SENATE BUDGET & FISCL REVIEW

Overview Of the 2003-04 Budget Bill

TABLE OF CONTENTS

SETTING A CONTEXT

The State faces an extraordinarily difficult budget problem in 2003. To deal with it effectively, the Legislature must put the budget in a context that clarifies the problem and possible solutions.

Introduction. On February 3, the Legislature passed a package of bills to reduce current-year spending by $3 billion. The package also clarified that the Director of Finance may raise the Vehicle License Fee (VLF) by $4 billion during the relevant period. The package included Assembly Bills 4x, 6x, 8x, 10x, 11x and Senate Bill 10x. Taken together, these bills were the Legislature's initial response to the state's $26 billion deficit.

On March 3, the Senate Budget and Fiscal Review Committee expects to begin its regular subcommittee process.

THE GOVERNOR'S BUDGET PROPOSAL:
Progress since January 10 and Continuing Challenges for the Legislature

The Department of Finance estimates that the state starts the 2003-04 year with a carry-over *deficit* of over $4 billion. The Governor proposes a comprehensive plan for eliminating the entire deficit by June 30, 2004. Below, we describe

- The General Fund condition,
- The Governor's proposal, and
- Timing for legislative action on the Governor's proposals.

Describing the General Fund Condition

The Department of Finance estimates that General Fund revenues will total $69 billion in the budget year. This is five percent below current-year revenues.

Under the Governor's proposal, General Fund spending falls to $63 billion for 2003-04. This is nearly one-fifth lower than the estimated current-year budget. The magnitude of the reduction is without precedent.

After accounting for the carry-over deficit ($4.5 billion) and current-year encumbrances ($1.5 billion), the state would end the year with a surplus of resources over expenditures of about $500 million. Table 1 summarizes the General Fund condition if the Legislature adopted the Governor's proposal. (See page 20 for a condition statement adjusted for the realignment transactions.)

Table 1
Comparison of General Fund Resources and Expenditures
Unadjusted General Fund Condition
(does not assume the "Realignment" revenues and expenditures in 2003-04)
Dollars in Millions

	2002-03	2003-04 (proposed)	Change
Prior-Year Balance	-$2,133	-$4,451	109%
Revenues and Transfers	73,144	69,153	-5%
Total Resources Available	**$71,011**	**$64,702**	**-9%**
Expenditures	**$75,462**	**$62,769**	**-17%**
Resources-Expenditures	-4,451	1,933	
Encumbrances	1,402	1,402	
Reserve	***-$5,853***	***$531***	

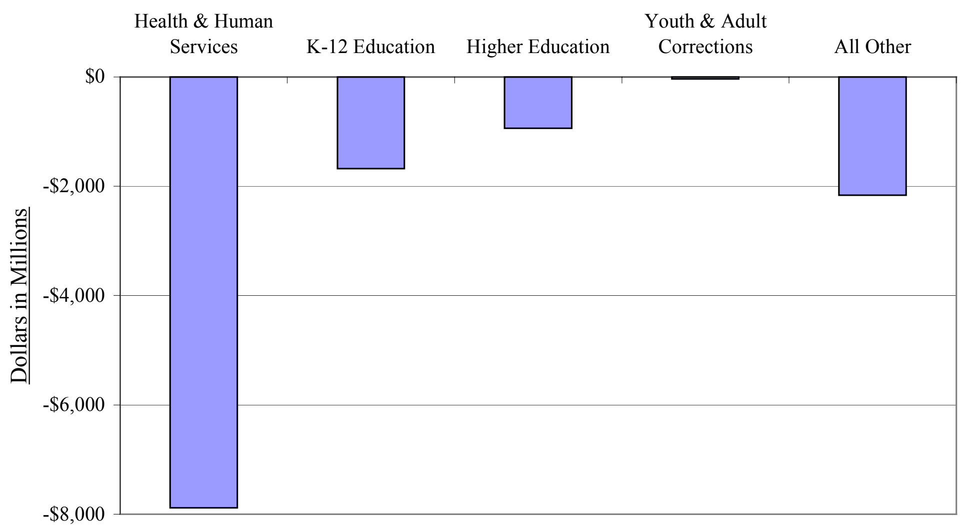
State Spending Significantly Reduced from Current-Year Levels. The Governor proposes to reduce General Fund expenditures from $75 billion in the current year to $63 billion in the budget year. This represents a 17 percent reduction in General Fund spending. As displayed in Graph 1, all areas of the budget received a reduction from current-year funding levels.

As proposed, Health and Human Services sustains the largest reduction, nearly $8 billion (a 34 percent reduction) from current-year levels. K-12 education falls by $1.7 billion (a six percent reduction). Higher Education is reduced by nearly $1 billion (a ten percent reduction).

Graph 1

Changes in General Fund Spending, by Major Spending Areas

Comparing 2002-03 with 2003-04 (Proposed)

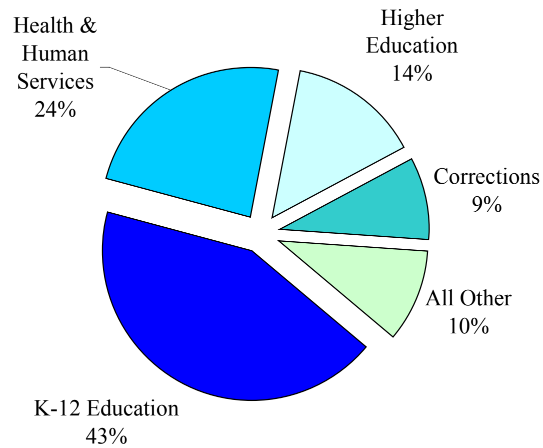


Governor Proposes To Concentrate General Fund Spending in Four Areas

Looking at the 2003-04 budget proposal, four policy areas account for 90 percent of General Fund spending. Graph 2 identifies the relative spending in these areas. Specifically, in the 2003-04 budget:

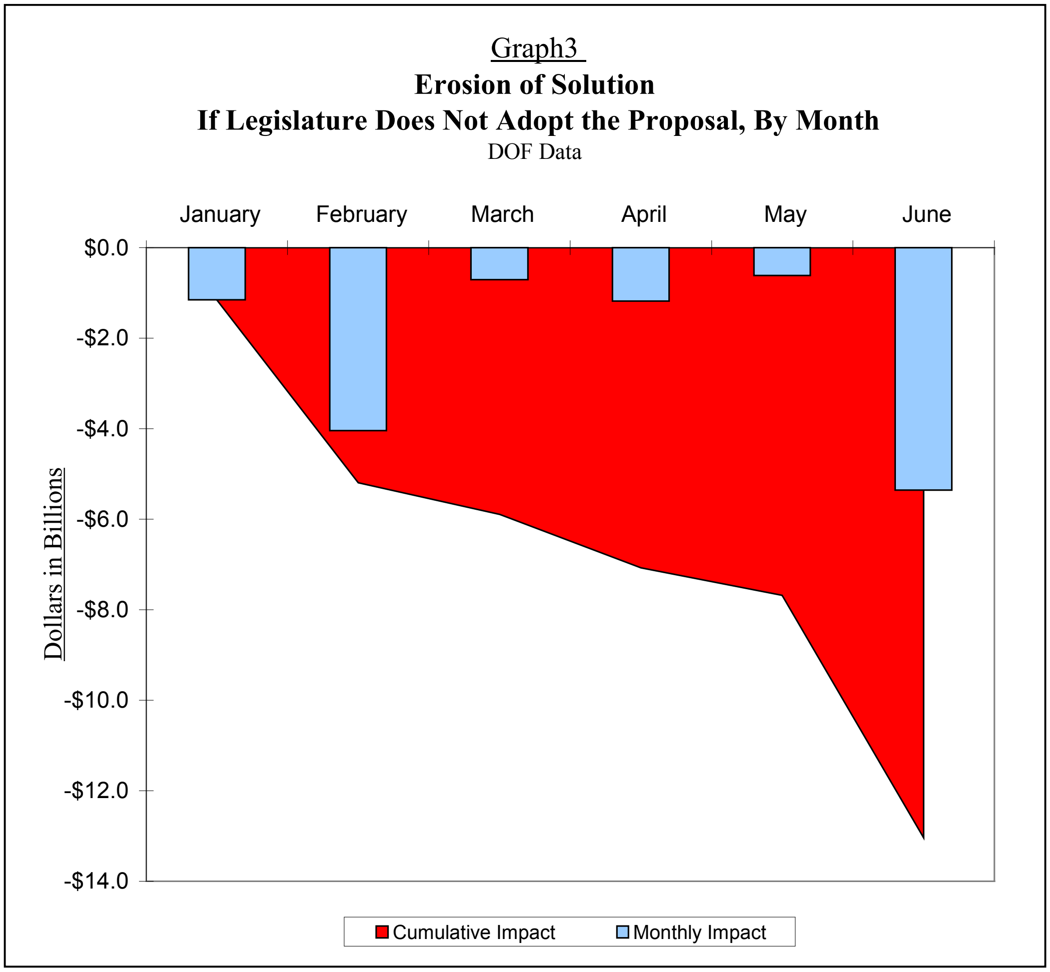
- K-12 Education receives $27 billion, accounting for 43 percent of General Fund spending,
- Health and Human Services receives $15.1 billion, accounting for 24 percent of the total,
- Higher Education receives $8.5 billion, accounting for 14 percent of the total, and
- Youth and Adult Corrections receives $5.6 billion, accounting for nine percent of the total.

Graph 2
Allocation of General Fund Spending
Governor's Budget
2003-04



Relating the December Revision to the January Budget Proposal. In December, the Governor proposed a package of current- and budget-year reductions. The Governor asked that the December Revision be considered as part of the First Extraordinary Session. By proposing early action, the Governor hoped to begin reducing spending in January, rather than July, thereby spreading the reductions over an 18 month, rather than 12 month, period. As modified on January 10, the early reductions generate current-year savings of $5.6 billion and budget-year savings of about $12.6 billion. Taken together, this package would halve the deficit identified by the Governor.

While early action on this proposal is important, not all statutory and budget decisions contained in the December Revision must be taken by January 31 in order to achieve the full savings proposed by the Governor. Throughout the six month period starting in January, there will be monthly losses if the Legislature does not act on a timely basis. Specifically, according to the Department of Finance, if the Legislature does not act on the December Revision by January 31, it will lose about $1.2 billion in solutions. Taking no action by February 28 will cost the state another $4 billion, for a total loss of $5.2 billion in solutions. Graph 3 summarizes the erosion of the solution over time. The bars in the graph represent the loss of solution if the Legislature does not act by the end of the month. The area in the background represents the cumulative loss by month.



Progress Since January 10. On February 3, the Legislature adopted a package of legislation which according to the Department of Finance provided savings of about $3.5 billion in both the current and budget years. The package also clarified that the Director of Finance had the authority to raise the Vehicle License Fee (VLF) under specified circumstances. If the Director were to use this authority, it would provide an additional $4 billion in budget savings. (The fate of this package was unknown at the time the committee published the *Overview*.) Relative to the Governor's estimate of the deficit, the action to date would have "solved" about one-third of the deficit.

DEFINING THE PROBLEM: THE STATE EXPECTS TO RUN CHRONIC BUDGET DEFICITS

If statutory law were left unchanged, the state can expect spending to exceed available General Fund resources for the foreseeable future. The resulting operating deficits--in excess of $15 billion annually--cannot be accommodated without major changes in law.

The deficits are deep and profound. Below, we discuss spending and revenue trends leading to the deficits, and describe how the Governor addressed the problem in his January 10 budget proposal.

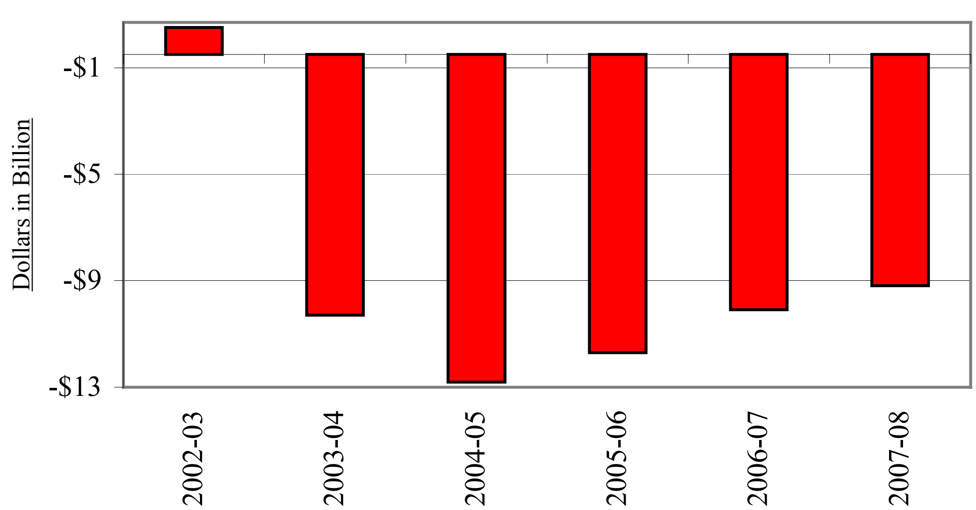
History: What Happened Last Year?

When the Legislature considered the budget last August, the Analyst estimated that the state would sustain a surplus of about $1 billion in 2002-03.

Graph 4

Chronic Deficits Were Forecast When Budget Passed

LAO Forecast (August 2002)



As displayed in Graph 4, the Analyst also made out-year estimates which showed that, starting in 2003-04, the state would run a General Fund operating deficit for each year, beginning with an operating deficit of about

$10 billion in 2003-04. Unless corrective actions were taken, it estimated that the operating deficit would rise to nearly $13 billion in the following year.

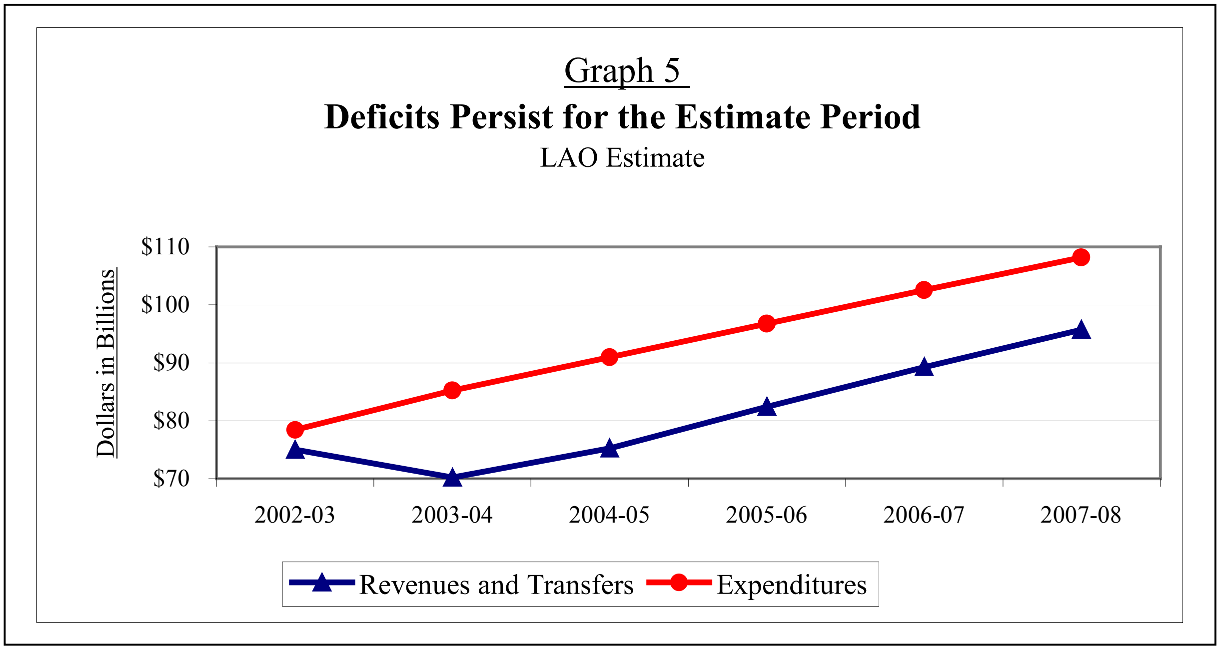
After August, the LAO Predicted a Higher Budget-Year Deficit. Since August, estimates of the current- and budget-year deficits have worsened. In November, the Analyst estimated that the state's *current-year deficit* would be about $6.1 billion. Of this amount, $4.1 billion is attributable to a loss in revenues and about $2 billion is attributable to higher-than-anticipated expenditures in the period ending June 30, 2003. Absent action by the Legislature in the current year, this deficit must be financed entirely in the budget year.

At the same time, the LAO raised its estimate of the *budget-year deficit* from $10 billion to $15 billion. Taken together, the LAO's estimates of the deficits have risen from a total of $10 billion to a total of $21 billion.

In January, the Analyst reported that the estimates are likely to change again. Although she has not revised her estimates yet, she expects that when the *Analysis of the 2003-04 Budget* is released on February 19 the estimate of the two-year deficit will increase by $5 billion. Of this increase, about $4 billion is the result of falling revenues and about $1 billion can be attributed to higher expenditures. Consequently, the Legislature should anticipate that it will have to finance an 18-month deficit of at least $26 billion.

> How Big Is the Deficit?
>
> In January, the Governor estimated that the 18-month deficit was $35 billion, while the LAO estimates about $26 billion. The LAO explains that the DOF estimate is higher in the following way:
>
> - ***$5 Billion Is "Definitional".*** DOF assumed a higher spending "baseline." DOF added certain costs into the baseline, then "cut" the baseline. For example, DOF includes paying all deferred local mandate reimbursements in the baseline, then propose deferring the payments. The LAO did not assume the full repayment of mandates in its baseline, so the LAO budget-year baseline is lower.
>
> - ***$4 Billion Is "Forecasting Differences."*** DOF forecast lower revenues and estimated higher caseloads than did the LAO.
>
> Next week, the Analyst will release a revised revenue forecast and expenditure estimate. At that time, the Legislature may consider whether the differences in the deficit are significant. If for example, the Legislature believes that budget-year revenues will be higher than those included in the Governor's budget, then the deficit problem—and solution—should be reduced accordingly.

Deficits Persist throughout the Foreseeable Future. According to the LAO, the deficits persist throughout the estimate period. As displayed in Graph 5, in each year through 2007-08, the state will run annual deficits of between $12 billion and $16 billion.



Deficits result from spending at rates greater than the revenue streams can support. Recent budget decisions and tax changes have contributed to the deficits. Below, we describe recent spending and revenue trends.

Trends in General Fund Spending

Since 1998, General Fund spending has increased from $58 billion to $77 billion, an increase of about $19 billion (33 percent). Graph 6 displays the growth by policy areas, as estimated by the Legislative Analyst's Office (LAO). Education programs received the greatest amount of the increase. The Legislature allocated $7.1 billion to Proposition 98-funded education programs. Other education spending, primarily spending on Higher Education, rose by an additional $2.1 billion. As such, increased spending on education programs account for $9.2 billion—nearly half—of the $19 billion increase in spending since 1998.

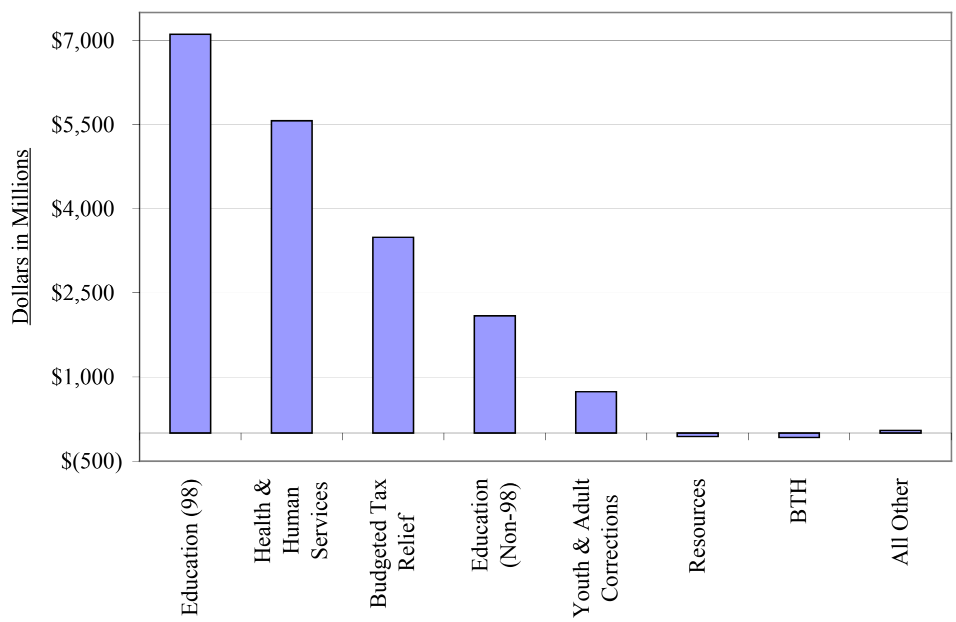
Health and Human Services received $5.6 billion of the increased General Fund spending (about 30 percent of the total growth). Most of this increase is attributed to changes in caseload and inflation. Over the period, the Legislature increased Medi-Cal provider rates, extended cost of living adjustments and expanded eligibility for the Healthy Families program.

Since 1998, budgeted tax relief grew from $931 million to $4.4 billion, and accounts for 18 percent of the total growth in expenditures. (Budgeted tax relief are tax reductions which are *appropriated* in the budget act. The costs of tax relief not appropriated—like the Manufacturer's Investment Credit (MIC) and Net Operating Loss (NOL)--are "off-budget," and they do not appear in budget totals.)

Graph 6

Change in General Fund Spending 1998 through 2002

LAO Estimates

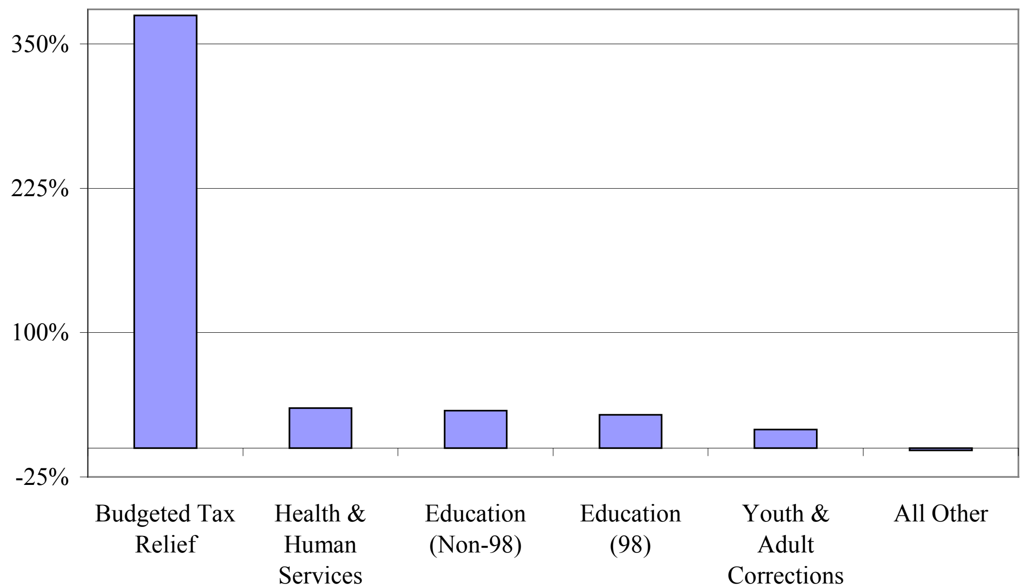


The growth in spending for budgeted tax relief is primarily associated with the costs of backfilling local governments for their revenue losses associated with the reduction in the Vehicle License Fee (VLF).

Corrections spending grew by over $700 million, accounting for about four percent of the growth over the period.

General Fund expenditures for resources, environmental protection, business, transportation and housing fell during the period.

