

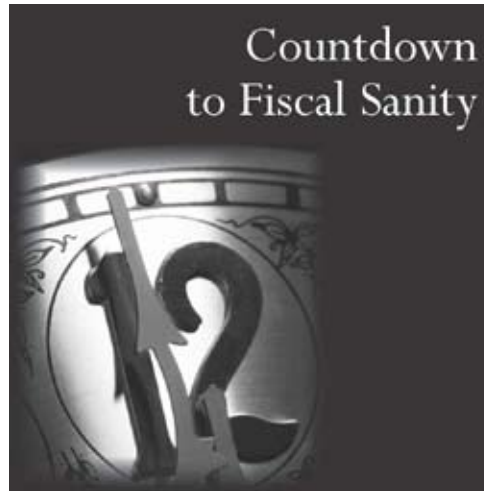


Countdown to Fiscal Sanity

Meeting the Challenge of the FY10 Budget

by Jim Stergios and Steve Poftak

It took one day for the House of Representatives to raise the sales tax 25 percent. It took just one day for the Senate to do the same. (The Governor has taken longer to put out his tax increase proposals, which range from a 19-cent gas tax increase, hundreds of millions of dollars in soda, candy and other targeted fees, as well as consideration of a graduated income tax.)



With all of this talk of taxes, you would think that taxpayers are sitting on mattresses of cash. They are not. They—we—are hurting. And before anyone comes knocking on the door, with a smile, an empty briefcase, and a pitch to fill it, we need an agenda of real reforms.

The impact of the global economic downturn is surely a contributing factor in the state's budget shortfall, but the fact is that states like Indiana, which have been frugal in expanding government and have sought new ideas and reforms at every turn, have budget surpluses. States that lost their way, like California and Massachusetts, are stuck in nineteenth century machine politics. Our current fiscal predicament is not merely a function of the economic downturn. It has been there for years, papered over by our leaders. It is a function of our dependence on highly volatile capital gains taxes and the inexorable increase of fixed expenses.

The Shamie Center for Better Government seeks limited, accountable government by promoting competitive delivery of public services, elimination of unnecessary regulation, and a focus on core government functions. Current initiatives promote *reform of how the state builds, manages, repairs and finances its transportation assets as well as public employee benefit reform.*

**Shamie Center
for Better
Government**

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Some hard choices have been made but much of the solution has so far consisted of incremental, across-the-board cuts, which result in underfunded, ineffective programs now, and have in the past led to even larger budget increases when the economy turned around. Despite protests that “everything is on the table,” sacred cows remain untouched. The willingness to raise the sales tax so quickly demands that we be equally zealous in our approach to find budget savings. The following suggestions should be considered and acted upon with the same dispatch that the Legislature enacted tax increases.

*Total Savings:
\$1.689 billion*

Meeting the challenge of the FY10 budget will require that Massachusetts examine every aspect of its budget and operations and face some hard truths. We would do well to follow the example of strategies used in the private sector and states that have bonafide surpluses in this time of economic turmoil. The time to do that is now. The clock is ticking.

10. Cut Supplier Costs

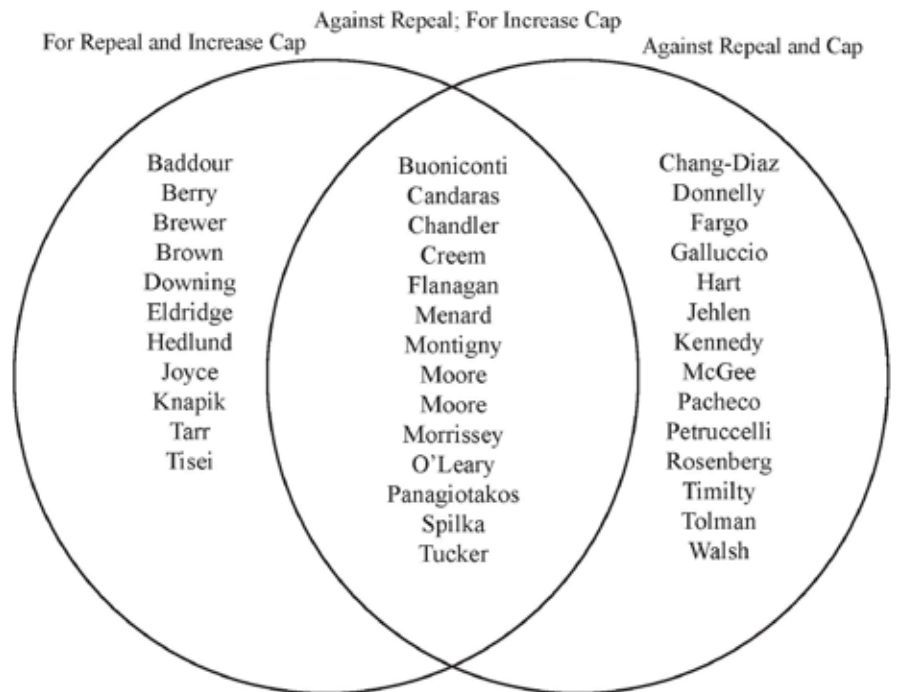
Cutting supplier costs is never easy. In the private sector, relationships with suppliers can be long-term friendships. In the public sector, they can run even deeper. Suppliers can include fundraisers, sign holders and campaign workers; too often these relationships include self-dealing and self-interest. In the private sector, the bottom line will win out. To date, in the public sector, our elected officials have let their friends win out.

