Revenue Patterns in the U.S. States

AN EMPIRICAL RE-EXAMINATION OF
PARTISAN POLICY VIEWS

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Work in Progress – Comments Welcome

Abstract
This paper empirically evaluates partisan policy influences on state-level general fund revenue changes in all 50 American states for the period 1987 to 2004. Contrary to the earlier literature on partisan tax policy in the U.S., I find little substantively meaningful evidence to back up the claim of a systematic difference in general fund revenue changes depending upon state governors’ party affiliation.

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1 Introduction

Few notions about economic policy in the U.S. command such wide-spread acceptance as the idea that there are marked differences in tax policy between Democrats and Republicans. Indeed, if one were to point out that Democrats favor high tax rates, while Republicans aim to lower them, many might conclude that not much more than the obvious has been stated.

Rather than re-affirming the conventional wisdom about tax policy in the U.S., however, this paper squarely challenges it. Employing state-level data for the fiscal years 1988 to 2004, I test how well partisan models of economic policy-making in the U.S. fit the actual record at the often neglected sub-national level. The surprising conclusion that I reach is that there is at best a limited difference between states ruled by Republicans vs. Democrats when it comes to revenue changes during the period under study. The regression results predict at most an average one-time partisan revenue adjustment effect of $70.72, which translates into a 4.85% difference in the average general fund revenue level per year.

As the results presented in this paper if not contradict, then at least challenge a vast, well-entrenched literature, extensive robustness checks are performed, and three different specifications of the dependent variable are discussed and various sub-periods of the data examined. Throughout, the main finding remains intact: There is no substantively meaningful evidence in favor of the partisan view of tax policy that is such a prominent feature of current thinking about economic policy in the U.S.

Section 2 of this paper reviews the central literature on state-level fiscal policy. Section 3 outlines the empirical approach pursued, discusses several important obstacles that have to be overcome in a sensible analysis of state-level revenue patterns, and shows how results based upon an analysis of revenue data in levels can lead to invalid inferences. Section 4 focuses on changes in revenue levels, shows that an OLS analysis is appropriate for the data, and discusses the regression results in detail, while section 5 concludes.
2 Earlier work

The determinants and effects of tax policy have been a topic of long-standing interest in the U.S. and around the world. Not surprisingly, this general interest is reflected in a vast scholarly literature on topics such as optimal taxation and its counterpart, the distortionary effects of taxation. Indeed, numerous textbooks have been written on these issues, too, and some of the best nowadays also include an extensive coverage of political determinants of tax levels. Yet, unlike in the case of the economic underpinnings of taxation, whether these political aspects travel easily from one setting to another—either across borders or to different, typically sub-national, levels within one country—remains relatively unclear.

While a voluminous body of work exists that discusses federal-level tax policy in the U.S., at the level of the 50 American states the literature on the revenue effects of political factors is still in its infancy. However, at least from the early 1990s on, several notable papers that focus on institutions such as term limits and balanced-budget requirements have been published in the leading journals in economics and political science, and I will briefly sketch their main ideas and results below.

Bohn & Inman (1996) conduct a comprehensive study of the effects that balanced-budget rules exert on the level of public deficits for a panel of 47 American states. Based on data for 1970-1991, they find that end-of-the-year balance requirements influence the level of a state’s general fund surplus positively. Importantly, spending cuts, not tax increases, are said to give rise to this result. In his study of states’ reactions to “fiscal shocks” in the early 1990s, Poterba (1994) also finds that balanced-budget rules matter. However, he attributes a much greater role to tax adjustments based on his data for 1988-1992, stating that “[b]oth the ordinary least squares and instrumental variables results suggest that states react to unexpected deficits with real changes in fiscal position. [...] Tax increases within the fiscal year make a relatively small contribution to deficit reduction, but tax changes that take effect
the next fiscal year are more important than spending cuts in closing unexpected deficits.”

Poterba (1994) also tests whether single-party rule, as opposed to divided government, has any effect on adjustment patterns. He concludes that in those states that have strict anti-deficit rules the two setups lead to different outcomes, with adjustment taking place more rapidly in states that are under single-party control. Indeed, this result could be explained by the fact that one would expect a gridlock over revenue vs. expenditure changes with divided government. By contrast, it is troubling for the view that under divided government the electorate has more difficulty attributing blame for unpopular measures to one of the parties that effectively share (some) power, which would lead one to expect that painful adjustments—raising taxes and cutting spending in already troubled times—should be easier to carry out under such circumstances. Apparently, balanced-budget requirements, which are often part of a state’s constitution, insulate policy-makers under unified government to a considerable extent from the wrath of the electorate.

