Overview of the 2009-10 May Revision

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SUMMARY

Governor Proposes $21 Billion of New Budget Solutions

Economy and May 19 Election Results In Major New Budget Problem. The Legislature and the Governor agreed to major reductions in state spending and temporary tax increases in February 2009 to address a $40 billion shortfall in California's General Fund. Since then, the continuing toll of a global recession and voters' rejection of ballot measures at the special election have resulted in a major new budget problem. The administration identifies these two factors as key reasons behind the need to adopt $21 billion in new actions to return the budget to balance.

Administration's Estimate of the Problem Is Reasonable. The Governor's estimate of the budget problem that now needs to be addressed is reasonable. Our updated estimates of General Fund revenues and expenditures differ somewhat from the administration's, indicating that the problem may be larger by about $3 billion.

Structural Deficit Persists. Our rough estimate is that even with adoption of all the Governor's proposals, the state would still have an imbalance between General Fund resources and expenditures of greater than $15 billion in 2010-11, with even higher annual operating shortfalls in the subsequent three years.

Extremely Difficult Choices for the Legislature and the Governor

Governor Proposes Major Expenditure Reductions. The Governor proposes major spending reductions across state government totaling around $10 billion—the largest chunk of his $21 billion of proposals to address the budget shortfall. Public schools, social services programs, Medi-Cal, and the prison system each would experience major cuts under the Governor's plan.

Previous Difficult Decisions Make These All the More Difficult. The choices now facing California's leaders will be much more difficult than budget solutions adopted in the recent past. The February budget package included significant temporary tax increases and more than $15 billion in spending reductions affecting K-12 schools, state workers, health and social services programs, and other areas. Actions to address the new budget gap will come on top of these solutions.

Setting Long-Term State Priorities Is Important. Coupled with the spending reductions adopted in February 2009, the Legislature's budget decisions in the coming weeks will affect the course of many major state programs for years to come. The state cannot continue current levels of services in all state programs. By focusing on what it deems to be the highest long-term priorities for California, the Legislature can preserve core services to address these priorities now *and* in the future. To do this, however, lower-priority programs must be cut substantially or eliminated.

Certain Major Proposals Are Very Risky

Governor Seeks to Push Billions of the Deficit Into 2010-11. The Governor proposes to finance $5.5 billion of the deficit by issuing revenue anticipation warrants (RAWs)—a debt instrument used on occasion to address temporary state cash flow problems, *not* an annual budget

deficit. Using RAWs to address the annual budget deficit would be a terrible precedent and a poor fiscal policy. The RAWs merely would defer part of the state's budget problem one fiscal year. If used now and in the future to address annual deficits, RAWs would render meaningless constitutional restrictions on state debt obligations and requirements for a balanced budget. As such, the Governor's RAW proposal presents serious legal concerns. We recommend that the Legislature reject the proposal and replace it with other solutions.

Savings From Several Other Big Proposals May Not Materialize. In addition to the RAW proposal, several billion dollars of the Governor's 2009-10 May Revision budget proposals are high-risk. It is very unlikely, for example, that parts of the State Compensation Insurance Fund (SCIF)—the publicly run workers' compensation insurer—can be sold during 2009-10 for $1 billion. In addition, it is uncertain whether the Medi-Cal savings proposal requiring federal government approval would actually save $750 million. Other proposals present similar concerns.

Some Long-Term Efficiencies Are Proposed

Governor's Proposals Merit Serious Consideration. In the May Revision, the Governor proposes a broad review and, in some cases, sale or refinancing of state properties. He makes credible proposals to eliminate and reorganize state boards and programs to achieve efficiencies. He proposes major changes to retiree health benefits for state employees hired in the future—a first step in addressing massive unfunded liabilities for these benefits. While we doubt that a sale of SCIF can help the 2009-10 budget, we believe a review of the insurer's role in the insurance marketplace is appropriate. Such changes could help the state achieve future efficiencies and savings.

Quick Action Is Advised

Budget Needs to Be Returned to Balance Promptly. Acting quickly to make the difficult decisions to address this budget shortfall would give lawmakers the broadest set of options in achieving program savings. Acting quickly would likely boost the confidence of the public and investors in the budget process. Acting quickly will also be necessary to prevent another state cash crunch this summer and fall.

LAO Bottom Line

The Governor's May Revision proposals include major spending reductions and serious efforts for long-term state efficiencies and savings. By acting quickly and reducing reliance on some of the Governor's riskiest proposals, the Legislature can return the budget to balance, prevent another state cash crunch, and preserve core funding for what it deems to be California's long-term priorities. To accomplish these goals, the Legislature now needs to cut lower-priority programs substantially or eliminate them. To address significant budget deficits forecast in future years, the Legislature also needs to begin work this year on measures that further improve the efficiency of state services for 2010-11 and beyond.

INTRODUCTION

Early Budget Enactment Makes This an Unusual May Revision. In February 2009, the Legislature and Governor approved measures that addressed a $40 billion shortfall in the 2008-09 and 2009-10 state budgets, including six measures that it placed before voters at a special election on May 19, 2009. (Our earlier report, *2009-10 Budget Analysis Series: The Fiscal Outlook Under the February Budget Package*, discusses the details of these February actions.) Accordingly, this May Revision is unusual. Instead of the usual practice of the administration proposing revisions to the budget *proposed* by the Governor in January, this May Revision proposes changes to the 2008-09 and 2009-10 budget package *already passed* by the Legislature in February.

Key Details Released Weeks Earlier Than Expected. The administration had planned to release the May Revision on May 28, 2009. The Governor, however, decided to release two versions of the May Revision on the traditional release date of May 14, five days before the election. Specifically, he released a May Revision with $15 billion of proposed budget solutions in the event voters approved Propositions 1A through 1E on May 19, 2009, and a set of contingency proposals with an additional $6 billion of budget solutions (for a total of $21 billion) in the event voters rejected the May 19 measures. In light of voters' rejection of Propositions 1A through 1E on May 19, this report discusses the Governor's proposed $21 billion package of solutions. Although the Governor released the framework of the May Revision early, many documents and details still had not been submitted to the Legislature at the time this report was prepared.

MAJOR PROPOSALS IN THE MAY REVISION

Large New Budget Problem Identified

Governor Identifies $21 Billion Budget Problem. The Legislature addressed a $40 billion budget problem in the February budget package, leaving a $2 billion reserve under the revenue and expenditure assumptions contained in the package. Since that time, various negative revenue and expenditure trends have emerged, as well as the voters' rejection on May 19 of $5.8 billion of budget-balancing measures included in Propositions 1C, 1D, and 1E. Figure 1 summarizes the various factors leading the administration to conclude that the state now has a new budget problem totaling $21.3 billion to resolve.

Figure 1

Administration's Updated Estimate Of the State's Budget Problem

(In Billions)

May 2009 Revenue and Expenditure Forecast	
Lower revenue estimates	
2008-09	$3.5
2009-10	9.0
Voters' rejections of propositions	
Proposition 1C	5.0
Proposition 1D	0.6
Proposition 1E	0.2
Other changes	3.1
New Budget Problem	**$21.3**

Weak Economy and Declining Revenue Outlook. California, the United States, and much of the rest of the world remain in a deep economic recession—the longest since World War II. As we discussed in our earlier report on the February budget package, significant negative developments in the economy occurred after the Legislature and the Governor reached agreement on the budget measures. Unemployment increased, steep declines in gross domestic product were reported, and stock market prices remained much depressed from levels of just one year ago. Housing prices also remain low, compared to prior years. California's tax system is very sensitive to changes in the state and national economies, and as a result of these recessionary impacts, state revenue collections lagged expectations through April 2009. The administration's revenue forecast reflects the state's weak collections since February 2009, as well as a lowered forecast for revenues for the rest of 2008-09 and 2009-10. As shown in Figure 1, the administration has lowered its revenue forecast by over $12 billion affecting all major taxes. The weak projected performance in these taxes alone accounts for nearly 60 percent of the $21 billion budget problem identified by the Governor.

