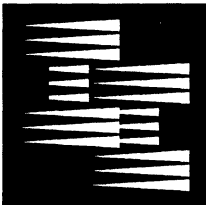


# INDEPENDENCE ISSUE PAPER

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## Tax and Spending Limits for Montana? Criteria for Assessing Current Proposals

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Sept. 19, 1994

## Tax and Spending Limits for Montana? Criteria for Assessing Current Proposals

*by Robert G. Natelson*

### *Executive Summary*

- This November, Montana voters will consider two proposals to place Tax-Expenditure Limitations (TEs) in the state constitution.
- There is a clear inverse correlation between level of state and local government revenue and comparative economic growth. From 1969 through 1984, for example, Montana state and local government revenue rose sharply, both in absolute terms and as a percentage of income. Montana's economic performance began to lag the nation a few years after this period began, and continued to lag until a few years after this period ended.
- From 1985 through 1991, the growth of government revenue was more restrained. Toward the end of this period, Montana personal income growth again began to outpace the rest of the nation.
- Recent legislative efforts to revive the high-spending, high-tax policies of the 1970s and early 1980s have prompted Montana citizens to propose two constitutional initiatives to control government's fiscal appetite. Constitutional Initiative 66 would require public approval of tax increases. Constitutional Initiative 67 would require legislative supermajorities for increases in taxes, fees, or spending.
- Over half of the states already have some form of tax-expenditure limitation.
- Opponents of tax and spending controls claim that Montana is "different" economically from the rest of the nation and requires a higher level of government. Careful examination reveals little support for this claim.
- The experience of other states shows that TEs that are not drafted carefully may prove ineffective or counterproductive. The author subjects both CI-66 and CI-67 to a 10-item test to gauge their likely effectiveness.
- Although both measures have various advantages and disadvantages, CI-66 likely would be more effective in practice. CI-66 and CI-67 are not legally inconsistent.

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# I. Introduction

Should Montana adopt a constitutional limit on taxes or spending? In this paper, I argue that such a limitation would serve the general welfare. But I also argue that each proposal needs to be judged on its own merits, employing certain criteria. I then show how those criteria might be applied to two current proposals: CI-66 and CI-67.

## II. Does Government Tax and Spend Too Much?

A substantial amount of research suggests that government taxing and spending are now at higher than optimal levels, especially given current methods of government service delivery. The research takes two forms: Studies of government operations and studies of the comparative economic performance of regions with more or less government. The findings form a good starting point for deciding whether Montana should adopt a constitutional limitation on taxes or spending.

### A. Research into government operations.

Representative democracies traditionally have featured popularly-elected legislatures operating by majority voting rules and either dependent executives (prime minister, cabinet) or independent executives (president, governor). These officials oversee bureaucracies organized more or less in pyramid fashion. Although modern representative government certainly is better than anything that has gone before, citizens have long been aware that it is not perfect—and that insight is supported by new and important research.

One imperfection appears to be that current structures result in more spending and special interest legislation than the general populace either needs or wants. This is not what one might expect. One might expect a legislature elected by a majority and operating by majority rules to reflect majority will. Further, one might expect a conscientious civil service to execute faithfully the orders of elected representatives. But this is not happening.

Part of the problem appears to be that traditional legislative structures create voting paradoxes, strategic voting, “logrolling,” and special interest influence—all of which impair the quality of legislative decision making.<sup>1</sup> Similarly, traditional bureaucratic structures encourage overstaffing, overproduction, and/or underperformance.<sup>2</sup> (Economists call the last problem “shirking”, and it becomes a factor later in our discussion.) Not surprisingly, therefore, empirical investigation has found that government enterprises are significantly less efficient than their private sector counterparts.<sup>3</sup>

## B. Partial confirmation from other research.

Tending to confirm government operations research are studies comparing economic growth rates in regions with different amounts of government. Most of these studies compare American states.<sup>4</sup> The state studies are particularly useful because American states are polities of substantial size that offer competing "policy packages" in a common market.<sup>5</sup>

The comparative state studies can be organized into three classes, with the first two classes yielding only mixed results and the third much stronger results. The studies showing mixed results include (1) those performed before the mid-1970s, which use cruder statistical techniques, unreliable independent variables (e.g., the results of business questionnaires), or narrow dependent variables (e.g. branch plant locations) and (2) newer studies relying on narrow measures of government and/or narrow measures of economic growth.<sup>6</sup> The studies showing stronger results are newer statistical analyses<sup>7</sup> of certain broad measures of government activity and broad measures of economic growth.<sup>8</sup> The better studies incorporate time lags between policy variables and economic variables.<sup>9</sup>

In general, this third group of studies shows strong correlations between larger and expanding government and *slower* relative economic growth in subsequent years. Correspondingly, it also finds correlation between smaller and shrinking government and *faster* relative economic growth in subsequent years. (In the state studies, the size of government at any one time seems less important than whether government is expanding or contracting.) Moreover, when we consider this third (broad variable) group together with the second (narrow variable) group, we can infer that the total size of government is more important than the state's particular mix of taxes and services—at least within broad limits.<sup>10</sup>

In sum, both research on operations and research on taxing and spending levels tend to support the thesis that government activity is at higher than optimal levels, and that changes in government decision making is necessary to promote the general welfare.

## III. Is Montana Different?

### A. Introduction.

When confronted with national research findings, a common response from Montana politicians is that Montana is different, and that rules generally applicable do not apply here because of unique and distinguishing factors. Thus, Montana is said to be unique because of (i) distance from markets, reliance on extractive industries, and small population (all supposedly explaining subpar economic growth); (ii) presence of severable

minerals and large numbers of tourists (justifying attempted tax “export”); and (iii) sparsity of population over a large geographical area (justifying an unusually large public sector).<sup>11</sup>

However, there is not much support for the view that the rules of the game are much different in Montana than in other states. First, many of Montana’s allegedly “unique” characteristics *are* common to other states. Large tourist industries, for example, are characteristic of California, Wyoming, Colorado, Florida, Hawaii, Nevada, New York, and other states. Second, there is no inherent reason why population sparsity should require more government than population density (with attendant urban problems), or why Montana should need far more government employees per capita than the sparsely-populated states of North Dakota, South Dakota, Nevada, or Idaho. Finally, the claim that Montana is somehow “different” loses its force when professional researchers control for such differences, yet still derive the same results.<sup>12</sup>

## **B. Support from recent history.**

Moreover, examination of Montana economic history over the past quarter-century does not support the view that Montana is immune from national connections between government policy and economic growth.<sup>13</sup> This can be shown by comparing many different types of statistics.<sup>14</sup> Because of space limitations, two variables will have to suffice. The first variable is a measure of the size of government: state and local government revenue as a percentage of Montana personal income—“OSR” (for “Own Source Revenue”). The second variable is Montana’s personal income growth in subsequent years relative to other states.

