



Passing a
Conservative Budget
for Tennessee in 2023

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Introduction

Not a day goes by without new reports of ever-increasing inflation in America. Recent reports by the U.S. Dept. of Labor's Bureau of Labor Statistics have noted that the Consumer Price Index (CPI) measure of price inflation is running at its highest rate in roughly 40 years.¹ High levels of inflation created by the Federal Reserve rob everyone of purchasing power by making our dollars less valuable. Essentially a hidden tax, inflation makes everything from your 4th of July cookout staples to basic necessities like gas and clothing, and even supplies for building homes more expensive. While the causes of inflation can be numerous, one clear contributing factor is too much money printing by the Federal Reserve and massive government spending. Both Republicans and Democrats in Washington have been on a massive spending spree for decades. But between multiple COVID-19 relief-related bills like the CARES Act and the American Rescue Plan Act, federal spending and deficits have reached record highs, thereby giving the Fed a way to inject trillions of newly printed dollars into the economy. Essentially, Washington poured lighter fluid on a market of ever-increasing prices, and we are poorer because of it.

Because Washington seems unlikely to change soon, Tennesseans are looking for relief from state policymakers. Yet what can Tennessee policymakers do? While the focus has been mostly on short-term relief efforts

like sales tax holidays, the best long-term solution is clear: control spending growth. While CPI is a national measure, different regions can have different rates of inflation and cost of living. Take one trip to California with its high spending, taxes, and labor market regulations and you will not only see how little economic freedom you have but also how high the costs of goods and services can vary from region to region.²

Luckily, for several decades Tennessee has been known for its fiscally conservative budgeting. Years of limited spending has helped keep taxes low thereby allowing Tennessee taxpayers to keep hundreds of millions of dollars in their pockets that might otherwise have gone to government bloat. In fact, according to the Tax Foundation, Tennessee residents pay less in state and local taxes than anyone else in the country.³ But sound economic policies and restraining spending are now more important than ever. This is a reason why during good or bad times that Tennessee families practice priority-based budgeting, making tough choices on how to spend their hard-earned dollars. If Tennesseans are having to scrimp and save to deal with higher inflation, state policymakers must also continue to make fiscally conservative choices. This means resisting the temptation of excessive spending and not making it more difficult for Tennessee taxpayers to fund their state government when they can least afford it.

1 Vance Ginn and Megan Henney, "The Ginn Economic Brief: An Insider's Insight on Today's Economy." The Cannon Online. August 12, 2022. <https://thecannononline.com/wp-content/uploads/2022/07/Ginn-Report-U.S.-08-22.pdf>.

2 Dean Stansel, Jose Torra, and Fred McMahon, "Economic Freedom of North America 2021." Fraser Institute. November 16, 2021. <https://www.fraserinstitute.org/studies/economic-freedom-of-north-america-2021>.

3 Janelle Cammenga, "How High Are State and Local Tax Collections in Your State?" Tax Foundation. April 14, 2021. <https://taxfoundation.org/state-local-tax-collections-per-capita-2021/>.

Overview of the Tennessee Conservative Budget

By passing conservative budgets, Tennessee lawmakers can prevent state spending from exceeding the average taxpayer's ability to pay for it. Conservative budgeting will ensure that state government does not drive the cost of living higher and pave the way for returning surplus tax revenues to taxpayers through tax cuts that can be used productively in the Volunteer State's economy. Conservative budgeting also ensures state spending does not grow so large that the state cannot afford its level of spending should a recession occur.

Beacon's Conservative Tennessee Budget (CTB) provides a path toward responsible state spending. The CTB sets a maximum threshold for the state budget based on the average taxpayers' ability to fund it, instead of how much should be appropriated. This threshold is an upper limit on initial appropriations of all funds (total state and federal funds) that increases by no more than population growth plus inflation above initial appropriations of the previous budget.⁴ We use all funds because it represents the full burden of the state government on taxpayers. This also allows appropriators the flexibility of determining how best to allocate resources between legislative priorities that may need more or less funding, as long as total spending

does not exceed the total CTB. If the amount matches this limit, it will essentially freeze real (inflation-adjusted) per-capita appropriations while covering essential government provisions. Research shows that limiting a state's budget to population growth plus inflation helps to stabilize budgets, increases certainty for taxpayers, and promotes economic growth.⁵ The resulting growth and stronger economic climate could then be turned into further state savings and tax cuts for citizens to foster even further prosperity.