Electoral accountability, in turn, is one of the main foci of the paper by Lowry et al. (1998). They conclude that accountability is higher under unified government, yet they also assert that Republicans are punished for an expansion of the size of state-level government activity, while Democrats are rewarded for it. Niemi et al. (1995), on the other hand, find that voters punish the incumbent party’s candidate for past tax increases, regardless of party affiliation, a finding echoed by Kone & Winters (1993).

Besley & Case (1995) examine budget data for the 48 continental U.S. states from 1950 to 1986. They find that Democratic incumbents faced with a term limit on average tend to

1Poterba (1994: 812)
2Krause (2000) shows for the federal level that the simple discrete distinction between unified and divided government can usefully be extended by considering the (continuous) degree of ideological fragmentation between the executive and the legislature. Data at this level of detail is not available at the state-level, however.
3Powell & Whitten (1993). See also the discussion in Berry & Berry (1992, 1994) on the politically most opportune moments for introducing new taxes or raising existing ones.
4To be more exact, Lowry et al. (1998: 759) state that Democratic governors may be rewarded for small increases in a state’s budget.
increase total taxes by $10 to $15 per year in their last term in office, while their Republican colleagues leave the tax burden unchanged. Moreover, “[a]n F–test rejects that, for Democratic governors taken as a group, the regression coefficients on different years in the electoral cycle are identical for governors who may run again and for governors who cannot.”

Clearly, both the notion that term limits will influence incumbent governors’ behavior and that Republicans and Democrats behave differently is vindicated by these results.

The explanation that Besley & Case (1995: 786) offer for the different taxation patterns is rather unconvincing, however: “Governors hold taxes and expenditures low in their first term [...] and voters allow them a second term. At that point the governors care less about putting in effort, resulting in increased taxes and spending.” Yet, this view leaves the difference in behavior between Democratic and Republican officeholders unexplained, as one is left to wonder why only Democrats but not Republicans give in to demands for higher spending levels that under balanced-budget rules accompany any revenue increase.

Alt and Lowry (2000) are the first to try to quantify the difference in the preferred scale of state-level expenditures and estimate that Democrats aim for an at least 50% larger public sector than Republicans. If their findings are correct, one should observe sizable differences in aggregate revenue trajectories under Democratic and Republican governors, as transitions in the governor’s mansion from one party to another were quite frequent during the period under study in this paper.

In a related article, Crain & Tollison (1993) have examined the effect of legislative stability and executive term limits on the volatility of fiscal policy for the U.S. states from 1969–1989. They find sizable effects for a wide range of political variables, including the legislature’s stability and gubernatorial term limits. Most importantly in the present context, “the impact of legislative stability on the volatility of taxes is 15 times the effect on the volatility of

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5Besley & Case (1995: 785)
6Alt & Lowry (2000: 1064)
spending. Approximately the same result holds for surpluses and deficits; surpluses and deficits respond much more dramatically to the expectation of legislative change than do expenditures.\(^7\) Yet, as so often, a result pointing in the opposite direction can be found, too. Kneebone & MacKenzie (2001) have studied the fiscal choices of Canadian provincial governments using data for 1966–1997 and find that “partisan responses are largely absent from revenues but appear more frequently in program spending choices.”\(^8\)

Overall, there is a near-consensus that it substantively matters whether the conservative or liberal party (or coalition) rules, with higher expected levels of taxation and revenue more generally under left-leaning governments, that divided government can attenuate these partisan effects, and that term limits might also play a role in the formulation and implementation of revenue policies. Consequently, the econometric analysis in this paper focuses mainly on these three political variables.

### 3 Empirics

Yearly data on the budget for all 50 states in the U.S. and on governors’ party affiliations as well as the states’ legislatures has been compiled for fiscal 1987—the earliest date for which data is available from the National Association of Budget Officers (NSABO)—to 2004.\(^9\) As there are good theoretical reasons to suspect that policies will differ not only between parties, but also under unified vs. divided government, a variable containing this information is included, too.\(^10\) Finally, the data set also contains dummy variables indicating

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\(^7\) Crain & Tollison (1993: 157–158)

\(^8\) Kneebone & MacKenzie (2001: 753)

\(^9\) Budget data is taken from NASBO (yearly). Per-capita state income data is taken from the Bureau of Economic Analysis. Political and demographic variables are compiled from the Statistical Abstract of the United States (various years), the CQ’s State Fact Finder (various years), and the websites of the National Conference of State Legislatures (www.ncsl.org) and the NGO U.S. Term Limits (www.termlimits.org). All U.S. dollar values were converted to constant 2000 U.S. dollars using Bureau of Labor Statistics data to control for the effects of nominal price-level changes.

