



# Testimony

## Simplify Texas's Rainy Day Fund

### *Testimony submitted to the Texas House Committee on Appropriations*

by Vance Ginn, PhD, Senior Economist

Chairman Capriglione and Members of the Committee:

My name is Dr. Vance Ginn, and I am chief economist at the Texas Public Policy Foundation. I am submitting this written testimony in response to [Charge 7](#) of the interim charges considered by this committee. I provide background on the state's Economic Stabilization Fund, also known as the "rainy day fund," and highlight the need for structural reforms to simplify its use so that money is there to cover tax receipt shortfalls while upholding a high credit rating by external agencies.

### Background on Texas's Rainy Day Fund

Production of crude oil and natural gas has historically fluctuated based on many market-driven and geopolitical factors. Because the Texas Legislature collects severance taxes from this volatile production to primarily fund the state's rainy day fund, the purpose for and use of the ESF must be worthy.

Texas voters approved the ESF with passage of a constitutional amendment in [1988](#) after an uncertain state tax receipts period when oil and gas comprised a large share of economic output and was highly volatile in the 1970s and 1980s. The ballot language that Texans approved was "The constitutional amendment establishing an economic stabilization fund in the state treasury to be used to offset unforeseen shortfalls in revenue." The Texas [Constitution](#) requires a three-fifths vote in each house to close a revenue shortfall and a two-thirds vote in each house to use it for other reasons.

Since its inception, deposits to the fund have totaled [\\$21.8 billion](#). While there have been many proposed uses for the money in the rainy day fund, the ballot language sold to Texas is clear that this money is to fill unexpected tax receipt declines. All told, only 27.4%, or \$3.2 billion, of the \$11.6 billion spent from the fund since its inception has been for general deficit reduction. In 2019, the Legislature appropriated [\\$4.9 billion](#) from the ESF for the 2019 fiscal year supplemental budget to help pay for expenditures such as ongoing Hurricane Harvey related relief and an additional [\\$1.2 billion](#) for the 2020-21 biennium. Clearly, a more stringent use of these funds outside of the intended purpose is warranted. In addition, the current economic slowdown as a result of the COVID-19 pandemic and a significant drop in the demand for oil and subsequently a decline in its price will likely reduce expected deposits into the rainy day fund.

Despite these uses of severance taxes for one-time and ongoing expenditures and the anticipated drop in deposits, the rainy day fund's balance is expected to be [\\$8.9 billion](#) at the end of the 2020-21 budget cycle. Given the fund's constitutional limit of 10% of general revenue (GR)-related funds excluding interest and investment income in the previous budget cycle, the cap this period is [\\$16.9 billion](#).

### Simplifying the Uses of the Fund

The cap of 10% on biennial GR-related funds is a 20% annual cap. Every dollar not in the private sector without a clear purpose is wasting potential productivity that could help Texans prosper, so these dollars should be used wisely and not be excessively collected. Moreover, the state's economy, and therefore tax revenue, is much less reliant on oil and gas activity as previously experienced. [Research](#) shows that Texas could have a biennial cap closer to 7%, or annually 14%, to cover the most severe fiscal downturns, which should primarily be solved with spending restraint. Alternatively, if this money is spent each session, the fund will quickly dwindle, and the state's credit rating could be at risk.

There will likely be interest in tapping the rainy day fund in 2021 if the expected drop in revenue materializes and more demands are put on the budget. Any use of these one-time funds to pay for ongoing expenditures only delays needed

*continued*

difficult decisions that should be made with general revenue funds and depletes one-time funds available for tax receipt shortfalls, future emergencies, or tax relief. In addition, using money from the fund for investment purposes that could support a higher rate of return to support unfunded state liabilities without considering major structural reforms to pensions and reductions to debt first is not warranted.

## The Facts

- The rainy day fund is expected to increase to \$8.9 billion by the end of FY 2021.
- Using one-time funds to pay for ongoing expenses is poor public policy.

## Recommendations

- Increase the threshold to use money in the fund “at any time and for any purpose” from the current two-thirds of members present to four-fifths of all members in each chamber.
- Lower the constitutional cap from 10% to 7% of biennial GR-related funds in the previous biennium.
- Use excess state tax receipts above the fund’s cap or from budget reductions to cut taxes instead of spending or investing them in riskier assets and growing the budget without reforms.

Thank you for your time in considering these key reforms to simplify the rainy day fund so that taxpayer dollars are used sparingly and wisely while keeping a high credit rating by external agencies. Thank you for the work you do, and I look forward to continuing the discussion on this topic. ★

## Resources

[\*Don't Grow Government with the Texas Rainy Day Fund\*](#), by Vance Ginn, Texas Public Policy Foundation (April 2019).

[\*Fiscal Size Up 2020-2021 Biennium\*](#), Legislative Budget Board (May 2020).

[\*Economic Stabilization Fund Overview\*](#), Legislative Budget Board (Jan. 2019).

[\*Leaky Umbrella: The Need to Reform Texas' Rainy Day Fund\*](#) by Vance Ginn, Talmadge Heflin, and Owen Smitherman, Texas Public Policy Foundation (Oct. 2016).

## ABOUT THE AUTHOR



**Vance Ginn, PhD**, is chief economist at the Texas Public Policy Foundation, a 501(c)(3) non-profit, non-partisan free market think tank based in Austin. He is the former associate director of economic policy for the Office of Management and Budget at the Executive Office of the President, former college lecturer, and an expert on economic and fiscal issues with research that seeks opportunities to let people prosper in Texas, D.C., and beyond. He earned his doctorate in economics at Texas Tech University.

## About Texas Public Policy Foundation

The Texas Public Policy Foundation is a 501(c)3 non-profit, non-partisan research institute. The Foundation promotes and defends liberty, personal responsibility, and free enterprise in Texas and the nation by educating and affecting policymakers and the Texas public policy debate with academically sound research and outreach.

Funded by thousands of individuals, foundations, and corporations, the Foundation does not accept government funds or contributions to influence the outcomes of its research.

The public is demanding a different direction for their government, and the Texas Public Policy Foundation is providing the ideas that enable policymakers to chart that new course.

