MISSOURI STATE AUDITOR'S OFFICE
FISCAL NOTE (06-19)

Subject

Initiative petition from Patrick Tuohey regarding a proposed constitutional amendment adding a new Article XIV relating to state spending, version 2. (Received March 1, 2006)

Date

March 21, 2006

Description

This initiative petition would add a new Article XIV with subsections to the Missouri Constitution. The initiative petition would prohibit the state, in any fiscal year, from increasing fiscal year spending above the State Spending Limit. The State Spending Limit would include: (i) the total amount of fiscal year spending in the preceding fiscal year increased by a percentage amount equal to the result obtained by adding the percentage change in inflation plus the percentage change in state population from January 1 of the year in which the immediately preceding fiscal year began to January 1 immediately preceding the start of the fiscal year for which the appropriation is to be made or (ii) the State Spending Limit for the previous fiscal year; whichever is greater.

The State Spending Limit calculation for a fiscal year may be increased if the following conditions are met: (a) the decision to increase the State Spending Limit receives approval of a two-thirds vote of each legislative chamber and the approval of a majority of voters casting ballots at a statewide general election; and (b) the maximum total dollar amount of the proposed increase in the State Spending Limit is predetermined legislatively, limited to altering the spending limit for a specific fiscal year and a prominently placed ballot advisory.

Whenever spending limit revenues exceed the State Spending Limit for a fiscal year, the excess revenues not otherwise rebated to taxpayers pursuant to Article 10, Section 18(b), or specifically distributed or reserved by a provision of this constitution shall be designated as "surplus" and assigned to the Emergency Reserve Fund and the Revenue Shortfall Reserve Fund.

Surplus revenues will be deposited into the Emergency Reserve Fund until the fund balance is equal to 3% of the State Spending Limit. Money in the Emergency Reserve fund may be expended only for an emergency declared by law. Appropriation from the fund may only occur upon a three-fourths approval vote of all elected members of each house of the General Assembly. Interest income shall accrue to the fund and unused revenues shall carry forward to the next fiscal year.

After any amount required to be transferred to the Emergency Reserve Fund, any remaining surplus shall be transferred to the Revenue Shortfall Reserve Fund. The amount transferred to the Revenue Shortfall Reserve Fund shall be equal to the lesser of (1) the amount necessary to bring the total of the Revenue Shortfall Reserve Fund to an amount equal to 10% of the State Spending Limit for the ensuing fiscal year, or (2) the amount equal to 50% of any such remaining excess amount of total state revenues. Income earned on the Revenue Shortfall Reserve Fund shall accrue to the fund.

For any fiscal year that commences on or after July 1, 2008, if the total amount of spending limit revenues is less than the amount of the State Spending Limit, the state treasurer may transfer money from the Revenue Shortfall Reserve Fund to the general fund from the available funds in the minimum amounts necessary to offset the shortfall.

Any remaining surplus shall be rebated to those individual taxpayers who have filed personal income tax returns with the state in proportion to the tax liability of all such taxpayers equal to the amount of any remaining surplus. Rebates shall be in the form of checks payable to each taxpayer for any amount not offset by an existing tax liability and exceeding $25 for the 2007-2008 fiscal year. Any rebate amount not distributed or credited to individuals within 180 days of the end of the fiscal year shall bear interest of 4% per annum above the Federal Funds Rate.

The amendment is to be voted on in November, 2006, or at a special election called by the governor.

Public comments and other input

The State Auditor's Office received input from the Attorney General's Office, the Department of Agriculture, the Department of Higher Education, the Department of Health and Senior Services, the Department of Mental Health, the Department of Mental Health, the Department of Corrections, the Department of Labor and Industrial Relations, the Department of Public Safety, the Department of Social Services, the Governor's Office, the House of Representatives, the Department of Transportation, the Office of Administration, the Public Defender, the Secretary of State, the State Treasurer's Office, Adair County, Rockwood School District, Hannibal 60 School District, the City of Joplin, the City of Wentzville, Linn State Technical College, Metropolitan Community College, and St. Louis Community College.

Assumptions

Officials from the Attorney General's Office indicated the costs associated with implementing the proposed initiative petition can be absorbed with existing resources.

Officials from the Department of Agriculture indicated the fiscal impact of the petition is unknown. There is likely to be less funding available for the operation of department programs in high revenue growth years (compared to current law) and more funding available in low growth years. However, the specific impact is dependent upon economic conditions in a given fiscal year and future budgetary priorities, both of which are difficult to predict accurately.

