



**FINAL SUMMARY OF
2008-2009 SPECIAL SESSION BUDGET
ADJUSTMENT
AND
2009-2010 STATE BUDGET ACT
As Chaptered February 20, 2009**

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THE 2009-2010 STATE BUDGET

FLOOR REPORT

Summary

On February 20, 2009, the Governor signed a series of bills into law that are intended to address California's fiscal crisis as well as help improve the State's economy. The 37-bill package includes reductions, revenues, and other answers 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. This report provides a summary of all of the elements of the finalized budget package, including the impact of vetoes.

The total shortfall projected in the Governor's budget was \$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:

- ◆ \$14.9 billion in expenditure reductions.
- ◆ \$12.5 billion in multi-year General Fund tax increases.
- ◆ \$7.8 billion of federal stimulus revenue that is conservatively estimated base amount for the current and budget year.
- ◆ \$5.4 billion in borrowing.
- ◆ \$957 million in Governor's vetoes, including \$510 million in vetoes to higher education that are anticipated to be backfilled with federal economic stimulus dollars.

The final budget reserve is \$2.049 billion.

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

Summary of all Solutions

\$ Millions	FY 2008-09 Solutions	FY 2009-10 Solutions	Two Year Total Solutions
Expenditure Reductions	\$6,725.4	\$8,129.1	\$14,854.5
Revenues	\$1,533.6	\$11,980	\$12,513.6
Lottery	-	\$5,001.0	\$5,001.0
Borrowing	\$268.2	\$134.4	\$402.6
Preliminary, conservative estimate of Federal Stimulus	\$2,730.0	\$5,048.8	\$7,880
Vetoes	-	\$957.0	\$957.0
Total	\$11,257.2	\$30,351.8	\$41,608.1

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Federal Revenue Trigger

- ◆ **\$10 billion trigger.** The budget includes \$947.7 million in spending cuts and \$1.8 billion in tax increases that will not take effect if it is determined that California will receive federal stimulus funds that offset General Fund spending by at least \$10 billion prior to the end of the 2009-10 budget year.

On or before April 1, 2009, the Director of Finance and the Treasurer will meet to determine whether they project federal legislation enacted by that point will result in reduced General Fund spending by the end of the 2009-10 budget year.

- ◆ **Governor's Preliminary Estimate.** The Governor's preliminary, conservative estimate is that California will receive \$8.4 billion in federal stimulus funds that will replace General Fund spending. These funds are assumed in the budget just signed and are counted toward the \$41.6 billion in solutions.
- ◆ **What counts toward the trigger?** It is important to note, that only certain federal stimulus funds can replace General Fund spending, such as FMAP and State Fiscal Stabilization. Funds specified for infrastructure, unemployment benefits, and tax relief do not count toward the \$10 billion trigger figure.
- ◆ **What taxes are subject to the trigger?** Fifty percent of the .25 percent rate surcharge on Personal Income Tax brackets will not take effect if the \$10 billion trigger level is achieved. This will lower the tax increase by \$1.8 billion.
- ◆ **What cuts are subject to the trigger?** The following cuts will not take effect if the \$10 billion trigger level is achieved, these cuts total \$947.7 million:
 - \$267.8 million by reducing SSI/SSP grant by \$20 per month for individuals and \$35 per month for couples;
 - \$183.6 million in Medi-Cal savings by reducing public hospital reimbursement rates by 10 percent and the elimination of certain optional benefits, listed below:
 - 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
 - \$78 million by capping state participation in In-Home Supportive Services wages to \$9.50 per hour for wages plus \$0.60 an hour for benefits to

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prohibit any new IHSS clients from receiving a Medi-Cal Share-of-Cost Buy-Out;

- \$146.9 million by reducing CalWORKs grants by four percent;
- \$100 million reduction to higher education funding;
- \$100 million reduction to court funding; and
- \$71.4 million by rejecting new judgeships.

Constitutional Provisions and Ballot Propositions

The budget package includes seven 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 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 Recovery 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 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.

