HOT TOPIC: The Economy

State Budget Gaps Continue to Grow

10 Ideas to Help State Budgets

South Dakota Governor Mike Rounds on Prosperity

6 Steps to Healthier Pensions

Has the Stimulus Helped States?

States Race to the Top

This national recession will cost jobs — some of which will not come back. And as those jobs are permanently eliminated from the employment opportunities, other types of jobs have to replace them.

—Governor Mike Rounds

PLUS: Predicting Winners and Losers After the Census

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ON THE COVER
South Dakota Gov. Mike Rounds, CSG’s 2010 national president, pictured in front of his state’s capitol, believes states must refocus on the assets they currently have in order to bring jobs and prosperity. In South Dakota, the state is looking to its agriculture industry—where corn is also used for ethanol. It’s also courting the firearms industry to help meet that goal. See article on page 23.

COVER PHOTO BY LAWRENCE & SCHILLER

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  - Meet Douglas Henry, the longest-serving member of the Tennessee Senate.
It’s the Economy

“Life is divided between the horrible and the miserable.” Woody Allen’s comment could easily apply to the circumstances confronting most state leaders today. These are bleak days for the leaders governing our states and territories. Revenues are falling, needs for services continue to grow and the ability to make ends meet is more elusive than ever. As a Kansas lawmaker, I chaired the committee that wrote the budget and the committee that wrote tax laws. That experience taught me that even in good times it is hard to allocate limited resources to the multitude of interests seeking state support. Often I heard the words of J. Eldon Fields, my freshman political science professor, echoing in my ears. He defined politics as “who gets what, when and how.” That certainly was true during my time working on the state budget and it remains true today.

Although the recession ended as growth spurred by stimulus spending began in the third quarter of 2009, states are still experiencing an unprecedented financial crisis. State tax collections dropped 10.7 percent in the third quarter of 2009—the third consecutive quarter of double-digit revenue decline. And although the second half of 2009 saw growth, another 800,000 jobs were lost.

The elements that generally drive an economic recovery after a recession, increasing jobs, wages, consumer demand, production and sales, have yet to appear. And state revenues usually do not begin to grow for 18 to 24 months following the end of a recession. So it is fair to say for most state leaders, the effects of the recession are far from over.

In this issue of Capitol Ideas we focus on what you have told us is important—the economy and its effect on the states and territories. At The Council of State Governments we are committed to connecting state leaders to the information they need to navigate these difficult times and to the ideas and insights that will inspire transformations and innovations in state government.

Whether it is a state’s unemployment insurance fund, pension plan, correctional system, schools or Medicaid programs—there are simply too many essential government programs that are unsustainable as currently deployed. Fundamental questions about the proper role of government must be examined.

I believe CSG is a great place to start those discussions—and we have plans to do just that. At the request of many state leaders, we will convene the first-ever Economic Summit of the States May 20–23 in New York City. This forum will give our members the chance to learn from one another, hear from top administration officials and have the benefit of experts in the fiscal arena. This is a can’t miss opportunity for state leaders struggling with how to address the immediate budget crisis while reinventing state government into a sustainable, governable process for meeting essential public needs. Registration is available online at www.csg.org/events/2010economicsummit/.

CSG’s National President, South Dakota Gov. Mike Rounds, and CSG’s National Chairman, Kentucky Senate President David Williams, are convening the summit with the goal of finding ways to empower state leaders to lead their states back to prosperity. Like you, they realize even in crisis there are opportunities—we should collectively explore those opportunities to craft a better tomorrow. Please join us for the summit—its success will depend on the participation of a broad cross section of state leaders.

Despite the current challenges, I am optimistic about the future of the states, our nation and CSG. I hold that view because I believe in the strength of our nation to continually reinvent itself. At CSG we look forward to working at your side to make that brighter future a reality.

Very truly yours,

David Adkins
“The worst of the storm has passed.”
—President Barack Obama, discussing the economy in his State of the Union speech Jan. 26

“We’re going to fall off a cliff unless we get our revenues and our expenditures in true sync.”

“We can’t say that state government should be insulated from the same types of things that the private sector’s already seen.”
—Virginia Delegate Christopher Peace, discussing state budget cuts, as quoted in the Henrico Citizen

“(The stimulus) was the catalyst for going from the Great Recession to economic recovery.”
—Mark Zandi, chief economist for Moody’s economy.com, at Governing magazine’s Outlook Conference in February

“The key to economic recovery is our schools.”
—Nevada Assembly Speaker Barbara Buckley, discussing her opposition to additional cuts proposed for the state’s education budget, as quoted by the Associated Press

“Choosing government that is necessary—over government that is merely desired.”
—Arizona Gov. Jan Brewer, discussing tough choices state officials must make, in her State of the State address Jan. 11
New Hampshire Looks for Ways to Cut Corrections Spending

New Hampshire could save millions if it were to drastically change how it handles inmates on probation and parole, according to the AP. Also during that time, the state’s inmate population grew 27 percent, swelling from 2,291 to 2,915, the AP reports.

The rise in corrections costs and the inmate population is because inmates who are on probation or parole and who are sent back to prison make up more than half of the total prison admissions, according to the CSG Justice Center. Inmates returning to prison also often get stuck there due to a lack of resources helping moves back into the community, according to the CSG Justice Center.

New Hampshire Senate President Sylvia Larsen is sponsoring legislation to put the findings from the CSG Justice Center into action, the AP reports. See a perspective on the subject from Larsen on page 34.
The South

WAter WArs
A two-decade-long water dispute among Alabama, Florida and Georgia is still in negotiation. Water released from Georgia’s Lake Lanier is the main resource for Atlanta and other downstream communities and is used to produce electricity in Alabama. Last summer, a federal judge ruled the three states have no legal rights to the water and must agree upon a water-sharing plan.

CREAtInG JOBS
Alabama Gov. Bob Riley has a three-prong “Jumpstarting Jobs” plan, and told The Huntsville Times that although government may not be able to create jobs, “government can at least create an environment” for businesses to grow. The plan includes an income tax credit for employers hiring employees on unemployment benefits, the newspaper reports.

CASInOS In reSOrTS
Florida legislators want to allow full casinos in some of the state’s resorts, according to The Miami Herald. Under the proposal, voters would first have to OK the casinos in local referendums and then a state gaming commission would give out permits, the newspaper reports.

hIGh-teCh JOBS
Kentucky Gov. Steve Beshear announced that nine of the state’s high-tech companies will share nearly $2.2 million in state funds, according to the governor’s office. The incentives are a part of an initiative meant to attract and support high-tech small businesses, according to a press release.

ARKANSANS & THE ECONOMY
According to a poll by Mason-Dixon Polling & Research Inc., 54 percent of Arkansans think the economy is on the wrong track, according to the news Web site, Arkansas News. Thirty-seven percent also believe President Obama’s actions have hurt the nation’s economic situation, according to the poll.

Southern Growth Policies Board Plans Economic Forums

The Southern Growth Policies Board, headquartered in Atlanta, is looking for community leaders to start a conversation on economic challenges facing the region.

The board believes state policymakers can garner information about community ideas and priorities through these conversations; it will also share the results of the community discussions with leaders throughout the South in its 2010 Report on the Future of the South.

The Southern Growth Policies Board provides materials to use during a two-hour discussion, and the forums can be run using a moderator’s guide and discussion guide for citizen participants. That information is available on the board’s Web site, www.southerngrowth.org.

The forums are part of the Southern Growth’s annual Listening to the South initiative. Each year, Southern Growth starts a conversation in the South on an important issue related to economic development through community forums or moderated discussions in communities across the region.

In 2009, for instance, more than 2,300 Southerners participated in community forums, state policy dialogues and an online survey to share their thoughts and opinions on how best to capitalize on the economic development opportunities associated with energy.

To learn more about past forums, visit the Web site at www.southerngrowth.org.

To learn more about planning or moderating a community forum, contact Linda Hoke at (919) 941-5145.

To learn more about these and other developments in the Southern Region, visit: capitolideas.csg.org or www.sclatlanta.org.
**The Midwest**

**HOME SALES**
Bucking the national trend, Chicago-area home sales increased by 33 percent in December 2009, making an optimistic case that 2010 may be a small comeback year for the housing market, according to The Chicago Tribune. Homebuyers are taking advantage of low mortgage interest rates and the extended and expanded federal homebuyer tax credits, the newspaper reports.

**DEMOLISHING FORECLOSED HOMES**
Flint, Mich., received $25 million in federal stimulus funds to demolish, acquire and rehabilitate foreclosed homes in neighborhoods that are in some parts 50 percent or more vacant, according to the Flint Journal. The city will use the money to demolish large concentrations of foreclosed homes to stabilize areas, according to the newspaper.

**UNION MEMBERSHIP**
The portion of workers in Minnesota who are union members dropped to 15.1 percent last year, down from 16.1 percent in 2008, according to the Bureau of Labor Statistics. The state’s unions lost 30,000 members last year, the largest drop since 2005, according to The Pioneer Press in St. Paul, Minn.

**REINJURED WORKERS**
Missouri’s fund that covers claims from workers with previous injuries or conditions who are reinjured on the job is financially troubled, according to the Associated Press. Analysts warned for years the fund was running out of cash, and the state attorney general’s office stopped settling injured workers’ cases last fall, the AP reports.

**PUPPY MILLS**
Dog breeders in Iowa could see increased fees and strict regulations, according to the Quad-City Times in Davenport, Iowa. That’s because legislators are backing a measure meant to crack down on so-called puppy mills that they say often abuse animals, the newspaper reports. Iowa’s 400 licensed breeders produce an estimated 20,000 dogs a year, making it third in the nation, according to the newspaper.

Indiana’s construction industry, battered by the recession, is still recovering at a slow pace, according to the Post-Tribune in Merrillville, Ind.

Anecdotally, Randy Palmateer, business manager and lobbyist for the Northwestern Indiana Building & Construction Trades Council, told the newspaper that 40 percent of his organization’s 30,000 members were unemployed last year. It may be getting a little better, but very slowly.

“We’re probably at 30 percent now. It’s picking up a little,” Palmateer told the newspaper.

Northwest Indiana lost 2,100 construction jobs last year, down 11 percent from the same time a year before, the newspaper reports.

Nationally, a report from the Associated General Contractors of America, said construction employment declined last year in 324 out of 337 metropolitan areas nationwide, according to the newspaper.

Another national survey from the group said for the first time since the start of the recession, every state and Washington, D.C., lost construction jobs last year. The report found few signs of recovery for the construction industry—only six states reported construction job increases late last year, according to the report.

Mississippi was at the top of the list of states adding construction jobs late last year while Wyoming posted the largest monthly percentage decline in construction employment, according to the Associated General Contractors of America report.
New Mexico Aims to Save Jobless Fund

The jobless fund in New Mexico is headed down a rough road—the state unemployment insurance trust fund will run out of money by next year if the governor and legislature don’t agree on a plan for its rescue, according to the Associated Press.

The fund is drained from effects of the recession—an estimated 75,000 residents were unemployed in November 2009, an increase of 31,000 over last year, according to the AP.

Under New Mexico Gov. Bill Richardson’s proposal, businesses in the state could pay $20 million in higher taxes that would go to helping the jobless fund get back in the black, the AP reports. That plan would have employers paying higher contributions averaging 22 percent, according to the AP. That means average tax payments paid by businesses for each employee would increase to an estimated $190 a year in July, up from $156, if Richardson’s plan is approved, the AP reports.

But, if a rescue plan isn’t in place before the fund goes into the red, under state law, tax rates will automatically increase as needed to replenish the fund, according to the AP. Under that scenario, average payments by businesses could go to $529 for each employee, according to the AP.

Read more about the condition of state jobless funds on page 26.

The West

ARIZONA FORECLOSURES
Curbing foreclosures in Arizona is the key to the state’s recovery, according to an article in The Arizona Republic. “Arizona’s problems are not just cyclical, like markets. They’re structural,” John Graham, president of the think tank, Urban Land Institute Arizona, told the newspaper.

