

CALIFORNIA BUDGET PROJECT

Paving the Way:

Does the Governor's Proposed 2006-07 Budget Prepare California for the Future?

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A PRESENTATION BY
THE CALIFORNIA BUDGET PROJECT
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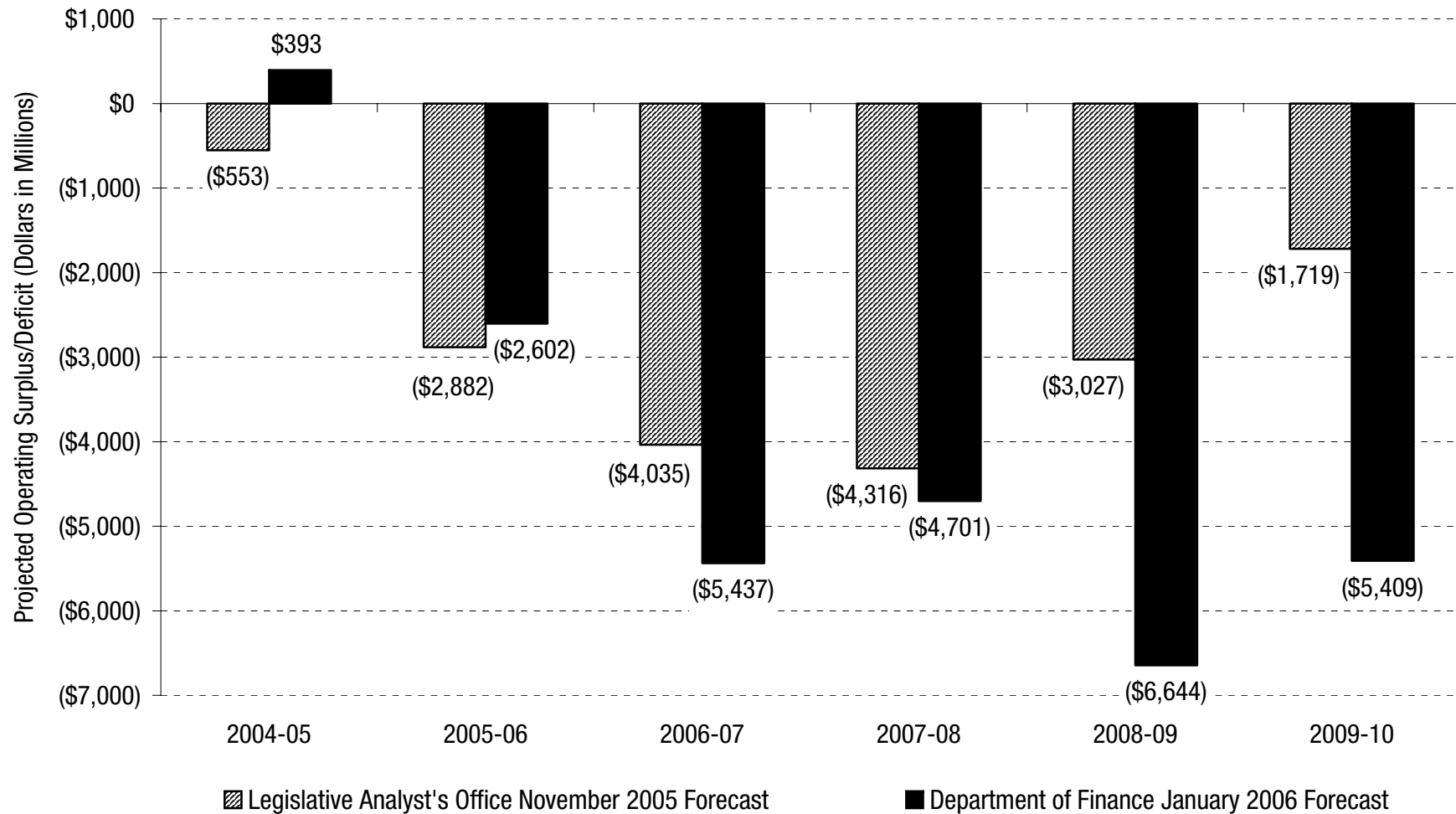
The Big Picture

The Governor's Proposed 2006-07 Budget:

- Increases spending for education and transportation and outlines an ambitious public works proposal. In 2006-07, the new spending would be financed by higher-than-anticipated revenues, largely in the current and prior years.
- Significantly reduces spending for child care and employment services in the CalWORKs Program and further delays a federally-funded cost-of-living adjustment for aged and disabled Californians in the SSI/SSP Program. Virtually all of the spending reductions proposed by the Governor affect programs for low-income and other vulnerable Californians.
- Would widen the state's budget gap in 2007-08 and beyond. In November, the Legislative Analyst's Office (LAO) projected that the state's operating shortfalls would begin narrowing significantly. The Governor's proposals would lead to wider than previously forecasted gaps.
- Asks the voters to "lock in" certain transportation spending and the Legislature to give governors the ability to make unilateral mid-year budget cuts. Voters soundly rejected Proposition 76, which included similar provisions in November.

The Governor's Budget Proposals Would Lead to Widening Operating Deficits

Operating Deficits Under the Governor's Proposed Budget as Compared to the LAO's November 2005 Baseline Forecast



California Faces Critical Choices

- California is at a crossroads. While higher than previously anticipated revenues are sufficient to support increased spending in the short term, the state still faces serious long-term fiscal challenges. The Governor's Proposed Budget raises important budget and policy choices that will affect California in 2006-07 and beyond:
 - How should the state balance competing needs for programs and services with demands for increased spending on public works?
 - What steps are needed to ensure that the state has adequate resources to balance its budget and pay for quality public services?
 - What should the state do to prepare for a population that is growing, aging, and becoming increasingly diverse?
 - How can public policies help narrow the widening gap between the state's high-income and low- and middle-income families?

How Does the Governor Propose to Use the Additional Revenues?

- The Governor's Proposed 2006-07 Budget assumes significantly stronger than previously anticipated revenue collections. The Proposed Budget assumes that combined 2004-05 and 2005-06 revenue collections will be \$5.5 billion higher than was forecast when the current year's budget was signed into law and \$1.7 billion above the LAO's November 2005 forecast. The Governor's 2006-07 revenue forecast is \$929 million above that of the LAO's November 2005 estimate.
- The Governor uses a portion of the higher than anticipated revenues to boost spending for K – 14 Education above the constitutional minimum (\$1.7 billion) and to “buy out” (\$129 million) student fee increases at the University of California and the California State University. The 2006-07 Proposed Budget also funds the expansion of after-school programs, as required by Proposition 49 of 2002.
- The Governor's spending plan also “prepays” some of the state's outstanding debts, including partial repayment of some transportation loans (\$920 million) and an additional payment on outstanding deficit financing bonds (\$460 million).

What Has Changed: The Good News

- The Governor's Proposed 2006-07 Budget assumes significantly stronger than previously anticipated revenue collections. The Proposed Budget assumes that combined 2004-05 and 2005-06 revenue collections will be \$5.5 billion higher than was forecast when the current year's budget was signed into law and \$1.7 billion above the LAO's November 2005 forecast. The Governor's 2006-07 revenue forecast is \$929 million above that of the LAO's November 2005 estimate.
- The increase in revenues is relatively broad-based. Corporate tax collections were significantly above forecast levels during the first half of 2005-06, while personal income and sales tax revenue collections modestly exceeded expectations.
- One outstanding issue is the status of so-called "protective claims" filed under the state's 2005 tax amnesty. Earlier forecasts assumed that the state would give back all but \$380 million of the \$3.8 billion generated by the amnesty. Recent estimates suggest that the outstanding tax issues may take longer to resolve and some observers believe that the state may keep a larger share of the outstanding dollars than previously expected.

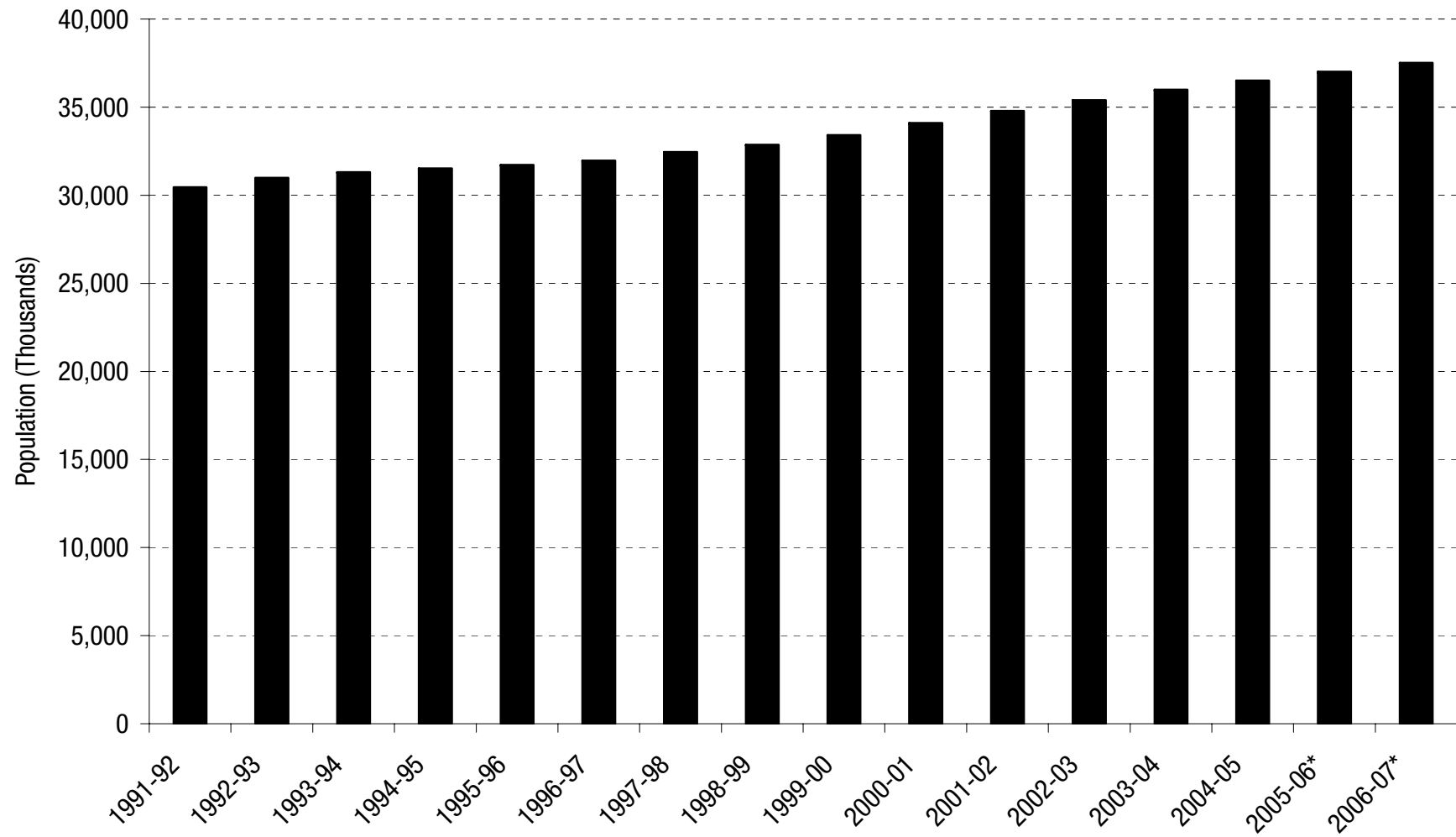
What Has Changed: The Bad News

- The Governor's spending plan reflects higher than previously anticipated costs due to a delay in the issuance of a proposed pension obligation bond (\$525 million). A court rejected the proposed bond for a second time; however, the state plans to appeal the current decision.
- The Governor's proposed spending plan does not take into account the impact of spending reductions and policy changes in the recently approved federal Budget Reconciliation bill.
- The Governor's Proposed Budget includes \$460 million in savings from assuming that it will prevail in a legal challenge over the October 2003 cost-of-living adjustment that is due to families with children in the CalWORKs Program. A lower court previously ruled that the increase should be paid.

California's Changing Demographics Will Increase Demands on the Budget

- Between 2000 and 2020, the state is projected to add approximately 10 million people, an increase roughly equal to the population of the state of Michigan.
- The state's changing demographics will present schools with new challenges. In 2013-14, 61 percent of California's school-age population is expected to be Latino or black, and a sizable minority is likely to be English language learners. These groups of children currently have lower levels of educational attainment at all grade levels.
- Enrollment in California's public colleges and universities is projected to continue to rise, at least through 2013. Undergraduate enrollment at the University of California, the California State University, and the California Community Colleges is anticipated to rise by over 700,000 between 2000 and 2013.
- The most dramatic shift is the projected increase in the number of older Californians. Between 2000 and 2020, the number of Californians age 65 and above is expected to increase by 71.3 percent, compared to a 28.8 percent increase for the state's population overall. Older Californians are expected to be healthier than in the past, but their sheer numbers could strain programs such as Medi-Cal, In-Home Supportive Services, and the Supplemental Security Income/State Supplementary Payment (SSI/SSP) Program.

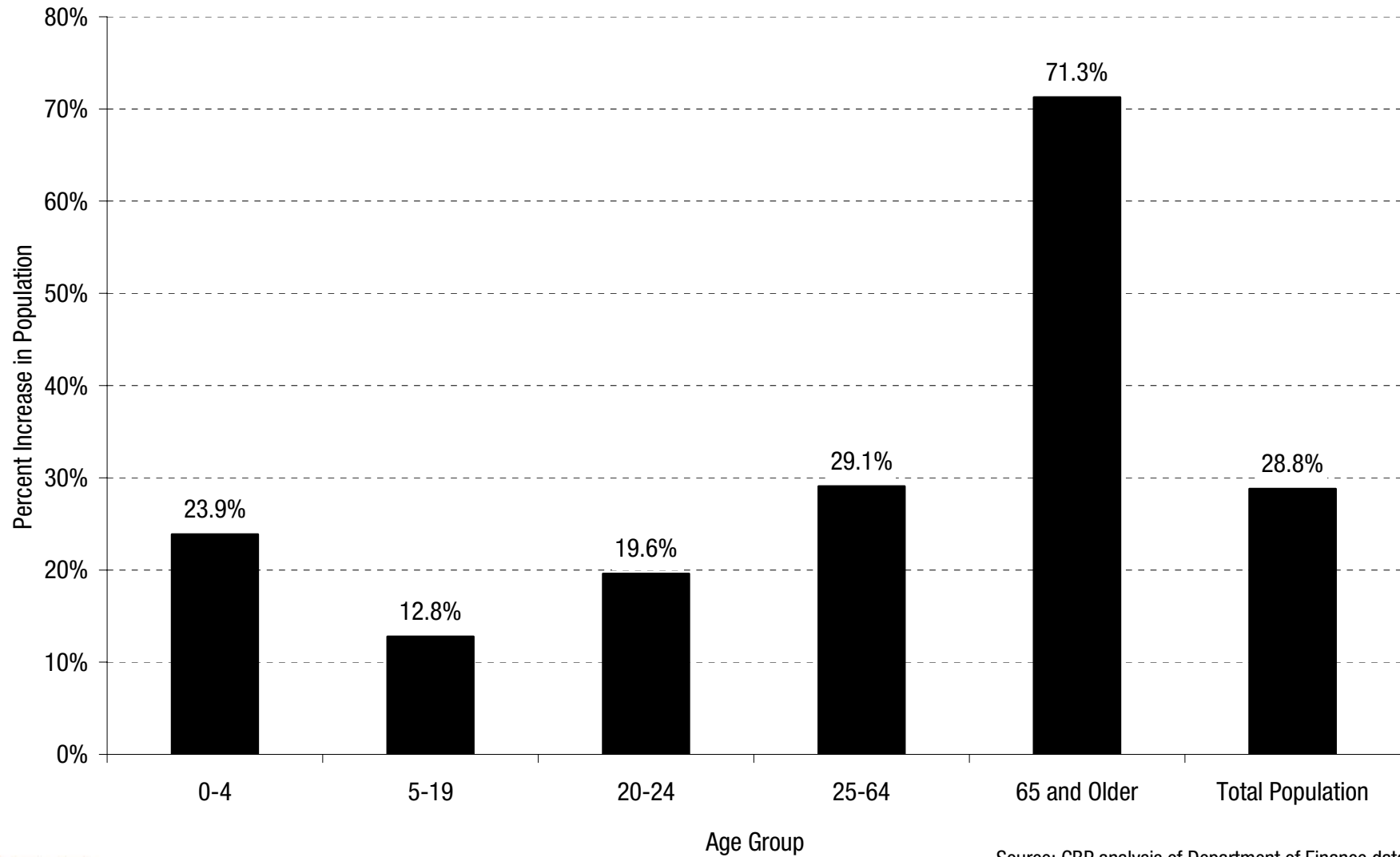
California's Population Continues to Rise



* 2005-06 and 2006-07 estimated.

