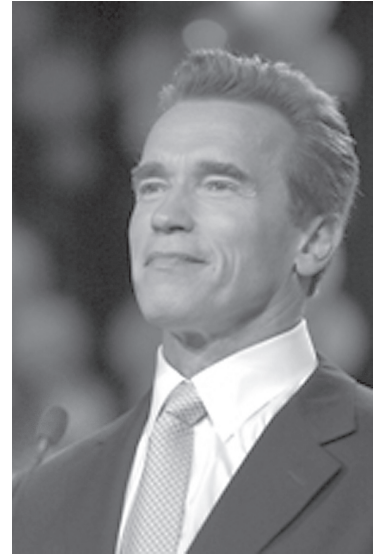




GOVERNOR
ARNOLD SCHWARZENEGGER

January 10, 2005



To the Senate and Assembly of the Legislature of California:

In a difficult fiscal environment, this balanced budget provides a 4.2 percent increase in General Fund spending over last year to protect essential programs like education and social services. It does not raise taxes on working families and businesses that create jobs. And, it lays the groundwork for fundamental budget reform that our state desperately needs.

Just one year ago, California was facing economic ruin. We were staring at a budget gap of more than \$14 billion and a cash crisis of \$14 billion in June that would have sent the state into bankruptcy.

We chose a different path. We joined together to take action and began turning around years of fiscal mismanagement. Republicans and Democrats put Propositions 57 and 58 before the people of California, who gave it their solid approval. And, Republicans and Democrats passed a budget that began to bring spending in line with revenues - without raising taxes.

Last year, we stopped the bleeding. This year, we must begin to heal the patient.

Because of our formula-driven system of budgeting, we face a budget gap of more than \$9 billion if we do nothing. The budget I send to you today will close that gap, and do so again without raising taxes.

But unless we act to fundamentally change the laws that put so much of our spending on automatic pilot, we will continue to face huge deficits - year after year after year. We must fix a budget system that is broken. We must change the way that state government spends the people's money. That is why budget reform is a critical part of the reform agenda I will ask you to approve in a Special Session.

The California recovery is underway, bringing with it more jobs and growing revenues. However, if we leave in place a budget system that forces us to spend more money than we take in, we will fail to solve one of the most critical problems the people of California sent us to Sacramento to fix - the state budget.

Last year, we worked as partners to begin to make change. I ask you to continue our partnership this year to make even greater progress for the people.

Therefore, in accordance with Article IV, Section 12 of the California Constitution, I submit to you the Governor's Budget for 2005-06.

Sincerely,

Arnold Schwarzenegger