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Policy Report

# Senate Resolution 20

## What a Tax and Expenditure Limitation Would Mean for Georgia

by Alan Essig, Executive Director

## Overview

Senate Resolution 20 is a proposal designed to cripple Georgia's ability to invest in state services such as schools, health care, transportation and public safety, and would place Georgia's hard earned AAA bond rating in danger.

The legislation would arbitrarily limit how much Georgia can raise and spend each year. It would thwart majority rule by requiring a two-thirds vote of the legislature to pass any additional investments that are needed, handing power over to a small, determined minority. Since the rule would be added to Georgia's Constitution, it would take away the legislature's and the governor's flexibility in responding to crises. By tying crucial policy decisions to an unyielding formula rather than the judgment of the public and its representatives it would bring lasting harm to the state's economy and the well-being of Georgia families.

Bills such as this – known around the country as the Taxpayer Bill of Rights, or TABOR – are based on a false claim that state taxes and spending are "out-of-control." Georgia is already a fiscally conservative state and one of the lowest-taxing, lowest-spending. It ranks 45th in state revenue as a share of personal income, 49th in state and local spending per capita, and 41st in the amount of taxes collected from business. The caps being proposed are a solution in search of a problem.

This is the opposite of what Georgia needs. The state's growing and aging population and the need to compete in the diverse 21st century economy require investments in the foundations of future growth, like education and infrastructure, rather than continued cuts to such vital services. To be an attractive place to live, work, and raise a family we cannot afford to ignore these needs. Senate Resolution 20 would put Georgia's economy at risk at this critical time of recovery.

## Background

Senate Resolution (SR) 20 is a constitutional amendment that would limit spending growth by setting a cap on the amount of revenue the state can budget each year. Under SR 20, the cap on spending growth is population growth plus government inflation growth (i.e. the rising cost of inputs to the services provided by state and local governments). For example, assume last year's spending was $18 billion and the most recent available estimate of population growth is 2 percent and government inflation growth is 3 percent. Then the current year spending cannot exceed $18.9 billion (5 percent growth over the prior year).

Any "excess" revenues above the spending limit would be used for the following items in order:

1. K-12 student enrollment increases,
2. the Revenue Shortfall Reserve, and
3. a cut to the income tax rate by one quarter of 1 percent.

SR 20 allows for an override to the spending formula if the reserves are empty and both houses of the General Assembly adopt a joint resolution by a two-thirds vote to spend beyond the cap.

SR 20 is a modified version of Colorado's tax and expenditure limitation, commonly known as Taxpayers' Bill of Rights or TABOR. Colorado adopted TABOR in 1992 as a way to limit state spending, with the following results, among others:[1]

- Colorado dropped from 35th in 1992 to 49th in 2001 for K-12 funding as a percentage of income.
- Colorado dropped from 35th in 1992 to 48th in 2001 for higher education funding as a share of income.
- The percentage of children lacking health insurance doubled in Colorado, even as the national percentage of uninsured children fell. Colorado fell from 24th to 50th in the percentage of children receiving their full vaccinations.

In 2005 Colorado residents voted to suspend TABOR for five years to stop the deterioration of state services.

As SR 20 is being debated in Georgia, it is important to look at the conceptual flaws of tax and expenditure limitations, spending trends in Georgia, and the possible effects the proposal would have on basic services such as education, health, and public safety.

## Flaws with "Population plus Inflation"

There are several key problems with using "population plus inflation" as a limitation on state spending. For the inflation measure, the traditional TABOR model relies on the Consumer Price Index (CPI), which captures the increasing costs of goods and services for consumers. Since government purchasing is very different from household purchasing, CPI inflation growth is an inadequate tool to use for government spending. SR 20 attempts to correct this problem by replacing the CPI inflation measure with a "state government inflation" measure from the Bureau of Economic Analysis (BEA). While this step improves the bill somewhat, there still exist flaws in the formula. For example, the BEA does not include Medicaid in its state government inflation measure and, thus, does not capture a significant portion of state spending that continues to increase in cost.

**Population and Inflation Estimates Continually Revised**

It is important to note that a significant drawback to the population and inflation measure is the availability of data. For the current budgeting session for the FY 2013 budget, legislators would have to rely on 2010 to 2011 population change since that is the most recent available data. In addition, these data estimates from the Census and BEA are continuously updated and revised. For example, the most current BEA government inflation index was last revised in July 2011 and will be again in July 2012 and 2013. SR 20 would tie state spending to outdated information and fluctuating estimates.

For the population measure, the specific populations that state governments serve tend to grow more rapidly than the overall population growth used in the formula. In Georgia, the state population increased by 31 percent between FY 1996 and FY 2009.[2] Over that same time period, the prison population increased by 57 percent, the number of students served by our post-secondary education systems increased by 78 percent, and the number of Medicaid and PeachCare recipients increased by 70 percent.[3] A rigid population and government inflation growth formula can put fast-growing state programs at risk as their specific populations and costs outpace regular population and inflation. Other state programs, not just those with cost pressures exceeding the population plus inflation formula, also are threatened since growth in one area can force cuts in another spending area.

