

**SPEECH OF GOVERNOR EARL WARREN OUTLINING
PLANS FOR "RAINY DAY FUND" FISCAL POLICY**

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The State and the Taxpayer

I was thinking, as I came here today, that perhaps one of the reasons I was invited was that some of you people wanted a good look at the first California Governor who ever had to sit up nights and try to figure out what to do with all the surplus money pouring in the State Treasury.

Then I remembered that Jim Beebe, Chairman of my Citizens Tax Committee, and a number of Legislators would probably be here and that they might have told you that an even bigger problem is trying to figure out what not to do with the money. As a result, I decided I had best devote my time to further confusing the issue by reciting some of the reasons why we may not have as much money to spend as we expect and may actually be participating in a discussion of how to head off a future deficit.

I am going to start with the simple assertion that the term 'surplus' is a misnomer when applied to the California situation. Our State, at the moment, is merely in the same position as many individuals as they walk away from the cashier's window with their first pay check after a long spell of idleness. We and they merely use the word "surplus" to indicate that there is money in the pocket – that there is more money coming in at the moment than is being spent at the moment.

I do not believe anyone can make a careful analysis of California's financial position and outlook and reach the conclusion that our problem is as simple as the word "surplus" might indicate. It is more like the individual whom I just mentioned as he walks from the cashier's window to his home and finds a lot of old bills awaiting him. It doesn't quite describe the position of a State with a bonded indebtedness of \$139,823,000. It isn't a good word either if we grant recognition to the fact that the available source of supplies that produce tax revenues can change the size of our income almost overnight. It isn't even a good word when you realize that most of the present excess is invested in war bonds and is helping the war effort.

California, in a matter of months, has become one of the great industrial States of the Union and is teeming with industrial activity to a degree little dreamed of a year ago. The impact of global war has had a tremendous influence upon our entire economy. The tremendous stimulant of war expenditures has, under our existing tax structure, produced a value of tax income which surpasses any and all expectations based on previous experience.

Perhaps all this should make a new Governor feel good, for it is certainly the opposite of the condition experienced by most Governors. It does make a man feel good until he stops to realize just how artificial the situation is and that the conditions which have brought so much money into the treasury are all connected with war industry.

Actually, what we now term a surplus is the result of a terribly abnormal situation. It has no relationship with careful financing in state government. It is something that has developed wholly without stimulant or regulation on our part. In fact, we have had just about as much to do with it as we usually have when we find ourselves caught in a serious depression and go into a tailspin which plunges us headlong into the red.

War industries and payrolls have stepped up our revenues because we have had a tax structure in existence which was ready-made for the harvest. The sales tax and use tax have been the big producers. In fact, they have of late reaped what might be termed an unripened harvest for the income reflects a rush of pre-ration buying which cannot be immediately repeated. Offsetting some of these gains in revenue is the fact that war restrictions and curtailments have closed down on the opportunities for revenue from other tax sources. A serious financial situation is in the making, for example, in connection with the highway system.

Because we are taxed so heavily for war purposes there is a temptation existing to deal drastically with our state tax structure in general. To those who reason in this matter, I want to bring the warning that we can rest assured that the situation we now enjoy will change as soon as the war is over. What is now an enormous surplus can, with the return of relief problems and a drop in revenues, suddenly change into an enormous deficit unless we proceed with caution.

I believe we must approach the problem of state finances with the utmost caution and deliberation. The existent dangers are several. When a surplus exists in tremendous amounts everybody can find a use for it in all levels of government. We must, therefore, immediately establish safeguards against raids which are not the product of thoughtful planning. We can always find legitimate use for more money that we ever had to spend before, but we must keep in mind that the standards we set through expenditures now may add to our disappointments later on. When our revenues fall off, we will not only be obliged to face the decrease but will have to try to measure up to the new standards acquired during the period of affluence. There is a saying that it is not wise to burn a candle at both ends and I believe it has significant application in regard to treatment of our surplus.

We should, in my opinion, proceed to protect ourselves against the inevitable reaction which will follow the war by conserving a considerable portion of our surplus for post-war works projects which will have the double effect of rehabilitating our governmental plants and putting men to work instead of forcing them to turn to a dole.

We must of necessity measure our present abnormal position in the light of past experiences and not forget that had it not been for the stimulant of war, our state would

still be in the red. There is still need for effective economies in State Government and I trust more can be done even though the major portion of the expenditure requirements are frozen in the Constitution and Statutes by direct action of the people.

