

*Report of the  
State Budget Crisis Task Force*

# FINAL REPORT







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## *Statement from the Task Force Co-Chairs*

The State Budget Crisis Task Force was created in the aftermath of the global financial crisis to examine the increasingly perilous position of many states. In our initial report, we unambiguously concluded that, “The existing trajectory of state spending, taxation, and administrative practices cannot be sustained. The basic problem is not cyclical. It is structural. The time to act is now.”

A confluence of trends and circumstances have placed state and local governments in a position of fiscal instability and undermined the ability of their economies to compete in the global marketplace:

- State and local revenues only partially recovered since the recession that began in 2008.
- Reductions in federal spending have made state and local finances more chaotic and more difficult to manage.
- Retirement and health care expenditures continue to rise at a rate faster than state and local revenues, and many state and local governments have not addressed serious pension funding shortfalls.
- Few states have mounted new capital infrastructure investment programs that keep pace with deterioration and will keep their infrastructure modern and competitive.
- The near-total absence of serious consultation between federal and state fiscal policymakers has often obscured the long-term impact of expenditure cuts and revenue reductions.

We also studied, in detail, the financial conditions in each of six states: California, Illinois, New Jersey, New York, Texas and Virginia ([www.statebudget.org](http://www.statebudget.org)). We held discussions with partners and stakeholders to review our findings in four of those states.

Some of the most serious problems detected were:

- Cash-based budgeting, which facilitated gimmicks and obscured state fiscal condition;
- The absence of meaningful multiyear financial planning;
- Budgets and financial reports that failed to set out the future costs of financial obligations already made.

In sum, without deep-seated reform in state government fiscal affairs or federal recognition of the strains on state and local budgets, the future health of America’s communities and its economy are at great risk of further deterioration.

One concern raised throughout the Task Force’s work is that fiscal stress runs downhill, making local governments the collecting point of the greatest fiscal stress. This adversely affects the public support systems on which Americans depend — core services for which local governments are primarily responsible, such as police and fire protection, safe roads, clean water, and disaster response. The concentration of deterioration in these systems at the local level is in addition to erosion of educational quality and capital infrastructure.

This grim but realistic assessment of state and local fiscal health set the context for Phase Two of the Task Force’s work, which included National Dialogues to examine four high-priority areas, including:

- Improving the State/Federal Partnership of Medicaid
- Managing the Impact of Federal Deficit Reduction;

- Unfunded Pension Promises; and
- Increasing Transportation Funding to Benefit the Economy.

In each of these key areas, the Task Force prepared a white paper<sup>1</sup> and brought together four National Dialogues, which included individuals with expertise in different dimensions of the areas under examination. The goal was to find common ground and generate viable ideas to address the challenges in each area. Those participating included business leaders, elected officials, union officials, public policy experts, community leaders, advocates, and academics — all with a resolve to generate progress through creative and conscientious governing. These Dialogues created valuable forums that informed this final report and spurred continuing discussion among the parties.

State and local spending has been extremely important to the American economy, especially in the areas of education and infrastructure. The Task Force is not in a position to make specific proposals in programmatic priorities, expenditure levels, tax rates, or structures that could deal with budgetary problems. However, those political and policy discussions must rest on honest, reliable budget estimates and easily accessible and transparent data on financial and programmatic results in order to build trust and support for reforms. Understanding of basic, clear data is essential for solving and preventing financial problems.

***To That End, the Task Force Recommends the Following:***

**Modified Accrual Budgeting by States and Localities.** The practice of cash-based budgeting facilitates gimmicks and short-term measures that obscure actual financial conditions. Where appropriate, using consistent, modified accrual-based budgeting would facilitate comparison and avoid budgets based on inaccurate representations of future obligations or revenues.

**Multiyear Financial Plans.** States should include meaningful, forward-looking financial plans as part of their annual budget submission and adoption process as well as require local governments in their jurisdictions to do the same. A comprehensive annual budget presented by the governor and reviewed and approved by the legislature should serve as the first year of the forward-looking multiyear plan. These plans should encompass both operating and capital expenditures and should set out the basic assumptions regarding revenue and expenditures, showing clearly when future costs of promises, such as debt service and leasing balloon payments, are due. The capital plan should also indicate the source of financing to be used for projects.

**Reserve Funds.** Reserve funds, often called rainy day funds, should be required and should be adequate to meet any reasonably anticipated eventuality. It is heartening to see that many states have begun, in small steps, to replenish these funds.

**Borrowed Funds Never Treated as Revenue.** Proposed and adopted operating budgets should not be dependent on borrowed funds disguised as revenue. At times, governments must borrow to meet intrayear cash flow problems, because tax revenues are not necessarily received on the same schedule as expenditures, or to address sudden revenue shortfalls within the year. While it is recognized that, due to sudden revenue shortfalls, cash balances at times may need to be bolstered with the proceeds of short term borrowing, that borrowing should never be treated as an element of revenue and provision should be made for its repayment.

**Strengthened State Oversight of Local Financial Reporting and Communicating Prospects.** Recent developments in several states demonstrate the need for statutory mechanisms that allow states to provide strong oversight of local governments in advance of financial emergencies. Periodic reporting by local governments and timely review of financial data by state governments is essential to anticipating and dealing with the threats to public services. States should have statutory processes for imposing corrective actions on localities whose financial positions indicate a high risk of their ability to meet their obligations to the public.

**Budget Standards.** Budgeting standards should include definition of the nature of revenues, limitations on the use of nonrecurring items, multiyear planning, fair presentation of pension and other benefit liabilities, and the size and pace of funding of reserve funds. Budgets should not be on a cash basis.

**Easily Understandable Financial Reports.** Similarly, standard-setting bodies should work with associations of states to develop rules for the creation of concise, timely and readable financial reports. The convoluted, sprawling nature of state financial statements make them of limited use for all but individuals with extensive training. Both budgetary and asset-based information for all special funds should be easily accessible. Such data should be used in disclosure statements for borrowing in the same format.

**Implications for the Federal Government.** There is little evidence today that the Congress and Executive Branch consider the impact of its decisions on the other levels of government in setting policy and spending levels for the federal government. The reality is that all three levels of government serve the same people and have a responsibility to ensure that the unintended consequences of their fiscal actions do not multiply the contradictions, harm, or disruption experienced by the citizens who must adjust to the impact of all three levels of government in their lives. The federal government needs to be more cognizant of the effects its actions have on the fiscal condition of the states and localities.

**Projections of the Impact on State and Local Finances and Services of Federal Actions and Policies Should be Required.** The Task Force's analysis found that no mechanism now exists for determining, assessing, and communicating the fiscal impact of federal actions on state and local governments.

**Adequate Disclosure of Terms, Conditions, and Risks of Municipal Finances.** The current jurisdiction of the U.S. Security Commission (SEC) with respect to municipal finance issuers is narrowly limited to fraud due to the so-called "Tower Amendment," and no other body has the affirmative obligation or authority to require full transparency and disclosure of risk. The Tower Amendment should be revisited so that the SEC can require issuers to comply with sensible disclosure requirements as well as with robust accounting standards.

