The Maine View

Published by The Maine Heritage Policy Center

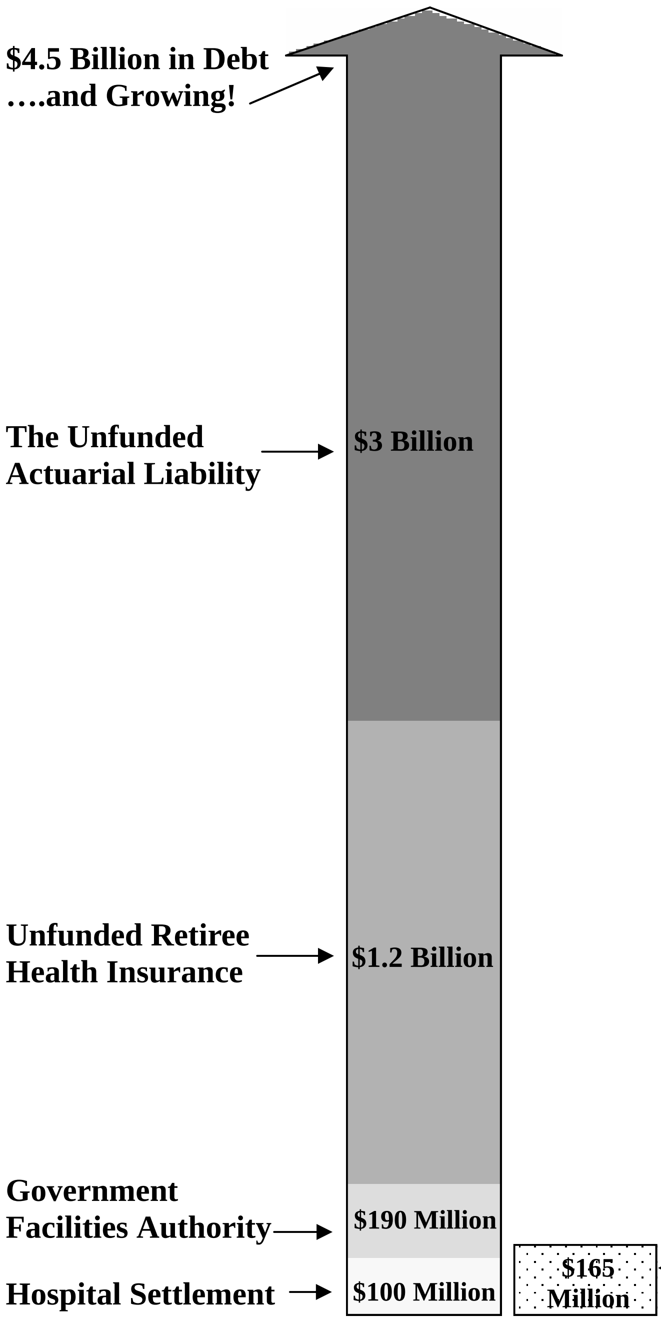
Vol. 4, Issue No. 4

March 29, 2006

Beyond the Supplemental Budget:

What About State Debt, Per Capita Tax Burden, Future Reserves, and the Structural Gap?

by Roy Lenardson



*This is the “**surplus**” driving the current supplemental budget*

Once again the legislature is busy spending the “surplus” that arrives miraculously each year sometime after Christmas, but before the sap flows from Maine’s maple trees. There are a few important points that need to be made about the alleged surplus, from which the Supplemental Budget is derived.

Let us be clear**, <u>there is no surplus</u>.** Ignored hospital bills, growing unfunded liabilities of the retirement system, and shifted costs to future budgets are more than sufficient evidence of the absence of any surplus. Hopefully, policymakers will look beyond the alleged surplus, and instead, make significant policy changes to stem the expanding structural gap forecast for 2008, as well as the **growing mountain of debt**.

