Montana Policy Institute

Policy Analysis: SB0245 – Content of Fiscal Notes

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SENATE FINANCE & CLAIMS
Exhibit No. 3
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Bill No. SB 198

Background: The Montana Policy Institute (MPI) is providing this analysis of SB0245 as a means to better evaluate policy options for improving the accountability of state government. This analysis does not endorse or oppose SB0245 or any other proposed legislation. Its purpose is to discuss the Bill's primary components in the context of MPI's research into the topic, and in light of MPI's desire to make Montana government fiscal information and the impacts of government actions easily accessible to its citizens.

Discussion: SB0245 would alter the substance of fiscal notes drawn up as a result of proposed legislation in two significant ways. First, fiscal notes would go beyond static measures of direct expenditures and/or revenues to include follow-on effects based upon behavioral changes brought about by the legislation. Second, the bill would require that fiscal notes "estimate costs that will occur to the private sector as a result of the policy changes in the bill." Both of these measures would significantly enhance the public's understanding of a proposed Bill's true costs and benefits by acknowledging the self evident truth that people react to incentives and disincentives. In the case of fiscal or regulatory stimuli, they will alter their behavior in ways that may offset (or enhance) the proposed legislation's intended effects. The following is a section by section analysis of the draft.

SB0245 would require fiscal notes to consider fiscal impacts beyond immediate revenues and expenditures. In addition, fiscal notes would estimate costs to the private sector of policies under consideration.

Section 1: Amends MCA 5-4-201 to incorporate changes outlined in MCA 5-4-205 as amended.

Section 2: Section 5-4-205 proposed amendments:

1. Requirement to estimate changes in behavior that would occur as a result of policy changes, and the resulting fiscal impact of those behavioral changes:

    a. Static analyses of fiscal effects resulting from a policy change do not take into account the longer term impact of behavioral changes by the public in reaction to the new policy. Put simply, people react to incentives and disincentives. This reaction can alter the impact of the original action. If the cost – however measured – of a thing goes up people will "use" less of it. If the cost goes down, people will "use" more of it. In the case of fiscal matters, this often results in counterintuitive outcomes, especially with regard to tax policy.

        i. In the 1980s, the federal government cut the top personal income tax rate from 70% to 28%. This along with other tax reductions resulted in significant increases in savings and investment. The resulting economic upturn caused federal tax receipts to almost double from $517 billion to $1,032 billion.[1]

        ii. Federal tax receipts increased more than 40% from 2003-2006 following a reduction in dividends tax rates from 39.6% to 15% and capital gains from 20% to 15%, among other cuts.[2]

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b. Static analysis also does not account for changes in behavior among government entities and employees. Texas recently put into place a web site where government employees (and the public) could access detailed information about state expenditures. While the cost of implementing this web site was about $400,000, direct savings resulting from employees' ability to see, optimize, and consolidate costs across offices resulted in nearly $9 million dollars of documented savings, more than offsetting the web site's cost. These savings would not have been captured with fiscal note procedures like those currently used in Montana.

2. SB0245 also would require fiscal notes to include estimated costs to the private sector as a result of policy changes. Whether resident in SB0245 or not, capturing these costs is a necessary measure to quantify the true cost of regulation and government intervention.

Static analysis does not account for changes in behavior based on policy initiatives that often result in counter-intuitive outcomes.

Policies that increase costs to businesses hide the costs of policies in product pricing and inhibit a true cost/benefit analysis.

a. In the case of policy changes that increase costs to businesses through reporting requirements, compliance costs, and other real expenditures, the government is simply placing a tax on the public and using business as a collector by forcing them to incur costs that are then passed on to the consumer. This hides the true cost of policies by including them in the price of items sold. The costs associated with a policy should be open and transparent so that citizens can do an explicit cost/benefit analysis on the policy's merits.

b. In the case of policy changes that directly or indirectly increase costs to taxpayers, again through stipulations like reporting requirements or compliance expenditures, these costs should be explicitly included in fiscal notes that describe costs and benefits to Montanans.

c. Similar arguments hold true for legislation favoring businesses or individuals. Fiscal notes should recognize and articulate savings that will be incurred by or benefits that will flow to private entities as a result of policy changes.

Conclusion: SB0245 would increase legislators' ability to see the potential short and long term fiscal impacts of policy proposals under consideration. The Montana Policy Institute believes that these measures will be effective as far as they go and will provide more tools for citizens and leaders to make informed decisions about the costs and benefits of specific legislation. The long term effects of individuals and businesses reacting to incentives and disincentives have the proven potential to offset and even exceed short term fiscal impacts from taxing and spending policies. MPI believes that every effort should be made to capture all costs and benefits flowing from policy decisions to allow a more informed and focused debate.

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[1] Arthur B. Laffer and Stephen Moore, *Rich States Poor States* (Washington D.C.: American Legislative Exchange Council, 2007), p. 40.

[2] Ibid.

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