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To: Senate Committee on Government Operations and Consumer Protection

From: Jon Peacock, Research Director  
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Re: **Opposition to SJR 55, which would constitutionally require the use of GAAP**

Chairperson Stroebel and Committee:

Thank you for this opportunity to testify about our concerns relating to SJR 55, which would establish a constitutional requirement to use Generally Accepted Accounting Principles (GAAP) in balancing the state budget.

I'm here on behalf of the Wisconsin Council on Children and Families (WCCF) where I'm the research director and I head up the work of a WCCF initiative known as the Wisconsin Budget Project. The Budget Project analyzes state fiscal issues, particularly those that affect low and middle-income families in our state. We have a strong interest in proposals that would affect the budget process and could change the state's capacity to ensure that there's adequate state and local funding to support services for children and families.

Before getting into our concerns about SJR 55, I want to commend the authors of this resolution for their interest in fiscally responsible and transparent budgeting. We share that interest, but we do not believe that putting a GAAP requirement into the state constitution is the prudent way to improve Wisconsin's budget practices.

To the best of my knowledge, approval of this constitutional amendment would make Wisconsin the only state to constitutionally require the use of GAAP for balancing the budget. I think there are a number of good reasons why other states don't have such requirements in their constitutions:

**Constitutionally requiring the use of GAAP for balancing the budget would tie the hands of state lawmakers.** – Economies are cyclical, and there will inevitably be recessions when revenue is down and spending needs are up. In the middle of a recession, the state doesn't want to have to raise taxes or cut spending. At times, other options – such as delaying a payment until the next biennium – may be the best choice. The need for choices like that may be even more important in coming years because the chances are diminishing that the next recession will bring a substantial infusion of federal funds. If we put GAAP standards into the constitution, there will be future recessions when spending will have to be cut for programs like BadgerCare and Wisconsin Works at the very time when more spending in those programs is especially important.

**SJR 55 would delegate to a private national organization the authority to set the parameters of Wisconsin's budget options.** – GAAP standards are not static. They are changed frequently by a private national organization – the Governmental Accounting Standards Board, known as GASB. Approval of the proposed constitutional change would mean that future changes in GAAP approved by GASB, with no involvement by Wisconsin lawmakers or their constituents, could restrict the options for balancing the state budget. At this point we have no idea what those changes might be. Rather than improving budget transparency and public involvement, an inflexible requirement to use GAAP would hurt democracy by making legislators and the governor less responsible and accountable for budget choices in Wisconsin.

**The proposed amendment might impede using money from the Rainy Day Fund during economic downturns, when it is needed most.** – My preliminary analysis of SJR 55 and material about GAAP raises a concern that an inflexible requirement to use it and to reduce the GAAP deficit each year might limit transfers from the state's Rainy Day Fund during economic downturns. However, I'm not certain that that's the case, and I urge the committee to take a careful look at that issue.

**The constitutional change wouldn't necessarily reduce structural deficits.** – GAAP budgeting is just a current snapshot of the budget; it doesn't preclude a number of practices that can yield large structural deficits, such as phased-in spending or tax cuts. In fact, the approval of SJR 55 might increase structural deficits in the short term because of the money that would have to be set aside in the next budget period to phase down the GAAP deficit.

**There are better ways to improve budgeting in Wisconsin.** – As I said at the outset, I commend legislators who are seeking to make state budgeting more transparent and more fiscally responsible; however, we think there are better ways to pursue those goals. First, Wisconsin could improve budget planning and transparency by establishing an improved method of calculating structural deficits (or balances), by measuring revenue projections against better estimates of the "current services" or base level budget, rather than against agency budget requests. In addition, those projections should look out four years, rather than just two.

Another option would be to adopt legislative rules requiring GAAP deficit estimates and the LFB's structural deficit calculations to be made public at each stage of the budget process, to enhance public understanding of how the budget is being balanced. More generally, I think we need more leadership from whichever party is in the majority to follow statutory requirements like adding money to the Rainy Day Fund when tax revenue exceeds expectations.

In closing, if you decide that it's important to use GAAP for balancing the state budget each year, I hope you will accomplish that by amending the statutes rather than the Wisconsin Constitution. Granted, we can all probably think of times when state lawmakers exempted themselves from statutes intended to achieve more prudent and fiscally responsible budgets, and those decisions make it tempting to want to move the requirements from the statutes to the state constitution. But, on balance, I think it is critical to remember that there will be future recessions or fiscal emergencies that create times when some budget latitude is urgently needed.

With those considerations in mind, I urge you not to make Wisconsin the first state to put a GAAP requirement into its constitution.



# WISCONSIN LEGISLATURE

P. O. Box 7882 Madison, WI 53707-7882

November 19, 2015

## JOINT TESTIMONY ON SENATE JOINT RESOLUTION 55

**Senators Howard Marklein, Chris Kapenga  
Representatives Dale Kooyenga, John Macco**

Thank you to Chairman Stroebel and the rest of the Senate Committee on Government Operations and Consumer Protection for the opportunity to jointly testify in favor of Senate Joint Resolution 55.

Currently in Wisconsin, the state does its budgeting and finances on a cash basis. This is not the same accounting method that is used by businesses, counties, cities, school districts, and townships. Every year, the state prepares a report on the basis of generally accepted accounting principles (GAAP), which shows that the state currently has a deficit.

The reason for the GAAP basis deficit is that the state has historically used a cash basis budget to “balance” its books. Over the years, it has led to all kinds of creative techniques to balance the cash basis books. Many of these “techniques” have been well publicized. They have used the sale of the tobacco settlement, raided the Transportation Fund, raided the Patient Compensation Fund, withheld reciprocity payments to Minnesota, delayed state aid to school districts, among other things.

The path that we were on was unsustainable. By the end of fiscal year 2011, the general fund deficit had grown to nearly \$3 billion! People were taking notice of these budgeting gimmicks. The bond rating agencies in New York were concerned about these deficits and it had a negative impact on our bond rating.

Tremendous progress has been made in the last four years. In 2011, the Wisconsin GAAP deficit stood at \$2.9 billion and by the end of fiscal year 2014, the GAAP deficit has decreased 52% to \$1.4 billion. The decrease represents the fact that Wisconsin has made significant progress in achieving solvency and more honest accounting practices.

There is still more work to be done. We believe the only permanent solution is to have the voters in Wisconsin approve an amendment to the state constitution that will require future legislatures and governors to budget on the basis of generally accepted accounting principles. In essence, this amendment would require the state to budget the same way that businesses, school districts, counties, townships, cities, and villages budget. We should live by the same rules as our constituents. The joint resolution also requires that any GAAP-based deficit affected by a budget bill be reduced annually by 10% of any projected increase in tax revenues in that fund. Once the deficit has been eliminated, the legislature would not be able to pass any legislation that results in a budget deficit.

We would be happy to take questions from the committee at this time.