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Governors' Initiatives in 2005: Facing Up to the Problem?

By Katherine Willoughby, Georgia State University

State governors' loathing of tax increases is never more apparent than in this year's state of the state addresses. In 2005, most governors are promoting economic development through tax cuts and credits in order to be able to light up an "open for business" sign in their state. Many governors are also calling for spending reductions and/or agency and program reorientations or reorganizations in order to reach budget balance.

Introduction

Last year, governors' addresses to their citizens about state fiscal environments were somber, "less dire" than in 2003, but "no less worrisome." This year, governors are still hesitant to claim seeing more than some clouds parting to reveal a bit of blue in their fiscal skies.[1] In the words of Nebraska's governor, "the budget proposal before you reflects both optimism and caution." Idaho's governor is equally cautious, "even with a conservative spending plan, and the benefit of year-end surpluses, we may very well find ourselves with a shortfall in FY2007." The bulk of worry rests with ever increasing Medicaid costs. Thus, it is not surprising that a prominent theme of state government chief executives in 2005 is change. South Carolina's governor speaks for many regarding the future of the states, "to prosper and to thrive economically and academically, things have to change. That has to be our path." While these chief executives have laid out a profusion of tax and spend ideas to reach budget balance, focused attention seems directed mostly to the spending side of the state budget equation. That is, governors in 2005 are claiming out of control spending as the biggest fiscal varmint.

As expected, most state of the state addresses begin with a litany of successes and changes realized in fiscal 2004 for which governors are claiming credit. Many drum relevant statistics—that personal income is up, jobs are on the increase, wages are growing, and that tourism and/or housing starts are on the rise. Still, there is hesitancy in declaring that state fiscal skies are clear. Common refrains include, "We should do more" or "We should do better." In the words of New Hampshire's governor, "I am not here to advocate for more government, but better government, and that starts with open, ethical, honest government." As noted above, a primary view of governors is that states have a spending problem and not a revenue problem. In Vermont, a state with a fairly diversified tax structure and one that is very inclusive of citizens in budgetary decisions, Gov. Jim Douglas declares that "it is important to acknowledge that we did not get in this situation because Vermonters are taxed too little; we're here because government has spent too much." Indiana's governor is even more direct, "state government is too expensive, too antique in its practices, too indifferent to real, provable results, and in place after place after place, too slow . . . overhanging all our difficulties is the simple, brute fact that our state's public finances are in ruin. We have outspent our income year after year." Minnesota's Gov. Tim Pawlenty concurs that "[s]ome will argue that we should raise taxes rather than slow the growth in these programs. That is simply unrealistic. Income tax revenues would have to double every eight years to pay for these programs at their current rate of growth. We must restrain the growth in these programs to sustainable levels by wisely and humanely changing them so they are comparable to surrounding states, and more focused on those with the fewest resources and the greatest needs."

There are a few exceptions to the focus on spending. South Dakota's Gov. Mike Rounds points out that "some people have falsely claimed that the structural deficit [in this state] was caused because past legislatures just wanted to spend more money. The truth is that the structural deficit was caused by the repeal of the inheritance tax, the loss of gold mining taxes and the repeal of the transportation tax. All that added up to $39 million less in ongoing taxes collected every year." Some governors are emphasizing both sides of the budget equation as problematic. Perhaps Utah's governor sums up the general tenor of addresses this year. "My administration's policy priorities focus on four commonsense fundamentals—economic revitalization, education, quality of life and governance. . . . To that end, we need a tax policy that is not only friendly to our citizens, but also creates a competitive environment for business. Business as usual will leave us behind our neighboring states."

Tax Collections and Changes, Then and Now

Table 1 illustrates a comparison of state tax proportions in 1994 and 2004. Subtle change in proportions over time indicates that states now depend equally on general sales and personal income taxes. The category "All other taxes" comprises a larger share of total tax proportion in the states than 10 years ago. Continued chipping away at business-related taxes in the last decade is most clearly evidenced in the decline of the corporate income tax as a significant state tax resource.

