COMMITTEE REPORT

SENATE

FURTHER: None

5/5/81

Date: 6/10/81

Mr. President:

The Committee on FINANCE has had SJR 4

proposing an amendment to the Constitution of the State of Alaska relating to limitations on appropriations of state money

under consideration and (a majority of the committee) (the committee) reports it back with the following recommendations:

[ ] do pass [ ] do not pass

[ ] do pass with attached amendments(s)

[X] replace with CS for SJR 4 (fin) [X] same title [ ] new title

and recommends do pass

[ ] AND attaches a "Letter of Intent" [ ] New Fiscal Note

[ ] reports it back without recommendation

[ ] referred to the ______ Committee

MEMBERS SIGNING DO PASS

MEMBERS HAVING OTHER RECOMMENDATIONS:

CHAIRMAN

S 60 (Rev. 12/78)

6/10/81

CS SJR 4 (finance)

Proposing an amendment to the Constitution of the State of Alaska relating to limitations on appropriations of state money.

BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* Section 1. Article IX of the Constitution of the State of Alaska is amended by adding new sections to read:

SECTION 16. APPROPRIATION LIMITATIONS. The amount of State money the governor may request or the legislature may appropriate during a fiscal year shall not exceed the amount appropriated in the preceding fiscal year by more than the increase in the federal consumer price index for the State for the calendar year preceding the governor's submission of the budget under section 12 of this article plus or minus a percentage equal to the cumulative average yearly growth or loss in the State's population as shown by the last two federal censuses or renumerations. Money appropriated under any exception prescribed by section 17 of this article shall not be included in the base for determining the allowable increase from year to year. For purposes of this section, the amount of $2.7 billion shall be used as the amount of appropriations in fiscal year 1982.

SECTION 17. EXEMPTIONS FROM APPROPRIATION LIMITATIONS. The limitations on increases in appropriations do not apply to money received from another in trust for a specific purpose; to appropriations of money to be deposited in the permanent fund; money appropriated to pay principal and interest on general obligation bonds; money appropriated

to capitalize loan funds, but only if the money to subsidize these loans at below market interest rates is appropriated separately under the limitations; money appropriated by the affirmative vote of two-thirds of the membership of each house, whether of bond proceeds or otherwise, to construct capital improvements, not to exceed $1,500 per capita; or money appropriated by a vote of two-thirds of the membership of each house and approved by the governor to meet disasters of natural or human origin which are declared by the governor.

* Sec. 2. The amendment proposed by this resolution shall be placed before the voters of the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska, and the election laws of the state.

BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA

Section 1. Article IX of the Constitution of the State of Alaska is amended by adding a new section to read:

Section 16. APPROPRIATION LIMITATIONS. The amount of State money the Governor may request or the Legislature may appropriate during a fiscal year shall not exceed the amount ________ billion for the base fiscal year of 1982 by more than the cumulative increase in the national consumer price index for the calendar years preceding the Governor's submission of the budget under Section 12 of this Article, plus or minus a percentage equal to the cumulative average yearly growth or loss in the State's population as shown by the last two federal consensus or renumerations. Money appropriated under any exception prescribed in Section 17 shall not be included in the base for determining the allowable increase from year to year.

Section 17. EXCEPTION FROM APPROPRIATION LIMITATIONS. The limitation on increases in appropriation do not apply to appropriations to the Permanent Fund or to other funds which produce income at market rates. Income from appropriations excepted from the appropriation limitation shall be returned to the General Fund and subject to the appropriation limitation. The Legislature may, by affirmative vote of threequarters of the membership of each house, or by a two-thirds vote of the membership of each house on appropriation requests from the Governor, make appropriations in excess of this limit by enactment of appropriation bills limited to a single item of appropriation for a single purpose, but these appropriations shall not be included in calculating the limit for the next fiscal year.

Section 2: The amendment proposed by this resolution shall be placed before the voters of the State at the next General Election in conformity with ART. XIII, Sec. 1, Constitution of the State of Alaska, and the election laws of the State.

EXPLANATION

The working philosophy behind this amendment is an aim for consistency with the bulk of the Alaska Constitution. The Alaska Constitution contains simple and explicit statements of intent and design. To lose this simplicity of approach is to also lose ease of understanding by readers. Further, it was felt that keeping a spendng limitation as simple as possible would ease voter understanding of the issue when the issue comes on the ballot.

Also in keeping with the idea of mirroring the Constitution, this amendment attempts to reinforce and strengthen the existing system of checks and balances so that the addition of an amendment does not do damage to the political system. The philosophical approach used in this amendment is the desire to limit expenditures of State revenues.

BASE

The amendment calls for a number to be used instead of a fiscal year or other indication of the starting point. Specification of a number will, most likely, decrease ambiguity and lessen the likelihood of litigation. Further fiscal analysis is necessary to determine the proper number.

COVERAGE

The spending limitation will apply to any appropriation from the General Fund. This allows for the direct control of expenditures of all General Fund revenues. Language included in the amendment would also require that the return on any investment or trust funds established through State appropriations be contributed to the General Fund. This will ensure that the expenditure of those receipts will also come under the spending limitation.

Federal receipts and program receipts from other non-State sources (such as user fees and private endowments) would be exempt from the expenditure limitation. This will allow flexibility for State programs to respond to changes in non-State revenues, while requiring that any State assumption of the funding of those programs come under the spending limitation.

Because of the variability of non-State revenues, the inclusion of only State-source General Fund revenues in the spending limitation makes the identification of a base year figure easier and makes future year revenue projections similarly easier.

FORMULA

The formula for adjusting the base year figure is a national measurement of inflation and a measure for State population growth. The change in the national consumer price index has been used as the measure of inflation rather than a measure of inflation in Anchorage or in Alaska as a whole.

This is necessary in that the rate of inflation within Alaska results, in part, from State spending levels. The pattern of State spending has affected living costs in Alaska, and would likely continue to do so under spending at current levels. The rate of inflation reflected in the national consumer price index should be more stable and will not be influenced by the State's own spending pattern.

The portion of the formula which allows adjustment of the spending limit for the average rate of State population growth over the past two census periods is the same as is contained in both versions of the spending limit bill (HJR 57 and SJR 4). The identification of the federal census as a basis for population growth rates ensures that the population change figures are determined by a source outside State Government. Any other formula which would allow a State entity to set population growth figures could potentially create a situation wherein the State adjusts its spending limit (upward) based on its own (inflated) population growth figures. It is questionable whether the State has a reliable population monitoring system.

EXTRAORDINARY APPROPRIATIONS

A mechanism is included within the amendment to allow for unusual, unanticipated events or for needed projects which have wide general support. Since an addition is being made to the Constitution, we need to insure that future Governors, legislators, and citizens have an opportunity to respond to events and needs which we cannot foresee. However, it was felt to be equally important to insure that a door was not left open to routinely exceed the spending limitation. Therefore, the amendment presents a means by which to exceed the spending limit, but makes use of that means only by an extraordinary majority. In keeping with the concept of checks and balances, two options were provided. The first means calls for initiation of the extraordinary appropriation from the Governor. When so initiated, passage of the appropriation act depends upon the concurrence of two-thirds vote of each house of the legislature. Extraordinary appropriations can also be initiated by the Legislature; but in this case, three-fourths vote of each house must pass the appropriation measure, thus insuring a majority sufficient to overcome a possible veto. The reason for the differences in the majority needed for passage lies in the belief that the chief executive is elected statewide and is more responsive to statewide needs than a coalition of legislators. On the other hand, a three-quarters majority of both houses is fully as representative of statewide interests; hence, the inclusion of a means for legislatively initiated extraordinary appropriations.

The amendment specifies that each appropriation bill can contain only a single item. Again, this works toward the goal of common agreement on need to exceed the limitation, as "log rolling" is more difficult when single appropriation bills are at issue.

It should be pointed out that, while there is no mention made in this amendment, the amendment does not change the Governor's existing power to act in cases of disaster or emergency. Furthermore, the referendum process remains unchanged, whereby the Legislature can decide by simple majority vote to put spending questions before the voters, although funding of these items (aside from revenue bonds) falls under the spending limitation.

EXPENDITURE LIMITATION CHECKLIST

BASE

A fiscal year

A number   Which number?

Only state funds?   Federal funds?   All?

FORMULA

Private sector growth

CPI plus population

other

COVERAGE

Should coverage by of operating budget only?

Should there be exemptions? and if so, should they be open-ended or enumerated?

Sould general fund and federal funds be covered?

Should these be exemptions or override:

- Disasters - how to identify & who votes? (See Excess below)
- Disaster reserves
- Permanet Fund contributions
- Permanent Fund dividents
- Capital projects
- Loan capitalization - What to do about operational expenses and large maintenance costs?
- GBO repayment funds
- Increases in user fees
- Costs from court orders
- Costs from transfer of federal authority
- One-quarter of income from Permanent Fund
- Money in trust

OVERRIDE

By vote of Legislature   2/3 or 3/4?

By vote of people   Should this by limited by type? New operating programs?

OTHER ISSUES

Local government

"Apple pie/pork" trade

Proportion of capital to operating

Unfunded obligations

EXCESS

Where can it go and how can it get there?

Permanent Fund only Allow "earmarking"?

Trust accounts

By whose vote?

Invest at market rate

PLAN A

Lid	Except	Excess
general fund only	(simple majority)	automatically into PF at market rates
	other people's money	

In Plan A, the tradeoff is tightest in favor of holding the line - e.g. expenditure vs. expansion of new services.

PLAN B

Lid	Except	Override	By Referendum
State general fund only	(simple majority)	2/3 or 3/4 legislative	
op/cap/etc	GOB	vote	?
	PF	specified types	
	User Fees	very limited	
	Fed/other		

MALONE

Lid	Except	Override
General fund &	(simple majority)	2/3 legislative majority
federal dollars	PF	everything else
op/cap/everything	GOB debt service	

GOVERNOR

Lid	Except	Override	By Referendum
General Fund only	(simple majority w/	2/3 legislative majority	Excess capital
op/cap/etc	veto possible)	disaster dollars	projects
	money in trust		
	PF		
	PF dividents		
	Loan capitalization		
	GOB service		
	disaster fund		
	user fees		
	court ordered dollars		
	fed-state authority transfer		
	1/4 PF income		

Exemptions

A. Costs from Court Orders.

The costs of complying with court orders seem, at first blush, limited to legal costs and onetime program costs to "remedy" some problem that may be addressed by the court. However, a court order might have long-term program cost implications. Also, it is not clear that an exemption would apply just to the the budget year in which a court order would initially import, or would exempt permanently program costs that were initially "added" to the budget by court order rather than by legislative action.

The "Molly Hootch" agreement is a case in point. (Technically, this was an agreement approved by the court, but could as easily have been a court directive.) This case resulted in tremendous capital construction for village schools, as well as the attendant operating budget expenditures, maintenance and operation. The construction of Molly Hootch school committed the State to a pattern of educational service delivery that had significant, ongoing capital and oeprating budget implications.

The question is - should these types of expenditure be exempted from State spending limitations? Should the State's education budget be split between "exempt" and "limited" types of expenditures?

The problem is basically a question of ultimate responsibility for expansion of governmental services. A court case may require the State to take on a new service or expand a current service significantly. While it may not be "fair" to have that service counted against the expenditure limitation, it also seems against the whole purpose of the expenditure limitation to allow for the complete exemption (or separate accounting) of services "added" by court order from any comparison with a spending limitation.

The concern is that court decisions may result in services that have a completely separate identity from those originally under a spending limitation. Such services, if exempt from the spending limit could grow, flourish and have life of their own.

While one-time legal costs resulting from a court order might logically be exempted from a spending limitation, any service delivery expenditures resulting for a court mandate should be included in the general mix of State services delivered to the public. A court mandated service becomes a service such as any other demanded by the public.

(While it is true that including a court mandated service (or any other new service) under the spending limitation places more pressure on that spending limit, this is not a reason to create a "dumping ground" for State services that are added after the adoption of the spending limit. An exemption should not be used simply to delay the time when an expenditure limitation simply becomes too tight.)

C. Money Received in Trust for a Specific Purpose.

The meaning of this exemption needs to be clarified. First, appropriation of money to a trust for a specific purpose could be argued as an allowable exemption, to get general funds out of the capital and operating budget stream. However, unless it is specified that those funds are to be invested at market rates of return, this type of exemption could be used to subsidize a loan or investments project.

Second, it should be clear that the return from "trust fund" investments be returned to the General Fund for appropriations under the spending limit. This will prevent the operating expenses of any particular service from being removed from the expenditure ceiling through the creation of a "trust" or "endowment." If the purpose of an expenditure limit is in part to control the growth of government, program costs should not be exempted from limitation simply through the creation of an endowment.

MONEY RECEIVED IN TRUST

The intention of this exception is to allow for the acceptance and expenditure of bequests to the State; for example, support of the University. It seems appropriate to except from the limit other people's money given to the State for specific purposes.

LOAN CAPITALIZATION

This is one of the most difficult problems. On the one hand, the State has created a large constituency for loans. Subsidized loans distribute State benefits unequally. No one is recommending that the subsidy portion be placed outside the limit. However, if the caitalization is portion be placed outside the limit. However, if the capitalization is placed outside, then it is predictable that large sums will flow into those loan programs, whether they are needed or not. Additionally, the argument can be made that placing capitalization outside the limit will make it very difficult to identify the subsidy cost. Most of the return on loan funds go into the General Fund, although some of the "revolving loan" funds keep a level of capitalization (declining balance) within the fund. A strong argument can be made for placing loan capitalization under the limit: loans are but one way of achieving State goals; the Legislature should have the flexibility to determine the best way of achieving such goals. If loan capitalization is excepted, it should be clear that neither the subsidy portion nor the administrative costs are to be removed from the limit. In any event, the structure and control over the loan programs should be thoroughly explored.

INCREASES IN USER FEES

On the one hand, three is a risk of a tax being relabeled a "user fee" and, therefore, any user fees collected by a State agency or the State itself should be subject to the limit. On the other hand, user fee increases could be subject to legislative approval (or disapproval).

It seems poor public policy to deny a government service to those who are willing to pay for it.
Is there anything that would prevent charge of debt service of revenue bonds as a user fee?

PERMANENT FUND CONTRIBUTIONS

If the desire is to keep the Constitutional amendments wording as general as possible, "exemptions" could be handled as follows:

> "Appropriations to funds which serve only to produce income at market rates and which income shall be returned to the General Fund and subjected to the State spending limit, are exempt from the State spending limit."

DISASTERS

There seems to be agreement that "disasters" should be provided for outside the limitation. Questions, however, occur regarding the tightness of a definition or process that would restrict the use of this exemption to those situations truly qualifing.

If a situation is beyond question a "disaster," then it should be relatively simple to collect a super majority to override the spending limitation.

Restricting the definition to those disasters declared by the Governor and voted on by a super majority would also serve the purpose of preventing abuse.

CAPITAL PROJECTS

"Appropriation" is debt service on State revenue-bonded capital projects is subject to the limit?

The exception of capital projects has appeal to those who feel that Alaska has a great need for infrastructure development, etc. However, excepting capital projects from the limit creates problems. First, new capital projects place burdens on the operating budget. The cumulative effect of these increases may distort the usual budget by its demands. It would also be politically as difficult to say "no" to constituents who want new football fields, etc., as it is now, if capital projects were exempt from the limitation. The Governor's solution is to suggest voter approval. However, there is no reason for voters to turn down projects, since alternatives for the money are not offered. The situation could be improved by requiring that capital projects' operating and program costs be both identified and accommodated within the spending limitation. Another solution is to provide for a fund which is limited in some way that would provide for local capital projects (viz. Capital Foundation Fund). Without some control, capital projects' expenditures could be as uncontrollable as now and become a time bomb ready to explode the spending limitation. Another solution which has been suggested is to include capital projects within the limit (a higher limit) and specify that capital budget items can be no more than x percent of the annual expenditures. If capital projects are outside the limit, consideration could also be given to defining those capital projects eligible for funding as those which are needed to meet essential government services and necessary to the health, safety and welfare of residents.

STATE OF ALASKA

THE LEGISLATURE

BUDGET AND AUDIT COMMITTEE

ROOM 508
CAPITOL BUILDING
POUCH V
JUNEAU, ALASKA 99811

907-465-3818
907-465-3810

MEMORANDUM

TO: Senator Arliss Sturgulewski, Chairman
Legislative Budget and Audit Committee

FROM: Glen L. Svendsen, Special Assistant
Legislative Budget and Audit Committee

DATE: June 5, 1981

SUBJECT: Local Government Issues related to State Expenditure Limitations

Spending Limitation

Issues related to local government expenditures, and their relation to State expenditure limitations.

1. Property Tax Relief and State Policy on Repayment

   A) may not be related to either inflation or population change, as municipal decisions to take on or upgrade services may be separate from new population growth.

   B) If State does not repay full amount, political pressure may follow to do so, but the Legislature does not have to fully fund local property tax relief under present circumstances. That is, the Legislature has not formally taken on responsibility for local tax relief under municipal assistance or other programs.

   C) If State, through other legislation, restricts the ability of local governments to raise revenue (i.e., repeal rules taxes, reduce mill levy limitation or changes in levies) the State has, in effect, voluntarily taken on the responsibility of funding local governments. This may, in turn, have impacts on the State budget that have nothing to do with the formula for adjustments to the base year's expenditures, as local resident demands for improved services are translated into legislative budget requests.

D) Relation to resolutions before the Committee: Under HJR 57, increase appropriations for local tax relief that would be above the level otherwise allowed by expenditure limitation, but could be approved by a 2/3 majority vote of both houses. Under SJR 4, appropriations for property tax relief must fall under the limitation. Under the Governor proposed sponsor substitute for SJR 4, some form of "trust" could conceivably be established for property tax relief, and money directed to that trust could be exempt from inclusion in the expenditure formula. (P.S. - The ability to account for "trust funds" separately under the Governor's substitute encourages the creation of such trusts, which raises separate policy questions.)

2. Municipal Bonded Debt

A) There is a good deal of interest in the Legislature's role toward municipal debt. A bill now in process would provide an appropriation to help subsidize municipal bonds by paying the difference between current market rates and the eight percent maximum rate of interest at which those municipal bonds would be sold. In addition, the Municipal Bond Bank purchases municipal bonds for resale; State funds are then used in sales, guarantees and to cover potential defaults by communities.

B) If the State's policy is to continue support for municipal bonding, the spending limitation could create a problem in meeting the costs of increased levels of bonding. There is a major backlog of significant capital project needs in most Alaskan communities. It is conceivable that these projects could result in growth in State costs in excess of the growth allowed under either version of the spending limitation.

C) The problem arises in fitting the State's subsidy of local bonds into the list of exempted expenditures. HJR 57 would allow a special appropriation upon 2/3 majority vote of both houses. The Senate version, SJR 4, would not allow such an exemption, although there may be some evidence of intent to do so. State bonds and capital construction funds approved by the voters would be exempt from the budget limitations; however, the State could not have the same budgetary freedom in regard to local projects that are approved by local voters. As noted above, the Governor's sponsor substitutes to SJR 4 would allow appropriations subsidizing local bond projects to exceed expenditure limitations if some sort of trust and dedication system were established.

D) Local capital projects may result in higher local operating budgets, just as at the State level. What this means is a need for additional local revenue. Local citizen dissatisfaction with local tax rates, coupled with State level budget surpluses,

will be translated into more pressure on the Legislature to fund local governments. This will add operating costs to the State through local capital expenditures that might not originally be predicted in State expenditure forecasts.

3. Shifting of services from the State to the local level.

A) One means of holding down State budget growth is to shift various program (and budget) responsibilities to the local level. This, obviously, increases the cost of local government while reducing the budget liabilities of State government. Without increased appropriations to local government, the shifting of responsibility to the local level would require an increase in revenue derived from local sources. Coming on the heels of a period of local tax reductions and demands for complete elimination of local taxation, such an increase in local tax rates would create strong pressures on the Legislature to increase funding of communities and curtail their ability to raise revenues. In effect, the State may not actually (i.e., politically) be able to shift major fiscal burdens to local governments.

B) Shifting program responsibilities to local government and restricting the ability of local governments to raise revenue are mutually contradictory actions. The Legislature has, in effect, forced itself to choose between increased appropriations to local governments, or curtailment of the services it has shifted to the local level. (Curtailment of some services transferred to local control may be an option. It all depends upon whether the service is nonessential, or whether the State requires provision of a service after responsibility is transferred - such as requirements that locals adopt a permit system, etc.)

4. Local government expenditures in general.

A) Implicit in the argument linking expenditure limitations to population growth and the rates of inflation is the assumption that the existing levels of service are adequate, or that there are enough "frills" in government expenditures that an adequate level of services can be provided if the budget is "properly" appropriated. This basic assumption, however, may not be true, especially for local governmental expenditures. for it is at the local level that the existence and quality of public services varies so markedly from what might be considered to be desired by most people. This means that there is a built-in capacity for local governments to use - and demand - more money than would be allowed under an expenditure limitation, if revenues were otherwise available.

B) I think that the existence of large sums of money in the State treasury will lead to expectations for service improvements at the local level, as well as public resistance to paying higher local taxes. This will lead to pressures for the State to pick up not only State budget increases, but local government costs as well. The Legislature needs to have a clear policy toward local taxation from the outset. Presently, the Legislature seems to be accepting arguments that the State should pick up a portion of the local tax effort (i.e., full funding of revenue sharing and municipal assistance, local debt service subsidy, etc.). _If_ the State adopts an expenditure limitation, it should reevaluate whether the State should pick up local tax effort (i.e., which result from expenditure decisions controlled at the local level.)

421

Introduced: 1/13/81
Referred: Transportation, Judiciary and Finance

1 IN THE SENATE

BY THE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

2 SENATE JOINT RESOLUTION NO. 4

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 TWELFTH LEGISLATURE - FIRST SESSION

5 Proposing an amendment to the Constitu-
6 tion of the State of Alaska relating to
7 limitations on appropriations of state
8 money.

9 BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

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17 cle plus a percentage equal to the average yearly growth in the State's
18 population as shown by the last two federal censuses or renumerations.
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26 funds, but the money to subsidize low interest loans must be appro-
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28 to construct capital improvements, whether of bond proceeds or other-
29 wise, where the appropriation for the capital improvements is approved

by the voters; money appropriated to escrow accounts or otherwise to repay general obligation bonds; money appropriated as a reserve for disasters of natural or human origin or other emergencies; money appropriated to coincide with increases in user fees; money appropriated to meet increases in costs to the State resulting from court orders or a transfer of authority or responsibility to the State from the federal government; money derived from one-quarter of the income from those contributions made to the permanent fund which exceed the minimum required by this constitution; or money appropriated by a vote of two-thirds of the membership of each house and approved by the governor to meet disasters of natural or human origin which are declared by the governor.

* Sec. 2. The amendment proposed by this resolution shall be placed before the voters of the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska, and the election laws of the state.

Original sponsor: Rules/Governor

Offered: 5/5/81
Referred: Finance

1 IN THE SENATE BY THE JUDICIARY COMMITTEE

2 CS FOR SENATE JOINT RESOLUTION NO. 4 (Judiciary)

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 TWELFTH LEGISLATURE - FIRST SESSION

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SJR 4

STATE CHAMBER of COMMERCE
310 Second Street
Juneau, Alaska 99801
Phone 586-2323

January 5, 1981

1981 LEGISLATIVE GOALS OF THE ALASKA STATE CHAMBER OF COMMERCE

STATE SPENDING LIMIT, TAX RELIEF, BONDING

1. Limit state spending as proposed in the Alaska State Chamber of Commerce's current initiative by establishing Fiscal Year 1981 as the base year and tieing future expenditures to population and per capita income.

2. Exempt the first $250,000 in taxable corporate profits for all Alaskan corporations.

3. Eliminate future bonding and support capital improvements from the general fund as long as revenues are available. Require all projects over one million dollars to have voter approval so as to create public awareness.

4. Increase state revenue sharing to municipalities to cut or end property taxes.

5. Conduct comprehensive review of all oil and gas taxes, including a study of the windfall tax exemption for oil and gas companies.

ECONOMIC DEVELOPMENT GOALS

1. Establish a permanent power fund for statewide power projects..

2. Appropriate funds for electrical grid interties to stabalize power supplies statewide.

3. Support state encouragement for petrochemical industry development in Alaska.

4. Implement long term sales of state royalty oil and gas at prevailing rates to supply in-state refineries at maximum capacity.

5. Support full public use of the state highway from the Yukon River to Dietrich Pass (commonly called the "haul road") effective June 1, 1981. Support immediate action to provide adequate funding to bring this highway up to secondary road standards and properly maintained for the full length of the highway. Paving of this entire highway as soon as possible is in the best public interest.

(continued)

6. Recommends that integrated policy boards be established to administer the International Airport Revenue Fund composed of a majority of private business interests with the authority and responsibility to provide technical and policy direction in the development, planning, and operation of the airports to the Department of Transportation and Public Facilities. Further, that a comprehensive capital improvements program be established and funded through the general fund to support the facilities necessary for current demands as well as latent potential.

7. Endorse accelerated coal development in Alaska.

8. Propose the Department of Natural Resources rewrite state regulations to encourage timber, petroleum and mining development.

9. Request a rewrite of the U. S. Interior Department regulations to allow tourism, mineral, and oil exploration on national monuments.

10. Urge the state take a firm stand to encourage all possible domestic manufacture of forest products from public lands. Exceptions to primary manufacture should only be made when it can be clearly shown through the hearing process there are no possible domestic markets.

LABOR LEGISLATION

Encouraged by the preliminary work of the legislature's Workers' Compensation Study Commission, we support their efforts to improve the administration of the system and make the compensation program more competitive.

The Chamber further believes that their recommendations must also encourage realistic benefit revisions necessary to restore the incentive for injured workers to return to productive employment and to remove the excesses in employers workers' compensation costs.

GENERAL LEGISLATION

1. Institute a national campaign to improve Alaska's image and boost Alaska tourism.

2. Develop without delay a ten year capital improvement plan

3. Increase vocational training at the University of Alaska.

4. Abolish the Alaska Public Offices Commission.

5. Encourage state government to assist and support private enterprise in meeting the needs of the public. We further encourage state government to provide direct services only when it has been proven that private enterprise cannot fill the needs of the public.

6. Recommend the Alaska Renewable Resources Corporation be limited to equity or venture capital investment and grants, not loans in connection with equity capital investments. Allow not just renewable, but also non-renewable equity participation. The investment agreement should be more specific in the buy-out option (Example - Salamontof Seafood problem). ARRC should develop a banker-borrower relationship, not be both.

October 4, 1980 DRAFT

WHEREAS during the 1980's, Alaska faces the dual challenge of either the precipitous decline of revenue, or the possibility of new resource production and a continuing high volume of revenue; and . . .

WHEREAS either of the above cases requires the state to mobilize substantial restraint to control the rate of state spending and thus the burgeoning size of state bureaucracy and governmental influence; and . . .

WHEREAS governmental spending has grown to higher levels in Alaska than any other state in the nation using virtually any standard of comparison, including: per capita costs of the state legislature, per capita number of full-time state employees, rate of growth of government employment, rate of government salary increases, per capita costs of state government in general; and . . .

WHEREAS public support for statutory limits on state spending has been demonstrated by public opinion polls; and . . .

WHEREAS some legislative leaders and the state administration have shown support of a limit on state spending; and . . .

WHEREAS numerous public and civic organizations throughout Alaska have endorsed the need for controlling state spending; and . . .

WHEREAS the level of service established by state government in FY 1981 is considered adequate for our citizens' needs, and that year is appropriate to serve as the base year upon which to establish future budget limits;

NOW THEREFORE be it resolved that the Alaska State Chamber of Commerce endorses the concept of a limitation on government growth in statutory if not constitutional form; and . . .

BE IT FURTHER RESOLVED that the attached initiative is endorsed as an appropriate first step toward establishing a control on the growth of Alaska state government.

AN INITIATIVE

AN ACT ENTITLED: "An Act limiting state government spending."

