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To: Chairs of the Board
CSAC Board of Directors
County Administrative Officers

From: Paul McIntosh, CSAC Executive Director
Jim Wiltshire, CSAC Deputy Director
Jean Kinney Hurst, CSAC Legislative Representative

Re: *Highlights of the 2009-10 Proposed State Budget*

As we reported last week, Finance Director Mike Genest released the Governor's 2009-10 Proposed Budget on December 31, 2008. Citing the unprecedented budget crisis, the Governor reportedly directed the Department of Finance (DOF) to prepare and release the proposal early, indicating that the state could not wait for the customary January 10 deadline.

The state's General Fund deficit through the end of the 2009-10 fiscal year is \$41.6 billion.

The Governor's proposal intends to resolve that deficit by adding \$4.6 billion in new solutions to proposals previously released during the November Special Session. Director Genest emphasized that the value of these solutions erodes dramatically if not enacted immediately. Please note that most of the solutions were included in the Governor's November Special Session proposal and are summarized in [CSAC's Budget Action Bulletin Special Session No. 1](#). This summary will review new proposals in the Governor's plan, as well as several of the previously proposed budget solutions.

It remains unclear how this proposal will affect the ongoing negotiations between the Governor and Democratic leadership about the budget package approved in December. One thing is abundantly clear: without immediate action, the state will meet fiscal disaster.

Origins of the Deficit

The summary of the proposed budget identifies two sources for the extraordinary budget gap. The first is the "massive and unsustainable new spending commitments" the state made in the midst of a revenue surge whose source was capital gains revenues from the dot-com boom. This structural deficit was never fixed, as the state relied instead upon one-time measures — such as borrowing — each year.

The second source of the state's current shortfall is the "dramatic decline in revenues that has resulted from the current recession." DOF now estimates a year-over-year revenue decline of \$15.1 billion, or 14.7 percent, for the current fiscal year.

The Cash Situation is Dire

The Governor notes that the state will run out of cash in March even if the Legislature were to enact all of the proposed special session solutions by the beginning of February. Therefore, the state will have to

defer some payments, or else begin issuing registered warrants. While there is little detail to this component of the package, we will continue to educate the Administration and Legislature as to the difficulties of deferrals at the local level.

Last week, State Controller John Chiang released his [letter](#) to state agencies notifying them of the process for issuing registered warrants (commonly referred to as IOUs). Please note that among the [list](#) of direct deposit payments that would be impacted if the State Controller's Office is forced to issue registered warrants are Citizens' Option for Public Safety (COPS) and Juvenile Justice Crime Prevention Act (JJCPA) grants, Williamson Act subventions, reimbursement for the Homeowners Property Tax Exemption, and certain Medi-Cal payments from the Department of Health Services.

We understand that the State Controller's Office will have more information about the process for issuing registered warrants after it has received additional cash flow information later this week. We hope to know more about the impacts on counties next week and will share this information as soon as we are able.

Revenue Anticipation Warrants

Perhaps the most notable component of the new budget proposal is the proposed issuance of Revenue Anticipation Warrants (RAWs) in July 2009. The Governor indicates that the state will not be able to manage its cash flow in the budget year 2009-10, without a "substantial infusion of cash." The Governor proposes selling over \$4.5 billion of RAWs in July of 2009. RAWs differ from Revenue Anticipation Notes (RANs) in that they need not be paid back until the next fiscal year, so the state would have until June 30, 2011 to repay this loan.

Selling RAWs requires a return to some level of stability in the financial markets, enactment of a balanced budget, and establishment of a plausible repayment plan, including triggers for revenue increases or program reductions to protect investors should the state find itself otherwise unable to make the required payment. Director Genest stressed that the RAW issuance is a last resort in times of fiscal crisis, but has been utilized as a tool in previous economic emergencies.

By the Numbers

The following charts show the "workload budget" (the budget with no policy changes), the budget with all of the Governor's proposed solutions, a summary of all proposed solutions by category, and a summary of proposed solutions by revenue and expenditure category.