Source: Department of Finance

California's 65+ Population to Post the Largest Growth Between 2000 and 2020

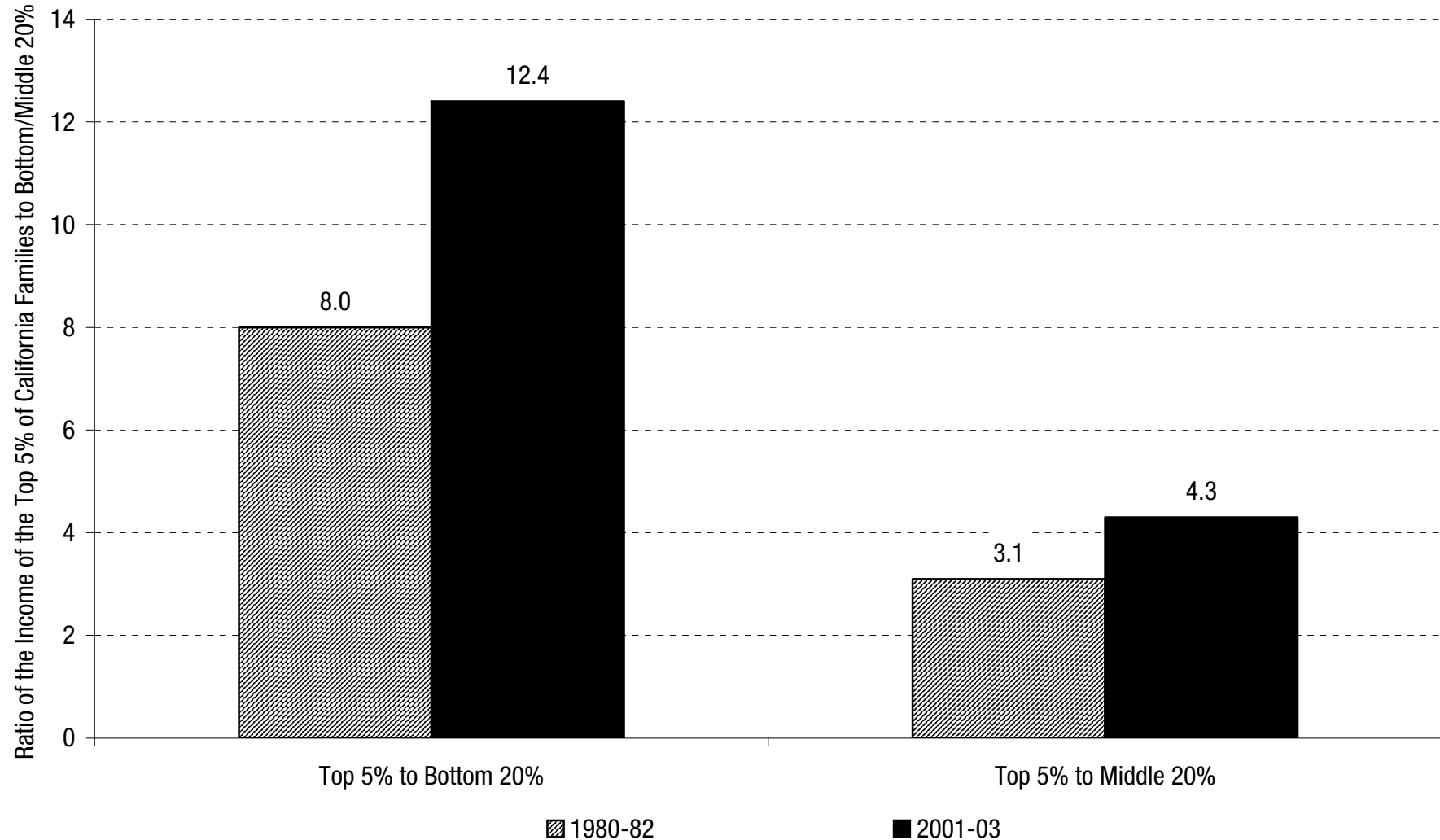


Source: CBP analysis of Department of Finance data

The Growing Gap Between California's Rich and Poor

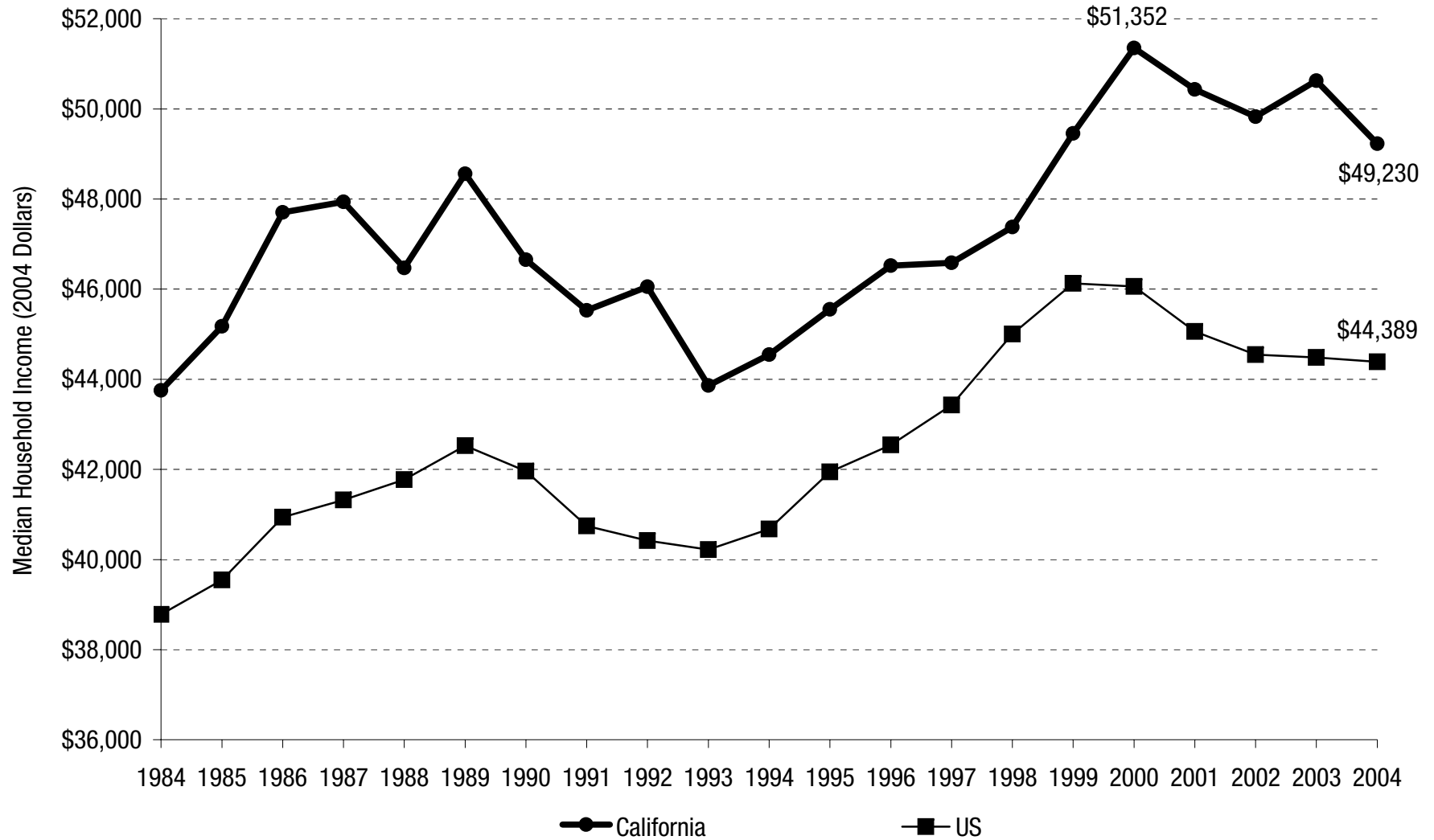
- The gap between California's rich and poor is wide and growing more so. In the early 1980s, the average income of the top 5 percent of California's families was 8.0 times that of the poorest fifth of families. By the beginning of this decade, the top 5 percent earned, on average, 12.4 times as much as the bottom fifth of the state's families. The gap between the top 5 percent and middle fifth of the state's families also widened over the same period, with the average income of the top 5 percent rising from 3.1 times that of the middle fifth in the early 1980s to 4.3 times as much in the early 2000s.
- Between 2003 and 2004, the most recent year for which data are available, the state's median income – the income of the household at the midpoint of the income distribution – fell from \$50,625 to \$49,230.
- During the same period, the share of California's children living in families with incomes below the federal poverty level increased from 18.5 percent to 19.0 percent. The total percentage of Californians with incomes below the poverty level increased from 13.1 percent to 13.3 percent.

The Gap Between Low- and Middle-Income Californians and the Wealthy Has Widened



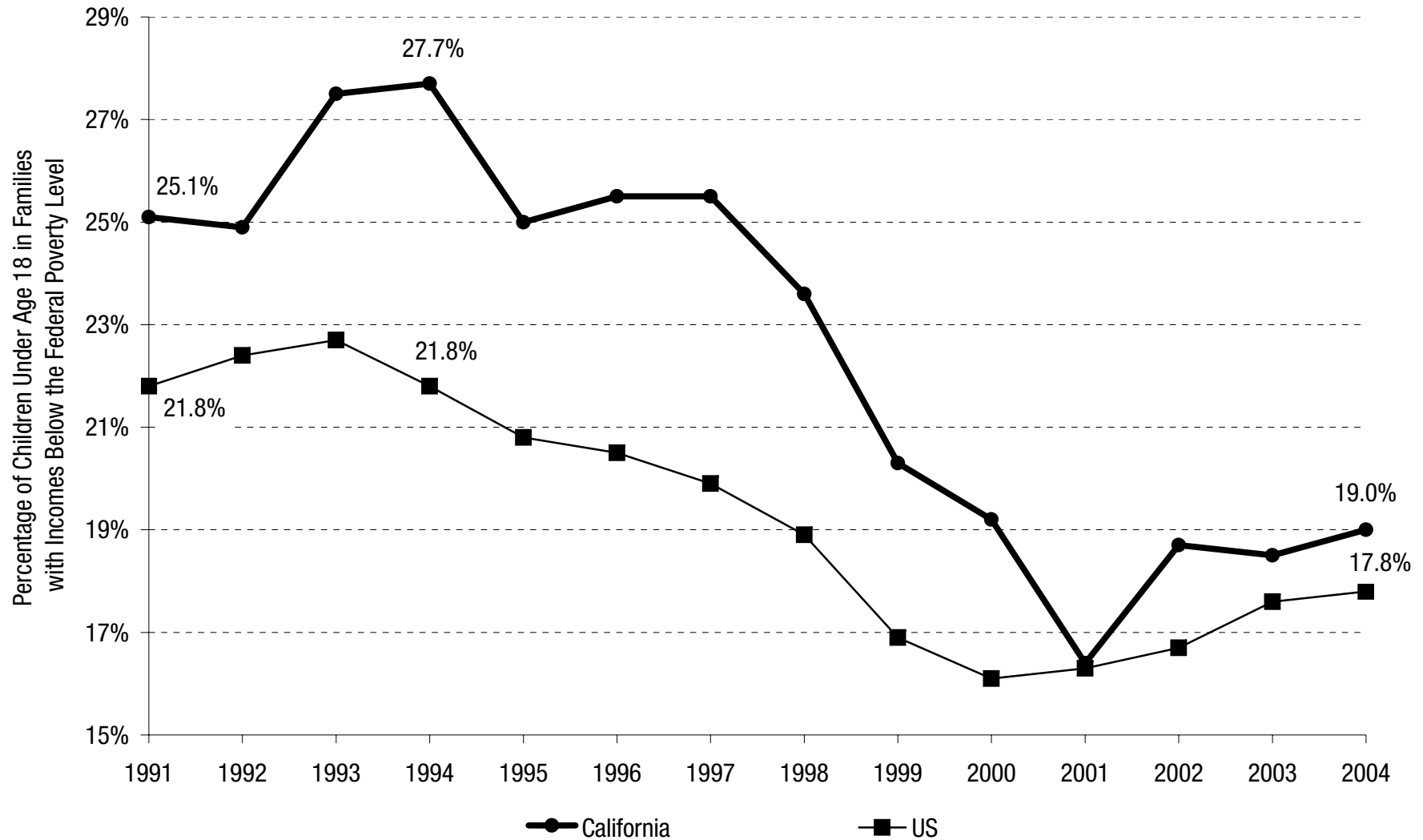
Source: Center on Budget and Policy Priorities and Economic Policy Institute

Median California Household Income Declined in 2004



Source: US Census Bureau

A Larger Share of California's Children Live in Poverty

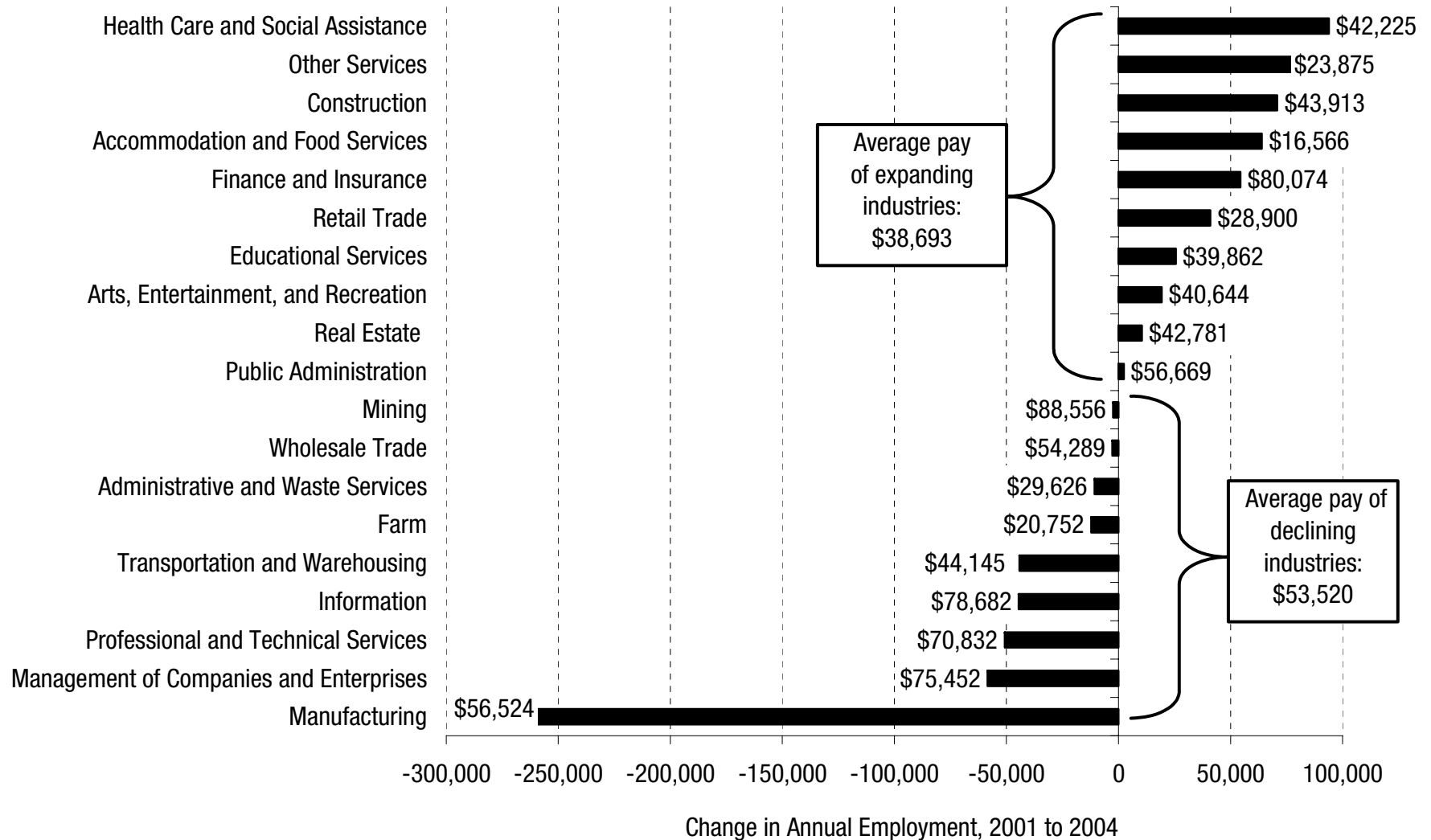


Source: US Census Bureau

The Structure of the State's Economy Has Contributed to the Widening Gap

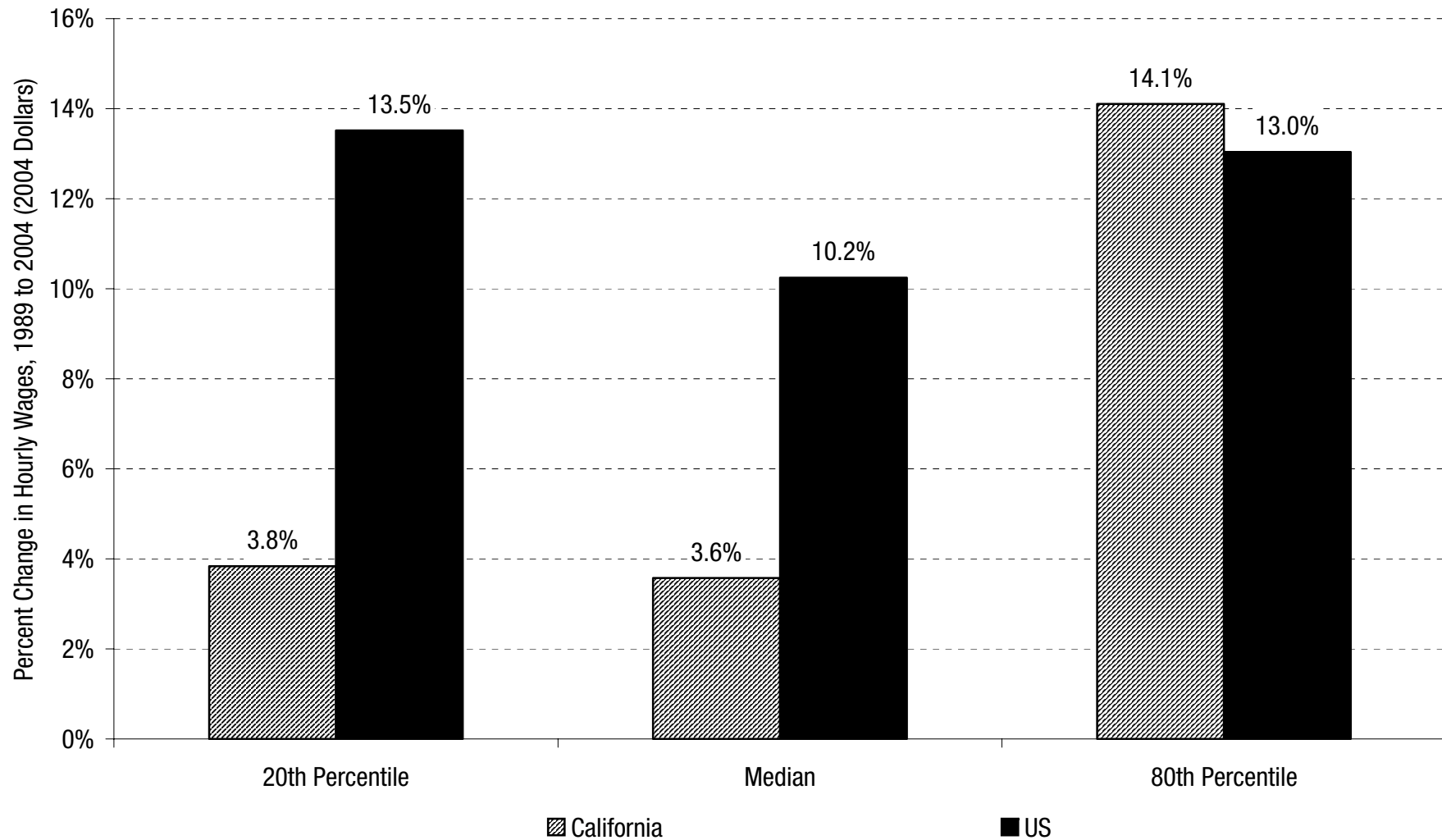
- The structure of the state's economy contributes to the widening income gap:
 - The average annual pay of sectors that lost jobs between 2001 and 2004 was substantially higher (\$53,520) than that of sectors that gained jobs (\$38,693).
 - The growth in hourly earnings of California workers at the bottom and middle of the wage distribution lagged that of the nation between 1989 and 2004. The growth in earnings of high-wage California workers, in contrast, exceeded that of the nation.
 - Five of the 10 occupations with the largest projected job growth pay the typical worker – the worker at the midpoint of the earnings distribution – less than \$10 per hour, equivalent to an annual salary of \$20,800 for full-time, full-year work.
- The percentage of non-elderly Californians lacking health coverage increased in 2004, from 20.3 percent to 20.8 percent.