⁴ Vance Ginn, "The Responsible American Budget." Texas Public Policy Foundation. May 25, 2021. <https://www.texaspolicy.com/the-responsible-american-budget-bringing-fiscal-sanity-to-the-federal-budget/>.

⁵ John Merrifield and Barry Poulson, "State Fiscal Policies for Budget Stabilization and Economic Growth: A Dynamic Scoring Analysis." Cato Journal, Vol. 34, No.1. 2014. <https://www.cato.org/sites/cato.org/files/serials/files/cato-journal/2014/2/v34n1-3.pdf>.

A Look Back at Past Tennessee Budgets

By looking back to budgets since 2011, we can see Tennessee has been below or met the CTB for all but two years, cumulatively \$480 million under the CTB's full allowance—saving each family of four, on average, a total of \$272 (Figure 1). Because spending and taxes are two

sides of the same coin, these savings have allowed Tennessee legislators to eliminate various taxes like the Hall income tax, death tax, and gift tax, and for the majority of professions originally subject to the professional privilege tax.

Tennessee's Total Budget

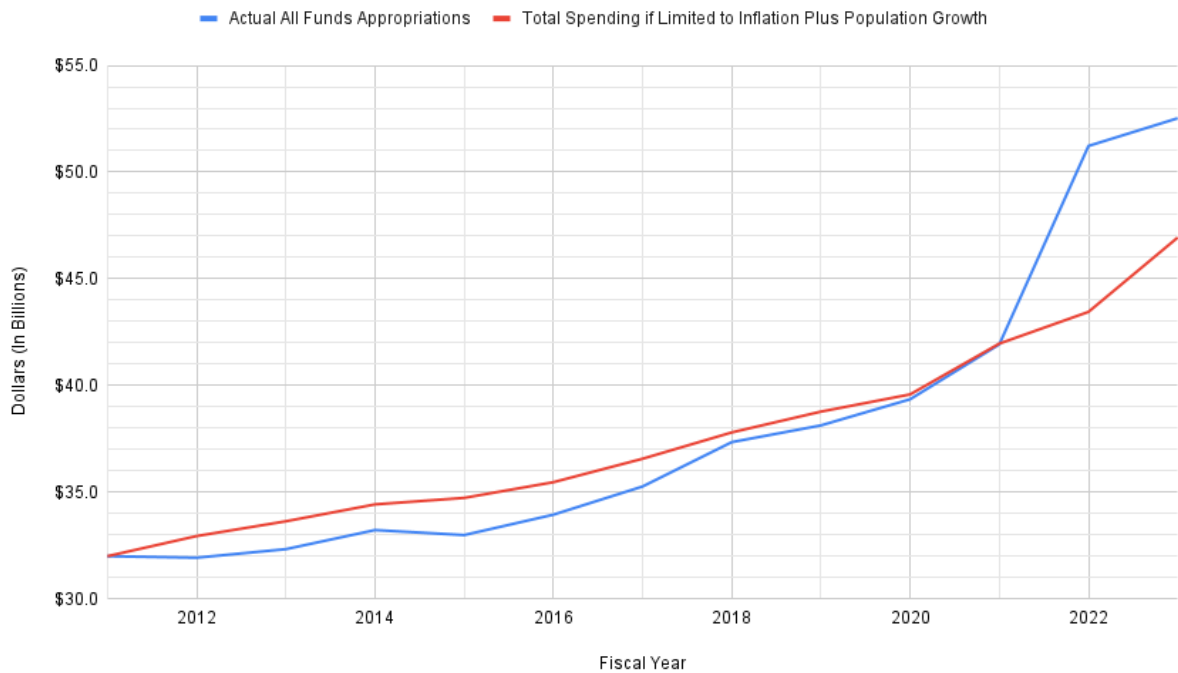


Figure 1: For years until receiving pandemic-related federal funding, Tennessee lawmakers have passed fiscally conservative total budgets, saving Tennessee taxpayers money.

While for most of recent history state spending has become below the threshold, it has broken the CTB threshold in the past two years due to large

amounts of pandemic-related spending, even with higher levels of inflation that create a faster rising CTB limit.