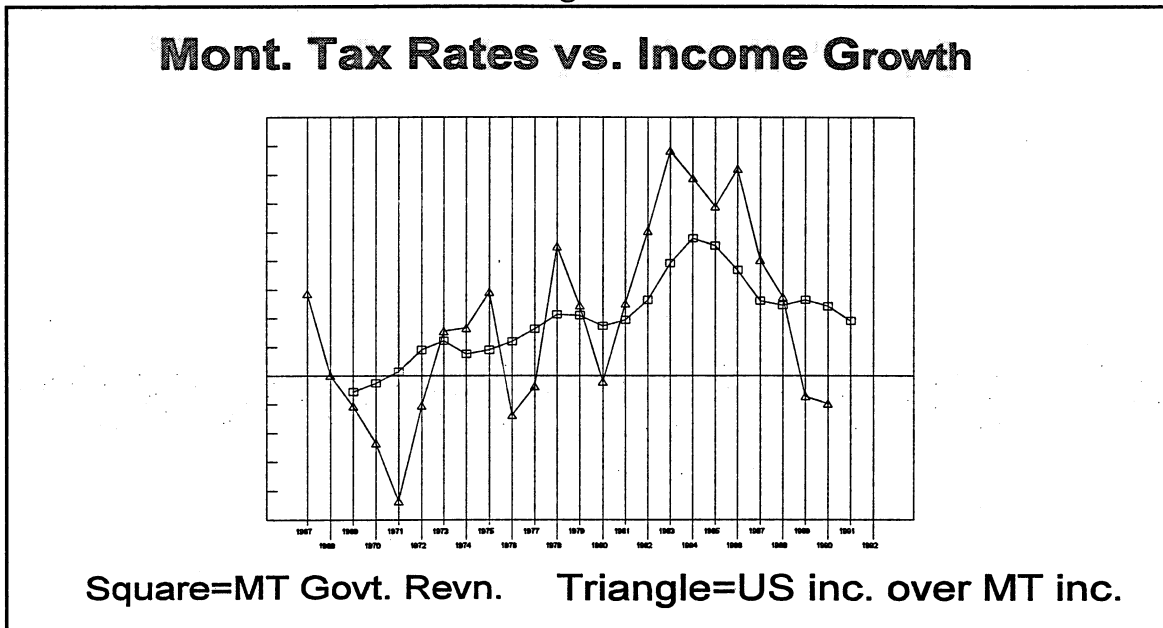
**1. Montana vs. the nation.** In 1969, Montana OSR was 15.3% of personal income, 17th among all states.<sup>15</sup> About that time, however, state politicians decided to increase greatly government’s share of the state economy. By 1972 OSR had grown to 17.7% on a much larger income base.<sup>16</sup> National research might predict relative economic decline 2-5 years after such a large increase. This happened: Beginning in the mid-70s, Montana began a period of underperforming the rest of the nation in personal income growth.

In the late 1970s and early 1980s, government’s share of the Montana economy continued to jump. Relative to other states, Montana OSR was 12th in the U.S. in 1975 and fourth in 1984. While part of this increase was due to higher severance taxes, there were steep hikes in other levies as well. For example, from 1969 to 1979 the amount of inflation-adjusted dollars paid in personal income taxes more than doubled, and the share of income Montanans paid in income taxes rose nearly 61%.<sup>17</sup> Montana’s economic underperformance, as measured by personal income growth, continued to be severe during this period.

After 1984, government revenue growth was more restrained: it no longer outraced growth in Montana personal income. By 1989, Montana had dropped from fourth to eleventh among states in OSR. Research would predict that, other things remaining equal, this development should be followed by good economic news. Once again, this happened: In 1989, Montana's personal income growth outstripped the nation for the first time in nearly a decade, while in 1991 Montana's personal income growth led the nation.

The following chart shows the correlation between a two-year rolling average of annual OSR and a *lagged* two-year rolling average of how much the nation's percentage of personal income growth exceeded Montana's percentage of personal income growth:<sup>18</sup>

Figure 1



The line with square points represents Montana in-state government revenue, as a percentage of personal income. The line with triangular points represents the degree to which US income growth outperformed Montana income growth two years later. In general, the higher the Montana government's share of the economy goes, the more the rest of the country outperforms Montana.

**2. Montana vs. the region.** A comparison of Montana with nine other states in the region<sup>19</sup> also lends no support to the hypothesis that Montana is insulated from the tax/economic associations observed for the nation as a whole. In the six years previous to 1974 (when the "big government" policies were being instituted, but when the effect could not yet have been fully felt), Montana personal income growth closely approximated the rest of the region. But after 1974, Montana personal income growth lagged her neighbors by a wide margin—a margin even wider than that by which Montana personal income growth lagged the nation. Of the ten states in the region, Montana's economy



outperformed only that of North Dakota—which also generally pursued big government policies.<sup>20</sup>

**3. Montana vs. Idaho.** Montana and Idaho form a useful case study. In 1969, Idaho was a state very much like Montana: reliant on extractive industries, far from markets, sparsely populated, with no significant urban centers. Moreover, each state routed a similar percentage of its economy through government: Idaho had an OSR of 15.9% *versus* Montana's 15.3%. But while Montana expanded government, Idaho kept it in check. By 1975, Montana's OSR had risen to 17% while Idaho's had dropped to 14.7%. In 1985, the figures were 20.2% for Montana and 14.8% for Idaho.

Now look at these states' respective economic histories: In 1969, personal income in Idaho was 2.4% less than personal income in Montana. In 1991 it was 26% *more*. Today, Idaho remains sparsely populated with all the rural delights of the Great Northwest—but it also has become an important high-technology state. Boise was once smaller and sleepier than Great Falls, but is now a thriving economic center. Just as Montana cannot match Idaho's success, neither Great Falls nor any other major Montana town can match the success of Boise.

**4. The lessons of a quarter-century.** The foregoing statistics give no support to the notion that Montana can pursue "big government" policies and avoid the economic consequences generally associated with them. On the contrary, they suggest that Montanans cannot pursue such policies without suffering similar consequences.

## IV. 1992-94: Montana's Return to High Tax Policies

### A. Taxes, Taxes Everywhere.

Since July 1992, Montana reverted to the taxing policies of the 1970s. That month, a Democratic-controlled legislature "solved" a budget shortfall with a seven percent, across-the-board hike in virtually every tax in the state—the "seven percent solution." Retiring Republican Governor Stan Stephens objected, but allowed the measure to become law without his signature.

In the autumn of 1992, Republicans campaigned against the seven percent solution, picking up control of the state house of representatives while retaining the governorship. Republicans then proposed tax increases of their own. In subsequent months the legislature imposed steep hikes in fuel, income, and payroll taxes; raised mandatory fees; and adopted a school equalization bill that triggered large increases in local property taxes. Even after the income tax hike (H.B. 671, now IR-112) was suspended by citizen petition, the

aggregate annual state-local tax burden may be nearly \$200 million higher than it was in early 1992. Had voters not defeated the sales tax and suspended the backup income tax, the increases would have been much larger.

The decision by the Governor and 1993 legislature to raise taxes at a time when most states were freezing or reducing them received wide-spread, and unfavorable, national attention. One source reported that the 1993 general session's tax package represented the second largest proportional increase in the nation.<sup>21</sup> A fiscally-conservative study group awarded Governor Racicot an "F" for his revenue proposals and "D" for his overall fiscal policies.<sup>22</sup> A University of Maryland professor writing in *Forbes Magazine* called Racicot the "Jim Florio of Montana politics."<sup>23</sup>

Yet the tax increases still did not end. In 1994, Montana public school lobbyists began to characterize the ambiguous actions of the November 1993 special legislative session as a "cut" in state school aid. In many cases, they were able to convince voters to agree to further mill levy increases.<sup>24</sup>

## **B. The Political Response to Higher Taxes.**

Many Montanans objected to the return of high tax policies. The Republican successes of November, 1992 were widely attributed to dissatisfaction with the "seven percent solution." When the Republicans proposed further tax increases, a coalition of general interest groups, led by Montanans for Better Government, mobilized to convince the legislature to reject those proposals. When policy makers proved unresponsive, those groups led the charge against the R-111 sales tax proposal, which was defeated by a 3-1 margin. They then sponsored a citizen petition that suspended the backup income tax hike (H.B. 671, now IR-112).

Meanwhile, several groups began to consider more permanent solutions: constitutional tax and expenditure limitations. Thus, United We Stand America (Montana), one of the groups that sponsored the IR-112 petition, announced plans for a constitutional initiative to require public approval of all tax increases (CI-66). The Tax Equity Action Movement, another petition sponsor, drafted CI-69 to roll back property taxes to 1986 levels. And a group that did not participate in the suspension movement, Citizens Against Prolific Spending (CAPS), announced CI-67, which would require supermajority approval before any legislative body could raise taxes, fees or spending. Two of these measures—CI-66 and CI-67—gathered enough signatures to win spots on the November 1994 election ballot.

Amid this activity, the 1993 Montana legislature referred to the voters two preemptive<sup>25</sup> constitutional amendments involving taxes. Neither represents a serious attempt at tax or expenditure limitation, and therefore this paper does not examine them in detail. Suffice to say that C-27, which would cap any prospective retail sales levy to

four percent, was part of a design to induce voters to authorize *higher* government revenues through R-111. Because R-111 was defeated, C-27 limits a nonexistent levy. C-28 does not restrict revenues at all, but would amend the constitution to give lawmakers more power to allocate property assessments. The result would be to encourage further the special interest influence that has made the Montana property tax system one of the most convoluted in the nation. In short, C-27 and C-28 are the latest in a series of political attempts to sell tax reallocation as a substitute for limitation.

