



Revised January 13, 2010

Governor's Proposed Budget Includes Deep Cuts, Assumes More Federal Funds

Governor Schwarzenegger released his final Proposed Budget on January 8. The Proposed 2010-11 Budget addresses a \$19.9 billion gap, consisting of a \$6.6 billion shortfall in the remainder of 2009-10 and a \$12.3 billion gap in 2010-11, using a combination of spending reductions, federal aid, and fund shifts. The Proposed Budget would end 2010-11 with a \$1.0 billion reserve. The Governor proposes no new tax increases, but does include tax cuts that would reduce state revenues and widen the budget gap. The Proposed Budget would spend \$82.9 billion from the state's General Fund in 2010-11 and assumes \$89.3 billion in 2010-11 General Fund revenues and transfers. The Governor assumes that 43 percent of the "solutions" used to balance the budget come from spending reductions, 35 percent from federal funds, 20 percent from "alternative funding," and 3 percent from fund shifts and other revenues.

As noted above, the Governor assumes the state ends 2010-11 with a modest reserve. However, the Administration's multi-year budget forecasts show significant shortfalls emerging in 2011-12 and beyond. The Governor also assumes that transfers to the state's budget reserve would be suspended through the end of the forecast period in 2013-14.

The Governor's proposals include deep cuts to health and human service programs; a permanent pay cut for state employees; reductions in K-14 education spending; reductions to corrections spending; and a complex swap that eliminates the sales tax on gasoline, raises the excise tax on gasoline and diesel fuels, and uses the increase in fuel tax revenues to pay certain transportation costs currently borne by the General Fund. The tax swap would result in a net tax reduction for consumers and an \$836 million reduction in the Proposition 98 guarantee. The reduction in the Proposition 98 guarantee would occur since the sales tax on gasoline counts toward the school funding guarantee, while gas taxes do not. The Governor also proposes to divert revenues earmarked for early childhood programs by Proposition 10 of 1998 and for mental health by Proposition 63 of 2004. Diversion of these revenues would require voter approval and a similar attempt last year was defeated in the May special election. Finally, the Governor proposes to transfer financial responsibility for certain children's programs from the state to counties. Under this proposal, counties would pay for the additional responsibilities with savings achieved from other program reductions. Just over one-third (34.0 percent) of the Governor's \$8.5 billion in proposed "expenditure solutions" target health and human services programs. K-14 education and child development programs covered by the Proposition 98 guarantee would receive 28.6 percent of the proposed reductions; state employee compensation accounts for 19.2 percent of the cuts; corrections and rehabilitation would receive 13.7 percent of the cuts; and all other areas of state government account for 3.7 percent of the reductions.

The following update provides a “quick and dirty” summary of key provisions of the Governor’s Proposed Budget. As additional details become available, the California Budget Project (CBP) will update this document. The CBP also will prepare in-depth analyses of major proposals contained in the budget over the upcoming days and weeks. Please check the CBP website (www.cbp.org) for corrections and additions to this analysis as additional information becomes available. The Governor’s budget documents are available on-line at <http://www.ebudget.ca.gov/>.

Digging Deeper: New Tax Cuts, Extension of Temporary Tax Increases if Federal Funds Are Not Received

The Proposed Budget would not raise taxes to help close the state’s budget gap unless the state fails to receive a specified level of federal funds, but it does include several measures that would reduce General Fund revenues. The Governor also assumes enactment of a number of fee increases, including student fees in both the California State University (CSU) and University of California (UC) systems. The Proposed Budget would impose a 4.8 percent surcharge on all residential and commercial property insurance premiums and use the revenues raised to support the Department of Forestry and Fire Protection and for other emergency response costs. The surcharge is estimated to raise \$238.1 million in the remainder of 2009-10 and \$478.6 million in 2010-11. The Proposed Budget also assumes \$100 million in 2009-10 and \$119 million in 2010-11 in lease revenues from oil drilling at Tranquillon Ridge. The Governor states that the “revenue will be used to fund state parks.”

In his State of the State address, the Governor proposed to extend and expand the \$10,000 tax credit for homebuyers enacted in February 2009 for a cost of \$200 million. The Governor also proposed a new sales tax exemption for certain types of manufacturing equipment used for “advanced transportation, renewable energy, and other clean technology projects.” The Governor’s proposal would expand the homebuyer tax credit to existing homes, as well as never before occupied homes. Unlike the federal homeownership tax credit, the state credit is not limited to first-time homebuyers, has no income limitations (eligibility for the federal credit is limited to individual taxpayers with incomes of no more than \$95,000 and married taxpayers with incomes of no more than \$170,000), and is not recaptured at the time a home is sold. The Tax Policy Center at the Urban Institute and Brookings Institution described the more limited federal credit as “likely to do little to solve the housing market’s problems.” In an assessment of the existing state tax credit published in the State Controller’s August 2009 *Statement of General Fund Cash Receipts and Disbursements*, economist Chris Thornberg wrote, “all these sales and more could have occurred without any money from the state if builders had just collectively lowered their prices by the \$40,000 needed to keep up with price declines in existing homes. Similarly, claims that the rebate program would create jobs were empty.”

