



BUDGET ACTION BULLETIN

CALIFORNIA STATE ASSOCIATION OF COUNTIES

2010-11 State Budget Week of October 4, 2010

October 6, 2010

TO: CSAC Board of Directors
County Administrative Officers
CSAC Corporate Associates

FROM: Paul McIntosh, CSAC Executive Director
Jim Wiltshire, CSAC Deputy Executive Director
Jean Kinney Hurst, Legislative Representative

RE: **Budget Action Bulletin #6**

Today, the Budget Conference Committee released an outline of the budget agreement recently reached between the four legislative leaders and the Governor and held an informational hearing to discuss the package. Hopefully, this conversation begins the public process that will lead to the eventual passage of the state budget tomorrow when the Legislature convenes.

The Conference Committee discussion was very summary in nature. The Committee used the Democrats' California Jobs Budget as a basis for the discussion; Senator Ducheny indicated that anything that was NOT expressly mentioned as OUT of the package remained. The Assembly and Senate are scheduled to convene tomorrow morning, Thursday, October 7 at 9:00 a.m. to take votes on the budget agreement.

This Budget Action Bulletin outlines what CSAC staff knows at the time of publication about the components of the package. Because budget specifics and trailer bill language have been closely guarded, we do not yet have the full details of all of the components of the package. However, we do plan to prepare a written report on the full budget when trailer bill language becomes available and the Governor takes action on the budget package. If you have specific questions about aspects of the budget, we encourage you to contact CSAC staff directly.

STATEWIDE ISSUES

The 2010-11 budget package includes a combination of expenditure reductions, federal assistance, additional revenues, and fund shifts, as outlined below:

	(dollars in billions)
Budget Deficit	-17.9
Expenditure Reductions	7.5
Federal Funds	5.3
Additional Revenues	2.5
Fund Shifts, Other Revenues	2.8
Alternative Funding	0.5
Baseline Workload Adjustments	-0.2
Total Solutions	\$18.3
Final Reserve	\$0.3

The Governor had previously proposed a budget reserve of \$1.2 billion in his May Revision. Recall that, last year, the Governor used his line-item veto to bolster the reserve. It is unclear at this point how vulnerable programmatic funding is to the line-item veto under this agreement.

Notably, the 2010-11 budget package suspends the Proposition 98 guarantee for K-14 schools, but includes Proposition 98 funding at \$49.7 billion, in addition to a new deferral of \$1.9 billion and additional federal funds for total state funding on K-14 schools at \$52.5 billion.

The University of California and California State University systems receive an augmentation for past reductions for total higher education funding of \$5.5 billion.

TAX PACKAGE

As widely touted by the leaders who negotiated the deal, the budget agreement does not increase any tax rates. (Which is not quite the same as not raising taxes, though perhaps that's a distinction without a difference.) There are several important changes to taxes in this budget agreement.

The budget "framework" anticipates \$2.5 billion in additional revenues, \$1.4 billion of which is from the Legislative Analyst's revenue projections that are much more recent than the May projections used to previously define the deficit's size. The brief outline the Budget Conference Committee released today notes that the first three months of the fiscal year have already delivered this extra revenue.

The budget agreement suspends corporate Net Operating Loss tax benefit for two more years; over 90 percent of corporations are exempted from the suspension based on income thresholds or other criteria. This provision results in about \$1.2 billion in General Fund revenue for the budget year.

Leaders agreed to ease up on corporations that underpay their tax liability by more than \$1 million, penalties for which were recently toughened. This change, combined with restoring old "cost of performance" rules for certain multi-state tax apportionment, reduces state tax revenues by about \$132 million.

The budget *does not delay* the Elective Single Sales Factor corporate tax cut. It *does not include* an oil severance tax, or the related state sales tax reduction. It also *does not include* the effort to collect sales and use taxes from out-of-state retailers (sometimes called the “Amazon” provision).

BUDGET REFORM

The Big 5 have decided, as part of the budget agreement, to ask voters to approve a strengthened rainy day fund. The proposed changes would implement a stronger reserve than the one currently in place, but one weaker than version voters defeated in the ill-fated special election of May 2009.

