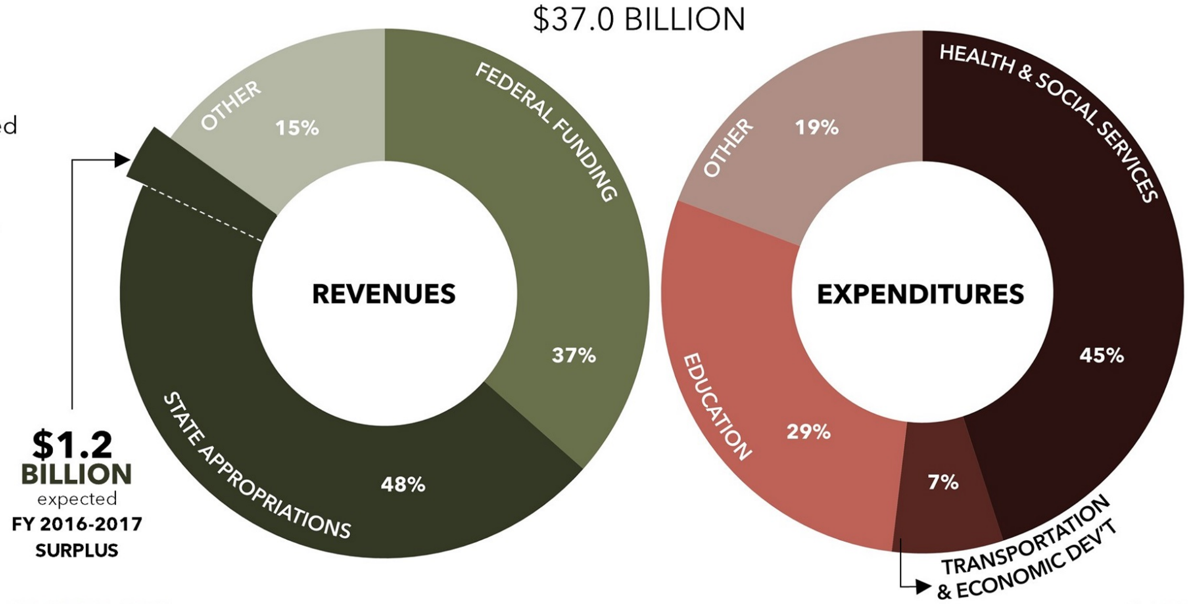
TENNESSEE STATE BUDGET
GOVERNOR'S FY 2017-2018 RECOMMENDATION

TOTAL BUDGET

On January 30, 2017, Governor Bill Haslam released his recommended FY 2017-2018 Tennessee state budget for consideration by the state Legislature.

FY 2017-2018 RECOMMENDED BUDGET
$37.0 BILLION



TOP INVESTMENTS & INCREASES

RECURRING

- **+$300M** for the Highway Fund
- **+$239M** for items like changes to state employee salaries and benefits
- **+$201M** for K-12 education

NON-RECURRING

- **$655M** for capital outlays
- **$110M** for state retiree liabilities
- **$108M** for economic and community development

TOP REDUCTIONS

RECURRING

- **-$20M** from TennCare
- **-$10M** from Strategic Health Care Programs
- **-$3M** from Corrections

NON-RECURRING

- **-$49M** from Strategic Health Care Programs

SAVINGS

26 DAYS

the number of days the state government could function with expected **RAINY DAY FUND** and **TENNCARE RESERVE** balances in 2018

+2 DAYS vs. 2017
-16 DAYS vs 2007

TAX REVENUE GROWTH

+$879 MILLION
estimated FY 2017-2018 revenue growth under current law **vs. budgeted FY 2016-2017 revenues**

+$367 MILLION
estimated FY 2017-2018 revenue growth under current law **vs. revised FY 2016-2017 revenue estimate**

THE IMPROVE ACT

FY 2017-2018 impact

+$396 MILLION
transportation-related taxes & fees

+$279 MILLION
to the state Highway Fund

+$117 MILLION
to cities & counties for transportation projects

-$102 MILLION franchise & excise taxes on manufacturers

-$79 MILLION Hall income tax on investment income

-$56 MILLION sales tax on groceries

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THE BUDGET IN BRIEF

SUMMARY & ANALYSIS OF THE GOVERNOR'S FY 2017-2018 TENNESSEE BUDGET

February 24, 2017

BOTTOM LINE & KEY POLICY QUESTIONS

On January 30, 2017, Governor Bill Haslam released his recommendation for the FY 2017-2018 Budget – along with re-estimates and recommended changes for the FY 2016-2017 Budget. **The Budget recommendation effectively shifts part of the General Fund's robust revenue growth to the Highway Fund by cutting taxes for the General Fund and increasing those for the Highway Fund. The Budget also uses projected revenue growth and spending reductions to fund continued cost increases for state employees, TennCare, and K-12 Education along with new investments for capital improvements.** It is now the job of the Legislature to consider and act on this recommendation.

KEY QUESTION: HOW DOES THE BUDGET ADDRESS THE $1.2 BILLION SURPLUS EXPECTED FOR FY 2016-2017?
The projected General Fund in FY 2016-2017 is driven largely by a $656 million surplus from FY 2015-2016 and $512 million in greater-than-budgeted revenues for FY 2016-2017. The Budget recommends putting some of these funds to work in FY 2016-2017 via a $121 million one-time transfer to the Highway Fund and $67 million in supplemental appropriations.

The result of these updated estimates and recommendations for FY 2016-2017 is a projected surplus of $1.2 billion that becomes available as a non-recurring revenue source in FY 2017-2018. The FY 2017-2018 recommendation includes new non-recurring investments in capital projects, economic and community development projects and incentives, and K-12 education, among others.

KEY QUESTION: HOW DOES THE BUDGET USE NEW REVENUE GROWTH EXPECTED FOR FY 2017-2018?
The Budget estimates an increase of +$879 million in General Fund tax revenues in FY 2017-2018 relative to the expected tax revenues on which the FY 2016-2017 budget was based. This includes both the +$512 million greater-than-expected revenues for FY 2016-2017 and an additional +$367 million over the revised FY 2016-2017 estimates.

Some of these increased General Fund revenues are proposed for reduction via the tax proposals included as part of the Governor's IMPROVE Act. These include reductions to the Franchise & Excise taxes on manufacturers, the Hall Income Tax on investment income, and the sales tax on groceries. The Budget also includes new recurring investments and cost increases related to state employee salary and benefit costs, K-12 Education, TennCare, and Higher Education.

