Federal Reserve Bank of Boston

Fiscal Facts

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Cash Assistance
for New England's Needy

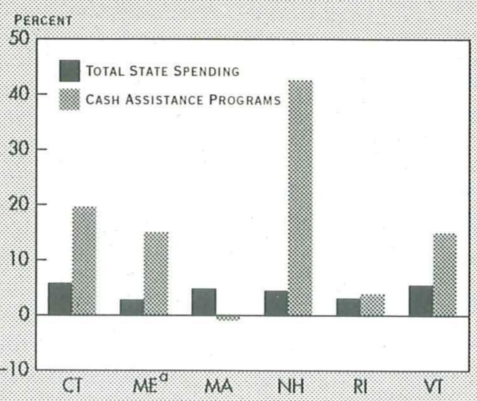
Fiscal stress has led all New England states to limit growth in cash assistance to the needy. Nevertheless, the rate of growth in these programs since FY91 has varied widely, from −1 percent in Massachusetts to +43 percent in New Hampshire (Chart 1). Why such variation? Has Massachusetts really become so much more restrictive and New Hampshire so much more generous?

The answer is a qualified "no." To be sure, the decline in Massachusetts' cash assistance reflects in part the conservative bent of its governor, William F. Weld. However, shifting political cultures explain only a small part of the variation displayed in Chart 1. More important factors include interstate differences in the mix of cash assistance programs, job losses, and the role of local government in providing assistance.

States provide most of their cash assistance through three programs: Aid to Families with Dependent Children (AFDC), Supplemental Social Security Income (SSI), and General Assistance (GA). AFDC benefits children (and their caretakers) who are needy because at least one of their parents is continuously absent, incapacitated, or unemployed. SSI benefits needy aged, disabled, and blind individuals. GA helps needy people who do not qualify for either AFDC or SSI.

Chart 1

Total State Spending and Cash Assistance:
Rate of Growth, FY91 to FY93



Note: Rate of growth based on FY91 spending and FY93 appropriations. See table 2 for method of estimating total state spending.
[a]Includes an estimate of a supplemental appropriation to be passed by Maine legislature in FY93.
Source: Official budget documents, state financial statements, and conversations with state budget and welfare officials.

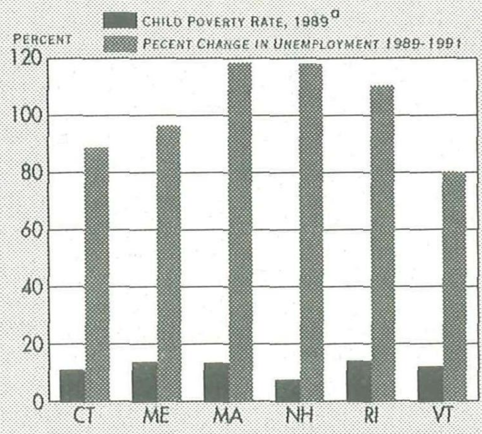
Of the three programs, GA is the easiest to cut for at least two reasons. First, the federal government plays no role either in setting minimum benefit levels and thresholds of eligibility or in financing GA, unlike AFDC and SSI. Second, many GA recipients are perceived to be more "employable" than those of the other two programs.

Not surprisingly, therefore, the two New England states that have experienced the slowest growth in their cash assistance budgets, Massachusetts and Rhode Island, also provided a relatively large proportion of their assistance through GA in FY91 (Table 1). Massachusetts has cut GA by 24 percent in each of the last two years, largely by tightening eligibility criteria. Rhode Island, in addition to tightening eligibility, has reduced the length of time that an individual can receive GA from 12 to six months per year.

By contrast, the two New England states that provide little or no state-funded GA, New Hampshire and Vermont, have increased total outlays for cash assistance since FY91 by 43 percent and 15 percent, respectively (Chart 1). They

Chart 2

Child Poverty Rate, 1989 and Percent Change in Unemployment, 1989-1991



[a] Percent of related children under 18 years of age who live in poverty.
Source: U.S. Bureau of the Census, *New England Economic Indicators*

have had difficulty slowing growth in this assistance because it requires trimming the more intractable AFDC and SSI. In addition, Vermont has been reluctant to abandon its tradition of generosity toward the needy, although it did cut average monthly AFDC allowances by 1 percent in both FY92 and FY93. New Hampshire's AFDC caseload has expanded faster than that of any other New England state, both because it lost more jobs (except for Massachusetts) and it had a relatively low incidence of child poverty in 1989, when the recession began (Chart 2). In addition, New Hampshire may have been lulled into a false sense of fiscal security by the large Medicaid windfalls it has reaped from the federal government (*Fiscal Facts*, Spring 1992).

Given that in FY91 Connecticut had the highest ratio of GA to total cash assistance in New England, one would expect the state to have been relatively successful in restraining total assistance growth. Instead, its total assistance has grown more rapidly than that of any other state in the region except New Hampshire (Chart 1). And this has occurred even though the state has cut GA benefit levels sharply.

