INSTITUTE BRIEF

Volume 17, Number 31 November 2010

We must Control Government Spending

By Deborah D. Thornton

Tax and Expenditure Limits (TELs) are used to control growth in government spending. Constitutional limits are generally stronger and more effective, because Legislative statutory limits are easier to override. Limits are put on the amount of revenue that can be raised (taxes), the amount of money that can be spent (budget), or the amount that can be authorized (appropriated) by the Legislature, or a combination of all three.

Increased government growth and spending have resulted in new movements across the U.S. to require voter approval before implementing tax increases, such as a Taxpayer Bill of Rights (TABOR). Other popular options are Legislative supermajority requirements, known as Tax Limitation Amendments (TLAs), requirements for "waiting periods," and Internet posting of legislation before final passage.[1]

According to the Center on Budget and Policy Priorities (CBPP), the current recession has resulted in the "steepest decline in state tax receipts on record."[2] As many as 46 state budgets are facing shortfalls in Fiscal Year (FY) 2011, the current fiscal year. Revenue shortfalls will total at least $112 billion and may reach $180 billion, with additional shortages in FY 2012. Governors and Legislators must address the problem of reduced tax collections by either cutting spending or raising taxes, or, in this era of government bailouts, accepting handouts from the Federal government.[3]

Future state budget problems are even more likely. Historically, state tax collections have lagged behind the general economic recovery, typically by several years. This was demonstrated during the minor recessions of the 1980s, 1990s, and early 2000s.[4] This recession has broadly affected almost all areas of the economy, from employment, to housing, to consumer sales, to household wealth. Because of pervasive weaknesses in all these areas, sales tax, personal income tax, and property tax collections are down. As a result, state governments are having significant trouble meeting their commitments.

State budget cuts are actually more severe later in the financial cycle because states use their reserves or rainy-day funds to initially backfill the budget — postponing cuts as long as possible. Much of the potential FY 2010 budget shortfalls were also backfilled by federal stimulus funds.

Philosophically, if a government's (or an individual's) income is unexpectedly decreased, then expenditures should be correspondingly decreased. Because of the balanced budget requirements of state governments, this was done, to some extent, for both FY 2009 and FY 2010. In Iowa, the Governor and Legislature are required by law to use the December Revenue Estimating Conference (REC) Report of expected tax revenues to budget for the next fiscal year. Thus, the December 2008 REC report was used for the FY 2009 budget and the December 2009 report for FY 2010 — the fiscal year that ended June 30.

For FY 2009, which ran from July 2008 to June 2009, the REC began generating preliminary estimates in October 2007. This initial number was $6.72 billion. It was increased in April 2008 to $6.85 billion, and then decreased by a little less than one billion dollars by March of 2009

A Publication of: **Public Interest Institute *at* Iowa Wesleyan College**
600 North Jackson Street, Mt. Pleasant, Iowa 52641-1328

E-Mail: public.interest.institute@limitedgovernment.org
Website: www.limitedgovernment.org Phone: 319-385-3462 Fax: 319-385-3799

— three-fourths of the way through the fiscal year — to $5.97 billion. The final net expenditures, following reconciliation and all tax refunds, were $5.75 billion. This included an across-the-board budget cut of 1.5 percent and transfer of $45.3 million from the Emergency Fund.[5] The overall decrease from the high estimate to the actual net spending was just over $1.1 billion, or 16 percent.

The FY 2010 REC budget estimates were also optimistic, beginning with a high of $6.16 billion in October 2008, and then falling to $5.4 billion in March 2009. As tax collections fell over the intervening months, the REC again revised its estimate, with the biggest drop of over $400 million, or 8.4 percent, occurring between the March and October 2009 reports. Significant changes were required to meet the legal requirement of a balanced budget.[6] Accordingly, last October Governor Chet Culver (Democrat) ordered an across-the-board cut of 10 percent, less than a month after touting the FY 2009 balanced budget. In addition, another $1.9 billion in federal stimulus money was allocated to Iowa.[7]

In both years, in order to end up with a legally balanced budget, a combination of spending cuts, federal money, and transfers from reserve funds were required. For the current fiscal year, 2011, the March 2010 REC estimate of available tax revenue is $5.44 billion. This number is actually an increase of $33 million from the December 2009 estimate. March statements by the REC indicate that it believes the “extended economic decline has leveled out” and that the “economy should begin ticking up.” You’ve gotta love its optimism, but based upon the retail sales, personal income, housing, and employment numbers of the last six months, it may have to retract those statements.

From 2000 to 2009, the Iowa Gross Domestic Product (GDP) grew 60 percent, but total state and local government expenditures grew over 65 percent, from $17 billion to $28.4 billion.[8] This is almost 20 percent of GDP. Iowa’s population has only grown by 81,000 people, a 2.4 percent increase. As a result, the expenditures per capita have increased dramatically, to over $9,400 per person.

As government takes more and more from our workers and families, what funds will be used to support future private sector growth? To educate our children? To save for our retirement? We need stronger tax and expenditure limits on both state and local governments.

Tax and Expenditure Limits (TELS) Helping to Control Government Spending, Policy Study #10-4, August 2010, is available at www.limitedgovernment.org/publications/pubs/studies.html

(Endnotes)
[1] “Waiting Periods for Fiscal Bills,” Center for Fiscal Accountability, <http://www.fiscalaccountability.org/budget-timeouts> (July 21, 2010).
[2] Elizabeth McNichol and Nicholas Johnson, “Recession Continues to Batter State Budgets; State Responses Could Slow Recovery,” Center on Budget and Policy Priorities, p. 1, May 27, 2010, <http://www.cbpp.org/cms/?fa=view&id=711> (July 6, 2010).
[3] McNichol, p. 2.
[4] McNichol, Figure 2, “How Bad Will It Get?” p. 2.
[5] “Governor Culver: FY2009 Budget Balanced,” Office of the Governor, news release, September 25, 2009, <http://www.governor.iowa.gov/index.php/press_releases/single/118/> (July 19, 2010).
[6] “Preliminary Departmental Plans Released on State Budget Cuts,” Office of the Governor, October 21, 2009, <www.governor.iowa.gov/index.php/press_releasea/single/148/> (July 19, 2010).
[7] “Stimulus Spending by State,” *The Wall Street Journal*, August 6, 2009, <http://online.wsj.com/public/resources/documents/info-STIMULUS0903.html> (July 9, 2010).
[8] Sunshine Review, Establishing the Standard for Government Transparency, <http://sunshinereview.org/index.php/Main_Page> (July 7, 2010).

Deborah D. Thornton is a Research Analyst with Public Interest Institute, Mount Pleasant, Iowa.