KEY QUESTION: HOW DOES THE BUDGET APPROACH THE BACKLOG OF TRANSPORTATION PROJECTS?
Tennessee has a $6 billion backlog of approved transportation projects and an additional $4.5 billion of projects identified as priorities by the Tennessee Department of Transportation. The Budget proposes addressing this backlog with +$300 million in increased state dollars for the Highway Fund. This increase is made up of expected revenue growth under current law and +$279 million from increases to taxes and fees on fuels, car registrations, and electric and rental cars. These increases are proposed as part of the IMPROVE Act.

RECOMMENDED BUDGET PRIMER READING

Look for the pink boxes for recommended reading from our Tennessee State Budget Primer: A Foundation for Understanding Our State's Public Policies. These readings provide deeper discussions, related themes, and additional context for the Governor's current Budget recommendation.

FY 2016-2017 CHANGES

RECOMMENDED CHANGES TO THE FY 2016-2017 BUDGET SINCE JULY 1, 2016

+$1.4 BILLION
in estimated revenue

+$656 MILLION
from last fiscal year's budget surplus
+$512 MILLION
in unbudgeted revenue growth this fiscal year
-$39 MILLION
in changes to revenue from proposed legislation
+$228 MILLION
in other one-time revenues and balances

+$187 MILLION
in one-time spending

+$67 MILLION
in supplemental appropriations
+$120 MILLION
for a one-time transfer to the Highway Fund

$1.2 BILLION

FY 2016-2017 BUDGET SURPLUS

Source: "Available Funds Fiscal Year 2016-2017" (pA23) from the FY 2017-2018 Tennessee State Budget.

Each year, the Budget not only includes a recommendation for the upcoming fiscal year. It also includes changes to the current fiscal year that reflect new estimates for tax collections and additional spending requests for any emerging needs. Understanding these changes for the current fiscal year (FY 2016-2017) provides context for the recommendations for FY 2017-2018.

KEY FACTS:

- The Budget reflects **$1.4 billion in new revenue** that was not accounted for and budgeted when the current fiscal year began on July 1, 2016. These updated revenue estimates include **surplus from last year**, **better-than-budgeted revenue growth this year**, a handful of **proposed legislative changes** to revenues this year, and other one-time revenues and balances.
- The Budget recommends putting a portion of the unexpected revenues to use through one-time (i.e. non-recurring) supplemental appropriations and a **one-time +$120 million transfer to the Highway Fund**.
- Of the **+$67 million supplemental appropriation** recommendation, a few key recommendations include:
  - +$25 million for Fast Track Infrastructure and Job Training Assistance within the Department of Economic and Community Development
  - +$15 million to fulfill a state match requirement for the Foothills Parkway
  - +$10 million for wildfire suppression costs
- Together, these revisions to FY 2016-2017 leave a **$1.2 billion FY 2016-2017 surplus that becomes available as a source of non-recurring expenditures for FY 2017-2018**.

RECOMMENDED BUDGET PRIMER READING

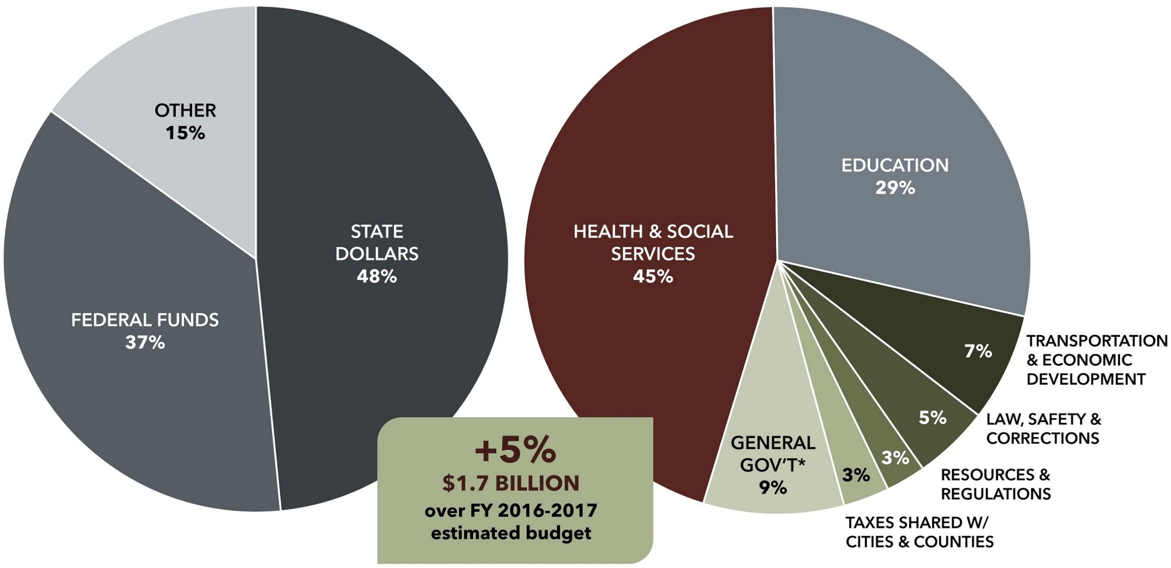
Pages 7-13 "Budget Process" explains the process and key budget concepts like recurring/non-recurring, overappropriations, and the state's balanced budget requirement.

FY 2017-2018 RECOMMENDATION

TOTAL TENNESSEE BUDGET

FY 2017-2018 Recommended Budget

$37.0 Billion



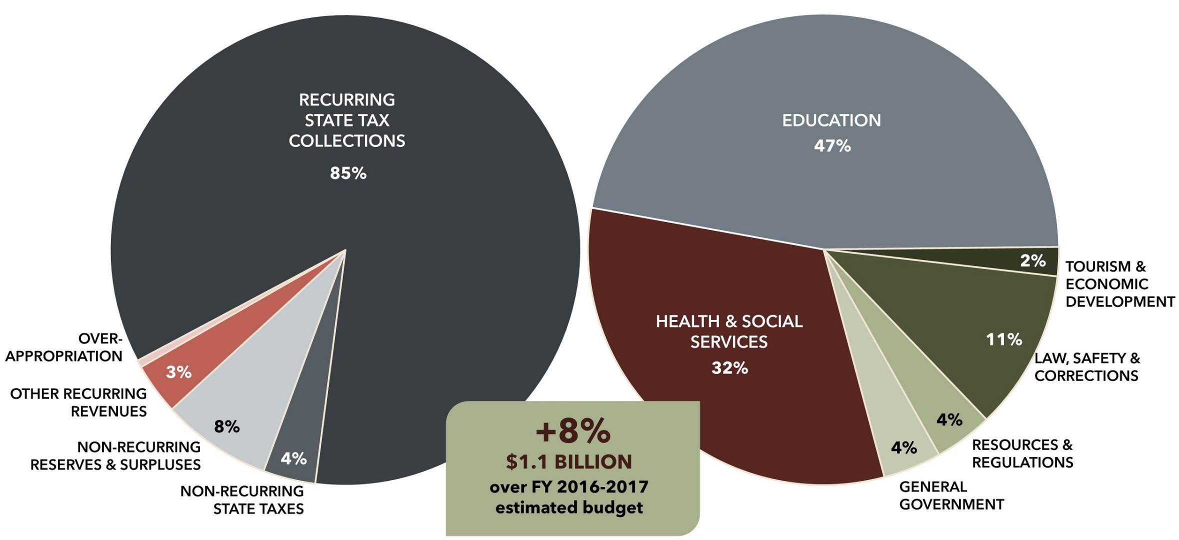
**The General Government category includes Miscellaneous Appropriations, Capital Outlays, and other spending. Page A6 of the Budget distributes these costs to the functional area to which they will be distributed once appropriated.*

