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Does the Canciamilla – Richman Plan Pencil Out for California?

On June 17, Assemblymembers Joe Canciamilla (D-Pittsburg) and Keith Richman (R-Northridge) released a plan to bridge the state's budget gap. The plan increases the state's sales tax rate by ½ cent to repay bonds issued to finance the 2002-03 deficit, assumes that an increase in Vehicle License Fees would be triggered pursuant to existing law, and suspends the teacher tax credit for three years. The plan also calls for $5.5 billion in 2003-04 spending reductions above and beyond those included in the Assembly's version of the budget and increases state borrowing by selling $1.8 billion in bonds backed by the state's tobacco settlement payments, a proposal dropped by the Governor in his May Revision. Finally, the measure calls for a number of "fiscal reform" and "economic stimulus" measures.

This paper examines some of the major proposals contained in the Canciamilla-Richman plan. Many of the proposals included in the plan have been analyzed by the California Budget Project (CBP) in detail in papers available at www.cbp.org.

Fiscal Reform

Calls for structural reform have become hallmarks of recent budget plans. In January, the Governor stated that he wouldn't sign a budget unless it contained meaningful structural reform. In the face of inaction by the Legislature and acknowledging the difficulty of meaningful reform, the Governor scaled back his call in May, asking the Legislature to pass an on-time spending plan and work on reform for the remainder of the legislative session. The Canciamilla – Richman plan calls for:

- An unspecified change to the state's **spending limit**. The plan calls for a spending cap based on "population and inflation," but does not address how this proposal differs from the state's current cap that is based on population and inflation. A limit based on the Consumer Price Index (CPI) would be fundamentally incompatible with the formula that determines school spending under the Proposition 98 guarantee. Under normal ("Test 2") conditions, the inflation factor for the Proposition 98 guarantee is per capita personal income. Between 1979 and 2001, California per capita personal income increased by an average of 5.5 percent per year, while the California CPI increased by an average of 4.7 percent per year. Over time, the disparity between the inflation factor used for the spending cap and that used for Proposition 98 would steadily reduce the share of the budget available for programs outside the Proposition 98 guarantee. Proposition 140 of 1990 also tied the Legislature's budget to per capita personal income growth. If the state switched to a spending cap based on CPI, over time spending for K – 14 education and the Legislature would account for a steadily increasing share of the budget.
- **Narrowing the ability to enact fees by a majority vote** as clarified by a state Supreme Court decision in the Sinclair paint lawsuit. Voters defeated a prior attempt to narrow fee

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authority when they defeated Proposition 37, which appeared on the November 2000 ballot. For an analysis of a similar proposal, see the CBP's *Taxes vs. Fees: What Will Proposition 37 Mean for California*?

- Limiting spending to 95 percent of the revenues projected in the May Revision until the state builds **a 5 percent reserve**.
- Closing the state's current defined benefit pension plan to new state and local government employees and **requiring new employees to join a new defined contribution plan**. A defined benefit plan guarantees workers a fixed benefit based on salary and years of service. Under a defined contribution plan, workers' benefits would shrink if the value of their accounts declines, similar to the decline experienced by many private-sector workers during the current slump in the stock market.
- Reviewing and "reforming" existing state-mandated programs and increasing legislative oversight of public programs and policies.

The plan also calls for action on issues described as economic stimulus by the authors:

- Permanently extending the Manufacturers' Investment tax credit (MIC). Under current law, the credit would expire at the end of 2003, since it has failed to meet the job growth performance targets contained in existing law. For additional information on the MIC, see the CBP's *Unkept Promises: California's Manufacturers' Investment Tax Credit*.
- A call for workers' compensation reform, an end to "abusive commercial lawsuits," and "energy cost reform."

Revenues

The plan embraces some, but not all of the revenue increases assumed in the Governor's May Revision. The plan includes:

- A temporary ½ -cent sales tax increase dedicated to deficit bond retirement. The plan assumes the issuance of $10.7 billion in bonds to retire the current year shortfall, but would defer issuing $3.0 billion of debt until 2004-05.
- Rejection of the Governor's proposed 10.3 percent personal income tax rate and tobacco tax increase and accompanying realignment proposal.
- Sale of a second round of tobacco settlement securitization bonds to raise $1.8 billion in additional revenues. The Governor's May Revision rejected selling a second round of bonds due to market uncertainty and the high interest rates the state was required to pay on the first round of bonds.
- Suspending the teacher tax credit for three years, raising $175 million per year.
- Eliminating the income tax exclusion for lottery winnings. Since the original exclusion was contained in the ballot measure that created the lottery, repeal would potentially require voter approval.
- Allocating $1.42 billion in funds received as part of the state fiscal relief provisions of the recent federal tax bill evenly between 2003-04 and 2004-05.

