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Is Iowa's Budget in a Deficit Again?

by Steven B. Garrison

Near the beginning of the year, Governor Vilsack sent the Legislature his budget recommendations for fiscal year 2002. Each year's budget, or the fiscal year, starts on July 1 of the previous year, and ends on June 30 of the current year, so fiscal year 2001 began in July 2000. About the same time in January, it became obvious that the state was not receiving the anticipated revenues that had been planned and budgeted for last year.

According to law, the state is only allowed to spend 99% of what it takes in from taxes and fees. The Revenue Estimating Conference estimates what the state will take in each year, meeting four times a year to continually update their estimates. The December meeting is generally what the Governor and Legislature use to determine the next year's budget. However, because of the shortfall in revenue collections that was obvious by early February, Republican

lawmakers decided to wait until the REC met in March and updated its previous December estimates of what the state could expect to take in from taxes and fees for this fiscal year, as well as fiscal year 2002. They felt if they did not do this, they would be basing their budget on outdated data, and they would just have to go back and redo the whole thing again when the new estimates came out. However, this delay in laying out the budget created a clamor from the Democrat leadership in the legislature, especially when the Republicans started discussing budget cutbacks for the then-current fiscal year 2001.

When the Dubuque Telegraph Herald reported on February 19, 2001 that the Legislature was looking at cuts, Senate Minority Leader Michael Gronstal, D-Council Bluffs, complained about

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The Iowa Scorecard Forecast

Item	2001 2nd Qtr	2001 3rd Qtr	Comments	Source
State Tax Revenue	\$2,422,000,000	NA	Dollars	Revenue Estimating Conference
Personal Income Tax	\$1,448,000,000	NA	Dollars	Revenue Estimating Conference
Corporate Income Tax	\$308,900,000	NA	Dollars	Revenue Estimating Conference
Personal Income	\$81,890,000,000	\$86,197,414,000	Dollars	Iowa Economic Forecast
Farm Income	\$1,050,000,000	NA	Dollars	Iowa Economic Forecast
Non-Farm Employment	1,512,560.00	1,545,836.32	Total	Iowa Economic Forecast
CPI	2.5%	3.2%	National	Blue Chip Economic Indicators

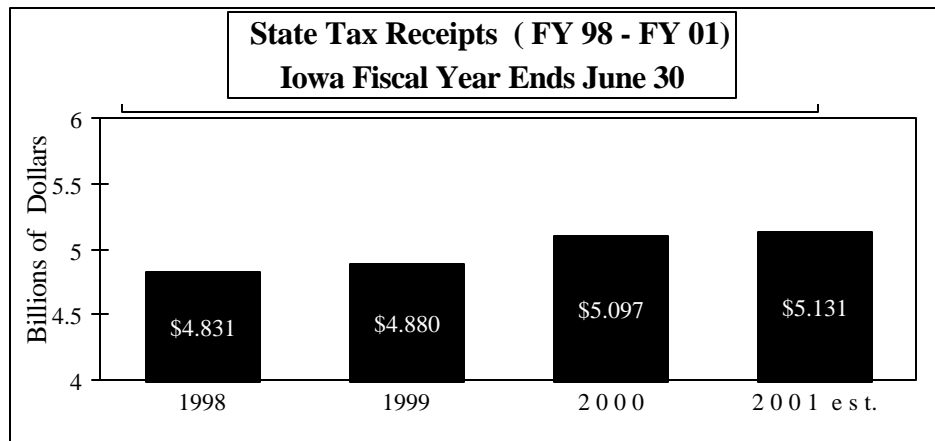
The Iowa Scorecard For Recent Quarters

Item	2000 4th Qtr	2001 1st Qtr	Comments	Source
Business Formations	1,589	1,469	Actual	Secretary of State's Office
Consumer Confidence	130.6	138.5	Midwest Region	Consumer Confidence Survey
Housing Permits	2,254	3,426	Actual	Department of Economic Development
Total Employment	1,531,467	1,517,060	Estimated	Department of Employment Services
Unemployment Rate	2.3%	3.4%	Estimated	Department of Employment Services

Figure 1.

State Tax Receipts Forecast for Fiscal Year 2001.¹

¹ Iowa Revenue Estimating Conference, March 14, 2000.



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the effort and implied it was a waste of time, saying “The governor has a whole completed budget out there, they don’t have a budget.”¹ The Senator did not comment on the potential need for budget cuts in that article, nor did he address how it would be a valuable use of time to go through the lengthy budget procedure then, in February, only to have to go back and redo the whole procedure in March when the REC was to meet, and revise its estimates downward. The Senator’s remarks were particularly disingenuous because he knows that the Legislature’s work on the budget does not even start until after the Governor submits his proposal².

In the same article, however, Governor Vilsack did comment on the growing consensus that the state was not going to have the revenues for fiscal year 2001 that it had planned on having just last winter. He claimed that last year’s surplus of \$150 million would cover any lost revenues for this year, saying “Even if not a single dime of increase came in, we

would still have enough money in the existing budget with the ending balance to cover all of our budget.” He then went on to blame the effort to lower the state’s tax burden over the last several years as the reason for the shortfall. But he continued to refuse to look at any spending cuts, saying “There’s no reason to look at budget cuts in (fiscal year) ’01.”