Sources: The Sycamore Institute's analysis of "Total State Budget: Comparison of Programs and Revenue Sources" (pA8) and "Comparison of Programs" (ppA17-A22) from the FY 2017-2018 Tennessee State Budget.

GENERAL FUND STATE REVENUES & APPROPRIATIONS

FY 2017-2018 Recommended Budget

$15.4 Billion



Note: Includes the General Fund, Education Fund, the Capital Outlay Program, and the Facilities Revolving Fund – which the Budget refers to together simply as the General Fund. Excludes the Highway Fund, tax collections distributed to cities and counties, and debt service. The revenues analysis excludes negative adjustments for a $132 million rainy day fund deposit, $4 million designated to other funds, and a $0.5 million expected end-of-year balance.

Source: The Sycamore Institute's analysis of "The General Fund Budget" (pA7) and "General Fund and Education Fund Comparison of Appropriation Requirements and State Revenues" (pA11) from the FY 2017-2018 Tennessee State Budget.

The top figure on the previous page shows where the state's revenues are coming from and where they are going for the total state budget. This provides context for **the rest of the discussion and analysis, which focus on the state dollars piece of the total state budget pie**. The bottom figure on the previous page shows the revenue sources and expenditures only for the General Fund state revenues. The General Fund state appropriations represent 86% of total state appropriations spending and include everything except transportation costs, tax collections distributed to cities and counties, and debt service costs. See page 7 for how each of the state's various taxes contribute to the state's total tax collections.

Our Analytic Approach: It is important to remember that the starting point for a fiscal year's budget is the prior fiscal year's recurring base budget. Any non-recurring items essentially reset to zero, since these expenditures and revenues are considered one-time. For this reason, the Budget's own analysis often focuses on how the recommendation is different than the base budget. Many Tennesseans, however, may be more interested in comparisons between the recommendation's bottom line to the prior year's bottom line that includes both recurring and non-recurring items. In our analysis below, we explain how the Budget recommendation balances while providing both points of comparison for non-recurring items. We discuss totals for non-recurring items along with analysis of how those non-recurring totals compare with the FY 2016-2017 non-recurring totals. The first approach shows how the recommendation compares to the base budget while the second shows how the recommendation compares to the bottom line budget that includes both recurring and non-recurring items.

NOTE: The figures presented here balance when considering overappropriations, end-of year balances, and a few small adjustments not itemized here. See pA11 of the Budget Document and p1 of the Budget Overview for a detailed accounting from 2 different perspectives of how the recommended Budget balances.

WHAT ARE THE BUDGET'S RECOMMENDED INVESTMENTS AND COST INCREASES?

General Fund: The Budget includes a number of investments and cost increases in the General Fund. Among these are **+$881 million in recurring cost increases** and a total of **$1.6 billion in non-recurring spending, which is +$365 million more than total non-recurring spending in FY 2016-2017**.

THE BUDGET'S TOP RECURRING INCREASES

- +$239 million for Miscellaneous Appropriations for things like state employee salary increases, retirement contributions, and health insurance rate increases (see ppB20-B24 of the Budget).
- +$201 million for K-12 Education for increased teacher pay and benefits costs, Basic Education Program (BEP) formula growth, and additional English language learners teachers (see ppB82-B85 of the Budget).
- +$201 million for TennCare for expected increases in pharmaceutical spending and health care costs (see ppB140-B143 of the Budget)
- +$132 million for Higher Education primarily for capital maintenance, increased operating costs, and salary increases (see ppB86-B90 of the Budget).

THE BUDGET'S TOP NON-RECURRING EXPENDITURES

- $655 million for the Capital Outlay program, including the Facilities Revolving Fund, which is +$185 million more than in FY 2016-2017.
- $110 million for the state's Other Post-Employment Benefits (OPEB) liability (see ppB21 of the Budget). This is a new non-recurring investment for this purpose.
- $108 million for the Department of Economic and Community Development to help the state broadly and rural areas specifically recruit new business and expand broadband access (see ppB314-B316 of the Budget). This amount is -$2 million less than the non-recurring amounts budgeted for ECD in FY 2016-2017.
- $48 million for K-12 Education to increase funding for current year enrollment growth, upgrade technical education equipment, and support a charter school facilities fund (see ppB82-B85 of the Budget). This amount is +$34 million more than the non-recurring amounts budgeted for K-12 education in FY 2016-2017.

The Budget also includes a **$132 million non-recurring deposit to the Rainy Day Fund**, which is **+$32 million** more than planned for deposit this year (see p11 of this analysis).

Highway Fund: In addition to these increases, the Budget includes a **+$300 million state revenue increase to the Highway Fund** (see pp6-7 of this analysis).

HOW ARE THESE INVESTMENTS AND COSTS FUNDED IN THE BUDGET?

Tennessee's budget must be balanced, which means that any new spending increases must be funded either from new revenues or from cuts to existing programs.

INCREASES TO BUDGETED REVENUES

General Fund: The FY 2017-2018 recommendation **budgets an additional +$1.1 billion in General Fund revenues over the re-estimated FY 2016-2017 Budget**. These budgeted revenues are a mix of both recurring and non-recurring revenues. **This distinction between recurring and non-recurring is important because it limits the kinds of expenses that the revenues can be spent on in FY 2017-2018**.

+$758 million of the budgeted increase is made up of changes to recurring revenues. These funds are available for recurring cost increases or recurring revenue cuts. This increase is primarily comprised of the +$512 million better-than-budgeted revenue growth estimated for FY 2016-2017 (see p2) and an additional +$367 million in revenue growth for FY 2017-2018 (see p8). We would note that the $512 million revenue growth occurred from recurring sources of state revenue, but the Budget classifies it as non-recurring in FY 2016-2017 because the FY 2016-2017 unbudgeted collections become a non-recurring source of revenue in FY 2017-2018 (see below). These revenue increases are partially offset by the Governor's legislative proposals that, together, reduce recurring General Fund taxes by -$208 million.