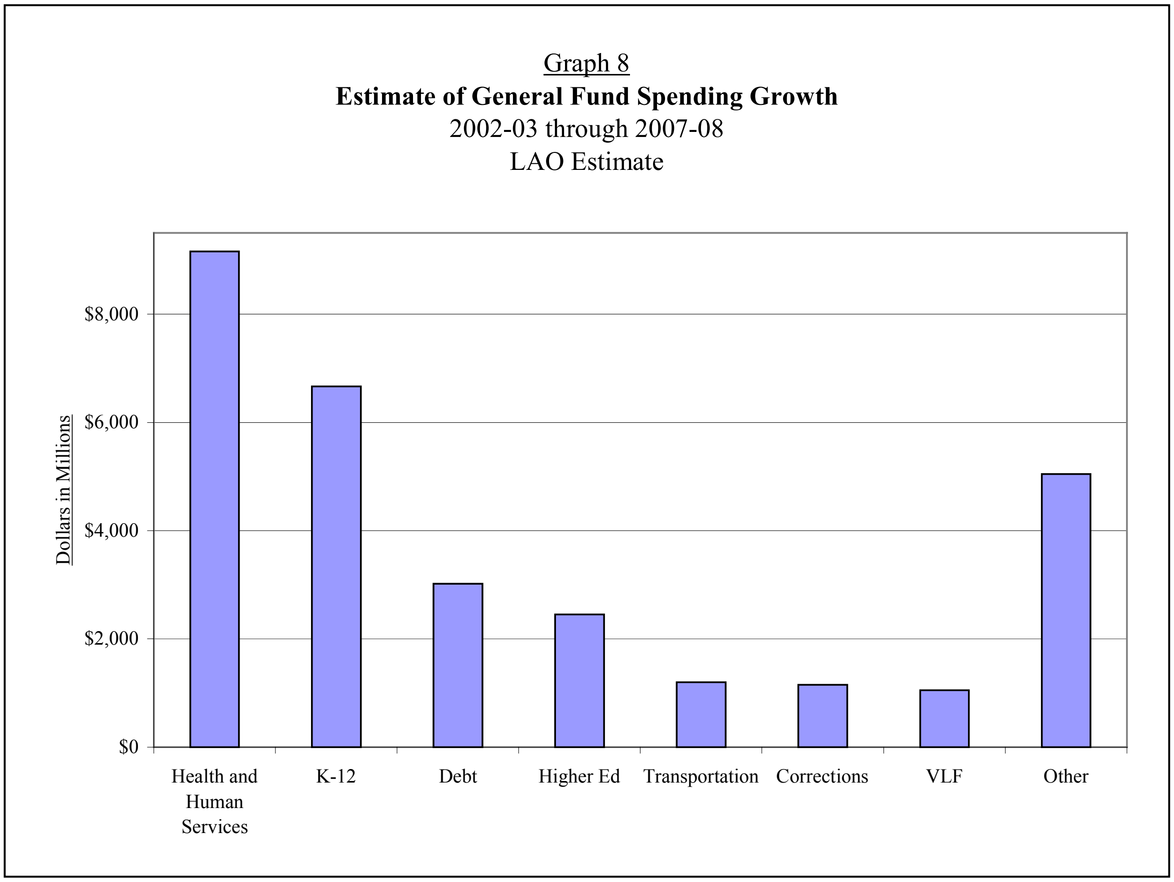
Graph 7
Rate of Growth in General Fund Expenditures
1998-99 through 2002-03



An alternative way of looking at the spending changes since 1998 is to consider the rates at which programs grew. Though education, health and human services programs received the greatest *amount* of increased funding, budgeted tax relief sustained the highest growth *rate*. Budgeted tax relief has increased by 375 percent over the four year period, while education, health and human services programs grew by about 33 percent. Corrections spending grew about 16 percent. The rest of the budget contracted. Graph 7 compares the growth rates by major program area.

The LAO Spending Estimates. In November, the LAO forecast spending for the period ending June 30, 2008. The estimates, which assume no change in substantive law, identify about $30 billion in new costs, a five-year growth rate of about 40 percent. The estimates, which assume no program expansions, merely account for changes in population and inflation. In Graph 8, we display the estimated growth in General Fund spending, by policy area.

The policy area with the greatest amount of growth will be Health and Human Services. The Analyst expects these programs to grow by about $9.2 billion, a 42 percent rate of growth. In this policy area, the largest increase in spending would



be associated with the cost of maintaining Medi-Cal benefits. The Analyst estimates that state cost for benefits will increase by about $5.1 billion between 2002 and 2007. Costs will also increase rapidly for the provision of services under the SSI/SSP and IHSS programs as well. Graph 9 breaks out the estimate of increased spending for the Health and Human Services.

The Analyst expects K-12 education spending to grow by $6.7 billion and higher education spending to grow by $2.4 billion, for about a $9.1 billion increase over the next five years.

Debt service costs will also account for a large share of growth in state spending. In recent years, the state has increased its borrowing significantly. Some of this is attributable to the costs of paying for the General Obligation bonds which were approved by the voters for school construction and resource acquisition. It is also associated with an increased reliance on lease-revenue bonds for accommodating the state's capital needs. In addition, as part of last year's budget compromise, the Treasurer restructured state debt which provided some short term budget relief, but increased the state's long-term costs.

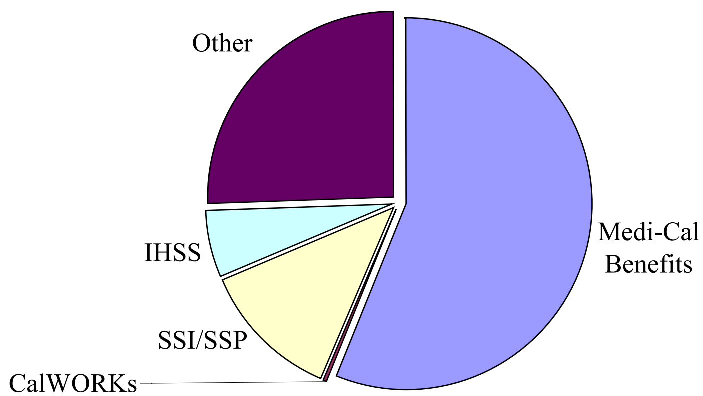
Graph 9

Estimate of General Fund Spending Growth

Health & Human Services Programs

2002-03 through 2007-08

LAO Estimate



Because the Legislature committed to increasing support for transportation, General Fund costs for transportation will increase by $1.2 billion in 2007-08.

The Analyst also expects that the costs for the VLF backfill and Corrections will increase by about $1 billion each in the next five years.

Other programs, including the costs for the General Fund support of employee compensation and local government mandates, will increase state costs by about $5 billion.

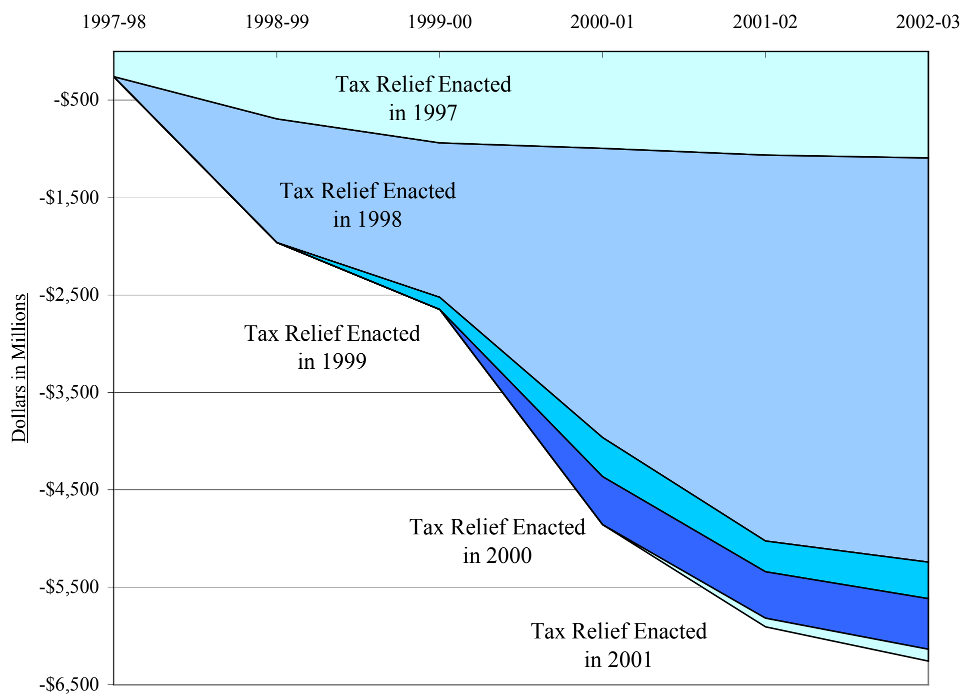
Revenue Trends

The Legislature reduced taxes between 1997 and 2001. For the 1997-98 fiscal year, the Legislature's actions reduced taxes by $260 million. In each subsequent year, the tax relief provided by the 1997 changes reduced annual taxes by an even greater amount.

The Legislature approved additional tax reduction measures in 1998, 1999, 2000 and 2001. According to the Analyst, by the current and budget years, the relief provided in legislation enacted since 1997 had an annual value of $6.3 billion and $6.5 billion respectively. Graph 10 illustrates the effect of the tax changes enacted in the five-year period ending in 2001. Cumulatively in six years, the tax relief enacted between 1997 and 2001 reduced taxes by over $28 billion. The effects of the tax reductions enacted since 1997 were offset in part by a temporary tax increase enacted in 2002. As part of the 2002 budget compromise, the Legislature temporarily suspended the application of the Net Operation Loss (NOL) and other tax relief, and raised taxes by $2.8 billion and $1 billion in 2002-03 and 2003-04, respectively.

In subsequent years, the 2002 tax package provides for on-going reductions in taxes.

Graph 10
General Fund Effects for All Tax Measures Enacted Between 1997 and 2001
1997-98 through 2002-03

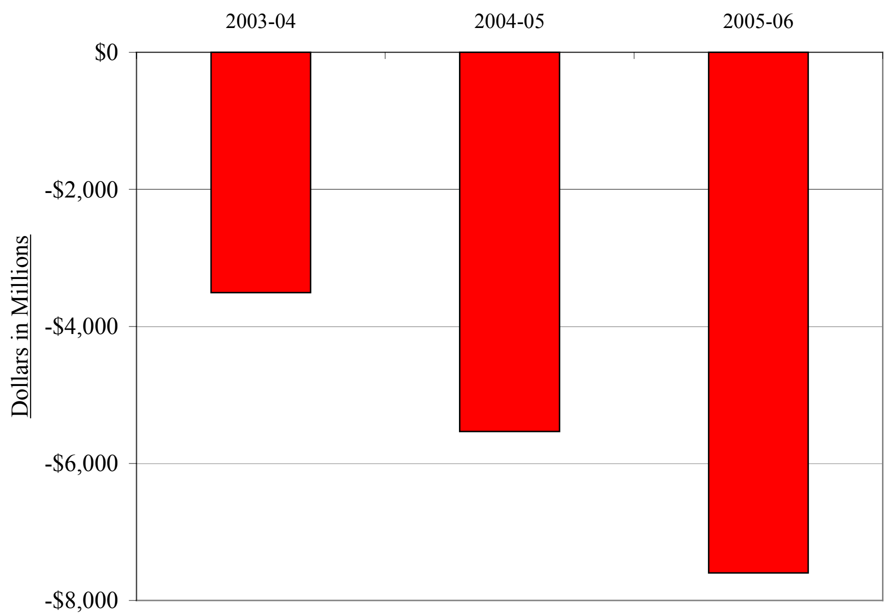


LAO Estimates

Tax Measures Enacted Between 1997 and 2002 Reduce Annual Tax Burdens by $7.6 Billion. Taken together, the net effect of all tax measures enacted between 1997 through 2002 will reduce tax burdens by $3.5 billion in the budget year. In 2005-06, when the temporary tax increases expire, tax measures enacted between 1997 and 2002 will reduce revenues by $7.6 billion. Graph 11 illustrates the net effects of all tax measures enacted since 1997.

For a more extensive analysis of the recent tax changes and their fiscal effects, please see the revenue discussion in the section of this report entitled "Selected Major Issues."

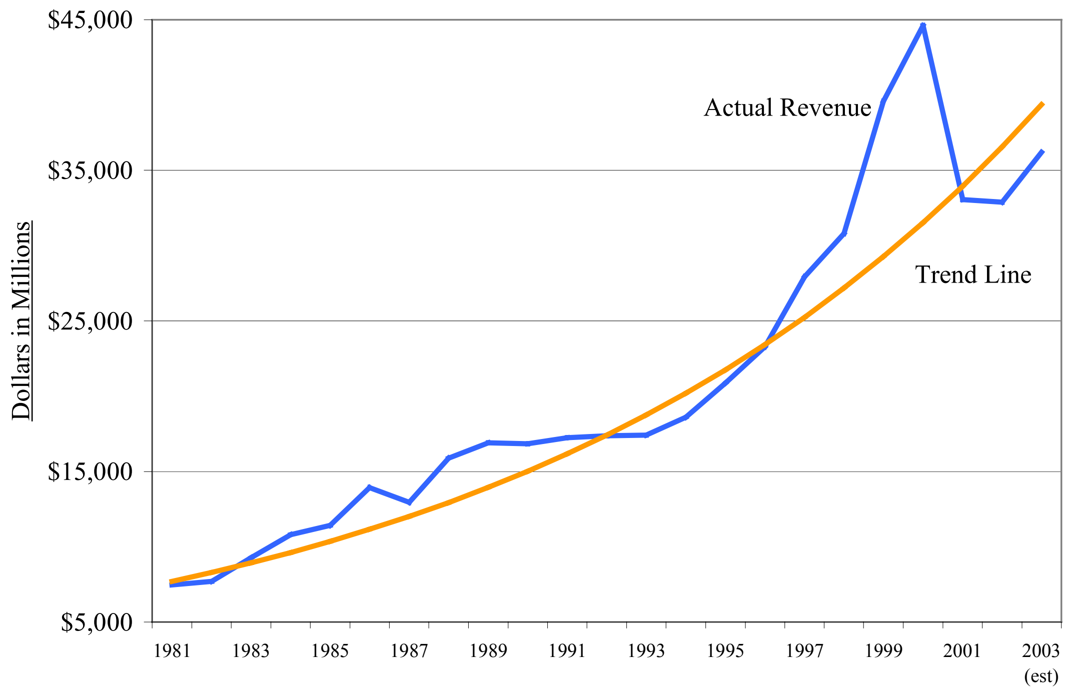
Graph 11
General Fund Effects
of All Tax Measures Enacted between 1997 and 2002
2003-04 through 2005-06
LAO Estimates



Did the State's "Revenue Bubble" Burst in 2001? Between 1996 and 2000, the state experienced rapid growth in its personal income tax (PIT) revenue base. In those years, PIT revenues grew from $23.3 billion to $44.6 billion, a 92 percent increase. This growth was fueled by increased taxes on capital gains and stock options.

While the state experienced an unprecedented increase in income tax revenue, tax analysts were not certain whether the tax base had permanently or temporarily expanded. The nature of the expansion is important for determining whether the state could afford to make a permanent increase in programs or reduction in taxes. For example, if the base were permanently expanded, then the Legislature could expect an on-going source of higher revenue. On the other hand, if the increase in revenues were a temporary expansion of the tax base, then the Legislature should expect to return to a lower level of revenues in the future.

Graph 12
Personal Income Tax Over Time
1981 through 2003 (estimated)



It now appears that the extraordinary revenue increases achieved in 1996 through 2000 were a temporary and unsustainable increase in the tax base. Since 2000, PIT revenues have dropped significantly. The amount collected in the 2001 and 2002 tax returns was lower than the amount collected in 1999, and only slightly more than the amount collected in 1998.

The extraordinary growth in the tax base in the late 1990's may have been a "bubble" which burst in 2001. The "bubble" is illustrated in Graph 12. The blue line plots actual PIT revenues. The orange line, plotting a 7.7 percent growth rate from amount collected in 1981, shows a constant-growth trend line. As displayed in the graph, the major variation from the trend line occurs during the period 1996 through 2000, forming a "bubble," where actual revenues are significantly above the trend line.

If the capital gains phenomenon of the late-1990s turns out to be a one-time event, then the state's long-term PIT revenues will more likely attain growth rates similar to the trend line displayed in Graph 12, rather than those actually achieved in the four-year period starting in 1996.

Putting the Governor's Solutions in Context

The contraction of the PIT tax base, the growth in programs and the reduction in tax burdens created an on-going budget deficit. The Legislature first grappled with this deficit in 2001. In the budget year, the state faces a carryover deficit of nearly $5 billion and the persistent on-going deficits. To address the one-time and on-going deficits, the Governor proposed the following budget adjustments in the 18-month period starting January 1, 2003:

- ***Program Reductions.*** The Governor cuts programs by nearly $14 billion. Of this amount, about $5.5 billion is associated with the current-year budget and must be enacted before June 30, 2003. We assume the entire budget-year amount can be scored as a permanent reduction.

- ***Revenues.*** In the current year, the Governor proposes an increase in revenues of $200 million and $10.1 billion in the budget year. Of these increases, $8.2 billion would finance realignment. Presumably, the entire budget-year amount is permanent.

- ***Local Government Shifts.*** By reducing the VLF backfill, shifting revenues from redevelopment agencies and eliminating certain subventions, the Governor shifts about $5 billion of the problem to local governments. This total does not include mandate deferrals. (The deferrals are included in the description below under loans.) About $3.3 billion of this shift reduces on-going General Fund deficit.

- ***Fund Shifts.*** The Governor proposes to increase student fees in higher education, trial courts, resources programs and the Department of Industrial Relations. He proposes shifting the costs of child care to the federal government and moves capital outlay projects to a lease-revenue basis. These shifts provide $2.2 billion in solution. About $1.4 billion is attributable to the budget year. Presumably most of the budget-year solution provides permanent deficit reduction.

- ***Loans and Borrowing.*** The Governor proposes to defer payments on mandates and retirement contributions for a budget year savings of about $3.3 billion. None of this relief provides permanent, on-going deficit relief.

Table 2 summarizes the Governor's proposal by fiscal year.

Because the Legislature expects to address both the one-time carry-over deficit and the chronic deficit, it will be important for the Legislature to keep a tally of one-time and on-going reductions. While staff have not completed their analysis of the Governor's budget, some preliminary conclusions can be drawn.

The current-year proposals are, by their nature, one-time in their impact on the out-year deficit. They can all be scored as addressing the carry-over deficit. Assuming all the program reductions, taxes and shifts in the budget year are permanent, the Governor's proposal provides $24 billion in on-going budget relief.

Table 2
Budget Proposals Addressing the Deficit
Impact in Current and Budget Years
LAO Estimates
Dollars in Billions

	Current Year	Budget Year	Totals
Program Reductions	$ 2.7	$ 11.0	$ 13.7
Taxes, Transfers and Other Revenues	0.2	10.1	10.3
Local Government Shifts	1.8	3.3	5.1
Fund Shifts	0.8	1.4	2.2
Loans and Borrowing		3.3	3.3
Totals	**$ 5.5**	**$ 29.1**	**$ 34.6**

Accounting for the Realignment Transaction in the General Fund Condition Statement. The General Fund condition changes if the realignment proposal is accounted for in the condition statement. By including the Governor's realignment proposal in the statement, both expenditures and resources increase. This adjustment facilitates comparisons with the current year and may be a more appropriate reflection of the tax change.

The Governor proposes to shift responsibility for several state programs to local governments. He would eliminate about $8 billion from state General Fund spending and make local governments responsible for administering these programs. At the same time, he proposes to raise state-levied taxes by about $8 billion. The new tax revenues would be deposited in a special fund to be earmarked for allocation to local government.

If the General Fund condition, as displayed in Table 1, were adjusted to reflect the realignment transaction, revenues and spending would be significantly increased. Specifically, after accounting for realignment described in the *Governor's Budget Summary*, revenues increase by three percent between the current year and the budget year. Expenditures fall by six percent. Please see Table 3 for a display of this adjusted General Fund Condition.

Table 3
Comparison of General Fund Resources and Expenditures
Adjusted General Fund Condition
(Assumes the Realignment Transaction)
Dollars in Millions

	2002-03	2003-04	Change
Carry Over Deficit	-$2,133	-$4,451	
Revenues and Transfers	73,144	69,153	
Realignment Revenues		8,334	
Total, Resources	**$71,011**	**$73,036**	2.9%
General Fund Expenditures	$75,462	$62,749	
Realignment Expenditures		8,154	
Total, Expenditures	**75,462**	**70,903**	-5.9%

HOW CAN THE LEGISLATURE PROCEED?

The Senate's review of the budget typically begins the first week of March. The budget subcommittees work with the Administration and the Legislative Analyst's Office to develop an agenda for each department in the budget.

As the subcommittees begin their work, the Legislature must consider the following broad questions:

- *Determine How Quickly To Re-Balance the Budget*. The structural deficit is deep and profound. The Legislature must consider whether it is most prudent to eliminate the accumulated deficit entirely during 2003-04 or to reduce the deficit in stages over several years.

- *Retire the Current-Year Deficit*. The state starts the new fiscal year with a carryover deficit of about $4.5 billion. The carryover deficit can be addressed with either one-time budget cuts (such as reductions to capital outlay projects) or with on-going reductions.

- *Address the Chronic Deficit*. To address the chronic deficit averaging around $15 billion, the Legislature must take action to reduce annual spending by $15 billion, raise annual tax revenue by $15 billion or use a combination of spending cuts and tax increases to close the gap between expenditures and revenues. The chronic deficit cannot be addressed with one-time solutions.

- *Consider the Circumstances when Short-Term "Solutions" Create Long-Term "Problems."* Based on the Analyst's estimates, the state cannot expect that the state's fiscal condition will improve in the foreseeable future. Even if the economy were to improve, the Legislature would still face chronic deficits.

  Solutions which shift costs beyond June 30, 2004 may help balance the 2003-04 budget, but exacerbate the problem in outyears. The Governor's proposal to issue a pension obligation bond is such a measure. Under the proposal, the state would sell $1.5 billion in *taxable* bonds. With the proceeds of the sale, the state would make its payment to the state's retirement systems. The bonds, carrying an interest rate of six percent (about three times the interest paid on the energy bonds issued last Autumn), the state would repay the bondholders over a 20 year period. This proposal provides budget relief in the current year but costs the state for the next 20 years.

Practically speaking, before the subcommittees begin their work, the Senate may want to answer the following questions about how the subcommittees should proceed:

1. *Will There Be a Revenue Increase?* To balance the budget, the Governor proposes increasing taxes by $8.2 billion, raising fees by millions of dollars and assessing gaming interests $1.5 billion. To what extent will the Legislature increase revenues?

2. *Should Local Governments Participate in the Solution?* The Governor proposes shifting about $5 billion in revenue from local government to state activities. The shifts are from local discretionary revenues. To what extent will the Legislature act to reduce local discretionary revenue?

3. *Can the Federal Government "Help"?* In the early 1990s, Governor Wilson assumed that the federal government could provide additional assistance to the state to offset the cost of federal immigration policy. Under what circumstances is it likely that the federal government will provide greater assistance to California? For example:

   - Can the state restructure its programs so it can increase federal reimbursements for state costs?

   - Should the Legislature adjust the state tax structure to increase those state taxes which are deductible on the federal income tax and lower the tax which are not deductible?

To the extent the Legislature cannot increase revenues, shift costs to locals or secure additional federal assistance, then it must consider reducing programs more than proposed by the Governor.

Analysis prepared by John Decker, Senate Budget and Fiscal Review

SELECTED MAJOR ISSUES

DOWNSIZING THE CALIFORNIA YOUTH AUTHORITY: CHALLENGES AND OPPORTUNITIES

With a proposed annual budget for 2003-04 of $414 million, the California Youth Authority (CYA) operates eleven institutions and four fire camps and provides parole supervision for some of the state's most serious juvenile offenders ranging in age from 12 to 25.

In the last seven years, the CYA has experienced dramatic reductions in its caseload. In 1996, more than 10,000 wards were incarcerated at CYA. The ward population is now projected to decline to 5,340 by June 2003. While CYA's population has declined by over 46 percent since 1996, the department's expenditures have failed to decline at a comparable pace. Indeed, expenditures have dropped by only 26 in inflation adjusted dollars over this period. As CYA's ward population has downsized, many fixed costs have retained intact. In addition, public scrutiny, litigation and legislative concerns have fueled the demand for additional funding to improve treatment programs.

When reflecting on these trends in recent budget deliberations, legislators raised concerns about CYA's response. This essay evaluates the fiscal and policy implications of the population changes at CYA. Specifically:

- To what extent has the population dropped, and what are the most likely factors for the decline?
- How has CYA responded to the population changes?
- What options can the Legislature exercise to reduce costs or increase accountability?

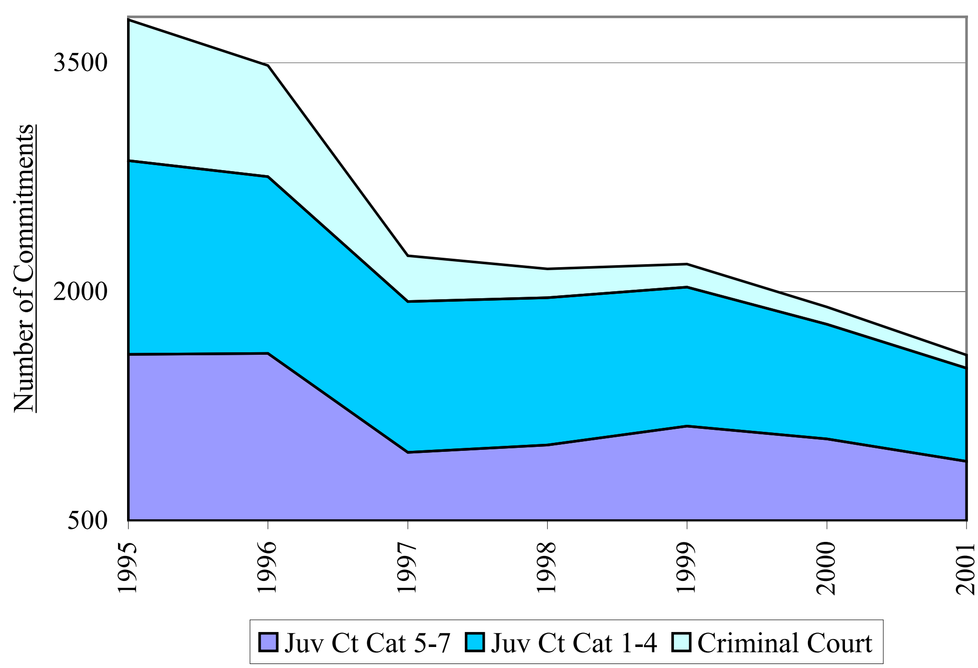
Population Decline Significant

Looking at CYA new admissions – the institutions' "front door" -- juvenile and criminal ("M" cases) commitments to CYA have dropped by nearly 60 percent since

1996 from 3,800 to 1,600. Much of this decline has been influenced by policy changes adopted by the Legislature and the Governor. Significantly, this decline has occurred across all offense categories – not just among lower level offender categories.

As illustrated by Graph 1, the decline since 1995 for category 1-4 offenders – committed for more serious crimes – was 52 percent. Youthful offenders in categories 5-7 – committed for relatively less serious crimes – has declined by 40 percent.

