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STATE EXPENDITURES Projections to 2010

By

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STATE EXPENDITURES

Projections to 2010

The decisions to appropriate and expend public funds are always political choices. Some parts of the body politic will believe spending is too low in particular areas, while other parts will believe it is too high. What is actually appropriated and spent depends in a significant way on which parts of the body politic hold power. Hence any attempt to forecast such expenditures presupposes how political forces will interact in the budgetary process.

What is offered here are not expenditure forecasts, which require forecasts of political decisions that no one can make with reliability. Rather, expenditure projections are offered given certain basic and plausible assumptions. As a general matter, it is assumed that per capita expenditures for major areas in the South Carolina general fund budget remain constant in real (inflation-adjusted) terms. That is, the average expenditure per capita is constant at fiscal year 1997-98 levels after adjustment for inflation. In areas such as education, corrections, and various programs for the elderly, this assumption is modified so that expenditures are constant on a per capita basis for the affected segment of the population, that is, per pupil, per prisoner, and per person over age 65.

The expenditure projections presented are based upon the 1997-98 appropriations bill.¹ Because this analysis requires data for specific services/expenditures like Medicaid or the Education Finance Act, using detailed data is essential to the accuracy of the projections. The appropriations bill is the only available source of data at the program level, a level of detail appropriate to this project. Additionally, using appropriations as a measure of expenditures requires the assumption that the appropriations and the actual expenditures will be only nominally different, and therefore, the margin of error will be insignificant. This assumption is reasonable because departments and/or programs have every incentive to fully utilize appropriated funds.

Population Projections

The most important factor driving long-term demand for expenditures in the state is population growth. Of special interest is not only total population growth, but the growth of particular age cohorts, especially the school-age population and the elderly population. The school age population is approximated by the cohorts for ages 5-19 for K-12 population and ages 20-24 for the traditional post-secondary education population. The elderly population is encompassed by the cohort for age 65 and over. For the purpose of expenditure projections in this study, population projections from the U.S. Bureau of the Census are used (Table 1, Table 2).²

¹ General Appropriation Bill 1997-98, SC. Act No. 155 (1997).

² Campbell, Paul R., 1996, *Population Projections for States by Age, Sex, Race, and Hispanic Origin: 1995 to 2025*, U.S. Bureau of the Census, Population Division, PPL-47. "Table 4. Projections of the Population, by Age and Sex, for Regions, Divisions, and States: 1995 to 2025 - Series A (Preferred Series)".

Table 1
Projected Population by Age
South Carolina, 1995-2010

Year	Total	5-19	20-24	65 & over
1995	3,673,000	788,000	277,000	440,000
2000	3,858,000	828,000	254,000	478,000
2005	4,033,000	849,000	269,000	517,000
2010	4,205,000	842,000	289,000	584,000

Table 2
Projected Compounded Annual Population Growth by Age
South Carolina, 1995-2010

Year	Total	5-19	20-24	65 & over
1995-2000	0.99%	1.00%	-1.72%	1.67%
2000-2005	0.89%	0.50%	1.15%	1.58%
2005-2010	0.84%	-0.17%	1.44%	2.47%

Overall, the projections show that total population growth in South Carolina between 1995 to 2010 will be an annual rate of just under one percent, with that growth rate slowing somewhat in the first decade of the new century. The K-12 school age population is expected to grow a bit slower than the overall population growth, and a small decline in the K-12 school age population is projected for the period 2005-2010. Similarly, a decline in the population of the cohort traditionally in post-secondary education is projected for the period 1995-2000, with the population of that cohort projected to begin increasing again in the first decade of the new century.

The fastest growing segment of the South Carolina population is projected to be those 65 years of age and older. This cohort is expected to increase nearly twice as fast as the population as a whole through 2005 and beyond. Indeed, examination of projections for the years beyond 2010 indicate rates of growth of the population 65 and over of more than three times the rate of growth of the population as a whole.

