State Strategies for Maintaining a Balanced Budget

Case studies offer lessons on identifying and managing nonrecurring revenue
The Pew Charitable Trusts

Susan K. Urahn, executive vice president and chief program officer
Michael D. Thompson, vice president

Project Team

Steve Bailey
Kil Huh
Akshay Iyengar
Airlie Loiaconi
Mary Murphy
Patrick Murray
Alexandria Zhang

External reviewers

This report benefited tremendously from the insights and expertise of two external reviewers: James A. Richardson, John Rhea Alumni Professor of Economics and director of the Public Administration Institute, Louisiana State University, and a member of the Louisiana Revenue Estimating Conference; and John Nixon, vice president of administrative services, University of Utah, and a former state budget director in Michigan and Utah. These experts have found the report’s approach and methodology to be sound. Although they have reviewed the report, neither they nor their organizations necessarily endorse its findings or conclusions.

Acknowledgments

We thank Catherine An, Timothy Cordova, Casey Ehrlich, David Frazier, Richard Friend, Kimberly Furdell, Alan van der Hilst, Elizabeth Hughes, Jim Jukes, Bronwen Latimer, Adam Levin, Erin McNally, Cindy Murphy-Tofig, Colton Naval, Bernard Ohanian, Jeremy Ratner, Dan Rockey, Lonnie Shekhtman, Anne Usher, Liz Visser, and Robert Zahradnik for their valuable editing and production assistance on this report.

Contact: Catherine An, communications officer
Email: can@pewtrusts.org
Project website: pewtrusts.org/states-fiscal-health

The Pew Charitable Trusts is driven by the power of knowledge to solve today’s most challenging problems. Pew applies a rigorous, analytical approach to improve public policy, inform the public, and invigorate civic life.
Overview

Many states ended 2017 flush with unexpected cash. Federal legislation that caps some tax deductions beginning in 2018 prompted many Americans to prepay their state and local taxes. While this surprise revenue was positive news for state budgets, several policymakers struck a cautious tone.

“This is not a windfall,” Robert Mujica, director of the New York State Division of the Budget, said in January 2018. He predicted that the bump in tax collections would be offset by a corresponding drop in receipts in the year ahead.

In fact, states have seen one-time revenue spikes like this before. In 2013, several of them recorded unexpected revenue boosts when many investors—anticipating an increase in federal capital gains taxes—took stock market profits before the change went into effect. Many states grappled with how to treat this influx of cash. While most of the spike in revenue came from annually collected sources like personal and corporate taxes, the nature of the increase meant some of the gains might be temporary.

Utah, for example, initially projected that individual income tax revenue in 2013 would grow by 7.8 percent. (The final numbers showed that growth was actually 16 percent.) State economists believed the higher tax revenue was temporary and suggested that policymakers treat 90 percent of it as a nonrecurring, or one-time, event. Taking the cue, lawmakers spent the unexpected revenue on short-term priorities such as the construction of a courthouse for juvenile hearings. And the next fiscal year, the state planned conservatively, accurately anticipating a substantial decline in tax collections.

Not all states planned—or fared—as well. Despite cautious forecasts, seven states missed their April 2014 individual income tax revenue estimates by more than 10 percent. In Kansas, revenue from this source had beaten projections in 2013 after the state cut its taxes, causing lawmakers to be optimistic about future revenue. However, revenue came in 28 percent under the forecast, leading the state to draw down reserves that it has yet to rebuild.

These events underscore the importance of identifying and managing nonrecurring revenue. Failure to do so does not affect only one year’s budget; it can often create or perpetuate a fiscal imbalance that lasts several years. Conversely, when states regularly allocate nonrecurring revenue to one-time priorities, they can mitigate potential budget problems before they form.

While budget challenges from nonrecurring revenue exist in every state, there is no universal practice for how to manage or define this revenue. Economists, budget officers, and policymakers in some states formally distinguish it from revenue that is expected to be collected in future years, while others rely on informal and ad hoc ways to track the revenue.

