

Starving the Monster or Preparing for the Future: What Does the Governor's Proposed 2005-06 Budget Mean for California?

California Budget Project
921 11th Street, Suite 502
Sacramento, CA 95814
(916) 444-0500
cbp@cbp.org
www.cbp.org

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The Bottom Line

- ▶ The Governor's Proposed Budget:
 - Outlines \$9.1 billion in “solutions” to the state’s ongoing budget gap in the current and upcoming budget years. The state faces a shortfall of approximately \$8.6 billion in 2005-06.
 - Addresses a gap that is largely **structural**. A structural gap can only be closed by permanently increasing revenues, permanently reducing spending, or some combination of the two.
 - Relies on borrowing, deep reductions in education, social services, state employees’ compensation, and transportation spending, but no new taxes, to bridge the budget gap.
 - Would leave the state facing a shortfall of approximately \$5 billion in 2006-07 if fully enacted, because of its reliance on one-time solutions.
- ▶ Options for closing future years’ gaps are limited due to the passage of Proposition 1A, which requires the state to reverse the two-year property tax shift included in this year’s budget agreement, and could be further constrained if the Governor’s proposed constitutional changes are enacted.

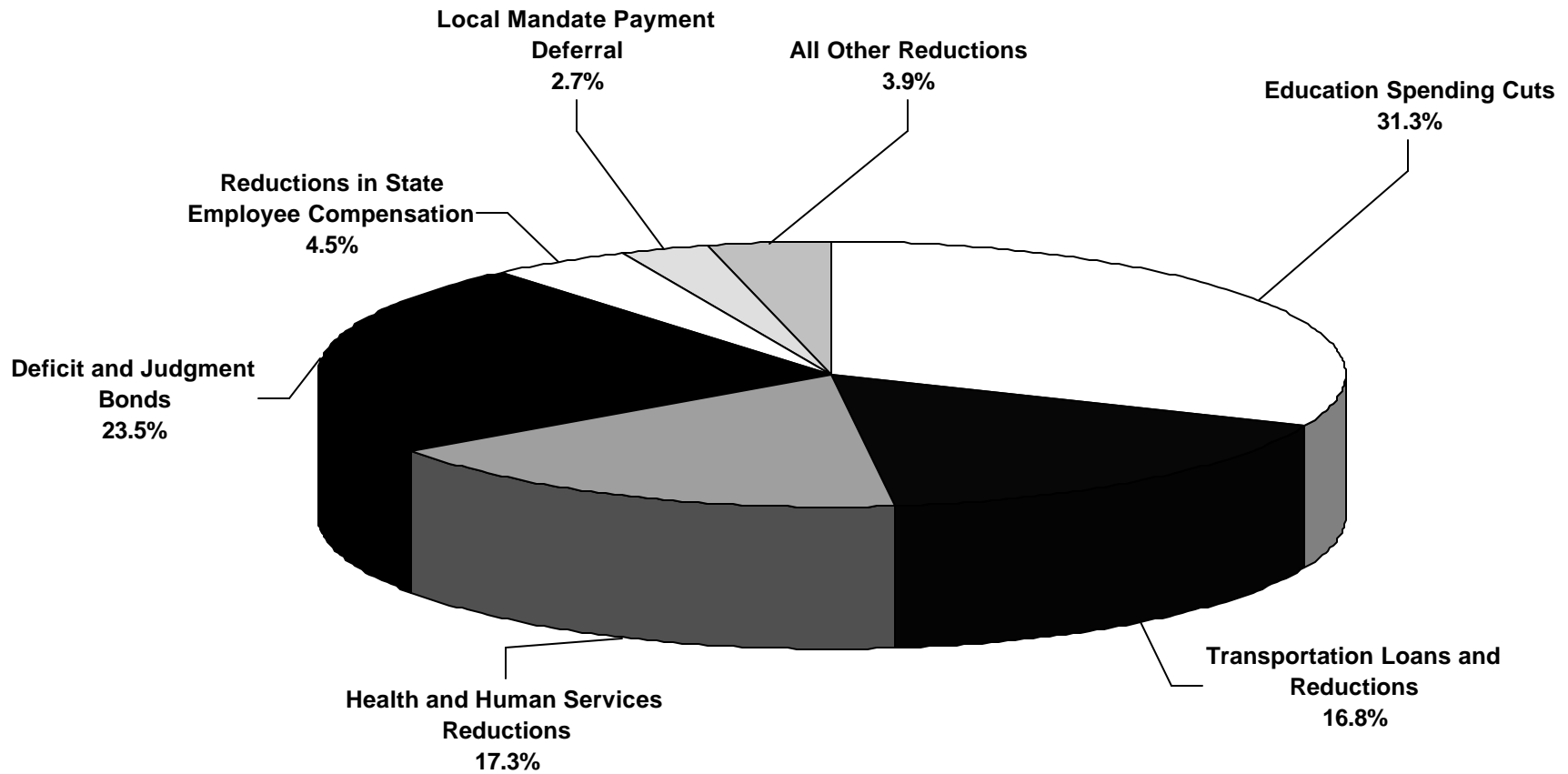
Californians Face Critical Choices

- ▶ The Governor's Proposed Budget, and the constitutional amendments proposed by the Governor, pose critical choices for the future of California:
 - What is the best way to bring the budget into balance?
 - Should the state continue to rely on debt and spending reductions to balance the budget, or should additional revenues be part of the solution to the budget crisis?
 - How can public policies contribute to an economic future that brings prosperity to all Californians?

How Does the Governor's Budget Close the Gap?

- ▶ **\$4.9 billion in program reductions and savings**, including \$2.8 billion in reductions in K - 14 education, \$714 million in CalWORKs and SSI/SSP grant reductions, \$195 million in reduced state wage payments for In-Home Supportive Service workers, and \$408 million in reductions in state employee pensions and compensation.
- ▶ **\$2.1 billion in borrowing**, including \$1.7 billion from the proceeds of the deficit reduction bonds authorized by Proposition 57 and \$464 million in new borrowing to pay the state's obligations in a legal settlement for flood damage. In addition, the Governor proposes to issue a \$765 million pension obligation bond using authority provided in the 2004-05 budget agreement.
- ▶ **\$1.3 billion in loans from Proposition 42 transportation funds**. This loan would be repaid over 15 years. The state has already borrowed \$2.1 billion from the same funds in 2003-04 and 2004-05.
- ▶ **\$250 million in deferred reimbursements to local governments for mandated programs and services**. Beginning in 2006-07, the state must reimburse local governments for mandates or the mandates will be suspended.
- ▶ **\$542 million from other measures**, including reductions to the Senior Citizens Renters and Property Tax Assistance programs, shifting the cost of certain prenatal services to federal funds, and additional revenues from stepped up tax enforcement efforts.

How Does the Governor Propose to Balance the Budget? Percentage of Total "Solutions"



Total "Solutions" = \$9.1 Billion

Does California Have a Spending Problem?

- ▶ In his State-of-the-State address, the Governor argued that, “We don’t have a revenue problem. We have a spending problem.”
- ▶ In fact, state spending has not kept pace with the growth in personal income, a measure that takes into account population growth as well as taxpayers’ ability to pay. If General Fund spending equaled the same share of personal income in 2005-06 as it did in 1978-79, spending would be \$12.6 billion higher than the level proposed in the Governor’s Proposed Budget. If total spending equaled the same percentage of personal income in 2005-06 as it did in 1978-79, total spending would be \$1.7 billion higher than the level proposed in the Governor’s Budget.
- ▶ California falls in the middle of the states, ranking 24th in 2001-02, in total spending as a percentage of personal income. While California ranks relatively high with respect to health care spending, the state spends the least per Medicaid recipient and ranked 23rd with respect to the share of non-elderly persons with incomes below the poverty line who received their health coverage from Medicaid in 2003.

How Does California's Spending Compare to That of Other States?

State Expenditures as a Percentage of Personal Income, 2001-02

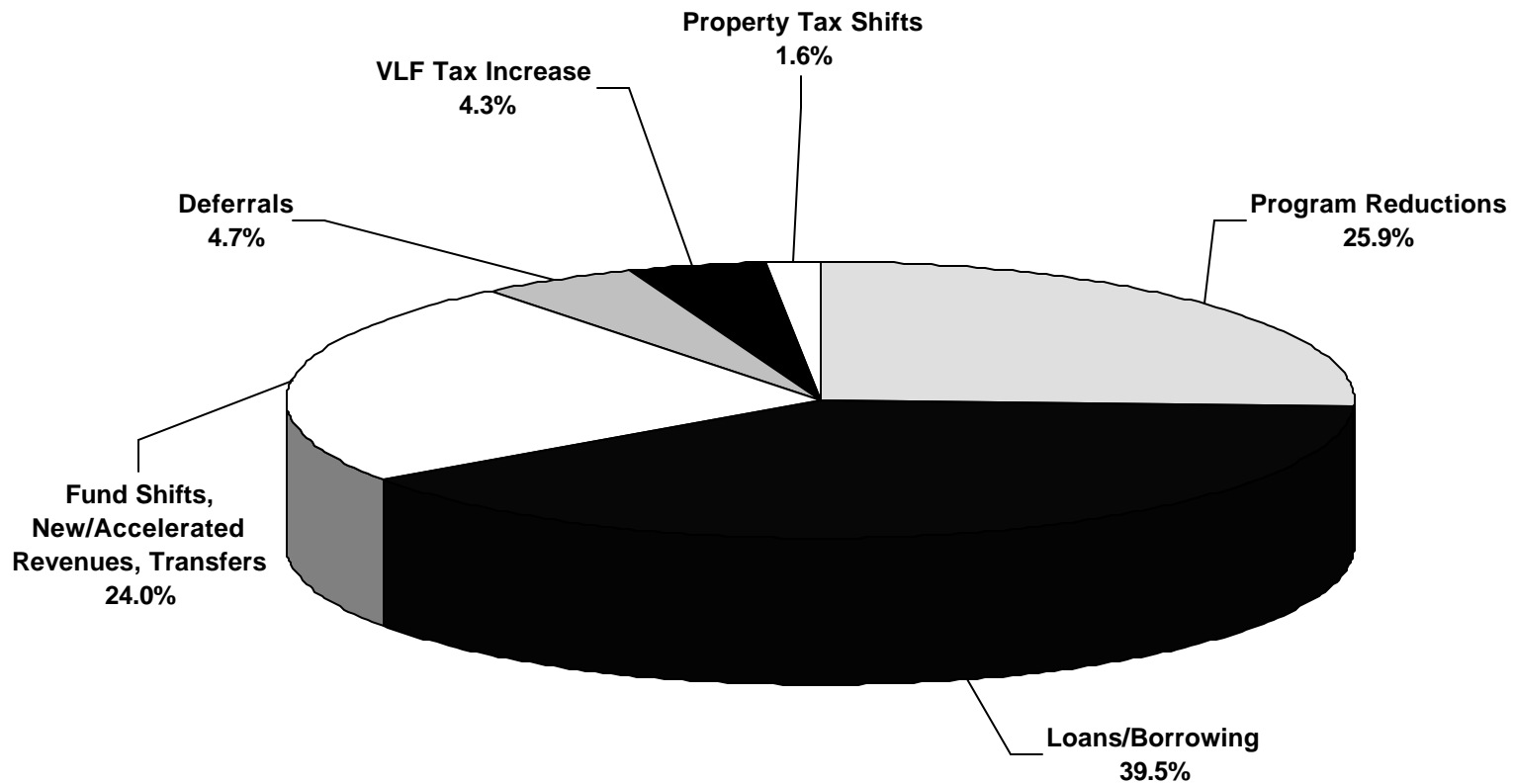
	<u>California Rank*</u>	<u>California</u>	<u>US</u>
Total Expenditures	24	16.2%	14.6%
General Expenditures	26	13.9%	12.6%
Education	29	4.7%	4.4%
Hospitals	24	0.4%	0.4%
Health	6	0.9%	0.6%
Highways	46	0.7%	1.0%
Police Protection	24	0.1%	0.1%
Corrections	16	0.5%	0.4%
Natural Resources	23	0.3%	0.2%
Parks and Recreation	20	0.1%	0.1%

*All rankings exclude the District of Columbia.

The Cost of Avoiding the Problem

- ▶ The proposed, current year, and prior year's budgets have largely relied on borrowing and other temporary solutions.
- ▶ The state's Legislative Analyst estimates that by 2004-05, the state had accumulated \$26 billion in budget-related debt, including \$18 billion in bonds, \$4 billion in loans from local governments, and approximately \$4 billion in loans from transportation and other special funds.
- ▶ Debt service on **existing** budget-related debt will cost the state nearly \$4 billion per year between 2006-07 and 2008-09.
 - The annual cost of budget-related debt service exceeds combined General Fund spending for the California State University (\$2.6 billion), Environmental Protection Agency (\$68.9 million), Child Protective Services Program (\$645.1 million), and Foster Care Program (\$412.7 million).
- ▶ The Legislative Analyst estimates that repayment of the \$26 billion of accumulated debt will account for over 40 percent of the operating deficits in the next several years' budgets.
- ▶ The Governor's Proposed Budget would add over \$4.2 billion to the state's outstanding budget-related debt, and includes new borrowing to pay off the settlement of a lawsuit related to flood damages and additional use of the deficit bonds authorized by Proposition 58.

How Have Past Budgets Been Balanced? Budget Solutions by Category, 2002-03 to 2004-05



Note: The Vehicle License Fee (VLF) tax increase of 2003-04 was subsequently reversed.

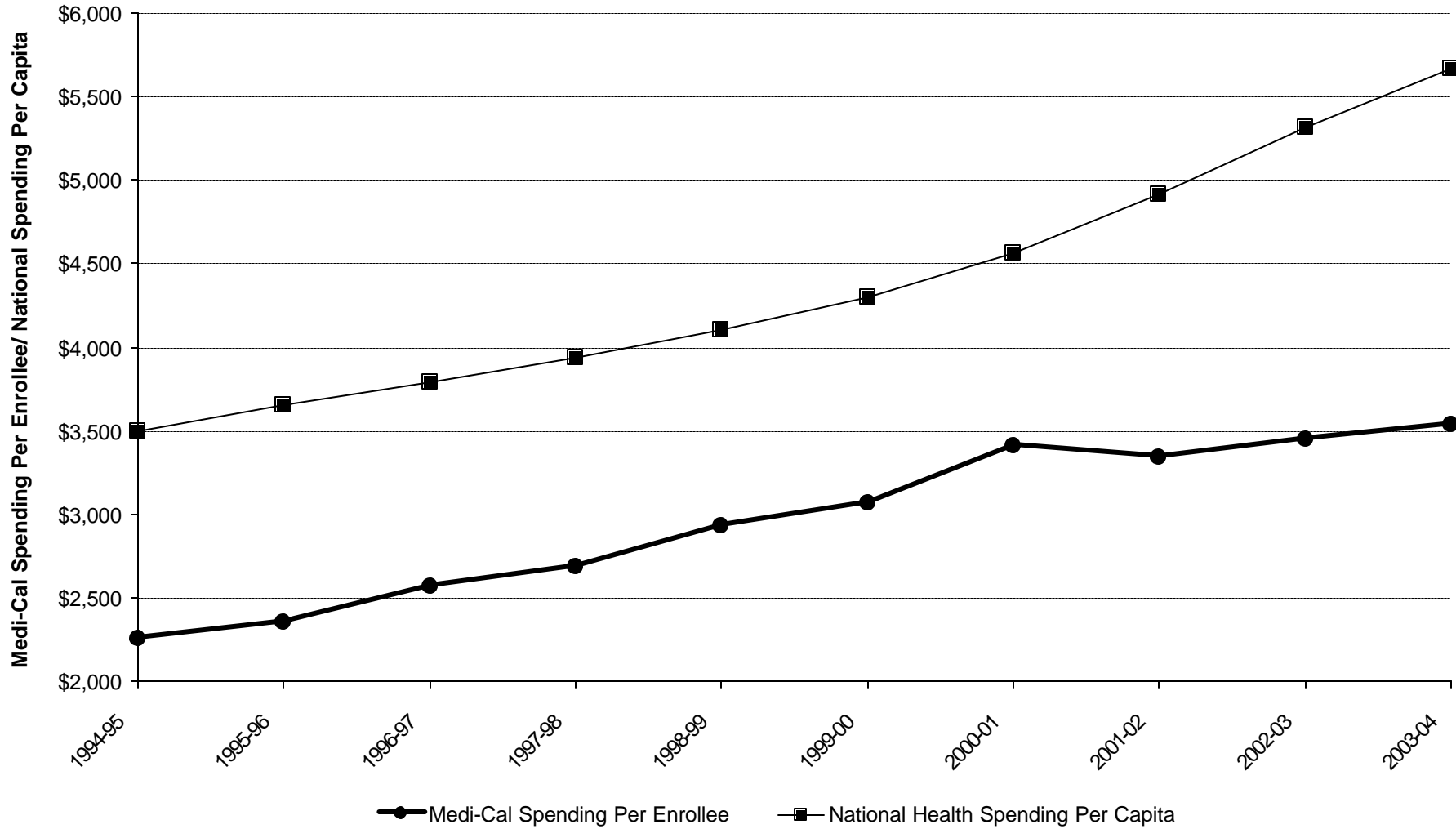
How Should We Look at the Budget?

