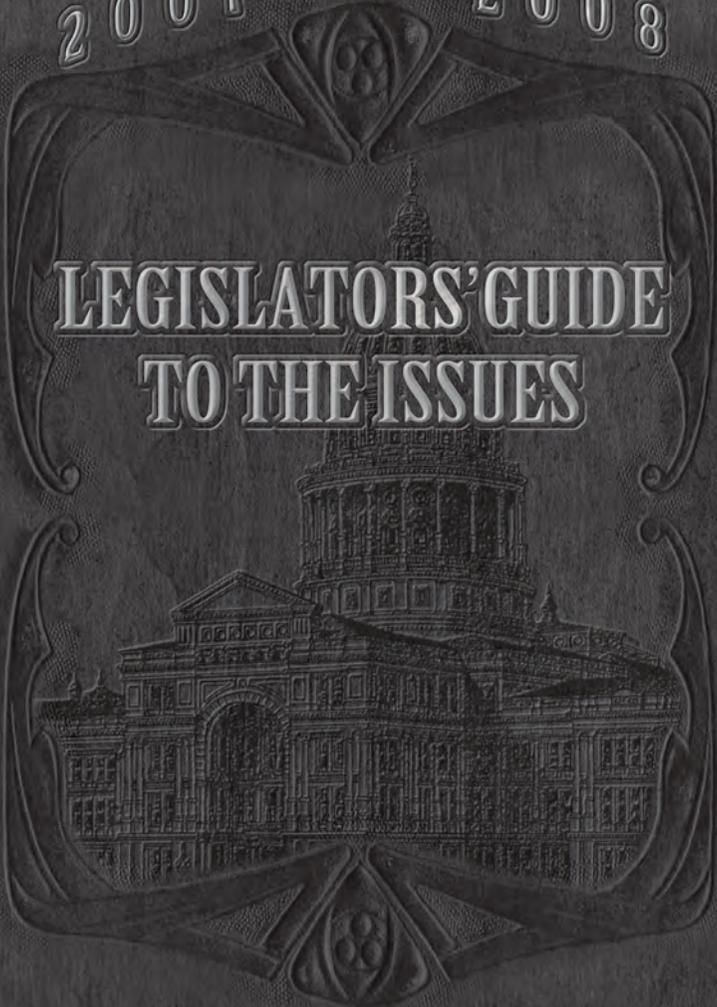


2007 ★ 2008

LEGISLATORS' GUIDE
TO THE ISSUES



★
Texas Public Policy
Foundation

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~ RONALD REAGAN

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TEXAS PUBLIC POLICY FOUNDATION

2007-2008
Legislators'
GUIDE TO THE ISSUES

Edited by Bill Peacock
Texas Public Policy Foundation



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“*History does not long entrust the care of
freedom to the weak or the timid.*”

~ DWIGHT D. EISENHOWER

When considering the challenges facing the world of 2007, President Eisenhower's insight still rings true. Courage is required to challenge the status quo, and only a firm, steady resolve allows us to overcome the weight of complacency.

But even the most courageous and resolute will ultimately fail in their efforts to improve the cause of liberty if they are not well armed and properly prepared.

This third installment of our popular *Legislators' Guide to the Issues*, the 2007-2008 edition, is designed to do just that. This book couples the sound research conducted by the Foundation's experts with practical policy recommendations. In this way, we hope to provide lawmakers, opinion leaders and the general public with the tools needed to govern in the 21st Century. In the 19th and 20th centuries, Texas' economic competitors were Oklahoma, California and Mexico. Today our competitors for jobs and investment include countries in formerly remote corners of the world such as India, China, Singapore and Africa.

Scottish historian Alexander Fraser pessimistically reported in the 18th Century that the history of great civilizations took them “[f]rom bondage to spiritual faith; from spiritual faith to great courage; from courage to liberty; from liberty to abundance; from abundance to selfishness; from selfishness to complacency; from complacency to apathy; from apathy to dependency; from dependency back again to bondage.”

If the Lone Star State is to run counter to Fraser's view of history and continue to be a brightly shining economic beacon in the world, we must set aside selfish complacency and courageously pursue sound, research-based policies that empower individuals, liberate the market, and promote prosperity.

The Foundation looks forward to standing with you as we labor together for Texas' bright and boundless future.



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THE ISSUE

Some policymakers have proposed establishing an income tax to provide increased revenue for expanding government services. Advocates of the personal income tax claim that a tax system is a “three-legged stool,” but the third leg—an income tax—is missing in Texas. They claim the absence of an income tax prevents Texas from raising sufficient revenue and that current revenue sources are insufficient as spending needs grow. While such claims are unfounded, demands for increased state funding for health care and education stimulate periodic discussions about the efficacy of the income tax.

While an income tax could provide more revenue for the state, an increase in any other tax could accomplish the same. However, because the income tax relies on such a volatile base, it is a more unstable source of revenue than many other taxes. In addition, an income tax would bring with it adverse impacts on the Texas economy.

In fact, the absence of an income tax has been the primary reason for Texas’ prosperity in recent decades. The experience of states with income taxes demonstrates they are particularly pernicious in their adverse economic impact. This experience is mirrored internationally; analysis of 23 other nations indicates the increase in revenue raised by taxing income has a negative correlation with economic growth.

In other words, the income tax damages an economy. The overall tax burden increases more rapidly in states with taxes on income, and state spending in income tax states exceeds that of states without an income tax.

THE FACTS

- ★ Income taxes have the most adverse economic impact of all tax systems—depressing capital investment, production, business expansion, job creation, wages, and living standards.
- ★ Texas is one of seven states without a personal income tax.
- ★ Twelve states that implemented income taxes during 1957-1999 experienced an average 37.2 percent overall increase in taxes compared to 10.5 percent in states without income taxes.
- ★ States with an income tax spend more than states without an income tax.
- ★ Income taxes lead to high levels of taxation that “crowd out” more productive economic activity in the private sector.
- ★ All taxes ALWAYS more negatively affect those with low incomes.



RECOMMENDATIONS

- ★ Do not create a personal income tax in Texas.
- ★ Do not expand the revised franchise tax by broadening it or increasing the rates.

RESOURCES

- *Taxing Texans Part 1: The Worst Tax for Texans?* by Richard Vedder, Texas Public Policy Foundation (Feb. 2002) <http://www.texaspolicy.com/pdf/2002-02-28-tax-taxingtexans1.pdf>.
- *Taxing Texans Part 2: The Effect of Taxes on Economic Growth* by Richard Vedder, Texas Public Policy Foundation (Mar. 2002) <http://www.texaspolicy.com/pdf/2002-03-29-tax-taxingtexans2.pdf>.
- *Taxing Texans Part 6: Does Bigger Government Help the Poor?* by Richard Vedder, Texas Public Policy Foundation (Oct. 2002) <http://www.texaspolicy.com/pdf/2002-10-29-tax-taxingtexans6.pdf>.
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THE ISSUE

One of Texas' biggest economic strengths is the state's reliance on the sales tax to fund state and local government. The greatest virtue of a sales tax is that it does not directly impede investment, work effort, or job creation. Compared to the alternatives, the sales tax is more visible to taxpayers, simpler, less intrusive, and less subject to manipulation. The sales tax has proven to be a stable and robust source of revenue for the state, growing faster than the sum of the population growth rate and inflation.

The sales tax, however, gets a major black eye from those who claim to advocate for low-income individuals. They claim the sales tax is regressive, and that it does not and cannot meet the needs of the state.

Measured in terms of economic progress, the sales tax is a relatively desirable tax. States that depend on it instead of the income tax, which is considered progressive, have seen healthier economies and stronger fiscal situations when faced with the inevitable downturns. Truly progressive policy is that which creates the greatest possible economic opportunities for individuals at all income levels. Compared to other tax systems, the sales tax is part of just such progressive policy. Sales tax transparency helps to keep the tax and government burden low, promoting economic opportunity.

Sales tax revenues have consistently grown, even when the sales tax rate and base have remained constant. Nevertheless, it is true that the sales tax has not kept up with state-financed expenditures. What this points to, however, is a spending problem rather than a revenue problem. State expenditures, net of federal revenues, have consistently grown 2 percentage points faster than population growth plus inflation. (See *Spending Priorities and Expenditure Limits*, pages 20-23.)

The current sales tax is also criticized as being outdated. Many services that constitute an increasing share of the state's economy are not taxed by the sales tax. This criticism is not justified where services are provided by one business for another business. However, the economy is distorted to the extent that some final consumer goods and services are exempted or otherwise not taxed under the sales tax. Many goods and services, such as car washes, newspapers, and interior decorating services, could be included in the sales tax.

Any broadening of the sales tax—or any other change that would result in greater revenues—should be offset by reductions in other taxes. While it is possible the sales tax could be broadened and the rate reduced to offset the increased revenues, it might be more prudent to reduce other taxes, such as the property tax or the revised franchise tax.

THE FACTS

- ★ The sales tax is simple, easy to understand, relatively easy to administer, and has low taxpayer compliance costs.



- ★ The sales tax does not directly tax work, job creation, or investment.
- ★ The sales tax is transparent—i.e., it is not hidden from those who pay it.
- ★ The sales tax can be easily applied regardless of the types of industries that prevail in the state.
- ★ Fifteen states tax the sale of food; 13 states tax the sale of non-prescription drugs.
- ★ Only five states have no sales tax at all.
- ★ Texas is tied with California with the seventh highest weighted average state and local sales tax rate—7.95 percent. Tennessee has the highest weighted average state and local sales tax rate at 9.4 percent.
- ★ Texas has the sixth highest state sales tax rate, at 6.25 percent; the highest in the nation is 7 percent.

RECOMMENDATIONS

- ★ Should the legislature determine that more state revenue is needed in order to offset cuts in other types of taxes, it should broaden the sales tax.
- ★ The sales tax could be broadened to final goods and services which are currently exempted or excluded, allowing a decrease in the sales tax rate as well as decreases in other taxes.
- ★ Some controversial final goods and services could be taxed at a lower rate in order to reduce concerns about regressivity.
- ★ Any broadening of the sales tax that produces more revenue for local entities should be offset with property tax reductions.
- ★ Increases in the sales tax rate should be offset with reductions in other taxes and should be very modest.

RESOURCES

- *Virtues of a Consumption Tax* by Byron Schlomach, Texas Public Policy Foundation (Mar. 2006) <http://www.texaspolicy.com/pdf/2006-03-testimony-bs.pdf>.
- *All Taxes Are Not Created Equal* by Byron Schlomach, Texas Public Policy Foundation (Feb. 2006) <http://www.texaspolicy.com/pdf/2006-02-PP-consumptiontax-BS.pdf>.
- *The Best Tax Plan For Texas*, Texas Public Policy Foundation (May 2005) <http://www.texaspolicy.com/pdf/2005-05-taxplan.pdf>.
- *An Economic Analysis Of Property Tax Relief Funded By A Sales Tax Increase* by Milton L. Holloway, Texas Public Policy Foundation (Apr. 2004) <http://www.texaspolicy.com/pdf/2004-04-sales-property-tax.pdf>.

THE ISSUE

Businesses do not pay taxes. Only people do—in lost jobs, lost wages, lost profits, and higher prices.

Nevertheless, it does make a difference how and what types of taxes are levied in an economy. Human beings do react to incentives, and taxes are negative incentives. Business taxes directly penalize certain productive activity including hard work, capital investment, job creation, and thrift. Property taxes penalize capital investment and property development. Anything that is taxed—i.e., penalized—will be reduced; that is, compared to what they would do otherwise, people will avoid taxed activities.

A society and its members are made prosperous through productive activity. Therefore, the last thing government should do is tax it. When productive activity shrinks, so do job opportunities, and when job opportunities shrink those who are least skilled are the first to feel the effects. Business taxes hurt low-income individuals more than anyone else through lost employment opportunities.

Unfortunately, Texas has one of the highest state and local business tax burdens in the nation, when direct business taxes are measured as a percentage of gross state product. According to the Council on State Taxation, Texas currently has the 11th highest business tax burden. That ranking will likely rise with the implementation of the revised franchise tax in 2008, even though the reduction in the property tax will significantly accrue to the benefit of business.

THE FACTS

- ★ Of the 60 taxes, fees, and assessments in the Comptroller's Sources of Revenue Growth report, at least 39 are derived in whole or in part directly from Texas businesses; this includes a substantial portion of the sales tax.
- ★ According to the Council on State Taxation, state and local taxes directly on business constitute 5.6 percent of Texas' gross state product.
- ★ Texas' business tax burden is greater than that of California, Massachusetts, Michigan, and Florida.
- ★ Only three states see a higher proportion of their revenues come from state and local business taxes than Texas.
- ★ Sixty-one percent of state and local tax proceeds in Texas come directly from business.
- ★ More than half of the revenue raised by the six major state and local taxes analyzed by the Texas Comptroller in the Tax Exemptions and Tax Incidence report comes from business.



RECOMMENDATIONS

- ★ Further increases in direct business taxes should be avoided.
- ★ State-level business taxes should be gradually repealed with lost revenues financed either from future surpluses or changes to the sales tax rate or application.
- ★ Reductions in business taxes should NOT be accomplished through targeted tax credits but through general decreases and repeals.
- ★ If the revised franchise tax collects more than was anticipated, the tax rate should be reduced.

RESOURCES

- *All Taxes Are Not Created Equal* by Byron Schlomach, Texas Public Policy Foundation (Feb. 2006) <http://www.texaspolicy.com/pdf/2006-02-PP-consumptiontax-BS.pdf>.
- *The Business of Taxing Business* by Byron Schlomach, Texas Public Policy Foundation (Nov. 2005) <http://www.texaspolicy.com/pdf/PP14-2005-taxingbusiness.pdf>.
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- *Total State and Local Business Taxes* by Robert Cline, Tom Neubig, and Andrew Phillips, Ernst & Young LLP, Council on State Taxation (Mar. 2006) http://www.statetax.org/Content/ContentGroups/Home_Page_Content/COST_Studies,_Articles_and_Testimony/50StateTaxStudyMarch2006.pdf.
- *Tax Exemptions & Tax Incidence* by Texas Comptroller of Public Accounts (Jan. 2005) <http://www.window.state.tx.us/taxinfo/incidence05/>.

THE ISSUE

School taxes represent the bulk of property tax bills, while county and city taxes make up much of the rest. The school portion, however, has increased most rapidly, creating a double squeeze on taxpayers as property values and tax rates have risen simultaneously.

Property taxes at the city and county levels, and for many special districts, have a rational basis in that property ownership is somewhat correlated with demand for services from these entities. Property taxes for education have less of a rational basis, since the value of real property owned bears little relationship to demand for education services.

The school tax issue is further complicated by the complex nature of the school funding system and repeated lawsuits against the state over issues surrounding the school property tax. Large differences in property values across school districts and the Edgewood court decisions have necessitated the creation of the so-called “Robin Hood” school funding system. This system almost inevitably leads to a de facto statewide property tax, which the Texas Supreme Court has also ruled unconstitutional.

For these reasons—the rising school property tax burden, the lack of a rational link between school property taxes and educational services, and the constitutional complexities surrounding the school property tax—many believe it is necessary to substantially reduce, if not eliminate, school property taxes.

During the Third Called Session of the 79th Legislature, substantial reductions in the school property tax were enacted. Using a large portion of the state’s regularly-occurring surplus, a mandated reduction of seventeen cents in property tax rates was offset with state funds.

Even before the special session, it was calculated that if the growth in state-funded expenditures were limited to the sum of population growth and inflation, and if school expenditures were similarly limited, the school M&O property tax could be reduced to zero within two decades. This could be accomplished just by slowing the growth of state expenditures. With the school property tax reduced substantially by 2008, this could be accomplished even more quickly, and using future surplus windfalls for property tax reduction would even more swiftly accomplish this task.

THE FACTS

- ★ In fiscal year 2004, Texas ranked 13th in per capita local property tax collections at \$1,254.
- ★ In 2004, property taxes comprised 43.5 percent of all state and local taxes in Texas; only New Jersey and New Hampshire depended more heavily on property taxes.



- ★ The property tax is strictly a locally-determined tax in Texas; this is true of only 12 other states.
- ★ Of all state and local in-state revenues, state revenues in Texas comprise only 47.7 percent of the total, the third lowest percentage among the states.
- ★ Property taxes raise more money in Texas than any other tax, including the sales tax.
- ★ There is substantial evidence that some local funding for education is associated with better school performance than if there is no local funding source.

RECOMMENDATIONS

- ★ Use future state surpluses to fund reductions in school M&O property tax rates.
- ★ Maintain a local share of school funding.
- ★ Make property tax reductions more substantial by implementing stricter expenditure limits at the state and local levels.
- ★ If any tax is increased in order to reduce property taxes, it should be the sales tax; no other tax should be created or increased for the sake of property tax relief.

RESOURCES

- *Putting The Sides Together: Twelve Perspectives On Texas Public School Finance* edited by Chris Patterson, Texas Public Policy Foundation (Dec. 2003) <http://www.texaspolicy.com/pdf/2003-12-sf2.pdf>.
- *Splitting The Difference: Residential And Business Property Taxes In Texas* by Byron Schломach, Texas Public Policy Foundation (Jan. 2004) <http://www.texaspolicy.com/pdf/2004-01-26-sf-splitroll.pdf>.
- *Effective, Efficient, Fair: Paying For Public Education In Texas* by Richard Vedder and Joshua Hall, Texas Public Policy Foundation (Feb. 2004) <http://www.texaspolicy.com/pdf/2004-02-25-vedderhall-all.pdf>.
- *Follow The Money: A 50-State Survey Of Public Education Dollars* by Chris Patterson, Texas Public Policy Foundation (Oct. 2003) <http://www.texaspolicy.com/pdf/2003-10-22-sf-followmoney.pdf>.

THE ISSUE

Any time a change in the state's tax structure is contemplated, the first issue brought to the attention of decision makers is how it will affect Texans at various income levels. Texas' current tax structure is often derided as "regressive." That is, lower-income households allegedly pay a greater share of their income in state and local taxes than do higher-income households. So-called "progressive" tax policies would have higher-income households paying a higher percentage of their incomes in taxes than would lower-income households.

Any tax based on purchases of goods and services, such as the sales tax, is likely to be regressive as measured by prevailing methods. At best, those who measure tax incidence—a measure of who truly bears the burden of a tax—can observe who directly pays a tax to government, surmise some share borne by consumers, producers, and employees, and attempt to build into the analysis some dynamic economic effects. Long-term effects such as growth rates, investment, and population migration are virtually impossible to quantitatively forecast and measure accurately even though such qualitative effects are easily predictable.

The best example of the law of unintended effects, with respect to tax incidence, is the short-lived federal luxury tax. Intended as a tax on the rich, the burden was actually borne by low and middle-income Americans who worked in targeted luxury industries. Though it could be predicted that high-income Americans would reduce purchases of luxury items, the exact degree of reaction could not be predicted. In the end, while the exact cost of this failed tax policy cannot be calculated, it was much higher than the amount of tax collected and the rich bore little of it.

The only tax that is generally considered "progressive" is the progressive income tax. This tax is invariably associated with relatively stagnant economic growth, out-migration of individuals who would otherwise invest in an economy, and disincentives to work, invest, and create jobs. The more steeply progressive this tax is, the worse its effects.

Every type of tax is a drag on an economy. Those most negatively affected by factors negatively impacting an economy are those with low incomes. Therefore, since government—and thus taxes—are necessary, the most truly progressive tax policy is that which does the least harm to the economy as a whole. But popular notions of what constitutes a "regressive" or "progressive" tax ignore this and prove harmful when allowed to permeate policy discussions about taxation.

More care must be taken in analyzing tax recommendations to ensure their long-term effects and their unintended consequences are carefully considered and fully understood.



THE FACTS

- ★ The franchise tax, on average, is measured as more regressive than the sales tax by the Comptroller's Office.
- ★ The federal luxury tax, intended as a tax on the rich, was actually a tax on low and middle income jobs in luxury industries.
- ★ Attempts to achieve "fairness" by taxing high incomes and businesses backfire by reducing investment and job availability.
- ★ Due to the complexity of our economy and human behavior, measures of regressivity and progressivity of taxes cannot take long-term dynamic effects into account and provide no meaningful input into policy debates on taxation.
- ★ ALL taxes ALWAYS more negatively affect those with low incomes.