Graph 1
Juvenile & Criminal Court ('M' Cases)
Commitments to CYA
1995-2001



Causes

Several factors appear to be contributing to the continuing decline in CYA's ward population, including: (1) the transfer of criminal court "M" cases to the

Department of Corrections (CDC); (2) the imposition of "sliding scale" fees on counties; (3) the development of local prevention programs and detention alternatives; (4) the decline in juvenile crime; and (5) the perception by judges that CYA lacks adequate and appropriate treatment.

1. ***Transfer of "M" Cases.*** In June of 1994, 16 percent of CYA's population was comprised of persons who were convicted in criminal court when they were under the age of 21. These so-called "M" cases were ordered by the court to serve their time at CYA. In 1996, the law was changed to limit the housing of "M" cases in CYA to only inmates under the age of 18. As a result, 824 inmates were transferred that year from CYA to CDC. By 2001, only 74 "M" cases were admitted to CYA.

2. ***Sliding Scale Fee Legislation.*** Prior to 1995, counties paid the state a negligible amount -- $25 per offender per month – to commit wards to CYA. In 1995, legislation was enacted to establish a new fee structure, which provided incentives for counties to treat less serious offenders in county-level placements, thereby reducing their dependence on costly CYA commitments. Legislation enacted in 1998 froze the per capita costs on which the sliding scale fees are based at the levels in effect on January 1, 1997. Under the sliding scale monthly fee schedule, counties pay 100 percent of the average cost for category 7 wards ($2,600), 75 percent for "category 6 wards ($1,950), and 50 percent for category 5 wards ($1,300). In addition, the fee for category 1- 4 wards has increased from $25 to $150 per month. Counties now pay $52.1 million annually for their commitments to CYA. Note: The Governor's 2003-04 budget assumes enactment of legislation to adjust the sliding scale fees to reflect inflation. This would increase county costs by $7 million.

3. ***Development of Local Prevention Programs and Detention Alternatives.*** While the sliding scale fees provided a strong fiscal incentive to treat juvenile offenders locally, state policies also have sought to strengthen local juvenile justice programming by encouraging an array of alternatives and graduated sanctions. State funding for Juvenile Justice Challenge Grants and the Repeat Offender Prevention Program has helped counties develop effective approaches to juvenile crime and intensive intervention for high risk, chronic offenders. In 2000, the Legislature established the Juvenile Justice Crime Prevention Act to provide counties with stable funding to maintain and expand programs that work to reduce juvenile crime. In addition, since 1997-98, almost a half billion dollars in state and federal funds have been dedicated to assist counties in renovating and constructing local juvenile facilities. As a result, counties are keeping more of

their offenders locally. Kern County, for example, sent 162 wards to CYA in 1995; in 2001, the county sent only 19.

4. ***Decline in Juvenile Crime.*** California has experienced a remarkable decline in serious juvenile crime, thereby reducing the pool of potential offenders going to CYA. For example:

   - Between 1991 and 2000, juvenile arrests for homicide fell from 969 to 160.

   - Between 1990 and 2001, the rate of juveniles committing felony offenses dropped by 47 percent (compared to a 25 percent decline for adults during the same period.)

   The number of juveniles booked and detailed for serious, violent crimes (Section 707(b) offenses) dropped by almost 50 percent since 1999.

   Although California's investment in the local juvenile justice system has influenced the decline in juvenile crime, other factors have also contributed to this trend, which has been experienced across the country. These factors include, among others, changes in demographics, the economy, gang truces, and alternative criminal justice strategies.

5. ***Judicial Perceptions That CYA Provides Inadequate and Inappropriate Treatment***. In recent years, CYA has become the subject of litigation and intense public scrutiny concerning its conditions of confinement and institutional operations. The Inspector General has investigated and confirmed abuses and management deficiencies consistent with what has been reported publicly. During the past two years, CYA appears to be making concerted efforts to address its many problems. Still, the difficulties faced by the department continue to be extensive, including: CYA's inability to effectively handle gang problems that appear to increasingly interrupt institutional operations; the significant number of wards on restricted programming who are not receiving mandated education services; the lack of adequate formal treatment for sex offenders and drug addicted wards; and an overall inadequacy of mental health services.

Many Probation Chiefs and their staff – who make placement recommendations to the juvenile court -- are increasingly concerned about these conditions at CYA and are willing to send offenders to CYA only if all local alternatives have failed or are unavailable. It is acknowledged that many juvenile court judges -- who have the ultimate placement responsibility – have similar concerns. Moreover, some judges have also raised concerns about the length of time wards stay at CYA. Under current law, judges commit wards to CYA, but it is the Youthful Offender Parole Board (YOPB) that determines how long the ward stays and what treatment is ordered. The YOPB short circuits accountability for CYA wards, increasing judicial frustration and reluctance to send juvenile offenders to CYA in the first place.

The CYA Struggles to Respond

CYA's population has declined by over 45 percent since 1996, but the department's expenditures have not declined at nearly the same rate (expenditures have declined by 26 percent in inflation adjusted dollars over this same period). During this same period, public scrutiny, litigation, and legislative concerns have sought additional funding for improved treatment programs.

1. ***CYA has closed individual living units across the state, instead of closing entire institutions. As a result, per capita costs at CYA have soared.*** Instead of closing institutions to address the declining population, CYA has closed individual living units at each institution. As of November 2002, 24 living units were closed across the state. This policy choice prevents CYA from gaining any of the potentially significant cost savings associated with consolidation and forces the department to continue supporting its full infrastructure and overhead with a smaller budget. As CYA's ward population continues to drop, the average institution cost per ward (adjusted for inflation) has steadily risen from $43,500 in 1996 to nearly $66,000 by December 2002

2. ***CYA has increased its spending on mental health treatment programs over the past few years***. CYA has increased its spending on mental health services and treatment programs over the past few years in response to a growing recognition that many wards sent to CYA have complex mental health issues (also reflecting a lack of county-level facilities and programs for this population). A 2002 report by Stanford University researchers identified extremely high prevalence rates of psychiatric problems among CYA wards and parolees, and significant understaffing in mental health care services. The report also made specific recommendations for an appropriate continuum of care. To address this need, CYA increased mental health staffing at three institutions over the past two fiscal years. In his proposed budget, the Governor has included $1.45 million to increase staffing for CYA's correctional treatment facilities and $3.4 million for a new 20 bed inpatient mental health facility to be jointly run by CYA and DMH. Despite the recent augmentations, CYA is still far short of meeting the mental

health needs identified by the Stanford report.

3. ***CYA has cut spending in education because their education budget is driven by a formula devised years ago. As a result of this out-of-date budget formula, CYA is unable to provide adequate education services today.*** Because so much of CYA's budget is population driven, the department has experienced a rapid reduction in some of its funded staffing positions. This is perhaps most evident in the education area, where funding is based on a formula of ward-to-teacher ratios devised decades ago, which is no longer reflective of the department's needs. For example, when the baseline for the education formula was determined, CYA did not provide education to wards on restricted programming. Today they do, but the formula has never been adjusted to include these wards. Theoretically, CYA's population could drop to a point where they would not be budgeted for any teachers, but they could still have close to one thousand wards needing education.

4. ***CYA has reduced spending on parole and aftercare services during the last fiscal year. As a result, CYA may experience higher rates of recidivism.*** To achieve short term savings, budget reductions were adopted that reduced parole and aftercare services. However, research suggests that aftercare services and successful reintegration into the community may be the key components to reducing recidivism. Therefore, while the department may be able to "save" some dollars in the short term by cutting aftercare programs, there may be longer term costs in terms of increased recidivism rates.

Legislative Directive to Downsize

In 2002, legislation was enacted as part of the budget requiring CYA to prepare by November 1, 2002 a written plan to close at least three facilities by June 30, 2007. CYA also is required to close at least one facility pursuant to the plan by June 2004. In addition, Supplemental Report Language was approved requiring CYA, in consultation with the Legislative Analysts Office and the State Department of Education, to review their education funding formula.

As of January 10, 2003, these required reports have not been provided to the Legislature.

Other Options to Improve CYA and Enhance California's Juvenile Justice System

- *Realignment*. This strategy suggests that cost efficiencies and improved outcomes can be achieved by "realigning" program and fiscal responsibilities. In the case of the juvenile justice system, California maintains a bifurcated state-county approach in which the state operates the CYA for the most serious offenders while the counties – mostly probation departments – supervise the rest. In past years, the Legislature has considered proposals to realign juvenile justice programs at the county level. This could be accomplished through a phased in process that transfers to counties the state dollars that are now expended for CYA; counties could then use their resources to contract with CYA for juvenile placements that meet local needs. Any funds not used for state placements could be used by counties for community based programs.

- *Eliminate YOPB*. SB 1793 (Burton) from the 2001-02 session proposed to eliminate YOPB. Eventually, although it was narrowed to shift only length-of-stay and treatment decisions to the juvenile court, the bill was vetoed. CYA would be a more responsive state agency if it were reconnected to its "consumers" – that is, local governments and judges. By shifting parole and treatment order responsibilities to courts, CYA would have a direct link to the source of its commitments rather than a "middleman" state agency. In this way, CYA would be challenged with the kind of marketplace incentives that would lead to more effective correctional treatment and programming for youthful offenders.

- *Retool CYA as a Service Provider to Counties*. CYA could have the infrastructure to provide specialized services which counties cannot affordably provide themselves. Juvenile offenders requiring intensive mental health services, sex offender treatment and other specialized treatment beyond the capacity of county-based services might be handled more effectively if CYA was refashioned to provide contract services to county consumers.

- *Expand the Availability and Use of Community Programs for Drug Treatment and/or Mental Health Services.* Community-based substance abuse treatment programs can be more cost-effective than institution-based programs. For some juvenile offenders, effective local drug treatment or mental health service programs can be at least as successful in meeting treatment needs without risk to public safety.

Trends suggest that CYA's population will continue to decline. This affords the Legislature with an opportunity to reduce costs . However, the Legislature should also consider strategies that can improve long term public safety by refocusing on treatment services and greater accountability.

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CHILD CARE AND DEVELOPMENT

In December, the Governor proposed to eliminate stage three child care. This proposal ends subsidized child care services for certain former CalWORKs participants. This essay provides background on the state's child care programs, outlines the Governor's proposal and outlines alternatives to the proposal.

Background. Under current law, families remain eligible for subsidized child care as long as three conditions are met:

- The parent or parents are in the work force,
- The family's income is at or below 75 percent of the state median (by family size), and
- The youngest child in care is no older than 13 years of age.

When the Legislature established the CalWORKs program in 1997, it provided three stages of child care services for families participating in welfare-to-work programs.

Stage one is roughly that time period when the cash-aid recipient participates in initial CalWORKs activities and looks for work. The county administers these stage-one funds. For the current year, the California Department of Social Services (DSS) reports that stage one child care enrolls 75,300 children from 39,600 families, with a budget of $497.1 million. (Education Code §8351 establishes stage one.)

Once participants' schedules stabilize and they are in the labor force – or when recipients are transitioning off cash aid, they receive ***stage two*** services: these funds are administered by local child care and development programs under contract with the California Department of Education (CDE). CDE's current-year budget for stage two is $622.9 million; an additional $15 million goes to community colleges. CDE reports that approximately 104,000 children from 58,000 families receive stage-two care daily. (Education Code §8353 establishes stage two.)

In addition, there is a ***reserve account for stages one and two*** of $101.5 million that is divided and distributed to counties and to child care agencies on an as-needed basis when the year's enrollment patterns become clear.

When a parent leaves cash aid and depends entirely on low-wage employment, the child care services come under the rubric of ***stage three***. In the current year, its budget is $236.3 million. CDE reports that 51,000 children from 28,000 families are in care. (Education Code §8354 establishes stage three.)

Table 1
Budget and Enrollment in Stage Three
Dollars in Millions

Stage	Budget	Enrollment: Children	Enrollment: Families
One	$ 497	75,300	39,600
Two	638	104,000	58,000
Three	236	51,000	28,000
Reserve	102	unknown	unknown
Total	$ 1,473		

There are aspects of this structure that are important to note. These divisions among the three stages are not hard and fast. The Legislature purposely gave *flexibility to counties and child care agencies* regarding when to move a child from one stage to another. When these moves occur, the family should feel no effect. Their child care arrangements should remain the same. Counties can determine when to move a family from stage one to stage two; the community agencies managing stage two and stage three determine when to shift families to the next stage.

The Governor's Mid-Year and Budget-Year Proposal. In December of 2002, to save $100 million between March and June 30 of 2003, and an additional $400 million in the budget year, the Governor proposed to eliminate stage three care. This proposal ends subsidized child care services for former CalWORKs participants who have been off cash aid due to employment for 24 months or more, even though they would otherwise qualify for partial child care subsidies because of their low incomes.

Low-income working parents who have been off cash aid for more than 24 months would lose their child care subsidy.

There is a rationale for the Governor's proposal. Before 1997, when the federal Temporary Assistance for Needy Families (TANF) replaced Aid for Families with Dependent Children (AFDC), there was a limit on subsidized care within welfare to work programs. A family was limited to 24 months of "transitional child care" after leaving cash aid for a low-paying job. The Governor's proposal returns this aspect of child care to pre-welfare-reform status.

In addition, providing partial subsidies for the child care of low-wage workers who have left cash aid does put pressure on the General Fund: all CalWORKs participants who engage in welfare to work are entitled to subsidized child care. Because most former cash-aid recipients remain in low-wage jobs, they continue to qualify for partial child care subsidies. The Governor wants to put a time limit on this entitlement in order to control rising child care costs that result from the success of many aid recipients' entering and remaining in the low-wage workforce.

A large number of families currently enrolled in stage two have been off cash aid for more than 12 months. During the next 17 months, these families and all families currently in stage three will exceed 24 months since their last aid payment. Under the Governor's proposal, these families would cease to receive subsidized care, unless they moved into an opening in the programs funded through CDE separate from CalWORKs.

The Governor's proposal directly effects at least 50,000 children and as many as 80,000 children – from nearly 50,000 families. These parents have "played by the rules": leaving cash aid, entering the workforce and remaining there. They are now part of the working poor.

Without child care assistance, some of these families might well return to the welfare rolls. Many others will patch together child care arrangements of poor quality and, in some cases, without basic health and safety features.

Cost-Saving/Cost-Shifting Options

California's child care and development programs are rich in history, diverse in their organization, and sensitive to community needs. While the system has many regulatory nuances and can seem inordinately complex on first viewing, the structure is relatively straightforward.

The following pages discuss alternatives to the Governor's proposals for reducing General Fund costs for child care and development. They embody the following principles:

- Maintain or enhance the quality of care whenever possible.
- Focus on what particular agencies and programs do best.
- Include partners that have sources of funding outside the General Fund.
- Keep as much focus as possible on direct services to families.

All options, except option 6 (which makes the State Preschool program a partnership with county children and families commission), maintain the basic structure of the current system.

1. Reduce the Percentage of Contract Funds Used for Administration and Support Services by Alternative Payment Programs. Potential Savings, $15 Million To $35 Million

Currently, alternative payment programs (APP) administer close to two billion dollars of child care funds. These programs certify a parent's eligibility for care, assist them in finding care if necessary, pay the child care provider that provider's rates (up to a ceiling), and collect any fee the parent owes (based on the state's sliding scale). In addition, the APP is responsible for providing "locally designed support services for parents and providers … [including] professional and technical assistance and information for providers [and] parenting information." (Education Code §8220.5) Further, an APP shall document that "subsidized children, as necessary and appropriate, receive supportive services" through the county and other community resources. (Education Code §8266.5)

To cover the costs of these administrative and support services, the APP contractor can keep up to 20 percent of its contract amount. In general, administrative costs are up to 15 percent of the contract total; support services are the remainder.

The Legislature can perhaps lower the cost of APP administrative services provided. Before budget subcommittee hearings begin, the CDE should meet with APP administrators to discuss streamlining the administrative process. Cost-saving possibilities include re-certifying a parent's continued eligibility for care less often and using electronic-benefit-transfer technology for attendance reporting and for paying providers.

Also, APP contractors provide a range of support services to children, to their families, and to child care providers. Which of those support services is essential? If it is possible for the Department of Education and the APP administrators to identify essential support services and estimate the cost of providing those. The Legislature could then adopt language defining those essential services and limiting expenditures to them. This reduction could be temporary – for the budget year only – and considered again in 2004.

In 1976, at the outset of APP contracts, support services were envisioned to include assessment and referral for health and social services that a child or family needed. Limiting support services to those might be a place the department and the APP administrators could begin their discussion.

Such actions on the administrative and support-service costs, taken together, could shave one or two percent off the contract total. Each percent reduced represents savings of nearly $20,000,000 per year.

2. Change the Reimbursement Calculation for Licensed Facilities Caring Primarily For Subsidized Children. No Estimate: Savings Probably in the $5 Million To $10 Million Range.

At present, no more than 75 percent of the children enrolled in a licensed child care center or family child care home can be subsidized through an alternative payment program. This rule is in effect so that licensed programs charge rates that are driven by the market, not by the maximum the state is willing to pay. (See Education Code §8222.5.)

The Legislature could remove the limit on the percentage of subsidized children enrolled at a center or licensed home. When the percentage of subsidized children rises above a designated percent (such as 60 or 75 percent), the facility would be reimbursed at the mean cost of care per child for that county.

This change would reduce state costs and make the state payments more reflective of the market rate.

3. Adjust Payments for License-Exempt Care to Reflect the Market Rate. Estimated Savings, $30 Million.

Currently, a family receiving subsidized child care can, under some circumstances, select a child care provider who is not licensed. These so-called "license-exempt providers" can be relatives, neighbors, friends, or strangers (nannies). These providers are exempt from licensure as long as they care only for the children of one parent in addition to their own children.

Providers are reimbursed on a per-child basis at 90 percent of the maximum reimbursement paid to a licensed provider within the county. (There is a county-by-county calculation to establish the maximum amount a licensed provider can be paid. They are paid the rate they charge parents who are not subsidized or they are paid an amount equal to 1.5 standard deviations above the mean cost of care for their county – whichever is less.)

Instead of paying 90 percent of that top reimbursement level, the Legislature could set the rate for license-exempt providers at a percentage of the mean cost of care in a county – say, 80 percent or 90 percent of the mean. For example, in a county where the mean cost of full time care for a preschooler is $100/week, a license-exempt provider would be paid $90 (90 percent) or $80 (80 percent) per week, rather than at $112.50, which is the amount being paid in the current year (90 percent of $125, the top rate paid to licensed providers in that county).

This option would provide substantial savings. This option should still give parents a full range of choices.

4. Review "Quality Improvement" Expenditures and Work With the State's Children and Families Commission To Identify Projects the Commission Could Adopt. Savings: $20 Million To $40 Million.

Federal law requires that four percent of federal child care block grant be spent for "quality improvement programs." For more than ten years, California has used this set-aside and additional funds to support the child care workforce.

Current expenditures finance community college coursework, stipends for master teachers to work with new teachers, and repay student loans. A portion of these funds augment the contracts of resource and referral programs, enabling them to provide more parents with information about their child care options. The budget for all quality activities in the current year is $76.8 million.

Since Congress established the child care block grant and its quality set-aside, the voters of California have passed the Children and Families initiative (Proposition 10, 1998). A 50-cent per-pack surcharge on cigarettes provides funds for programs and services to children from birth to five years of age. A state commission and 58 county commissions receive $600 to $700 million in revenues each year.

The state commission manages three funds reserved for "education, including … professional and parental education and training, … the education and training of child care providers, … [and] expenditures for the research and development of best practices and standards for all programs and services relating to early childhood development" (Health and Safety Code §130100). These three funds receive 11 percent of the annual tobacco tax surcharge – a minimum of $65 million per year.

Many of the current Quality Improvement Projects fit easily within the statutory language that guides the state commission's expenditures. The commission has provided leadership on some of these same quality issues. The commission could identify Quality Improvement Projects which, though currently receiving state and federal funds, could be supported exclusively with state funds. This would free up federal funds that could be redirected to programs currently supported by the General Fund and that meet the federal Quality Improvement definitions. These include community care licensing activities and resource and referral services.

In addition, there may be projects currently funded through the Quality Improvement set-aside that county children and families commissions may want to adopt. During the budget process, the Legislature may want to direct the CDE to work with county commissions and their statewide association to identify those projects.

When proposing to use Proposition 10 funds in the budget year for activities currently provided by state and federal funds, some may ask if this is "supplantation," as proscribed in the language of Proposition 10. (See Health and Safety Code §30131.4.) Legislative counsel could provide an opinion of the application of this section to a new budget year – if it would preclude the state commission or a county commission from funding an activity that is no longer supported by state or federal funds.

5. Work With Head Start to Take Over More Part-Day Programs for Preschool-Aged Children – Limit State Preschool to Four-Year-Olds. Estimated Savings Up To $45 Million.

Both the state and the federal governments finance a part-day part-year program for three- and four-year-old children from low-income families. The federal program is Head Start; the state program is called State Preschool. When these two programs began in the mid-1960s, they received similar per-child funding. Over time, the Head Start per-child reimbursement increased more rapidly than has the State Preschool reimbursement.

Head Start's average per-child reimbursement for preschool children is more than $6,400, while State Preschool reimburses about half that. Head Start's higher reimbursement rates allows it to finance a higher level of services, such as support services for children and families.

From 1970 until 1990, Congress expanded Head Start to serve additional children. During this same period, California expanded its commitment to full-day full-year child care, while providing little in the way of new appropriations for State Preschool.

Since 1996, federal and state welfare policy has added significant pressure on low-income parents to join the workforce. As a result, part-day programs such as Head Start and State Preschool are in less demand. There are now many low-income communities in California where the demand for part-day preschool programs is fully met, while the demand for full-day and full-year child care continues to be greater than the supply.

The California Department of Education (CDE) and the federal regional Head Start office in San Francisco have a long-standing administrative collaboration. The Legislature could adopt options to reduce the size of the State Preschool program and direct the CDE to work with the Region IX office of Head Start to mitigate the impact of such reductions on any loss of local services:

- The Legislature could limit State Preschool enrollment in the budget year to four-year-olds and reduce budget-year contracts by each contractor's percentage of three-year-olds enrolled in the current year. Because about 15 percent of current enrollees are three, this would be a budget-year savings in the range of $45 million from the General Fund. Savings might not equal 15 percent because small contractors would still need enough funding for a full classroom. In those instances, local coordination with Head Start could ensure full State-Preschool classrooms of four-year-olds, with Head Start serving more three-year olds. (See Education Code §8235 and §8236.)

- Any expansion in Head Start funding could, through coordination between CDE and Region IX, be focused on communities with current State Preschool classrooms: those classrooms could be phased out as Head Start increases enrollment.

Head Start would be the primary provider of part-day, part-year services to 3- and 4-year-old children from low-income families; and have CDE provide the lion's share of full-day, full-year child care and development services to the children of low-income working families. Over time, Head Start has proved itself in the part-day, part-year arena. Future efforts to establish universal preschool within California will draw on the Head Start experience.

6. Invite Local Proposition 10 Commissions to Provide Leadership for Preschool Programs. Savings Up To $155 Million.

In the context of both the state's current budget difficulties and the recent report of the Joint Committee on a Master Plan for Education, the Legislature could explore the option of inviting county children and families commissions to become laboratories for the testing models for a universal preschool in California.

In the current year, the General Fund provides $310 million to support the State Preschool program. (California Head Start programs receive $800 million in federal funds.)

The Legislature could end the direct funding of State Preschool and enter into partnerships with county children and families (Proposition 10) commissions to fund and evaluate various approaches to preschool education. As such, the state would match local expenditures on a dollar-for-dollar basis, up to $155 million (half this year's General Fund appropriation for State Preschool.)

Programs would have local design (e.g., The counties could set limits: Be available to four year olds only, be part day or be embedded in a full day; be means tested or be for all children.)

The counties, through their children and families commissions, would become "laboratories of change."

To ensure continuity of service within communities and to promote a wide range of approaches to preschool, the Legislature could make the matching funds available to counties in the same proportion that State Preschool funds are currently allocated.

7. Enact a Time-Limited Moratorium on New Enrollments in Alternative Payment Programs to Reduce Total Child Care Budget.

Since 1989, subsidized child care has increased by more than $1 billion (state and federal funds). Almost the entire amount is allocated within the Alternative Payment

Programs (APPs). Because APPs are flexible, it is easy for them to add new children. The Legislature could use this flexibility to manage costs. For example, it could:

- Place a six-month moratorium on replacing exiting families. There is a predictable turnover in enrollment every year, much of it happening during July, August, and September. By not replacing exiting families, savings to the General Fund would accrue.

- Set a target for savings. Ensure the savings are met by prohibiting enrollment until the target is reached. Only then would the California Department of Education authorize an APP contractor to enroll a new family after another family has exited the program.

- Guarantee contractors a fixed dollar amount for administration and support services for at least the first six months of the budget year.

By working with the APPs in this manner the Legislature could maintain current eligibility criteria for families and reimbursement rates for providers.

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REVENUE AND TAX PROPOSALS

The Department of Finance estimates General Fund revenues and transfers at $69.2 billion in 2003-04. This is $3.9 billion, or 5 percent, less than General Fund revenues and transfers in the current year. This essay covers the following issues:

- Tax Structure and Revenue Volatility
- The Governor's General Fund Tax and Revenue Proposals
- Other Tax and Revenue Issues the Legislature May Want to Consider
- Realignment Tax Proposals

The Governor maintains that there is a $34.6 billion shortfall in the state budget for the 2002-03 and 2003-04 fiscal years. In December 2002, the Governor proposed urgency legislation to implement budget reductions totaling $10.2 billion including $3.4 billion in 2002-03 and $6.8 billion in 2003-04.