The Governor also assumes that the federal estate tax, including the “pick up” tax which is passed through to the state, is restored in 2011. The Proposed Budget assumes the state receives \$892 million from the restoration of the pickup tax in 2010-11. While current federal law would restore both the federal tax and the state pick up tax, observers generally believe that Congress will likely modify the tax prior to 2011 and that restoration of the pick up tax is unlikely. The Legislative Analyst notes, for example, that a measure modifying the tax that passed the House in December did not restore the pick up tax. California’s stand alone inheritance tax was repealed by the voters in 1982 and the measure that eliminated that tax prohibits the state from enacting a tax on bequests absent voter approval.

The Legislative Analyst also notes that the Governor’s Proposed Budget assumes the receipt of \$450 million in additional revenues, but does not state how these revenues should be raised, and that the loss of revenues from the Governor’s proposed tax cuts is not reflected in the Budget’s revenue estimates.

Transportation Tax Swap

The Governor proposes a complex swap that would eliminate the sales tax on gasoline and raise the excise tax on gasoline and diesel fuel by \$0.108 per gallon. Under the Governor’s proposal, \$929 million in costs currently paid out

of the General Fund would be paid by the new special fund tax, Public Transit Account (PTA) funded programs would lose \$1.658 billion, the state's school funding obligation would be reduced by \$836 million, and net revenues would be reduced by \$976 million. Taken together, these changes would lower General Fund spending by \$1.8 billion. In 2010-11, the Governor's proposal would allocate the same amount of funding to transit capital projects, intercity rail, transit planning, and local streets and roads as was allocated in 2009-10. The proposal would spend \$929 million for debt service costs. Of this amount, \$603 million would have otherwise been paid from the General Fund and \$326 million from the PTA.

The goal of this swap is two-fold. First, courts have ruled against the state's diversion of a portion of the current sales tax on gasoline from the PTA to benefit the General Fund. The Governor's proposal would use the proceeds of the increased fuel tax for purposes that result in General Fund savings. Second, Proposition 42 of 2002 and Proposition 1A of 2006 which dedicated a separate portion of the sales tax on gasoline to transportation provided that these monies would be treated as General Fund revenues for the purpose of calculating the Proposition 98 guarantee, but that their use would be dedicated to transportation. Fuel excise taxes, in contrast, are special fund revenues that do not count toward the Proposition 98 guarantee. The Governor's proposed swap would result in an \$836 million reduction in the Proposition 98 guarantee by reducing General Fund revenues that count toward the guarantee and raising special fund revenues that don't count toward the guarantee.

Switching to Autopilot

The Governor's proposals include a constitutional amendment that would cap state spending for prisons at 7 percent of General Fund spending beginning in 2014-15 and require at least 10 percent of General Fund spending to go to higher education. Beginning in 2011-12, monies saved from reducing prison spending would be transferred to higher education and in 2014-15 and beyond, the Legislature would be required to allocate at least 10 percent of the General Fund to the UC and CSU systems. The Governor's proposal would also give the Department of Corrections and Rehabilitation broad constitutional power to privatize operations of state prisons and prison services, such as medical and educational services and give private correctional facility employees the power to carry weapons. The proposed measure also prohibits the use of "early release" to gain the savings required to fulfill the higher education spending obligation. The funding cap for prisons and funding guarantee for higher education could be suspended by either a proclamation of an emergency by the governor or a two-thirds vote of the Legislature.

Recession May Be Over, But Recovery Remains a Long Way Off

California and the US are slowly emerging from the longest and most severe recession in the post-World War II era. Many experts believe the national downturn came to an end in the third quarter of 2009, when inflation-adjusted gross domestic product (GDP) – the value of all goods and services produced in the US – grew on an annual basis for the first time in more than one year. Some forecasters believe the recession ended in the fourth quarter of 2009 in California.

The Governor's forecast reflects the general consensus among economists that the worst of the downturn is over, but that the economic recovery will be long and slow for both the nation and California. The Governor's economic outlook projects relatively weak growth in national inflation-adjusted GDP compared with two out of the last three recoveries, and these projections are in-line with those of other forecasters, including the Legislative Analyst's Office (LAO). The Governor estimates that US GDP declined by 2.5 percent in 2009 and forecasts that it will increase by 2.2 percent in 2010, followed by a 2.9 percent increase in 2011.