Average Pay of Expanding Industries Was Lower Than That of Declining Industries



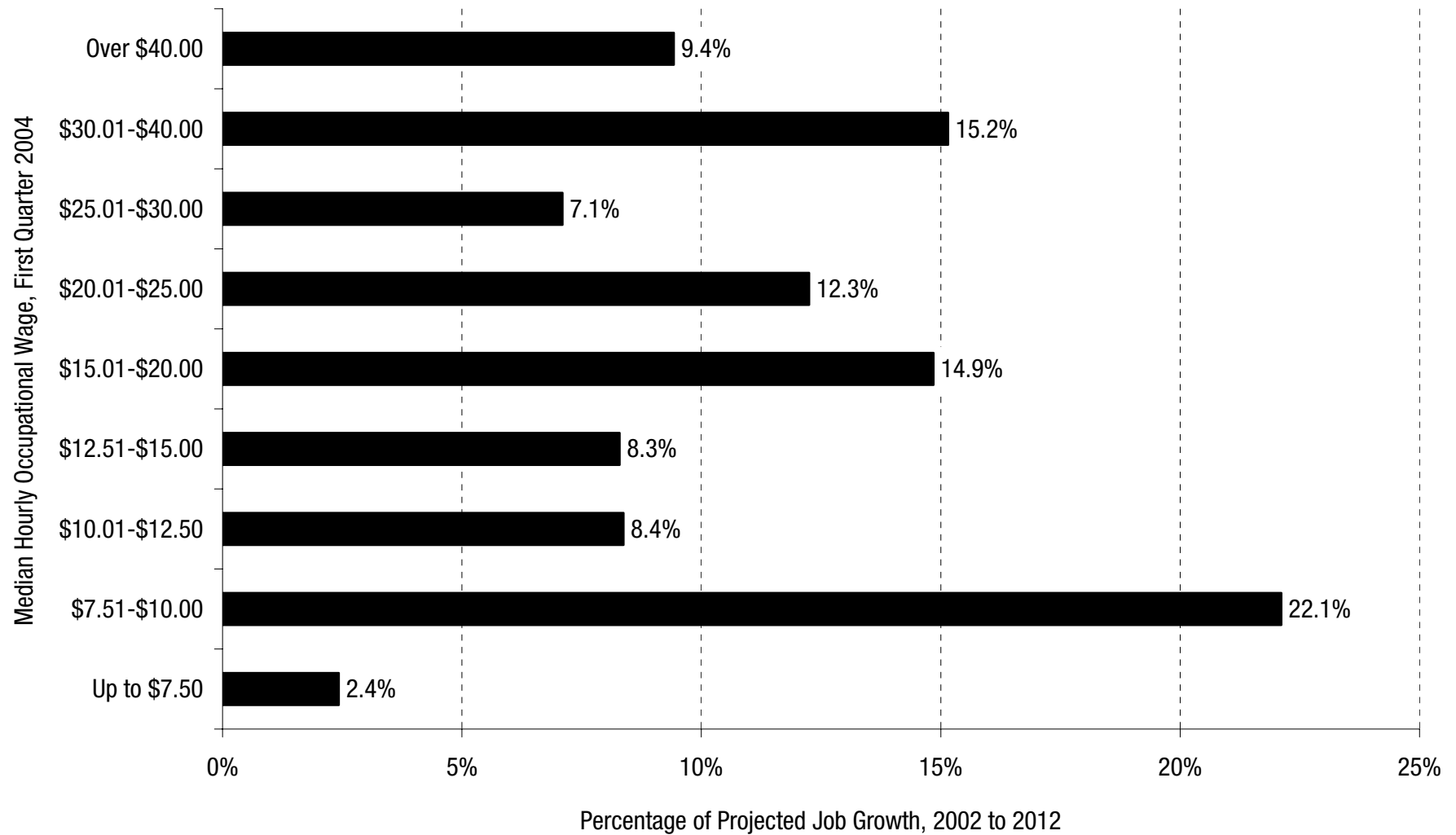
Source: Employment Development Department

California's Wage Growth Lagged That of the Nation Except Among High-Wage Earners, 1989 to 2004



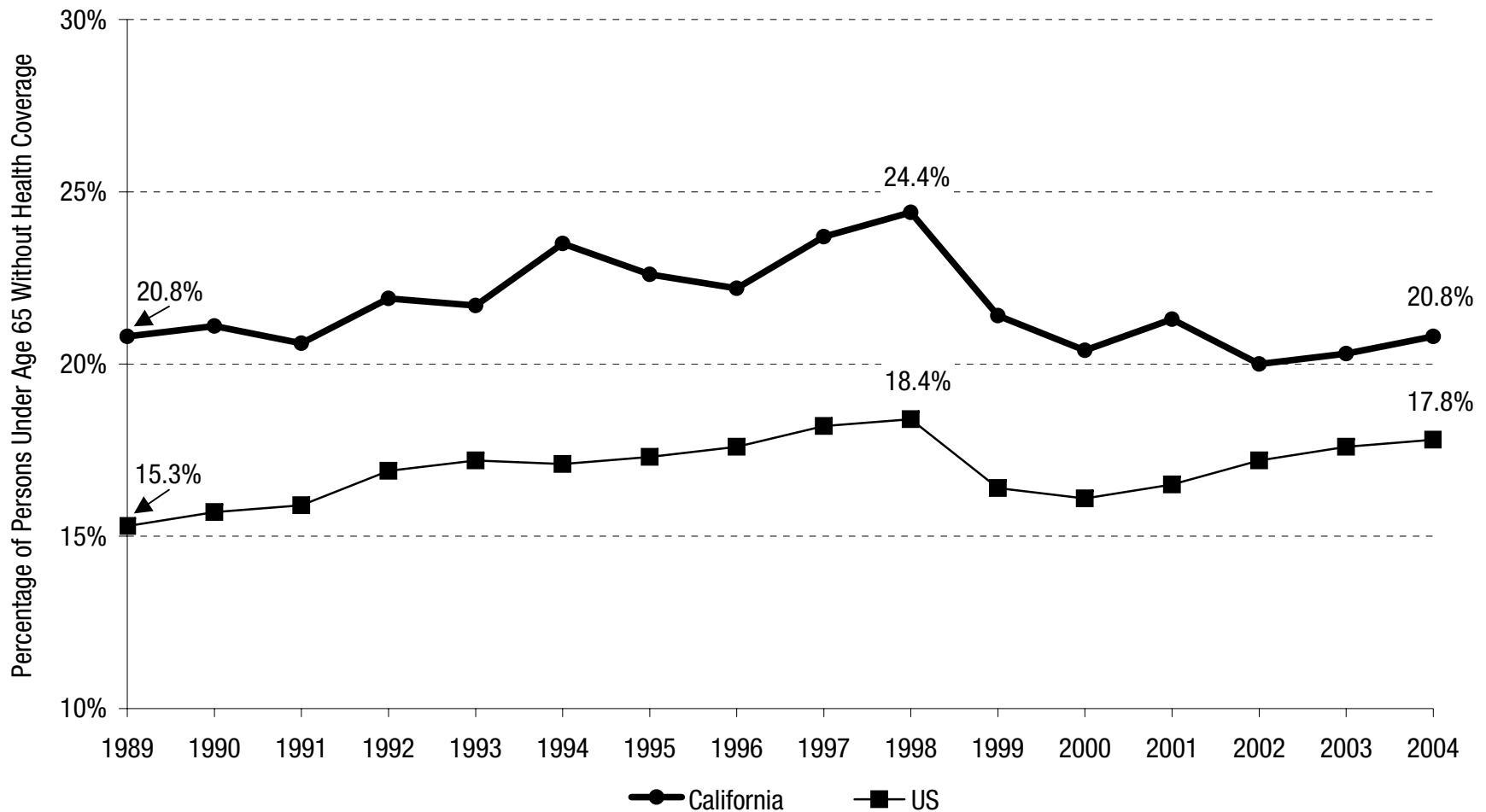
Source: Economic Policy Institute analysis of Current Population Survey data

A Quarter of Projected New Jobs Typically Pay \$10 Per Hour or Less



Source: CBP analysis of Employment Development Department data

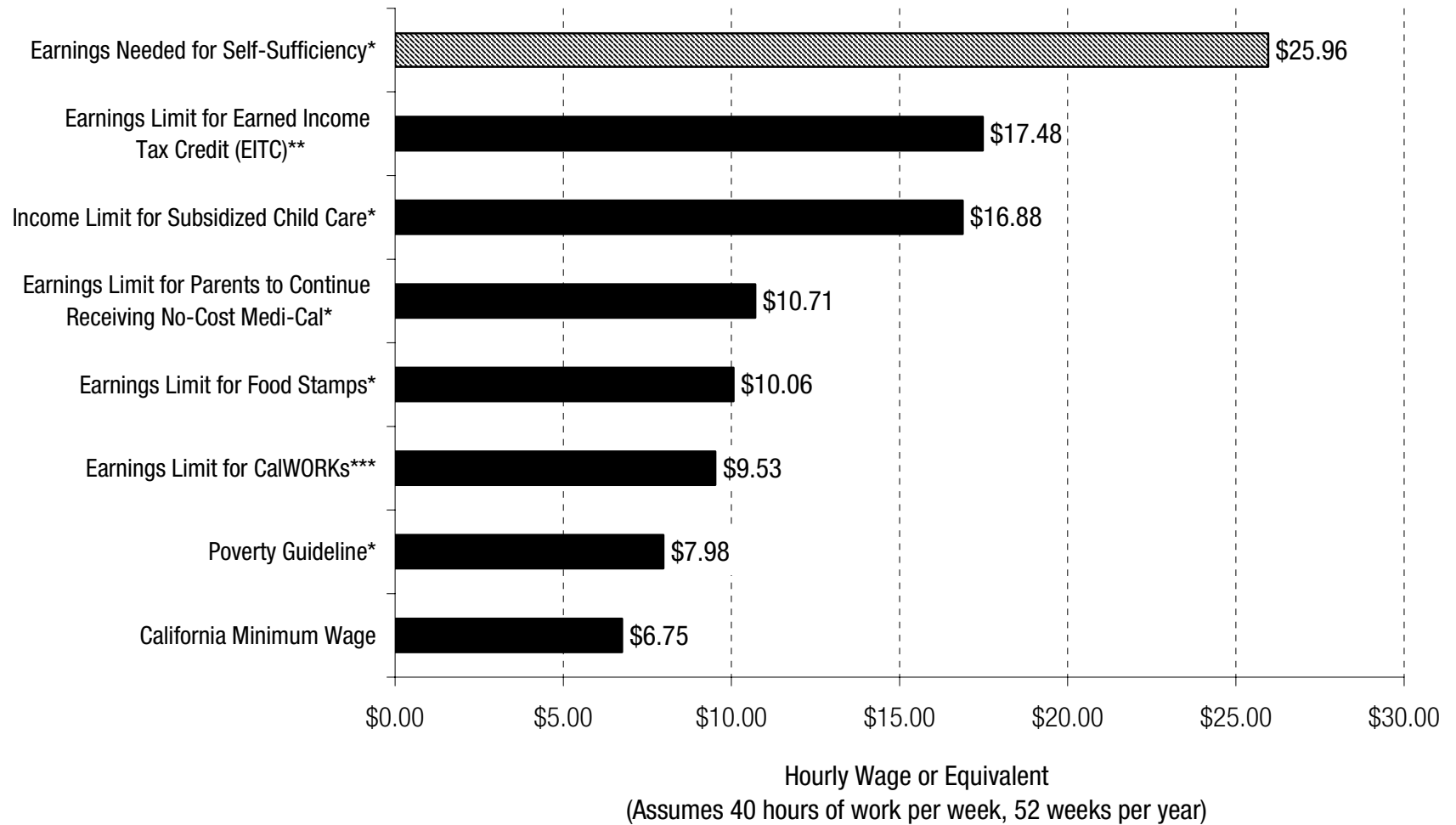
The Share of Non-Elderly Californians Without Health Coverage Increased in 2004



Note: Methodological changes led to lower estimates of the number of uninsured persons beginning in 2000.

Source: US Census Bureau

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.

Governor Proposes to Increase the Minimum Wage

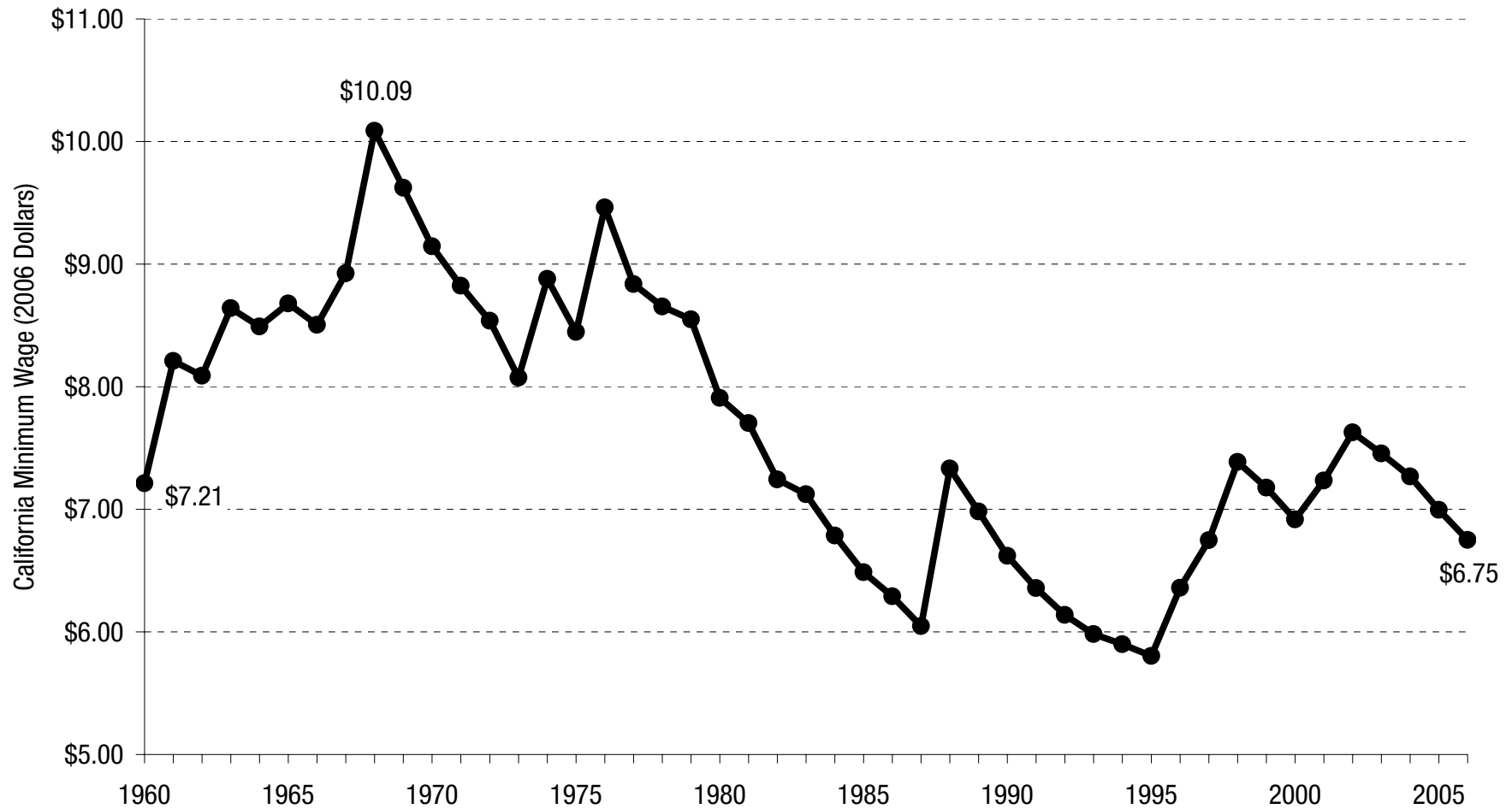
- In his State of the State address, the Governor proposed to increase California's minimum wage by one dollar per hour over 18 months.
- 1.4 million California workers – 10.3 percent of the workforce – earn within one dollar of the minimum wage. These low-wage workers work throughout the economy, but are concentrated in leisure and hospitality and wholesale and retail trade.
- Contrary to popular stereotypes, most workers earning within one dollar of the minimum wage are adults and/or full-time workers.
- The purchasing power of the minimum wage has declined by 33.1 percent since 1968. The Governor's proposal would increase the purchasing power of the minimum wage to just below its 2002 level.
- Absent periodic adjustments for inflation, the purchasing power of the minimum wage will continue to erode.