\(^10\) See for instance the work by Alt & Lowry (1994) and Heller (1997).
(binding) gubernatorial term limits and the fiscal years before and after a party change in
the governor’s mansion between a Republican and Democratic officeholder.

I employ three different specifications of the dependent variable in my analysis. The first
two feature a dependent variable that is expressed in levels, while the third one captures
changes in levels. The former setups echo common practices in the literature on state-level
fiscal policy, and I proceed to show that they are inadequate for the data at hand. The
third specification is the preferred one, and all substantive results that I derive are based
upon information obtained via the various models that employ a measure of the general fund
revenue’s change as the dependent variable.

The first model used here has the level of per capita general fund revenue in U.S. dollar
amounts as the dependent variable. Using this specification, several variables are found to
be statistically significant, yet these results are misleading, as there is a time trend in the
data. Moreover, a swing in party dominance from Democratic to Republican from fiscal 1996
onwards proves problematic in this context, too.\footnote{See Andrews (2005) for a detailed discussion of the interplay between cross-section regressions and potential problems with them when common shocks are present.}

Next, a regression that relies on a “burden” measure for the general fund revenue level
is performed. It expresses the per capita general fund revenue levels in a given state as a
fraction of per capita state income. To take a very simple example, consider a state where the
per capita general fund revenue level stood at $1,000, while income per capita was $20,000
on average. The burden would then simply be 5%. Yet, just like in the case of using the
U.S. dollar amount of the general fund revenue as the dependent variable, the time series of
the actual burden level is integrated of order 2 and exhibits a positive time trend that leads
to biased OLS estimates.

The final measure of state-level revenue trajectories I use as a dependent variable in the
econometric analysis below measures the year-over-year change of the burden level. In order
to treat increases and decreases symmetrically, I compute the yearly change as a function of the natural logarithm of the burden, i.e., \( \text{change} = \ln(\text{burden}_t) - \ln(\text{burden}_{t-1}) \). After this adjustment, away from levels and towards changes, the aggregated series for the years 1988–2004 is stationary, as indicated by an Augmented Dickey-Fuller (ADF) test.

**Summary statistics and first OLS results**

All in all, budget data and information on other economic and political variables has been collected for a panel of all 50 U.S. states for the fiscal years 1987 to 2004, resulting in 900 complete observations.\(^{12}\) The 33 observations where the governor was neither a member of the Democratic nor the Republican Party were excluded, as were all 17 observations where the year-over-year change in general fund revenues exceeded 25 percent.\(^{13}\) In addition, the observations for the year 1987 are needed to initiate the change rate computation, yet in the end, even after all adjustments, 801 observations remain and form the basis for the analysis. Table 1 reports key summary statistics.

All regression results reported in this paper make heavy use of qualitative regressors to ensure that the variables that have theoretically been identified as potentially relevant are all included in the regression models at some point.\(^{14}\) Table 2 presents information on the influence of party affiliation and binding term limits for the three different specifications of the dependent variable discussed above. Interestingly, while in models 1 and 2 in table 2 several variables are reported as statistically significant, in the last set of results no variable is statistically significant at conventional levels, i.e., at the 90% level or above. In what follows, I argue that only model 3’s results are valid, while the estimates for models 1 and 2

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\(^{12}\)Note that a fiscal year is named after the calendar year in which it ends. The federal fiscal year 2006, for instance, began on October 1, 2005, and ended on September 30, 2006. Information on fiscal year start and end dates, which vary between states, can be found in compact form in ACIR (1995: 4–5, table 2).

\(^{13}\)These changes often reflect one-time events, such as new revenue sharing agreements between state and local governments.

