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**THE IMPACT OF LEGISLATIVE TERM LIMITS ON STATE FISCAL POLICY**

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Submitted to the Economics Faculty  
In partial fulfillment of the requirements for the degree of  
Bachelor of Science in Business Administration

December 2009

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*In an effort to improve the efficient operation of political markets in the 1990's eleven states successfully adopted legislative term limits. By limiting the number of terms that a legislator can serve in office, term limits effectively shorten the time horizon under which a legislator must operate. With a shorter time horizon I hypothesize that legislators will prefer legislation with a greater impact in the short-run. This would entail higher expenditure levels on social programs which are easily implemented in the short-run; and conversely, lower expenditure levels on long-term projects such as infrastructure spending. Using panel analysis of all fifty states between 1992 and 2004, I find that term limits reduce levels of state infrastructure spending proportionate to public welfare expenditures.*

JEL classifications: H7, H3

Key words: term limits, rent-seeking, capital outlays, public welfare, time horizon

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## **I. Introduction**

At a time when the American public was becoming increasingly frustrated with its government leaders, legislative term limits were popularized as a solution to various shortcomings in the American political system. Proponents of term limits argue that when politicians are permitted to run for reelection indefinitely they develop an incumbency advantage which distances them from the voters and obstructs the efficient operation of political markets. The expectation is that voters' interests will be better represented if elected officials are limited to two or three terms in office<sup>1</sup>. Since 1990, fifteen states have adopted legislative term limits.

At the time of their passage, legislative term limits were virtually an untested experiment. Prior to 1990, it was common practice to impose term limits on the executive office, but never before had a state legislature been subject to this constraint. Almost two decades later the impact of legislative term limits is becoming evident on a number of fronts. While previous research has focused on the behavioral and institutional changes that term limits have brought to state legislatures, little analysis has been done on the policy outcomes associated with the adoption of legislative term limits.

The focus of this paper is to explore the relationship between term limits and fiscal policy outcomes. Specifically, I examine how the rent-optimizing calculus of a term limited legislator might lead the lawmaker to favor one fiscal policy over another. I argue that the shorter political time horizon that term limits impose on legislators will cause legislators to favor fiscal policies that have short-term political payoffs. Specifically, this entails higher expenditure levels on

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<sup>1</sup>While there was a strong push to impose term limits on federal legislators, the effort was blocked by the Supreme Court which ruled such a move unconstitutional (*U.S. Term Limits, Inc. v. Thornton*, 1995).

social programs which are easily implemented in the short-run; and conversely, lower expenditure levels on long-term projects such as infrastructure spending.

I find that that term limits reduce levels of state infrastructure spending relative to public welfare expenditures, such that term limits create a substitution effect between these two expenditure items.

## **II. Literature Review**

### *A. Term Limits and Political Incentives*

The primary purpose of term limits is to address problems associated with incumbency advantage. In an efficiently operating political market politicians are rewarded based upon how well they represent the interests of their constituents. Good politicians therefore should be rewarded with reelection, and poorly performing politicians sent home. However, this is not always the case. Politicians are often able to develop an incumbency advantage that is in part divorced from their political performance. Various theories explain this phenomenon. Yakovlev (2007) attributes the incumbency advantage to a risk aversion among voters, who would rather an ill-performing incumbent to an untested newcomer. Berry et al. (2000) finds that politicians actively seek ways to insulate themselves from their political, economic, and social environments, a process referred to as “institutionalization”. Institutionalized legislatures tend to have better paid legislators, longer sessions, and more legislative staff. Berry demonstrates that greater levels of legislative institutionalization significantly increases the reelection rate among incumbents. Having achieved this incumbency advantage, politicians are at greater liberty to pursue their self-interests, irrespective of whether such behavior is in the public’s best interest.

The expectation then is that term limits will relinquish the hold of incumbents on state offices and make legislators more accountable to their constituencies. Proponents of term limits

predicted that limiting the number of terms a legislator can serve in office would usher in a new sort of “citizen legislator”, more concerned with serving the interests of the voters than with advancing his or her own political career (Will, 1992).

Much of the literature finds this argument unsatisfactory and the empirical results suggest likewise. It is a well accepted view in political theory that political processes are affected by a rent-seeking calculus (Kreuger, 1974). In other words, politicians are self-interested agents. They seek to extract rents from holding office, whether these be ego rents or else career advancement. Accordingly, the effect of term limits is not to change or eliminate rent-seeking behavior in politicians.

