



## Economic and Revenue Developments

### Revenues Up Nearly \$1.1 Billion In Current Year

General Fund revenue collections in April from all sources were up \$704 million above the January Governor's Budget projection for the month. Given that collections through March were up \$380 million, cumulative receipts through April are nearly \$1.1 billion above the budget projection.

### Sources of the Gain

Most of the gains both during April and for first ten months of 1995-96 are from higher-than-expected personal income tax payments. However, as shown in Figure 1, all three of the major taxes are running ahead of the January forecast.

**Figure 1**

#### April General Fund Revenue Collections

(In Millions)

Revenue Source	April 1996			1995-96 Year to Date		
	January Estimate	Actual	Difference	January Estimate	Actual	Difference
Personal Income	\$3,462	\$3,842	\$380	\$17,390	\$17,973	\$583
Sales and Use	708	958	250	12,005	12,361	356
Bank and Corporation	817	875	58	4,540	4,616	76
Other <sup>a</sup>	450	466	16	2,802	2,871	69
<b>Totals</b>	<b>\$5,437</b>	<b>\$6,141</b>	<b>\$704</b>	<b>\$36,737</b>	<b>\$37,821</b>	<b>\$1,084</b>

<sup>a</sup> Data are preliminary.

Specifically:

- ❖ *Personal income taxes* were up \$380 million in April, and are now \$583 million above the estimate in cumulative terms. The cumulative gain is related to both stronger-than-predicted final payments on 1995 returns, as well as consistently higher-than-expected withholding payments.
- ❖ *Sales and use taxes* were up \$250 million in April and are running \$356 million ahead in cumulative terms. Most of April's \$250 million gain is due to the earlier-than-expected processing of final tax payments on first quarter 1996 taxable sales. These final payments were due on April 30, and the monthly gain will largely be offset by lower "spill-over" collections in early May. Even after accounting for this cash-flow factor, however, the underlying trend in sales tax receipts is slightly stronger than anticipated in the January budget forecast.
- ❖ *Bank and corporation taxes* were up \$58 million in April, and are now \$76 million above the year-to-date estimate. These gains suggest that corporate profits in California are running slightly ahead of the budget forecast.

## Large Withholding Gains Imply Stronger Economy

The most positive revenue development over the past several months has been the consistently higher-than-expected levels of income tax withholding payments. April's withholding

receipts were 16 percent higher than last April's, while cumulative 1995-96 payments through April are running 9 percent ahead of last year.

Historically, the performance of withholding has been a good general indicator of the state of California's economy. For example, withholding fell sharply in the early 1990s, reflecting the severe nature of the recession that hit California at that time. Similarly, the current withholding gains provide encouraging evidence that the underlying trend in wages is stronger than previously thought. The withholding gains are especially strong in view of the elimination of the top 10 percent and 11 percent marginal state income tax brackets as of this January.

## Implications For 1995-96 Revenues

If current tax-related trends continue over the near term, most of the current \$1 billion-plus revenue gain would be expected to hold through the end of 1995-96. In fact, a continuation into May and June of the recent trend of higher-than-projected withholding and quarterly prepayments would lead to further increases in personal and corporate tax receipts. Offsetting these pluses, however, are two negative factors. First, personal income tax refunds on 1995 final returns are running higher than expected, and this trend appears to be continuing in May. Second, as indicated above, collections data for early May suggest that much of the \$250 million increase in sales taxes during April will be offset this month.

## **Implications For 1996-97 Revenues**

The exact implications of the current-year revenue gains for the 1996-97 revenue outlook will depend on a variety of factors, including what the stronger revenue performance implies about the economic outlook for the remainder of 1996 and 1997. At this time, however, it appears that much of the current-year revenue gain may carry forward into the 1996-97 revenue base.

Later this month, the Administration will be releasing its May Revision to the January budget proposal. This revision will include revised economic and revenue projections for both the current and budget years. Shortly after the May Revision is released, our office will also update the economic and revenue projections for the current and budget years which we released in February.

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## **Public Safety Has Been Highest Local Funding Priority**

The recession of the early 1990s, combined with the shift of more than \$2.5 billion annually in property taxes to schools, has reduced the available revenues for California's 58 counties. At the same time, the recession resulted in increased demand for many social services. As a result, many counties have been forced to reduce the level of services they provide.

Recognizing the difficult financial condition of California's counties and the fact that public safety services could be compromised by the reduction in available resources, the Legislature placed Proposition 172 on the November 1993 ballot. This measure was in turn approved by the voters. Proposition 172 created a permanent, one-half cent sales tax for public safety purposes (generally the sheriff, district attorney, and probation departments). The Public

Safety Sales Tax generates more than \$1.5 billion for local public safety purposes each year, with 95 percent of this revenue going to counties.

### **How Has Public Safety Funding Fared?**

To see how public safety funding has fared in recent years, we surveyed seven counties (representing 50 percent of the state's population). We found that between 1992-93 and 1995-96 spending for public safety departments receiving Proposition 172 funding increased by an average of 7.9 percent. During this same period, counties' three largest general purpose revenue sources—the property tax, the sales tax (including Proposition 172 funds), and the vehicle license fee—increased by a combined total of just 3.2 percent. For comparison pur-

poses inflation during this period—as measured by the California Consumer Price Index—increased 5.9 percent (see Figure 2).

**Figure 2**

**Public Safety Spending, Revenues, and Inflation  
In Selected Counties<sup>a</sup>  
1992-93 Through 1995-96**

	Percent Change 1992-93 Through 1995-96
Public Safety Spending	7.9%
Revenues	3.2%
Inflation <sup>b</sup>	5.9%

<sup>a</sup> Includes Counties of Los Angeles, Orange, Alameda, Sacramento, San Mateo, Fresno, and Butte.

<sup>b</sup> California Consumer Price Index.

Within public safety departments, sheriffs' department budgets grew faster than all others. Spending on sheriffs' departments increased by 8.6 percent, while spending for other public safety departments covered by Proposition 172 increased by 5.2 percent.

## Funding Has Exceeded Minimum Requirements

Despite the slow growth in revenues resulting from the recession and the property tax shifts, counties have maintained public safety spending in excess of the minimum requirements of the maintenance-of-effort provision of the Proposition 172 implementing legislation, Chapter 886, Statutes of 1994 (AB 2788, W. Brown). This statute requires that counties increase spend-

ing for public safety departments above the 1992-93 funding level in accordance with growth in Public Safety Sales Tax revenues. Among a sample of 10 counties, spending for public safety exceeded the minimum requirements of the law by an average of 9.3 percent (see Figure 3).

**Figure 3**

**Counties Exceed Minimum Required  
For Public Safety Spending**

County	Percent in Excess of MOE <sup>a</sup>
Butte	10.5%
Fresno	13.8
Los Angeles	5.2
Merced	5.0
Monterey	12.6
Placer	3.3
Riverside	8.1
Sacramento	14.0
San Diego	17.0
Yolo	3.2
Average	9.3%

<sup>a</sup> Maintenance of effort.

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