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Arnold Schwarzenegger

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FACT SHEET

08/20/2008

Governor Schwarzenegger Proposes a Budget Compromise

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The Governor today is offering the Legislature a compromise proposal on a state budget that responsibly addresses California's remaining \$15.2 billion budget shortfall and reforms our broken budget system. The Governor's compromise proposal protects education funding, maintains important safety net programs, does not borrow funding from local government or transportation, and avoids massive out-year deficits. The key components of this compromise are as follows:

REAL BUDGET REFORM

A Strong Rainy Day Fund

- Increases the size of California's Budget Stabilization Account (BSA) from 5 percent of General Fund expenditures to 12.5 percent -or approximately \$13 billion dollars today.
- Requires annual transfers to the BSA of 3 percent of General Fund and eliminates the ability to suspend those annual transfers. In years when the BSA is full (at 12.5%), the annual transfer is reduced to 1.5 percent. During economic downturns, when funds can be drawn out of the BSA, the transfer would not occur.
- In addition to the annual transfer of 3 percent of General Fund to the BSA, the compromise proposal requires that all current-year revenue above the amounts included in the Budget Act be transferred to the BSA, after first providing funding to education as required under Proposition 98. This would mean that any unexpected spike in revenues that occur during the fiscal year - normally recognized in the Governor's May Revision - would be transferred to the BSA.
- Funds could only be transferred out from the BSA under the following conditions: 1) actual revenues during the Fiscal Year must be below a specified level: prior year spending adjusted by population growth and per capita personal income growth; 2) funds transferred from the BSA back into the General Fund must be appropriated in a stand-alone urgency bill, subject to a 2/3rds vote of the Legislature. The amount transferred out of the BSA during a fiscal year would be limited to the amount which would bring revenues up to prior year spending adjusted by population and per capita personal income growth.
- When the balance in the BSA reaches 12.5 percent, the excess would be available for one-time purposes only. One-time purposes would include: paying down debt, paying off outstanding General Obligation bonds, investing in infrastructure and capital outlay projects, paying for "settle-up" dollars owed to education, pre-paying health care liability for retired employees (OPEB), and tax relief.

Mid-Year Reduction Authority

- Authorizes the Director of Finance to do the following when s/he determines, mid-year, that revenues have fallen below specified levels:
- Reduce state operations budgets by up to 7 percent without modifying or suspending the law.
 - Freeze Cost of Living Adjustments (COLAs), rate increases or increases in state participation in local costs, as designated in the Budget Act, for up to 120 days.
 - Requires the governor to submit urgency legislation to permanently suspend COLAs and other rate increases. If the governor fails to act within the 120 days, or the Legislature fails to adopt the suspension, the COLAs and other rate increases are reinstated.

ADDITIONAL BUDGET CUTS

- Makes an additional \$2 billion in cuts on top of the reductions adopted by the Conference Committee Report, for a total of \$9.9 billion in spending reductions in 2008-09 (total expenditure reductions over the two years would be \$11.3 billion).
- Freezes spending year-over-year for the second year in a row, while protecting public safety, education funding, and important safety net services.

LOTTERY MODERNIZATION AND SECURITIZATION

- Proposes a ballot measure to modernize the state Lottery and improve the performance of this underperforming state-owned asset.
- Future proceeds of an improved state Lottery would be securitized (estimated to be approximately \$5 billion in 2009-10) with the additional revenues used to pay down debt and fill the rainy-day fund in the out-years.

LAW ENFORCEMENT FUNDING

- Makes technical changes to expedite construction of prison beds under AB 900.
- Restores funding to the May Revision level for most local law enforcement programs.

EDUCATION FUNDING

Funds the Proposition 98 guarantee at \$57.8 billion - \$1.2 billion higher than the current-year funding. This level of funding eliminates the proposed reductions in the Governor's May Revision and maintains funding to base categorical programs such as class size reduction, special education, child nutrition programs and child care; and provides a partial COLA of \$300 million.

TAX PACKAGE / TEMPORARY INCREASE / PERMANENT REDUCTION

Proposes a revenue package that includes a temporary increase and permanent reduction to the state sales tax. The package includes:

- A temporary 1-cent sales tax increase for three years (excluding diesel, gasoline and jet fuel) followed by a permanent 1¼-cent reduction beginning in year 4. The additional ¼-cent reduction would be a permanent base sales tax reduction beginning when the 1-cent increase is no longer in effect.
- A two-year suspension of the Net Operating Loss (NOL) tax deduction: Suspends for two years the ability of corporations to reduce their tax liability based on prior losses and phases in

conformity to federal law over three years starting in 2010 by allowing losses to offset profits in two prior years; also extends the period for carrying forward losses from 10 to 20 years.

- Modified Tax Amnesty Proposal to generate revenues while avoiding negative impacts on economic activity.
- Better align accrual of revenues and accrual of spending.

ECONOMIC STIMULUS

Proposes an economic stimulus package to stem job losses, facilitate creation of new jobs, and improve tax revenues:

- Expedites the allocation and disbursement of existing transportation, housing and water bond funds to stimulate economic growth and job creation immediately.
- Authorizes new lease revenue bonds to accelerate capital outlay projects for higher education and the Courts.
- Provides statutory authority to develop public-private partnerships with design-build authority to add new, and accelerate existing, infrastructure projects (Caballero (AB 1261) and Niello (AB 2600) bills).
- Provides flexibility in overtime laws to allow employers and employees to agree on mutually acceptable flexible work schedules:
 - Allows employees to voluntarily work four 10-hour shifts without requiring overtime. All hours worked above 10 hours per day or 40 hours per workweek pay time and a half. All hours worked above 12 hours per workday and in excess of 8 hours on a fifth, sixth or seventh day in a workweek pay double time. Flexible work schedule must be voluntary for employee. Exemptions for union and government employees.
 - Creates a highly compensated employee exemption for California that conforms overtime rules to federal law (\$100,000 or more).
 - Exempts high-paid software engineers in the competitive technology industry from overtime rules; applies only to employees whose primary duty includes non-manual work.
 - Provides clarification to on-duty personnel such as armored car drivers, security guards, etc., regarding meal periods.
- Targeted tax credits to retain jobs and encourage job expansion in California.
 - Runaway Hollywood production tax credit.

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