Coping with State Budget Deficits

Janet G. Stotsky*

In recent years, state budgets have been the bright spot amid government budgetary problems. But now, like the federal government, many states, especially those in the Northeast, are facing budget problems. And more bad news may be on the way for states that have so far slid by with only minor adjustments.

The primary reason for these budgetary imbalances is the slowdown in the national economy. After recovering from a severe recession in 1981-82, much of the nation, especially the East and West coasts, experienced robust economic expansion. Many coastal states used this opportunity to increase spending rapidly for a wide range of programs. But other regions, such as the Midwest, did not prosper to the same degree. Unable to engage in the same spending splurge, they were left with healthier budget situations as the economy slowed. Meanwhile, states heavily dependent on energy industries never experienced the boom at all, instead sinking into recession as oil prices fell in the mid-1980s. These states are finally emerging from their

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budget problems just as others tumble in (Figure 1).

What are the causes of recent state budget problems? How do states manage these problems? And are there ways in which states can minimize these problems?

WHY ARE THERE PROBLEMS?

Economic slowdowns cause budget problems for state governments by reducing revenues and increasing some expenditures above expected levels. (See How States Forecast Revenues, p. 16.) In the past decade, this fiscal stress during economic downturns has been compounded by cutbacks in federal government aid, increased demands from local governments, relentlessly rising costs for certain basic services, and the inability of states to accumulate sizable reserves.

The Impact of Economic Growth on Expenditures and Revenues. During slowdowns, state spending rises above expected levels as people lose their jobs or face reduced workweeks and become eligible for unemployment compensation, welfare, and other income-transfer programs. Moreover, slowdowns cause tax revenues to decline below expected levels.

States are cushioned somewhat from the full impact of these cyclical changes because they share funding responsibility with the federal government. States currently pay approximately 44 percent of the two largest means-tested

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**Figure 1a**

Regions in Which State Expenditures Grew More Slowly in the 1980s...

(Fiscal 1980 - 1988)

<table>
<thead>
<tr>
<th>Region</th>
<th>Growth of General Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td>West</td>
<td>3.6</td>
</tr>
<tr>
<td>South West</td>
<td>2.5</td>
</tr>
<tr>
<td>Rocky Mountain</td>
<td>2.4</td>
</tr>
<tr>
<td>Plains</td>
<td>1.8</td>
</tr>
<tr>
<td>Great Lakes</td>
<td>1.9</td>
</tr>
<tr>
<td>South East</td>
<td>2.9</td>
</tr>
<tr>
<td>Mid-East</td>
<td>3.5</td>
</tr>
<tr>
<td>New England</td>
<td>4.4</td>
</tr>
</tbody>
</table>

*Note: Balances are budget stabilization and rainy day funds. Because of inconsistencies that arise from definitional changes in General Fund data at the state level, we have chosen to use General Expenditures for the time series in Figure 1a.*

*Source: U.S. Bureau of the Census*
States can make the transition from boom to bust very quickly and unexpectedly. "Over the last 18 months, tax revenues have fallen precipitously and we still don't know where the bottom is," said S. Stephen Rosenthal, chief secretary to former Governor Michael S. Dukakis of Massachusetts, one of the states with the worst budgetary problems.\(^2\)

The sensitivity of revenues to changes in the level of economic output or income is measured by what economists term the income elasticity of revenues.\(^3\) The more sensitive tax


\(^3\)The income elasticity of revenues is given by the percentage change in revenues divided by the percentage change in income. An elasticity greater than 1 indicates that revenues change by a greater proportion than income, which is termed an elastic response. An elasticity less than 1 indicates that expenditures or revenues change by a smaller proportion than income, which is termed an inelastic response.

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**FIGURE 1b**

... and Had a Better Cash Balance in 1990

(Fiscal 1990)

Balances as a % of General Fund Expenditures

-5 0 5 10

Far West South West Rocky Mountain Plains Great Lakes South-East Mid-East New England

How States Forecast Revenues

State governments base spending on revenue forecasts, so it is essential that they have a precise method for forecasting revenues. Unfortunately, forecasting revenues is an imperfect science. State budget offices use several different methods. A common one is to simply extrapolate previous trends into the near future. This method, however, fails to incorporate all of the information about future economic conditions that may be available to budget planners. Another method, which has become more widespread in recent years, is to use regression analysis and formal econometric models.