Regardless of the fact that war necessity has advanced us toward our dream of industrialization and self-sufficiency, we must remember that we have not arrived at this position through our own efforts and that once the war is over Uncle Sam will not be likely to protect us from the pull of normal competition and the industrial habits which have kept us from winning such recognition in the past.

It is not difficult to see how people in other parts of the country would think California a good place to start curtailing industrial production once post-war reaction has set in. Those invisible strings which served as restraints upon the westward movement of industry before the war will start their competitive pull again once the war has ended. Our job is to capitalize upon the recognition of our resources and advantages which war need has forced upon us and fight to hold what the war has given us. I believe we can retain much of this industry if we plan for the future with the same ingenuity we have displayed in establishing and making war industries efficient. We can't do it by niggardly expenditures in connection with the exploitation of our resources. We can't do it with a financial policy which does not safeguard the future, and we can't do it with a policy which permits the indulgence in extremes, either in immediate expenditures or immediate tax slashes.

There is no denying the fact that California stands today in an exciting position and that if it can keep its balance it will soon come to realize that it has been standing on the threshold of an exciting future. What it does in regard to finances and taxes will play an important part in its future. We have assumed a role of great importance to the nation in maritime construction and shipping and we are pacing the world in aircraft production. We have subjected our entire economy to the war effort and, strangely enough, have reaped a dividend of temporary abundance in State revenue.

I believe we must follow the example of the cautious individual as we approach this unprecedented financial development. We must look ahead and keep in mind that the day will come when we will have to finance our necessities with less money and curb all new habits of extravagance which are the outgrowth of present day affluence. We must bear in mind that the problem faced by the individual under such conditions is magnified many times over in government. The bigger and more complicated the institution, the more difficult it is to correct spending habits. It is more difficult to accomplish curtailment in government than in business and the bigger the government the more the difficulties encountered.

The State of California is a tremendous institution. In the past two years, our State Government alone has expended over five hundred million dollars. The State budget now being considered by the Legislature calls for the expenditure of \$463,947,005. With totals such as these in mind, it is easy to appreciate that the discussion of California

finance involves serious considerations. These amounts would not have been expended or proposed had there been no need and public demand.

In the preparation of the budget submitted to the Legislature in January, I followed the general principle that war-essential services must be adequately provided for and less essential services curtailed. The budget total is \$55,000,000 less than the total requests submitted, yet it is still of such size that it could not have been easily financed by our present tax structure during the depths of the depression.

Argument Against New Extravagance

This fact alone, in my opinion, is an argument against the development of new and extravagant spending habits just because we have suddenly achieved a favorable balance in current revenues and expenditures. It is one of the reasons why I believe we should jealously guard and protect all excess monies which come our way during this abnormal period.

It is my belief that we are going to need the safeguard of a favorable financial balance soon after the war has ended and that the size of that balance will have a definite influence upon the facility with which we absorb post-war shocks. I want to see provision made now which will conserve a sufficient portion of the present surplus to ease the strain of post-war transition. It is my hope that the Legislature will take such action as is necessary to insure the use of funds now being accumulated for post-war purposes, particularly for purposes which give recognition to the need for keeping manpower employed and increasing State efficiency.

Tax Reduction Possible

Lastly, I believe we should give the public the benefit of any tax reduction that can be afforded after the necessary safeguards for our financial future have been erected.

It is fortunate that the present and prospective financial condition of State Government is such as to allow consideration of both ways of creating adequate future safeguards and tax reduction. It is because such a situation exists, however, that there is need for extra caution. In times such as these it is not safe to trifle with fundamentals, and I believe this reasoning must be applied to both expenditures and taxes.

You know of the time and effort the Citizens Tax Committee is devoting to a study of all the ramifications of the financial problem now confronting us and I know that the findings of this committee will be greatly appreciated by the Legislature as it will be by myself when it starts deliberations next month. I am confident that the Legislature will not only be appreciative of this cross section opinion but will make the same serious approach and that the session will not end without proper safeguards for our future being erected. I say this because one month of contact with Legislators in session has caused me to become appreciative of the spirit of serious cooperation now prevalent in Sacramento. Under such conditions, I believe we can look forward with the expectation

of real accomplishment, not only in connection with finances and taxes but in connection with all related problems.