RECOMMENDATIONS

- ★ Legislative committees should stop requesting so-called "Tax Equity Notes" from the Legislative Budget Board.
- ★ Tax policy should largely be based on its overall economic effects, recognizing that the goal is to minimize economic harm.
- ★ Institute strict tax-limiting measures to minimize harm to the economy—i.e., reduce the size of state and local government.

RESOURCES

- *Progressive or Regressive, Is That Really The Question?* by Byron Schломach, Texas Public Policy Foundation (Mar. 2006) <http://www.texaspolicy.com/pdf/2006-02-PP-taxincidence-bs.pdf>.
- *A Tax On One Is A Tax On All* by Byron Schломach, Texas Public Policy Foundation (Jan. 2005) <http://www.texaspolicy.com/pdf/2005-01-taxes.pdf>.
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- *Tax Exemptions & Tax Incidence: A Report to the Governor and the 79th Texas Legislature* by the Texas Comptroller (Jan. 2005) <http://www.texaspolicy.com/pdf/2002-10-29-tax-taxingtexans6.pdf>.



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There is no doubt that some expenditures in the state budget are higher priorities than others. Public education, higher education, and health care spending always take center stage in terms of the attention they receive because of their sheer size. Other pieces of the budget, such as criminal justice, the judiciary, and roads, are funded as a matter of course.

Regardless of whether state revenues are growing at a high rate or low rate, resources are finite and therefore choices must be made. Should more prisons be constructed, or should teachers receive a pay raise? Should more funds be devoted to health care where there is a federal match, or should higher education receive more funding?

A dollar devoted to one area in the state budget is a dollar that cannot be devoted to another. Therefore, priorities must be determined, but there has been no clear, consistent set of principles guiding budget development. Thus, taxpayers are left without a meaningful way to assess the efficacy of the use of tax dollars. Additionally, the system in place makes it easier for funds to be spent frivolously without accountability.

Lawmakers must first ask fundamental questions to determine if a program or agency should be funded at all, such as:

- ★ Is a program/agency consistent with the mission of Texas' state government?
- ★ Are the benefits from a program or agency unambiguous and universal?
- ★ Do the benefits of a program or agency clearly outweigh the costs?
- ★ Is the program or agency fulfilling a need only government can fill?
- ★ Does an existing program or agency show evidence of past success?

If an agency's or program's existence can be justified, lawmakers must then ask questions to help them determine which of these should get priority in receiving funding that will ALWAYS be limited. These questions might include:

- ★ Does a program or agency protect private property?
- ★ Does it protect individual liberty?
- ★ Does it enhance private enterprise?
- ★ How difficult is it to measure the performance of a program or agency?
- ★ How well does an agency's performance stack up compared to others?
- ★ How well does the success of a program or agency stack up over time?
- ★ Is there evidence that continued or increased funding will significantly improve or maintain outcomes?



- ★ Are the general benefits of a program evenly distributed across the state?
- ★ Does a program or agency exist only for the sake of gaining federal funds?
- ★ Is the program's existence owed to the fact that other states fund similar programs?

THE FACTS

- ★ There is no clear, consistent set of budgeting principles for determining spending priorities regularly followed by the Texas Legislature.
- ★ Relative expenditure levels among the major categories of the budget seem to vary most according to whether federal funds can be gained from additional state spending.

RECOMMENDATIONS

- ★ Adopt a set of budgeting principles that guide budgeting decisions.
- ★ Budgeting principles should not allow for the possibility of funding something just because it has been funded in the past.
- ★ The first budgeting principle should be to fund only those functions or programs that clearly benefit all Texans; the benefits must clearly outweigh the costs of any given program.

RESOURCES

- *Principles for Determining Budget Priorities* by Talmadge Heflin and Byron Schломach, Texas Public Policy Foundation (July 2006) <http://www.texaspolicy.com/pdf/2006-07-PP-budgetpriorities-bsth.pdf>.
- *Four Principles of Budget Process Reform* by Brian M. Riedl and Alison Fraser, Heritage Foundation (Apr. 2004) <http://www.heritage.org/Research/Budget/bg1746.cfm>.
- *Statement of Principles: California Budget and Tax Reform Initiative* by Joint Venture: Silicon Valley Network and Bay Area Economic Forum (Feb. 2004) <http://www.jointventure.org/PDF/StatementofPrinciples.pdf>.
- *Stewardship Series part I: Core Governing Principles* by Evergreen Freedom Foundation (Mar. 2000) http://www.ewfa.org/main/article.php?article_id=363.

THE ISSUE

The Third Called Session of the 79th Legislature saw the state come very near its expenditure limit as determined by the Legislative Budget Board (LBB). According to the LBB, the state was only \$80 million short of its expenditure limit after appropriating additional funds to education for property tax relief and other purposes. In order for appropriations from state tax sources for the 2006-2007 biennium to grow by more than \$80 million in a supplemental appropriation, the legislature will have to vote to declare an emergency.

This is perhaps one of only a few times Texas' expenditure limit, enacted constitutionally in 1978, has served as a significant limit on state expenditures. Interestingly, it served more to limit property tax relief than anything else. Why? Because property taxes are local taxes, so state expenditures (that is, state funding of local school districts) had to increase in order for local school taxes to be reduced.

More than half of the states have some form of expenditure limits. Texas has one of the weakest. By limiting government's growth to that of the economy, it allows government to maintain a share of the economy that cannot be justified given increasing prosperity.

Texas' expenditure limit law, in the constitution and in statute, falls short for the following reasons:

- ★ Lacks sufficient constitutional specificity by requiring easily amended enabling legislation;
- ★ Applies to less than half of the state budget;
- ★ Bases caps on predicted growth rates rather than actual growth rates;
- ★ Limits appropriations growth to personal income growth rather than the sum of population growth and inflation;
- ★ Allows a simple legislative majority to overrule the limit;
- ★ Applies only to the state, not including local governments;
- ★ Provides no automatic provision for tax refunds, rebates, or reductions.

THE FACTS

- ★ Thirty states have some type of tax and/or expenditure limit, with Colorado's generally considered the most effective.
- ★ Colorado's expenditure limit resulted in \$3.25 billion in tax rebates to Colorado residents from 1997 to 2001.
- ★ Real, per capita, non-federal Texas state expenditures increased almost 25 percent from 1990 to 2005—this does not include spending in the public schools that crowded out state funding due to property value increases.



- ★ States with effective spending limitations experience lower tax increases in periods of recession than states without such limitations.

RECOMMENDATIONS

- ★ Amend the state's expenditure limit to apply to expenditures made from all state revenues.
- ★ Amend the state's expenditure limit to allow growth at the same rate as the sum of population growth and inflation.
- ★ Fully enact the state's expenditure limit in the constitution rather than depending on statutory enabling provisions.
- ★ Enact an expenditure limit for local governments, limiting expenditure growth to inflation plus the growth of the populations they serve.
- ★ Account for how property valuation increases reduce the share of state funding in public education, at least in reporting by the LBB.

RESOURCES

- *Tax and Expenditure Limitation Reform: Is It Needed in Texas?* by Byron Schломach, Texas Public Policy Foundation (Aug. 2004) <http://www.texaspolicy.com/pdf/2004-08-TEL.pdf>.
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THE ISSUE

The Texas Constitution's Article 4, Section 14 grants to the governor power to veto items of appropriation. This is understood to be specific line items in the state's budget or appropriations act. However, nothing in the constitution defines what should be included in a single line item.

One reason for the line-item veto power is that the governor's perspective is generally less parochial than that of legislators. With respect to appropriations, the governor presides as an additional budget control, able to judge programs from a broader perspective, and presumably act for the benefit of state taxpayers as a whole.

The current format of appropriations bills makes it difficult—almost impossible—for the governor to exercise the constitutional authority granted that office. The legislature regularly rolls several programs into single items of appropriation so the governor cannot veto one wasteful, parochial program without also vetoing crucial ones.

Since the budget is often one of the last bills passed during a regular legislative session, it is impossible for the governor to issue a veto proclamation in time for the legislature to reconsider the bill and possibly re-enact crucial programs. Therefore, the governor's line-item veto authority can be severely limited just by what legislators choose to include in a single line of appropriation.

Additionally, riders that direct how money should be spent from a particular line item cannot be vetoed.

THE FACTS

- ★ Many items of appropriation fund multiple programs.
- ★ The governor can only veto an item as it appears in the appropriations act, even when it is known the item funds several programs.
- ★ The governor cannot veto a rider except when one separately appropriates funds (such as contingency riders).
- ★ The governor may only delete line items; the governor may not substitute other amounts for those already in the appropriations act.



RECOMMENDATIONS

- ★ The governor's office should be integrally involved in the appropriations process in both bodies of the legislature from the beginning of a session.
- ★ The practice of using riders to direct that funds from specific line items be spent on specific projects should be eliminated; instead, these projects should appear as separate line items in the budget.
- ★ The appropriations act should be broken down according to specific programs instead of the broader "goals" and "strategies" that currently appear in the budget.

RESOURCES

- *Impact of the Texas Governor on the State Budget* by Talmadge Heflin, Texas Public Policy Foundation (Apr. 2006) <http://www.texaspolicy.com/pdf/2006-04-PP-GovBudget-II-th.pdf>.

THE ISSUE

Most government programs are probably well-intended. Original intentions, however, are not the test of whether a program should continue in a given incarnation or at all. Instead, every program should have measures associated with it that gauge its success. Success is not merely the proper expenditure of funds for activities associated with a program. Success must be measured by real, measurable results.

For example, a road agency can measure how many lane miles it constructs or it can measure the mobility of the population and how its road construction and maintenance affects that mobility. The former measures activity. The latter measures results. Another example is the many tourism-related programs spread throughout the state budget. All should be judged by whether more Texans choose to vacation within the state. Instead, they are measured based on activity rather than whether they aid in attaining a specific goal.

Too much of what is reported to the Texas Legislature is activity rather than results. Legislators must demand performance measures more meaningful than the ones that are currently used in the budget process.

To the greatest extent possible, performance measures must examine what an average dollar spent on a program is buying. In three pages and dozens of measures associated with the Texas Education Agency in the appropriations act, only five take tax dollars into account with average cost measures. None attempt to measure the cost of a given amount of educational attainment. For example, cost-per-student performing at grade level could be calculated, and serve as a measure for success.

Programs must be constantly monitored for success, measuring not just “bang” but “bang for the buck.” Programs that do not show success or that cannot be measured for success must be discontinued. Only in this way can taxpayers be assured that their dollars are spent well.

THE FACTS

- ★ The current budget format in the appropriations bill includes outcome and efficiency measures for every agency.
- ★ Outcome and efficiency measures in the budget are not in an historical context and therefore are of questionable value in the budget itself.
- ★ Few of the outcome and efficiency measures in the Texas budget measure output per taxpayer dollar.



RECOMMENDATIONS

- ★ Reconfigure the state budget to reference a separate document that includes historical performance data.
- ★ Refocus performance data on outcomes rather than activities of agencies; current “outcome” measures mainly measure activity.
- ★ Create outcome measures that put accomplishment in the context of cost.

RESOURCES

- *Demanding Performance Part I: State & Agency Missions* by Talmadge Heflin and Byron Schlomach, Texas Public Policy Foundation (Aug. 2006) <http://www.texaspolicy.com/pdf/2006-08-PP-demandperformanceI-bsth.pdf>.
- *Demanding Performance Part II: Outcomes & Efficiencies* by Talmadge Heflin and Byron Schlomach, Texas Public Policy Foundation (Aug. 2006) <http://www.texaspolicy.com/pdf/2006-08-PP-demandperformanceII-bsth.pdf>.
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- *Best Practices for Output Performance Measures (Appendix)* New Zealand Treasury (1995) <http://www.treasury.govt.nz/publicsector/pag/default.asp>.



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THE ISSUE

School finance has been a major focus of the Legislature for the past several regular and special sessions. Most recently, it took center stage during the May 2006 special session, when lawmakers successfully met the Supreme Court's directive to give local districts meaningful discretion over school property taxes.

While the Court's June 1st deadline was met, school finance will continue to be at the forefront of legislative and public debate. If history is any indication, increases in school spending will continue to outpace enrollment and inflation growth, and the state will find itself back in court in a few years.

Because the state's obligations for funding public education are only loosely defined in the Constitution, terms such as "general diffusion of knowledge," "suitable provision," and "efficient system" have been left to interpretation by the courts. As a result, the school accountability system has been turned on its head. Whereas the accountability system was originally created to ensure that taxpayer-funded schools produced results, that same system is now being used to demand more dollars from taxpayers. The Legislature has a great opportunity to define the constitutional terms in statute, thus restoring its authority over education funding, and protecting taxpayers from further school finance lawsuits.

Just as the flip side of revenue is costs, the other concern with regard to school finance is spending—the way schools use their money. Less than two-thirds of education dollars make it to the classroom in Texas. And while there is no demonstrated correlation between overall school spending and student achievement, there is evidence to suggest that *how* schools spend money can have an impact.

Unfortunately, parents and taxpayers are discouraged from examining how their tax dollars are spent. While financial data is plentiful, it is difficult to access, navigate, and comprehend. House Bill 1, signed into law in June 2006, made great strides in increasing financial transparency, and also improving efficiency through means such as shared services. When taxpayers fully understand how school dollars are being spent, school districts will be held more accountable for spending, and more dollars will reach the classroom. And when classroom spending is a priority, both students and teachers benefit.

THE FACTS

- ★ Texas' education system costs more than \$10,000 annually per student.
- ★ Texas ranks 2nd among the 10 most populous states, or 12th among all 50 states, in K-12 total revenues and receipts per student when adjusted for cost of living.
- ★ In each of the last three decades, spending per student in Texas has increased by at least 20 percent over and above increases for inflation and enrollment.



- ★ In 2003, Texas ranked third among the 50 states in public education expenditures as a percent of total state expenditures—27 percent of the total state budget.
- ★ In a four state study, including Texas, high performing districts spent more of total funds on student instruction than lower performing districts, and spent relatively less on general administration and staff.

RECOMMENDATIONS

- ★ Define constitutional obligations for public education.
- ★ Protect and enhance local control.
- ★ Establish student-centered funding.
- ★ Tie new money for public education to enrollment growth and inflation.
- ★ Let scientific research on spending and learning guide school finance reform.
- ★ Continue increasing financial transparency so that parents and taxpayers can better hold schools accountable for spending and learning.

RESOURCES

- *Transparency for Taxpayers, Success For Students* by Jamie Story, Texas Public Policy Foundation (May 2006) <http://www.texaspolicy.com/pdf/2006-05-PB-edspending-js.pdf>.
- *Rhetoric Is Clouding the Facts: Legislature Must Be Cautious of Distortions* by Jamie Story, Texas Public Policy Foundation (Mar. 2006) <http://www.texaspolicy.com/pdf/2006-03-edspendingfacts-js.pdf>.
- *Spending and Learning: What Does the Research Say?* by Chris Patterson, Texas Public Policy Foundation (Nov. 2005) <http://www.texaspolicy.com/pdf/2005-10-25-65spending-pb.pdf>.
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THE ISSUE

The public school system is a monopoly. Parents and students, as consumers, have no choice about where their tax dollars go, so schools face no economic incentive to provide a high-quality product. Faced with a poorly-performing local school, a family's only alternatives are to move or attend a private school. Parents who choose to send their children to private schools not only pay tuition, but forego the taxpayer-funded school dollars originally designated for their child.

With this entrenched monopoly, it is no wonder schools have failed to significantly improve, despite a host of expensive reforms. The deadweight loss produced by monopoly cannot be regulated or legislated into productivity. Competition is the ultimate means of improving public education, and competition is best implemented through school choice. School choice must be understood to include both those who choose a non-traditional public school, as well as those who remain within the current system.

The effects of school choice must be measured for both groups. The preponderance of data from research in the United States and abroad indicates positive effects across-the-board.

Random-assignment studies of voucher programs in Charlotte, SC, Dayton, OH, Milwaukee, WI, New York, NY, and Washington, DC, all demonstrate positive benefits for voucher recipients. Similarly, the evidence suggests that public schools facing competition from vouchers and/or charter schools also improve, a positive development for students remaining in those institutions. Most evidence actually finds that school choice improves, rather than discourages, racial integration.

Not only is school choice good for students, it can also revolutionize the teaching profession. The public school monopoly ensures that all teachers are paid essentially the same, regardless of excellence or effort. In order to receive a pay raise, a teacher must move to a higher-paying district or private school, attain an additional degree, or leave the profession. With school choice, teachers would—as other professionals do—have more flexibility to choose schools with the philosophy of education, schedules, students, and salary they desire.

THE FACTS

- ★ The first system of Texas public schools created by the 1876 Constitution was essentially a voucher system, allowing parents to redeem government dollars at municipal or private schools.
- ★ In existing voucher programs, African-American students reduced the achievement gap by one-third within just two years.
- ★ Students who use vouchers in private schools have higher academic achievement and a higher likelihood of high school graduation, college enrollment, and attaining a post-secondary degree—even after controlling for differences in race, ethnicity, and income.



- ★ Per-pupil operating costs of private schools participating in voucher programs were about half the cost of public schools, indicating that school choice could lower overall public education costs while getting better results.
- ★ Research demonstrates that Texas students attending charter schools perform better than if they had remained in traditional public schools.
- ★ Texas students attending traditional public schools facing charter competition generally demonstrate higher academic gains than do students in schools that do not compete with charters.
- ★ Sixty percent of Texas voters support a school choice program in which scholarships would be given by the state to pay for a child's education at any public, private, or parochial school, according to a 2003 Baseline & Associates Poll.
- ★ School choice is strongly supported by African-American and Hispanic voters.

RECOMMENDATIONS

- ★ Introduce publicly funded vouchers as a pilot program for under-performing schools and disabled students.
- ★ Inject competition into the public school system, beginning with public school or inter-district choice.
- ★ Establish student-centered funding and offer school choice as the new form of public education for all children.

RESOURCES

- *What You Should Know about Charter Schools in Texas* by Chris Patterson, Texas Public Policy Foundation (Sep. 2005) <http://www.texaspolicy.com/pdf/2005-09-29-charterschools-pb.pdf>.
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- *An Education Monopoly: The Calculable Cost to Texas* by Byron Schlomach, Texas Public Policy Foundation (Jan. 2005) <http://www.texaspolicy.com/pdf/2005-01-monopoly.pdf>.
- *Choice is the Best Choice for Texas Education* by Chris Patterson, Texas Public Policy Foundation (June 2004) <http://www.texaspolicy.com/pdf/2004-06-07-choice.pdf>.
- *A Summary of Results from School Choice Research* by Jay P. Greene, Ph.D., The Manhattan Institute for Policy Research (Jan. 2006) <http://www.texaspolicy.com/pdf/2006-01-pogreene-voucherresults.pdf>.

THE ISSUE

After decades of expensive reforms, including class size reductions and across-the-board teacher pay raises, Texas public school students are still at or below the national average in many areas of academic performance. Some explain below-average scores on national tests by pointing out that Texas has a different demographic makeup than other states. Others feel it is a disservice to hold certain student groups to lower expectations based on their ethnicity or economic situation.

One thing is certain: Texas high school dropout rates are alarmingly high, with some estimates approaching 40 percent. Even those students who do graduate from high school and attend college are ill-equipped when they get there, with approximately 50 percent of Texas college students requiring remedial classes. As a result, Texas industries are growing increasingly concerned about the supply of high school and college graduates, especially in mathematics and science.

A major factor in the quality of Texas public education is the state curriculum, or the Texas Essential Knowledge and Skills (TEKS). Unfortunately, an analysis by ACT found that the curriculum promotes mastering lower-level skills, and the Texas proficiency standards (as measured by the TAKS) consistently receive one of the lowest grades in the country. Replacing the TAKS with end-of-course exams at the secondary level could help improve the curriculum, increase post-secondary readiness, close the achievement gap, and provide greater data by which to measure student achievement and implement performance-based pay for teachers.

In the 2006 special session, House Bill 1 raised high school graduation requirements to include four years of each of the four core subjects: language arts, math, science, and social studies. This reform could make a great impact on college readiness, considering that curriculum is a better indicator of post-secondary success than socioeconomic status, standardized test scores, or high school GPA.