Officials from the Department of Higher Education indicated the fiscal impact of the initiative petition to the department is unknown. However, as higher education receives approximately 82 percent of its budget from General Revenue, any limitations placed on these funds or change in the distribution of these funds may negatively impact higher education in Missouri.

Officials from the Department of Health and Senior Services deferred to the Office of Administration for the fiscal impact. The proposal could have significant, far-reaching impacts on the operation of state government and the services it provides. It is impossible to estimate the specific impact on the Department of Health and Senior Services because the proposal pertains to overall state spending. Even if it constrained spending below the level that would have occurred absent the proposal, it would be up to the legislature to choose how to apportion permissible spending amongst departments. The proper way to analyze the proposal is in reference to the overall state spending that would be allowable with and without enactment of this proposal.

Officials from the Department of Mental Health deferred to the Office of Administration for the fiscal impact of the proposed amendment.

Officials from the Department of Natural Resources deferred to the Office of Administration for the fiscal impact of the proposed amendment.

Officials from the Department of Corrections indicated the primary impact would be to the legislative prerogative to determine the level of appropriation of state funds. The fiscal impact to the Department of Corrections would depend upon the collective will of the legislature when appropriating fund. Therefore, the impact is unknown at this time.

Officials from the Department of Labor and Industrial Relations indicated the initiative petition would not have a fiscal impact on their agency. They did express some concerns. Section 3(3)(a) permits expenditures only when an emergency has been declared by law, but does not define who determines the emergency.

The first sentence of Section 3(3)(b) is unclear. Specifically, the Department cannot determine what the phrase "an amount of any remaining surplus" is intended to mean.

Section 3(3)(b)(ii) states the State Treasurer may transfer money from the Revenue Shortfall Reserve Fund in the first sentence and then in the second sentence states "Under no circumstances shall the State Treasurer transfer money…" This appears to be a contradiction.

Officials from the Department of Public Safety indicated they are unable to determine the possible fiscal impact in dollars. They do, however, believe this could curtail their ability to budget for replacement equipment, cars, program expansion, etc., as this type of item is only budgeted as the need for funding arises.

Officials from the Department of Social Services indicated the fiscal impact to the Department of Social Services cannot be determined because of a number of variables. If the state budget, as determined by the legislature to meet the state's needs, does not exceed the State Spending limit, there is no fiscal impact. Similarly, if the voters approve a budget higher than the State Spending Limit, there would be no fiscal impact. However, if the state's need, as expressed by the budget approved by the legislature, exceeds the State Spending Limit and the voters do not approve of spending in excess of the State Spending Limit, then the budget would have to be reduced to an amount less than the State Sending Limit. In this case, it is impossible to say how funds would be allocated among the various state Departments and functions. It is certainly possible that adequate funds would not be available to continue the existing programs in the Department of Social Services, resulting in a cutback of services.

Officials from the House of Representatives indicated the initiative petition would have no fiscal impact on the agency.

Officials from the Missouri Department of Transportation (MoDOT) indicated the initiative petition would impose some significant state spending limitations on state government, and much like the Hancock Amendment, would have to be determined based on an evaluation of all state revenues from all state funds. As a result, fluctuations between incoming revenues from these various funds could impact whether the state spending limitations are violated; however, it also makes it difficult to determine whether the initiative petition would have any impact on state spending, and the Highway and Transportation Commission/MoDOT spending in particular. Due to the broad language relating to state spending limitations in the petition, the fiscal impact to the Highway and Transportation Commission/MoDOT, if any, cannot be determined. The fiscal impact could be $0 or a negative unknown.

The Office of Administration (OA), Division of Budget and Planning, calculated the fiscal impact on the proposed initiative petition related to a state spending limit. The proposal would have an impact of a $280.6 million reduction in state appropriations for fiscal year 2008.

The OA made the following assumptions:

- Section 2(5)-definition of state-did not include [revenue from] institutions of higher education.
- Section 2(8)-definition of spending limit revenues-used the figures for total state revenues as defined in Article X, Sections 16 through 24.
- Section 2(8)(d)-exclusion of certain funds-used the definition determined by the Division of Accounting; used the FY2007 Governor's recommended budgeted amounts from the statewide financial system. OA further assumed that the revenues and expenditures from these funds would be identical.

