Matthew D. Mitchell, Jonathan Riches, Veronica Thorson, and Anne Philpot.

"Anti-Aid Provisions in State Constitutions"

Abstract

The constitution of nearly every state in the union contains a provision that, on plain reading, makes targeted corporate subsidies illegal. In this chapter, we review the history and effect of these constitutional anti-aid provisions. While anti-aid provisions may be able to limit the size and scope of subsidies, not all are effective. These provisions must be renewed and strengthened from time to time as they are constantly tested by special interests and have been weakened over time. We conclude with suggestions for how to strengthen these provisions.

I. Introduction

Policymakers are keenly interested in promoting economic growth, and targeted economic development incentives are an especially popular strategy.[1] These selective privileges are offered to particular firms or industries and can include targeted tax relief, targeted regulatory relief, cash subsidies, loans and loan guarantees, in-kind donations of land and other valuable goods and services, or some combination of the above.

By one estimate, states and localities spend about $95 billion per year on targeted economic development subsidies.[2] By another, as a share of industry contributions to GDP, incentives have tripled since 1990.[3]

Unfortunately, the economic case for targeted subsidies is rather weak.[4] Theoreticlly, a subsidy might boost net economic development in a region if the government manages to subsidize firms with positive externalities, using revenue derived from taxes on activities without

---

[1] This is not the only strategy. Another tactic is to create an environment that is conducive to growth by, for example, ensuring some degree of economic freedom.

[2] There have been various estimates of annual state and local spending on targeted economic development subsidies (Thomas (2011), Story (2012), Bartik (2017), Thomas (2019), Slattery and Zidar (2020). Among these, the most comprehensive estimate is Thomas (2011). Adjusting for inflation, it is equivalent to $95 billion in 2020 dollars. Cailin Slattery and Owen Zidar, "Evaluating State and Local Business Tax Incentives," Journal of Economic Perspectives 34, no. 2 (2020): 90–118; Kenneth Thomas, Investment Incentives and the Global Competition for Capital (London: Palgrave Macmillan, 2011); Timothy J. Bartik, A New Panel Database on Business Incentives for Economic Development Offered by State and Local Governments in the United States (Kalamazoo, MI: W.E. Upjohn Institute for Employment Research, February 2017); Kenneth Thomas, "The State of State and Local Subsidies to Business" (Mercatus Policy Brief, Mercatus Center at George Mason University, Arlington, VA, October 2019); Louise Story, "As Companies Seek Tax Deals, Governments Pay High Price," New York Times, December 1, 2012.

[3] Bartik, "New Panel Database," 2–3.

[4] Matthew D. Mitchell, Michael D. Farren, Jeremy Horpedahl, and Olivia J. Gonzalez, "The Economics of a Targeted Economic Development Subsidy" (Mercatus Special Study, Mercatus Center at George Mason University, Arlington, VA, 2019).

positive externalities (or from taxes on activities with negative externalities).[5] It is not clear, however, that policymakers have either the knowledge or the incentive to do this properly.[6] More often, the public case for subsidies rests on the jobs and economic activity the subsidized firm creates. For example, in 2017, Wisconsin offered up to $3.46 billion to Foxconn Technology Group to locate a plant in southeast Wisconsin. The company commissioned a study concluding that the plant would add more than $62.4 billion to Wisconsin GDP over 15 years.[7] Though widely cited in the debate over the subsidy, this estimate overstates the expected economic benefits attributable to the subsidy and ignores the costs.

The estimate overstates the benefits attributable to the subsidy because it implicitly assumes that the plant would not locate in Wisconsin but for the subsidy. A recent review of 34 academic studies concluded, however, that subsidies "probably tip somewhere between 2 percent and 25 percent of incented firms toward making a decision favoring the location providing the incentives."[8] Firms are often unswayed by subsidies—even very large ones—because other factors loom larger. Labor costs, business logistics, and access to location-specific resources tend to have a bigger effect on profit. For example, the costs of locally supplied labor are typically

[5] Industrial clusters are an often-cited positive externality. However, as Michael Porter, an originator of cluster theory has put it, "Most clusters form independently of government action—and sometimes inspite of it." Michael E. Porter, "Clusters and the New Economics of Competition." *Harvard Business Review* 76, no. 6 (December 11, 1998): 77-90, 89.
[6] Christopher J. Coyne and Lotta Moberg, "The Political Economy of State-Provided Targeted Benefits," Review of Austrian Economics 28, no. 3 (September 1, 2015): 337–56.
[7] EY Quantitative Economics and Statistics, "Quantifying Project Flying Eagle's Potential Economic Impacts in Wisconsin," *EY*, July 2017.
[8] Bartik, Timothy J. "'But For' Percentages for Economic Development Incentives: What Percentage Estimates Are Plausible Based on the Research Literature?" Working Paper, W. E. Upjohn Institute for Employment Research, Kalamazoo, MI, July 1, 2018.

about 14 times larger than state and local business tax costs.[9] A mere 2 percent difference in wages can offset as much as a 40 percent difference in taxes.[10]

If subsidies are decisive between 2 and 25 percent of the time, we should revise downward the expected gross benefits attributable to any given subsidy. If a bet pays $100 with a 25 percent probability of winning, it is only worth $25. Similarly, if a subsidized factory is expected to add $62.4 billion to Wisconsin's economy over 15 years and we assume a 25 percent chance that the subsidy was decisive, then the value of the subsidy is $15.6 billion, not $62.4 billion. If we assume a 76 percent chance the subsidy was decisive (which might be more realistic for a large subsidy), then the expected gross benefit of the subsidy is $47.4 billion over 15 years.[11]

Still, this ignores the other side of the ledger: the cost of the subsidy. All else being equal, the Foxconn subsidy will require Wisconsin to keep taxes 1.08 percent higher than they otherwise would be over the next 15 years. According to the range of estimates, if a state raises taxes by 10 percent, then over the long run, economic activity will tend to decline by about 5 percent, with a plausible range between 1.5 and 8.5 percent.[12] Thus, the Foxconn subsidies may cost the state about $29 billion, with a plausible range between $8.7 and $49.5 billion.[13] With gross benefits ranging from $15.6 to $47.4 billion and gross costs ranging from $8.7 to $49.5

---

[9] Timothy J. Bartik, Who Benefits from State and Local Economic Development Policies? (Kalamazoo, MI: W. E. Upjohn Institute, 1991), 61; these figures likely vary by sector. See James Papke, "Interjurisdictional Business Tax Cost Differentials: Convergence, Divergence and Significance," Tax Notes 9, no. 4 (1995): 1701–11.

[10] Leah Beth Curran et al., "Economic Wellbeing and Where We Live: Accounting for Geographical Cost-of-Living Differences in the US," Urban Studies 43, no. 13 (December 1, 2006): 2443–66; G. Cornia, W. Testa, and F. Stocker, "State-Local Fiscal Incentives and Economic Development" (Urban and Regional Development Series Number 4, Academy of Contemporary Problems, Columbus, OH, 1978).

[11] Mitchell et al. "The Economics of a Targeted Economic Development Subsidy."

[12] Timothy J. Bartik, Who Benefits from Economic Development Incentives? How Incentive Effects on Local Incomes and the Income Distribution Bary with Different Assuptions about Incentive Policy and the Local Economy (Kalamazoo, MI: W. E. Upjohn Institute, 2018), 11.