As of this writing, therefore, it appears that at the November, 1994 election Montanans will have the opportunity to vote on three important tax measures—the IR-112 income tax hike, CI-66 and CI-67. Because this paper is about constitutional tax and expenditure limitation, it focuses on CI-66 and CI-67.

## **V. Tax-Expenditure Limitations (TEs)**

### **A. Theory of Tax-Expenditure Limitations.**

The theory behind tax and expenditure limitations (TEs) is that they improve government decision making by reducing the influence of special interests (“high demand groups”) over the fiscal process. By limiting the amount of money politicians have at their disposal, TEs force decision makers to make tradeoffs among special interest groups rather than feeding them further at the expense of the general interest (i.e., through raising taxes). Carefully drafted TEs permit the waiver of those limits, but only through approval mechanisms designed to be more protective of the general interest (“middle demand groups”) than the usual legislative majority. The most popular approval mechanisms are legislative supermajorities and majorities of the whole electorate.<sup>26</sup>

TEs are, therefore, close cousins to constitutional restrictions on state debt, and they soon may be nearly as common. In fact, a majority of states now have at least one fiscal discipline mechanism—a formula for limiting taxes or spending, a supermajority requirement, a public vote requirement, or some combination.<sup>27</sup>

Not all TEs are created equal. Some have been more successful than others. A poorly drafted TE may either fail to restrain taxes and spending or actually cause more harm than good. In crafting a TE, therefore—particularly a constitutional TE—it pays to be cautious.

A fruitful way of judging a TE proposal is to ascertain the criteria for a successful measure and then test the proposal against those criteria. In identifying the criteria, two questions need to be asked:

1. Under what conditions will a TE actually restrain government taxing and

spending?

2. If the TEL actually restrains taxing or spending, is it nevertheless likely to do more harm than good?

## **B. Assessing a TEL's ability to restrain revenues or spending.**

Over the past decade, a fair amount of TEL scholarship has accumulated, much of it investigating whether TELs actually restrain taxes or spending.<sup>28</sup> When TELs are considered in the aggregate, they do not seem to have had much effect. But when we distinguish effective TELs from ineffective ones, we can identify criteria for success. A list and explanation of these criteria follow:

1. *The TEL must be constitutional rather than statutory.* Experience with statutory TELs has not been good: Partly this is because the legislature can alter an ordinary statute at any time. (This is usually true even when the statute is proposed by voter initiative.) Partly this is because statutory TELs often are “preemptive” measures—written by politicians to reassure the voters and thereby avoid more serious restrictions. Not surprisingly, preemptive TELs are generally lenient and easy to circumvent. The unsuccessful national experience with statutory TELs is paralleled in Montana.<sup>29</sup>

2. *The TEL must require some extraordinary procedure for raising taxes or spending.* Among procedures recommended are supermajorities in smaller (usually legislative) bodies and/or simple majorities in larger bodies (usually the electorate). The idea is to move critical decision making toward “middle demand” groups and away from the representatives of “high demand” groups.

3. *The TEL must ensure the integrity of the extraordinary approval process.* In most TELs, the process adopted is legislative, popular, or some combination of both. At the legislative level, the greatest problem can be to ensure accurate information flow; at the referendum level, it is necessary to protect information flow and the fairness and honesty of the election process.

4. *The TEL cannot permit taxes and/or spending to rise as fast as personal income or inflation.* When a TEL permits increases as large as personal income growth or inflation, then those ceilings tend to become floors, and government grows faster than personal income or inflation.

5. *Escape clauses must be drafted narrowly and must be difficult to trigger.* The research suggests that broad, undefined “emergency” clauses are a major reason for the ineffectiveness of some TELs.

6. *The TEL should cap more than estimated tax revenues.* Revenue estimates can

be inaccurate and are subject to manipulation. Hence, the TEL should cap other measures of fiscal growth, such as tax rates or spending.

7. *The TEL must be comprehensive.* Many, if not most, TELs are limited to particular level of government (e.g., state government), to a particular fund (e.g., the general fund), to a specific tax (e.g. the property tax), or to “taxes,” but not to mandatory fees. Although non-comprehensive TELs may be partially effective,<sup>30</sup> more carefully drafted TELs cover all fiscal exactions by government. Thus, a TEL should encompass all taxes and mandatory fees, whether appropriated at the state or local level.

8. *The TEL should not require official implementation.* Several TELs have become dead letters because the legislature refused to implement provisions that the legislature had responsibility to implement.

9. *The TEL should be enforceable by taxpayer suit.* A TEL likely never will be enforced unless individual taxpayers have standing to enforce it.

### C. Assessing the Non-Revenue Effect of a TEL.

The next question is, “If the TEL actually restrains taxing or spending, is it nevertheless likely to do more harm than good? In Montana, three principal arguments have been raised for the proposition that a TEL may not improve the general welfare. A fourth has received little attention in the current Montana debate. As it turns out, the three arguments that have been raised can be disposed of quickly, but the fourth is far more serious—especially in view of recent developments in our state.

The first argument is directed against the supermajority (required by CI-67) as a mechanism of decision making. As stated by Governor Racicot:

If a super-majority is such a darned good idea for revenue and spending bills, why don't we already have it for every other kind of bill?...our entire democratic system, with extremely rare exception, is based on half the voters plus one....Our government has always been based upon majority rule and CI 67 changes that concept, giving a minority the power to control revenue and budget issues.<sup>31</sup>

This argument is subject to at least two responses. First, it is *not* true that supermajority requirements are “extremely rare exception[s]” in our system of governance. The Montana Constitution, for example, contains nine different supermajority requirements, covering such matters as creation of state debt, legislative diversion of highway and coal trust funds, and veto override. Moreover, Montana statute *already* requires a two-thirds vote of the legislature to raise most state spending items above the rate of personal income growth.<sup>32</sup> The second response is that there is some evidence that

broader use of supermajorities actually is “a darned good idea” because it would improve the quality of political decision making, especially in bodies of relatively small size.<sup>33</sup>

The second argument, also raised by the Governor, is directed against the popular vote requirement of CI-66. The claim here is that popular votes would lead to more special interest taxation, as bare majorities sought to impose unfair burdens on minorities.<sup>34</sup>

As far as I can determine, however, this contention is without merit. As a conceptual matter, it is unclear how requiring a measure to pass a third legislative body (the electorate) would result in more special interest taxation than approval by the house and senate alone. More importantly, the contention receives almost no support from the history of Montana tax referenda,<sup>35</sup> while other empirical evidence strongly contradicts it.<sup>36</sup>

The third argument against change is that popular votes on legislation are contrary to the republican form of government. This contention is based on a too-literal reading of Madison’s papers No. 10 and 14 in THE FEDERALIST, which seem to say that republican government must be wholly representative. In later papers, however (Nos. 39 and 63), Madison makes it clear that a republic requires only *some* representative institution. This concession is necessary, for many republics, including the Roman, have been dominated or strongly influenced by institutions of direct democracy.<sup>37</sup> Montana’s Constitution, for example, already has at least 13 distinct popular vote provisions; adding a 14th would not constitute a radical alteration.

A far more serious objection to an effective TEL, but one that has received little currency in Montana thus far, is that, when faced with revenue restraints, bureaucrats will increase the extent to which they “shirk”—take leisure time or engage in activities that do not contribute to the missions of their agencies. If this happens to a sufficient extent, the bureaucracy will appropriate to itself most or all of the benefit of the TEL.<sup>38</sup> Furthermore, when services deteriorate the bureaucrats may use their agencies’ ineffectiveness as an argument for increased funding. And, indeed, this may be one reason the effectiveness of most TELs seem to tail off after five years or so.<sup>39</sup>

Note that this is not an argument against TELs in general; it is merely an argument that TELs must be coupled with “shirking control devices”—mechanisms to ensure the bureaucracy does the job it is supposed to do and does not divert its attention to other projects.<sup>40</sup> Shirking control devices could be enacted by the legislature or adopted as part of the TEL.

