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PolicyBrief

Securing a Fiscally Sound Future for Tennessee

Reforming the state spending cap to curb government growth and promote prosperity

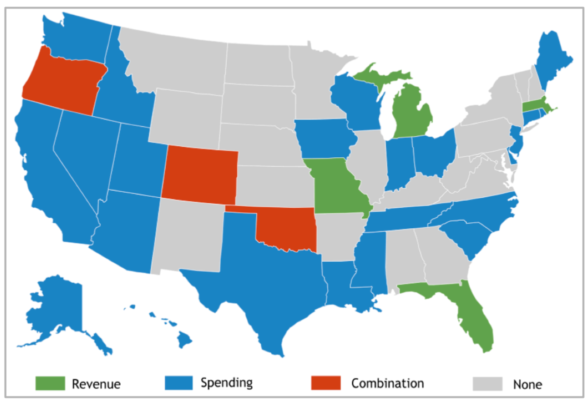
by Justin Owen

Introduction

Tennessee is hailed as a fiscally conservative state relative to its counterparts, and indeed government spending and debt are limited in the Volunteer State. As of 2012, Tennessee had the second smallest state debt per capita, out-performed by only Nebraska.[1] The state also remains well below the national average in total spending per capita.[2] One factor that is designed to restrain out-of-control government growth is the Copeland Cap, a spending limitation law enacted under the leadership of former state Rep. David Copeland (R-Ootelwah).

Voters approved the Copeland Cap as a constitutional amendment in 1978. In short, the cap ties the growth of the state budget to the growth of the state economy. If the proposed budget grows at a faster pace than the previous year's average personal income growth, the General Assembly must cast two collective votes to pass the budget. In addition to the vote on the budget bill, the legislature must pass all excess spending in a separate measure.[3] It is important to note that this limitation only applies to state expenditures, and does not impact federal expenditures related to federal or joint state-federal programs. Such a spending limit is not unique; 30 states have some form of spending or revenue limitation.

Figure 1. States with tax or spending limits (2010)



There are, however, two flaws in the existing Copeland Cap. The first is that the legislature may override the cap easily. The additional vote that must be cast to exceed the spending limit only requires the support of a simple majority of legislators. The second problem lies in the calculation of the cap itself. By calculating the cap using personal income growth, the legislature is allowed to make substantial increases in year-over-year spending, even without casting an additional vote. In order to promote fiscal responsibility into the future, the Copeland Cap should be revised in two ways: First, overriding the cap should require a supermajority, or two-thirds, vote of the legislature. Second, the calculation should be changed to the more limiting factor of population plus inflation growth. These two solutions will strengthen the Copeland Cap and preserve Tennessee's status as a fiscally responsible state for generations to come.

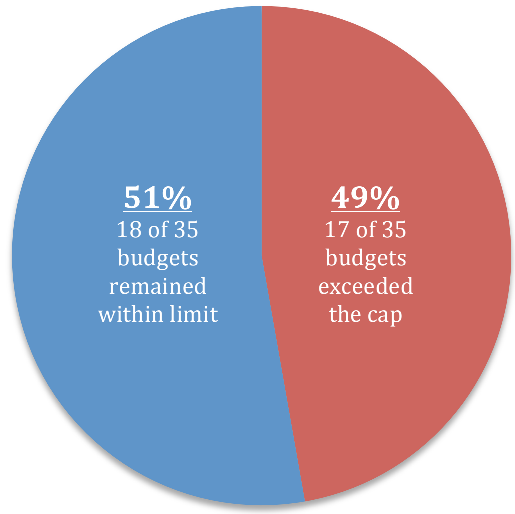
The Time to Act is Now

Fortunately, there is no better time to move forward with these adjustments. In May 2013, Gov. Bill Haslam signed a law that directs the State Funding Board, comprised of Haslam, the Commissioner of Finance and Administration, the Comptroller of the Treasury, the Treasurer, and the Secretary of State, to study the issue. It also directs the Funding Board to report its recommendations to the speakers of the House and Senate in February 2014, giving them time to consider and act on the recommendations during the 2014 legislative session.[4]

History of Spending Under the Cap

In order to understand the flaws in the current cap, it is instructive to review state spending trends dating back to the enactment of the Copeland Cap in 1978. Since that time, the legislature has passed 35 annual state budgets. Lawmakers exceeded the Copeland Cap 17 those years, or 49 percent of the time.[5] The longest period that the legislature went without exceeding the spending limit was the five years immediately following the law's passage.

Figure 2. Budgets Exceeding vs. Not Exceeding Cap



The total amount of excess spending allowed by these votes was more than $4.4 billion.[6] The legislature has exceeded the spending limit by as little as $46 million and by as much as $771 million in a given year, averaging $256.7 million each year it broke the spending threshold.

