



Texas Conservative Coalition

TEXAS CONSERVATIVE COALITION

Sense in Spending

A Conservative Rebuttal to the Preliminary Mid-Session Report of the House Select Committee on Federal Economic Stabilization Funding

APRIL 2009

Texas Conservative Coalition

www.txcc.org

Sense in Spending

A Conservative Rebuttal to the Preliminary Mid-Session Report of the
House Select Committee on Federal Economic Stabilization Funding

For more information on any of the arguments or recommendations contained in this
document, please contact the Texas Conservative Coalition:

Brent Connett, Policy Analyst – brent@txcc.org

Tom Aldred, Policy Analyst – tom@txcc.org

Texas Conservative Coalition
P.O. Box 2659, Austin, TX 78768
(512) 474-1798
www.txcc.org

The contents of this document do not represent an endorsement from any individual member of the Texas
Conservative Coalition or any member of its Board of Directors.

There may be some policy recommendations or statements of philosophy that individual members are unable to
support. We recognize and respect their position and greatly appreciate the work of everyone involved with the
organization.

Legislative advertising: Wayne Christian, President, Texas Conservative Coalition
(P.O. Box 2659, Austin, TX 78768).

Copyright 2009 Texas Conservative Coalition, all rights reserved.

About the Texas Conservative Coalition

“Winning the Fight. Building the Future.”

The Texas Conservative Coalition is a legislative caucus formed in 1985 committed to shaping public policy by promoting:

- ★ Limited Government
- ★ Individual Liberties
- ★ Free Enterprise
- ★ Traditional Family Values

The Texas Conservative Coalition was established to impact public policy from a conservative perspective and give legislators a platform to win debates at the Committee level and on the Floor. Our objective is to implement a conservative vision for state government.

Table of Contents

- I. Overview (5)
- II. Section by Section Rebuttal:
 - a. Core Recommendations (10)
 - b. Response to Questions from the Office of the Speaker (14)
 - c. Agency Testimony (19)
 - d. The Structural Deficit (24)

Sense in Spending

A Conservative Rebuttal to the Preliminary Mid-Session Report of the House Select Committee on Federal Economic Stabilization Funding

Overview

The federal stimulus package rushed through Congress and signed by President Barack Obama on February 17, 2009 (officially: the American Recovery and Reinvestment Act of 2009) issues unprecedented and unfunded levels of federal spending that include demands that the State of Texas change its laws to receive some of the funds.

President Obama has made it clear that he rests his hopes for an economic rebound on government spending. In a February press conference, President Obama stated that the “federal government is the only entity left with the resources to jolt our economy back into life.”¹ The House Select Committee on Federal Economic Stabilization Funding report echoes on that belief by arguing that “a unique opportunity will be lost” if Texas does not use the stimulus to “maximize job creation and stimulate the Texas economy.” The President and Congress are ushering the United States down a well-worn, yet dangerous path that the Select Committee report readily advances with its recommendations and rhetoric.

Federal stimulus funds represent an unprecedented increase in federal spending. On January 7, 2009, *before* passage of the \$787 billion stimulus bill, the Heritage Foundation reported on the federal budget and spending trends. According to Heritage, federal spending increased by \$249 billion in 2008, or 9.1 percent.² With the \$787 billion stimulus package signed by President Obama, and the \$700 billion bailout bill signed by President Bush, the federal government has spent nearly \$1.5 trillion in the name of economic recovery in less than six months.

By comparison, the federal budget for fiscal year 2009 totals \$3.1 trillion in outlays, of which \$987 billion is discretionary.³ The stimulus and bailout packages represent nearly half of the total federal outlays for FY2009, and are *higher* than annual discretionary spending. This analysis does not include President Obama’s proposed budget for fiscal year 2010, which will increase spending well above the \$787 billion stimulus bill.

The Report of the Select Committee on Federal Economic Stabilization Funding perpetuates the flawed premises that underlie the stimulus package by recommending that the state use “Federal stimulus money to maximize funds, create jobs, and stimulate the Texas economy.” This is a false promise.

Though hundreds of thousands of people are employed by government in Texas, the public sector never has and never will grow the economy or create jobs, except in limited circumstances such as tax reductions. Government can, however, produce the opposite effect. A report prepared by Arduin, Laffer & Moore Econometrics for the Texas Public Policy Foundation (TPPF) notes that the federal stimulus will cost, rather than create, jobs:

Every dollar the government spends must first be removed from the pocket of the private sector—through higher taxes today, or higher borrowing today implying higher taxes tomorrow. Either way, government spending crowds out private sector spending, diminishing the private economy’s rate of growth.⁴

While the Select Committee report concedes without supporting documentation that new state employees will be necessary to administer the influx of federal funds to state agencies, those few state jobs (which will likely exist long after the one-time stimulus funds expire) will come at the expense to the private sector, specifically taxpayers. In addition to the significant flaws in the principles behind the Select Committee report, there are other broad criticisms of both the Select Committee report and the stimulus in general:

1. **The Select Committee report rests its operating assumption on speculative promises of job growth made by the Administration.** The stated pretext of the stimulus is job growth. The federal government speculates that the stimulus will create *or save* 269,000 jobs in Texas.⁵ However, the President’s Council of Economic Advisors admits: “The state jobs estimates are inherently more speculative than the overall estimates.”⁶ The Heritage Foundation goes a step further by pointing out that the estimates of job creation or retention that were employed to advance the stimulus through Congress were “founded on loose assumptions that lack academic rigor.”⁷

Actual data show that Texas created 393,300 jobs over the past two years, which is *124,300 more jobs* than speculatively estimated as a result of the unprecedented federal stimulus bill.⁸ Government spending, particularly for transfer payments which are the core of the stimulus package, does not create jobs. Instead, private investments and risks will grow the economy and create jobs.

2. **Despite the huge increase in funds as a result of the stimulus package, the Texas allotment of federal stimulus dollars is de minimis compared to the state budget and economy.** The \$15.3 billion Texas allotment of stimulus fund represents:

- ★ 9 percent of the 2008-2009 budget (\$167.8 billion in All Funds spending).⁹
- ★ 1.25 percent of Texas’ \$1.2 trillion 2008 Gross State Product.¹⁰
- ★ \$640 per capita (based on a Texas population of 23.9 million).¹¹

In other words, the size of the federal stimulus funds relative to the state budget and the Texas economy makes it even less likely that the stimulus will achieve its speculative job growth and retention claims, although it will undoubtedly grow government spending.

