

CALIFORNIA LEGISLATURE

1975-76 REGULAR SESSION

ANALYSIS OF THE BUDGET BILL

of the

STATE OF CALIFORNIA

for the

Fiscal Year July 1, 1975, to June 30, 1976

Report of the Legislative Analyst

to the

Joint Legislative Budget Committee

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LETTER OF TRANSMITTAL

925 L Street, Suite 650
Sacramento, California 95814
February 6, 1975

THE HONORABLE DONALD L. GRUNSKY, *Chairman*
and Members of the Joint Legislative Budget Committee
State Capitol, Sacramento

Gentlemen:

In accordance with the provisions of Government Code, Sections 9140-9143, and Joint Rule No. 37 of the Senate and Assembly creating the Joint Legislative Budget Committee, defining its duties and providing authority to employ a Legislative Analyst, I submit an analysis of the Budget Bill of the State of California for the fiscal year July 1, 1975, to June 30, 1976.

The duty of the committee in this respect is set forth in Joint Rule No. 37 as follows:

"It shall be the duty of the committee to ascertain facts and make recommendations to the Legislature and to the houses thereof concerning the state budget, the revenue, and expenditures of the state, and of the organization and functions of the state, its departments, subdivisions and agencies, with a view of reducing the cost of the state government, and securing greater efficiency and economy."

I should like to express my gratitude to the staff of the State Department of Finance and the other agencies of state government for their generous assistance in furnishing information necessary for this report.

Respectfully submitted,

A. ALAN POST
Legislative Analyst

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PRELIMINARY STATEMENT

In his Budget Message Governor Brown establishes the principle that "We cannot spend more than we take in during the coming year. The current surplus is a minimum reserve in a period of economic uncertainty . . . I will oppose any legislation which would reduce necessary revenues or raise general taxes . . ."

If we turn from the Governor's statement to the Budget document and examine the general budget summary contained in its first schedule, we see that the budget does, in fact, reflect a substantial balance between General Fund outgo and General Fund income. Revenue and transfers are shown to be \$9,174,540,141. Expenditures are only slightly in excess of that at \$9,176,385,982. Correspondingly, the schedule shows that the fiscal year is expected to begin with \$349.9 million in unrestricted surplus available for expenditure, and it will end with a General Fund unrestricted surplus of \$361.7 million.

It should also be noted that in addition to these beginning and ending balances there is federal revenue sharing available for appropriation. The amount in the Federal Revenue Sharing Fund at the close of the 1975-76 fiscal year is shown to be \$212,515,000. Thus, the combination of the General Fund balance and federal revenue sharing leaves the state at the close of the budget year, June 30, 1976, with \$574.2 million. Although federal revenue sharing is placed in a special fund which requires legislative appropriation, and in prior years it has been appropriated for school apportionments, the current receipts and the accumulated unexpended balance in the fund (\$212.5 million) can be appropriated by the Legislature for any purpose.

Except for the fact that the General Fund is proposed to be the beneficiary of a transfer of approximately \$77 million which under existing law would otherwise be deposited in the Capital Outlay Fund for Public Higher Education (the so-called COFPE Fund), the balance between revenues and expenditures has been achieved primarily by keeping the amounts appropriated to all major programs down to the level of minimum workload requirements and by introducing no major new programs. In addition, the budget, in our view, has been held down by underestimating the probable growth in welfare and Medi-Cal costs resulting from the high level of unemployment which the budget assumes will exist during most of the months of the fiscal year.

The budget for 1975-76 is subject to precarious economic forecasting. Most economists have generally assumed as this budget does, that although economic conditions will become worse during the first half of the calendar year 1975, they will improve throughout the budget year. The trough of the current recession is expected, in fact, to occur at about the beginning of the budget year. Although there is general agreement that

an upturn will take place during that fiscal year, there is considerable disagreement as to its exact timing. The point at which the reversal of the downward trend in the economy actually takes place and the rate at which recovery is achieved will obviously have a significant bearing on the realities of the balance struck between income and outgo in this budget. Any later or less rapid recovery than fits the budget assumptions will increase welfare costs and provide less revenue with which to fund such costs. A major portion of the General Fund surplus may, in fact, as the Governor recognizes, be consumed in the process of funding such deficiencies.

In preparing this analysis of the budget we have addressed each program with the objective of indicating all areas in which we think appropriate economies or reductions can be made. While our own earlier forecasts predicted the austerity of the budget picture and led us therefore to make a special effort to achieve reductions wherever possible, our recommendations were not tailored to any particular budget figure. Because the Governor followed the austerity principles which have been mentioned, generally speaking any reductions recommended by us will effectively reduce existing expenditure levels. We have, however, attempted not to reduce effective levels of service below those which appeared to be necessary to achieve basic objectives of the programs. In numerous instances we have, in fact, recommended some increases where we felt that the erosion of inflation was reducing the effectiveness of the program below that which the Legislature had intended and below the level which, in our judgment, was justified by the program objectives and performance.

In the pages that follow, before we begin our item-by-item analysis of the budget bill, we have incorporated a series of charts and tables which provide ready reference to the principal financial features of the budget. In addition, we have incorporated summaries of major program expenditures and a brief review of the economic assumptions and associated revenue estimates contained in the budget. As stated before, both economic assumptions and revenue estimates are extremely precarious at this time. Nevertheless, they are inherent in the fiscal balance achieved in the budget, and an understanding of them is essential if the Legislature is to carry out its own responsibility in respect not only to the budget but other proposed legislation which requires funding.

THE OVERALL PICTURE OF EXPENDITURES

The total state expenditure program for 1975-76 looks like this:

The total program is	<i>Millions</i> \$17,306
Composed of:	
1. General Fund	9,176
2. Special funds	1,872
3. Bond funds	254
4. Federal funds	6,004

In Table 1 this combined expenditure program is shown for the last two fiscal years and is compared with the budget year, 1975-76.

Table 1
State of California
Combined Expenditure Summary for Indicated Years

	1973-74	1974-75	1975-76
General Fund	\$7,299,436,389	\$8,427,630,092	\$9,176,385,982
Special funds	1,694,697,774	2,004,520,276	1,872,473,744
State budget expenditures	\$8,994,134,163	\$10,432,150,368	\$11,048,859,726
Bond funds	317,131,572	402,883,471	253,966,810
Overall state expenditures	\$9,311,265,735	\$10,835,033,839	\$11,302,826,536
Expenditures of federal funds *	5,005,579,857	6,034,781,569	6,003,517,262
Combined total expenditures	\$14,316,845,592	\$16,869,815,408	\$17,306,343,798

* Includes grants-in-aid, reimbursements and special projects.

CHART I

STATE BUDGET PICTURE

1975-76 FISCAL YEAR

(Dollars in Millions)

