

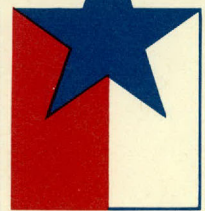
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TEXAS RESEARCH LEAGUE

RESEARCH FOR A BETTER TEXAS



ANALYSIS

Number of State Employees Keeps on Growing -- Total Surpasses 254,000

During the past few years, the corporate byword has been "downsizing," as one after another business giant has announced significant employee reductions. Generally, this has been accomplished by moving to a leaner, flatter organization and curtailing the number of middle management positions -- doing more with less.

This has not been the pattern in the case of Texas state employee ranks, where the numbers have moved ever upward -- topping the 254,000 mark last August, the close of the 1993-94 fiscal year.

The state comptroller has proposed that, with some exceptions, all state employment be capped at the levels in effect in February, 1996. See the related story on page 2.

State Property Tax Abatement Policy Could Make the State Less Competitive

In crafting the school finance law (SB 7), the legislature included a provision requiring property tax values subject to new tax abatements to be included when calculating per-student property wealth.

Above and below average wealth school districts object to this provision for different reasons. Wealthy districts would have to write bigger checks to the state; poor districts would see their state aid reduced.

Under present law, no abatement can be granted without participation -- and on the same terms -- by all local taxing jurisdictions. Thus, without school district participation, tax abatement agreements could not be implemented.

There is evidence that the financial consequences are such that school districts are going to be increasingly wary about granting abatements. See story on page 5.

OTHER LEAGUE REPORTS

The Expansion of Choice in Texas: The Availability and Use of Current School Choice in Texas Public Schools looks at the variety of options now used by schools to give parents and students some choice in education alternatives. Different approaches used in other states also are examined.

The TAAS Test as a Diagnostic Tool focuses on a different aspect of this controversial exam. Amid all of the critical discussion, little attention is paid to how it can be used to benefit students. The test should be an important tool to identify areas where students need extra attention, or where the curriculum and teaching methods need modification.

These and other reports are available to League supporters at no charge, and to the public at-large for a nominal charge.

1117 RED RIVER
P. O. BOX 12456
AUSTIN, TX 78711
512/472-3127
FAX: 512/472-4816

State Employment Tops 254,000; Comptroller Proposes Cap

In 1988 - the first year in which an accurate count of the number of state employees was available - state employment totaled slightly less than 204,000. Over the next six years, the state added 50,345 employees, bringing the total to just above 254,000 - an increase of 24.7% (see table on page 3).

Population growth often is cited as one reason for adding to the state workforce; providing services to a larger number of people equates to higher employment levels. But the simple fact is that the number of state

employees is growing considerably faster than is the state's population (see Table 1). The 24.7% state employment growth contrasts to a 9.2% (16.8 million to 18.4 million) population increase. This means that between 1988 and 1994 the state added 326 employees for each 10,000 increase in population.

1988	121.02
1989	123.69
1990	128.43
1991	129.31
1992	133.62
1993	136.35
1994	138.24

WHERE EMPLOYMENT HAS INCREASED

Three functional areas -- Law Enforcement and Corrections, Higher Education, and Health & Human Services -- dominate the employment growth picture. In combination, these three accounted for 95.4% of employee increases in the past six years. Looking closer at these areas gives some insight into the forces that have driven state employment. (See Table 2.)

Law Enforcement/Corrections. Two factors have been at play in this area. First, as a result of the *Ruiz* federal lawsuit, the state was forced to increase the ratio of corrections officers to inmates. Second, there has been a growing number of felons sentenced to prison.

Between 1988 and 1994, the Texas prison population doubled from 39,664 to 79,439. During the same period, the number of FTE state employees in this functional area grew by roughly 93% (see Chart 1). Moreover, this growth pattern is not expected to change in the near future; by

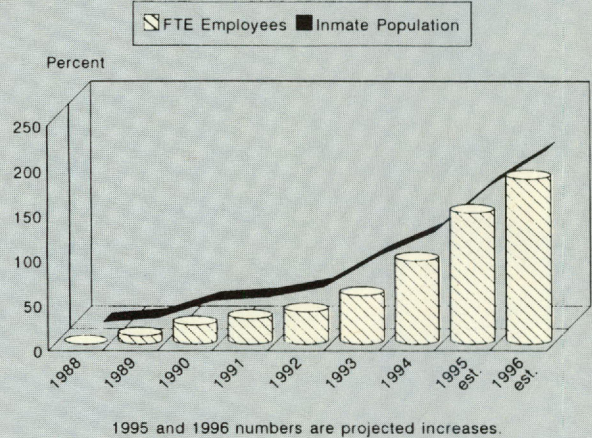
Table 2
Growth in State Employment, 1988 - 1994

