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FEDERAL FUNDS AREN'T "FREE": HOW FEDERAL SPENDING IN NEW MEXICO GROWS STATE GOVERNMENT

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For decades, New Mexico's elected officials have worked to "bring home the bacon" from Washington, DC. By and large, they have succeeded in this regard. According to recent data from Key Policy Data, New Mexico receives \$1.69 from Uncle Sam for every dollar it sends to Washington. As seen in the chart below, only Kentucky and Mississippi exceeded New Mexico during FY 2013 when it comes to federal largesse.

FEDERAL TAX AND SPENDING RATIOS BY STATE, FISCAL YEAR 2013



Over the decades, New Mexico has consistently received more from Washington than it has sent to the federal government. This pattern has continued to the present day and has transcended ideology. Senators Domenici and Bingaman (a Republican and a Democrat) were consistently seen as "bringing home the bacon" by national watchdog groups like the Citizens Against Government Waste when they were in office. ¹

Gov. Martinez, despite being a conservative Republican, accepted the federal Medicaid expansion provided for under the "ObamaCare" health law. This law provided states a 100% match through 2016 with that match moving to 95% in 2017 and to 90% in 2020.

Already, New Mexico policymakers are facing difficult questions about how to pay for half of a year of paying for 5 percent of the Medicaid expansion. According to recent news reports, the state needs to come up with an additional \$85.2 million, or 8.5 percent increase in Medicaid spending to keep up with skyrocketing enrollment. ²

¹ Jason Trenkle, "Domenici-Bingaman Nets State High 'Pork' Rating, Albuquerque Business First, April 23, 2006, <http://www.bizjournals.com/albuquerque/stories/2006/04/24/story3.html>.

² Dan Boyd, "State Medicaid Costs Called 'Runaway Train,'" Albuquerque Journal, October 28, 2015, <http://www.abqjournal.com/666735/news/state-medicaid-costs-a-runaway-train.html>.

Another attempt to leverage federal tax dollars has been undertaken by the supposedly conservative Republican Mayor of Albuquerque, RJ Berry. Berry's Administration has applied to the Federal Transit Administration for an \$80 million "small starts" grant to pay for a new bus rapid transit system down his City's Central Avenue.³

Construction of the bus rapid transit system is likely contingent on the \$80 million grant, but all cost overruns will be paid for by local taxpayers and the expected millions of dollars in additional operating costs will come out of the pocketbooks of local taxpayers as well. The tendency for federal grants to further increase spending by state and local governments is an inherent problem with Washington largesse. There are "strings" attached.

STRINGS ATTACHED

And, according to a [new statistical analysis by economist Eric Fruits, PhD](#), an adjunct scholar with the Rio Grande Foundation, those strings can be more significant than previously understood. When controlling for the economic and demographic factors that vary across states and over time indicates that—holding other variables constant—each additional dollar of federal intergovernmental transfers to New Mexico is associated with \$0.99 in additional taxes, charges, and other state and local own source revenue.

This new research further finds that New Mexico experiences a larger ratchet effect than states as a group. In 2012, New Mexico state and local governments received \$5.9 billion in federal intergovernmental transfers and spent \$13.1 billion raised from state and local sources. A hypothetical 10 percent increase in federal transfers to New Mexico would amount to about \$590 million more federal money to the state. The statistical analysis indicates that this would be associated with approximately \$590 million more in spending from state and local own sources, or an additional \$280 per person in taxes and charges.

A vast literature has examined the impact of federal grants on state and local spending. Recent academic peer-reviewed research finds a "ratchet" effect in which federal transfers to the states are associated with increased state and local taxes and charges.

Research points to several reasons why additional federal funding would lead to greater state and local own-source spending:

- A "flypaper" effect, in which federal funds are accepted as a supplement to, rather than a substitute for state and local taxes and charges.
- A "stimulus" effect in which matching fund and maintenance of effort requirements tied to

³ Chris McKee, "ABQ Bus Rapid Transit Construction May Begin Late 2015," KRQE Channel 13, February 16, 2015, <http://krqe.com/2015/02/26/abq-bus-rapid-transit-construction-may-begin-late-2015/>.

federal funds requires increased spending from state and/or local funds.

- In addition, matching requirements may stimulate state and local spending by encouraging projects that would not have been undertaken without the matching funds.

Recent academic research finds that each dollar of additional federal grants to states is associated with a total increase of 54–86 cents in new state and local taxes.

The research presented in this report supports the published finding. Our statistical study is the most comprehensive analysis to date, using information from U.S. states spanning the period from 1972 to 2012 and controls for state-by-state differences in economic and demographic factors. Our results clearly demonstrate that federal transfers to state and local governments result in higher own source revenue and taxes. Across states as a group, each dollar of additional federal grants to states is associated with a total increase of 82 cents in new state and local taxes.

CONCLUSION

As Nobel Prize-winning economist Milton Friedman was famous for saying, “There is no such thing as a ‘free lunch.’” This has always been true for federal grants to the states. Not only must taxpayers pay for those grants or incur additional debt, but as this new research shows, those federal dollars have a way of spurring the growth of state and local budgets.

In New Mexico, that means state and local spending growth of approximately \$1.00 for every federal grant dollar received from Washington. While the merits of each federal grant dollar and program are debatable, this information should at least dispel the unfounded notion that New Mexicans are somehow getting something for nothing when pursuing federal largesse.