

Cato Institute Briefing Paper No. 20: Missouri's Hancock II Amendment: The Case for Real Reform

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Executive Summary

In November 1980 Missouri voters approved the Hancock amendment, a constitutional amendment intended to prevent the Missouri state budget from growing faster than the Missouri family budget. Since then the effectiveness of that amendment has been eroded as legislators have discovered ways to evade its restrictions by exempting certain revenues from the cap. Those evasions have cost Missourians \$5 billion in higher taxes.

On November 8 voters in Missouri can repair the Hancock amendment by enacting the Hancock II amendment. Because it more precisely defines "total state revenue," Hancock II would be more difficult for politicians to evade.

The opposition's scare tactics--claiming that Hancock II will require a \$1-billion tax refund and necessitate massive spending cuts and service disruptions--are inaccurate and misleading. Any reduction in spending that may be necessary to comply with Hancock II would be only about one-eighth the size of the opposition's alarmist predictions.

Introduction

Missouri is one of 23 states that have some form of tax and expenditure limitation (TEL) to restrict the growth of the state budget. In November 1980 Missouri voters approved a constitutional amendment--called the Hancock amendment after its sponsor, Mel Hancock--that prevents the state government from increasing the percentage of residents' incomes taken as state revenues without voter approval.

Like most TELs, the Hancock amendment was initially effective at restraining the growth of state taxes and spending. However, over the years that effectiveness has been eroded as legislators--aided by sympathetic court rulings-- have discovered ways to evade the voter-imposed restrictions by exempting certain revenues from the cap.[1] For example:

* In 1982 only 2 percent of Missouri state revenue was considered exempt from the revenue limit. In 1993 the uncapped portion was nine times higher, or 18 percent.

* Increasing the amount of revenue excluded from the revenue limit has allowed Missouri's state politicians to collect \$5 billion more in revenue over fiscal years 1982- 93, than the Hancock amendment would have permitted.

* Since the Hancock amendment took effect, state own- source revenue, on a per capita basis, has risen 56 percent, the third fastest rate of state tax growth in the nation.

* Though state revenue was not supposed to rise faster than Missouri residents' incomes, between 1982 and 1993 state revenue grew by 134 percent while Missouri personal income grew by only 112 percent.

* In FY95 alone, due in part to state senate bill 380-- a \$310-million tax hike passed in 1993 but not approved by the voters--state revenue will rise 9.4 percent, more than double the 4.1 percent rise in Missourians' incomes.

Many Missouri residents would like to restore the integrity of the original Hancock amendment (Hancock I hereinafter). To that end, a new amendment, Hancock II, has been placed on the ballot this year. Because it provides a more precise definition of "total state revenue"--the item being limited--Hancock II would plug the loopholes that have substantially undermined the effectiveness of Hancock I.

One of the leading critics of Hancock II has claimed that the measure will require an immediate taxpayer refund of \$1 billion and that it will "completely change the way the state does business." However, as this analysis shows, the opposition's scare tactics are inaccurate and misleading. Any reduction that might be necessary to comply with Hancock II's restraints would be only about one-eighth the size of the opposition's alarmist predictions. Such a cut would not be as much evidence that Hancock II is a draconian measure as it would be indicative of just how successfully state politicians have been able to evade the voter-imposed restrictions of Hancock I. Hancock II would simply enforce the constitutional requirement that the Missouri state budget not grow faster than the Missouri family budget.

How Politicians Avoid the Constraints of Voter-Imposed Tax and Spending Limits

In 1978 the passage of California's revolutionary Proposition 13--which rolled back property taxes and severely restricted their rate of annual growth--launched a grassroots citizens' tax revolt that swept across the nation. By 1982, 20 states--including Missouri--had adopted some form of TEL. Although those measures were initially effective at reining in the growth of state government, over the years their effectiveness has been eroded as big-spending politicians have discovered ways to evade the restrictions.

For example, since many TELs apply (or are interpreted as applying) to only the general fund, one common way of circumventing a spending cap has been to set up new "special funds," which, by definition, are exempt from the cap. Similarly, state legislatures have enacted "earmarked" taxes, the revenue from which is set aside in a separate fund, exempt from most voter-approved caps. Such end-runs around the will of the people have eviscerated nearly all of the Proposition 13-era tax and spending limits, including Missouri's Hancock I.

Evidence that the effectiveness of TELs declines over time can be found by examining spending growth in the 15 states that had binding TELs in place by 1980.[2] From 1980 to 1985 the real growth rate of per capita state spending in those states was 3.5 percentage points below the U.S. average (6.3 percent vs. 9.8 percent). However, from 1985 to 1990 spending in those states actually rose faster than the U.S. average (16.7 percent vs. 16.3 percent).[3]

It seems that no matter how explicitly voters try to constrain the tax and spending powers of state government, politicians eventually find ways to circumvent those constraints.

Missouri's Hancock Amendment (1980): A History of Evasion

Missouri's original Hancock amendment, passed by the voters in 1980, has been routinely thwarted by the Missouri legislature. Hancock I was intended to prohibit the state legislature from increasing the percentage of Missourians' income taken as state revenue. (In that way it was similar to many of the other Proposition 13-era TELs.) Beginning with fiscal year 1982 (the first full fiscal year after Hancock I passed), that ratio was not allowed to rise above its level in FY81, when total state revenue consumed 5.64 percent of personal income.[4] In each fiscal year thereafter, the revenue limit was to be determined by multiplying the relevant personal income amount by the original ratio of 5.64 percent.[5]

Hancock I defined the specific item it intended to limit, total state revenue, as follows.

