

**THE 2009-2010 STATE BUDGET
CONFERENCE REPORT**



Summary

Since the Governor signed the FY 09-10 budget into law on February 20, 2009, the continual decline of California's revenues have necessitated the Legislature to revisit the budget for the next fiscal year. The State faces dire consequences unless action is taken to address the impact of the worldwide economic recession and hinders upon our ability to access routine cash flow borrowing. This crisis has created a sense of urgency to make budgetary decisions to bridge our projected deficit as quickly as possible but also forces profound decisions that could shape the direction of California's public policy for generations.

The Legislature's version of the budget is intended to bridge this gap through difficult and deep reductions, some small additional targeted revenue increases, and limited borrowing. This version preserves the fabric of California's public policy for the future by providing our residents with leaner and more efficient services. This approach is steeped in the belief in the inherent value of the public institutions that have been built over the last century and strives to protect them in a diminished capacity as we weather this economic storm.

California's budget reflects the harsh reality of diminished resources forced by this recession and mirrors the difficult decisions millions of our residents must make in these lean times. However, this budget is shaped by several guiding principles that resonate throughout the actions that have been taken:

- ◆ **Bridges the Deficit:** The Legislature's plan bridges the projected deficit for both FY 09-10 and FY 10-11.
- ◆ **Provides a Healthy Reserve:** The budget provides a reserve of \$3.8 billion in the budget year.
- ◆ **Protects Institutions Californians Depend Upon:** Does not eliminate CalGrants, Healthy Families, State Parks, CalWORKs, Poison Control and long term care programs (Adult Day Health Care, Linkages, MSSP) targeted by the Governor.
- ◆ **Makes Deep Cuts in Every Area:** Over half of the total solution is through program reductions and savings in every policy area of state government.
- ◆ **Protects California's Access to Federal Funds:** Targets cuts to avoid losing \$3.7 billion of TANF block grant funding, and hundreds of millions of other funds from enhanced Medi-caid matching funds, Ryan White Act funding, and other federal grants and revenues that would have been lost if the Governor's proposal had been adopted.

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- ◆ **Seeks Targeted Revenue:** Includes tax increases, but focuses these increases at oil companies and cigarettes. Also includes some fee increases to support parks and protect Californians against fires, earthquakes, floods, and other natural disasters.
- ◆ **Eliminates Loopholes and Increases Compliance:** Repeals recent changes to tax law, enacted in the September budget package, to allow the carry back of Net Operating Losses during the prior two years and another provision that allows corporations to assign a portion of unused tax credits to an affiliated corporation. Also includes various compliance measures to insure payment of taxes owed to the state.
- ◆ **Protects Local Governments:** Does not suspend Proposition 1A in FY 09-10, protecting funding for cities and counties.

How the gap is bridged:

The Governor's May Revision included \$24 billion of solutions targeting an expected \$21.3 billion deficit for FY 2009-10. This deficit is the result of an additional projected shortfall of \$15.4 billion combined with the need to make up for \$5.8 billion of solutions that voters rejected during the May 19, 2009 special election. The Governor proposed a \$4.5 billion budget reserve.

Based upon preliminary estimates, the Legislature's budget provides \$23.2 billion of solutions to address the same deficit addressed by the Governor, resulting in a \$3.8 billion reserve.

	\$ Billions
Starting Reserve	2.0
Reduced May Revision Revenues	-12.5
Increased May Revision Expenditures	-3.2
Loss of Special Election Solutions	-5.8
Projected Budget Shortfall	-19.5
Legislature's Solutions	23.3
Final Reserve	3.8

How the Legislature's \$23.2 billion of solutions are constructed:

- ◆ Over \$11 billion in program reductions and cuts. These solutions are detailed, by policy area, reflecting the targeted cuts to achieve efficiency and to provide a leaner level of services, meanwhile, preserving California's public infrastructure.
- ◆ \$5 billion in revenue accelerations and fees, including the Governor's proposals to accelerate Personal Income Tax withholdings and Corporate Estimated

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Payments. Also includes a 3 percent independent contractor withholding requirement that is expected to generate \$2 billion one-time in FY 09-10 and ongoing compliance revenue of about \$130 million per year.

- ◆ \$1.9 billion in new taxes. Of this amount \$1 billion is from a new \$1.50 per pack cigarette tax and nearly \$830 million is achieved through a 9.9 percent oil severance tax.
- ◆ \$5 billion in other solutions, also detailed later in this report. This includes a \$1.2 billion one-time savings by deferring the June 30th State employee paycheck to July 1st and \$1 billion from the sale of a portion of the book of business for the State Compensation Insurance Fund.

