The Liberty Bullhorn

A Weekly Economic Newsletter by

Sven R Larson, Ph.D., Research Fellow with The Wyoming Liberty Group
http://larson4liberty.com; larson4liberty@gmail.com

February 11, 2011

ECONOMIC NEWS

The Unitary State of America

State dependency on U.S. government now at a critical breaking point

From a fiscal viewpoint 2011 may be the year when the United States ceases to function as a federation and effectively becomes a European-style unitary state.

This year, Federal Funds may on average become the single largest fund in state budgets, for the first time passing General Funds as the prime source of state spending. A total of 27 states have already passed that point, but on average Federal Funds are still a smidge smaller than General Funds spending in state budgets.[1]

In 2005 Federal Funds (known as Federal Aid to States on the federal side of the transaction) represented 29 cents of every dollar spent in the average state budget. Due to sharp increases in General Fund spending that share dropped to 26 cents by 2008. In 2009 and 2010, the ARRA "Stimulus Bill" expanded existing federally funded programs and added new ones, discussed in a recent Cato Institute memo.[2]

Consequently, in 2010 the federal government on average supplied 34.1 percent of state spending. General Funds represented 36 cents on average, down from 40.3 percent in 2005 and 42.8 percent in 2008.

The highest state dependency rates are in Oklahoma (50.6 percent of state spending) and Louisiana (50 percent). Ten states, Alabama, California, Idaho, Kentucky, Michigan, Mississippi, Pennsylvania, South Carolina, South Dakota and Tennessee, have dependency rates in the 40s.

By contrast, in 2005 Louisiana had a dependency rate of 45.2 percent, being the only state above 40.

There is also growing conformity among states. We can see this through the following operation. We rank the 50 states by Federal Funds dependency rate. We then divide the states into quintiles and calculate the average Federal Fund dependency for each quintile.

Continued on page 2

know your State

Tricky tracking of federal funds.

Studying federal funds to states requires multiple sources. The Census Bureau reports on the program from the federal government's perspective, while the National Bureau of State Budget Officers (NASBO) reports on the state side of the transactions.

This creates discrepancies. For example, according to the Census, in 2009 Massachusetts received $7.85bn in federal Medicaid funds. Yet NASBO reports zero federal Medicaid dollars for The Bay State.

One reason for this discrepancy is that Medicaid in the Census report includes SCHIP, which NASBO reports separately.

know your stats

Largest Federal Aid to States programs:

Medicaid	$256.12 billion
Federal Hwy Adm.	$39.79 billion
Low-Rent Housing	$28.00 billion

The result is as follows, comparing 2005 to 2010:

- For the highest quintile the average dependency on Federal Funds has grown from 36.4 cents per dollar spent in the state budget to 45 cents;
- For the lowest quintile the average dependency on Federal Funds has grown from 14.5 cents per dollar spent in the state budget to 21.4 cents;
- The dependency rate for the highest quintile has grown by 23 percent;
- The dependency rate for the lowest quintile has grown by 47 percent.

This somewhat technical analysis conveys a profound message. Every state has increased its dependency on Federal Funds, and low-dependency states have increased their dependency the most. In other words: there is growing fiscal consensus among states that dependency on the federal government is tolerable, even desirable.

Looking at actual dollar amounts, it is once again clear that the ARRA "Stimulus Bill" is the main culprit. From 2005 through 2008 the Federal Funds dollar amount in state budgets grew by, on average, 3.4 percent per year. From '08 to '09, Federal Funds increased by 20.3 percent in absolute dollars; in 2010 the growth was 23.7 percent.

These figures represent non-weighted averages. A study of Federal Aid to States in its aggregate form yields slightly different numbers as the non-weight average is then neutralized. However, the non-weighted average method brings us closer to reality in state budgets.

As for individual states, the ARRA "Stimulus Bill" affected some states more than others. The sharpest increase in the Federal Funds dependency rate took place in Delaware. From 2008 to 2010 the share of Federal Funds in the Delaware state budget increased from 12.3 cents of every dollar the state spent to 29.3 cents. This represents an increase in the dependency rate by 127 percent.

Wyoming is a close second with a 95 percent increase. Alaska, Colorado, Massachusetts, Nevada and New Jersey also saw their Federal Funds dependency rates increase by more than 50 percent.

The flow of money from the U.S. Treasury to state coffers funds welfare state hallmarks like tax-paid child care, tax-paid health insurance and a plethora of welfare programs. Federal Aid to States is the carrier wave of the American welfare state, which makes the FAS program one of the most ideologically charged in the federal budget.

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[1] National Association of State Budget Officers, State Expenditure Report: http://nasbo.org.

[2] Available at: http://www.cato.org/pubs/tbb/tbb_63.pdf.

LEGISLATIVE NOTES

Even though Congress has to pass a budget every year, very few of its spending programs are zero-based. Most of them are in place permanently, with more or less automated appropriations.

With annual adjustments come annual revisions to programs, which are patch-worked on top of existing descriptions of spending programs.

As for federal funds to states, a good source for program analysis is the Green Book, published by the House Ways and Means Committee. The latest available version is from 2004. It discusses fiscal aspects of Federal Aid to States programs but still requires considerable study time to become an effective tool for the interested reader.

Find the Ways and Means Green Book at:
http://www.gpoaccess.gov/wmprints/green/2004.html

Wyoming Liberty Group **is a 501(c)(3) educational and research organization**
Address: 1902 Thomes Avenue, Suite 201; Cheyenne, WY 82009.
Website: http://wyliberty.org
Phone/Fax: 307.632.7020/307.632.7024