Voters' Decisions at May 19 Special Election. Propositions 1C, 1D, and 1E contained provisions that would have resulted in $5.8 billion of General Fund savings in 2009-10. Accordingly, voters' rejection of these measures—contrary to the assumptions included in the February budget package—means the Legislature and the Governor need to develop alternate budget solutions of this amount. In addition, passage of Proposition 1A would have extended the temporary tax increases in the February package by one or two years after 2010. Accordingly, voters' rejection of Proposition 1A affects the budgetary outlook in future fiscal years.

Other Changes. Various other changes contribute a net amount of $3.1 billion to the administration's estimate of the new budget problem:

- ***Lower Property Taxes and Higher Proposition 98 General Fund Spending.*** Due to continuing declines in property values, the administration has lowered its property tax revenue forecast by $1.3 billion, which generally results in increased requirements for the state General Fund to provide funding under Proposition 98 to K-12 schools and community colleges. As not all property tax revenue drops are automatically offset by the General Fund, state Proposition 98 spending requirements under the February budget package have increased by $1.1 billion under the administration's estimates. (Under the May Revision's estimates, the minimum Proposition 98 funding level has dropped in 2008-09 and 2009-10, as discussed later in this report. The Legislature, however, would have to take actions to reduce funding below that specified in the February budget package.)

- ***Workload, Caseload, and Program Issues.*** The May Revision always includes updates of program spending, including actual and estimated caseloads in the health and social services areas. In total, the administration has identified $1.1 billion in higher spending requirements of this type in the May Revision.

- ***Other Changes.*** The administration identifies other factors increasing state costs, including higher corrections costs attributed to actions of the prison medical care Receiver and higher debt-service costs.

Governor's Proposed Budget Solutions

In order to return the budget to balance and rebuild a $2 billion reserve, the Governor proposes $21 billion of solutions in the May Revision, as shown in Figure 2. The solutions consist of about $10 billion of spending reductions, $7.5 billion of borrowing, and around $3.5 billion of revenue actions.

Spending Reductions. The Governor proposes major spending reductions affecting most parts of state government, as well as many local governments and individual Californians. As shown in Figure 2, significant spending reduction proposals include:

- ***Proposition 98 Reductions.*** The Governor proposes to reduce 2008-09 and 2009-10 Proposition 98 spending for K-12 schools and community colleges by more than $5 billion below that required by the February budget package. (For more information on the Governor's proposal, see the section below discussing Proposition 98.)

- ***Medi-Cal Reductions.*** The Governor proposes $1.1 billion of total reductions to Medi-Cal, including $750 million of changes that would likely require federal approval.

- ***University System Reductions.*** The Governor proposes reducing General Fund support for the University of California and the California State University by a total of $1 billion and replacing the funds with a like amount of federal stimulus funds. The General Fund savings are on top of a $510 million federal funds swap assumed in the February budget package. Available federal stimulus funds, however, will not be sufficient to fully offset the combined $1.5 billion cut—leaving about a $230 million net reduction.

- ***In-Home Supportive Services (IHSS).*** The May Revision includes several proposals which would result in combined General Fund savings of about

Figure 2

May Revision Proposes Over $21 Billion In New Budget Solutions

(In Billions)

Borrow to address budget deficit with RAWs	$5.5
Reduce Proposition 98 spending for K-14 education	5.3
Borrow local property tax revenue by suspending Proposition 1A	2.0
Increase personal income tax withholding by 10 percent	1.7
Reduce Medi-Cal spending (various proposals)	1.1
Replace state funding for UC and CSU with federal stimulus money	1.0
Sell parts of State Compensation Insurance Fund	1.0
Accelerate receipt of estimated tax payments	0.6
Reduce In-Home Supportive Services spending (various proposals)	0.5
Use "spillover" sales tax revenues for transit bond costs	0.3
Reduce prison population and change sentencing laws	0.3
Reduce SSI/SSP grants to federal minimum	0.2
Identify additional Developmental Services savings	0.2
Other proposed solutions	1.5
Total	**$21.3**

$500 million in IHSS. Specifically, the May Revision would limit the scope of services and copayments currently provided to the less disabled, reduce state participation in wages to the minimum wage, restrict program eligibility to the more severely disabled, and enhance fraud prevention activities.

- ***Reductions in General Fund Costs by Using "Spillover" Revenues.*** The Governor proposes to use $336 million of spillover sales tax revenues in 2009-10 for transit bond debt service costs, thus relieving the General Fund of those costs.
- ***Prison System Reductions.*** Under the May Revision proposal, the Governor would begin approving applications for prison commutations submitted by undocumented immigrants. The administration's plan would result in their release from state prison and deportation by the United States government. In addition, the Governor proposes changing sentencing options for specified crimes that may be treated either as felonies or misdemeanors (known as "wobblers"), instead making these offenses punishable by jail and/or probation rather than state prison. The Governor's proposals would reduce corrections spending by $282 million.
- ***Supplemental Security Income/State Supplementary Program (SSI/SSP) Grant Reductions.*** The May Revision proposal would reduce maximum monthly grants under SSI/SSP grant programs to the federal minimum amounts, effective September 2009. This would reduce maximum SSI/SSP grants from $850 per month to $830 per month for aged, blind, and disabled individuals and from $1,489 per month to $1,407 per month for couples. The proposal would result in state savings of $249 million in 2009-10.

Borrowing. The Governor proposes use of $7.5 billion of borrowing proceeds to return the budget to balance. The proposed borrowing measures include:

- ***RAWs.*** The Governor proposes counting $5.5 billion of RAW proceeds in 2009-10 as helping to balance the 2009-10 budget. As described in our recent reports on the state's cash flow situation, RAWs are a rarely used financial instrument to help the state meet its monthly cash-flow requirements in times of extreme financial stress. Generally, RAWs must be repaid with interest to investors in the fiscal year following their issuance. The state may well have to issue many billions of dollars worth of RAWs for *cash-flow* purposes in 2009-10. Unlike the typical use of RAWs, however, the Governor instead proposes in the May Revision to count $5.5 billion of RAW proceeds as a *budgetary* solution. Under the Governor's plan, the state would have to repay the $5.5 billion of RAWs with interest by the end of 2010-11. Accordingly, this would shift this part of the budget problem one year into the future.
- ***Borrowing Local Government Property Taxes.*** The Governor proposes to use the constitutional mechanism authorized by Proposition 1A (the measure approved in 2004 related to local government

finance) to borrow almost $2 billion of property tax revenues received by cities, counties, and special districts. Under the Governor's proposal, the borrowing would be instituted on an across-the-board basis, with each agency lending 8 percent of its 2008-09 property tax revenues. Repayment would be required within three years with interest. In an effort to minimize the short-term financial strain for local governments associated with these loans, the Governor also proposes legislation to create an authority that would allow local agencies to borrow against future state repayments collectively, rather than just individually.

Revenue Proposals. The Governor's May Revision includes no proposed increases in existing tax rates. His revenue-related proposals—totaling around $2.5 billion—include:

- ***Increased Personal Income Tax Withholding.*** The administration's proposal would accelerate some personal income tax withholding payments from the 2010-11 fiscal year into 2009-10 by increasing withholding schedules for taxpayers by 10 percent. Taxpayers would be able to opt out by manually adjusting their withholding rates. The administration estimates the measure would result in $1.7 billion of increased 2009-10 receipts.