The Majority of California's Low-Wage Workers Are Adults and/or Full-Time Workers

	Low-Wage Workers	All Workers
<u>Age</u>		
16 to 19	16.8%	4.2%
20 to 24	23.5%	11.6%
25 to 64	59.7%	84.2%
<u>Gender</u>		
Male	50.4%	53.8%
Female	49.6%	46.2%
<u>Race/Ethnicity</u>		
Latino	57.1%	32.1%
White	26.5%	47.2%
Other	16.4%	20.7%
<u>Hours of Work</u>		
Full-time (35 or More Hours Per Week)	59.1%	82.0%
Part-time		
20 to 34 Hours Per Week	28.1%	13.1%
1 to 19 Hours Per Week	12.8%	4.9%
<u>Industry</u>		
Educational and Health Services	10.0%	20.2%
Leisure and Hospitality	25.5%	8.7%
Manufacturing	11.2%	11.9%
Wholesale and Retail Trade	22.2%	14.8%
All Others	31.1%	44.4%

Source: CBP analysis of Current Population Survey data

Purchasing Power of California's Minimum Wage Has Dropped 33 Percent Since 1968



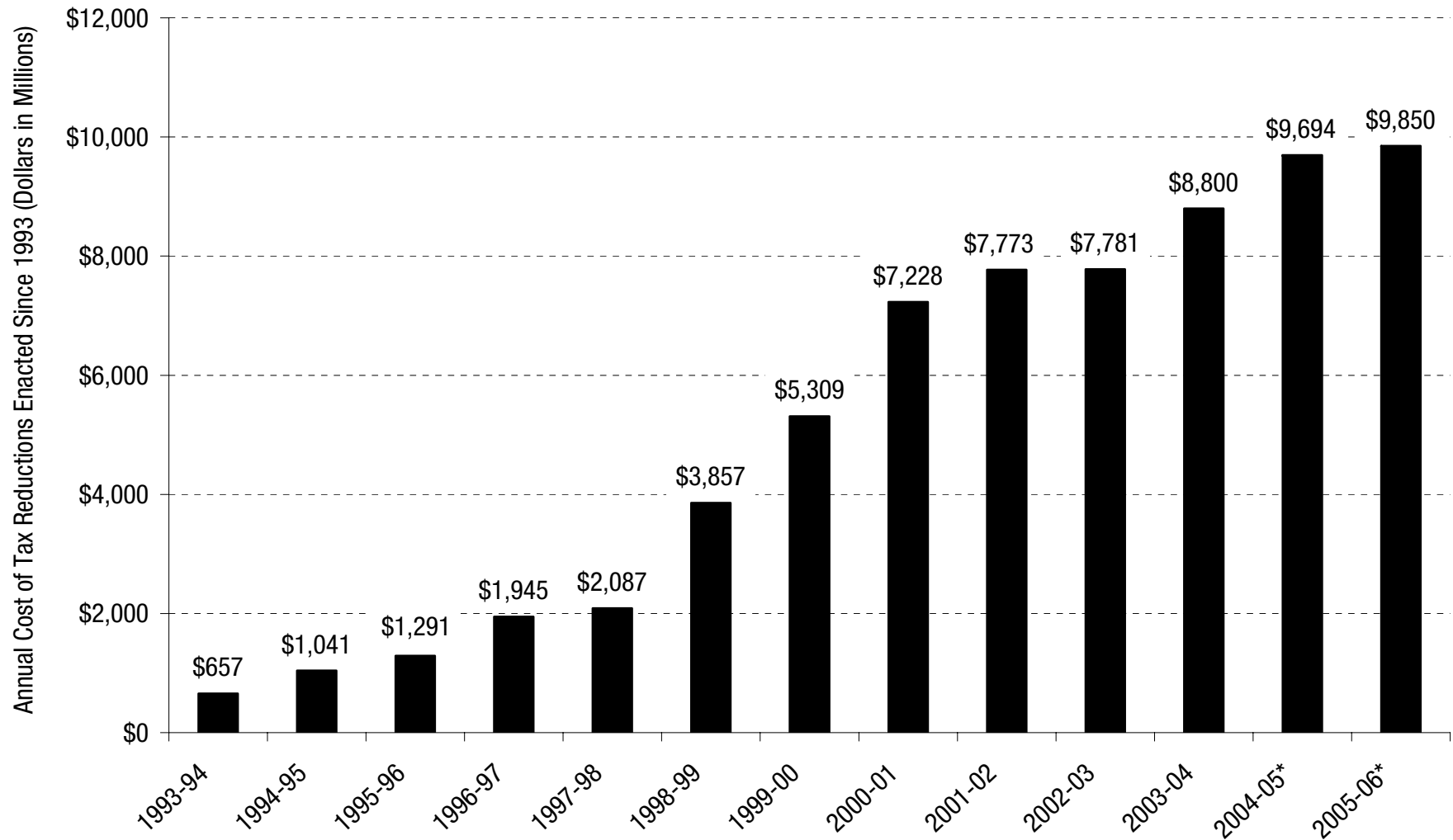
Note: 1968-73 reflects California minimum wage for women (\$1.65); minimum wage for men was \$1.60.

Source: Department of Finance

California's Tax System Fails to Generate Sufficient Revenues: A Revenue-Side Explanation of the State's Budget Gap

- Conventional explanations of the state's fiscal troubles focus on increases in spending during the late 1990s and formula-driven increases in school funding, transportation, and other programs.
- In fact, tax cuts enacted between 1993 and 2005 will reduce 2005-06 revenues by an estimated \$9.9 billion – an amount that far exceeds the state's ongoing shortfalls. The \$4.6 billion cost of the reduction in Vehicle License Fees alone exceeds the gap between projected 2006-07 revenues and expenditures. Other large cuts include an expansion of the dependent tax credit (\$886 million), a corporate tax rate reduction (\$506 million), and increased net operating loss deductions (\$505 million).
- The phase-out of the federal estate tax will cost the state over \$1.1 billion in 2006-07. The 2001 federal tax package phases 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 proposes making the repeal permanent.

Tax Cuts Enacted Since 1993-94 Will Cost \$9.9 Billion in 2005-06



*2004-05 and 2005-06 estimated.

Source: Franchise Tax Board, Legislative Analyst's Office, Department of Finance, and Assembly Revenue and Taxation Committee

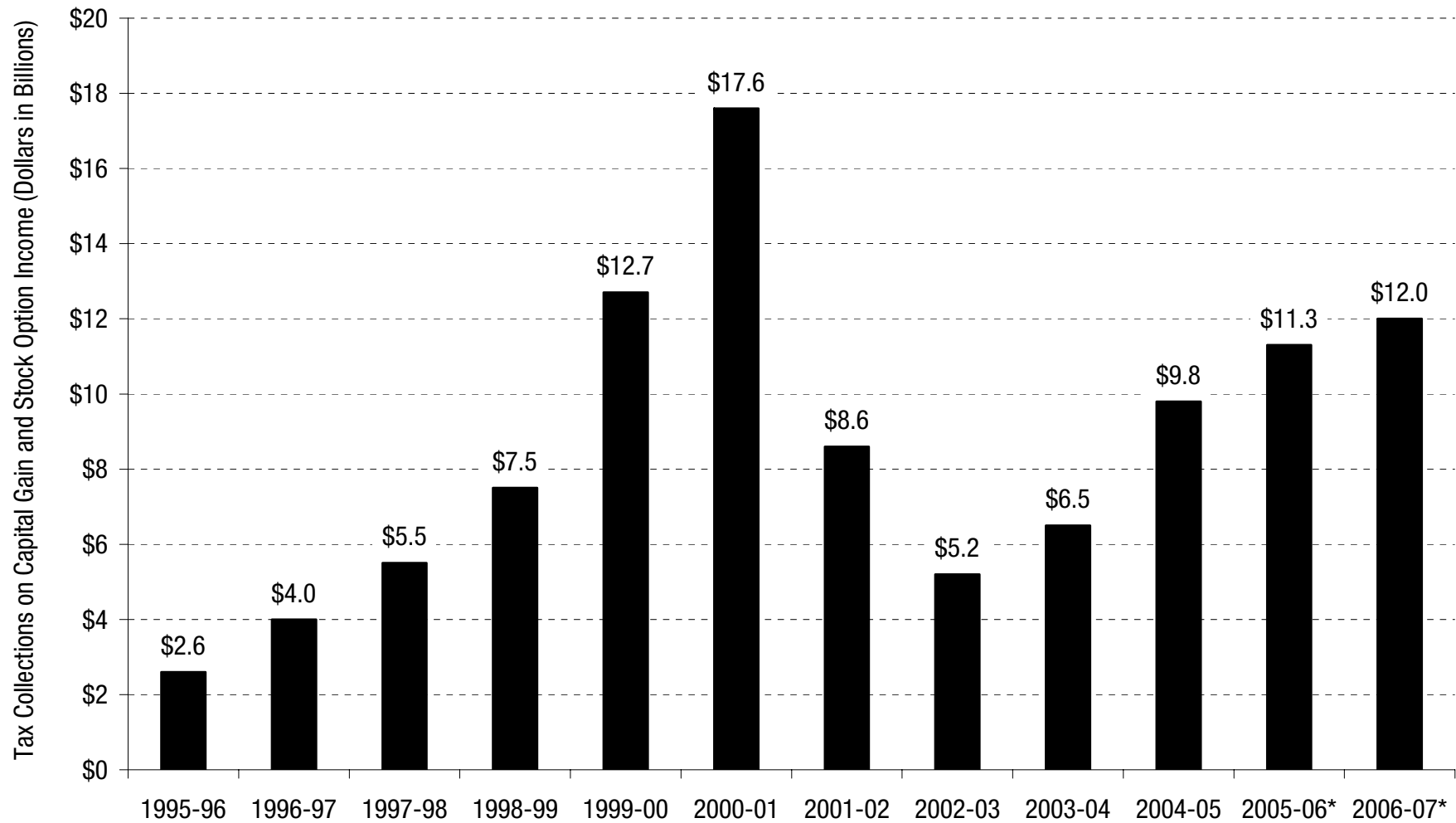
The Structure of the State's Tax System

Contributes to the Budget Gap

The structure of the state's tax system also contributes to the state's budget gap:

- The drop in tax collections attributable to stock options and capital gains exceeds the size of projected budget gaps. The state collected \$17.6 billion in income taxes paid on stock options and capital gains in 2000-01. Collections dropped to \$5.2 billion in 2002-03. The Department of Finance estimates that these sources of income will generate \$12.0 billion in tax revenues in 2006-07.
- Corporate income taxes have declined over time when measured as a share of total General Fund revenues and as a share of corporate profits. While revenues have increased modestly in recent years, the increase in tax collections lags far behind the growth in 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. If taxable purchases accounted for the same share of personal income in 2006-07 as they did in 1966-67, the state would collect an additional \$12.5 billion in sales tax revenues.
- Alcohol and tobacco tax revenues have been stagnant over time, reflecting societal consumption trends.

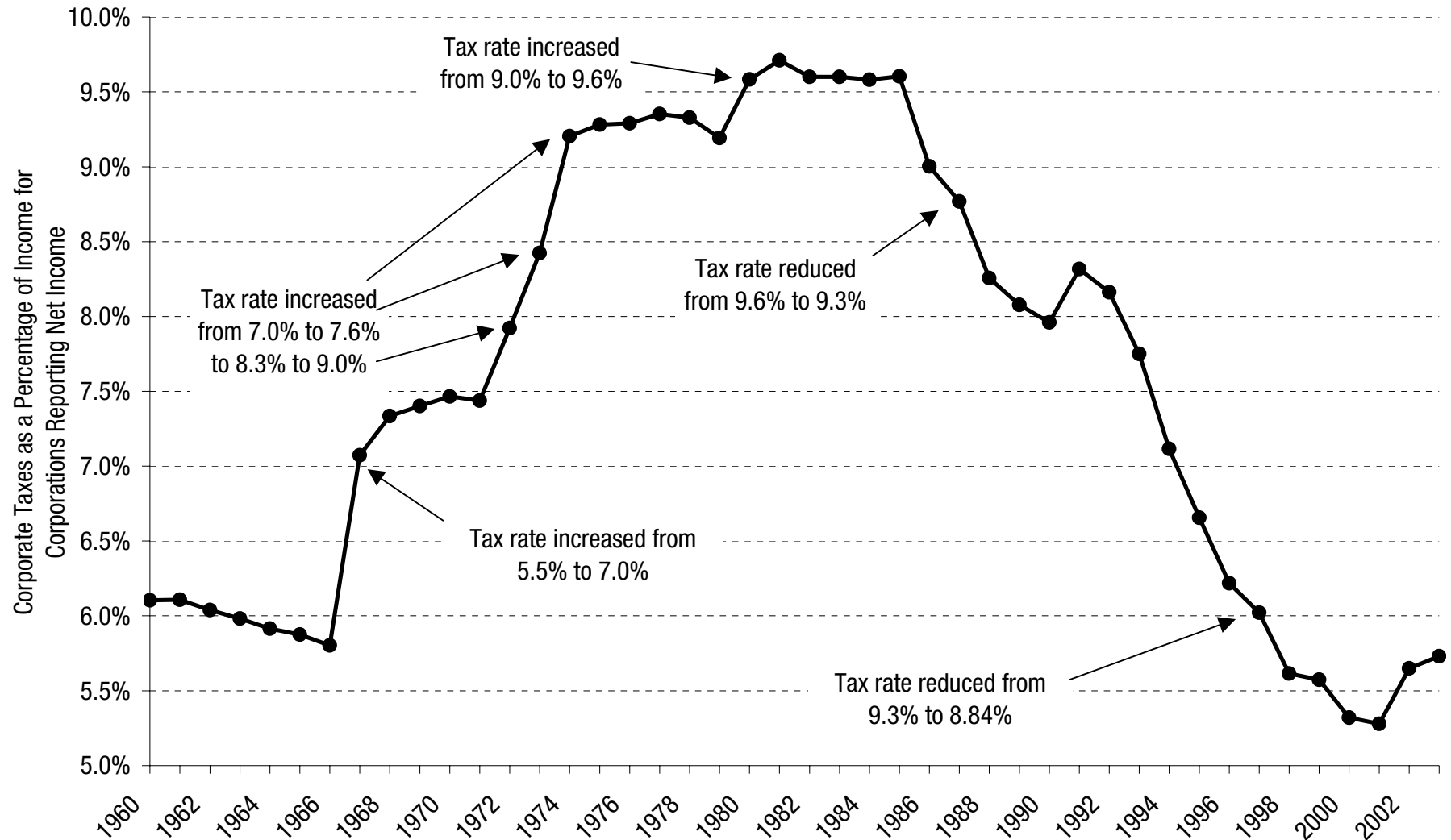
Revenues from Stock Options and Capital Gains Are Still Significantly Below Boom Levels



*2005-06 and 2006-07 estimated.

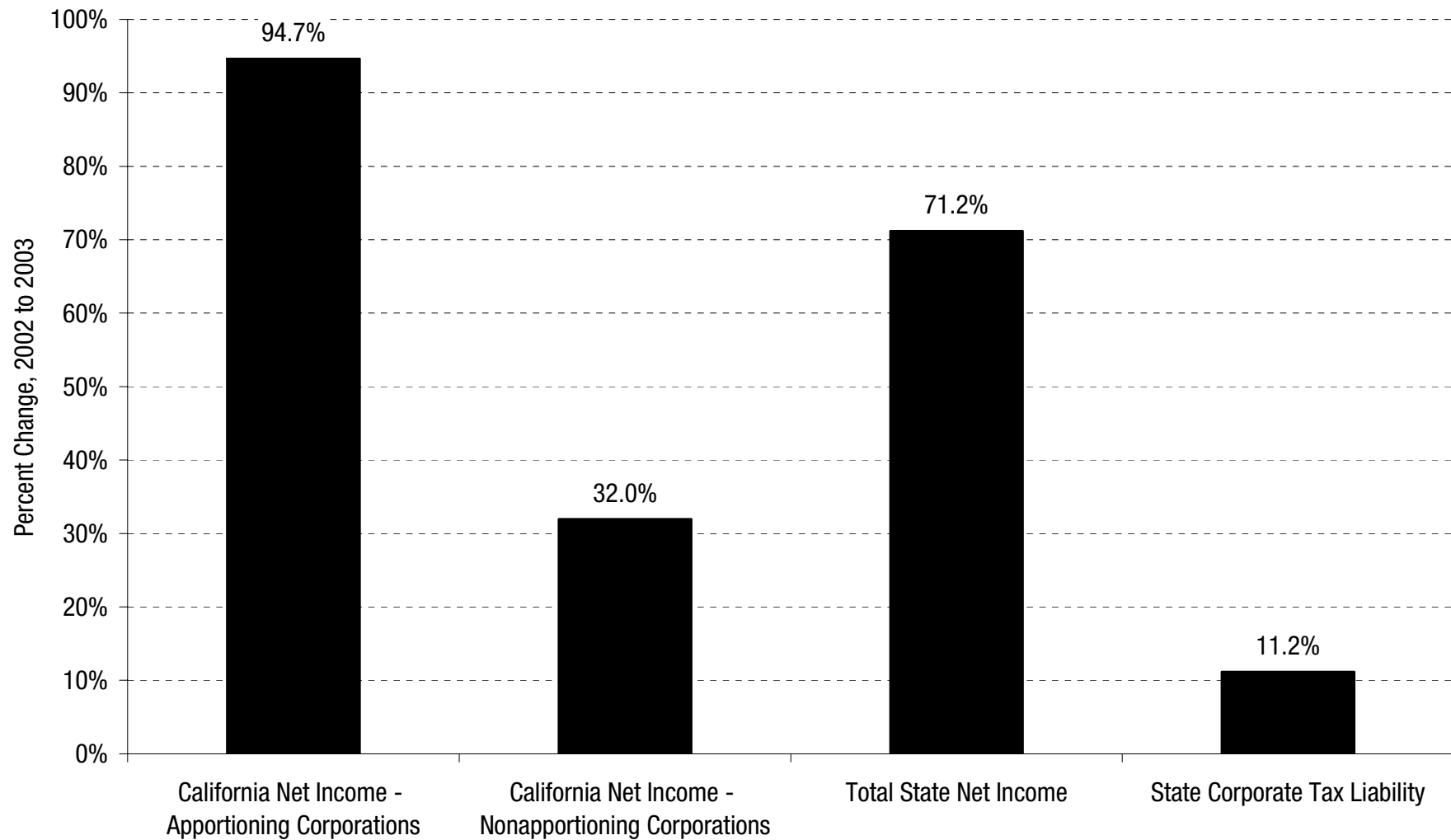
Source: Department of Finance

Despite Modest Increase Recently, Share of Corporate Income Paid in Taxes Has Fallen 41 Percent Since 1981



