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# Cyclicalities of State Budgeting: A Political-Economy Analysis.<sup>†</sup>

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## Abstract

This paper disentangles the effect political ideology and balanced budget rules have on fiscal cyclicalities across the U.S. states. Using panel data from 1963 to 2006, conservative states are found to be significantly more procyclical than liberal ones. The role of balanced budget constraints is contingent on the ideological orientation of the state in which they are imposed. Tight balanced budget rules are not binding on conservative states, but are binding on liberal ones. Where they are binding, budget rules mediate the link between voter preferences and policy outcomes skewing budgets toward greater procyclicalities.

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## I. Introduction

How do fiscal institutions and political ideology interact to affect government spending over the business cycle? Public finance literature has identified state balanced budget requirements as the principal institutional constraint facing state legislatures (Levinson 2006; Rueben 1995; Briffault 1996). Political scientists generally define an ideology as a set of beliefs about the role of government that shapes responses to a wide range of specific policy issues (Converse 1964; Peffley and Hurwitz, 1985). Political ideology refers to measurable shifts in voter preferences that shape policy outcomes, which; taken as a whole, communicate a view on the proper role of government in society.

Budget rules furnish a parsimonious measure of fiscal institutions; deriving from state constitutions, they are insulated from endogeneity by time and the inflexibility of state constitutions. Whereas state budget rules offer a parsimonious measure of fiscal institutions, identifying shifts in voter preferences is more challenging. Partisan voting in U.S. elections, based on bivariate correlations between party identification and voting behavior, has been particularly weak since WWII (Morris, 2002). Ideological realignments among white voters in the South and North created inconsistencies between voters' party affiliations and ideological orientations. Though party voting has reemerged gradually since 1980 as polarization across the major party platforms has expanded, only since the 2000 election cycle has party voting factored as a material determinant of electoral outcomes (Abramowitz and Saunders, 2006).<sup>1</sup> Inconsistencies between ideology and party identification have important consequences for

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<sup>1</sup> A party platform is a list of the actions that a political party supports in order to appeal to the general public for the purpose of having said party's candidates voted into office (The American Presidency Project).

voting behavior: when party voting is weak, traditional political science measures of party identification will be poor, highly inertial measures of voter preferences (Green, Palmquist and Schickler, 2002). Through a set of demographic variables dovetailing with major U.S. issue cleavages, political ideology is identified and endogeneity problems avoided.<sup>2</sup>

Public finance literature regarding fiscal institutions to state budgetary outcomes offers a breadth of perspectives relating the context and extent to which institutions affect policy outcomes. Fundamentally, the importance of budget rules turns on the question of whether fiscal institutions act as a veil, pierced by voters and their elected representatives. James Poterba (1996), synthesizing Alt and Lowry, (1994); Henning Bohn and Inman, (1995); Crain and Miller, (1990); and Reuben, (1995) makes the case for a broader, political economy argument, asserting that fiscal institutions mediate the link between voter preferences and policy outcomes.

Yet, political-economy arguments have been tested only indirectly. With case studies or measures of political fractionalization, much of the literature examines the response of budgetary outcomes vis-à-vis fiscal institutions using incomplete political measures. Alesina and Rosenthal, (1994) explore ways in which budgetary outcomes may vary across divided and unified party governments; Roubini and Sachs, (1989) look at the same issue across countries, finding that highly fractionalized governments are associated with larger budget deficits than unified ones.

The importance of fiscal institutions and political ideology as determinants of states' fiscal stance over the business cycle has not yet been established. Alt and Lowry (1994) study how states' revenues and expenditures respond to deficits using data from 1968 to 1987; they find that a one-dollar deficit triggers a 77-cent response within the next year among Republican

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<sup>2</sup> Cleavage issues divide voters along social divisions, which, in turn, become linked to party divisions and voting behavior (Lipset S. M. and Rokkan S., 1967).

states with strict balanced budget rules, while only a 34-cent response among Democrat controlled states. With data from the late 1980s, Poterba (1994) finds that when the same party controls the legislature and executive, deficit adjustment is faster regardless of party control.

Using data from 1963 to 2006, the role of fiscal constraints and ideology are disentangled to measure their influence on the cyclicity of government spending. Factor analysis is employed to construct a continuous measure of voter preferences across the following demographic variables: Union membership, abortions, executions, divorce rates, marriage rates, and educational attainment.

The results show that liberal states are significantly less procyclical than conservative ones. The role of budget rules is contingent on the ideology of the electorate upon which they are imposed. In conservative states, the voters themselves act as the relevant fiscal constraint. Where they are binding, budget rules eclipse majority preferences, substituting in their place a budgetary structure that precludes liberal outcomes and exacerbates the business cycle.

The following section on data explains the construction of measures for budget rule stringency and political ideology. Beyond that are sections covering methodology, results and conclusions.