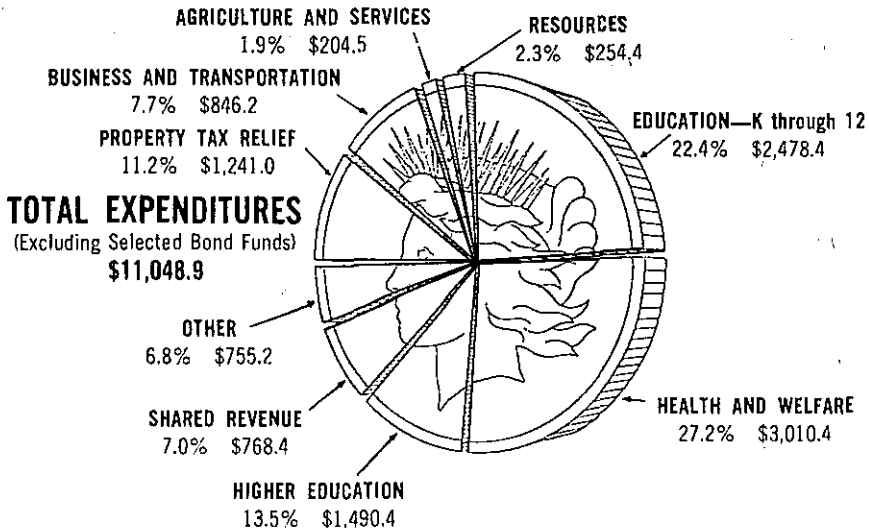
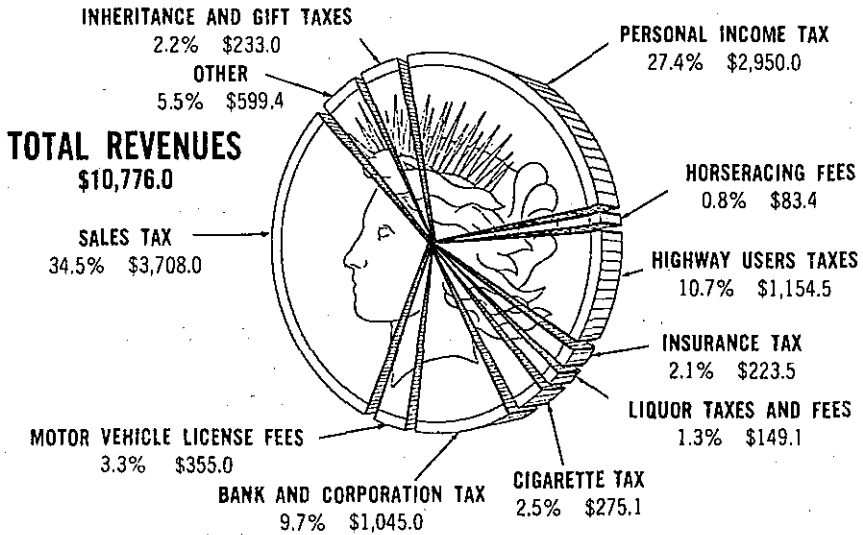
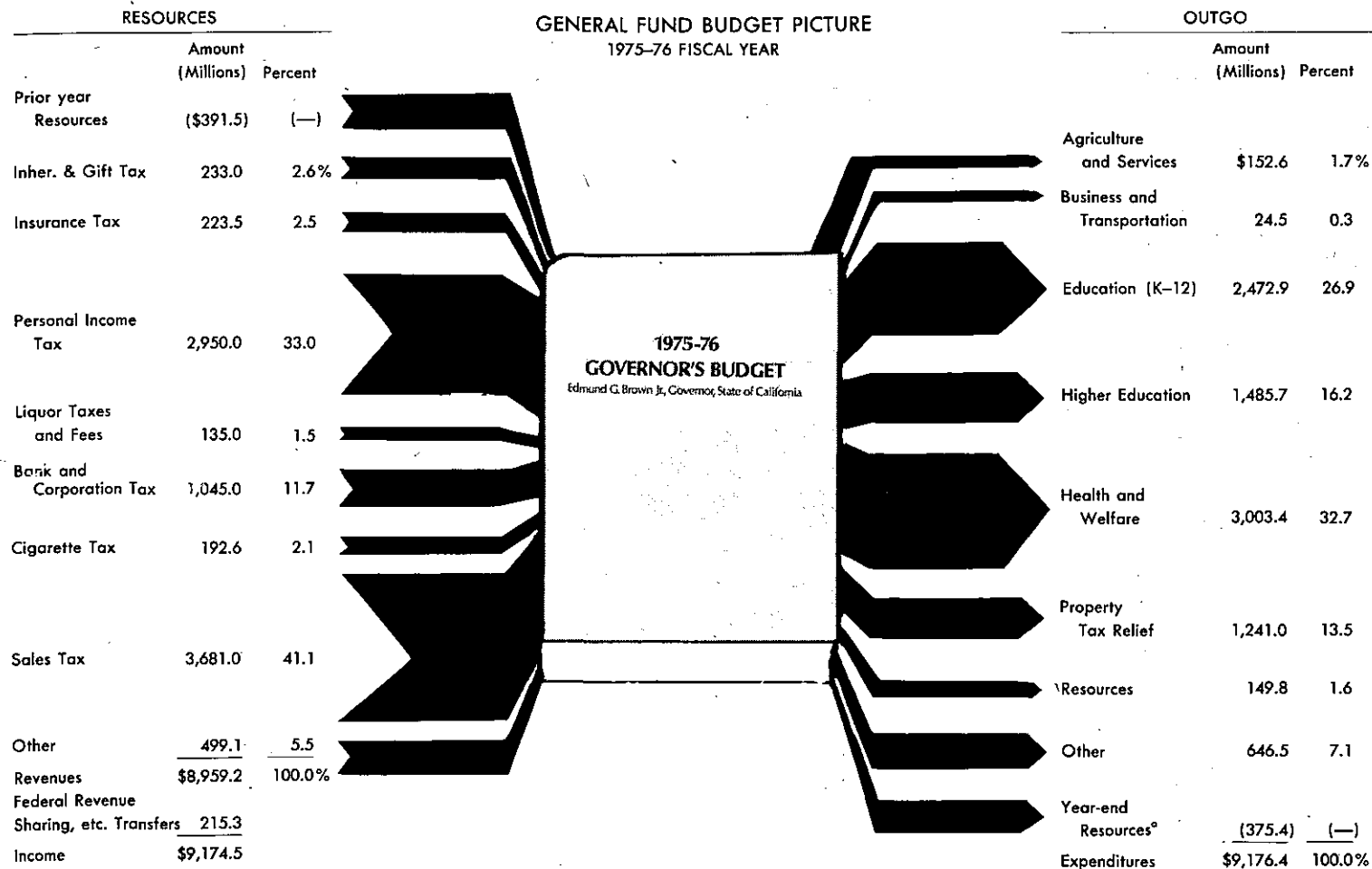


CHART II
GENERAL FUND BUDGET PICTURE
1975-76 FISCAL YEAR



^a Excludes \$212.5 million available from Federal Revenue Sharing Fund.

THE GENERAL FUND PICTURE OF EXPENDITURES
General Fund Budget Expenditures and Yearly Increases
(In Millions)

	<i>Actual</i>	<i>Estimated</i>	<i>Change</i>		<i>Proposed</i>	<i>Change</i>	
	<i>1973-74</i>	<i>1974-75</i>	<i>Amount</i>	<i>Percent</i>	<i>1975-76</i>	<i>Amount</i>	<i>Percent</i>
State operations ..	\$1,748.7	\$2,128.6	\$379.9	21.7%	\$2,390.1	\$261.5	12.3%
Capital outlay	21.8	52.8	31.0	142.2	17.3	-35.5	-67.2
Local assistance....	5,528.9	6,246.2	717.3	13.0	6,769.0	522.8	8.4
Totals	\$7,299.4	\$8,427.6	\$1,128.2	15.5%	\$9,176.4	\$748.8	8.9%

THE SPECIAL FUND PICTURE OF EXPENDITURES
Special Fund Budget Expenditures and Yearly Increases
(In Millions)

	<i>Actual</i>	<i>Estimated</i>	<i>Change</i>		<i>Proposed</i>	<i>Change</i>	
	<i>1973-74</i>	<i>1974-75</i>	<i>Amount</i>	<i>Percent</i>	<i>1975-76</i>	<i>Amount</i>	<i>Percent</i>
State operations	\$507.0	\$653.3	\$146.3	28.9%	\$689.1	\$35.8	5.5%
Capital outlay	376.9	464.2	87.3	23.2	343.2	-121.0	-26.1
Local assistance	810.8	887.0	76.2	9.4	840.2	-46.8	-5.3
Totals	\$1,694.7	\$2,004.5	\$309.8	18.3%	\$1,872.5	-\$132.0	-6.6%

THE GENERAL FUND PICTURE OF INCOME, OUTGO AND SURPLUS

General Fund Surplus* and Federal Revenue Sharing Availability

	<i>In millions</i>	
	<i>1974-75</i>	<i>1975-76</i>
Prior year resources available.....	\$358.3	\$391.4
(Unrestricted surplus prior year)	(180.1)	(349.9)
Income	8,451.0	9,153.4
Total Available	\$8,809.3	\$9,544.8
Expenditures	\$8,417.9	\$9,169.5
Current surplus (+) or deficit (-)	(+33.0)	(-16.1)
Reserves	-41.5	-13.6
Year-end unrestricted surplus.....	\$349.9	\$361.7
Federal revenue sharing balances available	202.2	212.5
Total Available, Year-End	\$552.1	\$574.2

* Adjusted to exclude General Fund special accounts.

