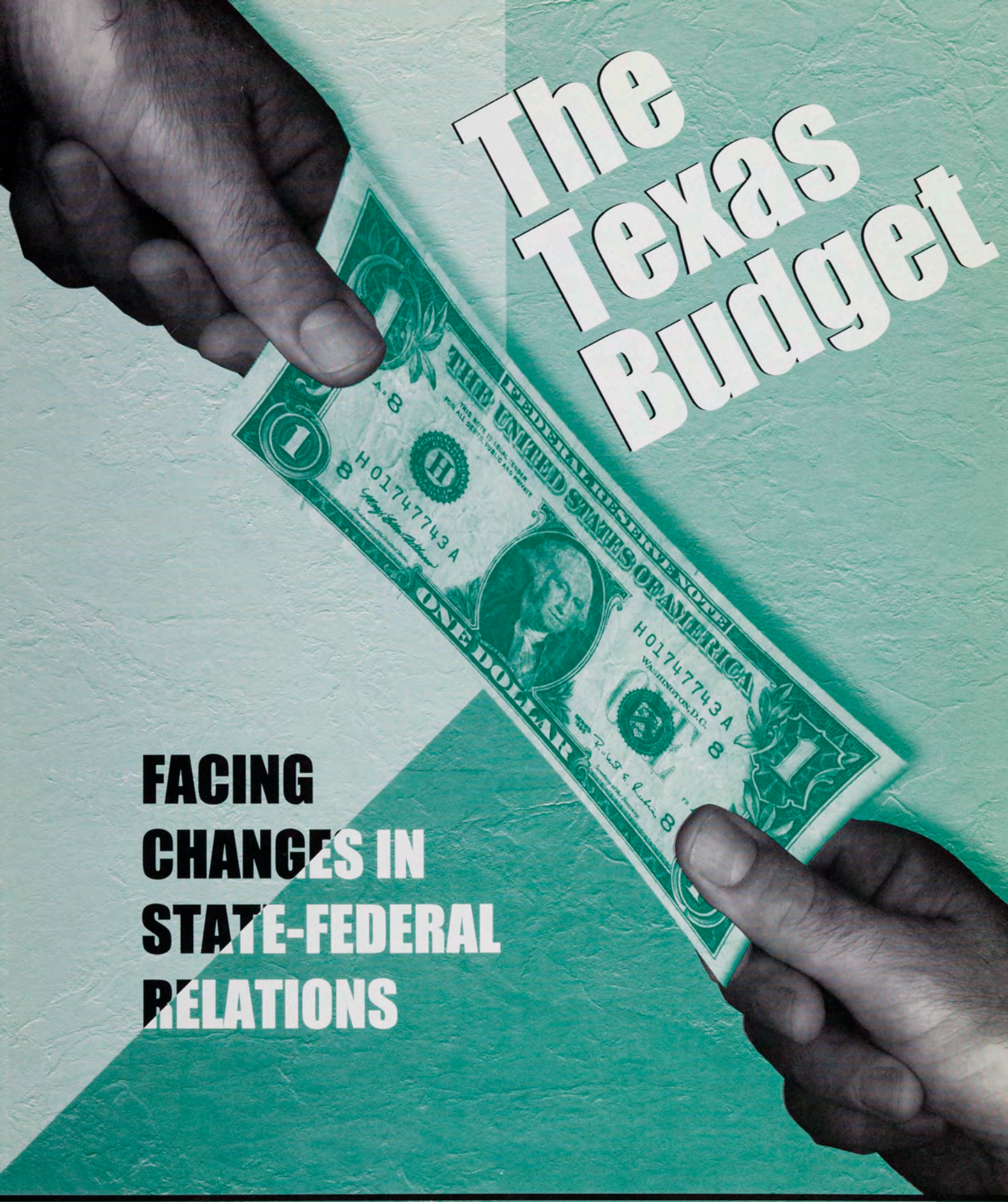

The Texas Budget

FACING CHANGES IN STATE-FEDERAL RELATIONS

Lyndon B. Johnson School of Public Affairs
The University of Texas at Austin
Policy Research Project Report

118

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Foreword

The Lyndon B. Johnson School of Public Affairs has established interdisciplinary research on policy problems as the core of its educational program. A major part of this program is the nine-month policy research project, in the course of which two or more faculty members from different disciplines direct the research of ten to thirty graduate students of diverse backgrounds on a policy issue of concern to a government or nonprofit agency. This "client orientation" brings the students face to face with administrators, legislators, and other officials active in the policy process and demonstrates that research in a policy environment demands special talents. It also illuminates the occasional difficulties of relating research findings to the world of political realities.

This report on the Texas state budget and the Texas Budget Simulator on the World Wide Web are the final products of a policy research project conducted in 1995-96 under a grant from the Legislative Budget Board. The product is twofold: a report analyzing key issues and trends that influence the development of the state budget and the Texas Budget Simulator, which attempts to demonstrate the impact of choices budget writers must make. The Texas Budget Simulator is intended to be an educational device that illustrates the restraints and problems facing legislators who must produce the biennial budget. The report and the simulator were prepared by students and have not been endorsed or approved by Legislative Budget Board staff. Neither are the policy options recommended by students necessarily endorsed by the board as the best course to follow. They are intended to illustrate possible choices.

The curriculum of the LBJ School is intended not only to develop effective public servants but also to produce research that will enlighten and inform those already engaged in the policy process. The project that resulted in this report has helped to accomplish the first task; it is our hope that the report itself will contribute to the second.

Finally, it should be noted that neither the LBJ School nor The University of Texas at Austin necessarily endorses the views or findings of this report.

Max Sherman
Dean

Preface

Our nation is in an extraordinary period of transition in the fiscal relationships among federal, state, and local governments. Fiercely debated proposals under consideration in Congress are likely to create dramatic changes in the amount of resources available to states and the channels through which they flow. Whatever changes Congress makes are likely to reduce federal aid to state and local governments. Texas, with high growth and a history of modest state funding, may be particularly affected.

In these times of transition, Texas must meet a unique challenge. Unlike Congress, the Texas legislature must produce a budget each biennium, and the budget must be balanced within anticipated revenue. The General Appropriations Act, containing the state budget and spending priorities for the next two years, is the result of thousands of hours of work by legislators, elected officials, the Legislative Budget Board, and other staff who try to meet this goal.

It is vital that Texans understand the decisions facing their state legislators. Not only must they abide by the "pay-as-you-go" provision of the Texas Constitution, but they must try to budget for state needs without a clear sense of future federal action. This is not an easy task. Federal funds have become increasingly important to state government—they are now Texas' single largest source of revenue.

This policy research project, sponsored by the Legislative Budget Board, was aimed at increasing the understanding of the budget process and the challenges facing Texas as intergovernmental fiscal relationships change. To do this, an understanding of current state revenue and spending priorities is also important.

The key element of the project is the Texas Budget Simulator (TBS), an interactive program on the World Wide Web (discussed in appendix C) that allows a user to view the state budget electronically. It includes much of the material in the report, including future budget projections and background information. It also allows the user to make policy decisions and see their impact on the budget. In addition to being a useful tool for members of the legislature, TBS will, it is hoped, help the public understand the difficulty of creating a budget that is balanced, efficient, and capable of meeting state needs.

The students and directors of this project are very grateful to the staff of the Legislative Budget Office, the Comptroller of Public Accounts and a number of state officials who shared their expertise. However, the projections and estimates are student work. They are not official and are not sanctioned by either the Legislative Budget Office, the Comptroller's Office, or other state agencies. While all the students contributed to this report and to the TBS, special thanks must go to Maureen Berner, teaching assistant, Catherine Ikels, administrative project coordinator, Pat Graves, student editor, and Peter Bradford, responsible for the Texas Budget Simulator site on the World Wide Web.

Chapter 1. Introduction

Fundamental changes and difficult decisions lie ahead for all the states, especially Texas. This report and the Internet-based Texas Budget Simulator seek to illustrate the forces that will shape those decisions. They aim to give lawmakers, policymakers, and the general public sufficient background on the issues and a range of viable options to enable them to make the best decisions possible.

The questions raised during the federal budget debate are not likely to be fully answered in the immediate future, perhaps not even by January 1997, when the 75th Texas Legislature convenes in Austin. Those legislators will be charged with producing a spending plan for the 1998-99 biennium, Texas' last biennial state budget of the 20th century. But that budget may profoundly affect generations of Texans well beyond the year 2000. Since 1993, federal funding has been Texas' largest source of revenue. During the 1996-97 biennium, the U.S. government is expected to provide Texas with approximately $24 billion, or about 30 percent of its total revenue.[1] Yet Texas remains a "net donor state," contributing more money to the U.S. Treasury than it receives.

In the midst of all this rethinking and retooling, however, some basic, traditional aspects of Texas state budgeting still hold true, with little or no sign of changing. For example:

- A relatively small portion—only about 17 percent—of the state's current $45 billion general revenue budget is purely discretionary, that is, subject to direct spending decisions of the legislature.[2] The remainder is obligated by dedicated funds (such as highways) and federal mandates (like Medicaid, a joint state-federal program providing health care to the poor) or generated by seldom-changed formulas (as in higher education).

- Unlike the federal government, the State of Texas is required to balance its budget and spend on a pay-as-you-go basis. This virtually precludes deficit spending and restricts debt, which can be incurred ordinarily only by amending the state constitution.

- Over the past 20 years, Texas has maintained one of the lowest overall state tax burdens per capita in the nation. In fiscal year 1993, it was $1,012, ranking Texas 47th.[3]

- Not surprisingly, Texas also has one of the most frugal state governments. Its state spending levels per capita consistently rank at or near the bottom among the 50 states.

- Expenditures are growing. More than 75 percent of all the money spent by Texas since annexation in 1845 has been spent since 1979.[4]

Most of the federal funds Texas receives are earmarked for health and human services, primarily Medicaid and welfare programs, such as Aid to Families with Dependent Children (AFDC). Being a growth state, Texas' increasing population will only put more pressure on state and state-run government programs to maintain, if not expand, current levels of services. This makes all the more critical the eventual outcome of the ongoing federal policy debate over returning programs to the states via block grants. Regardless of the final forms these programs take, even if they are more flexible, no one expects them to contain more money. It appears that in the next biennium, just as it has in the recent past, the demand for state services in Texas will initially outstrip anticipated revenues, presenting legislators with the prospect of a budget shortfall.

The current state budget puts a high priority on education. Legislators increased public school funding by 15.9 percent, or $2.4 billion, over the previous biennium and gave higher education 7.6 percent, or $455 million, more than in 1994-95. But concern is growing over the level of property taxes, which produce important funding for education in Texas. The Speaker of the house has said property tax relief will be a priority in the next legislative session. The governor has undertaken a study of "revenue-neutral" tax alternatives to relieve some of the burden on property owners, but any of the options that have emerged will shift the tax burden to other segments of the state's economy and arouse opposition. The state sales tax already is one of the highest in the nation, and a recently enacted constitutional amendment requiring voter approval of any proposed personal income tax all but eliminates that possibility. Can Texas continue to pay for its schools locally and control centrally?

The federal government has made more people eligible for several major entitlements, and Texas recently restructured how it delivers health services and is moving its welfare programs into the high-tech age. But it remains a high-population-growth, low-benefit state. If federal welfare and health care funds are reduced, how will Texas meet the growing demands of its poor, elderly, and infirm?

Texas is in the final phase of the largest prison expansion in the free world at a cost of more than $2 billion. It maintains more prison beds than do some countries, as well as an innovative state jail system and substance abuse treatment program, both of which currently are undercapacity. But what happens if juvenile and penal code changes combine with changes in the population to fill the prisons again? Will Texans spend more money to lock up more criminals, many of them teenagers?

Congress appears ready to reduce student loans. A college education is a bargain in Texas, attractive even to out-of-state students paying higher nonresident tuition that is lower than the in-state tuition in the student's home state. Is it time to raise tuition for Texas residents to keep universities competitive?

Texas has not had a major tax increase since 1991 when it undertook the massive prison expansion project. Due in large part to a rebounding economy and various efficiency programs, accounting measures, and streamlining, the previous two legislatures have maintained and, in some cases, actually expanded services without passing tax bills. Can the 75th Legislature make it three in a row?

This study cannot provide a definitive answer. What it does attempt to do is critically examine the major areas of revenue and expenditure in the state budget in light of proposed changes at the federal level. In most cases, the picture remains clouded, but this much is clear: as growing demands compete for more limited resources, the difficult task of deciding who gets what when isn't going to get any easier anytime soon.

Notes

[1]Texas Comptroller of Public Accounts, *Revenue Estimates for Certification of Major Fund Expenditures* (Austin, Tex., September 20, 1995), p. 21.

[2]Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1996), p. 1-7.

[3]Texas Comptroller of Public Accounts, *Sources of Revenue Growth: A History of State Taxes in Texas, 1972-1997* (Austin, Tex., January 1996), p. 89.

[4]Class presentation by State Senator John T. Montford, Chairman, Senate Finance Committee, at the Lyndon B. Johnson School of Public Affairs, Austin, Texas, December 5, 1995.

Chapter 2. Revenue

Introduction

In the 1998-99 biennium, Texas lawmakers can expect little relief from the fiscal constraints and external pressures that have made governing and, specifically, budgeting difficult in recent years. As a growth state, Texas is expected to see an increase in state revenues from sales taxes and fees generated by an expanding economy and state population. Demand for health care and education also can be expected to increase, however, as the state's population ages and diversifies. The budget picture is further clouded for Texas lawmakers by the new fiscal federalism in Washington and a statewide sentiment against tax increases and new taxes. If increased service expenditures are not offset by a corresponding increase in revenues, Texas lawmakers will confront difficult choices between program cuts or tax increases as they write the 1998-99 budget.

Background

State lawmakers have before them an enormous task: to find ways to meet the increased demand for social services within the constraints of diminished federal funding and taxpayer frustration. At issue in Congress is the legitimate role of the federal government, and, specifically, federal funds tied to regulatory compliance, in directing state-facilitated public programs, including Medicaid and Aid to Families with Dependent Children (AFDC). The shift to block grants under consideration for program funding would greatly affect state government and public programs by lifting federal regulations and giving state policymakers greater flexibility to determine where and how the bundled funds (block grants) will be used. But in exchange for greater autonomy, states may lose some of the funding traditionally granted through direct payments without a parallel reduction in mandated services.

Such a budgetary scenario could generate what likely would become one of the most contentious issues facing Texas lawmakers in writing the 1998-99 budget: whether or not to maintain current service levels in light of less federal aid. Any difference between Texas' current allotment of federal money and the amount received under block grants will have to be made up at the state level if current program spending levels are to be maintained. If so, Texas lawmakers will be forced to make up that difference with state-generated revenue.

Initiatives to consolidate and eliminate state government services and staff will generate savings, but not enough to offset a reduction in federal money or increased demand for services. For example, the consolidation of the treasurer's office into the Office of the Comptroller of Public Accounts is expected to save $20 million over five years—not nearly enough to compensate for the possible reductions in federal funds of billions of dollars.[1]

Increased revenue can only come from taxes and user fees. In 1993, voters amended the constitution to require voter approval of any income tax passed by the legislature. If an income tax ever were to be enacted, two-thirds of the revenue would be dedicated to school district property tax relief, and one third would be dedicated to public education. The amendment also requires voter approval of any subsequent increase in the tax rate. It is not known exactly how the income tax amendment will affect Texas' ability to respond to future funding demands. But the amendment will make an income tax more difficult to pass.

If additional revenues are necessary, the "easiest" means available to Texas policymakers to raise money are increasing the sales tax and expanding the sales tax base. Either of these options will meet resistance. The state's sales tax rate already is among the nation's highest, and Texas' motor vehicle rental tax rate is the highest in the United States.[2] Expanding the state's sales tax base to include groceries and other currently exempted necessities would increase the tax's regressive nature by hitting low-income families hardest and increase the state's dependence on favorable economic conditions. There are no easy solutions to Texas' revenue-generating dilemma.

Current Status of Revenue Sources

Texas receives revenue from a variety of sources, including taxes, fees, the state lottery, and federal funds. The state's revenue structure for fiscal years 1994-97 is shown in table 2.1.

State Budget Fund Structure

The 1996-97 biennial all-funds budget of $79.9 billion includes estimated appropriations of $44.5 billion from general revenue-related funds (see table 2.2), $24 billion from federal funds, and $11.4 billion from other funds.[3]

General Revenue Funds

General revenue and general revenue-related funds are available for general purpose appropriation by the legislature. General revenue funds are difficult to define due to ongoing changes in the state fund structure. In 1991, a four-year process of fund consolidation was initiated under which most statutory revenue dedications expired. That fund consolidation process was still in progress during the 1995 legislative session.[4] For purposes of this report, general funds include the nondedicated portion of the General Revenue Fund (including funds subject to consolidation and loss of dedication as of 1995) and three public education funds—the Available School Fund, the Textbook Fund, and the Foundation School Fund. The school funds are included in general revenue-related funds (sometimes referred to as "major funds" or "funds affecting certification") because of their interfund relationship in financing the state's Foundation School Program. While the state maintains more than 400 separate funds, these four funds accounted for almost 60 percent of all nontrust revenues deposited into the state treasury during fiscal year 1995.

Table 2.1

1994-99 State Revenue by Source, All Funds
(in millions of dollars)

Revenue Source	1994-95 Biennium Actual	1996-97 Biennium Estimated	1998-99 Biennium Estimated[a]	Percent Change 1994-95 to 1996-97	Percent Change 1996-97 to 1998-99	Per-cent Total 1994-95	Per-cent Total 1996-97	Per-cent Total 1998-99
Taxes								
Sales	20,068.7	22,105.2	24,577.5	10.1%	11.1%	26.6%	27.7%	41.7%
Oil & Gas Production	1,804.1	1,664.0	1,600.0	-7.8%	-3.8%	2.4%	2.1%	2.7%
Motor Fuels	4,405.6	4,666.7	2990.5	5.9%	-35.9%	5.8%	5.9%	5.1%
Cigarette & Tobacco	1,212.4	1,158.6	1,150.0	-4.4%	-0.7%	1.6%	1.5%	2.0%
Motor Vehicle Sales & Rental	3,405.0	3,802.3	4,200.0	11.7%	10.5%	4.5%	4.8%	7.1%
Corporation Franchise	2,684.2	3,075.2	3,500.1	14.6%	13.8%	3.6%	3.9%	5.9%
Alcoholic Beverage	807.2	820.8	974.4	1.7%	18.7%	1.1%	1.0%	1.7%
Insurance Occupation	1,374.8	1,236.6	1,302.7	-10.1%	5.3%	1.8%	1.6%	2.2%
Other	1,202.9	1,285.5	1,339.9	6.9%	4.2%	1.6%	1.6%	2.3%
Total	$36,964.8	$39,815.0	$41,615.0	7.7%	4.5%	49.0%	49.9%	[b]
Nontax Revenues								
Lottery Proceeds	3,248.1	3,650.2	3,759.7	12.4%	3.0%	4.3%	4.6%	6.4%
Interest & Dividends	3,412.4	3,238.9	3,592.0	-5.1%	10.9%	4.5%	4.1%	6.1%
Fees, Permits, Fines	6,896.0	6,638.4	7,361.8	-3.7%	10.9%	9.2%	8.3%	12.5%
Federal Funds	21,960.2	23,996.8	[a]	9.3%	[b]	29.1%	30.1%	[b]
Other	2,907.9	2,471.1	2,592.6	-15.0%	4.9%	3.9%	3.1%	4.4%
Total	$38,424.6	$39,995.5	[a]$17,306.0	4.1%	[b]	51.0%	50.1%	[b]
Total Revenue	$75,389.3	$79,810.2	[a]$59,258.6	5.9%	[b]	100.0%	100.0%	100.0%

Source: Texas Comptroller of Public Accounts, *Revenue Estimates for Certification of Major Fund Expenditures* (Austin, Tex., September 20, 1995). Note: All estimates for the 1998-99 biennium were calculated by class members.

[a]Indicates the absence of federal receipts.

[b]Estimates for the 1998-99 biennium were derived from a formula created for general revenue-related funds. Because these funds do not include federal funds, a projection could not be made in keeping with the process used for all other estimates. The absence of federal receipts affects the calculation of percentage changes between biennia and the total percentage of revenue per biennium.

Table 2.2

1994-99 State Revenue by Source, General Revenue Related
(in millions of dollars)

Revenue Source	1994-95 Biennium Actual	1996-97 Biennium Estimated	1998-99 Biennium Estimated[a]	Percent Change 1994-95 to 1996-97	Percent Change 1996-97 to 1998-99[a]	Percent Total 1994-95	Percent Total 1996-97	Percent Total 1998-99
Taxes								
Sales	20,022.5	22,053.4	24,500.0	10.1%	11.1%	50.2%	49.6%	53.7%
Oil & Gas Production	1,804.1	1,664.0	1,600.0	-7.8%	-3.8%	4.5%	3.7%	3.5%
Motor Fuel	1,186.2	1,560.5	1,000.0	31.6%	-35.9%	3.0%	3.5%	2.2%
Cigarette & Tobacco	1,212.4	1,158.6	1,150.0	-4.4%	-0.7%	3.0%	2.6%	2.5%
Motor Vehicle Sales & Rentals	3,405.0	3,802.3	4,200.0	11.7%	10.5%	8.5%	8.5%	9.2%
Corporation Franchise	2,685.8	3,075.2	3,500.0	14.5%	13.8%	6.7%	6.9%	7.7%
Alcoholic Beverage	697.1	707.6	724.1	1.5%	2.3%	1.7%	1.6%	1.8%
Insurance Occupation	1,372.4	1,234.0	1,300.0	-10.0%	5.3%	3.4%	2.8%	2.9%
Inheritance	324.0	349.5	375.0	7.9%	7.3%	0.8%	0.8%	0.8%
Hotel/Motel	317.0	349.8	360.0	10.3%	2.9%	0.8%	0.8%	0.8%
Utility	504.1	532.3	560.0	5.6%	5.2%	1.3%	1.2%	1.2%
Other	57.8	53.9	45.0	-6.8%	-16.5%	0.1%	0.1%	0.1%
Total	$33,588.4	$36,541.2	$39,314.1	8.8%	7.6%	84.3%	82.2%	86.5%
Nontax Revenues								
Lottery Proceeds	1,680.9	2,193.5	2,259.3	30.5%	3.0%	4.2%	4.9%	5.0%
Interest & Dividends	1,512.5	1,291.6	1,432.4	-14.6%	10.9%	3.8%	2.9%	3.1%
Fees, Permits, Fines	1,131.0	1,195.8	1,326.1	5.7%	10.9%	2.8%	2.7%	2.9%
Federal Funds	0.0	0.0	0.0	0.0%	0.0%	0.0%	0.0%	0.0%
Other	1,949.8	1,110.5	1,143.8	-43.0%	3.0%	4.9%	2.5%	2.5%
Total	$6,274.2	$5,791.4	$6,161.6	-7.7%	6.4%	15.7%	13.0%	13.5%
Total Revenue	$39,862.3	$44,472.6	$45,475.7	11.6%	2.3%	100.0%	100.0%	100.0%

Source: Texas Comptroller of Public Accounts, *Revenue Estimates for Certification of Major Fund Expenditures* (Austin, Tex., September 20, 1995).

[a]Indicates projected estimates calculated by class members.

Authorization to spend these dollars is contingent upon the comptroller's certification that estimated revenues and balances will cover the appropriations. If the comptroller's estimate of general revenue exceeds actual collections, then the result could be a cash deficit for that budget period. Revenue estimates for these funds are based largely on economic factors.[5]

Federal Funds

The federal funds category includes all funds received from the U.S. government by Texas state agencies and institutions named in the General Appropriations Act. These funds, in the form of federal grants, allocations, aid, payments, and reimbursements, are appropriated to those state entities responsible for administering federal programs and policies. Revenue estimates for federal funds are not based on economic factors because appropriations for these funds depend on the actions of the federal government.[6]

Other Funds

Sometimes referred to as "minor funds," other funds are dedicated for specific uses and not available for general purpose spending. Examples include constitutionally dedicated highway funds and higher education operating funds. Federal funds also can be categorized as other funds due to these types of limitations. Other-fund spending is limited to appropriations or actual revenues and available balances, whichever is smaller. Therefore, other funds can never have a cash deficit. Revenue estimates for minor funds are not based on economic factors because appropriations for these funds depend mainly on the actions of other governing bodies.[7]

Taxes

During the 1996-97 biennium, 49.9 percent of state revenues (all funds) come from taxes.[8] These taxes vary in nature and affect almost every sector of the Texas economy. Table 2.3 illustrates Texas' system of taxation and the contribution of each tax to the state's total collections.

Sales Taxes

Sales taxes in Texas include the limited sales and use tax, the motor fuel lubricants sales tax, and the boat and boat motor sales and use tax. In the 1996-97 biennium, these taxes are estimated to contribute $22.1 billion, or 55.5 percent of Texas' all-funds tax revenues (60.4 percent of the general revenue budget).[9] While the estimate for 1996-97 represents a 10.1 percent increase in the amount of sales tax revenue collected during the 1994-95 biennium in the general revenue budget, the rate of growth in the amount collected is expected to decline during the 1996-97 biennium due to a projected statewide downturn in consumer spending and economic activity.

The broadest of these taxes by far is the limited sales and use tax, first imposed in 1961. This tax is levied on transactions imposed on final sales, rentals, and leases of tangible personal property (physical goods) and on sales of some services, such as repair of tangible personal property, amusement services, and telephone services.[10] The limited sales and use tax currently is assessed at the rate of 6.25 percent statewide, fifth highest among the 45 states imposing statewide sales taxes in 1994.[11] Many local governmental units,

Table 2.3

Texas Tax Structure, All Funds

Tax	Percent Total Tax Revenues 1996-97	1994-95 Revenues (in millions of dollars)	1996-97 Revenues (in millions of dollars)	Percent Change from 1994-95 to 1996-97
Sales	55.5	20,068.8	22,105.2	10.1
Oil & Gas Production	4.2	1,804.1	1,664.0	-7.8
Motor Fuels	11.7	4,405.6	4,666.7	5.9
Cigarette & Tobacco	2.9	1,212.4	1,158.6	-4.4
Motor Vehicle Sales & Rental	9.6	3,405.0	3,802.3	11.7
Corporation Franchise	7.7	2,684.2	3,075.2	14.6
Alcoholic Beverage	2.1	807.2	820.8	1.7
Insurance Occupation	3.1	1,374.8	1,236.6	-10.1
Other	3.2	1,202.9	1,285.5	6.9
Total Tax Revenue	100.0	36,964.7	39,814.0	7.7

Source: Texas Comptroller of Public Accounts, *Revenue Estimates for Certification of Major Fund Expenditures* (Austin, Tex., September 20, 1995).

such as cities, counties, and metropolitan transit authorities, also are authorized to levy sales taxes of up to 2 percent in any locality in addition to the 6.25 percent statewide rate.

Certain goods, such as groceries, residential gas and electric utilities, and prescription medication, are exempt from state and local sales taxes. Additionally, most services, such as medical, legal, accounting, and engineering, are exempt from sales taxation. On January 1, 1995, all manufacturing equipment and machinery became exempt from the sales tax. Sales tax revenues are not dedicated and flow directly into the state's General Revenue Fund.

The motor fuel lubricants sales tax, first imposed in 1961, is a levy of 6.25 percent on the retail price of motor fuel lubricants sold in Texas. All the revenue from this tax goes to the State Highway Fund.

The boat and boat motor sales and use tax, enacted by the legislature in 1991, is a 6.25 percent levy added to every retail purchase of a boat in Texas as well as those purchased outside of the state and brought into Texas. Currently, 95 percent of the revenues from this tax is deposited into the General Revenue Fund. The remaining 5 percent goes to local tax assessor-collectors or the Texas Parks and Wildlife Department, depending on which entity collects the tax.

