AGENDA
ASSEMBLY BUDGET SUBCOMMITTEE NO. 4 ON STATE ADMINISTRATION

Assemblymember Warren Furutani, Chair

WEDNESDAY, MAY 19, 1:30 PM
STATE CAPITOL, ROOM 437

CONSENT CALENDAR

8950 CALIFORNIA DEPARTMENT OF VETERANS AFFAIRS

ISSUE 1: RECTOR CREEK, DAM, AND RESERVOIR SUPPLEMENTAL REPORTING LANGUAGE (SRL)

The Subcommittee heard the Yountville Rector Creek Dam and Reservoir, (operated through the Veterans Home of California –Yountville) on May 4th and approved (5-0) to instruct the CDVA to pursue efforts to maximize the value of the asset given the current budget difficulties.

Specifically, the Subcommittee took an action to require the CDVA to: (1) report back to the Subcommittee on the authority of the CDVA to sell water and the amount of surplus water that can be sold, (2) approve in concept the sale of surplus water, (3) adopt budget bill language that would direct any revenue that is generated.

Per that action, the Subcommittee is presented with the following Supplemental Reporting Language (SRL) that specifies the reporting requirements for the CDVA.

The Department shall report on:

1) Amount of carryover storage remaining in the reservoir at the end of each calendar quarter for the last three years;
2) Amount of inflow to the reservoir, by month or quarter;
3) Amount of water deliveries to City of Yountville, Veteran's Home and Department of Fish & Game hatchery base;
4) Amount of sewage water from the Veteran's Home treated by City of Yountville for the last three years;
5) All inquiries from private parties as to the possibility of purchasing water from Rector Reservoir; and,
6) All Department water conveyance facilities connected to the reservoir, which may be used to deliver water to other parties with or without adjustments to such facilities.

Staff Recommendation: Approve Supplemental Reporting Language

ISSUE 2: RECTOR CREEK, DAM, AND RESERVOIR TRAILER BILL LANGUAGE

In accordance to the action taken by the Subcommittee on May 4th, the following Trailer Bill Language authorizes the CDVA to sell any surplus water.

Trailer Bill Language

(a) The Legislature finds and declares that the current budget difficulties make it imperative that the Department of Veteran Affairs use all its resources to raise revenue to pay for the programs that serve California veterans, and the water in Rector Reservoir is one such resource.

(b) Notwithstanding Section 14715 of the Government Code, the Department shall be authorized to solicit proposals from private parties or public agencies to purchase water from Rector Reservoir before September 30, 2012. The Department shall be further authorized to negotiate the sale of surplus water from Rector Reservoir to such parties for delivery before September 30, 2012. The Department shall make efficient use of its water resources to maximize the amount of surplus water available for sale. The Department shall comply with State Water Resources Control Board requirements for a temporary urgency change, one-year water transfer or other procedure to allow a sale of water from Rector Reservoir

Staff Recommendation: Approve Trailer Bill Language

ITEM TBL 2009 BUDGET REFORM REPEAL

In the 2009 Budget Act Government Code Section 99040 was added to require the Governor to notify the Legislature and other specified entities if a Constitutional Amendment was approved by the voters in 2009 regarding transfers from the Budget Stabilization Account.

This language is now obsolete and no longer necessary, so the Governor' proposed to repeal it.

Staff Recommendation: Approve

ITEMS TO BE HEARD

ITEM 0860 BOARD OF EQUALIZATION

ISSUE 1: FUEL TAX SWAP ADMINISTRATIVE COSTS

This issue was discussed at the April 27 Sub-Committee meeting, but was held open upon direction from the Chair.

BOE administers the sales and use tax and various excise taxes on vehicle fuels. The Legislature approved ABx8 6 and SB 70 (the Fuel Tax Swap) which will result in (i) a reduction in the sales tax on gasoline and an increase in the excise tax on gasoline effective July 1, 2010, and (ii) an increase in the sales tax on diesel and a decrease in the excise tax on diesel, effective July 1, 2012. The Fuel Tax Swap also requires annual calculations and potential tax rate adjustments in order to maintain revenue neutrality.

Under the Fuel Tax Swap, BOE administrative responsibilities will expand as a result of potential annual increases and decreases in the tax rate. These responsibilities include reprogramming the Integrated Revenue Information System (IRIS); revising returns, notices and other forms; notifying taxpayers; and, registering taxpayers for the floor stock taxes. An increasing rate could result in more motor vehicle fuel accounts being subject to audit. Varying rates will also add complexity to refund processing and require additional field audits. This Finance Letter requests $1.5 million ($1.2 million Motor Vehicle Fuel Account) for 2010-11 and $1.4 million ($1.1 million Motor Vehicle Fuel Account) to administer the Fuel Tax Swap. This augmentation would add 11.4 PYs on an on-going basis.

