

## CHAPTER 8:

# Budgetary Reform<sup>1</sup>

The budget process is constantly evolving. Where it was once focused entirely on preventing overspending, it has since evolved into a primary executive management tool and a means of undertaking regularized strategic planning to achieve defined outcomes. Most analysts would consider this aspect of budgetary evolution to be commendable, but other evolutionary developments are less so. Both executive budget development and the legislative appropriations process in Ohio could be significantly enhanced from greater openness. While the state is a leader in government spending transparency, opportunities for further improvement remain.

## Improving Executive Budget Development

Two important aspects of executive budget development are its formatting and the estimation of revenues. Changes to both components could result in significant budget improvements. There is also a question of whether the public would be better served if there were more openness in the budget development process.

### Formatting the Budget

When it comes to public accountability for the expenditure of state funds in Ohio, little has changed over the last 50 years because the state's accounting, budgeting, and auditing systems are separate. This disjunction is reflected in the formatting of the state's financial system. One reason it is so difficult to understand state budgeting in Ohio is that three distinctly different formats are used:

- Agencies develop and present their budgets to the governor in a modified program format that is reflected in the Executive Budget Request, or "Blue Book."
- The legislature reviews and enacts appropriations in a line item format reflected in the appropriations bill.
- The state accounts for expenditures, and audits agencies, in an object of expenditure format reflected in annual audited financial reports, post-audits, and other supplementary accounting documents.

Many states, as well as the federal and local governments, have found ways to bring their financial systems into alignment. Hawaii is one of several states that seem to have “got it right.”<sup>2</sup> Its financial system combines budgeting and fiscal planning into a single comprehensive and cohesive system that provides useful information for management decision-making as well as operational control. In Hawaii, anticipated receipts and disbursements are allocated by program cost centers. Funding, programmatic objectives, performance measurement, and variance reporting are based on this lowest building block, the sub-program cost center. This streamlining makes it possible to link funding to the level of services provided and is especially conducive to automation and analysis.

By contrast, Ohio’s accounting is not linked to programmatic budgeting. The accounting system continues to be concerned with what is purchased by each dollar, for example personnel, health care, travel, and equipment. There is a separate accounting process that links those objects of expenditure back to the appropriation, but because the appropriation is by line item, not by program, the linkage falls apart. In Hawaii, appropriations are made neither by department nor by fund, but by program area, and sub-programs are each built up into higher programs.

In addition to making it difficult to understand Ohio budgeting, the disconnection of financial documents has made it impossible for Ohio to achieve the nationally recognized state budgeting goal of “budgeting for results.”

## Budgeting for Results

Results-based budgeting is a relatively recent management and budgeting trend and is the application to governments of results-based management. The concept originated in the private sector where managers are typically rewarded based upon the results they achieve. The components of a results-based budgeting system as applied to government are:

- **Strategic planning**, by which governments establish their mission and performance goals.
- **Performance measurement**, in which an agency quantifies how efficiently and cost effectively it has used its resources in delivering services by using a baseline, whether it be a standard, norm, or criterion, against which to assess performance in a program or services.
- **Benchmarking**, which is used to identify, analyze, adopt, and adapt the high-performance processes of other organizations that excel at doing a particular activity.
- **Managerial accounting**, which consists of (1) accumulating and reporting costs of activities on a regular basis for management information purposes, (2) establishing responsibility segments to match costs with outputs, (3) determining full costs of government goods and services, (4) recognizing the costs of goods and services provided among governmental entities, and (5) using appropriate costing methodologies to accumulate and assign costs to outputs.
- **Accountability in budgeting**, which means using a budgeting system that allocates resources according to results and holds agencies responsible for budgetary outcomes.
- **Service efforts and accomplishments (SEA) reporting**, which recognizes that a critical component of performance measurement is to report to decisionmakers and the public on the status of goal achievement.
- **Performance auditing**, which is undertaken by an independent auditor to systematically and objectively assess the performance of an organization, program, function, or activity of government.<sup>3</sup>

An interesting variation on results-based management is “Budgeting for Outcomes,” which produces results citizens value at a price they are willing to pay. Its basic steps involve:

- Setting the price of government.
- Setting the priorities of government.
- Setting the price of each priority.
- Developing a purchase plan for each priority.
- Soliciting offers to deliver the desired results.
- Negotiating performance agreements with the chosen priorities.

