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# **CALIFORNIA BUDGET REPORT**

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*Volume 4, Number 8*

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***LAO MAKES BUDGET  
ALMOST UNDERSTANDABLE:  
  
SOME GOOD, SOME BAD IS THE  
DESCRIPTION,  
BUT A STRONG RECOMMENDATION  
TO BE MORE PRUDENT***

You can read the full report at [http://www.lao.ca.gov/2006/may\\_revise/may\\_revise\\_051506.pdf](http://www.lao.ca.gov/2006/may_revise/may_revise_051506.pdf) or, if you prefer, in html at [http://www.lao.ca.gov/2006/may\\_revise/may\\_revise\\_051506.html](http://www.lao.ca.gov/2006/may_revise/may_revise_051506.html). But either way, there are some big points the LAO wants us to understand.

**How the 'new revenue' is proposed to be spent**

First, look at Figure 1 (p. 4)

**Figure 1**  
**How May Revision Allocates \$7.5 Billion in Additional Revenues Since January**

(In Billions)

<b>New Resources</b>	
Revenue increase relative to January:	
2005-06	\$4.8
2006-07	2.7
<b>Total, New Resources</b>	<b>\$7.5</b>
<b>New Uses</b>	
<b>Spending on Current Programs</b>	
Proposition 98	\$2.9
Health care: disaster preparedness	0.4
Other health and social services	0.1
Corrections: inmate population and health care	0.5
Local government grants and reimbursements	0.1
Flood control	0.5
Other (net)	-0.2
Subtotal	(\$4.3)
<b>Prepayment of Budgetary Debt</b>	
Deficit financing bonds	\$1.0
Special fund loans	0.2
Proposition 98 settle-up payments	0.2
Local flood control subventions	0.1
Local mandates	0.1
Subtotal	(\$1.6)
<b>Increased Reserve</b>	<b>\$1.6</b>
<b>Total, New Uses</b>	<b>\$7.5</b>

What lessons might we learn from this chart?

1. There is about \$7.5 billion in “New Resources” according to the LAO. However, as we understand budgeting, “new” means this amount was not previously anticipated. “New” does not mean “we get the same amount of additional money each and every year into the future”.
2. The Governor has allocated the “new” resources as follows:

Spending on current programs	\$4.3 Billion	57%
Prepayment of Budget Debt	\$1.6 Billion	21%
Increase State Budget Reserve	\$1.6 Billion	21%
3. Although this increasingly looks like an easy budget year, there are always things left to be done. Increased demands for child health coverage money for the Democrats and money for dams and storage facilities for Republicans will get the budget juices flowing.

We predict the Legislature will a) jump on the LAO statement “We believe that there is upside revenue potential in 2006-07.....” (p. 8) and appropriate some additional money --- maybe \$300-\$700 million, and b) not tinker with the amount for prepayment of debt or increased budget reserve, but c) talk about a slight refocusing of how repayment of debts occurs, as the LAO suggested.

**A good summary of the Governor’s May Revision Highlights** (Figure 4, p. 9)

We also like this chart, which is a more balanced presentation of the main programmatic recommendations in the May Revision. Add to this discussion the previously-adopted 2006 bond package, plus the Governor’s debt repayment and increased budget reserve, and you have a good summary for your next speech to the local Rotary.

By the way, buried in the middle of the following chart is a small notation “Provides no funding for 2006-07 mandate claims”. This refers to the legally-required, and often ignored or long-delayed payment to local governments for state mandates. Even in a ‘prudent’ budget there is no end to small tricks used to cover up an operational deficit. This is one. Another spending program that gets hidden in the middle of larger budget issues is Proposition 49, the Schwarzenegger after school program, a precursor to his election in 2003.

**Figure 4**

### **Key Programmatic Features of May Revision**

#### **K-14 Education**

- Increases K-14 Proposition 98 funding beyond January proposal by \$2.1 billion in 2005-06 and \$800 million in 2006-07. K-12 per pupil funding would increase from slightly over \$7,400 in the 2005-06 Budget Act to nearly \$8,300 in 2006-07.
- Funds used for a variety of one-time and ongoing purposes. For K-12, these include increased spending for teachers' supplies, instructional materials and equipment, school counselors, a targeted preschool initiative, school library block grants, and ongoing increases to schools' discretionary funding. For community colleges, provides funding for deferred maintenance and a general-purpose block grant.
- Also includes proposed settlement to lawsuit related to \$2.9 billion in additional one-time Proposition 98 funding. Annual payments would be made over seven years, beginning in 2007-08.