The chart below compares the Legislature's solutions to the Governor's May Revision proposal:

Governor's Budget compared to the Conference Legislative Budget

Categories	Governor, by Category			Conference, by Category		
	2008-09 and prior	2009-10	Total	2008-09 and prior	2009-10	Total
Borrowing	0.0	1,982.0	1,982.0	0.0	0.0	0.0
Revenue Accelerations/Fees	0.0	2,758.9	2,758.9	0.0	5,041.4	5,041.4
Fund Shifts	0.0	2,098.2	2,098.2	0.0	2,561.0	2,561.0
Cuts Requiring Federal Action	0.0	1,000.0	1,000.0	0.0	1,000.0	1,000.0
Program Cuts and Savings	3,124.5	11,978.1	15,102.6	3,127.5	7,275.0	10,402.5
Revenue Collection/Enforcement	0.0	0.0	0.0	0.0	143.0	143.0
Taxes	0.0	0.0	0.0	0.0	1,910.0	1,910.0
Other	0.0	1,097.8	1,097.8	0.0	2,206.4	2,206.4
Total	3,124.5	20,915.0	24,039.5	3,127.5	20,136.8	23,264.3
Reserve			4,586.5			3,811.3

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Summary of Solutions by Area

Starting Problem		\$ Billions		-19.5				-19.5				
Summary		Governor's Plan						Legislative Plan				Dif w Gov
Area	2008-09	2009-10	Total	%	2008-09	2009-10	Total	%				
Education	1.4	3.8	5.2	21.6%	1.4	3.1	4.5	19.5%	-0.7			
Higher Education	1.4	1.7	3.1	12.9%	1.6	1.1	2.8	12.0%	-0.3			
Human Services	0.0	3.3	3.3	13.7%	0.0	0.8	0.8	3.6%	-2.5			
Health	0.0	2.4	2.4	10.0%	0.0	1.8	1.8	7.6%	-0.6			
Transportation	0.0	1.6	1.6	6.8%	0.0	2.1	2.1	9.2%	0.5			
Resources	0.0	0.4	0.4	1.7%	0.0	0.3	0.3	1.4%	-0.1			
Public Safety	0.0	1.4	1.4	5.7%	0.0	1.0	1.0	4.3%	-0.4			
Gen. Government	0.1	4.3	4.3	18.0%	0.1	3.5	3.5	15.3%	-0.8			
Taxes	0.0	0.0	0.0	0%	0.0	1.8	1.8	7.9%	1.8			
Other Revenues	0.0	2.3	2.3	9.6%	0.0	4.5	4.5	19.3%	2.2			
Total	2.9	21.2	24.1		3.1	20.1	23.3		-0.7			
Final Reserve			4.5				3.8		-0.7			

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Education

- ◆ Adopts \$5.5 billion in Proposition 98 reductions for K-14 education for 2008-09 and 2009-10 including:
- ◆ Reductions to school district and county offices of education revenue limits of \$1.3 billion in 2008-09 and about \$1.9 billion in 2009-10. These amounts include commensurate categorical reductions for Basic Aid Districts and a partial backfill of \$282 million for Home to School Transportation.
- ◆ Deferral of \$1.7 billion in revenue limit payments from 2009-10 to 2010-11.
- ◆ Authorizes the next installment of American Recovery and Reinvestment Act (ARRA) funds, including about \$500 million in anticipated Stabilization Funds, to backfill K-12 revenue limit reductions and related categorical reductions for Basic Aid Districts.
- ◆ Provides several additional program and funding flexibility options, beyond what was provided in February, as follows:
- ◆ Suspends the High School Exit Exam as a requirement for graduation, beginning in 2009-10;
- ◆ Authorizes local education agencies (LEAs) to reduce the number of instructional days to 175 per year through 2012-13;
- ◆ Suspends the requirement to purchase newly adopted instructional materials through 2012-13;
- ◆ Allows school districts to sell surplus property not purchased with state funds and use proceeds for general fund purposes for nearly three years;
- ◆ Suspends the remaining routine maintenance reserve requirement of one percent through 2012-13 for school districts that meet the facility requirements of the Williams settlement;
- ◆ Provides LEAs with access to additional, prior-year fund balances in 2009-10 beyond those provided in February. Additions include: Targeted Instructional Improvement Grants, Instructional Materials, California High School Exit Exam, Adult Education, ROC/P Facilities, and Deferred Maintenance.
- ◆ Lowers the minimum reserves for economic uncertainty to one-third of the currently required level for 2009-10 provided that LEAs make annual progress in fully restoring these reserves by 2011-12.