The proposed budget including the December Revision proposes the following revenue proposals in the current and budget year:

- $2.1 billion from transfers and other revenues.
- $1.7 billion from loans and other borrowing.
- $8.2 billion in tax proposals for State-Local Realignment.

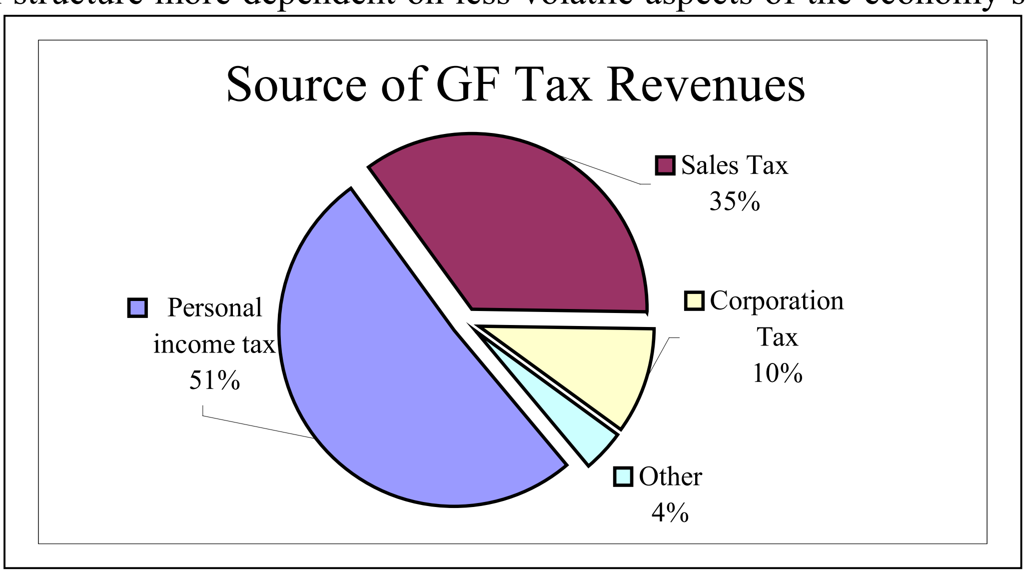
These issues are discussed in more detail below. Revenue and tax issues comprise $12 billion of the $34.6 billion deficit identified by the Governor.

Tax Structure and Revenue Volatility

The following factors contribute to the volatility of the California tax structure:

- The personal income tax accounts for more than fifty percent of General Fund revenues.
- A significantly larger share of total state adjusted gross income is attributable to high-income taxpayers.
- Income of high-income taxpayers is subject to more variation than the lower income taxpayers.
- Individuals at the lower end of the income scale pay a very small share of the personal income tax.
- Nonwage income (capital gains, stock options) is a significant contributor to revenue fluctuations.

Composition of General Fund Revenues. The General Fund relies on the personal income tax for more than one-half of its revenues. This is the most volatile of the tax revenues. The income tax structure is very progressive and relies heavily on high-income taxpayers. Revenue from the sales tax accounts for 35 percent of total General Fund revenues. The sales tax base is a relatively slow growing revenue source. Over 85 percent of the General Fund tax base are from these two tax sources. A broader tax structure more dependent on less volatile aspects of the economy such

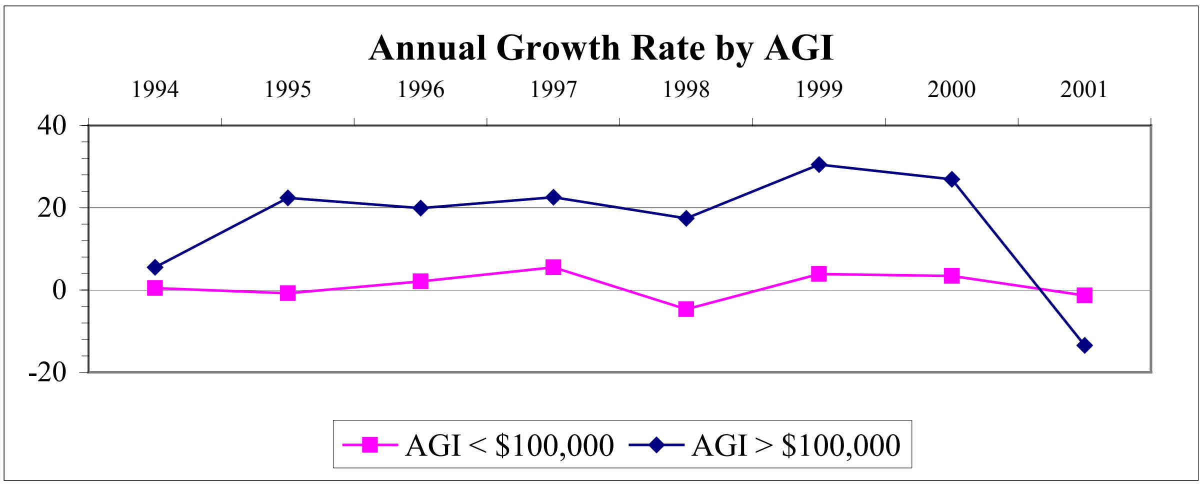


as property values or on a broader sales tax base would produce a more stable revenue base in both strong and weak economic circumstances.

Personal Income Tax Derived from High Income Taxpayers

The top ten percent of taxpayers in California pay 80 percent of the personal income tax in California. This top ten percent of taxpayers have an adjusted gross income (AGI) of $100,000 or more. Those taxpayers with AGI of $100,000 or more have incomes that are much more volatile than those with incomes less than $100,000.

The following chart shows the percentage change in total AGI for taxpayers with AGI less than $100,00 and those with $100,000 and above.

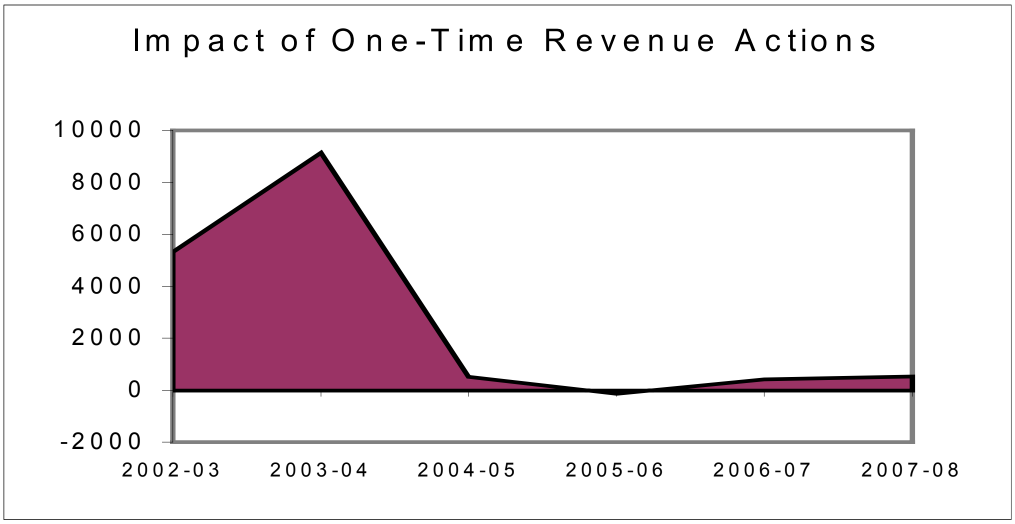


This chart shows that the AGI of taxpayers with higher incomes is much more volatile than the AGI of taxpayers with lower incomes. The AGI of these high-income taxpayers increases much faster than lower income taxpayers during strong economic periods and it decreases much more rapidly during weak economic periods.

Impact of One-Time Revenues and Transfers

The volatility of the tax system in California is not the only revenue problem confronting the Legislature this year. In addition, many of the actions taken in the 2002-03 budget and proposed in the 2003-04 budget result in one-time increases in revenues. Actions taken to address the General Fund revenue shortfall in 2001-02 and 2002-03 did not address the structural problem in the state tax system. The revenue solutions consisted of revenue accelerations, increased audit and collection activities, suspension of tax incentives, and loans and transfers to the General Fund. These actions create an artificial increase in revenues that intensify the tax structure problem. The issues are discussed in the next section on General Fund Tax and Revenue Budget Proposals.

The following chart displays the one-time revenues from revenue accelerations,



increased audit and collection activities, tax proposals, suspension of tax incentives, borrowing, and loans and transfers.

General Fund Tax and Revenue Budget Proposals

The following is a discussion of the tax and borrowing issues in the proposed budget.

Tax Issues

2003-04 Budget Proposals

The following tax proposals would result in General Fund revenue effects.

Regulated Investment Companies (RIC). The budget proposes to prevent banks from utilizing RICs to avoid California tax by improperly sheltering income. The proposal includes language that would preserve FTB's ability to litigate the issue for years prior to those resolved by the proposed statutory change. This proposal would increase General Fund revenues by $45 million in 20003-04, $55 million in 2004-05 and $65 million in 2005-06.

A RIC is a mutual fund that is eligible to pass the taxes on capital gains, dividends, or interest payments on to individual investors. RICs are exempt from paying federal and state income taxes. Federal law requires that RIC sponsors must sell shares to at least 100 private investors.

Manufacturers' Investment Credit (MIC) Clarification. The budget proposes to clarify that the MIC is intended to apply to manufacturing activities as specified in the Standard Industrial Code Manual. This clarification is intended to address a recent BOE decision to allow the MIC to be claimed by in-store bakeries and delis, two industries where there is little risk that the business owner will leave the state. This proposal would reverse the BOE decision and instead apply the FTB regulation limiting the application of the MIC to manufacturing firms. This would result in increased General Fund revenues of $50 million in 2003-04, $50 million in 2004-05, and $30 million in 2005-06.

Extension of the Sunset Provision for the Manufacturers' Investment Credit (MIC). The intent of the MIC was to create manufacturing jobs and the enabling legislation sunset the MIC if manufacturing employment does not exceed a specified level. Based on the economic forecast in the budget, decreases in manufacturing employment would cause the MIC to sunset on January 1, 2004. The budget proposes to revise the sunset provisions to extend the sunset date to January 1, 2009. The budget does not highlight that the revenue loss from this extension is $458 million in 2004-05 growing annually to nearly $600 million in 2008-09.

Indian Gaming Revenue. The budget proposes to renegotiate Tribal-State Gaming Compacts with 61 federally recognized Indian tribes in 2003. There are also other federally recognized that have indicated an interest in negotiating compacts with the Governor. The budget assumes that the Administration can generate $1.5 billion in revenue in 2003-04 and future fiscal years through revenue sharing agreements negotiated with the Compacts.

It is unlikely that this proposal will result in an additional $1.5 billion in General Fund revenue, since the tribes have to agree to be taxed by the state. If Indian tribes agree to this revenue increase, the Compact would most likely have to include significant favorable changes in gaming for the Indian tribes.

2002-03 Budget Trailer Bill Tax Legislation

The Legislature enacted two major tax packages in 2002-03. Before enactment of the budget, legislation was enacted to conform California income tax law to federal law relating primarily to retirement plans, pensions, IRAs, and deferred compensation plans. A budget trailer bill also contained tax and revenue acceleration provisions.

Pension and IRA Conformity

In May 2002, the Governor signed SB 657 (Scott) and AB 1122 (Corbett) which conformed California income tax law to federal Economic Growth and Tax Relief Reconciliation Act of 2001 relating to retirement plans and certain trusts, including provisions relating to annuities and certain proceeds of life insurance contracts, IRA's, employee annuities, qualified state tuition programs, retirement savings, deferred compensation plans, employee-funded pension trusts, and group legal service plans. These bills also contained conformed California income tax law to selected federal law changes enacted in 1998, 1999, and 2000. This bill resulted in increased revenues of $189 million in 2001-02, no net fiscal impact in 2002-03, and a revenue loss of $10.5 million in 2003-04.

2002-03 Tax Budget Trailer Bill

The 2002 tax budget trailer bill implemented the tax and revenue provisions related to the 2002-03 budget compromise. The package increased General Fund revenues in 2002-03 by approximately $2.4 billion and $800 million in 2003-04. The bill reduces annual General Fund revenues in 2004-05 and fiscal years thereafter by about $500 million. The trailer bill primarily contained one-time revenue accelerations offset by tax incentives in future fiscal years. Chapter 488 included the following tax provisions:

Suspension of Net Operating Loss Deduction. Deferred the net operating loss (NOL) deduction for tax years 2002 and 2003. The availability period for deducting these losses was extended for an additional two years.

Current law allows a NOL carry forward deduction of 60 percent for a period of up to ten years. This amount was scheduled to increase to 65 percent commencing January 1, 2004. AB 2065 increased the NOL deduction to 100 percent effective January 1, 2004.

This provision results in increased revenues of $1.2 billion in 2002-03 and $800 million in 2003-04. The increase in the NOL deduction to 100 percent will result in on-going General Fund revenue losses of about $500 million commencing in 2004-05.

Withholding on Stock Options and Bonuses. Increased withholding for stock options and bonuses from 6 percent to 9.3 percent, effective for payments on or after January 1, 2003. This will result in one-time increased revenues of about $400 million in 2002-03.

Withholding on Real Estate Transactions. Imposed withholding on the sale of commercial property for California residents to conform to the withholding provisions for nonresidents. Current law requires nonresidents to withhold 3.5 percent of the purchase price of commercial property for personal income tax purposes. AB 2065 extended this same treatment to residents of the state. This provision will result in one-time revenue increases of $225 million for 2002-03.

The bill provides an exemption from withholding for transactions involving like-kind exchanges, involuntary conversions, and loss on the sale of the property. The bill, however, inadvertently omitted provisions that would allow the Franchise Tax Board (FTB) to waive the withholding under certain circumstances. The FTB can waive withholding on the sale of property by nonresidents in cases where there is little or no gain on the sale or the withholding would exceed the tax liability from the sale.

Conform to Federal Law on Bad Debt. Changed the methodology for calculating deductions for bank bad-debt losses under the Bank and Corporation Tax to conform to federal law. Commencing with the 2002 tax year, the bill requires banks with more than $500 million in assets to deduct losses in the year in which they become worthless rather than allow these banks to deduct 50 percent of their existing bad-debt reserve balances. This change will result in a one-time increase in General Fund revenues of $285 million in 2002-03.

Suspend the Teacher Tax Credit. Suspended the Teacher Tax Credit for the 2002 tax year. This credit is available to credentialed teachers and varies from $250 to $1,500 per year, depending on the length of the teacher's service. This will result in a one-time revenue increase of $170 million in 2002-03.

Collections on High Risk Accounts. Authorized FTB and Board of Equalization (BOE) to forgive any penalties, interest, or fees on unpaid income tax and sales tax accounts if the outstanding tax liability is paid. The FTB and BOE identify the taxpayers with high-risk accounts and have the authority to offer this special treatment to those taxpayers. This authority is limited to the period October 1, 2002 through June 30, 2003. General Fund revenues are expected to increase by $145 million in 2002-03.

Loans and Transfers

Both the 2002-03 and 2003-04 budgets rely heavily on loans and transfers from special funds. In addition, several proposals involved borrowing of outside funds to pay current obligations or to secure future financing.

The proposed budget includes loans from special funds of $148 million and transfers of $107 million. It includes $1.5 billion in pension obligations bonds, which will result in a one-time General Fund revenue increase.

The 2002-03 budget authorized loans and transfers from special funds to address the shortfall in the General Fund. Loans to the General Fund total slightly more than $2 billion and transfers are more than $500 million. In addition, the budget package included the securitization of $4.5 billion of Master Tax Settlement payments scheduled to be paid to the state over the next twenty years.

Loans and Transfers from the General Fund

The loans and transfers from special funds to the General Fund were made from special funds that had available resources that could be used to address the General Fund shortfall. The transfers of $500 million in the current year and $107 million proposed for the December Revision and the budget year are one-time, but are not required to be repaid to the fund. The loans of $2 billion in the current year and $148 million in the budget year are generally from funds with statutory or constitutional restrictions on the use of funds and must be repaid.

Chapter 1124, Statutes of 2002, (AB 3000) sets conditions for the loans from special funds to the General Fund. This same trailer bill language is proposed for both current year and budget year loans. Money may be loaned from one state fund or account, if the following conditions are met:

- The loan is authorized in the Budget Act,
- The terms and conditions of the loan are set forth in the loan authorization, including an interest rate,
- The loan is considered part of the balance of the fund or account, and
- Fees and assessments will not be increased as a result of the loan.

Loaned moneys may not be considered a transfer of resources for purposes of determining the legality of using the funds. The Director of Finance is required to order the repayment of all or a portion of the loan if either the fund or account *making the loan* needs cash, or the fund or account *receiving the loan* does not need the money.

Repayment of Loans by Fiscal Year

The estimate of the General Fund cost of loan repayments is $450 million in 2004-05, $887 million in 2005-06, $345 million in 2006-07, and $50 million in years thereafter. The one-time benefit from these loans will be more than offset by the cost to the General Fund in future fiscal years for repayment of these loans.

Other Borrowing

Pension Obligation Bonds

The budget proposes legislation to authorize pension obligation bonds of $1.5 billion to fund the state's budget year retirement obligations to both CalPERS and STRS. Although the Administration requested action on this issue in the First Extraordinary Session, no specific proposal or trailer bill language has been provided. The budget summary indicates that the Administration will also be conferring with CalPERS and STRS about the possibility of a loan of the same amount. This proposal would need to be enacted by June 30 to suspend the payment of the PERS and STRS contribution in 2003-04.

This proposal would effectively increase General Fund revenues by $1.5 billion in 2003-04. These funds would be used to make the budget year contribution to PERS and STRS and would be repaid over some yet undetermined time. Thus, this proposal would provide one-time funds of $1.5 billion with an obligation to repay the funds.

Master Tax Settlement Securitization

In a 2002 budget trailer bill, the state was authorized to borrow $4.5 billion in future payments due the state from the Tobacco Settlement Fund. This represents one-half of what California is owed over the next twenty year. This one-time infusion of revenue in 2002-03 will be repaid over twenty years at nearly $500 million per year commencing in 2003-04. This proposal again exacerbates the tax structure problem the state faces.

Other Tax Issues the Legislature May Want to Consider

Given the magnitude of the budget problem, the Administration and the Legislature will likely look at other revenue and tax proposals for 2002-03 and 2003-04.

Vehicle License Fees

Current law imposes an annual vehicle license fee (VLF) on any vehicle subject to registration in this state equal to 2 percent of the market value of that vehicle. The VLF is in lieu of any ad valorem property tax upon vehicles. The market value of the vehicle is determined by the purchase price and depreciated over the life of the car. For vehicle license fees due after July 1, 2001, the VLF is “offset” or reduced by 67.5 percent. The Controller is required, upon receipt of monthly notification from the Department of Motor Vehicles of the amount of offsets applied, to transfer state General Fund moneys to reimburse local governments for losses resulting from the vehicle license fee offset.

If there are insufficient moneys in the General Fund for the Controller to fully reimburse local governments for the loss in VLF, current law requires the offset amount to be reduced in proportion to the shortfall in funding available to reimburse local governments for those losses. Existing law does not designate the person or agency responsible for making the determination of whether there are sufficient moneys in the General Fund to make these reimbursements.

The Legislature approved AB 4X in February 2003. AB 4X would require the Director of Finance to make the determination of whether there are insufficient moneys in the General Fund for the Controller to reimburse local governments for their losses resulting from the VLF offsets.

AB 4X also clarifies that the term "General Fund”, as used with reference to the vehicle license fee offset, has the same meaning as set forth in Section 16300 of the Government Code. It also provided that the term "General Fund" does not include any moneys that the state is obligated to repay to the source from which those moneys were received, or any moneys in that fund that are derived from loans or other forms of indebtedness.

The Governor indicated on February 4 that he planned to veto AB 4X.

Expand Sales Tax Base to Include Services

There have been various proposals to expand the sales tax base to include all or selected services. The question of which specific services should be taxed is a difficult policy decision.

Current law provides that the sale of services where no tangible personal property is transferred or where the transfer of property is incidental are not subject to sales and use taxes. Instead, persons that provide services are considered consumers of property used in their business activities and thus are subject to the sales and use tax. If the service supplier sells any tangible personal property to their customers, the tax applies to that sale.

Certain services are defined a s sales of tangible personal property. An example of a taxable service would be the charge for fabrication of tangible personal property is considered a taxable sale even when the consumer provides all the tangible personal property used to fabricate the final product.

Numerous services could be subject to a sales and use tax or an excise tax rate. Services can generate a substantial amount of revenue even at a relatively low rate. Some of the major service areas that would generate significant revenues are:

- Automotive Repair Services
- Custom Computer Programs
- Janitorial Services
- Admission Charges
- Lodging
- Cable TV/ Satellite TV
- Accounting and Bookkeeping Services
- Legal Services
- Cell Phone Services
- Engineering, Architectural and Surveying Services
- Management, Scientific and Technical Consulting Services

Equity Issues

A number of equity issues arise in determining which services should be subject to a sales and use tax or excise tax.

- Some of the services are already taxed at the state or local level.

  Admissions, lodging, and cable TV are frequently subject to local excise taxes at various rates throughout the state.

  The charge for intrastate cell phone services are subject to state tax at a rate of 0.72 percent for the State Emergency Telephone Number Account (911 Account). The budget proposes increasing this rate to 1.0 percent.

- Can result in unequal treatment of businesses.

  Businesses that have their own legal or accounting divisions would not be subject to a tax on services, while those businesses that contract out would be subject to the tax. Larger businesses are more likely to have legal or accounting divisions than smaller businesses.

Sales and Use Tax or Specific Tax Rate

The current sales tax rate (state, local, or combined) could be imposed on selected services or a state excise tax could be imposed on those services.

Revenue Proposals Related to Realignment

The Budget proposes the following state tax increases related to county realignment. The revenues would be deposited in the Enhanced State and Local Realignment Fund. Revenue in funds other than the General Fund are not subject to the Proposition 98 Guarantee. The proposed increases in rates and 2003-04 revenues are as follows:

• Increase sales tax rate by one cent	$4.6 billion
• Add 10 and 11 percent personal income tax rates	$2.6 billion
• Increase cigarette tax by $1.10 per pack	$1.2 billion
Total Revenue	$8.4 billion

This revenue would be deposited in the new Enhanced State and Local Realignment Fund. This revenue would fund realignment of state and local health and social services programs. In addition, loss of revenues to the special funds that receive cigarette tax revenues would be reimbursed for any loss resulting from decreased taxable distributions resulting from the cigarette tax increase.

Increase Sales Tax Rate by One Percent

The budget proposes a one-cent increase in the sales and use tax rate effective July 1, 2003. This would increase revenues by $4.6 billion in 2003-04.

The current state and local sales and use tax rate is as follows:

	Sales and Use Tax Rate	Comments
State Rates		
General Fund	5.00	Based on General Fund reserves, this rate may be temporarily reduced to 4.75 percent.
Local Revenue Fund	0.50	Dedicated to counties for state-local realignment.
Local Uniform Rates		
Bradley-Burns	1.00	Imposed by city and county ordinance for general purpose.
Transportation Rate	0.25	Dedicated for county transportation purposes.
Local Public Safety Fund	0.50	Dedicated to counties for public safety purposes.
Local Add-on Rates		
Transactions and Use Taxes	Up to 2.00	Levied in 0.25 percent increments in any county. Requires approval by the Board of Supervisors plus two-thirds of the electorate. For most counties, the maximum rate is 1.50 percent. The limit is 2.00 percent in San Mateo County, 1.75 percent in San Francisco County, and 1.00 percent in San Diego County.

Counties without add-on rates have a total sales and use tax rate of 7.25 percent. The highest state and local rate imposed is 8.50 percent in San Francisco County. If the increased sales and use tax rate of 1.00 percent were enacted, the highest state and local rate imposed in California would be 9.5 percent.

Sales and Use Tax Rates in Other States

There are 8 states and the District of Columbia that have a maximum state and local sales and use tax rate equal or greater than 8.5 percent. These are the highest rates imposed anywhere in those states and are not uniform state and local sales tax rates. The rates in those states are as follows:

State	**Maximum State/Local Rate**
Alabama	9.00
Arizona	8.60
Florida	8.50
Illinois	8.75
Louisiana	9.50
New York	8.50
Oklahoma	9.75
Tennessee	8.75
Washington, D.C.	8.80

If California were to adopt the proposed one percent sales and use tax rate increase, there would be one state (Louisiana) with the same maximum rate and one state (Oklahoma) with a higher sales tax rate than California.

Add 10 and 11 Percent Personal Income Tax Rates

The budget proposes to add the following income tax rates. It adds the following income tax rates for the following filers:

Filing Status	10 Percent Rate Applies to Taxable Income Above:	11 Percent Rate Applies to Taxable Income Above:
Single Filers	$136,115	$272,230
Joint Filers	$272,230	$544,460
Head of Household	$185,275	$370,550

The current personal income tax is progressive, with rates ranging from 1 percent to 9.3 percent. Personal, dependent, and other credits are allowed against the gross tax liability.

These increased rates apply to taxable income, not adjusted gross income (AGI). Certain items are deducted from gross income to calculate AGI. Items that can be deducted in calculating AGI include IRA contributions, fifty percent of self-employment tax, self-employed health insurance deductions, penalties on early withdrawal of savings; alimony paid; and moving expenses. Taxable income is AGI less the standard deduction or itemized deductions. Itemized deductions include items such as interest on mortgages, charitable contributions, certain state and local taxes, or medical expenses.

Issue

In California, personal income taxpayers do not pay state taxes until they have a relatively high AGI. The following chart indicates the taxation threshold by AGI both with and without the Renter's Credit. AGI gives a better reflection of an individual's or family's income level than taxable income.

