



COMMITTEE ON BUDGET & FISCAL REVIEW
Room 5019, State Capitol
Sacramento, CA 95814

SENATOR WESLEY CHESBRO, CHAIR

Quick Summary

The Governor's Budget Proposal

January 10, 2005

Earlier today, the Governor proposed his 2005-06 budget. Spending from all funds (General Fund, special fund and bond funds) total \$111.7 billion. General Fund spending is proposed to be \$85.7 billion, an amount that is approximately \$3.4 billion, or 4.2 percent, more than current-year spending. However, the assumptions used to estimate budget-year workload expenditures need further review.

Staff of the Senate Budget and Fiscal Review Committee prepared the attached briefing, which includes a summary of the Governor's budget proposal.

Staff is preparing a more detailed review of the budget, to be released in early February. If you have questions, please contact the committee at (916) 445-5202.

Status of Current Year (2004-05) Budget

In July of 2004, the Legislature enacted SB 1113 (Chapter 208, Statutes of 2004) – the Budget Act of 2004. The 2004 adopted Budget addressed a roughly \$16 billion General Fund (GF) budget shortfall. As enacted, the Budget included a General Fund reserve of approximately \$768 million.

The Budget Act, and its implementing legislation, contained a number of budget-balancing solutions, including:

- The use of Economic Recovery Bonds (approved by the state electorate as Proposition 57 in March 2004);
- A two-year diversion of local property taxes;
- Suspension of Proposition 98;
- Some targeted revenue increases and tax loophole closures;
- Other loans and borrowing – primarily from the proceeds of pension obligation bonds financed by a temporary reduction in payments to PERS;
- Program savings – including three-month delays in cost-of-living adjustments for California Work Opportunity and Responsibility to Kids (CalWORKs) and Supplemental Security Income / State Supplementary Payment (SSI/SSP) grants, reductions in support for the University of California and California State University; and
- Reductions in state operations spending.

Since the budget's enactment, there have been new developments affecting the revenues and expenditures expected for this fiscal year. According to the Department of Finance (DOF), revised estimates of total GF resources available (revenues and transfers) will be approximately \$83.7 billion. In addition, the DOF also estimates that revised current-year expenditures are approximately \$82.3 billion.

Finally, on January 5, the Governor called for a special session of the Legislature to consider and act on four constitutional amendments, to be presented to the voters in early summer 2005, on the following subjects:

- Changes to the State's budget process by requiring mid-year across-the-board cuts in virtually every state funded program area, including education, if state expenditures exceed revenues.
- Changes to the pension systems for future government employees.
- Changes to the education system by tying teachers' salaries to performance.
- Changes to the process of drawing California's legislative, congressional and Board of Equalization districts.

Governor's Proposed 2005-06 Budget

Definition of the Problem. The Governor's proposed budget identifies that the state has an accumulative \$9.1 billion difference between revenues (all available resources) and expenditures for the two-year period ending on June 30, 2006.

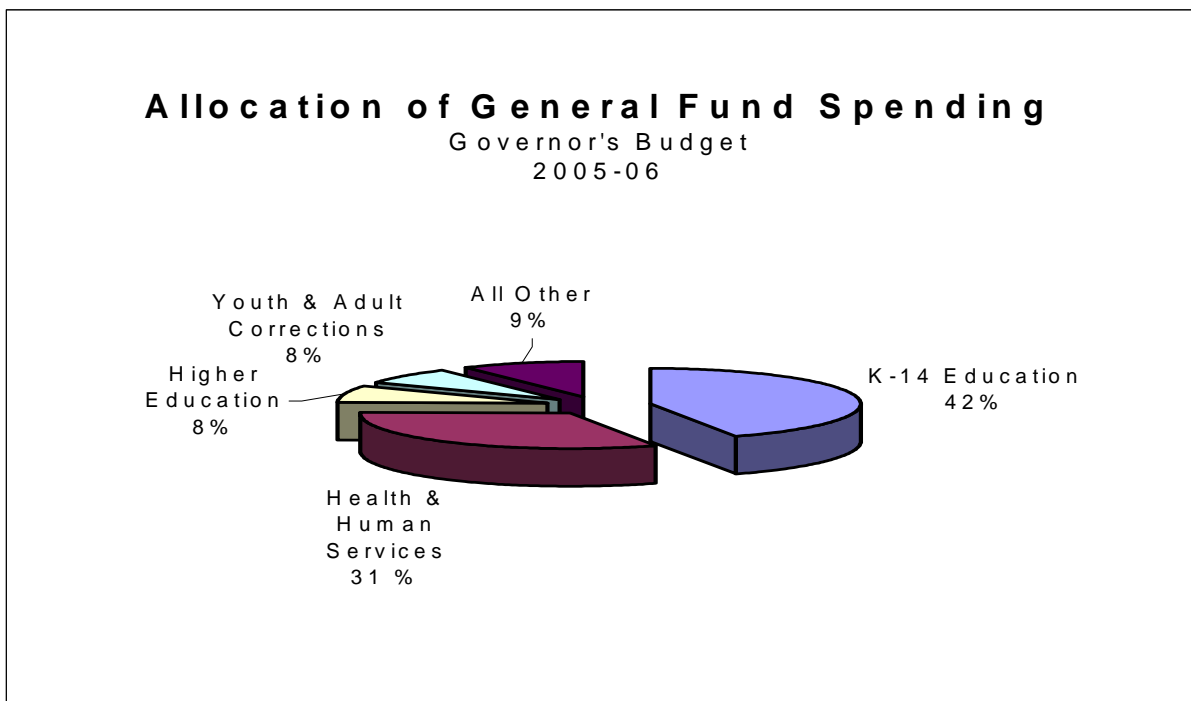
How Does the Governor Close the Deficit? In eliminating the deficit, the Governor relies on the following primary strategies:

- Utilization of approximately half of the remaining Economic Recovery Bonds - \$1.7 billion.
- Suspension of Proposition 42 - \$1.3 billion.
- Reduce funding for Proposition 98 by approximately \$2.3 billion.
- Reductions in health and human services of approximately \$1.2 billion.
- Reductions in education (non-Proposition 98) of \$453 million.
- Reductions in General government of \$928 million.
- Reductions in Resources of \$475 million.
- Reductions in Youth and Adult Correctional Agency \$292 million.
- Across-the-board reductions in departments \$150 million.
- Revenue adjustments of \$409 million.

Overview of the Governor's Budget Proposal

General Fund Spending Concentrated in Four Areas. Four policy areas account for approximately 90 percent of General Fund spending contained in the Governor's Budget. The chart shown below identifies the relative spending in these areas. Specifically, in the 2005-06 budget:

- K-14 Education (which includes funding for community colleges) receives \$36.5 billion, accounting for 42 percent of the General Fund spending,
- Health and Human Services receives \$26.7 billion, accounting for 31 percent of the total,
- Higher Education (UC, CSU and Student Aid Commission) receives \$6.7 billion, account for 7.8 percent of the total, and
- Youth and Adult Corrections receives \$7 billion, accounting for 8.2 percent of the total.



State Spending – Revised Current Year and Budget Year Comparison. The Governor’s budget proposes to increase General Fund expenditures in the budget year from \$82.3 billion to \$85.7 billion, which represents a 4.2 percent increase. The Department of Finance (DOF) estimates that revenues and transfers will increase from a revised \$80.2 billion to about \$85.5 billion (a 6.5 percent increase). The following table shows a comparison of the current- and budget-year spending.

