June 2009

Short-Term Budget Solutions for California

California stands on the precipice of destroying our safety net and putting our future prosperity in danger by cutting investments in education. This devastation is unwise and can be avoided with a combination of cuts, shared sacrifices and additional federal stimulus money, or, as a last resort, a temporary tax increase.

The key to getting started on a better path begins with understanding that, despite a lot of old myths about our budget problems, our current challenge is not our fault and state spending currently is not escalating out of control.

Some Budget Facts

The current budget challenge is 100% the result of the deepening national recession. Our current budget challenges are shared by many states and local governments throughout the nation. While California failed for many years to resolve our structural budget deficit and has no plan to close the gap for the future, we did our part for 2009-2010 back in February with more than $10 billion in spending cuts and more than $10 billion in temporary tax increases.

Moreover, when the 2009-2010 budget is adopted Californians will be spending the smallest share of our income on General Fund spending in the 30 years of the post-Proposition 13 era. The 2009-2010 spending level does not even keep pace with caseload and inflation growth over the past ten years. General Fund spending will rise 29% between the 2000 and 2010 budgets compared with a 53% increase in state population and consumer prices.

Finally, California ranks the 2nd lowest among states in state employees relative to population and 4th lowest when local government employees are included.

These key facts are documented at the end of this *Issues in the News*

Short-Term Budget Solutions

I encourage public sector employees, including those in local government and school districts, to take a temporary salary cut to save the jobs of their fellow public sector employees and to maintain public services as best we can. I do this with great respect for public sector employees and with the hope that President Obama's goal of higher pay for teachers can be reached. But, if the choice is between greater layoffs and a temporary pay cut, I think the model of shared sacrifice for the greater good adopted by the UAW is the way to go in California.

Budgets for health and social service budgets can be cut to the minimums required by law, but no further. Reforms in parole and sentencing for non-violent drug offenders can help reduce the prison budget. School districts should be allowed to spend categorical funding as they think best. Cutting K-12 funding to the Prop 98 minimum is a bad choice for our future but may be necessary.

But these steps are unlikely to balance the budget by themselves and certainly do not address the state's budget challenges after 2010.

There is a compelling case for additional **short-term** federal assistance. But it is a case for all states, not just California. On June 4th the National Governors Association and National Association of State Budget Officers reported "The 50 states are facing one of the worst fiscal periods in decades…states currently estimate that they will have faced $230 billion in reported budget deficits between fiscal 2009 and fiscal 2011."

We should join with governors and mayors in other states to remind the federal government of three key facts that support more stimulus aid to states.

First, states are tearing down their safety net programs at precisely the time when demand is growing rapidly. The Congress understood these rising safety net demands when they increased unemployment benefits and food stamps and offered to help unemployed workers with their health insurance.

Second, many states are now facing cuts in K-12 education and cuts in access to higher education. This comes right after President Obama said that increasing and reforming our investments in education and skill building is a national imperative for economic competitiveness.

Third, these programs provide valuable public services to local communities and the nation. The rationale that the public good requires maintaining continuity in the financial sector, for AIG and in the auto industry surely applies to preventing unwise cuts in education and the safety net.

It is time for a second stimulus package. We can start by using the TARP repayments from banks that will begin soon.

Republican gubernatorial candidate Tom Campbell recently suggested that another modest temporary tax increase is preferable to borrowing, gimmicks and even more drastic cuts to public services. I agree. If additional federal stimulus money is not forthcoming and the final choice is between hurting critical long-term investments and a temporary tax increase, our future should win that battle.

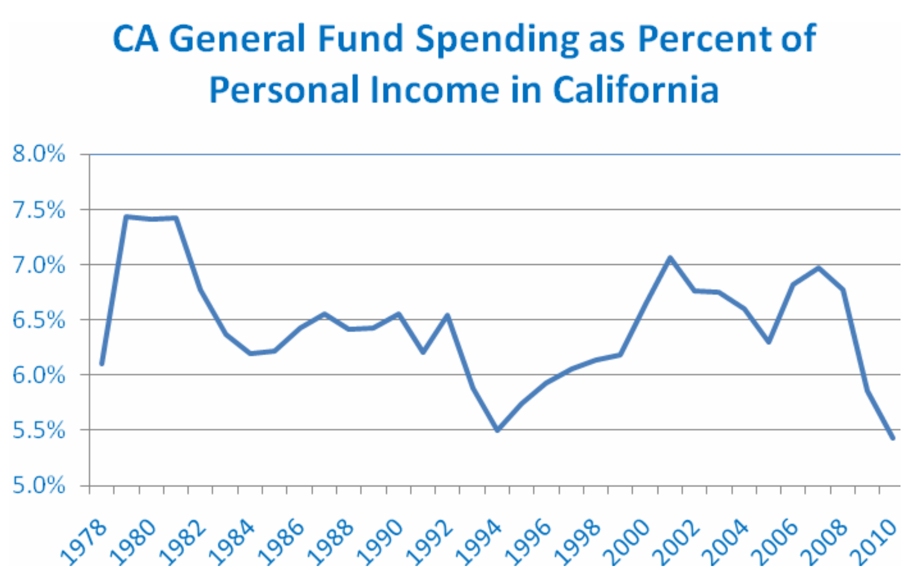
Longer-Term Budget Challenges

Addressing long-term budget balance will pose very difficult challenges. One immediate suggestion I have is for the governor to extend the term of the Commission on the 21st Century Economy and refocus their effort on longer-term revenue and budget challenges. A lot has changed since the commission goals were established. They are a great group of people and their ideas on the long term budget would be welcome.