To identify and evaluate state approaches to detecting and managing nonrecurring revenue, The Pew Charitable Trusts examined practices in all 50 states—focusing on policies codified in state statutes and constitutions. This report includes case studies that highlight the range of strategies that states use, with the goal of informing policymakers of promising practices. The featured strategies include:

- Techniques states use to identify nonrecurring revenue:
  - Case study 1. Alabama: Defining certain revenue sources as recurring or nonrecurring.
  - Case study 2. Tennessee: Separating a volatile tax source into recurring and nonrecurring parts.
  - Case study 3. Utah: Separating all major tax sources into recurring and nonrecurring parts.
Techniques states use to manage nonrecurring revenue:

- Case study 4. Louisiana: Limiting nonrecurring revenue to specific appropriations.
- Case study 5. Florida: Limiting the amount of nonrecurring revenue that pays for ongoing costs.
- Case study 6. Washington: Analyzing whether expected future spending is balanced by recurring revenue.

Based on this research, Pew recommends that states consider the following when deciding how to identify and manage nonrecurring revenue:

- Develop definitions for this revenue and regularly report on its ability to cover ongoing costs.
- Treat abnormal growth in annually collected taxes as nonrecurring revenue.
- Create guidance to ensure that nonrecurring revenue is used on one-time spending commitments.

**Why isolate nonrecurring revenue**

A state must bring in funds equal to what it spends to achieve a balanced budget in any given fiscal year. When revenue declines, such as during a recession, a state may need to spend more than it takes in—using reserves and other one-time measures to make up the difference. To offset that, most states collect more revenue than they spend during periods of economic growth. (See Figure 1.) In 2006, a relatively strong year for economic growth, median state revenue was 106.3 percent of spending, but only 94.4 percent in 2009 during the Great Recession. Achieving that equilibrium over a period of time is commonly referred to as having a structurally balanced budget.

**Figure 1**

50-State Median Percentage of Annual Expenses Covered by Revenue, 2002-16

States take in more than they spend in some years, less in others

Source: Pew Fiscal 50 indicator

© 2018 The Pew Charitable Trusts
The volatility of the U.S. economy hinders state efforts to achieve long-term structural balance. Total state revenue largely tracks the economy’s ups and downs, meaning policymakers must be careful not to overcommit resources during revenue peaks since they will need additional funds to navigate the valleys. To further complicate matters, some revenue sources are less consistent than others and may fluctuate independently of the business cycle.

For example, a state that receives a large legal settlement that boosts revenue in one year might want to distinguish that revenue from more regularly collected sources. Identifying a one-time settlement or transfer is relatively easy. But in other situations, annually collected taxes, such as those on personal or corporate income, may experience a spike that could be considered one-time in nature. Similarly, sales tax revenue can grow faster than average immediately after a natural disaster as residents purchase items to replace damaged property. Another common source of nonrecurring revenue is a surplus from the previous fiscal year, which many states build into their base budget. Without enough revenue growth to make up for that extra cash the next fiscal year, the state can be left with a budget shortfall, even during an economic expansion.

Figure 2
Common Sources of Nonrecurring State Revenue
Examples of revenue that may be one-time in nature

- Extraordinary growth in tax collections (especially from volatile sources)
- General fund ending balance
- Cash shift from other state accounts (such as rainy day funds)
- Large legal settlements
- Temporary state tax increases
- One-time transfers from the federal government

The implications of misusing nonrecurring revenue extend beyond one year. Continually relying on nonrecurring revenue during periods of growth to pay for ongoing costs—spending and tax reductions that are expected to be funded for the foreseeable future—puts a state at risk for long-term deficits. New Jersey has struggled with a structural deficit for years, partly because of its reliance on nonrecurring revenue to overcome deficits, even outside of recessions. Between fiscal years 2002 and 2006, the state spent over $16 billion from one-time sources such as court settlements and delayed payments. Rainy day funds and other reserves can act as a budget stabilizer during changes in the economy but should be counted on only as part of the solution. It is essential to separate recurring and nonrecurring revenue in budgeting to help provide this stability.
Most policymakers and budget experts agree that identifying nonrecurring revenue in the budget is important, as is managing it in a different manner. The Government Finance Officers Association recommends that the first step to achieve a structurally balanced budget is to identify nonrecurring and recurring revenue, expenditures, and other key categories. And in a 2017 report, “Truth and Integrity in State Budgeting: What Is the Reality?” The Volcker Alliance, a nonpartisan government research group created by former Federal Reserve Board Chairman Paul A. Volcker, states, “A basic tenet of budgeting is that one-time revenues should fund only one-time expenditures and that recurring revenues should cover obligations that come due every year.”

