TEXAS PUBLIC POLICY FOUNDATION
Testimony

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Center for Fiscal Policy

Time for a Conservative Texas Spending Limit

Testimony before the Senate Finance Committee in support of SB 9

by Vance Ginn, Ph.D.

Madame Chair Nelson and Members of the Committee:

My name is Dr. Vance Ginn, and I am an economist in the Center for Fiscal Policy at the Texas Public Policy Foundation, a 501(c)(3) non-profit, non-partisan free market think tank based here in Austin. Thank you for the opportunity to speak today in support of Senate Bill 9.

Although Texas has done better economically and fiscally than most states during much of the last two decades, the state's weak appropriations limit needs to be resolved for consistent restraint of excessive government spending so Texans can have more money in their pocket. The 2016-17 budget is up an estimated 11.8 percent above the pace of compounded population growth plus inflation since the 2004-05 budget. As a result, a Texas family of four pays $1,600 more on average in taxes this year than if the budget had increased each biennium by population growth plus inflation since then. With government spending ultimately being paid for by taxation, limiting spending growth is essential for a competitive economy to support prosperity. As examples of much room for improvement, the Mercatus Center ranks Texas 23rd in fiscal condition and the Fraser Institute ranks Texas 25th in taxes.

Fortunately, the 2016-17 budget and 2018-19 budget meet the needs of Texans while potentially keeping two consecutive state budgets below population growth plus inflation, a historic milestone. For the 2018-19 all funds appropriations to remain a conservative budget, supplemental appropriations in the 2017 special session and 2019 regular session must be below $2.79 billion.

Texas needs to keep past excessive budget cycles from repeating by passing a conservative spending limit that corrects the following current design flaws:

- **Limit covers less than half of the budget**. In Article VIII, Section 22(a) of the Texas Constitution, the only appropriations subject to the limit are those derived from "state tax revenues not dedicated by this constitution," which was about 45 percent of the 2016-17 total budget. By only capping less than half of the budget, legislators are left with perverse incentives to constitutionally dedicate funds thereby pushing them outside of the appropriations limit and excessively growing the budget.
- **Personal income is not a reliable indicator for the limit's growth rate**. The Texas Constitution requires that the limit be based on the growth in the state's economy, which is statutorily defined as projected growth in personal income. This measure is highly volatile and not reliable.
- **Growth rate limit relies on practically impossible projections**. Since several groups submit estimates of personal income growth to the Legislative Budget Board in November before a regular legislative session for the next two fiscal years, the projections are for about 33 months. The difficulty of accurately predicting this growth rate leads to large discrepancies between actual and projected growth rates that are never reconciled.
- **Legislators can exceed the limit with a simple majority vote in each chamber**.

With so many hindrances to budgetary prudence, Texas' appropriations limit fails to effectively limit growth in the state budget. The Foundation's recommended appropriations limit, which was adopted by the American Legislative Exchange Council as model legislation and outlined in SB 943 during the 2017 regular session includes:

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- **Limiting the total budget**. This would avoid perverse incentives and budget gimmicks.
- **Basing the limit's growth rate on the lowest of three metrics**. These metrics include the growth rate of the Census Bureau's measure of state population plus the Bureau of Labor Statistics' measure of inflation for the consumer price index for all items, the Bureau of Economic Analysis' measure of total state personal income, and the Bureau of Economic Analysis' measure of total gross state product.
- **Calculating growth rate with past data**. The growth rate limit would be calculated for the two fiscal years immediately preceding a regular legislative session when the budget is adopted.
- **Requiring a supermajority vote of two-thirds in each chamber to exceed the limit**.

Historically, population growth plus inflation has often been the lowest metric and relatively more stable over time than the other two metrics. However, we are mindful of the Great Inflation during the 1970s and do not find it appropriate to excessively burden taxpayers by growing government spending at that pace, which is why we suggest the lowest of the three metrics.

Population growth and inflation are two economic measures that account for most of the cost of funding public provisions to a changing population. Research finds that simply changing the appropriations limit to population growth and inflation will lead to tax relief and accelerated economic growth. The key is that a limit with these measures holds budget growth to no more than the means of taxpayers as more people pay taxes, and wages are often tied to price inflation. Adding these measures accounts for economies of scale whereby the average cost of providing many government provisions declines over time. Moreover, the appropriations limit growth rate's current measure of personal income can be represented as population growth plus inflation plus productivity. However, a more productive private sector signals that the marginal return per dollar would be greater in the private sector, meaning that more dollars should remain there instead of being taxed to pay for higher government spending. If government productivity is considered in this calculation, it would be practically impossible to measure and would likely be zero over time, thereby leaving population growth plus inflation.

Fortunately, SB 9 would substantially strengthen the appropriations limit by moving closer to the Foundation's recommended version by:

- **Limiting consolidated general revenue**. This includes both general revenue and general revenue-dedicated funds, which is roughly 55 percent of the total budget. If the limit covers more of the budget, there will be fewer opportunities for perverse incentives and budget gimmicks.
- **Base the limit's growth rate on population growth times inflation**. Although this metric is not used by any other state and would not account for economies of scale, it is more stable and relevant to the means of taxpayers than personal income. This growth rate limit difference with our recommended population growth plus inflation would be small each biennium but would grow faster by compounding.
- **Growth rate limit relies on average growth rate of the previous biennium and the upcoming biennium**. The calculation would be a substantial improvement to the current calculation.
- **Legislators must have a supermajority vote of three-fifths in each chamber to exceed the limit**.

The current appropriations limit has contributed to excessive government spending and taxation. Although SB 9 could be strengthened, we believe that it will help limit growth in Texas' government, allowing Texans more opportunities to improve their well-being. Thank you for your time, and I look forward to your questions.

Vance Ginn, Ph.D., is an economist in the Center for Fiscal Policy at the Texas Public Policy Foundation. He is an expert on Texas' state budget, franchise tax, tax and expenditure limit, and other fiscal issues. Before joining the Foundation in September 2013, Ginn taught at three universities and one community college in Texas. He has published peer-reviewed articles in academic journals, as well as commentaries in major media outlets across Texas and the nation.