The strengthened reserve seems to fulfill Governor Schwarzenegger’s demand for budget reform, and differs from the current rainy day fund in three ways.

First, the new reserve would be larger, topping out at 10 percent of General Fund revenue. To reach that goal, the state would have to deposit three percent of each year’s revenue into the reserve unless they use funds from the reserve to close a deficit (see the next paragraph). Half of that three percent could instead pay for debt service and infrastructure. Currently, the requirement that they deposit three percent in the reserve fund is so loose as to be next to meaningless.

Second, use of the reserve fund would be restricted. The state could only use funds from the reserve to spend up to the previous year’s spending plus inflation and population growth. They would not be allowed to use all the money at once, but up to 50 percent of the money in the one year, half of what remained the next, and the rest in a third year if necessary. Once the reserve reaches its cap of 10 percent, the required annual payments cease and any excess funding may pay for specific one-time purposes.

Note that, due to the above formula, once revenues have begun to recover from the lowest point of a significant drop (such as the ones over the last couple of years), or if new taxes are enacted, use of the reserve would be severely restricted, so the funds would enforce significant discipline during extraordinary shortfalls while also cushioning the blows. But during small, temporary dips in revenue, the formula would allow spending to remain essentially unchanged.

Third, in addition to the required three percent annual payments, the state would have to deposit any General Fund revenue that it collects above a calculation “based on” the previous 20 years of revenue into the reserve. New revenue needed to meet Proposition 98 (K-14) obligations is excluded from this calculation. Documentation released so far does not give much detail on this Prop. 98 aspect, so it is unclear exactly how it would work.

ADMINISTRATION OF JUSTICE

Corrections. The 2010-11 budget *does not include* a shift of state prison inmates to county responsibility. It does, however, attribute a reduction of approximately \$250 million to the

California Department of Corrections and Rehabilitation (CDCR). It also assumes savings of just over \$800 million to the federal prison healthcare receiver, some of which will be achieved by the implementation of [SB 1399](#) (Leno), the medical parole measure.

Transfer of Juvenile Parole Responsibility. The budget shifts responsibility for community supervision of 707(b) offenders upon their release from a Division of Juvenile Justice (DJJ) facility from the state to county probation. Under this plan, county probation departments would be responsible for the entire continuum of community supervision for youthful offenders. We understand that the design of the juvenile parole supervision transfer is expected to follow the SB 81 model, with the local court assuming jurisdiction. Funding to support the transfer of supervision responsibility will be redirected from state savings.

Funding for Local Youthful Offender Rehabilitative Facilities. It is our understanding that the budget sustains a commitment of funding (in the \$200 to \$300 million range) in additional lease revenue bonding authority for the construction or renovation of local juvenile rehabilitative facilities.

Local Public Safety Funding. The budget *does not extend* the Vehicle License Fee (VLF) increase dedicated to local public safety programs; the current VLF rate of 1.15 percent – 0.15 percent of which is dedicated to the Local Safety and Protection Account (LSPA) – is set to revert to 0.65 percent on June 30, 2011. Counties recall that revenue in the LSPA is statutorily dedicated to a range of local programs, including the Citizens’ Option for Public Safety (COPS), the Juvenile Justice Crime Prevention Act (JJCPA), the rural and small county sheriffs’ local assistance programs, booking fee “replacement” revenue, and a range of other local assistance programs. It will be critical for the Legislature to take action on the VLF extension early in 2011, both to provide continuity for programs and – for one very significant practical reason – to avoid a situation in which the DMV (if it appears that the extension is at risk of lapsing) is forced to reprogram its systems to reflect a return to the 0.65 percent rate. CSAC is [on record](#) supporting the VLF extension, which we regard as an absolutely critical funding source for both front-line enforcement and prevention activities at the local level.

Judicial Branch Issues. Perhaps most difficult to discern at this point is the substance of the judiciary trailer bill. Below we report what we anticipate will be included in the bill; we will not, of course, be able to confirm the specific details until we have had a chance to review and fully analyze the language.

