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Undermining the Texas Economy: The 2012-13 Texas State Budget

Introduction

The 2011 Legislature faced a revenue crisis caused by the collapse of state tax collections due to the Great Recession and a 2006 tax cut that left Texas with a biennial \$10 billion structural deficit. The Center for Public Policy Priorities urged a balanced approach to meeting our state’s needs that included using the Rainy Day Fund and adding new revenue. But the 2011 Legislature largely chose to underfund education and health and human services, damaging both our short-term economic recovery and our long-term economic prosperity.

Underfunding public services hurts our economy in the short run by increasing unemployment. The state budget directly eliminates 5,727 public jobs by 2013, while school districts will lose state aid that would have supported 49,000 jobs. Thousands of private-sector employees will lose their jobs too as the state reduces the purchase of goods and services from the private sector, and as unemployed public-sector workers curtail consumer spending.

In the long run, the budget cuts are bad for the economy because they reduce Texas’ investments in infrastructure such as transportation and services such as education. Texas’ relatively young population is increasingly challenging to educate with more children growing up in economically disadvantaged families. The state needs to invest in quality pre-kindergarten, strengthen public education, and improve access to higher education. And Texas needs to do this while strengthening social services. For example, with the highest rate among the states of residents without health insurance, Texas must improve access to health care.

Unfortunately, Texas has an antiquated tax system. Our state’s major tax, the sales tax, is primarily a tax on goods, but increasingly Texas businesses sell services. Consequently, even when our economy grows, Texas struggles to pay for schools, colleges, health care, roads, and prisons. When state tax collections are greatly reduced by an economic recession—as they were from 2009 to 2011—the state is unable to maintain even its already low levels of public investment.

In 2006, the state made the problem worse by pledging to pay for a local school property tax cut. While the state increased some taxes to help offset the cost, the 2006 changes ended up covering less than 30 percent. The uncovered cost is now almost \$10 billion per biennium.

In 2009, legislators wrote the 2010-2011 budget without spending the Rainy Day Fund or making massive cuts, but only because the federal government stepped in with Recovery Act funding in 2009. (By 2011, legislators had to tap the Rainy Day Fund and make cuts to balance FY 2011.) For 2012-13,



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the amount of federal aid was greatly reduced, to pre-Recovery Act levels. The refusal to appropriate the Rainy Day Fund for 2012 or 2013 meant over \$6 billion in current services general revenue underfunding of public education and almost \$5 billion in Medicaid underfunding.

This report analyzes our state's new budget, focusing on areas that are especially important to low- and moderate-income Texans. The report looks at both "General Revenue" spending (revenue that is primarily from state taxes) and "All Funds" spending (which also includes federal revenue, general revenue that is statutorily dedicated to a specific program, and "Other" legally earmarked revenue such as State Highway or Property Tax Relief funds).

Indicators of Need for Public Services in the Lone Star State

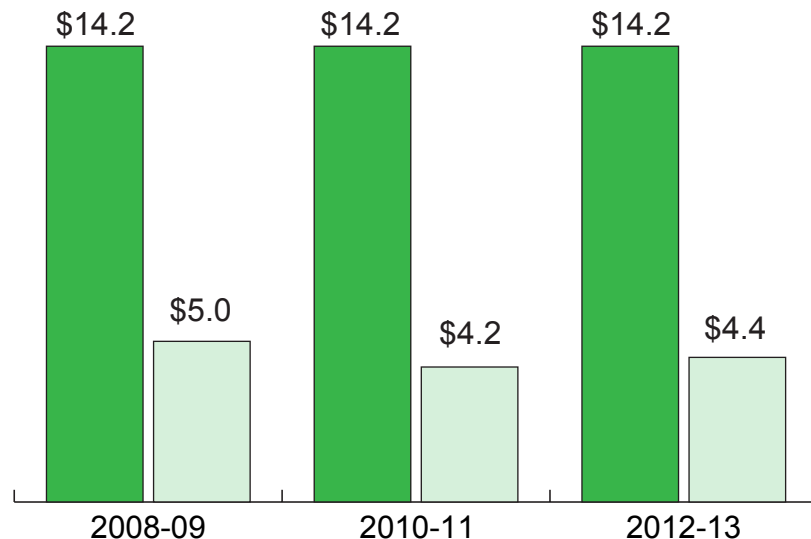
	Texas	U.S. Average	Texas rank
Under-65 population with no health insurance	26.2 %	17.7 %	1st
Share of population under age 18	27.3 %	24.0 %	2nd
Adults aged 25 or over without a high school diploma	19.3 %	14.4 %	1st
Child poverty rate	25.7 %	21.6 %	8th
Elderly poverty rate	10.7 %	9.0 %	8th

SOURCE U.S. Census Bureau, 2010 American Community Survey; Statistics are for 2010; rankings do not include Washington, D.C.