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- ◆ Prohibits the assignment of a negative or qualified fiscal certification due to a substantial loss of federal Stabilization Funds in 2011-12 and 2012-13.
- ◆ Adds statute that entitles school districts and community colleges to Proposition 98 maintenance factor in years when Test 1 is operative and lower than Test 2. These provisions would become effective July 1, 2011.

Child Care & Development (Proposition 98)

- ◆ Restores Child Care Services for CalWORKs families and families transitioning off CalWORKs.
- ◆ Rejects the Administration's proposal to increase family fees, which would have doubled fees in the case of the lowest income families.
- ◆ Denies the Administration's proposal to eliminate funding for ROC/P and Adult Education CalWORKs Services.
- ◆ Eliminates the Extended Day Care (Latchkey) program, but retains funding for services from July 1 until the start of school to ensure no children are immediately displaced, and adopts language to ensure that children receive priority placement in other subsidized programs.
- ◆ Holds constant the Regional Market Reimbursement rates at the 2005 levels, reimbursing up to a maximum of the 85th percentile.
- ◆ Appropriates \$110 million in American Recovery and Reinvestment Act federal stimulus funds in order to both hold program levels constant and increase child care slots in the voucher program.

Higher Education

- ◆ Includes \$2 billion in cuts to UC and CSU, which is the same level as proposed by the Governor. However, this proposal treats the UC and CSU equally and retains academic preparation programs.
- ◆ Achieves about \$700 million in savings from Community colleges, but offsets the reduction with an additional \$130 million in federal funds and \$80 million from restoring the fee increase to \$26 per unit.
- ◆ Provides the Community colleges Categorical Program "flexibility" by allowing funding from selected programs to be moved to better meet the needs of the districts.
- ◆ Rejects the Governor's cuts to Cal Grants, but does shift \$32 million of General Fund costs to the student aid fund.

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- ◆ Accepts Cal Grant programmatic reductions, beginning in 2010-11, by freezing income eligibility for Cal Grant A recipients and reducing the maximum Cal Grant award for all Private College award recipients by 5 percent.

Health

Department of Health Care Services

- ◆ Adopted the May Revise proposal to reduce funding for Medi-Cal by \$323.2 million General Fund in an unallocated cut.
- ◆ Adopted Budget Bill Language to reduce up to \$1 billion in General Fund upon receipt of increased federal funds for Medi-Cal.
- ◆ Rejected the May Revise proposal to reduce payments to private Disproportionate Share Hospitals by 10% (\$23.9 million) and reduced the Distressed Hospital Fund by \$23.9 million.
- ◆ Adopted several Medi-Cal pharmacy reforms included in the May Revise for a savings of approximately \$109 million General Fund.
- ◆ Adopted the May Revise proposal to increase long-term care fees for an additional \$18 million in revenue and reduced long-term care rates for a savings of \$75.7 million General Fund.
- ◆ Rejected the May Revise proposal to eliminate Adult Day Health Care (ADHC) benefits and adopted reforms to ADHC programs including a temporary 3-day cap, workgroup and minimum standards on medical necessity, on-site Treatment Authorization Requests, and anti-fraud measures for approximately \$25 million in General Fund savings.
- ◆ Rejected the May Revise proposal to eliminate all General Fund support for community clinic programs and reduced General Fund funding for these programs by approximately 30 percent – specifically: Rural Health Services (\$2.2 million); Seasonal Migratory Worker Program (\$1.9 million); Indian Health Program (\$1.5 million); and Expanded Access to Primary Care Program (\$4.5 million General Fund and \$3.9 million Proposition 99 funds).
- ◆ Rejected the May Revise Medi-Cal anti-fraud proposal and adopted a reduced version for a savings of \$35.9 million General Fund.

Department of Public Health

- ◆ Eliminated all \$18 million in General Fund dollars for the Immunization Program on a one-time basis.

