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States Are Facing Big Fiscal Crises, Governors Report

By ROBERT PEAR

WASHINGTON, Nov. 25 — Plunging tax collections and soaring medical costs have created the worst fiscal problems for states since World War II, the National Governors Association said today.

"Nearly every state is in fiscal crisis," the governors said in a new report surveying the states.

The states' fiscal woes will force governors, many of them newly elected, to propose politically sensitive tax increases or drastic cuts in services.

Raymond C. Scheppach, executive director of the governors association, said states were increasing tuition at public colleges and universities, cutting Medicaid eligibility and benefits, increasing taxes on individuals and corporations and laying off state employees.

"You will see huge cuts in Medicaid" next year, beyond the cutbacks already enacted, Mr. Scheppach said.

Medicaid and other health costs like employee health benefits account for 30 percent of state spending and grew last year by 13 percent, the largest increase in a decade, the report said. At a time when revenues are declining, Mr. Scheppach said, such growth is unaffordable and unsustainable.

Governors and state budget officers said the fiscal condition of the states was more dire than the condition of the national economy. The recession has reduced state revenues, especially personal income and capital gains taxes, Mr. Scheppach said, but the states' fiscal problems are also linked to long-term trends, like the increase in health costs and the growing importance of services in the economy.

Relatively few of the newly elected governors have said precisely how they will deal with these fiscal problems. "Most of them don't understand how bad it is," Mr. Scheppach said.

In its "Fiscal Survey of States," the governors association found that the amount of money states had on hand at the end of the most recent fiscal year had fallen to $14.5 billion, from a peak of $48.8 billion in 2000. The current balance equaled 2.9 percent of state spending, the smallest cushion since 1992.

Total state tax collections fell by 6 percent last year and declined in every quarter, even as spending grew by 1.3 percent, Mr. Scheppach said.

These figures are consistent with data reported recently by the Rockefeller Institute of Government at the State University of New York, which found tax revenues down 6.3 percent in the fiscal year that ended June 30. Among states reporting the largest reductions were Alaska, Oregon, California, Massachusetts, Connecticut and New York.

In New York, the budget director for Gov. George E. Pataki, a Republican, told state agencies last week to cut spending by 5 percent in the remainder of the fiscal year, which ends on March 31. The budget director, Carole E. Stone, also said that cuts next year would be deeper than expected. The state is facing a deficit that legislators have estimated at $5 billion to $10 billion.

Oklahoma is experiencing the worst budget crisis in decades. Oklahoma State University, in Stillwater, was told to return money to the state, and its library has reduced its hours. The state finance director has instructed all state agencies to reduce spending by 6.5 percent.

Gov. Gray Davis of California, a Democrat, said last week that he would call a special session of the State Legislature to consider $5 billion of spending cuts and other emergency measures to "stanch the bleeding" in state finances. The governor told legislative leaders that the deficit in the coming year could exceed $21 billion.

Herb J. Wesson Jr., the Democratic speaker of the California Assembly, said, "This is a terrible crisis, and every Californian will be affected."

In Illinois, a Democrat will become governor for the first time in 26 years, and he will inherit a huge problem: a deficit that could grow to $2.5 billion, in a budget totaling $50 billion.

In his campaign, the governor-elect, Rod R. Blagojevich, said that Illinois could resolve its budget problems without an increase in sales or income taxes. But aides to Gov. George Ryan, a Republican, said that spending cuts made last spring were overwhelmingly unpopular, and that further cuts would be extraordinarily difficult.

To deal with a fiscal crisis in Arizona, the governor-elect, Janet Napolitano, a Democrat, wants agencies to cut spending by 10 percent across the board, making exceptions only for education, corrections and some children's services.

The University of Iowa increased tuition and fees this year by 18.5 percent, the biggest increase in more than two decades, after an increase of 9.9 percent in the prior year. The state Board of Regents is considering further increases for the next academic year.

Most of the tax changes made by states in the last year affected tobacco levies. Nineteen states increased cigarette taxes, many by more than 50 cents a pack, the governors' survey said.

Services account for a growing share of state economic activity, but states have found it difficult, for political reasons, to increase taxes on services. Likewise, Mr. Scheppach said, "it's very hard to raise taxes on middle-income Americans, when they don't have secure health insurance, to pay for health care for low-income Americans."

State tax collections came in far below the states' original estimates in the most recent fiscal year, which ended on June 30 for most states. Sales tax revenues, $147.6 billion, were 3.2 percent lower than expected, while personal income tax revenues ($187.7 billion) were down 12.8 percent and corporate income tax receipts ($21.6 billion) were down 21.5 percent.

In July, the United States Senate overwhelmingly approved a proposal to provide fiscal relief to states through a temporary increase in federal grants for Medicaid and social services, but it never became law. The Bush administration and Senator Don Nickles, the Oklahoma Republican in line to become chairman of the Budget Committee in the new Congress, opposed the increase.

Federal officials say they have no money to spare at a time when the federal government faces growing deficits, after four years of surpluses.

Mr. Scheppach cataloged some of the states' needs. After the Sept. 11 attacks, President Bush sought $3.5 billion to train and equip local police officers, firefighters and rescue workers, but Congress adjourned last week without providing the money.

Mayor Thomas M. Menino of Boston, president of the United States Conference of Mayors, said cities were spending $2.6 billion on new security measures without receiving any direct federal assistance.

With great fanfare, Congress passed legislation last month to clean up the nation's election procedures. But it provided none of the money promised to states to help them buy new election machinery and to train poll workers to comply with the law.

On Oct. 1, states lost $1.2 billion that had been appropriated by Congress to provide health coverage for low-income children. The money, unclaimed after four years, reverted to the Treasury, and Congress did nothing to restore it, despite pleas from states.