Review

MTC
Multistate Tax Commission

Table of Contents

Working Together Since 1967 to Preserve Federalism and Tax Fairness

Multistate Tax Commission Review

A Journal on State Taxation of Multijurisdictional Commerce

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From the Executive Director

This issue of the ***Review*** is being prepared during an event-filled time for the Commission. The Executive Committee meets in person on May 12th. Former Oregon Commissioner, Commission Chair, and Wade Anderson Medal recipient Elizabeth Harchenko will be assisting the Executive Committee as they begin exploring, improving, and setting the Commission's organizational priorities and processes for the next five to ten years. In addition, two public hearings on Uniformity Proposals are scheduled the following week. The first hearing, scheduled for May 16th is for the "Proposed Statute Regarding Partnership or Pass-Through Entity Income That is Ultimately Realized by and Entity That is not subject to Income Tax." The second hearing, scheduled for May 18th is for "Sales and Use Tax Notice and Reporting Statute." On top of this, we are preparing for the Annual Meeting, July 24th through the 28th, at the Grouse Mountain Lodge in Whitefish, Montana. In addition to the regular Commission work, we are paying close attention to the progress of H.R. 1439, The Business Activity Tax Simplification Act of 2011 as it works its way through Congress.

This issue contains three articles and my letter of January 31st to Secretary of Treasury Timothy Geithner asking him to consider the impact on state tax systems during the debate on reforming federal income taxes. The first article, "Back to the BAT Cave," by our Director of Policy Research, Dr. Elliott Dubin, updates the article he and former Policy Research Intern Cameron Snow wrote three years ago on a previous proposed Business Activities Tax Simplification Act. The purposes of these articles are to provide some measure of state business activity taxes relative to the aggregate size of the private business sector, to provide a measure of the importance of business taxes to state and local governments, and to cast doubt on the assertion that Congressional efforts to impose physical presence nexus standards for state business activity taxes will result in any significant increase in business investment.

The last two articles assess the current fiscal condition of state and local governments. The first article is by Tracy Gordon, Assistant Professor, University of Maryland, College Park and Okun-Model Fellow in Economic Studies, Brookings Institution. This article was reprinted with permission from Tax Analysts. Professor Gordon finds that while state and local governments will face continuing stress for some time come, there is little danger of states defaulting on their debt obligations. The third article is another by Dr. Dubin, wherein using other data, he supports Professor Gordon's conclusions.

We welcome your comments on these articles, suggestions for topics, and submissions for future issues of the ***Review***. We also welcome you to join us in Montana July 24th through the 28th for our annual conference and committee meetings.

Joe Huddleston, *Executive Director*
Multistate Tax Commission

Corporate Tax Reform in a Time of Fiscal Crisis

Joe Huddleston
Executive Director
Multistate Tax Commission

Those who follow tax policy debates closely know that reform of the U.S. corporate income tax is a perennially favorite topic. At the beginning of this year, The House Ways and Means held hearings on this subject and President Obama also weighed in on this topic. In a recent speech to the U.S. Chamber of Commerce, the President said:

> "That's why I want to lower the corporate rate and eliminate these loopholes to pay for it, so that it doesn't add a dime to our deficit. And I am asking for your help in this fight."[1]

Over the years, numerous commentators have proposed a myriad number of possible ways in which they believe the corporate income tax should be reformed. However, in almost every discussion of federal corporate income tax reform, the impact on state corporate income taxes is given scant attention. Below is a reprint of my letter to Treasury Secretary Geithner requesting that state concerns regarding be given his attention.

"That's why I want to lower the corporate rate and eliminate these loopholes to pay for it, so that it doesn't add a dime to our deficit. And I am asking for your help in this fight."

[1]http://www.huffingtonpost.com/2011/02/07/obama-chamber-of-commerce-speech_n_819571.html

The Honorable Timothy Geithner
United States Secretary of the Treasury

Dear Mr. Secretary:

The Multistate Tax Commission is an organization of state governments that works with taxpayers to administer, equitably and efficiently, tax laws that apply to multistate and multinational enterprises. Created by the Multistate Tax Compact, the Commission is charged by this law with:

- Facilitating the proper determination of State and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes;
- Promoting uniformity or compatibility in significant components of tax systems;
- Facilitating taxpayer convenience and compliance in the filing of tax returns and other phases of tax administration;
- Avoiding duplicative taxation.

Created in 1967, forty-six states participate in the work of the Multistate Tax Commission. I am here today representing the Commission and its members asking you to keep in mind that changes in federal tax laws have significant impacts on state and local tax systems.

The United States, and many other nations are now undertaking the arduous task of fundamentally reforming their tax and revenue systems. It has been our experience that far too often, significant changes in federal tax law have been made with little or no input from representatives of state and/or local governments. It is in this regard that I am writing to you today.

The lack of input from the state and local government sector in the legislative process can have a negative impact on the private sector in terms of additional compliance costs; and, can mitigate the impact of changes to the Internal Revenue Code.

The most recent example of the potential adverse impact of federal tax law changes on state tax bases is the recent law change that would allow businesses to immediately deduct the entire costs of capital investments in machinery and equipment. While this may be good policy in that businesses would have greater incentive to invest in machinery and equipment, it can have a large, adverse effect on state governments. It has been estimated that this change in federal tax law could result in a revenue loss exceeding $11.0 billion in the coming fiscal year.[2] Because states, for the most part, use the federal definition of taxable income as the basis for their income taxes, increasing the amount of investment that can be immediately expensed rather than depreciated, reduces the income tax base for both individual and corporate income taxes for the majority of states. Given the large budget gaps facing states this next fiscal year, a number of states may be

[2]Nicholas Johnson and Ashali Singham, "Business Expensing Proposal Would Add to State Fiscal Problems," Center for Budget and Policy Priorities, December 16, 2010.

forced to decouple their tax bases from the Internal Revenue Code; and/or raise their marginal tax rates. Neither of these changes would help the nascent and fragile economic recovery.

Other instances in which a significant number of states have "decoupled" from the Internal Revenue Code include:

- The "bonus depreciation" tax law enacted March 9, 2002.
- The Qualified Production Activities Income (QPAI) tax law change, enacted in 2004 as Section 199 of the Internal Revenue Code.
- The repeal of the credit for state estate and inheritance taxes, which was part of the 2001 tax legislation, prompted 21 states to decouple from the federal tax code and continue to collect either an estate or inheritance tax.

The above examples illustrate the point that implementing federal tax legislation without consideration of state revenue needs may lead to increased compliance costs for taxpayers as states decouple their tax codes from the Internal Revenue Code in a non-uniform manner. Such actions increase compliance costs for taxpayers and blunt the impact of Federal tax law changes

If you would like to discuss this further, please feel free to get in touch with me.

Sincerely,

Joe Huddleston
Executive Director
Multistate Tax Commission

Back to the BAT Cave

Elliott Dubin, Director of Policy Research, Multistate Tax Commission

I. Introduction

Former MTC Policy Research Intern Cameron Snow and MTC Director of Policy Research Elliott Dubin wrote an article "Musings from the BAT Cave" which appeared in the summer 2008 issue of the ***Multistate Tax Commission Review***.[1] In light of the introduction of H.R. 1439, *Business Activity Tax Simplification Act of 2011*, the previous article is updated.

The great American philosopher, inventor, publisher, and public servant, Benjamin Franklin noted:

> **"In this world nothing is certain but death and taxes.**[2]

Furthermore, in his canons of taxation, Adam Smith stated:

> **"The tax which each individual is bound to pay ought to be certain, and not arbitrary."**[3]

Thus, good tax policy requires that taxpayers should be aware that their actions can result in tax liability; and, if they incur a tax liability, the amount of tax owed should be known with a reasonable degree of certainty.

Given the complexity of state nexus laws regarding Business Activities Taxes (BATS), the canon that taxes should be certain are frequently violated. Companies that wish to expand their operations across State lines are often uncertain as to how these BATS will be applied to them. Furthermore, this uncertainty, it is claimed, and not the taxes themselves is what is inhibiting new business investment and threatening to cripple the economy. In the opinion of the Coalition to Protect Interstate Commerce, overly aggressive state attempts to expand taxing authority have:

- led to unfairness and uncertainty;
- increased compliance costs (inevitably, such increased costs will be passed on to consumers in the form of higher prices);
- hindered business expansion;
- put companies at the risk of duplicative over-taxation;
- threatened the continued development of electronic commerce;
- threatened the revenue collections of states that fully comply with constitutional nexus requirements;
- stymied the intent of accounting reporting rules for publicly traded companies; and
- negatively affected international competitiveness.

Left unchecked, this unwarranted expansion of the states' power to impose business activity taxes on companies that do business across state lines will have a chilling effect on the entire economy as tax burdens, compliance costs, litigation and uncertainty escalate. [4]

In order to address these concerns, various corporate groups and Members of Congress have cosponsored H.R. 1439, the Business Activity Simplification Act of 2011 (BATSA). This bill was introduced by Bob Goodlatte (R-VA), Bobby Scott (D-VA), Jeff Duncan (R-SC), and Sheila Jackson-Lee (D-TX). According to Congressman Goodlatte:

> "This legislation will ensure that businesses are not subject to double taxation at the state level, which will ultimately facilitate the continued growth of e-commerce, job creation and the overall strength of the American economy."[5]

Unfortunately, the proponents of federal legislation to change state nexus standards for imposing state business activity taxes do not provide evidence that admittedly complex and sometimes confusing state BATS nexus laws have actually contributed to the perpetration of the perverse actions listed previously. Nor have they provided sufficient evidence to show that passage of H.R. 1439 will have a utopian effect on businesses — all business will be well managed, profitable, and able to grow unhindered by state taxes.

Furthermore, the proponents of H.R. 1439 provide no measures of the relative importance of BATS to either state government fiscs or to the business sector. Nor do they provide any empirical evidence on how the uncertainty of state business activity tax liability affects investment. As Thomas Lord Kelvin reminds us:

> "…when you can measure what you are speaking about, and express it in numbers, you know something about it; but when you cannot measure it, when you cannot express it in numbers, your knowledge is of a meagre and unsatisfactory kind; it may be the beginning of knowledge, but you have scarcely in your thoughts advanced to the state of Science, whatever the matter may be." [6]

The purpose of this article is quite limited. We shall define and measure the magnitude of BATS and relate the magnitude of BATS to all state and local taxes and to all state and local taxes initially imposed on business, (SLTIIB). We use the acronym SLTIIB because businesses, *per se,* do not "pay" taxes. The ultimate incidence of taxes could result in lower profits for the owners of the business, lower payments for business inputs such as labor, or higher prices for sales to the ultimate consumers.[7] Despite the fact that the burden of SLTIIB is not borne by the business, it is well known that taxes can have a negative impact on business investment. Taxes lower the profit potential of entering new markets and are, therefore, factored into the cost-benefit analysis of potential investors.

Then we will compare BATS to measures of the size of the business sector — Gross Domestic Product of Private Business and "business income"[8] We will then discuss the possible effects of federal legislation to change state nexus standards on new business investment. We will then discuss the possible effects of changing BATS nexus standards on new business investment. We find that BATS is small relative to measures of the size of the business sector and that uncertainty regarding BATS nexus standards should have little effect on new business investment.