Tax Threshold for the 2002 Tax Year by Adjusted Gross Income

Filing Status	**Without Renters' Credit**	**With Renters' Credit**
Single		
No dependents	$9,955	$12,955
One dependent	$19,655	$21,155
Married Filing Joint Return		
No dependent	$19,859	$25,859
One dependent	$32,459	$36,059
Two dependents	$39,359	$42,359
Head Of Household		
One dependent	$28,459	$34,059
Two dependents	$37,359	$40,359

Thus, an average married couple with two children would pay state personal income tax if their income were more than $42,359 per year. The state tax rate of 1.0 percent would apply to the first $11,668 of income over $42,359.

Cigarette Tax Increase Proposal

The budget proposes a tobacco tax increase of $1.10 per pack that would become effective July 1, 2003. This is expected to generate $1.2 billion in 2003-04 and $1.1 billion in 2004-05 according to the Department of Finance.

The current tax on cigarette and other tobacco products are as follows:

Fund	Rate Per Pack	Use of Funds
General Fund	$0.10	Not earmarked for any purpose.
Proposition 10	$0.25	California Children and Families First Trust Fund to develop a statewide system of information and services for early childhood development.
Proposition 99	$0.50	Cigarette and Tobacco Products Surtax Fund to support anti-smoking education programs, tobacco-related disease research, indigent health care, and public resources.
Breast Cancer	$0.02	Breast cancer research.
Total	**$0.87**	
Proposed increase	$1.10	State and Local Realignment
Proposed Total	$1.97	

This increase is expected to reduce taxable consumption of tobacco products by an additional 11 percent, in addition to the normal baseline decline in taxable consumption of tobacco products that has occurred since the major increases in the tobacco tax. The existing special funds that receive tobacco tax revenues will experience a reduction of approximately $96 million in 2003-04. Proposition 99 revenues will be reduced by $31 million, Proposition 10 revenues will be reduced by $62 million, and the Breast Cancer Fund will be reduced by $2.5 million. Revenues from the proposed tax increase will reimburse these funds for the reduced revenues from the decrease in taxable distributions.

Taxes in Other States

According to the Federation of Tax Administrators, California has the 12th highest state rate in the United States. If this proposal were enacted, California would have the highest state tax rate. New York has a state rate of $1.50 per pack and New York City imposes an additional rate of $1.50 per pack, so the state and local rate is $3.00 per pack.

Analysis prepared by Judi Smith, Senate Budget and Fiscal Review

SUBCOMMITTEE NO. 1

EDUCATION

K-12 EDUCATION

0558 Office of the Secretary For Education

The Secretary of Education, a member of the Governor's Cabinet, is responsible for advising the Governor and making recommendations on state education policy and legislation. The Office of the Secretary for Education (OSE) administers several education programs, including the Academic Volunteer and Mentor Service Program, the Governor's Reading Award Program. For the current fiscal year, the costs of the OSE are funded through the Governor's Office of Planning and Research (0650) pending legislation to establish the Secretary statutorily.

2002-03 Reductions

As adopted by the Legislature, reductions in 2002-03 include:

- $834,000 General Fund (Proposition 98) for the Academic Volunteer and Mentor Service Program and School-to-Career Program.
- $122,000 General Fund and 0.3 personnel year.

2003-04 Reductions

The 2003-04 budget proposes $3.4 million in reductions to Office of the Secretary of Education. They include:

- $2,000,000 General Fund (Proposition 98) to eliminate the School to Career Technology Grant Program
- $756,000 General Fund (Proposition 98) for the Academic Volunteer and Mentor Service Program
- $642,000 and 7.7 personnel years in state operations.

Issues

- Reductions to the Academic Volunteer and Mentor Service Program. The Governor proposes to reduce this program as a part of a package of reductions to selected categorical programs in 2003-04. Under this program, university students offer tutoring services to 20,000 at-risk children and youth.
- Elimination of the School-to-Career Partnership Grants Program. This program was established by Chapter 793, Statutes of 2000 (AB 1873, Wiggins) for the purpose of administering a competitive matching grant program to local entities. The program is a collaboration among OSE, SDE, the CA Community Colleges Chancellor's Office, and the Health and Human Services Agency. The Governor signed the AB 1873 with the caveat that unless the nonprofit and private sectors exceeded this amount in matching funds, he would not continue allocating funds toward this program.

6110 Department of Education

California's public education system is administered at the state level by the California Department of Education (CDE), under the direction of the Superintendent of Public Instruction and the State Board of Education, for the education of approximately 6.1 million students from infancy to adulthood. The primary goal of the Superintendent and the CDE is to provide policy direction to local school districts and to work with the educational community to improve academic performance.

At the local level, education is the responsibility of 985 school districts, 58 county offices of education, and over 8,700 schools. More than 301,000 teachers are employed in public schools statewide.

The 2003-04 Governor's budget proposes nearly $53.0 billion for K-12 education, which reflects a decrease of $497 million (0.9 percent) below the proposed 2002-03 revised budget. The Department of Finance estimates that average per-pupil funding from all sources (state, local, and federal) totals $8,899 in 2003-04, a decrease of $173 below the $9,072 per-pupil in 2002-03.

Table 1
Summary of Revenues

(dollars in millions)	2002-03 Revised	2003-04 Proposed	$ Change	% Change
General Fund	$28,286	$27,390	-$896	-3.2
Lottery Fund	800	800	0	0.0
Other State Funds	113	80	-34	-29.7
Local Property Taxes	13,140	13,775	635	4.8
Local Miscellaneous	3,716	3,716	0	0.0
Local Debt Service	828	828	0	0.0
Federal Funds	6,599	6,397	-202	-3.1
Total	$53,481	$52,985	-$497	-0.9

As indicated by Table 1, the $53.0 billion for K-12 education includes $27.4 billion from the state General Fund, $13.8 billion in local property taxes, $6.4 billion in federal funds, $800 million in state lottery funds and $80 million in other state funding.

The state General Fund provides 53 percent of school funding, while property taxes and other local revenues provide 35 percent and federal funds provide 12 percent. The state lottery contributes approximately 1.51 percent of this total.

As proposed, the budget General Fund decreases by $896 million (3.2 percent) and local property taxes increase by $635 million (4.8 percent). The budget also reflects a reduction of $202 million (3.1 percent) in federal funds.

Proposition 98

Total Proposition 98 funding for K-12 education in 2003-04 is proposed at $44.1 billion, an increase of $182 million (1.6 percent) over the revised 2002-03 budget.

Table 2
Proposition 98 Summary

(dollars in millions)	2001-02	2002-03 Revised	2003-04 Proposed	$ Change	% Change
General Fund					
K-12 Education	$38,363	$39,297	$39,939	643	1.6
Community Colleges	4,429	4,505	4,063	-442	-9.8
Other Departments	111	109	90	-19	-17.2
Loan Repayment	350	0	0	0	0
Total, General Fund	$29,682	$28,898	$28,225	-672	-2.4
Local Revenue	$13,570	$15,013	$15,868	854	5.7
Total, State and Local Funds	$43,252	$43,911	$44,093	182	.4
Proposition 98 K-12 ADA	5,809,083	5,895,275	5,954,154	58,879	1.0
K-12 funding per ADA (actual)	$6,455	$6,536	$6,708	$172	2.7

As indicated in Table 2, of the total $44.1 billion in Proposition 98 spending proposed for 2003-04, $39.9 billion is attributable to K-12 and $4.1 billion is for Community Colleges. The K-12 share of the Proposition 98 minimum funding level increases by $643 million; whereas Community Colleges funding decreases by $442 million in the budget year.

The 2003-04 budget proposes to provide K-12 education funding that will exceed the Proposition 98 minimum guarantee by an estimated $104 million. In making this estimate, the Department of Finance uses Test 3, as adjusted to reflect the reduction of Child Care funds. The Governor proposes to shift Child Care programs out from under Proposition 98 as a part of a local government realignment proposal in 2003-04.

The number of students in K-12 schools, as measured by unduplicated average daily attendance (ADA), is estimated to increase by 58,879 students in the budget year, an increase of 1.00 percent over the current year. Average per-pupil Proposition 98 funding is estimated to be $6,708 in 2003-04, an increase of $172 over the $6,536 per pupil funding in 2002-03.

Proposed Adjustments to 2002-03 Budget Act

Governor's Proposal

The Governor advanced proposals in December and January to reduce the 2002-03 Budget Act for Proposition 98 by $2.7 billion – including $2.2. billion for K-12 education -- as part of an overall package of $10.2 billion in reductions and adjustments to address a massive state revenue shortfall in the current and budget year.

The Governor's $2.2 billion reduction proposal in the current-year involves three major categories of reductions:

Across -the -Board Reductions -- $1.5 billion. This proposal includes a 2.15 percent reduction to general purpose revenue limits ($612.4 million). The proposal also reduces all education categorical programs ($843.9 million) including a 10.85 percent reduction to most categorical programs and a minimum 3.66 percent reduction for all programs. In addition, the proposal reduces Basic Aid school district revenue limits ($15.3 million) by 2.15 percent.

Other Targeted Programs Reductions – $157 million. The Governor proposes reductions to several specific education programs that include: eliminating State 3 Child Care effective April 2003 (98.6 million), delaying new High Priority Schools grants ($22.6 million), reducing Adult Education funds commensurate with an anticipated audit resolution ($13.5 million), capturing of the ROC/P property tax offset ($11.4 million), eliminating of state funds to support Workforce Investment Act youth services ($7.0 million), eliminate new Healthy Start grants ($2 million) and delete funding for new CSIS consortia ($1.6 million).

Funding Shifts and Deferrals -- $516 million. The Governor proposes to revert unexpended education program funds from previous years ($438 million) to the Proposition 98 Reversion Account and use these funds in 2002-03 to cover the costs of selected education programs – Adult Education and Regional Occupational Centers and Programs (ROC/Ps). In addition, this proposal includes a reduction in state general funds for Stage 3 Child Care ($78.3 million) by using one-time federal funds to offset cover remaining program costs under the Governor's proposal.

Program Savings -- $69.4 million. The Governor proposes reductions numerous programs to reflect natural savings in the program often due to lower than expected participation, unexpected savings, and alignment of program spending with the program services and payment schedules.

The Governor proposed most of these reductions, particularly the across the board reductions and other targeted program reductions, as ongoing reductions that would carry over into the budget-year. The Governor also proposed legislation to provide greater flexibility in the use of reserves to manage the effects of proposed 2002-03 reductions.

Legislative Action:

The Legislature has adopted a revised 2002-03 K-12 education budget, as contained in AB 8X (Oropeza), (First Extraordinary Session). The Legislature's revised plan provides $2.2 billion in reductions and therefore meets the overall level of K-12 education reductions proposed by the Governor. However, these proposals differ in several ways.

First, the Legislature rejected the across–the-board reductions proposed by the Governor totaling $1.5 billion and rejected many of the targeted program reductions proposed by the Governor, including the elimination of Stage 3 Child Care, delay of High Priority Schools grants, reduction of Adult Education funds pending audit resolution, capture of the ROC/P property tax offset, and elimination of new Healthy Start grants.

Secondly, the Legislature identified alternative reduction proposals as contained in AB 8X, including:

$**1.1 billion** in savings resulting from the deferral of P-2 school apportionment payments from the current year to the budget year. This proposal would permanently shift June payments to July each year;

$125.5 million to defer additional education mandate claims from the current year to the budget year;

$103 million reduction in instructional materials funds to delay the requirement that all schools districts purchase instructional materials "fully" aligned to standards;

$76 million to delay payments for the Immediate Intervention/Underperforming Schools (II/USP) and High Priority Schools programs to the budget year;

$75 million in savings for supplemental instruction (summer school).

$11.6 million to temporarily suspend the school library materials program;

$21.8 million to reduce the Peer Assistance and Review program, leaving adequate funds to cover local Beginning Teacher Support and Assessment (BTSA) matches; and

$29.2 million in additional program savings and reversions identified by the LAO.

Third, the Legislature adopted additional statutory language to provide additional flexibility to school districts in accommodating budget reductions. Beyond the reserve flexibility language proposed by the Governor, the Legislature also adopted new language allowing school districts to: tap into their local reserves in the current year, as tied to reductions; provide spending flexibility among the various Supplemental Instruction (summer school) budget items; continue to utilize AB 2519 instructional materials until June 2004; give first priority to instructional materials for English learners and grade 4-8 reading intervention; and eliminate the local match requirement for the deferred maintenance program.

Lastly, while the Legislature adopted a similar level of savings as proposed by the Governor in 2002-03, most of the savings are one-time only and do not continue in 2003-04. In contrast, the Governor proposes most of the 2002-03 reductions as ongoing reductions.

Major Adjustments for 2003-04

- **Growth Funding.** The budget fully funds statutory enrollment growth for apportionments to school districts, county offices of education and special education at a rate of 1.0 percent. The budget provides $358.7 million for apportionment growth, including $321.5 million for school districts, $22.3 million for county offices of education and $37.2 million for special education. The budget does not provide growth for any other categorical programs, except special education.
- **Cost-of-Living Adjustments.** No COLAs are proposed in 2003-04. (See **Program Reductions** below).
- **Deficit Factor**. The budget does not provide a "deficit factor" for revenue limit COLA's reductions that would allow funds to be claimed and restored when economic conditions improved.
- **Restoration of Deferred Appropriations.** A number of education programs had all or some of their payments deferred on a one-time basis in 2002-03. These programs include Home-to-School Transportation, Supplemental Grants, School Improvement Program, and Targeted Instructional

Improvement Grants. In 2003-04, the budget estimates that $315 million (net amount) is needed to restore these appropriations.

- **Equalization.** The budget proposes $250 million for revenue limit equalization. This provides $47 million over the $203 provided pursuant to AB 2781 (Chapter 1167; Statutes of 2002) in 2002-03.
- **Public Employees Retirement System (PERS).** The budget proposes to fund the 9.5 percent increase in the PERS rate, providing a $381.7 million increase in funds for school districts and county offices of education.
- **Unemployment Insurance (UI).** The budget provides $35.2 million to cover reimbursements to local education agencies for UI costs associated with a doubling of the UI rates.
- **Set-Aside for Fiscally Troubled Districts**. The budget provides $102 million in General Funds (non-Proposition 98) as a set-aside to cover possible emergency loans needed to cover fiscally troubled school districts.
- **State Special Schools**. The budget provides $5.3 million to the two California Schools for the Deaf, the California School for the Blind, and the three California Diagnostic Centers to cover costs associated with increased health benefits for employees.

Program Reductions:

- **Cost of Living Adjustments (COLAs).** The budget does not fund cost-of-living adjustments (COLAs) for any education programs – revenue limits or categorical programs -- in 2003-04. This results in a savings of $886 million. The statutory COLA for the budget year is estimated at 1.55 percent.
- **Categorical Growth.** The budget does not provide growth for other categorical programs, except special education, which saves an estimated $106 million in 2003-04.
- **Across-the-Board Reductions.** The 2003-04 budget proposes to continue the across-the-board reductions of 2.15 percent for revenue limits and the 10.85 percent across-the-board reductions for most categorical programs. While not approved by the Legislature in 2002-03, these proposals would result in $1.6 billion in savings if continued in the 2003-04. In addition to these savings, the Governor proposes an additional 1.28 percent reduction for most categorical programs ($51.3 million) and a 3.66 percent reduction to categorical programs that were deferred in 2002-03 ($70.9 million). (Programs exempt from the additional reductions include special education, child nutrition, child development, and K-3 class size reduction.) All together, these across-the-board reductions provide **$1.7 billion** in savings in 2003-04.
- **Mandate Claims.** The budget proposes to continue the deferral of $870 million in new education mandates identified by the Commission on State Mandates and deficiencies identified by the State Controller. (The Legislature approved deferral of an additional $122 million in mandates in 2002-03.)
- **PERS Offset.** The budget does not provide funding to buyout the PERS offset and thereby proposes elimination of the $35 million appropriated pursuant to Chapter 2, Third Extraordinary Session, Statutes of 2002.
- **Basic Aid Funds.** The budget proposes $17.8 million to eliminate Basic Aid funding ($120/ADA) to high property value districts that receive more property tax revenue than is needed to fully fund their revenue limits. The Governor proposes to meet the state's constitutional obligation to provide Basic Aid through the provision of categorical funds to these districts.

- **Property Tax for Basic Aid Districts.** The budget proposes $126.2 million in General Fund reductions from excess property tax from Basic Aid school districts that would be redistributed to offset revenue limit costs for school districts and county office of education.
- **Year Round Schools**. The budget proposes a $18.8 million reduction to the Year Round Schools grant program, which would be eliminated over a four-year period.
- **High Priority (HP) Schools Grants.** The budget reduces $16.8 million to limit participation of first cohort II/USP schools to one year of participation in the HP schools program.
- **Charter School Facilities Grants.** The budget provides a $6.6 million reduction in grants due to reduced demand for leased school facilities.
- **Regional Occupational Centers and Programs (ROC/P's).** A reduction of $12 million is proposed to limit participation in ROC/P programs to students who are in 11^{th} grade (or higher) or who are 16 years old.

Major Issues:

Categorical Programs Cuts Grant. The Governor proposes consolidating more than 64 education categorical programs into a single block grant. This new block grant would provide $5.1 billion redirected from existing categorical programs, as adjusted by the Governor's across-the-board reduction proposals. Legislation would be required to repeal the statutes for all the programs consolidated in the block grant, since the Governor's proposal provides schools with full flexibility in using these funds.

Table 3 provides a listing of all the categorical programs (and related funds) the Governor proposes to collapse into the categorical block grant. The list includes many major categorical programs directed to serve special populations and specific purposes, such as Economic Impact Aid, Adult Education, ROC/Ps, Home-to School Transportation, Targeted Instructional Improvement Grants, and Instructional Materials. Elimination of these categorical programs will be a major issue for the Legislature, as many categorical programs have been established to reflect important educational goals and priorities.

Fourteen categorical programs are excluded from the categorical block grant, including: Special Education, Child Development, Child Nutrition, K-3 Class Size Reduction, Public Schools Accountability Act programs, High Priority Schools Grants, Principal Training, Summer School Programs (Supplemental Instruction), and Math and Reading Professional Development.

Suspension of AB 1781 Maintenance Requirement. The budget assumes suspension of the maintenance requirements under AB 2781, the original 2002-03 budget trailer bill. This bill required the state to restore reductions to Proposition 98 resulting from deferring education categorical program payments in 2001-02 and 2002-03. Under AB 2781, the state would have to restore these funds -- estimated at $3.5 billion -- in one year. The Governor proposes suspending this requirement and paying for these restorations over time, as provided under the Constitution (Proposition 98).

Before and After School Programs. As part of the 2002-03 mid-year reductions, the Administration proposed to reduce funding for the Before and After School Learning and Safe Neighborhoods Partnership Program by $3.9 million Both the Senate and the Assembly concurred in this action and adopted additional reductions identified by the Legislative Analyst, for total programmatic savings of $8.2 million in the current year. In 2003-04, the budget proposes to further reduce the program by $3.9 million, which corresponds to both lower-than-expected participation levels and proposed K-12 categorical reductions.

Child Care Programs

*Background***.** The state makes subsidized child care services available to (1) families on public assistance and participating in work or job readiness, (2) families transitioning off public assistance programs and (3) other families with exceptional financial need. Child care services provided within the California Work Opportunity and Responsibility to Kids (CalWORKs) program are administered by both the California Department of Social Services and the California Department of Education, depending upon the "stage" of public assistance or transition the family is in. Stage 1 child care services are administered by the Department of Social Services for families currently receiving public assistance, while Stages 2 and 3 are administered by the Department of Education. Families receiving Stage 2 child care services are either receiving a cash public assistance payment or are in a two-year transitional period after leaving cash assistance. Families receiving Stage 3 child care services have either exhausted their two-year Stage 2 eligibility or are deemed to have exceptional financial need (the "working poor"). Child care services for Stage 3 are divided into two tiers, General Child Care is available on a limited basis for families with exceptional financial need while the Stage 3 Set-Aside makes child care slots available specifically for former CalWORKs recipients. Under current practice, services to these two populations are supplied by the same group of child care providers; however, waiting lists are kept separate with priority being granted to the former CalWORKs recipients.

Current-Year Reductions. As part of the mid-year (2002-03) reductions, the Governor proposed to eliminate all Stage 3 CalWORKS child care services effective April 1, 2003. Both the Senate and the Assembly denied this request.

Child Care Realignment. As part of the 2003-04 Governor's Budget, the Administration proposes to shift responsibility for the administration, oversight and fiscal management of subsidized child care services (along with other health and human services programs) from the State Department of Education to the local level. The proposed realignment of Child Care is estimated to save the state approximately $1 billion. While the details of the realignment proposal have yet to be determined, under the Administration's initial proposal, federal child care funds would remain with the Department of Education, pending legislation to solidify the realignment proposal. Further, the Department of Education would retain administration of the State Preschool and Before/After School Programs.

Since the Spring of 2000, the Administration has been undergoing a child care policy review with the goal of developing an alternative to the Stage 3 and Stage 3 set-aside programs, thus decreasing the total costs within all stages of child care. Under the current set of programs, the administration estimates that the out-year costs for Stage 3 would exceed more than $650 million by 2004-05. Further, the Administration views the current Stage 3 and Stage 3 set-aside as inequitable and believes that the two-tiered system creates an incentive for families to seek public assistance in order to obtain affordable child care services. In order to remedy these equity and fiscal concerns, the Administration has proposed several options in recent years to implement programmatic and budgetary changes. Each proposal has been met with Legislative opposition. The Governor's new proposal to realign responsibility for child care services from the state to local governments is the most recent of the Administrations efforts to revamp state-subsidized child care.

Special Education Funding Offset. The proposed 2003-04 budget includes $115.6 million ($135.0 million based on most recent estimates) in increased federal funds. As in the current year, these new funds will be treated as an "offset" to state funding and not as an augmentation that would increase special education base funding level by that amount. This offset complies with state law that requires federal funds to be used to supplant state funds in any year that total funding for special education funding is higher than the prior year.

Special Education Maintenance of Effort. The Governor proposes increasing ongoing General Funds for special education by $56.8 million in 2003-04. This includes $12.8 million for growth, which totals $37.2 million in 2003-04, but is offset by $23.6 million in property tax revenues. This General Fund increase also includes $44 million to restore funds the Governor proposed to cut in 2002-03 as a part of the across the board reductions for categorical programs. The Legislature did not adopt this proposal, so this precise action may not be required. Instead, the Legislature took alternative action to reduce the 2002-03 budget by deferring major K-12 apportionment payments from June to July 2003, including $214.1 million for special education. Since this is a permanent, annual deferral of special education payments, the Legislature will need to restore these funds in 2003-04 in order to meet maintenance of effort requirements under the federal special education law.

Realignment Funds & Proposition 98. The Governor proposes $8.3 billion in new tax revenues to cover the costs of local services under a new state-county realignment initiative. As proposed, new taxes would include: $4.5 billion from a one cent sales tax increase, $2.6 billion by increasing 10 and 11 percent personal income tax brackets, and $1.2 billion from a $1.10 increase in the cigarette tax. The Governor maintains that these new state taxes would not generate additional funds to Proposition 98 since they are allocated to local government agencies. As required by the Constitution, Proposition 98 generally captures one-half of the proceeds from new state taxes.

State Mandate Reimbursements. The budget proposes reductions of $870 million by continuing the deferral of several reimbursable education mandates to achieve savings in Proposition 98. By deferring these claims, the state is not eliminating its obligations. The state must eventually pay all claims once audited and approved. The state must also pay interest on overdue claims, based upon the rate established for the Pooled Money Investment Account.

Table 3 – Categorical Programs Included in the Governor's Block Grant Proposal	Proposed 2003-04 Block Grant Amount (in thousands)
Targeted Instructional Improvement Grant	$662,352
Adult Education	500,448
Home-to-School Transportation	467,315
Economic Impact Aid	438,989
Regional Occupational Centers/Programs (ROC/P)	342,307
School Improvement (Grades 1-6)	319,353
Supplemental Grants	229,906
Instructional Materials Block Grant Program/Incentive Grants	204,492
Staff Development Day Buyout	202,176
Deferred Maintenance	181,040
Class Size Reduction (Grade 9)	96,995
Teaching as a Priority Block Grant	78,038
Peer Assistance Review	76,611
Beginning Teacher Support and Assessment (BTSA)	75,403
School Safety lock Grant (8-12)	72,261
School Improvement (Grades 7-12)	66,619
Gifted and Talented	49,769
English Learners Student Assistance	46,832
California School Age Families Education (CalSAFE)	42,998
Charter School Categorical Block Grant	31,383
Community Day Schools	28,350
Elementary school Intensive Reading Program	26,892
Miller-Unruh Reading	25,465

School Library Materials	20,448
Partnership Academies	20,270
Dropout Prevention	19,266
Schools Apportionment, Apprentice Program	13,955
Adults in Correctional Facilities	13,946
Educational Technology – CTAP	13,918
Grade 7-8 Math Academies	11,232
National Board Certification Incentives	10,284
Tenth Grade Counseling	10,073
High Risk Youth Education and Public Safety Program	9,683
Safety -- School Community Policing	8,802
Teacher Recruitment Centers	8,275
Foster Youth Programs	7,705
Local Arts Education Partnership Grant Program	5,706
SAT College Preparation Partnership	4,755
Academic Improvement and Achievement	4,755
Administrator Training	4,650
Specialized Secondary Program Grants	4,521
Small School District Bus Replacement	4,012
Agricultural Vocational Education	3,811
American Indian Education Centers	3,452
Advanced Placement Teacher Training	3,190
Safety -- Plans for New Schools	2,854
Gang Risk Intervention	2,853
Opportunity Programs	2,298
Charter School Facilities Grant	2,254
Inter-segmental Staff Development	1,924
Special Education (Early Intervention for School Success)	1,910
Bilingual Teacher Training	1,583
Advanced Placement Fee Waivers	1,427
International Baccalaureate	943
Child Nutrition Breakfast Startup	880
Safety -- Schools Community Violence Prevention	616
Safety -- Partnership Mini-grants/Safe School Planning	553
Institute for Computer Technology	505
Native American Indian Education	486
Reader Services for the Blind	298
Safety - Conflict Resolution	267
Center for Civic Education	220
Pupil Residency Verification	142
Teacher Dismissal Apportionment	36
California Association of Student Councils	30
Total	**$5,142,451**

6120 California State Library

The State Library provides library and information services to the legislative and executive branches of state government, members of the public, and California public libraries. In addition, the State Library administers and promotes literacy outreach programs such as the California Literacy Campaign, develops technological systems to improve resource sharing and enhance access to information, and administers the Public Library Foundation Act, which establishes a formula under which the State contributes funding for basic local library services.