House Bill 1 made great strides towards holding low-performing schools accountable, but additional accountability is still needed for specific programs such as bilingual education and DAEPs.

THE FACTS

- ★ Nineteen of the 25 fastest-growing occupations in Texas require some post-secondary education, with half requiring at least a bachelor's degree.
- ★ Only one quarter of Texans aged 25 to 65 have a bachelor's degree or higher, while an almost equal number do not even have a high school diploma.
- ★ Twenty-five percent of Texas 8th graders exhibit proficiency on the math NAEP, and 23 percent in science—versus national averages of 36 percent and 42 percent, respectively.



- ★ Texas students scored 5th lowest in the nation on the math section of the SAT; over the past 10 years, the average SAT score in Texas has dropped one point, while the nation's average has increased by 18 points.
- ★ While 82 percent of Texas 4th graders exhibited proficiency on the math section of the TAKS in 2005, only 40 percent exhibited proficiency on the math NAEP.
- ★ A recent survey of its members by the Texas Federation of Teachers reported that 72 percent of respondents supported replacing the TAKS with end-of-course exams at the secondary level.
- ★ For a public school to be accredited, only 35 percent of students must pass the math TAKS, and only 25 percent must pass the science TAKS.
- ★ There is no evidence as to whether most DAEPs improve academic and behavioral outcomes of students.

RECOMMENDATIONS

- ★ Strengthen the state curriculum, aligning it with college readiness standards.
- ★ Couple or replace state assessments with a standardized, nationally norm-referenced test and/or end-of-course exams.
- ★ Establish high standards for graduation, post-secondary readiness, and closing the achievement gap as the basis for school accreditation.
- ★ Create meaningful state standards for specialized programs such as DAEPs and bilingual education.

RESOURCES

- *Texas, We Have a Problem: The Math/Science Education Deficit and the Need for High School Reform* by Jamie Story, Texas Public Policy Foundation (Mar. 2006) <http://www.texaspolicy.com/pdf/2006-03-PP-mathscience-js.pdf>.
- *Rhetoric Is Clouding the Facts: Legislature Must Be Cautious of Distortions* by Jamie Story, Texas Public Policy Foundation (Mar. 2006) <http://www.texaspolicy.com/pdf/2006-03-edspendingfacts-js.pdf>.
- *Accreditation of Texas Public Schools: Increasing the Value* by Chris Patterson, Texas Public Policy Foundation (Feb. 2006) <http://www.texaspolicy.com/pdf/2006-02-PP-accreditation-CP.pdf>.
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- *Testimony on Post-Secondary Readiness* by Chris Patterson, Texas Public Policy Foundation (May 2004) <http://www.texaspolicy.com/pdf/2004-05-10-testimony-patterson-pp.pdf>.
- *Texas Public Education Facts* by Chris Patterson, Texas Public Policy Foundation (Feb. 2006) <http://www.texaspolicy.com/pdf/2006-02-edfactsheet-cp.pdf>.

THE ISSUE

Research shows teacher quality is the most important in-school factor relating to student achievement, especially for low-performing students. It is vital, therefore, to place an emphasis on improving teacher quality.

At the same time, the teaching profession is attracting fewer high-ability individuals. Students with low standardized test scores enter teaching at higher rates than students with high scores. While there is no overall teacher shortage, Texas does face shortages in specific schools and subjects such as math, science, bilingual, and special education.

Why are high-ability individuals steering away from the teaching field? Limited pay and career opportunities are two commonly cited reasons. However, state and national surveys show that working conditions—including student discipline, administrative problems, and school district policies—are more important to teachers than pay. In a Public Agenda survey, a majority of teachers said they would choose schools with well-behaved students and supportive parents and administrators over schools that pay higher salaries.

While working conditions are important, pay is still a common concern of educators. Many educators tout an across-the-board pay raise as a means to increase teacher recruitment and retention. But, there is no evidence that across-the-board pay increases based on the current single-salary schedule reduce turnover or improve teacher quality, and in fact they serve to further cement the inequities in teacher quality and supply among districts. Despite its \$800 million price tag, the Legislature's recent \$2,000 across-the-board teacher pay raise will do little to address teacher quality or turnover.

Fortunately, lawmakers also created the largest teacher incentive pay system in the country, at an average of \$1,000 per Texas teacher. These funds will allow local districts to design specialized incentive programs in order to attract quality teachers where they're needed most, and to reward highly effective teachers.

Another concern is the existence of statutory job protections for teachers. It is time-consuming and expensive for districts to fire teachers who don't do their jobs. As a result, many ineffective teachers are merely transferred to other schools rather than being remediated or asked to leave the profession. Tenure laws in Texas must be reformed to enable principals to remove poor teachers from public schools.

THE FACTS

- ★ Texas teachers will be paid more than \$43,000 on average in 2006-07. They will rank about 24th in the U.S., before adjustment for cost of living.
- ★ According to the American Federation of Teachers, Texas average teacher salaries, adjusted for cost of living, ranked 16th among the 50 states in 2001-02.



- ★ The existing minimum salary schedule rewards seniority, not effectiveness. Studies show the two to be only mildly related, with seniority having no effect on teacher quality after the first few years.
- ★ Increasing teacher salaries across the board has no discernable effect on student performance in Texas public schools.
- ★ If the student-to-teacher ratio (currently 15:1) were increased to its 1969 level (24:1), the average Texas teacher could make \$70,000 per year with no increased spending.
- ★ Since 1995, if average teacher pay had increased at the same rate as per-student spending, Texas teachers would be making an average of \$48,000 per year.

RECOMMENDATIONS

- ★ Phase out the state minimum salary schedule to allow more freedom for differentiated pay.
- ★ Phase out laws and regulations limiting schools' ability to make employment decisions.
- ★ Implement any future teacher pay raises in the form of differentiated, rather than across-the-board pay.
- ★ Enact policy aimed at improving the school environment and teacher working conditions.
- ★ Develop the capabilities to assess "value-added" by individual teachers, for use in fair and effective performance pay programs.

RESOURCES

- *Better Salaries for Teachers in Texas Public Schools* by Chris Patterson and Jamie Story, Texas Public Policy Foundation (Nov. 2005) <http://www.texaspolicy.com/pdf/2005-11-teacher-pay-rr.pdf>.
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THE ISSUE

The question of who governs independent school districts is a complicated one. Many mandates are created at the state level by elected representatives, with other decisions left to local control. At the local level, authority is shared by the superintendent and board of trustees. Ultimately, however, school district officials must answer to local taxpayers.

The primary ability of local taxpayers to impact district policy is through school board and bond elections. Unfortunately, most school elections have historically been held on separate dates and/or at separate locations from general elections, leading to extremely low turnout numbers. House Bill 1 in the 2006 special session made some improvement in this area, requiring school elections to be held on the same dates and in the same locations as city elections. This is especially important now that rollback elections, as a result of HB1, are automatic at effective tax rate increases of four cents or higher. However, city elections are held separately from the general elections in November, when voter turnout is generally highest.

School board members serve as the elected representatives of local taxpayers. Unfortunately, the responsibilities of most board members are little more than hiring the superintendent, hearing appeals by terminated employees, and approving tax rates and bond issues.

School leadership—encompassing both principals and superintendents—is one of the most important factors in the academic and financial well-being of schools. Today's superintendents and principals shoulder politics, security, public relations, finances, personnel, and technology—essentially serving as CEOs and CFOs. Therefore, they should be recruited from among successful business executives, military officers, and non-profit managers—not just from existing teachers. Unfortunately, there is no alternative pathway to school leadership certification in Texas, regardless of an individual's proven experience and success. Current law requires prospective principals to serve for a minimum of two years in the classroom before becoming eligible for certification.

Another governance concern is the classroom authority of teachers. Working conditions are of utmost importance to teachers—even more important than salary in teacher polls—so attention must be paid to ensure teachers have adequate control over discipline and other classroom policies.

THE FACTS

- ★ Among registered voters in Texas, 57 percent voted in the November 2004 general elections; as a comparison, local election turnout percentages often dip into the single digits, with school elections typically even lower.
- ★ Voter turnout would be higher if school elections were held in November.
- ★ In 1983, *A Nation at Risk* identified educational leadership as both a leading cause of American educational malaise and a key to reform.



- ★ A recent survey of school superintendents found that fewer than 2 in 5 were satisfied with their principals' ability to make tough decisions, delegate responsibility, engage teachers in developing policies, or spend money efficiently.
- ★ State policies linking teacher salary to academic degree attainment have contributed to growth in the number of certified administrators, but only one-third of certified individuals are actively seeking administrative positions.

RECOMMENDATIONS

- ★ Require school elections to be held concurrently with November general elections.
- ★ Provide school boards more authority over organizational decisions.
- ★ Establish an alternative path to superintendent and principal certification.
- ★ Allow proven leadership credentials to take the place of the required two years of classroom teaching experience for prospective principals coming from outside of public education.
- ★ Give teachers expanded authority over classroom policies and discipline issues.

RESOURCES

- *Education Reforms of the Special Session: the Great, the Good, and the Not-So-Good* by Jamie Story, Texas Public Policy Foundation (May 2006) <http://www.texaspolicy.com/pdf/2006-05-PB-edreformspecial-js.pdf>.
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THE ISSUE

The notion of universal pre-K—publicly-funded preschool for all 4-year-olds—is gaining momentum throughout the country. Georgia implemented the first statewide universal pre-K program in 1993, and Oklahoma, New York, West Virginia, and Florida are in various stages of implementation. However, in June 2006, California voters handily defeated a proposition to fund universal public pre-K for all 4-year-olds. Clearly there is disagreement about the benefits of universal pre-K.

Advocates cite a variety of reasons for instituting universal pre-K. They claim positive returns on investment in pre-K due to decreased incarceration costs, reduced welfare dependence, and increased future wages for children who participate in pre-K. However, these conclusions are largely based on studies over the past several decades that focused on small groups of extremely disadvantaged children, and it is inappropriate to assume that these benefits apply to all children. Advocates also cite universal pre-K as a solution to our public education woes, because it will ensure that children are prepared for school upon kindergarten entry. Recent studies, however, show that any academic benefit from pre-K has “faded out” by the third grade.

On the other hand, there are several arguments against universal pre-K. One argument is economic: the vast majority of Texas 4-year-olds already participate in public or private preschool. Universal pre-K, then, would do little more than subsidize parents who already choose, and can afford, to send their children to private preschool. Not only would universal pre-K cause the cost of preschool to skyrocket, but it would likely force many private sector providers out of business.

Some studies even find negative effects on children who enroll in universal childcare. A study of Quebec’s universal preschool program suggested that children demonstrated increased anxiety, hyperactivity, and aggressive behavior in the years following introduction of the universal program. Researchers from UC Berkeley have found similar results.

In summary, universal pre-K is an expensive proposition with uncertain, even negative, results.

THE FACTS

- ★ In 1965, only 11 percent of 3 and 4-year-olds in the U.S. enrolled in school; that number rose to 55 percent by 2001.
- ★ In the 2003-04 school year, more than 160,000 Texas 4-year-olds enrolled in public pre-K, at a cost to taxpayers of \$488 million.
- ★ Forty-three percent of Texas 4-year-olds participate in state pre-K, 11 percent in Head Start, and approximately 35 percent in private preschool or childcare. This totals 94 percent of Texas 4-year-olds, although the actual percentage is likely lower due to overlap among programs.



- ★ The TEA estimates 75 percent of qualified children (economically disadvantaged, homeless, and/or LEP) are enrolled in public pre-K. The rest either choose not to participate, or live in the minority of school districts where pre-K is not offered.
- ★ Quebec started a universal pre-K program eight years ago. The program now costs \$1.7 billion each year—33 times the original projection—and has actually caused supply to decrease, crowding out many of the lowest-income students.
- ★ In the California universal pre-K plan, three-quarters of the funding would have gone to children who attended preschool without the initiative.
- ★ Two school districts in California hold the Ready to Start program, a five-week preschool program taking place in the summer before kindergarten. It costs \$350 per student (rather than \$8,000 for year-round preschool), and it's short-term success is similar to that found after one year of preschool.
- ★ Although U.S. students fall behind in later grades, our 4th graders routinely outscore their international peers—including those from Germany and France, which have higher preschool enrollment rates than the U.S.

RECOMMENDATIONS

- ★ Rather than implement universal pre-K, legislators should look at ways to ensure that all children who already qualify for state pre-K (economically disadvantaged, homeless, and/or limited English proficient) are able to access it.
- ★ Similar to K-12, pre-K should be held accountable for success. Effectiveness should be measured in terms of kindergarten readiness so that parents and taxpayers know their money is being spent effectively.

RESOURCES

- *The Early Bird Misses the Worm: Evidence on Early Childhood Education* by Jamie Story, Texas Public Policy Foundation (Jan. 2006) <http://www.texaspolicy.com/pdf/2006-01-ECE-JS.pdf>.
- *No Magic Bullet: Top Ten Myths About the Benefits of Government-Run Universal Preschool* by Lance T. Izumi and Xiaochin Claire Yan, Pacific Research Institute (May 2006) <http://www.pacificresearch.org/pub/sab/educat/2006/magic-bullet.html>.
- *Assessing Proposal for Preschool and Kindergarten: Essential Information for Parents, Taxpayers and Policymakers* by Darcy Olsen with Lisa Snell, Reason Foundation (May 2006) http://www.reason.org/ps344_universalpreschool.pdf.



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THE ISSUE

The Employees Retirement System of Texas (ERS) oversees the retirement and insurance benefits of state employees across Texas. ERS operates five retirement plans: state employees, elected officials, law enforcement, and two judicial plans, making up the 53rd largest pension fund in the United States in 2005. In addition to retirement benefits, ERS provided insurance benefits to 504,985 state employees, retirees and their dependents in Fiscal Year 2005. In total, ERS received a five and a half percent increase for the 2006-07 biennium over 2004-05 estimated expenditures.

The cost of providing health benefits to Texas' state employees has been climbing for years, increasing from about 5 to 9 percent a year from Plan Year 2004 to Plan Year 2007. In an effort to control mounting costs and combat a \$10 billion budget shortfall, the 78th Texas Legislature directed significant changes in employee health benefits, including added cost sharing and a 90-day waiting period for new hires. Yet the cost of health benefits for state employees continues to be the full obligation of the state; the state covers the entire cost of state employee's health benefits, and 50 percent of the cost for dependent premiums established by the ERS board.

While individual state employees have not realized any increase in the cost of their coverage, those who share in the cost of dependent coverage have seen their monthly cost rise every year. However, state employees have also experienced an increase of their benefits every year as well.

THE FACTS

- ★ In FY 2005, ERS provided insurance benefits to almost 505,000 state employees, retirees, and their dependents.
- ★ Texas pays the full cost of the premium for state employees and half the cost of the premium for an employee's dependents, a total appropriation of about \$2.1 billion for the 2006-07 biennium.
- ★ Texas state employees also have the option of participating in the TexFlex program, providing employees a Flexible Spending Account to make pre-tax savings deposits for out-of-pocket health and child care expenditures.
- ★ ERS reports that there were more than 32,000 TexFlex accounts in FY 2005 with a total contribution of \$53 million dollars, for a tax savings of approximately \$76.5 million.
- ★ Overall increases in the cost of health care, running roughly 12 percent, fueled an increase of almost \$200 million in appropriations for the state employees' group health insurance over the 2004-05 biennium.
- ★ In Plan Year 2004, the premium for employee-only benefits was approximately \$298/month, increasing to roughly \$361/month in Plan Year 2007—an increase of more than 20 percent.



- ★ The Federal Employee Health Benefits Plan began offering federal employees the option of a high deductible health plan (HDHP) coupled with a Health Savings Account (HSA) in January 2005; federal employees choosing the HDHP/HSA option had 14 different plans to choose from.
- ★ A survey of state health benefits in Fall 2005 found that state employees in Arkansas, Colorado, Florida, Georgia, Kansas, Mississippi, Oklahoma, South Carolina, and South Dakota all had an HDHP/HSA option, or would have the option in the next benefits year.
- ★ In some states, state employees who smoke pay a higher health insurance premium than their non-smoking co-workers; Georgia charges state employee smokers a surcharge of \$40/month.

RECOMMENDATIONS

- ★ Readjust cost sharing for state employees, requiring state employees to pay a portion of the monthly premium.
- ★ Offer state employees the option of a high deductible health plan and health savings account to control cost and allow employees to share in the premium savings.
- ★ State employees should have the choice of enrolling in a high deductible health plan with the minimum high deductible allowed under law (\$1,050 for an individual) and a plan with an even higher deductible, in order to give state employees the most choice.

RESOURCES

- *Health Savings Accounts: Affordable, Portable, and Accessible Health Insurance* by Mary Katherine Stout, Texas Public Policy Foundation (Mar. 2005) <http://www.texaspolicy.com/pdf/2005-03-pp-hsa.pdf>.
- *Survey of State Employee Benefits* by Mary Katherine Stout, Texas Public Policy Foundation (Aug. 2005) <http://www.texaspolicy.com/pdf/2006-08-PP-statebenefitsurvey-mks.pdf>.
- *HSAs for State Employees* by Mary Katherine Stout, Texas Public Policy Foundation (Sep. 2005) <http://www.texaspolicy.com/pdf/2006-09-PP-HSAsforstate-mks.pdf>.
- *Healthy Competition: What's Holding Back Health Care and How to Free It* by Michael Cannon and Michael Tanner, CATO Institute, 2005.
- *Health Savings Accounts: Answering the Critics, Parts I-III* by John Goodman and Devon Herrick, the National Center for Policy Analysis, Brief Analysis Nos. 544, 545, and 546 (Mar. 2006) <http://www.ncpa.org/pub/hea.html>.

THE ISSUE

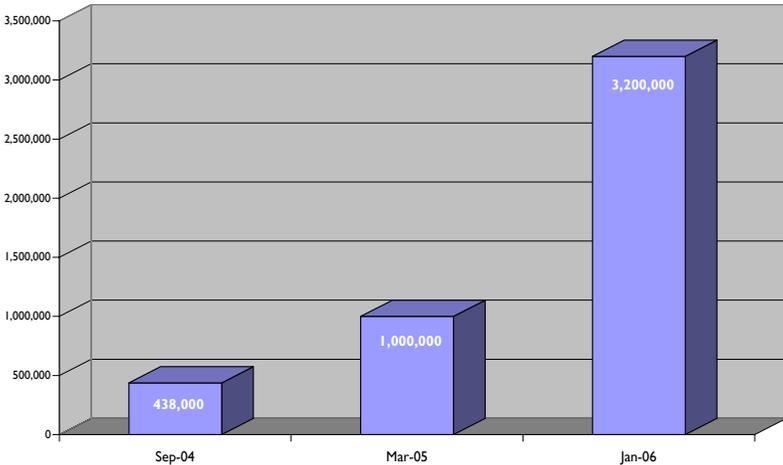
Consumer-driven health care has become a popular term with the creation and wide spread adoption of personal health accounts, such as Flexible Spending Accounts (FSAs), Health Reimbursement Arrangements (HRAs), and Health Savings Accounts (HSAs). However, as the popularity of these accounts has grown, so have issues that impact the ability of individuals to make decisions about their health care. Issues like price transparency and an emphasis on measuring quality have emerged as central issues in the health care debate, driven largely by the growth of these new methods of paying for health care services.

Health Savings Accounts

FSAs and HRAs preceded HSAs, which were created by Congress in 2003 and first became available on the market in 2004. Since that time the use of HSAs has grown rapidly around the country, offering greater patient control and more flexible features than even the other similar accounts offer.

HSAs refer to the savings account portion of the combination between a high deductible health plan (HDHP) and a savings account to pay for health care with pre-tax dollars. An HDHP requires participants to meet their deductible by paying medical bills out-of-pocket (presumably with funds in the HSA), rather than co-payments and co-insurance. By putting the individual's cost sharing obligation up front with a high deductible of at least \$1,050 in 2006 for an individual, premiums are often lower than traditional health insurance plans that feature high premiums and low or no deductibles or cost sharing.