The cost of their friendships is high. Every dollar wasted through

inefficiency is a dollar that cannot be used for education, services to the vulnerable, or public (including health and environmental) safety. Every dollar wasted is a lost opportunity to modernize our government.

The most effective way for Massachusetts’ state government **\$55M+** to cut its supplier costs is to **repeal the Pacheco Law**. Enacted in 1993, the Pacheco Law prevents the state from achieving faster, better, and cheaper delivery of state services through outsourcing, lease arrangement, and outright privatization. We must maximize the effectiveness and efficiency of state dollars by repealing this law.

Outsourcing is never easy. It requires the clear definition of objectives, effective state oversight, and protections from conflicts of interest. But repealing the Pacheco Law would allow state entities to access a full range of procurement options available to other similar public entities across the country and around the globe.



For transportation and infrastructure procurement, the state would have options to employ Design-Build-Finance-Operate-Maintain and Design-Build-Operate-Maintain agreements. The use of these procurement options has elsewhere reduced life-cycle costs by up to 40% while reducing delivery time by 25%.¹ They would serve as an important tool to address underinvestment in maintenance. Unfortunately, due to Pacheco Law restrictions, our public servants cannot currently use them.

Recently, the State Senate took two votes related to the Pacheco Law. The first was to repeal the law altogether — which failed. The second was to increase the cap on the law. Currently, contracts under \$200,000 are exempt from the Pacheco Law's restrictions. The vote was to raise that minimum to \$2 million. Fortunately, it passed. The diagram on the previous page shows the breakdown in voting.

Against the legislature's lack of urgency stand numerous reports and commissions, including the Transportation Finance Commission, that have called for the state to use a full range of procurement options. Pioneer believes that savings could range from a minimum of \$55 million annually to a figure much higher than that, depending on the number and scope of state services put out to competitive bid. For more, see our October 2008 policy brief, *Hard Decisions, Needed Leadership*.²

Massachusetts stands alone by having the most restrictive anti-competition measures in the country. We must join the dozens of states benefiting from the combined savings and enhanced quality that can result from opening public service delivery to competition.

9. Cut Payroll Costs

State Payroll is among the largest areas of expense in the state **\$342M** budget. The current fiscal climate requires that these costs be addressed, both for short-term savings and long-term sustainability. At both the municipal and state levels, employee compensation has long suffered from a lack of transparency. While official documents and press reports frequently focus on negotiated wage increases, they fail to capture other forms of compensation, like automatic step increases, additional leave, and various bonuses and stipends. Actuarial records suggest that the average annual salary increase for state employees ranges from 8% annually in their initial year of employment to 4.5% after 20 years.³ As an instructive, but non-parallel frame of reference, average annual pay in the private sector in Massachusetts increased at an average rate of only 3.4% annually from 2001 to 2007.⁴ In this environment, some combination of controlling headcount (layoffs, hiring freeze, attrition) and controlling payroll (salary freezes, wage concessions) is a vital part of shared sacrifice.

Reduce Headcount to 2004 levels: Since 2004, state government has increased unsustainably. Using data from the same time period in each year to control for seasonal employees at environmental and higher education agencies, the Commonwealth's workforce increased by almost 10% — 7,500 additional employees -- between 2004 and 2008.⁵ The state's workforce now totals 83,636. Of the new hires, only 1,100 joined Health and Human Services, which we take as a proxy for those added to 'safety net' programs.

