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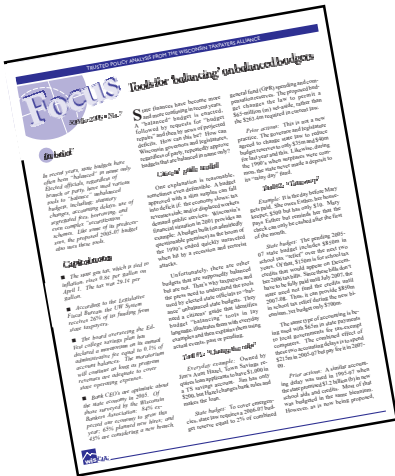
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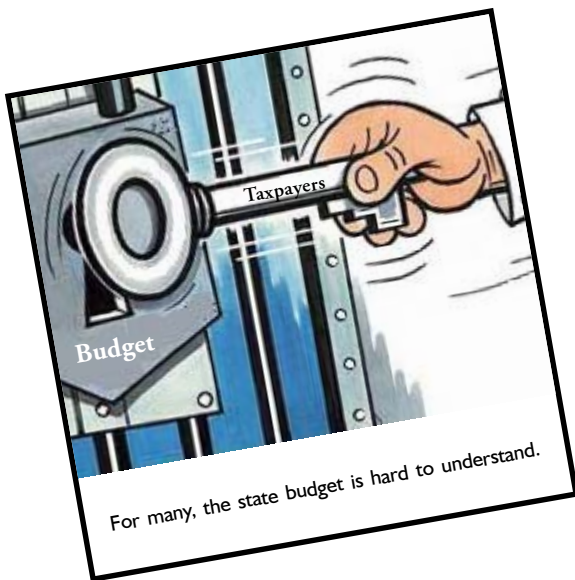
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Info Request



A monthly review of Wisconsin government, taxes and public finance

The Wisconsin Taxpayer



Also in this issue:

Wisconsin Notes: Wisconsin Wired

WISTAX Focus: Property Tax Increases; State Finances

Unlocking the Mysteries of the State Budget

IN BRIEF

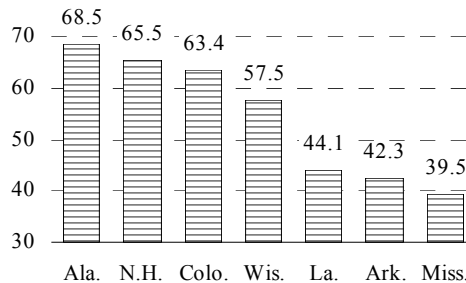
State agencies, legislators, elusive language and hard-to-follow numbers leave many thinking the state budget is an impenetrable mystery. Yet it is important for citizens to understand how the budget is prepared, and how the money is raised and spent. This report uses the 2005-07 state budget to do both.

- Wisconsin's governor has considerable power to modify the budget through his partial veto pen. And, over time, governors have used it extensively.
- Annual expenditures are budgeted at \$26.0 billion in 2005-06 and \$26.8 billion in 2006-07.
- Less than half the state's revenue comes from Wisconsin taxes. Federal aid alone accounts for 25.6%.
- Over 43% of the state's general fund taxes go to aid public schools. No other program cracks 12%.
- From all funding sources, the budget authorizes over 66,000 full-time equivalent positions by June 30, 2006. This is a decrease of over 2,000 from 2005.

Wisconsin Notes

■ **Wisconsin Wired.** Wisconsin households are more likely than households in other states to be connected to the Internet. According to a report by the U.S. Census Bureau, 57.5% of Wisconsin households had Internet access in 2003. That was above the U.S. average (54.7%) and 17th highest nationally. Alaska, at 68.5%, led the nation, while Mississippi was last with 39.5%. Among neighboring states, Wisconsin finished below Minnesota (61.7%, 7th), while Iowa (57.0%, 18th), Michigan (52.0%, 35th) and Illinois (51.2%, 38th) trailed. In Wisconsin, 34.0% of Internet households had high-speed connections, ranking the state 23rd nationally. The U.S. average was 35.8%.

Wisconsin 17th in Internet Access
% of Homes in 2003 (U.S. Avg. = 54.7)



Wisconsin also ranked high in a recent *Education Week* study on technology in schools. Statewide, there were 2.8 students per computer in 2004. This ranked Wisconsin 8th in the U.S. and one full student better than the national average (3.8). As for students per Internet-connected computer, Wisconsin was 11th with 3.5 students. The national average was 4.1. On both measures, Wisconsin ranked highest in the region.