- ▶ Budgets are typically structured (and budget deficits estimated) around the concept of a “current services” budget. A current services budget estimates the cost of providing the level of services authorized under current law, adjusted for inflation and population growth. A “current services” revenue estimate forecasts the revenues raised by the state’s current mix of taxes and fees, adjusted for changes in the economy.
- ▶ In order to understand whether the *purchasing power* of state spending has increased or decreased, it is important to understand the underlying cost, demographic, and policy factors that influence the delivery of services.
- ▶ Spending that simply keeps pace with inflation and population growth may not reflect the cost of delivering the same level of public services. This is particularly true since the costs of many key “drivers” in the state budget have increased more rapidly than inflation. The Consumer Price Index (CPI), which some argue should be used to measure the adequacy of public spending, is designed to measure increases in the cost of goods purchased by households, not governments.

What Factors Drive the Cost of Public Services?: The Health Care Example

- ▶ Health care accounts for 6.1 percent of the expenditures measured by the CPI, but accounts for approximately one out of five dollars spent by the state. The most common measure of national inflation (the CPI-U) increased by 27.5 percent between 1994 and 2004. In contrast, the Medical Care component of the CPI-U increased by 47.0 percent over the same period.
- ▶ State Medi-Cal spending per enrollee has actually increased at a lower rate than national per capita health care spending. Between 1993-94 and 2003-04, Medi-Cal spending per enrollee increased at an average annual rate of 4.4 percent, while national per capita health care spending increased at an average annual rate of 5.4 percent.
- ▶ California spends the least per Medicaid (Medi-Cal in California) recipient among the 50 states and the District of Columbia. In 2000, California's per enrollee spending was just over half (55 percent) as much as was spent in the Medicaid Program in the nation as a whole.

Spending Per Medi-Cal Enrollee Flattens While National Health Spending Continues to Rise

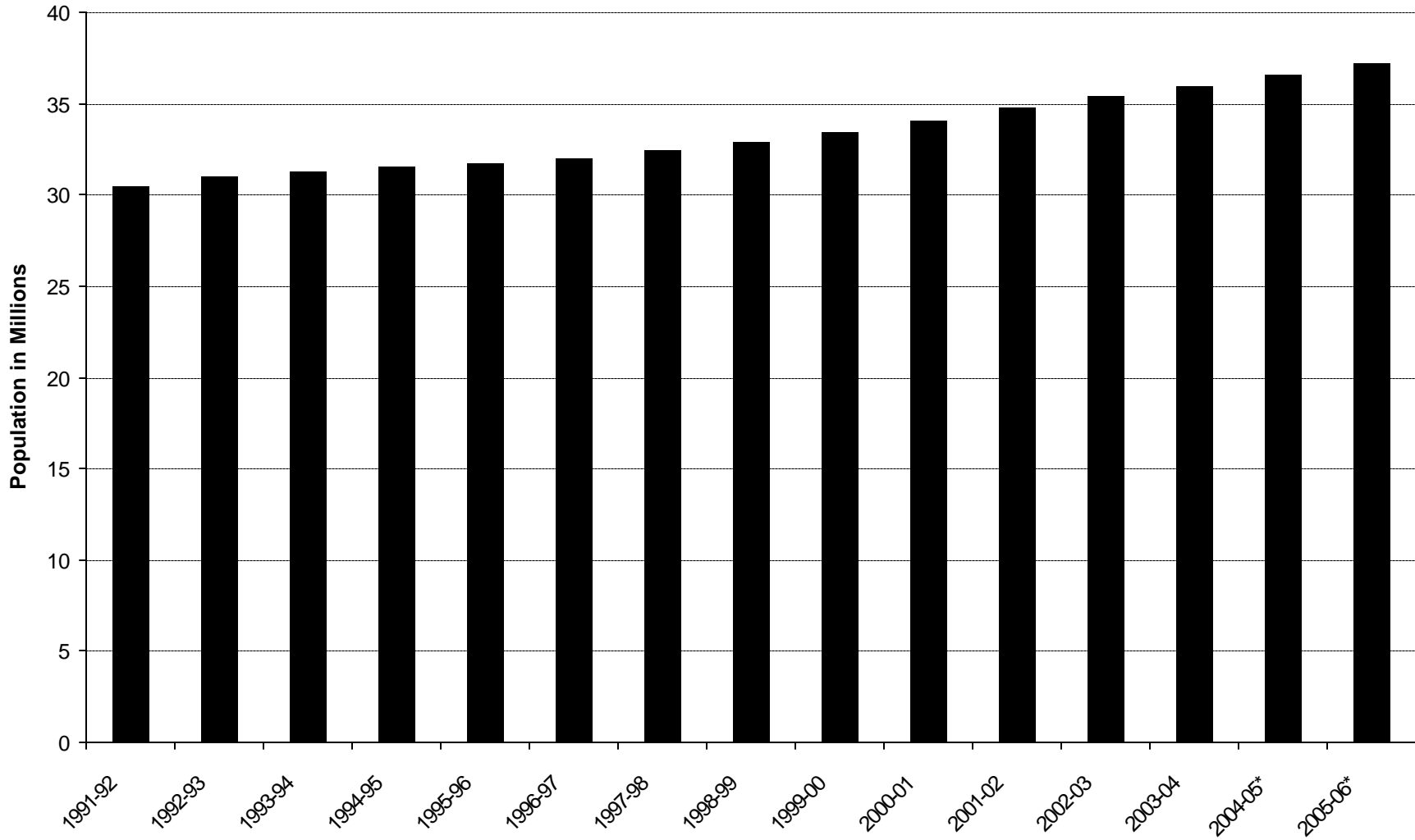


How Has the Need for Public Services Changed?

Recent demographic changes have increased demands on public services:

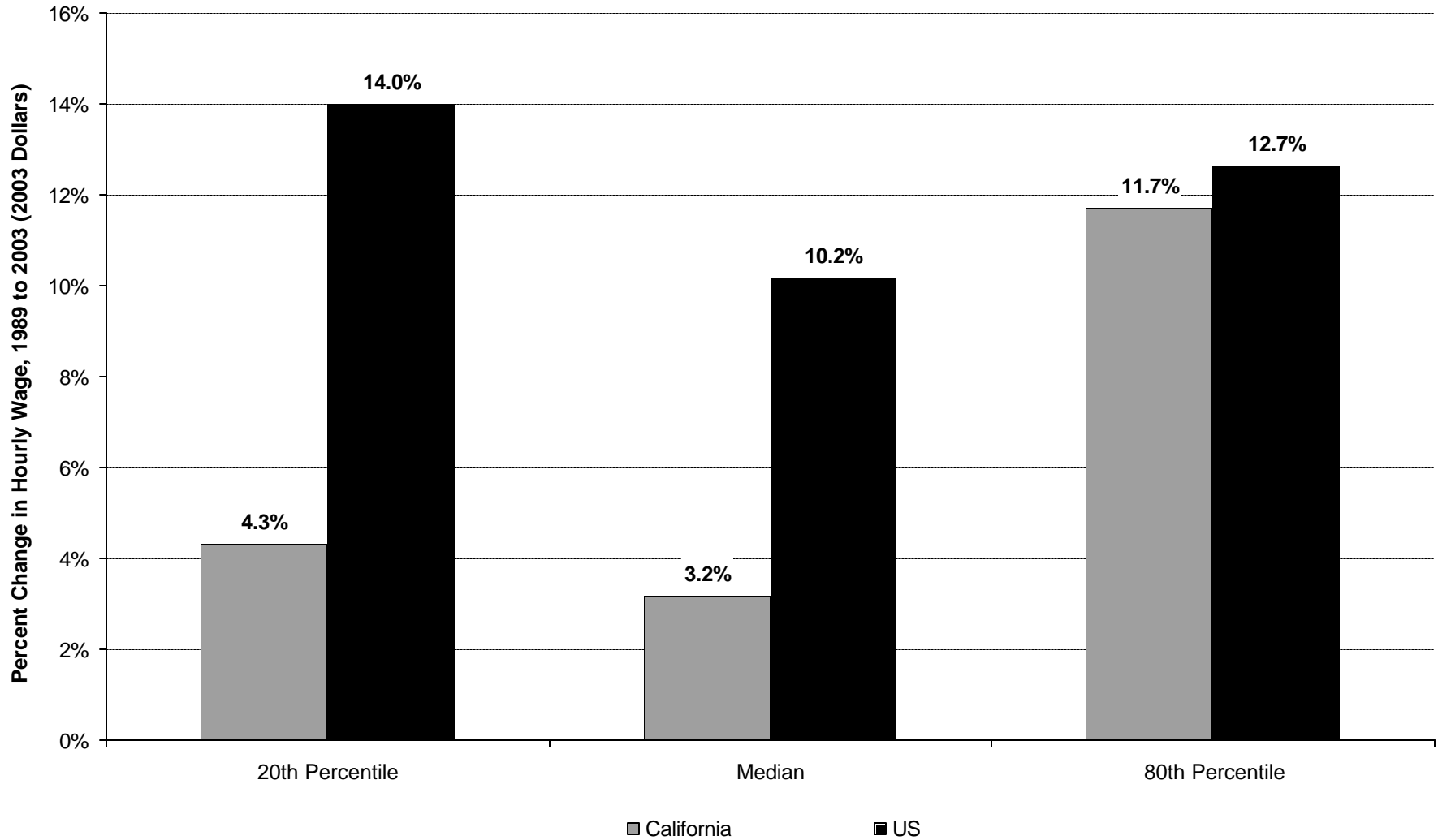
- Between 1994-05 and 2004-05, California added 5.1 million new residents, a 16.1 percent increase.
- Enrollment in California's public schools increased by nearly half a million (493,943) between 1994-95 and 2004-05.
- The number of Californians enrolled in public higher educational institutions increased by 515,301 between 1993 and 2003.
- The number of Californians under the age of 65 without health coverage increased by 1.8 million between 1987 and 2003.
- Growth in the hourly wages of many California workers has not kept pace with inflation. Between 1989 and 2003, the hourly wage of the worker at the midpoint (median) of the California wage distribution increased by 3.2 percent, while during the same period the hourly earnings of the median worker in the nation as a whole rose by 10.2 percent.

California's Population Continues to Rise

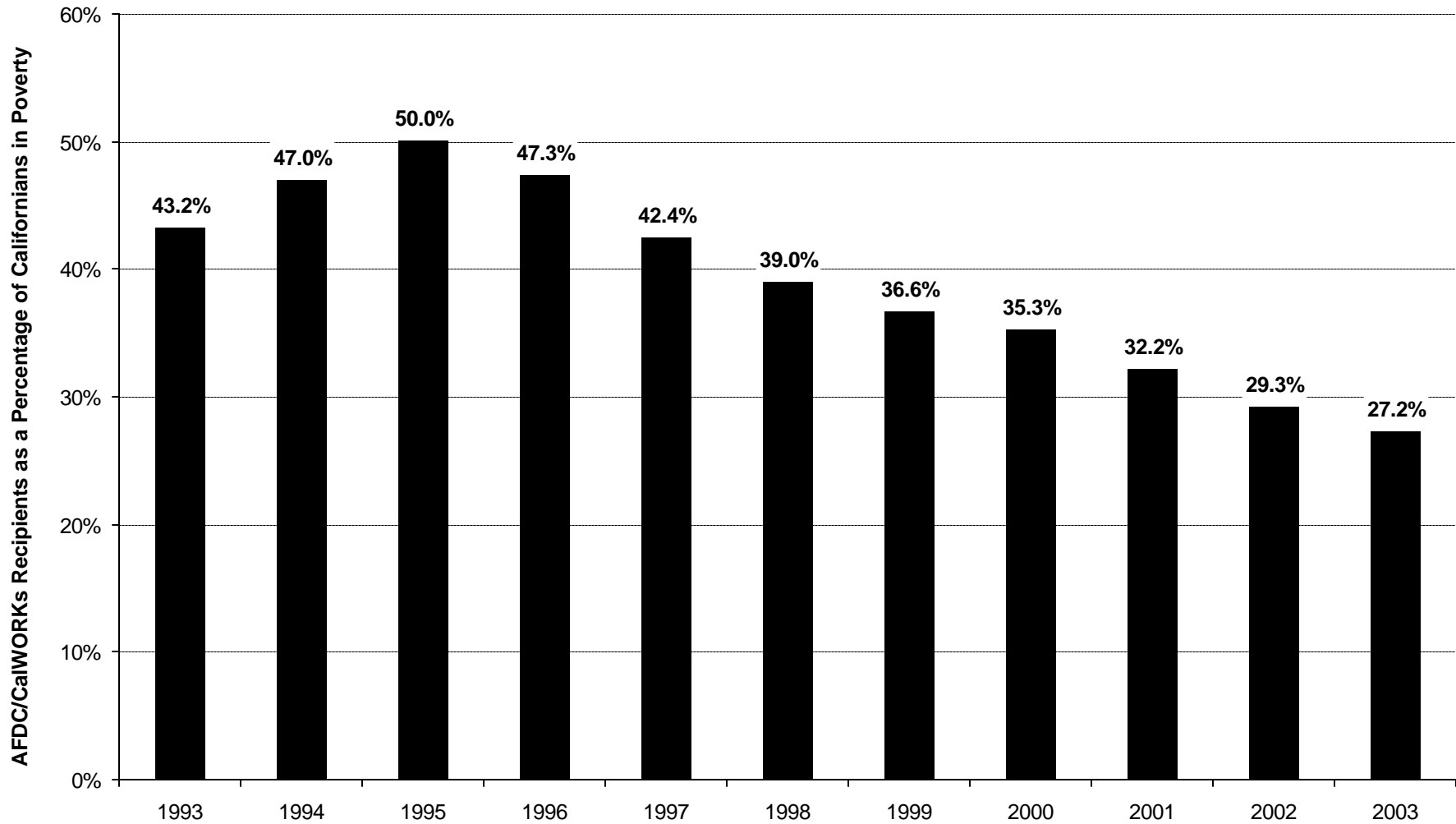


* 2004-05 estimated and 2005-06 projected.

