Lack of Spending Restraint Illustrates Need for New Mexico Taxpayer Protections

Richardson's Spending Record Exacerbates Historical Trend

By: Paul J. Gessing and Harry Messenheimer, Ph.D.
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New Mexico Governor Bill Richardson has built a reputation as a fiscal moderate because of reductions in the rates on taxes on personal income and capital gains that he proposed and that were passed early in his term. While those tax cuts are to be applauded and their economic impact has been positive, Richardson's reputation for fiscal conservatism is overblown. In fact, New Mexico's Governor has been on a spending spree throughout his term and the positive economic impact of his tax cuts has been largely offset by tax and fee increases elsewhere.

While the recent spending binge is not unique; in fact, rapid growth in government has been the rule and not the exception in New Mexico. With the exception of the eight years of the Johnson Administration (FY 1995-FY 2003), New Mexico's political leaders have failed to create the conditions necessary to allow entrepreneurs to generate economic growth.

How Fast Should Government Grow?

In the absence of specific additional needs, government spending should grow at a rate that closely tracks the combined effects of inflation and population growth.[1] This is considered the "natural" rate of growth because it accounts for additional demands for services and keeps up with prices, without resulting in a government that is bigger in real terms than before. In reality, even if a strict inflation and population growth limit were placed on New Mexico government, the state would have plenty of resources to spend:

- Plenty of waste and "fat" now exists in government spending figures. Constraining government growth would be a powerful tool in eliminating waste and would allow government to take on new tasks without requiring additional revenues;
- Expanding government at the rate of population growth allows government to take advantage of efficiencies of scale.[2] Since it costs proportionately less to allow one more person or family to use a road or sewer system, governments, were they to act like private businesses, should be able to do even more with each additional tax dollar than it could previously;
- Governments can/should benefit from the decreasing costs associated with new technologies. Just as we now get more computer processing power, a better television, and better gas mileage than we did in the past, government benefits from technological advancement.

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[1] Barry Poulson, PhD, "The Next Generation of Tax and Expenditure Limits," Americans for Prosperity Foundation, May 12, 2004, http://64.203.102.204/news/spend_0040512b.html.
[2] Wikipedia, "Returns to Scale," http://en.wikipedia.org/wiki/Economies_of_scale.

Of course, as most citizens and taxpayers will readily acknowledge, government does not operate as efficiently as a private business. Government officials are not competing in a free marketplace and instead of serving customers, they are more often concerned with serving special interests that will fund them and lend them support at the ballot box. This dynamic creates powerful incentives for government growth and inefficiency. Absent strict limits on spending and taxes, government will grow rapidly, crowding out economic growth in other sectors of the economy.

Pattern of Failure

New Mexicans are the first to admit that their state relies on government at all levels to a greater extent than most other states. At the federal level, New Mexico receives $2 for every $1 its taxpayers send to Washington, a level of largesse greater than any other state.[3] New Mexicans have little control over and little reason to stop much of the defense spending or research done by the energy department that takes place in the state, but federal ownership of 42 percent of the land in New Mexico[4] and transfer payments in the form of Medicare, Medicaid, and Social Security tend to create a culture of dependency.

Our control over federal activities taking place within New Mexico's borders is of course limited, but we do have control over state and local governments. Unfortunately, here again, New Mexico is among the most prolific in supporting big-government. In fact, according to data from the U.S. Census Bureau, state and local governments in New Mexico employ more workers as a percentage of total population than all but two other states (Alaska and Wyoming).[5]

Unfortunately, reliance on government handouts and the creation of a bloated state bureaucracy are proven failures when it comes to raising the living standards of average New Mexicans. When it comes to per-capita personal income – a number that strongly correlates with living standards – New Mexico ranks an abysmal 46th in the nation.[6]

A History of Big Government

As the chart below illustrates, New Mexico state spending has been growing faster than the natural rate for some time. In fact, since FY 1989 the gap between New Mexico's actual General Fund spending and the natural rate of spending growth has grown to $1.5 ***billion***.

