



WHAT WOULD PROPOSITION 1E MEAN FOR CALIFORNIA?

Proposition 1E, which will appear on the May 19, 2009 special election ballot, would temporarily divert a portion of funds raised by Proposition 63 of 2004 – the Mental Health Services Act (MHSA) – to help balance the state’s budget. This *Budget Brief* provides an overview of this measure and the policy issues it raises. The California Budget Project (CBP) neither supports nor opposes Proposition 1E.

What Would Proposition 1E Do?

Proposition 1E was placed on the ballot by the Legislature as part of the recent budget agreement to help close the state’s budget shortfall. If approved by the voters, Proposition 1E would use a portion of the revenues raised by Proposition 63 to offset costs that would otherwise be paid for out of the General Fund. Specifically, Proposition 1E would shift \$226.7 million in 2009-10 and up to \$234.0 million in 2010-11 from the Mental Health Services Fund (MHSF) to the General Fund, resulting in equivalent General Fund savings. Proposition 1E specifies that the diverted Proposition 63 funds would be used to support the Early and Periodic Screening, Diagnosis and Treatment (EPSDT) Program – a federally mandated program that requires the state to provide certain screening, diagnostic, and treatment services to Medi-Cal recipients under age 21.¹

What Does Proposition 63 Do?

Proposition 63, approved by voters in November 2004, imposes a 1 percent tax on the portion of individuals’ taxable incomes that exceeds \$1 million.² Revenues from the tax provide dedicated funding for mental health services for children and adults. The state allocates most of the revenues raised by Proposition 63 to county mental health programs.³ Specifically, the funds raised by the tax must be spent on:

- Services for children with severe mental illness through the Children’s System of Care model;
- Services for adults with severe mental illness through the Adult and Older Adult System of Care model;

- Services that increase access for underserved groups, increase the quality of services, promote interagency collaboration, and increase access to care;
- Prevention and early intervention programs designed to prevent mental illness from becoming severe and disabling;
- Education and training programs to address the shortage of qualified mental health service providers; and
- Support for capital facilities and technology needed to provide mental health services.⁴

Proposition 63 requires that funds raised be used to expand mental health services and specifically prohibits the use of the revenues to generate budget savings by replacing existing state or county funds for mental health services.⁵ Proposition 1E would amend Proposition 63 to authorize the temporary diversion of a portion of MHSA revenues to the General Fund to help close the budget gap. Since this change is not consistent with the intent of Proposition 63, it must be approved by the voters.⁶

What Policy Issues Are Raised by Proposition 1E?

By diverting a portion of Proposition 63 revenues to the General Fund, Proposition 1E would provide state savings as California’s policymakers grapple with an unprecedented budget crisis.

Should a Portion of Proposition 63 Revenues Be Used To Generate Budget Savings?

In February 2009, California’s policymakers closed an unprecedented \$40 billion budget gap for 2008-09 and

How Are Mental Health Services Currently Provided?

In California, counties administer local mental health programs.⁷ Current law requires counties to provide services to individuals who have a severe mental illness, to the extent that resources are available. There are no income eligibility requirements for individuals to receive services.

Over the past several decades, California's mental health system has moved increasingly toward a community-based service delivery system. The Short-Doyle Act of 1957 supported the development of community-based mental health services as an alternative to institutionalization. Prior to 1957, many individuals requiring mental health services were treated in state hospitals. Subsequently, California passed other laws to facilitate the use of community-based mental health services. Community-based services include short- and long-term treatment and case management.

In 1991, the state significantly changed the governance structure for mental health programs to support local delivery of services. Under "realignment," the state shifted 100 percent of program and funding responsibility for certain mental health services to the counties, including community-based services.⁸ Counties were given the flexibility to allocate resources based on program effectiveness and local priorities. Realignment provided counties with a dedicated funding source to finance the new program responsibilities consisting of an increase in both the sales tax rate and the Vehicle License Fee.

Counties receive federal and state General Fund dollars to cover the costs of mental health services provided to low-income individuals under the state's Medi-Cal Program.⁹ Counties also receive federal dollars for mental health services provided to children under the Healthy Families Program.¹⁰ Other sources of funding for county mental health services include federal and state funding for specific projects and the Traumatic Brain Injury Fund.¹¹

2009-10 with a package of spending cuts, temporary tax increases, borrowing, and funds from the federal economic recovery bill.¹² As part of this package, the Legislature placed Proposition 1E on the ballot to divert up to a total of \$460.7 million of Proposition 63 revenues to the General Fund over two years. Specifically, this measure would provide \$226.7 million in General Fund savings in 2009-10 and additional state savings of up to \$234.0 million in 2010-11, a year in which the Legislative Analyst's Office projects that the state will face an operating shortfall of \$12.6 billion.¹³

If voters approve Proposition 1E, the total amount of funds available for Proposition 63-supported mental health programs would decline. Moreover, Proposition 1E also could reduce federal funds available for mental health services, since some Proposition 63 funds are matched by federal dollars to provide mental health services to Medi-Cal recipients.¹⁴ By reducing the funds available for mental health programs, Proposition 1E could impact the provision of mental health services. The impact on services may not be immediate, however, because of the substantial balance of unspent funds in the MHSF, and would likely vary from county to county since Proposition 1E does not specify how the state or counties should adjust their MHSA-supported programs in response to reduced funds.