Number of People with an HSA Qualified High Deductible Health Plan





In September 2004, 438,000 people had an HSA-qualified HDHP, rapidly increasing to more than 1 million by March 2005, and then tripling to almost 3.2 million people by January 2006. By February 2006, balances in the accounts nationwide reached almost \$1 billion. Recent studies show that roughly a third of the people purchasing an HSA-qualified HDHP in the individual market were previously uninsured, perhaps attracted by the low price and tax benefits.

HSA's are frequently criticized as being only for the healthy and wealthy, but much of the experience disputes this. Indeed, individuals with chronic conditions can benefit from the flexibility that an HSA provides, not to mention a fixed out-of-pocket expenditure and a family deductible, rather than a per person deductible found in other traditional health insurance plans. In addition, the opportunity to save for health care with pre-tax dollars is at least as appealing as the premium savings that an individual (or an employer) would realize from purchasing a high deductible plan, rather than a plan with low or no deductible and co-payments.

Critics also claim that individuals with an HSA will forego needed care in an effort to save money, which studies have shown to be true, but only in minor circumstances. In fact, it is more reasonable to expect an individual responsible for making choices about their health care would receive screenings or adhere to treatment regimens more closely if failure to do so results in higher costs.

Overall, HSA's provide individuals with greater control over both health care decisions and the way in which health care services are paid.

Price Transparency

When individuals are insulated from making health care decisions, they are not sensitive to the cost of their care; however, the new focus on consumer driven health care and the wide spread adoption of HSA's has fueled new interest in the cost of care. As evidence of this trend, a McKinsey & Company survey found that individuals with a consumer directed health plan were 50 percent more likely to ask about cost and 33 percent more likely to independently identify treatment alternatives.

Yet the price of health care services remains a mystery to many. A Harris Poll in July 2005 found that people were able to predict the price of a Honda Accord within \$300 of the actual cost, but missed the price of a four-day stay in the hospital by more than \$8,100. The question of price becomes a particularly important issue not only for those who must meet their deductible out-of-pocket, but even more important for uninsured individuals who are often charged several times more than what a provider would bill or expect to be paid from an insurer. The same Harris Poll found that 63 percent of adults didn't know the cost of their care until after they received the bill, a practice that has been commonplace in an area where consumers have little sensitivity to price.

Yet patients report that when they act like consumers with an interest in price, they can often negotiate lower rates. A Harris Poll in December 2005 found that 70 percent of adults reported that they were successful in negotiating a lower price with a hospital, 61 percent were successful in negotiating a lower price with a doctor, and 45 percent were successful negotiating a lower price with a health insurer.

Quality Care

One thing has become increasingly clear, patients are concerned about the quality of care that they receive in addition to the price of care. A Harris Poll in 2005 found that only 4 percent of adults ranked cost as the most important factor, while two-thirds of adults said quality was most important. Yet measuring quality becomes difficult, and even publications from the U.S. Agency for Health Quality and Research offer patients basic, common sense advice on how to get good quality care, typically in thorough consultation with their doctor. A Time magazine article from April 2006 found that when patients were in consultation with their doctors, the rate of surgery dropped by 23 percent and outcomes and satisfaction improved.

Interestingly, a recent New England Journal of Medicine article found that health insurance status is largely unrelated to the quality of care a patient receives, but notes that health insurance can help improve access to health care. In many cases, however, quality is measured in quantity of inputs such as access to beds and specialties, rather than the outcomes.

THE FACTS

- ★ In September 2004, 438,000 people had an HSA-qualified HDHP, more than doubling to more than 1 million in March 2005, and then tripling to almost 3.2 million people by January 2006.
- ★ By February 2006 combined account balances in HSAs reached \$1 billion.
- ★ Almost one third of the people enrolling in an HSA in the non-group market were previously uninsured.
- ★ Individuals with a consumer directed health plan were 50 percent more likely to ask about cost and 33 percent more likely to independently identify treatment alternatives.
- ★ Recent polls have found 63 percent of adults didn't know the cost of their care until after they received the bill.
- ★ Seventy percent of adults polled reported that they were successful in negotiating a lower price with a hospital, 61 percent were successful in negotiating a lower price with a doctor, and 45 percent were successful negotiating a lower price with a health insurer.



RECOMMENDATIONS

- ★ Offer state employees an option to enroll in an HSA/HDHP.
- ★ Make price and quality information readily available for Medicaid, allowing taxpayers and recipients to compare the prices the government pays for services.

RESOURCES

- *Consumer-Driven Price Transparency: Making Health Care Prices Transparent Through the Free Market* by Mary Katherine Stout, Texas Public Policy Foundation (June 2006) <http://www.texaspolicy.com/pdf/2006-06-PP-hctransparency-mks.pdf>.
- *HSA's for State Employees* by Mary Katherine Stout, Texas Public Policy Foundation (Aug./Sep. 2006) <http://www.texaspolicy.com/pdf/2006-09-PP-HSAsforstate-mks.pdf>.
- *Health Savings Accounts: Affordable, Portable, and Accessible Health Insurance* by Mary Katherine Stout, Texas Public Policy Foundation (Mar. 2005) <http://www.texaspolicy.com/pdf/2005-03-pp-hsa.pdf>.
- *Healthy Competition: What's Holding Back Health Care and How to Free It* by Michael Cannon and Michael Tanner, CATO Institute, 2005.
- *Health Savings Accounts: Answering the Critics, Parts I-III* by John Goodman and Devon Herrick, the National Center for Policy Analysis, Brief Analysis Nos. 544, 545, and 546 (Mar. 2006) <http://www.ncpa.org/pub/hea.html>.

THE ISSUE

The uninsured have proven to be a policy issue of particular concern to state and national policymakers, often leading to the creation and expansion of government programs and, more recently, a requirement that all residents of Massachusetts purchase health insurance. The uninsured present serious policy issues and strain on the health care system, as the cost of providing uncompensated care to the uninsured and questions about access and quality of care dominate the debate. However, there are serious questions about how well Texas, as well as the nation, has done in accurately estimating and identifying the uninsured.

How many uninsured people are there? The U.S. Census Bureau estimates the number of uninsured based on survey data that asks individuals about insurance coverage in the previous calendar year, which is thought to underreport insurance coverage as respondents' recollections might not be entirely accurate. In addition, Census numbers often undercount Medicaid and Medicare enrollment when compared to data from the Centers for Medicare and Medicaid Services. Both underreporting coverage and undercounting Medicaid enrollment likely impact the accuracy of the estimate. Statistics show that roughly a quarter of the Texas population is uninsured—the highest percentage of uninsured people in the nation.

Who are the uninsured? Most people think the uninsured are poor, not working, in poor health, and receiving poor care, but the data shows how much more complex this population really is. Studies show that as high as 82 percent of the nation's uninsured are in working families, many employed by small businesses who cannot afford to provide employee health benefits. Research has also shown that many of the uninsured are in middle to upper income families, and that the fastest growing portion of the uninsured are those in households making more than \$50,000. Accurately identifying the uninsured and their reasons for going without health coverage is essential. The statistics show that the uninsured are represented in all income groups and among the healthy and sick alike.

THE FACTS

- ★ Approximately one quarter of Texas' population is uninsured; out of the roughly 5.5 million uninsured, 1.3 million of those are children.
- ★ The percentage of uninsured Texans has remained largely unchanged over the past decade, despite tremendous growth in Medicaid and the creation of the Children's Health Insurance Program.
- ★ In Texas, the majority of the uninsured are male; 43 percent work full time and only 27 percent do not work at all; 28 percent have a household income of more than \$50,000; and 70 percent are above the federal poverty level.
- ★ Between 1995 and 2004, the National Center for Policy Analysis



reports that the number of uninsured people living in households making \$50,000-\$75,000 a year has increased by 57 percent, and by 153 percent in families making \$75,000 or more.

- ★ The National Center for Policy Analysis also reports that between 1995 and 2004, the number of low income families making less than \$25,000 who have health insurance coverage—often through Medicaid or CHIP—has actually increased by 19 percent.
- ★ One third of immigrants lack health insurance, which is two and a half times the rate of the native-born uninsured (legal and illegal).
- ★ Immigrants and their U.S. born children account for almost 75 percent of the increase in the uninsured population since 1989 (legal and illegal immigrants).
- ★ All of the states on the U.S./Mexico border exceed the national average in their percentage of the uninsured.
- ★ Roughly 70 percent of the uninsured in Texas were born in the U.S.
- ★ A report from the *New England Journal of Medicine* finds that “health insurance status was largely unrelated to the quality of care among those with at least minimal access to care. Although having health insurance increases the ease of access to the health care system, it is not sufficient to ensure appropriate use of services or content of care.”

RECOMMENDATIONS

- ★ Promote consumer-directed health care alternatives, such as health savings accounts that offer lower cost health insurance coverage to individuals.
- ★ Reduce the cost of basic insurance by eliminating state regulations that mandate benefits.
- ★ Reduce state regulations that prevent lower cost providers to deliver health care while ensuring the safety and quality of health care.
- ★ Resist recent policy efforts that require individuals to carry health insurance, focusing instead on efforts to make health insurance a more attractive product at better value.
- ★ Form a multi-state insurance coalition between Texas and neighboring or regional states, allowing Texans the option to purchase health insurance across state lines.

RESOURCES

- *Sorting the Facts About the Uninsured* by Mary Katherine Stout, Texas Public Policy Foundation (May 2006) <http://www.texaspolicy.com/pdf/2006-05-PB-uninsured-mks.pdf>.

THE ISSUE

When Medicaid was established by Congress in 1965 and in Texas in 1967, the program was originally focused on providing health care benefits to recipients of certain cash assistance programs. However, more than four decades of incremental policy expansion have resulted in the largest government health program—providing benefits to more people and at a higher cost than the Medicare program.

In Texas, Medicaid has become the significant budget driver in health and human services spending, as well as the budget in general. According to the Legislative Budget Board, projected spending on Article II (health and human services) grew by 10 percent, or roughly \$4.5 billion, between 2004-2005 and 2006-2007. Of that, appropriations for Medicaid constituted almost 76 percent of the growth in health and human services spending. Texas Medicaid did not exceed \$2 billion in annual expenditures until 1987—20 years after it was created—though it has since grown rapidly and will meet or exceed \$20 billion in annual expenditures when the 80th Legislature convenes in 2007.

Much of this growth is driven by caseload growth as a result of policy decisions in Washington and in Austin that have added expanded eligibility for the program. According to the Health and Human Services Commission, the Medicaid caseload grew by more than a million people between 1990 and 1995, and again added roughly a million people from 2000-2005. Children make up the majority of the caseload, with enrollment of non-disabled children growing 80 percent between 2000 and 2005 to just under 2 million, but the aged, blind, and disabled populations account for the majority of the spending. The LBB has reported that the aging population has been going up in real numbers, but going down as a percentage of the caseload, a trend they say will reverse in 2011 with the aging population.

THE FACTS

- ★ Medicaid is an entitlement program—Texas must provide medically necessary care to all eligible individuals who seek services.
- ★ Health and human services spending represents roughly 35 percent of the state budget, with Medicaid accounting for approximately three quarters of health and human services spending.
- ★ In Fiscal Year 2006, Texas Medicaid is projected to cost taxpayers more than \$20 billion in All Funds, including the Disproportionate Share Hospital funding.
- ★ Medicaid is jointly financed with federal and state tax revenues according to the Federal Medical Assistance Percentages (FMAP), which varies between states and usually changes from year to year; Texas pays roughly 40 percent of Medicaid costs and the federal government pays roughly 60 percent.



- ★ Health and human services agencies account for just more than 60 percent of all state federal funds, and federal Medicaid funding account for more than 80 percent of federal spending for Texas health and human services.
- ★ In FY 2007 it is estimated that the Texas Medicaid program will cover more than 3 million Texans and 2.2 million of those will be children.
- ★ In 2006 Medicaid cost every man, woman, and child in the state of Texas more than \$850.
- ★ Despite large increases in enrollment, the state's uninsured rate remains relatively unchanged.
- ★ Never in the history of the Texas Medicaid program has state spending (general revenue) on Medicaid declined from one year to the next; only in 1982 did total Medicaid spending decline from the previous year as the result of reductions at the federal level.

RECOMMENDATIONS

- ★ Seek a federal waiver similar to the approved Florida waiver using risk-adjusted premiums to bring increased competition in coverage and greater recipient control.
- ★ Pursue federal approval for Texas to serve as a pilot state for Health Opportunity Accounts authorized under the Deficit Reduction Act passed by Congress in 2006.
- ★ Continue to pursue the most cost effective care settings, offering recipients incentives to share in any resulting savings.
- ★ Strengthen cost sharing in the Medicaid program using a sliding scale that ties the out-of-pocket cost of medical care to the recipient's income, applying the highest level of cost sharing authorized by the Deficit Reduction Act passed by Congress in 2006 to the highest income Medicaid recipients.

RESOURCES

- *Medicaid: Yesterday, Today, and Tomorrow; A Short History of Medicaid Policy and Its Impact on Texas* by Mary Katherine Stout, Texas Public Policy Foundation (Mar. 2006) <http://www.texaspolicy.com/pdf/2006-03-RR-medicaid-mks.pdf>.
- *Ending the Forty Year Entitlement* by Mary Katherine Stout, Texas Public Policy Foundation (July 2005) http://www.texaspolicy.com/commentaries_single.php?report_id=888.
- *Medicaid's Unseen Costs* by Michael Cannon, The Cato Institute (Aug. 2005) http://www.texaspolicy.com/commentaries_single.php?report_id=888.
- *Reforming Florida's Medicaid Program with Consumer Choice and Competition* by Michael Bond, The James Madison Institute (Feb. 2005) <http://www.jamesmadison.org/pdf/materials/331.pdf>.

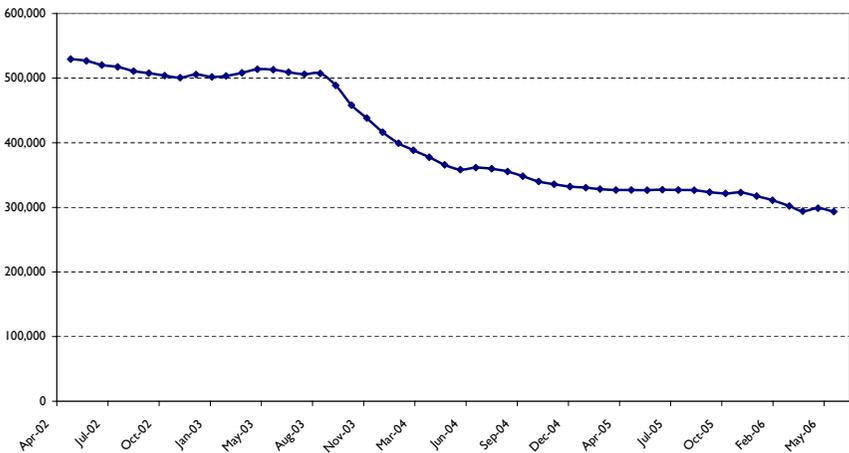
THE ISSUE

When Congress established the Children's Health Insurance Program (CHIP) in 1997, it did so in response to mounting pressure to address the number of uninsured children in the United States. Proponents of the plan argued that CHIP would deliver health insurance coverage to half of the nation's 10 million uninsured children by 2000. Through Federal Fiscal Year 2005, however, the CHIP program had never reached enrollment of even 4 million children at any given time.

The Texas Legislature established the CHIP program in 1999, though the new program did not begin to enroll children until June 2000. Texas' CHIP program is limited to children under age 18 in families whose incomes fall below 200 percent of the federal poverty level (FPL) and who are not eligible for Medicaid. Some states extend eligibility to children in families whose incomes meet or exceed 300 percent FPL, just as states may extend CHIP benefits to CHIP parents who meet income eligibility requirements.

From its implementation in June 2000 to its peak enrollment of 529,211 in May 2002, the CHIP caseload steadily increased; however, since its enrollment peak, the CHIP program has been in almost constant decline. These declines have been the result of a variety of factors, including a growing economy and policy changes made by the Texas Legislature in 2003 to shorten the eligibility period, tighten enrollment processes and better verify eligibility, and increase cost sharing. Though the Legislature also reduced the CHIP benefits package at the same time, those reductions were restored by the Legislature in 2005.

**Texas CHIP Enrollment by Month
May 2002-June 2006**





While the CHIP program is for all intents and purposes an expansion of the Medicaid program, it does have fundamental policy differences in comparison to the Medicaid program. There are two main differences:

- 1) CHIP, unlike Medicaid, is not an entitlement, and
- 2) Federal funds that are available to states through a matching arrangement are capped.

Importantly, since CHIP is not an entitlement, states have greater flexibility to design a benefits package and require recipients to share in the cost of care.

THE FACTS

- ★ CHIP is not an entitlement program—Texas can limit enrollment, require cost sharing among participants, and exercise flexibility in designing the benefits package.
- ★ CHIP serves children under age 18 who are ineligible for Medicaid and whose family makes less than 200 percent FPL.
- ★ In 2005, the Legislature approved expanding CHIP to include a new perinatal benefit to cover pregnant women up to 200 percent FPL; Medicaid currently covers pregnant women up to 185 percent FPL.
- ★ For the 2006–07 biennium, CHIP funding totaled \$1.4 billion, a 41 percent increase over CHIP's estimated/budgeted appropriation for 2004–05; state general revenue funds account for \$444.4 million of the CHIP total.
- ★ The CHIP caseload peaked in May 2002 shy of 530,000 children enrolled, followed by almost constant decline; in the 47 months following the peak, the caseload declined each month in all but eight months.
- ★ Health and human services agencies account for just more than 60 percent of all of the state's federal funds, and federal Medicaid funding account for more than 80 percent of federal spending for Texas health and human services.
- ★ Although CHIP is said to be budget certain, it has required supplemental appropriations to prevent budget shortfalls.
- ★ Reforms passed during 2003 and implemented since allow the state to direct care to those who are truly eligible, and to limit fraud and abuse.
- ★ In almost every month since the program began in June 2000, the most common reason for disenrollment was the family's failure to renew, followed by a determination that the family was no longer eligible for benefits.
- ★ Despite the creation of the CHIP program and coverage of more than 2.2 million children between Medicaid and CHIP, the state's uninsured rate remains relatively unchanged.

RECOMMENDATIONS

- ★ Maintain identical periods of continuous eligibility in Medicaid and CHIP of no more than six months.
- ★ Maintain reforms passed and implemented since 2003 such as the 90-day waiting period for benefits, the assets test, and income and asset verification.
- ★ CHIP benefits should be no more generous than state employee benefits; additional benefits, such as dental and vision services, should come at the family's option with separate cost sharing.
- ★ Texas should reevaluate the CHIP immigrant program, which is funded only from general revenue and cannot be matched with federal funds.

RESOURCES

- *The Children's Health Insurance Program in Texas* by Mary Katherine Stout, Texas Public Policy Foundation (Apr. 2006) <http://www.texaspolicy.com/pdf/2006-04-RR-CHIP-mks.pdf>.
- *CHIPs Down When Times Are Good* by Mary Katherine Stout, Texas Public Policy Foundation (Apr. 2006) http://www.texaspolicy.com/commentaries_single.php?report_id=1085.



Legislators' Guide to the Issues

WELFARE REFORM 58

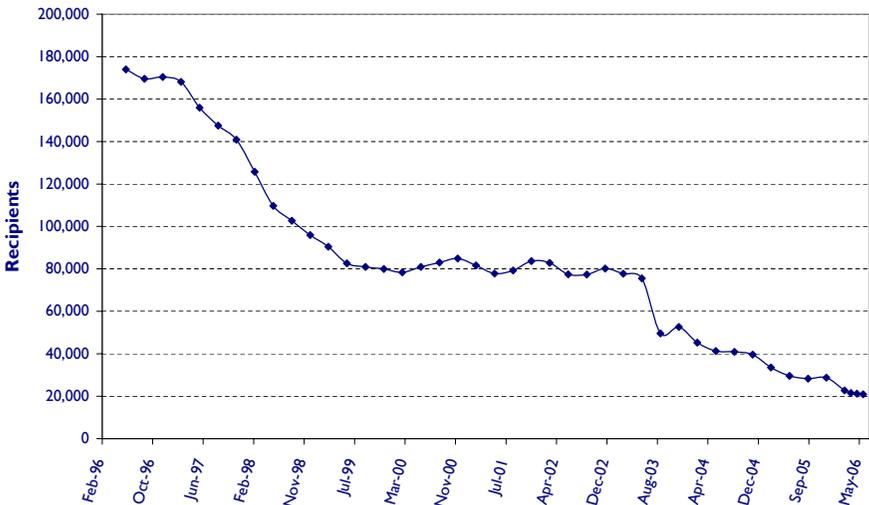
THE ISSUE

In 1996, the United States Congress passed sweeping legislation to reform the nation's welfare system through the Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA). PRWORA ended welfare as an entitlement, instead creating a system of reciprocal obligation, requiring welfare recipients to be engaged in work activities, and time-limiting the receipt of benefits. In addition, welfare reform changed the name of the welfare program from Aid to Families with Dependent Children to Temporary Assistance for Needy Families (TANF), and funded TANF through a federal block grant to the states.