Comparison of General Fund Spending
2004-05 and 2005-06
(Dollars in Millions)

	<u>2004-05</u>	<u>2005-06</u>	<u>Change</u>
K-14 Education (Proposition 98)	\$34,124	\$36,532	7.1%
Higher Education (all Non-Prop 98)	7,912	8,589	8.6%
Health & Human Services	25,519	26,689	4.6%
Youth & Adult Corrections	6,897	6,980	1.2%
STRS Contribution	1,149	581	-49.4%
General Government	1,683	980	-41.7%
Resources / Environmental Protection	1,141	1,339	17.3%
Judicial	1,764	1,928	9.3%
All Other	<u>2,108</u>	<u>2,118</u>	<u>0.5%</u>
Totals	\$ 82,297	\$ 85,736	4.2%

Judiciary and Trial Court Funding

Proposed Expenditures. For the first time, the budgets for the Judiciary and State Trial Court Funding are combined into one item. The Governor proposes a total of \$3.4 billion (\$1.9 billion General Fund and \$1.5 billion from other funds) and 1,879 positions for the entire Judicial Branch. This represents an increase of \$176.9 million (\$164.5 million General Fund) and 100 positions above the revised 2004-05 budget.

Funding Increases for the Trial Courts. For Trial Court Funding, the Governor proposes a budget increase of \$220.4 million above the revised 2004-05 budget, including a General Fund increase of \$174.7 million. The increase is primarily due to the restoration of a one-time reduction, a baseline increase of \$92.6 million related to court employee salary and benefits, court employee retirement, and court security, and a growth factor augmentation, discussed below.

Growth Factor Increase for the Trial Courts. The Governor proposes an increase of \$97.4 million as a growth factor increase for the trial courts. This amount is consistent with the statutory requirement that the budget for the state's trial courts increase by a factor related to the State Appropriations Limit (SAL). The amount of the increase will be revised at the time of the May Revision. The Governor proposes to provide a similar annual adjustment based on the SAL for the budget for the Judiciary, starting in 2007-08.

Employee Compensation

Defined-Contribution Retirement Plan for New Employees. The Governor proposes that future government employees receive a defined-contribution retirement plan. Employees would receive a state contribution each year into their employee pension account, and their benefit level at retirement would depend on the investment earnings of their individual account. Existing government employees would continue to receive a defined-benefit level at retirement. This proposal would amend the Constitution and is included in the special session called by the Governor.

Defined-Benefit Retirement Plan Changes for Existing Employees. Beginning in 2005-06, the Governor proposes to require employees to pick up one-half of the total charges approved by CalPERS. This would shift \$374 million (\$206 million General Fund) from the state to employees in 2005-06. Additionally, the Governor proposes to allow employees to opt out of CalPERS, with an estimated savings to the state of \$164 million (\$90 million General Fund). This proposal would be phased in as collective bargaining agreements are renegotiated.

Five-day Furlough of State Employees. The Governor proposes a five-day furlough of state employees to save the state an estimated \$109 million (\$60 million General Fund) in 2005-06.

Eliminate Leave from the Overtime Calculation. The Governor proposes to eliminate holiday, sick leave, vacation, annual leave, or compensating time off, from the calculation of overtime. The Administration estimates this will generate 2005-06 savings of \$36.4 million (\$20 million General Fund).

Health Benefit Reductions: The Governor proposes the following reductions to generate total 2005-06 savings of \$55.3 million (\$30.0 million General Fund):

- New employees must work 6 months before health care is provided.
- Enroll employees retired from the military in the federal health care program.
- Reduce the amount the state contributes to health care by \$14.20/month.

Eliminate 2 State Holidays: The Governor proposes to eliminate 2 state holidays to save the state an estimated \$3.1 million (\$1.7 million General Fund).

Cap the Accrual of Vacation and Annual Leave. The Governor proposes to cap the accrual of vacation and annual leave at 640 hours. While the Administration indicates this will result in cost savings, it does not score any 2005-06 budget savings from this proposal.

State Teachers Retirement System (STRS) Contribution Reduction. The Governor proposes a \$469 million reduction (all General Fund) to the state's STRS contribution.

Transportation

Suspension of the Proposition 42 Gasoline Sales Tax Transfer. The Governor proposes to fully suspend Proposition 42 in 2005-06 to generate General Fund savings of \$1.3 billion. Repayment of the suspended amount would be due within a 15-year period. As part of this proposal, a proposition would be submitted to voters to “firewall” Proposition 42 – to make it more difficult to suspend in 2007-08 and thereafter. The budget is silent on the 2006-07 Proposition 42 transfer; however, the proposal does not include “firewall” projection for that fiscal year. The Administration indicates that if Proposition 42 has “firewall” protection in the Constitution, it may be possible to issue bonds in advance of this revenue.

Tribal-Gaming Bond Financing. The Governor’s Budget assumes \$1.2 billion in Tribal Gaming Bonds will be successfully sold in 2005-06. The 2004 Budget Act assumed these bonds would be sold in 2004-05. If successfully sold, the bonds would repay loans from the Traffic Congestion Relief Fund to the General Fund, and associated loans from the State Highway Account and the Public Transportation Account to the Traffic Congestion Relief Fund.

Public Transportation Account Spillover Revenue. The Governor proposes to retain gasoline sales tax “spillover” revenue of \$216 million in the General Fund instead of transferring this revenue to the Public Transportation Account for support of mass transportation projects and services.

Elimination of the High-Speed Rail Authority (Authority). The Governor proposes to transfer the functions of the Authority Board to the California Transportation Commission. The Authority Board has nine members (five members appointed by the Governor, two appointed by the Senate Committee on Rules, two appointed by the Speaker of the Assembly) who do not receive a salary. This proposal is one of the structural changes the Governor will submit to the Little Hoover Commission. The Governor did not propose legislation to repeal the High-Speed Rail Bond Initiative, which will go before voters in November 2006. Despite the elimination proposal, the budget augments funding for the high-speed rail project by \$2.7 million for the legal defense of the Environmental Impact Report, a route realignment study, and a business plan.

General Government

Elimination of Boards and Commissions in the Department of Consumer Affairs. The Governor proposes to eliminate the below 39 Boards and Commissions with their functions assumed by the Department of Consumer Affairs. This proposal is one of the structural changes the Governor will submit to the Little Hoover Commission.

9-1-1 Advisory Board	Physical Therapy Board of California
Accountancy, California Board of	Physician Assistant Committee
Acupuncture Board	Pilot Commissioners Board *
Alarm Company Operator Disciplinary Review Comm.	Podiatric Medicine, Board of
Architects Board, California	Private Security Disciplinary Review Commission (North)
Barbering and Cosmetology, California State Board of	Private Security Disciplinary Review Commission (South)
Behavioral Sciences, Board of	Professional Engineers and Land Surveyors, Board of
Building Standards Commission	Psychology, California Board of
Contractors State License Board	Registered Nursing, California Board of
Court Reporters Board of California	Registered Veterinary Technicians Committee
Dental Auxiliaries, Committee on	Respiratory Care Board of California
Dental Board of California	Seismic Safety Commission, California
Geologist and Geophysicists, Board for	Service Agency Advisory Committee
Guide Dogs for the Blind, State Board of	Speech-Language Pathology and Audiology Board
Hearing Aid Dispensers Advisory Committee	Structural Pest Control Board
Landscape Architects Technical Committee	Mexican American Veterans' Memorial Commission
Medical Board of California	Veterans Memorial Commission, California Vietnam
Occupational Therapy, California Board of	Veterinary Medical Board
Optometry, State Board of	Vocational Nursing and Psychiatric Technicians, Board of
Pharmacy, California State Board of	

* Not currently within the Department of Consumer Affairs

Unspecified General Fund Reductions of \$150 million. The Governor requests authority to reduce state operations budgets by up to a total of \$150 million for vacancy savings and procurement reductions. Similar authority was provided in the 2004 Budget Act.

Strategic Sourcing. The Governor requests authority to reduce budgets for savings generated from leveraging the buying power of the state. The Administration indicates \$95 million in General Fund savings can be generated in 2005-06. A similar proposal was approved with the 2004 Budget Act.