**2009-10 Governor's Budget
General Fund Budget Summary
Workload Budget
(dollars in millions)**

	2008-09	2009-10
Prior Year Balance	\$3,326	-\$13,692
Revenues and Transfers	\$87,471	\$86,300
Total Resources Available	\$90,797	\$72,608
Non-Proposition 98 Expenditures	\$62,109	\$68,708
Proposition 98 Expenditures	\$42,380	\$42,381
Total Expenditures	\$104,489	\$111,089
Fund Balance	-\$13,692	-\$38,481
Reserve for Liquidation of Encumbrances	\$1,079	\$1,079
Special Fund for Economic Uncertainties	-\$14,771	-\$39,560
Budget Stabilization Account	\$0	\$0
Total Available Reserve	-\$14,771	-\$39,560
Target Reserve		\$2,000
Budget Gap		-\$41,560

**2009-10 Governor's Budget
General Fund Budget Summary
With All Proposed Budget Solutions**
(dollars in millions)

	2008-09	2009-10
Prior Year Balance	\$2,375	\$1,079
Revenues and Transfers	\$91,117	\$97,708
Total Resources Available	\$93,492	\$98,787
Non-Proposition 98 Expenditures	\$56,630	\$55,036
Proposition 98 Expenditures	\$35,783	\$40,488
Total Expenditures	\$92,413	\$95,524
Fund Balance	\$1,079	\$3,263
Reserve for Liquidation of Encumbrances	\$1,079	\$1,079
Special Fund for Economic Uncertainties		\$2,184
Budget Stabilization Account	\$0	\$0
Total Available Reserve	\$0	\$2,184

Proposed Budget Solutions
(dollars in millions)

	Dec. 19 Special Session Proposals		Additional Special Session Proposals		Proposals to be Enacted by July 1*		Total	
Expenditure Reductions	\$9,811	44%	\$4,049	87%	\$3,567	24%	\$17,427	42%
Revenues	\$12,505	56%	\$236	5%	\$1,545	10%	\$14,286	34%
Lottery	\$0	0%	\$0	0%	\$5,001	34%	\$5,001	12%
Borrowing	\$0	0%	\$358	8%	\$0	0%	\$358	1%
RAWs	\$0	0%	\$0	0%	\$4,673	32%	\$4,673	11%
Total	\$22,316		\$4,643		\$14,786		\$41,745	

*Includes minor policy issues of \$72m (\$102m in revenues and -\$30m in expenditures).

General Fund Revenue Sources
(dollars in millions)

	2008-09 at Budget Act	Revised 2008-09*	Proposed 2009-10	Percent Change
Personal Income Tax	\$55,720	\$46,807	\$47,942	2.4%
Sales and Use Tax	\$27,111	\$27,778	\$33,793	21.7%
Corporation Tax	\$13,073	\$10,197	\$10,445	2.4%
Motor Vehicle Fees	\$29	\$26	\$27	3.8%
Insurance Tax	\$2,029	\$1,831	\$1,798	-1.8%
Liquor Tax	\$341	\$599	\$955	59.4%
Tobacco Taxes	\$114	\$113	\$111	-1.8%
Oil Severance Tax	\$0	\$358	\$855	138.8%
Other	\$3,574	\$3,408	\$1,782	-47.7%
Total	\$101,991	\$91,117	\$97,708	7.2%

*Revisions are due to economic downturn and Governor's proposals.

**Changed from Revised 2008-09

General Fund Expenditures by Agency
(dollars in millions)

	2008-09 Budget Act (as enacted)	Revised 2008-09*	Proposed 2009-10	Percent Change**
Legislative, Judicial, Executive	\$3,816	\$3,779	\$3,772	-0.2%
State and Consumer Services	\$563	\$566	\$577	1.9%
Business, Transportation & Housing Resources	\$1,628	\$1,466	\$2,336	59.3%
Environmental Protection	\$81	\$83	\$79	-4.8%
Health and Human Services	\$31,121	\$30,935	\$29,996	-3.0%
Corrections and Rehabilitation	\$10,342	\$10,310	\$9,615	-6.7%
K-12 Education	\$41,579	\$35,499	\$39,721	11.9%
Higher Education	\$12,113	\$11,745	\$12,389	5.5%
Labor and Workforce Development	\$98	\$102	\$104	2.0%
General Government				
Non-Agency Department	\$387	\$411	\$595	44.8%
Tax Relief/Local Government	\$779	\$647	\$463	-28.4%
Statewide Expenditures	-\$938	-\$5,160	-\$6,045	17.2%
Total	\$103,401	\$92,413	\$95,524	3.4%

*Revisions are due to economic downturn and Governor's proposals.

**Changed from 'Revised 2008-09'.

'Statewide Expenditures' for 'Revised 2008-09' includes \$4.7 billion of reimbursements from proceeds of RAWs.