In theory, shirking control devices could be implemented by top-down micro-management of the bureaucracy. But in practice, this has proven neither feasible nor desirable. Most experts now recommend shirking control through properly-structured competition: competition between local governments, competition among agencies serving the same area, and sometimes competition from the private sector.<sup>41</sup> The prospect of

competition, however, triggers another sort of bureaucratic behavior:

After a [TEL], therefore, bureaucrats have an incentive to lobby for those measures which reduce the productivity of shirking control devices. As described above, one means of doing this involves decreasing the number of alternative suppliers. This may be accomplished by a consolidation of bureaus within the bureaucracy. Other options for decreasing competition may also be available. For instance, a [TEL] placed on local government may elicit not only consolidation within a bureaucracy, but also consolidation among different local government units.<sup>42</sup>

Thus, we arrive at the final criterion for assessing a TEL:

10. *The TEL must include effective shirking control devices, or at least not inhibit the legislature's resort to such devices.*

We now proceed to examine currently-proposed TELs according to those criteria.

## VI. Tax Limitation for Montana: Assessing the Options

The two potentially meaningful TELs on the November, 1994 ballot are CI-66<sup>43</sup> and CI-67. We now apply the criteria identified above to each of them.

1. *The TEL must be constitutional rather than statutory.*

Both CI-66 and CI-67 are constitutional rather than statutory TELs, and both therefore satisfy this criterion.

2. *The TEL must require some extraordinary procedure for raising taxes or spending.*

Both CI-66 and CI-67 implement extraordinary procedures. CI-66, which is a cap on taxes only, would require a majority vote at a referendum in the district where any tax increase was proposed. CI-67, which caps both taxes and spending, would require a two-thirds vote of the state legislature or a vote *in excess* of two-thirds of any other legislative body.

While both approaches—supermajority of a legislative body, majority of the electorate—find support in the research, there is some evidence for believing that decision making by a majority of the electorate may be superior to that of a supermajority of the legislature. Research suggests that a two-thirds vote may be higher than optimal for a body the size of the Montana house of representatives.<sup>44</sup> Existing TELs, most of which rely on

legislative supermajorities, have won only modest success in restraining taxes and spending.<sup>45</sup> Research further suggests that electoral majorities are highly efficient processors of economic information.<sup>46</sup> Finally, if the goal is to move decisions from the “high demand” groups to the “middle demand” groups, then electoral approval seems to be a better way to do this than even supermajority approval in a body like the Montana legislature, at least a third of whose members are government employees or retirees.

3. *The TEL must ensure the integrity of the extraordinary approval process.*

In Montana, legislative action sometimes has been clouded with deceptive or incomplete information from the bureaucracy. CI-67, which relies on legislative supermajorities, makes no provision for improving this situation. On the other hand, CI-67 does not block appropriate reform.<sup>47</sup>

An analogous problem for CI-66 is that the tax referendum process has been compromised in Montana, especially (but not exclusively)<sup>48</sup> during school levy campaigns—the obvious prototype for CI-66 referenda. Specifically, school levy campaigns have been marred by such practices as:

- (1) repeated elections until the voters “get it right” (i.e., approve the levy),
- (2) government subsidy of pro-levy promotion,
- (3) localized press blackouts of anti-levy points of view,
- (4) repeated failure by levy promoters to comply with the financial rules governing political spending, and
- (5) official threats, especially against schoolchildren and their parents.<sup>49</sup>

Moreover, school levy referenda often draw a small percentage of the voters, allowing special interests to exercise disproportionate influence over the result. It is sobering to think of regular statewide referenda being corrupted by the same process.

Offsetting this problem somewhat is the fact that existing voter information pamphlet law<sup>50</sup> may mitigate the information imbalance and the fact that CI-66 includes some provisions designed to minimize abuse. Thus, under Section 15(5) of CI-66, tax referenda may be held no more than twice a year, and during even numbered years these must be the primary and general election dates—to ensure reasonable voter turnout. Further, under Section 15(1)(a), the tax increase proposal must be “clearly describe[d]” and include a “reasonably estimated annual dollar amount.” Taxpayers may sue to enforce these rules. Section 15(10).

Nevertheless, CI-66 does provide insufficient protection against some electoral abuse, especially threats and other official interference in electoral campaigns. Of course, CI-66 does not prevent appropriate electoral reform by the legislature or by voter initiative.



4. *The TEL cannot permit taxes and/or spending to rise as fast as personal income or inflation.*

It is reasonable to predict that CI-66 would cap revenues at levels below personal income or inflation. Section 15(7) of CI-66 apparently would permit revenue from existing income tax or excise rates to rise with economic activity. Under Section 15(2)(c), however, the amount receivable from property taxes would not rise with property values; instead, revenues would increase only if there were new construction or capital improvements. Mandatory fees would be capped at their current dollar amount [Section 15(4)].

This mixed approach to tax limitation—whereby income tax and excise revenue rises with economic activity, while fee and property tax revenue rises more slowly—is an appealing one. It gives policy makers incentives to adopt measures to improve the economy, because those policy makers receive *more tax revenue* as economic activity expands. On the other hand, the stricter limits on property taxes and fees renders it probable that government's *overall share* of the economy gradually will diminish.

It is less certain whether CI-67 would cap taxes and spending below the rise in personal income or inflation. Section 15(1) states that political units may not “increase any tax or fee....” Under the “ordinary meaning” rule of construction, as applied to taxes where revenues rise with economic activity, this probably means an increase *in rate* rather than in amount of revenue. Section 15(2) states that “[a]ppropriations...shall not exceed the actual expenditures in the previous appropriation cycle.” Under the same rule, appropriations probably would be measured by the *nominal dollar amount* appropriated previously, including federal aid. So a two-thirds vote would not be needed to receive more tax dollars but would be necessary to appropriate more tax dollars. In the real world, if a revenue rise comes from existing tax rates or from the federal government, legislatures probably will appropriate the extra money as a matter of course.<sup>51</sup>

Two further caveats are applicable to CI-67: First, if additional revenue from existing tax rates is not considered a tax increase, government could gradually raise its share of the economy by imposing an unindexed, progressive tax structure on income or property. In this way, government's proportion of the economy would rise as nominal values rose with inflation. It is unclear whether it would require a legislative supermajority to install such a system.<sup>52</sup>

And second, because CI-67 sets permissible appropriations for a given year by the level of *spending* in the previous year, it may encourage government overspending and discourage saving.

5. *Escape clauses must be drafted narrowly and must be difficult to trigger.*

One of CI-66's escape clauses is “difficult to trigger.” An emergency for not more than 12 months may be declared only by the governor in conjunction with three-quarters

of each house of the legislature—even for local levies. Another escape clause—permitting pass-through of non-labor costs “not subject to control by the governmental unit”—could serve as a basis for creative evasion.

Because CI-67 already provides for a two-thirds vote (or vote in excess of two-thirds) for all tax and spending increases, there is no additional emergency provision.

*6. The TEL should cap more than estimated tax revenues.*

As noted above, revenue estimates can be inaccurate and are subject to manipulation. CI-66 relies partly, but not exclusively, on revenue estimates. [Section 15(1)(a)]. In its taxation portion, CI-67 also seems to rely partly on revenue estimates. But CI-67 limits spending directly to the amounts spent in the previous budgetary period. On this criterion, it is the stronger of the two proposals.<sup>53</sup>

*7. The TEL must be comprehensive.*

Both measures are comprehensive; CI-67 somewhat more so. As explained below, this is both a virtue and a vice.

Both proposals apply to all taxes. Both measures apply to all levels of government. Both measures apply to mandatory fees (except, in the case of CI-66, certain fees attributable to utilities or increased costs). Indeed, CI-67 applies to *all* fees.

Neither measure includes devices for ensuring that the state legislature does not pass down responsibility to localities. In the event of a pass-down, any local tax or spending increase adopted in response still would require extraordinary approval procedures; unfortunately, there is no provision for adjustment in the tax/spending formulae applicable to each level of government. In event of a pass-down, a supermajority of the local legislative body probably would be easier to obtain than popular approval because legislators would use the media to shift the blame to the state—although this is by no means certain.

