



January 9, 2009

With a terse [message](#) Governor Schwarzenegger vetoed all 15 bills contained in the December 18<sup>th</sup> mid-year budget modification package, thus resuscitating the Williamson Act subventions and the rural crime program. The governor also issued an open [letter](#) to Senate pro Tem Darrell Steinberg and Assembly Speaker Karen Bass that provides further details on his reasoning.

So we are back to square one after two Special Sessions of the Legislature called to close the now \$15B revenue gap in the current budget year that is growing at a rate of \$40M per day according to the Department of Finance. The details of the stalemate have been well-covered elsewhere, but suffice it to say as the day of reckoning approaches (i.e., the day the State of California actually runs out of money to pay its bills, its employees, and income tax refunds) someone in this colossal game of chicken is going to have to blink. Although trite, it is all about the perceived challenges and opportunities for the parties involved. To the Republican members of the Legislature, the crisis is an opportunity to parlay their budget enactment power into long-term budget reforms, including a hard state spending cap tied to inflation and population growth and to leverage an economic stimulus package to create new jobs. Their challenge is to get their demands taken seriously and to eventually get their constituents to understand that some taxes will have to be raised. To Governor Schwarzenegger, it is an opportunity to raise revenue to avoid the state's fiscal collapse while extracting labor and environmental concessions to hopefully avoid future budget crises and to help pull the state out of its deep recession by fast-tracking much needed infrastructure projects. These projects would create jobs with borrowed bond funds and hopefully capture federal revenue under the highly anticipated Obama stimulus package. The governor's challenge is to find Republican votes for his proposed tax increases and Democrat votes to suspend CEQA for certain state projects. For the Democrats, it's mostly about challenges. There's no stomach for the Draconian cuts that would be necessary to address the greatest fiscal crisis in the state's history with an all cuts budget, and even less desire to budge on labor and CEQA issues due to the demands of their constituent base.

While the negotiations sputtered on the much-needed current year budget modifications, the governor's Department of Finance quietly released his [2009-10 General Fund Proposals](#) on New Year's Eve. The documents released on December 31<sup>st</sup> look more like a May Revision than a typical Governor's Budget Summary. But these are clearly atypical times and the governor's proposals are intended to address both the current year projected shortfall and the anticipated deficit in the coming budget year. Not surprisingly the governor is proposing deep cuts (\$17.4B) in all areas of the budget as well as raising \$14.3B in new revenues. His plan also includes \$10B in new borrowing almost equally split between securitization of future lottery proceeds, and short-term Revenue Anticipation Warrants (RAWs). Several aspects of the governor's proposals would require voter approval, including borrowing against the future lottery revenue, modifying Proposition 10 relating to early childhood development programs and Proposition 63 that provided increased funding for mental health programs so the state can transfer their dedicated revenue.

The Legislative Analyst's Office (LAO) weighed-in on the governor's 2009-10 spending plan with its traditional [overview](#) and generally gave it high marks with the notable exception of its heavy reliance of future borrowing. The LAO raised questions regarding the need to overcome the worldwide turmoil in the credit market, obtain voter approval for the lottery measure, and to overcome legal questions about shifting funds from Propositions 10 and 63. Then there is the prospect of issuing billions of more dollars in RAWs to investors unsure about fiscal viability of the State of California. Who would have thought it would ever come to that?

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