Oil and Gas Production and Regulation Taxes

Texas' oil and gas production and regulation taxes, known as severance taxes, are expected to produce 4.2 percent of the tax revenue in the all-funds budget in 1996-97 (4.6 percent of the state's total tax revenues in general revenue budget).[12] These taxes are based on gross production volume and the market value of crude oil and natural gas produced in the state. The oil production tax was adopted by the legislature in 1905. The legislature enacted the natural gas production tax in 1931. During the 1996-97 biennium, revenues from oil and gas production and regulation taxes are estimated to decline 7.8 percent from the general revenue budget 1994-95 biennium levels as a result of decreasing oil production rates in the state and lower natural gas prices, primarily caused by oversupply.

Since 1951, crude oil has been taxed at the rate of 4.6 percent of the value of the oil, with a minimum tax of 4.6 cents per barrel. Exceptions to the 4.6 percent rate are made for new or enhanced recovery projects, which are taxed at a rate of 2.3 percent. Natural gas is taxed at 7.5 percent of its market value, and condensate at 4.6 percent.

Current statutes define oil and natural gas severance taxes as occupation taxes. The state constitution puts 25 percent of the revenues collected from these taxes in the Foundation School Fund to finance public education. The remaining 75 percent of these revenues goes to the General Revenue Fund.

Historically, oil and gas severance taxes were a significant portion of Texas' revenue picture, especially during the early 1980s. As recently as 1982, oil and gas severance taxes brought in $1.3 billion and comprised 17.7 percent of the state's total tax revenue.[13] In recent years, however, oil prices and production levels have fallen and the state's economy has diversified.[14]

Motor Fuel Taxes

The motor fuel taxes levied on gasoline, diesel fuel, and liquefied petroleum gas are estimated to contribute 11.7 percent of total tax revenue in the all-funds budget, 4.3 percent of total tax revenues in the general revenue budget, in the 1996-97 biennium. This is a 31.6 percent increase in the amount collected in the general revenue budget during the 1994-95 biennium as a result of a change in the motor fuel taxes allocation schedule. If the allocation schedules had not been changed, motor fuel tax revenues would have grown by less than 3 percent.[15]

Gasoline and diesel fuel taxes are excise taxes on first sale or use. Both are taxed at 20 cents per gallon. Liquefied petroleum gas used for the propulsion of motor vehicles on public highways is taxed at 15¢ per gallon. Motor fuel taxes are dedicated to the State Highway Fund (75 percent) and to the Available School Fund (25 percent). The legislature enacted the gasoline tax in 1923 and the diesel fuel tax in 1941. The liquefied petroleum gas tax was collected under the diesel fuel tax until 1980 when the two were separated.[16]

Cigarette and Tobacco Taxes

Cigarette and tobacco taxes are expected to contribute 2.9 percent to the all-funds total tax revenue and 3.2 percent of total tax revenues during the 1996-97 biennium in the general revenue budget. As a result of declining consumption, these taxes are expected to raise 4.4 percent less revenue for the general revenue budget in the 1996-97 biennium than during the 1994-95 biennium.[17]

The cigarette tax, the largest portion, is levied at a rate of either 41¢ per pack of 20 or 50¢ per pack of 20, depending on weight. When the cigarette tax was enacted in 1935, the rate was 3¢ per pack. Until September 1, 1995, 1.83 percent of the revenue went to the Foundation School Fund with the balance to the General Revenue Fund. All cigarette tax revenue now goes into the general fund.

Cigars and other tobacco products were taxed under the cigarette tax until 1959 when they were separated because of differences in packaging methods. Cigars are taxed at a rate of 1¢ per 10-count, for weight under three pounds, to $15 per 1,000-count, for weight over three pounds. Chewing tobacco, snuff, and other tobacco products are taxed at a rate of 35.2 percent of the factory price. All revenue raised by taxes on noncigarette tobacco products goes into the General Revenue Fund.

Motor Vehicle Sales and Rental Taxes

Motor vehicle sales and rental taxes are composed of the motor vehicle sales and use tax, the motor vehicle use tax (direct), the motor vehicle rental tax, the manufactured housing sales and use tax, and the interstate motor carriers tax. Together these taxes are expected to bring in 9.6 percent of the total tax revenue in the all-funds budget, and 10.4 percent of total tax revenue to the general revenue budget during the 1996-97 biennium; this represents an 11.7 percent increase from the 1994-95 biennium.[18]

The motor vehicle sales and use tax, enacted in 1941, is by far the largest of these taxes and has five separate components. The tax applicable to each vehicle depends on whether the vehicle was purchased in or out of state without taxes paid, purchased out of state with taxes paid, exchanged for another vehicle, given as a gift, or purchased for use as scrap metal. Most of the revenue from this tax is generated by a 6.25 percent levy on the purchase price of each vehicle sold in the state, or brought into the state if taxes have not been paid elsewhere, less the value of any trade-in. County tax assessor-collectors retain five percent of the revenues raised by these two motor vehicle sales and use taxes for administrative costs. Of the remaining 95 percent, 25 percent goes to the Foundation School Fund, and 75 percent to the General Revenue Fund.

The motor vehicle rental tax, first levied in 1971, uses a staggered rate schedule. Vehicle rentals of 30 days or less are taxed at a rate of ten percent of the rental charge; rentals exceeding 30 days are taxed at a rate of 6.25 percent. 25 percent of revenues from the motor vehicle rental tax goes to the Foundation School Fund, the rest to the General Revenue Fund.

The manufactured housing sales and use tax is imposed on the initial sale or use of all new manufactured homes (mobile homes). This tax is levied at a rate of five percent of 65 percent of the manufacturer's sale price, less shipping or delivery charges. The manufactured housing sales and use tax was collected under the motor vehicle sales tax until 1982. All revenues collected under this tax go into the General Revenue Fund.

The interstate motor carriers tax, which is being phased out, is a tax on interstate motor vehicles, trailers, and semitrailers operated by motor carriers located or doing business in the state. The tax is 6.25 percent of the vehicle's purchase price multiplied by the percentage of total miles driven in Texas the preceding year. Vehicles with no previous mileage history in the state are taxed on an estimated basis. 25 percent of revenues raised by this tax goes to the Foundation School Fund, and the rest to General Revenue. The tax originally was part of the motor vehicle sales and use tax, but the legislature separated them in 1982. In 1995, the 74th Legislature repealed the interstate motor carriers tax effective September 1, 1997.

Corporate Franchise Tax

The corporate franchise tax, created in 1907, is expected to contribute 7.7 percent of Texas' total revenue in the all-funds budget and 8.4 percent of Texas' total tax revenues in the general revenue budget during the 1996-97 biennium. The corporate franchise tax is levied on all limited liability companies and corporations conducting business in Texas. Corporation franchise tax revenues collected in the general revenue budget in the 1996-97 biennium are expected to increase 14.5 percent over the 1994-95 biennium due to a robust state economy, continued business expansion into Texas, and strong corporate profits forecasts.[19]

In 1991, the legislature restructured the corporate franchise tax to provide a more stable tax base in response to criticism that the prior structure overtaxed capital-intensive businesses, such as manufacturers and oil producers, and undertaxed less-capitalized service corporations. The corporate franchise tax now levies a tax of $2.50 per $1,000 of net taxable capital; the franchise tax also is levied on the amount of a corporation's "earned surplus" that exceeds the tax on capital. The tax rate on earned surplus, roughly defined as the amount of the corporation's federal taxable income plus officer and director compensation, is 4.5 percent.[20] All funds raised by the franchise tax go to General Revenue.

Alcoholic Beverage Taxes

The mixed drinks and gross receipts tax, the liquor tax, the airline/passenger train beverage tax, the wine tax, and the malt liquor (ale) tax will contribute 2.1 percent of Texas' all-funds tax revenues in the all-funds budget, and 1.9 percent of total tax revenues in the general revenue budget in the 1996-97 biennium.[21] Revenues from alcoholic beverage taxes in the current biennium are estimated to rise 1.5 percent from the amount collected in the general revenue budget in the 1994-95 biennium. Under current laws, approximately 16 percent of the revenue raised by all alcoholic beverage taxes, except the mixed drinks gross receipts tax, is forwarded to the comptroller for administration, enforcement, and regulation

of alcoholic beverages. Of the remaining balance, 75 percent goes into the General Revenue Fund and 25 percent into the Available School and Foundation School funds.

The mixed drinks gross receipts tax rate is 14 percent of gross receipts from the sale of alcoholic beverages or ice and nonalcoholic beverages intended for use with alcoholic beverages. These beverages must be consumed on the premises of the permit holder. Revenue from the mixed drinks gross receipts tax is distributed as follows: 10.7 percent to the county of collection, 10.7 percent to the city of collection, and the remaining balance to the General Revenue Fund. The legislature first levied the mixed drinks gross receipts tax in 1971.[22]

The liquor tax has been levied on distilled liquors and liquor prescriptions since 1935. Distilled liquor is taxed at a rate of $2.40 per gallon. Liquor prescriptions are taxed at a rate of 22¢ per prescription.

The airline/passenger train beverage tax is 5¢ on each serving of an alcoholic beverage served by the holder of an airline beverage permit or passenger train beverage permit within the state. This tax first was levied in 1969.

The beer tax is $6 per 31-gallon barrel and is levied on the first sale or importation of beer. The malt liquor (ale) tax is imposed on malt liquor with an alcohol content greater than 4 percent at a rate of 19.8¢ per gallon. Tax liability in this case occurs when the liquor is received in the state for storage, sale, or distribution. The beer tax and the malt liquor (ale) tax first were imposed in 1935.

The wine tax, also imposed in 1935, is levied on wine based on its alcohol content. Wine with an alcohol content of 14 percent or less is taxed at 20.4¢ per gallon. Wine with an alcohol content greater than 14 percent is taxed at a rate of 40.8¢ per gallon. Sparkling wines are taxed at a rate of 51.6¢ per gallon.

Insurance Occupation Taxes

Insurance occupation taxes provide 3.1 percent of the current tax revenue in the all-funds budget and 3.4 percent of current tax revenue in the general revenue budget and consist of the insurance occupation tax, insurance companies maintenance tax, and the property and casualty, title, and other insurer assessments. Estimated insurance occupation revenues for the 1996-97 biennium have declined 10.1 percent in the general revenue budget from actual 1994-95 biennium levels. This is due primarily to 1993 legislative changes in how and when the taxes are collected and which state agency collects them.[23] Insurance occupation taxes are levied on the gross premiums collected in Texas, with rates determined by both the type of policy purchased and the amount of Texas-based investments owned by the insurance company relative to comparable states. Twenty-five percent of the insurance occupation taxes is allocated to the Foundation School Fund; the balance is deposited into the General Revenue Fund.

Life, accident, and health insurance policy premiums are taxed at rates varying from 1.7 percent to 2 percent. Policy premiums for property and casualty insurance are taxed at rates

varying from 1.6 to 3.5 percent. Title insurance policy premiums are taxed at rates varying from 1.3 to 2 percent. Surplus lines and unauthorized insurance are taxed at 4.85 percent of gross premiums.

Other Taxes

Texas has a number of taxes that each generate less than 2 percent of the state's total tax revenue, both in the general revenue budget and the all-funds budget. These taxes include the state inheritance tax, the hotel/motel tax, utility taxes, and an assortment of smaller taxes, such as the cement tax, the sulfur tax, and the bingo rental tax. In the aggregate, these taxes are estimated to contribute 3.5 percent of total tax revenue during the 1996-97 biennium in the general revenue budget (3.2 percent of the total revenue in the all-funds budget).[24]

Nontax Revenue

During the 1996-97 biennium, nontax revenue is estimated to contribute 50.1 percent to total state revenue in the all-funds budget. In recent years, after the creation of the state lottery and as the amount of federal funds flowing into the state increased, the percentage of the budget funded by nontax revenue has grown. Revenue received from the federal government will be the single largest source of income for the state during the 1996-97 biennium, 30.1 percent of all state revenue.[25]

State Lottery

Voters approved the creation of the Texas Lottery on November 5, 1991. The first lottery scratch-off game began on May 29, 1992. Net lottery revenue has risen each year since its inception and is expected to reach $2.2 billion in the general revenue budget during the 1996-97 biennium, an increase of 30.5 percent from the amount collected in the 1994-95 biennium. Lottery proceeds are anticipated to contribute 4.6 percent to the state's total revenue under the all-funds budget during the 1996-97 biennium and 4.9 percent of the general revenue budget.[26]

Under current statutes, 10 percent of net lottery proceeds goes to the Texas Lottery Commission for administration, 5 percent to lottery retailers, and the remainder to the General Revenue Fund.

Interest and Dividends

Derived principally from investments made by the Permanent University Fund and the Permanent School Fund, interest and dividends are an important source of nontax revenue for the State of Texas. Interest and dividends are estimated to contribute $3.2 billion, or 3.9 percent, to total revenues in the all-funds budget during the 1996-97 biennium. In the general revenue budget, interest and dividends represent $1.3 billion, or 2.9 percent of the general revenue budget, a 14.6 percent decline since the 1994-95 biennium. This downturn is the result of a new State Board of Education investment strategy designed to increase long-term interest income earned by the Permanent School Fund for the Available School

Fund at the expense of current interest income.[27] Interest and dividends from the Permanent University Fund and the Permanent School Fund accrue to the Available University Fund and the Available School Fund, respectively.

Fees, Permits, Fines, and Penalties

These sources are expected to account for 8.3 percent of state revenue in the all-funds budget in the 1996-97 biennium and 2.7 percent of the general revenue-related budget.[28] Some of the rates are set by the collecting agencies; others are set by statute. Usually, these charges include collection costs and, in the cases of fines and penalties, a punitive surcharge. In many instances, the levies generate extra revenue as well. This revenue helps offset the amount of general revenue that otherwise might have been required for the agencies.

Since the 1994-95 biennium, these revenues have grown largely because, in an atmosphere of "no new taxes," voters have preferred increases in fees, permits, fines and penalties because users directly incur costs.

Federal Funds

Federal funds are the single largest source of revenue in the state budget. In the 1996-97 biennium, receipts from the federal government are expected to amount to $24 billion, or 30.1 percent of total state revenue.[29]

Most federal funds come to the state in the form of grants requiring state matches and reimbursements of various sizes. This is the case with health and human services funds and highway funds, respectively: the more the state spends, the more the federal government must contribute. Federal funding formulas vary, however, and some grants do not require state contributions. Because federal funds are a major share of the state budget, they will be addressed more specifically in subsequent chapters.

Revenue Administration

Comptroller of Public Accounts

The Office of Comptroller of Public Accounts was created in 1836, the earliest days of the Republic of Texas. Back then, the appointed comptroller kept the new nation's books and made sure debts were paid. This is still true today, though the form and function of the comptroller 's office has expanded considerably and will continue to do so. For example, beginning in September 1996, the comptroller's office will assume responsibility for the duties and functions of the treasurer's office.

The comptroller is the state's chief accountant, keeping track of state expenditures and collecting 26 state taxes. The comptroller's office processes state agency payments, ensuring that the state remains within its budget. Further, it ensures that all state tax and fiscal laws are applied fairly and consistently. Additionally, the comptroller is responsible

for issuing the state's official revenue forecast at the start of each legislative session so the Texas Legislature can budget accordingly.

State Treasurer

The treasurer's office is responsible for six core functions: investments, cash and securities management, cash management programs, trust operations, management of the unclaimed property program, and collection of the cigarette and tobacco taxes, a duty currently contracted out to the Comptroller of Public Accounts. The treasurer is responsible for the safety of state funds and for ensuring the highest possible return on investment of those funds. The treasurer and comptroller together must sign all checks drawing on state accounts.

The treasurer's office was abolished by constitutional amendment November 7, 1995. The powers, duties, and property of the treasurer's office were transferred to the comptroller's office on September 1, 1996. A three- to four-year phaseout and transfer of duties is expected. Primary treasury functions, such as investment, management of public funds, and items processing, will become a new and separate division within the comptroller's office.

According to a Legislative Budget Board fiscal note, based on a comptroller's estimate, the elimination and consolidation of the treasurer's office is expected to save the state $20 million over five years, beginning in fiscal year 1997.[30]

Only the consolidation of internal departments and staff provides immediate, clear-cut savings. The total savings cannot be determined until the transition is complete, in fiscal year 2000. Representatives from the comptroller's and treasurer's offices are performing cost-benefit analyses for all treasurer's office functions to determine the true costs and savings of transferring and consolidating duties. The initial costs associated with converting the treasurer's computer system to the comptroller's system are expected to be recouped within a few years.

Revenue Trends

Texas revenue has grown in the past 20 years. From all funds in the 1974-75 biennium, Texas collected $10.6 billion in total revenue. In the 1994-95 biennium, Texas collected $75.4 billion in total revenue from all funds, but gains in revenue are not consistent across all categories. Although sales tax revenues have increased as the Texas economy has grown during the past 20 years, oil and gas severance tax revenues have declined since the 1974-75 biennium as production levels have fallen off.

Revenue Forecasting Methodology

The Comptroller of Public Accounts produces the revenue estimate that serves as the basis for certification of general revenue-related fund expenditures for each biennium. The comptroller's office uses several different approaches to produce revenue forecasts.

Regardless of the approach employed, judgment is critical. Furthermore, some forecasts will be subjective, based on the experience, intuition, and educated guesswork of people in the revenue forecasting division of the comptroller's office. Over the past 19 years, the Biennial Revenue Estimate has not varied from the actual amounts collected by more than 4.5 percent.[31]

The revenue forecasting process begins with a formulation of the economic outlook. The Texas economic outlook is based on national forecasts adjusted for regional and local variances. The comptroller relies on the *U.S. Economic Outlook*, a monthly report that provides detailed analyses of specific sectors of the U.S. economy, such as industrial activity, business investment, and consumer markets. Published by the WEFA Group, an economic and information consulting firm, this report provides short- and long-term micro- and macro-economic and regional forecasts and analyses.

The *Texas Economic History and Outlook for Calendar Years 1992 to 1997*, prepared by the comptroller's office, forecasts annual percentage changes in the gross state product, personal income, nonfarm employment, resident population, unemployment rate, oil prices, natural gas prices, and the oil and gas drilling rig count. The forecast is a key element in preparing the revenue forecasts produced by the state.[32]

The multiple regression model, a forecasting device used extensively by the comptroller's office, estimates revenue as a function of one or more independent economic variables, characterized as those that influence revenue streams. Table 2.4 shows several key determinants of major tax revenues in Texas.

Each equation used to estimate a revenue source is independent of the others. For instance, retail sales tax and franchise tax collections can be estimated as a function of calendar-year personal income, each in separate and unrelated equations. Other independent variables, such as demographic features of the economy, also can be a part of the equation.[33]

The equations generated by the multiple regression model ordinarily will be selected on the basis of which previous estimates produced by the equations coincide with actual revenue collections. Because many alternative specifications fit similarly to historic data, trial predictions (simulations) for earlier years also are prepared. The equation coming closest to a recent known result is selected. Ordinarily, separate equations are prepared for each major revenue category to allow for different responses to changes in independent variables.[34]

The basic steps in preparing a regression-based forecast are summarized below:

1. Develop economic forecasts.

   Look at national, regional, and state economic models; make exogenous assumptions.

2. Predict the revenue base.

   Translate economic activity into revenue base.

3. Estimate tax liability.

   Apply relevant tax rates to revenue base.

4. Estimate revenue timing.

   Adjust liabilities to fiscal year; accommodate legislative changes in tax structure.

Pending Litigation

Franchise Tax

In a case pending in the state's Third Court of Appeals, Caterpillar, Inc., is challenging the way the Comptroller of Public Accounts treats medical benefits when figuring a company's state franchise tax. Under consideration is whether the comptroller's policy violates a federal law forbidding state interference in federally approved employee benefit plans.[35]

Although only about $3.5 million is at stake in the case, many other companies would also be eligible for tax refunds if Caterpillar wins this lawsuit. The comptroller's office estimates that if Caterpillar prevails, the state might have to pay more than $1 billion in refunds to thousands of companies. The effect on future tax revenue would not be as great because of changes made in 1991 in the way franchise taxes are assessed. Nevertheless, the comptroller's office believes losing the appeal would cost Texas tens of millions of dollars in revenue annually.[36]

Sales Tax

In *Tyler Pipe Industries, Inc. v. Sharp et al.*, the issue before the court is whether equipment used to make molds to manufacture cast-iron pipe and fittings should be exempt as manufacturing equipment. Tyler Pipe Industries contends that, while they have been denied this sales tax refund, the comptroller has granted refunds to similarly situated taxpayers.

Should the case be decided in Tyler Pipe's favor, the company will be entitled to refunds for sales taxes paid to date. In addition, other companies across the state will be entitled to refunds for equipment previously not considered manufacturing equipment. Although the comptroller's office is still in the process of assessing the fiscal impact and has not reached a conclusion, the impact of annual losses that could result from an unfavorable ruling is considered to be substantial.[37]

Table 2.4

Major Determinants of Tax Revenue

Tax	Major Determinants
Sales	Texas disposable and personal income
	Texas mining, construction, and manufacturing employment
	Selected U.S. producer price indices
Motor Fuels	Population
	Fleet efficiency
Motor Vehicles	Texas disposable personal income
	Interest rates
Corporation Franchise	Gross state product
	Texas personal income
Oil & Gas Production	International oil prices
	Texas oil and gas prices
	Texas recoverable reserves
	Technological advances

Source: Adapted from Bob Bullock and John P. Moore, "Revenue Estimating: Methods and Results," in *Budgeting in Texas: Process, Problems, Prospects*, ed. Aman Khan (Lanham, Md.: University Press of America, Inc., 1991), p. 121; and conversations with Mike Wegner, Executive Assistant, Texas Comptroller of Public Accounts, 1996.

Issues in Taxation

Telecommunications

The comptroller's office will make a decision regarding collection of a new state tax on services. At issue is what rate to tax wireless companies' income. Currently, a 5-10 percent tax is under consideration.[38]

Determining the tax rate will prove challenging for the comptroller's office. Unlike most taxes, which are based on a fixed rate regardless of how much (or little) is raised, the telecommunications levy has to raise a fixed amount of money from an indeterminate number of companies with unpredictable revenue.[39]

Another complicating factor in this issue is that the cost of the tax likely will be passed on to consumers. Comptroller's office policy makes any increased charges subject to state sales tax and to the telecommunications levy as well.[40] Any future proposals for taxation in the rapidly evolving field of telecommunications must be carefully considered in light of these current difficulties.

Employee Leasing

The comptroller's office, according to its interpretation of a long-standing state law, has the power to collect sales tax from staff-leasing companies. The office waited while the industry made its case and attempted to exempt itself from the tax by trying to change state law. The proposal, which would have cost state and local governments about $100 million over the next five years, never reached a vote in the 1995 legislative session.[41]

The sales tax rate ranges from 6.25 percent to 8.25 percent and must be applied to the entire cost of leasing certain types of employees who perform taxable services as defined by state law, such as word processing, phone answering and janitorial work. Not included are many blue-collar manufacturing jobs, such as assembly-line work.[42]

Leasing companies argue that they should not pay sales tax because the workers they lease do not actually work for them. There is an important distinction: if the employees work for the lessors' clients, their services are not taxable. The comptroller's office maintains that, if it exempts staff-leasing companies from the sales tax, it would have to exempt other contractors. The concern is that this could prompt companies to restructure their businesses to avoid taxes.[43]

Areas of ambiguity must be clearly defined before additional revenue legislation can be effectively administered in the area of staff leasing.

Policy Options

Texas policymakers have a wide array of revenue-raising policy options available to them should the state budget require additional revenues during the 1998-99 biennium.

Accompanying the following policy options are revenue projections for the 1998-99 biennium. All estimates are for general revenue-related funds. These projections reflect research into general revenue estimating methods and were calculated using a historical projection model that considers and incrementally weights the actual and estimated revenue for the last three bienniums (1992-93, 1994-95, and 1996-97). The estimates are subject to change depending on economic and statutory factors.

Projected revenues for each policy option reflect additional amounts the state could expect to collect over the 1998-99 biennium.

1. Increase the sales tax rate effective January 1, 1998.

   Many Texans consider the sales tax a fair tax because everyone pays it. However, Texas already has the fifth highest sales tax rate in the country at 6.25 percent. Sales taxes are considered regressive because lower-income taxpayers spend higher proportions of their income on sales taxes than do higher-income taxpayers[44]

Sales Tax Rate Increase	Projected Revenue 1998-99
From 0.25% to 6.5%	$627 million
From 0.5% to 6.75%	$1.218 billion
From 1.0% to 7.25%	$2.391 billion

2. Broaden the sales tax base effective January 1, 1998.

   Expanding the state sales tax base to include services not currently taxed would make the sales tax more comprehensive and raise more money. The elimination of exemptions politically problematic. Sales taxes on services are more difficult to administer because a taxable service must be defined in law, and many definitions lack specificity.[45]

Exemption to Be Removed	Projected Revenue 1998-99
All Current Exemptions	$8.384 billion
All Exemptions Except Those for Food, Water, School Lunches, and Physician and Other Health and Dental Services	$6.158 billion
Manufacturing Gas and Electricity	$610.0 million
Containers, Packaging, and Wrapping Supplies	$253.4 million

Exemption To Be Removed	Projected Revenue 1998-99
Residential Gas and Electricity	$784.5 million
Legal Services	$202.0 million
Auto Maintenance and Repair Services	$201.5 million
Architectural and Engineering Services	$173.4 million
Coin Operated Amusements and Laundry	$53.9 million
Travel Arrangement Services	$49.7 million
Newspapers and Newspaper Inserts	$45.5 million
Car Washes	$18.5 million

3. Replace the corporate franchise tax with a two percent gross receipts tax.

   A gross receipts tax may prove more equitable in terms of the benefits principle. An unprofitable corporation receives many of the same benefits, or at least the same level of government cost effort, as a profitable one. A franchise tax does not reflect the industry's benefit from these efforts.[46] A gross receipts tax without standard deductions, even at modest rates, would have potentially devastating effects on certain industries, such as wholesalers, whose profit margins already are slim. Retailers, such as auto dealers, who also operate at low profit margins, would be hard hit as well. A substantial portion of the burden of a gross receipts tax might be shifted onto consumers.[47]

Gross Receipts Tax Provisions	Projected Revenue 1998-99[48]
Without Standard Deductions	$31.772 billion
With $500,000 Standard Deduction	$28.109 billion

4. Enact a flat-rate income tax with no deductions or minimum income.

   Increased public awareness of the concept of a flat-rate income tax, due in part to the 1996 presidential campaign, may have provided sufficient public interest to explore the flat personal income tax as a possible revenue source. In 1993, however, voters overwhelmingly adopted a constitutional amendment requiring

voter approval of any income tax legislation. Given the current antitax climate, it is unlikely that voters would approve such a tax. Under the amendment, two-thirds of the revenue generated by an income tax would be dedicated to local property tax relief; the remaining third would be available for general revenues, as shown below.

