

Controller *John Chiang*

California State Controller's Office



May 2008 Summary Analysis

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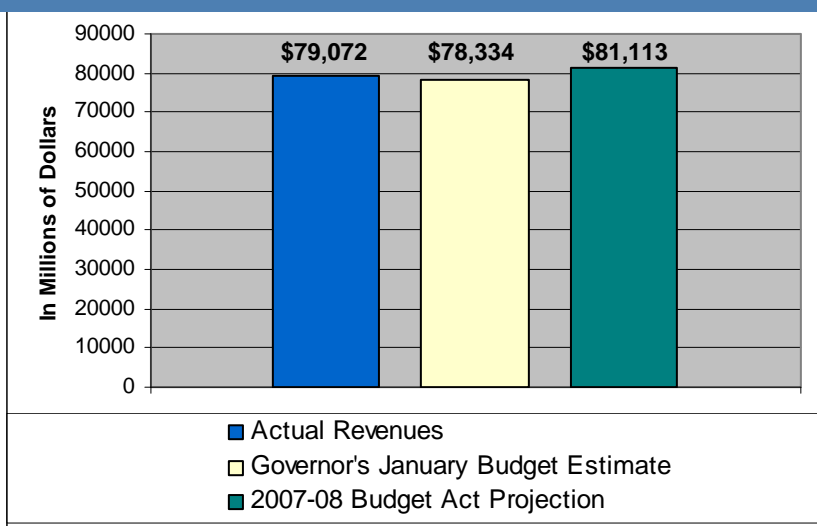
Statement of General Fund Cash Receipts and Disbursements

Tax Revenue in April 2008

- ⇒ General Fund revenue in April 2008 was \$1.6 billion above (10.6%) the Governor's January Budget estimate for the month. Income taxes were the largest contributor to this gain, coming in \$1.2 billion above (10%) the estimate. Sales taxes were below the estimate by \$168 million (-15.9%) while corporate taxes were \$126 million above (8.3%) the Governor's Budget estimate. Together, the three largest taxes (personal income, corporate and sales taxes) were \$1.1 billion above (7.9%) the Governor's January Budget estimate for April. Insurance tax receipts were above estimate by \$415 million, which may reflect delayed revenue from prior months.
- ⇒ Revenue in April was \$19 million below (-0.1%) the 2007-08 Budget Act estimate. Income taxes were \$169 million lower (-1.3%) than the Budget Act's figures. Retail sales revenue was below estimates by \$54 million (-5.7%). Corporate taxes were \$30 million above (1.8%) the Budget

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Table 1: General Fund Revenues: July 1, 2007–April 30, 2008 (in Millions)



The State Controller's Office is responsible for accounting for all State revenues and receipts and for making disbursements from the State's General Fund. The Controller also is required to issue a report on the State's actual cash balance by the 10th of each month.

As a supplement to the monthly *Statement of General Fund Cash Receipts and Disbursements*, the Controller issues this Summary Analysis for California policymakers and taxpayers to provide context for viewing the most current financial information on the State's fiscal condition.

This Summary Analysis covers actual receipts and disbursements for April 2008. Data are shown for total cash receipts and disbursements, the three largest categories of revenues, and the two largest categories of expenditures. This report also provides the state's latest revenue projections as points of comparison. In January, the Governor released his 2008-09 budget proposals, which contain updated revenue projections for the remainder of the fiscal year. A comparison to those projections is included. We also continue to include a comparison to the 2007-08 Budget Act passed in August 2007.

For the three largest sources of revenue (income taxes, corporate taxes and sales taxes), the Governor's January budget reduced revenue expectations in fiscal 2007-08 by \$3.6 billion. The largest was a \$2.4 billion reduction in expected income taxes, with April and May receipts expected to be down by almost \$2 billion from the projections given in the Budget Act.

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Act estimate. In total, the three major taxes were \$193 million below (-1.2%) the Budget Act estimate for April.