BE IT ENACTED BY THE PEOPLE OF THE STATE OF ALASKA:

Section 1. AS 37.07 is amended by adding the following sections to read:

AS 37.07.102. State Spending Limit. In no year shall the total annual operating appropriations of the state government exceed the total annual operating appropriations for the prior year, adjusted for annual net percentage changes in Alaskan per capita personal income and population.

AS 37.07.105. Additional State Spending Limit Adjustments. The annual operating appropriations limit provided for in Section 102 of this chapter shall be further adjusted as follows:

(a) If the legislature or any state agency transfers the financial responsibility of providing services, in whole or in part, from the state government to any local government, or mandates a new program or higher level of service on any local government, the state shall provide subvention of funds to reimburse such local government for the costs of the program or increased level of service.

(b) If the financial responsibility of providing services is transferred, in whole or in part, from any entity of government to a private entity, or the financial source for the provision of services is transferred, in whole or in part, from the proceeds of taxes or other revenues to appropriations which are not subject to limitation, then for the year of such transfer the appropriations limit shall be decreased accordingly.

(c) If a state of emergency is lawfully declared by the state government, the appropriations limit may be exceeded, provided that the appropriations limits in the following three years are reduced accordingly to prevent an aggregate increase in appropriations resulting from the emergency.

AS 37.07.107. Contingency Funding. Each entity of state government may establish such contingency, emergency, unemployment, reserve, retirement, sinking fund, trust, or similar fund as it shall deem reasonable and proper. Excepting contributions to the

Permanent Fund and payment for bonded debt, contributions to any such fund shall, for purposes of Section 102 of this chapter, constitute appropriations subject to limitation in the year of contribution. Neither withdrawals from any such funds nor expenditures of such withdrawals, nor transfers between or among such funds shall constitute appropriations subject to limitation.

Section 2. AS 37.07.120 is amended by adding the following subsections:

(7) "Total annual operating appropriations of the state government" shall be established by reference to the fiscal year 1981 "total annual operating appropriations of the state government", exclusive of budget surpluses.

(8) "Total annual operating appropriations of the state government" shall mean any authorization to expend during a fiscal year the proceeds of taxes, income, or other revenues collected by or for the state other than the following:

(a) refunds and/or reduction of taxes;

(b) benefit payments from unemployment, unemployment insurance, and disability funds;

(c) payments for bond debt;

(d) constitutional or legislative appropriations to the Permanent Fund as established by Article IX, Section 15, of the Alaska Constitution;

(e) appropriations required for the purpose of complying with mandates of any court of competent jurisdiction and any appeal therefrom, or of legally binding mandates of the federal government rendered after adoption of Sections 102-107 of this chapter, which, without discretion, require expenditure for additional services or which unavoidably make the provision of existing services more costly;

(f) appropriations to local governments which mandate and result in a reduction of real property taxes.

(9) "Subvention" shall mean any endowment, subsidy, or other financial assistance provided by one entity of government to another.

(10) "Alaska per capita personal income" shall mean the personal income of individuals residing within the state as determined and reported by the Alaska Department of Labor or successor agency of the State of Alaska.

(11) "Population" shall mean permanent resident individuals of the state and shall be determined by method prescribed by the legislature, provided that such determination shall be revised as necessary to reflect the periodic census conducted by the United States Department of Commerce or successor agency of the United States government.

<u>Section 3</u>. This Act does not repeal or affect any appropriation made or existing at the time it takes place.

<u>Section 4</u>. This Act does not and shall not be construed to impair the ability of the state to meet its obligations with respect to existing or future bonded indebtedness.

<u>Section 5</u>. This Act takes effect in accordance with AS 15.45.220.

Senator Arliss Sturgulewski
June 10, 1981

CS SJR 4 (FINANCE)

SUMMARY

The first is Section 16 and deals with APPROPRIATION LIMITATION. It states that appropriations are limited to the appropriation of the previous year, adjusted for inflation and population change. The base is FY '82 at $2.7 billion.

Section 17 deals with EXCEPTIONS to the appropriation limitation. Exempted are:

- trust funds received from third parties;
- Permanent Fund deposits;
- money for General Obligation Bonds;
- loan capitalization funds, if a subsidy is contained under the limitation;
- money for disasters;
- and a limited sum for capital appropriations ($1500 per capita).

Capital appropriations and disaster appropriations are made by a two-thirds vote of each house and are subject to the Governor's veto. The State of disaster must be first declared by the Governor.

CONSTITUTIONAL LIMIT ON SPENDING

The primary reason for the constitutional limit on spending is to guard against a dramatic increase in government spending during the boom portions of Alaska's economic cycles. To the extent that a spending limit encourages saving of revenues, there are a variety of benefits from the limit, including:

1. To limit expenditures controls growth. This will mean retaining the capacity to support ourselves when revenues decline -- by limiting outgo and providing for future income.

2. The limit helps minimize the extent to which government spending must be cut back during the downswings in the economy. Government expenditures seem much easier to increase rather than decrease, and large decreases can be especially disruptive.

3. The limit helps make government spending a stabilizing influence in the economy. Spending will represent a relatively smaller portion of Statewide economic activity during the booms, and be able to respond to economic downturns.

4. The limitation covers most areas in which representatives traditionally have "traded off" and established priorities. Competition for the scarce resource of expenditure limited funds will bring back to the political process a healthy competition. There will be reason for legislators to say "no" to some projects, and to support others with needed dollars.

PROPOSED AMENDMENT EXPLANATION

The proposed constitutional amendment contains two sections.

The first is Section 16 and deals with APPROPRIATION LIMITATION. It states that appropriations are limited to the appropriation of the previous year, adjusted for inflation and population change. The base is FY '82 at $2.7 billion.

Section 17 deals with EXCEPTIONS to the appropriation limitation. Exempted are:

- trust funds received from third parties;

- Permanent Fund deposits;

- money for General Obligation Bonds;

- loan capitalization funds, if a subsidy is contained under the limitation;

- money for disasters;

- and a limited sum for capital appropriations ($1500 per capita).

Capital appropriations and disaster appropriations are made by a two-thirds vote of each house and are subject to the Governor's veto. The State of disaster must be first declared by the Governor.

As with other versions of the spending limitation, neither appropriations exempt from the spending limit nor extraordinary appropriations can be used to "increase" the spending limitation for the next fiscal year.

The present veto powers of the Governor remain unchanged. Both appropriations under the limit and appropriations exempt from limitation are subject to the veto. In turn, legislative veto override powers also remain unchanged.

Overall, the proposed language creates only a few "automatic" exemptions from the spending limitation. It is simply not possible to control the growth of government spending (and, in turn, government itself) unless the spending limitation is as all-inclusive as possible. Again, appropriations to the Permanent Fund and to funds invested at market rates are exempted as an encouragement to the Legislature to save rather than spend for larger government programs.

An analysis of specific exemptions included in this version of the spending limitation are attached.

REASONS FOR THE FORMULA CHOSEN

Section 16

A constitutional limit should be appropriate for a long period of time. In designing the formula, we looked for a long-term solution which treated downturns, repeat booms, and overall trends in State income, as well as our present wealthy conditions.

The first element of the flexibility which we built into the limit, (as have almost all other advocates of a constitutional limit) was to allow for inflation. Any specific dollar limit must be in adjusted-dollar terms, as inflation is too great to make any other formula workable over a long period of time. A federal index of Alaskan inflation was specified because it was thought a third party source for the measure was desirable. In this way, the State will not be determining the rate used for its own limitations.

The second element of flexibility was to allow for a dampened amount of swing in government spending levels to accompany swings in the economy. During times of economic expansion, the constitutional limit is allowed

to grow, in real terms, to the extent that population grows. During the downswings we believe that taxpayer resistence and other economic realities will hold State spending in check, and that in a broad sense government spending will be regulated by ability to pay. Therefore, there was no need to make specific provisions in the constitutional limit for economic downswings.

It is important to note that the limit on spending refers to the previous year's appropriations as a base. It is a limit on the rate of growth, which in turn controls total size during boom periods. It is a much more flexible and effective limit than one which establishes a single base year and gives a cumulative adjustment for inflation and population growth, since the latter formula limit will probably grow beyond the State's ability to pay within ten or twenty years.

SCOPE OF THE CONSTITUTIONAL LIMIT

Section 17

The approach we follow is that aggregate levels of State activity must be controlled. Therefore, the limit must include -- and be appropriate for -- almost all State activity. The only reasons for an exclusion from the limit are:

1) Extraordinary items

2) Provisions to take care of excess State income during boom periods, through the Permanent Fund and other investments.

3) Allowing for a controlled response to the State's development needs through loans and capital improvements.

Money Received In Trust for a Specific Purpose

This exemption is designed to allow for the receipt of non-State funds which are restricted for specific purposes. The State presently receives money which must be spent for specific purposes. The intent of this exemption is to allow for the receipt and expenditures of these funds from non-State sources outside of the limitation. The language included in the bill specifically notes that the trust funds' exemption applies only to funds from another source. This exemption would apply to such items as benefactors' trust funds to a museum or the university.

Permanent Fund

Appropriations to the Permanent Fund are exempt from the expenditure limitation for two reasons. The first reason is to assure that deposits to the fund do not compete with appropriations for other purposes. By limiting State spending in other areas, more funds should also be available for deposits to the Permanent Fund. This will allow deposits to the fund to be larger than they might otherwise be under a spending limitation.

Secondly, the larger the contributions to the Permanent Fund, the more revenue from that fund will be available for State spending in future years. To meet the intent of the Permanent Fund as a source of major State revenues after oil revenues begins to decrease, deposits to the fund should be as large as possible. The exemptions of the Permanent Fund from the expenditure limitation will encourage generous Permanent Fund deposits which will stabilize State services over time.

Principal and Interest G.O. Bonds

The State's financial advisors tell us that our bond rating will be negatively impacted unless the bond market feels secure that principal and interest on General Obligation Bonds will be exempt from the limitation. This allows the State to meet previously made commitments.

Money to Capitalize Loan Funds

Loan fund capitalization, as distinct from the subsidy for loan funds, is excluded from the limitation. If loan funds earn market rates, then no appropriation limitation applies. If the Legislature desires to subsidize loans, then the subsidy difference between the market rate and the subsidized rate will be made up from under the limitation. It is equitable that the subsidy should compete with other statewide benefits to citizens that are also under the limitation.

Capital Improvements

The limitation figure includes money for capital construction. The sum of $1500 per capita has been added to the amount contained under the limitation. This means a secured sum of money will be available for capital projects needed in the State, but limits the total available in much the same way as the budget itself is limited in Section 16. Thus, two pools of money are available for capital construction allocation. The $1500 figure is not adjusted for inflation, providing a declining amount of money available parallel to the decline in Prudhoe Bay revenues, and the filling up of the operation budget of capital project operation, maintenance and programs costs that have accumulated over the years.

Disasters

Disasters are excepted from the State spending limit. The intent is to include such things as:

> Need for relief moneys after a natural disaster, providing that such relief is not taken care of by insurance or some other programs; or
>
> War or similar threats against the State.

Cases of disaster should be unusual and unforeseen. These constraints prevent the exception for emergencies from becoming a routine loophole.

When such a situation exists, the State spending limit may be exceeded upon a declaration of disaster by the Governor, and appropriation of the funds in excess of the State spending limit by a two-thirds majority vote of both the House of Representatives and the Senate. It should be noted that for both capital and disaster appropriations, the Governor retains the authority to veto the appropriation made by the Legislature.

Original sponsor: Rules/Governor

1 IN THE SENATE BY THE FINANCE COMMITTEE

2 CS FOR SENATE JOINT RESOLUTION NO. 4 (Finance)

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 TWELFTH LEGISLATURE - FIRST SESSION

5 Proposing an amendment to the Consti-
6 tution of the State of Alaska relat-
7 ing to limitations on appropriations
8 of state money.

9 BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. Article IX of the Constitution of the State of Alaska is
11 amended by adding new sections to read:

12 SECTION 16. APPROPRIATION LIMITATIONS. The amount of State money
13 the governor may request or the legislature may appropriate during a
14 fiscal year shall not exceed the amount appropriated in the preceding
15 fiscal year by more than the increase in the federal consumer price
16 index for the State for the calendar year preceding the governor's
17 submission of the budget under Section 12 of this article plus or minus
18 a percentage equal to the cumulative average yearly growth or loss in
19 the State's population as shown by the last two federal censuses or
20 reenumerations. Money appropriated under any exception prescribed by
21 Section 17 of this article shall not be included in the base for deter-
22 mining the allowable increase from year to year. For purposes of this
23 section, the amount of $2.7 billion shall be used as the amount of
24 appropriations in fiscal year 1982.

25 SECTION 17. EXEMPTIONS FROM APPROPRIATION LIMITATIONS. The
26 limitations on increases in appropriations established in Section 16 of
27 this article do not apply to money received in trust for a specific
28 purpose; to appropriations of money to be deposited in the Alaska
29 permanent fund; to money appropriated to pay principal and interest on

general obligation bonds; to money appropriated to capitalize loan funds, but only if the money to subsidize these loans at below market interest rates is appropriated separately under the limitations; to money not to exceed $1,500 per capita appropriated by the affirmative vote of two-thirds of the membership of each house, whether of bond proceeds or otherwise, to construct capital improvements; or to money appropriated by a vote of two-thirds of the membership of each house and approved by the governor to meet disasters of natural or human origin which are declared by the governor.

* Sec. 2. The amendment proposed by this resolution shall be placed before the voters of the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska, and the election laws of the state.

Tax and Expenditure Limitation:

A Policy Perspective

The Council of State Governments

The Council of State Governments

The Council is a joint agency of all the state governments—created, supported, and directed by them. It conducts research on state programs and problems; maintains an information service available to state agencies, officials, and legislators; issues a variety of publications; assists in state-federal liaison; promotes regional and state-local cooperation; and provides staff for affiliated organizations.

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Tax and Expenditure Limitation:

A Policy Perspective

By
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Lexington, Kentucky

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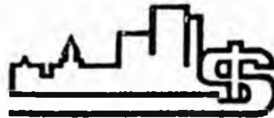

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Foreword

State governments since the nineteenth century have imposed limitations on the capacities of their local governments to raise revenues, especially property taxes. Since 1976, 18 states have also imposed limitations on their own capacities to raise revenues or spend money. In addition, a number of states have added to the traditional property tax limitations on local governments new limits on the total amounts these governments can raise or spend. All of these activities are now commonly referred to as tax and expenditure limitations (TELs). Since the passage of Proposition 13 in California in 1978, virtually every state legislature has considered one or more TEL-type proposals each year.

Attempts to limit all, or most, of a state's revenues or expenditures are very complex and raise many policy issues of critical importance to the fiscal integrity of the state and its economic and social well-being. This report focuses on the problems encountered in devising such legislation and reviews the manner in which the 18 states have dealt with them. The report is designed to raise issues for the consideration of legislators and their staffs who contemplate the adoption of such limitations for their own states. It should also be of interest to others studying this modern trend.

The study was funded in part by the U.S. Department of Housing and Urban Development under Grant No. H-5058.

Lexington, Kentucky
February 1981

Frank H. Bailey
Executive Director
The Council of State Governments

Introduction

Few events in the history of state and local government have received the attention and interest accorded the passage of Proposition 13 in California in 1978. A wave of publicity heralded a "taxpayer revolt," in which the overburdened taxpayer would wrathfully impose limits on governmental officials at all levels and force them to spend only what the average taxpayer could afford. The sponsors of the constitutional amendment in California traveled the country calling for similar actions in every state, and many elected officials in state and local governments seemed determined to lead their local movements. As the Institute for Contemporary Studies described this mood in 1978:

> The passage of California's Proposition 13 last June startled the nation's taxpayers as much as it did legislators and public officials. Almost overnight, taxpayers groups started springing up in communities across the country, and a number of states began drafting similar initiatives for consideration in upcoming elections.[1]

Since 1978, many publications have focused on this subject and carefully traced new developments.[2] The acronym TEL—short for "Tax and Expenditure Limitation"—is by now familar to all state executives and legislators. It is doubtful that any legislative session since 1978 has failed to address several such proposals, and the Council of State Governments has sought to keep its constituents abreast of these developments by reporting on proposed and adopted legislation and explaining the implications of each type of limitation. This report seeks to bring the record up to date and create a better awareness of the implications of TELs for financial and operating policies.

It is important to realize that limitations on governmental powers to raise revenues and spend money are not new. Indeed, they have been tried in various forms, especially at the local level, for more than a century. Proposition 13 is one dramatic indication that traditional tax limits have fallen short of perceived public needs in these times of rampant inflation (among other adverse economic trends). Nonetheless, a brief review of past ex-

periences with such limitations places current activities in an historical context that may temper the possibly unrealistic expectations of modern TEL zealots. This historical review is presented in Appendix II.

This report is written for the information of state legislators and executives who are considering the use of tax and expenditure limitations as means of gaining control of ever-increasing governmental costs. While such limitations are not unique in the history of American governments, in their new emendations, these constraints tie increases in revenues and taxation to economic indexes which are thought to represent the ability of people to support their governments. As a result, the emphasis overwhelmingly has been on curbing the needs of governments for revenues.

This report examines some of the more difficult analytical problems associated with the development and application of economic indexes, such as level of personal income, growth of the economy, and rise in the consumer price index. The application of these nationally developed tools to state and local purposes, the designation of base periods to which they apply, and the problems of limiting revenues that are elastic with respect to the economy all pose serious theoretical and practical problems to the drafters of TEL legislation. Attempts to limit expenditures likewise pose difficulties, given the large number of specialized funds with which most state governments operate. Finally, all of these factors must deal with the necessity of governments to provide ongoing services while being in the best possible position to meet life-threatening emergencies.

Proposition 13 focused national attention on the unpopularity of the property tax at the local level. Events since 1978, however, have also served to stress the necessarily close relationship between state and local governments in periods of fiscal stress and adjustment. The California experience has shown the need to reassess the state's role with respect to local government responsibilities, allocation of fiscal resources, and, ultimately, distribution of authority for dealing with public needs. Most states are now looking at the total revenue and expenditure picture within their states, and the policy issues being raised have profound implications for the future roles of governments at all levels.

It is not the purpose of this report to take a position for or against the adoption and use of tax and expenditure limitations. Financial administration at the state and local levels is an extremely complex process which has been complicated in modern times by the ever-increasing scope of governmental activities and the steady integration of federal, state and local responsibilities in addressing a wide variety of socioeconomic problems.

As a consequence of these developments, modern attempts to place effective constraints on the collection and use of taxes and other revenues will be extraordinarily difficult. In addition to the complexities of governmental financial administration, the variety of intergovernmental fiscal flows makes the application of limitations a very difficult undertaking. Given the bewildering array of interlocking federal-state regulatory provisions, state officials may find that reductions in certain types of expenditures may result in even greater reductions in federal assistance.

Adding to all these difficulties are the problems of developing data bases necessary to administer effective programs of limitations. No two states have the same system of accounting, so generalizations concerning the best methods of accountability (and, thus, adherence to any given TEL) are difficult to draw. Economic indexes developed by the federal government (e.g., state personal income, consumer price index, rates of inflation, levels of productivity) are approximations at best and are often very difficult to apply to highly localized circumstances. This problem is compounded when the states attempt to impose TELs on their local governments.

The report also discusses the shortcomings inherent in TELs. These types of limitations are no substitutes for the development of equitable systems of taxation, improved government productivity, and responsive and effective bureaucracies—to mention only some of the pressing issues included in the public's demand for economical and effective government. Properly developed as an integral part of a larger overall effort of governmental reform, a TEL could well play an effective role in finding a balance between the vital need for effective governmental services and the ability of citizens to pay the costs.

Eighteen states have some form of limitation on their own taxes or expenditures. There have been so few evaluations of the results of these limitations that assurance of success in curbing future governmental costs must be largely speculative at this time. Accordingly, this report seeks to direct attention to the obvious analytical problems and policy implications that will exist regardless of the objectives being pursued. Only time will tell whether these types of controls can assure the American taxpayer of more effective government.

The report is presented in two principal parts:

(1) **Modern Trends.** A brief description of the problems addressed and the techniques used in recent attempts to contain the costs of state and local governments.

(2) **Review of Policy Issues.** A detailed analysis of the technical problems with which TEL designers must contend and explanations of their implications for the operations and directions of state governments.

Modern Trends

The term "tax revolt" has come to characterize the period since June 1978, when Proposition 13 passed in California. Writing in 1979, Frank Levy made the following observation about this revolt: "Proposition 13 was not a spontaneous phenomenon, but was rather the latest inning in a biennial event, a restitching of numerous earlier initiatives."[3] Why then did Proposition 13 become such a powerful symbol which appears to have triggered a number of other efforts to put legal limitations on state and local spending? It definitely was a media event attracting national attention. In fact, as Donald Hagman pointed out in September 1978, the voters of California "were not likely voting their pocketbook. . . . They were voting an ideology that the public interest would be served by enactment of Proposition 13."[4] Clearly, the severity of this one-time decrease in local revenues, the use of the initiative to write the limitation into the state constitution, and the confusion of many prominent political leaders in attempting to deal with the issue all contributed to the attention the action received.

It is likely that few voters understood the implications of the initiative. Some of the issues related to the proposition that did not receive a great deal of attention at the time are the following:

- Property tax is declining in significance for local governments, compared to other sources of tax revenue.
- In spite of Proposition 13's prohibition against increasing other *taxes* to make up for lost property tax revenues, local governments can use a variety of nontax sources, especially fees and service charges, to compensate.
- To the extent that the state government bails out the local governments and school districts, as California has done, there will be increasing centralization of control toward the state level.
- For people in the higher income brackets, as is the case with many homeowners in California, property tax payments provide valuable federal income tax deductions; thus, by shifting the tax burden to other forms of taxation or fee payments, the homeowners have lost an important source of deductions.

Is it likely that California voters consciously voted for increased centralization of government at the state level and lower deductions for income tax purposes? They obviously voted for the direct, pocketbook issue of lower property taxes and undoubtedly wanted to send a broader message to governments at all levels that the growth in the cost of government must be brought into line with the financial capacity of the taxpayer. The more publicity given the proposition, the greater the ideological overtones. In this process, it is not surprising that many collateral issues were overlooked by many. Nonetheless, the impact of the national attention the proposition received is still being felt.

Without comparable national attention and before the passage of Proposition 13, the states of New Jersey, Colorado and Tennessee had already adopted limitations on *state* expenditures in a manner that was much more unusual historically than California's reductions of its property taxes. In fact, New Jersey adopted a package of state-local limitations that was unprecedented at the state level. It tied increases in state *expenditures* to the growth in state per capita personal income as measured during the second quarters of each of the two years preceding the year in which the budget would go into effect. New Jersey was the first state to attempt any comprehensive limitation of its expenditures since World War II, and it was the first state ever to take advantage of federally maintained data sources concerning state economic conditions to tie the growth in state costs to the apparent ability of the citizens to pay. For state governments, this established a very significant precedent.

Many of the problems involved in adopting the New Jersey approach (similar to that taken by several states) will be discussed throughout this report. One of these problems concerns the meaning and scope of the term "state expenditures." Obviously many governmental disbursements are unrelated to the income of the state's citizens (e.g., pensions, debt retirement, trust and agency transactions), while other expenditures will rise as the income of at least some sectors of the citizenry declines (e.g., unemployment payments and welfare-related costs). Recognizing these problems, New Jersey excluded from its limitation appropriations for state aid to local governments, expenditures of federal funds, and debt service costs for indebtedness authorized by referendum. There was a provision to exceed the limit if such an increase were approved by a majority of the voters in a referendum. New Jersey also placed a limit on municipalities and county governments of 5 percent over the prior year's appropriations (with exceptions for very small governments). And, the state limited the use of

revenues from state income tax to education and property tax relief.

By the end of 1980, 18 states had placed limitations on their own expenditures or revenues. A listing of these states, together with a brief explanation of the variations employed by each, is set forth in the chart presented at the conclusion of this report as Appendix I. A wide variety of approaches has been used; however, most of them are directed toward relating increases in state (and also local, in some instances) costs and/or revenue collections to the growth in the economy or to the level of personal income of state residents. The language used in various laws includes the following (note that several states use more than one criterion):

- Growth in the "state's economy" (Hawaii, Tennessee and Texas).
- Growth in personal income (Arizona, Idaho, Louisiana, Michigan, Missouri, New Jersey, Oregon, South Carolina and Utah).
- Increase in cost of living (California and Nevada).
- Growth in population (California and Nevada).
- Relationship of current year's spending plans or revenues to the past year *or* the average of several past years (Colorado and Rhode Island).
- Relationship of current spending plans to anticipated revenue collections (Delaware and Washington).

As straightforward as these indexes may seem, many problems arise when they are applied. Included among these are the following:

- How does one determine growth in the state's "economy" for tax-support purposes?
- Are cost-of-living or personal income data suitable as criteria for a state or local government's level of spending?
- Does a limit on state expenditures include all disbursements and obligations regardless of the financial basis of their support and the purposes to which they are to be put?
- How does the government limit revenues that are elastic with respect to economic conditions?

These questions, along with others, are the concern of this report. Their answers raise serious technical and policy problems for the drafters of TEL legislation.

There are extremely important practical and philosophical problems implicit in the whole process of considering tax and expenditure limitations. The analytical complexities attendant on the development of effective and equitable fiscal limitation systems are staggering. Experiences with similar efforts to limit governmental costs over a period of more than a century leave room to doubt the efficacy of statutory provisions alone. To assure

effectiveness, a comprehensive assessment of all the factors involved in the process of developing, implementing and assessing spending and revenue plans is essential.

Review of Policy Issues

The term "policy" is used so frequently that its meaning is all too often taken for granted. Policy issues have to do both with where an organization is going and how it should get there. A number of actors, including the general public, the legislature, the executive, departments, and other agencies of state governments and their local jurisdictions, have different roles with respect to each type of policy issue. Each of these actors and entities deals with policies at one time or another—even if only to vote in an election where the issue has been raised (directly for a proposition in a referendum or for a candidate espousing certain positions with respect to a given issue).

It is probably common for even important issues to arise and be addressed with respect to only one, or a few, of its important facets, while very important aspects are ignored. For example, virtually every major policy issue has the following three dimensions:

(1) *Directional.* What should the state government, or other governmental entity, do, and which sectors of the population should benefit in what respects?

(2) *Organizational.* Who should be responsible for what is to be done (e.g., agencies, levels of government, officials) and what organizational structures should be used in the process?

(3) *Resources.* How should funds be allocated, positions authorized, and other resources provided for undertaking the authorized activities?

The principal issues involved when considering TELs clearly concern the resources to be made available to governments in order to deal effectively with the problems with which the community, region or state is faced. Much of the data appearing in the news media concerning the tax limitation question focuses only on governmental resource problems, such as increasing levels of taxation, growing size of government at all levels (e.g., number of public employees), and the increasing difficulties of taxpayers in supporting governments under these conditions. While services are sometimes allud-

ed to, the observations are usually very generalized. The term "welfare," for example, characterizes a group of services unpopular to many taxpayers. While these reports to the public are often specific about the levels of taxes and the costs of government, they seldom are equally specific about the nature of the public problems addressed by governments or the quantity and quality of service provided. There is a visceral element in discussions about increasing taxes that is absent in discussions about sewage disposal facilities or public health nurse visits.

This chapter reviews existing tax and expenditure limitations from the perspective of all types of policy considerations. That is, while resource issues are the central focus of concern, the relationship of these issues to the ability of governments to achieve their objectives and fulfill their responsibilities is emphasized throughout.

The chapter is organized in the following manner:

• **Pressures for TELs.** The most important question is whether the means of direction, control and resource allocations available to state and local policymakers are so inadequate that they must be supplemented by these types of statutory or constitutional provisions.

• **Technical Problems.** Designing and implementing TELs present numerous analytical and administrative problems, especially if the limitations proposed involve the use of economic indexes, the use of a functional period of reference (e.g., the last fiscal year), and efforts to comprehend all, or most, types of disbursements and revenues.