3. **The Select Committee report fails to accomplish the tasks assigned by Speaker of the Texas House of Representatives Joe Straus.** In the February 12, 2009 proclamation that created the House Select Committee on Federal Economic Stabilization Funding, Speaker Straus wrote:

...the select committee shall make recommendations to any standing committee of the house regarding legislation necessary for the state to receive federal funds for economic recovery.¹²

The Select Committee report, however, makes no recommendations to committees and only supports one bill before the Texas Legislature: the Texas Government Accountability and Transparency Act of 2009. Furthermore, the report was released *after* draft budgets were passed by the Senate and the House Appropriations Committee.

4. **The Select Committee report ignores the costs that are associated with federal matching funds.** To receive federal matching funds, Texas must first make a state expenditure, exposing taxpayers to two tax increases due to increased spending at two levels. The Select Committee report argues that the state should use freed-up General Revenue to access federal matching funds for health & human services programs, representing a massive expansion of government health care.

Part and parcel to this increase in federal spending is the detrimental impact of federal spending on the state budget. In the House Substitute for SB 1 (81R), federal funds in the state budget are nearly equal to general revenue and general revenue dedicated funds combined. The infusion of federal funds to the state budget has three negative consequences:

1. Federal funds make it more difficult for the state control its own budget.
2. Federal funds make Texas, and indeed all states, more dependent on the federal government, which undermines the principle of federalism.
3. In many cases, federal funds necessitate increases in state general revenue spending where federal matching dollars are made available.

Increasing the appropriation of matching funds only accelerates budget increases in Texas at a cost to taxpayers.

5. **The Select Committee report bases arguments on a negligible or non-existent “multiplier effect”.** Transfers of wealth by the government may translate into “income” for some, but there is no multiplier effect from government spending on health care or any other policy goal. The stimulus, and the health care recommendations of the Select Committee report, amount to wealth redistribution, not wealth creation.
6. **The Select Committee report blames property tax rate relief for a so-called “structural deficit”.** By arguing that Texas has a “structural deficit” because of billions of dollars appropriated to school district maintenance & operations property tax rate relief, the Select Committee report implicitly argues the property tax rate relief is a misguided or inappropriate public policy decision. The contrary is in fact true. While property taxes remain a major though surmountable problem in Texas, property tax rate relief passed in the Third Called Session of the 79th Legislature was legally and financially necessary. Any argument to the contrary is purely a political point, and far beyond the scope of the Committee charge by the Speaker.

Although the federal stimulus package is a reality that the Legislature must face, legislators should not view the federal stimulus monies as a cure all. If state legislators exercise prudence in the spending of stimulus monies -- and the state General Revenue "freed-up" as a consequence -- the state can avoid long-term negative ramifications of the bill.

The superior strength of the Texas economy, relative to the rest of the nation, is a testament to a responsible economic approach by state government to limit spending, maintain a low tax climate, and make targeted investments that deliver returns in the form of capital investments and job growth. Since 2003, Texas has:

- ★ Addressed a \$10 billion budget deficit without raising taxes or creating new taxes (HB 1, 78R, 2003);
- ★ Appropriated \$18 billion to cut school district maintenance & operations property tax rates (HB 1 & HB 2, 79S3, 2006; and, HB 1, 80R, 2007);
- ★ Protected small businesses from the impact of the new gross margins tax by increasing revenue exemptions to the tax (HB 3928, 80R, 2007);
- ★ Invested \$333 million from the Texas Enterprise Fund which has translated into 53,954 jobs, and more than \$14 billion in capital investment in our state¹³ (SB 1771, 78R, 2003); and,
- ★ Maintained a Skills Development Fund at the Texas Workforce Commission that, in Fiscal Year 2008, awarded 41 grants totaling \$22,772,673, which served 148 businesses, generated 7,984 new jobs and upgraded the skills of 11,705 workers in existing jobs.¹⁴

These policies have allowed the Texas economy to prosper. Texas is home to 113 Fortune 500 companies, more than other state in the nation.¹⁵ On March 23, 2009, ABC News reported that only three of the top 39 major markets added jobs last year and all three were in Texas: Austin, San Antonio, and Houston.¹⁶ Texas is one of only seven states to enter 2009 *without* a budget deficit.¹⁷

Despite this evidence, the Select Committee report claims that the stimulus funds will right the economy, ignoring the reality that the Texas economy remains stronger than the national economy, and the economies of other states. While the economic downturn is undoubtedly impacting Texas, the latest figures from the Comptroller and Workforce Commission show that Texas unemployment is two full points below the U.S. unemployment rate:

- ★ Texas: 6.5 percent
- ★ United States: 8.5 percent

The Comptroller reports that "the Texas unemployment rate has been at or below the national rate for 26 consecutive months."¹⁸ Still, the federal stimulus and the recommendations in the Select Committee report provide an easy opportunity for Texas to grow government at the expense of the private sector and taxpayers. Washington D.C. and California (10.5 percent unemployment¹⁹) have relied on government spending to prop up their economies, with disastrous results.

The Texas Conservative Coalition (TCC) has repeatedly urged that stimulus funds be spent only on one-time items that will not permanently grow the state budget or necessitate more taxes, increased debt, or both. As the TCC Board of Directors wrote to their colleagues on February 11, 2009, “Texas must continue to chart a smarter way to avoid the uncontrolled spending that is ruining the finances of so many other states and undermining the appropriate roles of state governments.”

To allow private businesses to take risks, grow the economy, and create jobs, Texas must continue to:

- ★ Lower taxes;
- ★ Make limited and targeted investments in economic development and workforce training programs that work;
- ★ Keep spending both limited and responsible by:
 - ★ Ensuring that stimulus funds are not used in any fashion to grow existing programs or future budgets;
 - ★ Ensuring that general revenue displaced by stimulus funds is not used to expand or create programs beyond one-time expenses; and,
 - ★ Including provisions for on-going auditing and oversight of federal stimulus funds, particularly if Congress and the Administration take additional steps after *sine die* to flow even more money to the states.