Research confirms that in the presence of term limits, legislators continue to exhibit rent-seeking behavior, which at times puts them at odds with their official legislative responsibilities. This tendency for legislators to shy from their legislative responsibilities is referred to in the literature as “shirking”. While term limits prevent politicians from becoming entrenched in office, they do not necessarily make politicians more responsive to their constituencies. By shortening the time horizon that a politician can expect to remain in office, term limits reduce the expected “rents” that a politician can look to obtain from running for and serving in office. Therefore the value of the office is reduced and the opportunity cost of shirking to a rent-seeking politician is lessened. Research finds evidence of increased shirking in the presence of term limits (Rothenberg and Sanders 2000, Lott and Bronars 1993, Besley and Case 1995, and Carey 1996). Specifically, term limited legislators are more likely to diverge from the policy preferences of the median voter (ideological shirking). Term limited legislators are also less likely to participate in roll-call votes, evidence of reduced legislative effort (participatory

shirking). Ironically, term limits appear to produce higher levels of shirking and encourage rent-seeking behavior in legislators.

In addition to reducing the opportunity cost of shirking, term limits also shift the attention and energy of legislators away from the offices they currently hold. Carey (1996) argues that legislators are systematically responsive to whomever controls their political (or non-political) futures. In the case of term limits Carey predicts legislators will shift their allegiance away from those who voted them into office and towards those who control access to higher office. Carey finds that aspiring legislators in the second session of their last term exhibit a larger ideological shift in voting behavior, as compared to legislators not running for higher office. Furthermore, he finds that this ideological shift aligns the legislators closer to their state party delegations, those with the most control over their next career step. Therefore, provided that term limits increase the number of political aspirants, which Carey also found to be the case, we can expect term limits to reduce the overall responsiveness of legislators to their current constituencies.

While term limits prevent legislators from making a career out of holding a single seat in the legislature, research shows that careerism is not ended by term limits. As opposed to remaining in one office, term limited legislators have a tendency to switch from office to office. (Sarbouagh-Thompson, 2004). Carey et al. (1998) finds that legislators in term limited states are more likely to have political backgrounds prior to serving in the legislature and are more likely to run for higher office. Therefore, term limits appear to give rise to a new breed of career politicians, ones who use the legislature office as a stepping stone for political advancement.

To summarize, the behavioral impact of term limits on state legislators has not matched expectations. Empirical evidence suggests that term limits have failed to usher in a new brand of “citizen legislator” who better serves the public interest. Rather, term limited legislators are

equally or more likely to shirk on their legislative responsibilities; and term limited legislators remain opportunistic in their political careers (Rothenberg and Sanders, 2000; Carey et al., 1998).

### *B. Term Limits and Fiscal Policy Outcomes*

The consequences of populating legislature with a class of transient-minded politicians holds important implications for the type of fiscal policies that these legislators are likely to implement while in office. Garri (2007) argues that politicians are biased to favor short-term policy solutions, an effect he calls “political short-termism”. He attributes this preference for short-term public goods to a politician’s desire to accumulate political capital before his or her term in office expires. By shortening the time horizon that a legislator can possibly serve in office, term limits should accentuate this effect.

Research links term limits with political short-termism in the area of state finances. Cummings (2008) theorizes that states with term limited legislatures should have a harder time managing its fiscal policies. He poses two reasons for this: one, term limits would produce inexperienced legislators ill-equipped to handle fiscal policy; and two, term limited politicians, who have short political time horizons, are likely to have a shortsighted approach to state finances. Cummings looks at fiscal data for forty-nine states from 1982 to 2005. He tests the fiscal impact of term limits by measuring their effects on year-end-surpluses and a measure of “fiscal health” (which is a function of a state’s general fund balances). Cummings finds that states with term limits are more likely to encounter budgetary problems. Specifically term limited states are more likely to run budgetary deficits, and in term limited states the year-end general fund balances are on average 2% lower.

Also measuring the impact of term limits on state finances, Erler (2007) finds evidence of political short-termism. Erler tests the claim that term limits will counteract a “culture of spending” in the state legislatures. Previous research had linked legislators’ tenure in office with a tendency for higher government spending (Payne, 1992). Term limits were seen to be a solution to wasteful government spending. Testing the claim that term limits would reduce state expenditures, Erler found just the opposite. States with term limits had higher expenditure levels than states without term limits. Erler’s research lends weight to the argument that term limits lead to short-sighted fiscal policies that are appealing in the short-term but harmful to the state’s long-term fiscal health.