	Growth	%
General Government	1,489	3.0%
Regulatory Agencies	(279)	(0.6)
Health & Human Services	13,882	27.6
Transportation	(1,283)	(2.5)
Law Enforcement/Corrections	19,600	38.9
Higher Education	14,544	28.9
Public Education	196	0.4
Natural Resource Agencies	1,815	3.6
Legislative	357	0.7
Judicial	26	0.1
Total	50,345	100.0

1996, the prison population and the number of employees are expected to almost double from 1994 levels.

Health & Human Services. Federal legislation has expanded the list of Medicaid eligibles for which the state must provide services. Including programs covering food stamps, AFDC, aged and disabled, aid to women and children, and child protective services, the number receiving state services increased from 3.0 million in 1988 to 5.7 million in 1994 -- up about 89%.

Chart 1
Cumulative Percentage Increases in FTE Employees
and Inmate Population, 1988-94
TEXAS DEPARTMENT OF CRIMINAL JUSTICE



Number of Full-time Equivalent State Employees for the Quarter Ending August 31, 1988-1994

RECAP	8/31/88	8/31/89	8/31/90	8/31/91	8/31/92	8/31/93	8/31/94	Change From 1988 to 1994	
								Number	Percent
EXECUTIVE BRANCH:									
GENERAL GOVERNMENT									
Texas Employment Commission	4,850	4,672	4,473	4,544	4,971	5,175	4,684	(166)	-3.4%
Comptroller of Public Accounts	2,851	2,936	2,934	2,883	3,151	3,168	2,797	(54)	-1.9%
Purchasing & General Services Commission	800	840	860	825	727	763	859	60	7.5%
General Land Office/Veterans Land Board	598	633	623	677	586	642	657	59	9.8%
Texas Department of Agriculture	591	591	588	539	522	522	511	(81)	-13.6%
Other General Government	2,690	2,829	3,033	3,793	4,063	4,125	4,362	1,671	62.1%
Subtotal	12,380	12,501	12,511	13,261	14,021	14,395	13,869	1,489	12.0%
REGULATORY									
Texas State Board of Insurance	1,198	1,552	1,610	1,694	1,308	1,143	924	(273)	-22.8%
Railroad Commission of Texas	892	886	898	899	982	1,018	965	73	8.2%
Texas Alcoholic Beverage Commission	689	682	730	724	689	655	525	(164)	-23.8%
Other Regulatory	1,404	1,392	1,341	1,375	1,398	1,421	1,489	85	6.1%
Subtotal	4,183	4,512	4,580	4,691	4,377	4,237	3,903	(279)	-6.7%
HEALTH AND HUMAN SERVICES									
Texas Department of MHMR	27,138	27,393	27,977	28,574	29,325	29,222	28,201	1,062	3.9%
Texas Department of Human Services	14,003	14,738	16,104	17,820	20,460	16,378	18,134	4,131	29.5%
Texas Protective & Regulatory Services						5,910	6,525	6,525	
Texas Department of Health	3,855	4,139	4,412	4,740	4,889	5,537	5,799	1,944	50.4%
Texas Rehabilitation Commission	1,970	2,076	2,080	2,244	2,245	2,089	2,439	469	23.8%
Texas Commission for the Blind	461	472	501	532	541	560	556	95	20.7%
Other Health and Human Services	711	717	756	818	799	886	366	(345)	-48.5%
Subtotal	48,138	49,535	51,831	54,730	58,259	60,583	62,020	13,882	28.8%
TRANSPORTATION									
State Department of Hwys & Public Trans.	17,699	17,667	17,317	16,402	16,125	16,687	16,418	(1,280)	-7.2%
Other Transportation	218	229	266	252	221	229	215	(3)	-1.3%
Subtotal	17,916	17,896	17,583	16,654	16,347	16,916	16,633	(1,283)	-7.2%
LAW ENFORCEMENT & CORRECTIONS									
Texas Department of Criminal Justice	17,376	18,955	21,104	22,336	23,662	26,815	33,455	16,080	92.5%
Texas Department of Public Safety	5,088	5,108	5,455	5,409	5,647	5,753	5,994	906	17.8%
Office of Attorney General	1,605	1,984	2,372	2,580	3,177	3,540	3,625	2,021	125.9%
Texas Youth Commission	1,639	1,677	1,871	1,916	2,017	2,048	2,118	480	29.3%
Other Law Enforcement & Corrections	495	500	524	501	624	627	610	115	23.2%
Subtotal	26,203	28,224	31,325	32,742	35,127	38,784	45,803	19,600	74.8%
HIGHER EDUCATION									
Academic Institutions	49,841	51,170	52,680	53,324	55,880	56,096	56,016	6,175	12.4%
Medical Facilities	28,614	29,332	30,029	30,890	33,549	35,589	36,459	7,844	27.4%
Other Higher Education	5,779	5,971	6,051	6,110	6,218	6,333	6,303	524	9.1%
Subtotal	84,234	86,473	88,760	90,324	95,647	98,019	98,778	14,544	17.3%
PUBLIC EDUCATION									
Texas State Technical Institute	1,556	1,858	1,785	1,724	1,519	1,532	1,592	36	2.3%
Texas Education Agency	899	942	1,047	1,100	1,063	1,073	1,055	156	17.3%
Texas School for the Deaf	484	476	501	497	380	416	413	(71)	-14.7%
Other Public Education	333	427	424	430	433	433	408	75	22.6%
Subtotal	3,272	3,704	3,757	3,751	3,395	3,454	3,468	196	6.0%
NATURAL RESOURCES									
Texas Parks & Wildlife Department	2,827	2,636	2,916	2,837	2,979	3,039	3,008	181	6.4%
Texas Natural Resource Conser. Comm.	1,249	1,322	1,507	1,487	2,084	2,560	2,797	1,548	124.0%
Other Natural Resources	255	264	295	293	298	324	340	85	33.5%
Subtotal	4,331	4,221	4,718	4,618	5,360	5,923	6,145	1,815	41.9%
LEGISLATIVE									
	1,672	1,849	1,824	2,265	2,054	2,190	2,029	357	21.3%
JUDICIAL									
	1,392	1,252	1,281	1,306	1,337	1,346	1,417	26	1.8%
TOTAL	203,720	210,166	218,169	224,343	235,923	245,847	254,065	50,345	24.7%