**Table 1 Growth in Populations Served by State Government Often Outpaces Overall Population Growth**

| | Population Growth 1996-2011 |
|---|---|
| Total Population | 31% |
| State Prison Population | 57% |
| Medicaid & PeachCare Recipients | 70% |
| Post-secondary Student Enrollment | 78% |

Sources: U.S. Census Bureau, Georgia Department of Corrections, Georgia Department of Community Health, Technical College System of Georgia, University System of Georgia.

The increases in certain populations are often due to specific policy decisions by the legislature. The significant increase in the prison population was due in large part to stricter sentencing policies put in place in 1994 by Senate Bill 441, commonly referred to as “Two Strikes and You’re Out”. Medicaid has grown at a faster rate than the overall population; in addition, Georgia created the PeachCare program to insure low-income children, thus driving the population for health services even greater. An SR 20 spending cap would have made it difficult to fund those new priorities, or other new priorities like teacher pay raises that go beyond the normal growth in population or cost. These policy decisions deserve debate; however, changes to such policies should be the result of thorough analysis and thoughtful policymaking rather than a hurried reaction to an unrelated cap on spending.

In addition, the spending cap would make it difficult to fund new or expanded federal mandates, such as the Department of Justice settlement for services for Georgians with developmental disabilities and mental illness. According to SR 20, the cap can only be exceeded when the reserves are depleted and the General Assembly adopts a joint resolution by a two-thirds vote to override the limit. SR 20 strips the governor and General Assembly of its ability to fund new priorities or even the growth of certain services above the cap without harming other services.

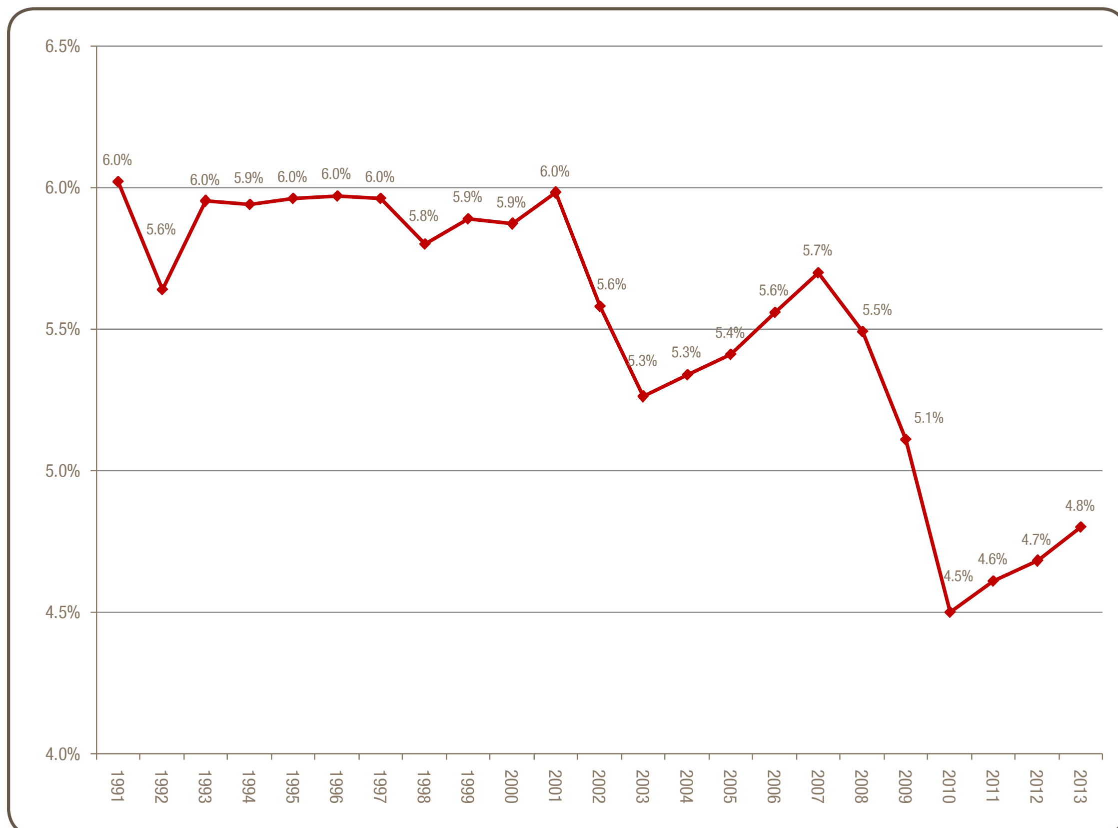
## Does Georgia Have a Spending Problem?

Those who propose tax and expenditure limitations use the rationale that the state budget is “out-of-control.” But does Georgia have a spending problem?