The apparent anomaly can be explained by the explosive rate of growth in the state's GA caseload (54 percent since FY91), the result, in turn, of the state's weak economy and liberal eligibility criteria. Connecticut's reluctance to limit eligibility may be attributable both to its traditional generosity and to the manner in which its GA program is funded. The state pays for 85 percent of base benefit levels. Local governments pay for the remaining 15 percent plus any additional benefits they choose to provide. As a result, attempts to tighten eligibility, as well as to cut the state share of total costs, have become entangled in the politics of local aid. Maine, the only other New England state with a similar cost-sharing arrangement with its cities and towns, has experienced the second highest rate of growth in state GA spending since FY91.

The New England states' projections of cash assistance outlays for FY93 assume that a slow, steady improvement in the regional economy will cause growth in welfare caseloads to level off. How will states react if this economic prognosis proves to be overly optimistic? Will they appropriate supplemental funds, cut assistance further, or attempt comprehensive welfare reform, as several states in other regions have already done?

Fiscal Facts will monitor how states adapt. We now turn to our summaries of recent fiscal developments in each New England State.

Connecticut

Approved FY93 spending out of own-source revenues is about 4 percent higher than comparable spending in FY92 (Table 2). However, the total approved general spending for FY93 is about 10 percent below the amount required to keep existing programs operating at FY92 service levels.

Although Governor Lowell Weicker and the legislature agreed on the amount the state should spend, they differed sharply on how to spend it. Governor Weicker wanted deep cuts in local school aid, general assistance, Medicaid, and pensions for teachers and state employees. The legislature opted for smaller cuts in these programs and smaller increases in other budgetary functions. It also enacted a new tax on nursing homes. The tax, projected to generate $23 million in additional revenue, will trigger additional federal Medicaid grants (*Fiscal Facts*, Spring 1992).

Connecticut has recently expanded existing business tax incentives and created new ones. It has broadened existing property and sales tax exemptions for manufacturers and has enacted incremental tax credits for research and development and employee training. Offsetting these tax reductions are increases in fees and charges, expected to raise an additional $25 million in revenue in FY93.

Maine

Maine ended FY92 narrowly in the black, despite the enactment in March of a $26 million supplemental funding bill appropriating additional FY92 funds for Medicaid, AFDC, general assistance, mental health services, and corrections. The most daunting fiscal task of the last quarter of FY92 was the elimination of a projected deficit for FY93, estimated in April at $155 million. The legislature accomplished this mainly by cutting the compensation of state workers, requiring them to take furloughs without pay, and reducing their workweek.

In June, voters approved a $79 million bond issue primarily to finance infrastructure. Maine's projected ratio of debt service costs to total revenues will remain well within the state's self-imposed ceiling of 7 percent. (Bond-rating agencies generally recommend 9 percent.) The current ratio is 4 percent.

The legislature rejected Governor John McKernan's proposed package of investment and job tax credits.

Massachusetts

FY93 appropriations are about 4 percent above FY92 spending. Items enjoying disproportionately large increases are higher education and state aid for local schools, two items that suffered especially large cuts in FY91 and FY92. Governor Weld vetoed the increase in school aid because it was not tied to educational reform. The legislature overrode his veto.

The legislature enacted none of the tax cuts recommended by the governor, which included an array of business tax credits. However, the budget authorizes the phasing out of most of the state's current estate tax between FY94 and FY97, leaving only a so-called "sponge tax." (A sponge tax is an estate tax imposed by a state that can be used entirely to offset federal estate tax liability. As a result, it generates state revenue at the expense of the federal Treasury.)

Table 1

Cash Assistance Programs for the Needy:

State Spending and Growth Rates, FY91 through FY93

		Percent of Total State-Funded Cash Assistance to the Needy	Level ($ Millions)		
	PROGRAM	FY91	FY91[a]	FY92[a]	FY93[b]
CT	AFDC	44.0	174.9	189.1	199.1
	GA	28.7	114.1	167.0	173.6
	SSI	27.3	108.0	104.0	102.5
ME[c]	AFDC	53.7	36.2	44.3	43.6
	GA	22.1	14.9	17.4	17.4
	SSI	24.2	16.3	16.5	16.6
MA	AFDC	51.2	350.8	369.3	385.2
	GA	27.7	189.6	143.6	108.7
	SSI	21.1	144.6	161.7	185.0
NH	AFDC	73.6	20.8	26.8	31.4
	GA[d]	—	—	—	—
	SSI	26.4	7.4	8.0	8.8
RI	AFDC	52.8	47.0	53.2	54.9
	GA	32.9	29.3	32.1	22.9
	SSI	14.3	12.7	13.8	15.0
VT	AFDC	58.3	21.3	25.6	26.9
	GA	13.9	5.1	5.0	5.0
	SSI	27.8	10.2	10.8	10.3

[a]Spending.
[b]Appropriations for spending.
[c]Includes estimates of supplemental appropriations, yet to be passed.
[d]Program paid for entirely by cities and towns.
Source: Official budget documents, state financial statements, conversations with state budget and welfare officials.