"Total state revenues" includes all general and special revenues, licenses, and fees, excluding federal funds, as defined in the budget message of the governor for fiscal year 1980-1981. Total state revenues shall exclude the amount of any credits based on actual tax liabilities or the imputed tax components of rental payments, but shall include the amount of any credits not related to actual tax liabilities.[6]

Apparently, that language was not explicit enough for state officials. In its first annual review of Hancock I, the state Auditor's Office described the situation as follows.

The amendment, beyond the language above [section 17 (1), above], is not specific as to the types of revenues that are included or excluded in determining TSR [total state revenue]. Further, the amendment does not specify the methodology to be used in determining TSR. Consequently, the division [7] [Missouri budget office] established procedures to calculate TSR. The division also had to make certain decisions as to items that would be either included or excluded, except for items ruled on by the attorney general or the Missouri courts. [8]

Much of the confusion stemmed from the failure of the legislature to enact implementing legislation. That left unanswered the question of which agency was responsible for enforcing and monitoring the state's compliance with the amendment. The Missouri budget office, an executive-branch agency under the control of the governor, took upon itself the responsibility of fulfilling that crucial role. Nevertheless, the state Auditor's Office has also tried to define the revenue limit by producing its own annual reports on Hancock I. Those reports have often been in disagreement with the findings of the budget office. As a result, there is no consensus on what "total state revenue" is each year, nor on whether or how much the limit has been exceeded. Much of that confusion could have been avoided if the legislature had simply passed implementing legislation, something it still has not done after 14 years.

The problem was complicated by the passage, in November 1982, of Proposition C, the first major voter-approved tax hike since the passage of Hancock I. Proposition C was a \$0.01 sales tax hike, 1/2 of which was earmarked to roll back local property taxes and the other 1/2 of which was devoted to public schools.[9] The Missouri budget office asserted that since Proposition C was approved by the voters, it was not subject to the revenue limit. The state Auditor's Office concurred, stating that "including voter approved increases as TSR achieves the illogical result that voters agreed to additional taxes so they could receive a refund."

That analysis misses the point. Proposition C did not include a provision excluding its revenue from the Hancock limit. Thus, all that voters approved in passing Proposition C was a statutory \$0.01 sales tax hike earmarked for particular purposes. They clearly did not endorse excluding that revenue from the limit. Further, as a statute, Proposition C can have no bearing on the constitutional revenue limit that voters approved when they passed the Hancock amendment in 1980. If Proposition C had caused total revenue to exceed the limit, the legislature could have complied with Hancock I by cutting other nondedicated taxes.

Nevertheless, the Missouri Supreme Court, in *Goode v. Bond* (1983), agreed with the budget office's contention that voter-approved tax increases--even statutory ones--should not be subject to the revenue limit.[10] That ruling created a loophole in the Hancock amendment. Further, it indicated to state politicians who disliked the constitutional constraints of the Hancock amendment that they could evade those constraints without actually amending the constitution. That could be achieved by sending statutory tax increases--for example, ones dedicated to high-priority programs such as schools, roads, and prisons--to the voters for approval. If approved, those sources of revenue, as Proposition C was, would be exempt from Hancock's constitutional revenue cap. In essence, *Goode v. Bond* told politicians that they could amend the state constitution with a statute.

Not surprisingly, since that court ruling, numerous tax-hike proposals have appeared on the ballot. Three such proposals were approved by the voters as constitutional amendments, the language of which clearly excluded their revenues from the Hancock revenue limit.[11] However, like Proposition C, Proposition A--a motor fuel tax--was statutory and did not contain any provision for excluding its revenue from the Hancock revenue limit. Thus, although voters did approve those specific tax hikes, they did not approve excluding those revenues from the limit. Stated differently, by approving Propositions A and C, voters did not approve an overall increase in the tax revenue limit under Hancock, though in effect that is what they have gotten.

In FY95 alone those two sources of revenue that the court excluded from the limit are expected to cost Missouri residents over \$650 million in extra taxes.[12] That amounts to \$125 in higher taxes for every man, woman, and child in Missouri. The next section will shed more light on just how damaging the court's ruling in *Goode v. Bond* has been to Missouri's taxpayers.

The Cost of TEL Evasion

Most observers agree that the current tax burden in Missouri is lower than it would have been without the Hancock amendment.[13] Nevertheless, over the years, thanks to the loophole described above, the amendment's effectiveness at restraining the growth of taxes and spending has been substantially reduced. As a result, despite the fact that voters approved a constitutional limit to the growth of the state budget, taxes and spending have continued to climb in Missouri.

As Table 1 shows, from 1982--the year the Hancock amendment went into affect--to 1992, Missouri's spending growth far outpaced that of its Plains State neighbors and the rest of the country.[14] After adjusting for inflation:

- * Missouri's state budget grew by 63 percent--the 15th fastest in the United States--while the Plains State average grew by only 40 percent.

- * Per capita state spending in Missouri rose by 54 percent--8th fastest in the nation--compared to only 31 percent for the Plains State average.

- * State spending as a share of personal income rose by 22 percent in Missouri--11th fastest in the country--while the Plains State average rose by only 13 percent and the U.S. average by only 12 percent.

As Table 2 indicates, the same pattern holds true for state revenue, which Missouri residents voted to cap in 1980.[15] From 1982 to 1992, after adjusting for inflation:

- * Total own-source revenue in Missouri rose by 65 percent--15th fastest in the U.S.--while the Plains state average rose by only 45 percent.[16]

- * On a per capita basis, state own-source revenue in Missouri climbed 56 percent--3rd fastest in the nation-- compared to only 31 percent for the Plains State average.

