

# The PARCA Quarterly

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PUBLIC AFFAIRS RESEARCH COUNCIL OF ALABAMA



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## In this issue...

Public Opinion and the State Budget Shortfall .....	page 1
Proration in 2009 .....	page 4
Proration Budget Cuts in the Alabama Community College System .....	page 5
Responding to Proration: The University of North Alabama Experience .....	page 6
About the Contributors.....	page 7

### PUBLIC OPINION AND THE STATE BUDGET SHORTFALL

By Randolph Horn

With a shortfall in the current state budget and the prospect of reduced revenue in the coming year, PARCA surveyed Alabamians to assess the public response to the current budget dilemma. The poll addressed several areas: 1) public priorities concerning major areas of government service provision; 2) attitudes concerning two state financial processes – earmarking and proration; 3) public assessments of the impact of large budget cuts on state services; and 4) public willingness to pay increased taxes to avoid cuts in state services. A scientific sample of 494 respondents was collected between January 6th and 22nd through random-digit dialing of Alabama households and cell phone users. The margin of error for the total sample is  $\pm 4.4\%$ . Some questions were asked of a subsample of 360 respondents. The subsample has a margin of error of  $\pm 5.2\%$ .

#### I. Public priorities

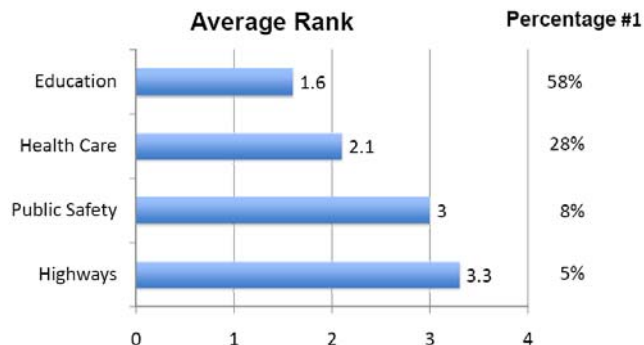
Respondents were asked a series of questions related to their priorities for state legislative action this year and their assessments of state government performance. When asked what was the most important issue for the legislature to address this year, over a third gave responses related to jobs and the economy. One-fifth identified education, and nearly 10% identified the budget shortfall or proration. There was little variation across demographic groups, although those with higher levels of education were more likely to list education as a priority, while those with less education were more likely to identify jobs and the economy. Those with higher income levels were slightly more likely to identify the budget shortfall or proration as the most important issue.

Four major areas of government investment were identified for respondents in random order: education, health care, highways, and public safety. Respondents were asked to identify one of these areas as the most important service the state provides and to rank the remaining areas. Nearly three-fifths identified education as the most important area of government service. Just over a quarter listed healthcare, and fewer than ten percent identified both public safety and highways. While a majority of every identifiable demographic group and region of the state listed education as the most important area of service, those with more education were more likely to rank education number one. Women and older respondents were slightly more likely than others to list health care as the most important service. While only a small proportion of respondents identified highways as important, whites and males were more likely to rank it higher than others.

**Figure 1** shows the percentage of #1 rankings and average rank for each of the four functions, with 1 being the highest rank and 4 the lowest.

**Figure 1**

#### Funding Priorities for State Government



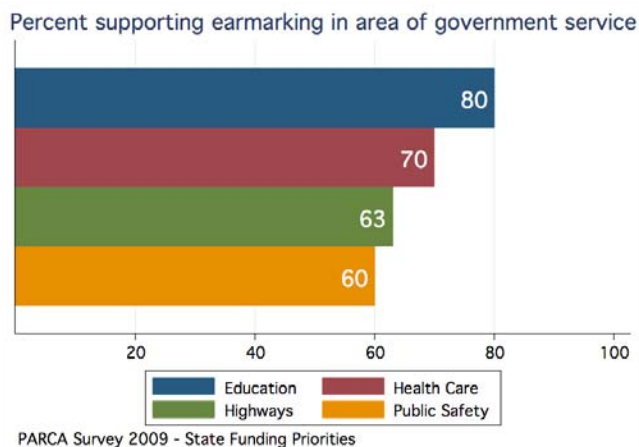
Source: PARCA Survey 2009 – State Funding Priorities.