Two recent studies find that state revenue forecasts tend to have a downward bias, meaning that revenues tend to be underestimated. This bias should, in theory, help states guard against budget shortfalls. Several reasons have been suggested for a downward bias to revenue estimates. First, uncertain tax revenues mean that states cannot be assured of meeting revenue targets. With a balanced-budget requirement, a downward bias to the forecast protects against an unexpected shortfall. Second, a downward bias to the revenue forecast means that a state is less likely to end up with a surplus and may create discretionary funds for the executive.

In separate studies, William Klay and William Gentry suggest that a downward bias to revenue forecasts is undesirable because, with a balanced-budget requirement, such a forecast constrains spending. An upward bias (revenues are overestimated) may allow states with balanced-budget requirements to realize budget deficits when the state runs out of money at the end of the fiscal year. But politicians are under pressure when either a large deficit or surplus occurs. Large deficits must be eliminated, and surpluses suggest that taxes were set too high. This bias against either deficits or surpluses should mitigate the tendency for either a pronounced downward or upward bias.

Politics may unduly influence economic forecasts and budget policy. Even if a state budget office were successful in predicting an economic downturn, it might be hard to convince elected officials to cut spending plans or raise revenues before the downturn had actually materialized. Thus, the political bias may be to ignore the signs of a downturn until the budgetary situation has become dire and support can be galvanized for cutbacks in spending or for revenue increases.

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1 See Daniel R. Feenberg, William Gentry, David Gilroy, and Harvey S. Rosen, "Veering the Rationality of State Revenue Forecasters," The Review of Economics and Statistics (May 1980) pp. 300-08. They find little evidence to suggest that econometric techniques provide superior forecasts, though their sample is limited to only three states.


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revenue is to changes in income, the greater the elasticity. Personal and corporate income taxes are generally regarded as having the greatest income elasticities, followed by the general sales tax, wealth taxes, and selective sales taxes. 4

Since state governments derive a large part of their tax revenues from a mix of income taxes and the general sales tax, their tax revenues tend to be elastic. This dependence on income-elastic taxes exerts a destabilizing influence on the budget because revenues grow more rapidly than income in expansions and revenues shrink more rapidly in recessions. 3 In recent decades, state governments have relied increas-
ingly on income-based taxes, making state taxes more sensitive to economic fluctuations.\footnote{This was first noted in Harold M. Groves and C. Harry Kahn, "The Stability of State and Local Tax Yields," American Economic Review (March 1962) p. 88. William F. Fox and Charles Campbell, in "Stability of the State Sales Tax Income Elasticity," National Tax Journal (June 1964) pp. 201-2, investigate the stability of the sales tax income elasticity over the business cycle and argue that a varying elasticity may provide more stability than a constant one.}

\textbf{Intergovernmental Pressures.} State budgets have responded to these challenges by shifting funds from one level of government to another. Federal grants-in-aid have increased as a percentage of total state-local outlays. This has led to the development of new federal-state-local partnerships, often referred to as "fiscal federalism." The Federal Grants-in-Aid (FGA) program is a key example of this new fiscal federalism, where the Federal government provides direct grants to state and local governments to support various programs.

\textbf{FIGURE 2} Federal Grants-In-Aid Decline as a Percentage of Total State-Local Outlays (Fiscal 1970 - 1989)

\begin{center}
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|}
\hline
\hline
Percent & 19.0 & 22.6 & 25.8 & 24.7 & 21.6 & 31.3 & 20.9 & 20.9 & 20.5 & 18.2 & 18.1 & 17.1 \\
\hline
\end{tabular}
\end{center}


As state and local governments have become more dependent on federal grants, concerns have risen about the fiscal health of these levels of government. The Federal government's role in funding programs has increased, leading to questions about the sustainability of this funding model. States and localities have shifted their reliance on federal grants, leading to a more diversified funding base.

\textbf{7We aggregate state and local aid because the break-down between state and local responsibilities varies from state to state and because some of the federal aid to states is passed through to local governments. An increasingly large percentage of the aid in direct grants to individuals through income-transfer programs, rather than aid for state and local government programs.}
a result, states must depend more on their own resources to pay for public services. One recent change in the federal tax law has compounded the effects of these aid cutbacks. The Tax Reform Act of 1986 eliminated the deductibility of the state sales tax for federal tax purposes. This deductibility had lowered the cost of the sales tax for taxpayers who itemized deductions on their federal income tax returns. In effect, these taxpayers did not pay federal taxes on income used to pay the state sales tax. The elimination of deductibility means that states cannot shift part of the burden of the sales tax to the federal government.