For the purpose of calculating the unrestricted surplus shown above we have reduced the totals by the amount of income and expenditures in General Fund special accounts. These are dedicated funds specifically earmarked for each program. An example is the State Energy and Resources Conservation and Development Special Account. Revenues for 1975-76 will total \$15.3 million and expenditures of \$1.0 million are proposed, but the Governor indicates this amount may be increased later. This account supports the new Energy Resources Conservation and Development Commission. These adjustments are:

	<i>In millions</i>	
	<i>1974-75</i>	<i>1975-76</i>
Unadjusted income	\$8,460.8	\$9,174.5
Less special account income.....	9.8	21.1
Adjusted Income	\$8,451.0	\$9,153.4
Unadjusted expenditures	\$8,427.6	\$9,176.4
Less special account expenditures.....	9.7	6.9
Adjusted Expenditures	\$8,417.9	\$9,169.5

MAJOR GENERAL FUND PROGRAM ELEMENTS

This summary presents a brief overview of major expenditure programs such as health, education, higher education, and property tax relief. These major programs comprise 90.2 percent of the total of \$9,176.4 million in General Fund expenditures for 1975-76.

A detailed analysis of each of the programs can be obtained by referring to the appropriate budget item in following sections of this Analysis.

Table 2 indicates the major program changes in General Fund expenditures.

Table 2
1975-76 Selected General Fund Budget Program Changes
From 1974-75 Expenditure Level
(In Millions)

	<i>Amount of Increase</i>	<i>Percent of Increase</i>
Major Program Increases:		
Health (excluding Medi-Cal).....	\$30.7	5.2%
Medi-Cal	92.3	11.1
Benefit Payments (Social Welfare)	184.8	19.1
K-12 Education ^a	105.9	4.6
California Community Colleges—apportionments.....	49.3	15.1
University of California.....	31.5	6.1
State University and Colleges	11.9	2.4
Debt Service	26.3	15.3
Property Tax Relief	71.1	6.1
Major Program Decreases:		
Capital Outlay	\$-35.4	-67.1%

^a Excludes debt service on school building aid bonds.

Department of Health (Excluding Medi-Cal)

	<i>Estimated 1974-75</i>	<i>Projected 1975-76</i>	<i>Increase</i>	<i>Percent</i>
General Fund	\$585,729,929	\$616,437,406	\$30,707,477	5.2%

A total 1975-76 General Fund expenditure of \$616.4 million is proposed for the Department of Health (excluding Medi-Cal which is discussed in the following section). This is an increase of \$30.7 million or 5.2 percent over the current year. The budget reflects an increase of \$36.8 million in the mental disabilities program and a \$3.9 million decrease in the developmental disabilities program. However, a change in the method of distributing hospital overhead distorts any simple comparison between fiscal years or programs.

Total average population at the state hospitals is estimated to increase by 87 or 0.5 percent between the current year and the budget year. The average population at the hospitals for the mentally disabled is estimated to decrease by 76 or 1.2 percent, while the average population at the hospitals for the developmentally disabled is estimated to increase by 163 or 1.6 percent.

Average Populations at the State Hospitals

	<i>1974-75</i>	<i>1975-76</i>	<i>Change</i>	<i>Percent</i>
Hospitals for the Developmentally Disabled	10,097	10,260	163	1.6%
Hospitals for the Mentally Disabled.....	6,431	6,355	-76	-1.2
Totals	16,528	16,615	87	0.5%

California Medical Assistance Program (Medi-Cal)

	<i>Estimated 1974-75</i>	<i>Projected 1975-76</i>	<i>Increase</i>	<i>Percent</i>
General Fund	\$826,283,305	\$918,588,591	\$92,305,286	11.2%

General Fund appropriations for Medi-Cal are proposed at \$918.6 million for 1975-76. This is an increase of \$92.3 million or 11.2 percent over 1974-75. Significant program changes include an eight-percent increase in the utilization of professional services and the full year costs related to the implementation at the state level of the 1972 social security amendments. Program costs were also increased by Chapter 1531, Statutes of 1974 (AB 3970) which established separate eligibility for persons needing renal dialysis and related services who do not otherwise qualify for Medi-Cal.

Medi-Cal Average Monthly Caseload

	<i>Estimated 1974-75</i>	<i>Projected 1975-76</i>	<i>Increase</i>	<i>Percent</i>
Cash grant eligibles	2,025,300	2,175,516	150,216	7.4%
Medically needy	191,200	220,900	29,700	15.5
Medically indigent	198,700	233,300	34,600	17.4
Total	2,415,200	2,629,716	214,516	8.9%

The average monthly caseload is projected to increase by 8.9 percent. However, the components of this increase vary from a 17.4 percent increase for medically indigent to a 7.4 percent increase for cash grant.

Department of Benefit Payments

	<i>Estimated 1974-75</i>	<i>Projected 1975-76</i>	<i>Increase</i>	<i>Percent</i>
General Fund	\$968,256,236	\$1,153,104,105	\$184,847,869	19.1%

A total General Fund expenditure of \$1,153.1 million is proposed for the Department of Benefit Payments. This is an increase of \$184.8 million or 19.1 percent over the current year. The welfare operations program consists of the five elements shown below:

Welfare Operations Program Costs (General Fund)

	<i>Estimated 1974-75</i>	<i>Projected 1975-76</i>	<i>Increase</i>	<i>Percent</i>
Payments to children	\$438,166,952	\$522,774,150	\$84,607,198	19.3%
Payments to adults	477,885,414	574,780,168	96,894,754	20.3
Food stamps	581,409	607,514	26,105	4.5
County administration	48,485,700	51,903,500	3,417,800	7.0
Special programs	191,937	191,937	—	—
Totals	\$965,311,412	\$1,150,257,269	\$184,945,857	19.2%

Education (K-12)

	<i>Estimated 1974-75</i>	<i>Projected 1975-76</i>	<i>Increase</i>	<i>Percent</i>
Apportionments ^a	\$1,919,134,456	\$1,998,171,590	\$79,037,134	4.1%
Total Education ^b	\$2,320,680,075	\$2,426,625,126	105,945,051	4.6

^a General Fund only.

^b Excludes debt service on school building aid bonds.

General Fund apportionments for 1975-76 are projected at \$1,998.2 million, an increase of \$79.0 million or 4.1 percent over 1974-75. Most of the increase is a result of provisions of Chapter 1406, Statutes of 1972 (SB 90) and Chapter 208, Statutes of 1973 (AB 1267) which provided a \$63 per average daily attendance (ADA) increase in the foundation program for 1975-76.

Chapter 1527, Statutes of 1974 (AB 3854) requires school districts to establish special programs for autistic children. The budget contains \$7.4 million to fund this program in 1975-76.

A comparison of the estimated ADA in 1974-75 and 1975-76 is shown below by school level.

Estimated Average Daily Attendance

	<i>1974-75</i>	<i>1975-76</i>	<i>Change</i>	<i>Percent</i>
Elementary	3,075,000	3,039,000	-36,000	-1.2%
High school	1,488,500	1,501,000	12,500	0.8
Adults, high school	61,000	60,000	-1,000	-1.6
Totals	4,624,500	4,600,000	-24,500	-0.5%

The total average daily attendance is projected to decrease by 0.5 percent between 1974-75 and 1975-76. However, the components of this decrease vary from a 1.6 percent decline among high school adults to an 0.8 percent increase in the regular high school program. The enrollment decline in the elementary schools will be reflected in high school enrollment in about two years.

California Community Colleges

	<i>Estimated 1974-75</i>	<i>Projected 1975-76</i>	<i>Increase</i>	<i>Percent</i>
Apportionments	\$327,127,947	\$376,435,531	\$49,307,584	15.1%

Expenditures for California Community College apportionments are projected to increase by \$49.3 million largely as a result of statutory increases enacted in Chapter 209, Statutes of 1973 (SB 6). This bill provided annual increases in the educational foundation program.

Estimated Average Daily Attendance

	<i>1973-74</i>	<i>1974-75</i>	<i>Increase</i>	<i>Percent</i>
Community Colleges	521,360	542,736	21,376	4.1%
Adults, community colleges	125,398	130,539	5,141	4.1
Totals	646,758	673,275	26,517	4.1%

Total average daily attendance is projected to increase by 4.1 percent for 1975-76.

University of California

	<i>Estimated 1974-75</i>	<i>Projected 1975-76</i>	<i>Increase</i>	<i>Percent</i>
General Fund appropriation.....	\$511,904,720	\$543,372,496	\$31,467,776	6.1%

General Fund appropriations for the University of California are proposed at \$543.4 million for 1975-76. This is an increase of \$31.5 million over the 1974-75 appropriation. Significant increases include \$8.8 million for merit salary adjustments, \$8.8 million for general price level changes, \$5.3 million for utility price increases and \$8.6 million for enrollment related costs. Decreases include \$3.9 million because of increased federal overhead and \$1.4 million because of termination of the extended University pilot program.