The recommendations above and the commentary included in this Final Report of the State Budget Crisis Task Force are the result of three years of research, analysis, and debate. The Task Force Advisory Board has endorsed these recommendations and hopes that the highly regarded participants in each of our National Dialogues will help to disseminate and promote them in their day-to-day contact with policymakers in their respective fields of advocacy and expertise.

National inattention to the financial pressure bearing down on state and local government can no longer be tolerated. What is at stake is the strength of our educational institutions, of our infrastructure and public systems, of our health care and

judicial systems, and of the safety and security of the American society. What is required is recognition of the collective responsibility of our federal and state governments for action.

It is, after all, our children and grandchildren who will pay the price of failure, and who will have to cope with the diminished strength and competitiveness of the American republic.

Sincerely,



Richard Ravitch  
Co-Chair



Paul Volcker  
Co-Chair



## Foreword

Former New York Lieutenant Governor Richard Ravitch and former Federal Reserve Board Chair Paul A. Volcker created the State Budget Crisis Task Force because of their growing concern about the long-term fiscal sustainability of the states and the persistent structural imbalance in state budgets, which was accelerated by the financial collapse of 2008.

After extensive planning and fundraising in 2010 and early 2011, Messrs. Ravitch and Volcker were joined by a board of individuals with extensive and varied careers in public service and public policy. The Task Force was officially launched in April 2011.

In addition to the co-chairs, the board of the State Budget Crisis Task Force includes these members:

<b>Nicholas F. Brady</b>	<b>Joseph A. Califano, Jr.</b>
<b>Phillip L. Clay</b>	<b>David Crane</b>
<b>Peter Goldmark</b>	<b>Richard P. Nathan</b>
<b>Alice M. Rivlin</b>	<b>Marc V. Shaw</b>
<b>George P. Shultz</b>	

A core team of experts with budget and financial planning experience at the national, state, and local levels and practical experience derived from the management of previous fiscal crises published the Report of The State Budget Crisis Task Force in July 2012. Since it was not feasible to study each of the fifty states in depth, the Task Force targeted six states — California, Illinois, New Jersey, New York, Texas, and Virginia — for in-depth, on-site analysis. In each state, the core team worked closely with experts who were deeply familiar with the substance, structure, procedures, documents, and politics of the state's budget.

The Task Force Report drew national attention to the eroding fiscal condition of states. The Report put a spotlight on several key drivers compromising states' fiscal stability:

- Medicaid Spending Growth Is Crowding Out Other Needs;
- Federal Deficit Reduction Threatens State Economies and Budgets;
- Underfunded Retirement Promises Create Risks for Future Budgets;
- Narrow, Eroding Tax Bases and Volatile Tax Revenues Undermine State Finances;
- Local Government Fiscal Stress Poses Challenges for States;
- State Budget Laws and Practices Hinder Fiscal Stability and Mask Imbalances.

To address the declining fiscal condition of states, in 2013 the Task Force hosted four National Dialogues focusing on the most urgent areas of concern, including: Infrastructure, Underfunded Retirement Promises, Medicaid, and Managing the Impact of Federal Deficit Reduction. During each daylong Dialogue, the Task Force gathered experts to discuss options for new organizational structures, consultative processes, or legislative mechanisms that can promote a cooperative approach between the federal and state governments to solving these challenges. The input of participants of each National Dialogue informed the Task Force recommendations outlined in this final report.

The names of the full project team can be found on the Acknowledgments page at the end of this report.

## Introduction

In the July 2012 Report of State Budget Crisis the Task Force (Task Force Report), Task Force Co-Chairs Paul Volcker and Richard Ravitch said:

*The conclusion of the Task Force is unambiguous. The existing trajectory of state spending, taxation and administrative practice cannot be sustained. The basic problem is not cyclical. It is structural.*

The Task Force is compelled to reiterate this conclusion. The costs of inaction are high. The ability of state and local governments to meet their obligations to public employees, to creditors, and, most critically, to the education and well-being of the public is deteriorating. Particular harm could come to the most vulnerable populations as federal cuts are compounded by state and local reductions. And the damage is compounded by the fact that the federal government does not structure its own fiscal and programmatic actions to complement the objectives of state and local government. When resources are scarce, the penalties of acting without consultation and cooperation increase harshly.

In July 2012, the nation was in the midst of a nascent but halting recovery from the global financial crisis that began in 2008. Currently, government revenues continue to improve modestly in most states, sometimes enhanced by revenue initiatives or buttressed by efforts to contain expenses. These endeavors have allowed some rainy day funds to be replenished, as recommended in the Task Force Report. But the misguided and widely held belief that states can rapidly grow out of their financial problems through natural revenue growth persists as a rationale for the lack of corrective and necessary action. In many states, structural reforms have not been proposed, let alone implemented. Rising pension and postemployment benefit costs continue to threaten states, as does the uncertainty of Medicaid funding and federal spending. The fiscal course of many states and their local governments remains unsustainable.

A theme of the Task Force Report and the individual State Reports is that fiscal stress runs downhill and that local governments are the collecting point. This adversely affects the delivery of public services and makes investment most difficult at the point where it is needed most. The 2013 Chapter 9 bankruptcy filing of Detroit, and like filings in California and elsewhere, suggests that some states and localities are overextended in terms of retirement promises and other commitments. Few states or localities have undertaken rigorous analyses of their liabilities and proposed thoughtful multiyear plans to address them. In most states there has been a studied ambiguity about long-term costs and obligations about which unions, the municipal bond industry, and politicians have been relatively passive.

Since the July 2012 Task Force Report and the issuance of six State Reports,<sup>2</sup> the Task Force has focused on five subject areas:

- Accountability and Transparency in Budgeting and Financial Reporting;
- Underfunded Retirement Promises;
- Transportation Investment;
- The State/Federal Medicaid Partnership; and
- The Impact of Federal Deficit Reduction.

The Task Force convened four National Dialogues on the topics above. These Dialogues created valuable forums that informed this final report and spurred continuing discussion among the participating parties.<sup>3</sup> This report summarizes the

white papers prepared for, and the insights drawn from, the National Dialogues. Where appropriate, recommendations are made.

## Findings

The objective of the Task Force is to inform the public of the character and gravity of the fiscal issues confronting the states and the consequences of deferring corrective actions. This Final Report of the State Budget Crisis Task Force culminates three years of research, analysis, and debate. The Task Force encourages governments at all levels to consider its process recommendations and implement policies and programs that will lead to long-term structural adjustments. A summary of the findings is presented below.