Given the importance of these population projections for the analysis that follows, it is appropriate to ask how reliable these population forecasts are. The answer is that they are highly speculative. It is clear that the population of persons 65 and older will increase substantially in the United States in the early years of the next century as baby boomers reach 65. What is less clear is where these older persons will choose to live. Given the apparent attractiveness of South Carolina to retirees, one cannot rule out substantial in-migration of persons 65 and older to South Carolina. Hence, it is possible that the projections underestimate the future elderly

population for South Carolina. On the other hand, some demographers think that baby boomers will have fewer financial resources than the generation that preceded them and thus be less likely to relocate after retirement. For planning purposes and until better projections are available, the population projections used in this study represent the most reasonable expectation about the growth of the elderly population in South Carolina.

Similarly, projections of the primary school population are also speculative. Children who will be entering kindergarten after 2001 are not yet born. While the trend toward lower birth rates is expected to continue, one cannot be absolutely sure that birth rates might not rise. In-migration of young families could also increase school-age population. Accordingly this analysis assumes a slow but constant increase of one percent annually in the primary and secondary school population in these projections.

The traditional college age cohort is not as difficult to project as the primary school population, though speculation continues to taint these data. Unlike the primary school dilemma, the future 20- to 24-year-old population is currently living, which provides a firmer foundation for the projection. However, because this age group can be highly mobile, it is difficult to know where today's children will be in 2010.

General Fund Expenditure Projections

Education: Kindergarten Through Grade 12 (K-12)

Traditionally, expenditures on primary and secondary education represent the largest single component of the general fund budget in South Carolina. These expenditures in recent years have been driven largely by the Education Finance Act of 1977 (EFA) and the Education Improvement Act of 1984 (EIA), but the state outlays for education go back to earlier years. Total state appropriations for K-12 education for 1997-98 are \$1.4 billion, of which \$1.15 billion is direct aid to local school districts.

Much of the aid to school districts is allocated in accordance with formulas established in the EFA. The purpose of this act was to assure resources for a minimum foundation education in even the poorest school districts. Under the act, the state assumes funding responsibility for 70 percent of the aggregate statewide cost of the foundation program, although the formula is such that the state provides more or less than seventy percent to individual school districts according to their ability to meet fiscal needs. There is also a provision in the formula for weighting enrollment by grade level.

The foundation level, as defined by law, is a defined minimum program (DMP), established annually by the State Board of Education. Excluded specifically from the DMP are fringe benefits for employees, transportation costs, capital outlays, text books, food service, any pilot or experimental programs, and adult education. For 1997-98, the foundation requirement for the DMP was calculated at approximately \$1,836 per pupil. Hence, the state appropriation for 1997-98 is almost 70 percent of \$1,836 or \$1,285 per pupil.

In addition to funding under the EFA, the state also funds programs for school districts under the EIA. In 1997-98, funding was also provided to help offset employee fringe benefits and transport costs.

Projections of state expenditure requirements for K-12 education assume constant, real (inflation adjusted) per pupil expenditures (Table 3). Specifically, these assumptions include three percent annual inflation and a one percent annual growth rate in weighted student enrollment. If general fund real per pupil outlays for K-12 education remain constant, they can be expected to grow by about \$900 million by 2009-10. Even then, the state will be funding only about 30 percent of the estimated total cost (including fringe benefits, transport, amortization of capital facilities, maintenance, etc.) of the actual total cost of educating children in grades K-12 with the other 70 percent falling upon local property tax payers.³

Post-Secondary Education

Projections of state general fund expenditures for post-secondary education include appropriations for the state-supported colleges and universities, tuition grants for private colleges and universities, the technical education system, and administration of the Commission on Higher Education. These projections are based on maintenance of constant real per student expenditures at the 1997-98 level, assuming the enrollment in all the various post-secondary institutions grows at an annual compound rate of one percent. Maintenance of that level of funding effort will require an outlay of about \$1.1 billion in 2009-10.

At this writing, however, the basis for funding higher education in South Carolina is in a state of flux. New funding mechanisms are being devised by the Commission on Higher Education to replace a formula that was driven by full-time student equivalents. Full funding under the old formula would have required an outlay in 1997-98 of approximately \$963 million or about \$300 million in excess of the actual appropriation.

Table 3
Education Expenditures
(in millions of dollars)

	1997-98	2009-10
	Appropriation	Projection
K-12	\$1,442.2	\$2,309.0
Post-Secondary	672.9	1,077.3
Total	\$2,115.1	\$3,386.3

³ The local school district revenue forecast is addressed in further detail in *Local Revenue: Projections to 2010*, working paper 2 of this series by Holley Hewitt Ulbrich.

