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Publication Date

2008-02-01

FROM JERRY-RIGGED TO PETERED OUT: LESSONS FROM THE DEUKMEJIAN ERA FOR CONTEMPORARY CALIFORNIA STATE BUDGETING

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The new governor took office in the midst of a major state budget crisis. At the time he took office, it was unclear that state could pay its bills if drastic action were not taken. Yet the incoming governor was committed to a no-tax-increase program. Through borrowing, the state managed to surmount its budget crisis. As the economy recovered and resulting tax revenue flowed in, it even was able to engage in major construction projects. When he stood for re-election, the governor was overwhelmingly returned to office for a second term. Sadly, however, the economy began to slow during that second term. Fears mounted that the state could face a renewed budget crisis.

This description may seem to depict the career to date of Arnold Schwarzenegger. He inherited a budget crisis from Gray Davis who he replaced in the 2003 recall. But the introductory vignette actually refers to the story of George Deukmejian (“Duke”) who was first elected in 1982, inheriting a budget crisis from Jerry Brown. (Deukmejian’s construction projects leaned towards prisons for most of his terms in office, needed as state sentencing laws tightened, rather than the roads and other infrastructure pushed by Schwarzenegger.) And as it turned out, the economic downturn that began to take shape towards the end of Deukmejian’s second term indeed did produce a major budget crisis, a legacy he left for his successor, Pete Wilson.

While the consensus economic forecast for California at this writing is not for recession, some slowing is anticipated. As described in the budget chapter of *California Budget Options 2007*, Wilson spent the better part of his first term wrestling with the Deukmejian legacy – even after imposing a major tax increase *à la* Governor Ronald Reagan.¹

Unique Budget Crises

“The only thing new in the world is the history you don't know.”

Harry S. Truman²

Is the history of the Deukmejian era just that – history? Or does it have relevance for contemporary state budgeting? In past budget chapters, we have noted that there have been a series of budget crises faced by California governors over the decades. Each one was thought to be unique. Ronald Reagan – elected governor in 1966 – inherited a budget crisis from Pat Brown. That crisis was largely the result of enhanced state spending under Brown, a personality clash between Pat Brown and the then-leader of the state Assembly, “Big Daddy” Jesse Unruh, and fuzzy thinking about state budgeting. While fuzzy budget thinking endures – a problem we have also reviewed in previous editions of *California Policy Options* – the Reagan episode (in which the new governor reluctantly put through a major tax increase) seemed unique at the time.³

Similarly, the budget crisis faced by Deukmejian when he took office also seemed to be a special event. In 1978, California voters passed Proposition 13, an initiative that substantially cut local property taxes. Proposition 13 also made it more difficult for the state to enact tax increases by requiring a two thirds vote of the Legislature for such increases. A year later, voters passed Proposition 4 limiting state taxes by formula relative to population, inflation, and personal income.

California at the time was running a budget surplus and initially provided a partial bailout for local governments – especially school districts – that had lost major property tax funding. But the early 1980s saw two back-to-back recessions engineered by the Federal Reserve to halt double-digit inflation. The combination of the drain of bailout funding and loss of tax revenue related to the economic downturn produced the budget crisis faced by incoming governor Deukmejian. Again, the combination of Prop 13 and recession seemed unique to folks back then.

The crisis faced by Pete Wilson also seemed unique. California had long benefited from Cold War military spending. But by the time Wilson was elected in 1990, the Soviet Union was falling apart. The state's aerospace industry was soon dramatically downsizing and military bases in California were closing. Add to this defense downsizing a national recession in the early 1990s and the result was a state budget crisis. Since Cold Wars don't end on a regular basis, the Wilson crisis was interpreted as an unusual one-time event.

But only a decade later, another unique event occurred. Although California's version of high-tech was at one time centered on aerospace, by the 1990s, the Internet and the dot-com boom developed, especially centered in the Silicon Valley. Dot-com mania lifted the stock market and inflated state revenues as taxpayers cashed in their stocks and stock options and paid substantial capital gains taxes on their profits to the state. When the bubble burst, the revenue windfall suddenly disappeared, producing the budget crisis that unseated Gray Davis and brought Arnold Schwarzenegger to the governorship.

Each crisis episode was indeed unique. But it appears that unique events occur on a regular basis. Moreover, some elements of budget making in California remain constant, notably the requirement that to pass a budget, a two thirds vote of the Legislature is needed. Thus, the Deukmejian story – from bust to boom to bust – is a cautionary tale of relevance to today's state budget policymakers. In this chapter, the Deukmejian history is reviewed in detail. Then the focus turns to contemporary budget issues facing California.

Letting George Do It

“Deukmejian is precisely what he appears to be: the quintessential middle-class man, cautiously conservative, but not anti-government, proud of his ethnic heritage, close to his family, interested in making the machinery work better but not intrigued by intellectual movements or revolutionary action.”

Dan Walters
Sacramento Bee columnist⁴

George Deukmejian was not a native Californian. He was born in upstate New York and came to the state after completing his law degree and military service in the mid-1950s. A family-oriented Republican, Deukmejian was elected to the state Assembly from the Long Beach area in the early 1960s and then to the state Senate. He was majority leader in the Senate under Governor Reagan and established himself as a “law-and-order” advocate, at one point pushing through a bill that restored the death penalty in California. In 1978, he became state Attorney General, an office that had been used as a stepping stone to the governorship by such figures as Earl Warren (in 1942) and Pat Brown (in 1958).

Unlike his predecessor and successor as governor, Deukmejian seemed to harbor no ambition beyond the governorship.⁵ He did not run for president as did Jerry Brown (who ran in 1992) or Pete Wilson (in 1996). And he declined to be considered as George H.W. Bush’s vice presidential candidate in 1988.

Deukmejian defeated Lieutenant Governor Mike Curb in the 1982 Republican primary for the gubernatorial nomination. Curb was known for taking advantage of the oddity in the California constitution that makes the Lieutenant Governor the acting governor whenever the governor is out of state. He would sign bills, issue executive orders, and take other such actions whenever Jerry Brown left California. But these mischievous activities counted for less in the primary than did Attorney General Deukmejian’s anti-crime stance.⁶

In the general election, Deukmejian very narrowly won over Democrat Tom Bradley, the mayor of Los Angeles.⁷ A rematch in 1986 between Bradley and Deukmejian, however, produced a landslide for the incumbent governor. A major element in Deukmejian’s re-election campaign was success in resolving the budget crisis left by Jerry Brown.

The Willie Brown Phenomenon

“I tell you I haven’t been around that much glamour since the last time I had lunch with Willie Brown.”

Governor George Deukmejian after a trip to Hollywood⁸

All governors have to deal with the Legislature, a potentially tricky matter when the Legislature is controlled by the opposite party as it was during Deukmejian’s two terms. The most prominent figure in the Legislature at that time was the Speaker of the Assembly, Willie Brown.⁹ Brown, the first African American to hold the speakership, had entered the Assembly in the 1960s as something of a radical. Although he initially clashed with Assembly Speaker “Big Daddy” Jesse Unruh, he eventually learned Unruh’s techniques of keeping control of his house. Those techniques were primarily extensive fundraising shared with Democrats in the Assembly, maintaining a level of goodwill or at least trust with the opposition (something Unruh sometimes failed to do), and always having 41 votes – the number needed to elect the speaker of the 80-seat Assembly.¹⁰

In fact, Brown and Unruh shared a background of growing up in Texas poverty and were alike in many ways. Both were flamboyant personalities. In contrast, Brown and Deukmejian had little in common. Deukmejian did not believe in dramatic social interventions by

government. In his inaugural address in 1983, he called for a “Common Sense Society,” not a New Deal or a New Frontier. Willie Brown was definitely dramatic – not so much in policy initiatives – but in quotable remarks, stylish suits, and public attention. In many respects, Prop 140 of 1990 – which imposed term limits and cut the Legislature’s budget – was an anti-Willie Brown initiative.¹¹ It was the electorate’s way of putting an eventual date-certain ending to the legislative career of Willie Brown – and it did.

However, both Willie Brown and Deukmejian were sufficiently pragmatic to get along at strategic junctures despite their differences in viewpoint and behavior. (As a member of the Legislature, Deukmejian had led the opposition in the state Senate to a Willie Brown bill – ultimately enacted – legalizing homosexuality.) There was sufficient mutual dependence or mutual self interest of the two – particularly when budgets needed to be passed – to keep the relationship at such times on a business-like basis. Indeed, there was often more friction between Brown and his Democratic counterpart in the Senate, Senate President Pro Tem David Roberti, than with Deukmejian.¹²

Background Issues of the Deukmejian Governorship

“Californians reminded their government that in our democracy the people are the highest authority. They told us again, as they have so many times in the past, that life is sacred and that we must do everything that we can to protect the lives of innocent citizens.”

Governor George Deukmejian after voters rejected three state Supreme Court justices over the death penalty issue¹³

The pragmatic relationship between Willie Brown and other key Democrats that sometimes existed in the Legislature and George Deukmejian did not mean that all went smoothly. Republicans pushed for redistricting throughout the 1980s, including attempts at redistricting by initiative.¹⁴ The taxpayer revolt that started with Prop 13 in 1978 continued to echo throughout the Deukmejian era and beyond. And there was a persistent focus on the death penalty.

All of these issues in a complicated way led back to the California Supreme Court and its chief justice Rose Bird. Bird had been appointed as chief justice by Governor Jerry Brown in 1977.¹⁵ As chief justice, she managed to hit all these hot button issues, particularly for Republican voters. Her 1978 confirmation election turned into a major affair when the Court was accused of holding up a case regarding a “use-a-gun, go-to-prison” law until after the election (in which she was narrowly confirmed). The resulting uproar led to a year-long investigation which itself became controversial. But in the end, no charges against the members of the Court were filed.¹⁶

Under Bird, the court overturned various Republican efforts at redistricting. It regularly reversed death penalty cases. And when Prop 13 was litigated, Bird was dubious about upholding a key feature of the popular initiative. Writing for the majority in one case which had involved Deukmejian when he was attorney general, she suggested that he had handled it in a way that garnered “substantial free publicity for his then upcoming (1982) gubernatorial campaign.”¹⁷

The Bird court certainly became an issue in Deukmejian's re-election campaign in 1986 when Bird and other justices were on the ballot for reconfirmation. The governor opposed Bird and two other justices on the grounds that their decisions were marked by a "lack of impartiality and objectivity."¹⁸ Ultimately, the campaign to remove Bird and the others succeeded, giving the governor a chance to replace the three justices.

Another area in which there was a clash of personalities involved the governor and Bill Honig, the Secretary of Education. Prop 13 played a part here because in the post-Prop 13 period, the state played an increasing role in financing local education. Honig, a former local school superintendent, was elected in 1982 to the technically "nonpartisan" position. Although Honig was a Democrat, he defeated a liberal Democrat – Wilson Riles – running as the more conservative candidate (with support from elements of the business community) who favored standards and testing.¹⁹ As such, Honig might have been expected to be compatible with Deukmejian. But in his elected capacity, Honig became a strong advocate for increased school finance, often accusing the governor of shortchanging education.

The school financing issue eventually moved to the ballot in 1988 with the passage of Prop 98, an initiative sponsored by the California Teachers Association and strongly supported by Honig. Under Prop 98, roughly 40% of the state's General Fund was earmarked under complex formulas for K-14 education.²⁰ Prop 98 was in part prompted by the earlier Prop 4 of 1979, whose revenue cap formula led to tax rebates in 1987 – monies that might have otherwise gone to schools – as the state economy picked up.²¹

Economic Background of the Deukmejian Era

"Any fair-minded person knows that predicting the economy is at best somewhat of a primitive art form."

Larry Thomas
Governor's Press Secretary²²

Because economic data are more limited within a single state such as California relative to the entire nation, California economic forecasters often focus on readily available employment information. There are no comprehensive national income accounts for California as there are for the U.S. as a whole. Growth in employment, however, indicates the pace of economic expansion (or contraction during recessions) and therefore is useful information for estimating state revenues for budgeting purposes. Generally, periods when forecasts turn out to be *lower* than the subsequent actual results tend to be periods in which revenues for budgeting are *underestimated*. Periods when forecasts turn out to be overestimates are likely to be associated with budget crises as revenues fall short of planned expenditures.

Table 1 compares forecasts made in December of the year before the forecast period for the percent change in non-farm payroll employment growth (year-over-year) with actual results. These forecasts were made by the UCLA Business Forecast Project and can be taken as in the general ballpark of what other state forecasters were predicting, including those at the California Department of Finance (which has to put together the governor's budget proposal at about the same time). Under that assumption, and given the actual results that occurred, it seems

reasonable that the early 1980s – the final years under Governor Jerry Brown – would be a period of budget crisis (revenues falling short of planned spending).

The early Deukmejian years would, in contrast, be expected to be a period in which there turned out to be surprising large revenue growth – allowing for increased spending and a buildup of budgetary reserves. We might further predict a mini-crisis – but one that could be absorbed – around 1986, followed by pleasant budgeting until the final year or so of the Deukmejian era when a new crisis would unfold. What Table 1 suggests might have happened is what in fact occurred.

