GUIDE TO THE ISSUES

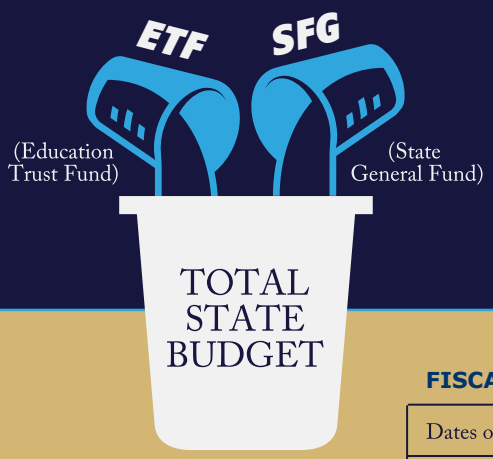
Follow the Money and See Where It Goes:

ALABAMA CITIZENS PAY FOR BIG GOVERNMENT

The government of Alabama is dependent on one thing for its survival: the tax dollars of Alabama citizens. In recent years, state government has taken in and spent more of Alabama's money than ever before. This expansion of government has been largely ignored. The purpose of this report, therefore, is to explain the current fiscal status of state government. Our goal is that the citizens of Alabama will know and understand the budgeting and financial processes of state government so that they can determine if lawmakers are acting in the people's best interest and advocate for change if they are not.

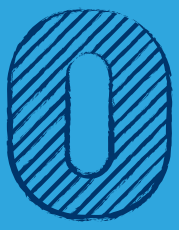
ALABAMA POLICY INSTITUTE

ALABAMA STATE FINANCIALS CHEAT SHEET



ALABAMA
has a bifurcurated budget
(**TWO SEPARATE** operating budgets)

	FISCAL YEAR	2019	2020	2021	2022
	Dates of Fiscal Year	10/1/18-9/30/19	10/1/19-9/30/20	10/1/20-9/30/21	10/1/21-9/30/22
	Year Legislature Approved	2018	2019	2020	2021
ENACTED BUDGETS	ETF	$6.633B	$7.125B	$7.217B	$7.672B
	SFG	$2.038B	$2.192B	$2.393B	$2.483B
	Total	**$8.671B**	**$9.317B**	**$9.610B**	**$10.155B**
ACTUAL REVENUE COLLECTED	ETF	$7.215B	$7.424B	$8.644B	
	SFG	$2.151B	$2.299B	$2.562B	
	Total	**$9.366B**	**$9.723B**	**$11.206B**	
RAINY DAY ACCOUNT AVAILABILITY	ETF	417.105M	431.174M	463.183M	469.132M
	SFG	187.161M	205.507M	222.234M	239.327M
	Total	**604.266M**	**636.681M**	**685.417M**	**708.459M**



No money from rainy day funds were used in 2019, 2020, or 2021 (even in the midst of a pandemic).

Total Alabama Trust Fund (which feeds rainy day accounts) balance as of 3/31/3021 was $3.221 Billion

The State of Alabama collected hundreds of millions of dollars over budget in FY 2019, 2020, and 2021.

EDUCATION
$4.5B

CARES ACT
$1.9B

AMERICAN RESCUE PLAN
$4.04B

Federal Stimulus Handouts Since 2020

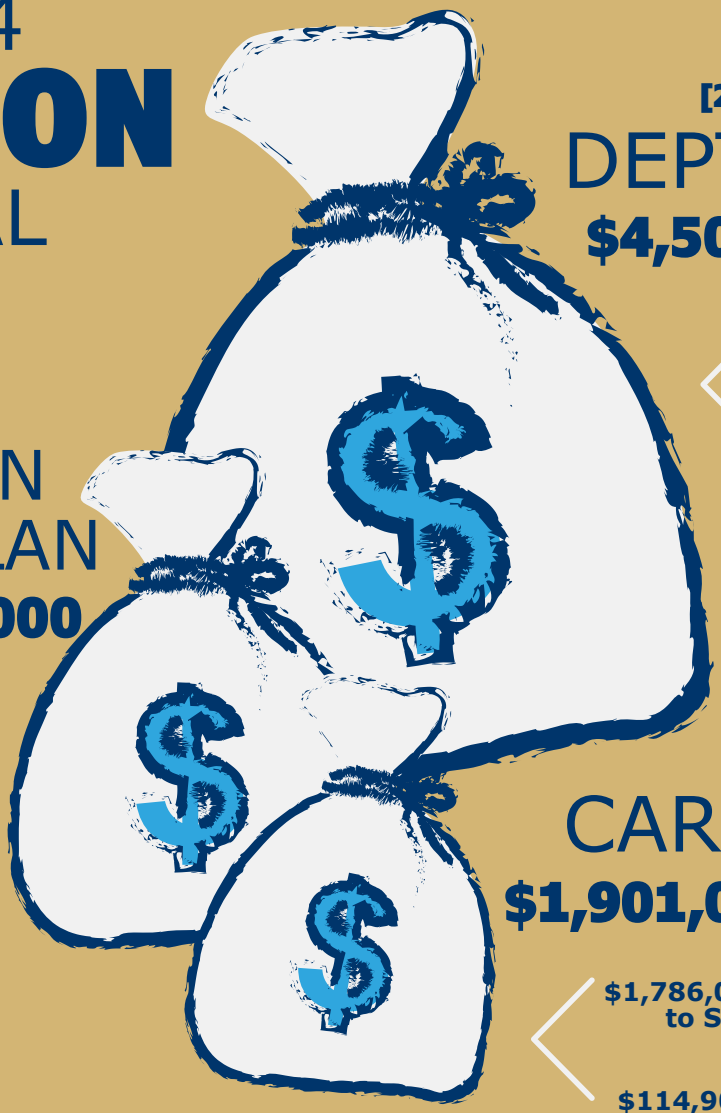
10.444
BILLION
TOTAL

[2020-2022]
DEPT OF ED
$4,500,000,000

- **$3,700,000,000 to K-12**
- **$1,300,000,000 to Higher Ed**

[2021-2022]
AMERICAN RESCUE PLAN
$4,043,000,000

- **$2,100,000,000 to State Dept.**
- **$1,900,000,000 to County/Municipal**



[2020]
CARES ACT
$1,901,000,000

- **$1,786,000,000 to State**
- **$114,900,000 to Jefferson County**

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I

INTRODUCTION

KEY TAKEAWAYS

- **In 2010 – after 136 years of Democratic Party control in Alabama – Republicans, once touted as the party of fiscal responsibility, took control of all aspects of state government.**
- **Since 2018, the legislature has raised taxes, increased spending to record levels, and sought new revenue streams.**
- **Republicans are outpacing the path Democrats were on in regard to government spending and growth.**
- **At the beginning of the current quadrennium, the total state budget was $8.7 billion. Legislators have increased that 17% in only three years to $10.2 billion. (That increase is 14.5% higher than the average inflation rate over the same period.)**
- **Legislators allocated over half (51.8%) of nearly $2 billion in CARES Act funds to state government, leaving citizens and the private sector behind.**

In the aftermath of the 2018 election cycle, Alabama Republicans declared that Alabama was seeing "one of the most conservative governments" in its history. One GOP campaign strategist claimed that newly elected Republicans were more right leaning than their predecessors, a representation of the increasingly conservative values of the state.[1]

Most Alabamians expect conservative fiscal principles from their elected officials. But far too often, that is not what they are getting. In the three years since the last election, the legislature has raised taxes, increased spending to record levels, and sought new revenue streams, such as legalizing medical marijuana and attempting to allow casino-style gambling in the state.

When the current quadrennium began, lawmakers inherited a combined education and general fund budget of $8.7 billion. In just three years they have increased spending to $10.2 billion, a 17 percent increase.[2] The increase is about 14.5 percent higher than the average inflation rate over that same period. And the budget increases do not correspond with population increases. From 2010 to 2020, 10 years, not three, Alabama's population only increased by just over five percent.[3]

Most Alabamians expect conservative fiscal principles from their elected officials. But far too often, that is not what they are getting.

Alabama taxpayers, many of the same people who thought they were voting for a conservative state government, are the ones paying for expanded government.

As the State of Alabama closes out fiscal year 2021 and heads into 2022, one thing is clear: state government is booming. While Alabama continues a brisk recovery from the COVID-19 pandemic, government is taking in and spending more money than ever. And by its nature, the state is choosing who benefits from that money. Despite record state revenues, elected officials are not satisfied. The 2021 Regular Legislative Session saw numerous efforts (both successful and unsuccessful) to take more money from Alabama taxpayers. This was on top of billions of dollars received by state government from a series of federal stimulus bills enacted to fight the health and economic impacts of COVID-19. And most "conservative" legislators still voted for those tax and spending increases.

But what are Alabamians getting for every dollar that is taken by state government in the form of taxes or spent via gifts from the federal government? Ultimately, citizens being taxed are not necessarily receiving a proportional share of the benefits. Most of it goes back into the public sector and to those who receive public benefits. The private sector receives very few of its tax dollars back.

This is especially clear in the state's use of CARES Act funds. The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) was the first in a series of federal stimulus bills legislated in response to the 2020 coronavirus pandemic and sent nearly $2 billion directly to Alabama.[4] For months much of the money went unspent and was not used to help struggling Alabamians when they needed it the most. When it was eventually spent, over half (51.8%) went back into state government.[5] The small amount distributed to the private sector came through the form of grants, allowing government to pick the winners and losers.

This disparity was not necessarily because Alabama's lawmakers did not want to try to help, but their delayed actions would leave you to think there was no real COVID-19 economic crisis in Alabama.
The same theme follows with recently enacted and proposed state revenue engines. In 2019 the state approved a perpetual gas tax increase that leaves much discretion to the governor as to how those funds are spent – again allowing government to choose who benefits – and leaves you paying more at the pump.

The 2021 Regular Session saw the legalization of medical marijuana, which could boost state revenues significantly. But medical marijuana will not operate under a free market approach, rather the state will again determine who can grow, process, distribute, and sell these products, meaning a financial windfall for the state and the select few who are chosen to participate in the process.[6]

2021 also saw another failed attempt at legalizing expanded casino-style gambling and creating a state lottery, which could generate hundreds of millions of annual revenues for the state. Other arguments aside, lawmakers once again clearly ignored free-market and limited government principles by stacking the deck in favor of casino operators that already had facilities within the state.[7]

There are more examples, but the main theme remains the same. Despite already booming revenues, state government wants to determine the beneficiaries of revenue and spending windfalls. Choosing beneficiaries is simply the nature of government: it taxes all individuals, takes some for its own operating costs, and then extends it to those it determines should get funds. In this operation, the government is never not a beneficiary itself. With an incentive to grow, the government inevitably does. It then expands into most aspects of daily life, including the free market. It also means a greater reliance on federal government, which Alabama becomes increasingly dependent on as both federal and state programs expand.

America was founded on the concept of limited government. The erosion of the principles of federalism at the national level have trickled down to state governments, including Alabama. That does not mean that all hope is lost though. In 2010 – after 136 years of Democratic Party control in Alabama – Republicans, once touted as the party of fiscal responsibility, took control of all aspects of state government. But in terms of spending, Republicans are outpacing the path Democrats were on expanding the scope of government in the party's final years controlling the State House.

As Alabama begins fiscal year 2022 and begins planning for the 2023 budget cycle, there is an opportunity for the state to return to the limited government, fiscally responsible roots that flipped control of state government just a decade ago. But it will take strong leadership and courage from a coalition of current lawmakers or a generation of new lawmakers that want to change the status quo and transform state government to be less invasive in the lives of all citizens.

II

ALABAMA BUDGET PROCESS

KEY TAKEAWAYS

- **Alabama uses what is known as a bifurcated budget system, meaning the state has two separate operating budgets: one for education and one for everything else.**
- **Both the ETF and SGF have rainy day funds from which money can be transferred if proration is declared in either account.**
- **Rainy day funds were not used in the height of the COVID-19 pandemic. If COVID-19 was not a "rainy day," then what is?**
- **The last time that either Alabama budget was prorated – i.e., had funding cuts – was the SGF in 2012. This is not because of fiscally sound governing. Rather, it is because the state has consistently had more money available than ever.**
- **If the legislature was taking in the minimum amount necessary to provide only for the essential functions of government, then the need for proration and use of reserve funds would be more common.**

Bifurcated Budget System

Before discussing the current fiscal state of Alabama's government, it is important to know more about the unique system under which the state operates. Alabama uses what is known as a bifurcated budget system, meaning the state has two separate operating budgets: one for education and one for everything else. Each budget has separate revenue streams that are dictated constitutionally and statutorily. Alabama is one of just three states that has two separate operating budgets. [8]

Alabama's bifurcated budget process dates to 1927 and then-Governor Bibb Graves. Graves pointed to Alabama's struggling education system as a need to setup a dedicated budget and revenue stream for those programs.[9] In some ways though, the two-budget structure was set up to limit the powers and responsibilities of the legislature itself. Programs identified as priorities, like education, will always have substantial funding and there is little that lawmakers can do to obstruct that.

