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**California's deficit should fall, but by how much?**

Tax revenues have continued at a strong clip, so state leaders can reduce the deficit with one change in the ledger, as we've noted.

The Legislative Analyst's Office reported today that the state is now $2.54 billion ahead of projections based on April data from the Franchise Tax Board and Board of Equalization that accounts for all three major tax sources.

The question is how will this affect the bottom line. We've been citing the deficit as $15.4 billion ever since Gov. Jerry Brown signed bills in March to cut the $26.6 billion shortfall by $11.2 billion.

Brown and his aides have indicated a desire to downplay the revenue growth when he releases his revised budget on May 16. When we asked Brown about it last month, he pooh-poohed the robust revenues and left it to Finance Director Ana Matosantos to explain how various factors come into play.

As political strategists have noted, it could very well hurt Brown's case for tax extensions if voters keep hearing about the state taking in more money than it expected, even though that additional cash won't solve the entire deficit.

Here's a look at some of the changes that may be made to the $15.4 billion figure when Brown releases his next budget.

**POSITIVE IMPACTS:**

- **Current revenues** are ahead of projections by $2.54 billion. This is money in the bank, so the governor could reasonably apply it directly to the bottom line. Ordinarily this money would be subject to Proposition 98 education requirements, giving schools part of the cash instead of shrinking the deficit. But the Legislature suspended Proposition 98 in 2010-11, so this doesn't apply.

  * **Caveat:** The Department of Finance could always make the case that it expects May and June revenues to slide. This would be questionable, given that the Analyst's Office said yesterday that April's quarterly tax filings suggest good things for June.
• **Lawmakers approved** $2.6 billion in budget solutions that Brown has yet to sign. We have not reflected this in the deficit calculation because the budget bill remains on hold at the governor's request.

*Caveat:* The influx of cash could cause Brown to rethink some of the cuts already approved and seek to block them. For instance, he could always decide to reduce the cuts to higher education.

• **Higher than expected revenues** for this fiscal year are typically used as a basis for assuming more money in the next fiscal year. That means revenue analysts could decide the state should be more optimistic about the economy in the next year and decide the state will take in an additional $2 billion or more than it had been predicting for 2011-12.

*Caveats:* The governor could decide that jobless figures or other economic indicators do not bode well for the 2011-12 year and not adjust projections going forward. Even if the governor assumes higher revenues in the next fiscal year, not all of it can apply toward deficit reduction since the state would owe schools a good share of the revenue growth under *Proposition 98.*

**NEGATIVE PRESSURES:**

• **The state faces lawsuits** regarding $1 billion in First 5 revenues that Brown and lawmakers took in March. The governor could cancel out that solution for the time being.

• **The Legislative Analyst says** state worker contracts do not hit their projected savings targets in the current or budget year. State worker pay savings will likely be adjusted to reflect this, possibly by around $250 million general fund based on the Analyst's estimates.

• **Expenditures in social services and other programs** will be revised based on caseload and population updates. This could go either way.

• **Savings in social service programs** could be adjusted to reflect more accurate savings. The Legislative Analyst has already pointed out that the governor overestimated savings in *In-Home Supportive Services,* for instance.

*Posted by Kevin Yamamura*