



October 2013

National Economic Climate

Slow Economic Growth in 2013, Stronger Growth Expected Starting in 2014

The national gross domestic product [grew by 2.5 percent](#) in the second quarter of 2013, an uptick from the 1.1 percent growth in the first quarter of the year. The Congressional Budget Office (CBO) has [projected](#) that U.S. economic growth will continue to be slow for the balance of 2013 due to federal spending reductions and tax increases, but forecasted stronger economic performance in 2014. Similarly, the Federal Reserve's GDP projections from September 2013 [predict](#) GDP growth around 2 percent in 2013, with a 3 percent growth rate expected in 2014 and beyond. The U.S. economy may also be adversely affected by a [slower growth abroad](#), as the International Monetary Fund (IMF) lowered its forecast for global economic growth due to weaknesses in emerging markets. [Historically](#), the U.S. has witnessed an average GDP growth rate of 3.2 percent.

Repercussions of Congressionally-Manufactured Fiscal Crises

The recently-concluded political brinkmanship in Washington has resulted in (once again) avoiding an 11th hour first-ever default on the nation's debt. However, economic damage done by the 16-day government shutdown and threat of default is evident; Standard and Poor's estimated the [cost of the shutdown](#) on the economy at \$24 billion. And, the reprieve from the budget agreement will only be weeks long: to be exact—11 weeks through which the U.S. government is funded (Jan. 15), and 15 weeks before the debt ceiling is reached (Feb. 7). Consumers and businesses will likely hold back spending in the near term absent the likelihood of significant Congressionally-led reforms involving long term entitlement spending and tax policy that are requisite to engendering confidence in the U.S. economy. The continued uncertainty heading into the next set of government shutdown and default deadlines may well, in turn, negatively impact growth in state revenues.

Unemployment Rates Hold Steady with Downward Trend Forecasted

U.S. Bureau of Labor Statistics (BLS) data indicate that the U.S. [unemployment rate](#) stood at 7.3 percent in August, unchanged from the month prior. While still high, the unemployment rate is an improvement on the August rates of 9.5, 9.0, and 8.1 percent in 2010, 2011 and 2012, respectively. The Federal Reserve's national [unemployment forecast](#) for 2013 remains around 7.2 percent, with unemployment expected to drop to 6.4-6.8 percent in 2014. The [historical average](#) for the U.S. unemployment rate is 5.8 percent. *Nevada* had the highest unemployment rate among the states in August, at 9.5 percent, followed by *Illinois* and *Rhode Island*, at 9.2 and 9.1 percent, respectively. *North Dakota* again had the lowest jobless rate, at 3.0 percent.

State Economic Conditions

Tax Revenues Continue Steady Improvement

State general fund revenues witnessed strong growth in fiscal year 2013, based on the August 2013 [State Budget & Tax Actions preliminary report](#) compiled by the National Conference of State Legislatures (NCSL). Concurrently, state expenditures were generally on target. These two factors enabled many states to boost their reserves and provide supplemental expenditures, according to the analysis, leading to a solid fiscal situation in almost every state.

The NCSL report cautions, however, that the budget outlook for fiscal year 2014 is more tepid, with expectations that revenue growth will slow. Fiscal year 2014 expenditures are likely to outpace revenue projections, undermined by continued growth in Medicaid costs and the persistent aftereffects of the Great Recession.

States' cumulative year-end balances, consisting of general fund dollars and rainy day funds, climbed to 9.6 percent in fiscal year 2013, up from 8.2 percent the year prior, but are projected to decline to 5 percent by the end of fiscal year 2014 (the amount typically recommended by ratings agencies). It should be noted, however, that Alaska and Texas hold well over half of all state rainy day fund balances, thus skewing the national average. Omitting these two states from the calculation brings the change in aggregate year-end balances to 6.4 percent in fiscal year 2013.