While Proposition 1E specifies that the diverted funds would be used to support EPSDT mental health services, federal law requires the state to provide these services. Thus, if voters reject Proposition 1E, state General Fund dollars would be used to support EPSDT mental health services and additional spending

reductions and/or tax increases would be needed to backfill the loss of funds that would have been provided by Proposition 1E.

Most of the Revenues Raised by Proposition 63 Have Not Been Spent

The majority of the revenues raised by Proposition 63 have not been spent due to implementation delays. A recent audit found that the Department of Mental Health (DMH) had developed an inefficient process for implementing Proposition 63 and had deviated from some of the measure's requirements, both of which contributed to delays.¹⁵ As a result the distribution of funds to counties was "untimely" and "not in compliance" with Proposition 63.¹⁶ The most recent report documenting expenditures from revenues raised by Proposition 63 shows that as of the end of 2007-08, just under \$2 billion of the more than \$4.1 billion raised by Proposition 63 had been distributed by the DMH to county programs.¹⁷ Thus, a substantial amount of the total revenues collected remained unspent.

Proposition 1E Would Shift Funds From a Revenue Source That Is Likely To Increase Over Time

Unlike Proposition 1D, which would divert funds from tobacco tax revenues – a revenue source that is declining as tobacco consumption falls – Proposition 1E would shift funds from a revenue source that is likely to increase over time as Californians' incomes rise and more taxpayers – and larger shares of their incomes – are subject to Proposition 63's tax.¹⁸ Since Proposition 63 took effect, the number of "millionaire" taxpayers – those with

incomes of more than \$1 million – has increased considerably. Between 2004 and 2007, the number of millionaire taxpayers rose by 48.6 percent, while the total number of personal income taxpayers increased by 8.6 percent.¹⁹ During this period, the total adjusted gross income (AGI) – income reported for tax purposes – of millionaire taxpayers increased by 65.0 percent, compared to a 26.4 percent increase in the total AGI of all personal income taxpayers.²⁰

Proponents Argue

Proponents of Proposition 1E argue that it is needed to “help reduce the magnitude of cuts that would otherwise have occurred in other state funded programs.” In addition, proponents claim that the amount of Proposition 63 funding “sitting in state coffers ... is more than is needed to fund current services” and that even though “in the long run this money is probably best spent on Proposition 63 programs, we cannot afford to only do that right now.”²¹

Opponents Argue

Opponents of Proposition 1E argue that “even in this difficult time, we ought to respect the will of the people” who approved Proposition 63. In addition, opponents claim that Proposition 63 programs “are working and save the state money” and that diverting a portion of Proposition 63 funding “will impede us from serving even more people.”²²

Conclusion

Proposition 1E would divert a portion of funds raised by Proposition 63 to help balance the state’s budget. The fundamental policy choice posed by Proposition 1E is whether a portion of revenues raised by Proposition 63 should be used to help close the budget gap or whether these funds should be spent solely for purposes consistent with the measure’s original intent. Voters should weigh Proposition 1E’s potential impact on the provision of mental health services if the measure is approved against the potential for additional General Fund spending cuts and/or revenue increases if the measure fails.

Alissa Anderson prepared this Budget Brief. The California Budget Project (CBP) neither supports nor opposes Proposition 1E. This Budget Brief is designed to help voters reach an informed decision based on the merits of the issues. The 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 CBP is provided by foundation grants, individual donations, and subscriptions. Please visit the CBP’s website at www.cbp.org.