• **Revenues or Expenditures.** Legislators and analysts have all taken pains to distinguish between curbs on revenue sources (as with Proposition 13 and the property tax) and expenditures; however, the significance of the difference may often be misunderstood.

• **Scope of Limitations.** The problems associated with curbing revenues that are elastic with respect to the economy (e.g., sales tax and income tax), limiting types of expenditures whose dynamic characteristics are beyond budgetary discretion (e.g., pension commitments, trust and agency funds, countercyclical assistance programs), and otherwise laying the fiscal basis for economical government by statutory enactments raise significant challenges to legislative draftsmen.

• **Control Methods.** In an effort to make government affordable, legislatures are choosing between the use of flat rates (e.g., percentage increases over previous years) and indexes of economic conditions (e.g., increases in personal income, increases in the cost of living), both of which pose policy problems.

• **Provisions for Exceptional Circumstances.** Governments must be able to contend with unforeseen events which threaten the health, safety or welfare of the public; therefore, drafters of TEL legislation must face the challenge of providing for emergencies in ways that will not destroy the effectiveness of the limitations themselves.

• **Limitations on Local Governments.** The special problems faced by state governments seeking to impose revenue and expenditure limitations on local governments are similar to most of the problems listed above *and* challenge the continued integrity of home rule.

These issues are discussed in the following sections. The references to statutory variations used by the states are very brief and assume the reader will refer to the compilation of state provisions provided at the conclusion of this report.

Pressures for Tax and Expenditure Limitations

It should be noted that the term "tax and expenditure limitations" is something of a misnomer. While Proposition 13 and several other limitations in use are in fact directed toward forms of taxation, most other limitations are on all, or most, *revenues*. However, in the media and many other publications, the initials TEL have become popular and recognized as referring to all of these efforts to curb governmental costs and growth. In this report, when TEL is used, "taxation" should be regarded as synonymous with "revenues" unless an exception is specifically made. In subsequent discussions in this and other sections, the significance of the casual use being made of such terms as taxation, revenue, expenditure, and income will be noted.

Of the 18 states with limitations on their own revenues or expenditures, eight have constitutional provisions. Of these, seven were imposed by referendum. In these latter instances, the question of the desirability of a limitation was not in the hands of the state legislatures. Yet, ten of the states imposed the limitations by statute, and it is likely that most of the remaining states considering such actions will have to make a conscious *legislative* decision about whether to impose such fiscal strictures on themselves. They will have to ask: Why should we limit our powers in this vitally important area of legislative prerogative?

A bedrock principle of Anglo-American governmental philosophy is that the legislature initiates spending programs and authorizes the revenues (e.g., taxes, fees) required to finance them. The great civil war in seventeenth-century England was fought primarily, though not exclusively, over this principle.[5] Embedded in the Constitution of the United States and every other charter of government in this nation is this supreme right of the legislature. Powers associated with this role include authorizing the spending program for each fiscal period; levying taxes and imposing fees and charges; allocating responsibilities among governments and agencies; authorizing staff complements for all agencies; authorizing the overall administrative infrastructure; imposing controls and other means for administrative accountability; and overseeing operations, evaluating results, and redirecting governmental activities. In short, the government of a state or local jurisdiction can only undertake such activities, use those resources, and operate in the ways authorized by the cognizant legislature. Historically, legislatures in England and America have been loath to give up this authority. At least in principle, these powers are adequate for any legislature wishing to reduce governmental costs and associated taxes.

Pressures for spending are nothing new in America. In the early years of the Republic, representatives of armament manufacturers, railroad developers, shipping concerns, and countless other pressure groups sought to sway public demands and make legislative cooperation as convenient and lucrative as possible. In fact, few eras in our history have seen reduced governmental spending (though a particular government might occasionally retrench) or lessened involvement of government in the private lives and business enterprises of Americans.

Undoubtedly the Great Depression and World War II placed governments at all levels in a new perspective in which they assumed increasing responsibility for the health, safety and well-being of their citizenry. In this process, not only did the number of programs and their costs increase, but the programs were also established in ways that made their escalating costs uncontrollable as far as any one session of legislatures was concerned (at least this has become a colloquial disclaimer). Hence, tying Social Security, unemployment payments, welfare assistance and similar social programs to economic indexes created a situation in which the apparently all-powerful legislature was effectively helpless in attempting to curb rising governmental costs and expanding bureaucracies. In addition, so many groups were supported, in whole or in part, by these programs, that legislative efforts to cut back could often be overcome by effective political action.

Of course, these are only some of the factors pushing the costs of government upward. During the past 20 years, the demands of organized public employees, especially at the local levels, have often been reinforced by strikes and other actions which all too often posed hopeless political dilemmas to local officeholders. Settlements of these confrontations have usually been demanded by an inconvenienced public, but these agreements were reached at great long-term cost to the taxpayer. In addition, since World War II, a continuous inflation has forced up all costs for government and taxpayer alike. Overall, an extended period of increasing public demands for personal security and governmental service, effective actions by public employees for higher wages, and ever higher costs of all governmental operations have posed to legislators at all levels of government an impossible array of obstacles to the establishment of smaller, cheaper and more efficient governments.

Under these circumstances, an imposed limitation on spending and/or taxation can be a welcome relief to the harried legislator. He or she can point to this "cap" as a point beyond which the aggregate demands for spending cannot go, leaving only the decisions of how best to allocate restricted resources. Indeed, this option may be so attractive that a legislature would like to see it imbedded in the state constitution, and a number of states have proceeded in exactly this manner.

The basic question under these circumstances is whether the legislature feels a limitation must be imposed on its power to raise revenues or appropriate funds if it is to keep the cost of government under control. Given the apparently clear language of most TELs limiting expenditures or revenues in accordance with specific criteria (e.g., percentage increase over previous year's revenues, increase in level of state personal income), this type of constraint may appear to be a simple answer to the problem of runaway budgets. A closer look at the implications of these criteria, however, discloses many technical problems and policy issues that deserve comprehensive analysis and careful consideration. This is especially the case if the legislator is as concerned with meeting the state's service responsibilities and policy objectives as he or she is in controlling costs. An examination of these problems is the subject of the remainder of this report.

Technical Problems

The language used in the statutes and constitutional provisions concerning tax and expenditure limitations is usually straightforward and apparently easy to apply. The different approaches taken by the states to date will be discussed in a later section; however, examples will serve to illustrate some significant problems:

- Arizona limits state spending to 7 percent of the personal income of its residents.
- Colorado limits general fund spending to 7 percent more than the previous year.
- Hawaii limits the rate of growth of general fund appropriations to the estimated rate of growth of the state's economy.
- Michigan limits its revenue (defined as general and special revenues, less federal aid, with some minor adjustments) to approximately 9.84 percent of the personal income in the previous calendar year, or the average of the personal income in the three previous calendar years, whichever is greater.
- New Jersey limits increases in state expenditures to the growth in state per capita personal income as measured by changes between the second quarters of each of the two years immediately preceding the year when the budget is to go into effect (applicable to general state operations and to capital outlays).
- Texas limits the rate of growth of appropriations from tax revenues in a biennium to the estimated rate of growth of the state's economy.

While every TEL state has some variation on the theme, these are representative of the approaches used. Clearly, every effort is being made to relate costs and taxes to the apparent ability of the people to pay. Per capita personal income or total personal income is the principal, but by no means only, index in use. Estimates for these indexes are made by the U.S. Department of Commerce for each state, Standard Metropolitan Statistical Area (SMSA) and county and are used for a number of purposes. However, there are many problems in using them as guides to tax equity. In this section, the following three special problems will be addressed very briefly:

- **Use of Economic Indexes.** Are these dependable criteria of ability to pay, and are they applicable as constraints on governmental spending?
- **Use of a Base Year or Period.** Have all factors involved in calculating expenditures and receipts in a given completed fiscal period been determined in a consistent and accurate manner?

• **Fund Structures.** Considering the special purposes of most of the funds and the existing conditions controlling their receipts and disbursements, can revenue and expenditure limitations be applied to all or most of a state's financial transactions?

Economic Indexes

It is important to note that the equitable imposition, assessment and collection of taxes are the subjects of an enormous body of technical literature. The incidence of sales, property, income and other taxes (especially the degree to which each type is progressive, proportional or regressive) has been studied for decades and is still being analyzed extensively. Most of these studies are directed toward the need, as most experts see it, for tax reform. The mixes of types of taxes, the allocation of powers to tax among different levels of government, the actual formulas used in imposing taxes, tax assessment practices and collection processes are all subjects of great concern. It is possible that some people regard a TEL which is based on the economic conditions of a government's population (e.g., personal income, growth in the economy) as a substitute for tax reform. This is a grave error. Problems in the distribution and incidence of taxes will remain regardless of the *level* of total taxes imposed. A regressive sales tax (usually regarded as one imposed on the basic necessities of life) is still regressive whether it is fixed at 6 percent or 10 percent. Thus, any concern about the fairness of a given state's system of taxation for each sector of the population will not be met to any significant degree by the imposition of an overall tax or expenditure limitation.

States already have come to realize the difficulties involved in determining and applying such indexes as personal income or economic growth. Thus, different procedures are being used to derive appropriate indexes:

• In Arizona, a three-member Economic Estimates Commission ascertains personal income.

• In Tennessee, state personal income is derived from an econometric model maintained by the University of Tennessee.

• In Texas, projections of growth in the state's economy will be taken from an econometric model developed by the State Comptroller's Office. No comment can be made here about the specific models proposed or in use. Presumably they take the most important factors into account. However, particular attention should be given to assessing the accuracy of

models that *project* economic variables for future periods since these could be of doubtful reliability.

Many other states use estimates for *earlier* periods such as those for total personal and per capita personal income prepared by the Bureau of Economic Analysis of the U.S. Department of Commerce. In using these estimates, states should take into account the fact that they are not based on special statistical surveys of each state. Rather, the Commerce Department uses more than 175 income components for a given time period to derive estimates of personal income in several different types of geographical areas (state, SMSA or county). Total and per capita personal income estimates are both developed. However, neither of these income estimates takes account of the *distribution* of income. An unusually high proportion of wealthy people could skew per capita figures upward in a manner that overlooks an even larger proportion of poor people who are very heavily burdened by regressive taxation. States with large sectors of migrant workers, high welfare rolls, increasingly large numbers of the elderly, and similar demographic characteristics have found these concerns to be far from theoretical.

The use of personal income as the index for growth in revenues or expenditures can also lead to another problem. In a recession, personal income will drop just at the time countercyclical spending (e.g., unemployment payments, welfare payments, food stamps) is triggered. Of course, all states have some type of override provisions in their limitations; however, these are usually invoked slowly, especially where a referendum is required, and could be extremely difficult to get past a determined minority in states where unusual majorities are required. The state may well find itself in a position of having to cut vital services in areas such as health, education and prisons because the TEL forces most available revenue into the countercyclical programs. Efforts made in good faith to relate taxation and expenditures to ability to pay may prove to be unsuccessful or even counterproductive unless the consequences of the formulas imposed are thoroughly understood by the drafters of the legislation.

The Use of a Base Year or Fiscal Period

A number of limitations are based on the previous year's (or fiscal period's) expenditures or on averages of several years. The extent of any increase is related to increases in personal income or other economic variables. References to past years are probably unavoidable when attempting to

develop a formula limiting the growth of state expenditures; however, great care must be exercised in determining what the use of a particular base period implies.

If a state starts its new plan with the most recent or current fiscal period, it is building existing policies, administrative practices, levels of service, and many other operational and policy matters into its future. Before a base period is selected, careful consideration should be given to what economic conditions, executive/legislative policies, current emergencies and contingencies, or similar factors prevailed during the period under consideration which might make it suitable or unsuitable as a reference point for the future. If some "normal" or "representative" period is to be the base, this might well be quite different from the combination of accidental decisions and policies which, in total, constituted the preceding fiscal period.

In analyzing base-year considerations, many factors must be weighed, including the following:

• Does the accounting method (e.g., accrual, cash, modified accrual*) provide a true picture of fiscal activities, or does it tend to report relatively higher disbursements than receipts (as might be the case with the modified accrual basis of accounting)?

• Do the accounting records accurately and comprehensively record payables and receivables so that the full scope of activities is included in the reference period?

• Have any special economic upturns, one-time federal reimbursement policies, multi-fiscal period reimbursements, or similar windfalls artificially inflated receipts? (And likewise, have downturns in the economy or unusual losses deflated receipts in a nonrepresentative manner?)

• Has the state been giving adequate support to its pension funds, prescribed debt reserves, capital maintenance, and similar responsibilities (which all too often are postponed but will eventually have to be made good)?

• Have changes in regional characteristics (e.g., influx of retirees, discovery of new mineral resources, development of new industrial enterprises) occurred, or are they clearly in the process of occurring, so that demands for services and available fiscal resources may well be significantly different from the reference fiscal period?

Several states, notably Michigan and Oregon, use more than one year as the base period in an apparent effort to smooth out single year peculiarities;

*Modified accrual refers to a system of accounting where expenditures are charged as they are incurred but cash is accounted for only when it is received.

however, without additional analysis it is doubtful that this is a completely satisfactory technique. As is stressed throughout this report, every significant factor in the process of gaining control over costs and revenues should be subjected to intensive study and evaluation before being incorporated in any state's particular version of a TEL.

Fund Structures

Based on the language used in the legislation, no state attempts to limit all disbursements or revenues, though several come very close—for example, Michigan, Missouri, New Jersey and Oregon. Most states restrict the limits (again, with exclusions) to the "general fund." This brings into focus the complexities of fund structures that control the disposition and uses of all state and local expenditures. The general fund is usually the principal means state and local governments have of providing basic governmental services. It is the principal source of revenues for the operating departments of government, and most state and local budgets in fact do no more than provide for the receipts and disbursements of the general fund.

Seldom does the general fund actually handle more than half of the moneys received and disbursed by a state government as a whole. A recent study in one major state determined that the general fund accounted for approximately one-third of the receipts and disbursements recorded by the accounting office, and this is not an unusual case. Under these conditions, a limitation dealing only with the general fund may seem to be ignoring the bulk of state costs; however, a close look at the nature and purposes of other funds may be reassuring. For example, several funds clearly do not lend themselves to this type of limitation:

- **Debt Service.** Moneys placed in these funds are generally pledged to the retirement of existing obligations.
- **Enterprises.** Both state and local governments are responsible for operations which "sell" services and products to those who choose to buy them (e.g., special recreational facilities, water and electric utilities).
- **Trust and Agency.** Large sums of money pass into and out of special funds which are handled by the state acting as a trustee or agent for individuals or organizations (e.g., contributions to retirement funds, endowment funds).

These are only a few of the examples in which tax and expenditure limitations would be of dubious value in checking rising taxes and the continued

growth of government. In fact, it is often doubtful whether these types of funds can legally be limited in this manner.

As in the case of selecting a suitable base year, a hard look must be taken at the fund structure of each particular state and local government considering the imposition of these types of limits. Sweeping inclusions of revenues and expenditures without careful attention to sources and purposes may turn out to be completely unsuitable, or actually illegal, in application.

Revenues vs. Expenditures

The term "tax and expenditure limitations" implies a significant dichotomy that should be taken into account by those considering such legislation. In fact, Proposition 13 was a limitation on one source of taxation—the property tax. Polls taken before and after this referendum in California indicate that most people were not greatly dissatisfied with the types and quality of services they received, but they hated the property tax, believed it could be reduced, and were convinced that local governments could absorb this loss of revenue without serious cutbacks or deterioration in services.[6] Responses to polls consistently indicated that there was a popular belief that governments were wasteful, inefficient and unproductive.[7] Proposition 13 was seen as one way to make government officials start shaping up. The accuracy or fallacy of these beliefs have yet to be proven because of the support the state of California has been able to provide from existing surpluses.

Limiting a particular source of revenue such as property tax is relatively straightforward and effective, insofar as reducing that source of revenue is concerned. Limiting revenues at the state level is another matter, since most of these resources, particularly sales and income taxes, are highly elastic with respect to the economy. At the beginning of a fiscal period, a budget-maker can only speculate what the economy will provide in revenue through an 8 percent sales tax or a 10 percent tax on earnings above $20,000. Unless it is made impossible for the state to realize a surplus by conservative budgetary estimates, the limitation is not likely to be meaningful. For example, Louisiana uses a formula by which the same percentage of personal income is taken from taxpayers each year. Any surplus resulting from unusually favorable economic developments must be deposited in a special fund for tax rebates. While this does entail a certain amount of expense to establish the machinery for calculating and making

the rebates, it is an assurance to taxpayers that, in total, this group will pay only a limited amount. The state of Missouri has similar rebate provisions.

None of the state-level revenue limitations has yet been subjected to a comprehensive and objective study. In fact, most of these laws have been enacted so recently that impact studies would be impossible as of the beginning of 1981. However, problems inherent in the revenue limitation formulas are fairly obvious. In an arrangement like that of Louisiana, for instance, the tax rebate formula will provide a serious challenge to financial analysts if equity is to be preserved. Receipts to the general fund of the state may well be from a combination of income tax, sales tax and a mixture of fees and charges. Revenues to this fund are fungible, and any surplus will be difficult to attribute to any one source of revenue. While rebates to payers of income tax (higher income people) would be a relatively simple undertaking, refunds to the payers of sales taxes (which include most of the population) will be difficult in the extreme unless purely arbitrary allocations are made. If not handled with great care and technical sophistication, rebate systems could exacerbate the inequities (to the extent they exist) inherent in the present systems of state governments.

Aside from these technical difficulties, revenue limitations obviously have only an indirect impact on expenditures unless a balanced budget is required. In that case, the formula imposed, especially during periods of recession, could force restraints on the normal level of state spending. On the other hand, in practice, it is possible for a formula such as that set forth in Louisiana (and several other states) to provide a sizable margin for additional expenditures for the state government.

Most TEL states place their limitation on expenditures. This is a more direct control, because appropriations can be fixed during the budgetary process with a much higher degree of certainty than is the case with attempts to curtail revenues. However, even expenditures cannot be limited strictly since many types of expenditures (e.g., welfare-related categories) are triggered by changes in economic conditions during the year regardless of the amounts of the original appropriations.

The advocates of revenue limitations wish to assure taxpayers that only a given amount of their money will be taken, and the advocates of expenditure controls are telling the taxpayer that governmental administrators are going to have to operate within tightly defined fiscal parameters. However, how "tight" these constraints are is subject to question. Virtually all the expenditure restrictions apply only to general fund appropriations, a condition which usually leaves most expenditures outside the limit. In addition,

several states do not include federal funds within the limits (Hawaii, Louisiana, Michigan, Missouri, New Jersey, Tennessee, Utah), and other states set forth additional exclusions, especially the cost of debt retirement.

An additional problem with expenditure limitations is that they are limited in application to the appropriation process; however, in practice, original levels of appropriations all too often bear very limited relationship to the actual patterns of disbursements during the year. Unless accounting methods, budgetary controls, and executive/legislative oversight are adequate, the apparently tight limitations set forth by the budget could be lost during the ensuing year.

An interesting feature of TELs is that, if undertaken with adequate analytical care, they pose a challenge to the entire system of financial management. Expenditure limitations in a budget mean very little if there is no adequate system of budgetary control and administration or if the competence of management throughout the system is substandard. The drafters of TEL legislation should realize that the statutory provisions may constitute little more than statements of intent unless steps are taken to provide the administrative and fiscal infrastructure necessary to implement them.

Experience has shown that neither revenue nor expenditure limitations can assure improved efficiency or increased productivity in governmental operations. Cutbacks in available revenues or authorized levels of spending may simply result in proportionate (or worse) reductions in the quality or quantity of services. This may lead to cheaper government, but it does not necessarily assure better, or even adequate, government. Without accompanying improvements in organizational structure, executive direction, administrative procedures and controls, and means of accountability, neither type of limitation will achieve improved government. Regardless of the approach used in the development of limitations the continued capacity to meet obligations to the citizenry must be the ultimate goal.

For the drafters of TEL legislation, the overall objectives being sought should be articulated clearly at the outset and the program designed accordingly (or dropped altogether if a TEL clearly is not suited to the objectives). A TEL may lighten the load on the taxpayer, or at least give him or her that feeling; however, it is only one factor among many in any program to develop more efficient and effective governmental operations.

Scope of Limitations

Any attempt to limit *all* expenditures or revenues of government is certain to fail for the many legal and practical reasons already presented in the discussion of fund structures. As was noted, most of the limitations apply only to the general fund, and exceptions often are made even from those. A complete list of these exceptions for state TELs is presented in the chart at the conclusion of this report.

Beyond the legal limitations on dealing with trust funds and earmarked revenues of various types, the following are some of the sources of revenue that pose special problems to the framers of TEL legislation:

- **Federal Assistance.** Few states want to discourage the receipt and use of these funds, and the matching requirements and associated mandates require types and levels of disbursements the state might not ordinarily undertake during a period of austerity. Arizona, Louisiana, Missouri and New Jersey are examples of states that exclude these funds from the limitations.
- **Dedicated Funds.** Receipts from fuel taxes (usually dedicated to highway maintenance), tolls or similarly earmarked receipts obviously are already limited in application.
- **Self-Supporting Enterprises.** For those services that are supported entirely by fees, as is the case with most government-owned public utilities, a spending limit may simply deny people a service for which they are willing to pay; however, the trend to transfer vital services (e.g., garbage collection, police protection) from a tax- to a fee-supported basis can be very inequitable with respect to the poor and people on fixed, tight incomes.
- **Pensions.** Many state and local pension funds are in such bad shape that their conditions have sometimes been regarded as a serious national problem.[8] Any overall limitation that ignores this continuing condition in a state with this problem may well be fiscally irresponsible.
- **Debt Service.** Debt which has been properly approved constitutes an obligation that legally and morally must be met. Inclusion of these expenditures within the limitation can have repercussions on the bond market and can also act to encourage a government to delay undertaking necessary capital maintenance and initiating important projects during periods in which such delays can be extremely costly.
- **Bond Funds.** Directly related to debt service is the question of whether receipts from the sales of bonds should be excluded from the limit. Again, steps which discourage the timely building of necessary facilities or adequate maintenance of existing facilities can be very costly in the long run.

On the other hand, every effort must be made to discourage the use of these funds for operating purposes.

• **Local Assistance.** Where state-collected taxes are distributed to local units of government (including schools), the question arises as to where the limitations (if any) should be imposed. If the state collects the funds on behalf of the local governments, as with proportions of the sales or income taxes in some states, then state-imposed limits are of dubious propriety unless the entire arrangement is reexamined.

These are some of the more obvious problems inherent in imposing truly comprehensive limitations on revenues or expenditures. As has been stressed repeatedly, the ultimate objectives of the limitation process must be articulated in advance or the inclusion within the limits of certain types of expenditures or revenues may defeat these purposes and prove extremely costly in the long run.

Methods of Control

Most states with TELs have sought to relate expenditures and revenues to some index of the apparent ability of the taxpayers to support operations. By and large, some form of index is used to warrant increases in expenditures proportionate to increases in personal income (or another surrogate for "the economy"). The general problems associated with the application of indexes to a given base period were discussed earlier. At this point, attention will be given to some specific arrangements which have been made and their principal implications.

Every state has taken its own approach to the development of a formula for tying costs to ability to pay. Any categorization of these approaches is a risky matter since the classifications are really in the eye of the beholder. From the perspective of this report, however, the 18 states appear to fall into the following five categories:

• Expenditures Related to Personal Income. Growth in expenditures is related to increases (or the rate of increases) in personal income in Arizona, Hawaii, Idaho, New Jersey, Oregon, South Carolina, Tennessee, Texas and Utah.

• Revenues Related to Personal Income. Revenues are limited by the level of personal income in Louisiana, Michigan, Missouri and Washington.

• Combined Cost-of-Living and Demographic Formula. Formulas combining increases in the cost of living with changes in population are used in California and Nevada.

• Expenditures Tied to Revenue Estimates. Expenditures are limited to 98 percent of estimated general fund revenue in Delaware.

• Expenditures Limited by a Flat Rate. Expenditures are limited to a flat percentage over the previous year's expenditures in Colorado and Rhode Island (though the latter is only a suggested limitation which is not binding on the legislature).

As can be seen in Appendix I, the actual formulas in use are more complicated than the above indicates, and there are usually exceptions to the prescribed limitations. While nearly half of the states with TELs relate increases in expenditures to increases in personal income (the first option listed above), none of them is exactly alike. In fact, no two states have adopted the same methods; however, the net results, for most practical purposes, are probably the same in all states except Nevada, California, Delaware, Colorado and Rhode Island. Nevada and California are very concerned about coping with continuing growth. Delaware and Colorado seem determined to tie themselves tightly to current levels of expenditures. Rhode Island has not actually committed itself to any limitation, though an 8 percent increase in the budget is given to the governor as a guideline.

For the drafters of new TEL legislation, there is no clear pattern among the states which have already taken this step. Unfortunately, very little has been done to evaluate the results of these various approaches. Most are too new to have established track records, and several states have been hit so hard by the recession that revenues have not reached the legislative limitations. Under these circumstances, each state will have to rely heavily on its own theoretical analysis to establish the approach best suited to its objectives.

Provisions for Exceptional Circumstances

Every state that has its TEL embodied in its constitution has an explicit arrangement for an emergency override. Most of the statutory states, such as Colorado, Idaho, Louisiana, Nevada, Oregon, Rhode Island and South Carolina, do not make such provisions; however, their limitations can be changed in the course of the normal legislative process. Presumably, the same perceived pressures that lead to limitations tend to impose conditions that make escape from these conditions more difficult than passage of the average piece of legislation. Thus, Arizona, Hawaii, Michigan, Missouri,

Utah and Washington all require a two-thirds vote of both houses of the legislature (though some additional conditions must also be met in several instances) to override the limitation, and New Jersey requires all exceptions to be approved by a majority of the voters in a referendum.

While the governor of Michigan and the legislatures of Missouri, Utah and Washington must declare an emergency as a condition of override, many states leave the entire process up to whatever circumstances arise. It does not appear that any state with a TEL has defined just what constitutes an emergency.

The recognition that exceptional circumstances threatening the health, safety or welfare of the people may arise which warrant taxation or spending without preconceived limitations poses at least a theoretical challenge to the entire concept of a TEL. Obviously, a state legislature must be able to meet the vital needs of its citizens to the extent its powers and resources permit. A TEL seems to say that these needs can be met only up to a certain point which is related to the apparent ability of the citizens to afford this service—except, of course, when emergencies arise. However, state and local governments are in business to deal with emergency conditions all the time. Staff and facilities are always available to deal with fires, crimes, riots, natural disasters, severe economic developments, sickness, epidemics, threats to the environment and many other adversities. The vast system of regulations imposed and enforced by state and local governments is designed to avoid many of these emergencies. Facilities such as modern highways, hospitals, fire stations, civil defense shelters and street lights also work as preventives to accidents and threats of calamity.

Under these circumstances, if a TEL is to be imposed, there must be an assumption of the adequacy of the standing machinery of government and the associated capital infrastructure with respect to some preconceived level or range of emergencies. Presumably, something like an occasional outbreak of flu could be handled routinely, but a devastating epidemic would require extra manpower, facilities, supplies and other costly actions. Storms, riots or similar misfortunes that cannot be anticipated when budgets are formulated can be provided for by override provisions to TELs. However, the fact that these unusual conditions almost invariably arise with little or no warning and pose serious threats to the lives and health of the citizens would seem to require governmental machinery ready, willing and able to respond quickly and adequately. Some might well feel, as appears from news reports following any disaster, that the true test of the worth of government is its ability to respond in exactly these situations.

Under the conditions of most current TELs, it is exactly at the point of the unusual or extreme emergency, when the resources of the state under normal conditions are inadequate, that additional resources can be provided only if an emergency is somehow declared and two-thirds of both houses of the legislature (or three-fifths in Delaware or a referendum in New Jersey) agree. The danger of delay in these instances is manifest; yet a relatively small minority of the legislature (in most cases just one-third of the members of just one of the houses) may effectively block action at the time when the overwhelming majority of the people and the legislators might be convinced that action is essential.