2006 Property Tax Cut Created a \$10 Billion Structural Deficit

In billion \$,
biennial

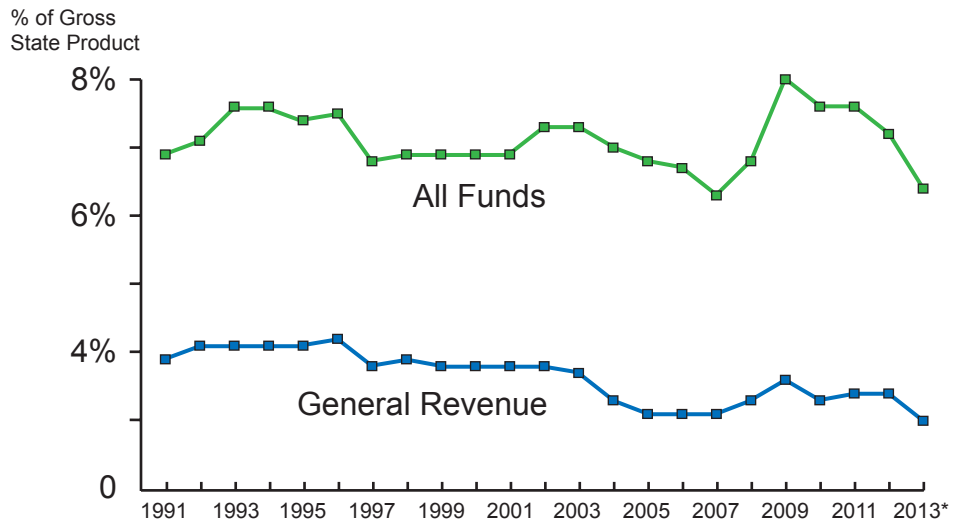
■ Cost of 2006 property tax cut
■ Revenue from 2006 tax changes



SOURCES Legislative Budget Board; Texas Comptroller of Public Accounts

The 2012-13 Texas State Budget

State Spending Decreases as a Share of the Economy



*2013 is adjusted to include deferred Foundation School Program payment and Medicaid IOU.

All-Funds Budget

2010-2011 All Funds spent: \$187.5 billion

2012-2013 All Funds appropriated: \$173.5 billion

7.5% below 2010-11; 17% below current services

Why the State Budget Should Have Grown:

Texas is a rapidly growing state, primarily because of its high birth rate. Its population increases annually by almost 2 percent—about 1 million additional residents every two years, with 168,000 more students enrolled in public elementary and secondary schools. Add inflation (also 2 percent annually), and the necessary increase just to maintain current services is 8 percent every two years, the time period covered by the Texas state budget.

How was spending cut? H.B. 1, the General Appropriations Act; H.B. 4, the supplemental appropriations bill; and S.B. 2 from the first called session make All-Funds appropriations for 2012-13 that are 7.5 percent below 2010-11 spending. After adjusting for a \$2.3 billion deferred school payment and supplemental Medicaid funding (discussed on page 9) that will be needed in 2013, the 2012-13 budget rises to \$187 billion. This is still 10 percent below current services levels for 2012-13 that would have taken into account student and client growth, health care cost increases, and other inflationary pressures.

All Funds spending will also be lower compared to expected growth in the state economy, as measured by Gross State Product. In 2011, state spending is 7.6 percent of GSP. Even after factoring in the school deferral and the Medicaid “IOU” that the 2011 legislature created, state spending will only be 6.4 percent of the economy by 2013.

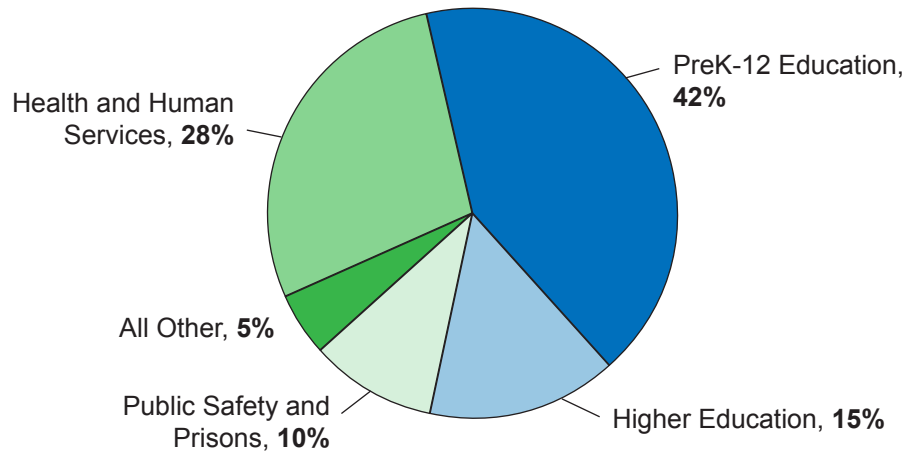
General Revenue spending, including the school deferral and Medicaid “IOU”, will be 3.0 percent of the Texas economy by 2013, more than 1 percentage point lower than the 1992-1995 level of 4.1 percent.

The necessary

increase just to maintain current services is 8 percent every two years.