## **II. Data**

The panel data covers each of the 48 continental U.S. states from 1963 to 2006 and is perfectly balanced.<sup>3</sup> Data on executions, union membership, marriage/divorce, and education come from the U.S. Bureau of the Census' Statistical Abstract of the United States. Data on abortion are compiled from the Alan Guttmacher Institute and Centers for Disease Control (CDC). Fiscal data comes from the U.S. Census Bureau and Gross State Product (GSP) data are

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<sup>3</sup> Alaska exhibits huge variation in several fiscal components as a result of variability in oil prices. Hawaii has a unique institutional structure.

from the Bureau of Economic Analysis (BEA). All data are in real terms; CPI data are from the International Monetary Fund (IMF).

GSP is the state-level counterpart of country-level Gross Domestic Product (GDP). Data on government expenditures refers to “general expenditures,” which entails all expenditures of a state government, and should not be confused with expenditures associated with the more restrictive “general fund.”

The cycle of government spending and GSP are calculated as the residual, of the natural logarithm, of the variable, less the predicted values of that variable regressed on a linear and quadratic trend for each individual state. The result is similar to a Hodrick-Prescott filter with a smooth parameter of 100.

## **II.a Measuring Balanced Budget Rules**

Since budget limitations derive from state constitutions or statutes dating back to the 19<sup>th</sup> century, an appropriate measure of their stringency need not vary over time. Every state, with the exception of Vermont, has important constraints on general operating deficits; the nature and scope of these constraints, however, varies across the states. The National Association of State Budget Officers (NASBO) measures their stringency by the stage in the budget process at which balance is required: 44 States require the governor to submit a balanced budget; 37 additionally require the legislature to enact a balanced budget. Of the 37 states requiring the legislature to enact a balanced budget, 24 impose a strict prohibition on deficit carry-forward. Prohibitions on deficit carry-forward require a budget to be balanced at the end of a fiscal year or biennium such that deficits cannot be transferred from one budget to the next.<sup>4</sup>

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<sup>4</sup> Prohibitions against carrying deficits into the next fiscal year and restrictions on the issuance of state debt help enforce balanced budget provisions by making it difficult to finance a deficit (National Conference of State Legislatures, 1999).

Budget rules also vary by the proportion of the budget subject to the rule. State and federal budgeting differ in that states practice fund accounting. Fund accounting mandates that assets and liabilities must be grouped according to the purpose for which they are used; all state revenues must be designated for a particular fund, and all state expenditures must derive from a particular fund.<sup>5</sup> The stringency of budget rules varies according to the number of funds, or overall percentage of a budget, that is subject to the rule. At a minimum, all state budget rules are applicable to the general fund, or state-operating budget (NASBO, 1992). In addition to the general fund, many states' rules apply to capital spending funds, insurance trust funds, and earmarked funds.<sup>6</sup>

Combining these dimensions of variation, states are divided into those with “less-strict” and “more-strict” rules. The label “less-strict” should not be misconstrued as implying all-together few limitations on budgeting, however. All of the states, in fact, are relatively constrained. In comparison to other countries with federal systems, the fiscal rules imposed on the U.S. states are particularly onerous (Sorensen, 2000). The criterion used to divide the states follows the construction used by Arik Levinson (2006), who synthesizes the relevant literature to create a classification system for budget rule stringency.<sup>7</sup>

## II.b Measuring Political Ideology

To create a more direct measure of voter preferences relative to bivariate correlations between party identification and voting behavior, factor analysis is used on a set of demographic variables to generate a measure of ideology. Factor analysis allows for the

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<sup>5</sup> The practice of fund accounting has survived from the 19<sup>th</sup> century when unified state budgets did not exist, and most revenues were earmarked for a specific expenditure.

<sup>6</sup> 34 States apply budget rules to special funds, such as those that receive earmarked tax revenue or are used to fund particular programs; in 33 states budget rules apply to capital spending funds; and, in 30 states budget rules apply to highway and social insurance trust funds.

<sup>7</sup> Levinson uses a NASBO study to resolve discrepancies between the classification systems of the General Accounting Office (GAO) and Advisory Commission on Intergovernmental Relations (ACIR). The States classified as having “less-strict” budget rules are: AK AZ CA CT IL LA MA MD MI MH NH NY OR PA TX VA VT WA WI WY.

common variation across the demographic variables to be consolidated into one, underlying dimension of political ideology. The variables composing the factor are measured at the state level. They include: percentage of workforce belonging to a union, percentage of pregnancies aborted, per capita executions, the per capita marriage rate less the per capita divorce rate, percentage of 25+ year-old population having completed high school, and the percentage of 25+ year-old population with a bachelor's degree or higher.

The resulting factor measures the extent to which the electorate of a given state is "liberal." For the value of the factor "liberal" to be high in a given state-year, one should expect the following: a larger proportion of the workforce belonging to a union, a greater percentage of pregnancies aborted, fewer executions per-capita, fewer marriages, more divorces, and higher levels of educational attainment. Figure 1 presents the mean "liberal" score for each of the 48 states. Excepting Utah and Colorado, which are examined with the results, Figure 1 conforms to contemporary ideas of red states, blue states, and battleground states.