In practice, the situation may be even more difficult than first appears. Major floods, epidemics or similar calamities almost certainly would elicit an appropriate response with reasonable speed (though not necessarily as fast as the victims might like); however, it is the borderline case that may well pose the most serious headaches and lead to delays in undertaking appropriate preventive actions. Thus, unusual or less-than-overwhelming economic downturns could lead to the need for exceptional, but not drastic, increases in public assistance and economic development. Could the need for such tempered action overcome the likely objectives of enough legislators to get the necessary programs under way? Much the same thing could be said about incremental deteriorations in the environment, correctional systems, hospital and health facilities and services, or the educational system. At what points do adverse trends or conditions merit "emergency" status so that overwhelming majorities can be raised to meet them?

For the drafters of TEL legislation, these are serious and extremely difficult problems with which to deal. It does not appear that any of the existing legislation is this finely tuned, and it may well be that it is impossible to strike exactly the right balance. Certainly, setting forth override provisions that are so easy to invoke that the limitation is worthless, or establishing barriers to effective action when action is most sorely needed, provides alternatives that are not attractive to anyone. Nonetheless, it is exactly in this middle ground that the challenges to the development of reasonable and effective limitations rest historically.

Limitations on Local Governments

This report does not review the policy implications of actions local governments have taken to limit their own activities or of popularly initiated efforts by referendum to place limitations on costs or revenues at the local level. Thus, movements that truly emulate Proposition 13 are not included here, though they may be alluded to for limited purposes as examples. Most states traditionally have imposed limitations on local governments with respect to various aspects of property taxation. In recent years, state governments have imposed new forms of limitations which relate to all or most local expenditures or revenues. These trends have profound implications for the future of state-local relations and should be considered by drafters of TEL legislation.

Before going into the specific steps that have been taken in several states, a brief look should be taken at the nature of "local governments" and the roles they play in the intergovernmental system. Overall, our system of government has always been torn by centrifugal and centripetal forces. For example, while it is well understood that local governments are creatures of the state, forces for home rule have succeeded in establishing rights for local governments which often provide a high degree of independence from their state governments. In deciding whether to impose new limitations on local governments with respect to their powers of taxation and expenditure, many state governments must contend with the provisions of special charters and provisions in their constitutions which limit their powers to make these demands.

Beyond the legalities, however, lie the complexities of applying any blanket limitations. The brief observations which follow should be kept in mind if such steps are contemplated:

- **Education**. School districts nationally have a long-standing tradition of local control, and today they are faced with special problems of tax equity and nondiscrimination which are court-imposed, highly controversial and costly to solve. Additional TEL-type limitations, which neglect the special difficulties of many school districts, can only exacerbate already difficult situations.

- **Municipalities**. Even within the boundaries of a single state (especially the larger, more urbanized ones), municipal governments present a maze of variations in powers, services, forms of government, organizational arrangements, and methods of financing. General municipal laws that establish different classes of municipal governments are often supplemented

by special charters. General, across-the-board limitations can have widely varying impact on these jurisdictions and may well serve to place the large urban areas, contending with the ravages of crime, poverty and other socioeconomic problems, in very difficult positions.

• **Counties.** In general, the powers and duties of county governments vary from being full-fledged urban governments (as with Nassau County, N.Y.) to little more than geographical designations (as with Connecticut counties, just across Long Island Sound). In most states with large urban concentrations that still rely on the county form of government for basic services, bridging the gaps between urban and rural counties is extremely difficult. These differences pose additional difficulties to the imposition of local TELs.

• **Special Districts.** These districts continue to comprise the majority of "governments" in the United States, and it has been fashionable for a number of years to decry their continued existence and, in some cases, proliferation. Nonetheless, they are part of the local government scene and are often virtually the only practical means of dealing with large-scale, specialized, multijurisdictional problems such as water supply, sewage disposal, regional parks, port facilities, river improvements and environmental controls. Generalized limitations must be imposed here only with great caution and careful consideration of the nature of services each district is designed to provide.

Further complicating this difficult situation is the fact that it is often virtually impossible to get accurate, detailed information concerning economic activities in particular communities or governmental regions. Few states (if any) have undertaken economic base studies of each of the principal economic regions within their borders. The federal government maintains its economic data by the types of regions that suit its analytical needs. Thus, attempting to tie a municipal government's revenues or expenditures to cost-of-living data for its area could prove to be an arbitrary exercise, and apparently no state has tried to do this. This leaves the state with much less refined tools to use when it chooses to apply TEL-type limitations locally, as will be seen below.

For more than a century, state-imposed limitations on property taxes have been commonplace in the United States. Thirty-eight states now have millage limits, either set forth as mills or as dollars of taxation per hundred dollars of assessed valuation. Of the 12 that do not, half are the New England states (Connecticut, Maine, Massachusetts, New Hampshire, Vermont and Rhode Island). The variations in the imposition, levels, techni-

ques of assessment and collection practices are exceedingly complex and are beyond the scope of this report except for noting the precedents they establish for state involvement in the limitation process at the local levels of government. In addition, considering the commonplace, almost universal nature of these types of controls, it is surprising that Proposition 13 received the attention and had the impact it did. By contrast, the passage of Proposition 4 in California in November 1979 received much less nationwide attention, though it tied the growth of state and local appropriations financed by taxation to increases in the cost of living and changes in population—a much more novel and far-reaching change than that imposed by Proposition 13.

The general public may not be as interested in comprehensive controls over expenditures as it is in slashing attacks on the hated property tax. In furtherance of this mood, in the last half of the 1970s, 19 states added overall collection limitations to existing millage limitations. As was the case with state TELs, these new limits included arrangements that tied increases in revenues to increases in the cost of living (Michigan), fixed percentage increases over previous years (Arizona, Colorado, Florida, Indiana, Iowa, Massachusetts, Oregon and Washington), a fixed percentage of the value of the property (Alabama, California and Idaho), a fixed percentage increase over the previous year plus allowance for population growth (Minnesota and Nebraska), a percentage growth equal to the percentage growth of statewide equalized valuation (Wisconsin), or a formula designed to disallow revenue growth due solely to inflationary factors (Kansas and Ohio). Nevada has placed special controls on school districts which recognize both enrollment growth and a five-year average of the consumer price index. Interestingly, a constitutional amendment ratified by the voters of Alabama adds to other limits the restriction that "all taxable property shall be forever taxed at the same rate." Clearly, property taxes will continue to be the target of limitation movements for some time to come with little objection on the part of the public.

It is at least questionable whether these added property tax controls will have long-term significance except to the extent that local governments shift their dependence on revenues to other sources or that service responsibilities are shifted to other jurisdictions—probably from the local to the state levels, in many instances. When only one or a few sources of income are restricted, successful efforts have been made in the past to get around them, as is shown in Appendix II. The use of special districts for this purpose has been common for at least 75 years. Proposition 13 has had limited impact

on the operations of California's local governments because the state has been in a position to provide relief almost to the same extent that property tax revenues have been reduced, and this relief apparently will continue on a reduced scale until June 1981.[9] In fact, most municipal governments in the United States have depended on property taxes to a much lesser extent since World War II than before. All the trends are toward restricting the use of this source of revenue, and the process of restructuring state and local responsibilities and revenue configurations promises much more profound long-range changes than the current limitations themselves.

An indication of the new approaches to local limitations is seen in the eight states that have imposed tax and revenue limitations on their local governments. Given the additional sources of revenues (especially sales and some form of wage tax) and the lessening dependence of local jurisdictions on property tax, any effective attempts to limit local costs will have to be more inclusive than in the past; and, as these eight states demonstrate, they are more comprehensive:

- Arizona requires counties, cities and towns to hold public hearings as a condition of any increase in expenditures over the previous year; and in no event (except a state-certified emergency) can the budget or levy increase by more than 10 percent.
- California limits increases in total annual appropriations to increases in the cost of living and growth of population.
- Kansas places a limit on educational operating expenses per pupil of 16 percent more than the previous year's budgeted amount, or to 6 percent of median budget per pupil in the 1978-79 school year, whichever is less.
- Massachusetts, for the years 1980 and 1981, limits local government units to 104 percent of their 1979 appropriations and property tax levy. (Note: Massachusetts does not have millage limitations, so this is the only restraint on local spending and taxation.)
- Nebraska limits the combined receipts of local governments to a 7 percent increase over the prior year, and additional increases may be added that are proportionate to increases in the population.
- Nevada limits local appropriations to those of the 1978-79 fiscal year, with increases permitted for growth in population plus 80 percent of the previous five years' average change in the national consumer price index.
- New Jersey limits increases for municipalities to 5 percent of the prior year's tax levy and increases for school districts to approximately three-fourths of the annual increase in the value of real estate (though this differs from one school district to another to some degree).

• Utah limits increases in revenue to local governments to 90 percent of the state's per capita personal income growth plus an allowance for population growth.

As can be seen, all of these limitations dodge the tough problems posed by limited local economic data by not tying local appropriations to changes in *local* economic conditions. Where economic data are used at all, state or national indexes serve as surrogates for the local economy in spite of the very difficult problems such generalized standards may pose for the affected jurisdictions. Clearly, in many of these states the differences in general wealth and the economic bases that distinguish one jurisdiction from another may leave the more impoverished communities in very straitened circumstances. An overall imposition of this type poses serious questions of equity among communities. In addition, in California, Proposition 4 spending limits now overlap the earlier Proposition 13 limits on property taxes which, in turn, overlap a myriad of traditional millage limitations. When these layers of conditions are then applied to the overlapping spending and taxation practices of cities, counties, school districts and other layers of government in any one area, the prospects for the taxpayer are bewildering. Even more important, the development of an equitable revenue system throughout the entire state will be extremely difficult.

When anticipating future efforts of state governments to control and limit the overall expenditure and revenue patterns of local governments, a profound look must be taken at current notions of home rule. Just as each of the 18 states has taken its own route to establishing TELs, it is reasonable to expect that local units of government within any given state will have varied requirements if they are to meet the special needs of their citizens under the prevailing socioeconomic conditions. The extreme variations in missions, scope of operations and other administrative conditions of these governments have already been emphasized by way of stressing the dangers inherent in using the designation "local" as the basis for imposing standard, undifferentiated fiscal limitations. The impact of a 4 percent limitation on any increase in expenditures, for example, may have profoundly different effects on a county, municipality and school district serving exactly the same group of citizens. The use of base fiscal periods by no means indicates each of these entities is starting from the same point of need, service levels, or fiscal resources since any one year is the result of a long history of plans, operations, changing service demands, governing policies, referendums and similar factors in each and every jurisdiction. The complexity of this problem is reflected, in part, by the differences

represented in the approaches of each one of the states that have imposed such limitations.

In addition to overlapping governmental structures, wide variances in the conditions from one locality to the next within a state, and the absence of accurate, local economic data, TELs for local governments have exactly the same range of problems with economic indexes, base years, scope of coverage, method of control, and similar matters which have been discussed above with respect to the TELs states have imposed upon themselves. These local governments have similar types of fund structures, use federal funds (with matching requirements and mandates), operate self-supporting enterprises, have pension problems (except where pensions are included in the state systems), and borrow money and retire debt. To the extent that state governments have difficulty coping with these problems in developing effective overall limitations at their own level, caution should be exercised in treating local units in generalized, undifferentiated ways.

Evaluating Results

Sponsors of limitation proposals obviously seek effective means of curbing the rate of increase in governmental costs. These objectives, however, are not always clearly enunciated. Especially since the adoption of Proposition 13 in California, leaders of the tax revolt have made sweeping claims for the value of limitations as restrictions on expenditures and revenues. These claims include predictions that the costs of government will plummet and that a new mind-set on the part of governmental officials at all levels will sensitize them to the needs of the beleaguered taxpayer. Certainly the activities of the past two years have resulted in an increase in awareness by government officials and the public of the rising costs of government, especially at the state and local levels. As indicated earlier in this report, virtually every state has dealt with limitation proposals during the past few years.

Beyond these generalizations, however, it is difficult to provide much objective information concerning the efficacy of existing TELs. The earliest limitation at the state level (the level with which this report is most concerned) was passed by statute in New Jersey in 1976; however, most of this activity has occurred since 1978 when Tennessee adopted a constitutional amendment to limit expenditures. Of 18 states with TELs, only seven enacted the statutes or constitutional provisions before 1979. Any statistical analysis of governmental tax and expenditure policies will require several years' experience. Presumably such studies would include incidence of tax policies, changes in quality and quantity of services, adjustments in intergovernmental patterns of responsibility and authority, development of improved administrative procedures, and changes in taxpayers' attitudes. Unfortunately, at this time, there is little upon which the analyst can rely.

In the process of writing this report, a telephone survey was made of the seven states which passed their limitations before 1979 (New Jersey, Colorado, Tennessee, Arizona, Hawaii, Michigan and Texas). Only one of these, New Jersey, has undertaken any formal study of the results of its

limitations. Three states (Hawaii, Michigan and Texas) indicated that it is too soon to determine any results at all. Three other states (Tennessee, Colorado and Arizona) indicated that because of revenue shortfalls, their limitations have not been reached. In fact, all of the seven states have been able to operate well within their limitations due to adverse economic conditions during the past two years. There has not been an instance in which the emergency override provisions came into play, so this feature of the limitations could not be evaluated.

New Jersey's statute is extremely complicated and relates as much to local taxation as it does to state activities. As a result, its evaluation concentrated principally on the results of using revenue from the state income tax to provide property tax relief at the local level. The study did not result in unequivocal conclusions concerning the efficacy of these limitations at any level of government. It was perceived that expenditures at the state level were somewhat stabilized.

In general, state officials have found that imposed limits have provided adequate margins for normal operations under prevailing economic conditions. There was no indication that the limitations should be dropped or changed significantly at this time. However, no state has been put to a test because of emergencies or the types of economic conditions that would challenge the assumptions upon which the limitations are based. On balance, it is just too soon to reach conclusions.

Notes

1. Editorial, *Taxing and Spending*, October/November 1978, p. 5.
2. State public interest groups have released a number of publications concerning tax and expenditure limitations, including the following: The Council of State Governments, *Limiting State Taxes and Expenditures*, November 1978; National Governors' Association, *Tax and Expenditure Limitations, 1978*, December 1978; National Conference of State Legislatures, *A Legislator's Guide to State Tax and Spending Limits*, March 1979.
3. Frank Levy, "On Understanding Proposition 13," *The Public Interest*, Summer 1979.
4. Donald G. Hagman, "Proposition 13: A Prostitution of Conservative Principles," *Tax Review*, September 1978, p. 39.
5. The clearest statement of this principle is to be found in the "Petition of Right," Third Parliament of Charles I, May 1628, which laid the basis for Parliament's undeviating demand that only it could authorize taxes.
6. Education Finance Center, *Public Opinion and Proposition 13*, Education Commission of the States, Denver, Colo., February 1979.

7. National Governors' Association, *State Tax Policy*, 1979, p. 14.
8. U.S. General Accounting Office, Comptroller General, *Funding of State and Local Government Pension Plans: A National Problem*, Aug. 30, 1979.
9. Winnifred M. Austermann and Dan Pilcher, "The Tax Revolt Transformed," *State Legislatures*, July-August 1980, p. 32.

Appendix I

LIMITS ON STATE EXPENDITURES AND REVENUES:
A REVIEW OF THE GENERAL PROVISIONS AS OF OCTOBER 1980

State Year-Basis Application	*Method of control*	*Scope*	*Provisions for waiver*
Arizona 1978—C Expenditures	Limits state expenditures to 7 percent of the personal income of residents. A committee establishes the level of income to be used as the index.	Includes all tax funds appropriated by legislature.	To override provisions requires two-thirds approval of both houses of the legislature.
California 1979—C Expenditures	Limits increases in state appropriations to changes in cost of living and the level of population. Revenues exceeding this amount must be offset by changes in the tax schedules over the ensuing two years.	Excludes approximately 60 percent of state expenditures—debt service, federal court mandates, tax refunds, various insurance funds.	An override permitted; however, extra costs must be compensated for by reduced expenditures in the three ensuing years. Voters also can vote an increase, but this approval is operative for only four years.
Colorado 1977—S Expenditures	Limits General Fund spending to 7 percent of the preceding year. Any receipts exceeding this limit by 4 percent must be used for tax relief.	Applies to all General Fund appropriations.	No special provisions; however, statute can be amended at any time.
Delaware 1980—C Expenditures	Limits General Fund appropriations to a maximum of 98 percent of estimated revenue for that year. Excess revenue goes to a reserve account which cannot accumulate to more than 5 percent of estimated General Fund revenue.	Applies to all General Fund appropriations.	Upon approval of 60 percent of each house voting, the additional 2 percent may be used in an emergency, or the reserve fund balance may be so utilized.

Hawaii 1978—C Expenditures	Limits increases in General Fund expenditures to the estimated rate of growth of the state's economy [in practice, state personal income is the index]. If General Fund surplus exceeds 5 percent of revenue two consecutive years, tax refunds or credits must be provided.	Applies to all General Fund expenditures except those using federal funds.	Upon the governor recommending a definite amount required, a two-thirds vote of each house may approve.
Idaho 1980—S Expenditures	Limits General Fund expenditures to 5-1/3 percent of total state personal income.	Applies to all General Fund expenditures.	Statute can be amended at any time.
Louisiana 1979—S Revenues	Limits state revenues to a percentage applied to current state personal income. The percentage is derived by dividing FY 78-79 revenues by 1977 state personal income. Excess revenues are deposited in a surplus fund which can only be used for tax refunds.	There are numerous exclusions, including federal funds, severance taxes, utility income.	No special provisions; however, statute can be amended at any time.
Michigan 1978—C Revenues	Limits state revenues to a ratio (derived by dividing state revenue received in the prior fiscal year by state personal income the year before that) applied to state personal income reported during the prior year. [Note: In deriving the ratio, a three-year average of personal income may be substituted for the prior year if it will result in a higher percentage.]	Federal funds are not included in the calculations of state revenues. In addition, the cost of general obligation debt service and loans to school districts are excluded.	Upon declaration of an emergency by the governor, and designation of amount required and method of funding, may be approved by a two-thirds vote of each house.

Missouri 1980—C Revenues	Limits state revenues to a ratio (derived by dividing state revenues in FY 81 by state personal income in calendar year 1979) applied to personal income in the calendar year prior to the year of appropriations. [Note: In determining personal income, a three-year average may be substituted if it results in a greater amount than the one-year level.]	Neither federal funds nor revenues raised to retire voter-approved debt are included in the revenue limitation.	Governor must request legislature declare an emergency and indicate the reasons and the amount required to meet it. In 1981-82, a simple majority of both houses is required. In subsequent years, a two-thirds vote of each house will be required. If revenues exceed limit by 1 percent or more, they must be used as refunds to income taxpayers.
Nevada 1979—S Expenditures	Limits executive budgetary requests (not legislative action) to the rate of inflation and population growth using the biennium 1975-77 as the base fiscal period.	Applies to all appropriations included in the budget request.	Legislature is not limited.
New Jersey 1976—S Expenditures	Limits expenditures for state operations and capital outlays to increases in state per capita income as measured between the second quarters of the preceding two years.	Excluded are appropriations supported by state aid to local governments, federal assistance, and retirement of debt authorized by referendums.	Limit can be exceeded only if approved by the majority of voters in a statewide referendum.
Oregon 1979—S Expenditures	Limits expenditures to the rate of growth of state personal income for the preceding two years. If revenues exceed limit by more than 2 percent, they must be used as refunds to corporate and personal income taxpayers.	Excluded are debt service and appropriations for tax relief.	Statute may be amended at any time.

Rhode Island 1977—S Expenditures	Suggests that the governor limit his budget request to an 8 percent increase over the preceding year's appropriations.	Applies to all General Fund appropriations.	Statute can be amended at any time.
South Carolina 1980—S Expenditures	Limits increases in state expenditures over the preceding year to the growth of personal income averaged over the preceding three years.	Applies to all state expenditures.	Statute can be amended at any time.
Tennessee 1978—C Expenditures	Limits the growth of appropriations financed by tax revenues to the growth in the state's economy. In practice, the increase in personal income is used as the index.	Applies only to appropriations funded by tax revenues.	Legislature can approve a specific act by majority vote delineating exact amount required.
Texas 1978—C Expenditures	Limits growth in state appropriations to the growth of the state's economy. In practice, growth in state personal income is used as the index.	Excludes revenues dedicated by the state constitution.	Legislature may find an emergency and authorize a specific amount by majority vote.
Utah 1979—S Expenditures	Limits increases in appropriations to 85 percent of the increase in state personal income.	Exclusions include federal funds, debt service, and user charges.	Upon declaration of an emergency by the legislature, the limit can be overridden by a two-thirds vote of each house.
Washington 1979—S Revenues	Limits tax revenues to the rate of increase in state personal income as averaged over the preceding three years. Any excess receipts become part of the tax revenue for the next year.	Applies to all state tax revenues.	Upon declaration of an emergency by the legislature, a specified amount may be approved by a two-thirds vote of each house.

Appendix II
Historical Perspective

Tax limitations have a long history in America, and anyone proposing these types of constraints would do well to review past efforts. This special section seeks to highlight conditions and public actions in the past which many people today seem to feel are unique to the present.

Proposition 13

In spite of the attention it received, Proposition 13 was directed toward a very limited objective—reduction of property taxes. The proposition was aimed only at this one source of revenue at the local level of government. The proposition had the following principal provisions:

(1) It limited real property taxes to 1 percent of market value—a step designed to cut revenues from this source by more than half.

(2) It set assessable "market value" at that established during the 1975-76 fiscal year, with increases to be made in evaluations only at the time of subsequent new construction or when ownership changed hands—probably the first time in history when values were legally frozen to give preferential treatment to existing property owners over developers and new purchasers.

(3) It placed a limit on increases in assessed values of 2 percent annually, regardless of actual market values.

(4) It prohibited increases in other taxes to offset property tax reductions unless such increases are endorsed by two-thirds of all members of both houses of the state legislature or by two-thirds of those eligible to vote at the local level at a referendum.

Proposition 13 was unique only in its severity and the amount of publicity it received. It was the result of an interesting set of circumstances that bear inspection. Per capita taxes in California increased overall by 151 percent from 1969 through 1978—a lower rate of increase than state and local taxes nationally. However, local governments in California were heavily dependent on the property tax. For example, in 1976, property tax in California was $64 per $1,000 of personal income, compared to a national average of $45. In addition, California communities were very aggressive in reevaluating property. Given the spectacular increases in housing prices in California during the 1970s, local governments were able to reap large

dividends in additional receipts while keeping tax rates fairly steady. For the average homeowner who held on to his property and depended on a regular salary, this tax on unearned income became burdensome to the point of intolerability.[1] It is well recognized that property tax is the most unpopular tax nationally, and these circumstances were greatly exacerbated in California. It is little wonder Proposition 13 passed by such a large margin. In many ways, this was a special case.

Early American Concerns

A brief look at the long history of limits on taxation in the United States will help place the California experience in perspective. Since the basic purpose of this report is to provide policy guidance to state legislators considering the adoption of some form of TEL, this retrospective necessarily will be selective and brief; however, it will serve to demonstrate the difficulties inherent historically in the use of statutory and constitutional limits to control spending.

In New York state, the Constitutional Convention of 1846 was concerned with "evidence of local graft, corruption and extravagance." The Convention amended the Constitution to make it the duty of the Legislature "to restrict" the local power to tax and borrow "so as to prevent abuses." In the following years, the New York Legislature set up boards to oversee local expenditures, required submissions to the state of local budgets for review, and established a 2 percent real estate tax limitation on New York City. It was subsequently determined that all of these actions "failed to eliminate or substantially reduce the incidence of graft, corruption and extravagance." As a result, in 1884, a new constitutional provision placed a limit of 2 percent of assessed value (real and personal) on taxes throughout the state, and these limitations were tightened further in 1938.[2] As will be seen, none of these actions achieved the desired results.

New York was not unique in its problems and concerns. Especially after the Civil War, there was a boom in the activities of Northern cities in terms of capital improvements and services. Costs-per-capita for governmental operations soared, and a great deal of debt was incurred. Much of this was "floating debt," carried forward from year to year, to pay for current operating expenses. As the prominent urban historian Ernest S. Griffith explains, "In 1872-73 this had gone so far in Chicago that its tax levies went mostly for interest on the debt and redemption of the scrip."[3]

The "extravagance, overoptimism, and dubious and corrupt decisions" that characterized many state and local governmental activities after the Civil War received a severe jolt with the crash of 1873. This financial panic was a serious blow to every city government in the nation—especially the cities of the South. As a consequence of economic conditions, Pensacola, Fla.; Memphis, Tenn.; Fayetteville, Ark.; Mobile, Ala.; Duluth, Minn.; Elizabeth, N.J.; and a number of other smaller cities forfeited their charters. Selma, Ala., had its charter annulled by the governor, and Nashville's fiscal affairs went into the hands of a receiver. So serious was the situation overall, writes Griffith, that: "During the decade, it was estimated that one-fifth of the total municipal debt at one time or another was at least technically in arrears in interest, and much was in actual default."[4]

The 1873 crash led to demands from many quarters for more economical government by making it "impossible to spend more or to incur a greater debt." These demands led, in the 1870s, to "charter, statutory, or constitutional tax and debt limits." In most instances, limitations on taxes were based upon a percentage of the assessed valuation of property. As a result of these developments, by 1880, 10 states had such limitations, and by 1901, two-thirds of the cities had tax limits. It should be noted that: "One-half of the cities with a legal tax limit taxed up to the limit."[5] This latter observation is interesting because it is often contended that "limits" in fact constitute "floors" for revenue estimation purposes in many jurisdictions today.

With the imposition of these types of limitations on property taxes, cities started looking for alternative sources of revenues; however, they could not easily continue use of debt because: "By 1880, more than half of the states had constitutional limitations of city debt in one form or another."[6] Other methods were pursued. Increased use of charges and fees for services became commonplace. Chicago found itself in a very difficult situation by the turn of the century and began turning to the use of special districts with independent taxing and borrowing powers as a device for getting around restrictions on the city's taxing and borrowing powers. This approach became so popular throughout the nation that these types of districts are far more numerous today than any other form of local government in the United States.

Largely as a result of these pressures to avoid limitations, the reforms of the late nineteenth century, which sought economy in government, did not produce the desired results. As Griffith notes: "A great majority of states

continued to employ such tax and debt limits, even though these were impaired or even failing for a number of reasons." For example, a special legislative committee in Massachusetts in 1912-13 concluded that both tax and debt limits were failures, and generally resulted in bond issues for current expenses. In 1913, limits were removed on all local governments in Massachusetts other than Boston.[7]

A number of different devices were being used to control expenditures during the first two decades of the twentieth century. By 1920, several states based tax limitations on the taxes or tax rates of the previous year, varying from the same to 110 percent. As seen in this report, these controls were virtually identical to those imposed by several states in the late 1970s. Indiana was one of these earlier states. In addition to normal limitations, it also established a State Tax Commission to review and, if possible, reduce local budgets. It went through a stormy period between 1919 and 1921 but stayed in business until 1937.

Following World War I, there was much discouragement among reformers about the effectiveness of tax and debt limitations. In 1920 in New York state, the Davenport Committee issued a report that included these observations:

> . . . there is no way in a democracy of blocking a genuine popular demand for increased governmental service through an arbitrary limitation on the tax levy. The only effective method of securing reduction of tax levies lies along the line of centering full responsibility upon a single elected official through (a) a comprehensive budget, (b) a sound bonding act, (c) a wide distribution of the direct tax burden.[8]

Expenditure constraints during the 1920s were not limited to tax and debt limitations. Oregon tried expenditure constraints in the early 1920s whereby a "limitation was fixed at 106 percent of the previous year unless the voters approved an increase above this figure." Interestingly, in 1979 Oregon passed a statute which limits increases in appropriations to the growth in state personal income. Two other states (Colorado and Rhode Island) in 1977 tied increases in appropriations to fixed percentages over the previous year's appropriations.