Funding Source	2009-10 (000s)	2010-11 (000s)	2011-12 (000s)
General Fund		$138	$118
Special Funds		$1,249	$1,128
Reimbursements		$151	$129
Total		$1,538	$1,375

STAFF COMMENTS

Some of the activities identified by the department appear to be short-run costs that should eventually decline as taxpayers get used to the annual adjustments. Of the 11.5 positions, only 2 are temporary (limited term and temporary overtime). The suggested increased workload due to increased complexity that would be expected to decline over time and warrant positions associated with short-term costs to be limited-term. This suggests that a good proportion of the positions should be limited term. In addition, the proposals appear to overstate the amount of resources necessary for taxpayer information services. This can be accomplished by additional education and web services.

BOE staff suggests that on the excise tax side, costs will increase because more revenue is at risk. On the sales tax side, they indicate that cost will go up due to complexities because the sales tax change is a partial exemption. The argued increase in complexity is not clear, since the state already has additional partial exemptions for other purchases.

Staff Recommendation: Approve 10 positions, 8 in 2010-11 and 2 in 2011-12. Convert ½ of permanent positions to 2-year limited-term.

ISSUE 2: REPORTING LANGUAGE FOR TAX AGENCIES

Board of Equalization and Franchise Tax Board have received augmentations for the purposes of increasing revenues though expanded and improved audit and collections activities, as well as other related efforts to increase revenue collection. Legislative oversight may be advisable to ensure that such additional resources are deployed in an effective and efficient manner.

Both agencies either have, or formerly had, annual reporting requirement regarding the their revenue collection activities. Pursuant to 2002 and 2006 Budget Acts, BOE reports to the Legislature by December 1 each year on its audit and collection activities. Prior to 2008, FTB also prepared a similar report, at which point the report was discontinued and is no longer being provided to the Legislature.

STAFF COMMENTS

Refinement of the existing or former reporting requirements would be necessary to gauge the success of any augmentations to the department's budgets for revenue collection activities. To the extent possible, any required reports should build off the analytical work the agencies already carry-out for their administrative purposes and not entail additional workload.

Staff Recommendation: Direct staff to consult with BOE and FTB to draft reporting language, or amend existing language, that evaluates the effectiveness of budget augmentations related to revenue collections.

ITEM 1730 FRANCHISE TAX BOARD

ISSUE 1: FEDERAL TREASURY OFFSET PROGRAM

This issue was discussed at the April 27 Sub-Committee meeting, but was held open upon direction from the Chair.

FTB's compliance efforts benefit significantly from the interchange of data with other state departments and the federal government. Cross–matching data increases the likelihood of reaching successful conclusions in enforcement efforts and also increases the speed with which such activities are concluded. One of these cooperative programs is the Federal Treasury Offset Program (FTOP) which allows the state to collect on tax liabilities through a reduction in the amount of federal refunds owed to federal taxpayers.

Federal law provides authority for the federal government to collect various past due liabilities owed to states—including state tax obligations—by reducing the amount of refunds owed to its taxpayers. In return, the federal government requires states participating in the program to offset against state refunds certain federal obligations past due. Forty states currently participate in this federal program; California is only one of two states with a state income tax that does not currently participate. In 2008, the program resulted in $380 million being collected for participating states.

The FTOP project will consist of four phases. The first phase will incrementally expand the current pilot program as well as begin the design, development and enhancements of FTB's accounting and collection systems for personal income tax cases. The second phase will begin the automatic transmission of personal income tax data to the federal program. Phases three and four will implement a similar program for businesses entities. This proposal is for phases one and two and consists of a request for $847,000 and 11 positions.

Project Estimates	2010-11 ($ millions)	2011-12 ($ millions)	2012-13 ($ millions)	2013-14 ($ millions)	Total ($ millions)
Revenue	$6.0	$80.0	$113.0	$93.0	$292.0
Expenses	$1.8	$3.6	$2.8	$2.8	$11.0
Net Revenue	$4.2	$76.4	$110.2	$90.2	$281.0

STAFF COMMENTS

The Federation of Tax Administrators (FTA) considers the offset program an effective collection tool for states to use. Its effectiveness was demonstrated in a pilot program put in place last year by FTB. The program effectiveness is demonstrated not only through the offsets actually made, but the number of taxpayers who—upon receiving a Notice to Offset from FTB—chose to submit payment directly to FTB. The initial year of the project has a benefit:cost ratio of 3.3:1. Once established, the project is estimated to have a benefit:cost ration of 33:1.

Staff Recommendation: Approve.