A subsample of survey respondents was asked if they could name an agency of state government that was doing a good job. Just over half named a specific agency. We grouped the responses into the four major areas of government expenditure explored in the survey. Nearly one-fifth of the responses named an agency related to public safety, while about one-seventh named an agency related to education. Health care, highways, DHR, and the Agriculture Department were each mentioned by about seven percent of respondents. Asked how they knew about that program, over half mentioned first-hand contact with the agency, while about 16% had learned about the agency from a friend or relative. Nearly three-quarters of information about successful state agencies came through personal contacts while less than a quarter identified media reports as their source of information.

**II. Attitudes about state budgeting processes.**

Respondents were told about the dedicated revenue streams for education and highways. They were then asked if it was a good idea or a bad idea to earmark taxes to fund a particular area of government service. Nearly two-thirds identified earmarking as a good idea. Those with higher levels of education were more likely to say that earmarking was a good idea. Respondents were evenly divided when asked if it was okay for some government services to be earmarked while others were not, with about two-fifths saying that it was okay and about two-fifths saying it was not okay. White respondents and those with higher levels of education were slightly more likely to say that it was okay for some programs to be earmarked while others were not.

**Figure 2**



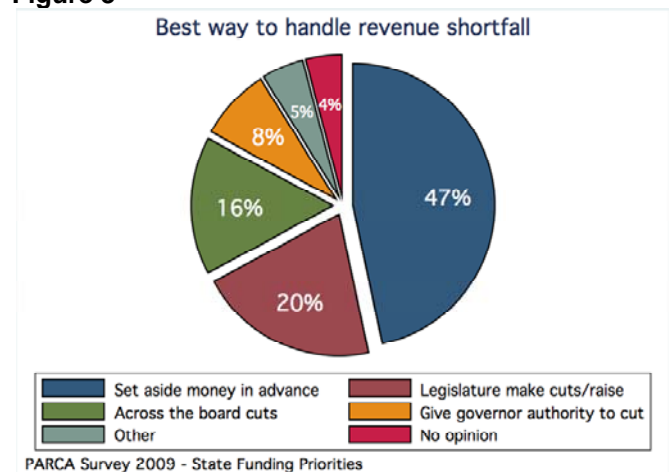
Respondents were asked if revenues should be earmarked in each of the four main areas of government investment. **Figure 2** shows the response. An overwhelming majority, about four-fifths, indicated that revenues should be earmarked for

education. While this function received a supermajority in every demographic group and region of the state, women were slightly more supportive of earmarking revenue for education than were men.

Just over two-thirds thought revenue should be earmarked for healthcare, with women indicating slightly more support than men. Nearly two-thirds thought revenue should be earmarked for highways. About three-fifths said that revenue should be earmarked for public safety, with women being slightly more supportive of earmarking than men. Across all four categories and all demographics groups support for earmarking was widespread among Alabamians.

Respondents were also asked about strategies for dealing with budget shortfalls. Respondents were informed that state law requires across-the-board cuts when revenue falls short during a budget year. They were asked if this was a good way to keep the budget in balance, or if the budget should be balanced in some other way. A majority preferred to balance the budget another way; less than forty percent indicated that across-the-board cuts were a good way to balance the budget. Older respondents were more likely to support proration than others. Even though proration is required by law, respondents were asked what they thought would be the best way to address revenue shortfalls. Nearly half indicated support for setting aside money in advance to address shortfalls, with a fifth advocating having the legislature reconvene to address a budget crisis. Only about 16% supported across-the-board cuts when other options were available. **Figure 3** shows these results.

**Figure 3**



**III. Impact of revenue shortfalls**

Respondents were briefed on the current state of the budget and prospects for the coming year, and asked to assess the impact of budget cuts on state programs. The shortfall was described in this way:

“The economy today is the worst in many years. At the start of this year, the education budget was 5% below

the year before. However, actual revenues won't cover the budget, so proration has begun. By the end of next year, education spending may be 15% or more below where it was last year. Analysts say that a 15% cut would represent a large cut in any organization's budget. Similarly, spending in the general fund also may drop substantially without outside help."