Resources

Total Proposed Expenditures. The Governor's budget proposes \$4.8 billion (\$1.3 billion General Fund) for all departments, boards, and commissions under the Resources Agency. This represents a reduction of \$1.8 billion from 2004-05. This reduction is primarily due to the reduction in bond funding available for appropriation in 2005-06.

Debt Service. Debt service has increased by \$44 million in the Resources and Environmental Protection area due to the large number of resources bonds issued and expended over the last several years.

Fire Protection. The Governor proposes \$25 million for emergency fire protection costs. This is about one-half of what was provided for emergency fire protection in 2004-05. The Governor also proposes \$10.8 million for replacement of outdated fire engines and helicopters and \$2.9 million to update telecommunications equipment used to coordinate fire protection with other jurisdictions.

Year-Round Fire Protection for Southern California. The Governor proposes \$9 million and about 50 new positions to provide year-round wildland fire fighting capacity in Riverside, San Bernardino, and San Diego counties.

Flood Protection. The Governor proposes \$9.7 million General Fund and 27 new positions to develop and implement a comprehensive flood protection plan for the Central Valley flood control system. In addition, the administration is exploring other statutory reforms to provide more sustainable funding for the state's flood protection role in the Central Valley. These reforms are being proposed in response to the recent court decision (*Paterno v. State of California*) that found the state facing increased liability for the structural integrity of the aging levee system in the Central Valley.

All-American Canal Lining. The Governor proposes \$59.1 million General Fund for the lining of the All-American Canal. This funding is consistent with the Quantification Settlement Agreement to reduce California's use of Colorado River water.

CALFED Bay-Delta Program. The Governor proposes the finance plan adopted by the CALFED Bay-Delta Authority in December. The proposed plan provides the following:

- Establishes a set of principles to guide future funding decisions.
- Identifies program priorities, funding needs, and beneficiaries across all CALFED activities.
- Reduces the average annual cost of the program from \$1.3 billion to \$807 million annually.
- Proposes cost share for all program activities.
- Reduces the state's overall contribution from 59 percent over the last four years to 30 percent over the next ten years.
- Assumes the federal contribution will increase from 7 percent over the last four years to 21 percent over the next ten years.
- Increases water user and local contributions from 33 percent over the last four years to 49 percent over the next ten years and identifies new potential water user fees for specific programs.

The plan proposed by the Governor does not include specifics on how the non-state and federal share of the CALFED program will be financed. These specifics will be incorporated in the Governor's May Revision.

State Parks. The Governor proposes further park fee increases to help fund repairs and improvements to state park water, wastewater, and sewer systems in order to achieve compliance with state and federal legal mandates for drinking water and waste discharge. The Governor also proposes \$1.3 million for the management and operation of the coastline acquired through the state's purchase of the Hearst Ranch.

Marine Life Protection Act. The Governor proposes \$500,000 to continue efforts to implement the Marine Life Protection Act by conducting work on the design and management of marine protected areas.

Fish Hatcheries. The Governor proposes support of state fish hatcheries using unexpended tidelands oil revenues allocated to support fish hatcheries in 2004-05.

Other Fish and Game Activities. The Governor proposes 15 new positions for the Department of Fish and Game. The Governor also proposes an increase of \$2.2 million from Proposition 12 and reimbursements for development, enhancement, and restoration of wildlife areas, ecological reserves, and donated lands managed

by the department, including the eradication of noxious weeds on department lands in San Diego County.

Sierra Nevada Conservancy. The Governor proposes \$3.6 million and 13.5 positions for the first year of operation of the Sierra Nevada Conservancy.

California Tahoe Conservancy. The Governor proposes appropriation of \$20.7 million in bond funds and special funds to the California Tahoe Conservancy to continue California's commitment to Tahoe's Environmental Improvement Program.

California Ocean Protection Act. The Governor proposes \$1 million from tidelands oil revenues to implement the Ocean Protection Council. The Council will coordinate statewide activities related to protecting coastal waters, coastal watersheds, and ocean ecosystems.

Coastal Conservancy. The Governor proposes \$31.5 million in bond funds to plan, design, and implement watershed protection projects by the Coastal Conservancy. The Governor's budget also provides the Coastal Conservancy with \$18.8 million in bond funds to support the San Francisco Bay Area Conservancy Program and the Santa Monica Bay Restoration Project.

Environmental Protection

Total Proposed Expenditures. The Governor's budget proposes \$1.4 billion (\$68.9 million General Fund) for all boards, departments, and offices under the Environmental Protection Agency. This is \$192 million less than the 2004-05 budget primarily due to a reduction in bond funding available for appropriation in 2005-06.

Air Quality Regulation. The Governor proposes \$8.6 million and 20 positions to meet increased workload associated with monitoring, assessing, and mitigating fine and ultrafine particulate matter (Particulate Matter 2.5).

Air Quality Grant Programs. The Governor's budget proposes \$30.5 million for the Carl Moyer Program, which is a full year of funding based on increases enacted

as part of the 2004-05 budget. The Governor's budget also provides an additional \$25 million to fund Chapter 707, Statutes of 2004 (AB 923, Firebaugh) to provide additional mobile source emissions mitigation grants to local air districts.

Water Quality Programs. The Governor's budget proposes \$164.7 million in bond funds to fund projects in the following areas: CALFED watershed protection, clean beaches, water recycling, groundwater monitoring, and integrated regional water management.

Brownfield Clean Up. The Governor's budget proposes \$2.7 million (\$1.6 million to the State Water Resources Control Board and \$1.1 million to the Department of Toxics Substances Control) to remediate contaminated brownfield sites and encourage reuse and redevelopment of these sites.

Agriculture

Total Proposed Expenditures. The Governor's budget proposes \$302.8 million (\$100.1 General Fund) to support the California Department of Food and Agriculture for 2005-06. This is a \$6.4 million increase over the 2004-05 budget.

Mediterranean Fruit Fly Preventative Release Program. The Governor's budget proposes \$8 million General Fund to support the Mediterranean Fruit Fly Preventative Release Program.

Emerging Threats to Food Production. The Governor's budget proposes \$2.7 million General Fund to address emerging threats to California's food supply, including Avian Influenza, Mad Cow Disease, and bioterrorism.

Energy and Telecommunications

California Energy Commission. The Governor's budget proposes \$316.7 million to support the Energy Commission's programs. This is a decrease of \$62.7 million from the 2004-05 budget, which is largely due to reduced funding available from the Renewable Resources Trust Fund.

Energy Research and Development. The budget proposes that the Energy Commission expend \$10.6 million from the Public Interest Research, Development, and Demonstration Fund to bring environmentally safe, affordable, and reliable electricity services and products to the marketplace. The budget also includes \$15 million from the Natural Gas Consumption Surcharge Fund to initiate a natural gas research program at the Energy Commission that will improve energy efficiency in consumer gas appliances and manufacturing processes.

California Public Utilities Commission. The Governor's budget proposes \$1.2 billion to support the California Public Utilities Commission, including its various telecommunications subsidy programs and energy efficiency, research, and subsidy programs.

Health & Human Services

Total Proposed Expenditures for Health & Human Services. The Governor proposes expenditures of \$69.8 billion (\$26.7 billion General Fund) for health and human services programs, including state support. The Governor proposes to make \$1.2 billion (General Fund) in adjustments, or “budget solutions”, in the health and human services area. These adjustments include program cuts, redesigns, fund shifts, and related items. Key adjustments include the following:

- Reductions to CalWORKs for proposed savings of almost \$653 million (General Fund), including a reduction of the grant level and elimination of the cost-of-living-adjustment;
- Proposes implementation of federal regulations regarding unborn children for assumed savings of \$242 million (General Fund);
- Assumes savings of \$15 million (General Fund) by restructuring the processing and treatment of Sexually Violent Predators within the State Hospital system; and
- Assumes savings of \$12.3 million (General Fund) through various Medi-Cal redesign proposals.

