Many articles on public budgeting are informative. Some are also thoughtful. Few are wise. The discussion of revenue forecasting and the budget process by John L. Mikesell and Justin M. Ross in their article “State Revenue Forecasts and Political Acceptance: The Value of Consensus Forecasting in the Budget Process” goes beyond informative and thoughtful to wise. The case study of revenue forecasting in Indiana state government is informative. The review of the literature on state revenue forecasting is thoughtful. The wisdom lies in the authors’ conclusion that the parties involved in the budget process are better served by a forecasting process that produces revenue projections that are accepted and operate as constraints in the budgetary process than by projections that sometimes turn out to be more accurate after the fact. As Mikesell and Ross put it,

[T]he forecast represents the beginning of a political bargain over what assumptions are to be used in determining the policies that will take place in the near-term budget cycle, and this suggests that the study of revenue forecasting must expand to include an understanding...
of what elements of the forecast process make its resulting output the accepted baseline from which these determinations are made.

This is an important insight, buttressed by the description of the revenue forecasting process in the state of Indiana, where forecasts are produced by the Revenue Forecast Technical Committee (RFTC). The RFTC is a nonstatutory group with a representative from the State Budget Agency as well as a tax economist from the state university as a neutral expert. They are joined by appointees selected by the majority and minority leaders of each house of the legislature; in the past, those appointees have been staff members of the Senate Finance and House Ways and Means committees.

The RFTC has been producing forecasts for more than three decades. During that period, the official revenue forecasts have been accepted as constraints for the budget, and the governor and the legislators have been able to focus debate and discussion during the biennial budget process on substantive spending and tax issues instead of squabbling about revenue forecasts. Mikesell and Ross speculate that forecasts produced by a nonpartisan commission would not command the same level of acceptance as the projections produced by a diverse group representing the governor and the leaders of both political parties in each house of the legislature.

The authors are not dismissive of the issue of forecasting accuracy. Indeed, their careful analysis shows that the RFTC forecasts are generally more accurate than “naive” forecasts based on simpler methodologies that are sometimes recommended in the literature on public budgeting. But the heart of their argument is that the state budget process is better served by politically acceptable forecasts that provide workable constraints during budget adoption than by other approaches aimed at producing modest increases in accuracy. In any case, they argue, no other methods have been shown to produce estimates that are consistently more accurate.

The involvement of leaders of both political parties balances out at least one potential source of forecasting bias—the ideological tilt of each of the political parties, one toward increased spending and the other toward more limited government. It also means that a leader from each caucus in the legislature has some stake in the forecasting process and is able to speak up for the RFTC estimates if a legislator criticizes them. The authors do not discuss whether the RFTC process also reduces the risk of a tilt toward overestimation in election-year revenue forecasts.

The authors recognize that the Indiana solution may not be as effective in other states with different political cultures. Political leaders in states in the Upper Midwest or the Northwest may find nonpartisan forecasts by technical experts more politically acceptable. States such as Virginia, where considerable value is placed on high-grade credit ratings, may be more willing to tolerate revenue estimates that are conservatively biased, thus reducing the risk of overestimation, budget shortfalls, and the associated risks of ratings shocks.

Another jurisdiction where revenue estimates are not contentious is New York City. This huge local government relies on economically sensitive taxes for more than $20 billion of its budget and, in this regard, behaves more like a state government than a city. Unlike most states, the chief executive—the mayor of New York—is granted complete unilateral control over revenue forecasts in the City Charter. Underestimation of revenues has been a long-standing tactic by the executive to produce resources for the city’s peculiar structure of budget reserves. This tactic is widely recognized but rarely criticized, although Mayor Rudy Giuliani did draw some fire in the 1990s for revenue estimates that appeared to be grossly underestimated.

Another source of bias that the authors discuss briefly is risk aversion, the risk in question usually being criticism for overestimation of revenues. Presumably, this type of bias affects bureaucrats more than elected officials. Mikesell and Ross also note that collections seem more likely to exceed revenue estimates during periods of higher economic growth and that overestimates leading to revenue shortfalls are more likely when the economic is slumping.

For readers who have tried to manage state budgets through the vicissitudes of the business cycle, that pattern hints at a broader management strategy aimed at stabilizing the operating budget. During the growth period of the economic cycle, conservative revenue estimates can help build reserves; during downturns or stagnant periods, budget officials in some jurisdictions may be more willing to live with less conservative estimates, with the expectation that budget reserves will be available to fund shortfalls. These forecasting tilts presumably would be only one part of a multifaceted set of managerial actions aimed at stabilizing the budget through swings in the economic cycle.

We have more to learn about revenue estimating in states and large cities. I hope that other scholars who work on these problems will follow the lead of Mikesell and Ross and maintain an analytic framework that explicitly considers the politics of the budget process as well as processes and methods of revenue forecasting. This article makes the connection clear, and it encourages us to sustain and elaborate that dual focus in future research and discussion.