Highlights from the *State Budget and Tax Actions Preliminary Report* National Conference of State Legislatures / August 2013

- State general fund revenues grew by 5.3 percent in fiscal year 2013 but a slowdown is expected in fiscal year 2014 with projected revenue growth of 1.3 percent.
- Fiscal year 2014 appropriations are budgeted to increase 3.9 percent, led by increases in Medicaid and higher education spending.
- Fiscal year 2013 year-end balances rose 23 percent above prior year levels, but are expected to decline 11.6 percent by the end of fiscal year 2014.
- As a result of the mismatch in state spending and revenue, state year-end balances (as a percentage of state spending) are projected to fall to 5 percent by the end of fiscal year 2014, down from 9.6 percent at the end of fiscal year 2013.
- Substantial changes in income tax, sales taxes and transportation funding mechanisms dominated 2013 legislative tax discussions.

Health Care, Pension, Other Costs Stack Up for State, Local Governments

Tax revenue increases have improved state budget outlooks, yet [structural fiscal challenges remain](#) for state governments. These include growing Medicaid expenditures and state retirement obligations. The U.S. Government Accountability Office (GAO) explained in its [April report](#):

“In the long term, the decline in the sector’s (state and local government) operating balance is primarily driven by the rising health-related costs of state and local expenditures on Medicaid and the cost of health care compensation for state and local government employees and retirees. Since most state and local governments are required to balance their operating budgets, the declining fiscal conditions shown in our simulations continue to suggest that the sector would need to make substantial policy changes to avoid growing fiscal imbalances in the future. That is, absent any intervention or policy changes, state and local governments would face an increasing gap between receipts and expenditures in the coming years” (p. 2).

The latest [Fiscal Survey of the States](#) from the National Governors Association (NGA) and the National Association of State Budget Officers (NASBO) found that states' budget pictures are slowly improving, yet spending pressures remain, as well as demands for state funds for programs that were cut during the recession. The NGA/NASBO fiscal analysis determined that governors' budget blueprints called for a moderate increase in spending in fiscal year 2014, with 42 governors presenting higher spending levels in the new fiscal year.

Sweeping Tax Reforms Called for by Some Governors, Legislators

Improving state budget conditions have spurred some governors and state legislators to propose broad-based changes in state tax structures, with some policymakers seeking deep reductions in state tax rates as one strategy intended to spur economic growth and job creation. Legislatures in 35 states have discussed changes in tax policy in the 2013 legislative session, with 16 debating revisions in state personal income taxes, based on a National Conference of State Legislature (NCSL) study cited in [Stateline.org](#).

A few examples of these proposals include:

- **Kansas:** Gov. Sam Brownback (R) [proposed](#) phasing out the state's income tax in early 2013 as part of a sweeping plan to lower state taxes. Brownback and the legislature reached an [agreement](#) in June to lower tax rates. Higher education funding was cut as a result, followed by increases in tuition to partially offset the reduction.
- **Louisiana:** Gov. Bobby Jindal (R) [called for](#) ending the state's income and corporate taxes and replacing the revenue sources with an enhanced sales tax, but has backed off the proposal.
- **Missouri:** The Republican-led Missouri legislature has passed a major tax reform package that would cut taxes by an estimated \$800 million. The plan has been vetoed by Gov. Jay Nixon (D). Republicans will seek an override vote this fall. Nixon has [called on](#) higher education leaders to oppose the tax cuts, fearing that it will leave a large budget gap and deep program cuts.
- **Nebraska:** Gov. Dave Heineman (R) called for ending the state's income tax in favor of an expanded sales tax in early 2013. His plan [failed](#) to acquire requisite support from state legislators.

In other states, plans have been introduced to increase taxes in order to make investments in state programs.

- **Massachusetts:** Gov. Deval Patrick (D) outlined an ambitious plan to significantly raise the state income tax while reducing the state sales tax. Patrick ultimately [signed a state budget](#) with a \$159 million funding increase for public higher education that allowed for a tuition freeze.
- **Minnesota:** Gov. Mark Dayton (D) and legislative leaders [passed a budget](#) that will increase state taxes by over \$2 billion over two years via an increase in tax rates on wealthy state residents, closing corporate tax loopholes and raising the tax rate on cigarettes. The governor signed a state budget that includes added funding for higher education and a tuition freeze.

A complete analysis of state tax proposals can be found on Stateline.org.