Various measurement criteria are used to determine the appropriate level of funding for each function of the University. One is the enrollment in terms of full-time equivalents (FTE). A comparison of the FTE enrollment in 1974-75 and 1975-76 is shown below.

Estimated Full-Time Equivalent Enrollment

	<i>1974-75</i>	<i>1975-76</i>	<i>Change</i>	<i>Percent</i>
General Campus	104,203	106,672	2,469	2.4%
Extended University	772	0	-772	-100.0
Health Sciences	9,870	10,642	772	10.5
Totals	114,845	117,314	2,469	2.1%

Total full-time equivalent enrollment is projected to increase by 2,469 or 2.1 percent for 1975-76.

California State University and Colleges

	<i>Estimated 1974-75</i>	<i>Projected 1975-76</i>	<i>Change</i>	<i>Percent</i>
General Fund	\$487,213,528	\$499,082,747	\$11,869,219	2.4%
Enrollment (full-time equivalents)	231,295	229,630	-1,665	-0.7%

The proposed State University and Colleges General Fund support budget totals \$499.1 million. This is an increase of \$11.9 million or 2.4 percent. Significant program increases include \$4.4 million for merit salary adjustments, \$2.1 million for full-year position funding and \$7.9 million for price level changes. These increases are partially offset by decreases of \$1.2 million for enrollment related reductions and \$0.9 million due to elimination of the external degree and international programs.

Enrollment, measured by full-time equivalents (FTE), is projected to decrease by 1,665 in 1975-76 when compared to 1974-75 estimated FTE.

Salary Increases and Continuation of 1974-75 Benefits

	<i>Estimated 1974-75</i>	<i>Projected 1975-76</i>	<i>Change</i>	<i>Percent</i>
Salary Increase	\$144,373,956 ^a	\$151,409,000	\$7,035,044	4.9%
1974-75 Benefits Program	51,007,714	50,657,419 ^b	-350,295	-0.7
Totals	\$195,381,670	\$202,066,419	\$6,684,749	3.4%

^a Does not include funds appropriated by the Budget Act of 1973 which were withheld as a result of action by the federal Cost-of-Living Council.

^b An additional unspecified amount to fund increased employee benefits is also included in the 1975-76 budget. This program is discussed in the next section.

A 1975-76 General Fund expenditure of \$151.4 million is proposed for salary increases. This is \$7.0 million or 4.9-percent more than the estimate for the current year.

The \$151.4 million program will provide funds for approximately an 8.5 percent increase to state employees (other than judges and justices) supported by the General Fund. The distribution of the 1975-76 salary increase amount by group is shown below:

Civil Service, exempt and statutory	\$69,765,000
University of California	
Faculty	21,132,000
Nonfaculty	19,023,000
California State University and Colleges	
Instructional	25,938,000
Noninstructional	12,992,000
Judicial ^a	2,559,000
Total General Fund increase	\$151,409,000

^a By statute, the salary increase for judges and justices is based on the change in the California Consumer Price Index (CCPI) between the two preceding Decembers. The CCPI increased 13.4 percent between December 1973 and December 1974.

The 1975-76 budget contains \$50.7 million (General Fund) to continue the total equivalent compensation (TEC) benefits already authorized in 1974-75. The 1975-76 Budget also contains a lump sum appropriation for three dissimilar purposes of which TEC is one, as follows.

Price Augmentations—Total Equivalent Compensation (TEC)

	<i>Projected 1975-76</i>
General Fund	\$85,000,000

The budget contains a lump sum of \$85 million to fund (1) price increases of state operating and equipment costs, (2) rate increases for providers of medical and related services including Medi-Cal and (3) increases in new TEC benefits. The amount included for each of these is not specified.

Capital Outlay

	<i>Estimated 1974-75</i>	<i>Proposed 1975-76</i>	<i>Change</i>	<i>Percent</i>
General Fund capital outlay expenditures	\$52,763,379	\$17,339,504	\$-35,423,875	-67.1%
Major Changes				
Department of General Services.....	9,170,384 ^a	532,500	-8,637,884	-94.2
Department of Food and Agriculture	1,029,450	-	-1,029,450	-100.0
Department of Conservation	3,274,385	142,420	-3,131,965	-95.7
Department of Parks and Recreation	9,990,992	350,000	-9,640,992	-96.5
Department of Health	21,877,112	8,901,902	-12,975,210	-59.3

General Fund expenditures for capital outlay are budgeted to decrease by \$35.4 million between fiscal years 1974-75 and 1975-76. The most significant decreases are in the budgets of the Department of Health, the Department of Parks and Recreation and the Department of General Services.

In addition to the \$17.3 million requested for capital outlay expenditures for 1975-76 the budget proposes a \$20.4 million loan to the California Community Colleges from the General Fund. The loan is to be repaid with the first proceeds from an anticipated new bond issue in June 1976. The \$20.4 million loan is the General Fund portion of a \$38.8 million capital outlay expenditure program for the community colleges. The balance of \$18.4 million will be contributed by the community college districts.

Property Tax Relief

	<i>Estimated 1974-75</i>	<i>Proposed 1975-76</i>	<i>Increase</i>	<i>Percent</i>
Senior citizens property tax assistance	\$49,900,000	\$54,700,000	\$4,800,000	9.6%
Personal property tax relief	294,700,000	334,500,000	39,800,000	13.5
Homeowners' property tax relief	702,600,000	716,000,000	13,400,000	1.9
Open space	15,000,000	16,000,000	1,000,000	6.7
Payment to local governments for sales and property tax revenue loss.....	2,700,000	4,840,000	2,140,000	79.3
Renters tax relief	105,000,000 ^a	115,000,000	10,000,000	9.5
Totals.....	\$1,169,900,000	\$1,241,040,000	\$71,140,000	6.1%

^a Includes \$60,000,000 which is currently not appropriated but treated as a credit against personal income tax liabilities.

The state's property tax relief program provides reduced property taxes to senior citizens, personal property owners (business inventory), homeowners and renters. Subventions for open space and payments to local governments for sales and property tax revenue loss are also included within property tax relief as they provide a measure of tax relief to local governments including school districts.

Projected General Fund expenditures for property tax relief total \$1,241.0 million in 1975-76. This is an increase of \$71.1 million or 6.1 percent over the current year. Significant increases include \$39.8 million (13.5 percent) for personal property tax relief, \$13.4 million (1.9 percent) for homeowners property tax relief and \$10.0 million (9.5 percent) for renters tax relief.

Under current law only the refund portion (\$45 million in 1974-75) of the renters tax relief program is appropriated. The remaining portion, which is a credit against tax liabilities, is treated as a reduction of income tax revenues. The budget indicates that legislation will be proposed early in 1975 which will provide that the entire program be appropriated. Accordingly, this program is presented as an expenditure in the budget.

GENERAL OBLIGATION BONDS

State general obligation bonds outstanding on December 31, 1974 totaled \$5,420,830,000, an increase of \$177,516,000 or 3.4 percent over the \$5,243,314,000 outstanding on December 31, 1973.

There are two types of general obligation bonds: (1) those in which the debt service (includes interest and redemption payments) obligation is fully paid, or the major portion is paid, from the General Fund, and (2) those in which debt service is paid from project or program revenues, but the full faith and credit of the state is pledged to make these payments from the General Fund should revenue be insufficient to cover these costs.

State agencies also issue revenue bonds for certain projects on which only the revenue generated from the enterprise is pledged for payment of the bonds. These have been issued for University of California and state college dormitories, parking lots, Cal-Expo facilities, pollution control, bridges and other construction projects and purposes. The revenue bonds are not included in the totals in this summary but rather are mentioned merely to indicate the different types of debt instruments with which the state is involved.

In addition to legislative approval, general obligation bonds must be authorized by the electorate. Bond issues have been approved in this manner for the development of water resources, school building aid, construction of higher educational facilities and other capital construction, purchasing and developing park and recreational facilities, veteran's farm and home purchases, clean water programs, and for other purposes.

The state general obligation bonded debt by the various program categories is shown in Table 3. Information is included to show the amount by program for the \$1,670,900,000 in authorized bonds which have been approved but not sold, as well as bonds sold and outstanding on December 31, 1974.