The Governor-Elect

“I would predict my relations with the Legislature will be better than Jerry Brown’s.”
Governor-Elect George Deukmejian²³

The story of Deukmejian’s initial budget crisis is well known. As Chart 1 shows, the state ran a surplus (revenue > expenditures) in the years immediately before Prop 13 was enacted in 1978. Thereafter, the post-13 bailout of local government – especially schools – turned the surplus into a deficit. The problem was aggravated by the economic downturn of the early 1980s, which cut into tax revenue. By the time Deukmejian took office, there were questions as to whether the state would be able to pay its bills.

Just after the election, a Deukmejian spokesperson – his incoming Director of Finance Michael Franchetti – accused the Jerry Brown administration of deliberately adopting a budget in the current fiscal year (1982-83) that would “fall apart” just when he left office.²⁴ Since Brown did not know who would follow him in office – Democrat Tom Bradley or Republican George Deukmejian – it is doubtful that he intended to leave a budgetary time bomb aimed at his successor. But he probably did see an advantage in postponing the budget problem until after the November election in which he was running – unsuccessfully as it turned out – against Pete Wilson for the U.S. Senate.²⁵

Whatever Jerry Brown’s intentions may have been, the budget was indeed falling apart. Governor Brown’s Director of Finance Mary Ann Graves admitted the current budget had been based on forecasts of revenue that were “overly optimistic.”²⁶ And almost immediately after the election, Deukmejian suggested outgoing Governor Brown should call a special session of the Legislature to deal with the budget crisis.

At that point, the state was already arranging emergency loans from Bank of America to cover expenses through the issuance of revenue anticipation warrants – somewhat of a misnomer since adequate revenue was not in fact anticipated. Even the Republican Assembly leader Robert Naylor indicated that the crisis was so threatening that a tax hike might be needed. On the other hand, Governor-Elect Deukmejian initially indicated he would veto any tax increase once he became governor (a threat that would not preclude enactment of such an increase in the remaining days of the Brown administration).²⁷ Within a day of his declaration, Deukmejian changed tack and said that he was “*not one who uses the word never, ever, or always.*”²⁸ But he

essentially returned to “never” as the budget battle later unfolded, although applying “never” only to general tax increases as opposed to other revenue-raising measures.

Jerry Brown did call a special session in early December 1982, when the newly elected members of the Legislature were sworn in.²⁹ Meanwhile, state Treasurer Jesse Unruh froze issuance of general obligation bonds to avoid further deterioration of California’s credit ratings. The Community College Board enacted a contingent emergency fee for students, anticipating that the budget situation could worsen. (Community College enrollment had been largely free up to that point.) However, the Legislature was not focused only on fiscal affairs. Democrats were more interested in enacting a legislative redistricting plan that could be signed by outgoing Governor Brown before Republican Deukmejian took office. And in the end no budget fix emerged before Brown left office.

The First Year

“The California Economy is in a hell of a mess.”

David Shulman
UCLA Business Forecast³⁰

“We felt like we couldn’t work with leaders of the Assembly. There were too many issues and too many personalities, so the governor convened a ‘Big Five.’”

Stephen Merksamer
Deukmejian’s Chief of Staff³¹

Since no action on the budget had been taken in the post-election waning days of the Brown administration, whatever was to be done would be under the auspices of the incoming governor and the new Legislature. In his inaugural address, Deukmejian indicated the fiscal crisis could be solved without a “net” tax increase – without defining what “net” as an adjective was supposed to mean – and leading to more speculation that he would ultimately accept a tax hike.³² On taking office, he froze state hiring and cut other expenditures that were within the authority of the governor. Cuts in educational spending triggered increases in University of California and California State University tuitions.³³

Ultimately, however, any major budgetary actions required legislative ascent. Early discussions on taxes involved the possibility of temporary hikes that would disappear automatically when the fiscal situation improved. But the governor’s official budget proposal for fiscal year 1983-84 in fact contained no tax increase, only spending cuts.

Table 2 shows data reported by the Legislative Analyst for each year of the Deukmejian administration shortly after the governor’s initial proposal. Included are the Analyst’s estimate of the current General Fund budget in column 1 (fiscal year 1982-83 when Deukmejian first took office) and the proposal for the coming budget year (1983-84) in column 2. An improved “final” estimate the following summer for the prior year’s budget (1982-83) is shown in column 3.

The surplus or deficit in each year is the difference between “revenues and transfers” and “expenditures.” The reserve can be viewed as the stock of money “in the bank” for the General

Fund at the end of the fiscal year. In principle, the reserve at the end of any fiscal year should be the reserve at the end of the prior year plus the surplus or deficit. In fact, later corrections on the revenue and expenditure sides – unfortunately of unclear origin – lead to still later corrected reserve estimates, shown in column 4. Differencing the final estimate of the reserve (column 5) is an alternative measure of what the surplus or deficit in a given fiscal year actually was.³⁴ In the text that follows, references to budget numbers refer to Table 2's figures.

At the time Deukmejian took office, estimates at the time suggested that the deficit for the current fiscal year (1982-83) was \$1.5 billion and that the reserve at the end of the fiscal year would be \$1.6 billion. Later estimates for the year showed somewhat more revenue and a good deal less of expenditure – in part because of subsequent expenditure cuts. Still, by the end of that fiscal year – which was half over when the new governor took office, the reserve was in negative territory; even the final adjusted figure shows a reserve of about \$450 billion, not a good result for what was then a \$21 billion annual budget. However, the path even to that result was rocky. And although the governor's budget for the 1983-84 fiscal year projected a surplus, it would (based on the numbers available at that time) have left a significant negative reserve at the end of that year.

A week after submitting his no-tax-increase/negative reserve budget for 1983-84 – and hearing an outcry from the Legislature – the governor came back with a revised budget. It appeared that the state would soon run out of cash and would need to issue more registered warrants – even to those expecting tax refunds in the spring of 1983. There would be significant cuts in Prop 13 bailout funds for cities and counties during the 1983-84 fiscal year, tuition increases in higher education, and other unpleasant consequences. Given California's shaky budget situation, state bond ratings fell.

By late January, Tom Bradley – who Deukmejian had only narrowly defeated three months earlier - was already talking about a rematch for the governorship in 1986.³⁵ And there was more discussion about a tax increase that would be triggered on and off automatically by a formula linked to economic conditions. Deukmejian became more and more committed to a budget with no tax increase even though it involved negative reserves and deficit finance – although the trigger-tax idea remained on the table. Other ideas were floated such as a state lottery which the governor initially opposed but later said he was “willing to review.”³⁶

Ultimately, the cash crisis and the threat of the state having to pay its bills in registered warrants produced the pressure needed for a short-term solution. Treasurer Unruh and Controller Kenneth Cory called a press conference and sang “Turn out the lights; the party's over.”³⁷ A bank loan was soon arranged by Treasurer Unruh and a 1-cent sales tax increase – to be triggered in October 1983 or January 1984 by shortfalls in revenue receipts – was passed in mid-February. This device permitted the governor not to enact a general tax increase while at the same time providing some assurance to lenders and bondholders.

With the immediate pressure off the budget issue, Deukmejian began to unveil other initiatives in the areas of crime, education, and welfare. He complained about excessive educational spending demands being made by Bill Honig and about state supreme court decisions under Rose Bird. Whatever the merits of those complaints, the budget crisis and the

fact that Deukmejian had been narrowly elected gave him a narrow based of support. Deukmejian was the only governor from Pat Brown through Arnold Schwarzenegger with a public approval rating below 50% within a short time after taking office.³⁸

May is traditionally the month in which governors issue a revised budget proposal for the coming fiscal year. Complicating the process was the sales tax trigger which was linked to whether the coming fiscal year (1983-84) would end with a negative reserve. The governor predicted there would be a positive reserve while Legislative Analyst William Hamm projected a deficiency. It turned out – after the fact – that the governor was correct, as can be seen on Table 2. Indeed, the reserve turned out to be much larger than the governor was projecting. But all of this depended on the condition of the state economy a year hence, which did not seem especially bright at the time.

The governor proposed no explicit tax increases but suggested closing various “loopholes” in the tax system – which effectively would generate more money. These proposals caused complaints by Republicans in the Legislature that they were *de facto* tax increases about which they had not been consulted. And as is often the case – particularly when the Legislature and governorship are in the hands of different parties – the budget issue became entangled with other concerns such as the operation of the state’s Agricultural Labor Relations Board.

Technically, the Legislature is supposed to pass a budget by June 15. A more significant date is June 30, so that the state can start the new fiscal year with a budget in place. Although in recent years starting the fiscal year with no budget is routine – and various court decisions keep much of the state’s spending going without a budget – in 1983, the June 30 deadline was more ominous than it is today. Nonetheless, there was no budget on July 1, 1983. The Legislature’s majority essentially was insisting on a 1-cent sales tax hike; the governor opposed a budget that included such a hike.

Due to the stalemate, various state checks were not written, including unemployment benefits, disability benefits, and welfare benefits.³⁹ Aggravating tensions in the Legislature between Democrats and Republicans was a ballot proposition – the “Sebastiani initiative” – to undo the redistricting plan passed in the waning days of the Brown administration.⁴⁰ The initiative qualified for the next ballot and Deukmejian could – and did – call a special election to pass the initiative that could cause redistricting before the regular 1984 elections.

Democrats withheld agreement on the budget partly on that issue. But eventually the governor called the election, effectively removing redistricting from the budget negotiations agenda. Within the Republican ranks in the Senate, conservatives deposed minority leader William Campbell and replaced him with Jim Nielsen – seen as less concessionary to the Democrats. A similar coup attempt in the Assembly, however, failed to unseat minority leader Robert Naylor.

The eventual budget worked out with the majority and minority leaders in the Legislature the governor – a grouping later known as the Big Five – was three weeks late. By that time, the Democrats were litigating the special election and much depended on how much spending the governor would veto. As it turned out, he vetoed \$1.1 billion, enough to avoid triggering the

potential sales tax hike. Deukmejian's vetoes enhanced his reputation as the "Iron Duke," protector of California's fiscal integrity.⁴¹

Not all the cuts-via-veto were strictly for fiscal reasons. Substantial cuts were made, for example, in the budget of the Agricultural Labor Relations Board, a body seen by growers as favoring the United Farm Workers union of Cesar Chavez. As noted earlier, although there was no general tax increase, a variety of loophole closings and other technical adjustments in the final budget in effect raised the tax yield, despite complaints from the Republican minority. Nonetheless, the crisis of the first year was essentially over once the new 1983-84 budget was in place. And Governor Deukmejian was widely seen as having bested the Democrats in the Legislature despite their majority.

The New Outlook

"As governor, Reagan promised 'to cut, squeeze, and trim.' But he was never as successful in two terms as Deukmejian has been in half a year of a first term."

Commentator William Endicott⁴²

"I expect the public expects an era of good feeling."

David Roberti
State Senate President Pro-Tem⁴³

"We've exhausted all the hate."

Willie Brown
State Assembly Speaker⁴⁴

Deukmejian's gain in reputation as a winner in the contest with the Legislature was not all positive for the governor. One poll suggested that many Californians regarded him as "stubborn."⁴⁵ A variety of tussles with the Legislature were left over from the budget battle including funds for local governments and whether community colleges would charge added tuition to students. The special election to reopen the redistricting issue was killed by the state Supreme Court, leading the governor to propose his own redistricting plan, first to the Legislature and then – if it refused – to the electorate in another initiative.

All of these issues could have led to bruising confrontations over further cuts but for one development; the California economy began to recover. Revenue flowed into the state. Combined with the budget squeeze built into the 1983-84 budget (including the vetoes), by October 1983, the new revenues led to a sea change in the fiscal climate. Suddenly, Deukmejian's budget director was forecasting large budget surpluses into the future.⁴⁶ Now the conflicts were about where to spend the windfall. The governor wanted to build up the reserve first and then – if sufficient revenue were available – to offer tax rebates. Democrats preferred restoring past spending cuts.

The first round of the new conflict was a refusal of the Legislature to confirm budget director Michael Franchetti. Since Franchetti had been serving for a year without confirmation,

he was forced to step down in early January 1984. Nonetheless, by that time the proposed budget for 1984-85 was already prepared for unveiling.

As Table 2 shows, the estimate for the existing 1983-84 budget surplus had climbed to over \$700 million and would eventually be revised to over \$1 billion. The proposal for 1984-85 contained such attractive elements as a cut in the tuitions charged at UC and CSU. With such pleasant news, the relations between the Legislature and governor began to warm. One Democratic Assemblyman said of Deukmejian, “He’s getting the honeymoon this year that he didn’t get last year.”⁴⁷ But honeymoon was an exaggeration; the governor launched his campaign for a new redistricting initiative shortly after presenting his budget.

Still, the budget climate is easier when revenue is expanding. And for much of the 1980s, despite some budgetary bumps, there was an expansionary climate in the budgetary sphere and in the California economy more generally. But there were differences in priority between the governor and the Legislature. The governor generally pushed for various welfare cost-containment strategies. In the background was the fact that in fiscal 1983-84 and fiscal 1984-85, the state ran a surplus, the General Fund reserve grew, and the earlier emergency bank loan to the state was paid off.

It was this background that produced ongoing debates concerning tax cuts or rebates and increased spending. Particularly pushing for the increased spending option was Secretary of Education Bill Honig arguing for more resources for K-12. The governor was more focused on enhancing higher education, a position reinforced by a *de facto* partnership with UC president David Gardner who took office in the spring of 1984. State labor unions pushed for catch-up pay increases, including “comparable worth” increases for female-dominated jobs.⁴⁸ Despite their differences, the Legislature actually passed the 1984-85 budget by the June 15 deadline. Deukmejian vetoed over \$700 million including money for the comparable worth pay raise.