Using demographic variables to elucidate a measure of ideological orientation is an approach grounded in a large body of political science research showing that political identities, like religious identities, are highly stable at both the individual and the aggregate level. Indeed, party identification in the U.S. has shifted rapidly only when the social imagery of a party itself has changed rapidly (Abramowitz and Saunders, 2006). The political transformation of the South, for instance, where African Americans moved quickly to the Democratic Party following the passage of the Voting Rights Act, changed the social imagery of the party itself. . The defining contemporary research on American political identities is Donald Green, Bradley Palmquist, and Eric Schickler's *Partisan Hearts and Minds: Political Parties and the Social Identities of Voters* (2002). In it they posit that party identification is based primarily on identification with social groups rather than a rational evaluation of ideology or policy.



Social identity theory stands in sharp contrast to ideological realignment theory, however. Ideological realignment theory offers compelling evidence that the correlation between ideology and party identification has been increasing with party polarization since the realignment of the 1980 presidential election (Abramowitz and Saunders, 1998).<sup>8</sup> As it pertains to the 1963 to 2006 period, however, party identification is an unequivocally poor measure of ideology. The debate over the relative importance of social identities and ideological preferences as determinants of party identification hinges importantly on the extent of party polarization since the 1980s.<sup>9</sup> Though polarization may be gradually realigning ideology and party loyalties - making them consistent with one another - that ideology and party identification were inconsistent from 1960 to 1980 is well established.

Creating an underlying measure of ideology with factor analysis is akin to controlling for the inconsistencies between party identification and ideology that have only recently abated. The construction of the factor, therefore, relies on social identity theory to create a continuous measure of ideology from 1963 to 2006. The demographic variables chosen compare strongly with those used in American National Election Study (NES) surveys on trends in party identification. They include items on the following issues: Abortion, the death penalty, GLBTQ<sup>10</sup> rights, government aid to blacks, government vs. personal responsibility for jobs and living standards, government spending and services, government vs. personal responsibility for health insurance, the role of women in society, and defense spending.<sup>11</sup>

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<sup>8</sup> Four realigning elections potentially confound the use of party identification: Nixon's 1964 "Southern Strategy," initiating the realignment of the South; the Democratic Convention of 1968 marking the collapse of the Liberal Accord and the rise of race as a dominant issue cleavage; Reagan's landslide victory in 1980, and Newt Gingrich's 1994 Contract With America.

<sup>9</sup> "According to this ideological realignment hypothesis, the increasing clarity of ideological differences between the parties during the Reagan and post-Reagan eras has made it easier for citizens to choose a party identification based on their ideological orientations." (Abramowitz and Saunders, 2006)

<sup>10</sup> Gay, Lesbian, Bisexual, Transgender, Questioning.

<sup>11</sup> The NES adjusts the items of its survey so they conform to salient issues at the time the survey is administered. For instance, what above is listed simply as "GLBT Rights," appears in the NES surveys of 1992-1996 as "laws barring

The variables used to calculate the factor, “liberal,” are intended to capture interstate variation in only the most highly politicized socioeconomic shifts of the post-WWII era. On their face, the two educational variables do not appear to fit this criterion, however. These variables are used to capture varying lags in the equalization of educational opportunities for blacks, which, at the time, reflected prevailing social views. Thus, the education variables serve as a proxy for the penetration of the civil rights movement and correspond to the NES item “government aid to blacks.”

### III. Methodology

Having developed measures of voter preferences and fiscal institutions, panel fixed-effects regressions are run to measure how budget rules and ideology influence the cyclicity of government spending. The specifications build on a simple equation regressing the cycle of state government spending ( $c\_g$ ) on the cycle of GSP ( $c\_gsp$ ). The role of ideology ( $liberal\_id$ ) and budget rules ( $lsbbr$ ) are first assessed separately, and then interacted with one another. The regressions are presented in the same order as they appear in Table 1.

$$c\_g_{i,t} = \alpha_0 + \beta_1 c\_gsp_{i,t} + \eta_i + \varepsilon_{i,t} \quad (1)$$

$\beta_1$  measures the cyclical stance of government spending over the output cycle. The coefficient, 0.60\*\*\* indicates that government spending is procyclical, meaning it reinforces the business cycle.

$$c\_g_{i,t} = \alpha_0 + \beta_1 c\_gsp_{i,t} + \beta_2 (lsbbr * c\_gsp)_{i,t} + \eta_i + \varepsilon_{i,t} \quad (2)$$

Equation two introduces state balanced budget rules alone, where “lsbbr” corresponds to a dummy variable equal to one if a state has less strict budgetary constraints.  $\beta_2$  is not statistically

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discrimination against gays and lesbians,” and “allowing gays and lesbians to serve in the military,” while in 2004, this component of ideology is assessed with an item on “gay marriage.”

significant (-0.04), indicating that budget rules, by themselves, do not influence the cyclicity of government spending.

$$c\_g_{i,t} = \alpha_0 + \beta_1 c\_gsp_{i,t} + \alpha_1 dem\_gov_{i,t} + \beta_3 (dem\_gov * c\_gsp)_{i,t} + \eta_i + \varepsilon_{i,t} \quad (3)$$

Here an indicator variable for the party of the governor, “d\_gov,” is used to check the hypothesis that traditional political science measures are poor measures of voter preferences.