- ***Accelerated Estimated Payment Receipts.*** Individuals and corporations make quarterly estimated income tax payments throughout the year. For example, an individual may have to make estimated tax payments during the year if he or she expects payroll withholdings for state income taxes to be considerably less than his or her total income tax obligations for the year. The Governor proposes to require an increase in the amount of estimated payments due by individuals and corporations in June from 30 percent of estimated tax liability to 40 percent. The administration projects this would accelerate $610 million of payments from the 2010-11 fiscal year into 2009-10. (This is in addition to similar accelerations adopted in September 2008 as part of the *2008-09 Budget Act*.)

- ***Proposed Partial Sale of SCIF.*** The Governor proposes that the state sell parts of SCIF's business. The SCIF, a publicly run workers' compensation insurer, was created in large part to act as the "insurer of last resort" for California's workers' compensation insurance system—insuring workers in occupations deemed too risky to be insured by private-sector companies. The state also contracts with SCIF to administer its workers' compensation insurance program for state employees. In addition to these lines of business, SCIF also competes with private-sector insurers, and the administration's proposal assumes that this part of SCIF's business could be sold to generate $1 billion of proceeds to help address the 2009-10 budget deficit.

- ***Other Proposals.*** Various other revenue proposals by the Governor include an additional payment on all residential and commercial property insurance premiums to fund state and local fire and emergency response activities, higher fees for employers to fund occupational safety and health and labor standards enforcement activities, and higher state fees at certain state parks.

Figure 3

Governor's May Revision General Fund Condition

(Dollars in Millions)

	2008-09	2009-10 Amount	2009-10 Percent Change
Prior-year fund balance	$2,308	-$3,631	
Revenues and transfers	85,947	92,218	7.3%
Total resources available	$88,255	$88,587	
Expenditures	$91,886	$90,956	-1.0%
Revenue anticipation warrants	—	-5,500	
Ending fund balance	-$3,631	$3,131	
Encumbrances	$1,079	$1,079	
Reserve	**-$4,710**	**$2,052**	
Budget Stabilization Account (BSA)	—	—	
Special Fund for Economic Uncertainties	-$4,710	$2,052	

$2 Billion Reserve Proposed. The $21 billion of proposed solutions would address the deterioration in the budget situation since February and restore a $2 billion state reserve balance in 2009-10. Figure 3 shows the Governor's estimate of the condition of the General Fund under his May Revision proposals. The February budget package already assumed the state would end 2008-09 with a $3.4 billion deficit in the state's budgetary reserves. Under the new revenue and expenditure estimates and assuming adoption of the Governor's May Revision proposals, the administration estimates that the deficit at the end of 2008-09 would grow to $4.7 billion. Under the Governor's proposals, the administration projects that 2009-10 General Fund revenues would exceed expenditures by $1.3 billion. Combined with the RAW proposal, the state would end 2009-10 with a positive reserve balance of $2.1 billion.

ADMINISTRATION'S ECONOMIC AND REVENUE OUTLOOK

Economic Forecast

The economic forecast underlying the May Revision's fiscal estimates assumes that California has several more months of rough waters before the beginning of the recovery. The administration's forecast indicates that the United States economy will resume growing in the fourth quarter of 2009. The May Revision forecast, however, expects only modest growth of 1.4 percent for the gross domestic product in 2010. For California, the administration's forecast anticipates a 1 percent decline in personal income in 2009. The forecast anticipates the resumption of income growth in the first quarter of 2010, with an increase for the year, however, of only 1.4 percent.

Revenue Forecast

$12 Billion Fall in Revenues. The May Revision estimates General Fund revenues and transfers of $85.9 billion for 2008-09 and $92.2 billion for 2009-10. The substantial year-to-year growth reflects the implementation of the tax increases adopted in February. Figure 4 summarizes the major changes included in the May Revision compared to the Governor's January budget. As the figure illustrates, baseline revenues over the two years are anticipated to decline by $12.4 billion as compared to February. For the three major taxes, the declines are as follows:

- ***Personal income tax*** receipts fall $5.9 billion over the two years as most categories of income are expected to decline in 2009.
- ***Sales and use taxes*** fall by $4.4 billion due in large part to weak housing and car sales.
- ***Corporation taxes*** are down $2.4 billion due to the fall in corporate profits.

Figure 4 also displays the major proposals included in the May Revision that would increase revenues. The proposals, described earlier in this report, would increase 2009-10 revenues by $3.4 billion.

Figure 4

May Revision Revenue Changes Compared to February Budget

(In Millions)

	2008-09	2009-10	Two-Year Totals
Baseline Revenues			
Personal income tax	-$1,517	-$4,351	-$5,868
Sales and use tax	-1,720	-2,638	-4,358
Corporation tax	-414	-2,006	-2,420
Insurance tax	210	115	325
Other taxes	-24	-82	-106
Other revenues and transfers	39	39	78
Subtotals, Baseline Revenues	(-$3,465)	(-$8,962)	(-$12,427)
New Proposals			
Estimated payments	—	$610	$610
Withholding	—	1,700	1,700
State Compensation Insurance Fund	—	1,000	1,000
New oil lease	—	100	100
Other	—	3	3
Subtotals, Other Revenues	(—)	($3,413)	($3,413)
Totals	**-$3,465**	**-$5,549**	**-$9,014**

LAO Assessment of May Revision Revenue Forecast

Our review of the Governor's May Revision revenue forecast indicates that the administration's General Fund estimates are reasonable but may be somewhat optimistic. Under our updated forecast, combined revenues in 2008-09 and 2009-10 are about $3 billion lower than the administration's. Our economic outlook projects somewhat slower growth in jobs and personal income in 2009 and 2010. All three of the major state revenues—personal income, sales, and corporate taxes—are affected by this slower growth.

PROPOSITION 98—K-14 EDUCATION

May Revision Proposal

Minimum Guarantee for K-14 Education Drops. Proposition 98 consists of a set of formulas that establish a minimum level of funding for K-12 education and the California Community Colleges (CCC). When General Fund revenues drop, the Proposition 98 minimum guarantee often falls in tandem. This is the case in 2008-09 and 2009-10—with the drop in estimated General Fund revenues resulting in notable drops in the minimum guarantee. From levels assumed in February, the administration estimates that the Proposition 98 minimum guarantee has fallen by $1.6 billion in 2008-09 and $3.8 billion in 2009-10. As shown in Figure 5, the Governor's May Revision reduces Proposition 98 funding in both years to these lower levels.

May Revision Proposes Additional Cuts to K-14 Education. Figure 6 shows how the administration proposes to reduce K-14 spending. The top part of the figure shows proposed reductions in 2008-09 spending, and the bottom part shows proposed reductions in 2009-10 spending. By far, the largest current-year proposal is a $1.3 billion decrease in general purpose funding for K-12 school districts (commonly called "revenue limits"). This is a revenue limit reduction of 3.7 percent (for a total cut of 6.4 percent when combined with earlier 2008-09 reductions). Under the Governor's plan, revenue limits would be reduced an additional $387 million in 2009-10 (for a total cut of 8.1 percent when combined with earlier reductions). For community colleges, the May Revision reduces support for categorical programs by $85 million in 2008-09 and an additional $249 million in 2009-10—equating to a cumulative reduction of almost 50 percent. In addition, for 2009-10, the administration proposes to reduce enrollment growth from 3 percent to 1 percent ($127 million savings) and lower the funding rate for recreational courses ($120 million savings).