Meanwhile, despite the on-time budget, politicking continued over such items as a ballot initiative to petition Congress to pass a (federal) balanced budget amendment (removed from the ballot by the state Supreme Court), another initiative aimed at trimming the Legislature’s budget and changing various legislative rules (see below), and an initiative aimed at closing “loopholes” in Prop 13, placed on the November 1984 ballot by Howard Jarvis (co-author of the original Prop 13) – Prop 36, which failed. Another initiative imposed various restrictions on welfare and Medi-Cal payments (Prop 41 – failed). A lottery initiative – pushed by a firm that produced lottery equipment – provided funds earmarked for education (Prop 37 – passed). And finally, a legislative redistricting bill was also headed for the November ballot as Prop 39 – which failed.

The budget for 1985-86 – a fiscal year that would end 4 months before the 1986 gubernatorial election – was also developed in the context of rising revenues. Generally, there were rising resources for education. Indeed, the Legislative Analyst criticized the governor’s initial proposal as oversized. And there were differences in priorities between the governor and the Legislature. The governor tended to emphasize resources for UC and CSU. Assembly Speaker Willie Brown pushed for more aid to Community Colleges. The governor stressed issues of efficiency in government which he translated into contracting out for services and holding down state civil service employment. However, squeezing public employment and

contracting out for services were not concepts favored by the Democratic majority in the Legislature.

A hang-up in budget negotiations was an effort in the Assembly – supported strongly by Speaker Willie Brown – to use the budget process to force divestment from state pension funds of stocks of companies doing business in South Africa. Ultimately, the governor vetoed the South African language in the 1985-86 budget. (He signed an executive order later in the summer instead directing pension funds to review the operations of firms doing business in South Africa.) On the other hand, he left intact a drafting error that prohibited state funding of abortions.⁴⁹ (A court decision subsequently blocked the prohibition from taking effect.)

About \$500 million in spending was vetoed by the governor. The Legislative Analyst at the time argued that the cuts were more than needed to maintain the governor's target of a \$1 billion reserve.⁵⁰ However, as Table 2 shows, the reserve at the end of the fiscal year turned out to be about \$700 million, thanks to an unanticipated deficit as the economy slowed.

By December, the Analyst was pointing to revenues falling below budget projections.⁵¹ California was still benefiting from the defense build-up at the time – the end of the Cold War was not yet in sight – but the national economy was deliberately being slowed by the Federal Reserve, which was antsy about inflation. California could not escape the impact of the national slowdown. Of course, it is precisely with unanticipated adverse events that budget reserves are supposed to deal.

In any event, an oddity of the federal tax code induced California to borrow in the summer of 1986 despite its large reserve. Public sector borrowing receives tax-favored treatment under the federal Internal Revenue Code. The state could borrow by issuing securities whose interest was not taxable, and thus could pay lenders a low rate of interest. It could use the artificially cheap funds to invest at normal market rates of return, and those returns would not be taxed since they were earned by a public entity. In effect, the state could borrow-low, earn-high, and profit from the difference, which state Treasurer Jesse Unruh, in cooperation with the Deukmejian administration, proceeded to do to the tune of over \$2 billion.⁵²

Election Year 1986

“You and I know I desperately want a Democrat down there in the governor’s office.”

Willie Brown
Speaker of the Assembly⁵³

“California has become what it once was and must always remain – America’s leadership state... California has gone from IOU to A-OK.”

Governor George Deukmejian
1986 State of the State address

“I have never entertained the notion of not running (for governor) again.”

Los Angeles Mayor Tom Bradley⁵⁴

By the fall of 1985, the groundwork for the 1986 gubernatorial campaign was being laid. The issue would be the death penalty, law-and-order, and Rose Bird and the California Supreme Court. Budget issues that were so salient in 1982 were relegated to a background role (despite the deficit that actually resulted in 1985-86). Deukmejian could take credit for fixing the budget crisis left by Jerry Brown. And it was becoming apparent that the gubernatorial election would be a re-match with Tom Bradley.

Here Today; Gann Tomorrow

“If we get close to the (Gann) limit, and if, indeed, there are some additional unanticipated revenues, then we would have to consider returning those revenues, because that is what the initiative requires.”

Governor George Deukmejian⁵⁵

Paul Gann was the neglected co-author – with Howard Jarvis – of Proposition 13, the initiative on the 1978 ballot that cut property taxes and created a two-thirds requirement for tax increases.⁵⁶ Although he remained in the shadow of the more flamboyant Jarvis, Gann and his family-run organization, Peoples’ Advocate, moved into the spotlight the following year with Prop 4 – sold as the “Spirit of 13.”⁵⁷ Prop 4 limited state expenditures to a formula based on population, personal income, and inflation.⁵⁸ If revenue exceeded the limit, the excess funds had to be returned to taxpayers.

The taxpayer revolt was in full swing at the time so that apart from Gann himself, the then-Speaker of the Assembly, Democrat Leo McCarthy, was one of the official endorsers of Prop 4. Unlike a related initiative unsuccessfully pushed by Governor Reagan earlier and later budget-limit-by-formula initiatives of Pete Wilson and Arnold Schwarzenegger, Prop 4 passed with 74% of the vote.⁵⁹ Indeed, Prop 4’s victory margin exceeded the 65% “yes” vote received by Prop 13. After Props 13 and 4, an endorsement by Gann became sought after by Republican fiscal conservatives.⁶⁰ However, the economic slump of the early 1980s pulled state revenue and expenditures well below the Gann limit. Years would pass before the limit became an actual constraint.

Gann continued pushing various propositions. His Prop 8 of 1982 – the “Victims’ Bill of Rights” – dealt with issues in criminal justice such as plea bargaining; it passed with 56% of the vote. He sponsored an anti-Legislature, anti-Willie Brown initiative on the ballot as Prop 24 in the June 1984 primary – that imposed various rule changes and budget cuts on the Legislature. Prop 24 passed but was challenged in court by the Legislature, a challenge that ultimately voided the initiative. Nonetheless, some cuts in the Legislature’s budget and staff were made while the challenge was pursued. Meanwhile, Gann began to hint at another initiative to return the Legislature to part-time status (as it was before the mid-1960s). Instead, he put Prop 61 on the November 1986 ballot which would have capped state salaries and which failed.⁶¹

According to former Legislative Analyst William Hamm, prior to Prop 13 and Prop 4, it had been thought that only monied interests could afford to put initiatives on the ballot successfully. But Gann demonstrated with Props 13, 4, and the others, that money could be made by pushing initiatives and seeking contributions to support the effort.⁶² Thus, even

unsuccessful initiative proposals could be profitable. In fact, this supposed discovery was actually a rediscovery of techniques used by California's pensionite movements in the 1930s and 1940s.⁶³

Whatever his motivation, Gann's legacy remained Prop 4. When the governor announced his new budget proposal for 1986-87 in January 1986, he pushed it up almost to the Gann limit by his finance director's calculation. That would mean that it would be difficult for the Legislature to add to the budget without cutting into the reserve and appearing fiscally irresponsible. Indeed, the Legislative Analyst, William Hamm, estimated that the Gann ceiling would be exceeded in the budget proposal.⁶⁴ Beyond that disagreement, Deukmejian criticized the Analyst for characterizing some of the initial "loophole" closing in his first year in office as a *de facto* tax increase. However, Hamm soon left for the private sector, leaving the debate on the Gann limit and the definition of what is a tax increase to others.⁶⁵

One of the ironies of the Gann issue was that business interests, which had originally supported the Gann initiative in 1979, began to back away from it and push for constitutional changes as the ceiling approached. The Gann initiative lumped spending from the General Fund with spending from special funds, notably transportation. As the limit loomed, it began to appear that spending on roads and other infrastructure favored by business interests might suffer. However, the governor, through the Department of Finance, let it be known that he viewed talk of changing the Gann provisions of the state constitution to be "premature."⁶⁶ And he later attacked Bradley for advocating repeal of Gann.⁶⁷

Budget Issues vs. Other Concerns

"Judges should not be independent of the people. They should be as accountable to the people as the governor should be and as legislators should be."

Governor George Deukmejian⁶⁸

Although the Gann matter and other technical fiscal issues were important within policy circles in Sacramento, in 1986 it was hard for Tom Bradley, Deukmejian's Democratic opponent, to obtain traction on such concerns. Two decades later, Phil Angelides campaigning against Arnold Schwarzenegger, would have similar problems. In the public's perception, California was in a severe crisis when the incumbent took over. But at the time of the next election, no one was talking about bankruptcy and paying the state's bills in registered warrants. So the budget problem was popularly assumed to be fixed.

While the Commission on State Finance – a since-terminated agency which made independent forecasts of the budget at the time – predicted (correctly) in the spring of 1986 that fiscal year 1985-86 would show a deficit, state services were functioning normally and the reserve was sufficient to keep them that way.⁶⁹ Exactly what was in the reserve was an issue, since the governor's final budget proposal involved moving some state pension funds into the General Fund. Bradley accused Deukmejian of "*trying to pirate that money, steal it if you will.*"⁷⁰ And, indeed, even the Republican candidate for Lieutenant Governor expressed concern about the idea.⁷¹ But again, outside Sacramento, the controversy was too technical to follow and

the controversy – such as it was – was in any case defused when the Legislature would not go along with the pension diversion.

Of course, many other issues were in play, some of which had budgetary implications but some of which did not. Concerns were raised about the quality of K-12 education, the level of tuition in higher education, abortion, toxic waste programs, AIDs treatment, whether the Agricultural Labor Relations Board was functioning appropriately, and needs for new infrastructure. On South African divestment, the governor reversed his earlier opposition, partly after continued pressure from Willie Brown.⁷²

However, the issue that began to eclipse all others was Rose Bird, chief justice of the California Supreme Court, and her rulings on death penalty cases, Prop 13, and other high-profile matters. “*She has ruled against the people,*” Governor Deukmejian declared.⁷³ And he criticized rival Bradley for failing to take a stand on Bird, who would be up for confirmation (or rejection) in the November 1986 election. The budget entered the campaign only indirectly with Deukmejian labeling Bradley “tax-hike Tom” and boasting of the state’s Triple-A bond rating.⁷⁴ And in the end, Bird was out along with two other justices and Deukmejian had gained a significant victory over Bradley with over 60% of the vote.

Hitting the Ceiling

“We have a limit on what we can spend. It’s easy to say I want more money. It’s harder to say where you can get it.”

Bill Cunningham
Assistant to the Governor for Education⁷⁵

Shortly after the election, the conservative Pacific Legal Center indicated it was considering taking the state to court for exceeding the Gann limit on spending. The position of the Deukmejian administration was that California was still below the limit but that it would be difficult to remain there in the following fiscal year.⁷⁶ However, the new Legislative Analyst, Elizabeth Hill, agreed that limit was likely being exceeded already.⁷⁷ And Bill Honig, re-elected as Superintendent of Schools, was by then talking about an initiative that would relax the Gann ceiling for the benefit of schools. The plan to put such an initiative over would involve mobilizing parents on behalf of the proposition.⁷⁸

At about the same time, there were indications from the Department of Finance that the governor’s goal of keeping a \$1 billion reserve in the General Fund was endangered by higher than anticipated expenditures and lower than anticipated revenues. The earlier forecasts for the economy were scaled back. But there were also pressures to expand funding for transportation. And the Gann limit applied to all state funding, including spending outside the General Fund. (Most state transportation funding was outside the General Fund.) Thus, more roads would have to come at the expense of fewer dollars for ongoing spending from the General Fund (schools, health and welfare, etc.).

In late December, the governor called for mid-year cuts (cuts in the 1986-87 budget) of 2% across the board (which would be 4% for the remaining 6 months of the fiscal year).

Cutbacks in Medi-Cal reimbursements to doctors and other health providers triggered an outcry and litigation. With the Gann limit in place, the alternative of raising taxes (even if the votes could be found for doing so), was off the table. Under Gann, when spending was at or beyond the limit, more revenue would not enable the excess in spending. One solution that began to be pushed was a transfer of programs and revenue sources from the state to local governments to keep the state under the Gann ceiling. Assembly Speaker Willie Brown, however, was hostile to the idea and indicated the Assembly was unlikely to pass such a plan.⁷⁹

The 1987-88 Budget Proposal

“You can’t talk about a surplus when you look at the educational system. You can’t do it.”