CONSTRUCTION JOBS
Last year California lost 116,100 construction jobs, the most in the nation, the Los Angeles Times reports. And the housing bust is still battering the state: California lost more than 300,000 construction jobs total—that’s nearly a third of the industry’s labor force—since the industry’s peak of 948,500 jobs in February 2006, the newspaper reports.

COLORADO PENSIONS
Colorado is considering cuts to its pension fund, according to The Denver Post. Colorado Senate Bill 1 calls for raising the retirement age, reducing or eliminating cost-of-living increases, and increasing employee and employer contributions, the newspaper reports.

FOOD STAMPS
More Idaho residents than ever are on food stamps, according to The Idaho Statesman. Tom Shanahan, spokesman for the Department of Health and Welfare, told the newspaper the state is setting records every month. It’s processing 9,000 new food stamp applications each month and more than 176,000 people are on food stamps, he told the newspaper.

ENERGY & AGRICULTURE
For a number of Western legislators, energy and agriculture got top billing over the recent fall and winter months. The Wyoming legislature convened a West-wide symposium in Jackson last October to look at ways states can create sustainable and more efficient energy delivery systems. The Council of State Governments-WEST assisted the effort and the full report is now available at www.csgwest.org. In January, Western legislators attended the annual national conference of state agricultural and rural leaders in Orlando, Fla. CSG-WEST sponsored the meeting.

New Mexico Aims to Save Jobless Fund

To learn more about these and other developments in the Western Region, visit: capitolideas.csg.org or www.csgwest.org.
State Retirement Systems

There are 2,547 public retirement systems in the U.S. 218 of them are state retirement systems. 16.8 million people are members of state retirement systems. 6.4 million people are beneficiaries receiving periodic benefit payments from state retirement systems.

Source: The Book of the States 2009, from U.S. Census Bureau data based on 2007 fiscal year figures

A $1 Trillion Gap

A new report from the Pew Center on the States finds a $1 trillion gap between the $2.35 trillion states have set aside to pay for employees’ retirement benefits and the $3.35 trillion price tag of those promises. The report, The Trillion Dollar Gap: Underfunded State Retirement Systems and the Road to Reform, found in eight states more than one-third of the pension liability was unfunded as of the 2008 fiscal year, while two states—Illinois and Kansas—had less than 60 percent of the necessary assets on hand. The Government Accountability Office says 80 percent is the preferred benchmark funding level. For more information on this report, visit www.pewcenteronthestates.org.

Funding levels for pension funds

- ≥100%
- 80–99.9%
- 60–79.9%
- ≤59.9%

Source: The Trillion Dollar Gap: Underfunded State Retirement Systems and the Road to Reform, Pew Center on the States, released February 2010

For more information on The Book of the States, visit www.csg.org.
Retiree Health Benefits Funding Gap

Smallnest Funding Gap per capita

1» North Dakota—$48.75
2» Indiana—$70.64
3» Oregon—$72.73
4» Arizona—$73.59
5» Iowa—$74.44
6» South Dakota—$97.43
7» Kansas—$106.48
8» Minnesota—$110.48
9» Wyoming—$142.14
10» Florida—$173.77

Biggest Funding Gap per capita

50» New Jersey—$7,950.84
49» Hawaii—$7,635.80
48» Connecticut—$6,218.58
47» Alaska—$4,689.30
46» Louisiana—$4,361.75
45» West Virginia—$4,298.23
44» Delaware—$3,688.03
43» Maine—$3,624.39
42» North Carolina—$2,740.61
41» Maryland—$2,609.47

Note: States have funding gaps for retiree health benefits ranging from $48.75 per capita in North Dakota to $7,950.84 per capita in New Jersey. The gap is the difference between all accrued liabilities and any assets the employer, in this case the state, has set aside in an irrevocable trust for other post-retirement health benefits—known as OPEB, generally health benefits for retirees.


Since 1935, The Council of State Governments’ The Book of the States has been the leading authority on information about the 50 states and territories.
States Can Pay **Now or Pay More Later**

by Mary Branham

for Employee Retirement, Benefits

**Girard Miller**, an authority on the investment of public funds, believes states must make changes to pensions and other post-employment benefits now if they wish to sustain the programs in the future.
“The problem is every dollar you don’t pay toward your actuarial costs today will cost you $2 or $3 in the future…”

—Girard Miller

1. What is the current condition of state retirement funds?
“...The unfunded liabilities of pension plans have doubled from their 2007 levels. They were 85 percent funded and now that number is closer to 70 percent. So the result of that is that now the future budgets of states and local governments will have to double the amount of employer contributions that are required to pay for the deficits.”

2. So what does that mean in terms of state budgeting regarding pensions?
“The amount of total unfunded liability is somewhere in the range of $500 billion to a trillion dollars, depending on where the market is at any given week. That money is going to have to be recaptured over the next 25 years or thereabouts, which puts an additional annual cost of pension funds to amortize that in the neighborhood of $20 billion to $40 billion of additional pension expense.”

3. And pensions aren’t the only problem?
“The problem in the (other post-employment benefits) area for retiree medical is far more significant, because most of the states have not funded it and so they’ve got another liability of approximately the same size. Again $500 billion is probably a fair estimate. When you combine all of that, the state budgets going forward probably need to be paying an additional $30 billion to $40 billion a year for retirement expenses, and it could be as high as $50 billion … on top of what they are putting in now.”

4. What will happen if states don’t make that kind of investment?
“The problem is every dollar you don’t pay toward your actuarial costs today will cost you $2 or $3 in the future because you don’t earn investment income on the money that should be in the fund. … Many states are required by law to make their contributions to the pensions, so they won’t have a choice. If they don’t have additional revenue they’ll have to cut other services or other funding in order to balance the budgets. They are not typically required to make the OPEB contributions … so they could kick the can down the road to the next generation, but if they do so they will triple the costs in today’s dollars by doing so.”

5. How did we get to this point? Some states took holidays for making contributions to the funds in the flush years of the 1990s …
“That is part of the answer. A second part of it is, the pension plans—whether they did it themselves or whether they did it with the political pressure from within the legislature in some cases—granted benefits increases retroactively in the expectation that financial markets would continue to earn 10 percent on stocks all of the way through 2000 to 2010. Instead, however, during that period, the stock market earned almost zero. There are literally hundreds of billions of investment gains that were expected to occur in the first decade of this century that never actually happened.”

6. What should states be doing to address the problem?
“A few of the states have begun to reduce retirement benefits for new employees. That’s politically the easiest thing to do because you don’t touch the incumbents … The point is that most states have avoided making benefit reductions for current incumbent employees. They’ve tended to focus on the new employees. They’ve also, in some cases, increased the retirement age to make it closer to Social Security.”

7. Does reducing the benefits for new employees help?
“In the long run, those changes will eventually accumulate and they’ll become significant, but it’ll take us 10 to 15 years before the new employees outnumber the incumbent employees. … It’s partly cosmetic and it’s hopeful and of course it’s better to do that than to do nothing, but it doesn’t really do anything to deal with the pension deficits.”

8. What about changes to the other benefits?
“A lot of states provide benefits for the employee and their spouse and dependents and survivors, and they’re finding they can’t do that. So they may change the benefits, may raise the retirement age and they may require an employee contribution. They also need to put a (consumer price index) cap rather than the cost of medical inflation, which seems to be going up three times as fast as the CPI.”

9. Are defined contribution plans a good option for states?
“Defined contribution plans do not necessarily reduce your costs. … I’m an advocate of something like Washington state where they’ve gone to half defined benefit, half defined contribution … In a defined benefit plan—the pension plan—the state bears all of the responsibility if investments underperform. In a defined contribution plan, the employee bears the investment risk if investments underperform. If you’re going to view this as a partnership, it makes sense that there be a combination of the two forms.”

10. What have states with lower unfunded liability in their pension plans done right?
“If there’s one single factor it’s the ones that did not give away the store in the late 1990s and 2000; (they) are probably the ones that have held up the best. On average they tend to have a slightly more frugal benefit formula. The ones that have required a larger employee contribution have tended to have better finances than the ones that have left the taxpayers paying the whole thing.”

6 Steps to Healthier Pensions

Girard Miller recommends states take these steps to reduce unfunded liabilities in state pension and other post-employment benefit plans.

» Require a new or higher employee contribution—which will have the biggest financial impact.
» Establish a consumer price index limit on other post-employment benefits, for retiree medical—which could be very significant.
» Establish new lower benefit tiers for new employees. “That would probably be the third step that you have to do even though it will take longer to get an impact,” Miller said.
» Raise the retirement age for unreduced retirement as close to the Social Security age as possible to increase contributions and reduce the time for retirement payout.
» Eliminate spouse, dependent and survivor benefits for OPEB.
» Limit OPEB benefits for retirees before they become eligible for Medicare. Those who retire before Medicare eligibility cost the state more than those who retire after they are eligible for Medicare.
The Hardest of Times

... and What They Mean to Governors and Legislatures

In our system of separated but shared powers, governors have the upper hand in making public policy. As a rule, they do the leading, legislatures the following. This is largely because the governor is one, while the legislature is many. The governor decides on his or her own; the legislature has to struggle to achieve majorities before reaching a decision.

This imbalance between the two branches applies especially to power over the budget. In four-fifths of the states, governors formulate the budget, which legislatures then review and enact. And governors possess the item veto with which to fend off legislative incursions. The budgetary imbalance becomes even greater in hard fiscal times.

Presently, the states are living through the hardest of fiscal times. California’s problems may be in “a league of their own,” according to the Pew Center on the States, but nine other states are not terribly far behind and, with few exceptions, the rest are in trouble as well. Although the national economy appears to be recovering, the states still have further to go. It will be some time before they have replenished funds they have drawn on and caught up with investments that they have postponed.

This means that during the foreseeable future, the budgetary power of governors will increase further because legislatures are politically and structurally disposed toward lowering taxes and increasing spending, which is not the path toward a balanced budget.

The legislature is the most representative branch of government, and legislators are highly responsive to their constituencies. Their DNA is to make people happy. As many states limp toward economic recovery and wrestle with structural deficits, however, the challenge will not be that of making people happy but rather trying to keep them from getting angrier. Every legislator will be running scared and majority party caucuses will be circling their wagons as the minority party fires away. Under conditions such as these, fiscal and budgetary leadership is unlikely to come from the legislature.

Governors are no more inclined to promote unhappiness by cutting services or hiking taxes than legislatures. But governors have little choice. The governor is responsible for the entire state, not just one legislative district. Being one, rather than many, the governor cannot evade responsibility. In the legislature the party caucuses and individual members can weave and dodge; responsibility is shared and therefore diffused.

In sharp contrast, the buck stops at the governor’s desk; there is no alternative but to lead.
REST AREAS BECOME HOT BUTTON ISSUE
RICHMOND, VA.—Signs and barriers mark the closing of an Interstate 64 rest stop near Richmond, Va. The Virginia Department of Transportation closed 18 rest stops due to budget cuts but will reopen them this year.

Photo: Steve Helber/©2010 The Associated Press

It was a cost-cutting measure that didn’t stick. When Virginia shut down 19 rest stops throughout the state in summer 2009 because of budget shortfalls, officials didn’t think anybody would really notice, or really care. After all, it’s just a highway pit stop, right?

But boy did people care.

“Rest areas became a hot button issue,” said Jeffrey Caldwell, chief of communications for the Virginia Department of Transportation.

“We understand that rest areas are an amenity people have gotten used to. But we couldn’t afford to operate as many rest areas as we had. There was no easy choice here.”

So to deal with the $4.6 billion shortfall in revenue for transportation, the state closed the rest areas, hoping to save more than $7 million a year.

But Bob McDonnell, who took office as governor this year, ordered the state to re-open the highway pit stops, even though the Virginia Department of Transportation isn’t sure where to find the money to keep the lights on and the plumbing going, and to pay the custodians needed to clean the rest areas, according to Caldwell.

