California’s Budget Stalls, Bond Ratings Sink

"Moody’s believes that as the days and weeks go by without enacted solutions to the current cash crisis and the $26 billion budget gap, the risk to priority payments, and eventually debt-service payments, is increasing," Moody’s said in its rating report. "The downgrade incorporates the risk we believe exists at the current time, as well as the state’s inability to resolve the current difficulties in a timely fashion."

California began its fiscal year on July 1with a $26.3 budget shortfall and a declaration of fiscal emergency by Governor Arnold Schwarzenegger. The state also began issuing IOUs to vendors as well as taxpayers owed refunds. But by mid July many major banks were announcing that they would no longer cash the pay-you-later warrants. They include U.S. Bancorp, Bank of America Corp., Wells Fargo & Co., and JPMorgan Chase & Co.

By Friday, July 17, the budget impasse still had not been resolved, with Republicans insisting that the gap must be solved with spending cuts and the Democrats calling for more taxes. However, spokesmen for both Governor Schwarzenegger’s office and the legislature’s Democratic leadership said that progress was being made and they are hopeful that ongoing negotiations over the weekend will result in a budget agreement by Sunday night.

If the agreement involves higher taxes, there will surely be a major public backlash. In a special May election, outraged taxpayers sent a clear message to Sacramento, with a resounding 2 to 1 rejection of the five "budget reform measures" promoted by Schwarzenegger, a Republican, and the Democratic-controlled state legislature. All of those ballot measures would have allowed the spendthrift politicians to spend even more freely. The only ballot measure to pass was Proposition 1F, which prohibited pay increases for the governor, state legislators, and other state officers during years when the state budget is running a deficit.

State Layoffs That Aren’t Really Layoffs

One of the obvious ways to reduce the deficit would be to cut state spending by cutting some of the more than 230,000 state government jobs. In February, Governor Schwarzenegger warned that 20,000 state employees could lose their jobs if a budget deal were not soon reached. Since then, Californians have been subjected to a steady stream of stories about state layoffs and pink slips, leading most to believe that thousands of government workers actually have been laid off already. After all, virtually every company in the private sector has been forced to tighten its belt, and most — from major corporations to mom and pop businesses — have had to lay off employees.

But how many state government workers really have been laid off so far? The answer: Zero. That's right: none, nada, zilch. The political theater calls for the governor to announce layoff "warnings," which are then denounced by the state employees unions and reported by the media as if they are announcements of actual, imminent layoffs, not hypothetical-maybe-perhaps-possibly-someday-in-the-far-distant-future layoffs.

Here's a report from Channel 10/KXTV on July 16 that provides a window into the statistical legerdemain employed by the politicians regarding state employee layoffs:

> According to the California Department of Personnel Administration, no state workers have actually been laid off this year….
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> Last February, 28,000 layoff warnings went out to state employees. At least 6,000 workers have since taken other state jobs not paid from the general fund.
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> In May, 4,600 state employees received actual layoff notices which take effect in September if workers can't find other state jobs by then.

That's how the government layoff charade works in La-La Land, where the militant government employee unions have gained a lock-hold on the state legislature. Thousands of workers are given layoff "warnings" in February; by May a fraction of that number have received layoff "notices"; and by September *maybe* some of them actually will be laid off. But California has already run out of options, and the state will soon be forced to make painful cuts.

U.S. Congressman Tom McClintock (R-Calif.), a former California state senator, outlined the grim reality facing the Golden State in a July 10 speech to the Competitive Enterprise Institute. He noted:

> Today, California is like the shopkeeper who leased out too much space, ordered too much inventory, hired too many people and paid them too much. Every month the shopkeeper covers his shortfalls with borrowing and bookkeeping tricks. Ultimately, he will reach a tipping point where anything he does makes his situation worse. Borrowing costs are eating him alive and he's running out of credit. Raising prices causes his sales to decline. And there's only so much discretionary spending he can cut.
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> That's the state's predicament in a nutshell. California's borrowing costs now exceed the budget of the entire University of California and it is increasingly likely that it will fail to find lenders when it must borrow billions to pay its bills at the end of this month.
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> Ignoring dire warnings, Gov. Schwarzenegger and legislators from both parties earlier this year imposed the biggest state tax increase in American history.
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> And I can assure you that the Laffer curve is alive and well. In the first two months after the tax increase took effect, state revenues have plunged 33 percent.
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> Although there are many obsolete, duplicative or low priority programs and expenditures that the state can — and should — do without, there aren't enough of them to come anywhere close to closing California's deficit.
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> Sadly, California has reached the terminal stage of a bureaucratic state, where government has become so large and so tangled that it can no longer perform even basic functions.

Rep. McClintock, who for many years was almost a lone voice for fiscal sanity in the California legislature, ended his peroration with this warning to the nation:

And before anyone gets too smug at California's agony, remember this: Congress is now enacting the same policies at the national level that have caused the collapse of California. So whistle past this cemetery if you must, but remember the medieval epitaph: "Remember man as you walk by, as you are now so once was I; as I am now so you will be."

The good news is there is still time for the nation to avoid California's fate. If anything, the collapse of California can at least serve as a morality play for the rest of the nation — unfortunately in the form of a Greek tragedy.