While Erler (2007) finds term limits to increase state expenditures overall, each expenditure item in a state’s budget is not impacted by term limits alike. Extending upon her research, Erler breaks state budgets down into four categories: highway expenditures, public welfare, education, and health. Erler finds that all four categories receive higher levels of funding in the presence of term limits, but in varying degrees. Transportation expenditures have the smallest marginal increase, where education and public welfare demonstrate substantial increases.

Therefore term limited legislators discriminate between expenditure items in a state budget, preferring some items over others. Discriminating between expenditure items is consistent with term limited legislators’ attraction for short-term policy solutions. Some expenditure items in state budgets promise immediate political payoffs, while the benefits of other expenditure items may not be fully realized until a later date. The literature has identified two such expenditure items: public welfare expenditures and infrastructure spending, respectively.

Hefner (1992) argues that the transient nature of office holding would bias legislators to underfund infrastructure projects. Hefner hypothesized that capital outlays are crowded out by competing demands for state funds; specifically by spending for state and local social service programs. Accordingly, the durable nature of public capital would make it easier for legislators to divert funds to programs that would have an immediate and favorable impact. Examining capital outlay expenditures from 1969 to 1987, Hefner finds that capital outlays are inversely related with public welfare expenditures.

Cadot et al. (2006) lends further support to the inverse relationship between capital outlays and public welfare expenditures. Cadot sought to determine the extent to which infrastructure expenditures are affected by pork-barrel spending initiatives. He finds that pork-barrel spending has a positive, though small, effect on levels of infrastructure spending. While on the other hand, pork-barrel spending has a large impact on public welfare expenditures, suggesting that public welfare expenditures are more attractive to rent-seeking legislators. As Cadot observed, roads and railways are not built to reduce traffic jams, but to get politicians reelected and advance political careers. If legislators stand to benefit more from public welfare expenditures as opposed to capital outlays, then that is where state funds (and pork-barrel spending) will be channeled.

### **III. Methodology**

#### *A. Data*

To test the hypothesis that term limits bias state legislators to adopt short-run fiscal policies I use a balanced longitudinal panel of the fifty states. The dataset corresponds to the time period during which term limits were adopted among the states: 1992 to 2004. The focus of

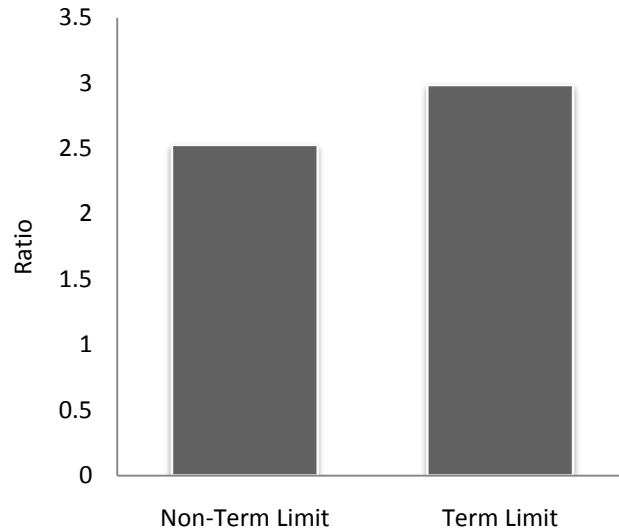
my analysis is to measure the impact of term limits on capital outlays and public welfare expenditures. Capital outlays consist of major infrastructure improvements (excluding routine maintenance expenditures which would be classified as current operations<sup>2</sup>). Public welfare expenditures consist mainly of cash assistance paid directly to needy persons under the purview of various welfare programs, and the general provision for welfare institutions<sup>3</sup>. In addition to capital outlays and public welfare expenditures, I also examine total state expenditures, along with total state revenues. The data comes from the *Statistical Abstract of the United States*, *Fiscal Survey of the States*, and the *Bureau of Economic Analysis*.

The following graph displays the average ratio of public welfare expenditures to capital outlays for states with term limits and states without:

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<sup>2</sup>**Capital Outlays:** Direct expenditure for contract or force account construction of buildings, grounds, and other improvements, and purchase of equipment, land, and existing structures. Includes amounts for additions, replacements, and major alterations to fixed works and structures. However, expenditure for repairs to such works and structures is classified as current operation expenditure. See Construction and Equipment. (U.S. Census Bureau. <http://www.census.gov/govs/definitions/> (accessed November 20, 2009).)