Department of Health Services

The Governor proposes a total of \$37.6 billion (\$12.6 billion General Fund) for the Department of Health Services. This reflects an increase of \$1 billion in General Fund support, or 7.9 percent, over the revised 2004-05 budget, a decrease of about \$400 million in Federal fund support, and a decrease of \$300 million in special funds, including reimbursements. Of the total amount, \$987.3 million is for state support and \$36.6 billion is for local assistance.

Medi-Cal Program Proposals

Total Proposed Expenditures for the Medi-Cal Program. The Governor proposes total expenditures of \$34.1 billion (\$12.9 billion General Fund) which reflects a General Fund increase of \$981.7 million, or 8.2 percent above the revised current-year budget. The General Fund increase primarily reflects increases in caseload and cost per eligible person, increased Medicare premiums, the elimination of 2004-05 one-time savings, changing assumptions of estimated anti-fraud savings,

and the implementation of quality improvement fees. Total caseload is anticipated to be 6.8 million eligible people.

Proposed Medi-Cal Program “Redesign”. The Governor proposes to “redesign” Medi-Cal through implementation of the following key components:

- (1) ***Expansion of Managed Care—More Counties and Required Enrollment:*** The managed care model would be expanded to include 13 additional counties, including El Dorado, Imperial, Kings, Lake, Madera, Marin, Mendocino, Merced, San Benito, San Luis Obispo, Sonoma, Placer and Ventura. New Medi-Cal enrollees who are aged, blind, and disabled would be required to enroll in a managed care plan. The expansion is to be achieved through a phased-in process, and when fully implemented, Medi-Cal managed care plans would be in 35 counties. The budget proposes increased costs of \$7.6 million (\$3.3 million General Fund) to hire 48 new state positions for this expansion effort. The Administration projects that savings of \$177 million (\$89 million General Fund) will be achieved in 2008-09.
- (2) ***Restructuring Hospital Financing through Federal Waiver.*** The Governor is seeking a five-year hospital financing waiver with the federal government that would completely restructure the \$3.8 billion reimbursement system and would directly affect the financial viability of about 240 hospitals statewide. This is a complex proposal and requires further in-depth discussions with the hospital industry and federal government, along with substantive review by the Legislature, prior to any enactment. At least \$900 million in federal funding is at risk for the state.
- (3) ***Modifying the Medi-Cal Benefit Package--Dental:*** The Governor proposes to capitate the Medi-Cal dental package by establishing a limit of \$1,000 for services to adults (excluding federally mandated services provided by physicians, emergency services, and hospital costs associated with dental treatment), over a 12-month period. The budget assumes savings of \$50 million (\$25 million General Fund) from this proposal.
- (4) ***Beneficiary Cost Sharing:*** Under this proposal, Medi-Cal enrollees with incomes above the federal poverty level would pay a monthly premium (\$4 per month for children under 21 years and \$10 per month for adults) to maintain their Medi-Cal coverage. This would include about 460,000 families and children with household incomes above 100 percent of poverty (i.e., \$1,306 per month for a family of three), and 90,000 seniors and individual with disabilities with incomes above the SSI/SSP level (i.e.,

\$1,006 a month for a single person and \$1,339 a month for a couple). A maximum of \$27 per month per family would apply.

The budget assumes increased costs of \$2.3 million (\$650,000 General Fund) in 2005-06 for system changes and then savings of \$11.1 million (\$5.5 million General Fund) in 2006-07 from both the collection of premiums as well as from disenrollment (i.e., people are dropped due to lack of payment).

- (5) ***Single Point of Entry—Processing Change for Children’s Applications:*** Under this proposal, Medi-Cal applications for children received through the “Single Point of Entry” process operated by the Healthy Families Program’s eligibility processing vendor will be completely processed by the vendor and will not be forwarded to a county for processing. There are about 120,000 applications for children received annually by the vendor which would be affected. The budget assumes savings of about \$1.2 million (General Fund).

Federal Regulations for Funding Prenatal Care: The Governor proposes to reduce by \$242 million in General Fund support and obtain corresponding federal funds through the use of certain federal regulations that pertain to unborn children. To implement this proposal, the state would need to file a Medicaid State Plan Amendment under the federal State-Children’s Health Insurance Program (S-CHIP) to claim a 65 percent federal fund match for prenatal care that is currently funded solely using the state’s General Fund. This action would require legislation to authorize this action.

Medicare Modernization Act and Medicare Drug Benefit Implementation: The Medicare Modernization Act of 2003 implements the Medicare Part D drug program that provides drug benefits to all Medicare enrollees, including those that are Medi-Cal eligible (i.e., dual eligibles), effective January 1, 2006. Due to this coverage, the federal government will no longer provide federal funding for Medi-Cal coverage for dual eligibles. In addition, the state must reimburse the federal government a portion of savings gained from not providing these drugs. The phased-down contribution, or “clawback”, is 90 percent of the savings in 2006, based on a formula set in the Act, reduced each year until it reaches 75 percent.

The budget assumes savings from no longer providing Part D drugs to dual eligibles at \$746.8 million (General Fund). The cost of the “clawback” is estimated to be \$646.6 million (General Fund). Therefore, the budget assumes a net savings of \$100.2 million (General Fund).

California RX Initiative. The Governor proposes an increase of about \$4 million (General Fund) to implement his proposed California RX (Cal RX), a prescription drug discount program intended to provide drug discounts to certain lower-income individuals. Legislation on this proposal is currently being crafted. Of the proposed amount, \$2 million would be for state support and \$2 million is for local assistance.

Public Health Proposals

Total Proposed Expenditures for Public Health Programs. The Governor proposes expenditures of \$3.5 billion (\$703 million General Fund) for 2005-06. This represents an increase of \$53.5 million, or 8.2 percent, above General Fund expenditures in the revised 2004-05 budget.

AIDS Drug Assistance Program (ADAP). The Governor proposes total expenditures of \$263.6 million (\$91.2 million General Fund) for ADAP. This reflects an increase of \$18.8 million (increase of \$24.6 million General Fund and decrease of \$5.8 million in federal funds) over the revised current-year budget. It is estimated that ADAP will serve 30,446 clients in 2005-06.

California Obesity Initiative. The budget includes \$ 6 million (General Fund) for an obesity prevention program. Of this amount, \$3 million will be used to fund state support activities and \$3 million will be used for local assistance functions.

Eliminates Office of Binational Border Health. The Governor proposes elimination of this office for proposed savings of \$694,000 General Fund.

Proposition 99 Funding Shifts. The budget proposes various funding shifts using the Cigarette and Tobacco Product Surtax Fund monies (Proposition 99 funds). These shifts are contingent upon approval of the proposal to access increased federal funds for prenatal services as referenced under the Medi-Cal Program.

Healthy Families Program

Total Proposed Expenditures for Healthy Families Program. The Governor proposes to provide a total of \$894.9 million (\$325.2 million General Fund) for the Healthy Families Program in 2005-06, an increase of \$33.3 million (General

Fund), or 11.4 percent over the current-year. It is anticipated that 789,300 children will be enrolled as of June 30, 2006, for an increase of 75,400 children, or 10.6 percent over the current-year.

Restoration of Certified Application Assistance Fees. The budget includes an increase of \$14.2 million (\$7.3 million General Fund) for the restoration of certified application assistance fees and the related increased enrollment impact. It is anticipated that an additional 14,372 children will enroll in Healthy Families due to the restoration of this outreach funding.