Willie Brown
Assembly Speaker⁸⁰

The governor’s January budget proposal for 1987-88 was predicated on keeping within the Gann limit and restoring the reserve to the \$1 billion target. In the short run, the constraint of the limit produced a predictable outcry from those sectors, especially K-12, that felt adversely affected. Within K-12, the governor called for funds for the reduction to be spent on class-size reduction – a major theme of the Pete Wilson administration in the 1990s – but the new funds were to come from cuts in existing educational programs. Cal-OSHA, the job safety program run by the state, would be abolished and the function left to federal OSHA, thus relieving the state of the administrative cost.⁸¹ Not surprisingly, the proposal to terminate Cal-OSHA put the governor in collision with organized labor – which filed litigation to halt the plan. Ultimately, after being shut down, Cal-OSHA was revived by an initiative.⁸²

Deukmejian’s budget proposal led to a series of unfriendly exchanges with school superintendent Bill Honig who termed the governor’s plan a “disaster.” The governor, in turn, called Honig a “demagogue.”⁸³ The atmosphere was more friendly at the higher education level. UC President David Gardner said that at present he would not push for a *change* in Gann, only a *review*, although he might reconsider in the future if the University were harmed.⁸⁴ UC was soon enmeshed in an ill-fated effort to entice the federal government to build the giant Superconducting Super Collider in California – an effort that needed gubernatorial support.⁸⁵

In the longer-run, the Gann limit and the impact on K-12 education set in motion a process that continues to be felt today in the form of a new kind of budgetary constraint, Prop 98 of 1988. Prop 98 earmarks a substantial portion of the budget for K-14 education. In between the passage of Prop 98 and the initial pinch of the Gann ceiling came a large tax rebate for Californians.

The Gann Rebate: Phase I

“I don’t think anything’s going to happen except that people are going to discuss it – period.”

Willie Brown
Assembly Speaker on the Gann Limit⁸⁶

“We are awash in money.”

Jesse Unruh
State Controller⁸⁷

“I’m confident that Californians don’t want to take money from children to give a short-term rebate of a few dollars.”

Bill Honig
Superintendent of Schools⁸⁸

Although the original January 1987 budget proposal was based on an assumption of a revenue shortfall relative to projections, by May it had become apparent that revenues and the economy generally were in fact running ahead of projections. Apart from the state’s economy, changes in federal tax law induced taxpayers to take capital gains, an action that enhanced state income tax receipts on a one-shot basis. Governor Deukmejian soon announced that pursuant to Gann, he would be providing a \$700 million rebate to taxpayers. The announcement sparked a debate with Legislative Democrats pushing for ways to put the money into education rather than return it.⁸⁹

In June, the governor vetoed a bill to spend the \$700 million on education. With Republicans supporting the rebate, an impasse in passing the 1987-88 budget developed. Deukmejian proposed giving taxpayers a choice on their income tax forms of keeping the rebate or giving it back to the government “in the interest of breaking the budget deadlock.”⁹⁰ The proposal did not break the deadlock – which was centered in the Assembly – and the state found itself without a budget at the beginning of the new fiscal year.

Meanwhile, the estimate of the potential surplus that might be rebated had grown to \$1.1 billion. But on July 2, the Assembly relented and the Legislature sent a budget to the governor which – while not explicitly providing a rebate – did not spend the extra funds. It appeared that Assembly Speaker Willie Brown had in effect conceded the general concept of a rebate, but not the precise form it would take. The governor meanwhile made further cuts in the budget, exercising his veto power to remove \$663 million in expenditures.

The Gann Rebate: Phase II

“There is no rush to pass a rebate this year.”

David Roberti
Senate President Pro Tem⁹¹

“We organized. We made our point. But the governor was firm on (the rebate) and had the votes in the Assembly and there was nothing we could do about it.”

Bill Honig
Superintendent of Schools⁹²

“When it became clear there would be a rebate, we moved swiftly to form a compromise that assures that this money will be rebated quickly and in a manner that is fair to the average taxpayer.”

Willie Brown
Assembly Speaker⁹³

In late summer, a California Field poll suggested that a majority of registered voters favored giving the rebate money to schools instead of sending it back to taxpayers. If offered an option of taking it or leaving it to schools themselves, about half said they would take it.⁹⁴ However, the governor had already won the battle that there would be a rebate in principle.

By late summer, after negotiations with the Legislature, Deukmejian pushed for, and received, a rebate plan whereby taxpayers would receive a check in the mail. Other ideas such as a sales tax holiday had been negotiated off the table. In the background for Republicans was the idea that there might be a ballot initiative to relax the Gann limit in 1988. And an ultimately unsuccessful revolt by a group of conservative Democrats – known as the “Gang of Five,” put pressure on Willie Brown to agree to the governor’s preferred rebate.⁹⁵

Voters who received something as tangible as a check in the mail might be less likely to vote for such an initiative. In contrast, a tax holiday – although involving lower administrative costs – would not necessarily affect voter behavior. For Democrats, there was the threat that an initiative to provide rebates might be put on the ballot in 1988 by Republicans if the Legislature didn’t pass its own version. Then voters would be choosing rebates for themselves at the same time they were being asked to relax the limit that made their rebates possible.

Under the rebate plan, checks ranging from \$32 to \$236 would be sent out during the period November 1987 – January 1988 to anyone who filed a 1986 income tax return. Not long after the plan was enacted, the stock market crashed, creating uncertainty over the likely impact on the California economy and the state’s tax revenue. It was unclear whether the pain on Wall Street would reach Main Street. However, by that time the rebate plan was firmly in place. While the impact of the crash proved less damaging than initially feared, the event was a reminder that the economic predictions about the future on which any budget is based contain an element of risk. And having an adequate reserve to deal with adverse contingencies is a fiscal plus.

The Budget for 1988-89

“Once again we said ‘no’ to the tax-raisers and the revenue accelerators and California’s prudent reserve is intact.”

Governor George Deukmejian⁹⁶

The development of the plan for fiscal 1988-89 began relatively calmly. There were, of course, disagreements over priorities. But then revenue for the current 1987-88 year turned out to be less than was projected in January 1988 at the time of the budget message (although somewhat more than what was projected a year earlier). And when all was said in done, the 1987-88 year ended in a deficit well over \$400 million instead of the original planned surplus of well over \$400 million.

Suddenly, the benign budgetary outlook began to appear threatening. Deukmejian proposed some tax “adjustments” which would have raised revenue to deal with the problem, but eventually withdrew them when faced with the charge of *de facto* increasing of taxes, leading instead to charges of a flip-flop. What saved the day was that there was enough of a reserve, even with the rebate, to absorb the cost.

The governor and the Legislature came to agreement on infrastructure bonds, partly because debt repayments were exempt from the Gann limit. But when the governor’s transportation bond appeared on the ballot in June 1988, it lost narrowly, another blow to Deukmejian along with the flip-flop on taxes and the budget deficit.⁹⁷ Gann himself put on the June ballot a proposition – Prop 72 which failed with 38.5% of the vote – to provide more money for transportation, partly by earmarking certain revenue for that purpose.

Also in June 1988, Prop 71 – supported by Superintendent of Schools Bill Honig – would have raised the Gann limit. It failed narrowly with 48.9% in favor.⁹⁸ Along with these electoral efforts, there was an attempt by a rump group of Democrats in the Assembly to depose Willie Brown from the speakership – which he survived with the support of Republican votes.⁹⁹ Despite the excitement on the initiative front and in the Assembly, a new budget for 1988-89 was in place on July 9, after about \$470 million in gubernatorial vetoes. And the final estimates put the budget surplus for that year at around \$1 billion.

Despite the turn of events, the governor had been injured by the sequence of Gann rebate and then budget deficit for the 1987-88 fiscal year. His tight budget and vetoes led to complaints, even from UC officials who normally were pleased with the governor’s interest in higher education. UC President Gardner called the new budget a “*formula for disaster*.”¹⁰⁰

Proposition 98

“They’re going to take all of the cookies out of the cookie jar before we can have any.”

Jeff Thompson

Lobbyist for the California Correctional Peace Officers Association commenting on Prop 98¹⁰¹

“We will give California a first-rate school system. That’s a pretty good bargain.”

Bill Honig

Superintendent of Schools commenting on Prop 98¹⁰²

“Pretty soon, maybe we won’t need to have a Legislature and a governor any more and we’ll do all this by special interest propositions.”

Governor George Deukmejian¹⁰³

While the June 1988 initiatives dealing with the Gann limit failed, an opening was created for revisiting the budget issue. In particular, Honig’s June initiative came close to passing which suggested that with some reframing an initiative relaxing Gann could succeed. The strategy could be to recast the issue – not as a technical adjustment in an abstract budgetary

formula – but as protecting education. If the focus were on education – a popular issue – rather than an obscure formula, the needed 50%-plus-1 might be obtained. Essentially, that was the appeal of Prop 98 which appeared on the ballot in November 1988.

Prop 98 in its original form used two alternative formulas to provide minimum funding for K-14 education relative to the overall budget. (A third formula was later added by Prop 111 of 1990.) It was designed so that had it been in effect the prior year, the tax rebate would have been cut roughly in half and the other half would have gone to education. Rather than overtly lift the Gann limit, Prop 98 earmarked a share of any Gann surplus for K-14 so that the full amount would not be rebated.

Given the education focus, the initiative started out with a California Field Poll in July indicating 63% of voters would approve it. But there was considerable opposition to Prop 98, and not just from budget tightwads. Since the proposition would earmark a substantial chunk of the General Fund for K-14, other possible claimants might see a decline in their shares if it passed. By October 1988, 50% of voters were leaning to “yes.”¹⁰⁴ And in the end, Prop 98 passed with 50.7% of the vote. Voters also passed initiatives reviving Cal-OSHA (the job safety agency that Deukmejian had killed through a budget cut a year earlier) and rolling back and regulating auto insurance. Both of these initiatives were opposed by the governor.¹⁰⁵

The passage of Prop 98 illustrated both the path dependence of public policy and the law of inadvertent consequences. Prop 13 of 1978, by cutting local property taxes, made schools more dependent on Sacramento. The Gann limit of 1979 – which was carried by the coattails of Prop 13 – put a cap on state spending and led to a rebate, angering school supporters who wanted the rebate money for education. In turn, the Gann limit became entangled with a mini-budget crisis in the spring of 1988, which made voters wonder why tax rebates had just been given out. As a result, the natural appeal of doing something for education created the climate for Prop 98 to squeak through at the polls.

With Prop 98, a major restructuring of state fiscal affairs – now built into the state constitution – had been passed by a margin of less than 190,000 out of 9.2 million votes. Shortly after the election, the word from the governor’s office was that another initiative to modify Gann and Prop 98 might be in the works. Meanwhile, cautionary notes were being sounded about the future of the California economy as the Cold War was coming to an end, with adverse consequences for military spending in the state.

Military base closings in California were already sparking concern in areas where such bases were located. More significantly, the end of the Cold War threatened employment in aerospace and allied industries. Perhaps with these clouds over the budget, Governor Deukmejian also announced he would not seek a third term in 1990.

Back to the Future

“There’s no question about our strength, and maintaining our AAA bond rating.”

Governor George Deukmejian¹⁰⁶

“I think all Californians know me well enough by now to know that I would never allow the state to end a fiscal year with a deficit.”

Governor George Deukmejian¹⁰⁷

“California is hampered by home prices that are nearly twice the national average, and if its economy slows, other states will begin to look more attractive. California also suffers from fiscal gridlock, and has spent inadequately on its infrastructure, including transportation... Add to this mix a substantial cut in the defense budget and a corresponding slowdown in the state’s economy, and it may be that these problems will no longer be overlooked.”

David G. Hensley
UCLA Business Forecast in December 1990¹⁰⁸

“The conclusion is nearly incontrovertible: the bleak evidence on employment, help-wanted advertising, and retail sales in California – reflected in budget problems throughout the state – strongly suggest that, like the U.S., California has slipped into recession.”

David G. Hensley
UCLA Business Forecast a year later in December 1991¹⁰⁹

The Department of Finance did not initially forecast an economic slowdown when the governor made his proposals for the 1989-90 budget in January 1989. While the 1988-89 fiscal year finished with a significant budget surplus, the forces that would throw the California economy into severe recession in the early 1990s were already becoming apparent by the end of 1990. The 1989-90 budget, signed a week after the July 1 deadline, ended in significant deficit despite substantial cuts by the governor using his veto power. As a result, the General Fund reserve was partially depleted, setting the stage for even worse results the following year.

Tax Exceptions

“This proposal will give the people of this state the opportunity to decide whether they are willing to pay a little bit more for congestion relief, safer trips, cleaner air and a dynamic economy...”

Governor George Deukmejian on Prop 111¹¹⁰

Meanwhile, complaints about traffic congestion were mounting. The governor called a “transportation summit” in February 1989. Another summit followed in March. Eventually, political forces around transportation infrastructure cut a deal with the educational establishment and put Prop 111 on the ballot in June 1990. With budgetary problems becoming apparent, the floating of already-approved bonds for various capital projects was delayed in January 1989.¹¹¹ So if there was to be investment in transportation, a new revenue source would be needed, something Prop 111 – termed by Willie Brown “*an awesome legislative achievement*” – promised to provide.¹¹² When put to the voters, Prop 111 passed with 52.4% of the vote.

Prop 111 added another formula to Prop 98 and set the share of any Gann surplus going to K-14 at 50%. It carved out exceptions to Gann for transportation and capital projects and raised the gas tax. In an exception to his usual stance on taxes, Deukmejian supported the gas tax increase (9 cents/gallon) or at least the idea of putting it on the ballot for voters to decide.

The combination of Props 98 and 111, along with the deep recession that was awaiting California in the early 1990s, effectively made the Gann limit a non-constraint for a decade. It was only at the next budget peak during the dot-com boom that Gann again began to become a constraint. Official estimates now indicate the modified Gann limit was exceeded in 1990-00, but this overage was not clear at the time and no rebates were provided. The subsequent dot-com bust and the resulting budget crisis of the early 2000s once again made the modified Gann limit a non-issue. In contrast, Prop 98 remains to this day a major factor in California budgeting as does its indirect progenitor, Prop 13.