⇒ Total General Fund revenue for April 2008 was \$1.2 billion above (8.1%) the revenue seen in April 2007. Income taxes accounted for \$817 million of the increase while sales taxes added another \$324 million. In total, the three largest taxes (including corporate tax, which showed little growth) were \$1.2 billion above (8%) the revenue seen in 2007.

Tax Revenue Fiscal Year to Date

⇒ For the fiscal year through April 30, 2008, General Fund revenue was \$738 million above (0.9%) the Governor's January Budget estimate.

Sales taxes were \$602 million below (-2.8%) the estimate, corporate taxes were \$216 million under the estimate (-2.6%), and income taxes were \$1.4 billion above (3.2%) the estimate. Together, the three largest taxes were \$612 million above (0.8%) the Governor's Budget estimate for this date.

⇒ Through April, General Fund revenue was \$2 billion below (-2.5%) the Budget Act estimate. Retail sales receipts were \$994 million below (-4.6%) the Budget Act year-to-date estimate, while corporate taxes were \$717 million lower (-8.1%) than expected. Income taxes were below the year-to-date estimate by \$269 million (-0.6%). In total, the three largest taxes were \$2 billion below (-2.6%) the level expected in the Budget Act.

⇒ Of the three largest taxes, corporate taxes showed the weakest growth in a year-over-year comparison, having dropped \$559 million below (-6.4%) the levels seen last year. Sales taxes also were weak, yielding \$117 million less (-0.6%) than in the same period during the last fiscal year. Personal income tax receipts were \$2.2 billion higher (4.9%) than last year at this date. Withholding continued to provide most of the increased revenue, yielding \$1.5 billion more (5.4%) than last fiscal year at this time.

⇒ Compared to last fiscal year at this date, General Fund revenue was \$910 million higher (1.2%). All revenue sources except income taxes were either lower than last year, or flat.

Table 2: General Fund Receipts, July 1, 2007-April 30, 2008 (in Millions)

Revenue Source	Actual Receipts To Date	Governor's Budget Estimate	Actual Over (Under) Estimate	Budget Act Projections	Actual Over (Under) Projection
Bank And Corporation Tax	\$8,142	\$8,358	(\$216)	\$8,859	(\$717)
Personal Income Tax	\$46,805	\$45,376	\$1,430	\$47,075	(\$269)
Retail Sales and Use Tax	\$20,645	\$21,247	(\$602)	\$21,639	(\$993)
Other Revenues	\$3,480	\$3,353	\$127	\$3,540	(\$60)
Total General Fund Revenue	\$79,072	\$78,334	\$738	\$81,113	(\$2,041)
Non-Revenue	\$6,821	\$6,533	\$287	\$1,364	\$5,457
Total General Fund Receipts	\$85,893	\$84,867	\$1,026	\$82,477	\$3,415

Note: Some totals may not add, due to rounding

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⇒ Totals from the three largest taxes show a declining rate of growth. In April of 2006 the year-to-date increase in the big three taxes was 10.5% higher than the same period of the prior year. In 2007, the growth was 3.1%. By April 2008, the fiscal year-to-date growth had slipped to 2.1%.

Summary of Net Cash Position as of April 30, 2008

⇒ In April, the State closes much of the gap between expenditures and revenue. At the end of March, the State had a fiscal year spending deficit of \$17.6 billion. In April, revenue receipts exceeded expenditures by \$8.1 billion. Expenditures were \$8.2 billion and receipts totaled \$16.3 billion. The year-to-date spending deficit was reduced to \$9.5 billion.

⇒ The two main sources of the \$6.8 billion in non-revenue receipts in Table 2 were from \$3.3 billion in Economic Recovery Bond proceeds in February and the transfer of \$1.4 billion from the Budget Stabilization Account in January. The Governor's January Budget included these monies, but the August 2007 Budget Act did not.

⇒ For the fiscal year to date, the State spent \$9.5 billion more than it received in revenue (see Table 3). Total receipts were \$85.9 billion (see Table 2); while total expenditures were \$95.4 billion (see Table 4).

