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HEADLINE: What Us Worry? Budget Deadlock Takes State to the Brink.

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HIGHLIGHT:

A stubborn lame-duck governor and an Assembly in disarray caused the Legislature to pass the budget 43 days late.

BODY:

They took the deadlock over a state budget to the brink -- to the 11th hour, 59th minute, 59th second. They yammered and bellowed and stamped their feet and held their breaths until they turned blue, these politicians who sit as governor and legislators. Along the way, they skewed what could have been substantive debate into surreal posturing. And finally, nearly a month late, they produced a patched-together, \$55 billion budget that postponed the crunch rather than dealt with it.

Not that the problem was easy to solve. In fact, the five budget negotiators -- Governor George Deukmejian, Senate Democratic leader David Roberti, Senate Republican leader Ken Maddy, Assembly Speaker Willie Brown Jr. and Assembly Minority Leader Ross Johnson -- faced two problems: an immediate \$3.6 billion deficit in the 1990-91 budget; and permanent budget structures that mandate state-financed services for ever-increasing numbers of people regardless of how much revenue the state has to spend.

From day one, the solution to the most pressing problem -- the deficit -- was obvious to everyone: some combination of spending cuts and additional revenue to spread the pain equitably.

And yet the deadlock dragged on for six weeks, exacerbated by two factors.

First, the fact that the budget bill needed a two-thirds majority in each house of the Legislature gave a small band of Assembly Republicans the chance to cripple the entire process. Second, and most important, Deukmejian insisted on tackling the most complex dilemma -- the budget's permanent structure -- as a prerequisite to fixing the deficit.

Thus, the budget deadlock turned on a fundamental question: Will government generate revenues to pay for programs, or spend on programs according to the revenue on hand?

The governor, supported by Assembly Republicans, took the latter view. He wanted the Legislature to grant him what he called "structural reforms" -- permanent, procedural tools that would allow him to cut all spending according to his own set of priorities. Republicans saw this as protecting their natural constituencies: basically, those who have bulky tax bills, like upper- and middle-income taxpayers, businesses and corporations. On the other hand, the Democrats who control the Legislature were loathe to cede to Deukmejian -- or to any governor -- that kind of power. They wanted to protect their constituencies -- for instance, labor and the poor and elderly -- who are helped by laws established over the years to guarantee spending levels for entitlement programs, especially in health and welfare and in education.

In a sense, Deukmejian's point on structural reform was well taken; constraints placed on budgeting by a myriad of state and federal laws hamper government's ability to adequately meet fiscal emergencies and to shift resources among various programs to address the needs of a dynamic and changing state.

"We wanted structural reforms that would bring expenditures more into line with revenues," explained Michael Frost, Deukmejian's chief of staff. "We need to get the state off automatic-pilot growth that is unrelated to our ability to pay for it."

But Deukmejian, who leaves office in January, ignored a basic political reality when he insisted on sweeping changes that would shift purse-string power from the Legislature to the governor: No Democratic-controlled Legislature was about to bestow that kind of control on a lame-duck Republican.

Yet Deukmejian insisted on those structural reforms and, in so doing, prolonged the budget deadlock. He waited for the other side to cave in -- Democrats always do the responsible thing and cave in; after all, it is their constituents who are waiting for the delayed state checks -- and he waited and he waited, long past the time when evidence indicated that the other side would not cave in; right up to the brink of fiscal disaster for the state. In the end, Deukmejian caved in on his main reform priority -- the suspension of laws guaranteeing a certain percent of the budget for education (Proposition 98) -- accepting instead a modest reform and agreeing to a compromise over spending cuts and revenue enhancements that could have been reached at the beginning of June.