+$317 million of the budgeted increase comes from changes to budgeted non-recurring revenues, which **total $1.6 billion** in FY 2017-2018. To make balancing the budget easier in the long-term, non-recurring sources of revenue are generally only used for non-recurring costs. The largest source of these non-recurring revenues: $1.2 billion from the expected FY 2016-2017 budget surplus (see p2).

Highway Fund: The Budget includes a total of +$300 million in increased state revenues for the Highway Fund - $279 million of which are obtained from increased state taxes and revenues proposed as part of the Governor's IMPROVE Act (see pp6-7).

BUDGET REDUCTIONS

General Fund: Changes in the revenues available for spending are not the only sources available for new spending or new tax cuts. In addition to the overall General Fund increase, the Budget also makes room for new investments by recommending **-$43 million in recurring base reductions** and **-$49 million in non-recurring reductions**.

THE BUDGET'S TOP 3 RECURRING REDUCTIONS (see p10)

- -$20 million from TennCare related primarily to delivery system reform savings and Intellectual and Development Disabilities waiver utilization (see p25 of Volume 2 of the Budget).
- -$10 million from Strategic Health Care Programs primarily from the use of reserves and lower expected enrollment in the CoverKids program (see p43 of Volume 2 of the Budget).
- -$3 million from Corrections related to the food services budget (see p31 of Volume 2 of the Budget).

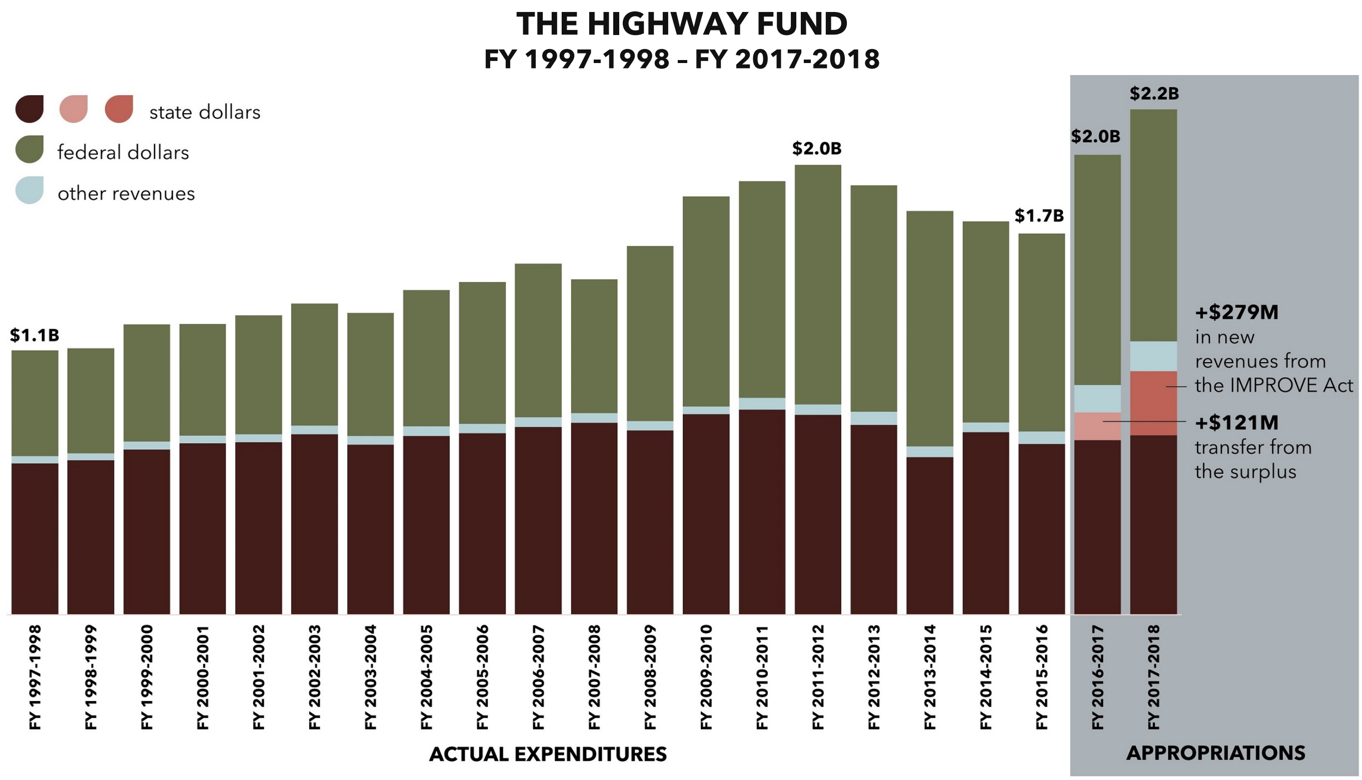
THE BUDGET'S NON-RECURRING REDUCTION

- -$49 million from Strategic Health Care Programs associated with an increase in the federal match rate (see p43 of Volume 2 of the Budget).

OTHER ADJUSTMENTS

In addition to these recommendations, the Budget also includes **-$83 million in recurring preliminary base budget reductions**. These preliminary adjustments are often outside the control of the state's policymakers. For example, the state was informed by the federal government that the state's match rate for TennCare in FY 2017-2018 is lower than for FY 2016-2017. Under the new match rate, Tennessee's appropriations requirements would be about -$49 million less than under the current match rate. These dollars become available for other recurring expenses.

