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Those of us who lived in the Commonwealth in the late 1980s vividly recall the "Massachusetts Miracle," a spectacular economic boom that -- swiftly and painfully -- went bust. As difficult as the ensuing deep recession was for individuals and businesses, the situation was even worse for state government. In the euphoria of the exceptional economic times, the state had made significant new commitments that depended upon an unsustainable pace of annual revenue growth. When the boom collapsed, Massachusetts was left with a huge deficit that had to be filled by massive borrowing, and the state’s bond rating plummeted to the bottom of the 50 states. Repairs the fiscal damage took the better part of the 1990s.

Is it really possible only a decade after the state's fiscal debacle that we will again commit to more than we can afford, and then see the fiscal stability we have achieved begin to unravel? A series of forces -- including new spending pressures, slower economic expansion, and major tax cutting ballot questions -- are combining to create uncertainty about the state's financial future. Unless we make the right choices in the coming months, both our hard-won fiscal flexibility and our ability to undertake critically important investments will be put into jeopardy.

In the face of these uncertainties, the Massachusetts Taxpayers Foundation recently advanced two major proposals to protect the extraordinary record of fiscal progress over the past decade while strengthening the state's long-term competitiveness. In response to the announcement of massive cost overruns, the Foundation proposed a $2.5 billion plan to finance both the Central Artery and other transportation infrastructure projects around the state that are essential to our growing economy. Most of the key elements of this plan were incorporated in the transportation financing proposal recently enacted by the Legislature and submitted to federal officials.

At the same time, MTF has put forth a plan to tie reductions in the income tax rate to 5 percent to growth in the state's economy, an alternative to the Governor's ballot initiative cutting the rate to 5 percent over a fixed three-year timetable. MTF's approach -- which has been endorsed by the House -- would bring our high personal income tax down to a more competitive level, while providing an important fiscal contingency against an economic slowdown and ensuring that the state will be able to meet capital and other pressing needs.
The major factors putting Massachusetts at risk include the following:

C Although the state's debt burden is the third highest in the country, we face a huge array of new infrastructure investments -- ranging from the Central Artery and university facilities to environmental cleanups and seaports -- that are critical to our economic future. The recent revelations of major Big Dig cost overruns and the long list of investment needs that are not addressed in current capital plans underscore the enormous capital financing challenge that lies ahead.

C Although the Massachusetts economy is still growing, the peak of our economic game for this cycle is likely behind us. The rate of employment growth has been slowly sagging for the last several years, and personal income gains barely exceeded the national average last year. With our very low population growth and a high cost of living, the state's labor scarcities, particularly in key knowledge-intensive industries, are almost certain to intensify, acting as a brake on future economic growth and, ultimately, on the state's tax revenues.

C Over the last four years, the state's underlying tax revenue base has grown ten percent a year on average in a period of six percent personal income growth. Where did the extra four percent per year come from? The answer lies to a large degree in nonrecurring gains from a euphoric run-up of stock values and a resulting surge in taxable consumer spending. While this has been good for the Commonwealth's tax revenues, it also leaves the state vulnerable given the current volatility of the financial markets. Even a slowdown in the meteoric rate of market growth -- much less a major decline in stock values -- will have a significant impact on tax revenues. To complicate the revenue picture further, over $500 million of previously adopted tax cuts must still be phased in over the next several years.

C Concurrently, the state is facing spending pressures on a scale that goes well beyond the requirements of the last decade, with a surge of largely unavoidable cost increases in the former "budget busters" and an appetite for new spending that ignores the changing fiscal outlook. In particular, the state budget is heavily exposed to increased health care costs, including an expensive new prescription drug program for seniors that is included in both the House and Senate budgets. At the same time, the state needs to sustain its financial commitment to education, one of the bedrocks of our future economic success. Overall state spending is now growing at almost three times the rate of inflation with larger percentage increases each year, a pattern that is not sustainable over the long term.

C Further complicating this picture, two questions headed for the November ballot would in combination reduce annual state revenues by about $1.8 billion. The proposal to lower the 5.85 percent income tax rate to 5 percent over three years would shrink revenues by over $1 billion annually when fully implemented. Massachusetts has one of the highest personal income tax burdens in the nation, and reducing the rate is an important step to improve the long-term competitiveness of the Massachusetts economy. In light of the other pressures on the state budget, however, cutting the income tax over a fixed three-year schedule will make it difficult for the state to keep its commitments if economic growth falters. The proposal to provide an income tax credit for tolls and auto excise taxes is an especially bad idea. It would shift the burden of fair and reasonable user fees onto the taxpayers at large and would reduce revenues by more than $600 million per year at a time when the state needs to put more, not fewer, resources into capital investments.
While this picture is daunting, our prospects are far from bleak. The Governor and Legislature have, by and large, sustained a bipartisan effort to manage the budget prudently, and their fiscal discipline has paid off well. The state’s substantial rainy day fund will help stabilize the budget in the event of a recession and the Massachusetts economy is much more diversified than it was ten years ago.

To avoid dissipating our fiscal stability, however, we will have to make realistic choices, in particular about how to pay for our capital needs and how to address further tax cuts. Though the recently approved Artery finance plan successfully resolves the Commonwealth’s most immediate crisis and offers relief from the squeeze on other road and bridge projects around the state, the larger issue of financing important capital priorities must still be addressed.

The two major revenue reducing petitions headed for the November ballot represent an even greater fiscal challenge. The state clearly cannot accommodate the almost $2 billion combined annual revenue impact of these two proposals over the next three years, a fact underscored by the Governor's decision not to support the tolls/auto excise credit because it was unaffordable. While MTF favors cutting the income tax to 5 percent, the Foundation's plan is a preferable alternative to the ballot proposal backed by Governor Cellucci given the many uncertainties about future revenue growth and the other pressures on the budget. Tying the pace of cuts to economic growth would achieve the goal of the proposed initiative while allowing the state to address its spending needs and protect fiscal progress.

Over the last ten years, the Commonwealth has demonstrated that it can make the right choices. If we are to preserve our hard-won fiscal strength and the ability to make key investments for the future, our choices in the coming months must be equally prudent. The adverse consequences of our fiscal misadventures of the late 1980s should not be forgotten -- it would be a travesty to make the same mistakes again.

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