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Texas General Revenue Budget, 2012-13



General Revenue Budget

2010-2011 General Revenue spent: \$90.2 billion*

2012-2013 General Revenue appropriated: \$81.3 billion

9.9% below 2010-11, 18% below current services

Why was the General Revenue part of the budget cut?

Lack of state revenue: The state constitution's "pay as you go" provision requires the General Revenue (GR) part of the budget to be "certified" by the Comptroller. This means that appropriations requiring General Revenue cannot exceed the amount of GR that the state will have through the end of that budget cycle. The Comptroller estimated in January 2011 that a \$4.3 billion GR revenue shortfall for 2011, subtracted from projected net GR collections of \$76.4 billion, gave legislators only \$72.2 billion GR to appropriate for 2012-13.

Current services needs: State agency budget proposals prepared in Fall 2010 requested almost \$107 billion in General Revenue for the 2012-13 biennium. Of this, a minimum of \$99 billion in General Revenue was needed to continue funding education, health care, and other basic services as required by state law, including \$8.2 billion needed to replace federal Recovery and Reinvestment Act dollars used instead of General Revenue in the 2010-11 budget. With \$99 billion in General Revenue needs, but \$72 billion in General Revenue collections available, legislators faced a \$27 billion gap as the 2011 regular session began.

How the \$27 billion budget gap was closed: In addition to General Revenue, the Comptroller had informed legislators that \$9.4 billion in the Economic Stabilization Fund ("Rainy Day Fund") was available for spending. Legislators used \$3.2 billion of the Rainy Day Fund to help close the 2011 shortfall (H.B. 275, Regular Session) but did not appropriate any Rainy Day Fund dollars for 2012 or 2013.

Along with tapping the Rainy Day Fund, legislators were able to increase the amount of GR they could budget for 2012-13 primarily because the Comptroller added \$1.5 billion to the GR forecast by May 2011, and because S.B. 1 in the

* Includes \$8.3 billion in American Recovery and Reinvestment Act funds used as state General Revenue, as estimated by the Legislative Budget Board in June 2011.

The 2012-13 Texas State Budget

Eliminating the 2011-13 General Revenue Shortfall	In billion \$
Starting point: Gap between \$72 billion in available General Revenue and \$99 billion in current services needs for 2012-13	\$27
Spending	
\$1.3 billion in interim cuts to 2011 budget, offset by \$500 million in FY 2011 new spending from Foundation School Fund	-0.8
Current services reduction for public education, incl. Teacher Retirement System (after federal EduJobs offset)	-5.6
Foundation School Payment postponed to fiscal 2014	-2.3
Current services cuts to higher education	-1.6
Cuts to Medicaid through rate, benefit, and managed care changes	-2.0
Underfunding of Medicaid in Fiscal 2013 (“IOU”)	-4.8
Other current services cuts to public safety and prisons (\$0.9 billion); general government (\$0.6 billion); non-Medicaid health and human services (\$0.45 billion); and all other state services (\$0.5 billion)	-2.5
Increase in General-Revenue-dedicated balances used for certification (from \$3.7 billion in 2009 session to \$4.9 billion in 2011 session)	-1.2
Revenue	
Rainy Day Fund used to help close 2011 shortfall	-3.2
Improved revenue estimates for 2011 and 2012-13	-1.5
“Borrowing” from 2014 tax revenue and from State Highway Fund	-0.7
Other net new revenue from SB 1/other revenue-raising bills	-0.5
Permanent School Fund changes	-0.3

special session increased GR by about \$880 million (mostly through one-time tax speed-ups or delayed transfers). S.B. 1 also postpones a payment to schools until 2014, a savings to the 2012-13 budget of \$2.3 billion, and cuts state aid for the Foundation School Program by \$4 billion for the biennium.

Legislators also expanded the practice of leaving certain earmarked revenues unappropriated so the fund balances could help count towards certification. This meant that programs that were supposed to receive that funding, such as the low-income utility discount program supported by the System Benefit Fund, saw their budgets cut. According to the Comptroller, the total amount of dedicated GR that was unappropriated and therefore helped certify the budget will reach \$4.9 billion by the end of 2013, up from \$3.7 billion after the 2009 session and \$3.1 billion in 2007.