#### **Health and Social Services**

- Provides \$400 million for hospitals and public health clinics to increase patient care capacity to meet public health emergencies.
- Drops January proposal to further delay "pass-through" of the federal January 2007 Supplemental Security Income/State Supplementary Program cost-of-living adjustment until July 1, 2008, resulting in lost savings of \$44 million.
- Provides targeted increases in areas of children's health care, child support payments, and child welfare services.

#### **Corrections**

- Includes increases of about \$500 million for additional inmate population and corrections-related health care costs.

#### **Local Government**

- Makes \$87 million prepayment of state's 2007-08 obligation for prior-year mandate costs.
- Provides no funding for 2006-07 mandate claims.
- Increases funding for the Citizens' Option for Public Safety (COPS) and Juvenile Justice Challenge Prevention Act programs by \$43 million, and provides \$40 million to new county trust funds for local detention facilities.

#### **Resources**

- Reflects \$500 million in funding for flood control provided in AB 142, (Nuñez).
- Makes \$100 million in additional payments for local flood control subventions, and includes various other one-time emergency funds for flooding earlier this year.

#### **Transportation**

- Retains January proposal to prepay \$920 million of Proposition 42 loan repayment due in 2007-08.
- Proposes that "Public Transportation Account spillover" funds (related to sales taxes on gasoline) be diverted from transit programs to debt-service payments on transportation-related general obligation bonds.

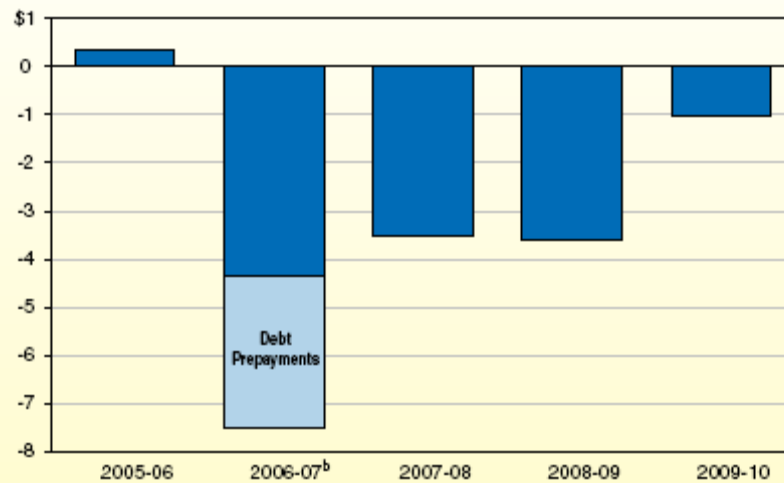
**It still looks like ongoing deficits, far into the future (Figure 10, p. 16)**

We wrap up this discussion with something that may need no mention. Even in this year, with all the 'new' money coming in, the state is still spending more than it brings in. There should be no surprise that this will continue for many years to come. Consider the final LAO chart we are sending.

Figure 10

### Operating Deficits<sup>a</sup> Persist Under May Revision

General Fund (In Billions)



<sup>a</sup> Annual revenues minus expenditures. Legislative Analyst's Office estimates of Governor's revenue and expenditure policies.

<sup>b</sup> 2006-07 operating deficit includes \$3.2 billion in prepayments of budgetary debt plus numerous other one-time expenditures.

Take a hard look at this chart. Remember, this is the optimistic description of future state operating deficits; based on the assumption that there are no new state programs adopted, nor unusual funding increases to current programs, and no new state tax cuts. The LAO also adds a warning that these calculations "...did not include the potential budget risks or pressures, including lawsuits, retiree health benefit liabilities, federal actions, and steeper-than-expected slow-downs in the economy." (p. 16).

We leave to a later *California Budget Report* our musings on just why this continues to happen. For now, let's hope that the Governor and legislators restrain their enthusiasm for spending more money than they have.

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