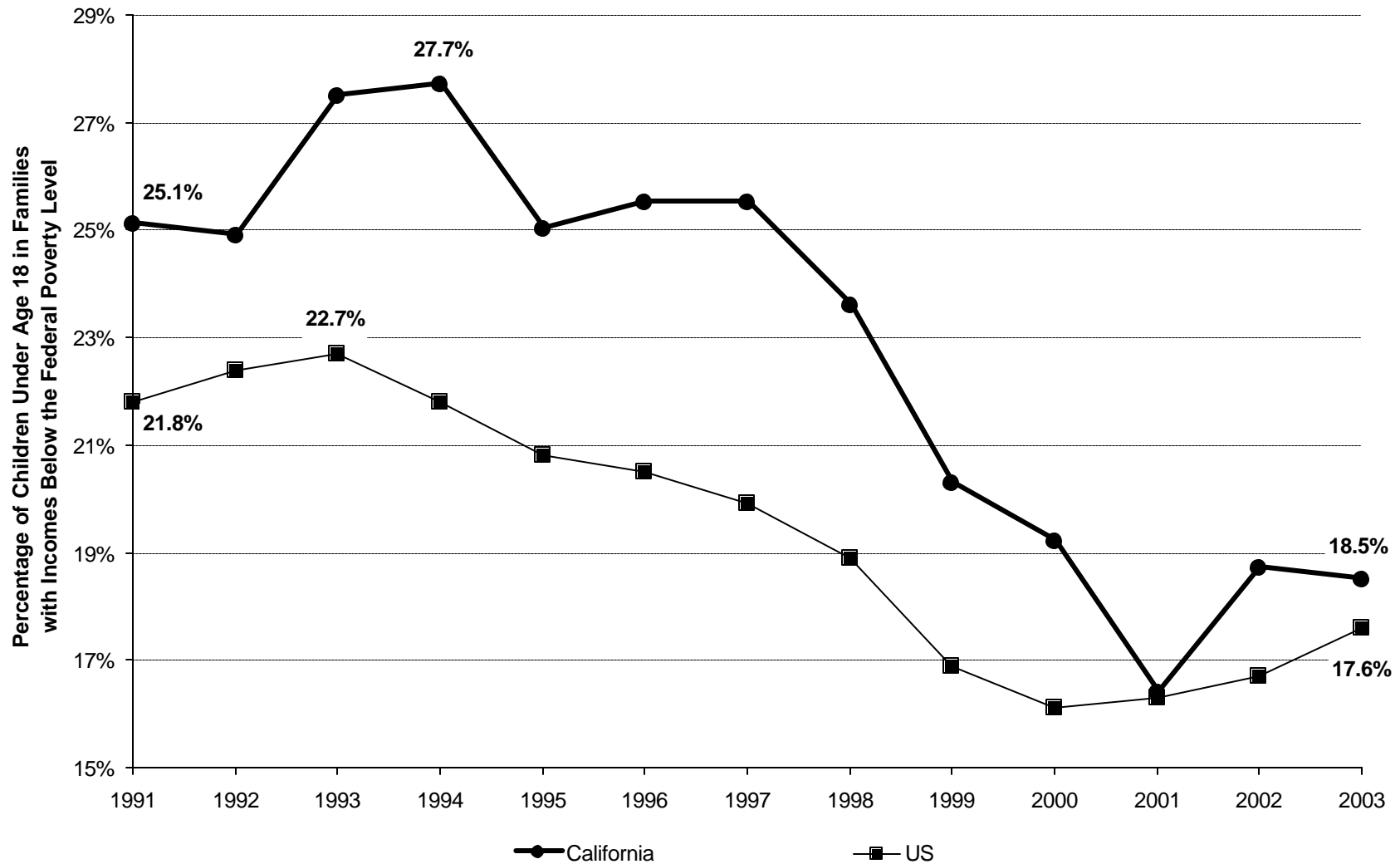
California's Wage Growth Lags Behind That of the US



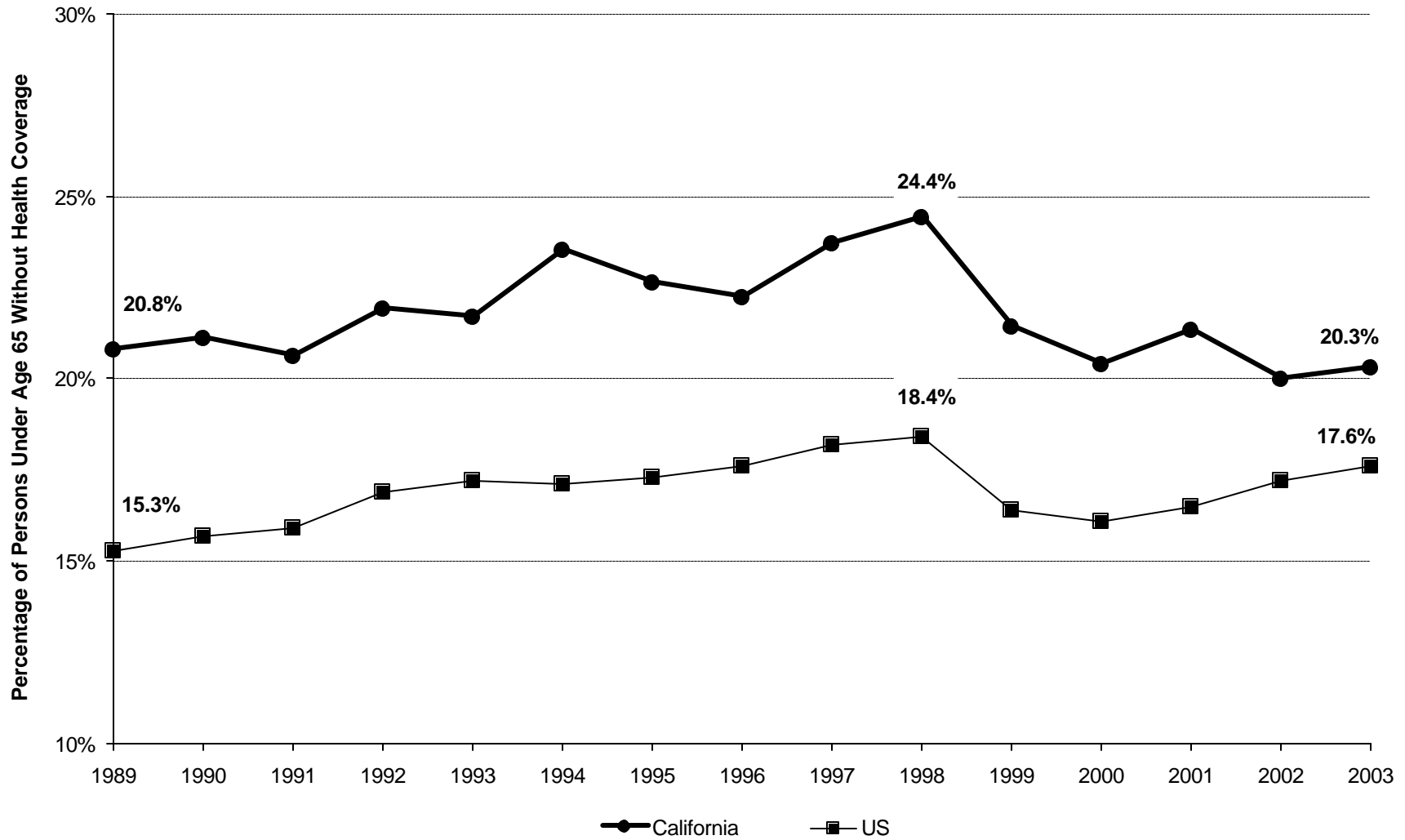
Californians in Poverty Are Less Likely to Receive Cash Assistance Than in Prior Years



Share of California's Children Living in Poverty Higher Than That of the Nation



The Share of Non-Elderly Californians Without Health Insurance Increased in 2003

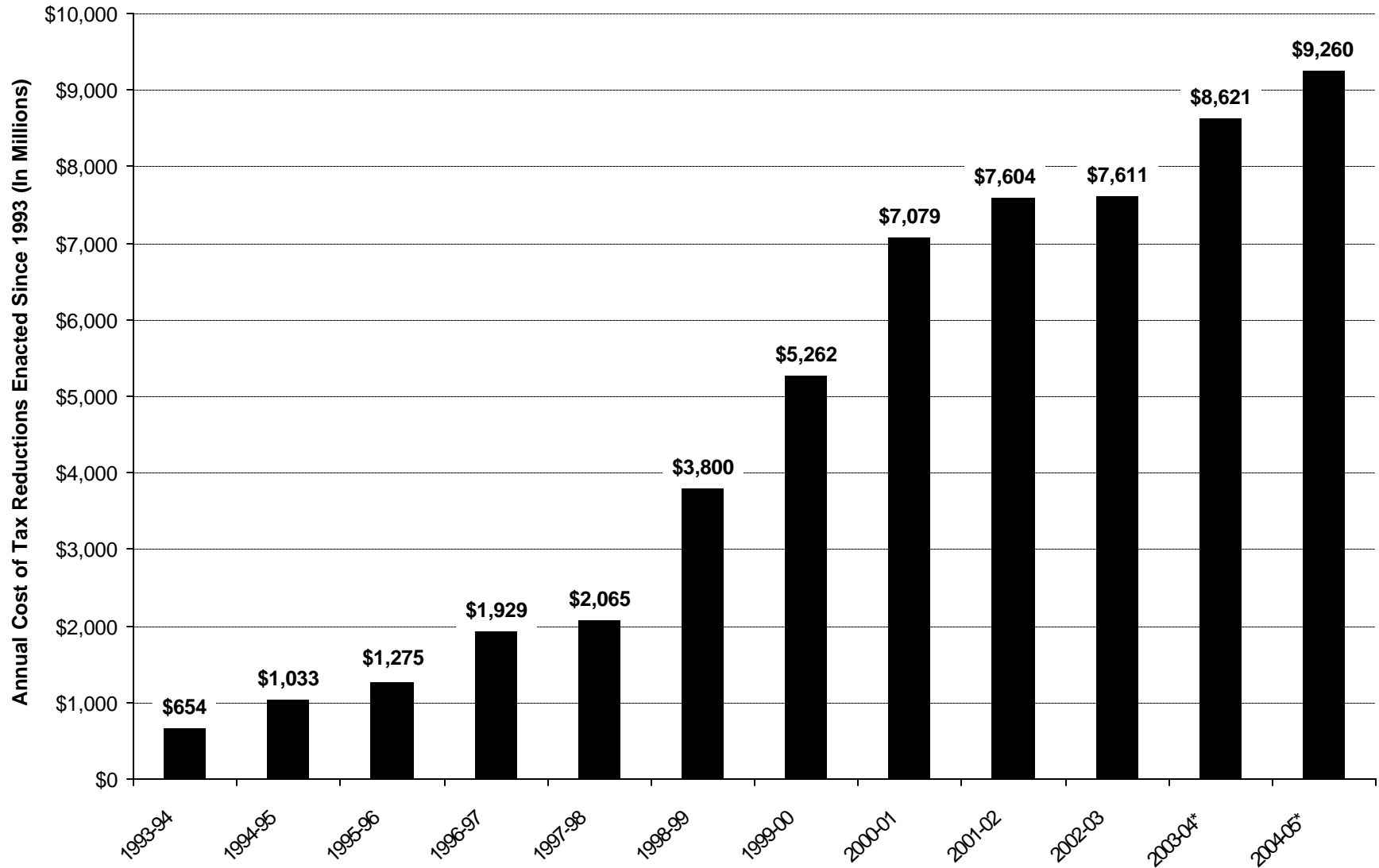


Note: Changes in survey methodology led to lower estimates of the number of uninsured persons beginning in 2000.

The Cost of Recent Tax Cuts Exceeds the State's Structural Budget Deficit

- ▶ While the Governor argues that California has a spending, not a revenue problem, the facts show that state lawmakers have enacted tax cuts that will cost the state an estimated \$9.3 billion in 2004-05 – an amount that exceeds the \$8.6 billion shortfall in the 2005-06 budget.
- ▶ The largest reductions include the Vehicle License Fee cut (\$4.5 billion), dependent tax credit increase (\$897 million), corporate tax rate reduction (\$467 million), and increased net operating loss deductions (\$478 million).
- ▶ Lawmakers have continued to cut taxes, despite the state's budget crisis. Bills passed in 2004 alone will reduce 2004-05 revenues by an estimated \$233 million.
- ▶ The phase-out of the federal estate tax will cost the state over \$1.1 billion in 2005-06. The 2001 federal tax package phased out the federal estate tax in 2010 and eliminated states' share of the tax beginning in 2005. Under current law, the estate tax would be reinstated in 2011. However, the President has proposed making the repeal permanent.

Tax Cuts Enacted Since 1993-94 Will Cost \$9.3 Billion in 2004-05

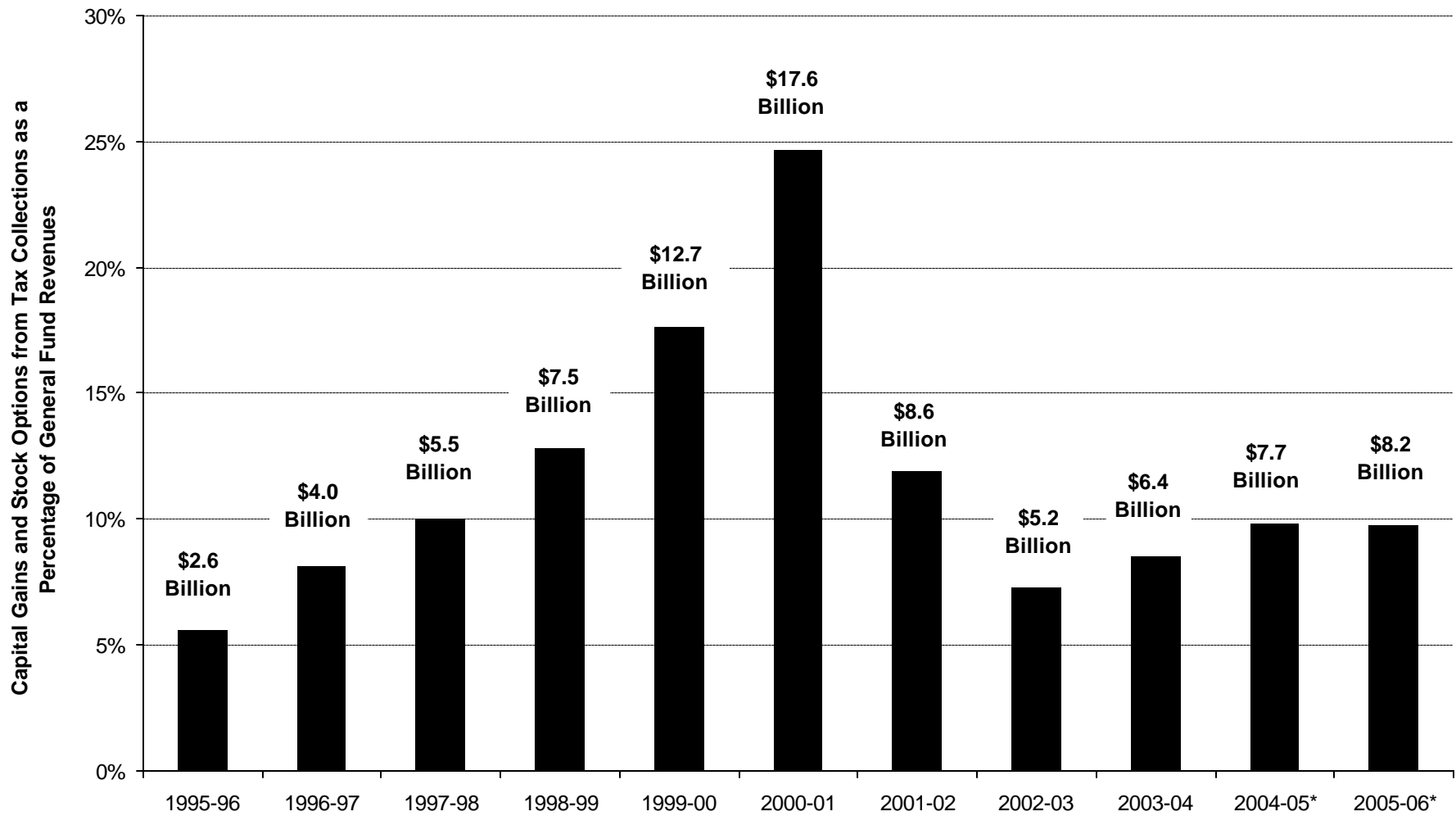


*2003-04 and 2004-05 estimated.

