

THE 2009-2010 STATE BUDGET
FLOOR REPORT



**2008-2009 SPECIAL SESSION BUDGET
ADJUSTMENT**

2009-2010 STATE BUDGET ACT

FLOOR REPORT

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Summary

This report summarizes the contents of the package of legislation that addresses California's fiscal crisis. The package includes reductions, revenues, and other solutions that provide ongoing solutions to the state's fiscal crisis as well as policy changes and reforms intending to provide immediate and long-term benefits to California's economy.

The total shortfall projected in the Governor's budget is \$39.56 billion (\$41.7 billion assuming a \$2.1 billion reserve.) With a combination of deep expenditure reductions and new revenues, this 17-month budget provides a sound fiscal blueprint for California to solve this \$39.56 billion fiscal shortfall.

How the \$39.56 billion gap is bridged:

- \$15.1 billion in expenditure reductions.
- \$14.4 billion in multi-year General Fund tax increases.
- \$11.4 billion in borrowing.

The final budget reserve is \$1.276 billion.

The chart below illustrates how these solutions are achieved over the 17-month period:

Summary of all Solutions

\$ Millions	FY 2008-09 Adjustments	FY 2009-10 Changes	Two Year Total
Expenditure Reductions	6,776.9	8,318.9	15,095.8
Revenues	1,807.5	12,580.4	14,387.9
Lottery	-	5,001.0	5,001.0
RAWS	5,918.2	-	5,918.2
Other Borrowing	268.2	164.4	432.6
Total	14,770.8	26,064.7	40,835.5

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Federal Revenue Trigger

The budget package does not rely on federal revenue to bridge the deficit, but does include a mechanism to restore some of the reductions and revenue provisions if the State receives federal revenue that offsets at least \$9.1 billion of General Fund costs. If the Director of Finance and the Treasurer determines that the federal funds have met this test by April 1, 2009, the following would occur:

- State would not issue \$5.9 billion in long-term RAWS.
- The following reductions would be restored:
 - SSI/SSP grant reduction of \$20 per month for individuals and \$35 per month for couples;
 - Elimination of optional Medi-Cal Benefits;
 - Adult dental
 - Acupuncture services
 - Audiology Services and speech therapy services
 - Chiropractic services
 - Optometric and optician services, including services provided by a fabricating optical laboratory
 - Podiatric services
 - Psychology services
 - Incontinence creams and washes
 - 10 percent reduction in public hospital rates;
 - Cap State participation in In-Home Supportive Services wages to \$9.50 per hour for wages plus \$0.60 an hour for benefits;
 - Prohibit any new IHSS clients to receive a Medi-Cal Share-of-Cost Buy-Out;
 - 4 percent reduction in CalWORKs grants;
 - \$100 million reduction to Higher Education Funding;
 - \$100 million reduction to court funding; and,
 - \$71.4 million for new judgeships.
- 5 percent surcharge on Personal Income Tax would be reduced to 2.5 percent.

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Constitutional Provisions and Ballot Propositions

The budget package includes five provisions that will require voter approval to be enacted. These provisions will appear on the ballot on May 19, 2009. These provisions are:

Spending Cap. ACA 1 / SCA 1 places a Constitutional provision on the ballot to cap spending by limiting the amount of revenue that can be appropriated for General Fund purposes. The provision requires that each year the Department of Finance forecast a revenue amount for the fiscal year that is derived from the last ten years of revenue growth amounts. Any revenue that exceeds this forecasted amount must be deposited in a new fund, the Budget Stabilization Fund, with the exception of revenue that is required for Proposition 98 purposes that exceed revenue growth.

The Budget Stabilization Fund can be used when State revenues are insufficient to cover prior year expenditures, adjusted for inflation and population. The funding in the Budget Stabilization Fund can also be used in cases of a declared emergency. Revenue accumulates in the fund until it equals 12.5 percent of General Fund revenue, at which point excess funding can be used for one-time expenditures. Up to \$5 billion of the amount deposited in this fund would be dedicated to retiring Deficit Recover Bonds over time.

In addition ACA 1 / SCA 1 requires that annually 1.5 percent of State General Fund revenue be deposited each year in the Budget Stabilization Fund and as of October 2011, 1.5 percent of revenue be deposited in the Supplemental Education Payment Account, which pays for the Proposition 98 obligations outlined in ACA 2 / SCA 2.