The Governor’s remarks on this issue were more portentous than anyone could have imagined at that time. He seemed to completely brush off any need to exercise fiscal discipline at the current time, and rejected the idea of any cuts in the current year’s spending, deciding instead to consistently urge the legislature to budget for the next fiscal year immediately, and not wait until the REC’s next meeting in March. This was particularly curious since, as pointed out in an Institute BRIEF in April³, the Governor had approved an end of the year budget cut of \$18 million the previous year with no problems, and no widespread media criticism. And by the Governor’s own admission, that fiscal year

Figure 2

Blue Chip Economic Indicators²

Published by Capitol Publications, Inc.

* Projections current as of June 2001.

Blue Chip U.S. Economic Outlook							
Indicator	1996	1997	1998	1999	2000	2001 *	2002 *
Real GDP Growth	2.8%	3.8%	3.6%	3.9%	5.1%	1.8%	3.1%
GDP Implicit Price Deflator	2.3%	2.0%	1.0%	1.4%	2.2%	2.3%	2.1%
Consumer Price Index	3.0%	2.3%	1.6%	2.2%	3.4%	3.2%	2.5%
Industrial Production Index	2.8%	5.0%	3.3%	2.8%	5.5%	-0.7%	2.9%
Non-Residential Investment	9.2%	9.9%	11.2%	9.2%	13.3%	1.7%	4.4%
3-Month T-Bill Rates	5.1%	5.1%	4.8%	4.7%	5.9%	3.9%	4.0%
10-Year Treasury Note Rates	6.4%	6.4%	5.2%	5.7%	6.1%	5.2%	5.6%
Jobless Rate	5.4%	4.9%	4.5%	4.2%	4.0%	4.6%	4.9%
Housing Starts (millions)	1.47	1.48	1.59	1.66	1.6	1.58	1.57

ended in a \$150 million surplus. Yet when facing a year with a drastic slow-down in government revenues, he flatly refused any spending cuts to forestall possible budget deficits, and to ease budget constraints for the next fiscal year.

Then, on March 14, 2001, the Revenue Estimating Conference revealed at its quarterly meeting what House and Senate Republicans had been warning about. In fact, the revenue shortfall predicted by the REC was far worse than anything anyone had previously suggested.

The REC reported two different sets of numbers. The first was an updated revenue projection for the current fiscal year of 2001. This was the number that had been debated so furiously in the first few weeks of 2001. The Republicans had insisted that this current shortfall demanded immediate action, while the Governor insisted that last year's surplus would make up for any potential shortfall. As it turned out, Governor Vilsack's assumption that the \$150 million surplus from last year would be enough to make up any revenue shortfall was wishful thinking. The REC predicted a \$165 million reduction in its revenue estimate for fiscal year 2001, which was about to end. This revenue shortfall puts Iowa at risk of having a budget deficit this fiscal year. If the Governor had approved the \$35 million cut to the budget for 2001, Iowa would not only have been able to avoid a budget deficit for this fiscal year, but would have had an extra cushion for fiscal year 2002, which did not fare any better in the REC's updated revenue estimates.

For fiscal year 2002 the REC revised its estimate from \$5,505.5 million to \$5,352.6 million, or a difference of \$152.9 million. Since the state government is required by law to use these REC estimates, this new, lower-revenue estimate meant that Governor Vilsack had to go back to the drawing board and completely redo his entire budget for 2002. It also drastically limited the funds which budget makers could use to fund state activities and agencies. These facts forced even the Governor to face the need for spending cuts.

However, the cuts the Governor proposed were far less than the actual budget shortfall as predicted by the REC. In an effort to spend more money than the law would otherwise allow, the Governor suggested the difference come out of Iowa's emergency funds. Since the law only allows the state government to spend 99% of any year's income, the extra 1% is put into two emergency funds to be used in times of natural disaster, or other unforeseen occurrences. They exist to give the state a sound financial foundation.

Governor Vilsack declared the revenue shortfall to be such an emergency, and decided those funds would be used. The debate opened

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The debate opened then on not only what actually constitutes an emergency, but when would that money be replaced? This seemed like a temporary quick fix, but not a long-term solution.

As it stands, the Legislature has given in to the Governor's demands, just as it did when it proposed budget cuts to fiscal year 2001. Millions of dollars will be "withdrawn" from the state's emergency funds, with no clear plan to replace that money. Additionally, only moderate cuts have been made in state Government spending. All this means that if Iowa's economy does not start roaring again like it did throughout the last decade, we will be revisiting this issue of deficit spending again next spring. The industrious nature of the citizens of Iowa provided the cushion the state is using to finance its voracious and insatiable appetite for spending. This same economy that gave the state government its cushion also prevented them from ever having to really test their devotion to spending within their means. This law mandating the state spend only

99% of its income was passed in 1992, which was about the beginning of Iowa's, and the nation's, economic boom.

If a state cannot curb its spending in the face of a law that makes it illegal to spend more than it takes in, and the amount of money that state is taking in drops sharply below current spending patterns, then is there anything that could really convince the state to cut spending? Or is that state going to face deficit spending forever?

ENDNOTES:

¹ Telegraph Herald; State Lawmakers Look For Ways to Trim Budget, Monday, Feb. 19, 2001

² http://www.state.ia.us/government/dom/overview_of_state_budget_process.htm

³ Institute BRIEF: Who's Playing Political Games? Vol. 8 No. 11, <http://www.limitedgovernment.org/pubs/brf/brf8-11.PDF>

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