The Structure of the State's Tax System Contributes to the Budget Gap

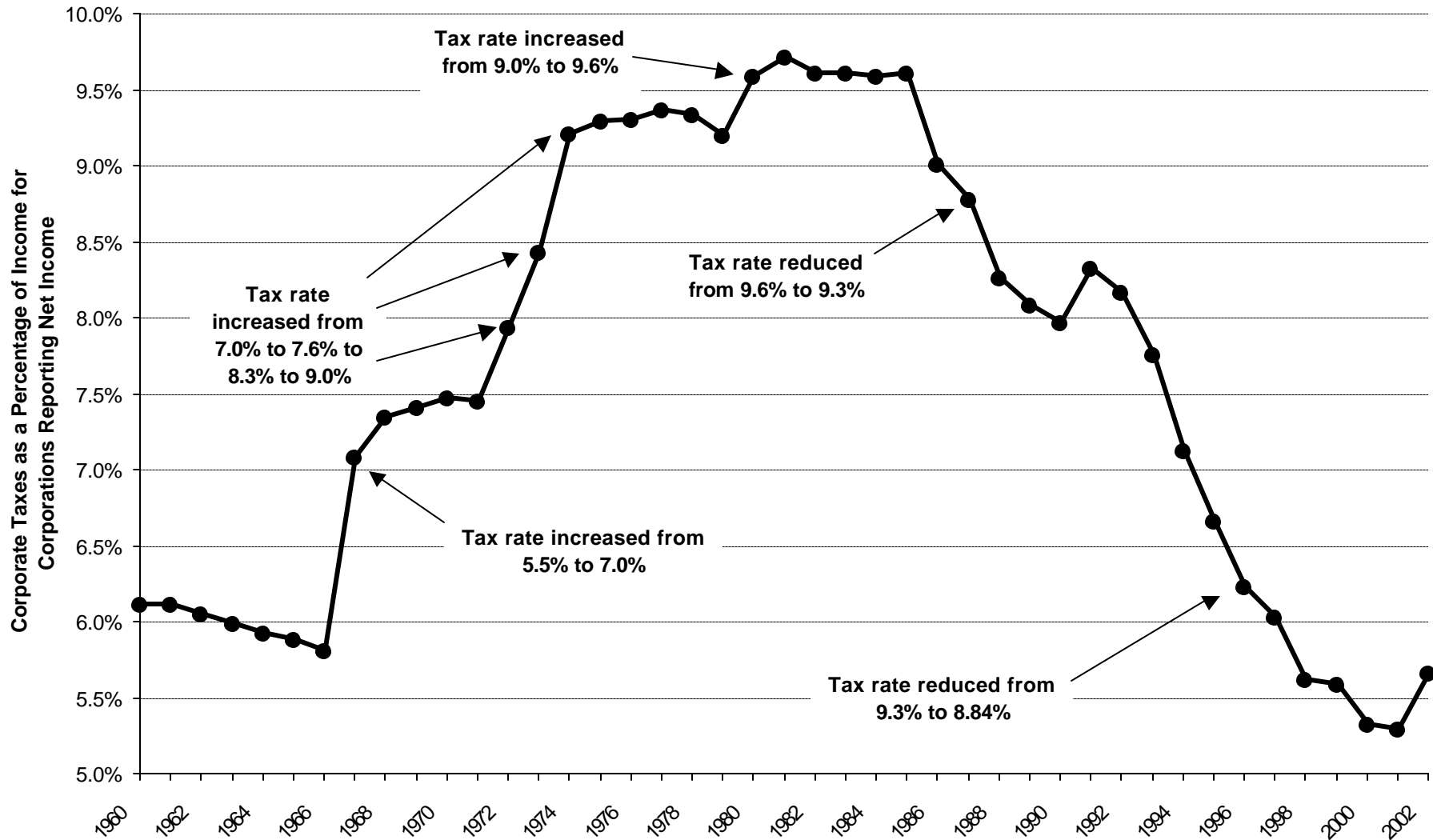
- ▶ The drop in tax collections attributable to stock options and capital gains exceeds the size of the state's structural budget gap. The state collected \$17.6 billion in income taxes paid on stock options and capital gains in 2000. The Department of Finance estimates that these sources of income will generate \$8.2 billion in tax revenues in 2005.
- ▶ Corporate income taxes have declined over time when measured as a share of total General Fund revenues and as a share of corporate profits.
- ▶ The yield of the state's sales tax has declined over time, reflecting broader economic trends, such as the shift in economic activity from goods to services and the rise of Internet and electronic sales that escape taxation.
- ▶ Alcohol and tobacco tax revenues have been stagnant over time, reflecting societal consumption trends.
- ▶ While the state's personal income tax has posted the most robust growth of all of the state's major taxes over time, the drop in collections related to stock options and capital gains is largely responsible for the structural budget gap.

Budget Gap Largely Due to Drop in Revenues from Stock Options and Capital Gains



* 2004-05 estimated and 2005-06 projected.

Despite Modest Increase in 2002, Share of Corporate Income Paid in Taxes Has Fallen 42 Percent Since 1981



Sales Tax Collections Have Declined as a Share of Personal Income



*2004-05 estimated and 2005-06 projected.

California's Tax System: How Does It Compare?

- ▶ Based on the most recent available data – which compares state tax collections at the peak of the boom – California's total state and local revenue burden was moderate compared to that of the nation as a whole. California ranked 18th among the 50 states on this measure in 2000-01.
- ▶ California's relatively high personal and corporate income tax collections are offset by significantly lower than average property tax collections. California also has relatively low motor vehicle fuel, alcohol, and tobacco tax burdens.
- ▶ The poorest fifth of California's non-elderly taxpayers pay the largest share of their incomes in state and local taxes. Yet, California's tax system is less regressive than those of most other states and the state tax threshold – the income level at which families are subject to the income tax – is the highest in the nation and high-income Californians pay the majority of the state's personal income tax.

How Does California Compare?

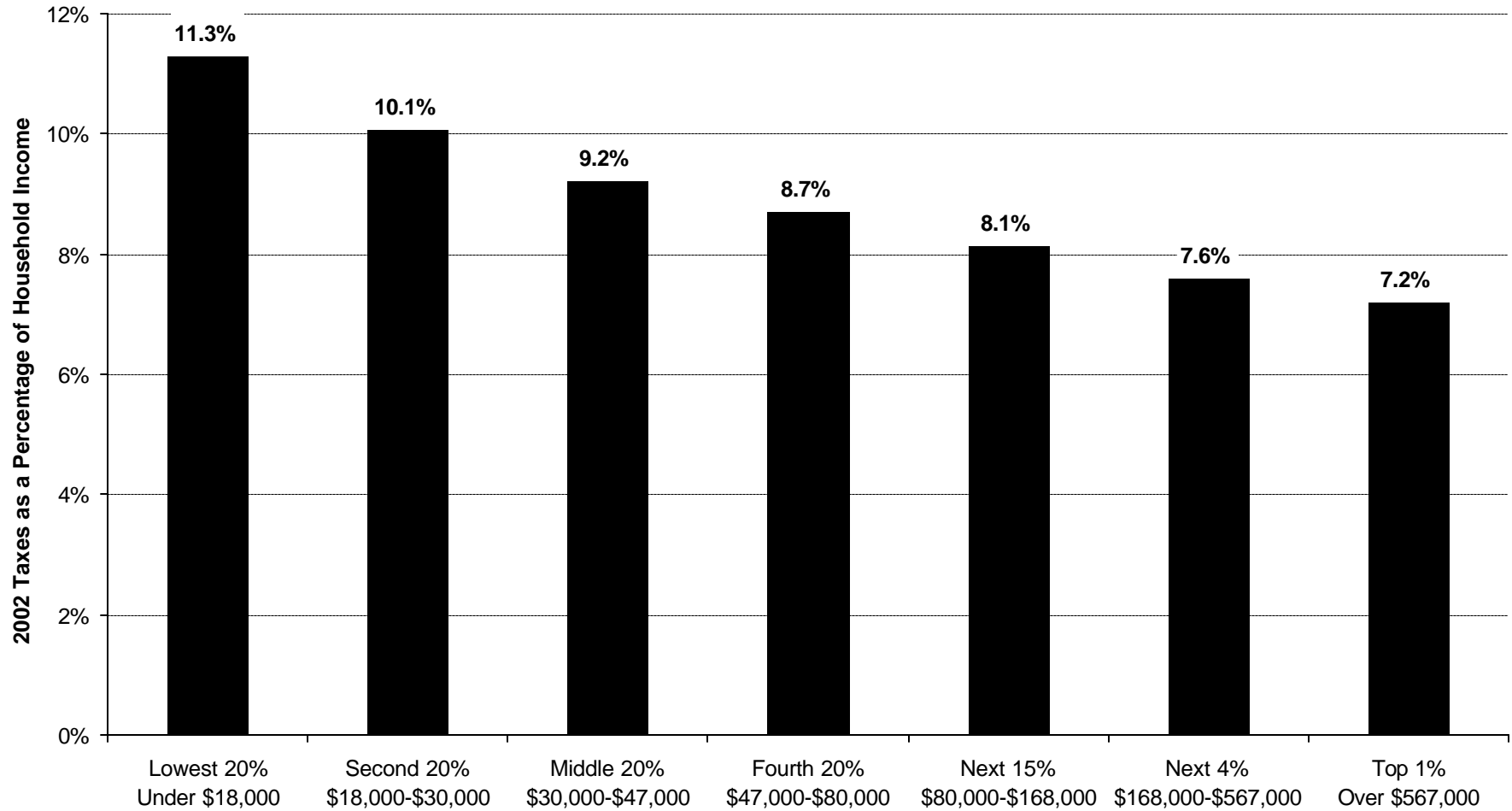
Revenues as a Percentage of Personal Income

	<u>California Rank^a</u>	<u>California</u>	<u>US</u>
Total State and Local Own Source (2001-02) ^b	18	15.69%	15.11%
Total State and Local Taxes (2001-02)	14	10.59%	10.32%
State Taxes (2002-03)	16	6.76%	6.06%
Local Taxes (1999-00)	32	3.47%	4.04%
State and Local General Sales Taxes (2001-02)	19	2.75%	2.54%
State and Local Property Tax (2001-02)	35	2.66%	3.18%
State General Sales Tax (2002-03)	27	2.13%	2.05%
State Motor Fuels Taxes (2002-03)	44	0.27%	0.36%
State Tobacco Tax (2002-03)	32	0.09%	0.13%
State Alcoholic Beverage Taxes (2002-03)	39	0.02%	0.05%
State Individual Income Tax (2002-03)	8	2.79%	2.02%
State Corporate Income Tax (2002-03)	6	0.59%	0.32%

^a All rankings exclude the District of Columbia.

^b Total Own Source revenues, which excludes federal government transfers, is the broadest measure of state and local government revenues.

Lowest-Income Households Pay the Largest Share of Their Income in State and Local Taxes



Note: Calculated for non-elderly, married couples. Includes offset for federal deductibility of state taxes.

The Governor Would Make Major Constitutional Changes Affecting the Budget

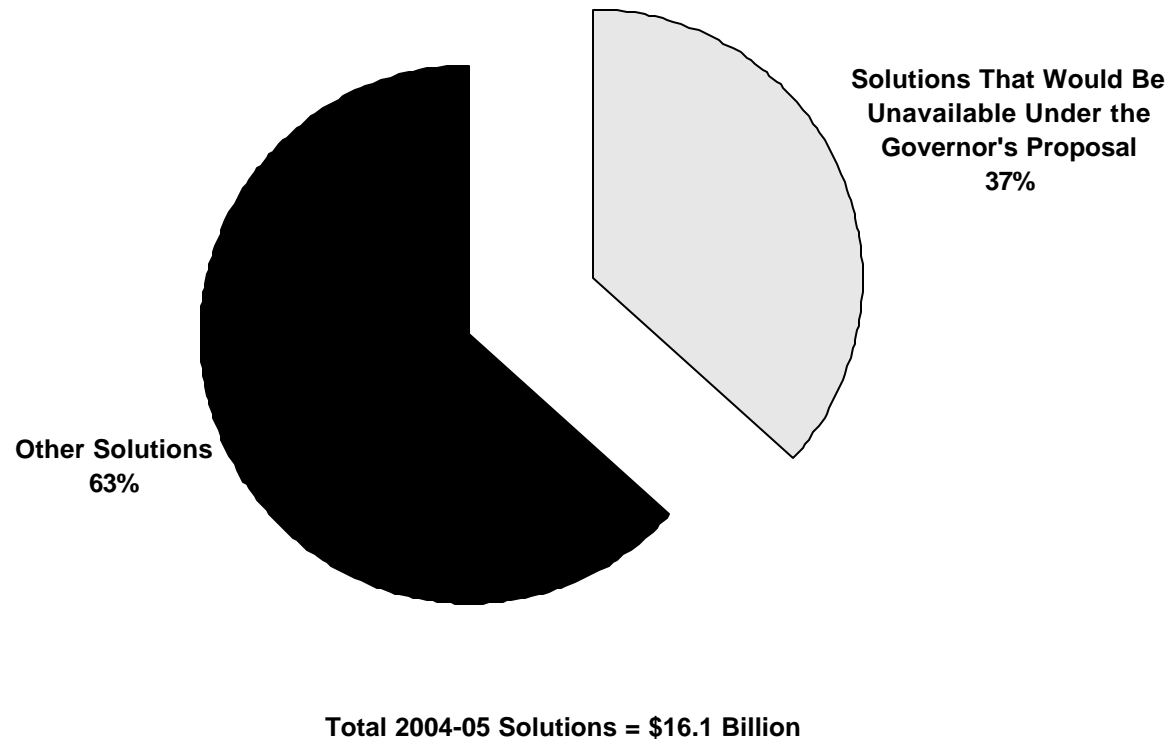
The Governor has proposed a constitutional amendment (ACAX1 4) that would:

- ▶ Require automatic across-the-board spending reductions if the Governor determines that expenditures will exceed revenues by \$250 million or more during the fiscal year.
- ▶ Implement the across-the-board reductions by reducing checks issued by the state from the General Fund and checks issued by a local government in proportion to the General Fund support for a particular program or service. The only exclusions would be payments for debt service, those required by federal law, and payments made on contracts executed before the effective date of the Governor's proposal.
- ▶ Eliminate the state's obligation to restore school funding levels in future years to make up for lower funding levels during the current budget crisis. This provision would reduce long-term education funding by more than \$3.5 billion per year.
- ▶ Eliminate a provision of the Proposition 98 school funding guarantee that allows a temporary reduction in school spending in "bad budget" years ("Test 3").
- ▶ Eliminate the Legislature's ability to suspend the Proposition 98 guarantee.
- ▶ Eliminate the Legislature's ability to suspend the transportation funding authorized by Proposition 42.
- ▶ Eliminate the state's ability to loan monies from Special Funds to help close a General Fund budget gap.

The Governor's Proposals Will Increase, Not Decrease, Autopilot Spending

- ▶ The Governor claims that “autopilot,” formula-driven spending is the source of the state’s budget problems. However, the Governor’s proposed constitutional amendment would put a much greater share of the budget on “autopilot” and eliminate the “safety valves” in several key programs that have been used to help close recent budget gaps.
- ▶ Proposition 1A, which ratified the Governor’s agreement with local governments, also results in “autopilot” spending by locking in state spending to make up for the 1998 Vehicle License Fee reduction and will significantly limit the state’s ability to reallocate local property tax dollars to generate state budget savings.
- ▶ The Governor-sponsored Proposition 49 of 2002 created a new spending obligation for after-school programs that cannot be reduced in the event of a budget shortfall.
- ▶ Had the Governor’s proposal and Proposition 1A been in effect in 2004, over a third of the “solutions” used to bridge this year’s \$16.1 billion budget gap would not have been available, forcing deep cuts in other areas of the budget.
- ▶ The across-the-board reductions required by the Governor’s proposal could:
 - Cause the state to lose federal matching funds.
 - Reduce the wages for state and local government workers below the state’s minimum wage.
 - Result in disparities between state workers, based on whether they are paid by General or Special Funds, and between school districts and community colleges based on their “mix” of state and local funds.

If the Governor's Proposed Constitutional Changes Had Been in Effect in 2004-05, More Than One-Third of the Solutions Used to Balance the Budget Would Not Have Been Available, Forcing Deep Cuts in Areas of the Budget Without Constitutional Protection

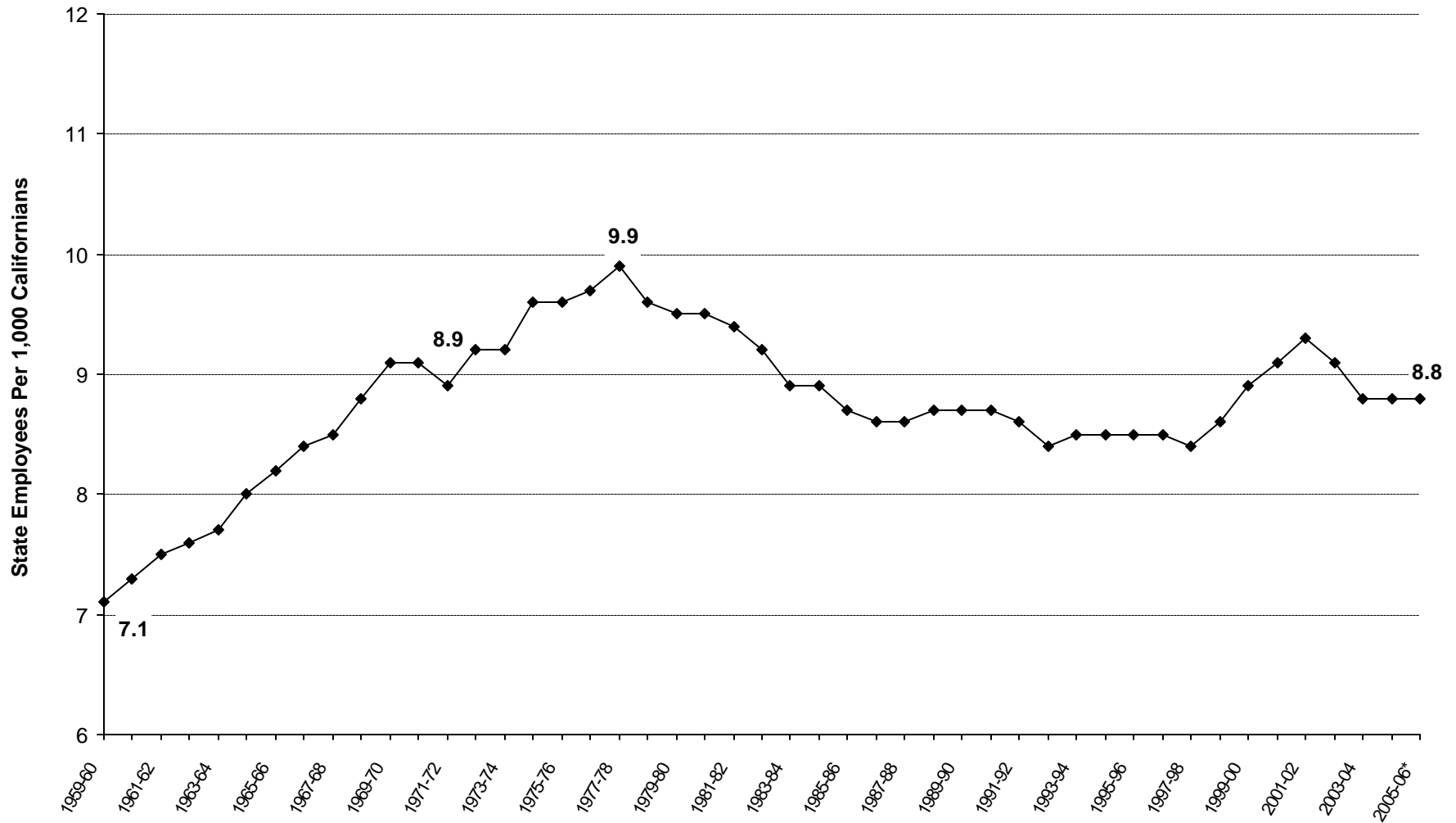


Note: Solutions that would not have been available include \$1.3 billion in property tax revenues shifted from local governments to schools.