Plan Relies Heavily on Additional Deferrals. The May Revision includes two additional K-14 deferrals. Under the administration's plan, $115 million in 2008-09 community college

Figure 5

Overview of Proposition 98 Funding Under the May Revision

(In Millions)

	2007-08	2008-09			2009-10		
	Actual	February Enacted	May Revision	Change From February	February Enacted	May Revision	Change From February
K-12 education	$50,304	$44,660	$43,250	-$1,410	$48,315	$45,196	-$3,119
California Community Colleges	6,112	5,972	5,734	-237	6,482	5,784	-698
Other agencies	121	106	106	—	107	107	—
Totals	**$56,538**	**$50,738**	**$49,091**	**-$1,648**	**$54,904**	**$51,087**	**-$3,817**
General Fund	$41,978	$35,036	$33,691	-$1,345	$39,461	$36,651	-$2,810
Local property tax revenue	$14,560	$15,703	$15,400	-$303	$15,442	$14,436	-$1,006

apportionment payments would be deferred until 2009-10 and $1.7 billion in 2009-10 K-12 revenue limits payments would be deferred until 2010-11. These deferrals represent approximately one-third of the administration's proposed May Revision K-14 solutions.

Some Measures Would Provide Additional Flexibility. To help districts respond to a tight budget, the May Revision includes two major new flexibility proposals. For K-12 school districts, the administration proposes changing state law to provide school districts with the option of reducing instructional time the equivalent of up to 7.5 days a year for the next three years. For community colleges, the administration proposes to consolidate the vast majority of the existing 22 California community college (CCC) categorical programs into a block grant (similar to the "flex item" created for K-12 school districts in the February package). Under the block grant approach, community colleges no longer would need to adhere to underlying program requirements. They would have discretion to shift funding among existing categorical programs or away from these programs to other priorities.

Reductions Mitigated by Federal Stimulus Funding. In program terms (excluding deferrals and funding swaps), the May Revision reduces K-12 education by $2.8 billion and CCC by $820 million over the 2008-09 and 2009-10 period. These program reductions would be mitigated by the federal economic stimulus funding available to California. For K-12 education,

Figure 6

Major Proposition 98 Changes Under the May Revision

(In Millions)

2008-09 February Revised Level	**$50,738**
Baseline adjustments	$15
K-12 Education	
Reduce base revenue limits	-$1,311
Eliminate High Priority Schools program	-114
California Community Colleges	
Defer apportionment payments	-$115
Reduce categorical programs	-85
Do not fund property tax shortfall	-37
Total 2008-09 Adjustments	**-$1,648**
2008-09 May Revision Level	**$49,091**
Baseline adjustments	$592
K-12 Education	
Backfill one-time solutions	$4,274
February reductions	-702
Defer revenue limit payments	-1,679
Further reduce base revenue limits	-387
Use one-time child care carryover for preschool	-66
Reduce child care Alternative Payments	-36
Fund Behavioral Intervention Plans	65
Other	92
California Community Colleges	
Backfill one-time solutions	$455
Further reduce categorical programs	-249
Reduce enrollment growth funding	-127
Reduce funding for recreational courses	-120
Do not fund property tax shortfall	-117
Total 2009-10 Adjustments	**$1,996**
2009-10 May Revision Level	**$51,087[a]**

[a] The Governor's proposal also includes $408 million in special funds for Home-to-School Transportation.

California will receive approximately $6.3 billion in federal stimulus funding over this period. As a result, compared to the February funding level, K-12 funding, on average, would increase by about $600 per pupil. Compared to the earlier September *2008-09 Budget Act* level, however, per pupil K-12 funding would fall by about $250, or roughly 3 percent. The programmatic impact experienced by a particular district would depend on the amount of federal stimulus funding it receives. As some stimulus funding (such as Title I funding) is not distributed to every district, programmatic effects will vary across districts. Under the May Revision, community colleges also would receive a small amount of federal stimulus funding to partially mitigate proposed cuts.

LAO Assessment of the May Revision Proposition 98 Proposal

We recommend the Legislature achieve the same level of General Fund savings as the Governor's May Revision by reducing spending to the minimum guarantee. Yet, to achieve these savings, we recommend making more targeted reductions based on the merits of individual programs and avoiding additional deferrals. In addition, we recommend the Legislature work with the administration to explore additional flexibility options.

Continue to Evaluate Programs Based on Their Merits. The May Revision misses several opportunities to eliminate existing programs that are duplicative, inefficient, ineffective, or overbudgeted. We believe about ten existing categorical programs fall into this category (as well as many education mandates). For example, we recommend the Legislature eliminate: a childcare extended-day program that is largely duplicative of the After School Education and Safety program; the California Technology Assistance Project, which can be more efficiently operated by the High-Speed Network; the Year-Round Schools program, which has largely outlived its original purpose; and CCC's high school exit exam remediation program that has shown low success rates with high per-student costs. The Legislature could also better align funding with estimated program need in several programs, such as the Charter School Facility Grant program. We recommend the Legislature make targeted reductions to these kinds of programs as a first order of business—taking every opportunity to achieve savings by reducing existing inefficiencies before reducing districts' general purpose funding.

Avoid Additional Deferrals Across Fiscal Years. The May Revision includes $1.8 billion in new K-14 deferrals. Together with already existing K-14 deferrals, the state would be deferring $6.3 billion in K-14 payments from 2009-10 into 2010-11. That is, about 12 percent of state K-14 payments would be paid after the end of 2009-10. In essence, the administration is expecting districts to run a program in 2009-10 that the state cannot afford. (This "credit card" debt does not include the state's obligation to pay about $1.3 billion in outstanding K-14 mandate claims or about $6.6 billion in revenue limit payments that the state has committed to pay at some point in the future.) Another sizeable deferral could make many districts, especially small districts with small cash cushions, more susceptible to becoming insolvent. Moreover, we advise against planning for deferrals even before a fiscal year has begun. While deferrals have helped the state address midyear drops in the Proposition 98 minimum guarantee, the state has never before gone into a year relying on new interyear deferrals to balance its education budget.

Seek Ways to Provide Additional Flexibility. Although we have concerns with the administration's proposals noted above, we think the administration's flexibility proposals have merit and that the Legislature could build upon them. For example, as the administration proposes, we recommend the Legislature adopt a CCC flex item and consider reducing K-12 instructional time requirements. In addition, we recommend adding the K-3 Class Size Reduction and Home-to-School Transportation programs to the K-12 flex item. The Legislature also might consider adding several K-12 career technical programs to the flex item. Given the proposed cuts to CCC categorical programs, the Legislature might also consider giving districts more flexibility to respond to local needs by waiving the so-called 50 percent law (which currently restricts how much districts can spend on student support services and other noninstructional programs). In general, we recommend exploring many ways to maximize district flexibility while still ensuring positive incentives are in place to promote good teaching, learning, and fiscal practice.

LAO'S OVERALL ASSESSMENT OF THE MAY REVISION

Major Future Budget Shortfalls Would Persist

Reasonable Estimate of Current Budget Problem. The Governor's estimate of the budget problem that now needs to be addressed—$21.3 billion—is reasonable. Our updated estimates of General Fund revenues and expenditures differ somewhat from the administration's, indicating that the problem may be larger by about $3 billion.

Structural Deficit Would Remain. In March 2009, we projected that the state faced huge operating shortfalls in future years even after the adoption of the February budget package. Our rough estimate is that the Governor's May Revision proposals would leave the General Fund with an imbalance between resources and expenditures of greater than $15 billion in 2010-11, with the annual shortfall rising even more in the subsequent three fiscal years.

Bulk of Governor's Proposals Is One-Time in Nature. Figure 7 (see next page) shows several major budget-balancing proposals from the Governor that are one-time in nature—that is, they would help the Legislature address this year's budget problem, but their benefit to the General Fund would not continue after 2009-10. In fact, most of these solutions would make solving future budget problems even more difficult. In total, about $12 billion—over one-half of the Governor's proposed solutions—are one-time in nature. This is a key reason—along with the non-recurring nature of federal stimulus funds incorporated into the February budget package and the temporary nature of the tax increases adopted in February—why the state's out-year budget gaps remain so large under the Governor's plan.