II. State and Local taxes Initially Imposed on Business

A. *All State and Local Taxes Initially Imposed On Business*

Before we examine BATS, it is useful to examine all SLTIIB, over time, and relative to all state and local taxes, and in relation to the overall size of the business sector. A study released by Ernst & Young and COST in April 2010 defines SLTIIB as:

1. Property taxes on business property
2. General sales tax on business inputs
3. Corporate income tax
4. Unemployment insurance
5. Business and corporate licenses
6. Excise and gross receipts taxes
7. Individual income tax on business income

8. Public utility taxes
9. Insurance premiums taxes
10. Other business taxes

Table 1 below shows the magnitude and the composition of SLTIIB for selected years 1980 to 2009. Property taxes were the largest state and local tax imposed on business representing 36 percent of total SLTIIB. These were followed by sales taxes which accounted for 23 percent of total SLTIIB.[9] Property taxes on business property and general sales tax on purchases of business inputs combined have averaged about fifty nine (59) percent of all SLTIIB during this period. Corporate income taxes were about 12.8 percent of SLTIIB in 1980 but declined in relative importance to about 7.1 percent in 2002. Since 2002, corporate income taxes, as a proportion of all SLTIIB, have risen to a maximum of about 10.6 percent in 2007 but have declined since then as a result of the recession. Business license taxes and individual income taxes on business income were 1.3 percent and 1.62 percent of all SLTIIB in 1980. These taxes have grown in relative importance to where they account for 6.5 percent and 5.5 percent of all SLTIIB in 2009 respectively.

Table 1: State and Local Taxes Initially Imposed on Business by Type: Total and as Percent of All State and Local Taxes Initally Imposed on Business: Selected Years 1980 to 2009

Year	All State & Local Taxes Initially Imposed on Business	Property Tax on Business Property	General Sales Tax on Business Inputs	Unemployment Insurance	Insurance Premiums Tax	Corporate Income Tax	Public Utility Taxes	Excise Taxes	Business License Taxes	Individual Income Tax on Business Income	Other Taxes Initially Imposed on Businesses
	(Billions)										
1980	$104.9	$38.0	$22.6	$5.5	$3.1	$13.4	$5.9	$4.6	$1.4	$1.7	$7.2
1985	164.1	57.6	37.1	9.1	4.5	19.3	10.0	7.2	2.8	2.2	11.8
1990	229.4	84.7	53.4	12.4	7.4	23.7	11.4	10.6	7.3	6.7	11.8
1995	303.2	110.7	70.2	15.8	8.6	31.7	15.0	16.0	11.4	9.7	14.1
2000	382.4	136.8	94.4	20.9	9.8	36.4	17.7	20.1	14.8	15.0	16.5
2001	395.3	142.6	97.6	20.8	10.3	35.8	17.9	20.2	15.0	16.2	18.9
2002	401.8	152.9	97.9	21.0	11.2	28.5	20.3	20.8	17.0	14.8	17.4
2003	424.2	160.9	100.9	23.9	12.6	31.9	21.2	21.9	16.8	14.6	19.5
2004	459.9	169.7	107.3	31.9	14.0	34.1	21.3	23.4	18.9	17.5	21.8
2005	502.0	176.6	115.2	35.5	14.9	43.5	22.6	23.9	29.5	21.5	18.8
2006	546.5	187.9	123.8	36.4	15.6	53.3	23.6	25.1	38.0	21.2	21.6
2007	577.4	199.9	131.5	35.8	16.1	60.9	26.8	28.3	32.9	23.6	21.6
2008	611.1	209.6	133.2	32.5	16.4	58.1	28.0	29.2	37.5	37.5	29.1
2009	590.0	215.3	126.9	30.7	15.6	50.6	28.8	26.3	38.3	32.3	25.2
	(Percent)										
1980	100.00%	36.22	21.54	5.24	2.96	12.77	5.62	4.39	1.33	1.62	6.86
1985	100.00%	35.10	22.61	5.55	2.74	11.76	6.09	4.39	1.71	1.34	7.19
1990	100.00%	36.92	23.28	5.41	3.23	10.33	4.97	4.62	3.18	2.92	5.14
1995	100.00%	36.51	23.15	5.21	2.84	10.46	4.95	5.28	3.76	3.20	4.65
2000	100.00%	35.77	24.69	5.47	2.56	9.52	4.63	5.26	3.87	3.92	4.31
2001	100.00%	36.07	24.69	5.26	2.61	9.06	4.53	5.11	3.79	4.10	4.78
2002	100.00%	38.05	24.37	5.23	2.79	7.09	5.05	5.18	4.23	3.68	4.33
2003	100.00%	37.93	23.79	5.63	2.97	7.52	5.00	5.16	3.96	3.44	4.60
2004	100.00%	36.90	23.33	6.94	3.04	7.41	4.63	5.09	4.11	3.81	4.74
2005	100.00%	35.18	22.95	7.07	2.97	8.67	4.50	4.76	5.88	4.28	3.75
2006	100.00%	34.38	22.65	6.66	2.85	9.75	4.32	4.59	6.95	3.88	3.95
2007	100.00%	34.62	22.77	6.20	2.79	10.55	4.64	4.90	5.70	4.09	3.74
2008	100.00%	34.30	21.80	5.32	2.68	9.51	4.58	4.78	6.14	6.14	4.76
2009	100.00%	36.49	21.51	5.20	2.64	8.58	4.88	4.46	6.49	5.47	4.27

Sources: *Robert Cline, Tom Neubig, and Andrew Phillips, Total State and Local Business Taxes: 50-State Estimates for Fiscal Year 2006, Ernst & Young, Washington, DC, February 2007, p. 15; and, 50-State Total State and Local Business Taxes, for 2009.*

Three ways to measure the relative size of SLTIIB are to compare them all state and local taxes; and to the size of the business sector as measured by the Gross Domestic Product of Private Business, and by business income. State and local governments currently rely on SLTIIB for about 45 percent of all their tax collections (see Table 2 below). This ratio has been fairly constant since 1990, rising with economic expansions and falling during periods of economic contraction. In 1980 and 1985, SLTIIB accounted for nearly 47 percent of all state and local taxes.

SLTIIB are a significant cost for private businesses – accounting for more than 5 percent of the Gross Domestic Product of Private Business. In comparison, labor compensation accounts for more than half of all income generated in the domestic business sector.[10] SLTIIB, as a percentage of Gross Domestic Product of Private Business, has been rising fairly consistently since 2002, the trough of the last recession. This coincides with the rapid rise in both state and local taxes on corporate profits and corporate profits before taxes.[11] SLTIIB when measured against business income, a narrower measure of

Table 2: State and Local Taxes Initially Imposed on Business: Total and as Percent of Gross Domestic Product of Private Business, Business Income, and as Percent of Total State and Local Tax Receipts: Selected Years 1980 to 2009

	All State & Local Taxes Initially Imposed on Business	Total State and Local Taxes	Gross Domestic Product of Private Business	Business Income	All State & Local Taxes Initially Imposed on Business		
					As Percent of:		
					All State and Local Taxes	Gross Domestic Product of Private Business	Business Income
Year	(billions)						
1980	$104.9	$223.4	$2,186.1	$756.2	46.96%	4.80%	13.87%
1985	164.1	350.3	3,461.5	1,257.1	46.85	4.74	13.05
1990	229.4	514.0	4,453.9	1,695.0	44.63	5.15	13.53
1995	303.2	676.4	5,677.8	2,280.3	44.83	5.34	13.30
2000	382.4	892.6	7,715.5	3,098.5	42.84	4.96	12.34
2001	395.3	929.4	7,913.6	3,144.7	42.53	5.00	12.57
2002	401.8	926.1	8,132.8	3,236.7	43.39	4.94	12.41
2003	424.2	966.2	8,502.8	3,376.2	43.90	4.99	12.56
2004	459.9	1,041.2	9,084.6	3,742.0	44.17	5.06	12.29
2005	502.0	1,130.0	9,695.5	4,108.7	44.42	5.18	12.22
2006	546.5	1,227.0	10,284.1	4,479.4	44.54	5.31	12.20
2007	577.4	1,311.3	10,771.4	4,421.9	44.03	5.36	13.06
2008	611.1	1,355.5	10,863.5	4,331.8	45.08	5.63	14.11
2009	590.0	1,299.1	10,520.8	4,272.5	45.42	5.61	13.81

Sources: *50- State Total State and Local Business Taxes for Fiscal Year 2009, " State Tax Notes, Tax Analysts, Inc, Falls Church, VA, April 10, 2010 Gross Domestic Product of Private Business and Business Income: Department of Commerce, Bureaau of Economic Analysis..*

incomes generated in the private sector, is now back to the ratios of SLTIIB to business income that occurred in the 1980's. From 200 through 2006, this ratio hovered around 12.4 percent.

B. Business Activity Taxes

There are no official definitions of Business Activity Taxes. For the sake of simplicity, we will use a subset of all SLTIIB defined by Cline, Fox, Neubig and Phillips – corporate income taxes; public utility taxes; excise and gross receipts taxes; business and corporate license taxes; and individual income taxes on business income. BATS currently constitutes about 30 percent of total SLTIIB; and, on average, has constituted about 28 percent of all SLTIIB since 1980. Currently, BATS comprises more than 13 percent of all state and local taxes. And have averaged about 12.4 percent of all state and local taxes since 1980 (see Table 3 below).

Although BATS as a percentage of all SLTIIB has remained fairly constant from 1980 to present, the composition of BATS has changed significantly (see Figure 1). For example, corporate income taxes, which accounted for more about one-half of BATS in 1980, made up slightly more than 28 percent of those taxes in 2002. Since then the share of BATS going to corporate income taxes has risen to more than 35 percent in 2007 This increase in the corporate income tax share of BATS is due to the rapid growth of corporate profits and thus corporate income taxes. In 2009, corporate income taxes were 27.7 percent of all BATS public utility taxes as a share of all BATS have declined fairly consistently since 1980, except for the period of 2001 to 2002. Conversely, business and corporate license taxes and individual income tax on business income have risen from $1.4 billion and $1.7 billion respectively in 1980 to $338.3 billion and

Table 3: Business Activity Taxes, by Type: Total and as Percent of: All State and Local taxes Initially Imposed on Business, All State and Local Taxes, and Business Income, Selected Years 1980 to 2009

Year	Business Activity Taxes: Total	Corporate Income Taxes	Public Utility Taxes	Excise & Gross Receipts Taxes	Business and Corporate License Taxes	Individual Income Tax on Business Income	As Percent of: All State and Local Taxes Initially Imposed on Business	All State and Local Taxes	Gross Domestic Product of Private Business	Business Income
	(billions)									
1980	$27.0	$13.4	$5.9	$4.6	$1.4	$1.7	25.74%	12.09%	1.24%	3.57%
1985	41.5	19.3	10.0	7.2	2.8	2.2	25.29	11.85	1.20	3.30
1990	59.7	23.7	11.4	10.6	7.3	6.7	26.02	11.61	1.34	3.52
1995	83.8	31.7	15.0	16.0	11.4	9.7	27.64	12.39	1.48	3.67
2000	104.0	36.4	17.7	20.1	14.8	15.0	27.20	11.65	1.35	3.36
2001	105.1	35.8	17.9	20.2	15.0	16.2	26.59	11.31	1.33	3.34
2002	101.4	28.5	20.3	20.8	17.0	14.8	25.24	10.95	1.25	3.13
2003	106.4	31.9	21.2	21.9	16.8	14.6	25.08	11.01	1.25	3.15
2004	115.2	34.1	21.3	23.4	18.9	17.5	25.05	11.06	1.27	3.08
2005	141.0	43.5	22.6	23.9	29.5	21.5	28.09	12.48	1.45	3.43
2006	161.2	53.3	23.6	25.1	38.0	21.2	29.50	13.14	1.57	3.60
2007	172.5	60.9	26.8	28.3	32.9	23.6	29.88	13.15	1.60	3.90
2008	190.3	58.1	28.0	29.2	37.5	37.5	31.14	14.04	1.75	4.39
2009	176.3	50.6	28.8	26.3	38.3	32.3	29.88	13.57	1.68	4.13

Source: Table 1 and Table 2.

