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Data Analysis: State Rainy Day Fund Balances Over Time

Introduction

Before the COVID-19 crisis, state rainy day funds and total balances were at an all-time high, after a decade of rebuilding reserves following the Great Recession. In spring 2020, when the pandemic first hit, this financial cushion softened the immediate blow for states facing revenue shortfalls and helped them to close budget deficits by the end of the fiscal year – something most states are required by law to do. At the same time, as state revenue projections were plummeting further, concerns grew that states might end up depleting the rainy day funds they had worked so hard to build in recent years.

As it turns out, these concerns did not come to pass, mainly because state revenues later performed considerably better than was expected early in the pandemic. This was driven by an influx of federal funds, higher-income workers being relatively insulated from the effects of the COVID-19 recession, the shifting of consumption from services to goods (more commonly taxed at the state level), and the expanded ability to tax online sales following the South Dakota v. Wayfair Supreme Court decision.

Now, nearly two years after the initial onset of the pandemic, state rainy day fund balances have reached new record levels. This is largely due to revenues exceeding lowered budget forecasts in the vast majority of states and increased federal aid, which led to substantial budget surpluses in some cases that were at least partly deposited into rainy day funds. However, it also has a lot to do with deliberate steps that states took in the years leading up to the pandemic to strengthen their reserves, informed by lessons learned from the Great Recession.

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