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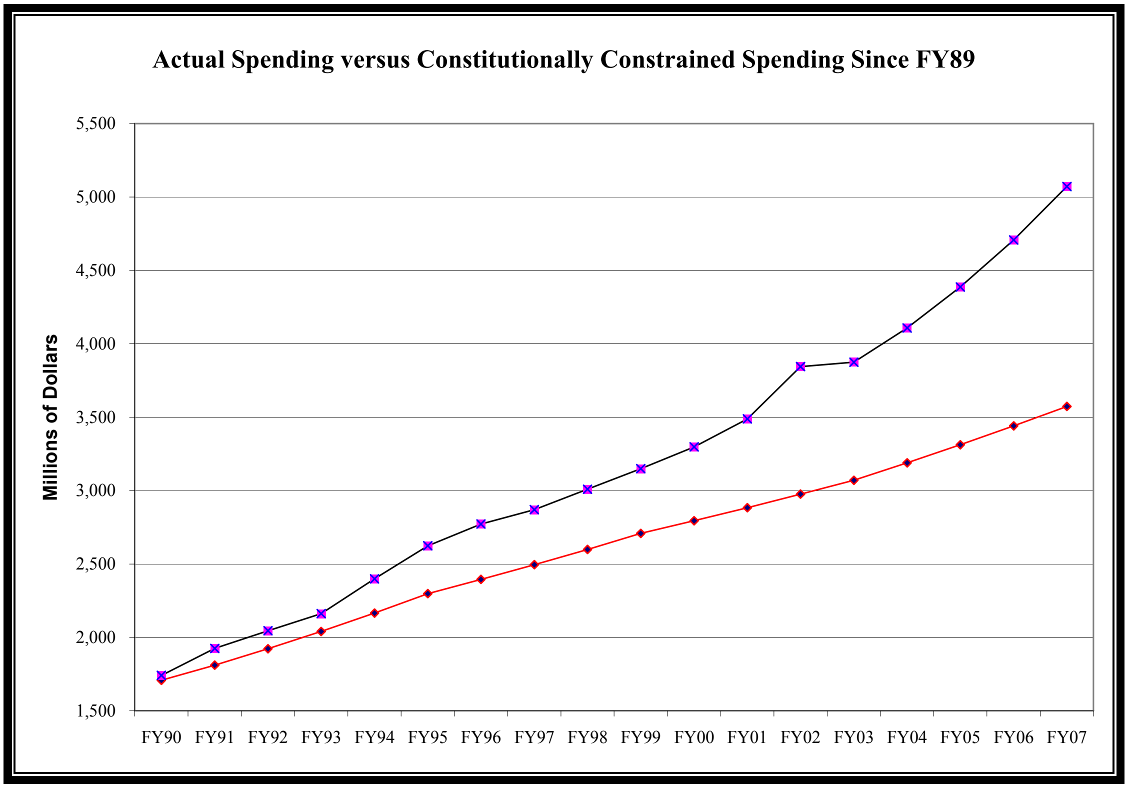
[3] Curtis Dubay, "Federal Tax Burdens and Expenditures by State," The Tax Foundation, March 2006, http://www.taxfoundation.org/files/sr139.pdf.
[4] Representative Mike Pence, "Federal Land and Building Ownership," The Republican Study Committee, May 19, 2005, http://www.house.gov/pence/rsc/doc/Federal_Land_Ownership_05012005.pdf.
[5] U.S. Census Bureau, "2005 Public Employment Data State and Local Governments," Information found in individual state summary tables, http://www.census.gov/govs/www/apesstl05view.html.
[6] Bureau of Business & Economic Research, UNM, "Per Capita Income By State," http://www.unm.edu/~bber/econ/us-pci.htm.

Figure 1.