WISTAX Focus

■ **Property Tax Increases.** With talk of a “freeze,” citizens have been eager to see their property tax bills for 2005-06. A recent issue of *Focus* estimated that net property tax levies statewide will rise 2.0%. According to projections in “Property tax increases average 2%” (#27-05), total gross levies will reach \$8.3 billion, a record when unadjusted for inflation. Increases in county, municipal and technical college taxes will be partially offset by a drop in school district levies. The overall increase will be the smallest since 1996-97.

■ **State Finances.** In “New state ‘GAAP’ deficit tops \$2.1b” (*Focus* #28-05), WISTAX examines a report on the state’s finances that uses generally accepted accounting principles (GAAP). Unlike the state budget, the GAAP report accounts for expenditures when they are authorized, not when payments are made. Since GAAP accounting began in 1990, the state has been in the red each year. At \$2.1 billion, the GAAP deficit is the second largest in 16 years (behind 2003) and \$191 million larger than in 2004.

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The Wisconsin Taxpayers Alliance, founded in 1932, is the state’s oldest and most respected private government-research organization. Through its publications, civic lectures and school talks, WISTAX aims to improve Wisconsin government through citizen education. Nonprofit, nonpartisan and independently funded, WISTAX is not affiliated with any group—national, state or local—and receives no government support.

Unlocking the Mysteries of the State Budget

No other government in Wisconsin is as large or pervasive as state government. From all sources, it will spend \$26.0 billion this year—a consequential sum given state personal income exceeds \$180 billion.

State government is primarily responsible for funding public schools and is a major source of revenue for municipalities, counties, higher education, and individuals with a variety of health and social needs.

What the state does through taxing and spending can impact: how Wisconsin is perceived elsewhere; the economic health of the state; and the quality of life of its people. In short, how the governor and legislature tax, borrow and spend matters.

As voters and taxpayers, state citizens need basic knowledge of their budget. This issue of *The Wisconsin Taxpayer* uses the 2005-07 state budget to promote greater understanding of the state's principal taxing-and-spending plan—its development, contents and associated controversies.

BUDGET PROCESS

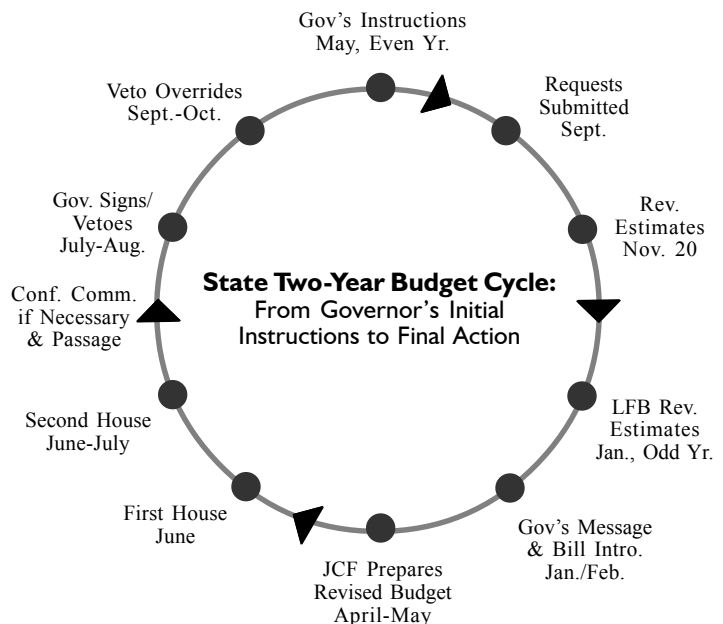
State government is financed on a two-year, or biennial, basis. A biennium runs from July 1 of an odd-numbered year to June 30 two years hence. Thus, the 2005-07 biennium began on July 1, 2005, and will end on June 30, 2007.

Governor Begins Process

Preparing a budget is initially the responsibility of the governor and the state agencies his appointees generally head. Usually in May of the even-numbered year preceding a new biennium—2004 for 2005-07—the governor issues budget instructions to the agencies along with guidelines on how

to prepare their budget requests. Due to state fiscal problems in recent years, these instructions have usually called for limited, or no, requests for additional funding.

Requests are usually submitted to the executive budget office in September. State elections occur in early November and as



required by state law, the requests, together with estimated revenues for the coming two years, are released on or before November 20.

This is usually when citizens, the press and lawmakers get their first look at state fiscal prospects for the coming biennium. Almost invariably, spending “wishes” exceed available revenue. During the next two months, the governor and staff work with state budget analysts to review and make decisions on various requests.

In January, the legislature's budget arm, the nonpartisan Legislative Fiscal Bureau

JCF has 16 members, with eight lawmakers from each house.