Increased State Support for Enrollment and Retention Functions. The budget proposes an increase of \$2.5 million (\$867,000 General Fund) to fund 27.5 new state positions to process application appeals, re-establish the application assistance payment process, and monitor the administration vendor contract.

Access for Infants & Mothers (AIM) Program

Total Program Expenditures. The budget proposes total expenditures of \$99.8 million (\$28.5 million General Fund) which reflects a decrease of \$23.4 million or 19 percent. This decrease in funding is primarily the result of the enrollment of infants born to AIM mothers directly into the Healthy Families Program which commenced in 2004-05.

Developmental Disability Services

Total Proposed Expenditures. The Governor proposes expenditures of 3.7 billion (total funds) in 2005-06, an increase of \$166 million (total funds) or 4.7 percent over the revised current-year budget for the developmental services system. Of this amount, about \$3 billion is proposed to provide services in the community, an increase of \$187 million from the current-year. Total expenditures for the state Developmental Centers is proposed at \$699 million (total funds), a decrease of \$22 million.

Continues Cost Containment Actions Taken in the Budget Act of 2004. The Governor proposes to continue several cost containment actions enacted as part of the Budget Acts of 2003 and 2004. These include (1) continuation of the Day Program rate freeze, (2) continuation of the contract services rate freeze, (3) continuation of the Community Care Facility rate freeze, (4) continuation of the

elimination of the SSI/SSP pass-through, (5) continuation of the delay in intake and assessment (60 days to 120 days), (6) continuation of the non-community placement plan start-up suspension, (7) an unallocated reduction in Regional Center Operations of \$6.5 million, and (8) an unallocated reduction in the Purchase of Services area of \$7 million.

Cost Containment Guidelines. The Governor is proposing new cost containment guidelines for the Purchase of Services in order to grant more authority to Regional Centers when developing consumer services plans and purchasing services. The budget assumes savings of \$14 million (\$10.5 million General Fund) from this proposal.

Status of Rate Standardization Project. The Administration notes they are working to address the issue of standardizing negotiated rates for vendors who provide services to consumers in the community. Though no detail is provided in the Governor's budget, they note that proposals may be forthcoming in his May Revision.

Plan for Closure of Agnews Developmental Center in San Jose. The Governor proposes to close Agnews Developmental Center by June 30, 2007 and is releasing a plan for closure along with his proposed budget. About 350 individuals with developmental disabilities currently reside at Agnews. Key elements to the plan include the following:

- Establishing a permanent stock of housing in the Bay Area dedicated to serving individuals with developmental disabilities;
- Expanding community-based residential options to serve individuals with special health care needs and challenging behaviors by creating new residential service delivery models and pilot projects (legislation required);
- Utilizing Agnews' employees—about 200 staff—on a temporary basis in community settings to augment and enhance services, including health care, clinical services and quality assurance (legislation required);
- Enhancing medical case management and related specialized services in the Bay Area by purchasing a medical care policy to supplement Medi-Cal provided services for individuals who transition to the community; and
- Implementing a quality management system that focuses on assuring that quality services and supports are available prior to, during, and after the transition of each person leaving Agnews.

Mental Health Programs

Total Proposed Expenditures for Mental Health Programs. The Governor proposes expenditures of almost \$2.8 billion (\$1 billion General Fund) for an overall General Fund increase of \$78.1 million, or 8.1 percent over the revised current-year budget. This General Fund increase is the net result of significant adjustments in the State Hospital budget as well as the funding of local mandates after three years of suspended payments.

In addition to the state budget expenditures, it is estimated that a total of \$1.220 billion will be available for mental health services, including those services provided to indigent individuals, through County Realignment Funds. This 2005-06 realignment amount reflects an increase of \$19.4 million, or about 1.6 percent more than in 2004-05.

Proposition 63 the Mental Health Services Act. In November 2004, voters approved this proposition which will provide a dedicated funding source for public mental health services from the personal income tax revenues of individuals whose adjusted gross income exceeds \$1 million annually. For the current-year, projected revenues to be deposited into the Mental Health Services Account are \$254 million, and for 2005-06 estimated revenues are \$683 million. The Administration notes that an expenditure plan for these funds will not be forthcoming until the Governor's May Revision. It should also be noted that the Mental Health Services Account is a special fund which provides for a continuous appropriation and is not therefore contingent upon an annual Budget Act appropriation.

Activation of Coalinga State Hospital. The Governor proposes an increase of \$65.7 million (General Fund) for the continuing activation of Coalinga State Hospital which is scheduled to open in September 2005 with a capacity of 250 beds. Sexually Violent Predators (SVPs) currently at Atascadero State Hospital will be transferred to Coalinga. Of the amount proposed, \$38.3 million is to support about 660 level-of-care positions, \$8.7 million is to support 140 non-level-of-care positions and \$18.7 million is to support operating expenses including relocation costs for state employees choosing to transfer to Coalinga.

Early Periodic Screening Diagnosis and Treatment Program (EPSDT). The Governor proposes a *net* increase of \$47.5 million (\$27.2 million General Fund) for the Early Periodic Screening Diagnosis and Treatment Program (EPSDT).

State Mandates on Local Programs. With the passage of Proposition 1A, the state is now obligated to reinstitute payments to local agencies for state mandated costs. A General Fund increase of \$12.5 million is proposed for payments to local agencies for mental health related mandates. However it should be noted that the Governor continues to suspend payments to counties for mental health services provided to special education students even though these services are mandated per federal education law.

Mental Health Managed Care Program. A net General Fund increase of \$5.7 million for both inpatient and specialty mental health services is being proposed. Most of this adjustment is due to caseload increases.

California Work Opportunity and Responsibility to Kids (CalWORKs)

The Governor proposes to reduce the CalWORKs program by 12 percent, or \$652.8 million. This reduction allows \$316.5 million in federal TANF funds to replace General Fund resources in other programs, including \$55 million in Foster Care, \$60 million in the Department of Developmental Disabilities, and \$201 million in Juvenile Probation.

Reduction of CalWORKs Grants and Permanent Elimination of Cost of Living Adjustments (COLAs). The Governor proposes to reduce CalWORKs grant levels by 6.5 percent to generate \$212.3 million in TANF and General Fund savings. These savings would be used to offset General Fund costs in other departments. Further, the Governor proposes to suspend the July 2005 CalWORKs COLA, for \$163.8 million in General Fund savings, and permanently suspend all future COLAs.

Under the Governor's proposal, the maximum monthly cash grant for a family of three would be reduced by \$47 to \$676, a level below the grant level in effect in 1989. The reduction would be partially offset by a \$10 increase in monthly food stamps benefits.

Expand Work Participation Requirements and Sanction Savings. The Governor proposes to expand the CalWORKs work participation reforms that were included in the 2004 Budget Act. The additional reforms are not specified, but will be based

on the result of a pending evaluation of CalWORKs sanction policies, and are estimated to result in \$12 million General Fund savings in 2005-06.

Reduction of Earned Income Disregard. The Governor proposes to reduce the Earned Income Disregard for CalWORKs families. This proposal would result in savings of \$79.5 million in 2005-06 and \$109.3 million annually, thereafter. Current law allows the first \$225 of income per month to be exempt under CalWORKs eligibility guidelines, plus 50 percent of any remaining income. The Governor's proposal would reduce the income disregard to \$200 and 40 percent of remaining income. This proposal would reduce the level at which low-income working families remain eligible for CalWORKs benefits, and would affect 112,669 families in 2005-06.

County Pay for Performance Proposal. The Governor proposes to tie county administration funding to CalWORKs client outcomes. County allocations for 2006-07 will be adjusted based on employment and work participation rates in 2005-06. This proposal is estimated to result in savings of \$22.2 million in 2005-06 due to lower grant costs as clients increase earnings and the number of hours worked.