Alabama is one of just three states that has two separate operating budgets.

As recently as 2015, the size and revenue streams of the Education Trust Fund (ETF) and State General Fund (SGF) Budgets were generally equal with each accounting for around 50% of spending and revenue. However, in the last decade that trend has changed. For FY 2022, the ETF is projected to consume 75.5% of state spending, with the SGF accounting for 24.5% of the state's $10.2 billion in total spending.[10]

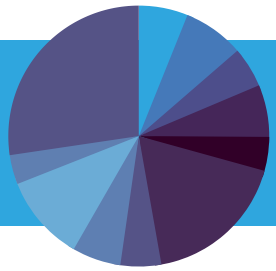
As noted previously, the two funds also have separate dedicated revenue streams, which account for the growing disparity between the size of the two budgets. The ETF's two main revenue streams are state income and sales tax receipts. In FY 2020, 91% of ETF revenues came from these two sources. The SGF depends on a greater number of revenue streams to fund its activities. In 2020, the largest sources of SGF revenue were insurance company taxes, use taxes, property taxes, cigarette taxes, alcoholic beverage taxes, and the Simplified Sellers Use Tax (online sales tax). Other combined tax provisions provided more than a quarter of revenues to the SGF.[11]

A bifurcated budget process with statutory earmarking – i.e., funds only going toward enumerated purposes – presents several challenges to state government. First, it means that state budgets are much more susceptible to downturns in the economy. With the ETF so dependent on income and sales tax receipts, a sudden economic decline could mean that there are less funds available and the budget faces a shortfall. Because of Alabama's balanced budget requirement, this would force the state to make across the board cuts known as proration. Since the SGF relies on smaller revenue streams, it too runs the risk of a shortfall and proration. In the 32-year span from 1980-2012, the ETF was prorated 11 times while the SGF faced cuts 8 times. The last time that either Alabama budget was prorated was the SGF in 2012.[12]

Alabama's current budget system also means that lawmakers have little flexibility when one fund falls short of revenue projections. A 2018 report from Alabama's Joint Task Force on Budget Reform estimated that 93% of all state revenues are earmarked.[13] In contrast, the National Conference of State Legislatures has estimated that the national average is less than 25%.

Having two separate and heavily earmarked budgets makes it much harder to reprioritize revenue when there is a deficit in the SGF or ETF. It also makes budgeting more expensive and resources less likely to be efficiently managed due to inflexibility of the budgets. Regardless, as government spending continues to rise, state revenue sources will face increased risks of budget shortfalls.

SGF Revenues



6.09%	Alcoholic Beverage Taxes
7.55%	Property Taxes
5.00%	Alabama Trust Fund
6.46%	Cigarette Tax
4.19%	Corporation Taxes
17.92%	Insurance Co. Taxes
5.05%	Sales Tax
6.04%	Simplified Sellers Use Tax
10.71%	Use Tax
3.64%	Lease Tax
27.34%	All Others

ETF Revenues

91% come from Income & Sales Tax

Rainy Day/Reserve Funds

The state does have backstops in place to minimize the impacts of a shortfall in either the ETF or SGF. Both the ETF and SGF have rainy day funds from which money can be transferred if proration is declared in either account. The ETF also has a rolling reserve fund that can be utilized if additional money is needed to close a budget gap.

The ETF rainy day account was created in 2002 by Amendment No. 709 to the Alabama Constitution. In 2008, Amendment No. 709 was repealed and replaced by Amendment No. 803 which reestablished the ETF rainy day account and created a new rainy day account for the SGF.[14] Both funds are financed through the Alabama Trust Fund which was established in 1985 and receives revenue from the sale of offshore oil and gas drilling rights and the resulting royalties from gas production.[15]

Under the Alabama Constitution, 6.5% of the previous year's ETF appropriation can be transferred to the ETF from the rainy day account to cover a shortfall. For FY 2022 that would mean that up to $469.1 million will be available if proration is declared.[16] Borrowing from the ETF rainy day account must be paid back within six years. For the SGF, up to 10% of the previous year's appropriations can be transferred from its rainy day fund if proration is declared. SGF transfers must be repaid within a decade. At least $239.3 million will be available for transfer in 2022.[17]

An additional backstop includes the Education Rolling Reserve Act of 2011 which created an appropriations cap within the ETF and required that any ETF revenues above that cap be transferred into the Education Trust Fund Budget Stabilization Fund created by the law.[18] In the event that proration is declared for the ETF, an amount totaling the estimated budget deficit can be withdrawn from the stabilization fund, though it must be paid back to the fund within 30 days of the end of the fiscal year for which proration was declared. The Finance Department can also temporarily borrow funds from the stabilization account during the first six months of the fiscal year. Temporary borrowing must be paid back within 90 days of the original transfer.[19]

As previously noted, state government has not faced a budget shortfall or been forced to tap into either rainy day fund since 2012. This may sound like a good thing, but this may not be the case. Alabama has not avoided proration because of fiscally sound governing. Rather, the state has had more money available than ever. If a rainy day fund was not needed during the height of the COVID-19 pandemic, when would it be?

Government is necessary to carry out functions that are ill-suited for the private sector. But at the end of the day the primary goal of the legislature should be to protect the rights of and take less from citizens and be good stewards of the resources that government does take. If the legislature was taking in the minimum amount necessary to provide those essential functions of government, then budget shortfalls would be more common. They would also be smaller and easily covered by balances in the ETF and SGF rainy day accounts. As it currently stands, there is so much money flowing into state government that there is little use for a rainy day fund.

If a rainy day fund was not needed during the height of the COVID-19 pandemic, when would it be?

III

HOW DID ALABAMA DIVERT FROM ITS LIMITED GOVERNMENT PRINCIPLES?

KEY TAKEAWAYS

- **Larger revenue streams mean a larger government, and a larger government means that the state has more resources to engage in activities outside of its essential scope. For the past several years, the governor and legislature have continued to seek new revenue streams to increase the state's largesse.**
- **The legislature and governor went full speed ahead, despite great uncertainty amid the COVID-19 pandemic, to pass record high FY 2021 budgets. If not for the pandemic, spending would have only been higher.**
- **Lawmakers not only passed record-setting budgets each session, but also found time to put the state further into debt during the 2020 Regular Legislative Session: they approved a $1.25 billion debt spending package for education (which will cost the state $80 million/year in annual debt payments).**
- **The State of Alabama has been directly awarded $4 billion in additional stimulus funding from the CARES Act and American Rescue Plan. This doesn't include over $2 billion flowing directly to counties and municipalities, or the $4.5 billion going to the Department of Education. (This means "stimulus funds" alone have, in effect, doubled the size of Alabama's annual budget.)**
  - **Only 23.1% of CARES Act funds went toward the private sector.**
  - **Over half the CARES Act money has been used to support government, rather than citizens.**
  - **The Department of Education still plans to ask for an additional $800 million increase in the 2023 budget!**
- **During the pandemic, all aspects of state government remained essential – and most saw increased funding – while "non-essential" private sector jobs and businesses were forced to shut down for a time. Some never reopened.**
  - **State government proved unwilling to make the same sacrifices that it forced upon Alabama's private sector employees and businesses.**
- **Alabama literally has more money coming into the state now than it ever has in its more than 200-year history – it is drowning in cash. Yet, government only continues to seek more.**

III How Did Alabama Divert From its Limited Government Principles?

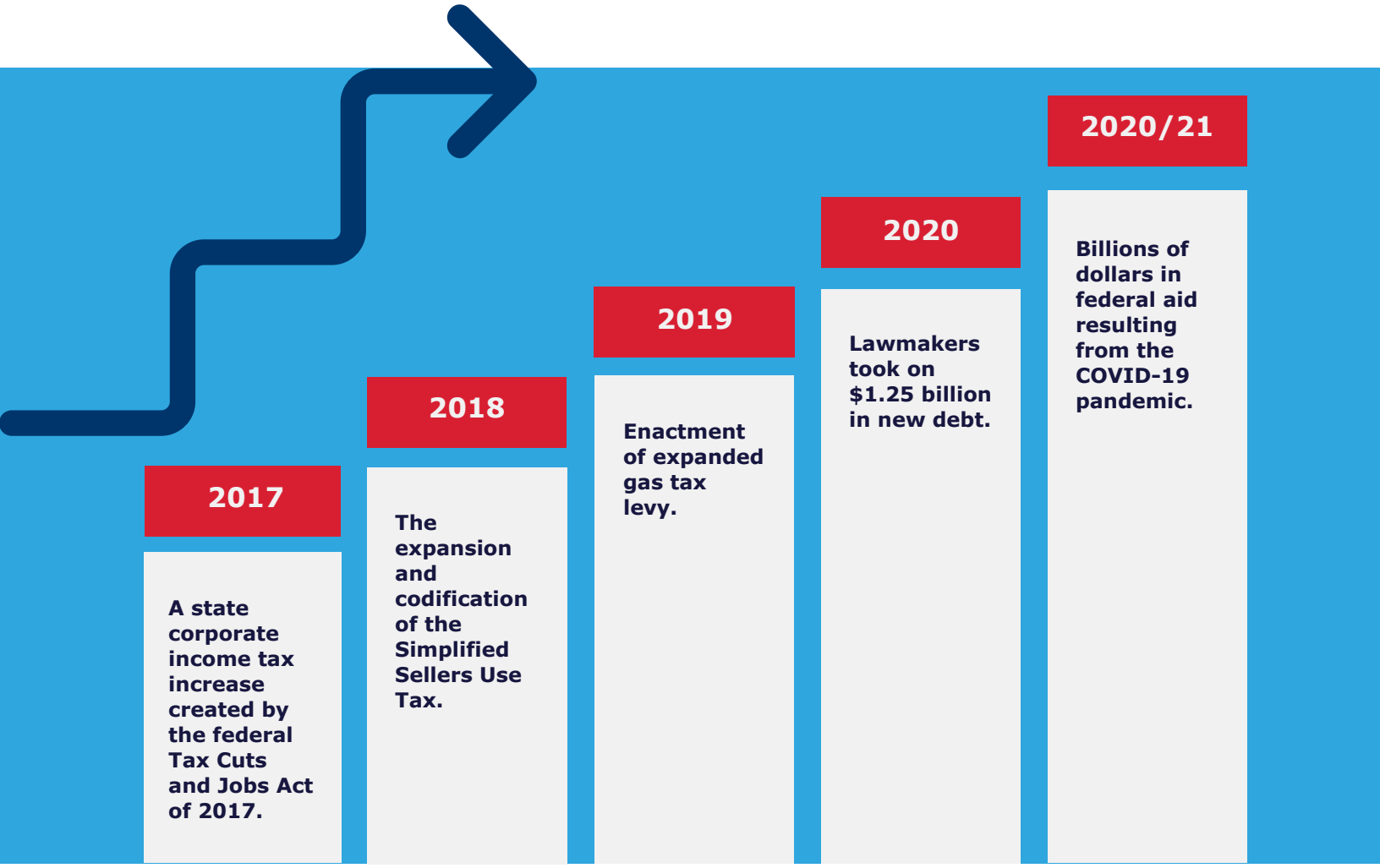
Regardless of what party controlled Alabama's government, the state has always been perceived as a conservative state. In some ways, that is certainly still the case, but as government grows, fiscal conservatism, personal choice, and individual liberties are challenged with more frequency.

While this report focuses on state spending and revenue, all policy issues are connected. Larger revenue streams mean a larger government, and a larger government means that the state has more resources to engage in activities outside of its essential scope.

Several events demonstrate the recent expansion of state taxes and record high spending:

1. Lawmakers took on $1.25 billion in new debt.
2. Enactment of expanded gas tax levy.
3. A corporate income tax increase created by the Tax Cuts and Jobs Act of 2017.
4. The expansion and codification of the Simplified Sellers Use Tax.
5. Billions of dollars in federal aid resulting from the COVID-19 pandemic.