After some efforts in the 1990s, Ohio has not actively pursued results-based management, although the Auditor of State has recently undertaken performance auditing activities. This may indicate a movement in Ohio toward results-based management.<sup>4</sup>

## **Revenue Estimating**

The methodology that the governor’s revenue estimators use is technically as good as is used in any other state, but during recent years the estimates in some states have been better than those of Ohio. Why? The answer lies not within the methodology, but in the assumptions made in the preparation of the estimates.

Revenue forecasters base their methodology on the assumption that the past can be used as a predictor of the future. The problem is that this process does not always work well in forecasting individual income, commercial activity, and sales taxes that are dependent on economic changes. Since those economically sensitive taxes constitute the bulk of Ohio’s General Revenue Fund, they are the ones that are most important to predict accurately. This imperative means that a revenue forecaster has to examine what factors will affect collections from those taxes and use that knowledge to change the assumptions that a pure mathematical formula using historical data would generate.

When assumptions are erroneous, the consequences for revenue forecasting and those impacted by them can be severe. Budgeting on a biennial basis can further complicate the work of the revenue forecaster. During conference committee deliberations on the FY 2018–2019 budget, the state Budget Director requested that revenue estimates be adjusted downward by \$949 million over the biennium in light of FY 2016 and 2017 trends. Significant underperformance of the individual income tax and the non-auto sales tax portion of the sales tax had become apparent as early as mid-FY 2016. This led to a significant diminution in FY 2017 revenues and the need to adjust forecasts for both that fiscal year and the following biennium. Among the factors cited for the reduction in anticipated FY 2018–2019 revenues was lower than national average wage and salary growth, retail deflation, and increased e-commerce sales that were depressing non-auto sales tax collections.

Accurate revenue forecasting proved particularly elusive during the Great Recession, when the Office of Budget and Management was forced to revise its revenue projections on an all too frequent basis. Economic forecasting models had consistently understated both the depth and duration of the downturn in Ohio and its impact on personal income and business and consumer activity. Legislative tensions escalated to the point that the House Minority Leader called for the resignation of the then-budget director in March 2009. This demand echoed a similar demand made several years

earlier. In 2003, when the recession was less steep but when revenue estimates were still off by \$500 million, there were also partisan calls for the removal of the then-budget director.

During the 1990s, personal income grew disproportionately at the upper levels of the income distribution table. This uneven growth was because there were larger numbers of people investing in mutual funds making annual taxable distributions; exceptionally high capital gains resulting from insupportably high stock prices and lower federal capital gains tax rates; and huge bonuses paid to employees of the financial sector. Since the individual income tax is progressive, Ohio collected increased revenue from taxes from high-income taxpayers. This collection meant that the foundation for the high tax revenues rested with the strength in the financial markets. A dependence on this source of revenue proved extremely risky. The states that correctly assumed the stock market would collapse had more accurate individual income tax estimates than those that simply forecast the continuation of this aberration.

A similar forecasting miscalculation happened during the recession of the 1980s. The economy was buoyed by double-digit inflation during the 1970s, which resulted in huge gains in state revenues from sales taxes levied on goods with inflated values and in high individual income taxes levied on inflated wages. The assumption that this would continue indefinitely is what resulted in the poor revenue estimates during that economic downturn.

Until 1973, when the Legislative Budget Office of the Legislative Service Commission was created, economic forecasting and revenue estimation was the exclusive purview of the governor and executive staff. By controlling the estimation process, the governor was also able to control fiscal decision making. If there was a surplus, the governor would learn of it and propose to either spend it where he chose or choose which taxes to propose cutting. The governor would, in essence, be setting the legislative agenda. The same would hold true if revenue estimates were too high, but that never occurred until the state adopted the somewhat volatile individual and corporate income taxes in 1971. In 1973, the legislature decided to do its own revenue forecasting through the Legislative Budget Office. The state legislature intended these estimates to serve as a check on the reasonableness of the executive branch's forecasts. However, it never worked as originally planned.

The Legislative Budget Office should have used its independent forecasting ability to challenge the assumptions in the governor's forecast. Instead, the legislative estimates simply quibbled at the edges of the executive forecast, never departing from its underlying economic assumptions. Thus, Legislative Budget Office's estimates became simply a means for the legislature to pressure the executive to raise or lower its revenue forecasts to fit the spending needs defined by the General Assembly. The legislature has ultimately accepted the governor's forecast on most occasions, but it uses those of the Legislative Service Commission to push executive revisions. Under these circumstances, there is little reason to continue having the legislature make "independent" revenue forecasts. It would be more effective for the state to adopt the process of consensus forecasting, which most other states use.