- Section 2(8)(f)-payments of user charges and fees-estimated the amount from 12 revenue service codes deemed to be user charges or fees. OA further assumed these charges and fees do not exceed the cost of providing the service and the revenues and expenditures from these funds would be identical.
- Section 3(1)-the spending limit was reduced by the same exclusions on the revenue limit:
- Section 3(1)-inflation figures (3.18%) are from the U.S. Census Bureau 2005 consumer price index; population figures (.71%) are from July 1, 2005 estimates provided by the state demographer and do not include military personnel stationed overseas.

The OA did not attempt to project the impact of the proposal for fiscal years 2009 and 2010 because doing so would require a great many estimates of future CPI levels and population statistics making any projections highly subjective.

FY 2007 Total Fiscal Year Spending	
Description	**FY2007 Amounts**
Total Appropriations – Governor's Recommendation	$21,081,568,778
Less Federal Funds	7,386,589,710
Less Bond Sale Proceeds	0
Less Debt Service	208,092,250
Less Fund Exclusions	398,634,121
Less Monies Transferred from the Emergency Fund	0
Less Discretionary User Charges or Fees	99,710,746
Less Sale of Government Property to Non-Governmental Entities	506,389
Less Gifts or Bequests	2,832,156
Adjusted Total	$12,985,203,406
% Change	3.89%
Estimated State Spending for FY2008	$13,490,327,818
Estimated Spending Limit for FY2008	$13,209,757,040
Difference	$280,570,778

Officials from the Office of the State Public Defender indicated it is impossible to determine whether or not this constitutional amendment would have any fiscal impact on the State Public Defender System. There is no guarantee as to the percentage of the whole for any state agency and funding could/would be adjusted.

Officials from the Secretary of State's Office indicated the petition does not have any specific cost to the Office of the Secretary of State other than the cost of newspaper publication in advance of the election that is required should enough valid signatures be collected to result in the issue being placed on the ballot. The Office of the Secretary of State deposits revenue into its funds that would both be counted and excluded from the calculations of the spending and revenue limit. For example, revenues that would be excluded for the Office of the Secretary of State include donations, gifts, and bequests that come to the Wolfner Library Trust Fund. They have contacted the Office of

Administration Division of Budget and Planning and understand that they are calculating the overall limit for the state. They assume that the Office of the Secretary of State would be affected in the same manner as other state agencies for increases or decreases in spending that might be required after the effective date of this act. At this time, the impact of the amendment is unknown and is dependent upon the growth in the economy and many other factors.

Officials from the State Treasurer's Office indicated the petition would have no fiscal impact on their office.

Officials from Adair County indicated any reduction is state revenue coming to Adair County would have an adverse effect. They provided a partial listing of grants and revenue generating programs that affect Adair County. Loss of any of the programs would result in a disservice to the citizens of Adair County.

Officials from Rockwood School District indicated the primary intent of the petition is to impose a state spending limit upon the Missouri State government. The "state" as defined in the petition includes all branches of state government including the offices, authorities, agencies, boards, commissions, institutions, instrumentalities, and any division or unit of state government which are directly supported in whole or in part with tax funds. Obviously the proposed constitutional amendment would include school districts under the terms of this new spending limit.

The limitations established by the petition appear to be relatively similar to the existing Hancock Amendment in that state spending would be limited to the amount of spending in the preceding fiscal year with increases permitted for inflation and the percentage change in state population. It appears that this petition would supersede the ability of local taxpayers to enact locally approved tax increases to meet the needs of local school districts. This appears to be the case because the petition states that the state's spending limit could be increased only upon meeting certain conditions including the approval of two-thirds of each legislative chamber and the approval of a majority of voters at a statewide general election.

The Rockwood School District would be opposed to this initiative petition primarily because it would override the local control provided by our locally elected Board of Education as well as circumventing the ability of the taxpayers in our district to enact additional taxes to meet identified needs. In addition, the expenditure growth in a local school district could substantially vary from the limitations imposed by this petition. Expenditure growth in school districts is primarily driven by the number of students served. Due to demographic changes across the state it is quite possible that the number of students served in Rockwood or by all districts throughout the state could grow at a different rate than the percentage change in the overall state population. Furthermore, inflationary costs in school districts are often substantially different from the change in the Consumer Price Index. About 80% of all school district expenditures are incurred for salaries and benefits. While our salary increases may approximate the rate of inflation, frequently our benefits will increase at a substantially greater rate. Like most businesses, most school districts have experienced health care cost increases substantially greater than the general inflation rate. School districts are also required to make mandatory contributions to the state established employee retirement systems and these systems have been requiring annual increases in all school districts' contribution rates to meet the actuarial requirements of the statutorily provided benefits (all employees participate in these defined benefit plans). The increase in our school textbook and other instructional materials, natural gas price increases, and diesel fuel costs for our school buses are but three additional examples of areas in which school district costs have substantially exceeded the rate of inflation.

