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June 5, 2001 Joint Committee on Finance Paper #240

Statutory Limit on State GPR Appropriations (Budget Management and Compensation Reserves)

[LFB 2001-03 Budget Summary: Page 153, #3]

CURRENT LAW

No provision.

GOVERNOR

Create a statutory limit, first effective for the 2003-05 fiscal biennium, on the percent by which year to year total GPR appropriations can be increased.

DISCUSSION POINTS

1. Under the bill, the statutory limit would specify that for any biennial budget period, the total amount of GPR appropriated (after certain enumerated exclusions) in that biennial period may not exceed the projected percentage increase in state personal income for the next two calendar years. The applicable projected increase in state personal income would have to be determined by Department of Revenue by December 5th of each even-numbered year for the two calendar years for which January 1 of that calendar year immediately precedes respectively the first or second fiscal year of the budget biennium. For example, for the 2003-05 biennial budget, the two calendar years that would be the reference point for projected personal income growth would be January 1, 2003 and January 1, 2004 and thus projected personal income growth for calendar years 2003 and 2004 respectively. The Department of Administration (DOA) would then be required to use the projected respective percentage increases in personal income to determine the allowable increase in GPR appropriations for the forthcoming fiscal biennium and to include in the Executive Budget Book a statement of this determination. DOA would have the authority, in accord with the statute,

to determine the prior year total GPR appropriated level to which the limit is to be applied.

2. Under the bill, the following GPR appropriations would be excluded from the total GPR appropriations otherwise subject to the expenditure limitation:

- Any appropriation passed by at least a two-thirds vote of each house of the Legislature

- Principal and interest payments on public debt

- Principal and interest payments on operating notes

- Payments to honor statutory moral obligation pledges

- Payments to the federal government from bond revenues to avoid designation of state bonds as arbitrage bonds

- Payments for legal expenses and the costs of judgments, orders and settlements of actions and appeals incurred by the state

- Payments for tax relief under s. 20.835(2) of the statutes

- Payments to execute a transfer from the general fund to the budget stabilization fund

- Payments to execute a transfer from the general fund to the tax relief fund (also created under the bill)

3. The most recent survey of states concerning state expenditure limits done by the National Conference of State Legislatures identified 26 states with some type of limit (either statutory or constitutional) on amount by which expenditures in those states could increase over the prior year. Ten of the 26 states had a limit that was established statutorily and the remaining 16 had a limit that was constitutionally established.

4. In general, questions relating to placing limits on state appropriations, fall into three categories: (a) what appropriations or categories of appropriations, if any, are excluded from the limit? (b) what is the allowable increase amount (typically expressed as a percentage increase over some base level) based on? and (c) how effective is the limit, that is, how easy is it for the Legislature to ignore or override the established limit? One way of reviewing the Governor's proposed limit on state appropriations is to examine the provisions in the bill in terms of these three general categories.

5. <u>Exclusions from limit.</u> Under the bill, the statutory limit would apply only to GPR appropriations; appropriations from program revenues, segregated funds or federal funds would not be subject to the limit. Further, certain categories of GPR appropriations would also be excluded from the limit. The three most significant categories in terms of current dollar impact are those relating to exclusions of: (a) principal and interest payments on public debt; (b) principal and

interest payments on operating notes; and (c) payments for tax relief under s. 20.835 (2) of the statutes. As a point of reference, these three categories of appropriations in the bill total $548.6 million in 2002-03 and represent about 4.6% of total GPR appropriations plus compensation reserves under the bill for that fiscal year. The other excluded categories (payments to honor statutory moral obligation pledges, payments to the federal government from bond revenues to avoid designation of state bonds as arbitrage bonds, payments for legal expenses and the costs of judgments, orders and settlements of actions and appeals incurred by the state, and payments to execute a transfer from the general fund to the budget stabilization fund or the proposed tax relief fund) could potentially be significant in dollar amounts under certain situations but are not likely to be a significant exclusion in terms of year-to-year budgeted levels. Further, any specific appropriation that was passed by at least a two-thirds affirmative vote of the Legislature would be excluded from the limit. Because the limit provision is statutory, any session of the Legislature could amend it to include or exclude additional individual GPR appropriations or categories of appropriations.

6. Basis for calculation of the permitted increase. The survey of the states done by NCSL indicated a variety of ways in such limits have been designed, often with some unique adaptations in different states. In general terms, however, the 26 states with limits may be categorized, with respect to what the permitted increase is based upon, into the groupings shown in Table 1.

TABLE 1

Summary Categorization of State Spending Limits Increase Basis

Increase Basis Category	Number of States
Percentage Increase in State Personal Income	11
Percentage Increase in State Personal Income and State Population	1
Fixed Percent of Total State Personal Income	4
Fixed Percent of Total Available Revenues	5
Percentage Increase in CPI and State Population	4
Percentage Increase in CPI	1
TOTAL	26

7. The groupings in the above table may be further summarized by stating that of the 26 states identified in the survey, 16 states (62%) based their limits on a factor relating to state personal income, another five states (19%) based their limits on a factor relating to estimated available revenues and the remaining five states (19%) based their limits on a factor relating to the percentage increase in the CPI or the CPI plus state population growth.

