

Golden (State) Opportunity

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California voters sent a blunt but welcome message Tuesday about runaway government. By rejecting by nearly two-to-one the political establishment's \$16 billion in higher taxes, spending gimmickry and more borrowing, the voters said it's time government faced the same spending limits that the recession is imposing on everyone else.

Teachers unions, business leaders and the politicians outspent initiative opponents by six-to-one, and they still lost. Governor Arnold Schwarzenegger had warned that if these initiatives were voted down, government services would have to be slashed, criminals released early and public employees furloughed. But voters decided that as painful as these cuts may be, the alternative of letting the state's tax-and-spend machine continue was worse. How right they are.

The response so far from Sacramento is typically short-sighted. Mr. Schwarzenegger, legislators and public-worker unions are now conspiring to roll out plan B: a federal bailout. The Governor was in Washington on Tuesday and, sounding like a Detroit auto executive, declared: "We need assistance." As a starter he wants a federal guarantee on California's next \$6 billion bond offering.

But a federal bailout is an injustice to the residents of other states, especially those that run their governments responsibly. Why should taxpayers in Colorado, Virginia or Ohio pay for California's incompetence? Worse, one price of a bailout could be an Obama Administration demand that California remove its requirement for a two-thirds legislative majority to pass a tax increase. Another possible political target is repeal of the Proposition 13 property tax limitation. Yet these are the only remaining restraints on the appetites of the political class.

Tuesday's vote was a voter cry that the state needs more such restraints, and now is the time to push them. First, California needs a sturdy cap on the rate of spending growth. Thirty years ago this November, when California's economy was in a similar rut, three-quarters of the voters approved the famous Gann Amendment. That limited the annual growth rate of spending to population growth and inflation.

The result was that California's annual average rate of spending growth after inflation fell to 2% through the 1980s from 9% in the 1970s. California's state per-capita expenditures fell to 16th in the nation in 1990 from 7th in 1979. The economy soared, growing by 121% -- 14% faster than the U.S. average. The Gann limits were effectively neutered in 1988 and 1990 by initiatives that exempted education and transportation from the cap.

The next step is to fix California's steeply progressive and antigrowth tax code. California's 10.55% income tax and 9% sales tax are driving businesses and high income taxpayers out of the state, depleting the tax base month after month. They also lead to overspending during the good times as revenues boom, but to budget crises when those revenues fall precipitously during the busts. A 5% to 6% tax rate on sales and income without deductions would halt the flight to low-tax neighboring states and invite newcomers who could start buying houses again.

The state's public-employee pensions also need to be overhauled. According to the California Foundation for Fiscal Responsibility, the state pension funds are more than \$200 billion underfunded. Public employees can retire after 30 years on the job in their early 50s, with lifetime retirement benefits at 90% of their final salary. Some retirees receive \$200,000 a year or more in pensions. The solution is to follow Florida's lead and require new workers to accept defined contribution pensions like the 401(k) plans now dominant in the private work force. Without such a reform, many California cities will go bust and the state's tax burden will grow inexorably.

Despite the panic from Sacramento, Tuesday's vote was the best fiscal news out of California in 30 years. It showed that the voters are paying attention to the games their elected leaders have been playing, and they have finally blown the whistle. We hope the sound was heard as far away as another out-of-control government, the one in Washington, D.C.