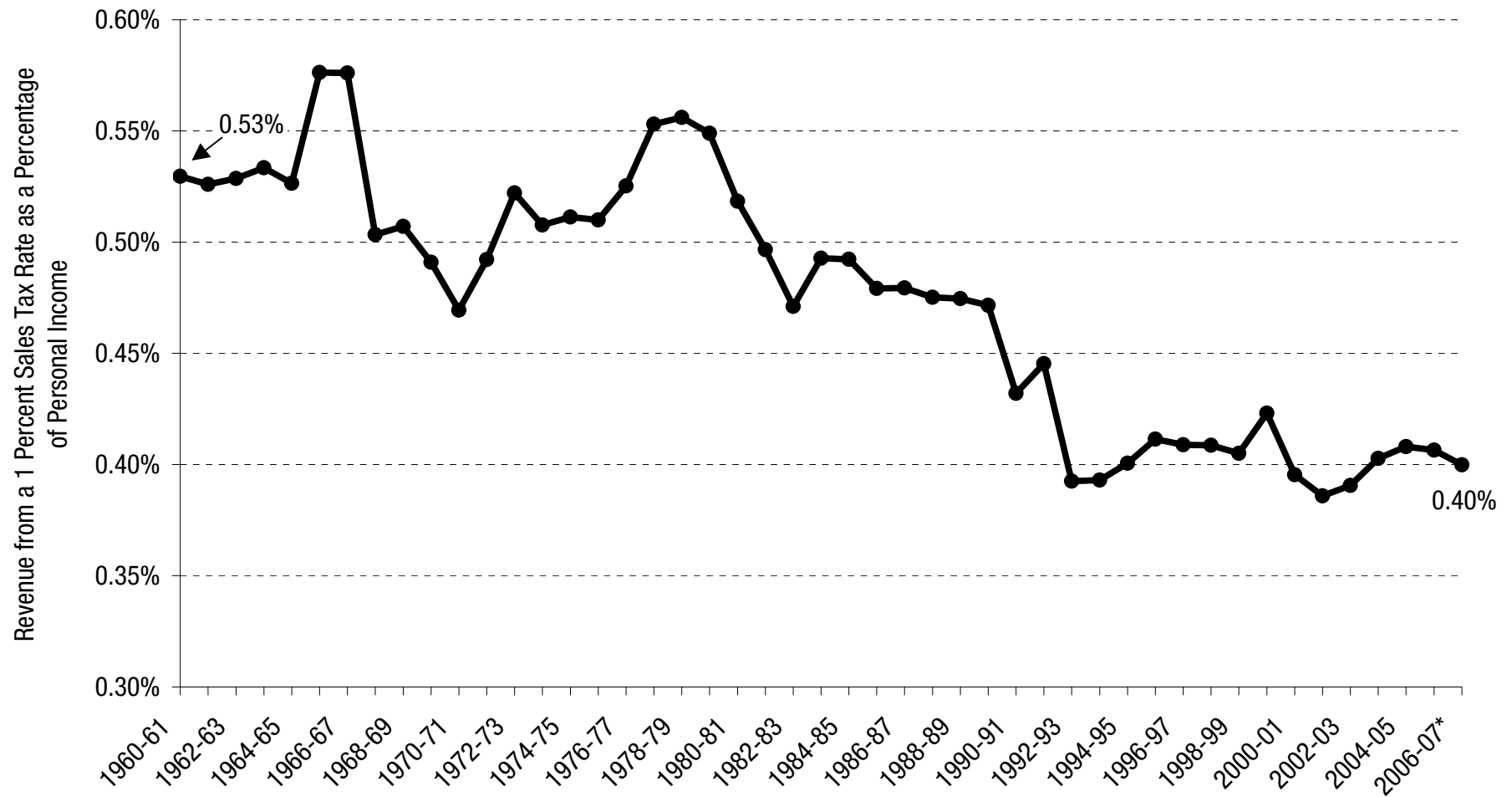
Source: Franchise Tax Board

Growth in Profits Far Outstrips the Increase in Corporate Tax Liability



Source: Franchise Tax Board

Sales Tax Collections Have Declined as a Share of Personal Income



* 2005-06 estimated and 2006-07 projected.

Source: Legislative Analyst's Office, Department of Finance, and Board of Equalization

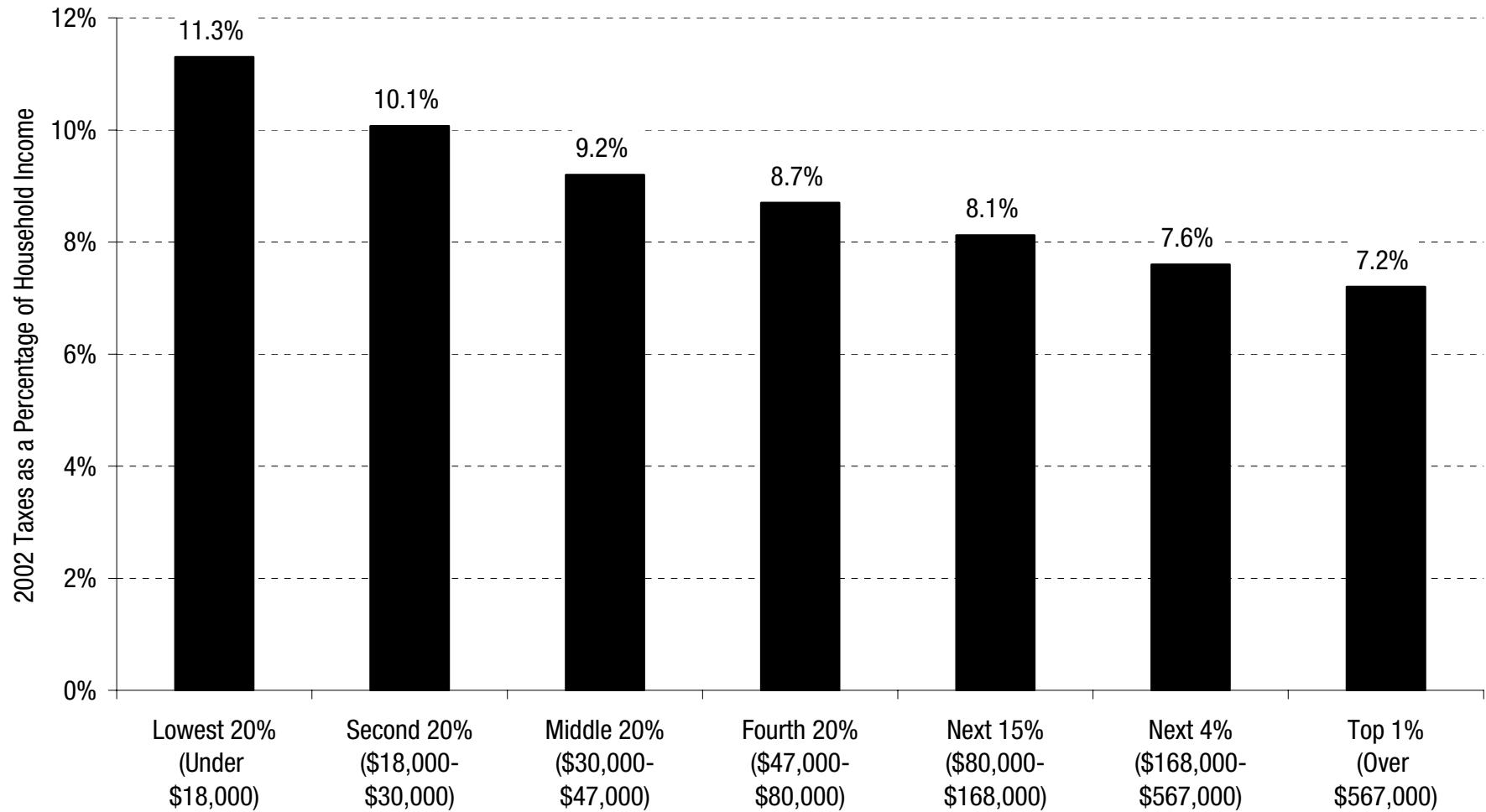
How Does California Compare?

Revenues as a Percentage of Personal Income

	California Rank	California	US
Total State and Local Own Source (2001-02)	18	15.69%	15.11%
Total State and Local Taxes (2001-02)	14	10.59%	10.32%
State Taxes (2003-04)	15	7.03%	6.33%
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 (2003-04)	28	2.17%	2.12%
State Motor Fuels Taxes (2003-04)	45	0.27%	0.36%
State Tobacco Tax (2003-04)	36	0.09%	0.13%
State Alcoholic Beverage Sales Taxes (2003-04)	39	0.03%	0.05%
State Individual Income Tax (2003-04)	7	2.98%	2.11%
State Corporate Income Tax (2003-04)	5	0.57%	0.33%

Source: US Census Bureau and US Bureau of Economic Analysis

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.

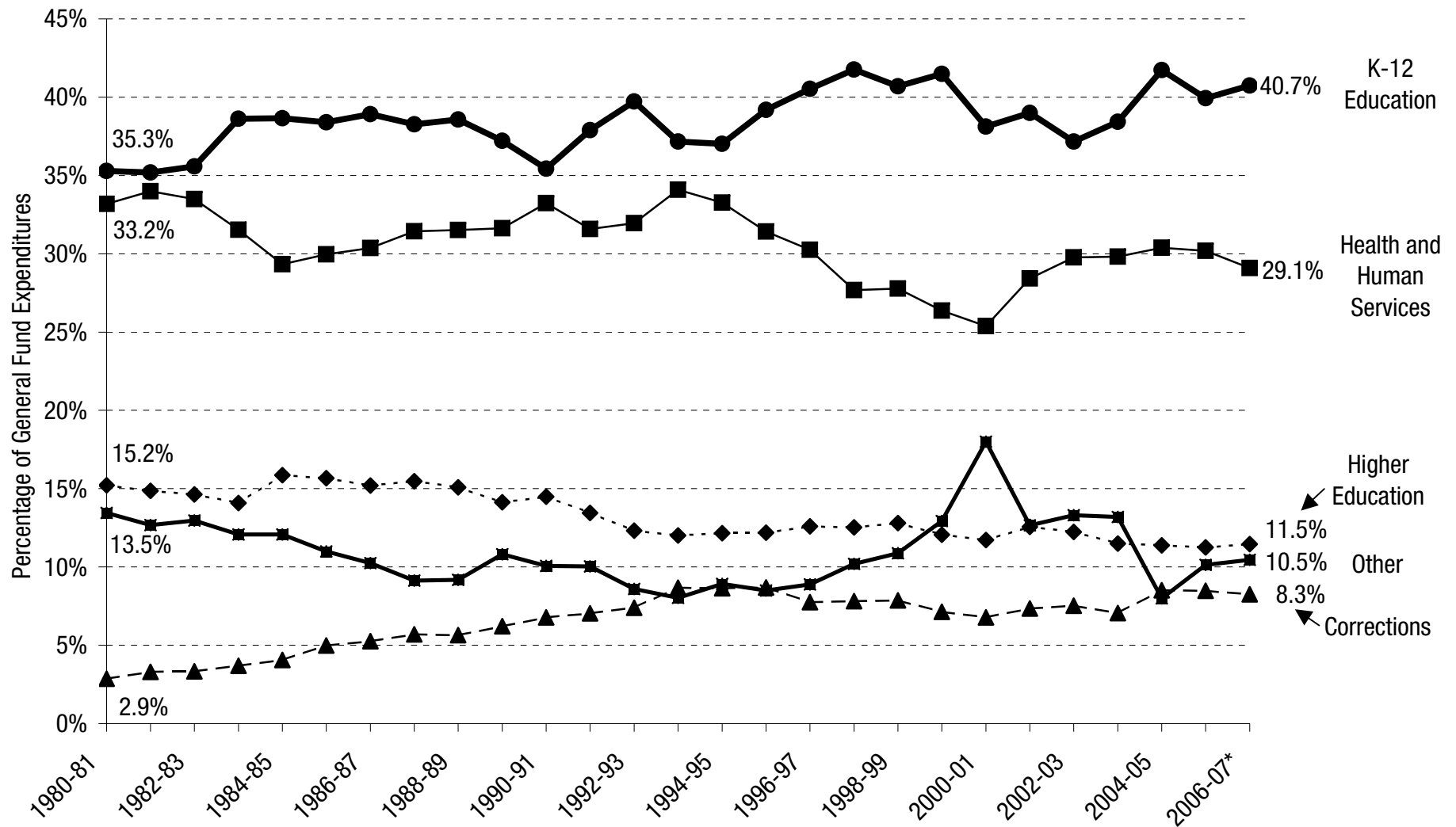
Source: Institute on Taxation and Economic Policy

The Basics

The Governor's Proposed 2006-07 Budget:

- Increases spending by \$7.6 billion (8.4 percent), including a \$460 million prepayment on the state's deficit financing bonds, and assumes that revenues will increase by \$4.3 billion (4.9 percent). Under the Governor's proposals, the state would end the fiscal year with reserves of \$613 million, equal to 0.6 percent of proposed expenditures.
- Uses a \$7.0 billion balance carried forward from the current year to bridge the gap between anticipated revenues and proposed expenditures.
- Includes significant increases for K – 12 Education, Higher Education, and Transportation.
- Cuts spending for CalWORKs, SSI/SSP, and does not fund inflation adjustments for county-administered human service programs.
- Does not include funding for additional salary or benefit costs for 18 of the state's 21 collective bargaining units that have expired or soon-to-expire agreements.
- Assumes \$258 million in unallocated reductions to state agency and personnel spending.

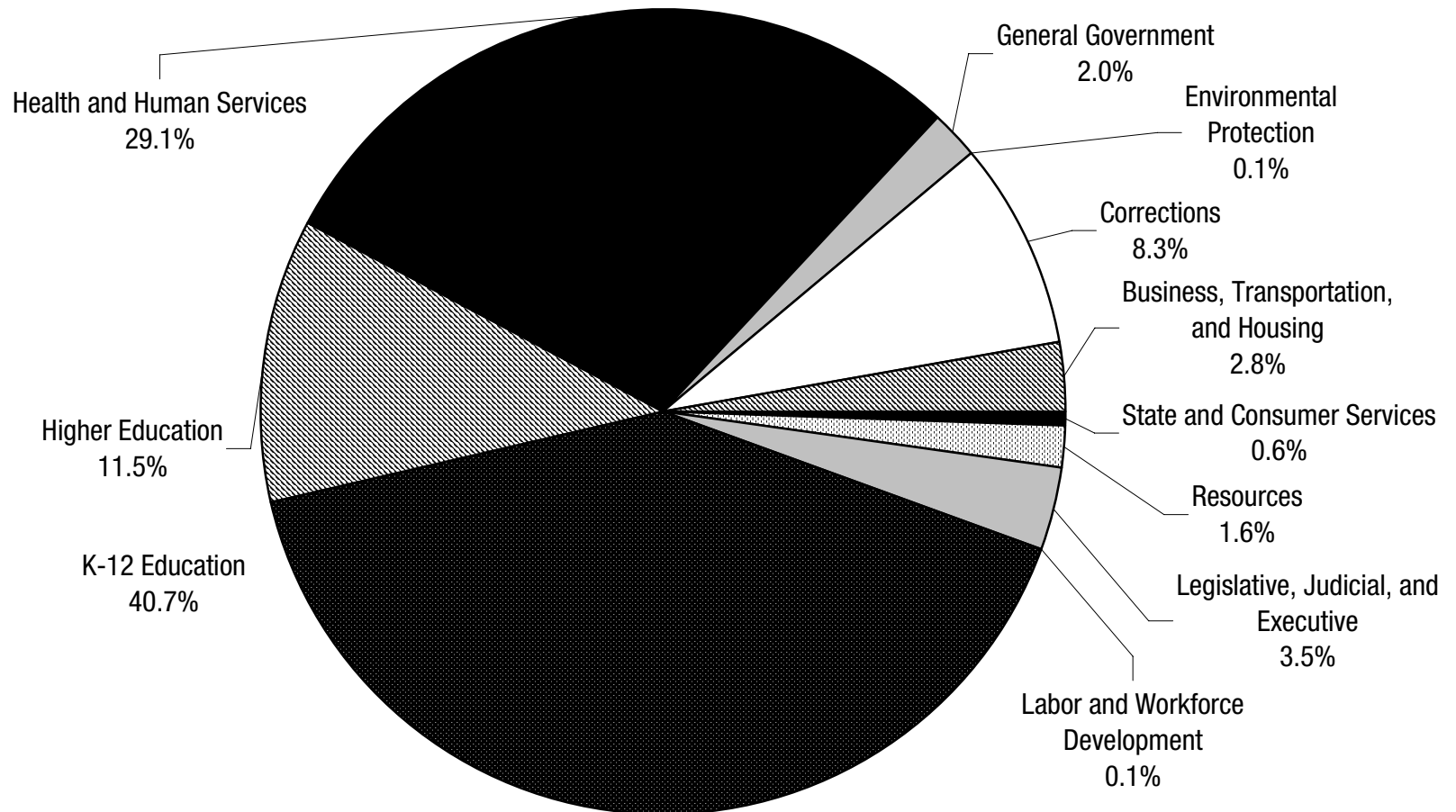
K-12 Education Accounts for the Largest Share of State General Fund Spending



