cost of maintaining current services growing faster than available revenue in good times as well as bad, more aggressive action is needed to bring spending and revenue into equilibrium. Similarly, if excessive spending increases have caused the problems, then spending reductions may be the solution. If spending growth has been moderate while tax cuts were excessive — as this analysis shows — that points to quite a different solution.

II. LOOKING AT OVERALL BUDGET GROWTH

The first challenge in determining the role spending has played in the state's structural deficit is to look at changes in total spending over time. Between fiscal years 1991 and 2002 – from the last budget under the Dukakis administration to the most recently completed budget – state spending grew from $13.3 billion to $22.6 billion, an increase of $9.3 billion.[1] While this may sound like a large amount, it needs to be understood in context.

Adjusting for Inflation

To understand spending growth over the 11-year period, it is necessary first of all to account for the impact of inflation. Any family knows that if its income had stayed flat between 1991 and 2002, it would be far less able to pay for food, housing, and other basic goods today. Just as obviously, if increases in government spending lag behind inflation, we will have fewer teachers and firefighters, parks will deteriorate, and other services will decline. Between 1991 and 2002, the cost of living has grown by fully one-third. The real increase in spending that occurred beyond inflation represents a moderate average annual growth rate of just 2.3 percent. That rate stands in marked contrast to the experience of the 1980s, when spending grew at an average annual rate of 4.7 percent between 1983 and 1991.

Spending Growth & Personal Income

A reasonable method to gauge the appropriate growth of state spending is that, over time, state spending should roughly keep pace with the growth of personal income. As President Bush noted in his State of the Union speech, it makes sense for spending to grow "about as much as the average family's income is expected to grow…and that is a good benchmark for us." While this growth would routinely exceed the rate of inflation, that should not be disturbing; under this scenario, state spending would remain a constant

[1] These data are derived from the Commonwealth's annual *Statutory Basis Financial Report*, including the most recent report for fiscal year 2002. The FY91 spending figure is adjusted to remove spending on the MBTA, as is reflected in current practice. Failure to have made this adjustment would have indicated even slower spending growth over time.

The Lottery Effect

Including the growth of lottery aid in the calculations on state spending is misleading; changes in spending from the proceeds of the state lottery are quite different from other spending programs. The lottery was set up as a source of revenue for local governments; the state would operate the lottery, but after paying expenses and prizes all of the profits would go directly to cities and towns across the Commonwealth to finance local government services. Thus the state is no more than a collection agency for local revenue. If more people play the lottery, or those who do so spend more money, lottery revenue and distributions go up. This increase, however, does not expand state programs. On the contrary, increases in lottery proceeds result in increased local government resources. Thus increases in lottery spending no more reflect "liberal" spending policies than do reductions in lottery spending reflect conservative or restrictive fiscal policies.

In the late 1980s, however, this system of using the state lottery to fund local services was changed. Facing deep budget deficits, state officials "capped" lottery payments to municipalities, essentially siphoning off revenue originally intended for local services and redirecting it toward state services. (As a result, lottery spending declined in real terms, but it is obvious that this decline was not an indication of "fiscal discipline.") In recent years, the legislature gradually "uncapped" lottery aid, returning to the original practice of returning all lottery profits to cities and towns.

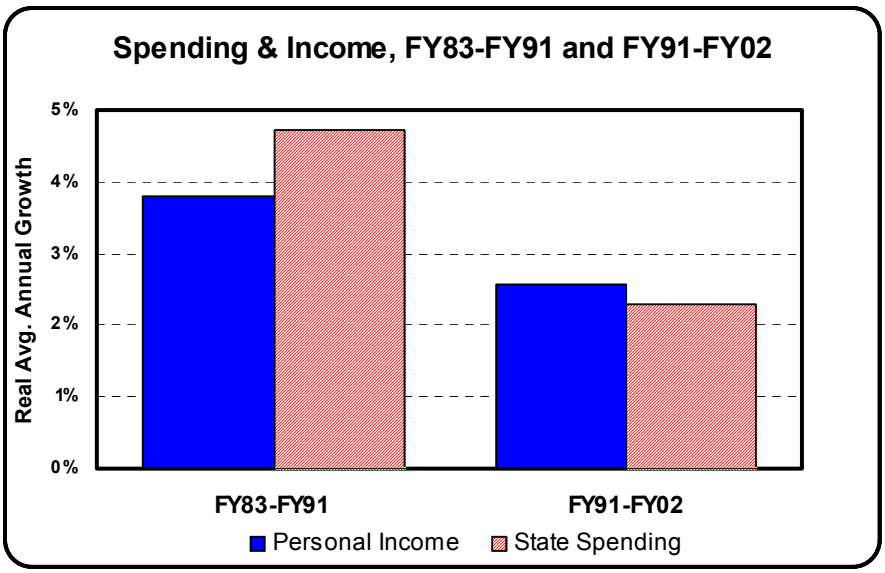
The analysis of overall changes in state spending included lottery aid in the calculations. However, the result of the policy to "uncap" lottery aid is that local aid funded by the lottery grew by 6.1 percent between FY91 and FY02, much more rapidly than other state spending. If lottery aid is taken out of the base of state spending, the annual rate of growth falls from 2.3 percent a year to 2.2 percent during the 11-year period.