On the other hand, as Stansel observes, devolution of some functions to local government may be desirable: In general, the local government’s proximity to the electorate and the fact of inter-jurisdictional competition tend to render local government more efficient than central government.<sup>54</sup>

CI-67 applies to appropriations as well as revenues; CI-66 applies only to revenues. One risk of CI-67’s separate approval requirements for revenues and appropriations is the increased possibility of litigation or other uncertainty, as Colorado’s Amendment I has demonstrated. This is less of a risk under CI-66.<sup>55</sup>

Advocates of CI-67 acknowledge that in the long run capping revenue would control spending. But they also point out that in the short run if revenues are capped but

appropriations are not, the legislature may invade accounts it should not invade, such as pension trust funds or emergency reserve accounts. On the other hand, advocates of CI-66 might point out that many state assets really should be in private hands, and that it would be *desirable* to ease into expenditure limitation by inventorying and selling such assets.<sup>56</sup>

Ultimately, assessment of these risks and opportunities remains subjective. In any event, adoption of C-25, a referendum proposed by the 1993 state legislature, would reduce the risk of pension fund invasion.

8. *The TEL should not require official implementation.*

Neither CI-66 nor CI-67 require official implementation; they are self-executing.

9. *The TEL should be enforceable by taxpayer suit.*

CI-66 is enforceable by taxpayer suit. Section 15(10). If the taxpayer is successful, he is to be reimbursed for litigation costs. There is also a refunding mechanism for excess taxes collected. Section 15(9). CI-67 has no such provisions, and it is uncertain how the limits imposed by the measure would be enforced. As noted above, there is a long history of legislative bodies circumventing constitutional spending restrictions not enforceable in the courts.<sup>57</sup>

10. *The TEL must include effective shirking control devices, or at least not inhibit the legislature's resort to such devices.*

As noted above, all or most of the benefit of a TEL is lost if the bureaucracy is allowed to sabotage it. This sabotage takes the form of "shirking," coupled with protective agency consolidation and insistent (often taxpayer-funded) lobbying for additional money.

During and after the Montana tax revolt of 1993, Montanans witnessed numerous examples of agency sabotage. School districts threatened to cut the most visible programs unless voters approved mill levy hikes. They threatened to fire teachers according to criteria unrelated to teacher quality. The Montana University System raised tuition without noticeably raising productivity. The Motor Vehicle Division of the Department of Justice cut back services. The Board of Regents adopted a reorganization plan that consolidated five university units into two. And the Governor's "Task Force to Renew Montana Government," heavily laced with political insiders,<sup>58</sup> focused almost exclusively on proposals to elongate the bureaucratic pyramid—which might unwittingly foster an environment of shirking and special interest domination.<sup>59</sup>

Unfortunately, neither CI-66 nor CI-67 contains shirking-control devices. It would be the responsibility of state policy makers to implement such devices. At least it can be said that CI-66 is not inconsistent with the "entrepreneurial government" necessary for effective shirking control. Section 15(3) contains broad exemptions for true user fees, investment earnings, and the like. Adoption of CI-66 would not ensure reform in government operations, but it would not preclude such reform either. However, extensive

adoption of such devices is unlikely without a dramatic change in the direction of current state policy.

CI-67, on the other hand, actually may *thwart* adoption of shirking control devices. Effective shirking control requires “entrepreneurial government”—competition among agencies for taxpayer and consumer approval—and such competition requires substantial reliance on subsidized or unsubsidized true user fees and decentralized pricing flexibility. A competitive regime would be difficult to implement if fees cannot be increased without supermajority legislative approval.

It has been argued that the definition of “fees” in CI-67 is not intended to include true user fees or those currently set by agencies rather than by the legislature. Unfortunately, this position receives no support in the wording of CI-67, and probably is not legally sustainable. Montana statutes and cases employ the term “fee” to include both disguised taxes and true user fees, even those currently fixed by individual agencies.<sup>60</sup> In short, under CI-67, Montana government could become, even more so than today, a bureaucratic system of interlaced cross-subsidies, governed top to bottom by politics.

Of course, one could avoid CI-67’s tight control of discretionary fees by privatizing certain government functions, such as liquor stores or park administration. But government runs many agencies that rely on user fees, where privatization would be unconstitutional, undesirable, or unfeasible politically. Examples include public schools, environmentally-sensitive lands, and the Montana University System. Moreover, CI-67 enables a doctrinaire legislative minority to block even worthwhile privatization, by refusing to approve higher appropriations unless those appropriations are funded wholly by taxes rather than asset sales.

## VII. Conclusion

CI-66 and CI-67 have certain common advantages. Both are constitutional rather than statutory, and are therefore binding on legislative bodies. Both apply to all funds, to all levels of government, and to mandatory fees as well as taxes. Under either it would be difficult to waive normal limits. Both are self-implementing. And both measures set caps low enough so that if they work as intended government’s share of the Montana economy would slowly decline.

In addition to common advantages, each of these TELs has advantages over the other than may compensate for disadvantages with respect to the other. The referendum required by CI-66 likely would lead to better decisions than the legislative mechanism contemplated by CI-67. But decision making under CI-67 would be less expensive than under CI-66. Similarly, under CI-66 it would be easier to sell assets that should be privatized. But under CI-67, it would be easier to protect trust funds from irresponsible

legislatures. CI-66 does not constrain appropriations of federal aid. CI-67 provides better protection against increases in ill-conceived programs financed with federal dollars.<sup>61</sup>

Finally, each measure has certain clear, uncompensated-for disadvantages. Neither includes the kind of shirking control devices necessary to ensure that ordinary Montanans receive full benefit from the TEL. CI-66's protection against electoral corruption is a good start, but additional legislation will be necessary. CI-67 relies on the legislative process, which already is dominated heavily by special interests. CI-67 has no enforcement mechanism.

Selection of one or both (they are not legally inconsistent<sup>62</sup>) really comes down to the question of how Montanans can deal with the disadvantages of each. Legislative action (or constitutional amendment in lieu thereof) would be necessary to cure the disadvantages of CI-66. But only constitutional amendment could cure the problems in CI-67. This is because it is unlikely that lawmakers would put enforcement devices in place, and because CI-67's restriction on user fees may prevent the legislature from implementing some of the competitive devices necessary to control shirking.

In practice, therefore, CI-66 probably would be a more successful measure than CI-67.

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## ENDNOTES

1. For an introduction to the economic analysis of legislative decision making, see Tollison, *Public Choice and Legislation*, 74 VA. L. REV. 339 (1988). For an analysis of the impact of a particular kind of special interest group—public employee unions—see Hunter & Rankin, *The Composition of Public Sector Compensation: The Effects of Unionization and Bureaucratic Size*, 9 J. LABOR RES. 29 (1988).

For an engaging discussion of the most famous voting paradox—“Arrow’s Paradox,” propounded by Nobel Laureate Kenneth Arrow—see Arrow, *Representative Government and Popular Distrust: The Obstruction/Facilitation Conundrum Regarding State Constitutional Amendment by Initiative Petition*, 17 OKLA. CITY UNIV. L. REV. 3 (1992).

2. A classic discussion of problems in traditional structures is William Niskanen, *BUREAUCRACY AND REPRESENTATIVE GOVERNMENT* (1971). Niskanen’s early insights entered popular discussion with publication of D. Osborne & T. Gaebler, *REINVENTING GOVERNMENT* (1991) and the support of President Clinton, Vice-President Gore, and a bipartisan contingent of the nation’s governors. These insights also are understood in several foreign countries. See, e.g., Margaret Thatcher, *THE DOWNING STREET YEARS* (1993); Sir Roger Douglas, *UNFINISHED BUSINESS* (Auckland, New Zealand 1993).