Yet Prop 13 might also have been modified in June 1990. An initiative nearly made it to the June 1990 ballot that would have created a “split-roll” system of property assessment, essentially raising property tax revenue from non-residential commercial land and structures. Proponents handed in their petitions to the Secretary of State, fully expecting to put their proposal on the ballot. Opponents by then were already mounting a fundraising campaign with the same expectation. However, the petitions unexpectedly fell short by about 50,000 signatures and the anticipated contest never occurred.¹¹³ What might have happened to the split-roll proposal at the hands of voters will never be known. Nor can the effect that proposal might have had on the vote for Prop 111 (if both had been on the ballot at the same time) ever be known.

Just as Prop 111 involved a shift in the governor’s normal stance against tax-raising, so, too, did an act of nature. An earthquake in the Bay Area in October 1987 badly damaged the Bay Bridge and caused the collapse of a section of the I-880 freeway. After discussion with legislative leaders, the governor called a special session of the Legislature to deal with emergency spending on repairs and other earthquake-related relief. After some contentious debate, the Legislature passed a temporary one-quarter cent increase in the sales tax effective for the 13 months beginning December 1989.

Leave it to Pete

“I am saying to my friends in the Legislature, and to those who wish to succeed me in office, that sooner or later we have to pay the piper.”

Governor George Deukmejian
1990-91 budget message¹¹⁴

“I don’t want to leave the next administration, regardless of who it is, with (a budget) problem.”
Governor George Deukmejian¹¹⁵

In January 1990, California’s Self Esteem Task Force produced its final report.¹¹⁶ While the much-parodied Task Force reinforced the state’s psycho-babble/hot-tub image, the national picture of the state was soon to change to one of fiscal, economic, and social decay. A coming combination of national recession, reinforced in the state by cutbacks in military spending – not to mention a major urban riot in Los Angeles – led to an image of California in continual crisis. Whatever esteem California had for itself was soon to be depleted. The full extent of this unfortunate state of future affairs was not yet apparent, but there were already signs that the next fiscal year would not be benign.

The January budget proposal by the governor for fiscal 1990-91 – a budget that would be inherited half way through by his successor – started with the usual cautionary notes. Soon, the legislative analyst was pointing to a need for cutbacks in existing services to make the budget balance.¹¹⁷ As disappointing revenue reports came in for the current fiscal year (1989-90), it became apparent that the state was already likely to be running a deficit. But in a gubernatorial election year – particularly with the gas tax hike under Prop 111 already on the June ballot – there was little political incentive for candidates to focus on California’s fiscal difficulties.

U.S. Senator Pete Wilson had little opposition in obtaining the Republican nomination for governor and didn’t have to say much until the Democrats had a nominee. The two Democratic rivals, Dianne Feinstein – former mayor of San Francisco – and John Van de Kamp – the state’s attorney general – were involved in a tough primary campaign but one focused on the death penalty and other general issues of leadership.¹¹⁸

The governor – who was not running for anything – threatened vetoes if fiscal “reforms” were not part of the budget package.¹¹⁹ And in May he ordered a freeze on certain categories of spending and personnel. It had become clear that his originally proposed 1990-91 budget was not balanced and would push the declining reserve into negative territory.¹²⁰

As the July 1 deadline approached, the governor submitted a list of major cuts including suspension of Prop 98 guarantees. Given the magnitude of the estimates required to deal with the revenue squeeze, however, the July 1 budget deadline came and went without an agreement. By the latter part of July, judges were ordering the state controller to pay this or that bill despite the lack of a budget. A new budget was finally signed at the end of July including vetoes of over \$1 billion. The governor had to give up on his Prop 98 suspension which became a major hang-up in the budgetary negotiations.¹²¹ His intent was to maintain the reserve but final estimates put the reserve when the new fiscal year ended at around \$900 million.

By September 1990, the California Field Poll found that 7 out of 10 surveyed thought that Governor Deukmejian was leaving the state the same or worse than he found it when he inherited the fiscal crisis from Jerry Brown.¹²² Meanwhile, during the campaign, Pete Wilson said only that he would consider raising taxes as a last resort, while Diane Feinstein specifically proposed extending the temporary sales tax that had been enacted to deal with the 1989 earthquake. She also proposed raising income taxes on higher income individuals and families.¹²³

Wilson supported a term limits initiative on the November 1990 – Prop 140 – that would primarily affect the Legislature; Feinstein opposed it – thus identifying her campaign with Willie Brown, who was a public symbol of legislative dysfunction. In the end, Wilson won by less than 200,000 votes, a narrow finish reminiscent of George Deukmejian’s first win against Tom Bradley in 1982 – also in a time of budget crisis. And Prop. 140 passed, permanently altering the legislative landscape in California.

After the election, the outgoing governor called the Legislature back into session to deal with a further drop in projected revenues. He imposed another cut in state spending and a hiring freeze. But the Legislature effectively decided to await the new governor and took no action, a repeat of what occurred during Jerry Brown’s final days. Unlike Brown, however, Deukmejian

did not seek political office after leaving the governorship but returned to private law practice and various civic causes. However, he was involved in the 2002 gubernatorial election, supporting a candidate for the Republican nomination.¹²⁴

Absent action by the Legislature to deal with the budget crisis immediately after the 1990 election, the problem was passed along to Deukmejian's successor. In what turned out to be an understatement, Pete Wilson – shortly before taking office – said, *“It’s going to be tough. I’m going to present a budget... where I am compelled to spread some pain.”*¹²⁵ And so he did.

Contemporary Lessons

“We are a big state and we have big needs.”

Governor Arnold Schwarzenegger¹²⁶

Despite the efforts of the “Iron Duke” to protect state fiscal soundness, in the end he left his successor a multi-year budget crisis – one at least as severe as he had inherited from Jerry Brown. Eventually, as described in detail in the 2006 edition of *California Policy Options*, Pete Wilson was able to resolve the problem, in part because the dot-com boom in northern California was beginning to overwhelm the depressed economy in the south where aerospace cutbacks were concentrated. Thus, Wilson's successor – Gray Davis – had a rising economy and a major influx of revenue when he took office in January 1999.

Sadly, as Chart 2 illustrates, however, the boom inherited by Davis turned to bust in 2000-01.¹²⁷ Flaws in the deregulation scheme for the state's electricity market led to rolling blackouts. General Fund revenues of over \$6 billion were used to bail out the utilities. These funds were subsequently reimbursed to the state through the issuance of special bonds – to be repaid by electricity ratepayers. But by that time the dot-com bust had substantially reduced state tax revenues. The General Fund reserve was soon exhausted and the state resorted to short-term borrowing through revenue anticipation notes and warrants. Creative financing through tobacco bonds (which securitized the flow of payments the state had been receiving from tobacco litigation) was also used. By 2003-04, the state faced a major cash crunch in keeping its services going.

These circumstances produced the unprecedented recall of Governor Davis and his replacement by Arnold Schwarzenegger in the fall of 2003. The immediate cash crunch was handled by voter-approved, large-scale, long-term borrowing for general operations during the first year of the Schwarzenegger administration. After that period, various positive developments aided the state's fiscal outlook.

General economy recovery from the trough of the dot-com bust added to state tax receipts. In addition, a one-time tax amnesty added \$4.6 billion in 2004-05, producing the surplus for that year shown on Chart 2. (There would have been a deficit, absent the amnesty.) Refinancing of the tobacco bonds produced over \$500 million in 2005-06. In addition, a rising stock market and escalating real estate values produced tax revenue from capital gains, an echo of the experience of the dot-com boom of the Davis years. The budget showed a surplus in 2005-06 but reverted to a deficit in 2006-07.

Throughout the recovery period, the Legislative Analyst continued to warn of a structural deficit in the General Fund, i.e., a chronic tendency toward imbalance running into the future. Table 3 shows various iterations of the state budget proposed for 2007-08. The governor's January 2007 proposal included a deficit of over \$800 million. His May revise made roughly the same assumptions on revenue but the proposed deficit rose to about \$1.5 billion. It included a controversial proposal to lease the state lottery to a private operator and a sale of the "EdFund" that makes loans to students. Note that sales of assets – while they bring in one-time shots of cash – can mean reduced future revenues.

Other Concerns

"You can feel that the time is right. As a matter of fact, both leaders have said to me, 'We will get this done.' My Republican friends have said, 'We will get this done.' Ladies and gentlemen, we will get this done. California is going to lead the nation in breaking new ground to meet the health care needs of its people."

Governor Arnold Schwarzenegger
2007 State of the State speech

Although enacting a budget is a major gubernatorial priority, there are many other issues on the political agenda – some which have budgetary implications; others which don't – in any given year. As it happened, 2007 was a full year on that dimension. There were continued concerns about enhancing state infrastructure, an effort that had begun in 2006 with a series of bond measures. In particular, contentious proposals were put forward relating to "water storage," a euphemism increasingly applied to dams, and revival of the Peripheral Canal in some form, a northern California project rejected by voters in the early 1980s.

To the infrastructure issue, the governor added his objective of a universal health insurance plan, modeled on a program recently passed in Massachusetts which included an individual mandate. The governor's health proposals were soon augmented by plans from the Democrats in the Assembly and Senate – eventually melded into a single proposal – which involved a somewhat less comprehensive employer mandate/pay-or-play proposal.¹²⁸ Various environmental concerns related to greenhouse gas were also on the table.

Apart from items the governor was pushing, prison overcrowding and problems in the prison health care system were leading to increasing court intervention of the state correctional system. Connected to these matters were proposals to export excess prisoners to facilities in other states, to construct more prison capacity, and to change sentencing and parole policies. The Democratic leadership in the Legislature also had its own agenda of pushing up the date of the California presidential primary of 2008. That move would also enable an initiative to be put on the ballot in time to modify terms limits. These revised limits would allow the current legislative leadership to continue in office.

Various interest groups had items for the state's agenda, too. Community Colleges were always included under the Prop. 98 umbrella, but tended to be stepchildren relative to K-12. The Colleges began to push for a funding guarantee initiative of their own, which qualified for the

2008 presidential primary. If passed, such an initiative would add to the complications already entailed in ballot box budgeting. Indian gaming tribes signed compacts with the governor which unlike some earlier accords did not include the collective bargaining protections sought by labor unions. In a complicated way, the gaming compact issue became tied to that of the initiative changing term limits.¹²⁹

Budget Impasse

"He thinks it's better to have respect for all four caucuses and allow them to do their jobs."

Governor's spokesperson Aaron McLearn
on the governor's absence from budget negotiations¹³⁰

"State services are disrupted and hard-working families are not going to get their paychecks. I think that Californians deserve much better than that."

Governor Arnold Schwarzenegger
on the absence of a budget in early August 2007¹³¹

Despite the full policy agenda for 2007, Governor Schwarzenegger seemed oddly aloof from the goings on in the Legislature until August. No Republican was willing to introduce the governor's health insurance plan and it was initially said that health would be deferred until after a budget was enacted. An impasse developed and on July 1, 2007, the state had no budget in place. However, the Assembly eventually passed a budget with an ostensible deficit of around \$700 million which the Senate – needing at least two Republican votes and having only one – was unable to pass.¹³² All of the budget proposals dipped in one way or another into the transportation fund, a practice which voters have disapproved but which is seemingly impossible completely to halt. But any thought of dealing with state pension obligations by issuing bonds – an idea that had come and gone in varying intensity going back to Gray Davis – was seemingly taken off the table by a court decision in early July.¹³³

When Deukmejian was governor, lack of a budget after July 1 led to immediate adverse consequences. State bills went unpaid. But because overdue budgets have become commonplace since that era, court decisions keep much of the money flowing. And that fact that not having a budget in place has little immediate consequence to the general public means that there is reduced pressure on the Legislature and governor to come up with a deal.

There were periodic negotiations between legislative leaders, sometimes with the governor, sometimes not, as the summer wore on. The legislature adopted a deal – albeit a deficit deal – in July but obtaining the necessary votes from Senate Republicans proved to be a sticking point. Republicans came up with a list of budget cuts they wanted designed to bring the budget to a nominal balance. They also wanted assurances that Attorney General Jerry Brown would not use environmental rules to challenge local infrastructure and development efforts.

Two Republican Senate votes were needed. But only Senator Abel Maldonado (Santa Maria) – viewed as coming from a swing district – was willing to supply a vote. Another Republican senator, Jeff Denham (Atwater) – also seen as having a swing district – was seen as a likely eventual vote. But Denham was also expected to run for Lieutenant Governor – and

would thus need to appeal to the Party's base in the 2010 primary. In the end, he was unwilling to bend.

Without the Denham vote, the budget negotiation remained stalemated until the third week of August. Governor Schwarzenegger began visiting organizations that were not receiving state funds and were threatened with closure or shutdown. There was increased talk – including musings from the governor – about relaxing the two thirds vote requirement.¹³⁴ Such a move would require a constitutional amendment but were such an amendment to pass, Republicans would be greatly disempowered. There was also pressure on the governor to produce a budget deal so that his health insurance proposal could be debated. In the end, Senate Minority leader Dick Ackerman – after reaching an accord with the governor and the majority leadership – provided the second Republican vote.

