Howard Dean's Vermont Legacy

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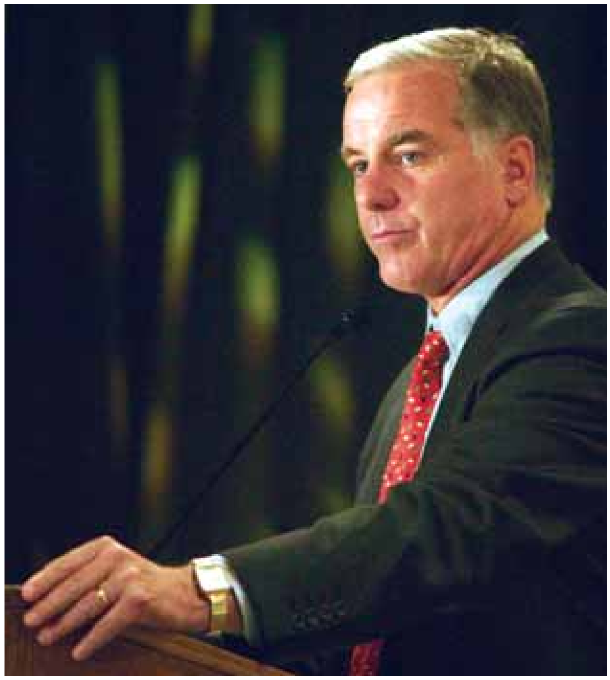
TIE's co-executive editor, who has known the Democratic presidential candidate for years, offers the inside story.



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The emergence of Howard Dean as a leading contender for the Democratic presidential nomination is naturally provoking interest in his record as governor of Vermont. The governor argues that he is a fiscal conservative because he consistently balanced the budget despite the lack of a constitutional mandate to do so. The media have generally accepted this assertion and portray Dean as a moderate chief executive.

The reality is much more complex. There is little doubt that Dean preferred a middle way in many areas of public policy but his freedom of action was greatly constrained by four factors. First, Vermont has a long tradition of high public spending which also requires a tax burden above the national average. Second, Dean inherited a program of fiscal austerity from his predecessor which shaped policy choices during his initial years. Third, Vermont's courts mandated changes in education spending which led to the most far-reaching transformation in the structure of Vermont government since the 18th century. Finally, Vermont requires its governors to seek reelection every two years. Such an electoral schedule limits the potential for politicians to promote structural reforms except when special circumstances prevail. Dean did not face any serious reelection challenges during his initial years but he did face a populist revolt at the end because of court orders pro-

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moting educational tax reform and gay marriages. The Dean legacy is very much a byproduct of both Vermont's political culture and the revolutionary changes mandated by the courts.

Vermont was a one-party Republican state before the 1960s. But it was not a conservative state. The state had a long tradition of high public spending because of its political structure. Vermont had a legacy of strong town governments ("Little Republics") and practically no county or regional governments. The towns were powerful because each of them had a seat in the state legislature irrespective of its population size. In 1900, 20 percent of Vermont's citizens elected a majority of the legislature. The ten largest towns had 25 percent of the population and 4 percent of the seats. During the late 19th century, many Vermont towns experienced depopulation because their rocky mountainous terrains caused people to move west in search of better land. The decline of the small towns created great pressure on the state government to provide financial assistance in order to maintain public services. The Republicans responded by enacting an income tax during the 1930s and using the funds to provide state aid for education as well as other public services. When the Democrats took power under Philip Hoff during the 1960s, they further expanded public spending and bequeathed the Republicans a large budget deficit. The deficit was $12.2 million in 1968 or 16 percent of general fund expenditures. The new Republican governor, Deane Davis, persuaded the legislature to enact a sales tax in order to sustain the new spending. As a result, Vermont's state and local government tax burden during 1971 was 14.8 percent compared to 12.1 percent for the nation.

In its period of ascendancy, the Vermont Republican Party supported a high level of public spending and taxation because of its belief that it was essential to provide good public services, especially education. Vermont is also a homogenous state without the conflicts over race and ethnicity that have undermined popular support for public spending in places such as the South. The new development in Vermont politics since the 1960s has been the emergence of a large group of left-wing legislators hostile to business for ideological reasons who favor income redistribution to reduce inequality, not just to finance education. Many of Vermont's left-wing politicians are urban dropouts from the 1960s. The most famous is the state's sole member of Congress, Representative Bernie Sanders (I). Sanders is an aging Peter Pan from Brooklyn who regularly wins reelection by campaigning as a left-wing populist challenging the evil ways of big corporations and Washington. Although Dean also comes from New York, he was never a populist and frequently clashed with the left-wing members of the legislature.