ISSUE 2: RESTORATION OF FURLOUGH REVENUE

This issue was discussed at the April 27 Sub-Committee meeting, but was held open upon direction from the Chair.

As indicated above under the general discussion of the FTB and staffing level, the department was significantly affected by the furlough program in terms of revenue generation. This request would serve two purposes. It would:

1. Exempt FTB from any furlough requirements if the furloughs were to continue. Furloughs are not part of the budget; however, one personal leave day per month is included in the May Revision.
2. Provide additional temporary resources for the agency to address the backlog in various divisions that occurred due to the furlough program.

In the current year, FTB directed staff toward workload which had the highest benefit:cost ratio in order to maximize revenue to the state. These revenue loss mitigation steps were discussed in the overview section of the department present on April 27. The result was an increased buildup of workload which was set aside, even though this represents work that can be efficiently and effectively undertaken. This workload consists of direct revenue production including new and expanded audits, return processing, and additional filing enforcement efforts.

The contingent portion of the BCP—exemption from any 2010-11 furlough programs—would generate $860 million in revenue. In order to accomplish a reduction in the accumulated backlog of work, FTB has additionally requested $14.7 million General Fund and 158 PYs for the budget year. The request is for $9,193,000 in overtime and 158 PYs with associated compensation of $4,818,000. All funding/positions are temporary and only for the 10/11 fiscal year. This will consist entirely of overtime and temporary help authorization and result in revenues of $50 million in the budget year.

In response to questions from the Chair and members regarding positions, FTB provided additional detail regarding the request. 98 positions are seasonal clerks and students, 55 positions are data entry and tax compliance positions, and 5 are analyst and IT positions necessary to support the processes and systems impacted by additional staffing levels. Positions will be filled predominantly with seasonal permanent intermittent staff, retired annuitants, and student assistants. Overtime funding will be used for existing staff. The 158 temporary positions and overtime funding allow us to work on tasks not completed in 2009/10 and recovers $50 million of the $465 million. The following tasks are a few of the tasks these resources will be used for:

1. Close existing collection cases faster and open new ones. (overtime, seasonal staff, and students assistants)
2. Open audits that would otherwise not be open but noncompliance has been identified. (overtime and retired annuitants)
3. Key critical data from the 2009 tax returns that is critical in our efforts to evaluate compliance on returns filed and prioritize existing collection accounts. (overtime and seasonal staff)

STAFF COMMENTS

FTB staff should comment on how the Governor's May Revision proposal requiring one personal leave day per month will affect the department's activities, especially with respect to revenue collection.

Staff Recommendation: Approve.

ISSUE 3: ACCOUNTS RECEIVABLE GROWTH

FTB maintains an inventory of accounts receivable, which is subject to collection efforts based on criteria including: the potential revenue, the probability of collection, and the costs of such collection efforts. FTB's accounts receivable inventory has increased steadily of the last three years—with personal income tax accounts receivable up by 25 percent and business entities up by 43 percent. In August 2009, the accounts receivable balance was $8.1 billion, of which $5.5 billion was deemed collectible.

The accounts receivable increase is due to a variety of factors, including:

- Staff reductions at FTB from the furloughs.
- Increase in taxpayers unable to pay their taxes.
- Reduction in the ability to resolve cases early in the process.
- Increase in the number of filing enforcement actions.

FTB's tax collection activities against accounts receivable include both an automatic billing system as well as staff administered activities. The automated system manages the collection process by issuing billings, notices, levies, and attachment of assets. FTB staff then follow-up on the cases that require addition work to reach resolution. In order to reduce the accounts receivable inventory to a reasonable level and maintain it, FTB proposes to maximize the use of data and enforcement tools, enhance the call center technology to resolve cases early in the process, and out-source certain cases to vendors.

The request is for $8.2 million General Fund to for 111 permanent positions to reduce FTB's accounts receivable to a reasonable level and maintain it. Estimated revenues for the augmentation are $52.5 million in 2010-11 and $111 million in 2011-12. This would result in benefit:cost ratios for each of the respective years of 6.4:1 and 14:1.

STAFF COMMENTS

It is not clear why permanent positions are necessary for this activity. The increase in accounts receivable inventory appears to be the result of short-term economic and budgetary influences rather than long-term trends that have developed in accounts receivable. In addition, the staff that would be directed to this activity does not require the same type of training as other activities in the department that are of a more technical nature. This suggests that limited-term positions would be appropriate.

Staff Recommendation: Approve, based on 2-year limited-term positions.