The symbolic battleground for the squabble between Deukmejian and the Legislature became Proposition 98 -- the successful 1988 initiative that altered the budget structure to guarantee a sizable chunk of the state's general fund for K-14 education (kindergarten through community college). Deukmejian had opposed Proposition 98, considering it bad law to lock up so large a share of the state budget for any purpose. But his view of the measure was further skewed by the fact that one of its main political beneficiaries was Superintendent of Public Instruction Bill Honig -- Deukmejian's number-one political bogeyman whose whining public criticisms of Deukmejian over the years more often than not threw gasoline on a smoldering relationship.

Based on Proposition 98, K-14's share of the general fund is determined in one of two ways. The administration recommended what it called "test one:" a flat 41 percent. Assembly Democrats, backed by the education establishment and with help from dissident Assembly Republicans, wanted "test two:" full funding for Proposition 98 based on the previous year's budget allocation, plus increases for cost-of-living and inflation. The initiative calls for the higher of the two amounts but also allows the Legislature to waive the full-funding provision in a fiscal emergency. The difference between the two versions amounted to between \$700 million and \$800 million dollars.

"During June and July," said a source close to the budget negotiations, "however we approached the revenue issue or the reduction issue -- one-time revenue stuff for reserves, or transfers of revenue to counties to backfill the reductions -- there was never closure within \$600 to \$800 million on the deficit because that was always the amount ... that was the supposition of (waiving Proposition 98)."

And it was this final \$700 to \$800 million gap that provided the key to the deadlock. Deukmejian wanted to close it by waiving Proposition 98; Democrats wanted to make up the difference with a few more cuts, a few more fee increases, and some budgetary hocus-pocus.

Complicating the squabble was the behavior of Assembly Republicans. In June a group of Republicans, led by Tom McClintock, held a press conference that essentially torpedoed the governor's strategy for Proposition 98. During that press conference, McClintock and the others vowed to protect Proposition 98 -- all of it. No waiver, period.

It has been suggested that the Republicans took this stand on political grounds, to drive a wedge between Assembly Democrats and one of their most consistent and wealthiest allies -- the powerful California Teachers Association.

"They wanted to go out there and look like heroes because they were all for education," said a source close to the negotiations. "They (the Republicans) figured that if they held absolutely tough on the amount of revenue increases they were willing to accept, and absolutely tough on protecting Proposition 98, Democrats simply couldn't balance the budget without suspending Proposition 98. Democrats would be the bad guys by putting 98 on the table because they couldn't take the extreme cuts in other programs. They (Republicans) thought Democrats would blink, and this would break the political connection between Democrats and the CTA."

The strategy backfired, however, for about the same time Assembly Democrats were reaching the conclusion that they, too, would stand solid behind Proposition 98. Not that all Democrats were sold on the measure; privately, many of them agreed with Deukmejian that it was bad law. Unfortunately, it was operative law, and many school districts throughout the state had made contractual salary commitments, especially to teacher unions, based on a certain level of Proposition 98 funding.

"The reality of suspending 98 meant a \$800 million cut for education, and the reality was that a lot of teacher contracts had already been signed," said Democratic Assemblyman

Richard Katz of Los Angeles. "Given those contracts, if we were to reduce the amount to education, the money had to come from somewhere, and the somewhere was other cuts in education. This meant larger class sizes or fewer textbooks and other materials. Given these realities, the impacts in the classroom would have been severe."

Too severe for Democrats to stomach. Thus, when the CTA approached them in the wake of the Republican news conference, and asked for a similar commitment to protecting all of Proposition 98 funding, Democrats agreed.

Proposition 98 was, as they say, "off the table."

Yet Deukmejian continued to hold out, getting what Chief of Staff Frost said were "mixed signals" from various factions in the Legislature over whether the political will existed to waive Proposition 98. Thus, as the deadlock dragged on through a sweltering July, the governor sat on his hands, offering no more solutions, content to let a hopelessly befuddled Legislature wrangle and grope in circles, holding the process hostage to his desire to suspend Proposition 98.