**Consensus Forecasting.** The technical experts who prepare revenue forecasts are not necessarily proficient in formulating or revising core assumptions. This lack of expertise means that the revenue estimates prepared by the technical experts need to be evaluated to determine how realistic they are, how well they explain recent trends, and how insulated they are from political judgments. The best way to do that is through a process called "consensus forecasting," a process that is used in over half of the states.<sup>5</sup> The oldest and most institutionalized user of the process is Florida.

Since 1970, Florida has placed the responsibility for revenue forecasting in a committee specifically designed to perform this function. In 1982, the process was made statutory. The committee consists of one member each from the governor's office, the Senate, the House of Representatives, and the Legislative Office of Economic and Demographic Research, which is under the Joint Legislative Management Committee of the Florida Legislature. These four representatives, or their principals, must achieve consensus in order to issue an official revenue forecast, which is then used in all planning and budgeting actions in the state.

The committee's meetings are open to the public, and any of the principals can bring a forecast to the committee. They can also ask for outside parties to bring information or forecasts of their own in order to assist in formulating the official forecast. Because Florida adopts a budget annually, their revenue estimating committee meets in late autumn, and the forecast extends through the forthcoming year. The governor uses their forecast in preparing the executive budget request, and, in the spring, in determining the amount available for appropriation by the legislature. However, a meeting can be called by any principal whenever it is needed.

The most important takeaway from this process is that Florida uses the committee to select the appropriate scenario from all of the alternative scenarios presented by national economic forecasting services. The assumptions of the national forecast are then inserted into equations developed by the Legislative Office of Economic and Demographic Research. All principals have to agree about assumptions on such things as the level of employment, housing starts, population growth, personal income, personal consumption, and tourism. Then, revenue estimates are separately made for all taxes; each revenue source is then debated and agreed to at a subsequent committee meeting.

The product of the committee is a "Long-Range Financial Outlook" statement that identifies the official revenue forecasts not only as to amount but also whether they are recurring or nonrecurring. The nonrecurring revenues can be used only for one-time expenditures or placed in the state's reserve fund, thus helping to prevent the state from over committing to continuing programs or passing tax reductions with delayed effective dates.

This process has resulted in more accurate revenue forecasts. Moreover, it has the added advantage of not politicizing the process with lengthy and fruitless debates in House and Senate appropriations committees over whose revenue estimates to accept. Finally, this process creates a forum for challenging the assumptions used in the forecasts. Importantly, the committee sessions and discussions are open to the public, which can also offer useful information.

Ohio could improve its revenue estimating process and the budget process as well, if it were to eliminate the separate revenue estimating forecasts of the governor and the Legislative Service Commission and substitute consensus forecasting similar to that employed in Florida and most other states.

## **Democratizing Budget Development**

The preparation of the governor's Executive Budget Request is conceived in secrecy with no one knowing its contents until its official unveiling. The only reason there is an Executive Budget Request, formally consolidating the requests of individual state agencies, both independent and under the control of the governor, is because state statutes tell the governor exactly what the legislature wants in the budget request and how it should be prepared. Ohio has made appropriations since it became

a state more than 200 years ago, but it has had an Executive Budget Request for only half of that time. The statutes governing its content and development have been altered on several occasions.

The idea of an Executive Budget Request emerged as a substitute for a state budget system that, by the turn of the 20th century, had gone completely out of control. Agencies bargained directly with the state legislature for their appropriations, and the governor had no central control over the process. This free-for-all system meant there was much departmental logrolling, no central fiscal coordination to make expenditures meet anticipated revenues, and frequent deficits to be covered by the legislature in an ad hoc fashion. The intent of the Executive Budget Request was to remedy this chaotic system by making the governor responsible for presenting the legislature with an integrated, consolidated, single state budget with the executive's recommendations for the amounts to be given to each agency, as well as recommendations on how to pay for the budget in total. As it is, this goal has never truly been met.

The independently elected officials, the legislature, judiciary, Attorney General, Auditor of State, Secretary of State, and Treasurer of State, present their budget requests without executive alteration. Large areas of spending, notably primary and secondary education, present their budget requests through independent authorities. Nevertheless, all agency requests are integrated into a single balanced whole under an Executive Budget Request. The legislature then considers the package as presented by the governor rather than weighing the individual departmental budget requests that were submitted. Missing in the legislative analysis is the benefit of rigorously vetting the relative value of the budget requests of competing programs and activities.

Despite the fact that the Executive Budget Request is a significant improvement over the budget process it replaced does not mean that it must be conceived secretly without legislative or public input. The legislature could, in fact, require such input if it considered it to be desirable.