Flat Tax Rate	Projected Revenue 1998-99[49]
0.5%	$2.819 billion
	$940 million (general revenue)
1.0%	$5.638 billion
	$1.880 billion (general revenue)

5. Increase gasoline and diesel fuel tax rates by 5¢, from 20¢ to 25¢ per gallon.

   Gasoline and diesel fuel tax revenues are dedicated by statute: 75 percent to the State Highway Fund and 25 percent to the Available School Fund. According to the comptroller's office, fuel taxes are simple to administer, are easy to understand, and promote energy consumption. They are essentially user fees in that the more one drives on the state's highways, the more fuel is consumed, and ultimately the more taxes are paid. According to data from the Consumer Expenditure Survey conducted by the U.S. Department of Labor, most of the fuels taxes are paid by higher income groups (who tend to have higher rates of automobile ownership). However, fuels taxes may ultimately prove to be regressive because, as a percentage of family income, fuels taxes tend to consume a greater proportion of the income of lower income taxpayers.[50]

Fuels Tax Increase	Projected Revenue, 1998-99
5¢ per Gallon	$1.029 billion
	$771.9 million (Highway Fund)
	$257.3 million (Available School Fund)

Conclusion

Issues of tax equity, exemptions, rate increases, and base expansions likely will dominate revenue discussions in the next biennium. While these policy options reflect a range of choices available to lawmakers for generating additional revenue, they are nevertheless not politically expedient. As is often the case with taxes and spending, there are no easy answers, only difficult decisions. With population growth straining the state's service capacity, the public's increasing antitax sentiment, and the potential for a restructuring of

federal programs and funding, state lawmakers in the 1997 legislative session will contend with immediate fiscal crises as well as long-range budget issues.

The loss of federal dollars to social and economic programs could force lawmakers to devote more general revenues to these programs. Legislators will have to decide whether to maintain current service levels—and make up for less federal funding with state, local, or private-sector money—or decrease service levels in proportion to diminished federal assistance. Neither choice is politically palatable, but, in the current federal fiscal environment, one of them appears inevitable.

Notes

[1]Texas Comptroller of Public Accounts, *Fiscal Note Estimate for Senate Bill 20 as Engrossed, April 5, 1995* (Austin, Tex.).

[2]Texas Comptroller of Public Accounts, *Sources of Revenue Growth: A History of State Taxes in Texas, 1972-1995* (Austin, Tex., 1994), p. 15.

[3]Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1996), p. 1-1.

[4]Ibid.

[5]Class presentation by Mike Wegner, Executive Assistant, Texas Comptroller of Public Accounts, at the Lyndon B. Johnson School of Public Affairs, Austin, Texas, February 29, 1996.

[6]Legislative Budget Board, *Fiscal Size Up*, p. 1-7.

[7]Class presentation by Mike Wegner.

[8]Texas Comptroller of Public Accounts, *Revenue Estimates for Certification of Major Fund Expenditures* (Austin, Tex., September 20, 1995).

[9]Ibid., p. 3.

[10]Texas Comptroller of Public Accounts, *Special Financial Report: Sales and Franchise Tax Exemptions* (Austin, Tex., January 1993), p. 3.

[11]Texas Comptroller of Public Accounts, *Sources of Revenue Growth*, p. 15.

[12]Texas Comptroller of Public Accounts, *Revenue Estimates for Certification of Major Fund Expenditures*, p. 8.

[13]Texas Comptroller of Public Accounts, *State of Texas Revenue and Expenditure History: 1960-1993* (Austin, Tex., November 1993), p. 90.

[14]Texas Comptroller of Public Accounts, *Revenue Estimates for Certification of Major Fund Expenditures*,

p. 8.

[15]Ibid., pp. 3-4.

[16]Texas Comptroller of Public Accounts, *Sources of Revenue Growth: A History of State Taxes in Texas, 1972-1995* (Austin, Tex., 1994), p. 13.

[17]Texas Comptroller of Public Accounts, *Revenue Estimates for Certification of Major Fund Expenditures*, pp. 8, 13.

[18]Ibid.

[19]Ibid., p. 3.

[20]Texas Comptroller of Public Accounts, *Sources of Revenue Growth*, p. 15.

[21]Texas Comptroller of Public Accounts, *Revenue Estimates for Certification of Major Fund Expenditures*, pp. 8, 15, 27-28, 47, 50, 60.

[22]Ibid., pp. 15, 44.

[23]Ibid., pp. 4-8.

[24]Ibid., p. 8.

[25]Ibid., p. 21.

[26]Ibid., pp. 5, 21.

[27]Ibid.

[28]Ibid., p. 21.

[29]Ibid.

[30]Texas Comptroller of Public Accounts, *Fiscal Note Estimate.*

[31]Caleb Solomon, "In the Forecasting Game, Comptroller Stands Out," *Wall Street Journal* (September 13, 1995), p. T-2.

[32]Interview by Susan Proctor with Michael Reissig, Chief Revenue Estimator, Texas Comptroller of Public Accounts, Austin, Texas, October 31, 1995.

[33]John L. Mikesell, *Fiscal Administration: Analysis and Applications for the Public Sector*, 4th ed. (Belmont, Calif.: Wadsworth Publishing Co., 1995), p. 406.

[34]Ibid.

[35]Michael Totty, "Caterpillar's Lawsuit Could Cost State $1 Billion," *Wall Street Journal* (October 11, 1995), p. T-1.

[36]Ibid.

[37]Interview by Proctor with Reissig.

[38]Michael Totty, "Paging Firms Say New Tax Will Lift Rates," *Wall Street Journal* (November 15, 1995), p. T-1.

[39]Ibid.

[40]Ibid.

[41]Laura Johannes, "State Audits Leasing Firms over Sales Tax," *Wall Street Journal* (November 29, 1995), p. T-1.

[42]Ibid.

[43]Ibid., p. T-4.

[44]Texas Comptroller of Public Accounts, *Sources of Revenue Growth*, p. 15.

[45]State of Texas, *Report of the Staff Work Group on Property Tax Relief: Part II* (Austin, Tex., March 1996), p. 39.

[46]Ibid., p. 33.

[47]Michael Totty, "Study by Governor's Staff Lays out Options for Replacing Property Tax," *Wall Street Journal* (January 31, 1996), p. T-1.

[48]Ibid. The 1999 figures cited in the article were reduced by 5 percent to estimate 1998 revenue figures.

[49]Personal income levels are based on IRS statistics for adjusted gross income in Texas and projected at an average annual rate of 3.5 percent.

[50]State of Texas, *Report of the Staff Work Group*, pp. 50-54.

Chapter 3. Public Education

Introduction

Local, state, and federal relations concerning public education in Texas will take on added significance in the near future as the state seeks to decrease reliance on local school property taxes, decreases its regulation of education programs, allows for the creation of more charter schools, and faces probable reductions in federal funding.

Background

The passage of the Gilmer-Aikin Act in 1949 focused attention on the issue of equity and fairness in Texas education. This law created the Minimum Foundation Program, establishing a fiscal floor under fiscally disadvantaged schools. It eliminated the per capita system of school finance and adopted a plan based on an economic index measuring the ability of each district to raise revenue.[1] The new system of financing schools, however, left a large funding gap between property-rich and property-poor districts. This gap has been the subject of protracted litigation over the past 15 years.

In May 1984, several school districts filed a lawsuit claiming that the existing structure for funding the public school system was unconstitutional in several respects. Ultimately, the question of constitutionality hinged on the need for an efficient and equitable system providing school districts with substantially equal revenue for substantially equal tax effort at all levels of funding.[2]

In 1995, having laid to rest (however temporarily) the question of school finance, Texas lawmakers rewrote the Texas Education Code. The Ratliff-Sadler Act seeks to decentralize public education by reducing the scope and powers of the State Board of Education and the Texas Education Agency (TEA). It provides an alternate method of operating public schools by allowing a school district, a school campus, a group of parents or teachers, or a nonprofit organization or governmental entity to operate under a charter that frees it from most state regulations.[3]

The Texas system of public education currently serves an ethnically, culturally, and economically diverse group of more than 3.6 million schoolchildren.[4] Texas has 1,045 public school districts, 100 of which are considered to possess a significant wealth advantage over the rest, where such an advantage is attributable to a larger per capita property tax base. This reality is inextricably tied to the themes discussed in this chapter.

The following section describes Texas public education's current fiscal and budgetary status. It discusses the mechanism for disbursing public education funds as well as the options available to wealthy districts under which they must share their wealth.

Current Budgetary Status

The legislature appropriated $20.6 billion for public education in the 1996-97 biennium. This figure includes appropriations for the Foundation School Program (FSP), appropriations from the State Textbook Fund, and appropriations from funds accounting for federal dollars earmarked for public education in Texas.[5] In the 1996-97 biennium, 46 percent of total public education funding comes from the state, 46 percent from local sources, and 8 percent from the federal government.[6]

Current Funding Mechanism

The Foundation School Program is the formal mechanism through which the state allocates funds to local school districts. [7] The FSP's two components are State Aid (Tier I) and the Guaranteed Yield Program (Tier II). These appropriations are made from an ordered combination of two sources: the Available School Fund (ASF) and the Foundation School Fund (FSF). The legislature appropriated a total of $16.5 billion to school districts through the FSP in the 1996-97 biennium.

The ASF is funded by a combination of income from the Permanent School Fund (PSF), whose expendable income goes directly into the ASF, and one quarter of the revenues generated by the state motor fuel tax. According to state constitutional mandate, the ASF must be distributed to each county on the basis of scholastic population. That portion of state funds committed to Tier I and Tier II not provided by the ASF comes from general revenue appropriations, which are accounted for in the Foundation School Fund.

State Aid (Tier I) is the FSP's major component. It is intended to cover the costs of an educational program that meets state accreditation standards. The two types of aid are regular program aid (calculated by a number of formulas) and categorical aid, or aid to the various educational program categories subject to different funding formulas (vocational education, special education, gifted education, etc.). Each biennium, this tier of the FSP is subject to cost-of-education index (CEI) adjustments over and above the statewide basic allotment. The basic allotment is established by the Foundation School Fund Budget Committee. To receive state funding for Tier I, school districts must levy a property tax rate of at least 86¢ per $100 of assessed property valuation within districts. If revenues generated from the minimum 86¢ rate are insufficient to cover both regular program aid and categorical aid, then the state pays for the difference out of an appropriate combination of ASF apportionment and general revenue appropriations.

The Guaranteed Yield Program (Tier II) is intended to provide equal revenues for enrichment beyond the basic Tier I program. This aid is aimed at low-wealth school districts making a tax effort beyond the basic Tier I program. Under Tier II, districts making a tax effort beyond the 86¢ per $100 of assessed property valuation are guaranteed $21.00 (set by the most recent appropriations bill and slightly over the $20.55 set by current statutes) per penny over the 86¢ tax rate, up to a rate of $1.50 per $100.00 of assessed property valuation. If a district's tax base is too small to yield revenues of $21.00 per penny of property tax rate per pupil, then the state will fund the district up to the $21.00

level. For example, if a district has a tax rate of $1.00 per $100.00 of assessed valuation, and this only generates revenues of $15.00 per penny per pupil, the state will give the district $91.70 per pupil (14 x $6.55, or 14¢ above the 86¢ rate, multiplied by the difference between $21.55 and $15.00). Tier II guaranteed yield is funded by the same combination of revenue sources as Tier I state aid.

Additionally, to achieve the goal of what is usually termed "substantially equal access to equal revenues per pupil," the legislature enacted a set of requirements giving property-rich school districts five options to reduce their overall wealth advantages.[8] Each of the options is designed to reduce districts' property wealth to $280,000.00 per weighted average daily attendance (WADA). Each option is designed to achieve equal wealth per pupil in average daily attendance (ADA) across districts.[9] The options apply directly to about 100 of the wealthiest of Texas' 1,045 school districts and are listed below.

1. Consolidation with other districts.

   A wealthy district simply merges with another less wealthy district, thereby automatically combining property tax bases to a level below $280,000 per WADA.

2. Tax base consolidation.

   A wealthy district merges its tax base with that of a less wealthy district. This has the same fiscal effect as total consolidation of districts and thus equalizes wealth per WADA as well.

3. Transfer of property.

   A wealthy district can shift property away from its tax base to a less wealthy district's tax base, thus reducing the wealthier district's property wealth level to $280,000 per WADA.

4. Education of nonresident students.

   A wealthy district can pay for the education of students in a less-wealthy district in an amount sufficient to reduce the wealthier district's property wealth level to $280,000 per weighted average daily attendance.

5. Payments to the state.

   Under this option, the wealthy district can purchase "phantom WADA" from the state by making payments to the state sufficient to reduce the district's wealth per WADA to $280,000.

With only one exception, in which a district chose the transfer of property option, wealthy school districts in Texas all have chosen one of the latter two options.

The state commissioner of education believes that the question of equity in public school funding has been adequately addressed, and the courts have agreed with him thus far.[10]

The question of the *adequacy* of public education is the next hurdle the state must overcome. Changes in federal funding along with growing pressures on the education system will demand greater increases in spending on public education by the State of Texas. These and other trends are examined in the next section.

Current Trends Affecting Public Education

Demographics

Public education enrollment will continue to grow, but as our population ages, student enrollment per capita will decrease slightly.[11] The most recent data available indicate that during the 1993-94 school year, the state's student population was 14.3 percent African-American, 35.5 percent Hispanic, 47.7 percent Anglo, and 2.5 percent Asian or Native American. The 1990-91 school year was the first year that ethnic minority children were in the majority in Texas' public schools.[12] And no ethnic group is growing faster than Hispanics.

As a result, Hispanic students account for 70 percent of annual enrollment growth.[13] Likely consequences of this demographic change include increased demand for bilingual teachers and the development of innovative and effective bilingual programs. Addressing the needs of Hispanic students may require additional financial resources, but sources of financial support for such programs may be declining. Federal education programs targeting students with special learning needs as well as students from low-income families face potential cuts. If such federal programs as bilingual and special education and safe and drug-free schools suffer funding cuts, Texas legislators will be challenged to replace those funds and/or find additional, innovative methods for addressing the needs of Hispanic students.

Decentralizing Authority

The belief that local school districts know what is best for their students has translated into a shift in policy toward empowering localities to choose how to educate their children. The Ratliff-Sadler Act facilitates decentralization by minimizing the powers of the State Board of Education and the Texas Education Agency. The law provides for three types of home-school charters and emphasizes parents' rights and responsibilities to be fully involved in their children's education. Legislators, educators, and parents will be carefully monitoring the creation, development, and success of charter schools over several years. Legislators hope charter schools will provide Texas with potential cost savings as well as improved student performance and increased parent satisfaction. Costs, academic performance, and parental satisfaction with charter schools likely will affect future support for education policies that decentralize authority.

In 1996, the U.S. Department of Education awarded Texas Ed-Flex status. The Ed-Flex program was created by Congress as a part of the Goals 2000: Educate America Act. Ed-Flex status gives the state commissioner of education the authority to grant three-year statewide waivers of federal laws or regulations sought by individual school districts. It is

expected that the use of Ed-Flex waivers will allow public education in Texas to be less bureaucratic. For example, using Ed-Flex waivers, Texas could combine federal and state monitoring requirements, thereby reducing paperwork and time spent complying with federal monitoring regulations. Texas educators hope that less bureaucracy will mean lower costs for the state and for local school districts. Texas educators also anticipate that Ed-Flex waivers will allow local officials to tailor educational programs to fit the needs of their local communities.

Federal Funding

Though federal money comprises only 8 percent of all public education funding in Texas, federal funding is far from insignificant.[14] Texas received $1.58 billion for federal and nonstate-funded programs in fiscal year 1995.[15] Federal education programs target students with special learning needs and students from low-income families. Such programs include Title I, directed toward districts with high concentrations of low-income families; safe and drug-free schools Programs; special education; and the Career and Technology Education Program among others.

In late April, Congress finally passed the federal Labor-Health and Human Services appropriations bill for fiscal year 1996, which funds education programs. Like several other programs important to Texas, Title I funding remained essentially level. However, in the recent budget debate, many programs were targeted for significant cuts. Table 3.1 contains current federal funding estimates for selected education programs.

Table 3.1

Federal Funding of Selected Education Programs

(in millions of dollars, rounded)

Program	FY 1995	FY 1996
Title I (Basic)	5968.0	5982.0
Goals 2000	362.0	340.0
(State/Local Grants)		
Safe and Drug-Free Schools (State Grants)	441.0	441.0
Vocational Education (State Grants)	973.0	973.0

Source: Education Funding Research Council, *Guide to Federal Funding for Education Budget Update Supplement* (Arlington, Va., June 1996).

The three federally funded education programs with the largest budgets are Title I, the Individuals with Disabilities Education Act (IDEA), and Medicaid. Title I funding is the

largest source of federal dollars for public education in Texas. In fiscal year 1995, it provided more than $628 million for five programs that provide supplemental resources to districts to help schools with high concentrations of students from families with low incomes.[16]

IDEA helps school districts and regional education service centers ensure that students with disabilities are provided a free, appropriate public education as required by federal law. This program received more than $163 million in federal funding for fiscal year 1995.[17]

In recent years, public education in Texas has become linked to federal Medicaid funding for low-income and disabled individuals. Medicaid reimbursements have provided another source of revenue for special education services for Medicaid-eligible students. How Medicaid funding is handled by both Congress and the Texas Legislature will affect revenues in this area.

While the potential cuts to federal education programs represent a relatively small amount of the state's total education budget, those cuts would be felt by school districts throughout Texas. Specifically, districts with high proportions of students from low-income families and with large numbers of students with special education learning needs would be hardest hit by such cuts.

If cuts in federal education programs become a trend, Texas will have to take action. Ethnic and racial minority students are becoming the majority in many Texas public schools. These students and their school districts are the primary beneficiaries of federal education programs. To prevent a crisis in Texas public education, officials must replace any lost federal funds or provide the necessary programs.

Policy Issues

Analysis of the current funding mechanism, budgetary status, demographic trends, and potential federal funding cuts raises many issues for Texas educators and lawmakers. A summary of some of these issues follows.

State, local, and federal relations will become more important as alternative state financing methods are considered and federal funds are reduced. To the extent that potential cuts in federal funding continue into the next century and current trends in public education demographics hold, state policymakers will confront an unsettling dilemma: a student population with multiple learning needs, yet fewer resources to meet those needs.

Current funding for the Foundation School Program would be affected by increased demands for appropriations arising from the FSP formulas. Specifically, if the funding formulas called for greater appropriations for a given biennium, and income from the Permanent School Fund and revenues from the occupation and motor fuel taxes remained constant, then general revenue appropriations for public education would have to increase in amounts sufficient to cover the projected increase. In the face of limited general revenues and increasing enrollment in Texas public schools, this scenario is not unrealistic.

Consequently, the legislature and the TEA must make certain that appropriate mechanisms are in place to allow for this contingency.

The State of Texas uses a performance budgeting system in which dollars are appropriated for agencies and programs based on anticipated units of outcome and output. Money is appropriated to the FSP according to legislatively established formulas while performance measures are being developed for the FSP. Therefore, the FSP is incompatible with the state's present budgeting system. The state might consider redeveloping the FSP funding formulas in such a way that appropriations for public education are tied to some extent to outcome and output measures.

Policy Options

Policy Options with a Direct Impact on General Revenue

Taking action to address public education issues will be a challenge for Texas legislators, given the many budget issues facing the state. In light of the state's budgetary predicament, these policy options appear to be the most realistic and viable.[18]

1. Raise public schoolteachers' salaries to the national average.

   Biennial cost $2.64 billion

   In the 1994-95 academic year, Texas schoolteachers earned an average of $31,223 a year; the national average was $36,874. If teachers' salaries were appropriated through the FSP, this would have represented approximately a 17 percent increase in the FSP for the 1994-95 academic year.[19] Available data indicate that the gap between teachers' average salaries in Texas and the nation will remain approximately the same through the 1998-99 biennium.

2. Raise expenditures per student to the national average.

   Biennial cost $3.42 billion

   In the 1994-95 academic year, Texas spent an average of $5,006 per student; the national average was $5,472. If this amount were appropriated through the FSP, this would have represented approximately a 20 percent increase in FSP appropriations for the 1994-95 academic year.

3. Increase the compensatory education weight.

   Biennial cost $262.0 million

   The compensatory education weight is an additional allotment of funds that targets educationally disadvantaged children. The weight currently is set at 0.2. To replace $131 million in federal funding cuts during the next school year by adjusting the compensatory education weight upward, for example, the weight would have to be

increased to 0.22. Assuming that compensatory education funds are spent on their targeted population, this policy option is desirable because it would address the population most affected by the potential cuts in federal funds.

Policy Options without a Direct Impact on General Revenue

4. Increase the amount of property tax revenue recaptured from wealthy school districts.

   This would involve redefining eligibility to increase the number of schools defined as wealthy. To replace $131 million in federal funding cuts during the next school year, for example, the equalized level of property wealth would drop from $280,000 to $245,000 per weighted average daily attendance. This action would cause approximately 70 districts to lose revenue.

5. Use Texas' new Ed-Flex status to mitigate the effects of any cuts in federal funds.

   Ed-Flex waivers could be used to redefine eligibility for certain programs, thereby reducing the amount of services provided by the state.

Conclusion

The Foundation School Program needs to become more flexible in two significant ways: (1) it must be responsive to large differences between public education expenditures in Texas and in other states, and (2) because the FSP represents such a large proportion of general revenue appropriations, steps ought to be taken to make the FSP more amenable to Texas' current performance budgeting system. Otherwise, the state's objective of tying appropriations to performance indicators will be difficult to achieve.

The interaction between federal funding trends and the changing demographics of Texas' public school children may result in significant challenges for educators and lawmakers. Facing reductions in funds for programs serving students with multiple learning needs and students from low-income families, state policymakers may have to find new ways to serve this population. Furthermore, Texas will need to assess carefully whether decentralizing power and authority to local communities actually improves the quality of education received by its public schoolchildren.

Notes

[1]Supreme Court of Texas, no. 94-0152, argued May 25, 1994; available from gopher://www/tea.state.tx.us:70/11/juris/edgewood (cited October 30, 1995); INTERNET.

[2]Ibid.

[3]Texas Education Agency, *An Overview of Senate Bill I, The Ratliff-Sadler Act, As Enacted by the 74th Legislature* (May 1995); available from gopher://www.tea.state.tx.us:70/00/juris/sb1/summary (cited September 30, 1995); INTERNET.

[4]Texas Education Agency, *Academics 2000; available from* http://www.tea.state.tx.us:70/0/A2000/a2000 (cited October 30, 1995); INTERNET.

[5]Ibid.

[6]Texas Education Agency, *Snapshot, 1993-1994* (Austin, Tex., Winter 1994).

[7]Material for this section was taken primarily from Legislative Budget Board, *Fiscal Size Up: 1994-95 Biennium, Texas State Services* (Austin, Tex., 1994), pp. 4-2–4-13 passim; Legislative Budget Board, *Summary of Conference Committee Report on House Bill I, Recommendations for the 1996-97 Biennium* (Austin, Tex., May 1995); and personal and telephone interviews by Molly Bolte and Dan Galperin with Joe Wisnoski, Coordinator for State Funding, and other officials and consultants with the Texas Education Agency, Austin, Texas, January-February 1996.

[8]The term "wealth advantage" means wealth deriving from local property tax revenues, because direct state aid is theoretically equal, relative to tax effort, under the FSP.

[9]Note that "equal wealth" technically means "equal wealth for tax effort," where "tax effort" is defined as the property tax rates imposed by school districts. Mills represent cents per $100 valuation for property tax purposes. For example, if District A has a tax base of $1 million and District B has a tax base of $100,000, but A taxes at 15 mills and B at only 10 mills, "equal wealth" would be achieved if the tax bases were equalized at $500,000 each and A continued to tax at 15 mills and B at 10 mills. Both districts would then have the same wealth by which their tax rates are multiplied to produce a tax levy, and thus can be said to have equal wealth for their tax efforts.

[10]Class presentation by Dr. Michael A. Moses, Texas Commissioner of Education, at the Lyndon B.

Johnson School of Public Affairs, Austin, Texas, November 14, 1995.

[11]Legislative Budget Board, *Summary of Conference Committee Report on House Bill I*, p. III-1.

[12]Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1996), p. 6-7.

[13]Legislative Budget Board, *Summary of Conference Committee Report on House Bill I.*

[14]Texas Education Agency, *Snapshot.*

[15]Texas Education Agency, *Program Budgets for Federal Funds, Fiscal Year 1995-1996* (Austin, Tex., 1995), p. 1.

[16]Ibid.

[17]Ibid., pp. 1, IV-141.

[18]The data for the policy options addressing the replacement of federal funds were taken from discussions with David Dunn, Director of the Public Education Team at the Legislative Budget Board, and with Debra Haas, member of the Public Education Team at the Legislative Budget Board, in February and April 1996.

[19]The data for the policy option related to teachers' salaries were taken from an interview with Carey Hedgcock, statistician for the Texas Education Agency, on March 26, 1996.

Chapter 4. Higher Education

Introduction

Accessibility and affordability of higher education are major concerns of students, university administrators, and state legislators. Higher education institutions in the United States are the envy of the rest of the world, with Texas playing a significant role in fostering that strength and dominance. But how does Texas ensure that the quality of its higher educational institutions will continue to improve? Texas must continue to fund and support its higher educational institutions at least at its current levels, but it also must stay abreast of several trends affecting Texas higher education, including rising student enrollment, indirect cuts in federal support for higher education, and the declining numbers of patients in the state's teaching hospitals. Texas should consider several options to deal with these trends, from increasing general revenue funding for certain programs to raising tuition.

Background

The public higher education system in Texas is one of the largest and most extensive in the nation, with 50 public community/junior college districts, 35 general academic institutions, three dental and seven medical schools, three lower division institutions, and one technical college with three main campuses and four extension centers. Additionally, Texas is home to 38 private senior colleges and universities, two private junior colleges, one private medical school, and one accredited independent law school. In 1995, more than 925,000 students were attending colleges and universities in Texas, 90 percent of them in public institutions.

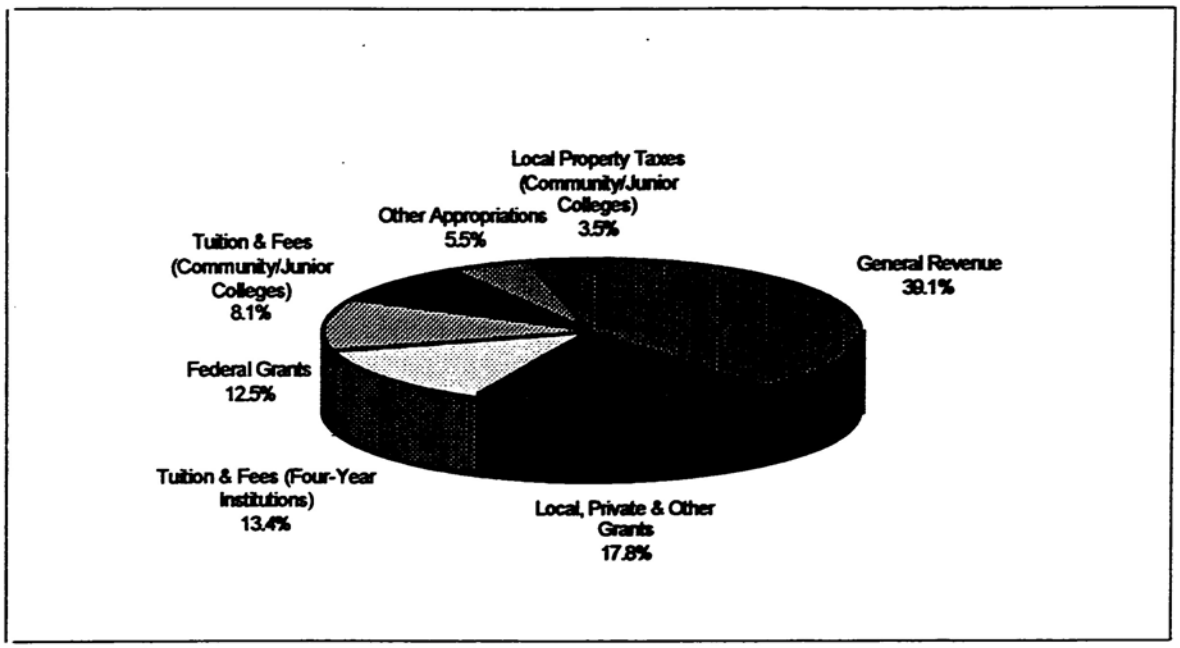
The General Revenue Fund will provide 39.1 percent of the funding for higher education in the 1996-97 biennium. The remaining sources are local and private grants, 17.8 percent; all other tuition and fees (four-year institutions), 13.4 percent; federal grants, 12.5 percent; junior colleges' tuition and fees, 8.1 percent; other legislative appropriated funds, 5.5 percent; and local property tax revenue for community/junior colleges, 3.5 percent (see figure 4.1).[1]

Funding for building construction comes from two constitutionally dedicated funds: the Permanent University Fund (PUF) and the Higher Education Fund (HEF).