Respondents were then presented with recent achievements or challenges confronting state agencies and asked if large budget cuts would hurt a lot, some, a little, or not at all. In general, respondents indicated that budget cuts would affect the quality of service. Large majorities (from 65-80%) indicated that cuts in every program would hurt some or a lot.

**A. Education** – Respondents were asked if large cuts would hurt the progress being made in public schools on reading and math test scores. Nearly two-thirds said that cuts would hurt a lot. The impact of cuts on college affordability was seen as serious, although less dramatic. After being informed that tuition at colleges and universities was above the regional average, a majority indicated that large cuts in state funding would hurt college affordability a lot. The impact of cuts on job training programs was seen as less serious still. Respondents were informed of the Alabama's top-ten ranking in economic development success and asked if cuts in job-related education programs would hurt economic development. Just under half indicated that it would hurt a lot.

**B. Healthcare** – Respondents were informed of state involvement in two areas of health care provision, namely that three-fourths of nursing home care and nearly half of inpatient childbirths are paid for by state health programs. Nearly two-thirds said that cuts would hurt a lot.

**C. Highway Maintenance** – Respondents were informed of a challenge confronting the Transportation Department, namely that 24% of highway bridges fail to meet federal safety standards or are rated structurally unsound. A majority indicated that cuts in state funding would hurt highway maintenance a lot.

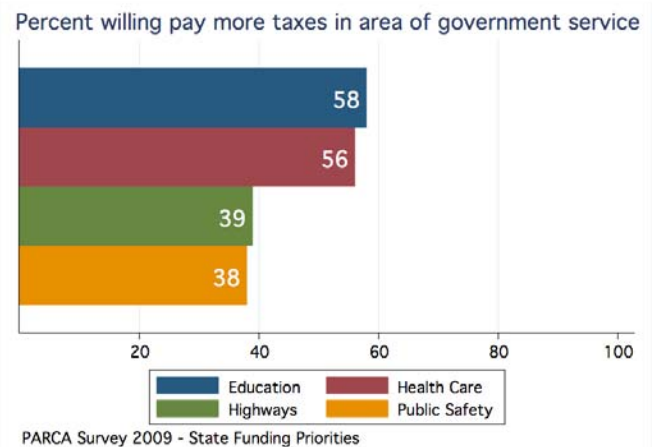
**D. Public Safety** – Respondents were informed that public safety officials have reduced the number of highway deaths and asked if a large cut in funding would hurt public safety services. About two-fifths indicated that a large cut would hurt public safety services a lot. Women were more likely than men to indicate that a cut would hurt a lot.

#### IV. Willingness to pay increased taxes to avoid cuts in services

Respondents were asked if they would be willing to pay more in state taxes to avoid substantial cuts in each of the major areas of government service. Nearly

three-fifths of respondents indicated a willingness to pay more in state taxes to avoid cuts in education. Majorities in all demographic groups showed their support for education, although younger respondents tended to be more willing to pay taxes for education than older respondents. A majority of respondents were willing to pay increased state taxes to avoid substantial cuts in health care. African-American respondents were slightly more supportive in this area than others. Majorities were opposed to paying more taxes for either public safety or highways, with no significant variation across any demographic group or region of the state. **Figure 4** shows these results.

**Figure 4**



#### Conclusion

The 2009 PARCA survey reveals much about public priorities and expectations with regard to the budgeting process of the State of Alabama. The public endorses earmarking to dedicate revenue streams to important programs. Those who see earmarking as overused or overly restrictive confront a considerable challenge in bringing the public around to their position. Proration is less favorably viewed. Most Alabamians would prefer alternative methods for addressing revenue shortfalls.