$32.3 billion respectively in 2009. Business and corporate license taxes, as a proportion of all BATS, have quadrupled since 1980. In 1980, these taxes were slightly more than 5 percent of all BATS; in 2009 their share had risen to 21.7 percent. The rise in the share of individual income tax on business income can be attributable to the rise in the use of pass-through entities rather than traditional corporations as the preferred business form. Fox and Luna show that the rise of pass-through entities has reduced the rate of growth of corporate profits taxes.[12]

BATS remains a relatively small percentage of "business" income. During the period studied, BATS, as a proportion of business income, has ranged from a low of 3.1 percent in 2002 to 4.4 percent in 2008. When compared to the Gross Domestic Product (GDP) of these companies BATS is quite small. In 2009 BATS was approximately 1.7 percent of the GDP of private businesses (1.68%). Similarly, for the two preceding decades BATS has been roughly 1.5 percent of their GDP (averaging 1.31%). In 1980 and 1985, BATS as a proportion of GDP of private business were about 1.2 percent. Thus, while BATS is an important source of revenue for the State and local governments, it is a relatively small component of business costs in general and when compared to other SLTIIB.

In the next section, we ill discuss the possible impacts of the uncertainty of BATS nexus and the impact on electronic commerce and new business investment and.

III. BATS Impact on Electronic Commerce and Potential Business Investment

A. Electronic Commerce

As stated earlier, the purpose of H.R. 1439 is to facilitate the continued growth of e-commerce, job creation and the overall strength of the American economy. The use of the tax system to promote one form of commerce over other forms of commerce violates a canon of good tax policy – tax neutrality. Tax neutrality can be defined as;

> "...the tax being so designed as not to affect resource allocation either within or among the affected categories or between them and the other activities not subject to the tax."[13]

In less formal terms, the use of the tax system to promote e-commerce over other forms of commerce misallocates the nation's resources resulting in lower output and undue interference in consumer preferences. The use of the tax system to correct market imperfections is justified; however the taxes used to correct these imperfections are usually commodity taxes. If it can be shown with some degree of statistical certainty that state BATS nexus laws interfere with optimal consumer preferences regarding the type of commerce – e-commerce versus all other forms of commerce – than the use of the tax system to correct the resultant misallocation of resources. However, there is no evidence that current state BATS nexus laws have actually impeded the growth of electronic commerce, nor is there evidence that H.R. 1439 is the optimal tax policy to correct market distortions caused by state BATS nexus laws if such distortions actually exist. Furthermore, a 2004 study by, Bruce, Fox, and Deskins, showed that if there is a tax instrument that limits internet access and therefore the growth of e-commerce it is sales taxation of computer purchases.[14]

B. Effect on Business Investment

The expected rate of return, after taxes, and the risk or uncertainty regarding the rate of return is major determinants of new business investment. That being said, ***all*** taxes – Federal and state and local – play a significant role in determining the expected after-tax rate of return. When all SLTIIB are considered, it seems logical to expect that property taxes on business properties and sales and use tax on business inputs would have a larger impact on the investment decision than would BATS. These taxes account for approximately 60 percent of all SLTIIB; and, they directly affect the cost of acquiring and using physical capital. BATS are smaller, and indirectly affect the expected rate of profit. This hypothesis has not been tested here. It is logical to assume that uncertainty about whether a new investment would create nexus for a company would not cause that company to completely forego the investment; given that BATS are approximately 4 percent of business income. It would the case of the tip of the tail wagging the dog.

IV. Conclusion

While BATS remains an integral part of State revenues it is a small factor in terms of business income. The argument that uncertainty in states' BATS policy will have a "chilling" effect on new business investment is clearly not very convincing. In fact, property and use taxes, which are far greater costs, are much more likely to hinder investment than the relatively tiny BATS. Therefore, any attempts to make BATS nexus standards more uniform across states should be undertaken for the sake of reducing compliance costs for both businesses and revenue agencies and not for the sake of creating a new wave of investment.

More research is needed on the subject of how aspects of the administrative structure of business activity taxes affect business investment decisions.

(Endnotes)

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[2]Benjamin Franklin in a letter to Jean Baptiste Leroy (1789)
[3]Adam Smith, *The Wealth of Nations*, page 639 (Edited by S.M. Soares, MetaLibri Digital Library, May 29, 2007)
[4]http://BATscoalition.org/about.html
[5]http://BATscoalition.org/files/Goodlatte_02132009.pdf
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[7]Robert Cline, William Fox, Thomas S. Neubig, and Andrew Phillips, "A Closer Examination of the Total State and Local Business Tax Burden," *State Tax Notes*, Tax Analysts, Inc., Arlington, VA, January 23, 2003, p.295.
[8]Gross Domestic of Private Business is a set of accounts that present the contribution of each private industry to the Nation's gross domestic product (GDP). An industry's contribution is measured by its value added, which is equal to its gross output minus its intermediate purchases from domestic industries or from foreign sources. Business income is defined as Gross domestic income (GDI), is the costs incurred and the incomes earned in the production of gross domestic product (GDP) plus taxes on production and imports less subsidies. http://www.bea.gov/glossary/glossary.cfm?letter=G
[9]Andrew D. Phillips, Robert Cline, Thomas Neubig, and Julia C. Thayne, "50-State Total State and local Business taxes for 2009," *State Tax Notes*, April 26, 2010, pp. 275-295. Tax Analysts, Inc., Falls Church, Virginia.
[10]Bureau of Economic Analysis, http://www.bea.gov/national/nipaweb/TableView.asp?SelectedTable=293&ViewSeries=NO&Java=no&Request3Place=N&3Place=N&FromView=YES&Freq=Year&FirstYear=1980&LastYear=2006&3Place=N&Update=Update&JavaBox=no#Mid
[11]Elliott Dubin, "Trends in State Corporate Income Taxes Revisited," *Multistate Tax Commission Review,* Winter 2007, Vol. XX, No. 1, page 9.
[12]William F. Fox and LeAnn Luna, "Do Limited Liability Companies Explain Declining State Corporate Tax Revenues?" *Public Finance Review*, Vol. 33 No. 690-720.
[13]Harberger, Arnold C. "neutral taxation." The New Palgrave Dictionary of Economics. Second Edition. Eds. Steven N. Durlauf and Lawrence E. Blume. Palgrave Macmillan, 2008. The New Palgrave Dictionary of Economics Online. Palgrave Macmillan. 14 April 2011 <http://www.dictionaryofeconomics.com/article?id=pde2008_N000053> doi:10.1057/9780230226203.1178
[14]Donald Bruce, John Deskins, and William F. Fox, "Has Internet Access Taxation Affected Internet Use?" *State Tax Notes*, May 17, 2004, Tax Analysts, Inc., Falls Church, VA, pp. 519-525. This article was originally published in *Public Finance Review*, Vol 3, No.2, pp. 131-147, copyright 2004 Sage publications.

State and Local Finances: Where We're Going

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Try a little party game in which you ask your friends and neighbors where their tax dollars come from and where they go. Most will probably know their federal tax bite. They may also be able to tick off major federal spending programs like Social Security, Medicare, and national defense. It is likely that few, however, will mention the nation's 50 states and nearly 90,000 counties, cities, towns, school districts, and other local agencies.

That omission is unfortunate because states and localities do much of the heavy lifting in our federalist system. Although the federal government raises more revenue, states and localities undertake more spending on domestic goods and services (that is, spending net of intergovernmental grants and national defense). They outspent the federal government in nine of the last 10 fiscal years and in most years since World War II (**Figure 1**).[1] The exception was 2009, when federal expenditures spiked in response to the Great Recession.

As most Americans are probably aware, the recession also put state and local governments through a fiscal wringer. States in particular suffered historic revenue declines, with taxes plummeting 17 percent in the second quarter of 2009 compared with a year earlier.[2] At the same time, spending pressures mounted for Medicaid and other public assistance programs.

The result was record state budget gaps, estimated at up to $618 billion from fiscal 2009 through fiscal 2013.[3] In most states, lawmakers were called back to the bargaining table shortly after enacting a budget to find more revenue or spending cuts.[4] At the local level, revenues have been more stable but are starting to dip as state aid cuts take effect and property taxes increasingly reflect market values (**Figure 2**).[5]

Commentators frequently note that all states except Vermont are constitutionally or statutorily required to balance their budgets. Some requirements are looser than others, requiring the governor to propose, or the legislature to enact, a balanced budget rather

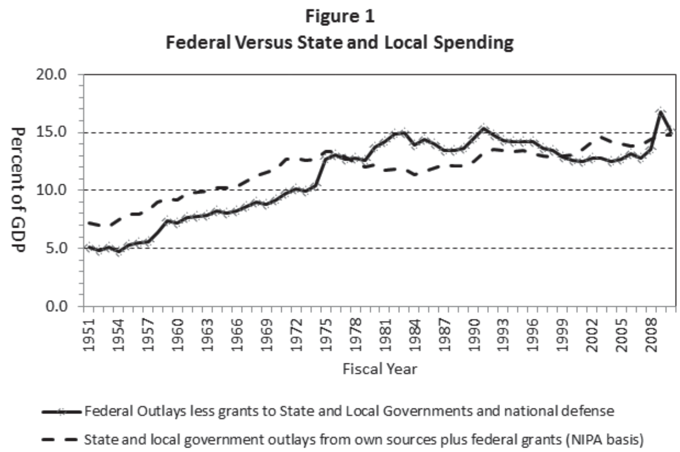
[1]U.S. Office of Management and Budget, ''Historical Tables, Budget of the United States Government, Fiscal Year 2012'' (Washington: U.S. Government Printing Office, 2011), available at http://www.whitehouse.gov/omb/budget/Historicals.

[2]Donald Boyd and Lucy Dadayan, ''State Tax Revenues Gained New Strength in Fourth Quarter'' (Albany: Rockefeller Institute of Government, 2011), available at http://www.rockinst.org/pdf/government_finance/state_revenue_report/2011_02_01_SRR_82.pdf.