Georgia currently ranks 49th in state and local expenditures per capita among the states.[4] Rather than increasing over the past 25 years, state revenues as a percentage of income have decreased significantly. That decline is not just a result of the most recent recession in which revenues dropped by 20 percent. Even the growth years of 2005 through 2007 included state revenues below the historic norm when measured as a percentage of income. As the Special Council on Tax Reform and Fairness for Georgians noted in their final report:

> **“Overall, Georgia’s taxes are low, have not increased over the past 30 years as measured by taxes as a share of personal income, and are competitive.”[5]**

**Figure 1 State Total Revenues as a Percentage of Personal Income Have Declined over the Last Decade**




Author’s calculations are based on data from the Bureau of Economic Analysis and the governor’s budget books.

## What Would SR 20 Mean for Georgia?

SR 20's spending limit would necessarily impact some of our most vital public services because that's where the money is. The majority of funds are dedicated to a handful of essential services, such as education, health care, and public safety. Ninety-five percent of the proposed FY 2012 budget will be expended in six areas: education, health care, public safety, human services, debt service, and transportation. All other state government comprises only 5 percent of state spending.

Although the potential impact of SR 20 on specific programs such as education and health care is unknown, it is apparent that state revenues will need to grow at a faster pace than recent population plus government inflation figures in order to climb out of the current budget gap caused by the recession. In the last two years, population and government inflation combined have been between 3 percent and 3.8 percent. Georgia will need to grow at a pace of at least 6 percent to fund the normal enrollment growth of services, minimal pay raises for teachers and state employees, typical bond packages, and new funding for the Department of Justice settlement. Revenues would need to grow well beyond 6 percent to begin restoring the almost $2 billion in cuts to services made in recent years.

**Table 2 FY 2013 State Funds Budget Breakdown**

| | |
|---|---|
| Education | 51.8% |
| Health | 20.5% |
| Public Safety | 9.4% |
| Debt Service | 6.2% |
| Transportation | 4.3% |
| Human Services | 2.7% |
| All Other Government | 5.1% |

**Table 3 Population and Inflation Growth in Recent Years Trails What Georgia Will Need to Regain the Ground Lost in the Recession**

| | Population Growth | State & Local Government Inflation |
|---|---|---|
| 2008 | 1.7 | 5.6 |
| 2009 | 1.2 | -0.3 |
| 2010 | 1.0 | 2.1 |
| 2011 | 1.1 | 2.7 |

Source: Bureau of Economic Analysis; National Income & Product Account Tables

SR 20 could also negatively affect Georgia's bond rating. In 2002 Colorado's bond rating was downgraded, with TABOR given as a specific factor in the decision.[6] In 2011 Nevada's credit rating was downgraded after the passage of a super majority restriction on raising taxes.[7] Standards and Poor's U.S. Ratings Methodology cites restrictive budget and revenue requirements as negative aspects in credit ratings.[8]

## Conclusion

Supporters of the caps acknowledge the flaws of the TABOR model but claim that modifying Georgia's proposal will fix earlier mistakes. However, the policy's fundamental problems and impact would be the same. As in Colorado – the first state to adopt TABOR, and which with bipartisan support suspended its key provisions because of the harm done to the state – investments by the state would be constrained by an unrealistic formula that does not reflect changing demographics or the cost of serving low- and middle-income families, children, the elderly, and people with disabilities.

In short, this legislation would be disastrous, not allowing Georgia to meet the basic needs of a growing 21st century state. Rather than strengthening Georgia's ability to invest in critical areas that grow the economy and create jobs, the caps would lock state lawmakers into a never-ending cycle of cuts that would crowd classrooms, close libraries and parks, and block the path to the middle class for thousands of hard-working men and women. Instead, Georgia must take sensible and balanced steps to ensure a more prosperous state. Our success depends on our ability to make investments in good schools, a quality health care system, world-class infrastructure, and a skilled workforce.

## Endnotes

[1]Lav, Iris and Erica Williams, "A Formula for Decline: Lessons from Colorado for States Considering TABOR," Center on Budget and Policy Priorities, March 15, 2010.

[2]U.S. Census Bureau, Population Estimates.

[3]Population data from the websites of the Georgia Department of Corrections, University System of Georgia, Technical College System of Georgia, and Georgia Department of Community Health.

[4]Tax Policy Center calculations from U.S. Census Bureau data

[5]2010 Special Council on Tax Reform and Fairness for Georgians, "Recommendations," January 7, 2011

[6]Standard & Poor's, Colorado; Appropriation, Ratings Direct, June 28, 2002

[7]Moody's Investor Services, Global Credit Research Press Release, "Moody's Downgrades State of Nevada's General Obligation Bonds to Aa2 from Aa1," March 24, 2011.

[8]Standard & Poor's, U.S. State Ratings Methodology, Global Credit Portal, Ratings Direct, January 3, 2011

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