### **Obligations Are Rising Faster Than States' Ability to Meet Them**

The Rockefeller Institute April 2013 *State Revenue Report* states:

*Total state tax collections are growing but remain below prerecession peak on a real-dollar, per capita basis, i.e. after adjusting for inflation and population growth. According to data collected by the Rockefeller Institute and the U.S. Census Bureau, overall state tax revenues increased by 8.6 percent from the first quarter of 2012 to the first quarter of 2013. Personal income and sales tax revenues particularly are improving, with personal income tax collections increasing by 18.4 percent, and sales tax collections rising by 5.5 percent in the period. However, the rapid income tax growth in the first quarter of 2013 and in the 2012 fourth quarter reflects actions taken by taxpayers to minimize their expected 2012 federal tax liability in light of the federal tax increases associated with the 2013 "fiscal cliff."*

*Some states, such as California, have taken serious steps to address their revenue shortfalls and begun to see promising results. But most states are on a revenue roller coaster, and it will be a bumpy ride for them and even bumpier for their localities. It will be hard for states to interpret revenue data in coming months, and hard to rule out the possibility that any short-run revenue surge is at least in part borrowed from the future. It will be tempting to treat unexpected revenue growth as a sign of continuing economic improvement, when it could mean instead that future revenue will be lower. Caution should be the watchword.<sup>4</sup>*

### **The Rising Costs of Unfunded Pensions Continue to Pressure State Budgets and Balance Sheets**

Since 2008, forty-three states have enacted pension reforms, are attempting reforms, or are contemplating them. Most reforms have been in respect to new hires and have had minimal effect on unfunded liabilities.<sup>5</sup> In many states there has been strong political resistance to reform. Pennsylvania, for example, has not been able to achieve legislative change and faces severe pension underfunding consequences. Illinois' reforms may be too little, too late. The costs of pensions and other postemployment benefits generally are growing faster than revenues and continue to crowd out other necessary budget items. Health care, education, and infrastructure funding are victimized, as is aid to the vulnerable. In 2012, state funding for pre-K programs experienced its largest one year drop ever, to well below the inflation adjusted average of 2002; the nation's youngest learners are bearing a disproportionate share of budget cuts.

### **The Effect on the States of Federal Deficit Reduction Is Unknown and Often Unconsidered**

Federal deficit reduction presents new difficulties for the states. States already have felt the impact of sequestration. More than \$5 billion of cuts in 2013 due to sequestration have been levied against states. Discretionary programs were hardest hit, while some mandatory programs like Medicaid were largely exempt. Cuts to Supplemental Nutrition Assistance

programs, Low Income Heating Assistance, Special Education, Headstart, Meals on Wheels, Public Health funding through the Mental Health Block Grant Program, and U.S. Environmental Protection Agency (EPA) grants all directly impact states.

As Congress considers new spending plans, it is unclear if sequestration will continue or be replaced by new cuts. States cannot anticipate budgetary relief from the federal government and are hoping that Congress will not impose increased federal cuts, further impacting crucial services. There is little consideration of the impact on states by the federal government as it creates its own fiscal plans in a very contentious environment.

### ***Infrastructure Funding Remains Inadequate***

In transportation infrastructure, there is great uncertainty about federal funding of water resources, highways, and aviation trust funds, which face continuing shortfalls. Several states are trying to raise state revenues to meet transportation infrastructure needs, which are staggering and difficult to measure. According to the ongoing accounting of organizations and institutions that attempt to quantify spending needs, America is investing inadequately in our public infrastructure. A recent Center for American Progress report on America's infrastructure funding gap estimated that the federal government is underinvesting in infrastructure by approximately \$48 billion per year, assuming a goal of adequately maintaining existing infrastructure and preparing for projected economic and population growth.<sup>6</sup> There are hundreds of thousands of highway miles and tens of thousands of bridges across America that have been classified as deficient, and continue to deteriorate in spite of evidence that the problem increases dramatically as critical investment is delayed.

### ***The Affordable Care Act's Impact is Uncertain***

States are trying to determine the impact of the Affordable Care Act and whether to participate in its Medicaid expansionary provisions. As of October 2013, according to the Kaiser Family Foundation, twenty-two states have opted out of the Act's Medicaid expansion. The Act remains under assault by Republicans and its clumsy initial implementation has created new skepticism.

The certainty of rising retirement costs, coupled with the uncertainty associated with revenue trends, federal budget actions, transportation funding and the implementation of the Affordable Care Act, all make the creation of truly balanced state budgets a difficult task. As the Task Force Report emphasized, forty-nine states have a balanced budget requirement either by constitution or statute, but they do not define revenue — and thus many states use the proceeds of borrowing and asset sales as revenues for budgeting purposes, particularly in challenging times. This is a practice that accomplishes little in the short term and offers only increased pain and havoc in the long run.

## *Focus Areas*

### **Accountability and Transparency in Budgeting and Financial Reporting**

Public trust in government is at or near all-time lows. According to the Pew Research Center, 43 percent of the public distrusts their state government. Honest, reliable budget estimates and clear, accessible data on financial and programmatic results might increase trust, which is necessary to build support for structural reforms. Equally significant, clear data are essential for solving and preventing financial problems.

The financial crisis, which began in 2008, and the attention it spawned, did not create the structural budget problems of state and local governments. Rather, it revealed them. This suggests that had government, the media, taxpayers, and the electorate been aware of the poor fiscal condition of state governments and the underlying trends and causes of those conditions, they may have been able to implement preventive and ameliorative steps.

At their heart, the economic events beginning in 2008 generated a severe revenue crisis. Lack of transparency and accountability constitutes bad financial, government, and political practice. Self-deception, either deliberate or unwitting, causes inaction and ignorance. Thus, not only is transparency in budgetary and fiscal reporting desirable, the absence of it can be a major cause of government fiscal problems.

Two specifics illustrate how the lack of transparency can contribute to fiscal problems:

In respect of pensions, actuaries have calculated a government's annual required contribution to the government's pension funds. Usually, these calculations are not made public contemporaneous with the calculation. They should be. Otherwise, it is too easy for the Executive and the legislature to ignore the calculation and underfund the pension systems.

Audited financial statements of governments generally are slow to be prepared, overly complex, and are published too late to be as meaningful as they could be. Governments should establish statutory provisions that require the timely publication of clear, readable, audited financial statements so that fiscal decisionmaking can be better informed.

### **Accountability and Transparency Recommendations**

#### ***The Task Force Recommends the Following:***

**Modified Accrual Budgeting by States and Localities.** The practice of cash-based budgeting facilitates gimmicks and short-term measures that obscure actual financial conditions. Where appropriate, using consistent, modified accrual-based budgeting would facilitate comparison and avoid budgets based on inaccurate representations of future obligations or revenues.

**Multiyear Financial Plans.** States should include meaningful, forward-looking financial plans as part of their annual budget submission and adoption process and require local governments in their jurisdictions to do the same. A comprehensive annual budget presented by the governor and reviewed and approved by the legislature should serve as the first year of the forward-looking multiyear plan. These plans should encompass both operating and capital expenditures and should set out

the basic assumptions regarding revenue and expenditures, showing clearly when future costs of promises, such as debt service and leasing balloon payments, are due. The capital plan should also indicate the source of financing to be used for projects.

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**Strengthened State Oversight of Local Financial Reporting and Communicating Prospects.** Recent developments in several states demonstrate the need for statutory mechanisms that allow states to provide strong oversight of local governments in advance of financial emergencies. Periodic reporting by local governments and timely review of financial data by state governments is essential to anticipating and dealing with the threats to public services. States should have statutory processes for imposing corrective actions on localities whose financial positions indicate a high risk of their ability to meet their obligations to the public.

**Budget Standards.** Budgeting standards should be developed to include definition of the nature of revenues, limitations on the use of nonrecurring items, multiyear planning, fair presentation of pension and other benefit liabilities, and the size and pace of funding of reserve funds. When feasible, budget presentations should be on the basis of accrual rather than cash accounting. Budgets should not be on a cash basis.