(LFB), updates November revenue estimates. The governor incorporates these into his final budget proposals.

By law, the governor must submit a budget message and accompanying executive budget bill(s) to the legislature in late January. However, the norm has been for the governor to request and for the legislature to grant an extension into February.

Legislature Takes Over

Once legislation and supporting executive-branch briefing materials are released, attention shifts to the legislature. The budget bill is introduced and referred to the legislature's 16-member Joint Committee on Finance (JCF). Meanwhile, state capital budget and related building recommendations are made by the State Building Commission, which the governor chairs, and forwarded to JCF.

Unlike other states, Wisconsin has one legislative committee that handles both taxing and spending decisions in all issue areas. This makes it one of the nation's most powerful. Individual legislative committees can also review and hold hearings on specific budget items related to their assigned topics. But it is JCF that makes final decisions.

The legislature's budget-writing committee is one of the nation's most powerful.

In the ensuing weeks, the LFB prepares a detailed summary of executive budget proposals, JCF members are briefed on the budget by state agencies and LFB staff, and public hearings are held. During this period, JCF often removes from the budget items considered "nonfiscal."

The finance committee works on the budget from April until late May or early June, eventually producing a substitute bill. The bill then moves sequentially through the two legislative houses. Party caucuses are briefed and may offer any amendments to the substitute; legislative floor action follows. If the senate and assembly cannot

agree on a budget, a conference committee "irons out" the differences, and a final legislative vote occurs.

Final Steps

Although a new biennium begins on July 1 of the odd-numbered year, the legislature usually does not finish its work until sometime that month. Occasionally, whether due to fiscal problems, partisan differences or the controversial nature of proposals, final budget action has not been completed until fall.

Usually, though, the governor reviews the budget passed by the legislature and signs it in late July or early August. The governor invariably modifies the budget with his partial veto pen, arguably the nation's most powerful. The biennial budget becomes law the day after it is published in the official state newspaper.

Gubernatorial vetoes may be considered for override by the legislature. In recent decades, overrides have become rare to nonexistent. In late fall, a comprehensive LFB summary reviewing the budget item by item is released.

The following May, budget instructions are again issued by the governor. And the two-year budget cycle for the next biennium begins anew (see graphic, page 3).

BUDGET'S "BIG PIECES"

How much the state spends annually varies widely by source and method of accounting. For 2005-06, politicians and reporters talked about annual budget expenditures of \$12.8 billion or \$26.0 billion, and both were correct.

The larger figure is total spending in the "all-funds" budget shown on page 5. The smaller figure represents expenditures budgeted from general purpose revenues (GPR) deposited in the general fund (see page 7). As detailed in the next section, GPR con-

sists almost entirely of state income and sales taxes. General fund revenues also include some fees and charges paid by users of general fund programs, although those amounts are comparatively modest.

“All-Funds” Revenue

The largest single source of “all-funds” revenue is GPR (49.5% in the 2005-07 biennium). The percent is slightly lower (48.1%) if \$1.5 billion in bond proceeds are included.

The next largest revenue source for the all-funds budget, about a quarter of the \$54.3-billion total, is \$13.5 billion from the federal government. The state receives smaller amounts of program (\$7.65 billion), segregated (\$5.43 billion) and bond revenue (\$1.54 billion), as shown in the table (right).

Some state agencies are more reliant on federal and various fee dollars than others. Put another way, they make relatively little use of GPR taxes.

From an all-funds perspective, the Department of Health and Family Services (DHFS) will spend the most (\$13.2 billion) over the next two years. However, a majority of that (\$6.8 billion) is from the federal government, with the bulk of that funding health care for those with low and moderate incomes through Medicaid, BadgerCare and SeniorCare. Only 38.0% of DHFS’s biennial revenues come from the general fund (see table, page 6).

Examples of other large agencies that rely less on the general fund are Transportation (DOT, 2.4% of all revenues) and the University of Wisconsin System (UWS, 24.4%). DOT is the best illustration of reliance on segregated, or “seg,” fees. Gas taxes and license fees are both deposited in the segregated transportation fund reserved for transportation-related uses.

However, in the 2003-05 and 2005-07 budgets, the governor—and some legislators—successfully advocated using DOT dollars to pay for general fund programs (most notably school aids) and to keep the GPR budget “balanced.”

The UWS is a prime example of the use of program revenue (PR). Of the \$7.9 billion it is to spend this biennium, \$4.2 billion is PR, e.g., student tuition. The UWS—mainly the Madison campus—also relies heavily on federal funds (\$1.8 billion).

In addition to DHFS, DOT and the UWS, the table (page 6) shows six other agencies and programs that will spend \$1 billion or more during this biennium. These nine account for \$48.1 billion, or 91.2%, of the \$52.7 billion in all-funds expenditures (excluding bonds).