Alabama's state and local governments are literally drowning in cash right now. The people of Alabama do not even fully know how government intends to spend it or who exactly it will benefit. The only sure thing is that Alabama has more resources right now than ever before.



Record Spending

Despite the disruptions of the COVID-19 pandemic, Alabama's state government has continued to boom, pushing spending higher each year. The FY 2020 State General Fund and Education Trust Fund budgets were approved before the pandemic began. At the time, they were the largest budgets in state history, totaling more than $9.3 billion.[20]

Despite the disruptions of the COVID-19 pandemic, Alabama's state government has continued to boom, pushing spending higher each year.

The FY 2021 budget process occurred in the spring of 2020, amidst disruptions caused by the pandemic. There was great economic uncertainty at the time, leading a few lawmakers to advocate for delaying the budget process until later in the year, when there might be more certainty on budget projections. Others were in favor of passing a "bare-bones" budget and then passing additional appropriations later in the year if revenues performed better than expected.[21]

Despite the uncertainty, the legislature and governor went full-speed ahead with both the fiscal year 2021 ETF and SGF budgets, again enacting record-high spending levels for each. While the ETF grew at a more modest rate of 1.3%, SGF spending increased by 7.7% compared to fiscal year 2020. In the previous five years, the average growth rate of the SGF budget was 3.2 percent.[22]

The only mitigating factor for fiscal conservatives was the fact that if not for the pandemic, spending would likely have been even higher.

One would think that this would have been a divisive or at least thoroughly debated issue considering the economic uncertainty at the time. It was not. Just one member of the legislature, Representative Andrew Sorrell, voted against the two budgets. Not a single other lawmaker out of 140 elected state legislators objected to increasing spending during the heart of the COVID-19 pandemic.[23]

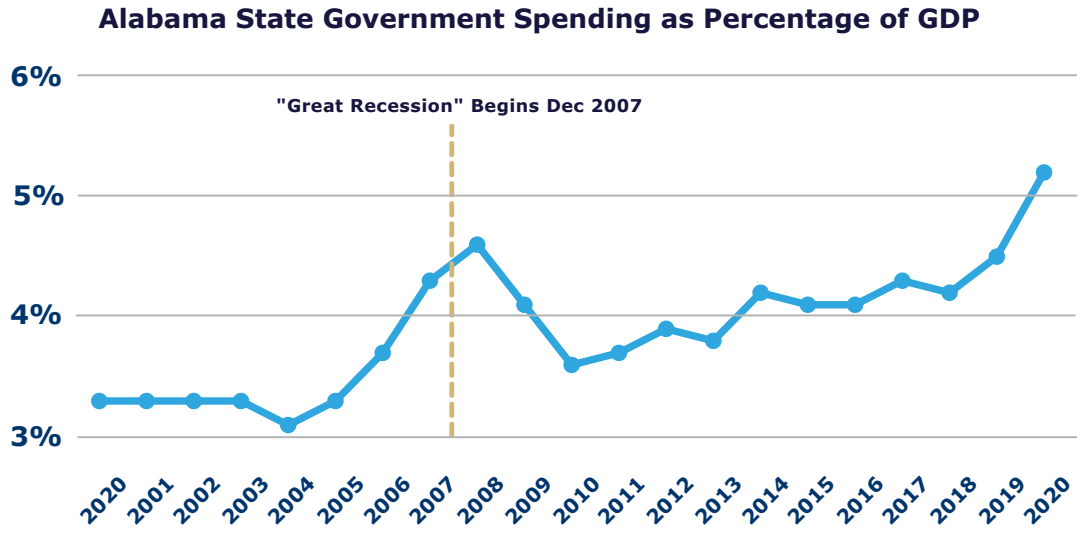
Only one lawmaker out of 140 elected state legislators objected to increasing spending during the heart of the COVID-19 pandemic.

Take a moment to consider this. Budgets are supposed to represent the priorities of the majority party. In Alabama that currently means that the state budget should represent a conservative vision for the future of the state. If that were the case, then no Democrats should vote for a budget proposed by Republicans. Even if Republicans are unified, it seems hard to believe that every member of the Republican caucus would vote in favor of a budget.

The fact that only one member of the legislature voted no on the fiscal year 2021 budget shows that almost everyone was happy with the budget because they, or hopefully some of their constituents, benefited from it. It also means that it was not a conservative budget.

The ETF and SGF budgets were both enacted in the first 10 days of May 2020, on the heels of Alabama recording a 13.2% unemployment rate in April. While nearly 300,000 private sector Alabamians were wondering where their next paycheck would come from,[24] the legislature was more concerned with growing government than providing aid to those who were struggling the most, an issue that will be examined in more detail later in this section.

While nearly 300,000 Alabamians were wondering where their next paycheck would come from, the legislature was more concerned with growing government than providing aid to those who were struggling the most.



For perspective on government spending continuing to trend higher, in 2020 Alabama's real gross domestic product (GDP) was $195.5 billion. According to Certified Annual Financial Reports from the State Comptroller's Office, actual disbursements from the ETF and SGF totaled $10.2 billion in fiscal year 2020. That means that government reinvested 5.2% of the state's economy back into itself. 20 years earlier, state government spending was 3.3% of GDP. In just two decades state spending as a percentage of GDP increased by almost 58% in constant dollars.[25]

Perhaps some of the blame for the legislature's lack of fiscal responsibility during the first months of the pandemic lays at the hands of the federal government. There was so much federal money already coming into the state that there was never a real risk of a revenue shortfall.

The CARES Act provided a wide variety of benefits to businesses and individuals that also helped state government see record revenues. First, the act provided $600 per week in additional unemployment benefits. On top of Alabama's $275 per week in benefits, a person could have made $875 per week to not work.[26] Between April and July of 2020 (when the additional $600 benefit expired), an unemployed person could have made almost $15,000 to not work. Though unemployment benefits are not taxed by the state, the influx of money meant that despite being unemployed people's purchasing patterns were not significantly disrupted and state revenues were not hurt by the temporary spike in unemployment.

In addition to unemployment benefits, many Alabamians received stimulus payments from the federal government regardless of their employment status. Individuals were eligible to receive as much as $3,200 through three separate stimulus payments, while joint filers received up to $6,400, with additional payments available for dependents of both tax filing groups.[27] For some Alabamians this money was undoubtedly a lifeline, but for others it was just a gift from the federal government and bolstered the state's sales tax revenues.

The CARES Act also created the Paycheck Protection Program (PPP), which provided loans to businesses through May 31, 2021. While the payments were technically loans, the debts were forgiven if 60% of the proceeds were used for payroll costs.[28] Alabama businesses were granted an estimated 175,215 federal PPP loans totaling $9.5 billion.[29] Because of the federal loans coming into the state, more individuals were able to remain employed and not see a decline in pay. That translates to more stability in Alabama's income tax revenue.

By the end of fiscal year 2020, Alabama had taken in $9.7 billion in revenue with the ETF and SGF revenues streams seeing 2.9 percent and 6.8 percent growth respectively.[30] Because of already growing state revenues and federal dollars, Alabama saw record high revenues in 2020 despite the COVID-19 pandemic. According to the Legislative Services Agency, the SGF took in an additional $147 million (6.8% growth) compared to 2019. The ETF saw real revenues grow by $209 million in 2020. When combined with transfers, the ETF grew by nearly $526 million (7.3%).[31] This allowed lawmakers to ignore fiscally responsible principles and push spending levels higher.

6.8%
+ $147 million

SGF revenue growth

Alabama saw record high revenues in 2020 despite the pandemic. The SGF took in an additional $147 million (6.8% growth) compared to 2019. The ETF grew by nearly $526 million (7.3%). This allowed lawmakers to push spending levels higher.

7.3%
+ $526 million

ETF revenue growth

Lawmakers Took on More Debt

While lawmakers were busy passing record-setting budgets each session, they also found time to put the state further into debt. During the 2020 Regular Legislative Session, lawmakers approved a $1.25 billion bond issuance to fund capital improvement projects at Alabama's K-12 and higher education institutions. The Legislative Services Agency estimated that the bond issuance would cost the state $80 million per year in annual debt payments.[32]

Lawmakers justified the new bond issuance being at little additional cost to taxpayers because $67 million in previous annual debt payments were being retired, thus only costing the state $13 million more each year.[33] That is misguided logic. Permanently retiring debt from a previous bond issuance would have meant $67 million less that had to be paid each year. Instead, the state is on now the hook for $80 million in new debt for the next 20 years.

And if there is ever a budget shortfall, the bond debt service payments would be the first thing to be paid, because not doing so could have farther reaching impacts for Alabama's economy.

The issue, then, is not over the state taking on a new $80 million obligation each year. In the scope of more than $10 billion in annual spending, $80 million is less than one percent of the budget. But issuing more debt during the pandemic shows the misguided priorities of Alabama's elected officials.

At a time when the state had more money coming in than it ever has before, lawmakers were willing to borrow and spend even more of taxpayer's money.

At a time when the state had more money coming in than it ever has before, lawmakers were willing to borrow and spend even more of taxpayer's money.

An Influx of Tax Revenue and Federal Stimulus Dollars

If lawmakers want to grow government, that means that they need to take more money from citizens and businesses operating within the state. For the past several years, the governor and legislature have continued to seek new revenue streams to increase the state's largesse. There has also been a combination of changes in federal tax provisions and massive federal stimulus bills that has led to even more money flowing into the state.

New Tax Increases on Alabama Citizens

Gas Tax

There have been several sources of new revenue that have fueled the growth of state government over the past few years. Perhaps the most notable was the gas tax increase that became law under the Rebuild Alabama Act of 2019. The act provided for a three step increase in Alabama's gasoline and diesel tax rate beginning October 1, 2019. The first new levy would be a $0.06 per gallon tax in 2019 with an additional $0.02 added in October of 2020 and 2021, increasing the total additional tax levy to $0.10 per gallon.[34] Only 26 of the 140 lawmakers voted against the tax increase on Alabamians.[35]

Two-thirds of the new revenues go back to the state, a quarter to counties, and the remaining 8.33% to municipalities. $10 million is taken off the top for local grant projects, which are determined by the governor and Alabama Department of Transportation (ALDOT).[36]

The majority of the county and municipal share of the gas tax proceeds are distributed based on population, meaning that metropolitan areas will get a larger share than rural counties.[37] The money is intended to be used for road and bridge construction and maintenance projects, even though $11.7 million per year is dedicated to improving the shipping channel in the Port of Mobile.[38]

Gas tax revenue is intended to be used for road and bridge construction.

However, an often ignored aspect of the gas tax increase is that beginning October 1, 2023, the tax rate can increase by up to $0.01 per gallon every two years. The act allows this to be done by the Alabama Department of Finance based on changes in the National Highway Construction Cost Index.[39] The Rebuild Alabama Act created an automatic tax increase that never has to be approved by the legislature or voted on by citizens. It allows lawmakers to quietly increase the gas tax revenue stream with little opportunity for public accountability.

In its first year of existence, the new tax levy brought state government $153.5 million in new revenues. The Alabama Legislative Services Agency estimates that the $0.10 tax levy could generate $323 million in annual revenue by 2022. Additional $0.01 levies in subsequent years would mean even more money flowing into state government.[40]

According to the distribution formula, ALDOT should have received approximately $94.5 million in proceeds from the new tax levy in 2020. Yet according to ALDOT's fiscal year 2020 Annual Report, only about $40 million of that was spent through the Alabama Transportation Rehabilitation and Improvement Program-II (ATRIP-II) and Annual Grant Program.[41] The Rebuild Alabama Act states that up to $50 million annually can be spent on ATRIP-II and a minimum of $10 million per year is to be spent on local grants.[42] ALDOT left at least $20 million unspent that could have gone towards state road projects.

New Tax Increases on Alabama Citizens

Corporate Income Tax Windfall

Changes to the federal tax code enacted through the Tax Cuts and Jobs Act of 2017 (TCJA/Trump Tax Cuts) have inadvertently led to higher corporate income tax receipts for Alabama's state government. Alabama practices what is known as rolling conformity with the federal tax code, meaning that it automatically adopts provisions of the federal code into state law.

The TCJA lowered federal corporate tax rates from 35% to 21%.[43] This meant that most Alabama-based companies paid a lower federal tax bill. However, since Alabama allows federal corporate taxes paid to be deducted from a business's Alabama corporate income tax filing, an entity that paid less in federal taxes had less to deduct from its Alabama return and paid higher state taxes.