[13] Mitchell et al. "The Economics of a Targeted Economic Development Subsidy."

billion, it is entirely possible that the expected *net benefits* of the Foxconn subsidy are negative. This conculsion is bolstered when one considers that subsidies likely entatil a host of other difficult-to-quantify costs, including rent-seeking,[14] unproductive entrepreneurship,[15] and the long-run costs of anticompetitive policy.[16]

The theoretical case against subsidies is supported by the empirical record. Since 1990 there have been more than 100 academic studies of targeted subsidies.[17] Most of these studies evaluate subsidies in light of their effects on the privileged firms, regions, or industries. But subsidies are rarely sold as a means to boost the well-being of these narrowly targeted interest groups. Instead, subsidies are typically sold as a means to benefit the communities paying for them.[18] Among those studies that evaluate subsidies in light of their effects on these broader communities, the vast majority find little to no support for subsidies.[19]

Yet despite the economic case against them, subsidies persist. Public choice models explain why.[20] Subsidies confer highly visible benefits on concentrated, politically organized

[14] Gordon Tullock, "The Welfare Costs of Tariffs, Monopolies, and Theft," *Economic Inquiry* 5, no. 3 (June 1, 1967): 224–32; Matthew D. Mitchell, "Rent Seeking at 52: An Introduction to a Special Issue of *Public Choice*," *Public Choice* 181, no. 1 (October 1, 2019): 1–4.

[15] William J. Baumol, "Entrepreneurship: Productive, Unproductive, and Destructive," *Journal of Political Economy* 98, no. 5 (October 1, 1990): 893–921; Kevin M. Murphy, Andrei Shleifer, and Robert W. Vishny, "The Allocation of Talent: Implications for Growth," *Quarterly Journal of Economics* 106, no. 2 (May 1, 1991): 503–30.

[16] Harvey Leibenstein, "Allocative Efficiency vs. 'X-Efficiency,'" *American Economic Review* 56, no. 3 (June 1, 1966): 392–415; Matthew Mitchell, *The Pathology of Privilege: The Economic Consequences of Government Favoritism* (Arlington, VA: Mercatus Center at George Mason University, 2012).

[17] Matthew D. Mitchell, Jeremy Horpedahl, and Olivia J. Gonzalez, "Do Targeted Economic Development Incentives Work as Advertised?" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, forthcoming).

[18] See Mitchell, Horpedahl, and Gonzalez, "Work as Advertised," for more details. But note that from Alexander Hamilton to Donald Trump, policymakers who advocate for subsidies almost universally speak of the benefits to the broader community.

[19] Again, see Mitchell, Horpedahl, and Gonzalez, "Work as Advertised." Among those studies that evaluate subsidies for their effects on the broader community, about two-thirds find either mixed or insignificant effects. Just 16 percent find positive effects, while 20 percent find negative effects for the broader community.

[20] Public choice is the economic study of political markets. For an overview, see Randy T. Simmons, *Beyond Politics: The Roots of Government Failure* (Oakland, CA: Independent Institute, 2011); Matthew D. Mitchell and Peter J. Boettke, *Applied Mainline Economics: Bridging the Gap between Theory and Public Policy*, 1st ed. (Arlington, VA: Mercatus Center at George Mason University, 2017).

special interests, while their costs are less obvious and spread across diffuse, politically unorganized taxpayers, consumers, and small businesses.[21] This pattern of concentrated benefits and diffuse costs explains the persistence of many inefficient policies.[22] The problem is compounded because voters are often ignorant or confused about the technical aspects of economic development policy.[23] As a result, political leaders may misclassify costs as benefits and believe that a project is more valuable because it involves a large investment or requires a large workforce.[24]

Given the persistence and prevalence of targeted subsidies despite the economic case against them, institutional constraints—such as state anti-aid provisions—are needed to limit their use.

[21] As the economists Robert Ekelund and Robert Tollison have put it, "The undergirding principle of the interest-group approach is nonetheless organizational costs. The theory begins and ends with this principle. Organized groups gain political wealth transfers at the expense of unorganized or less-well-organized groups." Robert B. Ekelund Jr. and Robert D. Tollison, "The Interest-Group Theory of Government," in *The Elgar Companion to Public Choice*, ed. William F. Shughart Jr. and Laura Razzolini, 357–78 (Cheltenham, UK: Edward Elgar, 2001).
[22] Mancur Olson, *The Logic of Collective Action: Public Goods and the Theory of Groups*, 2nd ed. (Cambridge, MA: Harvard University Press, 1965); Theodore J. Lowi, *The End of Liberalism: The Second Republic of the United States*, 40th anniv. ed. (New York: W. W. Norton, 1969); Peter Schuck, *Why Government Fails So Often: And How It Can Do Better* (Princeton, NJ: Princeton University Press, 2014).
[23] Because their votes are unlikely to make a difference in any election, voters tend to be rationally ignorant about policy and its effects. Worse, they have little incentive to spend time thinking about public policy, causing irrational notions to persist. Anthony Downs, *An Economic Theory of Democracy* (New York: Harper & Row, 1957); Bryan Caplan, *The Myth of the Rational Voter: Why Democracies Choose Bad Policies*, new ed. (Princeton, NJ: Princeton University Press, 2008).
[24] Barry R. Weingast, Kenneth A. Shepsle, and Christopher Johnsen, "The Political Economy of Benefits and Costs: A Neoclassical Approach to Distributive Politics," *Journal of Political Economy* 89, no. 4 (August 1, 1981): 642–64.

II. The Rise of Favoritism in the US

Governments have favored particular firms, industries, and interests for centuries. And for almost as long, economists have been critical of the practice.[25] At the time of the American founding, what Adam Smith dubbed “mercantilism” had dominated European economic policy for nearly three centuries. Yet despite its long and entrenched practice, early US policymakers showed ambivalence toward mercantilism, especially at the national level. Congress rejected Hamilton’s plan to promote manufacturing through tariffs and subsidies in 1791, and when it later resurfaced as Henry Clay’s “American system,” that too was largely rejected. Thus, for the first several decades of the republic, neither the states nor the federal government actively promoted particular firms or industries.[26]

Beginning in the 1820s, state spending changed in both size and scope. First, states—especially southern states—began to invest in private banks.[27] Then, following the rejection at the national level of John Quincy Adams’s proposals to spend heavily on “internal improvements” (modeled on Henry Clay’s “American system”), some states began funding infrastructure projects on their own.

The success of the publicly funded Erie Canal, completed in 1825, provided further impetus. It inspired two decades of state-supported railroads, turnpikes, and canals across the

[25] For an early critique, see Adam Smith’s *Wealth of Nations*. For more recent critiques, see Douglass C. North, John Joseph Wallis, and Barry R. Weingast, *Violence and Social Orders: A Conceptual Framework for Interpreting Recorded Human History*, 1st ed. (Cambridge: Cambridge University Press, 2009); Daron Acemoglu and James Robinson, *Why Nations Fail: The Origins of Power, Prosperity, and Poverty*, 1st ed. (New York: Crown Business, 2012).

[26] Some of this opposition likely arose from the unique circumstances of the American founding. The much-reviled Tea Act of 1773, for example, was a mercantilist tax privilege for the East India Tea Company, a British government-chartered firm that already enjoyed several regulatory privileges. The founding era also coincided with the birth of classical economics, which rejected the earlier mercantilist theories.