In truth, 2004 actual revenues bested 2004 estimates in most states. Still, following passage of fiscal 2005 budgets, virtually

Table 1 State Tax Collections by Type of Tax, 1994 and 2004, 3rd Quarter

Tax	1994	2004
General sales and gross receipts	34.6%	33.8%
Individual income tax	31.5	33.5
Motor fuel sales	7.1	5.8
Corporate net income	6.6	5.5
Motor vehicles	3.3	3.0
Other sales and gross receipts	2.3	2.1
Tobacco products	2.0	2.1
Insurance	2.0	2.0
All other taxes including: property tax, public utilities, pari-mutuels, amusements, beverage and other licenses, death, gift and severance taxes, taxes on document and stock transactions	10.4	12.3

Source: Table 3: State Tax Collections by State and Type of Tax.

Data available in excel files qtx043t3 and qtx943t3 at http://www.census.gov/govs/www.qtax.html. Accessed on March 4, 2005.

half (24) of the states instituted tax and fee changes expected to yield $3.5 billion more in revenues. The breakdown of revenue changes to realize this $3.5 billion includes:

- 25 percent from changes to cigarette/tobacco taxes
- 20 percent from changes to sales taxes
- 20 percent from additions or changes to other taxes[2]
- 14 percent from changes to or institution of new fees
- 12 percent from changes to personal income taxes
- 8 percent from changes to corporate income taxes
- 1 percent each from changes to taxes on motor fuels and alcohol[3]

As illustrated above, collectively the states have relied most heavily on "sin" taxes for added revenue—the greatest proportion of new revenue in 2005 is expected from tax and fee increases related to cigarettes and tobacco products. Also, "collections of sales, personal income, and corporate income taxes are projected to increase by 7.1 percent over prior year tax collections in fiscal 2005, based on enacted budgets" (NASBO, ix). After two years of real decline in state general funds in 2002 and 2003, and no growth in 2004, the real increase of 1.8 percent in 2005 is heartening (NASBO, p. 4). On the other hand, 2005 state expenditures have increased by 4.5 percent above prior years. And total year-end balances as a percent of expenditures are expected to remain below those in 2004; in 2005, this ratio is expected to be 3.4 percent, compared to 4.8 percent in 2004.

State Budget Balancing Measures

The 2005 Government Performance Project (GPP)[4] examined states regarding their financial management capacities. The project's recent survey results confirm how difficult it has been for states to balance in the last few years. When asked about the actions taken to stay on budget in recent years, states responded to using a multitude of revenue and expenditure actions. Table 2 illustrates that in 2003 more than half of states used one-time revenues, non-routine transfers, carry-forward balances, and accessed stabilization or rainy day funds to pump up revenues. By 2004, in addition to using windfall revenues, making non-routine transfers and increasing fees or charges, more than half of states also increased tax collection enforcement efforts, while a third of states changed tax structures and refinanced debt. By 2004, more states increased the sale of assets, while fewer made use of rainy day funds or drew down other funds to reach balance.

Other revenue generating strategies used in either 2003 or 2004 include changing tax structures, using additional debt financing or conducting debt refinancing, and tapping rainy day or budget stabilization funds. A number of states also indicate using different methods not listed on the survey to increase revenues in these two years. Such methods include:

- Initiating tax amnesty programs;
- Accelerating tax payments (specifically, withholding);
- Pausing tax rate reductions and setting rates to begin later in the year;
- Joining a multistate lottery consortium;
- Adding new games to the state's lottery;

Table 2 State Revenue Generating Strategies in Fiscal Years 2003 and 2004

Revenue generating strategy (a)	Fiscal year 2003	Fiscal year 2004
Use one-time/windfall revenue	53%	69%
Increase tax collection enforcement	41	59
Use non-routine transfers from other fund	63	55
Increase and/or add fees/charges	49	51
Use carry-forward balances in the general fund	51	39
Change tax structure to generate revenue increase	27	37
Conduct debt refinancing	31	35
Use budget stabilization or rainy day fund	51	24
Conduct sale of assets	14	22
Use additional debt financing	16	14
Draw down other contingency funds	22	8
Increase short-term borrowing	6	6

Source: Government Performance Project 2005 State Survey, http://results.gpponline.org.