share of overall income in the state, still leaving a growing amount of resources to be used for private consumption.[2]

During the 1990s, however, state spending grew more slowly than personal income. Between 1991 and 2002, as shown in Figure 1, personal income in Massachusetts grew at an annual rate of 2.6 percent, after adjusting for inflation, compared to spending growth that grew at a rate of 2.3 percent a year (or 2.2 percent annually if we exclude lottery spending). As a result, over the course of the 11-year period, Massachusetts state spending fell from 9.4 percent of personal income to 9.1 percent of personal income. Again, this pattern stands in direct contrast to the pattern that existed during the 1980s. As we have seen, state spending grew at a rate of 4.7 percent annually from 1983 to 1991 after adjusting for inflation. But personal income grew by 3.8 percent annually during

[2] There are certainly circumstances where state spending would appropriately exceed the growth of personal income. If the state were taking over responsibilities previously held by either localities or the federal government, state spending could grow faster than income while the *total* tax burden would remain constant. Alternatively, if voters wanted improved services such as better schools, expanded health care, or greater environmental protection, they could essentially direct their elected officials to increase state spending faster than income growth.

Figure 1



this period. Thus, during this period state spending increases exceeded the growth of personal income, notwithstanding the fact that income growth was considerably higher than during the 1990s. This disparity between the growth of spending and income played a role in the ensuing fiscal crisis of the late 1980s and early 1990s, but the same cannot be said in the current situation.

Census Bureau Measures of Spending

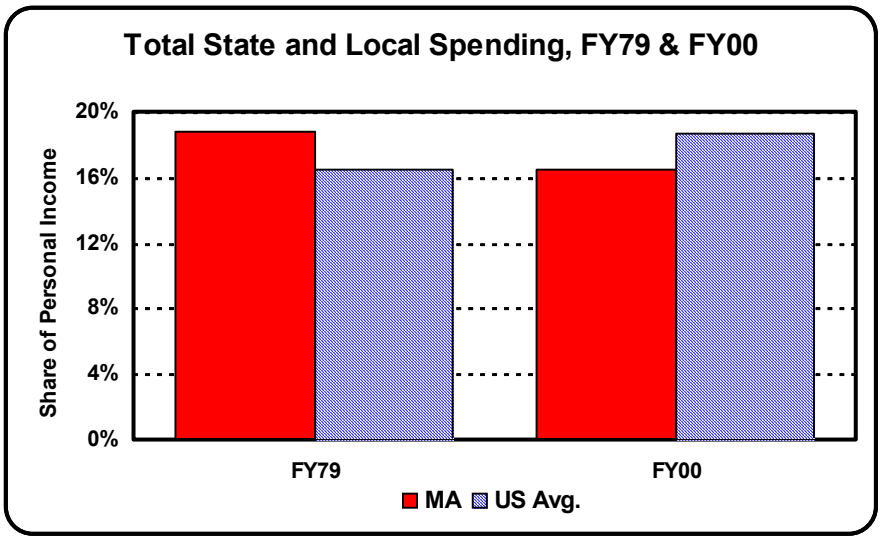
In addition to the data used so far in this report derived from the Comptroller's Statutory Basis Financial Report, the U.S. Census Bureau compiles state and local spending data from all 50 states in an annual report.[3] While the process of compiling this information from all 50 states means that there is a greater lag between the end of a fiscal year and publication than the Commonwealth's own documents, the advantage of the Census Bureau's report is that it allows comparisons among the various states. These comparisons permit a fuller understanding of the pressures facing state and local governments across the country, as well as the relative emphasis states place on priorities such as education or human services, and place Massachusetts in the context that all states face.