[27] Wallis, “American Government Finance,” 67; Rodden, *Hamilton’s Paradox*, 58.

nation.[28] State governments hoped to stimulate their economies through investment in private firms, especially as interstate competition for economic development escalated.[29] During this era, "railroad promoters encouraged towns to bid against each other for influence in locating the railroads."[30] And towns obliged because railroads were believed to have "great potential for public benefit"[31] and to be "critical for economic development since the existence of the railroad would attract other economic enterprise."[32] Given the Jacksonian era's disdain for national spending on such projects, it was the states that took the lead.[33] But, as Columbia Law School's Richard Briffault notes, "Many of these projects blurred public and private lines, with states investing in private firms, or providing grants, loans and loan guarantees to private companies."[34]

Though the political appetite for locally funded infrastructure was high, the appetite for taxes to pay for it was low. Early on, states had relied on property taxes.[35] As they began earning income on private projects, however, confidence in infrastructure investments grew, and some states reduced or eliminated their property taxes. By 1835, Alabama, Georgia, Maryland, Massachusetts, New York, Rhode Island, Pennsylvania, and South Carolina had all eliminated state property taxes.[36] Direct taxation—including property, poll, and income taxation—had all but disappeared.[37] In its place, the main sources of state revenue became sales of public lands,

---

[28] Richard Briffault, "Disfavored Constitution: State Fiscal Limits and State Constitutional Law," *Rutgers Law Journal* 34, no. 4 (Summer 2003): 911.
[29] Briffault, "Disfavored Constitution, " 911.
[30] Brian Libgober, "The Death of Public Purpose (And How to Prevent It)" (Harvard Law School Discussion Paper, Cambridge, MA, March 2016), 13.
[31] Nicholas J. Houpt, "Shopping for State Constitutions: Gift Clauses as Obstacles to State Encouragement of Carbon Sequestration," *Columbia Journal of Environmental Law* 36 (2011): 381.
[32] Schaefer, "State Investment Attraction," 342.
[33] See, for example, Jackson's famous veto of the Maysville Road. The president not only noted that the project was "purely local" but also warned of "artful expedients to shift upon the Government the losses of unsuccessful private speculation." Andrew Jackson, "Veto Message," American Presidency Project (website), May 27, 1830.
[34] Briffault, "Disfavored Constitution," 911.
[35] Wallis, "American Government Finance," 67.
[36] Wallis, 67.
[37] Rodden, *Hamilton's Paradox*, 57.

returns on private investments, and proceeds from issuing bank charters.[38] The economic historian John Joseph Wallis termed this the era of "taxless finance."[39] Reminiscent of modern loan guarantees, under taxless finance, taxpayers took a loss on projects such as canals, roads, or banks only if they failed.[40] And evidently, policymakers everywhere convinced themselves that failure was impossible. A delegate to the Maryland Reform Convention reflected two decades later, "Every man dreamed he was about to reach a new *El Dorado*. Taxation was to exist no longer—public debt was to become an obsolete idea."[41]

State debt did not become an obsolete idea. In fact, it grew substantially. At the beginning of the 1820s, most states had little or no debt.[42] But between 1836 and 1839, states incurred more debt than they had in their entire previous histories.[43] Between 1810 and 1840, state debt per capita rose 144 percent.[44] By the late 1830s, state debt soared to eight times all federal and local debts combined.[45] In 1830, Arkansas, Florida, Illinois, Indiana, Michigan, and Mississippi had no debt. But a decade later, their combined general obligation debt was more than $44 million (in current dollars).[46] As collateral against these debts, states relied on the federal government's implied support and the option of resuming property tax collection.[47]

---

[38] Rodden, 57.
[39] John Joseph Wallis, "Constitutions, Corporations, and Corruption: American States and Constitutional Change, 1842 to 1852," *Journal of Economic History* 65, no. 1 (2005): 213.
[40] Wallis, "Constitutions, Corporations, and Corruption," 213.
[41] Quoted in Carter Goodrich, "The Revulsion against Internal Improvements," *Journal of Economic History* 10, no. 2 (1950): 153.
[42] Rodden, *Hamilton's Paradox*, 57.
[43] Rodden, 58.
[44] Wallis, "American Government Finance," 61, 65.
[45] Wallis, "American Government Finance," 62.
[46] Dale F. Rubin, "Constitutional Aid Limitation Provisions and the Public Purpose Doctrine," *Saint Louis University Public Law Review* 12 (1993): 156.
[47] The federal government had bailed out state Revolutionary War debts in 1790 and again repaid some state debts following the War of 1812. Then, in 1836, Congress agreed to pay $1.5 million in debts incurred by the District of Columbia. Many believe that these actions caused creditors to assume that the federal government would always bail out state governments. Rodden, *Hamilton's Paradox*, 55–60; Thomas J. Sargent, "Nobel Lecture: United States Then, Europe Now," *Journal of Political Economy* 120, no. 1 (February 2012): 15.

Because these ventures permitted private actors to gamble with public money—privatizing gains and socializing losses—there was a strong incentive to pursue risky projects. According toRutgers University law professor David Pinsky,

> There was practically no public control over the planning of the railroad project[s] or over the actual expenditures of publicly contributed funds. These functions were completely delegated to private corporate officials. To phrase it more dramatically, but no less accurately, there was a total abdication of public responsibility. Not infrequently, railroad planning was so speculatively conceived and incompetently executed that the proposed line was never completed. Waste and dishonesty in the expenditure of funds led to corporate insolvency and abandonment of routes.[48]

The unsustainable nature of these public investments in private ventures was laid bare by the panic of 1837 and the significant recession that lasted from 1839 to 1843.[49] As the economy contracted, infrastructure projects across the country—marked “by waste, overbuilding, and mismanagement”—failed to generate expected revenues.[50] By 1842, eight states and one territory had defaulted.[51] Four states—Arkansas, Florida, Michigan, and Mississippi—repudiated nearly $14 million in debt.[52] Out of these circumstances, the first wave of state constitutional anti-aid provisions was born.

III. Anti-Aid Clauses

As state fiscal positions eroded, support for federal assumption of state debts grew, especially among politicians representing the most heavily indebted states. Ultimately, however, the assumption proposal was tabled. Unable to shift their debts onto federal taxpayers, states were

---

48 Pinsky, “State Constitutional Limitations,” 280.
49 Rodden, *Hamilton’s Paradox*, 58.
50 Briffault, “Disfavored Constitution,” 911.
51 The defaulting states were Arkansas, Illinois, Indiana, Louisiana, Maryland, Michigan, Mississippi, Pennsylvania, and the territory of Florida. Rodden, *Hamilton’s Paradox*, 59.
52 Benjamin Ulysses Ratchford, *American State Debts* (Durham, NC: Duke University Press, 1941), 114. As Joshua Bates, the umpire of the Anglo-American claims convention of 1853, put it, “It is to be hoped that sooner or later the people of Florida will discover that honesty is the best policy; and that no State can be called respectable that does not honorably fulfill its engagements” (111).

left to clean up their own messes. And one important consequence was that citizens and local leaders mobilized to prevent future messes. A particularly important strategy was to adopt constitutional limitations on public aid to private entities.[53] As law professor Dale Rubin notes, “The impetus for the adoption of both state and local constitutional aid limitation provisions was the untrammeled and indiscriminate borrowing by governmental entities and the ruthless profiteering by private corporations and individuals.”[54]

Moreover, the aim of public aid limitations was, as one delegate to the Ohio conventions of 1850 and 1851 put it, “to see the State Government brought back to its simple and appropriate functions, [leaving] railroad, canal, turnpike and other corporate associations, to get along on their own credit, without any connection or partnership with the State whatever.”[55] And as Josiah Scott of the Ohio Supreme Court put it, these provisions aimed to prohibit the union of public and private capital: “The mischief which this section interdicts is a business partnership between a municipality or subdivision of the State, and individuals or private corporations or associations. It forbids the union of public and private capital or credit in any enterprise whatever.”[56]

Commented [VT1]: Since this is a different audience than the paper, I think we can delete all of these introductions. Reader can always see the footnote to find out where the quote is from.