ISSUE 4: HOMEBUYER TAX CREDIT WORKLOAD

The Legislature adopted statutes that established a tax credit equal to the lesser of $10,000 or 5% of the home purchase price for first time homebuyers and purchasers of new homes. The FTB will administer the credit in a manner that will allow a total amount of credits not to exceed $200 million over the life of the program. Activities required of FTB to administer the program include maintaining credit reservations, accepting and reviewing credit applications, reviewing certifications of purchase contracts, accepting and reviewing settlement statements, and maintaining a program waiting list. The program is similar too, but larger, than a similar tax credit program last year. FTB cites a number of higher cost factors in the new program and requests additional resources of $887,000 General Fund and 9 positions.

STAFF COMMENTS

The tax credit program replaces a $100 million credit program which was in effect last year. FTB received 3 limited-term positions. The new program is twice as large, but not twice as complex. Given this, there is little justification for a tripling of resources. Staff recommendation is based on similar fixed costs for this program and the prior one. A modest increase from the resources needed for the prior program is justified.

Staff Recommendation: Approve 6 positions for a 1-year limited-term.

ITEM TBL CAPITOL OUTLAY TRAILER BILL LANGUAGE

ISSUE 1: MINOR CAPITOL OUTLAY PROJECT LIMIT UPDATE

The Governor's Budget requests trailer bill language to update the project limit for statewide minor capital outlay from the current level of $400,000 to $800,000 and require the Department of Finance to adjust the minor capital outlay project limit every two years to reflect the percentage change in the annual California Construction Index.

Statewide capital outlay projects are budgeted as either major or minor projects. Major capital outlay projects are those with a total cost exceeding $400,000. Each major capital outlay project is budgeted to an agency as a separate line item and in one or more phases; i.e., land acquisition, preliminary plans, working drawings, construction, and equipment. With the exception of some state agencies that have delegated authority, major capital outlay projects are administered by the Department of General Services (DGS) on behalf of the various state agencies. Minor capital outlay projects are those with total costs of $400,000 or less, and are typically budgeted in a lump sum appropriation to the state agency. In general, state departments can contract directly for minor capital outlay projects without using DGS management services. The $400,000 limit for minor capital outlay was established in statute in 2001 and had not been updated since that time.

COMMENTS

Staff notes that this proposed trailer bill language is also being pursued in the policy process in AB 2181 (Hagman). AB 2181 passed the Assembly Appropriations Committee on May 5 and is pending further action.

Staff Recommendation: Deny, without prejudice, and defer to the policy process (AB 2181).

ITEM 9966 VARIOUS LEASE-REVENUE BOND DEBT SERVICE ADJUSTMENTS

The Governor proposes various technical corrections for the payment of lese-revenue debt service in fiscal year 2010-11. The total of these changes is an increase of approximately $4.5 million in General Fund expenditures, and $10.6 million in other funds for the payment of lease –revenue bonds that were sold to finance the Department of General Services Central Plant Renovation project. The state sold bonds in the Fall of 2009 to finance the construction phase of this crucial project that provides heating and cooling to 23 state office buildings in downtown Sacramento.

COMMENTS

These bonds have been sold and must be paid. This request simply allocates the appropriate costs and payments to the departments who benefit from the project.

The Central Plant Renovation project has long been considered a top priority for state operations because of its health and safety impact for 23 state buildings.

Staff Recommendation: Approve

ITEM VARIOUS VARIOUS SPECIAL FUND LOANS/TRANSFERS/EXTENSIONS

The Governor proposed the following actions:

- 0890 Secretary of State - $10 million loan from the Victims of Corporate Fraud Compensation Fund.
- 0968 Tax Credit Allocation Committee - $25 million loan from the Tax Credit Allocation Fee Account.
- 0968 Tax Credit Allocation Committee – Delay $10 million loan repayment for the Tax Credit Allocation Fee Account from June 2011 to July 2013.
- 0968 Tax Credit Allocation Committee – $25 million loan from the Occupancy Compliance Monitoring Account.
- 0968 Tax Credit Allocation Committee – Delay $10 million loan repayment from the Occupancy Compliance Monitoring Account from June 2011 to July 2013.
- 0956 Debt and Investment Advisory Commission – Delay $2 million loan repayment from June 2011 to July 2013.
- 0959 Debt Limit Allocation Committee - Delay $2 million loan repayment from June 2011 to July 2013.
- 1110 Department of Consumer Affairs - $10 million loan from the Accountancy Fund, Professions and Vocations Fund.

The net result of these actions is $94 million in general fund benefit.

COMMENTS

Staff has reviewed all the above fund balances, and concurs with the Department of Finance that these funds can handle these loans/loan extensions. Additionally, these loans will have to be paid back with interest, and if any program utilizing these funds requires this funding in order to complete its required functions, these provisions include language requiring a repayment of the funds at that time.

Only one affected department has brought concerns to staff's attention. That is the Secretary of State's Office. The Committee may wish to ask them to come forward to share their concerns, and ask the Department of Finance to respond.