THE HIGHWAY FUND



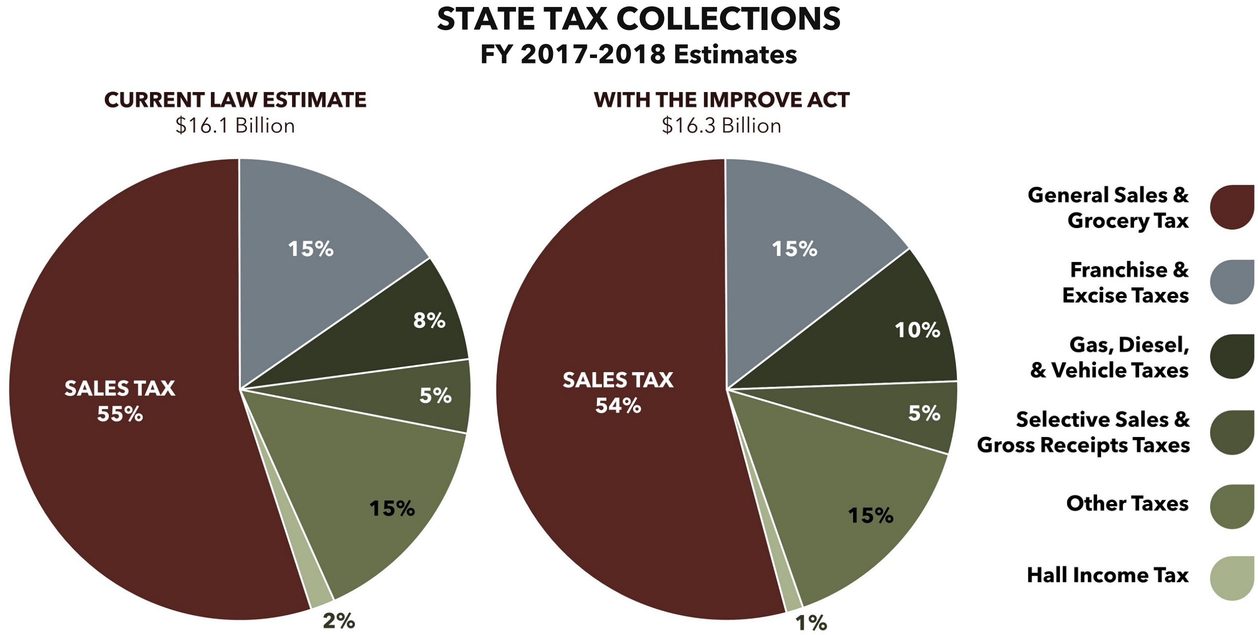
Note: Funds appropriated in one year may be spent and reported as actual expenditures in a future year. For this reason the FY 2016-2017 and FY 2017-2018 appropriations estimates are not considered comparable to the FY 1997-1998 – FY 2015-2016 amounts. Includes a total of $596M in one-time federal funding provided by the Recovery Act that was spent on transportation between FY 2008-2009 and FY 2013-2014.
Sources: The Sycamore Institute's analysis of "Total State Budget: Comparison of Programs and Revenue Sources" from the FYs 1996-1997 through 2017-2018 Budgets, Recovery Act funding information in the FYs 2012-2013 through 2015-2016 Budgets, and the 2009 Tennessee Comprehensive Annual Financial Report.

One of the key pieces of the Budget is the inclusion of the Governor's **Improving Manufacturing, Public Roads and Opportunities for a Vibrant Economy (IMPROVE) Act**, which aims to increase funding for transportation projects.

KEY FACTS:

- As part of its recommended changes to the current year, the Budget includes a **one-time $121 million transfer from the General Fund to the Highway Fund** in FY 2016-2017. These funds are available because of greater-than-expected General Fund revenue collections.
- The IMPROVE Act proposes boosting transportation funding in FY 2017-2018 and beyond **by increasing the revenue sources for the Highway Fund**. These revenue sources include taxes and fees on gas, diesel, motor vehicle registrations, electric cars, and rental vehicles.
- The IMPROVE Act would result in revenue increases to the **Highway Fund** that total an estimated **+$279 million** in FY 2017-2018.
- Additionally, these increased revenues would increase the amounts shared with **cities and counties** for transportation projects by an estimated **+$117 million**.
- The proposal includes indexing some of these taxes to inflation, which means that these amounts would grow over time.
- In FY 2014-2015, federal dollars made up 51% of Tennessee's Highway Fund – the 7th highest proportion in the country.[1]
- The appropriations estimates for FY 2016-2017 and FY 2017-2018 are not considered comparable to other years because funds appropriated in one year may be spent and reported as actual expenditures in a future year.
- See our Tennessee Highway Fund Fact Sheet for additional information and context.

STATE TAX SOURCES



Source: The Sycamore Institute's analysis of "Comparison Statement of State Revenues" (pA64) from the FY 2017-2018 Tennessee State Budget and slide 2 from the FY 2018 Recommended Budget presentation by the TN Department of Finance and Administration (LINK).

The figure above displays the distribution of Tennessee's FY 2017-2018 state tax collections both with and without the IMPROVE Act. It includes all taxes collected by the state – including those shared with cities and counties.

KEY FACTS:

- The IMPROVE Act (see p6) pairs Highway Fund revenue increases with reductions to revenue sources for the General Fund – which funds nearly all the non-transportation activities of the state. The impacted revenue sources include the sales tax on groceries, the franchise and excise taxes on manufacturers, and the Hall Income Tax on investment income. Most of these Highway and General Fund taxes are also shared with cities and counties.

IMPROVE ACT REVENUE PROPOSALS

(total FY 2017-2018 Impact)

TAX REDUCTIONS		TAX INCREASES	
-$102.1M	Modify the formula for Franchise & Excise Taxes on manufacturing businesses to account for only in-state sales (versus a mix of in-state sales, property, and payroll).	+$395.7M	Increase taxes and fees on gas, diesel, motor vehicle registrations, rental cars, and electric cars, including: +$0.07/gallon on gas +$0.12/gallon on diesel +$5/year, on average, for car registrations +3% charge on rental cars
-$78.8M	Reduce the Hall Income Tax rate on investment income from 5% to 3.5%.		
-$56.4M	Reduce the Sales Tax rate on groceries from 5% to 4.5%.		

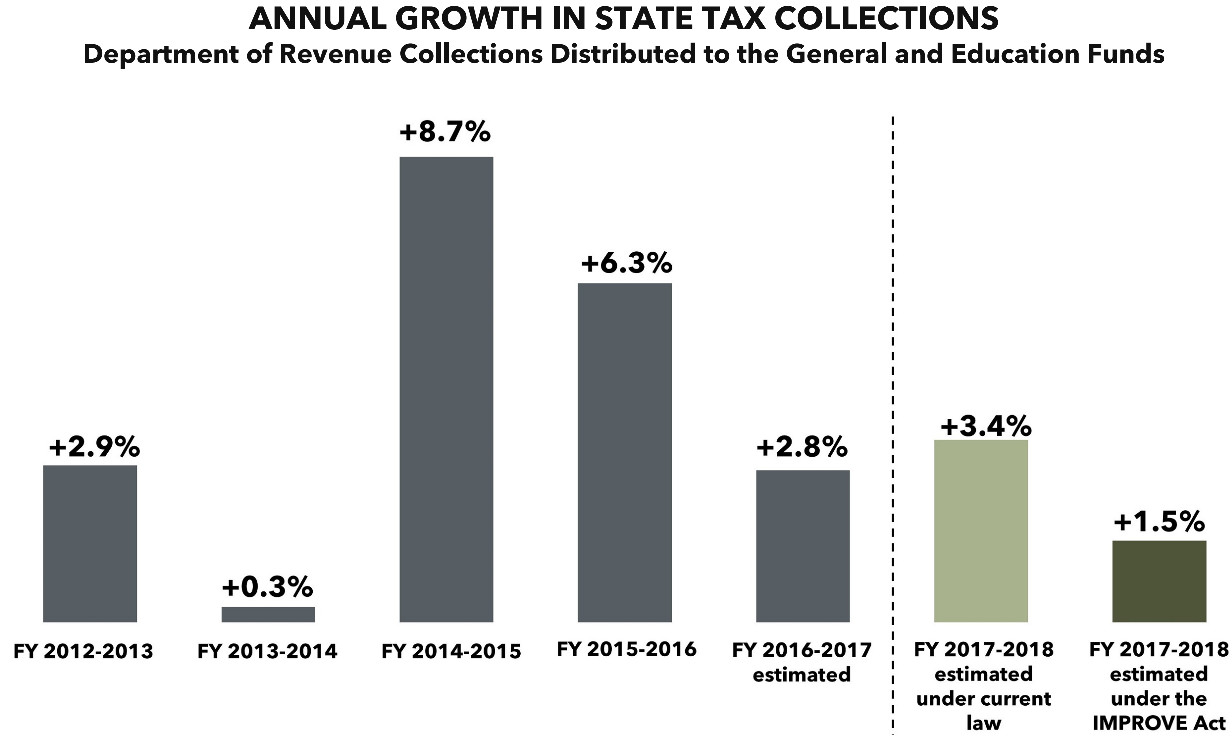
Source: Slide 2 from the FY 2018 Recommended Budget presentation by the TN Department of Finance and Administration. LINK