Sound fiscal policy is the key to economic growth. Legislators should reject the philosophical underpinnings of the Report of the Select Committee on Federal Economic Stabilization Funding.

Core Recommendations:

The Select Committee makes core recommendations to the Legislature, each of which is addressed here:

Recommendation 1: 2009 Supplemental Appropriations Act

The Select Committee Report suggests appropriating all FY 2009 stimulus funds in the Supplemental Appropriations Act (HB 4586 (81R) by Pitts). Irrespective of this recommendation, the Supplemental Appropriations Act already proposes making the following FY 2009 stimulus appropriations²⁰:

- \$662,200,000 to the Texas Department of Transportation for highway and bridge construction.
- \$758,084,423 to the Texas Education Agency for providing formula distributions to school districts and charter schools for the purchase of textbooks and continuing contracts related to instructional materials.
- \$27,300,000 to the Office of the Attorney General to provide child support enforcement.
- \$220,915,577 to the Texas Education Agency to provide additional technology and instructional materials through the Technology Allotment.
- \$1,640,156,643 to the Health and Human Services Commission for increased Medicaid funding.

Because the Supplemental Appropriations Act is the vehicle through which the Legislature makes current biennium budget adjustments and appropriations, it is clearly the correct method for allocating FY 2009 stimulus funds. This is a non-substantive recommendation.

Recommendation 2: 2010-11 General Appropriations Act

The Select Committee Report recommends including all stimulus funds for FY 2010-11 in a separate article of the 2010-11 General Appropriations Act. The current version of the state budget (the House Committee Substitute for Senate Bill 1) already has all federal stimulus funds in Article XII, which was created for that purpose. This Select Committee recommendation is redundant to the work done by the Senate and the House Appropriations Committee.

Recommendation 3: Temporary Increase of Full-Time State Employees

Without providing justification, the Select Committee Report recommends a temporary increase in the number of full-time state employees to handle administration of federal stimulus funds. This recommendation is too broad, and pays no attention to the requests of individual agencies noted later in the Select Committee report.

For instance, the report notes that the Texas Commission on Environmental Quality “assured [the Select Committee] that they have proper personnel and systems in place to assure rapid distribution of funds while not sacrificing accountability.” However, the report also notes that HHSC testified that “[the agency] will immediately advise the Select Committee if any enhancements in personnel and systems are needed to assure rapid distribution of funds.”

A blanket recommendation to increase state employees, regardless of agency need, reinforces the obvious point that stimulus funds are largely a tool for growing government. Regardless of whether new state employees are intended to be temporary, taking on new employees when they are not required is fiscally irresponsible.

Recommendation 4: Transparency of Stimulus Funds

The Select Committee Report suggests five budget riders that deal with the transparency of federal stimulus funds. These recommendations include:

- Requiring each agency and higher education institution to file all documentation relating to the stimulus funds with the Legislative Reference Library;
- Designating “lead” agencies to maximize state and local stimulus funding; and,
- Requiring all state agencies and institutions of higher education to post all information pertaining to the stimulus in the prominent location on their website.

Many of the recommendations are poorly constructed and would result in duplicative effort on the part of state agencies. For instance:

- The Legislative Reference Library is not equipped to deal with complex financial data filed by state agencies. Documentation of this sort should be filed with the Legislative Budget Board or the Comptroller of Public Accounts.
- The state should not be in the business of “maximizing” stimulus funding to cities and counties. Federal stimulus funds are already flowing directly to units of local government across the country: the state need not duplicate efforts by inserting itself into the process unnecessarily. For instance, the Select Committee’s own report notes that “cities and

counties in Texas will receive their Community Development Block Grant funding directly from the Federal government.”

- Requiring state agencies and institutions of higher education to post all information pertaining to the stimulus funding on their websites is duplicative of the role of the Legislative Budget Board and the Comptroller of Public Accounts. Between these two agencies, the LBB’s “Texas Budget Source” and the Comptroller’s “Where the Money Goes,” the state is already capable of tracking expenditures. Agencies and institutions of higher education should simply link directly to LBB and the Comptroller, rather than maintain their own separate internet pages containing their specific stimulus expenditures. Indeed, the Select Committee report notes that:

Officials from the Texas Comptroller of Public Accounts presented a detailed spreadsheet which attempts to identify all of the funds in the economic stimulus bill that will potentially benefit Texas...the agency continues to expand and refine the information as more information becomes available.

It is also worth pointing out that while the Select Committee’s report makes several recommendations related to transparency, it fails to address the specific shortcomings of the stimulus legislation in this area. The Federal Office of Management and Budget (OMB) noted in February that:

Reporting requirements only apply to the prime non-Federal recipients of Federal funding, and the subawards (i.e., subgrants, subcontracts, etc.) made by these prime recipients. They do not require each subsequent subrecipient to also report. For instance, a grant could be given from the Federal Government to State A, which then gives a subgrant to City B (within State A), which hires a contractor to construct a bridge, which then hires a subcontractor to supply the concrete. In this case, State A is the prime recipient, and would be required to report the subgrant to City B. However, City B does not have any specific reporting obligations, nor does the contractor or subcontractor for the purposes of reporting for the Recovery.gov website.²¹

Testifying before the U.S. House Committee on Oversight and Government Reform, Jerry Brito, a Senior Research Fellow at George Mason University argued that:

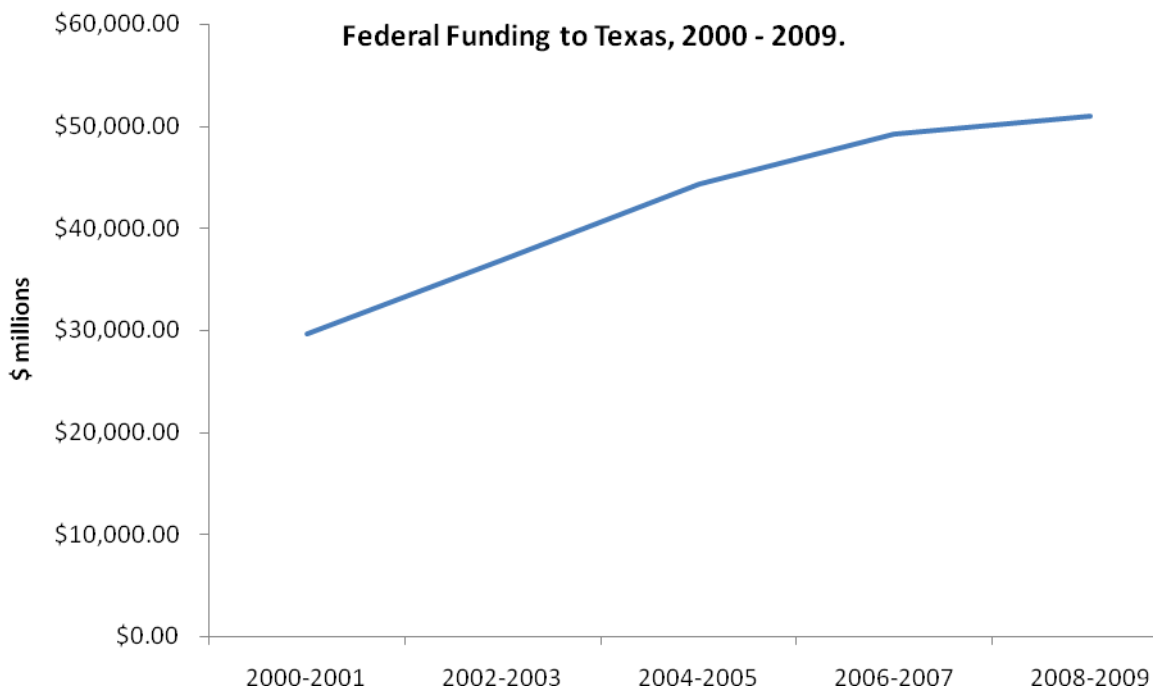
If the government wants to ensure meaningful accountability, then we must have transparency at every level of transaction. It is not enough for citizens to know that the EPA made a grant to New Jersey, which in turn made a sub-grant to Newark. We also need to know that Newark made a payment to “Barone Sanitation,” which a citizen with local knowledge could recognize as a firm owned by a councilmember’s son-in-law.²²

Despite these well-documented criticisms of the lack of transparency of federal stimulus funds, the Select Committee report fails to identify how agencies in Texas should record or present their use of stimulus funds. Hiding behind the ubiquitous phrase “all information pertaining to Federal stimulus funding,” the report does not make serious recommendations related to adopting a standardized

process or recording and documenting information, or indeed a standardized method of presenting information to the public. The Select Committee’s overtures to transparency ring hollow.

Recommendation 5: Highest and Best Use of Stimulus Funds

Without defining the meaning of the phrase, the Select Committee report recommends utilizing stimulus funds based on the “highest and best use” of each part of the funds. The report specifically asserts that “this is a unique opportunity to...draw down significant Federal matching funds.” This assertion is plainly false: there is nothing unique about drawing down federal funds. Indeed, using state funds to draw down matching funds from the federal government is common practice that occurs in multiple parts of the state budget *every biennium*. This process of drawing down federal funds has resulted in massive increase in federal funding to Texas:



Source: Legislative Budget Board

As the chart shows, federal funding has increased by more than \$20 billion in the last decade alone. This expansion of government is almost entirely as a result of using state funds to draw down federal dollars. Furthermore, the concept of “federal dollars” is a myth: all federal dollars are paid by state taxpayers and Texans lose out in the process.

Questions from the Speaker:

The Select Committee was directed to respond to a number of questions from the Speaker of the House. Those questions, the Committee's responses, and a conservative rebuttal are presented here:

1. Where do we get the most use of the stimulus funds in the budget – where can we maximize freed-up General Revenue and/or pay for one-time items?

In response, the Select Committee report makes an argument for vast and permanent expansions to health & human services programs that will far outlast the the one-time influx of federal stimulus funds.

The Select Committee report argues “we can maximize freed-up General Revenue by reinvesting those funds in programs that draw down significant matching funds, e.g., providing 12-month continuous eligibility for children enrolled in Medicaid...” These represent major policy changes and vast expansions to state health care programs. Federal stimulus funds should not be used as an excuse to change state policy or expand state programs, though, like President Obama's Chief of Staff Rahm Emanuel, the Committee report appears enthusiastic about not letting a “crisis go to waste.”

Expanding Medicaid is precisely the kind of expansion that the state must guard against. Clearly, the Committee report runs counter to Special Provision 9 of Article XII of the House Committee Substitute to Senate Bill 1 (Prohibition on Expansion of State Government), which was passed out of the Senate Finance Committee with 15 aye votes to zero nays; and out of the House Appropriations Committee with 27 aye votes to zero nays.

Furthermore, accepting federal matching funds carry great costs. The Arduin, Laffer & Moore report notes that:

...growth in government crowds out growth in the private sector. Increases in government expenditures as a share of domestic output causes an increase in the expenditure wedge and an overall decrease in private sector growth.²³

Additionally, this section of the Select Committee report bases much of its reasoning on the false notion of the “multiplier effect”, stating: “the multiplier effect of health care spending is high and will result in lower tax burdens and maximum economic stimulus effect.” The Select Committee report makes no effort to substantiate how increases in both state and federal spending on health & human services programs will *lower* taxes and stimulate the economy.

The “multiplier effect” is a false economic machination with little definite impact. As Alan Reynolds, a senior fellow of the Cato Institute, explains:

Because people employed in burying and digging up bottles will supposedly employ other people by spending their paychecks, the initial increase in government spending was thought to have a *multiple* effect on total spending. And that, said [John Maynard] Keynes, will lead to an “increase in employment and hence in real income.” But checks received for producing nothing are not *real* income. Real income per worker depends on real *output* per worker — incentives to *produce*, not incentives to spend.

If there is no multiplier effect, the multiplier is one — a billion dollars of government spending adds a billion to national income, but no more.²⁴

Transfers of wealth by the government may translate into “income” for some, but there is no multiplier effect from government spending on health care or any other policy goal. The stimulus, and the health care recommendations of the Select Committee report, amount to wealth redistribution, not wealth creation.

Furthermore, the Select Committee report makes a contrived argument that significant expansions to public health care programs are a one-time expenditure, but remains silent as to any other one-time, responsible uses of federal stimulus money. Such uses could include:

- ★ The purchase of bonds to reduce state debt.
- ★ Additional appropriations to border security law enforcement efforts.
- ★ Hurricane recovery.
- ★ Purchase learning materials such as textbooks and technological equipment that contributes to student learning, including electronic textbooks and other devices appropriate for the use of technology in the classroom.
- ★ Fund the Virtual School Network.
- ★ Provide resources for professional development for educators in Texas’ public schools.