The most current Census Bureau report is for fiscal year 2000. The Census Bureau figures clearly reinforce the conclusion that spending growth has not caused the state's current fiscal crisis. Based on the most current national data available, state and local spending as a share of personal income in Massachusetts ranks 45th in the nation; that is, only five states in the nation commit a smaller share of available resources to public services than does Massachusetts.[4]

[3] State spending and revenue data are found at http://www.census.gov/govs/www/estimate00.html. The personal income figures used to make the fiscal data comparable across states are from the Bureau of Economic Analysis' website at http://www.bea.gov/bea/regional/sqpi/.

[4] *Measuring Up: Taxes and Spending in Massachusetts, FY00*, Jeff McLynch and Jim St. George, Massachusetts Budget and Policy Center, January 2003.

These relatively low rankings are the result of explicit policy changes in Massachusetts. In fiscal year 1979, before enactment of Proposition 2½, total state and local spending in Massachusetts ranked 14th in the nation. Over the next 21 years, while total state and local spending nationwide rose from 16.5 percent of personal income to 18.6 percent, spending in Massachusetts fell from 18.8 percent of personal income to 16.5 percent (see Figure 2). During this period, ***state and local spending relative to personal income fell more in Massachusetts than in any state in the nation.***



The Census Bureau data can also help us make sense of concerns that there are simply too many public employees in Massachusetts, or that they are paid too much, and that efforts to balance the budget should be focused on reducing public employment. The Census data show that Massachusetts has fewer public employees than nearly any state and that providing these employees with both pay and benefits consumes a smaller share of personal income here than in most states.

- On average, states and localities across the U.S. employ 535 full-time workers for every 10,000 people in a state; in contrast, Massachusetts employs 516 workers for every 10,000 people. Thus the Commonwealth ranks 42nd in the nation in terms of public employees per capita.[5]

- Not only are there fewer public employees in Massachusetts than in most states, but they are less likely to be "bureaucrats" or patronage hires and more likely to be the sort of front line employees — teachers, fire fighters, and police officers — that the public wants, the loss of which would immediately be felt in every community. On average, just over one-third of all public employees are police officers, fire fighters, and primary and secondary school teachers. Here in Massachusetts, 43 percent of public employees are teachers, fire fighters, and police officers, second only to Rhode Island.

[5] Data on the number of public employees can be found at http://www.census.gov/govs/www/apesstl00.html.

- Ignoring police, fire fighters, and teachers, Massachusetts employs 297 state and local workers for every 10,000 people in the state. That figure is 16 percent below the national average and lower than any state except Pennsylvania and Nevada.

- Not surprisingly, given this relatively low number of state and local government workers, Massachusetts also spends less to pay these workers than most states. While on average, wages and benefits for public employees amount to 6.8 percent of total personal income in a state, Massachusetts spends just 5.7 percent of its income on public employees. Only Hawaii, Connecticut, and New Hampshire spend less by this measure than Massachusetts.

Summary of Findings on Overall Spending

There are several key points regarding overall spending that should be emphasized.

- Massachusetts spends a smaller share of its income on state and local services than most states. Moreover, the share of state resources dedicated to public services has fallen more here over the last two decades than in any state in the nation.

- Inflation-adjusted spending grew much more slowly between 1991 and 2002 than it did between 1983 and 1991. While spending rose at an average rate of 4.7 percent per year during the earlier period, it grew by just 2.3 percent, less than half the earlier rate, between 1991 and 2002.

- Growth in spending during the 1990s failed to keep pace with growth in personal income, which rose by 2.6 percent annually, in contrast to the 2.3 percent annual average growth rate for spending. This trend contrasts sharply with the experience of the 1980s, when spending grew *faster* than personal income.

- Massachusetts has fewer public employees, and spends a smaller share of personal income to pay those employees, than nearly any state in the nation. Of the limited number of state and local employees in Massachusetts, a far greater percentage are the front line teachers, fire fighters, and police officers most valued by the public than in other states.