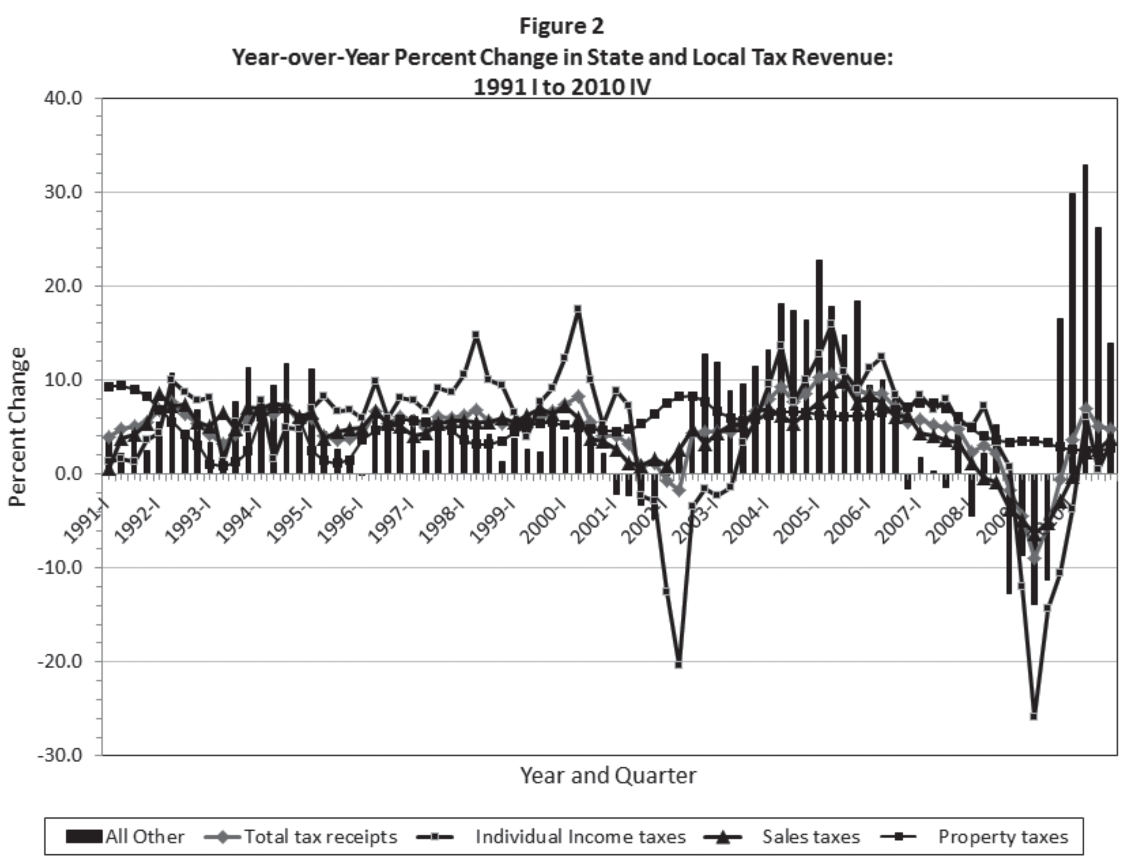
[3]Elizabeth McNichol, Phil Oliff, and Nicholas Johnson, ''States Continue to Feel Recession's Impact'' (Washington: Center for Budget and Policy Priorities, 2011), available at http://www.cbpp.org/files/9-8-08sfp_CBPP_03_2100.pdf.

[4]National Governors Association and the National Association of State Budget Officers, ''The Fiscal Survey of States'' (Washington: Fall 2010), available at http://www.nasbo.org/ LinkClick.aspx?fileticket=C6q1M3kxaEY%3d&tabid=38.

[5]Christopher Hoene and Michael A. Pagano, ''City Fiscal Conditions in 2010'' (Washington: National League of Cities, 2010), available at http://www.nlc.org/ASSETS/AE26793318 A645C795-C9CD11DAB3B39B/RB_CityFi scalConditions2010 .pdf. See also U.S. Congressional Budget Office ''Fiscal Stress Faced by Local Governments,'' Economic and Budget Issue Brief (Washington: U.S. Government Printing Office, 2010), available at http://www.cbo.gov/ftpdocs/120xx/doc12005/1209-Municipalities_Brief.pdf.



Source: U.S. Office of Management and Budget (2011)



Source: U.S. Department of Commerce, Bureau of Economic Analysis than preventing a state from carrying over a deficit year to year. However, bond markets also tend to limit funds for deficit-related borrowing.

States and localities must therefore increase taxes or cut spending to balance their books. Those actions can harm vulnerable populations and short circuit a national economic recovery. States and localities are the nation's largest employer — responsible for one out of seven jobs — and in most years they contribute a third percentage point in real annual GDP growth. In 2009, however, their contribution was negative.[6] Since the start of the recession, local governments have cut 377,000 jobs and surveys suggest as many as 481,000 more cuts may be coming.[7]

Concerned about those spillover effects, federal policymakers often provide aid for state and local governments. Examples include the Antirecession Fiscal Assistance program, the Local Public Works program, and the Comprehensive Employment and Training Act of the early 1970s. More recently, the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA) provided $10 billion in state fiscal relief through a temporary increase in federal Medicaid matching rates.[8]

The American Recovery and Reinvestment Act of 2009 (ARRA) went much further, directing more than $280 billion to states and localities, including roughly $135 billion in flexible funds. Under ARRA, federal grants are estimated to have reached a historic peak in nominal terms and as a share of GDP.[9] Nevertheless, ARRA covered at most 40 percent of state budget shortfalls; and most payments will expire next year, while revenue is not expected to recover for another two to three years because of standard lags in rehiring and reinvestment.

The longer term is even more troubling. Sovereign debt crises abroad and a few high profile municipal bankruptcies at home have some observers worried about a tsunami of state and local defaults.[10] Although those worries may be overstated, difficult challenges loom.[11] In particular, states and localities face unfunded pension and retiree health care obligations of up to $4 trillion depending on modeling assumptions.[12] The U.S. Government Accountability Office has estimated that rising health care costs and aging populations — the same pressures busting the federal budget — will lead to operating shortfalls on the order of 5 to 6 percent of GDP by 2060.[13]

Say that you were still at that party and, unbelievably, your friends and neighbors were still listening. Is there any room for optimism?

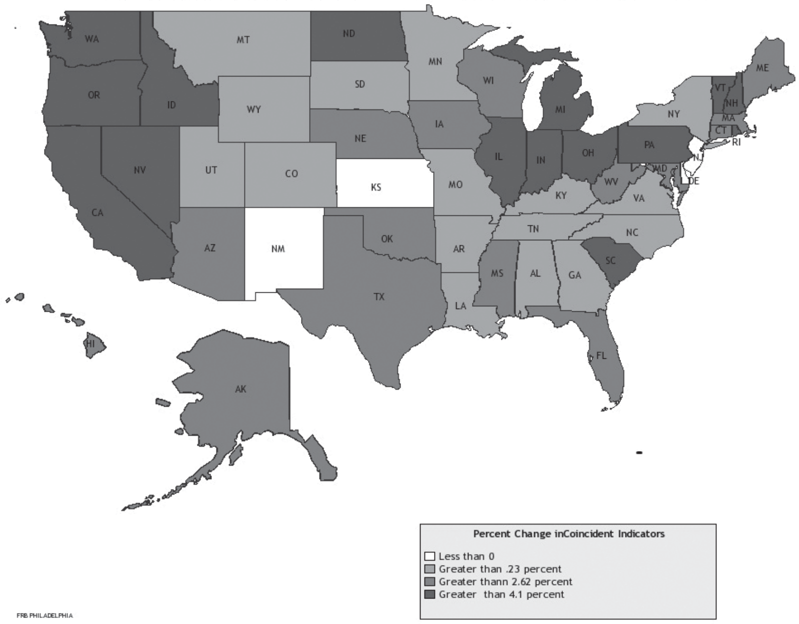
[6]U.S. Bureau of Economic Analysis. ''National Income and Product Accounts'' (Washington: U.S. Government Printing Office, 2011), available at http://www.bea.gov/national/ nipaweb/SelectTable.asp.
[7]U.S. Bureau of Labor Statistics, ''BLS News Release March 4, 2011, page 3. available at http://www.bls.gov/news.release/pdf/empsit.pdf; Christopher W. Hoene and Jacqueline J. Byers, ''Local Governments Cutting Jobs and Services'' (Washington: National League of Cities and National Association of Counties, 2010), available at http://www.nlc.org/ ASSETS/06F2CD78F5FB4A7DA1B84D A4A92008A8/LJAreport_ FINAL.pdf.
[8]Richard H. Mattoon, ''Should the Federal Government Bail Out the States? Lessons From Past Recessions,'' Chicago Fed Letter 265 (Chicago: Federal Reserve Bank of Chicago, 2010), available at http://www.chicagofed.org/digital_assets/ publications/chicago_fed_letter/2009/cflaugust2009_265.pdf.
[9]U.S. Office of Management and Budget (2011).
[10]See, e.g., David Wessel, ''Local Debts Defy Easy Solution,'' The Wall Street Journal, Sept. 23, 2010, available at http://online.wsj.com/article/SB10001424052748704814204575507842266619222.html); Michael Cooper and Mary Williams Walsh, ''Mounting Debts by States Stoke Fears of Crisis,'' The New York Times, Dec. 4, 2010, available at http://www.nytimes.com/2010/12/05/us/politics/05states.html?_r=1&pagewanted=1.
[11]As noted below, local government defaults (missed debt service payments) and bankruptcies are rare. Only 16 states authorize local governments to declare bankruptcy, although 10 provide limited access. Unlike personal or corporate filings, the threshold for a municipality to declare bankruptcy is insolvency, or inability to pay debts. Also, judges cannot order a municipality to liquidate, so there are often holdout problems as in Vallejo, Calif., where bankruptcy proceedings have continued since May 2008. See, e.g., Milken Institute and the Ewing Marion Kauffman Foundation, Ensuring State and Municipal Solvency (New York and Santa Monica, Calif.: Milken Institute and the Ewing Marion Kauffman Foundation, 2010), available at http://www.kauffman.org/uploaded files/ensuring-state-and-municipal-solvency.pdf.
[12]Pew Center on the States, ''The Trillion Dollar Gap: Underfunded State Retirement Systems and the Road to Reform'' (Washington: Pew Charitable Trusts, 2010), available at http://downloads.pewcenteronthestates.org/The_Trillion_Dollar_Gap_final.pdf; Robert Novy-Marx and Joshua Rauh, ''Policy Options for State Pension Systems and Their Impact on Plan Liabilities,'' NBER Working Paper #16453, October 2010, Cambridge, Mass.: National Bureau of Economic Research, available at http://www.nber.org/papers/ w16453.; Robert Novy-Marx and Joshua Rauh, ''The Crisis in Local Government Pensions in the United States,'' working paper, Oct. 13, 2010, available at http://www.kellogg.north western.edu/faculty/rauh/research/NMRLocal20101011.pdf.
[13]U.S. Government Accountability Office, ''State and Local Governments' Fiscal Outlook,'' GAO-10-358 (Washington: U.S. Government Printing Office, 2010), available at http:// www.gao.gov/new.items/d10358.pdf.

Maybe. First, as has been widely reported, revenue collections are picking up. State and local tax receipts were up almost 5 percent in the fourth quarter of 2010, compared with the same time last year.[14] To be sure, much of that increase is the result of $24 billion in legislated — and often temporary — tax rate increases.[15] Without those changes in states like California, New York, North Carolina, and Massachusetts, nominal tax receipts would have declined slightly in the second quarter of 2010. Even with those actions, state tax revenue remains significantly below their pre-recession peak.[16] Nevertheless, we have now seen three consecutive quarters of revenue increases as compared with previous years, a welcome change from five consecutive quarters of negative growth in 2008 and 2009.

Second, just as the average national temperature is not terribly informative, neither are average state fiscal conditions. Some states are emerging from the Great Recession faster than others as illustrated by the Philadelphia Federal Reserve Bank's State Coincident Index (a composite of labor market measures, including non-farm payroll employment, average hours worked in manufacturing, the unemployment rate, and real wage and salary disbursements). For the three-month period ending in February 2011, 46 states saw an improvement, while 4 (Delaware, Kansas, New Jersey and New Mexico) saw reductions.[17] Again, the latest news compares favorably with May through August 2010, when the three-month index was in decline for 7 states. (**Figure 3**).