Proposition 98 Maintenance Factor Clarification. ACA 2 / SCA 2 places a Constitutional provision on the ballot that would require the State to increase annual school funding by \$9.3 billion in future years in lieu of any maintenance factors that could be required by Proposition 98. This additional funding would build up over several years, beginning in FY 2011-12. Funding for this provision would come from the Supplemental Education Payment Account specified in ACA 1 / SCA 1.

Funding provided by this provision would be allocated to school districts in the same manner as the revenue limit per unit of average daily attendance. \$200 million would be appropriated in the FY 2011-12 for Equalization funding.

Proposition 63 – Mental Health Services Act (MHSA). Subject to approval by the voters at a statewide election, utilizes MHSA funds in the amount of \$226.7 million in 2009-10 and up to \$234 million in 2010-11, if caseload adjustments require this marginal increase, to support the Early and Periodic Screening, Diagnosis, and Treatment (EPSDT) Program as administered by the State Department of Mental Health. Additional statutory changes are made in the Health Omnibus Trailer bill to improve the use and effectiveness of MHSA funds, consistent with the recommendations of recent audit reports.

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Proposition 10 – California Children and Families Act of 1998. Subject to approval by the voters at a statewide election, expands use of Prop. 10 funds for health and human services through state programs for children up to five years of age. Transfers Prop. 10 reserve funds of \$340 million on a one-time basis for these state program purposes, and additionally transfers \$268 million annually for five fiscal years starting with 2009-10 to be appropriated by the Legislature as part of the annual budget process. Further directs the use of Prop. 10 funds to provide direct health care services, human services, including services for at-risk families who are involved in the child welfare system, and direct early education services, including preschool and child care.

Lottery. Makes changes to clarify education appropriations, clarify the lottery director's authority relative to state employees, and require that lottery audits be posted on the internet. These changes would be placed before the voters, along with various sections of Chapter 764, Statutes of 2008 (AB 1654), the lottery modernization trailer bill for the Budget Act of 2008.

Summary of Revenue Solutions (Savings Over the 17-month Period)

The budget package includes \$14.4 billion in temporary General Fund tax increases.

These taxes result in the follow savings over the 17-month period:

- \$5.8 billion from a 1 cent increase to the State Sales and Use Tax, effective April 1, 2009 (\$1.2 billion in 2008-09 and \$4.6 billion in 2009-10). This tax increase is temporary and will sunset on June 30, 2012 if the voters approve the proposed Budget Stabilization constitutional amendment. If the voters reject the amendment, the rate increase will expire one year sooner, on June 30, 2011.
- \$3.3 billion from a 5 percent surtax on Personal Income Tax liabilities, effective starting in tax year 2009. This surcharge would apply through tax year 2012 if the voters approve the proposed Budget Stabilization constitutional amendment. If the voters reject the amendment, the surcharge will expire two years sooner—applying only to tax years 2009 and 2010. Furthermore, if the federal revenue trigger is activated, the surcharge rate will be cut in half (to 2.5 percent).
- \$1.4 billion from reducing the dependent credit allowed against the Personal Income Tax to the amount of the personal credit beginning in the 2009 tax year. The dependent credit reduction would apply through tax year 2012 if the voters approve the proposed Budget Stabilization constitutional amendment. If the voters reject the amendment, the dependent credit reduction will expire two years sooner, applying only to tax years 2009 and 2010. The personal credit applies to the taxpayer (and spouse), while the dependent may be claimed for children and

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other dependents. For 2008, the personal credit was \$99 and the dependent credit was \$309.

- \$1.7 billion from increasing the Vehicle License Fee (VLF) from the current rate of 0.65 percent to 1.15 percent, except for heavy vehicles. Revenue from the portion of the increase to 1 percent will be retained by the General Fund (\$121 million in 2008-09 and \$1.2 billion in 2009-10) and revenue from the additional increase of 0.15 percent will be transferred to a new special account dedicated to funding local public safety programs (\$82 million in 2008-09 and \$502 million in 2009-10). The VLF rate increase will become effective for registrations beginning May 19, 2009 and expire June 30, 2013 if the voters approve the proposed Budget Stabilization constitutional amendment. If the voters reject the amendment, the rate increase will expire two years sooner—June 30, 2011. The 0.15 percent rate component dedicated to local public safety would end earlier if the funds are spent for any other purpose.
- \$2.1 billion from a 12-cent per gallon increase in the excise tax on gasoline and diesel motor fuel, effective April 1, 2009. Of this amount, \$250 million in 2008-09 and \$1.8 billion in 2009-10 will offset General Fund debt service costs for transportation bonds. The fuel tax increase will expire June 30, 2013 if the voters approve the proposed Budget Stabilization constitutional amendment. If the voters reject the amendment, the increase expires two years sooner—on June 30, 2011.

