

Term Limits: evidence from the US states

Lecture No. 7 Timothy Besley and Anne Case (QJE 1995)

Zhuravskaya/Sonin, Political Economics, Lectures No 7
www.cefir.ru/ezhuravskaya/PE_NES_05
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Timothy Besley
(LSE)



Anne Case
(Princeton University)



Stephen Coate
(Cornell University)

“Does electoral accountability affect economic policy choices? Evidence from gubernatorial term limits” Besley and Case (1995)

Why look at the US states?

- Advantages:
 - Plentiful comparable **panel** data on a wide range of policy outcomes and political variables
 - Similar economic and constitutional setting
- Disadvantages:
 - Relatively limited differences in institutional variation
- DATA:
 - Panel of US states between 1950s and 1990s.

Question:

Why would opportunistic politicians care for voter needs?

Reputation-building models of political behavior:

- **Asymmetric information about politicians type or about the state of the world**
- **Possibility of reelection raises politicians' effort since they are after political rents of the next term**
 - Start with Barro (1970)
 - Besley&Case (1995) also belongs to this literature

Term limits

- **Can be used to test reputation-building models**
 - **Exogenous change in the discount rate**
 - **Prediction: If politician cannot stand for reelection, reputation mechanism does not work**
 - **Should observe more opportunistic behavior (smaller payoff to voters, higher payoff to politicians)**

What may have an effect on the quality of testing?

Alternative mechanisms of disciplining politicians:

- **Party Control**
 - Parties may want to maintain reputation and may have other instruments to influence governor's career concerns other than elections
- **Life after Governorship**
 - Politicians independently of the party may want to continue political career and run for another office
- **Lack of Gubernatorial Discretion**
 - If the politician has no discretion, the policy outcome will not depend on T
- **These stories weaken the prediction of the theory**

A lot of variation...

TERM LIMITATIONS BY STATE, 1950–1986

State law:

States with no term limits	AZ, AR, CA, CO, CT, ID ^a , IL, IA, MA, MI, MN, MT, NH, NY, ND, RI, TX, UT, VT, WA, WI, WY
States limiting governors to 1 term in office	KY, MS, VA ^b
States limiting governors to 2 terms in office	DE ^c , NJ, OR
State law changed from no limit to 2-term limit (year of change)	KS (1974), ME (1966), MD (1954), NB (1968), NV (1972), OH (1966), SD (1956)
State law changed from allowing 1 term to allowing 2 terms in office (year of change)	AL (1970), FL (1970), GA (1978), IN (1974), LA (1968), MO (1966) ^c , NC (1978) ^c , OK (1968), PA (1972), SC (1982), TN (1980), WV (1972)
State law changed from 2-term to 1-term limit (year of change)	NM (1972)

a. No term limitation after 1956.

b. Restriction on terms enacted in VA in 1954.

c. Two-term limit over a lifetime. Enacted in DE (1968), MO (1968), and NC (1978).

Summary statistics:	All states All years	States with term limits	States without term limits
Number of observations	1776	1073	703
Sales tax	276.26 (127.43)	275.60 (127.59)	277.27 (127.27)
Income tax*	96.93 (110.04)	89.68 (105.21)	108.00 (116.24)
Corporate tax*	32.43 (29.07)	30.81 (25.93)	34.87 (33.11)
Total tax*	405.33 (198.00)	395.63 (187.97)	420.14 (211.67)
State spending*	849.74 (392.60)	811.59 (367.88)	907.97 (421.23)
Minimum wage* (<i>n</i> = 1769)	1.85 (1.48)	1.59 (1.48)	2.26 (1.36)
Maximum weekly benefits* (<i>n</i> = 1650)	177.99 (77.99)	162.53 (64.66)	201.83 (89.93)
State income*	8588.87 (2476.72)	8366.10 (2517.57)	8928.89 (2374.80)
Proportion elderly (65+) (<i>n</i> = 1728) ^b	0.099 (0.020)	0.099 (0.022)	0.100 (0.018)
Proportion young (5–17) (<i>n</i> = 1728)	0.238 (0.030)	0.239 (0.030)	0.236 (0.029)
State population (millions)*	4.080 (4.210)	3.542 (2.673)	4.902 (5.726)
Party of governor (=1 if Dem)*	0.598 (0.490)	0.656 (0.475)	0.509 (0.500)
Governor cannot stand for reelection	0.308 (0.462)	0.510 (0.500)	0

^aAsterisks denote that the mean of this variable is significantly different in states with and without term limits (*p*-value < 0.01).

Can we conclude from this that term limits lead to lower taxes and lower wages?