Similarly, all three major U.S. credit rating agencies discuss in their methodology sections the link between matching recurring revenue to recurring expenditures and attaining a structural balance. In its framework for evaluating the financial health of states, Fitch Ratings notes, “Concerns arise when operating expenditures consistently exceed operating revenues, as the use of nonrecurring revenue is unsustainable and usually leads to depletion of reserves and deeper financial imbalances.” Standard & Poor’s Ratings Services advises that “a track record of aligning recurring revenues and expenditures over time is an important element of fiscal performance.” And Moody’s Investors Services notes that although use of a nonrecurring revenue source to balance the general budget is common during economic downturns, an overreliance can lead to long-term fiscal pressures and is more likely to generate a ratings downgrade.

Despite widespread acknowledgment of the importance of understanding and managing one-time revenue in the budget, there is no commonly accepted guideline for defining which funding sources recur and which do not. In fact, most states have no definition in their constitutions or statutes. This can lead to uncertainty, as policymakers’ views may vary.

The six state examples in this report explore the two key steps policymakers should consider when attempting to manage one-time resources. The first set of case studies focuses on the definitions that states use to identify nonrecurring revenue, while the second set explores laws that states have passed to manage this revenue once it has been identified.
Some States Deposit Nonrecurring Revenue Growth Into Rainy Day Funds

Forty-eight states have a rainy day, or budget stabilization, fund to set money aside in good times to be available in bad. Of those states, 20 have adopted laws to save money when revenue growth exceeds a certain threshold.

Some states tie these deposits to growth in general fund revenue. Virginia, for example, deposits half of general fund revenue growth that exceeds a six-year trend line. Other states link deposits to extraordinary growth in an especially volatile tax source.

Maryland sets aside the most unpredictable portion of its personal income tax when it exceeds its 10-year average share of general fund revenue. This is a promising practice for preventing unsustainable and possibly nonrecurring revenue growth from going toward recurring costs.

For revenue that is allocated through general appropriations, determining what might be recurring versus nonrecurring can be especially important. Anticipating every budget scenario that may produce nonrecurring revenue is almost impossible, but the guidance below can help policymakers better manage unexpected boosts in revenue and prevent structural imbalances down the road. The three case studies feature ways these states codify nonrecurring revenue in law.
Case study 1.
Defining certain revenue sources as recurring or nonrecurring

One of the most straightforward ways to identify nonrecurring revenue is by its source. A payment made or received as the result of a legal settlement, for example, is almost always a “one-time” occurrence. Exceptions to the one-time nature of such payments are rare. The most notable recent one was the 1998 Master Settlement Agreement, which required the top U.S. tobacco manufacturers to make annual payments to 46 states in perpetuity.¹¹

Alabama differentiates in statute between recurring and nonrecurring revenue in its education trust fund, its largest spending fund, defining recurring revenue as “any permanent and continuing source of revenue of any kind or type” that existed in previous fiscal years. The statute also notes that transfers from other funds, such as reserves or the end-of-year balance, are nonrecurring revenue sources.¹²

Since 2011, this distinction has helped remove some of the budget noise caused by inflows and outflows of nonrecurring funds. Getting a better handle on recurring revenue was important for Alabama, which had repeatedly cut its education budget midyear. “One problem in flush years is the Legislature’s tendency to spend on ongoing expenses without long-term funding solutions,” said Sally Howell, executive director of the Alabama Association of School Boards.¹³

The state uses this information to calculate a long-term growth trend for recurring revenue. To manage the amount allocated to ongoing spending commitments, a portion of recurring revenue growth that exceeds the trend line is set aside for the state Budget Stabilization Fund and the Advancement and Technology Fund. This account is for school facility repairs and deferred maintenance, classroom instructional support, transportation, new equipment, and other categories.¹⁴ Growth in excess of the trend in fiscal 2016 was $116 million, of which $59.6 million went to the stabilization fund and the rest to the technology fund.¹⁵

Alabama’s use of the recurring revenue trend line may not fit every state. Since 2011, the state has modified its rules to reduce the amount of excess recurring revenue put into savings for fear it was setting aside too much.¹⁶ Nevertheless, all states can benefit from clearly identifying recurring and nonrecurring revenue during the budget process, regardless of how strict the requirements are for how that revenue is spent.
Sometimes a regularly collected revenue stream can exhibit one-time bumps that should be distinguished from recurring revenue. This commonly occurs when streams are often volatile, such as personal or corporate income tax collections.