While majorities support earmarking revenue in each of the major areas of government service addressed in this survey, there are significant differences in how the services are valued. Education is not only ranked number one, but more people express willingness to pay additional taxes to support it. That is not to say that support is uniform for all things educational: there are some differences in public assessments of the impact of large cuts in different education programs. While health care ranks number two in the list of priorities, it mirrors education in terms of the public's desire to protect its revenue stream and willingness to pay additional taxes to avoid substantial cuts. Alabamians evince support for public safety and highways, with majorities supporting earmarking and large minorities indicating willingness to pay additional taxes to avoid cuts in these areas. Even though

recognized as important, public safety and highways are seen as second-tier priorities behind education and health care.

Note: Complete question text and survey results may be found at <http://parca.samford.edu/presentations> .

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## PRORATION AND K-12 SCHOOL SYSTEMS IN ALABAMA

By Jodi Newton

### What is Proration?

Proration is a technique used to avoid shortfalls in budgeting for Alabama public schools, as well as all other state-funded agencies and institutions. It occurs when the revenue in a given fiscal year is insufficient to meet the budgets that were passed into law by the Legislature. When this happens, the Governor declares proration and a percentage reduction is applied to all recipients of state funds. The monthly allotments to K-12 schools and other agencies are cut, or prorated, by that percentage.

### From Budget to K-12 Monthly Allocation

School systems in Alabama earn their state funding primarily from Foundation Program funds. A school system's annual allocation is based on formulas that take into account enrollment and other factors such as the teachers, textbooks, and classroom supplies necessary to the instructional program. For example, through these formulas a school system may earn \$14 million from the state's foundation program. The budget comes with requirements for expenditure of a significant portion of that \$14 million, especially in the number of teachers to be hired, their salary, and benefits. The school system's "fair share" contribution from local funds is equal to the value of 10 mills of property tax in that system. If our school system's local ten mills equal \$2 million, then the state will provide the remaining \$12 million to fund its foundation budget of \$14 million. Any local funds above the 10-mill requirement are raised and spent at local discretion. So with the expectation of receiving \$12 million from the state for the fiscal year, our hypothetical school system begins to get monthly allocations of \$1 million per month in October, when the budget goes into effect.

### What happens to the money when proration is called?

If the school system is expecting \$1 million per month, and proration is called with a resulting rate of 9%, the monthly allocation is cut to an average of \$910,000 per month for the 12 months. The actual amount sent to the school system is reduced by more than the \$90,000 to make up for the months when the system received the full allocation. So the actual reduction in

the monthly allocations depends on when proration is declared.

For example, if the proration were called two months into a fiscal year, the effect of the reduction on the monthly allocation goes from 9% to 10.8% and the cut goes from \$90,000 to \$108,000 per month for the remaining ten months. The earlier proration is announced, the less certain forecasters are of the amount of the shortfall in revenue for the entire year, but facing the reality of proration early can be helpful for weathering the cuts.

### "Rainy Day" Funding

To the legislature's credit, in recent years it has passed legislation to create a mechanism to set aside reserve funds to cover revenue shortfalls. Also, the people of Alabama passed a constitutional amendment in November 2008 to enhance the funding available for "rainy days." The total amount in rainy funds available is approximately \$437 million for the education budget. Once these funds are used, they must be repaid before the state can borrow again from the rainy day account.

### Proration Declared for FY2009

In December 2008 the Governor declared proration of 12.5 % for the education budget and released \$218 million, about half, of the rainy day funds available, lowering the effective rate of proration to 9%. Since the declaration came two months into the fiscal year, the remaining payments to school systems will have to be reduced by 10.8% to achieve the planned reduction by the end of the fiscal year.

### Why proration?

It is easy to simply accept the years of proration in Alabama schools and the subsequent budget cuts as inevitable. After all, proration of the education budget has occurred nine times in the last thirty years. In part this is due to Alabama's tax structure and the allocation of economically sensitive income and sales taxes for education.

However, the economic cycle is to some extent predictable, and proration has a decidedly negative impact on our public schools. The creation of budget reserves and rainy day funds are helpful steps, but recent state budgets have relied on significant fund balances and estimates of revenue growth that did not pan out. As a result, the 2009 education budget was \$333 million smaller than the 2008 budget from the beginning. Thus, even prior to proration being called, schools were already operating with fewer funds than in the prior year.