It could be that voters in the states with term limits prefer smaller government and higher turnover

Need covariates, Need fixed effects both for states and time

Identify effect from within-state variation

Empirical strategy

- **Estimate:** $P_{st} = \zeta_s + \psi_t + \gamma T_{st} + \alpha Z_{st} + \epsilon_{st}$
- P_{st} – taxes, expenditures, state min wages, worker compensation
 - in constant dollars
- T_{st} – dummy =1 if governor cannot run again
- Z_{st} – set of controls (income, demographics)

Basic results

	Dep var: sales taxes	Dep var: income taxes ^b	Dep var: corporate taxes	Dep var: total taxes	Dep var: state expenditure per cap	Dep var: state minimum wage ^c	Dep var: maximum weekly benefits ^d
Incumbent cannot stand for reelection	7.86 (2.58)	8.74 (2.54)	0.57 (0.67)	6.71 (1.56)	14.38 (2.10)	-0.14 (2.57)	2.25 (0.83)
State income per capita (1000s)	17.46 (4.58)	9.96 (2.52)	6.60 (5.27)	25.46 (4.87)	3.52 (0.46)	-0.04 (0.88)	8.64 (3.92)
Proportion state popu- lation elderly	980.78 (5.38)	20.68 (0.08)	8.36 (0.13)	695.14 (2.74)	-1143.34 (2.21)	-9.22 (3.69)	-1358.73 (6.65)
Proportion state popu- lation young	229.57 (2.08)	1564.84 (9.39)	221.38 (5.92)	1590.94 (9.95)	1293.53 (4.00)	0.18 (0.10)	646.86 (6.67)
State popula- tion (mil- lions)	-0.99 (1.04)	7.68 (5.02)	2.61 (8.39)	-1.41 (0.62)	-16.70 (4.07)	-0.05 (4.39)	-7.74 (5.90)
R^2	0.8938	0.8721	0.8253	0.9170	0.9397	0.7619	0.7462
Number of observations	1728	1327	1364	1728	1728	1721	1604

T-stat – in parentheses

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Basic results -2:

- **When face binding term limits, governors go for:**
 - larger taxes
 - larger spending
 - smaller minimum wages
 - Governors may restrict certain special interests or the legislature when do not run again...
- **But parties may be important in extending the time horizon of policy-making**
 - Add party affiliation

Add party affiliation...

	Dep var: sales taxes	Dep var: income taxes ^b	Dep var: corporate taxes	Dep var: total taxes	Dep var: state expenditure per cap	Dep var: state minimum wage ^c	Dep var: maximum weekly benefits ^d
Democratic incumbent cannot stand for reelection	11.25 (3.55)	9.43 (2.56)	1.86 (1.95)	11.30 (2.42)	17.28 (2.17)	0.03 (0.51)	6.41 (2.02)
Republican incumbent cannot stand for reelection	-0.21 (0.04)	4.38 (0.78)	-1.61 (1.23)	-4.28 (0.68)	4.91 (0.50)	-0.46 (5.90)	-4.89 (1.28)
Governor's party (= 1 if Democratic)	2.72 (1.02)	8.07 (2.61)	-2.03 (2.30)	4.18 (1.13)	13.39 (2.13)	-0.15 (3.38)	-6.70 (2.42)
Controls included: income per capita, state population, proportion elderly and young	YES	YES	YES	YES	YES	YES	YES
R ²	0.8942	0.8734	0.8261	0.9175	0.9401	0.7660	0.7474
Number of	1728	1327	1364	1728	1728	1721	1604

- All of the tax effect is due to behavior of democratic governors (that's why the effects were weaker in the basic specification).
- Why? Internal party discipline may differ; also the way in which parties select candidates may differ

Total state taxes per capita

Dependent variables: ^a	All governors	Democratic governors only	Dem govts, term-limit states
Explanatory variables:			
Election year X governor can run for reelection	529.67 (10.01)	448.52 (26.72)	449.68 (20.11)
Election next year X governor can run for reelection	528.41 (11.13)	442.93 (27.40)	449.89 (21.24)
Election in 2 years X governor can run for reelection	534.26 (9.78)	452.53 (27.41)	451.78 (21.95)
Election in 3 years X governor can run for reelection	524.84 (11.33)	444.75 (27.69)	450.14 (21.73)
Election year X governor cannot run for reelection	541.25 (9.59)	472.43 (27.56)	469.85 (21.23)
Election next year X governor cannot run for reelection	536.60 (9.91)	464.71 (27.74)	463.31 (21.65)
Election in 2 years X governor cannot run for reelection	536.54 (9.29)	466.82 (27.53)	465.29 (21.33)
Election in 3 years X governor cannot run for reelection	533.76 (10.04)	460.59 (27.73)	457.88 (21.57)

