Rhode Island's FY 2021 Enacted Budget and the Fiscal Challenges Ahead

RIPEC

Executive Summary
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In the fourth in a series of reports on the fiscal impact of the COVID-19 pandemic, RIPEC analyzes the so-called "skinny" FY 2021 state budget enacted mid-year by the General Assembly. The report focuses on how a shortfall in general revenues has been addressed using federal COVID relief funding, and how the enacted FY 2021 budget impacts the more challenging task of developing a balanced budget plan for FY 2022 and beyond.

Facing a massive shortfall in revenues and anticipating an additional federal relief package, the Assembly deferred action on a budget for FY 2021, which commenced on July 1, 2020, until December. While a federal relief package stalled, the budget picture brightened considerably. In September, the State Controller issued preliminary closing statements reporting a total positive swing of $187.9 million. Then, in November, estimated revenues and caseload expenditures for the FY 2021 budget were revised at the Revenue Estimating and Caseload Estimating Conferences for a net increase of $461.6 million over May estimates.

The pared-down, or skinny, budget enacted by the General Assembly for FY 2021 includes a large appropriation for federally funded COVID response costs but otherwise contains no significant policy or programmatic changes to current law. The enacted FY 2021 budget therefore maintains the status quo in large part, but importantly does not freeze taxes and expenditures at the levels appropriated in FY 2020. Rather, the enacted FY 2021 budget increases expenditures and reduces taxes consistent with current law. To pay for this expansion of financial commitments and produce a balanced budget for FY 2021, the General Assembly relied on over $400 million of one-time federal COVID relief funding to cover state general revenue expenditures.

The FY 2021 budget also includes a relatively large amount of borrowing connected with ballot initiatives to be presented to the voters on March 2, 2021. In her original FY 2021 budget submission in January 2020, the governor proposed three ballot initiatives totaling $268 million. In late July, she proposed a budget revision to nearly double the total amount of the ballot measures to $496.8 million. The General Assembly ultimately approved $400 million in borrowing for higher education, beaches and parks, housing, transportation, early childhood, cultural arts, and industrial facilities.

With respect to the outlook for FY 2022, Rhode Island's budget picture is complicated by large, atypical changes in funding sources connected with the COVID-19 pandemic in budgets enacted for the previous and current fiscal year. To determine whether the state has sufficient general revenues to pay for the cost of running state operations in FY 2022, RIPEC calculates that the adjusted level of recurring state general revenue expenditures incurred for FY 2021 is $4,572.9 million, more than $400 million greater than the actual general revenue expenditures of $4,153.2 million authorized in the FY 2021 budget. Employing an assumption that recurring general revenue expenditures will grow by three percent in FY 2022 and adding $30 million owed to the rainy day fund, expenditures for FY 2022 are projected to total $4,740.1 million. Since available general revenues are expected to be only $4,080.3 million for FY 2022, this leaves an initial projected deficit of $659.8 million. However, $146.1 million in FY 2021 general revenue expenditures appear to be covered through federal COVID funding under the $900 billion COVID relief legislation enacted by Congress in late December. Accounting for this positive adjustment reduces the projected deficit for FY 2022 to $513.7 million.

A projected deficit of $513.7 million, representing more than 10 percent of the budget, presents a very challenging situation for FY 2022. However, the availability of additional federal funding is likely to improve the deficit picture. The recent COVID relief package passed by Congress does not include broad relief for state and local government but does include funding to cover additional anticipated direct costs connected with the pandemic, as well as funding for a variety of state functions affected by the pandemic, including assistance for K-12 education, higher education, childcare, mental health, and transportation. There appears to be an opportunity to utilize some of this new federal funding to replace general revenue funding for ongoing state expenses in the FY 2022 budget. There also remains potential that the next Congress will pass legislation that provides additional relief to state and local government.

While the FY 2022 budget may become more manageable, there likely will remain a stubborn gap between the state's revenues and expenditures that eventually will need to be reconciled. In consequence, RIPEC recommends the following specific considerations for policymakers:

- While essential social services should be maintained, the state should act with more urgency to assess spending priorities.

- Given the eventual need to reconcile expenditures with available revenues, the state should consider structural changes in programs to make them more sustainable for the long term.

- With the availability of ballot initiatives and one-time federal funds, the state should expedite and target investments to support and accelerate economic recovery.

- Despite fiscal challenges, the state should remain vigilant to protect and advance the progress made in improving Rhode Island's business tax climate.