“All-Funds” Spending

Several other ways to view the all-funds budget deserve mention. In its budget summary by program area, the LFB reports that \$20.7 billion, or 39.2%, of these expenditures are devoted to education, and another \$18.2 billion (34.5%) go to human services. The only other areas of any size are environment (\$5.7 billion, or 10.9%) and shared revenue/tax relief (\$3.7 billion, or 7.0%).

General taxes are less than half of state revenues from all sources.

“All-Funds” Budget Has Many Revenue Sources
2005-07 Biennium (\$ Bill.)

Fund Source	Year (\$ Bill.)		Total	% of:	
	05-06	06-07		Subt.	Total
General (GPR)	12.77	13.35	26.13	49.5	48.1
Federal (FED)	6.70	6.83	13.52	25.6	24.9
Program (PR)	3.74	3.91	7.65	14.5	14.1
Segregated (SEG)	2.74	2.69	5.43	10.3	10.0
Subtotal	25.95	26.78	52.73	100.0	97.2
Bonding			1.54		2.8
•Gen. Obligation			1.31		2.4
•Revenue			0.23		0.4
Total			54.27		100.0

These four categories represent 91.6% of biennial expenditures. Relatively little is spent on areas the public would most likely identify as “government”: 4.0% for general executive activities; 0.4% for courts; and 0.2% for the legislature.

A second way to recap the 2005-07 all-funds budget breaks spending into fewer categories. The largest is state aid to various local units of government (\$19.2 billion, or 36.4% of all expenditures), followed closely by state operations (\$19.1 billion, or 36.2%). The final category is aid to various individuals and organizations (e.g., Medicaid) which totals \$14.4 billion (27.4%).

The state operations category is sometimes divided between the university and state government. Including pending pay adjustments, the UWS accounts for 14.4% of all-funds spending and state government, 21.8%. Said another way, what citizens think of as the “state bureaucracy” accounts for about one in five dollars spent, be it from state taxes, the federal government or program users.

A third view of state expenditures comes from the perspective of employee numbers.

From all revenue sources, only 21.8% goes to run state government.

Just as there is a big dollar difference between the all-funds and general fund budgets, the employee positions they fund vary greatly, as well. The total number of full-time equivalent (FTE) positions authorized by the end of the next fiscal year is 66,132, or 2,069 less than the 2004-05 base. Only 34,412 of those jobs, however, are GPR-funded. This is 785 fewer than in 2004-05.

GPR BUDGET: “THE” BUDGET

When the state budget is discussed in the press or debated in the legislature, the focus is usually on the general fund budget. That is not surprising, for most of the state taxes paid are GPR.

Revenues

Taxes. Of GPR taxes, the “big three” are the individual and corporate income taxes, and the sales tax. Biennially, they represent 92.1% of GPR taxes.

As the table (page 7, bottom) indicates, the individual income tax, created by Wisconsin in 1911, is the state’s main (51.7%) source of revenue with more than \$6 billion in annual collections (\$12.6 billion for the biennium). Comprising 34.9% of GPR taxes, the sales tax takes in more than \$4 billion annually. The only other tax of any consequence, the corporate income tax, will produce close to \$700 million both this year and next (5.5% of the total).

At the outset of 2005-07 budgeting, the governor and legislative leaders said they would not increase general fund taxes. Indeed, the budget includes some modest tax reductions, most notably an increased tuition deduction and eventual exclusion of social security benefits from taxation.

Although no rates were increased, revenues are growing for several reasons. The primary one is that tax collections grow with the economy. Estimates suggest they

Nine “Billion-Dollar” Agencies, Programs Dominate But Some Rely Little on GPR, 2005-07 Biennium

Agency	All-Funds (A-F)		Gen. Fund (GPR)		
	\$ Bill.	% Tot.	\$ Bill.	% Tot.	% A-F
Administration	1.49	2.8	0.42	1.6	27.9
Corrections	2.06	3.9	1.80	6.9	87.4
Health & Family	13.16	25.0	5.00	19.1	38.0
Nat'l Resources	1.02	1.9	0.29	1.1	28.1
Public Instruct'n	12.06	22.9	10.70	41.0	88.7
Shared Rev. +	3.67	7.0	3.28	12.6	89.4
Transportation	4.60	8.7	0.11	0.4	2.4
UW System	7.93	15.0	1.93	7.4	24.4
Workforce Dev.	2.08	4.0	0.36	1.4	17.2
Subtotal	48.08	91.2	23.89	91.4	49.7
All Other	4.65	8.8	2.23	8.6	48.0
Total	52.73	100.0	26.13	100.0	49.5

Biennium To End with Slim Balances

General Fund Condition, 2005-07 (\$ Mill.)