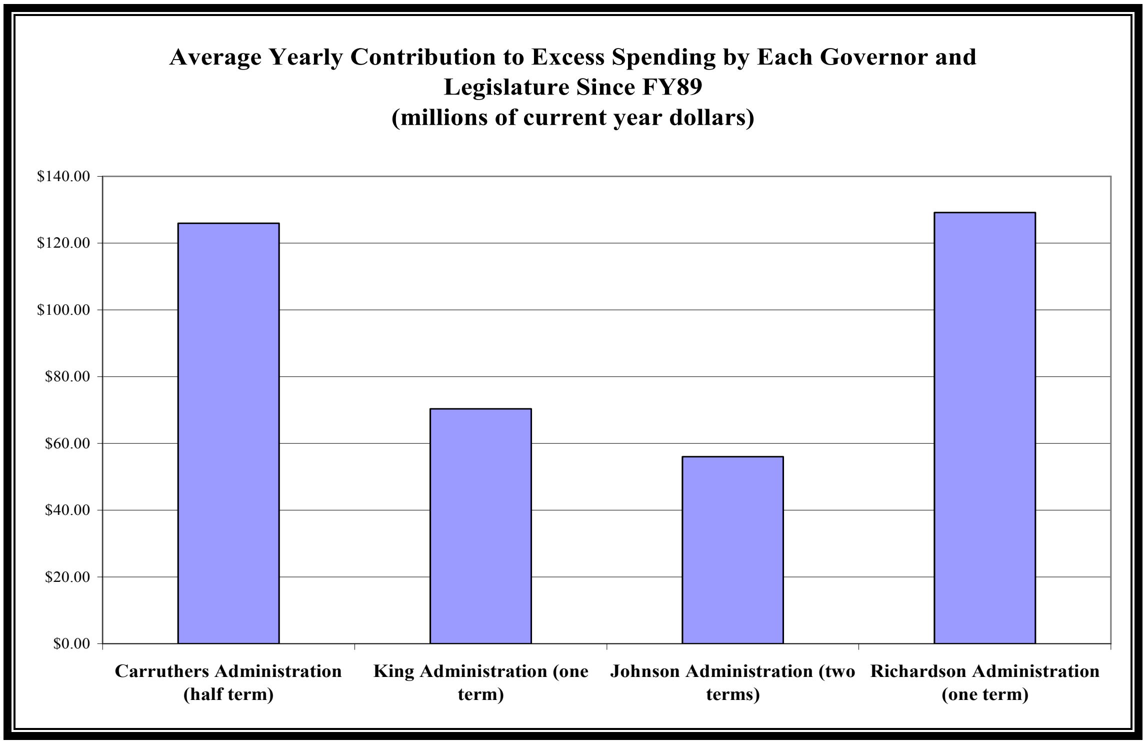


While it would be easy to make spending restraint (or the lack thereof) a partisan issue, that is not really the case. Personal dedication to spending restraint and economic/political considerations often factor into the equation. As figure 2 illustrates, Gary Johnson, a Republican and New Mexico's Governor from 1995-2003, was the most fiscally-responsible of the state's last four governors, but Democrat Bruce King (1991-1995) was far more frugal than either Republican Garrey Carruthers (1987-1991)or current Democratic Governor Bill Richardson (2003-present)[7].

Figure 2 illustrates the spending ***in excess of*** the natural rate of growth (population and inflation) by each of New Mexico's last four governors as adjusted to 2007 dollars. When examining these charts, it is important to ask what benefit the citizens of New Mexico derived from all of this spending. After all, our educational system is consistently ranked poorly and we are not as wealthy as our neighbors. Much of this excess spending has been wasted or used so inefficiently as to have a net negative impact on our state.

[7] Calculations of inflation and population growth were for each term of the relevant governor. Since we were unable to obtain spending data before FY89, calculations were made for one-half of Gov. Carruthers's term. Data sources are Bureau of Labor Statistics for inflation and Bureau of Economic Analysis for population. Our data and calculations are available on request.

Figure 2.



The Johnson Record

Spending under Governor Johnson was effectively restrained to allow the government to grow just a bit faster than inflation and population rates combined each year. By way of comparison with Governor Richardson, spending has increased during the last four years by more than it did for Gary Johnson's entire two terms ($516.62 million versus $448.00 million).

Unfortunately, while Johnson kept spending growth at reasonable levels, needed reforms in education, health care, and in state budget processes were stymied by the Legislature.[8] Johnson's tax cuts were also denied repeatedly by the Legislature. So, while spending growth was restrained, New Mexico's government remained systemically-flawed and its tax and budgeting systems escaped reform. Clearly, strong leadership from the Executive Branch is not enough to generate long-term spending restraint since time is on the side of special interests and those who would delay needed reforms.

The Richardson Record

Governor Richardson's aforementioned tax cuts were good first steps towards making New Mexico more prosperous. Far more needs to be done for the state's economy, however, and by not controlling spending during the current economic recovery, Richardson missed an

[8] Joseph Giordono, "Early Legislation Focus on Taxes, Education, Cooperation," *Stateline,* March 29, 1999, http://www.stateline.org/live/ViewPage.action?siteNodeId=136&languageId=1&contentId=13645.

opportunity to really move New Mexico in the same economic direction as its prosperous (and economically freer) neighbors in Texas, Arizona, and Colorado.

Using general fund budget data from the Legislative Finance Committee, we found that New Mexico's General Fund spending has increased by nearly 12.2 percent in real terms under Bill Richardson (adjusting for the effects of inflation and population growth). That amounts to well over one-half **billion** dollars. The major contributors to that budget busting number are summarized in Table 1 below.

Table 1.

