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New Year, Old Problem - Missouri Facing Major Budget Shortfall in FY 2013

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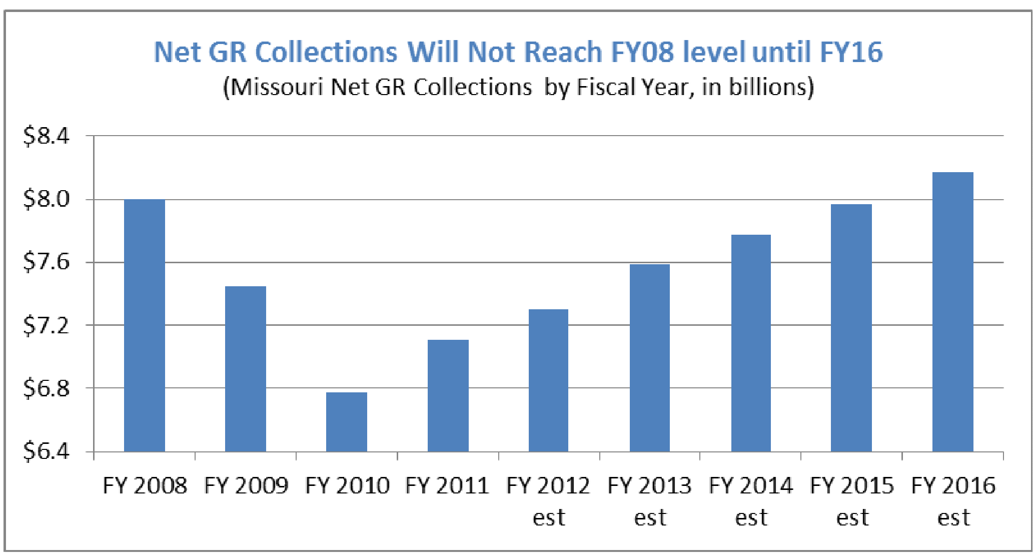
Next week, Governor Jay Nixon will unveil his fiscal year (FY) 2013 budget proposal. While economic conditions have generally improved and Missouri general revenue (GR) collections have been growing, the Missouri Budget Project estimates that the **FY 2013 budget shortfall will be approximately $800 million.** This shortfall stems primarily from two factors: the end of federal assistance to state budget from the American Recovery and Reinvestment Act (ARRA) and the sluggish growth in GR collections.

Despite Increasing Revenue Collections, Missouri Remains in a Deep Hole

In FY 2008, state net general revenue collection totaled $8 billion. Even if the state achieves the consensus revenue estimate of $7.586 billion forecast for FY 2013, **that amount will remain $418 million below the amount collected in FY 2008, prior to the recession.**[1] In fact, assuming that state revenue continues modest growth each year, Missouri still won't reach its pre-recession level of general revenue until FY 2016.[2]



Source: Actual and estimated revenues for FYs 2008 through 2013, *MO Office of Administration;* Estimates for FYs 2014 through 2016, *Missouri Budget Project*

[1] The Consensus Revenue Estimate for FY 2013 is based on 3.9 percent growth compared to FY 2012.
[2] Projected using the historical average growth rate for general revenue of 2.5 percent per year.

Further, Missouri's general revenue remains extremely low by historic measures. As a percentage of the state's economy, Missouri general revenue is lower today than it was in 1985, reflecting just 3.174 percent of the economy compared to 3.774 percent. This measure indicates deep erosion in state revenue and a significant decline in Missouri's ability to invest in services.

Certainly, the sluggish economy that has characterized much of the last three years is a major factor causing the decline in revenue. However, the state's revenue woes are also the result of explicit state policy, including the substantial growth in tax credits as well as tax reductions.

For example, tax credit redemptions in Missouri increased from $343 million in FY 2001 to $545 million in FY 2011 – a 59 percent increase.[3] Moreover, state lawmakers passed the elimination of the corporate franchise tax during the 2011 state legislative session. The tax will be phased out over several years, decreasing state revenue by $35 million in FY 2013 and by $87.5 million annually in FY 2016 when fully phased in.[4]

Analysis - Why the Range of Forecasts?

Missouri's Division of Budget and Planning has estimated that Missouri will face a $460 million budget shortfall in FY 2013 compared to the Missouri Budget Project's estimate of an $800 million shortfall.[5] Both entities begin with the same basic revenue assumptions to calculate their projections. However, the MBP also then includes in its shortfall projection the combined increased cost to cover inflationary adjustments, funding increases that are required by legislation, and the amount of funding needed to maintain current levels of service. For example, the Missouri Budget Project shortfall estimate includes the need to increase "Foundation Formula" spending by about $100 million, as required by statute. By comparison, the Division of Budget and Planning does not take all these cost factors into account when determining the official shortfall estimate.

Therefore, to determine the revenue available in FY 2013, Missouri Budget Project utilizes the state's official "Consensus Revenue Estimate" as prepared by the Office of Administration's Division of Budget & Planning. The most recent estimate calls for net GR growth of 2.7 percent and 3.9 percent in FY 2012 and 2013 respectively, resulting in $7.585 billion in general revenue collections for FY 2013.[6]

Next, the MBP assumes that the base appropriations for FY 2013 will equal FY 2012, or $7.897 billion. The MBP then adds to this amount the following costs:

- The decline of federal stimulus (ARRA) funding;
- An estimated $150 million in disaster recovery costs resulting from the multiple natural disasters impacting Missouri in 2011[7]; and
- An estimated $346 million in statutorily required increases and/or inflationary costs needed to maintain the current level of state services, including increased costs for education, Medicaid, state employee payroll and benefits, and other services.

As a result, the MBP is able to provide a more comprehensive picture of the outlook for FY 2013.

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[3] Missouri Senate Appropriations Committee "Red Books," Annual Fiscal Reports, 2004-2011.

[4] http://www.moga.mo.gov/Oversight/OVER11/fishtm/0336-02T.ORG.htm

[5] http://oa.mo.gov/bp/2013budinst.htm

[6] According to the Office of Administration (http://oa.mo.gov/co/releases/2012/State_Releases_December_2011), through the end of December, net GR collections have grown only 1.2 percent. The state may attain this level of net GR growth given a generally improving economy; however, the current net GR estimate may be optimistic.

[7] Note that there is uncertainty as to this number. In FY 2012 the Senate Appropriations staff reports that only $20 million has been expended for this purpose as of early January.