**Easily Understandable Financial Reports.** Similarly, standard-setting bodies should work with associations of states to develop rules for the creation of concise, timely, and readable financial reports. The convoluted, sprawling nature of state financial statements make them of limited use for all but individuals with extensive training. Both budgetary and asset-based information for all special funds should be easily accessible. Such data should be used in disclosure statements for borrowing in the same format.

**Implications for the Federal Government.** There is little evidence today that the Congress and Executive Branch consider the impact of its decisions on the other levels of government in setting policy and spending levels for the federal government. The reality is that all three levels of government serve the same people and have a responsibility to ensure that the unintended consequences of their fiscal actions do not multiply the contradictions, harm, or disruption experienced by the citizens who must adjust to the impact of all three levels of government in their lives. The federal government needs to be more cognizant of the effects its actions have on the fiscal condition of the states and localities.

**Projections of the Impact on State and Local Finances and Services of Federal Actions and Policies Should be Required.** The Task Force's analysis found that no mechanism now exists for determining, assessing, and communicating the fiscal impact of federal actions on state and local governments.

**Adequate Disclosure of Terms, Conditions, and Risks of Municipal Finances.** The SEC’s current jurisdiction with respect to municipal finance issuers is narrowly limited to fraud due to the so-called “Tower Amendment,” and no other body has the affirmative obligation or authority to require full transparency and disclosure of risk. The Tower Amendment should be revisited to see if the SEC should be given the same jurisdiction over the issuance of municipal securities as it has over issuance of corporate securities.

## Managing the Impact of Federal Deficit Reduction

The Task Force Report states:

*There are no standing structures and procedures within the federal government for analyzing the impacts on states and localities of reduced federal spending or federal tax changes, and there is little dialogue about these issues between the federal government and state and local governments.*

In fact, there can be an alarming disconnect between federal and state policymakers. Highly reported recommendations from the Simpson-Bowles Commission on the Federal Budget Deficit and the proposed budget prepared by the House Budget Committee Chair Paul Ryan illustrate the disconnect. Both the Commission and Mr. Ryan proposed raising the Medicare eligibility age to 67. Since most state and local governments provide family medical benefits to their eligible retirees and employees until they age qualify for Medicare, the impact on the states of an increase to age sixty-seven would be very costly. There is no apparent evidence that the Commission or the Congress considered this consequence.

Members of the Task Force believe that there should be a centralized entity within the federal government charged to measure and report publicly on the impact of federal initiatives on state and local governments. There should be adherence to the principle that the Executive and Legislative branches of the federal government should be responsible for all of the consequences of what they do, not just for the consequences that they intend.

The Task Force White Paper on Managing the Impact of Federal Deficit Reduction explores this phenomenon:

- While there is no agreement on the elements of federal fiscal reform, whatever actions are taken — lower expenditures, increased revenues, or both — will have a significant impact on states. However, there has been little serious analysis of potential impacts and little dialogue between the states and the federal government about the nature of what could occur. An equally troubling reality is that there is no organized mechanism to have continuing discussions on these and other critical issues concerning both the federal and state governments.
- Over the past two years, Task Force members who have discussed with members of Congress and their staffs the impact of federal legislation on states, particularly budget items and tax changes, report that very few seem focused on it.

## Recommendations on Managing the Impact of Federal Deficit Reduction

### *The Task Force Recommends the Following:*

- **Create a centralized, independent mechanism for improved reporting and analysis of state financial data.** This mechanism could be housed in a federal department or agency or with the Congressional Budget Office and would have comprehensive responsibility for data collection and analysis.



- **Encourage development of mechanisms for better coordination between state and federal governments.** A Presidential Executive Order should be issued that would require cabinet agencies to coordinate with state and local governments when taking major actions that would affect them. Information about these actions should also be shared with Congress to inform them about the impact of potential decisions.
- **In cooperation with the states, the federal government should engage in a major review of policies affecting state governments.** Two of the proposals that could be considered are: (1) a “sorting” process similar to one undertaken during the Reagan administration that would identify major federal programs and analyze where their functions would be performed best and (2) joint development of an analytic model that would facilitate broad assessment of the impact of various tax reform proposals.

## Underfunded Retirement Promises

In many state and local governments a significant cause of fiscal distress is the increase in pension contributions that must be made to support past promises to pay for work performed by employees in previous years. These payments have the increasing effect of crowding out needed current services within existing revenue structures.

The Task Force commissioned a staff white paper on Underfunded Retirement Promises and held a National Dialogue on Underfunded Retirement Promises on April 19, 2013, at the New York Federal Reserve Bank. Excerpts from the white paper include:

- State and local government retirement systems cover more than nineteen million workers (about a sixth of the U.S. workforce) and more than eight million beneficiaries. About a quarter of state and local government workers are not covered by Social Security, and many workers, beneficiaries, and their families rely primarily on their public pensions for retirement security. Retirement benefits have played an important role in attracting and retaining workers for the crucial services that state and local governments deliver.
- Pension contributions for most governments have been rising and many state and local government retirement systems are underfunded, some severely. A few are nearing the point at which their ability to pay benefits will be threatened without dramatic increases in contributions. Underfunding creates risks to the retirement security of current and former state and local government workers and risks to people, businesses, and others who benefit from and pay for public services. Efforts to fund retirement benefits crowd out funding for essential services and impose risks to taxpayers and fee-payers that finance those services. These groups are the principal stakeholders in any discussion of the problems caused by pension underfunding.
- Governments have been making widespread changes in response to rising pension contributions. Some changes affect both current workers and retirees through changes in contributions, age of retirement, and benefits. Other changes affect stakeholders in governments more generally through cuts in services, increases in taxes, and fiscal legerdemain designed to postpone service cuts or tax increases by proverbially kicking the can down the road.
- Changes should be made in the context of honoring promises made to public sector employees and retirees, preserving public services, and creating reasonable burdens on taxpayers and feepayers. We expect all stakeholders share these principles and goals despite sharp disagreements about the appropriate distribution of the burden.

### ***Underfunded Pension Liabilities***

Actuaries develop estimates of benefits likely to be paid in the future based upon interpretations of legal documents describing pension plans, expectations for how those plans will be implemented in the future, and assumptions about future service, future earnings, mortality, and other factors. Although workers, retirees, and governments may expect these benefits to be paid, not all benefits are promised formally or are immune from legal change. Actuaries estimate the present value of these expected future benefits using a chosen discount rate; the portion attributed to past service is called an actuarial accrued liability, although it is based on expected benefits rather than a full assessment of whether those benefits are required by law to be paid. The portion of liability not covered by actuarial assets is referred to as the unfunded actuarial accrued liability.

Economists and financial analysts generally discount future payments using rates that reflect the risk associated with the promised payments, relative to the broader market. Since most public pension benefits have strong legal protections, the appropriate discount rates should be comparable to other low risk assets. Of course those legal protections are in jeopardy in any jurisdictions that can use the federal bankruptcy code, which will preempt any local or state protections. Such rates are generally much lower than those chosen in actuarial valuations, which currently average about 7.75 percent. When states use higher discount rates, they are able to make lower and often inadequate contributions, ultimately resulting in higher unfunded liabilities. For the nation as a whole, state and local pension systems had self-reported levels of approximately 76 percent funded on an actuarial basis at the end of their 2011 fiscal years, leaving them actuarially underfunded by approximately \$1 trillion.

