TEXAS PUBLIC POLICY FOUNDATION
Testimony

March 30, 2021

SB 1336
Strengthening Texas's Spending Limit

Testimony in Support of SB 1336
Before the Texas Senate Committee on Finance

by Vance Ginn, PhD, Chief Economist

Chair Nelson and Members of the Committee:

My name is Vance Ginn, and I am chief economist at the Texas Public Policy Foundation. Thank you for the opportunity to testify in support of SB 1336, which would provide key improvements to the state's weak spending limit, protecting taxpayers by keeping spending growth within their ability to pay for it.

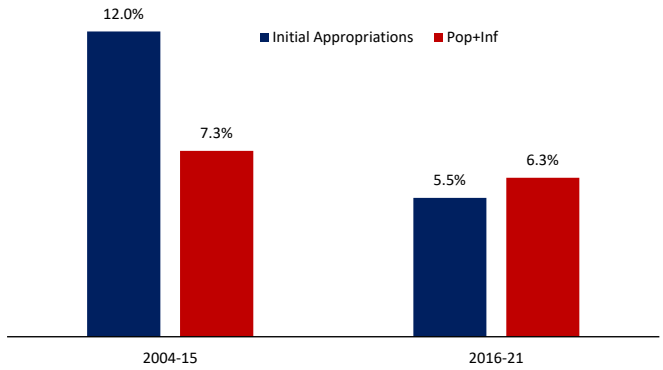
Texas's Spending Limit Weaknesses

Texas has done better economically and fiscally than most states during much of the last two decades. This success is a result of a limited government philosophy encapsulated in the Texas Model. However, weaknesses within the state's spending limit threaten this success as excessive government spending over time has necessitated higher taxes and debt. Weaknesses include (a) covering less than half of the budget, (b) using a volatile metric and unreliable indicator of the average taxpayer's burden with personal income, (c) relying on practically impossible growth projections, and (d) having only a simple majority vote in each chamber to exceed the limit.

Recommendations for a Spending Limit to Reflect Taxpayers' Burden

While there are many possible ways to limit a government's budget, an effective limit will reflect the average taxpayer's ability to pay for government spending, not an appropriator's cost of providing provisions. The latter results in excess spending because the government's provisions often dominate those markets, and so the cost is likely inflated, meaning spending, and therefore taxes given our balanced budget amendment, would be higher than necessary. To reflect the average taxpayer's tax burden, we recommend that a spending limit, which is similar to ALEC's model legislation and in a forthcoming committee substitute for HB 594 this session, include—

Figure 1
Texas's Budget Growth Has Slowed Since Creation of the CTB in 2015



Note. Data from *Fiscal Size-Up*, Legislative Budget Board (https://www.lbb.state.tx.us/FSU.aspx) and authors' calculations of average biennial growth.

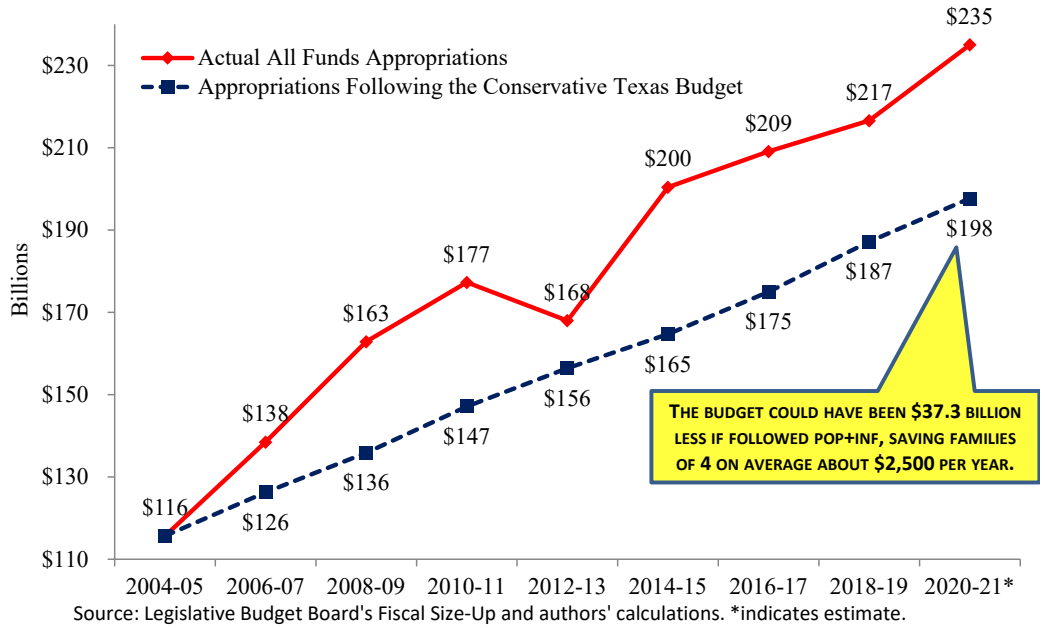
- Limiting growth of all-funds appropriations, helping avoid moving state funds outside the narrower limit or not counting federal funds;
- Basing the limit on the growth rate of the Census Bureau's measure of state population plus the Bureau of Labor Statistics' measure of inflation for the consumer price index for all items (i.e., pop+inf) over the 2 fiscal years immediately preceding a regular legislative session; and
- Requiring a supermajority vote of two thirds in each chamber to exceed the limit.

This methodology has been the crux of the Foundation's Conservative Texas Budget (CTB) since its inception in 2015, which essentially freezes inflation-adjusted state government appropriations per capita. **Figure 1** shows how the average biennial growth rate of the last three completed budgets has

continued

Figure 2

Texas's State Budget Exceeds Population Growth Plus Inflation Since 2004-05



Note. Data from Fiscal Size-Up, Legislative Budget Board (https://www.lbb.state.tx.us/FSU.aspx) and authors' calculations.

slowed since 2015 to less than half of the rate of the prior five budgets and has been almost a full percentage point below pop+inf.