Corrections

Corrections, which includes operations and construction for the state prison system, juvenile justice, and probation and parole programs, has been one of the faster growing components of general fund expenditures in South Carolina in recent years. Despite a decline in the population of males age 18-30, the age cohort that is usually thought to track prison population, stricter sentences have caused the general prison population in South Carolina to increase. In 1997-98, the total appropriation for all correction-related activities was \$383 million.

In projecting corrections expenditures, note must be taken of the fact that the population of males age 18-30 in South Carolina is no longer decreasing and, indeed, is expected to increase at an annual rate of about 0.5 percent for the next ten years. It seems reasonable to assume, therefore, that the rate of growth in the prison population and other clientele served by the various corrections agencies will grow at a rate at least equal to growth of this male age cohort. Due to stricter sentences and the resulting rise in prison population, however, corrections expenditures are expected to grow even faster. Projected corrections expenditures, therefore, are premised on the assumption of a two percent annual growth rate in this client population plus three percent inflation.⁴

Corrections expenditures were projected to 2009-10 in four categories: operations (largely state prisons), juvenile justice, probation and parole, and new prison construction (Table 4). Current state projections on new prison construction only go through 2005-06. For purposes of this analysis, new prison construction after 2005-06 was extrapolated from earlier planned spending, but no such construction is planned at this writing. Taken in sum, projected expenditures for corrections will roughly double, growing from \$383 million in 1997-98 to \$729 million in 2009-10.

Table 4
Corrections Expenditures
(in millions of dollars)

	1997-98	2009-10
	Appropriation	Projection
Operations	\$282.1	\$506.7
Juvenile Justice	67.7	121.6
Probation	20	29.6
New Prisons	13.3	70.9 ^a
Total	\$383.1	\$728.8

^a Extrapolation of planned expenditures.

⁴ Client population growth based on discussion with State Budget and Control Board staff.

Medicaid and Social Services

Medicaid and social services, including various so-called welfare programs, also represent a relatively large portion of general fund expenditures in South Carolina. Because the underlying dynamics affecting growth in Medicaid are different from those for other social service programs, the two types of expenditures deserve separate consideration.

Medicaid is a state and federal matching funds program to provide medical services for those lacking sufficient resources to cover their own health care costs. Unlike Medicare, which is totally a federal responsibility, Medicaid requires state money—in South Carolina, about 28 cents for every 72 cents of federal money. Much of the state’s Medicaid responsibility is related to unwed mothers and the health of low-income residents. Medicaid is also a significant factor in funding long-term nursing home care for the elderly. For these reasons the state’s Medicaid obligations can be expected to track closely the number of births out of wedlock and the growth of the population 65 years and older.

After growing at rather alarming rates in the 1980s, the number of unwed mothers in the state began to level off in the 1990s and show some modest decline. With the age cohort of young women in the population growing slowly, it is reasonable to assume that there will be no dramatic increase in the number of unwed mothers through 2010. On the other hand, the cohort of persons in the population 65 and older is expected to be the fastest growing segment of the population. Even if the fraction of the elderly population requiring Medicaid support does not grow, the state’s aging population almost assures that Medicaid expenses will grow at one of the fastest rates of any element of the state budget.

Projections of Medicaid expenditures assume a rate of growth equal to inflation plus the annual rate of growth in the population of persons 65 years and older in South Carolina (Table 5). It could be argued that these projections are low because as people live longer, they are more apt to exhaust their savings and make greater demands upon Medicaid. If that were to happen, the Medicaid expenditures could be expected to grow faster than the rate of growth in the elderly population. Moreover, if large numbers of retirees of limited means migrate to and remain in South Carolina until death, Medicaid obligations could increase unpredictably. The big ques-

Table 5
Medicaid and Social Services Expenditures
(in millions of dollars)

	1997-98	2009-10
	Appropriation	Projection
Medicaid	\$333.2	\$602.3
Other Social Services	108.5	173.8
Total	\$441.7	\$776.1

tion concerns how many of these elderly in-migrants will return to their places of origin for nursing home care.