• The largest state debt is the **unfunded actuarial liability** owed to the **Maine State Retirement System**. The short fall is estimated to be $3 billion, with a constitutional requirement to pay down the unfunded liability no later than June of 2028.[1]

• The state of Maine is currently carrying approximately $1.2 billion in an **unfunded obligation for health insurance premiums** for retired teachers and state employees. In 1999, Governor King created the Retiree Health Insurance Fund to begin whittling away at the unfunded obligation. However, during the 2004 session, this entire fund was spent in supplemental budgets.[2]

• The **Maine Governmental Facilities Authority** was started in 1998 and allows lawmakers to avoid voter approval for bonding. With a simple majority vote, the Legislature can borrow at will and pass the debts on to future legislatures.[3]

• Under **Medicaid,** hospitals are paid a **provisional interim payment** (“PIP”) every month. The backlog of money owed to hospitals at this time is approximately $300 million in state and federal funds. The state share is about $100 million. It should be noted, that the federal funds are available now, but cannot be released until state funds are committed.[4]

We the people of Maine...
THE MAINE HERITAGE POLICY CENTER

Table 1

Year	National Avg.	Maine's State and Local tax Burden	Maine's Rank
2002	10.2%	12.7%	1
2003	10.1%	12.9%	1
2004	10.2%	13.0%	1
2005	10.1%	13.0%	1

Source: Tax Foundation.

Tax Burden

Another issue often lost in the budget debate is the actual consequence of passing budgets—the resulting tax burden. Recall in 2004, with the introduction of L.D. 1, Governor John E. Baldacci and the Legislature indicated that they were willing to address Maine's tax burden. The legislation even went so far as to statutorily state the policymakers' tax burden reduction goal with the passage: *". . . that by 2015 the State's total state and local tax burden be ranked in the middle 1/3 of all states . . ."*[5]

Well, it stands to reason that if we are currently among the highest in the nation in terms of tax burden, the Governor and the Legislature would need to enact budgets that have the effect of lowering that burden. So, that begs the question—How did they do? Not so well, according to the Tax Foundation, a nationally recognized organization. Table 1 shows that in the first year of Governor Baldacci's term Maine ranked number 1 in terms of state and local tax burden. At 12.7 percent, Maine was 24 percent higher than the national average of 10.2 percent. In 2005, the last year of complete data, Maine ranked number 1 again at 13 percent, or 28 percent higher than the national average of 10.1 percent.[6]

*This year, Maine's tax burden ranked **number 1 again** at 13% . That's 28% higher than the national average of 10.1%.*

If the goal was a lower tax burden, then we are moving in the **wrong direction**.

It's not necessary to use national data. One can look right here in Maine at the figures provided by the Maine State Legislature's Office of Fiscal and Program Review. Maine's per capita total tax burden continues to increase at a rate significantly greater than inflation. In fact, Chart 1 indicates that since 1999 the Maine tax burden has grown more than 25 percent, or about 50 percent faster than the rate of inflation.[7]

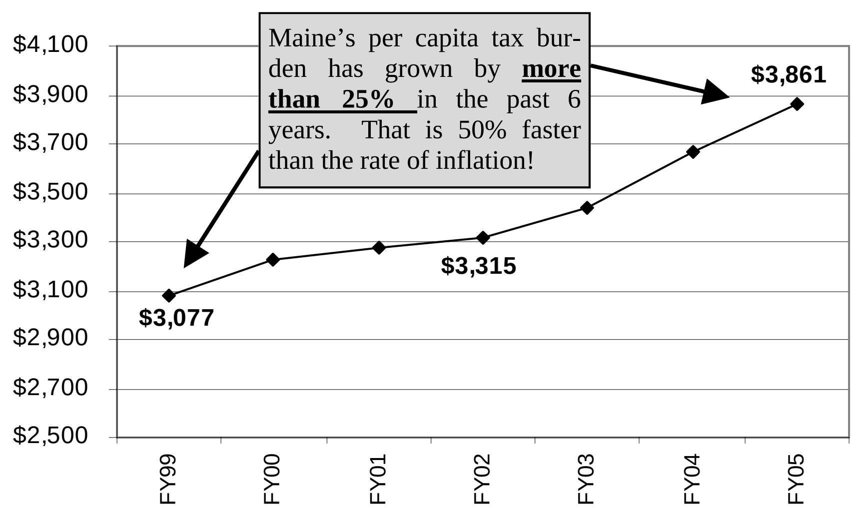
The question is very simple: How does the Governor and the Legislature plan to move Maine's tax burden to the middle of the pack? The follow three budget line items will add to, not lower, the Maine tax burden.

1. **More Positions**. The Supplemental Budget adds **46.5 more state employee positions** paid for in the General Fund. Another 29 state employee positions are financed by Other Special Revenues.[8]

2. **More Mainecare/Medicaid Spending.** The supplemental budget continues to feed the state's fastest growing welfare program, Medicaid/Mainecare**, by adding another $86.7 million in additional spending**.[9] This increased funding creates future problems down the road because it postpones the inevitable expansion of eligibility to the next biennium, as opposed to making the structural changes needed today. In fact, the structural gap analysis prepared by the Legislature's fiscal office, indicated that spending is projected to grow by almost 25 percent in the next biennium. This growth is a direct result of the failure to make long term adjustments to the program.