Retirement systems vary greatly in their estimated underfunding. There are no regularly reported estimates of underfunding based upon lower-risk discount rates, so we must compare using actuarial estimates based on assumed rates of return. Of the 126 major plans in the Public Fund Survey maintained by the National Association of State Retirement Administrators, twenty had actuarial funded ratios of approximately 90 percent or higher at the end of the 2011 fiscal year. These included two of the largest retirement systems in the nation: the New York State and Local Employee Retirement System and the New York State Teachers Retirement System. Seventeen plans had actuarial funding ratios below 60 percent. If estimates of funded ratios based on low-risk discount rates were available, the funded status of virtually every plan would look notably worse.

The most significant cause of actuarial underfunding for the nation in recent years (as opposed to specific distressed pension plans) is shortfalls in investment income relative to assumed investment returns, although there have been extended periods in which actual returns exceeded assumed returns. In 2000, pension funds in aggregate were approximately fully funded on an actuarial basis (using discount rates based upon earnings assumptions). If funding levels had been estimated using lower-risk discount rates, they would have been estimated to be underfunded, although the difference between assumed returns and low-risk yields was much smaller in 2000 than it is now. Using earnings assumptions to value liabilities can make systems appear better funded than they are, making it easier for governments to avoid hard choices needed to shore up funding and potentially encourage changes to benefits or contributions in ways that would reduce future funding levels.

Another cause of underfunding has been retroactive benefit increases. The most significant example of this is California. Underfunding can be worse when the dynamics of new rules are not totally understood and can lead to worker actions that expand the values of pensions with expanded base salary through overtime.

### ***Pensions Enjoy Significant Legal Protection***

The most important legal consideration for states pursuing pension legislative changes is whether there is a binding, legally enforceable contract between the employer and the employee that vests rights either at the time of hire, at a point during the employee's tenure, or at retirement. If a contract exists, it enjoys a measure of protection by virtue of Article One, Section 10, of the U.S. Constitution, which provides, in part, that no state may pass any law that diminishes or impairs a contract. The breadth of this U.S. constitutional protection depends on the terms of the contract and the materiality and circumstances of the legislatively enacted modifications.

Forty-two states adhere to the theory that a pension contract is created by virtue of public service employment. These states regard pensions as deferred compensation. A contract may be declared in the underlying legislation, prescribed by explicit state constitutional language, or found or implied and so determined by the state courts. Whenever a state constitution explicitly prescribes that a contract exists, the state constitution or state law usually also provides that the benefits of the contract cannot be diminished or impaired.

If a pension contract is deemed to exist, the most important questions to be asked in assessing the amount of constitutional protection available to that pension contract are: When was the contract created? And, what are its terms? Subsequently important questions are: What is the core promise of the contract? And, is there clear, unambiguous legislative intent to establish a contract, to bind future legislatures to the contract's terms, and, thereby, relinquish the sovereignty of the state to make future changes?

Pensions have enjoyed significant protection under constitutions and statutory frameworks in many states. This protection is being challenged as state and federal courts consider the relationship of pension payments to other obligations such as bond payments. In Detroit, for example, the court determined that federal bankruptcy laws can be used to preempt the Michigan Constitution. While states cannot file under the bankruptcy laws, the practical issues of crowding out will likely lead to addressing the nature of legal protection of pensions.

### ***Which Reforms Would Have the Greatest Impact?***

Governments can change pension benefits for new hires without legal restrictions, although they may raise concerns about attractiveness as employers and about retirement security. It has been common for governments to add new tiers with reduced benefits for new workers. It is important to note that such changes have absolutely no impact on unfunded liabilities, but can slow growth in future liabilities and very gradually affect contributions required by governments.

Governments are reluctant to reduce benefits for retirees, as this involves reducing incomes at a point in people's lives where they have a limited ability to recover. Retiree benefits also typically have relatively strong legal protections. Some courts have allowed changes to cost of living adjustments (COLAs), but several state courts have found COLA's are entitled to the same level of protection as base benefits.

The in-between area is nonaccrued benefits for current workers, where there is a distinction between benefits previously earned and benefits yet to be earned attributable to future service. There have been relatively few efforts to reduce benefits previously earned. Earned benefits have strong legal protections and the holders of them have little incentive to negotiate in respect of them.

### **Observations from the Pension Dialogue**

Participants in the National Dialogue on Underfunded Retirement Promises included elected officials, actuaries, academics, and union and business leaders. Although unanimity was nonexistent and there was contention, every participant agreed that Defined Benefit Plans should be preserved; that the obligation to retain benefit promises made to retirees and current vested employees enrolled in defined benefit plans was an overarching goal. One participant observed:

*There should be no moral distinction between a commitment to pay interest to someone who lends you money than a commitment to pay someone who works for you. [Nineteen] million people work for state and local governments; it's crazy that we wouldn't want to find a way to fix this problem so we can continue to attract the best people to government service.*

Discussion also centered on the need to create and incentivize forums so that stakeholders (unions, management, bondholders, and others in distressed cities) could participate in a collaborative process that would begin well before anything resembling the failure of collaboration that is municipal bankruptcy.

### **Continuing Pension Analysis**

The Task Force generally endorses the analyses and suggestions contained in *Strengthening the Security of Public Sector Defined Benefit Plans*, published by the Rockefeller Institute and authored by former Task Force staff members Don Boyd and Peter Kiernan (forthcoming.) Mr. Boyd and Mr. Kiernan also authored the Task Force's Pension White Paper.

## **Increasing Transportation Investment to Benefit the Economy**

The condition of our transportation infrastructure has been characterized by near failing grades from many sources, including the American Society of Civil Engineers (ASCE).<sup>7</sup> In its 2013 Report Card, the ASCE gave the condition of the nation's infrastructure a grade of D+ saying, "While the modest progress is encouraging, it is clear that we have a significant backlog of overdue maintenance across our infrastructure systems, a pressing need for modernization, and an immense opportunity to create reliable, long-term funding sources to avoid wiping out our recent gains."

In the Task Force Report, the general focus was on infrastructure spending and the pressure that was being put on available funds from potential federal cutbacks and from competing needs at the state level. To provide context for infrastructure spending, the Task Force stated:

*States and their localities finance nearly three-quarters of all public infrastructures — schools, highways and transit systems, drinking water, and other projects crucial to economic growth and public health and safety.*

The carrot of federal money, particularly in transportation, can drive infrastructure investment. More than \$90 billion flows annually from the federal government to states for infrastructure. As projected by the Congressional Budget Office (CBO) this will decrease by more than 35 percent in the period from 2012 to 2022 as a result of the need to decrease overall federal spending as part of efforts to reduce the federal deficit.