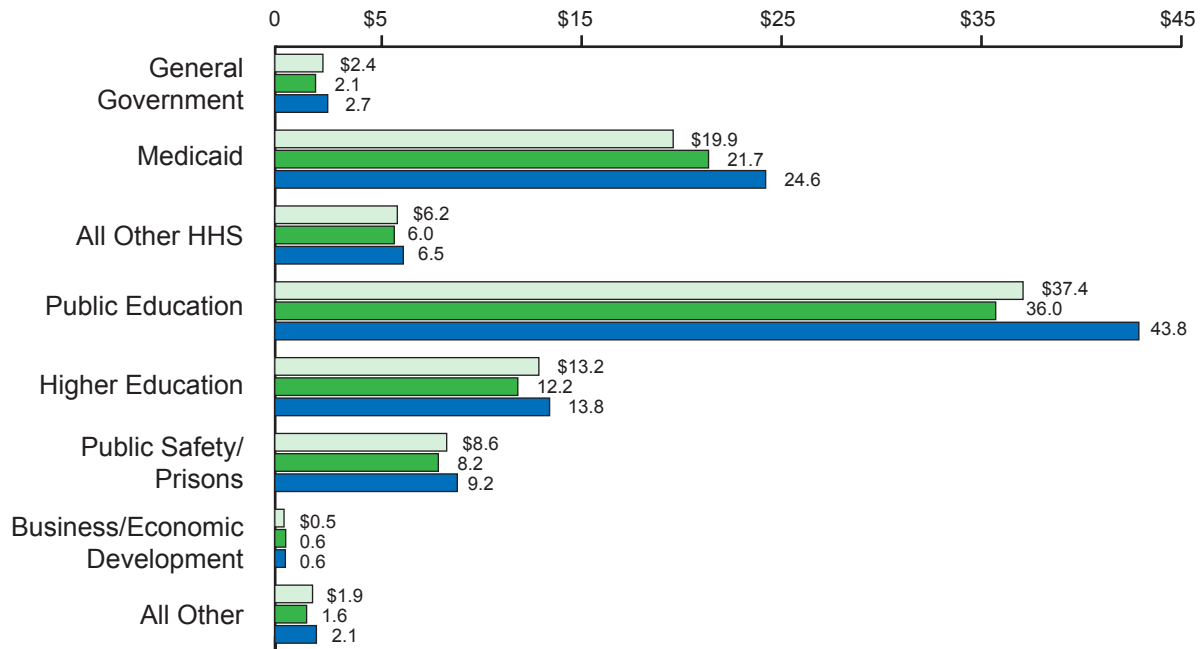
The next legislature will face the challenge of funding a 2013 supplemental bill for Medicaid and finding additional revenue for “current services” growth in 2014-15.

The General Revenue budget in 2012-13 is mostly unchanged from historical spending: 57 percent is for education; 28 percent is for health and human services; 10 percent is for public safety and criminal justice; and 5 percent is for all other areas combined—general government, judiciary, natural resources, business and economic development, regulatory agencies, the legislature, and general provisions.

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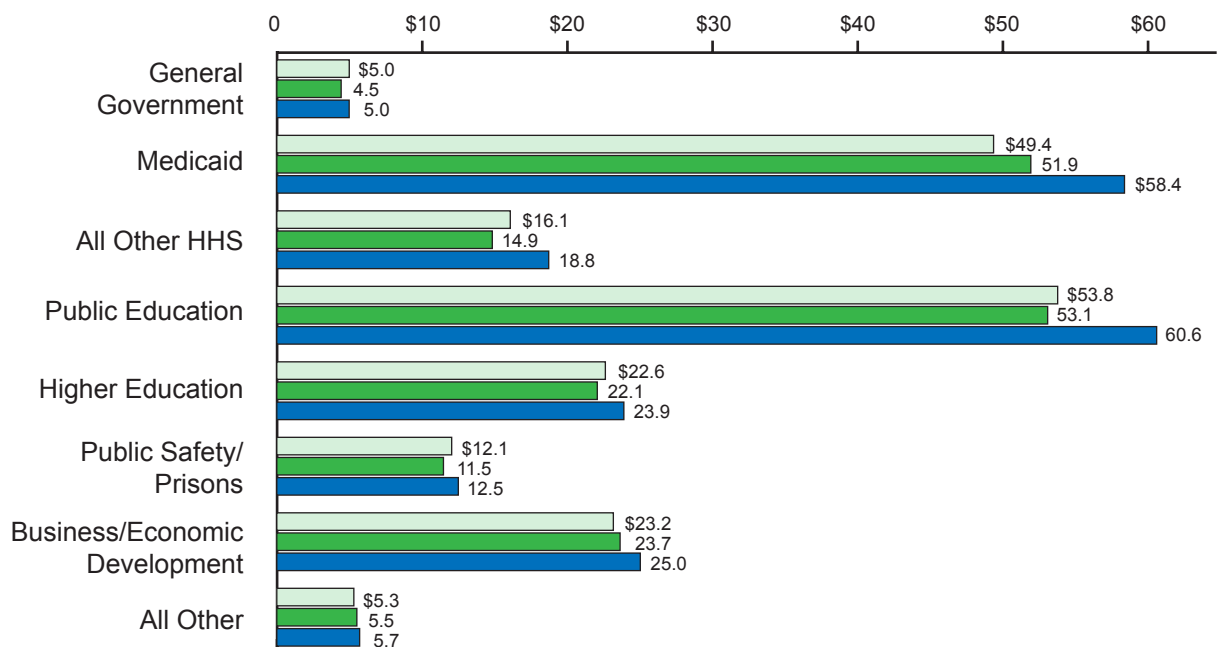
General Revenue Budget (Billions)

■ 2010-11 Budget
 ■ 2012-13 Budget (with FSP delay, Medicaid IOU)
 ■ 2012-13 Current Services



