

SUBJECT: Appropriating \$3.1 billion from the rainy day fund for fiscal 2011

COMMITTEE: Appropriations — committee substitute recommended

VOTE: 27 ayes — Pitts, Turner, Aycock, Button, Chisum, Crownover, Darby, Dukes, Eiland, Giddings, Gooden, Hochberg, Johnson, S. King, Margo, Martinez, McClendon, D. Miller, Morrison, Otto, Patrick, Riddle, Schwertner, Shelton, Torres, Villarreal, Zerwas

0 nays

WITNESSES: None

BACKGROUND: Art. 3, sec. 49-g of the Texas Constitution establishes the Economic Stabilization Fund, which was ratified by voters in 1988. The fund, also known as the rainy day fund, receives 75 percent of any oil or natural gas production tax revenue that exceeds the amount collected in fiscal 1987. Additionally, the comptroller must transfer one-half of any unencumbered balance remaining in the General Revenue Fund at the end of a biennium to the rainy day fund.

Money in the rainy day fund may be spent only with legislative approval. Subject to various limitations, approval by at least three-fifths of the members present in each house is required for spending from the fund that does not exceed the amount of any unanticipated deficit or revenue decline during a biennium. However, any amount from the fund may be spent for any purpose if at least two-thirds of the members present in each house approve it.

According to the comptroller, the rainy day fund will reach \$8.2 billion by the end of fiscal 2010-11 and is estimated to have \$9.4 billion by the end of fiscal 2012-13.

DIGEST: CSHB 275 would appropriate \$3.1 billion from the rainy day fund and deposit it in the General Revenue Fund for use during fiscal 2011. The funds would be available for general revenue expenditures already authorized by the general appropriations act enacted by the 81st Legislature.

CSHB 275 would take effect only if finally passed by a three-fifths record vote of the members present in each house and subject to the comptroller's certification.

The bill would take immediate effect.

**SUPPORTERS
SAY:**

CSHB 275 would help balance the fiscal 2010-11 budget by making a necessary and responsible transfer from the rainy day fund into the general revenue fund. In January, the comptroller projected that fiscal 2010-11 would end with a negative balance of \$4.3 billion. Under the Texas Constitution, this negative balance must be eliminated for the comptroller to certify a balanced budget for the next biennium. Unless the Legislature directly addresses this shortfall, billions of dollars from fiscal 2012-13 will have to be used to cover the shortfall in fiscal 2011. CSHB 275, along with the cuts made by CSHB 4 by Pitts, the supplemental appropriations bill also on today's calendar, would address the shortfall in this fiscal year rather than use the next biennium's tax revenues to pay the current one's debts.

CSHB 275 would work in tandem with the substantial spending cuts in CSHB 4 to help close the revenue shortfall in fiscal 2011. It would tap the fund for the bare minimum needed to cover the current shortfall. It would not authorize use of the rainy day fund for any new spending, either for the remainder of fiscal 2011 or in fiscal 2012-13.

The rainy day fund was created to stabilize wide fluctuations in state revenue that occur as part of the cycle of economic expansion and contraction. Designed to save money for when state revenues falter, the goal of the fund at its creation was to cover budget deficits.

The Legislature cannot pay off fiscal 2010-11's debts through cuts alone. The state must pay off its tax revenue anticipation notes (TRANs) in a timely manner. Texas takes out TRANs for cash flow purposes and must repay them by the end of the fiscal year in August. If Texas failed to make timely payments, its debt rating could be downgraded. The comptroller has publicly stated that she will pay off the TRANs when they come due. She is authorized to borrow temporarily from the rainy day fund without legislative authorization to repay these notes, though she is required to pay the fund back, with interest, by the end of the fiscal year. However, the state does not have enough money in its treasury to pay back the rainy day

fund under this scenario. This failure to repay also could negatively affect the state's credit rating.

Deferring state-obligated payments from this fiscal year into the next would not actually resolve the deficit, but it would shift significant costs to the next budget. Using a combination of cuts and the rainy day fund to close the deficit is the best solution to the fiscal 2011 shortfall.

Using the rainy day fund to close the revenue shortfall in fiscal 2011 would be responsible. In the past, the fund has been used to address both revenue shortfalls and spending on future projects for the next biennium, including schools, prisons, Medicaid, Children's Health Insurance Program (CHIP), and the creation of the Texas Enterprise Fund. CSHB 275 would not authorize any new spending and or dedicate funds for the next biennium.