Item	05-06	06-07
Revenues		
Surplus	5.8	65.2
Taxes	11,957.1	12,506.8
Tribal Gam'g	118.6	86.3
Other	674.8	513.6
Tot. Avail.	12,756.3	13,172.0
Appropriations		
Gross	12,681.2	13,176.2
Comp. Res.	90.1	178.3
Other Adj.	-80.1	-252.9
Net	12,691.1	13,101.6
Balances		
Gross	65.2	70.4
- Req'd Res.	-65.0	-65.0
Net	0.2	5.4

will be \$560.5 million, or 4.9%, higher this year than last, and \$549.7 million, or 4.6%, more in 2006-07. Included in these figures is \$29 million that will be collected through "enhanced collection" of current taxes.

"Nontax" Revenues. When more modest amounts of carryover, departmental and "other" revenues are added to GPR taxes, the result is total general fund revenues available: \$12.8 billion in 2005-06 and \$13.2 billion the year after for a biennial total of \$25.9 billion. These and other key components of the 2005-07 general fund condition are summarized in the table (above).

One interesting aspect of 2005-07 revenues is the unusually large amount classified as "other." The two-year total of \$1.2 billion exceeds all taxes, except the "big three," and approaches the size of corporate income tax collections.

Part of this is due to agencies charging and/or increasing user fees. For example, various professions pay to be licensed. When an individual goes to court, costs are recovered through court fees. Additionally, the amount of "other" revenues is

much larger than normal because the state is moving money from non-GPR sources to the general fund to keep it balanced.

The largest transfer is from the transportation fund, nearly \$430 million over two years. To replace that, borrowing for projects the fund would normally support with gas taxes and registration fees will continue to increase. Transportation revenue-bonding authority is expected to rise \$228.8 million this biennium. Between 1990 and 2005, transportation debt service increased 180%. By comparison, spending on highway construction was up 68%.

Other major sources of one-time transfers include: the conservation fund (\$31.6 million); the petroleum inspection fund (\$30.9 million); the recycling fund (\$30.6 million); and the public benefits fund (\$55.5 million).

All told, the LFB estimates that \$647.9 million is being taken from segregated funds or lapsed from program revenue accounts and "used for purposes other than those for which the fund was generally established." Because these one-time transfers will not be available to pay for permanent, continued spending in 2007-08, a potential budget problem lies ahead.

Income and sales taxes are 92.1% of general fund taxes.

Income and Sales Taxes Dominate GPR Taxes 2005-07 Biennium (\$ Mill.)

Tax	05-06	06-07	Total	% Tot.
Ind. Inc.	6,144.5	6,502.8	12,647.3	51.7
Sales	4,181.6	4,358.1	8,539.7	34.9
Corp. Inc.	683.3	670.3	1,353.6	5.5
Utility	267.5	281.1	548.5	2.2
Excise				
Cigarette	287.8	286.8	574.6	2.3
Liq./Wine	40.8	41.6	82.4	0.3
Tobacco	16.5	17.4	33.9	0.1
Beer	9.6	9.6	19.2	0.1
Insurance	131.0	137.7	268.7	1.1
Estate	105.0	110.0	215.0	0.9
Misc.	89.5	91.5	181.0	0.7
Total	11,957.1	12,506.8	24,463.9	100.0

Expenditures

In addition to revenues, the general fund summary on the previous page recaps expenditures, as well. Biennial appropriations, total \$26.1 billion. This is \$2.39 billion, or 10.1%, more than spending in the prior biennium as measured by the LFB's 2004-05 "base-year doubled" approach.

Added to gross appropriations of \$25.9 billion are \$268.4 million to cover two years of state-employee compensation increases. Appropriations are further adjusted by a one-time transfer to the Medicaid Trust Fund, which raises spending, and lapses

of budgeted monies back to the general fund, which lowers it. The result is net appropriations of \$12.7 billion in 2005-06 and \$13.1 billion in 2006-07, or \$25.8 billion overall.

By Program Area. How Wisconsin spends its general tax revenues can be thought of in several ways. The most obvious is by agency (see table on page

6). Of the \$26.1 billion in total biennial appropriations, the five largest recipients are the following departments, plus local aid/tax relief programs:

- Public Instruction (\$10.7 billion, or 41.0% of the total);
- Health and Family Services (\$5.0 billion, 19.1%);
- Shared revenues and tax relief (\$3.3 billion, 12.6%), which includes "no-strings" aids to municipalities and counties, and some tax credits;
- UW System (\$1.9 billion, 7.4%); and
- Corrections (\$1.8 billion, 6.9%).