3. See, e.g., Boardman & Vining, *Ownership and Performance in Competitive Environments: A Comparison of the Performance of Private, Mixed, and State Owned Enterprises*, 32 J. LEGAL STUD. 1 (1989); Megginson, Nash & Randenborgh, *The Financial and Operating Performance of Newly-Privatized Firms: An International Empirical Analysis*, 49 J. FIN. 403 (1994). See generally James T. Bennett & Manual H. Johnson, *BETTER GOVERNMENT AT HALF THE PRICE* 37-73 (1981).

4. Bibliographies include (1) Appendix A in R. Tannenwald, *MASSACHUSETTS’ TAX COMPETITIVENESS* (Working Paper Prepared for Mass. Spec. Comm’n on Business Tax Policy 1993), (2) Papke, *RESEARCH ON TAXATION AND INDUSTRY LOCATION: A SURVEY OF THE EMPIRICAL EVIDENCE* (Center for Tax Pol. Studies, Purdue Univ. 1986), and (3) R. Vedder, *DO TAX INCREASES HARM ECONOMIC GROWTH AND DEVELOPMENT?* (Goldwater Inst. 1989). Tannenwald’s collection is subject to the caveat that his text, especially his executive summary, does not capture the richness of the data and seems to overstate the findings on business and progressive taxes. It also misreports the strong negative sign on welfare expenditures in Benson & Johnson, *Capital Formation and Interstate Tax Competition* in D. Lee, ed., *TAXATION AND THE DEFICIT ECONOMY* (1986).

Another study not included in those bibliographies is G. Scully, *HOW STATE AND LOCAL TAXES AFFECT ECONOMIC GROWTH* (Nat. Center for Pol. Anal. 1991).

City studies show similar results. See, e.g., Moore & Stansel, *The Myth of America’s Underfunded Cities* (Cato Inst. 1993).

5. The insight that political jurisdictions compete with each other is called the Tiebout Hypothesis. Examples of empirical support include American Legislative Exchange Council, *The Tax Incentives and Economic Consequences of Cross-Border Activity*, 16 THE STATE FACTOR (July 1990)(summarizing a Price Waterhouse study of differential sales tax rates); Cebula, *A Brief Empirical Note on the Tiebout Hypothesis and State Income Tax Policies*, 67 PUBLIC CHOICE 87 (1990) (migration affected by whether state has a personal income tax); Benson & Johnson, *supra* note 4; Santerre, *Representative versus direct democracy: A Tiebout test of relative performance*, 48 PUBLIC CHOICE 55 (1986).

6. An example of a narrow measure of government is one kind of tax rather than taxes in general or one kind of expenditure rather than expenditures in general. Examples of narrow economic measures are retailing jobs or Fortune 500 branch locations rather than jobs or investment in general.

On the tax side, there is some evidence that progressivity is economically negative, Vedder, *Federal Tax Reform: Lessons From the States*, 5 CATO J. 571 (1985) and *Papke* at 19-20, but even this finding is contradicted. See Tannenwald, *supra* note 4, at 6.

On the expenditure side, see the survey in R. Vedder, *ECONOMIC IMPACT OF GOVERNMENT SPENDING: A 50 STATE ANALYSIS* (Nat. Center for Pol. Anal. 1993). Vedder notes that there is relatively little consensus as to which government spending is economically wise, although in this study, he finds parks and recreation positively correlated with economic growth; education expenditures statistically insignificant; and welfare, highways, and public employee compensation in excess of private sector counterparts all negative. In another study [R. Vedder, *MEETING CALIFORNIA'S BUDGET CHALLENGE* (1991)], his findings on education spending are negative.

The varying results on expenditures may be because states (and agencies within states) differ in how efficiently they deploy available dollars. In one major expenditure area, public education, spending levels no longer affect quality. See Hanushek, *Impact of Differential Expenditures on School Performance*, EDUCATIONAL RESEARCHER (1989) (statistical summary of all empirical studies to date on factors that influence and fail to influence K-12 student achievement). *Accord*: J. Chubb & T. Moe, *POLITICS, MARKETS, AND AMERICAN SCHOOLS* (1990) (report of extensive research project into school performance); Walberg, *LOSING LOCAL CONTROL OF EDUCATION* (Heartland Inst. 1993).

7. Most studies rely on regression analysis.

8. Government activity often is measured by aggregate state and local tax revenue as a share of personal income rather than per capita figures. Per capita figures do not seem to be important for these purposes. One can readily see why: If government size is to be measured by per capita taxes, then North Korea is a "low tax" area! Taxes should be quantified with respect to ability to pay.

These studies gauge economic activity by absolute or relative changes in personal income or personal income per capita, in- and out-migration, or total employment or investment.



9. E.g. Benson & Johnson, *supra* note 4.

10. Hence the implicit assumption behind Montana's ill-fated Referendum 111—that reallocation to include a general sales tax would help more than the net tax hike would hurt—was probably wrong.

11. On a full-time equivalent basis, Montana is fourth in the U.S. in the percentage of the population employed by state and local government. U.S. Dep't of Commerce, Bureau of the Census, GOVERNMENT EMPLOYMENT (1991).

12. See, e.g., Abrams & Dougan, *The effects of constitutional restraints on government spending*, 49 PUBLIC CHOICE 101 (1986) (government spending not statistically related to percent of population in urban areas); R. Vedder, MEETING CALIFORNIA'S BUDGET CHALLENGE (1991) (population density and resource factors found far less significant in explaining income growth than tax factors).

When a state is just too different, a researcher may drop it from the sample, but those most frequently dropped are Alaska and Hawaii—not Montana.

13. Note the point in the text: The following statistics are not consistent with the belief that Montana is "different." Of course, these statistics only suggest, they do not *prove*, that the growth in government was implicated in Montana's economic decline.

14. See *infra* note 18.

15. Unless otherwise stated, statistics in the following sections are from the annual issues of U.S. Dep't of Commerce, Bureau of the Census, GOVERNMENT FINANCES (with Montana Dep't of Revenue corrections in the tax and OSR figures for 1990 and 1991).

16. In nominal dollars, aggregate state and local spending rose nearly 60% in three years! Apparently much of this new money went to build bureaucracy. Between 1973 and 1977, Montana state and local FTE employment rose a stunning 31%! *Source*: State by state, year by year, print-out provided by U.S. Bureau of Labor Statistics to the author, 12/22/92. [1973 is the first year Montana state-local employment was broken out from total (including federal) employment.]

The magnitude of Montana's spending increases in this general period is captured by Table 1 appearing in Bails, *A Critique on the effectiveness of tax-expenditure limitations*, 38 PUBLIC CHOICE 129 (1982), which shows Montana first among states in per capita spending increases over inflation for 1974-78.

17. While politicians sometimes promote severance taxes as substitutes for other levies, higher severance taxes actually may *encourage* increases in other taxes. See Abrams & Dougan, *supra* note 12 (when all states are included, \$1 increase in severance tax capacity raises state and local spending by \$4; excluding Alaska, \$1 in severance tax capacity still raises other taxes, although finding not statistically significant).

18. The lag depicted here is two years. However, this connection is strong and statistically significant at the 95% level for lag times of 1-4 years: 4 years:  $R^2 = .26$ ,  $t = -2.51$ ; 3 years:  $R^2 = .38$ ,  $t = -3.48$ ; 2 years,  $R^2 = .44$ ,  $t = -3.95$ ; 1 year,  $R^2 = .37$ ,  $t = -3.49$ . Results at longer or shorter lags are not statistically significant. Independent review uncovered no evidence of serial correlation. Breakdown into "late" and "early" periods suggest the lag times are growing shorter.

I used a two year rolling average because Montana state government budgets on a biennial basis and to reduce the effect of anomalies in any one year. However, when rolling averages are not used, the figures remain significant on 2 and 4 year lags.

I chose OSR rather than total general revenue or taxes because (1) I wanted to exclude federal aid, (2) avowed taxes are declining as a portion of OSR, partly because of renaming taxes as mandatory "fees" (more so in Montana than elsewhere), so using only "tax" revenue could lead to an "apples-and-oranges" effect over time, and (3) Census Bureau statistics on total revenue are not available before about 1980.

Nevertheless, I obtained roughly similar results when the independent variable was (1) taxes alone, (2) total general revenue, (3) OSR plus workers' compensation payments to the state fund (arguably a kind of tax), or (4) taxes plus workers' compensation payments.