It also appears the amendment would be contrary to the intent of the revised school funding formula as included in SB287 passed by the legislature in 2005. This legislation was passed to attempt to address constitutional concerns related to the adequacy and equity of school funding by increasing and revising the distribution of State aid in support of K-12 public education. By limiting State funding of education, this amendment could undermine the legislature's efforts to adequately fund public education.

Because of the above-described concerns this legislation has the potential to have a significant adverse fiscal impact on the Rockwood School District as well as all school districts across the State of Missouri. School districts need to continue to be locally controlled by locally elected boards of education with local taxpayers retaining the ability to determine the fiscal needs of their districts.

Officials from the Hannibal School District #60 indicated the amendment would take control away from the local educational agency (LEA) which produces the concern that additional dollars will be taken away from the LEA. This is a very "broad" amendment and is therefore hard to calculate exactly how much of a fiscal impact it will have on the school district.

Officials from Linn State Technical College indicated that the true fiscal impact for the College is unknown at this time. They stated that the petition would provide state taxpayers the opportunity to vote on spending limits within State Government and establishes a surplus fund that could be used in times of fiscal crisis in the State of Missouri. The spending limit requirements would cost the State of Missouri millions of dollars to implement. Costs directly related to a statewide general election. The percentage change in inflation and the percentage change in the population may not keep pace with the cost of mandatory increases such as wages, benefits and consumables. Therefore, a continuous need for ballot measures would be necessary to meet the minimum increases. To manage a state spending limit could become quite costly for the state to administer.

Officials from Metropolitan Community College (MCC) used an historical period of growth in funding to estimate the fiscal impact. Between fiscal years 1992-93 to 2000-01, state general revenue growth was about 77%. MCC funding over this period increased approximately 104%. The U.S. City Average Consumer Price Index for All Urban consumers increased only 23%. If this amendment had been in effect during the period, state funding would have only increased 23% instead of 77%. If that had been the case, then MCC would have only received about 69% of the funding they did receive that year and the peak state aid revenue in 2000-01 would have only been $24.6 million, instead of the $35.6 million they did receive, or about $11.0 million less.

This would have been severe to say the least. In order to compensate for this lost revenue, MCC would have had to increase the average tuition rate by approximately $32.50 per credit hour, which would have had a drastic impact on enrollment. Since as a community college they are all about access, that solution would have been a non-solution anyway, since they would never increase tuition to those levels to solve a revenue problem of this type.

Officials from the City of Wentzville indicated the fiscal impact is "unknown" at this time.

Officials from the City of Joplin indicated they have several concerns regarding the affect this amendment would have on local and state government. This would certainly create a negative fiscal impact for the City of Joplin, if it would indeed apply to the city. The City of Joplin operates under the "pay as you go" philosophy, ultimately to try to save taxpayers money. It has been our philosophy to build up fund balance for a period and then make large capital purchases at certain times. The city avoids borrowing money to pay for certain items, thereby avoiding interest payments at the expense of taxpayers. So, there are many years that we spend less than we bring in and many years that we spend into fund balance.

Furthermore, they have a philosophical issue with legislatures trying to dictate what the city considers to be accounting rules. The city understands what legislatures are trying to accomplish with this type of legislation. But, the city believes that good internal controls, policies that are written and enforced, and audits can accomplish the same thing. Accounting rules, to a certain degree, address a lot of what legislatures are trying to protect.

These types of constitutional amendments tie the hands of what governments need to accomplish to provide services to its taxpayers. It is costly to have elections. To put in place a mechanism for an election any time that the state spends certain funds is much more detrimental than beneficial.

Officials from St. Louis Community College indicated that the fiscal impact of the petition would be best determined by the Office of Administration. They indicated that 1% reduction in state aid equates to approximately $440,000 which means that the college would have to cut some services, increase the burden on their students with higher fees, increase the burden on the local property tax payers or a combination of all three actions.

The State Auditor's Office did not receive a response from the Department of Economic Development, the Department of Elementary and Secondary Education, the Department of Conservation, the Office of the State Courts Administrator, the Senate, Cass County, Taney County, St. Charles County, Cape Girardeau 63 School District, the City of Springfield, and the University of Missouri.

Fiscal Note Summary

The estimated fiscal impact on state government is approximately $280 million for fiscal year 2008. The impact on state government for future years is unknown. The impact on local government is unknown.