



Highlights of GAO-10-899, a report to the Ranking Member, Committee on the Budget, House of Representatives

## STATE AND LOCAL GOVERNMENTS

### Fiscal Pressures Could Have Implications for Future Delivery of Intergovernmental Programs

#### Why GAO Did This Study

State and local governments work in partnership with the federal government to implement numerous intergovernmental programs. Fiscal pressures for state and local governments may exist when spending is expected to outpace revenues for the long term. GAO was asked to examine (1) the long-term fiscal pressures facing state and local governments and historical spending and revenue trends, (2) spending and revenue trends to identify patterns among states, and (3) what is known about the implications of these fiscal pressures for federal policies.

Using aggregate data from the Bureau of Economic Analysis's National Income and Product Accounts, this analysis draws on results from the March 2010 update to GAO's state and local government fiscal model. GAO's model uses historical data to simulate expenditures and revenues for the sector for the next 50 years. Data from the U.S. Census Bureau are used to analyze patterns of state and local government expenditures and revenues among the states from 1977 to 2007, the most recent 30-year period for which these data were available. A review of GAO and other reports synthesizes what is known about the implications of these long-term fiscal pressures for future federal policies.

GAO does not make recommendations in this report.

View GAO-10-899 or key components. For more information, contact Stanley J. Czerwinski, (202) 512-6806, [czerwinski@gao.gov](mailto:czerwinski@gao.gov).

#### What GAO Found

Understanding patterns in state and local government expenditures and revenues is crucial for identifying and analyzing potential future fiscal pressures for the sector. The March 2010 update to GAO's state and local fiscal model updates simulations that state and local governments' long-term fiscal position will steadily decline through 2060 absent policy changes. The primary driver of the fiscal pressure confronting the state and local sector is the continued growth in health-related costs. Over the last 30 years, health care spending has increased as a share of state and local spending, growing from 12 percent of overall state and local expenditures in 1978 to 20 percent in 2008. While the temporary infusion of funds from the American Recovery and Reinvestment Act of 2009 helped cushion near-term revenue shortfalls, states will continue to be fiscally stressed.

The rates of growth in expenditures and revenues varied among the states during the past 30 years, both overall and within specific categories. Current expenditures grew faster than own-source revenues in almost all states between 1977 and 2007. Average annual growth rates of state and local government expenditures and revenues varied substantially by category and among states. For example, public welfare (which includes Medicaid) was one of the fastest growing expenditure categories. In the aggregate, inflation-adjusted spending on public welfare grew at an average annual rate of 5.3 percent per year and growth rates in individual states ranged from 2.3 percent to 10.9 percent. The growth of intergovernmental revenue from the federal government (grants) also varied among the states. State and local current expenditures grew faster than federal grant revenues in more than half of the states. Despite these trends, the sector in the aggregate usually remained in surplus during this 30-year period. The sector avoided operating deficits, in part because of federal grant growth, and in part because, from 1995 to 2007, the sector increasingly financed capital purchases by issuing debt, rather than with revenues, which left more revenues available to pay for current expenditures. However, if the overall trend of state and local government expenditure growth in excess of revenue growth persists, this growth will put increasing pressure on state and local governments going forward.

All levels of government face long-term fiscal challenges which could affect future federal funding of intergovernmental programs, as well as the potential capacity of state and local governments to help fund and implement these programs. The interconnectedness which defines intergovernmental programs requires that officials at all levels of government remain aware of and ready to respond to fiscal pressures. These pressures have implications for a wide range of federal, state, and local programs, policies, and activities, and include costs associated with health care, physical infrastructure, state and local employee pensions and retiree health benefits, and education, among other areas. Actions to address the nation's long-term fiscal outlook will be needed at all government levels in coming years and the challenges cannot be adequately met by shifting burdens from one level of government to another.