The final budget, as shown on Table 3, was nominally balanced, thanks to vetoes of \$700 million by the governor (although not identical to cuts earlier requested by the Republican legislators). There was also a deal which ostensibly would limit the Attorney General in challenging projects funded by infrastructure bonds on environmental grounds.¹³⁵ The Legislative Analyst noted that while the budget was ostensibly balanced, in the sense that the two components of the reserve was projected to remain unchanged through the 2007-08 fiscal year, it may have underestimated the amount of K-14 spending required under Prop 98, possibly as much as \$800 million. It assumed a sale of the EdFund, really an asset sale rather than what might properly be considered “revenue” of \$1 billion. Beyond those issues, a slowdown in the economy or reductions in capital gains revenue associated with the stock market and the real estate market, could reduce revenues below projections.

The Longer Term Outlook

“California’s budget still lives on the razor’s edge. When there is an economic slowdown, we usually have three choices; we increase taxes, or we make deep cuts, or both.”

Governor Arnold Schwarzenegger¹³⁶

In the short term, no budget crisis is at hand. But the longer term is more worrisome. The 2006-07 year finished with a (declining) balance in the General Fund reserve of about \$4 billion. However, the state during the budget crisis of the early 2000s borrowed well over \$15 billion in deficit financing bonds and tobacco bonds. Thus, absent the earlier borrowing, the reserve – even if it does not decline during 2007-08 – would be substantially negative.

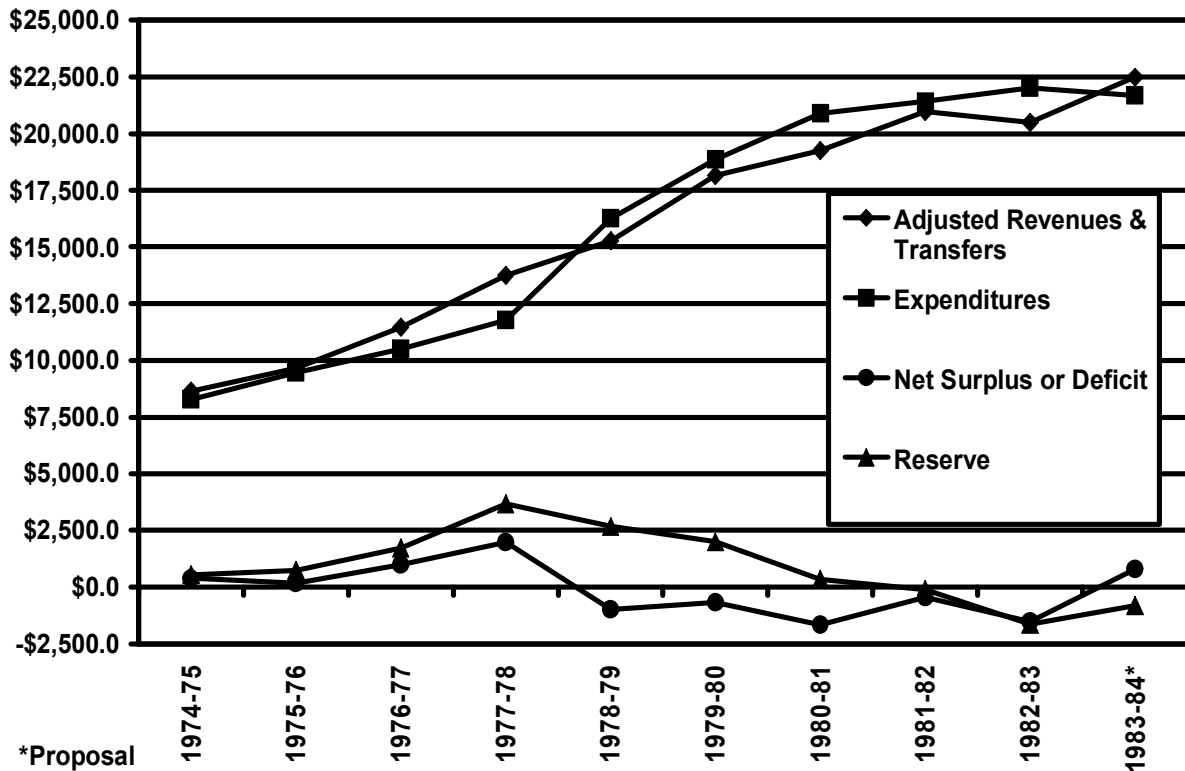
The controller estimates that the state has well over \$14 billion in “unused borrowable resources” (funds outside the General Fund that could in principle be used to cover deficits). So California could go on with deficit finance for a limited time, even if the economy slows and produces revenues below those assumed in the budget compromise. But the lessons of history suggest that resources can disappear quickly in a crunch unless drastic action is taken – which is not always feasible given the political roadblocks in the Legislature.

Governor Schwarzenegger’s term will end in January 2011. Will he go out as a Pete Wilson – who started with a budget crisis but left a healthy budget to his successor? Or will he

go out following the path of George Deukmejian – who started with one crisis and ended with another? When he thinks about the budget, that question should be upper-most in the mind of the governor.

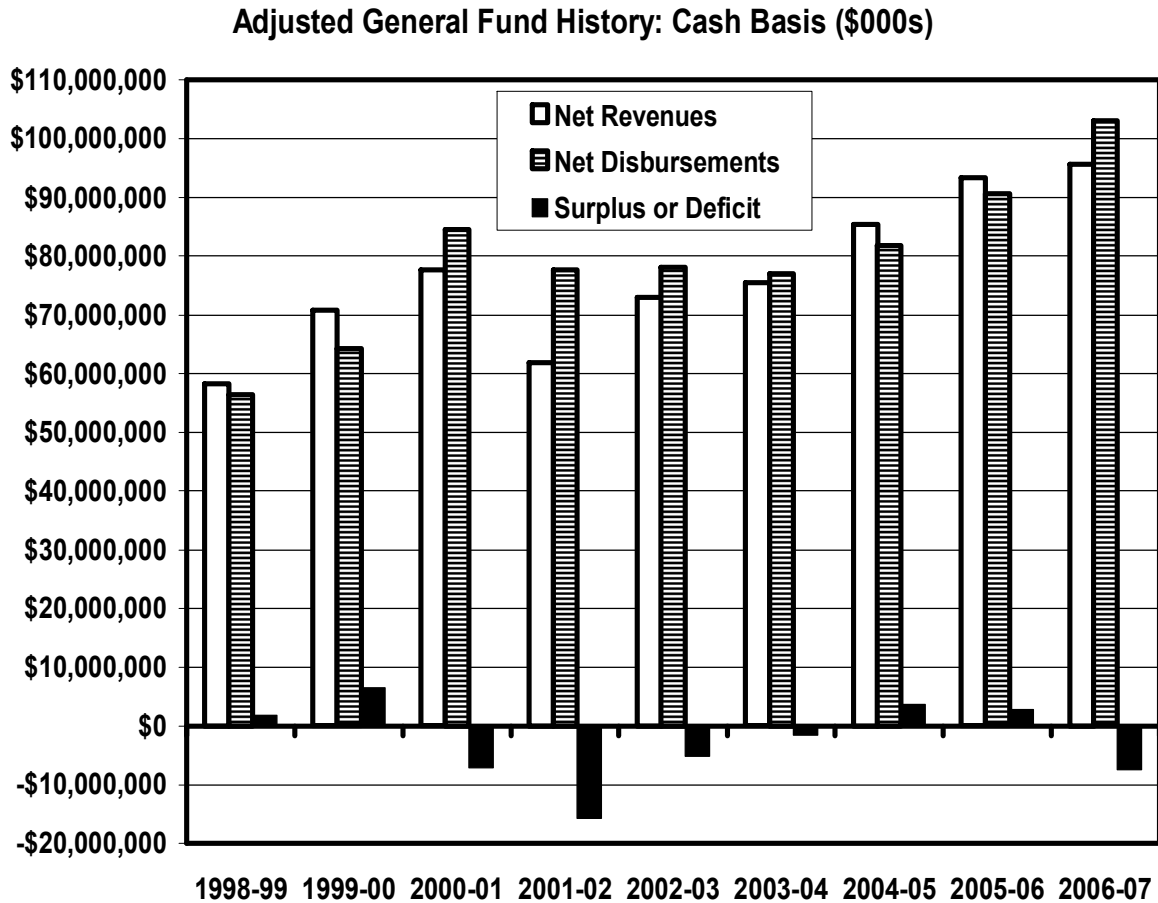
Chart 1

Background: Deukmejian's Initial Budget Proposal (\$ millions)



Source: Data from Legislative Analyst's annual reports on the January budget.

Chart 2



Note 1: 2000-01 includes state spending on electricity during power crisis.

Note 2: 2001-02 and 2002-03 includes as revenue reimbursement of General Fund for electricity from electricity bonds.

Note 3: 2001-02 and 2002-03 exclude receipts from tobacco bonds.

Note 4: 2004-05 includes receipts from tax amnesty.

Note 5: "Non-revenues" reported in the cash statements are excluded from the revenues shown on the chart. These flows generally involve transfers between other funds and the General Fund.

Source: State Controller, cash statements.

Table 1: UCLA California Employment Growth Forecast vs. Actual Results

Year*	Forecast	
	Made in Prior December	Actual Result
1981	3.0%	1.4%
1982	-5%	-1.8%
1983	0.2%	1.1%
1984	4.3%	4.8%
1985	3.5%	3.7%
1986	3.1%	2.6%
1987	3.2%	2.9%
1988	1.0%	3.8%
1989	2.2%	2.7%
1990	1.9%	2.1%
1991	-6%	-1.1%

Note: Figures are year-over-year changes.

Source: UCLA Business Forecasts for California, December before each year shown. Statistical Abstract of California.

Table 2: California State Budget History, General Fund

\$ Millions	Column 1	Column 2	Column 3	Column 4	Column 5
	1982-83E	1983-84P	1982-83	1982-83	1982-83
Rev+Trn	\$20,489.7	\$22,479.4	20943.3		
Expend	\$22,005.0	\$21,674.6	21461.5		
Surp/Def	-\$1,515.3	\$804.8	-\$518.2		-446.5
Reserve	-\$1,633.8	-\$829.0	-521.3	-449.6	
	1983-84E	1984-85P	1983-84	1983-84	1983-84
Rev+Trn	23367.6	25825.5	23515.5		
Expend	22641.2	25076.4	22575.2		
Surp/Def	\$726.4	\$749.1	\$940.3		1021.4
Reserve	205.2	\$954.3	\$490.7	571.8	
	1984-85E	1985-86P	1984-85	1984-85	1984-85
Rev+Trn	26076.9	27922.1	26280.8		
Expend	25582.2	27864	25466.4		
Surp/Def	\$494.7	\$58.1	\$814.4		883.5
Reserve	985.3	\$1,043.4	1386.2	1455.3	
	1985-86E	1986-87P	1985-86	1985-86	1985-86
Rev+Trn	28186.6	31023.6	27801.8		
Expend	28709	30698.9	28570.9		
Surp/Def	-\$522.4	\$324.7	-\$769.1		-741.2
Reserve	843.3	\$1,168.0	686.2	714.1	
	1986-87E	1987-88P	1986-87	1986-87	1986-87
Rev+Trn	30764.8	31742	32277.1		
Expend	30889.8	31263.6	31227.2		
Surp/Def	-\$125.0	\$478.4	\$1,049.9		-52.6
Reserve	561.3	\$1,039.7	625.9	661.5	

See definitions on next page.

Table 2: California State Budget History, General Fund – Continued

\$ Millions	Column 1 1987-88E	Column 2 1988-89P	Column 3 1987-88	Column 4 1987-88	Column 5 1987-88
Rev+Trn	33678	36249	32264.9		
Expend	33343	36101	32751.8		
Surp/Def	\$335.0	\$148.0	-\$486.9		-436.9
Reserve	962	\$1,110.0	174.6	224.6	
	1988-89E	1989-90P	1988-89	1988-89	1988-89
Rev+Trn	36002	38877	36648.3		
Expend	36002	38010	35763.7		
Surp/Def	\$0.0	\$867.0	\$884.6		1027.2
Reserve	-83	\$784.0	1109.2	1251.8	
	1989-90E	1990-91P	1989-90	1989-90	1989-90
Rev+Trn	39775	43102	38749.5		
Expend	40120	42613	39455.9		
Surp/Def	-\$345.0	\$489.0	-\$706.4		-460.6
Reserve	485	\$974.0	545.4	791.2	
			1990-91	1990-91	1990-91
			38213.5		
			40263.6		
			-\$2,050.1		-1710.8
			-1258.9	-919.6	

Definitions for Table 2:

Rev+Trn = Revenue and transfers. Expend = Expenditures. Surp/Def = Surplus or Deficit. E = Estimate. P = Proposed. Column 1 = Estimate for the current fiscal year made in January of that year, i.e., half way through the year. Column 2 = Governor’s January proposal for the coming fiscal year. Column 3 = “Final” figures for the fiscal year from the Department of Finance but excluding adjustments for differences later determined for revenues and expenditures. Column 4 = Final figures for reserves including adjustments for differences later determined for revenues and expenditures. Column 5 = Surplus or deficit calculate from differences in reserves in Column 4.

Source: Department of Finance; Legislative Analyst’s Office.