\(^{14}\)See Gujarati (2003), chapter 9, on this approach.
<table>
<thead>
<tr>
<th></th>
<th>Democratic</th>
<th>Republican</th>
<th>Sum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Governors’ party affiliation</td>
<td>373</td>
<td>428</td>
<td>801</td>
</tr>
<tr>
<td></td>
<td>(46.4%)</td>
<td>(53.4%)</td>
<td>(100%)</td>
</tr>
<tr>
<td>Unified government</td>
<td>177</td>
<td>149</td>
<td>326</td>
</tr>
<tr>
<td></td>
<td>(22.1%)</td>
<td>(18.6%)</td>
<td>(40.7%)</td>
</tr>
<tr>
<td>Binding term limit</td>
<td>83</td>
<td>104</td>
<td>187</td>
</tr>
<tr>
<td></td>
<td>(10.4%)</td>
<td>(13.0%)</td>
<td>(23.3%)</td>
</tr>
<tr>
<td>Average per capita income</td>
<td>$25,192</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average per capita general fund revenue level</td>
<td>$1,457</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average burden</td>
<td></td>
<td></td>
<td>5.74%</td>
</tr>
</tbody>
</table>

Frequency of party switches in the sample (Governor/Legislature) [if unreported, then = 0]

<table>
<thead>
<tr>
<th>Party Switches</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Republican/Republican to Democratic/Republican</td>
<td>5</td>
</tr>
<tr>
<td>Republican/Democratic to Democratic/Republican</td>
<td>1</td>
</tr>
<tr>
<td>Republican/Democratic to Democratic/Democratic</td>
<td>17</td>
</tr>
<tr>
<td>Democratic/Democratic to Republican/Democratic</td>
<td>17</td>
</tr>
<tr>
<td>Democratic/Republican to Republican/Republican</td>
<td>5</td>
</tr>
</tbody>
</table>

Note: Percentage figures may not add up exactly due to rounding.

are plagued by biases arising from the presence of time trends in the data and thus cannot serve as a sound basis for inference.

**Examination of the data in levels**

Model 1 uses the general fund revenue level expressed in U.S. dollar amounts as the dependent variable. This is the simplest possible setup, yet it is plagued by a notable time trend in the data: Figure 1 shows the trajectory of revenues from 1988 to 2004 and a ten-year forecast based upon an ARIMA(2,2,0) specification.\(^{15}\) What is evident from figure 1 is that even

\(^{15}\)The aggregate data is obtained by adding up the real per capita revenue for all 50 states for every year in the sample, thus eliminating the effect of population growth. On a more technical note, only differencing the series shown in figure 1 twice gives us a stationary series, as the Augmented Dickey-Fuller test shows. The plots of the auto-correlation function (ACF) and partial auto-correlation function (PACF) hint at an autoregressive process, as the ACF does not end abruptly at some point, while the PACF does not dampen
## Table 2
OLS regression results for the impact of term limits

<table>
<thead>
<tr>
<th>Independent variable</th>
<th>Model 1</th>
<th>Model 2</th>
<th>Model 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Republican governor without binding term limit</td>
<td>$-99.46$ (73.99)</td>
<td>$-0.0020$ (0.0023)</td>
<td>$-0.0052$ (0.0063)</td>
</tr>
<tr>
<td>Republican governor with binding term limit</td>
<td>$-150.55^*$ (76.73)</td>
<td>$-0.0048^\Diamond$ (0.0025)</td>
<td>$0.0010$ (0.0072)</td>
</tr>
<tr>
<td>Democratic governor without binding term limit</td>
<td>$-123.00$ (76.28)</td>
<td>$-0.0009$ (0.0025)</td>
<td>$0.0021$ (0.0067)</td>
</tr>
<tr>
<td>Intercept</td>
<td>$1560.79^{**}$ (66.33)</td>
<td>$0.0592^{**}$ (0.0022)</td>
<td>$-0.0022$ (0.0055)</td>
</tr>
</tbody>
</table>

**Benchmark**

Democratic governor with binding term limit

Dependent variable: model 1 = revenue level, model 2 = burden level, model 3 = change ln(burden). *Heteroscedasticity-adjusted standard errors are shown in parentheses. Levels of statistical significance are denoted as follows: $^\Diamond p < 0.10$, $^* p < 0.05$, $^{**} p < 0.01$. N = 801.