⇒ The State began the fiscal year with a cash balance of \$2.5 billion. The net cash deficit at the end of April was \$7 billion. The \$7 billion Revenue Anticipation Note (RAN) issued last Fall is covering this short-term deficit. The cash report shows an outstanding loan balance of \$8.1 billion, which includes the \$7 billion RAN as well as a \$1.1 billion loan from special funds that was necessary for the school apportionment payment in April.

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Estimated Taxes

Estimated tax payments are generally filed quarterly to pay taxes due on income not subject to withholding. This can include income from self-employment, interest, dividends, gains from asset sales, or if insufficient income tax is being withheld from a salary, pension, or other income.

Payroll Withholding Taxes

"Payroll Withholdings" are income taxes that employers send directly to the state on their employees' behalf. Those amounts are withheld from paychecks during every pay period throughout the calendar year.

Economic Recovery Bonds

Voters approved \$15 billion in recovery bonds for State operations when they adopted Proposition 57 in 2004. The final \$3.3 billion were sold in February to cover projected shortfalls in future budget years.

Revenue Anticipation Notes

Traditionally, to bridge cash gaps the state borrows money in the private market by issuing Revenue Anticipation Notes (RANs). RANs are repaid by the end of the fiscal year.

Table 3: General Fund Cash Balance As of April 30, 2008 (in Millions)

	Actual Cash Balance	Governor's Budget Estimate	Actual Over (Under) Estimate	Budget Act Projection	Actual Over (Under) Projection
Beginning Cash Balance July 1, 2007	\$2,462	\$2,462	\$0	\$2,462	\$0
Receipts Over (Under) Disbursements to Date	(\$9,479)	(\$13,077)	\$3,598	(\$12,707)	\$3,229
Cash Balance April 30, 2008	(\$8,116)	(\$10,615)	\$2,499	(\$10,245)	\$2,129

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The RAN will be repaid by the end of the fiscal year with a combination of available cash and borrowable resources. Internal loans will be repaid according to cash management procedures as resources are available.

⇒ Of the largest expenditures, \$69.5 billion went to local assistance and \$23.6 billion went to State operations (See Table 4).

Table 4: General Fund Disbursements, July 1, 2007-April 30, 2008 (in Millions)

Recipient	Actual Disbursement	Governor's Budget Estimate	Actual Over (Under) Estimate	Budget Act Projection	Actual Over (Under) Projection
Local Assistance	\$69,503	\$71,569	(\$2,065)	\$68,120	\$1,383
State Operations	\$23,556	\$23,157	\$399	\$22,862	\$693
Other	\$2,313	\$3,218	(\$905)	\$4,203	(\$1,890)
Total Disbursements	\$95,372	\$97,944	(\$2,572)	\$95,185	\$187

Borrowable Resources

State law authorizes the General Fund to internally borrow on a short-term basis from specific funds, as needed.

How to Subscribe to this Publication

This Statement of General Fund Cash Receipts and Disbursements for April 2008 is available on the State Controller's Web site at www.sco.ca.gov. To have the monthly financial statement and summary analysis e-mailed to you directly, sign up at www.sco.ca.gov/ard/cash/email-sub.shtml.

Any questions concerning this Summary Analysis may be directed to Hallye Jordan, Deputy Controller for Communications, at (916) 445-2636.

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Featured Articles on California's Economy

Controller John Chiang's Council of Economic Advisors informs the Controller on emerging strengths and vulnerabilities in California's economy, major issues and trends that may affect the State's fiscal health, and how to make the best use of limited government revenues and resources.

The advisors also contribute monthly articles on issues regarding California's economy. The opinions in the articles are presented in the spirit of spurring discussion and reflect those of the authors and not necessarily the Controller or his office.

This month, we are reporting a summary of the meeting of the Council, held on May 2, 2008. To further illustrate the state's economic position, this section also includes charts showing various indicators such as employment growth, construction activity, and housing sales.