Despite their early adoption by a few states in the 1840s, it took more than a decade for a majority of states to adopt anti-aid provisions.[57] These provisions generally took three forms. The most common was a *credit clause*, which forbade the government from loaning credit to a private individual, association, or corporation. A variant of this clause first appeared in the

[53] These approaches were not mutually exclusive. Rhode Island’s debt clause read, “The general assembly shall have no power hereafter, without the express consent of the people, to incur state debt to an amount exceeding 50,000 dollars, except in time of war, or in case of insurrection; Nor shall they in any case, without such consent, pledge the faith of the state for the payment of the obligations of others.” Rhode Island Constitution of 1842, art. 4, sec. 13, 1842.
[54] Rubin, “Constitutional Aid Limitation Provisions,” 156.
[55] Quoted in Kermit L. Hall and Peter Karsten, *The Magic Mirror: Law in American History*, 2nd ed. (New York: Oxford University Press, 2008), 103–4.
[56] Josiah Scott, Walker v. City of Cincinnati, 21 Ohio St. 14 (1871).
[57] Rubin, “Constitutional Aid Limitation Provisions,” 144n5.

Rhode Island Constitution of 1842, requiring electoral approval for such deals. Shortly thereafter, New Jersey (1844) and New York (1846) adopted credit clauses that forbade lending credit with or without electoral approval.[58] The second type of anti-aid provision was a *stock clause*, which forbade the government from becoming a stockholder in any corporation. This was pioneered by Iowa in 1846.[59] The final provision was a *gift clause*, which forbade the government from granting loans or donations to any individual, association, or corporation. This provision first appeared in Pennsylvania's 1873 constitution.[60]

The spread of anti-aid provisions was by no means uniform. Some states adopted just one provision, some two, and others all three. Moreover, especially in their earliest iterations, anti-aid provisions did not necessarily apply to substate governments, such as counties, cities, or school districts.[61] Despite these variations, however, by 1900 some form of public aid limitation had been adopted by a large majority of states.[62] Even those that had withstood the panic of 1837 without defaulting adopted these provisions to avoid the fate of their neighbors.[63]

In the decades following the advent of these anti-aid provisions, state aid to private corporations did not end altogether, but it was sharply curtailed.[64] As Wallis notes, "The tide of events had turned against state activity."[65] Following the adoption of these provisions, there was a dramatic change in state and local fiscal policy; states reduced their reliance on debt finance,

[58] Pinsky, "State Constitutional Limitations," 278n70.
[59] Pinsky, 278n71.
[60] Pinsky, 279n77.
[61] Pinsky, "State Constitutional Limitations," 280.
[62] Pinsky, 280.
[63] Tarr, *Understanding State Constitutions*, 112.
[64] Wallis, "American Government Finance," 70.
[65] Wallis, 70.

and more activity shifted from state to local governments.[66] In 1841, the states' share of all government debt was 86.4 percent, but by 1902, it was 7.0 percent.[67]

IV. Anti-Aid Provisions Applied to Localities

The first wave of anti-aid provisions did not always apply to localities.[68] Consequently, as states curtailed their direct support of private interests, localities ramped it up. In many cases local governments began to take on the sorts of risks that states had once assumed. Sometimes states abetted this local circumvention of anti-aid provisions. Constitutional scholar Alan Tarr writes, "From 1866 to 1873, legislatures approved over eight hundred proposals to grant local aid to railroad companies. New York, Illinois, and Missouri together authorized over $70 million worth of aid."[69]

As with the state aid that had preceded it, much of this local aid was financed through government borrowing or guarantees of private debt. Thus, as the states' share of all government debt was declining, localities' share rose, going from 11.4 percent in 1841 to 57.1 percent in 1902.[70] Similarly, while local government revenue per capita was about 40 percent greater than state revenue per capita in 1840, by 1902 it was 260 percent greater.[71]

As before, the precarious fiscal position of governments—this time, local governments—was laid bare by a national economic contraction. As the panic of 1873 gave way to a deep and lasting economic depression, property values plummeted, and railroads began to default on their

66 Wallis, 66–70.
67 Wallis, 66.
68 Houpt, "Shopping for State Constitutions," 381; Pinsky, "State Constitutional Limitations," 278–80.
69 Tarr, *Understanding State Constitutions*, 114.
70 Wallis, "American Government Finance," 66.
71 Wallis, 70.

debts. By 1874, about 25 percent of all railroad bonds were in default.[72] Next, municipalities that had guaranteed many of these debts began to default on their own obligations en masse. It is estimated that roughly 20 percent of all municipal debt obligations were defaulted on in the 1870s.[73]

These defaults prompted a second wave of constitutional reforms that extended anti-aid provisions to local governments.[74] While a few states (Indiana in 1851, Nevada in 1864, Georgia in 1868, and Illinois in 1870) had already extended their anti-aid provisions to localities, the municipal debt crisis of the 1870s prompted more than a dozen other states to do so over the course of the next fifteen years.[75]

The second wave of anti-aid provisions was more successful than the first. With the municipal fiscal crisis fresh in mind and the framers' intentions abundantly clear, courts were active over the next half century in policing governments that overstepped the bounds of anti-aid clauses, certainly more active than they would come to be as the 20th century wore on.

---

72 John A. Dove, "Financial Markets, Fiscal Constraints, and Municipal Debt: Lessons and Evidence from the Panic of 1873," *Journal of Institutional Economics* 10, no. 1 (2014): 76.

73 C. H. Chatters, *Municipal Debt Defaults: Their Prevention and Adjustment* (Chicago: Public Administration Service, 1933); A. M. Hillhouse, *Municipal Bonds: A Century of Experience* (New York: Prentice-Hall, 1936); Dove, "Financial Markets, Fiscal Constraints."

74 Tarr, *Understanding State Constitutions*, 114; Briffault, "Disfavored Constitution," 912.

75 Credit and stock clauses were applied to local governments by Arkansas, New York, and Pennsylvania in 1874; Alabama, Florida, and Missouri in 1875; Colorado and Texas in 1876; Connecticut and New Hampshire in 1877; Maine in 1878; California in 1879; and Montana and Washington in 1889. Dove, "Financial Markets, Fiscal Constraints," 77.

Importantly, early courts understood that the framers of these provisions intended them to limit public aid to private interests regardless of the aid's purpose.[76]

Courts were, however, by no means universally rigorous in policing state and local violations of anti-aid provisions.[77] Over time, legislatures circumvented these rules while courts invented new doctrines that vitiated these provisions. Nevertheless, the case history of this period shows that—for a time—in geographically and politically diverse regions of the country, courts were willing to stop the elected branches when they transgressed constitutional anti-aid provisions.[78]

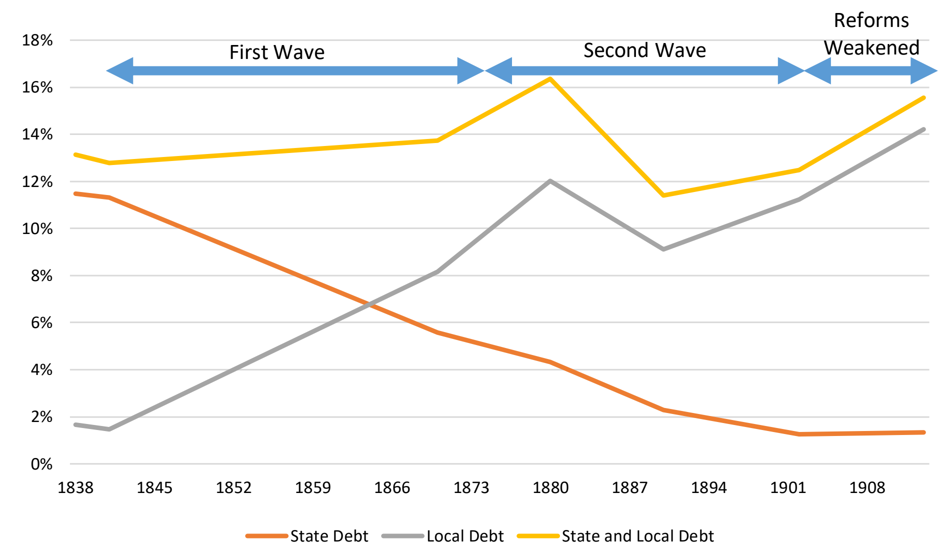
What was the result? While it is impossible to determine a causal relationship or to disentangle the effects of these provisions from those of other reforms adopted at this time, anti-aid provisions did coincide with improved policy. First, the financial footing of government grew stronger. Figure 1 shows state, local, and combined state and local debt as a share of national income from 1838 through 1913. Immediately following the first wave of reforms, state debts as a share of national income began to fall. Given the local loophole, however, local debt as a share of income rose. Following the second wave of reforms, local debt as a share of GDP also began to fall and then leveled off. By the end of the 19th century, combined state and local debt stood