There are arguments both for and against opening up the executive budget development process. Dr. Howard Miller, a professor at Syracuse University and a political budget staff appointee of former New York Governor William Averill Harriman wrote a series of articles entitled "Behind the State Budget" for the *Albany Times Union*. In one article, he made a strong case for maintaining secrecy in the development of the state executive budget. In summary, his arguments were:

- Allowing separate releases of information from agencies before the formulation of a unified executive budget would distract the public and legislatures from the job of adopting a budget that balances all of the interests represented by it.
- Department heads appointed by the governor must demonstrate administrative loyalty and support the governor's final decisions, even if he recommends a lower level of program financing than they originally requested.
- Release of information about inflated departmental budget requests in advance of the release of the governor's budget would pit appointive department heads against the governor for leadership over public policy in the public eye.
- Advance public disclosure of agency budget requests would ensure a larger state budget than under a system of internal budget negotiations.
- Executive budget hearings need to be freewheeling; the presence of the public or legislators would hamper free and open discussions.
- If budget requests and executive budget hearings were made public, every administration would

develop ways of circumventing the process, and the budget requests and hearings would become simple window dressing.

One argument that Professor Miller did not make was the one usually advanced in favor of secrecy: the principle of separation of powers. He did not raise it because he recognized that, historically, none of the framers of the national or state constitutions envisioned complete separation of powers. Instead they sought a balance of powers. Thus, there are requirements for legislative confirmation of certain appointments and the executive veto. What the constitutional framers feared most was a strong executive, and thus they sought instead to lodge policymaking and appropriations powers in a representative legislative body. Therefore, the separation of powers argument used in the context of supporting secrecy in budget preparation is a specious one. A good case can be made for opening up the process to more public and legislative scrutiny, if not participation.

What might happen if representatives of the public and/or legislators and their staff were allowed to attend executive budget hearings is that sounder and more supportable public policy and budget decisions would result. Many good policy ideas work their way up through the agency budget development process, including ideas for changing the course of a program, eliminating it, or starting a new one. Many of these, perhaps most, are eventually abandoned for political or budgetary reasons, not because they are bad policy. Allowing the public to hear the details about these proposals would enable them to be resurrected during legislative consideration of the budget.

Although Ohio publishes information about the requests made by agencies not included in the Executive Budget Request, there is usually insufficient time during legislative budget hearings to dredge up the details needed to reconsider them. If there is no interested party to bring the issue to the attention of the legislature, including its own staff, then the matter simply will not be considered. A good deal of important public policy is never brought forth for legislative discussion because of this lack of information and time.

It is also the case that an executive budget hearing serves as the instrument for a thorough review of agency performance during the preceding biennium. This kind of review is generally much more complete than when it occurs during a legislative budget hearing, where it is in the interests of the executive branch to circle the wagons against outside attacks. Public and/or legislative participation in the performance review conducted by the executive branch could lead to important budgetary and policy changes with the final result being greater public accountability for the expenditure of public funds.

On balance, there is more to be gained from an open executive budget development process than the possible negative outcomes it may produce. Under the more secretive process, the governor has the upper hand because the executive controls access to vital policy development information that should be available to legislators in weighing the merits of new policies.

## **Improving the Legislative Appropriations Process**

The part of the budget process where the General Assembly reviews the Executive Budget Request in order to reach spending decisions formulated in an appropriations bill is the place where the public

has its greatest, and sometimes only, opportunity to influence spending decisions. Yet, as this process has evolved, it has become less open to public scrutiny and accountability.

## Openness in the Appropriations Process

Budget hearings on the several operating appropriations bills begin in the subcommittees of the House Finance Committee. The subcommittees hold public hearings with the agencies that explain and defend their budget requests. Then, separate hearings are held for testimony from other interested parties. The hearings are not recorded, and minutes are not transcribed in great detail. News reporters may attend budget hearings, but few report on them. Two paid subscription news services, Gongwer and Hannah, attend and regularly report on the hearings. Since they cover hearings in all committees, however, their coverage of budget hearings is necessarily limited and only available to its paid subscribers. Thus, the best and sometimes only way to find out what happened during a budget hearing is to be there. However, budget hearings are not public in the sense of offering an opportunity for ordinary citizens to express themselves on tax and spending matters.

Another important aspect of a legislative budget hearing is the lack of legislative attendance. Initially, in order to hold a hearing, there must be a quorum of members in attendance, defined under chamber rules as being a majority. However, once the roll is taken, legislators begin to drift out of the hearing room. It is not unusual to witness a hearing on a budget proposing to spend hundreds of millions of dollars with only the chair and ranking member of the subcommittee present to listen to the request.

