



# Comments on Your Government

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**RIPEC**

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## **Rhode Island at a Crossroads 2010 - 2011 Operating Program**

Rhode Island's economic and fiscal situation – high unemployment, falling revenues and a collapsing housing market – has had, and will continue to have, a significant impact on the State's ability to support government functions. Although economic recovery may be on the horizon, experience has told us that it will take the better part of a decade for the State to recover from the current fiscal crisis. Funds from the American Recovery and Reinvestment Act (ARRA) have provided temporary relief but are not a permanent solution to the problems the State faces. Ultimately, these funds may intensify the budgetary pressure when they run out unless steps are taken to structurally rebalance State and local budgets.

Rhode Island is at a crossroads. If we continue on our current path we will continue to cobble together budgets that are balanced only on paper and must be adjusted mid-year due to lower-than-expected revenues or spending overruns. We can continue ending fiscal years with deficits and we can find ourselves in even more dire fiscal straits in FY 2012 when the ARRA funding ends. Alternately, we can look to the ARRA funds as a temporary stop-gap measure that will provide the State and local governments with the needed breathing room to create comprehensive reform of our current system. We can enact reforms that will better position the State to attract investment and we can create an inclusive fiscal plan that will allow the State to rebound from the current crisis and weather future downturns.

These goals cannot be reached through a business-as-usual approach, nor can they be achieved through a single entity acting alone. These problems will not be solved through increases in taxes or rash cuts to services. However, these changes will require considerable political will, courage and determination to implement. Further, all levels and branches of government must work in concert; expecting one to solve the problems of the other will not solve the problems we face in this State. Rhode Islanders must work together to build a solid financial foundation upon which our ability to make key investments for the future will depend. Making these changes will require new tools and informed public input to help decision-makers focus on solutions and their relative costs and benefits.

Therefore, RIPEC has proposed a two-year operating program focused on areas in which State and local policymakers may affect the type of comprehensive change needed for the State to regain a solid fiscal base and grow its economy. The operating program is designed to be implemented over a two-year period and will provide the evidence-based research to policymakers, stakeholders, researchers, and the general public needed to make effective decisions regarding spending and taxation as we move toward the development of a structurally-balanced, investment-based, outcome-oriented budget.

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## **I. Addressing the Budget Structure**

The first and foremost issue facing Rhode Island is the financial capacity of State and local governments to support services in an era of dwindling resources and increasing demands. The current economic turmoil necessitates a different approach to the operation of government; a new set of policy choices need to be made regarding the structure and delivery of government services. State and local governments must be able to live within their currently limited resources while providing quality services efficiently and effectively. In order to address this fundamental issue, RIPEC proposes the following:

### **A. 2012 Budget - A Look Forward**

The FY 2012 budget year will mark a turning point for Rhode Island. ARRA funds will run out and the State will face a significant deficit in out-years if revenues have not recovered. In addition, FY 2012 will be the first year in office of a new governor. State and local governments must think ahead and work to achieve the necessary structural changes that will ease the challenges of this transition period.

Working with the Department of Administration, General Assembly finance personnel and others, RIPEC will begin to outline issues the State will face over the next several years by developing a potential FY 2012 budget as the guiding document. RIPEC will focus its attention on an analysis of the major components of the financial structure of State and local governments. This document will set the stage for discussions regarding what services government should provide and which level of government should provide these services.

In addition, RIPEC will focus on key public agenda issues that should be considered in the development of the FY 2012 State budget and will also address areas impacting local governments. Questions around major funding issues include:

- Is this program/activity mandated by State or federal law?
- If so, what is the level of service that is mandated and should the mandate be maintained?
- Are services being provided in the most cost-effective manner?
- Are department resources being duplicated within the State?
- Can the process or processes be improved or streamlined?
- Would a change result in cost-savings or cost-shifting?
- What is the long-term financial impact?
- How will change impact service delivery?
- What are the actual savings that will be gained in year one and out-years?

### **B. Rhode Island Budget in Context**

Annual RIPEC publications *How Rhode Island's State and Local Expenditures Compare* and *How Rhode Island State and Local Revenues Compare*, highlight expenditures and revenues in the Ocean State vis a vis other states in the country and the United States average, with a specific comparison to our neighbor states. These reports include a ten-year trend analysis and provide a context for Rhode Island's ability to support government spending with regard to available resources.

### **C. Budget Drivers**

In the FY 2010 Enacted Budget, “Grants and Benefits” accounted for 30 percent of general revenue expenditures, while “Aid to Local Governments” accounted for 33 percent of general revenue expenditures. While these two categories account for the majority of State spending, it is important to understand the underlying factors which drive these expenditures. RIPEC will work to identify the factors that drive State expenditures by:

- Forecasting and analyzing how recent demographic and economic changes influence the level of demand for various State and local government programs;
- Analyzing entitlement programs, providing reports on the progress of the Global Medicaid Waiver and using RIPEC’s recent Safety Net analysis to identify alternative delivery mechanisms and operational efficiencies, in order to develop a cohesive vision for the provision of basic services to those most in need;
- Examining the feasibility of changing the retirement system for future employees from a defined benefit to a defined contribution or hybrid plan and evaluating the viability of creating a personnel system that emphasizes performance and accountability in human resources decisions; and
- Assessing the impact of proposed health care reforms and the potential outcome of the national debate on health care which will impact both State and local government.