[76] See, for example, Adams v. Jackson Elec. Ry., Light & Power Co., 30 So. 58, 59 (Miss. 1901) (invalidating expenditure with no discussion of public purpose); State ex rel. Bd. of Control of St. Louis Sch. & Museum of Fine Arts v. City of St. Louis, 115 S.W. 534, 548 (Mo. 1908) (invalidating expenditure despite claim of public purpose and discussing history of provisions); Wyscaver v. Adkins, 37 Ohio St. 80 (1881) (striking down a statute authorizing a township to raise $20,000 to make a private railway and finding that the state's anti-aid clause "forbids the union of public and private capital or credit in any enterprise whatever"); Counterman v. Dublin Township, 38 Ohio St. 515 (1882); Taylor v. Comm'rs of Ross County, 23 Ohio St. 22 (1872); Pleasant Township v. Aetna Life Ins. Co., 138 U.S. 67, 11 S. Ct. 215, 34 U.S. (L. ed.) 864 (1891); Alter v. Cincinnati, 56 Ohio St. 47 (1897); State v. City of St. Louis, 115 S.W. 534 (1908) (invalidating a statute that permitted St. Louis to levy a tax that benefited a private corporation, the St. Louis School and Museum of Fine Arts); Garland v. Board of Revenue of Montgomery County, 6 So. 402 (1889) (invalidating a municipal proposal to build a bridge for a railroad); Mayor of Jersey City v. North Jersey St. Ry. Co., 73 A. 609 (1909) (holding that failure to collect licensing fee from railroad for 30 years was a violation of the state's anti-aid clause).
[77] Rubin, "Constitutional Aid Limitation Provisions," 161.
[78] Rubin, 161.

as a smaller share of national income than at any previous point since the crisis of the early 1840s. Second, as their fiscal positions improved, municipalities found themselves facing lower borrowing costs. Economist John Dove analyzed the prices of bonds issued by dozens of US cities in the latter decades of the 19th century.[79] He found that among those cities that had defaulted during the 1870s, those that subsequently adopted either a credit or stock clause faced borrowing costs that were between 170 and 249 basis points lower.[80] Finally, as state and local governments curtailed their use of targeted economic development subsidies, the US economy entered a period of prolonged and robust economic expansion.[81]

[79] Dove, "Financial Markets, Fiscal Constraints."
[80] His analysis is based on an ordinary least squares (OLS) regression that includes a large set of control variables that account for other socioeconomic factors that might affect borrowing costs. Dove, 92.
[81] Christina D. Romer, "Is the Stabilization of the Postwar Economy a Figment of the Data?," *American Economic Review* 76, no. 3 (1986): 314–34.

Figure 1. Government Debt as a Share of National Income



Sources: Debt figures are reported in John Joseph Wallis, "American Government Finance in the Long Run: 1790 to 1990," *Journal of Economic Perspectives* 14, no. 1 (2000). National income figures are from US Department of Commerce, Bureau of the Census, *Historical Statistics of the United States 1789–1945: A Supplement to the Statistical Abstract of the United States*, Washington, DC, June 1949, 14. National income figures are not available for every year, and some data are interpolated.

Researchers have found that well into the latter half of the 20th century these constitutional prohibitions were influencing the types of incentives governments offered, making gifts of land and money the least-used.[82] More recently, economist Carlianne Patrick has developed an index measuring the strength of constitutional aid limits.[83] Places with weaker limits—and therefore more subsidies to private businesses—experience significantly lower

[82] John C. Gray and Dean A. Spina, "State and Local Industrial Location Incentives—a Well-Stocked Candy Store," *Journal of Corporate Law* 5 (1980): 528.
[83] Carlianne Patrick, "Does Increasing Available Non-Tax Economic Development Incentives Result in More Jobs?," *National Tax Journal* 67, no. 2 (June 2014): 351–86.

levels of rural employment in the medium term. In subsequent work, she has found that states with weaker anti-aid provisions tend to subsidize capital, causing firms to substitute such capital as computers and robots for labor. She finds that this decreases employment density and causes an employment shift from labor-intensive to capital-intensive industries.[84]

V. The Weakening of Anti-Aid Provisions

Courts have weakened constitutional anti-aid provisions over the past century.[85] They did solargely by turning the judicially created Public Purpose Doctrine on its head. The doctrine dates back to an 1853 case called *Sharpless v. Mayor of Philadelphia*,[86] which was decided two decades before an anti-aid provision was added to the Pennsylvania Constitution.[87] In the 1840s and 1850s, the Pennsylvania legislature had authorized Philadelphia to use borrowed money to buy shares in two private railroads.[88] A Philadelphia taxpayer named William P. Sharpless brought suit claiming that the state had no authority to use the public taxing power to support a private interest.

At least in principle, the Pennsylvania Supreme Court agreed: "It is said that this is a taking of *private* property for *private* use. If this be so, it is palpably unconstitutional." Though

---

[84] Carlianne Patrick, "Jobless Capital? The Role of Capital Subsidies" (working paper, W. E. Upjohn Institute for Employment Research, Kalamazoo, MI, January 1, 2015).

[85] State legislatures have also done much to circumvent constitutional restrictions and provide public resources for private purposes. Though it is beyond the scope of the current analysis, state legislatures frequently circumvent anti-aid clauses through the creation of revenue bonds, moral obligation bonds, and special districts. Governments typically issue revenue bonds to finance the purchase of property that they then lease to private firms. Unlike a general obligation bond, a revenue bond is not backed by government credit or taxing authority; the bond is only secured by the property and by the rental payments from the firm, sparing taxpayers the risk and making it similar in function to a private bond. Because of this, these bonds have not been found to run afoul of state credit clauses. Federal taxpayers do bear a cost, however, because the interest on revenue bonds is exempt from federal income taxation. Moreover, many states exempt the projects financed through these bonds from state and local property taxes because they deem the property to be owned by the public and not by the private entity that occupies it. See Rubin, "Constitutional Aid Limitation Provisions," 161; Gray and Spina, "State and Local," 533–37.

[86] Sharpless v. Mayor of Philadelphia, 21 Pa. 147 (1853).

[87] Dove, "Financial Markets, Fiscal Constraints," 77.