The PUF was established in 1876 as a separate public endowment of more than two million acres in land grants. Mineral and surface use income from these lands is invested in corporate and government securities. The dividend and investment income is deposited in the Available University Fund, whose moneys are distributed to the institutions in the University of Texas and Texas A&M systems.

Figure 4.1

Revenue Sources for Texas Higher Education, 1996



Source: John O'Brien, Texas Legislative Budget Board, *Role of Texas Legislature in Higher Education: Presentation to Chinese Higher Education Policymakers* (Austin, Tex., October 1995), p. 9.

The HEF was created in 1984 for the benefit of colleges and universities not covered by the PUF. Investment income from the HEF is distributed to these non-PUF institutions based on space deficits, facility conditions, and institutional complexity. When the HEF reaches $2 billion, appropriations to it will cease.[2]

Tuition and fees charged to students are clearly important to students and the institutions they attend. Institutions increasingly rely on fees to pay for construction projects. Charles Franklin, vice president for business affairs at the University of Texas at Austin (UT), said that UT is relying more on the general fee for building construction because state funding is decreasing and PUF bond proceeds are going to be "frozen."[3] Additionally, students are paying higher tuition and fees. In 1995, the 74th Texas Legislature raised tuition $2 per semester hour annually until the 2000-01 academic year, when undergraduate resident tuition will reach $40 per semester hour.[4] While the rise in tuition and fees is significant to students and their parents, Texas public higher education is still a bargain compared to other states. Texas ranks 42nd in the nation in resident undergraduate tuition and fees, and 45th in the nation in resident graduate tuition and fees.[5]

Current Status and Trends

Equal Access to Public Higher Education

As with all other areas of government, public higher education must adapt to meet the needs of the growing and changing Texas population. By 2000, the state's population is expected to exceed 19 million; 44 percent of all Texans will be ethnic minorities.[6] The Higher Education Coordinating Board expects 908,000 students in public higher education institutions by 2000. Hispanics and blacks will account for 33.6 percent of these students.[7]

Texas must ensure access to higher education for all its citizens. One of the ways Texas is working to provide an affordable, accessible higher education for its residents is through the Texas Tomorrow Fund. This program took effect on January 2, 1996. It allows Texas families to purchase their children's future college education by locking into today's tuition prices. Money placed in the fund will be invested and earn interest during the years before the student goes to college in order to yield enough to pay for the student's education. This is not a guarantee of admission, however, and all regular entrance requirements must be met. In addition, if the student chooses not to attend a Texas college or university, then the money is refunded without interest.

According to State Comptroller John Sharp, the major difficulty in designing a prepaid tuition program is "to structure the program to benefit all citizens. A poorly designed program could be viewed as a state guarantee—and potentially a subsidy—primarily for upper-income families."[8]

The Texas Tomorrow Fund is part of the state's effort to provide access to higher education. But, if successful, the plan may help reduce the dependence on other sources of financial aid and make attending college a viable option for more students.

Growth in Number of Students Attending Community and Junior Colleges

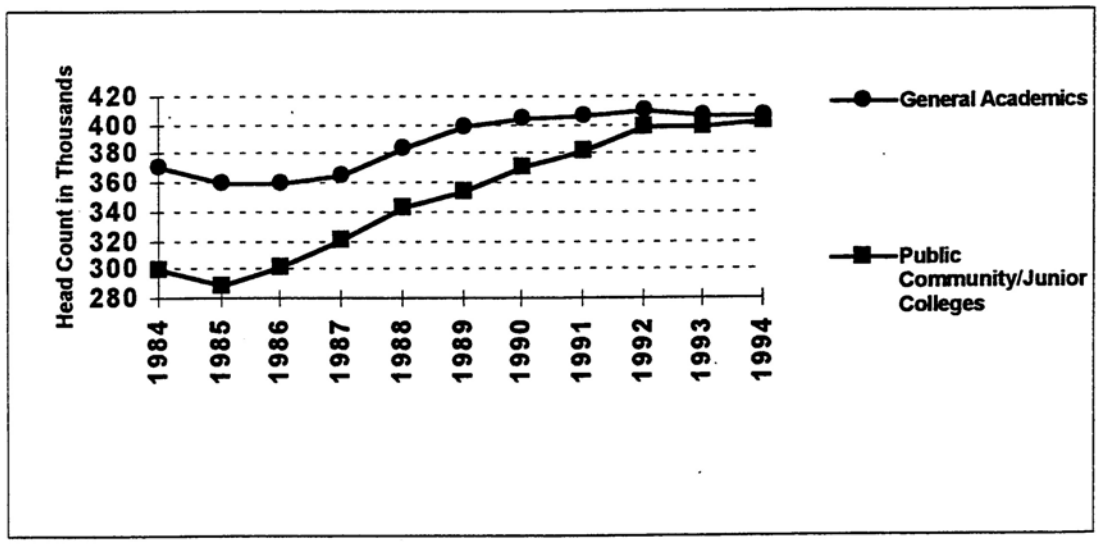
Community and junior colleges in Texas are experiencing more growth in student population than four-year institutions. While enrollment at public universities has remained relatively constant over the past decade, since 1986 community and technical college enrollment has grown from roughly 300,000 students to more than 400,000 in 1996 (see figure 4.2).[9]

In 1995, the legislature appropriated $500,000 to the coordinating board and $5 million to these institutions to address this dramatic increase in enrollment.[10] These institutions must hire more faculty and administrators, expand classes, and provide facilities to accommodate additional students.

One of the funding sources for community college districts is the local property tax, although this revenue comprised only 3.4 percent of total higher education revenue for the 1996-97 biennium.

Figure 4.2

Ten-Year Enrollment Growth, Head Count Comparison of Public Community Colleges and General Academic Institutions



Source: Texas Higher Education Coordinating Board, "Statistical Reports," as cited in Legislative Budget Board, *Trends in Texas State Government Finances, 1982 through 2005* (February 1995), p. 113.

Texas State Technical College System

The Texas State Technical College (TSTC) system was created in 1965 to meet the changing needs of Texas business and industry. Through its three main campuses and four extension centers, TSTC provides one- and two-year college programs in highly specialized technological and vocational fields to approximately 7,600 students. Its mission is "to support the economic development of Texas by offering occupation-oriented programs to meet statewide industrial and technological workforce needs. ...TSTC [emphasizes] the offering of vocational and technical programs which are highly specialized, advanced and emerging, or capital intensive."[11] Funding for TSTC primarily comes from general revenue appropriations, unlike local community college districts, which receive local property tax revenue.

The primary issue that Lieutenant Governor Bob Bullock instructed the Senate Education Committee to address during the 1995-96 interim is the future of the Texas State Technical College system. Concerns regarding duplication of missions and courses offered are a "source of ongoing disputes among TSTC, community colleges, and the Texas Higher Education Coordinating Board."[12] In January 1996, the Senate Education Committee began its review of TSTC by asking about TSTC's original mission, alternative methods of financing the technical schools, and the role of community colleges.[13]

Senator Bill Ratliff, chairman of the Senate Education Committee, believes that some of the problems TSTC is facing have surfaced as a result of legislative action. Ratliff has stated that the "Legislature has put TSTC in a position of having to offer courses that were not part of the TSTC mission because we haven't funded high-tech courses adequately. If we can't fund [TSTC] the way it ought to be done, then we need to rethink the entire system."[14]

Quality of Public Higher Education

While providing access to growing numbers of students, Texas also must maintain the quality of public higher education. Class sizes have been increasing in recent years, and institutions are relying more on part-time faculty to teach classes. Dr. Kenneth Ashworth, commissioner of higher education, sees both of these trends diminishing the quality of education in Texas. He would like to reverse the trend toward increasingly larger class sizes. In addition, he recommends curtailing part-time faculty, increasing the number of undergraduate courses taught by tenured faculty, and increasing faculty salaries.[15]

Loss of Educational and General Income for Health-Related Higher Education Institutions

Texas' public teaching hospitals serve a large number of low-income patients through the Medicaid Disproportionate Share Hospital Program (DSH). This program is an effort to compensate hospitals that serve large numbers of poor and uninsured patients for any losses they incur from serving them. The DSH is at risk of elimination by the federal government. This could mean serious financial problems for those hospitals receiving DSH funding, especially smaller hospitals.[16] The Clinton Administration proposed cutting DSH funds by an estimated $239 million in fiscal year 1997.[17]

Accompanying this decline in DSH funding is the increase in managed health care plans. The shift to managed health care for Medicaid patients has greatly reduced the number of Medicaid recipients seeking care at health-related higher education institutions. This patient loss diminishes the learning opportunities for students at these teaching hospitals who would have worked with these patients and reduces a major source of hospital revenue. The decrease in educational and general income for all health-related institutions is estimated at $89.3 million for the 1996-97 biennium. Lost patient income at M. D. Anderson Cancer Center alone accounts for $50.6 million of the projected total loss.[18] These two trends—loss of DSH funding and increased reliance on managed health care—may affect the ability of teaching hospitals to provide services for uninsured patients as well as maintain quality instruction for students.

Legislative/State Budget Issues

The Texas Legislature continues to be generous to higher education with adequate funding for its programs. Examples of financial support from the 1995 legislative session include a $250 million increase in funding for the HEF, authority for general academic institutions to

retain $44.6 million in tuition income, increased utility funding of $26 million, and increased construction debt service funding of $30.9 million.[19]

On November 7, 1995, Texas voters approved Proposition 1 with 65 percent of the vote. This proposition authorized the sale of $300 million in general obligation bonds by the Higher Education Coordinating Board to meet demands for student loans through the Hinson-Hazlewood student loan program. Hinson-Hazlewood is a self-supporting loan program open to all Texas residents attending public or private colleges and universities. The program has loaned more than $900 million to more than 250,000 students since 1965 by selling $660 million in general obligation bonds. Hinson-Hazlewood loans help students who cannot or do not get federal loans and are mainly used to assist middle-income borrowers with cash flow problems.[20] Many students rely on loans to cover rising tuition costs. More than 47.5 percent of all Texas public college and university students received some type of financial aid in fiscal year 1993, and the use of loans increased from 50.1 percent of the financial aid mix in fiscal year 1990 to 62.7 percent in fiscal year 1993.[21] Demand for loans has risen from $12 million in fiscal year 1989 to $90 million in fiscal year 1994. The $300 million in bonds will provide $80 million in loans annually for four to five years.[22]

Federal Role in Higher Education

The federal government provides no direct assistance to the states for higher education. Indirectly, however, it provides research grant dollars to colleges and universities and financial aid to students.

Federal Research Programs

A significant area of federal support for higher education is research grants. In fiscal year 1993, of the $1.14 billion in research expenditures to Texas public institutions, more than 52 percent came from the federal government, 24 percent from the state, and the remainder from business, industry, and other private sources.[23] As federal research money declines, a valued source of revenue for universities may disappear. This is one of the greatest threats to the continuing dominance of this country's higher education institutions in the global marketplace.

State Research Programs

In 1987, the Texas Legislature created two programs to provide research grants to Texas colleges and universities: the Advanced Research Program (ARP) and the Advanced Technology Program (ATP). The ARP is a broad-based, basic research program providing funds for numerous diverse projects. In 1995, this program was funded at $20.2 million.[24] The ATP is "devoted to research with a technological objective and a long-term economic goal. ...It is designed to promote the state's economic growth and diversification by increasing the number and quality of scientists and engineers in Texas."[25] In 1995, its funding allocation was $36.1 million. These state research programs provide educational opportunities for more than 3,000 undergraduate and 5,600 graduate students. A third type

of state research program is the Development and Transfer Grants Program, funded at $4.2 million in 1995. These grants require matching funds from private industry.[26]

Student Loans

Although financial support for higher education students has been relegated mainly to the individual states, the federal government does play a significant role by supplying student loans. Through the Federal Family Education Loan Program and Pell Grants, the federal government provides access to college funds for thousands of students. In 1993-94, Texas received nearly $1.5 billion in student aid from the federal government; the state provided only $183 million.[27] This federal support was threatened in the 1996 budget showdown in Washington when cuts as deep as $10.1 billion in student aid over a seven-year period were proposed in original House legislation.

The deep cuts have not materialized, however, for this year. Although the states, including Texas, do not have to deal with a serious decline in the availability of financial aid, it is an issue that must be monitored in the future due to students' heavy reliance on outside sources of aid.

Policy Options

In light of the trends discussed above, we recommend the following policy options as those best addressing the major problems facing Texas higher education today: the potential losses of federal funding and state budget constraints.

1. Increase state funds available to students.

   Biennial cost $206 million

   The number of Texas residents seeking higher education will increase with general population growth. At the same time, as the state's minority population increases, a corresponding increase in the number of minorities in higher education is anticipated. Because poor and minority students are more likely to face economic barriers to higher education, the state government should focus on increasing sources and amounts of financial assistance to encourage equal opportunity for all students to pursue higher education.[28]

   More money for loans can be made available by increasing funding for the Hinson-Hazlewood program over a four-year period. This level of funding should be increased to provide more than $100 million each year (adjusted for inflation and tuition increases) to meet the anticipated increase in demand for loans. Hinson-Hazlewood loan administrators can more actively target minority students to receive Hinson-Hazlewood loans in order to meet these students' anticipated needs for college funding.

Additionally, Texas should provide more grant money to its resident students. Texas is well below the national average in the amount of grant money that it provides students. The legislature should create a trust fund, or endowment, similar to the Higher Education Fund, to pay for these grants. This would be a student grant fund that could be endowed by the legislature. Once it reaches an agreed-upon level sufficient to generate generous amounts for grants, the appropriations would cease. Grants would continue to be awarded to students from the interest income the trust generates.

2. Increase research funding to the Advanced Technology Program and the Advanced Research Program.

   Biennial cost $60 million

   The state government's $285 million contribution to research was less than 25 percent of the total research funds spent in Texas in 1993 ($1.14 billion) and less than half the amount that the federal government provided ($606 million).[29] Because federal research dollars are likely to decline with the demands for a balanced budget, Texas should increase its funding for university research projects in the next biennium to partially fill the gap. Unfortunately, one of the difficulties involved in budgeting for higher education is the near-impossibility of estimating how much federal funding may be lost. Various federal departments support higher education, and determining how much each will cut is extremely difficult. While state research spending likely will never equal federal research spending, the state should recognize and fund its commitment to higher education research. Besides providing educational opportunities to graduate and undergraduate students, public research money also helps Texas public colleges and universities recruit and retain quality faculty members and attract private research dollars.

3. Raise resident undergraduate tuition.

   Projected biennial revenue $570 million

   In the 1994-95 academic year, Texas resident undergraduate tuition was $1,659 per year, only 69 percent of the national average of $2,402 per year. Texas graduate tuition rates averaged $1,106 per year, roughly 43 percent of national levels.[30] While this has been a great benefit to Texas residents, it is not entirely practical. To offset some shortages of both federal and state funds, and to make higher education in Texas more equitable with other states, Texas should raise its tuition to 90 percent of the national average, or $2,162 per year. The rationale for this figure is the fact that per capita personal income in Texas is 90.2 percent of the national average.[31] The increase could be phased in over a five-year period but ought to reach 90 percent of the national average by 2005. Texas residents should be able to afford higher tuition rates that approach the national average yet remain within the percentage range of average per capita personal income.

For those students now facing financial difficulties attending college, the increased access to loans and grants recommended in Option 1 should provide adequate financial assistance for tuition increases. Increased loans and grants could offset any potential decline in enrollment that the tuition increase might cause.

The money raised from increasing resident tuition should be used by each institution to provide student benefits, such as smaller class sizes, career guidance counseling, on-campus tutoring services, and minority outreach programs. To ensure this, some dedication must be mandated by the state legislature.

4. Instruct the coordinating board to study privatization.

The Higher Education Coordinating Board should study privatizing aspects of the Texas higher education system with a goal of short- and long-term cost savings. Privatization is a method of using private industry to bring competition and cost savings to areas normally under government control. While privatization is not appropriate or cost-effective in all areas, it can result in substantial cost savings in some areas of public services. A two-year study using consultants, experts, state government, and university resources could produce detailed and professional research into privatization measures that could save Texas money in the operation of higher education. The coordinating board has conducted special studies at the request of the legislature in the past. This study could be conducted and presented to the legislature on or before August 31, 1998.

Conclusion

With nearly half of its higher education funding coming from the General Revenue Fund, Texas has a great deal of control over its system of public higher education. Consequently, our policy options have outlined actions that the Texas Legislature can readily take. These policy options address the critical issues; they are feasible options that Texas can implement now. But at the same time, Texas needs to remain vigilant in monitoring federal budget issues because it may need to react quickly to drastic federal funding cuts. Texas should anticipate any potential reductions and be prepared to respond accordingly.

Notes

[1]John O'Brien, Texas Legislative Budget Board, *Role of Texas Legislature in Higher Education: Presentation to Chinese Higher Education Policymakers* (Austin, Tex., October 1995), p. 9.

[2]Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1996), p. 6-33.

[3]Tom Vaughn, "Moffett Did Not Ask for Building Naming," *Daily Texan* (November 28, 1995), p. 1.

[4]Office of the Governor, State of Texas, "The Texas Budget: 1996-1997," p. III-4 (draft).

[5]Higher Education Coordinating Board, State of Washington, "1994-95 State Ranking of Tuition and Fees at Senior Level Institutions," distributed by the Texas Higher Education Coordinating Board, 1995 (mimeographs).

[6]Texas Higher Education Coordinating Board, *Strategic Plan: 1995-1999* (Austin, Tex., June 1, 1994), p. 7.

[7]Texas Higher Education Coordinating Board, *Enrollment Forecasts 1995-2010: Study Paper 27* (Austin, Tex., January 1995), pp. 3, 45-46.

[8]Texas Comptroller of Public Accounts, *Gaining Ground: Progress and Reform in Texas Government* (Austin, Tex.: Texas Performance Review Agency), p. 148.

[9]Texas Higher Education Coordinating Board, "Statistical Reports," as cited in Legislative Budget Board, *Trends in Texas State Government Finances, 1982 through 2005* (February 1995), p. 113.

[10]Office of the Governor, "The Texas Budget," p. III-11.

[11]Letter from Cecil L. Groves, Chancellor of Texas State Technical College System, State of Texas, to Senator Bill Ratliff, December 29, 1995.

[12]Lawrence F. Alwin, Office of the State Auditor, *A Management Control Audit of the Texas State Technical College System*, SAO report no. 4 (Austin, Tex., November 1993), p. 4.

[13]Letter from Senator Bill Ratliff, Texas Senate, to Chancellor Cecil L. Groves, Texas State Technical College, November 17, 1995.

[14]James E. Garcia, "Technical College Gets Hard Look, Some Support," *Austin American-Statesman* (January 18, 1996), p. B-1.

[15]Class presentation by Dr. Kenneth Ashworth, Texas Commissioner of Higher Education, at the Lyndon B. Johnson School of Public Affairs, Austin, Texas, November 21, 1995.

[16]Sandy Lutz, "L.A. Ponders Novel Way to Plug Its 'Dispro Hole'," *Modern Healthcare* (June 27, 1994), p. 62.

[17]Legislative Budget Board, State of Texas, *Federal Funds Watch*, vol. II, no. 4 (February 22, 1996), p. 3 (newsletter).

[18]Legislative Budget Board, *Summary of Conference Committee Report on House Bill I, Recommendations for 1996-97 Biennium* (Austin, Tex., 1995), p. III-10.

[19]Office of the Governor, "The Texas Budget," p. III-4.

[20]Ibid.

[21]Texas Higher Education Coordinating Board, *Facts on Higher Education in Texas, 1995*. (Pamphlet.)

[22]Texas Higher Education Coordinating Board, "Hinson-Hazlewood College Student Loan Program," October 1995 (mimeographs).

[23]Texas Higher Education Coordinating Board; available from http://192.16.72.17:70/R204538871m/facts/factbroc.txt (November 29, 1995); INTERNET.

[24]Texas Higher Education Coordinating Board, *Advanced Research Program/Advanced Technology Program: 1995*. (Fact sheet.)

[25]Texas Higher Education Coordinating Board; available from http://192.16.72.17:70/r2045-3887-1m/facts/factbroc.txt.

[26]Texas Higher Education Coordinating Board, *Advanced Research Program/Advanced Technology Program.*

[27]Texas Higher Education Coordinating Board, *Trends in Student Aid* (Austin, Tex., 1994).

[28]Texas Higher Education Coordinating Board, *Strategic Plan*, p. 8.

[29]Texas Higher Education Coordinating Board; available from http://192.16.72.17:70/R2045-3887-1m/facts/factbroc.txt.

[30]Higher Education Coordinating Board, State of Washington, "1994-95 State Ranking of Tuition and Fees."

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Chapter 5. Health and Human Services

Introduction

Any consideration of how to match expected revenues to projected expenditures must include an examination of spending for health and human services in Texas. Spending by the 13 health and human services agencies in Texas represents the second largest expenditure category of the Texas state budget. Total all-funds appropriations (general revenue, federal funds, and other funds) for all 13 health and human services agencies for the 1996-97 biennium were $26.4 billion, a 10 percent increase over the previous biennium. The 1996-97 appropriation represents 33 percent of the all-funds budget, 66.4 percent of the federal funds budget, and 23.4 percent of the general revenue budget.[1] Whether considering state dollars alone or state and federal dollars combined, changes in health and human services expenditures will significantly affect the Texas budget.

The 13 health and human service agencies provide funding for an array of programs including cash assistance, health care, community and institutional care for the mentally retarded, and protection of abused and neglected children and adults. Two of the largest programs are Medicaid and Aid to Families with Dependent Children (AFDC). Both programs are funded by state and federal dollars. Both include federally mandated requirements and confer entitlements on those eligible.

Total state and federal expenditures for the Medicaid program alone for federal fiscal years (FFY) 1996 and 1997 are estimated at $19.2 billion (including special payments to hospitals discussed in the section titled "Background"), or 24 percent of all-funds appropriations.[2] Medicaid expenditures from the General Revenue Fund are estimated at $7.2 billion, or 16 percent of the general revenue budget.[3] Total state and federal expenditures for the AFDC program for the 1996-97 biennium are estimated at $1.1 billion. General revenue funds appropriated for AFDC for the 1996-97 biennium are $421 million.[4] Although expenditures are much less for AFDC, Medicaid is a benefit for AFDC recipients. Therefore, changes in the AFDC program will affect Medicaid expenditures.

This chapter focuses on Medicaid and AFDC, not only because of the large expenditures made for these two programs, but also because both have been the primary focus of recent public discussion related to federal welfare reform. If any of the proposed reforms are enacted, they could substantially affect future health and human services expenditures and/or services at the state level. Such changes affect not only the direct recipients but, in the case of Medicaid, health care providers as well. The medical component of welfare, including Medicaid and long-term (nursing facility or community) care, "...is a major resource in the health care economy of Texas."[5] Any changes in the level and/or distribution of expenditures affect large provider constituencies, for example, physicians, hospitals, and nursing homes, as well as local taxpayers.

Because of the effect of the Medicaid and welfare programs on the state budget, analysis of the budget requires a basic understanding of these programs and available options. In addition, an understanding of these programs is crucial to policymakers in determining whether Texas is disadvantaged when compared to other states under any proposed reform scenario.

The Texas Medicaid Program

Background

The Medicaid program is a joint state-federal program providing health care services for various categories of adults and children with low family incomes. It was established in 1965 by Title XIX of the Social Security Act. State funds are matched with federal funds based on a formula comparing the average per capita wealth of a state to the average national per capita wealth.[6] The FFY 1996 Texas-federal funds match is 37.6 percent for state shares and 62.4 percent for federal shares.[7]

In addition to paying for direct medical services, Medicaid makes special payments, called "dispro" payments, to hospitals serving a "disproportionate" share of uninsured and low-income patients compared to private pay patients. The amount of dispro funds is capped at $1.5 billion per fiscal year and is paid from state and federal funds at the same matching rate of 37.6 percent and 62.4 percent. Texas uses intergovernmental transfers from local hospital districts, public hospitals, and state-owned hospitals for the state's share. Texas requires, among other things, that participating hospitals make annual reports on their use of dispro funds and develop primary care alternatives to emergency room use.[8]

Who Is Eligible?

The federal government mandates certain eligibility requirements that states must accept in order to receive federal matching funds. States are granted options whereby they can choose to serve additional recipients. Also, states set the percentage of the federal poverty level (FPL) at which persons are eligible for AFDC. Currently, the percentage set by the Texas Legislature is 18 percent.[9] Table 5.1 shows persons who are eligible for Medicaid benefits in Texas.

Clearly, only the most vulnerable Texans—children, the elderly, or people with disabilities—receive benefits.

What Services Are Provided?

In general, Medicaid provides basic health services, such as hospital and physician services, as well as special services for the elderly or disabled in nursing homes. The federal government has mandated certain services for Medicaid recipients. Other services can be provided at the option of the state. Texas provides some optional services, including prescription drugs (limited in some cases), intermediate care facilities for the mentally retarded, community care for the disabled, eyeglasses, and hearing aids.

Table 5.1

Medicaid Eligibility
Federally Mandated Eligibility

Group	Maximum Income As % of FPL
AFDC Families	18
Pregnant Women and Children Five and Younger	133
Children Ages 6 through 12[a]	100
SSI and Low Income Aged or Disabled Cash Benefit Recipients	73

Optional Eligibility in Texas

Group	Maximum Income As % of FPL
Pregnant Women and Infants up to Age One	134-185
Families with High Medical Expenses	26
Elderly or Disabled Persons Requiring Nursing Home, Mental Retardation Intermediate Care Facility, or Community Care[b]	74-219

Source: Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1996) p. 5-13; State Medicaid Office, Texas Health and Human Services Commission, *Texas Medicaid in Perspective* (Austin, Tex., May 1994), p. 31.

[a]The maximum age in this category will increase each year until all children 19 and under at or below 100 percent of FPL are covered.

[b]These recipients pay all except $30 of their income to the facility.

Recipients and Expenditures

In FFY 1995, more than 2.5 million Texans received Medicaid services. Of this total, 57 percent were children (not including children with disabilities), 12 percent were elderly, 11

percent were blind or disabled, and 21 percent were adults (pregnant women and AFDC parents).[10]

Children constitute the largest category of Medicaid recipients. Twenty-six percent of all Texas children depend on Medicaid, which also pays for more than 40 percent of all Texas births. The fact that children in low-income families are the largest group of Medicaid beneficiaries in Texas reflects the state's relatively young population, the high percentage of its population that is medically uninsured, and the high poverty rate among children.[11]

The largest percentage of money spent for client services, however, is for persons who are elderly, blind, or disabled. Fourteen percent of all elderly Texans depend on Medicaid, which pays some portion of the bill for 71 percent of nursing home residents.[12]

Medicaid spending by category of recipients in FFY 1995 was 28 percent for the elderly, 31 percent for the blind or disabled, 23 percent for children, and 18 percent for parents and maternity (see table 5.2).[13] Per capita costs are lower for children because these expenditures include relatively low-cost routine health checkups and preventive care, whereas the elderly and disabled typically have conditions that incur high costs.

