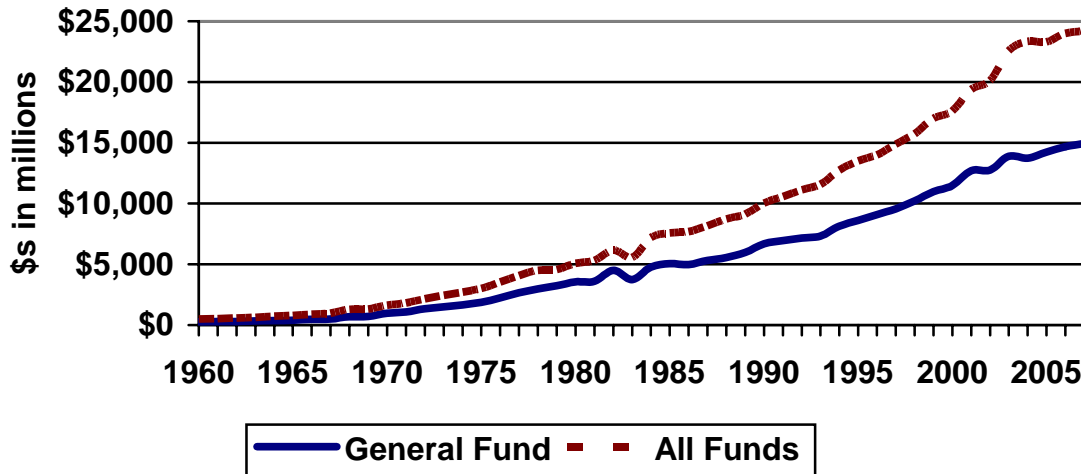


STATE BUDGET BACKGROUND

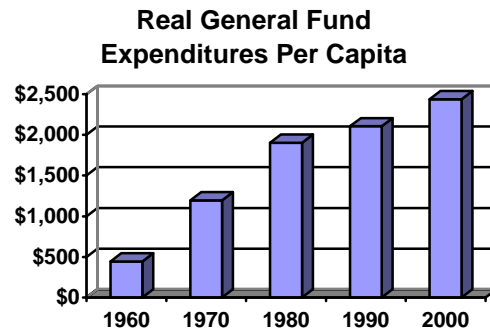
Budget history. In 1960, total general fund expenditures were approximately \$250 million. General fund expenditures are expected to be \$16.4 billion in 2008 and \$16.8 billion in 2009. General fund spending grew at an annual average rate of 14.6 percent during the 1960s, 13.7 percent during the 1970s, 6.5 percent during the 1980s, and 5.5 percent during the 1990s.

State Government Expenditures



General fund expenditures per capita and per \$1,000 of personal income. General Fund spending per capita also has risen significantly. In 1960, per-capita general fund expenditures were \$73. That amount increased to \$2,333 in 2000. After adjusting for inflation, general fund expenditures per capita still demonstrated significant growth. The graph on the right shows that expenditures per capita expressed in 2002 dollars increased from \$444 in 1960 to \$1,196 in 1970 to \$1,902 in 1980. In 1990, real general fund spending per capita rose to \$2,105 and it was \$2,437 in 2000.

On a per \$1,000 of income basis, general fund spending grew substantially from 1960 to 1980 and has declined slightly since then. In 1960, general fund expenditures represented 3.4 percent of state personal income. That percentage grew to 6.3 percent in 1970 and to 8.4 percent in 1980. General fund spending fell to 7.6 percent of personal income in 1990 and to 7.2 percent in 2000. This does not mean general fund spending declined in actual dollars during the 1980s and 1990s. Personal income grew by 277 percent during this period while general fund spending grew by 223 percent.

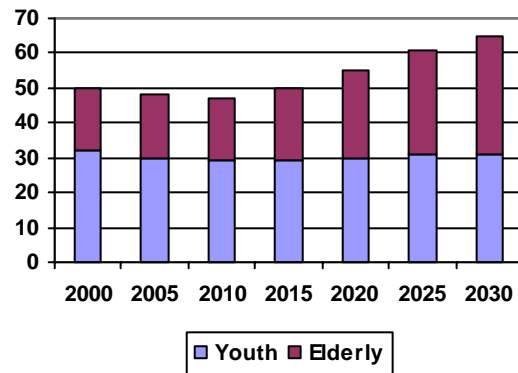


Demographics. The State Demographic Center calculates the total dependency ratio. This statistic combines the youth dependency ratio – the number of people from birth to age 14 per 100 people between the ages of 15 and 64 (working age people) – with the elderly dependency ratio – the number of people 65 years of age and older per 100 people of working age. These ratios compare how many individuals are in their high government service usage years to the number of working age people. In 2000, Minnesota’s total dependency ratio was 50 – youth dependency ratio of 32 plus an elderly dependency ratio of 18. The total dependency ratio declines slightly until 2010 and then steadily increases to 65 in 2030. In 2030, each 100 people of working age will have to support 15 more people in

their high government service usage years than 100 working age people did in 2000. The growth in the dependency ratio comes from the projected change in Minnesota's elderly population. In 2000, there were 18 people age 65 and older per every 100 people of working age; however, in 2030, there are expected to be 34 elderly people per 100 working age individuals.

Spending reform. In 2003, the business community proposed several spending reform proposals to address many cost drivers of the state budget. Four principles guided the spending reform initiatives: (1) target resources to those in need; (2) finance individuals rather than institutions; (3) utilize competition; (4) reduce overhead expenses.

Total Dependency Ratio



- **Target resources to those in need.** To the extent possible, government programs should be means tested to target subsidies to those with lower incomes and wealth. For example, the current long-term care system provides an incentive for individuals with the means to provide for their own care to hide assets and take advantage of the state's medical assistance program. This is no longer affordable.
- **Finance individuals rather than institutions.** Whenever possible, government should direct subsidies to individuals rather than institutions because it is the most efficient way to ensure subsidies go to those in need. For example, student aid for higher education could increase while state aid to the University of Minnesota and the Minnesota State College and University system decreases. Such a change would protect lower-income students and their families from tuition increases and eliminate a portion of the higher education subsidy that more wealthy students and families currently receive.
- **Utilize competition.** Competitive sourcing aligns institutional self-interest with the public interest for low-cost, quality services. Public employees and nongovernmental organizations, including for-profit businesses, should be allowed to compete for government service contracts. For example, state payroll services, local government highway construction, and K-12 food service and transportation could be put out for competitive bids. In addition, government can use reverse auctions to reduce the cost of purchasing many goods and services.
- **Reduce overhead expenses.** The public expects government to deliver the same level of service even though revenue is not growing as fast as it did. To do so, government will have to address overhead expenses. Reductions in government personnel levels, compensation and benefits are justified given the stagnation of private-sector wages that recently occurred and the wage and benefit differential between many public employees and their private-sector counterparts. Government also should seek ways to cut its energy and other occupancy expenses (i.e. rent, janitorial service) as well as its costs for various supplies. For example, group purchasing arrangements with other government units could reduce purchasing costs while negotiating long-term contracts with utilities or installing on-site generating equipment could lead to energy savings.

During the 2003 session, the Legislature enacted several spending reforms that reflected these principles. First, the state implemented reverse auctions for the purchase of a variety of goods. Second, state aid for local governments was reduced and the LGA formula was reformed so it distributed resources based on need. Third, the Department of Human Services agreed to seek a federal waiver to change the look-back period for determining assets and income eligible for medical assistance estate recovery. Fourth, the Pawlenty administration negotiated an increase in the employee contribution for family health insurance coverage.