Current-Year Reductions. As part of his mid-year (2002-03) reductions, the Governor proposed reducing funding (for both 2002-03 and 2003-04) for the Public Library Foundation by 50 percent or $15.8 million. Both houses of the Legislature denied this current year request, but will likely have to revisit this issue for the 2003-04 budget, since the Administration proposes to continue reduction into the next fiscal year.

2003-04 Proposed Reductions. The 2003-04 Governor's Budget proposal is unique in that, if enacted, it would allow local libraries to assess user fees for specific types of library loans, in particular: (1) inter-library loans (up to $5 per book) and (2) "direct loans" which are made to individuals who are not resident's of the library's service area (up to $1 per book). Under current practice, the state helps cover the costs incurred by local libraries for these types of loans. The Administration proposes to eliminate this practice by allowing local libraries to keep the revenue derived from the fees, while reducing General Fund support by $12.2 million.

Further, the Administration proposes to allow the California State Library (CSL) to assess user fees to cover its overall administrative costs. Under this scenario, the CSL would be allowed to require patrons (individuals and governmental entities) to purchase a library card in order to borrow materials or use its services.

HIGHER EDUCATION

6420 California Postsecondary Education Commission

The California Postsecondary Education Commission (CPEC) is a statewide postsecondary education coordinating and planning agency. CPEC serves as the principal fiscal and program advisor to the Governor and Legislature on postsecondary educational policy. CPEC's responsibilities include conducting analyses and making recommendations related to long-range planning for public postsecondary education, and analyzing both state policy and programs involving the independent and private proprietary educational sectors.

As part of the 2003-04 proposed budget, the Administration proposes to dramatically reduce the funding available for the California Postsecondary Education Commission by $1.12 million and 23.5 personnel years, leaving only $700,000 in operational support, 4.5 positions and $5.3 million in grant and federal program dollars. The Administration entertained a similar proposal last year which would have essentially eliminated CPEC; however the Legislature denied the Governor's proposal and appropriated $2.2 million to continue supporting the organization.

6440 University of California

The University of California (UC) was founded in 1868 as a public, state-supported land grant institution and was established constitutionally in 1879 as a public trust to be administered under an independent board, known as the Regents of the University of California. The Board of Regents consists of 20 members appointed by the Governor, one student member appointed by the Board, and seven ex officio members.

The original 1960 Master Plan for Education designates the University of California as the primary state-supported academic agency for research and instruction in the professional fields of law, medicine, dentistry and veterinary medicine. The UC consists of nine campuses--Berkeley, Davis, Irvine, Los Angeles, Riverside, San Diego, San Francisco, Santa Barbara, and Santa Cruz--which offer undergraduate, graduate and professional education. The University of California, San Francisco is solely dedicated to the health sciences, and a tenth campus is currently being planned and constructed outside of Merced in the Central Valley. In addition to its instructional facilities, the University operates teaching hospitals and clinics at the San Francisco and Los Angeles campuses as well as operating the Sacramento, San Diego and Orange county medical facilities.

Current-Year Reductions. As part of the mid-year (2002-03) reductions, the Administration proposed reducing General Fund support for the University of California by $74.3 million specifically targeted at: Academic and Institutional Support ($20 million); Unused Research Funds ($18 million); Student Services ($6.336); AP on-time ($4 million); Student Outreach ($3.33 million); Public Service ($2.5 million); K-12 Internet ($1.1 million) and an unallocated reduction of $19 million.

In order to recoup the funds lost through the current year unallocated reduction ($19 million), the UC Board of Regents voted in December of 2002 to increase student fees by 10 percent annually, or 5 percent for the Spring Term. As is the policy of the Regents, one-third of the new revenue derived from the fee increase will be used to fund financial aid in order to support financially-needy students.

In response to the Administration-proposed reductions, the Legislature has made it clear that it is not supportive of either the reduction to Student Outreach or the full reduction to state-supported research.

Partnership for Higher Education. First initiated in 1995 as a "compact" with then Governor Wilson, the Davis Administration's *Higher Education Partnership Agreement* sought to carry on many of the same principles, including the goal of providing stable funding for public higher education in exchange for the UC and California State University (CSU) commitment to meeting broad accountability goals. Unlike prior Davis Administration budgets which were predicated upon fully-funding the *Higher Education Partnership Agreement* this budget fails to honor that agreement due to the fiscal condition of the State.

While the Partnership Agreement initially promised annual General Fund increases of 5 percent (4 percent base budget increase plus 1 percent for long-term core needs such as maintenance, equipment and libraries), the 2003-04 proposed budget provides the UC with no core Partnership funds. This lack of Partnership support equates to an approximate $186.5 million loss of expected revenue for the UC. While the lack of funding does not equate to a base budget reduction, the $186.5 million revenue loss is included in the Administration's calculation of total budget reductions it proposes for the 2003-04 fiscal year. Further, the loss of Partnership revenue is "real" to the UC, as it relies on this funding source to grow its academic programs and support the student services necessary to accommodate the dramatic spurt in enrollment growth. While the Administration fails to provide Partnership funding, it does fully fund enrollment growth (both in the current year and 2003-04) as well the continuing contractual obligations such as annuitant benefits and debt service.

2003-04 Proposed Reductions. In addition to the lack of expected Partnership revenue, for 2003-04, the Administration proposes to continue the current year reductions and increase the amount being reduced (for cuts totaling approximately $299 million) from the following programs: Academic and Institutional Support (for a total reduction of $36.5 million); Student Outreach (total reduction of $33.3 million, which equates to 50 percent of the Student Outreach budget); Research (total reduction of $28.8 million); Student Services (total reduction of $25.3 million); and Public Service (mainly Cooperative Extension – for a total reduction of $15 million).

In addition, the 2003-04 budget proposes to eliminate all but one of the California Subject Matter Projects, a teacher-training-teacher model of professional development, retaining the Science Subject Matter Project which is presently funded with federal dollars. This action will result in a General Fund savings of $15 million.

The 2003-04 budget contains an additional "unallocated" reduction (total of $194.8 million) which the Administration believes can be "backfilled" with further student fee increases. *(Note: please see discussion of student fees below.)*

Enrollment Growth. The Governor's 2003-04 budget contains $117.2 million in new funding to support a 4.5 percent increase in student enrollment. This funding covers an additional 8,000 Full Time Equivalent (FTE) students in 2003-04 and 5,000 FTE students for which no support was provided in the current year, bringing total budgeted enrollment (all campuses, including health sciences) to 202,628 FTE students.

Student Fees. For the first time in eight years, student fees have been increased (in the current year) at the UC and are proposed to increase further in the 2003-04 budget year. Specifically, student fees were increased by the UC Board of Regents in December by $135 per quarter in order to provide revenue to "backfill" the unallocated reductions to the UC support budget. This brings the total mandatory systemwide fees at UC to $3,834 per year. Additional fees which are assessed on students enrolled in graduate-level professional schools (law, medicine, dentistry, optometry, pharmacy, nursing, veterinary medicine, theater/film/TV) were also increased by the UC Board of Regents and are expected to increase by anywhere from $700 to $2,000 per year, depending on the course of study. Fees at the UC comparison institutions (the universities of Michigan, Illinois, New York, and Virginia) average $6,074, which is $2,057 higher than the fees for UC resident undergraduates. Non-resident tuition, which was increased substantially for 2002-03, is slated to increase by approximately 4 percent for both undergraduate and graduate students.

University of California Student Fees*

	Undergraduate		***Graduate***	
	Resident	Nonresident	Resident	Nonresident
1994-95	$4,111	$11,810	$4,585	$12,284
1995-96	4,139	11,838	4,635	12,334
1996-97	4,166	12,560	4,667	13,061
1997-98	4,212	13,196	4,722	13,706
1998-99	4,037	13,611	4,638	14,022
1999-00	3,903	14,077	4,578	14,442
2000-01	3,964	14,578	4,747	15,181
2001-02	3,859	14,933	4,914	15,808
2002-03	3,859	15,361	4,914	16,236
2002-03*	4,017	16,396	5,017	16,393
2003-04	5,082	18,562	6,196	18,033

Note: Actual fees may vary by campus depending on the particular level of campus-based fees. Data in the table include an average of the campus-based fees for the nine campuses.

* Effective January 2003. UC Regents voted in December 2002 to increase student fees due to budget reductions.

UC Merced. Despite the poor economic conditions of the state and the lack of available General Fund support, the Governor and the UC continue to strive towards opening the new UC Merced campus to students in the Fall of 2004. To meet this end, the 2003-04 budget proposes to allocate an additional $11.3 million for start-up costs associated with the Merced campus.

Specifically, the capital outlay portion of the budget in the current year (2002-03) includes $205.6 million in predominately lease-revenue bond funds for working drawings and construction associated with all phases of site development and infrastructure (specifically related to site grading, drainage, flood control, roadways and utilities) construction of the Science and Engineering Building, the Library/Information Technology Center and the initial classroom and office building. In 2003-04, the Governor's Budget proposes an additional $16.7 million in primarily General Obligation Bonds to continue Phase 3 of the site development and infrastructure, begin planning the logistical support and service facilities and make improvements and renovations to space at the former Castle Air Force Base which will be used to temporarily house various university functions while the campus is being completed.

Capital Outlay. Including the $16.7 million proposed in the 2003-04 budget for the Merced campus, the budget proposes to fund 37 UC capital projects (17 previously approved projects and 20 new projects) using $307.5 million in General Obligation Bonds approved by the voters in November of 2002.

6600 Hastings College of the Law

Hastings College of the Law was founded in 1878 by Serranus Clinton Hastings, California's first Chief Justice, and became affiliated with the University of California in the same year. Policy development and oversight for the college is established and carried out by a board of directors, who are appointed by the Governor for 12-year terms. The juris doctorate degree is granted by the Regents of the University of California and signed by both the University of California President and the Dean of Hastings College of Law.

Current-Year Reductions As part of the mid-year reductions proposed by the Administration, funding for Hastings College of Law was reduced by $1 million. For 2003-04, the Administration proposes total reductions of $4.1 million (from a $14.4 million base General Fund budget in 2003-04). Unlike reductions proposed for UC and the California State University, the reductions slated for Hastings College of Law are targeted at specific academic functions (rather than leaving the allocation of the reductions up to the Hastings College of Law Board of Directors) and will impact the core educational function of the college. Specifically, the Administration targets the reductions at law library and scholarly journal acquisitions, Moot Court travel costs, and prescribes that the college will replace visiting professors with adjunct professors.

In addition, the Administration anticipates that Hastings will increase student fees (commensurate with the differential fee adopted by the UC Regents for students enrolled in Law programs) and collect an additional $4.5 million to offset the reductions proposed in the Governor's Budget.

6610 California State University

The California State University (CSU) system is composed of 22 campuses, including 21 university campuses and the California Maritime Academy. Administered and managed by an independent governing board of Trustees, the CSU has achieved a high level of academic excellence through distinguished faculty and high-quality undergraduate- and graduate-level instruction. Each campus in the system is unique, with its own curriculum and character; however, all campuses require a basic "general education" breadth curriculum regardless of the institution or baccalaureate-level major of study. In addition to providing baccalaureate- and masters-level instruction, the CSU trains approximately 60 percent of California's K-12 teachers and administrators, and in limited circumstances, has the ability to jointly offer doctoral-level education with the University of California and private and independent institutions.

Current-Year Reductions. As part of the mid-year (2002-03) reductions, the Administration proposed reducing General Fund support for the California State University by $59.6 million. While the reductions to other higher education institutions were targeted at specific programs, the reduction to the CSU was "unallocated" and as such, the allocation of the cuts was left to the discretion of the CSU Board of Trustees. The Trustees acted to partially address the current-year shortfall by reducing funding for technology equipment, libraries, and scheduled maintenance as well as reducing support for administration, travel and filling only critically-needed staff positions. The remainder of the cuts (approximately $20 million) are being "backfilled" by an increase in student fees, which was approved by the CSU Board of Trustees in December 2002. *(Note: please see discussion of student fees below.)*

Partnership for Higher Education. First initiated in 1995 as a "compact" with then Governor Wilson, the Davis Administration's *Higher Education Partnership Agreement* sought to carry on many of the same principles, including the goal of providing stable funding for public higher education in exchange for the UC and California State University (CSU) commitment to meeting broad accountability goals. Unlike prior Davis Administration budgets which were predicated upon fully-funding the *Higher Education Partnership Agreement* this budget fails to honor that agreement due to the fiscal condition of the State.

While the Partnership Agreement initially promised annual General Fund increases of 5 percent (4 percent base budget increase plus 1 percent for long-term core needs such as maintenance, equipment and libraries), the 2003-04 proposed budget provides the CSU with no core Partnership funds. This lack of Partnership support equates to an approximate $132.6 million loss of expected revenue for the CSU. While the lack of funding does not equate to a base budget reduction, the $132.6 million revenue loss is included in the Administration's calculation of total budget reductions it proposes for the 2003-04 fiscal year. Further, the loss of Partnership revenue is "real" to the CSU, as it relies on this funding source to grow its academic programs and support the student services necessary to accommodate the dramatic spurt in enrollment growth. While the Administration fails to provide Partnership funding, it does fully fund enrollment growth (both in the current year and 2003-04) as well the continuing contractual obligations such as annuitant benefits, debt service and increased PERS costs.

2003-04 Proposed Reductions. In addition to the lack of expected Partnership revenue, for 2003-04 the Administration proposes to increase base budget reductions to the CSU to a total of $324.6 million, and does so by imposing the following targeted reductions: Student Services Funding ($53.2 million); Academic and Institutional Support ($58.1 million); Student Outreach($12.6 million); Cal Teach ($2 million); Unallocated Base Budget Reduction (142.8 million); Increase class size (Student-to-Faculty Ratio) ($53.5 million).

Enrollment Growth. The Governor's 2003-04 budget contains $150.8 million in new funding to support a 5.0 percent increase in student enrollment. This funding covers an additional 16,056 Full Time Equivalent (FTE) students in 2003-04 and 8,000 FTE students for which no support was provided in the current year, bringing total budgeted to 338,872 FTE students.

Student Fees. For the first time in eight years, student fees have been increased (in the current year) at the CSU and are proposed to increase further in the 2003-04 budget year. Specifically, student fees were increased by the CSU Board of Trustees in December by $72 per term in order to provide revenue to "backfill" the unallocated reductions to the CSU support budget. Further fee increases are expected in 2003-04, which would bring the total mandatory systemwide fees at CSU to $2,466 per year for a full-time undergraduate student and $1,410 per year for a part-time undergraduate student. Fees at the CSU comparison institutions average $4,584 which is $2,118 higher than the fees for CSU resident undergraduates.

Capital Outlay. In addition to the $188 million worth of project being funded in 2003-04 with lease-revenue bond funds, the budget proposes to fund 8 additional CSU capital projects (3 previously approved projects and 5 new projects) using $192 million in General Obligation Bond funds approved by the voters in November of 2002.

6870 California Community Colleges

The California Community College system (CCC) provides a variety of general and vocational education program at 108 community colleges throughout the state. The CCC offers academic programs that (1) emphasize transfer courses for students continuing their education at CSU, UC or other institutions of higher education, (2) provide vocational training to enhance the education of California's work force, and (3) offer courses to students who need or desire basic education courses. In addition, the CCCs are also charged with administering many of the state's economic development programs.

Current-Year Reductions. As part of the mid-year reductions, the Governor proposed reducing funding for the California Community College system by $288 million. Included in this amount is a $50.9 million "swap" which would change the funding source for the Extended Opportunity Programs and Special Services (EOPS) from General Fund (Prop. 98) to the Proposition 98

Reversion Account. Also included under this reduction proposal is an ongoing $80 million cut to the community colleges for alleged concurrent enrollment abuses (involving K-12 students enrolling in unauthorized community college classes).

Both the Assembly and Senate have voted to approve a total of $174.6 million in mid-year reductions for the community colleges, which include:

-- $129 million in programmatic/categorical program reductions to the community colleges. These reductions were both identified and "approved" by all the various community college constituency groups. Included in the package adopted by the Legislature is a $12 million augmentation to reduce the impact of the reductions on the Basic Skills program.

-- $33.3 million "swap" which changes a portion of the funding source for the Partnership for Excellence Program - from General Fund (Proposition 98) to Proposition 98 Reversion Account.

-- The Legislature denied the Governor's proposal to cut $80 million for K-12 concurrent enrollment.

2003-04 Proposed Reductions. In the 2003-04 budget year, the Governor proposes to further reduce funding for the California Community Colleges above the amount proposed in the current year. Additional reductions include: $60.3 million for an across-the-board 7.46 percent reduction to all community college categorical programs and $211.5 million for reductions targeted at: the Partnership for Excellence; Student Outreach; EOP services; Matriculations; Part-Time Faculty Office Hours; Economic Development; Building Maintenance and Repairs; Instructional Equipment and Library Materials. Additional reductions include a $3.2 million cut from Student Outreach, which represents 50 percent of the program's budget; further, the Administration does not provide a COLA to either the community colleges or K-12.

Enrollment Growth. The Governor's 2003-04 budget proposes to provide $115.7 million to fund a three percent increase in student enrollment growth. While UC and CSU are proposed to be fully-funded for enrollment growth of five and 4.5 percent respectively, for both 2003-04 and 2002-03, community college enrollment funding has continuously failed to keep pace with actual student enrollment, as is evidenced by the over 60,000 full time equivalent students (FTES) currently enrolled on community colleges campuses throughout the state.

Student Fees. For 2003-04, the Governor proposes to increase student fees over 100 percent, from $11 per unit to $24 per unit, increasing the cost for a full-time student from $396 per semester to $864. Although the Governor's budget states that the fee increase is necessary to "continue providing a quality education and maintain access amidst weak economic conditions", the $149 million in revenue which is expected to result from the fee increase does not remain on the campuses but flows back to the General Fund (through a General Fund offset).

At present, approximately 40 percent of community college students are be eligible for Board of Governor (BOG) Student Fee Waivers, and the Administration believes that this percent will likely remain constant. However, the Administration also believes that the fee increase will lead a substantial number of students to drop out (or simply fail to enroll). In anticipation of this attrition, the Governor's Budget cuts core instructional funding for the community colleges by an additional $215 million.

Proposition 98 "Split" The community college share of the Proposition 98 guarantee is slated to decrease substantially from approximately 10.2 percent in the current year (2002-03) to 9.22 percent.

Capital Outlay. The Governor's 2003-04 Budget proposal includes $526 million in General Obligation Bond funds, approved by the voters in November of 2002, for 45 previously approved projects and 52 new projects.

7980 Student Aid Commission

The Student Aid Commission (SAC) administers federal and state student financial aid programs including grants, work study, and loan programs for postsecondary students attending California educational institutions. The SAC provides leadership on financial aid issues and makes policy recommendations concerning student financial aid programs. In addition, the SAC compiles information on student financial aid issues, evaluates financial aid programs compared to the needs of the state's student population and, provides financial aid information to students, parents and California's education community.

Background. In 2000 the Legislature passed and the Governor signed into law SB 1644 (Chapter 403, Statutes of 2000) which dramatically expanded the scope of the Cal Grant program and re-tooled the eligibility criteria to ensure that all financially needy and academically meritorious students are guaranteed a grant to attend college. Under the new Cal Grant Entitlement Program all graduating high school students who meet specified grade point average (GPA) and income requirements are guaranteed a state grant for up to four years. Cal Grant awards generally cover the cost of fees at public colleges and are worth up to approximately $8,000 to $9,000 at private colleges and universities. In addition, the Cal Grant B, which is provided to students with exceptional financial need, includes a living allowance of approximately $1,551 per year.

To be eligible for a Cal Grant A award, a student must have a minimum GPA of 3.0 ("B" average) and must not exceed the family income limit, which is approximately $66,000 for a family of four or $77,000 for a family of six. Students with GPAs under 3.0, but higher than a 2.0 ("C" average), are eligible for a Cal Grant "B" award provided their annual family income does not exceed $34,800 for a family of four. In addition, community college students meeting specified GPA and income requirements, who are transferring to a four-year college or university, prior to age 24 years, are also eligible to receive an award. Students who did not qualify for the Cal Grant Entitlement Program (either due to age, GPA or income requirements) have a "second chance" to receive a Cal Grant and are eligible to compete for a bloc of 22,500 annual awards, provided they are now financially and academically eligible. Of the 22,500 awards, 11,250 are reserved specifically for community college students.

2003-04 Proposed Adjustments. As part of the Governor's 2003-04 Budget proposal, the Cal Grant A and B programs are slated to increase by approximately $48.3 million to cover the proposed student fee increases at public postsecondary institutions. In contrast, the Administration proposes to reduce -- by nine percent -- the maximum Cal Grant award paid to students attending private colleges and universities. At present, the current maximum award is $9,708, that amount will be decreased to $8,832 for new Cal Grant recipients electing to attend a private institution.

As part of the Governor's budget reduction measures, the 2003-04 budget proposes to eliminate the California Workstudy Program, reduce the number of Cal Grants for vocational students (Cal Grant C) by 3,040 leaving 7,690 awards available annually, and further reduce the number of Cal Grant T awards for teacher credentialing students by 540 (from 1,390 to 850 awards available annually).

SUBCOMMITTEE NO. 2

NATURAL RESOURCES, ENVIRONMENTAL PROTECTION,
PUBLIC SAFETY, ENERGY and GENERAL GOVERNMENT

Natural Resources

Environmental Protection

Public Safety

Energy

General Government

NATURAL RESOURCES

OVERVIEW

The Resources Agency is responsible for the state's policies, programs, and activities relating to the conservation, management, and enhancement of California's natural and cultural resources. The agency consists of the following 22 state departments, boards, commissions, and conservancies:

- Baldwin Hills Conservancy
- Coachella Valley Mountains Conservancy
- Coastal Commission
- Colorado River Board
- Conservation Corps
- Department of Boating and Waterways
- Department of Conservation
- Department of Fish and Game
- Department of Forestry and Fire Protection
- Department of Parks and Recreation
- Delta Protection Commission
- Department of Water Resources
- Energy Resources Conserv & Dev. Commission
- Native American Heritage Commission
- San Francisco Bay Conserv. & Dev. Commission
- San Gabriel Mountains/Lower Los Angeles River Conservancy
- San Joaquin River Conservancy
- Santa Monica Mountains Conservancy
- State Lands Commission
- Tahoe Conservancy
- Wildlife Conservation Board
- San Diego River Conservancy

The budget proposes a total of $4.0 billion ($698 million, General Fund) for all Resources Agency programs (not including capital outlay). This is a decrease of $1.0 billion (20.2 percent) from the 2002-03 budget. Please note that these figures do not factor in general obligation bond debt financing when calculating total expenditures.

All Resources Agency Budgets Summary of Expenditures (dollars in thousands)	2002-03	2003-04	Change: Dollar	Change: Percent
General Fund	818,801	698,009	-120,792	14.8
Special Funds	1,208,193	1,262,676	54,483	4.5
Selected Bond Funds	2,785,376	1,862,294	-923,082	33.1
Federal Funds	209,418	182,239	-27,179	13.0
Total	5,021,788	4,005,218	-1,016,570	20.2

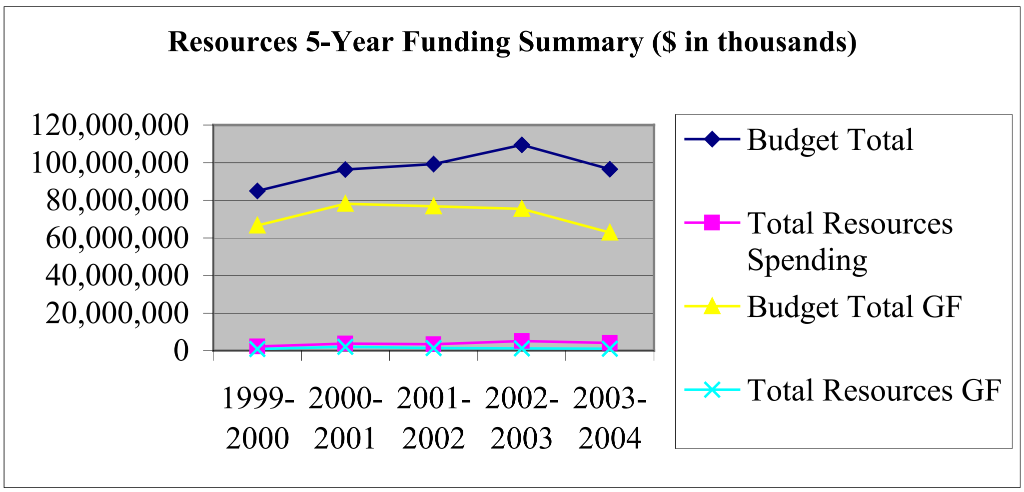
Issues

Funding for Natural Resources Programs

Resources will face a significant reduction in spending when looking at the Governor's proposed mid-year reductions, and the 2003-2004 budget proposals. Specifically, the total proposed reductions for all Resources Agency departments, boards, and commissions, are as follows:

2002-2003 Mid-Year Reductions		2003-2004 Proposed Reductions	
General Fund	$143,622,000	General Fund	$203,572,000
Special Funds	$52,045	Special Funds	$70,527

Compared to the reductions proposed in other areas of the budget, the dollar amounts associated with the natural resources section do not appear to be that drastic. However the Legislature has been forced to significantly reduce General Fund support for natural resource programs for three consecutive years. As we consider the 2003-2004 budget proposals, a question for the Legislature to consider is what effect these cuts will have had on natural resources programs.