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- ◆ Rejected the May Revise proposal to eliminate all General Fund support for domestic violence shelter programs and reduced General Fund support by 20%, from \$20.4 million to \$16.3 million.
- ◆ Rejected the May Revise proposal to eliminate all General Fund support for Maternal, Child and Adolescent Health (MCAH) programs and made the following reductions: Black Infant Health Program (\$900,000), Adolescent Family Life Program (\$1.75 million), Local County Maternal and Child Health Grants (\$2.1 million) and MCH state support (\$3.5 million).
- ◆ Adopted the May Revise proposal to suspend the Children's Dental Disease Prevention Program for a General Fund savings of \$2.9 million.
- ◆ Adopted the May Revise proposal to eliminate Proposition 99 funds for County Health Services for a savings of \$25.6 million.
- ◆ Adopted the May Revise proposal to reduce \$438,000 in Proposition 99 funds from the Asthma Program.
- ◆ Reduced General Fund support for the Alzheimer's Research Centers of California by 50%, from \$6.2 million to \$3.1 million.
- ◆ Rejected the May Revise proposal to reduce the AIDS Drug Assistance Program and other Office of AIDS Programs by \$80 million and reduced these programs achieving \$35 million General Fund savings.

Emergency Medical Services Authority

- ◆ Rejected the May Revise proposal to eliminate all General Fund support for the California Poison Control System and reduced General Fund funding by 50%, from \$5.9 million to \$2.95 million.

Managed Risk Medical Insurance Board

- ◆ Rejected the May Revise proposal to eliminate the Healthy Families Program and to reduce program eligibility from 250 to 200 percent of federal poverty.
- ◆ Reduced \$70 million in General Fund funding for the Healthy Families Program and adopted intent language that outside sources of funding support the program.
- ◆ Adopted the May Revise proposal to eliminate \$2.7 million in General Fund funding for Certified Application Assistance for the Medi-Cal/Healthy Families joint application.

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- ◆ Adopted the May Revise proposal to reduce \$4.9 million in Proposition 99 funding for the AIM program.
- ◆ Adopted the May Revise proposal to reduce \$6.6 million in Proposition 99 funding for the MRMIP program.
- ◆ Approves trailer bill language to effectuate the \$100 million General Fund reduction in the Department of Developmental Services budget to Regional Centers that was already included in the enacted 2009-10 budget. Additionally, approves placeholder trailer bill language and a list of proposed reductions to Regional Centers and Developmental Centers that is the product of an administration-led stakeholder work group process for additional savings totally \$234 million, of which \$80 million is attributable to obtaining additional federal funds.
- ◆ Approves May Revision proposals in the Department of Mental Health (DMH) to eliminate state support for health services other than federally required inpatient hospitalization and medication services for a General Fund reduction of \$64 million in the Mental Health Managed Care Program. Additionally eliminates state support for a General Fund savings of \$53.4 million for county programs developed in the Early and Periodic Screening, Diagnosis, and Treatment (EPSDT) Program using Mental Health Services Act funds that DMH contends increased services within EPSDT.
- ◆ Approves a May Revision proposal in DMH to increase fees by 18 percent for licensing and certification of Psychiatric Health Facilities and Mental Health Rehabilitation Centers. Approves new positions for Coleman v. Schwarzenegger bed capacity also in DMH.

Human Services

- ◆ Rejects the Governor's May Revision proposal to eliminate the CalWORKS program and instead cuts roughly \$240 million from the program, primarily from allowing local control to streamline services to meet current economic realities. This cut is greater than the Governor's original May Revision cut to CalWORKS. Rejects the grant reduction, safety net elimination, child-only elimination, and Self-Sufficiency Review requirements proposed in the May Revision.
- ◆ Rejects the May Revision proposals to eliminate virtually all funding for the In-Home Supportive Services Program and to reduce state participation in wages to the minimum wage, but includes savings of over \$100 million for various changes to the program. Increased the Share of Cost by 50 percent for all recipients receiving a state buyout, limit domestic and related services for recipients with FI rankings in these services below 4, with critical exemptions for high-need recipients, and eliminates services for those with FI scores below 2, again with critical exemptions for high-need and medically fragile recipients. These

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changes are effective September 1, 2009.