These findings demonstrate that, despite the healthy expansion of the Massachusetts' economy, state spending did not grow at an excessive rate during the 1990s. To the contrary, spending did not rise as fast as one might have expected, given the growth in personal income. Moreover, and perhaps most striking, by at least one measure — the percent of personal income devoted to spending — Massachusetts lagged behind the rest of the country.

III. SPENDING PRIORITIES IN THE 1990S

Spending Priorities in the 1990s

While measuring overall spending growth in a realistic way is important, and while it is clear that this growth was moderate, it is also important to look at the priorities manifested in the spending changes that did occur. Voters could reasonably be concerned about spending increases if the new priorities did not reflect accurately their goals and desires. On the contrary, however, state spending increases since 1991 were concentrated in just three areas, all of them with significant public support: K-12 education, health care, and corrections.[6]

Figure 3

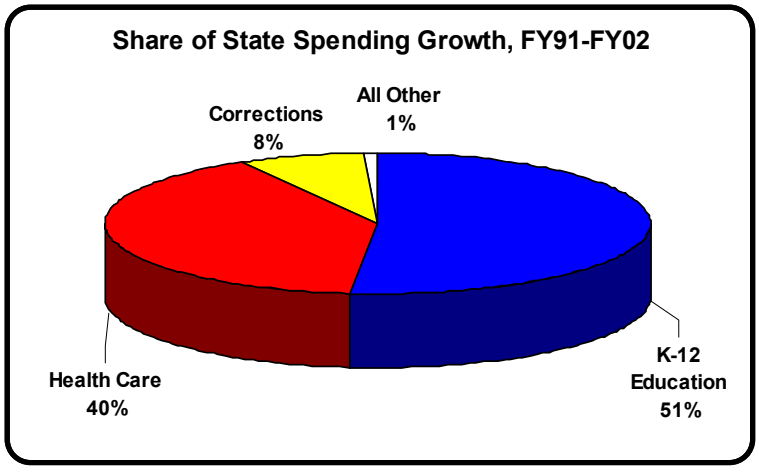


Figure 3 shows that increases in K-12 education, health care, and corrections account for 99 percent of the total increase in state spending between fiscal years 1991 and 2002.[7] In other words, all but one penny on the dollar in inflation-adjusted increases in state spending went to these three priorities. All other spending areas account, on net, for the remaining one percent of

[6] Throughout this section, the report relies on budgeted spending as enacted by the legislature, taking into account all vetoes and supplemental bills, as opposed to actual spending. The SBFR used to measure actual spending changes does not provide sufficient program-area detail to allow a comprehensive analysis of changing priorities.

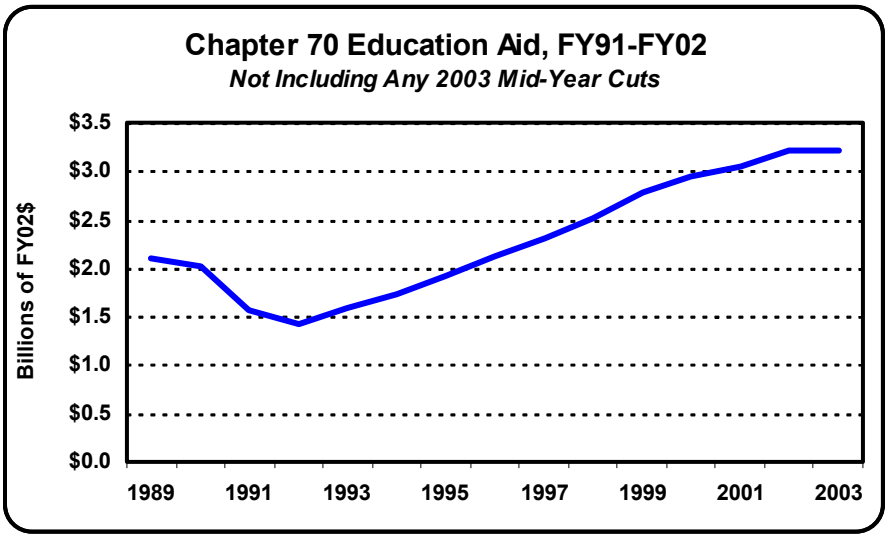
[7] Education includes Chapter 70 local education aid and other Department of Education spending, including School Building Assistance. Changes in health care costs reflect the rise in spending on Medicaid, but do not include the recently implemented senior prescription drug program. Corrections increases reflect new spending on state prisons and county jails.

growth in the budget. Those who would argue that state spending grew too fast during the 1990s ought to explain which of these three priorities should have received less funding.