Although the national economy is projected to expand in 2010 and 2011, growth will not be sufficient to substantially reduce unemployment. The Governor's forecast shows the annual US jobless rate peaking at 10.0 percent in 2010,

then dropping modestly to 9.4 percent in 2011. In California, where the recession has taken a greater toll on the labor market, the annual unemployment rate is projected to peak at 12.0 percent in 2010 – up from an estimated 11.6 percent in 2009 – then fall to 11.2 percent in 2011. The Governor’s outlook for the state and national job markets is nearly identical to that of the LAO.

Continued weakness in California’s job market over the next few years means personal income growth and taxable sales growth will be weak. This translates into slow growth for the state’s two largest revenue sources – the personal income tax and sales tax. The Governor projects that California’s annual personal income will gradually rise over the next few years, but yearly gains will remain well below the average growth rate of past decades. Personal income is expected to increase by 2.4 percent in 2010, 3.6 percent in 2011, and 4.8 percent in 2012, according to the Governor’s projections. In contrast, the Governor notes, personal income rose by an average of 5.6 percent per year between 1988 and 2008. Annual taxable sales dropped by 15.6 percent in 2009, according to the economic outlook, and they are projected to increase by a modest 1.9 percent in 2010, followed by a more robust 8.8 percent rise in 2011.

Governor Assumes Substantial Increase in Federal Funds

The Governor assumes receipt of a total of \$6.9 billion in additional federal funds primarily in 2010-11 in order to help close the state’s budget gap. Specifically, the Governor assumes that the federal government will:

- Extend the period during which states receive additional federal funding for a range of health and human services programs under the American Recovery and Reinvestment Act of 2009 (ARRA) for savings of \$7.5 million in 2009-10 and \$2.1 billion in 2010-11. Currently, ARRA funding is available through September 30, 2010 or December 31, 2010, depending on the program. While advocates are hopeful that Congress will approve a second round of ARRA funding to help states avert deep program cuts, Congress has yet to act on proposals of the magnitude assumed by the Governor. The Governor assumes the federal government will extend ARRA funding through 2010-11 for the following programs:
 - Medi-Cal Program (\$1.2 billion);
 - CalWORKs Program (\$538 million);
 - Developmental and Regional Centers (\$162.7 million);
 - Early and Periodic Screening, Diagnosis, and Treatment and Mental Health Managed Care (\$86.5 million);
 - In-Home Supportive Services Program (\$49.8 million);
 - Adoption Assistance Program and Foster Care Program (\$26.8 million);
 - Early Start Program (\$32.9 million); and
 - Child Support Program (\$20.8 million).

In addition, the Governor assumes that the federal government will:

- Permanently increase the federal government’s share of Medi-Cal Program costs from 50 percent to 57 percent, for savings of \$1.8 billion in 2010-11.
- Provide a \$1 billion reimbursement to California in 2010-11 for state costs related to mandated special education services.
- Increase federal funding by \$879.7 million in 2010-11 to fully fund the cost of incarcerating undocumented immigrants in California state prisons.
- Reimburse California for services to people with disabilities that were provided through Medi-Cal rather than through the federal Medicare Program for savings of \$700 million in 2010-11.

- Allow California to pay less toward the Medicare Part D prescription drug benefit in 2010-11 by:
 - Revising the formula that determines how much California pays to the federal government to help finance the cost of Medicare Part D for annual savings of \$75 million, and
 - Applying the higher ARRA federal cost-sharing ratio to Medicare Part D for savings of \$250 million.
- Increase federal payments for the Foster Care Program for savings of \$7.5 million in 2009-10 and \$86.9 million in 2010-11.

The Governor Proposes Additional Cuts and Revenue Increases if California Does Not Receive Assumed Federal Funding

The Governor proposes to implement additional spending cuts and certain tax increases if the state does not receive the \$6.9 billion in additional federal funds assumed in the Proposed 2010-11 Budget. These spending cuts and tax increases would be made on a dollar-for-dollar basis to reflect the amount by which federal funds fall short of the level assumed by the Governor. The Governor cannot implement these cuts and revenue increases unilaterally, so this proposal would have to be part of budget negotiations with the Legislature.