In Tennessee, for example, corporate franchise and excise taxes traditionally experience large annual swings. (See Figure 3.) Since 1981, yearly fluctuations in these taxes have nearly doubled. In addition to being volatile, they are also significant tax sources, second only to sales and use taxes. While any revenue source that fluctuates widely from year to year can cause budget problems, those can be exacerbated when that source makes up a large portion of overall revenue. In fiscal 2012, franchise and excise tax revenue grew by 32 percent, then fell by 9 percent the next year and another 4 percent in 2014. That decline was the main reason the state’s general fund was in the red at the end of that fiscal year. Lawmakers partially offset the shortfall by cutting spending, taking money from reserves, and forgoing a planned raise for some state employees.

**Figure 3**

**Tennessee Franchise and Excise Tax Fluctuations, 2007-17**

Volatile tax sources are prone to unsustainable revenue spikes

Source: Pew analysis of Tennessee Department of Revenue data

© 2018 The Pew Charitable Trusts
When the next legislative session launched in 2015, Tennessee lawmakers passed a bill that required the Department of Revenue to separate revenue from its corporate franchise and excise taxes into recurring and nonrecurring portions to the extent possible. State Senator Randy McNally (R) explained that the statutory provision was intended to prevent “one-time abnormalities” from becoming part of the state’s base revenue forecast.20

The law allows the state to better categorize annual shifts in the revenue stream. In Tennessee, as in other states, it is common for one company’s actions to drastically influence business tax revenue performance. One-time events—including mergers, litigation, and audit assessments—can create large but temporary shifts in revenue. Under the new law, the Department of Revenue must report the nature of each company’s tax payment and analyze the potential impact it would have on the next fiscal year’s revenue.

While the state may not be able to publicly disclose the underlying cause for the nonrecurring change due to a company’s confidentiality concerns, it does give the state enough information to avoid allocating nonrecurring revenue to ongoing expenses. For fiscal 2017, the Department of Revenue anticipated about $180 million in nonrecurring tax payments.21

Case study 3.
Separating all major tax sources into recurring and nonrecurring parts

While one-time spikes in volatile revenue sources like corporate income taxes may be easier to identify, many revenue sources exhibit periods of above-normal growth. When a state economy reaches peak growth during the business cycle, for example, it is likely that sales tax revenue—largely a product of income growth—will also record higher-than-normal growth rates. (See Figure 4.) As the economy cools, this revenue growth will decline as well. Despite these fluctuations, most states do not typically think of more traditional revenue sources like the sales tax as having a nonrecurring component apart from temporary tax increases or decreases.

Yet regardless of the source, above-normal revenue growth is by definition unsustainable. This concept has proved true in Utah. Since 2014, the revenue report from the Office of the Legislative Fiscal Analyst and the governor’s budget proposal must include an analysis of the 15-year trends for each tax type.22 When revenue exceeds that trend line, legislative rules require legislators to consider excess revenue growth as one-time revenue when crafting the budget. In other words, each tax source may be considered to have nonrecurring parts when they are growing faster than normal.
Figure 4
Utah’s Sales Tax Revenue vs. 15-Year Trendline, 2012-18
State identifies periods of nonrecurring growth, shortfalls in major tax sources

For example, the Office of the Legislative Fiscal Analyst forecast that fiscal 2016 revenue would be $116 million above Utah’s 15-year trend.23 When budget writers adopted that forecast, they designated this revenue as one-time, ensuring that it would not be used for ongoing spending. State Representative Brad Wilson (R), who proposed the rule change, said moving those funds into the “one-time bucket” had an important effect. “It helped all the lawmakers who were paying attention to the budgeting process understand we are in fact above trend,” Wilson said. “We are at a point in the business cycle where we should be preparing for lean times again.”