**Public Involvement.** Most decisions about appropriations levels are made during the subcommittee hearings. The full House Finance Committee usually hears initial agency testimony on the large state agencies, but then decision-making is delegated to the subcommittee charged with responsibility for that agency's budget. Thus, for the public, the subcommittees of the House Finance Committee are especially critical. Senate Finance Committee and subcommittee deliberations follow a similar pattern. However, the Senate Finance Committee focus is given primarily to the largest state agencies and issues because the Senate committee has fewer members as well as less time than the House Finance Committee to conduct the hearings. Ideally, legislative budget hearings would give the public the opportunity to express opinions on spending priorities. Unfortunately, public input at this point is quite limited.

Anyone can, of course, attend a public budget hearing. However, when it comes to the participants, they are all paid to do their jobs resulting in a *pro forma* process. The hearings are conducted by legislators assisted by their staff. State employees testify in favor of their budget requests. Paid representatives of those constituents who are the subject of the budget hearing testify on behalf of those who benefit from the programs. It is rare that someone not paid to be at a hearing testifies, and when this testimony occurs it is usually meant to advance a strategy that a lobbyist believes will gain legislative attention. These dynamics mean that everyone has a personal stake in the outcome of the appropriations process that goes beyond the merits of individual budget proposals. Supporting a tax increase to support increased spending could cost a legislator their job. Failing to gain legislative approval for a spending item could result in a constituent representative losing their job, or losing prestige, a bonus, or a client in the case of advocates representing multiple interests. The general public has very little participation in decision-making involving the expenditure of billions of their tax dollars each year.

**Importance of Budget Hearings.** Despite the lack of general public involvement, legislative budget hearings could be made more citizen-friendly if minutes of meetings were more detailed. House



and Senate rules require that minutes of committee proceedings only need to include the barest of information: a record of member attendance, motions and votes, plus the names of persons speaking before the committee, and whether the persons are proponents, opponents, or interested parties, and the names of the persons' firms, associations, or corporations on whose behalf they appeared.

Another useful reform would be to actively solicit the opinions of the general public about spending priorities. States such as Oregon and Washington have pioneered processes where public opinion about spending priorities is not only sought, but later used in budget development, including the appropriations process.

**Lack of Openness in Budget Hearings.** Much of what goes into the appropriations decision-making process occurs outside of the open public budget hearings. Every participant in the process is somewhat jaded about the games that occur during the hearings. In every budget, there are winners and losers, regardless of budget restrictions. Even when a budget is cut many times, the legislature still increases some programs above the amount the governor requested, and new programs are still started that the governor did not request. The reality is that most of these decisions are made outside of the budget hearing process and outside of public view. Clearly, a great deal of the budget process is external to its formal process. A remedy is to restore total openness to the appropriations decision-making process and ban private meetings for the purpose of making those decisions, although this would be impossible to enforce.

**Lack of Openness in Conference Committee.** The conference committees for the state's main operating appropriations bills use an especially egregious process. Not only do the committees keep the public in the dark about their deliberations as they seek to resolve differences between the House and the Senate on every single appropriations line item, but they also exclude state agencies, advocates, and other paid budget process participants.

In theory, state budget conference committee meetings are open to the public. In reality, the conferees, and usually only those from the majority party, meet privately to decide their actions before convening a public meeting of the conference committee. The governor, generally through the Office of Budget and Management Director, often weighs in at this stage as well. At these "pre-meetings," actual decisions are made. Under these circumstances, the public meetings are nothing more than a staged presentation of predetermined, private decision-making. If legislators would follow their own rules, the process would be made more open and democratic.

Even legislators have difficulties accessing budget information about the conference committee's version of the budget. The state's main operating appropriations bill runs thousands of pages in length, and the conference committee typically makes hundreds of changes in its provisions. Yet, legislators are asked to vote on those changes with no opportunity to read its provisions. Votes are taken in the House and Senate without a new version of the appropriations bill even being available to read, assuming that the time between the conclusion of conference committee deliberations and the votes, usually a day, was sufficient to read the new bill. Instead of receiving a new version of the appropriations bill, legislators are given a list of amendments as adopted by the conference committee, usually to the latest version of the bill. To understand it, a legislator would have to lay that bill alongside the several hundred pages of amendments and read the two together to truly understand what the conferees had done. The actual revised bill on which legislators are to vote is not even prepared until weeks after it has been enacted.