Dean became governor in 1991 upon the unexpected death of Richard Snelling, a Republican who had previously served during the late 1970s and early 1980s. He had returned in 1991 to clean up the large fiscal deficits resulting from the 1990–91 recession and the spending expansion during the administration of Democrat Madeleine Kunin. The deficits peaked at $65 million in 1992 or a sum equal to 10 percent of general fund expenditures. Snelling imposed a program of severe fiscal austerity in order to eliminate the deficit. He reduced public spending. He hiked the sales tax rate from 4 percent to 5 percent with a plan to sunset the hike in 1993. He significantly boosted Vermont's piggyback tax rate. Under Vermont's tax system, citizens pay a share of their federal tax liability to the state government. In the late 1980s, the piggyback tax rate was 25 percent. Instead of the traditional flat rate, Snelling made the tax system more progressive by introducing a 31 percent tax rate on federal income tax liability over $3,400 and a 34 percent rate on federal income tax liability over $13,100. Everyone else paid a 28 percent tax rate.

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Dean did not initially tamper with Snelling's policies because of the state's fiscal deficit. The $65 million deficit in 1992 was followed by a $46.2 million deficit during fiscal 1993. Vermont's fiscal position also was not as extreme as it had been at the end of the 1960s. State and local government taxation was equal to only 11.8 percent of the state's income compared to a national average of 10.8 percent. Dean allowed the income tax hikes to expire but he did not allow the sales tax hike to sunset. Two months after it expired, he called a special session of the legislature to sustain the sales tax rate at 5 percent. Many liberal Democrats were opposed to reducing the income tax but Dean was determined to restrain income taxes because of concern about the state's competitive position. Clinton had hiked the top marginal income tax rate to 40 percent at the federal level, so the Vermont piggyback system threatened to produce a top state tax rate above 11 percent. Dean recognized that such a high income tax rate would greatly erode the state's capacity to attract new business and produce jobs. Dean was also opposed to funding the government with new forms of gambling. As Vermont has no Indian reservations, the gambling advocates have never been able to develop any popular support for a casino. Dean also promoted many small tax increases on business. He raised the taxes on rooms and meals, telecommunications, gasoline, electrical energy, liquor, cigarettes, and corporate income.

Dean claims that he is a fiscal conservative because he balanced the Vermont budget, but he did not severely restrain public spending. During his tenure, Vermont's state and local tax burden grew from 11.8 percent to a peak of 12.5 percent in 1998 before dipping back to 12.1 percent in 2000. The Vermont general fund rose from $656.7 million in 1992 to $872.1 million in 2002, or a gain of nearly 33 percent over ten years. Vermont's high level of public spending is driven primarily by three factors. Vermont spends 5.7 percent of its personal income on education for children, the fourth-highest level in the nation and 1 percent above the national average. Vermont also spends 2.4 percent of its income on university education compared to a national average of 1.7 percent but much of this expenditure is covered by fees and tuition, not taxation. Vermont is very generous when it comes to spending on public welfare. Vermont recently spent $701 million on welfare or 4.5 percent of the state's income. Such spending causes Vermont to rank fifth in the nation and well above the state average of 3.0 percent. Public welfare includes aid to the poor, Medicaid, and other public spending on health care. Vermont spends heavily on transportation because of its rural character. The state spends 2.1 percent of its income on highways compared to 1.3 percent for the nation. The one sector where Vermont saves money is police and fire protection. It spends only 0.7 percent of its income on police and fire protection compared to 1.0 percent for the nation. As a result of the state's rural character, it has few police and many volunteer fire departments.

The state's sole member of Congress is Bernie Sanders (I), an aging Peter Pan from Brooklyn who regularly wins reelection by campaigning as a left-wing populist challenging the evil ways of big corporations and Washington.