* 2005-06 estimated and 2006-07 proposed.
Source: Department of Finance

Education Accounts for the Largest Share of 2006-07 Spending

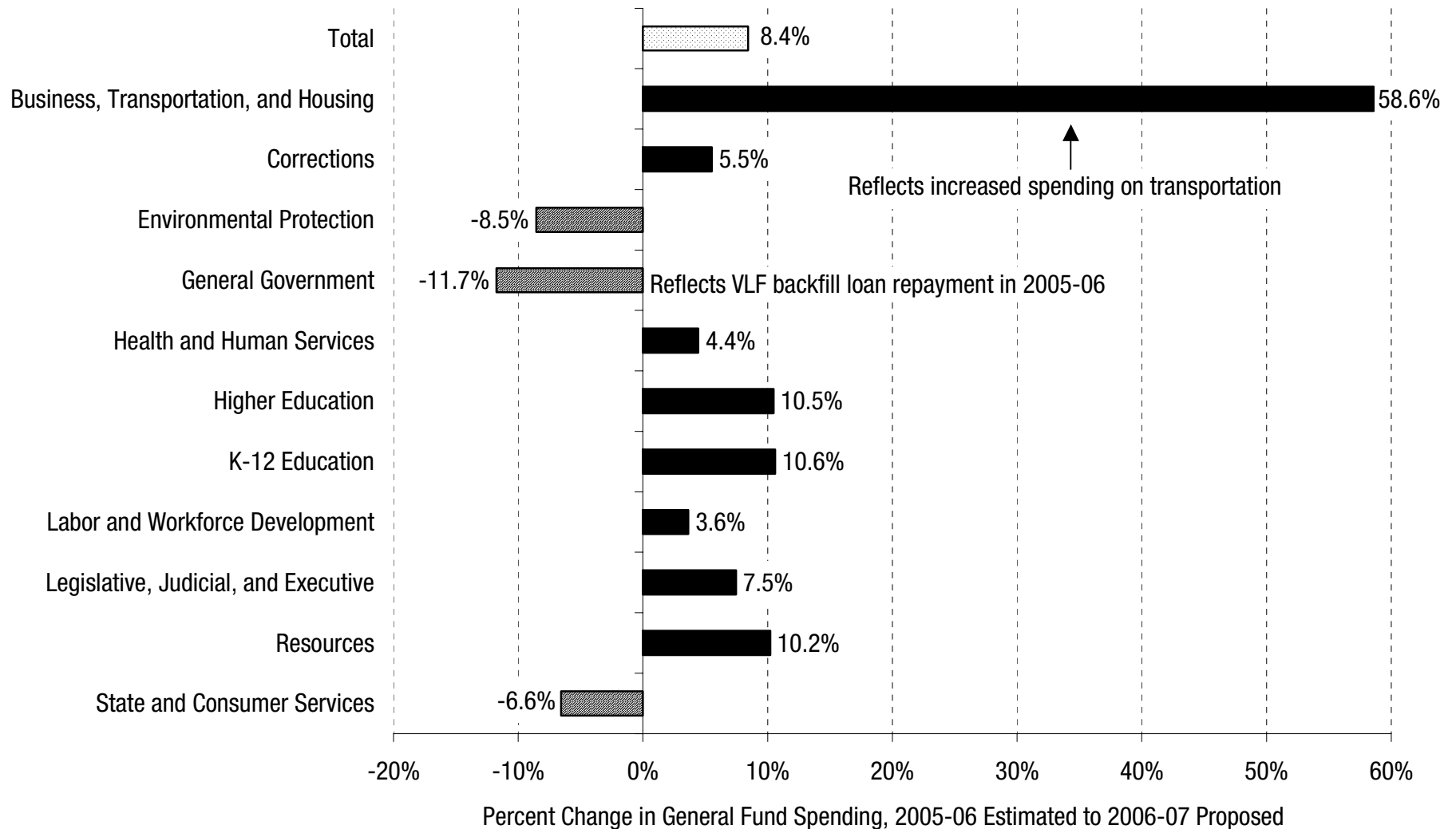
General Fund Spending by Agency



Proposed 2006-07 General Fund Expenditures = \$97.9 Billion

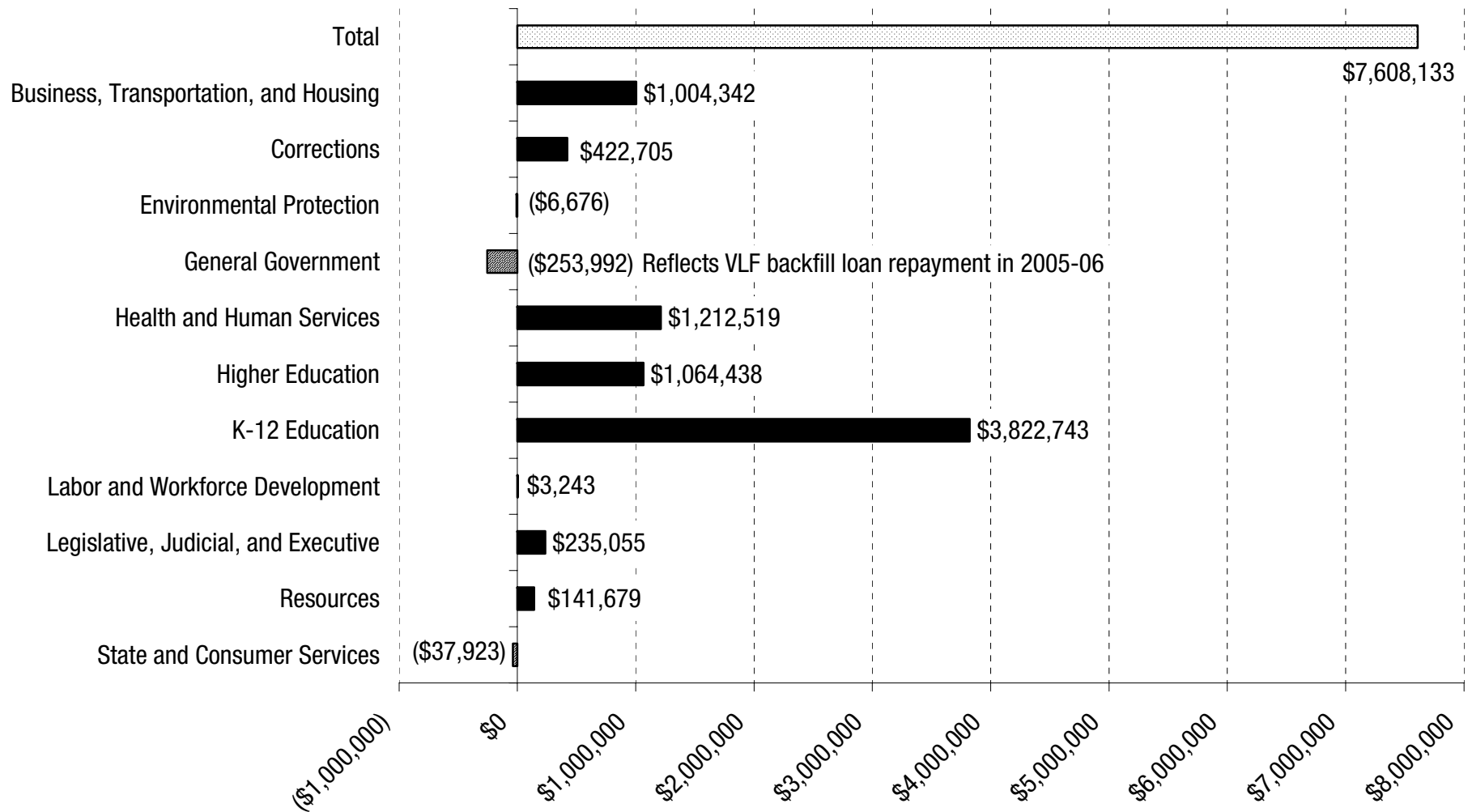
Source: Department of Finance

Spending Up Significantly for Transportation, Education, Resources



Source: Department of Finance

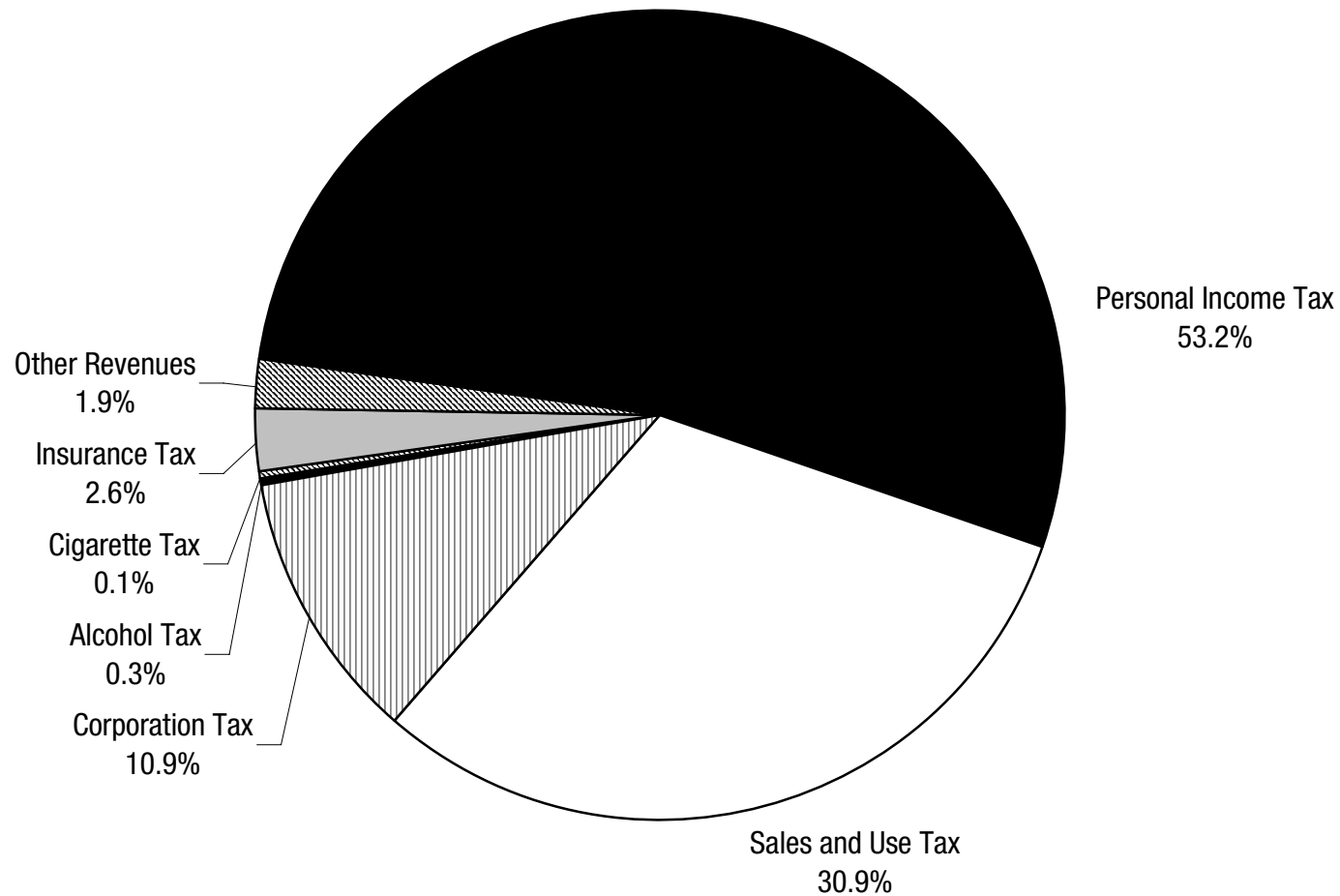
General Fund Spending Up By \$7.6 Billion



General Fund Spending Change, 2005-06 Estimated to 2006-07 Proposed (Dollars in Thousands)

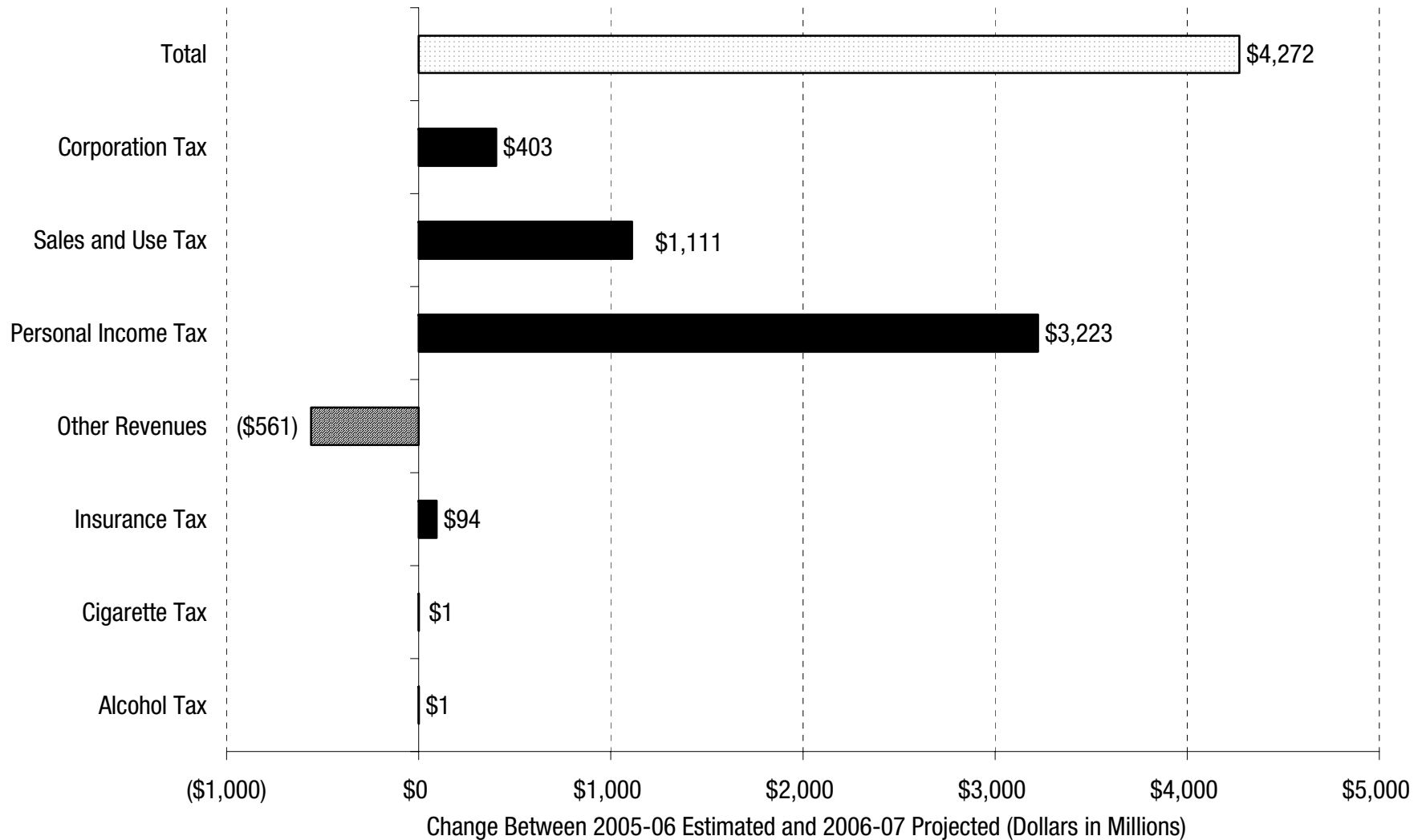
Source: Department of Finance

Personal Income Tax Provides Half of 2006-07 General Fund Revenues



Projected 2006-07 General Fund Revenues = \$91.5 Billion

General Fund Revenues Are Expected to Increase Modestly

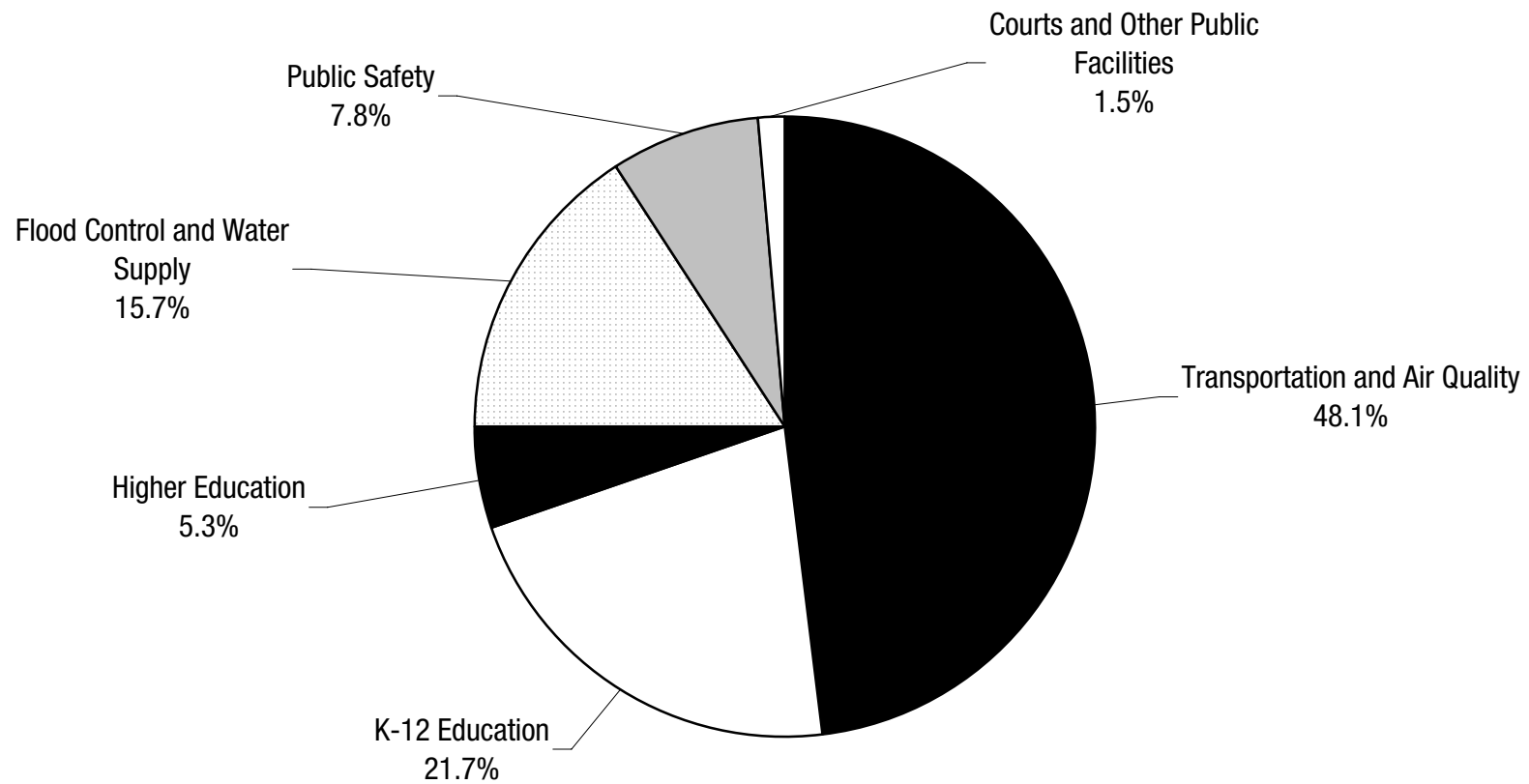


Source: Department of Finance

The Governor's Public Works Proposal

- The Governor announced a 10-year public works plan in his State of the State address. The Strategic Growth Plan (SGP) would cover \$222.6 billion in spending, including:
 - \$100.8 billion from existing funds, including \$1 billion from previously authorized bonds backed by the proceeds from tribal gaming and \$4.1 billion from previously authorized, but unissued, K – 12 and Higher Education general obligation (GO) bonds.
 - \$68 billion in new GO bonds.
 - \$53 billion in “new” funds. New funding sources would include revenues generated from fees, federal funds, and assumed savings.
 - \$800 million in lease-revenue bonds used to fund public safety, courts, and other public facilities.
- The Governor's proposal does not include housing, parks and open space, or health facilities.
- The Governor has asked the Legislature to approve the entire plan as a single package that would be placed before the voters in a series of elections between 2006 and 2014.
- The Governor would ask voters to approve a 6 percent cap on General Fund debt service costs.

