



Agenda Item #: \_\_\_\_\_

# Staff Report

## City of Manhattan Beach

**TO:** Honorable Mayor Aldinger and Members of the City Council

**THROUGH:** Geoff Dolan, City Manager

**FROM:** Lindy Coe-Juell, Assistant to the City Manager

**DATE:** December 4, 2007

**SUBJECT:** Consideration of the State Budget and Legislative Update

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**RECOMMENDATION:**

Staff recommends that the City Council receive and file the December 2007 Budget and Legislative Update from Tony Rice, the City's legislative advocate.

**FISCAL IMPLICATION:**

There are no fiscal implications associated with staff's recommendation.

**BACKGROUND:**

The City contracts with Tony Rice of Rice, Englander and Associates, for legislative advocacy and representation. One of the deliverables of the contract is to provide regular updates on the state budget and legislative activity.

**DISCUSSION:**

The December 2007 Budget and Legislative Update from Tony Rice is attached.

December 4, 2007

To: City of Manhattan Beach

Fm: Rice/Englander & Associates

**RE: SACRAMENTO UPDATE**

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### **Regular and Special Sessions**

The Regular Session of the Legislature, the time when the most activity is associated with the Legislature's activities, continues to be in abeyance until January 7, 2008. However, as we have reported before, the Governor called two separate Special Sessions on the last day of the Regular Session this year to continue activity on the desires to expand healthcare coverage to California's uninsured as well as increase the state's water storage, and the ability to move that water in California. Initially, leadership in the Senate and the Assembly wanted to dispense with the Session on water early through agreement between the Democrats, Republicans and the Governor, and then focus on, and pass, a deal on healthcare. While numerous meetings have occurred on both topics, no tangible agreement has been reached.

As with the failure of most big ticket agendas, the devil is in the details, and more importantly, the funding of those details. Healthcare, while laudable and agreeable to most of the legislators has been hinged on who would pay for the expansion of healthcare. The current estimate is that there are approximately 7.5 million uninsured in California. The cost to provide even a modicum of insurance to those individuals is in excess of \$10 billion. The general funding package that has been floated as the financial solution is a mixture of payments from the federal government, state government, businesses, the hospitals providing the care as well as some amount of individual contribution. Given the current state of the economy, coupled with the economic forecasts showing a continued slowdown, the prospects for a viable funding package appear slim to none.

Regarding the Special Session on water, again, there is general agreement amongst policy makers that the efficient movement of water, as well as the increase in general water storage, are laudable and agreeable goals, however the funding split is the major hang up. The funding source for the package has traditionally been a lease revenue bond, needing to be approved by the voters of course, so the State's General Fund would not be called upon to provide financing. However, the allocation of the revenue (generally considered to be approximately \$5-6 billion) has been the primary issue. The Republicans have demanded that increased surface water storage be a part of the discussion. The Democrats are favorable to that request but do not believe the State should pay a large share of the costs to build the dams.

Instead, the Democrats believe historical precedence should be observed whereby the users and direct benefactors of the dam should pay most of the costs. The Republicans, including the Governor, would like the State to pay at least 50% of the costs. A meeting of the “Big 5” (Governor, Speaker, Pro Tempore, Senate and Assembly Minority Leaders) met as recently as last week to discuss the ability to get a deal done quickly on this issue, however they were unable to reach an accord. As 2007 winds to a close the likelihood of any deal on either of these issues in the near future becomes increasingly unlikely.

## **Budget**

While we normally do not provide budget updates so early, we believe it is important to foreshadow the very dire budget situation California appears to be facing. On November 16, 2007, the non-partisan Legislative Analyst’s Office released it’s preliminary forecasts for the state’s budget. As you know, the Governor must release his Proposed 2008-09 State Budget on or before January 10, 2008. Therefore, all his state agencies and departments are submitting their budget requests and matching them against the Department of Finance’s budget projections. While the LAO and the DOF do not always agree, there is a history that the respective projections are fairly close. The LAO’s summary of their budget projections follow:

### *Deterioration of the 2007–08 Budget*

At the time the *2007–08 Budget Act* was enacted in August 2007, the budget plan focused on closing the gap between General Fund revenues and expenditures for the fiscal year and maintaining a \$4.1 billion reserve. Since that time, the 2007–08 budget situation has deteriorated by almost \$6 billion. Under our forecast, absent corrective action, the state would end the current fiscal year with a \$1.9 billion deficit. The state’s dimming fiscal outlook is due to:

- Continued softness in the state’s economy lowering the forecast of revenues.
- Lower property taxes, driving state General Fund spending on K–14 education upwards.
- A likely delay in the sale of EdFund and a reduction in anticipated revenues.
- Delayed implementation of new tribal gambling compacts.
- A court–ordered payment to the state’s teacher retirement system.

### *State Also Faces \$8 Billion Shortfall in 2008–09*

In addition to a negative carry–in balance from 2007–08, we project the state will face an \$8 billion operating shortfall in 2008–09. Revenues are projected to grow by 4.6 percent, hampered by the ongoing effects of the weakened economy. On the expenditure side, spending is projected to grow by 7 percent—reflecting both cost increases in most state programs and the end of many 2007–08 one–time budget solutions.

### *Multibillion Dollar Shortfalls Through 2012–13*

Like in 2008–09, we project state costs will exceed revenues by \$8 billion in 2009–10. After that, the shortfall will drop to the range of \$3 billion each year. The primary factor responsible for this drop between 2009–10 and 2010–11 is that \$11.3 billion in previously issued deficit–financing borrowing would be fully paid off in the spring of 2010. This will free up over \$3 billion in annual debt service payments beginning in 2010–11.

### *LAO Bottom Line*

In order to balance the 2008–09 budget, the state will have to adopt nearly \$10 billion in solutions. Addressing the state’s current budget problem is even more urgent because we forecast a *continuing* gap between revenues and expenditures. A plan to permanently address the state’s fiscal troubles must involve a substantial portion of ongoing solutions. This is not only because of the persistent operating deficits projected throughout the forecast, but also because of the downside risks inherent with the economy, General Fund revenue volatility, and a wide range of budgetary uncertainties. Making tough choices now will allow the state to move closer to putting its fiscal woes in the past.

The reason these concerns are so substantial is that we fear the state may look to alternative funding sources, like Proposition 42 funding (transportation revenue) and local revenue that the state has tapped before, as potential solutions. We must remain vigilant to protect local discretionary revenues.