Staff Recommendation: Approve

ITEM 0840 STATE CONTROLLER'S OFFICE

ISSUE 1: 21ST CENTURY PROJECT

This issue was originally heard on April 21, 2010.

The Governor's budget requests 111 two-year limited term positions and $66 million ($30 million General Fund) to continue the implementation of the 21st Century Project which will result in an integrated human resource management system to replace the existing payroll, employment history, position management and leave accounting legacy system.

The SCO pays approximately 249,000 employees, including state civil service, California State University and Judicial Council employees, judges, and elected officials. The 21st Century Project (Project) will replace the existing statewide human resource management systems in order to improve management processes and fulfill payroll and reporting obligations accurately and on time. The Project began in May 2004 and is currently projected to end in 2012-13; the current estimated total cost (one-time and continuing) is $307.8 million.

In January 2009, the state terminated the contract with BearingPoint, the Project systems integrator, for failure to meet contractual commitments. There is the potential for recovery of a performance bond from the prior systems integrator, anticipated to offset project costs by $25 million. <u>The Committee may wish to ask if there is any update on the effort to recover those funds.</u>

After contract termination, the SCO developed a "go-forward" strategy to complete implementation of the Project. The major change in this strategy included revising the scope of the Project to exclude CSU employees, which the SCO indicated will be addressed in a separate project at a future time. This revised approach was included in Special Project Report No. 3 which was approved by the Office of the Chief Information Officer (OCIO) in May 2009. The SCO then began the process to procure a new systems integrator to complete the Project. The SCO has since completed the procurement and selected SAP Public Services, Inc., as the new systems integrator. The new contract includes the system integrator services and supplemental software tools necessary for the completion of the Project.

On January 21, 2010, the Joint Legislative Budget Committee (JLBC) approved a Control Section 11.00 request from the SCO related to the Project. This Section 11.00 request was based on the OCIO's December 16, 2009, approval of Special Project Report No. 4 for the Project which delineated several contract changes and cost adjustments. In its letter approving the SPR, the OCIO specified several conditions for the Project including submission of a detailed cost tracking report on a quarterly basis.

As noted, the JLBC approved the Section 11.00 request. However, due to the magnitude and complexity of the Project, the JLBC requested that the SCO provide the Senate Budget and Fiscal Review Committee and Legislature with regular updates as the Project progresses, including the quarterly cost tracking report that is provided to the OCIO. Additional requested information included updates on the status of the Bearing Point litigation and more information about how the Project is managing risks that could impact the performance of the system or the cost of the Project.

COMMENTS

The need to transition the state from a transaction-based system to an enterprise database system that supports the business needs of state government is clear. This project continues to be on track, and provide constant updates to the Legislature on their progress. Their first report will be provided in a matter of weeks, and the Controller's Office staff has consistently been very responsive to all requests from the Legislature.

Pursuant to the Joint Legislative Budget Committee request, the Controller's Office will continue to provide quarterly reports on progress to the Legislature, allowing proper oversight of this important project.

Staff Recommendation: Approve

ISSUE 2: MAY REVISE – MOTOR VEHICLE FUEL STORAGE TAX

The Governor requests $100,000 and one one-year limited-term position to address the additional workload associated with AB 6 of the 8th Extraordinary Session affecting motor vehicle fuel tax activities.

The new code requires, buy August 31, 2010, that each taxpayer subject to the storage tax shall prepare and file with Board of Equalization (BOE) a tax return accompanied by a remittance payable to the Controller. The BOE has requested additional assistance from the Controller to deal with this new task. The Controller's role is to maintain accounting records, bill and collect delinquent account receivables, process payments received, and issue refunds. The Controller's office estimates the new tax will require the establishment of approximately 7,500 new accounts. Current motor vehicle tax issues are handled by one position at the Controller's office and they cannot absorb the workload of this new and more complex system.

COMMENTS

AB 6 8X was a very complex bill and without proper tracking and follow-up by the Controller's office significant revenue the state is counting on could be lost. This position is requested on a one-year limited-term basis to allow them to appropriately evaluate the actual workload created by the new system.

Staff raises no concerns with this proposal.

Staff Recommendation: Approve

ITEM 9620 CASH MANAGEMENT AND BUDGETARY LOANS

This budget item appropriates funds to pay interest costs on General Fund borrowing used to overcome cash flow imbalances during the fiscal year. Because receipts and disbursements occur unevenly throughout the fiscal year, the General Fund borrows in most years, even though each budget is balanced when enacted and funds are repaid within the fiscal year. Interest is paid on both internal borrowing (such as cashflow loans from special funds) and for external borrowing (such as Revenue Anticipation Notes (RANs). This item additionally pays interest costs for budgetary borrowing by the General Fund from special funds. Budgetary borrowing is across fiscal years and is "counted" as a budget solution, whereas cashflow borrowing is not counted as a budget solution (only a cash solution).

