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## **Editorial: A dire fiscal crisis calls for strong action**

### **GOVERNOR'S PLAN IS A GOOD STARTING POINT; NOW EVERYONE MUST SHARE THE BURDEN**

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In his 2005 State of the State address, Gov. Arnold Schwarzenegger repeated one of his famous lines about California, "We don't have a revenue problem. We have a spending problem."

Yet as the governor acknowledged Thursday, California does have a revenue problem. It has nurtured one for decades.

Because of the state's reliance on capital gains taxes and sales taxes, its revenues gyrate from year to year based on stock market performance and consumer confidence. This year, the revenue roller coaster has taken an epic downturn. Tax revenues in the current fiscal year – already one-third over – have dropped 11 percent from earlier projections.

That means that lawmakers, in a special session convened by the governor last week, must reduce spending and/or increase revenues by a staggering \$11 billion in the current year. And they can't dawdle. Every day, the state spends \$1 for every 90 cents it brings in, and the hole gets deeper.

To add to their challenges, lawmakers can't simply borrow or defer payments. That's because the revenue slide isn't just a one-year headache, it's a multiyear one. Without multiyear cuts or new revenues, the deficit in 2009-10 will mushroom to at least \$13 billion, according to the governor's Department of Finance, with increased spending obligations on top of that pushing the total to \$20 billion or more.

The fairy-tale budget that lawmakers approved in September is partly to blame – but only partly. The collapse of Wall Street and rising unemployment have driven down tax receipts to levels no one could have foreseen. Income tax receipts are expected to be \$7.2 billion lower than projected two months ago. Revenues from sales and corporation taxes are expected to fall by \$3.2 billion.

To close the gap and stimulate the economy, Schwarzenegger on Thursday proposed a mix of spending cuts, tax increases, mortgage reforms and infrastructure projects. There's much to like in this package. Perhaps its greatest virtue is that it is adequate to the task at hand.

Among other things, the governor calls for an oil severance tax, a higher booze tax, parole reforms and accelerated bond spending. Enacting all of these would allow lawmakers to avoid the worst possible cuts to schools, universities, welfare programs and Medi-Cal. Such programs would still face harsh reductions under Schwarzenegger's proposal, but they'd be meat-cleaver cuts, not those of a chain saw.

Even so, both Democrats and Republicans should urge the governor to reconsider some of his revenue proposals.

To generate the bulk of his new receipts, the governor is proposing a temporary 1.5 cent sales tax increase that would generate \$3.2 billion this year and \$6.6 billion in the following fiscal year. The governor prefers a sales tax because he believes it would generate a quick and reliable source of revenue. In the long run, the sales tax should be extended to services. But with auto dealers closing and consumers cutting back, relying on the regressive sales tax as a quick fix is a dubious idea.

A better alternative would be a temporary surcharge on personal income taxes. Such a tax would have less impact on the economy, because it would disproportionately hit upper-income earners. Individuals can easily deduct this tax from their federal income taxes, which means Washington would help bridge California's budget gap. If you want to raise tax revenues while maximizing the amount of dollars flowing back into a faltering economy, a hike in income taxes is the way to go.

Lawmakers should also consider other ways to free up monies in the general fund. Consider, for example, the money lawmakers raided last year from transit systems. Much of that money went to pay debt service on transportation bonds that voters approved two years ago.

Instead of robbing Peter to pay Paul, lawmakers should consider raising the excise tax on gasoline. Gas prices have dropped, so consumers could absorb a small hike in the gas tax. The revenue could then be used to pay off debt for transportation projects, freeing money to help transit systems and transit riders.

Republicans in the Legislature would likely resist such proposals. They say California's spending is out of control.

The trouble is, that claim is not true. As the Legislative Analyst's Office has noted, per capita state spending, adjusted for inflation, has not changed in California in a decade. Sure, overall spending has increased, but so have population and the cost of living.

It's also hard to argue that taxpaying Californians can't afford to pay a bit more in taxes. A couple earning \$80,000 a year currently pays about \$3,176 in state income taxes. A 10 percent surcharge would add \$317 to that tax bill – hardly an insurmountable hardship in a state facing an \$11 billion emergency.

And it is an emergency. If lawmakers in California can't come to agreement on fixes, the state could run out of money by February, according to the governor.

To avoid that prospect, lawmakers of both parties must act quickly and put the state's interests above ideology. Republicans must accept the inevitability of new taxes. Democrats must accept cuts to vital programs and state employment (and support the governor's furlough proposal, even if it raises the ire of their supporters in the public employee unions).

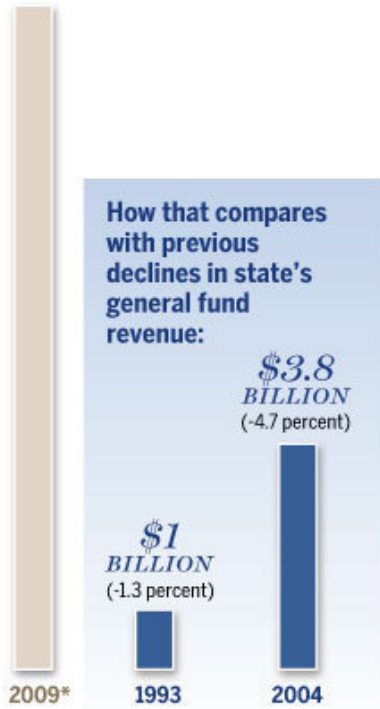
Elected officials aren't the only ones who need to behave responsibly. Employee unions must face the reality that work force cuts are inevitable. The state's business community must mobilize to exert serious pressure on both parties.

And Californians who approved nearly \$11 billion in additional debt in Tuesday's election need to recognize their contribution to this crisis. If they want bullet trains, they must dig into their pockets and help the state dodge a bullet known as insolvency

# An epic slide in state revenues

Because of the economic downturn, Gov. Arnold Schwarzenegger and his finance team are projecting that tax revenues will fall during the current fiscal year by ...

... **\$11.2 BILLION**  
(11 percent decline over previous year's general fund revenues.)



\*Current fiscal year

Sources: California Department of Finance; Next 10 Budget Challenge

If nothing is done this year, the deficit in 2009-10 could approach:

**\$20 BILLION**  
total

**\$7 BILLION**  
in increased spending obligations

**\$13 BILLION**  
reduction in general fund revenue

What \$20 billion looks like:

## Schools

It's half what the state spends each year to educate 6.3 million K-12 students.



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## Higher education

It's \$9 billion more than the state spends yearly on the University of California, state universities and community colleges.



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## Criminal justice

It's \$8 billion more than the state spends yearly on courts, juvenile justice and its prison system with 170,000 inmates.



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