Other social services expenditures include all non-Medicaid programs of the Department of Social Services. The dynamics of expenditures for these programs depends in great part upon the success of welfare reform programs. Since 1994-95, state general fund expenditures for these programs actually have declined at an annual average rate of 5.4 percent. It is doubtful that such a decline will continue, and prudent expenditure projections must allow for some modest increase in the budget of the Department of Social Services. For purposes of projection, 1997-98 non-Medicaid social services spending was increased at the assumed rate of inflation plus the rate of population growth or four percent compounded annually. If welfare reform efforts prove successful, the rate of growth in non-Medicaid social services spending might be somewhat reduced below this level.

Taken together, there is some possibility that the 2009-10 projections for Medicaid underestimate growth and that those for non-Medicaid social services overestimate growth. On balance, however, the estimating errors are likely to be compensating, and hence, the totals appear to be reasonable projections of the combined Medicaid/social services expenditures required to meet legal obligations and maintain current levels of service in South Carolina. These projections suggest that the combined expenditures from 1997-98 to 2009-10 are likely to increase about 75 percent with most of the increase associated with growth in Medicaid.

State Aid to Local Governments

Three major state programs in South Carolina return funds to local governments: the Local Government Fund; the homestead exemption, which provides an exemption on the first \$20,000 of appraised value of owner-occupied residences for persons 65 years and older; and the property tax relief program, which provides rebates to fund a tax credit on school property taxes against the first \$100,000 of appraised value of owner-occupied residences with certain caps on school district millage. The obligations imposed upon general fund revenue by the first two of these programs are relatively easy to project. The property tax relief rebates, however, are much more difficult to project. The techniques and assumptions behind the projections for each program are discussed in detail below.

All other state funds received by local governments are included in either state budget line items or the all other spending category. Such funds include reimbursement for the merchant's inventory tax, direct appropriations for counties, and state grants.

Local Government Fund. By far, the easiest obligation to project is the Local Government Fund portion of state-shared revenue. The Local Government Fund was put in place when the General Assembly abandoned the process of sharing revenue from certain earmarked sources and simply set aside four and one-half percent of all general fund revenue off the top for refunding to counties and municipalities on a per capita formula basis. Since the allocation is based on revenue for the most recent full year in which actual revenues are known, the formula provides for an effective two-year lag. That is, the allocation for 1997-98 of \$173.6 million is based on

4.5 percent of actual general fund revenue for 1995-96. The projected Local Government Fund allocation for 2009-10 of \$323.6 million is based on projected revenue in 2007-08 (Table 6).⁵

Homestead Exemption. Projecting expenditures needed to cover the homestead exemption is a bit more complicated. There are no means tests for the homestead exemption: all persons 65 years of age and older qualify for an exemption from all property taxes (city, county, and school district) on the first \$20,000 of fair market value on an owner-occupied residence. Since almost all such residences now have an appraised market value greater than \$20,000, almost all principal residences of persons in South Carolina age 65 and over qualify for the exemption. The state returns to local governments the revenue lost as a result of this exemption.

If there is no significant shift in the percent of elderly persons owning their residence as opposed to renting, growth in state spending for the homestead exemption will be the rate of growth in the number of persons in the state who are 65 years and older. Hence, these spending projections are based on the projected rate of growth in that age cohort of the population. The projections in Table 6 show that expenditure growing from \$51.2 million in 1997-98 to \$64.1 million in 2009-10, with the rate of growth in the state's obligation increasing at an increasing rate as the population of the elderly grows rapidly late in the first decade of the new century.

Table 6
State Aid to Local Governments
(in millions of dollars)

	1997-98	2009-10
	Appropriation	Projection
Local Government Fund	\$173.6	\$323.6
Homestead Exemption	51.2	64.1
Property Tax Relief	209.8	335.9
Total	\$434.6	\$723.6

Property Tax Relief. Projecting state expenditures for the tax relief program is complicated. To understand this property tax relief program which applies to owner-occupied residences, it is useful to refer to the statutory language. As of 1997, the state rebates to school districts an amount sufficient to

fund a property tax exemption of one hundred thousand dollars based on the fair market value of property . . . calculated on the school operating millage imposed for tax year 1995 or the current school operating millage, whichever

