Center for Public Policy Priorities

Policy Page

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RECOVERY ACT STATE BUDGET UPDATE

The American Recovery and Reinvestment Act (ARRA) is making a vital difference in Texas. Potentially injecting as much as $38 billion into the state economy, ARRA temporarily increases grants to federal, state, or local government agencies while providing tax cuts or tax credits to families and businesses. This *Policy Page* discusses the importance of the ARRA funds in the Texas state budget for 2010-11—the budget cycle that begins on September 1—and related developments.

- **ARRA funds in the 2010-11 Texas budget helped avoid or reduce cuts in Medicaid, other health care programs, and pre-K-12 public education.**
- **ARRA funds also are temporarily increasing state spending on highways, child care, job training and employment services, energy, housing, water/wastewater projects, and other improvements.**
- **A recent NCSL report identifies Texas as the state that most heavily relied on ARRA to close fiscal 2010 budget gaps.**
- **ARRA helped the Texas legislature write a balanced budget for 2010-11, but tough fiscal challenges loom in the coming biennium and in the next legislative session.**

ARRA in the Texas State Budget

About $16 billion of Texas' Recovery Act funding had to be appropriated by the legislature through the state budget or required the legislature to change state law. For example, Texas' receipt of $555 million was contingent on modernizing the state's Unemployment Insurance system.

In the 81st Regular Session, Texas legislators appropriated $14.4 billion of ARRA funds through the 2009 supplemental spending bill (H.B. 4586) and the general appropriations act for 2010-11 (S.B. 1, Article XII). Of this $14.4 billion, 56 percent will be used for Medicaid and public education to avoid or reduce cuts by taking the place of General Revenue that would otherwise have been needed for those areas. The other 44 percent, or $6.3 billion, will pay for highways, child care, Workforce Investment Act services (or additional job training), energy programs, housing, water/wastewater projects, and other improvements. Some of these, particularly job training, energy conservation, and housing, are areas of the budget in which Texas has not traditionally invested much General Revenue. Higher funding levels for these areas will cease once ARRA funds are exhausted. Most of the ARRA funds will be distributed to state agencies—and in some cases to local governments such as school districts, cities, and counties—through existing formulas.

ARRA Helped Prevent Cuts

Without ARRA funds to the states, Texas would probably have used some of its Rainy Day Fund to cover some of the General Revenue lost to the economic recession, but not all of it. Instead, without ARRA funds, the Texas budget would have made larger cuts to Medicaid and education than it did, and improvements such as the teacher pay raise would not have been funded.

A recent report by the National Conference of State Legislatures identifies Texas as the state that relied most heavily on federal ARRA funds to close its fiscal 2010 budget gap. NCSL's report covers information from 35 states on ARRA uses. Twenty-five reporting states said they used ARRA to help close gaps, and Texas closed an estimated 96.7 percent of its fiscal 2010 budget gap with federal funds.

The NCSL report warns that, even though many states managed to write balanced budgets for 2010—using a combination of ARRA funds, budget cuts, tax and fee increases and one-time revenue such as Rainy Day Funds or accounting gimmicks—new and large budget gaps could open up once the fiscal year starts, if revenues turn out to be lower than forecast, or costs exceed state budget assumptions. Many states also expect large budget deficits for 2011 and 2012. A more recent report by the Center on Budget and Policy Priorities echoes the NCSL's grim budget scenarios: combined state budget shortfalls could be as large as 24 percent of general spending in 2010, and 15 percent in 2011.

Texas Revenue Developments

Revenue shortfalls are a very real possibility in Texas, where the sales tax has been performing below the January 2009 forecast. In addition to reducing the ending balance for 2009, lower-than-forecast sales and other tax collections could require legislators meeting in 2011 to use Texas' $9 billion Rainy Day Fund for 2010-11 budget needs, rather than saving it all for 2012-13. This would make writing the 2012-13 budget even more difficult, as state officials who submitted the Texas information to the NCSL survey indicated that "For [Fiscal Year] 2012, a structural gap of $4 billion to $5 billion a year is expected based on current spending levels (without ARRA) and revenue levels." This translates to an 8 percent General Revenue gap between anticipated spending and revenue.

One positive development: the Texas Medicaid budget for 2010-11 may not have as large of a shortfall as originally expected. On August 12, the Health and Human Services Commission informed a state legislative committee that if unemployment rates exceed budget assumptions, an additional $474 million in federal ARRA funds could be available to help fund health care for the almost 2.8 million Texans on Medicaid.

Conclusion

ARRA has been a critical lifeline for Texas state services. Due to this important piece of federal assistance, our state has been able to maintain Medicaid and other programs along with pre- and K-12 education. The act also allowed a temporary injection of funds into public structures including highways, child care, job training, employment services, and others. The fact that Texas relied most heavily on ARRA funds to close budget gaps, however, should alert state policymakers to the pressing need to find other ways to adequately fund public structures once ARRA funds expire. Unless we shore up state revenue, Texas faces deep cuts in 2011.