“We have to find $7.5 million to run those. It’s a zero sum game,” he said.

The department pulled $3 million out of its emergency maintenance reserve fund to pay for the reopened rest areas through June 30, Caldwell said.

Cuts will be made elsewhere in the budget to pay for reopened rest areas—but where was still up in the air in February, according to Caldwell, when the first four closed rest areas were reopened along Interstate 81. The others re-opened in phases in mid-March, with the final seven scheduled to be reopened by April 15.

And that’s just it. Services states have been used to providing in good years are things residents have come to expect. In the bad years, those cuts can be painful and there may not be the political will to make the cuts, experts say.

“States have tried the cut, cut, cut, approach and they’re realizing that that can only go so far,” said Sujit CanagaRetna, senior fiscal analyst with The Council of State Governments.
Southern office, the Southern Legislative Conference.

“My belief is that this Great Recession will result in this sort of philosophical transformation of what state government is and I think we’ll end up with a very core set of services that are limited to what state government can do just because we can’t afford to do anything else.”

So state policymakers are rethinking the role government should play.

“There may be some thinking on the part of states about what their functions can be in the future, and there will be some talk about should they do less,” said Jon Shure, deputy director of State Fiscal Project at the Washington, D.C.-based Center on Budget and Policy Priorities. “But, that’s not because they got too big, it’s because their revenues took such a huge hit because of the recession.”

Shure’s project with the Center on Budget and Policy Priorities gathers state tax and budget information.

What Can States Afford?

In Idaho, with more budget cuts looming, the Park and Recreation Board was looking to close two state parks early this year—Thousand Springs State Park in southern Idaho and the Land of Yankee Fork State Park in central Idaho.

Idaho Department of Parks and Recreation Director Nancy Merrill said the closures were almost unavoidable with the state of the budget. “When you look at ways to control your budget, you can no longer do services if you don’t have the people,” she said. The department didn’t hire 25 percent of its summer employees in 2009, she said, because it just couldn’t afford to.

It’s not the first time the state has gone down the path of closing parks, Merrill said. In 1981, because of budget cuts, the state closed three parks, two of which were reopened later, she said.

Even though state parks may not be what most call “core” services, “we realize that parks have a lot of impact,” Merrill said. Although the parks remain open for now, the department will likely suffer other major cuts.

But some say state courts certainly qualify as core services. And in California, even the judicial branch is shouldering its share of state revenues that come in, it spells trouble, he said.

“It’s not just the economy. The economy is about half the problem,” Martin said. “The other half was self-inflicted.”

Even though the treasurer’s office warned of the coming recession and the shortage of revenues, the warnings were ignored and the state was spending more, said Martin, who is running for Arizona governor this year.

“The state’s broke, basically,” Martin said. “The state is literally out of money.” When the state first ran out of cash in January 2007, that meant basically the state’s checkbook was negative and it was burning through its reserves, he said.

That said, no matter how bad it gets, a state can’t actually file for bankruptcy, Martin said. “The state cannot go into bankruptcy—bankruptcy laws do not apply to states,” he said. “Basically you slip into defaults, which is kind of the same thing. You bounce a check effectively and when you bounce a check you send the person an IOU.”

California has been sending out IOUs since last year; Arizona is also sending them, although not to the general public.

And that’s what happens when a state runs out of cash—the IOUs keep coming. The problem may continue as long as states don’t address structural problems within the budgets, Martin said. As long as states spend more than the revenues that come in, it spells trouble, he said.

What Happens When a State Runs Out of Cash?

By Mikel Chavers

Arizona Treasurer Dean Martin is no stranger to handling cash shortages and other budget issues. His state has been crying recession since January 2007, when the state first ran out of cash.

“We actually beat a lot of economists to that forecast because of what we were seeing,” said Martin, who served as a state senator for six years before his post as treasurer.

In fact, a few days before Christmas 2009, Arizona’s credit rating was downgraded by Moody’s because of failure to pass a balanced budget, Martin said.

Credit ratings have declined in other states. Recently, Standard & Poor’s cited concerns over California’s finances when it downgraded the state’s only remaining “A” rating early this year, including a possible shortage of cash, according to The Los Angeles Times. But just what would happen if a state ran out of cash?

Take a lesson from Arizona, perhaps one of the hardest-hit states in the recession.

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Even though the treasurer’s office warned of the coming recession and the shortage of revenues, the warnings were ignored and the state was spending more, said Martin, who is running for Arizona governor this year.

“The operating liabilities of the state in fiscal year 2008 grew by 10.5 percent, when revenue dropped by 9 (percent),” Martin said. So that’s
how the state ran out of cash, he said.

“What happens from a state perspective, as long as the state doesn’t have a permanent structural solution, they continue to erode their cash base,” Martin said. And when that happens, states will have to resort to drastic measures to bring in more cash.

Arizona sold a variety of state buildings early this year, including the archives building, the tower at the capitol that houses the governor’s office and six prison buildings in Florence, according to the Arizona Republic.

The proceeds from the selloff generated enough cash to pay the state’s bills for about a month, Martin said. The state will lease the buildings and hopes to buy them back in the future.

Drastic measures to raise cash may become more frequent as states continue to run out of money, experts say. Nearly every state faces a budget shortfall, according to the Center on Budget and Policy Priorities, and although most states have closed budget gaps for the 2010 fiscal year, all but six states face an anticipated budget shortfall for the 2011 fiscal year budget.
“The fiscal black hole that we’re in has not improved,” said Justice Richard Huffman of the California Court of Appeals in the Fourth Appellate District in San Diego.

The state is still grappling with the largest shortfalls in the U.S., an anticipated $14.4 billion budget gap for the 2011 fiscal year, according to figures from the Center on Budget and Policy Priorities. In fact, little known budget-cutting measures have forced the state’s courts to shut down for one day a month, a practice that was still going on early this year, according to Huffman.

An estimated 80 to 90 percent of the state’s judges are even giving up part of their pay, either by voluntary salary waivers that fund trial court operations or through direct contributions that go to funding their own courts, according to Lynn Holton, spokeswoman for California state courts. Huffman is one of the judges voluntarily giving up part of his pay.

“You could say that if (states are) only cutting parks and rest areas, that at least it doesn’t affect whether some people will make it or not. But they’re not. They’re cutting education and health care, which obviously does have an impact on people’s future in a more tangible way,” Shure said.

Shure said some states can’t even afford their level of core services—education and health care, according to him—two areas that make up large portions of state budgets.

“With cuts of this magnitude, they are cutting core services,” Shure said. “And what concerns us most is that they are cutting services that are needed by the most vulnerable parts of the population.”
States Seek More Money

Shure is advocating states take a more balanced approach to deal with the recession. By that he means states should not cut spending alone—as they’ve been doing—but states should also raise taxes to bring in more revenue.

In fact, CanagaRetna said states are starting to raise taxes, although politically it isn’t easy, he said. In the 2009 fiscal year, states raised taxes and fees to the tune of nearly $24 billion, he said. The bulk of that came from California and New York where personal income and state sales taxes increased.

Missouri Rep. Allen Icet, chairman of the budget committee in his state, echoes the dilemma facing states. “The two options that a state has is we either cut programs accordingly to get to that balanced budget, or we go back to the people of the state, the citizens of the state, to ask for a tax increase,” Icet said.

In Missouri, the legislature could increase taxes and raise an estimated $75 million, “and obviously that’s not nearly enough,” Icet said. Although he said the legislature won’t do that, in order to raise enough revenue to pay for everything, a tax increase would have to go on the ballot in a general election, he said.

“I think we’d all agree that that proposition will never pass, so that gets us back to the first option—that’s to cut budgets.”

There’s the dilemma.

“We think the budgets that are being worked on now in most states (that) will take effect July 1, are probably going to be worse than the budgets of this current year—as bad as these budgets were—because state revenues are continuing to fall,” Shure said. And even if the nation slowly recovers, states won’t get better for a while.

“Traditionally state finances are one of the last things to turn around in a recovery because they don’t turn around until employment reaches pre-recession levels.”

10 Strategies to Close the Gap

Budget gaps have states using a variety of measures to either cut spending or bring in more money. Here are some of the top strategies states are using to help the bottom line, according to the experts. But whether they’ll reap long-term benefits remains to be seen.

1. Privatize: States are considering privatizing everything from state highways to state parks. Remember the public-private partnerships hype? The Center on Budget and Policy Priorities’ Jon Shure said privatizing highways could mean “possible significant upfront money and great cost down the road (pun intended). And if these are toll roads, the state would give up revenue, long-term.”

2. Look at tax incentives, clawbacks: States are using what’s known as tax ‘clawback’ provisions that require companies to pay back tax incentives if they didn’t meet employment or investment targets. In North Carolina, when Dell closed a plant near Winston-Salem, the company had to pay back millions in state and city tax breaks.

3. Reform sentencing laws: On releasing nonviolent offenders, Scott Pattison, executive director of the National Association of State Budget Officers, said there’s a “huge reluctance to do this although it obviously saves a lot of money.”

4. Tax Internet sales: States are watching New York’s 2008 legislation requiring Internet giant Amazon to collect sales tax from New York customers, said Sujit CanagaRetna, senior fiscal analyst with CSG’s Southern Legislative Conference. CanagaRetna said state and local governments are losing billions in e-commerce if they don’t tap this.

5. Consolidate state agencies: “Guaranteed savings could be small,” Shure said.

6. Trim pensions: “Better idea might be to raise enough revenue to fund obligations,” Shure said. Many states avoided payments instead of raising revenue, he said.

7. Consider tax amnesty programs: In December 2009, North Carolina recouped more than $420 million in back taxes owed by corporations, “which is a huge number compared to what they were expecting,” CanagaRetna said. North Carolina agreed to waive penalties on corporations that paid taxes they owed, he said, and the state was back in the black for the 2010 fiscal year.

8. Cut salaries: Virginia’s Gov. Bob McDonnell, when he took office in January, took a pay cut and cut his top advisers’ pay by 5 percent.

9. Impose four-day work weeks: Utah started the trend in 2008 and other states are following suit. “I think there’s an open question about whether it saves that much money,” Pattison said.

10. Raise income taxes on upper-income households: Shure said raising additional revenue is essential.
PREVENTING FORECLOSURE

COMMERC CITY, COLO.—A homeowner listens during a foreclosure prevention workshop held by the Adams County Housing Authority in Commerce City, Colo. The county, which has one of the highest foreclosure rates in the state, puts on several workshops a month to help residents learn ways to avoid foreclosure. Colorado operates a Foreclosure Hotline to connect borrowers with nonprofits like this one, who can provide information on a borrower’s options when facing foreclosure.

No state has felt the foreclosure crisis as acutely as Nevada.

“We describe Nevada as ‘Ground Zero’ for the foreclosure epidemic,” House Speaker Barbara Buckley said. “Especially in Clark County (home to Las Vegas) you cannot drive through a neighborhood without seeing three or four foreclosed homes on a block.”

Nevada led the nation in the rate of foreclosures for the third year in a row in 2009. But it was bad across the country and the foreclosure crisis isn’t over yet. Foreclosure filings increased by 21 percent in 2009 over 2008, according to RealtyTrac, a real estate data service that tracks foreclosures. Owners of 2.8 million properties nationally received foreclosure notices last year.

In Nevada and across the country, state officials are responding—trying to keep people in their homes and foreclosures from further wrecking the economy.

Buckley is frank about the impact of foreclosures: “It was and is impacting our economy, and it was just a spiraling effect that had to be addressed,” she said.

She responded to the foreclosure crisis with Assembly Bill 149, which the legislature approved and Gov. Jim
Gibbons signed into law in 2009. It gives homeowners the right to request mediation that may result in the loan terms being modified. Once a homeowner requests mediation no further action can be taken to sell the property under foreclosure until the mediation is complete.