California's State Government Is Relatively Lean; Most State Spending Occurs in Local Communities

- ▶ The ratio of state employees to state residents has remained relatively constant since the mid-1970s. The number of state employees per 1,000 Californians peaked in 1977-78, increased between 1997-98 and 2001-02, and has since declined. In terms of state employees per 10,000 population, California ranked 47th among the 50 states in 2003.
- ▶ Combined state and local government employment is also low relative to that of other states. California ranked 42nd among the 50 states with respect to state and local employment per 10,000 residents in 2003.
- ▶ Over three-quarters of the state's General Fund is spent in the form of "local assistance" – payments that go out to school districts, local governments, health care providers, and individuals.

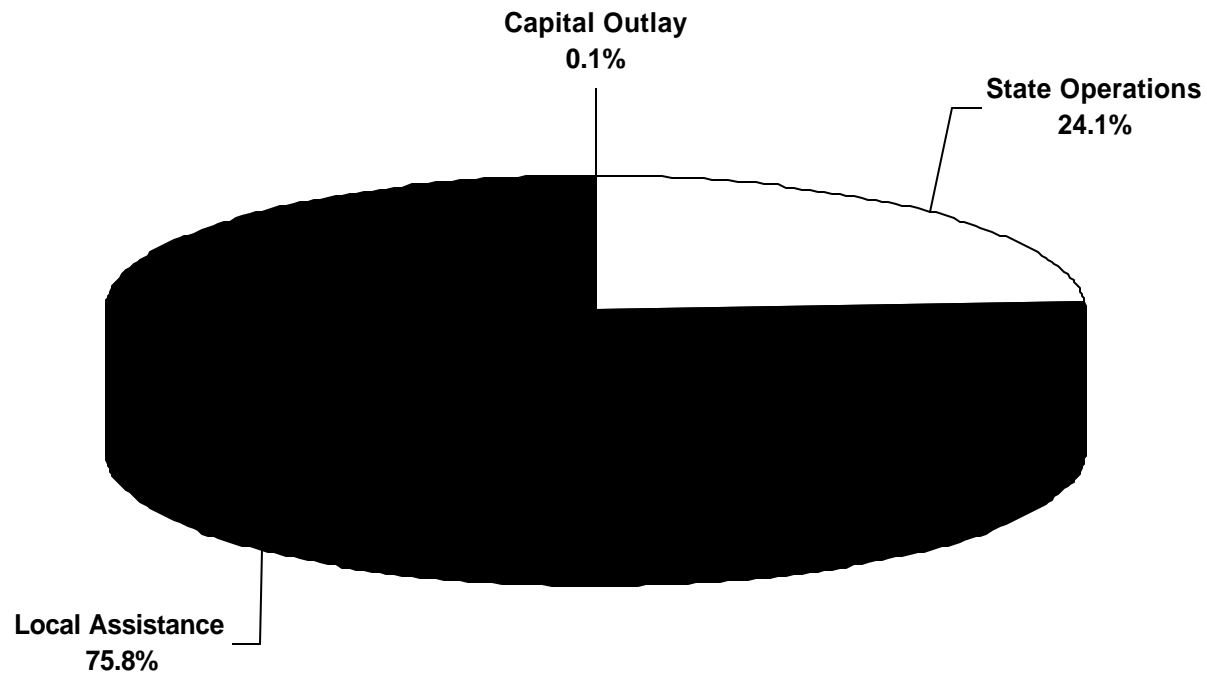
Number of State Employees Per 1,000 Californians Has Been Relatively Constant Since the Early 1970s



*2004-05 estimated and 2005-06 proposed.

How Does the State Spend Its Money?

2004-05 Estimated General Fund Spending



Note: Local Assistance includes funds for K-12 education, social services programs administered by counties, Medi-Cal provider payments, and other funds that flow to local governments and individuals, including CalWORKs and SSI/SSP cash grants. State Operations includes the California State University and the University of California.

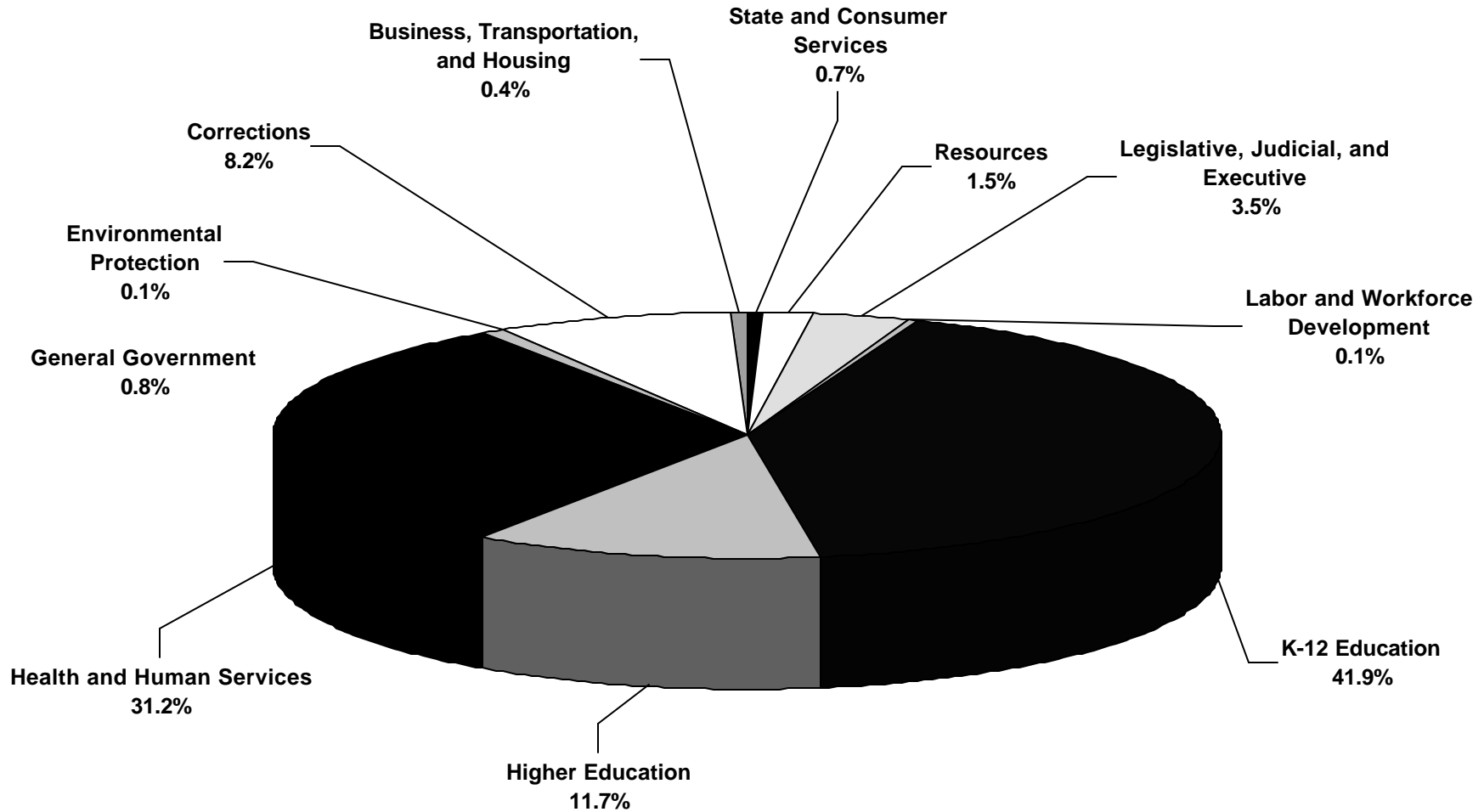
The Basics

The Governor's Proposed 2005-06 Budget:

- ▶ Increases General Fund spending by \$3.4 billion (4.2 percent) and assumes that available resources (including borrowed monies) will increase by \$5.2 billion (6.5 percent). Spending for health and human services programs would increase by \$1.2 billion, primarily due to caseload increases in Medi-Cal, SSI/SSP, and IHSS, offset by reductions in the CalWORKs, SSI/SSP, and IHSS programs. K - 14 education spending would increase by \$2.9 billion (including \$2.4 billion of state funds), which is \$2.3 billion less than would have been required absent the suspension of the state's school spending guarantee as part of the 2004-05 budget agreement.
- ▶ Assumes that General Fund revenues will increase by \$5.3 billion (6.8 percent) in 2005-06. Personal income tax revenues are expected to post a gain of 8.5 percent (\$3.4 billion) and sales and use tax revenues are forecast to increase by 7.1 percent (\$1.8 billion). Estate tax revenues will drop to zero, due to the phase-out of the federal tax, down from \$934.7 million in 2000-01.
- ▶ Uses the proceeds of \$1.7 billion in deficit refinancing bonds in 2005-06, down from \$2.0 billion in 2004-05.
- ▶ Provides a reserve of \$500 million, equal to 0.6 percent of proposed General Fund spending.

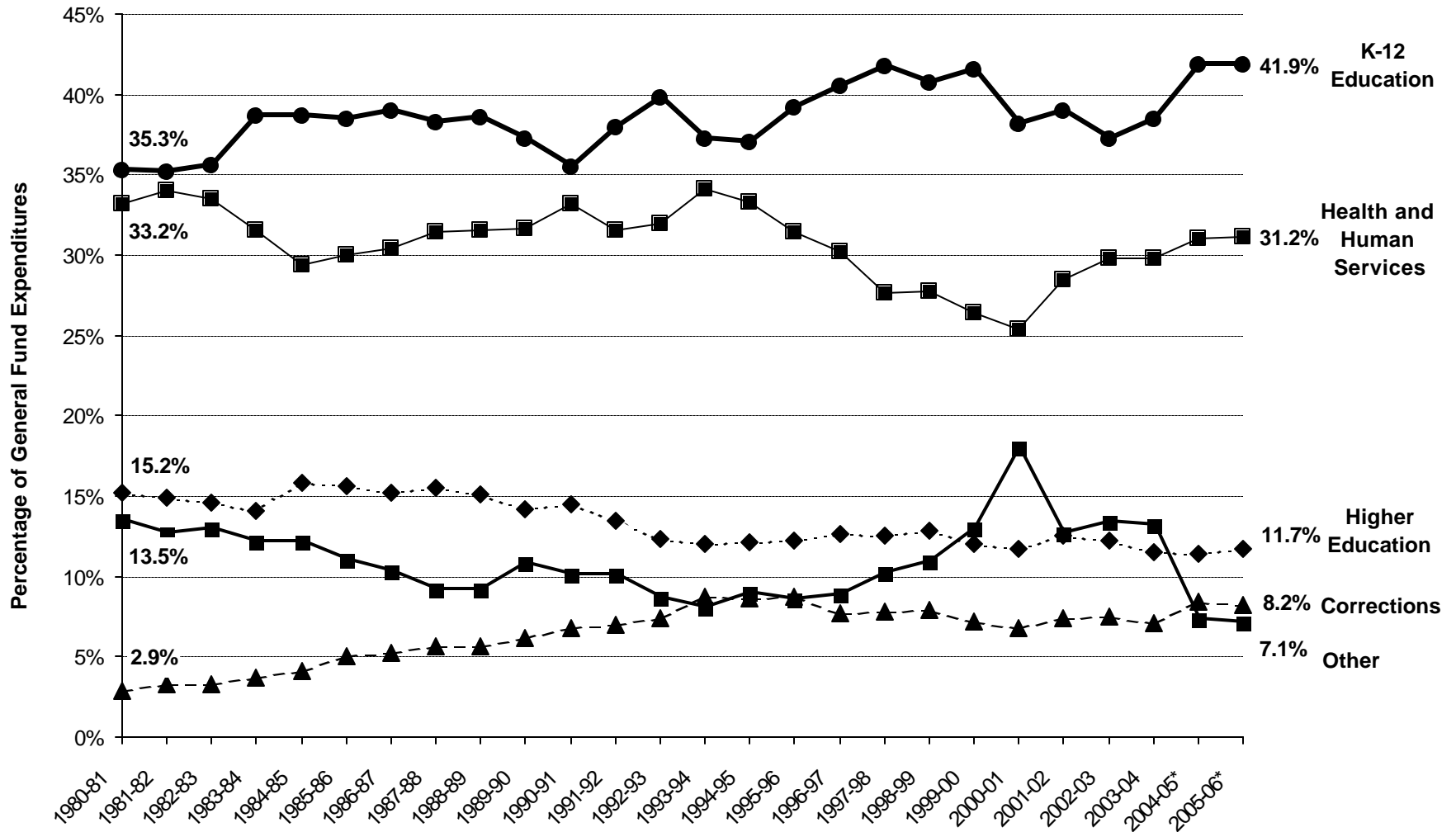
Education Accounts for Largest Share of 2005-06 Spending

General Fund Spending by Agency



Proposed 2005-06 General Fund Expenditures = \$85.7 Billion

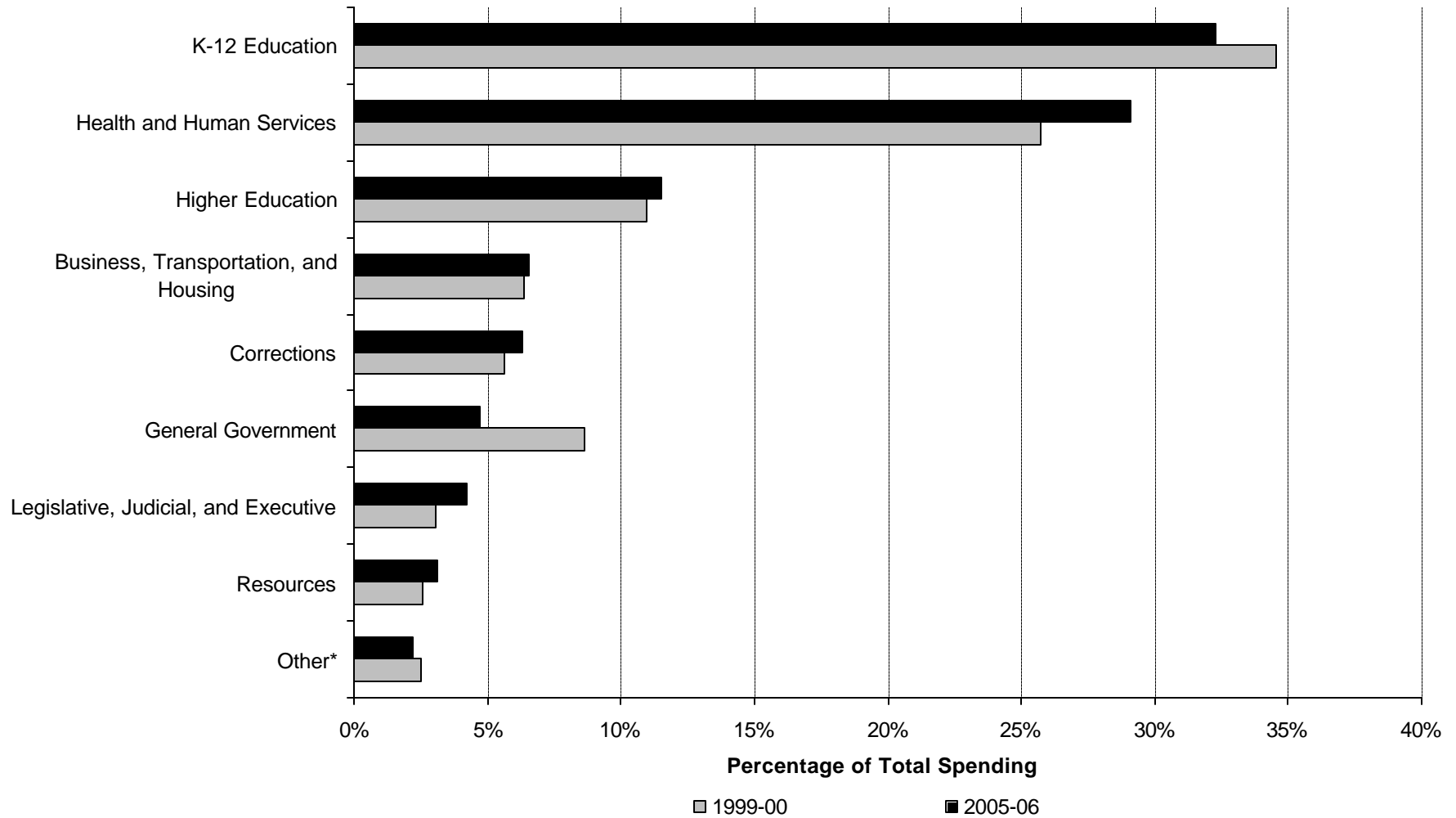
K-12 Education Accounts for the Largest Share of State General Fund Spending



*2004-05 estimated and 2005-06 proposed.