ISSUE 1: CASHFLOW

The Governor's Budget includes $540 million for interest costs on cashflow borrowing and $58 million for interest costs on budgetary borrowing – all General Fund. Of the cashflow amount, $150 million is for internal borrowing and $390 million is for external borrowing. Overall, expenditures in this item are up significantly – a total of $598 million is proposed for 2010-11, versus revised expenditures of $353 million in 2009-10. The 2009-10 funding in the table reflects May Revise adjustments. The amount originally budgeted for 2009-10 was $546.6 million. That amount was reduced to the current estimate after the cost of external borrowing came in significantly below estimates.

Type of loan	2008-09 Actual Cost	2009-10 Revised Estimated Cost	2010-11 Estimated Cost	2010-11 May Revise
External Cashflow Borrowing	$152.3	$130.0	$390.0	$250.0
Internal Cashflow Borrowing	$124.9	$75.0	$150.0	$100.0
Budgetary Loans	$0	$8.0	$58.0	$26.0
Contingency	$0	$69.0	$0	$0
TOTAL	**$277.2**	**$282.0**	**$598.0**	**$376.0**

The table above indicates the interest costs per category across the three fiscal years (in millions):

May Revise: The May Revise significantly reduced borrowing cost estimates for both the current year and budget year. Cost reductions were based on lower than anticipated interest rates, updated interest projections, and a reduced number of loans being repaid.

Budget Flexibility to Augment Funding: Funds to pay interest for external cashflow borrowing are continuously appropriated and therefore expenditures may exceed the amount budgeted as necessary. Funds to pay interest for internal cashflow borrowing and to pay interest for budgetary borrowing are appropriated in the budget act; however, budget bill language allows the Department of Finance to augment the appropriation if needed to pay interest costs. Due to this budgetary flexibility, the Legislature need not build in contingency funding for this item, but rather, can fund at the level of anticipated expenditures.

Deleted Budget Bill Language for Joint Legislative Budget Committee (JLBC) Reporting: The 2009 Budget Act included the following budget bill language (BBL) for Item 9620-002-0001 related to budgetary loans; however, this language is deleted from the proposed 2010 Budget Act:

> *Provision 2: The Director of Finance shall notify, in writing, the Chairperson of the Joint Legislative Budget Committee within 30 days of ordering the repayment of any loan included within the provisions of this item.*

COMMENTS

The Committee may wish to ask the Department why it chose to remove the reporting language.

The Committee may wish to ask if they believe they have reduced these amounts as much as is prudent, given the fact that there is no need to over-estimate these amounts.

Staff Recommendation: Approve May Revise numbers and restore the JLBC reporting language.

ITEM 9625 INTEREST PAYMENTS TO THE FEDERAL GOVERNMENT

This budget item provides expenditure authority for the payment of interest to the federal government for federal funds held in state accounts. Under federal law, interest is sometimes required for the period between when federal funds are deposited in a state account and the disbursement of the funds for the program purpose.

ISSUE 1: INTEREST PAYMENTS

The Governor's January budget included $30 million General Fund and about $1 million in Special Funds for interest payments. This is the same level of funding approved with the 2009 Budget Act; however, the Department of Finance has since reduced the estimate of 2009-10 General Fund interest costs from $30 million down to $5 million (as shown below). The table below, with data from the Governor's Budget, shows the three-year costs (in millions):

Type of loan	2008-09 Actual Cost	2009-10 Revised Estimated Cost	2010-11 Estimated Cost	2010-11 May Revise
General Fund cost	$13.9	$5.0	$30.0	$10.0
Other funds cost	$0.3	$1.0	$1.0	$1.0
TOTAL	**$14.2**	**$6.0**	**$31.0**	**$11.0**

In past budgets, provisional language in the budget bill has allowed the General Fund amount to be augmented by up to $10 million, and for the Special Fund amount to be augmented by up to $1 million – both after 30-day Joint Legislative Budget Committee (JLBC) reporting. The language proposed this year would remove any caps on augmentations but would retain 30-day JLBC reporting.

COMMENTS

The Administration should indicate why they propose to remove the statutory caps on funding augmentations. Due to the budgetary flexibility to augment funding, the Legislature need not build in contingency funding for this item, but rather can fund at the level of anticipated expenditures. The Committee may wish to ask if the new $10 million estimate has been reduced as much as is reasonable for next years estimates.