Figure 3

Percent Change in Coincident Indiators, November 2010 to February 2011, at Annual Rates



Unfortunately, some states started farther behind. To take one example, most states experienced their pre-recession revenue peak in fiscal 2008. For Michigan, the peak year was 2000.[18]

Put another way, states differ in their underlying fundamentals, or fiscal capacity. One way to see that is by applying national average state and local tax rates to the economic conditions in each state, as under the Representative Revenue System. In a 2002 study, Yesim Yilmaz and coauthors performed this exercise and found that the average U.S. state had a revenue capacity of $4,659.[19] The top five states were Connecticut, Delaware, Massachusetts, Alaska, and New Jersey, while the bottom five were Mississippi, West Virginia, Arkansas, Alabama, and Oklahoma. Results were qualitatively similar in 2005, although they may have changed more recently.

Consider two states that have been in the news lately. Illinois recently reported the largest midyear state budget shortfall in the nation at

[14]U.S. Bureau of Economic Analysis (2011).
[15]NASBO and NGA (2010).
[16]Boyd and Dadayan, supra, note 2.
[17]Federal Reserve Bank of Philadelphia (2011), ''State Coincident Indicators'' (Philadelphia: Federal Reserve Bank of Philadelphia, 2010), available at http://www.philadelphia fed.org/research-and-data/regional-economy/indexes/coincide nt/.

[18]Eric Scorsone and David Zin, ''The Michigan Economy and State Revenue: A 10-Year History'' (1999-2009) (Lansing: Senate Fiscal Agency, 2010), available at http://www. senate.michigan.gov/sfa/Publications/Issues/StateRevenueTenYears/StateRevenueTenYears.pdf.
[19]Yilmaz, Yesim, Sonya Hoo, Matthew Nagowski, Kim Rueben, and Robert Tannenwald, ''Fiscal Disparities Across States, FY 2002'' (Washington: Urban Institute and the New England Public Policy Center at the Federal Reserve Bank of Boston), available at http://www.urban.org/url.cfm?ID=311 -403.

$13 billion, or 47 percent of its general fund.[20] California was dubbed the ‘‘Lindsay Lohan of States’’ after its non-partisan Legislative Analyst’s Office projected $20 billion plus shortfalls through fiscal 2016.[21] The two are tied for the lowest credit rating of any state, and they topped bank analyst Meredith Whitney’s list of states in fiscal trouble, with California in first place and Illinois tied for second with New Jersey, Illinois, and Ohio.[22]

The gap between revenue capacity and effort means that if Illinois levied taxes and fees at nationally representative rates, it would have raised an additional $3.8 billion.

However, a look at those states’ revenue capacities reveals a more complicated picture (**Table 1, next page**). All those states except Ohio had above average revenue capacity as of 2002, but only California and New Jersey demonstrated above average revenue effort (actual collections). The gap between revenue capacity and effort means that if Illinois levied taxes and fees at nationally representative rates, it would have raised an additional $3.8 billion or 7 percent of total revenue in 2002. More recent analyses also suggest that Illinois, like many states, has untapped revenue potential in income and retail sales taxes (especially in broadening the base to include services).[23]

No discussion of state finances would be complete without mentioning political gridlock. California is notorious for budgets that arrive late and are balanced on a wing and a prayer.[24] Illinois and New York also missed their budget deadlines this year because of partisan wrangling.

In California a recent initiative lowered the vote threshold for new state budgets and may improve timeliness. However, legislators will still have to contend with recalcitrant voters. Residents of California and other fiscally challenged states, including Arizona, Florida, Illinois, and New York, are united in the belief that their state is headed in the wrong direction.[25] At the national level, large majorities say that they will resist any actions to balance state budgets, including spending cuts, tax increases, and a federal bailout.[26]

What about recent talk of a U.S. state and local debt crisis? Comparisons with Greece, Ireland, and Spain have escalated in recent weeks amid mutual fund sell-offs and rising yields for of municipal bonds and credit default swaps.[27] There is some disagreement about whether those trends reflect a heightened awareness of state and local fiscal troubles or just adjustments in the municipal bond market. In particular, with the end of the Build America Bonds (BABs) program on December 31, 2010, states and localities may be upping the supply of new issues, thereby depressing prices and

[20] National Conference of State Legislatures, ‘‘State Budget Update,’’ Denver, National Conference of State Legislatures, November 2010, available at http://www.ncsl.org/ ?TabId=21829.
[21] NCSL (2010); Allysia Finley, ‘‘California: The Lindsay Lohan of States,’’ The Wall Street Journal, Nov. 2, 2010. Available at http://online.wsj.com/article/SB1000142405274 8703506904575592612400443370.html.
[22] Betty Liu and Martin Z. Braun, ‘‘Whitney Says U.S. States May Need Federal Bailout,’’ Bloomberg, Sept. 30, 2010, available at http://www.bloomberg.com/news/2010-09-30/ whit ney-says-states-may-need-federal-bailout-in-next-12-months .html.
[23] Matthew N. Murray, ‘‘The Search for Revenues to Fill the Illinois Fiscal Gap,’’ Presentation to the Chicago Federal Reserve Bank, June 2010, available at http://www.chicagofed.org/digital_assets/others/events/2010/charting_illinois _fiscal_future/murray. pdf. (Illinois lawmakers voted on January 12, 2010, to increase individual income tax rates from 3 percent to 5 percent and corporate rates from 4.8 percent to 7 percent. The increases are expected to raise roughly $7 billion annually for the next four years before being rolled back to 3.75 and 5.25 percent, respectively.)
[24] Tracy Gordon, ‘‘The Year of Magical Thinking,’’ Tax Vox: The Tax Policy Center Blog (Washington: Urban Institute and Brookings Institution Tax Policy Center, 2010), at http://taxvox.taxpolicycenter.org/blog/_archives/2010/10/12/46 53983.html.
[25] Pew Center on the States and Public Policy Institute of California, ‘‘Facing Facts: Public Attitudes and Fiscal Realities in Five Stressed States’’ (District of Columbia and San Francisco: Pew Charitable Trusts and PPIC, 2010), available at http://www.ppic. org/main/publication.asp?i=951.
[26] Pew Research Center for the People & the Press, ‘‘Public Rejects Variety of Options for Fixing State Budgets’’ (Washington: Pew Research Center, 2010), available at http:// people-press.org/ report/628/.
[27] Dan Seymour, ‘‘Muni Mutual Funds Keep on Bleeding,’’ Bond Buyer, Dec. 13, 2010, available at http://www. bondbuyer. com/issues/119_486/-1021008-1.html; Josh Barro, ‘‘Evaluating States’ Credit With Bond Yields,’’ Issue Brief 6 (New York: Manhattan Institute, 2010), available at http:// www.manhattan-institute.org/html/ib_06.htm.

Table 1

Representative Revenue System Rankings

State	Total Per Capita Revenue Capacity	Revenue Capacity Index	Rank	Total Per Capita Revenue	Index	Rank	Revenue Capacity (billions)	Revenue Collections (billions)
United States	$4,659	100		$4,659	100		$1,338.9	$1,338.9
California	$5,075	109	11	$5,174	102	20	$177.6	$181.0
Illinois	$4,844	104	15	$4,540	94	37	$61.0	$57.1
New Jersey	$5,657	121	3	$5,554	98	29	$48.5	$47.6
Ohio	$4,369	94	27	$4,584	105	13	$49.8	$52.3

Source: Yilmaz et al, (2006).

raising yields.[28]

Alternatively, municipal bond investors may be expressing uncertainty about a future without not only BABs but also other financial instruments — variable rate demand obligations, auction rate securities, and tender option bond pricing — that have until recently made long-term debt more palatable to short-term buyers. Although new products may be emerging, some analysts suggest that muni yields are returning to higher pre-credit bubble levels.[29]

Also, it is important to recall some differences between U.S. states and localities and the eurozone. U.S. state and local debt levels are modest compared with those of sovereign nations in trouble — for example, 16 percent of GDP in 2009 compared with Greece's 127 percent.[30] Moreover, states and localities issue debt to build physical assets like bridges and airports, not to finance day-to-day operations. Short-term borrowing generally constitutes no more than 2 percent of municipal debt outstanding.[31] As a result, states and localities are less vulnerable to so-called rollover risk when short-term notes come due but further borrowing is prohibitively expensive.[32]

U.S. states and localities have other strengths as well. In addition to explicit debt and implicit pension and other liabilities noted above, states and localities have assets (**Table 2**). As of the fourth quarter of 2010, they held $2.7 trillion (18 percent of GDP) in financial assets apart from employee retirement funds and another $8.4 trillion in nonfinancial assets such as buildings.[33] Although not all those assets are liquid, similar to untapped revenue capacity, some might be leveraged through sale-leaseback and other one-time arrangements.[34]

[28]The BABs program was created under ARRA. Unlike traditional tax-exempt municipal bonds, BAB payments to investors are taxable, but the federal government subsidizes 35 percent of the issuer's borrowing costs. That feature allows the federal government to provide a deeper and more targeted subsidy to state and local governments. The tax exemption also can make state and local debt more attractive to foreign investors. U.S. Congressional Budget Office and Joint Committee on Taxation, ''Subsidizing Infrastructure Investment with TaxPreferred Bonds'' (Washington: U.S. Government Printing Office, 2010), available at http://www.cbo.gov/ ftpdocs/106xx/doc10667/10-26-TaxPreferredBonds.pdf. See also Diana B. Henriques, ''Revised Fed Data Raises Doubt on Foreign Appetite for Build America Bonds,'' The New York Times, Dec. 9, 2010, available at http://www.nytimes.com/ 2010/12/10/business/economy/10muni.html?scp=1&sq=revise d%20fed%20data%20raises%20doubts&st=cse.

[29]Dan Seymour, ''BABs: The Last Pillar Standing,'' Bond Buyer, Nov. 29, 2010, available at http://www.bondbuyer.com/ issues/119_476/build_america_bonds-1020407-1.html.

[30]Those comparisons do not account for state and local taxpayers' share of total debt. See, e.g., U.S. Congressional Budget Office, ''Economic Impacts of Waiting to Resolve the Long-Term Budget Imbalance'' (Washington: U.S. Government Printing Office, 2010).

[31]U.S. Census Bureau, 2008 Annual Surveys of State and Local Government Finances (Washington: U.S. Government Printing Office, 2010), available at http://www.census.gov/ govs/estimate/.

[32]That is not to say that states don't experience cash crunches. California famously paid vendors with IOUs in 2009, and Illinois is currently seeking investors to help cover $4.5 billion in overdue bills. Mike Spector and Michael Corckery, ''Illinois Seeks Wall Street Cash,'' The Wall Street Journal, Dec. 11, 2010, available at http://online.wsj. com/article/SB10001424052748703727804576011644076639916.html.

[33]Board of Governors of the Federal Reserve System, ''Flow of Funds Accounts of the United States,'' Table L.105, March 10, 2011, available at http://www.federalreserve.gov/ releases/z1/current/. Also see: http://www.bea.gov/national/nipaweb/Ni_FedBeaSna/TableView.asp?SelectedTable=17&FirstYear=2006&LastYear=2010&Freq=Qtr

[34]Of course, sale and lease-back arrangements can involve many issues. See, e.g., Michael Cohen, ''Sale Leaseback of State Office Buildings'' (Sacramento: California Legislative Analyst's Office, 2010), available at http://www.lao.ca.gov/ reports/2010/infr/sale_leaseback/sale_leaseback_110910.pdf.)