It is reasonable to assume that there will be new restraints on federal government spending, pressure to cut grants-in-aid to states, cuts in federal procurement, and uncertainty about federal tax changes that might modify the tax-free characteristic

of municipal bonds used to finance infrastructure. Such developments would hit the Task Force Study states (i.e., New York, Illinois, California, Texas, Virginia, and New Jersey) particularly hard. These six states are among the top recipients of federal aid. In addition, their businesses and economies have strong links to the federal government. In 2010, Virginia, California, and Texas ranked first, second, and third, with New York ninth, in receipts from federal procurement spending. Finally, according to the CBO, four of the study states benefit more from the tax-free income of municipal bonds than the nation as a whole.

Below are observations from the Task Force staff White Paper on Increasing Transportation Investment to Benefit the Economy:

- Historically, the federal government and states have shared the primary funding responsibility for roads, highways, bridges, and transit. However, fiscal pressures at both the state and federal level are putting stress on this partnership, and increasingly putting maintenance and new project implementation in peril. At the federal level, funding infrastructure through available cash flow is expected to decline. There is major political resistance to fees and levies. The lack of federal funding is a severe impediment to maintenance and progress. A new, dedicated revenue source should be established nationally and states need to increase their respective infrastructure efforts. To do so, they will have to dedicate less of their recurring revenues to retirement costs and Medicaid.
- The importance of the transportation system as a whole is widely understood by both the public and private sectors. The interconnected partnership among the modes to move goods from ports or airports to rail or roads is the primary ingredient for just-in-time delivery and the movement of bulk cargo. While the importance of an interconnected system to commerce and state economies is clearly substantial, the benefits have been difficult to quantify.
- Given current funding projections, the American Society of Civil Engineers (ASCE) estimates that from 2013 through 2020, the national economy will feel a negative impact of almost \$900 billion in lost GDP due to deteriorating surface transportation infrastructure conditions. When this time period is extended to 2040, the impact increases to approximately \$3.1 trillion. ASCE estimates that \$94 billion per year is needed in additional funding for surface transportation. Additionally, airports face a funding gap of \$39 billion through 2020, and \$95 billion through 2040. Critical to commerce, the nation's ports and inland waterways are estimated to have a funding gap of \$16 billion by 2020, which will grow to \$46 billion by 2040.

Federal funding for surface transportation was most recently reauthorized for two fiscal years by legislation named Moving Ahead for Progress in the 21<sup>st</sup> Century (MAP-21). This leaves a funding gap for surface transportation of more than \$3.6 trillion through 2040.

Funding for all aspects of aviation has been declining since 2009 when appropriated levels were over \$17 billion. In 2012, authorization of the use of Federal Aviation Administration (FAA) revenues was several years in the making. A timely, fundamental review of aviation finances by Congress is unlikely.

Reauthorization of the Water Resources Development Act of 1986 is before the Congress with final action projected for 2014. The macro question across all of the modes is, "How should responsibility be divided between states, the federal government, and the private sector for decision making and funding across the modes?"

With extremely limited resources, maximizing the effectiveness of transportation projects is important. The American people require confidence that their money is being well spent in order to establish public support for new funding. Historically, the use of earmarks and other funding devices produced too many projects that could be characterized as “bridges to nowhere.” These projects sometimes benefit limited constituencies, and are often very expensive for the benefits that they provide, further eroding public trust.

Even when projects have broad benefits that are easily recognizable, they require a significant investment. The CBO notes, “The ratio of benefits to costs for economically justifiable projects varies widely from project to project.... Carefully ranking and funding projects so that only those with the highest net benefits are implemented could yield a large share of the total possible benefits at a fraction of the cost.” Benefits and costs are difficult to measure, but estimating and evaluating them is an important element of selecting sound projects.

The need to assure the timely implementation of these projects is vital. As noted by Former Under Secretary of Transportation Roy Kenitz:

*The amount of time it takes many infrastructure projects to move from initial idea to final construction frustrates everyone from the policymakers to the public. Eight to ten years of total elapsed time or more is not uncommon for large, complex projects. Many benefits would undoubtedly flow from reducing this time; accomplishing this requires us first to understand why the process takes so long today.*

### **Observations from the National Dialogue on Transportation Infrastructure**

The National Dialogue on Transportation Infrastructure was presented in partnership with the AFL-CIO and the U.S. Chamber of Commerce. Participants agreed that retirement and health care expenses are growing at a rate dramatically faster than revenues and, in addition to education funding, the biggest victim of that growth is maintenance and modernization of our nation’s infrastructure.

The magnitude of the infrastructure cost is enormous and growing. There is an inexhaustible demand for infrastructure funding. The group considered options for adequate revenue to tackle the seemingly endless list of necessary projects.

Task Force Co-Chair Paul Volcker suggested that progress would continue at an abysmal rate if no clear vision is outlined:

*This is about community investment, and creating a vision for how those communities collectively operate in a safe and efficient manner. Without a clear vision for investing in infrastructure, including a dedicated revenue source, we cannot compete.*

Finally, the Dialogue focused on project selection and implementation. The unreasonably long gestation period for infrastructure projects, combined with the difficulty in proving how deteriorated an infrastructure is before safety becomes the propellant for action, commands serious attention.

Former Pennsylvania Governor Ed Rendell noted the largest impediment to progress is the electorate’s general aversion to raising revenue. The governor observed:

*The answer to generating political will is just do it. When I was governor, we passed the second biggest tax increase in Pennsylvania history. People hated the notion that taxes were being raised, but then they went*

*about their business and they saw things changing, and their anger dissipated. They saw the economy booming. Erie Canal, transatlantic railroad, and interstate highway: all came about thanks to Presidential leadership. We need presidential leadership. The [slow] rate at which projects are completed is causing us to fall rapidly behind. The main question is “How can we convince Congress to keep us from falling behind at a rapidly declining rate?”*

Like education, the state of infrastructure in the United States impacts our ability to compete abroad. The quality of our infrastructure is associated with our competitiveness.