Table 5.2

Medicaid Spending by Category

FFY 1995 Category	% Medicaid Recipients	% Medicaid Expenditures
Children	57	23
Elderly	12	28
Blind/Disabled	11	31
Adults (Parent/Maternity)	21	18

Source: Texas Department of Human Services, *Statistical Report on Medical Care: Eligibles, Recipients, Payments, and Services,* form HCFA-2082-84 (10-84) (Austin, Tex., fiscal year 1995); and State Medicaid Office, Texas Health and Human Services Commission, *Texas Medicaid in Perspective* (Austin, Tex., May 1994), p. 39.

Medicaid Operations in Texas

The State Medicaid Office of the Texas Health and Human Services Commission operates the Medicaid program in Texas. The three state agencies with major Medicaid responsibilities are the Texas Department of Human Services (TDHS), the Texas Department of Mental Health and Mental Retardation (TMHMR), and the Texas Department

of Health (TDH). TDHS determines eligibility and administers the nursing home and community care programs for the elderly, blind, and disabled. TMHMR administers Intermediate Care Facilities for the Mentally Retarded, an institutional care and treatment program for Medicaid-eligible people with mental retardation. TDH oversees payment for client services.[14]

Claims Administration

Claims payments for client services are administered through a contract with a private claims administrator. Claims for the basic Medicaid program for children, the Early and Periodic Screening, Diagnosis and Treatment Program (EPSDT), are administered by the claims administrator on a cost-plus-fee, nonrisk basis. Texas pays premiums to the claims administrator for non-EPSDT Medicaid claims under a limited shared-risk structure. Texas is the only state that operates under a shared-risk structure, the purpose of which is to act as an incentive to the contractor to control claims costs.[15] Negotiations with the claims administrator play an important role in determining Medicaid costs.

Growth in Medicaid Spending

Total Medicaid expenditures include payments for client services, payments to disproportionate share hospitals, and administrative costs of approximately 4 percent. Medicaid spending in Texas significantly increased between 1984 and 1994, both in total and on a per capita basis. The amount of all state and federal funds spent on Medicaid in FFY 1984 was $1.5 billion for 600,000 recipients, or $2,500 per recipient. Spending for FFY 1994 was $12.1 billion (in constant dollars) for 2.6 million recipients, or $4,654 (in constant dollars) per recipient.[16]

While increased per capita costs resulted in part from expansion of mandated benefits for Medicaid recipients, the primary cause of increased Medicaid costs in Texas is the growth in the number of federally mandated beneficiaries. Because eligibility in Texas was highly restrictive relative to other states prior to the imposition of these mandates, the number of beneficiaries in Texas grew at rates higher than the national average in response to federal requirements.[17] Since the federal government is currently working to reduce Medicaid costs, federal expansion of the Medicaid program is not likely over the next few years. The growth rate in Texas Medicaid recipients began to level off in FFY 1994. The average annual growth rate in the number of recipients from FFY 1986 to FFY 1993 was 18 percent. The growth rate for FFY 1994 was 9 percent, and the growth rate for FFY 1995 had decreased to 2 percent.[18] Growth in the number of Medicaid beneficiaries in Texas should remain at a low rate over the next few years, subject to growth in population and the proportion of persons living in poverty.

Other causes for the growth of Medicaid spending in Texas include medical inflation higher than the national average and a court-mandated requirement to reimburse Medicaid providers at a "reasonable and adequate" level to meet the costs of "efficiently and economically" operating facilities. This requirement has resulted in provider reimbursement levels closer to private-sector levels.[19]

Comparison of Texas to Other States

How does Texas compare to other states in providing health care services to low-income citizens? Table 5.3 illustrates comparisons based on various attributes.

Table 5.3

Medicaid in Comparison

Attribute	National Rank
Number of Poor Persons Per Capita, 1993	11
Average Annual Growth in Medicaid Cases, 1988-93	5
Average Annual Growth in Medicaid Expenditures, 1988-93	5
State Medicaid Spending Per Capita, 1993	34
Ratio of Medicaid Recipients to Number of Persons in Poverty, 1991	42

Source for 1993 figures: Kaiser Commission on the Future of Medicaid, *State Variations in Medicaid: Implications for Block Grants and Expenditure Growth Caps*, Policy Brief (Washington, D.C., March 1995). Source for 1991 figures: State Medicaid Office, Texas Health and Human Services Commission, *Texas Medicaid in Perspective* (Austin, Tex., May 1994), p. 83.

Current Initiatives

Managed Care

The State Medicaid Office initiated two managed care projects, one in Travis County and one in the tricounty area of Jefferson, Galveston, and Chambers counties in 1993. A preliminary study of these projects indicates possible savings of approximately 4 percent as reflected in lower premium rates for the Medicaid claims administrator.[20]

According to the Texas Department of Health, the purpose of managed care is not just to save dollars. Managed care can also improve the delivery of services by providing improved access to primary and preventive care for Medicaid patients. Patients who previously used emergency room services for routine care will be able to more readily

access primary and preventive care, "...health care delivery [systems] that truly focus on 'health care' and not just on 'sick care'."[21]

To avoid raising revenues or cutting recipients and/or benefits, and to improve delivery of services, the 1995 legislature directed the State Medicaid Office to expand managed care pilot projects to three service areas—the core counties of Lubbock, Tarrant, and Bexar, plus their surrounding counties.

The 1995 legislature also passed Senate Bill 10 which, among other things, required the State Medicaid Office to apply for a waiver with the federal Health Care Financing Administration (HCFA) that would allow expansion of managed care statewide. One of the purposes of filing the Medicaid waiver was to expand Medicaid benefits to adults in AFDC families earning up to 45 percent of the FPL and to children ages 6 and older in families earning between 100 percent and 133 percent of the FPL.[22] The waiver was filed August 31, 1995. The waiver application is currently being revised to allow for expansion only to currently ineligible children ages 6 to 18 in families with incomes between 100 percent and 133 percent of the FPL, or $12,980 to $17,310 for a single parent with two children.[23]

Charge to House Public Health Committee

On February 5, 1996, Speaker of the House, James E. "Pete" Laney, directed the House Public Health Committee to study the possibility of improving access to health care for children. The committee is to conduct a comprehensive review of health care options for children and will present its findings to the 1997 legislature.[24]

Speaker Laney stated that the need for this review is based on soaring health care costs and on the lack of private health care insurance or Medicaid coverage for more than one in three Texas children. Approximately 60 percent of these uninsured children reside in homes in which both parents are present and at least one parent is employed.[25] Employer-supported health insurance for dependents is declining. In addition, a family of four generally needs to earn at least 250 percent of the FPL, or $39,000 in 1996, to be able to pay a portion of health insurance costs.[26] One of the issues to be studied is providing incentives for businesses to offer health insurance coverage to their employees.[27]

One possibility for improving access is the expansion of Medicaid to children not currently eligible. The estimated cost of expanding Medicaid to all children 19 and under with family incomes up to 200 percent of the FPL was $741.7 million for the 1996-97 biennium.[28]

Federal Medicaid Reform and Its Impact on Texas

Federal reform of Medicaid, as well as AFDC, has been the subject of recent congressional debate. Although no reform bills have been enacted as of the publication date of this report, the proposals discussed will likely form the framework for future debate.

The major reform under consideration eliminates Medicaid as an entitlement program and replaces it with Medigrants, block grants to the states in fixed amounts based primarily on a state's Medicaid expenditures history. Medigrants would have fewer federal requirements,

thus giving Texas and other states broad new responsibilities to define eligibility and benefits. An alternative approach that has been discussed is to set maximum limits on per capita expenditures.

Opinions differ about the effect these changes will have on Texas. Some believe that the block grant approach will allow Texas greater flexibility to use federal funding more efficiently and effectively. Others argue that the level of federal funding under the proposed formulas will be inadequate for Texas to keep up with expected growth, forcing state officials to make difficult choices to restrict eligibility, reduce benefits, and/or lower reimbursement rates to Medicaid providers. They also argue that Texas would be at a disadvantage for federal funds in relation to other states because federal funding would be based in part on a state's spending history. Texas pays an average of $2,800 in annual benefits per Medicaid recipient; New York pays about $5,000; the national average is $3,900.[29]

The fate of documented and undocumented aliens in the federal reform debate also could have important implications for Texas. State and local governments in Texas spent an estimated $543 million on health care for undocumented aliens in 1993. Although one reform provision would provide supplementary federal funds to help pay for services to this population for the next five years, the proposed allotment for Texas would be less than $100 million a year. An alternative provision, however, would require the federal government to be solely responsible for the costs of emergency care for undocumented aliens with Medicaid-eligible incomes, now paid in part by the state's share of the state-federal Medicaid match.[30]

Policy Options

If the 1997 legislature should be faced with the need to make changes in the Medicaid program, options would be limited under present law. Given current federal requirements, and in the absence of federal reform or federal approval of the waiver, Texas would be limited to the following options:

1. Eliminate the state Medicaid Program.

   Biennial savings $8.5 billion

   While eliminating the entire Medicaid program is an unlikely scenario, considering the possibility is useful for clarifying the benefits of the program. What would happen if the program were eliminated?

   1. More than 2.5 million Texans would lose health care benefits, including 1.4 million children and 600,000 elderly and/or disabled persons.

   2. Texas hospitals would lose revenues of more than $8.6 billion; Texas nursing homes would lose revenues of more than $2.8 billion; Texas physicians would lose revenues of more than $1.7 billion; and Texas pharmacies would lose revenues of more than $1.4 billion.

3. Texas would save $8.5 billion in general revenue funds, but Texas would lose more than $14.1 billion in federal matching funds.[31]

While the state would save $8.5 billion, people would lose health care and providers would lose revenues. In addition, costs incurred for providing health care to these recipients could be shifted to local communities—counties and local hospital districts, private-pay patients and payers of private insurance premiums, local charities, and families and individuals. Public and other hospitals dependent on Medicaid for their patient bases would suffer major financial losses, as would nursing homes.[32] Taxpayers who support public hospitals could be faced with higher property taxes. Disproportionate share funds to reimburse hospitals for the uncompensated care of indigent patients also would be lost. Hospitals affiliated with Texas medical schools would lose patients and dollars necessary to function as teaching hospitals for medical students, thus adding to revenue demands for higher education.[33]

2. Reduce the number of optional services recipients by 10 percent.

Biennial savings $500.0 million

While the per recipient costs of all optional categories cannot be precisely calculated, using the average biennial costs for four major recipient categories provides a useful tool for estimating costs of decreasing the number of recipients in these categories. Table 5.4 provides an estimate of the changes in general revenue funds for decreasing recipients by 10 percent for a biennium, based on actual FFY 1995 expenditures.

3. Eliminate optional services.

Biennial savings $1.6 billion

As previously discussed, Texas has elected to provide certain optional services to recipients. These services include prescription drugs (limited in some cases); community care (i.e., home health care and day care facilities) for elderly persons who are frail and for persons with disabilities; intermediate care facilities for persons who are mentally retarded; eyeglasses; and hearing aids. These services represent approximately 28 percent of total service costs.[34]

Based on projected costs for the 1998-99 biennium, Texas could save approximately $1.6 billion by eliminating these services.[35] However, 88 percent of these services are provided to persons who are aged, blind, and disabled. These services are designed to assist these recipients in remaining as self-sufficient as possible to avoid being placed in institutional facilities (e.g., nursing homes for persons with disabilities and state hospitals for persons who are mentally retarded). Such institutional care is more costly than community care.[36]

Table 5.4

Decrease in Medicaid Recipients

	Average Biennial Cost (in millions of dollars)	10% Decrease in Recipients (number indicates the decrease)	Biennial General Revenue Savings (in millions of dollars)
Children	778	145,132	113
Adults (Parent and Maternity)	1,598	53,245	85
Aged	4,440	30,799	137
Disabled/Blind	5,624	27,018	152
Total Client Expenditures			$487 million
2.7% Administrative Costs			$13 million
Total General Revenue Savings per 10% Decreases in Recipients across All Categories			$500 million

Source: Adapted from Texas Department of Human Services, *Statistical Report on Medical Care: Eligibles, Recipients, Payments, and Services,* form HCFA-2082-84 (10-84) (Austin, Tex., fiscal year 1995) and administrative cost calculations, State Medicaid Office, Texas Health and Human Services Commission, *Texas Medicaid in Perspective* (Austin, Tex., May 1994), p. 64.

4. Maintain current expenditures if federal funds are reduced 10 percent.

   Biennial savings $1.4 billion

   If the federal government should block grant the Medicaid program, and federal funds for the Medicaid program in Texas were reduced, for example, by 10 percent, the state would face some hard choices. The legislature would have to decide whether to reduce the number of persons eligible, to reduce benefits, or to maintain current recipients and services by making up for lost federal funds with general revenue funds. Ten percent of projected federal funds to be received in the 1998-99 biennium is $1.4 billion. Texas would be required to spend general revenue funds in this amount to make up for lost federal dollars in order to maintain current services.

Under current law, the legislature has few options. Those options that are available are difficult and significantly affect the lives of persons most in need. In addition, even if Texas reduced the number of eligible people or eliminated services, the need for these services would not be eliminated. Local governments—counties and hospital districts—could be forced to increase property taxes to fill in the gap left by the loss of Medicaid benefits. Texas health care providers would experience significant loss of incomes. Lower incomes could eliminate jobs and businesses. Costs of services provided as charity care could be passed on to private-paying patients.

Welfare in Texas

Background

The financial aid and social services programs, collectively known as welfare programs, created by the Social Security Act are administered by the Texas Department of Human Services. These programs include AFDC, food stamps, the Child Support Enforcement Program, and the Social Services Block Grant.

For the 1996-97 biennium, $7.0 billion in state and federal funds were appropriated to TDHS, $2.5 billion in general revenue. TDHS is the second largest of the health and human services agencies when ranked by total appropriations, and it receives the third largest general revenue appropriation of all state agencies.[37] Following is a brief description of the two major programs providing financial assistance to low-income families—AFDC and food stamps.

Aid to Families with Dependent Children

Congress established AFDC in the Social Security Act of 1935. The program provides cash assistance to support children in poor families with the goal of encouraging self-sufficiency and independence of these families. The Texas Legislature determines eligibility requirements and sets program appropriations. TDHS determines the maximum grant amount for each household size. Table 5.5 shows a comparison of the number of recipients and benefits paid for fiscal year 1993 through 1997.

Who Is eligible?

To qualify for AFDC, a family must have less than $1,000 in assets, excluding a home and one car with equity value of less than $1,500, and income at no more than 18 percent of the federal poverty level for the same family size. The typical AFDC family, a mother and two children, can have a net income of no more than $188 a month after allowable deductions. Two-parent households can receive assistance through the AFDC-UP (unemployed parent) program while the primary wage-earning parent is temporarily unemployed. AFDC-UP is limited to six cash benefits for a 12-month period, although Medicaid benefits can continue throughout the year.[38]

Table 5.5

AFDC

FY	Number of Families	Number of Individuals	All-Funds Appropriations (in millions of dollars)	General Revenue Funds (in millions of dollars)	Average Monthly Grant (in dollars)[a]
1993	277,242	778,686	533.5	203.1	179
1994	282,929	786,395	544.8	205.8	182
1995	274,457	763,835	523.2	223.7	183
1996	283,127	772,366	543.4	204.4	183
1997	289,554	798,659	563.1	214.7	187

Source: Texas Department of Human Services, *Program Budget and Statistics* (Austin, Tex., September 1995).

[a]Single parent or caregiver and two children.

Benefits

Recipients receive monthly cash grants and are eligible for food stamps and Medicaid benefits. The total monthly value of these benefits for a typical family of mother and two children in FY 1996 is $809: $188 in cash benefits, $311 in food stamps, and $310 in health care (Medicaid).[39]

Cash benefits were increased in March 1994 for the first time since 1986. When adjusted for inflation, the average monthly grant has fallen more than 60 percent since 1970.[40]

Reforms in the 1995 Legislature

In 1995, the Texas Legislature directed the Texas Health and Human Services Commission to file a waiver application with the federal government to make certain changes in the AFDC program. The waiver was recently approved by the federal Department of Health and Human Services. The goal of the waiver is to save money by moving parent/caretaker recipients from welfare into the job force. Texas joins 37 states that have received permission to depart from federal welfare rules and is the first state granted permission to issue time limits on welfare benefits tied to a client's prior work experience and education.[41]

Among reforms are the following:

1. Applicant must provide proof of citizenship or have satisfactory immigration status and be a Texas resident.

2. The state must specify clear and tangible goals for the recipient (for example, education, job training).

3. The state must ensure efficient and fraud-free services.

4. The state must allow communities flexibility in developing alternative programs.

5. Recipients must cooperate in establishing paternity of their children; must complete medical screens of their children if services are available; must immunize their children; must not voluntarily terminate paid employment without a good cause; must participate in an activity to build self-sufficiency; must not use, sell, or possess drugs or abuse alcohol; and must attend school and parenting classes.

6. A time limit on benefits of one to four years has been established, beginning when the client becomes eligible for a slot in a jobs training program, with the length of the benefits period depending on the client's education level and work experience.

7. Once a recipient leaves the AFDC program, a time lapse of five years must occur before a client can again be eligible for assistance.

Texas is one of only three states that has a time limit for the caretakers portion of the assistance; the children's portion continues. House Bill 1863 also establishes a pilot program allowing clients to keep larger percentages of benefits as they begin work and to start saving money for the transition from AFDC to independence from public assistance. Also, an effort will be made to move AFDC recipients with disabilities to the federally funded Supplemental Security Income program (SSI) in order that clients may be more appropriately served.

Critics say expected savings may not materialize because the system only removes people from the welfare system—it does not make them employable. Many recipients require remedial education even before they can begin a job training program, and remedial education is not addressed in the reform package.[42]

Comparison with Other States

The national average maximum income for AFDC is 43 percent of the FPL. As of 1994, the income cap in Texas for a mother and two children was 18.3 percent of FPL, or $188 per month. Only two states, Alabama and Mississippi, had lower caps than Texas.[43]

Growth in AFDC

Nationally, AFDC rolls grew steadily during the 1950s and 1960s. They increased dramatically during the 1970s and 1980s as the number of poor single-parent households

increased. The 1990s brought increased scrutiny to AFDC as the number of recipients hit an all-time high in March 1994, supporting 14.36 million people in 5.08 million families nationally. However, in August of 1995, AFDC rolls dropped to 13.2 million people in 4.72 million families.[44] According to officials at the Texas DHS, growth in AFDC in Texas followed the national trend. AFDC rolls are not expected to increase dramatically in the 1998-99 biennium, and program expenditures will remain constant. This translates into an overall trend for Texas of declining growth in AFDC rolls at the margin. In other words, the number of AFDC clients increases almost every year, but the increase is slowing. This reduction is due in part to the increased scrutiny of welfare fraud, which has led to a greater stigma being placed on welfare recipients, and in part to the overall economic boom in the Texas economy.[45]

Food Stamp Program

The federally funded state-administered Food Stamp Program supplements the diets of low-income families, elderly people, and single adults. To be eligible for food stamps, the people living in a household must have combined incomes of less than 130 percent of federally established limits for poverty and countable resources of less than $2,000. Each recipient's food stamp allotment is based on the number of people living in the household and income after allowable deductions.[46] Table 5.6 shows selected statistics for the program.

Table 5.6

Food Stamps

FY	Value of Food Stamps Issued (in billions of dollars)	Number of Recipients (monthly average in millions)	Average Monthly Allotment (in dollars)
1995	2.30	2.68	71
1996	2.38	2.71	73
1997	2.60	2.83	77

Source: Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1996), p. 5-26.

Concerns over food stamp fraud led to the Electronic Benefits Transfer (EBT) project, a joint effort involving TDHS, the Texas Comptroller of Public Accounts, the State Treasury, and the Department of Information Resources. Each eligible household receives a Lone Star electronic billing card to purchase food at grocery stores, farmers' markets, and

other food retailers. EBT has replaced paper food stamps and AFDC warrants with plastic debit cards similar in appearance to bank or credit cards. EBT is expected to reduce paperwork, processing costs, and fraud. Additional goals of EBT are to get benefits to clients more quickly and safely and to lessen the stigma associated with public assistance.[47]

Federal Welfare Reform

Reform of the current AFDC program also has been the subject of much debate in Congress. Like Medicaid reform discussions, the issues recently debated will likely provide the framework for future reform. Proposed reforms include abolishing guaranteed assistance to be replaced by block grants to the states. States would have broad discretion in the design of their programs. In 1995, two bills containing provisions for reforming welfare were debated: the Omnibus Budget Reconciliation Act (OBRA), and the Personal Responsibility and Work Opportunity Act of 1995, commonly known as the welfare reform bill. OBRA was vetoed by President Clinton, and the conference agreement on the welfare reform bill stalled due to a disagreement over provisions to convert child nutrition programs to a block grant. A new welfare reform bill, incorporating essentially the same aspects of last year's legislation, is being considered this year.

Temporary Assistance for Needy Families Block Grant[48]

Under the 1995 welfare reform bill, the current AFDC, JOBS, and Emergency Assistance (EA) programs would be combined into a new Temporary Assistance for Needy Families (TANF) block grant. This block grant includes a requirement that by 2002 parents or caretakers in 50 percent of all families and in 90 percent of two-parent families receiving TANF funded services be engaged in work. The bill reduces funding for the programs folded into TANF and repeals the current guarantee that child care assistance be provided to participants in the JOBS and other job training programs.

Under TANF, levels of federal funding to the states are permanently frozen based on the states' recent federal spending for the programs in the block grant. States could use either their FY 1994 federal spending level, an average of their FY 1992-94 levels, or their FY 1995 funding level as the base year. Annual 2.5 percent adjustments for FY 1997-2000 are available to high-population-growth, low-benefits states such as Texas. There is also a small contingency fund for states with high unemployment. Only states that continue to spend 100 percent of FY 1994 state spending qualify.

Other components of the TANF include a provision that states are required to continue spending at least 75 percent of their historic state expenditure. States are allowed to transfer up to 30 percent of their TANF block grant to other grants (for example, Child Care and Development Block Grant or the Child Protection Block Grant). States would also receive bonuses for reducing their "illegitimacy ratio" and penalties for noncompliance with new federal standards, including work participation requirements. Prohibitions for spending TANF money will include new restrictions on children born to mothers receiving TANF assistance (optional), unmarried parents under age 18, fugitives and felons, and parole violators.

Work Requirements and Child Care

States would be required to institute a more stringent work requirement. Under this provision, states must require a parent receiving TANF assistance to engage in work once the state determines the parent is ready to do so or once the parent has been on the program for 24 months, whichever is earlier. States would have to meet annual work participation rates. States not meeting those rates would be subject to a penalty of 5 percent of their total TANF grant. The penalty for Texas in the first year would be $25 million.

A single child care block grant will be distributed to states based on either their FY 1994 federal spending in AFDC child care, Transitional Child Care, and At-Risk Child Care, or on the average funding for those programs for FY 1992-94. Funding for child care under this new formula is projected to fall $14.6 billion short nationwide over the next seven years of the amount needed to provide child care services to all the families required to work if the states are to meet the work participation targets in this bill.[49]

As in the case of Medicaid, many believe that Texas would be hurt by AFDC reform in comparison to other states. Texas is a low-benefit, high-growth state. Federal funding as proposed during congressional debate would not keep pace with Texas needs because other states provide more generous benefits.[50] For example, Michigan has an average AFDC payment of $457 per month; Wisconsin, $517 per month. This compares to Texas, where the maximum benefit for a family of three is $188 per month.[51]

Policy Options

1. Eliminate AFDC.

   Biennial savings $421.0 million

   Participation in the AFDC program is optional. A state can decide to participate in the program and receive federal matching dollars. If Texas chose to eliminate AFDC, the state could save $421 million in general revenue funds based on 1996-97 appropriations; but Texas would lose $685 million in federal funds.

   The question is "What would Texas do instead?" Funds could be returned to general revenues for use in other areas or to find alternative welfare programs. Monthly cash benefits in Texas are already so low they do not cover expenses for housing and utilities. (Health care and food assistance are covered by other programs as discussed previously in this chapter.) If current reform efforts do not accomplish Texas goals, the legislature could look at reform in other states. Many states, such as Wisconsin, are redesigning the program entirely. Instead of distributing any cash grants to recipients, the Wisconsin program will help recipients locate jobs in addition to job training. Other programs would give the grants to employers as an incentive to hire welfare recipients.

2. Maintain current expenditures if federal funds are reduced by 10 percent.

   Biennial cost $68.5 million

   If the federal government should block grant the AFDC program, and federal funds for the AFDC program in Texas were reduced by 10 percent, Texas legislators would have to decide either to reduce the number of people eligible to receive AFDC, reduce the size of the cash assistance per eligible family, or maintain current spending and make up for the lost federal dollars with general revenue funds. Ten percent of the projected federal funding of the AFDC program for the 1998-99 biennium is approximately $68.5 million.

Conclusion

With or without Medicaid and AFDC reform at the federal level, Texas faces choices that are indeed hard if demands for these and other health and human services continue to increase. Options are limited. Costs are high. Suspicion of fraud is prevalent, though not confirmed by the data. Some groups of constituents demand cutbacks in programs to save tax dollars. Other groups of constituents demand increased services. All demand cost effectiveness. Most agree on expected outcomes (e.g., improved health, increased self-sufficiency of low-income families), but they cannot agree on how to accomplish these outcomes. Most popular reforms in other states would require significant new investment for Texas. Effective strategies are often difficult to measure in welfare programs.

Few would argue with providing Medicaid benefits to children, elderly persons, and persons with disabilities. Providing health care to children may or may not save future dollars, but certainly it improves the quality of individual lives. Improvements in the quality of individual lives benefits society as a whole—healthier individuals are more likely to learn and become better educated. Better educated individuals in turn are more likely to be employed and to contribute to society in a positive way. Relieving the physical and mental problems caused by old age or physical disabilities is a goal all would support. But the costs to taxpayers for these services are high.

The AFDC program has been controversial. Some believe that the program encourages irresponsibility; others believe it is the only support keeping women and children from becoming homeless. Many believe that the program is plagued by fraud committed by people who lie about their income. As discussed in the "Welfare" section, the legislature has responded to these perceptions by initiating reform that encourages AFDC parents to become employed by limiting the length of time a family is entitled to AFDC benefits and that discourages fraud in the Food Stamp Program through the use of the Lone Star card.

Having now taken two major steps to control costs and improve outcomes—managed care expansion in the Medicaid program and AFDC reforms—the 1997 legislature will need to carefully evaluate the effects of these reforms. Legislators will have the opportunity to determine if true reform can be achieved, costs controlled, and outcomes improved. Beyond such analysis, the legislature as well as the public needs to understand what these

programs do, what they cost, and what the consequences would be should they be reduced or eliminated so lawmakers can chart the best course.

Notes

[1]Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1996), pp. 1-2–1-4, 5-1.

[2]Medicaid expenditure estimates are based on federal reporting forms for the federal fiscal year (October 1-September 30), not on Texas' state fiscal year (September 1–August 31). The estimates should be considered the same as appropriated amounts, however, because appropriations are based on anticipated expenditures. There is no single Medicaid appropriation. Funds for Medicaid appropriations are included in the appropriations for eight health and human services agencies, primarily the Texas Department of Health (TDH), Texas Department of Human Services (TDHS), Texas Department of Mental Health and Mental Retardation (TMHMR), and the Texas Department of Protective and Regulatory Services (TDPRS). Federal fiscal year (FFY) data noted where used.

[3]State Medicaid Office, Texas Health and Human Services Commission, *Medicaid Program Budget Report*, form HCFA-37.1 (01-93) (Austin, Tex., February 16, 1996), p. 1; and Legislative Budget Board, *Fiscal Size Up*, p. 1-2.

[4]Tex., House Bill. I, 74th Leg. (FY 1996-97).