Legislature Should Attempt to Reduce Reliance on One-Time Measures. The current budget problem is so severe that it is difficult to imagine a budget package that does not include many one-time measures to help balance the budget. Such one-time measures can help the budget temporarily without resulting in long-term negative effects for taxpayers and programs. Nevertheless, if the Legislature acts to reduce somewhat the reliance on one-time measures proposed by the Governor, it will place the state on a sounder long-term financial footing by reducing the out-year structural deficit. To do this, the Legislature would need to identify ongoing revenue increases or expenditure decreases to replace the Governor's one-time budget-balancing proposals listed in Figure 7. Such ongoing solutions are the key to reducing the structural deficit.

Tough Decisions Will Require Prioritization

Setting Long-Term State Priorities Is Important. Coupled with the spending reductions adopted in February 2009, the Legislature's budget decisions in the coming weeks may affect the course of many major state programs for years to come. The state cannot continue current levels of services in all state programs. By focusing on what it deems to be the highest long-term priorities for California, the Legislature can preserve core services to address these priorities now *and* in the future. To do this, however, lower-priority programs must be cut substantially or eliminated.

Figure 7

One-Time Budget Solutions Proposed by the Governor in the May Revision

2008-09 and 2009-10 Combined (In Billions)

Borrow to balance the budget with revenue anticipation warrants	$5.5
Borrow property tax revenue from local governments	2.0
Increase suggested personal income tax withholding by 10 percent	1.7
Replace state funding for UC and CSU with federal stimulus funding	1.1
Sell parts of State Compensation Insurance Fund	1.0
Accelerate receipt of estimated tax payments	0.6
Shift Proposition 99 tobacco surtax funds to Medi-Cal	0.1
Other one-time budget solutions	0.1
Total	**$11.9**

Previous Difficult Decisions Make These All the More Difficult. These types of choices will be much more difficult than budget solutions adopted in the recent past. Accordingly, the Legislature should consider the broadest possible range of alternatives, including alternative options we list in the appendix to this report. By considering many alternatives, lawmakers will have a variety of tools to use when deciding how to direct scarce state resources to the highest long-term priorities for California. As we discuss in the nearby box, spending reductions in many parts of the budget are constrained by federal requirements and provisions of the State Constitution. While these restrictions make balancing the budget more difficult, we believe enough flexibility remains to craft a solution to the current budget problem.

Various LAO Alternatives Can Replace Governor's Proposals. In particular, the Legislature may wish to consider the following major options listed in the LAO appendix:

- ***Proposition 42 and Other Transportation Loans.*** While we recommend rejecting the

Some Reduced Flexibility in Rebalancing the 2009-10 Budget

Federal Stimulus Funds Restrict Flexibility in Some Key Programs

Proposition 98 K-14 Education

Under the federal stabilization rules of the American Recovery and Reinvestment Act (ARRA), state General Fund spending must remain above a "maintenance of effort" (MOE) level tied to 2005-06 spending. Using the administration's May Revision numbers, the proposed 2009-10 Proposition 98 spending level is at the constitutional minimum guarantee and slightly above the 2005-06 MOE level. If the state's revenue situation were to further deteriorate and the Proposition 98 minimum guarantee were to fall, however, the state could be constrained in its ability to further reduce K-14 spending.

University of California and California State University

Under ARRA, General Fund spending must remain at or above an MOE tied to 2005-06 spending. After the May Revision reduction proposals, university spending would be hundreds of millions of dollars above the MOE level.

Medi-Cal

Under ARRA, eligibility can not be constrained beyond its July 1, 2008 level. However, optional benefits can be eliminated. In addition, enhanced federal matching rates must be passed through to counties. Reductions to provider rates have generally be restricted by the courts. The administration intends to seek federal approval for program flexibility in order to reduce spending.

In recent years, the state's budget has become increasingly complicated and confusing—particularly as a result of a number of statutory and voter-approved formulas and court-imposed actions that drive state spending. Yet, even with these formulas and other restrictions, virtually all aspects of the state budget are controllable. This is particularly true with enough time to restructure programs and formulas. In tough budget times, however, these formulas and other restrictions add another level of complexity to reducing state spending and crafting an overall budget package.

In seeking to rebalance the 2009-10 budget, the Legislature will face several additional restrictions on its flexibility:

- The acceptance of billions of dollars of federal stimulus funds—particularly in the education and health areas—has created new maintenance-of-effort requirements and restrictions on implementing some savings proposals. These restrictions are summarized in the figure above.

- The time remaining before the start of the fiscal year means that many savings proposals cannot be implemented in time to generate a full year of savings in 2009-10.

While meeting constitutional and federal requirements presents an additional challenge, the flexibility that remains should be sufficient to rebalance the 2009-10 budget.

Governor's RAW proposal, including additional borrowing proposals in the budget plan is probably unavoidable. We suggest several legal approaches to borrowing transportation funds, including Proposition 42 and gas tax subvention funds.

- ***Community College Fees.*** The federal government recently expanded the tax credits available to college students. By increasing community college fees, the state could take advantage of this federal aid and mitigate hundreds of millions of dollars of the Governor's proposed reductions—without substantially affecting the pocketbooks of most students and their families. (Such a fee increase would be part of an overall Proposition 98 solution, discussed in more detail above.)

- ***Vehicle License Fee (VLF)—Public Safety.*** In February, the Legislature carved out a piece of the adopted VLF increase to protect local public safety programs. These activities are primarily a local responsibility, and these funds are a small part of the resources available for front-line law enforcement. With the continued decline in the state's finances, the Legislature could revisit that decision and instead consider redirecting half of the extra revenues into the General Fund.

- ***California Work Opportunity and Responsibility to Kids (CalWORKs).*** The Governor's CalWORKs proposals result in General Fund savings of $157 million but also forgo about $600 million in federal emergency contingency funds. By making work participation voluntary through September 30, 2010, the LAO CalWORKs proposal results in combined net welfare-to-work services and child care savings of about $200 million without losing any federal stimulus funds during 2009-10. In addition, the LAO presents several alternatives that are more targeted in scope but achieve less savings than the Governor.

- ***Employee Compensation.*** The Legislature could direct the administration to score budgetary savings if it chooses not to approve the labor agreements proposed by the Governor with the state employee units represented by Service Employees International Union Local 1000. (These agreements reduce the number of furlough days for these state workers from two days per month to one day per month.) In addition, the Legislature could reduce state employee salaries by an additional 4.6 percent in 2009-10 for more General Fund savings.

- ***Tax Expenditure Programs and Fees.*** We agree with the Governor's choice not to propose any additional tax rate increases. The Legislature, however, could still increase ongoing revenues by making targeted changes in tax expenditures and tax administration. In addition to the Governor's fee proposals, we suggest other ways to offset General Fund costs by implementing proposals to charge users appropriate fees for government services.

Reject the Governor's RAW Budget Proposal

Terrible Precedent and Poor Fiscal Policy. We strongly recommend that the Legislature reject the Governor's proposal to count $5.5 billion of borrowed RAW proceeds toward helping to balance the 2009-10 budget. The state may well need to issue billions of dollars in RAWs in 2009-10 to help address its monthly cash-flow problems, but RAWs were not established to help balance annual state budgets. This proposal—the single largest proposal in the Governor's 2009-10 May Revision—would simply defer this $5.5 billion of the 2009-10 budget problem one year to 2010-11. It would set a terrible precedent for state finances in the future by rendering meaningless constitutional restrictions on state debt obligations and requirements for a balanced budget. As such, the proposal presents serious legal concerns. We recommend that the Legislature reject the proposal and replace it with legal forms of borrowing (such as the suspensions of Proposition 42 and gas tax subventions), spending cuts, and/or revenue increases, such as those listed in the appendix to this report.