Source: Office of the State Auditor, Classification Office, Quarterly. Quarterly Report of Full-Time Equivalent State Employees, Quarter Ending August 31, 19__.

Correspondingly, FTE state employment for these functions grew 76% (see Chart 2).

Higher Education. The drivers here are patient loads in teaching hospitals and student enrollment in both medical and academic institutions. On the academic side, the number of students grew 5.5% (385,000 to 406,000) between 1988 and 1994. FTE employees at the public universities increased by a little more than 12% during that same period (see Chart 3). Most of that growth (enrollment and employment) occurred between 1988 and 1992; in the next two years enrollment showed slight declines and employment stayed about level.

It is interesting to note that only about 31% of public university employees are involved in instruction. Comparable figures for some other large states are Indiana, 42%; Illinois, 40%; New York, 39%; and Pennsylvania, 36%.

COMPTROLLER PROPOSED CAP

In *Gaining Ground*, the 1994 Texas Performance Review report, the comptroller proposed that:

Texas should cap state government employment in executive-branch agencies and institutions of higher education. Only positions necessary to the maintenance of public safety should be exempted. This new baseline for state employment should be accomplished no later than February 29, 1996.

The comptroller suggests that the goal "is to maintain levels of service while reducing the number of managers and supervisors, **not frontline employees.**" A rider to implement this recommendation, with an estimated \$300 million in savings, is included in the 1996-1997 appropriation bill now under consideration in the legislature.