Modern Developments

Beyond the use of tax and debt limitations, it is difficult to compare governments in the 1870s with those in the 1970s. Griffith makes this very important observation in this respect: "No city in 1880 even approached the

imagination and concern for all its citizens that constitute the standards accepted for the American cities of the 1970s."[9] This statement could be extended to all levels of government. Indeed, it is this concern for all citizens that characterizes much of the reason for the modern levels of governmental costs.

As has been seen, people were concerned with extravagant government throughout the nineteenth century; however, the total burden of governmental costs was far below what it has been in modern times. The Tax Foundation recently summarized current trends. In 1950, expenditures for all governments were $70.3 billion—8.4 percent of the 1979 level of $830 billion. Federal expenditures increased from $44.8 billion in 1950 to $531.8 billion in 1979, or 1,087 percent, while state and local expenditures increased from $25.5 billion in 1950 to $297.8 billion in 1979, or 1,069 percent. Of course, for a true comparison, these data should be changed to constant dollars, a step which would reduce the disparity; however, the gross scope of the change in a period of less than 20 years is startling.[10]

A great deal of attention has been given in recent years to the apparently extraordinary increases in state and local expenditures. Between 1968 and 1978, general tax collections (excluding unemployment insurance) increased by nearly 187 percent. During this same period, the nation's population increased by only 9 percent, consumer prices by 88 percent, and personal income by 151 percent. In fact, also during this period, federal tax collections increased by 161 percent—26 percent less than the state and local increases. On the other hand, the Foundation points out the following:

> In the last four years, from 1975 to 1979, Federal spending growth has outpaced that of state and local governments by a significant margin. Federal spending has increased at the rate of 11.8 percent annually, 50 percent faster than the 7.9 percent annual growth in state-local spending.[11]

Some of the reasons for these increases become more apparent in another Tax Foundation report which cites the following conditions with which modern governments are faced:

> . . . from 1950 to 1978 the number of persons aged 65 and over, together with the number of persons of school and college age (5 to 24 years) increased by more than 42 million, or 72 percent. Population in the remaining ages rose by only 24 million, or 26 percent. . . . The 65-and-over age group gained 12 million persons, or a 94 percent increase. For the school-age group, the rise was 31 million, or 66 percent.[12]

As the Foundation went on to observe, "These two age groups traditionally are major beneficiaries of government programs." For example, major programs for the elderly (e.g., OASI, railroad retirement, public employee retirement, Supplemental Security Income, old age assistance, hospital and

medical insurance, and Medicaid) increased from $3.26 billion in 1950 to $152.7 billion in 1978, while public education costs increased from $7 billion in 1950 to $103.1 billion in 1978. Nor should it be forgotten that these are only two types of social programs underwritten by American governments. Since 1950, equally impressive increases could be cited in such programs as housing, welfare and health.

The principal point in this brief review is to stress the fact that increases in governmental costs in modern times have not been due to the "graft, corruption and extravagance" that worried the delegates to New York's 1846 Constitutional Convention. The reasons for these increases today are tied to an infinitely intricate web of socioeconomic and demographic circumstances largely beyond the control of governmental officials. The people demand (as do their representatives in local, state and federal governments) that the ravages of poverty and old age be ameliorated, that excellent educational resources be provided to our youth, and that governments otherwise provide for safe and healthy communities. As the 1920 New York Davenport Committee said, given these "popular demands," increased governmental services (and associated costs) are inevitable.

It would be improper to conclude from this summary of pressures for higher levels of governmental costs that limitations on state and local expenditures are useless and a waste of time to impose. In the absence of significant economic changes, sudden increases or decreases in population, or other factors which tend to put unusual strains on the availability of revenue or the demands for services, these types of limitations clearly do influence the decisions of executives and legislators in state and local governments. Budget directors routinely use the prescribed limitations to determine total available resources or expenditure limits, and these constraints are cited constantly in negotiations with governmental employee representatives. Without these limitations over the years, governmental costs undoubtedly would have increased significantly more than they did.

On the other hand, history has shown that significant socioeconomic developments and unremitting demands for increased or improved services will result in the limitations either being changed or avoided in some way. Modern adaptations of these types of limitations attempt to provide for some flexibility in the traditional system. The nature of these new efforts has been the subject of this report. In the years to come, everyone concerned with the costs of government will be watching them, and their successes and failures will continue to be the subjects of studies and reports.

Notes

1. C. Lowell Harriss, "Property Taxation after the California Vote," *Tax Review*, August 1978, p. 35.

2. State of New York, Temporary State Commission on the Constitutional Convention, *Local Finance*, Volume 3 (New York: Temporary State Commission on the Constitutional Convention, 1967), p. 48.

3. Ernest S. Griffith, *A History of American City Government, 1870-1900* (New York: Praeger Publishers, 1974), p. 15.

4. Ibid., p. 5.

5. Ibid., p. 230.

6. Ibid., p. 21.

7. Ernest S. Griffith, *A History of American City Government, 1900-1920* (New York: Praeger Publishers, 1974), p. 179.

8. Ibid., p. 180.

9. Griffith, *American City Government, 1870-1900*, p. 22.

10. Tax Foundation, *Monthly Tax Features*, August 1979, p. 1.

11. Ibid.

12. Tax Foundation, *Monthly Tax Features*, November-December 1979, p. 1.

Appendix III

The following is a list of knowledgeable officials in the 18 states with tax and expenditure limitations. This list is current as of January 1981.

ARIZONA
Hank Reardon
Joint Legislative Budget Committee
1812 W. Monroe, Room 201
Phoenix, AZ 85007
602-255-3042

CALIFORNIA
Bion Gregory
State Legislative Counsel
3021 State Capitol
Sacramento, CA 95814
961-445-3057

COLORADO
Douglas G. Brown, Director
Legislative Drafting Office
Room 30, State Capitol
Denver, CO 80203
303-866-2045

DELAWARE
Nathan Hayward III
Office of Management, Budget
and Planning
Townsend Building, 3rd Floor
P.O. Box 1401
Dover, DE 19901
302-736-4271

HAWAII
Rick Kahle
Legislative Bureau
Rm. 004, State Capitol
Honolulu, HI 96813
808-548-6237

IDAHO
Myron H. Schlechte, Director
Legislative Council
Rm. 334, State Capitol
Boise, ID 83720
208-334-2475

LOUISIANA
Donald Vandal
Deputy Legislative Fiscal Officer
Legislative Fiscal Office
P.O. Box 44097, Capitol Station
Baton Rouge, LA 70804
504-342-7233

MICHIGAN
Douglas C. Drake, Co-Director
House Democratic Research Staff
Office of the Speaker
State Capitol
Lansing, MI 48909
517-373-8615

MISSOURI
Frank M. Masters, Director
Committee on Legislative Research
Rm. 117-A, Capitol Building
Jefferson City, MO 65101
314-751-4223

NEVADA
Ron Sparks, Director
Legislative Fiscal Division
or
Dan Miles, Deputy Fiscal Analyst
Assembly Taxation Committee
Rm. 341, Legislative Building
Carson City, NV 89710
702-885-5640

NEW JERSEY
Maurice Shier
609-292-8872
or
Larry Levit
609-292-8254
Office of Legislative Services
Rm. 232, State House
Trenton, NJ 08625

OREGON
Richard Munn
Legislative Revenue Office
Rm. 140, State Capitol
Salem, OR 97310
503-378-8873

RHODE ISLAND
James F. Mahoney
House Finance Commission
Rm. 306, State House
Providence, RI 02903
402-277-2738

SOUTH CAROLINA
Robert Heilman
Chief Staff Attorney
Legislative Council
P.O. Box 11417
Columbia, SC 29211
803-758-2334

TENNESSEE
Don Borton
Fisal Review Committee
G-19 War Memorial Building
Nashville, TN 37219
615-741-2564

TEXAS
Tom Keel, Director
Legislative Budget Board
P.O. Box 12666, Capitol Station
Austin, TX 78711
512-475-3426

UTAH
Melvin Leslie
Legislative General Counsel
Rm. 403, State Capitol Building
Salt Lake City, UT 84114
801-533-6581

WASHINGTON
Greg Pierce
House Revenue Committee
Rm. 213, House Office Building
Olympia, WA 98504
206-753-3962

31-01LH

STATE OF ALASKA

THE LEGISLATURE

BUDGET AND AUDIT COMMITTEE

AUDIT DIVISION
POUCH W—ALASKA OFFICE BUILDING

FINANCE DIVISION
POUCH WF—STATE CAPITOL

JUNEAU 99801

M E M O R A N D U M

SUBJECT: ANALYSIS OF DEFENDANTS' MEMORANDUM -
WHO MAY EXPEND FEDERAL AND OTHER UNAPPROPRIATED FUNDS?

Defendants claim (pages 18 through 20) that "no appropriation is required to expend funds received 'in trust' for specific purposes." In support of this, they open with an obscure reference from the Alaska Constitution, Article IX, Section 13: "No money shall [with certain exceptions] be withdrawn from the treasury except in accordance with appropriations made by law."

Taking Article IX, FINANCE AND TAXATION, as a whole, we find there are several powers granted or denied that have specific exception language attached. For example, Section 1, TAXING POWER, provides that the power to tax shall never be surrendered "except as provided in this article." Section 7, DEDICATED FUNDS, provides that the proceeds of any state tax or license shall not be dedicated to any special purpose "except when required by the federal government for state participation in federal programs." Section 8, STATE DEBT, provides that no state debt shall be contracted "unless authorized by law for capital improvements and ratified by a majority of the qualified voters". The section continues by authorizing emergency debt "for the purpose of repelling invasion, suppressing insurrection, defending the State in war, meeting natural disasters. . . ." Section 11, EXCEPTIONS. The restrictions on contracting state debt are waived for "debt incurred through the issuance of revenue bonds by a public

enterprise or public corporation". They are further waived for "indebtedness to be paid from special assessments on the benefitted property "and for" refunding indebtedness of the state. . . ." Even Section 13, EXPENDITURES, contains exceptions. It says that no money shall be withdrawn from the treasury "except in accordance with appropriations made by law." It continues, "no obligation for the payment of money shall be incurred except as authorized by law." Does it not seem logical to assume that had the framers of the Alaska Constitution intended to insert the underscored phrase, "No money shall, with certain exceptions, be withdrawn from the treasury except in accordance with appropriations made by law", they could and would have done so? To further substantiate this point, Mr. Leslie Nerland, Chairman of the Constitutional Convention Committee on Finance and Taxation, explained on the floor his committee's thinking on a proposed amendment to the section dealing with dedicated funds:

> "The Committee felt that in inserting the word 'public' after 'all', making it 'all public revenues' would eliminate the question regarding such things as donations or bequests by private individuals that might have specific purposes attached to them."

As stated, this language was proposed for the section on dedicated funds, but it clearly indicates that the Committee on Finance and Taxation had considered differentiating between "public revenues" and "other revenues", the latter specifically described as "donations or bequests by private individuals".

The report of the Committee on Finance and Taxation (attached in full), in the commentary on the proposed section restricting the earmarking of revenues (Sec. 8, p. 11) provides:

"The allocation of certain revenues to special purposes is prohibited, with two exceptions:

(1) If required in order to participate in a federal program, or [emphasis added]

(2) If the earmarking is in existence at the time of ratification of the Constitution."

Again, it seems logical to assume that if the framers of the Alaska Constitution had intended to exempt from appropriation federal and other funds--be they now called "trust funds", "custodial funds", "contractual arrangements", or other similar names--they would have specifically provided for such a by-passing of the appropriations process.

Since the Constitution makes no provision for special classes of money to bypass the appropriation process, (this is emphasized in Article IX, Section 12. BUDGET. "The governor shall submit to the legislature. . .a budget for the next fiscal year setting forth all proposed expenditures and anticipated income of all departments, offices, and agencies in the state. The governor, at the same time, shall submit a general appropriation bill to authorize the proposed expenditures. . . .") how have federal and other program receipts been appropriated since statehood? The procedures are summarized in defendants' memorandum, pages 2 through 4.

From 1963 through 1970, "federal program receipts or other program receipts" received during the year and not otherwise appropriated were made available for expenditure by "budget amendment approved by the Governor". In other words, the Legislature in each General Appropriation Act granted the Governor open-ended authority to receive and expend any amounts of federal or other program receipts that the state could get its hands on. Beginning with the 1971

General Appropriations Act, the Legislature has continued to require that budget amendments for receipt and expenditure of "additional federal or other program receipts" be approved by both the Governor and the Legislative Budget and Audit Committee. Thus, prior to 1971, with the apparent exception of the first two years of statehood, the Governor has not received nor expended federal or other program receipts "except in accordance with appropriations made by law"; nor, with the exception of certain amounts "processed inadvertently" early this fiscal year, has he since.

The defendants argue that by virtue of some implied executive authority or non-statutorily defined receipt categories the Governor should be allowed to receive and expend substantial sums of money without legislative review and approval. This is an interesting concept when viewed in relation to certain other powers and restrictions granted by the Constitution. Article XII, Section 11, discusses law-making powers. It ends with the sentence, "Unless clearly inapplicable, the law-making powers assigned to the legislature may be exercised by the people through the initiative. . . ."

Article XI, Section 1, provides that the people may enact laws by initiative and approve or reject actions of the legislature by referendum. But, Section 7, RESTRICTIONS, provides, "The initiative shall not be used to dedicate revenues, <u>make or repeal appropriations</u>. . . . The referendum shall not be applied to dedications of revenue, to <u>appropriations</u>. . . ." [emphasis added]

Are we now to assume that powers denied the people to make or repeal appropriations by initiative/referendum--appropriation powers specifically provided by Article IX, Section 13, to be "made by law"--are to be given by summary judgment to the Governor?

SUMMARY OF SJR 4 --
CONSTITUTIONAL AMENDMENT ON SPENDING LIMITATIONS

The expenditure limitation proposed by Governor Hammond will constitutionally limit the growth in appropriations of state funds to a rate determined by inflation and population growth. Inflation will be measured by the increase in the consumer price index for the preceding calendar year and population growth will be an annual average calculated from federal censuses or renumerations. These two measures of growth will allow the state to keep up with increasing cost factors, while constraining growth within reasonable and responsible bounds.

Certain exceptions are allowed to provide for particular requirements and circumstances which relate to the Alaska situation. These exceptions are listed below:

1. Contributions to the Permanent Fund (the state's savings account).

2. Payments of the Permanent Fund Dividend (the public's return on those savings).

3. Appropriations to loan funds, provided that any loan subsidies are appropriated and are constrained by the spending limit.

4. Appropriations for capital improvements approved by the voters.

5. Appropriations to repay outstanding general obligation debt of the state.

6. Appropriations to a disaster reserve account (rainy-day account).

7. Appropriations funded through increased user fees.

8. Appropriations required by court orders or federal transfer of functions to state government.

9. Appropriations funded by one-quarter of the earnings which result from extra contributions to the Permanent Fund, i.e., contributions in excess of those required by the Constitution.

10. Appropriations for natural disasters. This includes reserve funds from the account referred to in 6. above. Such appropriations would require a gubernatorial declaration of disaster, passage by a two-thirds majority of membership of each house, and approval by the Governor.

If this proposal is passed by the Legislature, it will go on the 1982 general election ballot and would, if approved by voters, be effective for the fiscal year 1984 budget.

1 IN THE SENATE — BY THE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

2 SPONSOR SUBSTITUTE FOR

3 SENATE JOINT RESOLUTION NO. 4

4 IN THE LEGISLATURE OF THE STATE OF ALASKA

5 TWELFTH LEGISLATURE - FIRST SESSION

6 Proposing an amendment to the Constitu-
7 tion of the State of Alaska relating to
8 limitations on appropriations of state
9 money.

10 BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

11 * Section 1. Article IX of the Constitution of the State of Alaska is
12 amended by adding new sections to read:

13 SECTION 16. APPROPRIATION LIMITATIONS. The amount of State money
14 The governor may request or the legislature may appropriate during a
15 fiscal year shall not exceed the amount of $2.5 billion for the base
16 fiscal year of 1982 by more than the cumulative increase in the federal
17 consumer price index for the State for the calendar years preceding the
18 governor's submission of the budget under section 12 of this article
19 plus or minus a percentage equal to the cumulative average yearly
20 growth or loss in the State's population as shown by the last two
21 federal censuses or renumerations. Money appropriated under any excep-
22 tion prescribed by section 17 of this article shall not be included in
23 the base for determining the allowable increase from year to year.

24 SECTION 17. EXCEPTIONS FROM APPROPRIATION LIMITATIONS. The limi-
25 tations on increases in appropriations do not apply to money received
26 in trust for a specific purpose; to appropriations of money to be
27 deposited in the permanent fund; money appropriated to pay permanent
28 fund dividends; money appropriated to capitalize loan funds, but only
29 if the money to subsidize these loans at below market interest rates is

appropriated separately under the limitations; money appropriated to construct capital improvements, whether of bond proceeds or otherwise, where the appropriation for the capital improvements is approved by the voters; money appropriated to escrow accounts or otherwise to repay general obligation bonds; money appropriated as a reserve for disasters of natural or human origin or other emergencies; money appropriated to coincide with increases in user fees; money appropriated to meet increases in costs to the State resulting from court orders or a transfer of authority or responsibility to the State from the federal government; money derived from one-quarter of the income from those contributions made to the permanent fund which exceed the minimum required by this constitution; or money appropriated by a vote of two-thirds of the membership of each house and approved by the governor to meet disasters of natural or human origin which are declared by the governor.

* Sec. 2. The amendment proposed by this resolution shall be placed before the voters of the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska, and the election laws of the state.

Original sponsor: Rules/Governor

Offered: 5/5/81
Referred: Finance

1 IN THE SENATE BY THE JUDICIARY COMMITTEE

2 CS FOR SENATE JOINT RESOLUTION NO. 4 (Judiciary)

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 TWELFTH LEGISLATURE - FIRST SESSION

5 Proposing an amendment to the Constitu-
6 tion of the State of Alaska relating to
7 limitations on appropriations of state
8 money.

9 BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. Article IX of the Constitution of the State of Alaska is
11 amended by adding new sections to read:

12 SECTION 16. APPROPRIATION LIMITATIONS. The amount of State money
13 requested by the governor and appropriated by the legislature during a
14 fiscal year shall not exceed the amount appropriated in the preceding
15 fiscal year by more than the increase in the federal consumer price
16 index for the state for the calendar year preceding the governor's
17 submission of the budget under section 12 of this article plus a per-
18 centage equal to the average yearly growth in the State's population as
19 shown by the last two federal censuses or renumerations. Money appro-
20 priated under any exemption prescribed by section 17 of this article
21 shall not be included in the base for determining the allowable increase
22 from year to year.

23 SECTION 17. EXEMPTIONS FROM APPROPRIATION LIMITATIONS. The limi-
24 tations on increases in appropriations do not apply to appropriations
25 of money to be deposited in the permanent fund; money appropriated to
26 pay permanent fund dividends; money appropriated to capitalize loan
27 funds, but the money to subsidize low interest loans must be appro-
28 priated separately and is subject to the limitations; money appropriated
29 to construct capital improvements, whether of bond proceeds or other-

wise, where the appropriation for the capital improvements is approved by the voters; money appropriated to escrow accounts or otherwise to repay general obligation bonds; money appropriated as a reserve for disasters of natural or human origin or other emergencies; money appropriated to coincide with increases in user fees; money appropriated to meet increases in costs to the State resulting from court orders or a transfer of authority or responsibility to the State from the federal government; money derived from one-quarter of the income from those contributions made to the permanent fund which exceed the minimum required by this constitution; or money appropriated by a vote of two-thirds of the membership of each house and approved by the governor to meet disasters of natural or human origin which are declared by the governor.

* Sec. 2. The amendment proposed by this resolution shall be placed before the voters of the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska, and the election laws of the state.

Introduced: 1/13/81
Referred: Community & Regional Affairs and Finance

1 IN THE SENATE BY COLLETTA

2 SENATE JOINT RESOLUTION NO. 3

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 TWELFTH LEGISLATURE - FIRST SESSION

5 Proposing an amendment to the Consti-
6 tution of the State of Alaska relat-
7 ing to limiting increases in expendi-
8 tures and requiring payment by the
9 state of mandated increased expendi-
10 tures of a political subdivision of
11 the state.

12 BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

13 * Section 1. Article IX, Constitution of the State of Alaska is amended
14 by adding new sections to read:

15 SECTION 16. APPROPRIATION GROWTH LIMIT. In no year shall the
16 rate of growth of appropriations from state revenues, excepting appropria-
17 tions to the permanent fund established in Section 15 of this article
18 and excepting appropriations for capital improvements, exceed the esti-
19 mated rate of growth of the economy of the State as determined by law.
20 An appropriation in excess of this limit shall not be made unless a
21 state of emergency is declared to exist, as provided by law. The
22 appropriation limit for each of the three years following the
23 declaration of emergency shall be adjusted equally so that the total
24 appropriations for the year of the emergency and the succeeding three
25 years do not exceed the appropriations which could have been made under
26 this section if no emergency had been declared. The limit on rate of
27 growth of appropriations for each year shall be calculated without
28 regard to a declared emergency or the subsequent three-year adjustment.

29 SECTION 17. RETURN OF REVENUES TO TAXPAYERS. Revenues received

1 by the State in excess of the amount appropriated in compliance with
2 this article during a fiscal year shall be distributed to the taxpayers
3 of the State as provided by law. No appropriation is required for a
4 distribution under this section within the succeeding fiscal year.
5 * Sec. 2. Article II, Constitution of the State of Alaska is amended by
6 adding a new section to read:
7 SECTION 22. INCREASED COSTS TO POLITICAL SUBDIVISIONS. No general
8 law requiring increased expenditures by a political subdivision shall
9 become effective unless the legislature has provided that the State pay
10 the amount of increased cost to the political subdivision.
11 * Sec. 3. The amendments proposed by this resolution shall be placed
12 before the voters of the state at the next general election in conformity
13 with art. XIII, sec. 1, Constitution of the State of Alaska, and the
14 election laws of the state.
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Introduced: 2/4/81
Referred: Finance and Judiciary

BY THE RULES COMMITTEE BY REQUEST OF THE GOVERNOR

1 IN THE HOUSE

2 HOUSE JOINT RESOLUTION NO. 5

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 TWELFTH LEGISLATURE - FIRST SESSION

5 Proposing an amendment to the Constitu-
6 tion of the State of Alaska relating to
7 limitations on appropriations of state
8 money.

9 BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. Article IX of the Constitution of the State of Alaska is
11 amended by adding new sections to read:

12 SECTION 16. APPROPRIATION LIMITATIONS. The amount of State money
13 appropriated during a fiscal year shall not exceed the amount appropri-
14 ated in the preceding fiscal year by more than the increase in the fed-
15 eral consumer price index for the state for the calendar year preceding
16 the governor's submission of the budget under section 12 of this arti-
17 cle plus a percentage equal to the average yearly growth in the State's
18 population as shown by the last two federal censuses or renumerations.
19 Money appropriated under any exception prescribed by section 17 of this
20 article shall not be included in the base for determining the allowable
21 increase from year to year.

22 SECTION 17. EXCEPTIONS FROM APPROPRIATION LIMITATIONS. The limi-
23 tations on increases in appropriations do not apply to appropriations
24 of money to be deposited in the permanent fund; money appropriated to
25 pay permanent fund dividends; money appropriated to capitalize loan
26 funds, but the money to subsidize low interest loans must be appro-
27 priated separately and is subject to the limitations; money appropriated
28 to construct capital improvements, whether of bond proceeds or other-
29 wise, where the appropriation for the capital improvements is approved

by the voters; money appropriated to escrow accounts or otherwise to repay general obligation bonds; money appropriated as a reserve for disasters of natural or human origin or other emergencies; money appropriated to coincide with increases in user fees; money appropriated to meet increases in costs to the State resulting from court orders or a transfer of authority or responsibility to the State from the federal government; money derived from one-quarter of the income from those contributions made to the permanent fund which exceed the minimum required by this constitution; or money appropriated by a vote of two-thirds of the membership of each house and approved by the governor to meet disasters of natural or human origin which are declared by the governor.

* Sec. 2. The amendment proposed by this resolution shall be placed before the voters of the state at the next general election in conformity with art. XIII, sec. 1, Constitution of the State of Alaska, and the election laws of the state.

Introduced: 5/19/81
Referred: Finance and
Judiciary

1 IN THE HOUSE BY MALONE AND BEIRNE

2 HOUSE JOINT RESOLUTION NO. 57

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 TWELFTH LEGISLATURE - FIRST SESSION

5 Proposing an amendment to the Con-
6 stitution of the State of Alaska
7 relating to limitations on appropri-
8 ations of state money.

9 BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

10 * Section 1. Article IX of the Constitution of the State of Alaska is
11 amended by adding a new section to read:

12 SECTION 16. APPROPRIATION LIMITATIONS. Except for appropriations
13 to the permanent fund and appropriations required to pay the principal
14 and interest on general obligation bonds, the amount of money appro-
15 priated during a fiscal year, from whatever source and for whatever
16 purpose, shall not exceed the amount appropriated in the base fiscal
17 year by more than the cumulative increase in the federal consumer price
18 index for the State for the calendar years preceding the governor's
19 submission of the budget under Section 12 of this article plus or minus
20 a percentage equal to the cumulative average yearly growth or loss in
21 the State's population as shown by the last two federal censuses or
22 renumerations. The legislature may, by affirmative vote of two-thirds
23 of the membership of each house, make appropriations in excess of this
24 limit by enactment of appropriation bills limited to a single item of
25 appropriation for a single purpose but the excess appropriations, if
26 any, shall not be included in calculating the limit for the next fiscal
27 year. The governor shall cause any unappropriated balance to be
28 invested at market rates. The base fiscal year for purposes of this
29 section is the period from July 1, 1980 to June 30, 1981.

1 * Sec. 2. The amendment proposed by this resolution shall be placed
2 before the voters of the state at the next general election in conformity
3 with art. XIII, sec. 1, Constitution of the State of Alaska, and the election
4 laws of the state.
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Senator Arliss Sturgulewski June 4, 1981

SENATE FINANCE

EXPENDITURE LIMITATION ISSUES

WHAT SHOULD BE USED AS THE BASE?

Should we pick a FY budget? What should be exempted from the budget? Should they be the same items exempted from the ceiling or others? If the base is too low, how will agencies handle budget cutbacks? If there are few ceiling exemptions, should the base contain room for innovative new programs (Energy Center, Delta Barley, Etc.)? How will the base account for assistance/revenue sharing for local governments? Should a number be used instead of a base year to allow for adjustments of, for example, income tax refunds, etc. If so, what should the number be?

WHAT FORMULA SHOULD BE USED TO CALCULATE INCREASES?

Should the formula for calculating the increase be a cumulative index applying to a single original base, or should the formula apply as an adjustment to the previous year's actual appropriation?

Should the formula be tied to population growth as well as inflation? Are there alternative indices?

Should the formula have a factor which will reduce the real per-capita spending limit overtime (such as only using .95 of the annual CPI increase)?

WHICH APPROPRIATIONS AND EXPENDITURES SHOULD BE COVERED BY THE LIMITATION?

Should the limit apply to both state and federal funds?

Should increases in user fees be covered? If exempted, what oversight should be available to keep increases reasonable?

Most likely revenue bonds should be excluded, but should General Obligation Bonds? Bond debt service?

Should capital projects be excluded and, if so, how can we manage the operating budget impacts of capital projects?

Should loan capitalization be excluded?

There is agreement that contributions to the Permanent Fund should be excluded, but should Permanent Fund dividends? Should arrangement be made for the possibility of the State losing the law suit, if so of what sort? Should a portion of permanent fund income (or real income) be exempted? Should the Permanent Fund be the only recipient of "surplus" funds, and if so, how can this be insured?

If the base is very inclusive, then the exemptions should be very limited. If the base is restricted, what level of exemptions are reasonable?