Figure 3. Years Cap Exceeded and Excess Amount

Fiscal Year	Excess Spending
1984-1985	$396.1 million
1985-1986	$58.0 million
1986-1987	$100.0 million
1988-1989	$101.0 million
1989-1990	$74.0 million
1991-1992	$703.1 million
1992-1993	$450.0 million
1996-1997	$55.0 million
1999-2000	$270.0 million
2002-2003	$771.0 million
2003-2004	$275.0 million
2006-2007	$46.0 million
2007-2008	$57.3 million
2009-2010	$248.5 million
2010-2011	$376.6 million
2011-2012	$250.0 million
2012-2013	$132.5 million
TOTAL	**$4.4 billion**

The Problems with the Current Cap

The ease of exceeding the cap speaks to the first flaw in the law's well-intentioned design. Rather than allow the General Assembly to exceed the spending limit by casting a simple majority vote, the Tennessee Constitution should be amended to require a supermajority, or two-thirds, vote to exceed the cap. This will strike an important balance by raising the threshold for approving excess spending, while preserving the legislature's ability to increase spending in times of emergency or disaster.

The second, and more important, flaw in the current cap, should be addressed immediately. This relates to the method used to calculate the spending limit. The Tennessee Constitution limits budgetary growth to "the estimated rate of growth of the state's economy as determined by law."[7] Statute dictates that the "state's economy" is reflected in the average personal income growth.[8] Thus, the state budget cannot grow at a faster rate than the previous year's personal income growth rate without a separate vote of the legislature.

Since the passage of the Copeland Cap in 1978, personal income has grown by an average of 6.21 percent.[9] It has grown by as much as 11.5 percent in a given year, and has only once declined year over year (-1.97 percent in 2009). As a result, this method of calculating the spending limit has allowed for consistent growth in the state budget. In fact, only twice since 1978 have state appropriations declined from one year to the next, once in 2001 and again in 2008. In all other years, state budget expenditures increased from the prior year.

In addition to allowing for substantial growth in spending, personal income growth has no direct correlation to government services. There is no rational reason to tie spending to the growth in personal income. Rather, there should actually be a negative correlation between the two. If the economy is growing and personal prosperity is rising, Tennesseans will have less need for government services, allowing state spending to decrease rather than escalate.

A Better Solution

A more sensible and fiscally responsible method for calculating the spending limit would be to measure population growth plus inflation. Population changes most significantly influence government spending. If Tennessee becomes more populous, the *number* of people using government services (driving on roads, receiving welfare services, etc.) will therefore likely increase. Such population growth could drive up government spending as a result. Further, inflation also impacts the value of the dollar, therefore affecting government expenditures. For these reasons, basing spending increases or decreases on population trends plus inflation is a truer and more accurate method for calculating the Copeland Cap.

In practice, this calculation method would be more effective at constraining government spending and stabilizing the state budget. Population growth plus inflation has averaged a total of five percent per year as compared to the 6.21 percent growth in personal income.[10] This may seem like a nominal difference, but in sheer dollars it is substantial. If the

Copeland Cap was calculated using population plus inflation at the advent, taxpayers could have saved an astounding $38.4 billion between 1979 and 2013, as reflected in the graphs in Appendices A and B below.

In Appendix A, the blue line represents actual budget growth since the enactment of the Copeland Cap. The red line represents the spending that would have occurred if the state budget grew at exactly the rate of personal income growth, which is on a similar trajectory to actual spending. Finally, the green line represents spending capped at population plus inflation, the proposed calculation outlined in this brief. The gap between the blue (actual spending) and green (proposed spending cap) lines is highlighted in Appendix B. This highlighted gap represents massive taxpayer savings—$38.4 billion—that could have occurred during the same time period. Except for a seven-year period between 1979 and 1985, during which inflation was often in the double digits, the alternative calculation would have produced a smaller annual state budget than the current cap provides, and in most cases, significantly smaller.

While state appropriations grew to $13.7 billion annually with the passage of the 2013-2014 state budget, a more stringent spending limit would have held spending to $10.8 billion, a savings of nearly $3 billion for the current fiscal year alone. A revised calculation would have returned $450 to every man, woman, and child in Tennessee for 2013. Taking into account annual population totals, every single Tennessean could have saved more than $6,300 under the alternative calculation since 1979.[11]

Conclusion

Ultimately, both solutions—raising the threshold required to exceed the cap to demand a supermajority vote and changing the calculation to population growth plus inflation—should be placed in the state Constitution via a constitutional amendment. Due to Tennessee's stringent and lengthy amendment process, the earliest that could take place is 2018. In the meantime, lawmakers can amend the pertinent statute to change the way the Copeland Cap is calculated, moving from a personal income basis to population plus inflation. These two adjustments could significantly bolster Tennessee's ability to maintain a sound fiscal footing for generations to come and return more of taxpayers' hard-earned money back to their pockets.