- ◆ Reduces SSI/SSP grants for couples to the federal minimum, pursuant to the Governor's proposal, and reduces grants for individuals by \$5 per month to save \$155 million on an annual basis. This reduction is effective October 1, 2009.
- ◆ Rejects the Governor's elimination of all General Fund support for the Multipurpose Senior Services Program and the Brown Bag program. Approves smaller reductions than proposed by the May Revision for the Linkages Program, or \$2.5 million General Fund from a local assistance budget of \$6 million, and the Alzheimer's Day Care Resource Centers, or \$1.2 million General Fund from a local assistance budget of \$2.84 million.
- ◆ Rejects the Governor's proposal to eliminate the Cash Assistance Program for Immigrants and the California Food Assistance Program. CAPI recipients' grants are aligned with those in SSI/SSP, so the CAPI share of this reduction is approximately \$1 million General Fund.
- ◆ Approves the May Revision proposed reduction of Drug Medi-Cal rates by 10 percent for a General Fund savings of \$8.8 million.
- ◆ Approves the May Revision proposal to eliminate General Fund, or \$90 million, for the Prop. 36 Substance Abuse and Crime Prevention Act and rejects the reduction proposal for the Offender Treatment Program, maintaining \$18 million General Fund. Federal funds are expected to be used to provide similar services to make up about half of the reduction that is sustained here.
- ◆ Approves the May Revision proposal to reduce rates by 10 percent for Group Homes, Foster Family Agencies, and Seriously Emotionally Disturbed for a savings of \$26.6 million General Fund without federal stimulus funds taken into account. Rejects the 10 percent reduction to the Supplemental Clothing Allowance and the Specialized Care Increment rates. Additionally rejects the May Revision proposed reduction to Child Welfare Services of \$70.7 million General Fund.
- ◆ Approves a reform for the Adoption Assistance Program to tie benefit levels to need, rather than automatically increase them by age, scoring savings of \$900,000 General Fund. Additionally, adopts a \$5 million General Fund reduction to the Transitional Housing Program-Plus programs on a one-time basis.
- ◆ Rejects the May Revision proposal to overhaul Community Care Licensing and eliminate all General Fund support, allowing for Family Child Care Homes to self-certify. Instead rescinds Subcommittees' previous action to approve positions for specific activities and retains a 10% fee increase to raise \$2.1 million in revenue to offset General Fund spending. Takes additional General Fund savings of \$5.3

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million as a result of additional federal stimulus funds.

- ◆ Eliminates state General Fund support for the Statewide Fingerprint Imaging System for a savings of \$7.7 million.
- ◆ Achieves \$300 million in savings by transferring additional CalWORKs grant costs to counties and providing additional revenues to pay for the new responsibilities.

Natural Resources and Environmental Protection

- ◆ Achieves approximately \$150 million in savings for CAL FIRE through various measures, including the Governor's Emergency Response Initiative and by establishing a State Responsibility Area fire fee.
- ◆ Approves the Governor's proposal to eliminate all General Funds for State Parks and instead fund parks through a \$15 annual "parks pass" fee added to car registration.
- ◆ Shifts \$5.2 million in baseline program support for the Office of Environmental Health Hazard and Assessment from the General Fund to various special funds.
- ◆ Approved Governor's proposal to apply a 4.8 percent surcharge on property insurance to fund emergency response programs, particularly offsetting General Fund expenditures for CalFIRE. The surcharge is projected to result in \$119 million in revenues in 2009-10.
- ◆ Approves an \$8 increase in fees for the Environmental License Plate and rejects cuts to various resources programs proposed by the administration
- ◆ Shifts \$4.4 million in baseline funding for the Department of Fish and Game to implement the Marine Life Protection Act from General Fund to Proposition 84 bond funds.
- ◆ Shifts on a one time basis \$30 million from the Fish and game Preservation Fund to replace General Fund funded activities at the Department of Fish and game.
- ◆ Rejected \$40 million (Special Funds) in the California Energy Commission's budget for hydrogen vehicle infrastructure.
- ◆ Approved \$5 million (Proposition 1E) for the state's share of the Pajaro River Flood Control Project.
- ◆ Approved 15 positions on a 2-year limited term basis to support the Department of Water Resources' Delta Habitat and Conveyance Program with budget bill language stating that no funding can be used for the construction of an alternative conveyance facility.

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- ◆ Approved Trailer Bill language to require that the Department of Pesticide Regulations enforce a 20 percent reduction in Volatile Organic Compound emissions in the Central Valley.
- ◆ Approved a transfer of the Pesticide Risk Assessment program from the Department of Pesticide Regulations to the Office of Environmental Health Hazard and Assessment.
- ◆ Increased the Underground Storage Tank Fee from \$0.014 to \$0.02 per gallon to raise approximately \$100 million in new revenue to fund the remediation of an additional 2,000 petroleum contaminated sites per year.
- ◆ Approved a complete moratorium on Suction Dredge Mining Permits issued by the Department of Fish and Game.