As counties will recall, CSAC has been engaged over the last many months with the Judicial Council as well as court- and county-operated collections programs in an initiative to improve recovery of court-ordered debt. The provisions of a multi-element collections process improvement package are expected to be incorporated into the judiciary trailer bill. Other related items of interest – corrections to counties’ ongoing authority to collect a surcharge and a provision to establish a parking penalty audit “safe harbor” provision (both jointly pursued by CSAC and the Judicial Council) as well as a provision relating to installment payments – are outlined below. Finally, a package of revenue enhancements to support the judicial branch is also expected to be included in the judiciary trailer bill. These provisions were negotiated among

judiciary officials, Capitol budget and policy staff, and various court stakeholders. Several of these items are very technical, so we have attempted to provide the necessary background.

- **Collection of Court-Ordered Debt: Strategies to Improve Collection and Discharge Debt.**
SB 1407 – the 2008 measure authored by Senate President pro Tempore Don Perata that authorized increases for a range of fees, penalties, and assessments to support the state’s courthouse capital plan – codified a joint commitment between the Administrative Office of the Courts (AOC) and CSAC regarding improvements to court-ordered debt collection programs. The expression of this commitment in Penal Code Section 1463.010 reflects the courts’ and counties’ shared objective of strengthening and improving, where appropriate, existing collaborative collection efforts across the state.

In response to this legislative directive, the AOC and CSAC convened meetings beginning last fall with a group of collection professionals – representing programs administered through both the counties and the court – to brainstorm ideas of mutual interest and benefit that would help achieve the objectives set forth in Penal Code Section 1463.010. The group reviewed dozens of potential options for process improvement and provided valuable input and insights; those discussions produced a set of five elements that the AOC and CSAC are moving forward through the budget process to enhance court and county collection efforts. The elements are as follows:

- Strengthen existing authority and responsibility for a comprehensive collection program of delinquent court-order debt.
- Develop and implement an amnesty program for infractions.
- Clarify authority related to discharge of accountability.
- Authorize intercept on unclaimed cash property in cooperation with State Controller’s Office.
- Clarify authority for enforcing court-ordered debt beyond the 10-year period applicable to civil judgments.

Language to carry out this multi-part initiative was drafted and negotiated by the joint court and county collections working group and has been further vetted by other key county stakeholders.

- **Corrections to Government Code Section 76000 (e).** SB 1732, the Trial Court Facilities Act of 2002 (Escutia – Chapter 1082, Statutes of 2002), modified Government Code (GC) Section 76000, which governs the amount of surcharge that may be added to fines, penalties, and forfeitures imposed and collected by a court for criminal offenses, including non-parking offenses involving violations of the Vehicle Code or any local ordinances adopted pursuant to the Vehicle Code. The authorized use of the surcharge revenue is limited to support special funds, including Courthouse Construction Funds (CCF), Criminal Justice Facility Construction Funds (CJFCF), and Maddy Emergency Medical Service funds. It will be recalled that counties were authorized, and sometimes directed, to create and maintain these funds well before enactment of SB 1732.

SB 1732 added subdivision (e) to GC Section 76000, to address the amount of surcharge that could be collected for a “local courthouse construction fund established by Section 76100 as of January 1, 1998 when the money in the fund is transferred to the state under Section 70402” (i.e. after a county transfers all of its trial court facilities to the state). The limitation contained in subdivision (e) was not intended to affect or limit the amount of surcharge that can be collected to support other local funds such as Criminal Justice Facility Funds or any purpose other than local CCF.

CSAC undertook an extensive research and survey process this spring to identify any errors and make needed corrections to Section 76000(e). Based on counties’ responses, dollar amounts for approximately a dozen counties will be updated in the chart to correctly reflect those counties’ individual authorities.

- **Parking Penalty Audit Provision.** Prior to 2008, GC Section 70372(b) required an additional penalty of \$1.50 on parking offenses for state courthouse construction. At the same that time, Section 70375 allowed the penalty required in 70372 to be reduced by the amount collected for the local courthouse construction fund, authorized pursuant to Section 76100 (an “offset” provision). In 2007, the public safety omnibus bill (SB 425, Margett), amended Section 70375(b) to provide clarification on an unrelated matter. In so doing, the legislation inadvertently eliminated the so-called “offset” provision. The change to 70375 in SB 425, which became effective January 1, 2008, made mandatory the collection and remittance of a \$1.50 parking penalty, regardless of amounts collected for deposit into the local courthouse construction fund pursuant to GC Section 76100.