The Administration has already pledged to cut state employment by 750 employees; however, it is not yet clear if this will be achieved through layoffs, attrition, or hiring freezes. Attrition is an ongoing process that occurs throughout every year; it will not achieve any

1. Pioneer White Paper #44: *Life Cycle Delivery of Public Infrastructure: Precedents and Opportunities for the Commonwealth*, John Miller, December 2008. (<http://pioneerinstitute.org/pdf/wp44.pdf>)

2. *Hard Decisions, Needed Leadership* (http://pioneerinstitute.org/pdf/081017_pb_budget_cuts.pdf)

3. pg.28, January 1, 2008 Commonwealth Actuarial Valuation Report, PERAC

4. Data table from Bureau of Labor Statistics website.

5. pg. 182, 2008 Comprehensive Annual Financial Report, Office of the State Comptroller, Commonwealth of Massachusetts. It should be noted that these numbers are all consistently from the same year-end pay period and do not include part-time higher education contractors. Therefore, the numbers should be comparable and any seasonal variations should be eliminated.

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incremental savings alone. Similarly, a hiring freeze only holds open an already unfilled position; again, it achieves little in the way of incremental savings. Conversely, many municipalities have already undertaken substantial layoffs. We believe cutting employment levels back to where they were in 2004, with the exception of the 1,100 safety net employees cited above, will allow the Commonwealth to maintain core state services while still reining in costs. At an average salary of \$53,436⁶, eliminating 6,400 workers from state payrolls would result in savings of \$342 million.

Seek reasonable wage concessions: Massachusetts public employees make as much, and typically more, than their peers in the private sector. Significantly more. According to data from the U.S. Department of Labor that analyzed compensation for private sector, state, and local employees in Massachusetts and New Hampshire, state employees make an average of 15 percent more than employees in the private sector.

Looking more closely at various occupational groupings, we see **\$500M+** a more nuanced picture, with some occupations earning better compensation in the private sector. However, in the available occupation group classifications, no average public sector wage was more than 10% below the private sector level of compensation. On the other hand, certain public sector occupations received huge premiums – wages 90% higher for service workers and 40% higher for transportation-related employees. Moreover, these calculations only examine wages and other forms of salary; they do not account for the public sector's more generous pension, leave, and health benefits.⁷

Massachusetts' municipalities and other states have negotiated wage concessions, frequently in exchange for reduced layoffs, even though the same superior compensation levels, vis-à-vis private sector peers, cannot be claimed for municipal public servants. Comparable compensation is to be wished for;

unfettered growth in state employee compensation is unsustainable. Now is the time to stop it.

At a time when taxpayers will be expected to pay billions in additional taxes, constraining the growth of public sector compensation is required. We hope state officials will undertake a combination of layoffs and wage concessions to reach annual savings of at least \$500 million.

8. Lower Structural Costs

If the Commonwealth wants to address escalating payroll costs, our leaders must be prepared to show political courage. What follows are three ways to rein in public employee health care costs and one to address pensions costs. None of our recommendations is punitive; all of them are reasonable.

- We currently face a \$13 billion liability for **unfunded public employee retiree health insurance**. If we want to stop the liability from growing, the state must curtail eligibility for this benefit. Right now, any municipal or state worker who works for 10 years is eligible. This is an absurdly low standard and there is no remotely parallel benefit in the private sector. A higher threshold should be set and maintained. Along with a responsible program for funding the liability, raising the eligibility threshold has the potential of reducing the liability by billions of dollars. For more, see our policy brief on retired public employee healthcare benefits, *The Elephant in the Room*.⁸
- The Governor's proposal to **increase cost sharing for \$60.4M state employee healthcare insurance purchasing** should be enacted. This change will bring what state employees contribute to levels consistent with the private sector, saving in the process \$60.4 million annually. We should also examine the possibility of moving to a

6. Pg.14, January 1, 2008 Commonwealth Actuarial Valuation Report, PERAC

7. Boston–Worcester–Manchester, MA–NH National Compensation Survey October 2007, Department of Labor.

8. *The Elephant in the Room* (http://pioneerinstitute.org/pdf/06_gasb_45_elephant_in_the_room.pdf)

defined contribution system whereby the state's contribution would be set at a fixed amount of a standard plan type (most likely the PPO options offered by the GIC). This would create an incentive for more employees to access lower cost plans rather than the higher-priced indemnity plans favored by many.