<sup>3</sup>**Public Welfare:** Support of and assistance to needy persons contingent upon their need. Excludes pensions to former employees and other benefits not contingent on need. Expenditures under this heading include: Cash assistance paid directly to needy persons under the categorical programs Old Age Assistance, Temporary Assistance for Needy Families (TANF) and under any other welfare programs; Vendor payments made directly to private purveyors for medical care, burials, and other commodities and services provided under welfare programs; and provision and operation by the government of welfare institutions. Other public welfare includes payments to other governments for welfare purposes, amounts for administration, support of private welfare agencies, and other public welfare services. Health and hospital services provided directly by the government through its own hospitals and health agencies, and any payments to other governments for such purposes are classed under those functional headings rather than here. (U.S. Census Bureau. <http://www.census.gov/govs/definitions/> (accessed November 20, 2009).)



**Figure 1.** The ratio of per capita public welfare expenditures to per capita capital outlays in termed and un-termed states. (1992-2004).

A visual inspection of the data in Figure 1 indicates that on average states with term limits spend more on public welfare in proportion to capital outlays. Where the ratio of public welfare to capital outlays in term limited states is 3:1, in states without term limits it is 2.5:1. This difference suggests that legislative term limits cause states to spend proportionately more on public welfare and less on capital outlays. A substitution effect between public welfare expenditures and capital outlays is consistent with the hypothesis that term limits bias legislators to adopt short-run fiscal policies that promise immediate political payoffs. The material benefits of public welfare expenditures are quickly realized by the voters, and in turn the political benefits are more immediately reaped by legislators. Capital outlays, on the other hand, fund large scale projects which take time to implement, spreading the material and political benefits over a longer period of time.

However, Figure 1 could be misleading. State specific variation can easily distort the real impact (or lack thereof) that term limits have on fiscal policy decisions. Rather than being driven by term limits, these fiscal outcomes could be influenced by other variables unique to

term limited states. A multivariate analysis must be conducted to separate out endogenous characteristics between states and thereby uncover the actual impact of term limits on public welfare expenditures and capital outlays.

The main explanatory variable of interest is term limits. To measure its impact on fiscal expenditures I construct a dummy variable to indicate the presence of term limits in a state. I assign a 0 for each time observations prior to the term limit restriction taking effect, and a 1 starting the legislative session in which the first class of legislators are no longer eligible to run for re-election. Following previous literature (Carey et al. 2000b; Johnson and Crain 2004; Meinke and Hasecke 2003; Moncrief et al. 2004, Erler 2007), I choose not to make the term limit dummy effective the year in which the voters passed the legislation. In most states there was a significant time lag between the passage of the term limit law and the term limit restriction taking effect. For example, Colorado passed term limit legislation in 1990, but it did not block a class of legislators from running for reelection until 1998. Furthermore, uncertainty existed as to whether the term limit legislation would remain binding in many states. Four states passed term limits, only to have their state supreme courts overturn them. Two other states adopted term limits and later repealed the legislation<sup>4</sup>. States that adopted and afterwards repealed term limits and states that never had term limits are coded 0 for the entire dataset. The following states are treated as term limited states within my analysis: Alabama, Arkansas, California, Colorado, Florida, Louisiana, Michigan, Montana, Missouri, Ohio, Oklahoma, Ohio, and South Dakota<sup>5</sup>.

I also include within my models control variables that economic theory and previous research would suggest. These include federal aid to the states, gross state product, and the

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<sup>4</sup> Term limits were repealed by the state legislature in Idaho and Utah. The state supreme courts of Massachusetts, Oregon, Washington, and Wyoming struck down term limits.

<sup>5</sup> See Appendix A

unemployment rate (Erler 2007, Cummings 2008). To control for political factors I include a variable for the proportion of the state legislature that is Republican. Variance inflation analysis does not show high collinearity between any of the explanatory variables. Finally, I include an outlier dummy variable for the states Alaska and Hawaii. Other research (Erler, 2007) finds the fiscal structures of these states to be unique and therefore incomparable to the other states. Rather than completely exclude Alaska and Hawaii from my analysis I utilize a dummy variable to account for the outlier effect created by these states.

The following table provides a summary of the variables utilized within my analysis:

**Table 1 - Variable Description and Summary Statistics**

<i>Variable Name</i>	<i>Variable Description</i>	<i>Mean</i>	<i>Std dev</i>
$gnlex_{it}$	General state expenditures in state $i$ and time $t$ (per capita)	3,933	(1,297)
$cptl_{it}$	Capital outlays in state $i$ and time $t$ (per capita)	313	(154)
$pw_{it}$	Public welfare expenditures in state $i$ and time $t$ (per capita)	821	(269)
$pw/cptl_{it}$	The ratio of per capita public welfare expenditures to per capita capital outlays in state $i$ and time $t$	2.99	(1.34)
$N_{it}$	Dummy variable indicating the presence of term limits in state $i$ at time $t$ (1 = term limits, 0 = other)	0.10	(0.31)
$fedaid_{it}$	Federal aid to the states in state $i$ and time $t$ (per capita)	1,098	(416)
$gsp_{it}$	Gross state product in state $i$ and time $t$ (per capita)	31,152	(6,304)
$unplmt_{it}$	Unemployment rate in state $i$ and time $t$ (per capita)	0.05	(0.01)
$legrepub_{it}$	Proportion of the legislature in state $i$ and at time $t$ that identifies itself with the Republican party	46.8	(15.5)
<i>outlier</i>	Dummy variable to control for outlier states: Alaska, Hawaii, and Nebraska <sup>1</sup>	0.060	(0.237)
$gnlrev_{it}$	General state revenues in state $i$ and time $t$ (per capita)	3,595	(1,368)

\*All nominal values are adjusted for inflation using state specific GDP deflator

<sup>1</sup>While conducting a similar analysis to mine Erler (2007) also excludes Nebraska from the dataset given that its legislators are selected in non-partisan elections and the existence of a unicameral legislature. To remain consistent, and rather than completely excluding Nebraska from my analysis, I include the state in the outlier dummy variable. My results are consistent with those of Erler (2007).

## *B. Econometric Model*

In my analysis I control for unobserved heterogeneity. Running a Hausman and Breusch-Pagan test I determine that using fixed effects is the appropriate procedure. However, conventional fixed effects could prove problematic for my analysis, since the procedure has a tendency to absorb time invariant and rarely changing variables in the model, such as my term limit dummy. To address this issue, I use an econometrics method called fixed effects vector decomposition, FEVD (Plümer and Troger 2007). FEVD estimates fixed effects models in the presence of time-invariant or rarely changing variables. When both the time-invariant and time-varying variables are correlated with the unit effects, then the FEVD procedure gives more efficient and reliable estimators than PCSE or OLS. Using a pair-wise correlation matrix, I calculate and find that the term limit dummy used in my models is significantly correlated with the state fixed effects, affirming my use of FEVD.

I run the FEVD procedure using panel corrected standard errors to account for groupwise heteroskedasticity and contemporaneous correlation (Beck and Katz, 1995). I also correct my regression results for first-order autocorrelation. Finally I use year dummies to control for year-specific effects.

## **IV. Results and Analysis**

I begin my analysis by replicating the work of Erler (2007), who examined the impact of term limits on total state expenditures. After reproducing Erler's work, I create three more models that are variations of the first, where I estimate the impact of term limits on public welfare, capital outlays, and the ratio of public welfare to capital outlays. These four models are specified in equations one through four:

$$gnlex_{it} = \alpha + \gamma N_{it} + \sum_{j=1}^5 \beta_j X_{it} + h_i + \varepsilon_{it} \quad (1)$$

$$pw_{it} = \alpha + \gamma N_{it} + \sum_{j=1}^5 \beta_j X_{it} + h_i + \varepsilon_{it} \quad (2)$$

$$cptl_{it} = \alpha + \gamma N_{it} + \sum_{j=1}^5 \beta_j X_{it} + h_i + \varepsilon_{it} \quad (3)$$

$$pw/cptl_{it} = \alpha + \gamma N_{it} + \sum_{j=1}^5 \beta_j X_{it} + h_i + \varepsilon_{it} \quad (4)$$

Where  $gnex_{it}$  is general expenditures,  $pw_{it}$  is public welfare,  $cptl_{it}$  is capital outlays, and  $pw/cptl_{it}$  is the proportion of public welfare to capital outlays. Each of these dependent variables is regressed on the term limits dummy  $N_{it}$ . I include five control variables specified by  $X_{it}$  (federal aid, unemployment rate, gross state product, the proportion of the legislature republican, and an outlier dummy).  $h_i$  is the state fixed effects estimator, and  $\varepsilon_i$  is the disturbance term. The subscripts  $i=1, \dots, 50$  and  $t=1992, \dots, 2004$  represent states and years, respectively. The results from equation 1 are shown in Table 2:

**Table 2.** The Impact of Term Limits on Total Expenditures

Regressors	Model 1
	Total Expenditures per cap.
Term Limits	71.9 (41)*
Unemployment	41.8 (25.9)
Legislature Republican	-1.06 (1.67)
Federal Aid	0.476 (0.116)***
Gross State Product	0.094 (0.005)***
Outlier	3073 (180)***
Constant	190.148 (275)
R <sup>2</sup>	0.96
Fixed effects vector decomposition, $n = 637$ Panel corrected standard errors reported in parenthesis * $p < 0.1$ ** $p < 0.05$ *** $p < 0.01$	

These results closely replicate the findings of Erler (2007) who also examined the impact of legislative term limits on total state expenditures. The coefficients are of a similar magnitude, and while Erler finds term limits to increase total state expenditures at the 95% confidence level, I find this to be the case, but at the 90% confidence level. Model 1 shows that I term limits lead to a \$71 per capita increase in total state expenditures. The term limit coefficient indicates that on average total expenditures are 1.8 percentage-points higher in term limited states than in non-term limited states over the time period examined.