Connecticut has a similar program. Through the foreclosure mediation program’s first 16 months, 4,448 cases completed the mediation process, and in 2,700 of those cases, homeowners were able to stay in their homes, according to figures released in January from the state’s judicial branch. Another 611 cases resulted in a negotiated settlement that allowed the homeowner to avoid foreclosure, but leave the property—"a "graceful exit" for homeowners,” Roberta Palmer of the Connecticut Judicial Branch said.

Those states aren’t alone in addressing the crisis. More than 30 states and Puerto Rico enacted nearly 100 new laws in 2009 addressing foreclosure and mortgage issues, according to a January report from the National Governors Association. Two-thirds of those laws focused on foreclosure mitigation strategies.

**New York’s Landmark Legislation**

In December 2009, New York Gov. David Paterson signed into law one of the nation’s most comprehensive foreclosure bills to provide additional protections for homeowners facing foreclosure. The measure builds on Paterson’s subprime lending reform law enacted last year and is taking effect in phases. The law:

- Requires a 90-day pre-foreclosure notice to be sent to all home-loan borrowers. This allows additional time for homeowners to work with lenders to avoid foreclosure;
- Requires lenders to file documents with the Banking Department, which allows the Banking Department and Division of Housing and Community Renewal to provide targeted assistance to distressed homeowners during the critical pre-foreclosure period;
- Requires lenders who obtain a judgment of foreclosure to maintain the foreclosed property; and
- Enhances consumer protection to prevent homeowners from being victimized by rescue scams, and prevents brokers who perform distressed property consulting services from accepting upfront fees.

“This effort is about keeping New Yorkers in their homes and protecting them during this economic crisis,” Paterson said when he signed the bill into law.

New York’s statute is similar to one in Massachusetts that gives homeowners 90 days to make any overdue mortgage payments and stay in their homes.

**Courts Take The Lead**

State foreclosure protection initiatives are often led by the courts.

In January, New Hampshire’s courts created a mediation program that provides a neutral forum for discussions between lenders and homeowners. The Foreclosure Mediation Program was designed by a group of lawyers involved in mediation, representatives from the bank and mortgage industry, and lawyers who represent troubled borrowers.

In December 2009, Florida’s Supreme Court issued an administrative order requiring mediation programs.

**2009 State Foreclosure Laws**

Several states passed laws in 2009 to offer protection to homeowners and renters.

**Notification**

- Michigan requires foreclosure notices to include certain information and to be accompanied by a list of counselors and contact information for the state bar association’s referral service.
- Washington requires that renters and borrowers receive information regarding resources and rights and lenders have in-person conversations with borrowers 30 days prior to initiating foreclosure proceedings.

**Mandatory Mediation**

- Connecticut requires for any foreclosure commenced between July 1, 2008, and June 30, 2009, a borrower must be notified of the state mediation program and a mediation must begin within 15 days.
- Maine added a new mandatory foreclosure mediation program for borrowers.

**Defer or Suspend Foreclosure Process**

- California created a 90-day deferment on home foreclosures.
- Michigan requires the homeowner to contact a counselor within 14 days to receive a 90-day foreclosure deferment.
- Colorado allows a 90-day foreclosure deferment as long as the homeowner agrees to contact a U.S. Department of Housing and Urban Development-approved housing counselor within 20 days.
- New Jersey allows a six-month delay period to the foreclosure made possible by a special agreement between the lender and borrower for borrowers who seek mediation and counseling.

**Protection for Renters**

- Colorado makes it a criminal offense for property owners to continue to collect rent from a tenant after a foreclosure sale.
- Illinois requires lenders to provide notification if a foreclosed property is acquired and before the current tenants are required to move.
- Maine forbids foreclosure from terminating tenancy.
Florida ranks third in the number of foreclosures, according to RealtyTrac. Under the court’s rules, only properties where homeowners actually reside are covered and mediation can be waived if agreed upon by the lender and borrower.

Foreclosure filings in New Jersey increased in each of the past four years, with more than 60,000 in 2009. In October 2008, Chief Justice Stuart Rabner unveiled a statewide judiciary program to help homeowners. Under the program, the courts require mediation in all cases in which homeowners contest owner-occupied foreclosure actions. Volunteer mediators meet with eligible homeowners and their lenders in an effort to resolve the foreclosure action and renegotiate the terms of mortgage agreements.

Michelle Perone, chief of Civil Court Programs for the New Jersey Judiciary, said mediation “provides that forum where somebody has an opportunity to be heard and to try to make things work, and if not, rather than be forcibly ousted by a sheriff from their house, to leave with dignity.”

She insists mediation is also beneficial to lenders.

“If a loan modification results in a performing loan, then I think there’s a benefit to the lenders and their investors,” she said.

**Some Efforts Blocked**

But blocking foreclosure action hasn’t come easily in every state. Minnesota Gov. Tim Pawlenty vetoed a 2008 effort to defer foreclosure action for as many as 15,000 Minnesotans. “If Minnesota creates a statutory right for individuals to remain in their homes beyond our already extensive foreclosure laws, mortgage providers will factor this additional business risk into mortgage agreements and Minnesota mortgages will be more expensive,” Pawlenty said in vetoing the legislation.

The action hasn’t discouraged state Sen. Linda Scheid, who is sponsoring similar legislation this year to require mediation be offered to homeowners served with a foreclosure notice.

“My instincts are to not interfere with contracts, but I also understand enough about contract law that you need to have pretty equal bargaining power. And homeowners just don’t have any kind of leverage whatsoever,” Scheid said.

**The Lenders’ Perspective**

The Mortgage Bankers Association, a Washington, D.C.-based organization representing the real estate finance industry, has reservations about state mediation programs.

“Most often, we are finding that mediation is simply being used as a stall tactic, while the delinquent borrower continues to fall further and further behind on payments and the property falls into further and further disrepair,” said association spokesman John Mechem. “Mediation is time-consuming and costly for both the borrower and the lender; time and money that could be better used determining whether there is a realistic opportunity for the borrower to keep the home and trying to implement that solution.”

He believes mandatory payment forbearance or a moratorium on foreclosures don’t work. They “only serve to drag out the pain for borrowers, communities and lenders alike,” said Mechem.

Lenders will sometimes delay foreclosure action, as many did during the holidays and during implementation of President Obama’s modification plan, according to Mechem.

Buckley disagrees, adding Nevada’s banking industry largely supported her legislation.

“These programs would not be necessary if the lenders were able to work with the borrowers and obtain modifications on their own,” she said.

Mechem concurs that there are legitimate roles that state policymakers can take to intervene during the foreclosure crisis.

“The most important role that state officials can play is helping spread the word that borrowers need to contact their lender if they want to keep their home,” he said. “We are still seeing nearly half of all foreclosures are on properties where the borrower has not responded to repeated calls and letters from their lender. If borrowers won’t work with their lender, there is not much we can do to help them.”

Mechem said that’s where state government officials come in.

“State and local officials are a trusted and respected voice in their communities,” he said. “They can help convince borrowers to work with their lenders.”

Mechem believes states should also encourage cities and counties to participate in the Mortgage Electronic Registration System, or MERS, vacant property registration system (http://www.mersinc.org/ppc/index.aspx). This industry-developed database is designed to help local officials identify property owners. When local officials see a property in disrepair, they can look up the property and identify the loan servicer responsible for maintaining the property. This will help stop the downward spiral of property values and degradation of neighborhoods, Mechem said.
In South Dakota, corn is now made into ethanol and dry distiller's grain is made in the same process. Turkeys used to be sent out for processing, but now there’s a processing plant in the state. The state is also courting the firearms industry and is turning an old gold mine in western South Dakota—the deepest in North America—into an underground lab where experiments can be conducted deep into the earth.

Those new areas for jobs naturally fit with the state’s strengths—existing assets just needed a little repositioning, so to speak. “This national recession will cost jobs—some of which will not come back. And as those jobs are permanently eliminated from the employment opportunities, other types of jobs have to replace them,” said South Dakota Gov. Mike Rounds. “It’s a refocusing on what we already have that we can add value to.”

Only then will states move forward into recovery and into prosperity, Rounds said. In fact, that’s Round’s focus as the 2010 president of The Council of State Governments—helping states move forward into prosperity.

Lots of states are desperate for jobs. With unemployment at 9.7 percent nationally for January, states are looking for new and creative ways to attract jobs.

And with many industries hit hard by the recession, attracting jobs may be even more difficult. “The economy really dictates … how automakers expand. It’s been a rough year for us,” said Wade Newton, spokesman for the Alliance of Automobile Manufacturers, a trade association representing automakers.

With that said, states can still look to the business community for advice on attracting the jobs that are out there—and it isn’t just about incentives, those in the industry say. “I think that more than any one type of incentive program or plan, what businesses are really looking for is friends,” said Dan Colegrove, senior director of state and local government affairs with Kraft Foods Global Inc.

“Legislators tend to do a fairly good job of reaching out to small business owners and companies that are based in their own states,” Colegrove said. “I would encourage policymakers to remember that large, multi-national corporations like ours also have a lot of advice to offer them.”

Incentives are just “one of several things that we feel like we need to make a major commitment and investment in the state,” said Barbara McDaniel, spokesperson for Toyota Motor Engineering and Manufacturing North America in Erlanger, Ky.

For example, when Toyota was considering its Mississippi plant, which broke ground in 2006, the company wanted to check out the area’s work force, McDaniel said. So executives visited area employers to get an honest opinion. “The executives were really blown away by how complimentary the management was of the work force,” McDaniel said.

So Toyota chose Mississippi. But to Rounds’ point, it’s not just about incentives for traditional industries.

“The old, traditional jobs that someone might have been in for 10 or 15 years go away because of the new way to deliver the product, or the old product is no longer necessary. Or, they found a more effective way of delivering the product without as many individuals being involved in the process,” Rounds said.

Here is a glimpse into how states in each region are attracting jobs. The states are hard on the trail in the hunt for jobs.
Vermont Uses Unspent Stimulus Cash to Create Jobs

What enjoys bipartisan support in Vermont? Dairy farmers.
In fact, the dairy farm industry is just one that will benefit from Vermont Gov. Jim Douglas’ proposed job creation package that uses $8.6 million in unspent federal stimulus money from the state fiscal stabilization fund.
That’s because, “our agricultural industry, especially dairy, is a big part of our heritage, our landscape and our economy,” said David Coriell, the governor’s spokesman.
The package includes:
» $2 million to lower interest rates on loans to Vermont companies;
» $1 million for the state’s work force training program;
» $1 million for subsidized, low-cost loans to farmers for feed, fuel and fertilizer;
» $1 million for businesses impacted by a bridge closure;
» $500,000 for tourism; and
» $3.17 million for rural broadband.
“On top of the recession, dairy farmers have struggled with very low milk prices,” Coriell said. It costs $18 to produce the equivalent of 100 pounds of milk, but that same amount sells for $12, he said.
“It’s really important that they have help to get through this time,” Coriell said.
For more on this story, visit capitolideas.csg.org.

Michigan Energizes Jobs with Next-Generation Batteries

With the state’s unemployment rate hovering around 14 percent, Michigan is looking for jobs to energize its economy.
Michigan Gov. Jennifer Granholm and the Michigan Economic Development Corporation think they found it in next-generation lithium ion batteries that can be used in high-tech, energy efficient cars and more.
Part of Michigan’s strategy to attract alternative energy jobs, the battery sector is a natural fit for the state—especially considering its association with automobile manufacturing.
Because next generation battery packs are made up of groupings of cells, state officials knew if they could get the cell manufacturers in the state, they’d be well on their way to creating a hub for the specialized technology.
“We’ve captured cell manufacturing now from six different companies,” said Greg Main, president and CEO of Michigan Economic Development Corporation. “A couple of the companies who have decided to locate in Michigan are providers of materials.”
The state also awarded battery tax incentives worth more than $800 million to four major lithium ion battery cell manufacturers. One of the companies, Johnson Controls-Saft, is in the process of refitting its plant in Holland, Mich., to create more than 1,000 jobs to make the batteries, Main said.
“They’re good jobs too,” Main said. The average weekly wage is $600, he said.
For more on this story, visit capitolideas.csg.org.
Florida Hosts Jobs Summit for Business Input

Florida Sen. Mike Haridopolos and Florida Rep. Dean Cannon know their state needs jobs—but they wanted feedback from the business community. So the senate president and house speaker held the Florida Jobs Summit in early January.