Meanwhile, the budget debate dissolved into political theater. The state missed a payroll, allowing thousands of state workers to go unpaid, sending some of them to charities for free food. A \$598 million payment to counties, cities and Medi-Cal providers was missed. Counties, in turn, did not issue checks to families dependent on welfare, while some directors of programs for the mentally disabled took out bank loans to keep their doors open. The Department of General Services froze all state purchases, sending a ripple throughout the entire economy. The courts intervened piecemeal when various judges began ordering the state to pay up so that counties could issue welfare checks.

There was some movement on July 10th when the state Senate, coaxed along by Maddy and Roberti, passed a compromise budget that included \$1.7 billion in cuts and \$1.3 billion in increased revenues. The Senate version, however, still left nearly \$600 million for Deukmejian to axe to bring it into balance. The Senate passed its budget, then left town, with even its architects agreeing that it was not an end-all, be-all, but a document for the Assembly to negotiate over.

But the Senate document was burned before the ink dried. Deukmejian didn't like it because it gave him no reforms while adding more revenues. Moreover, the effort was pronounced dead-on-arrival in the Assembly, with Republican Bill Baker calling it "dog doo" because of the increased fees and taxes. Democrats didn't like many of the cuts, and didn't like the fact that Deukmejian's blue pencil would still have to slash \$600 million.

And the deadlock continued. A few members -- Assembly Democrats, mostly -- worked at ideas, at solutions, at compromise. Others -- notably, Assembly Republicans -- fomented chaos, playing "air raid" with any proposal; shooting first, asking questions never, and controlling enough votes to prevent the 54-vote majority needed to pass a budget. They were emboldened by Deukmejian's continued insistence on structural reform.

Under the best of circumstances, a \$3.6 billion deficit would be difficult to fix without what The Sacramento Bee called a "book of pain." It would require the governor to work closely

with Republicans and Democrats in both the Senate and Assembly to craft a solution that spread the pain around, but also one that accommodated political realities. It would require the application of a standard of reason acceptable to a wide variety of interests.

But 1990 was far from the best of circumstances. A lame-duck governor was displaying his well-known stubborn streak. The Senate passed a flawed budget and left town. And the Assembly lurched out of control, fractured into so many pieces that a small group of ideologues could practically paralyze attempts to patch together 54 votes. One entire caucus -- the Republicans -- was rudderless, with no effective leader to coax its various factions toward an acceptable solution.

Thus, the process evolved into a surrealistic Tower of Babel where everything was familiar but nothing was as it should have been; rather like athletes playing football on a baseball diamond. Libertarianish Republicans vowed to protect every nickel of education money mandated by a law (Proposition 98) they loathed, while proposing to make up the difference by privatizing everything from prisons to street lighting. The governor and other Republicans proposed solving the deficit solely with program cuts, a suggestion so draconian that some observers warned it might require shutting down one or two UC campuses. Conservative Assembly Republicans tried to hold up the budget at the 11th hour over what they said were unacceptable cuts in mental-health programs. Democrats conceded, early in the process and without a fight, suspension of cost-of-living adjustments (COLAS) for the poor and elderly. And they, too, publicly went to the mats to protect Proposition 98 while privately lamenting that the law existed in the first place.

Finally, on July 25th, Deukmejian resurfaced, having held out to the last gasp for suspension of Proposition 98. He had received word from the East Coast bond raters that failure to adopt a budget would soon put the state's triple-A bond rating in jeopardy. The governor called another "leadership meeting" with Roberti, Maddy, Brown and Johnson. And when that meeting convened, Deukmejian conceded defeat on Proposition 98. A combination of budget cuts and fee and tax increases was patched together with some deferred payments -- all carried in 18 trailer bills -- and a budget was proposed to each house of the Legislature that bore a the stamp of approval from leadership and from the governor (see box, page 424).