Data for Key Budget Facts

The 1978-79 state budget was the first one after Proposition 13 when the state took over major funding responsibility for K-12 education. After that year the lowest share of personal income dedicated to General Fund spending was 5.5% in the 1994-95 budget year.

If General Fund spending for 2009-2010 is $85 billion as proposed in the May revise, that amount would represent 5.4% of the income of residents as forecast by the Department of Finance for 2010—the lowest share of personal income for General Fund spending since Proposition 13 was enacted. If General Fund spending is $90 billion, that would represent 5.8% of expected personal income. The historical data comes from Schedule 6 of the Governor's Budget released in January 2009.



There has been a lot of discussion about how recent state spending has surged far ahead of population and inflation growth. First, population and inflation is not a universally agreed upon standard for budget growth. The share of personal income spent on General Fund programs is the usual benchmark for whether state spending is growing in line with the economy or faster or slower. As shown above, the share of personal income in California allocated to General Fund spending in 2009-2010 is the lowest in the post-Proposition 13 era.

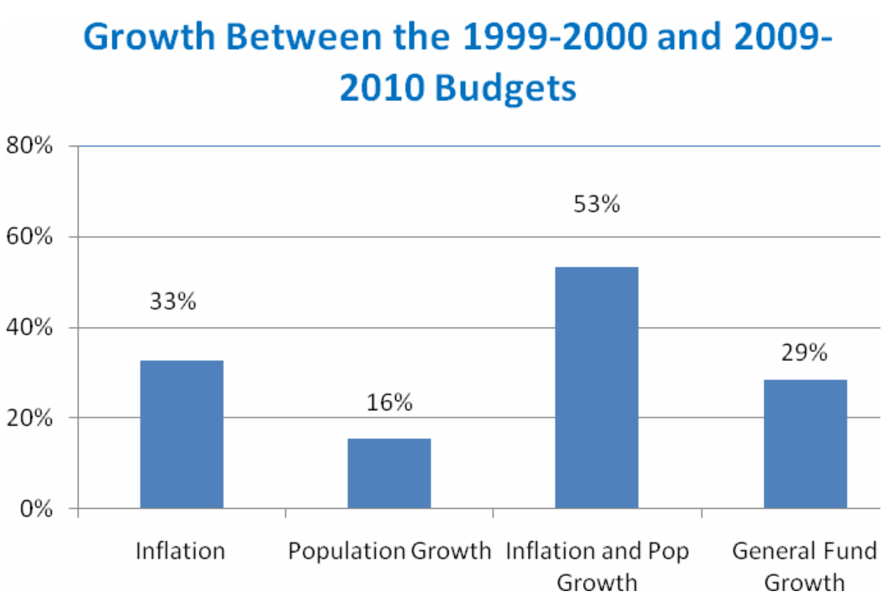
But even on the more restrictive criterion of population and inflation growth, the proposed 2009-2010 General Fund spending level falls far behind the increase in population and the Consumer Price Index over the past ten years.

State population growth was 16% between 1999 and 2009. The California Consumer Price Index rose by 33%. The combined effect of these two factors is a 53% increase—the math is that the increases are multiplied, not added. But the proposed 2009-2010 General Fund spending of just over $85 billion is only 29% above the $66.5 billion spent in the 1999-2000 budget.

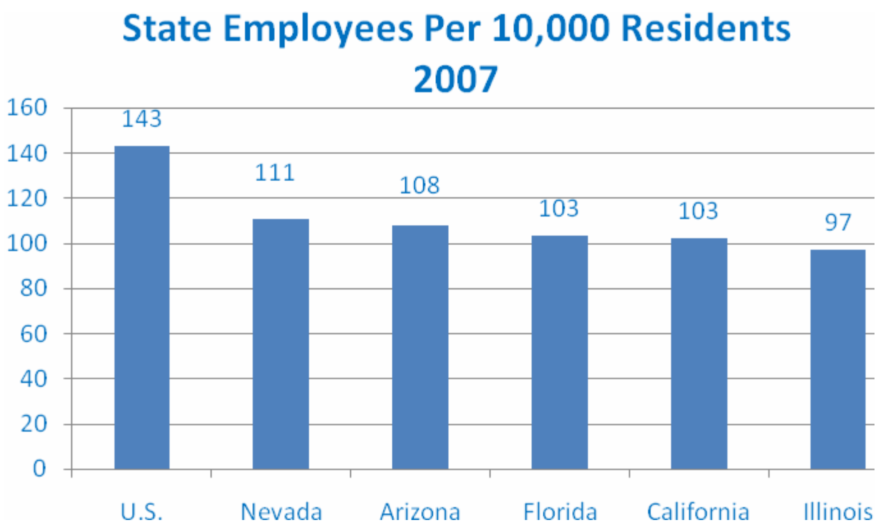
If General Fund spending reaches $90 billion in 2009-2010, that would still be only a 36% increase over ten years ago and if the General Fund spending reached $95 billion, that would result in a 44% ten-year gain, still far below population and inflation growth.

It is true that spending outpaced population growth and inflation between 2003 and 2007 but that is picking a very selective set of years. Recent budget cuts have pushed spending far below any possible criterion for reasonable budget growth in terms of caseload, inflation and keeping pace with the economy.

All of the data is from the California Department of Finance website.



California has the second lowest ratio of state employees to population among all states. In 2007, the latest year for which data was reported; California had 103 full-time equivalent state employees per 10,000 residents, second to Illinois with 97. The national average was 143 state employees per 10,000 residents.



California ranks 4th lowest among states for state and local government employees, including school districts, with 484 employees per 10,000 residents. The national average in 2007 was 544 state and local government employees per 10,000 residents.