Should provision be made for exceeding the limit? If so, should it be by legislative vote--by what majority? Should a referendum be provided for? If provision is made for exceeding the limit, what should be voted on-single appropriations or multiple ones? If provision is made for exceeding the limit, should there be a special prohibition against voting to exceed the limit on items which had previously been appropriated within the limit?

STATE OF ALASKA

THE LEGISLATURE

BUDGET AND AUDIT COMMITTEE

AUDIT DIVISION
POUCH W—ALASKA OFFICE BUILDING

FINANCE DIVISION
POUCH WF—STATE CAPITOL

JUNEAU, ALASKA 99811

May 28, 1981

To: Senator Arliss Sturgulewski
Chairman
Legislative Budget and
Audit Committee

From: Margo Waring
Senior Policy Analyst

Subject: Expenditure Limitation

You asked me to provide you with background information on expenditure limitations and specific analysis of constitutional spending limitations.

Background

Throughout the nation taxpayers are concerned about the growth of the public sector, growth that sometimes has outpaced the rate of inflation and the growth in real personal income. This concern translates into debate about the size and scope of government, efforts to increase efficiency and effectiveness of existing governmental services, and sometimes, efforts to inhibit increasing tax burdens by way of limits of the amount of revenues and, therefore, expenditures available to government. Throughout the nation, states have looked at ways to control the growth of government expenditures by curbing state taxes. Generally, this has been done by linking the amount of revenue collected to a measure of economic growth. Those who have looked at this issue use the terms "expenditure limitation" and "tax limitation" interchangeably. Hence, proponents select revenue or expenditure controls for a variety of political reasons, knowing that the same effect will be achieved. Usually, spending limit campaigns have been fought in the context of tax increases. Proponents hope not only to limit expenditures, but also to reduce taxes, permitting no real growth, or even reducing existing size of government. Thus, the availability of excess revenues is seen as inevitably leading to their expenditure: the only way to curb growth is to curb revenues and, thus, expenditures. The relationship is seen as one in which to effect any one element is to effect the others.

Alaska's Tax History

Alaska's tax history is not representative of the experience of other states. Alaskan law defines several personal and business taxes for different levels of government. Each of these has a statutorily defined ceiling. State individual income tax, set at a relatively low rate, brought funds into the state treasury which were spent on state government services, as well as for services which are generally provided at the local level, such as schools and roads. Local property taxes, relatively modest by national standards, fund a narrower range of services than elsewhere. When local governments have elected to provide services at the local level instead of having them provided by the state, these transfers of authority have been accompanied by transfers of funds with which to partially provide for the services.

Government growth, in terms of numbers of state employees and in terms of goods and services provided by the state to the citizens, has been fueled not by personal income tax or by property taxes but by corporate oil taxes, lease sale bonuses, and other forms of petroleum revenues.

As government has grown and as revenues have risen, Alaskans' response has been to cut taxes, not so that government growth will be curbed, but so that others will pay for the goods and services. Gross business receipts tax was effectively eliminated in 1978. Property tax revenues from petroleum properties were shared with local governments in 1973 and 1975. And in 1980, the individual personal income tax was eliminated. During the same year, faced with a decline in revenues from one source, but an increase in revenues from petroleum sources, the legislature significantly increased the extent of state funding to schools, capital projects, revenue sharing to local governments, and so forth. In essence, transfer payments to local governments and to private citizens (in the form of actual checks, subsidized loans, and other benefits) have increased, while non petroleum revenue sources have steadily disappeared.

Petroleum revenues, while increasing substantially over the next few years, will in about 10 years begin to decline substantially. By about 2000, revenues from Prudhoe Bay will have declined to the level of 1978 revenues. Thus, goods and services supported by petroleum revenues will be in jeopardy once petroleum revenues decline.

While some Alaskans seek to limit the growth of government for reasons of political philosophy, others seek such limitations in order to insure that future revenues will meet governmental obligations. Some Alaskans are also advocating repeal of such other non petroleum taxes as the local property tax,

shifting that burden to state revenues. Thus, expenditure limitation desires coincide with efforts to reduce taxes paid by residents of the state. If, however, the tax repeal efforts are sucessful, then state government obligations will increase by having a heavier reliance placed on petroleum revenues, even if an expenditure limitation is also enacted. It is estimated that, exclusive of further tax repeals, by FY'82, 94% of the state's revenues will come from petroleum sources of all varieties.

Alternatives

1. Both the legislature and the Governor have, in past years, sought to place a lid on annual appropriations as part of the budget process. In 1978 statutory amendments to AS 37.07.070, the legislature specified for itself an identified ceiling and early production of the budget. The Governor too has identified the administration's upper spending limit. However, these approaches have not been successful, apparently because of constituent pressures to increase governmental spending.

2. There has been discussion of either a statutorily imposed or constitutionally defined ceiling on expenditures. This approach has, apparently, been met with mixed success in other states. A bill, using Tennessee's law as a model, was introduced in the 1980 session to place a limit on expenditures. Some of the issues involved in such a limitation are: the factor on which the limit should be based, the expenditure level that should be sustained, how to avoid shifting tax burdens, what to do with excess revenues, what exemptions should be provided, how to provide for emergencies, and what budgetary items should be included under the ceiling (debt service, capital projects, operating budget, loan programs, etc.) and treatment of the surplus. Opponents have expressed concern that this approach is too inflexible to meet Alaska's needs and that our boom-burst economy is not suited to the factors proposed for defining allowable growth.

3. Since in Alaska an expenditure limitation is not a revenue limitation, other suggestions have been made that would effectively impose an expenditure limitation by reducing the amount of available revenue by not placing that revenue in the general fund. For example, if a higher percentage of all petroleum revenues were automatically to be placed in the Permanent Fund, the amount of revenues available for expenditure would be curtailed. Permanent Fund income could be placed

either in the general fund or plowed back into the Permanent Fund itself. Thus, if 100% of petroleum revenues were placed in the Permanent Fund, expenditures would be limited to recurring revenues and recurring income of the Permanent Fund.

Expenditures could also be limited by increasing the amount of funds funneled into loan programs, although there are significant concerns regarding the ability of Alaska's economy to absorb hugely increased loan funds without under-taking highly risky ventures.

Alternatively, it has been suggested that Alaska use some of its excess petroleum revenues to invest in projects of national interest and benefit, projects supportive of national economic and social goals to "prove" to national critics that Alaska is capable of wise wealth management.

4. If we desire to peg expenditures to recurring revenues, one alternative would be to increase the number and amount of recurring revenues. This is not a particularly viable alternative in Alaska, except to the extent that such revenues are corporate taxes generated by renewable resource development.

Summary

Increased government growth in Alaska has alarmed many people, especially because this growth is based on non-recurring petroleum revenues. Prudence and concern for residents who will be here in 10-15 years indicates that steps should be taken to restrain governmental expenditures to the level that can be sustained by recurring revenues. This could be accomplished by statutorily or constitutionally limiting expenditures, increasing recurring revenues, or placing non-recurring revenues in the Permanent Fund and using Permanent Fund income as a recurring revenue source.

Constitutional Limitations

For those who favor spending limitations, the focus has been on the establishment of constitutionally defined limits to the growth of the budget. While there are certain drawbacks to this approach (lack of flexibility, difficulty in establishing an adequate formula, the "log rolling" that would occur to gather enough votes for an override, etc.), Alaskans have favored this approach as one less likely to be ignored by legislators and more likely to restore "rationality" and prioritization among spending options.

Prior to discussion of the bills currently before the legislature, I will briefly summarize the key issues facing decision makers regarding constitutionally defined spending limitations.

Limitation Components

A. Spending Formula

All spending limitations consist of an expenditure base and an adjustment factor. The base is the selected budget year. Selection of the expenditure base will be a function of the year in which a constitutional limitation is approved by the voters. Delay in this regard can mean significant differences in terms of the base, as the budget has been growing by over 20% per year.

The adjustment factor is the means by which calculations of year to year changes are made. Other states have used such factors as growth in personal income or population changes or the cost of living index.

The use of growth in personal income to determine the growth rate of spending is based on the rationale that personal income is a proxy for ability and willingness to pay for government services; or, alternatively, on the belief that government spending should not become a greater proportion of total economic activity.

Use of an adjustment factor involving population growth and inflation (both of which are also reflected in changes in personal income) allows spending to expand in response to these direct cost pressures. Such a real per capita limit would over time reduce the percentage of state spending to personal income. This would occur to the extent that private economic growth exceeded population changes and inflation. It is to be expected that this formula would be more restrictive than would one depending upon changes in personal income.

Another alternative that has been suggested is to simply select a percentage of budget growth that appears reasonable. The rationale for this approach is the difficulty of finding adequate data for more complex formulae. For example, Commonwealth North and others have suggested basing the adjustment factor on the growth of the private sector in Alaska. The difficulty here would be in determining that figure, and insuring that the figure itself was not a function of state expenditure.

Coverage

A. The formulae generally apply to expenditure of general fund revenues, after exempting federal funds, and occasionally exempting certain capital expenditures and/or local government aid. In general, the more inclusive the base the more effective the limit and the fewer distortions expected in expenditure patterns. The "adjustments" which are made to such limits tend to be a redefinition of activities to fit into the allowable expenditure categories. Since in Alaska the limit impetus comes from a need to reduce rather than redirect spending, a broad limit would appear most applicable. The federal funds exemption seems to be the least damaging, although this might lead to an increased emphasis on federal, as opposed to state, priorities.

Greatest concern focuses on the possible exemption of capital spending. If capital projects are not covered by the limitation, the impact on the operating budget, new operation, maintenance and programs costs may result in either unmet obligations or a decline in funding of those programs not associated with capital facilities.

Another concern in coverage is how to insure that state expenditure burdens are not being deferred to local governments. If services now funded by the state are delegated to local governments, who pays for these services and are those costs to be included in the expenditure limitation? Similarly, the state has been increasingly funding services through grants to non-profit groups. Again, should such grants be included in an expenditure limitation? Assuming a desire to restrict expenditures, changes in service patterns should not be used as an escape valve through which expenditures in excess of the limitation may flow. Some states have specifically stated in their constitutional amendments language that requires the state to fund under the spending limitation services which are being delegated to other levels of government.

B. Escape Clauses

There are a variety of emergency override provisions contained in other states' spending limits. Over half the limits are statutory and thus may be amended through the usual legislative process. The constitutionally established limits require approval of specific excess amounts by a simple, or a strong majority (3/5 or 2/3); or, by voter approval.

Some provision must be made for unforeseen circumstances. One approach is to include two overrides: one procedure for natural disaster or other similar emergencies and another (perhaps more rigorous) procedure for simply exceeding the formula amount.

C. Treatment of Surplus

Any effort to limit state spending must include provisions for the general fund surplus.

This is probably the most crucial component of an Alaska spending limit and also that area where other states' experience offers the least guidance. Those states which address this question provide for tax rebates or reductions with some allowing for a budget stabilization or rainy day fund. Since the Alaska limit intent is to enhance the long-term fiscal security and stability of the state, it would be inappropriate to return the total unspent windfall oil revenue to individuals. Here are some other possibilities:

1. Increased contribution to the Permanent Fund. The Permanent Fund was conceived and established as a mechanism for preserving our oil wealth in income producing investments which could fund the on-going provision of traditional government services. Depending on the size of the principal and the return on investments, the income from the permanent fund could provide an important source of recurring revenues in the future as our non-recurring mineral revenues decline. One approach would be to provide for an additional contribution to the Permanent Fund of some fixed percentage of the general fund surplus, say 75%. The remainder could be allocated to a budget stabilization fund, emergency fund, or other use.

2. Endowments and a semi-permanent fund. This would involve design of a semi-permanent fund styled after the existing Permanent Fund, but from which expenditures could be made once oil revenues and Permanent Fund interest earnings are insufficient to support even the "limited" state expenditure levels. This would, in essence, be a long-term budget stabilization fund, which would be invested in income earning assets.

Endowments also offer the possibility of providing a funding source for future government services. However, unlike the more general semi-permanent fund concept, endowments, by assuring funding for such specific services as education, raise the possibility of future budget distortions and limitations on the appropriation authority of the legislature.

3. Loans. Direct loans or investments are another possibility. It is assumed that appropriation of funds to increase the capitalization of loan funds (existing or new) and appropriation of loan subsidies would both be covered by the expenditure limit. If this were not the case, the state would be in a situation similar to the recently resolved problem of the general fund balance automatically funneling into loan programs. Most of the existing loan programs are revolving funds, where repayments return to the fund to be reloaned for a similar purpose, though, due to inflation and low interest rates, the fund experiences a "declining balance" over time. Direct loans from the general fund, for industrial development or other purposes, could be designed to repay the general fund on schedules which would help offset declining oil revenues. Another possibility would be to make general fund loans to existing loan programs. This money could then be leveraged, loaned, and repaid to the general fund (i.e. would not be part of the revolving accounts).

4. "Altruistic" expenditures. The question has been raised whether some portion of currently surplus revenues should not be used in a way to furnish long-term, national benefits. Both "investments" in public and private income producing activities in the lower 48 states and contributions to medical, educational and social programs have been suggested. The important elements of such an expenditure would be potential benefits to the nation as opposed to benefits to Alaska. In considering such an approach it must be remembered that this is basically a spending option which would contribute to long-term fiscal security only in so far as to offer an offsetting advantage to the federal government.

Other Issues

In addition to the questions discussed above, there are several other issues that need to be addressed in the design of a spending limit. These are outlined briefly below.

A. Impact on State Credit Rating

If bond buyers become concerned about a spending limit affecting the ability of the state to pay its debts, this could negatively influence the State's credit rating, thus increasing the cost of borrowing. Bond repayment can be guaranteed either by granting such payments first claim on State spending (priority status) or by exempting such payments from the limit. The former method appears preferable, in that a limit exclusion would encourage bonding and discourage the careful evaluation of the impact of debt service on the State's future fiscal health.

B. Unfunded Obligations

Legislation is sometimes passed which creates programs without provisions for funding these activities. A spending limit might create an incentive to design programs without concurrent funding, thus disguising, at least temporarily, the fiscal impact of government actions. An example of such action might be the incremental funding of a large project, or the raising of unemployment benefits. Another aspect of this problem is programs which represent obligations to make future payments. Difficulties arise if these obligations (e.g., pensions or other benefits) are not adequately funded between the commitment time and the time payment is due. This problem can be avoided by the requirement that actuarily sound current appropriations be made for pensions and other future obligations.

C. Treatment of Dedicated Funds and User Charges

Alaska has certain dedicated funds, and the conclusion or exclusion of expenditures from these funds in a limit calculation must be decided. For example, it may be desirable to count expenditures from the Fish and Game Fund and Renewable Resources Funds under the limit. If these expenditures do not "count," there would be a great incentive to refinance programs from these sources rather than from the general fund.

Another consideration of this nature is the treatment of user charges. Some have argued that spending financed from such sources should be excluded from the general limit, where the purchase of such goods or services by the user is discretionary. It would be important to define carefully program receipts, since there would be pressure to inflate and extend user charges as a means of circumventing a limit. Also, since dedication of funds is constitutionally limited, such an exclusion might pose legal difficulties.

D. Mandated or Shifted Costs

Limiting the expenditures of one level of government results in an incentive to transfer expenditures to another (unlimited) government, or to mandate new functions without providing new funding. Some limits, therefore, provide that the current proportion of state expenditures going to municipalities is not to be reduced unless there is a shift of program responsibility; and, if such a shift is made, provide that the expenditure base be appropriately adjusted.

E. Effect on the Economy

Alaska's economic history is characterized by "boom and bust." Depending upon the specific formula selected in a spending limitation, there is concern that insufficient funds will be available when booms occur with their increase in population, inflation, and higher demand for government services. Similarly, when the "bust" occurs, will the formula be based on lagging data? This concern can also be stated in terms of whether the spending limitation formula will function to heat up and cool down the economy at the right or the wrong times.

Proposed Legislation

Bills have been introduced on both the House and Senate sides proposing an amendment to the State Constitution relating to limiting increases in expenditures. Copies of these resolutions are attached.

SJR 4 and CSSJR 4 (Jud)

Formula: growth in appropriations is limited to the amount of increase in the federal consumer price index for Alaska for the preceding calendar year plus "a percentage equal to the average yearly growth in the state's population as shown by the last two federal censuses or renumerations."

Base: the preceding fiscal year appropriations minus exempted expenditures. Exemptions: exempted appropriations include appropriations into the Permanent Fund, Permanent Fund dividends, loan capitalization, capital improvements approved by the voters, accounts for the repayment of general obligation bonds, reserves for disasters, increases in user fees, costs resulting from court orders or from "the transfer of authority or responsibility to the State from the federal government" and money derived from one-quarter of the income from those contributions made to the Permanent Fund which exceed the minimum required by this constitution; or money appropriated by a vote of two-thirds of the membership of each house and approved by the governor to meet disasters of natural or human origin which are declared by the governor."

HJR 4

Formula: growth in appropriations adjusted to the "rate of growth of the economy of the State as determined by law."

Base: the appropriations of the previous year, minus exemptions or appropriations for emergencies.

Exemptions: appropriations as a result of a declaration of a state of emergency.

Coverage: all appropriations except appropriations to the Permanent Fund and loans made by the State.

Other: the title declares this amendment to also require "payment by the state of mandated increased expenditures of a political subdivision of the state."

HJR 5

The same as SJR 4.

HJR 57

Rep. Malone's proposed amendment has a
Formula: cumulative increase in federal consumer price index for Alaska, plus or minus population growth or loss.
Coverage: all appropriations except to the Permanent Fund and to pay principal and interest on GBOs. Includes federal funds.
Override: to exceed the ceiling requires a two-thirds vote of both houses; appropriation bills limited to single items.
Base: FY 81, minus votes in excess of the limitation.
Other: Unappropriated balance invested at market rates.

Please let me know if you would like a more through discussion of the implications and expectatble effects of each of these bills.

SSSJR 4

BASE: 2.5 billion in FY 82
FORMULA: Cumulative increase in federal CPI for Alaska adjusted (plus or minus) for average yearly growth or loss of population. Excludes excepted appropriations.
EXCEPTIONS: Money received in trust, deposits to permanent fund, permanent fund dividends, loan fund capitalization, capital construction if approved by the voters, appropriations for escrow or other GBO debt service, disaster reserve fund, money coinciding with increased user fees, money for court ordered payments or transfer of responsibility to state from federal government, one-quarter of permanent fund income over the constitutional 25%, money approved by 2/3 of each house and the governor to meet disasters declared by the governor.

FOLLOWING IS A SUMMARY OF A PAPER BY:

Mr. John Shannon, Assistant Director of the Advisory Commission on Intergovernmental Relations (ACIR), a man knowledgeable about the experiences of other states which have sought to limit state expenditures. Mr. Shannon addresses the question of "How much state spending is enough? and how should limits be established?" Mr. Shannon says that the big problem faced by states wishing to limit expenditures is the political one: How much should legislative authority be restricted? The issue revolves around whether a simple majority, now required for spending decisions, should be replaced by an extraordinary majority (two-thirds or three-quarters). How to exceed the defined spending level has been as important as the spending level itself. The conservative view favors as a constitutional amendment that can be exceeded only by an extraordinary majority. The liberal view opposes constitutional lids, expressing a fear that when spending is slowed the poor and minorities will suffer most. ACIR takes a moderate view favoring restrictions and greater fiscal discipline, achieved through statutory rather than constitutional change and keeping the simple majority vote.

Mr Shannon states that, after the political issue, the next most important issue is the economic one: Should spending be allowed to go at a faster, slower or the same pace as the state economy? Different states have favored each of these approaches. Mr. Shannon thinks that if Alaska moves to a constitutional lid, the citizens might favor permitting a small amount of per capita real growth in spending because of the fast growth rate of the State and its relative state of early development.

Mr. Shannon identifies two secondary issues. Most local governments have feared that spending limits will adversely affect them. To allay that fear, most states have specified that the state must reimburse local governments for any additional cost mandates, thereby preventing states from shifting responsibilities to local governments without providing adequate funds at the same time. One state has specified that local government receipts could not be reduced. The other issue is what to exclude from a spending lid. Usually states exclude debt service, federal receipts and capital expenditures.

In summary, Mr. Shannon says that, "The task of slowing down or limiting State government expenditures in Alaska will be far more difficult than in any other state in the union for three reasons." In other states the slowdown demand is usually associated with increasing tax burdens. "In Alaska the consideration of a spending slowdown is taking place when real tax burdens are rapidly declining." In all other states, the demand for a showdown has come from the people; only then are leaders willing to build greater fiscal discipline into systems. "In Alaska the demand for effective expenditure lids must come from the leaders, because they alone have responsibility for making sound plans for the future." In other states the "challenge is to hold the pain of taxation down to tolerable levels. Ironically, in Alaska the challege is to maintain at least a semblance of general taxation so that the State does not become completely addicted to the painless taxation of the oil industry."

ADVISORY

COMMISSION ON INTERGOVERNMENTAL RELATIONS

WASHINGTON DC 20575

SLOWING DOWN THE GROWTH OF STATE AND LOCAL EXPENDITURES

Outline of Paper

by

John Shannon, Assistant Director
Advisory Commission on Intergovernmental Relations

and

Robert Lucke, Fellow
Advisory Commission on Intergovernmental Relations

Anchorage, Alaska
September 18, 1980

If a recent report in the New York Times is correct, Alaska is moving into a fiscal Nirvana. The massive growth in your "exportable" oil taxes will permit Alaska to repeal virtually all of the major taxes paid by its residents, to increase state expenditures, and to build up a great reserve for the lean years when the oil reserves are depleted.

The amount that Alaska can set aside for the lean years ahead and for economic development will depend on the degree of spending discipline that can be built into your state and local fiscal system. The need for discipline is especially acute for this state because the rapid growth of "easy tax revenue" is bound to cause the rapid growth of new and expanded expenditure programs. Your situation calls to mind the wisdom of Parkinson's Second Law--"expenditures rise to meet revenues and to exceed them."

Ironically, while growing fiscal affluence has caused increased concern for spending lids in this state, growing fiscal austerity has spurred the demand for an expenditure slowdown in most of the other 49 states. While clearly recognizing the uniqueness of your fortunate position, it may be helpful to trace out the way other states are trying to build greater fiscal discipline into their systems.

This paper, therefore, will analyze: (1) the recent and fairly significant slowdown in the rate of state and local spending in the United States and (2) the key issues involved in any attempt to put a lid on state spending.

PART I: THE GREAT SLOWDOWN IN STATE AND LOCAL SPENDING

A. The Change in Spending Rates

Between 1955 and 1976, the state and local public sector experienced fast growth--expanding at almost twice the rate of the economy. For the last three years there has been a real slowdown as state and local spending has lagged the growth in the economy (Appendix Figure 1 and Appendix Table 1).

B. What are the Causes of This Slowdown?

1. Change in Political Attitudes--from one that either supported or tolerated fast growth to a growing demand that public spending not exceed the growth of the economy. Underpinning this changed political attitude is growing skepticism about the efficacy of public spending (Appendix Figure 2).

2. Change in the Economy--from one characterized by relatively fast growth and low rates of inflation to slow growth and fairly high rates of inflation. This change in the economy strengthens the hands of the fiscal conservatives:

   a. Because the economic pie is no longer expanding. Citizens become more concerned about the relative size of the slice taken by the public sector.

   b. A weak economy spurs growing concern about the care and treatment of the private sector--the "reindustrialization of the economy." Investment incentives for individuals and business firms become the order of the day. Kenneth Galbraith is "out"--Milton Friedman is "in."

3. Change in Demography--from one marked by steadily rising school enrollments to one of declining numbers.

   a. During the 1950s and 1960s, rising school enrollments provided the driving force behind the move to strengthen state revenue systems and to increase property taxes. During this period, 13 states enacted income taxes and 12 states adopted sales tax levies.

   b. The stabilization--if not the actual decline--of enrollments has deprived pro spending forces of one of the most effective arguments for higher taxes.

4. Change in the Fiscal Position of the Federal Government--from one of relative fiscal ease to growing stringency.

   a. In the last few years the federal government has lost three trump cards:

      (1) The Military Trump Card--During most of the post-Korean era, Congress was able to shift resources from the Pentagon to the domestic sector in general and to federal aid programs in particular. As a result, federal military outlays dropped from almost 13% of GNP in 1954 to 6.5%

by 1979. Now the pendulum is swinging the other way--the generals are back in the budgetary arena and they will undoubtedly command an increasing share of federal resources over the next five years.

(2) The Social Security Trump Card--Throughout most of the post World War II period, Congress could repeatedly raise social security tax rates with little public opposition because they were viewed as simply higher premium rates for expanded insurance coverage. Now Congress is running into increasing opposition to scheduled hikes in social security levies and general fund tax revenue will have to be used to finance expanded social security commitments. Because the social security program is the single most important federal domestic responsibility, it will move to the head of the line--well ahead of federal aid programs to states and localities.

(3) The Deficit Finance Trump Card--For 19 of the last 20 years, Congress has been able to paper over revenue shortfalls with deficit financing. Now that inflation has become one of the nation's major domestic problems it is becoming increasingly difficult for the Congress to take a relaxed view of budget deficits.

b. The aging of our population is also working against the federal government because the feds have the primary responsibility for providing income support to the elderly and also for paying for their doctor and hospital bills.

c. The federal fiscal condition is made even more difficult because of the growing demand for income tax relief for individuals and business firms to offset, partially, both inflation-induced income tax hikes and scheduled increases in the social security levy. Income tax cuts will also be urged to revive an ailing economy by providing greater incentives for private investment.

C. How Has the Slowdown Been Effected?

Four general policies have been used to effect this spending slowdown.

1. Ad Hoc Decisions--to pursue more conservative fiscal policies. This approach has probably had the most significant effect to date. This policy is pursued at the federal level by President Carter and at the state and local levels by many governors and mayors (Appendix Table 2, track II).

2. Statutory Reforms--to strengthen legislative accountability. This middle-of-the-road approach has been favored by the ACIR and many moderates. For example, it calls for indexing the income tax to prevent income tax windfalls (Appendix Table 2, track III).

3. Constitutional Spending Constraints--to slow down the growth in spending. This approach is favored by the economist, Milton Friedman (Appendix Table 2, track IV).

4. Constitutional Cut-Back Provisions--to reduce the size of government. This general policy can be labeled the Jarvis or Proposition 13 approach (Appendix Table 2, track V).

D. Is This Slowdown in State-Local Spending Likely to Persist Over the Next Five Years?

Yes, because:

1. The basic economic, demographic, and political factors that have combined to produce this slowdown are not likely to disappear. It would take a dramatic lessening of international tensions, rapid economic recovery, and a major breakthrough on the energy front.

2. The pacesetters in state-local spending during the 50s and the 60s--New York, Massachusetts, and many of the other frostbelt states--are suffering from high and rising fiscal blood pressure readings. They will be forced to cut back their tax and spending programs in an effort to become more competitive.

3. Most of the sunbelt states will probably continue to exhibit a rather conservative taste for public goods and services despite the fact that their economies will experience above average economic growth.

4. Most of the energy-rich states can also be expected to pursue fairly conservative spending policies because of the fear of the day of reckoning when the petroleum or coal reserves play out.

PART II: SPENDING LIMITATION CONSIDERATIONS: KEY ISSUES AND STATE EXPERIENCES

A. The Primary Political Issue--How tightly should legislative authority be restricted? There are three general views of legislative budgetary behavior which dictate radically different forms of restraints on government expenditures.

1. The Traditional Liberal View: This is the "Galbraithian" perspective which argues that the public sector is under-funded. Those who hold this view are fearful that a slowdown in public spending is most likely to adversely effect low income and minority groups. Thus, they oppose all proposals--statutory or constitutional--that would make it more difficult for legislative bodies to tax and to spend.

2. The New Moderate View: This school of opinion believes that government spending has increased too rapidly due largely to the shortcomings in the way legislators are held politically accountable for their tax and spending decisions. Inflation, for example, enables the income tax states and the federal government to reap a tax windfall as taxpayers are automatically pushed into higher brackets by inflation. This painless form of taxation encourages overspending in the absence of rigorous fiscal self discipline.