- * State own-source revenue as a share of personal income soared by 24 percent in Missouri--10th fastest in the country--while the Plains State average rose by only 13 percent and the U.S. average by only 10 percent.

Clearly, taxes and spending continue to spiral out of control even with the Hancock limit. That growth of taxes and spending is not what Missouri voters intended when they approved Hancock I in 1980. Excessive growth has been caused largely by the court's ruling on the definition of revenue, which excluded revenue from voter-approved tax hikes. Table 3 shows the effect of that redefinition of "total state revenue." (Note: these figures are in current dollars, that is, they have not been adjusted for inflation. Thus the accumulated cost to the taxpayer of evasions of the Hancock limit is actually substantially larger than it appears herein.)

- * The percentage of state own-source revenue[17] considered exempt from the cap skyrocketed from 2 percent in 1982 to 22 percent in 1987. Since then that figure has leveled off at about 18 percent, nine times higher than in 1982.

- * Over the period FY1982-93, the redefinition of "total state revenue" exempted \$4.9 billion in state revenue from the cap.

As Table 4 shows that , contrary to the voters' stated intent in passing the Hancock amendment, political end-runs and anti-taxpayer court decisions have allowed state revenue growth to significantly outpace the growth of Missourians' personal income. (Note: as in Table 3, these figures are in current dollars.)

- * Total state revenue was supposed to increase only as fast as Missouri residents' incomes. However, between 1982 and 1993 state revenue grew by 134 percent while Missouri personal income grew by only 112 percent.[18]

- * Beginning in FY83, only one year after the Hancock amendment went into effect, total state revenue has exceeded the cap every year. The most recent final budget numbers show that the cap was exceeded by nearly \$400 million in

FY93 alone.[19]

* If the intended definition of "total state revenues" had been adhered to, Missouri residents would have paid \$3.7 billion less in taxes over the period 1982-93.[20]

* In FY95 alone, due in part to Senate Bill 380--a \$310-million tax hike for education, passed, but not approved by the voters, in 1993--state revenue will rise 9.4 percent, more than double the 4.1 percent rise in Missourians' incomes.[21]

In sum, state politicians have been very successful at ignoring the original Hancock amendment's call for budget discipline. That amendment merely asked the state government to prevent the budget from growing faster than Missouri residents' ability to pay for it. Indeed, several states have more stringent caps, such as those that restrict revenue growth to the rate of population growth plus inflation. Nevertheless, even Missouri's modest provision could not be adhered to. Despite the clear pattern of abuses, Missouri's legislators continue to claim that the Hancock revenue limit has never been exceeded.[22]

Hancock II: Requiring Voter Approval for New Taxes

In Missouri, as in some 20 other states, politicians have thwarted the will of the people by plainly violating voter-imposed tax and spending limits. In many of those other states voters have approved new amendments to plug the loopholes that were created in their existing TELs. For example, just last year voters in Washington state approved an amendment that limits the growth of state spending to the growth rate of population plus inflation. A similar measure was passed in Colorado in 1992.[23]

This November Missouri's taxpayers will have an opportunity to tighten the constraints of Hancock. As the previous section has documented, the original Hancock amendment has been severely weakened, costing Missouri's taxpayers billions of dollars in higher taxes over the past decade. Those taxpayer losses continue to rise every year. In an attempt to restore the integrity of the original Hancock amendment, the Hancock II amendment has been offered. Hancock II would close many of the loopholes that court rulings and political end-runs have created over the years, thereby making it more difficult for politicians to defy the will of the people.

The new amendment is very similar to the first one. However, as have taxpayer activists in many states, those in Missouri have learned from past experience and written an amendment that is more precise and thus more difficult for politicians to evade. Hancock II would make two main changes:

1. Its definition of "total state revenue"--the specific item being limited--is significantly more precise. Unlike the original amendment, Hancock II explicitly provides that the constitutional revenue limit cannot be exceeded simply by the voters' passing a statutory tax hike (as occurred with Propositions C and A).
2. As did the original, Hancock II contains a voter approval requirement. If politicians wish to increase the percentage of residents' incomes taken as state revenue, they must first obtain the permission of the people who pay those taxes, the voters of Missouri. Such provisions are increasingly popular; they have recently been adopted by several other states and will be on the ballot in many more this year and in the years to come.

The Opposition to Tax Restraint

Despite the reasonableness of measures such as Hancock II, which cap revenue at the rate of income growth, the opposition to such measures is enormous. The most vocal opposition comes from those who benefit directly from government spending, including career politicians, lobbyists, teachers' unions, and government workers. Since those groups have a stake in seeing that government revenue and spending grow, they have tended to campaign strongly against fiscal limitations in Missouri and elsewhere.[24] To overcome the populist appeal of TELs, the opposition frequently resorts to trying to scare voters about the consequences of such measures. They often claim that the TEL would force politicians to make massive cuts in essential government services.

In Missouri the opposition to Hancock II is led by various Missouri educational associations, public employee unions, and organizations that do business with the state. Those groups have organized and funded the Committee to Protect

Missouri's Future. That group commissioned a report estimating the impact of Hancock II on the state budget. The report, written by James Moody, a lobbyist in Jefferson City, has become known as the Moody report. Moody's clients have included several organizations seeking to do business with the state government (for example, firms seeking contracts or leases with state agencies). Moody has worked as a state government administrator for both Democratic and Republican administrations. He is the furthest thing from an unbiased observer.

