THE 2005-2006 STATE BUDGET

Borrowing and Cost Deferrals

The 2005-06 Governor's Budget proposes General Fund revenues and transfers totaling $83.8 billion and expenditures of $85.7 billion. Consequently, the proposed budget has an explicit operating shortfall of almost $2 billion—even with the significant spending reductions proposed by the Governor. The budget fills in this explicit operating shortfall primarily with more borrowing--$1.7 billion of additional Economic Recovery Bonds (drawing down the reserve covers the remainder of the shortfall). However, there is much more borrowing embedded in the budget. Some of this borrowing is in the form of revenue that the General Fund will repay later, and some is in the form of cost deferrals. The major elements of General Fund budgetary borrowing or deferrals are as follows:

- $1.7 billion of additional Proposition 57 Economic Recovery Bonds. This would leave approximately $2 billion of remaining unused bond authority out of the $15 billion of Economic Recovery Bonds authorized by Proposition 57.

- $765 million from the issuance of Pension Obligation Bonds that were authorized in the current-year budget. The bond proceeds will be used to pay for the state's regular employer contribution on behalf of state employees to the Public Employees Retirement System (PERS). However, due to litigation challenging the bonds, the budget now assumes that these bonds will be issued in fiscal year 2005-06.

- $464 million from proposed "Judgment Bonds" that the state would issue to fund a settlement of the *Paterno* lawsuit concerning state responsibility for the 1986 levee breaks and flooding north of Sacramento.

- $1.3 billion from the suspension of the Proposition 42 transfer of gasoline sales tax funds from the General Fund to various transportation accounts in fiscal year 2005-06. The budget proposes to repay this amount over 15 years, as part of its Budget Reform proposals. Existing law also requires the General Fund to repay a total of $2.1 billion of previous transportation loans in fiscal year 2007-08 and 2008-09. These repayments also would be extended over 15 years under the Budget Reform proposals. In the interim, bonds would be sold, backed by the General Fund loan repayments, in order to maintain funding for transportation projects. These bonds would be in addition to $1.2 billion of bonds backed by future revenues from tribal gaming that now are planned to be sold in fiscal year 2005-06 to repay other previous transportation loans to the General Fund.

- $250 million from the deferral of payments to reimburse local governments for their costs of carrying out state mandates. In addition, the Budget Reform proposal would extend the payment period for approximately $1 billion of previously deferred mandate reimbursement payments to 15 years. Current law requires the state to pay these obligations over a 5-year period from fiscal year 2006-07 through 2011-12.

- The Budget Reform proposals establish a 15-year period for the General Fund to repay a wide variety of existing loans from special funds (excluding transportation funds).

- $4.9 billion of Proposition 98 K-14 education obligations $3.6 billion for "maintenance factor" and $1.3 billion in "settle-up" payments—also would be paid over 15 years under the Budget Reform proposals. However, the Budget Reform proposals would offset these future costs with substantial reductions in future state Proposition 98 funding obligations.