The Governor's proposal includes a total of \$4.6 billion in spending reductions. The Governor proposes to:

- Eliminate the CalWORKs Program (\$1.044 billion).
- Use Proposition 63 funds to pay for existing mental health services, a change that would require approval by the voters (\$847 million).
- Reduce Medi-Cal eligibility to the minimum allowed under current federal law and eliminate most remaining optional benefits (\$532 million).
- Reduce state employee salaries by an additional 5 percent (\$508 million).
- Eliminate the In-Home Supportive Services (IHSS) Program (\$495 million).
- Redirect additional county savings from the Governor's proposed program reductions to offset state costs (\$325 million).
- Eliminate non-court required rehabilitation programs, implement "banked parole" for low-risk serious and violent offenders, increase the number of crimes for which convicted felons serve their sentences in local jails, and increase the number of parolees supervised by each parole agent (\$280 million).
- Eliminate the Healthy Families Program (\$126 million).
- Eliminate various health services programs funded by Proposition 99 (\$115 million).
- Eliminate funding for enrollment growth at the UC and the CSU (\$111.9 million).
- Make an unallocated reduction to trial courts (\$100 million).
- Freeze the level of the awards and income eligibility for Cal Grants (\$79 million).
- Eliminate funding for the Transitional Housing Placement for Foster Youth-Plus Program (\$36 million).

The Governor's proposal includes a total of \$2.4 billion in revenues, which would be raised by extending several of the temporary tax increases enacted in the February 2009 budget agreement and delaying implementation of some of the corporate tax cuts that were included in recent budget agreements. These changes would remain in effect for one year. The Governor proposes to:

- Extend suspension of a business's ability to claim net operating loss deductions (\$1.2 billion).
- Extend reduction in the dependent tax credit from \$319 to \$102 (\$504 million).
- Delay the ability of businesses to share certain tax credits among members of a unitary group (\$315 million).
- Delay the implementation of changes to the formula used to allocate corporate income to California for tax purposes (\$300 million).

- Reduce the amount of losses that businesses are allowed to carry back and reduce prior years' taxes to 30 percent (\$20 million).

Medi-Cal Program

The Governor proposes a number of reductions to the Medi-Cal Program for total savings of \$1.1 billion in 2009-10 and 2010-11. Some of the proposals have been rejected by the Legislature in previous years. Specifically, the Governor proposes to:

- Impose limits on Medi-Cal services and require increased copayments, premiums, or both for savings of \$750 million in 2010-11. The Administration has not yet specified how these reductions would be made. The proposal to limit Medi-Cal services follows last year's elimination of 10 benefits, including dental care for adults, podiatry services and incontinence creams and washes.
- Eliminate Medi-Cal eligibility for certain immigrants, such as those who have been living in the US for less than five years, effective March 1, 2010 for total savings of \$118 million through 2010-11. The Governor proposed, and the Legislature rejected, this cut in each of the two previous years. Individuals affected by this proposal could still receive certain services, such as emergency or pregnancy-related care.
- Eliminate Adult Day Health Care benefits effective March 1, 2010 for total savings of \$104 million through 2010-11. Last year's budget limited benefits for Adult Day Health Care to three days a week, but that reduction was blocked by the courts in September 2009.
- Assume savings of \$26.4 million in 2010-11 from a Medi-Cal Anti-Fraud Initiative, targeting pharmacies, physicians' services, transportation, and medical equipment. The July 2009 budget agreement also assumed savings from Medi-Cal anti-fraud measures.
- Reduce family planning reimbursement rates effective March 1, 2010 for total savings of \$28.7 million through 2010-11. The governor proposed, and the Legislature rejected, this cut last year.

Other Health Programs

The Governor proposes to:

- Limit eligibility for Healthy Families to children in families with incomes through 200 percent of the federal poverty line effective May 1, 2010 for savings of \$10.5 million in 2009-10 and \$63.9 million in 2010-11. Another decrease of \$3.9 million would come from the disenrollment of severely disabled children qualifying for California Children's Services under the Healthy Families Program. This reduction in eligibility was proposed in the Governor's May Revision last year. Currently, children in families with incomes up to 250 percent of the poverty line are eligible for the program. If passed, approximately 240,000 children could lose coverage, according to previous estimates from the Administration.
- Increase premiums for some children in the Healthy Families Program. The Governor also proposes to eliminate vision benefits for children in this program. These two actions effective July 1, 2010 would save a total of \$21.7 million in 2010-11. Currently, children in families with incomes between 151 percent and 200 percent of the federal poverty line pay \$16 per child per month for Healthy Families, up to a maximum of \$48 per family. The premium increases would result in premiums of \$30 per child per month, up to an increase per family of \$90 per month. As of November 1, Healthy Families enrollees began paying higher premiums and co-pays as a result of legislation passed in 2009.