The Moody report claims that, because Hancock II implements the original intent of Hancock I by eliminating existing loopholes in the definition of "total state revenue," the new measure will require a spending cut--and revenue refund--of \$1.024 billion in FY96.[25] After accounting for monies that are constitutionally earmarked for specific purposes or otherwise exempt from spending reductions, Moody alleges that the result will be an across-the-board cut of 32.36 percent in spending for many of the most popular government services, such as highways, schools, colleges, and prisons. The report goes on to editorialize about the potential impact of those budget cuts. For example, Moody claims:

With this reduction, it appears certain that Missouri will not match all available federal [highway] funds, thereby eliminating necessary improvements to Missouri roads and sending the federal funds for Missouri to other states.[26]

Elementary and Secondary Education will be reduced by \$284.6 million, and this reduction could renew litigation regarding the inadequacy of funding for this purpose.[27]

The quality and delivery system for higher education in Missouri would be shaken to its very foundation. The only feasible approach may to be consider the complete closure of state colleges or universities or community colleges.[28]

The likely policy reaction to a reduction of \$55.42 million [for corrections] would be an enormous reduction in prison bed spaces and shorter sentencing due to a lack of capacity.[29]

The impacts on every department listed above would be dramatic, and may bring their activities nearly to a halt.[30]

The Moody report paints a frightening picture of what would happen if Hancock II passed, one that virtually no one would like to see become a reality. Those conclusions have received widespread media attention all over the state.

Fortunately for Missouri's taxpayers, Moody's analysis is seriously flawed. His assertion that the passage of Hancock II will require massive cuts in state services is inaccurate and misleading.

Assessing the Moody Report

The Moody report claims that the passage of Hancock II will require a tax refund (and thus a spending cut) of \$1.024 billion in FY96. Table 5 shows how that number was derived. As discussed earlier, the main purpose of Hancock II is to return to Hancock I's intended definition of "total state revenue." As a result, certain revenues that the court has interpreted as exempt from the cap are intended to be brought back under Hancock II's cap. In Table 5, Moody's estimates of those amounts are shown as "new revenues included by Hancock II." According to Moody's calculations, adding that "new" revenue to "total state revenue" (as currently defined by the Missouri budget office) causes the sum to exceed the revenue limit by \$516.7 million in FY95 and \$507.2 million in FY96.

Moody assumes that Hancock II will take effect immediately and that the excess revenue from both FY95 and FY96 will be returned to the taxpayers in the form of tax refunds in FY96. (As Moody concedes, however, "an argument could be made that [the FY96] refund would be made in Fiscal Year 1997.")[31] Combining the FY95 and FY96 figures, Moody thus arrives at the sum of \$1.024 billion, which he concludes must be refunded to the taxpayers and cut from the state budget in FY96.

Moody further estimates that the \$1.024-billion budget cut would require a 32.36 percent cut in spending. Table 6 shows how that number was derived. Moody first assumes that, in response to Hancock II, the legislature will repeal two taxes that would have brought in \$182 million in revenue in FY96.[32] Thus, that \$182 million is subtracted from

both the projected level of FY96 revenue and the amount of the spending cut. Moody then excludes \$3,882.7 million in spending that he asserts is protected from spending cuts.[33] That reduces the pool of "unprotected spending," from which \$841.9 million must be cut, to \$2,601.6 million. As Table 6 indicates, and as the Moody report asserts, accomplishing that feat would require spending to be cut by 32.36 percent.

Flaws of Moody Report

Moody's analysis contains four major flaws. Table 7 indicates how those flaws inflate Moody's estimate of the FY96 tax reduction necessary to comply with Hancock II.

1. Moody incorrectly assumes Hancock II applies to FY95. As the text of the Hancock II amendment clearly states, it becomes "effective the first full fiscal year after adoption." [34] Since FY95 is already in progress, it cannot be the first full fiscal year after adoption. Thus, Hancock II would not take effect until FY96. Adjusting for that error lowers Moody's tax reduction estimate by \$516.7 million, the amount of his FY95 tax reduction estimate.

2. Moody's "cut" is not what most people think of as a cut (i.e., it is not an actual reduction from the prior year's level). Moody's analysis employs the misleading "current services baseline" methodology made famous by the U.S. Congress. That is, when Moody claims that Hancock II will require spending to be "cut" by \$1.024 billion, he does not really mean that after the cut the level of spending will be \$1.024 billion less than the year before. Instead, he merely means that spending would be \$1.024 billion lower than it would have been if politicians had continued to let the budget grow unchecked. Adjusting for that misleading accounting trick lowers Moody's estimate of the necessary tax reduction by \$311.2 million, the amount that the Missouri budget office and the Moody report assume revenue would grow from FY95 to FY96 without Hancock II (see Table 5).

3. Moody ignores the 1 percent refund threshold. Hancock II stipulates that a refund is required only if total state revenue exceeds the limit by more than 1 percent.[35] (That is true of Hancock I as well.) Moody's estimates of the "required refund" ignore that 1 percent threshold. Moody incorrectly assumes that to avoid triggering a "required refund," FY96 revenue must be reduced to the level of the revenue limit, when in reality it must merely fall below the refund threshold. Adjusting for that discrepancy by subtracting the amount of the 1 percent refund threshold lowers Moody's estimate of the necessary tax reduction by \$61.6 million.