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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.

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.

Open Primary. SCA 4 would require primaries to be open to voters from all party registrations for congressional and state-elected offices.

Legislative Salary Increases. SCA 8 would not allow legislative or constitutional officer salaries to be increased in years where the state faced a projected fiscal deficit.

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Summary of Revenue Provisions

General Fund Solution Tax Provisions

The budget package includes \$12.9 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.
- ◆ \$3.7 billion from a .25 percent rate surcharge on Personal Income Tax brackets, 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 .125 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 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. The budget package also includes a bill that unbundles the VLF taxes charged by this increase from rental car rates.

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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.
- ◆ **Homebuyer's Credit.** Provides \$100 million one-time for a homebuyers credit that would pay up to \$10,000 for newly constructed homes.
- ◆ **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.

	Begins	Sunset 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 (PIT) Surcharge .25 (.125% Surcharge If Federal Funding Triggers is pulled)	Tax Year 2009	Tax Year 2010	Tax Year 2012
PIT Dependent Credit Reduction	Tax Year 2009	Tax Year 2010	Tax Year 2012
VLF Increase from 0.65 percent to 1.15 percent	May 19, 2009	June 30, 2011	June 30, 2013

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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.
- ◆ 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% will occur to each.
 - Districts given flexibility to move money among 43 of the 57.
 - Nine 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 \$10 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.

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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.

Triggered Cuts, effective July 1, 2009—Would not be enacted if more than \$10 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 \$10 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.

Controller's Office

- ◆ \$1 million reduction to State Controllers office. This reduction includes language that prohibits the controller from expending State funds on modular office furniture.

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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 \$10 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.

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.

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Summary of Vetoes:

The Governor made \$957 million General Fund vetoes from the FY 2009-10 budget including:

- ◆ \$400 million from Corrections and Rehabilitation, to reflect savings expected to be achieved as a result of various reforms and actions implemented by the Secretary of the California Department of Corrections and Rehabilitation.
- ◆ \$255 million from CSU, to be backfilled with federal stimulus revenues.
- ◆ \$255 million from UC, to be backfilled with federal stimulus revenues.
- ◆ The following vetoes were intended to reflect personal services savings to constitutional officer budgets which reflects the state employee compensation savings:
 - \$23.7 million from the Department of Justice
 - \$9.944 million from the Board of Equalization
 - \$5.27 million from the Department of Education
 - \$1.3 million from the Secretary of State
 - \$578,000 from the State Treasurer
- ◆ \$1.7 million from the Lieutenant Governor's office budget.
- ◆ \$24 million of special funds vetoed from the Department of Insurance budget for to achieve the corresponding savings.
- ◆ A technical veto of \$275 million special fund in the Department of Transportation that would have only been available if excise fuel taxes were increased.

Other Key Highlights of the Final Compromise

Reserve

The budget includes a reserve of \$2,045 million, assuming the federal trigger is not pulled.

Borrowing

- ◆ Lottery. Assumes \$5 billion provided by the securitization of future lottery revenues.
- ◆ Special Fund Loans and Transfers. An additional \$432.6 million in various

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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**

**General Fund Update
(Dollars in Millions)**

	2008-09	2009-10
Prior Year Balance	\$2,375.7	-\$2,434.8
Revenues and Transfers	<u>\$89,373.2</u>	<u>\$97,728.5</u>
Total Resources Available	\$91,748.9	\$95,293.7
Non-98 Expenditures	\$59,148.1	\$51,641.7
Prop-98 Expenditures	\$35,035.6	\$40,523.6
Total Expenditures	\$94,183.7	\$92,165.3
Fund Balance	-\$2,434.8	\$3,128.4
Budget Reserves:		
<i>Reserve for Liquidation of Encumbrances</i>	\$1,079.4	\$1,079.4
Final Reserve	-\$3,514.2	\$2,049.0