Staff Recommendation: Approve May Revise

ITEM TBL CASH RELATED TRAILER BILLS

The Administration has proposed various pieces of trailer bill language related to cash. The first issue below is suggested clean-up to action already taken in the 8th Extraordinary Session. The remaining issues are Administration proposals from the January Budget and from April Finance Letters.

ISSUE 1: CLEAN-UP TO SPECIAL SESSION CASH MEASURES

Additional amendments have been suggested by the Administration and other parties to clean-up or clarify the cash-related measures adopted in the 8th Extraordinary Session (AB X8 5 and AB X8 14). Specifically, the proposed language would: (1) clarify the process for school districts to apply for a hardship waiver to be excluded from any deferrals in 2010-11; and, (2) create a hardship waiver process for the deferral of Highway User Tax Account (HUTA) apportionments to exempt a city that has bonded against the HUTA apportionment, as specified.

Staff is not aware of any concerns with this language.

Staff Recommendation: Approve as placeholder language

ISSUE 2: TAX CREDIT ALLOCATION FEE ACCOUNT RECLASSIFICATION

In a January proposal, the Administration requests language to reclassify the Tax Credit Allocation Fee Account, such that any General Fund cashflow borrowing will require an interest payment. The Department of Finance indicates that is a technical fix and this type of special fund should receive interest under state law. Since the fund balance is relatively small (about $4.2 million) any additional General Fund interest costs would be minor.

Staff is not aware of any concerns with this proposal.

Staff Recommendation: Approve as placeholder language

ISSUE 3: PROMPT PAYMENT ACT

In a January request, the Administration proposes language to revise the Prompt Payment Act, which defines deadlines for the state to timely pay invoices and pay refunds. Current law requires payment of an undisputed invoice within 45 days and undisputed refunds within 31 days. This language would standardize the timeline, and make both deadlines 45 days. Current law requires late payment penalties for certain small and nonprofit businesses to accrue at 0.25 percent of the amount due, per calendar day. This equates to an over 90 percent annual interest rate for these small businesses and nonprofit organizations. The proposed language would change the penalty to accrue at 10 percent above the United States Prime Rate on June 30 of the prior business year.

<u>LAO Recommendation:</u> The LAO recommends that the Legislature approve the proposed trailer bill. The legislation would consolidate code provisions, thereby reducing potential

administrative confusion about the state's late payment penalties. Penalties owed to certain small businesses and nonprofit organizations for late payments would remain substantial and still deter late payments by state departments, but these payments would be reduced to a much more reasonable level.

COMMENTS

This language would reduce the state's costs in the case of undisputed refunds that are paid more than 31 but less than 45 days after receipt of the notice. This bill would also reduce the state's penalty costs for late payment of bills to certain small and nonprofit businesses.

Staff Recommendation: Approve as placeholder language

ISSUE 4: FEDERAL FUNDS FOR STATEWIDE INDIRECT COSTS

In a January request, the Administration proposes language to allow the Director of Finance to reduce a department's budget and transfer associated funds to the Central Service Cost Recovery Fund, the General Fund, or both, in a case where the department has not collected indirect cost funding from the federal government. For a federally-funded program, the federal government allows the state to direct a portion of the federal funds to cover the proportional centralized administrative costs of the state. The transfer authorized by this action would occur, if in the judgment of the Director of Finance, a department has not collected indirect cost funds from the federal government, regardless of the reason.

COMMENTS

It is unclear if uncollected federal indirect cost funds are a problem for California – the Department of Finance should speak to the problem they are trying to solve with this language. To the degree federal funds are under-collected, this proposal could result in relief to the General Fund as department budgets would be cut with related state funds shifted to the Central Service Cost Recovery Fund or the General Fund.

Staff concurs with the concept the Administration is attempting to address, but questions the specifics of the proposal. Since the language provides exclusive authority to the Director of Finance to make these adjustments, amendments may be warranted to limit the amount of any budget reduction and reporting requirement.

Staff Recommendation: Approve Control Section language similar to the proposed TBL, but include JLBC required reporting and a cap on the amount that may be transferred. Language to be drafted by staff.

ITEM 2240 DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT

ISSUE 1: APRIL FINANCE LETTER – COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG) DISASTER RECOVERY INITIATIVE

This issue was originally heard May 4, 2010.

The Governor requests approval for an increase in Federal Trust fund expenditure authority of $39.5 million to administer the Community Development Block Grant, Disaster Recovery Initiative.

In September of 2008, Congress appropriated over $6 billion in supplemental funding for "necessary expenses related to disaster relief, long-term recovery and restoration of infrastructure, housing and economic revitalization in areas affected by hurricane, floods, and other natural disasters occurring in 2008." On June 10, 2009, the US Housing and Urban Development department (HUD) announced the allocation of $3.7 billion in disaster aid, including $39.5 million for California.