- On the municipal level, **greater participation in GIC** (or other buying consortia that offer similar savings) and **mandatory enrollment of retirees in Medicare** should be enacted. In Springfield, these two steps resulted in savings of over \$10 million per year.⁹ Viewed statewide, from 2001 to 2007, GIC's health expenditures grew at 7.5% per year on average versus 13.2% for municipalities. If municipal health expenditures had grown at GIC's rate, it would have resulted in a savings of \$500 million in 2007.¹⁰ For more, see *Learning from Springfield*.¹¹
- Finally, we must go beyond the current reforms to the public employee pension system under discussion in the legislature. They will address some of the most egregious loopholes but will fail to address the fundamental problems underlying the system. Just as quickly as loopholes can be closed, others can be opened. The only cure for this is to **require all legislation affecting pensions to contain an accounting of the current cost of any change to benefits and an appropriation from current funds to cover those costs**. The Commonwealth spent more than a billion dollars from its operating budget this year to fund its unfunded pension liability. Reducing the growth of this liability will reduce future expenditures.

For more on Pioneer's works on public pensions, see *Public Pensions: Unfair to State Employees, Unfair to Taxpayers*.¹²

7. Shed Unneeded Assets

State government is the largest landowner of record in the Commonwealth. It has difficulty managing and maintaining a number of assets, many of which have fallen into disuse. **\$30M**

From 2003 to 2005, the Division of Capital Asset Management was given **expanded powers to sell, lease or otherwise dispose of unneeded state assets**. Finding higher and often taxpaying use for unneeded assets brought multiple benefits — for municipalities the transfer of tax-exempt property to productive use, for the state a one-time cash inflow and relief from maintenance expense.

During this period, the state received approximately \$30 million annually. Yet, the Legislature has allowed these powers to lapse and has repeatedly failed to pass viable alternatives. The reasons? Local control and compensation. Legislators want control over the disposition of these properties because, among other things, they want to limit large-scale development of (possibly affordable) housing and other uses they deemed undesirable in their communities.

There have been attempts to compromise on the issue, including offers of right-of-first-refusal to municipalities, involving them in the buyer selection process, and other forms of compensation. Most recently, the Patrick Administration put forward a proposal that appears to incorporate seemingly every possible concession to municipalities, short of outright donation. After four years of obstruction, the Legislature should enact a law that allows for the reasonable disposal of unneeded state property.

For more, see our 2005 Better Government Competition Special Recognition entry, *Accelerating Disposition of Surplus State Property*, submitted by the Massachusetts Division of Capital Asset Management and Maintenance.¹³

9. Carey, Robert L., *Controlling the Cost of Municipal Health Insurance: Lessons from Springfield*, May 2009. Collins Center/Rappaport Institute.

10. Author's Calculations. Based on data from "Increase in Health Insurance Expenditures vs. GIC" spreadsheet on Mass. DOR DLS website.

11. *Learning from Springfield: An Asset Management Approach to Tax Title Collection* (http://pioneerinstitute.org/pdf/090216_pb_panagore_taxtitle.pdf)

12. Pioneer White Paper #30: *Public Pensions: Unfair to State Employees, Unfair to Taxpayers*, Ken Ardon, May 2006. (updated February 2009). (http://pioneerinstitute.org/pdf/090323_public_pensions.pdf)

13. 2005 Better Government Competition Compendium, *Streamlining Government*, Special Recognition Recipient, p. 40.

6. Postpone or Eliminate Speculative, High Cost Initiatives

The current fiscal crisis requires leadership to make hard, long avoided decisions. The time for business as usual is past. The state should prioritize core programs such as K-12 education and public, health and environmental safety. More importantly, it should avoid expansion of new programs.

Many of the new programs proposed or partially implemented over the past few years must be curtailed. For example, the various initiatives of the *Readiness Project* (which carry an estimated annual price tag of \$970 million to \$2.3 billion¹⁴) should be taken off the table. Other initiatives, such as the *Life Sciences tax credit and grants program*, and the *film industry tax credits*, cannot continue even as we sink further and further under a sea of red ink.