Many states require a “cooling-off” period before a final vote is taken on legislation. In these states, legislators are only allowed to vote on a bill, including the budget bill, after they have had it in front of them for several days. Legislators are therefore hard pressed to deny knowledge of the contents of bills they vote upon, as has happened many times in Ohio after conference committee reports are reported and votes taken. Requiring a final copy of the appropriations bill, and a cooling-off period before a final vote is taken, would be a beneficial reform to the state’s appropriations process.

## **Biennial vs. Annual Budgeting**

According to the National Conference of State Legislatures (NCSL), the trend among states during the last 50 years has been to switch from biennial to annual budgeting. Whereas 41 states had biennial budgets in 1940, only 20 have them now and, of these states, Ohio is the second largest. The NCSL cites as reasons for the switch to annual budgets the increased complexity of state finances, the importance of federal actions that occur annually on state budgets and, most importantly, the dependence of states on the individual income and sales taxes that are less stable revenue sources than was previously the case.

One of the main advantages of an annual budget is that the state would be able to forecast revenues and anticipate expenses with greater accuracy one year in advance rather than two years, as is the case currently. Annual budgets are also more flexible. Financial problems occur continuously, not once every two years. A biennial budget, based on a two-year revenue estimate and spending forecast, is more rigid and less suited to accommodating necessary change.

Furthermore, in addressing fiscal issues occurring after the biennial budget is adopted, the legislature does so in isolation of what is going on throughout state government and in all its programs. Supplemental budget requests for education or Medicaid are not placed in the correct context of a total budget as they should be, and as they are with annual budgeting when the need for supplemental budgets is reduced or eliminated. Moreover, consideration of supplemental budgets can be nearly as time consuming as a full annual budget request. More often, by continuing the practice of biennial budgeting, flexibility and decision-making is effectively transferred to a handful of legislators operating through the state’s Controlling Board and the executive branch of government, raising serious constitutional questions.

An advantage of biennial budgeting is that it effectively removes the budget from the election cycle. An even bigger advantage cited for the use of biennial budgets is that it would seem to be conducive to long-term planning. However, a study of the subject by the Council of State Governments could neither confirm nor reject this argument. Subsequent studies by the faculty of Texas A&M University and the U.S. General Accounting Office reached the same conclusion.

Even if the only advantages were more accurate revenue and spending forecasts, changing to annual budgets would be a worthy recommendation for Ohio to undertake. The NCSL report concluded, “As one would expect, the consensus is that forecasting is more accurate in states with annual budgets. Accuracy in forecasting, in turn, reduces the need for special sessions of the legislature, supplemental appropriations, and reserves.”<sup>6</sup>

Existing state law permits the state to switch to annual budgets; no statutory change would be needed. The reason Ohio has a biennial budget is historical. In the early 1900s, the state began to have biennial

legislative sessions because it was difficult to convene legislators more frequently, and also because legislative business was comparatively light. Today, the state has a very complex and diverse economy with legislators meeting annually and in session almost year-round. As a result of these changes, there is little reason to continue biennial budgets.

Governor John Kasich's Mid-Biennium Reviews contained a myriad of public policy changes as well as budget corrections. This new process may signal a de facto move, if not an actual one, by Ohio to annual budgeting.

## Improving Spending Transparency

Ohio is a leader in the area of government spending transparency. In December 2014, State Treasurer Josh Mandel instituted the "Ohio Checkbook" providing online detailed information on state government finances. With numerous charts and graphs, the online checkbook provides information on state expenditures in an extremely user-friendly format. Its database is searchable by agency, employee, and type of transaction. However, tax refunds, public assistance payments, and employee paychecks are not included in the online checkbook because of privacy restrictions.

Between 2014 and 2015, the Public Interest Research Group elevated Ohio's ranking among the states in spending transparency from 46th place to 1st because of the development of the online checkbook, a ranking that it retained the following year. No sooner had work been completed on the initial online checkbook when Treasurer Mandel began to encourage Ohio's local governments, school districts, and pension funds to add their financial information to the database. This effort, which was initiated in April 2015, has been partially successful, as more than 1,000 local governments and schools posted their financial information on the online checkbook by January 2017, with additional entities added since this time.

While progress with the online checkbook is commendable, the effort to bring Ohio local governments onboard is voluntary and still only includes barely one quarter of all such entities. A statutory change to require compliance is needed to ensure that the database is comprehensive in scope. It would allow data to be analyzed in a much more meaningful way than is possible under the current voluntary system. Legislation to this effect has passed the Ohio House of Representatives on two separate occasions but has fallen short in the Ohio Senate.

