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CALIFORNIA STATE TREASURER BILL LOCKYER

FOR IMMEDIATE RELEASE
October 1, 2007

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Treasurer Lockyer Issues Report on State Debt That Takes 20-Year Look at Budget and Calls for Action Now to Fix Deficit

Landmark Report Cites $14.6 Billion Shortfall as Obstacle to Needed Investment

SACRAMENTO – State Treasurer Bill Lockyer today issued a landmark report that looks at California's budget 20 years into the future, provides a new, long-range fiscal planning view of infrastructure investment and debt affordability, and urges policymakers to fix a structural budget deficit that could grow to $14.6 billion by 2027-28.

"Business as usual is not an option – not for our children and not for the next generations who deserve our best effort to build a better state," said Lockyer. "We need to repair our decayed infrastructure and strengthen it for the growth that's coming. To put ourselves in the financial position to make that investment, and maintain crucial programs, we need to lengthen our planning sights, look at debt affordability in a new way and act now to shore up our fiscal house. The good news is that we can accomplish the task. But success will require hard work and intelligent choices."

The report, *"Looking Beyond the Horizon: Investment Planning for the 21st Century,"* offers a California debt affordability planning model unprecedented in two respects. First, it provides a 20-year planning horizon. Second, it bifurcates projected General Fund spending between debt service payments and operating expenditures. Lockyer said the new approach provides a clearer picture of the General Fund's capacity, over the long term, to cover both investment and program needs. Among the report's major findings:

- Total General Fund revenues will increase from $107.1 billion in 2008-09 to $253.8 billion in 2027-28. Over the same period, the General Fund budget for operating expenditures (excluding debt service payments) will grow from $106.8 billion to $252.6 billion.

- Through 2027-28, the State will issue $224 billion of new General Fund-backed debt to finance infrastructure development. The annual cost to the General Fund to pay debt service will grow from $5.3 billion in 2008-09 to $15.8 billion in 2027-28. The report makes no judgment on whether the $224 billion will be sufficient.

- The amount of General Fund revenues available, after subtracting operating expenditures, to pay debt service starts at $269 million in 2008-09, peaks at $7.1 billion in 2011-12, then gradually declines to $1.2 billion in 2027-28.

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- By 2027-28, the State's General Fund balance sheet will show a gap of $14.6 billion between the amount needed to pay debt service ($15.8 billion) and the amount of General Fund revenues available ($1.2 billion) after subtracting operating expenditures. In other words, the State will face a $14.6 billion shortfall between how much General Fund revenues it takes in and how much it needs to pay for both debt service and operating expenditures.

Over the 20-year period, according to the report, the budget imbalance works out to an average annual revenue deficit of 3.5 percent. A gap of that size can be closed, the report says. But it adds, "The Governor, the Legislature, the Treasure – all Californians – need to start that work now. In this endeavor, there should be no sacred cows, only a commitment to providing the means to build a better California."

To eliminate the structural budget deficit, the report says, the Governor and Legislature have three routes open to them: "They can raise revenues, cut expenditures or take meaningful steps to make government operate more efficiently." The report discusses numerous ideas that have been offered on both the revenue and expenditure side of the budget. Those proposals include lessening the life-cycle costs of government facilities by increasing energy efficiency, reducing criminal recidivism and broadening the sales tax base by extending it to certain services.

To ease pressures on General Fund revenues, the report notes the Treasurer's Office is taking steps to reduce and manage the costs of issuing debt. The report urges the Legislature and Governor to give the Office more tools to structure debt to give taxpayers the best possible deal.

The State also could free up General Fund revenues by funding infrastructure development and operation through user-pays financing. The user-pays debate frequently includes a discussion of public-private partnerships, or P3, under which private entities own or operate facilities. But the report stresses user-pays financing can be accomplished without the use of private capital or ownership. Financing transportation infrastructure with revenue bonds also would provide relief to the General Fund, the report says. The report recommends the Legislature create a California Transportation Financing Authority (CTFA) to issue revenue bonds to support publicly-owned and operated highways. The bonds could be backed by a variety of revenue sources such as the State gas tax, local transportation sales taxes, tolls and developer fees.

The report adopts a fundamentally different approach to measuring debt affordability. Traditionally, the yardstick has been numerical. The most prominently used measurement has been debt service payments as a percentage of General Fund revenues, with the limit typically set at around six percent. Unlike prior versions, the 2007 report analyzes the flaws in numerical measurements. It notes, for example, that while the State's budget deficit in the final year of the forecast will be an estimated $14.6 billion, debt service payments will consume only 6.3 percent of General Fund revenues.

"The right amount of debt for California is not reflected in a single number," the report concludes. "It is not indicated by any one ratio or percentage. The right amount of debt for California is a policy choice. If we decide capital investment is important, then we should take appropriate actions, consistent with other priorities, to ensure we can make those investments."

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