The specification that provides the best fit by econometric standards does poorly when one considers its substantive adequacy, and the long-witnessed trend of increasing per capita state revenue levels would be broken if we believed the forecast to be accurate, an unlikely, albeit not impossible result. As a consequence of the seemingly poor substantive fit of the ARIMA(2,2,0) model, I do not pursue the analysis of state revenue in U.S. dollar amounts any further, but rather turn to an examination of the state-level tax burden (model 2) next.\(^1\)

The only change in model 2 vs. model 1 is that the dependent variable now is the relative tax burden, which is simply the fraction of per capita general fund revenue relative to per capita state income, thus controlling for the fact that especially many Southern states in the U.S. grew faster during the sample period than the national average. When using the relative tax burden as the dependent variable, the regression results show that unified Republican governments are associated with lower burdens than all other setups, yet down, either, and because the Akaike information criterion (AIC) indeed reaches its lowest value for an ARIMA(2,2,0) specification, it is used as the basis for the forecast for the fiscal years 2005–2014.\(^2\)

\(^1\)Lowry et al. (1998) discuss the historic upward trend in state spending in more detail.
a Republican governor faced with a non-Republican legislature appears to act no different than a Democratic governor faced with a non-Democratic legislature. Once more, however, these results have to be interpreted with considerable caution. As an ADF test shows, the aggregated time series for the general fund revenue burden is not stationary, suggesting biased OLS results yet again. Some descriptive statistics are interesting in this context, too.

On average, the burden level rose from 5.40% to 5.64% (+0.24 percentage points) in the first year after a transition to a Democratic governor, while it also rose, albeit a little less, from 5.44% to 5.49% (+0.05 percentage points) after a transition to a Republican governor, and the partisan difference in the first year after a switch is equal to just 0.19 percentage points.
Overall, given the well-known econometric problems that a time trend causes (Phillips 2003), including the fact that using an OLS framework will produce biased coefficient estimates in its presence, the results reported for models 1 and 2 in table 2 are not trustworthy, the intuitively appealing findings they produce notwithstanding. To compound the problems with using the level of general fund revenues as the dependent variable further, there is also a marked downward trend in the share of states with Democratic governors in the second half of the time-period under study. Taken together with the upward time trend, this pattern renders any statistical analysis of levels highly suspect and points towards the conclusion that the effects reported for models 1 and 2 might simply be statistical artifacts.

4 Examination of the data in changes

Unlike in the two cases discussed so far, the third specification of the dependent variable, which looks at the change in the natural logarithm of the per capita general fund revenue burden (model 3), is not plagued by econometric complications arising from the presence of a time trend, as indicated by an ADF test. However, one persistent problem when examining this data is that there are often no strong theoretical priors that could guide the analysis. Consider, for instance, the effect a term limit might have on an incumbent’s behavior. As she cannot be re-elected, she might decide to implement her preferred policy in her last term in office. In her first term in office, however, she might not feel so uninhibited, as she cannot disregard the electorate’s wishes too much if she plans on standing for re-election. Conversely, she might want to change revenue levels most when coming into office in order to signal her type to voters, especially if there has been a switch in ruling parties, and there

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17 A time-trend in the data violates the assumption of mean-stationarity that is a crucial component of the unbiasedness proof for OLS, and—common practice notwithstanding—simply including year dummies or a one-year lag term in the regression analysis does not adequately address this problem.

18 For the ADF test, the yearly change in the burden is set to the average of all 50 states’ changes in that year. One should keep in mind that in the econometric analysis below no such step takes place and that the results presented are therefore not influenced by any averaging.
is simply no need for vigorous action in her second term as revenue levels are already in line with her preferences. Indeed, there are good theoretical reasons to suspect either a move towards higher or lower revenue levels for all the political variables safe party affiliation, so that the empirical record has to settle the question which of the countervailing effects prevail.

Despite the weak guidance that theoretical considerations provide us with, one can identify some cases where partisan influences should be particularly pronounced if the partisan policy view is correct. First, when a Republican governor is succeeded by a Democrat, revenue levels should subsequently increase. Likewise, when a Democrat is succeeded by a Republican, revenue levels should fall. These expectations could be moderated by the effects of divided government, though, so that we might expect the most pronounced revenue level increases when there is a switch to a Democratic governor who is faced with a Democratic legislature, while revenue levels should fall most after a switch to a Republican governor who is backed by a Republican legislature. There are some arguments regarding the impact of unified vs. divided government that point in the opposite direction, however, so the possibility that the strongest effects ensue when governors are faced with divided government is also examined. The rationale behind this approach is that voters will generally find it easier to attribute blame for unpopular policies to a specific party under unified government, a fact that might attenuate the fervor of both governors and legislatures when it comes to implementing their preferred policies under such circumstances.¹⁹

• Term limits

The first regression analysis carried out, whose results were already presented in table 2 above, sheds light on the behavior of governors who are faced with a term limit. Given the uncertainty about the effect of term limits, I did not have any theoretical priors regarding the signs of the regression coefficients. Discounting the results for models 1 and 2 for the reasons discussed at length above, the analysis reveals for model 3 that, strikingly, not a

¹⁹See Berry & Berry (1994) and Powell & Whitten (1993).
single coefficient is statistically significant at the 95% level, and I thus conclude that the presence or absence of term limits does not exert any systematic influence on state-level general fund revenues.