California Work Opportunity and Responsibility to Kids (CalWORKs) Program

The Governor proposes to:

- Reduce CalWORKs grants by 15.7 percent effective June 1, 2010 for savings of \$68.9 million in 2010-11. This cut would reduce the maximum monthly grant for a family of three in high-cost counties from \$694 to \$585. Previously, the February 2009 budget agreement reduced CalWORKs grants by 4 percent effective July 1, 2009. This proposal also would result in savings of \$42.7 million in the Department of Developmental Services budget and \$18.3 million in the California Student Aid Commission due to the shifting of federal funds.
- Eliminate CalWORKs benefits for legal immigrants who have been in the US for less than five years effective June 1, 2010 for savings of \$22.5 million in 2010-11.

Supplemental Security Income/State Supplementary Payment (SSI/SSP) Program

The Governor proposes two changes that would result in total savings of \$21.8 million in 2009-10 and \$285.1 million in 2010-11. Specifically, the Governor proposes to:

- Reduce maximum SSI/SSP grants for elderly and disabled individuals from \$845 per month to \$830 per month, the minimum allowed by federal law, effective June 1, 2010, for savings of \$13.7 million in 2009-10 and \$177.8 million in 2010-11. Previously, the February and July 2009 budget agreements cut the maximum SSI/SSP grant for individuals from \$907 to \$845 between May 1 and November 1, 2009, and cut the maximum grant for couples from \$1,579 to \$1,407 during the same period. The grant for couples is already at the minimum level permitted by federal law, and therefore the state cannot cut it further.
- Eliminate the Cash Assistance Program for Immigrants (CAPI) effective June 1, 2010 for savings of \$8.1 million in 2009-10 and \$107.3 million in 2010-11. CAPI provides state-funded cash assistance to elderly and disabled legal immigrants who are not eligible for SSI/SSP grants solely due to their immigration status.

In-Home Supportive Services (IHSS) Program

The Governor proposes two changes that would result in total savings of \$77.9 million in 2009-10 and \$922.6 million in 2010-11. Specifically, the Governor proposes to:

- Cap the maximum amount up to which the state will share in the cost of wages and benefits for IHSS workers at the state's minimum wage, currently \$8.00 per hour, plus \$0.60 per hour for benefits effective June 1, 2010 for savings of \$21.3 million in 2009-10 and \$271.8 million in 2010-11. Currently, the state shares – along with counties and the federal government – in combined wage and benefit payments of up to \$12.10 per hour for IHSS workers. Counties could continue to provide compensation above the proposed level, but would have to use their own dollars to make up for lost state funding. In June, a federal judge blocked the state from reducing combined wage and benefit payments for IHSS workers to \$10.10 per hour, a provision that was included in the February 2009 budget agreement.
- Limit IHSS services to individuals with "functional index" scores of 4.0 and higher, effective June 10, 2010, for savings of \$56.6 million in 2009-10 and \$650.8 million in 2010-11. This change would eliminate services for 87 percent of the IHSS caseload, reducing the number of recipients from 485,000 to 63,000. In October, a federal judge blocked the state from implementing less restrictive IHSS eligibility changes that were included in the July 2009 budget agreement. Those changes would have eliminated some IHSS services for 97,000 recipients and all services for an additional 36,000 recipients.

Other Human Services Programs

The Governor proposes to:

- Use First 5 funds to support children enrolled in programs administered by the Department of Developmental Services and the Department of Social Services for state savings of \$550 million in 2010-11 – a change that would require voter approval. The \$550 million fund shift would be composed of \$308 million from state and local First 5 reserves and \$242 million from shifting approximately half of First 5's projected 2010-11 tobacco tax revenues. In addition, the Governor's proposal would continue to shift about half of First 5's annual revenues to offset state General Fund costs from 2011-12 to 2014-15. First 5 supports programs for children from birth to age 5, using funds provided by a 50-cent-per-pack state tax on cigarettes imposed by Proposition 10 of 1998. In May 2009, voters rejected Proposition 1D, which would have diverted First 5 funds to help balance the state's budget.
- Increase counties' share of the cost of certain human services programs for state savings of \$505.5 million in 2010-11. The Administration suggests that counties would fund these increased costs by redirecting a portion of the county savings that result from the Governor's proposed reductions to the CalWORKs and IHSS programs.
- Eliminate the California Food Assistance Program (CFAP) effective June 1, 2010 for savings of \$3.8 million in 2009-10 and \$56.2 million in 2010-11. CFAP provides state-funded nutritional benefits to qualified legal immigrants who are ineligible for federal food stamp benefits.