Richardson's First Term Budget Busters		
	Real Growth (percent)	Real Growth (Millions of Dollars)
Medicaid	36.25%	$ 168.80
Public Education	8.72%	$ 190.19
Higher Education	8.10%	$ 58.94
Health & Welfare	4.82%	$ 100.07

Source: Legislative Finance Committee and authors' calculations

The major driver of spending growth is Medicaid. In fact, under Richardson, Medicaid has grown by over 36 percent in real terms. Medicaid's growth is significantly greater than the overall growth of the General Fund as a whole (a little over 12 percent.

Medicaid's problems are driven by the fact that it is essentially free to recipients and that the federal government encourages increased spending with a matching rate as high as 3-to-1. While some states are working to fix the problems they have control over by giving recipients incentives to engage in preventative care and use money wisely, Governor Richardson has instead proposed a massive expansion of the program that will only continue this trend.[9]

A massive expansion of Medicaid, absent needed reform, is symbolic of the economic model New Mexico politicians have followed for far too long. While it may be politically popular to use federal matching funds and other programs to fleece federal taxpayers, such efforts ultimately hinder our own economic progress by growing New Mexico's government while putting more citizens on the dole.

Although this study is designed to focus attention on New Mexico's General Fund spending, the state will actually spend more than $12 billion during FY 2007.[10] Aside from Medicaid, which needs to be completely reformed, there are dozens of "corporate welfare" programs and other costly initiatives on which taxpayer money have been squandered over the years. These projects may sound nice in concept, but they inevitably wind up costing taxpayers hundreds of millions of dollars and preventing essential reforms.

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[9] Diana Heil, "State Panel to Study Universal Health Care," *The Santa Fe New Mexican,* July 21, 2006, http://www.freenewmexican.com/news/46755.html.

[10] "Addendum to LFC 2006 Post-Session Review," Legislative Finance Committee, April 17, 2006, http://legis.state.nm.us/LCS/lfc/lfcdocs/2006Addendum.pdf.

The $318 million cost of the Rail Runner commuter rail project for which taxpayers are providing a 9-to-1 match for each dollar collected in fares, is a waste no matter how many passengers ride the rails.[11] When an individual is paying only one-tenth of the true cost of a particular good such as the Rail Runner, it is almost free. The Mid-Region Council of Governments, in keeping with this concept, have made the Rail Runner "free" for passengers for the first six months of operation and occasionally run it as a free tourist ferry for events such as the New Mexico Wine Festival and the Balloon Fiesta.

The $100 million taxpayers will spend to subsidize millionaire astronaut wannabes taking off from the spaceport is another feature of the rapid growth of New Mexico government under Richardson. Like nearly all government spending programs it is assumed that the Spaceport will pay off in future "economic development," but New Mexico is not alone in hoping to reap the benefits of space tourism dollars. In fact, at least six other commercial spaceports are either planned or have already been opened in the United States.[12] Foreign countries like Australia and Russia are also hoping to get a piece of the space tourism business. While being on the "cutting-edge" of new industries may be nice in concept, New Mexico's undeveloped land and weather would have likely drawn the space industry to the state without subsidies.

The fact is that strong oil and gas revenues have enabled New Mexico's economy to grow fast enough to keep up with rapid spending growth over the past four years. In fact, on a per-person basis, since 2003 severance taxes have grown from $257.44 to $369.57, an increase of 44 percent.[13] Severance tax collections are extremely volatile and with prices on the way down, New Mexico's budgetary stability could be in trouble. This reliance on an unstable revenue source means that New Mexico's government is currently growing at an unsustainable pace.

Colorado's Model

In 1992, by citizen initiative, Colorado's voters approved of a plan known as the Taxpayers' Bill of Rights that amended the state's Constitution to provide citizens greater control over exactly how much of their money state and local governments are allowed to spend.

As Table 2 below shows, since adopting the Taxpayers' Bill of Rights in 1992, Coloradoans have seen their personal incomes grow enough relative to other states to rise from 17th place to 8th. New Mexicans, on the other hand, have been running in place. We were stuck at 46th in the nation in 1992 and we are now stuck in 46th place (we would be 47th had it not been for Hurricane Katrina having dropped Louisiana from 42nd to 50th and behind us).[14]

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[11] Jeff Jones, "Train Will Lose Millions, Rail Runner Fares May Cover 10 percent of Cost," *Albuquerque Journal,* http://www.wheelsmuseum.org/012406.html.
[12] Alan Boyle, Spaceports Compete in Race for Business," MSNBC, October 7, 2004, http://www.msnbc.msn.com/id/6191567/.
[13] Calculations were made by Harry Messenheimer using data from the Bureau of Economic Analysis.
[14] Excel spreadsheets containing detailed historical data are available at: Bureau of Business & Economic Research, UNM, "Per Capita Income By State," http://www.unm.edu/~bber/econ/us-pci.htm.