### **D. Tax Competitiveness**

RIPEC will continue to address the competitive nature of Rhode Island’s tax structure by evaluating how the State compares to others with regard to business taxes, estate taxes, property taxes, and capital gains. RIPEC will also follow-up with the work of the Strategic Tax Working Group recommendations proposed by the Governor. Additional non-tax revenue sources, such as charges and user fees, will also be examined. In addition, RIPEC will work with municipal officials, the Department of Revenue and others to develop legislation to establish property tax classification parameters and will advocate for keeping the current property tax reevaluation cycle intact.

This work will be supported through RIPEC’s semi-annual report on property taxes in the Ocean State which examines property tax burdens in the State’s 39 cities and towns and *How Rhode Island State and Local Revenues Compare* which highlights major revenue sources in comparison to the 49 other states and the national average.

### **E. An Investment-Based Approach**

In addition to focusing on the near-term difficulties Rhode Island is facing, there is a need to take a long-term view of the State’s finances and priorities. As such, it is important to examine the Ocean State’s economic development strategy, transportation system and other policy choices that will guide and determine future investments. To achieve these ends, RIPEC will:

- Work with the Administration and Legislature to comprehensively review the economic strategy of Rhode Island with particular emphasis on tax competitiveness, tax expenditures and economic indicators;
- Provide policymakers with an understanding of the current economic picture by undertaking an analysis of the current economic condition facing Rhode Island supported

by demographic data, identify historical trends in the State's economic sectors using national studies on competitiveness to guide analyses, and relate the current economic structure to a national forecast on the economic growth over the next several years;

- Update the 2002 RIPEC report *Rhode Island at the Crossroads*, which addressed the transportation system in Rhode Island; and
- Develop an analysis on the concept of asset maximization for Rhode Island and the many public assets of the State.

## **II. Rethinking Local Government**

Rhode Island has a population of over one million citizens who receive local government services from 39 municipalities, 36 school districts and a variety of special purpose districts. These units of local government are largely supported by property taxes. This organizational infrastructure may be a contributing factor to Rhode Island's continued high property tax burden, which is among the highest in the country. Budgetary pressures at the State level have led to the suspension of general revenue sharing, which may place additional fiscal stress on municipalities. This, in turn, will require either cuts to services or an increase in residents' already high property tax burden unless steps are taken to change the way services are provided at the local level.

RIPEC's *Rethinking Local Government Project* will focus on developing data and building coalitions aimed at local government cooperation and reorganization. Working with Senate Committees formed in the fall of 2009, RIPEC will help to identify potential cost-sharing opportunities for municipal and school governments and assess the economic, fiscal and programmatic benefits of consolidating local government functions.

In addition, RIPEC will continue to support Rhode Island's landmark property tax reform legislation, S-3050, by monitoring the efforts to implement property tax relief throughout the State and by evaluating systems to reconcile municipal and school budget disputes in Rhode Island and other states. RIPEC will also examine issues of local aid and intergovernmental relations between the State and municipalities.

Rethinking local government will require that cities, towns and school districts control the cost of providing health care and retirement benefits. RIPEC will update past pension and health care studies which provide an overview of the current level of benefits and provide recommendations as to how cities, towns and school districts may begin to control the cost of providing health care and retirement benefits.

## **III. Education Reform**

The provision of education is one of the most important roles of state and local government and has a profound impact on the overall fiscal health of the State. In recognition of the vital role of education, and the challenges the State's educational system faces, RIPEC will:

- Publish *Results: Education in Rhode Island* – a publication that examines education trends in the State, including student enrollment, school finance, and student performance relative to other states, and *How Rhode Island Schools Compare*, which compares

education expenditures, revenues, and salaries in Rhode Island to the rest of the country and to the United States average;

- Continue to work with the Governor’s panel on urban education to identify best practices and determine areas of improvement in the State’s urban centers;
- Focus on ways to reform public school finance, continuing to work on the establishment of a school funding formula, coupled with initiatives designed to hold schools accountable for results, enhance operating efficiencies, and allow for the effective implementation of the Property Tax Relief Act of 2006 (S-3050); and
- Review the recently adopted Basic Education Plan (BEP) and assist in the development of the fiscal note on the financial impact of the BEP, providing a detailed model of the cost of providing education in the State and how the State plans to assess the effectiveness of the BEP.

#### **IV. Public Education and Technical Assistance**

In addition to the program outlined in the preceding pages, RIPEC will continue to publish the following reports:

- State Budget Analyses – A series of reports on the Governor’s proposed budget, the results of the May and November revenue and caseload estimating conferences, and the budget as enacted by the General Assembly. These publications will highlight key points regarding revenues, expenditures, trends, out-year financial forecasts, and general state aid programs.
- How Rhode Island Compares – Annual publications that highlight the major taxes and expenditures in the State in comparison to the other states in the country and the United States average.
- Technical Assistance – RIPEC will continue to respond to requests from public officials to identify areas where sound practices can help control costs and improve operations.