- The Budget also includes estimates of the tax collections under current law without the changes proposed in the IMPROVE Act (see pA63 of the Budget).
- The Budget's recommended levels of spending, however, reflect the revenue changes proposed in the IMPROVE Act. Compared to revenue projections under current law, the Budget's spending levels reflect fewer revenues available for General Fund expenses and greater revenues for Highway Fund expenses.

RECOMMENDED BUDGET PRIMER READING

Pages 22-27 "Digging Deeper: State Taxes" provides an overview of and context for Tennessee's overall tax structure.

STATE TAX GROWTH



Note: The Budget cites growth estimates for Department of Revenue Collections that are recurring, deposited in the General and Education Funds, and before inter-fund reallocations; however, the level of detail provided in the Budget tables used for this analysis does not allow us to recreate these precise estimates comparably across the years displayed.
Source: The Sycamore Institute's analysis of "Distribution of Actual Revenue by Fund" (pA65) from the FYs 2014-2015 through 2017-2018 State Budgets, "Distribution of Revised Estimated Revenue by Fund" (pA66) and "Distribution of Estimated Revenue by Fund" (pA67) of the FY 2017-20018 Budget, and slide 2 from the FY 2018 Recommended Budget presentation by the TN Department of Finance and Administration.

The figure above shows the Budget's estimates of how state tax collections for the General Fund are expected to grow both with and without the IMPROVE Act in FY 2017-2018. Recent years' annual growth in these collections also appear alongside these estimates.

KEY FACTS:

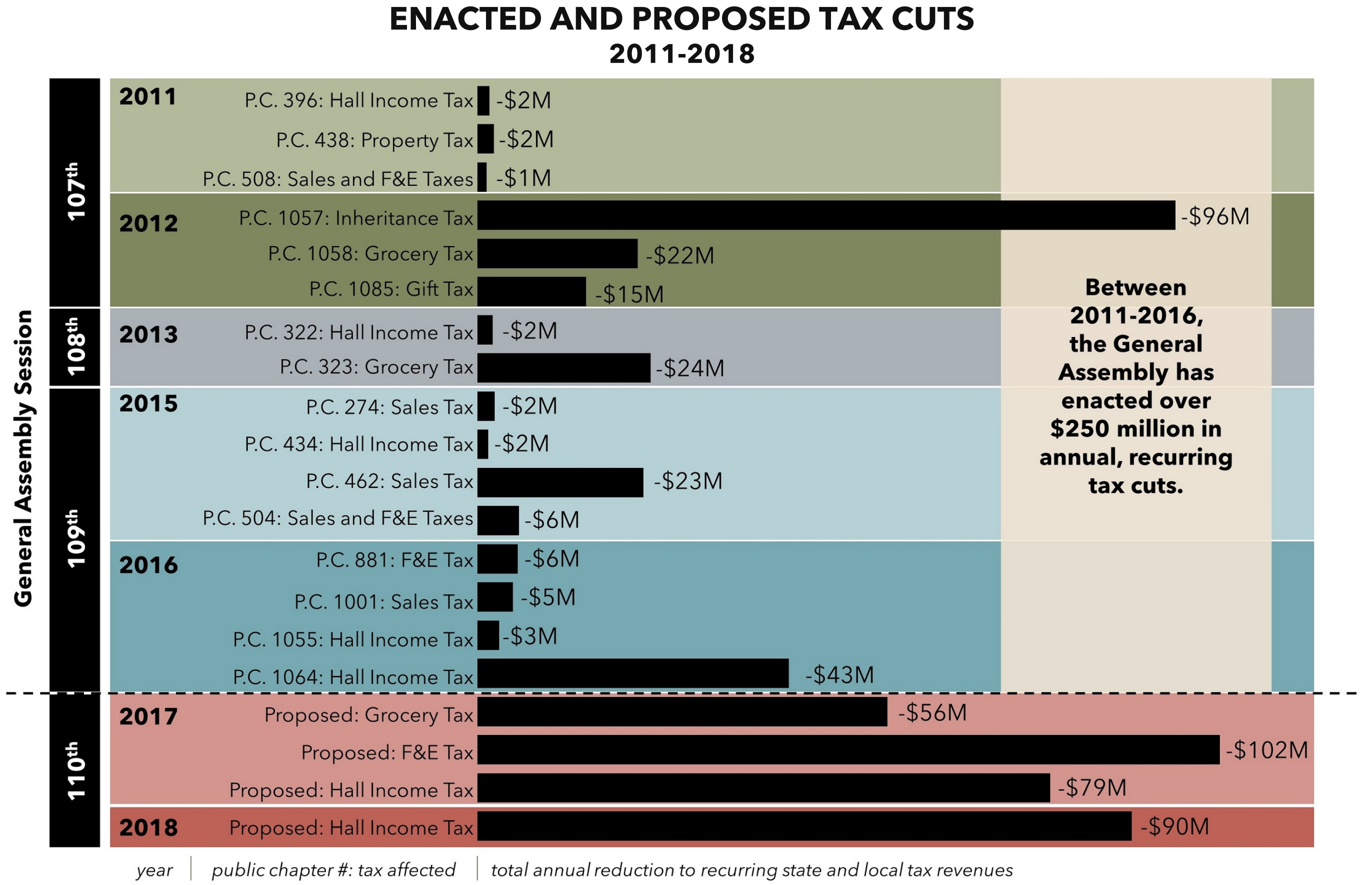
- State taxes dedicated to the General Fund pay for nearly all of the non-transportation services and activities supported by Tennessee.
- The recent budget surpluses have been the result of **unexpectedly large annual growth in these collections**.
- As shown above, the Budget estimates that Department of Revenue collections distributed to the General and Education Funds will increase by **+3.4% or +$393 million in FY 2017-2018**. The recurring portion of these tax collections are expected to grow by +3.17% or +$367 million.
- The Budget proposes forgoing some of this expected growth by reducing General Fund taxes as proposed in the IMPROVE Act (see p7).