The other variables in the model make intuitive sense and also exhibit consistency with Erler's (2007) findings. When regressed on total expenditures, gross state product is positive and significant. The same holds for federal aid to the states. The outlier dummy is primarily

capturing the effect of Alaska which has per capita expenditure levels three times the average level<sup>6</sup>.

Using a similar approach, I break total expenditures down into two of its main components: public welfare expenditures and capital outlays. The question is whether term limits affect expenditure items alike. The table below reports the impact that term limits have on public welfare expenditure (model 2), capital outlays (model 3), and finally the ratio between public welfare and capital outlays (model 4).

**Table 3.** The Impact of Term Limits on Public Welfare Expenditures and Capital Outlays

Regressors	Model 2	Model 3	Model 4
	Public Welfare per cap.	Capital Outlays per cap.	Ratio of Public Welfare to Capital Outlays
Term Limits	60.7 (14)***	-40.1 (5.19)***	0.971 (0.088)***
Unemployment	13.1 (8.42)	1.89 (2.89)	6.68 (3.78)*
Legislature Republican	2.41 (0.762)***	0.346 (0.236)	0.007 (0.002)**
Federal Aid	0.191 (0.037)***	0.050 (0.015)***	0.0003 (0.0001)***
Gross State Product	0.012 (0.003)***	0.010 (0.001)***	-0.000001 (0.000008)
Outlier	78.9 (89.6)	452 (71.8)***	-1.73 (0.264)***
Constant	37.4 (109)	-89.2 (38)**	2 (0.407)***
R <sup>2</sup>	0.84	0.81	.77
Fixed effects vector decomposition, $n = 637$ Panel corrected standard errors reported in parenthesis * $p < 0.1$ ** $p < 0.05$ *** $p < 0.01$			

Looking at the impact of term limits on public welfare expenditures (model 2), I find that states with term limits will average \$60 more per capita in spending on public welfare, significant at a 99% confidence level. The term limit coefficient translates into at 7.4 percentage-point increase

<sup>6</sup> Alaska's high expenditure levels are explained by its severance tax revenues received from oil extraction.

in public welfare expenditures for term limited states over non-term limited states. My finding is consistent with model 1 which shows higher total expenditures for term limited states.

On the other hand, model 3 indicates that states with term limits spend \$40 less per capita on capital outlays, also significant at a 99% confidence level. On average this is a 13 percentage-point reduction. At a first glance, lower capital outlays would seem inconsistent with higher total expenditures in term limited states. However, I argue that lower capital expenditures reinforce the intuition behind the sort of impact that we would expect term limits to have upon fiscal policy decisions. As I have argued before, term limits should bias the focus of legislators toward the short run. Legislators will demonstrate a decreased preference for expenditure items that by nature provide mainly long-run benefits, accompanied by a higher preference for expenditures that offer political returns in a shorter period of time. Research indicates that capital outlays is the sort of expenditure item that already suffers from a short-run bias in the budget making process (Bourque, 1985). Since term limits serve to strengthen this short-run bias in lawmakers, it is consistent then to find that term limits reduce capital outlays.

Finally, in equation 4, I regress the ratio between public welfare expenditures and capital outlays on term limits. Previous literature finds an inverse relationship between these two expenditure items. I look to see whether term limits will accentuate that dynamic. I find that term limits significantly increase the ratio of public welfare expenditures to capital outlays at the 99% confidence level. In states with term limits, for every additional dollar spent on capital outlays, an additional \$.97 will be spent on public welfare. At the mean ratio, that increases the amount of state spending on public welfare as compared to capital outlays from 2.8 to 3.7.

Our visual inspection of figure 1 is confirmed. A higher ratio of public welfare expenditures to capital outlays is consistent with the inverse relationship that previous research

has identified between infrastructure spending and public welfare spending, except now it is more pronounced. Term limits increase the ratio of public welfare expenditures to capital outlays, suggesting that term limits create a substitution effect between these two expenditure items. A higher ratio between public welfare expenditures and capital outlays lends support to the argument that term limits shift the focus of legislators from long-run expenditure projects with intangible benefits to short-run expenditures that produce an immediate benefit to the voters and politicians alike.