Child Care and Development Programs

The Governor proposes to:

- Reduce CalWORKs Stage 3 child care funding by \$122.9 million "to achieve additional ongoing Proposition 98 General Fund savings." Under the Governor's proposal, Stage 3 child care would be available only to the "neediest families," rather than to all former CalWORKs families who meet income eligibility requirements.
- Reduce the reimbursement rate limits in voucher-based programs – including the non-CalWORKs Alternative Payment Program and CalWORKs Stage 2 and 3 child care – from the 85th percentile to the 75th percentile, based on the 2005 Regional Market Rate survey, for savings of \$77.1 million in 2010-11. This proposal would take effect July 1, 2010 and also would reduce the reimbursement rate limits for license-exempt providers from 90 percent to 70 percent of the limits for licensed family child care homes.

State Employees

The Governor proposes to cut state employees' compensation and benefits in 2010-11, rather than continue the three-day-per-month state worker furloughs, which began in February 2009. The state has lost a number of legal challenges to the furlough program, and many more court decisions are pending. The Governor assumes that his proposed reductions to state worker pay and benefits would generate savings of \$1.6 billion, which would be offset by \$1.1 billion in costs when the furloughs end. Specifically, the Governor proposes to:

- Reduce state workers' pay "across-the-board" by 5 percent for General Fund savings of \$529.6 million.
- Increase state employees' retirement contributions by an additional 5 percent of salary, reducing state employers' contributions by an equal amount for General Fund savings of \$405.8 million.
- Issue an executive order requiring state departments, other than constitutional offices, to reduce personnel costs by 5 percent by July 1, 2010 for General Fund savings of \$449.6 million.
- Reduce costs for state employees' health coverage by contracting directly with a lower-cost health insurance provider or through the California Public Employees' Retirement System for General Fund savings of \$152.8 million.

million beginning in January 2011. Beginning in 2011-12, the Governor proposes to use the savings generated by this shift to “pre-fund” retiree health care costs.

- Reduce “pre-funding” of retiree health care costs – the amount of money that would need to be invested today to cover the future costs of retiree health coverage promised to workers – for savings of \$98.1 million in 2010-11.

K-12 Education

The Governor’s Proposed Budget would reduce Proposition 98 funding by \$892.6 million in 2009-10 and by \$1.540 billion in 2010-11.

To achieve the proposed \$1.5 billion in 2010-11 savings, the Governor would:

- Reduce funding for school district central administration by \$1.2 billion. The Governor’s proposal also would limit school district spending for central administration costs.
- Reduce funding for the K-3 Class Size Reduction Program by \$550 million.
- Reduce funding for school districts and county offices of education by \$300 million by allowing administrative functions to be contracted out to the private sector.
- Reduce revenue limit and categorical funding for school districts and county offices of education by \$229.5 million due to lower average daily attendance, retirement costs, and cost-of-living adjustments (COLAs). Revenue limits provide general-purpose funding for schools.
- Reduce funding for county office of education administration by \$45 million. The Governor’s proposal would require county offices of education to consolidate services and functions, which could include forming regional consortia to provide administrative services.
- Reduce Proposition 98 funding for the Department of Corrections and Rehabilitation Juvenile Justice Division and State Special Schools by \$23.4 million.
- Suspend payments for most K-12 education mandates. The Governor would provide an increase of \$65 million for mandated behavioral assessments and intervention plans, \$7.7 million for mandated costs related to interdistrict and intradistrict transfers, and \$6.8 million for costs related to the California High School Exit Exam.

The Governor also proposes to:

- Continue the science graduation requirement without providing funding to pay for the reimbursement rate adopted by the Commission on State Mandates. Last year, the Governor proposed to eliminate the science graduation requirement which would have cost the state \$196 million in 2009-10.
- Make statutory changes to give school districts the ability to lay off, assign, reassign, transfer, and rehire teachers without regard to seniority.
- Repeal statutes that require that teachers who have been laid off receive first priority for substitute assignments and to modify current law that requires that these teachers be paid at their prior salary level if they work for a specified number of days.
- Modify teacher layoff notification requirements that would allow school districts to notify teachers of an impending layoff 60 days after the state budget is adopted or amended. Current law requires school districts to notify teachers by March 15 in order to lay them off the following school year.
- Continue to allow school districts to reduce the school year by up to five days through 2012-13.

To achieve the proposed \$892.6 million in 2009-10 savings, the Governor proposes to:

- Reduce funding for the K-3 Class Size Reduction Program by \$340 million.
- Reduce general purpose funds for school districts and county offices of education by \$229.3 million due to lower average daily attendance, unemployment insurance, and retirement costs.
- Reduce Proposition 98 funding for the Department of Corrections and Rehabilitation Juvenile Justice Division and State Special Schools by \$17.8 million.
- Reduce categorical funding by \$14.3 million.