Chart 1

Maine State and Local Taxes Per Capita 1999-2005



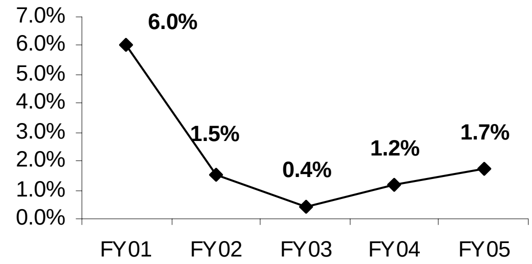
Source: Maine State Legislature. Office of Fiscal and Program Review.

3. **More Education Spending**. On the education front, the continued ramp up of school funding to 55 percent of the full costs of essential program and services (EPS) will result in double digit increases, ranging from 17-20 percent, in both the FY06-

biennial budget, and the FY08-FY09 budget (projected).[10] While the additional school aid will undoubtedly be welcome at the local level, the evidence of a lowered tax burden as a result of the infusion of cash remains questionable, and will remain that way until the Governor and the Legislature implement meaningful controls on spending at all levels of government.

Chart 2

Ending Balance of the Maine Budget Stabilization Fund as a % of General Fund Revenue



Source: Maine State Legislature. Office of Fiscal and Program Review, Compendium of State Fiscal Information, Jan. 2006.

Future Reserves

In 2003, the Governor and the Legislature replaced the Maine Rainy Day Fund with the Maine Budget Stabilization Fund. The amended fund is primarily used for the prepayment of General Fund bonds or for major construction (projects greater than $500,000).[11] In the last session of the Legislature (2005), the Legislature further amended the Maine Budget Stabilization Fund so that it's primary purpose is to address revenue shortfalls.

In 2005, the ending balance was just 1.7 percent of General Fund Revenue, down from the high and statutory cap of 6 percent, in 2001 (see Chart 2). The Governor's Supplemental Budget proposes to place $35 million in the Budget Stabilization Fund, in 2007. Of course, the same budget also proposed to undo a budget gimmick from 2005, in which the Legislature in essence, created money out of thin air to balance the books in 2006. The Legislature achieved this by loaning some money to the 2006 budget from the 2007 resources.[12]

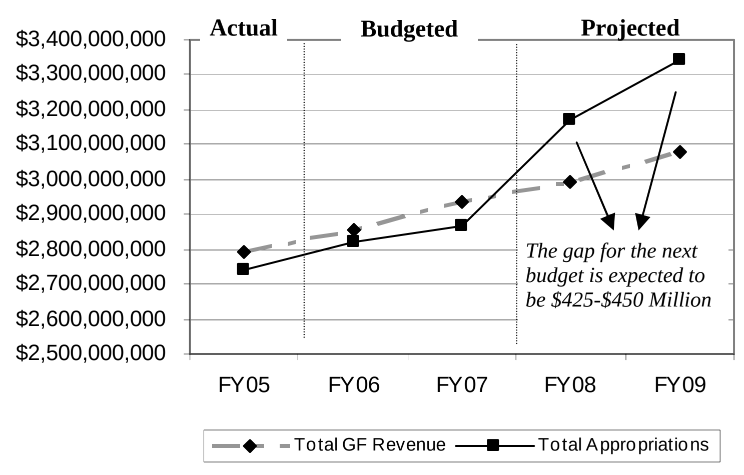
Unfortunately, that plan backfired. The state coffers swelled, making the loan unnecessary. Here comes the best part: as a result of the legal requirements governing budget resources, a law was triggered that would automatically move the "loan" money to the Maine Budget Stabilization Fund.[13] Unfortunately for Maine taxpayers, that money will likely never make it to the Maine Budget Stabilization Fund. The Governor proposed to "undo" the "loan," which triggered the transfer. At the end of the day, he can claim $35 million more for the Maine Budget Stabilization Fund, but in truth, more than **$7 million** was cut in reserve revenue from what would have transpired if the dubious borrowing never happened.[14]

The Structural Gap

What about the next biennium? Will Maine be on the right track to move toward the middle of the pack in the next budget? One excellent barometer of future budget stability can be found in the structural gap analysis provided by the Office of Fiscal and Program Review in the ***Structural Gap Estimate: March 2006***.