Counties were informed of the change and were instructed to (1) ensure they are complying with the requirements of Section 70372(b) and (2) account for the elimination of the offset previously authorized under Section 70375. It is apparent from state remittance information that most entities overlooked the change codified in SB 425; records indicate that three counties remitted the \$1.50 appropriately in 2009, pursuant to the change to Section 70375.

In recognition of the fact that the impact of these statutory changes was overlooked, CSAC – in collaboration with the Judicial Council – proposed that, for audit purposes, counties not be penalized for the failure to remit the \$1.50 in parking penalty revenue, once the “offset” provision was eliminated if the funds were instead directed to a local courthouse construction fund and expended on allowable purposes as identified by statute. The proposed provision would apply only to the first year following enactment of SB 425 – that is, for the calendar year 2008.

- **Increased Flexibility for Initial Payment for Installment Plans.** The Judicial Council also is modifying current law to help address an issue that has emerged in collections programs. Under current law, Vehicle Code Sections 40510.5 and 42007 allow the court to create an installment plan for violators convicted of an infraction violation. For each installment plan, violators must pay a \$35 administrative fee to cover the cost of establishing the plan and 25 percent of the total bail amount. Individuals can seek relief from the 25 percent requirement by going before a judicial officer and requesting that the court accept a lower amount. It is being reported by the court that – likely due to the economic conditions and

given increased total bail amounts on Vehicle Code infractions — the volume of individuals seeking relief from the required 25 percent bail installment is increasing. It has become a significant workload problem, especially at a time when the courts are facing increased pressures given the statewide court closures.

To address the increasing numbers of hearings, the Judicial Council is seeking statutory modification to allow each court to accept an amount less than 25 percent, in accordance with local rules established by the court. The proposal does not provide any new authority to the court, but merely modifies the court's existing authority in a manner that should decrease the number of hearings needed.

- **Court Funding Package.** It should also be recalled that Senate and Assembly budget subcommittees previously approved a package of fund transfers, fee increases, and other surcharges to fund court operations in 2010-11 and to avoid court closures. Among the notable items:
 - a proposed \$10 court security fee increase;
 - a new \$3 parking fee surcharge;
 - a transfer of funds from the State Courthouse Construction Fund, which is not expected to affect projects in the pipeline; and
 - a \$40 administrative fee tied to individual automated traffic enforcement citations (red light camera violations), which could be shared among the red light equipment vendors, cities, and counties.

AGRICULTURE AND NATURAL RESOURCES

Emergency Response Initiative. The budget package *does not include* the Governor's proposed fee on property insurance to fund CalFIRE.

GOVERNMENT FINANCE AND OPERATIONS

Mandate Securitization. Given the statements during the Budget Conference Committee hearing, we assume that the budget package continues to include authorization for local governments (cities, counties, and special districts) to securitize future state payments for mandate reimbursements. Counties will recall that Proposition 1A requires that payments for mandate reimbursements owed prior to 2004 be repaid over a period of years; statute sets that time frame at 15 years, starting with the 2006-07 and ending in 2020-21. These amounts total about \$1 billion, with counties owed the bulk (about 80 percent) of funds.

Using the VLF Gap Loan and Proposition 1A Securitization as a model, a joint powers authority would be authorized to pool local agency reimbursements and sell a bond with proceeds going to local agencies. When we are able to fully review the trailer bill language, we will report to counties on the particulars.

State Employees. The budget package assumes a reduction in spending for state employees of about \$1.5 billion. This amount assumes savings from collective bargaining agreements that are currently in negotiation and six agreements that have been ratified.

The budget package also includes pension changes for new state employees. Retirement benefits would be returned to the pension benefit levels that existed prior to the adoption of SB 400 (Chapter 555, Statutes of 1999), the three-year final compensation method of calculating benefit levels for new state employees would be required, and additional analysis and oversight of CalPERS' actuarial assumptions would occur.