More than 300 people attended from all types of businesses and “most importantly we were there to listen to folks who are actually in the business world and identify some of the barriers to job creation,” Haridopolos said.

Mostly, the business community is looking for certainty before investments, Haridopolos said.

“There’s just a lot of uncertainty coming out of government, especially out of Washington right now with the health care bill,” he said. “And a lot of employers were just saying ‘look, just have everything stable, don’t do anything radical so as we prepare in these very difficult times, we know that the government is not going to hand out a new tax or a new mandate that’s going to make it more difficult for us to get out of this difficult spot’.”

With that advice, Haridopolos and Cannon hope to boost investment, economic growth and job creation in the Sunshine State. First on the list? Haridopolos is proposing a film and digital media tax credit.

For more on this story, visit capitolideas.csg.org.

Washington Aims for 40,000 Jobs, Goes Green

Washington Gov. Christine Gregoire has a 10-point plan that could create as many as 40,000 new jobs this year. The centerpiece of the plan is a clean energy business development program to spur energy efficiency projects in the state, starting with the state-owned buildings.

The state will basically provide low-cost financing so state agencies can afford to take on major energy efficiency projects that will take longer to pay back, according to Daniel Malarkey, deputy director of the state’s commerce department.

In order to make the energy-efficiency renovations, the state will partner with the private sector to get the job done—and that means immediate jobs, according to Malarkey. The state will leverage the promised energy savings for the loans, he said.

Major energy efficiency investments include replacing the chiller or boiler and could take 20 to 25 years to pay back, Malarkey said. But those bigger energy efficiency projects mean more jobs, he said. “We’re able to employ more engineers, architects and installers and we also get to help stimulate an industry that has real growth prospects,” he said.

“There’s a big net gain from making things more efficient,” Malarkey said.

For more on this story, visit capitolideas.csg.org.
In the past year alone, Colorado’s jobless fund dropped by more than $530 million, from $562 million in January 2009 to $30 million in January 2010.

That’s according to Donald J. Mares, executive director of the Colorado Department of Labor and Employment, who also said the state processed more than 22,000 new applications in November from people who lost their jobs and were applying for unemployment benefits. Just two years earlier, the monthly average for new applications was about 11,000, he said.

“Like all states, Colorado has been hit hard. More people are tapping into the benefits,” Mares said in a statement following a presentation before the state’s Joint Budget Committee.

Borrowing to Pay the Bills

The nation’s unemployment rate was at 9.7 percent in January, according to the U.S. Bureau of Labor Statistics. Americans are spending more time unemployed during the economic downturn—up from 18 weeks in November 2008 to 28 weeks in November 2009. That puts a significant strain on state resources.

The primary reason state trust funds—the pots of money states use to pay workers who have lost their jobs—are running out of money is simple: The amount of money coming into the funds has stayed the same or even decreased at a time when the number of jobless workers needing the benefits has skyrocketed.

“The base wage that employers pay in to the (unemployment) trust fund hasn’t changed in 25 years,” Jane Oates, assistant secretary for U.S. Department of Labor’s Employment and Training Administration, told C-SPAN in January. “So when you have more people using benefits and you haven’t increased the amount of revenue that you are putting in, you are going to come up with a situation where you are short on funds.”

And short on funds is exactly where a lot of states are in their unemployment insurance trust fund balances. Some state trust funds have already run out of money—some are deeply in the red—and have been forced to borrow from the U.S. Treasury, which lends money to states to help stabilize the funds during volatile times.

As of February, the average amount borrowed from the feds per state was just more than $1.1 billion, according to the U.S. Department of Labor. California borrowed the most of any state—$6.9 billion; it’s been borrowing federal funds since January 2009. Colorado, the first state forced to seek help this year, borrowed $27 million by the end of January.

Michigan, which faced unemployment rates as high as 15.3 percent over the past few years, was the first state to begin borrowing money, starting in September 2006. Its loan balance was $3.37 billion in January.

By the end of January 2010, states had borrowed more than $30 billion from the federal government to pay unemployment benefits.

Making Cuts, Raising Taxes

Although the Recovery Act includes a provision that delays interest from accruing on the loans until the end of 2010, the bill eventually will come due. Oates said some
Some States Will Get More Money

Thirty-five states expect to collect more unemployment taxes in 2010 from employers because of changes in tax laws, according to a survey by the National Association of State Workforce Agencies. Hawaii expects to see the highest increase, unless action is taken to cap tax hikes on employers, and Kentucky projects the lowest increase. Two states, New Mexico and Nevada, expect to collect less in unemployment tax revenue from employers in 2010, while Michigan, North Carolina and West Virginia expect no change.

West Virginia in the Black

West Virginia’s unemployment trust fund balance in January 2010 was still in the black at approximately $100 million. The state has not yet had to borrow from the federal government.

Although the recession hit West Virginia hard, the state didn’t see a major increase in unemployment claims until December 2008, several months later than many states, said Mike Moore, the state’s unemployment compensation director.

West Virginia’s trust fund was relatively stable before the recession started, leaving the state in a better position to weather the coming storm, Moore said.

The state also took several pre-emptive steps to ensure the fund stays solvent. In May 2009, Gov. Joe Manchin signed Senate Bill 246, which increased the amount of wages businesses must pay taxes on from $8,000 to $12,000, meaning businesses must now pay taxes on the first $12,000 of each employee’s income.

The legislation also froze benefits at the current range of $24 to $424, until the trust fund reaches $220 million. The state also transferred $40 million from the old workers’ compensation fund, which was privatized in 2005, into the unemployment trust fund.

states will be paying back those loans in 2020.

And that interest will rack up; at the end of 2009, the interest rate on borrowed funds was approximately 3.8 percent, according to Ben Fendler, an analyst for the National Association of State Workforce Agencies. Unless the deadline on interest accrual is extended a second time, states will have to look elsewhere for money to pay back the interest, because interest on borrowed funds cannot be paid back using unemployment revenues.

That spills over into general fund budgeting, which is forcing states to take action.

A recent survey by the National Association of State Workforce Agencies shows 35 states increased taxes on employers in 2010 and seven states enacted legislation to raise the portion of each employee’s income businesses must pay taxes on.

Washington is one state that raised unemployment taxes. According to the state’s Employment Security Department, the bottom rung for 2010 tax rates will rise from 0.35 percent to 0.95 percent. Taxes apply to the first $36,800 of earnings for each worker.

Washington recalculates tax rates each year using a formula established in state law. Because the state’s unemployment rates were low from 2005 through 2008, tax rates remained low in 2009. Higher-than-usual unemployment in 2009 has caused record benefit payouts, leading to the 2010 tax increase.

Washington’s fund stood at $2.79 billion in November 2009, enough to provide about 14 months of benefits in a severe recession, according to the department. Washington paid out around $2 billion in benefits in the last fiscal year but collected only $1 billion in taxes. Officials say without action, the fund will be in danger.

“So far, more than two dozen states have drained their unemployment funds and have racked up billions of dollars in federal debt to pay benefits, and more are going bankrupt every month,” Employment Security Commissioner Karen Lee said in a press release. “After the recession, those states will have to doubly tax their employers to pay off their loans and also replenish their unemployment funds, while also paying ongoing claims — and that will be a competitive advantage for businesses in our state.”

Some states have resorted to cutting benefits.

Pennsylvania saw its unemployment rates rise from 6.4 percent in December 2008 to 8.9 percent one year later, sending its trust fund balance into a negative balance. The state began borrowing in March 2008 and by the end of January had borrowed almost $2.2 billion.

Troy Thompson, a spokesman for the Pennsylvania Department of Labor and Industry, said unemployment benefits were cut by 2.3 percent starting in January to preserve the fund and lessen federal borrowing. The reduction is based on a statutory requirement that triggers when unemployment rates are high or benefits paid out increase significantly.
MONEY WELL SPENT?

Stimulus May Have Helped States Now, but Policymakers Still Face Tough Decisions

by Alan Greenblatt

“… We found ourselves in such a world of hurt that (stimulus money) did get used for ongoing operations—but then you still have issues when the stimulus money goes away.”

—Kansas Sen. Jay Emler
Immediate Past Chair, CSG Midwest

Kansas state Sen. Jay Emler has mixed feelings about the federal stimulus package. He continues to have the nagging sense that $787 billion could have been spent more wisely.

“My whole thought on the stimulus money was that we should have used it for one-time expenses and not operational purposes,” said Emler, who chairs the Kansas Senate Ways and Means Committee. “However, we found ourselves in such a world of hurt that it did get used for ongoing operations—but then you still have issues when the stimulus money goes away.”

Emler’s ambivalence is widely shared among state lawmakers and others. Whether states have made a success of the stimulus depends on how you look at it.

The law, officially known as the American Recovery and Reinvestment Act, has clearly had many beneficial effects, both at the state level and in terms of reviving the broader economy. But the law attempted to do so many different things that it couldn’t succeed entirely in any of them.

“It was a lot of things to a lot of people,” said Jim Schowalter, Minnesota’s state budget director. “The initial act had several different objectives. Not all of them were consistent, and I think that leads to some of these differences of opinion.”

Benefits of Recovery Act

In contrast with other massive federal intervention programs, the Recovery Act has prompted few reports or even allegations of misspent funds—despite, or perhaps because of, unprecedented accountability require-

ments. “The transparency aspect has put people on notice that the whole world is watching, or at least the whole country is watching,” said California state Auditor Elaine Howle.

Howle notes that, in most areas of the stimulus, states already had experience running the relevant programs for the feds. But the Recovery Act has also forced state officials to work more closely with cities, counties and other local entities in order to meet federal requirements.

“The way that it was structured really encouraged partnering in ways we hadn’t partnered before,” said Jill Satran, Washington Gov. Christine Gregoire’s economic recovery coordinator.

Many state officials say such partnership, while sometimes painful or frustrating, has ultimately proved beneficial and will form the foundation for more cooperative efforts in the future.

But some critics argue the myriad levels of government involved in running Recovery Act programs have delayed and diminished their impact.

States were given roughly $135 billion to help erase their deficits. David Wyss, chief economist for Standard & Poor’s, said this did little to help the economy. “A lot of it just transferred state deficits to the federal level, without actually increasing spending,” he said.

Because their revenues have fallen by amounts greater than the federal infusion, states on average were able to use stimulus funds to fill about 30 percent of their shortfalls last year. The stimulus, then, was not enough to entirely stave off spending cuts and tax increases that put downward pressure on the economy.

Alan Greenblatt, a freelance writer in Washington, D.C., is a former staff writer for Governing.
OLYMPIA, WASH.—Jill Satran, Washington Gov. Chris Gregoire’s executive policy adviser for stimulus spending, said the American Recovery and Reinvestment Act of 2009 encouraged partnering in a way the state never had before. She and others involved with the Recovery Act say such partnership, though sometimes frustrating, has proved beneficial.

There’s Still Some Stimulus Money to Get ...

Grants Available to States

<table>
<thead>
<tr>
<th>Program</th>
<th>Deadline</th>
<th>Total Available</th>
<th># of Grants</th>
</tr>
</thead>
<tbody>
<tr>
<td>Diabetes Research Grants</td>
<td>3/11/10</td>
<td>$3 million</td>
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</tr>
<tr>
<td>Science Research Grants</td>
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<td>Provider Behavior Research Grants</td>
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<td>Postdoctoral Global Health Research Grants</td>
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<tr>
<td>Provider Behavior Research Grants</td>
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<td>N/A</td>
<td></td>
</tr>
</tbody>
</table>

For more information on these grant opportunities for states, visit capitolideas.csg.org.