Chart 3

General Fund Structural Gap



Source: Maine State Legislature. Office of Fiscal and Program Review.

> *"Despite revenue revisions increasing 2008-2009 General Fund revenue projections by almost $50 million, updated estimates of the costs of General Purpose Aid for Local Schools and Medicaid/ MaineCare programs result in virtually no net change in the General Fund structural gap estimate of **$425 to $450 million** released after the 1st Regular and 1st Special Sessions of the 122nd Legislature.*
>
> *The extent of the future imbalances will depend largely on the decisions regarding the use of the current biennium budgeted ending balance of $113.1 million and the initiatives used to address the 2008-2009 General Fund structural balance. Even assuming that GPA growth declines dramatically in the 2010-2011 biennium and that the methods to balance the 2008-2009 biennium do not exacerbate the gap further,* ***the 2010-2011 structural gap may exceed $600 million*** *based on longer term projections of revenue growth and spending needs."*[15]

It is not difficult to pinpoint the drivers in the structural gap. MaineCare spending is projected to grow nearly 25 percent in FY08-FY09 and education spending is expected to grow by almost 20 percent.[16] Fiscal restraint seems highly unlikely if the past decade is any indication of future performance.

Conclusion

In the end, whether it is the **ballooning debt**, the **expanding per capita tax burden**, the **anemic reserves** for rainy days, or the **ominous structural gap** forecast, there is little hope that Maine will ever see a lower tax burden as long as these four fiscal challenges continue to plague the Maine taxpayer.

Methodology

The total state debt number was calculated based on state debt incurred by the Maine State Legislature. General Obligation Bonds were not included in the calculation because those bonds were not only approved by the Legislature, but also, approved by the Maine voters. The voter approval legally obligates Maine government to issue the debt. However, all other outstanding debt is the direct result of legislative action. Currently, Maine has $487 million in outstanding General Obligation Bonds.[17]

Sources

1. State of Maine, Office of the State Treasurer, *Maine's 2004 Tax-Supported Debt profile as of June 30, 2005.*
2. IBID.
3. Maine State Legislature, Office of Fiscal and Program Review, *Compendium of State Fiscal Information*, Jan. 2006.
4. Maine Hospital Association, *Testimony in Support of LD 1968.* http://www.themha.org/advocacy/2006supplementalbudget.htm
5. MRSA, section 7301.
6. Tax Foundation, *Tax Freedom Day Report*, 2002-2005.
7. Maine State Legislature, Office of Fiscal and Program Review, *State and Local Tax Burden*. http://www.maine.gov/legis/ofpr/taxinfomain.htm.
8. Maine State Legislature, Office of Fiscal and Program Review, *LD 1968, Governor's 2006 - 2007 Supplemental Budget 122nd Legislature, 2nd Regular Session*.
9. IBID.
10. Maine State Legislature, Office of Fiscal and Program Review, *Compendium of State Fiscal Information*, Jan. 2006.
11. Maine State Legislature, Office of Fiscal and Program Review, *Structural Gap Estimate: March 2006*.
12. State of Maine, Bureau of the Budget, *2006-2007 Biennium Budget*.
13. Maine State Legislature, Office of Fiscal and Program Review, *Compendium of State Fiscal Information*, Jan. 2006.
14. Maine State Legislature, Office of Fiscal and Program Review, *Overview of the Governor's 2006-07 Supplemental Budget*
15. Maine State Legislature, Office of Fiscal and Program Review, *Structural Gap Estimate: March 2006*.
16. IBID.
17. Maine State Legislature, Office of Fiscal and Program Review, *Compendium of State Fiscal Information*, Jan. 2006.

Roy Lenardson is a Senior Adjunct Fellow at The Maine Heritage Policy Center. The author can be reached at rlenardson@mainepolicy.org.

The Maine View is a publication of The Maine Heritage Policy Center that provides research, historical perspective, updates and commentary on current public policy issues. All information is from sources considered reliable, but may be subject to inaccuracies, omissions, and modifications.

The Maine Heritage Policy Center is a 501 (c) 3 nonprofit, nonpartisan research and educational organization based in Portland, Maine. The Center formulates and promotes free market, conservative public policies in the areas of economic growth, fiscal matters, health care, and education – providing solutions that will benefit all the people of Maine. Contributions to MHPC are tax deductible to the extent allowed by law.

Editor and Director of Communications, Jason A. Fortin

P.O. Box 7829
Portland, ME 04112
207.321.2550 (p)
207.773.4385 (f)
www.mainepolicy.org