Education

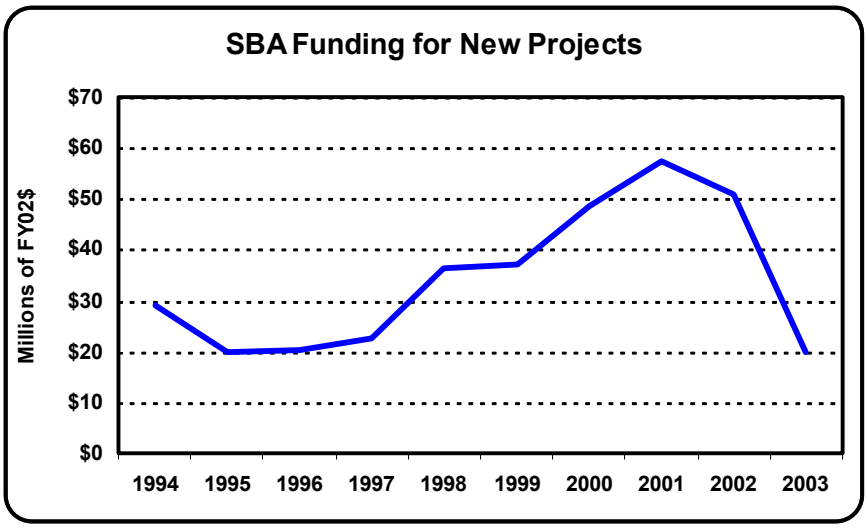
K-12 education alone accounted for over half the increase in state spending during the 1990s after adjusting for inflation, with most of the increase concentrated in Chapter 70 local aid. However, this increase in education spending must be considered in the context of the deep spending cuts that occurred in the years just prior to 1991.
In fiscal year 1989, before the last fiscal crisis hit Massachusetts, Chapter 70 local education aid amounted to $2.1 billion, measured in inflation-adjusted 2002 dollars (see Figure 6). With the onset of the deep recession that hit the state, Chapter 70 was cut deeply over the next three years; by 1991 it had fallen to $1.6 billion, and fell further to $1.4 billion in 1992. In other words, in just three years, real education aid fell by one-third during the last fiscal crisis, creating dramatic impacts on the quality of education in Massachusetts.

Figure 4



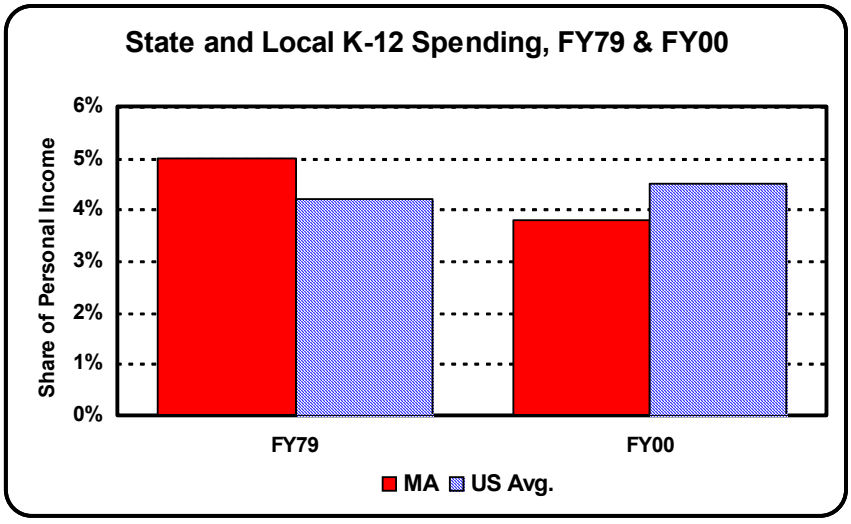
Since then, of course, the legislature has reversed course, implementing education reform and providing regular increases in local aid to education. Even so, it wasn't until 1996 that Chapter 70 education aid returned to the inflation-adjusted level of 1989. Moreover, spending increases have slowed dramatically over the last few years. While inflation-adjusted spending increases averaged over 10 percent a year from 1993 to 1999, the average increase fell to just 3.7 percent a year from 1999 through the current fiscal year. Indeed, the nominal increase in FY03 amounted to less than $50 million, which means that real per pupil expenditures will actually fall slightly. Any new cuts imposed by Governor Romney may mean that even nominal spending would decline.