Another source of pressure on state governments has come from local governments. To recent years, state governments have been under pressure from hard-pressed cities, counties, and school districts to assume responsibilities for certain programs and to increase intergovernmental aid. This aid is substantial, comprising more than one-third of state general expenditures. Revenues from the local property tax, the mainstay of local tax revenues, have been unable to keep up with demands for local public services. The pressures stem also from demands at the local level for redistribution from wealthier communities to poorer communities.

Cost Pressures. In addition to the intergovernmental pressures, state governments face relentlessly rising costs for many important public services. Medicaid is one such area. In recent years, health care costs have been rising more rapidly than inflation. In addition, Congress has mandated new benefits for Medicaid enrollees or expansion of coverage, and federal courts have ordered states to increase reimbursement rates to hospitals. States are also spending an increasing share of their budgets for corrections because of severe prison overcrowding. In fact, many states are under court-ordered mandates to improve conditions in their prison systems.

Low Levels of Reserves. A contributing factor to states' current budgetary problems is the low level of cash reserves they hold. Many states have Rainy Day Funds in which they hold surplus revenues for times of budgetary stress. A generally accepted rule of thumb in state government budgeting is that reserves be equal to approximately 5 percent of the current budget. Cash reserves can be used to create a countercyclical fiscal policy. As revenues fall in a downturn, previously accumulated cash reserves can be used to cushion the impact of

8For every $1 the taxpayer pays in deductible state and local taxes, federal taxable income is lowered by $1. Thus, the effective price of a dollar of state taxes is 1 minus the taxpayer's marginal tax rate. If the taxpayer faces a marginal tax rate of 28 percent, the effective price of $1 of state tax payments is $1 minus 28 cents, or 72 cents. See Harvey S. Rosen, "Thinking About the Deductibility of State and Local Taxes," this Business Review (July/August 1988) pp. 10-23, for a discussion of this issue.

Another change was limiting the use of tax-exempt state debt for private purposes, which state governments use to subsidize private businesses. The tax-exempt feature of this debt allows state governments to issue it at a lower interest rate than prevails in the market because its return must only be competitive with the after-tax return to taxable debt. By curtailing the use of this debt, state governments will have to find other means to provide these subsidies.

9Public education is one area where most state governments are under pressure to increase their funding responsibilities. Although public primary and secondary school education was once largely the responsibility of local governments, approximately half of the funding for it now comes from state governments. In some states, this spending results from court-ordered mandates to equalize spending across school districts. An example is the June 1990 New Jersey Supreme Court decision that requires substantial increases in funding to poor school districts. In 1990, the New Jersey legislature enacted an increase in the state income tax for the purpose of funding equalizing aid to school districts across the state, with the lowest-income communities scheduled to receive a larger share of this aid. Litigation, currently under way in many states, may require similar actions elsewhere.
this shortfall. As revenues rise in an upturn, surpluses can be allowed to accumulate.11
In recent years, the arrangements for Rainy Day Funds have become more formalized, even
though most states have not met their reserve goals. As a practical matter, it is difficult for
state governments to maintain reserves, since there are always pressing needs and political
pressure for government spending. Thus, the

National Tax Journal (December 1986) pp. 483-97, for a dis-
cussion of how states can use Rainy Day Funds to achieve
fiscal stability. Also see Peter D. Skaperdas, “State and
Local Governments: An Assessment of Their Financial Po-

tition and Fiscal Policies,” Federal Reserve Bank of New

LIMITATIONS ON STATE GOVERNMENTS
Unlike the federal government, states cannot submit a budget that will be balanced by
the issuance of debt. All, except Vermont, face balanced-budget requirements on their oper-
ating budgets. In contrast to the federal gov-

ernmment, state governments separate their budgets into a current (or operating) budget and a capital budget. The operating budget refers to expenditures and revenues for the
current year. Operating expenditures include
general expenditures for all functions, some
utilities expenditures, pension contributions,
and payments for debt service. Operating

\[ \text{FIGURE 3} \]

The Sizes of Total State Year-End Balances
Are Low as a Percentage of Expenditures
(Fiscal 1978-1991)

\[ \text{Percent} \]

\[ \begin{array}{cccccccccccc}
6.6 & 8.7 & 4.0 & 4.4 & 2.9 & 3.8 & 5.2 & 4.3 & 4.9 & 3.0 & 2.7 & * & & \\
\end{array} \]

\* Estimated
Source: Fiscal Survey of the States (March 1990)
revenues include taxes, fees, intergovernmental aid (mostly from the federal government), and interest on investments. The capital budget refers to expenditures and revenues for long-term capital projects, such as the construction of schools and highways. Capital projects are typically financed by borrowing.