### **Summary on Infrastructure**

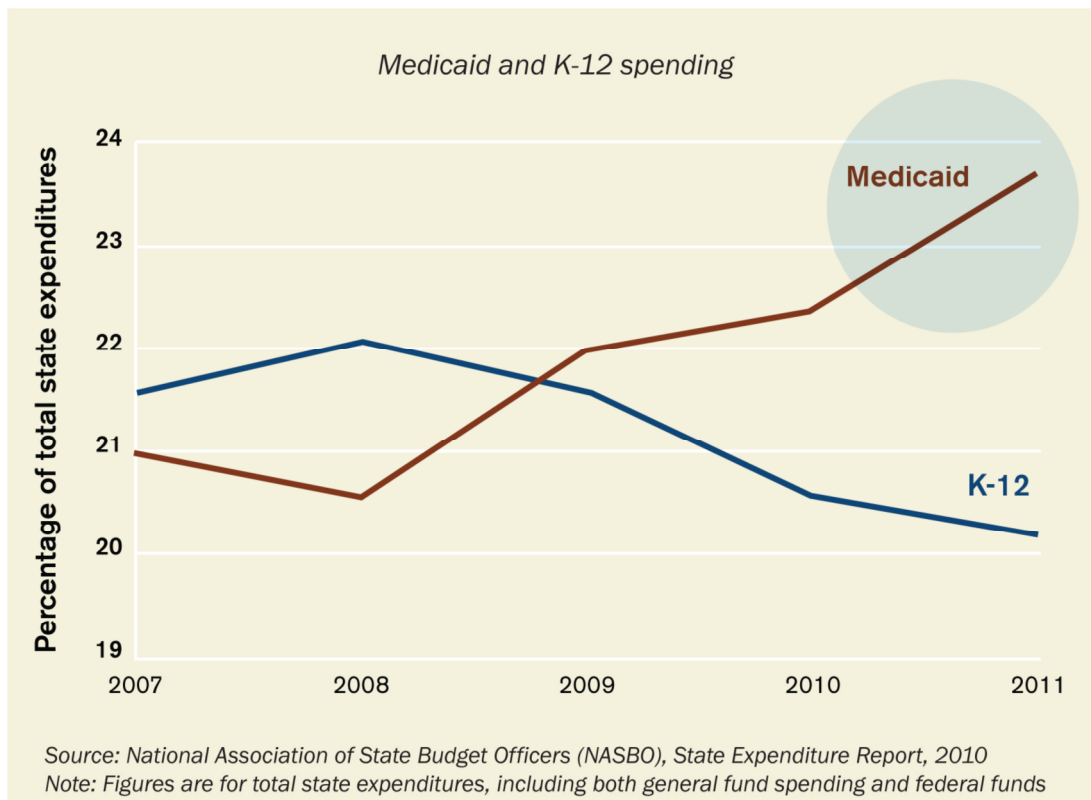
The members of the Task Force agreed that it would not be appropriate to offer recommendations in respect to the specific levels of required transportation investment funding. The need for additional transportation investment at all levels of government is overwhelming, making enormous demands on government revenues and the ability of government to finance and, thus, impose burdens on subsequent generations to pay for projects from which they may and should benefit, but may have no role in choosing. The vast demand for transportation infrastructure requires the setting of priorities and selections of patterns of economic development. These are difficult political and substantive choices that necessarily must be made by elected and appointed officials in a democratically accountable manner that is reflective of our values and politics.

Accordingly, the Task Force determined to confine itself to make recommendations only with respect to matters of process, administration, and governance such as budget transparency, budget making, financial reporting, the metrics of pension funding, and federal-state relations.

### **Improving the State/Federal Partnership of Medicaid**

Below are observations from the Task Force White Paper on Improving State/Federal Partnership of Medicaid.

*Medicaid recently surpassed K-12 education as the largest area of state spending when all funds, including federal funds, are considered.*



- In 2011, combined federal and state Medicaid spending topped \$432 billion, with significant implications for both federal and state budgets. The Congressional Budget Office baseline projections for federal Medicaid spending show a rise from \$258 billion in 2012 to \$622 billion in 2022. The federal expenditure trend is driven in large measure by the Affordable Care Act’s provision that funds the program’s expansion to more low-income adults. Except for the so-called “woodwork” effect that some states (e.g., California) think will create a rise in state Medicaid funding, the state expenditure trend line will rise more slowly since state Medicaid programs are expected to shoulder a small fraction of the cost of the expanded access to health care.
- Although state and federal governments share the financial obligation for Medicaid, this intergovernmental partnership is under pressure as fiscal difficulties at all levels of government make it harder for states to afford to cover their costs of the program. There are two ways of measuring Medicaid as a share of a state’s spending. The first treats Medicaid spending as a proportion of the “unified state budget” (e.g., all federal and state spending combined), and the second looks at expenditures as a share of state revenues only. The State Budget Crisis Task Force found that total Medicaid expenditures now account for the largest single expenditure in unified state budgets, surpassing spending for public education, infrastructure, and other state safety net obligations.
- When looking at spending supported with state revenues across all states, Medicaid accounted for \$132 billion in state spending in 2012. It accounted for approximately 16 percent of state general expenditures. On this basis, Medicaid spending ranks second behind state spending on education.



- Medicaid is not immune from system-wide health care cost pressures. Both health care costs and utilization have increased significantly over the last three decades due to the use of expensive and lifesaving technology and improved life expectancy. In spite of these system-wide cost pressures, Medicaid has been able to contain per-enrollee health care cost increases more effectively than either private market insurance or Medicare.
- Medicaid must absorb the financial burden of overall health care cost increases as well as rising enrollment due to the increasing share of Americans who are low-income and must turn to the program for health care, long-term care, or both. In spite of these pressures to drive up program costs, an improving economy, strenuous state cost containment efforts, and the expiration of enhanced federal Medicaid funding under the American Recovery and Reinvestment Act have resulted in slower-than-projected program cost growth. Total cost growth dropped from 9.7 percent in 2011 to 2 percent in 2012.
- According to the Kaiser Commission on Medicaid and the Uninsured, enrollment growth in Medicaid slowed to 3.2 percent in 2012, down from 4.4 percent in 2011 and 7.2 percent in 2010. Although enrollment growth brings rising costs, the fact that the program is responsive to changes in the private economy and thus offers countercyclical support to working families is an especially useful attribute of the Medicaid program. Without Medicaid, these families would have been largely uninsured and the cost of treating their illnesses could have fallen on other participants in the health care system, including hospitals and providers. Ultimately those costs would be passed on as increased insurance premiums charged by commercial payers.
- Against this backdrop of Medicaid cost growth, the Medicaid expansion provisions of the Affordable Care Act, which are estimated to enable more than 21 million adults to become insured, are being debated at the state level. The federal government will pay 100 percent of the cost of covering the newly eligible enrollees beginning in 2014, phasing down to 90 percent in 2019. As of May 6, 2013, twenty-six states have opted for the expansion, and three states are still considering if they will expand their programs or not. While states will face some new costs associated with the expansion, many states opting to expand have determined that the net impact of opting to expand is positive for the state for several reasons: because of its effect on the state's fiscal situation, on the health of the state's population, its macroeconomic impact (including job creation), or all of the above.
- The recent recession has forced more Americans to turn to Medicaid, increasing the program's overall cost. However, Medicaid's per-enrollee costs for the typical working age adult and their children is modest. The program's per-enrollee cost growth is greatest for the disabled, the dually eligible adults who are either disabled or elderly, adults with behavioral-based illnesses, and low-income Medicare recipients who need long-term care. While the per-enrollee costs of the special populations are relatively expensive, were it not for Medicaid, many of these individuals would have little or no access to health or long-term care services. The absence of such care would allow the human costs of hardship and pain and, in some cases, premature death. In addition, without Medicaid as the insurer of last resort, private insurance rates would have to be higher to cover the charity or uncompensated care provided for the adults who end up in hospitals or nursing homes without insurance.
- Medicaid spending on long-term care services for all enrollees accounted for 31.5 percent of all program spending for service in 2010, according to the Kaiser Commission on Medicaid and the Uninsured. The Center for Medicare & Medicaid Services (CMS) Actuary points out that, "As the number of people age sixty-five or older increases — and especially the number of those over age eighty-five — there is a corresponding projected increase in the amount of long-term care spending, since elderly beneficiaries tend to use more long-term care than younger beneficiaries."

