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From the Los Angeles Times

## Schwarzenegger calls back legislators for emergency budget session

With California's revenue plummeting, the governor says lawmakers will reconvene next week. They will discuss solutions to the foreclosure crisis and an economic stimulus package.

By Evan Halper

October 28, 2008

Reporting from Sacramento — Gov. Arnold Schwarzenegger has set Nov. 5 -- the day after next week's election -- as the start of an emergency legislative session to address the state budget deficit, which has swelled by several billion dollars in recent weeks as the stock market has continued its tumble and the economy has soured.

Schwarzenegger said this year's deficit will be "much more" than the \$3 billion that state officials projected two weeks ago. Capitol budget analysts say preliminary data indicate the problem will probably grow to at least \$10 billion.

The governor and legislative leaders made the announcement to reporters in the hallway outside Schwarzenegger's office, where they had been meeting in private to discuss the fiscal crisis. They said that in the coming days they also will form a commission to study ways to restructure the state tax code to make revenue more stable.

Schwarzenegger's move comes a month after lawmakers passed the current budget and adjourned until December, when the next class of lawmakers is scheduled to begin work. But the governor said state revenues are dropping so fast that he and legislative leaders decided to call a lame-duck session.

"The situation is far more severe than it was when we were negotiating the budget" over the summer, Schwarzenegger said.

At that time, experts had warned that the spending plan lawmakers were drafting was optimistic.

"They ignored the obvious," said Christopher Thornberg, principal at Beacon Economics. "They refused to recognize we were heading into this painful recession. It wasn't rocket science."

The state's problems are being compounded by the stock market bust. State revenues are expected to suffer substantially as a result of the carnage on Wall Street.

Relative to other states, California gets a disproportionate share of its revenue from the personal income taxes of the wealthy. The richest 1% of Californians pay half of all the personal income taxes the state collects each year.

"A lot of those folks receive much of their income from capital gains," said H.D. Palmer, deputy director of external affairs for the state Department of Finance.

When the stock market falters and capital gains fall off, state income plummets. This month the Standard and Poor's 500 Index has dropped 24%.

The state also relies heavily on sales taxes. Economists are predicting that those receipts will also take a dive as consumers tighten their belts.

The governor said he opted to bring sitting lawmakers back to town rather than wait for the new class because "they have dealt with the problem throughout the year." Some analysts have suggested that the governor stands a better chance of pushing through a temporary tax hike -- something he tried but failed to do during the summer -- with the current crop of lawmakers, because several are termed out of office and will not be part of a newly elected Legislature.

Republican leaders say their caucuses will continue to block any tax increase as they did in summer. They handed the governor a letter Monday calling for tax cuts.

The legislators proposed new tax breaks for a range of companies, including those involved in manufacturing, building new facilities in California and hiring out-of-work Californians.

"California has one of the highest tax rates on business in the nation," wrote Assembly Republican Leader Mike Villines of Clovis and Senate Republican Leader Dave Cogdill of Modesto. "With the tight credit market and worldwide economic turmoil, we must help California businesses to create, retain and expand job opportunities."

Legislators will no doubt be forced to weigh steep program cuts as part of the special session. The estimated shortfall already has grown so large -- \$10 billion is nearly 10% of the general fund -- that even the sales tax hike the governor proposed earlier in the year would erase only a fraction of it.

In their special session, lawmakers will also consider proposals to deal with the state's foreclosure crisis, and an economic stimulus package designed to create more jobs in the state. One way to do that, legislative leaders and the governor said, would be to speed up allocation of public-works bond money already approved by voters. They are also seeking billions of dollars in relief from Washington, D.C., some of which could take the form of extended unemployment benefits for Californians out of work.

The top-to-bottom review of the state's tax code was initially proposed by Assembly Speaker Karen Bass (D-Los Angeles).

"California's tax structure was set up at the beginning of the last century," Bass said. "We know it needs to be modernized."

Several previous attempts to overhaul the tax code have been rejected. Experts say lawmakers easily find taxes to cut but can rarely agree on how to replace the lost revenue.

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