⁵ See projected revenue based on analysis of revenue components in *State Revenue, Projections to 2010* by Holley Hewitt Ulbrich, working paper 1 of this series.

is lower, excluding taxes for bonded indebtedness and payments pursuant to lease purchase agreements for capital construction.⁶

The cap on millage makes provisions for certain exceptions. But in general, the Property Tax Relief Act, as amended, tends to reduce the role of reassessment in determining how much property tax relief is afforded. That is because another state law⁷ prohibits local governments from increasing their revenue by more than the rate of inflation plus a modest amount as a result of reassessment. In general, local governments respond to the increased property values resulting from reassessment by reducing the mill rate on property. The reduction in the mill rate seldom compensates completely for the increase in assessed value, however, and that complicates considerably the problem of trying to estimate further property tax relief funding requirements.

The law requires each county to reassess property on a five-year cycle. But that does not mean that one-fifth of the state's property is reassessed in any given year. Because the large counties tend to have larger proportions of the total taxable property in the state, the growth in the state's obligation for property tax relief will be uneven from year to year and will depend in part upon how much of the total eligible property in the state is reassessed in any given year. In 1997, for example, only about 12 percent of the taxable property in the state is due for reassessment, but in 1999, about 39 percent is scheduled for reassessment. Hence, the state's obligation under current law for funding property tax relief is not expected to increase significantly from 1997-98 to 1998-99, but is likely to jump significantly from 1999-2000 to 2000-01.

Because of all the complications involved in projecting the funding requirement for property tax relief, all projections are subject to considerable error. Attempts to model the process in all its complications have not proven practical for technical reasons. For this reason, property tax relief projections were prepared in accordance with the assumption that the state's property tax relief outlay grows at a rate of four percent compounded annually. This assumption accounts for a three percent annual rate of inflation plus a one percent annual growth rate in the total assessed value of eligible property due to population growth. This assumption would appear to be a conservative one, particularly with regard to the growth rate of new eligible property being added to the tax books. It is important to note that these projections are smoothed, that is, no account is taken of the step-like growth in the state property tax relief obligations associated with differences from year to year in the amount of property being reassessed (Table 6).

Debt Service

Debt service refers to the annual payment of interest and principal (generally into a sinking fund) on outstanding debt. The current year's general obligation debt service is \$150 million. As of this writing, the amount of debt service anticipated in the future was indeterminable. However, the legislature recently approved the issuance of \$2.15 billion worth of bonds, which increases the state's debt service requirements by \$172.4 million annually (assuming 20 years amortization and 5% interest) beginning in 1998-99.⁸ The debt service schedule of the State

⁶ SC Code of Laws, Sect. 12-37-251.

⁷ County Equalization and Reassessment. SC Code of Laws, Sect. 12-43-220.

⁸ The debt service schedule for this new bond issue was not available when the projections were prepared.

Treasurer’s Office sets debt service on current obligations for 2009-10 at \$13.1 million (Table 7). Thus, debt service in 2009-10 was projected to be \$185.5 million, the sum of these two components for debt service. Clearly, the intermediate and end year debt service projections are subject to change based on new issues and changes in the state’s debt retirement schedule.

Although no projections can be made in regards to future debt issuance, it is important to note that it is probable that additional debt will be issued during the period covered by this report. One indication of this likelihood is the new Transportation Infrastructure Bank, which has the authority to issue general obligation bonds to raise funds for qualifying state and local projects. Therefore, the debt service projections in this report are extremely conservative, and actual future debt service expenditures are likely to be higher.

All Other Expenditures

The five categories of expenditures detailed above—education, corrections, Medicaid and social services, state aid to local governments, and debt service—represent about 75 percent of all general fund appropriations in South Carolina in 1997-98. All remaining categories of general fund spending by state agencies are grouped together for projection purposes. Appropriations for these diverse programs in 1997-98 totaled \$1.1 billion. Projecting these miscellaneous expenditures at the rate of inflation plus the rate of population growth (that is, at a rate that would hold per capita expenditures in all other programs constant in real terms) yields projected 2009-10 spending of \$1.8 billion (Table 7).

