ISSUES BRIEF: PLANNING AND BUDGETING

Perspective

During a time that politicians and newspapers across the nation have dubbed "the biggest recession since the Great Depression," state and local governments have struggled to balance their budgets. In light of these struggles, elected officials are looking at ways to reform their budgeting and planning processes. Many are looking past immediate, short-term budget fixes and are asking bigger questions:

> *Can we establish long term planning processes that will help us maintain a sustainable budget—even in the face of future recessions?*
>
> *Do we have the appropriate balance of revenues coming in and expenditures going out?*
>
> *How can we judge whether we are spending these revenues efficiently, effectively and appropriately?*
>
> *How are we communicating to the public? Is it our responsibility to be more transparent?*

Resources

Primary resources for this brief include National Association of State Budget Officers (NASBO), The National Advisory Council on State and Local Budgeting (NACSLB), Government Finance Officers Association (GFOA), National Governor's Association (NGA), PEW Center on the States, National Conference of State Legislatures (NCSL), Colorado Office of State Planning and Budgeting (OSPB), Colorado Joint Budget Committee (JBC).

Principles

NACSLB:

The National Advisory Council on State and Local Budgeting (NACSLB) has identified "four essential principles of effective budgeting." These principles have been adopted by the Government Finance Officers Association (GFOA), and include:

1. Set broad goals to guide decisions,
2. Develop strategies and financial policies,
3. Design a budget supportive of strategies and goals, and
4. Focus on the necessity of continually evaluating a government's success at achieving the goals that it has set for itself.

PEW (from "Grading the States")

When the PEW center grades states on how successful their fiscal systems are, they incorporate the following into account:

1. The degree to which a state takes a long-term perspective on fiscal matters,
2. The timeliness and transparency of the budget process,
3. The balance between revenues and expenditures, and
4. The effectiveness of a state's contracting, purchasing, financial controls and reporting mechanisms.

Pew notes that transparency in transactions and public access to state fiscal information have become two of the leading indicators of a state that is functioning well in the area of "Money."

This includes best practices in real-time tracking of statewide expenditures and budgeting decisions, as well as joint executive and legislative revenue forecasting approaches. The states with the highest scores are:

- **Utah** (A). Low debt, "balanced scorecard," shared financial system, public participation, performance contracting.
- **Delaware, Nebraska, Virginia, Washington** (A-). Rainy day funds, consensus budgeting, consensus forecasting, centralized/online contracting, performance budgeting, long-term forecasting, structural balance, risk management (audit team).

*Note that **Colorado** received a grade of C+.*

What States are Doing:

Below are examples of budgetary and planning measures various states have taken.
(Sources: NASBO report on State Restructuring Commissions, PEW Grading the States, NGA Fiscal Survey of the States, NASBO Budget Processes in the States)

Budgetary Changes:

Since the beginning of the recession, most states have made necessary changes to their budgets to offset a significant decline in revenues. In general, states are looking towards actions that either 1) reduce expenditures, or 2) increase revenues. Some of these changes, such as furloughs, are immediate, short-term "fixes" to the current budget crisis and are often limited to one or two budget cycles. Others, such as increased taxes, are focused more on ensuring long-term budget stability.

Short-term budgetary changes in 2010 included actions such as:

- Hiring freezes/furloughs/layoffs
- Salary reductions
- Across-the-board percent and/or targeted program cuts
- Reduction of aid to local governments
- Early retirement incentives
- Temporary repeal of tax credits
- Asset sales

Longer-term changes in 2010 focused on:

- Fee/tax increases. In 2010, 23 states enacted net increases in taxes, including increases in sales, personal and corporate income, tobacco, motor fuels, alcohol and other taxes.
- Lottery/gambling expansion
- Cuts to employee/retiree benefits
- Privatization of services/functions (IL, GA, NJ, VA)

Planning Reform:

In addition to making budgetary changes, many states are focused on reforms to their planning process. This includes structural changes, as well as an increase in transparency and performance measures. States have recently looked at/acted on such ideas as:

- Agency reorganizations/mergers (Massachusetts, Indiana, Washington)
- Sunset reviews of all departments on a rolling basis