Where Does the Money Go? Governor's Public Works Proposal

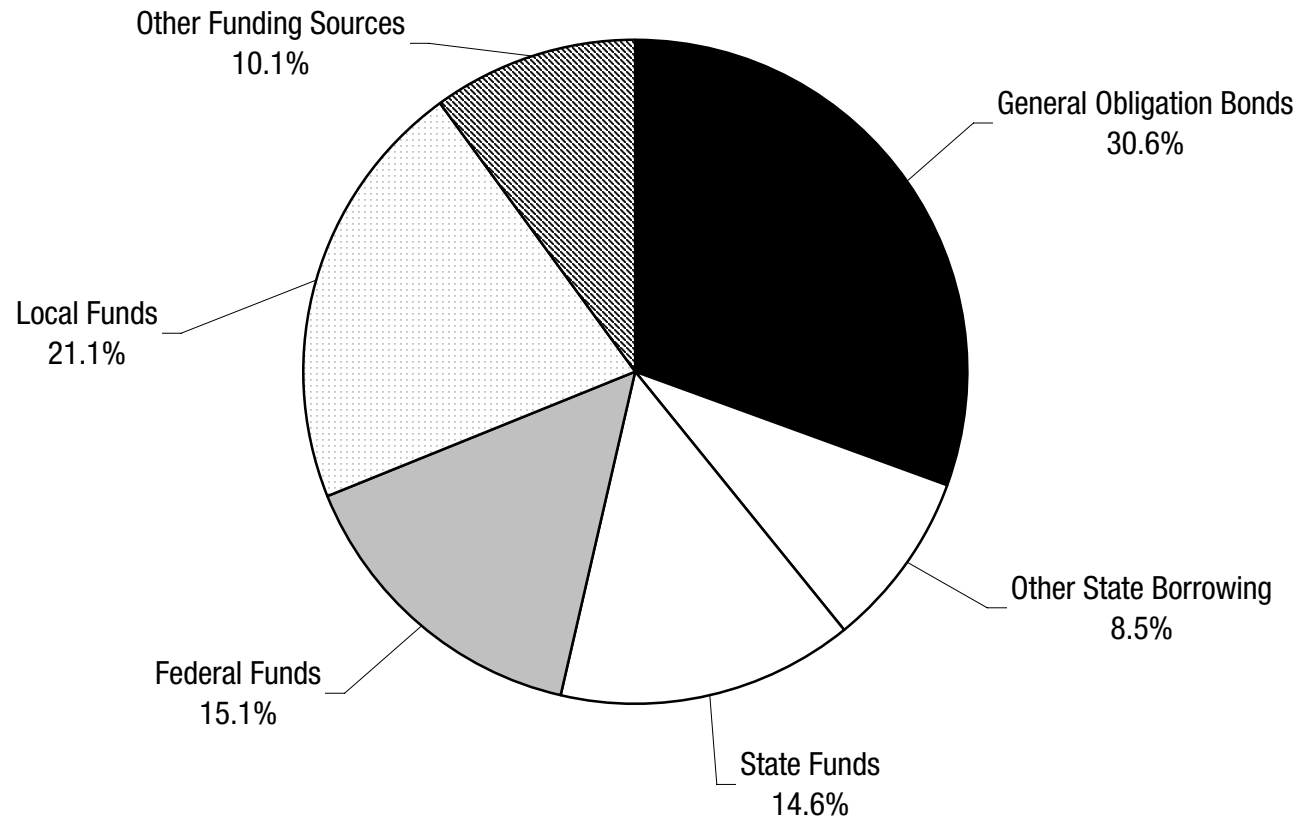


Total = \$222.6 Billion

Source: Department of Finance

Where Does the Money Come From?

Governor's Public Works Proposal



Note: Other Funding Sources includes public/private partnerships for high occupancy toll (HOT) lanes, toll lanes, port mitigation, and goods movement; CalTrans efficiencies savings; design-build and design sequencing savings; and revenues from a new water user fee.

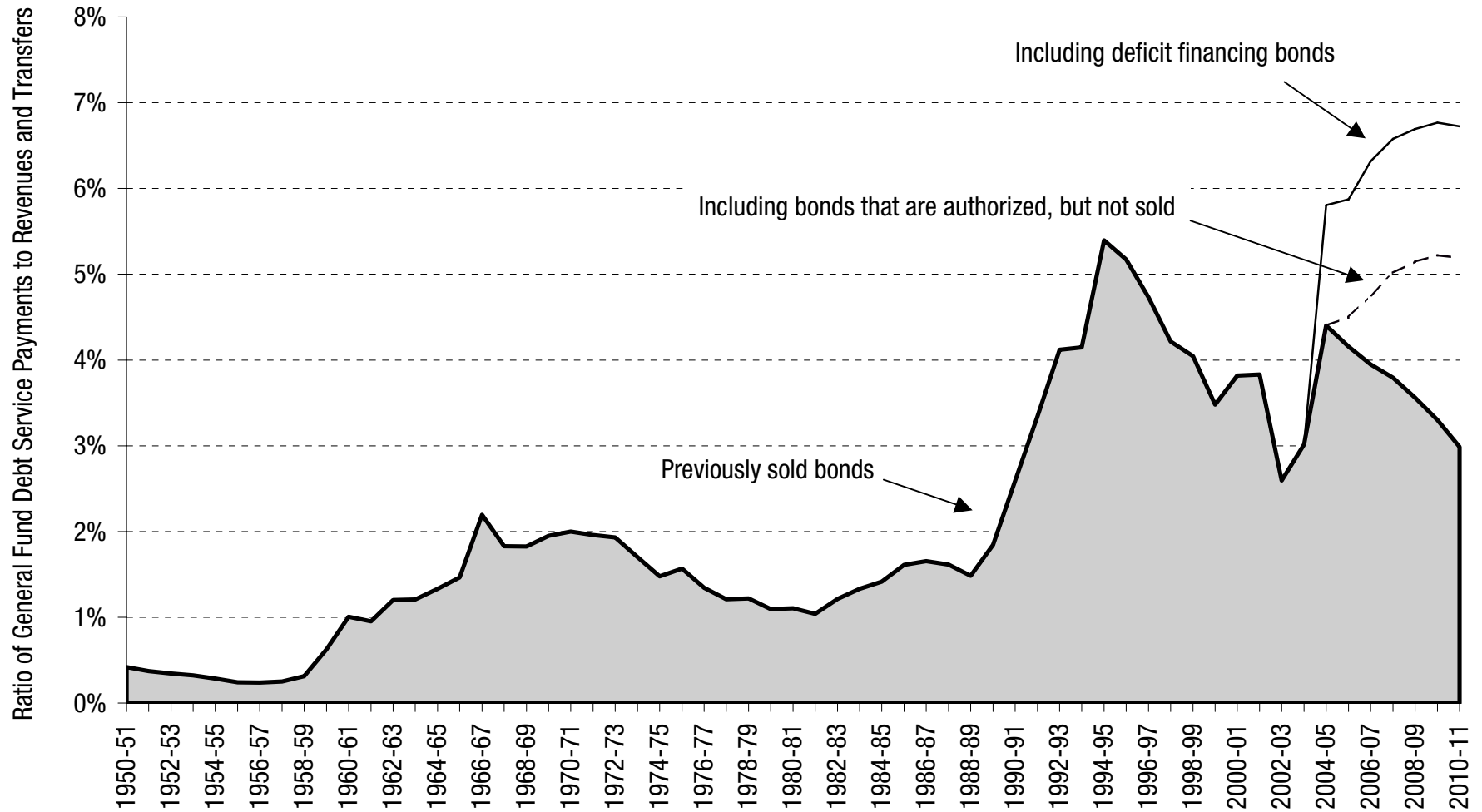
Source: Department of Finance

Critical Policy Issues Raised by the Governor's Public Works Proposal

- Can California afford a new program of this magnitude without additional revenues? Debt service on the Governor's proposed GO bonds would total approximately \$4.4 billion per year once all the proposed bonds are sold and leave the state with record debt service obligations.
- Is the Governor's proposal based on a comprehensive assessment of the state's infrastructure needs? This Administration has not published the statutorily required annual infrastructure plan since the Governor assumed office.
- Does the Governor's proposal adequately address the diversity of the state's needs? Should the proposal include funding for additional needs?
- What is the right balance between debt-financed investment and "pay-as-you-go financing"? The Governor's plan would borrow against future revenues earmarked for transportation, which means that fewer dollars will be available to meet future needs.
- Would the Governor's proposal limit the state's ability to issue future bonds in response to emergencies or emerging needs?

Deficit Financing Bonds Put California's Debt Service at Record Levels

Does Not Include Governor's Proposed \$68 Billion in Bonds



Source: Legislative Analyst's Office

K—12 Education

The Governor's Proposed Budget:

- Translates into K – 12 Proposition 98 per pupil spending of \$8,052 in 2006-07, up from \$7,428 in 2005-06. The change in per pupil spending levels between 2005-06 and 2006-07 is not strictly comparable due to the increase in funds for after-school programs included in 2006-07.
- Increases the Proposition 98 funding level for K – 14 Education by \$4.3 billion (\$4.1 billion in state funds). Of this increase, the Proposed Budget provides approximately \$1.7 billion above the minimum guaranteed level that will reduce the state's maintenance factor obligation. The Governor also includes an additional \$428 million for after-school programs required by Proposition 49 as part of the increase in Proposition 98 funds. The Proposed Budget would count this amount toward the state's maintenance factor obligation.
- Funds statutory average daily attendance (ADA) growth and a 5.18 percent cost-of-living adjustment for revenue limit apportionments, child care and development programs, class size reduction, special education, and other categorical programs.
- Provides \$100 million to school districts for a newly created School Enrichment Block Grant. The funds would support strategies to recruit and retain teachers and principals in high-priority schools. Strategies would include student loan forgiveness, signing bonuses, recognition pay, and professional development.

How Does California's K-12 Education Spending Compare?

	California Rank	California	US
K-12 Per Pupil Spending (2004-05)	35	\$8,051	\$9,102
K-12 Spending as a Percentage of Personal Income (2004-05)	39	3.80%	4.15%
Number of K-12 Pupils Per Teacher (2004-05)	48	19.3	14.7
K-12 Per Pupil Spending, Adjusted for Regional Cost Differences (2002-03)	43	\$6,765	\$8,041
Percentage of K-12 Pupils in Districts with Per Pupil Spending At or Above the US Level (2002-03)	44	6.1	44.7

Source: National Education Association, US Bureau of Economic Analysis, and Education Week

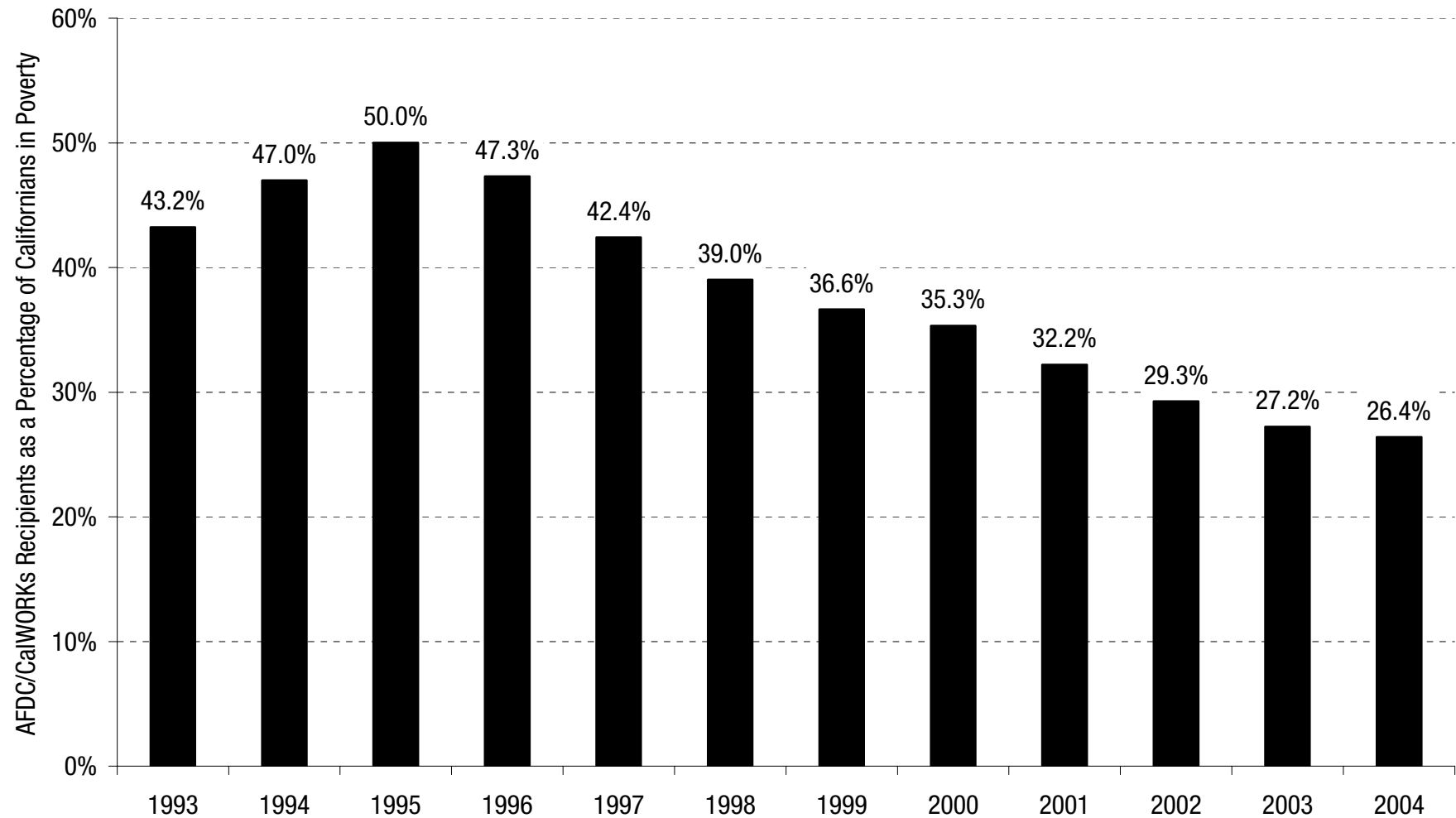
CalWORKs/TANF

■ The Governor's Proposed Budget:

- Continues to suspend the July 2005 and July 2006 cost-of-living adjustments (COLAs) for CalWORKs grants included in the 2005-06 budget agreement and withholds the October 2003 CalWORKs COLA. In 2004, a superior court ruled that the state must provide the COLA retroactively to October 1, 2003. However, the state appealed the ruling, withholding the payments until the appeal is resolved. The state's action will cost CalWORKs families \$460 million in additional grant payments.
- Cuts current-year child care funding for the CalWORKs Program by \$114.6 million. The Administration indicates that fewer CalWORKs recipients have moved into work than was anticipated, and that the funding is not needed. County representatives note that this funding is flexible and could be used to provide other services to help move CalWORKs families into the workforce.
- Diverts \$379.7 million in federal TANF funds in 2005-06 and 2006-07 to replace state funds in Child Welfare Services, Foster Care, and Developmental Services.

- CalWORKs grants have lost ground to California's rising housing costs. The maximum 2005-06 grant for a family of three in a high-cost county is less than two-thirds (62.9 percent) of the average Fair Market Rent for a two-bedroom apartment.

Californians in Poverty Are Less Likely to Receive Cash Assistance

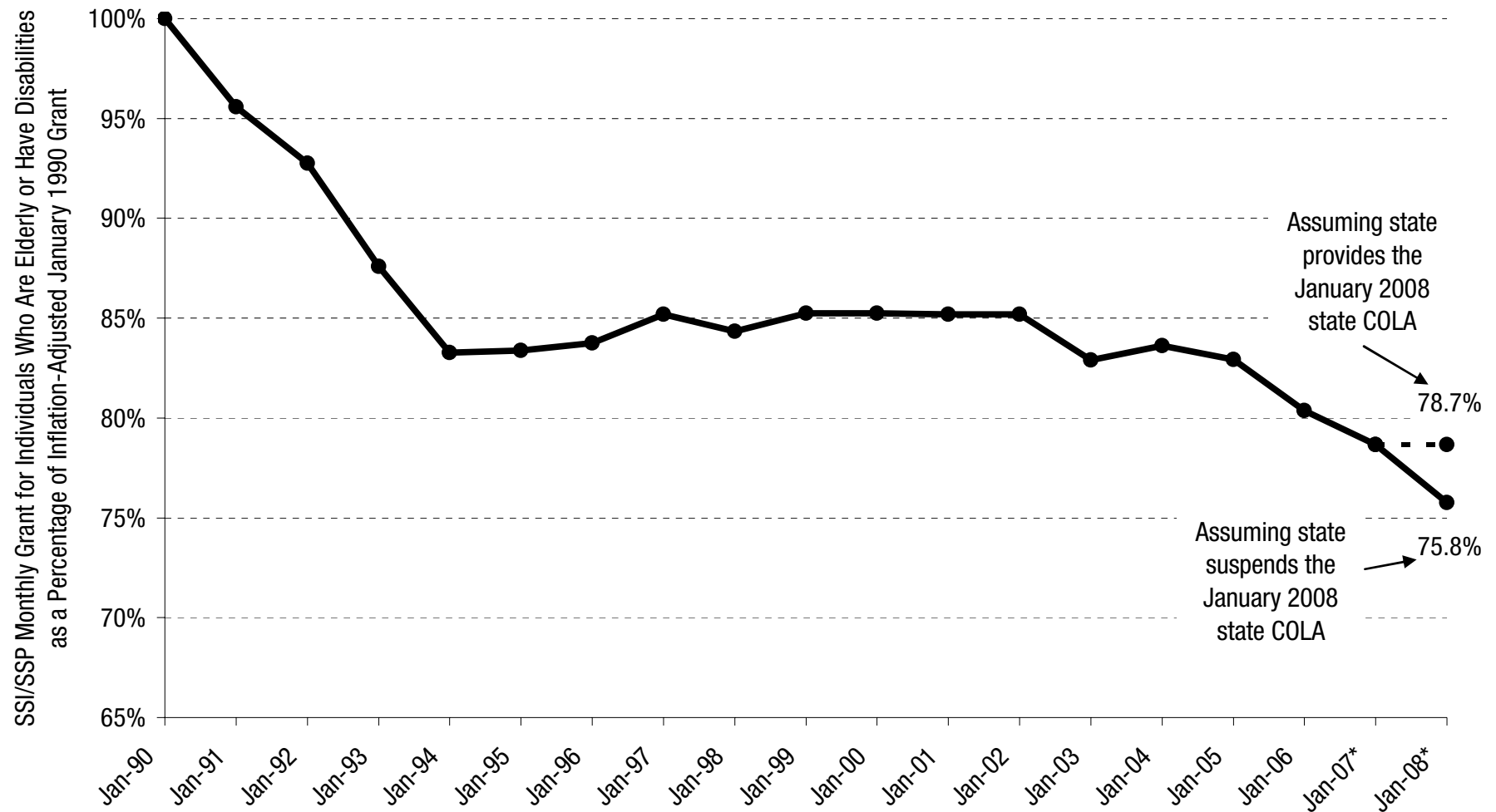


Source: US Census Bureau, Department of Social Services, and US Department of Health and Human Services

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

- The Governor's Proposed Budget:
 - Delays providing the federal January 2007 COLA to SSI/SSP recipients until July 2008 – more than one year longer than the three-month delay included in the 2005-06 budget agreement. The state would use those funds to reduce spending, for savings of \$48.1 million in 2006-07 and more than \$185 million in 2007-08. The SSI/SSP Program helps low-income seniors and people with disabilities meet basic living expenses.
 - Retains the suspension of the state January 2006 and January 2007 COLAs for SSI/SSP grants included in the 2005-06 budget agreement.
- Under the Governor's proposal, the monthly grant level for an individual would be \$836 in 2007 and would have 21.3 percent less purchasing power than in 1990.