Meeting of Controller Chiang's Council of Economic Advisors: May 2, 2008

The Controller and his executive staff meet with the Controller's Council of Economic Advisors twice a year. Advisors attending the meeting this month were Esmael Adibi, Christopher Thornberg, Ross DeVol and Robert H. Edelstein. The morning session was a round table on the economy and budget issues. In the afternoon, guest speakers discussed affordable housing and health care for the growing elderly population.

The Economy

There was consensus that both California and the nation's economy are in recession. The only divergence was the expected magnitude and duration of the downturn. Among the points made by the Council:

- ◆ Housing is still in decline; building, sales and prices continue to fall. Estimates of expected price declines (peak to trough) ranged from 15% to 50%. Housing will continue to be a drag on the economy for at least the remainder of this calendar year.



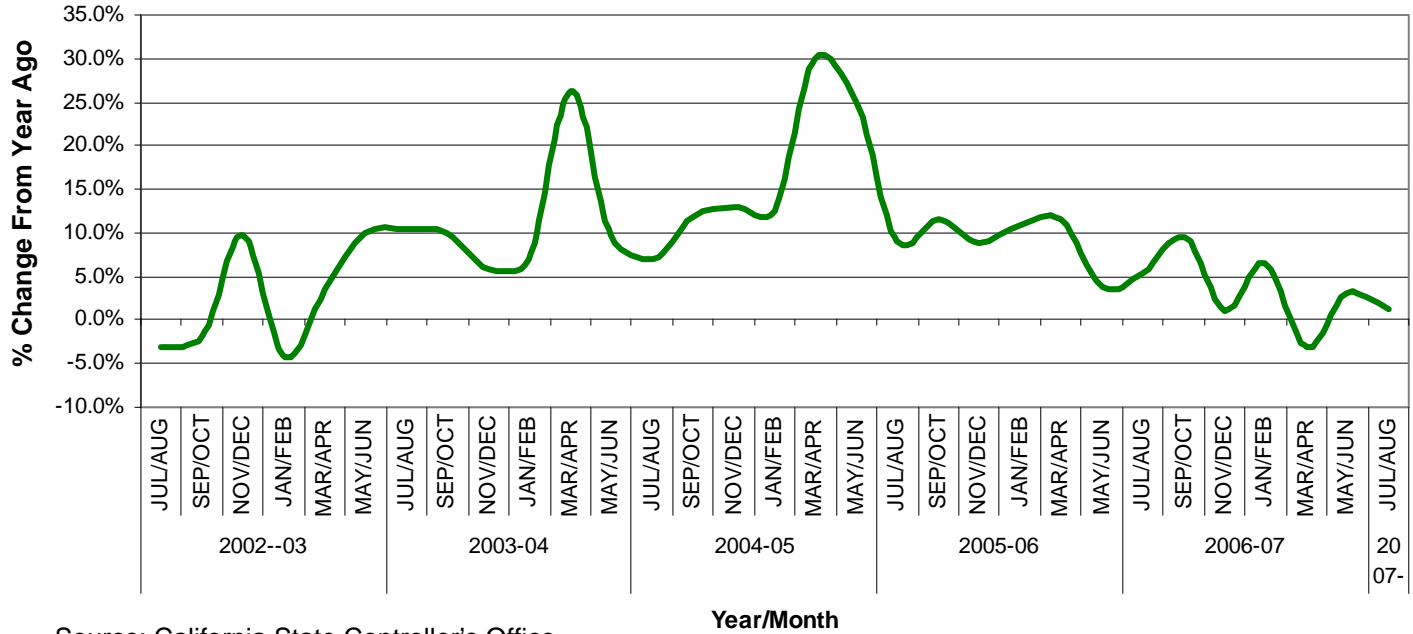
- ◆ Foreclosures are at record levels and will not level off until sometime after the peak of adjustable rate mortgage resets later this summer. Usually foreclosures rise at the end of a recession - not at the beginning. The high levels so early in the downturn increases the risks to the housing market.