The framework gives the state a longer-term view of how to allocate revenue throughout the business cycle, which Utah’s legislative fiscal analyst, Jonathan Ball, refers to as “temporal balance.” Ball said understanding a state’s nonrecurring revenue “is an important first step” for lawmakers. Having a better picture of where revenue stands in relation to the trend helps Utah lawmakers decide when and how to use nonrecurring revenue. The state can better decide when, for instance, to pay for capital projects with cash instead of borrowing, the best times to make allocations into rainy day funds, and what money should be included in next year’s base budget.24

Managing nonrecurring revenue

Once policymakers have identified nonrecurring revenue, they can use that data to make more informed budget decisions. There are many appropriate uses for these funds. Managing nonrecurring revenue appropriately is less about whether it should be used than the purpose and timing of its use. For that reason, states benefit from establishing guidelines to ensure that it can be used strategically.
Managing nonrecurring revenue appropriately is less about whether it should be used than the purpose and timing of its use.

Techniques for managing the timing and use of nonrecurring revenue vary in their formality. When Utah allocates such funds, it is largely up to the Legislature to decide whether the use is a one-time event. This is a fairly common practice. As is the case with identifying revenue, few states have laws that dictate how nonrecurring revenue is spent, relying instead on ad hoc approaches. In an era of greater uncertainty about revenue, states would benefit from having formal guidance in place. The next three case studies explore state laws on managing nonrecurring revenue.

Case study 4.
Limiting nonrecurring revenue to specific appropriations

Although there is general acceptance that nonrecurring revenue should be dedicated to one-time spending, defining such spending can be challenging. Some expenditures are required by law, while legislatures approve others annually or biennially. Many of those appropriations may not be included in future budgets, though few people would argue that all of those spending items are truly one-time. For example, money allocated to state employee salaries is unlikely to be nonrecurring in nature.

Louisiana attempts to eliminate confusion by listing appropriate uses for such funds. Each year, the state’s Revenue Estimating Conference determines what revenue sources are nonrecurring. These could include funding streams that were not available for the previous two fiscal years and won’t be for the next two, such as large legal settlements or end-of-year budget surpluses. Once the nonrecurring revenue sources are identified, the Legislature can allocate those funds only to pay off bonds, reduce the state’s public retirement system debt, fund capital projects, and make deposits into the state’s rainy day fund and wetlands conservation fund. (See Figure 5.)
This approach has multiple benefits. Not only does it promote a structurally balanced general fund, but it also helps Louisiana manage its long-term obligations. Nonrecurring revenue collections are an ideal opportunity for states to pay down debt and spend on capital plans and other one-time needs.

This practice is having an impact on the state’s budget discussions this year. At the end of fiscal 2017, Louisiana had a $120 million budget surplus due to higher-than-expected revenue. However, forecasters are anticipating an almost $1 billion budget gap by fiscal year 2019, largely because a temporary sales tax hike will expire. Because the surplus from fiscal 2017 was designated as nonrecurring, the state is unable to use it to help close the anticipated gap.28

Although lawmakers face a challenge balancing the budget, the rule also prevents them from using one-time funds to smooth over a structural budget issue caused by the expiring tax increase. This illustrates the trade-off that states face when they have policies for nonrecurring revenue: They are pushed to institute changes to correct systemic budget problems, but it also means tougher immediate decisions and less flexibility for using one-time funds.
While Louisiana lists uses for nonrecurring revenue, another approach is to set a threshold for what portion of these funds can be included in each year’s budget. In 2006, voters in Florida approved a constitutional amendment to create more guidance in the budget process. The amendment requires an annual three-year budget and revenue forecast that includes strategies for the state and its departments to help the Legislature make budget decisions. The amendment also limits the nonrecurring revenue that can be allocated to recurring costs at 3 percent of projected general revenue.

The law prevents policymakers from relying too much on nonrecurring revenue in a given year, allowing them to determine a small share that can be safely included in the long-term base budget. The limit may be overridden by three-fifths of the members of each house. In general, Florida decides if a revenue source is recurring or nonrecurring by whether collections are expected to continue for at least five years. But determining what counts as nonrecurring revenue is determined largely through a consensus-based revenue forecasting process.