- Long term planning, e.g. 2 year budget planning cycles. (20+ states have some form of biennial budget cycle. OR,WY, ND have consolidated 2 year budget)
- Rainy day/reserve accounts (Connecticut's "Salary Reserve Account;" Nebraska has big rainy day reserve requirement, as does Delaware)
- Allocation and funding structural changes (e.g. severance taxes, off-the-top transportation dollars)
- Zero-based budgeting (AL, CA, IL, GA, IA, KS, MA, MS, NC, NJ, OH, PA, SC, TX, VA)
- Performance-based budgeting (20+ states use some measures)
- Performance based contracting + online/consolidated contracting (Utah, Delaware)
- Dynamic budgeting/Balanced Scorecard
- Shared services/consolidations, e.g. purchasing, benefits, IT
- Transparency/public process (Michigan dashboard)
- Electronic budgeting systems/Shared financial systems (WI, UT, WV)
- Efficiency reviews (e.g. Colorado's 2007 GEM project + many other states)
- Consensus forecasting requirements (26 states)

Colorado

<u>Budget practices:</u>

Colorado is one of at least 44 states to require a balanced budget. It is a constitutional requirement that the Governor submit a balanced budget, that the Legislature approve a balanced budget, and that the Governor sign a balanced budget. Deficits cannot carry over.

A few specifics about Colorado's budget:

- In Colorado, the Governor can do a line item appropriations veto.
- Colorado does not require consensus revenue forecasting.
- The state's General Fund receives about 95 percent of its revenue from income and sales taxes.
- Colorado has no general obligation debt without voter approval, although the state does carry a unique type of debt in the form of Certificates of Participation (COPs).
- As specified under TABOR, General & Cash Fund revenues are limited to growth of population and inflation
- TABOR provides that revenues which are received that exceed the TABOR revenue limit are to be refunded to taxpayers.
- Colorado's General Fund appropriation growth limit (Arveschoug-Bird) was repealed with SB09-228.
- Colorado does not have formal/statutory performance measurement requirements (23 states require some measures). Note that HB10-1119 took initial steps towards a performance budgeting requirement.
- Colorado's budget does not reflect GAAP—Generally Accepted Accounting Principles (16 states require this).
- Colorado has a limited integration of financial management systems (accounting, payroll).

Colorado Reserve funds:

- Colorado has a 4.0% of General Fund appropriations GF Reserve requirement (statutory), and a TABOR reserve requirement of 3.0% of GF and Cash Fund revenues (constitutional).

- Under current law, the General Fund reserve will gradually increase by 0.5% a year over a five-year period beginning in FY 2012-13 from 4.0% of General Fund appropriations to 6.5 %, assuming a trigger based on Colorado personal income growth is met. Should a budget shortfall occur, current law requires the Governor to formulate a plan to balance the budget after the General Fund reserve has been drawn down to half of its value.
- The TABOR reserve may only be used for emergency purposes – fiscal deficit does not qualify as an emergency under the TABOR reserve.

Pew “Grading the States”:

Colorado’s C+ grade was attributed to factors such as:

- A lack of joint forecasting
- Lack of dynamic budgeting
- A lack of performance budgeting/widespread costs analyses
- “Budget stressing constitutional amendments”
- Contracting/purchasing issues

Note that the Pew report was done in 2008, and at least some changes have occurred in Colorado since that time.

Recommendations from Hickenlooper Transition Committee:

The committee recommended the following items for consideration:

- Change from the short-term planning system currently in place to a comprehensive long-term plan that instills a vision for the state.
- Set strategic goals, including better transparency and objective measurement of efficiency gains.
- Legislatively move to a two year budget cycle.
- Create a comprehensive communications plan.
- Bifurcate the current OSPB director position into a Budget Director and a Planning Director.
- Designate a knowledgeable and experienced CFO in the Governor’s Office

Recommendations from Long-Term Fiscal Stability Commission:

The Commission recommended the following items for consideration:

- Creation of a budget stabilization reserve fund
- Authorization for agencies to enter into public-private initiative agreements
- Comprehensive tax study (i.e. Charlie Brown’s group)
- Creation of a fiscal policy constitutional commission