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Published by the Caesar Rodney Institute

RELEASE: CRI - Center for Economic Policy and Analysis

RE: Does Governor Markell deserve a "D"?

DATE: 11/9/2012

In their recent "Fiscal Report Card on America's Governors," the CATO Institute gave Delaware's Governor Markell a "D". The basis for the grade was that over the past four years the Governor has increased taxes (i.e., personal income, gross receipts, corporate franchise, cigarettes) while plunging ahead on state spending.

Is a "D" a fair grade?

First, the responsibility for the grade of "D" must be shared equally with the state legislature. The legislature passed all the tax increases and all the state budgets. And other constituencies in Delaware share part of the responsibility as well. The Delaware State Chamber of Commerce, for example, did not oppose any of the tax hikes.

Second, is an increase in taxes such a terrible thing? Every credible analysis of the differences among states' economic growth rates shows that relatively higher taxes deter growth. Analysis of 20 years of Delaware data by the CRI produces the same result.

Over the past two decades every increase in Delaware's top personal income tax rate has subsequently decreased employment and every decrease has spurred employment. Based upon average relationships, the 17% hike in the state's top personal income tax (from 5.95 to 6.75) will over time reduce employment by 7%, or 28,000 jobs, all other things being constant.

Similarly, over the past two decades every increase in Delaware's gross receipt tax rate for retail trade has subsequently reduced employment throughout the state and every decrease has been followed by gains in employment. Again, based upon average relationships, the 31% increase in the retail trade gross receipts tax rate (from .576 to .7543) will eventually lead to a 15% drop in employment, or over 60,000 jobs, all other things being constant.

This is why the CATO Institute looks dimly on states that raise taxes, especially during recessions.

Third, can state government be expected to cut spending when so many state services are essential? The reality is that Delaware state government has been on a spending binge. Over the past decade (FY-03 to FY-13) state spending from Delaware General Fund has risen 50%.

Over this same decade Delaware personal income has increased 45%, with earned income up only 32% and transfer payments up 116%. Total employment in Delaware has been flat and inflation (prices) is up only 30%. In other words, spending from the General Fund has out-stripped inflation, population (a 10% increase), and the economy.

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Wouldn't it be difficult to identify areas of state services that might be candidates for cuts? Over the decade just four areas of state government have accounted for more than 83% of the absolute dollar rise in General Fund spending.

The Department of Health and Social Services led the pack with an increase of $415 million. Especially notable were the 97% increase in General Fund Medicaid spending ($306 million), a 120% jump in spending on facility operations, and a 780% increase in welfare (Temporary Assistance to Needy Families).

The $374 million rise in General Fund spending by the Department of Education was accounted for primarily by a 118% jump in personnel costs. This is unusual given that total public school enrollment fell over this decade and inflation was only 30%.

State debt service, excluding schools, soared from $3 million to $146 million as Delaware hit the top five among all states in debt per capita.

Finally, personnel costs in the Delaware Department of Corrections rose 48% and spending on medical services jumped 117%.

While state employees in the Delaware Office of Management and Budget and the Department of Finance are far more qualified to identify specific areas of spending that seem to be substantially out of control, just a cursory examination raises some questions.

What about going forward? Has state government learned some lessons? Perhaps.

State spending for the current fiscal year is expected to go up slower than the expected tax revenues flowing into the General Fund. Borrowing is projected to ease up. On the other hand, no serious efforts are underway to deal with neither runaway Medicaid costs nor looming health care costs for retirees and a rising pension fund shortfall.

At the same time, the Governor and legislature are entertaining delays in the roll backs intended to occur in both the top state personal income tax rate and the gross receipts tax rates. Hopefully, this will just end up being talk.

As the CATO Institute observes, "Intense global economic competition makes it imperative that states improve their investment climates." This includes broad based tax reform, holding the line on spending, addressing future state employee benefit liabilities, and serious school reform.

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