South Coast Rail is another project that deserves reconsideration. Although politicians of both parties have pledged to build it, we should stop and consider the project's costs and its relatively limited popularity with potential riders. Right now, the state estimates the line would generate between 1,500 to 4,900 boardings per day (the variation is caused by the different possible configurations of the service¹⁵) even after more than 10 years of operation. Press reports have put the capital cost of the project as high as \$1.4 billion and state planning documents, while vague on the actual price, note that certain options still under consideration may cost up to 50% more than baseline estimates.¹⁶

Even with the generous assumption that only 80% of the boardings are round-trip, the South Coast Rail would only serve 1000 to 3000 passengers daily. And at least some of those would be diverted from other forms of transit. At the high end of the estimate, the per daily passenger capital cost of the project would be in excess of \$450,000.

That astronomical figure also fails to take into consideration that the MBTA is currently carrying a \$160 million deficit for the upcoming fiscal year and cannot finance or operate any expansion project. Meanwhile, the State's capital and operating budgets have not identified funding for these projects beyond relatively small planning grants. The Patrick Administration has been adamant (to the point of publicly disciplining a former Transportation Secretary who strayed off message) about the project's ability to finance itself based on cash flows from new jobs and development. Beyond the tax district and regime associated with the Convention Center Authority, no similar financing, in scope, size and structure, has been attempted in the Commonwealth.

Our resources are limited and, as a result, there are a number of proposed projects and programs that will never occur. We should be honest with ourselves and, more importantly, with taxpayers.

5. Leverage Low Cost Policies

Without reform, the fiscal crisis could translate into underfunded core services, such as education, public safety and programs for the poor. For that reason, attempts to manage state government more efficiently will require expanding programs that have proven effective and, maybe more importantly, cost-effective, rather than launching new ones. While there are a number of successful programs operating currently, we will limit our list to the following three.

Lift the cap on charter schools: One component of the Governor's Readiness agenda for education, with its price tag of between \$970 million and \$2.3 billion, are Readiness schools. These new schools would be run by independent operators—groups of teachers, existing charter school organizations, or for-profit education companies—under the supervision of local

14. *Education in Massachusetts: Governor Patrick's Education Proposals and the Current State of Massachusetts Primary and Secondary Education Funding*, January 21, 2008, Massachusetts Budget and Policy Center.

15. Table 4, CTPS Memorandum, South Coast Rail Travel Demand Analysis Results.

16. Figure 4-34, South Coast Rail Environmental Notification Form.

school committees, and would be freed from some of the bureaucratic red tape that currently constrains district schools.

Allowing schools the flexibility to better manage themselves is an innovation Pioneer has long advocated. But while we expect Readiness schools will cost no more than charter schools, the question is whether they will be as successful. Experience suggests they won't. Readiness schools are hardly distinguishable from Horace Mann charter schools, which have not performed as well as Commonwealth charter schools.

In fact, the data on Commonwealth charter schools are overwhelming. A recent Boston Foundation report highlighted the success the city's charter schools have had closing the achievement gap. So much so, we can reasonably start referring to another achievement gap: that between students who attend charter schools and those who remain mired in our underperforming district schools.

In fact, recognizing the success of Commonwealth charter schools, the Administration has noted that their operators are eligible to create the new Readiness schools. If successful operators of Commonwealth charter schools can create Readiness schools, why not simply let them create more charter schools? That is, rather than create a whole new category of school, why not simply replicate what works?

For more, see our study, *Charter Public School Operations, Funding, and Financial Accountability*.¹⁷

Align district curricula: A 2006 Pioneer study of 76 school districts revealed that 58 percent had not yet aligned their local curricula with the Commonwealth's frameworks, as prescribed by law. Since MCAS exams are based on the material included in the frameworks, the results mean that 16 years after passage of education reform, students in

these districts are still being tested on material they haven't learned in class.

The failure to align local curricula is, perhaps unsurprisingly, most prevalent in our underperforming school districts. Massachusetts' curriculum frameworks are considered among the best in the country. All of our children, particularly our most vulnerable, deserve access to their rich, liberal-arts content. Aligning local curricula with state standards requires little more than the will to do it. It is a small, but relatively easy step we can take to improve student performance and move more urgently to close the achievement gap.

For more, see *Education Reform in Massachusetts: Aligning District Curricula with State Frameworks*.¹⁸

Consolidate grant programs: On top of local and Chapter 70 aid, the state usually provides about \$50 to \$60 million annually in grants to cities and towns to support housing, transportation and environmental efforts. Too often this additional assistance is uncoordinated and therefore not as effective as it could be, particularly in our Middle Cities such as Springfield, Fall River and Lawrence.