4. Moody ignores one of his own assumptions. In calculating spending cut estimates, he makes the assumption that, in response to Hancock II, the legislature will repeal two taxes.[36] Those taxes were expected to bring in \$182 million in revenue in FY96. Since by Moody's own assumption, that \$182 million will never be collected, his estimate of FY96 revenue, and thus of the tax reduction necessary to comply with Hancock II, should have been reduced by the same amount.[37] (Note that since adjustment 2 above essentially employs a baseline of FY95 revenue rather than projected FY96 revenue, subtracting \$182 million from Table 7's adjusted tax reduction estimate would involve an element of double counting, thus it is listed separately.)

In sum, as Table 7 indicates, the total effect of adjusting for the three main flaws in Moody's analysis would lower his estimate of the tax reduction necessary to comply with Hancock II by \$889.5 million. Rather than \$1.024 billion, the necessary tax reduction would be only about one-eighth of that amount, or \$134.4 million.

Furthermore, even ignoring the first three flaws, under Moody's own assumptions, his \$1.024-billion estimate of the tax reduction necessary to comply with Hancock II is incorrect. The correct figure is \$841.9 million, nearly 20 percent lower than Moody claims.

Finally, Table 8 recalculates Moody's FY96 percentage spending cut estimate (from Table 6), correcting for the flaws described above. Assuming that 58.2 percent of the budget is protected from spending cuts (as Moody assumed for FY96),[38] and employing an FY95 baseline of \$6,355.1 in revenue (the Missouri budget office's projection used in the Moody report), the amount of unprotected spending in FY95 would be \$2,656.4 million. Using the corrected spending cut reduction figure of \$134.4 million from Table 7, the percentage cut in unprotected spending necessary to comply with Hancock II would be 5.06 percent, less than one-sixth of the 32.36 percent cut Moody claims is required.

To summarize, while Moody asserts that Hancock II would necessitate revenue refunds and spending cuts of over \$1

billion in FY96, in reality those cuts need be only \$134.4 million. That is a far cry from a \$1-billion cut. In addition, Moody's claim that a 32.36 percent reduction would have to be made in all areas of unprotected spending, including schools, colleges, prisons, and highways, is overstated by a factor of six. That reduction need be only about 5 percent.

Furthermore, reductions are only necessary because, despite the Hancock amendment's provisions, the Missouri legislature has refused to rein in the growth of the state budget. In fact, in FY95 alone, due in part to state senate bill 380--a \$310-million tax hike for education, passed, but not approved by the voters, in 1993--state revenue will rise 9.4 percent, more than double the 4.1 percent rise in Missourians' incomes.[39] Thus, over the past two years Missouri state revenue has gone up by over \$700 million. That amounts to a 12.2 percent tax increase, nearly double the U.S. average for that period.[40]

Conclusion

The Moody report claims that the passage of Hancock II will require a tax refund of \$1.024 billion, or \$194 for every resident of Missouri. Although that may sound very enticing to Missouri's taxpayers, those numbers are sheer fantasy. The huge tax refund and the corresponding deep spending cutbacks that Hancock II's opponents are predicting if the measure is passed are vastly overstated. Voting for Hancock II will not put a check for \$194 into the hands of each Missouri resident. Nor will it require the massive cuts in government services that its opponents are alleging. In reality, the actual reduction required by Hancock II would be, at most, 5 percent. That cut would be necessary only to compensate for the years of accumulated overspending outlined in this paper.

Despite the alarmist claims of its opponents, by linking state revenue growth to the growth of state personal income, all Hancock II would really do is require politicians to live under the same set of rules that Missouri's taxpayers have been struggling under. Hancock II would merely restrain the ability of politicians to raise taxes and the budget faster than the growth of state taxpayers' incomes. It would not require legislators to make drastic reductions in revenue and expenditures. In fact, it would not even prohibit them from raising taxes faster than personal income. If the state legislature wanted to pass a budget with a larger than allowed increase in revenue, Hancock II would not prevent them from taking that action. All Hancock II would require is that the legislature first obtain the permission of the people who must pay those higher taxes, the voters of Missouri. That seems a sensible response to 12 years of inflated state budgets and rapidly rising tax burdens in Missouri.

Table 1 Growth of Missouri State Spending Since Enactment of Hancock Amendment, 1982-1992						
	Real Increase	U.S. Rank	Real per Capita Increase	U.S. Rank	Increase Per \$1,000 Personal	U.S. Rank
Missouri	63%	15	54%	8	22%	11
Plains States Avg.*	40%		31%		13%	
U.S. Average	55%		38%		12%	

*"Plains States" refers to the Census Bureau's "West North Central" region which is made up of seven states: Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, and South Dakota.
Source: U.S. Census Bureau, State Government Finances, 1982 & 1992 editions.

Table 2 Growth of Missouri State Revenues* Since Enactment of Hancock	
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Amendment, 1982-92						
	Real Increase	U.S. Rank	Real per Capita Increase	U.S. Rank	Increase Per \$1,000 Personal	U.S. Rank
Missouri	65%	15	56%	3	24%	10
Plains States Avg.*	45%		31%		13%	
U.S. Average	51%		34%		10%	

*Total revenue minus intergovernmental revenue from the federal government.

***"Plains States" refers to the Census Bureau's "West North Central" region which is made up of seven states: Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, and South Dakota.

