Obama warns US governors of “hard choices”

Tom Eley
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Barack Obama spoke to some 40 governors of US states on Tuesday, the second day of the annual conference of the National Governors Association at Philadelphia’s Independence Hall. The conference was dominated by the economic crisis, which has imposed significant budget deficits on most states. Yet in his brief remarks, the president-elect presented not a single concrete proposal and made only a few vague references to the social problems engulfing state governments.

Obama’s sharpest comments served as public notice that his administration will be a regime of fiscal austerity. “Make no mistake,” Obama warned, “these are difficult times, and we’re going to have to make hard choices in the months ahead about how to invest precious tax dollars and how to save them—hard choices like the ones you’re making right now. I won’t stand here and tell you that you’ll like all the decisions I make. You probably won’t.”

The “hard choices” being made by the governors are sharp cuts in social spending, such as assistance programs for the poor, funding for public education, and unemployment benefits.

The governors are requesting a portion of whatever stimulus package the new president signs into law after his inauguration. At the moment, the high-end figure being cited for the plan is $500 billion, although Congressional Democrats have hedged their bets by warning that any final legislation would be dependent upon Republican Party support, even though the latter saw its minority reduced further in November’s general election.

There is little chance that the Obama administration will deliver to the states anything approaching the governors’ full request of $160 billion, of which $120 billion would go toward funding infrastructure development and $40 billion to fund rising Medicaid costs. Whatever resources the Obama administration makes available will prove woefully inadequate to meet the unfolding social crisis. Furthermore, the figure will be a pittance compared to the sum allocated to bail out Wall Street by the Bush administration with the support of Obama and leading Congressional Democrats.

The states confront a cascading fiscal crisis. Including cuts already made in the current fiscal year, it is anticipated that the collective 2009-2010 budget deficit for US states will be a minimum of $140 billion. This figure could run higher than $200 billion by the middle of 2010, threatening infrastructure spending, unemployment benefits, public education at all levels, and social assistance programs such as Medicaid—the health insurance program for low-income people.

States have already collectively trimmed $53 billion from budgets for the 2008-2009 fiscal year, according to statistics gathered by the National Conference of State Legislatures. So far, for fiscal year 2010, 25 states anticipate around $60 billion in combined deficits.

Most states are prohibited from deficit spending, due to the enactment of reactionary “pay-as-you-go” laws over the past few decades—the legislative equivalent of the “no new tax” pledges crafted to benefit the rich. State budgets have been left particularly vulnerable to the economic crisis in part due to decades of shifting the tax burden onto working class families. This has resulted in state tax regimes in which financial resources are dependent upon regressive forms of taxation such as the “sales tax,” whereby a flat percentage fee is tied to most purchases, as well as other forms of consumption taxes. These sources of tax revenue are susceptible to cutbacks in consumer spending. The collapse of the housing market has also sharply cut into tax receipts based on property values and sales.

The economic crisis is hitting states from two sides. Due to layoffs, foreclosures and evictions, states face increased demand for the provision of social services.

Due to the same conditions, however, they have seen a steep decline in tax revenue. The problem is particularly severe for the provision of health care services through Medicaid, as more unemployed workers, having lost their privately funded insurance and medical benefits, turn to state programs. As a national average, the federal government contributes 57 percent of a state's Medicaid costs, while the state budget provides the rest. But when state funding is removed, so are federal matching funds, meaning that state cutbacks in Medicaid are effectively doubled.

An estimated forty-one states face budget shortfalls in the next two years. Leading the way is California, the nation's most populous state, and estimated to rank as the world's sixth largest economy. On Monday, Republican Governor Arnold Schwarzenegger declared a fiscal "state of emergency," convening the state legislature in special session in order to force new spending cuts. Publicly funded construction projects have now ground to a halt in California, throwing more people out of work. The state's total two-year budget deficit is $31.7 billion, of which $11.2 billion is a current revenue shortfall.

New York, the third most populous state, faces the second largest deficit—$6.4 billion for this year and next. New York has been hammered by mass layoffs in the financial sector, centered in New York City. Neighboring New Jersey has been similarly affected, with a shortfall is $2.9 billion. Florida, the fourth most populous state, is $5.1 billion short on its budget. The sixth most populous state, Illinois, Obama's home state, faces a deficit of nearly $2 billion.

The budget deficits are already devastating social programs and educational funding. The following are only a handful of examples reported over the last few days:

• New York Governor David Patterson, a Democrat, has demanded cuts of over 10 percent from most state agencies. Some have been unable to comply, such as the Department of Motor Vehicles, which stated that such large cuts would threaten its ability to generate income for the state. The Department of Transportation insists that it cannot realize the full cut, as winter snow removal would cease. The state police and prison system have been the only state agencies to be exempted from the 10.3 percent mandatory cuts.

• Florida has seen 100,000 people request food stamps in the last year, while about 1 million people applied for unemployment insurance in October alone.

• A Kentucky newspaper reports: "Out-of-work Kentuckians who want to contest their unemployment benefits before Christmas are out of luck: They may have to wait up to two months to get their appeals heard." The decision results in part from a rapid increase in the number of appeals.

As bleak as the situation with state budgets is now, it is likely that current predictions underestimate the crisis. At the same time, states are less prepared than at any moment in recent history to confront the social consequences of the economic crisis. After decades of cuts to social spending—including the Clinton-era "welfare reform," eviscerating assistance to the poor—state and local governments find themselves with few tools or resources.

Obama's appearance at the National Governors Association conference—and his appeal for state governors to prepare for the "hard choices" ahead—underscores that whatever the specifics of the incoming Democratic administration's stimulus plan, the full brunt of the economic crisis will be borne by working people and the poor across the US.