Billion dollar shortfall? It's the truth
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When Governor Fletcher was elected, were we really 'facing a billion dollar deficit'?

He inherited a $303 million dollar budget shortfall in the first year. And just before his inauguration, the government published a projected shortfall of $710 million for the following year. Thus, within 60 days of his inauguration, the Governor was faced with a billion-dollar problem. He had to cover a $303 million deficit in the current fiscal year and the $710 million projected deficit in the first year of the next budget cycle.

I think most financial observers would agree that combining the projected shortfalls of the two fiscal years provides a reasonable shorthand measure of the state's financial condition at that time.

Others may disagree, but I have not heard any better way of quantifying the financial crisis which confronted Governor Fletcher's first 18 months. It would certainly be very misleading to say that the newly elected governor's only problem was to make it through the first year.

With hindsight, it is easy to say that the Kentucky economy just needed a little time before, as Governor Patton recently stated, it "took off like a rocket."

With hindsight, it is easy to say that the revenue forecasts behind the projected $710 million deficit were simply wrong.

With hindsight, it is easy to say that in the Fall of 2003, the government underestimated its own ability to work more efficiently.

But in December, 2003, Governor Fletcher staked his political career on those convictions and his own vision of a leaner, stronger state.

And no one denies that at the end of this period, Governor Fletcher had achieved a $214 million General Fund surplus, one of the largest in the state's history.

My purpose here is to outline the broader lesson of the state's move from deficits to surpluses, beginning with the fact that, unlike the federal government, our state is not permitted to engage in deficit financing.

When we speak of deficits or shortfalls, we are speaking of an insufficiency of funds to satisfy a particular benchmark of expenditure needs, whether enacted or proposed.

Just before Governor Fletcher's inauguration, in a report entitled "Kentucky's Fiscal Crisis" (still posted on the government's website), the Patton Administration calculated the government's General Fund expenditure needs for the next biennium (FY05 and FY06) at $16.018 billion.

This benchmark was pretty reasonable, and when measured against projected revenue, it anticipated the huge deficit which concerned so many editorial writers in November, 2003.

Having carefully based its calculation on 13 identified principles and assumptions, and having determined that "almost all the efficiency efforts in state government have been made," the report concluded that the only alternative to a "major reduction in the level of services" was a "major tax increase."

I do not question the sincerity of that calculation, but to Governor Fletcher, there were compelling needs not mentioned in his predecessor's list:

- the need to deliver higher value to Kentucky taxpayers, and
- the need to avoid long term injury to the state's economic recovery.

Having found the state's rainy day fund depleted by the previous administration, believing that revenues would continue to be tight and intending to fulfill his pledge of increasing efficiency, Governor Fletcher and the several managers he drew largely from the private sector, set out to find ways of getting more from less.

On the spending side, the record shows that by the end of FY04, Governor Fletcher made spending reductions of $214.3 million, many of which had a recurring benefit in the succeeding biennium. In FY05, he made further spending reductions, carrying forward $468.9 million into FY06.

How did he do it? The list is quite long, but three of the prominent methods were Medicaid reform, the self-funding of the state's health insurance plan and a reduction in government employment by 2,000 positions.

Reasonable people, including all 138 legislators, differ on the need to increase one government program or another, but no reasonable observer has noted a "major reduction in the level of services." Governor Fletcher has achieved a genuine and material improvement in the ratio of outputs to inputs, thereby giving each tax dollar higher impact.

What happened on the revenue side is even more interesting: Instead of a general tax increase, the Governor took 490,000 Kentuckians off the tax rolls, reversed the ITW decision and reduced the rates of individual and corporate income taxes to the benefit of the overwhelming majority of Kentuckians.

He aggressively advanced the state's economic development and a strategy of "showcasing" (World Equestrian Games, Louisville Arena, Ryder Cup). The result: the economy rebounded; employment rose and revenues increased dramatically, almost 10% each year.

Even without the funds carried forward from FY04, the undisputable fact is that General Fund receipts in the FY05-FY06 biennium ($16.021 billion) were $3 million higher—yes, *higher*—than the expenditure needs calculation on which the pre-inaugural call for higher taxes had been based.

By last spring, legislators realized that Governor Fletcher's two-part policy—cost control and economic growth—had produced a wide new stratum of discretionary funds available for deployment against the state's urgent needs, dramatically thickening the icing on the sometimes stagnant budgetary cake.

With the enthusiastic support of the General Assembly, Governor Fletcher used these enlarged resources to strengthen our education program, achieving a phenomenal 25% increase in P-12 education in a single gubernatorial term with a budget widely hailed as the best education budget since 1990—a budget which also confirmed that our university campuses would receive more new facilities in four years than in the previous eight.

Governor Fletcher *did* turn a $1 billion deficit into a surplus and sound fiscal management has been the strength of his first term.