Figure 5



Looking at other education spending, the school building assistance program and "other" Department of Education spending grew at rates similar to that of Chapter 70. Significant increases were particularly warranted in the case of the school building assistance program. Federal research in the mid-1990s showed that Massachusetts had some of the worst school buildings in the nation.[8] But as shown in Figure 5, while spending on new projects rose from $20 million in FY95 to $57.5 million in FY01 (measured in constant 2002 dollars), the emerging fiscal crisis has already had a brutal impact on efforts to improve school buildings. In just two years, spending has plummeted by nearly two thirds, leaving spending on new school improvement projects today just where it was in the aftermath of the last fiscal crisis.[9]

Figure 6



Finally, it is important to understand that while Massachusetts did make a significant commitment to K-12 education after the passage of the Education Reform Act in 1993, the state still ranks low when its commitment to education is measured as a share of personal income. Looking again at census

[8] U.S. General Accounting Office, "School Facilities: Profiles of School Condition by State," June 1996.

[9] Because of the expansion of the school building assistance program during the last half of the 1990s, the amount spent to finance the state's share of projects already approved and typically finished has gone up substantially since the late 1980s. The cut identified here is for the initiation of new projects.

data, the state ranks 49th in the nation in the share of personal income dedicated to K-12 education. It has not always been this way; in 1979 the state spent 5.0 percent of its personal income on K-12 spending, compared to a national average of 4.2 percent, and ranked 7th in the nation on this measure of spending. By 2000, as Figure 6 demonstrates, the national average had risen to 4.5 percent, but Massachusetts had fallen to 3.8 percent.

Health Care

The story of increased state spending on health care services for the public is largely the story of Medicaid. And while the increase in spending on medical assistance has been significant — after adjusting for inflation it grew by $1.7 billion between 1991 and 2002, accounting for two-fifths of the total budget increase — the story of Medicaid is complex.

In the first place, spending on Medicaid in the state budget is paid for by both the state and federal governments; roughly half of all state Medicaid spending comes directly from the federal treasury. So while the Medicaid line item increased by $1.7 billion during this period, half of that increase or roughly $850 million was financed by the federal government. Thus the increase in Medicaid spending had a far smaller impact on state taxpayers than may be apparent at first glance.

Second, some of the increase in Medicaid spending actually represents a shift in state accounting — but a shift that saves state taxpayers money. During the 1990s the state maximized federal reimbursements under the Medicaid match by ensuring that any public assistance that could qualify as a Medicaid expenditure was shifted to the Medicaid budget. Far from reflecting an increase in state spending, these accounting changes brought in federal dollars that were appropriately due to the state. Again, then, we see that the apparent increase in Medicaid spending exceeds the actual increased cost to taxpayers.

Third, it is important to recognize that only a reasonably small portion of the increase in Medicaid spending actually increased services. Medical costs in Massachusetts, as in the rest of the nation, have begun again to rise quickly. Core costs in the Medicaid program grew slowly here during much of the 1990s, as the state undertook a variety of cost savings strategies. However, once those cost savings strategies were fully implemented, Medicaid costs again began to rise along with the underlying rate of health care inflation.

In fact, the cost of providing continuing services to Medicaid beneficiaries — largely long-term care for the frail elderly and disabled — accounted for nearly two-thirds of the Medicaid increase. All told, expanding coverage to children and their parents accounted for just $622 million of the $1.7 billion increase. With half of that paid by the federal government, state taxpayers financed just over $300 million to expand health care

coverage in the state. Even adding the $80 million senior pharmacy program,[10] health care expansion amounts to less than $400 million, hardly enough to explain continuing multi-billion dollar budget deficits.

Corrections

Next to education and health care, the biggest increase in the state budget during the 1990s was in the area of corrections, including prisons and state funding for county jails. Increases in this area of the state budget accounted for 7.5 percent of the spending growth between FY91 and FY02. This increase reflects a commitment to reduce crime in Massachusetts, another initiative that enjoyed broad public support. During the 1990s, spending on corrections grew by $311 million, an average growth rate of 4.5 percent after adjusting for inflation, or nearly double the rate of growth in the budget as a whole.