Finally, states and localities have staying power. Unlike corporations, they have the power to tax, although, of course, taxpayers may flee if they don't feel they are getting their money's worth and if there's someplace more attractive or less financially burdened to go. As sovereign entities, states cannot legally declare bankruptcy. Municipal defaults and bankruptcies are rare and usually limited to special purpose entities, like water districts.[35]

So what is to be done? Recent dust-ups over extensions of unemployment insurance and enhanced federal Medicaid matching funds for states suggest further help from Washington will not be coming.

However, states and local governments are not sitting idly by. Most states have set up tax reform or performance review commissions to look for efficiency improvements.[36] Many states are identifying cost savings through prison reform, school district consolidation, and public employee compensation restructuring, among other areas.[37] The federal government has also gotten into the act, providing incentives for local policy innovation (for example, Race to the Top education funds).

To be sure, state and local governments face difficult days and even years. However, as we've heard a lot lately, crises also create opportunities. States and localities may find new ways to raise revenue and provide services that are valued by taxpayers — or to drop the ones that aren't. Living up to Justice Louis Brandeis's vision of the state and local sector as a ''laboratory of democracy'' may be one way for those often overlooked governments to stand up and be noticed.

Table 2

State and Local Government Assets and Liabilities (excluding employee retirement funds) 2010 -IV

	(Billions)	Percent of Gross Domestic Product
Total financial assets	$2,739	18.4%
Checkable deposits and currency	91.6	0.6
Total time and savings deposits	275.5	1.9
Money market mutual fund shares	90.9	0.6
Federal funds and security repurchase agreements	174.0	1.2
Credit market instruments	1,373.2	9.2
Commercial paper	49.4	0.3
Treasury securities, including SLGS	519.8	3.5
Agency- and GSE-backed securities;	449.4	3.0
Municipal securities and loans	6.4	0.0
Corporate and foreign bonds	163.9	1.1
Total mortgages	184.5	1.2
Corporate equities	115.3	0.8
Mutual fund shares	37.6	0.3
Trade receivables	183.5	1.2
Taxes receivable	298.0	2.0
Unidentified miscellaneous assets	99.2	0.7
Total liabilities	3,135.2	21.1
Credit market instruments	2,464.7	16.6
Municipal securities and loans	2,450.3	16.5
Short-term municipal securities and loans	150.0	1.0
Long-term municipal securities and loans	2,300.3	15.5
U.S. government loans	14.4	0.1
Trade payables	670.5	4.5

Source: Board of Governors of the Federal Reserve System, (2011).

[35]U.S. Congressional Budget Office (2010).
[36]National Association of State Budget Officers, ''Recommendations from State Restructuring Commissions and Agencies'' (Washington: 2010), available at http://www. nasbo.org/LinkClick.aspx?fileticket=7nTvXpAImnY%3d&tab id=138.
[37]Lauren Stewart, ''State Government Redesign Efforts 2009 and 2010'' (Washington: National Governors' Association, 2010), available at http://www.nga.org/Files/pdf/101 0STATEGOVTREDESIGN.PDF.

State and Local Finances: Part Two

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Multistate Tax Commission

I. Introduction

In the preceding article, Professor Tracy Gordon illustrated the difficulties facing state and local governments – falling revenues combined with rising expenditures resulting in budget gaps that must be filled currently. Dan White's recent commentary reinforces Professor Gordon's findings. Mr. White, using data from the Center on Budget Policies and Priorities, projected that all states, with the exception of Alabama, Alaska, Arkansas, North Dakota, and Wyoming, will face more budget gaps in fiscal 2012. In nine of those states, the budget gaps will exceed more than 20 percent of the states' 2011 expenditures. Mr. White noted that local governments are also financially challenged due to falling state aid, states shifting responsibility for some programs, and for the first time since 1979, a decline in property tax collections. State and local pension funds are also in financial difficulty, but those problems are in the not-too-distant future. The problems have been exacerbated in some states as the need to maintain current services have forced them to delay making deposits to their employee pension funds. [1]

Congress has also taken note of the fiscal troubles facing state and local governments. The major concern is that the current difficulties confronting state and local governments will force these governments to take actions that will weaken the current economic recovery. In order to forestall such an event, state and local governments may require additional federal assistance. In addition, Congress is concerned state bankruptcy and the increase in bond default risk. Another major concern for Congress, albeit in the future, is underfunding of state and local pensions and the possible cost of bailing out these funds.[2]

Congressional concern about state and local government actions that could weaken the recovery is indeed well founded. In addition to raising revenues, state and local governments have been cutting expenditures. In the fourth quarter of 2010, real gross domestic product increased at an annual rate of 3.1 percent, despite a decrease in real spending by state and local governments of 2.6 percent (annualized rate). State and local government contribution to real GDP growth in the fourth quarter was negative 0.31 percent. That is, if state and local governments maintained their rate of spending, real GDP growth in the fourth quarter would have been approximately 3.4 percent.[3]

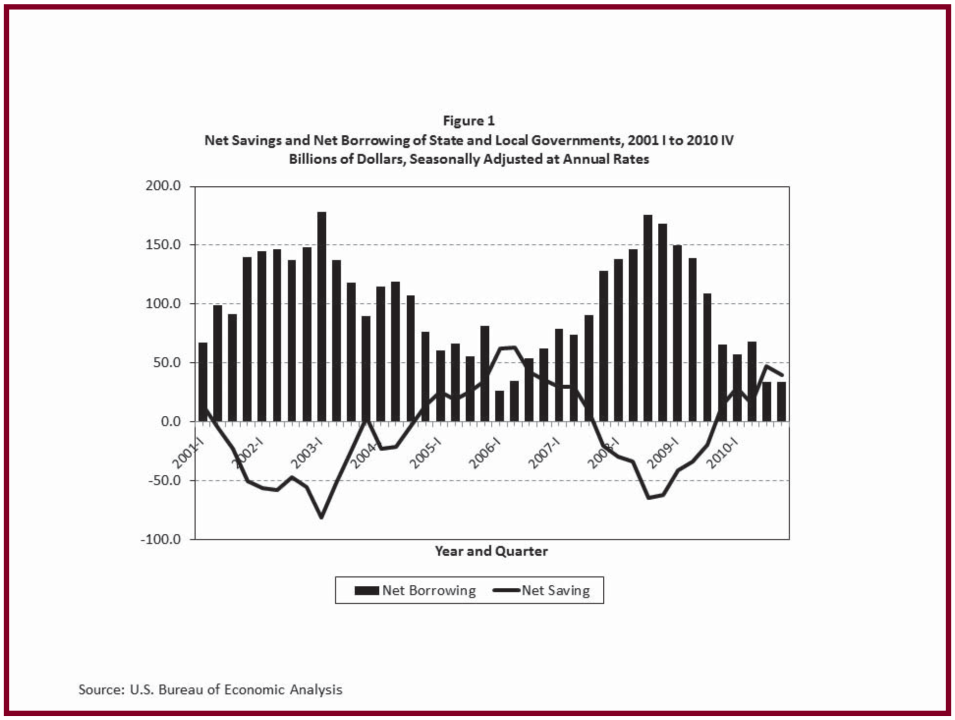
However, things may not be all bad for state and local government finances. Professor Gordon did hint that while the current fiscal condition of state and local governments is bad, the good (?) news is that fiscal conditions are not necessarily getting worse. Tax revenues have been rising for the past year due to a slowly improving economy and tax rate increases. These tax increases have been used to offset the decline in Federal aid.

This short article presents traditional views of the fiscal condition of state and local governments – trends in net saving and net borrowing, trends in receipts and spending, and another measure of state and local fiscal conditions beyond current deficits -- the net worth of state and local governments, excluding state and local government pension funds. The more traditional measures of the

[1]Dan White, "State and Local Government Outlook: A Fiscal Tightrope," Dismal Scientist, Moody's Analytics, February 28, 2011. Available by subscription at: http://www.economy.com/dismal/pro/article.asp?cid=196773.

[2]Steven Maguire, "State and Local Government Debt: An Analysis." Congressional Research Service Report for Congress, RA 1735, March 31, 2011, p.1.

[3]U.S. Department of Commerce, Bureau of Economic Analysis, http://www.bea.gov/national/nipaweb/TableView.asp?SelectedTable=2&Freq=Qtr&FirstYear=2008&LastYear=2010



fiscal condition of state and local governments – revenues, spending, and deficits may be regarded as the income and loss statement. The net worth of state and local governments is akin to the balance sheet of a business. While this imperfect measure shows an improvement in state and local government financial conditions; state and local governments are still under fiscal stress because of the requirement to cover budget gaps in the short-term. Furthermore, employee retirement systems in many states are underfunded which will add to future budgetary problems.

Both this article and the previous article treat state and local governments as if they were a single entity. In reality, there are almost 90,000 local government units – both general purpose and special purpose governments.[4] However, state and local governments are financially intertwined. In fiscal year, approximately one third of local government revenues came from state governments.[5]Thus, the aggregate measures of fiscal conditions may not apply to any individual unit of local government or to any state government.

The next section presents the measures of state and local government fiscal conditions. The third section discusses the findings; and the fourth section is the summary and conclusion.

II. State and Local Government Fiscal Conditions

A. Traditional Measures – Receipts and Expenditures NIPA Basis

Perhaps the simplest measure of state and local government fiscal conditions is the difference between how much revenue is taken in and how much is spent. Figure 1 below shows the difference between state and local government current expenditures and current revenues (net saving), and the difference between total revenues and total expenditures (net borrowing). Current revenue includes: tax revenues, federal grants-in-aid, income receipts (interest, dividends, etc.) on assets, contributions for social insurance (employee retirement, workers compensation, and temporary disability), current surplus or deficit of government enterprises, and other minor receipts. Current expenditures include: consumption expenditures, social benefits payments, and interest payments. Total receipts include current receipts plus federal grants-in-aid for capital expenditures. Total expenditures include current expenditures plus gross investment less capital consumption allowances plus net purchases of non-produced assets.[6]

The levels of state and local government net saving and net borrowing are clearly influenced

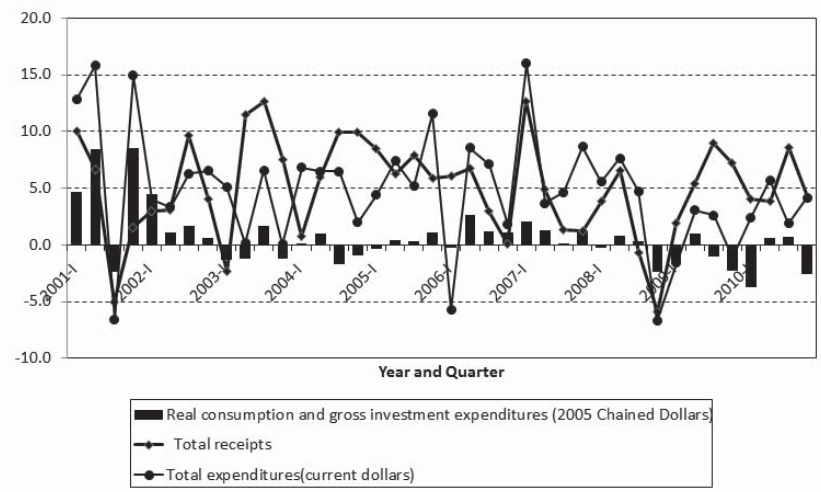
[4]http://www.census.gov/govs/cog/GovOrgTab03ss.html
[5]U.S. Census Bureau, ***State and Local Government Finance Summary Report, 2008***, http://www2.census.gov/govs/estimate/08statesummaryreport.pdf.