- ◆ The April jobs report showed a loss of only 20,000 jobs in the U.S. - a much larger loss was expected. But that number is likely to be revised downward. Among the anomalies in the report: retail jobs increased in April. Retail sales are weak - it is hard to believe that hiring actually occurred in that sector.

- ◆ Estimates of maximum unemployment rates in California over the next 18 months ranged from 6.3% to 8.5%.
- ◆ Consumer spending will continue to be depressed. Consumption was fueled by an unsustainable growth of debt, primarily borrowing against home equity. The economy

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**Year Over Year Change in Revenue Receipts
For State Sales, Personal Income and Corporate Taxes
Bi-Monthly Totals**



Source: California State Controller's Office

**California Employment Growth
Year over Year Percent Change in Total NonFarm Jobs**



Source: California Employment Development Department

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will not stabilize until spending is consistent with incomes.

- ◆ Exports have added to economic growth this year. The weak dollar has helped exports but has increased the price of oil for the U.S. California is being negatively impacted by the decline of imports since we serve as the point of entry for a large proportion of imports.
- ◆ Bank losses are at \$300 billion and climbing. Regional banks are in trouble. There may be 200 to 300 bank failures over the next year. Auto, home equity and commercial loans are seeing increasing problems.

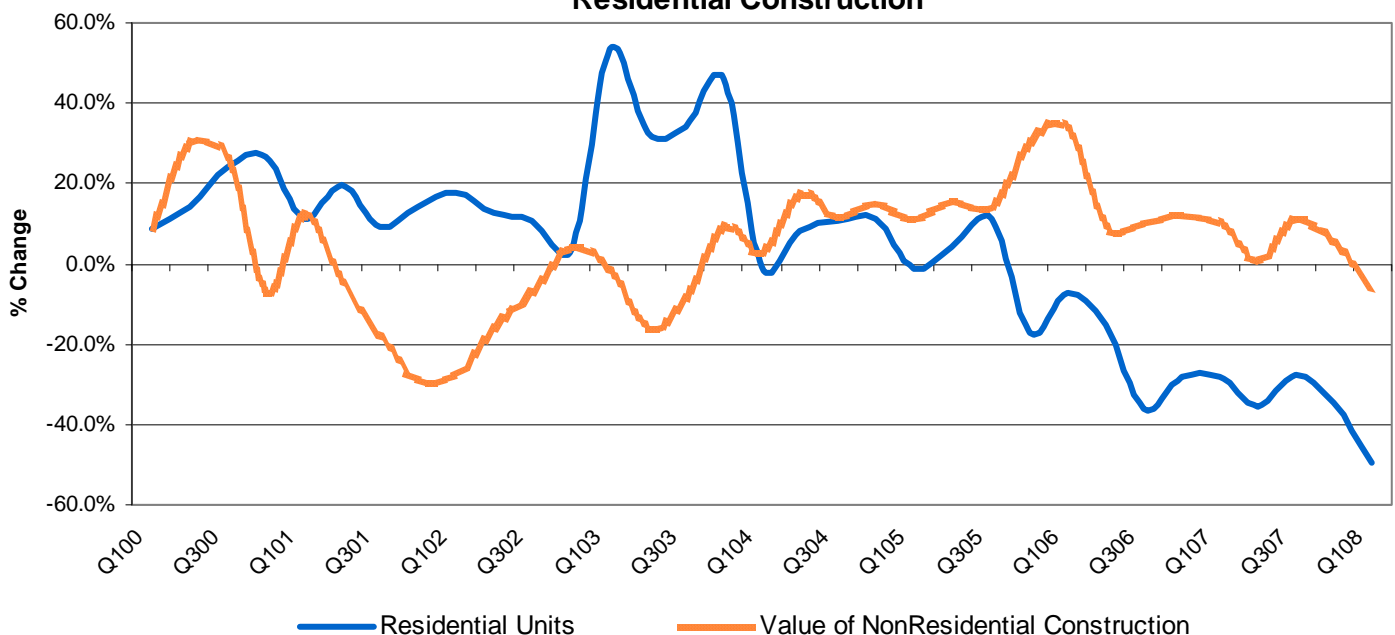
The Budget

The focus was on smoothing out the boom/bust cycle in the California budget. The spending patterns of the State are cyclical – more money is spent during expansionary periods and more services are cut during contractions. Among budget topics discussed were:

- ◆ Controller Chiang's proposal to remove a major portion of capital gains from personal income tax revenues, as capital gains create most of the volatility in General Fund revenue.
- ◆ Using one-time revenue windfalls only for one-time expenditures.
- ◆ Using the growth of wage and salary income to determine how much personal income tax should be for General Fund programs. Taxes derived from capital gains could be placed in a Rainy Day Fund to supplement state finances during economic downturns.
- ◆ Extending sales taxes to services – sales taxes are less volatile and services are an increasing share of personal expenditures.
- ◆ Limiting growth in General Fund expenditures to an average of revenue growth over a 10-year time period, as proposed in the Governor's Budget.
- ◆ Planning better, which would require multi-year forecasts and budgets.

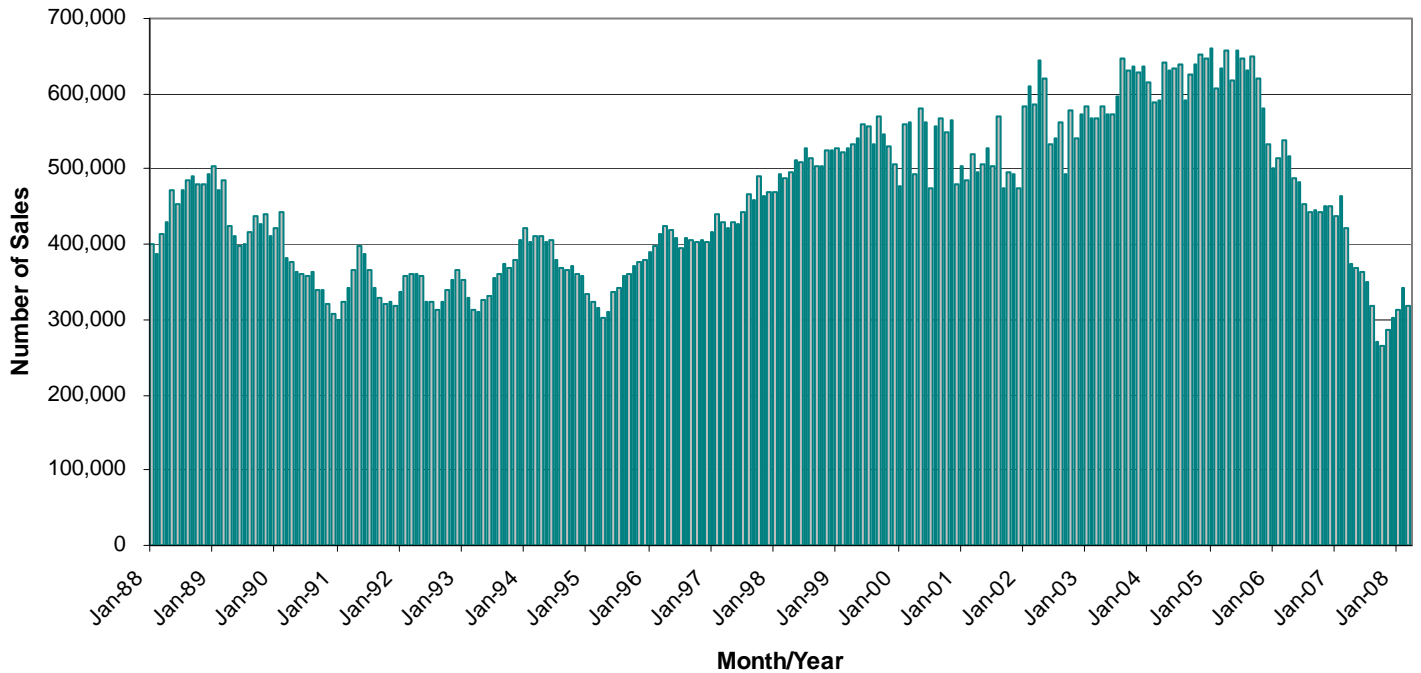
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Construction Activity in California
Year Over year Change in Residential Units Constructed and the Value of Non-Residential Construction