Table 3
General Obligation Bonds of the State of California
by Purpose as of December 31, 1974

<i>Purpose</i>	<i>Unsold</i>	<i>Outstanding</i>
General Fund Bonds:		
State Construction	—	\$689,900,000
Beaches, parks, recreational and historical facilities	\$225,000,000	140,700,000
Higher education construction	—	180,035,000
Junior college construction	—	53,500,000
Community college construction	70,000,000	89,250,000
Clean water	350,000,000	137,500,000
Recreation and fish and wildlife	10,000,000	47,000,000
Health science facilities	140,900,000	14,250,000
School building aid ^a	425,000,000	1,146,750,000
Totals	<u>\$1,220,900,000</u>	<u>\$2,498,885,000</u>
Self-Liquidating Bonds:		
Water resources development	200,000,000	1,545,800,000
Veterans' farm and home	250,000,000	1,329,000,000
Harbor bond programs	—	47,145,000
Totals	<u>\$450,000,000</u>	<u>\$2,921,945,000</u>
Totals, All bonds	<u>\$1,670,900,000</u>	<u>\$5,420,830,000</u>

^a School districts bear part of the debt service. The General Fund contributes the remainder.

Source: State Treasurer

California State Bond Fund expenditures in those programs separately identified in Schedule 3 of the 1975-76 budget document are estimated at \$254 million for the 1975-76 budget year, a decrease of \$148.9 million or 37.0 percent from the estimated \$402.9 million in expenditures for 1974-75. Expenditures in 1975-76 are listed in Table 4.

Table 4
State of California
Bond Fund Expenditures, 1973-74 Through 1975-76^a

	1973-74	1974-75	1975-76
State Construction Program	\$75,527,598	\$49,410,721	—
State Beach, Park, Recreational and Historical Facilities (1964)	3,333,722	14,074,590	\$53,000
State Beach, Park, Recreational and Historical Facilities (1974)	4,817,790	120,887,420	25,094,015
California Water Resources Development	96,535,800	90,397,704	114,072,297
Central Valley Water Project	30,671,095	31,968,651	15,577,630
Clean Water Bond Fund	29,916,547	32,941,000	51,028,000
Recreation and Fish and Wildlife Enhancement ..	10,744,820	25,231,385	1,293,468
Health Science Facilities Construction Program....	65,584,200	37,972,000	—
Higher Education Construction Program Fund ^b ..	—	—	26,441,000
Community College Construction Program Fund ^c ..	—	—	20,407,400
Total Bond Fund Expenditures	\$317,131,572	\$402,883,471	\$253,966,810

^a Includes only those programs separately identified in Schedule 3 of the Governor's Budget.

^b Funded by a loan from the Capital Outlay Fund for Public Higher Education pending approval and sale of a proposed bond issue.

^c Funded by a loan from the General Fund pending approval and sale of a proposed bond issue.

One major general obligation bond issue which was approved by the Legislature in 1972 is pending a vote by the electorate:

Legislation	Program	Vote by Electorate	Amount
Chapter 152, Statutes of 1972 (SB 220)	Health Science facilities	November 1976	\$138,100,000

Two bond issues are currently before the Legislature. If passed by the Legislature and signed by the Governor they will be placed on the ballot as indicated below:

Legislation	Program	Vote by Electorate	Amount
AB 120	Recreation, fish and wildlife	November 1976	\$65,000,000
AB 121	Safe drinking water	June 1976	\$150,000,000

The Governor's Budget also proposes two other bond issues. One issue is for community college construction, for which a \$20.4 million loan is proposed from the General Fund as temporary financing until this issue is placed before the electorate in 1976. A similar bond issue is for higher education construction. The budget reflects interim loans to the University of California (\$12.6 million) and to the California State University and Colleges (\$13.8 million) from the Capital Outlay Fund for Public Higher

Education (COFPHE). This bond issue will also be placed before the electorate in 1976. Detailed information on these two proposed issues is not included in the Budget. As noted in Table 4 expenditures for these programs are reflected as bond fund expenditures. If the two proposed issues fail to pass the Legislature and be approved by the electorate the funds making the loans will bear the cost of the programs.

Total sales of \$515 million in general obligation bonds are anticipated in 1975-76. General obligation bond sales for 1973-74 to 1975-76 are shown in Table 5.

Table 5
General Obligation Bond Sales
1973-74 to 1975-76
(In Millions)

	<i>Actual</i> 1973-74	<i>Estimated</i> 1974-75	<i>Projected</i> 1975-76
Community College	\$25	\$100	\$20
Health Science Facilities		40	50
Recreation and fish and wildlife	10	15	10
Beaches, parks, recreational and historical facilities		75	50
Clean Water		50	100
State School Building Aid ^a	50	50	125
Veterans ^b	200	200	150
Water Resources Development ^b		10	10
Totals	\$285	\$540	\$515

^a Debt service partially paid by school districts.

^b Debt service paid from project or program revenues.

General Fund Debt Service

Table 6 projects the total General Fund debt service for the period 1973-74 through 1977-78. This projection indicates that debt service charges will be \$198.3 million in fiscal year 1975-76 and increase to \$232.8 million in 1977-78. Included is all bond debt service fully funded from the General Fund and the General Fund portion of school building aid bond debt service (see Tables 7 and 8). These estimates are based only on currently authorized bond issues and include neither those issues yet to be voted on by the electorate nor those issues proposed in the Governor's Budget. Should these or other new issues be authorized and sold, the cost to the General Fund will rise faster than projected.

Table 6
Estimated Total General Fund Debt Service

1973-74	\$164,613,857
1974-75	172,021,995
1975-76	198,300,825
1976-77	219,202,177
1977-78	232,793,288

Tables 7 and 8 divide the General Fund debt service into its two major components. Table 7 projects the debt service on those programs fully funded from the General Fund and Table 8 projects those charges for school building aid bonds including the estimated portion projected to be contributed from the General Fund.

Table 7
Estimated Interest and Redemption Charges on General Fund Bonds
Fully Funded by the State 1973-74 to 1977-78 ^a

<i>Fiscal Year</i>	<i>Total Debt Service</i>	<i>Debt service on bonds sold as of Dec. 31, 1974</i>	<i>Debt service on anticipated sales^b</i>
1973-74.....	\$118,773,723	\$118,773,723	
1974-75.....	126,808,053	125,433,052	\$1,375,001
1975-76.....	152,120,718	131,943,636	20,177,082
1976-77.....	171,279,775	129,011,067	42,268,708
1977-78.....	183,708,508	126,845,038	56,863,470

^a Accrual basis. Includes state construction; state beach, park, recreational and historical facilities; clean water; state higher education construction; community college construction; recreation and fish and wildlife; and health science facilities.

^b Estimated debt service on anticipated \$140 million in sales during the last half of the 1974-75 fiscal year; \$230 million in sales during 1975-76; \$150.9 million during 1976-77; and \$150 million during 1977-78. Does not include debt service for proposed bond issues to be placed before the electorate in 1976. Assumes a 5.5 percent average interest rate on bonds sold.

Table 8
Estimated Interest and Redemption Charges on State School Building Aid Bonds
Partially Funded by the State 1973-74 to 1977-78 ^a

<i>Fiscal Year</i>	<i>Total Debt Service</i>	<i>Debt Service on bonds sold as of Dec. 31, 1974</i>	<i>Debt service on anticipated sales^b</i>	<i>General Fund portion of total debt service^c</i>
1973-74	\$124,064,542	\$124,064,542		\$45,840,134
1974-75	128,218,380	127,072,547	\$1,145,833	45,213,942
1975-76	134,432,552	125,000,260	9,432,292	46,180,107
1976-77	140,948,240	120,230,011	20,718,229	47,922,402
1977-78	144,367,000	113,767,522	30,599,478	49,084,780

^a Accrual basis

^b Estimated debt service on anticipated \$50 million sales during the last half of 1974-75 fiscal year; \$125 million during 1975-76; \$100 million during 1976-77 and \$100 million during 1977-78. Assumes a 5.5 percent average interest cost on bonds sold.

^c General Fund portion of debt service is projected at 34.4 percent for 1975-76 and 34 percent for 1976-77 and 1977-78.

REVENUE ANALYSIS

Summary and Conclusions

The uncertainty that surrounded the economic outlook at the beginning of 1974 has not been diminished by the events of the past year. Contrary to most forecasts, the rate of inflation continued unabated through most of the year, output of goods and services declined in each quarter, and unemployment continued to rise. Real output in the fourth quarter of 1974, which was predicted to grow at a better than "normal" rate, suffered the sharpest decline since 1958. In Washington, anti-inflation measures under consideration in October were dropped and replaced in mid-January by major economic programs to combat the deepening recession.