Table 3 The Effect of the Court's Redefinition of "Total State Revenue"						
	FY1982	FY1983	FY1984	FY1985	FY1986	FY1987
Actual Amount of Total State Revenue (TSR) Under Differing Definitions						
Missouri budget office's definition*	\$2,397	\$2,603	\$2,841	\$3,120	\$3,326	\$3,583
Hancock-I's intended definition**	\$2,397	\$2,710	\$3,157	\$3,461	\$3,688	\$3,968
Amount of revenue exempted from Hancock-I's intended definition.***	\$0	\$107	\$316	\$341	\$362	\$385
Percentage of State Own-Source Revenue Exempted from the Revenue Limit Under Differing Definitions of TSR						
Missouri budget office's definition*	2.1%	6.5%	15.5%	14.5%	15.9%	22.1%
Hancock-I's intended definition**	2.1%	2.7%	6.1%	5.2%	6.8%	13.7%

	FY1988	FY1989	FY1990	FY1991	FY1992	FY1993	1982-93 Increase
Actual Amount of Total State Revenue (TSR) Under Differing Definitions							
Missouri budget office's definition*	\$3,917	\$4,175	\$4,422	\$4,630	\$5,011	109.1%	109.1%
Hancock-I's intended definition**	\$4,445	\$4,726	\$4,993	\$5,201	\$5,531	\$5,620	134.4%
Amount of revenue exempted from	\$528	\$551	\$571	\$571	\$586	\$609	\$4,926

Hancock-I's intended definition.***							
Percentage of State Own-Source Revenue Exempted from the Revenue Limit Under Differing Definitions of TSR^							
Missouri budget office's definition*	18.7%	16.8%	17.3%	16.0%	17.1%	17.9%	
Hancock-I's intended definition**	7.7%	5.9%	6.6%	5.6%	7.2%	7.9%	

*Refers to TSR as defined by the Missouri budget office (Office of Administration, Division of Budget and Planning).

**Hancock I's intended definition differs from the budget office's definition only in that it includes the amount of revenue from Proposition C and Proposition A.

***Equals the amount of revenue from Proposition C and Proposition A.

^"State Own-Source Revenue" excludes only federal funds. Note: Unless otherwise indicated, all figures are in millions of current dollars (i.e., not adjusted for inflation).

Source: Office of the State Auditor of Missouri, annual Hancock reports, FY1982-1993. Figures for 1989-93 taken from 1993 report, 1988 from 1992, 1987 from 1991, 1986 from 1990, 1985 from 1989, 1984 from 1988, 1983 from 1987, and 1982 from 1986 report.

Table 4 Contrary to the Intent of the Hancock Amendment, Total State Revenues Have Outpaced Personal Income Growth							
	FY 1982	FY 1983	FY 1984	FY 1985	FY 1986	FY 1987	FY 1988
State Personal Income*	\$43,698	\$47,697	\$50,423	\$54,817	\$60,466	\$66,605	\$70,503
Annual Inceas		9.2%	5.7%	8.7%	10.3%	10.2%	5.9%
Total State Revenue under intended definition of Hancock I (TSRH)**	\$2,397	\$2,710	\$3,157	\$3,461	\$3,688	\$3,968	\$4,445
Annual Increase		13.1%	16.5%	9.6%	6.5%	7.6%	12.0%
Revenue Limit***	\$2,480	\$2,706	\$2,860	\$3,110	\$3,430	\$3,776	\$3,998
Annual Increase		9.1%	5.7%	8.7%	10.3%	10.1%	5.9%
Amount TSRH exceeded the limit		\$4	\$297	\$351	\$258	\$192	\$447
Percent TSRH exceeded the limit		0.2%	10.4%	11.3%	7.5%	5.1%	11.2%
TSRH as a share of personal income	5.49%	5.68%	6.26%	6.31%	6.10%	5.96%	6.30%

	FY 1989	FY 1990	FY 1991	FY 1992	FY 1993	FY 1994
State Personal Income*	\$74,825	\$79,458	\$84,864	\$89,611	\$92,733	
Annual Inceas	6.1%	6.2%	6.8%	5.6%	3.5%	112.2%
Total State Revenue under intended definition of Hancock I (TSRH)**	\$4,726	\$4,993	\$5,201	\$5,531	\$5,620	
Annual Increase	6.3%	5.6%	4.2%	6.3%	1.6%	134.4%
Revenue Limit***	\$4,242	\$4,507	\$4,814	\$5,082	\$5,258	
Annual Increase	6.1%	6.2%	6.8%	5.6%	3.5%	112.0%
Amount TSRH exceeded the limit	\$484	\$486	\$387	\$449	\$362	\$3,716
Percent TSRH exceeded the limit	11.4%	10.8%	8.0%	8.8%	6.9%	
TSRH as a share of personal income	6.32%	6.28%	6.13%	6.17%	6.06%	

*As stipulated by Hancock I, the personal income figures used for FY 1982 are from calendar year 1980, for FY 1983: from CY 1981, etc. This is done because fiscal years end before calendar years.

**Hancock I's intended definition differs from the budget office's definition only in that it includes the amount of revenue from Proposition C and Proposition A.

***As defined by the Missouri budget office (Office of Administration, Division of Budget and Planning).

Note: Unless otherwise indicated, all figures are in millions of current dollars (i.e., not adjusted for inflation).

Source: Office of the State Auditor of Missouri, annual Hancock reports, FY1982-1993. Figures for 1989-93 taken from 1993 report, 1988 from 1992, 1987 from 1991, 1986 from 1990, 1985 from 1989, 1984 from 1988, 1983 from 1987, and 1982 from 1986 report.