The plan outlines a number of spending reductions in addition to those included in the Assembly's version of the budget and assumes adoption of $150 million of selected savings already scored by the Budget Conference Committee. Specifics include:

Education ($781 Million)

The plan would reduce 2002-03 education funding to the minimum level required by Proposition 98 for a savings of $162 million in 2003-04.[1] In the budget year, the plan shifts CalWORKs Stage 2 child care and the Early Start program under the Proposition 98 spending guarantee. In and of themselves, these shifts would not result in savings. In order to achieve savings, the Legislature would be required to cut $634 million out of spending currently under the guarantee, a $106 per pupil reduction in K – 12 spending. The reductions could be made to any program under the Proposition 98 guarantee, which includes child care, K – 12 education, and community colleges.

Higher Education ($461 Million)

The plan:

- Eliminates $138 million in spending for higher education outreach programs and increases student fees at the University of California and California State University by an additional 10 percent, on top of the 25 percent fee increase proposed in the Governor's January Budget and assumed in the Assembly's version of the budget.
- Increases Community College fees from $11 to $26 per unit, an increase of 136.4 percent. The Governor's May Revision proposed an increase to $18 per unit. The Governor's January Budget, which increased fees to $24 per unit, assumed that enrollment would fall by 5.7 percent in response to higher fees.
- Includes a $200 million unallocated cut to the University of California and California State University. The plan is silent on how the cut would be divided between the two systems and this reduction would be in addition to those already adopted by the Assembly spending plan, which were deeper than the cuts proposed by the Governor in the May Revision.

Health (Total Health and Social Services savings of $1.4 billion)

The plan:

- Includes a 10 percent reduction in the General Fund contribution to Medi-Cal provider reimbursement rates. The plan's authors state that they would use a portion of the funds the state will receive from the recently enacted federal tax bill to mitigate a portion of the rate reduction. However, it is unclear how this offset would work in practice. Medi-Cal recipients already suffer from a lack of access to physician services. A recent report issued by the Medi-Cal Policy Institute found that, "Nearly half of the physicians in California are unwilling to accept new patients covered by Medi-Cal, the state's health insurance program for low-income families and elderly, blind and disabled individuals. As a result, the supply of physicians available to Medi-Cal patients is significantly less than that available to the general population."

  A study by University of California at San Francisco researchers concluded that the Governor's proposed 15 percent reduction in Medi-Cal reimbursement rates for nursing

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[1] On June 30, the Legislature passed SB 1040, which deferred $80 million in 2002-03 Proposition 98 spending to 2003-04, thereby reducing current year education spending to the minimum guarantee level. By reducing the base from which the guarantee is calculated, this action lowers the level of funding required by Proposition 98 in 2003-04 for a combined current and budget year savings of approximately $160 million.

homes would have, “a dramatic effect on the profitability or ‘bottom-line’ losses of most free standing facilities in California…In the absence of any mitigating factors such as deep financial reserves, it is hard to imagine how the many facilities with projected financial losses could continue to staff adequately, deliver adequate care, and maintain resident safety.”

- Rescinds existing law that ensures that children have continuous eligibility for Medi-Cal for a year. The Department of Health Services estimated that continuous enrollment will extend health coverage to 471,500 poor children in 2003-04. The Assembly Budget assumed that the state will require adults to submit semi-annual status reports in order to maintain coverage.
- Eliminates 12 of the 14 Medi-Cal benefits targeted in the Governor’s May Revision, including psychiatric, chiropractic, acupuncture, and podiatric services, occupational therapy, optician and optical lab services, optometry, hearing aids, speech and audiology services, and physical therapy services. The plan rejects the Governor’s proposed elimination of durable medical equipment and medical supplies coverage.