Finally, Democrats gave in on a modest budgetary reform -- a so-called "trigger mechanism" that would reduce most state general-fund programs 4 percent across the board when the governor's projected budget indicates a revenue shortfall of one-half percent. It would not affect K-14 education, debt service or the homeowner's exemption because they are protected by the state constitution. Had the trigger been in place for the current year, it would have axed \$210 million from the budget up-front. The governor considered the trigger a major reform because it gives him the ability to make blue-pencil reductions in welfare COLAs, something he could not do without the trigger.

Ultimately, Deukmejian returned to the negotiations because the administration finally realized that it did not have the political clout to suspend Proposition 98. Why did it take so long? Michael Frost, Deukmejian's chief of staff, said that the administration sensed that both Assembly caucuses were split on the issue of waiving Proposition 98, and that

eventually they would come around to the governor's view. He argued that the initiative itself calls for waiver in a fiscal emergency.

"If this wasn't a financial emergency, I don't know what is," said Frost.

Even after leadership agreed to a budget proposal, all was not peaceful in Oz. The Senate quickly adopted the plan and the trailer bills, although there was some notable squabbling over a Deukmejian bill to fund construction of a prison in East Los Angeles. The Assembly, however, broke down once again. Liberal Democrats considered the program cuts too deep, while conservative Republicans thought the revenue increases too lavish. Between the two extremes, there was enough dissatisfaction to prevent a 54-vote majority. Republicans also grumped about more substantive structural reforms, calling the trigger mechanism a sham.

In the end, it came down to leadership: The Democratic caucus had some; the Republican caucus did not. Democratic Speaker Willie Brown and his lieutenants -- Katz, Speaker pro Tem Mike Roos, Majority Leader Tom Hannigan, Phil Isenberg and others -- brought the caucus in for the budget, albeit kicking and screaming. But Republican leader Ross Johnson seemed to lose control of his membership, with enough of them voting "no" or not voting at all to deny the budget 54 votes. Ultra-conservative Tom McClintock summed up the view of many when called the proposal a "chewing-gum and baling-wire budget" put together with "happy thoughts and pixie dust."

Thus, when the Assembly finally took up the budget on Friday evening, July 27th, it received only 47 votes on the first go-around. Many of the trailer bills also failed to pass. The situation was further complicated by the absence of eight members, including five Democrats: Sam Farr, Tom Bane, Jerry Eaves, Willard Murray and Elihu Harris. The three missing Republicans were Robert Frazee, Sunny Mojonier and John Lewis. (One Democrat who was present was Sal Cannella of Modesto, who that morning had undergone gallbladder surgery and left a hospital bed to cast a critical vote on the budget.)

Finally, after subsequent unsuccessful votes, as debate meandered into the wee hours of July 28th, and with the budget one vote short, Speaker Brown dispatched a car to Oakland to bring ailing Democrat Elihu Harris out of a sickbed to cast the deciding tally. Before the car arrived in Oakland, however, the speaker managed to shame two Republicans -- Pat Nolan and Paul Woodruff -- into changing from "not voting" to "aye" in order to pass the budget.

A dogfight continued later that afternoon over the trailer bills but eventually they, too, passed, and passed the Senate, and were sent on to the governor, who made \$753 million in additional cuts. On August 1st, California had a 1990-91 budget.

In the wake of any political brawl, it is common to assess winners and losers. But there may be no winners here. Governor Deukmejian is considered a loser because he caved in on Proposition 98 and because he agreed to tax and fee increases that he had vowed to avoid. And because after eight years as a fiscal watchdog, he leaves his successor with as much of a budgetary mess as he inherited from Jerry Brown in 1983. But much of that mess is beyond his control.

And on the issue of structural reform, he was right -- the budget is hamstrung by too many laws, Proposition 98 among them, that mandate money to special interests and at levels that are often not in tune with how much the state has to spend.

The state Senate, led by Maddy and Roberti, emerged with its reputation for deliberate and reasonable debate intact. It, at least, made some attempt to pass a compromise budget on time. In fact, its budget, although flawed, laid the groundwork for the final compromise.

