



The Associated Press, May 19, 2008

States debate whether to dip into their rainy day funds

By Andrew Welsh-Huggins

Lawmakers around the country are engaging in a tricky bit of economic forecasting these days, trying to figure out whether — or when — to tap into their states' rainy day funds.

The calculation involves deciding if it is better to raid the fund for fiscal emergencies now or to wait, in case the economic slowdown worsens and the need for revenue becomes more desperate.

Already, Arizona lawmakers dealt with a \$1.2 billion shortfall for this fiscal year, which ends in most states on June 30, by spending more than two-thirds of the state's rainy day reserve.

In Virginia, House Republicans opposed Democratic Gov. Tim Kaine's proposal to use \$423 million of the state's rainy day fund to close a projected revenue gap in the current fiscal year. They relented and agreed to a compromise of about \$352 million.

In Tennessee, Gov. Phil Bredesen is resisting similar calls to tap that state's reserves to fix its deficit.

"Early on in any recession, which is where we are now, is not the time to start diving into the savings account," Bredesen said.

States generally try to maintain reserves of at least 5 percent of their budgets to protect their credit rating. The decisions that trigger the use of rainy day funds vary from state to state and, of course, involve politics as well as economics.

Governors and lawmakers tend to be reluctant to dip into the funds out of fear that, without the cushion, unpopular tax increases aren't far behind.

But officials also see draining rainy day funds as more politically popular than cutting health care programs or school funding, or raising the dreaded "t" word.

A National Conference of State Legislatures survey conducted last month found several states — including Alabama, Massachusetts and Minnesota — plan to tap their rainy day funds to close budget gaps in the year beginning July 1.

The decisions are being made amid an anemic economy that is hitting states hard. Earlier this month, the Rockefeller Institute of Government reported that state sales tax revenue delivered the weakest performance in six years during the first quarter of 2008.

In April, the NCSL said the finances of many states have deteriorated so badly that they appear to be in a recession, regardless of whether that is true for the nation as a whole.

Such dire news is one reason some states are holding off raiding their reserves.

"They're worried that, as bad as it might be, it might get worse," said Scott Pattison, executive director of the National Association of State Budget Officers.

Complicating matters, states tend to lag behind the nation when it comes to recovering from a downturn.

"You start picking up on your income and even your sales tax, but then you get hit with the Medicaid caseload growth," said Ray Scheppach, executive director of the National Governors' Association.

Rainy day funds were relatively healthy at the end of 2001, even after a recession and the shock of the Sept. 11 attacks. Over the following two years, however, the funds plummeted as cash-starved states looked for help.

State coffers have since been refilled, hitting a historic high in 2006, when states reported \$69 billion in their reserves, including rainy day funds, or 12 percent of total revenue. That figure will drop to about \$46 billion, or 7 percent, by June 30, the end of the business year for most states, according to the NASBO.

States worry about the effect on their credit ratings if the funds dip too low. But one fiscal group says states should not hesitate if they are needy.

“Having a rainy day fund and not using it is the same as not having a rainy day fund at all,” said Liz McNichol of the Washington-based Center on Budget and Policy Priorities.

At first, Nevada hoped to avoid tapping its fund by making changes to one-time spending. As the downturn continued, the state opted to draw from the fund to avoid layoffs and cuts in essential government services, said Gov. Jim Gibbons, a Republican.

“The decision to tap into your savings account is always a very difficult decision simply because it

is taking your economic cushion, your safety net out, and putting it into the budget process,” Gibbons said.

In Ohio, Democratic Gov. Ted Strickland ordered spending cuts of more than \$700 million to fill a budget hole rather than use the rainy day fund, which was drained in the previous recession under a Republican administration. Strickland said he would consider the fund if things got worse.

But in Tennessee, Bredesen, a fellow Democrat, is holding firm, even as the state saw its worst month of collections in April in 40 years. In response, Bredesen has proposed \$468 million in new cuts and the elimination of up to 2,000 state jobs.

“This recession is still very early. I don’t know how deep it will be,” he said. “What I’m trying to do is keep us structurally in balance here and keep those rainy day funds aside to give us some protection if things were to get much worse.”