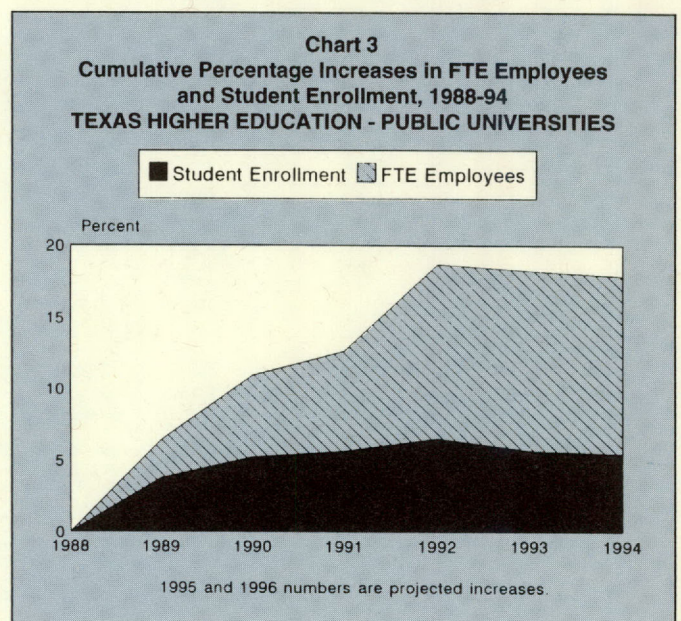
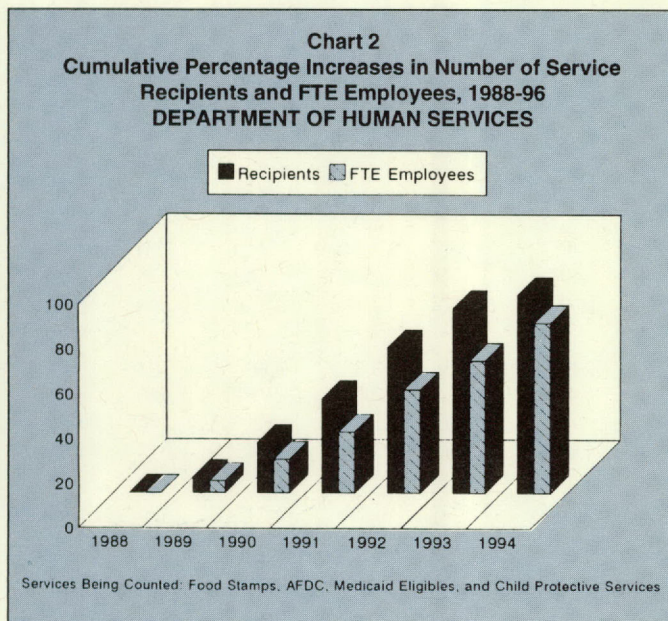
The Texas Department of Transportation is a good example of what can be accomplished. Between 1988 and 1994, TDOT reduced its employment level by almost 1,300, 7.2%. This was done by better use of technology and by increased reliance on private contractors.

The comptroller's suggestion, and TDOT's performance are right in line with what has been happening in the state's business sector. One executive expressed the business approach as follows:

We have outgrown the manufacturing mentality of a chain of command style....We are all focused on forming teams...where the team is measured rather than the individual. We need to apply the business unit mentality to state government immediately.

Other businessmen, coming out of recent corporate downsizings, noted that:

If the state measures outcomes based on numbers served rather than the quality of the service, based on the number of permits issued rather than the shortened life cycle of the permitting process, then public sector reinvention is nothing more than window dressing.



Tax Abatement Policy in Texas

*About This Article -- This is a summary of the League report, **Tax Abatement Policy in Texas**. The full report is available to League supporters at no charge, and to others for a nominal charge. The present property tax abatement policy could have an adverse impact on the ability of local governments to compete for new industry or for expansion of existing businesses. Several alternatives for changing the abatement policy are discussed.*

BACKGROUND

The 1995 Texas legislative session will be an important one for economic development policy in general, and for ad valorem property tax abatement issues in particular. *First*, the tax abatement statute, the Property Redevelopment and Tax Abatement Act ("Chapter 312"), expires September 1, 1995, and is scheduled for sunset review. *Second*, the new school finance law ("SB7"), which contains a provision requiring abated property values to be included when calculating per-student property wealth, is expected to come under question from a variety of business, education and economic development leaders.

TAX ABATEMENT PRACTICES IN TEXAS

As a business incentive, tax abatement, total or partial property tax exemption, is particularly popular in state-designated *enterprise zones*-economically depressed areas which offer a variety of state and local incentives. In fact, according to the Texas Department of Commerce, tax abatements made up 94% of the \$75.58 million spent in enterprise zones on local incentives in FY 1993.