[88] Howard Gillman, Mark A. Graber, and Keith E. Whittington, *American Constitutionalism*, vol. 1, *Structures of Government, Supplementary Material* (New York: Oxford University Press, 2013), 1.

the constitution had no "express inhibition" against such legislation, the court concluded that the assembly had no authority "to take one man's property and give it to another."[89] Thus was born the Public Purpose Doctrine: the state may only tax to fund projects that are in the public interest; projects that benefit private interests are forbidden. In 1874, the US Supreme Court issued its first ruling regarding the Public Purpose Doctrine, finding that state legislatures may confer to municipalities the right to levy taxes, but only if those taxes serve a public purpose.[90] By 1917, the Court had incorporated the doctrine into the 14th Amendment.[91]

On its face, the Public Purpose Doctrine would seem to complement state constitutional anti-aid provisions. Like these provisions, it prohibits the expenditure of public resources in service of private interests. In practice, however, it has come to thwart anti-aid provisions for two reasons. First, from the beginning, courts have shown an extraordinary tendency to construe "public purpose" as broadly as possible. Even in *Sharpless* itself, the court did *not* side with the taxpayer. Instead, the court concluded that, even though the railroad was private, the railroad subsidy nevertheless served a public purpose: "It cannot be denied that a railroad company is a private corporation. But the right to tax depends on the ultimate use, purpose, and object for which the fund is raised, and not on the nature or character of the person or corporation whose intermediate agency is to be used in applying it."[92]

In other words, the court concluded that the government could buy shares in a private corporation so long as the goal was to serve a public purpose. Second, decades later, courts would come to see the Public Purpose Doctrine as an *exception* to anti-aid provisions rather than a *complement* to them. In the 1918 case of *Georgia v. Cincinnati Southern Railway*, for example,

[89] *Sharpless*, 21 Pa. at 167.
[90] Loan Association v. Topeka, 87 U.S. (20 Wall.) (1874).
[91] Jones v. City of Portland, 245 U.S. 217 (1917).
[92] *Sharpless*, 21 Pa. at 169.

the US Supreme Court held that Georgia could grant a right-of-way to a railroad despite the constitutional bar against “any donation or gratuity in favor of any person, corporation or association,” because a “conveyance in aid of a public purpose from which great benefits are expected is not within the class of evils that the constitution intended to prevent.”[93] Courts reached similar conclusions in a number of other states.[94]

In all of these cases, courts found that the judicially created Public Purpose Doctrine was an exception to constitutional anti-aid provisions.[95] They viewed the doctrine as a justification for public aid to private enterprise so long as the expenditure served some public or quasi-public purpose. This interpretation contradicts the doctrine’s initial articulation as a *restraint* on government expenditures, requiring all public projects to serve purely public purposes. It also contradicts the plain language of anti-aid provisions, which forbid government aid to private firms or individuals regardless of the aid’s purpose.

Another problem with this interpretation is that the Public Purpose Doctrine was first adumbrated in *Sharpless* in 1853, decades *before* most states adopted anti-aid provisions. As Rubin notes, “Since most of the aid limitation provisions were adopted *after* the Public Purpose Doctrine was judicially enunciated, the courts could not have conceived the doctrine either as an exception or as a doctrine devised to preempt such limitations.”[96]

In the landmark *Munn* decision of 1876, the US Supreme Court held that the government could regulate economic arrangements that were “affected with a public interest.”[97] Following

---

93 Georgia v. Cincinnati Southern Railway, 248 U.S. 26, 30 (1874).
94 City of Oakland v. Garrison, 228 P. 433 (Cal. 1924); Alameda County v. Janssen, 106 P.2d 11 (Cal. 1940); Brazoria County v. Perry, 537 S.W.2d 89 (Tex. 1976); City of Charlottesville v. Dehaan, 323 S.E.2d 131 (Va. 1984); Hayes v. State Property and Buildings Comm’n, 731 S.W.2d 797 (Ky. 1987); City of Aurora v. Public Utilities Comm’n, 785 P.2d 1280 (Colo. 1990).
95 For a fuller discussion, see Rubin, “Constitutional Aid Limitation Provisions.”
96 Rubin, “Constitutional Aid Limitation Provisions,” 166 (emphasis in original).
97 Munn v. People of State of Illinois, 94 U.S. 113, 126, 24 L. Ed. 77 (1876).

this decision, state constitutions written in the ensuing decades, and legislation enacted during this period, began using "public interest" phraseology.[98]

Government involvement with and regulation of private enterprise increased dramatically during the Great Depression. Economists, legal theorists, and policymakers challenged long-held beliefs about the proper role of government in the private economy.[99] Aware that courts saw the Public Purpose Doctrine as an exception to anti-aid provisions, state legislatures were careful to include the words "public purpose" in their subsidy legislation. This practice dates back to Mississippi's famous 1936 Balance Agriculture with Industry (BAWI) program, which is widely considered to mark the beginning of the modern era of targeted economic development subsidies. The BAWI program permitted local governments to hold bond elections to purchase land, build factories, and rent these facilities to private manufacturers at low cost.[100] In the preamble to the act, legislators wrote that the "general welfare of its citizens demand, as a public purpose, the development within Mississippi of industrial and manufacturing enterprises."[101] As economist James Bennett states, "By invoking those magic words, those constitutional talismans *general welfare* and *public purpose*, this act, which plainly violated the state charter of the Magnolia State, became kosher."[102] When the BAWI program came before the Mississippi Supreme Court, a majority of justices found it did not violate the state's anti-aid provision, because "in all its parts it contemplates that the proposed industry shall be operated for the accomplishment of the

[98] Timothy Sandefur, "A Natural Rights Perspective on Eminent Domain in California: A Rationale for Meaningful Judicial Scrutiny of 'Public Use,'" *Southwestern University Law Review* 32 (2003): 648–51.
[99] Robert Higgs, *Crisis and Leviathan: Critical Episodes in the Growth of American Government*, 25th anniv. ed. (Oakland, CA: Independent Institute, 1987); Price Fishback, *Government and the American Economy: A New History* (Chicago: University Of Chicago Press, 2007).
[100] Peter K. Eisinger, *Rise of the Entrepreneurial State*, La Follette Public Policy Series: State and Local Economic Development Policy in the United States (Madison: University of Wisconsin Press, 1989); Bennett, *Corporate Welfare*, 80.
[101] Quoted in James C. Cobb, *The Selling of the South: The Southern Crusade for Industrial Development, 1936–1980* (Baton Rouge: Louisiana State University Press, 1982), 14.
[102] Bennett, *Corporate Welfare*, 83.

purposes outlined therein."[103] In his blistering dissent, Justice Anderson said the decision "drove a steam shovel through our constitution."[104] The US Supreme Court dismissed an appeal of the case and thus, in the words of two scholars, "closed the door on federal court review of the basic principles underlying industrial development bond financing."[105]

The evolution of anti-aid provisions in many states progressed from strict enforcement after they were first adopted to subsequent approval of subsidies for low-income housing (or "slum clearance") programs and other support for the poor, then to approval of industrial manufacturing projects, and finally to approval of all manner of economic development schemes.[106]

In time, courts came to take what Briffault describes as "a posture of extreme deference to state legislatures, finding that a broad range of goals fall under the rubric of public purpose, and that legislative determinations that a spending, loan, or tax incentive program will promote the public purpose are to be accepted as long as they are 'not . . . irrational.'"[107]

---

[103] Albritton v. City of Winona, 178 So. 799 (Miss. 1938).
[104] 178 So. at 812 (Anderson, J., dissenting).
[105] Gray and Spina, "State and Local," 538.
[106] See, for example, Humphrey v. City of Phoenix, 55 Ariz. 374 (1940) (upholding revenue bonds to finance a slum clearance project); In re Constitutionality of ORS 456.720, 272 Or. 398 (1975) (same); Opinion to the Governor, 112 R.I. 151, 155–56 (1973) ("The elimination of overcrowded, unsanitary and dangerous dwelling accommodations and the assisting in making available decent, safe and sanitary housing for people whose income would make such an acquisition impossible unquestionably serves a public purpose."); Utah Hous. Fin. Agency v. Smart, 561 P.2d 1052, 1054 (Utah 1977) ("It cannot be said that the finding of the legislature that a public purpose is served by increasing the availability of financing for construction, purchase, and rehabilitation of low and moderate income housing, is incorrect or unreasonable on its face."); Suber v. Alaska State Bond Comm., 414 P.2d 546, 552 (Alaska 1966) (public purpose for relief and support of the poor); Wright v. City of Palmer, 468 P.2d 326, 330–31 (Alaska 1985) (public purpose for improvement program to encourage industrial development); Carruthers v. Port of Astoria, 249 Or. 329, 336 (1968) (listing several cases in which revenue bonds for industrial development were upheld as a public purpose); Maready v. City of Winston-Salem, 342 N.C. 708, 725 (1996) (listing 46 states that have upheld economic development as a public purpose).
[107] Briffault, "Disfavored Constitution," 914, quoting Delogu v. State, 720 A.2d 1153 (Me. 1998).