Public Safety

- ◆ Approved \$169 million reduction to the Judicial Branch, which will be absorbed (along with previous cuts to the Judicial Branch's budget) by such measures as one-day per month court closures, redirection of funds designated for court initiatives such as IT projects and construction, utilizing trial court reserves, and various increases to court fees.
- ◆ Approves total reduction solutions for the Department of Corrections and Rehabilitation (CDCR) of \$1.2 billion (which includes plan to deal with \$400 million vetoed from the budget passed in February) by commuting sentences of inmates who have been identified by the federal government for deportation, making various crimes that are currently punishable by either a misdemeanor or felony punishable by only a misdemeanor, providing the Secretary of the CDCR the discretion to place certain offenders under house arrest with GPS monitoring, reforming certain parole, credit, and sentencing policies, and reducing funding for inmate and parolee programs.
- ◆ Reduces \$20 million from the Department of Justice's (DOJ) budget by requiring the department to charge state and local law enforcement agencies lab fees for forensic services.
- ◆ Reduces \$20 million from DOJ's budget to reduce support for the department's Bureau of Narcotics Enforcement.

General Government

- ◆ Accepts the Governor's proposal to sell a portion of the State Compensation Insurance Fund (SCIF), which is expected to generate about \$1 billion in revenues.

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- ◆ Rejects the Governor's proposal to cut state employee compensation by another 5 percent (state employees are already experiencing a pay reduction of over 9 percent), but instead defers the June 30 pay check until July to generate a one-time savings estimated to be \$1.2 billion. This would be similar to the roughly \$4 billion of deferrals included in the Proposition 98 budget.
- ◆ Sweeps the Workforce Development Fund for \$6 million in General Fund revenue.
- ◆ Eliminates the Rural Health Care Equity Program for \$17.2 million in savings in 2009-10, with ongoing savings of approximately \$15 million.
- ◆ Scores \$100 million in savings from a 2 month holiday in PPO premiums for the state.
- ◆ Shifts \$40 million in General Fund costs for the Department of Industrial Relations to Special Funds funded through fees.
- ◆ Fully funds the "Citizens Redistricting Initiative" with the constitutionally required \$3 million allocation.
- ◆ Suspends funding of Capitol repairs for a one time savings of \$5 million.
- ◆ Approves a \$6.8 million General Fund loan, to be repaid within the 2009-10 fiscal year out of American Recovery and Reinvestment Act (ARRA) funding, to establish an ARRA Task Force and Inspector General within the Department of Finance.
- ◆ Approved \$3 million to provide funding necessary to meet the requirements of the Citizens Redistricting Initiative (Prop 11).
- ◆ Approves \$450,000 of Prop 63 funding to support mental health needs of the California National Guard.

State Controller

- ◆ Approves the May Revision increase of \$22.4 million (\$7.2 million General Fund) and 7 positions to implement the first year of a re-procurement of the Human Resources Management System (21st Century Project). This amount is in addition to \$9.6 million (General Fund) and 80.6 positions included as a placeholder in the 2009-10 enacted Budget. The former primary contractor for this information technology project was terminated for non-performance. Continuation of the project will make use of work already done and protect the state's claims against the former contractor.

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California Tax Credit Allocation Committee

- ◆ Approves May Revision increase of \$517 million of federal funds provided by the American Recovery and Reinvestment Act (ARRA) for tax credit programs to stimulate the production of affordable rental housing for low-income families and households. This amount is in addition to \$550 million in the current year, which was the subject of a recent Section 28.00 notification to the Legislature—making a total of \$1.1 billion of new tax credit financing available for low-income housing.

Franchise Tax Board

- ◆ Reduces by \$4.8 million and 69 positions to reflect the suspension of the Senior Citizens' and Disabled Homeowners and Renters Assistance Program. Funding for payments under the program was vetoed in the current year and was not included in the 2009 Budget Act. This reduction recognizes administrative savings due to program suspension.

State Board of Equalization

- ◆ Rejects a May Revision proposal to redirect \$965,000 (\$454,000 General Fund) savings resulting from increased e-filing to implement the Return Process Efficiencies information technology project because the return on this expenditure is relatively low in the context of the current budget shortfall.
- ◆ Reduces by \$285,000 (\$129,000 General Fund) to correct over budgeting for workstations.