[5]State Medicaid Office, Texas Health and Human Services Commission, *Texas Medicaid in Perspective* (Austin, Tex., May 1994), p. 1.

[6]Ibid., p. 16.

[7]Texas Department of Health, *History of Medicaid Match* (Austin, Tex., March 1995).

[8]State Medicaid Office, *Texas Medicaid in Perspective*, pp. 47-48, 62.

[9]Legislative Budget Board, *Fiscal Size Up*, p. 5-13.

[10]Texas Department of Human Services, *Statistical Report on Medical Care: Eligibles, Recipients, Payments, and Services*, form HCFA-2082-84 (10-84) (Austin, Tex., fiscal year 1995).

[11]Texas Comptroller of Public Accounts, *Medicaid Block Grants*, Austin, Tex., June 1995. (Pamphlet)

[12]State Medicaid Office, *Texas Medicaid in Perspective*, p. 39.

[13]Texas Department of Human Services, *Statistical Report on Medical Care*.

[14] State Medicaid Office, *Texas Medicaid in Perspective*, p. 20.

[15]Ibid., pp. 67-68.

[16]Ibid. pp. 33, 67-68; State Medicaid Office, *Medicaid Program Budget Report*; and U. S. Bureau of the Census, *Statistical Abstract of the United States: 1995* (Washington, D.C., 1995), table 761.

[17]State Medicaid Office, *Texas Medicaid in Perspective*, pp. 3, 58.

[18]Calculations based on State Medicaid Office, *Texas Medicaid in Perspective*, pp. 33 and 66; and Texas Department of Human Services, *Statistical Report on Medical Care.*

[19]State Medicaid Office, *Texas Medicaid in Perspective*, pp. 9, 58.

[20]Lyndon B. Johnson School of Public Affairs and School of Public Health, University of Texas at Houston, *Effects of LoneSTAR in Travis County,* Policy Research Project Report Series, (Austin, Tex., April 1995), p. vii.

[21]Texas Department of Health, *Medicaid Reform: Improving the Health of Texans through Community Focused Managed Care* (Austin, Tex., July 1995), p. 3.

[22]Texas Health and Human Services Commission, *Texas 1115 Medicaid Waiver Summary* (Austin, Tex., August 15, 1995), p. 24.

[23]Texas Health and Human Services Commission, *Texas Medicaid Program 1115 Waiver Revisions Concept Paper* (Austin, Tex., March 28, 1996).

[24]"Many Uninsured Kids Aren't Poor," *Austin American-Statesman* (February 9, 1996), p. B-1; and "Lawmaker Urges Solutions for Texas' Uninsured Kids," *Dallas Morning News* (February 9, 1996), p. A-32.

[25]"Many Uninsured Kids Aren't Poor;" and Lyndon B. Johnson School of Public Affairs, *Children's Health Care Policy Issues in Texas: Data Book*, Working Paper Series, no. 84 (Austin, Tex., 1995), pp. 2, 7-8.

[26]Lyndon B. Johnson School of Public Affairs, *Children's Health Care Policy Issues in Texas: Options for Financing Coverage*, Preliminary Report, Policy Research Project Series (Austin, Tex., February 1995), p. 11.

[27]"Lawmaker Urges Solutions for Texas' Uninsured Kids," p. A-32.

[28]Lyndon B. Johnson School of Public Affairs, *Children's Health Care Policy Issues in Texas,* pp. 28-34.

[29]Texas Comptroller of Public Accounts, *Medicaid Block Grants.*

[30]State Medicaid Office, *Texas Medicaid in Perspective*, p. 93; and Center for Public Policy Priorities, "Comparison of House Commerce and Senate Finance Medicaid Proposals," *Washington Watch* (October 24, 1995) (newsletter).

[31]Texas Health and Human Services Commission, *Revised Medicaid Block Grant Projections* (Austin, Tex., November 29, 1995); and Texas Department of Human Services, *Statistical Report on Medical Care.*

[32]Texas Comptroller of Public Accounts, *Medicaid Block Grants.*

[33]Paul Burka, "State Secrets," *Texas Monthly* (December 1995), p. 206.

[34]State Medicaid Office, *Texas Medicaid in Perspective*, p. 65.

[35]Texas Health and Human Services Commission, *Revised Medicaid Block Grant Projections.*

[36]State Medicaid Office, *Texas Medicaid in Perspective*, pp. 64-65.

[37]Legislative Budget Board, *Fiscal Size Up*, p. 5-20.

[38]Ibid., p. 5-25; and State Medicaid Office, *Texas Medicaid in Perspective*, p. 51; and Texas Department of Human Services, *1994 Annual Report* (Austin, Tex.), p. 18.

[39]Legislative Budget Board, *Fiscal Size Up*, p. 5-25.

[40]"Welfare Raises Questions; An Expert Gives Answers," *Austin American-Statesman* (September 22, 1995), p. D-2.

[41]"Texas Wins Federal OK to Change Welfare Rules," *Austin American-Statesman* (March 23, 1996), p. A-1.

[42]Ibid.

[43]State Medicaid Office, *Texas Medicaid in Perspective*, p. 22.

[44]"Number of Families on Welfare Dropping Sharply," *Austin American-Statesman* (November 4, 1995), p. A-4.

[45]Telephone interview by Monica Greenhalgh with Clarissa Olson, Budget Analyst, Texas Department of Human Services, Austin, Texas, April 1996.

[46]Texas Department of Human Services, *1994 Annual Report*, pp. 21-23.

[47]Legislative Budget Board, *Fiscal Size Up*, p. 5-25.

[48]While this report was being prepared, new welfare reform legislation was awaiting presidential signature.

[49]Center for Public Policy Priorities, *Washington Watch* (December 15, 1995), pp. 1-2 (Newsletter).

[50]"Welfare Raises Questions," p. D-2.

[51]Partnership for Hope, Inc., and John Sharp, *Texas Demands Its Fair Share from Block Grants* (Austin, Tex., Summer 1995), p. 1.

Chapter 6. Criminal Justice

Introduction

To a great extent, the priorities of a state are reflected in its criminal justice system. Does the system focus on punishment, spending resources to incarcerate as many criminals as possible, or does it invest in crime prevention and rehabilitation? In Texas, the answer to this question largely has been increased incarceration.

Background

In the 1970s and 1980s, the Texas criminal justice system was inundated by a flood of inmates into the state's prisons. From 1984 to 1995, the state prison population rose from 36,000 to 129,462, an increase of about 310 percent.[1] Combined with a lack of prison space, this created a crisis of overcrowding, exacerbated by several lawsuits and an increasing fear of crime among the general public. Consequently, the Texas Legislature began a dramatic expansion of the state's prison capacity in the late 1980s. Since 1987, the state has added 100,000 new prison beds at a construction cost of more than $2 billion. The state also instituted a series of sweeping reforms, culminating in 1993 with the revision of the state's sentencing policies and the creation of a new state jail system. Because of the great increase in the number of prison beds, and the surplus that followed it, the prison population continues to expand. Experts estimate that current capacity will be exceeded by the year 2000.[2]

Who Commits Crimes

To combat crime effectively, Texas must understand who commits crimes and why. The following are some important demographic statistics about crime in Texas:

- In 1990, males comprised 85 percent of all adults arrested and more than 70 percent of all juveniles arrested in Texas.
- In 1990, males age 15 to 34 accounted for 17 percent of the state's population but 59 percent of all arrests.
- For violent crime arrests, people under age 25 comprised 47 percent of the total; 17 percent were younger than age 18.
- In 1992, the Texas prison population was 48 percent black, 28 percent white, and 24 percent Hispanic.
- In 1996, the average prison inmate has a seventh-grade achievement level.
- In 1996, two-thirds of Texas' prison inmates lack high school diplomas.

- Thirty-seven percent of all parolees who did not complete high school returned to prison, compared to only 24 percent who graduated from high school or received a general equivalency diploma.

These crime statistics show that Texas must address the educational needs of young people, particularly minorities, in order to decrease crime effectively.[3]

Demographic Trends

An important trend in the demographics of criminal justice is the rapid increase in crime by juveniles. Since 1981, Texas' juvenile crime rate has increased 281 percent, and the trend is not reversing.[4] Over the next ten years, the rate is expected to increase another 25 percent.[5] This new criminal population poses a special problem for Texas, as a younger criminal population will be a long-term challenge to our criminal justice system. In response to this trend, George W. Bush made juvenile justice reform one of the main themes of his successful gubernatorial campaign. Once in office, he helped pass a bill that increases punishment for juvenile crimes. The measure lowers the age at which juveniles can be tried as adults to 14 and includes a youth boot camp program and a training program to assist offenders in rejoining society. The law increases the number of detention beds for juveniles from 2,500 to 6,300 over the next four years. The 1996-97 budget included a spending increase of $218 million to combat juvenile crime.[6]

Correctional Capacity/Duty to Accept

Three lawsuits and subsequent legislation resulted in the reduction of correctional facility capacity, leading to overcrowding and creating a state duty to accept prisoners from county jails. While pursuing a policy of early paroles in order to create more space in prisons, Texas began a massive prison construction program.

Ruiz v. Estelle

Filed in 1972 and settled in 1992, the *Ruiz* lawsuit decided by U.S. District Judge William Wayne Justice brought about sweeping reform of the Texas prison system. *Ruiz* charged overcrowding in the state prison system. A federal court order resulted in a formula setting a cap on prison populations, established guard-inmate ratios, and guaranteed inmate access to the courts. The terms of *Ruiz*, however, apply only to prisons constructed prior to the 1992 settlement.[7]

Inmate David Ruiz filed a handwritten federal complaint against W. S. Estelle, director of what was then the Texas Department of Corrections (TDC). In April 1974, Judge Justice combined this complaint with those of six other prisoners incarcerated in the federal Eastern District of Texas, thereby creating a consolidated class-action lawsuit challenging almost every aspect of TDC's operations.[8]

After one of the longest civil rights trials in U.S. history, Judge Justice held the state liable for unconstitutional conditions in the Texas prison system. Justice cited several different constitutional and human rights violations revealed during the trial, including the routine

use of "building tenders," or inmate trustees, to maintain order. Justice also cited overcrowded conditions, insufficient security and supervision, inadequate health care, and a failure to provide meaningful care for physically and mentally disabled inmates. The U.S. Fifth Circuit Court of Appeals reversed many of Judge Justice's findings but upheld the bulk of his opinion. Consequently, the Texas prison system was forced to make radical changes. In 1982, disclosure that the building tender system was being maintained secretly caused a furor that effectively broke the old TDC power structure, opening the way to meaningful systemwide reform.[9]

The focus of the ongoing *Ruiz* case rapidly shifted to the issue of overcrowding. In reviewing Judge Justice's opinion, the Fifth Circuit adopted a wait-and-see approach on the issue of whether two inmates could be placed in each of the cells throughout the system. Meanwhile, a special master appointed by Judge Justice forged a compromise between the parties. The result was the crowding stipulation, which set maximum unit and system population levels at TDC. This stipulation provided the population stability needed to implement the broad reforms that are *Ruiz'* legacy.[10]

In the late 1980s, a backlog of TDC-bound prisoners in county jails began to grow at an alarming rate, largely as a result of the federal "war on drugs." The limitations on prison capacity set by the crowding stipulation prevented the state from accepting those inmates, whose numbers were swelling. This volatile mix of jail population pressures and limited prison capacity thrust state and local officials into a bitter and costly fight in the courts and the Texas Legislature.[11]

The County-State Jail Wars

To comply with the provisions of the crowding stipulation, TDC developed a scheduled admissions policy specifying the number of inmates to be received weekly from each county. Even with this policy, however, TDC was unable to accept all state inmates, and the prisoner backlog continued to rise. In November 1988, a Houston federal district court instructed the Harris County sheriff to deliver a number of inmates from overcrowded Harris County jails to TDC, exceeding the levels specified in the scheduled admissions policy.[12] The court's order set a population cap for the Harris County jails and fined the state $50 per day for every jail inmate over that cap, to the extent the overcrowding was due to a backlog of inmates awaiting transfer to TDC.[13] Thus began a legal battle between state and county officials over who should alleviate the jail backlog.[14]

To comply with the *Ruiz* court orders and maintain its policy of evenhanded allocation of bed space to all the counties, TDC refused to accept any inmates above the number set forth in its admissions policy. In October 1988, a dozen of Texas' most populous counties sued TDC, seeking to force the state to accept more inmates. The case eventually became a suit for compensation from the state for housing prisoners in county jails.[15]

In 1989 while the litigation was pending, the 71st Legislature passed House Bill 2335 creating the Texas Department of Criminal Justice to centralize and streamline the state's corrections, probation, and parole agencies. This massive criminal justice reform bill consolidated several agencies into the Texas Department of Criminal Justice (TDCJ). In

1990, TDCJ officially replaced the Texas Adult Probation Commission, Texas Board of Pardons and Paroles, and the Texas Department of Corrections. The bill also sought to alleviate conditions in local jails while maintaining compliance with *Ruiz* court orders. House Bill 2335's primary purpose was to provide financial incentives and disincentives aimed at controlling prison population pressures. This mechanism provided state financing for sentencing alternatives, such as community sanctions designed to divert offenders from state prison, while asking local governments to assume the costs of the backlogged inmates sentenced from their own counties. Explicit language that would have forced the counties to assume the duty for backlogged inmates was removed from the bill before its passage, however, thereby leaving the matter open to judicial interpretation.[16]

The question of financial responsibility for TDC-bound inmates awaiting transfer in local jails initially was decided by a state district court. The court ruled that TDCJ must accept all jail inmates sentenced to prison within seven days of completion of the necessary paperwork or compensate the counties at a rate of $40 per day per inmate. A federal court upheld the state court's ruling, thereby forcing the state to assume financial responsibility for county-held state inmates. In July 1991, the U.S. Fifth Circuit Court of Appeals affirmed TDCJ's financial liability, effectively requiring a state-financed solution to local jail overcrowding.[17]

This ruling came during a heated legislative debate on criminal justice financing. Some members of the legislature, especially those from rural counties with little or no inmate backlog, vigorously opposed state financing of the entire backlog. In part, their opposition was based on the disproportionate use of prison resources by populous urban counties. Some state legislators insisted that if Harris County was compensated, then all the counties should be compensated for the backlog. Consequently, the legislature dismantled the system of incentives and disincentives placed on counties to ease population pressures. In July 1991, the legislature passed House Bill 93 authorizing compensation to the counties for inmate backlogs and forcing the state to accept by 1995 all jail inmates sentenced to state prison within 45 days.[18]

The Effects of Ruiz

On January 28, 1991, Texas Attorney General Dan Morales filed a motion in the *Ruiz* case seeking to terminate the federal court's jurisdiction and bring the case to a conclusion. The motion argued that the state prison system had achieved compliance with all applicable court orders. Moreover, during the 1991 legislative session, the legislature passed House Bill 124 at Morales' suggestion. This statute provided an orderly mechanism to control prison population levels in TDCJ and prevent the recurrence of unconstitutional conditions in Texas prisons.[19]

Later in 1991, state officials and plaintiffs' attorneys, along with representatives of the *Ruiz* Special Master's Office, periodically met to seek a negotiated settlement. The final judgment agreed upon by the parties allowed TDCJ to increase its systemwide population 2,300 inmates above the crowding stipulation. In addition, the judgment allowed TDCJ to use tents or tentlike structures for appropriate correctional programs. Under the terms of the judgment, TDCJ is to take "reasonable steps to ameliorate the effects of crowding on each

of the prison units." TDCJ's top managers have interpreted the agreement to apply to new prison units designed within *Ruiz* limitations, such as the Michael prison prototypes (2,250-bed, state-of-the-art facilities). As a result of TDCJ's decision, Michael units now have additional benches and tables in their recreation yards, as well as color televisions in the infirmary waiting rooms, all purchased with the declared intent of ameliorating overcrowding. The 1994 Texas Performance Review's survey of prison population patterns, however, indicates that TDCJ's present inmate management practices are highly inefficient. Improvements in these practices could make thousands of additional prison beds available without violating the spirit of the agreement.[20]

The overall effect of prison litigation in Texas has been to accelerate the state's trend toward building new prisons as a remedy for population pressures created by local officials exercising their sentencing or prosecutorial discretion. These population pressures have been exacerbated by aggressive restrictions on parole.[21]

Getting Tough on Crime

During the 1970s and 1980s, public concern for safety resulted in harsher sentencing laws. In every recent session, the legislature has broadened the definition of capital crimes, upgraded offenses, and increased mandatory sentences. The average sentence of a Texas inmate has almost doubled, from 5 years in 1970 to 9.9 years in 1991. Because of a lack of prison space, however, the state began paroling more inmates in the mideighties. From 1986 to 1990, the number of prisoners paroled almost tripled, increasing from 14,376 to 42,163. Thus, despite harsher sentencing laws, inmates actually were serving less time than they did 20 years before. The average time served decreased by 32.8 percent, from 2.8 years in 1970 to 1.8 years in 1991. In 1971, prisoners served 55 percent of their sentences; in 1991, only 18 percent.[22]

With the recent expansion of the state prison capacity and tougher parole policies, the average time served increased to three years in 1994, almost doubling since 1991. By 1994, the average sentence length had increased to 10.9 years. The number and percentage of inmates paroled from Texas prisons have declined annually since 1990.[23]

Federal Anticrime Initiatives

In 1994, to give states financial incentives to strengthen sentencing policies, Congress passed the Violent Crime Control and Law Enforcement Act. The law established the Violent Offender Incarceration Grant Program providing states $4 billion over five years for increasing the capacity of state correctional facilities. Funds are distributed according to a formula based on the crime rate. According to the National Conference of State Legislatures and the National Governors' Association, Texas would be eligible to receive approximately $226 million in grants from 1996 to 2000. Congress must appropriate money for this grant program each year, and it remains unclear whether these appropriations will be made.[24]

The second program established by the Violent Crime Control and Law Enforcement Act of 1994 provides grants to encourage states to increase the percentage of time inmates serve.

To qualify for the Truth in Sentencing Incentive Grant Program, states must adopt policies to ensure that violent offenders serve 85 percent of their sentences. In Texas, offenders serve a significantly lower percentage than this standard. Therefore, Texas does not qualify for this program, although harsher sentencing laws ensure that Texas prisoners on average serve more calendar time than the national average.[25]

According to *Federal Funds Information for States*, between 1996 and 2000 Texas would be eligible for $296 million in federal grants if policies were enacted to increase the percentage of time served. To meet these standards, Texas would need to install 10,400 more prison beds by the year 2000 to accommodate the increase in demand for space accompanying an increase in time served. Also, Congress must appropriate money for this program each year.[26]

Current Status and Trends

TDCJ is governed by the Texas Board of Criminal Justice, whose members are appointed by the governor to six-year terms. They, in turn, select the executive director. In this new position, the director is responsible for the daily management and operation of the department and its four divisions: the Institutional Division, the Pardons and Paroles Division, the Community Justice Assistance Division, and the State Jail Division.[27]

The Institutional Division

The Institutional Division of TDCJ is responsible for the custody and rehabilitation of felony offenders sentenced to prison. At the beginning of fiscal year 1995, the Institutional Division operated and managed 61 prison units, including the Skyview and Jester IV psychiatric units and the University of Texas Medical Branch hospital unit in Galveston. At that time, the total capacity of the Texas prison system was 93,945. This includes 89,023 beds operated by the Institutional Division, 2,830 privately operated beds, 1,528 psychiatric beds, and 564 boot camp beds. During fiscal year 1994, the average cost of housing each inmate was $44.40 per day. In 1995, the average daily inmate population in the Texas prison system was 129,462.[28]

Five private prison facilities house medium and minimum security prisoners. The Institutional Division contracts with private prison operators at a cost of $35.25 per day per inmate. This rate includes the costs of housing, educational services, minor medical services, transportation, and lease expenses. Although assigned to a private facility, inmates remain the responsibility of the Institutional Division, which completes diagnostic and classification procedures and provides medical care for inmates who become seriously ill. The Institutional Division also employs monitors to guarantee contract compliance.[29]

The Pardons and Paroles Division

The Pardons and Paroles Division of TDCJ supervises the parole and mandatory supervision system in Texas. As part of the division, the Board of Pardons and Paroles determines which inmates to release on parole, establishes the terms and conditions of

parole, advises the governor on clemency, determines who should be released from the mandatory supervision program, and revokes parole for violation of the terms and condition of release. The members of the board are appointed by the governor and confirmed by the senate. Each member serves a six-year term.[30]

The Community Justice Assistance Division

The Community Justice Assistance Division (CJAD) funds community corrections services. CJAD disburses state aid to local community supervision and corrections departments located throughout the state and establishes uniform state standards and guidelines for community supervision and corrections programs. CJAD does not directly administer programs or supervise offenders.[31]

The Community Justice Assistance Division disburses state aid and grants through three funding categories: basic supervision, diversion target programs, and community corrections programs. Basic supervision funding allows local community supervision and corrections departments to provide supervision and basic services to offenders. Diversion target programs and community corrections program funds, on the other hand, provide money for electronic monitoring, residential, and supplemental services. Community corrections program funds may also be used to supplement basic supervision funds. At the end of fiscal year 1994, 110,550 misdemeanants and 146,856 felons were under direct community supervision.[32]

The State Jail Division

In 1993, to ease overcrowding and facilitate the transfer of state prisoners housed in county jails, the 73rd Legislature created the state jail system to confine inmates convicted of state prison felonies, a class of nonviolent offenses. The 73rd Legislature also created the State Jail Division of TDCJ to manage the 22,000 beds located in the new state jail system. The state jail system attempts to ensure that criminals serve greater percentages of their sentences by making beds available for long-term prisoners. Also, with a relatively low construction cost, the state jail system is much less expensive than conventional prisons.[33]

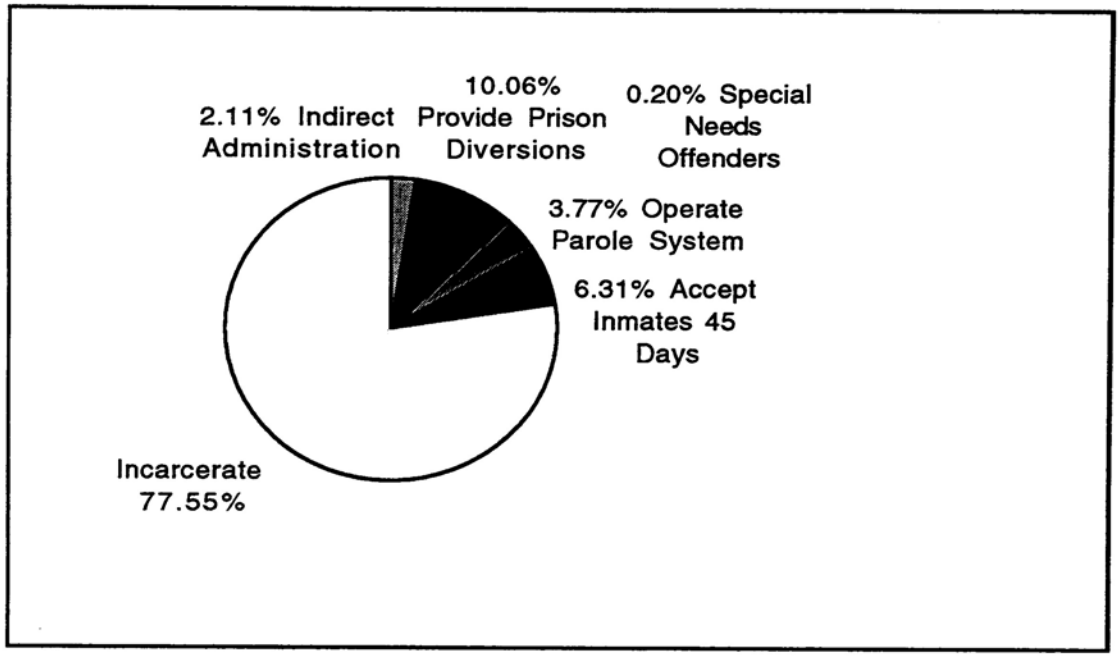
Legislative/State Budget Issues

The 74th Legislature appropriated $6.9 billion from its all-funds budget for public safety and criminal justice for the 1996-97 biennium. Of that amount, $5.7 billion came from Texas general revenue. TDCJ received approximately $4.5 billion, including almost 43,000 full-time equivalent positions. More than half of the funds appropriated to TDCJ are for the incarceration of felons, including operating the state jail facilities, educating and training inmates, and providing health care, psychiatric services, and substance abuse treatment for state prisoners (see figure 6.1). The General Revenue Fund is the single largest funding source for TDCJ expenditures.[34]

Although the current public safety and criminal justice appropriation of $6.9 billion represents only 8.6 percent of the total state all-funds budget (12.5 percent of the general

Figure 6.1

Goals as a Percentage of TDCJ Budget, 1996-97



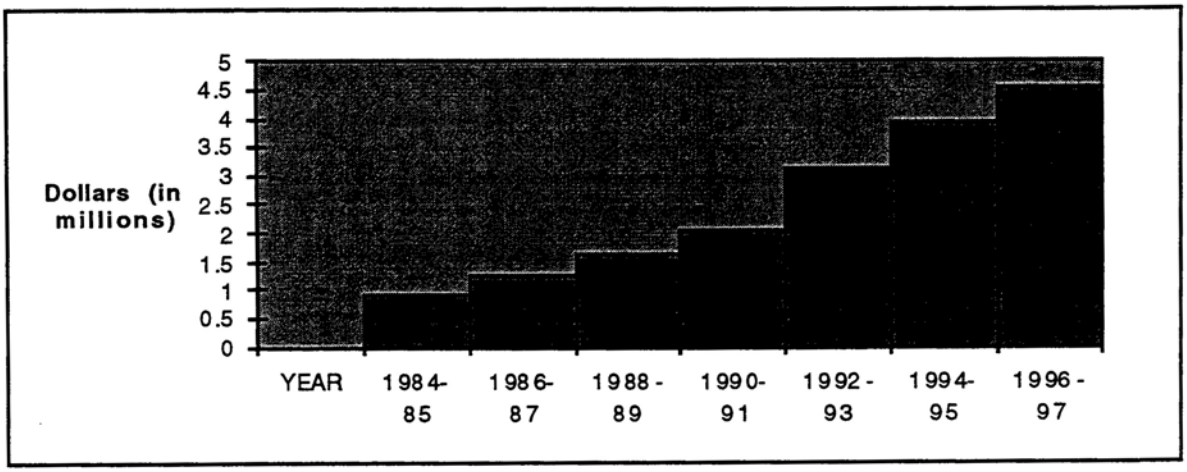
Source: State of Texas, *Supplement to House Journal, Seventy-Fourth Legislature, Regular Session, Text of Conference Committee Report, House Bill No. 1 (General Appropriations Act) and Governor's Veto Proclamation* (Austin, Tex., 1995), pp. V-12–V-16.

revenue budget), appropriations for criminal justice have skyrocketed in recent years and are expected to continue rising. From the 1984-85 biennium, appropriations for public safety and criminal justice have increased by almost $6 billion (see figure 6.2). More important, costs will continue to rise as the supply of prison space begins to fall behind demand.[35]

What factors are driving these costs? Why is Texas continuing to pay more for criminal justice each year? There are two primary reasons for the increase in appropriations for criminal justice. First, accommodating the increased number of prisoners in the conditions mandated by the *Ruiz* lawsuit required that Texas build new prisons and hire new staff. Second, as standards for prison construction and maintenance rose, the size of the prison population was expanding. The result was greatly increased operating costs for the Texas prison system.

Figure 6.2

Criminal Justice Appropriations, 1984-97



Sources: Texas Comptroller of Public Accounts, *Forces of Change,* vol. II, part I (Austin, Tex., 1993), p. 349; and the State of Texas, *Supplement to House Journal, Seventy-Fourth Legislature, Regular Session, Text of Conference Committee Report, House Bill No. 1 (General Appropriations Act) and Governor's Veto Proclamation* (Austin, Tex., 1995), pp. V-12–V-16.