This report examines the tax abatement practices in communities that have both enterprise zones and Enterprise Projects (qualified businesses that locate in an enterprise zone and are eligible for certain state and local tax incentives). Participating communities are required by law to develop a tax abatement policy, or "Guidelines and Criteria." The policies adopted in Texas enterprise zones vary significantly in both scope and sophistication; however, at least five elements are typically included.

1. The type of property eligible for abatement:

Real property tax abatement is specifically authorized in all zones; personal property tax abatement is authorized in only 51% of the zones.

2. The type of industries eligible for tax abatement:

One-half of the surveyed zones specifically limit industry eligibility. Among the most widely authorized industry types are manufacturing, transportation, communications, utilities and regional services.

3. The amount of investment required to be considered for tax abatement incentives:

Economic threshold criteria for job creation, capital investment, projected added property value, and/or projected increases in local annual payroll are employed in 87% of the zones. Full-time permanent job creation and capital investment are the most widely employed criteria.

4. The maximum length of the abatement period and the maximum percentage of taxes subject to abatement:

In the sampled communities, tax abatement periods range from a high of ten years (the legal maximum) to a low of five.

5. The method of determining the value of the tax abatement:

Approximately one-third of the zones determine tax abatement value predominantly on a case-by-case basis. The remaining zones have established specific (and in some cases elaborate) tax abatement schedules and guidelines.

THE IMPACT OF SB7 ON SCHOOL DISTRICT PARTICIPATION IN TAX ABATEMENTS

Senate Bill 7 introduced a major shift in economic development and tax abatement policy. It requires that property values subject to tax abatement agreements executed on or after May 31, 1993, be included when calculating wealth-per-student levels.

From an economic development perspective, three questions are particularly compelling.

1. First, how many tax abatements have been granted since the passage of SB7?

In the 82 surveyed enterprise zones, 78 offer tax abatement as a business incentive. Of these zones, 56 (72%) reported *pre-SB7* school tax abatement activity in their jurisdiction. However, only 16 of these same 56 enterprise zones (28%) reported *post-SB7* school tax abatement activity. A total of 30 tax abatements were granted during the first full year following the passage of SB7 (May 31, 1993 to May 31, 1994).

2. Second, has SB7 influenced the behavior and/or decision-making processes of local school administrators and economic development officials regarding the use of tax abatement? If so, how?

A telephone survey of 15 of the 19 school districts that reported post-SB7 tax abatements suggests that the SB7 tax abatement provision has significantly impacted the way tax abatements are considered and/or executed in Texas. The 15 school districts that have granted post-SB7 tax abatements may be classified into four categories:

A. Category One-No New Abatements:

Three districts reported that they did not anticipate granting any new tax abatements because of the financial hardships imposed by SB7.

B. Category Two-Conservative and Cautious:

The three districts that granted post-SB7 tax abatements for relatively small projects indicated that they plan to approach larger tax abatement projects with considerably more caution.

C. Category Three-Recapture Lost Funding:

Three districts plan to continue granting tax abatements, but have inserted "reimbursement clauses" in their tax abatement Guidelines and Criteria and/or agreements. These give school districts the option of requiring businesses to reimburse the school districts either for any losses in state aid or for any increased payments resulting from higher wealth per-student calculations.

D. Category Four-Continued Abatements:

Six districts reported that they will continue to grant abatements despite the financial ramifications of SB7. Of these six school districts, four are located in newly created

enterprise zones where the momentum for economic development activity is quite high. SB7 did not play a major role in tax abatement negotiations in these districts.

3. Third, has SB7 caused a decline in the number of tax abatements granted by Texas school districts?

A simple time-series analysis tracking the number of tax abatements granted by school districts between 1990 and the first full year following the passage of SB7 shows that school participation in tax abatement has dropped rather significantly since the passage of SB7. However, this decline may be attributed, at least partially, to other factors.

POLICY ALTERNATIVES TO CONSIDER

The Chapter 312 Question

In the general area of tax abatement policy and Chapter 312, four possible approaches are offered.

1. Extend Chapter 312:

Property tax abatement is an important economic tool and is offered by many of Texas' major competitor states. The legislature might consider extending Chapter 312 until the end of the decade, during which time the necessity and prudence of tax abatement could be better evaluated.