Texas has been a leader in welfare reform, passing its own version in 1995 and receiving a waiver to grandfather the state's system until 2002 when the state was forced to fully comply with PRWORA. In addition, the 78th Legislature continued the work of welfare reform, establishing stricter sanctions for non-compliance with work requirements and the state's Personal Responsibility Agreement. The full-family sanction terminates the entire family's TANF grant and is not restored until the adult recipient becomes compliant. Similarly, the state terminates the Medicaid benefit for TANF adults who do not comply with work requirements.

The results of the stricter sanctions have been dramatic. The percentage of adults under sanction every month has dropped dramatically, while the percentage of adults participating in work activities has climbed. The stronger sanctions have created an incentive for more responsible behavior, driving greater compliance with work requirements to ensure clients earn the full benefit for their family.

Adult TANF Recipients By Selected Months





As a result of welfare reform and the emphasis on work, Texas has been a leader among the states for moving people off of welfare and into the workplace. A July 2006 USA Today article shows the number of families receiving welfare in Texas declined by 68 percent between August 1996 and December 2005.

Through the Deficit Reduction Act of 2005 (DRA), Congress has continued to drive welfare reform further, tightening definitions of work activities and recalibrating the way states demonstrate their success in reducing their welfare caseload. States are required to have 50 percent of all TANF families participating in work activities, and 90 percent of two-parent families participating in work activities. However, in the past, states have received credit for reducing their caseload since 1995 which lowers the work participation percentage states must meet. The DRA will change the benchmark year for giving states credit for reducing their caseload from 1995 to 2005, thereby forcing states to more closely meet the 50 percent and 90 percent participation rates for all families and two-parent families, respectively.

To meet the participation rates under the recalibrated system, Texas will need to engage more TANF recipients in work activities. However, due to exemptions in state law and in Health and Human Services Commission (HHSC) rules, Texas may have difficulty engaging enough people in work activities to meet the participation rate, particularly for two-parent families. Failure to meet the work participation rate will result in a loss of part of the state's TANF block grant.

THE FACTS

- ★ The Personal Responsibility and Work Opportunity Reconciliation Act passed by Congress in 1996, fundamentally changed welfare across the country.
- ★ Texas has been a leader in welfare reform, receiving almost \$80 million in high performance bonuses from the U.S. Department of Health and Human Services through December 2005.
- ★ Between August 1996 and December 2005, Texas reduced the number of families on welfare by 68 percent.
- ★ Stricter state sanctions established by the 78th Legislature have improved compliance.
- ★ The number of individuals sanctioned for non-cooperation with work requirements declined by 92 percent from August 2003-April 2006.
- ★ The number of families sanctioned for non-cooperation with the state's Personal Responsibility Agreement dropped by 84 percent between September 2003 and June 2004.

- ★ The number of adults participating in work activities climbed 55 percent from State Fiscal Year 2003 to April 2006.
- ★ TANF recipients are exempt from work requirements under state law if they are the caretaker for an ill or disabled child, or a single parent/caretaker with a child under age one (applies only to the first child).
- ★ TANF recipients are exempt from work under HHSC rules if they are age 18 or younger, an adult unable to work due to a mental or physical disability lasting for more than 180 days, age 60 or older, an adult caring for a disabled adult, a pregnant woman not able to work, or a single grandparent age 50 or older and caring for a child under age three.

RECOMMENDATIONS

- ★ Maintain the full-family sanction for non-compliance with work requirements and the Personal Responsibility Agreement.
- ★ Maintain the adult Medicaid sanction for non-compliance with work requirements.
- ★ Review exemptions in state law and in agency rule that exempt TANF clients from work, though their benefits remain time-limited.
- ★ Remove exemptions that impede the state's ability to engage recipients in work and prepare them for self sufficiency.

RESOURCES

- *Continuing Welfare Reform in Texas* by Mary Katherine Stout, Texas Public Policy Foundation (July 2006) <http://texaspolicy.com/pdf/2006-07-PP-welfare-reform-mks.pdf>.
- "How welfare reform changed America" *USA Today* (18 July 2006) 1A.
- *The Impact of Welfare Reform*, testimony of Robert Rector to the Committee on Ways and Means, United States House of Representatives, The Heritage Foundation (19 July 2006) <http://www.heritage.org/Research/Welfare/tst071906a.cfm>.



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TORT REFORM 62

THE ISSUE

Since 1995, Texans have embarked on an unprecedented effort to restore justice to its rightful place in Texas courtrooms. The civil justice reforms of the last 11 years are too numerous to fully catalog, but a short listing would include reforms in areas such as: venue shopping; product liability; punitive and non-economic damages; frivolous lawsuits; class action lawsuits; medical liability; and asbestos and silica litigation.

While Texans have clearly benefited from past tort reforms, more work remains to be done in completing the overhaul of the Texas civil justice system.

For instance, Texas became infamous in the late 1980s for its hospitality of lawsuits filed on behalf of residents of other states. Tort reformers worked for years to bring this abuse of the system to an end. However, their success did not mean the end to lawsuit abuse in Texas—it merely caused the plaintiff's bar to put its resources into more profitable areas.

One of the new profit centers that sprung up in Texas was asbestos and silica litigation. Texas became a favorite venue for plaintiffs in asbestos cases. Three counties, Harris, Galveston and Jefferson, led all other jurisdictions for new filings for much of the 1990s. While other states such as Mississippi and New York vied for second and third, Texas led the nation in asbestos filings for over a decade.

An even more recent example of entrepreneurial trial lawyers is the current wave of Vioxx lawsuits. In the first Vioxx lawsuit to go to trial in the country, last August an Angleton jury awarded by more than \$253 million in damages against the maker of Vioxx. The actual economic damages in the case totaled only \$400,000. Noneconomic damages, however, were \$24 million, including \$22 million for mental anguish and loss of companionship. Punitive damages were \$229 million.

Texas clearly needs to continue working on tort reforms in order to counter the ongoing efforts of entrepreneurial trial lawyers to mine profits from the tort system.

THE FACTS

- ★ A recent study by the Pacific Research Institute ranked Texas as having the best tort reform system among the 50 states.
- ★ The American Medical Association dropped Texas from its list of states that are in a medical liability crisis.
- ★ Five of the largest malpractice insurers in the Texas market have instituted rate cuts that will save doctors (and their patients) about \$50 million.
- ★ Every liability insurance provider in Texas except one had lowered premiums by 2005.



- ★ Doctors recanted more than 4,000 of 10,000 silicosis diagnoses when questioned under oath in the Corpus Christi courtroom of Judge Janis Jack. One West Virginia radiologist testified he didn't interview, conduct physical exams on or check the work records of 2,700 of the claimants in the silica cases.
- ★ Despite its successes, Texas still has an image problem; a 2005 study of 1,400 practicing corporate attorneys ranked Texas' tort system 44th in the nation.

RECOMMENDATIONS

- ★ Improve jury selection by reducing the 10 peremptory challenges and the scope of questioning currently available to attorneys in jury selection.
- ★ Improve expert testimony by encouraging judges to use independent professionals to help them determine whether expert testimony should be admitted in court, and require that doctors who testify as expert witnesses be understood to be practicing medicine, which would give the Texas Medical Board the authority to discipline those who fraudulently testify.
- ★ Place caps on noneconomic damages by extending the current noneconomic damage caps in Texas to actions other than medical liability.
- ★ Split punitive damage awards by adopting punitive damages sharing, which directs a percentage of the damages to the state—much like a civil penalty in a regulatory enforcement case.

RESOURCES

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Legislators' Guide to the Issues

EMINENT DOMAIN 66

THE ISSUE

When the U.S. Supreme Court announced its decision last year allowing the City of New London, Connecticut to take Susette Kelo's house for an office park and an upscale residential development, the public—unlike five of the Court's justices—correctly recognized the decision as a frontal assault on private property rights. As a result, Texans and all Americans have virtually no protections against eminent domain abuse based on the U.S. Constitution. Any protections will now have to come from state governments.

State legislatures around the country responded to this situation and began looking for ways to rectify the problem. To their credit, Texas lawmakers were among the first to take action, passing SB 7 in the 2nd Called Special Session. But even they recognized their work as a stopgap measure to improve the situation until a more permanent solution could be found.

However, many local governments are taking advantage of the current freedom to take property and do not want to add any more property rights protections to Texas law. For instance, the Texas Municipal League put out the statement, "The Kelo decision is good for Texas cities. . . . It simply confirms what cities have known all along: under the Fifth Amendment to the U.S. Constitution, economic development can be as much a 'public use' as a road, bridge, or water tower."

While *Kelo* is only the latest advance in the evolutionary erosion of property rights, it represents a significant change from prior law. The public reaction to *Kelo* spurred the Texas Legislature's initial efforts to address this problem in SB 7. But the Legislature still has much to do to rein in the many local governments that are content to exercise their new freedom to take the property of their citizens.

THE FACTS

- ★ Even before *Kelo*, Texas courts had allowed a steady erosion of the protections against eminent domain abuse, adopting a rather liberal view as to what is or is not a "public use" and allowing the taking of a property in a blighted area constituted a public use, even if the property itself was not blighted.
- ★ The *Kelo* decision represents a real erosion of property rights in Texas because prior to *Kelo*, property owners could look to the U.S. Constitution for protections that Texas courts had eliminated from the Texas Constitution. They can no longer do so.
- ★ The restoration of these rights cannot be guaranteed to last unless they are put into the Texas Constitution.



RECOMMENDATIONS

- ★ Allow all determinations of public use and public necessity by condemners to be freely reviewable by the courts.
- ★ Require governments/entities to use the property only for the stated purpose for which it was condemned. If the property is not used for its original purpose in a timely manner, it should be offered back to the original owner at the original price paid.
- ★ Prohibit eminent domain from being used to acquire any property that will be subsequently transferred to a private party, unless the property in question is itself blighted, and the property owner receives market-based compensation, i.e., compensation based on the new use of the property.
- ★ Define public use: "Public use means that the state or a political subdivision of the state must own, or the citizens of the state as a whole must have the legal right to use, any taken, damaged or destroyed property, and does not mean public purpose or benefit."
- ★ Consider replacing the term "economic development" with "commercial purposes" and revisiting the need for all of the exemptions in the current law.

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THE ISSUE

The maze of telecommunications taxes is as hard on consumers' pocket-books as it is difficult for them to understand. Texans pay an average of 25.29 percent in state and local telecom transaction taxes—third highest in the nation. This includes state and local sales taxes, municipal franchise fees, and charges for the Texas Universal Service and Texas Telecommunications Infrastructure funds.

The average Texas local telecom tax rate is 11.32 percent and the average state tax rate is 13.97 percent. Adding federal taxes to the mix means that the average Texan's total telecom tax bill is just under 30 percent, almost one third of the cost of telecommunications services. In comparison, the general transaction (or sales) tax rate in Texas is 8.25 percent.

These average tax rates are representative of the tax burden on traditional local phone service. Cellular service in Texas is taxed less because it is not subject to the municipal franchise fee. Cable service has an average rate in Texas of about 14 percent, though cable companies offering traditional phone service generally face a similar level of taxes and fees on that service as phone companies do. Satellite service faces an even lower burden, having to pay only state and local sales taxes.

The Legislature needs to address both the high overall telecom tax burden and the disparate tax treatment of the different technologies. The Foundation has identified over \$382 million of telecommunications tax cuts that could be implemented by the 80th Texas Legislature, to address both of these issues.

THE FACTS

- ★ The Telecommunications Infrastructure Fund (TIF) fee is a gross receipts tax intended to fund the installation of communications infrastructure at public institutions. With that goal achieved, the fee was scheduled to expire. However, the Texas Legislature extended it through 2011 at a cost of about \$200 million per year.
- ★ The Universal Service Fund (USF) is funded by a charge on the monthly phone bill equal to about 5.65 percent of local and intrastate phone service, costing consumers over \$500 million a year. While the Fund helped promote the transition to a market-based system, today the fund is often more a hindrance than a help in fostering competition, essentially subsidizing some consumers and businesses at the expense of others.
- ★ Municipal franchise fees have become divorced from paying for the cost of managing the right-of-way, and turned into just another revenue source for cities.



- ★ The sales tax levied on telecommunications services function as taxes on a tax, since they are levied on several other telecom taxes, including the Federal USF charge, the Texas USF charge, the TIF fee, the Utility Gross Receipts Assessment, and Municipal Franchise Fees. This tax on a tax costs Texas consumers over \$90 million a year.

RECOMMENDATIONS

- ★ Eliminate the tax on a tax aspect of the state and local sales taxes. Taxpayer Savings: \$90 million per year.
- ★ Eliminate the Telecommunications Infrastructure Fund (TIF) fee. Taxpayer Savings: \$200 million per year.
- ★ Universal Service. Bring rates for all basic residential phone service to parity with urban rates and provide for a corresponding reduction in Universal Service charges. Taxpayer Savings: \$90 million per year.
- ★ Municipal Franchise Fees. Restructure these fees to reflect the marginal costs of placing facilities in the right-of-way. Taxpayer Savings: Unknown.
- ★ Private Network Service. Eliminate mandated provision of Private Network Service. Taxpayer Savings: \$2 million per year.

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THE ISSUE

Telephone subsidies are a way of life in Texas. However, their usefulness is rapidly drawing to an end. Subsidies have been used to help the state achieve its policy goal of providing universal, low cost telephone service for citizens across the state, particularly in rural Texas.

Under the previous heavily regulated telephone system, subsidies could be used to transfer wealth without major economic distortions. However, now that the transition of the telecommunications market to a competitive marketplace is well under way, they are often more a hindrance than a help in fostering competition. The two largest subsidies in place today are the Texas Universal Service Fund and intrastate long distance access rates.

Texas established the Universal Service Fund in 1987 to pay for a number of programs intended to enable all state residents to obtain basic telephone service at low prices. The vast majority of the funding is for subsidies in high-cost/rural areas, but it also subsidizes Lifeline and Linkup service for low-income customers and low-cost Internet access for certain state agencies and institutions of higher education (Private Network Service).

Up until 2006, the average intrastate access rate in Texas, which is set by the Legislature, was approximately 6 cents per minute, compared to about 1 cent per minute for interstate access. This began to change this year, as some companies—most notably AT&T—started reducing their access rates on July 1 under the provisions of SB 5, passed by the Texas Legislature in 2005.

THE FACTS

- ★ Because of subsidies, we estimate that only 281,000 out of 5.5 million residential lines we examined are priced at rates that cover their long-run incremental costs.
- ★ Charges for basic phone service run from \$13.82 per month in rural areas to \$16.72 in urban areas, but long-run incremental costs for service range from \$11.84 per month in urban areas to more than \$250 per month in rural areas.
- ★ Texas USF payments for FY 2004 were estimated to be \$586 million.
- ★ Almost 90 percent of the USF payments currently go toward high-cost and small rural carriers—not to low-income households that might not be able to afford phone service.
- ★ USF assessments on long-distance and wireless service reduces consumer and producer welfare in Texas by about \$166 to \$173 million annually.



- ★ Though intrastate access charges are not a traditional tax, this regulated charge functions as a hidden tax on consumers of intrastate long distance. If this charge were deregulated, intrastate long distance rates would surely decrease.
- ★ While information is not available for the entire state, large incumbent carriers' (AT&T, Verizon, Central, and United) revenue from intrastate long-distance access charges might exceed the cost of providing the service by \$172 million.

RECOMMENDATIONS

- ★ Bring rates for all basic residential phone service to parity with urban rates and provide for a corresponding reduction in Universal Service charges. This would reduce USF assessments on local phone bills by \$90 million per year.
- ★ Eliminate mandated provision of Private Network Service, at a savings to consumers of \$2 million per year.
- ★ Provide more careful targeting of USF programs to those who truly need them.
- ★ Firm timelines should be put in place to remove the relics of monopoly regulation—such as price caps and floors—from the current system. As companies are given more pricing flexibility, both USF assessments and intrastate access rates can be reduced at the same time.

RESOURCES

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THE ISSUE

Municipal franchise fees are levied on telecommunications services by cities for the use of the public right of way (ROW). These fees, which average from 4 to 6 percent of a typical telephone, cable, or video bill, make up a significant portion of the high telecommunication taxes levied on Texans.

There are three different forms of telecommunications franchise fees: 1) franchise or licensing fees for telephone service, 2) cable franchise fees, and 3) the new statewide video franchise fee created by SB 7 in 2005.

Though courts (and local governments) have said that franchise fees are “essentially a form of rent: the price paid to rent use of public right of ways,” it is wrong to think of them in this way. Governments are not private landlords seeking to extract maximum profits from private property, but guardians of the public interest in public lands. As such, they should not seek to extract maximum rents from the public for the use of the ROW, but instead should facilitate orderly public access to the ROW by imposing access prices equal to marginal costs. Rates higher than this disrupt the most efficient use of the ROW by imposing monopoly pricing on consumers via franchise fees that reduce the quality and availability of services to the public.

THE FACTS

- ★ Franchise fees have become divorced from paying for the cost of managing the right of way and have instead become just another revenue source for cities.
- ★ In 2005, 182 certified telecommunications providers paid approximately \$222 million in telephone franchise fees to 1,128 cities.
- ★ Telecom franchise fees for Houston, Dallas and Austin are about \$50 million, \$20 million and \$15 million, respectively.
- ★ Local governments, which have many other sources of revenue, have sufficient “budget bandwidth” to accommodate reduced franchise fees.
- ★ State and local governments are scrambling to maintain franchise fee revenues they feel are being threatened by new technologies. Services like satellite video and VoIP are threatening revenues, because in many cases they do not have to pay franchise fees.
- ★ Franchise fees do not include payments or costs incurred to relocate, remove or alter facilities in the right of way. One provider estimated that over the last year it spent an additional \$20 to \$25 million to relocate its facilities for road straitening and widening projects.



RECOMMENDATIONS

- ★ Franchise fees should be priced not to extract maximum rents from the public for the use of the ROW, but instead to facilitate orderly public access to the ROW by imposing charges equal to the marginal cost of providing access.
- ★ Franchise fees should be based on the physical occupation of the public right of way and the associated costs, not on the provision of individual services.
- ★ To assist in the transition to facilities-based franchise fees, new, emerging technologies, such as VoIP, should be exempt from franchise fees.
- ★ Incumbent providers are currently required to maintain their existing municipal franchise agreements until they expire. They should be allowed to opt out of them in order to utilize the new statewide video franchise.

RESOURCES

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THE ISSUE

For most of the last century, cheap and universally available local residential phone service was the primary telecommunications goal of policymakers across the country. The resulting regulatory regime kept competition at bay in order to maintain an elaborate web of subsidies that supported artificially low local service prices.

In the 1970s, when it became clear to everyone that consumers were demanding services that the regulated system couldn't deliver, the country began to move into the new era of telecommunications deregulation.

Texas has recently been one step ahead of the rest of the country, passing major telecom reform legislation in both 1995 and 2005. Thanks to the most recent legislation—Senate Bill 5—local telephone service for more than 15 million Texans was significantly deregulated as of January 1, 2006. This was a major step forward in reducing costs and bringing new technologies and services to millions of Texans.