### Proration – What's a School to Do?

So what do local K-12 school leaders do as proration is thrown into their collective laps? Virtually all schools make cuts to programs, personnel, and services for students. School systems use accumulated fund balances, the same fund balances

that are considered essential for stability and cash flow operations.

First, they try to avoid cutting classroom essentials. This means they try to reduce operating expenses such as supplies, utilities, professional development and travel, technology, software, and even maintenance. But two-thirds of a school system's core educational expenditures, omitting food and transportation, go to instruction, and most of this is allocated for teacher compensation. One simplistic solution is to make cuts in central administration, but the reality is that this is only 5% of total educational spending. A second is to reduce building operation and maintenance costs, which unfortunately are only 11% of total educational spending. These two areas account for only 16% of the typical Alabama school system's educational spending, including personnel in these areas. Our hypothetical school system, faced with cutting 10.8% of spending in each of the last ten months of the fiscal year, would find it impossible to keep schools open and make all of the required cuts in these two areas alone.

### **The Classroom and the School**

In times of proration, most administrators try to minimize the classroom impact by cutting other areas first. However, many school teachers will face classes without the materials necessary to sustain and enhance learning. Programs that provide academic support for students, such as interventions and tutorials, may be eliminated or diminished during proration. Technology support and printing may be one of the first areas cut, and teachers either do without or dip into their own pockets. Extracurricular activities are often cut, and students have fewer opportunities to use their talents and special abilities, along with fewer scholarships.

### **Can Jobs or Salaries Be Cut?**

In years of proration, teacher jobs cannot be cut midyear and salaries cannot be prorated. Teachers work under annual contracts, and salaries are paid based on a salary schedule. Support personnel include all non-certified positions, such as teacher aides, bus drivers, secretaries, child nutrition workers, custodians, and bookkeepers. Support personnel earn continuing service status after three years, much like teachers earn tenure. In some cases, support positions may be cut midyear—or more likely not filled midyear should a vacancy occur, but these opportunities are limited.

The reality is that the budget items one can cut are restricted drastically, partly because so much of the total budget is in salary and benefits for personnel. A local school district's payroll may well be as high as 80% or more of the total budget. Let's consider a scenario of the hypothetical school district that has 79% of budget in personnel and a rate of proration of 10.8% for ten months. In having 79% of budget in

payroll, that school system has only 21% left from which to cut 10.8%. That computes to cutting just over 50% of all non-salary items. Some of the major non-salary expenditures, such as insurance and utilities, are impossible to cut by 50% in most cases. Local school systems, their superintendents, and school boards find themselves in extremely difficult positions, having to turn to local funds and fund balances.

### **Local Funds**

The more a school system relies on state funding, the harder the system is hit by proration. Local funds above the required 10 mill property tax may help offset the effects of proration. If the local funds are in property taxes, additional stability is theirs, since property taxes typically provide consistent annual funding. Many school systems rely on local sales tax and may see local revenues diminished. Occasionally during tough economic times, a local government will take away a school system's sales tax or direct allocation. These school systems are hit doubly hard, and often find themselves with nowhere to turn.

### **Fund Balances**

Almost every school system will have to use some portion of fund balances to complete the FY '09 budget year. The larger a school system's fund balance, the better it will be able to weather proration. Building fund balances, while trying to give students a strong education, is tough work for every school system. Rebuilding those fund balances will mean providing less for schools and students for years.

Proration is more harmful than just the losses from the immediate budget cuts. Proration will make it more difficult to recruit and retain excellent teachers, impair a school's ability to deliver what is best for students, and limit student learning opportunities. When a school system is forced to make budget cuts, shortchanging students and teachers, it takes years to recover.

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## **PRORATION BUDGET CUTS IN THE ALABAMA COMMUNITY COLLEGE SYSTEM**

**by PARCA Staff**

Chancellor Bradley Byrne's plan for coping with the necessity of budget-cutting in the Alabama Community College System centers around two main priorities:

- Preserve the core mission of academics, adult education and workforce development.
- Protect existing jobs.

