

Out of Cash, California Turns to IOUs

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Editor's Note: Today, California enters a new fiscal year without a budget, and an estimated deficit of \$24 billion. Gov. Arnold Schwarzenegger refuses to sign a budget that raises taxes while Democrats in the state legislature are unwilling to eliminate social services. As the economy worsens and the budget gap becomes larger and even more difficult to close, the state controller is issuing IOUs.

SAN FRANCISCO — If you're waiting for a check from the state of California, keep waiting. You won't be getting it anytime soon.

Whether you're a student waiting for your financial aid to come through, a taxpayer waiting for a refund, a defense lawyer representing a prisoner on death row, a businessman with a contract, a mental health care provider, or a state-funded community clinic, you won't be getting any of the money California has promised you.

Instead, starting Wednesday, you can expect an IOU.

"It's ridiculous," said Teri McGinnis, director of Lyon Martin Health Services in San Francisco's Castro District, a community clinic with a specific emphasis on lesbian and bisexual women and transgender health care. "I don't get to IOU my staff or use IOUs to pay our lab fees. There's a gap in logic about our providing medical services to our patients and then the state not paying for them."

The clinic's only doctor, Dawn Harbatkin, worries that the IOUs will have an immediate impact on outside providers' willingness to furnish services for the clinic's patients.

"For example, instead of having to wait a month for their mammogram, patients will have to wait two months," she said. "It's going to delay all kinds of services."

McGinnis said a representative at the clinic's bank, Wells Fargo, called the state IOU "worthless" and said he would not cash the note.

"There's not a bank that is willing to lend against this IOU," McGinnis said. "What's an IOU from the state of California at a time when everyone's laughing at our budget?"

According to Beth Mills, a spokesperson for the California Bankers Association, no financial institution has yet agreed to redeem the IOU.

"This situation has put everyone in a really, really, really difficult spot," she said, noting that many banks were already having problems with liquidity.

"We value the relationships we have with our customers," Mills said. "But on the other hand, if you're taking these things, you have to look at who's issuing them."

Today, the state of California enters a new fiscal year without a budget and an estimated deficit of \$24 billion. Gov. Arnold Schwarzenegger refuses to sign a budget that raises taxes while Democrats in the state legislature are unwilling to completely eviscerate social services. Meanwhile, the economy worsens and the budget gap becomes larger and even more difficult to close.

State Controller John Chiang, who is issuing the IOUs, describes the crisis this way: "We start a fiscal year with a massively unbalanced spending plan and a cash shortfall not seen since the Great Depression."

Absent a budget agreement in Sacramento, the state's cash shortfall will grow from approximately \$3 billion at the end of July, to a projected \$3.7 billion in August, and \$6.5 billion in September.

"Unfortunately, the state's inability to balance its checkbook will now mean short-changing taxpayers, local governments and small businesses," Chiang said.

State workers will still get their salaries and the federal government has agreed to pick up the state's share of SSI/SSP, cash assistance to the aged, blind, and disabled — at least for now.

But nearly everyone else who gets a check from the state will be getting an IOU this week, and this first round of IOUs will not be able to be

cashied until Oct. 1.

Lynn Holton, the spokesperson for the Judicial Council of California, said that means the state's judges, prosecutors and clerks will still get paid, but that "the entire monthly funding for non-payroll operations costs for trial courts" would be paid with IOUs, including private security, contract mediators and probate investigators.

Criminal defense attorneys in death penalty appeals will also get IOUs. The courts will even have to use funny money to pay for their office supplies and their energy bill.

California's 58 counties will take the biggest immediate hit because local governments administer the bulk of social service programs. Local governments have seen this crisis coming for months, and have attempted to secure lines of credit to paper over the IOUs, but "credit markets have been frozen," said Kelly Brooks of the California State Association of Counties.

"Counties cannot even find lenders for routine cash flow borrowing," Brooks said.

As a result, Brooks said, already lean local budgets would likely get slashed again.

"We're going to see counties shut libraries down, not do street repair, not maintain parks," she said. "Anything that's not mandated by the state or federal government will be on the chopping block."

And if the budget stalemate continues, Brooks said, counties may begin issuing their own IOUs.

"God willing, we are out of this by then," Brooks said, "but it is written in government code and state law giving counties the authority to issue registered warrants (the official term for IOUs.) We're not aware of a single instance of a county issuing them before but this is uncharted territory."

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