Limit Reliance on the Governor's Riskier Proposals

Governor's Largest Solutions Have Large Risks. With a budget shortfall as huge as the state's current one, any budget package is going to include a greater amount of risk than normal. Yet, the May Revision's largest solutions carry with them some of the largest risks. In addition to the RAW proposal, these risks include assumptions of $1 billion of proceeds from the sale of SCIF in 2009-10 and federal government approval for reductions in Medi-Cal benefits ($750 million).

Depending on Solutions Chosen, a Lower Reserve Could Be Appropriate. In an ideal environment, the state's reserve fund should be sized based in part on the uncertainties facing state finances—with a larger reserve needed if revenue and expenditure uncertainties are greater. The purpose of a reserve fund, however, is to help policy makers balance the budget when times are toughest, as they certainly are now. Accordingly, the Legislature may wish to consider budgeting for a reserve of less than the $2 billion level proposed by the Governor. We think the Legislature has more flexibility to do this if it significantly reduces its reliance on the riskiest proposals made by the Governor, as summarized above.

Recognize Impact on Local Government

May Revision Would Strain Local Government Finances. California's cities, counties, and special districts also have been experiencing fiscal stress due to the economic downturn. Some of the Governor's budget solutions would exacerbate this stress because they (1) decrease local revenues (particularly the property tax) or (2) indirectly increase demand for local programs (such as county jails and indigent health programs). Any budget package that the Legislature adopts is likely to negatively affect local governments in some way—whether by budgetary cuts or payment delays. Consequently, we recommend that the Legislature acknowledge the impact of the state's budget solutions on local governments, implement budget solutions in a targeted fashion, and take actions to maximize local government program flexibility and resources whenever possible. This approach is similar to the one proposed for school districts earlier in this report.

Proposition 1A Borrowing Could Be Adjusted. The Constitution does not require that the property tax borrowing be implemented on an across-the-board basis as proposed by the Governor. Instead of borrowing 8 percent from *each* local agency, the state could borrow a larger percentage from agencies that have greater capacity to (1) reduce programs or (2) replace property taxes with fees or other revenues. For example, the state could borrow over a quarter of the total loan amount from waste and water enterprise special districts, a group of local agencies the Legislature previously directed to get off the property tax roll entirely. (These special districts typically depend on property taxes for less than 7 percent of their operating revenues and have broad authority to increase fees or reduce programs.) Borrowing more property taxes from waste and water enterprise special districts would allow the state to borrow less from agencies with less fiscal flexibility.

Return the Budget to Balance Quickly

More Than Usual, Delay Will Limit the Legislature's Options. In budgeting, time almost always equals money. The sooner an action is taken the more benefit can accrue to the state. Accordingly, the more quickly the Legislature takes action on the budget, the more options it has available to address any given budget problem. Early action often means a somewhat less substantial program cut or revenue increase can produce the same amount of budgetary benefit as a greater cut or revenue increase later. The need for quick action to return the budget to balance is even more imperative this year. As we described in our recent update on the state's cash flow situation, acting quickly to return the budget to balance and address the state's cash flow challenges would help the Treasurer and Controller access the investment markets in the most efficient manner as soon as July. This could relieve state cash flow pressures earlier in the fiscal year and reduce somewhat the need for payment deferrals to school districts, local governments, and others. Finally, acting quickly to address California's severe budget problems could increase confidence of the public and investors in the state's budget process.

Need to Begin Work on Future Reforms and Savings

Governor's Proposals Are a Credible Start to the Discussion. With the May Revision, the Governor raised several proposals to reduce future state costs; generate revenues and savings for future state budgets; and consolidate, eliminate, or streamline programs. The Governor proposes the sale or refinancing of some major state properties. He proposes major changes to retiree health benefits for state employees hired in the future—a first step in addressing massive unfunded liabilities for these benefits. While we doubt that a sale of SCIF can help the 2009-10 budget, we believe a review of the insurer's role in the insurance marketplace is appropriate. We believe the Legislature should consider all of these proposals seriously, although achieving budgetary savings from them—particularly in 2009-10—can be difficult to do. The state's ongoing structural budget deficit is so severe that proposals that require time to implement need to be enacted soon to help balance the budget in future years.

After Addressing the Immediate Shortfall, Focus on Future Reforms and Savings. We recommend that the Legislature—after acting quickly to return the 2009-10 budget to balance—use the rest of its 2009-10 legislative session to focus on longer-term state reforms that can produce savings to help close future years' budget shortfalls. The Governor's proposals deserve consideration, and we have offered many others in past publications.

CONCLUSION

The Legislature and the Governor need to make very difficult decisions now that will affect major state programs for years to come. The Governor's May Revision proposals include major spending reductions and efforts for long-term state efficiencies and savings. By acting quickly, rejecting the Governor's RAW proposal, and reducing reliance on some of the Governor's riskiest proposals, the Legislature can return the budget to balance, prevent another state cash crunch, and preserve core funding for what it deems to be California's long-term priorities. To accomplish these goals, the Legislature now needs to cut lower-priority programs substantially or eliminate them. To address significant budget deficits forecast in future years, the Legislature also needs to begin work this year on measures that improve the efficiency of state services *even more* beginning in 2010-11 and beyond.

Appendix

LAO Budget Options

General Fund Benefit (In Millions)

Department	Option	2009-10	2010-11
K-14 Education			
K-12 Education	Suspend General Fund support for Program Improvement schools participating in the Quality Education Investment Act.	**$326.0**	**—**
K-12 Education	Suspend General Fund support for special education residential placements.	**59.0**	**—**
K-12 Education	Suspend General Fund support for state special schools.	**38.7**	**—**
K-12 Education	Eliminate 200 California Department of Education positions associated with categorical programs eliminated in February package.	**10.0**	**—**
K-12 Education	Place measure on ballot to remove autopilot funding formula for After School Education and Safety program.	**—**	**$550.0**
K-14 Education	Eliminate six of costliest K-12 mandates and three of costliest community college mandates.	**—**	**—**
Higher Education			
CPEC	Eliminate non-core functions of commission.	**$0.4**	**$0.4**
CSAC	Raise Cal Grant B eligibility to 2.5 GPA.	**11.0**	**11.0**
CSU	Phase out state support for professional schools.	**—**	**10.0**
CSU	Increase average faculty teaching load by 1 course per year.	**120.0**	**120.0**
CSU	Increase average class size by another 5 percent.	**67.5**	**67.5**
CSU	Reduce non-instructional staffing 5 percent through hiring freeze, furloughs, and layoffs.	**70.0**	**70.0**
CSU	Increase fees an additional 5 percent to offset General Fund support (net of additional Cal Grant costs).	**37.5**	**37.5**
CSU	Suspend Math and Science Teacher Initiative.	**2.7**	**2.7**
CSU	Eliminate state subsidy for students taking excess units for out-year savings of $48 million annually.	**—**	**—**
CSU	Fund pre-collegiate coursework at CCC rate.	**12.4**	**12.4**
UC	Phase-out state support for professional schools.	**—**	**25.0**
UC	Increase average faculty teaching load by 1 course per year.	**135.0**	**135.0**
UC	Increase average class size by another 5 percent.	**50.0**	**50.0**
UC	Reduce non-instructional staffing 5 percent through hiring freeze, furloughs, and layoffs.	**140.0**	**140.0**
UC	Increase fees an additional 5 percent to offset General Fund support (net of additional Cal Grant costs).	**42.0**	**42.0**
UC	Reduce state portion of research support by 10 percent.	**26.6**	**26.6**
UC	Eliminate California Summer School for Math and Science.	**1.9**	**1.9**
UC	Eliminate state subsidy for students taking excess units for out-year savings of $10 million annually.	**—**	**—**