Table 2.

2005 Rank	1992 Rank	State	2005 Rank	1992 Rank	State
1	1	Connecticut	27	31	Texas
2	4	Massachusetts	28	33	Iowa
3	2	New Jersey	29	27	Oregon
4	5	Maryland	30	24	Missouri
5	3	New York	31	36	South Dakota
6	12	New Hampshire	32	38	North Dakota
7	13	Virginia	33	30	Indiana
8	**17**	**Colorado**	34	35	Maine
9	15	Minnesota	35	28	Georgia
10	8	Delaware	36	34	Tennessee
11	10	California	37	32	North Carolina
12	26	Wyoming	38	37	Arizona
13	18	Rhode Island	39	44	Montana
14	9	Illinois	40	39	Oklahoma
15	11	Nevada	41	40	Alabama
16	7	Alaska	42	41	Kentucky
17	14	Washington	43	43	South Carolina
18	16	Pennsylvania	44	42	Idaho
19	6	Hawaii	45	48	Utah
20	24	Nebraska	**46**	**46**	**New Mexico**
21	23	Wisconsin	47	49	West Virginia
22	29	Vermont	48	47	Arkansas
23	19	Florida	49	50	Mississippi
24	20	Michigan	50	45	Louisiana
25	22	Kansas			

How can we emulate Colorado's success? Colorado limits the growth of spending at both the state and local level to account for the natural rate of spending growth (the combined effects of inflation and population). If politicians want to spend more, they have to get permission in the form of a "yes" vote in a major election from a majority of the electorate. In addition, voters are given the opportunity to vote on any and all tax hikes.

Revenues above-and-beyond the limits proscribed by the Taxpayers' Bill of Rights are refunded to voters – between 1997 and 2002, Colorado had issued annual tax rebates that have totaled more than $3.2 billion.[15] Putting money back into the voluntary (non-governmental) economy is the best single way to create economic growth and should be considered the major reason for Colorado's stellar performance since 1992.

[15] Michael New, "Fiscal Trail Blazer," *National Review Online,* November 4, 2002, http://www.nationalreview.com/nrof_comment/comment-new110402.asp.