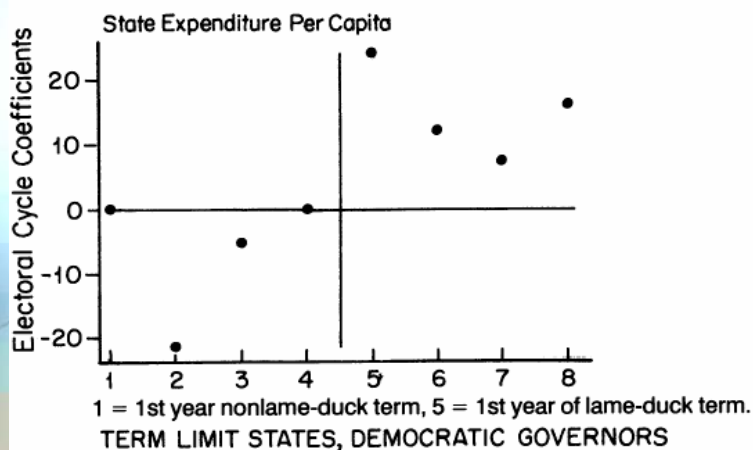
Induced fiscal electoral cycle

For Dem. Gov. - cycles:

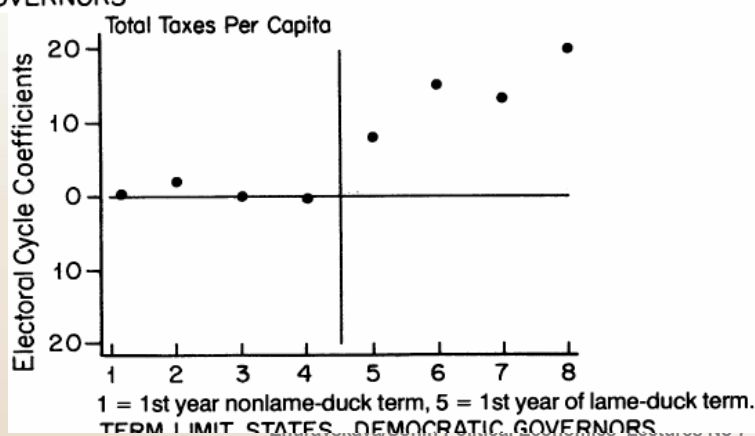
- between the terms
- within the term with binding TL b/w t=-3 & t=0
- It could take time to incorporate the shift in governor preferences into policy

F-test: (cycle X can run) = (cycle X cannot run) ^b	1.15 (.3312)	4.04 (.0029)	2.55 (.0383)
F-test: (election year X cannot run) = (election in 3 years X cannot run)	1.22 (.2693)	3.44 (.0639)	3.72 (.0544)

Estimated Fiscal Policy Cycle



- **Governors hold taxes and spending low in the first term to get re-elected and in the second term – increase both taxes and spending**



TL and Natural Disasters

Dependent variables: ^a	Total state taxes		
Explanatory variables:			
Incumbent cannot run for reelection	13.97 (2.72)	.1855 (3.38)	—
Democratic governor cannot run	—	—	27.56 (4.61)
Republican governor cannot run	—	—	-0.80 (0.11)
Natural disaster	12.65 (3.20)	—	—
Disaster X incumbent cannot run	—	0.52 (0.08)	—
Disaster X incumbent can run	—	17.19 (3.70)	—
Disaster X Dem incumbent cannot run	—	—	-4.99 (0.65)
Disaster X Rep incumbent cannot run	—	—	14.98 (1.42)
Disaster X Dem incumbent can run	—	—	16.58 (2.87)
Disaster X Rep incumbent can run	—	—	18.49 (2.35)
Governor's party = Democratic	—	—	-3.48 (0.86)

- **Exogenous source of variation in voter preferences for spending and taxes**
- **“Lame ducks” do not increase it further in response to a shift in voter preferences!**
 - They increase taxes and spending independently of a disaster
 - Again – all action is among governors-democrats

TL, Retirements and Congressional bids

	Dep var: total state taxes per cap				Dep var: state expenditure per cap			
Governor cannot stand for reelection	7.97 (1.83)	—	—	8.21 (1.87)	17.98 (2.60)	—	—	18.52 (2.68)
Governor retires and does not run for Congress	—	3.13 (0.59)	—	3.83 (0.72)	—	7.27 (0.75)	—	8.83 (0.92)
Governor retires and does run for Congress	—	—	-9.27 (1.65)	-9.20 (1.64)	—	—	-25.07 (2.50)	-24.91 (2.49)
R^2	.9102	.9101	.9102	.9104	.9374	.9372	.9374	.9377
Number of observations	1776	1776	1776	1776	1776	1776	1776	1776

(T-stats)

- No retirement effect for those who do not continue political career;
- Opposite from TL, effect for those who bid for Congress after retirement

Costs and Benefits of Term Limits

- **Grand conclusion:** reputation-building models found strong support in the data!!!
- These are more convincing results that x-section
- Fiscal electoral cycles due to term limits are a source of inefficiency
 - MDWL of taxation should be equalized over time; Distortion both in taxation and PG provision
- Why do we have TL?
 - TL reduce possibilities for entrenchment in politics
 - Accumulation of some forms of political capital by politicians who are in power for too long may damage electoral competition
 - “Breach of trust” with some privileged special interests