[6]See U.S. Department of Commerce, Bureau of Economic Analysis, http://www.bea.gov/national/nipaweb/TableView.asp?SelectedTable=88&Freq=Qtr&FirstYear=2008&LastYear=2010

by the cyclical changes in the overall economy; and, are mirror images of each other. From 2001 1 to 2003 1 net savings declined from approximately $16 billion to -$81 billion.[7] Similarly, net borrowing increased from a seasonally adjusted annual rate of $67 billion to nearly $178 billion in the first quarter of 2003. State and local government net saving reached a peak of $63 billion in the second quarter of 2006 and declined to a trough of -$65 billion in the fourth quarter of 2008. Net borrowing rose from a seasonally adjusted annual rate of $26 billion in 2006 1 to $176 billion in the fourth quarter of 2008. Since 2009 IV, state and local government net saving has been positive. In the third quarter of last year, net savings reached nearly $48 billion; in the last quarter of last year net saving s were approximately $40 billion. Net borrowing has declined from $176 billion in the last quarter of 2008 to about $34 billion in the third and fourth quarters of 2010.

The recent improvement in net savings and the reduction in net borrowing can be attributed partly to economic growth, partly to legislated revenue increases, and partly to budget cutting by state and local government policy makers. For the past two years, with the exception of 2010 II, the annualized rate of growth of state and local government receipts, from all sources, has outpaced the rate of growth of total state and local government expenditures (See Figure 2). This has not always been the case. Prior to 2009, the rate of growth of expenditures usually exceeded the rate of change of total receipts. An extreme example of the differences between changes in expenditures and revenues took place in the fourth quarter of 2001. In that period, total expenditures grew at a seasonally adjusted annual rate of nearly 15 percent and total receipts grew at a seasonally adjusted annual rate of nearly 1.6 percent.

Figure 2
Percent Change from Preceding Quarter, at Annual Rates, 2001 I to 2010 IV



Source: U.S. Bureau of Economic Analysis

Annualized rates of change in state and local government consumption and gross investment expenditures[8] in constant 2005 chained dollars have also been relatively low in the past few years. The first quarter of 2007 was the last period in which the annualized rate of growth exceeded 2 percent. Constant dollar consumption and gross investment expenditures have declined seven times in the

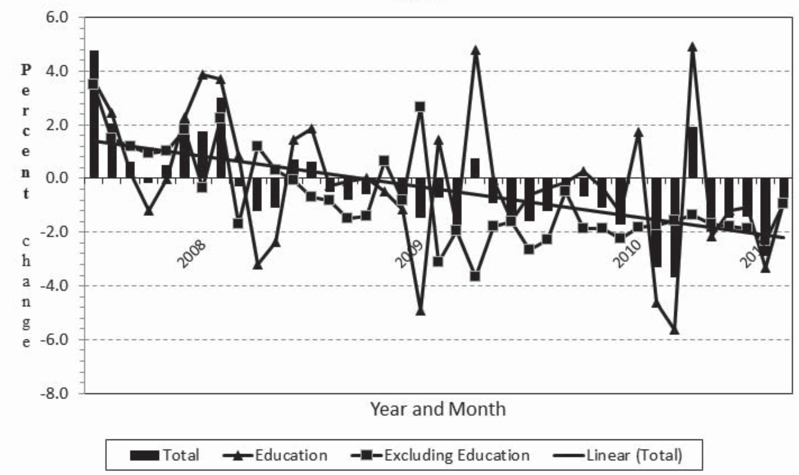
[7]Figures are seasonally adjusted at annual rates.

[8]Government consumption expenditures are services such as education, police, and fire protection that are valued at their cost of production. Sales to other sectors of government and own account investment (construction and software) are excluded. Gross investment consists of purchases or creation of fixed assets for general government and government enterprises; inventory investment is included in government consumption expenditures.

last twelve quarters.

One reason for the decline in state and local government consumption expenditures is the recent decline in state and local government employment. Data from the Bureau of Labor Statistics show that total state and local government employment has declined fairly consistently since the recent peak of 19.811 million (seasonally adjusted at annual rates) reached in August of 2008 to 19.314 million (preliminary) in March of this year – a decrease of nearly one-half million employees. Education employment has declined by approximately 190 thousand since September 2008 – from 10.488 million to 10.298 million. The number of state and local government employees in functions other than education decreased by 315 thousand during the period of August 2008 to March of this year.[9] Figure 3 presents the percentage change in the number of state and local government employees from the preceding month, at annualized rates. As shown on Figure 3, there is an accelerating negative trend in state and local government employment. In January of 2008, total state and local government employment was growing by 1.6 percent per year. In March 2011, the trend line indicated that state and local government employment was declining by slightly more than 2.0 percent per year.

Figure 3
Percent Change in State and Local Government Employment from Preceding Month at Annual Rates, January 2008 through March 2011



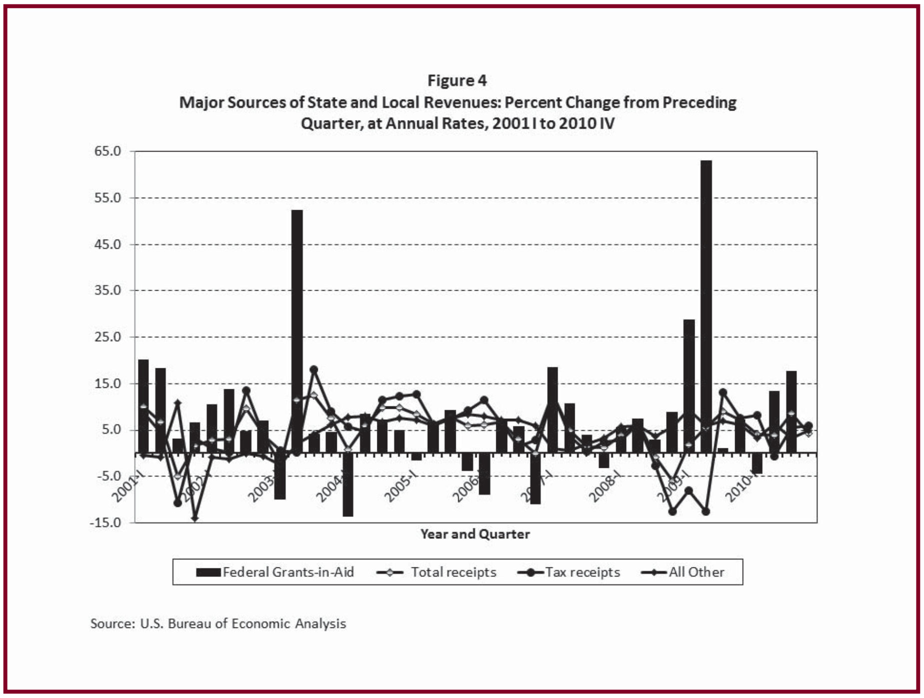
Note: employment data are seasonally adjusted at annual rates

Source: U.S. Bureau of Labor Statistics

Figure 4 presents quarterly percent changes at annualized rated in state and local government receipts by major type from 2001 I to 2010 IV. The current recession's impact on tax receipts has been dramatic. For the four quarters, beginning with the third quarter of 2008, tax receipts declined by 2.7 percent, 12.5 percent, 7.9 percent, and 12.5 percent respectively. Total receipts declined by 0.7 percent and nearly 6 percent in the third and fourth quarters of 2008. Massive increases in federal grants-in-aid in the first and second quarters of 2009 – nearly 29 percent and more than 63 percent respectively – prevented further declines in total receipts. In addition, enacted revenue increases have partly counteracted the effects of the recession on tax revenues; cumulative enacted state revenue increases between fiscal year 2008 and 2011 have totaled \$35.1 billion.[10] Two thirds of that increase occurred in the last fiscal year when states enacted \$23.9 billion in revenue increases. Since the middle of 2009, total receipts and tax receipts have exhibited fairly steady increases. This steady increase in

[9]http://data.bls.gov/pdq/SurveyOutputServlet

[10]National Association of State Budget Officers, ***Fiscal Survey of the States, Fall 2010,*** pages 54-55.



net incurrence of financial liabilities. The discrepancy between net lending or net borrowing derived in the capital (NIPA) accounts and the same concept derived in the financial account reflects differences in the sources of data, timing of recorded flows, and other statistical differences between the capital and financial accounts.[11] State and local governments, according to the financial account definition of net lending or net borrowing, have been net *lenders* in eight of the past forty quarters – the acquisition of financial assets exceeded the incurrence of liabilities (see Table 1).

state and local government tax revenues has brought state and local tax receipts in the fourth quarter of 2010 -- $1.35 trillion (seasonally adjusted at annual rates) back to the level of tax receipts in the second quarter of 2008.

B. *Financial Condition of State and Local Governments*

Perhaps the most common measure of any entity's financial condition is whether their receipts cover their expenditures. On a National Income and Products Account (NIPA) basis, state and local governments have been net borrowers in every quarter from 2001 until the fourth quarter of last year (see Figure 1). However, there have been periods in which current receipts have exceeded current expenditures – net saving on the part of state and local governments.

Table 1 presents two definitions of state and local government net borrowing: the NIPA definition, and the financial account definition of net lending or borrowing. The financial account definition is obtained from observing state and local government activity in credit markets. Net lending or borrowing can be defined as the difference between net acquisition of financial assets and the

In the trough of the most recent recession, state and local governments were borrowing at annual rates exceeding $150 billion. In contrast, in the third and fourth quarters of 2010, state and local governments were small net lenders -- $3.0 billion and $7.6 billion at annual rates respectively. Both accounts reflect improvement in state and local government financial condition from the trough of the recession.

Perhaps the most comprehensive picture of the financial condition of state and local governments is their net worth: the difference between total assets – financial and nonfinancial – and total liabilities. According to the U.S. Department of Commerce, Bureau of Economic Analysis, the net worth of state and local governments, excluding employee retirement funds, as of the end of the fourth quarter of 2010 was $8.0 trillion.[12] Total assets were $11.1 trillion -- $8.4 trillion in nonfinancial assets and $2.7 trillion in financial assets and $3.1 trillion in total liabilities (see Table 2). The net worth of state and local governments has increased in the thirty-

[11] http://www.bea.gov/national/nipaweb/Ni_FedBeaSna/DownSS2.asp?3Place=N
[12] ***Ibid.***

seven of the forty quarters between the first quarter of 2001 and the fourth quarter of 2010 – from $4.5 trillion to $8.0 trillion. State and local government net worth declined from $7.91 trillion in the first quarter of 2009 to $7.76 trillion in the fourth quarter of 2009 – a decrease of $150 billion. During this period, the value of nonfinancial assets declined by $134 billion.

III. Discussion of the Findings

In the introduction to this article, it would have seemed that state and local governments are facing imminent collapse. However, the findings in this article show that the fiscal health of state and local governments – measured by revenues and expenditures, net borrowing, and net worth show that (the fiscal condition of state and local governments) is stable; or, perhaps, improving slowly. These aspects of state and local government fiscal condition are not necessarily contradictory. In the immediate period, state and local governments face yawning budget gaps that must be filled. Beyond the immediate future, things may not be so bad. Revenues are rising, and expenditures have been cut so that current account deficits are declining. In addition, the net worth of state and local governments will continue to rise, ***if*** the values of financial assets continue to rise. Furthermore, estimates of the aggregate net worth of state and local governments are flawed because physical assets, which make up the bulk of state and local governments assets are substantially undervalued. Nonfinancial assets, for example, nonresidential structures, equipment, and computer software are valued at their replacement costs.[13] The market values of these assets are not available to provide a truer measure of net worth.