Stringency of the balanced-budget requirement varies from state to state. Some states' governments are required only to submit a balanced budget, but may be allowed to borrow at year-end if they run out of funds. Other state governments are required not only to submit a balanced budget, but to realize a balanced budget at year-end. This requirement is more restrictive since it means that states must act immediately to bring their budgets into balance if expenditures exceed or revenues fall short of expectations. The advantage, however, is that states are forced to address their problems immediately and cannot compound fiscal woes by pushing off deficits into the future.

The Third District States—Delaware, New Jersey, and Pennsylvania—all share the limitation that the governor must submit a balanced budget, the state legislature must pass a balanced budget, and the governor must sign a balanced budget. Of the three, only Pennsylvania is allowed to carry over the deficit into the next fiscal year, which gives it greater budget flexibility.

Although balanced-budget requirements limit a state government's flexibility in times of budget shortfalls, this limitation on the uses of government debt is important. The use of long-term debt to finance capital projects, for example, spreads out the cost of these projects over a long-term horizon. If the benefits of these projects accrue over the same or a similar horizon, then it is fair that future taxpayers pay part of the cost of these projects. The use of long-term debt to finance current expenditures is not justified unless the government seeks to make an explicit transfer from future taxpayers to present taxpayers.

To avert cash-flow problems under normal budgetary conditions, some state governments may issue short-term debt. But states may create fiscal dilemmas if they issue large volumes of short-term debt and carry this debt over into subsequent years to hide persistent budget deficits. States may also create fiscal problems if they redefine current expenditures as capital expenditures, in order to circumvent balanced-budget requirements.12

High levels of long- or short-term debt can impose undue debt-service burdens on government. For instance, high levels of debt and debt per capita have been linked to lowered bond ratings and higher interest costs on debt.13 These higher interest costs can substantially raise the cost of capital projects, possibly leading to inadequate investment in infrastructure.

Tax Limitations. State governments fight a difficult battle to obtain tax increases. The points President Bush scored with his "no new taxes" pledge suggests the hostility taxpayers have to tax increases. And voters convey this message loudly and clearly at the polls, having frequently voted to overturn tax increases and budgets in recent years. In addition, the tax revolt of the late 1970s and early 1980s led to the passage of tax and expenditure limitations in many states. The most common form is to limit the growth of revenues or expenditures to the growth of state personal income. Several states limit growth to the sum of the inflation rate and the growth in population, or to fixed

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annual percentage increases. Evidence sug-
gests, however, that these limitations have not
been very effective in constraining state gov-
ernments. Nevertheless, state officials work
within a constrained environment, having lim-
ited ability to raise additional revenues.

CURES FOR BUDGET DEFICITS
If a budget deficit arises, it can be financed in
several different ways. One way is to draw
down any reserve funds. Large deficits, how-
ever, require spending and revenue adjust-
ments that can either be short or long term in
nature.

Postpone or Cut Spending. On the spend-
ing side, a large deficit may require states to
postpone or cut spending. States may have
some short-term flexibility in paying their obli-
gations. One well-known tactic is to move
expenditures—such as payments to state gov-
ernment employees, to vendors, or to local
governments—into the next fiscal year. This
tactic may allow a state to avoid a current-year
operating deficit; however, it is at best a stop-
gap strategy because the additional revenues
must be raised in the following year. States
may also defer or eliminate capital expendi-
tures, though delaying needed projects may
raise their ultimate cost. Other tactics include
undermaintaining the infrastructure and un-
derfunding the contribution to the employees’
pension system or borrowing from it. But these
tactics, while they may result in some short-
term gains, only thrust the problems onto fu-
ture taxpayers. State governments can also cut spending.