The variable (d\_gov) is equal to one if the governor of a state is a Democrat.  $\beta_3$  measures the ability of party identification to proxy for ideology as it pertains to states’ governors. The coefficient on  $\beta_3$  is statistically insignificant (-0.01), suggesting this measure of party identification is a poor proxy for ideology.

$$c\_g_{i,t} = \alpha_0 + \beta_1 c\_gsp_{i,t} + \alpha_2 dem\_legis_{i,t} + \beta_4 (dem\_legis * c\_gsp)_{i,t} + \eta_i + \varepsilon_{i,t} \quad (4)$$

An additional test of party identification, the partisan composition of state legislatures is used to approximate voter preferences. The variable (dem\_legis) weights the percentage of Democrats in the upper chamber equally with the percentage of Democrats in the lower chamber.<sup>12</sup>  $\beta_4$  measures the extent to which partisanship can predict the cyclicity of budgetary outcomes. Its coefficient, 0.30, is not statistically significant.

$$c\_g_{i,t} = \alpha_0 + \beta_1 c\_gsp_{i,t} + \alpha_3 liberal\_id_{i,t} + \beta_5 (liberal\_id * c\_gsp)_{i,t} + \eta_i + \varepsilon_{i,t} \quad (5)$$

The variable (liberal\_id) corresponds to the factor measuring political ideology.  $\beta_5$  captures the influence of voter preferences on the cyclicity of state spending independently of state budget rules. The coefficient, -0.45\*\*\*, indicates that where electorates hold liberal policy views, state governments tend to budget less procyclically.

$$c\_g_{i,t} = \alpha_0 + \beta_1 c\_gsp_{i,t} + \beta_2 (lsbbr * c\_gsp)_{i,t} + \alpha_1 dem\_gov_{i,t} + \beta_3 (dem\_gov * c\_gsp)_{i,t} + \alpha_4 (lsbbr * dem\_gov)_{i,t} + \beta_6 (lsbbr * dem\_gov * c\_gsp)_{i,t} + \eta_i + \varepsilon_{i,t} \quad (6)$$

<sup>12</sup> Regressions including the partisan composition of state legislatures drop the state of Nebraska, as it, uniquely, has a unicameral legislature.

Executive partisanship ( $dem\_gov$ ) is interacted with the measure of budget rule stringency ( $lsbbr$ ) as an additional test to observe any interaction that might influence spending cyclicity.  $\beta_6$  measures if, conditional on fiscal institutions, executive partisanship influences the cyclicity of spending. The coefficient estimate, -0.01, is statistically insignificant.

$$c\_g_{i,t} = \alpha_0 + \beta_1 c\_gsp_{i,t} + \beta_2 (lsbbr * c\_gsp)_{i,t} + \alpha_2 dem\_legis_{i,t} + \beta_4 (dem\_legis * c\_gsp)_{i,t} + \alpha_5 (lsbbr * dem\_legis)_{i,t} + \beta_7 (lsbbr * dem\_legis * c\_gsp)_{i,t} + \eta_i + \varepsilon_{i,t} \quad (7)$$

Testing the partisanship of state legislatures ( $dem\_legis$ ) with budget rules, equation seven observes the interaction of legislative partisanship with fiscal institutions.  $\beta_7$  captures the effect partisanship may have on budgetary outcomes conditional on budget rules.<sup>13</sup> The coefficient on  $\beta_7$ , -0.36, is not significant.

$$c\_g_{i,t} = \alpha_0 + \beta_1 c\_gsp_{i,t} + \beta_2 (lsbbr * c\_gsp)_{i,t} + \alpha_3 liberal\_id_{i,t} + \beta_5 (liberal\_id * c\_gsp)_{i,t} + \alpha_6 (lsbbr * liberal\_id)_{i,t} + \beta_8 (lsbbr * liberal\_id * c\_gsp)_{i,t} + \eta_i + \varepsilon_{i,t} \quad (8)$$

Here the factor measuring ideology ( $lib\_ideo$ ) is interacted with budget constraints.  $\beta_8$  captures the interaction of ideology and state budget rules. The coefficient estimate for  $\beta_8$ , -0.35\*, indicates that liberal states with less strict balanced budget rules tend to budget less procyclically than conservative states as well as liberal states with stringent budget rules.

## IV. Results

The first column of results presented in Table 1 shows that government spending is significantly procyclical over the output cycle. As a state moves into an expansionary phase of a business cycle, government spending rises with output, thereby exacerbating cycle. This result conforms to the literature, (Sorenson et. al, 2000) yet is potentially surprising considering that, at the federal level, fiscal policy among industrialized countries is significantly countercyclical.