The Governor's Proposed Budget would fund K-14 education at the minimum required by the Proposition 98 guarantee, a reduction of \$2.433 billion in 2009-10 and 2010-11 combined. The guarantee reflects a funding level lower than that previously assumed for two reasons. First, the guarantee would fall due to lower-than-anticipated tax collections due to the weak economy. Second, the transportation tax swap described above would reduce the Proposition 98 guarantee by \$836 million in 2010-11.

The Governor's Proposed Budget reflects a 2008-09 funding level that is \$2.3 billion more than the funding level that would be required by the Proposition 98 guarantee. The Governor proposes an \$89.2 million reduction in the guarantee to reflect the actual level of 2008-09 expenditures. The Governor proposes to count a portion of the remaining \$2.2 billion toward the \$1.3 billion owed to schools in outstanding maintenance factor payments for 2007-08. The Governor also proposes to delay certain allocations made "in lieu" of maintenance factor payments as provided in the July 2009 budget agreement. Both of these proposals would reduce the Proposition 98 minimum guarantee in 2009-10 and 2010-11.

California Community Colleges

The Governor proposes to:

- Maintain community college fees at the current level of \$26 per unit.
- Increase enrollment growth funding by \$126 million, which represents 2.2 percent growth in apportionments, sufficient to fund approximately 26,000 Full-Time Equivalent Students (FTES).
- Reduce ARRA State Fiscal Stabilization Fund (SFSF) payments by \$95 million in 2009-10 and \$130 million in 2010-11. The July budget agreement provided \$130 million in 2009-10 ARRA SFSF payments for community colleges. However, because 2008-09 cuts to community colleges were less severe than proposed in the 2009 May Revision, they only received \$35 million.
- Provide a negative COLA of -0.38 percent, reducing funding for community college apportionments and categorical programs by \$22.9 million.
- Backfill community colleges for lower-than-anticipated local property revenues (\$33.7 million), oil and mineral revenues (\$1.6 million), and student fee revenues (\$1.9 million). The Proposed Budget also provides \$2.1 million to cover colleges' cost of administering fee waivers.

Higher Education

The Governor:

- Would increase 2010-11 funding by \$610 million to backfill one-time reductions of \$305 million each in support for the UC and the CSU. This amount replaces a \$255 million allocation of federal funds from the ARRA to each segment in 2009-10 and restores a \$50 million reduction implemented as part of the trigger reductions included in the February 2009 budget agreement.

- Assumes \$335.1 million in 2009-10 funding to reflect the 15 percent mid-year fee increase approved by the UC Regents in November 2009 and a 20 percent CSU fee increase approved by the Board of Trustees in July 2009. The Governor also assumes \$1.1 billion in 2010-11 support from continuation of the 2009 fee increases and imposition of an additional 15 percent UC fee increase as approved by the Regents. The 2010-11 fee increases would provide \$662.7 million in support to the UC and \$390.7 million to the CSU. Budget documents state that “consistent with current policy, at least one-third of additional fee revenue will be set aside for institutional financial aid to preserve equitable access for low-income students.”
- Would increase funding by \$111.9 million to reflect an increase in enrollment at the UC (\$51.3 million) and CSU (\$60.6 million). The proposed increase would fund 2.5 percent enrollment growth, approximately 5,121 FTES at the UC and 8,290 FTES at the CSU. According to the Senate Budget Committee, “due to current over-enrollment in the UC and CSU systems, this increase will not provide new student enrollment and will still leave current enrollment levels underfunded.”
- Would increase annuitant benefit payments by a total of \$14.8 million for the UC, CSU, and Hastings College of Law. Of this amount, \$14.1 million is for the UC.

Student Aid Commission

The Governor proposes to:

- Suspend new awards for the Competitive Cal Grant Program for savings of \$45.5 million. According to the Assembly Budget Committee, the suspension would affect access for 22,500 students. Budget documents state the “Competitive Program is largely duplicative of the Cal Grant High School Entitlement Program and the Community College Transfer Entitlement Program.”
- Use \$18.3 million in TANF funds to cover a portion of the cost of the Cal Grant Program. Budget documents state that the TANF Funds are available as a result of the 15.7 percent CalWORKs grant reduction.”
- Increase funding by \$197.4 million in 2010-11 to backfill the one-time use of Student Loan Operation Fund monies in 2009-10 and to cover added costs related to UC and CSU student fee increases in both the current and budget years. The Governor would also provide \$32.9 million in 2009-10 funding to reflect increased Cal Grant costs, primarily due to UC and CSU fee increases.