All Funds Budget (Billions)

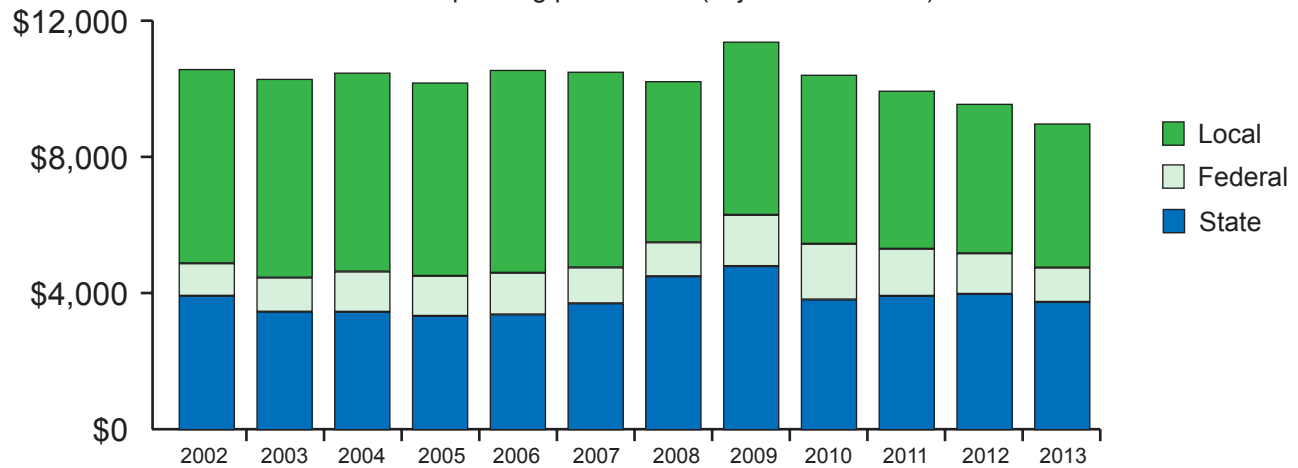
■ 2010-11 Budget
 ■ 2012-13 Budget (with FSP delay, Medicaid IOU)
 ■ 2012-13 Current Services



The 2012-13 Texas State Budget

Per-Pupil Spending Will Fall by Almost \$1,000 Unless Local Property Taxes Increase

Spending per Student (adjusted to 2011 \$)



Texas is

spending less on education both in total and per student.

PreK-12 Education

2010-2011 General Revenue spent: \$37.4 billion*

2012-2013 General Revenue budgeted: \$36.0 billion**

3.7% below 2010-11; 15% below current services

How General Revenue Cuts Were Made:

The legislature cut public education funding in two main ways: 1) a \$4 billion cut was made to the state funding that schools would have received under current law for the Foundation School Program (FSP, or state formula aid for local school districts); 2) a \$1.3 billion cut was made to programs outside the FSP, such as preK grants, the Student Success Initiative, teacher incentive pay, and other grants. In the first year of the budget, \$831 million in federal EduJobs funding helps offset a \$2 billion cut in state aid. In the second year, no additional federal help is assumed, making the impact of the lost state aid more pronounced. The state budget projects that public school enrollment will increase by about 168,000 students in 2012-13, but does not provide the \$2.2 billion in state aid needed to pay for this growth. School funding cuts would have been worse if not for the Legislature's decision to postpone an August 2013 \$2.3 billion payment to districts to fiscal 2014 (S.B. 1, First Called Session).