State appropriations provide about half of the revenues of a typical Alabama community college, with tuition and fees adding another fourteen percent, according to data feedback reports from the National Center for

Education Statistics. As is true of educational institutions generally, personnel costs make up a major part of a college's operating expenditures.

### **Tuition Increases?**

Tuition policy for the Alabama Community College System is set at the System level, and there have been no tuition increases in the past three years, nor are there plans to do so in the current economic environment. The policies of the State Board of Education and the Chancellor call for each of the state's community colleges to work toward setting aside a budget reserve. The target has been to create a reserve equal to three months of operating expenditures, as a hedge against future budget uncertainty.

### **Fund Balances?**

The Chancellor recently presented a report to the State Board of Education detailing the methods by which community colleges plan to make the reductions required by proration in the current fiscal year. Those reductions total \$32 million. Colleges will use their fund balances to cover \$8 million of this amount and take the remainder from personnel, operating, and capital expenditures. For nine colleges, fund balance reductions are the largest item; others rely more heavily on operating reductions.

### **Reductions**

Ten million dollars will be cut from salary expenditures. The Alabama Industrial Development Training Institute, which hires personnel on a project basis to provide training services for employers coming into the state, accounts for \$3.7 million of these salary reductions. Colleges will cut the remainder by eliminating positions and not filling vacancies. For seven colleges, personnel costs are the largest source of reductions.

Full-time teaching personnel in Alabama's community colleges are generally employed under nine-month contracts, with three-month extensions for those who teach during the summer. At least half of the faculty should be full-time, according to accrediting standards. The institution must pay the balance of the personal services contract upon dismissal, making mid-year personnel reductions uneconomical. Part-time faculty are hired on a semester-to-semester basis based on demand, which affords greater flexibility to the institution in making budget adjustments.

Other full-time college employees are hired on twelve-month contracts. All full-time employees, both teaching and non-teaching, receive tenure-like protection after three years in their positions.

Another \$11 million will be cut from operating expenditures. Of this amount, \$5.7 million will come from reducing expenditures for materials and supplies. Professional fees and contracts will be cut by \$2 million, travel by \$1 million, and the remainder from

other operating accounts. Eight colleges will rely on operating accounts as the largest source of proration cutbacks.

The remaining \$3 million of proration cutbacks in community colleges will come from postponing capital expenditures. In two instances, this is the largest source of reductions.

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## **RESPONDING TO PRORATION: THE UNIVERSITY OF NORTH ALABAMA EXPERIENCE**

**By William G. Cale, Jr.**

Proration is a budgetary condition declared by the Governor of Alabama, and occurs when state revenues are insufficient to meet obligations (expenses). This condition can arise at any time during the fiscal year and is implemented by reducing each affected agency's annual budget by the prorated amount. In the instance at hand, Governor Bob Riley declared a state of proration in December, 2008, in the amount of 12.5%, but limited that to 9% through partial liquidation of assets made available to the Educational Trust Fund as a result of passage of Amendment One in November, 2008.

The University of North Alabama, located in Florence, is a school of 7,200 students which has historically received about 50% of its operating budget through state appropriations. In the fall of 2007 our state appropriation was \$33,906,526 and we began last fall with a budgeted appropriation of \$30,741,447, a loss of \$3.165 million. In December, with proration declared at 9%, an additional \$2.766 million needed to be removed from the budget, for an FY 2009 loss of \$5.93 million. Other universities in Alabama have experienced similar percentage reductions, all on the order of 20%.

### **Fiscal Resources**

Universities have two principal sources of revenue for instruction: state appropriations and tuition income. Income from auxiliary activities, contracts, and grants, do not support basic instruction. Endowment income and gifts are almost always designated for specific purposes such as scholarships, new facilities, or supplemental funds for excellence. Endowment funds essentially never support operational costs or base salaries. Thus, in periods of declining state appropriations, institutions respond by combining tuition increases with a variety of budget cuts. The financial burden shifts increasingly to students and their families, and the ability of the university to live up to its full potential is diminished.