'Statewide Expenditures' for 'Proposed 2009-10' includes \$6.1 billion of reimbursements from proceeds of lottery securitization and lottery revenues.

New Revenue Proposals

While the largest category of proposed budget solutions is expenditures, the Governor also includes revenue suggestions. Revenue proposals represent 34 percent of the total solutions, or \$14.286 billion over 18 months. None of these funds are from a possible federal bailout.

The major revenue proposals include:

- Temporarily increasing the Sales and Use Tax by 1.5 cents.
- Broadening the Sales and Use Tax to certain services.
- Increasing the excise tax on alcohol by a nickel per drink.
- Instituting a 9.9 percent tax on oil extraction.
- Bringing the personal income tax dependent exemption credit down to the same level as the personal exemption credit.
- Increasing vehicle registration fees (primarily to backfill cuts to local public safety programs, as detailed elsewhere in this report).
- Shifting revenues from tribal gaming compacts from transportation to the General Fund.
- Borrowing money from various special funds.

Administration of Justice

The Governor's proposed 2009-10 budget released on December 31, 2008, features many recommended budget changes in the justice area that have been contained in previous proposals over the last several months, with certain differences noted below. Funding for public safety programs are proposed for steep cuts and, in certain instances, outright elimination.

Shift in Funding Source for Some Local Public Safety Programs. The Governor continues to propose the creation of a Local Safety and Protection Account into which Vehicle License Fee (VLF) funds will be directed to support on an ongoing basis several public safety initiatives. (The VLF redirection would be replaced by a \$12 increase in vehicle registration fees.) The table below details these programs and proposed funding levels in the current and budget years.

Program	2008-09 Budget Act (as enacted)	Governor's Proposed 2009-10 Funding Level*
Citizens' Option for Public Safety (COPS)	\$107.1 million	\$95.8 million
Juvenile Justice Crime Prevention Act (JJCPA)	\$107.1 million	\$95.8 million
Juvenile Probation	\$151.8 million	\$135.9 million
Local Detention Facility Accounts (Booking Fees)	\$31.5 million	\$31.5 million

* Programs would be supported exclusively from VLF funds.

Note that the Governor's budget proposal maintains the current \$100,000 minimum allocation grant for the COPS program.

Elimination of Other Public Safety Programs. The Governor's spending plan also proposes elimination of funding for other significant public safety programs including:

Program	2008-09 Budget Act (as enacted)	Governor's Proposed 2009-10 Funding Level
Juvenile Camps and Ranches Funding	\$29.4 million	\$0
Rural and Small County Sheriffs Program	\$18.5 million	\$0
Cal-MMET	\$11.4 million	\$0

The Governor's 2009-10 budget also proposes to eliminate funding for all other local public safety assistance programs administered by the Office of Emergency Services, including rural crime prevention, gang suppression, SAFE team, and vertical prosecution grants.

Youthful Offender Block Grant. It is notable that the Governor's budget again leaves untouched the Youthful Offender Block Grant, which is intended to support counties' responsibilities to provide local programming and supervision for a new population of youthful offenders, pursuant to [SB 81 \(2007\)](#). The proposed block grant allocation for the 2009-10 budget year is \$92 million. Counties will recall that the full impact of the 2007 population realignment is expected to be felt in the budget year.

Parole Reforms. Further, the Governor's 2009-10 budget continues to feature an array of parole reform measures, all of which were part of various iterations of the 2008-09 regular and special session budget proposals. These reforms, which are expected to save the state nearly \$600 million, are summarized below:

- **Parole Supervision for Most Serious Offenders.** The California Department of Corrections Reform (CDCR) would focus parole supervision efforts on offenders who have committed serious,

violent, or sexual crimes; offenders without current or previous serious, violent, or sexual crime convictions who have six months of clean time would be discharged from parole.

- **Earned Credit.** State prison inmates could receive four months of earned credit for each program successfully completed while incarcerated. In addition, eligible inmates will receive day-for-day credits for complying with institutional rules, awaiting transfer to a state prison and enhanced credit for inmates who are awaiting an assignment to a conservation camp.
- **Increased Threshold for Property Crimes.** Changes would be made to adjust the threshold values for certain property crimes that are prosecuted as felonies, resulting in more crimes being classified as misdemeanors.

Agriculture and Natural Resources

Williamson Act. The Governor's 2008-09 budget reduced the Williamson Act subventions by 10 percent, leaving \$34.7 million from the General Fund to make these payments. The Governor's 2009-10 proposed budget would eliminate \$34.7 million for the Williamson Act in both 2008-09 and 2009-10.