Vermont Budget Position

1990	0
1991	-57.2 million
1992	-65.1 million
1993	-46.2 million
1994	0
1995	-14.5 million
1996	-14.5 million
1997	0
1998	0
1999	0
2000	0
2001	-8.4 million
2002	0
2003	0

Dean's most significant fiscal policy initiative was in the area of health care. Governor Madeleine Kunin had brought children in the age range of 0–6 under Medicaid during the 1980s. Dean broadened the coverage to include children aged 6–18 during the mid-1990s. Dean boosted the share of Vermonters covered by Medicaid from 8.0 percent of the population in 1990 to 18.4 percent in 1999. During the 1990s, the share of Vermonters without health insurance averaged close to 10.0 percent whereas in the nation it increased from 14.1 percent to 15.5 percent. The decision to broaden the state's role in health care also reduced the role of private insurance. The percentage of Vermonters with private health insurance fell from 80 percent in 1990 to 70.4 percent in 1999. Many insurance companies withdrew from the state because the Dean policies mandated that they charge the same price as Blue Cross and Blue Shield (no discrimination on the basis of age, health, etc.). Several thousand Vermonters lost their insurance coverage as a result of this policy. Dean's health care policy is the one factor which calls into question his claim to be a fiscal conservative. He never developed a new funding source for health care. He relied heavily on cost shifting from other departments which had surpluses. There were modest revenue gains from new taxes on tobacco and health care services. Expenditures have therefore been growing more rapidly than potential sources of funding. The Joint Fiscal Office of the Vermont Legislature is projecting that Medicaid will run a deficit of $52 billion in 2008 on spending of $262 million. Practically all states have growing Medicaid deficits, so Dean's legacy is not unique. But it does serve as a reminder that Dean is not a fiscal conservative when it comes to health care. The Cato Institute gave Dean a ranking of B for his fiscal policies during the early 1990s. But in the end they lowered the ranking to D because of the increased spending on health care and numerous small tax increases.

The most dramatic change in Vermont public policy during the 1990s was not initiated by Governor Dean. It resulted from a public order to equalize education spending among the towns. Vermont had a long tradition of funding education primarily through town property taxes supplemented by state aid to compensate for differences in local wealth. The legislature regularly devoted a large share of its time to developing education aid formulas reflecting differences in property wealth and income among Vermont's towns. As a result of the fiscal austerity during Dean's early years, there was a large decline in real state aid to education during the mid-1990s. A group of people from one of the poor towns filed a lawsuit to protest inequality in education funding and the Vermont Supreme Court responded by demanding a major change in the state's educational aid in order to reduce inequality. The legislature responded by abolishing Vermont's ancient tradition of relying on town property taxes to finance education and introduced a statewide property tax instead. Under the new law (Act 60), Vermont effectively centralized education spending at the state level and applied penalties on towns that attempted to spend more than the state average. In 1995, Vermonters had paid 55 percent of local taxes to the state and 45 percent to the towns. In 2000, they paid 79 percent to the state and 21 percent to the towns. In the nation, by contrast, taxpayers still pay 38 percent of local taxes to the towns/cities and 62 percent to the states.

What was distinctive about Dean's role in the debate about education tax reform was his failure to play a clear leadership role. Dean ruled out any attempt to use the income tax or gambling to bolster state aid to education and then abdicated the issue to the Democratic leadership of the Vermont legislature. Before the court order, the Democratic leaders of the House had been attempting to lay the groundwork for a statewide property tax. They favored a statewide tax because of their perception that the tradition of local control resulted in towns with ski resorts and large vacation-home communities being under-taxed relative to towns with less property wealth and larger populations. They hoped to use a statewide property tax to redistribute income from the rich ski towns to poorer communities. They were prepared to sacrifice Vermont's tradition of local control over education in order to achieve their economic objective.

New Hampshire had a similar crisis over education finance because of a court order to reduce inequality. But its political leaders reacted very differently. Democratic Governor Jeanne Shaheen ruled out abandoning New Hampshire's tradition of not taxing retail sales or wage income. She and the New Hampshire legislature instead cobbled together a compromise program which included a modest statewide property tax and increased fiscal transfer to poor towns. The legislature recently curtailed the statewide property tax but the courts have not yet intruded with new orders. On the contrary, there was an attempt to impeach the chief justice of the state in part because of popular resentment over this attempt to change the state's system of educational finance. Vermonters, by contrast, never attempted to challenge their Supreme Court despite the fact that it was driven by a clear political agenda resulting from the appointment of a former Kunin political advisor to the court.