<sup>13</sup> Many additional political science variables were tested alone, interacted amongst one another, and interacted with the measure of budget rule stringency. These variables included: Dummy variables corresponding to majority control of the upper and lower legislative chambers; a dummy variable corresponding to unified majority control of both chambers; a dummy variable corresponding to unified party control of the legislature and executive; and, the partisan composition of each state's House delegation.

Using two measures of party identification to approximate shifts in voter preferences, columns 3, 4 and 6 of Table 1 yield estimates to confirm the hypothesis that weak partisan voting from 1963 to 2006 makes political science variables poor proxies for voter preferences. Consistent with the aforementioned limitations, none of the party identification measures produce statistically significant results.

Employing the new measure of political ideology (*liberal\_id*), column 5 shows that liberal states are significantly less procyclical than their peers suggesting that budgetary policy in liberal states is more flexible over the business cycle. Though it would be convenient to attribute this flexibility to liberal preferences for more interventionist government; progressivity is not necessarily synonymous with flexibility. Granted, liberal states are less willing to cut spending in the event of revenue shortfalls. This should not preclude liberal states from spending procyclicality, however. Just as conservative states are known to cut taxes during expansions, nothing prohibits liberal states from embarking on program expansions at the peak of the business cycle. A direct, causal, link between a specific tenet of liberal ideology and budgetary flexibility is difficult to conceive, much less measure. Yet there is no explicit evidence to suggest the link between countercyclicality and liberal ideology is so simple as liberal preferences for larger, more interventionist government.<sup>14</sup>

With regard to the precision of the factor measuring liberal ideology, Utah and Colorado were noted as states whose classification diverges from current conceptions of red states and blue states. On closer examination, Utah and Colorado score highly for their historically leading levels of educational attainment. As it pertains to the cyclicity of government spending,

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<sup>14</sup> Liberal ideology, like conservative ideology, is situated within the broader context of American political thought. Liberal ideology incorporates notions of material equity that, necessarily, manifest themselves in greater centralization. Wholly antithetical to a society founded on the diffusion of power, liberals may struggle to justify (nonessential) program expansions when the economy is at full employment. Tax cuts, however, easily gain support during economic expansions.

however, are these states misclassified? No. Figure 3 takes the case of Utah to show that as its relative stance as “liberal” shrinks dramatically relative to that of U.S., the correlation between Utah’s spending cycle and output cycle increase dramatically. Utah’s relative decline in liberal preferences, then, is bourn out by the increasing correlation between its GSP and spending cycles. As its relative liberal stance declines, the correlation increases indicating greater procyclicality.

Observing the role of budget rules alone, the coefficient estimate for the budget rule cycle ( $lsbbr*c\_gsp$ ) in column 2 confronts unresolved issues in the literature. Its insignificance suggests that budget rules are, in fact, only veils that are pierced by voters and their elected officials. If state budget rules lack the requisite enforcement mechanisms, and are easily circumvented by voters and elected officials, then fiscal institutions will not play a mediatory role between voter preferences and budgetary outcomes. If this is the case, then the limitations on U.S. states are being incorrectly labeled as stringent relative to those of other countries.

Yet, if budget rules are only a veil, then some other disciplining factor must be compelling the states’ notable compliance with the principle of a balanced budget. Otherwise stated, balanced budget rules may not be the proximate source of fiscal discipline. If the electorate presumes the budget will be balanced annually, then the voters themselves may act as the relevant enforcement mechanism independent of fiscal institutions. It, therefore, is necessary to account for voters’ preferences in disentangling the determinants of budgetary outcomes.

Interacting budget rules with shifts in ideology yields a more nuanced picture of the interceding role fiscal institutions play in the translation of voter preferences into budgetary outcomes. Column 8 presents results for the fully specified regression interacting ideology with fiscal constraints. Here, the coefficient estimate for ( $lsbbr*lib\_id*c\_gsp$ ),  $-0.35^*$ , reveals that

liberal states with less strict budget rules are countercyclical relative to liberal states with tight budget rules. Thus, when liberal states are not bound by fiscal constraints they will budget less procyclically.

For liberal states, tight balanced budget rules interfere between voters' preferences and policy outcomes. In this way fiscal constraints selectively eclipse majority preferences, substituting in their place a budgetary structure that precludes liberal outcomes and reinforces the business cycle. As figure two illustrates, this interference is likely to frustrate increasingly more state electorates in the future as social progress moves forward and the country becomes more liberal.

Budgets set goals and decide among alternative policy objectives; budgets can push reform or they can discourage it. Transferring decision-making from the public arena to unaccountable institutions limits voters' capacity to control and account for the expenditure of public resources. So long as they are held as immovable, budget rules will impede responsiveness and accountability, thereby constraining the realization of majoritarian policy outcomes.