Department	Option	2009-10	2010-11
Health			
DADP	Redirect state and federal asset forfeiture proceeds to support drug treatment programs.	**$10.0**	**$10.0**
DADP	Use federal Byrne Grant funds to supplement substance abuse treatment activities provided by the Offender Treatment Program.	**50.0**	**15.0**
DDS	Expand the Family Cost Participation Program to all regional center (RC) purchase of services except 24-hour care.	**7.5**	**11.3**
DDS	Define the term cost-effective in the Lanterman Developmental Disabilities Services Act.	**5.0**	**11.0**
DDS	Implement regulations to govern RC expenditures for miscellaneous services.	**Unknown**	**Unknown**
DDS	Increase RC's authority to conduct utilization reviews of all RC-funded services.	**Unknown**	**Unknown**
DDS	Reduce provider payments and limit access to services if stakeholder process is unsuccessful.	**234.0**	**234.0**
DHCS	Suspend grants (Seasonal Agricultural and Migratory Workers Program, Indian Health Program, Rural Health Services Development Program) to primary care clinics.	**22.0**	**22.0**
DHCS	Suspend state-only funding for the Expanded Access to Primary Care program.	**13.5**	**13.5**
DHCS	Implement a pilot program to contract with a broker for Medi-Cal non-emergency medical transportation.	**Unknown**	**Unknown**
DHCS	Implement copays for nonemergency use of emergency rooms.	**5.8**	**7.7**
DHCS	Apply Federal Deficit Reduction Act eligibility requirements to Minor Consent Program to obtain federal funds	**10.9**	**14.5**
DHCS	Shift eligibility determinations from the counties to the state.	**—**	**17.5**
DHCS	Reduce benefits to the federal minimum—eliminate payment for over the counter drugs in the Medi-Cal Program.	**8.6**	**11.5**
DHCS	Impose a temporary rate cap on nursing home rate increases.	**9.2**	**22.2**
DHCS	Eliminate Medicare Part B payments for all beneficiaries who have not met their Medi-Cal share-of-cost.	**4.1**	**5.4**
DHCS	Use the Public Assistance and Reporting Information System to disenroll beneficiaries no longer in California.	**2.7**	**5.4**
DPH	Reduce several HIV/AIDS programs: (1) expand client cost-sharing and limit the formulary in AIDS Drug Assistance Program; and (2) reduce other HIV/AIDS programs.	**24.6**	**24.6**
DPH	Suspend General Fund support for Alzheimer's Disease research.	**6.2**	**6.2**
DPH	Suspend General Fund support for immunization assistance to local agencies.	**18.0**	**18.0**
DVA	Delay opening the Adult Day Health Care programs at the new veterans homes in Lancaster and Ventura.	**1.1**	**4.6**

Department	Option	2009-10	2010-11
MRMIB	Implement co-payment increase in Healthy Families Program (HFP) as proposed by Governor in his 2008-09 budget proposal.	**$1.9**	**$2.9**
MRMIB	Lower HFP Dental Cap to $1,000 as proposed by Governor in his 2008-09 budget proposal.	**1.9**	**2.8**
MRMIB	Increase HFP premiums for beneficiaries with family incomes over 150 percent of the federal poverty level by $8-$13 per month.	**19.1**	**28.2**
MRMIB	Modify eligibility for Access for Infants and Mothers so women with high-deductible private coverage would keep their coverage and receive assistance in paying their deductibles.	**5.6**	**11.0**
Social Services			
Aging	Eliminate Linkages program.	**$7.9**	**$7.9**
Child Support Services	Create matching program for local child support agencies.	**4.0**	**4.0**
Child Support Services	Reduce child support automation staff by 10 percent.	**0.5**	**0.5**
EDD	Shift Workforce Investment Act funds to offset General Fund costs in the California Departmento of Corrections and Rehabilitation (CDCR) parolee employment programs or California Conservation Corps.	**37.0**	**37.0**
OSI/Social Services	Reduce welfare automation maintenance and operations by 10 percent in 2009-10 and 2010-11.	**6.0**	**6.0**
OSI/Social Services	Reduce child welfare system maintenance and operations by 10 percent in 2009-10.	**4.0**	**—**
OSI/Social Services	Delay CalWORKs Business Analytics and Reporting System by two years.	**1.8**	**4.2**
Social Services	Make CalWORKs work participation voluntary through September 2010.	**201.8**	**0.0**
Social Services	Adopt community service requirement for parents who have been on aid for more than five years effective Oct. 1, 2010.	**—**	**16.7**
Social Services	Make an in-person interview a condition of eligibility for CalWORKs effective Oct. 1, 2010.	**—**	**16.8**
Social Services	Modify CalWORKs earned income disregard to better reward work effective Oct. 1, 2010.	**—**	**15.0**
Social Services	Suspend "hold harmless" budgeting methodology for Child Welfare Services (CWS) for three years.	**9.7**	**9.7**
Social Services	Reform Adoption Assistance Program (AAP) prospectively.	**2.0**	**12.0**
Social Services	Eliminate the supplemental clothing allowance for Foster Care, Kin-GAP, and AAP.	**10.0**	**10.0**
Social Services	Eliminate the Dual Agency Rate Supplement.	**5.4**	**5.4**
Social Services	Reduce funding for the Extended Independent Living Program.	**10.0**	**10.0**
Social Services	Eliminate funding for emancipated foster youth stipends.	**3.6**	**3.6**
Social Services	Reduce Community Care Licensing visit protocol from 30 percent to 10 percent random sample for non-residential faclities and 20 percent random sample for residential facilities.	**10.0**	**10.0**
Social Services	Eliminate the Kinship Support Services Program.	**4.0**	**4.0**

Department	Option	2009-10	2010-11
Social Services	Cap fully loaded CWS social worker costs at $155,000.	**$4.0**	**$4.0**
Social Services	Establish 30 percent county share for Transitional Housing Program Plus for emancipated foster youth.	**12.3**	**12.3**
Social Services	Restrict California Food Assistance Program to legal non-citizens residing alone.	**25.3**	**40.8**
Social Services-IHSS	Eliminate or reduce In-Home Supportive Services (IHSS) share-of-cost buyouts.	**35.6**	**47.5**
Social Services-IHSS	Make IHSS advisory committees optional and eliminate state support.	**1.6**	**1.6**
Social Services-SSI/SSP	Reduce SSI/SSP couples grants to federal minimum.	**80.0**	**98.0**
Social Services-SSI/SSP	Eliminate veterans program for Philippine residents.	**2.5**	**3.3**
Social Services-SSI/SSP	Eliminate SSI/SSP Restaurant meal allowance and allow for one-time purchase of cooking equipment.	**25.0**	**30.0**
Social Services-CAPI	Restrict Cash Assistance Program for Immigrants (CAPI) to most vulnerable populations, such as those living alone or those without adequate sponsors.	**34.0**	**45.0**
Judiciary and Criminal Justice			
CalEMA	Eliminate California Gang Reduction Intervention and Prevention program and Internet Crimes Against Children Task Force.	**$10.0**	**—**
Corrections	Close one youth correctional facility.	**—**	**$15.0**
Corrections	Use AB 900 funds for reentry facility site evaluations.	**5.0**	**—**
Corrections	Release inmates who have no current or prior serious, violent, or sex offenses 30 days early.	**50.0**	**50.0**
Corrections	Release inmates over the age of 55 who have no current or prior serious, violent, or sex offenses.	**9.0**	**9.0**
Corrections	Enhance credit earnings available for inmates.	**104.0**	**104.0**
Corrections	Exclude new admissions to prison who would serve less than six months.	**51.0**	**57.0**
Corrections	Require second and third "strikes" to be serious or violent for an offender to get a full "Three Strikes" sentence enhancement.	**10.0**	**50.0**
Corrections	Adjust property crime thresholds.	**51.0**	**51.0**
Corrections	Reduce time served for parole revocations.	**96.0**	**143.0**
Corrections	Exclude parolees with technical and misdemeanor violations from revocation to prison.	**262.0**	**350.0**
Corrections	Expand the use of alternative sanctions for parole violators.	**94.0**	**94.0**
Corrections	Implement earned discharge program for parolees.	**100.0**	**175.0**
Department of Justice	Charge forensic lab fees.	**20.0**	**40.0**
Department of Justice	Eliminate Underground Economy program.	**0.6**	**0.6**
Department of Justice	Reduce funding for the Bureau of Narcotics Enforcement.	**20.0**	**20.0**
Judicial Branch	Suspend conservatorship program for an additional year.	**—**	**17.4**