Note: To balance budgets many states make changes to revenues, expenditures and debt. States indicated that the following revenue actions were used to realize a balanced budget at the end of each fiscal year noted (percent of states responding that action was used).

Key: (a) Data was available for 49 states.

Table 3 State Expenditure Reduction Measures in Fiscal Years 2003 and 2004

Expenditure strategy (a)	Fiscal year 2003	Fiscal year 2004
Make targeted spending cuts	80%	71%
Conduct across-the-board spending cuts	71	49
Initiate program reorganization	42	49
Freeze hiring	62	40
Cut local aid	29	27
Implement privatization initiatives	13	18
Initiate layoffs	24	16
Reduce contribution to pension funds	16	11
Delay payments for purchases	18	9

Source: Government Performance Project 2005 State Survey, http://results.gpponline.org

Note: To balance budgets many states make changes to revenues, expenditures and debt. States indicated that the following expenditure actions were used to realize a balanced budget at the end of each fiscal year noted (percent of states responding that action was used).

Key: (a) Data was available for 45 states.

- Securitizing tobacco settlement proceeds;
- Diverting tobacco settlement proceeds to the general fund; and
- Suspending implementation of voter initiatives to divert general funds elsewhere.

States also engaged a multitude of measures to reduce spending in these years. As illustrated in Table 3, the most common expenditure reduction strategy used is simply cutting spending—most likely in a targeted way, but across the board as well. A majority (60 percent) of states conducted a hiring freeze in 2003; just 38 percent of states claimed use of this measure in 2004. Many states, although not a majority, also conducted program reorganizations in both years to reduce costs. Cutting aid to local governments was a fairly popular method of reducing or delaying state expenditures in both years—over a quarter of states cut local aid in 2003 and 2004. Close to a quarter of states indicate initiating layoffs in 2003; down to 15 percent of states indicating layoffs by 2004. All of the other methods for reining in spending were used in both years, even if by just a few states. A number of states also indicate using methods not listed to reduce expenditures in these two years. Such methods include:

- Initiating early retirement program(s);
- Freezing merit raises of state employees; suspending annual employee cost of living adjustments;
- Terminating and/or amending state contracts;
- Eliminating funding to nonessential appropriations;
- Suspending transfers from the general fund;
- Delaying scheduled payments to K–12 schools and payments to counties for property tax relief;
- Lapsing unspent agency appropriations to the General Fund and not allowing appropriations to be carried forward;
- Requiring or increasing employee contributions to health care costs; placing HMO plans into cost/efficiency tiers; engaging a pharmacy-benefits manager;
- Establishing holidays on state payments for state employee sick leave conversion liability; and
- Implementing monthly agency spending targets.

Recurrent Themes

Recurrent themes throughout the 2005 gubernatorial addresses include increasing and/or creating state relief programs for the military—through tuition assistance, increased death benefit payments, and/or new programs and services specifically for veterans and their families. For example, the governor of Oklahoma proposes "Operation Homefront" to provide "a tax exemption for military pension income for all veterans and purchase a $250,000 life insurance policy for every Guardsman." Some state legislatures are beginning to respond accordingly by passing part or all of such initiatives. Governors also brought up the Indian Ocean tsunami disaster and either recognized their state's support thus far or pledged additional relief to this part of the world.

Most governors recognize the influence of the "global economy" on the direction of their state, many couching their initiatives as methods of engagement with this economy. Minnesota's governor explains, "We all need to grasp the importance of the Rochester model. They're a successful global competitor. Why? Because they have seamlessly integrated science, technology, infrastructure, entrepreneurship, a partnering role for government, and lots and lots of hard work. Global competitiveness is Minnesota's strategic objective. We have lots of work to do to get us there." This theme coincides with governors' concerns related to economic development, job growth and specifically the out-migration of their young citizens. Many are advertising their states as "open for business." Others seek to initiate and/or strengthen programs that make it attractive for native-born citizens to settle in state and pursue productive work. For example, Maine's governor suggests an "aggressive telecommunications strategy" so that every Mainer can "plug into the global economy from their community." Iowa's governor talks of expansion of "Great Places" throughout the state by energizing a consortium of state agencies to work together to streamline application processes, better package resources, and target the most innovative communities in the state. In Illinois, the governor is asking for more financial incentives to draw in companies that make homeland security products, as well as support for building a new airport in Peotone to expand air travel into and through the state. New Mexico's Gov. Bill Richardson offers tax exemptions for that state's aviation industry, and he seeks to create the New Mexico Spaceport Authority to further develop this industry. In general, recommended education programs, research and development and other initiatives mentioned are geared to stemming out-migration as well as advancing in-migration. New York's Gov. George Pataki wants New York to become first in insourcing jobs. "Let's focus not just on keeping jobs, but on attracting new jobs and new investments from around the world."