RECOMMENDED BUDGET PRIMER READING

Page 8 "The Budget Process: Budget Formulation – Planning and Estimation" summarizes how the Governor goes about estimating tax collections for the Budget.

Page 10 "How Are We Doing? Revenue Estimation" discusses the implications of revenue estimation under a balanced budget, just how hard it is to do well, and how estimates have stacked up against actuals in recent years.

STATE TAX CUTS



Note: Includes all enacted legislation for which the Cumulative Fiscal Note estimated a combined decrease of at least $1 million to state and local revenues attributable to tax changes.
Sources: The Sycamore Institute's analysis of the 2011-2016 Cumulative Fiscal Notes from the TN General Assembly's Fiscal Review Committee and the FY 2018 Recommended Budget presentation by the TN Department of Finance and Administration.

Over the last several years, state policymakers have prioritized cutting the tax load for Tennesseans and businesses operating in Tennessee. The figure above shows all of the tax cuts enacted in the last 3 sessions of the General Assembly alongside the tax cut proposals in the current Budget. The numbers displayed represent the estimated combined annual, recurring impact on state and local revenues.

KEY FACTS:

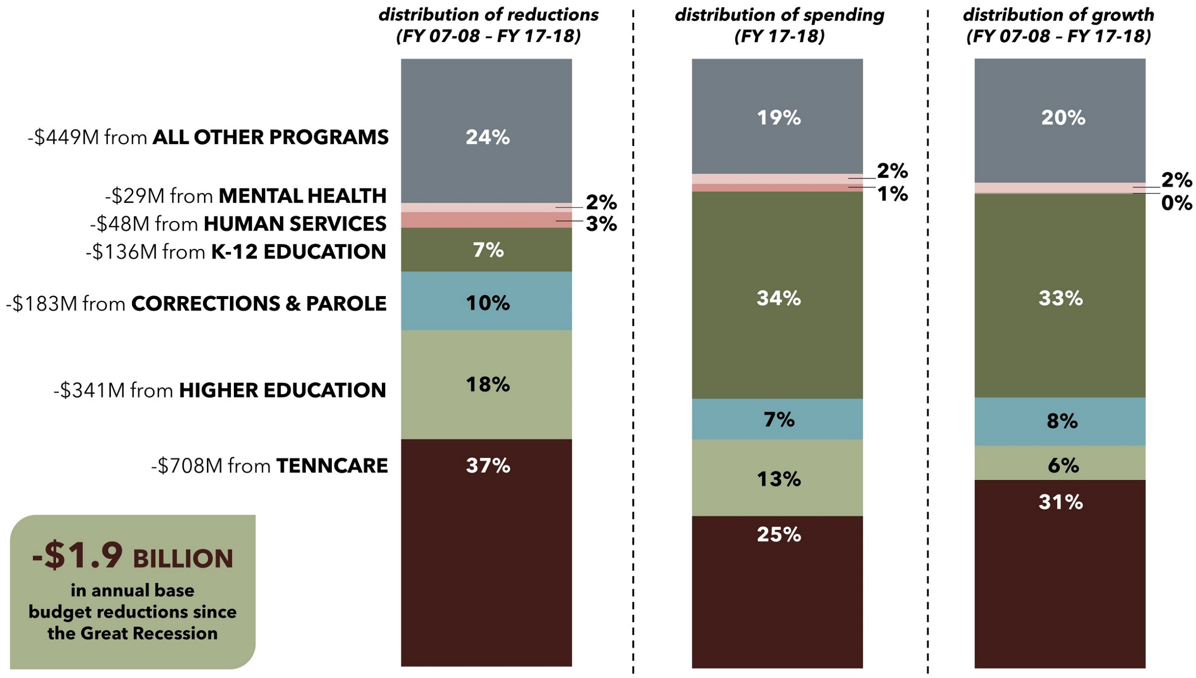
- Between 2011-2016, the General Assembly and Governor have enacted over $250 million in annual, recurring tax cuts, including:
  - o -$111 million from **repealing the Inheritance and Gift Taxes**
  - o -$51 million in **cuts to the Hall Income Tax**
  - o -$46 million in **cuts to the Sales Tax on Groceries**
- As part of the IMPROVE Act package, the FY 2017-2018 Budget proposes the following additional cuts:
  - o -$169 million from accelerating the **phase-out of the Hall Income Tax** over the next 2 years
  - o -$102 million from **restructuring the Franchise & Excise (F&E) Taxes** on manufacturers
  - o -$56 million from **reducing the Grocery Tax** from 5% to 4.5%
- If enacted, total tax cuts between 2011 and 2018 would total **$580 million in annual, recurring reductions**.

RECOMMENDED BUDGET PRIMER READING

Pages 22-27 "Digging Deeper: State Taxes" provides an overview of and context for Tennessee's overall tax structure.

BASE BUDGET REDUCTIONS

RECURRING BASE BUDGET REDUCTIONS SINCE THE GREAT RECESSION
vs. ALLOCATION OF STATE REVENUE SPENDING



Note: Includes only General Fund reductions and appropriations. Excludes any recurring reductions which were restored in later budget years and preliminary base budget reductions.
Sources: The Sycamore Institute's analysis of "6-Year Recurring Base Reduction Summary – State Appropriations FYs 2009 through 2013 Recommended" (p59) of the FY 2013-2014 Tennessee State Budget: Volume 2 Base Budget Reduction, "Seven-Year Recurring Base Reduction Summary – State Appropriations FYs 2012 through 2018 Recommended" (p9) of the FY 2017-2018 Tennessee State Budget: Volume 2 Base Budget Reductions, and "Comparison of Programs" (ppA17-A22) from the FY 2017-2018 Tennessee State Budget.

