STATE OF TENNESSEE
OFFICE OF THE ATTORNEY GENERAL

April 2, 2015

Opinion No. 15-30

Authority of State to Withhold State-Shared Revenue from Municipality

Question

Can the State of Tennessee lawfully and/or constitutionally withhold from a municipality state-shared revenue for an area that was lawfully annexed by the municipality between the operative dates set forth in SB 121?

Opinion

Yes. The General Assembly has the authority to change the portion of state-shared revenue that it allocates to a municipality both retroactively and prospectively.

ANALYSIS

Senate Bill 121 proposes legislation that, if enacted, would reduce the State's distribution of state-shared revenue to municipalities for annexations by ordinance that occurred within a specified timeframe. Specifically, SB 121 provides that

> [i]f a municipality extended its corporate limits by means of annexation by ordinance between April 15, 2013, and May 15, 2015, or if an annexation by ordinance became operative or effective during that time, then the state shall reduce the state-shared revenue that would otherwise be distributed to the municipality in an amount equal to the increase in property tax revenue that the municipality receives from the territory annexed by ordinance.

Senate Bill 121 addresses the period between April 15, 2013, and May 15, 2015. The General Assembly previously imposed a moratorium on most annexations by ordinance during this period, subject to certain exceptions. Tenn. Code Ann. § 6-51-122. For annexations by ordinance that were permitted during that time period, SB 121 would change the distribution of state-shared revenue generated from the annexed area. Specifically, SB 121 would reduce the municipality's state-shared revenue by an amount equal to the increase in property tax revenue that the municipality received from the annexed territory.

As a general rule, neither the Contract Clause of the federal Constitution nor its Tennessee counterpart applies to relations between a municipality and its creating state.[1] *See generally* Tenn. Att'y Gen. Op. 07-51 (Apr. 16, 2007) (citing, *inter alia*, *Hunter v. Pittsburg*, 207 U.S. 161 (1907); *First Util. Dist. v. Clark*, 834 S.W.2d 283 (Tenn. 1992); *Cunningham v. Broadbent*, 177 Tenn. 202, 147 S.W.2d 408 (Tenn. 1941)). "[L]ocal governments are creatures of the state and possess no more authority than has been conferred upon them by the General Assembly." *Southern Constructors, Inc. v. Loudon County Bd. of Educ.*, 58 S.W.3d 706, 714 n.9 (Tenn. 2001). "[P]olitical power conferred by the Legislature upon a municipality cannot become a vested right as against its creator." *Smiddy v. City of Memphis*, 140 Tenn. 97, 102, 203 S.W. 512, 513 (1918). As a "creature of the State," a municipality can acquire no vested rights in the legislative enactments that benefit it. *Metropolitan Dev. & Hous. Agency v. South Cent. Bell Tel. Co.*, 562 S.W.2d 438, 443 (Tenn. Ct. App. 1977).

In *Cunningham v. Broadbent*, 177 Tenn. 202, 147 S.W.2d 408 (1941), for example, the General Assembly enacted legislation reducing the statutory interest rate paid by the State to counties on highway reimbursement bonds. Dickson County and other plaintiffs attempted to sue state officials, contending that the legislation impaired their vested contract rights in violation of Section 20, Article 1, of the Tennessee Constitution, and Section 10, Article 1, of the United States Constitution. *Id.* at 205, 147 S.W.2d at 409. In rejecting Dickson County's claims of impairment, the Court reasoned,

> first, that no contractual relationship exists between the State and the County by virtue of these enactments, and, second, that if a contract was created thereby, the County being merely a political subdivision of the State, such contract is not protected by the State or Federal Constitutions from alteration or revocation. In disposing of this question the learned Chancellor very concisely and forcefully said: "The County is a subdivision and arm of the State, and the parties were dealing with governmental purposes and objects. Neither the Constitution of Tennessee, nor of the United States, imposes any restraint upon legislation affecting the contractual relations between the State and its political subdivisions, entered into in their governmental capacities and dealing with governmental functions. In such functions the County has no rights which the Legislature may not subsequently modify or abrogate."

Id. at 207, 147 S.W.2d at 410.

In accordance with these authorities, the General Assembly has the power, at any time, to alter the method in which it distributes state-shared revenue to the cities and counties of this State. This principle is broad enough to allow the legislature to change, and require reimbursement for, funds that have previously been distributed under a different formula. Neither the Tennessee nor

[1]Article I, Section 20, of the Tennessee Constitution states "[t]hat no retrospective law, or law impairing the obligations of contracts, shall be made." Article I, Section 10, of the United States Constitution similarly provides that "[n]o state shall . . . pass any law impairing the obligation of contracts." The Tennessee Supreme Court has held that the meaning of these provisions is identical. *First Util. Dist. v. Clark*, 834 S.W.2d 283, 287 (Tenn. 1992).

the United States Constitution imposes any restraint upon legislation affecting the relations between the state and its political subdivisions. As against the state, a municipality cannot acquire any vested right to continue receiving state-shared revenue under any particular formula or at any previously-established rate. The General Assembly remains free to enact legislation amending this distribution scheme as it sees fit.

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