As noted earlier, governors are very cognizant of the continued mismatch between state revenues and expenditures—many consider that it is not taxes that are too low, but spending that is too high. This is a scenario that most recognize cannot continue without significant consequences to the wealth of states and well-being of citizens. Minnesota's governor emphasizes that "keeping a lid on taxes is not just good for the taxpayer. It's a powerful way to force government to be more accountable, set priorities and spend smarter." Most point to Medicaid as the primary spending culprit. Arkansas Gov. Mike Huckabee paints a picture evidenced in most

states—almost all (91 percent) of the state's general revenue funds Medicaid, education and prisons. Thus, many governors expressed worry about how to fulfill Medicaid commitments, both now and in the future. Vermont's governor characterizes this area of state budgets as "growing at an unsustainable rate." Gov. Mitch Daniels proposes big changes to Medicaid in Indiana. "We will slow this unsustainable growth rate by half. Over time, we will rebuild a broken, antiquated system so that it delivers better care to those who cannot afford to care for themselves, while remembering that taxpayers deserve compassion too."

State chief executives continue to have management reform on their minds as well. Washington's governor proposes "legislation to establish a new government management accountability and performance approach to government—GMAP for short." In this state—already well known for doing an excellent job managing information, the mantra "We should do better" helps focus on holding state agencies accountable for achieving results effectively and efficiently. Similarly, Oregon's governor claims to have thrown out the old rulebook—"This is not a current services budget. It funds programs based on whether they produce measurable outcomes." This budget also boasts a spending limitation and rainy day fund. According to Gov. Ted Kulongoski, "in 2005, we need to think and act differently."

Governors from both Rhode Island and South Dakota propose a red tape reduction task force to help eliminate barriers to conducting business and streamline government operations. New Hampshire's governor has been busy "zero-basing every department budget," requiring justification to the penny. Michigan's Gov. Jennifer Granholm mentions state reorganization as well as the abolishment of numerous boards and commissions as paths to greater efficiency. New York's governor is also asking to eliminate or consolidate "hundreds of commissions, task forces, boards and authorities that have been established over the course of many decades." In addition, Gov. Pataki asks that the state pass its budget on time—an important component of public budgeting transparency. Interestingly, Rhode Island's governor is throwing "open the doors of the state to all citizens who want to participate" by asking Rhode Islanders to apply for appointments on numerous boards and commissions in that state.

Other efficiency efforts focus on specific management areas. Nebraska's governor suggests advancing technology and "striving to be a customer friendly, customer responsive government in everything we do, from issuing permits to answering telephones." Efficiency efforts promoted by Tennessee's chief executive run the gamut from revamping the issuance and renewal of driver's licenses to continuing the overhaul of Medicaid. Missouri's governor presents a budget that includes a reduction of more than 1,000 full-time state positions. Illinois' governor wants the state's Finance Authority to "look at new ways to provide financing for wind farms."

Reorganization ideas abound as well. Delaware's governor proposes a significant reorganization, "centralizing the administrative and support functions of state government in one agency." West Virginia's Gov. Joe Manchin wants reorganization in that state "with the goal of being more accountable for our actions and more coordinated in our economic development efforts." This governor also seeks pension reform to remedy the fact that the state is currently spending over 11 percent of its revenues annually on pension liabilities. Specifically, Gov. Manchin is asking citizens to support a referendum to establish "a fixed mortgage payment to pay off unfunded liabilities." Gov. Daniels is calling for dramatic reorganization of Indiana's bureaucracy and has appointed the state's first inspector general to ferret out government waste. New Jersey's governor is creating an inspector general too. Maine's Gov. John Baldacci seeks to "consolidate financial, information technology, payroll, human resources, and administrative hearings services" to save the state $11 million in the next two years.