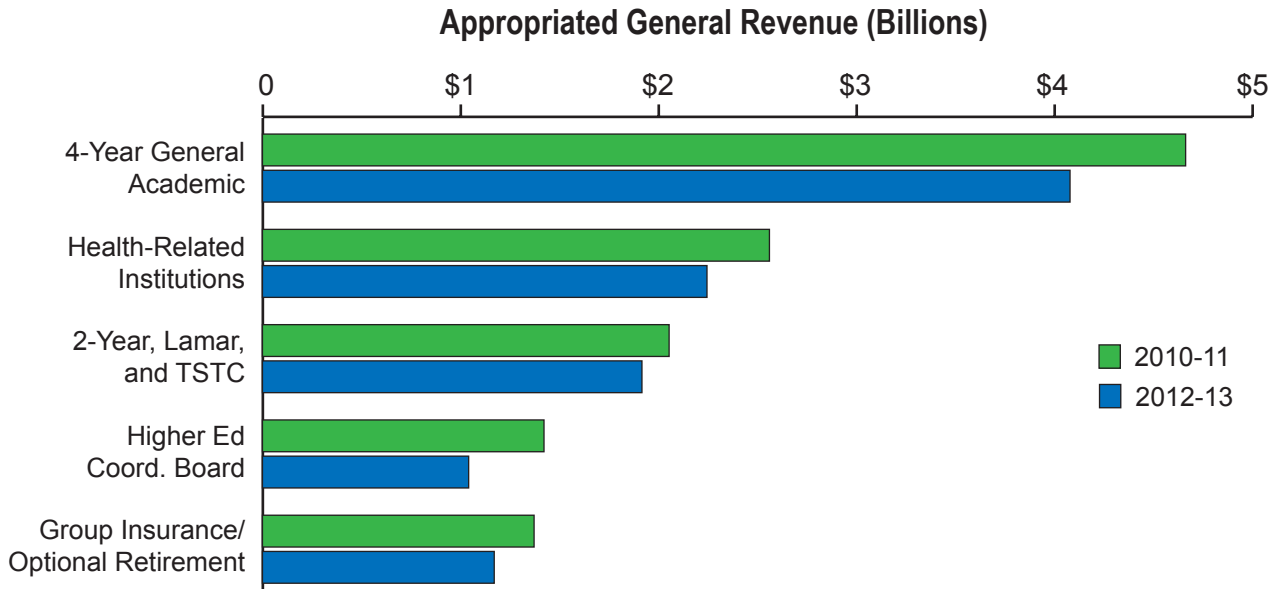
Programs outside the Foundation School Program that no longer get an appropriation include: Pre-K Early Start Grants; High School Completion/Success; Science Lab Funding; Reading, Math, and Science Initiatives; Early High School Graduation; Extended Year Programs; Teen Parenting; Middle School Physical Education and Fitness; Limited English Proficiency Student Success Initiative; Disciplinary Alternative Education (Safe Schools); Rural School Technology; School-Based Prevention Services; School Improvement/Parental Involvement/AVANCE; Arts Education; Science and Math Outreach; and One Community, One Child.

After adjusting for inflation, Texas per-student spending will fall to its lowest point in over a decade. The 2012-13 budget assumes that local property taxes will not rise to offset the decrease in state aid.

* Includes \$3.6 billion in American Recovery and Reinvestment Act funds used as state General Revenue, as estimated by the Legislative Budget Board in June 2011.

** Includes \$2.3 billion deferred school payment.

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Higher Education

2010-2011 General Revenue spent: \$13.2 billion*

2012-2013 General Revenue appropriated: \$12.2 billion

8.0% below 2010-11, 12% below current services

General Revenue Cuts:

H.B. 1 and H.B. 4 reduce General Revenue support for all major areas of higher education spending. The fiscal 2011 interim cuts (5 percent and 2.5 percent) made \$500 million in GR budget cuts to higher education, while \$1 billion in GR cuts are implemented in 2012-13, not counting unfunded enrollment growth. Some areas will see a much larger cut than the 8 percent overall biennial decrease. For example, the Higher Education Coordinating Board (HECB)—primarily financial aid—got 27 percent less GR, and the Optional Retirement Program received an 18 percent GR cut. Community college employee benefits were slashed, with 39 percent less state aid for health insurance and 48 percent less for retirement benefits in the 2012-13 budget.

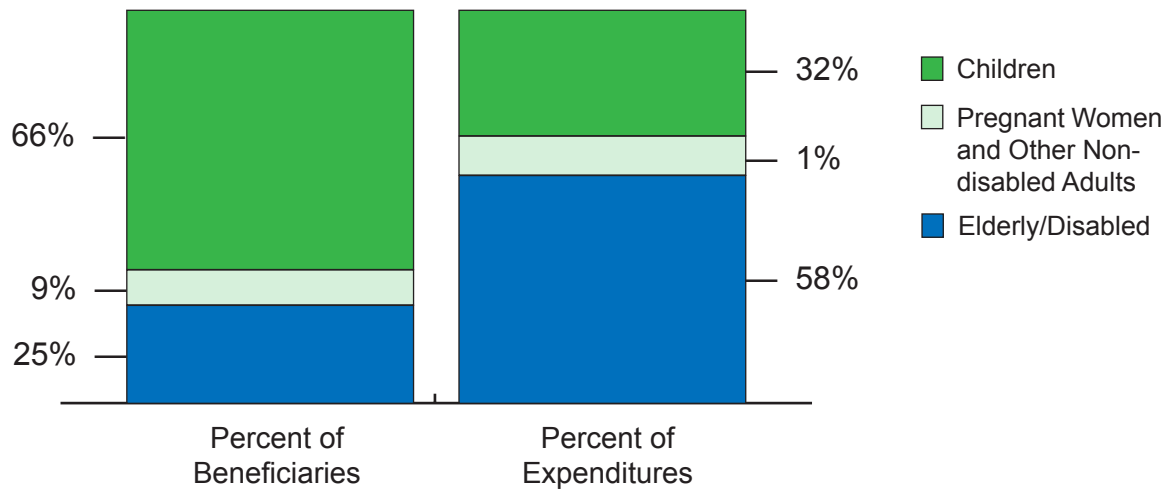
Financial aid: The main financial aid strategy in the HECB budget was reduced by 15 percent, from \$1 billion to \$879 million. The TEXAS Grant program took a 10 percent cut but will still assist all renewal recipients plus 33,000 new students—combined, about 30 percent of all eligible students. If the maximum TEXAS Grant award is reduced, as HECB is recommending, another 34,700 new students could be helped. The Tuition Equalization Grant for students attending private universities was cut by 20 percent; the B-On-Time zero-interest loan program will receive 29 percent less funding; and Top 10% Scholarships will receive 23 percent less funding. Texas Educational Opportunity Grants and Work Study assistance were not cut below their 2010-11 budget levels. The Texas Armed Services Scholarship, with an additional \$5.4 million from S.B. 2 in the special session, had its funding quadrupled.