Eliminate Employment Services Augmentation. The Governor proposes to eliminate \$50 million in 2005-06 that was included in the 2004 Budget Act for CalWORKs employment services. This funding was intended to provide support for the ongoing increased work participation requirements that were implemented in the 2004 Budget Act.

Offset Current Year Changes with Savings. The Governor proposes to change CalWORKs budgeting practices by using unexpected prior year savings in CalWORKs for current year expenses, resulting in \$42.9 million in current year savings.

Other Human Services Programs

Reduction of State Funding for In-Home Supportive Services (IHSS) Worker Wages and Benefits. The Governor proposes to permanently reduce the level at which the state participates in IHSS provider wages and benefits from \$10.10 to the State minimum wage (\$6.75) for General Fund savings of \$206.7 million in 2005-06 and \$259.5 million annually, thereafter. The Governor proposes to repeal current law, which provides for state participation in wages and benefits resulting

from collective bargaining agreements up to a maximum of \$12.10 per hour. Under the Governor's proposals, counties would have to reduce IHSS provider wages or fund the difference between minimum wage and the negotiated wage with county funds upon expiration of current collective bargaining contracts.

Suspension of Supplemental Security Income/State Supplementary Payment (SSI/SSP) Cost of Living Adjustments (COLA). The Governor proposes a one-time suspension of the January 2006 state SSI/SSP COLA and the withholding of the federal COLA, for General Fund savings of \$258.9 million in 2005-06 and \$517.8 million annually, thereafter. The maximum SSI/SSP grant would remain at the April, 2005 level, which is \$812 for individuals and \$1,437 for a couple.

Labor

Merger of Three Labor Boards. The Governor proposes to merge the Occupational Safety and Health Appeals Board, the Unemployment Insurance Appeals Board, and the Workers' Compensation Appeals Board into a single newly-created nine-member commission. The existing boards rule on disputes between workers and employers in their specific subject matter areas. All board members are paid a salary. This proposal is one of the structural changes the Governor will submit to the Little Hoover Commission.

Elimination of the Industrial Welfare Commission (Commission). The Governor proposes to transfer the functions of the Commission to the Labor and Workforce Development Agency. The Commission includes five members with two members representing labor, two members representing employers and one member representing the general public. All members are appointed by the Governor with the consent of the Senate. Statute requires the Commission to conduct a full review of the adequacy of the minimum wage at least once every two years. The Legislature de-funded the Commission for 2004-05, so it is not currently in operation. This proposal is one of the structural changes the Governor will submit to the Little Hoover Commission.

Elimination of the Commission on Health and Safety and Workers' Compensation (Commission). The Governor proposes to transfer the functions of the Commission to the Labor and Workforce Development Agency. The Commission is a joint labor-management body created in 1993 and charged with overseeing the health and safety and workers' compensation systems and recommending administrative or legislative modifications. Commission members do not receive salaries. Four members are appointed by the Governor and four by the Legislature. This proposal is one of the structural changes the Governor will submit to the Little Hoover Commission.

Benefit Audit Augmentation. The Governor proposes an augmentation of \$9.1 million for the Employment Development Department and 147 temporary positions to liquidate the benefits audit backlog.

Economic and Employment Enforcement Coalition. The Governor proposes to augment the Employment Development Department (\$2.5 million and 23.7 positions) and the Department of Industrial Relations (\$3 million and 27.5

positions) to conduct increased enforcement activities against employers who violate labor laws. The Governor indicates that this is part of a new effort to combat the underground economy.

Veterans' Affairs

Funding for Veterans' Homes. The Governor proposes a \$3 million increase in the Veterans' Affairs budget (increased federal funds and a reduction of \$899,000 in General Funds) and the addition of 11.8 positions to maximize federal funds and improve service and equipment at the state's veterans' homes.

Education

Proposition 98

Proposition 98 – Maintain Current Year Funding. The Governor proposes to maintain Proposition 98 funding for K-14 education (K-12 schools and community colleges) at the level appropriated by the 2004-05 budget act. The 2004-05 budget appropriated \$47 billion for K-14 education, which was approximately \$2.0 below the minimum guarantee at the time of enactment. Due to larger than estimated state revenues and student enrollments, the minimum guarantee has grown an additional \$1.1 billion since then. The Governor does not propose to fund this overall increase, estimated to save \$2.3 billion over two years.

Proposition 98 – Budget Year Increase. The Governor proposes \$50.0 billion for K-14 education in 2005-06, an increase of \$2.9 billion (6.1 percent) over 2004-05.

Overall Budget Reforms: As a part of the Governor's overall budget reform, the Governor proposes a Constitutional Amendment to change the state's budget process by requiring mid-year, across-the-board reductions in virtually every state funded program area, including education, if state expenditures exceed state revenues. As part of this overall budget reform the Governor proposes changes to Proposition 98 to (1) eliminate the Test 3 calculation and payment of maintenance factor and (2) eliminate suspension in future years. The Governor also proposes to expedite the calculation of Proposition 98 settle-up and to provide payment via continuous appropriations. Existing Proposition 98 maintenance factor obligations (estimated at \$3.9 billion) and accumulated settle-up obligations (estimated at over \$1 billion) would be deemed one-time obligations and paid off over a 15 year period.

K-12 Education

Overall Increase. The Governor proposes a total of \$44.7 billion in Proposition 98 funding for K-12 schools in 2005-06, an increase of \$2.5 billion (6.0 percent) above the 2004-05 budget. As proposed, the budget provides \$7,374 per-pupil in Proposition 98 funding in 2005-06, an increase of \$362 per-pupil above the 2004-05 budget.

Statutory Growth and COLA's Fully Funded. The Governor proposes expenditures of \$2.0 billion to fully fund statutory growth and COLA's (cost-of-living adjustments) for K-12 revenue limit and categorical programs in 2005-06. Of this amount, the Governor proposes \$395 million for enrollment growth, estimated to increase by .79 percent in 2005-06. In addition, the Governor proposes \$1.65 billion for education program COLA's, estimated at 3.93 percent in 2005-06.

Additional Funding for Deficit Factor Payment. The Governor's Budget proposes an additional \$328 million to pay down the revenue limit deficit factor to compensate for revenue limit reductions that originated in the 2003-04 budget. This proposal nearly cuts the outstanding deficit factor in half.

Program Increases to Backfill One-Time Funding. The Governor's Budget proposes approximately \$146 million in 2005-06 to restore funding for several categorical programs that were funded with one-time funds in 2004-05.

Budget Policy Initiatives

The Governor's Budget proposes a number of budget and policy reforms and initiatives as a part of the 2005-06 budget, beyond changes to Proposition 98 discussed earlier. Most notably, the Governor proposes:

- ***Merit Pay for Teachers & Administrators and School Budget Accountability.*** The Governor has identified this issue as one of four issues before the current Special Session of the Legislature. Specifically, the Governor proposes a Constitutional Amendment that would base pay and other employment decisions on the performance of teachers and

administrators, rather than on tenure. In addition, the Governor proposes to improve the transparency and accountability of school budgets.

Other reforms and initiatives include:

- ***Career and Technical Education.*** The Governor proposes some additional funding and a number of changes to K-12 and Community Colleges programs to ensure that all students have access to quality career technical education programs.
- ***Fitness and Nutrition.*** The Administration seeks to improve the quality of food and beverages and to increase physical fitness activities opportunities and activities on school sites as a part of the Governor's Obesity Initiative
- ***Accelerated English Language Acquisition Program.*** The Administration proposes a new program to provide targeted reading instruction to English learners in 4th through 8th grades.
- ***Alternatives for Failing Schools.*** The Administration proposes that the State Board of Education take action in failing schools to either convert them to charter schools or assign School Recovery Teams to manage schools. The administration proposes a number of new programs to build capacity in these areas.
- ***Local Control School Pilot Program.*** The Governor proposes to establish a new pilot program to increase student achievement by delegating budget authority and academic decision making to the school site level.
- ***School Size Reduction.*** The Governor proposes to create smaller learning environments within the state's elementary, middle and high schools through changes to the school facility funding incentives and new technical assistance and planning resources.
- ***Improving Fiscal Health.*** The Administration proposes new training programs to improve the skills of school district business officers.
- ***Categorical Program Reforms.*** The Governor proposes providing additional flexibility for categorical programs included in the Professional Development Block Grant established by the AB 825 reforms enacted last

year. The Governor also proposes changes to simplify and clarify funding calculations under the Charter Schools Categorical Block Grant.