A caveat is in order with regard to the projections of this diverse package of miscellaneous expenditures. In the future it may not be either possible or desirable to hold every line item in this set of expenditures to the rate of population growth plus inflation. For example, increased state law enforcement efforts can have the effect of causing court dockets to become seriously backlogged unless outlays for courts are also increased. On the whole, it would seem probable that increases in some line items within this group of expenditures could be accommodated without major effects on the total by reducing other items below the projected rate of growth.

Table 7
Miscellaneous Expenditures
(in millions of dollars)

	1997-98	2009-10
	Appropriation	Projection
Debt Service	\$149.9	\$185.4
All Other Spending	1,151.5	1,843.6

However, the possibility exists that some unidentified item in this group will necessitate faster growth in spending than the projections shown in Table 7.

General Fund Expenditure Projections

In summary (Table 8, Appendix 1), state expenditures are projected to grow at an average annual rate of 4.5 percent overall with faster-than-average growth anticipated in certain large segments of the budget like corrections and Medicaid/social services. It is believed that these figures provide a suitable foundation for planning purposes.

Table 8
Total General Fund Expenditures
(in millions of dollars)

	1997-98	2009-10
	Appropriation	Projection
Education	\$2,115.1	\$3,386.3
Corrections	383.1	728.8
Medicaid/Social Services	441.7	776.1
State Aid to Local Gov't	434.6	723.6
Local Government Fund	173.6	323.6
Homestead Exemption	51.2	64.1
Property Tax Relief	209.8	335.9
Debt Service	149.9	185.4
All Other Spending	1,151.5	1,843.6
Total	\$4,675.9	\$7,643.9

Appendix 1
Projected South Carolina Expenditures, 1997-98 to 2009-10
(in millions of dollars)

	1997-98 ^a	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Property Tax Relief	\$209.8	\$218.2	\$226.9	\$236.0	\$245.4	\$255.3	\$265.5	\$276.1	\$287.1	\$298.6	\$310.6	\$323.0	\$335.9
Homestead Exemption	51.2	52.1	53.0	53.9	54.8	55.6	56.5	57.6	58.6	59.8	61.1	62.5	64.1
Local Government Fund ^b	173.6	204.9	213.1	221.9	230.9	240.6	250.7	261.4	272.7	284.5	296.9	303.9	323.6
Corrections	383.1	410.6	447.8	482.0	504.8	528.7	553.7	580.0	607.5	636.3	664.2	695.8	728.8
Education (K-12 & Higher)	2,115.1	2,199.7	2,287.7	2,379.2	2,474.4	2,573.3	2,676.3	2,783.3	2,894.7	3,010.4	3,130.8	3,256.0	3,386.3
K-12	1,442.2	1,499.9	1,559.9	1,622.3	1,687.2	1,754.7	1,824.9	1,897.9	1,973.8	2,052.7	2,134.8	2,220.2	2,309.0
Post-Secondary	672.9	699.8	727.8	756.9	787.2	818.6	851.4	885.4	920.9	957.5	996.0	1,035.8	1,077.3
Medicaid/Social Services	441.7	461.7	482.6	509.5	527.4	551.6	577.5	605.0	634.7	666.5	700.3	736.9	776.1
Medicaid	333.2	248.8	365.2	387.4	400.4	419.6	440.2	462.2	486.2	512	539.6	569.8	602.3
Other Social Services	108.5	112.9	117.4	122.1	127.0	132.0	137.3	142.8	148.5	154.5	160.7	167.1	173.8
General Obligation Debt Service	149.9	292.8	288.6	300.0	273.4	279.3	258.3	250.9	243.2	229.5	216.6	221.5	185.4
All Other Spending	1,151.5	1,197.6	1,245.5	1,295.3	1,347.1	1,401.0	1,457.0	1,515.3	1,575.9	1,638.9	1,704.5	1,772.7	1,843.6
Total Expenditures	\$4,675.9	\$5,037.6	\$5,245.2	\$5,477.8	\$5,658.2	\$5,885.4	\$6,095.5	\$6,329.6	\$6,574.4	\$6,824.5	\$7,085.0	\$7,378.3	\$7,643.9

^a 1997-98 expenditures from appropriations act. Expenditure projections for later years are based on these appropriations.

^b Based on projected revenue by components; full formula funding assumed.