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Legislative Analyst Forecasts \$8 Billion Revenue Shortfall

In a report reviewing the just enacted 2009-10 State Budget and the anticipated federal stimulus funds, the Legislative Analyst's Office (LAO) forecasts that General Fund revenues in 2009-10 will fall short of budgeted levels by almost \$8 billion. This forecast comes less than a month after the Governor signed the 2009-10 Budget Act.

Released on March 13, 2009, the LAO report, titled *The Fiscal Outlook Under the February Budget Package*, indicates that the state and national economies continue to trend down. The report notes that California's unemployment rate reached 10.1% in January compared to 8.7% just one month earlier. Similarly, the national unemployment rate increased to 8.1%. For the month of February, state tax collections from the three major taxes-the personal income tax, the sales and use tax, and the corporation tax-were \$815 million short. (Note: This shortfall is measured against the major downward revision that accompanied the January Governor's Budget, which cut revenues \$15 billion in the current year.)

This dismal economic and revenue news has prompted the LAO to forecast a delay in the economic recovery and a shortfall in 2009-10 revenues of \$7.837 billion compared to the budgeted level. It is interesting to note, however, that the LAO is not projecting a revenue shortfall in the current year, despite the weakness in February receipts. The key revenue month will be April, since personal income tax liabilities for 2008 are due on April 15, 2009.

Given the deterioration in the state's economic and revenue outlook, the LAO recommends that the Legislature "optimize" the use of federal funds. For K-14 education, the LAO anticipates a drop in the Proposition 98 minimum funding guarantee as a result of the drop in General Fund revenues. The LAO recommends that the federal funds be used to replace currently appropriated General Fund revenues in support of K-14 education, thus lowering the state appropriation to the new minimum level. These freed up General Fund dollars would presumably be used to support other state programs. The LAO also suggests that the state "preserve as many federal dollars as possible to help balance the Budget in future years-as opposed to committing them now for augmentations." This advice, however, could run counter to the intent of the federal funding, which is to avoid cuts that are immediately pending.

Finally, the LAO report highlights vulnerabilities to the State Budget related to the upcoming May 19, 2009, special election in which voters will decide on a plan to borrow \$5 billion against the State Lottery and the transfer of more than \$800 million in special fund revenues to the General Fund. If these measures are rejected by state voters, the Legislature will have to find other solutions to balance the 2009-10 Budget.

The full report can be downloaded at www.lao.ca.gov.

-Robert Miyashiro

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