April Income Tax Revenues Short Almost $2.0 Billion

Yesterday, May 1, 2012, the State Controller's Office reported that the April 2012 income tax revenues came in $1.961 billion short of the January Budget estimate, a whopping 21% below the budgeted level of $9.132 billion. Coupled with the shortfall through March, this deficiency puts General Fund revenues almost $3.0 billion behind the Budget projection for the current year. With two months remaining in the 2011-12 fiscal year, revenue collections could fall short an additional $1.0 billion to $2.0 billion, especially since June is one of the biggest revenue months.

Recall that before passing the 2011-12 Budget, the Legislature added $4.0 billion to the Department of Finance's (DOF's) revenue forecast and included midyear trigger reduction language to avoid enacting greater cuts in June. By December 2011, the DOF projected a $2.2 billion shortfall, triggering the midyear apportionment reductions and the summer fee increase. With this latest information on April revenues, it appears that the state will not only fail to realize any of the $4.0 billion added by the Legislature, but will likely fall short of the original DOF forecast by $1.0 billion to $2.0 billion.

This current-year shortfall has significant implications for the 2012-13 Budget. With this shortfall as a backdrop, DOF forecasters will likely lower their baseline forecast and reexamine their outlook for economic growth and tax collections for next year. The Legislative Analyst's Office (LAO) has previously cautioned that the current DOF forecast is overly optimistic, especially as it relates to revenue growth tied to capital gains income. Specifically, the LAO has noted that the Administration's projection for capital gains income for the Budget year is in line with the gains experienced during California's robust growth period of 2002 to 2006, even though future home price appreciation in the state, a significant factor in capital gains, is expected to be only a small fraction of that past growth. The LAO has warned of a revenue shortfall of $3.0 billion to $4.0 billion in 2012-13 due to this vulnerability.

The May Revision, scheduled for release on May 14, 2012, will take all of these factors into consideration, in addition to incorporating the latest information on caseload growth in all of the state's entitlement programs. Expect the Budget gap to grow from the $9.2 billion projected in the January Governor's Budget to potentially over $15.0 billion, given the weak revenue collections experienced thus far.

While there might be some positive developments that mitigate this deteriorating situation, such as a slowdown in the state prison population or lower caseloads in the California Work Opportunity and Responsibility to Kids program and Medi-Cal, do not expect the positive developments to be sufficient enough to offset the downward revenue revision.

Moreover, to achieve a balanced Budget for next year, the Governor is relying on voter approval of his tax hike initiative, which has yet to qualify for the November 2012 General Election ballot. If ultimately approved, this measure would provide $7.0 billion to $9.0 billion toward bridging the Budget gap. Clearly, the latest revenue information makes the Governor's task of proposing a balanced Budget at the May Revision even more daunting.