Dean recognized that a high income tax rate would greatly erode the state's capacity to attract new business and produce jobs.

Chester Allen Arthur

Ralph Flanders

George Aiken

Vermont's Own Foreign Policy

Vermont politicians have often played novel foreign policy roles. In the 1880s, the first Vermont president, **Chester Allen Arthur,** tried to resist highly racist legislation from the U.S. Congress banning immigration from China. The Vermont Legislature declared war on Nazi Germany in September 1941, three months before Pearl Harbor. The first ambassador to the United Nations was Vermont Senator **Warren Austin.** The first member of Congress to challenge the anti-communist witch-hunt of Senator Joe McCarthy was Vermont Senator **Ralph Flanders.** Senator **George Aiken** proposed a unique solution to the crisis over Vietnam in 1967. He suggested that the United States declare a victory and withdraw.

If Dean had played a leadership role in Vermont's crisis, he might also have been able to forge a compromise which increased state aid without totally undermining the role of the towns in providing education for their children. But by allowing the legislature to play the leadership role, he presided over a constitutional revolution that has abolished an ancient tradition of local control and created the most centralized system of education finance in the nation. He did achieve his objective of avoiding higher income taxes but at a cost which it is still not possible to quantify.

The Vermont Republican Party supported a high level of public spending and taxation because of its belief that it was essential to provide good public services, especially education.

The court order effectively gave the left-wing Democrats in the Vermont legislature political cover for a radical change in public finance which would never have been endorsed by either a general election or a referendum. The legacy of the new legislation is that education spending has been growing rapidly because towns no longer have any incentive (local taxes) to restrain themselves. In order to avoid raising property taxes further, the legislature recently enacted an increase in the state sales tax rate to 6 percent and announced plans to study new ways to restrain education spending. The ultimate outcome will be a further erosion of local control over education. Some Republicans have proposed radical alternatives to the new system, such as using the statewide property tax to finance vouchers for every student, but the new Republican governor has been focused on fine-tuning the revenue consequences of Act 60, not launching a new revolution in Vermont's philosophy of education.

The one consolation of Act 60 is that it eliminated the risk of a budget deficit when the economy slowed during 2001 and 2002. As with the nation, Vermont has experienced large increases in house prices during the past five years. The property inflation has allowed the state to significantly boost its revenue from the property tax without hiking tax rates. If the state still depended as heavily upon income tax or sales taxes, its revenue growth would have faltered with the economy and pushed the budget into deficit.

Dean was generally supportive of Vermont's tradition of carefully regulating development in order to protect the environment. His critics allege that he did little to reduce the cost burden on business of complying with the laws but did intervene occasionally to help some companies get special treatment in return for expanding employment. Dean, for example, worked hard to persuade the Husky Injection Moulding Company from Canada to locate a factory in Vermont. He promised that he would make sure that the state's environmental regulations would not delay the project despite the fact that it violated the town plan and the regional development plan.

Vermont's economy experienced modest prosperity during the Dean years but generally trailed the nation. The decade of the 1990s began with the state experiencing a severe recession. If we compare Vermont with the nation, its growth rate during the decade ranked 37th. If we exclude the year 1990, its growth rate ranked 31st. Vermont's gross state product per capita grew by 1.9 percent annually during the 1990s compared to 2.2 percent for the nation. Vermont ranked below every New England state except for Maine and far behind the New Hampshire growth rate of 4.3 percent. Vermont's private-sector employment grew by 22 percent during the Dean years compared to 21 percent for the nation, 14 percent for New England, and 30 percent for New Hampshire. There was stagnation in manufacturing employment but construction employment grew by 27 percent. The number of jobs in state government expanded from 13,600 to 17,500. In 2002, Vermont's per capita income shot up to $29,567 or a level ranking 24th in the nation compared to 30th in the mid-1990s. Vermont's per capita income is also now equal to 95.6 percent of the national average or a record high in relative terms. The previous peaks were in 1930, when Vermont's per capita income was equal to 93 percent of the U.S. average and 1989, when it was equal to 94 percent of the U.S. average.

