

Overview

On Friday, January 9, 2004, Governor Schwarzenegger unveiled his proposed budget for the 2004-05 fiscal year.

The proposed budget is now in the hands of the Legislature to review, analyze, debate, revise, and return to the Governor. Assembly Bill 1800 (Oropeza) and Senate Bill 1095 (Chesbro) will serve as the budget bills for the Assembly and the Senate, respectively. Multiple "Trailer Bills" will also be introduced in both houses as vehicles for statutory changes necessary to implement the final budget agreement.

California continues to face significant budget challenges. Ongoing tax reductions and expenditure increases during the late 1990's left the state in a critical budget situation as booming revenues during the late 1990's turned into record revenue decreases when the economy soured.

In total, the Governor proposes \$16.2 billion in budget solutions to balance the budget for 2004-05. The solutions contain a mix of one-time and on-going borrowing, fund shifts, and spending reductions. Central elements of the Governor's proposed solution include shifting \$1.3 billion of property taxes from local governments, suspending and deferring \$2.9 billion in Proposition 98 funds, and increasing the reliance on borrowing with the \$15 billion bond the March 2, 2004 ballot.

However, according the Legislative Analyst, the Governor's plan leaves a 2005-06 deficit of approximately \$6 billion.

The Preliminary Review provides an in-depth look at the entire proposed budget. The issues discussed in this report will be followed up throughout the entire budget cycle with final decisions being contained in the budget passed by the Legislature.

The rest of this section includes information on the General Fund summary, detailed information on how the Governor proposes to close the gap, and projected revenues and proposed expenditures.

General Fund Summary

The proposed budget includes General Fund revenues for 2004-05 to be \$76.4 billion, an increase of \$1.8 billion above the 2003-04 year, and proposes General Fund expenditures for 2004-05 to be \$79.1 billion, an increase of \$4.1 billion above the 2003-04 year. The Governor's proposed budget projects a final reserve of \$635 million.

| 2004-05 Governor's Budget General Fund Budget Summary (in millions) | | |
|--|-----------------|-----------------|
| | 2003-04 | 2004-05 |
| Prior Year Balance | \$1,608 | \$1,219 |
| Revenues and Transfers | \$74,627 | \$76,407 |
| Bond Proceeds | 3,012 | -- |
| Total Resources Available | \$79,247 | \$77,626 |
| Expenditures | \$75,016 | \$79,074 |
| Transfer of Bond Revenues from 2003-04 to 2004-05 | \$3,012 | -\$3,012 |
| Total Expenditures | \$78,028 | \$76,062 |
| Fund Balance | \$1,219 | \$1,564 |
| Budget Reserves: | | |
| Reserve for Liquidation of Encumbrances | \$929 | \$929 |
| Special Fund for Economic Uncertainties | \$290 | \$635 |

Closing the General Fund Gap

As a result of continuing budget challenges, the Governor's proposed budget closes a \$16.2 billion General Fund gap. Many of the proposals to close the gap are the primary budget proposals that will get the most attention of the Legislature throughout the budget process. Each section of the Preliminary Review contains discussions of these proposals. A complete list of the General Fund solutions is provided in Appendix

The following chart illustrates how the \$16.2 billion of solutions are allocated by solution type, such as spending reductions, increased borrowing, and special fund transfers.

| Governor's Proposed \$16.2 Billion General Fund Gap Solution (in millions) | | | | | |
|---|----------------|------------------|-------------------|-------------------|-------------|
| Solution Type | 2002-03 | 2003-04 | 2004-05 | Total | % |
| Spending Reductions | \$161.8 | \$1,158.0 | \$4,618.9 | \$5,938.7 | 36.6% |
| Fund Shifts | 0 | 41.1 | 1,043.6 | 1,084.7 | 6.7 |
| Cost Avoidance: | | | | | |
| ◆ Suspend Prop 42 | 0 | 0 | 947.2 | 947.2 | 5.8 |
| ◆ Re-base (suspend) Prop 98 | 517.8 | 448.4 | 1,910.3 | 2,976.5 | 17.7 |
| ◆ Other | 0 | 609 | 106.5 | 107.1 | 0.7 |
| Economic Recovery Bonds | -1,433 | 0 | 3,014.0 | 1,578 | 9.7 |
| Debt Service Savings | 0 | 0 | 1,256.0 | 1,256.0 | 7.7 |
| Pension Obligation Bonds | 0 | 0 | 949.7 | 949.7 | 5.9 |
| Transfers/Other Revenues | 0 | 771.1 | 475.6 | 1,246.6 | 7.7 |
| Loans / Borrowing | 0 | 203.8 | 45.0 | 248.8 | 1.5 |
| Total | \$753.8 | \$2,623.0 | \$14,364.7 | \$16,233.9 | 100% |

The proposed General Fund solutions affect every area of the budget. However, the solutions fall most significantly with reductions to Health and Human Services being 19.4 percent of the solutions and the suspension and deferrals of K-14 Proposition 98 funding being 18.3 percent of the total solutions. Other areas of the budget containing significant portions of the proposed solutions are increased deficit recovery bonds, the suspension of Proposition 42 which reduces funding for transportation, and a \$1.3 billion reduction to local governments.