A similar effort, "Ohio's Interactive Checkbook," was launched by the Ohio Office of Budget and Management in June 2016. It also contains information on revenues and agency budgets and expenses, and has a searchable database, although it does not have a local government component. Developmental costs for the Office of Budget and Management product of approximately \$150,000, exclusive of staff time, were significantly less than the online checkbook developed by the Treasurer's office, which cost \$811,000 to set up plus staff time.<sup>7</sup> Ohio would be well served if these two projects could be integrated into a single product.

Auditor of State Dave Yost has developed a tool to help Ohio counties and cities avoid fiscal stress. The online tool, which mirrors similar efforts developed in the states of Michigan, New York, and Washington, twice annually provides information on 17 separate "financial health indicators." It categorizes all counties and cities on each of the indicators as having a "positive outlook," a "caution-

ary outlook,” or a “critical outlook.”

In the initial report released in January 2017, 82 percent of counties and 92 percent of cities were flagged as having at least one indicator noting either an area of caution or a critical shortcoming. Several areas of general concern were noted by Auditor Yost. Counties and cities have not spent sufficiently on capital assets in recent years, and year-end general fund balances have been on the decline. These developments are perhaps not surprising given recent cutbacks in state support of local government. However, it could be quite useful ammunition against those arguing for further cuts to local government. The tool could have increased value if it could include Ohio villages and townships as well as counties and cities in the future.

## Where Ohio Stands

Does Ohio have the ability to effectively and accurately chart its fiscal course and make the corrections needed to meet the challenges that it will inevitably face during the 2020s and beyond? This is a question without a simple answer, as it is dependent upon a number of factors, although many are interrelated. The Center on Budget and Policy Priorities has identified both strengths and weaknesses in state fiscal tool chests, ranking Ohio as only average in this regard at 24th. It cited as positives the presence of a legislative fiscal office and its preparation of fiscal notes, regular budget status reports, a well-designed rainy-day fund, and the oversight of tax expenditures and state pension systems. The state has few peers when it comes to system integrity, including digitalization and budget transparency.<sup>8</sup> The *U.S. News* “Best States” study ranked Ohio as first in the nation on measures of both of these items.

The Center on Budget and Public Policy mentioned the lack of consensus revenue forecasts and multi-year forecasts as negatives. The lack of consensus forecasting is of particular concern. More than half (28) of states employ consensus forecasting for revenue forecasting. Twenty-two states forecast revenues for three or more years beyond the upcoming fiscal year.<sup>9</sup>

The study did not examine state tax structures, but Ohio’s increasing emphasis on sales transactions rather than income would also seem to be a shortcoming, one that will be exacerbated as the state’s population continues to age. The lack of future focus is certainly not helped by term limits which serve to narrow the horizon of members of the General Assembly. Developing more of a future orientation is essential to Ohio’s fiscal health, given the challenges that the state will likely confront on a whole host of policy dimensions.

## Budget Reform Realities

Despite the desirability of budget reforms, the reality is that Ohio’s budgeting process remains reactionary. Modifications will be undertaken only when there are strong proponents for change and when there are political rewards for undertaking such changes. Students of politics and of the budget process understand that the end result of budgeting is to determine who gets what and why, and ultimately, these are political decisions. In an economic sense, political decisions are irrational. The economic notion of rationality proclaims that an expenditure decision will be rational if it equates the marginal cost with the marginal benefit. Placed in a governmental context, this would mean that

the final dollar allocated for, say, primary and secondary education purposes should provide equal benefits with the final dollar allocated for building highways. Unfortunately, in government there is really no way of adding up all of a community's satisfactions and dissatisfactions and then striking a marginal balance between them in an economically rational fashion. Since most government services are given away, not sold, there is no way of assigning them market values, and without assigned prices, values cannot be objectively compared.

Dividing up the budget pot is ultimately a political process. Therefore, budget reforms that attempt to add greater rationality to the process might meet a rationality test but not a political test, and there is little or no political gain from supporting process changes. Elected officials benefit from actions that result in more money for their home constituencies or from the passage of legislation improving living conditions or solving extant problems, and not from creating a single integrated financial system.

These challenges are not to suggest that change is impossible but rather to recognize that change is most likely to occur when there are political advantages to be had and when there is strong leadership supporting it.

## Summary

The state budget can be analyzed from both a theoretical and practical viewpoint. Budgeting is, of course, a process. There is a budget cycle, which has four stages, the executive budget request, the appropriations process, budget execution, and auditing and legislative oversight. Budgeting must operate within certain limits. The Ohio Constitution and the Ohio Revised Code have many provisions that direct how the budgeting process must be carried out. There are also political influences and formal and informal agency practices that shape the budgetary process in Ohio.