Most economic forecasters, including the Department of Finance, now are predicting a slowing of the current economic decline through the first half of 1975, with a moderate recovery commencing in the third quarter. Consumer spending is expected to provide the necessary impetus to reverse the decline and start the economy on an upward path by midyear. Gross National Product is estimated at \$1,510 billion, up 8 percent from 1974 in current dollars. Personal income in California is expected to register a gain of 9.4 percent to \$136 billion.

Based on these economic assumptions, the Department of Finance estimates General Fund revenues for the current year at \$8,243 million, up 10.7 percent from 1973-74 after adjusting for law changes. For the budget year, the department estimates a gain in General Fund revenues of \$716 million over 1974-75, including a \$77 million transfer in state land oil revenues.

The department's estimates of revenues for the current and budget years are generally consistent with its underlying economic assumptions. Most forecasters agree with the department's expectation of an improvement in economic conditions in the second half of 1975, and this may represent the "most likely" outcome for the economy in the year ahead. There are, however, several factors that strongly support the minority view that the economic slump will persist beyond midyear. These factors include the year-long decline in real spendable earnings, no substantial relief from price increases before year-end, continuing energy shortages, and a highly unstable international situation, all of which suggest the possibility of a later recovery than the budget forecast assumes. Fourth quarter 1974 preliminary results are worse than assumed by the forecast and could indicate that the recession will be deeper than anticipated. The final shape of the economic program that will be enacted to provide fiscal stimulus to the economy and to conserve energy resources is unknown at this time, and whether the ultimate effects will be beneficial or detrimental to the economy is yet to be seen.

If the upturn does not materialize until early 1976, we estimate that General Fund revenues could be lower than forecast by \$200 million to \$250 million for the budget year. We believe that a revenue loss of this magnitude should be taken into consideration in preliminary budget expenditure decisions. Revised revenue estimates will be available in May before final budget decisions are made.

1974—A Disappointing Record

The year 1974 began in an atmosphere of uncertainty. The oil embargo had been imposed in October of 1973 and by December the adverse impact of reduced petroleum supplies on the economy was being felt. Most forecasters, although not in close agreement, believed a downturn in the economy would continue through the first quarter of the year and possibly into the summer months. There was general agreement that a turnaround would occur sometime between April and September and that the economy would be well into the recovery phase by the end of the year.

The slowing of economic activity in the first half of the year followed the pattern generally expected. Despite the lifting of the oil embargo in April, however, the recovery failed to materialize in the second half. Real output continued to decline in the third quarter and the unemployment rate began to edge upward. Business investment, which was expected to provide strength in this period, remained essentially flat. In the final quarter of the year real output dropped by more than 9 percent, the worst drop since 1958, plunging the nation into a full-fledged recession.

Throughout the year, prices continued their steady upward climb. The rate of change in the consumer price index stayed above the double digit level and was considered to be the nation's most serious economic problem as late as October, despite the continuing drop in output. Concern over the sluggishness in the economy was mitigated by the relative stability of employment and the fact that only moderate increases in the unemployment rate had occurred since the beginning of the year. Through September the administration in Washington continued to seek solutions to the problem of inflation, and in October the President proposed anti-inflation measures which included a 5 percent surcharge on income taxes. The economic slump had not yet been characterized as a recession and the terms "stagflation" and "sideways waffling" were being used to describe the slowdown in economic activity. Events in November and December, however, left no doubt that the economy was in trouble and that a recession had indeed arrived. The number of nonagricultural jobs shrank by over 1 million during the last two months of 1974 and the unemployment rate jumped from 6.0 percent in October to 7.1 percent in December. Auto sales, industrial production and new factory orders were all dropping sharply at year-end. In mid-January of 1975 the administration had reversed its posture on economic policy and was proposing tax reductions to stimulate the economy.

The final scoreboard for 1974 shows real output down by 2.0 percent from the previous year, consumer prices up by 11.2 percent over 1973 and an average unemployment rate of 5.5 percent compared to 4.9 percent of a year earlier. New car sales were down 22 percent from 1973, with declines of 34 percent and 26 percent in November and December from the same months a year earlier. The year was generally disastrous for the housing industry, with high mortgage rates and skyrocketing construction costs holding new housing starts to 1,360,000, more than one-third below the level of the previous year.

1975—Outlook Still Uncertain

Last year we noted that the disparity among forecasters was greater than it had been for 1973, and commented that the range in the forecasts of Gross National Product (GNP) included in Business Week's survey had widened from \$15 billion for 1973 to \$40 billion for 1974. For 1975 that range has doubled to \$80 billion with predictions of GNP ranging from a high of \$1,528 billion to a low of \$1,445 billion. Predictions of general price level increases (GNP deflator) in 1975 range from a low of 5.3 percent to a high of 10.9 percent while the unemployment rate is forecasted to average from 6.3 to 8.3 percent. The budget forecast by the Department of Finance is roughly near the midpoint of this wide range of predictions. The department anticipates a decline in gross national product in real terms of 2.2 percent, with a price level increase of 10.4 percent pushing GNP in current dollars up to \$1,510 billion. Table 1 compares the Department of Finance budget forecast with the two prior years.

The department's forecast assumes a continuation of the downward trend of economic activity through the second quarter of 1975. A moderate upturn is expected in the third quarter with a growth in output accelerating in the fourth quarter and a strong recovery underway by the beginning of 1976. This pattern of quarterly changes roughly corresponds with the composite of the national forecasts referred to above. While there appears to be general agreement that a recovery will follow the first half downturn, there is a wide disparity in the predictions of when the turnaround will actually take place.

Table 1
National Economic Data
(dollars in billions)

	<i>Actual</i> 1973	<i>Estimated*</i> 1974	<i>Percent</i> <i>Change</i>	<i>Budget</i> <i>Forecast</i> 1975	<i>Percent</i> <i>Change</i>
Gross National Product	\$1,294.9	\$1,398.0	8.0%	\$1,510.0	8.0%
GNP in 1958 dollars	839.2	822.1	-2.0	804.4	-2.2
GNP price deflator	154.3	170.0	10.2	187.7	10.4
Personal income.....	\$1,055.0	\$1,151.3	9.1	\$1,258.0	9.3
Disposable income	903.7	980.2	8.5	1,071.0	9.3
Savings	74.4	72.5	-2.6	73.0	0.7
Corporate profits.....	122.7	144.6	17.8	121.0	-16.3
Consumer price index	133.1	148.0	11.2	163.2	10.3
Employment (thousands)	84,409	86,200	2.1	86,200	N.C.
Unemployment (thousands).....	4,305	5,005	16.3	6,550	30.9
Unemployment rate	4.9%	5.5%	—	7.1%	—
Housing starts (thousands)	2,045	1,360	-33.5	1,350	-0.7
New car sales (thousands)	11,550	9,000	-22.1	8,500	-5.6

* By the Department of Finance in the Governor's 1975-76 Budget

Table 2 compares key elements of the forecast of the Department of Finance with forecasts of the University of California at Los Angeles and the Wells Fargo Bank.

The overriding concern of economic planners, forecasters and policy-makers during the past year has been the dilemma of combating inflation and recession simultaneously. Both the presidential and congressional proposals announced in January 1975 have shifted strongly in the direction

of mitigating the recession and appear to have relegated the problem of inflation to second or even third place (behind energy) in the ranking of priorities. There is general agreement that a federal tax reduction would stimulate the economy. Critics are asserting, however that the large federal deficits that would accompany the proposed tax cuts would refuel inflationary pressures and that financing the deficit would strain the money markets and force interest rates up. Others argue that the dampening effect of the proposed energy conservation measures might more than offset the stimulative effect of a tax cut.

Table 2
Comparison of National Economic Forecasts For 1975

	<i>Dept. of Finance</i>	<i>Univ. of Calif. Los Angeles</i>	<i>Wells Fargo Bank</i>
Percent changes in			
Gross National Product.....	8.0%	7.5%	8.5%
Due to price level	10.4	9.4	8.5
Due to real growth	-2.2	-1.8	—
Personal income	9.3	10.2	9.0
Corporate profits	-16.3	-24.6	NA
Consumer prices	10.3	9.6	9.0
Unemployment rate	7.1	7.7	6.7

Consumer Expected To Spark Recovery

Most forecasters, including the Department of Finance, are expecting a resurgence of consumer spending to lead the recovery in the second half of 1975. The sluggish consumer demand over the past year and, in particular, the sharp decline in the level of automobile sales, indicates that major consumer purchases of autos, appliances and other big ticket items have been deferred. Forecasters anticipate that a slowing of price increases coupled with tax rebates or other federal fiscal measures will encourage consumers to resume higher spending levels by mid-summer. Price rebates, currently being offered by automobile manufacturers, may lend some of the needed stimulus to consumer spending.