In so doing, they forgot or ignored the initial aim of the provisions—namely, as the Arizona Supreme Court declared, "to prevent governmental bodies from depleting the public treasury by giving advantages to special interests or by engaging in non-public enterprises." [108] The purpose of these provisions is no less relevant today, especially in the context of prolific public aid to private businesses for the so-called public purpose of economic development (despite the fact that the public is no better off for it).[109]

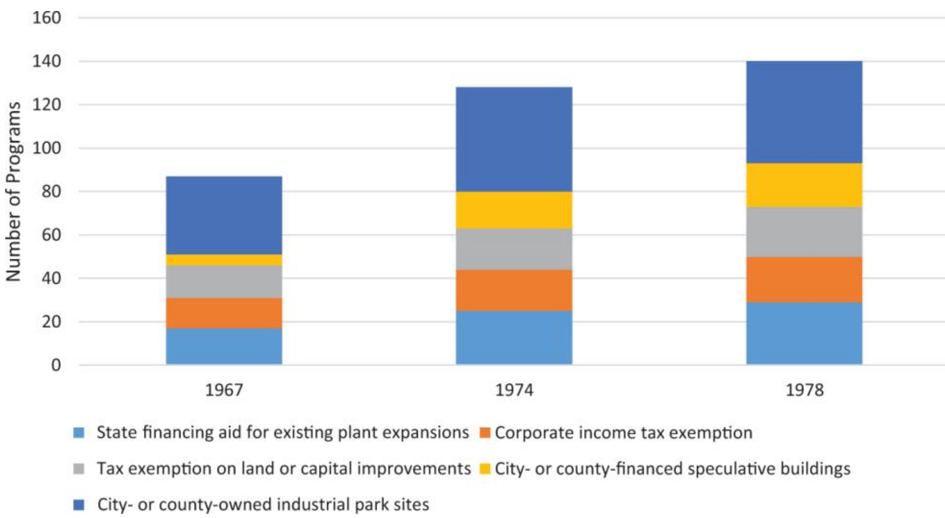
Following the BAWI program and the courts' acceptance of it, other southern states initiated their own targeted economic development programs, and in the years following World War II, the practice became all but universal. Figure 2 shows the proliferation of such programs in the 1960s and 1970s. Even when courts did not defer to legislative judgments and declared subsidies unconstitutional, state legislators reacted by amending their constitutions to once again permit subsidies. For example, in 1987, Texas amended its constitution to read as follows: "Notwithstanding any other provision of this constitution, the legislature may provide for the creation of programs and the making of loans and grants of public money . . . for the public purposes of development and diversification of the economy of the state."[110] In some cases, courts appealed to such extraconstitutional considerations as interstate economic competition as a rationale for upholding subsidies.[111] As North Carolina's Justice Robert Orr stated in a 1996 dissent, the judicial philosophy in these cases seems to boil down to "everybody's doing it."[112]

---

[108] Wistuber v. Paradise Valley Unified Sch. Dist., 141 Ariz. 346, 349 (1984). See also Bannon v. Port of Palm Beach District, 246 So. 2d 737, 741 (Fla. 1971) (to "protect public funds and resources from being exploited in assisting or promoting private ventures when the public would be at most only incidentally benefited"); Idaho Falls Consolidated Hospitals v. Bingham County Board of Commissioners, 102 Idaho 838 (1982) (apparent that framers "were primarily concerned about private interests gaining advantage at the expense of the taxpayer"); Lawrence v. Schellstede, 348 P.2d 1078, 1081–82 (Okla. 1960) (to prevent the investment of public funds in private enterprises).
[109] See section II above.
[110] Tex. Const. art. 3, sec. 52-a (1987).
[111] For a thorough discussion of this and citations, see Schaefer, *State Investment Attraction*.
[112] *Maready*, 342 N.C. at 739 (Orr, J., dissenting).

Briffault reports, "By the end of the [20th] century virtually every state supreme court had upheld at least some economic development programs that involved direct assistance—including cash grants, low-interest loans, and tax breaks—to individual firms."[113]

Figure 2. Growth in the Number of States Offering Incentives



Source: "The Fifty Legislative Climates," an annual survey of the states published in the November–December issue of *Industrial Development* for the years 1967, 1974, and 1978, reprinted in H. McKinley Conway, *Legislative Climates for Economic Development* (Atlanta: Conway Publications, 1979), A-3 to A-5, A-99 to A-101, A-255 to A-257.

VI. The Current State of Anti-Aid Provisions

Currently, 45 states have anti-aid provisions that prohibit public financing of private entities through credit, stock, or gift clauses (see figure 3):[114] 44 have a credit clause prohibiting government bodies from lending money or credit for nonpublic uses; 32 have a stock clause

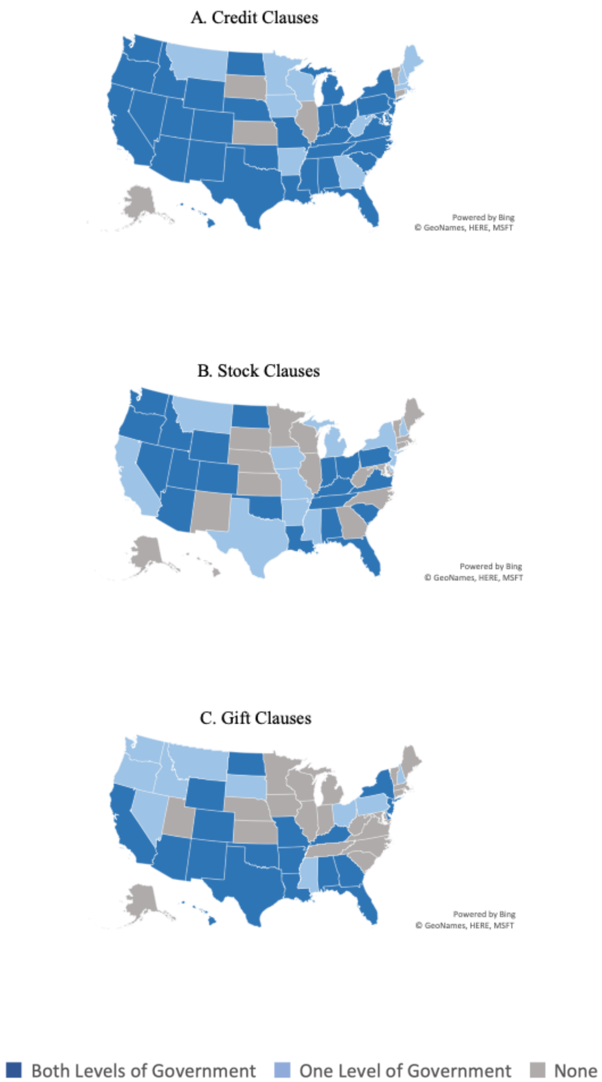
[113] Briffault, "Disfavored Constitution," 913.
[114] The exceptions are Alaska, Connecticut, Illinois, Kansas, and Vermont. South Dakota has a state credit clause, but it permits lending of credit with a supermajority of the legislature.

prohibiting stock subscription in and joint ownership of private ventures;. and 29 have a gift clause prohibiting expenditures of public money for which the government fails to receive anything valuable (i.e., consideration) in exchange, rendering the expenditure a mere gratuity.