R. Vedder, *MEETING CALIFORNIA'S BUDGET CHALLENGE* (1991), has found negative associations between state acceptance of federal aid and subsequent economic growth; I found no clear relationship, positive or negative for Montana.

19. The region used includes Colorado, Idaho, North Dakota, Nevada, Oregon, South Dakota, Utah, Washington, and Wyoming. I've obtained similar results in earlier tests using narrower definitions of "region."

20. The period in the text ends in 1991. The slowest growing states during this period were Wyoming, South Dakota, Montana, and North Dakota; all but South Dakota followed "big government" policies.

21. State Policy Research, 12 *STATE BUDGET & TAX NEWS* 6 (1994) (reporting on a study by Steven Gold of the Center for the Study of the States). The ranking drops to fifth with the suspension of H.B. 671, but it does not reflect fuel tax increases scheduled by the 1993 legislature for FY 1995.

22. S. Moore & D. Stansel, *A Fiscal Policy Report Card on America's Governors* 29, 55 (Cato. Inst. 1994).

23. Nelson, *The New Populism*, 153 *FORBES* 100 (1994). See also Berthoud, *As Montana Piles on the Taxes, Residents Rise Up in Protest*, Waterbury (Conn.) Republican-American, Dec. 22, 1993, p. 13A, col. 1. Florio was, of course, the New Jersey governor whose huge revenue hikes, implemented after a promise not to raise taxes, infuriated the voters and triggered his 1993 re-election defeat.

24. In a number of cases, the school campaigning methods bordered on electoral corruption, in my opinion. See *infra* note 49.

25. Scholars use the term “preemptive TEL” to describe a relatively weak tax or expenditure limitation adopted by politicians to avoid stronger limitations imposed by initiative. See, e.g., Poulson & Kaplan, *A rent-seeking model of TELs*, 79 PUBLIC CHOICE 117, 120 (1994).

26. D. Stansel, TAMING LEVIATHAN: ARE TAX & SPENDING LIMITS THE ANSWER? 28 (Cato Inst., 1994).

27. *Id.*

On debt limitations, see Sterk & Goldman, *Controlling Legislative Shortsightedness: The Effectiveness of Constitutional Debt Limitations*, 1991 WISC. L. REV. 1301. About three-quarters of the states have such limitations.

The Montana Constitution provides:

No state debt shall be created unless authorized by a two-thirds vote of the members of each house of the legislature or a majority of the electors voting thereon. No state debt shall be created to cover deficits incurred because appropriations exceeded anticipated revenue.

Mont. Const., Art. VIII, §8

28. See D. Bails, A TAX AND SPENDING LIMITATION BIBLIOGRAPHY (Pub. Int. Inst., Mt. Pleasant, Iowa, 1993); D. Stansel, *supra* note 26; Poulson, *The Rules of the Game: Designing a State Fiscal Constitution* in Berthoud & Brunelli, eds., THE CRISIS IN AMERICA’S STATE BUDGETS: A BLUEPRINT FOR BUDGET REFORM (1993); Poulson & Kaplan, *supra* note 25; Abrams & Dougan, *supra* note 12; Bails, *supra* note 16; Hughes & Rieman, *Comment: A New Generation of State Tax and Expenditure Limitations*, 22 HARVARD J. LEGIS. 269 (1985); Weiss, *Comment: The Texas Tax Relief Act After Twelve Years: Adoption, Implementation & Enforcement*, 23 ST. MARY’S L.J. 491 (1991); Wyrick, *The Hancock Amendment and Economic Growth in Missouri* (Heartland Inst. 1992).

The following discussion draws on this material without detailed footnote references.

29. Mont. Code Ann. §§17-8-105 and 17-8-106, written by the legislature, have been ineffective in restraining state expenditure. D. Stansel, *supra* note 26, at 32. Among statutory initiatives, I-86 (Mont. Code Ann. §15-30-103), which imposed income tax indexing, would have been completely repealed by the 1993 sales tax proposal, and would have been diluted by H.B.671 (now IR-112). The legislature amended the property tax limitation I-105 (Mont. Code Ann. §15-10-402) soon after passage to exempt school districts—the largest property tax consumers. Further, the legislature has weakened I-105 several times since. There is some evidence that I-105 was preemptive of proposed CI-27, which would have abolished property taxes completely.

30. D. Stansel, *supra* note 26, at 15 (TELEs limited to state expenditures resulted in some cost shifting to local government, but not enough to obviate complete effectiveness). See also Hughes & Rieman, *supra* note 28, at 284.

31. M. Racicot, *Remarks to Missoula Rotary, 2/23/94*.

32. Mont. Code Ann. §§17-8-105, 17-8-106. This limit has not been generally effective, however. D. Stansel, *supra* note 26, at 32.

33. Two leading economists have thus stated the case for supermajorities:

When the benefits and costs of voters are directly related, productive government action will be favored by huge majorities. Correspondingly, support by a supramajority, say 80 or 90 percent of the voters, is strong evidence that the project is productive. Conversely, if a supramajority cannot be achieved, this is strong evidence that the project is counterproductive ....

J. Gwartney & R. Stroup, *WHAT EVERYONE SHOULD KNOW ABOUT ECONOMICS AND PROSPERITY* 73 (1993). The authors point out that a project can be non-productive and still garner support of a bare majority by offering each member of the majority small gains while inflicting large costs on the minority. See also W. Niskanen, *supra* note 2, at 222. But see Wickstrom, *Optimal Majorities for decisions of varying importance*, 48 *PUBLIC CHOICE* 273 (1986).

The smaller the size of the decision making body, the more compelling the need for supermajorities. Nitzan & Paroush, *Are qualified majority rules special?* 42 *PUBLIC CHOICE* 257 (1984).

34. M. Racicot, *Remarks to Missoula Rotary, 2/23/94*. ("CI 66 would create a cumbersome system of costly elections that place bulls-eyes on our extractive industries, on our farmlands, on our small and large businesses....")

The Governor also argued that CI-66 would spark litigation, which is undoubtedly true. See however, note 55 *infra* and accompanying text.

35. There have been 13 Montana tax referenda since 1914, nine approved and four rejected. Only two of the nine approved taxes were levies on particular products, and they were imposed on products long accepted as special subjects of taxation: tobacco and liquor. The other seven approved taxes were broad-based property levies for university purposes.

The four defeated tax proposals were all broad-based: two property levies for education and two sales tax proposals. In addition, a broad-based income tax (House Bill 671) was suspended in 1993.

It is probably more significant that proponents of the 1993 sales tax and of the 1993 income tax hike both tried to sell those measures as *desirable* because they purportedly

imposed disproportionate burdens on select groups (tourists and the “rich”). With the electorate and with petition signers, these arguments proved unconvincing.

36. Madison observed that special interests combinations have *less* power as the voting group increases in size. THE FEDERALIST, No. 10. This observation is supported by an empirical analysis of state legislatures, which finds that larger state legislatures produce less special interest legislation than smaller ones. R. McCormick & R. Tollison, POLITICIANS, LEGISLATION, AND THE ECONOMY 29-60 (1981).

Recent experience with public tax votes in Oklahoma and Colorado has been that special interest proposals, such as Colorado’s 1993 tourism tax proposal or Oklahoma’s 1992 welfare proposals, are defeated, while general interest measures often pass. T/C with Dennis W. Arrow, Professor of Law, Oklahoma City University, 3/29/94; T/C with Tom Tancredo, President, Independence Institute, Golden, Colorado, 3/9/94. On the other hand, experience has shown the Montana legislature highly prone to special interest taxation. See, e.g., Mont. Code Ann. §15-6-101 *et seq.* (property tax classification system).

If direct democracy increases by special interests (or targeting of special interests) control, this should impair direct democracy’s position in intergovernment competition. But Santerre, *supra* note 5, finds the contrary.

37. In any event, Madison’s views should not be taken as controlling: The framers were split deeply on the meaning of the term “republic.” F. McDonald, NOVUS ORDO SECLORUM 5 (1985).