Social Services

The plan:

- Reduces SSI/SSP cash assistance payments to the elderly, blind, and disabled to the federal minimum, a reduction of approximately 6 percent, for savings of $497 million. The Assembly Budget suspended the June 2003 and January 2004 cost-of-living adjustments. For a detailed analysis of this proposal, see the CBP’s April analysis, *Governor's 2003-04 Budget Proposes to Reduce Supplemental Security Income/State Supplementary Payment (SSI/SSP) Grants*. The 2002 Fair Market Rent for a studio apartment exceeds the SSI/SSP grant for a single individual in 12 counties, including Contra Costa, Alameda, Orange, and San Francisco. Since SSI/SSP recipients do not receive food stamps (they do qualify for Medi-Cal), their grants must cover not only rent, but also food, transportation, clothing, and other necessities.
- Suspends cost-of-living adjustments for CalWORKs recipients for three years. As a result of the elimination of cost-of-living adjustments between 1990-91 and 1997-98 and grant reductions during the same period, the purchasing power of the current maximum CalWORKs grant is 30.0 percent lower than it was in 1989-90 (after taking into account the June 2003 cost-of-living-adjustment). For a detailed analysis of the impact of this proposal, see the CBP’s April report *CalWORKs at a Critical Juncture: A Review of Caseload Trends and the Governor’s Proposals*.
- Eliminates state programs that provide benefits to legal immigrants who lost eligibility for federally funded assistance as a result of the 1996 federal welfare law. The California Food Assistance Program (CFAP) would provide food stamps to 11,400 legal immigrants in 2003-04, while the Cash Assistance Program for Immigrants (CAPI) would assist 9,720 legal immigrants in 2003-04 who are elderly, blind, or disabled.
- Reduces support for child welfare services by capping the amount the state pays counties for child welfare services caseworker costs ($21 million) and shifting to quarterly caseworker visits ($8 million).

Criminal Justice ($150 million)

The plan:

- Eliminates rural county law enforcement grants ($19 million) and the COPS program ($116 million), eliminates the gang violence reduction program ($2 million), and eliminates the young men as fathers program ($1 million), and suspends juvenile justice grants for three years for annual savings of $116 million.
- Adopts a number of proposals included in the Senate's budget that reform parole services and restructure correctional education for combined savings of $80 million. The plan also adopts the Senate's proposed increase in trial court fees ($50 million) and the Governor's proposal to reduce and restructure trial court spending, both of which were rejected by the Assembly, for annual savings of $53 million.

General Government ($400 million)

The plan:

- Eliminates the California Arts Council ($8 million), state support for the Science Center ($13 million), the Fair Employment and Housing Department and Commission ($15 million), the Office of Planning and Research and the Commission on the Status of Women ($5 million), the Film California First program ($6 million), and the Cesar Chavez Grant Program ($5 million).
- Establishes a second tier in the state and local government employees' pension fund for new employees. This proposal would have minimal ($1 million) savings in 2003-04, but larger savings in future years. As noted above, the shift would deny new employees access to the state's current retirement system that bases benefits on salary and years of service. Under this proposal, new employees' retirement benefits would be based on the performance of their investment accounts.
- Increases savings from state employee compensation from 8 percent to 10 percent. The plan is silent on how these savings would be achieved.
- Shifts $81 million in funding for housing projects to bond support.
- Caps general obligation bond debt issuance at $3.5 billion per year. This proposal would potentially limit the state's ability to issue bonds for schools, water programs, transportation, and other traditionally debt-financed investments or shift a greater share of the burden of infrastructure finance to lease-revenue debt that is traditionally more costly than general obligation debt.
- Eliminates remaining General Fund support for trade and commerce programs ($28 million).

Local Government

- The plan assumes a one-time $500 million reduction. Neither the method for achieving the savings nor the allocation of the cut among different types of local governments is specified. The plan would also eliminate the state's reimbursement of cities for booking fees charged by county jails ($38 million) as well as $564 million worth of unspecified mandates in 2004-05.

Transportation

- The plan increases the net transfer to the Transportation Investment Fund relative to the proposal adopted by the Assembly by $438 million.

The Bottom Line

The Legislative Analyst estimates that the Canciamilla-Richman plan would leave the state facing a $1.4 billion shortfall in 2004-05 (as compared to a $8.6 billion shortfall under the Assembly's Budget plan), and a $3.3 billion shortfall in 2005-06. Failure to enact any of the specified spending reductions and/or tax increases outlined in the plan would widen the gap in 2004-05 and beyond.

Jean Ross prepared this paper. The California Budget Project (CBP) was founded in 1994 to provide Californians with a source of timely, objective, and accessible expertise on state fiscal and economic policy issues. The CBP engages in independent fiscal and policy analysis and public education with the goal of improving public policies affecting the economic and social well-being of low- and middle-income Californians. General operating support for the California Budget Project is provided by foundation grants, individual donations, and subscriptions. Please visit the CBP's web site at www.cbp.org.