8. For growth in state personal income, a number of states look backwards by

measuring the actual growth in state personal income over the last two to five years. For those that use percentage increase in state population and/or the percentage increase in the CPI, again the increase is typically calculated by measuring that growth over a past number of years. Under the bill, the applicable limit would be forward-looking in that the increase would be calculated based on an estimate to be prepared by the Department of Revenue on the projected growth in state personal income for the two calendar years corresponding to the legislative biennium in which the biennial budget is considered. For example, under the bill, this limit would be first effective for the 2003-05 biennial budget. Thus DOR would be required to provide by December 5th of calendar year 2002 its estimate of growth in personal income for calendar years 2003 and 2004. Those projected percentage increases would then determine the allowable annual percentage increase in state appropriations subject to limit in each year. In terms of having a limit that is tied to some kind of ability to pay type approach, relating the limit to estimated revenue growth in the future budget biennium could be seen as preferable to looking at past years' growth. An argument against using such a measure is that it relies on projections of growth that may not happen.

9. Effectiveness of the limit. In general, limits such as this can be established in one of two ways: (a) as a statutory limit; or (b) as a limit established under the state constitution. Of the 26 states that have some kind of limit, a majority (16 states) established the limit in their state constitutions. Under the bill, the limit would be established statutorily. With regard to regulating the Legislature, a statutory provision obviously has legislative intent value. Further, failure to follow the statutory requirement may subject the Legislature to public criticism. However, if the Legislature wishes to not have a given biennial budget subject to the limit it could exempt that budget from the limit by including a provision that the budget is deemed to be valid notwithstanding that it does not comply with the statutory limit or by including a repeal of the statutory limit provision in that budget bill. Moreover, if a given Legislature were to simply ignore the statutory limit on permissible increases in appropriation levels, it is reasonable to assume that the State Supreme Court would likely not hold that budget to have been be enacted illegally. The State Supreme Court has held on several occasions that the remedy for noncompliance with this type of procedural provision lies exclusively within the legislative branch of government. Others would argue, however, that such a statutory limit would provide a considerable pressure for the Governor and Legislature to comply with the statutory provisions. They would note, for example, that the Governor and Legislature follow the statutory requirement that each biennial budget have a percentage amount of total GPR appropriations set aside as a reserve (required statutory balance).

10. In considering any proposed limit on increases in appropriations, the first question that usually arises is what impact such a limit would have had if it been in effect for past budgets or if it were to be made effective for the applicable budget under consideration. Table 2 provides such a comparison for the limit as proposed under the bill using the 2001-03 the budget as introduced by the Governor and for the final applicable budgeted levels for the six previous biennia. For the 2001-03 budget, the applicable projections of personal income growth (for calendar years 2002 and 2003) were used. For prior biennia, the actual personal income percentage increases were used.

TABLE 2

Comparison of GPR Budgeted Amounts to Estimated Bill Limits
Limit Calculated Separately for Each Biennium
($ In Millions)

Biennium	Budgeted Amount	Limit Under Bill	Limit Less Budgeted Amount
1989-91	$11,546.8	$11,548.9	$2.1
1991-93	12,912.3	12,986.3	74.0
1993-95	14,519.1	14,284.8	-234.3
1995-97	16,503.0	16,212.5	-290.5
1997-99	18,861.3	19,031.5	170.2
1999-01	20,952.6	20,599.4	-353.2
2001-03	22,504.0*	22,887.3	383.3

*Represents applicable SB 55/AB 144 levels.

11. As can been seen from Table 2, under the Governor's budget, the amount of the GPR budget that would be subject to the limit (about 95% of the total GPR budget) totals $383.3 million less than the proposed limit, if the limit were made applicable to the budget as recommended by the Governor. Three of the past final budgets, including the budget for the 1999-01 biennium, would have been in excess of the estimated applicable limit amounts for those fiscal biennia and three of the past final budgets would have been under the applicable limit amounts.

12. Since the Assembly has recently passed an appropriation limit bill, another question is how the provisions of that bill, as passed by the Assembly, compare with the appropriation limit provisions of the bill. The provisions of Assembly Substitute Amendment 1 to 2001 Assembly Bill 1, as amended by Assembly Amendments 2 and 3 [referred to as ASA 1 in the following points], are the same as the provisions contained in the bill, with the following exceptions:

- Under ASA 1, the limit would apply to the current budget rather than first being effective for the 2003-05 budget as proposed under the bill.

- ASA 1 would have the Legislative Fiscal Bureau make the determination, using the estimates of state personal income growth projected by the Department of Revenue, of the amount appropriated from general purpose revenue for any fiscal biennium to which the appropriation limit applies. Under the bill, the Department of Administration would make this determination.

- Under the bill, the estimates of growth in state personal income would have to be prepared by December 5th of each even-numbered year. Under ASA 1, that date would instead be by November 20th of each even-numbered year. Under the bill, the determination of the GPR amount appropriated would have to be completed no later than December 31st of each even-numbered year. Under ASA 1, that date would be changed to December 1st of each even-numbered year.