Dean never articulated any views on American foreign policy during his tenure as governor. It is unusual for governors to engage in debates about foreign policy but Vermont politicians have often played a novel role in that area. In the 1880s, the first U.S. president from Vermont, Chester Allen Arthur, tried to resist highly racist legislation from the U.S. Congress banning immigration from China. The Vermont legislature declared war on Nazi Germany in September 1941, three months before Pearl Harbor. The first ambassador to the United Nations was Vermont Senator Warren Austin. The first member of Congress to challenge the anti-communist witch-hunt of Senator Joe McCarthy was Vermont Senator Ralph Flanders. Senator George Aiken proposed a unique solution to the crisis over Vietnam in 1967. He suggested that the United States declare a victory and withdraw. Dean has developed a high rating in the opinion polls during recent months by criticizing the President's policy in

Iraq but it is the first time he has articulated any public views on foreign policy.

What does Howard Dean's record in Vermont portend for the nation if he becomes president?

It would imply three things. First, he will attempt to bolster the government's role in providing health care and reduce the number of Americans without health insurance. Second, he would be prepared to fund future growth of health care with taxes on consumption rather than income. Third, he will give Congress considerable discretion in proposing tax reforms and shaping fiscal policy.

Dean's campaign manifesto clearly spells out the first conclusion. He is an advocate of the government providing health insurance for all Americans. His position on federal fiscal policy contradicts his Vermont legacy. He wants to repeal the Bush income tax cuts and use the money to finance health care spending. If he were successful, there would be a large increase in both federal and Vermont marginal income tax rates. The great risk facing Dean is that his hostility to the Bush income tax cuts could turn him into the Walter Mondale of 2004. He could broaden his appeal beyond the left wing of the Democratic Party by returning to his Vermont roots and pledging not to raise income taxes.

The challenges that confront a governor are very different from those that confront a president, so it would be dangerous to extrapolate too heavily from state policies in defining a Dean agenda for the nation. But there is a Dean legacy from Vermont which defines him as a political leader. He understands the need for a state to have a competitive tax system. He is clearly obsessed with the health care issue, almost to the exclusion of everything else. He responds to major shocks or crises by turning to others for ideas as well as leadership. There is little doubt that Dean as president would immediately invest most of his political capital in obtaining health insurance coverage for all Americans. He would initially try to finance his plans to repealing the Bush income tax cuts, but if he failed he would not be opposed to relying on consumption taxes. The great uncertainties in a Dean presidency would center on his leadership style. The fact that he abdicated leadership on the most important tax question in Vermont's modern political history raises disturbing questions about how he would respond to national shocks or crises. Would he simply avoid confronting the issue? Would he turn over decision making to the cabinet or the Congress? Would he take responsibility for the policy they produced?

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There is no way to predict how a President Dean would behave compared to a Governor Dean. But the legacy from Montpelier during the 1990s clearly implies that in a Dean presidency there could be a major power shift from the White House to Capitol Hill. Ironically, congressional leaders, such as John Kerry and Richard Gephardt, could play a more influential role in a Dean presidency than they have ever played before.

The financial markets have not yet formed a clear view on the Democratic presidential candidates. Dean has clearly emerged as a frontrunner by appealing to the left wing of the party and people deeply hostile to the Bush administration. But as president, Dean would probably pose no greater threat to the economy than the new president of Brazil, Lula da Silva. As a result of his leadership style, however, the markets would not be able to fully grasp the risks and opportunities of a Dean presidency without knowing the composition of Congress. If Dean took office with a Republican Congress, there would be gridlock on many issues. If Dean took office with a Democratic majority in the House and Senate, the markets would be concerned about the fiscal consequences of his health care proposal. Would Congress risk repealing the Bush tax cuts? Would Dean risk expanding the federal deficit to $600–700 billion in order to enact the health insurance program without tax changes? As with Vermont during his early years as governor, President Dean would inherit a fiscal legacy from the Bush administration that would significantly constrain his freedom of action. In Vermont, he hiked the sales tax and waited for the deficit to fade away. As president, he could be forced to choose between significantly increasing the federal deficit or deferring his health care agenda until the end of his term. At present, it is doubtful that even Howard Dean knows how he will reconcile his spending ambitions with the economic legacy of George Bush. ◆