38. Toma & Toma, *Bureaucratic responses to tax limitation amendments*, 35 PUBLIC CHOICE 35 (1980). See also McCroskey & Hall, *Amendment One: Hurdles, Opportunities, and the Lessons of California* (Independence Inst. 1993).

39.D. Stansel, *supra* note 26, at 25-26. For a contemporary example of using agency failure as a reason for increased funding, see *Argument in Support of Legislative Referendum 112* (Montana Voter Information Pamphlet, 1994). Another reason may be greater government sophistication in utilizing the TEL’s escape mechanisms. Poulson & Kaplan, *supra* note 25.

40. Toma & Toma, *supra* note 38.

41. The initial insight came from Niskanen, *supra* note 2, further developed in Toma & Toma, *supra* note 38. There is now extensive empirical support. See, e.g., Couch & Shughart, *Private school enrollment and public school performance*, 76 PUBLIC CHOICE 301 (1993) (competition from private schools improves public schools); McGuire & VanCott, *Public versus private economic activity: A new look at school bus transportation*, 43 PUBLIC CHOICE 25 (1984) (operating in competitive environment increases public sector service delivery to within 12% of private sector efficiency); D. Osborne & T. Gaebler, *supra* note 2.

42. Toma & Toma, *supra* note 38, at 344-45. Protection of “shirking” through consolidation apparently has been going on in the nation’s public school systems for many years. Cost benefits of consolidation are debatable, but educational decline has been rather strongly associated with it. Compare Burnell, *The effect of school district structure on education spending*, 69 PUBLIC CHOICE 253 (1991) (small cost savings associated with consolidation, but savings may have other explanations) with Walberg, *supra* note 6 (doubting financial benefits of consolidation and finding strong negative correlations between consolidation and pupil achievement). On the negative associations of achievement and school bureaucracy, see also J. Chubb & T. Moe, *supra* note 6, at 169-70.

43. A purist might take the position that CI-66 is not a true TEL because it does not limit taxes according to formula, but merely imposes an additional condition precedent to tax increases: voter approval. There are several problems with this distinction, and I have ignored it in this paper.

44. Wickstrom, *supra* note 33.

45. See generally D. Stansel, *supra* note 26. (See pp. 16-17 for waiver mechanism.)

The Montana state budget director, a fiscal conservative, has observed that the legislature sometimes must “build a Christmas tree”—authorize more capital projects than necessary to obtain the two-thirds majority required for creation of state debt. Thus, if applied to the ordinary budget process the two-thirds provision ultimately may *increase* appropriation levels. T/C with Dave Lewis, state budget director, 5/23/94.

46. Peltzman, *How Efficient is the Voting Market?* 33 J. LAW & ECON. 27 (1990) (“...the voting market emerges as a strikingly efficient aggregator of economic information.” *Id.* at 62).

When electoral voting occurs after legislative input—as in tax referenda—voters seem to be more fiscally conservative than when acting without legislative intervention. See Zax, *Initiatives and Government Expenditures*, 63 PUBLIC CHOICE 267 (1989) (indirect initiative process does not have the higher spending propensities of the direct initiative). Cf. Montana’s experience with sales tax referenda.

47. Some necessary reforms have been put in place quite recently, including improvements in the Legislative Fiscal Analyst’s budget presentations, and adoption by the 1993 special session of H.B. 7 (Mont. Code Ann. §17-7-102) which abolished the practice of budgeting exclusively up or down from projected budget *increases*.

48. Among other examples: During the 1993 petition campaign on IR-112 (H.B. 671), the state Office of Public Instruction used public money to draft and mail flyers opposing the petition and the Board of Regents authorized use of mandatory student fees to fund a lawsuit to invalidate the suspension.

49. The Missoula County High School mill levy election of May 3, 1994 is a good example. The high school district used taxpayer funds to print flyers and place newspaper advertisements promoting the levy with “information” of dubious accuracy. Campaigning went on at the schools and on school time, apparently in violation of law. Mont. Code Ann. §13-35-226(3)(“No public employee may solicit support for or opposition to ...passage of a ballot issue while on the job or at his place of employment.”) The daily newspaper (which benefitted financially from the pro-levy advertisements) promoted the levy strongly: Reporters failed to investigate school officials’ assertions or to report opposing points of view, opinion columns and editorials were unanimously pro-levy, and the letters to the editor nearly all pro-levy. The chief “alternative” paper covered the election in much the same way.

School officials may have failed to comply with the financial reporting and other political committee requirements of Mont. Code Ann. §13-37-201, *et seq.* The school district’s campaign was replete with explicit and implied threats. For example, children were given two alternative schedules for the following year: They were told that if the levy passed they could have the schedule they wanted; if the levy failed, they would receive a less desirable schedule. Employees were warned of unrealistically high layoffs if the levy failed.

50. Mont. Code Ann. §13-27-401 *et seq.*

51. The alternative would be to cut taxes or allow the excess money to accumulate. Both are possible, but unlikely. Although supporters of CI-67 argue that higher spending drives higher taxes, current scholarship suggests that (granting some dual causation) revenues drive spending more than the other way around. Joulfaian & Mookerjee, *The Government Revenue-Expenditure Nexus: Evidence from a State*, 18 PUB. FIN. Q. 92 (1990), and sources cited therein.

52. If, for example, a flat rate property tax were replaced with a progressive structure that was revenue neutral for the next biennium, would this be “an increase” in a tax? A “new” or merely amended tax? See CI-67, Section 15(1).

53. D. Stansel, *supra* note 26, at 20.

54. D. Stansel, *supra* note 26, at 23. See also Walberg, *supra* note 6.

55. Probably the largest single source of Colorado litigation has been over the issue of separate authorization and appropriations for bond issues. Colo. Const., Art. 10, §20. Compare CI-66, Section 15(2)(d).

56. McCroskey & Hall, *supra* note 38.

57. See, e.g., Bails, *supra* note 16.

58. Six of the 16 members of the task force are representatives of the state's large education establishment; a clear majority are either legislators or other present or past government employees.

59. On the empirical effects of top-down consolidation (that is, consolidation that is not market-driven), see note 38 and accompanying text. Among the ideas floated by the Task Force are reducing the size of the legislature, consolidating all education agencies into a single department, rendering two elective positions appointive, consolidating county offices, consolidating human services agencies, consolidating natural resource agencies, consolidating counties, consolidating law enforcement, and consolidating other agencies. See Buchanan, *Montanans can't afford all the government we've created*, Great Falls Tribune, 2/13/94, col.1; Johnson, *Government reshapers make final alterations*, Missoulian, 4/18/94, p. B-2, col. 1.

This approach is captured well by Mark Twain's remark: "When the only tool you have is a hammer, everything begins to look like a nail."

60. For disguised taxes, see, e.g., the petroleum storage tank cleanup fee imposed by Mont. Code Ann. §§75-11-302(13) & 75-11-314 or the nursing facility utilization fee imposed by §15-60-101 and 102. For a true user fee set by the agency rather than by the legislature, see, e.g., §23-1-105(2) (park user fee); for some set by statute, see §7-32-2141 (sheriff's fees). Relevant case law includes *State v. DeMers*, 192 Mont. 367, 628 P.2d 676 (1981) and *State v. District Court*, 53 Mont. 350, 165 P. 294 (1917).

61. Hughes & Rieman, *supra* note 28, at 285 favor expenditure limits, but argue that federal aid ought to be excluded from those limits. On the other hand, some researchers believe acceptance of federal funds may depress a state's economy. See R. Vedder, *supra* note 6, at 16.

62. As we go to press, some critics of CI-66 and CI-67 are arguing that the two proposals are mutually inconsistent, and that they also conflict with the referendum provision of the Montana Constitution (Art. III, § 5). The effect of simultaneous adoption of CI-66 and CI-67 would be to impose different conditions precedent on taxes and spending. The conditions are not mutually exclusive; increased taxes and spending would simply require fulfilling all of the relevant requirements of CI-66 and CI-67.

To the extent that CI-66 and CI-67 conflict with the referendum provision of Article III, section 5, and the conflict cannot be reconciled, the later adopted provisions (CI-66 and CI-67) would supersede.