The current CTB is a maximum threshold of $246.8 billion based on pop+inf of 5% for the 2022-23 budget—the base budgets currently fall below this threshold—excluding $6 billion toward maintaining last session's property tax relief and one-time declared disaster recovery funds. The Legislative Budget Board has used population times inflation (i.e., pop*inf) as the spending limit metric in the three budgets including the current one without a change in law. Given the Texas Legislature has been appropriating taxpayer dollars at a growth rate less than population and inflation and has been imposing it upon itself without a change in statute, now is the time to put it into law, especially given the long-term problem of excessive spending noted in **Figure 2**.

Because of excessive appropriations before 2015 and the effect of compounding, the 2020-21 budget is 18.9% higher than if each budget since the 2004-05 budget had followed pop+inf. Therefore, every state budget should grow by less than the CTB—and ideally by much less, if even at all—in order to correct the past spending excesses and associated elevated tax burden on Texans.

Reasons for this spending limit approach

- Capping the total budget provides legislators flexibility to appropriately fund spending categories instead of limiting each category's budget to the population served and costs of representative goods and services, which are primarily government-driven and difficult to calculate.
- Pop+inf is a metric influencing the economy that reflects the average taxpayer's ability to pay for spending as more Texans pay taxes, and wages are tied to inflation.
- The state's current limit of personal income growth can be represented as the functional form of the growth rates in pop+inf+productivity. From the taxpayer's perspective, productivity growth in the private sector suggests an increase in government spending, but this indicates the marginal return per dollar is greater in the private sector, so more dollars should remain there. Conversely, a less productive private sector results in less spending. Either scenario indicates this variable is zero or negative, so removing this variable leaves pop+inf.

- Pop*inf in its functional form of growth rates is (1+pop)*(1+inf), which results in 1+pop+inf+pop*inf, so the difference with population plus inflation is the last term. But given that the average taxpayer's ability to pay is not directly related to the multiple of population growth and inflation, then the result is pop+inf.
- Meanwhile, the growth rate differences are small, with the compounded average annual growth rate from 2000 to 2019 being 3.63% for pop+inf and 3.67% for (1+pop)*(1+inf). However, this small difference amounts to a larger increase in spending and therefore taxes over time when considering compounding, as pop+inf has increased by 104% and (1+pop)*(1+inf) has increased by 106% over those 20 years, representing what would have been almost $700 million in higher taxes. Given the unprecedented levels of recent federal spending and the equally unprecedented levels of liquidity created by the Federal Reserve, even the small percentage difference between pop+inf and pop*inf will amount to a large disparity in state spending as inflation rates increase in the near future.
- Pop+inf has grown the least compared with pop*inf and personal income growth (i.e., compounded average annual growth rate was 4.86% since 2000) in 15 of the last 20 years, with personal income growth being the lowest in those other 5 years during economic downturns.
- Population plus inflation has been less volatile over time with a standard deviation of 0.014 compared with 0.015 for population times inflation and 0.033 for personal income since 2000, which helps improve expectations by taxpayers to fund the state budget and by legislators to meet needs.
- Research finds that a limit on appropriations like the one outlined in the CTB could lead to tax relief and accelerated economic growth.
- Therefore, population plus inflation is a reasonable metric for the state to use as a spending limit.

Details of SB 1336

This legislation would strengthen the spending limit by

- Limiting growth of consolidated general revenue appropriations, which exceeds half of the budget;
- Basing the growth rate on population times inflation, which is not ideal as it is not used by any other state and would compound faster than adding them while not accounting for economies of scale, but it is more stable and relevant to the average taxpayer's means than personal income;
- Calculating the growth rate by averaging the rates of the previous biennium and the upcoming biennium, substantially improving the current flawed almost three-year projections; and
- Requiring a supermajority vote of three fifths in each chamber to exceed the limit.

Recommended improvements

- Broaden the base to all state funds if not all funds, given that's the footprint of government;
- Clarify the exclusion of "disaster recovery" costs to "an appropriation to pay one-time costs associated with recovery of a declared disaster";

- Update the metric used to population plus inflation instead of population times inflation to better match the average taxpayer's ability to pay for government;
- Use just the last 2 fiscal years for the growth rate calculation to exclusively use actual data instead of forecasts; and
- Increase the supermajority vote to exceed the limit to two thirds for an increased restriction.

Considering that high taxes and debt are always and everywhere a government spending problem, the state's current weak spending limit has contributed to excessive government spending that has resulted in less economic prosperity for Texans. Fortunately, the Legislature has taken strides to improve the budget picture during the last three budgets by better following the Conservative Texas Budget, which is why it is crucial to put this responsible, conservative fiscal management in statute. In fact, I am working with other states, such as Georgia, Iowa, Alaska, and Montana, to do the same with their own Conservative Texas Budget approach, so Texas must improve its budgeting to remain competitive.

While SB 1336 could be strengthened, we strongly support it as a valuable path to effectively limiting the footprint of government, allowing Texans more opportunities to flourish. Thank you for your time and the work you do, and I look forward to seeing this bill become law.

ABOUT THE AUTHOR

Vance Ginn, PhD

Dr. Ginn is chief economist at the Texas Public Policy Foundation. He is the former associate director of economic policy for the Office of Management and Budget at the Executive Office of the President, a former college lecturer, and an expert on economic and fiscal issues with research that seeks opportunities to let people prosper in Texas, D.C., and beyond. He earned his doctorate in economics at Texas Tech University.

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