State offices offering grants to cities and towns run into double digits, meaning that municipalities have to dedicate far too much time (sometimes years) and too many resources to cobbling together various grants that will allow a single project to move forward. Moreover, the grants are then often diffused across too broad an area, thus diluting their effectiveness.

Simple innovations could enhance the ease and impact of the grant process. For example, we should designate a single point of contact for local officials to process grants through the state, and offer in exchange for local reforms (from pension and health insurance purchasing to planning and permitting reforms) larger block grants that can be used within

17. *Charter Public School Operations, Funding, and Financial Accountability*. (http://www.pioneerinstitute.org/pdf/06_04_chartschool2.pdf)

18. *Education Reform in Massachusetts: Aligning District Curricula with State Frameworks*. (http://www.pioneerinstitute.org/pdf/06_curriculum%20paper_final.pdf)

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anchor neighborhoods to refurbish public parks, sidewalks and deteriorated housing stock, and to augment targeted community policing.

For more, see pages 42-46 of our study, *Rehabbing Urban Redevelopment*.¹⁹

4. Reengineer Existing Systems

A budget crisis provides an opportunity to reassess not only what services government provides but how it provides them. One area in particular need of systemic reform, the single largest area of state spending in fact, is Medicaid. **\$690M+**

An analysis of the MassHealth Medicaid managed care program²⁰ indicates that state officials should **enroll all Medicaid members currently receiving full benefits into the state's managed care program**. Medicaid Managed Care Organizations (MMCOs) offer MassHealth members access to more benefits, services and programs than currently available through the Primary Care Clinician (PCC) Plan. Through preventive care and chronic disease management programs, MMCOs offer a quality and access advantage for the MassHealth population that is compelling, particularly for MassHealth's disabled members.

Furthermore, there are obvious fiscal advantages to enrolling Medicaid members into an all-managed care model. The analysis cited above indicates the Commonwealth would save between \$690 million and \$1.05 billion between fiscal years 2009 and 2013. These savings would result from the MMCO's lower costs, the elimination of the inefficient PCC Plan and attendant investment requirements and other administrative cost savings.

If you would like to see a study, not performed by Pioneer, on this topic, please contact us.

3. Strengthen Your Relationship With Your Best Customers

Massachusetts seems to go out of its way sometimes to deter job-creating firms and high net-worth individuals from locating here. Yearly 'loophole closures', code for business tax increases, are used to fill budget gaps. Advocates push for graduated income taxes. The results are unsurprising – CEOs and CFOs consistently rate Massachusetts as one of the least friendly places to do business. CEO Magazine's annual survey of chief executives places Massachusetts 47th in their ranking of the best and worst states to do business (up from 49th four years ago).²¹ Similarly, a 2009 survey of CFOs ranks Massachusetts as being only second to California among the least fair and most unpredictable tax environments.²²

The Commonwealth's hostile attitude to business is reflected in these rankings. But this attitude ignores our overwhelming reliance on a select group of wealthy and well-paid taxpayers. Roughly 9,500 high net-worth individuals (defined as having adjusted gross income in excess of \$1 million) paid almost a billion dollars of capital gains taxes in 2006, well over half the total collected.²³

Similarly, higher income taxpayers (defined as having incomes above \$100,001) saw their share of total income taxes rise from 47% to 65% between 1997 and 2006.²⁴

These high-income earners are not the problem, they are part of the solution. Our task is to create a business and political environment that attracts the businesses and well-compensated employees who make up our tax base. Ironically, doing this doesn't require action. It requires inaction.

Stop aggressively pursuing new forms of corporate taxation. Stop using the environmental and land-use regulatory processes to impede business growth. Stop

19. *Rehabbing Urban Redevelopment*. (http://www.pioneerinstitute.org/pdf/07_urban_development.pdf)

20. *Managed Care: Improving Quality for MassHealth Members, Improving Value for the Commonwealth*, December 2007, authored by various healthcare entities.

21. *CEOs Select Best, Worst States for Job Growth and Business*, CEO Magazine, January/February 2009.