## V. Other Findings and Suggestions for Future Research

While it is not the chief focus of this paper, I also examine the impact that term limits have upon state revenues. Thus far, I have only considered how term limits affect the expenditure side of fiscal policy. This is simpler to do, since expenditure outcomes are linked directly to policy choices made by legislators. The impact of fiscal policy choices on revenue levels is harder to discern since economic fluctuations and other exogenous variables can cloud the outcomes. However, the revenue side of fiscal policy holds important implications for identifying the full impact of term limits on state budgetary processes. Using a similar approach as my previous analysis, I estimate equation 5:

$$genrev_{it} = \alpha + \gamma N_{it} + \sum_{j=1}^5 \beta_j X_{it} + h_i + \varepsilon_{it} \quad (5)$$

Where  $genrev_{it}$  is general state revenues regressed on the term limit dummy  $N_{it}$ , along with the control variables  $X_{it}$  and the fixed effects estimator  $h_i$ . The results for equation 5 are shown in the following table:

**Table 4.** The Impact of Term Limits on General Revenue

Regressors	Model 5
	General Revenue per cap.
Term Limits	-94.1 (28.5)***
Unemployment	4.60 (12.2)
Legislature Republican	3.39 (1.09)**
Federal Aid	-0.09 (0.167)
Gross State Product	0.120 (0.010)***
Outlier	506 (276)*
Constant	-239 (271)
R <sup>2</sup>	0.93
Fixed effects vector decomposition, $n = 637$ Panel corrected standard errors reported in parenthesis * $p < 0.1$ ** $p < 0.05$ *** $p < 0.01$	

I find term limits to be negative and significant when regressed on general revenues, at a 99% confidence level. Term limits reduce state revenues by \$94 per capita, which translates into a 2.8 percentage-point reduction in state revenues. Again, I would argue that lower state revenues are a function of the horizon-shortening nature of term limits. Term limited legislators may hold a stronger preference for tax cutting policies as a means to generating a better rapport with voters.

Recall that in model 1, I found term limits to increase overall state expenditures. Now in model 5, I find that term limits reduce state revenues. According to my findings, term limits are a cause of fiscal stress in state budget-making processes. Because every state (excluding Vermont) has balanced budget requirements, state governments cannot simply run budget deficits; nor are states able to issue debt routinely (Briffault, 1996). Rather, when fiscal imbalances occur states must adopt expedients to resolve the discrepancy. These expedients

include dipping into the general fund (Cummings, 2007), the sale of state assets, delaying payment of liabilities to vendors, and finally using creative accounting practices. Such expedients highlight the fiscal stress that stems from the reluctance of legislators to cut expenditures and increase taxes. Equations 1 and 5 indicate that term limits contribute to the reluctance of legislators to reduce expenditures and raise revenues.

Just as I found term limits to impact specific expenditure categories differently, I would expect that term limits to have a non-uniform impact on different revenue sources. A preliminary analysis indicates that term limits have no significant impact on income tax revenues, a negative impact on sales taxes, and a positive impact on tobacco revenues. Measuring the effect of term limits on revenue sources is an ideal area for future research. This would provide better insight into the full impact that legislative term limits have had on fiscal policy outcomes.

## **VI. Implications**

The implications of my research do not paint a favorable picture for term limits and their impact on state fiscal policy. In the presence of term limits lawmakers are biased to favor public welfare expenditures over capital outlays. First, this could contribute to rising public welfare costs. The full fiscal impact of newly implemented public welfare programs usually are not felt until a later date. If lawmakers already have a tendency to create welfare programs without realistically considering their long-term fiscal costs, my research suggests that term limits will reinforce this short-sighted approach that lawmakers take to public welfare expenditures. Secondly, the substitution effect that term limits create between public welfare expenditures and capital outlays could hurt infrastructure projects, which already show signs of underfunding. In

its 2009 report the American Society of Civil Engineers gave the infrastructure in the United States a 'D' grade. The report estimates that \$2.2 trillion will be needed to bring America's infrastructure into a state of good repair. My research suggests that by diverting state funds to public welfare expenditures term limits will contribute to the underfunding of state infrastructure.

