ESSAY

"EATING YOUR SEED CORN": A NOTE ON NEW YORK STATE'S FISCAL POLICY FROM LIEUTENANT GOVERNOR RAVITCH

*Richard Ravitch**

I. INTRODUCTION

When I think of the state of New York's finances, I often think of the term in farming "eating your seed corn." Before a farmer sells or eats the corn he has harvested, he puts aside part of his crop as seed for next year's planting. If he consumed his whole crop instead, he would be "eating his seed corn"—getting by in the short run, gambling on an upturn in his fortunes, and risking his long-term chances of survival.

For the past decade New York State, through its budgeting practices, has been eating its seed corn by acting only with an eye to the short term. The state essentially spent down its reserves and set aside little for the future. Now, faced with revenue declines, the state is challenged to weather the hard times.

II. FISCAL OUTLOOK

Budget Gaps in the Coming Years

The state is currently in a fiscal crisis which is expected to continue over the next few years. There are projected budget deficits of $8 to $9 billion in 2010–2011 and $12 to $13 billion in 2011–2012.[1] State obligations are expected to rise faster than

* Richard Ravitch is the Lieutenant Governor of New York. Throughout his career he has served in a number of public leadership positions including the Chairman and CEO of the Metropolitan Transportation Authority, Chairman of the New York State Urban Development Corporation, and Co-Chair of the Millennial Housing Commission.

[1] The numbers are provided by the New York State Division of the Budget and the estimates calculated by the Office of the Lieutenant Governor. N.Y.S. Div. of the Budget,

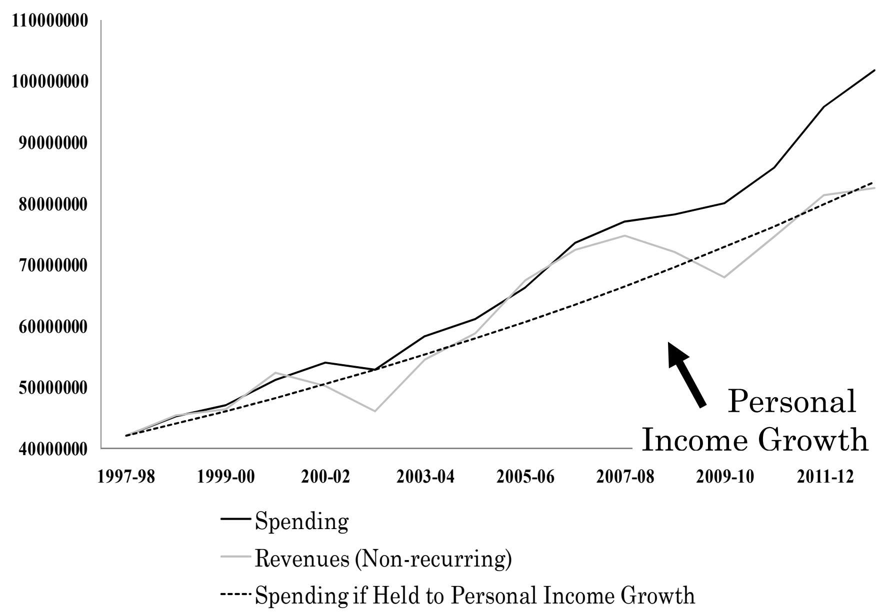
revenues. The deficits will grow even larger in the next few years. New York is not alone; many other states are facing large and growing deficits. According to the Center on Budget and Policy Priorities, the states have faced, and will face, combined budget shortfalls estimated at $375 billion in fiscal years 2010 and 2011.[2]

III. HISTORICAL CONTEXT: BUDGET HISTORY

A. Structural Imbalance

To understand how New York arrived at this point, with projected budget deficits of $8 to $9 billion in 2010–2011 and $12 to $13 billion in 2011–2012, it is important to look at the state's recent budget history. Over the past ten years, the state's spending has increased at a rate 20% faster than its revenue growth.

Figure 1: New York's Structural Imbalance



http://www.budget.state.ny.us (last visited Mar. 2, 2010).

[2] *See* ELIZABETH MCNICHOL & NICHOLAS JOHNSON, CTR. ON BUDGET AND POLICY PRIORITIES, RECESSION CONTINUES TO BATTER STATE BUDGETS; STATE RESPONSES COULD SLOW RECOVERY (2010).

The long-term gap between spending and recurring revenues is what budget specialists call "structural imbalance." This gap has widened in recessions and narrowed in good times. Figure 1 above illustrates the structural gap and shows how expenditures have outpaced revenues and have also grown faster than personal income growth.

Even in years of normal economic growth, the gap has been significant. Instead of limiting spending to normal income growth and building reserves in good times, the state has let spending rise in boom years—and stay at boom-year levels. Little has been set aside for the lean years that inevitably arise.

B. Non-recurring "One-shots"

To sustain spending that outpaces revenue growth, the state has used "one-shots," non-recurring actions—like borrowings, asset sales, the use of reserves, and accounting devices—which increase receipts or decrease expenditures temporarily, but do not change long-term revenue and expense patterns. Over the past decade the state has used at least $20 billion in one-shots to sustain its spending habits.

Some one-shots, like using reserves to fund spending in down years, are just good budget planning. Other one-shots are justified if they cover one-time expenses for important policy objectives or help to implement reforms whose savings will show up only in future years. But New York has often used one-shots to mask the structural deficits generated by spending trends that outpace reliable, recurring revenues.

One such one-shot was the $4.2 billion that the state received in 2003–2004 by issuing "tobacco bonds," which were financed by future payments owed to the state under a national settlement with tobacco companies.[3] This one-time injection of funds was not applied against a one-time expense or used to finance a reform that promised future savings. It merely propped up spending and pushed hard choices off into the future.

Some people say there is no harm in using one-shots to meet the current crisis. In this view, the state's troubles stem solely from the

[3] N.Y.S. DIV. OF THE BUDGET, 2003–2004 ENACTED BUDGET REPORT 9 (2003), *available at* http://www.budget.state.ny.us/pubs/archive/fy0304archive/enactedBudgetReport0304.pdf.

recession; if we cobble together enough temporary measures, we can last until the up cycle. Even if the country heads into an economic recovery, however, past experience shows that the state typically lags behind and cannot expect budget relief from revenue growth for at least another year or two. Also, more fundamentally, the current recession did not create the state's budget troubles; it merely exposed the state's structural imbalance.

IV. As We Face the Crisis: Concluding Thoughts

What Should Be Done to Resolve the Fiscal Crisis?

The state faces unprecedented fiscal challenges—a result of too many years of "eating the seed corn." Closing the state's structural gaps will be difficult and painful. And returning the state budget to structural balance will also take a number of years. The problem is of a scale and scope that it cannot be remedied in one year. It must be done over a period of years and in the context of a firm commitment to multi-year budgeting and new principles of fiscal accountability.

The state can rebalance its books and reposition itself for future growth and prosperity through adoption of a multi-year financial plan that provides a policy roadmap for returning the state to sound fiscal health. This will require an honest discussion about spending priorities and revenue needs. Undeniably, there is a tremendous amount of uncertainty in many of the variables inherent in such a multi-year plan (tax revenues, federal aid, and Medicaid and welfare enrollments)—variables that will almost never remain constant over four years or even one. Therefore, to operate effectively, the state must simultaneously bind itself to a budget process that is engineered to cope with uncertainty and adjust to changing conditions in a way that maintains stability, order, and the trust of the electorate. By embracing multi-year budgeting and a flexible framework for adjustments and rebalancing, the state will be in a better position to manage its finances and "store seeds" for the years to come.