State Teacher's Retirement System (STRS)

Reductions to State Contributions to CalSTRS. The Governor proposes to reduce state general funds (Non-Proposition 98) for the California State Teacher's Retirement System (CalSTRS) by \$567.4 million in 2005-06. This proposal would eliminate state general fund support -- estimated at \$469 million in 2005-06 -- for the CalSTRS Defined Benefit Program. The Administration proposes shifting responsibility for the CalSTRS Defined Benefit Program to school districts and teachers. In addition, the Governor proposes an additional \$100 million in savings from avoided costs for STRS contributions and other baseline adjustments.

Child Care

Child Care Reform. The Governor proposes a variety of child care reforms aimed at generating savings in the amount of \$157.4 million: \$94.8 million from General Fund Proposition 98 and \$62.6 million from Temporary Assistance for Needy Families (TANF) funds. Specifically, the Governor proposes to reduce reimbursement rates for license-exempt providers in an attempt to create a financial incentive for providers to acquire additional training and education; limit the length of time recipients can receive subsidized care; alter the reimbursement level for providers serving only subsidized children; and re-bench income eligibility to the Federal Poverty Level rather than previously-established income levels. Other reforms include the implementation of a single child care wait list per county. The Governor provides \$7.9 million to counties to establish and maintain these waiting lists. These reforms follow in the footsteps of prior-year reforms authored by the Administration.

Public Libraries

Public Library Foundation. The Governor proposes to reduce by \$2.2 million the level of spending on the Public Library Foundation, which provides monies to local libraries based on a statutory formula. Funding provided for this program is proposed at \$12.15 million.

Additional changes to the California State Library budget include an \$828,000 reduction to Library Development Services, a \$276,000 reduction from English Language Acquisition services, and a \$170,000 unallocated reduction to the State Library's operations.

In addition, the Governor proposes an augmentation of \$329,000 to implement a new automated library for the Braille and Talking Book Program.

Higher Education

Governor's Compact with UC and CSU. In the Spring of 2004, the Governor reached an agreement with both the University of California (UC) and California State University (CSU) to establish a "compact" which would provide a set level of financial support for those systems beginning in the 2005-06 fiscal year and continuing through the 2010-11 fiscal year.

Under this compact, the Governor agreed to provide (1) funding equivalent to a 3 percent base General Fund increase in both the 2005-06 and 2006-07 fiscal years and (2) General Fund augmentations to support student enrollment growth of 2.5 percent annually.

Further, the Governor, UC, and CSU agreed that undergraduate student fees would increase by 8 percent annually in 2005-06 and 2006-07, and graduate student fees would move toward the goal of 150 percent of undergraduate fee levels

General Fund Support. As part of the Governor's "compact" his proposal includes an additional 3 percent or \$147.8 million in General Fund support for the UC (\$76.1 million) and CSU (\$71.7). This augmentation is proposed to be offset by a \$24.3 million unallocated General Fund reduction (\$17.3 million UC; \$7 million CSU).

Student Enrollment Growth at UC and CSU. Pursuant to the Governor's "compact" the 2005-06 budget proposes an additional \$88.7 million to UC and CSU to support increased student enrollments of 2.5 percent. This equates to an additional 5,000 full-time equivalent students (FTES) at UC (\$37.9 million) and 8,000 FTES at CSU (\$50.8 million).

Total FTES enrollments at UC are expected to reach approximately 206,000 (all campuses) while CSU enrollments will be approximately 332,223 FTES.

Growth in Student Enrollments at the Community Colleges. The Governor proposes to provide \$136.7 million to fund three percent enrollment growth at the Community Colleges. These funds would be used to support an additional 34,000 Full-Time Equivalent Students (FTES), bringing the total number of Community College students to approximately 1.18 million statewide.

Student Fees. Pursuant to the “compact”, the Governor proposes to increase undergraduate fees at the UC and CSU by 8 percent (this action was already taken by the UC Board of Regents and the CSU Board of Trustees in November 2004). Graduate student fees are proposed to increase by 10 percent; UC Professional School students will see fee increases of 3 percent (after last year’s substantial hike in fees); and CSU teacher credentialing student fees are proposed to increase by 8 percent (same as undergraduate students).

- Resident Undergraduate fees at UC will be approximately \$6,769 per year;
- Resident Undergraduate fees at CSU will be approximately \$3,102 per year.

Under the Governor’s proposal, UC and CSU will retain the fee revenues derived from the above-noted increases. Further, the Governor’s Budget directs the UC and CSU to dedicate a “substantial portion” of this fee revenue to aid for financially-needy students.

No fee increases are proposed at the Community Colleges.

Student Outreach. The Governor’s Budget proposes no direct reductions to student outreach programs at either the UC or CSU. However, the Governor has given the authority to implement the above-noted unallocated reductions to the UC and CSU respectively and it is unclear how those reductions will be actualized.

Institute for Labor Studies. The Governor proposes to eliminate all state support (\$3.8 million) for the Institute for Labor Studies at the UC.

UC Merced. The Governor provides an additional \$14 million to support one-time start-up costs associated with opening the new UC Merced campus for the 2005-06 academic year. Total support for UC Merced is proposed at \$24 million.

Capital Outlay. The Governor proposes capital outlay expenditures for all three segments of higher education totaling \$916.4 million. This includes \$305.2 million in GO bond funds for 24 projects at the UC; \$261.5 million for 19 projects at the CSU; and \$349.7 million for 50 projects at the community colleges.

Community College Proposition 98 Support. General Fund Proposition 98 support for community colleges is proposed to increase by a total of 7.5 percent over the current year. This brings the Proposition 98 amount appropriated to community colleges to approximately \$3.3 billion. Total support for the community colleges is proposed to exceed \$5.7 billion (from all funding sources).

Community College COLA. Similar to K-12 education, the Governor proposes to fund a 3.93 percent cost-of-living-adjustment for community colleges general apportionments and select categorical programs.

Additional CCC Adjustments. The Governor proposes to appropriate \$20 million (on a one-time basis) to the community colleges to better coordinate technical and vocational education-related curricula with K-12 schools. Further, the Governor proposes to make permanent a \$3 million appropriation to support the Foster Parent Training Program. Lastly, the Governor is “setting aside” \$31.4 million for the community college Partnership for Excellence Program, pending resolution on district-specific accountability/outcomes.

No additional support is provided for either community college equalization or noncredit instruction.

Hastings College of Law. Under the Governor’s proposal, Hastings College of Law would see a \$244,000 increase in its general support. Hastings enrollments have remained stable for many years, so enrollment growth funding is not necessary. Fees at Hastings are expected to reach approximately \$22,000 for California residents and over \$33,000 for nonresidents.

California Institute for Regenerative Medicine (CIRM). Pursuant to the recent passage of Proposition 71, the Governor establishes the CIRM to oversee and administer \$3 billion in bond proceeds for stem-cell-related research.

Cal Grant--Ongoing Support. The Governor provides an additional \$44.8 million General Fund to maintain the Cal Grant program (shifting funding from the current year to the 2005-06 year due to revised current year estimates). Total number of Cal Grant entitlement awards is expected to exceed 186,000; competitive Cal Grant awards are expected to reach approximately 56,000.