In the past, examples of nonrecurring revenue included unspent funds from the previous fiscal year, settlement agreements, proceeds from certain state trust funds, and time-limited federal grants. In fiscal 2017, those funds also included money from a settlement agreement with BP after the Gulf of Mexico oil spill, reimbursements from the Federal Emergency Management Agency for storm recovery, and fixed capital outlay reversions. Those revenues went to fund nonrecurring costs such as capital projects, response to the Zika virus outbreak, and transfers to the budget stabilization fund.

Florida’s strategy has evolved. It has institutionalized the identification of recurring and nonrecurring revenue and expenditures for several years. Even before the 2006 constitutional amendment, the state’s financial outlook statement clearly identified both nonrecurring revenue and nonrecurring expenditures built into the budget. But with no list of what constitutes nonrecurring revenue or appropriations, forecasters and policymakers must determine them each year. That flexibility can be a good thing—as it is hard to anticipate every case in which a revenue source or appropriation is one-time—but it also requires some consistency and adherence to the law for it to operate as intended.
Some states are not only making an effort to match revenue and spending in the current budget year, but also looking ahead to future years to ensure that they can maintain that balance. Every other year, Maine’s Bureau of the Budget produces a structural gap report designed to show how well the state can support its services with ongoing revenue based on current law and program trends.

Washington codified its long-term state budget outlook in 2012, extending revenue and spending projections to the subsequent biennium for both the governor’s budget proposal and the enacted budget. This means that for the 2019 biennium, revenue and cost projections were extended out to the biennium ending in 2021.

The outlook provides a snapshot of the state’s future budget health in the absence of most nonrecurring revenue items. For example, one-time transfers for the next two years are included only if they are statutorily required or if lawmakers adopted language to maintain the transfers. The long-term recurring revenue projections are compared to the future cost forecast—which reflects the cost to continue current programs, entitlement program growth, and actions required by law in the subsequent fiscal biennium—giving policymakers an early warning of potential structural problems.33

Washington takes its long-term budget a step further than most states. The Legislature must ensure that projected costs for the ensuing biennium do not exceed available fiscal resources. These are defined as the existing general fund balance plus the greater of the projected revenue forecast or an assumed 4.5 percent growth rate.34 When he introduced the bill codifying the practice, former state Senator Jim Kastama (D) said, “We need to take concrete action here in Washington state to assure [citizens] that we aren’t coming back every single year with increased deficits.”35

We need to take concrete action here in Washington state to assure [citizens] that we aren’t coming back every single year with increased deficits.”
—Former state Senator Jim Kastama (D)

While not all states may choose to tie their current budget decisions to future projections in this way, it is still prudent to understand how current budget decisions affect the future. A long-term budget can be used to predict future fund balances and identify any potential revenue shortfalls, helping policymakers understand likely recurring revenue and expenditures to achieve structural balance. The policy “makes fiscal common sense,” Kastama added. “Our budgets need to align with future projections.”36
**Recommended policy practices**

1. Develop definitions for nonrecurring revenue and regularly report on its ability to cover ongoing costs

States benefit from early warnings of a growing structural imbalance, which occurs when recurring expenditures consistently exceed recurring revenue. To accomplish this, states should measure and report on their long-term budget trends. This process involves understanding which revenues are likely to continue and which are nonrecurring, and assessing recurring costs. States should analyze the difference between recurring revenue and recurring costs in the current budget as well as future budget years to identify potential areas for concern. This analysis can help policymakers properly manage nonrecurring revenue across the business cycle. To ensure consistency and budget transparency, a state could mandate a report on a recurring basis, such as the structural gap report in Maine or the state budget outlook process in Washington.

2. Treat abnormal growth in annually collected taxes as nonrecurring revenue

Temporary events can cause one-time revenue spikes from regularly collected sources. As a part of identifying nonrecurring revenue in a budget or projection, states should expand their traditional definition and consider isolating some of those one-time spikes. This will help prevent an overreliance on revenue growth during economic booms, leaving the state in a better position to respond when revenue drops below normal. Examples include Tennessee, which separates revenue from its unpredictable business taxes into recurring and nonrecurring; and Utah, which makes a similar distinction for all major tax sources.