Transportation

- ◆ Accepts the Governor's proposal to shift approximately \$1 billion of transportation revenues from local governments and instead use the funds to pay debt service on transportation bonds. The shift will be in place for two years instead of the Governor's permanent proposal. Proposition 1B funds will be accelerated to mitigate the impact of this cut on local governments.
- ◆ Accepts the Governor's proposal to shift approximately \$300 million of public transit funds from home-to-school transportation to repay public transportation bonds. Most of the funds for home-to-school transportation will be made up through Proposition 98 funds.
- ◆ Recognizes the updated revenue estimates of the February budget cut to public transportation, which provides over \$300 million in General Fund savings.
- ◆ Includes the LAO proposals to borrow \$134 million from the State Highway Account, which will be repaid within three fiscal years, and transfer \$70 million from the Motor Vehicle Account to the General Fund.

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- ◆ Suspends local airport grants for \$4 million in savings.
- ◆ Provides full funding to the High Speed Rail Authority (\$139 million) from Proposition 1A bond funds.

Local Government

- ◆ Rejects the Governor's proposal to borrow \$1.982 billion from local governments through the suspension of Proposition 1A (of 2004). Suspension would have diverted 8 percent of property tax revenues of cities, counties and special districts, which the state would have been required to repay with interest within three years.
- ◆ Generally adopts the Legislative Analyst's recommended revisions to the May Revision proposal to defer \$100.3 million of payments by suspending 32 local mandates. The conference action defers about \$99 million of payments. The conference action retains mandates requiring consistent voting procedures, including making absentee ballots available to all voters. It recasts two victims' rights mandates to reflect recent voter-approved measures (thereby eliminating future state payment obligations), retains the Open Meetings Act mandate and suspends the enhanced holding period under the animal adoption mandate (while retaining the prior 3-day holding requirement). Deferred payments will continue to be state obligations to local governments but will be deferred to a future time. Proposition 1A (of 2004) generally requires the Legislature to suspend mandates if valid claims from prior years are unpaid. For suspended mandates, local governments would not be required to comply with them in 2009-10 and would not be entitled to futures reimbursement for any costs that they choose to undertake that year. The \$58 million of funding that would remain is the amount needed to pay for various law-enforcement, tax administration and voting process mandates in order to avoid suspension of those mandates in 2009-10.
- ◆ Eliminates state subventions to local governments (primarily counties) under the Williamson Act Program for a General Fund savings of \$34.7 million. Under this longstanding program, the state backfills a portion of the revenue lost by local governments when they enter into contracts with land owners to limit property tax assessments for lands that are maintained as open space or agriculture lands.
- ◆ Redirects \$350 million annually in 2009-10 and 2010-11 from redevelopment agencies to schools in the vicinity of redevelopment project areas in order to offset state education costs. Also revises the provisions of the 2008-09 \$350 million redirection to be consistent with a recent court decision.

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Revenue

- Approved Governor's proposal to apply a 4.8 percent surcharge on property insurance to fund emergency response programs, particularly offsetting General Fund expenditures for CalFIRE. The surcharge is projected to result in \$119 million in revenues in 2009-10.

General Fund Tax Provisions

- ◆ Imposes a 9.9% tax on the gross value of each barrel extracted from California. This will increase revenues by \$830 million in 2009-10 and \$1.1 billion annually at current prices. Stripper wells are exempt from the tax whenever the average price of the oil they produce falls below \$30 per barrel. Effective October 1, 2009. Annual cost to Department of Conservation of about \$10 million to administer program. Revenue estimates assume current price of about \$60 per barrel for California crude oil.
- ◆ Repeals recent corporate tax breaks. Rolls back provisions enacted with the 2008-09 budget which (a) permit net operating losses incurred on or after January 1, 2011 to be carried back to offset earnings during the two prior years; and (b) allow corporations to assign all or a portion of their unused tax credits earned on or after January 1, 2008 to an affiliated corporation that is a member of the same combined reporting group. These actions result in a revenue increase of \$80 million in 2009-10 and rising annually thereafter to \$850 million by 2014-15.
- ◆ Increases cigarette taxes. Raises state cigarette excise taxes (currently \$.87 per pack) by an additional \$1.50, and imposes an equivalent increase for other tobacco products, effective October 1, 2009. This action increases revenue by \$1 billion in 2009-10 and \$1.2 billion in 2010-11.