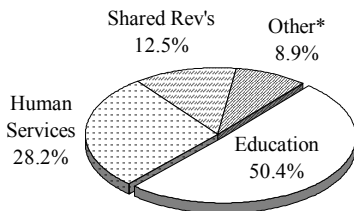
This view of spending can be misleading; a state agency can perform different

services that have little to do with each other programmatically.

Another, perhaps more useful, perspective is spending by program area. When the budget is viewed this way, education is the state's top priority, claiming 50.4% of 2005-07 gross appropriations (see pie chart, left). At \$13.2 billion, it dwarfs the other major areas: human services (\$7.4 billion, 28.2%) and shared revenue/tax relief (\$3.3 billion, 12.5%). These three categories represent 91.1% of expenditures.

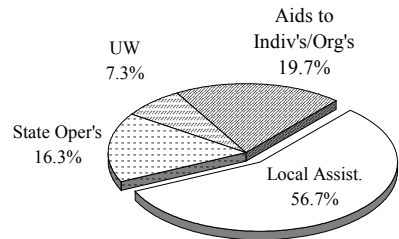
Again it is clear that state spending is concentrated in a few areas. It is also evi-

Education Dominates Spending
% GPR Spending (\$26.1 Bill.)



*Executive (2.8%), Environment (1.9%), General Appropriations (1.5%), Compensation Reserves (1.0%), Judicial (0.8%), Legislative (0.5%) and Commerce (0.4%).

Local Aids Dwarf State Operations
% GPR Spending (\$26.1 Bill.)



dent that the share of spending devoted to activities generally thought to be "government" or "bureaucracy"—executive (2.8%), judicial (0.8%) and legislative (0.5%)—is relatively small.

By Recipient. Often, state analysts view GPR spending not by program, but broadly by type of recipient. The single largest category is local assistance, which includes various aids and payments to school districts and local governments, as well as credits to property taxpayers. Such assistance accounts for 56.7% of GPR spending (see pie chart, above). This percentage is actually an understatement, for this budget pays out an additional \$215 million in local assistance during this biennium that is not "booked" until the next.

More than three-quarters of local assistance goes to local school districts in the

form of aid and to property taxpayers as school levy tax credits. Together, these two items are used to estimate the “two-thirds” funding level for state aid to public schools.

Other beneficiaries of local assistance are municipalities and counties receiving shared revenues; technical colleges; and counties that are paid several kinds of human service aid.

The second-largest share (19.7%) of GPR spending aids individuals and organizations. About 60% of this is paid as Medical Assistance (MA) to low- and moderate-income individuals and families. Related BadgerCare and SeniorCare push the Medicaid percentage over 64%. Various public assistance and income-support payments and tax credits are included in this category, as are student grants and aid, and funding for choice and charter school programs.

The remaining two categories are for operating state agencies (16.0%) and the UWS (7.6%). That local assistance is more than three times the size of state operations is a useful reminder that the business of state government is more focused on funding local governments than on its own operations.

By Size. A final way to think about general fund expenditures is simply by the size of appropriation. The table at right (originally prepared by the LFB) lists the 10 largest GPR programs for this biennium. Not surprisingly, aid for elementary and secondary schools dwarfs all other programs, as it claims about two of every five general fund dollars spent. This percentage is even larger (over 43%) if school levy tax credits counted as part of “two-thirds” school funding are included.

The second-largest appropriation is for Medical Assistance, or Medicaid. This is a

fast-growing part of the state budget. This year, its spending share is 10.7%, and next year it will be 12.9%.

All of the remaining “top-10” programs are losing “budget share” over the biennium. With little or no growth in most areas, and a 26.1% increase in MA from first to second years, it is easy to understand why. In the case of shared revenues and the UW System, it could be argued that they have been ceding share to school aids, more or less, since the early 1970’s.

School Aids and Credits 43% of GPR Budget
2005-07 Biennium, % GPR Spending (\$26.1 Bill.)