CSHB 275 would use only part of the rainy day fund, not all of it, and that limited use would not affect the state's credit rating. Credit rating agencies have consistently praised Texas' wisdom in establishing and maintaining a rainy day fund. Having a rainy day fund reflects positively on the state's credit rating because it allows Texas to respond quickly to budget shortfalls. In 2003 and 2005, the Legislature used almost all of the rainy day fund with no adverse effect on its bond rating. In 2007, Minnesota, North Carolina, and South Carolina spent their entire rainy day funds and did not lose their AAA ratings, the highest rating possible. These funds exist to be used. Credit rating agencies acknowledge this and expect funds to be used when needed to ensure that a state meets its obligations. CSHB 275 would represent such a use.

While it is prudent to prepare for an uncertain future, the Legislature should spend from the rainy day fund now to mitigate decreased tax revenues and protect the economy. If the Legislature did not use some of the rainy day fund to help pay for state expenses, the state would be forced to resort to layoffs and service reductions, which could significantly hamper the economic recovery. If the Legislature appropriated from the rainy day fund now and the economy did not recover or entered another recession, the Legislature could always make additional cuts to state spending in the future.

Appropriating funds from the rainy day fund would not be a tax increase. The money in the fund comes from taxes that have already been paid by

the oil and gas industry. Using them now would not negatively impact Texas taxpayers or the nascent economic recovery.

It is not necessary to save the rainy day fund for a natural disaster. Most of the damage that a natural disaster might inflict on the public sector would be to local governments, which are insured against losses like hurricane-related wind damage where appropriate.

OPPONENTS
SAY:

While the current budget shortfall and the recent recession meet the technical criteria for using the rainy day fund, that does not mean the Legislature should do so. The Legislature should not tap the rainy day fund until it has first exhausted all other efforts to find available funds or has cut unessential services. The current state budget spends heavily on unessential items such as the Arts and Historical Commissions, subsidies for films and Formula One racing, and economic development funds. Further, the state has yet to adopt money-saving options that other states have used successfully, including furloughing state employees or implementing four-day school weeks and four-day work weeks for government employees.

The Legislature should not use the rainy day fund to cover recurring expenses. The state needs a permanent solution to its ongoing budget deficit. According to some experts, there currently is a \$10 billion gap between the 2006 property tax reductions and revenue from taxes such as the business margins tax that were meant to offset those reductions. Until state leaders address this deficit, they should not paper over it by tapping the rainy day fund. A basic principle of sound financial planning is not to use savings to cover recurring expenses, and the Legislature should not do so here without first addressing the causes of the long-term structural deficit.

Current potential uses of the rainy day fund should not be compared with past uses. Prior appropriations from the fund were made when it was clear that the recession at the time was ending or had ended. It is not at all clear that Texas' economy has safely exited the recession. As such, Texas should save as much of the rainy day fund as possible in case the economy re-enters a recession and state tax revenue declines further.

Every dollar spent from the rainy day fund is a dollar the Legislature will not be able to spend to address future needs. The state's financial condition may be worse during the next few budget periods. Medicaid and

other costs will consume an ever-larger share of the state budget. Unpredictable costs also may increase. Texas also may need to use the rainy day fund to mitigate natural disasters such as the hurricanes that strike every few years.

Drawing down the rainy day fund could negatively affect the state's credit rating. Texas enjoys a good credit rating because it maintains a healthy and well-designed rainy day fund. Creditors rest easy knowing that Texas has a reserve fund with a large balance and can respond quickly to shortfalls and other emergencies.

OTHER
OPPONENTS
SAY:

CSHB 275 would not spend enough of the rainy day fund during the current biennium. According to the Henry J. Kaiser Family Foundation, Texas ranks near the bottom of the country (47th) in per-capita state spending. The Legislature should use more of the rainy day fund to shore up existing critical programs upon which the citizens and businesses of Texas rely every day.

State agencies were asked by state leaders to make 5-percent cuts to their budgets in January 2010 and to make further 2.5-percent cuts in December 2010. CSHB 275 should tap more of the rainy day fund in order to avoid making most or all of the additional 2.5-percent cuts contained in CSHB 4. These cuts are not insignificant and are in addition to earlier cuts made to an already anemic state budget.

NOTES:

The committee substitute differs from the original version of the bill as filed by appropriating \$3.1 billion from the rainy day fund instead of \$4.3 billion.

CSHB 4 by Pitts, also on today's calendar, would make supplemental appropriations of \$648.4 million in all funds and reductions of \$1.5 billion in all funds for fiscal 2011, a net decrease of \$853.6 million.