2. How do we avoid expanding existing programs with one-time Federal funds?

The Select Committee report makes no attempt to consider how we might avoid expanding existing programs. In fact, the contrary is true. As noted above, the report actually argues for expanding Medicaid and makes the specious argument that “expanding existing programs may be unavoidable unless we are willing to turn back Federal funds...” A willingness to turn down federal funds in some instances is precisely the type of sensible policy that would help the state avoid deficits in future years.

Legislators must avoid any and all uses of federal stimulus funds and freed-up General Revenue that will create a new and/or ongoing obligation for Texas taxpayers once the one-time stimulus funds are spent.

Additionally, if existing health & human services programs are expanded to draw down federal matching funds, as suggested by the Select Committee report in answering the Speaker’s first question, then the answer to the second question is a foregone conclusion.

In their January 30 letter, the Lieutenant Governor and the Speaker argued that: “we must avoid spending one-time money on on-going projects which will result in unsustainable future costs to the state budget.”

In their February 11, 2009 letter, the Board of Directors of the Texas Conservative Coalition agreed, writing:

We must not be tempted by irresponsible and short-sighted measures. Our budget will be unsustainable if we permit the stimulus package to grow the size of Texas government. The best use of the stimulus funds, beginning as early as the current budget year, would be non-recurring expenses for capital outlays, equipment purchases, technology enhancements and a short-term, sunsetted, intensive workforce skills training program to help the unemployed get through the current financial crisis.

Ensuring that the one-time influx in federal stimulus funds does not grow the state budget permanently is the central policy debate of the 81st Texas Legislature. The Select Committee report is wrong to suggest that expanding existing programs is “unavoidable”. There are numerous one-time expenditures that the Legislature should consider as a top priority in spending stimulus funds.

3. How can UI provisions be implemented to comply with Federal requirements but avoid long-term costs to the trust fund?

While Unemployment Insurance stimulus monies are discussed at length on pages 20 and 21, the Select Committee report's answer to Speaker question number three makes a misrepresentation of the costs of accepting the federal Unemployment Insurance monies and the strings attached.

The Select Committee report claims that the annual cost of "modernizing" the Texas Unemployment Insurance program is \$75 million per year, arguing that the \$555 million in federal money "will cover the cost for approximately 7.5 years (10 years if the time-value of money is factored in)".

However, the fiscal note to House Bill 2623 (which would make the changes to statute necessary to qualify for the federal money), notes a cost of \$506,436,886 (over five years) to the Unemployment Trust Fund. The need for more state employees to administer the expanded Unemployment Insurance program will cost \$16,151,240 over five years. In total, House Bill 2623 is estimated to cost \$522,588,126 over five years, or over \$130 million per year. This far exceeds the Select Committee estimate of \$75 million per year, and would represent a permanent cost to employers in barely over 4 years, as opposed to the 7.5 years suggested by the Select Committee.

4. How can we ensure that agencies will maximize use of the funds and get them out of the door as quickly as possible?

While the Select Committee report correctly notes that "agencies are receiving funds right now and the Legislature has yet to establish any reporting, accountability or transparency requirements," the Committee makes no effort to explain how it might be possible to expedite expenditures. Indeed, state agencies, notably the Texas Department of Transportation, has already designated federal stimulus funds for specific projects long before the Committee report was issued.

Even though the Committee fails to address the Speaker's question, the underlying premise of speeding through expenditures without careful deliberation leads to poor public policy. The entire stimulus package was debated and passed in less than one month. States are still determining the implications of the excessive and unprecedented spending contained therein. Additionally, the stimulus bill makes at least two policy mandates that are antithetical to conservative principles: forcing states to expand Unemployment Insurance programs to receive federal funds; and reversing welfare reform by doing away with block grants and returning to funding state welfare programs based on enrollment (which incents states to increase enrollment). The federal government simply has no business dictating terms under the Tenth Amendment to the Constitution. Yet, in the "rush" to get stimulus funds flowing to the states, Congress attempted to usher in significant policy changes without serious debate.

Legislation is best when it is deliberative and slow. To the extent possible given federal law and federal rules, spending of the federal stimulus should not be rushed.

Furthermore, where the Select Committee report calls for public announcements, advertising, and public education by state agencies, there are multiple resources existing so that new efforts by the state need not be made; two such resources are: www.ReadtheStimulus.org and www.StimulusWatch.org. Additionally, the Legislative Budget Board currently maintains a Texas Budget Source website that could serve as a resource for tracking stimulus spending and contracts related to stimulus spending. Texas need not reinvent the wheel or engage in advertising efforts to make information widely available to the general public.

This is a recommendation in search of a problem. The state should not engage in the practice of making expenditures on advertisements and public education programs, only to spend more money as those programs grow. This is another example of the Select Committee ignoring and exceeding its charge from the Speaker. Advertising and public education are not consistent with making “recommendations to any standing committee of the house regarding legislation necessary for the state to *receive* federal funds for economic recovery.”²⁵ [emphasis added]

5. What sort of federal accountability requirements can we expect we’ll have to deal with?

The Select Committee Report notes that “Texas was selected as one of 16 states the U.S Government Accountability Office will monitor and audit regularly.” As result, the report concludes, “the state will need to exercise greater diligence in requiring transparency and accountability.”

This conclusion is correct, and the Select Committee makes a number of recommendations pertaining to transparency and oversight. However, these recommendations (discussed on page 11 of this report) are poorly thought out and would result in duplicative effort on the part of state agencies and institutions of higher education. The state should utilize the expertise and existing capabilities of the Comptroller of Public Accounts and the Legislative Budget Board to track stimulus spending.

Specifically regarding the federal government’s decision to monitor Texas closely, a rider should be attached to the 2010-11 biennial budget that requires the State Auditor’s Office to monitor all stimulus funds to ensure that they are used appropriately, and that stimulus funds are not wasted or used inefficiently. In this way the state can have an additional measure to ensure agencies meet all federal requirements.