## **VII. Conclusion**

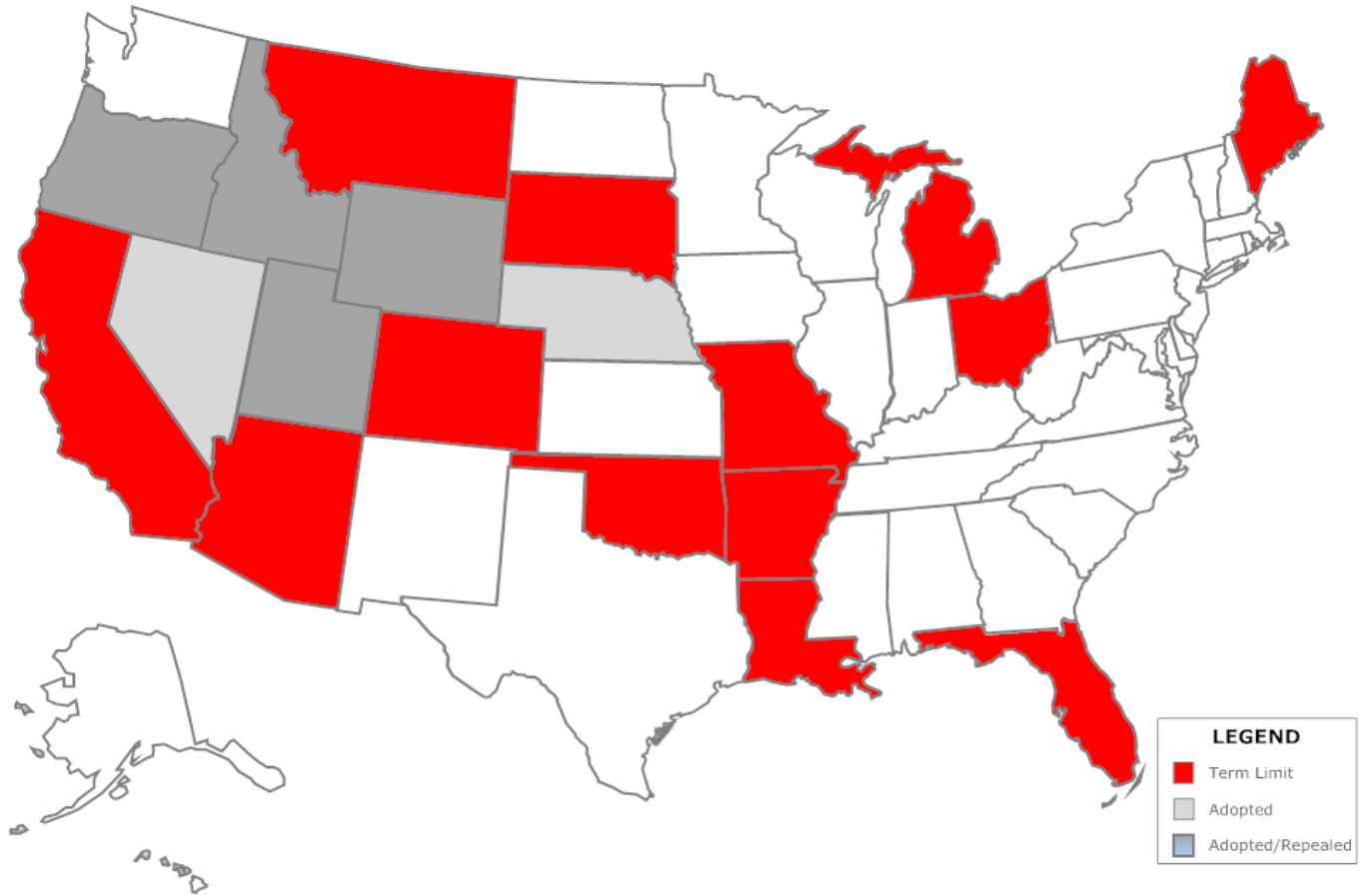
The purpose of this study was to test whether legislative term limits bias state lawmakers to adopt fiscal policies with short-term benefits while neglecting the long-term implications of these spending practices. In line with my hypothesis, I find an inverse relationship between public welfare expenditures and capital outlays. Specifically, I find that this relationship is more pronounced in the case of term limits. I attribute this preference for public welfare expenditures over capital outlays to the attraction lawmakers have for legislation that produces short-term benefits to voters and politicians alike (Garri, 2009). My research indicates that the impact of legislative term limits on capital outlays and public welfare expenditures creates a substitution effect between these two expenditure items.

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## Appendix A



Term Limited States: Alabama, Arkansas, California, Colorado, Florida, Louisiana, Michigan, Montana, Missouri, Ohio, Oklahoma, Ohio, and South Dakota