Because individual anti-aid provisions are, as Pinsky puts it, a product of “specific evils which had manifested themselves” in the different states during the industrial expansion of the 19th century, some state constitutions forbid only one form of public aid, while others forbid two or all three.[115] Likewise, some anti-aid provisions apply to the state, others apply to political subdivisions of the state, and some apply to both levels of government. In addition, some anti-aid limitations are contained within a single clause, while others are found in two or more separate clauses.

115 Pinsky, “State Constitutional Limitations,” 280.

Figure 3. The Current State of Anti-Aid Provisions



Source: Authors' research.

Nine state constitutions expressly prohibit both levels of government from aiding private entities in any of the three forms discussed above.[116] For example, Arizona's anti-aid provision provides:

> Neither the state, nor any county, city, town, municipality, or other subdivision of the state shall ever give or loan its credit in the aid of, or make any donation or grant, by subsidy or otherwise, to any individual, association, or corporation, or become a subscriber to, or a shareholder in, any company or corporation, or become a joint owner with any person, company, or corporation, except as to such ownerships as may accrue to the state by operation or provision of law or as authorized by law solely for investment of the monies in the various funds of the state.[117]

Arizona's anti-aid clause is textually stronger than provisions in most other states because it applies to both levels of government, prohibits all three forms of aid, and allows only two exceptions, both related to legitimate government functions.[118] Most of the other nine constitutions that prohibit all three forms of aid at both levels of government also contain textual exceptions (e.g., Oklahoma and Wyoming permit support for economic development).[119]

In comparison, anti-aid provisions in 36 states likewise have various textual exceptions but either fail to address both levels of government or fail to limit all three forms of public aid. Other provisions contain few exceptions, apply to both levels of government, and prohibit more than one form of public aid. Logically, those that contain fewer textual exceptions, address more varieties of aid, and apply to both levels of government tend to be stronger. Most anti-aid provisions fall somewhere in between.

---

116 These are Arizona, Colorado, Florida, Kentucky, Louisiana, Montana, North Dakota, Oklahoma, and Wyoming.

117 Ariz. Const. art. 9, § 7. The exception at the end of the clause is meant to permit state investment of public funds, such as pension funds or rainy day funds. Ideally, these funds will have their own statutory restraints that require the fund managers to be fiduciaries so that investments are made in the public's interest and not in anyone's private interest.

118 However, Arizona amended its constitution in 1940 to exempt "irrigation, power, electrical, agricultural improvement, drainage, and flood control districts, and tax levying public improvement districts" from the anti-aid provision. See Ariz. Const. art. 13, § 7.

119 Okla. Const. art. 10, § 15(B); Wyo. Const. art. 16, § 12.

Despite being weakened by textual exceptions and gutted by judicial interpretation, anti-aid provisions have recovered some of their former strength in a few states, and this jurisprudence provides hope for resuscitating failed provisions in other states. For example, Arizona's seminal gift clause case, *Turken v. Gordon*, clarified that public purpose alone cannot justify an expenditure of public money that benefits private interests; instead, the government must receive something sufficiently valuable in return for the expenditure (i.e., it must obtain consideration).[120] If the government receives consideration that is "grossly disproportionate" to what it spent (i.e., if it spends a lot of money but gets very little or nothing in return), the expenditure is an illegal subsidy.

Even better, the court found that *indirect* benefits—such as anticipated tax revenue and employment opportunities for city residents—are not valid consideration if private entities are not contractually required to provide these benefits.[121] Thus, in Arizona, public expenditures for economic development are unconstitutional unless the government receives valuable and direct (arising from the private entity's obligation) consideration in return for the expenditure. Before the *Turken* case, government bodies had successfully argued that indirect public benefits resulting from an expenditure suffice to justify public aid to private interests.[122] This argument is especially problematic given the tendency of policymakers to rely on the indirect gross multipliers associated with new economic activity, which they often overestimate, while ignoring the negative effects of the taxes that pay for these subsidies. *Turken*'s rejection of that overly lax theory illustrates that it is possible—with strategically litigated cases—to realign anti-aid

[120] Turken v. Gordon, 223 Ariz. 342, 348 (2010) (holding that consideration cannot be "grossly disproportionate to what is received in return").
[121] *Turken,* 350.
[122] *Turken*, 351–52.

jurisprudence with the intended purpose of these provisions. In short, it is possible to prevent the application of public money to private purposes.

Other states with relatively strong anti-aid provisions also require that government bodies receive a fair return for an expenditure of public funds. In Oklahoma, economic development has a public purpose only if the government receives adequate consideration for the expenditure and there is accountability or control over the expenditure.[123] And in Mississippi, the state supreme court recently, and without discussing public purpose, held that a city cannot lawfully pay the attorney fees of a mayoral candidate in an election contest because the expenditure lacks consideration and is therefore a donation or gratuity to the candidate.[124]

Some state courts have created tests that strengthen anti-aid clauses. In those states where courts have not already adopted these tests, state legislatures can strengthen their anti-aid clauses by explicitly requiring courts to do so. To prevent the enrichment of private interests at public expense, three criteria should be satisfied for every expenditure of public funds:

1) The public expenditure should be primarily for a public purpose.
2) The government should maintain sufficient control over the expenditure to ensure its public purpose is accomplished.
3) The public should receive direct, ascertainable, obligatory, and proportional consideration for every outlay of public resources.

As noted, these requirements should apply to both the state government and political subdivisions and prohibit all three varieties of aid (gifts, stocks, and credit). Additional safeguards can also ensure that the provisions are as widely applicable as possible by including revenue bonds, industrial development bonds, and special districts.

[123] Burkhardt v. City of Enid, 771 P.2d 608, 611 (Okla. 1989).
[124] McAdams v. Perkins, 204 So. 3d 1257, 1265 (Miss. 2016).

VII. Conclusion

Economic development subsidies do not work as advertised. Both economic theory and experience suggest that, on net, subsidies are more likely to undermine than enhance a region's economic development. There are a number of reasons for this. Among other things, firms tend to collect subsidies for doing what they would have done anyway, subsidies involve significant opportunity costs, and subsidies invite a host of economic problems, including rent-seeking losses and anticompetitive effects.

Despite the problems with subsidies, the incentive for policymakers to dispense them is strong. Consequently, state policymakers have periodically attempted to bind their own hands by outlawing subsidies through various constitutional anti-aid provisions. Our review suggests that anti-aid provisions can affect the size and scope of subsidies, reducing their negative economic and social effects. But the details matter, and some provisions are stronger than others. Moreover, these provisions must be strengthened periodically.

The strongest anti-aid provisions apply to both state and local governments and restrict government extensions of credit, stock puchases, and gifts. These provisions are more effective if courts apply three tests. First, courts should require public expenditures to primarly serve public purposes. Second, they should require the government to maintain sufficient control over expenditures to ensure their public purpose is accomplished. And third, they should ensure that the public has received direct, ascertainable, obligatory, and proportional consideration in return for expenditures. Anti-aid clause litigation is most likely to be successful in states where these tests, or portions of them, are applied. And in states where courts do not currently apply these tests, legislators can strengthen statutory restraints by requiring that all public expenditures satisfy these criteria.