Fiscal Year 2014 State Higher Education Funding

Increases in state appropriations, steadying tuition rates mark major turnaround

Two years removed from the largest decline in state higher education funding in nearly a half century, state lawmakers have used increases in state revenues to begin reinvesting in public higher education. Based on the results of an informal survey conducted by AASCU of state operating support for public universities for fiscal year 2014 (which began July 1 in 46 states), 37 of the 49 states in which data was received reported year-over-year increases (see table). This compares to last fiscal year when only 30 states increased higher education funding, preceded by only 8 states in fiscal year 2012, according to similar preliminary prior estimates conducted by AASCU. The largest gains in state higher education funding support were reported in *New Hampshire* (28%), *Massachusetts* (16%) and *Washington* (12%).

Seven states cut operating support for public universities for this fiscal year. Topping the list were *Louisiana* (-17%), *West Virginia* (-9%) and *Wyoming* (-6%). This compares to 11 states last fiscal year and 31 states in fiscal year 2012. Five states provided flat funding this year, compared to nine last year.

There was considerable variation in year-to-year changes among the states this fiscal year—a 46 percent spread, driven largely by extremes in two states: New Hampshire's 28.6 percent increase and Louisiana's 17 percent cut. It should be noted that New Hampshire suffered a 48 percent cut in state higher education funding two years ago. Last fiscal year, there was a 25 percent spread between the states with the largest gain and steepest cut, and a remarkable 57 percent spread in fiscal year 2012. Overall, the collective average percent change in year-over-year state operating support for public universities heading into fiscal year 2014 was 3.5 percent. When excluding New Hampshire, the 49-state average reflects an increase of 2.9 percent. This compares to a 0.2 percent decline in overall state fiscal support for higher education between fiscal years 2012-2013 and a 4.7 percent decline between fiscal years 2011-2012, according to Illinois State University's [Grapevine compilation](#) of data on state fiscal support for higher education.

Approximate Year-Over-Year Percent Change in FY 2014 State Operating Support for Public Four-Year Universities			
	%		%
Alabama	1.8	Montana	8.7
Alaska	3.6	Nebraska	4
Arizona	4.1	Nevada	2.1
Arkansas	1.6	New Hampshire	28.6
California	5	New Jersey	0
Colorado	4.4	New Mexico	- - -
Connecticut	4.8	New York	0
Delaware	3.4	North Carolina	-4.5
Florida	11	North Dakota	10.7
Georgia	2.8	Ohio	2.3
Hawaii	1	Oklahoma	1
Idaho	3.8	Oregon	7
Illinois	0.2	Pennsylvania	0
Indiana	3.1	Rhode Island	6.4
Iowa	2.6	South Carolina	3
Kansas	-3.3	South Dakota	7.5
Kentucky	0	Tennessee	7.8
Louisiana	-17.6	Texas	6.2
Maine	0	Utah	7
Maryland	9	Vermont	3
Massachusetts	16.8	Virginia	3.3
Michigan	2	Washington	12
Minnesota	6.8	West Virginia	-8.9
Mississippi	5.3	Wisconsin	-2.9
Missouri	-1	Wyoming	-6
		<i>49-State State Average</i>	<i>+3.5%</i>
		<i>48-State State Average (Excluding New Hampshire)</i>	<i>+2.9%</i>

**Approximations; Original figures are as of July 11, 2013. North Carolina figure added Oct. 17, 2013. Data compiled by AASCU.*

Notes: North Dakota—the percent change increase reflects an increase from the state’s 2011-13 biennial budget to the 2013-15 biennial budget. Minnesota—percent figure reflects blended percent change for both the Minnesota State Colleges and Universities system and the University of Minnesota. Connecticut—percent figure is only representative of the Connecticut State University System. New Mexico—data was not received as of July 11.

Higher Education Policy Round-Up—States’ 2013 Legislative Sessions

Provided below is a brief overview of higher education state policy and programmatic initiatives stemming from states’ 2013 legislative sessions, as aligned with the topics from AASCU’s annual list of the [top 10 higher education state policy issues](#). For a more exhaustive list of higher education legislation in 2013, visit the [Education Commission of the States](#).