2. "Unhook" Taxing Jurisdictions:

Under the tax abatement law, school districts and counties must adopt abatement terms identical to those of cities, although cities are less dependent on the property tax for revenue. The legislature might consider amending the law to authorize taxing entities to grant tax abatements on terms that best suit their individual financial status. This approach would allow school districts to adopt less financially demanding abatement terms, and as a result, to possibly approve tax abatement requests that would otherwise have been rejected because of fiscal limitations.

3. Mandate Economic Feasibility Study:

A large number of taxing jurisdictions do not perform a comprehensive economic feasibility or impact analysis study before granting a tax abatement. The legislature might consider mandating comprehensive studies so that communities will develop a better understanding of the costs and benefits associated with granting a tax abatement.

4. Penalize Non-Compliant Taxing Entities:

A large number of taxing jurisdictions do not report reinvestment zone and/or tax abatement activity to the Texas Department of Commerce (TDOC) as required by law. To improve the quality and availability of data on tax abatement activity, the legislature might consider imposing a financial and/or administrative penalty on taxing jurisdictions that fail to report tax abatement activities to TDOC.

THE SB7 QUESTION

When reconsidering the SB7 impact on tax abatements, seven policy alternatives are offered.

1. Status Quo:

One alternative is to keep the SB7 tax abatement provision intact. This approach may encourage school districts to approach tax abatement applications with more prudence and deliberation. Keeping SB7 intact also addresses school finance equity and cost-containment concerns. However, the SB7 tax abatement provision apparently has had a negative impact on economic development activity in Texas.

2. Tax Abatement Provision Removal:

A second alternative is to remove the SB7 tax abatement provision and to return to the pre-SB7 tax code authority. This approach will have a positive effect on economic development activity and will enhance Texas' position in the highly competitive realm of industry relocations. However, removing the SB7 tax abatement provision might cause equity and cost-containment problems.

3. Cap Tax Abatements:

A third alternative is to remove the SB7 tax abatement provision and to establish a cap on the percentage of property value that a school district may legally abate. This approach might encourage school districts to evaluate tax abatement requests more carefully and could limit a wealthy district's ability to participate in excessive tax abatement agreements in an attempt to lower taxable property values. However, the utilization of a cap is a two-edged sword. If the cap is set too high, it might undermine the twin goals of SB7 (lower state expenditures on education and equitable school financing); if the cap is set too low, it would have little positive economic development benefits.

4. Shift Economic Development Costs:

A fourth policy alternative is to keep the SB7 tax abatement provision intact but to offer businesses relief from some other state tax such as the corporate franchise tax. This approach recognizes that the state also benefits from local economic development and should assume some of the related costs. Although this approach might be in accord with the equity (and perhaps the cost-containment) goal of SB7, the application of this measure is somewhat limited since the corporate franchise tax is the only broad-based business tax in Texas and franchise tax reductions already are offered as a major state incentive for Enterprise Projects. Moreover, not all businesses in Texas are incorporated.

5. Decrease Impact of SB7:

A fifth alternative is to amend SB7 to require the commissioner of education to include only a portion of tax abatement value when calculating school district assigned property values. This approach would reduce the impact of SB7 by a set percentage (e.g. 50%), and might satisfy economic development, school finance equity and cost-containment objectives.

6. Company Reimbursement for Education Costs:

Another alternative is to require companies that enjoy tax abatement benefits to reimburse local school districts for the costs of educating the children of their employees. This measure would help restore some of the competitiveness of Texas' tax abatement policy by making abatements more affordable for school districts and more accessible to industry.

7. Establish State-Wide Competition:

A final alternative is to keep SB7 intact and to establish a state-wide competition for pre-SB7 privileges, allowing a limited number of school districts to participate in tax abatements without the negative fiscal impacts associated with SB7. Although this approach would require additional government resources, competition might improve the overall quality of tax abatement projects. Moreover, limiting the number of tax abatements should help hold down state education costs and facilitate efforts to equalize state education funding.

CONCLUSION

The most successful tax abatement policies take into account the needs and concerns of both the public and private sectors. The current legislative session is an excellent opportunity to reevaluate tax abatement practices in Texas and to consider the impact of SB7 on economic development activity. A careful and thoughtful discussion of these issues should help foster a "win-win" public/private partnership for economic development in Texas.

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Texas Research League
P. O. Box 12456
Austin, Texas 78711

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