Economic Stimulus Tax Provisions

- **Single Sales Factor Apportionment.** Allows most multi-state businesses to apportion income to California using only their percentage of sales in California as an alternative to using the current apportionment methodology, which averages a business's proportion of sales, property, and payroll in California (with the sales factor double-weighted). This provision will be effective starting in tax year 2011 and is permanent. This change will reduce California taxes for firms with significant employment and property in the state, but most of whose sales are outside the state. The estimated annual revenue loss will be approximately \$700 million, eventually growing to \$1.5 billion.
- **Film/TV Production Credit.** Provides a credit of 20 percent or up to 25 percent of the qualified production cost of qualified motion pictures or TV series that are produced in California. Producers must first apply to the California Film Commission for a credit allocation, and, upon completion receive a credit certificate from the commission. The commission would be limited to \$100 million of credit allocations in any fiscal year. Allocations would begin in 2009-10, and the first tax credits could be claimed for tax year 2011. A total of \$500 million of allocations would be available over five years.

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- **Small Business Hiring Credit.** Provides a credit of \$3,000 per full-time equivalent employee added by small businesses (20 employees or less). The credit will be available for the 2009 and 2010 tax years. The estimated revenue loss from this measure is approximately \$400 million over the two years combined.

Revenue Enactment Dates and Sunsets

The duration of each tax increase depends upon whether a spending cap provision passes on the ballot. The chart below outlines the dates when these taxes begin and end:

Timing and Triggers fro Tax Provisions

	Sunset		
	Begins	If Ballot Fails	If Ballot Passes
1-cent Sales Tax Increase	April 1, 2009	June 30, 2011	June 30, 2012
5 percent Personal Income Tax Surtax 5 (2.5% Surtax If Federal Funding Triggers is pulled)	Tax Year 2009	Tax Year 2010	Tax Year 2012
Personal Income Tax Dependent Credit Reduction	Tax Year 2009	Tax Year 2010	Tax Year 2012
Vehicle License Fee Increase from 0.65 percent to 1 percent	May 19, 2009	June 30, 2011	June 30, 2013
Vehicle License Fee 0.15 percent increase	May 19, 2009	June 30, 2011	June 30, 2013
\$.12 Excise Gas Tax	April 1, 2009	June 30, 2011	June 30, 2013

Summary of Expenditure Reductions (Savings over 17-month Period)

Education

- Does not suspend Proposition 98.
- \$8.6 billion in reductions including:
 - \$2.3 billion in programmatic reductions;
 - \$3.2 billion deferral (current-year to budget year);
 - \$1.1 billion counting current-year appropriation toward Prop. 98 “settle-up; and,
 - \$618 million Using Public Transit Account (rather than GF) for Home-to-School Transportation.

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- Programmatic reduction in K-12 split evenly between revenue limits and categorical programs (categorical cuts are across-the-board).
- No cuts to 4 of the 61 categoricals: Special Ed., Economic Impact Aid, K-3 Class Size Reduction, and School Lunches.
 - Of the remaining 57, across-the-board cuts of about 15% to each.
 - Districts given flexibility to move money among 43 of the 57.
 - 9 relatively small categoricals are excluded because of unique circumstances (federal requirements, unique populations they serve, etc.).
- Penalties temporarily relaxed for districts that exceed 20:1 in K-3 class size ratio.

Higher Education

- \$264.4 million from an across-the-board 10 percent reduction to CSU and UC funding.
- \$427.6 million in savings from eliminating the UC and CSU compact funding.
- \$95.7 million from reduced funding for retirement contributions.

Triggered Cuts, effective July 1, 2009—

Would not be enacted if more than \$9.1 billion federal funds are identified by April 1, 2009

- \$100 million in reductions divided equally between CSU and UC, offset by CalGrant increases, if segments increase fees.

Human Services

- \$79.1 million from suspending the July 2009 CalWORKs grant Cost of Living Adjustment.
- \$594.1 million from suspending the June 2010 SSI/SSP grant Cost of Living Adjustment and providing no pass-through of the federal SSI COLA.
- \$188.9 million from a 3 percent rate reduction and additional reductions for Developmental Disabilities Regional Center rates.
- \$40 million by suspending the CalWORKs Pay-for-Performance Incentive program.
- \$50.7 million from delaying certain technology projects.