Further, the Governor proposes to fund \$35 million worth of one-time Cal Grant expenditures using Student Loan Operating Funds (from EdFUND, the state’s student loan auxiliary organization). This shift in funding is similar to actions taken by the state in the current year to pay \$146.5 million in one-time Cal Grant expenses from the same funding source.

Cal Grant Award Level. The Governor proposes to reduce the grant amount for students attending private and independent colleges by \$883 annually (from the

current maximum level of \$8,332 down to \$7,449). This change is expected to reap \$7.5 million in General Fund savings.

APLE Program. The Governor provides an additional \$6.8 million for increased Assumption Program of Loans for Education (APLE) costs in the 2005-06 fiscal year. The Governor additionally proposes to fund 100 new National Guard APLE awards and appropriates \$200,000 for this purpose.

Public Safety & Corrections

Department of Corrections (CDC)

Total Proposed Expenditures. The Governor proposes \$6.5 billion (\$6.4 billion General Fund and \$138.3 million other funds) and 51,848 positions for the CDC. This represents an increase of \$247.5 million (\$250 million General Fund), or about 4 percent and 1,575 positions above the revised 2004-05 budget.

Population Costs Increase. The Governor proposes an increase of \$280.1 million due to a higher than anticipated inmate population. The Governor's proposal for the budget year assumes that CDC's average daily population will decrease from 163,019 in 2004-05 to 162,755 in 2005-06, a reduction of 264 inmates, or 0.2 percent. However, the current inmate population is approximately 164,000, and the 2004 Budget Act assumed an average daily population of only 157,259. The projected reduction in inmate population is due to the anticipated impact of the parole reforms from the 2003 and 2004 Budget Acts. In the current year, CDC estimates that funding of \$207.5 million will be needed to fund the higher than anticipated inmate population.

Restructure and Reform of Youth and Adult Correctional Agency (YACA). As part of a proposed reorganization for the YACA, the Governor submitted a reorganization plan to the Little Hoover Commission. The budget proposal does not assume any of the elements from the reorganization at this time.

Workload Budget Adjustments. The Governor proposes an increase of \$91.9 million related to a number of workload adjustments. Specifically, the proposal contains \$35 million related to eliminate salary savings for posted positions, \$45 million for a price increase, \$9.8 million to increase the budgeted relief for non custody positions, and \$2.1 million and 20 positions related to increases for inmate employee discipline.

Unallocated Reduction. The Governor proposes an unallocated reduction of \$95.3 million from CDC's Inmate and Parolee Programs. No specific proposal for reductions has been submitted at this time, but reductions to Inmate and Parolee Programs could potentially include cuts to substance abuse treatment programs, inmate or parolee employment programs, academic education programs, and vocational education programs. The Administration indicates that this reduction

may be replaced with savings generated through revisions to the labor agreement with Bargaining Unit 6 that expires at the end of fiscal year 200506.

Employee Compensation Adjustment. The Governor proposes an increase of \$271.5 million General Fund related to previously negotiated compensation increases for employees of the CDC.

Incarceration of Undocumented Felons. The Governor assumes \$78.5 million in federal State Criminal Alien Assistance Program (SCAAP) funding. This amount represents only 10.8 percent of the estimated \$729.7 that CDC and CYA expect to spend million in 2005-06 on the incarceration of foreign nationals.

Inmate Medical Services Augmentation. The Governor proposes an increase of \$30.1 million and 101 positions to improve the quality of inmate medical services and to continue to comply with the requirements of the Plata lawsuit settlement.

Other Public Safety and Criminal Justice.

Valdivia Remedial Plan. The Governor proposes an increase of \$6.9 million General Fund to provide sufficient staffing and resources to address the increased number of revocation hearings resulting from the implementation of the Valdivia Remedial Plan.

Conditions of Confinement and Treatment at CYA. The Governor's budget does not contain any proposals related to the settlement of the conditions of confinement lawsuit at the Youth Authority (CYA). The Administration indicates that details of the remedial plan and any associated funding needs will be provided as part of the May Revise.

Juvenile Justice Reform. The Administration indicates that it is working with local government and other stakeholders in the juvenile justice system to develop a comprehensive plan to reform California's juvenile justice system and to redefine the role of the CYA, but no specific plan is included with the budget. Potential policy changes that are being evaluated include shifting responsibility for supervising youthful offenders on parole from CYA to the counties, and limiting the types of offenders that can be sent to CYA.

DNA Fingerprint, Unsolved Crime and Innocence Protection Act (Proposition 69). The Governor proposes a current year augmentation of \$11 million from the

DNA Identification Fund to fund the requirements of Proposition 69. The Governor also proposes \$11.2 million in 2005-06 from the DNA Identification Fund and 46 positions to address the workload resulting from expanded collections of DNA, palm prints, and thumbprints. The Governor also proposes \$4 million General Fund in the current year and \$3.6 million in the budget year for the costs that CDC will incur for collecting DNA samples from all parolees and inmates.

Local Government

Local Government Agreement

The local government agreement -- made effective by the approval of the electorate in the November 2004 ballot -- provides \$1.3 billion of annual General Fund (GF) savings in 2004-05 and 2005-06 by reducing payments to, or shifting funds from, local governments.

Other Local Government Proposals

The Governor's budget highlights the following changes: (1) Eliminates grant funding for small and rural sheriffs for a GF savings of \$18.7 million; (2) reduces grant funding for property tax administration by \$5.7 million GF (leaving approximately \$54.3 million GF for the program); (3) reduces funding associated with the Juvenile Justice Crime Prevention Act program by \$75 million, with the remaining \$25 million be shifted to the Board of Corrections for distribution to local governments; and (4) reduces funds available for the Public Library Fund grants by \$3.3 million (approximately \$12.2 million GF is remains available under this program).

In addition, no funding changes were proposed for either the COPS program or the Williams Act. Specifically, (1) the Citizen's Option for Public Safety (COPS) program -- provides discretionary funding on a per capita basis, for local police departments and sheriffs for front line law enforcement (with a minimum guarantee of \$100,000), sheriffs for jail services, and district attorneys for prosecution -- funding remains at \$100 million; and (2) Williamson Act subventions, remain at \$39.7 million.

Finally, the budget is predicated on not funding approximately \$250 million for local mandated costs.

State Administration and General Government

Revenue Adjustments

The budget includes various revenue adjustments of approximately \$409 million GF, the largest adjustments are from (1) the Public Transportation Account spillover revenues of approximately \$216 million, and (2) additional funding available as a result of increased Tideland Oil revenues of approximately \$121 million.

Furthermore, additional GF resources of \$10.4 million are being provided to the Franchise Tax Board for two measures: (1) additional staff to combat abusive tax shelters, which is expected to generate \$43 million in revenue in the budget year, and (2) additional staff for tax gap enforcement, which is expected to generate \$34 million in additional revenue. The tax gap is the difference between what taxpayers owe and what they voluntarily pay.

Impact on Senior Citizens

The budget includes two significant changes to the following programs: (1) The Senior Citizens Renters Tax Credit, the income threshold for eligibility in this program is changed – under the current program if an individual makes \$37,300 or less they are eligible, under the governor’s proposal income eligibility is reduced to persons with an income of \$13,200 or less, for \$100 million GF savings; and (2) Eliminates the Senior Citizens’ Tax Assistance Program for a net GF savings of \$35.8 million; however, the administration proposes to expand the Senior Citizens’ Tax Deferral Program at a cost of approximately \$4.7 million.

Unallocated Reductions

In addition to specific reductions in major program areas, the budget reduces state operations for various departments by a total of \$150 million GF. The budget proposes to give departments flexibility to use lay-offs, hiring freezes, procurement reductions, or other administrative means to achieve these reductions.