Alabama has a statutory corporate tax rate of 6.5%, which is higher than other southeastern states. However, before the TCJA the effective tax rate was 4.3%. Because changes in federal law have reduced the state income tax deduction, Alabama's effective corporate tax rate is now 5.2%. The change has meant more money for the state but makes it less attractive for businesses to move to Alabama. From fiscal year 2017 to 2020, net corporate income tax receipts increased by 28.1%, translating to more than $100 million in new revenue annually for state government.[44]

The solution to this problem is simple. Alabama should lower its statutory corporate tax rate and amend its deduction formula so that it is more competitive with neighboring states and not susceptible to changes in the federal tax code. State Representative Danny Garrett and Senator Dan Roberts introduced legislation to do both things during the 2020 Regular Legislative Session, but the changes were not adopted and the bills were not reintroduced in the same form during the 2021 session.[45]

Alabama should lower its statutory corporate tax rate and amend its deduction formula so that it is more competitive with neighboring states and not susceptible to changes in the federal tax code.

New Tax Increases on Alabama Citizens

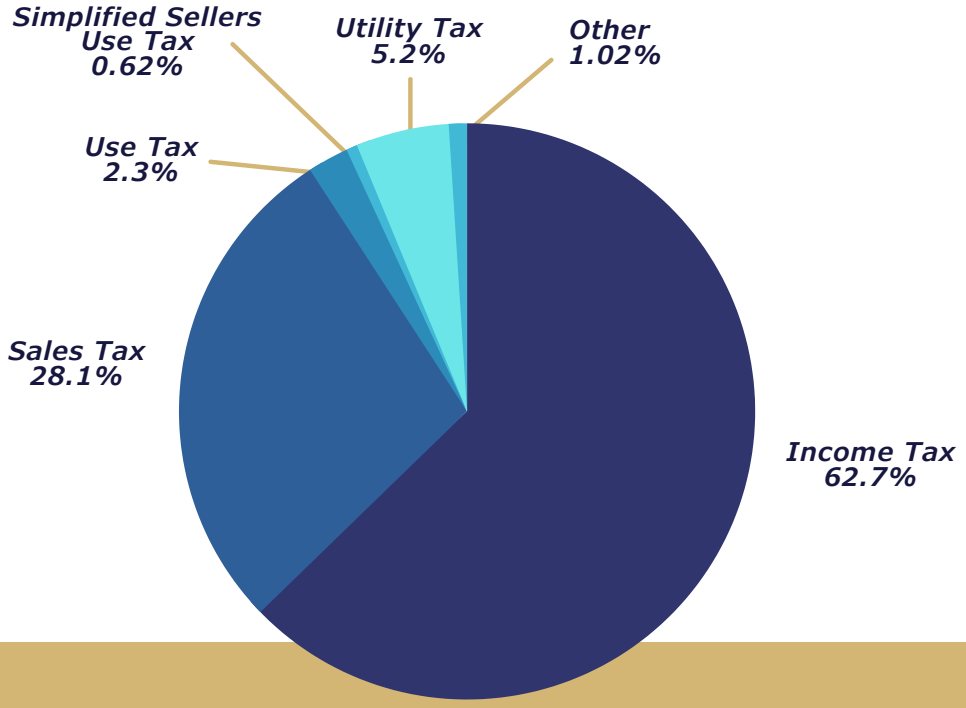
Simplified Sellers Use Tax Sees Massive Growth

The Simplified Sellers Use Tax (SSUT) is essentially an 8% sales tax on goods delivered into Alabama by companies that do not have a physical presence within the state, commonly referred to as online sales tax. The tax was first established in 2015, but compliance from sellers was voluntary. However, in 2018 the legislature enacted a law that required sellers to collect the tax beginning January 1, 2019. [46] 37.5% of the tax proceeds are distributed to the SGF, 12.5% to the ETF, and the remaining 50% to local governments.

When the SSUT became mandatory, state and local governments saw a sharp increase in revenues. In fiscal year 2018 SSUT tax receipts totaled $84.3 million. By 2019, collections increased more than 141%, reaching $203 million. Strong growth continued through 2020, with the COVID-19 pandemic and its state and local mandated business closures increasing online shopping. In 2020 the SSUT generated $386.3 million in revenue for the state.[47]

Despite the increase in online sales, state sales tax receipts, too, have continued to increase each of the past five years. In addition to traditional sales tax, the SSUT now pumps nearly $200 million annually into the two state budget funds: this money was virtually non-existent just a few years ago.

Fiscal Year 2020, Education Trust Fund Receipts by Tax



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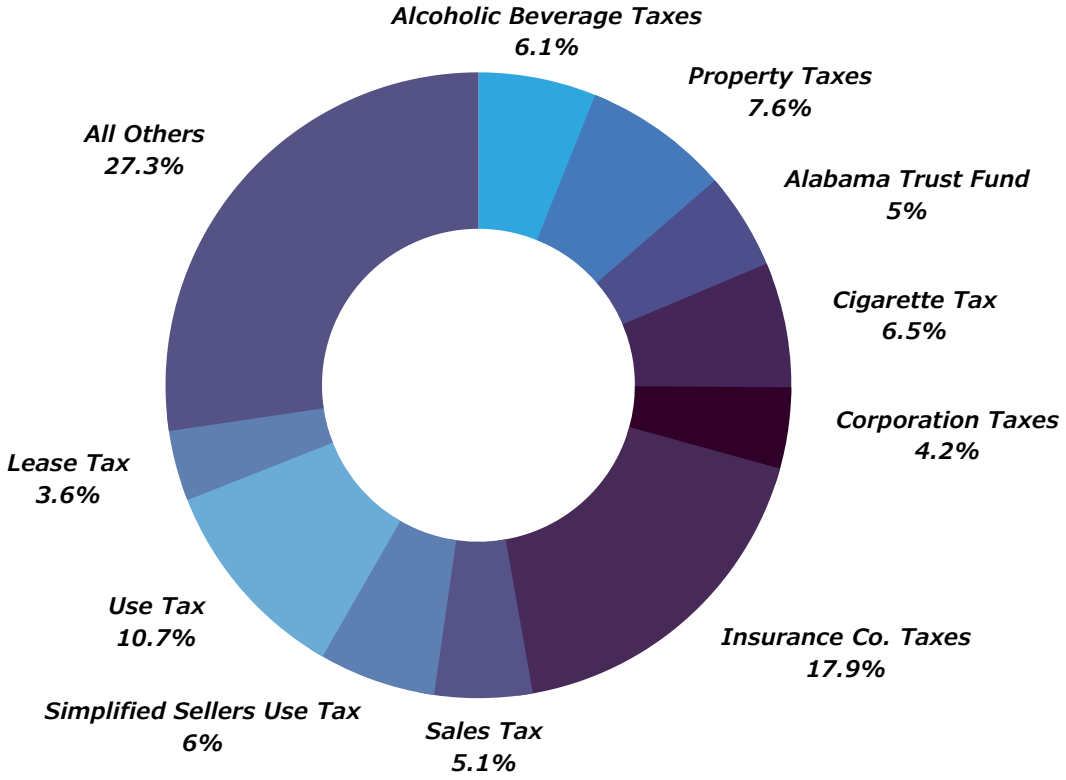
Fiscal Year 2020, State General Fund Receipts by Tax



Billions in Federal Stimulus Funds Come to Alabama

On January 20, 2020, the first case of the novel coronavirus (SARS-CoV-2) was diagnosed by officials in Washington State and from the Centers for Diseases Control and Prevention (CDC). [48]

As the coronavirus outbreak widened, federal, state, and local governments began an unprecedented response. Citizens were asked to wear face coverings when in public, many businesses were forced to shut down, and life as we knew it immediately changed.

The response also meant an influx of relief money from the federal government. In total, the State of Alabama has been directly awarded more than $4 billion in stimulus funding through the federal Coronavirus Aid, Relief, and Economic Security Act (CARES Act) and American Rescue Plan. Billions more has flowed directly to state agencies, such as the Department of Education, as well as to county and municipal governments.

In total, the State of Alabama has been directly awarded more than $4 billion in stimulus funding through the federal Coronavirus Aid, Relief, and Economic Security Act (CARES Act) and American Rescue Plan. Billions more has flowed directly to state agencies, such as the Department of Education, as well as to county and municipal governments.

Billions in Federal Stimulus Funds Come to Alabama

Unfortunately, much of Alabama's CARES Act funds went towards growing government and narrowly focused grant programs that allowed state officials to choose the beneficiaries. Instead of relief that could have helped all Alabamians, too frequently Governor Kay Ivey and other state officials chose to invest in government instead of the citizens that government is bound to serve. All aspects of state government remained essential – and many saw increased funding – while "non-essential" private sector jobs and businesses were forced to shut down for a time. Some never reopened.

The state has yet to spend money from the American Rescue Plan. The $2.1 billion state share will come in two payments, with the first already being delivered to the state and the second batch coming in 2022. Another $1.7 billion for local governments will be transferred in the same manner.[49] County and municipal governments have found themselves so flush with money that they are literally giving it away in the form of bonuses to government employees.

Lawmakers must examine the lessons learned from the CARES Act and responsibly use American Rescue Plan stimulus funds in ways that will benefit all Alabamians, not just government and a chosen few.

Coronavirus Aid, Relief, and Economic Security Act

On March 27, 2020, the federal CARES Act was signed into law. The $1.8 trillion stimulus bill aimed to provide wide-ranging assistance to healthcare providers, individuals, and businesses.[50]

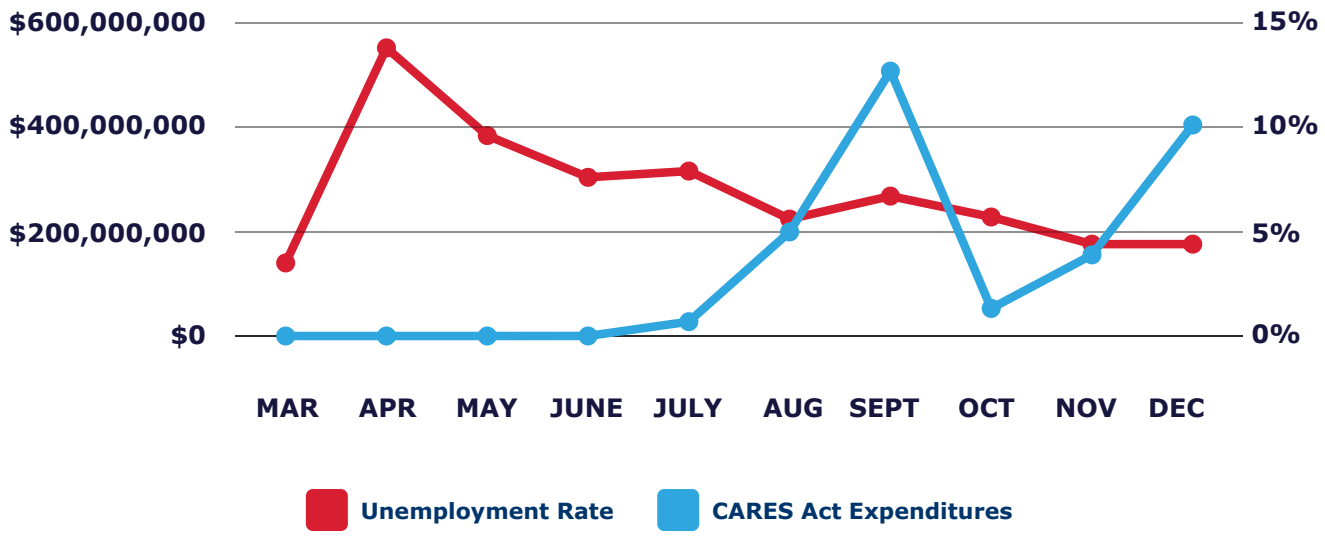
It also supplied direct relief to state and local governments through the creation of a $150 billion pot of money known as the Coronavirus Relief Fund. One stipulation was that all state and local funding had to be spent before the end of 2020 or it would go back to the United States Treasury.

Alabama's share of CARES Act funding was just under $1.8 billion, with an additional $115 million going directly to Jefferson County.[51]

Congress included several limitations as to how the stimulus funds could be spent, with the main goal being to provide economic relief as well as to support stressed healthcare capabilities, among others.[52] CARES Act funds were intended to act as an emergency lifeline for state and local government to provide for citizens. If the funds were truly needed, spending them in an efficient and effective manner by December 30, 2020, should not have been an issue.