- **Divided vs. unified government**

Next, the effect that divided vs. unified government has on state-level fiscal policy is examined. The results obtained by running this regression are shown in table 3. In contrast to the regression results for the impact of term limits, there are several coefficients that are statistically significant in this case. Yet, in substantive terms, the burden difference between a state that has a unified Democratic government and one that is under Republican control amounts to only 1.3% of 5.74% (model 4). Put differently, we expect the burden to differ on average by $18.92 between the two setups. As a fraction of average per capita GDP, this partisan difference translates into 0.075%. The estimated average difference falls even further to 1.02% of 5.74% for the unified Democratic and divided Republican case (model 5), or about $14.79.

To ensure that the results obtained for the full sample are not driven by unusually large swings in single years, an analysis of three ten-year sub-samples, spanning the years 1988–1997, 1991–2000, and 1994–2003, was performed, too. The analysis of the first subperiod does not yield a single statistically significant coefficient at the 95% level, even though the ones that are significant at the 95% level in table 3 are both significant at the 90% level, with their size very close to what is reported in table 3. For subsample 2, spanning the years 1991 to 2000, again not a single coefficient is statistically significant at the 95% level, and the $t$-values drop across the board. Finally, in the third subsample, for the years 1994 to 2003, only the intercepts are statistically significant at the 95% level. In the case of model 4, a unified Republican government is expected to on average lower general fund revenue levels by 1.41%, or $21.66, vs. all other constellations, while model 5 predicts that a Republican
Table 3
OLS regression results for the effect of divided vs. unified government

<table>
<thead>
<tr>
<th>Independent variable</th>
<th>Model 4</th>
<th>Model 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Democrat, unified government</td>
<td>0.0129* (0.0058)</td>
<td>0.0101* (0.0050)</td>
</tr>
<tr>
<td>Democrat, divided government</td>
<td>0.0015 (0.0064)</td>
<td>-0.0012 (0.0056)</td>
</tr>
<tr>
<td>Republican, unified government</td>
<td>—</td>
<td>-0.0027 (0.0052)</td>
</tr>
<tr>
<td>Republican, divided government</td>
<td>0.0027 (0.0052)</td>
<td>—</td>
</tr>
<tr>
<td>Intercept</td>
<td>-0.0076◊ (0.0043)</td>
<td>-0.0048 (0.0031)</td>
</tr>
</tbody>
</table>

Benchmark | Republican governor, unified government | Republican governor, divided government

Dependent variable: year-over-year change in ln(general fund revenue burden per capita).
Heteroscedasticity-adjusted standard errors are shown in parentheses. Levels of statistical significance are denoted as follows: ◊p < 0.10, *p < 0.05, **p < 0.01. N = 738.

governor operating under divided government will on average lower the revenue level by 0.79%, or $12.18, when compared to the three other possible combinations.

• Change in the governing party
Given the null result that was found for the effect of term limits and the substantively small effects of unified vs. divided government, one major aspect of state-level fiscal policy remains to be examined. This section studies the behavior of Democratic governors who succeeded a Republican officeholder and Republican governors who followed a Democrat in office. Under these two setups, the partisan policy model strongly suggests that revenue levels will rise in the former case and fall in the latter. Unlike in the earlier instances, where it could potentially be argued that there was no need for adjustments because revenue levels might already have been at or close to the governors’ ideal points, if no sizable adjustment effects are found here, then one has to wonder whether the partisan model actually generates useful
predictions or not.

In order to measure the impact of a partisan change in the governor’s mansion, I specify four models that once more rely heavily on qualitative regressors. Given the results from table 3, I distinguish not only between party affiliation and the time that has passed since a switch, but also between unified and divided government. The partisan policy view predicts the strongest effects in the case of a switch to either a unified Republican or Democratic government, and the adjustments that one ought to observe in these cases should be sizable.

As a look at table 4 shows, in the first year after a party change in the governor’s mansion, Democratic officeholders faced with a likewise Democratic legislature indeed do oversee rising revenue levels (model 7). Yet, over the longer run, i.e., when all later years after a switch and before the next change are taken into account, no further adjustments take place.20 Thus, there is a “jump” upwards in the first post-election (fiscal) year, but it is a one-time event, albeit one that persists during all subsequent years.