Program	05-06	06-07	% Chg.	Total	% Tot.
School Aids	5,116.4	5,251.6	2.6	10,368.0	39.7
School Tax Cr's*	469.3	469.3	0.0	938.6	3.6
Subt. Aids/Cr's	5,585.7	5,720.9	2.4	11,306.6	43.3
Medicaid (MA)*	1,360.8	1,716.1	26.1	3,076.9	11.8
Shared Revenues	947.9	952.6	0.5	1,900.6	7.3
UW System	948.4	950.5	0.2	1,899.0	7.3
Correctional Op's	791.7	768.3	-3.0	1,559.9	6.0
Comm./Juv. Aids	297.4	292.4	-1.7	589.8	2.3
Judic. Legal Svcs.	217.0	216.5	-0.2	433.4	1.7
App. Obl. Bonds	190.8	190.8	0.0	381.7	1.5
Pub. Assistance	154.3	150.1	-2.7	304.4	1.2
Subt. "Top 10"	10,494.0	10,958.2	4.4	21,452.2	82.1
Remainder	2,277.2	2,396.3	5.2	4,673.5	17.9
Total	12,771.2	13,354.5	4.6	26,125.8	100.0

*Items such as these may not reflect their total funding due to adjustments made for accounting shifts (credits) or fund deficits (Medicaid).

Bottom Line?

With all GPR spending accounted for in one way or another, it is natural to ask: Is the budget balanced? Is there money left over? As will become clear, answering these questions is not as easy as it seems. It is possible to say that, according to the general fund condition statement (page 7) and allowing for a statutory reserve as required by law, both fiscal years would end with slim net balances: \$0.2 million in the first year and \$5.4 million in the second.

STATE OF STATE FINANCES

However, whether the 2005-07 GPR budget is balanced is open to debate. Many of the same techniques used by past governors and legislatures to keep budgets in balance—at least on paper—are being used again this biennium.

The 2005-07 budget had fiscal challenges from the outset. In November 2004, the first biennial revenue estimates and spending requests were released, and headline writers suggested a \$1.6-billion deficit was possible—less than the \$3.2 billion they featured two years before.

2004-05 Difficulties

Late this fall, state officials got a surprise. They expected to end 2004-05 in the black. However, a series of adjustments reduced the general fund balance to \$4.1 million, a small amount considering the state spent almost \$11.9 billion. Even reaching \$4.1 million turned out to be a challenge.

A number of factors pulled down the expected higher balance. According to the LFB, these included: a \$27.4 million reduction in the 2003-04 ending balance; \$49.7 million less in 2004-05 tax collections than expected; an offsetting \$20.4 million due to higher fee revenues and lower expenditures; and a surprise error in individual income tax accounting.

Had nothing been done, 2004-05 would have ended with a \$50.9-million deficit. To avoid this, an earlier \$75 million transfer to the Medicaid Trust Fund was reversed and spread over two years, rather than one. That left the state general fund with a small 2004-05 surplus of \$4.1 million. But it also left the MA trust fund with a \$53.9 million hole.

Is the 2005-07 Budget Balanced?

As mentioned, the net ending balances for this and the next fiscal year are both positive, but slim. It does not take much,

however, to argue that the 2005-07 budget is only technically balanced.

For starters, the MA trust fund remains in debt, although the administration is taking actions to maximize revenues and cut anticipated costs. This summer, the LFB estimated deficits of \$46.4 million and \$60.2 million, respectively, for this year and next.

In addition, some expenditures are not being accounted for until after the biennium closes. School levy tax credits are being increased by \$124 million in 2006-07 so that state officials may claim “two-thirds” funding of schools. However, that amount will not be budgeted for until 2007-08. A similar maneuver will delay the payment date of \$65 million in state aid for tax-exempt computer equipment.

Including any of the above items in the general fund condition statement would result in a deficit.

Interstate Comparisons

Wisconsin’s fiscal situation is more marginal than most states, according to a December 2005 report from the National Governors Association (NGA). The report summarizes budget balances as a percentage of expenditures for each of the 50 states.

2003-04. In 2003-04, Wisconsin’s balance was positive, about 1.0% of expenditures. The 50-state average was 5.1%. Only three states had smaller balances than Wisconsin: Michigan (0.9%); Arkansas (0.0%); and Oregon (-8.1%). Five other states had balances larger than Wisconsin’s but less than 2.0% of spending.

2004-05. For the fiscal year just ended, the NGA assumed Wisconsin’s balance was about \$6 million, rather than the actual \$4 million. Either way, when rounded, the state’s balance was 0.0% of expendi-

Wisconsin’s net ending balance in 2004-05 was only \$4.1 million.

Nationally, only three states had smaller balances than Wisconsin.

tures. No states had smaller balances, but Michigan and Arkansas were both estimated to have 0.0% balances, like Wisconsin. The national average was 6.9%.

2005-06. Looking ahead to estimates for this year, NGA uses Wisconsin's gross balance budgeted at \$65 million, or 0.5% of spending. This does not include the statutory reserve of a similar amount, nor does it reflect any deficit in the MA trust fund.

The 50 states have balances averaging 4.6% of spending. Five states have smaller balances than Wisconsin: Kentucky (0.4%); Maine (0.3%); Arkansas (0.0%); Connecticut (0.0%); and Michigan (0.0%). Another five have balances greater than Wisconsin but less than 2.0%.

