



California Budget Project
Email Update
August 30, 2002

Where Is The Budget Debate Today?

California's budget stalemate is now the longest on record. In 1992, the Legislature passed a budget on August 29. While rumors of a looming agreement abound, as of the afternoon of August 30, the state still lacked an approved spending plan for the 2002-03 fiscal year.

The Status Of Budget Deliberations

The state Senate passed a budget and related implementing measures on June 29, 2002, before the start of the current fiscal year. The state Assembly has yet to pass a spending plan. While 50 Democratic Assemblymembers have supported the budget passed by the Senate, at least four Republican votes are needed to reach the two-thirds vote required to pass a spending plan.

Over the past two months, the Assembly's Democratic leadership has made a number of proposals in an attempt to win Republican votes. The Assembly's Republican leadership have steadfastly opposed the current package and, specifically, the inclusion of a tax increase as part of a final budget agreement. Proposals offered by Assembly Democratic leadership as part of attempts to win Republican votes includes an August 6, 2002 tax package that relies more heavily on a tobacco tax increase than the Senate's plan, which increased Vehicle License Fees. Last weekend, the Assembly Democratic leadership offered a larger business tax break, a 2003-04 expenditure cap; \$200 million in unspecified reductions; a reduction of 1,000 state employee positions by 2003-04; creation of a commission to study the state's fiscal situation; and passage of legislation requiring the Governor to establish a strategic plan for the state and accountability measures for state programs.

Recent rumors have suggested that a possible budget could include additional spending reductions and a smaller revenue increase than the budget passed by the Senate or prior Assembly Democratic proposals. Other issues under consideration include modifying the state's spending cap and earmarking a share of state revenues for infrastructure, such as the proposal contained in ACA 11 (Richman).

Earlier this week, the Speaker of the Assembly asked the Legislative Analyst to provide a list of program reductions totaling \$3 billion, excluding reductions to programs under the Proposition 98 school spending guarantee, to illustrate the magnitude of cuts that would be required to balance the budget without a revenue increase. An initial list, totaling \$2.3 billion in potential reductions, included \$858.9 million in services for the elderly and disabled; \$513.4 million in reductions to health care for the elderly, poor, and working families; \$14.1 million in reductions to children's services; \$202.7 million in reductions to mental health programs; \$490.9 million in higher education reductions; \$55.8 million in welfare-to-work program reductions; \$66.9 million

in agriculture and water program reductions; and \$110.6 million in reductions to housing and general government.

What Does The Democratic Tax Proposal Do?

The Assembly's August 6 tax proposal would:

- Increase the tobacco tax by \$2.13 per pack. The measure passed by the Senate increased the cigarette tax by \$0.63 per pack.
- Suspend net operating loss deductions for 2002 and 2003. This is consistent with the measure passed by the Senate.
- Suspend the teacher tax credit for 2002 and the solar energy tax credit for 2002 and 2003.
- Increase withholding for stock options and bonuses. The Senate measure suspended the teacher tax credit, but not the solar energy credit.
- Impose a 5 percent tax on direct satellite broadcast services.
- Authorize a number of enhancements to state audit and collection activities in order to boost revenue collections. These provisions are consistent with those passed by the Senate.

Should The State Enact A \$2.13 Per Pack Increase In The Cigarette Tax?

The Assembly's revenue package includes a substantially larger tobacco tax increase than that passed by the Senate. On an annual basis, the Assembly proposal, contained in SB 1849, would raise \$2.027 billion. Proponents of an increase of this magnitude argue that:

- Voters support higher cigarette taxes;
- Taxpayers can avoid the tax by quitting smoking, thus it is a "voluntary" tax increase;
- Positive public health outcomes associated with the decline in tobacco consumption would result from higher tobacco taxes and youth would be particularly likely to quit smoking as a result of a substantial tax increase; and
- Reduced tobacco product consumption would result in savings to public health programs, such as Medi-Cal, through reductions in tobacco-related disease.

Critics of an increase of this magnitude note that:

- Tobacco taxes are a declining revenue source due to falling consumption rates;
- The goal of reducing consumption of tobacco products conflicts with the goal of raising revenues;
- The health care savings associated with lower rates of tobacco product consumption are long-term, while the state's revenue needs are immediate; and
- Tobacco taxes disproportionately burden low-income Californians.

Who Would Bear The Burden Of Higher Tobacco Taxes?

The burden of higher tobacco taxes would fall on users of tobacco products. A pack a day smoker would pay an additional \$777.45 per year under the Assembly proposal. As a share of income, tobacco taxes fall most heavily on low-income households. An analysis prepared for the California Budget Project by the Washington, DC-based Institute on Taxation and Economic Policy found that the proposed increase would be equivalent to:

- 0.82 percent of the income of the bottom fifth of Californians, an average of \$94 per year;
- 0.27 percent of the income of the middle fifth of Californians, an average of \$109 per year; and
- 0.007 percent of the income of the top one percent of Californians, an average of \$107 per year.

Who Is And Is Not Getting Paid?

In the absence of a budget, the Controller has continued to make payments that are for a prior year appropriation, required by federal law, authorized by the state Constitution, or made pursuant to a continuous appropriation by state statute. Examples of programs protected by these provisions include the PERS and STRS retirement funds, State Disability Insurance, CalWORKs, In-Home Supportive Services, SSI/SSP, and most Medi-Cal services. The state is also making its debt service payments, disbursing income tax refunds, and paying most state employees their full salaries. The state is not making payments for goods and services provided after June 30, 2002 to state agencies, the University of California, trial courts, state highway transportation projects, or student financial aid in the form of CalGrants.

As of July 1, the Controller cut off payments to vendors that provide goods and services to the state and stopped paying the salaries of legislative staff, exempt appointees in state service, and elected officials, including state legislators and the Governor. The state will stop paying for abortion services and certain services for the disabled on September 1 if the Legislature does not pass a budget, according to State Controller Kathleen Connell. The Controller maintains the state does not have the authority to reimburse Medi-Cal providers who perform abortions or to fund regional centers and habitation services for the developmentally disabled after August 31.

What Happens If There Is No Budget?

Press reports state that the Governor will call the Legislature into special session if a budget is not reached by the August 31 scheduled adjournment of the Legislature. An earlier memo released by the Secretary of the State Senate outlined the rules applying to passage of legislation, including the budget, prior to the end of the legislative session. That memo states:

“The actual day the 2001-02 Session ends is November 30, 2002...The August 31 date is set to accommodate the provisions of the Constitution which give the Governor one month to sign bills and the public 90 days to review them, for purposes of potential referendum, prior to their January 1, 2003, effective date. All regular bills, therefore, must be passed by August 31. Urgency bills, statutes calling elections, tax levies, or appropriations for the usual current expenses of the state, can be taken up and passed after the August 31 deadline because they go into effect immediately and are not subject to referendum. However, they must be sent to the Governor by November 15, providing twelve days for him to sign or veto and three days for the Legislature to consider an override.

Bottom line: A budget bill may be taken up and passed any time after August 31 but no later than November 15 without any need for a special session. Urgency bills may be taken up. Tax levies may be taken up.”