Yet, budgeting is more than a process; it is a means of controlling spending, and through controlling spending, the legislative branch can hold the executive branch accountable for carrying out its will and the will of the public. Through the processes of authorizing expenditures and exercising oversight of the executive's budget execution, Ohio's legislature exercises a good deal of control over the state's financial policies, even with their terms limited to eight years.

Budgeting is inherently political. Budgeting decisions are irrational in an economic sense, but they have their own rationality. The governor and the legislature begin with a basic commitment to continue existing governmental services and activities and then consider additional spending alternatives. These incremental budget decisions exert the greatest political influence on elected officials. The outcomes are political in the sense that they are the product of consensus and bargaining.

The legislature has the constitutional authority to raise and appropriate revenues, but the budgeting process is a cooperative venture between the executive and legislative branches. Both branches participate in various stages of the budget cycle, and far more is to be gained through cooperation than through its opposite. State fiscal staff can help foster this cooperation by serving as a communication link between the executive and legislative branches of government.

Even though budgeting requires executive-legislative cooperation, it also is highly competitive and can be compared to a game. The competition for the outcome of budgeting, best defined as a share of state revenues, has rules, strategies, and other competitive elements that make it not dissimilar to chess. Access to it is limited through the restriction of information. A player must know a great deal, including how to access needed information, to be successful in playing the budget game.

Success in the budgeting game influences the relative power of the executive and legislative branches. Each biennium, the General Assembly makes numerous changes to the Executive Budget Request, and these changes clearly leave the legislature's imprint on the biennial budget. The legislature has taken other steps to establish itself as a more equal partner with the executive in budget making. It makes its own revenue estimates, it prepares fiscal notes on the fiscal effects of legislation using its own resources, and it has extended its oversight of the executive branch. However, there are areas of the budget-making process that deserve improvement.

Both the executive and legislative branches are hampered by faulty revenue estimates and a revenue-estimating process that fosters antagonism between the executive and legislative branches. The state fails to integrate the accounting and budgeting aspects of its financial system, making it difficult for the budget players, much less the public, to understand and make informed spending decisions. The state still budgets on a biennial basis, requiring many budget corrections and supplemental appropriations as well as delegating undue legislative authority to the joint executive-legislative Controlling Board. Both executive budget development and the appropriations process unduly restrict public access to critical budget decision-making. Exploring and then addressing these problems would result in an improved state budget process along with greater accountability for the expenditure of state resources.

## Endnotes

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- <sup>1</sup> Some material included in this chapter was presented in various essays in the series *State Budgeting Matters*, written by Richard G. Sheridan for The Center for Community Solutions during proceedings on the state's FY 2004–2005 and FY 2006–2007 budget. Those essays are available at [www.communitysolutions.com](http://www.communitysolutions.com).
- <sup>2</sup> Information about Hawaii's cohesive financial budgeting, reporting, and accounting system is derived from a report of the New York State Legislative Commission on Government Administration titled, "Reinventing Budgeting in New York State," dated October 1995. The report led to significant reforms of the New York budgeting, accounting, and fiscal information system.
- <sup>3</sup> *Managerial Cost Accounting Concepts and Standards for the Federal Government*, Statement of Recommended Accounting Standards #4, U.S. Office of Management and Budget. The word "government" is substituted for "federal" to suggest the most universal applicability of the statement to state and local governmental entities.
- <sup>4</sup> David Osbourne, "Reinventing Government: What a Difference Strategy Makes," January 2007.
- <sup>5</sup> Elizabeth McNichol, "Improving State Revenue Forecasting: Best Practices for a More Trusted and Reliable Revenue Estimate," Center on Budget and Policy Priorities, September 4, 2014.
- <sup>6</sup> Ronald K. Snell, "Annual and Biennial Budgeting: The Experience of State Governments," National Conference of State Legislatures, August 2002.

- <sup>7</sup> Andrew J. Tobias, "In Swipe at Josh Mandel, Pat Tiberi Says It's Crazy that Ohio Pays for Two Different State Websites Tracking State Spending," [cleveland.com](http://cleveland.com), April 3, 2017.
- <sup>8</sup> Elizabeth C. McNichol, Vincent Palacios, and Nicholas Johnson, "Budgeting for the Future: Fiscal Planning Tools Can Show the Way," The Center on Budget and Policy Priorities, February 2014.
- <sup>9</sup> Elizabeth McNichol, Iris J. Lav, and Michael Leachman, "Better State Budget Planning Can Help Build Healthier Economies," The Center on Budget and Policy Priorities, October 15, 2015.