Table 3: The 2007-08 General Fund Budget (\$ Millions)

	January Proposal	May Revise	August Final

Revenues & Transfers*	\$101,278	\$101,253	\$101,239
Expenditures	\$103,141	\$103,765	\$102,258
Total Reserve At End of Fiscal Year**	\$2,085	\$2,199	\$4,069
Change in net Reserve (Operating Surplus or Deficit)	-\$840	-\$1,489	+\$3

*Includes transfers to Budget Stabilization Account (part of net reserve). Such transfers are negatives (reductions in revenues and transfers).

**Combination of Budget Stabilization Account (a reserve established as part of the voter approval of the Economic Recovery Bonds) and the Reserve for Economic Uncertainties.

Note: The figures here follow the methodology of the Department of Finance.

Source: California Department of Finance

Endnotes

¹ Daniel J.B. Mitchell, "Wilson's Woes Should Keep Us on Our Toes: Where is Plan B for the California State Budget" in Daniel J.B. Mitchell (ed.), *California Policy Options 2007* (Los Angeles: UCLA School of Public Affairs, 2007), pp. 31-78. Past editions of *California Policy Options* can be found at: <http://repositories.cdlib.org/uclarpa/cpo/>

² Quoted on History News Network website: <http://hnn.us/articles/1328.html>

³ Daniel J.B. Mitchell, "Governor Reagan's Ballot Box Budgeting: One That Got Away," *Southern California Quarterly*, vol. 89, number 2 (2007), pp. 195-227.

⁴ Dan Walters, "Unspectacular Governance," *Sacramento Bee*, February 19, 1986.

⁵ There were flurries of speculation about presidential ambitions but little concrete evidence during the Deukmejian years.

⁶ Curb came from the entertainment industry, composing film scores and running a singing group. He returned to entertainment after losing a bid to reclaim the Lieutenant Governorship in 1986.

⁷ Some polls suggested that Bradley would win. The discrepancy between the polling results and the actual election is sometimes referred to as the "Bradley Effect," an alleged tendency of white voters to respond that they favored a black candidate when they in fact did not. However, in a very close election, virtually any event could be said to be the factor that tipped the election. Some analysts have expressed doubt that there was a Bradley Effect in the polling related to the 1982 gubernatorial race. See Jack Citrin, Donald Phillip Green, and David O. Sears, "White Reactions to Black Candidates: When Does Race Matter?," *Public Opinion Quarterly*, vol. 54 (Spring 1990), pp. 74-96.

⁸ "The Guv is Getting His Act Together," *Sacramento Bee*, February 9, 1986.

⁹ See James Richardson, *Willie Brown: A Biography* (Berkeley: University of California Press, 1996), Richard A. Clucas, *The Speaker's Electoral Connection: Willie Brown and the California Assembly* (Berkeley: Institute of Governmental Studies Press, 1995), and Willie Lewis Brown, Jr., "First Among Equals: California Legislative Leadership, 1964-1992," oral history conducted in 1991 and 1992 by Gabrielle Morris, Regional Oral History Office, The Bancroft Library, University of California, Berkeley, 1999.

¹⁰ Brown had also learned the lesson of counting the votes the hard way, having lost his first attempt at winning the speakership to Leo McCarthy (after not properly counting the votes he actually had).

¹¹ Prop 140 was pushed by Peter F. Schabarum, a member (and chair at that time) of the Los Angeles County Board of Supervisors. Pete Wilson endorsed Prop 140 as part of his campaign for the governorship in 1990.

¹² In contrast, although Pete Wilson discovered that Willie Brown could be cultivated when budget matters had to be resolved, Wilson was a more reluctant partner than Deukmejian. But Wilson needed Brown more than Deukmejian did because the Wilson-era budget crisis lasted longer.

¹³ Second inaugural address, January 5, 1987, available at http://www.californiagovernors.ca.gov/h/documents/inaugural_35b.html

¹⁴ Since the Pat Brown era, Republicans have rarely controlled the Legislature. Thus, they have been more likely to push for some kind of "neutral" redistricting plan – as opposed to one drawn up by a Democratic Legislature. One of Governor Schwarzenegger's "Year of Reform" initiatives in 2005 sought to create redistricting by a panel of judges. For another example, see Robert T. Monagan, *The Disappearance of Representative Government: A California Solution* (Grass Valley, CA: Comstock Bonanza Press, 1990). Monagan was briefly Speaker of the Assembly during a short period of Republican control (1969-70).

¹⁵ Bird had no judicial experience prior to her appointment to the Court but had been California Secretary of Agriculture and Services. She was confirmed narrowly to the chief justice position by the voters in 1978. Bird had a reputation of a difficult personality and ran an erratic campaign against her own recall. After being removed from the court, she had trouble finding steady employment and became a rather forlorn figure until her death in 1999.

¹⁶ A detailed account of these events can be found in Preble Stolz, *Judging Judges: The Investigation of Rose Bird and the California Supreme Court* (New York: Free Press, 1981). See also Erin Adrian, "Rose Elizabeth Bird: Choosing to Be Just," unpublished paper (April 5, 2002), available at: <http://womenslegalhistory.stanford.edu/papers/RoseBird.pdf>

¹⁷ Paul Jacobs, "Governor Fires Back After a Scolding by Justice Bird," *Los Angeles Times*, March 22, 1986.

¹⁸ Press released dated August 25, 1986 available in California State Library, Rose Bird collection, box 1662 (folder 8).

¹⁹ Honig's account of his campaign and his subsequent clashes with Deukmejian can be found in Oral History Interview with Bill Honig, Superintendent of Public Instruction and Director, Department of Education, 1983-1993. California State Archives, State Government Oral History Program, Conducted 2000.

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- ²⁰ Honig was removed from office in 1993 during the Wilson era, convicted of four conflict of interest charges in connection with the operations of a consulting firm run by his wife. He blamed a vendetta carried out by people associated with Deukmejian for the investigation and conviction. *Ibid.*, pp. 126-128.
- ²¹ Prop 98 largely gutted Prop 4. There still is a Gann ceiling on revenue but revenues did not come near it until the dot-com boom. After the fact, it appears that revenues may actually have hit the revised ceiling at the top of the boom, but no action was taken at the time.
- ²² Quoted in Amy Chance, "Glow Off Duke Forecast; Budget Cuts Loom," *Sacramento Bee*, December 18, 1986.
- ²³ "Deukmejian Names Top Aides," *Los Angeles Times*, November 4, 1982.
- ²⁴ Douglas Shuit, "Deukmejian Will Face State Budget Deficit," *Los Angeles Times*, November 4, 1982.
- ²⁵ Wilson and Brown were running for the seat being vacated by Republican Sam Hayakawa.
- ²⁶ Douglas Shuit, "Deficit of \$1.1 Billion Projected for State; Rumors Confirmed," *Los Angeles Times*, November 11, 1982.
- ²⁷ Douglas Shuit, "Break Seen in Deadlock on State Budget," *Los Angeles Times*, November 19, 1982.
- ²⁸ Douglas Shuit, "Deukmejian Eases Off Opposition to Tax Hike," *Los Angeles Times*, November 20, 1982.
- ²⁹ Among the new Assembly members were Gray Davis, Jerry Brown's former chief of staff, and Tom Hayden, then married to actress Jane Fonda.
- ³⁰ Patrick Boyle, "Economy High on Deukmejian's List," *Los Angeles Times*, January 2, 1983.
- ³¹ Steve Merksamer, Deukmejian's chief of staff, commenting on the creation of the Big Five institution in Kevin Yamamura, "Governor Foregoes Budget Haggling," *Sacramento Bee*, June 27, 2007.
- ³² William Endicott and Claudia Luther, "'Buzz Word' in Inaugural Speech Proves Puzzling," *Los Angeles Times*, January 4, 1983.
- ³³ The word "tuition" will be used in this chapter as opposed to the "fee" euphemism.
- ³⁴ Readers who have followed accounts of the budget in *California Budget Options* will know that "revenue and transfers" is a slippery concept since some of the transfers are in fact borrowings from other state funds. As noted in the text, the origins of the final corrections of the reserve are not clear. However, these corrections always lead the reserve to be more positive (or less negative) than earlier estimates. So either more revenue is eventually being found or expenditures turn out to be less than initially estimated.
- ³⁵ Nancy Skelton, "Has Bradley's Chance Passed? 2nd Governor's Race Debated," *Los Angeles Times*, January 24, 1983.
- ³⁶ William Endicott, "Deukmejian Eases Opposition to Plan for State Lottery," *Los Angeles Times*, April 6, 1983.
- ³⁷ Douglas Shuit, "Unruh Riding High Again in State's Circle of Power," *Los Angeles Times*, March 20, 1983.
- ³⁸ See *Field Poll*, January 15, 2004, p. 3, available at www.field.com. The percent approving ratings were Schwarzenegger, 52%; Gray Davis, 58%; Pete Wilson, 52%; Deukmejian, 42%; Jerry Brown, 67%; Ronald Reagan, 58%; and Pat Brown, 51%.
- ³⁹ Eventually, court actions led to issuance of the checks.
- ⁴⁰ The initiative was named after Don Sebastiani, a Republican assemblyman (and member of the winemaking family), who pushed it.
- ⁴¹ Generally, Deukmejian was far more prone to veto bills than his predecessor or successor as governor. See Daniel Weintraub, *California Insider (Sacramento Bee)*, weblog, October 14, 2003.
- ⁴² William Endicott, "Deukmejian's Big Advantage was Surprise," *Los Angeles Times*, August 7, 1983.
- ⁴³ Robert Forsyth and Jeff Rabin, "State's Goal is Excellence, Duke Pledges," *Sacramento Bee*, January 9, 1985.
- ⁴⁴ Robert Forsyth and Jeff Rabin, "State's Goal is Excellence, Duke Pledges," *Sacramento Bee*, January 9, 1985.
- ⁴⁵ William Endicott, "Deukmejian's Legislative Style Viewed as 'Stubborn,'" *Los Angeles Times*, August 18, 1983.
- ⁴⁶ Douglas Shuit, "State Budget Surplus May Spark New Fiscal Conflict," *Los Angeles Times*, October 18, 1983.
- ⁴⁷ Jim Costa (Fresno) quoted in John Balzar, "Abundance Makes the Job Easier," *Los Angeles Times*, January 11, 1984.
- ⁴⁸ The "comparable worth" issue was prominent in the early 1980s, although unsuccessful as a legal doctrine. It initially involved a movement to use civil rights laws to make pay comparable in female occupations relative to male occupations, using various "job evaluation" techniques to compare the different occupations. Later unions in the public sector pushed for comparable worth pay increases even though these were not mandated by civil rights statutes.
- ⁴⁹ The anti-abortion provision was supposed to have been deleted from the Assembly-Senate compromise on the budget, but wasn't. The compromise South African language would have prevented new investments as of January 1, 1986.
- ⁵⁰ "Duke Vetoes More Than Necessary," *Sacramento Bee*, July 19, 1985.