Still, a drastic situation would be a lot worse without the federal help—which was, despite Wyss’s complaints, used exactly as intended in filling budget shortfalls.

“It’s very clear that had we not used the stimulus money as we used it, there would have been layoffs, there would have been people losing jobs and programs closed,” said Utah Sen. Lyle W. Hillyard.

In addition to keeping states from making big cuts to Medicaid and education, the stimulus provided funds for expansions of many programs. There, too, the picture is mixed.

Construction Projects Seen as Boon

In some areas, the money was a boon, helping state transportation departments move thousands of projects from the drawing board out onto the streets—putting tens of thousands of Americans to work.

“If it wasn’t for the stimulus, we would have laid off 40 or 50 percent of our people,” said Jim Duit, president of a large construction company in Oklahoma.

Construction projects have had a ripple effect beyond providing jobs to crews of 50 or 250 people, as state departments of transportation point out. In south Texas, construction of a new bridge across the Colorado River has helped the city of San Angelo meet the shipping demands of the largest new manufacturing plant it’s attracted in two decades. In Johnston, R.I., a $3.4 million reconstruction of a main road through town has led directly to the redevelopment of a vacant property near town hall that had stood vacant for 19 years.

The first phase of the $40 million shopping and hotel center is scheduled to open when roadwork is completed this fall.

“It was one of those shovel-ready projects that you hear about in the press that this stimulus was supposed to get off the ground,” said developer Jeffrey Saletin. “Our project, with so much money being put in by the private sector, is probably a project that never would have started if this road hadn’t been improved because this road was a disaster.”

Some Projects Slow to Start

But if state departments of transportation stood ready to work on long-delayed projects, other program areas have been slower to show results. In this regard, weatherization is the poster child. Federal weatherization efforts transformed suddenly from miniscule to multi-billion dollars. States have had difficulty ramping up. By November, for example, Texas had spent just $1.8 million of $163 million available, weatherizing a grand total of seven
homes statewide.

Texas officials pledge to do better this year. They might learn from the example set in Washington state, which also fell badly behind schedule last year. At summer’s end, local agencies had weatherized just 10 percent of the units the state had planned. The problem drew the attention of Gregoire’s office, which helped untangle some of the regulatory and labor law problems that were hampering efforts. By the end of the year, the state had exceeded its targeted goals.

Washington’s Department of Community, Trade and Economic Development is now looking to contract directly for weatherization of large, multi-unit buildings. The department hasn’t typically been involved directly in contracting, Satran said, but it wants to handle major accounts itself rather than relying exclusively on local entities, so that it will be positioned to ease its efforts as the flood of federal weatherization dollars becomes a trickle after this year.

**After the Money is Gone**

Adjusting to the cliff effect of stimulus funds running out is going to be a challenge for states more generally. The Recovery Act helped states get through their worst patch in memory, but because revenues have not yet picked up, budget writers are going to have a hard time doing without the big influx of federal dollars.

States still seem to lack the political will to impose sales tax on services, but many states are starting to take a hard look at other fundamental changes. Californians are likely to vote on various reform measures this year, including a constitutional convention. Calls for constitutional conventions are also mounting in New York and Pennsylvania, while major overhauls of state governance structures and tax systems are receiving serious attention in Michigan, Ohio and Illinois.

Still, most state lawmakers are muddling through, seeking short-term solutions to what increasingly look like structural problems. In this regard, the Recovery Act has made the job states face in adjusting to an era of diminished budgetary expectations harder, by precluding them from making program cuts in core areas such as education, transportation and health care.

“There are really some tough decisions out there to be made,” said Emler of Kansas.

He said the stimulus allowed states to delay that decision-making, which is one of the biggest reasons it’s hard to say the Recovery Act, despite its many positive effects, was a complete success.
State policymakers toppled hurdles that had stymied them for years as they joined the Race to the Top for a piece of a $4 billion federal pie.

But those hurdles—such as linking student performance to teacher pay, lifting caps on charter schools and making it easier for states to take over failing schools—may only have fallen in certain parts of the country. Some states are racing to compete for the funding in the 2009 Recovery Act, while others are left at the starting gate.

Will Race to the Top funding mean lasting changes for education in this country? That answer may depend on where you live.

**Race to the Top, Strings Attached**

Congress set aside $4.35 billion in the Recovery Act for Race to the Top, a highly competitive grant program designed to reward states that have taken bold steps toward education reform. To qualify, states had to demonstrate a “comprehensive approach to education reform,” according to the application.

Given most states’ financial situations, the lure of more money has been a strong one. But strings attached to the funding tempered that draw in many areas. Texas Gov. Rick Perry, for instance, cited those strings when he pulled his state’s application.

Michael Griffith, senior policy analyst at the Education Commission of the States, said many of the requirements were highly unpopular. Among them: Tying teachers to student achievement data.

“This was a big sticking point,” said Griffith. “There were states where teacher organizations lobbied and pushed through legislation that said you cannot have any policy that creates this tie between teachers and student achievement.”

Making other changes, while not required, improve a state’s chance to win. States can earn up to 40 points, out of a total of 500, by lifting caps or bans on charter schools. Fifteen points are awarded to states that emphasize science, technology, engineering and math, or STEM, education.

**Some States Already On the Road**

Griffith said Colorado is considered to be one of the frontrunners for funding. Colorado Lt. Gov. Barbara O’Brien said teachers and state officials threw their full support behind the state’s application. She said it is just an extension of the education reforms she and Gov. Bill Ritter have been working on since 2007.

“We went at this with full bore enthusiasm, because we had such a good framework,” said O’Brien. “That means the legislature was on board; we had the support of the districts. Race to the Top pushed us to go even further.”

O’Brien said if the grant opportunity hadn’t come along, the state would be left trying to incrementally implement plans. “This really made us focus on where we want to be in a couple of years if we get this grant.”

O’Brien said Colorado must cut $260 million from the K-12 budget this year, but even if the state doesn’t receive Race to the Top funding, officials there plan to move ahead with many of the ideas in the application.

Kentucky policymakers share many of the same beliefs as those in Colorado. Kentucky was the first state to adopt the Common Core State Standards, which states must use to receive Race to the Top funding. State education agencies voted unanimously Feb. 10 to adopt the standards.

**LEARN MORE** about the Common Core State Standards Initiative states must participate in to qualify for the federal Race to the Top funding in the February Stateline Midwest story about the new state-led initiatives, available at [www.csg.midwest.org](http://www.csg.midwest.org).

**REGISTER** for a CSG Webinar March 10 on the Common Core State Standards Initiative at [www.csg.org](http://www.csg.org).
Kentucky has a head start in the funding race, said Lisa Gross, director of the Communications Division for the Kentucky Department of Education. “...The kinds of things Race to the Top calls for, we were moving in that direction anyway. We had to make sure that it was all codified and set in concrete,” she said.

Some States Left in Starting Gate
That’s not the story in other states.
North Dakota Lt. Gov. Jack Dalrymple, who chairs the North Dakota Commission on Education Improvement, said charter schools were an issue in his state. North Dakota has alternative schools, which are similar to charter schools, but those schools remain under control of local school districts. Dalrymple believes that difference alone would be enough to disqualify the state’s application. North Dakota did not apply for first round funding.

Dalrymple also believes the Race to the Top program is not designed for smaller, more rural states like his. Not only would it be difficult to fulfill the program requirements, he said, but it would also be difficult to devote enough staff to complete the estimated 600 hours it takes to complete the application.

“...We’re having a real dilemma,” he said. “We don’t want to seem like we’re not trying out here. We’re actually very proud of the progress we’ve made. ... We don’t know whether we should apply and then be turned down—at least then we’d get credit for having the right attitude—or just not do it.”

Indiana Rep. Greg Porter has issues with how his state handled the Race to the Top application. He said the legislature was asked to sign a letter of support for the application even though legislators did not have a clear picture of what the state was promising. Neither did local school districts, which were asked to sign a memorandum of understanding to show their support.

The state superintendent and governor’s office worked on the application and released few details, Porter said. The explanation for not sharing details with local districts was that it would also let other states know what was in the application.

“Schools did (sign the memorandums), but under duress. They did send letters of support, but they were general letters,” Porter said.
Florida faced similar lukewarm support. While most Florida school districts signed onto the state’s application, most local teachers unions opposed it.

Lasting Change Not Guaranteed
Griffith, of the Education Commission of the States, expects any lasting changes to education to be a mixed bag.

“I think obviously, anyone who wins is going to have to stay with all the changes,” he said. “I think some of those who don’t win will just continue on with the changes. They were looking for a reason to make these changes to begin with in some states. ... I think some states will keep some of them and retract others.”

PRESIDENT OBAMA VISITS GRAHAM ROAD ELEMENTARY SCHOOL
FALLS CHURCH, VA.—President Barack Obama and Secretary of Education Arne Duncan visit with sixth grade students at the Graham Road Elementary School in Falls Church, Va., in February. After he met with the students, the president delivered remarks on his “Race To The Top” program and his request for an additional $1.35 billion in 2011 for the program.

Photo: Kristoffer Tripplaar/Pool/SIPA USA/Corbis
New Hampshire has a low crime rate that has remained stable for years. So why is the number of people we incarcerate growing?

In the last 10 years, New Hampshire has seen a 3 percent increase in the number of offenders sent to prison for new offenses—and yet our prison population has grown by 26 percent.

Why has our corrections system turned into one of the leading cost drivers for our state budget and is there anything we can do to change that without endangering public safety?

These questions and others led lawmakers to reach out to The Council of State Governments Justice Center and its funders at the Pew Center on the States and the Department of Justice/Bureau of Justice Assistance. We invited researchers here last year to give a presentation on their work in other states. This year, we were very fortunate that our state was chosen for a three-year study that will allow for data collection, study and recommendations for improving our criminal justice system. Not only that, the study will include follow-up once changes are implemented to make sure they work.

As the head of the Interagency Coordinating Council for Women Offenders, I’ve long wanted this kind of data-based review to help us improve public safety and reduce costs. We need to understand our problem and target our resources to be most effective. I am optimistic we can make significant progress on this issue in 2010.

Since the Justice Reinvestment Initiative was launched, CSG Justice Center researchers have been meeting with state and county officials, law enforcement, behavioral health professionals, lawyers, judges and victim advocates to get a broad picture of how our system works.

One early finding points to a problem with how we handle people on probation and parole. We are revoking probation and parole and sending a record number back to prison. These revocations now account for about 57 percent of all admissions.

The majority do not involve commission of new crimes but technical violations of the rules laid out for the parolee or probationer. Furthermore, the revocation rate varies widely by county—why do some counties send more of their folks back to prison than others?

We don’t have answers to these questions yet, but what’s important is that we’re looking for them.

The researchers concluded that parole revocations will cost our state about $13.3 million in 2009. Would some of that money be better spent on community-based programs that treat underlying problems such as addiction and mental illness that challenge parolees and probationers?

The costs are likely even higher when we talk about women offenders with children. When women go to prison, someone has to care for their kids. Sometimes that’s a relative, but often the state must step in and find the kids a temporary home. The emotional suffering makes it that much harder for these youngsters to succeed in their own lives and research demonstrates they are at increased risk of becoming the offenders of the future.

While women make up a smaller portion of all offenders, their numbers are growing so we’d be wise to find ways to successfully treat and maintain or reunite families where possible.

CSG Justice Center researchers found that community-based treatment is generally more effective than prison-based treatment in preventing recidivism. What does this mean for how we allocate state dollars to get the most for our money?

I and my fellow lawmakers see a big potential payoff to the state if we can find more effective ways to target our money. Some money must continue to go to our prisons because society still needs to be protected from violent predators and other dangerous criminals. But can we do a better and more cost-effective job of treating other offenders and thus keep all of us safer and better able to lead productive lives?