* Includes \$227 million in American Recovery and Reinvestment Act funds used as state General Revenue, as estimated by the Legislative Budget Board in June 2011.

The 2012-13 Texas State Budget

: **Zeroed out:** Along with enrollment growth, the following HECB programs were
 : not funded at all: College Readiness Grants, the Performance Incentive Fund,
 : Early H.S. Graduation and TANF Scholarships, Engineering Recruitment,
 : Alternative Teaching Certification, Combat Tuition Reimbursement, Texas
 : Career Opportunity Grants, Doctoral Incentives, the Preceptorship Program, the
 : Primary Care Residency Program, Graduate Medical Education, Professional
 : and Vocational Nursing Aid, Dental Education Loan Repayment, Hospital-based
 : Nursing Education, and the Children’s Medicaid Loan Repayment Program.

Texas Medicaid Beneficiaries and Expenditures, 2010



Medicaid

2010-2011 General Revenue spent: \$19.9 billion

2012-2013 General Revenue budgeted: \$21.7 billion (with IOU)

9% increase from 2010-11; 11% below current services

General Revenue Reductions:

Medicaid is a critical state-federal program that funds health care for low-income children, pregnant women, elders, and people with a disability. Before the 2011 session began, the Health and Human Services Commission (HHSC) estimated that a \$9 billion All Funds increase (\$4.6 billion in additional GR) was needed for Medicaid current services caseload and cost growth in 2012-13. The All-Funds amount for Medicaid in H.B. 1 falls about \$17.8 billion short of this amount—31 percent below current services levels.

Supplemental appropriations for an estimated (in June 2011) \$4.8 billion GR “IOU” would restore about \$11.4 billion in All Funds for Medicaid health care services, but this will still be about 11 percent less than what Medicaid would have needed before cuts made by the legislature.

Actual reductions to Medicaid and CHIP for 2010-11 include \$805 million in General Revenue cuts to fees paid to health care providers; \$843 million GR in

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benefit and spending cuts; and \$386 million in GR savings that is expected to result from the expansion of managed care.

Caseloads Budgeted in H.B. 1: In 2011, more than 3.5 million Texans received Medicaid acute care services on a monthly average basis; more than 2.5 million were children. By 2013, Medicaid acute care programs are budgeted to reach 3.7 million Texans, almost 5 percent more than in 2011.

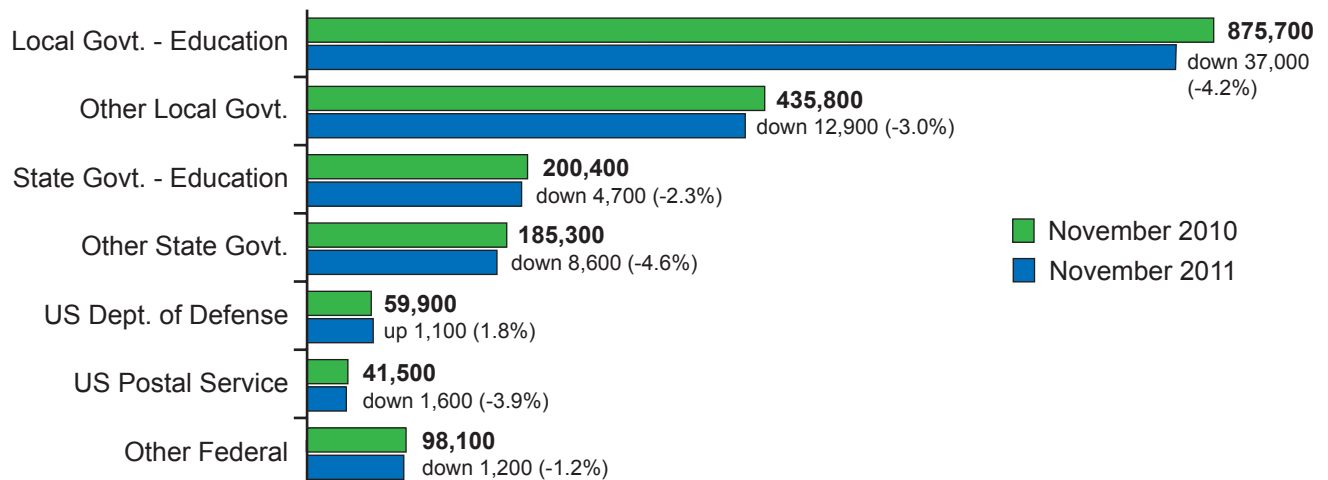
Children account for over two-thirds of Medicaid enrollees, but well over half of Medicaid spending is on Texans who are elderly or who have a disability. Hospital and long-term care services such as nursing homes are a big share of Texas Medicaid spending.