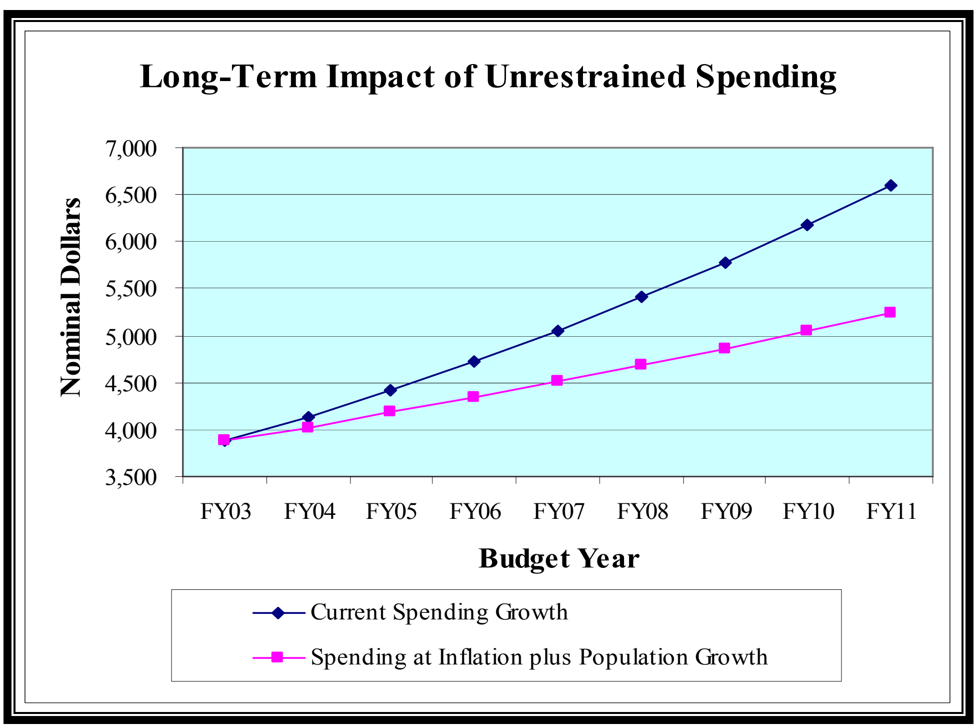
Applying Colorado's Model in New Mexico

Inflation and population growth are the measuring stick of government growth. Using these measurements in Colorado has enabled the state to avoid the boom-and-bust cycles of so many other states while strictly limiting government growth. This is not to say that government cannot grow under Colorado's system. In fact, in 2005, Colorado voters approved Referendum C by a narrow margin and thus allowed the state to hold onto all revenues over the next five years, a figure estimated to be more than $3 billion.[16]

Unfortunately, while Colorado voters have the right to vote whenever politicians want to raise taxes or grow government, New Mexicans have none of these rights. The growth of government under Governor Richardson is a perfect example of the natural tendency of government to grow over time without any real citizen input. As Figure 5 below illustrates, spending during Governor Richardson's first four budgets has grown significantly faster than it would had it been limited to inflation and population growth.

By FY 2007, had the limits imposed under Colorado law been imposed here in New Mexico, nearly **$550 Million** would have been returned to taxpayers out of the General Fund alone in just four years. If spending under Richardson's second term follows the same trend as it did during his first, New Mexicans will spend more than **$1.3 billion** more than necessary on government by FY 2011.

Figure 3.



[16] Alison Acosta Fraser, "*Colorado's Taxpayers' Bill of Rights Should Not Be Breached,*" The Heritage Foundation, July 28, 2005, http://www.heritage.org/Research/Taxes/bg1873.cfm.

The success of Colorado's model is clear and so are the problems associated with allowing the political process to allow the size of government to grow unfettered. Despite the controversy surrounding Referendum C and whether or not taxpayers would allow the government to hold on to more of their money, the fact is that Colorado taxpayers still support spending limits and efforts to build on Colorado's success are moving forward nationwide. In fact, voters in Maine, Montana, Nebraska, and Oregon will decide on similar spending limits this November.[17]

Conclusion: Economic Freedom = Prosperity

While the high oil and gas prices of the last few years have meant good budgetary times for the state, an economic downturn or a rapid decline in the price of oil and gas could soon result in economic hardship and the need for government layoffs, additional tax hikes, or both. None of these options is particularly palatable. New Mexico's politicians should break out of the tax-and-spend mindset and restrain government to build the state economy without relying as much on cyclical oil and gas prices or federal largesse.

Even if, as some analysts have predicted[18], we are in the midst of a sustained rise in oil and gas prices, the increase in severance tax revenues is unlikely to have the same widespread wealth impact as genuine spending restraint. Internationally, oil-rich nations as diverse as Venezuela, Saudi Arabia, and Nigeria have struggled economically, while economically-free nations such as Hong Kong, the United States, and New Zealand have been highly successful.[19]

Unfortunately, when compared to other states in this country, New Mexico more closely resembles Cuba or Venezuela than it does New Zealand or Hong Kong. This point becomes clear when analyzing data contained in the Study of Economic Freedom in North America compiled by the National Center for Policy Analysis and the Fraser Institute of Canada. According to this study, New Mexico lags behind every state in the union but West Virginia in providing the economic freedom necessary for its citizens to generate economic growth.[20]

In the final analysis, there is no inherent reason for New Mexico to be poor. After all, it is not natural resources, but the ingenuity of the people that create wealth. By limiting what government takes relative to what it leaves in the private sector, following Colorado's lead in adopting strict limits on the growth of state and local government will make all New Mexicans better off.

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[17] Kristina Rasmussen and Sterling Whitehead, "One Solution, Many Formulas: How States are Solving the Tax and Spending Problem," National Taxpayers Union, September 18, 2006, http://www.ntu.org/pdf/pp_ntu_122.pdf.
[18] The Associated Press, "PNM to Seek Higher Natural Gas, Electricity Rates," *Santa Fe New Mexican,* May 17, 2006, http://www.freenewmexican.com/news/43767.html.
[19] The Heritage Foundation, "2006 Index of Economic Freedom," http://www.heritage.org/research/features/index/countries.cfm.
[20] Amela Karabegović and Fred McMahon, "Economic Freedom of North America 2006 Annual Report," The National Center for Policy Analysis and the Fraser Institute, http://www.ncpa.org/pub/special/pdf/EFNA2006.pdf.