Government Finance and Operations

State Mandates. The budget proposes an increase of \$131 million for current state reimbursable mandates. However, an additional \$91 million that the state would have paid for pre-Proposition 1A mandates is being deferred and will be refinanced over the remaining payment period. The pre-2004 mandates statutorily must be fully repaid by 2020-21.

Senior Citizen's Property Tax Deferral Program. The plan proposes to suspend new property tax deferrals under this program beginning 2/1/9.

Employment Issues. In an effort to reduce state employee compensation costs, the Governor proposed the following:

- A decrease of \$414.6 million in state employee compensation costs in 2008-09 resulting from: two days furlough per month beginning February 1, 2009 (\$375.8 million); elimination of two state holidays and premium pay for hours worked on holidays (\$26.3 million); and, computation of overtime pay based on actual time worked (\$12.5 million).
- A decrease of \$1.01 billion in state employee compensation costs in 2009-10, resulting from: two days furlough per month (\$901.8 million); elimination of two state holidays and premium pay for hours worked on holidays (\$74.5 million); and, the computation of overtime pay based on actual time worked (\$30 million).
- A decrease of \$150 million through layoff of current state employees as well as additional efficiencies.
- A decrease of \$132.2 million in health care costs beginning in January 2010 by contracting for lower cost health care coverage directly from an insurer rather than through the California Public Employees Retirement System. Savings beginning in 2010-11 will prefund Other Post-Employment Benefit costs.

Health and Human Services

The Governor's 2009-2010 Budget, as released on December 31, 2008, proposes to cut the state's health and human services General Fund expenditures by \$1.03 billion, or three percent, in 2009-10. The following items are proposed to take effect on July 1, 2009, unless otherwise stated.

MEDI-CAL

The Governor's proposed budget includes a number of reductions in the Medi-Cal program, many of which have appeared in previous budget proposals throughout 2008:

County Administration: Suspend the statutory cost of living increase for County Administration of the Medi-Cal program for roughly \$49.4 million (\$24.7 million General Fund) in savings.

Eliminate Benefits: Eliminate optional benefits for adults, including dental, optometry, and psychology, for an estimated savings of \$40 million (\$20 million in General Fund (General Fund)) in 2008-09 and \$259 million (\$130 million in General Fund) in 2009-10.

Eligibility Changes: Increase Medi-Cal share of cost requirements to 2001 eligibility levels for the Aged, Blind, and Disabled program for a savings of \$29 million (\$14 million in General Fund) in 2008-09 and \$372 million (\$186 million in General Fund) in 2009-10.

Changes for Immigrants: Scaling back benefits to "limited-scope" for newly qualified immigrants and immigrants who permanently reside under the color of law (PRUCOL) for an estimated savings of \$4.4 million in 2008-09 (\$9.4 million in General Fund and increased federal funds of \$5 million due to diminished recoupment) and \$64.6 million (\$139.9 million in General Fund and increased federal funds of \$75.3 million) in 2009-10.

Implement month-to-month eligibility for undocumented immigrants unless a subsequent emergency ensues for an estimated savings of \$9.6 million (\$4.8 million in General Fund) in 2008-09 and \$142.4 million (\$71.2 million in General Fund) in 2009-10.

Reduce income eligibility for the Medi-Cal program 1931(b) program and redefine under-employment for two-parent families to reduce caseloads for an estimated savings of \$5 million (\$3 million in General Fund) in 2008-09 and \$176 million (\$89 million in General Fund) in 2009-10.

Safety Net Care Pool Funds for Public Hospitals: Reducing reimbursement rates for public hospitals by \$54.2 million from the Safety Net Hospital Care Pool fund. The Governor proposes to use the \$54.2 million – a sum that would normally go to public hospitals, including county-run hospitals, for the care of uninsured patients – to fund other public health programs.

Checkwrite Delays: Add an additional month delay to payments for Medi-Cal fee-for-service providers from 2008-09 fiscal year to 2009-10 fiscal year. This delay would come on top of an already-approved two-week checkwrite delay.

CALWORKS

Administrative Changes: Suspend the county CalWORKs Pay for Performance incentive program for a savings of \$40 million in 2009-10.

COLA Suspension: Suspend the July 2009 CalWORKs cost of living increase for a savings of \$79 million in 2009-10.