Georgia's governor has appointed a state property officer to conduct a complete inventory of and better manage state property. This governor has also invested in a business approach to government through engagement of a Commission for New Georgia which he touts in his address. This group of business and policy leaders feeds ideas about good management practices to Gov. Perdue. As well, the governor has reorganized his office, with an eye toward a state government that is customer service oriented. Similarly, Wisconsin's governor is redesigning the way that state conducts business. "We're rebidding costly state contracts. . . . We're trimming the state's vehicle fleet back to its level a decade ago. . . . For the first time, we're asking state employees to pay a portion of their health insurance. . . . We've cut discretionary pay bonuses by 92 percent. We've eliminated more than 1,500 cell phones and sold seven airplanes." In Montana, the governor has formed a performance review committee to ask citizens and state employees alike for their ideas on how to deliver state services more efficiently.

In the area of education, specifically, many different efficiency measures are being touted by governors. For example, more than a few mention developing "centers of excellence" in state university systems, possibly requiring increased tuition to do so. Colorado's example of funding students, rather than academic institutions is another way of thinking about changed funding and funding channels for education in states. Indiana's governor has called for a moratorium on school building to support "instruction before construction." In Michigan, the governor is asking the state's universities to institute credit amnesty—"accept old credits of adults who re-enroll within the next three years to finish their degrees." Governors also talked of support for student receipt of college credit in high school to more quickly advance students through educational systems and on to viable careers. In Arizona, the governor spoke of all day kindergarten, moving students beyond high school to enhanced career and technical education—highlighting a renewed interest in states about community and technical colleges—and commitment to funding a medical school collaborative.

Revenue Ideas

Budget worries have not stemmed gubernatorial ideas about cutting taxes. Idaho's Gov. Dirk Kempthorne outlines a very specific tax incentive package for businesses. If a company in this state makes certain investments within a given time frame, the governor proposes:

- A doubling of the investment tax credit to six percent for a five-year period;
- Removing the 50-percent limit on the investment tax credit;

- An enhanced jobs tax credit;
- A new income tax credit for real property improvement;
- Property tax abatement on qualified new construction; and
- Sales tax abatement on construction materials.

This governor also recommends that the state consider increasing the level of bonding to support capital investment. Idaho traditionally maintains a very low debt level compared to other states. Maine's governor joins Idaho's in looking to increased use of debt, in Maine's case, to support biomedical research and collaboration.

South Carolina's governor is depending upon reduction of the income tax to make that state more competitive. Pennsylvania's Gov. Edward Rendell is focusing on reducing the corporate income tax rate and modernizing the business tax structure of the Commonwealth. Tax credits are being recommended in New York, despite the fact that as Gov. Pataki notes, "New Yorkers' tax burden is $15 billion less today because of the broad, sweeping, fundamental changes we made in our tax code beginning in 1995." The governor is also recommending acceleration of the phase out of the state's temporary personal income tax increase. And, his plan includes property tax relief. The governor of Texas has a "game plan" to eliminate that state's corporate tax over the next few years, combined "with a short-term strategy on reducing the food tax and change income taxes." Washington's governor is calling for tax relief for small and startup enterprises.

Some states are taking advantage of increased revenues expected this year. In Alaska, the governor has proposed gas and oil credits for new fields. This state is experiencing a significant windfall in revenues for fiscal 2005, given high oil prices. This governor proposes to use the windfall for education and nonrecurring expenditures, expressing that the increase in revenues should be considered "temporary."

Wyoming and Montana are other states that have flush revenues, comparatively speaking. According to Wyoming's Gov. Dave Freudenthal, "We have money. Our revenues are remarkable and our prospects are bright. Money should not, and must not, change our commitment to solving problems and building this state. . . . The amount of money available changes the rate at which we can convert our values into action—it should not change our values." Hawaii's governor wants "to use some of the revenues generated by [the state's] recent prosperity to pay for a modest yet important $63 million tax cut over the next two years for individuals and families with low to moderate incomes." Gov. Linda Lingle calculates that this tax cut would mean that "27,000 people will no longer have to file state tax returns, and 78,000 more will see their taxes reduced." She is also proposing food and medical tax credits, credits to advance partnerships between the state university and business, a reduction in the unemployment insurance tax wage base, a tax credit for the purchase of long-term care insurance, and greater flexibility for the state's department of commerce to institute more cuts to fees and assessments.