Growth of Appropriations vs. Population Growth Plus Inflation Over Time

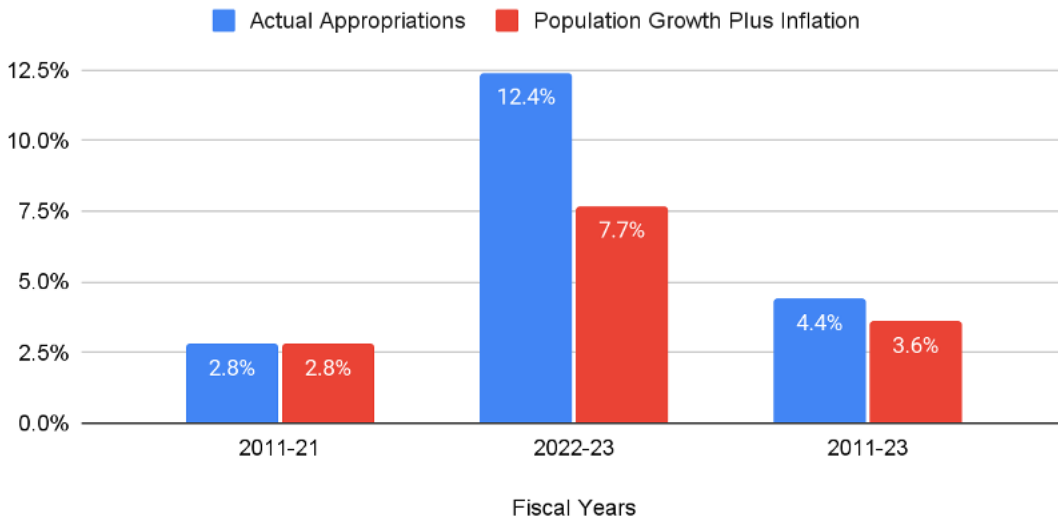


Figure 2: Even with the highest inflation rate in decades, state spending has outpaced population growth plus inflation due to high levels of spending of pandemic-related funds from the federal government.

Calculating the Conservative Tennessee Budget

The CTB growth rate for the fiscal year 2024 can be calculated with the state’s population growth and price inflation over the previous fiscal year. Using this information, we found a growth rate

of population growth plus inflation of 9.6 percent to serve as the maximum appropriations growth limit for fiscal year 24 budget (Table 1).

Population Plus Inflation Calculation

TN Population Growth	US CPI Inflation	Population + Inflation Limit
0.7%	8.9%	9.6%

Table 1: For the upcoming fiscal year, the state government will not exceed the average taxpayers’ ability to pay for the budget if it grows no more than 9.6 percent from last year’s appropriations.

The Conservative TENNESSEE BUDGET

Appropriations for the 2023-2024 Budget should not exceed

\$57.56 BILLION

*in state and federal funds,
excluding investments in
savings and trust funds*

9.6% INCREASE

*from 2022-2023 appropriations
based on population plus
inflation growth*

In our inaugural release of the Conservative Tennessee Budget last year, we excluded any explicit one-time federal COVID-19 pandemic-related federal funds from our calculations. However, the federal government has continued to send relief package after relief package to the states with years to spend the billions of dollars. Determining what federal funds are “one-time COVID funds” has become more of an art than a science. As a result, including all funds going forward will better reflect the nature of state spending and its spending growth. It is important to note that the \$57.56 figure is a ceiling and state policymakers ought to aim to budget well below that number, especially as the massive influx of federal funds begins winding down, which will help “reset the baseline” to more accurately reflect historical trends. It will be essential for legislators to remember that these federal funds will be one-time sources of funding so that they do not use them for ongoing expenses.

Additionally, because savings and tax cuts are not true spending if revenues exceed the CTB amount of \$57.56 billion, deposits into the rainy-day fund, TennCare reserves, or other reservoirs like the Mental Health Fund will not count towards the amount. Likewise, lawmakers could enact further tax reforms with surplus revenues, including but not limited to corporate tax reform or eliminating the rest of the professional privilege tax, without those reforms counting against the spending limit. Another option would be to begin phasing out the business tax, the state’s gross receipts tax. Gross receipts taxes are known to have extremely negative economic effects, and Tennessee is only one of seven states with such a tax, a rather “black eye” on an otherwise competitive economic landscape for the state.⁶

While the total amount of spending still serves as the best number to measure the growth of the state’s budget, due to the previously mentioned temporary

large increase in federal funds, looking at the growth of the appropriations of solely state revenues can provide additional insight into the growth of state government. While the total amount of spending has been at or below population growth plus inflation in every year except the last two when

the amount of federal funds received soared, state funds spending has been mixed. State funds appropriations were at or below appropriations following population growth plus inflation from 2012 to 2017 but above them since then.

