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# *The* FISCAL REPORT *an informational update*

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## **State Controller John Chiang Releases Disappointing October Revenue Report**

*[Editor's Note: "We report the cash receipts number as calculated by both the State Controller's Office (SCO) and the Department of Finance (DOF). The SCO generally reports earlier. The DOF number is generally issued later, but is more comprehensive, and is the number upon which decisions are made regarding the "triggers." We look forward to reporting the DOF number next week."]*

Today, November 10, 2011, State Controller John Chiang released his November 2011 Summary Analysis of October General Fund cash receipts and disbursements with the statement, "October's poor revenues capped a very disappointing first four months of the fiscal year. Unless revenues and expenditures begin to track with projections, the state will face increasing cash pressure in the months ahead."

According to the Controller's report, after accounting for October revenues, total year-to-date General Fund revenues are now behind the 2011-12 State Budget estimates by \$1.5 billion and expenditures are over projections by \$1.7 billion.

Total General Fund revenues in October 2011 were \$810.5 million lower than expected, with personal income taxes showing particular weakness as they came in \$451 million (-12.9%) lower than anticipated. The net \$1.5 billion shortfall year-to-date for the first four months of the 2011-12 fiscal year is more than 6% below the June estimates upon which the Budget was based.

The June adopted Budget assumed an additional \$4 billion of state revenues above the economic-based forecast of the May Revision, and the Department of Finance attributed \$1.038 billion of that increase to the first four months of the fiscal year. Significant cuts to K-14 education funding are triggered if revised revenue forecasts, released in November by the Legislative Analyst's Office and in December by the Department of Finance, are \$2 billion or more short of the Budget estimates.

The Controller's report did note that recent employment numbers may point to a substantially better economic picture ahead. The last few months of data saw solid gains along with upward revisions of earlier releases. Overall, the state added close to a quarter-million jobs over the course of the past year—nearly a 1.8% growth. The unemployment rate fell to 11.9%, down from 12.1% in August. The report also noted that one factor preventing California from experiencing faster growth is a mismatch of skills in the labor market. A Beacon Economics report stated, "There is a real dichotomy between the skill sets of the workers in those sectors that were pummeled by the downturn and the skill sets required by the sectors that are leading California out of the recovery." If true, this points to the importance of relevant and readily available skill-based education programs for the unemployed.

The Controller's summary report can be viewed by clicking [here](#).

—*Michael Ricketts*

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## October Revenues Fall Well Below Forecast

State General Fund revenues for the month of October fell \$608 million below the budgeted level, a shortfall of 10.5% from what was expected, making this the fifth consecutive month that collections have fallen short. The Department of Finance's (DOF's) *Finance Bulletin*, issued on November 14, 2011, indicates that year-to-date collections are now \$1.275 billion below the budgeted level through October, a shortfall of 5.1%.

The report indicates that in addition to the May Revision baseline forecast of \$5.511 billion for October, the current year budget anticipated an additional \$263 million, which is related to the \$4 billion added by the Legislature to close the Budget gap. Thus, October receipts were expected to reach \$5.774 billion, after adjusting for the Legislature's revenue augmentation. Actual collections, however, did not even reach the May Revision baseline forecast, missing that mark by \$345 million. This latest revenue development increases the risks that the mid-year expenditure trigger will be pulled.

The *Finance Bulletin* shows that of the three major taxes, the personal income tax was the weakest performer, falling short 10.6%, or \$362 million, with most of this related to a shortage in income tax withholding. The report, however, is misleading because it fails to allocate the \$263 million added by the Legislature for the month of October. After we adjust for the Legislature's assumed boost in revenues, actual collections for October are even more disappointing, showing that the personal income tax fell short almost 15% rather than 10.6% displayed in the *Finance Bulletin*; the sales and use tax came in only slightly up at 2.2% rather than the 7.3% reported; and the corporation tax missed the mark by 5.4% rather than hitting the mark as the report implies.

On a year-to-date basis, after adjusting for the Legislature's revenue augmentation, we find that the personal income tax and the sales and use tax are running short by about 3.7%, or almost \$800 million combined. The corporation tax is short more than 16%, or \$313 million; however, some of this may be attributed to cash flow timing.

(Note: Last week, State Controller John Chiang indicated that state revenues for October came in \$810.5 million below the budgeted level, significantly worse than the *Finance Bulletin* now shows. Similarly, the State Controller's Office (SCO) report overstated the revenue shortfall for September by \$240 million. We continue to caution clients about reading too much into the SCO reports, since they are prone to significant differences from the DOF totals.)

The *Finance Bulletin* also acknowledges some positive developments on the jobs front, highlighting an employment gain of 11,800 jobs in September and a net upward revision of 21,100 jobs gained in August (see "California Adds Jobs in September and the Unemployment Rate Drops," in the October 28, 2011, *Fiscal Report*).

Finally, the DOF report notes continuing weakness in the construction and housing markets. Single-family residential construction posted its ninth consecutive month of year-over-year losses and non-

residential construction suffered a 10% decline compared to October 2010. The median price of an existing home sold in September 2011 was \$287,440, down 8.3% from September 2010.

(Note: The Legislative Analyst's Office is expected to release their current year revenue forecast and trigger assessment on Wednesday, November 14, 2011. We will have a full summary of that report and our commentary shortly after its release.)

—*Robert Miyashiro*

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