Department	Option	2009-10	2010-11
Judicial Branch	Implement electronic court reporting.	**$12.6**	**$32.5**
Judicial Branch	Phase in competitive bidding for court security.	**20.0**	**40.0**
Judicial Branch	Transfer funding from the Immediate and Critical Needs Account to the General Fund for two years.	**275.0**	**275.0**
Public Safety Local Assistance	Redirect half the revenue from temporary .15 percent VLF increase to the General Fund, which supports various public safety grant programs. Remaining funds would support a consolidated juvenile justice program at a reduced level.	**250**	**250**
Resources			
CalFire	Eliminate funding for DC-10 aircraft contract.	**$6.8**	**$6.8**
CalFire	Delay vehicle replacements.	**17.0**	**(17.0)**
CalFire	Close low-priority fire stations and other facilities.	**10.0**	**10.0**
CalFire	Enact wildland fire protection fee.	**270.0**	**270.0**
Conservation Corps	Eliminate California Conservation Corps.	**17.1**	**34.2**
Energy Commission	Loan monies to General Fund from balance in Alternative and Renewable Fuel and Vehicle Technology Fund.	**35.0**	**—**
Energy Commission	Loan monies to General Fund from balance in Renewable Resource Trust Fund.	**140.0**	**(40.0)**
Fish and Game	Increase regulatory fees.	**3.0**	**3.0**
Fish and Game	Suspend General Fund support for Marine Life Protection Act Initiative.	**4.8**	**4.8**
Fish and Game	Eliminate General Fund support for California Environmental Quality Act review.	**2.5**	**2.5**
OEHHA	Fund regulatory support activities fully from fees.	**5.0**	**5.0**
Parks and Recreation	Increase state park fees (beyond the Governor's proposal).	**12.5**	**25.0**
State Water Board	Increase fees by expanding fee base to pay for water quality management activities.	**19.7**	**19.7**
State Water Board	Increase fees in core regulatory permitting and enforcement program.	**6.9**	**6.9**
State Water Board	Eliminate General Fund support for Total Maximum Daily Load program to regulate water pollution.	**10.6**	**10.6**
Various Resources Departments	Eliminate General Fund support for CALFED program oversight.	**7.2**	**7.2**
Various Resources Departments	Eliminate General Fund support for timber harvest plan reviews.	**21.6**	**21.6**
Water Resources	Increase fees to fully pay for (1) watermaster program and (2) Central Valley Flood Protection Board and related programs.	**8.7**	**8.7**
Water Resources	Eliminate General Fund support for California Irrigation Management Information System.	**1.0**	**1.0**
Water Resources	Eliminate General Fund support for Delta levees.	**4.9**	**4.9**
Transportation			
Caltrans	Partially suspend Proposition 42 transfer.	**$1,152.8**	**—**
Caltrans	Reimburse General Fund for transit debt service from "spill-over" revenues in Mass Transportation Fund (MTF).	**426.7**	**—**

Department	Option	2009-10	2010-11
Caltrans	Reimburse General Fund for transit debt service from Public Transportation Account (PTA).	**$273.0**	**—**
Caltrans	Reimburse General Fund for highway transportation debt service.	**112.0**	**—**
Caltrans	Suspend Local Airport Grants.	**4.0**	**—**
Caltrans	Suspend gas tax subvention to cities and counties.	**1,030.0**	**—**
Caltrans	Repeal Proposition 42.	**—**	**$1,624.0**
DDS	Increase PTA support of Regional Center Transportation (in-lieu of General Fund).	**15.0**	**—**
Education	Eliminate PTA and MTF funding for home to school transportation.	**-**	**—**
Motor Vehicle Account	Shift Non-Article XIX revenues to General Fund.	**70.0**	**—**
General Government			
Commission on State Mandates	Modify "Animal Adoption" mandate to reduce by three days the holding period for stray cats and dogs.	**$24.6**	**$25.1**
Commission on the Status of Women	Eliminate the commission.	**0.5**	**0.5**
Employee Compensation	Score savings if proposed labor agreements with Service Employees International Union Local 1000 are not approved.	**233.4**	**—**
Employee Compensation	Add third furlough day or reduce state employee base salaries by an additional 4.6 percent in 2009-10.	**450.9**	**—**
Employee Compensation	Extend policy for three furlough days per month for state employees into 2010-11.	**—**	**1,352.7**
Employee Compensation	Repeal statute providing automatic annual increase in judges' pay.	**0.5**	**0.5**
Employee Compensation	Direct CalPERS in statute to achieve a given level of premium cost reductions (alternative to Governor's proposal).	**132.2**	**238.7**
Food and Ag	Suspend various plant health and pest management programs funded from General Fund.	**8.0**	**—**
Office of Administrative Law	Eliminate the office and amend statute to transfer its core responsibilities to departments.	**1.6**	**1.6**
Office of Planning and Research	Eliminate General Fund support for the office.	**5.9**	**5.9**
Payment of Interest on General Fund Loans	In addition to actions to balance the budget, adopt intrayear payment deferrals to reduce the state's 2009-10 short-term cash-flow borrowing requirement below $10 billion.	Potentially hundreds of millions of dollars	**—**
Personnel Administration	Eliminate Rural Health Care Equity Program (RHCEP) for almost all state employees living in rural areas effective July 1, 2009. Eliminate RHCEP for Bargaining Unit 5 (CHP officers) after expiration of existing collective bargaining agreement.	**17.2**	**14.7**
Revenues			
Franchise Tax Board	Eliminate the extra personal income tax credit provided to those 65 and older.	**$190.0**	**$170.0**
Franchise Tax Board	Eliminate the exclusion of life insurance benefits from taxable income.	**100.0**	**105.0**

Department	Option	2009-10	2010-11
Franchise Tax Board	Eliminate the exclusion of subsidized parking benefits from taxable income.	**$100.0**	**$100.0**
Franchise Tax Board	Eliminate the exclusion from taxable income of profits on certain sales of small business stock.	**20.0**	**20.0**
Franchise Tax Board	Eliminate the exclusion from taxable income of profits from trading properties.	**350.0**	**360.0**
Franchise Tax Board	Cancel zones authorized in 2006 and phase out other zones as their designations expire.	**100.0**	**120.0**
Board of Equalization	Eliminate the exclusion for animal feed; seeds, plants, and fertilizers; drugs and medicines administered to animals; and medicated feed and drinking water.	**465.0**	**475.0**
Board of Equalization	Eliminate the exclusion for timber harvesting, farming, and post-production equipment for television and films.	**145.0**	**145.0**
Board of Equalization	Eliminate the partial exclusion for glasses, contact lenses, drugs and medicines used by veterinarians, and other medical specialty items.	**80.0**	**80.0**
Board of Equalization	Eliminate the exemption for diesel fuel, custom computer programs, and leasing of films and tapes.	**140.0**	**40.0**

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