Eligibility Changes for Safety Net Program: The Governor would like to modify the CalWORKs Safety Net program by imposing a 60-month time limit on assistance for certain child-only cases, implementing a six-month self sufficiency review requirement to engage families who are not participating in work requirements, and reducing monthly assistance payments by 10 percent. The Governor also proposes to give maximum safety net benefits to working families who are fully participating in federal work requirements. These changes would result in an estimated savings of \$123.5 million in 2008-09 and \$696.9 million in 2009-10.

SUPPLEMENTAL SECURITY INCOME/STATE SUPPLEMENTARY PAYMENT (SSI/SSP)

Suspend COLA: Suspend the June 2010 state SSI/SSP cost of living increase for a savings of \$27 million in 2009-10. The Governor also estimates that this proposal would create an annualized savings of \$323.9 million beginning in 2010-11.

Grant Reductions and Eliminations: Reduce the SSP grant to the federally required minimum and eliminate the Cash Assistance Program for Immigrants (CAPI) for a savings of \$200 million in 2008-09 and \$1.25 billion in 2009-10.

IN-HOME SUPPORTIVE SERVICES

The Governor proposes to provide only non-medical services to the neediest IHSS recipients, eliminating the state's share of cost contribution for the least-needy recipients, and reducing the state's participation in IHSS provider wages to the state minimum wage. These proposals combined are estimated to save the state \$62.7 million in 2008-09 and \$384.2 million in 2009-10.

MISCELLANEOUS

The Governor proposes to eliminate the California Food Assistance Program (CFAP) effective July 1, 2009, for a savings of \$37.8 million.

The Governor proposes to delay the implementation of Los Angeles County's automated benefit and eligibility determination system by six months for a savings of \$14.6 million.

FIRST 5 COMMISSIONS (PROPOSITION 10)

The Governor proposes to divert \$275 million from the statewide California Children and Families Commission (Proposition 10/First 5 Funding) and local First 5 Commissions in 2009-10. The diversion would mean the elimination of the California Children and Families Commission and take 50 percent of the local commissions' revenues. Local fund reserves would not be subject to the sweep. This proposal would be subject to voter approval. The Administration is proposing to use the First Five funds for social services programs serving children, including Foster Care, Adoptions Assistance Program, Child Welfare Services, and the IV-E Waiver.

MENTAL HEALTH SERVICES ACT (PROPOSITION 63)

The Governor proposes to save \$227 million in General Fund by sweeping Proposition 63 (Mental Health Services Act (the Act)) funds and using them to backfill the state's Mental Health Managed Care program. This proposal would require voter approval to amend Proposition 63 and would negatively impact local mental health services that are currently funded under the Act.

DRUG AND ALCOHOL FUNDING REALIGNMENT

The Governor has included in this budget a proposal to impose a 5-cent increase to the existing alcohol excise tax to fund a new Drug and Alcohol Prevention and Treatment Fund. The new fund would support existing alcohol and drug programs, including those administered by the Department of Corrections and Rehabilitation. The new alcohol tax is estimated to generate \$366 million for these programs and save the state a corresponding amount in General Fund. If approved, this proposal would become effective July 1, 2009.

Housing, Land Use and Transportation

The Governor's recently released proposal does not effect transportation funding for local streets and roads. There is no proposal to borrow from Proposition 42, although it was reported that those revenues are declining due to the drop of the price of gasoline and reduced consumption (apparently an estimated \$80 million statewide for 2008-09, and \$233 million statewide for 2009-10).

This proposal does not change the Governor's economic stimulus to accelerate the remaining Proposition 1B local streets and roads funds for cities and counties with \$450 million slated for counties and \$300 million for cities. However, with the state unable to issue bonds until our budget dilemma is resolved and the credit markets improve, there is no expectation of accessing these revenues until late 2009.

With respect to transit, the budget proposes the elimination of \$153.2 million in 2008-09, and \$306 million in 2009-10, for local transit grants previously funded with sales tax on fuels. Funds made available by this proposal are shifted to transportation programs previously funded by the General Fund including Home-to-School Transportation.

We believe that the Governor's budget proposal acknowledges that State Transit Assistance Program (STA) allocations have already been made for the first quarter of 2008-09, and that the second quarter will most likely be made (in mid-January) before any more budget actions are taken. Thus, the remaining "current year funding" proposed to be eliminated is the allocation for third and fourth quarters, or about This proposal reflects the Governor's continued push for total elimination of STA starting July 1, 2009. The "savings" from these changes would be diverted to the home-to-school transportation programs previously supported by the General Fund.