That is not what happened in Alabama though. As the state unemployment rate spiked from 3.5 percent to more than 13%, CARES Act money stayed in the state's coffers unspent. It took nearly five months for state government to begin spending the money in any significant way, and by that point it was too little too late to save many businesses impacted by government mandated closures.[53]

2020 Monthly Unemployment Rate vs. Monthly CARES Act Expenditures



If the funds were truly needed, spending them in an efficient and effective manner should not have been an issue.

After a battle between Governor Ivey and the legislature, the governor ultimately seized control of the CARES Act funds and determined how they would be spent. She designated 10 categories of spending, though they had little meaning once the money actually began to be spent.

When it was spent, much of it went right back into state government. Just 23.1 percent of the funds spent went towards the private sector, and much of that money was spent on limited scope grant programs where state government chose the beneficiaries.[54] The maximum grant award available for small businesses, non-profits, and faith-based organizations was $15,000.

While $15,000 may help some entities get by for a short time, it is not enough to substantially aid most organizations that were devastated by the coronavirus pandemic.

30 percent ($531.9 million) has gone towards reimbursing state and local government. The legislature was reimbursed by the Coronavirus Relief Fund for over $985,000 in equipment purchases, including a tablet system for socially distanced voting. In total, the legislature has charged over $1.1 million back to the fund despite there being virtually no legislative action between May 2020 and the end of the year.[55] When combined with a $385 million transfer to the state's depleted Unemployment Compensation Trust Fund, the proportion of funds used to reimburse state government rises to 52 percent ($916.9 million).[56] Over half of the money has been used to support government, rather than citizens.

It is important to remember that the rise in unemployment claims was to no small degree caused by Governor Ivey and the State Health Officer's decision to shut down businesses that were not deemed essential. At the same time, all public sector jobs, or at least the salaries attached to those jobs, remained "essential," regardless of how a particular function related to pandemic response. State government proved unwilling to make the same sacrifices that it forced upon Alabama's private sector employees and businesses.

Shutting down businesses undoubtedly increased unemployment and the strain on Alabama's Unemployment Compensation Trust Fund. Closing businesses was a major misstep, one that Governor Ivey admitted to in a December 2020 interview, saying that "[it] was a mistake because all businesses are essential."[57]

CARES Act funds were intended to provide a lifeline to state governments and, more importantly, the citizens that they serve. They were appropriated as emergency funds, with the connotation being that immediate aid was necessary. However, it took Alabama many months to begin spending the money.

Nearly six months after the passage of the CARES Act, Alabama had spent only $285 million of its $1.8 billion CARES Act allotment. As Alabama approached the original December 2020 spending deadline (which, by then, was extended for one year by Congress), nearly half a billion remained unspent.

If there was truly an immediate need for federal relief then the state should have had no problem finding effective ways to use the funding to help all Alabamians. The fact that the state spent virtually nothing for months after the pandemic began suggests that Alabama either did not need the money, or its elected officials were ineffective in using it to help the state recover from the pandemic.

State government proved unwilling to make the same sacrifices that it forced upon Alabama's private sector employees and businesses.

American Rescue Plan

On March 11, 2021, the federal government signed the American Rescue Plan Act into law. The $1.9 trillion stimulus bill surpassed the CARES Act as the largest relief bill in American history.[58]

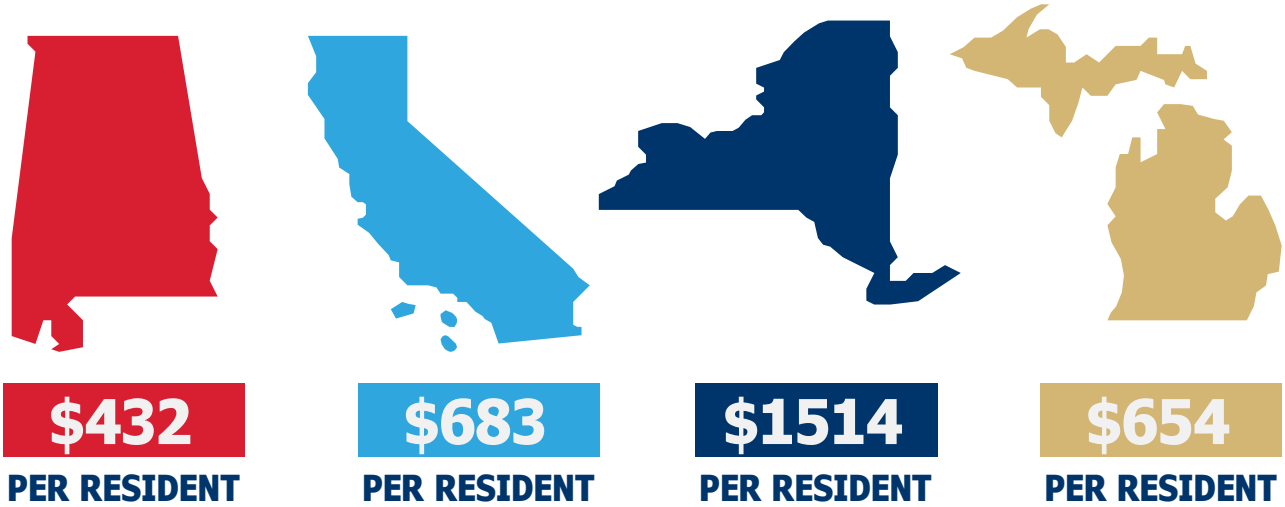
The passage of the American Rescue Plan means another major federal windfall for Alabama's state government. The state was directly awarded $2.1 billion in funding from the act, with another $1.9 billion flowing directly to counties and municipalities. Total funding to the state, not including direct aid to agencies such as the Alabama Department of Education, is $4.03 billion.

However, Alabama is not getting a proportional share of the funding compared to some other states. The state is actually being punished for imposing less restrictions on businesses and having a faster recovery than more restrictive states. This shows that perhaps the second major stimulus package was passed more out of political motivation than based on actual needs. It allowed Rescue Plan money to be weaponized for political gain.

Unlike the CARES Act which allocated all state and local government funding based on population, the American Rescue Plan does so with only 13% of the money. $169 billion out of $195.3 billion was proportioned to states based on unemployment levels from October through December 2020.[59] Alabama's unemployment rate averaged 4.7% during that time, about 8.5% lower than the height of the pandemic's business closures.

Alabama's direct state share of American Rescue Plan funding equates to around $432 per resident of the state. The state of New York got 3.5 times that amount, at $1514 per capita. California and Michigan, two more heavily restrictive states, received $683 and $654 per resident respectively.[60]

State Share of American Rescue Plan Funding



The federal government took on trillions of dollars in new debt to cover the costs of the American Rescue Plan. Because of the inequitable distribution of stimulus funding, Alabama taxpayers are financing a higher share of that debt than states that did not respond as well to the pandemic and had higher unemployment rates.

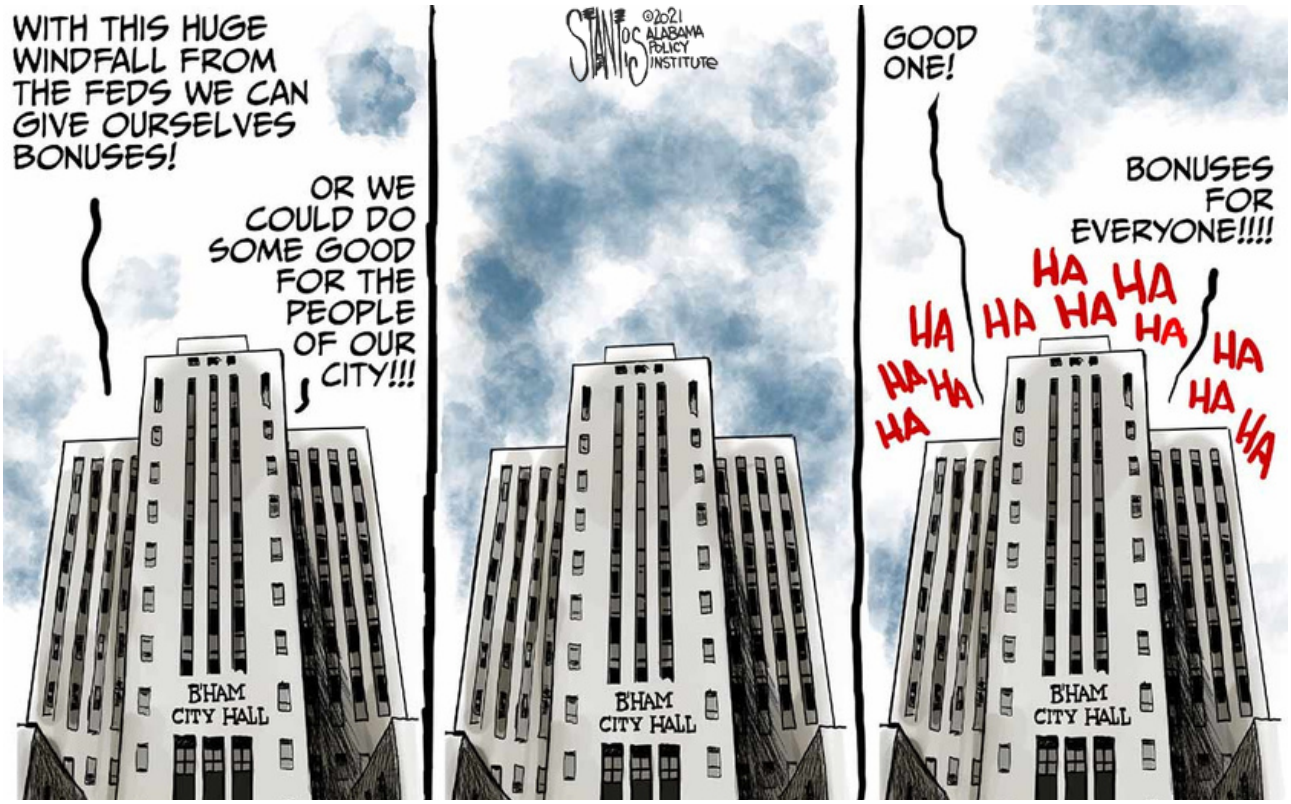
Nevertheless, the first half of the stimulus funds has already begun flowing into the state, with the second half scheduled to be transferred from the federal government early next year.

There has been much speculation as to what state government will use the funds for, but as of September 2021, all that has officially been designated is $400 million in American Rescue Act funds to address construction needs within the Alabama Department of Correction's aging prison facilities.[61]

One potentially positive sign from the state government side is that it appears that unlike the CARES Act spending process, which Governor Ivey seized nearly absolute control over, the legislature will take a more active role in determining how the Rescue Act money is spent.

There is some early data on how county and local governments are beginning to spend the American Rescue Plan money. For fiscal conservatives that data is disheartening, as it points to leaders continuing to grow government and to focus on public sector employees rather than all citizens.

For example, the City of Birmingham is scheduled to receive $148 million in direct federal payments as a result of the American Rescue Plan. Half of that money has already been received. What has Birmingham done with it? The city approved a plan to use $17 million, nearly a quarter of its first round of Rescue Plan funding, to provide bonuses to all full and part-time city employees. Bonuses range from $2,500 for part-time employees to $5,000 for full-time workers.[62]



Some may have the perception that many city employees were furloughed because of the pandemic, and this is a way to make their paychecks whole, but that is not the case. The city of Birmingham has around 4,000 employees.[63] Just 7% of Birmingham's workforce was furloughed in 2020 because of the COVID-19 pandemic. All other public sector employees remained essential, while private businesses were shut down or forced to endure reduced capacity requirements.[64] And the bonuses are on top of the city's biggest budget ever which includes merit increases, longevity bonuses, pension benefits, and additional contributions toward employee healthcare costs.[65]

Mobile announced that it would follow a similar track with its use of American Rescue Plan money. In August, the Mobile City Council approved a plan that would provide $2,200 to $5,000 bonuses to its full and part-time employees. The city plans to use just $17 million of over $58 million in total funding to address negative economic impacts caused by the pandemic.[66] This was in addition to $1,200 bonuses that the Mobile County School Board provided to all full-time employees (including non-teaching positions) earlier in the year.[67]

Highlighting teacher bonuses is intended in no way to diminish the importance of education or the role that teachers play. But it does lead to several observations. By granting bonuses to teachers, city employees, etc., one conclusion is that these local governments care more about continuing to feed government than the citizens that government is obligated to serve.

