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## **Daniel Weintraub: California Budget 101: What went wrong, when**

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When Gov. Arnold Schwarzenegger signed the state budget last summer, he all but declared "mission accomplished" in his administration's biggest battle. The spending plan not only eliminated the state's perpetual deficit, he said, it also boasted a record \$4 billion reserve. The state was fully funding education and public safety and repaying debt earlier than required, all without raising taxes.

"I applaud the Republicans for pushing us to take the operating deficit down to zero this year," Schwarzenegger said as he signed the document after a seven-week stalemate. "And I applaud the Democrats for being willing to compromise while sticking to their principles to get the budget done. It was a difficult process, but in the end, this is a good budget for California."

Even as Schwarzenegger spoke, however, trouble was looming. The tax projections on which the spending plan was based already were proving to be overly optimistic. And spending, especially in the state prison system, was heading higher than expected, thanks mainly to court-ordered payments for inmate medical care.

Now, nine months later, the governor is back in the fiscal swamp. His reserve has been wiped out, and projections for the end of the current year and the next fiscal year combined showed a potential shortfall of \$17 billion if Schwarzenegger and the Legislature were to do nothing more to avert it.

This month, as the governor released a revised spending proposal, readers reported to me that they did not understand how the state got itself into this predicament. As citizens, they said, they can't be expected to assess the relative wisdom of budget cuts, tax hikes, gimmicks or borrowing without a fuller explanation of the dimensions of the problem those remedies are meant to solve. This column begins to answer that question in a very abbreviated and simplified form.

So, what went wrong?

The latest trouble is partly the result of the sluggish economy. Employment growth flattened. Corporate profits sagged. The crash in the housing market slowed consumer spending. Tax revenues that last summer had been expected to total more than \$102 billion now figure to come in under \$98 billion for the year.

Spending is up, too, though. The forecast for the current year was about \$102 billion. The latest figures now put the cost of the state's commitments at more than \$104 billion.

But the economic issues only worsened a basic, structural problem in the state budget: Spending is programmed by law to grow each year at a rate that is generally faster than tax revenues can match. Current state law would push general fund spending to \$113 billion next year if nothing is done to slow it, according to the Schwarzenegger administration. Revenues, meanwhile, are projected to decline further, to about \$95 billion. The budget Schwarzenegger celebrated last summer would have bridged the gap for one year at best.

Since Schwarzenegger has been governor, the state's revenues have grown by 25 percent. But spending has grown even faster – far faster than population growth and inflation combined. The spending increase totals about \$26 billion, starting from a base of \$77 billion.

Where did all that money go? Most of it went to education, health and welfare programs, and prisons, with a good-sized chunk for transportation.

The state today reports spending \$13 billion more on kindergarten through 12th grade education than it did the year before Schwarzenegger took office, an increase of nearly 50 percent. That number overstates the growth in education spending because of accounting changes and the changing relationship between state and local finances. A better way to measure it is to look at state and local tax dollars combined for schools. But even by that yardstick, spending per pupil has still increased by 29 percent, from \$6,624 per student to \$8,564.

Health and welfare programs have grown at the same rate, 29 percent, or \$6.6 billion since 2002-03. The biggest cost driver there has been health care for the poor, which took about half the gain. The other half of the growth was split mainly among services for people with mental illness, help for the developmentally disabled and assistance to the elderly and the disabled in their homes.

Prison costs also have escalated rapidly, gobbling up about \$4 billion of the overall increase. Their rate of growth – 74 percent – has been by far the fastest among the state's major programs. Thanks to tough sentencing measures and a parole system that sees 70 percent of ex-cons going back to prison within three years of their release, the number of inmates behind bars has grown from about 160,000 to 169,000 on Schwarzenegger's watch. Correctional officers also got a 37 percent pay raise spread over five years that began just before Schwarzenegger took office. And the courts have ordered hundreds of millions of dollars in new costs for inmate health care.

The state is also spending a lot more on transportation, mainly building roads, bridges and public transit systems. Most of that increase – about \$1.3 billion – is money from sales tax collections that the voters redirected to transportation programs when they passed Proposition 42 in 2002. Spending on higher education has grown in step with population and inflation, about 25 percent, or \$2.3 billion.

So if you want to roll back spending, those are the places that have to be cut. If you want to slow the growth in government, then education, health and welfare, and

prisons are the places to look for the big bucks. And if you are asked to consider raising taxes, those are the programs that are going to benefit most from the increased revenues.

That's a bare-bones explanation. But I hope it helps.

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