Given that the legislature has set the wheels in motion for reform, and the appetite among Tennesseans for fiscally responsible government, the General Assembly should strengthen Tennessee's spending limitation laws by enacting these solutions. By reforming Tennessee's Copeland Cap, lawmakers can ensure that Tennessee remains fiscally sound, not just for current taxpayers, but for future generations as well.

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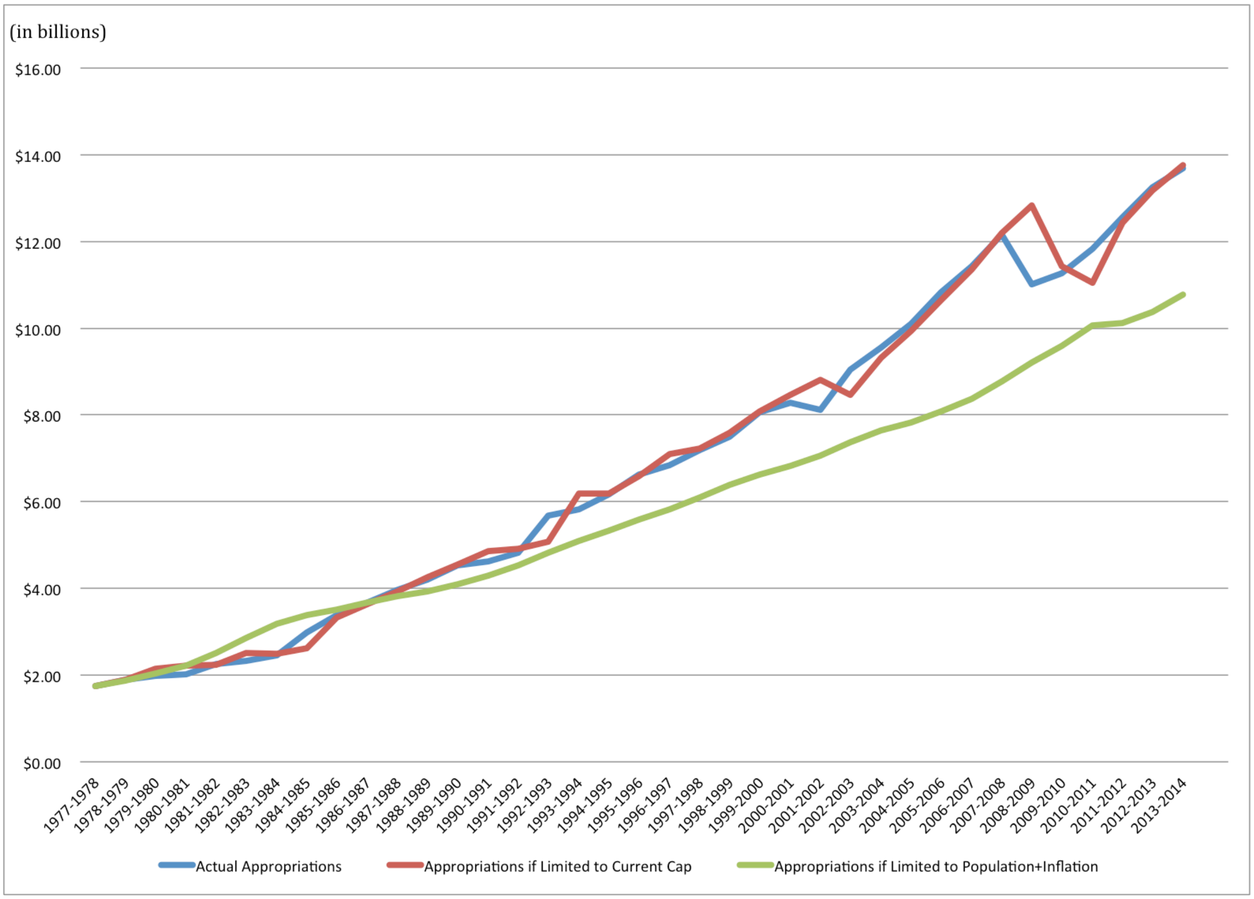
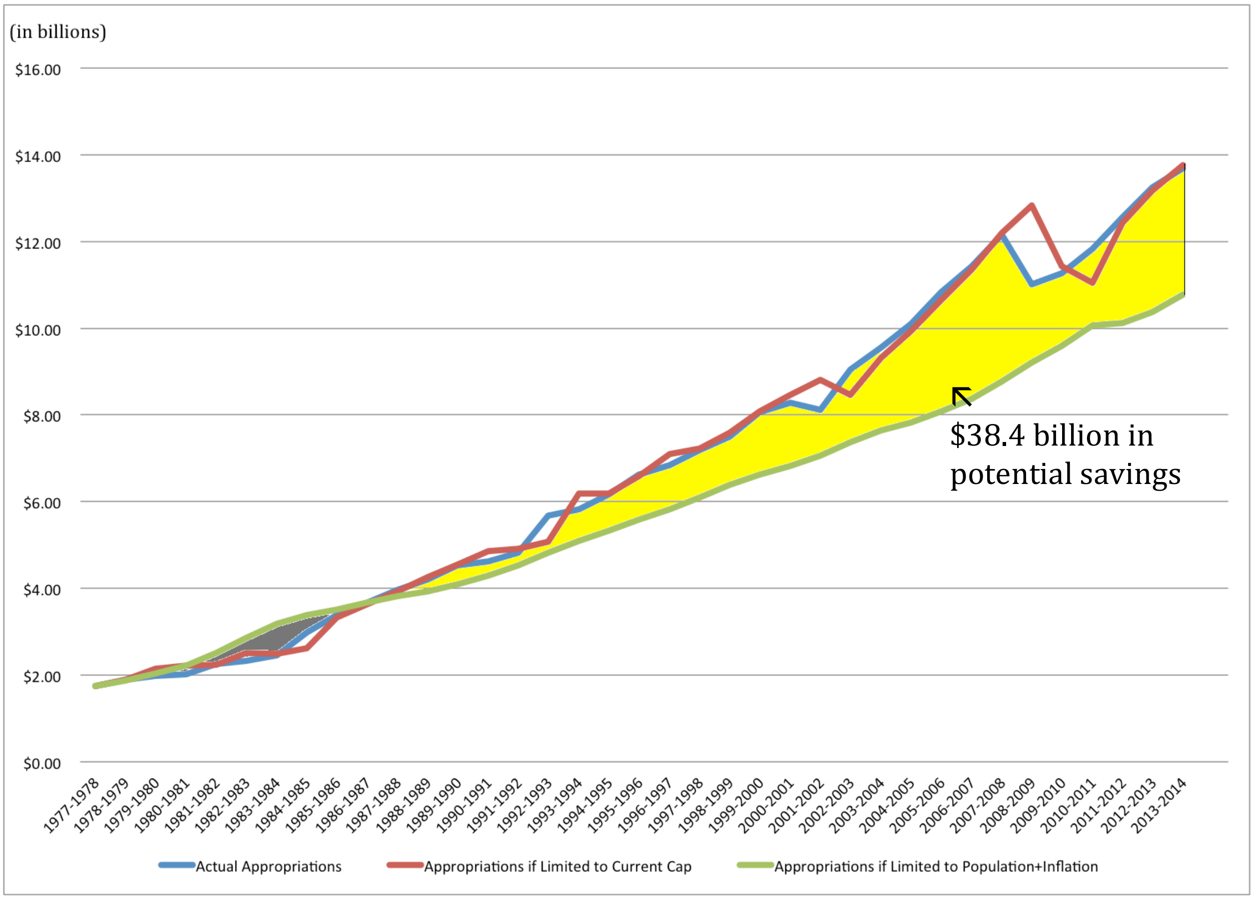
[1] Cory Eucalitto, "State debt more than $37,000 per private worker, $13,000 per capita." State Budget Solutions. Nov. 7, 2012.
[2] "Total State Expenditures Per Capita." Kaiser Family Foundation.
[3] Tenn. Const. Article II, Sec. 24; Tenn. Code Ann. § 9-4-5201.
[4] Public Act 346 (2013).
[5] Analysis compiled from state budgets and public acts related to appropriations between 1979 and 2013. NOTE: Now that the General Assembly calculates the cap in the subsequent session following the passage of the budget, it has not cast a final vote on excess spending for the 2013-2014 fiscal year.
[6] Ibid.
[7] Tenn. Const. Article II, Sec. 24.
[8] Tenn. Code Ann. § 9-4-5201.
[9] U.S. Bureau of Economic Analysis.
[10] U.S. Census Bureau; U.S. Inflation Calculator.
[11] Difference in actual budget appropriation and projected appropriation limited by population growth plus inflation, divided by annual population of Tennessee from 1979 to 2013.

Appendix A. State Budget Growth Comparisons



In the above chart, the blue line represents actual budget growth since the enactment of the Copeland Cap. The red line represents the spending that would have occurred if the state budget grew at exactly the rate of personal income growth. And the green line represents spending capped at population plus inflation.

Appendix B. Potential Savings Resulting from Proposed Calculation



In the above chart, the yellow highlighted area, less the gray highlighted area, represents $38.4 billion in taxpayer savings that could have resulted from a more fiscally responsible Copeland Cap calculation.

About the Author

Justin Owen is the president & CEO of the Beacon Center of Tennessee.

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