Policy Options

In this era of fiscal austerity, every dollar counts. Texas must reduce the burden its criminal justice system places on the state budget. What follows are several options for relieving this burden.

1. Build more prisons.

   Cost $62 million per unit

   Construction of new prisons is expensive. Each new prison bed costs approximately $28,000, making the average cost to build a 2,200-bed unit approximately $62 million.[36]

2. Eliminate court residential treatment centers.

   Biennial savings $90.8 million

   The Court Residential Treatment Center Program provides supervision, specialized services, and treatment to felony and misdemeanor offenders with special needs. Treatment is provided for offenders with alcohol and drug dependencies, mental

impairments, and emotional problems.[37] In 1994, the state spent $64.26 per offender per day on treatment in court residential treatment centers. Eliminating this program, which serves up to 1,934 offenders, will result in annual overall savings of $45.4 million ($124,279 per day).[38]

3. Increase electronic monitoring.

Biennial savings $269.8 million

Electronic monitoring services provide a supervision tool to departments enabling them to monitor offenders who pose a risk to communities. Electronic equipment monitors the presence or absence of an offender at a specific location and time.[39] In 1994, electronic probation monitoring cost $13.4 million, or $7.42 per offender per day (program capacity of 4,970, total daily cost of $36,880).[40] In comparison, the cost of housing a state prison inmate was $44.40 per day. Thus, by using electronic monitoring instead of incarceration as a means of punishment, Texas could save $36.98 per inmate per day. If Texas shifted 10,000 prisoners to electronic monitoring, the resulting savings would be an estimated $369,800 per day.

4. Eliminate substance abuse treatment facilities.

Biennial savings $230 million

The substance abuse treatment facility program provides intensive treatment to as many as 4,047 offenders with serious substance abuse dependencies.[41] In 1994, treatment at substance abuse treatment facilities costs $78 per offender per day. Eliminating this program will result in biennial savings of more than $230 million ($315,666 per day).[42]

5. Increase the number of halfway houses.

Biennial savings $164 million

The halfway house program provides residential placement in communities to offenders released from prison. Inmates are released to halfway houses directly from the Institutional Division as a condition of parole, or as an alternative when the parolee is unable to develop or maintain a suitable residential plan.[43] In 1994, $35.42 was spent per day per offender receiving treatment at halfway houses. The program capacity of 5,521 offenders resulted in an overall cost of $195,550 per day and $71,377,140 per year.[44] In comparison, the cost of housing an inmate in prison was $44.40 per day. Thus, by using the halfway house program instead of incarceration as a means of punishment, Texas could save $8.98 per inmate per day. If the halfway house program were used for 25,000 prisoners a year, Texas could save an estimated $224,500 per day.

6. Increase private prison contracting.

   Biennial savings $547.8 million

   The cost of housing inmates in Texas' prisons costs $44.40 per day per inmate. In comparison, the cost of housing inmates in private prisons costs the state only $35.25 per inmate per day. Increasing the number of prisoners sent to private prisons would thus result in a savings of $9.15 per inmate per day. Private prisons are minimum security facilities. Approximately 70 percent (82,000) of all prisoners are eligible to be placed in private prisons. Moving an additional 82,000 prisoners to private prisons would save Texas an estimated $750,300 per year.

7. Initiate staff restructuring.

   Biennial savings $141 million

   Reducing management layers within prison security by eliminating the captain position and reducing security staffing levels by eliminating unnecessary positions and transferring these employees to other units will result in an estimated savings of $61,700,000 in the first year and $79,100,000 in the second year.[45]

Conclusion

Can Texas build itself out of its crime problem? Will funds be available for indefinite expansion of the prison system? Though most would agree that incarceration punishes criminals deservedly and protects law-abiding citizens rightly, Texas already operates one of the largest prison systems. In the future, Texas will face difficult decisions about state priorities. The information in this chapter is offered as a tool in that difficult decision-making process, an examination of Texas' past and present criminal justice policy that aims to aid an informed discussion about its future.

Notes

[1]Criminal Justice Policy Council, *Biennial Report to the Governor and the 74th Texas Legislature: The Big Picture Issues in Criminal Justice* (Austin, Tex., 1995), p. 1.

[2]Telephone interview by Clint Small with Mike Eisenburg, Criminal Justice Policy Council, Austin, Texas, April 15, 1996.

[3]Texas Comptroller of Public Accounts, *Forces of Change,* vol. II, part I (Austin, Tex., 1993), pp. 323-48.

[4]Pauline Arrillaga, "House Approves Bill to Overhaul Juvenile Justice System," *Austin American-Statesman* (May 26, 1995), p. B-2.

[5]U.S. Congress, Senate Judiciary Committee, "Overhauling the Nation's Prisons," testimony by James A. Collins, July 27, 1995.

[6]Arrillaga, "House Approves Bill to Overhaul Juvenile System."

[7]Lyndon B. Johnson School of Public Affairs, *Hard Choices: Setting Priorities for the Texas State Budget,* Policy Research Project Report Series, no. 112 (Austin, Tex., 1994), p. 74.

[8]Texas Comptroller of Public Accounts, *Behind the Walls: The Price and Performance of the Texas Department of Criminal Justice* (Austin, Tex., 1994), p. 7.

[9]Ibid., p. 8.

[10]Ibid.

[11]Ibid.

[12]Ibid., p. 9.

[13]Lyndon B. Johnson School of Public Affairs, *Hard Choices*, p. 74.

[14]Texas Comptroller of Public Accounts, *Behind the Walls,* p. 9.

[15]Ibid.

[16]Ibid.

[17]*Alberti v. Sheriff of Harris County v. Richards,* 937 F. 2nd 984 1000 (Fifth Cir. 1991), cert. denied, 112 S. Ct. 1994 (1992); and Texas Comptroller of Public Accounts, *Behind the Walls*, p. 9.

[18]Ibid., p. 10.

[19]Ibid.

[20]Ibid., p. 11.

[21]Ibid., p. 13.

[22]Legislative Budget Board, *Fiscal Size Up: 1994-95 Biennium, Texas State Services* (Austin, Tex., 1994), p. 8-12; and Criminal Justice Policy Council, *Testing the Case for More Incarceration in Texas: The Record So Far* (Austin, Tex., October 1995), p. 9.

[23]Legislative Budget Board, *Fiscal Size Up,* p. 8-12.

[24]Criminal Justice Policy Council, *Biennial Report to the Governor*, p. 16.

[25]Ibid.

[26]Ibid., pp. 16-17.

[27]Legislative Budget Board, *Fiscal Size Up,* p. 8-9.

[28]Criminal Justice Policy Council, *Texas Correctional Cost Per Day, 1993-94* (Austin, Tex., February 1995), pp. 42-43.

[29]Ibid., p. 44.

[30]Legislative Budget Board, *Fiscal Size Up*, p. 8-12.

[31]Criminal Justice Policy Council, *Texas Correctional Cost Per Day*, p. 35.

[32]Ibid., pp. 35-36.

[33]Legislative Budget Board, *Fiscal Size Up,* p. 8-12.

[34]Ibid., pp. 8-1, 8-5.

[35]Texas Comptroller of Public Accounts, *Forces of Change*, p. 349.

[36]Interview by Small with Eisenburg.

[37]Criminal Justice Policy Council, *Texas Correctional Cost Per Day*, p. 38.

[38]Criminal Justice Policy Council, *Recidivism as a Performance Measure: The Record So Far* (Austin, Tex., January 1996), p. 20.

[39]Criminal Justice Policy Council, *Texas Correctional Cost Per Day*, p. 38.

[40]Criminal Justice Policy Council, *Recidivism as a Performance Measure*, p. 20.

[41]Criminal Justice Policy Council, *Texas Correctional Cost Per Day*, p. 39.

[42]Criminal Justice Policy Council, *Recidivism as a Performance Measure*, p. 20.

[43]Criminal Justice Policy Council, *Texas Correctional Cost Per Day*, p. 46.

[44]Criminal Justice Policy Council, *Recidivism as a Performance Measure*, p. 21.

[45]Texas Comptroller of Public Accounts, *Behind the Walls*, p. 363.

Chapter 7. Other Agencies

Introduction

In his 1996 state of the union address, President Clinton declared that "the era of 'big government' is over." Although this sentiment has been expressed primarily regarding the federal government, some Texans are similarly inclined toward their state government, as was demonstrated by their voting to abolish the treasurer's office in November 1995. While such positions as state treasurer may appear redundant or unnecessary to the public, there are a significant number of agencies that serve as the foundation for Texas state government. Without funding for the legislature, governor, judiciary, comptroller, and many other offices and agencies, no government activities would take place. These "other agencies" that perform basic government functions are the subject of this chapter.

This chapter provides background information and the current budgetary status and trends of the state's general government, natural resources, and business and economic development agencies. It also includes a brief discussion of the efficiency initiatives included in the Texas Performance Review, policy options, and some concluding remarks.

Background

More than 100 Texas state government agencies fall under the heading of "other agencies." These agencies can be subdivided into six major categories: general government, natural resources, business and economic development, regulation, the legislature, and the judiciary. Comprising approximately 17 percent of the state all-funds budget in the 1996-97 biennium, and 5.6 percent of the state general revenue budget, other agencies play an essential role in Texas state government.[1]

Among these other agencies, business and economic development accounts for the largest amount of funding, with natural resources and general government accounting for most of the remainder. The other three categories—regulatory, the legislature, and judiciary—make up only 7 percent of the funding for other agencies, and only 1.1 percent of the total state budget.[2] Of the general revenue budget, these three agencies make up less than one-third of the funding for other agencies and 1.8 percent of the total general revenue state budget. Because of their relative budgetary insignificance, these three categories are not discussed in this chapter.

Current Status and Trends

The following subsections provide specific financial data for selected general government agencies as well as a discussion of recent funding trends.

General Government

The general government category includes agencies in all three branches of Texas state government relating to the general administration of government. As table 7.1 indicates, the trend in general government is toward a reduction in funding. This trend is notable in light of the fact that overall state spending in constant real dollars has increased steadily for more than a decade. The decrease in funding from the 1994-95 biennium to the 1996-97 biennium is $113.1 million, or 5.8 percent. This change in funding may be attributed to several factors, including substantial completion of the capitol restoration project, the transfer of programs to agencies outside the general government category, and a significant reduction in the number of state employees.[3] Certain selected agencies are discussed in greater detail below.

Office of the Attorney General

The attorney general (AG), elected to a four-year term, serves as the legal counsel to the governor, the legislature, and state agencies. The AG issues advisory legal opinions in response to inquiries from state officials, enforces state and federal child support laws and regulations, investigates Medicaid fraud, administers the Crime Victims Compensation Program, approves public bond issuances, and performs other duties as required by statute.[4] Funding for the 1996-97 biennium is $516.6 million, 16.7 percent more than the previous biennium.

One of the major roles of the AG's office is to enforce state and federal child support laws. Of the estimated $216.5 million in federal funds to be received by the AG's office for the 1996-97 biennium, $199.3 million are matching funds used by the AG as reimbursements for legal costs and fees related to child support enforcement.[5] Since 1993, the agency has been able to increase efficiency of collections, and continued increases are expected in the 1996-97 biennium.[6] Because of these continued improvements in efficiency, no changes in funding are recommended for the 1998-99 biennium.

Office of the Governor

The Office of the Governor was established to provide administrative support to the governor. The governor's duties include convening the legislature for special sessions, making state or district appointments, approving or vetoing bills passed by the legislature, and preparing a proposed budget.[7] The 1996-97 all-funds appropriation to the governor's office is $23.3 million, 28 percent more than the previous biennium.

In addition to the basic operation of the governor's office, the office administers many trusteed programs that are the responsibility of the governor but that are not assigned to an agency or board by law or executive order. Some of the programs administered by the governor's office include the Committee on People with Disabilities, Regional Grant Assistance Program, women's groups, and others. The trusteed programs have been appropriated $146.1 million from the all-funds budget for the 1996-97 biennium. Of these funds, $65.2 million are federal funds used by the Criminal Justice Division as seed money

Table 7.1

Appropriations for Selected General Government Agencies, 1994-95 and 1996-97

(in millions of dollars)

Agency	1994-95 All-Funds	1996-97 All-Funds	Change All-Funds	Percent Change All-Funds	1994-95 General Revenue	1996-97 General Revenue	Change General Revenue	Percent Change General Revenue
Office of Attorney General	442.6	516.6	74.0	16.7	50.7	61.3	10.6	20.9
Workers' Compensation	98.4	70.8	-27.6	-28.0	79.0	51.7	-27.3	-34.6
Comptroller of Public	305.7	308.0	2.3	0.8	305.3	307.5	2.2	.01
Uniform Statewide Accounting System	36.0	31.4	-4.6	-12.8	36.0	31.4	-4.6	-12.8
Advisory Commission on Emergency Communications	28.5	34.0	5.5	19.3	0.0	0.0	0.0	0.0
Office of the Governor	18.2	23.3	5.1	28.0	18.2	22.8	4.6	25.3
Governor's Trustee Funds	203.0	146.1	-56.9	-28.0	36.0	37.2	1.2	3.3
General Services	167.5	149.8	-17.7	-10.6	67.4	66.7	-0.7	-1.0
Treasury Department	84.4	76.0	-8.4	-10.0	0.0	0.0	0.0	0.0
Library and Archives	37.1	40.1	3.0	8.1	20.1	23.3	3.2	15.9
Secretary of State	31.7	35.2	3.5	11.0	28.3	32.2	3.9	13.8
Department of Information	19.6	17.8	-1.8	-9.2	5.7	6.4	0.7	12.3
State Preservation Board	73.3	5.3	-68.0	-92.8	72.3	5.3	-67.0	-92.7
Employee Benefits/Payroll	153.3	153.7	0.4	0.3	108.3	119.2	10.9	10.1
Lease Payments to the Public Finance Authority	23.7	27.6	3.9	16.5	23.5	27.6	4.1	17.4
Other	215.7	189.9	25.8	12.0	70.2	58.8	-11.4	-16.2
Total, General Government	1938.7	1825.6	113.1	5.8	921.0	851.4	-69.6	-7.6

Source: Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1995), p. 4-1, p. A-1.

Note: All agencies listed separately in this table have appropriations greater than $15 million. "Other" also includes nondiscretionary spending (e.g., payment of small miscellaneous claims—government code, sec. 403.074).

grants for criminal justice programs.[8] The federal funds are provided as a result of three federal laws: the Juvenile Justice and Delinquency Prevention Act, the Victims Assistance Act, and the Anti-Drug Abuse Act of 1988.[9]

General Services Commission

The General Services Commission (GSC) manages an integrated state purchasing system, maintains the capitol complex, oversees travel services for state agencies, and handles leasing and rental of office space for state agencies.[10] The 1996-97 all-funds appropriation for the GSC is $149.8 million, 10.6 percent less than the 1994-95 biennium.

Approximately $500,000 in federal funds have been appropriated to the GSC for the 1996-97 biennium to implement the National and Community Services Trust Act of 1993 (commonly known as "AmeriCorps"), which promotes volunteer and community services. Although the GSC has served as the state's liaison to the Federal Corporation for National Community Service since establishment of the program in 1993, House Bill 1863, passed by the legislature in 1995, has transferred this function to the newly established Texas Workforce Commission. No other federal funds are allocated to the GSC for the 1996-97 biennium.[11]

Comptroller of Public Accounts

The comptroller's office is responsible for accounting for the state's funds, serving as the state's principal tax administrator and collector, and for providing revenue estimation and certification. The comptroller is required by statute to provide a sworn financial statement to the legislature indicating the financial condition of the state at the end of each fiscal year as well as the expected revenues and expenditures for the current fiscal year. The comptroller must certify that the general appropriations bill is less than or equal to the amount available in all of the required accounting funds.[12] The 1996-97 all-funds budget appropriation to the Office of the Comptroller of Public Accounts is $308 million, 0.8 percent more than the previous biennium. None of these funds are from federal sources.

The comptroller's office performs an important task in state government operations by conducting the Texas Performance Review (TPR). The TPR has produced numerous recommendations that have been implemented by the legislature to improve the efficiency and effectiveness of state government in Texas. It is discussed in more detail later in this chapter.

Natural Resources

A number of state agencies manage and protect Texas' natural resources, including oil and gas, water, land, and minerals important to the state's economy. Table 7.2 shows total appropriations to all natural resources agencies. This section describes several noteworthy agencies.

Table 7.2

Appropriations for Natural Resources Agencies, 1994-95 and 1996-97
(in millions of dollars)

Agency	1994-95 All-Funds	1996-97 All-Funds	Change All-Funds	Percent Change All-Funds	1994-95 General Revenue	1996-97 General Revenue	Change General Revenue	Percent Change General Revenue
Department of Agriculture	47.7	49.3	1.6	3.4	37.6	40.1	2.6	6.9
Animal Health Commission	24.4	24.5	0.1	0.4	17.6	18.6	1.0	5.7
General Land Office and Veterans' Land Board	73.5	80.2	6.7	9.1	23.8	24.0	0.2	0.1
Parks and Wildlife Department	284.5	317.2	32.7	11.5	83.5	96.9	13.4	16.0
Radioactive Waste Disposal Authority	9.8	44.3	34.5	352.0	0.0	0.0	0.0	0.0
Railroad Commission	107.2	98.4	-8.8	-8.2	43.3	42.8	-0.5	-1.2
Natural Resource Conservation Commission	725.1	901.4	176.3	24.3	24.3	25.8	1.5	6.2
River Compact Commissioners	0.8	0.8	0.0	0.0	0.8	0.8	0.0	0.0
Soil and Water Conservation Board	14.9	16.8	1.9	12.8	11.9	14.1	2.2	18.5
Water Development Board	40.0	43.2	3.2	8.0	14.0	16.8	2.8	20.0
Other/Debt Payments	149.8	159.5	9.7	6.5	56.1	63	6.9	12.2
Total, Natural Resources	1,477.7	1,735.6	257.9	17.5	312.7	343.3	30.6	9.8

Source: Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1996), p. 9-1, p. A-6.

Texas Natural Resource Conservation Commission

The Texas Natural Resource Conservation Commission (TNRCC) was created on September 1, 1993, to consolidate the functions of the Texas Water Commission, the Texas Air Control Board, and other programs. TNRCC protects the environment by enforcing state and federal air and water laws.[13] There are tight restrictions on how

TNRCC can spend federal funds. TNRCC negotiates directly with the Environmental Protection Agency (EPA) on a grant-by-grant basis regarding expenditure restrictions.

TNRCC is in the unusual position of having fiscal security and promises of greater spending flexibility. Current federal appropriation legislation provides for the creation of three categories of grant administration in the environmental arena. These categories differ in the level of spending flexibility afforded states for the federal funds granted. The highest level of flexibility is given only to states that achieve the EPA's Performance Excellence Designation. This designation will be given only to states that display superior achievement in performing environmental duties.

If TNRCC achieves the Performance Excellence Designation, it will be given the latitude to use federal funds in accordance with state priorities, to lower grant administration costs, and to implement programs according to agency criteria. This could result in more flexibility in regulatory decisions and in prioritizing expenditures among its three functional areas (air, water, waste). The consolidation of TNRCC's 21 grant accounts into fewer funds could save indirect costs.

General revenue appropriated by the legislature accounts for only 4.7 percent of TNRCC's budget. User fees earmarked for environmental purposes and other receipts make up 76.6 percent of its budget. Legislative discretion over environmental appropriations is minimal because revenue is usually dedicated by source for a particular purpose or purposes, but TNRCC has proposed that the legislature eliminate general revenue appropriations in exchange for greater latitude in spending user fees. If the general revenue appropriation were eliminated, the corresponding increase in spending flexibility must occur to sustain water programs that are currently funded almost exclusively through general revenue. Funds from other appropriation categories would need to be used to fund the water programs.[14]

Soil and Water Conservation Board

The Soil and Water Conservation Board has been in existence since 1939. This agency promotes the prudent utilization of Texas' water and soil. In 1994-95 the board received approximately $1.3 million in federal funds while in 1996-97 this amount increased 87.7 percent to approximately $2.4 million.[15]

This increase in funding is attributable to a federal pollution abatement grant. No further increases in federal funding are anticipated. Federal funds are not legally applicable to the board's administrative costs, so the increase in federal funds will not decrease the necessary level of general revenue. The bulk of federal funding received by the Soil and Water Conservation Board is passed through to other state agencies and local governmental entities to fund projects involving section 319 of the Federal Clean Water Act.

Water Development Board

In 1957, Texas voters approved a constitutional amendment creating the Texas Water Development Board (TWDB). Under this amendment the TWDB was authorized to issue

up to $200 million in general obligation bonds to develop a revolving fund. The revolving fund is used to provide financial assistance to eligible political subdivisions for water projects. Additionally, TWDB provides statewide coordination of long-term water management strategies.[16]

TWDB received $10.7 million in federal funds in the 1994-95 biennium and $9.8 million in the 1996-97 biennium, an 8.2 percent decrease. This decrease was partially due to a federal grant received in 1994-95 but not renewed in 1996-97.

Federal funding to TWDB will decrease further in the 1998-99 biennium due to a cost recovery bill passed by the U.S. Congress. This law requires TWDB to finance the administrative cost associated with the State Revolving Fund program, which will incur a $1-2 million loss. Though this fund is not reflected in the appropriations bill, it is the TWDB's largest federal program. Last year the program received $135 million which TWDB then passed on to localities.[17]

Business and Economic Development

The largest 1996-97 appropriation among other agencies is for business and economic development, which makes up 11 percent of the all-funds state budget.[18] Most of these funds, however, are federal funds. Business and economic development funds represent only a small portion of the general revenue budget. These agencies are important not only for providing direct services to Texans but also for promoting economic growth in Texas. One major change in this area was the creation of the Texas Workforce Commission by the 1995 legislature. In addition to other functions, the Texas Workforce Commission is now responsible for administering federal Joint Training Partnership Act funds. Table 7.3 shows total appropriations to all state business and economic development agencies in Texas. The agencies that receive federal funds were chosen for closer review. This section describes several noteworthy agencies.

Texas Department of Transportation

In 1991, the legislature merged the State Department of Highways and Public Transportation, the Texas Department of Aviation, and the Texas Motor Vehicle Commission into the Texas Department of Transportation (TxDOT). The Texas Turnpike Authority will become part of TxDOT in 1997. [19]

TxDOT serves 25 geographical districts through 18 functional divisions organized into seven directorates. Transportation Planning and Development handles environmental functions; construction and maintenance duties fall under Field Operations; Multimodal Transportation oversees the intracoastal canal, public transportation, and aviation; and Motorist Services deals with permits, licensing, and registration. Human Resources, Staff Services, and Administrative Services are the other three functional areas of TxDOT.[20]

Table 7.3

Appropriations for Business and Economic Development, 1994-95 and 1996-97

(in millions of dollars)

Agency	1994-95 All-Funds	1996-97 All-Funds	Change All-Funds	Percent Change All-Funds	1994-95 General Revenue	1996-97 General Revenue	Change General Revenue	Percent Change General Revenue
Texas Aerospace Commission	0.0	0.4	0.4	N/A	0.0	0.4	0.4	N/A
Department of Commerce	523.3	669.1	145.8	27.9	37.0	42.9	5.9	15.9
Texas Employment Commission	497.0	492.3	-4.7	-0.9	25.6	0.0	-25.6	-100
Department of Housing and Community Affairs	380.1	369.8	-10.2	-2.7	18.5	7.9	-10.6	-57.3
Lottery Commission	425.6	545.4	119.9	28.2	3.6	5.5	1.9	52.8
Department of Transportation	6,026.7	6,322.9	296.2	4.9	6.4	18.1	11.7	182.0
Council on Workforce and Economic Competitiveness	3.1	0.0	-3.1	-100.0	[a]0.0	[a]0.0	0.0	0.0
Employee Benefits/Payroll Expenses	383.3	383.7	0.4	0.1	3.6	4.0	0.4	11.1
Debt Service	0.0	0.4	0.4	N/A	0.0	0.4	0.4	N/A
Total, Business and Economic Development	8,239.1	[b]8,784.0	544.9	6.6	94.7	79.2	-15.5	-16.4

Source: Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1995), pp. 10-1, A-6–A-7.

[a]Insignificant funding.

[b]The 1996-97 amount does not include $25 million appropriated to the Texas Workforce Commission pursuant to the enactment of Senate Bill 596. This agency was created in 1995 by the 74th Legislature and, as a result, consolidated approximately 20 workforce development programs previously administered by the Department of Commerce, the Texas Employment Commission, and various other state agencies.

The legislature appropriated $6.3 billion to TxDOT for the 1996-97 biennium, or 4.9 percent more than the previous biennium. This appropriation is 7.9 percent of the total all funds state budget. Of this amount, only $18 million will come from Texas general revenue. In addition, TxDOT received $2.6 billion in federal funds, or 40 percent of the agency's entire budget. The federal authorization for Texas transportation funding will not be reviewed until 1997, so no major changes in federal funding will occur in the current biennium.[21] TxDOT officials predict, however, that federal funding will decrease in the 1998-99 biennium.[22]

In anticipation of possible changes and encouraged by the current discussion in the federal government, state governments are making suggestions regarding the restructuring of federal funding into the block grant format. The key factor with respect to federal transportation funding for Texas is that it is a net donor state. This means that Texas remits more motor fuel tax revenue to the federal government than it receives in federal dollars. Due to Texas' size in terms of geography and population, it consumes more motor fuel relative to other states. Whereas Texas can support its own highway system, smaller states cannot. Texas, therefore, must contribute more money to the federal highway system than some other states. In 1992, Texas ranked second among the 50 states in contributions to the Federal Highway Trust Fund.[23]

Donor states are primarily interested in getting back the money they pay into the federal system. Some donor states are interested in having a formula set by the federal government for payments into the federal highway system. After money is paid in, any additional money remitted to the federal government would be returned to the states through federal appropriations. If this is not possible, donor states want more latitude in spending the funds they do receive because specific federal expenditure requirements may not mesh with the needs of individual states. Should block grants decrease federal funding, the Texas legislature might be forced to consider raising the rates of the state motor fuel taxes. This could lead to further disparity among state motor fuel tax rates, an issue often discussed by donor states with high motor fuel tax rates.

Political opposition to greater spending latitude for the states stems from the fact that some federal funds are appropriated directly to local governments for their transportation needs and merely pass through state budgets. Local governments currently receiving funding in this way are concerned that, if given greater autonomy, states will decrease funding to local governments or change the expenditure requirements associated with those funds. In short, state control could diminish local autonomy with regard to transportation funds.

Department of Commerce

The Texas Department of Commerce was created in 1987 to build strategic partnerships that create economic opportunity and prosperity for all Texans. The department is governed by a nine-member board and an executive director, all appointed by the governor. The department's major functions are business development and tourism.

The commerce department aims to improve the state's economy through business creation, retention, and expansion as well as through diversification of the state's economic base.

The agency provides business and economic analysis through a series of information-sharing programs to Texas communities and to businesses seeking to locate in Texas. The agency also manages federal and state financial incentive programs, including the Texas Capital Fund and the Texas Rural Economic Development Fund.[24]

Another goal of the commerce department is to enhance the growth of the Texas economy through tourism development and the marketing of Texas as a travel destination. The Tourism Division promotes the state as a travel destination through national and international channels, and the staff coordinates buyer tours to educate tour operators and travel agents. The department estimates that $680 million in travel expenditures were generated from advertisements placed by the agency, supporting 13,546 Texas jobs.[25]

House Bill 1863, passed by the legislature in 1995, removed the Texas Department of Commerce's responsibility for overseeing the workforce development functions of the agency. All funding from the federal Job Training Partnership Act (JTPA) was transferred to the new Texas Workforce Commission. This has reduced the size of the department considerably, and while it still receives federal funding for the Texas Manufacturing Assistance Center, most of its federally funded functions are gone.[26]

Texas Workforce Commission

The Texas Workforce Commission was established in 1995 to consolidate the functions of more than 20 workforce development and training programs into one agency. Previously these functions had been spread among eight separate agencies.