The Justice Reinvestment Initiative is our best hope for the data we need to make these decisions. We want to keep our low crime rate but we also want to stop pouring money into a criminal justice system if it only recycles offenders.
CASE STUDIES

Kansas

THE SITUATION
» In 2007 the Kansas prison population was expected to increase 22 percent by 2016 at a cost of approximately $500 million in additional construction and operating costs.
» The CSG Justice Center found parole and probation revocations accounted for 65 percent of prison admissions.

THE ACTION
» During the 2007 legislative session, state policymakers approved policies designed to reduce the risk of individuals under supervision and directed $7.9 million to expand treatment programs and strengthen probation and parole.

RESULTS
» From 2007 to 2009, the state prison population declined by 4 percent.
» The average monthly number of parole revocations to prison for condition violations declined 53 percent from 2003 to 2009.
» The probation revocation rate declined 28 percent between the 2006 fiscal year and the 2009 fiscal year.
» The decline in the prison population enabled policymakers to close several smaller facilities in 2009 to help narrow the state budget gap.

Texas

THE SITUATION
» In 2007, Texas’ prison population was projected to grow by more than 14,000 people over the next five years.
» The CSG Justice Center conducted a detailed analysis and suggested policy options.

THE ACTION
» State lawmakers in 2007 enacted a comprehensive policy package to avert the anticipated prison population growth, including $241 million to expand substance abuse and mental health treatment and diversion programs.

RESULTS
» The state saved $443 million.
» The number of people on probation and parole who have been returned to prison has decreased significantly.
» The prison population stabilized and isn’t projected to grow.
» The state canceled plans to build additional prisons.
» Crime rates in nearly every major urban area in Texas have declined.

Data are Basis for Spending Cuts

Justice Reinvestment is the term coined for a data-driven approach to reduce corrections spending and use those savings for strategies that can decrease crime and strengthen neighborhoods.

The Council of State Governments Justice Center, with support from a diverse group of public agencies and private foundations, helps state and local policymakers use a justice reinvestment approach to increase public safety.

To get started, policymakers establish a small, high-level, interbranch, bicameral and bipartisan team of elected and appointed officials to work with the CSG Justice Center’s nationally recognized criminal justice policy experts. These experts then consult with a broad range of stakeholders including prosecutors, public defenders, judges, corrections and law enforcement officials, service providers and community leaders, victims and their advocates, people who have been incarcerated, and health, housing, human service, education and work force professionals.

Together, the policymakers, experts and stakeholders analyze data and develop policy options; adopt new policies and put reinvestment strategies in place; and measure performance.
"The combination of falling revenues, which accompany high unemployment, and an explosion in Medicaid enrollment, which occurs very late in an economic downturn, explain why a recession's greatest impact on state budgets occurs one to two years after the downturn is over."

—Ray Scheppach, National Governors Association

The fiscal condition of states deteriorated dramatically over the last two years because of the depth and length of the economic downturn, and state officials do not expect this situation to improve any time soon. Previous downturns have proved that the worst budget years for a state are the two years after the national recession is declared over. States’ recoveries from the current recession, however, may be prolonged, with most economists projecting a slow and potentially jobless national recovery.

Moreover, even when recovery begins, states will continue to struggle because they will need to replenish retiree pension and health care trust funds and finance maintenance, technology and infrastructure investments that were deferred during the crisis. They will also need to rebuild contingency or rainy day funds, and both implement and pay a portion of the Medicaid expansion under national health care reform.

The bottom line is that states will not fully recover from this recession until very late in this decade.

The Current Situation

The recent economic downturn started in December 2007 and likely ended in August or September 2009, making it one of the deepest and longest since the Great Depression. State revenues were down 4 percent in the last quarter of 2008, and 11.7, 16.6 and 10.9 percent in the first three quarters of 2009. These findings are consistent with the National Governors Association and the National Association of State Budget Officers joint publication, the Fiscal Survey of States, estimate that state revenues declined 7.5 percent in the 2009 fiscal year, which for most states ended June 30, 2009.

Revenues will likely continue down for another one or two quarters before turning up slowly. This precipitous drop in state revenues is consistent with past recessions in which the trough in state revenue generally coincides with the peak in unemployment. Most economists forecast unemployment will continue to increase into the first quarter of 2010.

Similarly, Medicaid spending, which is about 22 percent of state budgets, averaged 7.9 percent growth in the 2009 fiscal year, its highest rate since the end of the last downturn six years ago. Medicaid enrollment is also spiking, with projected growth of 6.6 percent in the 2010 fiscal year compared with 5.4 percent in 2009. The combination of falling revenues, which accompany high unemployment, and an explosion in Medicaid enrollment, which occurs very late in an economic downturn, explain why a recession’s greatest impact on state budgets occurs one to two years after the downturn is over.

States’ budget problems are reflected in the latest Fiscal Survey of States, which shows states closed budget gaps of $72.7 billion in the 2009 fiscal year and $113.1 billion in the 2010 fiscal year. This includes tax and fee increases of $23.8 billion in 2010. Even with cuts and tax increases, states are experiencing new budget shortfalls totaling $14.5 billion for 2010 and $21.9 billion for 2011. However, these projected shortfalls will increase dramatically over the next several months.

The American Recovery and Reinvestment Act

Of the $878 billion in Recovery Act funds, about $246 billion came to or through states in more than 40 programs. Most importantly, the $87 billion in Medicaid funds and the $48 billion in state stabilization funds were flexible and allowed states to offset planned budget cuts and tax increases. The Medicaid funds allowed states to reprogram state funds that were originally to fund Medicaid expansions, while the education money was targeted for elementary, secondary and higher education, which represents about one-third of state spending. If Congress had not made these funds available, state budget cuts and tax increases would have been much

by Ray Scheppach, Executive Director, National Governors Association
more draconian and devastating to state governments, their employees and citizens. States must plan for the serious cliff in revenues they will face when Recovery Act dollars expire.

The Recovery Period
While there is still uncertainty regarding the shape of the recovery, there seems to be a growing consensus that it will be slow. Numerous studies project that state revenues will likely not recover until 2014 or 2015. A recent forecast by Mark Zandi at Moody’s economy.com showed that the national unemployment rate, which straddled 5.5 percent during the 2001 to 2007 period, will not attain that level again until 2014. Similarly, Zandi’s forecast in January indicated state revenues will not return to the 2008 level in real terms until the 2013 fiscal year. Until employment improves, state revenues will continue to struggle. Work by the Nelson A. Rockefeller Institute of Government similarly indicates that per capita real revenues will not reach the 2007 level until 2014. Making matters worse, economist Robert Kuttner indicated that the states’ fiscal shortfalls will be about $350 billion over the next several years.

Deferred Investments
Even when recovery begins in the 2014 to 2015 period, states will be faced with a huge overhang in needs and will have to accelerate payments into their retiree pension and health care trust funds, as well as fund deferred maintenance and technology and infrastructure investments. They will also have to rebuild contingency or rainy day funds. All of these needs were postponed or deferred during the 2009 to 2011 period and will have to be made up toward the end of the decade. According to a recent Pew Center on the States report, states have an outstanding liability of about $3.35 trillion in employee retirement, health and other benefits coming due over the next several decades, of which more than $1 trillion is unfunded.

Medicaid Expansion
In 2014, states would have to expand Medicaid to all individuals below 133 percent of poverty as part of the Senate health care reform bill. For the newly eligible population of about 11 million individuals, the federal government will pay an enhanced match, which will average about 90 percent, if the Senate provisions prevail in the final bill. Unfortunately, the state’s share of this over the next decade is about $25 billion, according to the Congressional Budget Office. Moreover, states will incur other substantial costs as the 3 million to 4 million people currently eligible for—but not enrolled in—Medicaid come onto the rolls. Despite this projected increase in Medicaid participation, states would receive only their normal federal match. Furthermore, if states are forced to increase provider reimbursement rates to maintain access, they will only receive their normal match for this cost.
SOMETHING HAS TO GIVE

Scott Pattison
Executive Director
National Association of State Budget Officers

“Citizens and their elected representatives are going to need—over the next few years, because of the tight budget situations—to just step back and decide what is the role of government in the state and what should the state provide and what should the state not provide, because it’s going to have a huge bearing on whether taxes are raised or kept the same, whether certain things are going to need to be cut. I think there needs to be an acceptance and an understanding that there’s not enough money to do everything everybody wants state government to do. Something has got to give.”

BUDGETING IS A DIFFICULT BALANCE

Rep. Maxine Bell
Co-chair of the Joint Committee on Finance Appropriations, Idaho
Co-chair of CSG’s National Finance Committee

“We have core responsibilities, health and safety and education, and in a short budget year you cannot fully fund one of those core responsibilities to the detriment of the other responsibilities. It’s a terribly difficult balance. That little old person who is retired and lives on a back street in a small town, they only want to be safe. And yet there’s the family down the street with two or three bright little kids, and they only want them to be educated. They don’t ever seem to meet together and understand the issues from the other person’s point of view. We sit here and we see all those points of view and then we kind of muddle through it.”
**STRUCTURAL CHANGE IS NEEDED**

Sen. Susan Bartlett  
Chair of the Senate Committee on Appropriations  
Vermont  

“Government is always talking about structural change, but we don’t ever very often seem to get there until it hits the fan. We’ve already made a lot of reductions in services and this year we’re going to see a lot more in the way of reductions of services to folks. If we ever want to replace those services, we have to significantly restructure how we offer those services so we can do them in a much more affordable manner.”

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**GET BACK TO BASICS**

Sen. Randy McNally  
Chair of the Senate Committee on Finance Ways and Means  
Tennessee  

“I think certainly expectations should be lowered and I think that to the extent we can get back to our basic answering the basic needs of the people—such as education and public safety, mental health, developmental disabilities—that’s where we need to be. ... Having cycles in which you have growth and then you have downturns, it’s not all that bad because one can function, cut to more essential programs, and then in the good times if you’re smart you can either return the money to the taxpayers or make sure … your reserves are strong and adequate because there will always be the ups and downs.”

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**MANY TOOK SERVICES FOR GRANTED**

Sen. Donne Trotter  
Chair of the Senate Committee on Appropriations  
Illinois  

“Our coffers are bare. We just haven’t been able to keep up with the economic crisis. … When people aren’t working, they aren’t purchasing; when they aren’t purchasing, we aren’t generating taxes. When we aren’t generating taxes, it means we aren’t generating revenues to pay for those services that people need and expect. So the national (and) international crisis is exacerbated with our own critical needs here in Illinois. When people aren’t working, they become more dependent on the services that many just took for granted because they were there ...”
REGISTER!
EDUCATION WEBINAR
Learn more about Common Core State Standards that states must participate in to compete for federal stimulus Race to the Top funds at The Council of State Governments’ education policy group’s webinar March 10. Common Core State Standards are intended to provide a common rigorous set of standards that will ensure every student is prepared for college or a career, regardless of background. Register at www.csg.org.

Remember These Dates!
CSG South:
July 31-Aug 4, Charleston, S.C.
CSG Midwest:
Aug. 8-11, Toronto, Ontario
CSG East:
Aug. 15-19, Portland, Maine
CSG West:
Sept. 11-14, Sun Valley, Idaho

https://secured.csg.org/csg/Spring2010

Register!!!
POLLICY TALK ON CANCER, STROKE TREATMENT

Legislators from 18 states gathered at a CSG Health Policy Forum in December to learn about state policy solutions for cancer and stroke treatment. Advocate Heather Kirk shared her family’s crusade in Oregon to pass the first state law guaranteeing insurance coverage for oral therapy treatment of cancer equal to traditional chemotherapies. Illinois Rep. Tim Schmitz, a firefighter and emergency medical technician, explained his bill to allow ambulances to bypass the nearest hospital to take suspected stroke victims to a hospital specializing in stroke treatment.