   Supporters of this moderate view favor reforms that strengthen fiscal discipline and accountability--primarily statutory in nature--that can be changed if necessary by the vote of a simple majority of the state's legislature.

   Even constitutional constraints that can be changed by majority vote of the legislature would fall in this moderate category. For example, Tennessee and Texas have established spending lids which tie state spending to the growth in the state economy with the proviso that the ceiling can be exceeded throught a majority vote of the legislature. Thus, the growth in the state's budget will receive greater public scrutiny than it has in the past and thereby increase a legislator's accountability for its spending decisions. However--

and this is or critical importance--this restriction does not permit a conservative minority in the legislature to exercise a veto power over spending decisions.

3. The Conservative View: This view, characterized by Milton Friedman and the "public choice" theorists, postulates that there is a fundamental defect in the democratic budget-making process which results in too large a public sector. Even in the absence of economic conditions which are condusive to expenditure growth (inflation, oil royalties), the legislature will continue to overspend because of the power of the special interests.

According to this analysis, the special interests are able to pressure legislative bodies to accept their proposals which have relatively narrow benefits, but whose costs are diffused over all taxpayers. Because the benefits to the taxpayer of opposing any specific program are small, the power of the vested interests is not counterbalanced by taxpayer concerns. In this scenario, the legislator is presumed to succumb to lobbying pressure and neglect his/her fiduciary responsibility to the state's taxpayers.

The public choice advocates argue that stringent expenditure limitations are necessary in order to control spending. Constitutional restrictions which can only be exceeded by extraordinary legislative majorities (e.g., two-thirds) are needed to protect the taxpayer and offset special interest pressures. Such extraordinary majority requirements permit a minority to veto expenditure growth, and ensure that all budget increases are the result of substantial bipartisan agreement.

Two states which have strict provisions for exceeding their caps are Arizona and New Jersey. Arizona's law is written into the Constitution and can only be exceeded by a two-thirds vote of the legislature. New Jersey, on the other hand, requires a majority vote on a referendum in order to increase the expenditure ceiling.

While these types of restrictions make it exceedingly difficult for legislatures to yield to spending pressures, they are very inflexible except in times of emergency.

The National League of Cities sums up the restrictiveness of requirements for extraordinary majorities this way:

> "In the state legislature, the use of extraordinary majority to pass new tax bills is devastating to the likelihood of passing new taxes. Although a greater-than-simple majority was required to pass appropriation bills in California, the pork barrel phenomenon of adding a little something for everyone allowed the building of a constituency. No such phenomenon allows legislatures to build support for any tax bill."1/

B. The Key Economic Issue: Should government be allowed to grow at a faster clip, the same pace, or at a slower rate than a state's economy? Depending on which measure is used as an index, an expenditure limitation law can be made more or less restrictive relative to the economy. There are basically three types of indices which have been used by states so far.

1. Least Restrictive Expenditure Limitation--Tie the growth of state spending to that of the economy (Tennessee and Hawaii). An indicator of economic activity, such as personal income, will allow a state's expenditures to vary in direct relation to population changes and real and inflationary growth. As a result, govenment spending is effectively constrained to remain a constant percentage of a state's economic well-being. Under such an expenditure ceiling, government is allowed to expand, but not at a rate faster than the economy. Essentially, this kind of indexation is consistent with the view that government is currently the "right"

1/ The National League of Cities, Tax and Expenditure Limitations: A Plea for Governmental Reform, Washington, D.C., 1978, p. 5.

size relative to the private sector and should be permitted to expand in line with society's ability-to-pay.

2. Moderately Restrictive--Limit the growth in state expenditures to changes in the cost of living and population (California and Nevada). While such a ceiling would maintain government services at the present level, this strategy would cause government expenditures to decline slowly relative to the economy. It is based on the presumption that the current level of real services is optimal and should not expand even if economic growth takes place. As a consequence, any budget proposal that seeks to increase the real per capita level of government services must withstand open debate and public review.

3. Most Restrictive--Limit expenditures to a rate of growth below that of changes in the cost of living index adjusted for population. Utah limits the rate of growth in spending to 85% of the change in personal income. Colorado has set a maximum rate of growth in spending of 7% which is currently well below the inflation rate. These types of expenditure restrictions will reduce the real level of per capita government services. Public choice adherents endorse these restrictive policies based on their proposition that the current size of government is too large and must be reduced in real terms.

C. Secondary Issues

1. Definition of the Relevant Expenditure Base. In order to make a fiscal constraint effective it is important to design it so that it is as comprehensive as possible. However, there are certain types of appropriations whose exclusion from the expenditure base should be considered.

   a. Federal Funds. Without exception, federal grants are currently excluded from expenditure ceilings imposed on states. By excluding federal transfers, the ceiling will more effectively control the percentage of the state's income allocated to government.

b. Debt Service Funds. Limitation proposals usually exclude payments for debt service from the expenditure ceilings. Where debt service payments have been included within an expenditure limit, bond repayments have first claim on state revenues in order to protect their marketability.

c. Other Exclusions. Capital and pension expenditures might be excluded from a spending limitation. Their exclusion depends in part on whether the legislature can be "trusted" not to use them to avoid hard budget decisions.

2. The Local Government Issue. Local officials are usually very fearful that a lid on state spending will adversely effect their fortunes. To allay their worst fears, the framers of state spending lids usually provide that the state must reimburse local governments for any additional costs imposed on them by state legislative mandates. The drafters of the Michigan constitutional spending lid went even farther--"The state is hereby prohibited from reducing the state financed proportion of the necessary costs of any existing activity or service required of units of local government by state law." (Section 29)

PART III: SUMMARY

The task of slowing down or limiting state government expenditure in Alaska will be far more difficult than for any other state in the union.

A. In all other states, the demand for a slowdown arises in a period of increasing tax burdens. Here in Alaska, your real tax burdens are rapidly declining.

B. In all other states, the demand for the slowdown comes from the people--only then are their leaders willing to build greater fiscal discipline into their systems. In Alaska, the demand for effective expenditure lids must come from the leadership because it alone has the responsibility for making sound plans for the future.

C. In virtually all other states, the challenge is to hold the pain of taxation to tolerable levels. In Alaska, the challenge is to maintain at least a semblance of general taxation so that the state does not become completely addicted to the "painless" taxation of oil production.

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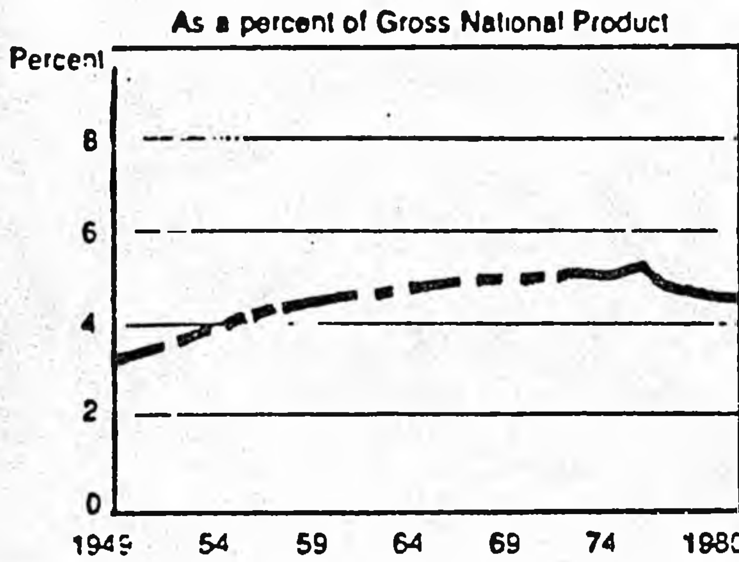
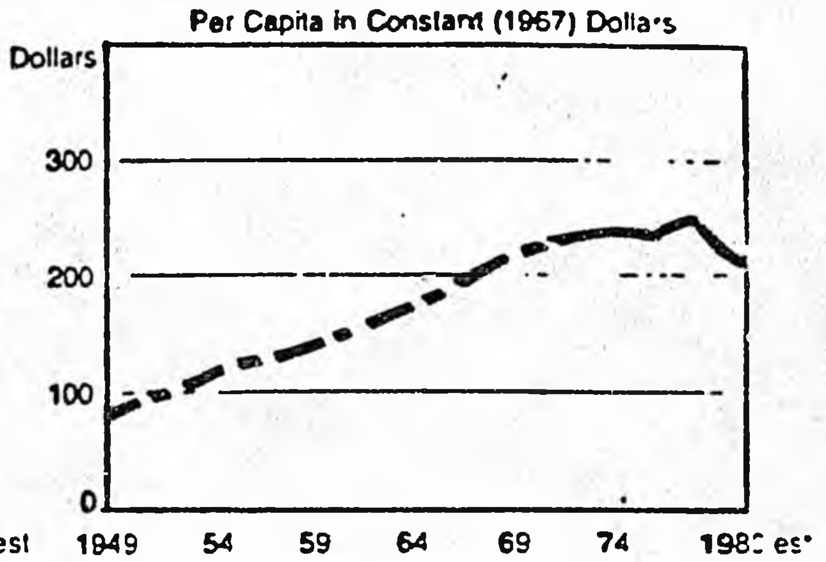
APPENDIX FIGURE 1

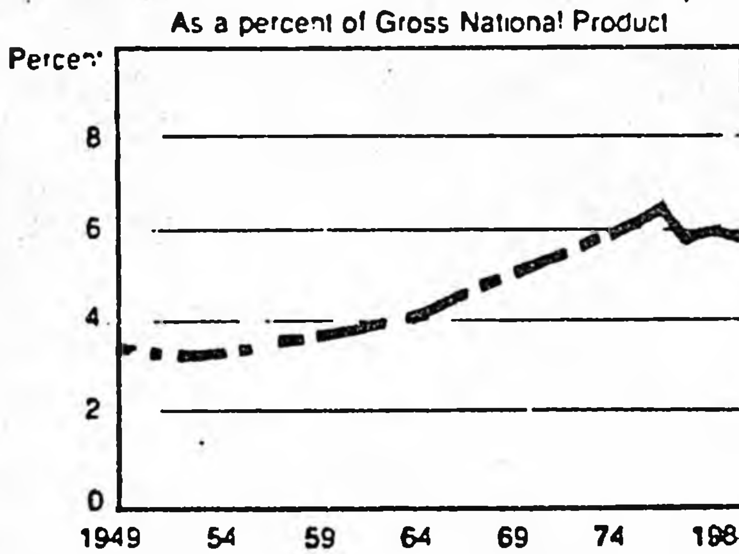
STATE AND LOCAL GOVERNMENT EXPENDITURE, AND FEDERAL AID, SELECTED FISCAL YEARS 1949-80
(State-Local Spending Slowdown)

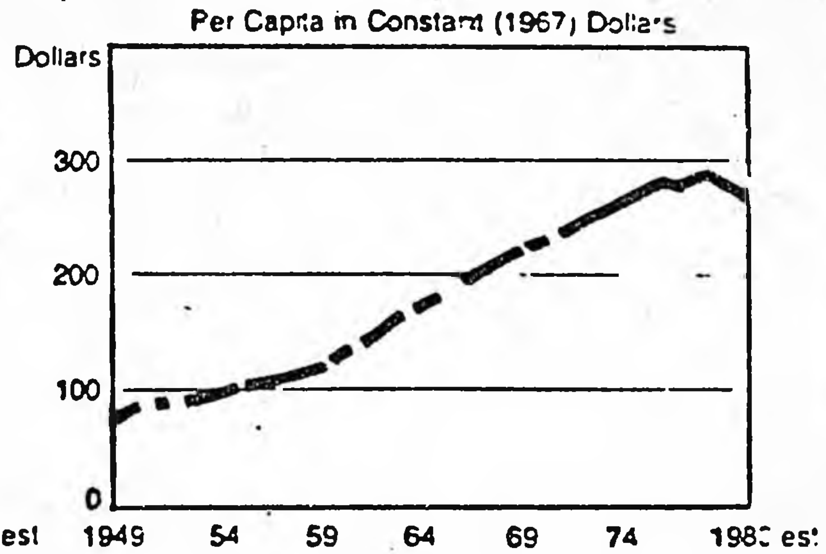
Local Expenditure (from own funds)



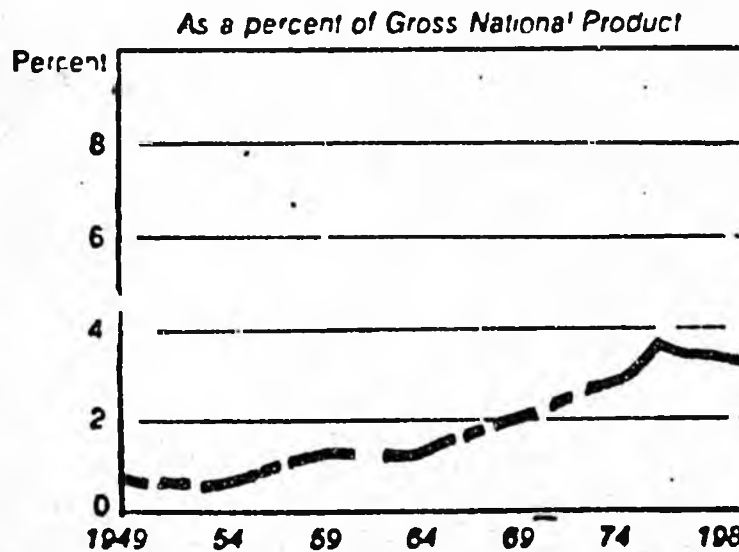


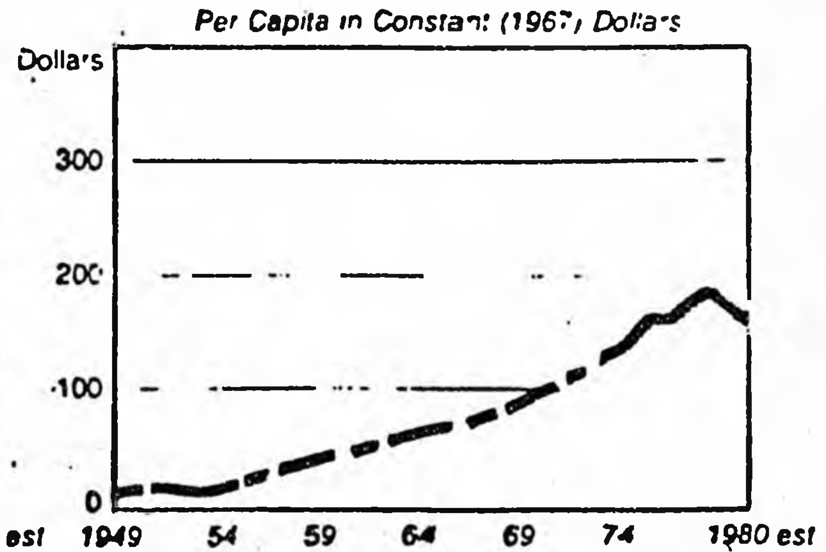
State Expenditure (from own funds)



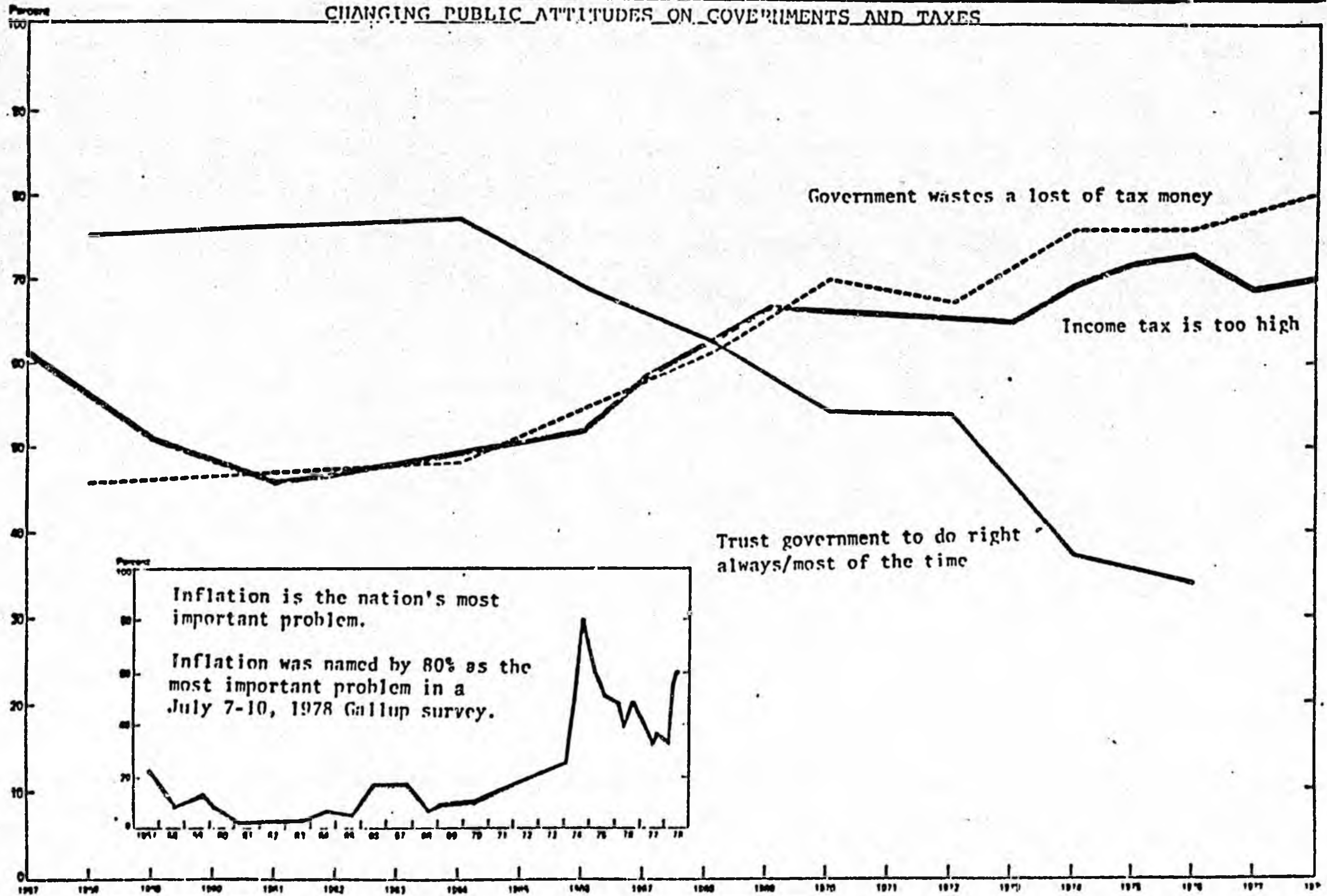


Federal Aid





APPENDIX FIGURE 2



PUBLIC OPINION, JULY/AUGUST 1978

APPENDIX TABLE 1

STATE AND LOCAL EXPENDITURES, INCLUDING FEDERAL AID, FOR THE UNITED STATES AND ALASKA, SELECTED YEARS 1959-1979

Fiscal Years	As Percent of Personal Income			Per Capita (Current Dollars)		
		Alaska			Alaska	
	United States	Percent	% of U.S.	United States	Amount	% of U.S.
1959	15.9	15.9	100	$ 332	$ 437	132
1969	18.6	34.5	185	652	1,443	221
1975	22.2	41.7	188	1,249	3,534	283
1976	23.3	39.1	168	1,422	3,951	278
1977	22.4	35.6	159	1,500	3,718	248
1978	21.5	38.7	180	1,590	4,172	262
1979 Prel.	21.1	46.2	219	1,740	5,084	292

Source: ACIR staff computations based on various reports of U.S. Bureau of the Census, Governments Division.

APPENDIX TABLE 2

A COMPARATIVE ANALYSIS OF FIVE POLICY POSITIONS CONCERNING THE GROWTH IN FEDERAL-STATE-LOCAL SPENDING OR THE SHIFT TO THE POLITICAL RIGHT

POLICY POSITION	PRO-FAST GROWTH: ANTI-LEGISLATIVE CONSTRAINTS I	AD HOC SLOWDOWN ANTI-LEG. CONSTRAINTS II	SLOWER GROWTH THRU GREATER LEG. ACCOUNTABILITY III	SLOWER GROWTH THRU TIGHTER LEG. CONSTRAINTS IV	GOVERNMENT CUT-BACK & TIGHTER LEG. CONSTRAINTS V
RATIONALE	Our "affluent society" in general & the poor & minorities in particular benefit from rapid growth of domestic programs voted by unfettered legislative bodies.	Govt. spending should accelerate or slow down in response to public opinion changes. Leg. bodies, therefore, should be given wide leeway in order to make ad hoc budgetary adjustments.	Public sector "fast' growth can be attributed in part to serious shortcomings in the way elected officials are held accountable for tax and spending decisions.	Public sector growth can be attributed in large part to the inability of a simple majority of legislators to balance off the general interest of taxpayers against the expenditure demands of the various special interest groups.	Public sector has grown too large because a simple majority in the legislature could not say "no" to all of the demands of the various special interest groups.
GENERAL PRESCRIPTION	Resist current efforts (ad hoc) to slow down domestic public sector growth and oppose all proposals (moderate or severe) that would make it harder to raise tax and spending levels in the future.	In view of the current conservative mood, go along with ad hoc slow down policies but resist all proposals (moderate or severe) that would make it harder to raise tax and spending levels in the future.	Support current slowdown policies and reform efforts (mostly statutory) that would focus a brighter accountability spotlight on tax and spending decisions. Resist the more drastic constitutional constraints on legislative majorities.	Support current slowdown policies, accountability reforms, and the more far-reaching constitutional changes that would make it more difficult for a simple legislative majority to raise tax and/or spending levels in the future.	Support accountability reforms and fairly drastic constitutional changes that would cut back existing tax and spending levels and make it more difficult for legislative bodies to raise tax and spending levels in the future.
EXAMPLES	"Fast" growth is reflected in the fact that domestic government spending grew consistently faster than the economy between 1949-1975.	Ad hoc state tax increases (1959-1975) when the public supported fast growth policies.1/ Ad hoc state tax cuts and "hold the line" expenditure policies now that the public wants a "slow down"--that is government spending that just keeps pace or slightly lags the growth of the economy.2/	Accountability Reforms: LOCAL: Truth-in-property taxation laws.3/ STATE AND FEDERAL: Indexation of the income tax.4/ Fiscal notes and reimbursement for expenditure mandates.5/ Budget reform. Tax and spending lids (both statutory and constitutional) that can be raised by majority vote of the legislature.6/ "Sunset" provisions.7/	LOCAL,8/ STATE,9/ & FEDERAL10/: Tax and spending ceilings and balanced budget controls that can be raised only with the approval of extraordinary majority of legislative body or the electorate voting in a referendum.	California's Proposition 13 (Jarvis I) which cut the property tax by more than half prohibits raising the property tax, and requires popular referendum at the local level and extraordinary majorities at the state legislative level to raise other taxes.
COMMENTARY	Liberalism's high spending citadel is experiencing serious erosion of support. Many of the Great Society followers have gone underground or defected to the right as inflation generates a new breed of born again budget balancers.	Traditionally, the great gathering place of the moderates before many of them lost confidence in ability of legislative bodies to cope with special interests. This sector is increasingly peopled by liberals who have burrowed in waiting for the high gales of fiscal austerity to blow over. Their motto--"If you can't lick 'em, ad hoc 'em."	The new moderate position--the rallying grounds for some liberals and many moderates hoping to check deeper penetration by the resurgent right by striking a better balance between the competing claims of the private and public sectors for the Nation's resources.	The traditional conservative stronghold now joined by the new radical chic of the right--Milton Friedman and his growing band of "right thinking" intellectuals. More significantly, the ranks of this sector are being swelled by the growing number of plain citizens defecting from the liberal and moderate camps.	The new far right--allegedly, reactionary "redneck" country controlled by Howard Jarvis. To the dismay of the establishment, Leader Jarvis has widespread support, particularly in the populist West where the citizenry can bypass the legislature and through direct initiative and referendum can change the basic (constitutional) rule of the fiscal game.*

*Under the traditional rules of the game, a simple majority of the legislature can raise tax and spending levels as high as it deems necessary.

See next page for footnotes.

John Shannon (April 15, 1980)

APPENDIX TABLE 2 (Continued)

Footnotes

1/ Between January 1, 1959, and December 1, 1976, 12 states adopted general sales taxes and in 76 instances states increased existing state sales tax levies. During the same period 13 states enacted personal income taxes and on 74 occasions states raised income taxes.

2/ Since 1976, there has been a virtual moratorium on raising state income and sales taxes and in 1979 about half of the states reduced one or the other.

3/ Truth in property tax provisions require automatic property tax rollback to offset most or all of the annual increase in the assessment base in the absence of a rigorous full disclosure procedure, i.e., paid announcement of proposed tax increase and public hearings. Since 1971, ten states have enacted this statute--Arizona, Florida, Hawaii, Maryland, Montana, Texas, Virginia, Kentucky, Rhode Island, and Tennessee.

4/ Since 1977, seven states have indexed their income taxes so as to prevent taxpayers from being automatically pushed into higher tax brackets through the silent action of inflation. These states are: California, Colorado, Arizona, Iowa, Minnesota, Oregon, and Wisconsin.

5/ About half of the states now attach fiscal notes to proposed legislation that would impose added expenditure responsibilities on local governments. Seven states have gone further down the path of fiscal accountability; state government either reimburses local governments for certain types of state expenditure mandates or refrains from enacting such mandates.

6/ Since 1976, 10 states have adopted limitations on state revenue or expenditure growth that can be set aside by majority vote in both houses of the legislature. In eight instances these limitations are statutory and in the other two cases (Tennessee and Texas) they are constitutional provisions. The limitation usually ties the growth in state taxes or spending to the growth in state personal income.

7/ In the last several years over 30 states have adopted some version of "Sunset"--a general statutory requirement that provides for the automatic termination of government programs and/or regulatory agencies at some point in time in the absence of explicit legislative reauthorization.

APPENDIX TABLE 2 (Continued)

8/ Since 1970, 20 states have imposed local property tax levy and/or general spending ceilings that can be raised only with the approval of an extraordinary majority of the local legislative body or (far more frequently) the approval of the local electorate voting in a referendum. These states are Alaska, Delaware, Indiana, Iowa, Kansas Kentucky, Louisiana, Minnesota, Ohio, South Carolina, Utah, Washington, Wisconsin, Florida, Massachusetts, New Mexico, New Jersey, Nevada, California, and Nebraska. Maryland allows these fiscal lids to be applied on a local option basis.

9/ Constitutional revenue and spending lids that require the approval of an extraordinary majority in both houses before fiscal ceilings can be lifted--Arizona, Hawaii, and Michigan in 1978 and California in 1979.

10/ At the present time there are numerous proposed constitutional amendments that would limit the federal government's tax and spending powers and others that call for a balanced budget. Thirty states have adopted resolutions directing the Congress to call a constitutional convention for the purpose of drafting a balanced budget amendment to the U.S. Constitution--34 state resolutions are needed to require the calling of a constitutional convention.

APPENDIX TABLE 2 (Continued)

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7/ In the last several years over 30 states have adopted some version of "Sunset"--a general statutory requirement that provides for the automatic termination of government programs and/or regulatory agencies at some point in time in the absence of explicit legislative reauthorization.