Purchasing Power of SSI/SSP Grants Has Declined Since 1990 and Would Fall Further Under Governor's Proposal



* January 2007 proposed and January 2008 projected.
Source: Department of Social Services

Still Stretched Thin

- For the sixth consecutive year, the Governor's Proposed Budget does not fund operating cost increases for several county-run human services programs, including the Adoption Assistance, Adult Protective Services (APS), and Foster Care programs.
- These and other program reductions have compromised the quality and availability of local services by:
 - Making it more difficult to keep families together, undermining counties' ability to recruit foster and adoptive parents, and reducing supportive services for families and children.
 - Reducing investigations of elder abuse, limiting outreach efforts, and making it difficult for counties to meet required response time targets for the APS Program.
 - Eroding the comprehensive welfare-to-work approach embodied in the state's CalWORKs Program, which may result in fewer families leaving cash assistance for work.
 - Reducing food stamp outreach and simplification efforts, resulting in a loss of 100 percent federally-funded benefits that could assist California families.

Operating Cost Increases Lost by Counties in 2005-06 Due to Multiple Years of Frozen State Funding

Dollars in Millions

	General Fund	Total Funds
Adoptions Program	\$3.3	\$5.7
Adult Protective Services Program	\$13.7	\$17.8
Child Welfare Services Program	\$11.7	\$24.3
CalWORKs Program	\$267.8	\$267.8
Food Stamp Program	\$54.1	\$154.8
Foster Care Program	\$10.4	\$29.7
In-Home Supportive Services Program	\$22.3	\$68.3
TOTAL	\$383.3	\$568.4

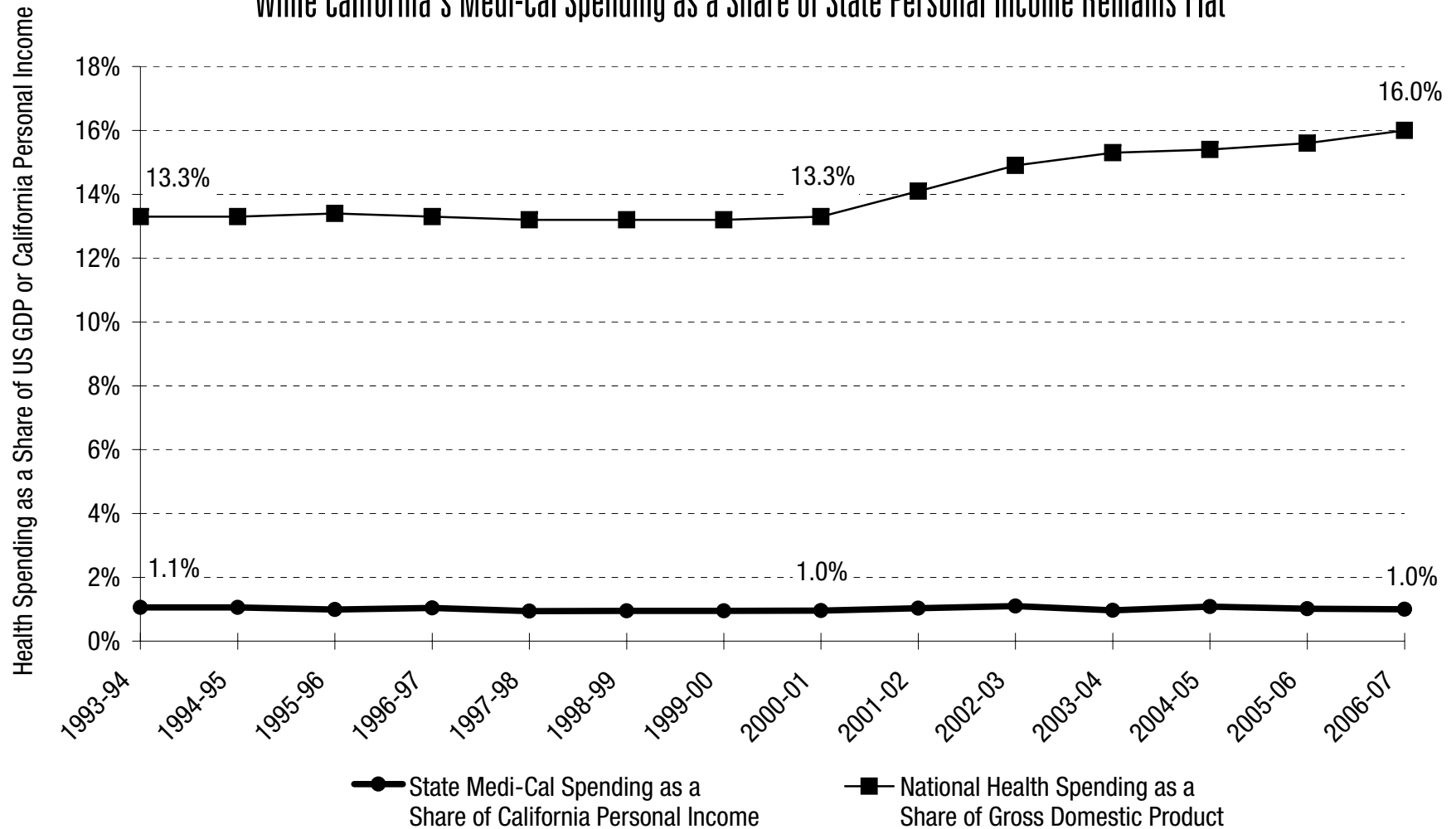
Source: County Welfare Directors Association of California

Health Care

The Governor's Proposed Budget:

- Includes \$72.2 million (\$34.2 million in state funds) to increase enrollment of eligible children in the Medi-Cal Program and the Healthy Families Program (HFP). Of this amount, \$45.5 million would cover the cost of anticipated enrollment increases attributable to streamlining the Medi-Cal application form. Remaining funds would support county outreach and enrollment efforts, a media campaign, and “incentive payments” for application assistants who successfully enroll increased numbers of children in Medi-Cal or the HFP. The Governor also allocates \$9.6 million (\$3.5 million in state funds) to streamline enrollment into the HFP, such as through increased use of an online application (Health-e-App). The Administration notes that over 400,000 children are eligible for, but not enrolled in, Medi-Cal or the HFP.
- Provides a 5.4 percent increase in Medi-Cal rates for long-term care providers.
- Reflects state savings of \$25.0 million in 2005-06 and \$42.6 million in 2006-07 from a previously approved 5 percent reduction in the rates paid to many Medi-Cal providers. This rate reduction was blocked by a court injunction, which was subsequently lifted by the 9th Circuit Court of Appeals in August 2005.
- Freezes funding for basic county operating expenses for the Medi-Cal Program, for savings of \$42.4 million (\$21.2 million in state funds).
- Does not include last year's proposal to require many enrollees who are seniors and people with disabilities to enroll in managed care plans.

National Health Care Spending as a Share of GDP Has Increased, While California's Medi-Cal Spending as a Share of State Personal Income Remains Flat

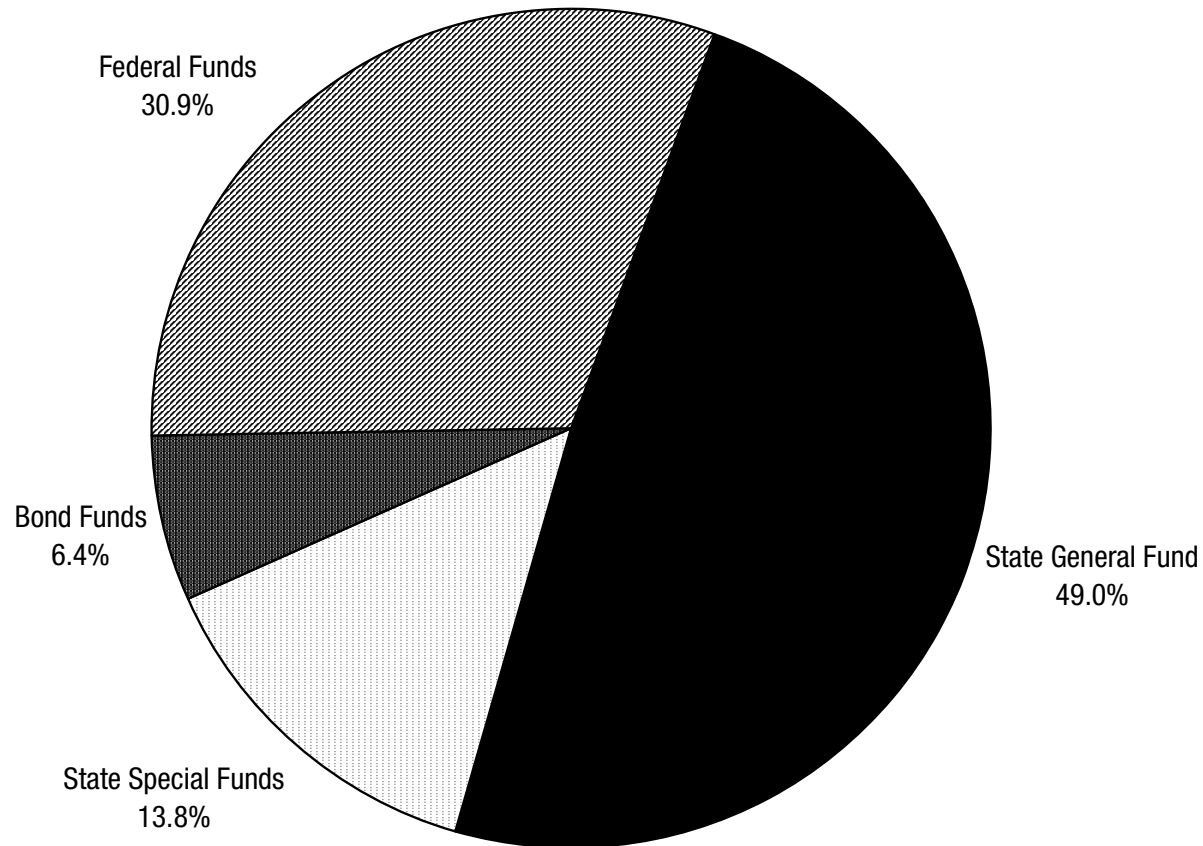


Source: Centers for Medicare & Medicaid Services, Department of Finance, and Department of Health Services

Recent Federal Budget Cuts Will Deepen the State's Budget Gap

- Congress recently approved a spending plan containing nearly \$40 billion in budget reductions over five years. The cuts target federal programs serving low-income and vulnerable families and children, including many programs where responsibility is shared with state and local governments. These cuts will cost the state over \$680 million per year once fully implemented and more than \$2.5 billion over five years.
- These reductions will:
 - Require increased state spending for the CalWORKs Program to meet stiffer TANF work requirements.
 - Limit states' ability to use provider taxes on managed health care plans as a match for federal Medicaid funds.
 - Prohibit states from using certain "incentive" funds as a match for federal child support funds.
 - Eliminate federal support for certain foster children living with relatives.
- House Republicans argue that cuts are necessary to reduce the federal deficit and pay for hurricane relief efforts. However, the savings from these reductions are lower than the nearly \$60 billion in new tax cuts passed by the Senate or over \$90 billion in new tax cuts passed by the House. Thus, the spending reductions will only partially offset the cost of proposed tax cuts.

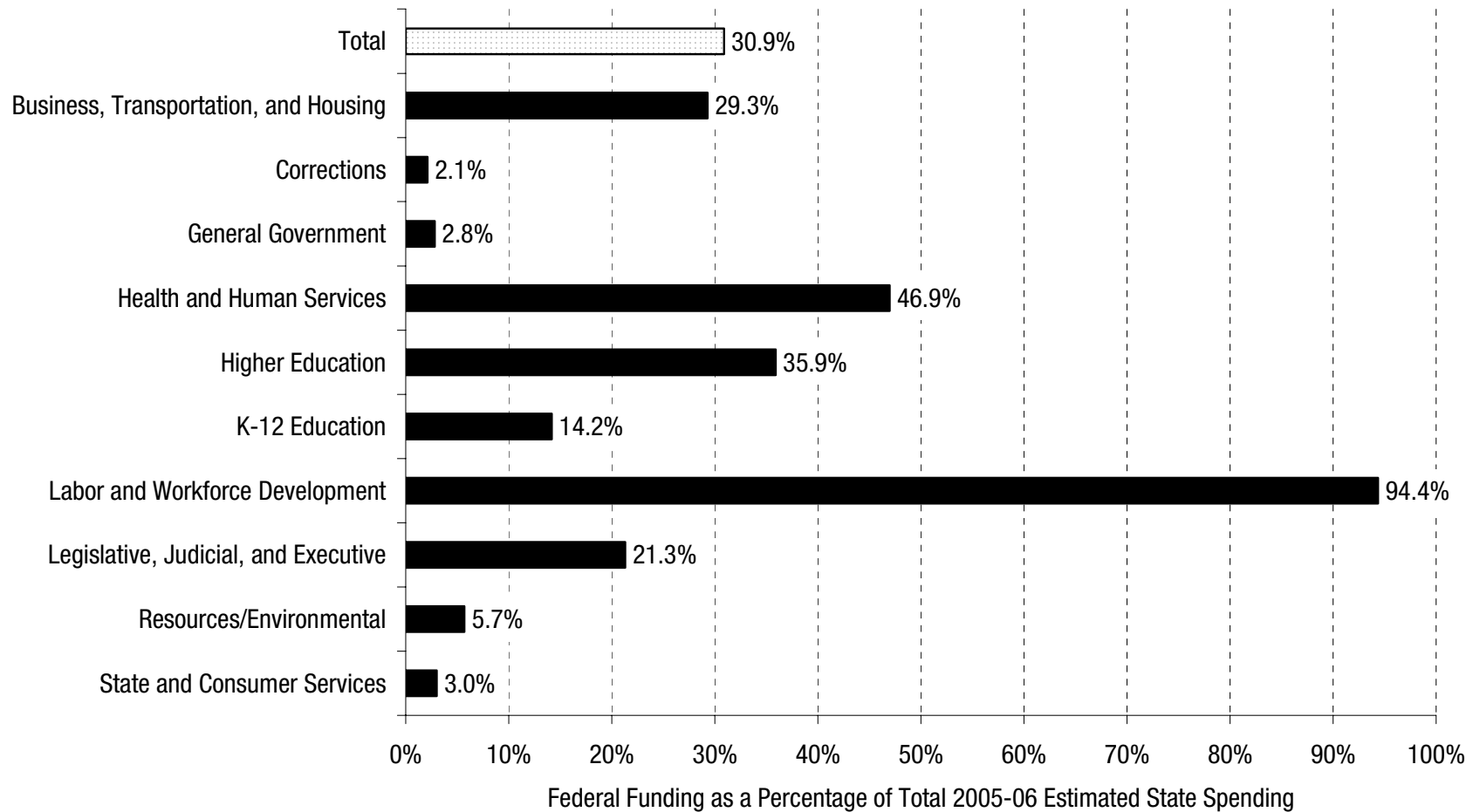
Federal Funds Account for Nearly One-Third of the Dollars Spent Through California's Budget



2005-06 Estimated Spending = \$184.4 Billion

Source: Department of Finance

Federal Funding as a Percentage of Total State Spending Varies by Agency



Source: Department of Finance

Estimated Impact of Recent Federal Cuts on California's State Budget

Program	Change	One-Year Cost at Full Implementation	Five-Year Cost (FFY 2006 - 2010)
TANF	Increase work requirements	Over \$400 million	Over \$2 billion
Medicaid	Eliminate California's current provider tax on Medi-Cal managed care organizations	\$166.5 million	\$166.5 million
Child Support	Prohibit states from using certain "incentive" funds as a match for federal child support funds	\$90 million	\$270 million
Child Support	Assess a \$25 per family fee	\$5 million	\$20 million
Foster Care	Eliminate federal support for certain children living with relatives	\$5 million	\$25 million
Foster Care	Limit federal administrative support for certain foster children	\$15 million	\$90 million
TOTAL		Over \$680 million	Over \$2.5 billion

Source: California Budget Project analysis, Center on Budget and Policy Priorities, Center for Law and Social Policy, and Legislative Analyst's Office

In Closing

- California needs additional revenues to implement the Governor's spending plan and balance the budget.
- The Governor's Proposed Budget begins to address the state's unmet needs for investment in public facilities, but fails to address the challenges raised by demographic and economic changes.
- Federal tax and budget policies will exacerbate California's long-term budget problems and weaken programs that are critical to the well-being of vulnerable families and children.