ENDNOTES

- ¹ Medi-Cal is California’s version of Medicaid, a federal-state program that provides health coverage for low-income families and individuals. Proposition 1E specifies that \$226.7 million would be diverted in 2010-11 “except that this amount may be adjusted to fund caseload as appropriate in the EPSDT program, but the total amount redirected for the 2010-11 fiscal year shall not exceed” \$234.0 million.
- ² For example, a taxpayer with \$1.5 million of taxable income pays an additional \$5,000 – the 1 percent rate applied to \$500,000. The \$1 million threshold is not adjusted annually for inflation and cannot be reduced by any of the state’s tax credits.
- ³ A portion of the revenues also can be used for state administration of mental health services.
- ⁴ Proposition 63 specifies the exact percentages of the revenues generated by the MHSAs that must be used for certain purposes in certain years. For example, Proposition 63 specifies that in 2004-05, its first year of implementation, most of the funds had to be used for education and training programs and capital facilities and technology, while in 2008-09 and each subsequent year, 20 percent of the funds must be used for prevention and early intervention and 80 percent of the funds must be used for the Children’s System of Care and Adult and Older Adult System of Care programs. See California Budget Project, *What Would Proposition 63, The Mental Health Services Act, Mean for California?* (September 2004).
- ⁵ Proposition 63 also requires the state to maintain the same level of General Fund support for mental health programs as was provided in 2003-04, essentially locking in a portion of the General Fund for mental health programs.
- ⁶ The Legislature may only amend Proposition 63 to further its intent; other changes must be approved by voters.
- ⁷ The Department of Mental Health (DMH) operates state hospitals that provide inpatient care to people with serious mental illness.
- ⁸ In addition to mental health services, California realigned responsibility for various health and human services programs by shifting program responsibilities from the state to local governments and changing cost-sharing requirements.
- ⁹ The federal government provides matching funds for mental health services provided to individuals under Medi-Cal. The state provides General Fund dollars to counties to match the federal Medicaid funds. The General Fund allocation for certain Medi-Cal mental health services is capped.
- ¹⁰ The Healthy Families Program provides low-cost health coverage to children with family incomes too high to qualify for Medi-Cal, up to 250 percent of the federal poverty line.
- ¹¹ The Traumatic Brain Injury Fund includes revenues from penalties assessed for traffic violations.
- ¹² California Budget Project, *Governor Signs Budget Plan* (Updated February 25, 2009).
- ¹³ Legislative Analyst’s Office, *2009-10 Budget Analysis Series: The Fiscal Outlook Under the February Budget Package* (March 13, 2009).

- ¹⁴ Legislative Analyst's Office, "Prop 1E Mental Health Services Funding. Temporary Reallocation. Helps Balance State Budget," in Secretary of State's Office, *California Statewide Special Election: Tuesday, May 19, 2009 Official Voter Information Guide*, pp. 38-39, downloaded from <http://www.voterguide.sos.ca.gov/pdf-guide/props/prop1e-analysis.pdf> on March 24, 2009. The extent to which federal support for mental health services could decline depends on how the state and counties adjust their programs in response to the reduction in Proposition 63 funds.
- ¹⁵ Department of Finance, Office of State Audits and Evaluations, *Performance Audit: California Department of Mental Health: Mental Health Services Act* (May 2008). At the time the report was written, only the Children's System of Care and Adult and Older Adult System of Care programs had been fully implemented, while the implementation of the other components had been limited.
- ¹⁶ Department of Finance, Office of State Audits and Evaluations, *Performance Audit: California Department of Mental Health: Mental Health Services Act* (May 2008), p. 7.
- ¹⁷ Another \$1.5 billion is anticipated to be distributed in 2008-09 and \$1.7 billion is anticipated to be distributed to county programs in 2009-10. According to this report, Proposition 63 has generated nearly twice as much revenue as expected and is projected to generate an additional \$1 billion in 2008-09 and \$914 million in 2009-10. Stephen W. Mayberg, Ph.D., *Mental Health Services Act Expenditure Report: Fiscal Year 2008-2009* (Department of Mental Health: January 2009), pp. 1 and 9.
- ¹⁸ Proposition 1D would annually divert \$268.0 million of state and county First 5 tobacco tax revenues to the General Fund between 2009-10 and 2013-14. Tobacco tax revenues have fallen as the prevalence of smoking in California has decreased. See California Budget Project, *What Would Proposition 1D Mean for California?* (forthcoming).
- ¹⁹ Franchise Tax Board. The number of millionaire taxpayers tends to fluctuate with the boom and bust of the economy. For example, the number of millionaire taxpayers reached approximately 44,000 in 2000 at the height of the economic boom, dropped to approximately 25,000 in 2002, then increased each year thereafter, reaching approximately 55,000 in 2007. Thus, revenues raised by Proposition 63 could fluctuate from year to year, but are generally likely to increase.
- ²⁰ Franchise Tax Board.
- ²¹ "Argument in Favor of Proposition 1E," in Secretary of State's Office, *California Statewide Special Election: Tuesday, May 19, 2009 Official Voter Information Guide*, p. 40, downloaded from <http://www.voterguide.sos.ca.gov/pdf-guide/props/prop1e-arguments.pdf> on March 24, 2009.
- ²² "Argument Against Proposition 1E," in Secretary of State's Office, *California Statewide Special Election: Tuesday, May 19, 2009 Official Voter Information Guide*, p. 41, downloaded from <http://www.voterguide.sos.ca.gov/pdf-guide/props/prop1e-arguments.pdf> on March 24, 2009.