APPENDIX TABLE 3

RECENT STATE AND LOCAL REVENUE/EXPENDITURE LIMITATIONS
JANUARY 1, 1976-JANUARY 1, 1980

State	Year	Constitutional or Statutory	State Limitation	Local Limitation	Remarks
New Jersey	1976	S	X	X	State expenditure growth is limited to the increase in state personal income. Municipalities cannot increase their budgets by more than 5% per year. Both limits can be exceeded only by a majority vote on a referendum.
Colorado	1977	S	X		State general fund expenditures are limited to a 7% annual increase. An additional 4% may be allocated to a reserve fund, but amounts over 11% must be refunded to taxpayers.
Michigan	1977	S	X		A Budget Stabilization Fund was established, with provisions for pay-in to the fund during periods of economic growth, and pay-out during recessionary periods. It is now used in conjunction with the 1978 state spending limitation.
Rhode Island	1977	S	X		The legislature adopted a non-binding "suggested" 8% cap on the annual growth of budget appropriations.
Tennessee	1978	C	X		Increases in appropriations from state tax revenues are limited to the estimated growth in the state's economy. The lid may be exceeded by majority vote of the legislature.
Arizona	1978	C	X		State spending is limited to 7% of total state personal income. The limit may be exceeded by 2/3 vote of the legislature.
Hawaii	1978	C	X		Increases in state general fund appropriations are limited to the estimated growth in the state's economy. Larger increases must be approved by a 2/3 vote of the legislature.
Michigan	1978	C	X		State tax revenues can increase only as fast as the growth in personal income. If revenues exceed the limit by more than 1%, the excess is refunded through the income tax. If the excess is less than 1%, it is placed in the Budget Stabilization Fund. The limit may be exceeded if the Governor specifies an emergency and 2/3 of the legislature concur.
Texas	1978	C	X		Increases in appropriations from state tax revenues are limited to the estimated growth in the state's economy. The limit may be exceeded by a simple majority of the legislature.
California	1979	C	X	X	Increases in state and local appropriations are limited to population growth and inflation. The limits may be exceeded, but appropriations in the following three years must be reduced to prevent an aggregate increase in expenditures. The limits may be changed by the electorate, but the change is effective only for three years.
Louisiana	1979	S	X		State tax revenues can grow only as fast as the increase in personal income. Proceeds from severance taxes are not included in the limitation.
Massachusetts	1979	S		X	Increases in local government expenditures are limited to 4%. Override provisions are included. The limitation expires December 31, 1981.

APPENDIX TABLE 3 (Continued)

RECENT STATE AND LOCAL REVENUE/EXPENDITURE LIMITATIONS
JANUARY 1, 1976-JANUARY 1, 1980 (Cont'd.)

State	Year	Constitutional or Statutory	State Limitation	Local Limitation	Remarks
Nebraska	1979	S		X	No political subdivision may adopt a budget in which the anticipated receipts exceed the current year's by more than 7%. Further allowances are included for population growth exceeding 5%. The limit may be exceeded in the event of an emergency or upon voter approval.
Nevada	1979	S	X	X	The state budget is limited to the 1975-77 biennium budget adjusted for population changes and inflation. Local budgets are tied to 1979 fiscal year budgets adjusted for population changes and a partial inflation allowance. The limits may be exceeded "to the extent necessary to meet situations in which there is a threat to life or property."
Oregon	1979	S	X		The increase in state appropriations for general governmental purposes for the 1979-81 biennium is limited to the growth in state personal income in the preceeding two years.
Utah	1979	S	X	X	The annual increase in state appropriations is limited to 85% of the percentage increase in state personal income. The increase in local revenues may not exceed 90% of the percentage increase in state personal income, with further adjustments for population growth allowed. The limits may be exceeded by a two-thirds vote of the legislative body of a unit of government.
Washington	1979	S	X		State tax revenues can grow only as fast as the average increase in state personal income over the three previous years. The limit may be exceeded by a 2/3 vote of the legislature.
TOTALS			15	6	

NOTE: C-Constitutional. S-Statutory.

NOTE WELL: Only the six state actions that placed overall limitations on local government revenues and expenditures are included in this table. Since 1970, states have imposed approximately 35 other restrictions on the ability of local authorities to raise property taxes.

SOURCE: ACIR staff compilations based on: Commerce Clearing House, State Tax Reporter; National Conference of State Legislatures, A Legislator's Guide to State Tax and Spending Limits, March 1979.

TABLE I

ANNUAL COMPOUND GROWTH RATES

Period	Anchorage Consumer Price Index	Alaska Population	General Fund Appropriations	General Fund Appropriations in Constant Dollars	General Fund Appropriations Per Capital in Constant $
1960 - 1980	4.73%	2.90%	23.78%	18.19%	14.87%
1960 - 1969	1.72	3.03	14.40	12.49	9.18
1970 - 1980	7.60	2.85	26.40	17.47	14.22
1969 - 1980	7.26	2.78	32.01	23.08	19.75
1970 - 1979	7.39	3.33	14.49	6.62	3.18

PREPARED BY:

Legislative Finance Div.
5-25-81

TABLE II

Calendar Year	Anchorage Consumer Price Index October 1967-100.0	Alaska Pop. 2/	General Fund Appropriations ($ millions) 3/	General Fund Appropriations in Constant Dollars ($ millions)	Per Capita General Fund Appropriations in Constant Dollars $
1960	92.0	226,167	45.9	49.8	220
1961	92.9	238,000	52.3	56.3	236
1962	92.6	246,000	65.8	71.0	289
1963	93.3	256,000	82.9	88.8	347
1964	93.9	263,000	79.1	84.2	320
1965	94.2	271,000	86.1	102.0	337
1966	97.9	271,000	93.8	95.8	354
1967	100.0	278,000	113.1	113.1	407
1968	102.6	285,000	124.1	120.9	424
1969	107.3	296,000	154.1	143.6	485
1970	111.5	302,361	314.2	281.7	932
1971	114.4	316,000	292.1	255.3	808
1972	116.9	326,000	333.5	285.2	875
1973	123.8	332,000	379.3	306.3	923
1974	140.0	343,000	451.3	322.3	940
1975	157.4	379,000	590.3	375.0	989
1976	167.6	405,000	692.3	413.0	1020
1977	177.3	408,000	819.1	462.0	1132
1978	194.8 1/	411,000	1071.7	550.2	1339
1979	211.8	406,000	1062.3	501.6	1235
1980	232.0	400,331	3270.8	1409.8	3521

1. 1978-1980 figures are Anchorage price index for urban wage earners and clerical employees as of November.

2. 1960, 1970, and 1980 figures based on April 1st census; other figures refer to estimated July 1st population of the U. S. Bureau of the Census.

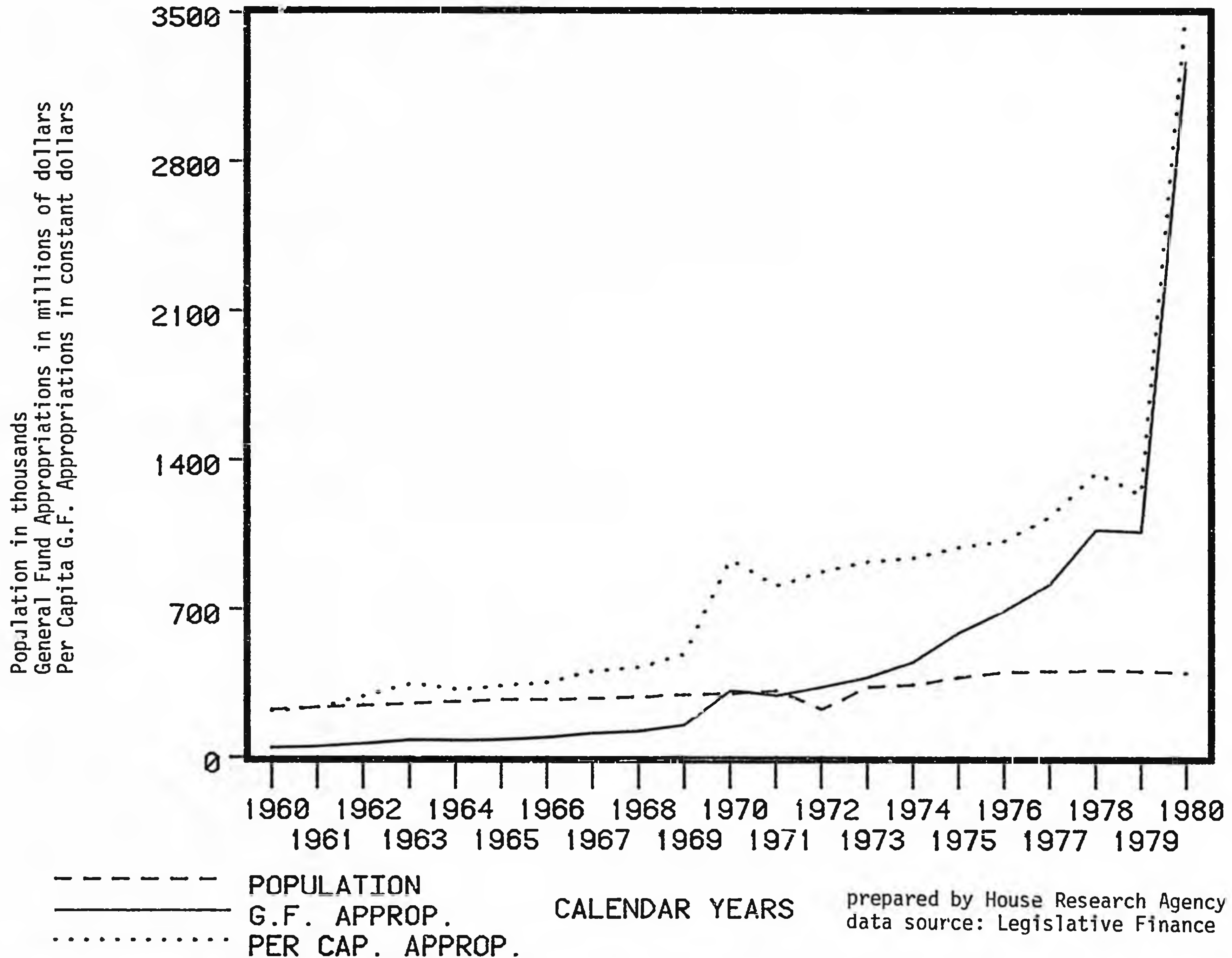
3. (a) The figures are for the fiscal year following the listed calendar year, e.g., in 1960 the fiscal year 1961 appropriations act of $39.8 million in general funds was signed into law.

   (b) 1960-1972 figures from Governor's Budget Document; 1973-1980 figures from Free Conference Committee Report on the Budget.

   (c) Supplemental appropriations are excluded except for a $580.8 million capital projects supplemental in 1980.

   (d) Appropriations to the Permanent Fund and general reserve which are strictly for investment are excluded.

Prepared by:
Legislative Finance
5-25-81



HISTORICAL GROWTH IN GENERAL FUND PER CAPITA APPROPRIATIONS
FROM CALENDAR YEAR 1960 TO 1980
Population in thousands
General Fund Appropriations in millions of dollars
Per Capita G.F. Appropriations in constant dollars
3500
2800
2100
1400
700
0
1960 1962 1964 1966 1968 1970 1972 1974 1976 1978 1980
1961 1963 1965 1967 1969 1971 1973 1975 1977 1979
POPULATION
G.F. APPROP.
PER CAP. APPROP.
CALENDAR YEARS
prepared by House Research Agency
data source: Legislative Finance

Department of Revenue - Research

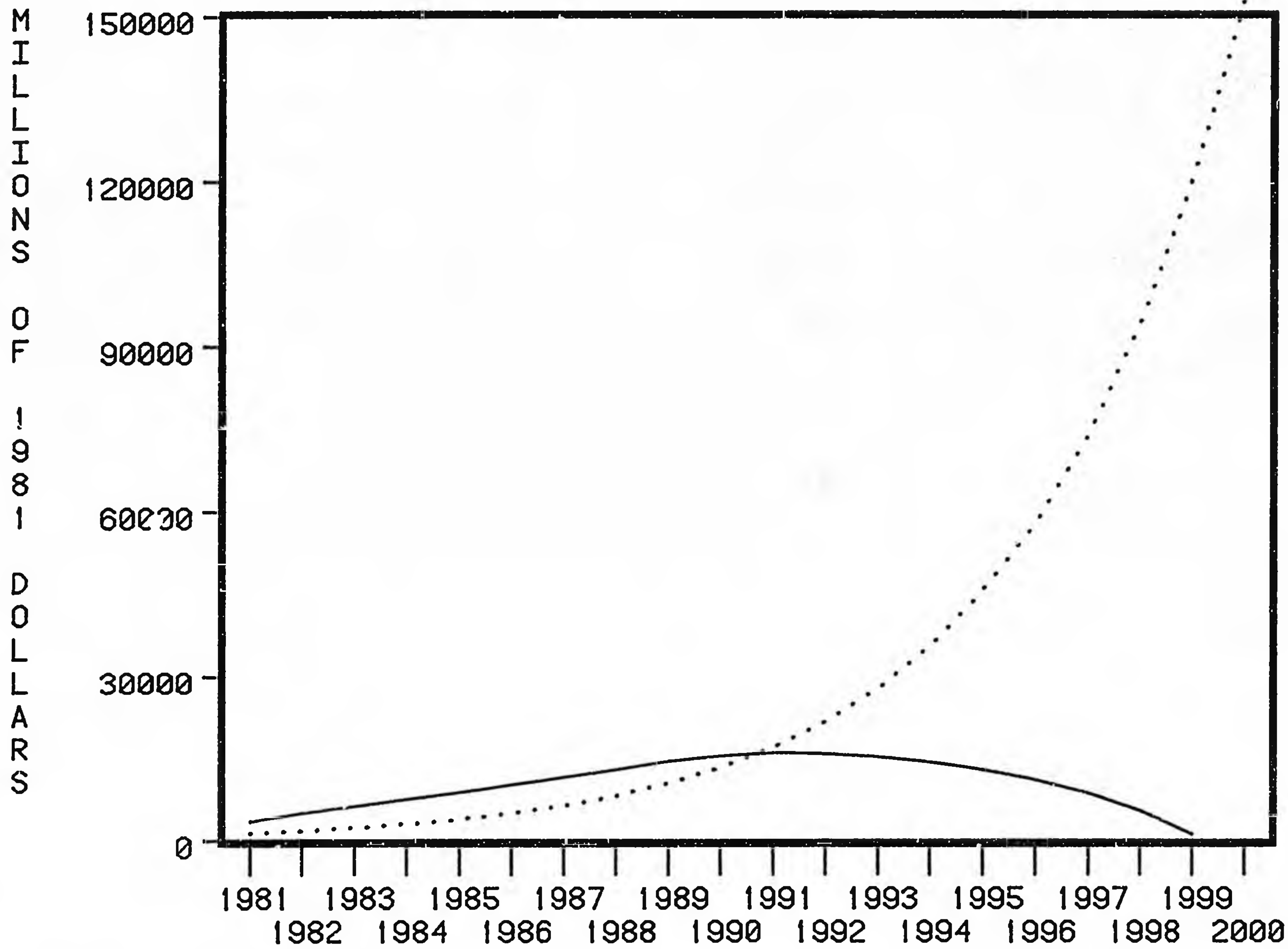
4/14/81

REVENUES-EXPENDITURES

NO GAS LINE
25% PERMANENT FUND
(MILLIONS OF CURRENT DOLLARS)
16% REAL EXPENDITURE GROWTH RATE (+10% inflation = 26% nominal growth rate)

FY	GENERAL FUND SUSTAINABLE REVENUES	UNRESTRICTED REVENUES GENERAL FUND	EXPENDITURES GENERAL FUND operating budget only	SURPLUS OR DEFICIT GENERAL FUND	GENERAL FUND BALANCE	PERMANENT FUND CONTRIBUTION	PERMANENT FUND BALANCE
81	330.8	3607.0	1500.0	2107.0	1677.0	1261.8	1796.0
→82	$ [illegible] 423.2	5191.1	1914.0	3277.1	4954.1	557.2	2446.2
83	637.6	6435.8	2442.3	3993.5	8947.5	679.3	3248.7
84	888.0	7660.5	3116.3	4544.2	13491.8	807.1	4223.6
85	1213.4	8939.6	3976.4	4963.2	18455.0	914.4	5319.8
86	1566.9	10326.5	5073.9	5252.6	23707.6	1068.5	6592.8
87	1945.0	11687.1	6474.3	5212.8	28920.4	1190.7	8019.1
88	2341.3	13133.7	8261.2	4872.5	33792.9	1320.9	9606.9
89	2742.8	14647.3	10541.3	4106.0	37898.9	1451.2	11356.7
90	3130.5	15621.4	13450.6	2170.8	40069.7	1523.6	13208.7
91	3450.9	16169.7	17163.0	-993.2	39076.5	1555.5	15116.6
92	3646.6	15829.6	21900.0	-6070.4	33006.1	1501.5	16985.2
93	3628.3	15346.8	27944.3	-12597.5	20408.6	1455.1	18811.2
94	3327.2	14303.0	35656.9	-21353.9	-945.4	1376.7	20554.1
95	2639.6	12919.7	45498.2	-32578.5	-33523.8	1304.2	22213.5
96	1452.2	11124.1	58055.6	-46931.5	-80455.4	1240.7	23795.2
97	-376.2	8663.6	74078.8	-65415.2	-145870.6	1191.0	25312.4
98	-3030.9	5421.5	94524.4	-89102.9	-234973.5	1142.3	26766.9
99	-6744.7	1149.1	120613.0	-119463.9	-354437.4	1095.7	28161.4
0	-11815.9	-4481.9	153902.0	-158383.9	-512821.3	1050.9	29498.8

GENERAL FUND REVENUES & OPERATING BUDGET EXPENDITURES
PROJECTED FROM FY 1981 TO FY 2000



GEN.FUND REVENUE
OPER.EXPENDITURE

FISCAL YEARS

prepared by House Research Agency
data source: Ak. Dept. of Revenue

DRAFT

ESTIMATED FY 82 APPROPRIATION CEILING UNDER SJR4 & HJR57

Governor's Office

SJR4	HJR57		
($mil GF)	($mil GF)	($mil Tot. Funds)	
$4772.5	$4772.5	$5545.1	Executive Budget Book I Total FY 81 Adjusted Authorizations Book
			Exemptions
(900.0)	(900.0)	(900.0)	Permanent Fund Contribution
(129.4)	0	0	Permanent Fund Dividends
0[1]	0	0	Loan Capitalizations
0	0	0	Voter Approved Capital Projects
0	0	0	Escrow Accounts
(93.7)	(93.7)	(96.8)	Debt Service
(350.0)	0	0	Reserve for Disaster/Emergency
0	0	0	User Fee Increase
0	0	0	Court Orders
0	0	0	Transfer of Fed. Responsibility
0	0	0	Quarter Income from P.F. Contributions
0	0	0	Two-thirds vote of Legislature for Disaster Needs
			Other Possible Exemptions[2]
-	-	-	Income Tax Relief
-	-	-	Native Land Claims
$ 3299.4	$ 3778.8	$ 4548.3	
x 1.1298	x 1.1298	x 1.1298	Estimated Growth Rate [3]
$ 3727.7	$ 4269.3	$ 5138.7	Estimated FY 82 Appropriation Ceiling

DRAFT

FOOTNOTES

1. Assume capitalizations for loans, which will be made at Market Rates, are exempt from limitation of appropriation increases. Capitalizations for loans which will be made at interest rates below the market rate are NOT exempt from limitation of appropriation increases.

2. The income tax relief appropriation $186.4 million and the Native Land Claims appropriation $292.6 million may also be considered possible exemption items. However, neither SJR4 nor HJR57 specifically recognizes these items.

3. 12.98% Growth Rate = 2.84% Av (1970-80) Pop. Increase + 10.14% Av 1980 CPI.
   NOTE: 10.14% is a weighted average of the CPI for all Urban Consumers, based on Anchorage and Fairbanks data. (Anchorage, population 173,992 with 1980 CPI increase of 10.0%; Fairbanks population 53,799 with 1980 CPI increase of 10.6%).

STATE OF ALASKA

THE LEGISLATURE

BUDGET AND AUDIT COMMITTEE

FINANCE DIVISION
POUCH WF—STATE CAPITOL
JUNEAU, ALASKA 99811
PHONE: (907) 465-3795

MEMORANDUM

TO: Honorable Ed Dankworth,
Co-chairman
Senate Finance Committee

FROM: Milt Barker, MB Fiscal Analyst
Legislative Finance Division

DATE: January 22, 1981

SUBJECT: FY 82 Budget Under Proposed Constitutional Limits

Following are estimates of what FY 82 budgets would be permitted if various proposed constitutional limits on budget growth were now in effect.

SJR 3 by Colletta

This limits growth of appropriations, except those for capital projects and contributions to the permanent fund, to growth of the economy. For calendar 1979, Alaska personal income grew 4.55%. Applied to an FY 81 operating budget of $1,282.0 million (see attached Table I), this would permit an FY 82 operating budget of $1,340.3 million. The Governor has proposed a general fund operating budget of $1,826.5 million.

HJR 5 & SJR 4 by Request of the Governor

This limits growth of appropriations to inflation in the calendar year preceding the Governor's budget submission plus the average yearly growth in the State's population as measured by the last two federal censuses. Using the most recent Anchorage consumer price index figures and the 1970 and preliminary 1980 census data, the permitted growth rate for the FY 82 budget would be 12.8% to 14.0%, depending on which of two Anchorage consumer price indices is used.

The limitation does not apply to:

1) permanent fund contributions
2) permanent fund dividends
3) loan fund capitalization (but loan subsidies are limited)
4) capital projects approved by voters
5) debt service
6) disaster reserve funds
7) increases in state expenditures resulting from court order or federal law
8) 1/4 of the income from contributions to the permanent fund above the 25% minimum

Referring to Table I again, the following FY 81 expenditures would be subject to growth limits:

Operating	$ 1,282.0
Capital	72.1
Special Appropriations	64.7
Renewable Resources	125.0
HB 60	580.8
Loan Subsidies[1/]	144.7
TOTAL	$ 2,269.3

The 12.8% or 14.0% growth rates applied to this figure, plus 1/4 of 10% interest on $900 million excess permanent fund contributions, would permit FY 82 budgets for restricted expenditures of $2,582.2 or $ 2,609.5 million. The Governor's FY 82 budget for such items totals $2,286.9 million:

Operating	$ 1,826.5
Loan Subsidies[1/]	233.0
Capital	227.4
TOTAL	$ 2,286.9

HJR 4 - by Gardiner

This limits growth of appropriations, except for appropriations to the permanent fund and for loans, to growth of the economy. Using the 4.55% growth in personal income in 1979 and an FY 81 base from Table I of $2,474.6 million,

Operating	$ 1,282.0
Capital (less native claims)	72.1
Special Appropriations (includes general fund reserve)	414.7
HB 60	580.8
Renewable Resources	125.0
TOTAL	$ 2,474.6

1. Figures provided by Budget and Management.

the permitted FY 82 budget would be $2,587.1 million. For these same restricted items, the Governor's FY 82 budget proposes $2,703.9 million:

Operating	$ 1,826.5
Capital	227.4
Rainy Day Funds (general fund reserve)	350.0
Escrow Account	300.0
TOTAL	$ 2,703.9

MB:dh

January 13, 1981

The Honorable Jalmar Kerttula
President of the Senate
Pouch V
Juneau, AK 99811

Dear Mr. President:

Under art. III, sec. 18, of the Alaska Constitution, I am transmitting a proposed constitutional amendment on spending limitations for the consideration of the legislature.

My proposal would amend the constitution's finance article to add two sections, one setting forth spending limitations and the other prescribing ten specific exceptions. Each of the exceptions is reasonably necessary, and some of them are for appropriations of money to be invested rather than expended, and, to that extent, do not really involve actual expenditures.

The proposed amendment limits annual increases in appropriations of state money -- but not of money from other, non-state sources such as federal money -- to the increase in the federal consumer price index for Alaska for the preceding year plus a percent equal to the state's average yearly growth in population.

At the present time, the only federal consumer price index for Alaska is that done for the Anchorage area. It appears that one will also be prepared for Fairbanks sometime soon. And indexes may also be prepared for other Alaskan cities in the future. The index for the state will consist of the weighted average of those indexes, that is, in proportion to each community's relative population.

The measure of the state's average yearly population growth is the federal decennial census and the interim renumeration to be taken at five year intervals. The latter, while called for by federal law, has yet to be funded. Nevertheless, even without a renumeration, the decennial census provides an accurate measure of the state's average yearly growth.

The use of data prepared exclusively by the United States is deliberate and essential. The pressure to shape cost and population data to justify increased expenditures would be enormous if those data were prepared by state or local agencies. Using data developed by an independent and separate government avoids that problem completely.

These two measures of growth, while not always coincident with all governmental needs, will allow the state to keep abreast of most needs and yet hold growth to reasonable and responsible limits. To the extent that the state still lags behind its sister states in some areas of governmental services and facilities, the exceptions prescribed by the second section will allow it to catch up, if that is what the electorate wants. Each of these exceptions will be discussed in turn, below.

The first exception is for appropriations of money to be deposited in the permanent fund, and the second is to pay permanent fund dividends to the people. It is self-evident that neither needs to be limited. The third exception is to capitalize loan funds, that is, appropriations of the money which will be loaned and repaid with interest under the state's loan programs. To the extent that low interest loans are subsidized, the appropriations for that purpose must be separate, and they are not within the terms of the exception. The fourth exception is for appropriations for capital improvements which have been approved by the voters. This includes those funded by appropriation from the general fund and those funded by bond proceeds. Voter approval is a must for the appropriations to be within the exception. But if the voters approve, there are no limits on appropriations for capital improvements.

The term "capital improvements" is used in the amendment in the same sense as it is used in sections 8 and 9 of the finance article relating to state and local debt. It refers, generally speaking, to public works or facilities of a permanent character as described in the case of <u>City of Juneau</u> <u>v</u>. <u>Hixson</u>, 373 P.2d 743 (Alaska 1962).

The fifth exception is for appropriations made to escrow accounts or otherwise to repay general obligation bonds. As a practical matter, it may be to the state's great advantage at any time to make a large payment, either into escrow or directly, to repay outstanding general obligation bonds. That kind of a payment would not constitute a true increase in expenditures, and it is, therefore, made one of the exceptions.

The sixth exception is for money appropriated as a reserve account for disasters of natural or human origin.

The device has been called a rainy-day account, and it is simply a means of setting aside a financial cushion for the state during a fiscal year in case of exceptional need. At the present time the Reserve for Emergency Operating Expenses Account has been established under AS 37.05.159 to meet this need. It will be superseded by this amendment, and in order to spend money appropriated to the reserve account, the provisions of the tenth exception will have to be followed.

The seventh exception is for money appropriated to coincide with increases in user fees. The term "user fees" includes all kinds of taxes or charges which are levied upon those who use a government facility or service. They range from hunting and fishing licenses to boiler inspection fees. So long as users are paying the money, no purpose would be served by placing this category within the limitations on expenditures. No big increases are foreseen at this time, but should users wish to have them, there is no reason to place a constitutional bar in their way.

The eighth exception is for appropriations required by court orders or by a transfer of functions from the federal to the state government. Transfers from local to the state government are within the legislature's control, and therefore are subject to the limitation. Court orders -- and that would include judgments for damages or orders for future relief -- are not within the legislature's control and could cause significant, temporary increases from time to time. The same could happen if the federal government were, for instance, to shift all of the social services or education burden to states. While one hopes this exception will be little used, prudence dictates its existence.

The ninth exception is for appropriations of money derived from one-quarter of the income from extra appropriations made to the permanent fund. The purpose of this exception is to encourage those who would spend more money to save more money. The more money that is placed in the fund, the more money there will be available under this exception to spend.

The tenth and final exception is for natural disasters. As safeguards against spurious spending under this exception, the disaster must be declared by the governor in the first instance and the appropriation bill must be passed by a two-thirds majority of the membership of each house and approved by the governor. If the governor does not approve the appropriation or vetoes it to reduce or strike any item, his veto is final. The purpose of the absolute veto is to preclude any excess spending on non-emergency items in a bill appropriating money for

disaster relief. Without an absolute veto, this exception would create an unacceptably large loophole.

The proposed amendment is conservative, responsible, and workable. It will not hobble the state or prevent the performance of any needed governmental function. It will set limits where they are needed, and it will not set limits where they are not needed. It will be good for both the private sector and the public sector, and I urge its favorable consideration.

Sincerely,

S/JSH

Jay S. Hammond
Governor