

Executive Summary

(View Mac Taylor's brief video summary of our major findings.)

Over \$20 Billion of Budget Problems Need to Be Addressed in Coming Months

Our forecast of California's General Fund revenues and expenditures shows that the state must address a General Fund budget problem of \$20.7 billion between now and the time the Legislature enacts a 2010-11 state budget plan. The budget problem consists of a \$6.3 billion projected deficit for 2009-10 and a \$14.4 billion gap between projected revenues and spending in 2010-11. Addressing this large shortfall will require painful choices—on top of the difficult choices the Legislature made earlier this year.

Failed Budget Solutions Responsible for Newly Identified Budget Problem

The vast majority of the new budget problem we have identified for 2009-10 can be attributed to the state's inability to implement several major solutions in the July 2009 budget plan, such as:

- The expected inability of several programs—in particular, the prison system and Medi-Cal—to collectively achieve billions of dollars of spending reductions assumed in the 2009-10 budget.
- The expected inability of the state to sell the State Compensation Insurance Fund (SCIF), a quasi-public workers' compensation insurer, for the budgeted amount of \$1 billion in 2009-10.
- The state's loss of a court case that makes the General Fund unable to benefit from over \$800 million in transportation funds in 2009-10.
- A nearly \$1 billion increase in the Proposition 98 funding guarantee for K-14 education in 2009-10.

The ongoing impact of most of these problems further expands the multibillion-dollar operating shortfall that policymakers already expected in the 2010-11 budget year. Additional court cases threaten to drive our identified budget problem even higher.

some past recoveries, it reflects the modest nature of our economic forecast for this period.

The second major factor affecting revenues is the impact of policy changes made in 2008 and 2009—revenue accelerations, temporary tax increases, and permanent tax cuts. These policy changes boost revenues significantly in 2009-10 and 2010-11, but lower revenues in the out-years of the forecast. The overall effect of these measures is to smooth out the pattern of revenues—mitigating the declines in 2009-10 but flattening revenues in 2010-11 and 2011-12. Beginning in 2012-13, revenues grow slightly below typical long-term growth trends.

Current Budget's Revenues a Little Soft

2008-09 Revenues—Down \$496 Million. Figure 9 (see next page) displays our assessment of General Fund revenues for 2008-09 and 2009-10 compared to the amounts assumed in the *2009-10 Budget Act*. Based on preliminary data from the State Controller and the state's tax agencies for 2008-09, we estimate that General Fund revenues and transfers totaled \$83.6 billion, or \$496 million (0.6 percent) below the level assumed in the *2009-10 Budget Act*. The main elements of the shortfall are related to SUT (-\$222 million), "other revenues and transfers" (-\$230 million, mostly due to a shortfall in vehicle license fee [VLF] revenues), and PIT (-\$135 million).

2009-10 Revenues—Down \$1.5 Billion. While the economy appears to be on the mend, General Fund revenues are still falling somewhat short of the 2009-10 budget assumptions. We project a \$1.5 billion fall in General Fund revenues and transfers in 2009-10—a 1.6 percent reduction from the \$89.5 billion level assumed in the *2009-10 Budget Act*. The single biggest factor relates to the assumption in the enacted budget that the state could realize \$1 billion in 2009-10 from the sale of insurance policies administered by the State Compensation Insurance Fund. The State Insurance Commissioner has opposed the sale in court, which makes it unlikely the sale will occur in the near term. Given the legal questions raised about the sale and the lack of a concrete sale plan to date, we do not include revenue from this proposal in our forecast.

After adjusting for this \$1 billion, other revenues are down by \$451 million. The big three taxes all are projected to decline somewhat. Personal income tax revenues are projected to fall \$299 million (0.6 percent), as both withholding and estimated payments for the first quarter of 2009-10 were below targets. Our forecast also reflects the continuing weakness in consumer spending, with sales tax revenues falling short by \$362 million (1.4 percent). Corporate tax revenues also fall by \$199 million (2.3 percent). The softness in the state's major taxes is offset somewhat by higher-

Figure 8
The LAO General Fund Revenue Forecast

(In Millions)

Revenue Source	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Personal Income Tax	\$43,689	\$46,932	\$46,212	\$46,305	\$50,235	\$54,479	\$58,658
Sales and Use Tax	24,066	26,322	28,103	25,506	27,345	29,092	30,420
Corporation Tax	9,773	8,306	7,824	7,766	8,673	9,288	9,892
Other revenues and transfers	6,073	6,530	5,654	4,844	5,383	6,339	6,750
Total Revenues and Transfers	\$83,601	\$88,090	\$87,793	\$84,422	\$91,636	\$99,197	\$105,720