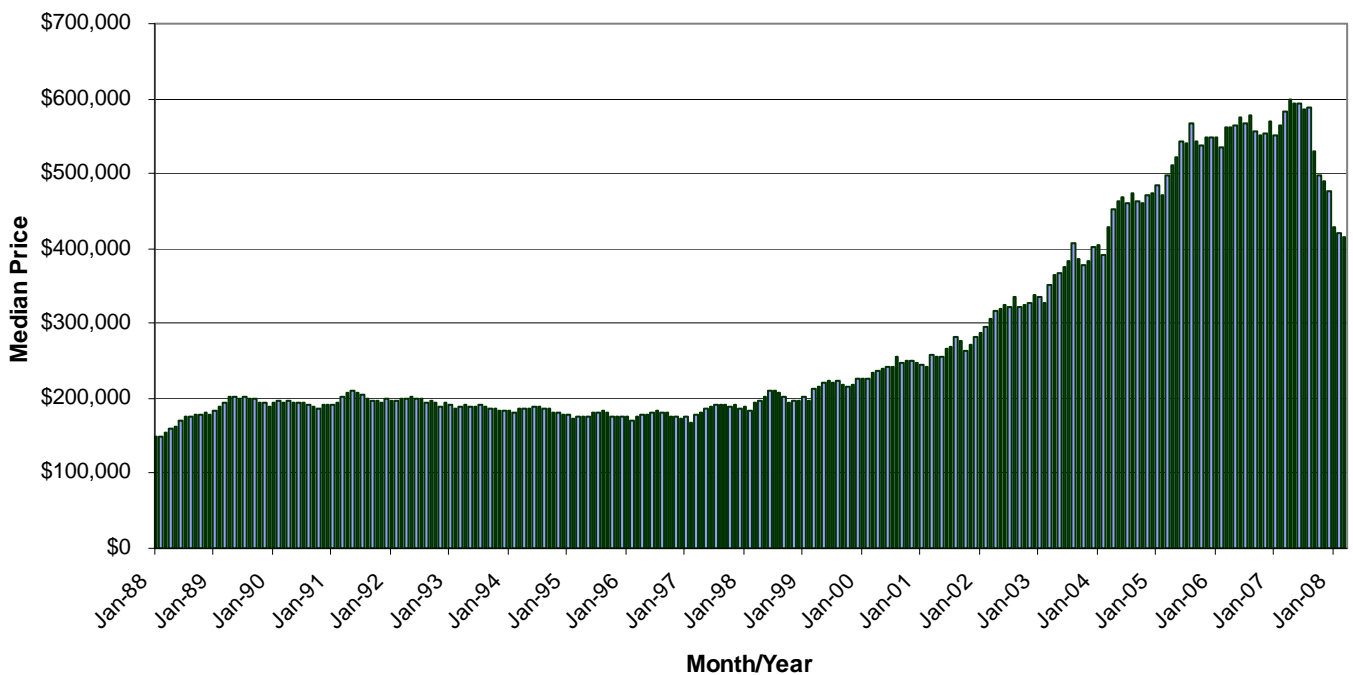
Source: Construction Industry Research Board

Monthly Sales of Single Family Homes in California Seasonally Adjusted



Source: California Association of REALTORS

Median Price of Single Family Homes in California



Source: California Association of REALTORS

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Affordable Housing

Tax credits are available to induce owners and investors to provide affordable housing. Participants must make the units available at affordable rents for an extended period of time. These tax credits are awarded on a competitive basis by the California Tax Allocation Committee. Two types of tax credits are available. The “9%” (of present value of the property) credit is designed so that 70% of the present value of the project can be used as a tax credit over a period of 10 years. The “4%” of present value credit is designed so that 30% of the present value of the project can be used as a tax credit over 10 years. The “9%” projects are typically new construction while the “4%” projects are usually rehabilitations.