But there is still room for improvement. Even though more than 15 million Texans live in areas where telephone service has been significantly deregulated, only three incumbent phone companies serve those people and there are still price controls in effect in those areas. For instance, companies cannot raise rates for basic service in deregulated markets until September 1, 2007. In addition, companies must apply rates evenly across a deregulated market, consistent with pricing flexibility that was available on August 31, 2005. Companies are also subject to price floors for all services set at the service's long run incremental cost. Finally, they are also subject to applicable PUC rules relating to discriminatory and predatory pricing under Chapter 60 of the Public Utilities Code.

The vast majority of phone companies continue to operate in regulated markets serving over 7 million Texans located mostly in rural Texas. In these areas, companies are subject to price caps, price floors and/or tariffs.

THE FACTS

- ★ Competition ALWAYS brings consumers the best products at the best prices. The history of telecommunications deregulation proves this time and again.
- ★ When the telecommunications equipment market was deregulated in the 1970s, the prices for phone handsets, key telephones, and private branch exchanges declined at a real rate of between six and seven percent per year between 1972 and 1987.
- ★ From 1984 to 1995, when there were just two cellular providers per market, inflation adjusted rates fell by an average of only 3 to 4 percent annually. However, in 1993, the government allowed up to six competitors in each market, resulting in declines in wireless rates averaging 17 percent annually from 1995 to 1999. A cellular phone call which



averaged 50 cents per minute in 1984 has declined to 8 cents per minute today.

- ★ Upon deregulation, interstate long distance rates fell 68 percent from 1984 to 2003, while intrastate rates fell 56 percent. The slower decline of intrastate rates is due largely to state regulators who have kept intrastate access charges artificially high in order to maintain subsidies of local phone rates.
- ★ The dual system in Texas of deregulated urban markets and regulated rural markets could create a “digital divide” between urban and rural customers.
- ★ The urban/rural digital divide could have a significant impact on taxpayers as it builds political pressure to increase, rather than decrease, telecommunications subsidies through the Texas Universal Service Fund.

RECOMMENDATIONS

- ★ The relics of monopoly regulation—such as price caps and floors—should be removed from the current system. Texas telecommunications policy should reflect the ongoing vibrant competition in many markets by immediately removing all price controls in deregulated markets to provide a positive incentive for companies to choose deregulation.
- ★ Firm timelines should be set for the deregulation of the currently regulated suburban and rural telecommunications markets. It is clear that technology brings real competition in telecommunications to every part of the state. A phased-in approach to deregulation in mid- and small-sized markets would encourage competition by ensuring that market participants (current and potential) understand that competition is inevitable.
- ★ Pricing flexibility that comes with deregulation should be paired with reductions in subsidies.

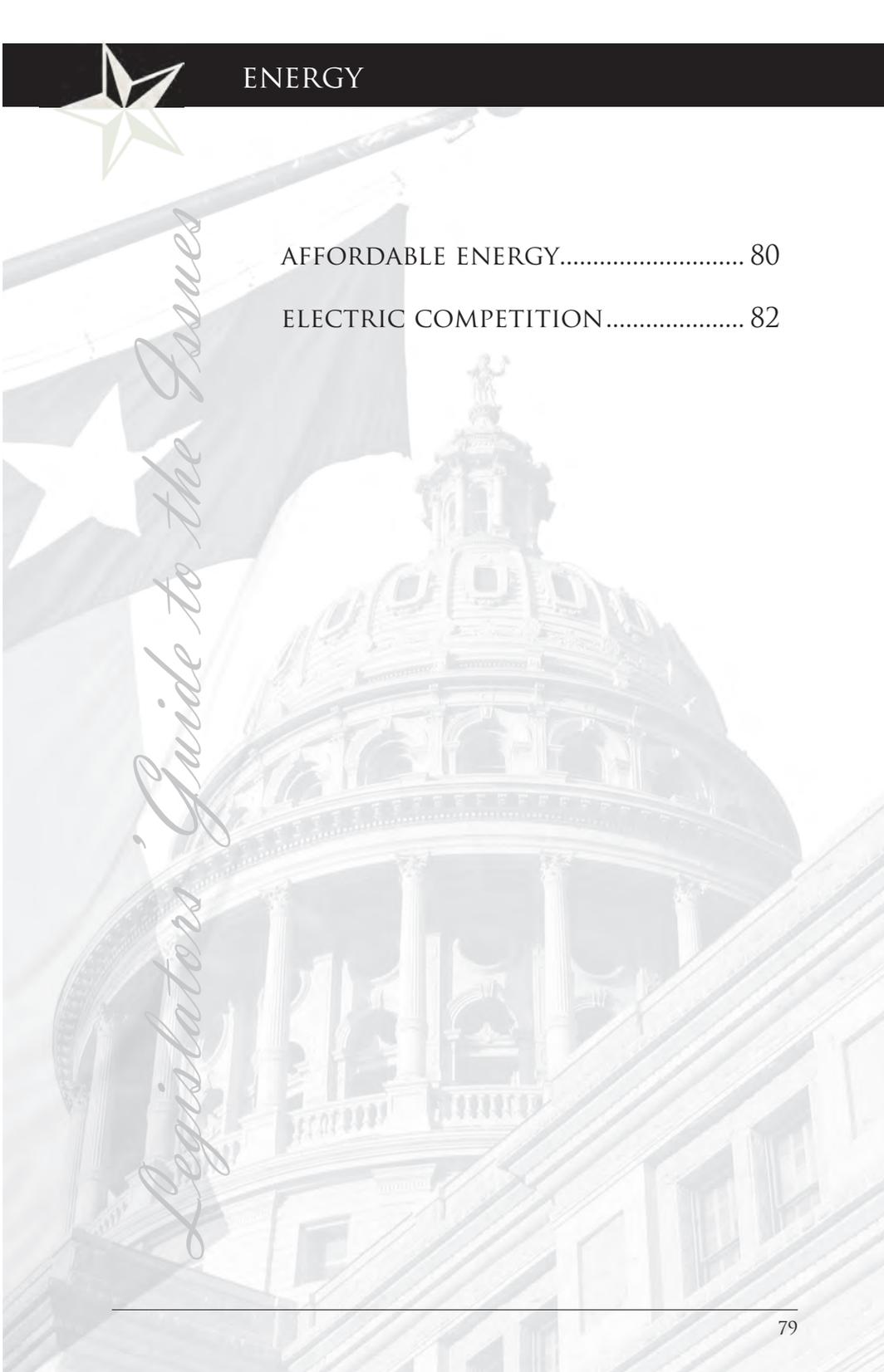
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Legislators' Guide to the Issues

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THE ISSUE

As gasoline prices continue to drift back to \$3 a gallon and Texas electricity prices move in tandem with natural gas prices, how to achieve affordable energy is a highly debated topic. Proposed and enacted solutions run from higher taxes to subsidies to mandated production from renewable sources such as wind, ethanol and biomass. However, these all miss the mark. A long-term solution for securing affordable, reliable energy supplies must rely on a proper understanding of our current situation and market-based innovations.

First, energy prices are not as bad as they are made out to be. Even at \$3 a gallon, the price of gasoline and oil does not surpass historical highs, and American gasoline prices are still well below those found in most of Europe. A recent report by the Texas Public Utility Commission found that increases in electricity prices have been lessened by the deregulation of the market. So while energy prices are high, Texans are in relatively good shape compared to many others.

Second, it must be understood that the energy problems we face today are largely the product of government regulations and interference in the market place. For instance, Texas' heavy reliance on high-priced natural gas to produce electricity came about because environmental laws made it expensive and difficult to build coal and nuclear plants. Similarly, the high price of oil and natural gas can be linked to regulations such as the limitation on exploration and production of domestic reserves of oil and gas, and the mandated use of ethanol for creating boutique gasoline blends for use during summer.

Additionally, efforts to promote energy diversity by mandating electric generation with renewable energy facilities only add to already high energy costs. The 3,000 megawatt increase in the renewable energy portfolio in SB 20, which passed in the 79th Texas Legislature, 1st Called Special Session, will cost Texas utility customers as much as \$536 million annually when fully implemented. That is the equivalent of \$31 per year for the typical consumer.

Finally, the Texas General Land Office reported that for fiscal year 2005, oil and gas revenues for the Permanent School Fund totaled over \$345 million, up from \$269 million in 2004. In the first four months of fiscal year 2006, approximately \$142 million was cleared, up from \$98 million for the same period in 2005. Oil and gas revenues have helped educate Texas schoolchildren, pave our roads, and provide for public safety.

THE FACTS

- ★ The price of oil peaked in late 1979 or early 1980 at around \$90 per barrel in 2005 dollars. This is compared to a price of \$71.58 per barrel of American light crude in May 2006 for July delivery. Oil is still cheaper today than it was 25 years ago.



- ★ In 1918, the price of a gallon of gasoline was about \$3.20 in 2005 dollars. After trending downward for about 50 years, the price spiked again in 1981 at just under \$3.00. The price of gasoline has only reached that level recently because of Hurricane Katrina and new regulations in last year's energy bill.
- ★ The total state and federal subsidies to businesses producing renewable energy could be as high as \$826 million per year when fully implemented.
- ★ The cost of building the transmission capacity needed to support wind energy production is estimated to be \$2.2 billion.

RECOMMENDATIONS

- ★ Maintain the path toward full deregulation of the retail electric markets by allowing the Price to Beat to expire in January 2007 without subsequently adopting any new price regulations.
- ★ Streamline the permitting process for new electrical generating production facilities, including coal and nuclear, in order to promote diversity and reduce reliance on natural gas.
- ★ Let the market determine the best allocation of production capacity; in this way, producers, not consumers, will bear the risk of new investments in production.
- ★ Maintain the renewable energy production mandate at or below the current level of 5,880 megawatts.

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THE ISSUE

Regulation came late to Texas, and markets came early. It became the last state to regulate retail rates when the Texas Legislature created the Public Utility Commission (PUC). Texas successfully deregulated wholesale power in 1997, requiring the Electricity Reliability Council of Texas (ERCOT) transmission owners to offer nondiscriminatory access to their lines. The foundation for retail competition was laid in 1997 when the Legislature said the public interest required that electric services and their prices should be determined by customer choices and the normal forces of competition. In 1999, the Legislature passed Senate Bill 7, which required the start of customer choice by Jan. 1, 2002.

SB 7 instituted a Price to Beat (PTB) per kilowatt-hour (kwh) for the customers of the incumbent retail providers, known as affiliated REPs. A REP's PTB was based on its 1999 costs, discounted by 6 percent. Affiliated REPs were required to charge the PTB, while unaffiliated REPs (new retail competitors) were free to set their own prices. One of the primary purposes of the PTB was to temporarily provide headroom for the unaffiliated REPs to earn a profit in order to encourage both unaffiliated REPs and consumers to participate, and thus foster the formation of competitive markets.

The new markets have been largely successful. Industrial and large commercial customers had no price to beat, but hardly needed one—over 65 percent of these customers have switched providers. The switching rate for small commercial and residential customers is lower, but not because of a lack of choice. For instance, residential customers in Houston can today choose from 26 rate plans offered by 14 suppliers—customers across the state have similar choices. A PUC study has shown that retail rates are lower today than they would have been without competition.

THE FACTS

- ★ Consumers have access to a variety of suppliers and plans, as seen in the following examples:

Corpus Christi—15 suppliers and 24 rate plans

San Angelo—13 suppliers and 22 rate plans

Houston—14 suppliers and 26 rate plans

Lewisville—12 suppliers and 23 rate plans

Ft. Worth—14 suppliers and 29 rate plans

- ★ A PUC study found that a residential customer in Houston who switched to a competitive retail electric provider four years ago and then switched each following year to the lowest-cost provider would have saved about \$1,450, compared to the estimated regulated rate; a similar customer in Dallas would have saved about \$800.



- ★ The PUC study also said that for each of the past four years, the average price of the five lowest competitive prices in the Houston and Dallas markets was lower than the estimated regulated price there for each year.
- ★ Rates are higher in Texas than in some other states because more power generators in the state rely on natural gas than other fuels to generate electricity. Companies here have generally had to raise rates in response to rising natural gas prices.
- ★ New coal-fired plants scheduled for construction will bring greater diversity to electric production in Texas and reduce reliance on natural gas.

RECOMMENDATIONS

- ★ Maintain the path toward full deregulation of the retail electric markets by allowing the Price to Beat to expire in January 2007 without subsequently adopting any new price regulations.
- ★ Ensure that other provisions of electric utility laws and regulations are not used as a back door to re-regulate electric rates.

RESOURCES

- *Growing Competitive Electricity: Why Texas Must End the Price to Beat* by Robert J. Michaels, Texas Public Policy Foundation (July 2006) <http://www.texaspolicy.com/pdf/2006-07-PP-electricity-bp.pdf>.
- *Report to the 79th Texas Legislature on Scope of Competition in Electric Markets in Texas* by the Texas Public Utility Commission (Jan. 2005) http://www.puc.state.tx.us/electric/reports/scope/2005/2005scope_elec.pdf.
- Texas Electric Choice <http://www.powertochoose.org/>.



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HOMEOWNERS' INSURANCE 86

THE ISSUE

The homeowners' insurance market in Texas has seen dramatic improvement since the mold crisis at the beginning of the decade. At that time, mold claims and homeowners' premiums were skyrocketing, and several companies were on the verge of leaving the Texas market—some homeowners were having a hard time finding policies at any price. However, late in 2002, the Texas Department of Insurance finally allowed insurance companies to use new forms that excluded coverage for mold, which had first been authorized by Senate Bill 1499 back in 1997. Further improvements followed the passage of Senate Bill 14 (2003) that relaxed some regulations on insurance prices, though unfortunately closed the Lloyds exception that allowed many insurers to compete in an unregulated market. Since these changes, the mold crisis has completely disappeared, consumers have generally benefited from reduced rates, and many insurance companies have returned to profitability.

The Texas Department of Insurance reported to the Texas Legislature in March 2003 “rates in 2003 appear to be leveling off.” TDI claimed insurance premiums could have increased as much as 20 percent without form deregulation—the primary reason for the end of the crisis. After the market stabilized, it became less concentrated, with smaller market shares for the largest companies and at least 17 new companies writing policies. The year 2004 signaled a return to profitability and price stability, though one year could not make up for an average annual underwriting loss over the previous decade of 10.6 percent. The 2004 level of profitability was not repeated in 2005, which featured hurricanes Rita and Katrina. However, today Texans hear political calls to regress to our roots of high government regulation on homeowners' insurance.

Though Texas officially has a “file and use” system for rate setting that would allow competition to regulate the marketplace, SB 14 left TDI with too much authority over prices, resulting in a system that is still too politicized and regulated. Total price and form deregulation is needed to bring the best products at the best rates to Texans. Consumer choice, not government regulation, has provided the best value for policyholders. More of this, along with some fair weather, will lead to lower insurance costs for Texas homeowners.

THE FACTS

- ★ “Toxic” mold claims caused insurance loses to soar with average claims of \$15,000 to \$30,000 that could reach upwards of \$100,000.
- ★ High levels of consumer stickiness indicate the presence of a very efficient market in which consumers can more readily confirm the validity of the choices they have made based on value. Loyal, i.e., sticky, customers are a sign of healthy competition.



- ★ The file and use system has the potential of creating a marketplace that allows companies to set rates based on competition with each other and consumer demand—if it is allowed to operate without government interference.
- ★ The Herfindahl Index for Competitiveness in the Texas Homeowners' Insurance Market dropped from 1662.736 in 1998 to 1388.108 in 2003, indicating Texas has become more competitive regarding homeowners' insurance.
- ★ Illinois, with no price regulation since 1970, has the highest number of companies writing homeowners' policies in the nation at or below the national average.

RECOMMENDATIONS

- ★ TDI should focus on market conduct, solvency, and consumer information, leaving pricing and forms to the market.
- ★ The Texas Legislature should develop a long-term plan for eliminating price regulation of homeowners' insurance that includes codifying terms to ensure a true, least-regulatory form of file and use that allows competitive pricing to determine the cost of insurance premiums.

RESOURCES

- *Consumer Stickiness: A Sign of Healthy Competition* by Bill Peacock, Texas Public Policy Foundation (Mar. 2005) <http://www.texaspolicy.com/pdf/2006-03-consumerstickiness-bp.pdf>.
- *Is the Free Market Working for the Texas Homeowners' Insurance Market?* by Bill Peacock, Texas Public Policy Foundation (Feb. 2006) <http://www.texaspolicy.com/pdf/2006-02-PP-homeowners-bp.pdf>.
- *Homeowners' Insurance: Moving Toward Competition or More Regulation?* by Bill Peacock, Texas Public Policy Foundation (May 2005) <http://www.texaspolicy.com/pdf/2005-05-homeowners.pdf>.
- *Deregulation, Pricing And Availability Issues In The Texas Personal Homeowners' Insurance Market* by Patricia M. Arnold and Patrick Brockett, Texas Public Policy Foundation (Dec. 2004) <http://www.texaspolicy.com/pdf/2004-12-home.pdf>.
- *Homeowners Insurance Price Comparisons* Texas Department of Insurance, <http://www.tdi.state.tx.us/consumer/txshoph.html>.
- *Comparing Homeowners Policy Coverages* Office of Public Insurance Counsel, <http://www.opic.state.tx.us/hoic.php>.
- *The Insurance Industry and Homeowners Adapt to a New Regulatory Framework* House Research Organization (Oct. 2004) <http://www.capitol.state.tx.us/hrofr/interim/int78-9.pdf>.



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THE ISSUE

For many years now, road congestion in Texas has seemed to become steadily worse. Today, Austin is considered the most congested city of its size in the nation, and the obvious traffic headaches in Houston and Dallas/Fort Worth are even worse. Roadways serving as major freight arteries between cities, such as IH-35, are under increasing pressure as a result of NAFTA and increasing traffic from Texas' sea ports.

Despite growing road demand in Texas, little had been added to the state's road network in recent years. Due to inflation and increasing vehicle fuel efficiency, the purchasing power of the Texas fuel tax has decreased. Construction costs, however, have risen markedly due to increased world demand for cement and steel.

Roads are a valuable commodity and have historically been essentially given away with no direct charge for their use. Fuel taxes have proven a very poor substitute for directly pricing roads. With the passage of HB 3588 in 2003, the Legislature radically departed from past policy. Today, there is a new emphasis on tolling road infrastructure so as to accelerate road projects and provide a long-term funding solution. New contracting methods have also been used. For example, parts of toll roads utilizing new contracting methods in the Austin area are estimated to be completed far ahead of schedule.

The Texas Legislature continues to be subject to pressure to retrench on transportation policy. It is debatable whether regional mobility authorities are the best way to get local input in planning and implementing toll funding strategies. The Trans-Texas Corridor's design and footprint should also be subject to continued discussion. High-cost, non-tolled projects also continue to be constructed in areas with no congestion. What should not be debated, however, is whether to maintain tolling as a principle method of funding roads. Pricing is the best way to allocate any valuable commodity, including roads. To leverage these funds will mean fast congestion relief for Texans.

THE FACTS

- ★ As of 2002, there were 301,778 miles of public roads in Texas—79,493 miles were owned by the state, 142,636 were owned by counties, and 78,653 were owned by municipal authorities.
- ★ Only 12.5 percent of Texans carpool and fewer than 2 percent use public transportation, including taxis.
- ★ The number of vehicle miles traveled per person in Texas in 2000 was 800 miles greater than the national average.
- ★ From 1990 to 2003, the number of lane miles of public road on the Texas state system increased 4 percent while the number of total vehicle miles traveled on the state system increased 52.8 percent.



- ★ In 2001, 22 percent of all Texas road bridges were functionally obsolete or structurally deficient, representing 10,555 structures, more than in any other state.
- ★ Travel delay caused by congestion in Texas increased from 750 million hours in 1982 to 3.6 billion hours in 2000.
- ★ Of the top 50 U.S. foreign trade freight gateways (by value of shipments), eight are in Texas, with four on the Texas/Mexico border.

RECOMMENDATIONS

- ★ Stop funding construction projects in areas where congestion is not a problem.
- ★ Convert high-occupancy vehicle lanes to managed (toll) lanes.
- ★ Make greater use of privatization of routine maintenance like the VMS contract in the Waco district.
- ★ Continue to pursue toll road financing for expansion of the state's road network.
- ★ Resist calls to increase state fuel taxes.
- ★ Create incentives for cities to allow the development of private transit services.