At the same time, healthcare workers across the state and country sacrificed more than perhaps any other sector. If a city or county wanted to use stimulus funds to pay bonuses, then why not give them to the workers impacted most by the pandemic?

Another potential conclusion is that all levels of government, both Alabama's state and local, did not need additional federal stimulus funds. State government made little impact on the day to day lives of Alabamians with its use of the $1.8 billion in CARES Act funds. The money was spent slowly and inefficiently. That does not mean it provided no benefit to anyone, but most citizens saw no direct impact.

Considering that reality, state government is now in the process of receiving another $2.1 billion in stimulus funds on top of the $1.9 billion local share. The combined state total, though not all being spent in one year, is more than one and half times the size of the 2022 State General Fund budget. And it seems like governments do not know good ways to use the additional funding, so the simple answer is to give out bonuses. The bonuses handed out in Birmingham and Mobile conveniently also came as those city's mayors were amid reelection campaigns.

The good news about American Rescue Plan money is that the first half has not been spent and the second half will not be here until next year. That means that there is still time for citizens to demand better and ensure that lawmakers at all levels use it to help all citizens that they represent, not just government and its employees.

There is still time for citizens to demand better and ensure that lawmakers at all levels use federal dollars to help all citizens that they represent, not just government and its employees.

Department of Education Receives $4.5 Billion Stimulus from Federal Government

In addition to the $4 billion that the state has been awarded through the various stimulus bills, as well as over $2 billion more in local dollars, the Department of Education and institutes of higher education within the state have received an additional $4.54 billion in federal funding. Unlike CARES Act funds, the education dollars have few strings attached and can be used over the next several years.[68]

K-12 education received $1.1 billion through two 2020 stimulus bills, the CARES Act and the Coronavirus Response and Supplemental Appropriations Act of 2020. The American Rescue Plan provided an additional $2 billion to the Alabama Department of Education for its K-12 programs. Much of the money has flowed directly to local school districts, however the state requires local districts to submit spending plans for the Department of Education's approval.[69]

Higher education institutions have received an additional $1.2 billion through federal stimulus bills. Half of the money must be spent on emergency financial aid to students while the rest can go towards replacing lost revenue and reimbursement of pandemic related expenses.[70]

To put the education funding into perspective, the $4.5 billion from the various stimulus acts represents 58% of the fiscal year 2022 enacted Education Trust Fund budget, which does not include the additional $1.25 billion debt spending package for education already approved by the legislature in 2020. For both the SGF and ETF the impact of stimulus funds is troubling because in a few years that additional money will be gone. Without careful planning and fiscal restraint state government could find itself in a hole that it must fill.

Despite record education funding, the state and its institutions still want more. State Superintendent Eric Mackey has already said that he plans to ask for more than an additional $800 million for K-12 schools in the 2023 budget. Mackey reportedly told board members that "the amount of [state] money we think is going to be available this year is going to be phenomenal."[71] This comment shows the mindset of state government. If more money is coming in, government will continue to grow itself bigger each year.

Furthermore, despite higher education receiving over $1 billion in stimulus funds, the University of Alabama recently announced a $1.5 billion capital campaign. $600 million of the new funding from the capital campaign would go towards athletics.[72]

To reiterate, Alabama literally has more money coming into the state now than it ever has and already has more sitting in reserves than any other time in its more than 200-year history, yet government continues to seek more.

Alabama literally has more money coming into the state now than it ever has.

IV

WHAT HAS STATE GOVERNMENT DONE THE PAST THREE YEARS?

KEY TAKEAWAYS

- **The legislature passed a $0.10 gas tax increase in 2019 (which is expected to generate more than $320 million annually for the state). However, it can also continue to rise by an additional $0.01 every two years automatically. This is akin to taxation without representation. (Before the end of the next decade, the state could be taking in over half a billion annually in new revenue with no end in sight.)**
- **The legislature legalized medical marijuana in 2021, which provides several new revenue sources for the state including $10,000-$50,000 license fees, a $15,000 privilege tax for those in the business, and a 9% tax on retail sales. The established medical marijuana structure provides a way for the state to bring in millions of dollars and completely ignores free market and limited government principles.**
- **The legislature attempted to legalize casino-style gambling (and implement a state lottery) in 2021. Again, despite free market concerns, state government was highly compelled to pass this legislation for the hundreds of millions of dollars of revenue to be made through license fees and taxes on gaming revenue.**

Increased the State Gas Tax in Perpetuity

Legalized Medical Marijuana

Attempted to Legalize Casino-Style Gambling

(and Implement State Lottery)

Now that we have discussed how Alabama's state government grew to where it is, taking in and spending record amounts of money each year, it is worth recapping some of the signature achievements of the governor and legislature over the past three legislative sessions. The common theme has been finding ways to support the government growth that lawmakers have allowed to happen.

Increased the State Gas Tax in Perpetuity

Though the $0.10 gas tax increase has already been discussed, it is worth further examination. This was the signature "achievement" of the 2019 legislative cycle with many months of energy and a Special Legislative Session devoted to it.

When the tax is fully phased in at $0.10 per gallon it is expected to generate more than $320 million annually for the state. And this is potentially just the beginning. With the built-in indexing provisions of the law, it can rise by an additional $0.01 every two years without lawmakers or the people having any opportunity to stop it. [73] This is akin to taxation without representation.

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That means that before the end of the next decade, the state could be taking in over half a billion in new revenue with no end in sight. The only recourse would be for citizens to convince lawmakers that enough is enough and to amend the Rebuild Alabama Act to freeze, alter, or abolish the additional tax levy.

What is equally troubling about the taxes imposed by the Rebuild Alabama Act is that conservatives strayed so far from their principles in enacting it. The Alabama Republican Party only went so far as to oppose the bill unless certain conservative ideals were met. Even with their own party having clear reservations about the Rebuild Alabama Act, only 22 Republican lawmakers voted against it.

In keeping with fiscally conservative principles, new taxes should have been a last resort. But if taxation was the only solution, the legislation should have included reform elements that maximized every dollar already available to the Alabama Department of Transportation (ALDOT) and a corresponding tax cut from another revenue stream should have accompanied any rate increase.[74]

For example, until recently ALDOT was transferring tens of millions in transportation dollars to other executive branch agencies for purposes unrelated to transportation. Thankfully, Governor Ivey helped put an end to this practice, though it could return since it is not bound by statute.

There is also the principle of revenue neutral tax reform. This was the approach followed (at least on paper) when President Donald Trump spearheaded the passage of the Federal Tax Cuts and Jobs Act. While taxes were cut for many Americans, the Republican-led Congress theorized that by reducing taxes, citizens and corporations would put money back into the economy and pay for the loss of revenue to the federal government.

Alabama should have focused on a similar approach to the gas tax. If lawmakers wanted to raise that tax, then they should have looked to reduce the tax burden elsewhere, such as the regressive state tax on groceries.

Legalized Medical Marijuana

The 2021 Regular Legislative Session was consumed by two main issues: medical marijuana and a combined legalized gambling and state lottery effort.

While there are numerous arguments for and against each issue, from the standpoint of state government, both topics present an opportunity to generate more revenue and allow the reach of government to continue to grow.

36 states and four territories currently allow the use of medical marijuana.[75] While there is no exact dollar estimate of how much revenue medical marijuana sales will generate for the state, there is almost unlimited potential. Nationwide it is projected that medical marijuana will generate $7.3-$8.9 billion in sales by the end of 2021.

Alabama's medical marijuana law provides several new revenue sources. First, there is a $10,000-$50,000 annual license fee for facilities that process, transport, test, or dispense medical marijuana. In addition to the license fees, any person engaged in Alabama's legal marijuana business would face an annual privilege tax of up to $15,000. Finally, the state will levy a 9% tax of the gross proceeds of medical marijuana retail sales in the state.[76]

What is more troubling is that the taxing of medical marijuana could set a precedent for even more new taxes. Alabama currently does not have a sales tax on pharmaceutical medicines. The marijuana tax appears to be akin to a "sin tax" like what is paid on alcohol or tobacco products. However, the legislature approved the sale of marijuana for medicinal, not recreational, use. So, for the first time in state history, government is now taxing a medicine. Who is to say that this practice cannot or, under the legislature's logic, should not be expanded to all medicines?

The marijuana tax appears to be akin to a "sin tax" like what is paid on alcohol or tobacco products. However, the legislature approved the sale of marijuana for medicinal, not recreational, use. So, for the first time in state history, government is now taxing a medicine. Who is to say that this practice cannot or, under the legislature's logic, should not be expanded to all medicines?

One problem is that the Federal Drug Administration (FDA) has never approved cannabis for medicinal purposes. Since it is not an FDA-approved medicine, states can regulate and tax cannabis with great latitude.[77] Of course, if the FDA did approve medical marijuana it could cut into potential revenues for states.

Arkansas is another southeastern state that recently implemented medical marijuana sales. In the first two years the state reported over $330 million in sales and $31.7 million in tax revenue.[78] Arkansas's population is about two million less than Alabama, meaning that sales and revenues could be significantly higher here.

Beyond another revenue windfall for the state, there is the issue of the currently established medical marijuana structure ignoring free-market principles. Not everyone who wants to get involved in any aspect of Alabama's medical marijuana industry can do so. The Alabama Medical Cannabis Commission will license five facilities, three cultivators, three processors, three dispensaries, and testing laboratories and transporters. State Treasurer and former Agriculture Director Steve McMillan will serve as director of the commission. Based on sales from the medical marijuana industry as a whole and from southeastern states like Arkansas, the few businesses chosen by the state to participate in medical marijuana sales could stand to make millions of dollars.

Medical marijuana may prove beneficial to some Alabamians suffering from chronic health conditions. Hopefully that was the goal of most lawmakers who supported this legislation, but it is also big business with potentially big returns for state government.

Attempted to Legalize Casino-Style Gambling (and Implement State Lottery)

Much of the 2021 Regular Legislative Session was also dedicated to trying to implement casino-style gambling, sports wagering, and a state lottery in Alabama. Initial legislation failed to garner enough support to proceed, but late in the session a combined gambling and lottery bill was passed by the State Senate, though it never came up for a vote in the House of Representatives.

Much like the medical marijuana debate, there are economic, moral, and other arguments that can be made for and against expanded gambling and a state lottery. Regardless of those, one of the most compelling reasons for state government to want these things is revenue. A similar pitfall though is a lack of a free market environment. As with marijuana, the state would have chosen who can engage in the gambling industry, with a preference going to entities already operating facilities in the state under the current gaming structure.

The Senate passed legislation, which was spearheaded by Governor Ivey, that provided for five casino-style gambling locations within the state, with a sixth to be developed and owned by the Poarch Band of Creek Indians. Existing Poarch Creek gaming sites would have been able to implement casino-style gaming without the approval of the Alabama Gaming Commission.[79]

While gaming licenses would have been awarded based on a competitive bidding process, facilities could only be located at existing "covered locations," which inherently provides an advantage to the operators currently owning those locations. It also ensured that the Poarch Band of Creek Indians would have final bidding rights to the sixth casino location.[80]

Though the process was to be competitive in the sense that any entity could bid on the rights to operate a covered location, it was clearly skewed in favor of existing operators. This violates all free-market principles and, as with other cases examined in this paper, allows the state to determine who reaps the financial rewards.

Aside from the free market concerns, expanded gambling would have meant more revenue for and the expansion of state government. It also would have created several new levels of bureaucracy.

License fees for casino operators alone would have been an estimated $7 million-$10 million annually. The legislation authorized a 20% tax on gaming revenue which would generate an estimated $260 million-$393 million annually. After an initial set aside of $1 billion to implement statewide broadband access, a worthwhile purpose, 75% of annual revenues would have gone back to the State General Fund.[81] A huge revenue windfall for an already record large state government budget.

Even with the legislation running afoul of fiscally conservative principles, only four Senators voted against the bill.[82] This clearly shows the priorities of our current elected officials.

Though gambling legislation failed in the 2021 Regular Legislative Session, it will almost certainly be back in a future special or regular legislative session. In fact, in September 2021 the Alabama Track Owners Association began running advertisements aimed at pressuring lawmakers to take up the issue again, claiming that the state is losing $700 million per year in revenue.[83] Unless there is a major shift in the priorities of Alabama lawmakers, there is simply too much potential revenue and too strong of a desire for bigger future budgets being left on the table to abandon the fight.