The estimated coefficient on the budget rule cycle ( $\text{lsbbr}^*c\_gsp$ ) in column 8 remains insignificant, reinforcing the hypothesis that for conservative states it is the voters themselves acting as the relevant fiscal constraint. Where voter preferences supplant fiscal institutions, budget rules do not intermediate the link between the electorate and policy outcomes. In sum, the role of fiscal institutions is contingent on the ideology of the electorate upon which they are imposed. If an electorate is sufficiently liberal, tight budget rules will be binding, and policy outcomes will be skewed toward greater procyclicality.

## V. Conclusions

This paper offers a multidimensional view of fiscal institutions as determinants of the cyclicalities of government spending by incorporating a stronger measure of voter preferences. The results show that the role of balanced budget rules is contingent upon the ideological stance of an electorate. In conservative states, voters supersede fiscal institutions as the relevant budgetary constraint. For liberal states, tight balanced budget rules mediate voter preferences to preclude the realization of majoritarian policy outcomes.

Budget rules push policy toward greater procyclicality; begging the question of whether states constrained by these rules should not abandon them. Scraping balanced budget rules presents political challenges, however, and may not be optimal if their absence sufficiently exacerbates moral hazard problems to create irresponsible indebtedness among the states. Yet, the maintenance of an institution designed to thwart majority preferences should require extraordinary justification in a Democracy. While the policy question warrants further examination, the evidence presented here finds no case for their perpetuation.



**Table 1**

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
c_g	0.60*** (7.18)	0.61*** (6.53)	0.60*** (6.07)	0.42* (1.82)	0.60*** (9.00)	0.61*** (9.67)	0.36 (1.54)	0.61*** (9.13)
lsbbr*c_gsp		-0.04 (-0.21)				-0.05 (-0.17)		0.01 (0.04)
liberal_id*c_gsp					-0.45*** (-5.22)			-0.36*** (-3.97)
dem_gov*c_gsp			-0.01 (-0.12)			-0.01 (-0.08)		
dem_legis*c_gsp				0.30 (0.71)			0.54 (1.27)	
lsbbr*liberal_id*c_gsp								-0.35* (-1.80)
lsbbr*dem_gov*c_gsp						-0.01 (-0.06)		
lsbbr*dem_legis*c_gsp							-0.36 (-1.24)	
liberal_id					-0.56*** (-7.73)			-0.60*** (-6.80)
lsbbr*liberal_id								0.22 (1.24)
dem_gov			-0.25 (-0.36)			0.61 (1.08)		
lsbbr*dem_gov						-2.81 (-1.51)		
dem_legis				0.67 (0.37)			-0.44 (-0.22)	
lsbbr*dem_legis							5.26 (1.09)	
Constant	0.22*** (7.18)	0.22*** (7.20)	0.35 (0.93)	-0.16 (-0.15)	0.36*** (7.92)	0.33 (0.93)	-0.51 (-0.45)	0.32*** (7.23)
Observations	1968	1968	1968	1927	1968	1968	1927	1968
Number of States	48	48	48	47	48	48	47	48
R-squared	0.148	0.149	0.149	0.147	0.206	0.153	0.152	0.213
Robust t Statistics In Parentheses								
*** p<0.01, ** p<0.05, *p<0.1								