The main problem on the spending side is that
states have little flexibility for cutting their
budgets in the short term. A large proportion
of state spending goes for goods and services,
including contractual wages and salaries, leav-
ing state governments with little room for dis-
cretionary spending cuts. Even in the long
term, employees will not typically accept cuts in
their nominal wages. It may be possible, how-
ever, to cut spending by imposing a hiring
freeze or by reducing the size of the work force.

Since state governments provide sizable aid
to local governments, this is one area in which
they may have some flexibility in cutting spend-
ing, although, in the case of education, the
largest aid component, they may face restric-
tions on short-term cuts. In addition, reducing
aid to local governments may help a state
government tackle a budget crunch, but it ends
up pushing the problem onto local govern-
ments.

Where state governments have budget flexi-
bility, they may choose either across-the-board
or selective cuts. Across-the-board cuts give
the appearance of distributing the burden equi-
ably, but they are not typically justified on
economic grounds unless the last dollars spent
on all programs are equally valued. The prob-
lem state governments face with spending cuts is
that the need for these cuts generally appears
well into a fiscal year. Thus, the burden of
cutbacks falls more heavily on departments
and programs than if the cutbacks were spread
out evenly over the entire fiscal year. A cut-

12See Depline A. Kenyon and Karen M. Benker, “Fiscal
Discipline: Lessons from the State Experience,” National Tax
Effectiveness of Tax-Expenditure Limitations: A Reevalua-
tion,” American Journal of Economics and Sociology (April
1990) pp. 223-38. Balls presents evidence suggesting that
tax limits appear to resistable forces more than ceilings. He
does not, however, address the issue of how high taxes
would have risen in the absence of these limitations. Cali-
ifornia and Massachusetts would seem to be the two excep-
tions where tax revenue did result in a significant impact on
tax and spending levels.

13See Corina L. Eckel, “State Deficit Management Strate-
gies,” National Conference of State Legislatures (November

14See Robert P. Inman, “Paying for Public Pensions: Now or Later?” This Business Review (November/December
1985) pp. 3-12.
back of 4 percent for the year translates into an 8 percent cutback if it applies only to the latter half of the year.

In the long term, states may have to rethink priorities for state spending and redirect money to programs that they feel are the most essential. These changes require a certain degree of political consensus between the governor and the state legislature, however.

Rafael Taxes. On the revenue side, a large deficit may require governments to take such short-term measures as accelerating their collection of taxes or raising taxes or other revenues. State governments can accelerate tax collection by changing the interval for collection from annual to quarterly or from quarterly to monthly. This creates a bonanza in the first year because of the earlier collection of taxes. But unless the collection is slowed thereafter, this tactic can only be used once. State governments may also increase tax revenues by raising the rate of existing taxes, by broadening the base to which a tax applies, or by instituting a new source of tax revenues altogether. None of these methods is easily accomplished.

To raise substantial amounts of additional revenues, state governments generally turn to the general sales or income taxes, the largest state taxes, comprising approximately 20 and 23 percent of general revenues, respectively. Even a small change in these tax rates can produce large increases in revenues. The sales tax is typically viewed as falling disproportionately on lower-income households and the personal income tax as falling disproportionately on higher-income households, which may enhance the political appeal of the personal income tax. Selective sales or excise taxes may also be used as a source of revenues and are sometimes easier to raise expeditiously because they are perceived as involving smaller amounts of revenues than the more broad-based taxes.

State governments can also raise taxes by broadening the base of the tax. Although the general sales tax originally applied only to goods, many states have now extended it to services as well—potentially a large source of revenues. Taxing services would be likely to reduce cyclical variation in sales tax revenues because purchases of many services are less cyclical than purchases of consumer durables. Moreover, the general sales tax can be broadened by adding goods to the base that are now exempt. This would also reduce cyclical variation in sales tax revenues because exempt items tend to be necessities and expenditures on them would be less likely to vary with economic conditions. This would have the undesirable effect of increasing the tax burden on lower-income households. The elimination of sales tax deductibility for federal tax purposes has made sales taxes a less attractive source of new revenues for the states. They are more likely to cut back spending, or shift toward other forms of revenues. The base of the income tax can be broadened by eliminating deductions, exclusions, and other preferences.