The Department of Finance forecasts a gain in personal consumption expenditures of 10 percent for 1975 over 1974. This gain is higher than the growth in personal income nationally, which is projected at 9.3 percent. The relatively high level of consumer outlays will be financed by a reduction in the savings rate, which the department expects to decline from 7.4 percent in 1974 to 6.8 percent in 1975.

As pointed out by the department, the response to the 1975 model automobiles indicates that no increase can be expected in total unit car sales for 1975. The department estimates a total of 8.5 million units for the year, down from 1974's estimated level of 9 million units (actual sales were 8,856,000). A slow recovery in the housing market will continue to dampen the demand for household furnishings and appliances and purchases in these areas will probably not provide support for the recovery until early 1976. The department anticipates that the greatest strength in consumer spending will be in the services area.

Weakness Seen In Business Spending

Outlays for capital goods in 1975 will be less than 1974 when expressed in constant dollars, according to the latest U.S. Department of Commerce Survey. Although petroleum producers, chemical firms and iron and steel makers are projecting increases, auto makers and aircraft manufacturers indicate plans for substantial reductions in new capital equipment outlays in 1975. The Department of Finance forecasts purchases of producers durables to rise by 10.3 percent in current dollars and expenditures for nonresidential structures to be up by 4.1 percent over 1974.

Business inventories are expected to decline in current dollar value for the year as a whole. The department's forecast indicates inventory liquidation continuing through the third quarter of 1975 before turning up slightly in the final three months of the year. Relatively strong growth is then predicted during 1976. Indications point to a rapid accumulation of inventories in the fourth quarter of 1974 with the rising number of unsold 1975 model autos contributing substantially to this increase.

Corporate Profits To Shrink

Despite soft demand and a generally sluggish economy during 1974, corporate profits rose by almost 18 percent from a year earlier. The Department of Finance estimates that approximately \$40 billion of corporate earnings in 1974 is attributable to "inventory profits", which occur in a period of sharply rising prices when the lag between acquisition of goods and their sale allows companies to sell relatively low cost stocks at marked up prices. Although prices will continue to rise throughout 1975, the rise will be less rapid and inventory profits will decline by an estimated \$20 billion, according to the department's forecast. This will leave corporate profits for the year 16 percent below the 1974 level and at about the same level as 1973. The corporate profit picture is somewhat confused by the change in inventory accounting methods that firms are adopting to minimize reported earnings and corresponding tax liabilities.

Strong Gains Anticipated For Personal Income

The Department of Finance forecast for personal income indicates a gain of 9.3 percent in 1975, due primarily to wage increases which will amount to 10 to 12 percent for a large number of workers. During 1975 the number of employees whose contracts will be up for renegotiation will be substantially lower than in 1974. The impact of new first year wage adjustments should not be as significant, but many existing contracts contain automatic Consumer Price Index (CPI) adjustments which will boost the growth in wages and salary income.

Unemployment Rate To Reach Post-War High

The Department of Finance is forecasting an average national unemployment rate for 1975 of 7.1 percent, the highest rate since the pre-World War II period. This statistic is not as alarming as it may first appear because of structural changes in the labor force over the last few years and a continually growing participation in the labor force. The forecast assumes that the labor force will increase by 1.7 percent in 1975 and that the number of jobs will remain approximately the same as the average for

Table 6
California Employment by Type
(in thousands)

	1973	1974	Change	1975	Change
Mining	30	32	2	31	-1
Construction	346	334	-12	315	-19
Finance	430	440	10	443	3
Transportation and utilities	470	477	7	476	-1
Government	1,522	1,560	38	1,590	30
Services	1,469	1,538	69	1,575	37
Trade	1,719	1,756	37	1,775	19
Manufacturing	1,648	1,688	40	1,620	-68
Aerospace	491	503	12	490	-13
Other	1,157	1,185	28	1,130	-55
Other	545	530	-15	535	5
Total employment.....	8,179	8,355	176	8,360	5
Civilian Labor Force	8,792	9,065	273	9,220	155
Unemployment	613	710	97	860	150
Unemployment rate	7.0%	7.8%	0.8%	9.3%	1.5%

Current Year 1974-75 Revenue Estimates

The Department of Finance's latest estimate of General Fund revenues for the current year, 1974-75, is \$8,243 million. This is an increase of \$1,555 million above actual 1973-74 revenues. However, this increase is artificially ballooned because Chapter 296, Statutes of 1973, temporarily reduced sales and personal income taxes by \$761 million during 1973-74. If these one-time tax reductions were eliminated from the comparison, then Table 7 shows the growth would have been \$794 million, or 10.7 percent.

Table 7
Growth in General Fund Revenues Between
1973-74 and 1974-75, Adjusted for Legislation
(in millions)

	Adjusted Actual 1973-74*	Dept. of Finance Estimates 1974-75	Change	
			Amount	Percent
Sales and use.....	\$2,998	\$3,360	\$362	12.11%
Personal income.....	2,271	2,520	249	11.0
Bank and Corporation	1,051	1,180	129	12.3
All other taxes	820	828	8	1.0
Total taxes	\$7,140	\$7,888	\$748	10.5%
Interest income	166	169	3	1.8
Other income	143	186	43	30.1
Total revenues	\$7,449	\$8,243	\$794	10.7%

* Estimate of what revenues would have been without the adoption of Chapter 296, Statutes of 1973 which reduced the sales tax rate one-half cent for six months reducing revenues \$322 million and which granted a variable income tax credit reducing personal income tax revenues \$439 million.

This \$794 million growth in revenues is essentially due to price level changes rather than real economic growth. Real gross national product fell by two percent in 1974 and is expected to continue to decline at least through the first six months of 1975. Principal factors contributing to the 1974-75 growth in revenues are:

1. The consumer price index increased 10.6 percent in 1974 and an additional 10.8 percent increase is expected in 1975.
2. An increase in corporate profits of 10.3 percent in 1974 which was realized almost entirely from "inventory profits".

3. Personal income growth of 9.3 percent in 1974 in combination with an acceleration of revenues from higher withholding of income taxes.

Table 8 provides a history of the Department of Finance's revenue estimates for the current fiscal year. These data indicate that the revised budget estimates are \$615 million higher than the original (January 1974) projections. However, \$60 million of the increase is an accounting change in personal income tax revenues.

Table 8
History of Department of Finance 1974-75
General Fund Revenue Estimates
(in millions)

<i>Taxes</i>	<i>Original</i>	<i>Revisions</i>		<i>Revised</i>
	<i>Budget Estimate</i> <i>January 1974</i>	<i>May</i> <i>1974</i>	<i>Legislation</i>	<i>Total</i>
Sales and use	\$3,175.0	\$155.0		\$3,360.0
Personal income	2,289.0	76.0	\$60	2,520.0
Banks and Corporation	1,050.0	100.0		1,180.0
Inheritance and gift	300.2	-63.7		227.0
Cigarette	181.9	2.1		187.0
Insurance	205.0	9.0		204.0
Alcoholic beverage	131.6	.7		130.6
Horseracing	68.6	.4		71.4
Private car	7.1	.5		7.7
Total taxes	\$7,408.4	\$280.0	\$60	\$7,887.7
Interest income	72.2	52.0		169.0
Other revenues	147.6	-1.5		186.5
Total General Fund revenues	\$7,628.2	\$330.5	\$60	\$8,243.2

Major revisions to the current year estimate were made to sales and use taxes, personal income taxes, and corporation income taxes—the three revenue sources most sensitive to changes in the price level. Adjustments to other taxes were minor. The \$64 million reduction in May revised estimates of inheritance tax revenues reflected continued delay in receipts due to protracted estate litigation.

Sales and use taxes for 1974-75 are now estimated to be \$185 million above the original forecast. Although taxable sales are projected to increase from \$64.5 billion in 1973-74 to \$70.5 billion in 1974-75, all of this growth is due to price inflation with real taxable sales estimated to decline by 2.5 percent.

Actual cash receipts during December of 1974 were \$9 million below the latest budget estimates, which may reflect lower than estimated fourth quarter taxable sales. The total revenue loss for the quarter could be from \$15 million to \$25 million but will not be known until final fourth quarter returns are filed in February 1975. First and second quarter taxable sales estimates, however, are conservative and anticipate revenues to increase by 6.6 percent, an increase which is significantly below the expected increase in prices during the first and second quarter of 1975.