The gaming license awarding process skewed in favor of existing operators violates all free-market principles and, as with other cases examined in this paper, allows the state to determine who reaps the financial rewards.

V

UPCOMING BUDGET ISSUES FOR STATE GOVERNMENT

KEY TAKEAWAYS

- **For better or worse, billions of dollars in federal stimulus aid are here and will be spent over the next few years.**
- **Do Alabamians want to continue to grow and expand the reach of government every year? Do lawmakers really care what the average citizen thinks?**
- **The state should use the billions in federal stimulus funds to lower citizens' tax burdens.**
- **The state could use the funds to implement a state sales tax holiday, to permanently eliminate the state sales tax on groceries, and even to expand broadband capabilities across the state – three ways that would benefit all citizens.**
- **Additionally, the state will use a small amount ($400 million) in "stimulus" funds to address Alabama's aging Department of Corrections facilities, which have been under investigation by the Department of Justice for the past five years.**

Ever Growing Budgets

As previously discussed, the legislature and governor approved the largest SGF and ETF budgets in state history during the 2021 Regular Legislative Session. When the legislature reconvenes in January 2022, what direction will lawmakers go as they begin work on the fiscal year 2023 budgets?

Some will advocate for continuing the status quo, seeking to raise revenues and spending above last year's record levels. The more prudent approach would be to take a step back and reexamine the fiscal state of Alabama's government.

For better or worse, billions of dollars in federal stimulus aid are here and will be spent over the next few years. At least a portion of that money could be used to pay for existing budget expenditures, allowing the state to set aside money for a future rainy day instead of continuing to grow government.

What citizens really need though is a broader discussion by the legislature about budget priorities, one that focuses on what a majority of citizens consider to be essential services and necessities. Do Alabamians want to grow and expand the reach of government every year? Do lawmakers really care what the average citizen thinks?

Many of Alabama's citizens feel that state elected officials do not care about their best interests and cannot be trusted most of the time. 2018 polling data from the Political Affairs Research Council of Alabama found that 64% of respondents felt that state officials did not care what they think.[84] Similarly, a 2018 NBC News/Survey Monkey poll found that 28% of Alabamians trust state government only about half the time, with another 49% trusting government only some of the time or almost never.[85]

While the 2022 Regular Legislative Session could be another year of new taxes and more record spending, it does not have to be. Apathy from citizens will not change anything though. Alabamians must take a stand for the fiscally conservative principles that many in this state expound. If lawmakers continue to ignore the will of the people, citizens will have another opportunity to initiate change during the 2022 state election cycle.

Do Alabamians want to grow and expand the reach of government every year? Do lawmakers really care what the average citizen thinks?

POLL RESULTS SAY:

64% say they feel state officials do not care what they think

49% trust government only some of the time or almost never.

**2018 polling data from the Political Affairs Research Council of Alabama*

**2018 NBC News/Survey Monkey poll*

Biden Infrastructure Plan

In March of 2021, President Joe Biden unveiled a $2 trillion infrastructure plan that would send billions of dollars in new spending to state governments.[86] To clarify, this is not the same as the $3.5 trillion budget plan also introduced by Biden and still under consideration by Congress as of this writing.

Over the intervening months, the plan was debated by Congress and eventually cut in half, with a $1 trillion plus price tag. Though final passage of the President's infrastructure bill is not a done deal at the time of this writing, the U.S. Senate has already approved it and the House of Representatives has committed to having a final vote on it by the end of October 2021.[87]

Biden's infrastructure bill is nearly three times larger than the last major federal infrastructure bill. Even after being cut in half, it still includes $550 billion in new spending. But only $110 billion of the new spending will go directly towards roads, bridges, and other transportation projects. Other provisions in the bill include the largest investment ever in public transit programs, spending for electric vehicle charging stations and clean energy buses and ferries, $120 billion for broadband expansion and clean water initiatives, and a $66 billion federal subsidy for Amtrak.[88]

While much of the money that may eventually be obligated through Biden's infrastructure bill looks to be going towards purposes that most Alabamians would not consider priorities, there will still be billions of dollars in new road and bridge construction money flowing into the state on top of the fuel tax increase that Alabama has perpetually adopted. But will Alabama get its proportional share of this newly printed money?

Alabama is expected to receive nearly $7 billion in infrastructure funding over the next five years, which puts the state 22nd on the estimated distribution list. California, Texas, and New York are set to receive a combined $107 billion from the infrastructure bill. Our neighbors in Florida, Georgia, North Carolina, Tennessee, and Louisiana will all receive a larger share of the federal funds than Alabama.[89]

Alabama also does not fare as well as other states when distribution is looked at on a per capita basis. The state's share is about $1,400 per resident. 26 states (including the District of Columbia) will get a higher per capita share of funding than Alabama. Alaska is set to receive an estimated $6,700 per resident. Joe Biden's home state of Delaware will take in about $1,000 more per resident than Alabama.[90]

The bill has not reached final passage, so in theory there is still time for Alabama's Congressional Delegation to work to lower the overall costs of the bill or shift its priorities to purely infrastructure functions. Our federal lawmakers can also advocate for the citizens of Alabama to make sure they are receiving an equitable share of the money compared to other states.

Once the money reaches Alabama, lawmakers must hold the Alabama Department of Transportation accountable as to how another federal windfall is being spent.

But what would be good uses of the American Rescue Plan Money that all citizens of the state could benefit from?

The focus should be lowering citizens' tax burdens.

American Rescue Plan Spending

As previously discussed, state government is set to directly receive $2.1 billion in American Rescue Plan stimulus funding over the next two years. Alabama will have until the end of 2024 to spend the money.

But what would be good uses of the money that all citizens of the state could benefit from? The focus should be lowering citizens' tax burdens.

Provide Tax Relief to Citizens and Business Owners

One way that the money could be used to benefit every resident of the state is to use a portion of the American Rescue Plan funds to provide tax relief to citizens and/or businesses of Alabama who are still recovering from the economic impacts of the pandemic.

This does not mean handing out stimulus checks to citizens of the state or providing more small grants to whoever government chooses. Instead, the legislature should look for ways to put money back into people's pockets so that they will then stimulate the economy. It also means making Alabama a great place to do business so that new companies will want to come into the state and existing businesses will have incentives to expand their Alabama operations.

In 2020, the Alabama Policy Institute advocated using CARES Act funding to provide an extended sales tax holiday throughout the state. API estimated that using around 25% of the CARES funds for that purpose could have eliminated the state sales tax for several weeks.

While that plan did not come to fruition, principles of it still stand. A sales tax holiday would give money back to anyone in the state that shops at a brick and mortar store. The two-fold effect would be encouraging citizens to shop locally and helping businesses that were hardest hit by government mandated shutdown orders.

A sales tax holiday is just one tax relief option. This paper has already discussed the quirks of the Alabama tax code and the need to statutorily lower the state's corporate tax rate so that Alabama is more competitive with neighboring states. The state could also discuss broader economic incentives that make it easier to do business in Alabama. Some of these issues were addressed during the 2021 Regular Session but more could be done to improve the business environment within the state.

Regardless of how state lawmakers decide to use the funds, they must ensure that they go towards purposes that will help the people of Alabama, not to expand government or allow government to choose the winners and losers.

Permanently Eliminate the State Sales Tax on Groceries

Another option that benefits all citizens of Alabama would be to use these funds as a down payment towards eliminating the state's four percent sales tax on groceries. Alabama is one of only three states that continues to fully tax the sale of groceries, while 16 states tax groceries in some form.[91] It is a regressive tax that hurts Alabama's poorest citizens the most.

According to estimates from the Alabama Legislative Services Agency, the sales tax on groceries accounts for $514 million in annual revenue for the state.[92] It is unclear how much of the American Rescue Plan money could be used to replace lost revenue, but it would likely be enough to eliminate the tax for an extended period of time. Even if stimulus funds could not be used, the state already has enough new revenue to eliminate the grocery tax.

Combined with increased gas tax revenues, medical marijuana revenues, and the myriad of other new revenues coming into the state, lawmakers could use the Rescue Plan money to start the process of fully eliminating the grocery tax. Since all Alabamians buy groceries, this would be a way for lawmakers implement relief that would permanently benefit all citizens.

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Rebuild Alabama's Aging Prison Facilities and End Federal Oversight

The state has not officially decided how all of the Rescue Plan money will be used, but, if authorized by the U.S. Treasury Department, $400 million will be used to address Alabama's aging Department of Corrections facilities.

New facilities are a need because of several court orders from U.S. District Judge Myron Thompson. In 2017 Thompson ordered the state to improve mental health care access and facilities at Alabama's prisons. A year later he gave the state four years to address other issues, including hiring 2,000 new correctional employees.

For the past five years, Alabama's prison system has also been under investigation by the Department of Justice, who claims that current conditions violate inmates' constitutional rights. If the state does not meet certain conditions, the federal government could step in and force the state to do so.[93]

Governor Ivey had previously worked to enter into a public-private partnership that would have constructed three new prison facilities that the state was to then lease for 30 years at an estimated cost of more than $3 billion. Lawmakers balked at the lease plan and private funding was eventually pulled, ending the project.[94]

It is of note that members of the legislature derailed what may be considered Governor Ivey's last-ditch plan to avoid the federal government taking over. Crumbling prisons and the threat of a federal takeover have been an issue since at least 2016. Then-Governor Robert Bentley tried to get the legislature to enact a construction plan for several years, but there was never agreement. Legislators have continued to do little to fix the problem.

In August 2021, Governor Kay Ivey referenced discussion between her administration and legislative leadership and said she was "encouraged" by the approach they were taking to the issue.[95] On October 1, 2021, after a five day special legislative session called by the governor, the legislature approved the revised prison plan. The revised plan approved by the legislature in October has three phases.

Phase I calls for the construction of two new 4,000 bed male prison facilities on existing state property in Elmore and Escambia counties. Phase II would provide a new 1,000 bed facility for females in Elmore County and allow for specified existing facilities to be renovated or reconstructed. The final phase would give the state the option to renovate other existing facilities and further address capacity issues if needed. The plan also includes the purchase of a currently vacant private facility in Perry county. The focus of one facility would be to aid prisoners with mental health and substance abuse issues.[96]

It is estimated that the cost of just the first phase of the prison plan would be approximately $1.2 billion. The legislation provides that the state would borrow $785 million to begin construction. Annual debt payments that would be taken on by the SGF are an estimated $50 million. Lawmakers plan to use $400 million in American Rescue Plan funds to pay for a portion of phase I, while the remaining funding would come out of the SGF budget. Subsequent phases are to be completed with available funding.[97]

While it is certain that Alabama's prison conditions are a problem that must be dealt with, would that be the best use of pandemic relief funds? It could alleviate a problem for state government and allow the state to run its prisons without federal intervention, which most Alabamians would see as a good thing. But it would provide little direct benefit to most citizens.

There is also the issue of cost and if the stimulus money could even be used for prison construction projects. Officials are hopeful that a provision of the American Rescue Plan allowing funding to be used to replace lost revenue could be used for prisons, but until there is further guidance from the U.S. Department of Treasury, that is uncertain.

The previous prison plan carried a cost estimate of more than $3 billion. The recently enacted proposal is scaled back a bit but will likely still cost more than the $2.1 billion in Rescue Plan funds allotted to the state. Additional funding will come through the sale of bonds, which would be paid back through the Department of Correction's existing appropriation. If the Department cannot repay the debt payments, the draft legislation allows money to be drawn from Department of Human Resources revenue streams.

If the state had practiced fiscally responsible budgeting, there would be no need to even discuss a bond issuance. Four years ago, the state was spending nearly $1.5 billion less than it is set to spend in fiscal year 2022. That, combined with savings in the intervening years, would have more than covered prison construction costs without borrowing money or relying on stimulus funds.

The prison proposal funding mechanism still contains many unknowns. It could potentially put the state in a position where it does not have the resources to cover billions of dollars in construction and maintenance costs.

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Expand Broadband Capabilities Across the State

A lesson learned early on during the COVID-19 pandemic was the need for access to high-speed internet. With schools and businesses shuttered, many people depended on internet access to carry on with their daily lives. Schools went to online learning, businesses became almost entirely dependent on online sales, and telemedicine became a necessity for many.