HEALTH AND HUMAN SERVICES

While we know the outline of the health and human services aspects of the proposed budget agreement – it rejects some of the more controversial of the Governor's May Revision proposals and hews closely to the Conference Committee's August version of the budget – details will become available once the budget trailer language is released, presumably on Thursday.

For example, the budget does not eliminate CalWORKs, community mental health programs, and Adult Day Health Care. This proposed budget also contains restorations of funding for a few programs that were the subject of gubernatorial vetoes from last year, including \$80 million for Child Welfare Services and additional funds for the Office of AIDS.

For a complete list of budget proposals in 2010 through the Conference Committee's August actions, please [click here](#).

IHSS. The proposed budget does not include the significant cuts to the program called for by the Governor in May. It does outline a \$300 million reduction in General Fund spending to IHSS, but cuts to the program comprise only a small portion of that figure. The majority of the savings are achieved by the imposition of a new IHSS provider fee, which is estimated to bring in more than \$200 million in additional federal funding to the program.

The October budget proposal reduces the unallocated reduction in hours for IHSS to 3.6 percent and assumes additional caseload savings based on actual caseload numbers from 2009-10. The combination of these changes and the provider fee are estimated to bring in \$50 million more than what was assumed in the prior Conference Committee version of the budget.

Section 1115 Medicaid Hospital Financing Waiver. When the Legislature votes tomorrow to adopt the budget package, it will also vote on a bill – expected to be SB 208 (Steinberg) – to implement California's next five-year Medicaid Section 1115 Waiver. The bill is expected to provide the outline in state statute for implementing California's next Medicaid waiver, which is still the subject of ongoing negotiations between the state and the federal Centers for Medicare and Medicaid Services. The measure will include language related to the mandatory enrollment of seniors and persons with disabilities into Medi-Cal managed care and the county Coverage Initiatives.

Despite the inclusion of waiver-related language in tomorrow's budget debate, a number of waiver-related details remain in discussion between the state and federal government, including

the calculation of budget neutrality and the minimum service and coverage requirements for the county Coverage Initiatives. CSAC will provide additional detail on the waiver language when the final language becomes available in the coming days.

Mental Health. The document associated with the proposed budget makes reference to “a new proposal to contain costs at state mental hospitals,” but does not offer an explanation or details about such a proposal. CSAC will continue to seek additional information about this proposal.

Child Care. The budget proposal includes a \$48 million reduction in child care, which is achieved through a change in license-exempt rates and a reduction in administrative funds. The Department of Finance further explained before the Conference Committee this afternoon that the savings come from (1) a reduction in the reimbursement rate limits for licensed-exempt providers from 90 percent of the ceilings for licensed family child care homes to 80 percent, and (2) a reduction from 19.5 to 17 percent for administration. Please also note that this proposal differs from the August 27 Conference Committee version of the budget.

Public Health. The document associated with the proposed budget alludes to a “reduction of discretionary General Fund expenditures related to immunizations...” At the time of this writing, it is not clear what this means for local public health immunization programs, which currently receive about \$18 million in General Fund support. CSAC is working with county affiliates to obtain more information, but we do want to note that California is currently experiencing the biggest outbreak of pertussis – also known as whooping cough – in 50 years.

HOUSING, LAND USE AND TRANSPORTATION

Transportation Funding. CSAC understands that the 2010-11 budget package will include two critical clean-up provisions related to transportation funding, although actual language is not yet in print. First, per CSAC’s request, the budget should include a one-year “use-it-or-lose-it” extension for each Proposition 1B Local Streets and Roads appropriation made during the same fiscal year in which transportation deferrals were enacted. Second, legislative staff has drafted language to clarify that the Proposition 42 requirements related to eligible uses, “use-it-or-lose-it” requirements, etc. do not apply to the new Highway Users Tax Account (HUTA) enacted under the transportation tax swap. This is necessary due to an opinion by the State Controller that Proposition 42 provisions apply to the new HUTA. No further changes have been proposed to transportation funding in the 2010-11 state budget.

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