Among federally funded programs, the commission will inherit all of the JTPA programs, the low-income child care program, the jobs program, and the Food Stamps Employment and Training programs. There are some state employment programs as well, but these account for only 9 percent of all employment services.[27]

Currently the commission receives about $800 million, the majority if which comes from federal sources. It is uncertain how changes at the federal level will affect the commission's programs and clients, but one estimate from the agency forecast a 40 percent reduction in the current level of funding.[28]

Efficiency Issues

Many attempts at fiscal reform in the areas of general government and other agencies have been limited to identifying potential efficiency improvements. Starting in 1991, the comptroller's office was given authority by the legislature to conduct periodic performance reviews to identify such improvements. The first Texas Performance Review, *Breaking the Mold: New Ways to Govern Texas*, was completed that same year.[29]

The most recent TPR, *Gaining Ground: Progress and Reform in Texas Government*, was released in November 1994. The report contains more than 400 recommendations that would save the state approximately $2.1 billion in 1996-97. The recommendations

specifically related to general government would provide an estimated savings of $350.9 million. Other recommendations in *Gaining Ground* that could save money for other agencies are grouped in the Employee Issues and Cross Government Issues categories. If implemented, these recommendations could save the state of Texas $878 million and $200,000, respectively, for the 1996-97 biennium.[30]

Some of the recommendations in *Gaining Ground*, however, are not quantifiable in dollars. For example, the potential savings related to abolishing the treasurer's office (overwhelmingly approved in a statewide vote on November 7, 1995) cannot be determined precisely. Estimates for such savings may vary widely depending on who is performing the budget analysis. Furthermore, many of the other TPR recommendations have little or no effect on the total state budget. This lack of overall impact on the budget will be more apparent in the future as it becomes more and more difficult to find significant savings through incremental efficiency improvements. Although attempts to improve the efficiency of general government are admirable and should be continued, their effects on the overall state budget are fairly insignificant when compared to policy options that affect spending in other high-cost programs, such as health and human services. For these reasons, policymakers should minimize their dependence on the TPR as the key to savings in the Texas state budget.

Policy Options

Despite the relatively insignificant budgetary impact of further cuts to general government, this section presents a few policy options that are available to increase savings for the state. Changes in the funding and organization of the natural resources agencies would increase their efficiency and save general revenue expenditures. In addition, increases in TxDOT's funding base would help alleviate reductions in federal transportation funding to that department. The savings associated with the changes listed below would be significant within this sector of government and would contribute to its greater efficiency and effectiveness.

1. Eliminate the general revenue appropriation to TNRCC in exchange for greater flexibility in spending its user fees.

   Biennial savings $25.8 million

   One benefit of this option is that it is supported by TNRCC itself. While most of the commission's funding comes in the form of federal grants and assistance, it does receive 4.7 percent of its funding from state general revenue. A large portion of its funding, 76.6 percent, comes from fees and other receipts. The TNRCC is appropriated revenue from approximately 20 accounts or funds dedicated by statute and is a party to over 50 federal grant agreements to fund its operations. Legislative discretion over environmental appropriations is minimal, but TNRCC has proposed that the legislature eliminate general revenue appropriations in exchange for greater latitude in spending user fees. The state would save $25.8 million in general revenue under this proposal, but legislative oversight of the expenditure of user fees

would be limited. If the general revenue appropriation were eliminated, a corresponding increase in spending flexibility would have to occur to sustain water programs currently funded almost exclusively from general revenue. Funds from other appropriation categories would need to be used to fund the water programs.

2. Merge the Soil and Water Conservation Board and the Texas Water Development Board with TNRCC.

   Biennial savings $2 million

   Because of the similarity in each of these agencies' mission statements and program objectives, merging them is logical. A merger would streamline this sector of state government and increase the efficiency of the natural resources agencies. In addition, this would save state money needed to offset federal funding cuts. Federal funding to the Water Development Board will decrease in the 1998-99 biennium due to a cost recovery bill passed by Congress. This law requires the TWDB to finance the administrative costs associated with the State Revolving Fund program, which will mean a $1-2 million loss to TWDB. If the three agencies were merged, this loss could be offset by placing TWDB within the administrative structure of TNRCC.

   A possible drawback to this option is that it would give too much control to one agency, or that efficiency might actually be reduced by placing too many programs within the confines of one organization. The implementation of this option might also be politically unpopular with the individual leaders and constituencies of the agencies to be merged.

3. Raise motor fuel taxes by 1 cent per gallon to compensate TxDOT for any reduction in federal funds.

   Biennial savings $88.6 million

   In the 1996-97 biennium, TxDOT received 40 percent of its entire budget—$2.6 billion—from the federal government. The current prediction by TxDOT officials, however, is that federal funding will decrease in the 1998-99 biennium. In order to maintain current funding levels without increasing TxDOT's dependence on general revenue funds, the motor fuels tax rates could be increased by 1¢. This would increase biennial funding to the transportation department by $88.6 million. In addition, because 75 percent of motor fuels tax revenue constitutionally goes to TxDOT and the other 25 percent is allocated to the Available School Fund, this tax increase would benefit education as well.

   Although the motor fuels taxes historically are a stable revenue source, they also are regressive taxes. Increasing the rates places more of a burden on those who can least afford it. In addition, Texas' gasoline tax rate already is higher than the national average, and increasing it further would aggravate this disparity, as well as

motorists who often must drive long distances traversing the largest of the 48 contiguous states.

Conclusion

The category of other agencies encompasses a wide variety of agencies and functions essential to the everyday operation of Texas state government. Although political trends currently favor the "downsizing" of government agencies, there is a limitation to budget cuts that can be made to these basic administrative functions. While the Texas Performance Review, for example, is an admirable project aimed at increasing efficiency throughout state government, significant savings through incremental efficiency improvements will be harder and harder to achieve with each new review.

This chapter has outlined three policy options for the areas of natural resources and business and economic development, including two areas where savings and efficiency may be achieved. While they may not be significant in the overall state budget picture, these options could provide important savings within the category of other agencies.

Notes

[1]Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1995), p. 1-2.

[2]Ibid.

[3]Ibid., pp. 1-7, 1-10, 4-1.

[4]Lyndon B. Johnson School of Public Affairs, *Guide to Texas State Agencies* (Austin, Tex., 1994), pp. 44-50.

[5]Tex. House Bill I, 74th Leg. (1995).

[6]Legislative Budget Board, *Fiscal Size Up*, p. 4-4.

[7]Ibid., p. 23.

[8]Tex. House Bill I, 74th Leg. (1995).

[9]Legislative Budget Board, *Fiscal Size Up,* p. 4-21.

[10]Ibid., pp. 111-12.

[11]Tex. House Bill I, 74th Leg. (1995).

[12]Legislative Budget Board, *Fiscal Size Up,* p. 67.

[13]Ibid., pp. 164-65.

[14]Interview by Kathy Donellan and Caroline West with Jeff Grymkoski and John Janeck, Office of Administrative Services, Texas Natural Resource Conservation Commission, Austin, Texas, November 13, 1995.

[15] Legislative Budget Board, *Fiscal Size Up,* pp. 9-1, 9-22.

[16]Ibid., pp. 9-23–24.

[17]Rhonda Goike, Accounting Division, Texas Water Development Board. Answer to survey conducted by Kathy Donellan and Caroline West, February 22, 1996.

[18]Legislative Budget Board, *Fiscal Size Up,* p. 1-2.

[19]Ibid., p. 10-8.

[20]Ibid.

[21]Interview by Kathy Donellan and Caroline West with Tonia Ramirez, Policy Analyst, and David Soileau, Federal Policy Analyst, Texas Department of Transportation, Austin, Texas, November 11, 1995.

[22]Telephone interview by Kathy Donellan with Tonia Ramirez, Policy Analyst, and David Soileau, Federal Policy Analyst, Texas Department of Transportation, Austin, Texas, February 26, 1996.

[23]Ibid.

[24] Legislative Budget Board, *Fiscal Size Up,* p. 10-2-3.

[25]Ibid., p. 10-3.

[26]Ibid.

[27]Telephone interview by Caroline West with Steve Hudson, Director of Finance, Texas Workforce Commission, Austin, Texas, February 27, 1996.

[28]Ibid.

[29] Texas Comptroller of Public Accounts, *Breaking the Mold: New Ways to Govern Texas* (Austin, Tex., 1991).

[30] Texas Comptroller of Public Accounts, *Gaining Ground: Progress and Reform in Texas Government,* vol. 2 (Austin, Tex., November 1994), pp. iii, 683-85.

Chapter 8. Conclusion

As this report shows, each budget area faces unique pressures. All areas, however, share limitations on resources and an uncertain future. Although Texas cannot prepare for every potential budget crisis, it can be wise in its preparation for making the difficult decisions.

Whatever Texas does, it probably will have to do it without the benefit of the same level of federal funds, which have become this state's largest single source of revenue. Though the difficulties of reaching a budget agreement in 1996 have postponed the effects of any block grants or budget cuts that Congress might adopt, it is likely that the federal-state fiscal relationship will change. Because of the variety of proposals before Congress, predicting exactly what Texas' position will be is difficult. Most likely, Texas and the rest of the states will have to learn to do more with less. Texas is fortunate in that the legislature and several state agencies have already undertaken numerous efforts to streamline state government and make it more efficient. Efforts by state agencies have made Texas a leader in the pursuit of effective, efficient public service. As federal funds decrease, emphasis on quality and effectiveness must continue in order to serve the public's needs.

This study has been an attempt to understand and explain the dilemmas Texas faces and what different choices will mean for the state budget. The policy options outlined in this report are examples of the trade-offs that will exist as demands increase and revenues decrease.

We have attempted to present a survey of Texas' current fiscal situation and those trends that will come to bear on future budget decisions. The participants in this policy research project hope that their efforts will make it easier for those responsible to make those decisions and for those affected to understand them.

Appendix A. The Texas State Budget Cycle

Overview

Four distinct phases make up the state budgeting process in Texas: preparation, consideration, execution, and audit/evaluation. State agencies often are involved in multiple phases simultaneously for different programs, such that the budget is an ongoing process, rather than simply an exercise that policymakers and agency executives must undertake during each legislative session.

Preparation

Each new budget cycle begins in February/March in even-numbered years. At this point in time, budget instructions are sent to each agency. Based on these instructions, agencies prepare a Legislative Appropriation Request (LAR), which is submitted to the Legislative Budget Board (LBB) and the Governor's Budget and Policy Office (GBPO) in June (see figure A.1).

Once the LAR is submitted, LBB and GBPO staff analyze the request and conduct public hearings for consideration of the agencies' proposed budgets. The LBB staff prepares its own set of recommendations and the LBB meets to act on those recommendations. The last few months of the year are spent preparing an appropriations bill that the LBB will submit to the legislature in January of the following (odd-numbered) year, when the legislature begins its regular biennial session.

Consideration

The consideration phase begins when the legislature meets in regular session in January of odd-numbered years. The LBB-submitted appropriations bill is considered by the Senate Finance Committee, and various substantive committees in the house, including the House Appropriations Committee. Each chamber then votes on its version of the appropriations bill. If there are differences between the two versions, then the bill is sent to a conference committee made up of members of both houses. Once a committee budget is agreed to by the conferees, it is sent to both houses for approval.

After the budget is passed, the Comptroller of Public Accounts is required to certify that funds are available to enact the budget. If the comptroller does not certify the bill due to insufficient revenue or funds, the legislature may override the comptroller's decision with a four-fifths vote. Finally, the certified budget is sent to the governor for his or her signature. The governor may choose to veto all or portions of the bill; the legislature can override

such a veto with a two-thirds vote.

Execution

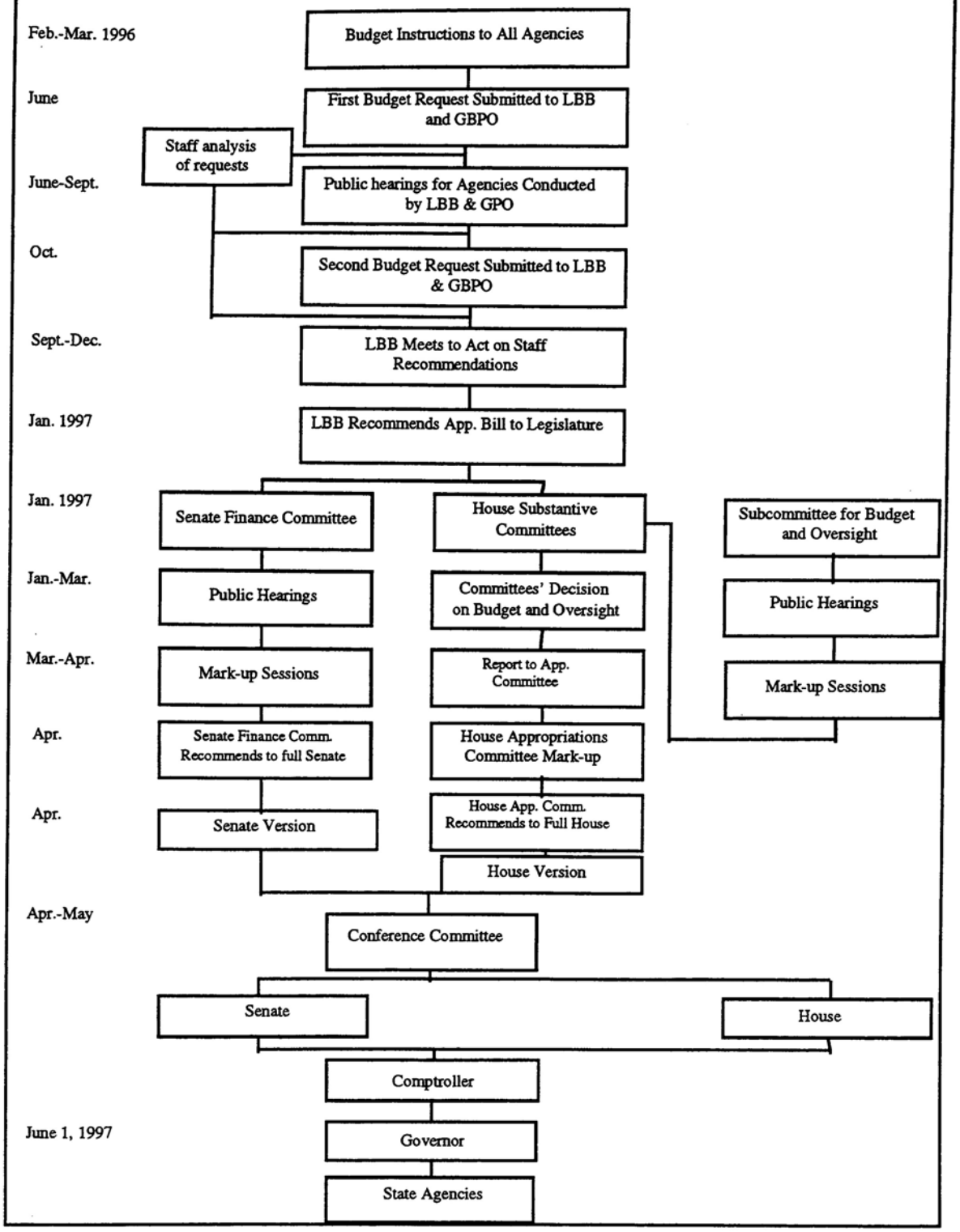
The execution phase of the budget occurs on September 1 of the same year in which a new budget is enacted. At the beginning of this fiscal year, the comptroller makes the appropriate amounts of funding available to state agencies to implement their programs. The comptroller monitors disbursements throughout the fiscal year to prevent overspending.

Budgets may be adjusted between legislative sessions if necessary. Changes of no more than 10 percent of an agency's budget may be requested by the governor, with the LBB approving or rejecting the recommendation. The LBB may also recommend budget changes in the interim, with those recommendations approved or rejected by the governor.

Audit/Evaluation

Following the end of a fiscal year, the LBB and state auditor perform audits on state spending for the fiscal year. The LBB evaluates the effectiveness and efficiency of agency programs by observing how well performance measures in the budget have been met. This performance monitoring is an ongoing process, and agencies are required to report their progress on a quarterly basis. When the next budget cycle begins, the legislature will take into account the performance of agencies when allocating funds in the appropriations bill.

Figure A.1 Texas Biennial Budget Cycle



Appendix B. State Rankings for Selected Financial Information

Table B.1

Per Capita State Tax Revenue for the 15 Most Populous States, 1993

State	Tax Revenue per Capita in Dollars
1. Washington	1,694.36
2. North Carolina	1,404.87
3. Massachusetts	1,727.12
4. California	1,561.58
5. New York	1,719.59
6. Michigan	1,390.29
7. Pennsylvania	1,377.87
8. Indiana	1,210.45
9. Georgia	1,178.31
10. New Jersey	1,653.21
11. Florida	1,199.45
12. Ohio	1,153.04
13. Illinois	1,239.62
14. Virginia	1,166.51
15. Texas	1,011.63

Source: Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1996), p. 3-4.

Table B.2

Per Capita State Expenditures for the 15 Most Populous States, 1993

State	Expenditures per Capita in Dollars
1. New York	4,082
2. New Jersey	3,671
3. Massachusetts	3,586
4. Washington	3,426
5. California	3,350
6. Ohio	2,855
7. Michigan	2,854
8. Pennsylvania	2,852
9. Indiana	2,474
10. North Carolina	2,436
11. Illinois	2,405
12. Virginia	2,268
13. Georgia	2,213
14. Florida	2,201
15. Texas	2,168

Source: Legislative Budget Board, *Fiscal Size Up: 1996-97 Biennium, Texas State Services* (Austin, Tex., 1996), p. 3-10.

Table B.3

State Medicaid Spending for the 15 Most Populous States, 1992

State	State Expenditures in Dollars
1. New York	15,281,047,394
2. California	8,691,730,347
3. Texas	4,406,614,843
4. Ohio	4,307,723,124
5. Illinois	4,070,009,564
6. Pennsylvania	3,546,869,899
7. Florida	3,518,403,365
8. Massachusetts	3,247,725,692
9. Michigan	2,801,998,826
10. New Jersey	2,801,587,341
11. Indiana	2,224,817,348
12. Georgia	2,149,142,492
13. North Carolina	2,083,160,750
14. Virginia	1,750,331,670
15. Washington	1,735,022,726

Source: Kathleen O'Leary Morgan, Scott Morgan, and Neal Quitno, eds., *State Rankings: 1994* (Lawrence, Kans.: Morgan Quitno Corporation), p. 488.

Table B.4

State Spending on Aid to Families with Dependent Children for the 15 Most Populous States, 1992

State	State Expenditures in Dollars
1. California	5,828,300,000
2. New York	2,927,200,000
3. Michigan	1,162,000,000
4. Ohio	984,000,000
5. Pennsylvania	906,100,000
6. Illinois	882,600,000
7. Massachusetts	750,900,000
8. Florida	733,100,000
9. Washington	605,900,000
10. Texas	516,500,000
11. New Jersey	515,700,000
12. Georgia	420,300,000
13. North Carolina	335,300,000
14. Virginia	224,800,000
15. Indiana	218,200,000

Source: Kathleen O'Leary Morgan, Scott Morgan, and Neal Quitno, eds., *State Rankings: 1994* (Lawrence, Kans.: Morgan Quitno Corporation), p. 477.

Table B.5

Per Capita State Public Education Spending for the 15 Most Populous States, 1993

State	Per Capita Expenditures for Public Education in Dollars
1. New Jersey	1,351
2. New York	1,265
3. Michigan	1,155
4. Washington	1,131
5. Pennsylvania	1,096
6. Texas	1,049
7. Indiana	1,029
8. Ohio	1,024
9. Virginia	940
10. California	919
11. Massachusetts	913
12. Illinois	865
13. Florida	864
14. Georgia	834
15. North Carolina	818

Source: Edith R. Hornor, ed., *Almanac of the 50 States: Basic Profiles with Comparative Data Tables*, 1995. (Palo Alto, Calif.: Information Publications, 1995), p. 432.

Table B.6

Per Capita State Higher Education Spending for the 15 Most Populous States, 1991

State	Per Capita Expenditures for Higher Education in Dollars
1. Washington	382.34
2. Michigan	349.46
3. Indiana	349.38
4. North Carolina	346.46
5. California	330.45
6. Virginia	328.14
7. Texas	282.06
8. Ohio	276.60
9. Georgia	232.77
10. New Jersey	228.16
11. New York	222.97
12. Illinois	222.38
13. Massachusetts	204.62
14. Florida	203.27
15. Pennsylvania	157.15

Source: Victoria Van Son, *CQ's State Fact Finder: Rankings across America* (Washington, D.C.: Congressional Quarterly, Inc., 1993), p. 127.

Appendix C. Creating Your Own Budget for Texas with TBS

The Texas Budget Simulator (TBS) is intended to be an educational tool that creates an environment similar to the one that legislators, particularly those on the Texas Senate Finance and House Appropriations Committees, encounter in drafting a biennial budget. TBS users will discover some of the restrictions, usually contained in state and federal constitutions and statutes, that constrain many budget decisions.

TBS is not intended to replicate the state budget prepared by the Legislative Budget Board. Of necessity, it is not comprehensive and is confined to major budget items of revenue and expenditure. Major items of expenditure include general government, criminal justice, health and human services, public education, and higher education. Major items of revenue include both tax and nontax categories. Numbers in the policy options are estimates made by the policy research group with advice from the Legislative Budget Board and the Comptroller of Public Accounts.

The Location on the Web

The Texas Budget Simulator can be accessed on the World Wide Web via the address http://uts.cc.utexas.edu/~wphwebpb/tbs.html.

The Home Page

The address above is the home page of the Texas Budget Simulator and includes links to the *Texas in Transition* home page, a guest list, and a credit page for contributors. The links appear in blue until they have been selected, after which time they will turn purple. The home page image is illustrated in figure C.1.

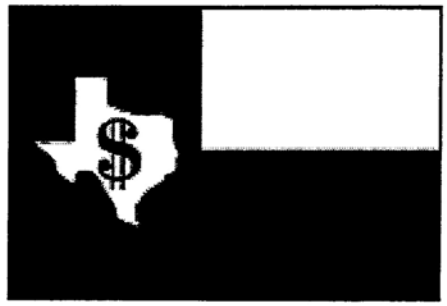
The Simulator

Select the Run the Budget Simulator button to go to the main Budget Simulation web page with the Texas state budget. The Texas Budget Simulator has most of the budgetary categories and line items in the State of Texas budget. Budget categories are listed under the headings of Expenditures or Revenues.

The Texas Budget Simulator includes only state funds, or general revenue, that the state legislature would control. Again, the real state budget includes federal funds, but these funds have been excluded here because state legislators cannot change federal spending.

Figure C.1

Texas Budget Simulator Home Page Image



The Texas Budget Simulator

Version 2.0

Welcome to the home of the Texas Budget Simulator (TBS). This simulation gives virtual bureaucrats and legislators like yourself the opportunity to change the state's biennial budget.

To continue, please select one of the following items:

Run the Budget Simulator	**The Texas in Transition Home Page**	**Please sign our guestbook**	**Contributors and sponsor**

At any time you can select an item highlighted in blue for more information on that item.

The legislative budget for the 1996-97 biennium and the projections for the 1998-99 biennium can be viewed on this page. The Modified Expenditures 1998-99 category will display the user's budget after changes are made.

TBS has two types of web pages: Budget Category pages, which provide background information on each category; and corresponding Line Items pages, which list the specific budgetary line items that fall under each category. By reviewing information on the Budget Category pages, the user can learn more about the broad categories of expenditures made in the state budget. The user can then create his or her own simulation budget by going to the Line Item pages for each category to make changes.

The Object of TBS

The object of TBS is simply to *balance the budget.* The main budget simulation page screen shows the budget totals for the current and future biennium. Once a user makes changes, he or she will be able to see the resulting impact on the overall budget. The user will see the message Surplus in black for a budgetary surplus or Deficit in red if the budget is in deficit.

Texas, like most states, requires the legislature to balance the budget. In Texas, this is known as the pay-as-you-go principle. Officials must rely on revenue estimates from the state comptroller's office to correctly gauge the revenue from a specific tax. Revenues from taxes in TBS are based on estimations calculated by the student research group.

Major budget categories displayed on the main budget simulation page include health and human services, public education, higher education, criminal justice, other agencies, and three revenue categories.

A user will start on the main budget simulation page listing the categories under Expenditure and Revenue. To go to the Budget Category page for a particular category, such as health and human services, select the category name. Background information on that area will appear. When finished with this information, return to the main Budget Simulation page.

To go to the Line Item page for a category, select the circle next to the category name in the Items column. Once you have selected the circle, go to the bottom of the page and press the Get Subcategory button. The Line Item page for that category will appear listing from left to right the item name, the 1996-97 budgeted amount for that item, the 1998-99 projected amount, the 1998-99 modified amount, and the available ways to modify the 1998-99 projected amount (the modifiers column). A user works on this page to make changes to projected spending or revenues for each line item. Once changes are made and saved, the new budget level for that line item will be shown in the 1998-99 modified column.

Remember: At any time, an item highlighted in blue can be selected for more information.

Changing Expenditures and Revenues

The Texas budget is created every two years and, therefore, choices in TBS are limited to the 1998-99 biennium. Expenditures and revenues can be changed with the Modifiers in the right hand column of each Line Item page. There are two types of modifiers: an Item Multiplier and Yes/No options. The Item Multiplier allows the user to change overall spending or revenue for a particular item. The Multiplier represents the percent level at which the user feels the item should be funded. The multiplier ranges from 0.0 or 0 percent (unfunded expenditures and abolished taxes or revenue sources) to 2.0 or 200 percent (doubling the expenditures or revenue source requirements). For example, to cut spending

for a particular item by 50 percent, select 0.5 from the pull-down menu next to the words "item multiplier." To increase spending by 25 percent, select 1.25 as the Item Multiplier. Similarly, to decrease revenues from a particular tax (decrease taxes), select an Item Multiplier less than 1.0, or to increase revenues (raise taxes), select an Item Multiplier greater than 1.0.

Instead of using the Multiplier, users can select specific Yes/No options. For each line item, options are listed below the Item Multiplier. These options are suggestions based on the *Texas in Transition* research group findings. The option name will appear in blue, indicating that more information is available by selecting the option name. Each option has a corresponding Yes and No next to it. If you wish to adopt or accept an option, select the circle next to the word Yes. If you do not select an option, the default, a filled circle next to No, will remain. More than one Yes/No option may be selected, but an option and the Multiplier cannot be used at the same time.

Changes made through the Multiplier or option selection are not saved until the Save Changes button at the bottom of the page is selected. When finished making changes on a page, go to the bottom of the page. Two choices are available to the user: the changes will be saved, the totals for that page will be recalculated, and the user will stay on the same page; or changes will be saved, the totals for the entire budget will be recalculated, and the user will be returned to the main budget simulation page. The default selection, to stay on the same page, is shown on a button at the bottom of each Line Item page. The user can simply select the Save Changes button immediately to the right to recalculate that page and remain. To recalculate the entire budget and return to the main page, press on the Calculate and Stay button. The other option, to Calculate and Return will appear. Move to Calculate and Return, and select. Press the Save Changes button again. The user will be taken back to the main budget simulation expenditure and revenue page and be able to see if the changes made have moved the modified budget closer to a surplus or more deeply into a deficit.

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