#1—Productivity (Boosting Institutional Performance via Incentivized State Funding)

A number of states have initiated efforts intended to boost institutional productivity, most notably through the use of performance-based higher education funding formulas. Modest growth in state budgets has spurred policymakers to attach performance requirements to higher education appropriations bills. Performance-based funding measures were

adopted this spring in many state budgets, including in *Minnesota, Montana* and *North Dakota*. *Florida* and *Mississippi* adopted performance-based funding through their state higher education governing board. *Arizona* earmarked \$5 million in performance-based funding for its three public universities. Performance-based funding measures were also discussed this year at the state or system level in *Louisiana, Missouri, Nevada, Texas* and *West Virginia*. According to collegeproductivity.org, 20 states now utilize some form of higher education performance-based funding. *Massachusetts* will use performance-based funding at the community college level.

#2—State Operating Support for Public Higher Education

Increases in state tax revenues have encouraged lawmakers to boost higher education funding in many states; for some it will mark the first time in years that public higher education will receive a funding increase. *California, Colorado*, and *Michigan* are among those which witnessed cuts to higher education in excess of 10 percent just two years ago and which this fiscal year will receive an increase in state investment.

While the economy is slowly improving and state higher education appropriations are likely to increase in a number of states in fiscal year 2014, years of state disinvestment have shifted the college cost burden to students and families. The latest State Higher Education Executive Officer (SHEEO) [State Higher Education Finance Report](#) indicates that state support per FTE student fell to \$5,906 in 2012, the lowest level in more than a quarter-century in inflation-adjusted terms. According to the report, in only two states did per-student appropriations increase from 2007-2012.

#3—Tuition Prices and Tuition Policy

Increased state revenues and subsequent funding increases for public colleges and universities have allowed a number of states to freeze tuition. Tuition freezes have been approved or are expected to be approved in *California, Iowa, Maine, Massachusetts, Minnesota, Montana, Nebraska, New Hampshire, Rhode Island, Washington* and *Wisconsin*. In *Florida*, Gov. Rick Scott (R) vetoed a 3 percent tuition increase and has urged the state's public universities to not raise tuition levels, with most state institutions approving modest tuition increases to keep pace with inflation. A few states, such as *Kentucky* and *North Dakota*, have set caps on tuition increases, while in other states modest tuition hikes have been approved. *Texas* lawmakers approved a "fixed for four" tuition option that will hold tuition rates constant for four years of a student's academic program. A similar bill died in the *Florida* legislature.

College Board [data](#) released in fall 2012 indicate that the average 4.8 percent increase in published prices of tuition and fees at public four-year colleges and universities for the 2012-13 academic year was the lowest increase since 2000-2001. Still, the report shows that average tuition and fee prices at public four-year colleges increased from \$5,213 in 2002-03 (in 2012 dollars) to \$8,655 in 2012-13, a 66 percent jump.

#4—State Student Grant Aid Programs

Lawmakers continued to make changes to their state student grant aid programs this year, with an eye toward providing incentives to spur college completion. *Arkansas* completed work this spring on legislation that will create a tiered scholarship starting at \$2,000 for freshman, increasing each year to \$5,000 for seniors. The state also created academic standards for students receiving state scholarships for their first year in school. Officials in *Colorado* have also encouraged institutions to adopt a tiered approach. *South Dakota* created a need-based state scholarship program. Lawmakers in *Iowa* have discontinued allowing public universities to utilize "tuition set-aside" programs that distribute a portion of student tuition revenues to low-income students. The state will now use general appropriations funds, similar to most states, to provide grant aid to low-income students. *Maryland* passed a state scholarship program for first generation students.

#5—College Readiness

Utah passed legislation that will require all high school juniors to take a college readiness test, such as the ACT. *Maryland* lawmakers completed work on the "College Readiness and Completion Act," which addressed issues such as dual enrollment, degree pathways, and caps on the number of credits required for an associate's or bachelor's degree.

#6—Immigration

Advocates for allowing undocumented students access to in-state tuition rates achieved a number of victories in the 2013 legislative sessions. Bills extending state resident tuition rates for undocumented students were signed into law in *Colorado, Minnesota* and *Oregon*. Similar legislation was introduced in a number of other states, including *New*

Jersey. The *University of Hawaii* Board of Regents extended in-state tuition rates to undocumented students, while the *Arizona Board of Regents* agreed to study the issue. *New York* was among a number of states that also debated whether to extend state student financial aid programs to undocumented students. And just this month, *New Jersey* Gov. Chris Christie changed his position and is now in support of that state’s version of the federal DREAM Act, known as the [Tuition Equality Act](#). According to the National Conference of State Legislatures, 16 states now have policies allowing undocumented students to be eligible for in-state tuition rates.