General Fund Tax Enforcement and Acceleration Provisions

- ◆ Adopts Governor's May Revision proposal to accelerate \$610 million of Personal Income Tax and Corporation Tax revenues into 2009-10 by increasing the June (second) quarterly estimated payment from the current 30 percent of tax annual tax liability to 40 percent, beginning June 2010. The percentage due with the first quarterly estimated tax payment (due in April) is 30 percent, so the total amount due in the first half of the year would be 70 percent. However, the proposal would eliminate the third quarterly estimated payment (now 20 percent of annual liability) and increase the final quarterly payment (due in December) from the current 20 percent to 30 percent of annual tax liability.

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- ◆ Adopts the Governor's May Revision proposal to increase payroll withholding schedules by 10 percent, effective January 2010, to accelerate \$1.7 billion of Personal Income Tax revenue into 2009-10.
- ◆ Imposes withholding on payments to independent contractors. Effective January 1, 2010, extends income tax withholding to payments to independent contractors. Requires businesses and government entities to withhold 3 percent of payments for goods or services to independent contractors that currently require the filing of a federal 1099-MISC. The amount withheld would be credited against the state income tax liability of the contractor, as with wage withholding. This provision accelerates revenue and improves compliance, but does not change tax liabilities. The acceleration of collections increases revenue in 2009-10 by \$1.965 billion. Most of this gain is one-time—the increase is \$130 million in 2010-11, with minor losses in the following two years and subsequent annual revenue gains of \$300 million annually due to improved compliance and growth. The Franchise Tax Board (FTB) estimates implementation costs of \$25 million in 2009-10 and \$20 million annually thereafter.
- ◆ Extends sales tax "nexus." Requires out-of-state sellers, such as Amazon, that pay commissions to California firms or residents for sales referrals (often through a website link) to collect sales tax on their sales to California residents. This provision improves compliance, but does not change tax liability. Existing law requires Californians to pay equivalent use tax on these purchases, but compliance is low. Provisions reflect AB 178 (Skinner). The estimated General Fund revenue gain is \$48 million in 2009-10 and \$110 million annually, with additional revenue increases in local sales tax revenues.
- ◆ Authorizes the Financial Institutions Records Match (FIRM) Program. Requires financial institutions to perform quarterly matches of their account records with a file of tax delinquents provided by the Franchise Tax Board in order to identify assets that can be applied to pay the delinquent tax debts. This provision improves collections, but does not change tax liability. Provisions reflect SB 402 (Wolk) and will increase revenue by \$27 million in 2009-10, \$60 million in 2010-11 and about \$100 million annually thereafter.
- ◆ Requires non-retailers to register with Board of Equalization. Businesses that provide services will be required to register with the board and file annual use tax returns by April 15. The annual use tax return and payment applies to purchases on which sales tax was not collected (generally from out-of-state sellers), excluding vehicles, vessels and aircraft. This provision increases compliance, but does not change tax liabilities. Provisions reflect AB 711 (Calderon). The estimated General Fund revenue gain is \$28 million in 2009-10, \$57 million in 2010-11, and potentially larger amounts in future years as compliance improves. There also will be increased local sales and use tax revenues.
- ◆ Requires backup withholding. This generally conforms California to federal

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income tax backup-withholding rules related to various non-wage payments. Requires a business to withhold 7% of reportable payments of interest, dividends, compensation for services, and other forms of income if the IRS determines a condition for withholding exists (such as significant underreporting of non-wage payments by the recipient on tax returns). Provisions reflect AB 1848 (Ma) of 2008. This requirement results in an annual revenue gain from improved compliance of \$26 million.

- ◆ Authorizes suspension of licenses for delinquent taxpayers. Permits the state to suspend state occupational and professional licenses because of unpaid income tax liabilities. Allows taxpayer to avoid suspension by entering into an installment agreement with FTB. Provisions reflect AB 478 (Eng). This provision results in a revenue gain from improved collections of \$10 million in 2009-10 and up to \$20 million annually thereafter.
- ◆ Strengthens the definition of abusive tax shelters by defining a “potentially abusive tax avoidance transaction” as: (1) a tax shelter; (2) an undisclosed reportable transaction; (3) a listed transaction; (4) an entity, investment plan or arrangement, or other plan or arrangement that has the potential for tax avoidance or evasion, as identified by the Secretary of the Treasury or the Franchise Tax Board; (5) a gross misstatement; or (6) a transaction subject to the noneconomic substance transaction understatement penalty. FTB indicates that the strengthened definition will result in increased penalty assessments of \$4 million in 2009-10 and up to \$15 million annually thereafter. Provisions reflect SB 401 (Wolk).