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Triggered Cuts, effective July 1, 2009—Would not be enacted if more than \$9.1 billion federal funds are identified by April 1, 2009

- \$146.9 million from a 4 percent reduction to the CalWORKs grant levels.
- \$300 million from a \$20 reduction to SSI/SSP monthly grant levels (\$35 per month for couples).
- \$78 million from reduction in State participation in IHSS wages to \$9.50 per hour (plus \$.60 for benefits) and ends the Medi-Cal Share-of-Cost buy-out for IHSS clients prospectively.

Health

- \$24.7 million from suspending the 2009 Medi-Cal Administration cost of doing business increase.

Triggered Cuts, effective July 1, 2009—Would not be enacted if more than \$9.1 billion federal funds are identified by April 1, 2009

- \$183.6 million from eliminating certain optional Medi-Cal benefits and reducing public hospitals by 10 percent.

State Employee Compensation

- \$1.4 billion in savings from changes to employee compensation, overtime, and the impact of furloughs. Includes statutory language to achieve savings.

Courts

- \$146 million reduction equal to the amount of restoring one-time reductions and fund shifts included in the FY 2008-09 Budget Act and the annual growth factor the courts would normally receive.

Triggered Cuts, effective July 1, 2009—Would not be enacted if more than \$9.1 billion federal funds are identified by April 1, 2009

- \$100 million one-time unallocated cut to courts.
- \$71.4 million from rejecting the proposal to add 100 new judges.
- \$17.4 million related to the delayed implementation of the Guardianship Conservatorship Reform Act of 2006.

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Payments to Local Governments

- \$91 million from the deferral of 2009-10 mandate payments.
- \$502 million for public safety grants will be funded with a dedicated 0.15 percent increase to the VLF in lieu of General Fund.
- \$188.7 million from current year funding for public safety grants. This reduction is partially offset by the increase in VLF fees.

Transit and Transportation

- Reduces current year funding for transit by \$150 million and eliminates transit funding through 2013.
- Does not suspend Proposition 42.
- Directs the Department of Finance to redirect approximately \$100 million in tribal revenues to the General Fund in FY 08-09 and FY 09-10.
- Allows the Director of Finance to use funds transferred to the Transportation Debt Services Fund (TDSF) from the State Highway Account, approximately \$250 million in FY 2008-09 and \$1.8 billion in FY 2009-10 that will reimburse the General Fund to offset transportation-related general obligation debt.

Other Key Highlights of the Final Compromise (Savings over 17 month period)

Reserve

The budget includes a reserve of \$1,276 million, assuming the federal trigger is not pulled.

Borrowing

- **RAWS.** The budget proposes selling \$5.918 billion of Reimbursement Warrants (commonly known as RAWs) in July of 2009. While RANs must be repaid within the fiscal year in which they are sold, RAWs can be repaid in the subsequent fiscal year. Thus the budget proposes repaying the RAWs no later than June 30 of 2011. These RAWs would not be issued if federal revenue triggers is pulled because the state has received more than \$9.1 billion in federal funds to offset General Fund expenditures.

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- Lottery. Assumes \$5 billion provided by the securitization of future lottery revenues.
- Special Fund Loans and Transfers. An additional \$432.6 million in various special fund loans and transfers over the 18 month period.

Cash Management

- Defers county Social Service payments for July and August to September 2009, instead of the seven month deferral proposed by the Administration.
- Also defers some fuel excise tax allocations for one month in the current year, the July Apportionment payment for three months in the budget year and reschedules specified mandate payments from August to October.

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Attachment #1
General Fund Update
FY 08-09 and FY 09-10
(Assumes no federal stimulus revenue)

General Fund Update
(Dollars in Millions)

	<u>2008-09</u>	<u>2009-10</u>
Prior Year Balance	\$2,375.7	\$1,079.4
Revenues and Transfers	<u>\$89,397.1</u>	<u>\$97,546.7</u>
Total Resources Available	\$91,772.8	\$98,626.1
Non-98 Expenditures	\$55,657.8	\$55,747.0
Prop-98 Expenditures	\$35,035.6	\$40,523.6
Total Expenditures	\$90,693.4	\$96,270.6
Fund Balance	\$1,079.4	\$2,355.5
Budget Reserves:		
<i>Reserve for Liquidation of Encumbrances</i>	\$1,079.4	\$1,079.4
<i>Special Fund for Economic Uncertainties</i>	\$0.0	\$1,276.1
Total Reserve	\$0.0	\$1,276.1