The following chart identifies how the General Fund solutions are allocated among the state agencies.

| General Fund Solutions By Agency (in millions) | | | | | |
|---|----------------|------------------|-------------------|-------------------|-------------|
| Agency | 2002-03 | 2003-04 | 2004-05 | Total | % |
| Legislative, Judicial, Executive | \$0.0 | \$0.0 | \$114.0 | \$114.0 | .7% |
| State and Consumer Services | 0 | 18.6 | 14.9 | 33.5 | .2 |
| Business, Transportation, and Housing | 0 | 886.8 | 999.3 | 1,886.1 | 11.6 |
| Technology, Trade, and Commerce | 0 | 6.6 | 0 | 6.6 | .0 |
| Resources | 132.2 | 8.7 | 47.3 | 188.2 | 1.2 |
| Environmental Protection | 0 | 0 | 9.3 | 9.3 | .1 |
| Health and Human Services: | 29.6 | 413.9 | 2,700.1 | 3,143.6 | 19.4 |
| <i>Medi-Cal</i> | 8.2 | 230.0 | 880.5 | 1,118.7 | 6.9 |
| <i>Public Health</i> | 0 | 4.4 | 9.7 | 14.2 | .1 |
| <i>Managed Risk Medical Insurance Board</i> | 2.3 | 0 | 32.1 | 34.4 | .2 |
| <i>CalWORKS</i> | 0 | 0 | 787.4 | 787.4 | 4.9 |
| <i>SSI/SSP</i> | 0 | 0 | 134.7 | 134.7 | .8 |
| <i>In-Home Supportive Services</i> | 0 | 129.2 | 126.5 | 255.7 | 1.6 |
| ➤ <i>Developmental Services</i> | 2.7 | 0 | 155.4 | 158.1 | 1.0 |
| ➤ <i>Mental Health</i> | 1.4 | .4 | 37.6 | 39.3 | .2 |
| ➤ <i>Other Health and Human Services</i> | 15.0 | 49.9 | 536.2 | 601.1 | 3.7 |
| Youth and Adult Correctional | 0 | 0 | 438.0 | 438.0 | 2.7 |
| K-12 Non Prop 98 | 0 | .6 | 0 | .6 | 0.0 |
| Local Government (ERAF) | 0 | 0 | 1,336.0 | 1,336.0 | 8.2 |
| K-14 Education (Prop 98 Suspension) | 517.8 | 448.4 | 2,004.0 | 2,970.3 | 18.3 |
| Higher Education | 0 | 157.7 | 728.8 | 886.5 | 5.5 |
| Labor Agency | 0 | .8 | .8 | 1.6 | 0.0 |
| General Government | 0 | 680.9 | 1,704.3 | 2,385.2 | 14.7 |
| Economic Recovery Bonds | -1,433.4 | 0 | 3,012.0 | 1,578.6 | 9.7 |
| Debt Service Savings | 0 | 0 | 1,256.0 | 1,256.0 | 7.7 |
| Total | \$753.8 | \$2,623.0 | \$14,364.7 | \$16,233.9 | 100% |

Revenues

The Governor's proposed budget projects General Fund revenues to be \$76.4 billion in 2004-05, an increase of \$1.8 billion over revised current year projections. The table below displays the composition of General Fund revenues.

| Projected 2004-05 General Fund Revenue Sources (in millions) | |
|---|-----------------|
| Personal Income Tax (PIT) | \$38,043 |
| Sales and Use Tax | 25,022 |
| Bank and Corporation Tax | 7,609 |
| Motor Vehicle Fees | 16 |
| Insurance Tax | 2,078 |
| Estate Tax | 136 |
| Liquor Tax | 294 |
| Tobacco Taxes | 115 |
| All Other | 3,094 |
| Totals | \$76,407 |

Expenditures

The Governor's budget proposes to appropriate a total of \$102.2 in General Funds (\$79.1 billion), Special Funds (\$21.1 billion) and Bond Funds (\$1.9 billion).

| Proposed Expenditures By Fund (in millions) | | | | |
|--|---------------------|----------------------|-------------------|-----------------|
| | General Fund | Special Funds | Bond Funds | Total |
| K-12 Education | \$30,317 | \$59 | \$36 | \$30,412 |
| Higher Education | 8,694 | 1,200 | 1,567 | 11,461 |
| Health and Welfare | 24,600 | 4,068 | 2 | 28,670 |
| Youth and Adult Corrections | 5,732 | 4 | -- | 5,736 |
| Resources | 939 | 1,685 | 125 | 2,749 |
| Environmental Protection | 70 | 764 | 12 | 846 |
| Local Government Subventions | 260 | 2,311 | -- | 2,571 |
| Tax Relief | 4,730 | -- | -- | 4,730 |
| State and Consumer Services | 478 | 559 | 13 | 1,050 |
| Business, Transportation and Housing | 375 | 5,528 | 148 | 6,051 |
| Courts | 1,569 | 1,121 | -- | 2,690 |
| Other | -1,702 | 3,845 | 35 | 2,158 |
| Total | \$76,062 | \$21,144 | \$1,938 | \$99,144 |