The legislature's version of the budget included two measures intended to ease the restrictiveness of Proposition 2-1/2, the limitation on property taxes in the Commonwealth, but they were successfully vetoed by Governor Weld. One measure would have raised the maximum annual rate of growth in a community's property tax levy from 2.5 percent to the rate of inflation. Another would have permitted localities to exceed the limit in order to pay for tax abatements.

In July, the legislature enacted a $234 million spending bill to be financed out of the Commonwealth's FY92 surplus, reported by Governor Weld to be $290 million. The bill appropriated $100 million for highway repair and $75 million for a cost-of-living increase for state workers. Governor Weld was threatening to veto large portions of the bill as this newsletter went to press.

New Hampshire

In April, the legislature enacted a $55 million supplemental appropriation to bolster funding for AFDC, food stamps, nursing homes, and other selected social services through the remainder of FY92. A more controversial measure, enacted in June, authorized $10.4 million primarily for the purchase of transportation equipment and building repairs at the University of New Hampshire. The controversy concerned how to finance the purchases and repairs and whether the state can afford them. In the initial version of the bill, they were to be financed entirely through the issuance of bonds. Governor Judd Gregg objected, on the grounds that all capital spending bills should be considered at the same time within the framework of a comprehensive capital budget. The final version of the bill stipulated that some of the expenditures should be financed out of current funds if revenues came in higher than predicted. Governor Gregg maintained that this financing arrangement was fiscally irresponsible, given the imprecision of revenue projections and disagreement over how much the state had actually spent to date from all accounts, both "off-budget" and "on-budget."

Governor Gregg vetoed the bill, and the legislature overrode his veto. Governor Gregg has challenged the override in court, maintaining that a valid override requires approval of two-thirds of the entire legislature. Only two-thirds of those legislators present voted for the override.

Rhode Island

Rhode Island is the only New England state to include broad-based tax increases in its FY93 budget. Before the enactment of the budget, the state imposed an income tax equal to 27.5 percent of a taxpayer's federal income tax liability (not

27.5 percent of income). The budget raised the rate to 32 percent for taxpayers with federal income tax liabilities equal to or greater than $15,000, effective July 1. The rate increase is to remain in effect for 18 months, after which the across-the-board 27.5 percent rate is to be restored. The temporary rate hike gives Rhode Island an effective marginal state tax on high-income taxpayers of 9.9 percent of income, the highest in the region.

The new budget also extends the 7 percent retail sales tax to over-the-counter drugs and authorizes state-sponsored video gambling. The legislature rejected Governor Bruce Sundlun's recommendations for further broadening of the sales tax base and a new 1.5 percent tax on hospital receipts.

On the spending side, as in many other states, the most sensitive budget issues concerned the level and distribution of state aid to education and the level of human services spending. The legislature rejected the majority of cuts proposed by Governor Sundlun in these two areas and made his proposed aid distribution formula more favorable to wealthy communities. Nevertheless, total appropriated general spending for FY93 is extremely close to the governor's recommendation.

Table 2

Total State Spending[a]
for FY92 and Appropriations for FY93

	Millions of Dollars		Percent Change
	FY92	FY93	92-93
CT	6,360	6,600	3.8
ME	1,720	1,810	5.2
MA	11,340	11,800	4.1
NH	880	920	4.5
RI[b]	1,500	1,540	2.7
VT	780	770	-1.3

[a]Unless otherwise noted, includes spending out of general fund and transportation fund only. Excludes expenditure of federal grants and reimbursements.
[b]Includes spending out of all funds, less federal grants and reimbursements. Rhode Island does not have a separate transportation fund. Preliminary and unofficial estimates, supplied by Rhode Island Public Expenditure Council (RIPEC), have been adjusted by RIPEC for retroactive Medicaid reimbursement arrangements and changes in accounting rules.
Source: Official budget documents, state financial statements, and conversations with state budget officials.

Vermont

In January, Governor Howard Dean unveiled a strategy to eliminate the state's cumulative deficit by the end of 1993. So far, the strategy has not worked as planned. Personal income tax revenues for FY92 came in 15 percent lower than expected. A consultant to the state attributes much of the shortfall to a sharp decline in unearned income. Due to the large proportion of retirees in the state's population, unearned income accounts for almost one-fifth of Vermonters' personal income. The drop in unearned income (according to the consultant) may have been caused by the recent decline in interest rates.

The shortfall in income tax revenues increased the state's cumulative deficit to $65.5 million as of the end of FY92, $10 million above the governor's goal. The deficit would have been $16 million higher, had the state not transferred $11 million from special funds and cut spending by an additional $5 million this spring.

In light of these disappointing results, Governor Dean has presented a revised game plan that would eliminate all but $4 million of the cumulative deficit by the end of FY93. He wants the state to spend $20 million less of its FY93 own-source revenues than the $770 million appropriated in April (general fund and transportation fund combined). The $770 million already represents a 1 percent decrease in spending from FY92 (Table 2).

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