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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	\$459.8	\$1,939.3	\$2,399.1
<i>Subtotal Reductions</i>	\$6,725.1	\$8,129.1	\$14,854.2
Federal Revenue			
Federal Revenue	\$2,730.3	\$5,048.8	\$7,779.1
<i>Subtotal Federal Revenue</i>	\$2,730.3	\$5,048.8	\$7,779.1
Taxes			
Sales Tax Increase of \$.01	\$1,202.7	\$4,553.1	\$5,755.8
Personal Income Tax .25 percent rate Surcharge	-	\$3,658.0	\$3,658.0
Vehicle License Fee Increase form 0.65 percent to 1.15 percent	\$345.9	\$1,692.4	\$2,038.3
Reduce Dependent Credit to Personal Credit Amount Beginning in 2009 tax year	\$ -	\$1,440.0	\$1,440.0
Single Sales Factor Apportionment-- Beginning 1/1/2011	-	-	-
Film Credit--Allocations begin 7/1/2011	-	-	-
Hiring and Retention Credits--Effective 2009 and 2010 tax years	\$ (15.0)	\$ (330.0)	\$ (345.0)
<i>Subtotal Taxes</i>	\$1,533.6	\$11,013.5	\$12,547.1
Borrowing			
Lottery	-	\$5,001.0	\$5,001.0
Other Borrowing	\$268.2	\$134.4	\$402.6
<i>Subtotal Borrowing</i>	\$268.2	\$5,135.4	\$5,403.6
Veto	-	\$957	\$957
Total All Solutions	\$11,257.2	\$30,350.8	\$41,608.0

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Attachment #3 The February 2009 Budget Package Enacted Bills

3rd Extraordinary Session Bills

SB 1 (Ducheny)	FY 09-10 Budget Bill
SB 2 (Ducheny)	Changes to FY 08-09 Budget Bill
AB 3 (Evans)	Tax Changes to VLF, Income Tax, and Sales Tax
SB 4 (Ducheny)	Education Trailer Bill
AB 5 (Evans)	Health
SB 6 (Ducheny)	Human Services
SB 7 (Ducheny)	Transportation Finance
SB 8 (Ducheny)	State and Local Government
SB 9 (Ducheny)	Proposition 10: use of funds: services for children
SB 10 (Ducheny)	The Mental Health Services Act: Proposition 63 amendments
AB 11 (Evans)	Special Election
AB 12 (Evans)	California State Lottery
AB 13 (Evans)	State and Local Government: cash management
SB 14 (Ducheny)	Prison facilities: construction.
AB 15 (Krekorian)	Tax Credits: apportionment: sales factor
SB 15 (Calderon & Florez)	Tax Credits: apportionment: sales factor
AB 16 (Evans)	State Finance
AB 17 (Evans)	California Children and Families Act
SB 19 (Ducheny)	Elections
SB 20 (Maldonado)	State Controller
ACA 1 (Niello & Adams)	State Finance
ACA 2 (Bass)	Education Finance

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2nd Extraordinary Session Bills

SB 3 (Florez & Denham)	Air Pollution: grants: farm equipment (Carl Moyer)
SB 4 (Cogdill)	Public Contract: design build: public private partnerships
AB 5 (Gaines)	Employment: alternative workweek
AB 7 (Lieu)	Residential Mortgage Loans: foreclosure
SB 7 (Corbett)	Residential Mortgage Loans: foreclosure
AB 8 (Nestande)	State Government
SB 9 (Padilla)	Public Works: labor compliance
SB 10 (Oropeza)	Vehicle License Fee
SB 11 (Steinberg)	Judges: employment benefits
SB 12 (Steinberg)	Court Facilities Financing
SB 15 (Ashburn)	Personal Income Taxes: credit: principal residence
SB 16 (Ashburn)	Horse Racing: license fees

Regular Session Bills

SB 6 (Maldonado)	Elections: primaries
SCA 4 (Maldonado)	Elections: open primaries
SCA 8 (Maldonado)	State officer salary increases