State governments also face the following dilemma: although in the short run raising taxes may help balance budgets of fund public services, in the long run these taxes may inhibit businesses and households from wanting to locate or remain in the state. Thus, the long-run tax base may be hurt by high taxes. But the effect may be mitigated to the extent that higher taxes pay for better public services.15

15See Janet G. Stetsky, "The Effect of the Elimination of State Sales Tax Deductibility on State Fiscal Decisions," Public Finance Quarterly (January 1990) pp. 23-46, for evidence that this change should lead to less reliance on the state sales tax.

User Fees. Another way to raise revenues is by charging or increasing user fees for services. These fees could be tolls for highways, bridges, and tunnels, or tuition at state universities. The advantage of user fees is that they are paid in proportion to the use of the service and thus resemble payments for private goods. The disadvantage is that they tend to discourage the use of these services, which may be basic services, and their burden falls disproportionately on lower-income households.

States may thus use many different methods to correct budget imbalances. On the spending side, they may delay spending or make cuts in already budgeted programs. On the revenue side, they may raise taxes or other fees. Some states may also issue short-term debt. Budget balancing usually requires a combination of methods, all of which involve a certain amount of discomfort.

HOW SOME STATES ARE COPING

State governments in the Northeast have dealt with their recent budget difficulties in different ways. In Massachusetts, budget deficits have all but paralyzed the state government for the past two years. The state has faced budget problems since midyear through fiscal year 1989 and in 1990 ran a deficit of approximately $661 million, the largest of any state in the nation. After relying on a temporary tax increase in 1990 to prevent this deficit from being even wider, the state legislature passed a tax-increase plan that will substantially raise state income taxes and extend the sales tax to cover, for the first time, some professional services. Nevertheless, the fiscal discord remains. Massachusetts recently elected a governor who campaigned on a platform of rolling back some of the tax increases, though a voter referendum to roll back taxes was defeated. Meanwhile, the rating agencies have given Massachusetts the lowest bond rating of any state.

In New York State, state government officials faced a large deficit in fiscal year 1990, but could reach no budget resolution until compelled by the severe downgrading of the state's bond rating to its lowest level ever. The legislature finally opted, in a budget accord seven weeks overdue, to forgo the last phase of a scheduled reduction in state personal income tax rates and to raise taxes on corporations, professional services, and various other items. Nevertheless, it is not clear that New York State officials will address some important management issues, particularly the state's extensive reliance on short-term debt and its unusually high ratio of state government employees to state residents. In New Jersey, the legislature made temporary cutbacks in spending to close a fiscal year 1990 budget gap and passed a tax increase to close an expected deficit for 1991. This plan extended the sales tax to certain exempt items and raised the general sales tax and some excise taxes. Swift passage of the bill allowed New Jersey to get by with its credit rating intact. Nevertheless, critics assert that the increases in taxes will ruin New Jersey's image as a low-tax state and discourage economic growth. After what was perceived as "anti-tax" voting in the November elections, the governor has now raised the possibility of rolling back some of the tax increases.

In Pennsylvania, state government officials were able to make some spending cuts and generate enough additional revenues to erase a fiscal year 1990 deficit; however, they severely restricted increases in spending to forestall tax


24 These changes are part of a comprehensive plan that also includes an increase in the state income tax with the revenues dedicated to funding state aid to local communities for public education.
increases in 1991. There are two reasons why Pennsylvania has so far avoided severe budget problems. First, coming out of the 1980-82 recessions more slowly than most of the other Northeastern states, it did not increase spending as rapidly. Second, its economy is not rooted in a dominant industry that experienced a boom-and-bust cycle.

CONCLUSION

Macroeconomic fluctuations make state government budgets inherently cyclical, and periods with varying degrees of budget stress are inevitable. A recent report prepared by the National Conference of State Legislatures concludes that, even in the absence of a recession, states should prepare for tight budgets.

State governments can take several steps to cope with the lean years ahead:

- Make use of sound budgeting practices, instead of spending more than they have and relying on short-term debt or accounting devices to circumvent balanced-budget requirements;
- Attempt to put money into Rainy Day Funds that provide some cushion against economic slowdowns;
- Improve their ability to forecast expenditures and revenues so that they can plan ahead and avoid serious budgetary shortfalls;
- Broaden and diversify their tax bases to minimize cyclical variability in their budgets and provide ample revenues for state spending without high tax rates. Extending the sales tax to services seems like a useful step toward this goal; and
- Invest in education, transportation, and other public infrastructure to enhance the climate for business growth and development, which will lead to a large and diversified tax base.