Table 5 Moody Report's Estimate of "Tax Reduction" Necessary to Comply with Hancock II					
				Annual Growth	
	FY 1994	FY 1995	FY 1996	1994- 95	1995-96
State Personal Income*	\$98,963	\$102,995	\$108,668	4.1%	5.5%
Total State Revenue**	\$5,170.1	\$5,657.2	\$5,946.0	9.4%	5.1%
New revenues included by H- II**		\$697.9	\$720.3		
TSR plus new revenues**		\$6,355.1	\$6,666.3		+\$311.2
Revenue Limit**	\$5,610.3	\$5,838.4	\$6,159.1	4.1%	5.5%
Amount TSR would exceed the limit**		\$516.7	\$507.2		
Tax reduction necessary to comply with Hancock II***			\$1,023.9		

*As stipulated by Hancock I, the personal income figures used for FY 1994 are from calendar year 1992, for FY 1995: from CY 1993, etc. This is done because fiscal years end before calendar years. Figures are official U.S. Department of Commerce projections used by Missouri budget office and in the Moody Report.

**Figures are Missouri budget office projections of total state revenue subject to Hancock II used in the Moody Report.

***This figure is merely the sum of the excess revenues from FY 1995 and FY 1996. Moody assumes that this amount would have to be refunded to the taxpayer in FY 1996.

Note: This is an adaptation of Table 3 of the Moody Report. The Moody Report uses the term "required refund" for the amount which revenue is projected to exceed the limit. However, a refund would be required only if the legislature votes to collect that excess revenue, in violation of Hancock II. All figures are in millions of current dollars (i.e., not adjusted for inflation).

Source: Moody Report, Table 3, p. 7.

Table 6 Moody Report's Estimate of "Spending Cuts" Necessary to Comply with Hancock II	
	FY 1996
Total state revenue subject to Hancock II*	\$6,666.3
Spending cut necessary to comply with Hancock II**	\$1,023.9
Projected FY 1996 revenue from taxes Moody assumes would be repealed***	\$182.0
Total state revenue subject to Hancock II (adjuste)^	\$6,484.3
Spending cut necessary to comply with Hancock II (adjusted)^	\$841.9
Moody's estimate of "protected expenditures" ^^	\$3,882.7
Amount of FY 1996 "unprotected spending"+	\$2,601.6
Spending cut as a % of "unprotected spending"++	32.36%

*Missouri budget office projection used in the Moody Report and in Table 5 of this report.

**Same as "tax reduction" figure from Table 5 of this report.

***In calculating his spending reduction estimates, Moody assumes that certain taxes will be repealed. The expected revenue from those taxes must be subtracted from both "total state revenue subject to Hancock II" and "spending cut necessary to comply with Hancock II." According to the Missouri budget office projections used in Moody's report, those taxes would have brought in \$182 million in FY 1996. (Moody Report, pp. 14-15.)

^These figures exclude the \$182 million in FY96 revenue that Moody assumes will not be collected.

^^This figure refers to spending on "a reasonable estimate of programs which are protected by federal law, the Missouri Constitution, federal courts, or Missouri state law or courts." (Moody Report, p. ii, and Table 4, pp. 13-14.)

+This figure is merely "total state revenue subject to Hancock II" minus "protected expenditures."

++Note that this corresponds with Moody's estimate of the required cut in non- exempted areas of spending. (Moody Report, p. 15.)

Note: All figures are in millions of current dollars (i.e., not adjusted for inflation).

Source: Moody Report, Tables 4 and 5, pp. 13-15.

Table 7 Adjustments to Moody's Estimate of the Tax Reduction Necessary to Comply with Hancock II		
	Amount of Adjustment FY 1996	FY 1996 Tax Reduction
Moody's estimate of the tax reduction necessary to comply with Hancock II		-\$1,023.9
Adjustments:		
1) Hancock II does not apply to FY95	\$516.7	
2) Projected FY 1995-96 revenue growth*	\$311.2	
3) Amount of 1% refund threshold in FY 1996**	\$61.6	

Total Adjustments	\$889.5	
Corrected estimate of the tax reduction necessary to comply with Hancock II		-\$134.4
Moody's estimate of the tax reduction necessary to comply with Hancock II		-\$1,023.9
4) Uncollected revenue from Moody's assumed tax repeals [^]	\$182.0	
Moody's estimate of the tax reduction necessary to comply with Hancock II, under his assumption of tax repeals		-\$841.9

*Moody's FY 1996 "required reduction" is a reduction from the projected level of FY 1996 revenue, rather than from the FY 1995 level. Since part of that "reduction" represents the elimination of projected 1995-96 growth, it does not measure the actual reduction from the prior year's level of revenue. The number listed here represents the projected growth in "TSR plus new revenues" from FY 1995 to 1996, used in the Moody Report. Subtracting that growth from Moody's reduction makes it an actual reduction. See Table 5 of this report.

**Hancock II (and Hancock I) allows revenue to exceed the limit by up to 1% without requiring a refund. The number listed is simply the amount of that 1% refund threshold by which FY 1996 revenue could exceed the limit without requiring a refund.

[^]In calculating his spending reduction estimates, Moody assumes that certain taxes will be repealed, however his "required refund" estimate of \$1,023.9 billion does not exclude that revenue. According to the Missouri budget office projections used in this report, those taxes would have brought in \$182 million in FY 1996. Note that since adjustment #2 above essentially employs a FY 1995 baseline (rather than Moody's baseline of expected FY96 revenue), subtracting this \$182 million, together with that adjustment, from his estimated tax reduction would involve an element of double-counting, thus it is listed separately. (Moody Report, pp. 14-15.)

Note: All figures are in millions of current dollars (i.e., not for inflation).