Agency Testimony:

A range of state agencies that are eligible to receive stimulus funds provided testimony to the Select Committee:

- **Texas Department of Housing and Community Affairs (TDHCA)**

The Select Committee’s report indicates that TDHCA will receive \$565 million in additional funding under the federal stimulus package, including:

- \$42 million for homelessness prevention
- \$327 million for weatherization
- \$48 million for community services grants
- \$148 million for the HOME Investment Partnerships Program

These uses of stimulus funds confirm that the federal stimulus is simply a tool to grow government. Using government funds to attempt to prevent homelessness and to subsidize community services may be fine policy objectives but have nothing to do with “stimulating” the economy; instead, it simply grows government. The House Committee Substitute for Senate Bill 1 (81R) recommends \$331 million in normal biennial funding for TDHCA; federal stimulus funds from Article XII increase that funding by more than 170 percent to \$896 million.

- **Texas Department of Transportation (TxDOT)**

TxDOT will receive roughly \$2.25 billion in stimulus funding. Road building and construction is perhaps the most appropriate use of stimulus funds; in Texas many highway construction projects are literally “shovel-ready” and TxDOT has already begun to distribute funds.

The Select Committee report notes that “only 27 percent of new construction funds are [sic] in ‘economically distressed’ areas.” This is in reference to a requirement in the federal stimulus legislation that “economically distressed” areas be given priority for transportation construction projects. This illustrates the flawed nature of the stimulus funding: paying for road construction is an appropriate use of federal funding, yet states should be free to determine where and how transportation funding can be best used.

Transportation needs may be greatest in relatively affluent areas with high levels of congestion, while spending transportation funding in “economically distressed” areas would create a smaller overall benefit, and be a less-effective use of funds. In short, a bridge to nowhere.

- **Texas Health and Human Services Commission (HHSC)**

The Select Committee reports that HHSC will receive \$4.7 billion in federal stimulus funding. A proportion of the stimulus funds are associated with a temporary increase in the Federal Medical Assistance Percentage (FMAP) – the rate at which federal funds “match” those expended on Medicaid at the state level. The federal stimulus legislation stipulates that increased FMAP funds cannot be received by a state that:

- Enacts more stringent Medicaid eligibility requirements than those in effect on July 1, 2008.
- Deposits “freed-up” state revenue into a rainy day or state reserve account.

These provisions mean that if Texas takes Medicaid stimulus funding, the state cannot tighten Medicaid eligibility requirements beyond those currently in effect, and cannot deposit General Revenue freed-up by Medicaid stimulus funds into the Economic Stabilization (Rainy Day) Fund.

These provisions are a clear over-reach of federal authority and another illustration of the fact that the federal stimulus legislation is simply intended to grow government to the detriment of taxpayers. Using stimulus funds for the Texas Medicaid program will not stimulate the economy; yet, by accepting stimulus Medicaid funds, the state will become tied to arbitrary Medicaid eligibility standards (ignoring the fact that Medicaid and CHIP eligibility requirements have been a subject of much legitimate legislative deliberation over the past decade in Texas), and is not able to use freed-up General Revenue to guard against future shortfalls and protect taxpayers.

- **The Texas Workforce Commission (TWC)**

The Select Committee report focuses on the \$555 million that Texas is able to receive for unemployment insurance as a result of the stimulus legislation. The report notes the changes to Texas’ unemployment insurance program that must be made for the state to receive the funds; and suggests that these changes should be made.

The required changes represent an unprecedented expansion of Unemployment Insurance eligibility to new groups. Expanding eligibility for Unemployment Insurance would increase the cost of the program in future years, which would place permanent burdens on Texas businesses and workers, just to access one-time federal money.

On March 31, the Legislative Budget Board estimated that House Bill 2623, which would make some of the changes required by the federal stimulus legislation, will cost the state and employers in excess of \$522 million over five years.

There are only four states with existing Unemployment Insurance eligibility requirements that would meet those established in the stimulus package. Those states each have higher average

tax rates on total wages than Texas. And while Texas created more new jobs than any state in 2008, those four states – Maine, New Jersey, New Mexico, and New York – lost almost a quarter of a million jobs between them in 2008.

In 2002, the state was in a similar position when the national economic picture contributed to increased unemployment and looming state budget shortfalls around the country. Unlike today, the federal government then made a no-strings-attached distribution to states, giving Texas \$596 million in federal unemployment funds to help cover benefit payments. If the President and Congress were truly concerned about unemployed Americans, they should give the states federal funds without strings attached just as the Bush Administration and Congress did in 2002.

Furthermore, the \$555 million rejected by the Governor is not “stimulus” money. Instead, it is money from the federal unemployment fund that is filled in part by taxes paid by Texas employers. The stimulus package only enacted the unacceptable hoops through which we were asked to jump to access the funds.

Texas’ approach to job creation and economic growth is rooted in the principle that the best way to retain existing jobs and create new jobs is to minimize the cost of government on employers. It is our businesses – large and small across the state – that create jobs. As a result of Texas’ low tax burden, the state is the country’s jobs leader. Texas is home to more Fortune 500 companies than any other state, and has created more than one million net new jobs in the last six years.

Accepting the federal Unemployment Insurance funding would create an additional tax burden on Texas’ businesses, which in turn would stymie job growth when we need it more than ever. Also, rejecting the federal Unemployment Insurance funds is a sound fiscal approach for Texas that is consistent with a healthy respect for the principle of federalism.

- **The Texas Education Agency (TEA) and the Texas Higher Education Coordinating Board (THECB)**

The majority of education stimulus funds flow directly to public schools and institutions of higher education via funding formulas. However, the Select Committee report notes that \$3.273 billion is available for the state to appropriate for education purposes, yet makes no recommendation as to how this money should be spent.

The Texas Conservative Coalition has issued recommendations in support of using education stimulus funds to:

1. Purchase learning materials such as textbooks and technological equipment that contributes to student learning, including electronic textbooks and other devices appropriate for the use of technology in the classroom.

2. Fund the Virtual School Network.
3. Provide resources for professional development for educators in Texas' public schools.