New Mexico's Gov. Richardson seeks to make a difference through tax cuts that include sales tax holidays, income tax exemptions, and eliminating the single parent penalty. Mississippi's governor just asks to reform the unemployment tax formula—"Over the last 20 years, because of flaws in the formula used in our state, we have been collecting much, much more in unemployment taxes than is needed to pay unemployment benefits." Ohio's governor has a tax reform plan to "cut personal income tax rates by 21 percent over five years, eliminate state income tax for Ohioans making less than $10,000 a year, and phasing out the tax on equipment and inventory and corporate tax." This plan is expected to reduce state revenues by $800 million in the next two years. The governor is asking for "restrained spending and reduced Medicaid growth" to support this tax reform package. Rhode Island's governor has presented a five-year tax reduction plan that includes "new lottery revenues dedicated to direct property tax relief."

Kentucky's governor is asking for extensive tax modernization—suggesting an income tax rate reduction along with numerous tax credits—in construction, research and development, Brownfields, clean coal technology and other environmentally related areas—historic preservation credits, and tuition tax credits. Gov. Granholm recommended the Michigan Jobs and Investment Act which, if enacted, would mean that "three out of four business tax payers will pay significantly less." Maryland's governor is encouraging business growth, specifically filmmaking "by offering film companies a rebate on the first $25,000 of wages paid to production employees on locations in the state." New Mexico's governor also seeks an extension of that state's 15-percent refund on filming expenses. Maryland's chief executive is also promoting extension of the state's research and development tax credit as well as addition of an "entrepreneurial investment technology tax credit" to advance business in-migration to the state.

Governors are marking the property tax for reform too. Missouri's governor suggests that school districts be allowed to use a sales or income tax to alleviate heavy dependence on the property tax. Maine's governor addressed the citizens of that state after signing into law government and property tax reforms that establish spending caps and expand property tax relief. Wisconsin's governor proposes simplifying the form used for the homestead credit—from 17 to one page. Also, "instead of just giving incentives to achieve a target property tax increase, we will provide bonuses for municipalities and counties that hold their property taxes even lower." In Texas, the governor agrees with property tax relief, taking it further, "It is time to cut property taxes for hardworking people of Texas. In fact, let's not only give Texans property tax relief . . . let's give them appraisal relief too. . . . Let's cap appraisals at three percent." Gov. Rick Perry seeks new revenues by instituting a "broad-based business tax that is fairly distributed, assessed at a low rate and reflects our modern economy."

Iowa's governor is asking for a tax rollback as well as a cap on future property tax increases. This governor also seeks an increase in the cigarette and tobacco related taxes, to be earmarked for health care. Kentucky's governor has requested an increase in the cigarette tax as "a matter of fairness and sound public policy." Even North Carolina's Gov. Michael Easley states that "the time has come to significantly increase the cigarette tax and reduce teen smoking."

Other interesting revenue generating strategies mentioned include Gov. Daniels' call to "the most fortunate among us, those citizens earning over $100,000 per year, for one year, to pay an additional one percent on the income they receive" to help balance the budget. Maryland's governor is asking for "a fully phased in slots program" that could mean more than $800 million in new

revenue to the state annually. California's governor is presently stumping for a referendum similar to the federal government's Gramm-Rudman-Hollings sequester law (Emergency Deficit Control Act of 1985). In a special legislative session, Gov. Arnold Schwarzenegger says, "I will submit to you legislation that cuts expenditures across the board when they grow above revenues. We must take back responsibility for the budget. We must have a new approach that overrides the formulas, overrides the special interests and overrides the forces that have turned some of you from legislators into clerks." The governor also characterized the state's pension system as "out of control," calling for movement from a defined benefit to a defined contribution system. Colorado's governor seeks fiscal redress through the "specific provisions of TABOR" to support the state's transportation infrastructure, higher education and public safety needs. "This plan also proposed tax relief for working families. We should take a commonsense step to prevent the government from collecting dollars it can't use. Let's roll the personal income tax rate back to 4.5 percent."

