Budget crisis racks state and local politics across U.S.

by Andrew Rotstein

A wave of state and local budget crises is breaking out around the United States, bringing gruesome cuts in essential services and politically explosive moves to increase revenues. Citizen outrage is on the rise, threatening or sweeping away political careers in the process.

In late March, Standard & Poor's, the nation's leading financial rating service, lowered New York State's bond rating two notches in one jarring stroke. The new rating is the lowest in New York's history, and places it third from the bottom among rated states, trailed only by basket cases Louisiana and Massachusetts. The downgrade immediately added an estimated $10 million in interest costs to $775 million in deficit notes issued by the state two days later. It is widely viewed as a major liability to the presidential ambitions of Gov. Mario Cuomo.

The same day, New York City Mayor David Dinkins announced $75 million in budget cuts, heavily hitting education, social services, and the beleaguered public hospital system (see *EIR* Investigation, March 9). He still faces a mammoth gap for the coming fiscal year of $1.8 billion—arguably worse than the bankruptcy crisis of 1975. Within days, the drop in the state's bond rating prompted Albany to cut $100 million in aid to the City.

Budget squeezes determine politics

One week earlier, Connecticut Gov. William O'Neill announced he will not seek a third term, explicitly citing voter backlash from $1 billion in new taxes he sponsored. In mid-March, West Virginia was hit by a statewide teachers' strike over the issue of pay, and while the teachers have returned to work, a promised special session of the legislature has not even been scheduled yet. The slow response of state house leaders is understandable in one sense: they already have to cut 2.4% of current expenditures to balance the books.

Drastic increases in property tax assessments have triggered a homeowners' revolt in suburban Washington, D.C. in recent weeks. The prevailing sentiment of a spate of mass meetings to "oust all incumbents" has already forced two counties to rescind the hikes. Newly elected New Jersey Gov. James Florio has asked for a whopping $2 billion in new taxes, including a doubling of the state tax on incomes over $100,000. In the November gubernatorial election in Illinois, Republican nominee Jim Edgar is considered vulnerable because of his endorsement of a permanent rise in the state income tax.

Perhaps most emblematic of the trend is the fate of Massachusetts Gov. Michael Dukakis. Just two years ago, Dukakis used his credentials as the maestro of the state's resurgent economy to capture the Democratic presidential nomination. The recurring phrase from his stump speech, "In my state . . .," still echoes in the mind.

Today, the image of Massachusetts has gone from "miracle" through "mirage" to "mess." Its bond rating is the lowest in the nation, and the thrice-elected Dukakis is an object of unmatched bitterness and ridicule, not least from his former allies. Dukakis has proposed a series of severely austere budgets, the last of which was described by his own secretary of administration, L. Edward Lashman, as "draconian, appalling, disgraceful, hideous, frightening."

Small wonder the Republicans are given good chances of electing his successor, although no Republican has won statewide office in 18 years.

The economic underpinning

Although the budget squeeze is most extreme in the Northeast, it is also the worst on a national scale since the depths of the 1982 recession. According to the National Conference of State Legislatures, eight states are running major deficits, and 19 others are collecting revenues substantially below expectations.

The current problems evince an economic slowdown far more serious than that suggested by standard indicators. For example, Northeastern states officially show an unemployment level that is stable at just under the 5.3% national average. Yet, just two weeks after proposing his $51 billion budget in January, New York's Governor Cuomo announced that tax receipts were grossly overestimated, and a $1.5 billion gap had to be filled. In Massachusetts, 1989 sales taxes were $200 million below estimates, Connecticut's were $300 million under projections, New Jersey's $200 million short. And the trend is worsening. In at least three states, 1990 sales tax receipts are expected to run *lower* than last year's, in Massachusetts by 5%. Income tax revenues also lagged expectations, by over $1 billion in New York, by $200 million in Massachusetts.

There is clearly a slump in industries like defense production, computers, construction, and financial services. The fall-off in home construction in turn affects purchases of building materials, furniture, and appliances—all taxable big-ticket items.

Other factors are likely at work. Many workers in the service sector are self-employed or work on commission, and may experience falling incomes without showing up in jobless statistics. The slump in sales tax receipts may reflect a saturation level in consumer debt, and falling corporate profits further crimp revenues.