As a matter of fiscal responsibility, stimulus funds should be used only for non-recurring expenses for capital outlays [such as transportation and infrastructure construction], equipment purchases, [and] technology enhancements. The three policy goals listed above meet those requirements:

Instructional Materials

- Using some portion of the federal stimulus education funding to pay for instructional materials such as textbooks and other learning technologies will help ensure that the stimulus funds are not used to permanently grow government or create ongoing obligations for TEA or Texas' school districts.
- Currently, revenue from the Permanent School Fund (PSF) is used to purchase instructional materials for public schools. However, as a result of declining market conditions over the past year, available revenues from the PSF could leave the state with a shortfall of anywhere from \$300 million to \$1.4 billion. Using stimulus funding to purchase instructional materials will help meet this shortfall.

The Virtual School Network

- Federal stimulus funding should also be used to fund the Virtual School Network. The Texas Education Agency has issued an exceptional item request to fund this program in the amount of \$18 million for 2010-11.
- The Texas Virtual School Network (VSN) was created by the 80th Legislature through the passage of Senate Bill 1788 in 2007. The VSN alleviates teacher shortages and scheduling conflicts by providing students access to advanced classes in which they would not normally be able to participate. Funds were used from Rider 31 to establish the network in FY2008.
- Fully funding the VSN will be particularly beneficial because it directly addresses the challenges that school districts face with regard to classroom space and transportation. Students will be able to study the very best courses in the state on the virtual school network without placing any burden on a new school in terms of classroom space or transportation costs. Additionally, through a virtual school network, school districts could share the costs of providing courses that they would not otherwise be able to afford.

Professional Development

- The Texas Education Agency has an exceptional item request for professional development funding in the amount of \$53.66 million for 2010-11. The request is the number one priority of the TEA's exceptional items. The funds would be used for, among other things, professional training for end of course exams. "Stimulus" funding for professional development programs would help meet this budget request.
- Professional development funding as requested by TEA will help build the infrastructure necessary for schools to be successful as both curriculum standards get tougher and the state implements end-of-course exams.

Structural Deficit:

The Select Committee report makes false claims relating to the nature of the “structural deficit” that the state will face in the next budget cycle. The report spuriously asserts that:

A “structural deficit” differs from a “cyclical deficit” in that it exists even when the economy is operating at its full potential. No matter how good the economy gets, the deficit cannot be cured.

That definition is manifestly false. Article III, Section 49a of the Texas Constitution establishes that:

It shall be the duty of the Comptroller of Public Accounts in advance of each Regular Session of the Legislature to prepare and submit to the Governor and to the Legislature upon its convening a statement under oath showing fully the financial condition of the State Treasury at the close of the last fiscal period and an estimate of the probable receipts and disbursements for the then current fiscal year...**no appropriation in excess of the cash and anticipated revenue of the funds from which such appropriation is to be made shall be valid.** No bill containing an appropriation shall be considered as passed or be sent to the Governor for consideration until and unless the Comptroller of Public Accounts endorses his certificate thereon showing that the amount appropriated is within the amount estimated to be available in the affected funds.
[Emphasis added]

Under the Texas budget process established in the Constitution, the concept of a “deficit” – structural, cyclical, or otherwise – does not exist. The Comptroller is required to certify the available revenue for the upcoming biennium and the Legislature is charged with allocating that revenue through the appropriations process. The concept of a deficit only arises through an assumption that all obligations funded in the previous biennium will be funded in perpetuity and at ever-increasing levels. This is at odds with the Texas Constitution, which requires that the Legislature appropriate only *certified available revenue*, not that the Legislature must fund every existing program, even if revenue is not available.

Additionally, the report blames the school district property tax relief enacted in 2006 for creating what it calls a “structural deficit” because “tax revenues anticipated from the 2006 property tax relief are lower than projected at the time.” Even if a structural deficit existed (which it does not), singling out property tax relief as the sole cause of a “deficit” is disingenuous: the Legislature enacted and funded property tax relief just as it enacts and funds a vast array of other programs. It can just as reasonably be argued that growth in Health and Human Services programs has created a deficit: Over the past decade, state (General Revenue) Medicaid spending has increased from \$6.9 billion in 2000 to \$14.5 billion in 2009²⁶, thus creating – in the Select Committee’s parlance – a \$7.6 billion “structural deficit” in the state budget.

Using property tax relief as a scapegoat is a politically-motivated position that ignores the numerous other expenditures that drive state budget growth. The Select Committee was created to “make recommendations to any standing committee of the House *regarding legislation necessary for the state to receive federal funds for economic recovery.*”²⁷ In concluding that “had the 2006 Property Tax Relief

Initiative been revenue neutral or not enacted...Texas would today have a \$700 million surplus in its recurring budget,” the Select Committee oversteps its authority.

Furthermore, the Select Committee report implicitly argues that property tax relief was a misguided or inappropriate policy decision, despite the fact that the Legislature was forced via court order to remedy constitutional shortcomings in the system of school finance and without regard to the increasingly heavy property tax burden on homeowners and businesses.

In general, to assert that a shortfall is a “structural deficit” that *cannot be cured* is false. Increased tax receipts accruing from economic growth, or cutting state expenditures would immediately address any state budget shortfall.

The Texas Conservative Coalition has supported several proposals to meet state priorities without raising taxes. For example, Lieutenant Governor Dewhurst and Speaker Straus called for a 2.5 percent spending cut for the 2010-11 biennium. In a January 30, 2009 letter to the Comptroller of Public Accounts, Lt. Gov. Dewhurst and Speaker Straus noted that:

[W]e will be looking for recommendations to reduce the Fiscal Year 2009 General Revenue and General Revenue-Dedicated appropriations by approximately 2.5 percent.

Cutting state expenditures in targeted areas would address budget shortfalls and help ensure that essential state services and obligations can be met. According to Lt. Gov. Dewhurst and Speaker Straus:

We do not anticipate an across the board cut if we have your guidance as to how to specifically achieve that goal while still preserving the funding for essential programs, including but not limited to the Foundation School Program, acute care Medicaid, CHIP and debt service for previously issued debt.

In addition to a targeted budget cut, TCC is also supportive of a stronger state spending limitation. The current constitutional spending limitation is poorly constructed and has not restricted state spending as much as could be expected. This is because the existing state spending limit (found in Article VIII, Section 22 of the Texas Constitution) limits spending growth to growth in personal income.