While there are many ways to implement a budget reduction, each is a variation or combination of two fundamental approaches. The first is the across the board cut, where each budget manager is required to

remove the appropriate percentage of funds from their line. The second is strategic, where the requisite funds are removed selectively, leaving core programs and personnel in place in order to minimize the impact on students. At UNA, as with most other universities, the largest percentage of funds expended is on personnel, and personnel lines are budgeted to account managers throughout the campus. Funds that are designated for purposes such as deferred maintenance and capital improvement, equipment, technology, and contingency, tend to be held centrally and allocated during the budget year to meet planned objectives and deal with unexpected needs. Thus, across the board cuts can impact personnel heavily while leaving other more discretionary budgets largely in place. At UNA we have implemented a budget plan that is strategic, with the principal goals of preserving instructional integrity, avoiding layoffs, and protecting departmental operating budgets so that the core functions and forward progress of the university can continue.

To accomplish these goals many activities must cease, some reserve funds must be used, and one must develop a plan on how to transition into a new operating mode if the State's economy remains the same or even worsens. Complicating this is the reality that many mandatory costs are increasing. At UNA we estimate that in FY2010 our health care costs, utilities, supplies, library subscriptions, and retirement contributions will increase at least \$750,000. In response to Governor Riley's declaration of proration, UNA undertook the following actions to balance the university's budget:

- All current year funds that are unspent will roll forward in place to next year;
- All contingency and discretionary accounts are eliminated;
- Freeze open positions; presidential approval required to replace any vacancy;
- Eliminate technology budget;
- Eliminate non-technology equipment budget;
- Use the Distance Learning Fee account to absorb two positions;
- Place all continuing education personnel, selected business staff, and international support staff on appropriate auxiliary budgets;
- Eliminate physical plant budget for supplies, equipment repair, building repair; replace on a critical needs basis from reserves;
- Fund convocation, homecoming, and commencement from reserves;
- Freeze unallocated athletic scholarships;
- Reduce institutional equity training and speaker budget by half;
- Allocate reserve dollars to cover essential unanticipated needs (since contingency lines have been eliminated).
- Each budget manager must prepare a contingency plan to implement a further 5% cut;

- All campus employees must be informed of our response to proration, and be afforded the opportunity to ask questions and provide advice.

What this means operationally is that funds budgeted for construction, deferred maintenance, and emergencies are eliminated. Some reserve funds are available in critical situations. Funds for new faculty and staff lines are eliminated; existing vacancies are frozen (effectively eliminated unless new dollars become available). The budget for new equipment and new technology is gone. Rolling unspent dollars forward encourages stewardship, and mitigates the impact of a further budget cut in FY 2010. With the opportunity to adjust tuition in each of the next two years, coupled with the conservative use of some reserve dollars and without further economic deterioration, we anticipate that UNA can weather this difficult period for at least two years.

It must be said that there are limits to how far cuts can go and how long they can last before the educational experience for students is deeply harmed. As solid as UNA's plan is, it can only be successful for a relatively short time. There is a limit to how long one can actually defer maintenance, not purchase equipment and computers, not replace personnel, not buy supplies from a budget line, and not allow faculty to stay current through their own professional development. There are also limits to how long one can sustain a productive group of faculty and staff when there are no pay raises, and we must surely be concerned about the damage we do to the future as access to higher education becomes more and more difficult due to rising tuition costs. Constraints on hiring top faculty and administrators have their own long term consequences. In my estimation, we as a State stand at a threshold.

#### About the Contributors

**Randolph Horn** is an Associate Professor of Political Science at Samford University and Director of the Samford University Survey Research Center.

**Jodi Newton, Ed.D.** is an Assistant Professor of Education at Samford University and a former Superintendent of the Homewood City School System.

**William G. Cale, Jr.** is President of the University of North Alabama.

Public Affairs Research Council of Alabama  
P.O. Box 292300, Samford University  
800 Lakeshore Drive  
Birmingham, Alabama 335229-7017

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