Shift to the states

While the Reagan and Bush administrations have rhapsodized about "lower federal deficits" as proof of their policies' success, careful scrutiny shows that a portion of the mission of government has simply been shunted to states and localities. In 1986, for example, federal revenue sharing was terminated. Typically, where New York City received 16% of its budget from the federal government in 1981, such aid accounts for only 9.6% today.

But although financial flows from Washington have abated, new federal policies have mandated higher expenditures by state and municipal administrations. Environmental regulations regarding solid waste disposal and new directives in the Medicaid program have required heavy additional outlays, only a fraction of which the feds have provided.

Thus, between 1980 and 1987, while federal income taxes on individuals fell from 8.9% of Gross Domestic Product to 7.9%, and federal corporate income taxes dropped from 2.3% to 1.7% of GDP, the revenues upon which states, counties, and cities depend rose relative to GDP: property taxes, from 2.6 to 2.8%; sales taxes, from 2.0 to 2.2%; and personal income taxes, from 1.5 to 1.7%.

This shift was cheerfully promoted by the Reagan administration as "The New Federalism." But to countless public officials, stuck with additional responsibilities but even fewer resources, it was a betrayal of the traditional federal-state partnership, and another bit of deception by which the actual magnitude of the federal deficit is disguised. One lobbyist for the National League of Cities termed it "a kinder and gentler shaft."

The resulting pattern is stark. State and municipal budgets taken aggregately have gone from a surplus of $20 billion in 1984, to a $7 billion surplus in 1986, to a $15 billion deficit by 1988. Now, the Commerce Department projects a staggering $35 billion shortfall for 1990.

Bookkeeping shenanigans

Because 49 of 50 states are constitutionally required to balance their budgets, spending cuts and tax incerases, not deficit financing, are the rule. Counties and municipalities are forced to rely heavily on property taxes, and such revenues have increased over 10% annually in the 1980s. Especially as the bubble in real estate values inflated, assessed values and/or millage rates went up. But now, especially where property values have leveled off, if not fallen, homeowners are in revolt. So, taxes on alcohol and tobacco, user fees, real estate transfer taxes, and registration and licensing fees of every sort are on the rise.

Like the federal government, which has become notorious for its perennial "smoke and mirrors" games to conceal the deficit, state officials are trying a little sleight-of-hand of their own. New York, for example, has gone to a system of two-year automobile registrations, allowing the state to count half of next year's fees as this year's income.

Governor Cuomo, who has conspicuously embraced the plan of the Democratic U.S. senator from New York, Daniel Moynihan, to stop diversion of the Social Security surplus, apparently has no such compunctions about looting schemes conducted within the confines of one's own state: His 1991 budget would transfer $230 million from the state workers' compensation fund to the general fund, and he proposes to save another easy $400 million by withholding scheduled contributions to the state's retirement system.

And just to prove that nothing is sacred—or too morbid—for him who is short of cash, New York has increased the cost of a death certificate from $5 to $15.

A bitter irony

The situation has a particularly ironic twist for the legacy of the civil rights movement. Over half of America's 10 largest cities have black or Hispanic mayors. These mayors, like their counterparts in the state houses, are left to preside over the further destruction of their jurisdictions. Having established symbolic precedents in a period of worsening material conditions, their achievements turn out to be largely pyrrhic.

Consider the case of New York's Dinkins. Dinkins's election as the city's first black mayor, coming after a period of highly-publicized racial incidents, was taken by many as a hopeful sign of minority progress and reconciliation. Now, he is announcing budget reductions that he confesses will "cut services to the marrow," insisting they are crucial to "preserve the city's fiscal integrity." As several have noted, Dinkins's approach to the financial emergency is essentially indistinguishable from that taken by Ed Koch, who especially antagonized the black and Hispanic population of New York by his brazen dismissal of the impact of his cuts on the poor.

Virginia's Douglas Wilder, the first elected black governor in American history, has also proposed an austerity budget to close his state's $181 million shortfall. Wilder is now touted as a "new breed" of fiscal-conservative Democrat.

Although elected officials tend simply to manage the crises they inherit, many are not altogether ignorant how the economics of disinvestment and speculation has caused their current, worsening plight. Tragically, few have said or done much about it, although—especially as a group—they are as well-situated as anyone to do so.