

## Federal Policies are Worsening State Budget Problems

Federal policies have a major and far-ranging impact on the fiscal situation of state government. In 2006, just under 40 percent of Oklahoma's state revenue was collected from taxes, while over 25 percent came directly from federal funding (Figure 1). Essential state services such as health care, social services, education, public safety and transportation all rely heavily on funding from the federal government. In addition, federal laws and regulations constrain choices made in the state by requiring or prohibiting certain state policies that can affect state tax revenues and expenditures.

With a state budget that provides flat funding for most agencies for the current fiscal year, federal funding has become even more important. Unfortunately, a whole set of federal policies are converging to worsen Oklahoma's budget problems. Examples of federal policies that are increasing the pressures on the state budget include:

- **UNFUNDED OR UNDERFUNDED FEDERAL MANDATES** — The federal government frequently enacts laws and regulations that impose binding responsibilities on state and local governments without adequate financial support to meet those obligations. No Child Left Behind, the Individuals with Disabilities Education Act (IDEA) and Real ID are among the most prominent and costly examples of underfunded federal mandates.
- **DECLINING MEDICAID CONTRIBUTIONS**— The federal government's share of Medicaid expenditures has been dropping in Oklahoma in recent years as a result of a falling federal matching rate, changes affecting Medicare-Medicaid "dual eligibles", and regulatory decisions. Over the last five years, the Oklahoma Legislature has had to supplement close to \$155 million in additional state appropriations to make up for lost federal funds.
- **CUTS TO FEDERAL GRANT PROGRAMS AND FUNDING STREAMS**— Federal grants constitute a vital funding source supporting the operation of core programs for many state agencies. In recent years, federal grant funding has remained largely frozen. Over the five-year period from FFY '02 – FFY '07, federal funding for the 60 largest discretionary federal grants decreased by an average annual rate of -3.16 percent in real (inflation-adjusted) dollars.
- **FEDERAL POLICIES THAT RESTRICT STATE TAXING CAPACITIES** — On the revenue side, federal policies have also affected the state's fiscal situation by depriving Oklahoma of tax revenues it could otherwise collect. A notable example is the Internet Tax Freedom Act, which bars states from taxing the access fees that people pay for their Internet service. Congress has also failed to pass legislation that would give states the option to tax remote sales as a way to promote tax equity between Internet sellers and brick-and-mortar vendors.

As a growing number of states face budget problems associated with the national economic slowdown, federal policies will assume heightened importance. While no one should expect the federal government to solve all the state's budget troubles, we can encourage the elected officials we send to Washington to display greater concern for the impact that their policy choices have on state budget situations and to promote policies that reflect a cooperative partnership between our various levels of government.

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