Personal income tax revenues are now estimated to be a net of \$171 million above the January 1974 forecast. This change does not include the \$60 million accounting change shown in Table 8 for legislation whereby the renter credit now will be treated as an expenditure rather than as a

tax loss which was the prior practice. The January estimate of 1974-75 personal income taxes has been increased to reflect the following changes:

1. Personal incomes subject to tax have been revised and are now 3 percent higher than the original estimates.
2. Estimates of withholding as a percentage of wages have been substantially increased for two reasons. First, higher withholding amounts reflect higher marginal tax rates which are applicable to increases in income. Secondly, overwithholding is expected to shift 1975 calendar year tax revenues into the current fiscal year, because withholding amounts are based upon the standard deduction, and therefore overstate the tax liabilities of a growing proportion of taxpayers who itemize deductions.
3. A one-time 1974-75 increase in revenues is expected from overwithholding because many heads-of-household have not switched from the single taxpayers schedule to the new heads-of-household schedule authorized by Chapter 1180, Statutes of 1973 (AB 6).

Bank and corporation tax revenues were originally estimated to be no higher in 1974-75 than amounts actually received in 1973-74. The \$130 million increase shown in Table 8 is composed entirely of changes estimated in May 1974 and January 1975. All of the increase expected is due to inventory profits, i.e., upward pricing of finished goods before sale. Excluding inventories, profit increases nationally were zero in 1974 and are estimated to fall by five percent in 1975.

Budget Year, 1975-76 Revenue Estimates

Total state revenues for 1975-76 are projected at \$10,776 million, up \$733 million over the current year. Of this amount, \$716 million represents gains in General Fund revenues which are estimated at \$8,959 million for the year. This increase includes a net transfer of \$77 million in royalties from state-owned lands which would normally go into the Capital Outlay Fund for Public Higher Education (COFPHE). Increases are expected in all major General Fund tax revenues except the bank and corporation tax which is forecast to drop by \$135 million from the current year. A decline of \$29 million in interest income to the General Fund is also expected.

Special fund revenues are forecast to rise by less than 1 percent in the budget year. Gains in motor vehicle license and registration fees and gasoline taxes will be largely offset by the \$77 million in oil and gas revenues that is being diverted to the General Fund. Table 9 compares the revenue estimates of the Department of Finance for the current and budget years.

Sales and Use Tax

Sales and use taxes are estimated at \$3,681 million for 1975-76, accounting for 41 percent of General Fund revenues for the budget year. Taxable sales for calendar year 1975 are estimated at \$73.8 billion, a gain of 7.9 percent over 1974. Table 10 shows taxable sales by major categories for calendar years 1974, 1975 and 1976, both in current dollars and in "real" dollars, i.e., dollars deflated by the consumer price index. The table shows that the overall growth in 1975 is more than accounted for by increases in

the consumer price index and no real gains are expected in the level of sales until 1976. Growth in retail store sales for 1975 is estimated at 9.7 percent, consistent with anticipated gains in personal income. Taxable sales categories for autos and building materials reflect a continuation of depressed conditions in both these industries in 1975. All categories of taxable sales are expected to show substantial increases in 1976.

Table 9
Estimated State Revenue collections During 1975-76
(in millions)

<i>General Fund</i>	1974-75	1975-76	<i>Change</i>	
			<i>Amount</i>	<i>Percent</i>
Sales and use taxes	\$3,360.0	\$3,681.0	\$321.0	9.6%
Personal income tax	2,520.0	2,950.0	430.0	17.1
Bank and corporation tax	1,180.0	1,045.0	-135.0	-11.4
Inheritance and gift taxes	227.0	233.0	6.0	2.6
Cigarette tax	187.0	192.6	5.6	3.0
Insurance tax	204.0	223.5	19.5	9.6
Alcoholic beverage taxes and fees	130.6	135.0	4.4	3.4
Horseracing revenues	71.4	73.8	2.4	3.4
Private car tax	7.7	8.2	0.5	6.5
Total taxes and fees	\$7,887.7	\$8,542.1	\$654.4	8.3%
Other Sources:				
Health care deposit fund	\$74.6	\$75.9	\$1.3	1.7%
Interest on investments	169.2	140.2	-29.0	-17.1
Oil and gas revenues	16.0	81.9	65.9 ^b	"
Other	95.8	119.1	23.3	24.3
Total General Fund	\$8,243.3	\$8,959.2	\$715.9	8.7%
<i>Special Funds</i>				
Motor Vehicle:				
Fuel taxes	\$767.0	\$796.0	\$29.0	3.8%
License fee (in lieu)	325.0	355.0	30.0	9.2
Registration, weight and misc. fees	344.4	350.3	5.9	1.7
Transportation tax	0.5	—	-0.5	"
Cigarette tax	80.1	82.5	2.4	3.0
Sales and use taxes	7.5	27.0	19.5	"
Alcoholic beverage fees	13.9	14.2	0.3	2.2
Horseracing revenues	10.2	9.6	-0.6	-5.9
Oil and gas revenues	106.1	27.2	-78.9 ^b	"
Other	145.1	155.0	9.9	6.8
Total, Special Funds	\$1,799.9	\$1,816.8	\$16.9	0.9%
Totals	\$10,043.1	\$10,776.0	\$732.9	7.3%

^a Percentage change is meaningless because of substantial impact on revenues of administrative or statutory revisions.

^b The \$77 million transfer in oil and gas revenues is the change in the use of these revenues during 1975-76.

Table 10
Taxable Sales in California
(in millions)

	1974	1975	Percent change	1976	Percent change
Retail stores	\$29,145	\$31,965	9.7%	\$35,435	10.9%
Autos, other vehicles and service stations	14,420	15,160	5.1	16,950	11.8
Building materials	6,585	6,980	6.0	7,570	8.5
Manufacturing, wholesaling and miscellaneous outlets	18,250	19,695	7.9	22,345	13.5
Total taxable sales	\$68,400	\$73,800	7.9%	\$82,300	11.5%
California CPI	144.0	159.5	10.8	170.5	6.9
Real taxable sales	\$47,500	\$46,270	-2.6%	\$48,270	4.3%

Personal Income Tax

Revenues from the personal income tax are estimated at \$2,950 million for the budget year. The anticipated gain of \$430 million represents a 17.1 percent increase over 1974-75. The progressive structure of the personal income tax rate schedule makes this tax highly responsive to changes in personal income.

Although the unemployment rate is expected to approach 10 percent during 1975, the average number of persons employed over the year is estimated to be slightly higher than that for 1974. The gains in personal income are anticipated to arise almost entirely from the large wage increases that will be realized in 1975. The higher levels of withholding on salaries and wages that produced upward revisions in the 1974-75 revenue estimate will continue to affect personal income tax revenues in the budget year.

Bank and Corporation Tax

The bank and corporation tax is expected to generate \$1,045 million in General Fund revenues for 1975-76. This amount represents a decline of \$135 billion from the current year resulting from a lower level of corporate income in 1975. Nationally, corporate profits are expected to drop about 16 percent, with taxable corporate profits down 11 percent in California. Corporate income in California is less sensitive to business cycle fluctuations because a smaller percentage of income is associated with the manufacturing sector. Most of the loss of corporate profits in 1975 will be due to a decline in inventory profits. The tax base will also be affected adversely by firms changing accounting methods to minimize the effect of inflation on reported earnings.

Other General Fund Revenues

Moderate gains are expected in inheritance and gift tax revenue (up \$6 million), the insurance premiums tax (up \$19.5 million), cigarette taxes (up \$5.6 million) and alcoholic beverage taxes (up \$4.4 million). Other sources of income include the \$77 million contribution from oil revenues mentioned earlier, partially offset by a decline in interest income from \$169 million in the current year to \$140 million for 1975-76. The lifting of controls on domestic oil prices could increase oil and gas revenues substantially. The amount cannot be estimated because a large portion of these revenues are related to the producers net income which could be restricted by proposed excess profits taxes.

Special Funds

Transportation Fund revenues from motor vehicle fuels are anticipated to rise by 3.8 percent to \$796 million in 1975-76. This estimate assumes an average consumption of 645 gallons of gasoline per vehicle for the budget year, up about 1.5 percent from the current year but 2.5 percent below 1972-73 levels. If measures to reduce gasoline consumption are successful-

ly implemented by the federal government, revenues from this source will be adversely affected. Motor vehicle fees of \$705 million are based on an increase from 15.8 million vehicles registered in 1974 to 16.2 million for 1975.