Tennessee's State Funds Budget

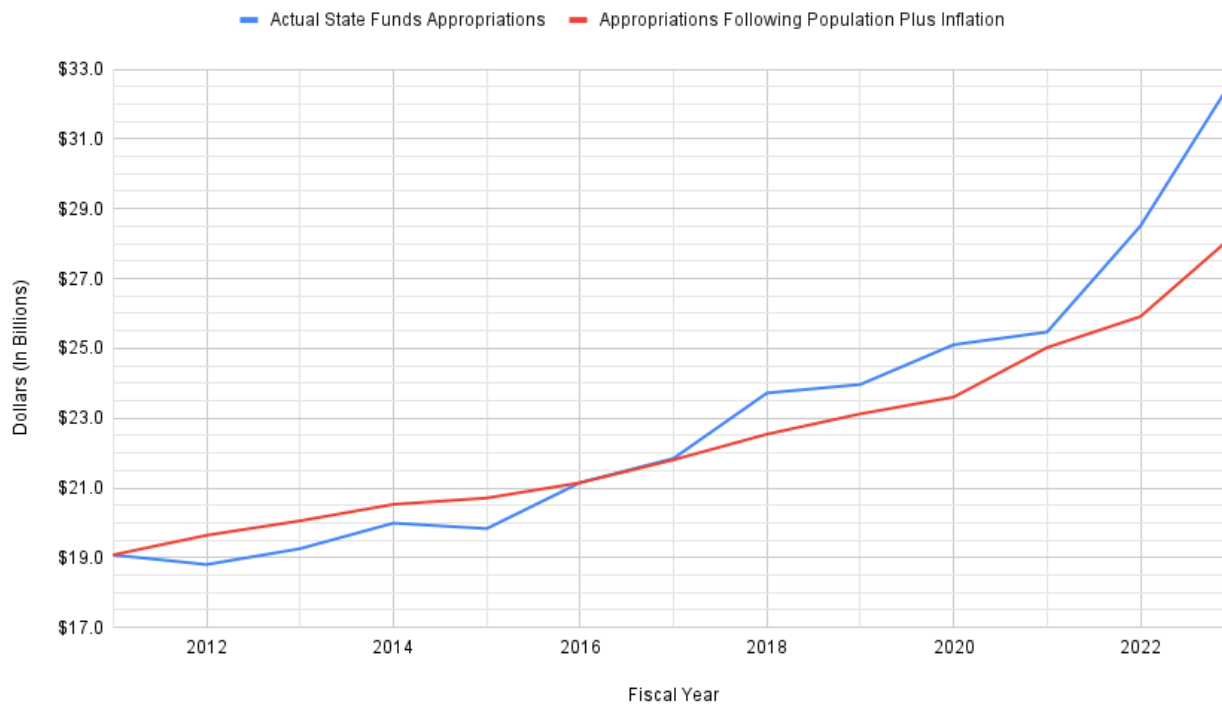


Figure 3: Since 2016, state funds have exceeded population plus inflation growth and should raise concerns for lawmakers, especially while economic conditions are uncertain.

Conclusion

For years, Tennessee leaders have practiced conservative budgeting, keeping increases in state spending below population growth plus inflation for at least a decade until the pandemic. This has saved Tennessee taxpayers hundreds of millions of dollars, allowing for pro-growth tax cuts. The CTB sets a maximum threshold for the General

Assembly at \$57.56 billion for the 2023-2024 budget. By keeping spending below this amount, we can ensure that the burden on Tennessee families to fund the state government will not increase beyond their means and that they have the best opportunity to prosper and live their version of the American dream.



About Beacon

The Beacon Center empowers Tennesseans to reclaim and protect their freedoms, so that they can pursue their version of the American Dream. The Center is an independent, nonprofit, and nonpartisan research organization dedicated to providing expert empirical research and timely free market solutions to public policy issues in Tennessee.

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