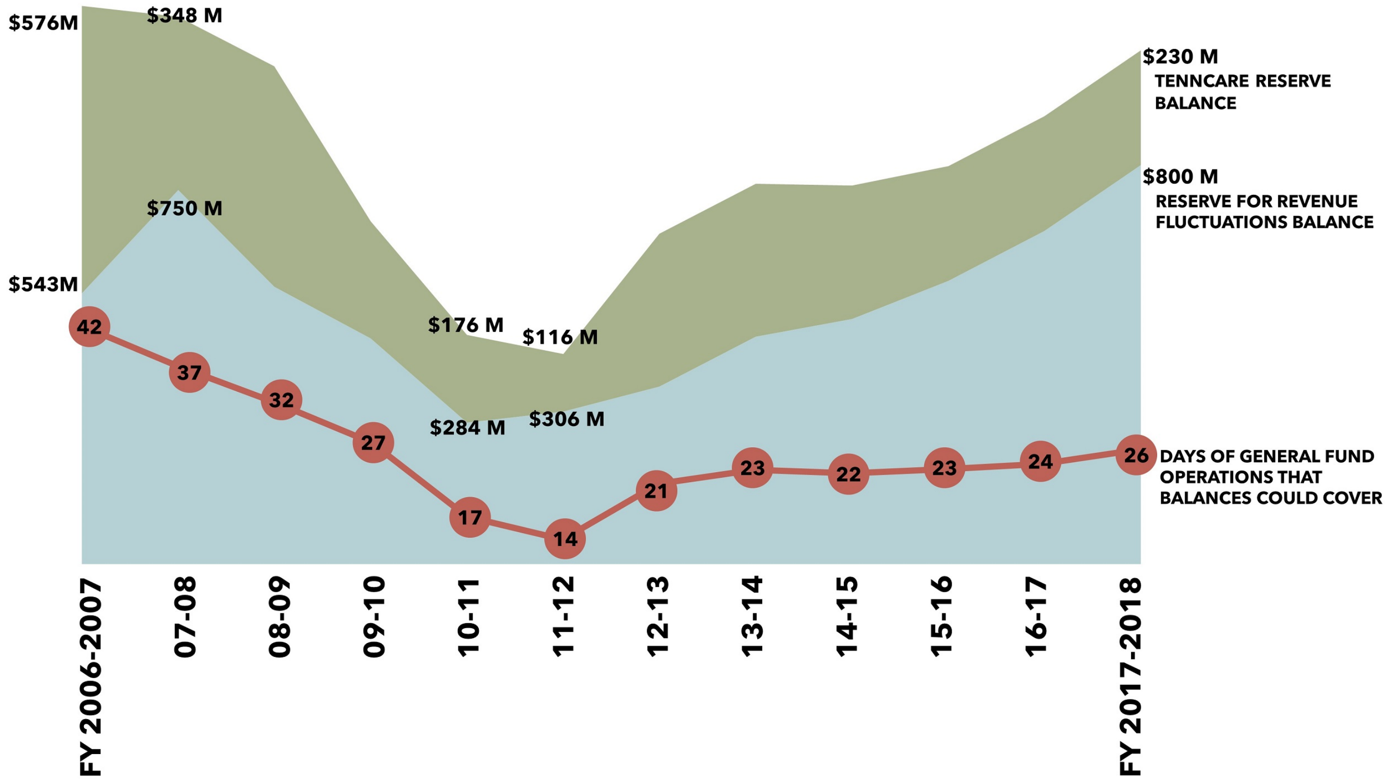
Over the last 10 years, state policymakers have also prioritized cutting the state's spending liabilities to respond to revenue shortfalls during the Great Recession (2007-2008) and, later, to offset tax cuts. These **long-term savings are known as recurring base budget reductions**. To provide context for the recommendations in the FY 2017-2018 Budget, the figure above shows the annual impact of reductions to the General Fund recurring base budget since the Great Recession began in FY 2007-2008.

KEY FACTS:

- The recurring base budget represents expenses that the state government expects to incur year after year and serves as the starting point for each year's budget decisions. Reductions to the recurring base budget decrease the state's long-term annual spending.
- Tennessee has enacted **-$1.9 billion in recurring base budget reductions since the Great Recession**.
- The FY 2017-2018 Budget recommends a total of **-$43 million in new recurring base budget reductions**. The top 3 reductions include:
    - **-$20 million from the TennCare program**, including -$5 million from payment and delivery system reform savings, -$4 million from lower than expected utilization in the Intellectual and Development Disabilities waiver, and -$2 million from changing TennCare's preferred drug for treating opioid addiction
    - **-$10 million from Strategic Health Care Programs** primarily from the use of reserves and lower expected enrollment in the CoverKids program, which provides health coverage to children in families with incomes under 150% of the federal poverty level
    - **-$3 million from Corrections** related to the food services budget
- The Budget recommendation also includes **+$42 million in TennCare to restore a prior year's recurring reduction**. This restoration is reflected in the figure above.

RAINY DAY FUND

RAINY DAY FUND RESOURCES



Sources: The Sycamore Institute's analysis of the FY 2008-2009 through 2017-2018 Tennessee State Budgets.

Economic downturns can create higher-than-usual needs for state programs and services with fewer-than-usual resources to fund them. The state's balances in the Reserve for Revenue Fluctuations and the TennCare Reserve represent Tennessee's ability to respond to an economic downturn (see Recommended Budget Primer Reading below).

KEY FACTS:

- The Budget recommends a **$132 million deposit** to the Reserve for Revenue Fluctuations in FY 2017-2018. This would bring the Reserve for Revenue Fluctuations balance to $800 million – the highest level in the state's history.
- The Budget recommends **a combined balance of $1.0 billion in the Reserve for Revenue Fluctuations and TennCare Reserve**. This amount is about $89 million less than what the state had on hand in both reserves in FY 2006-2007 just prior to the Great Recession of 2007-2010.
- The combined reserve balances alone could cover state-funded General Fund operations at recommended Budget funding levels for about **26 days**.
- State law sets a target balance for the Reserve for Revenue Fluctuations of 8% of General Fund revenues. The FY 2017-2018 recommended balance represents 7% of estimated FY 2017-2018 General Fund revenues under current law – falling **about $84 million short of the 8% target**.
- According to a recent fiscal survey of the states, Tennessee's expected reserve balances at the end of FY 2016-2017 rank 33rd as a percent of state expenditures.

RECOMMENDED BUDGET PRIMER READING

Pages 30-32 "Digging Deeper: Deficits & Surpluses – Cyclical Deficits" summarizes Tennessee's rules for the Reserve for Revenue Fluctuations, rainy day fund best practices, and the trade-offs involved in the state's decisions about stowing away funds for a rainy day.

PARTING WORDS

The Governor's FY 2017-2018 Budget recommendation effectively shifts part of the General Fund's robust revenue growth to the Highway Fund by cutting taxes for the General Fund and increasing those for the Highway Fund. The Budget also uses projected revenue growth and spending reductions to fund continued cost increases for state employees, TennCare, and K-12 Education along with new investments for capital improvements. It is now the job of the Legislature to consider and act on this recommendation – considering the larger historical context and the trade-offs that each of these decisions represent.

SOURCES CITED

[1] National Association of State Budget Officers, "State Expenditure Report FY 2014-2016," November 2016. [Online]. LINK

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