#7—Competency-Based and Online Education

State political leaders have continued to explore policies related to online and competency-based education programs. Governors in *Missouri* and *Tennessee* unveiled partnerships with Western Governors University (WGU). *Florida* lawmakers approved a measure that will allow the University of Florida to offer fully-online programs. *Nevada* higher education leaders have taken an interest in building out the state’s online higher education programming and created a working group to increase the number of online offerings. *Maryland* Gov. Martin O’Malley (D) called on state leaders to use technology to boost college graduation rates.

#8—Guns on Campus

A number of state legislatures debated the merits of bills related to guns on campus in the first half of 2013, with the vast majority of the bills seeking to loosen state laws or campus regulations related to guns. Among the states where legislation was introduced were *Arkansas*, *Georgia*, *Indiana*, *Kansas*, *Montana*, *Nevada*, *North Carolina*, *South Carolina*, *South Dakota*, *Texas* and *Wyoming*. A bill to re-instate a gun ban in *Colorado* failed to pass.

The most notable bill was in *Arkansas*, which now allows faculty and staff to carry guns on campus, however, campuses will retain the right to “opt-out” of the bill. Thus far, Arkansas campuses have exercised their right not to allow guns on campus. *Montana* Gov. Steve Bullock (D) vetoed a campus gun bill that reached his desk this spring. *Texas* will soon allow guns to be stored in locked cars on campus, but a broader gun measure did not pass.

#9—Economic and Workforce Development

According to an [analysis](#) of governors’ 2013 “State of the State” addresses conducted by AASCU, the connection between higher education and economic and workforce development was the leading higher education issue espoused by state chief executives, with several calling for legislation intended to tighten the link between higher education and workforce readiness. Other related proposals included state STEM initiatives, technology transfer, public-private partnerships and a focus on technical/vocational postsecondary education programs. Some notable initiatives include a plan in *New York* to create tax-free zones on unused campus lands. *New Mexico* passed a bill creating student loan repayment for teachers in “high-risk” schools, while *Idaho* repealed a student loan forgiveness program that aimed to keep teachers in the state. *South Dakota* created a scholarship program for students to teach in critically-needed teaching needs areas.

#10—Consumer Protection Involving For-Profit Colleges

State attorneys general have continued to pursue legal avenues to crack down on fraud and abuse in the for-profit college industry. California Watch, a non-partisan watchdog group, [identified 11 states](#) investigating for-profit colleges as of May 2013. Attorneys general in *California*, *Kentucky*, *Massachusetts* and *Minnesota* have been especially active in pursuing allegations of wrongdoing in the sector. *Wisconsin* embarked on an effort to better regulate the industry, but the panel was [disbanded](#) amid resistance from leading lawmakers and industry officials and questions related to the data used to develop benchmarks.

Other Notable Policy Issues

State Authorization

Measures related to authorization of institutions of higher education to operate in the state were passed in *Indiana* and *North Dakota*. *Tennessee* approved a bill that would provide state authorization exceptions to online education providers under certain circumstances.

Student Groups

A small number of states approved legislation that will allow student groups to discriminate in their membership selection, with a focus on political and religious groups. Bills were signed into law in *Idaho*, *Tennessee* and *Virginia*; and other states, including *North Carolina* and *Texas*, have discussed the issue.

Transparency

New Jersey lawmakers passed a bill that seeks to inform high school students about student loans by distributing information on monthly and annual loan repayments and the time it would take to repay a loan. *Connecticut* policymakers approved two transparency-related bills, one which will require higher education officials to appear before the legislature to discuss their budget, and other which will require regular reports on student-administrator ratios, administrator salaries and comparisons with peer institutions on specified metrics. *Illinois* passed a resolution creating a state-level college scorecard. *Maine* lawmakers passed a bill requiring a legislative report on first-generation students.

Veterans Education

Efforts to provide in-state tuition to veterans were successful in a number of state legislatures, including *Indiana*, *Missouri*, *Nevada* and *Oregon*. A few states also approved measures that will award prior learning credits for military training.

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