Figure 1

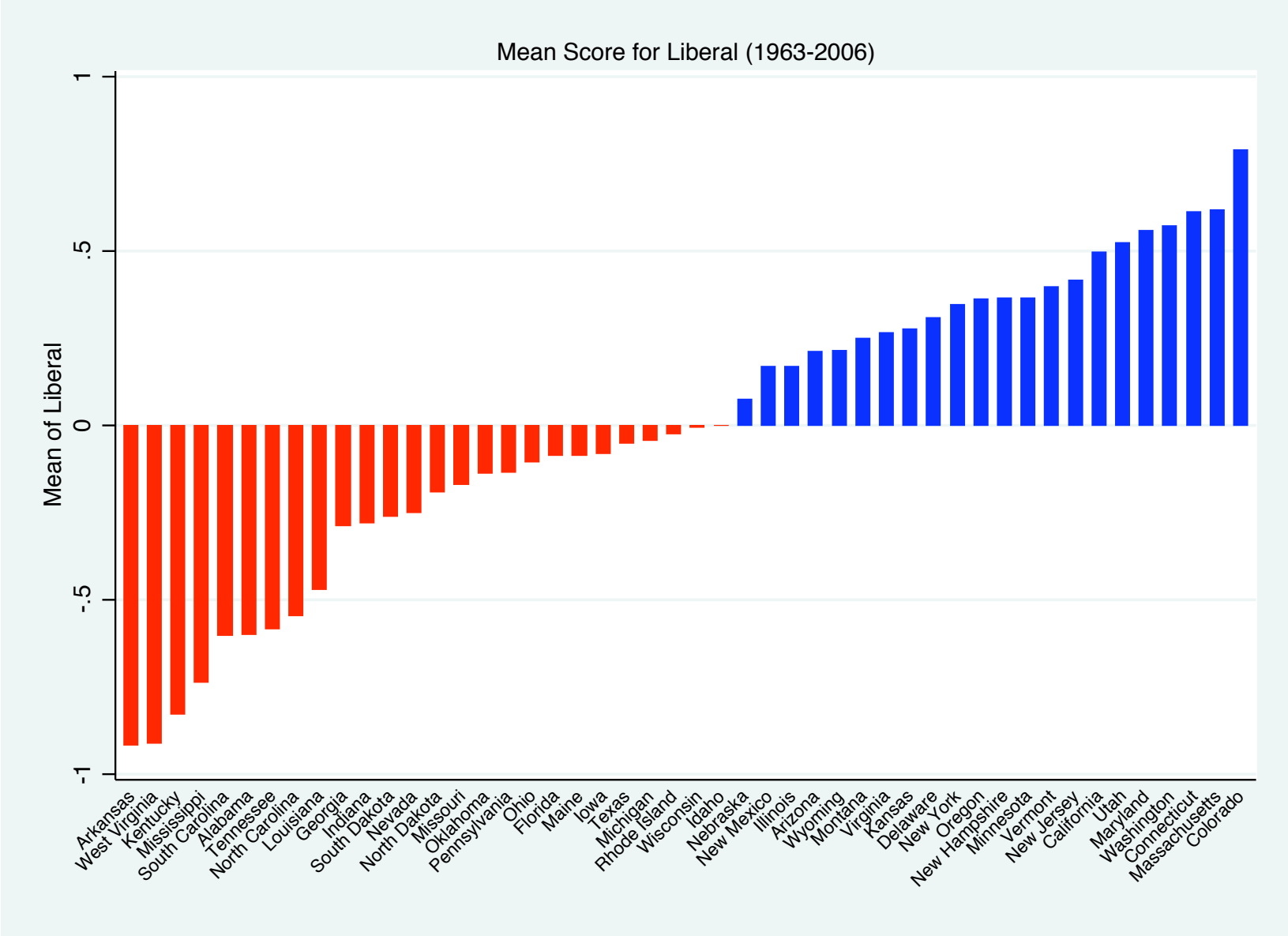


Figure 2

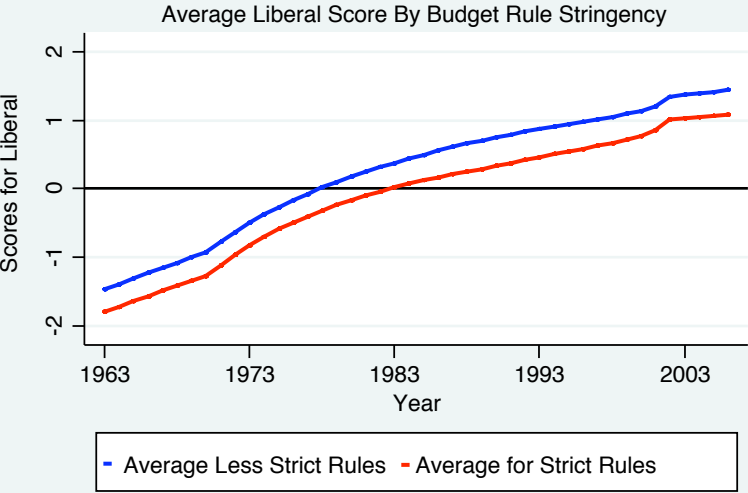
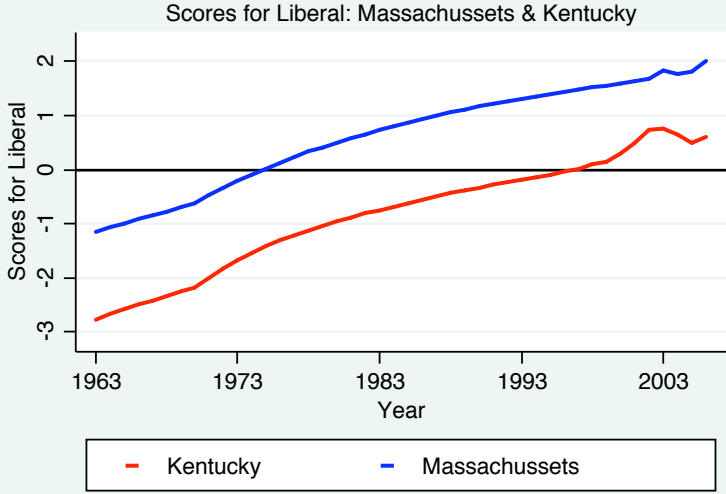