• As a separate bill, ASA 1 also contains a session law provisions to require that: (a) the Department of Revenue make its projections of personal income growth for calendar years 2002 and 2003, by the 15th day of the second month after the effective date of the bill; and (b) that the Legislative Fiscal Bureau make its determinations of the amount of GPR appropriated to which the appropriation limit would apply for the 2001-03 budget by the 15th day of the second month after the effective date of the bill. The bill contains no such provisions since the proposed appropriation limit would not be effective under the 2003-05 budget.

13. When proposals for appropriation limits have been discussed, an issue that has frequently been debated is what is the most appropriate measure to be used for calculating the allowable amount of increase? The use of personal income growth is probably most often advanced on the argument that it relates to a type of "ability to pay approach." Another factor that is sometimes suggested for use is the increase in the consumer price index (CPI) over some period of time. Any number of variations of these factors or others could be proposed. However, for the purposes of providing an example of how different factors might impact on the applicable budget base as proposed under both the bill and ASA 1 to 2001 AB 1, the comparison in Table 3 was prepared.

14. Table 3 compares, for the budget as recommended by the Governor and the final budgeted amounts for the 1999-01 and 1997-99 biennia, the limits that would result based on: (a) the projected percentage increase in state personal income growth factor that is proposed in both the bill and ASA 1; (b) the use of a factor based on that same projected percentage growth in state personal income less one percentage point; and (c) the use of a factor based on a percentage increase equal to 85% of the annualized increase in the CPI-U for the four calendar years immediately preceding the fiscal biennium to which the limit is to be applied.

TABLE 3

Comparison of GPR Budgeted Amount to Various Limit Amounts
Limits Calculated Separately for Each Biennium
($ in Millions)

Fiscal Biennium	Budgeted Amount	SB55/AB1 Factor	Limit Less Budget	Pers. Income Growth -1% Factor	Limit Less Budget	85% CPI Factor	Limit Less Budget
1997-99	$18,861.3	$19,031.5	$170.2	$18,760.2	-$101.1	$18,077.2	-$784.1
1999-01	20,952.6	20,599.4	-353.2	20,304.0	-648.6	19,701.7	-1,250.9
2001-03	22,504.0	22,887.3	383.3	22,557.1	53.1	22,060.8	-443.2

15. In considering this issue, the first question the Committee could consider is whether or not it wishes to establish a statutory spending limit of any kind. The argument could be made

that the determination of the appropriate level of taxes to be raised and the level of spending to be authorized in any fiscal biennium is something that needs to be assessed each biennium as an integral part of the biennial budget process and that this is a primary fiscal responsibility assigned to the Governor and members of the Legislature elected to make decisions for that fiscal biennium. Further, it can be argued that one session of the Legislature cannot bind a future session of the Legislature. If the Committee does not believe any type of limit provision should be created, then it could maintain current law.

16. The Committee could also take action based on a view that this issue is already under consideration by the Legislature as a separate bill (2001 Assembly Bill 1) and that that bill has already passed the Assembly. The Committee could remove these provisions from the bill on the basis that this issue will be addressed by the Legislature through the separate legislation route.

17. Alternatively, if the Committee does wish to have the creation of such a limit included in the budget bill, the following are several options that the Committee could consider. One would be to approve the Governor's recommendation. A second one would be to approve the Governor's recommendation with the modification that the proposal in the bill be changed by substituting the determination procedures specified in 2001 AB 1, as passed by the Assembly, except retaining the provision that the appropriation limit provisions would first apply to the 2003-05 budget and including the exception from the limit of any payments from the proposed tax relief fund. A third alternative would be to modify the Governor's recommendation to include the alternative determination procedures proposed in AB 1 as passed by the Assembly (again except for the immediate applicability provision) and in addition substitute the use of either: (a) a percentage increase factor based on growth in state personal income less one percentage point for the same time periods as proposed under the bill; or (b) a percentage increase factor based 85% of the increase in the consumer price index (CPI-U) for the prior four calendar years immediately preceding the fiscal biennium to which the limit is to be applied.

ALTERNATIVES TO BILL

1. Approve the Governor's recommendation.

2. Modify the Governor's recommendation by substituting the determination procedures for computing allowable growth under spending limit as proposed in 2001 Assembly Bill 1 (as passed by the Assembly) for those corresponding provisions in the bill but retain the bill provisions that would make this limit first effective for the 2003-05 biennial budget.

3. In addition to Alternative 2, further modify the Governor's recommendation to provide that the calculation of the permitted increase percentage be instead based on the future year's projected annual percentage increase in state personal income less one percentage point.

4. In addition to Alternative 2, further modify the Governor's recommendation to provide that the calculation of the permitted increase percentage be instead based on 85% of the increase in urban consumer price index (CPI-U) for the four calendar years immediately preceding

the fiscal biennium to which the limit is to be applied. *[Note: Alternatives 3 and 4 cannot both be adopted.]*

5. Remove the provisions from this bill on the basis that a separate bill dealing with this issue is already under consideration.

6. Maintain current law. *[Note: Either Alternative 5 or 6 will result in the same change to the bill itself.]*

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