Key Points to Consider

- Total spending for natural resources has increased from $2.2 billion in 1999-2000, to $4.1 billion in 2003-2004
- As a percentage of the total state budget, natural resources spending has increased from 2.6 percent in 1999-2000 of the budget to 5.3 percent of the budget in 2003-2004.
- Total General Fund spending for natural resources has increased from $926 million in 1999-2000, to $958 million in 2003-04
- As a percentage of total General Fund spending, natural resources GF spending has decreased from 1.8 percent in 1999-2000, to 1.5 percent in 2003-2004.

The numbers over the five-year are somewhat misleading for a couple of reasons. First, total spending for natural resource increased over this five-year period due in large part to the passage of Propositions 12 (2000), 13 (2000), 40 (2002), and 50 (2002). In total, voters have approved over $10 billion in natural resources bonds since the calendar year 2000. Subsequent to the passage of these bonds, the

Administration and the Legislature have adopted relatively aggressive expenditure schedules to allocate the bond funds.

Second, although total General Fund spending has slightly increase by $32 million over the five-year period, the increase is attributable to one area. The Governor's budget summary includes debt service on general obligation bonds when factoring total General Fund spending. In the 99-00 fiscal-year, the debt service on natural resources bonds was $199 million. In the 2003-2004 proposed budget, the debt service is estimated to be $260 million. So if the debt service is not considered, total GF spending for natural resources has decreased by $29 million.

Total General Fund spending for natural resources is proposed at $698 million for the 2003-04 budget-year. Five years ago (1999-2000), the state spent $726 million. Without factoring in for population growth, newly created programs, and inflation, the state spends less on natural resource programs.

When compared to spending five years ago, the perception of natural resources programs tends to center around land acquisitions and park openings, but vital programs have been established to protect and preserve the state's natural and cultural resources. Programs such as timber harvest plan review, enforcement, and regulating coastal development are all vital programs for the state. When compared to health care or public safety, natural resources may not warrant priority status, but determining how much of a priority resources programmatic funding should be an issue worth pursuing.

Proposition 50 Bond Funds Proposed in the Budget

The 2003-04 proposed budget utilizes approximately $1.1 billion in Proposition 50 bond funds. Proposition 50, The Water Security, Clean Drinking Water, Coastal and Beach Protection Act of 2002 authorizes $3.4 billion in general obligation bonds for various water projects and programs. Listed below is a brief summary of the bond elements, and the Governor's Proposition 50 proposals for the 2003-04 budget-year.

Water Security **$50,000,000**
Water security funds are discretionary to the extent that no water security program currently exists. The Legislature can appropriate these funds for projects that protect state, local, and regional drinking water systems from terrorist attack or deliberate acts of destruction or degradation.

<u>The budget proposes $15.1 million from the Water Security fund for 2003-2004.</u>

Safe Drinking Water **$435,000,000**
Safe drinking water funds are available to the Department of Health Services for grants and loans for infrastructure improvements designed to meet safe drinking water standards. Examples of the types of projects and grants that are eligible for funding include the following:

- Grants to small community drinking water systems to upgrade monitoring, treatment, or distribution infrastructure.
- Grants for the development of new technologies and related facilities for water contaminant removal and treatment.
- Grants for community water quality monitoring facilities and equipment.
- Grants for drinking water source protection.
- Grants for treatment facilities necessary to meet safe drinking water standards.

To help address the water demand issues, 60 percent of these funds can also be used for grants to Southern California water agencies to assist in meeting the state's commitment to reduce Colorado River water use to 4.4 million acre feet per year.

The budget proposes $102.1 million from the Safe Drinking Water fund for 2003-04.

Clean Water and Water Quality **$370,000,000**

These funds are scheduled as follows:

- $100 million to the Water Resources Control Board (SWRCB) for competitive grants for the following purposes:
  (1) Water pollution prevention.
  (2) Water reclamation.
  (3) Water quality improvement.
  (4) Water quality blending and exchange projects.
  (5) Drinking water source protection projects.
  (6) Projects to mitigate pathogen risk from recreational uses at drinking water storage facilities.
- $100 million to the Resources Agency Secretary for River Parkways projects.
- $40 million to the Tahoe Conservancy for land and water acquisition, development, and restoration to improve the water quality of Lake Tahoe.
- $100 million to the Water Board for projects that restore and protect the water quality and environment of coastal waters, estuaries, bays and near-shore waters, and groundwater. Of these funds, a minimum of $20 million is appropriated for projects in the Santa Monica Bay Restoration Plan.
- $30 million to the Secretary for Resources for water quality and land acquisition projects in the Sierra Nevada-Cascade Mountain Region.

The budget proposes $87.9 million from the Clean Water and Water Quality fund for 2003-04.

Contaminant and Salt Removal Technologies **$100,000,000**

The funds in this account are available the Department of Water Resources (DWR) to award grants for desalination projects. To qualify for these funds, a grant recipient must satisfy a 50 percent match requirement of non-state source revenues for the project.

The budget proposes $27.0 million from the Contaminant and Salt Removal Technologies fund in 2003-04.

CALFED Bay-Delta Program **$825,000,000**

Proposition 50 supports the state's ongoing commitment to the CALFED Bay-Delta Program. Key components of the proposal include $180 million for each of the following CALFED program elements: water supply reliability, ecosystem restoration, and water use efficiency.

The budget proposes $306.6 million from the CALFED fund in 2003-04. Additionally, the 2002-03 current-year budget contains $46.6 million of Prop 50 funds for CALFED.

Integrated Regional Water Management **$640,000,000**

The allocation of Integrated Regional Water Management funds will likely require legislation to establish and implement this new program. As stated in the bond, the funds in this account are intended to protect communities from drought, protect and improve water quality, and improve local water security. Fifty percent (50%) of these funds are allocated to the SWRCB to select projects that meet certain requirements, including projects that are consistent with approved integrated water management plans, and projects that include local matching funds. Other restrictions on these funds include prohibiting projects that include an on-stream surface water storage facility, or an off-stream surface water storage facility other than percolation ponds for groundwater recharge in urban areas.

The budget proposes $93.7 million from the Integrated Regional Water Management fund in 2003-04.

As part of this account, the Wildlife Conservation Board (WCB) will receive $140 million for projects and grants that protect water quality and improve water supply reliability.

The budget proposes $60.2 million to the WCB in 2003-04.

Colorado River **$70,000,000**
Twenty million ($20,000,000) of these funds are available to DWR for canal lining and other projects designed to reduce the state's use Colorado River water. Fifty million ($50,000,000) of the funds are available to the WCB for acquisition, protection, and restoration of land and water resources that help satisfy the states' limit on Colorado River water.

The budget proposes $54 million from the Colorado River fund in 2003-04.

Coastal Watershed and Wetland Protection **$200,000,000**
The Coastal Watershed and Wetland Protection funds are available for grants and/or projects that protect coastal watersheds. The allocation of these funds are as follows:

- $120,000,000 million to the State Coastal Conservancy
- $20,000,000 million for the San Francisco Bay Conservancy Program
- $40,000,000 million to the Santa Monica Mountains Conservancy, of which $20,000,000 is for the protection of the Los Angeles River watershed (north of the City of Vernon), and $20,000,000 million for the Santa Monica Bay and Ventura County coastal watersheds.
- $20,000,000 million for the San Gabriel and Lower Los Angeles Rivers and Mountains Conservancy.

The budget proposes $46.0 million from the Coastal Watershed and Wetland Protection fund for 2003-04.

Wildlife Conservation Board **$750,000,000**
Proposition 50 authorizes $750 million, continuously appropriated, to the WCB for acquisition, protection, and restoration of coastal wetlands, upland areas adjacent to coastal wetlands, and coastal watershed lands. The bond specifies that $300 million must be spent on projects within Los Angeles, Santa Barbara and Ventura Counties, and $200 million must go to projects in the San Francisco bay area. The WCB can also acquire at least 100 acres of upland mesa areas adjacent to the state ecological reserve in the Bolsa Chica wetlands in Orange County.

The budget proposes $272.0 million to the WCB in 2003-04. The Administration has also scheduled approximately $170.7 million of the WCB fund in the 2002-03 fiscal-year.

Selected Issues with Proposition 50 Proposed Expenditures

Although the Governor's budget was released in early January, the committee recently received the Administration's Proposition 50 expenditure plan. To avoid doing a cursory review of the Governor's plan, the following issues have been identified for the subcommittee to consider. As the subcommittee begins its process to consider the Governor's proposed expenditures, additional issues will likely develop. The following issues are not intended to be exhaustive or final, but rather these issues may serve as a starting point as the subcommittee formulates its plans to allocate Proposition 50 bond funds.

1. **Various bond elements will require legislation to establish program requirements and coordination.** For example, the Water Security and Integrated Regional Water Management funds do not have existing or a comparable programs to administer the funds. Although the SWRCB will receive half of the Integrated Water Management funds, the broad project criteria for these funds highlight the need for enabling legislation to establish this program. Additional funds may also require legislation or trailer bill language, however these two programs are fairly discretionary and appear to have the greatest need for program definition.

2. **River Parkway Program Continues to Receive Significant Amount of Bond Funds.** In Propositions 12, 13 and 40, the past three natural resources bonds, river parkway funds were available for urban creek protection, restoration, and enhancement, and for acquisition and restoration of riparian habitat, riverine aquatic habitat, and other lands in close proximity to rivers and streams and for river and stream trail projects. The language in Proposition 50 does not provide any further direction or guidance on the use of these funds.

   Since 2000 and the aforementioned Propositions (12, 14, and 40), and including funds in Proposition 50, river parkways have received over $300 million. The issue for the Legislature to consider is whether it is desirable to spend these funds through project lists that are proposed by the Administration and without much legislative input. Or, should the Legislature assert more control over this program and establish a more comprehensive program with a long-term approach to improving river parkways.

3. **Coordination is Needed for Watershed and Coastal Protection Programs.** In total Proposition 50 contains approximately $900 million for coastal protection programs, however most of these funds are spread across the Resources Agency and CalEPA. Both agencies and their respective departments, boards, commissions, etc, contribute a specific working knowledge and experience of how to maximize coastal protection programs. To ensure that the state is utilizing the valuable resources of these agencies, and to avoid duplicative work and/or redundancy, the subcommittee should consider establishing a structure to coordinate the use of coastal protection bond funds.

0540 Secretary for Resources

The Secretary for Resources has administrative responsibility for the 21 state departments, boards, commissions, and conservancies within the Resources Agency. The budget proposes total expenditures of $54.3 million ($1.3 million, General Fund), a decrease of $386.2 million from the current-year budget. This decrease is attributable to a reduction in the Bay-Delta Ecosystem Restoration Account. Funds in this account are now administered by the CALFED Bay-Delta Authority.

Highlights

The Secretary for Resources budget contains the following key items:

- $25 million from Proposition 50 for the River Parkways Program. Proposition 50 authorizes a total of $100 million for the program.

- $7 million from Proposition 50 for Sierra Nevada-Cascade Mountain grants. Proposition 50 authorizes a total of $30 million in grants for acquisitions for land and water resources in the Sierra Nevada-Cascade Mountain region.

- $12.7 million from Proposition 40 for the River Parkways and Urban Streams Restoration Programs.

3340 California Conservation Corps

Fund Source (dollars in thousands)	2002-03	2003-04	Change Dollars	Change Percent
General Fund	$45,688	$36,815	($8,873)	-19.4
Safe Neighborhood Parks, Clean Water, Clean Air & Coastal Protection Bond Fd	3,525	3,525	0	0.0
CA Environmental License Plate Fund	317	308	(9)	-2.8
Public Resources Account, Cigarette and Tobacco Products Surtax Fund	277	285	8	2.9
Collins-Dugan California Conservation Corps Reimbursement Account	33,949	27,320	(6,629)	-19.5
Federal Trust Fund	495	503	8	1.6
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Fund	4,071	5,224	1,153	28.3
Total	$88,322	$73,980	($14,342)	-16.2

Issue

Corps Member Health Benefits

The Governor proposes to reduce the Conservation Corps' General Fund budget by $8.9 million (19.4 percent) for the 2003-2004 budget-year. As stated in the department's mission statement, corps members provide numerous services that protect and enhance the state's natural resources, environment, and residential communities. More importantly, the Corps provides valuable job training and education to young men women who live in disadvantaged communities.

Since the 2001-02 fiscal-year, the corps General Fund budget has been reduced by $23.4 million; additionally the corps overall budget has been reduced by $11.4 million during the same time period. As part of the proposed 25 percent General Fund reduction for the 2003-04 budget-year, the Governor proposes the following:

- Eliminate health benefits to corps members: $2.3 million
- Lay off field administrative staff: $3.2 million
- Reduce operating expenses: $3.3 million
- Close two fire centers: $1.9 million

- Eliminate local corps contracts: $846,000

Although the dollar amount associated with these reductions may not appear to be significant, the proposal to eliminate corps member health benefits is not worth the limited General Fund savings. As the subcommittee considers the corps budget, staff will recommend denying the elimination of health benefits for corps members.

3480 Department of Conservation

The Department of Conservation (DOC) protects public health and safety, ensures environmental quality, and supports the state's long-term viability in the use of California's earth resources. The Department performs numerous functions relating to agricultural and open space lands and soils; beverage container recycling; geology and seismology; and mineral, geothermal, and petroleum resources.

The budget proposes total expenditures of $541.1 million ($5.4 million, General Fund), a decrease of $13.6 million (2.5 percent) from the current-year budget.

Fund Source (dollars in thousands)	2002-03	2003-04	Change Dollars	Change Percent
General Fund	$21,435	$5,396	($16,039)	-74.8
Safe Neighborhood Parks, Clean Water, Clean Air & Coastal Protection Bond Fd	21,862	473	(21,389)	-97.8
Surface Mining and Reclamation Account	1,938	841	(1,097)	-56.6
State Highway Account, State Transportation Fund	12	12	0	0.0
California Beverage Container Recycling Fund	408,847	416,672	7,825	1.9
California Environmental License Plate Fd	0	0	0	0.0
Soil Conservation Fund	1,298	1,308	10	0.8
Glass Processing Fee Account, California Beverage Container Recycling Fund	37,529	38,398	869	2.3
Hazardous and Idle-Deserted Well Abatement Fund	100	100	0	0.0
Bi-Metal Processing Fee Account, California Beverage Container Recycling Fund	16	16	0	0.0
PET Processing Fee Account, California Beverage Container Recycling Fund	44,689	44,784	95	0.2
Mine Reclamation Account	1,498	1,313	(185)	-12.3
Seismic Hazards Identification Fund	1,913	3,206	1,293	67.6
Strong-Motion Instrumentation Special Fund	3,271	4,450	1,179	36.0

Federal Trust Fund	1,665	1,685	20	1.2
Bosco-Keene Renewable Resources Investment Fund	0	680	680	100.0
Reimbursements	8,238	8,476	238	2.9
Oil, Gas, and Geothermal Administrative Fund	0	12,884	12,884	100.0
Agriculture and Open Space Mapping Subaccount	450	444	(6)	-1.3
Total	$554,761	$541,138	($13,623)	-2.5

Highlights

The Governor proposes the following:

- $965,000 augmentation for increased enforcement and fraud prevention in the Beverage Container Recycling Program. This proposal will add one staff member to the seven-member Los Angeles fraud investigative, as well as create an additional eight-member team.
- $80 million loan from the Beverage Container Recycling Fund (BCRF) to the General Fund. The BCRF is estimated to have a $522,000 fund balance in the 2003-2004 budget-year.
- $3.7 million General Fund reduction. The proposed reduction will effect the following programs:

  Eliminate North Coast Watershed Assessment ($1.8 million)
  Reduce Regional Geological Hazards Mapping ($693,000)
  Reduce Geological Publications Unit ($600,000)
  Reduce Mineral and Hazardous Mineral Classification Program ($425,000)
  Eliminate grants to Resource Conservation Districts ($120,000)
  Reduce out-of-state travel ($55,000)

3540 Department of Forestry and Fire Protection

The Department of Forestry and Fire Protection (CDF), under the policy direction of the Board of Forestry, provides fire protection services for timberlands, rangelands, and brushlands. The Department regulates timber harvesting on state or privately owned forestland and also provides a variety of resource management services for owners of forestlands, rangelands, and brushlands.

The Office of the State Fire Marshall is responsible for protecting life and property from fire through the development and application of fire prevention engineering, enforcement, and education regulations. The State Fire Marshall also trains and certifies fire service personnel throughout the state.

The budget proposes total expenditures of $603.7 million ($413.3 million, General Fund) a decrease of $52.6 million (8.0 percent) from the current-year budget.

Fund Source (dollars in thousands)	2002-03	2003-04	Change Dollars	Change Percent
General Fund	$482,306	$413,298	($69,008)	-14.3
Safe Neighborhood Parks, Clean Water, Clean Air & Coastal Protection Bond Fd	0	0	0	0.0
State emergency Telephone Number Account	1,505	1,406	(99)	-6.6
Unified Program Account	0	2,568	2,568	0.0
State Fire Marshal Licensing and Certification Fund	310	301	(9)	-2.9
California Fire and Arson Training Fund	1,891	1,810	(81)	-4.3
California Hazardous Liquid Pipeline Safety Fund	469	618	149	31.8
California Environmental License Plate Fd	1,581	1,564	(17)	-1.1
California Hazardous Liquid Pipeline Safety Fund	2,240	2,211	(29)	-1.3
Public Resources Account, Cigarette and Tobacco Products Surtax Fund	389	384	(5)	-1.3
Professional Forester Registration Fund	190	188	(2)	-1.1
Federal Trust Fund	20,122	22,508	2,386	11.9
Forest Resources Improvement Fund	0	11,514	11,514	0.0
Timber Tax Fund	28	28	0	0.0
Reimbursements	144,205	144,038	(167)	-0.1
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Fund	1,000	1,000	0	0.0
Water Security, Clean Drinking Water, Coastal and Beach Protection Fund of 2002	0	240	240	0.0
Total	$656,236	$603,676	($52,560)	-8.0

Highlights

The Governor proposes the following items for the department:

- $2.25 million (Federal Funds) expenditure authority for the Joint Agency Climate Team (JACT). The JACT is multi agency program that will develop a climate change strategy for the state. Through this budget proposal, the department will focus on the following initiatives:

  Support research and development in renewable technologies
  Support research in carbon sequestration
  Enhance the state's capacity to project future climates, assess impacts, and evaluate solutions

- $3.5 million reduction to the Forest Resources Improvement Fund (FRIF) due to a revenue reduction on forest products from the State Forest System. The proposal calls for the elimination of FRIF funding for the North Coast Watershed Assessment program.

3600 Department of Fish and Game

The Department of Fish and Game (DFG) administers programs and enforces laws pertaining to the fish and wildlife resources of the state. The Fish and Game Commission sets policies to guide the department in its activities and regulates the sport taking of fish and game. The DFG currently manages approximately 160 ecological reserves, wildlife management areas, habitat conservation areas, and interior and coastal wetlands throughout the state.

The budget proposes total expenditures of $275.8 million ($41.2 million General Fund), an increase of $4.5 million (1.7 percent) from the current-year budget. The proposed spending increase is attributable to Federal Trust Fund and reimbursement authority increases.

Fund Source			Change	
(dollars in thousands)	2002-03	2003-04	Dollars	Percent
General Fund	$48,651	$41,167	($7,484)	-15.4
Safe Neighborhood Parks, Clean Water, Clean Air & Coastal Protection Bond Fd	1,022	701	(321)	-31.4
California Environmental License Plate Fd	19,538	17,796	(1,742)	-8.9
Fish and Game Preservation Fund	94,598	90,896	(3,702)	-3.9
Fish and Wildlife Pollution account	2,371	2,392	21	0.9
California Waterfowl Habitat Preservation Account, Fish and Game Preservation Fun	207	207	0	0.0
Exotic Species Control Fund	871	877	6	0.7
Public Resources Account, Cigarette and Tobacco Products Surtax Fund	0	0	0	0.0
Oil Spill Prevention and Administration Fund	17,125	20,261	3,136	18.3
Oil Spill Response Trust Fund	0	0	0	0.0
Environmental Enhancement Fund	104	1,001	897	862.5
The Salmon and Steelhead Trout Restoration Account	0	0	0	0.0
Central Valley Project Improvement Subaccount	53	53	0	0.0
Harbor and Watercraft Revolving Fund	5	5	0	0.0
Upper Newport Bay Ecological Reserve Maintenance and Preservation Fund	(200)	(200)	0	0.0
Marine Life and Marine Reserve Management Account	0	0	0	0.0
Federal Trust Fund	50,209	62,059	11,850	23.6
Reimbursements	24,416	28,535	4,119	16.9
Coastal Watershed Salmon Habitat Subaccount	4,303	0	(4,303)	-100.0
California Clean Water, Clean Air, Safe Neighborhood Parks and Coastal Protection Fund	8,000	8,000	0	0.0
Water Security, Clean Drinking Water, Coastal and Beach Protection Fund of	0	2,030	2,030	0.0

2002				
Total	$271,273	$275,780	$4,507	1.7

Issues

The Department proposes a General Fund reduction of $11.6 million, which consists of the following items:

- A total reduction of 50 positions and $4.5 million ($1.64 million in 2002-03, and $2.9 million in 2003-04) for enforcement. As part of the first extraordinary session, the Senate approved the department's proposal to reduce funding for vacant enforcement positions in the current fiscal-year ($1.64 million), however the Senate submitted a letter to the journal stating intent to maintain the positions through the fiscal-year. The issues and concerns surrounding enforcement have been a priority for the Subcommittee over the past 3 years.

  Fish and Game Wardens perform numerous functions for the department, including the protection of California's public trust resources. Enforcement at the department has been historically been understaffed and underfunded. The Legislature approved $31.6 million and 200 positions in the 2000-01 Budget Act to address chronic underfunding of enforcement, monitoring, environmental review, maintenance, and administration at the department. Eliminating these positions would hinder any progress made by Department to increase enforcement activities, and would undermine the Legislature's intent to increase funding for enforcement.

- $1.9 million reduction for Wildlife Area and Ecological Reserve Operations.
- $1.6 million reduction to eliminate/reduce funding for fish hatcheries.
- $1.2 million to eliminate funding for the Urban Fishing Program.
- $900,000 (thousand) to eliminate funding for the North Coast Watershed Assessment program.

3640 Wildlife Conservation Board

The Wildlife Conservation Board (WCB), established within the Department of Fish and Game (DFG), administers a capital outlay program for wildlife conservation and related public access. The board acquires property to protect and preserve wildlife and provides fishing, hunting, and recreational access facilities. The board is composed of the directors from the Department of Fish and Game, the Department of Finance, and the Chairman of the Fish and Game Commission. In addition, three members of the Senate and three members of the Assembly serve in an advisory capacity to the board.

The budget proposes total expenditures of $417.7 million ($22.1 million, General Fund), a decrease of $274.3 million (85.4 percent) from the current-year budget. The decrease in spending is primarily associated with the capital outlay program. The board proposes a reduction of $276.8 million in capital outlay expenditures, and a reduction of bond funds from Proposition 40 ($283 million), and Proposition 12 ($153.8 million).

Fund Source (dollars in thousands)	2002-03	2003-04	Change Dollars	Change Percent
State Operations & Local Assistance				
General Fund	$319	$321	$2	0.6
Safe Neighborhood Parks, Clean Air, Clean Water, and Coastal Protection Bond Fund	$388	$0	(388)	-100.0
Environmental License Plate Fund	$254	$215		0.0
Habitat Conservation Fund	$274	$381	107	39.1
Wildlife Restoration Fund	$826	$882	56	6.8
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Fund	420	421	1	0.2
Water Security, Clean Drinking Water, Coastal and Beach Protection Fund of 2002	858	3,664	2,806	327.0
Reimbursements	0	0	0	0.0
Subtotal	$3,339	$5,884	2,545	76.2
Capital Outlay				
General Fund	$21,301	$21,736	435	2.0
Safe Neighborhood Parks, Clean Air, Clean Water, and Coastal Protection Bond Fund	$153,822	$0	(153,822)	-100.0
Habitat Conservation Fund	35,804	20,620	(15,184)	-42.4
Less Funding provided by General Fund	(21,301)	(21,736)	(435)	0.0
Inland Wetlands Conservation Fund	350	1,750	1,400	400.0
Natural Resources Infrastructure Fund	0	0	0	0.0
Wildlife Restoration Fund	500	500	0	0.0
Harbors and Watercraft Revolving Fund	0	0	0	0.0
Reimbursements	12,953	4,000	(8,953)	-69.1
River Protection Subaccount	5,762	0	(5,762)	-100.0
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Fund	299,500	16,500	(283,000)	-94.5
Water Security, Clean Drinking Water, Coastal and Beach Protection Fund of 2002	180,000	363,500	183,500	101.9
Oak Woodlands Conservation Fund	0	5,000	5,000	0.0
Subtotal	$688,691	$411,870	(276,821)	-40.2
Total	$692,030	$417,754	($274,276)	-39.6

Highlights

The board proposes the following items:

- $32.5 million from Proposition 50 for the Colorado River acquisition, protection, and restoration program.
- $24 million from Proposition 40 for Rangeland, Grazing Land & Grassland Protection, and Oak Woodlands protection program.
- $3.7 million and 9 positions to administer Proposition 50 bond funds.