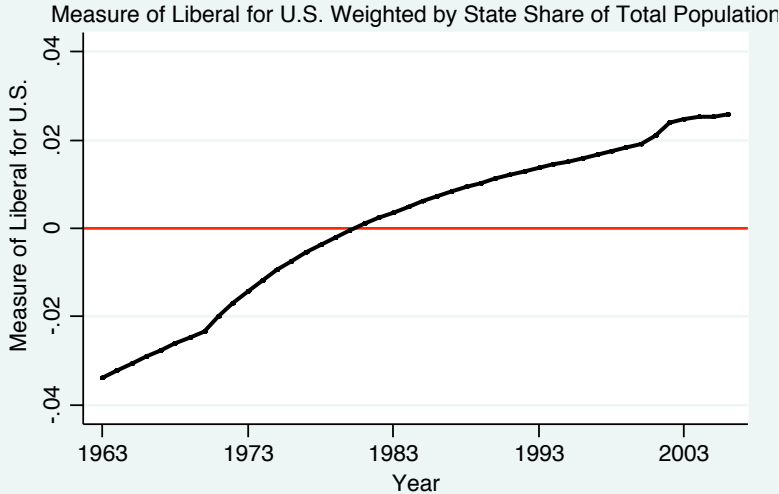
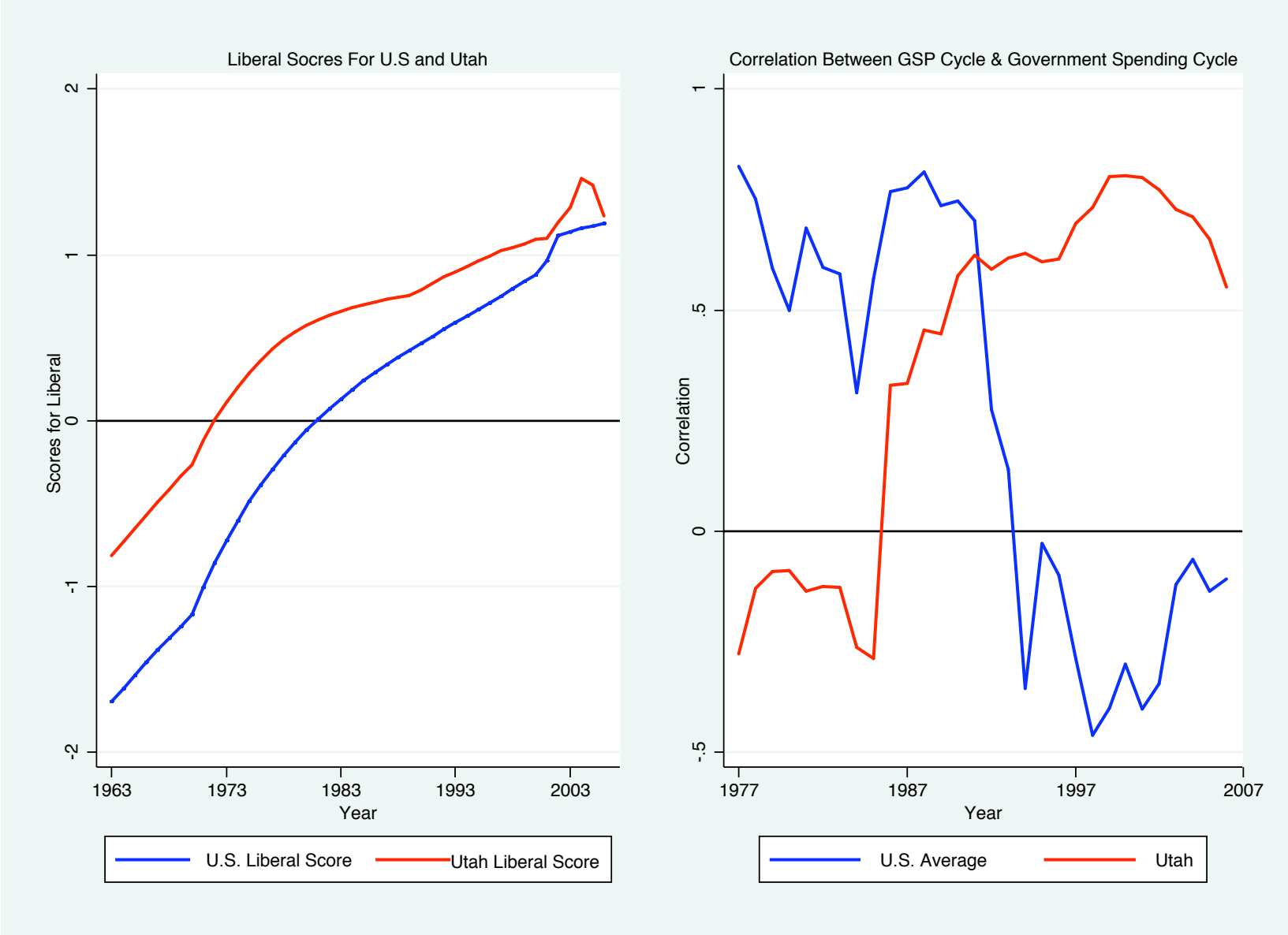


Figure 3



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