CSG LEGISLATIVE MANAGEMENT TRAINING

Nonpartisan legislative service agency and research directors from The Council of State Governments Western and Southern regions joined forces last fall for a training seminar in La Quinta, Calif. Highlights included a social networking discussion, “To Tweet or Not to Tweet,” by Washington Senate Counsel Mike Hoover.
Texas will be the big winner when the U.S. Census Bureau releases population counts next year.

The Lone Star State will pick up three Congressional seats—the biggest gain since statehood in 1845, according to projections from William Frey, an internationally known demographer at the Brookings Institution.

“(Texas) just happened to survive this housing bubble … its housing prices didn’t peak as rapidly as these other places and then it didn’t decline as much and its economy stayed pretty strong for most of the decade,” Frey said. That meant Texas was able to attract new residents, and it didn’t lose any.

In addition, Texas picked up residents following Hurricane Katrina, when many residents from neighboring Louisiana crossed the border for safety and stayed, he said. That’ll hurt Louisiana, which is likely to lose a congressional seat.

Economy Changes Census Projections

Louisiana isn’t alone in the loss column, and other states won’t see their usual growth patterns.

For the first time since the 1920 census, California won’t pick up a congressional seat, Frey said. California has been a big winner in the decennial census for the past nine counts. But its growth has slowed over the years, Frey said.

“Although they’ve grown in population because they’ve gained immigrants … they have lost internal migrants to other states,” he said. “Some of that has to be the growth of the rest of the West because of the relatively high housing costs in California compared to states like Nevada and Arizona.”

Other sunbelt states will pick up seats, which are based on census population counts, but it’s a different picture than it would have been if mid-decade projections had held. Projections changed when the economy slipped over the past few years because people haven’t been moving to other states.

“There’s always been, for 30 or 40 years, a big snowbelt to sunbelt shift,” said Frey. “It got the brakes put on in the last few years because of the recession and mortgage meltdown (because people tended to stay put).”

That’s good news for some snowbelt states, like New York, which was projected to lose two seats midway through the decade but now is projected to lose only one.

But states that suffered when the housing bubble burst will continue to feel the effects, Frey said.

Florida was expected to gain three congressional seats based on growing population numbers, but now is expected to gain only one, its smallest gain since 1940.

Arizona will gain one seat rather than two had the mid-decade projections held.

Nevada is gaining a seat, but likely would have gained more had it not been for the economic situation.

“We have the northern part of the country still losing to the South and West,” said Frey. And those population shifts have been more widespread in those two regions, according to Frey.

Frey based his projections in part on the American Community Survey, an annual count from the Census Bureau. The official numbers won’t be available until 2011 when the Census Bureau will release the bulk of information garnered in the census, which officially begins in March.

Redistricting

The new population counts don’t just affect congressional boundaries. States also drew the lines for legislative districts every 10 years.

“By rules of the states, some of these have to be within points of a percentage,” said Richard M. Leadbeater, industry solutions manager for ESRI, a software company that specializes in geographic tools and works with state governments and federal agencies to tie population databases to geography.

“Think about drawing those boundaries and trying to get that level of similarity between all those boundaries …,” he said.

Having geographic information to match with the population information helps in redistricting, he said.

Redistricting has been a primary mover of the use of GIS in state government, Leadbeater said.

“The census alone has hundreds of attributes about the households they count and states have to process that,” he said.

Processing that information can provide invaluable information to states, he said. Leadbeater believes redistricting should be the beginning of the process, not the end, because of the database rich with information about a state’s residents.

“Wouldn’t it be nice for policymakers to understand their constituents a little better and use that data in policymaking?” he said.
There’s always been, for 30 or 40 years, a big snowbelt to sunbelt shift. It got the brakes put on in the last few years because of the recession and mortgage meltdown (because people tended to stay put).”

—William Frey, demographer at the Brookings Institution
REAPPORPTIONMENT 101

What is Apportionment?
Apportionment is the process of allocating seats in a state legislature and the U.S. House of Representatives based on population.

How is it Determined?
The U.S. Census is the basis for apportioning seats. On the federal level, each state is assigned one representative, and the remaining 385 seats are split among the states based on a formula using each state’s apportionment population. On the state level, most states maintain a fixed number of legislators, while some allow the number to change as population grows or shrinks.

What is the Apportionment Population?
The apportionment population is the total resident population—both citizens and noncitizens—in the 50 states. Residents in Washington, D.C., Puerto Rico and the U.S. island areas are excluded from this count because they do not have voting seats in the U.S. House of Representatives.

What About Citizens Living Overseas?
U.S. Armed Services personnel and federal civilian employees stationed outside the U.S.—and their dependents living with them—are counted if they can be allocated, based on administrative records, back to a home state.

What is Redistricting?
Every 10 years, district lines are redrawn to reflect population shifts based on the census data. This is done for both congressional seats and state legislative seats.

When Do States Receive Information?
The Census Bureau will start sending data to states in March 2011. By statute, states must receive that information by April 1, 2011.

When are Redistricting Plans Due?
Each state has a different deadline, but it’s usually at the end of the legislative session after they receive the census information, and most states complete the process by 2012. Maine and Montana are scheduled to finish the process by 2013.

Who Redraws the Lines?
In most states, state legislatures have the responsibility to create the boundaries for their own districts and for the state’s congressmen. In 22 states, special commissions take part in the redistricting process. In five of those states—Alaska, Arizona, Idaho, Montana and Washington—independent commissions are tasked with the responsibility to draw legislative boundaries.

Do the Courts Play a Role?
In three states—Alaska, Colorado and Mississippi—the chief justice appoints at least one of the commissioners redrawing district lines. In New Jersey, the chief justice will appoint a tiebreaker if the bipartisan commissioners cannot agree on a plan.

Do Courts Review the Boundaries?
Three states—Colorado, Florida and Kansas—require automatic review of redistricting plans by the Supreme Court, while Washington calls for an automatic review if the plan is late. Fourteen other states—and Washington if the plan is completed on time—allow review upon request. Vermont requires at least five people make the request before the Supreme Court will review the plans.

Can the Governor Veto the Plan?
In 17 states, the governor can veto the redistricting plan recommended by the legislature or special commission.

Sources:
U.S. Census Bureau
Governor’s Races
- Governors & Executive Branch
- Governor’s Races on the Ballot
- Other Executive Branch Officers, But No Governor’s Race
- No State Races on the Ballot

Other Jurisdictions
- Guam—Governors & Executive Branch
- U.S. Virgin Islands—Governor’s Races on the Ballot

Legislative Races
- House & Senate
- House Only
- Unicameral
- No State Races on the Ballot

Other Jurisdictions
- American Samoa—House & Senate
- U.S. Virgin Islands—Unicameral

U.S. Senate
- Senate
- No Races on the Ballot

Governor’s races are on the ballot in 37 states and two territories. In 15 of those states and territories, incumbent governors are seeking re-election, while 23 leaders are retiring or are term-limited; Florida Gov. Charlie Crist is running for the U.S. Senate. The full membership of the lower house of the legislatures in 44 states or territories is up for election this year, while 47 of 94 North Dakota House seats are on the ballot; that’s 4,936 seats across the country. In the Senate—or unicameral body in Nebraska and U.S. Virgin Islands—all seats are up in 18 states or territories, half in 26 states or territories and none in 10 states or territories; that’s 1,185 seats on the ballot.
Engage Your Constituents

BEYOND THE USUAL SUSPECTS

Archon Fung, a professor at Harvard’s Kennedy School of Government, is an expert on civic participation and public deliberation. He looks at all sorts of ways people are getting involved in policymaking and the policy process—that’s where the public meeting comes in. Here are Fung’s tips on how to make one successful.

**BE CLEAR ON THE PURPOSE.**
The most common bad reason to hold a public meeting is because public officials think they should. “They’re basically either literally or figuratively checking off a box on a list of things that they ought to do,” Fung said. If public officials don’t know what people think about an issue and if government needs public participation to get its job done (think recycling, for example), those are good reasons to hold a public meeting, he said.

**GET HELP.**
Meetings are an art. Many resources are available to organize and conduct a town hall meeting to meet specific purposes, Fung said. Organizations like Everyday Democracy, Deliberative Democracy Consortium, National Coalition for Dialogue & Deliberation and the International Association for Public Participation are a few that offer such resources. (Visit capitolideas.csg.org to link to these resources.)

**AVOID THE USUAL FORMAT.**
Typical town hall meetings are announced, open to anyone and a brief, official talk is followed by a question and answer period. But that common format is bad, Fung said. Why? “Usually you hear from people who have already made up their minds before they even walked in the room and just want to express themselves,” he said. So again, get help. “There’s no magic chocolate chip cookie recipe—there are many good ways to do it,” Fung said.

**GO BEYOND THE USUALS.**
People who have a deep interest in the issue and people who have more money and stable employment, and those who are better educated tend to go to public meetings, Fung said. Publicize and advertise the meeting in communities and with organizations that reach people not normally heard from, he said.

**AVOID PROMISES YOU CAN’T KEEP.**
Be clear about how information from the public meeting will be used, Fung said. At the end of the day is it the public official’s call? Or, is there a promise to use information or suggestions? Let people know up front and stick to it, Fung said. Otherwise, the danger is people could get frustrated and stop attending such meetings, Fung said.

**GIVE US YOUR INPUT**
Share your tips for holding an effective town hall meeting at capitolideas@csg.org. We’ll post your insights on the CSG Website to share with other state leaders.

“Do the best you can to engage people who wouldn’t ordinarily show up. The one problem with ... almost all forms of public engagement, almost all town meetings and public hearings, is that only certain types of people tend to go.”

—Archon Fung
National and Regional Meetings

Registration and application deadlines may apply. Visit www.csg.org/events for complete details.

CSG WEST ANNUAL CONFERENCE
Sept. 11–14, 2010 • Sun Valley, Idaho

CSG-WEST WESTERN LEGISLATIVE ACADEMY
July 12–15, 2010 • Colorado Springs, Colo.

NEMA ANNUAL CONFERENCE

BOWHAY INSTITUTE FOR LEGISLATIVE LEADERSHIP DEVELOPMENT
July 9–13, 2010 • Madison, Wis.

CSG MIDWEST ANNUAL CONFERENCE
Aug. 8–11, 2010 • Toronto, Ont.

CSG 2010 ECONOMIC SUMMIT OF THE STATES
May 20–23, 2010 • New York City, N.Y.

Hotel cut-off and early registration deadline is April 27.
Mark your calendars to join us at the crossroads of technology, commerce, innovation and creativity—New York City. Under the backdrop of one of America’s most celebrated and diverse cities, state leaders from across the country will gather to exchange ideas, debate tough issues and develop creative solutions. If you can make it here—we’ll give you the tools to make it anywhere. Come be a part of it!

CSG 2010 NATIONAL CONFERENCE
Dec. 4–7, 2010 • Providence, R.I.

State leaders will come together in Providence, R.I., to learn from each other and nationally recognized experts as the Ocean State plays host to the CSG 2010 National Conference. You cannot afford to miss this important opportunity to discuss solutions, enhance results, and improve accountability. This meeting is designed to empower you to be an even more effective public servant.
Nashville native Douglas Henry served two years in the Tennessee House of Representatives in the 1950s, then left after one term to practice law. But he enjoyed his time serving his district, so when the 21st District Senate seat came open in 1971, Henry decided to run. He’s now the Senate’s longest-serving member. After nearly four decades, Henry still enjoys the office, except for the growing partisanship in government. His long experience taught him a lot about dealing with people. Henry, a former chairman of the Southern Legislative Conference of The Council of State Governments and member of various CSG boards and committees, said his best advice applies to everything in life, not just politics: “Always tell the truth so that your word is good,” he said. “If your word is good, people respect that. If your word is not good, you’ve wasted your most precious asset.”
i firmly believe the Toll fellowship Program is an excellent resource for anyone hoping to better their leadership capability as well as build their character.

2010 Economic Summit of the States

Hotel Cut-Off & Early Registration Deadline: APRIL 27

www.csg.org/events