Note: "Other" includes Legislative, Judicial, and Executive; State and Consumer Services; Business, Transportation, and Housing; Technology, Trade, and Commerce; Resources; Environmental Protection; Labor and Workforce Development; and General Government.

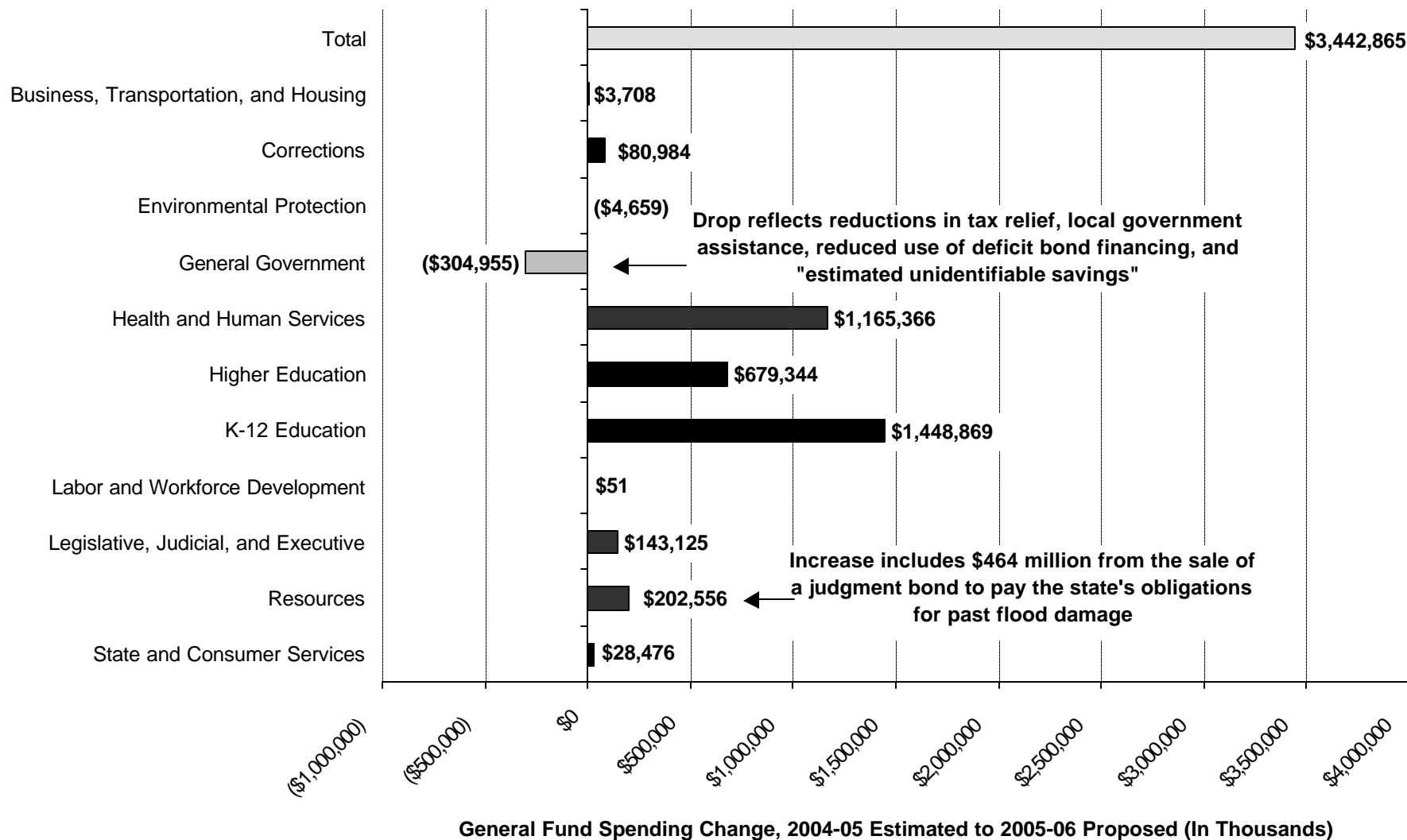
K-12 Education Has Decreased as a Share of Total Spending



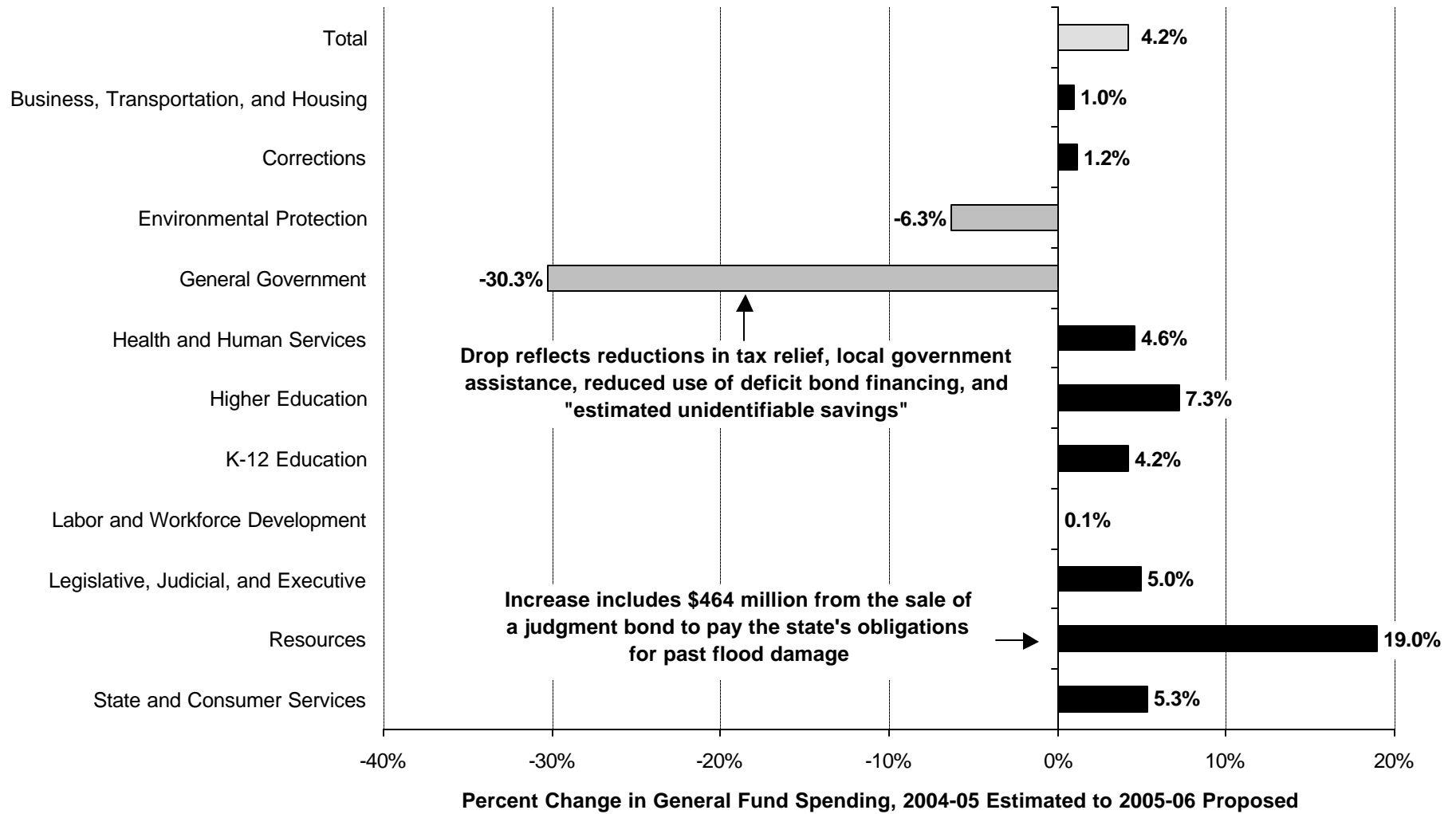
*"Other" includes Technology, Trade, and Commerce; State and Consumer Services; and Environmental Protection.

Note: 2005-06 Labor and Workforce Development Agency spending is counted under Health and Human Services and General Government.

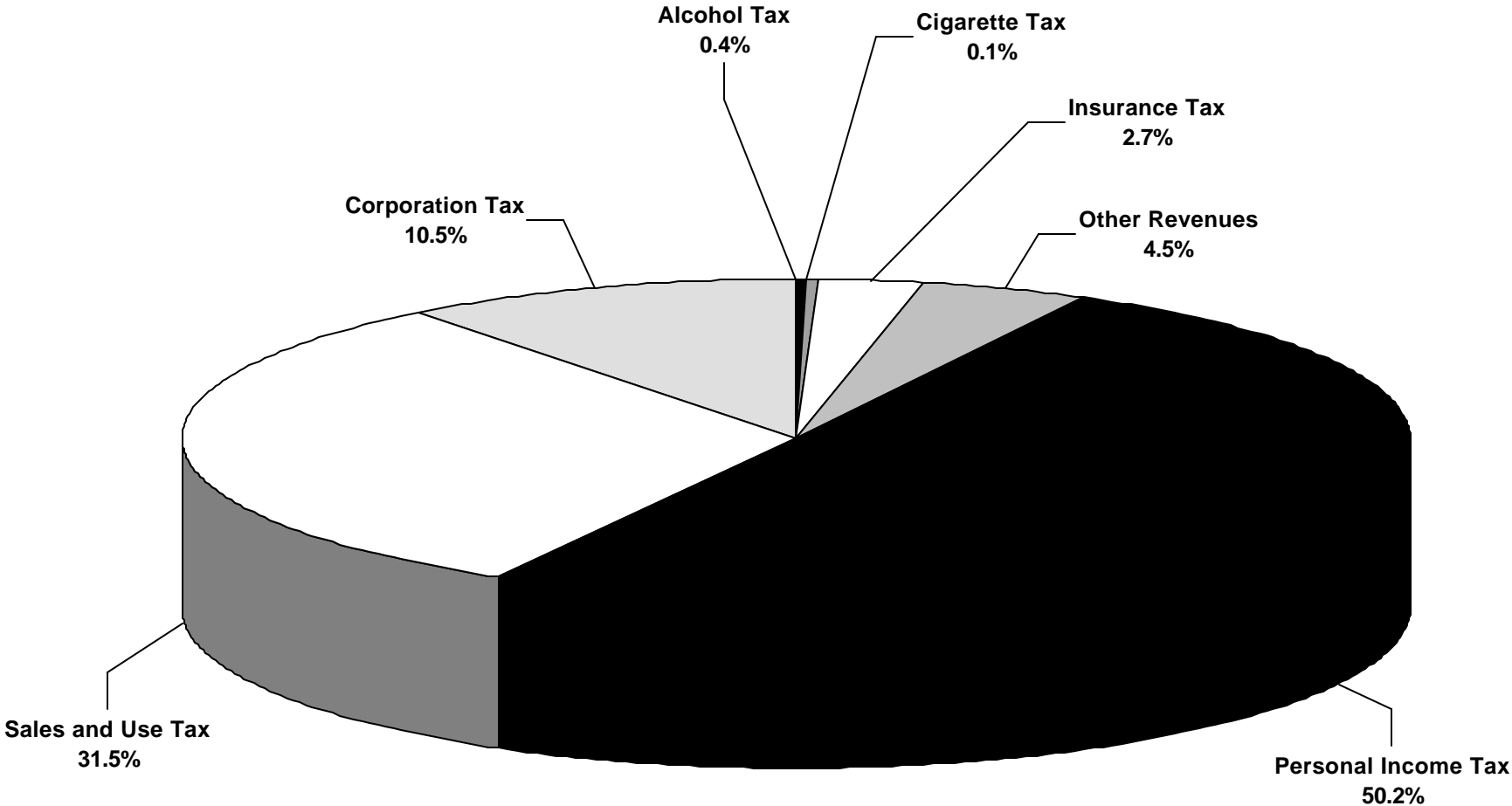
Total Spending Up Modestly



Total Spending Up Modestly



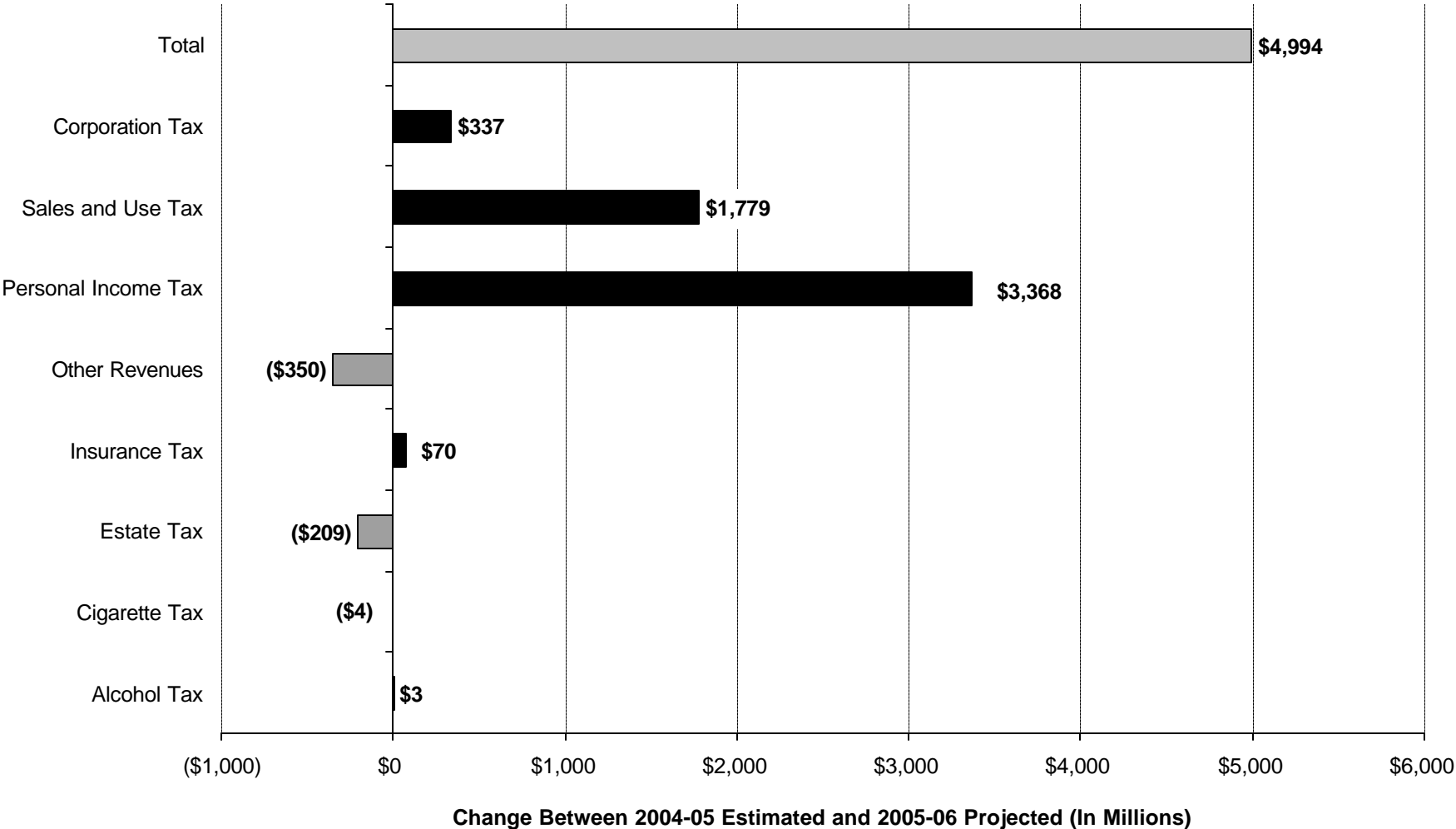
Personal Income Tax Provides Half of 2005-06 General Fund Revenues