Looking Back, Looking Ahead

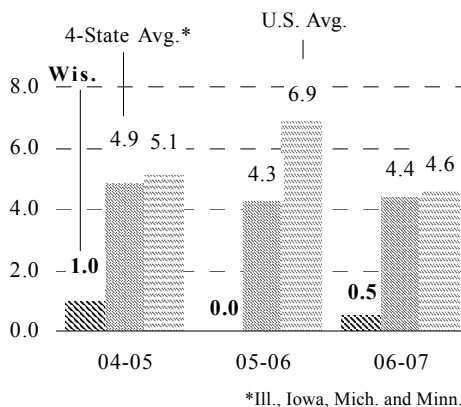
A practice that has made state finances worse over the past decade, regardless of party or personality, has been "advanced commitments." These are future spending plans and increases, or tax reductions, to which the governor and legislature have committed state government.

The accounting for school levy and computer tax credits just mentioned is one example that impacts the budget in 2007-08. Another is the income tax exclusion for social security income effective in tax year 2008 that will reduce income taxes by \$4.1 million in 2007-08 and \$24.1 million in 2008-09.

Using monies from other funds, e.g., transfers from the transportation fund, also has financial impacts beyond the current budget. These are one-time revenues used to cover ongoing expenditures, e.g., school aids funded with highway and vehicle user charges. In the future, another revenue source will be needed.

Looking Back. The projected gap between expenditures and revenues, when negative, is often referred to as the "structural deficit."

Wisconsin Budget Balances vs. Others
Balances as % of Expenditures, 2004-06



Wisconsin's budgeted balances are less than the U.S. average and those of surrounding states.

structural deficit." Structural deficits have dogged state officials since the 1990's.

As far back as 1997-99, a \$624-million structural deficit existed. Indeed, the LFB found structural problems in the opening year of that biennium, the three that followed, the current biennium (2005-07) and the one to come (2007-09).

The graph on the following page shows that the first year of each biennium opened with advanced commitments that had to be addressed.

Looking Ahead. The good news is that the structural problem for 2007-09 is smaller than it was at the beginning of this biennium (\$701 million) or the one prior (\$1.3 billion). The not-so-good news is that the state will still face a \$582-million

The state faces a structural deficit of \$582 million for 2007-09.

Continued on page 12

DATA SOURCES:

Legislative Fiscal Bureau; National Governors Association; Wisconsin Departments of Administration and Revenue; and WISTAX databases and publications.

Continued from page 11

Wisconsin's structural deficits have declined since 2003.

structural deficit as it begins budgeting for 2007-09.

According to the LFB, the \$582 million consists of \$319 million less in revenues and \$275 million more in spending. If no action were taken, the structural deficit would rise to \$779 million in fiscal 2009.

What this means for 2007-08 is that, before state government commits any money to new programs, to program expansions or even to cover the rising costs of present services, it will have to find \$582 million to fund existing commitments. Even routine employee-pay increases, no matter how small, will have to take a back seat to prior promises.

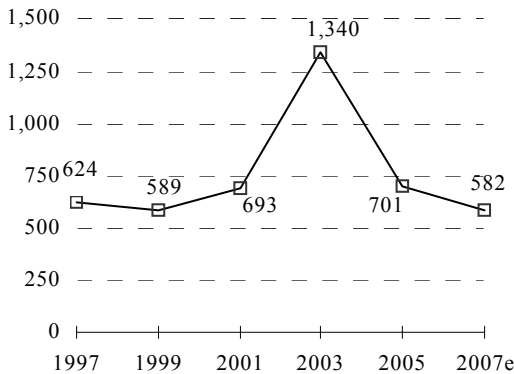
In order to generate \$582 million, state tax collections would have to grow about 4.6% from next year to 2007-08. When the economy is growing, this kind of

growth, or more, is common. Of course, more rapid increases in tax collections are needed if the governor and legislature will be able to pay for past promises and cover any rising costs of existing programs. School aids and Medicaid are two prime examples of programs whose costs rise inexorably.

Will there be a budget crisis in the 2007-09 biennium? Not necessarily. During the boom of the late 1990's, revenues repeatedly beat estimates, allowing elected officials to begin programs, increase spending, cut taxes *and* solve carryover problems such as this. Unfortunately, expenditures "got ahead" of revenues, with the recession of 2000-01 and the slowdown due to "9/11." Wisconsin has had budget difficulties ever since. □

"Tradition" of Structural Deficits?

First Year of Biennia, 1997 - 2007e (\$ Mill.)



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