3. Create guidance to ensure that nonrecurring revenue is used on one-time spending commitments

Money identified as nonrecurring revenue should be treated differently from recurring funds. When a state uses one-time revenue to fund recurring commitments—whether ongoing program spending or permanent revenue reductions—budget deficits can result. To prevent this, states should allocate nonrecurring revenue to savings, one-time expenditures, or temporary revenue reductions.

States can accomplish this in a number of ways, ranging from laws on how the money should be spent, as Louisiana has, or more flexible guidance, as found in Florida and Utah. Strict rules for how to manage one-time revenue might not be the best approach for every state, but policymakers should understand the impact of using one-time money to pay for ongoing expenses, consider ways to differentiate how nonrecurring revenue is used and built into the budget, and report on how it is allocated each budget cycle.

States that do this successfully can see benefits beyond their operating budget. By ensuring that stable revenue is used to fund ongoing costs, they can more actively and responsibly manage debt service, capital plans, and other one-time spending needs. Effective plans to pay down those obligations over time are equally critical to achieving long-term structural balance.
Conclusion

States are facing increasingly uncertain budget futures. Growing long-term costs, greater revenue volatility, and slower revenue growth leave states vulnerable to fiscal imbalances. Relying on one-time bumps in revenue is an easy short-term fix for these budget gaps, but it serves to exacerbate fiscal problems in the long run. Identifying and managing nonrecurring revenue better can help policymakers keep their budgets structurally sound and avoid a major problem.

Appendix A: Methodology

Identifying nonrecurring revenue practices

States have a variety of practices for identifying and managing nonrecurring revenue. Many states do not have guidance in statute, relying instead on a standardized practice that has been developed over time. While states find this approach valuable, Pew narrowed the scope of policies considered for the case studies to those that are codified in statute or the state constitution.

Pew identified those codified policies through a 50-state scan in LexisNexis using keywords related to nonrecurring revenue and expenditures in state statute and legislative rules. It focused on those related to revenue forecasting or budget formation. Keywords included “nonrecurring,” “one-time revenue,” and “one-time expenditures.”

Additionally, while states use many techniques to manage uncertain and possibly nonrecurring revenue gains—such as earmarking these sources to a rainy day fund or a capital fund—this report focused on practices that explicitly identify certain revenue as “nonrecurring” in the general budget or that manage the treatment of nonrecurring revenue.

Selecting case studies

Based on the codified practices identified during the data collection process, Pew created a typology to differentiate the ways states identify and manage nonrecurring revenue. These case studies are not intended as full summaries of all codified practices in this area but instead are designed to highlight a particular technique and its trade-offs.

These case studies were supplemented with background interviews with state officials to ensure accuracy of reporting and correct interpretation of state statutes. The team also used individual state revenue forecasts, executive budget requests, and appropriations bills for additional details.
# Appendix B: Citations for case studies

<table>
<thead>
<tr>
<th>Case study</th>
<th>State</th>
<th>Practice</th>
<th>Citation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Alabama</td>
<td>Defining certain revenue sources as recurring or nonrecurring</td>
<td>Code of Ala. § 29-9-2 (2018)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Code of Ala. § 41-4-3.1 (2018)</td>
</tr>
<tr>
<td>3</td>
<td>Utah</td>
<td>Separating all major tax sources into recurring and nonrecurring parts</td>
<td>Utah Code §36-12-12.13 (2018)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Utah Joint Rules § JR3-2-402 (2018)</td>
</tr>
<tr>
<td>4</td>
<td>Louisiana</td>
<td>Limiting nonrecurring revenue to specific appropriations</td>
<td>La. Const. art. 7, § 10 (2018)</td>
</tr>
<tr>
<td>5</td>
<td>Florida</td>
<td>Limiting the amount of nonrecurring revenue that pays for ongoing costs</td>
<td>Fla. Const. art. III, § 19 (2018)</td>
</tr>
<tr>
<td>6</td>
<td>Washington</td>
<td>Analyzing whether expected future spending is balanced by recurring revenue</td>
<td>Wash. Code § 43-88-055 (2018)</td>
</tr>
</tbody>
</table>
Endnotes


19 Tennessee State Funding Board, meeting agenda and presentations, 92.


23 Standard & Poor’s Ratings Services, “U.S. State Ratings Methodology.”
34 Ibid.
36 Ibid.