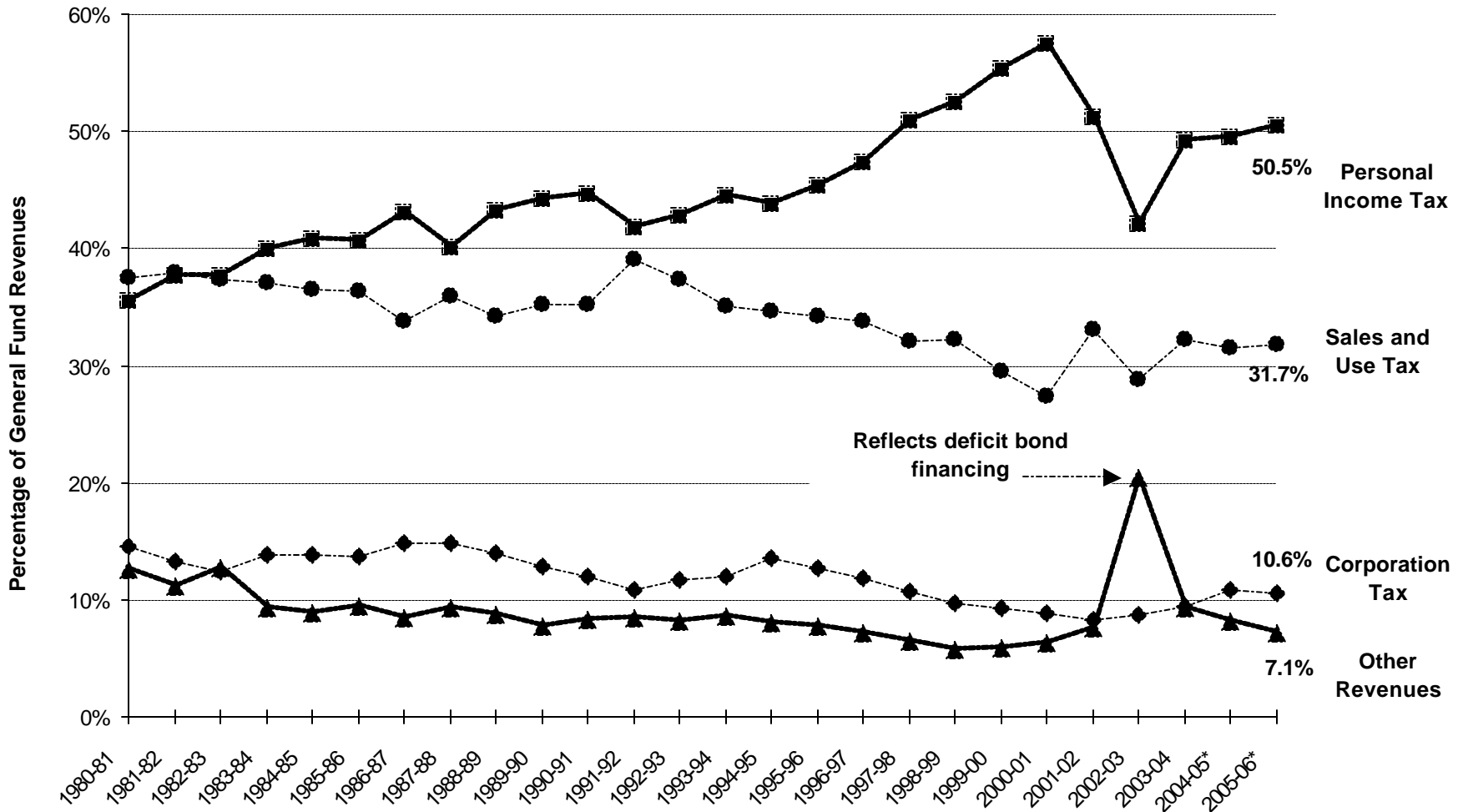
Projected 2005-06 General Fund Revenues = \$85.5 Billion

Note: "Other Revenues" include Horse Racing License Fees, Trailer Coach License Fees, Loans and Transfers, and Minor Revenues.

Revenues Are Expected to Increase Modestly



Personal Income Tax Provides the Largest Share of State General Fund Revenues



*2004-05 estimated and 2005-06 projected.

Note: "Other Revenues" includes Alcoholic Beverage Tax, Cigarette Tax, Horse Racing License Fees, Estate Tax, Insurance Tax, Trailer Coach License Fees, and Minor Revenues. Excludes Loans and Transfers.

K – 14 Education

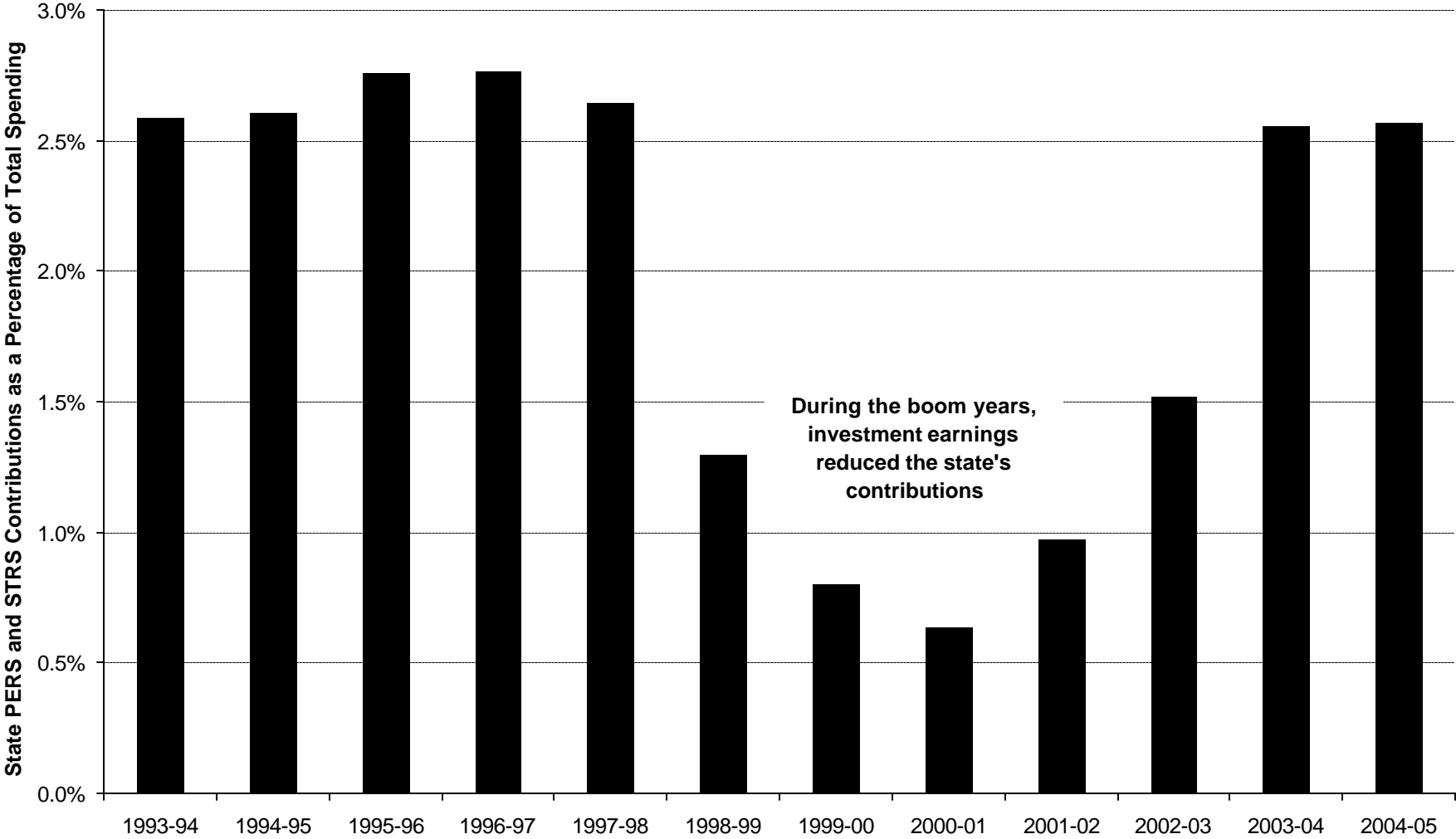
The Governor's Proposed Budget:

- ▶ Would not increase school spending to reflect the increase in the guarantee during the current year due to rising revenues. This results in a spending level that is \$2.3 billion lower than would have been required had the guarantee not been suspended as part of the 2004-05 budget agreement. The Governor also proposes to eliminate the state's contribution to the State Teachers Retirement System for savings of \$469 million.
- ▶ Reflects a per pupil funding level of \$7,374, a level that is \$188 above 2004-05 spending in inflation-adjusted dollars. However, local school districts would be required to make up for the state's contribution to teachers' pension plans out of revenues that were formerly available for other purposes.
- ▶ Allocates the combined \$2.9 billion in state and local K – 14 education funds to support cost-of-living adjustments and enrollment growth; a one-time allocation to implement the Williams settlement, which requires the state to improve school facilities (\$100 million); and \$329 million to partially restore previous reductions made to general purpose support for schools ("revenue limits").
- ▶ Does not propose a fee increase for community college students.
- ▶ Outlines a number of policy initiatives, including a constitutional amendment requiring "merit" pay for teachers, changes to the state's charter schools program, and a new initiative in the area of vocational-technical instruction.

State Employees

- ▶ \$408 million of the spending cuts proposed in the Governor's Budget come from reductions in state employee pensions and compensation. In addition, the Governor has proposed a constitutional amendment that would prohibit state and local governments from offering traditional defined benefit retirement plans to their employees. The Governor would also:
 - Shift a greater share of the cost of retirement benefits onto state employees. Currently, state employees fund approximately one-fourth of the state's pension contribution amounts.
 - Encourage state employees to "opt out" of CalPERS in exchange for a one-time stipend, for savings of \$90 million in 2005-06.
- ▶ The Governor proposes numerous other changes affecting state employees, including:
 - Allowing the state to make a fixed dollar contribution to each employee for health care, based on the number of family members to be covered;
 - Eliminating the state's contributions toward health care premiums for new employees until they have passed probation;
 - Allowing the Governor to furlough non-public safety and non-public health employees for up to five days during a fiscal crisis;
 - Eliminating two of the current 14 paid holidays;
 - Eliminating leave time from overtime calculations; and
 - Placing a cap on the amount of leave time state employees may accrue.

State Pension Contributions Account for a Similar Share of Total Spending as in the Early 1990s



During the boom years,
investment earnings
reduced the state's
contributions

Still Stretched Thin

- ▶ The Governor's Proposed Budget does not fund operating cost increases in the Adoption Assistance, Adult Protective Services, Foster Care, and In-Home Supportive Services programs for the fifth consecutive year.
- ▶ These and other program reductions are “squeezing” county-run programs and compromising the quality and availability of local services.
- ▶ Surveys of local programs have found that funding reductions in:
 - Children's programs, including the Adoption and Child Protective Services programs, have made it more difficult to keep families together, are undermining counties' ability to recruit foster and adoptive parents, and are reducing supportive services for families and children.
 - The Adult Protective Services Program, which assists functionally impaired adults, have reduced investigations of elder abuse, limited outreach efforts, and made it difficult for counties to meet required response time targets.
 - The CalWORKs Program have eroded the comprehensive welfare-to-work approach embodied in the state's welfare reform program, which may result in fewer families leaving cash assistance for work.
 - Food stamp administration have reduced outreach and simplification efforts, resulting in a loss of 100 percent federally-funded benefits that could assist California families.

CalWORKs/TANF

The Governor's Proposed Budget would:

- ▶ Eliminate the requirement to provide a statutory cost-of-living adjustment and reduce cash assistance levels by 6.5 percent for savings of \$376.1 million in 2005-06. This proposal would reduce the maximum monthly grant for a family of three from \$723 to \$676 in high-cost counties and from \$689 to \$644 in low-cost counties. The maximum CalWORKs grant for a family of three in high-cost counties in 2005-06 would be \$18 less than in 1989-90.
- ▶ Reduce the amount of earnings that families may exclude in determining a family's CalWORKs grant, for savings of \$79.5 million in 2005-06. This change would further reduce grant levels for more than 100,000 working CalWORKs families, with an average monthly grant reduction of \$79 per family. In addition, nearly 9,000 working CalWORKs families would become ineligible for CalWORKs cash assistance under this proposal.
- ▶ Use federal Temporary Assistance for Needy Families (TANF) funds in place of \$361.3 million in state funds for Child Protective Services, Foster Care, the Department of Developmental Services, and county juvenile probation facilities.
- ▶ Eliminate a \$50 million employment services augmentation that was included in the 2004-05 Budget Act.

Child Care

The Governor's Budget proposes to:

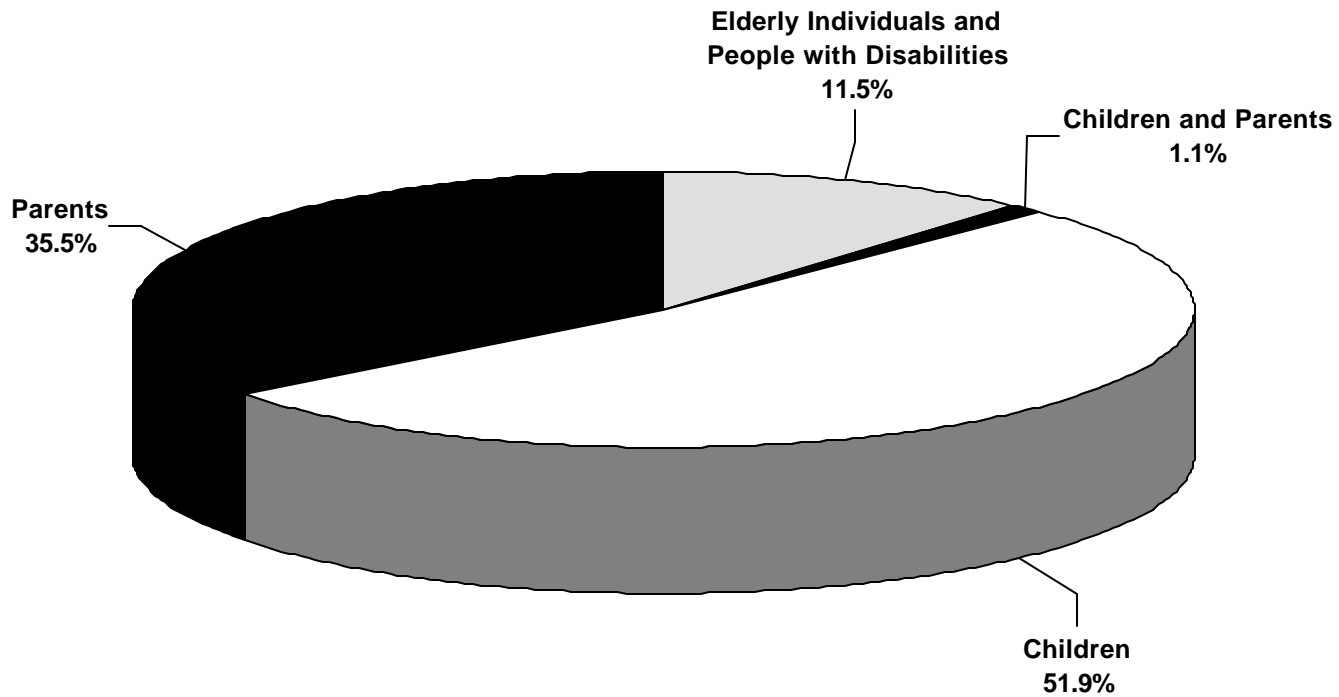
- ▶ Base income eligibility for the state's subsidized child care programs on the federal poverty level (FPL), rather than state median income (SMI). This change could potentially reduce the number of low-income families who qualify for subsidized child care, since the FPL tends to increase more slowly than the SMI over time. Between 1995 and 2003, the FPL increased at an annual rate that was half that of the growth in the SMI.
- ▶ Limit the amount of time that families may receive CalWORKs child care and require those families to seek subsidized child care through the state's Alternative Payment Program. This proposal would require working families to join already overcrowded waiting lists for subsidized child care.
- ▶ Reduce reimbursement levels for license-exempt child care providers by 39 percent for providers who do not obtain specified training and by 33 percent for providers who do obtain specified training.
- ▶ Require counties to establish centralized child care eligibility lists. Families who are not required to pay fees for subsidized child care would receive child care services on a first-come, first-served basis. Families required to pay fees would receive services according to their income level, with the lowest-income families in this category served first. It is not clear how this change would affect eligible families' access to subsidized child care.