Other Program Areas

Outside of these three budget areas — education, health care, and corrections — the rest of the state budget taken as a whole was essentially flat between 1991 and 2002, after adjusting for inflation; while some areas saw modest increases, those increases were balanced with cuts in other areas. When the spending cuts included in the FY03 budget are factored in, other spending areas on balance have fallen since the end of the Dukakis administration. This is hardly the story of excessive spending one might expect, given the overheated rhetoric about state spending and the insistence that the budget should be balanced by spending cuts rather than tax increases. The following is a brief description of budget trends in a variety of other areas.

- The trends in spending on higher education are particularly disturbing. While higher education spending grew modestly between 1991 and 2002 — from $810 million in FY91 to $1.0 billion in FY02 — this was again against a backdrop of deep cuts in the years leading up to 1991.[11] Between 1989 and 1991, spending on higher education fell by 26 percent after adjusting for inflation. Spending continued to fall for the next two years, so that the 1993 level was fully 38 percent below the level of 1989. It was not until 2001 that higher education spending in Massachusetts regained the level of 1989. Since then, however, spending on higher education has again been cut, so that we are once again spending less than in FY89.

[10] The senior pharmacy program cost $80 million in FY02; it is expected to grow to $96 million when fully implemented in the current FY03 budget.
[11] See the table "Ten-Year Schedule of Budgeted Funds Expenditures by Major Program Category" in the Commonwealth's *Statutory Basis Financial Report*, various years.

- *Human Services* — In contrast, spending on human services fell by 3.9 percent between 1991 and 2002. While some components of human service spending experienced small increases (the Departments of Social Services, Mental Retardation, and Public Health all saw modest expansion), much of that growth has been eliminated in the FY03 budget. In nominal dollars, for instance, spending in the Department of Public Health has been cut by $98 million — nearly 20 percent — between FY01 and FY03.

  At the same time, other human service programs were either level funded or cut during the decade. Spending in the Department of Elder Affairs, for instance, grew from $185 million in FY91 to $186 million in FY02 after adjusting for inflation, notwithstanding a significant increase in the elderly population during those years. During the same period spending in the Department of Mental Health fell by 5.9 percent, while spending on cash assistance programs fell by nearly 61 percent.

- *Housing* — Next to cash assistance payments, housing programs were the big losers during the 1990s. Measured in constant 2002 dollars, the state spent $283 million on housing programs in fiscal year 1991. Eleven years later, in FY02, spending in this area had fallen to $120 million, a cut of 57 percent. When the continued cuts in the FY03 budget are factored in, spending on housing programs has fallen by nearly two-thirds since the early 1990s. While it would overstate the impact state housing programs have on the overall housing market to claim that this cut has caused the crisis in affordable housing in Massachusetts, the budget cuts have certainly exacerbated the problems low- and modest-income families have in finding affordable housing.

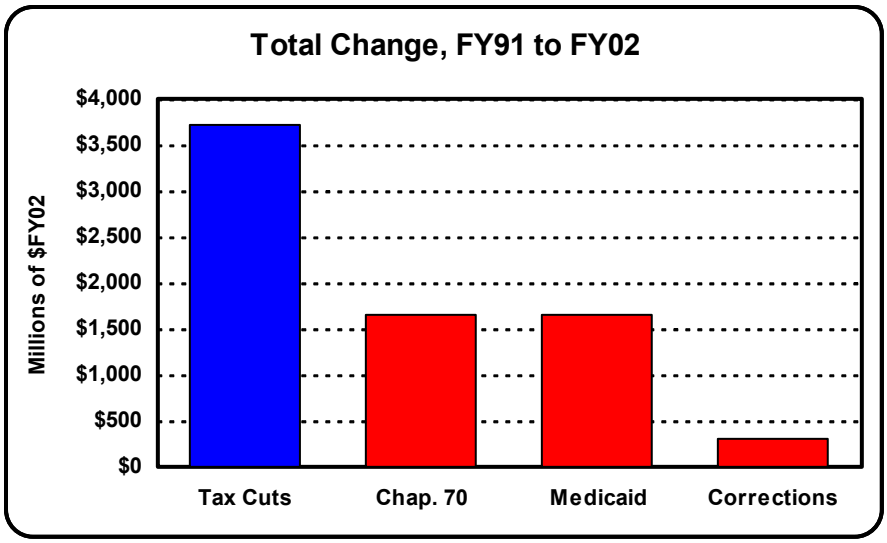
- *Environmental Programs* — Spending on environmental programs has been essentially flat since 1991. Between FY91 and FY02, spending on the environment — which includes everything from maintenance of parks and beaches to implementation of environmental clean-up and protection initiatives — fell by $10.4 million, from $237 million to $227 million. But again, as we have seen in other program areas, the cuts in the FY03 budget have driven the loss of funds far deeper. When the FY03 budget is taken into account, spending on environmental programs will have fallen by $41.5 million after adjusting for inflation, a cut of 19.2 percent since FY91.