The Government Accountability Office (GAO), however, predicts a bleaker future for state and local government. Absent any policy changes – reductions in expenditures or increases in revenues – the GAO projects the deficits in the operating balances of state and local governments would reach 4 percent of GDP in 2060. The main driver of these ever increasing deficits facing state and local governments is health care costs.[14] Closing gaps of this magnitude would require substantial increases in revenues and reductions in expenditures for education, public safety, and other essential services. Meeting the financial needs of employee

Table 1
Financial Condition of State and Local Governments, 2001 1 to 2010 IV, Annual Rates
(Billions of Dollars)

	NIPA Capital Account						Financial Account		
Year and Quarter	Net saving (NIPA basis)	Plus: Consumption of fixed capital	Plus: Capital transfers received (net)[1]	Equals: Gross savings plus net capital transfers received	Less: Gross investment[2]	Equals: Net lending (+) or net borrowing (-)	Net acquisition of financial assets[3]	Net incurrence of liabilities[4]	Addendum: Net lending (+) or borrowing (-) financial account5
2006 I	62.6	156.8	56.4	275.8	302.1	-26.3	141.7	140.9	0.8
2006 II	63.2	161.2	57.3	281.7	316.4	-34.7	225.5	169.2	56.3
2006 III	42.4	164.2	59.2	265.8	319.8	-53.9	181.3	195.1	-13.9
2006 IV	35.9	168.7	56.7	261.3	323.7	-62.4	235.8	247.3	-11.5
2007 I	29.8	173.8	52.8	256.4	335.6	-79.1	206.8	272.7	-65.8
2007 II	29.8	177.0	59.6	266.4	340.5	-74.0	134.1	249.6	-115.5
2007 III	10.0	180.2	63.4	253.6	344.4	-90.9	192.5	199.9	-7.3
2007 IV	-20.7	183.6	59.9	222.8	351.1	-128.2	82.9	190.2	-107.3
2008 I	-29.3	187.0	59.1	216.8	355.3	-138.4	32.1	150.1	-118.0
2008 II	-33.6	190.2	60.9	217.5	363.6	-146.2	-49.5	76.7	-126.2
2008 III	-64.9	194.1	64.0	193.2	368.8	-175.6	-32.3	122.4	-154.7
2008 IV	-61.8	198.8	63.7	200.7	369.1	-168.3	-135.5	15.3	-150.8
2009 I	-41.6	201.3	56.7	216.4	366.4	-150.0	23.9	163.5	-139.6
2009 II	-33.6	201.1	61.8	229.3	368.8	-139.4	44.6	133.1	-88.5
2009 III	-19.2	200.5	75.6	256.9	366.1	-109.3	102.2	170.8	-68.6
2009 IV	13.9	200.8	75.3	290.0	355.9	-65.9	79.5	122.6	-43.1
2010 I	28.6	202.3	55.4	286.3	344.0	-57.7	132.8	172.1	-39.3
2010 II	15.8	204.2	63.2	283.2	351.5	-68.4	-43.8	4.6	-48.5
2010 III	47.7	206.1	73.5	327.3	361.3	-34.0	171.3	168.3	3.0
2010 IV	39.6	208.2	73.3	321.1	355.6	-34.5	238.1	230.5	7.6

[1]Net disaster related insurance benefits received, estate and gift tax receipts, and capital investment grants received from the federal government.
[2]Includes fixed investment plus acquisition of nonproduced, nonfinancial assets, for example, land and mineral rights,etc.
[3]Primarily securities other than shares. Includes currency and deposits, shares and other equities, loans, and other accounts receivable.
[4]Primarily securities other than municipal shares. Includes loans, and trade payables.
[5]The discrepancy between net lending or net borrowing derived in the capital account and the same concept derived in the financial account reflects differences in source data, timing of recorded flows, and other statistical differences between the capital and financial accounts.

Source: http://www.bea.gov/national/nipaweb/Ni_FedBeaSna/TableView.asp?SelectedTable=17 and; Board of Governors of the Federal Reserve System, Flow of Funds Accounts of the United States, 2005-2010, March 2010.

[13]Charlotte Ann Bond, Teran Martin, Susan Hume McIntosh, and Charles Ian Mead, "Integrated Macroeconomic Accounts of the United States," February 2007, p. 22; and, http://bea.gov//scb/pdf/2007/02%20February/0207_macro_accts.pdf
[14]U.S. Government Accountability Office, ''State and Local Governments' Fiscal Outlook,'' GAO-10-358 (Washington: U.S. Government Printing Office, 2010), available at http:// www.gao.gov/new.items/d10358.pdf.

retirement systems would require additional increases in revenues and reductions in public services.

IV. Summary and Conclusion

Despite a net worth conservatively valued in the trillions of dollars, state and local governments will face difficult days and possibly years ahead. The reason for this apparent contradiction is that current budget gaps must be closed immediately; but, the bulk of the nonfinancial assets that could be used to close the current budget gaps are not readily available. State and local government would find it extremely difficult to either liquidate these assets, even if the assets were valued correctly, or to generate revenue streams from these assets. To meet these challenges, states and localities are searching for new sources of revenue and provide those services that are valued by taxpayers more efficiently and cut those that are not so valued. In the words of the late Steven Gold, an eminent authority on state and local government finance:

> "A fiscal crisis is the ideal time for rethinking existing policies and undertaking new initiatives."[15]

Following Gold's advice, a number of states have established tax reform and/or performance review commissions to look for efficiency improvements. The fact that Gold's words were written sixteen years ago underscores the reality that these crises are recurring and the steps taken by state and local governments, while helpful, will not eliminate cyclical fiscal stress. *Plus ça change, plus c'est la même chose* – the more things change, the more they are the same.

Table 2
Components of Net Worth of State and Local Governments (Excluding Employee Retirement Systems)
End of Quarter Data from 2001 I To 2010 IV
(billions of dollars)

			Financial assets						Liabilities				Net worth (Total assets less total liabili-ties)
Year and quarter	Total assets	Non-financial assets[1]	Total financial assets	Currency and deposits	Securities other than shares[2]	Loans	Shares and other equity[3]	Other accounts receivable[4]	Total liabilities	Securities[5]	Short-tem loans	Trade payables	
2006 I	8,582.2	6,292.2	2,290.0	242.7	1,220.4	299.5	202.5	325.0	2,370.8	1,869.7	10.7	490.4	6,211.4
2006 II	8,859.3	6,511.7	2,347.5	244.9	1,251.8	306.8	207.4	336.7	2,421.3	1,911.4	10.9	499.0	6,438.0
2006 III	9,074.5	6,682.2	2,392.3	252.6	1,271.5	313.8	212.1	342.2	2,454.6	1,935.8	11.1	507.7	6,619.9
2006 IV	9,374.6	6,913.8	2,460.7	271.4	1,314.2	321.0	217.0	337.1	2,524.6	1,997.0	11.2	516.4	6,849.9
2007 I	9,673.0	7,157.3	2,515.7	269.2	1,353.2	325.5	220.1	347.8	2,591.2	2,054.3	11.4	525.4	7,081.8
2007 II	9,831.4	7,283.9	2,547.5	264.2	1,378.6	327.0	221.2	356.4	2,660.4	2,114.1	11.6	534.7	7,171.0
2007 III	9,987.3	7,412.8	2,574.6	273.7	1,339.0	331.4	224.9	405.5	2,694.0	2,138.3	11.8	544.0	7,293.3
2007 IV	10,145.6	7,555.0	2,590.6	303.1	1,335.0	334.0	227.3	391.2	2,752.7	2,187.4	11.9	553.5	7,392.9
2008 I	10,297.9	7,683.0	2,614.9	299.0	1,328.1	338.3	229.4	420.2	2,788.3	2,213.1	12.0	563.2	7,509.6
2008 II	10,400.5	7,796.7	2,603.8	294.7	1,306.9	338.3	231.9	432.0	2,813.2	2,227.8	12.2	573.2	7,587.3
2008 III	10,537.3	7,962.3	2,574.9	298.1	1,270.3	336.2	225.5	444.7	2,827.0	2,231.2	12.5	583.3	7,710.2
2008 IV	10,687.1	8,178.6	2,508.6	330.7	1,212.8	328.2	200.1	436.8	2,843.8	2,238.1	12.7	593.0	7,843.3
2009 I	10,790.0	8,286.1	2,503.9	338.8	1,225.7	328.9	175.5	435.0	2,882.8	2,267.4	12.9	602.5	7,907.2
2009 II	10,767.9	8,233.6	2,534.3	352.7	1,196.6	334.3	194.2	456.5	2,921.5	2,296.3	13.1	612.1	7,846.4
2009 III	10,723.7	8,153.5	2,570.2	344.2	1,180.2	341.9	219.4	484.5	2,947.3	2,312.2	13.2	621.8	7,776.5
2009 IV	10,750.8	8,152.3	2,598.5	360.8	1,172.6	346.3	242.4	476.4	2,991.4	2,346.4	13.5	631.4	7,759.5
2010 I	10,840.5	8,197.3	2,643.2	362.9	1,176.1	353.6	239.9	510.7	3,032.3	2,377.6	13.7	641.1	7,808.1
2010 II	10,877.5	8,259.3	2,618.2	346.9	1,159.3	350.7	225.3	536.1	3,038.0	2,373.4	13.8	650.8	7,839.5
2010 III	10,985.1	8,319.1	2,666.0	350.0	1,161.6	356.4	231.1	566.9	3,062.8	2,388.3	13.9	660.6	7,922.3
2010 IV	11,133.5	8,394.7	2,738.8	367.1	1,188.8	358.5	243.8	580.7	3,135.2	2,450.3	14.4	670.5	7,998.3

1. Excludes land and nonproduced nonfinancial assets.
2. Includes: Open market paper, Treasury securities, Agency and GSE-backed securities, municpal securities and foreign bonds.
3. Includes: Money market fund shares, corporate equities, and mutual fund shares.
4 Includes trade payables, taxes payable, and miscellaneous assets.
5 Municipal securities other than mutaul fund and money market shares.

Source: U.S. Department of Commerce, Bureau of Economic Analysis, Integrated Macroeconomic Accounts of the United States

[15] Steven D. Gold, "The Fiscal Agenda to the Year 2000," ***The Fiscal Crisis of the States: Lessons for the Future,*** Steven D. Gold, editor. Georgetown University Press, Washington DC, 1995, p.392.

Calendar of Events

44th Annual Conference and Committee Meetings

Whitefish, Montana
July 24-28, 2011

This year's conference sessions feature noted state tax speakers and experts Warren D. Townsend of Wal-Mart Stores, Inc., David Brunori of Tax Analysts & George Washington University, and Jeffrey A. Friedman of Sutherland Asbill & Brennan LLP, addressing issues of sales and use tax compliance. Also, professor J. Richard Harvey of Villanova University's School of Law and Graduate Tax Program will reprise his talk on the Internal Revenue Service's Uncertain Tax Positions disclosure requirements that he gave in Kansas City in March, this time along with Philip M. Tatarowicz of Ernst & Young LLP.

For further details of these and future meetings, please visit our website at *www.mtc.gov*.

MTC Offers Training for State Personnel

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Current Schedule

Computer Assisted Audit Techniques Using Excel and Basic Random Sampling
August 22-25, 2011
Albuquerque, NM (*tentative*)

Corporate Income Tax: Principles and Audit Techniques for Allocation and Apportionment
September 19-22, 2011
Madison, Wisconsin (*tentative*)

Nexus School
Fall 2011
Little Rock, Arkansas (*tentative*)

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