Assembly Democrats behaved like Assembly Democrats. They engaged in long, arduous, often rancorous debates over budget proposals. Ways and Means Chairman John Vasconcellos, for one, released publicly a letter to Deukmejian telling how proposed budget cuts had reduced him to tears on a ride home from the Capitol. In the end, he was cut out of the process in favor of more practical Democrats, despite the fact that his name was on the budget bill itself. But at least Democrats produced budget proposals, including the final compromise. They were engaged in trying to solve the problem.

And then there are the Assembly Republicans. They came away from this budget ordeal as buffoons, the Keystone Kops of California government. From the start, they assumed the role of nay-sayers; their strategy was not to have a strategy. They never produced a budget proposal, or even any compromise solutions but remained content to wait for Democratic proposals at which they then threw supposedly slashing rhetoric. This lack of action, coupled with a lack of substantive proposals, revealed a caucus verging on political and intellectual bankruptcy. They were accorded power in this fight only as long as Deukmejian held out for Proposition 98 suspension. Once the governor gave up the fight and agreed to a compromise, the Assembly Republicans became politically isolated and irrelevant.

Repeated attempts were made to contact Assemblyman Ross Johnson for the Republican view, but Johnson did not return Journal calls.

The biggest loser, however, may have been government itself, and the notion that conflicts in government can be resolved by reasonable men and women engaged in substantive debate over alternatives. Reasonable and substantive debate was seldom heard during these budget negotiations.

And what about that fundamental question: Will government generate revenues to pay for programs, or spend on programs according to the revenue on hand? No one answered it; few even addressed it. Thus, it becomes a legacy for the next governor and the next Legislature.

The budget deal

The compromise deal hammered out by Governor George Deukmejian and legislative leaders at the end of July included:

\$741 million in new tax revenues (conforming California law with federal law, \$561 million; withholding provisions for capital gains on real estate deals involving out-of-state buyers

and sellers, \$43 million; accelerating state collection of unclaimed bank accounts, \$137 million);

\$102 million in fee increases (out-of-state vehicles, \$50 million; state parks, \$16 million; UC/CSU, \$13 million; pesticide mill tax, \$9 million; other, \$14 million);

\$1.32 billion in cuts (suspension of cost-of-living increases for welfare, the elderly, the disabled, Medi-Cal and home-support services, long-term-care facilities, \$329 million; GAIN workfare program, \$101 million; UC/CSU, \$109 million; local government reductions, \$223 million; local health programs for the poor, \$175 million; renters tax for couples, \$52 million; corrections, \$41 million; Medi-Cal reforms, \$107 million; local trial court funding, \$61 million; other, \$121 million);

\$987 million in program delays and funding shifts (recalculation and reallocation of contributions to teachers' retirement fund, \$447 million; same for public employees' retirement fund, \$245 million; other transfers and delays, \$265 million).

The 1990-91 budget Total: \$55.7 billion (\$42 billion, general fund)

Revenues:

Personal income taxes -- \$18.7 billion
Sales taxes -- \$14.5 billion
Special sales taxes -- \$600 million
Bank and corporation taxes -- \$5.9 billion
Highway user taxes -- \$3.5 billion
Insurance taxes -- \$1.3 billion
Cigarette taxes -- \$148 million
Proposition 99 cigarette taxes -- \$615 million
Other, general fund -- \$2.3 billion
Other, special fund -- \$1.7 billion

Expenditures (general fund, total):

K-14 education -- \$17.8 billion, \$19.6 billion
Health and Welfare -- \$13.2 billion, \$14 billion
Higher education -- \$4.4 billion, \$4.7 billion
Local government subventions -- 0, \$2.9 billion
Business, transportation, housing -- \$116 million, \$4.2 billion
Corrections -- \$2.8 billion, \$3.5 billion
Resources -- \$700 million, \$2 billion
State and consumer services -- \$300 million, \$600 million
Other -- \$1.9 billion, \$2.3 billion

Source: Department of Finance