RESOURCES

- *Texas Road Policy: Keeping Up With Demand* by Byron Schlomach, Texas Public Policy Foundation (Feb. 2005) <http://www.texaspolicy.com/pdf/2005-02-transportation.pdf>.



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THE ISSUE

In Texas, criminal law is not just for criminals anymore—at least not criminals as we have traditionally defined them. There are 779 Texas statutes that contain the word misdemeanor, but only 64 of these instances are in the Penal Code or Code of Criminal Procedure. Likewise, the word “felony” appears 418 times in Texas statutes, but only 64 of these occurrences are in the Penal Code or Code of Criminal Procedure. Many of the remaining 1,069 references to felony or misdemeanor are to the existence of criminal offenses for ordinary business activities in fields such as agriculture, health care, natural resources, and insurance.

There are significant differences between criminal and civil law, which make criminal law an overly blunt instrument for regulating non-fraudulent business activities. The centrality of punishment remains a distinguishing feature of criminal law. While incarceration is traditionally associated with violent crime, half of all Texans behind bars are there for nonviolent offenses.

Another distinction between the two systems of law is that criminal law, because it is enforced entirely by state prosecution, tends to minimize the importance of the harm to the victim. Traditionally, civil and criminal law have also been distinguished by the requirement that a criminal must have a guilty state of mind, expressed by the Latin term *mens rea*.

In the 79th Legislative Session, many bills would have criminalized conduct traditionally addressed through the free market or civil law. Proposed legislation would have criminalized everything from failure to recycle any piece of electronics equipment to placing a business sign on a rural road, and even leaving a dog tethered to a tree for a total of 8 hours in a 24-hour period. Other bills would have increased the criminal penalties for existing offenses. For example, legislation would have inexplicably made unscrupulous business practices relating to construction or repair of home a state jail felony, while such practices would remain a misdemeanor in all other industries. Fortunately, all of these measures were defeated. However, House Bill 1361 authorized the Texas Animal Health Commission to implement the National Animal Identification System (NAIS) being forced upon states by the U.S. Department of Agriculture and created a Class C misdemeanor for failure to comply.

The 79th Legislature commendably acted to rein in overcriminalization by prohibiting local criminal ordinances that dispense with strict criminal liability while authorizing a fine of more than \$500, reforming the public school zero tolerance law to allow a child’s intent to be considered in deciding whether expulsion is appropriate, and limiting the use of city nuisance laws to criminalize law-abiding businesses that are victimized by crime.

THE FACTS

- ★ The General Accounting Office tallied over 4,000 federal criminal laws before it stopped counting. No similar total is available for Texas.



- ★ After a torrent of criticism from small farmers and ranchers, the Texas Animal Health Commission decided in April 2006 to postpone consideration of the mandatory animal identification program until the winter or spring of 2007.
- ★ Prior to the passage of House Bill 1690 in the 79th Legislature, which reined in local nuisance laws, cities like Dallas were able to use businesses' reporting of crime against them to charge them with maintaining a nuisance.

RECOMMENDATIONS

- ★ Avoid creating new criminal offenses, especially for non-fraudulent business activities. If new regulations are necessary, civil fines and revocation of state permits and licenses can be used as enforcement mechanisms.
- ★ Ensure culpable mental state is required for conviction under most criminal statutes. With narrow exceptions such as speeding, due process requires a culpable mental state of at least criminal negligence for conviction.
- ★ Monitor state agencies to ensure they are not engaging in overly broad interpretations of criminal law contrary to legislative intent. The Texas Alcoholic Beverage Commission's recently suspended policy of arresting bar patrons for public intoxication may contradict the Legislature's intent that the 0.08 threshold be used for determining one's competency to operate a motor vehicle.
- ★ Revise mandatory animal identification program. This program should be voluntary. Short of that, the Legislature could also replace the current criminal penalty with a civil fine.

RESOURCES

- *Not Just for Criminals: Overcriminalization in the Lone Star State* by Marc Levin, Texas Public Policy Foundation (Apr. 2005) <http://www.texaspolicy.com/pdf/2005-04-pp-overcrim.pdf>.
- *Big Government's New Pet Project* by Marc Levin, Texas Public Policy Foundation (Mar. 2006) http://www.texaspolicy.com/commentaries_single.php?report_id=1057.
- *It Shouldn't Be a Federal Offense to Offend* by Marc Levin, Texas Public Policy Foundation (Feb. 2006) http://www.texaspolicy.com/commentaries_single.php?report_id=1025.
- *Overextending the Criminal Law* by Erik Luna, Cato Institute (Nov./Dec. 2003) http://www.cato.org/pubs/policy_report/v25n6/luna.pdf.
- *Criminalization Out of Control* by Gene Healy, Cato Institute (June 2005) http://www.cato.org/pub_display.php?pub_id=3883.
- *Sometimes There Ought Not Be a Law* by Paul Rosenzweig and Steve Muscatello, Heritage Foundation (Apr. 2005) <http://www.heritage.org/Press/Commentary/ed040605a.cfm>.

THE ISSUE

Drug courts are an alternative to incarceration for minor drug offenders willing to take responsibility for their actions, using prison only as leverage to ensure compliance. Drug courts involve comprehensive supervision, drug testing, treatment services, family and community interaction, and immediate sanctions and incentives. Successful completion of the drug court program results in dismissal of the charges (pretrial diversion) or satisfaction or reduction of the sentence (reentry or intensive probation).

The most well-known drug court in Texas is a pretrial diversion program overseen by Dallas Judge John Creuzot, which limits eligibility to first-time minor drug offenders. While participation is voluntary, Judge Creuzot informs prospective participants that they cannot opt out once they enroll.

The 77th Legislature authorized counties to create drug courts and required courts in counties with populations over 550,000. While Texas had only three drug courts in 2002, there are now 44 drug courts with another 20 in the planning stages, including adult, juvenile, family, DWI/DUI, and tribal drug courts. Nationally, there are over 1,600 drug courts, indicating that Texas has substantially fewer drug courts per capita than other states.

Although drug court judges are ideally situated to supervise a treatment regime, other judges can sentence a drug offender to inpatient or outpatient mandatory drug treatment as part of their probation agreement. Additional funding provided by the 79th Legislature has resulted in 500 new community corrections facility beds, some of which are at substance abuse centers, and outpatient drug rehabilitation services for 4,000 additional probationers. Yet, the state still has 1,400 fewer beds than in 1995 despite a larger population of probationers now totaling 450,000. As a result, Bexar County District Judge Mark Luitjen says waiting times are as long as six months to get a drug offender into a residential substance abuse treatment center and, because that time must be spent in the county jail, many judges and even some offenders choose prison instead.

THE FACTS

- ★ Texas offenders completing drug court programs have a 28.5 percent re-arrest rate compared to 58.5 percent in the control group of those who did not go through a drug court.
- ★ A comprehensive drug court program typically costs between \$2,500 and \$4,000 annually for each offender, a fifth of the cost of prison. A study of a drug court in Portland, Oregon found \$5,071 in savings, including victimization costs, due to reduced rates of drug use and recidivism.
- ★ Increased utilization of alternatives to incarceration for nonviolent drug offenders could help avoid the need to spend nearly \$1 billion in



constructing nearly 10,000 new prison beds that the Legislative Budget Board says will be necessary by 2010 if current policies and trends continue.

RECOMMENDATIONS

- ★ Divert funding for new prisons to drug courts. The state only provides \$3.75 million in funding for drug courts, but creating more drug courts could help avoid billions of expenditures associated with building and operating new prisons.
- ★ Increase capacity of inpatient and outpatient drug treatment programs. These programs are more cost efficient than jails and prisons, but long waiting times make them unattractive to many judges as alternatives to incarceration.
- ★ Raise threshold for amount of drugs that triggers a long prison sentence. For example, Chapter 481 of the Health and Safety Code creates a third degree felony for possession of between one and four grams of drugs in Penalty Group 1, which includes morphine. Under Section 12.34 of the Penal Code, a third degree felony requires a prison sentence of between two and ten years. By raising the threshold for the amount of drugs that turns a state jail felony into a third degree felony, dealers would continue to face significant prison terms while mere users can be redirected into mandatory treatment in inpatient or outpatient rehabilitation programs.
- ★ Reduce state jail felonies for possessing a small amount of drugs to Class A misdemeanors. This could redirect more minor drug offenders from state jails to probation with mandatory drug treatment. It would also spare many minor drug offenders the difficulty that convicted felons face when trying to find employment and housing, obstacles that often side-track recovery and community reintegration.

RESOURCES

- *Drug Courts: The Right Prescription for Texas* by Marc Levin, Texas Public Policy Foundation (Feb. 2006) <http://www.texaspolicy.com/pdf/2006-02-PP-drugcourts-ml.pdf>.
- *Drug Court Clearinghouse Project at American University: Summary of Drug Court Activity by State and County* (Sep. 29, 2005) http://spa.american.edu/justice/publications/us_drug-courts.pdf#page=892004.
- *Initial Process and Outcome Evaluation of Drug Courts in Texas* Criminal Justice Policy Council, Jan. 2003.
- National Association of Drug Court Professionals, <http://www.nadcp.org>.

THE ISSUE

In 1989, Texas adopted a constitutional amendment now in Article I, Section 30 of the Texas Constitution establishing the various rights of crime victims. This included the rights to reasonable protection from the accused throughout the trial process, notification of court proceedings, to be present at all public proceedings, to confer with a prosecutor's representative, and to receive restitution.

Current state law allows a victim to submit a written impact statement that the court shall consider prior to sentencing but after conviction of the defendant and an oral statement after the sentence is pronounced. In 2005, House Bill 1751 became law, strengthening Texas' restitution statutes by requiring that trial courts that decline to order restitution provide a written explanation.

The Texas Crime Victims' Compensation Fund offers victims reimbursement of up to \$50,000 in medical and other costs resulting from violent crime.

Texas has 14 restitution centers with a total capacity of 737 beds. Judges may sentence offenders, who might otherwise go to prison, to probation and confinement in a restitution center. Residents work full time, perform community service, and participate in educational and rehabilitative programs.

Texas does not have a statewide victim-offender mediation program (VOMP), although several Texas counties offer VOMPs for juvenile crime victims. Victims must choose a VOMP over the traditional court system and offender participation is also voluntary, since the offender is required to take responsibility for his conduct and waive his right to trial and appeal.

A written agreement is reached that typically requires restitution, community service, and counseling. The agreement is then ratified by the prosecutor or judge. Failure to comply subjects the offender to traditional prosecution and, if necessary, incarceration. There are now more than 300 VOMPs in North America, almost of all which are limited to nonviolent crimes, such as property offenses.

THE FACTS

- ★ In 2003, Texas collected roughly \$48 million in restitution payments.
- ★ Some 95 percent of cases resolved through victim-offender mediation result in a written agreement and 90 percent of these restitution agreements are completed within one year, a rate of restitution payments that far exceeds the national collection rate of 20 to 30 percent for court-ordered restitution.
- ★ One study found that 79 percent of victims who participated in VOMPs were satisfied, compared with 57 percent of victims who went through the traditional court system. Also, the 1,298 juveniles who participated in a pretrial VOMP were 32 percent less likely to recidivate.



- ★ The evidence indicates that restitution centers are efficient and effective. It costs the state an average of \$7,957 to place an offender in a community corrections facility, less than half the cost of prison. Moreover, restitution center residents paid more than \$4.5 million toward victim restitution, fines and fees and contributed another \$600,000 in community service restitution.

RECOMMENDATIONS

- ★ Allow victims to present an oral impact statement prior to sentencing. The 79th Legislature failed to hold a hearing on House Bills 338 and 442, which would have permitted this.
- ★ Allow victims to choose pretrial victim-offender mediation. Victims of property crimes should be empowered to select mediation with a binding restitution contract enforced by the state as an alternative to traditional prosecution and sentencing.
- ★ Give victims a seat at the table in plea bargaining. Follow Arizona in giving victims the right to participate in any plea negotiations.
- ★ Improve restitution monitoring. There is incomplete data on the success of the 121 local probation districts in collecting restitution. The state should evaluate these districts in part based on their success in collecting restitution.
- ★ Improve restitution collections. Explore the use of garnishment from wages, which the state uses for collecting child support, as a means of increasing the rate of restitution collections. Also, a procedure should be created whereby all victims can easily obtain a restitution lien against the offender's property. Finally, the law should be changed so restitution orders automatically follow a probationer revoked to prison when that offender is later released on parole.
- ★ Expand capacity of restitution centers. Victims can be better compensated and the state can save money by sentencing more nonviolent property offenders to work restitution centers as an alternative to prison.

RESOURCES

- *Restorative Justice in Texas: Past, Present & Future* by Marc Levin, Texas Public Policy Foundation (Sep. 2005) <http://www.texaspolicy.com/pdf/2005-09-restorativejustice.pdf>.
- *Victim-Offender Mediation and Plea Bargaining Reform in Texas* by Marc Levin, Texas Public Policy Foundation (Apr. 2006) <http://www.texaspolicy.com/pdf/2006-04-PP-VOM-ml.pdf>.
- TDCJ Victim Division Services, <http://www.tdcj.state.tx.us/victim/victim-home.htm>.
- *2004 Crime Victims' Compensation Fund Annual Report*, http://www.oag.state.tx.us/AG_Publications/pdfs/2004cvc_annual.pdf.
- *Restorative Justice Through Victim-Offender Mediation: A Multi-Site Assessment* by Mark S. Umbreit, *Western Criminology Review* 1:1 (1998) <http://wcr.sonoma.edu/v1n1/umbreit.html>.

THE ISSUE

Texas is again facing a prison crowding crisis, with prisons now at capacity with over 150,500 inmates. If policies are not changed to reduce prison inflows, the Legislative Budget Board projects that 9,600 new beds will be needed by 2010. This could mean prison construction costs of \$1 billion plus additional operation costs of \$224 million.

The 79th Legislature allocated \$19.9 million to lease beds in 2006 and \$43.8 million for 2007. Gov. Rick Perry vetoed all but \$10 million for leased beds in the current fiscal year. Most of these beds are leased from county jails. Yet county jails themselves are bursting with some 70,000 inmates. Some 44 county jails are out of compliance with Jail Standards Commission criteria.

The imperative to house more and more offenders devours much of the criminal justice budget, leaving little money for programming in prison, such as drug and mental illness treatment, as well as reentry services, which reduce recidivism.

State inmates who are diverted to leased beds in county jails receive even less programming. County jails are designed for temporary placement of offenders awaiting trial and serving short sentences for misdemeanors. County jails are not served by the Windham School District, which offers courses to state prisoners.

Crowding has long frustrated the intended design of the correctional system. In 1993, 17 state jails were created near urban areas to house minor drug and property offenders, segregating them from more serious offenders and bringing them closer to their point of reentry. Yet, due to crowding, transferees from prisons now fill more than half of state jail beds and reentry services are in short supply.

Approximately 15,000 Texas prison beds are in privately operated facilities. While outsourcing has produced significant savings, stringent state regulations imposed by the Texas Department of Criminal Justice (TDCJ) interfere with the ability of private prison operators to save money and improve programming. For example, TDCJ requires that private prisons use the state's key systems.

Similarly, TDCJ prevents private operators from implementing drug treatment programs that differ from those offered by the state. Instead, the private prison operators must use instructors with the same certifications and implement a program of the same duration as the state's treatment program. Some 63 percent of prison inmates are substance abusers, but less than 15 percent of inmates are actually enrolled in any of the state's drug treatment programs due to limited funds and the high per inmate cost of the state's programs.

THE FACTS

- ★ From 1988 to 2004, the state's prison population grew by 278 percent while the state's overall population rose by only 35 percent.



- ★ Only one-third of county jails offer any drug treatment.
- ★ Privately operated prisons save the state 10 to 14 percent while providing similar or better programming.

RECOMMENDATIONS

- ★ Minimize pretrial confinement in county jails. Defendants in drug cases, in particular, wait long periods due to delays in the Department of Public Safety's testing for controlled substances. All the while, taxpayers are paying about \$40 a day to put each county jail inmate behind bars.
- ★ Make state jail felons eligible for parole. State jail felons, who are primarily nonviolent drug and property offenders, are currently ineligible for parole. Space at state jails can thereby be freed up for violent offender transferees from state prison.
- ★ Expand faith-based programming. Faith-based prison programs such as the ecumenical Bridges to Life and the Christian Inner Change Freedom Initiative have been proven to reduce recidivism.
- ★ Lease beds from private operators in lieu of building new prisons or leasing beds from county jails. Private prison operators have offered to temporarily house overflow inmates at a lower cost than county jails and with a full array of education, job training, treatment, and reentry programs not found in most county jails.
- ★ Allow alternative treatment programs in privately operated jails. Private prison operators should be encouraged to innovate by implementing less costly drug treatment programs that have proven effective at their facilities in other states and can reach more inmates with the same amount of funds.

RESOURCES

- *How to Avert Another Texas Prison Crowding Crisis* by Marc Levin, Texas Public Policy Foundation (May 2006) <http://www.texaspolicy.com/pdf/2006-05-PP-prisoncrowding-ml.pdf>.
- *Aligning Incentives and Goals in the Texas Criminal Justice System* by Marc Levin, Texas Public Policy Foundation (Nov. 2005) <http://www.texaspolicy.com/pdf/2005-11-perversoincentives-pp.pdf>.
- *Adult and Juvenile Correctional Population Projections Fiscal Years 2005-2010*, Legislative Budget Board, (Jan. 2005) http://www.lbb.state.tx.us/PubSafety_CrimJustice/Projections_Reports_2005.pdf.
- *A Portrait of Prisoner Reentry in Texas* by J. Watson, A. L. Solomon, N.G. La Vigne & J. Travis, Washington, DC: Urban Institute (Mar. 2004) http://www.urban.org/UploadedPDF/410972_TX_reentry.pdf.
- *Privatization and Competition in Corrections* by Geoffrey Segal, Reason Public Policy Research Institute (Aug. 2003) <http://www.rppi.org/competitionin corrections.html>.

THE ISSUE

Some 455,000 Texans, or one out of every 20 Texans, are on probation. The 37 percent of prison intakes and 41 percent of state jail intakes that are revoked probationers account for \$547 million in direct incarceration costs. Texas has the longest probation terms in the country at up to 10 years.

The 79th Legislature offered the 121 local probation departments additional funds to hire new probation officers in return for implementing progressive sanctions, which reduce revocations by responding to each probation infraction with measured punishments, such as increased reporting requirements, a curfew, electronic monitoring, or a shock night in jail. In the first quarter of 2006, there has been a 12 percent decrease in felony probation revocations attributable to the departments that accepted the new money and implemented progressive sanctions.

Approximately 76,000 Texans are on parole or mandatory supervision. While mandatory supervision is determined based on the number of days served plus good time, the Texas Board of Pardons and Paroles (TBPP) makes discretionary decisions regarding applications for parole. Unlike the probation system which largely functions independently in the 121 districts, TDCJ's Parole Division supervises parolees, utilizing 66 local offices. Programming includes substance abuse counseling and Project RIO (Reintegration of Offenders), which provides job training and placement. In 2004, the statewide parole revocation rate was only 11 percent.

Each year, over 50,000 prisoners reenter Texas neighborhoods. Although 63 percent of prisoners have a substance abuse problem, only five percent received treatment while in prison, although as many as half receive such treatment as part of aftercare programs following release. Only 28 percent of mentally ill prisoners and parolees receive treatment.

THE FACTS

- ★ The Wisconsin Policy Research Institute found: "Even 10 percent less recidivism by those on probation, parole and pretrial release would mean nearly 20,000 fewer crimes a year, saving citizens \$122 million annually and offsetting about 88 percent of the cost of community corrections."
- ★ A TDCJ survey indicated that over 70 percent of judges would use probation more often as a sentencing option or as an alternative to revocation if more community corrections facility beds were available.
- ★ According to the Criminal Justice Policy Council, Texas saves 49.5 percent in reduced incarceration costs for each offender placed in a residential work restitution center or mental illness treatment facility.

RECOMMENDATIONS

- ★ Implement progressive sanctions statewide and release probationers who have met all of their obligations. Progressive sanctions have been proven



to reduce revocations and the 80th Legislature should insist that they be used throughout the state. By imposing gradual measures, probationers who miss a meeting, fail a drug test, or commit another technical violation can be reformed without resorting to revocation to prison, which results in an average sentence of more than four years.