Unfortunately, Alabama continues to lack the high-speed internet capabilities enjoyed by many states. Alabama ranks 47th nationally in broadband capability with over 70% of residents not having access to an affordable broadband plan.[98]

During the 2021 Regular Legislative Session, the legislature did acknowledge and address the issue of broadband expansion, establishing the Alabama Digital Expansion Authority and putting a financing mechanism in place to increase broadband capabilities across the state in the coming years. However, the Connect Alabama Act caps the amount of money that can be spent on broadband each year.[99] If American Rescue Plan funds were used, that process could start immediately and without funding restrictions, meaning faster access to high-speed internet throughout the state. It would also not create a new financial obligation for the state and its taxpayers.

VI

RISKS OF DEPENDENCE ON FEDERAL FUNDING

KEY TAKEAWAYS

- **The pandemic has only exacerbated Alabama's increasing dependence on federal funding.**
- **A combination of $10.2 billion in state money, an estimated $31 billion in direct payments from the federal government, and additional federal streams such as contracts, grants, loans, and other financial assistance, equals about $63.3 billion in aid from the federal government that went to state and local government as well as Alabama businesses in FY 2020.**
- **A 2020 report from the Tax Foundation identified Alabama as the 14th most dependent state when it comes to federal aid.**
- **Money from the federal government is not "free money." It is money that you, the taxpayer, have already paid to the federal government, or it is money that the federal government is borrowing in the form of greater short-term and future national debt.**
- **The wealth of federal spending in the state has given lawmakers little incentive to pursue fiscally responsible budgets.**

Before the influx of federal stimulus money that came as a result of the COVID-19 pandemic, the state was already becoming increasingly dependent on federal funding. The pandemic has only exacerbated that problem. Dependence on federal funding is a problem that could create increasing challenges in the state budgeting process for years to come.

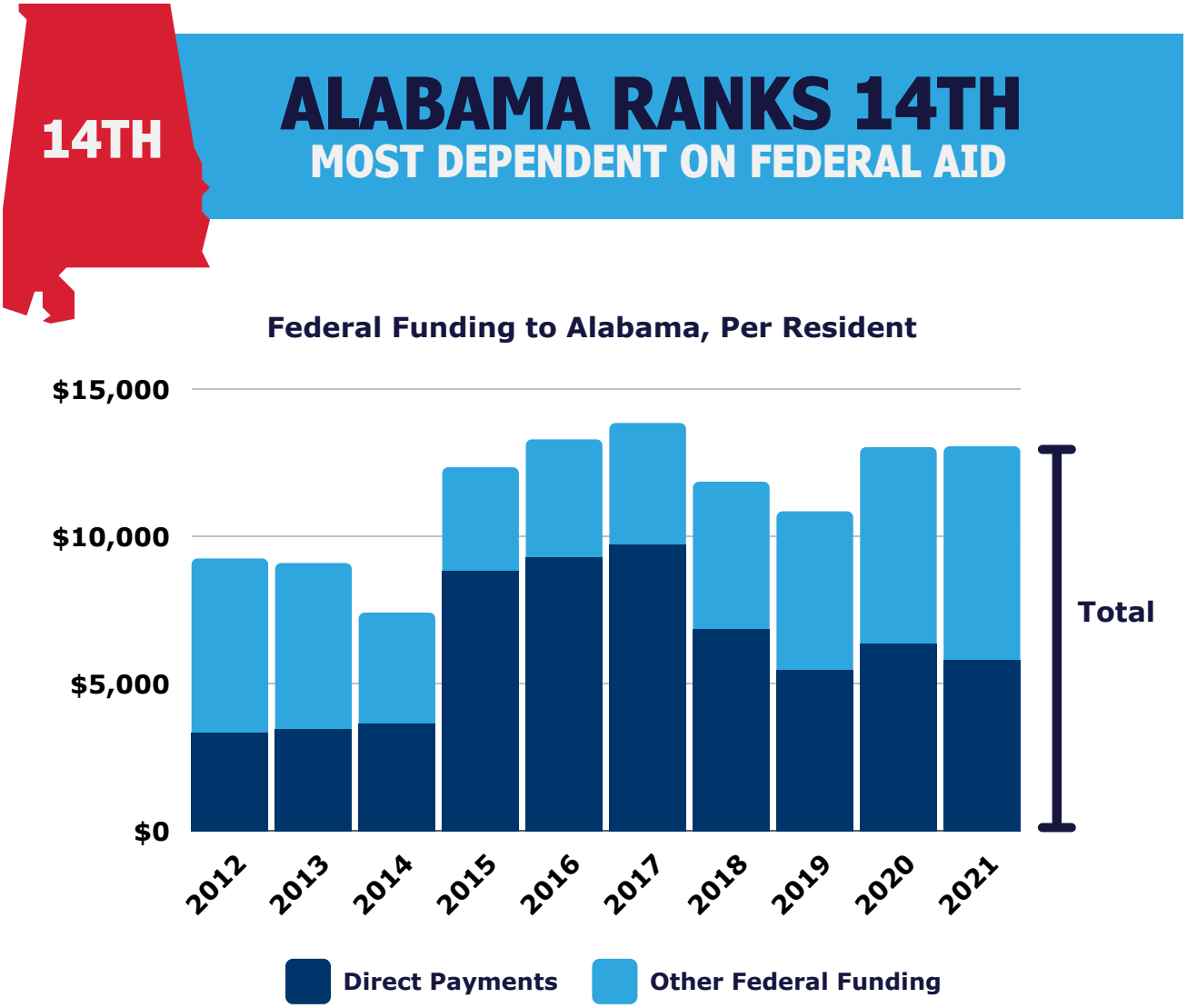
In fiscal year 2022 state government is set to spend $10.2 billion of its own funds to carry out government activities. As of July 2019, the Census Bureau estimated that Alabama had a population of 4.9 million people.[100] That means that the state will spend approximately $2,071 per resident in 2022.[101]

Dependence on federal funding is a problem that could create increasing challenges in the state budgeting process for years to come.

But that is just the start of it. In addition to the more than $10 billion in state money, USASpending.gov estimated that state and local governments within Alabama received an additional $31 billion in direct payments from the federal government in fiscal year 2020. Direct payments go straight to government, to be used on a variety of programs such as transportation, education, and Medicaid.

When combined with contracts, grants, loans, and other financial assistance, it is estimated that state and local government as well as Alabama businesses and other entities received $63.3 billion in aid from the federal government. That is $12,910 in federal intervention for each man, woman, and child of the state. And it is on pace to eclipse that level by the end of fiscal year 2021.[102] But that number could be misleading. For example, those who are public sector employees or persons who receive public benefits are receiving much more than a private sector worker.

The per capita amount of federal funding coming to Alabama has grown by nearly $4,000 per person in just the last decade.[103] A 2020 report from the Tax Foundation identified Alabama as the 14th most dependent state when it comes to federal aid.[104]



To some, this may not sound like a bad thing. In theory, more federal aid means that a state can do more for its citizens. But it is not that simple. First, there is the principle that any level of government should be a good steward of the taxpayer resources that it takes in. Money from the federal government is not "free money." It is money that you, the taxpayer, have already paid to the federal government, or it is money that the federal government is borrowing in the form of greater short-term and future national debt.

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According to IRS data for fiscal year 2020, Alabama citizens and businesses sent $26.4 billion to Washington, D.C., in the form of taxes. Individual income taxes, employment taxes, and estate and trust taxes accounted for $24.9 billion with much of the rest coming from corporate income taxes.[105] For every dollar that taxpayers sent to the federal government, the state received approximately $1.25 back from the federal government through direct payments. If you add other federal spending – such as contracts, grants, and other federal assistance to public and private entities – to be included that total more than doubles to $2.54 per dollar.[106]

There is also the issue of what that money is going toward. With tens of billions of both state and federal government dollars flowing into the state, it makes it very hard to hold government and other recipients accountable for how that money is being used. This invariably leads to waste, fraud, and abuse of your money.

Even more troubling though is what the reliance on federal money means for the present and future. Money coming from the federal government comes with strings attached. In the simplest form, that may mean that Alabama must produce a matching share of funds to receive a pot of federal funding. But moreover, the federal government will restrict how federal funding (and the state matching portion) can be used. Much of the time federal agencies, not elected officials, determine the conditions for states receiving money as well as distribution of federal funds to state.

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Since the government controls currency and can print more money, the federal government will continue to send the flow of funding to states on a conditional basis. But the federal government is far from having its finances in perfect order. According to USDebtClock.org, gross federal debt already exceeds 125% of GDP. By 2026, gross debt is projected to rise to more than 177% of GDP, and that is assuming no new major crisis, stimulus bills, etc., occur over that period.[107]

Washington also has a major problem brewing in two programs that Alabamians certainly care about: Social Security and Medicare. The latest Social Security and Medicare Trustees Reports estimate that by 2033 Social Security's Old-Age and Survivors Insurance Trust Fund will no longer be able to pay full benefits. In just five years, 2026, it is estimated that the Medicare trust fund for inpatient care (Part A coverage) will be insolvent.[108]

These are both important issues to Alabama citizens dependent on Social Security and Medicare coverage. It is unlikely that Washington will undertake much needed and widespread reforms to these programs in the near term, but the insolvency issues must be dealt with. Future political and policy change in Washington could impact how much money Alabama gets from the federal government.

In the near term, the reliance on stimulus money is troubling. Take the Alabama Department of Education as an example. In total, state education programs will receive over $4.5 billion in stimulus funding resulting from the pandemic. While some of it is has been aimed strictly at pandemic response, much of it is not. In the meantime, the legislature and Governor Ivey approved a $1.25 billion debt spending package for education in 2020 as well as the largest Education Trust Fund budget ever for fiscal year 2022.

In short, education spending is being inflated to new heights, both through federal stimulus dollars and a lack of fiscal restraint from Alabama lawmakers. The stimulus funding will be spent and gone over the next few years. If state leaders are not careful in how they spend it, they may create a budget shortfall that cannot be covered by existing revenue streams. This could lead to negative impacts for both taxpayers and Alabama's students. The most likely outcome would be education budget cuts in the form of proration or additional tax increases on Alabama's citizens to pay for irresponsible budgeting.

Alabama has almost a billion dollars available to cover a temporary budget shortfall which puts it in better position to deal with economic contractions than many other states. But the wealth of federal spending in the state has given lawmakers little incentive to pursue fiscally responsible budgets. A prolonged recession could leave Alabama ill prepared to handle such a downturn and negatively impact citizens of the state.

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VII

IT IS TIME FOR CHANGE

KEY TAKEAWAYS

- **In general, the economies of the U.S. and Alabama have prospered. But that is not a reason to abandon sound fiscal principles. In good economic times, it is even more important to show budgeting restraint because more resources may be needed when there is a negative shift in the economy.**
- **Many of Alabama's elected leaders ran for office on the very principles that they seem to have disregarded. It is past time for lawmakers to implement policies representative of those core beliefs.**
- **Data shows that this is what most Alabamians want from their government.**
- **It is time that citizens demand a government that truly represents them and serves their best interests.**
- **If the current regime in Montgomery cannot or is unwilling to do that, then it is time for voters to show their dissatisfaction at the polls and elect lawmakers that will.**

Over the past few quadrennium, Alabama's state government has gotten away from its core principles of limited government, supporting a free market environment, and being responsible stewards of taxpayer dollars.

Part of that may be because of conditions outside of lawmakers' control. COVID-19 aside, the U.S. has not experienced a major economic downturn since the end of the "Great Recession" in 2009.[109] Alabama has not experienced a budget shortfall since 2012. In general, the economies of the U.S. and Alabama have prospered.

But that is not a reason to abandon sound fiscal principles. As the pandemic showed, a sudden economic downturn could happen at any time. A more prolonged downturn could be just around the corner. In good economic times it is even more important to show budgeting restraint because more resources may be needed when there is a negative shift in the economy.

VII It is Time for Change

By taking more money from Alabamians every year, the citizens that state lawmakers serve will have less savings and be less prepared when an economic contraction occurs. When those same tax revenues that are being taken by state government every day begin to shrink, the state may find itself unable to pay for the bloated programs and spending that it has created.

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Many of Alabama's elected leaders ran for office on the very principles that they seem to have disregarded. It is past time for lawmakers to implement policies representative of those core beliefs. Government should provide leadership and services to its people that private industry cannot or that are not financially feasible for private industry to provide. It should not be an ever-expanding enterprise.

Data shows that this is what most Alabamians want from their government. After all, government is supposed to serve the people of this state, not vice versa. It is time that citizens demand a government that truly represents them and serves their best interests. If the current regime in Montgomery cannot or is unwilling to do that, then it is time for voters to show their dissatisfaction at the polls and elect lawmakers that will.

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