Substantively, the predicted jump in the first year on average amounts to just 4.85% of 5.74%, or $70.72, in the most favorable case, i.e., when the difference between the baseline category and the effect of the first-year switch is computed for model 7. In this case, there is a switch from a Republican governor and a non-Republican legislature to unified Democratic government, an event that took place 17 times during the sample period. Strikingly, Republican governors appear to neither lower revenues in the short nor in the long run when they succeed a Democrat under any constellation, at least not when standard levels of statistical significance are employed, nor does a switch to divided Democratic government appear to have any impact on revenue levels. In addition, given the magnitudes involved in those two cases where statistically significant coefficients were found, many would probably be hard-pressed to call the partisan effects computed here substantively significant.

20Alt & Lowry (2000) likewise find that adjustments only take place in the first two years after a change of the ruling party, yet they still maintain that there are marked differences in policy preferences between Democrats and Republicans.
Table 4
OLS regression results for after-switch behavior

<table>
<thead>
<tr>
<th>Independent variable</th>
<th>Model 6</th>
<th>Model 7</th>
<th>Model 8</th>
<th>Model 9</th>
</tr>
</thead>
<tbody>
<tr>
<td>Democrat, unified government, no switch</td>
<td>-0.0069 (0.0111)</td>
<td>-0.0097 (0.0110)</td>
<td>— (0.0111)</td>
<td>-0.0076 (0.0111)</td>
</tr>
<tr>
<td>Democrat, divided government, no switch</td>
<td>-0.0208 (0.0143)</td>
<td>-0.0198 (0.0143)</td>
<td>-0.0220 (0.0137)</td>
<td>— (0.0137)</td>
</tr>
<tr>
<td>Republican, unified government, no switch</td>
<td>— (0.0202)</td>
<td>-0.0129 (0.0202)</td>
<td>-0.0153 (0.0198)</td>
<td>-0.0114 (0.0198)</td>
</tr>
<tr>
<td>Republican, divided government, no switch</td>
<td>0.0043 (0.0122)</td>
<td>— (0.0122)</td>
<td>0.0057 (0.0122)</td>
<td>0.0036 (0.0122)</td>
</tr>
<tr>
<td>Switch to unified Democratic government (year 1)</td>
<td>— (0.0131)</td>
<td>0.0427** (0.0131)</td>
<td>— (0.0131)</td>
<td>— (0.0131)</td>
</tr>
<tr>
<td>Switch to unified Democratic government (year 2+)</td>
<td>— (0.0063)</td>
<td>0.0084 (0.0063)</td>
<td>— (0.0063)</td>
<td>— (0.0063)</td>
</tr>
<tr>
<td>Switch to divided Democratic government (year 1)</td>
<td>0.0166 (0.0126)</td>
<td>0.0182 (0.0127)</td>
<td>— (0.0127)</td>
<td>— (0.0127)</td>
</tr>
<tr>
<td>Switch to divided Democratic government (year 2+)</td>
<td>-0.0011 (0.0070)</td>
<td>-0.0004 (0.0071)</td>
<td>— (0.0071)</td>
<td>— (0.0071)</td>
</tr>
<tr>
<td>Switch to unified Republican government (year 1)</td>
<td>— (0.0125)</td>
<td>— (0.0125)</td>
<td>— (0.0125)</td>
<td>-0.0186 (0.0125)</td>
</tr>
<tr>
<td>Switch to unified Republican government (year 2+)</td>
<td>— (0.0061)</td>
<td>— (0.0061)</td>
<td>— (0.0061)</td>
<td>-0.0061 (0.0061)</td>
</tr>
<tr>
<td>Switch to divided Republican government (year 1)</td>
<td>— (0.0107)</td>
<td>— (0.0107)</td>
<td>0.0148 (0.0107)</td>
<td>— (0.0107)</td>
</tr>
<tr>
<td>Switch to divided Republican government (year 2+)</td>
<td>— (0.0048)</td>
<td>— (0.0048)</td>
<td>-0.0073 (0.0048)</td>
<td>— (0.0048)</td>
</tr>
<tr>
<td>Intercept</td>
<td>-0.0031 (0.0022)</td>
<td>-0.0047* (0.0023)</td>
<td>-0.0023 (0.0023)</td>
<td>-0.0023 (0.0022)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Benchmark</th>
<th>Republican governor, unified government</th>
<th>Republican governor, divided government</th>
<th>Democratic governor, unified government</th>
<th>Democratic governor, divided government</th>
</tr>
</thead>
</table>

Dependent variable: year-over-year change in \(\ln(\text{general fund revenue burden per capita})\).