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Attachment #2

**Detail of Total Solutions Contained in Budget Package
(Assuming federal revenue trigger is not pulled)**

(\$ in millions)	FY 08-09	FY 09-10	Total 17 Month
Expenditure Reductions			
Education	\$ 5,774.7	\$ 2,647.1	\$ 8,421.8
Higher Education	\$ 132.2	\$ 755.5	\$ 887.7
Health	\$ -	\$ 208.3	\$ 208.3
Human Services	\$ 104.4	\$ 2,171.7	\$ 2,276.1
Transportation	\$ 254.0	\$ 407.2	\$ 661.2
General Government/Other Solutions	\$ 511.6	\$ 2,129.1	\$ 2,640.7
Subtotal Reductions	\$ 6,776.9	\$ 8,318.9	\$ 15,095.8
Taxes and Revenue			
Sales Tax Increase of \$.01	\$ 1,202.7	\$ 4,553.1	\$ 5,755.8
Personal Income Tax 5 percent Surtax	\$ -	\$ 3,254.0	\$ 3,254.0
Vehicle License Fee Increase form 0.65 percent to 1.15 percent	\$ 374.8	\$ 1,721.3	\$ 2,096.1
Gasoline Excise Tax \$.12 per gallon	\$ 250.0	\$ 1,812.0	\$ 2,062.0
Reduce Dependent Credit to Personal Credit Amount Beginning in 2009 tax year	\$ -	\$ 1,440.0	\$ 1,440.0
Single Sales Factor Apportionment-- Beg. 1/1/2011	\$ -	\$ -	\$ -
Film Credit--Allocations begin 7/1/2011	\$ -	\$ -	\$ -
Hiring and Retention Credits--Effective 2009 and 2010 tax years	\$ (20.0)	\$ (200.0)	\$ (220.0)
Subtotal Revenue	\$ 1,807.5	\$ 12,580.4	\$ 14,387.9
Borrowing			
RAWS	\$ 5,918.2	\$ -	\$ 5,918.2
Lottery	\$ -	\$ 5,001.0	\$ 5,001.0
Other Borrowing	\$ 268.2	\$ 164.4	\$ 432.6
Subtotal Borrowing	\$ 6,186.4	\$ 5,165.4	\$ 11,351.8
Total All Solutions	\$ 14,770.8	\$ 26,064.7	\$ 40,835.5

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Attachment #3

**Detail of Total Solutions Contained in Budget Package
(Assuming federal revenue trigger is pulled)**

(\$ in millions)	FY 08-09	FY 09-10	Total 17 Month
Expenditure Reductions			
Education	\$ 5,774.7	\$ 2,647.1	\$ 8,421.8
Higher Education	\$ 132.2	\$ 655.5	\$ 787.7
Health	\$ -	\$ 24.7	\$ 24.7
Human Services	\$ 104.4	\$ 1,679.0	\$ 1,783.4
Transportation	\$ 254.0	\$ 407.2	\$ 661.2
General Government/Other Solutions	\$ 511.6	\$ 1,957.7	\$ 2,469.3
Subtotal Reductions	\$ 6,776.9	\$ 7,371.2	\$ 14,148.1
Taxes and Revenues			
Sales Tax Increase of \$.01	\$ 1,202.7	\$ 4,553.1	\$ 5,755.8
Personal Income Tax 2.5 percent Surtax	\$ -	\$ 1,627.0	\$ 1,627.0
Vehicle License Fee Increase form 0.65 percent to 1.15 percent	\$ 374.8	\$ 1,721.3	\$ 2,096.1
Gasoline Excise Tax \$.12 per gallon	\$ 250.0	\$ 1,812.0	\$ 2,062.0
Reduce Dependent Credit to Personal Credit Amount Beginning in 2009 tax year	\$ -	\$ 1,440.0	\$ 1,440.0
Single Sales Factor Apportionment	\$ -	\$ -	\$ -
Film Credit--Allocations begin 7/1/2011	\$ -	\$ -	\$ -
Hiring and Retention Credits--Effective 2009 and 2010 tax years	\$ (20.0)	\$ (200.0)	\$ (220.0)
Subtotal Revenue	\$ 1,807.5	\$ 10,953.4	\$ 12,760.9
Borrowing			
RAWS	\$ -	\$ -	\$ -
Lottery	\$ -	\$ 5,001.0	\$ 5,001.0
Other Borrowing	\$ 268.2	\$ 164.4	\$ 432.6
Subtotal Borrowing	\$ 268.2	\$ 5,165.4	\$ 5,433.6
Total Federal Funding		\$ 9,500.0	\$ 9,500.0
Total All Solutions	\$ 8,852.6	\$ 32,990.0	\$ 41,842.6