Corrections

The Governor proposes to:

- Reduce per-inmate medical care costs to a level comparable to that of New York for savings of \$811 million in 2010-11. The Administration suggests that these savings “can be achieved without adversely impacting inmate care through a combination of measures,” including reducing salaries, reducing “unnecessary referrals” to specialists, and reducing inmate “over-utilization” of medical services. California’s prison medical care system is currently being overseen by a federal court-appointed receiver. Therefore, any changes to medical care for inmates would likely require approval of the federal courts.
- Allow individuals who have been convicted of specified nonviolent, non-sex felonies, including drug possession, to serve their time in local jails instead of state prison for state savings of \$25.2 million in 2009-10 and \$291.6 million in 2010-11.
- Reduce the number of juvenile offenders by making a number of statutory changes, including transferring eligible offenders to adult institutions, for savings of \$41.3 million in 2010-11.

In addition, as described above, the Governor proposed a constitutional amendment that would limit spending on prisons to no more than 7 percent of General Fund spending beginning in 2014-15. The corrections savings would be used to increase spending on higher education to no less than 10 percent of General Fund spending.

Local Government

The Governor proposes to:

- Suspend most local government mandates consistent with those suspended in the July 2009 budget agreement and defer payments for current mandate claims, for savings of \$232.2 million. When the state suspends a mandate, local governments are no longer required to provide the mandated service and will not be reimbursed by the state if they continue to provide it.
- Continue to suspend the Williamson Act Program. In July 2009, the Governor used his line-item veto authority to reduce funding for the program to \$1,000.

In addition, the July 2009 budget agreement shifted \$1.7 billion in 2009-10 and \$350 million in 2010-11 from redevelopment agencies to schools. Budget documents state that funds shifted in 2010-11 would be used to offset the cost of local trial courts.

Labor and Workforce Development

The Governor proposes to use up to \$500 million from the Unemployment Compensation Disability Fund – more commonly known as the State Disability Insurance fund – to pay employers and training providers to train workers and to pay \$3,000 stipends to employers that hire unemployed workers. Employers would be required to retain workers used to qualify for the cash incentive payment for nine months. Employers would be required to retain workers used to qualify for the training payment for three months. The proposal would use revenue from a fund supported by a payroll tax paid by employees to pay employers and training providers. Up to \$230 million in payments would be available in 2010-11.

Resources

The Governor proposed to:

- Reduce funding for CalFIRE's emergency fire suppression costs below 2009-10 year-to-date levels by \$32.8 million to \$223 million in 2010-11. Budget documents state that the lower expenditure level represents "the historical average of emergency firefighting costs over the past five years."
- Allocate \$30 million to the Department of Fish and Game to restore a one-time fund shift in 2009-10 from the Fish and Game Preservation Fund to the General Fund.
- Provide \$54.8 million in 2009-10 and \$98.2 million in 2010-11 to repay loans to the General Fund from the Beverage Container Recycling Program.
- Reduce funding for the Department of Fish and Game's recreational hunting and fishing programs by \$5 million.

Legislative, Executive, and Judicial

The Governor proposes to:

- Increase funding for trial court operations by \$135.3 million in 2010-11.
- Provide \$30.7 million in funding to the State Controller's Office for the 21st Century Project, which would replace obsolete statewide employment history, payroll, leave balance accounting, and position control systems.
- Provide \$68.2 million in 2010-11 to reimburse counties for costs incurred for the May 19, 2009 statewide special election.
- Restore \$9.9 million of funding for the Board of Equalization's (BOE) collection activities, which budget documents state would generate approximately \$90 million in additional General Fund revenues in 2010-11.
- Increase funding for the BOE by \$4.4 million to expand the BOE's enforcement activities at agricultural inspection stations, which budget documents state would generate \$23 million in new General Fund revenues in 2010-11.
- Eliminate the Office of Planning and Research and transfer its functions to various other agencies.
- Reduce funding for the Department of Justice (DOJ) by \$53.9 million. These costs would be recovered by allowing the DOJ to bill state departments for legal services provided on their behalf.
- Assume savings of \$17.4 million from delaying the implementation of the Guardianship and Conservatorship Reform Act by one year.
- Assume receipt of increased revenue from implementation of an automated speed enforcement program. The \$337.9 million in increased revenues would offset a \$296.9 million General Fund reduction in trial court funding and provide \$41 million in additional funding for trial court security.
- Increase fines imposed for criminal offenses from \$1 to \$3 to fund DOJ's regional forensic labs for \$45.1 million in General Fund savings.