Heteroscedasticity-adjusted standard errors are shown in parentheses. Levels of statistical significance are denoted as follows: \(p < 0.10\), \(*p < 0.05\), \(**p < 0.01\). \(N = 738\).
Robustness checks

As the regression results presented in tables 3 and 4 contradict a good deal of the previous literature on state-level fiscal policy, a visual inspection of the underlying data might help lend some credibility to my results. Figure 2 shows the change of the natural logarithm of the general fund revenue burden per capita, i.e., the dependent variable, by party affiliation of the governor. Arguably, it is difficult to discern a major difference in the change of the general fund revenue burden depending upon party affiliation, maybe safe for the fact that policies under Democratic governors appear to exhibit some more variability than those of their Republican colleagues.

As a further robustness check, I estimated the (potential) breakpoints of the time series of the yearly changes in the burden. There was a pronounced change in party composition at the level of the U.S. states from fiscal 1996 onwards, and one might expect this fact to be reflected in the form of a break in the time series at that point. In fiscal 1995, 30 of the 48 states in the sample were governed by a Democrat, while 18 had Republican governors. In fiscal 1996, however, this relationship had been almost reversed, and only 19 states still had Democratic governors (−36.67%), whereas the Republicans recorded a large gain of 11 governorships for a total of 29 (+61.11%). Overall, if the partisan policy theory is accurate, one would expect a break in the general fund revenue time series at the end of fiscal 1995. Yet, as a structural break computation shows, the statistically most notable break present in the data is found at the end of fiscal 1997, i.e., at a time when there was no change in the number of Republican governors at all (31 in both 1997 and 1998), while the number of Democratic governorships in the sample fell by just 1 (from 17 to 16).²¹

Overall, this finding is in line with the regression results presented in table 4, which

²¹In fact, the six largest trend breaks are identified at the end of the fiscal years 1990, 1992, 1994, 1997, 2000, and 2002. Note that the year 1995 is conspicuously absent from this list. The trend break estimation was performed in R 2.1.0 using the command breakpoints() from the strucchange package. Enders (2004: 200-207) presents a compact overview of how to identify structural changes in time series, while Bai & Perron (2003) discuss the procedure used here in more technical terms and much greater detail.
show that Republican governors who succeed Democrats simply “sit tight,” i.e., they do not oversee lower revenue levels than their predecessors. In particular, the trend break analysis does not show any break between fiscal 1995 and fiscal 1996, which indicates that the many newly elected Republican governors simply left the revenue policies of their Democratic predecessors unchanged.
5 Discussion

Given the results reported in section 4, the notion that governors’ policies follow partisan patterns with regard to revenue levels can only be upheld with considerable qualifications based upon the state-level revenue data for the fiscal years 1987 to 2004 examined in this paper. The effects found have a one-shot character and are at best on the order of 5 percent of the average general fund revenue level, which translates into about 0.28% of the average person’s yearly $25,192 GDP. What explains the complete absence of partisan after-switch effects when it comes to members of the Republican party and the only minuscule adjustments that Democrats make to the general fund revenue level despite the appealing logic of the partisan policy model remains an open question, however. Likewise, the discrepancy between the findings of this paper and earlier work discussed in section 2, most notably the papers by Alt & Lowry (2000) and Besley & Case (1995), is a bit puzzling. Especially the claim by Alt and Lowry that Democrats strive for an at least 50% larger public sector than Republicans is cast into serious doubt in light of my findings.

The pattern that Democratic governors raise taxes during their “lame duck” term reported by Besley & Case (1995) is not echoed here, either. How much of the divergence between their results and mine are attributable to different time periods covered cannot be ascertained with certainty, but it seems unlikely that this is the main cause for the contrasting results. Indeed, it appears more likely that the insufficient regard earlier papers, including theirs, paid to time trends lies at the heart of this difference.22

Overall, the results presented here notwithstanding, it is entirely possible that the partisan policy logic applies in other settings, first and foremost at the national level. Whether patterns similar to the ones found for the state-level can be found at the local level in the U.S., too, is yet another open question and a potentially fruitful avenue for future research.

22To my knowledge, the only paper published in a political science journal that at length discusses time trends in the context of an econometric analysis of fiscal policy, albeit at the federal level, is Krause (2000).
References