However, as personal income grows, government spending should *decrease* since individuals and families earn more money. According to the Legislative Budget Board, the measure of personal income in Texas includes “social security, various retirement and unemployment insurance benefits, welfare, and disability [payments].”²⁸ Fundamentally, this makes personal income growth an ineffective restriction on state spending: when the state increases spending on welfare programs, aggregate personal income increases, leading to an even higher allowance for government growth. Rather than personal income, using growth of Texas’ population plus inflation (which reflects the increased cost of providing services to the population), would result in a far more effective constitutional spending limit.

It should not be surprising that Texas encounters occasional budget shortfalls when the state’s spending limit is so poorly constructed. Indeed, analysis by the Legislative Budget Board reveals that the state budget would have been \$21.6 billion lower in the 2006-07 biennium had a stricter constitutional spending limit (limiting budget growth to population growth plus inflation, and applying to all funds)

been introduced ahead of the 1990-91 biennium.²⁹ A more-effective spending limit could permanently eliminate deficits – both structural and cyclical – while still funding essential needs and services and the Property Tax Relief Fund.

ENDNOTES

- ¹ President Barack Obama, Monday, February 9 Press Conference. Transcript online at: <http://www.cnn.com/2009/POLITICS/02/09/obama.conference.transcript/>
- ² Brian M. Riedl, *CBO Budget Baseline Shows Historic Surge in Spending and Debt*, The Heritage Foundation, January 7, 2009; Online at: <http://www.heritage.org/Research/Budget/wm2193.cfm>
- ³ Government Printing Office, *Budget of the United States Government Fiscal Year 2009*, Summary Tables; Online at: <http://www.gpoaccess.gov/usbudget/fy09/pdf/budget/tables.pdf>
- ⁴ Arduin, Laffer & Moore Econometrics for TPPF, *The Economic Impact of Federal Spending on State Economic Performance: A Texas Perspective*; April, 2009. Online at: <http://www.texaspolicy.com/pdf/2009-04-federalspending-laffer-final.pdf>
- ⁵ Council of Economic Advisers; at: Recovery.gov, Impact; <http://www.recovery.gov/?q=content/impact>
- ⁶ Council of Economic Advisers, *Estimating Job Creation by State*, February 23, 2009; Online at: <http://www.recovery.gov/files/estmethods.pdf>
- ⁷ Dubay, Campbell, and Winfree, *Economic Stimulus Pushed by Flawed Jobs Analysis*, The Heritage Foundation, January 28, 2009; Online at: <http://www.heritage.org/research/economy/wm2252.cfm>
- ⁸ Texas Workforce Commission TRACER, Labor Market & Career Information; Online at: <http://www.tracer2.com/cgi/dataanalysis/?PAGEID=94&SUBID=142>
- ⁹ Legislative Budget Board, Fiscal Size-Up 2008-09; Online at: http://www.lbb.state.tx.us/Fiscal_Size-up/Fiscal%20Size-up%202008-09.pdf
- ¹⁰ Texas Comptroller, *Winter 2008-2009 Forecast*; Online at: <http://www.texasahead.org/economy/fcst0809/winter0809rgspcalendar.html>
- ¹¹ U.S. Census Bureau, *State & County Quick Facts*; Online at: <http://quickfacts.census.gov/qfd/states/48000.html>
- ¹² Speaker of the House of Representatives Joe Straus, *Proclamation on the Appointment of Select Committee on Federal Economic Stabilization Funding*, February 12, 2009.
- ¹³ Office of the Governor, Texas Enterprise Fund Grant Listing, as of February 28, 2009; Online at: http://governor.state.tx.us/files/ecodev/TEF_Listing.pdf
- ¹⁴ Texas Workforce Commission, Skills Development Fund. Online at: <http://www.twc.state.tx.us/svcs/funds/sdfintro.html>
- ¹⁵ Fortune 500, CNNMoney.com; online at: <http://money.cnn.com/magazines/fortune/fortune500/2008/states/TX.html>
- ¹⁶ Charles Gibson, ABC World News Tonight, *Lone Star Lure*, March 23, 2009; Online at: <http://abcnews.go.com/Video/playerIndex?id=7154605>
- ¹⁷ National Conference of State Legislatures, *Update on State Budget Gaps: FY 2009 & FY 2010*; February 2, 2009; Online at: <http://www.ncsl.org/programs/pubs/statebudgetgaps.pdf>
- ¹⁸ Texas Comptroller of Public Accounts, *Comptroller's Economic Outlook*, April 9, 2009; Online at: <http://www.texaspolicy.com/pdf/2009-04-federalspending-laffer-final.pdf>
- ¹⁹ Bureau of Labor Statistics, Local Area Unemployment Statistics, as of April, 2009; Online at: <http://www.bls.gov/lau/>
- ²⁰ Legislative Budget Board Fiscal Note for the Committee Substitute to House Bill 4586 (81R)
- ²¹ Office of Management and Budget, Initial Implementation Guidance for the American Recovery and Reinvestment Act of 2009, Feb. 18, 2009, pages 14-15, available at <http://www.whitehouse.gov/omb/asset.aspx?AssetId=703>.
- ²² Jerry Brito, Testimony before the U.S. House Committee on Oversight and Government Reform, March 19, 2009.
- ²³ Arduin, Laffer & Moore Econometrics for TPPF, *The Economic Impact of Federal Spending on State Economic Performance: A Texas Perspective*; April, 2009. Online at: <http://www.texaspolicy.com/pdf/2009-04-federalspending-laffer-final.pdf>
- ²⁴ Alan Reynolds, *Faith Based Economics*, National Review Online, February 9, 2009; Online at: <http://nrd.nationalreview.com/article/?q=YzVhZmI5MDAxMDEyZGIzMWVlZTUzZWU1ZDY2ZjExNTQ=>
- ²⁵ Speaker of the House of Representatives Joe Straus, *Proclamation on the Appointment of Select Committee on Federal Economic Stabilization Funding*, February 12, 2009.
- ²⁶ Texas Health and Human Services Commission, Texas Medicaid & CHIP in Perspective, January 2009.

²⁷ “Proclamation: Appointment of Select Committee on Federal Economic Stabilization Funding,” Speaker Joe Straus, February 12, 2009.

²⁸ “Tax Relief Amendment Implementation Limit on Growth of Certain State Appropriations,” Legislative Budget Board.

²⁹ Legislative Budget Board Analysis of HJR53(80R).