HCD was required to submit an action plan by December of 2009, which it did, and received approval of that action plan in January 2010. <u>The Committee may wish to ask if the Legislature was provided opportunity for input into the action plan before it was submitted.</u>

HCD's planned use for these funds are:

1) $18 Million for - Housing/infrastructure/economic recovery & revitalization;

2) $15 Million for - The development of forward-thinking land-use planning (disaster resistant building codes, safety elements of general plans, Local Hazard Mitigation Plans/LHMPs, hazard area buy-out programs, mitigation measures to improve residential properties making them less prone to damage, and other smart strategies incorporated into recovery activities);

3) $ 4.5 Million for - Affordable rental housing activities; and,

4) $ 2 Million for administrative costs for #1–3.

HCD has administered funds through this program before, and plans to use their existing structure in order to expedite and simplify the process. Funds will be awarded on a first-come first-served basis for all applicants meeting the minimum thresholds.

The Program has set deadlines for:

1) Releasing the NOFA/application for funds on May 17, 2010;

2) Accepting applications no later than July 13, 2010; and,

3) Making award announcements within 60 days of application receipt.

COMMENTS

In addition to these funds, already received from the federal government, HCD points out that an additional $15 million may be available to the state.

Staff Recommendation: Approve with SRL regarding who receives the funds

ISSUE 2: INFILL INCENTIVE GRANT FUNDING AVAILABILITY

This issue was originally heard May 4, 2010.

As part of all affordable housing programs, the Department is required to do long-term monitoring to ensure the facilities remain affordable. They are required to review, document and approve tenant occupancies, conduct monitoring visits, provide ongoing technical assistance to project sponsors to resolve issues of non-compliance, and much more. These costs continue for the life of the affordability requirements, often 55 years.

For Bond projects, bond funds must be set aside for the purpose of funding these activities, or else the cost will be born by the General Fund. Because of this, a portion of housing bond funds are often left unspent, but are in reality being held in reserve for this purpose. Because requests are often received for the use of these set-aside funds, we asked HCD to do a thorough analysis of their ongoing needs, and report back to the legislature as to whether any funds may be available for appropriation. In their review of the Infill Incentive Grant Program under Proposition 1C, HCD informed this Committee that approximately $9.7 million could be utilized. After accounting for administrative costs that will be incurred, $9.2 million could be allocated to new projects.

COMMENTS

There are many potential ways to expend these available funds. The primary proposals that have been proposed are to 1) allocate these funds to projects already qualified for these funds, but who did not receive their full funding request because funds weren't available; or, 2) allocate the funds to CALReUSE, a program that assists with the redevelopment of underutilized properties with hazardous material contamination issues (brownfields).

The Committee may wish to discuss these options and what results they wish to achieve by putting these funds out to projects (ie: jobs, affordable units, etc.).

<u>The Committee may wish to ask the Department:</u>

1) Why have they not proposed spending these dollars? Dollars that could be creating jobs and affordable housing units.
2) Were there more requests for funds from this program than funding available? If so, could these funds simply be allocated to the next projects on the list, or would a new request for projects have to be processed?
3) Does the Department have a suggestion on the best use for these funds?

Staff Recommendation: Approve funding for CalReuse

ITEM 9350 TRAILER VEHICLE LICENSE FEE BACKFILL

This issue was originally heard May 4, 2010.

The Governor requests approval of trailer bill language to eliminate the General Fund backfill of $11.9 million for the trailer vehicle license fee apportionment to local governments. This budget item apportions revenue to cities and counties that lost Vehicle License Fee (VLF) revenue when the State converted from an un-laden weight system to a gross vehicle weight system for purposes of assessing VLF for commercial vehicles. This change conforms to the International Registration Plan, a reciprocity agreement among US states and Canada for payment of commercial license fees based on distance operated in each jurisdiction. This funding is deposited in the Local Revenue Fund to support local health and welfare programs.

COMMENTS

This backfill is associated with a state/local healthcare realignment implemented in 1991. The Governor had proposed a reduction in this apportionment in the 2008-09 budget; however, the Legislature rejected the reduction due to the association with the 1991 realignment. The realignment involved local governments assuming certain healthcare responsibilities from the state in exchange for specified revenues to support those programs. The Department of Finance indicates that they believe the $11.9 million is actually outside the realignment calculation. The LAO looked into the history of the issue and determined that these funds are deposited into realignment accounts. This VLF backfill used to be provided directly to cities and counties as well, but that backfill was eliminated in the 2003 budget act. The backfill to the realignment funds, however, was left in place. LAO now recommends approving this proposal in light of the current fiscal situation.

Staff Recommendation: Approve