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LAO REPORT: GOVERNOR'S PROPOSAL "FALLS WELL SHORT"

Attached to this issue of the *California Budget Report* is the best available overview of the Governor's Budget. Regular readers will recall that the Legislative Analyst's Office provides one of the few neutral evaluations of the budget in almost-understandable language.

Here is a fast take on the LAO's key findings:

- The Governor's budget does not fully address the fiscal imbalance between spending and revenue.
- The Governor's revenue estimates are only slightly different from those of the LAO (only about \$260 million) and updated LAO estimates will be released in February.
- Although reductions in spending are proposed by the Governor, most of these are in the form of one-time loans or borrowing, pushing off a real solution until another year. Only half of the proposed savings are long-term.
- Most important, some of the proposed "reforms" of the budget process advocated by the Governor would make it more difficult to balance future budgets. Ironically, the Governor continues to advocate the automatic spending he decries, while also advocating automatic, across-the-board budget reductions.
- While recommending that the Legislature again, by a two-thirds vote, suspend the provisions of Proposition 98 in order to "save" \$2.2 billion, the Governor proposes that the Constitution be amended to remove the ability of future legislatures to ever again suspend the minimum funding requirement of Proposition 98!
- Virtually the same "use the money now, prohibit it later" policy is proposed for the state sales tax on gasoline, which under the provisions of Proposition 42 goes to transportation purposes—unless the Legislature agrees, by a two-thirds vote, to suspend the designation. The language allowing the Legislature to transfer these funds from transportation purposes to General Fund purposes was part of Proposition 42. The Governor proposes to prohibit the transfer of these funds away from transportation purposes after 2006, creating more automatic spending in the future.
- Although the details are not entirely clear, the Governor is also proposing to prohibit any internal borrowing from Special Funds in the event of other budget needs. Again, this will

lock in spending for designated purposes, regardless of the overall condition of the state budget.

We close this CBR with the most telling language in the LAO's report:

“One of the main concerns posed by this budget relates to its structural reform proposals. We strongly support the objectives of eliminating the state’s long-term structural problem, paying off its debts, and maintaining balanced budgets in the future. However, we believe that major proposals affecting future budgets— particularly the Proposition 98 and across-the-board reduction provisions—raise serious concerns.

*“First, they would dramatically reduce the ability of future policy makers to establish budget priorities, particularly during periods of revenue softness. For example, the proposed changes in Proposition 98 related to suspension and Test 3 would leave policy makers with limited discretion over the allocation of budget resources between Proposition 98 and other state programs. **During revenue downturns, the proposal would potentially shift all of the burden of balancing the budget on spending reductions in non-Proposition 98 programs (such as higher education, health, social services, and criminal justice)—or on taxpayers in the form of higher fees and taxes.** (Emphasis added) For example, if the state had not been able to suspend the minimum guarantee when the budget was enacted for 2004-05, school funding would have been required to increase by roughly \$4 billion (instead of the \$2 billion actually received), which would have necessitated either steeper reductions in other areas, more revenues, or additional borrowing.*

“Second, the proposed changes represent a serious diminution in the Legislature’s authority to appropriate funds and craft budgets. Under the State’s Constitution, only the Legislature can appropriate funds—and make mid-year reductions to those appropriations. Under the administration’s proposal, the Governor would have the authority to determine when the budget is not balanced, with the default being automatic across-the-board reductions to most state programs, without regard to program priorities.

“For these reasons, we believe the Legislature should carefully assess the administration’s proposals, starting with a clear understanding of the specific deficiencies in the budgetary process. For instance, the administration suggests that a key problem is that state spending is on autopilot. If the Legislature believes that this is the case, the solution would not be placing more spending on cruise control—as the administration is proposing for Proposition 98 and other areas of the budget. The solution would be to eliminate these types of provisions that limit the Legislature’s and Governor’s authority to make annual budgetary decisions. Similarly, the perceived deficiency may be that the recently enacted balanced-budget and mid-year correction provisions in Proposition 58 are not adequate to maintain fiscal balance. If so, there may be alternative proposals which strengthen the existing process while not diminishing the Legislature’s central authority in budgetary appropriations. (pp. 17-18)”

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