- Many states have instituted delivery system reforms that reduce long-term care costs by increasing the share of disabled and aging adults cared for in their homes, rather than nursing homes. These reforms have dramatically slowed the annual cost increases associated with long-term care. However, as the population ages, the cost implications for the Medicaid program for long-term care services suggest that substantial changes are needed both to ensure access to these critical care services and ensure the sustainability of the Medicaid program.
- Reforms to the Medicaid program are necessary to ensure the program's financial sustainability. The challenge is to identify reforms that do not undermine the health outcomes of poor, aging, or disabled Americans. In addition, reforms must protect against significant costs being shifted onto private payers. Often overlooked is the fact that the Medicaid program is also a driver of economic activity. It is responsible for the financial solvency of community health clinics and safety net hospitals and it is critical to the bottom line of nearly every health care system and a majority of primary care practices across the nation. Therefore, measures to restrain the rising costs of the program must be thoughtful, carefully researched, and considered from three critical perspectives: the needs of our poorest and most frail citizens, the risk that reforms may pose on other payers, and the economic impact reforms will have on the health care system of the nation.
- Medicaid is America's safety net health care system. Given the reach of the program, Medicaid can have an enormous influence on the approach and pace of health care delivery reforms that promote wellness, disease prevention, and chronic care management. However, while the program has substantial market share, it is not the dominant payer; therefore, it is bound by the norms of the health care delivery system writ large. Federal policy changes that accelerate the pace of reforms in the health care delivery marketplace affecting private payers as well as Medicare can benefit the Medicaid program.

### ***Observations from the National Dialogue on Medicaid***

The Task Force partnered with the Alliance for Health Reform and the SCAN foundation to present the National Dialogue on Medicaid at the Barbara Jordan Conference Center of the Kaiser Family Foundation. Advisory Board member Joseph Califano was the convener. Secretary Califano, who worked on the original team in the Johnson administration responsible for creating Medicaid, assessed the state of health care in America: 20 percent of Americans are insured through Medicaid, with spending and enrollment increasing by 360 percent and 300 percent, respectively, since 1975. The secretary warned:

*Without question Medicaid has improved the life expectancy and quality of life of vulnerable Americans for decades, and without some substantive changes to how the program is funded, its reach and impact could be undermined.*

Secretary Califano directed the discussion through three potential solutions:

- Health Care Delivery Reforms;
- Funding Reforms; and
- Administrative Reforms.

Debate focused on options for how the federal government can accelerate cost saving practices that promote improved health care quality and health outcomes, options for the federal and state focus and action to address the cost drivers of the most expensive enrollees while improving their health outcomes.

Health care spending as a share of gross domestic product (GDP) has grown from about 6 percent in 1966 to about 18 percent in 2010. Medicaid in that same period accounts for a rise from less than 1 percent in 1966 to 2.7 percent of GDP in 2010.

### ***Long-Term Services and Supports***

The U.S. Senate Commission on Long-Term Care, chaired by Dr. Bruce Chernof, chief executive officer of the SCAN Foundation, issued its final report on September 30, 2013.

The vision of the Commission in regard to service delivery is, “A more responsive, integrated, person-centered, and fiscally sustainable long-term services and supports (LTSS) delivery system that ensures people can access quality services in settings they choose.”

With regard to Medicaid, the Commission found that, “Medicaid is a critical safety net program, but it is not designed to meet the LTSS needs of a diverse population.” The Commission was not able to agree on a single recommendation for future financing of LTSS, but provided two alternative paths. While the Task Force does not endorse the recommendations of the Commission, it believes that their thoughtful approach to analyzing the increasingly expensive LTSS issues, especially in regard to state Medicaid obligations, warrants serious consideration by Congress and the administration.

### ***Summary on Medicaid***

Considering the complex and robust ongoing debate and analysis of experts, advocates, and academics surrounding the advancement of Medicaid, the members of the Task Force agreed that it would not be appropriate to offer recommendations. In respect of Medicaid funding and administration, as well as effects of the Affordable Care Act, there are difficult political and substantive choices that must be made by elected and appointed officials in a democratically accountable manner that is reflective of our values and politics.



## *Conclusion*

The Task Force recognizes the difficulties inherent in government change. It also recognizes the urgency for change. The primary reason the Task Force was created is that insufficient attention is directed to the fiscal imperatives of the states. States, and the local governments they create, are charged with providing the most important domestic government services. Yet important decisions on the national level often do not consider the impact of those decisions on their ability to deliver those services.

Nevertheless, states can improve their ability to provide services and enhance their financial and fiscal decisionmaking. Striving for structurally balanced, accrual based budgets when appropriate and providing clear analyses of the fiscal issues they confront can permit states to understand and recognize the challenges they must solve. The Task Force outlines those challenges and makes recommendations to address them.<sup>8</sup>



## Endnotes

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- 1 Papers are available on the Task Force's Web site: [www.statebudgetcrisis.org](http://www.statebudgetcrisis.org).
- 2 [www.statebudgetcrisis.org](http://www.statebudgetcrisis.org)
- 3 Accountability and Transparency in Budgeting and Financial Reporting had been covered extensively in the July 2012 Report of the State Budget Crisis Task Force and it was agreed that a Dialogue was not needed in this area.
- 4 Lucy Dadayan and Donald J. Boyd, *States Are Not Out of the Woods Despite Strong Revenue Gains in the Fourth Quarter*, State Revenue Report #91 (Albany, NY: The Nelson A. Rockefeller Institute of Government), [http://rockinst.org/newsroom/revenue\\_reports/2013/2013-04-24-SRR\\_91.pdf](http://rockinst.org/newsroom/revenue_reports/2013/2013-04-24-SRR_91.pdf).
- 5 See *Underfunded Pension Promises*, White Paper prepared by staff of the State Budget Crisis Task Force for the Dialogue on Underfunded Pension Promises, held at the Federal Reserve Bank of New York on April 19, 2013.
- 6 Donna Cooper, *Meeting the Infrastructure Imperative: An Affordable Plan to Put Americans Back to Work Rebuilding Our Nation's Infrastructure* (Washington, DC: Center for American Progress, February 2012), <http://www.americanprogress.org/issues/technology/report/2012/02/16/11068/meeting-the-infrastructure-imperative/>.
- 7 The American Society of Civil Engineers, *2013 Report Card for America's Infrastructure* (Reston, VA: The American Society of Civil Engineers, March 2013), <http://www.infrastructurereportcard.org/>.
- 8 Task Force Advisory Board member Joseph A. Califano, Jr., would add this thought to the conclusion: "In accommodating their financial difficulties the states should be particularly attentive to the needs of the most vulnerable in our society and to reducing the vast income inequality that has grown like Jack's beanstalk over the past two or three decades."

# ACKNOWLEDGMENTS

## ***Publications***

The Task Force has published the following documents:

- Report of the State Budget Crisis Task Force (July 2012)
- State Reports of the State Budget Crisis Task Force
  - California (September 2012)
  - Illinois (October 2012)
  - New Jersey (November 2012)
  - New York (December 2012)
  - Texas (November 2012)
  - Virginia (November 2012)
- Task Force White Papers
  - Improving the State/Federal Partnership of Medicaid (May 2013)
  - Managing the Impact of Federal Deficit Reduction (June 2013)
  - Unfunded Pension Promises (April 2013)
  - Increasing Transportation Funding to Benefit the Economy (April 2013)

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The Task Force is grateful for the work of its dedicated current and former staff:

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