

PANE & PANE ASSOCIATES, INC.

January 5, 2009

MEMO TO: California Bus Association Board & Members
FROM: Josh and Donna Pane
RE: Recap of State Budget Crisis

We thought this recap of the budget deficit situation facing the state would be of interest. This crisis will be the prevailing issue facing legislators and until it is resolved, there is no telling what will happen with other legislative issues in 2009.

NEW YEAR BEGINS WITHOUT BUDGET SOLUTION FOR CURRENT FISCAL YEAR.

As 2008 drew to an end, California does not have a budget solution in place to resolve the \$15 billion deficit for the current fiscal year. This is really incredible and shows an absolute failure of leadership in one of the most perilous times. California's leaders cannot agree on a way to fix the state's ailing finances and therefore, California can't sell bonds for public works projects that would provide paychecks for thousands of people. Here is a recap of what took place since December 1st when the Governor declared a fiscal emergency, which set in motion a new special session with a 45-day deadline for action:

Republican Proposal. In mid December, the Republicans finally put forward their "no-new taxes proposal" that called for easing the budget shortfall by cutting deeply into schools and social service programs. It also required that voters undo two of the initiatives that were recently passed. This was the most substantive proposal yet put forward by the Reps but it was dismissed by the Democrats, as well as the Governor as an exercise in futility and continues the game of who blinks first.

Democrats Counter Proposal. The following day (and night, with a possible threat of locking them up for the night) the Dems countered with a new \$19 billion plan that adopted the Governor's tax ideas. Surprise, it didn't get the two-thirds needed nor did the Republicans plan which was also put up for a vote. Back to square one.

Democrats Try Budget End Run. In the wake of the California Pooled Investment Board (CA Treasurer Bill Lockyer, CA Controller John Chiang & Dept. of Finance Director Genest) halting funds for public works projects, on December 18th the Dems put together a package of bills to deal with the budget deficit that are "revenue-neutral" and thus could be passed by a simple majority rather than the constitutionally required two-thirds vote for tax increases. This plan raised taxes on gasoline, personal income and sales; cut state spending on schools and lowered the state's payroll by \$657 million. Specifically the tax increases under the plan raised the sales tax by ¼ cent; a 2.5 percent surcharge on state income tax owed; raised gasoline tax from 26 cents to 39

cents per gallon; added a 3 percent withholding tax collected by businesses from money paid to contractors and added a 9.9 percent severance tax on oil produced in California. These bills passed with a majority vote and no Republican votes (lawsuits will follow if the Governor signs these bills) and then the Senate and Assembly adjourned the 1st Extraordinary session of the Legislature and said they'd be back January 5th.

Governor Vows to Veto Dems Plan, Unless. . . The Governor said his objections are not so much over the majority vote approach for the tax increases but over what they left out. The Governor wants broader exemptions from state environmental regulations and a streamlined permitting process and fewer requirements for state construction partnerships with private firms.

Governor and Democrat Leaders Continue to Negotiate (by teleconference) Without Republican Input. As this column goes to print, there is talk that the Governor and Dem leaders are close to an agreement on the Governor's requests for deeper cuts and more of his economic stimulus requirements and if that happens, he will sign the package of bills that were passed on December 18th. In the meantime, he has issued an Executive Order for a plan that would go into effect in February to furlough state employees and supervisors for two days per month and to initiate layoffs and other position reductions to achieve General Fund savings of up to 10 percent.

Governor Unveils Budget Plan Early, Proposes A Mini Version of Blow Up the Boxes. As the Governor and Dem leaders continue to talk via teleconference, the Administration released on New Year's Eve (9 days earlier than he would have revealed his 2009-10 budget), a comprehensive plan to close an estimated \$40 billion deficit over the next 18 months with \$17 billion-plus in spending reductions, \$14 billion-plus in new taxes and nearly \$10 billion in loans of one kind or another. Part of this proposal is to eliminate or downsize various boards and commissions, a lesser version of his plan to eliminate many state boards and departments several years ago. The best prospect for a resolution to the immediate shortfall is for the Dems to give in to the Governor's request for the stimulus package he wants; he'll then sign the package of bills they sent to him last month that will prevent the state from going "broke" in February. This is truly a crisis situation and nothing they do is going to be pleasant.

As always, if you have any questions or need additional information, please don't hesitate to contact us.