- ★ Release offenders from probation who have met all their obligations, including paying restitution or participating in a garnishment system to assure remaining restitution payments. This will allow probation resources to be focused on the offenders who need intensive supervision. The Travis County Probation Department developed a matrix for classifying probationers based on their original offense and socialization level to target each probationer with the most appropriate type and degree of supervision.
- ★ End revocations of probationers for drug relapses. Probationers who test positive for drugs or are arrested for drug possession are often revoked to prison for four or more years, even for a small quantity of marijuana (usually a fine or at most a brief stay in county jail for a non-probationer). Given that successful graduates of drug treatment programs often have several relapses, probationers in treatment or willing to undergo treatment should not be revoked to prison for possession of small quantities of drugs.
- ★ Expand availability of reentry programs. Reentry programs, including job training, treatment for substance abuse and mental illness, and faith-based programs, are correlated with reduced recidivism.
- ★ Eliminate past drug or alcohol use as a reason for denying parole. Among the factors that the TBPP uses in deciding whether to grant parole is “excessive drug or alcohol involvement in the instant offense or criminal history.” A substance abuse problem many years ago may not correlate with an offender’s risk of recidivism today, particularly if appropriate treatment programs are available in prison or on parole.

RESOURCES

- *How to Avert Another Texas Prison Crowding Crisis* by Marc Levin, Texas Public Policy Foundation (May 2006) <http://www.texaspolicy.com/pdf/2006-05-PP-prisoncrowding-ml.pdf>.
- *Aligning Incentives and Goals in the Texas Criminal Justice System* by Marc Levin, Texas Public Policy Foundation (Nov. 2005) <http://www.texaspolicy.com/pdf/2005-11-perverseincentives-pp.pdf>.
- *Keep the Keys: Texas Probation System Needs Correction* by Marc Levin, Texas Public Policy Foundation (Apr. 2005) http://www.texaspolicy.com/commentaries_single.php?report_id=790.
- Texas Senate Criminal Justice Committee Interim Report to the 79th Legislature, http://www.senate.state.tx.us/75r/Senate/commit/c590/downloads/112004CJ_Report.pdf.
- *A Portrait of Prisoner Reentry in Texas* by J. Watson, A. L. Solomon, N.G. La Vigne & J. Travis, Washington, DC: Urban Institute (Mar. 2004) http://www.urban.org/UploadedPDF/410972_TX_reentry.pdf.

THE ISSUE

Hundreds of thousands of Texas students are removed from regular schools and placed in Disciplinary Alternative Education Programs (DAEPs), Juvenile Justice Alternative Education Programs (JJAEPs), and Texas Youth Commission (TYC) residential facilities.

DAEPs are alternative settings to the regular classroom for students who commit virtually any disciplinary violation. All school districts must operate a DAEP. Many DAEPs are self-contained campuses while others are on the premises of a regular school. A student can be placed in a DAEP for any violation of the student code of conduct. School districts operate DAEPs with only minimal oversight by the Texas Education Agency. For example, state law requires that DAEPs provide only two hours of instruction everyday.

JJAEPs are juvenile justice day programs operated by county juvenile boards and overseen by the Texas Juvenile Probation Commission (TJPC). JJAEPs currently serve 6,907 students, the vast majority of whom have been expelled from school. JJAEPs also receive students who engage in serious or persistent misconduct while at a DAEP. Unlike DAEPs, JJAEPs are subject to extensive state oversight and accountability.

TYC residential facilities house approximately 2,500 juveniles who commit the most serious offenses.

In addition to the students who are sequestered, many other students receive misdemeanor citations in school for routine disciplinary violations. Rep. Harold Dutton (D-Houston) successfully defended an 8 year-old student in municipal court who had received a Class C ticket from a school police officer for chewing gum in class.

THE FACTS

- ★ DAEP placements have increased from 70,728 individual students placed in 1999-2000 to 103,696 in 2003-04. About 80 percent of DAEP placements are discretionary.
- ★ Students who remain at a JJAEP for at least 90 days are given the national Kaufman Test of Educational Achievement Analysis (KTEA) upon their entrance into and departure from the program. In 2003, the students tested gained slightly more than a half of a grade increase in achievement level.
- ★ Misdemeanor citations issued in school are on the rise. From September 2004 through August 2005, there were 10,149 Education Code cases referred to Texas municipal courts. During the same period from 1998 to 1999, there were 6,888 such cases.



RECOMMENDATIONS

- ★ Increase DAEP accountability. The state should no longer permit students at DAEPs to receive as little as two hours of instruction compared to the seven hours required for all other students. The state should also require that larger DAEPs offer the courses needed for high school graduation. The KTEA should be administered to determine whether students are learning at DAEPs and students' academic achievement, attendance, and behavior should be monitored after leaving a DAEP to gauge effectiveness.
- ★ Separate violent students from non-violent students. While most students at DAEPs have simply been disruptive in class, there are some who have committed violent crimes, but are not at JJAEPs because the crimes were off-campus and thus do not trigger expulsion. Fort Worth ISD has successfully created two tiers of DAEPs for these very different student populations. State law could also be changed to allow students guilty of violent off-campus crimes to be placed directly in a JJAEP.
- ★ Expand access to JJAEPs. In the 221 counties without JJAEPs, students are simply expelled to the street. The state could assist the most populous of these 221 counties by creating a JJAEP which could utilize distance education to reduce costs.
- ★ Reform zero tolerance. The 79th Legislature enacted House Bill 603, which allows schools to consider whether a student had a culpable mental state and a prior disciplinary history in issuing a mandatory expulsion or removal to a DAEP. However, reports that some districts continue to apply zero tolerance without common sense suggest that this legislation might need to be strengthened.
- ★ End issuance of criminal citations in school for routine disciplinary infractions that do not violate any state or local law. House Bill 443 in the 79th Legislature would have amended Section 37.102 of the Education Code to accomplish this.

RESOURCES

- *Schooling a New Class of Criminals* by Marc Levin, Texas Public Policy Foundation (Mar. 2006) <http://www.texaspolicy.com/pdf/2006-03-PP-DAEP-ml.pdf>.
- *Disciplinary Alternative Education Programs: What Is and What Should Be* by Marc Levin, Texas Public Policy Foundation (Dec. 2005) <http://www.texaspolicy.com/pdf/2005-12-DAEPs-pb.pdf>.
- *Education or Gateway to Incarceration*, Policy Primer Audio by Texas Public Policy Foundation (Dec. 2005) <http://www.texaspolicy.com/audio/2005-12-07-pp.html>.
- *Texas Youth Commission Annual Report*, http://www.tyc.state.tx.us/about/annual/section2/p6_profile.html.
- *Zero Tolerance Horror Stories* by George Clowes, Heartland Institute (June 2003) <http://heartland.org/Article.cfm?artId=12352>.
- *A Guide to Successful Practices: What Works for Disciplinary Alternative Education Programs?* Academic Information Management, Inc., <http://www.aimdata.com/aimdaep.htm>.



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THE ISSUE

Water promises to be one of the most urgent, complex, and contentious issues for the 80th Texas Legislature. Demands of an expanding population compete with agricultural, industrial, and environmental needs for a plentiful water supply. While shortages have required some cities to transport water from distant sources over the past several years, there is more than sufficient water to meet the needs of all Texans today. However, water shortages could loom in the future if population growth fulfills expectations and drought constricts supply.

The State Water Plan proposes that future water needs be largely met by voluntary redistribution of water. The challenge is to find the means to redistribute water and to supplement this supply with emerging technologies, such as desalination. The high cost of redistribution and technologies have stimulated state government to expand public-private partnerships and private markets to help underwrite the cost. Now, fundamental principles of state water law—state “ownership” of surface water, state regulation of ground water, prior appropriation, and beneficial use—must be reconfigured to meet the rapidly changing needs of Texans.

Although future water supply will largely depend on private sector engagement, at present the private sector is allowed a very restricted role in water production and distribution. Because ground and surface water are highly regulated, the current water debate focuses on the role of government. Policymakers must ask if government regulation is the best way to protect public interest, determine fair water use, and protect the environment.

Some policymakers press to curtail private rights and increase government regulation to protect public interest and the environment against ruinous exploitation. Others press for the alternative to water regulation—water marketing—where supply and demand determine production, allocation, and use. Based on the experience of several western states, some policymakers believe water marketing is more effective than regulation in increasing water supply, conservation, and environmental protection. These policymakers propose strengthening private property rights for all water uses, making water rights freely transferable, and creating a legal system that will enforce these rights.

THE FACTS

- ★ Texas has approximately 191,000 river miles flowing through 23 major river basins and nine major and 20 minor aquifers.
- ★ Texas is home to the Ogallala, the world’s largest aquifer—it stretches across eight states and underlies 174,000 square miles.
- ★ Over half of the water Texans drink comes from aquifers.



- ★ The average Dallas resident uses 250 gallons of water each day.
- ★ Over three-quarters of irrigation comes from groundwater.
- ★ Water development strategies proposed by regional water groups have a price tag of almost \$18 billion.
- ★ The Texas Water Development Board says Texas needs eight new major reservoirs and 10 minor reservoirs at a cost exceeding \$4 billion.
- ★ Almost 66 percent of future water needs will be met by voluntary redistribution.
- ★ Almost 14 percent of future water needs could be met by water conservation measures.

RECOMMENDATIONS

- ★ Strengthen private property rights.
- ★ Make water rights freely transferable.
- ★ Strengthen enforceability of private property rights.
- ★ Allow individuals and associations to lease or purchase surface water from the state.
- ★ Replace contested regulations with explicit legislation.
- ★ Implement a long-term plan for water marketing to serve as the primary means of providing an adequate water supply for human, agricultural, industrial, and environmental needs.
- ★ Transfer regulatory authority to local boards, but demand general uniformity and fairness.
- ★ Expand incentives for soil and water conservation.
- ★ Focus state resources on serving as a clearinghouse for water marketing and banking, coordinating regional boards, providing scientific information, and proposing voluntary standards.
- ★ Expand public-private partnerships for developing and delivering water.
- ★ Encourage public utilities to privatize water production and/or distribution services.

RESOURCES

- *Choppy Waters: Understanding The Challenges To Texas Water Policy* by Susan Combs, Katharine Armstrong, and Kathleen Hartnett White, Texas Public Policy Foundation (Aug. 2004) <http://www.texaspolicy.com/pdf/2004-08-choopy-waters.pdf>.

THE ISSUE

Within the next 50 years, the population of Texas is expected to double. Finding sufficient water to meet rapidly growing demands presents a critical challenge for Texas policymakers. Efficiently managed, Texas has sufficient water resources across the state to meet those demands. Both the 1997 and 2002 State Water Plans identify voluntary redistribution of water as one of the primary means to meet future water needs. Water transfer has been successfully used in Texas and throughout the American West to provide water for growing cities, recreational purposes, and environmental needs; to promote efficient water use and conservation; to provide an alternative to reservoir construction; and to encourage bargaining between divergent interests.

Cities, ranchers, farmers, and industries have been transferring water for decades. These transactions have proven that voluntary redistribution, instead of government-compelled reallocation and regulation, serves as the best means to meet growing water needs.

Private property rights must be strengthened and state regulatory burdens must be eased to encourage and expand efforts to transfer water from areas of surplus to areas of need.

Certain Texas laws and policies need rethinking. For instance, Junior Water Rights were created in 1997 to discourage interbasin transfer, the junior water rights law makes rights to transferred water secondary to other rights in the basin. This rule makes ownership conditional on available supply; thus, in times of water scarcity, purchasers of water have no rights to the water they purchase. Another issue is the regulatory requirements of the Texas Commission on Environmental Quality (TCEQ) that make small water transfers uneconomical. Although small transfers of 3,000 acre-feet have been determined to have no impact and are exempt from the junior water rights rule, the Commission is required to subject small transfers to potentially expensive contested hearings. Additionally, groundwater districts exercise regulatory authority that acts as a chilling effect on water transfers. Districts have the authority to limit the amount of water that can be sold and can impose an export fee on transfers; they can also limit where water is transported and how it is used. Finally, changing water needs require updates to state law to allow the private sector a larger role in developing water sources, transporting water, and distributing water—particularly in municipalities.

THE FACTS

- ★ Texans use about 16.5 million acre-feet of water annually.
- ★ Nine aquifers supply almost 97 percent of groundwater used in the state.
- ★ Groundwater accounts for about 60 percent of Texas usage.
- ★ Conservation districts cover 90 percent of groundwater in Texas.



- ★ Eighty percent of groundwater is used for irrigation.
- ★ Sixty-five percent of surface water is used for municipal and industrial purposes.
- ★ Municipal and industrial use of water is expected to increase 5.4 million acrefeet annually and increase 28 percent over current use within the next 30 years.
- ★ Water transfer and marketing is now occurring all across Texas; Amarillo, Lubbock, and nine other Panhandle cities pump water from rural wells.
- ★ Fourteen of the 16 Regional Planning Groups propose water transfer projects—groups propose transferring approximately 33 percent of Texas surface water and 25 percent of groundwater used today.
- ★ The Brazos Valley Water Alliance, a landowner cooperative, has accumulated 133,000 acres of land in Brazos, Burtleson, and Milam counties and currently seeks a purchaser for its groundwater.

RECOMMENDATIONS

- ★ Allow transactions of less than 3,000 acre-feet to be exempt from the no-injury and contested case hearing rule if TCEQ determines there is minimal impact.
- ★ Eliminate the Junior Water Rights rule on interbasin transfers to strengthen private property rights and develop efficient water markets.
- ★ Remove legal barriers to private investment in providing surface and groundwater for municipal use.
- ★ Redefine the role of groundwater districts—management of groundwater at the local level will prove successful as long as general fairness standards and uniform treatment of all groundwater owners are required. The State must have a way to stop regulatory discrimination and abuse.
- ★ Provide specific authorization for local governments to contract with private entities for developing water sources, transporting, and distributing water.
- ★ Examine the feasibility of developing a common carrier system to convey and transport water—regulating the conveyance system but allowing competing carriers within the piping network.

RESOURCES

- *Solving The Texas Water Puzzle: Market-Based Allocation Of Water* by Ronald Kaiser, Texas Public Policy Foundation (Mar. 2005) <http://www.texaspolicy.com/pdf/2005-03-water.pdf>.
- *A Free Market Solution To Groundwater Allocation In Texas: A Critical Assessment Of The House Natural Resources Committee Interim Report On Groundwater* by Clay J. Landry, Texas Public Policy Foundation (Dec. 2000) <http://www.texaspolicy.com/pdf/2000-12-01-enviro-water.pdf>.



Legislators' Guide to the Issues

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THE ISSUE

The opportunity to improve the benefits of government programs is offered by limited revenues, competing budget priorities, and revenue deficits. Using the principle of public benefit, state policymakers can make agencies and programs more efficient and effective by focusing on outcomes. Public benefit requires policymakers to guide decisions with the following questions.

- ★ How much money is available to be spent on government activities?
- ★ How should government functions take priority in the budget?
- ★ What is the goal of each government activity and what programs are most effective at achieving these goals?
- ★ How do tax and spending policies improve economic competitiveness?
- ★ How does the state budget reduce deficits and increase surpluses?

Competition is an essential tool for increasing the public benefit of government activities. The cost and quality of government services can be improved by introducing market forces, such as competition and economic incentives, into agency activities.

The most effective way of making government more responsive and responsible to the public is through comprehensive, whole-cloth reform. Partial, incremental, and gradual reforms have shown small success in changing the way government operates. Public school reforms furnish an example of the failure of incremental reform, while the success of school choice provides evidence that comprehensive, market-based reform maximizes public good.

New Zealand offers a model for governing according to the public benefit principle. In 1984, New Zealand was considered one of the most socialistic of nations. Government took 44 percent of the Gross Domestic Product and the budget deficit represented 15 percent. A new majority in parliament took control and initiated comprehensive, immediate, systemic reform. Parliament halted deficit spending, cut taxes, and reduced government services while improving public programs and increasing public satisfaction with essential services.

THE FACTS

- ★ New Zealand fully eliminated its budget deficit within six years and produced annual budget surpluses within nine years.
- ★ When New Zealand cut income taxes by 50 percent, revenue rose 20 percent in the first year.
- ★ When Turkey cut taxation by 40 percent, revenues rose 27 percent.



- ★ By introducing competition to road construction and maintenance, New Zealand cut costs by 40 percent and improved the quality of roads.
- ★ By allowing agencies to keep a percentage of annual efficiency gains, New Zealand achieved as much as 11 to 15 percent productivity gains by each government agency.
- ★ After school choice was established in New Zealand, more cents on the education dollar went to the classroom, more money was available to build schools and raise teacher salaries, and the achievement gap between public and private schools disappeared.
- ★ When legislators focus on public benefit, government services improve and costs decline.

RECOMMENDATIONS

- ★ Apply the principle of public benefit to all policy decisions.
- ★ Conduct ongoing budget analyses of spending and results.
- ★ Eliminate government activities except required activities or activities expressly required to achieve statutory charges.
- ★ Eliminate government activities that are ineffective or inefficient.
- ★ Fund only essential activities that produce direct public benefits.
- ★ Encourage private capital investment.
- ★ Do not increase taxes.
- ★ Introduce competition in all functions of government.

RESOURCES

- *Converting Challenges To Opportunities* by Maurice McTigue, Texas Public Policy Foundation (Feb. 2003) <http://www.texaspolicy.com/pdf/2003-02-03-mctigue.pdf>.

THE ISSUE

State and local governments replicate many commercial services that are available to Texans today. Government production of commercial goods and services pre-empts competition in the private sector, depresses economic growth, raises the cost of services, and lowers average family income.

Governments are directed to provide certain essential services that are deemed public good and cannot be commercially purchased—such as police protection and welfare. However, state law does not require that governments or government agencies be responsible for producing these services themselves.

Many states are increasing use of competitive contracting because the private sector can provide services more efficiently and effectively—finding that the private sector is capable of providing most government functions. Some states are divesting themselves of commercial operations, recognizing the financial penalties of state ownership on taxpayers.

In Texas, state and local governments are contracting out some administrative and support services today, but competitive contracting represents a small portion of government activity. Governments still command a sizeable segment of the commercial consumer market in Texas and compete with private enterprise at a significant advantage—bolstered by subsidies and tax breaks.

The cost of government competition challenges state policymakers to redefine the role of state and local government in Texas. What is the business of government? Should government own businesses? Should government produce consumer goods and services? Is government responsible for maximizing the economic good of its citizens? Is the primary job of government deciding policy or providing services?

THE FACTS

- ★ State government operates hospitals, correctional institutions, and universities; it runs licensing bureaus and maintains roadways.
- ★ Local governments operate airports, utilities, transit lines, radio stations, emergency services, and convention centers; they pick up garbage and run animal shelters.
- ★ Government businesses get subsidies and tax breaks—putting private enterprise at a significant financial disadvantage.
- ★ Texas governments earn more than \$11 billion annually selling consumer services that duplicate services that can be purchased from the private sector.
- ★ Texas governments spend more than \$8 billion annually operating support services for which there are well-developed commercial markets.



- ★ Government competition accounts for nearly \$20 billion dollars in Texas—the equivalent of 3 percent of Gross State Product.
- ★ Taxpayers pay extra when government gets involved with business—government costs are higher and government prices are usually subsidized below cost.
- ★ Government involvement in commercial business depresses personal income—depressing economic development, job creation, and wages.

RECOMMENDATIONS

- ★ Prohibit state and local governments from establishing commercial activities that are conducted by the private sector.
- ★ Annually review all government commercial activities to determine the potential for and implications of privatization.
- ★ Subject commercial activities of government to the same taxes and regulations as levied on private sector commerce.
- ★ Create incentives for governments to increase competition in all activities—administration, support services, and direct services.
- ★ Establish a “Petition of Interest” process to allow private companies to notify government of interest in providing a government service and initiate a competitive bidding process.

RESOURCES

- *The Business of Government? Competition Between Texas Governments & the Private Sector* by Wendell Cox, Texas Public Policy Foundation (Sep. 2003) <http://www.texaspolicy.com/pdf/2003-09-24-govt-competition.pdf>.

Notes



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