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Statement of Senator Charles E. Grassley
Senate Committee on Finance
Hearing on the Economic and Fiscal Condition of the States
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Rising oil prices, falling home prices, and declining job growth have led many observers to conclude the U.S. economy may dip into a recession this year. Although we often talk about our economy as a single unit, it is important to remember that economic conditions vary widely across the nation. For example, state unemployment rates vary from a low of 3.0% in Idaho, to a high of 7.6% in Michigan.

Just as economic conditions vary from state to state, so do state budgets. Some states have an income tax, but no sales tax, while other states have the reverse. Some states have integrated their income tax with the federal tax code, others have not. Some states have delegated much of their tax collection duties to their local governments, some have not.

According to the U.S. Census Bureau, total state and local revenue was \$2.5 trillion in Fiscal Year 2005, the latest year available. This total included \$438 billion in grants from the federal government. State taxes accounted for just 26 percent of total revenue. This amount ranged from a low of 16 percent in Alaska, to a high of 42 percent in Vermont (see Table 1).

Although most states have balanced budget requirements, these requirements are neither stringent nor binding. The states can and do run deficits. According to the Federal Reserve, total state and local debt outstanding in 2007 was \$2.2 trillion. That's up from \$1.1 trillion in 1997. It should also be noted that the federal government exempts the interest paid on state and local debt from federal income taxes. The Joint Committee on Taxation estimates this exemption is worth more than \$20 billion a year.

Congress has often responded with a package of fiscal relief during tough economic times. These packages have generally focused on broad-based tax relief for both consumers and businesses. When Congress enacted a state-aid package in early 2003, conditions were much different – state taxes had been declining and Medicaid costs had been rising at double digit rates. Today, revenue growth is positive and Medicaid growth is in single digits (see Chart 1).

Unfortunately, many states have responded to slower Medicaid growth by expanding their programs. For example, the Kaiser Commission on Medicaid and the Uninsured recently reported that thirty-two states have expanded access to their Medicaid and SCHIP programs between July 2006 and

January 2008.

The case for state-aid is harder to make in today's environment than in the past. But, today's hearing will allow us to examine these issues more closely in light of changing economic conditions.