Health

The Governor's Budget proposes to:

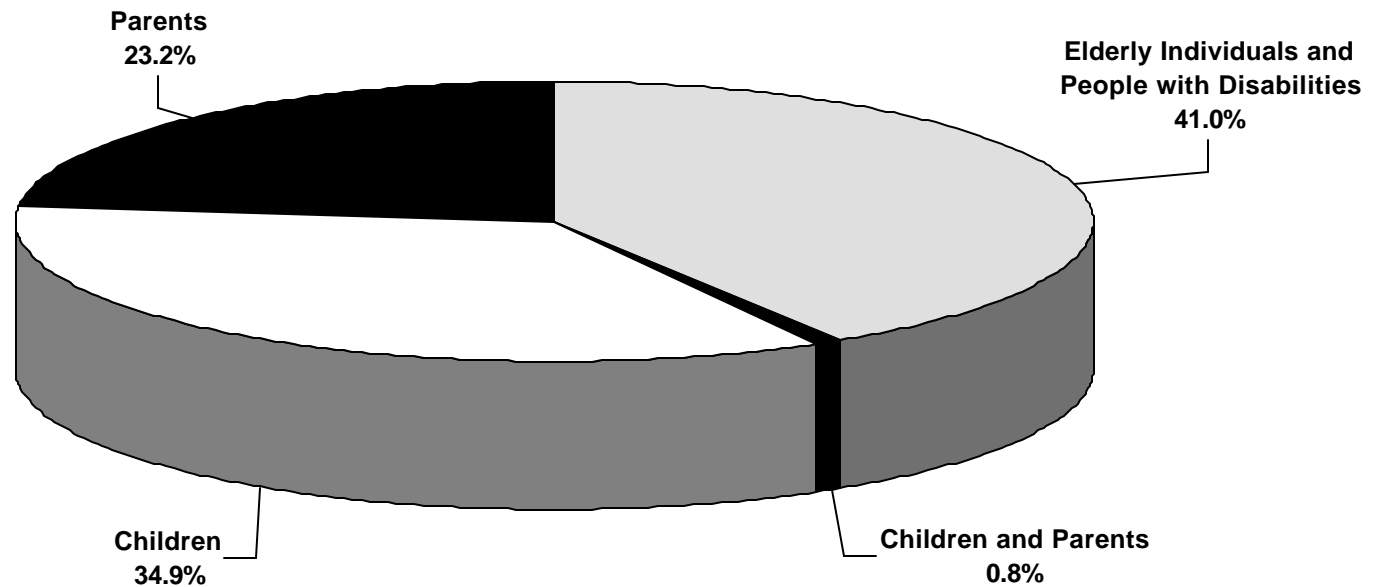
- ▶ Restructure the Medi-Cal Program by expanding the use of managed care; establishing an alternative hospital financing structure; capping adult dental services; requiring certain Medi-Cal recipients to pay monthly premiums; using a centralized vendor, rather than counties, to process Medi-Cal applications for children; and monitoring county compliance with Medi-Cal administration performance standards. The budget assumes \$12.3 million in savings from the proposed changes.
- ▶ Increase funding for application assistance for Medi-Cal and Healthy Families and to improve retention of children transitioning from Medi-Cal to Healthy Families; allow counties to “buy into” Healthy Families to provide health coverage for children who are not currently eligible for Medi-Cal or Healthy Families; and revise the joint Medi-Cal/Healthy Families application form.
- ▶ Provide \$6 million for a new obesity prevention program.
- ▶ Establish a discount prescription drug purchasing program for uninsured Californians based on voluntary participation by drug companies.
- ▶ Obtain federal funds for prenatal care provided to certain immigrant women, for state savings of \$191 million in Medi-Cal and \$51 million in the Access for Infants and Mothers Program.

**California Has Expanded Health Coverage for Low-Income Children,
Families, Elderly Individuals, and People with Disabilities**
Increase in Medi-Cal Caseload Due to Recent Enrollment and Eligibility Changes



2005-06 Caseload Attributable to Recent Medi-Cal Changes = 1.2 Million Individuals

**California Has Expanded Health Coverage for Low-Income Children,
Families, Elderly Individuals, and People with Disabilities**
Increase in General Fund Expenditures Due to Recent Enrollment and Eligibility Changes in
the Medi-Cal Program



2005-06 General Fund Expenditures Attributable to Recent Medi-Cal Changes = \$1.2 Billion

Seniors and Persons with Disabilities

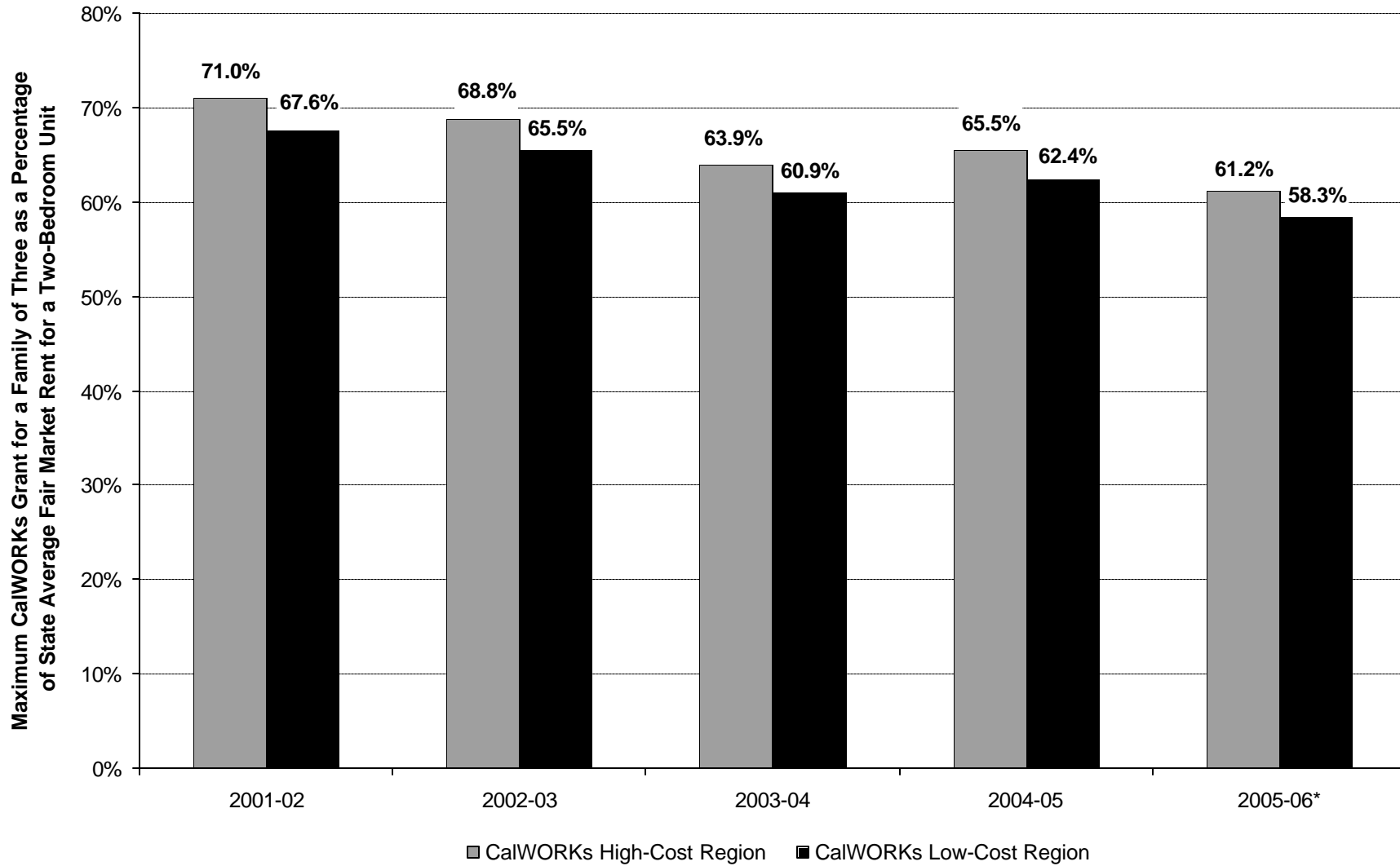
The Governor's Budget proposes to:

- ▶ Suspend the state COLA and withhold the federal COLA for Supplemental Security Income/State Supplementary Payment (SSI/SSP) grants scheduled for January 2006. Under current law, monthly grants would increase to \$849 for an individual and \$1,503 for couples. The Governor's proposal would keep grant levels at \$812 for individuals and \$1,437 for couples.
- ▶ Reduce the state's share of costs for In-Home Supportive Services (IHSS) provider wages and benefits to the state minimum wage. Currently, the state pays a share of cost for provider wages and benefits up to \$10.10 per hour and up to the Maximum Allowable Contract Rates for contract providers.
- ▶ Replace the Senior Citizens' Property Tax Assistance Program with a modestly expanded property tax deferral program.
- ▶ Reduce eligibility for and benefits provided by the Senior Citizen Renters' Tax Assistance Program.

What Would the Governor's Human Service Proposals Mean for Low-Income Californians?

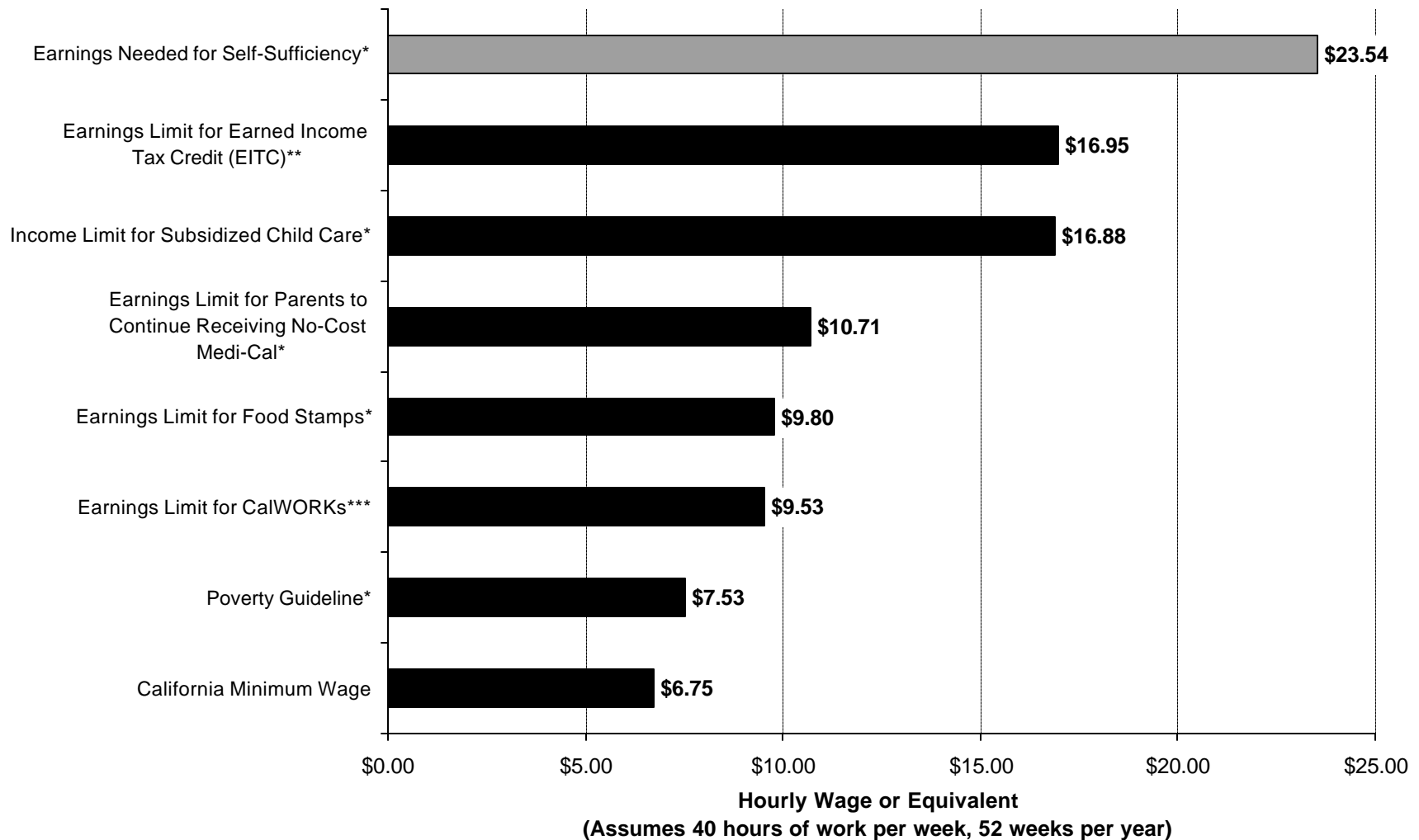
- ▶ If the Governor's proposed SSI/SSP freeze is enacted, the Fair Market Rent (FMR) for a studio apartment would exceed the proposed SSI/SSP grant for individuals in 10 counties and exceed 50 percent of the grant in 56 counties.
- ▶ The Governor's proposal to reduce the state's contribution toward IHSS workers' wages would reduce the earnings of a full-time worker to below the federal poverty line for a family of three. IHSS wages are the only source of earnings for about three-quarters (77 percent) of IHSS workers.
- ▶ If the Governor's proposed CalWORKs grant reductions are enacted, the FMR for a two-bedroom apartment would exceed the proposed maximum monthly CalWORKs grant for a family of three in 39 counties and exceed 85 percent of the grant in all 58 counties.
- ▶ Many individuals and families would face multiple reductions under the Governor's proposals. Seniors could, for example, face a freeze in SSI/SSP grant levels, a cap on Medi-Cal dental benefits, and a reduction of benefits under the Senior Citizens' Property Tax Assistance Program.

CalWORKs Grants Lose Ground to Rising Housing Costs



* Reflects the Governor's proposal to eliminate the 2005-06 COLA and reduce CalWORKs grant levels by 6.5 percent.

Supports for Working Families End Before Families Reach Self-Sufficiency



* Family of three.

** One-parent family with two or more children.

*** Family of three in a high-cost county. Does not reflect the Governor's proposal to eliminate the 2005-06 COLA and reduce CalWORKs grant levels by 6.5 percent.

“Blowing Up Boxes”

- ▶ In keeping with his campaign promise to “blow up boxes” in state government, the Governor has introduced two agency reorganization proposals:
 - The first would eliminate 88 boards and commissions. In many cases, the functions would be transferred from boards, which operate independently, to bureaus, which operate under the direct management of the overseeing department (Department Directors are appointed by the Governor).
 - The second would reorganize the Youth and Adult Correctional Agency (YACA) under a newly created Department of Corrections and Rehabilitation. Unlike the current YACA Secretary, the Secretary of the new department would have authority over all departmental activities.
- ▶ On January 6, the Governor submitted both proposals to the Little Hoover Commission (LHC) for analysis.
- ▶ The Governor may submit the proposals to the Legislature in early February. Within 30 days of the Legislature receiving the plans, the LHC must report its findings to the Legislature. The plans will become effective on the 61st day after the Legislature receives the plans – unless either house passes a resolution, by majority vote, rejecting either or both. The Legislature can only approve or reject reorganization plans; it cannot amend them.

Risks to the Budget

- ▶ Legal challenges threaten the state's ability to issue \$1.2 billion in bonds backed by tribal gaming revenues that would be used to repay various loans from transportation funds and a \$765 million pension obligation bond that would finance the state's contribution toward employees' retirement plans.
- ▶ The Governor's Proposed Budget assumes \$150 million in unallocated savings, two-thirds of which would come out of the Department of Corrections. In past years the state has not fully realized savings anticipated from similar reductions.
- ▶ The Governor's Proposed Budget assumes \$96 million in savings from changes in procurement policies. A similar level of savings was assumed in the current year's budget; however, the Administration now estimates that only half of the anticipated savings will occur.
- ▶ The Governor's proposed changes to state employees' pension plans ignore the transition costs that would be associated with the shift to the new system. These costs could outweigh any savings for many years to come.