22. O'Sullivan, Kate, *The Tax Man Cometh*, CFO Magazine, May 2009.

23. Huff, Cam, *Capital Gains: Avoiding Harm to the State Budget*, MassINC Policy Brief, December 2008. See Figure 10.

24. 2008 CAFR. Pg. 168.

the seemingly arbitrary enforcement and interpretation of tax policy. Stop promoting the graduated income tax.

2. Eliminate or Replace Non-Core, Duplicative or Inefficient Services

The Commonwealth should soberly assess what services it should provide (with a corresponding analysis of whether to provide them directly or through private providers) and what it should cease providing. **\$12M+**

We put forward as examples of areas where the state can cut costs without seriously affecting Massachusetts' citizens the following (a fuller list can be found in *Hard Decisions, Needed Leadership*.²⁵

- **Eliminate dual system of incarceration and release monitoring:** Between the Department of Corrections and the various Sheriffs, the Commonwealth spends over \$700 million operating multiple prison, jail, and correctional facilities as well as release monitoring programs. Consolidating these functions would provide the opportunity for significant savings.
- **Eliminate outdated distribution of court personnel:** The distribution of court facilities is based on colonial-era settlement patterns. The compensation for court personnel is micromanaged through legislative statute. While improving, staffing at our courthouses still defies standard management metrics. Closing certain low-volume courthouses and implementing data-driven staffing models for the entire court system would save tens of millions of dollars.
- **Ponkapoag and Leo Martin Golf Courses:** That the state owns and operates two golf courses, which require extensive capital improvements,

seems outrageous when the most vulnerable among us are facing cuts. Moreover, a state with more than 250 public courses (that's one for every 25,000 citizens) hardly needs to operate courses as a public convenience. The state could avoid future capital costs by selling these assets.

- **The State House Library:** The State spends more than a million dollars annually on this little-used facility. This spending should be cut or replaced with a similar investment in technology and imaging to make important documents available to a broader constituency. The practice of warehousing little-used archives in scarce space in Downtown Boston is costly and wasteful.
- **Commonwealth Museum and Archives:** Again, the State spends more than a million of dollars to operate a little-used facility.

1. Reengineer Systems To Avoid A Reoccurrence of the Current Crisis

Despite the need to focus on the immediate crisis, the Commonwealth should also take the opportunity to put processes in place to avoid a recurrence of these problems in the future. Those processes should include:

- **Cap Spending Increases:** State budgetary expenditures over the past ten years have grown at an annual rate of 5%, peaking in 2000 and 2008 at 20% and 12% respectively. This growth is faster than the growth in the state's GDP and per capita income. These increases build up an inflexible fixed cost base and create unsustainable momentum for cost increases that result in so-called 'maintenance budgets' (i.e. the amount needed merely to sustain the level of the previous year's services) that consume even modest increases in revenue. State spending should be constrained by growth consistent with our economy, not the much

25. *Hard Decisions, Needed Leadership* (see footnote 2).

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more volatile levels of tax revenue.

- ***Segregate of Capital Gains Funds in a absolute and durable way:*** Our reliance on capital gains, which are far more volatile than income taxes, creates budgetary crises during economic downturns when capital gains decline precipitously. A recent policy brief by MassINC puts forward some proposals for mitigating this problem and Governor Patrick's House 1 budget contains policy provisions to address the issue. The most sensible of these seeks to better track capital gains funds as they are received, set a maximum forecast for budgeting purposes, and redirect any receipts above that maximum into a dedicated fund.
- ***Stop Spending Emergency Funds for Non-Emergencies:*** During the last several budget cycles, when state revenues were healthy, the Legislature used stabilization funds for spending beyond available revenues. In addition, a complex network of funds and subfunds were created to consume much of the available year-end surplus that would have reverted to the Stabilization Fund. So-called 'Rainy Day funds' should be used only when it's raining. If the consensus revenue process is flawed, it should be fixed. Using Rainy Day Funds to plug perceived errors in revenue projections is inappropriate.

Conclusion

State leaders have lamented that the fiscal crisis forced the Legislature to raise taxes and make cuts to core services. That response ignores reality: Many common-sense actions that could reap hundreds of millions of dollars in savings remain unexplored. The rapid speed with which members of each branch of the Legislature voted to raise taxes in a recession represents a failure of political will and imagination. It will result in the loss of private sector jobs and a

further decline in our long-term competitiveness. Citizens, families and businesses across the state deserve better. As we navigate a time of great economic peril, the Legislature must change the way our government does business.



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