Jobs

About 1.8 million Texans worked in the public sector in November 2011, with 838,700, or 46 percent, employed in local government education jobs (school districts and community colleges). Combined, federal, state, and local public agencies employ more Texans than any private-sector industry, surpassing the 1.5 million working in educational services and health care or social assistance, and the 1.4 million working in professional or business services. The public sector, particularly local schools, has long been a major source of job growth in Texas, as the state's relatively young and fast-growing population adds more than 80,000 students annually to school enrollment. Between the first quarter of 2007 and 2011, the public sector created nearly 60 percent of Texas' net new jobs, growing by 7.1 percent compared to 1 percent for private-sector jobs. The federal American Recovery and Reinvestment Act helped preserve or create jobs, with as many as 46,000 Texas public sector jobs saved by ARRA dollars—almost 38,000 of them in local schools.* But with ARRA support ending and state budget cuts taking effect, Texas is now experiencing the same loss of public jobs that other states' economies have sustained, with the same harmful effects on private-sector employment.

* Legislative Budget Board, American Recovery and Reinvestment Act 2011 1st Quarter Reporting and Analysis (December 31, 2010), page 22.

Most Government Employees Are Teachers



Source Current Employment Statistics for Texas (Actual Series), December 2011, Labor Market & Career Information, Texas Workforce Commission.

The 2011-12 academic year is the first in over two decades to see an annual drop in Texas local government education employees (37,000 fewer jobs in November 2011). School districts and community colleges are expected to make additional cuts for 2012-13. The \$4 billion in state aid cuts to the Foundation School Program could ultimately cause a loss of 49,000 school jobs, if school districts are unable to raise property taxes and do not receive any additional federal aid. This in turn could cost the Texas economy another 68,000 private-sector jobs by 2013, because of the economic multiplier effect of local elementary and secondary education.

State government education jobs dropped by 4,700 between November 2010 and 2011. Fewer than half of these jobs are funded by the state budget; instead they rely on federal funds and other revenue that universities raise locally. State government jobs that are not in education also decreased, by 8,100 in the last year. This is significantly higher than the 8,600 jobs eliminated by the 2012-13 state budget because agencies were already reducing payrolls in response to the 2011 interim cuts.

Conclusion

The economy will recover, but the state will still be left with a biennial \$10 billion structural deficit created by the 2006 tax cut. To protect our long-term economic prosperity, the state must close this hole or be faced with continued underfunding of our schools, colleges, universities, and social services.

The path forward most likely will require several different steps. Scrubbing the tax code for wasteful tax loopholes is an important first step. To keep up with changes in the economy, the state must expand its sales tax base to include services, with a plan to offset the regressive effect on low-income families. The state's business tax, which has underperformed, needs to be revised. And the state needs to look closely at various healthy Texas taxes such as increasing tobacco and alcohol taxes or creating a sugar-loaded soft drink tax.

No one is talking about Texas becoming a high-tax state, but our state's revenue system isn't producing the minimum needed to ensure our continued prosperity. The state must develop a plan to close the structural deficit created in 2006. The state must raise the revenue needed to maintain our educational system, the proven path to good jobs at good wages, and our social services system, the safety net for our most vulnerable citizens.

More detailed CPPP State Budget Analyses:

The 2012-13 Budget for Child Protective Services: The Good, the Bad, and the Ugly, by Jane Burstain, June 9, 2011, www.cppp.org/research.php?aid=1120.

Major Medicaid-CHIP 2012-13 State Budget Decisions, by Anne Dunkelberg, July 25, 2011, cppp.org/research.php?aid=1127.

Sources

Texas Legislative Budget Board, *Comparison Tables: 2012-13 Biennial Appropriations Compared To 2010-11 Base Spending By Method Of Finance* (November 2011); Fiscal Size-Up for 2010-11 Biennium, Conference Committee Report on HB 1, Conference Committee Report on SB 2 First Called Session, and *Summary of Conference Committee Report on HB 1* (www.lbb.state.tx.us); the Texas Budget Source, tbs.lbb.state.tx.us/; state agency budget requests for 2012-13 (www.lbb.state.tx.us/External_Links/LAR_82R/Agency_LAR_Listing_82R.htm).

Texas Health and Human Services Commission, Health and Human Services System Consolidated Budget Request for 2012-13, Fall 2010, www.hhsc.state.tx.us/about_hhsc/Consolidated-BudgetFY12-13.pdf; FY 2012-13 Budget Update, June 23, 2011, www.hhsc.state.tx.us/about_hhsc/council/062311_Presentation.pdf; Operating Budget for Fiscal Year 2012, www.hhsc.state.tx.us/about_hhsc/2012-Operating-Budget.pdf.

Texas House Research Organization, *Texas Budget Highlights 2012-13*, December 6, 2011, www.hro.house.state.tx.us/pdf/focus/highlights82.pdf.

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