Developers submit proposals to the Tax Allocation Committee and awards are made on a competitive basis. In 2007, there were 202 applications for the 9% credits, of which 70 projects were awarded the credits. The \$830 million in federal/state credits will result in the construction of 4,500 affordable units. There were 119 awards of 4% credits. The \$949 million in federal/state credits will result in the rehabilitation of 13,600 units to be offered as

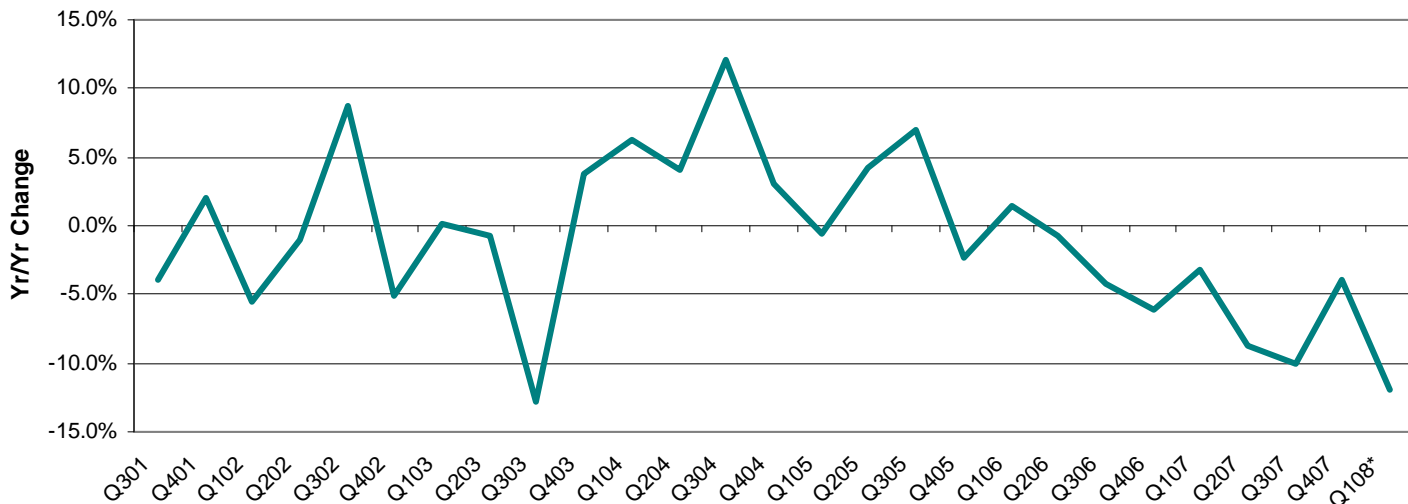
affordable housing. Panelists also discussed easing or eliminating parking space requirements to significantly lower developers’ construction costs for affordable housing.

Health Care for the Aging Baby Boomers

About 11% of Californians today are over 65 years old. In 20 years, that population will grow to almost 18%. The American medical system is not prepared to care for the impending tsunami of elderly patients. Currently, elderly poverty rates in California are low – 6.2% in 2006. However, 27.6% of Californians aged over 65 are classified as “near poverty.”

Disability rates and overall health of the elderly have improved over the past decade. This is good news since the cost of long term care for the elderly is a significant cost for states. More focus is needed on health issues that contribute to the elderly requiring nursing home care. Fragmentation of the health delivery system results in reduced oversight of patient care. An integrated information system could prevent medication mistakes and overlap/duplication of services. Use of technology to track care also might help identify effective programs and service patterns.

**New Auto Registrations
Year Over Year Quarterly Change in California**



Source: California Department of Motor Vehicles

Quarter