Table 8 How Moody's Flawed Tax Reduction Estimate Affected His Spending Cut Estimate	
	FY1995
Moody's estimate of the percentage cut in FY96 spending necessary to comply with Hancock II*	32.36%
Revised Estimate of Spending Cut	
TSR plus new revenues, FY 1995**	\$6,355.1
Total "protected expenditures," FY 1995***	\$3,698.7
Amount of FY 1995 "unprotected spending" [^]	\$2,656.4
Spending cut necessary to comply with Hancock II ^{^^}	\$134.4
Spending cut as a % of "unprotected spending"	5.06%

Notes

[1] For a fuller discussion, see Dean Stansel, "Taming Leviathan: Are Tax and Spending Limits the Answer?" Cato Institute Policy Analysis no. 213, July 25, 1994.

[2] Those 15 states are Arizona, California, Colorado, Delaware, Hawaii, Idaho, Louisiana, Michigan, Missouri, Oregon, South Carolina, Tennessee, Texas, Utah, and Washington.

[3] Stansel, p. 26.

[4] Note that, as stipulated by the Hancock amendment, the relevant personal income amount for the base year calculation was total personal income for calendar year 1979. Missouri State Constitution, article X, section 18(a).

[5] In future years, the relevant amount is for "the calendar year prior to the calendar year in which appropriations for the fiscal year for which the calculation is being made [are made], or the average of personal income of Missouri in the previous three calendar years, whichever is greater." Ibid.

[6] Missouri State Constitution, article X, section 17(1).

[7] The official name of the Missouri budget office is the Division of Budget and Planning of the Office of Administration.

[8] James Antonio, "Review of the Hancock Amendment Two Years Ended June 30, 1982," Offices of the State Auditor of Missouri, Jefferson City, Report No. 83-35, March 16, 1983, p. 5.

[9] Proposition C did not require that local property tax cuts be made. Further, the state legislature subsequently reduced the amount of non earmarked school funding.

[10] *Goode v. Bond*, 652 S.W.2d 98 (Mo. banc 1983).

[11] There is little disagreement that revenue that comes from a tax hike pursuant to a constitutional amendment, which specifically provides that said revenue be excluded from the limit, should indeed be excluded.

[12] Missouri budget office estimates used in James Moody, "The Impact of the Proposed Hancock II Amendment: Fiscal and Policy Implications for Missouri State Government," Committee to Protect Missouri's Future, Jefferson City, April 1994, Table 2, p. 5. Cited hereafter as Moody report.

[13] See, for example, Thomas Wyrick, "The Hancock Amendment and Economic Growth in Missouri," Heartland Institute Policy Study no. 49, June 25, 1992.

[14] U.S. Department of Commerce, Bureau of the Census, *State Government Finances*, various editions.

[15] Ibid.

[16] Own-source revenue excludes intergovernmental revenue from the federal government (as defined by the Census Bureau).

[17] Own-source revenues exclude federal funds.

[18] Hancock I's intended definition differs from the budget office's definition only in that it includes the amount of revenue from Propositions C and A, voter-approved statutory tax hikes.

[19] Ibid.

[20] Ibid.

[21] Calculated from Missouri budget office figures used in the Moody report, Table 3, p. 7.

[22] In FY85, according to the state budget office, the revenue limit was exceeded by 0.3 percent. However, since that excess was less than 1 percent, no refund was required.

[23] Because they limit the growth of the state budget to the growth rate of population plus inflation, rather than to the growth rate of personal income--as Hancock II and many other TELs do--these two measures are actually somewhat stricter than Hancock II.

[24] For a recent discussion of this issue, see Stephen Moore and Dean Stansel, "The Great Tax Revolt of 1994," *Reason*, October 1994, pp. 20-25.

[25] Note that the Democrat-controlled Legislative Oversight Committee, which produces the fiscal note for ballot

initia tives and determines precisely how the initiative will appear on the ballot (i.e., decides what the specific language will be), has estimated that the required cut will be between \$1 billion and \$5 billion. Those estimates include federal funds as part of total state revenue.

[26] Moody report, p. 16.

[27] Ibid., p. ii.

[28] Ibid., p. 17.

[29] Ibid., p. 16.

[30] Ibid., p. 17.

[31] Moody report, p. 9.

[32] Those two taxes are the local use tax and a gas tax hike that was scheduled to take effect in April 1996. According to the Missouri budget office projections used in the Moody report, those two taxes were expected to have brought in \$182 million in FY96. Moody report, pp. 14-15.

[33] This figure is Moody's estimate of spending on "programs which are protected by federal law, the Missouri Constitution, federal courts, or Missouri state law or courts." Moody report, p. ii, and Table 4, pp. 13-14.

[34] Text of proposed Hancock II amendment, article X, section 18(a).

[35] Text of proposed Hancock II amendment, article X, section 18(b).

[36] Moody report, pp. 14-15.

[37] Moody's assumption clearly would lower the "reduction required to comply with Hancock II" by \$182 million (from \$1,023.9 million to \$841.9 million). However, the number used throughout the Moody report is \$1.024 billion, in direct contradiction of Moody's tax repeal assumption, which lowers the necessary reduction to \$841.9 million.

[38] For the purposes of this paper, that assumption will be left unchallenged.

[39] Calculated from Missouri budget office figures used in Moody report, Table 3, p. 7.

[40] The U.S. average was 6.7 percent. Calculated from National Association of State Budget Officers, Fiscal Survey of the States, April 1994 edition, Tables A1, A3, pp. 22, 26.