Conclusion

While governors' tax and other revenue generating strategies generate the most interest, many other areas of policy interest were mentioned in this year's addresses. Governors also talked about:

- Cost containment of prescription drugs;
- Reducing the opportunities to develop and deal methamphetamines;
- Changing funding relationships with local governments;
- Advancing protection of natural resources, the environment, development of renewable energy resources, and water conservation;
- Strengthening government ethics law;
- Initiating elections reform;
- Negotiating related to tribal gaming;
- Advancing homeland security and public safety; and
- Legislating tort reform.

The Cato Institute's most recent fiscal policy report card[5] on U.S. governors finds most to be performing at an average to below average level, given their measure of excellence as keeping tax rates low and constraining spending. More than half (27) of governors received a grade of "C" or lower according to the Institute's fiscal policy measurement. Only four governors, two "freshmen" and two "seniors," received an "A" for promoting low tax rates and spending growth—those from California, Colorado, Montana and New Hampshire.

Certainly we can see that tax reform and, in particular, lowering taxes remains on the minds of most governors. And, many, if not most states have tinkered with their tax structures in the last few years. Finally, most states have employed many different revenue generating methods in the last two years in attempts to keep pace with spending. Perhaps North Dakota illustrates the fine line that governors walk concerning the need to increase revenues, support economic development, and manage spending commitments. North Dakota's Gov. John Hoeven (who received a "B" from the Cato Institute Study) explains this state's present good fortune. "As a result of growing revenues and good fiscal management, we will close this biennium with an ending fund balance of nearly $130 million, the largest in 20 years. And our state's revenues are projected to be strong through the next biennium. We have achieved these results through aggressive economic development efforts and we have achieved them without a tax increase." Going forward, this governor is calling for "more venture capital and investment tax credits for small businesses, . . . doubling the Homestead Tax Credit and repealing the unemployment insurance offset to Social Security for working seniors."

In light of their typical abhorrence for tax increases, it is hopeful that governors' focus this year is on restraining spending and retooling state government. Clearly, states cannot continue down a road in which revenues are lost (through tax cuts and credits) while spending commitments grow. If governors are going to stick to holding the line on revenues and even to retrenching revenues, then they must look to either increased borrowing to support spending growth or cut spending and/or the commitments that grow spending. Governors seem to be alerting their citizens that they have picked up some fiscal shears and are ready to start using them.

Endnotes

[1]U.S. governors report annually or biennially to their legislatures regarding the fiscal condition of their state, commonwealth or territory. Governors may use their address to lay out their policy and budget agendas for their upcoming or continuing administration. The 2005 state of the state addresses were accessed from January through March 1, 2005 at the National Governors Association Web site: just two states, Florida and Louisiana, did not have the 2005 state of the state addresses on this Web site during this time. All quotes and data presented here are from the addresses available on this Web site, unless otherwise noted.

[2]Other taxes include any taxes not falling into mentioned categories—examples include taxes on nursing homes, gas and oil production, real estate conveyance, live entertainment, research and development and other activities, services and items.

[3]NASBO, *The Fiscal Survey of the States*, (Washington, D.C.: NASBO, December 2004), Table 7: Enacted Fiscal 2005 Revenue Actions by Type of Revenue and Net Increase or Decrease, 10.

[4]The GPP mission is to provide states information that can advance government management to achieve public goals and objectives. The GPP conducts a 50-state survey every few years that assesses states' capacity in managing financial and human resources, information and technology and physical infrastructure. In 2005, the GPP conducted its survey online and integrated work of both academics and journalists to determine grades for states in each of these four areas. Results from this survey are available at www.results.gpponline.org. The GPP is sponsored by a grant from the Pew Charitable Trusts.

[5]Stephen Moore and Stephen Slivinski, "Fiscal Policy Report Card on America's Governors: 2004," *Policy Analysis Report* No. 537, (Washington, D.C.: The Cato Institute, March 2005).

Bio

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