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- ⁵¹ “Revenue Short of Goals,” *Sacramento Bee*, December 20, 1985.
- ⁵² Jeff Raimond, “State Heads to Wall Street With Plan to Borrow \$2.3 Billion – For Big Profit,” *Sacramento Bee*, July 26, 1985.
- ⁵³ Jeff Rabin, “Brown Beats Duke to Punch with ’86 Agenda,” *Sacramento Bee*, January 9, 1986.
- ⁵⁴ Jim Morris, “Bradley: Hungry for a Rematch,” *Sacramento Bee*, February 26, 1986.
- ⁵⁵ Laura Mecoy, “Duke’s Budget Challenge: Name Cuts or Raise Taxes, He Tells Critics,” *Sacramento Bee*, January 15, 1986.
- ⁵⁶ Gann and Jarvis originally pushed separate proposals but teamed up when their rivalry proved self-defeating.
- ⁵⁷ Jarvis was more bipartisan than Gann. When Governor Jerry Brown had a seeming conversion to the wisdom of Prop 13 after it passed, he ultimately received Jarvis’ support in his 1980 reelection. Then San Francisco Mayor Diane Feinstein asked for Jarvis’ support in 1980 regarding having the city relieved of certain bond payments related to the port. See Howard Jarvis collection, California State Library, box 1671 (folder 1), letter from Feinstein to Jarvis dated August 19, 1980.
- ⁵⁸ An explanation of the original Prop 4 and subsequent modifications can be found in Lisa Martin, “Exploring the Gann Limit,” *Cal-Tax Digest*, June 2000, available at www.caltax.org/documents/2000/jul00-9.htm. See also California Legislative Analyst’s Office, “The State Appropriations Limit,” available at www.lao.ca.gov/2000/041300_gann/041300_gann.pdf. According to former Legislative Analyst William G. Hamm, the actual text of the initiative was prepared by Gann by Vigo G. Nielsen, at the Republican-oriented law firm of Nielsen, Merksamer, Hodgson, Parinello & Mueller. See Oral History Interview with William G. Hamm, California Legislative Analyst, 1977-1986. California State Archives, State Government Oral History Program, Conducted 1989, p. 48.
- ⁵⁹ In contrast, a 1980 proposition cutting the state income tax pushed by Jarvis (“Jarvis II” or Proposition 9) did not pass, receiving 39% of the vote.
- ⁶⁰ For example, Tom McClintock who has emphasized tight budgets and low taxes throughout his legislative career asked for – and received – Gann’s endorsement in his first race for the Assembly in 1982. See letter from McClintock to Gann asking for endorsement and Gann’s response providing the endorsement in Paul Gann collection, California State Library, box 1392 (folder 5), letter from McClintock to Gann dated July 19, 1982, and box 1393 (folder 3), letter from Gann to McClintock dated August 2, 1982.
- ⁶¹ Gann – with Republican Assemblywoman Doris Allen - later became involved in trying to put a proposition on the ballot to earmark gasoline taxes for roads. The initiative did not end up on the ballot, however. See “Tax Hike Seen in ’89 With Duke’s Road Plan,” *Sacramento Bee*, January 13, 1987. Allen later had a brief, semi-comedic career as Assembly Speaker with Willie Brown still the power-behind-the-throne under Pete Wilson. See last year’s budget chapter for details.
- ⁶² Oral History Interview with William G. Hamm, California Legislative Analyst, 1977-1986. California State Archives, State Government Oral History Program, Conducted 1989, p. 49.
- ⁶³ Daniel J.B. Mitchell, *Pensions, Politics, and the Elderly: Historic Social Movements and Their Lessons for Our Aging Society* (Armonk, NY: M.E. Sharpe, 2000).
- ⁶⁴ Thorne Gray, “Duke’s Budget Tops Spending Limit, Analyst Says,” *Sacramento Bee*, January 28, 1986.
- ⁶⁵ Hamm was related by marriage to A. Alan Post, his predecessor as Legislative Analyst who held the job from 1949 to 1977. (Post’s sister-in-law was Hamm’s mother.) Thorne Gray, “Legislative Analyst Expected to Quit Job,” *Sacramento Bee*, February 28, 1986. Hamm was succeeded, after a selection process, by Elizabeth Hill, the current Analyst.
- ⁶⁶ Dan Walters, “Duke on Gann: Leave It Alone,” *Sacramento Bee*, June 15, 1986.
- ⁶⁷ “Deukmejian and Gann,” *Sacramento Bee*, July 20, 1986.
- ⁶⁸ Laura Mecoy, “Dukes Close Eye on Two Justices: Votes for Death Penalty Could Help Him Back Reynoso, Grodin,” *Sacramento Bee*, March 14, 1986.
- ⁶⁹ “Budget Forecast,” *Sacramento Bee*, March 27, 1986.
- ⁷⁰ Thorne Gray, “School Workers Protest Pension Fund ‘Raid,’” *Sacramento Bee*, August 7, 1986.
- ⁷¹ Rick Rodriguez, “Curb at Odds with Duke, Almost,” *Sacramento Bee*, September 3, 1986. Mike Curb was trying to regain the Lieutenant Governorship, having lost it in 1982 to Democrat Leo McCarthy.
- ⁷² In a subsequent interview, Deukmejian attributed his change of mind to sensitivities resulting from his Armenian heritage. Interview in “The University of California Office of the President and Its Constituencies, 1983-1995,” Volume III (Regents and State Officials), pp. 128-129. (Available from the California Digital Library.
- ⁷³ Laura Mecoy, “Duke: Bird Repeatedly ‘Ruled Against the People,’” *Sacramento Bee*, June 6, 1986.
- ⁷⁴ Jeff Rabin, “Bradley Would Hike Taxes, Duke Warns,” *Sacramento Bee*, October 4, 1986.

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- ⁷⁵ “Honig Seeks More Funds to Push School Reforms,” *Sacramento Bee*, January 2, 1987.
- ⁷⁶ Thorne Gray, “State May Slam into Budget Ceiling,” *Sacramento Bee*, November 26, 1986.
- ⁷⁷ Thorne Gray, “Analyst Says State May Outspend Gann Limit,” *Sacramento Bee*, December 4, 1986.
- ⁷⁸ “Honig Seeks More Funds to Push School Reforms,” *Sacramento Bee*, January 3, 1987.
- ⁷⁹ “Democrats Poke Holes in Governor’s Plans,” *Sacramento Bee*, January 8, 1987.
- ⁸⁰ “Duke’s Budget Surplus is a Big Cheat, Brown Charges,” *Sacramento Bee*, February 4, 1987.
- ⁸¹ The federal Occupational Safety and Health Act provides for states to substitute their own enforcement mechanisms so long as the standards are at least as strict as the federal minimums. If a state has no agency of its own, the federal standards are enforced by federal OSHA.
- ⁸² Although Cal-OSHA was operating under federal OSHA, it had a much earlier history pursuant to a state constitutional amendment of 1917. Since the Democrats would not eliminate Cal-OSHA from the 1987-88 budget, the governor – once the budget was passed – eliminated funding for the agency. A court decision in October 1988 went against the governor but an appeal kept the state agency closed for fiscal 1987-88.
- ⁸³ “Honig Arises, Battles Duke,” *Sacramento Bee*, January 15, 1987.
- ⁸⁴ “UC President Favors Review of Gann Limit, No Yes-Or-No Stand on Spending Limit,” *Sacramento Bee*, January 17, 1987.
- ⁸⁵ Texas eventually won the Super Collider which was then partially built and abandoned as the cost mushroomed.
- ⁸⁶ “Brown: Duke Will Back Off, Speaker Predicts More School Funds,” *Sacramento Bee*, April 3, 1987.
- ⁸⁷ “State Surplus: Is it Obscene?,” *Sacramento Bee*, May 8, 1987.
- ⁸⁸ “Duke Seeks \$700 Million Tax Rebate,” *Sacramento Bee*, May 20, 1987.
- ⁸⁹ As the debate heated up, Paul Gann announced he had received a diagnosis of AIDs, which he attributed to a blood transfusion. He died of complications from AIDs in 1989. The Paul Gann Act of 1990 regulates blood safety in California.
- ⁹⁰ “Let Taxpayers Decide Rebate, Duke Says,” *Sacramento Bee*, June 21, 1987.
- ⁹¹ “Demos Find Nothing Good to Say About Budget Cuts,” *Sacramento Bee*, July 8, 1987.
- ⁹² “Governor’s Overture to Honig,” *Sacramento Bee*, August 28, 1987.
- ⁹³ “Lawmakers’ Big Session, Major Actions Counter Tarnished Image,” *Sacramento Bee*, September 13, 1987.
- ⁹⁴ “Majority Would Spend Surplus on Schools,” *Sacramento Bee*, August 25, 1987.
- ⁹⁵ Richard A. Clucas, *The Speaker’s Electoral Connection: Willie Brown and the California Assembly* (Berkeley, CA: Institute of Government Studies Press, 1995), p. 143.
- ⁹⁶ “Legislature Closes Out Its Troubled Year,” *Sacramento Bee*, September 2, 1988.
- ⁹⁷ A third blow was the rejection by the California Supreme Court of the governor’s attempt to appoint a new Treasurer to replace Jesse Unruh who died in office. The Court contained the new justices appointed by the governor after Rose Bird and two colleagues were ousted.
- ⁹⁸ The governor opposed both Props 71 and 72.
- ⁹⁹ Republicans, as a minority, could not elect one of their own members as speaker. And they saw a plus in having Willie Brown remain as speaker – rather than some other Democrat – since he was in their eyes a figure to campaign against in future efforts to regain control of the Assembly. See “Brown Survives Ouster Try, 2nd Bid in 5 Days Fails,” *Sacramento Bee*, May 10, 1988.
- ¹⁰⁰ “UC Joins the Club,” *Sacramento Bee*, July 20, 1988.
- ¹⁰¹ “Proposition 98 Would Insulate Schools from Budget Cuts,” *Sacramento Bee*, October 8, 1988.
- ¹⁰² Ibid.
- ¹⁰³ “Deukmejian’s Complaint,” *Sacramento Bee*, November 11, 1988.
- ¹⁰⁴ “Support Declines for Props. 95, 97, 98, 99,” *Sacramento Bee*, October 26, 1988.
- ¹⁰⁵ Voters also raised the cigarette tax to fund certain health and other programs. Taxes collected were exempted from Gann.
- ¹⁰⁶ “Warning on Deficit After Duke Study Indicates ’91 May Be Red Ink Year,” *Sacramento Bee*, February 10, 1989.
- ¹⁰⁷ “Fiscal Estimates Irk Duke, Warns of Spending Vetoes in Face of Varied Deficit Totals,” *Sacramento Bee*, February 16, 1989.
- ¹⁰⁸ David G. Hensley, “California Has Arrived at a Watershed” in *The UCLA Business Forecast for California: December 1990* (Los Angeles: UCLA Anderson Graduate School of Management, 1990), p. 1.
- ¹⁰⁹ David G. Hensley, “Downturn Intensifies, California Is In Recession” in *The UCLA Business Forecast for California: December 1991* (Los Angeles: UCLA Anderson Graduate School of Management, 1991), p. 1.
- ¹¹⁰ “Deukmejian’s Key Political Asset,” *Sacramento Bee*, September 17, 1989.

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- ¹¹¹ “State Puts Off Selling of \$4 Billion in Bonds, Can’t Afford Repayment on Principal, Interest,” *Sacramento Bee*, January 24, 1989.
- ¹¹² “Capitol Saved from Disgrace,” *Sacramento Bee*, July 2, 1989.
- ¹¹³ The split-roll proposal was the product of an organization called Voters Revolt, which had successfully campaigned for the earlier Prop 103 which regulated the insurance industry. “Deflating the New Populism,” *Sacramento Bee*, December 19, 1989.
- ¹¹⁴ “Governor Calls for Tough Cuts,” *Sacramento Bee*, January 11, 1990.
- ¹¹⁵ “Governor’s Tough Talk on Budget,” *Sacramento Bee*, May 1, 1990.
- ¹¹⁶ California Task Force to Promote Self-esteem and Personal Social Responsibility, *Toward a State of Self Esteem* (Sacramento: Office of State Printing, 1990).
- ¹¹⁷ “New State Budget Means Cuts in Services, Analyst Says,” *Sacramento Bee*, February 22, 1990.
- ¹¹⁸ Jerry Roberts, *Diane Feinstein: Never Let Them See You Cry* (New York: HarperCollinsWest, 1994), pp. 240-255.
- ¹¹⁹ *Ibid.*
- ¹²⁰ “Duke Freezes State Spending, Order Goes Into Effect Immediately to Reduce Flow of Red Ink,” *Sacramento Bee*, May 11, 1990.
- ¹²¹ A.G. Block, “What Us Worry? Budget Deadlock Takes the State to the Brink,” *California Journal*, September 1, 1990.
- ¹²² “Dimmer View of Deukmejian,” *Sacramento Bee*, September 3, 1990.
- ¹²³ “Wilson Says Maybe on Taxes, Feinstein Opposes Shifting State Funds Away from Education,” *Sacramento Bee*, September 5, 1990.
- ¹²⁴ In the 2002, election Deukmejian supported the campaign of Secretary of State Bill Jones for the Republican nomination for governor, and pointedly opposed the candidacy – ultimately unsuccessful – of former L.A. Mayor Richard Riordan. He remained active in various Armenian causes
- ¹²⁵ “Budget Shortfall Soaring, Wilson Could Inherit Up to \$10 Billion Deficit,” *Sacramento Bee*, December 28, 1990.
- ¹²⁶ Kevin Yamamura, “An Expansive Agenda: Governor Urges New Initiatives on Public Works, Environment, Health Care for the Uninsured,” *Sacramento Bee*, January 10, 2007.
- ¹²⁷ Chart 2 is based on cash statements of the state controller rather than the methodology used by the Department of Finance and the Legislative Analyst to represent the budget. In addition, various adjustments have been made to the figures in the cash reports to make the data more meaningful for analytical purposes. These adjustments are listed in the notes to the chart.
- ¹²⁸ The individual mandate approach requires all Californians to have health insurance, either individually acquired or through some other arrangement such as an employer. Pay-or-play requires employers either to provide insurance or to pay into a state fund to provide it. Also on the table was a single-payer proposal, a state-run insurance fund that would replace private insurers, a plan the governor has vetoed in the past and would likely veto again.
- ¹²⁹ The Assembly Speaker endorsed the compacts to the chagrin of his traditional allies in organized labor. Reportedly, gaming interests threatened to campaign against the term limits initiative if he did not support the compacts.
- ¹³⁰ Kevin Yamamura, “Governor Foregoes Budget Hagglng,” *Sacramento Bee*, June 27, 2007.
- ¹³¹ John Hill, “Governor Tries to Apply Pressure to GOP Senators, Citing Payment Snags,” *Sacramento Bee*, August 3, 2007.
- ¹³² Senator Abel Maldonado who occupies a vulnerable district was the one Republican defector.
- ¹³³ *State of California ex rel. Pension Obligation Bond Committee v. All Persons Interested in the Matter of the Validity of the California Pension Obligation Bonds to be Issued*, Super. Ct. No. 04AS04303, July 3, 2007.
- ¹³⁴ George Skelton, “A Simple-Majority Vote Would End the Madness on Passing State Budget,” *Los Angeles Times*, August 20, 2007.
- ¹³⁵ There was debate over whether the deal in fact resulted in the legal constraints the Republicans were seeking. See Steven Maviglio, “Senate Republicans Snookered on Global Warming Budget Deal,” *California Majority Report*, August 21, 2007. (On-line Republican-oriented newsletter.)
- ¹³⁶ Judy Lin, “Battle Looms on List of Cuts,” *Sacramento Bee*, May 15, 2007.