MONITORING STATE AND LOCAL BUDGETS:

OR

DO YOU KNOW HOW MUCH MONEY IS IN YOUR PUBLIC PURSE?

I. WHY DO WE CARE?

AN IMPORTANT PROVIDER OF PUBLIC GOODS AND SERVICES

• Education, Safety, and Environment

AN IMPORTANT “HOLDER” OF HOUSEHOLD WEALTH

• Capitalization of Public Assets and Public Liabilities

• The Philadelphia Story

A POTENTIAL SOURCE OF FINANCIAL INSTABILITY

• Brazil, Argentina, and now Greece

• New York City, WPPSS, and Orange County
II. TODAY’S FISCAL PROBLEMS ARE NOT NEW

THE US HISTORY OF “DEFAULTS”

- The 1840 Defaults and the Emergence of Balanced Budget Rules
- The 1930's and the Great Depression
- New York City, Cleveland, Philadelphia, Bridgeport, Philadelphia (AGAIN!), Miami, Washington DC.

III. THE COMMON STRUCTURE OF DEFAULTS

DEFINING DEFAULT RISK

\[(\text{Principal} + \text{Interest}) > t_{\text{max}} \cdot Y + \text{AID} - (\text{Fixed Obligations})\]

or

\[
\frac{[(\text{Principal} + \text{Interest}) + (\text{Fixed Obligations}) - \text{AID}]}{t_{\text{max}}} = Y_{\text{CRITICAL}} > Y
\]

or

\[Y < Y_{\text{CRITICAL}}\]

Default Likelihood = Probability ( \(Y < Y_{\text{CRITICAL}}\))
IV. WHAT WE NEED TO KNOW TO SEE A DEFAULT COMING

**IS THERE A DEFAULT COMING?**

*The Default Condition:*

\[ t_{\text{max}} \cdot (Y < Y_{\text{CRITICAL}}) + \text{AID} - [(\text{Fixed Obligations}) + (\text{Principal} + \text{Interest})] < 0 \]

*Looks A Lot Like a Future Current Accounts Deficit*

\[ [\text{MAXIMAL REVENUES}] - [\text{REQUIRED EXPENDITURES}] = \text{DEFICIT} < 0 \]

*YES, IF UNDER THE “BEST OF CIRCUMSTANCES” THERE IS A DEFICIT*

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THE MONITORING PROJECT

A PILOT PROJECT: Philadelphia’s 1976 Budget

*ANITA VS. LENNOX*
V. THE MONITORING PROJECT

**DEFINING STATE AND LOCAL SURPLUS/DEFICIT:**

- SURPLUS/DEFICIT = \((DEFSURFG)\) = CURRENT REVENUES - CURRENT SPENDING

  \where:\n
- REVENUES = TAXES + FEES + AID + INTEREST EARNINGS + PROFITS
- SPENDING = WAGES/BENEFITS + TRANSFERS + INTEREST/PRINCIPAL + DEPRECIATION

**SO, HOW HAVE WE BEEN DOING?**

- Bohn/Inman (1996)
- Haughwout/Inman (20??)

  - Two short-cuts both biasing our results in direction of \(DEFSURGF > 0\).

  - \(p\ell = \text{Pensions Contributions} = (?) = \text{Normal Costs} + \text{Supplemental Costs} = \rho\ell\)

  - \(mK = \text{Maintenance Expenditure} = (?) = \text{Depreciation} = \delta K\)
Average DEFSURGF
Percentage of States with Negative DEFSURGF

Graph shows the percentage of states with negative DEFSURGF over the years from 1970 to 2005. The y-axis represents the percentage ranging from 0% to 100%. The x-axis represents the years from 1970 to 2005. The graph includes shaded areas indicating specific periods of time.
ABS(Standard Deviation of DEFSURGF / Mean of DEFSURGF)
Texas DEFSURGF

The graph shows the trend of Texas DEFSURGF from 1970 to 2005. The values range from approximately 500 to 0. The line indicates fluctuations over the years, with a significant drop around 1980 and a rebound towards the end of the period.
VI. WHAT DOES THE MONITORING PROJECT TELL US ABOUT OUR PUBLIC PURSE?

*FROM THE IDENTITY – “MONEY PAID = MONEY RECEIVED” – WE KNOW:*

SURPLUS/DEFICIT ≡ \{(p - \rho)\ell + [(m - \delta)(K_0 - A) + k] + [s - c] - d - \pi A\}

SUR ≡ [Add Pension Assets] + [Add Capital] + [Add Cash] + [Retire Debt] + [Buy Assets] > 0

DEF ≡ [Reduce Pension Assets] + [Deplete Capital] + [Cut Cash] + [Add Debt] + [Sell Assets] < 0

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THE “SAVING FLOWS” INTO (OR OUT OF) YOUR PUBLIC PURSE
CAPITAL GAINS AND LOSSES ON EXISTING ASSETS

\[ \Delta W_0 = [\Delta \text{PENSION UFL}] + [\Delta \text{MV ASSETS}] + [\Delta \text{MV CASH/SECURITIES}] + [\Delta \text{MV DEBT}] \]

THE “CAPITAL GAINS/LOSSES” ON CURRENT ASSETS AND LIABILITIES

TOGETHER WE HAVE THE VALUE OF YOUR PUBLIC PURSE

\[ W_1 = W_0 + [\text{SUR/DEF}] + [\Delta W_0] \]
## TABLE 1

**Average State and City Government Assets and Liabilities**

<table>
<thead>
<tr>
<th>Year</th>
<th>Savings</th>
<th>Tangible Assets</th>
<th>- Government Debt</th>
<th>- Unfunded Pension Liabilities</th>
<th>≡ Net Worth</th>
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<td>1972</td>
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</table>
How Much Money Is in a Philadelphian's Public Purse

Net Worth per Resident

Average State & City
PA & Philadelphia
Philadelphia
PA

Crisis
VII. DO WE REALLY NEED AN “OUTSIDE” MONITOR?

WHY WE NEED A “PUBLIC” MONITOR

- Budgetary information is complicated and expensive to assemble.
- Budgetary information is a public good

WHO SHOULD BE THAT MONITOR?

- Private Money: For Profit Rating Agencies? Non-Profit Research?
  - Charitable Funding: Local Foundations?
  - Federal Government? HUD?

FEDERAL RESERVE RESEARCH DEPARTMENTS
VIII. THE AGENDA OF THE S/L MONITORING PROJECT

🔹 KEEPING TRACK OF CONTEMPORANEOUS SURPLUS/DEFICITS & PUBLIC WEALTH

• SAMPLE: All States and Their Major Cities; Perhaps Every Two Years

• DATA: Build off of GASB Accounts; Consolidate All Funds

• METHODOLOGY: Common Methodology

▼

“The State of the States”

🔹 BUILD THE HISTORICAL RECORD

• SAMPLE: All States and Their Major Cities; Every Year

• DATA: Build off of Census Accounts

• METHODOLOGY: Common Methodology

▼

“The (Fed) Data Base on S/L Finances”
IX. THE PAYOFF: *STOP THE MISCHIEF*

“STATE OF THE STATES” to inform current policy debates.

• Information is Power
  
  • Lessons from Uganda
  
  • Lessons from Philadelphia

“DATA BASE ON S/L FINANCES” to inform best (and worst) practices.

• Rules that Work: No Carry BBR’s with Independent Courts
  
  • Executive Powers: Vetoes with Veto Coalitions
  
  • Bailouts and Bankruptcy

TOGETHER (Perhaps) WE CAN STOP THE MISCHIEF