- *Local Aid* — There are four major components of local aid: Chapter 70 education aid, school building assistance, lottery aid, and "additional" local aid. While the first two of these are obviously committed to schools, the last two are available for all local services. And while lottery spending increased during the 1990s, the cut in additional local aid exceeded the increase in lottery assistance, leaving general purpose local aid (i.e., non-education local aid) below the level of 1991 after adjusting for inflation. Specifically, combined lottery and additional local aid amounted to $1.4 billion in FY91, but had fallen by $122 million or 8.8 percent by FY02.

IV. TAX CUTS: THE REAL PRIORITY IN THE 1990S

As we have seen, spending in Massachusetts has grown at a modest rate since 1991, with the bulk of the limited growth dedicated to a small number of high priority items. In contrast, the policy agenda was cluttered with tax cuts throughout most of this 11-year period; in February 2002 the Department of Revenue identified 42 tax cuts implemented since 1991, with a total cost when fully implemented of $5.0 billion. After adjusting that figure to reflect some $190 million in tobacco tax increases enacted during the 1990s and last year's approval of a $1.1 billion tax increase, the net change in taxes since 1991 drains the state treasure of $3.7 billion annually.

Figure 7



The $3.7 billion in net tax cuts enacted during this period substantially exceeds the real increases in state spending during the same period. Figure 7 shows how the net tax cuts compare to the inflation-adjusted spending increases since 1991. While much of the political rhetoric in the statehouse since 1993 was focused on the commitment to funding education reform, it is clear from the figure that the state's top priority was cutting taxes.

- In total, Chapter 70 spending increased by $1.7 billion between 1991 and 2002, after adjusting for inflation (and, of course, after three years of deep cuts). That amounts to less than half the amount of revenue we lose each year due to tax cuts.

- Medicaid spending also grew by $1.7 billion during this period. It is important to recall that half of this increase was funded by the federal government, meaning that the state resources dedicated to Medicaid grew by less than $850 million or just over one-fifth the net value of tax cuts.

V. CONCLUSION

Based on this analysis, then, it is extremely difficult to assert that spending has been the major contributor to the state's fiscal crisis. Overall spending increases were modest, whether they are compared to national trends, income growth, or the previous decade. Growth in even the highest priority spending items pales in comparison to the large tax cuts enacted, even after adding back in the tax increase of 2002. The deep cuts already made in the FY03 budget will reduce the already-modest spending growth rates yet further.

This suggests, then, that tax increases to compensate for the overly ambitious tax cuts of the 1990s must be part of any solution to the state's fiscal crisis. The tax increase of 2002 was but a fraction of the tax cuts implemented during each of the previous 11 years. If the state raised even $2 billion in taxes for the FY04 budget, the net tax cut since 1991 would still be nearly $2 billion. There are a number of ways in which the state could restore some of its historic tax base to eliminate the structural deficit. State corporate tax revenue has fallen from 16 percent of state revenue in 1968 to just four percent today. The state income tax rate was at 5.95 throughout most of the 1990s without any damage to the state's economy. Total consumption taxes — including sales and excise taxes — rank 45th in Massachusetts compared to other states relative to personal income.

These varied revenue options make clear that there are reasonable alternatives to the further cuts in education, health care, local aid, or human service programs that would be inevitable if the state budget is balanced without new revenue. To propose that the budget should be balanced by cutting programs — few of which grew to any significant degree during the 1990s and many of which have already been cut substantially — without reconsidering what in retrospect are the clearly unaffordable tax cuts of the 1990s, ignores the reality of budget decisions and priorities of the last decade.