3760 State Coastal Conservancy

The conservancy is authorized to acquire land, undertake projects, and award grants for the purposes of (1) preserving agricultural land and significant coastal resources, (2) consolidating subdivided land, (3) restoring wetlands, marshes, and other natural resources, (4) developing a system of public accessways, and (5) improving coastal urban land uses. The conservancy's jurisdiction covers the entire coastal zone including San Francisco Bay and the Suisun Marsh. The conservancy governing board consists of the Chairperson of the Coastal Commission, the Secretary for Resources, the Director of Finance, and four public members. The conservancy office is located in Oakland.

The budget proposes total expenditures of $78.3 million ($0, General Fund), a decrease of $337.9 million (81.2 percent) from the current-year budget. The decrease in spending in primarily associated with the Capital Outlay program, and a reduction of bond funds from Proposition 12 ($157.6 million) and from Proposition 40 ($174.4 million).

Fund Source (dollars in thousands)	2002-03	2003-04	Change Dollars	Change Percent
State Operations and Local Assistance				
General Fund	$1,250	$0	($1,250)	-100.0
Safe Neighborhood Parks, Clean Water, Clean Air, and Coastal Protection Bond Fund	1,572	1,291	(281)	-17.9
State Coastal Conservancy Fund	4,068	4,209	141	3.5
Federal Trust Funds	116	117	1	0.9
Reimbursements	111	111	0	0.0
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Fund	740	742	2	0.3
Water Security, Clean Drinking Water, Coastal and Beach Protection Fund of 2002	0	550	550	0.0
Subtotal	7,857	7,020	(837)	-10.7
Capital Outlay				
General Fund	764	0	(764)	-100.0
Safe Neighborhood Parks, Clean Water, Clean Air, and Coastal Protection Bond Fund	157,642	0	(157,642)	-100.0
Public Resources Account, Cigarette and Tobacco Products Surtax	0	0	0	0.0
Habitat Conservation Fund	7,689	4,000	(3,689)	-48.0
San Francisco Bay Conservancy Program Account	0	0		
California Beach and Coastal Enhancement Account	609	0		
State Coastal Conservancy Fund	3,712	0	(3,712)	-100.0
Coastal Access Account	1,046	0		
Fish and Wildlife Habitat Enhancement Fund	801	0		
California Wildlife, Coastal and Park, Land Conservation Fund of 1988	2,627	0	(2,627)	-100.0
Federal Trust Funds	3,537	2,000	(1,537)	-43.5
Renewable Resources Investment Fund	0	0	0	0.0
Reimbursements	11,783	1,800	(9,983)	-84.7
River Protection Subaccount	11,795	0	(11,795)	-100.0
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Fund	206,400	32,000		
Water Security, Clean Drinking Water, Coastal and Beach Protection Fund of 2002	0	31,500		
Subtotal	408,405	71,300	(337,105)	-82.5

Total	$416,262	$78,320	($337,942)	-81.2

Highlights

The SCC proposes the following items:

- $550,000 (thousand) and 6 positions to administer Proposition 50 bond funds.
- $22 million from Proposition 40 for various acquisition and restoration programs.
- $6 million from Proposition 40 for the San Francisco Bay Conservancy Program.
- $4 million from Proposition 40 for coastal watershed protection.

3790 Department of Parks and Recreation

The Department of Parks and Recreation (DPR) acquires, develops, preserves, interprets, and manages the natural, cultural, and recreational resources in the state park system and in the State Vehicular Recreation Area and Trail System (SVRATS). In addition, the department administers state and federal grants to cities, counties, and special districts that help provide parks and open-space areas throughout the state. The state park system consists of 273 units, 31 of which are administered by local and regional park agencies. The system contains approximately 1.4 million acres of land, with 285 miles of coastline and 822 miles of lake, reservoir, and river frontage.

The budget proposes total expenditures of $912.0 million, ($97.9 million, General Fund), a decrease of $91.7 million (9.1 percent) from the current-year budget.

Fund Source (dollars in thousands)	2002-03	2003-04	Change Dollars	Change Percent
State Operations:				
General Fund	$128,758	$89,915	($38,843)	-30.2
Safe Neighborhood Parks, Clean Water, Clean Air & Coastal Protection Bond Fd	22,780	23,516	(10,822)	-47.5
California Environmental License Plate Fd	115	124	12,173	10585.2
Public Resources Account, Cigarette & Tobacco Products Surtax Fund	13,311	11,747	265,247	1992.7
Habitat Conservation Fund	61	0	(61)	-100.0
Off-Highway Vehicle Trust Fund	26,637	28,373	(26,637)	-100.0
Natural Resources Infrastructure Fund	0	0	7,956	0.0
State Parks and Recreation Fund	76,975	96,747	(76,975)	-100.0
Winter Recreation Fund	287	289	2,313	805.9
Harbors and Watercraft Revolving Fund	638	663	16,362	2564.6
State Parks System Deferred Maintenance Account	0	0	0	0.0
Recreational Trails Fund	25	0	(25)	-100.0
Federal Trust Fund	2,948	2,938	1,052	35.7
Reimbursements	11,958	11,958	8,042	67.3
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Fund	15,066	12,288		0.0
Total, State Operations	$299,559	$278,558	($21,001)	-7.0
Local Assistance::				
General Fund	$3,090	$7,956	$4,866	157.5
Safe Neighborhood Parks, Clean Water, Clean Air & Coastal Protection Bond Fd	299,315	0	(299,315)	-100.0
Habitat Conservation Fund	2,055	2,600	545	26.5
Off-Highway Vehicle Trust Fund	27,894	17,000	(10,894)	-39.1
Natural Resources Infrastructure Fund	0	0	0	0.0
California Wildlife, Coastal and Park Land Conservation Fund of 1988	8	0	(8)	-100.0
Recreational Trails Fund	9,807	4,000	(5,807)	-59.2
Federal Trust Fund	26,529	20,000	(6,529)	-24.6
Reimbursements	0	0	0	0.0
River Protection Subaccount	1,500	0	(1,500)	-100.0
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Fund	333,930	581,883	247,953	74.3
Total, Local Assistance	$704,128	$633,439	($70,689)	-10.0

Total	$1,003,687	$911,997	($91,690)	-9.1

3860 Department of Water Resources

The Department of Water Resources (DWR) is responsible for developing and managing California's water through the implementation of the State Water Resources Development System, including the State Water Project. The Department also maintains the public safety and prevents damage through flood control operations, supervision of dams, and safe drinking water projects.

The budget proposes total expenditures of $6.1 billion ($39 million, General Fund), an increase of $324.5 million (5.7 percent) from the current-year budget. The increase in spending is attributable to the allocation of Proposition 50 bond funds to the department ($300.1 million).

Fund Source			Change	
(dollars in thousands)	2002-03	2003-04	Dollars	Percent
General Fund	$68,435	$38,994	($29,441)	-43.0
Colorado River Management Account	18,000	39,000	21,000	116.7
California Environmental License Plate Fd	378	218	(160)	-42.3
Environmental Water Fund	6,683	0	(6,683)	-100.0
Central Valley Project Improvement Subaccount	1,568	1,568	0	0.0
Delta Levee Rehabilitation Subaccount	1,780	694	(1,086)	-61.0
Feasibility Projects Subaccount	1,445	1,446	1	0.1
Water Conservation and Groundwater Recharge Subaccount	123	123	0	0.0
Energy Resources Programs Account	1,739	1,657	(82)	-4.7
Water Project Funds	249,554	240,167	(9,387)	-3.8
Loan Repayments	(1,530)	(1,530)	0	0.0
Local Projects Subaccount	3,524	99	(3,425)	-97.2
Sacramento Valley Water Management and Habitat Protection Subaccount	16,569	2,624	(13,945)	-84.2
California Safe Drinking Water Fund	4,785	4,785	0	0.0
1984 State Clean Water Bond Fund	570	570	0	0.0
Loan Repayments	-325	(325)	0	0.0
1986 Water Conservation and Water Quality Bond Fund	5,064	5,064	0	0.0
Loan Repayments	-2,158	(2,158)	0	0.0
1988 Water Conservation Fund	9,017	9,017	0	0.0
Federal Trust Fund	60,211	11,223	(48,988)	-81.4
Bosco-Keene Renewable Resources Investment Fund	797	652	(145)	-18.2
Reimbursements	59,692	21,389	(38,303)	-64.2
Department of Water Resources Electric Power Fund	4,968,644	5,311,825	343,181	6.9
Flood Protection Corridor Subaccount	27,432	8,257	(19,175)	-69.9
Urban Stream Restoration Subaccount	10,172	674	(9,498)	-93.4
Yuba Feather Flood Protection Subaccount	5,456	3,957	(1,499)	-27.5
River Protection Subaccount	163	163	0	0.0

Water Conservation Account	51,675	30,425	(21,250)	-41.1
Conjunctive Use Subaccount	80,460	1,260	(79,200)	-98.4
Bay Delta Multipurpose Water Management Subaccount	29,574	23,722	(5,852)	-19.8
Interim Water Supply and Water Quality Infrastructure and Management Subaccount	9,050	422	(8,628)	-95.3
Water Security, Clean Drinking Water, Coastal and Beach Protection Act of 2002	43,000	300,104	257,104	597.9
Total	$5,731,547	$6,056,086	$324,539	5.7

3870 CALFED Bay-Delta Authority

The California Bay-Delta Authority, established by legislation enacted in 2002, provides a permanent governance structure for the collaborative state-federal effort that began in 1994. The Authority is composed of representatives from six state agencies and six federal agencies, five public members from the Program's five regions, two at-large public members, a representative from the Bay-Delta Public Advisory Committee, and four ex officio members, namely the chairs and vice-chairs of the Senate and Assembly water committees.

Prior to creation of the Authority, the Program functioned as a consortium of state and federal agencies, each operating under its independent statutory authority to implement various elements of the Bay-Delta Plan, set forth in the CALFED Bay-Delta program Record of Decision signed in August 2000. Under the Authority, the agencies have a more formalized role in advancing the goals of the Program. The Authority was established by enactment of Senate Bill 1653 (Costa) of 2002. The legislation calls for the Authority to sunset on January 1, 2006, unless federal legislation has been enacted authorizing the participation of appropriate federal agencies in the Authority.

The budget proposes $216.4 million ($12.6 million, General Fund) in total expenditures. Overall, the budget proposes $582.1 million in total funding for the CALFED Bay-Delta program.

Fund Source			Change	
(dollars in thousands)	2002-03	2003-04	Dollars	Percent
General Fund	$0	$12,590	$12,590	0.0
Bay-Delta Ecosystem Restoration Account	$5,074	48,531	43,457	856.5
Federal Trust Fund	0	29,352	29,352	0.0
Reimbursements	0	16,495	16,495	0.0
Water Security, Clean Drinking Water, Coastal and Beach Protection Fund	0	109,426	109,426	0.0
Total	$5,074	$216,394	$211,320	4164.8

ENVIRONMENTAL PROTECTION

OVERVIEW

The California Environmental Protection Agency (CalEPA) oversees and coordinates the environmental regulatory activities of the following boards, departments, and offices:

- Air Resources Board (ARB)
- Integrated Waste Management Board (IWMB)
- Department of Pesticide Regulation (DPR)
- State Water Resources Control Board (SWRCB)
- Department of Toxic Substances Control (DTSC)
- Office of Environmental Health Hazard Assessment (OEHHA)

A total of $1.21 billion ($86.1 million General Fund) is proposed for the agency's programs. This represents a decrease in overall funding of $267.8 million (22 percent) over the last two years.

Significant reductions to General Fund support for Cal EPA have occurred over the last two years. Special Fund support has slowly increased with the various departments looking user fees and polluter fees for alternative revenue sources. However, special fund support has not been able to stem the significant decrease in General Fund funding to Cal EPA programs.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$158,105	$86,142	-$71,963	-45.5
Special Funds	654,171	685,552	31,381	4.8
Selected Bond Funds	576,987	271,871	-305,116	-52.9
Federal Funds	167,086	167,116	30	0.0
Total	$1,556,349	$1,210,681	-$345,668	-22.2

While the state protects the environment through the work of the above departments, the Office of the Secretary for Environmental Protection received minimal reductions which appear reasonable. This office will not be discussed, however significant reductions or fiscal issues were proposed to the budgets of the ARB, IWMB, DPR, SWRCB, DTSC, and OEHHA that warrant discussion.

3900 Air Resources Board

The Air Resource Board is responsible for protecting air quality in California. Specifically, the board monitors ambient air quality standards, administers air pollution studies, evaluates regulations adopted by the United States Environmental Protection Agency, and administers programs to maintain California's air quality standards.

The budget proposes total expenditures of $152.6 million ($10.4 million General Fund), an increase of $2.2 million (1.4 percent) from the current-year budget. Despite the increase, General Fund support for the Air Resources Board has dropped dramatically with support shifted to the Air Pollution Control Fund (see ***Highlights*** section below).

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$23,887	$10,416	-$13,471	-56.4
Motor Vehicle Account	62,335	63,498	1,163	1.9
Air Pollution Control Fund	11,529	28,110	16,581	143.8
Other Funds	11,613	11,672	59	0.5
Federal Trust Fund	10,810	11,017	207	1.9
Reimbursements	5,261	4,886	-375	-7.1
Selected Bond Funds	25,000	23,000	-2,000	-8.0
Total	$150,435	$152,599	$2,164	1.4

Highlights

Stationary Source Fees. The budget proposes to increase Stationary Source Fees by shifting $10 million of General Fund support for the program to the Air Pollution Control Account. As part of the polluter pays principle, the proposal seeks remove the cap of $3 million in total fees collected and expand the scope of those under the fee structure to include manufacturers of consumer products and architectural coatings. As a result of the proposed fee increase, the board's stationary source program will receive approximately 1/3 of its revenue from the regulated community.

The Legislature recently approved this fee increase through AB 10X (Oropeza) during the Mid-Year Budget Revision process. This allows sufficient time for the ARB to develop and implement a new fee structure in time for FY 2003-04. However at the time of printing, the Governor had yet to sign the bill. If the Governor fails to sign AB 10X, the Legislature should propose the fee increase in the budget year.

General Fund Reductions. The budget proposes a $2.1 million reduction and 17 positions for various stationary source programs including: source testing, enforcement, and compliance; air quality emissions inventory; community health; permit coordination and review; and engineering and quality management. The stationary source program already received reductions of $4.4 million from the previous year.

Mobile Source Greenhouse Gases. The budget proposes $100,000 from the Motor Vehicle Account to develop and adopt regulations to reduce mobile source greenhouse gases.

3910 Integrated Waste Management Board

The Integrated Waste Management Board's (IWMB) mission is to promote source reduction, recycling, composting, and environmentally safe transformation as alternatives to the disposal of solid waste at landfills. The board also protects the public health and safety through the regulation of existing and new solid wasteland disposal sites.

The budget proposes total expenditures of $115.5 million ($0 General Fund), a decrease of $11.8 million (9.2 percent) from the current-year budget.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$49	$0	-$49	-100.0
Integrated Waste Mgt. Account	42,452	43,995	1,543	3.6
CA Used Oil Recycling Fund	32,221	22,628	-9,593	-29.8
Recycling Market Development Revolving Loan Account	8,168	8,134	-34	-0.4
CA Tire Recycling Management Fund	30,969	31,489	520	1.7
Solid Waste Disposal Site Cleanup Fund	7,582	5,462	-2,120	-28.0
Other Funds & Reimbursements	5,689	3,658	-2,031	-35.7
Selected Bond Funds	151	152	1	0.7
Total	$127,281	$115,518	-$11,763	-9.2

Highlights

Special Fund Loans. The budget proposes a loan of $2 million and $15 million from Board's Integrated Waste Management Account and California Tire Recycling Management Fund respectively.

3930 Department of Pesticide Regulation

This Department of Pesticide Regulation (DPR) was created in 1991 as part of the California Environmental Protection Agency to protect the public health and the environment from unsafe exposures to pesticides. The department (1) evaluates the public health and environmental effects of pesticides; (2) regulates, monitors, and controls the use of pesticides in the state; (3) tests produce for pesticide residue levels; and (4) develops and promotes pest management practices that can reduce the problems associated with the use of pesticides. The department primarily is funded from taxes on the sale of pesticides in the state, various registration and licensing fees on persons who use or sell pesticides, and the General Fund. The department is located in Sacramento. The budget proposes total expenditures of $53.3 million ($100,000 General Fund), a decrease of $1.1 million (2.1 percent) from the current-year budget.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$12,795	$1	-$12,794	-100.0
Dept. of Pesticide Regulation Fund	$37,861	$49,794	-11,933	31.5
Other Funds	$914	$869	-45	-4.9
Federal Trust Fund	$2,383	$2,160	-223	-9.4
Reimbursements	$479	$479	0	0.0
Total	$54,432	$53,303	-$1,129	-2.1

Highlights

Mill Assessment Branch. The budget proposes to redirect many positions and resources from various programs in DPR to create a new Mill Assessment Branch which would be responsible for maximizing collection, reporting, monitoring and compliance of the mill assessment program. DPR estimates that greater efficiencies from the consolidation will allow $2 million in General Fund savings.

General Fund Reductions. The budget proposes to reduce $2.8 million and 3.8 positions from the department's baseline budget. The several pesticide monitoring and enforcement programs are effected by this proposal including Pest Management Alliance Grants, Air Program, Surface Water Program, Marketplace Surveillance Residue Program, and permitting and enforcement programs.

Issues

Mill Assessment Fees and Pesticide Licensing/Examination Fees. The Governor's budget proposes shifting $8.6 million from the General Fund to the Department of Pesticide Regulation Fund (DPRF) by increasing pesticide mill assessment fees and pesticide licensing and examination fees.

The mill assessment is currently set at a rate of 17.5 mills (one mill is equivalent to $0.001 for each dollar of pesticide sold in the state). Also, a smaller amount of funds are generated through fees on pesticide registration, licensing and examination of pesticide dealers. In the current year, the DPRF accounts for close to 70% of DPR's funding, with a majority of the remaining funding coming from the General Fund.

The Administration's proposal establishes a new cap of 27 mills (one mill is equivalent to $0.001 for each dollar of pesticide sold in the state) and allows the Director of DPR to adjust fee levels within that cap to fully fund the pesticide programs. Also, the Director would be given the authority to adjust licensing and examination fees to cover the costs of those programs. This increase will fully fund the pesticide program from the DBRF.

Two years ago, the Legislature sought a stable funding source for the program by establishing a committee of stakeholders, department officials, and legislative representatives to address the long term funding issues of the pesticide program. That report is expected to be released very soon.

DPR believes that increasing the mill assessment to fully fund the department is the long term funding solution for the program. DPR states the fee increase will have an insignificant impact upon agriculture industry while relieving the General Fund through the polluters pays principle. In light of the impending report and the condition of the General Fund, stable, non-General Fund revenues for this essential environmental health program is necessary to maintain funding levels for this important mandated activities. However, issues of the proper funding levels of the department, proper oversight of pesticide activities, and appropriate assessment levels will have to be addressed.

3940 State Water Resources Control Board

The State Water Resources Control Board (SWRCB) regulates water quality in the state and administers water rights. The board carries out its water quality control responsibilities by (1) establishing wastewater discharge policies; (2) implementing programs to ensure that the waters of the state are not contaminated by surface impoundments, underground tanks, or aboveground tanks, and (3) by administering state and federal loans and grants to local governments for the construction of wastewater treatment facilities. Nine regional water quality control boards establish water discharge requirements and carry out water pollution control programs in accordance with state board policies. The board's water rights responsibilities involve issuing and reviewing permits and licenses to applicants who wish to appropriate water from the state's streams, rivers, and lakes.

The budget proposes total expenditures of $739.4 million ($73.2 million General Fund), a decrease of $332.0 million (31 percent) from the current-year budget.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
State Operations				
General Fund	$73,212	$44,633	-$28,579	-39.0
Underground Storage Tank Cleanup Fund	250,467	242,038	-8,429	-3.4
Waste Discharge Permit Fund	32,174	45,905	13,731	42.7
Public Resources Account	2,125	2,120	-5	-0.2
Integrated Waste GMT Account	5,250	5,339	89	1.7
Federal Trust Fund	37,800	37,830	30	0.1
Reimbursements	9,933	9,933	0	0.0
Prop. 50 Bond Funds	125	2,342	2,217	1773.6
Other Bond Funds	4,537	5,799	1,262	27.8
Other Funds	32,774	25,206	-7,568	-23.1
Subtotal	448,397	421,145	-27,252	-6.1
			0	0.0
Local Assistance			0	0.0
General Fund	0	0	0	0.0
State Revolving Loan Subaccount	15,000	15,000	0	0.0
Small Communities Grant Subaccount	21,000	6,000	-15,000	-71.4
Water Recycling Subaccount	63,883	20,600	-43,283	-67.8
State Water Pollution Control Revolving Fund	96,000	96,000	0	0.0
Prop. 50 Bond Funds	30,375	112,488	82,113	270.3
Other Bond Funds	383,505	60,300	-323,205	-84.3
Loan Repayments/Less Funding from Various Accounts	(85,730)	(90,730)	(-5,000)	5.0
Other Funds	9,000	8,580	-420	-4.7
Federal Trust Fund	90,000	90,000	0	0.0
Subtotal	623,033	318,238	-304,795	-48.9
Total	$1,071,430	$739,383	-$332,047	-31.0

Highlights

Waste Discharge Permit Fees. The Governor's budget proposes to fund shift $13.6 million from the General Fund to the Waste Discharge Permit Fund by increasing waste discharge permit fees and stormwater discharge fees.

The Legislature recently approved this fee increase through AB 10X (Oropeza) during the Mid-Year Budget Revision process. This allows sufficient time for the SWRCB to develop and implement a new fee structure in time for FY 2003-04. However at the time of printing, the Governor had yet to sign AB 10X. If the Governor fails to sign the fee increase, the Legislature should consider proposing the fee increase in the budget year.

Underground Storage Tank Cleanup Fund. The budget proposes a loan of $3.2 million from the Underground Storage Talk Cleanup Fund to the General Fund. Also proposed is a increase of $15 million from the fund for reimbursements.

Proposition 50 Bond Funds. The budget proposes $507.0 million from Proposition 50 bond funds for various program areas including water quality protection and improvement, watershed planning and implementation, coastal water protection and restoration, groundwater protection, and interregional water management. Of the $507.0 million, $450 million is appropriated directly to programs in SWRCB by Proposition 50, and $57 million is the Water Board's request for unallocated funds in Proposition 50 for water recycling projects in the CALFED Bay-Delta Program.

Issues

General Fund Reductions to the Water Quality Program. The budget proposes substantial reductions to the water quality monitoring activities. Water monitoring activities (particularly for groundwater quality) is a basic function of the Water Board, and is essential to permitting and enforcing water quality standards. A total of $11.3 million in reductions to this program are as follows:

Reductions to the Water Quality Program (dollars in thousands)	2002-2003	2003-2004
Program Title		
Data Management	$0	$500
Salton Sea Restoration	350	350
Regional Wetlands Management Plan	15	15
Spills, Leaks, Investigations, and Cleanup	25	290
Chromium 6	0	462
Monitoring & Assessment Programs	831	6,802
Agricultural Waste Management	450	1,124
Water Quality Planning	0	570
Underground Storage Talks	0	682
Nonpoint Source	0	89
CALFED	365	365
Training	63	0
Equipment	67	0
Out-of-State Travel	11	24
Total	$2,177	$11,273

The $11.3 million in budget year reductions are proposed on top of the recently approved $2.2 million in current year reductions. The Water Board has indicated that such reductions will substantially curtail their current water quality monitoring efforts.

Without proper monitoring abilities, the Water Board's permitting, investigation, enforcement, and cleanup activities will be significantly affected. Alternative revenue sources to the General Fund, such as the waste discharge permit fees *(see **highlights** above)*, should be examined for long term funding stability for the Water Board's regulatory and monitoring activities.

General Fund Reductions to the Water Rights Program. The budget proposes substantial reductions to the water rights program. The Water Board's water rights program allows parties who wish to "appropriate" (*i.e.,* use for their own purposes) state waters to perfect their right to do so through board approval. These approvals are generally granted with conditions which protect the rights of other parties and the beneficial uses of water.

According to the Water Board, "Before the SWRCB can grant an appropriate water right permit, it must find that there exists in the source stream sufficient unappropriated water to support the possible project and it must assess the environmental impacts of the project. Funds are used to contract with private consultants to perform a water availability analysis that determines whether sufficient unappropriated water exists."

The budget proposes to reduce General Fund support of the Water Rights Program by $3.3 million. This does not include the reductions this Legislature approved for the current year of $610,000. These reductions combined represents a 34.8% reduction in water rights funding in activities such as processing of water rights applications, complaint investigations, adjudication, and enforcement. In FY 2000-01, the Legislative Analyst Office (LAO) identified significant backlogs in the review and issuances of water rights by the board. The Legislature over last few years has generally sought to improve the process for issuance of water rights.

The LAO also recommended to the Legislature funding to this program should be increased by instituting a "user pays" system whereby parties applying for water rights would pay a fee to cover the costs of the Water Board in evaluating and issuing a grant of water rights.

Currently, there is a nominal water rights application fee which does not cover the extensive costs of evaluating applications. Given the significant impacts on the environment, an increased fee structure, taking into consideration the significant differences between efforts necessary for evaluation of water rights applications, should be considered to preserve funding for this over-burdened program.

3960 Department of Toxic Substances Control

The Department of Toxic Substances Control's (DTSC) mission is to protect the public health and the environment from unsafe exposure to toxic substances. In so doing it (1) regulates hazardous waste management, (2) cleans up sites that have been contaminated by toxic substances, and (3) promotes methods to treat and safely dispose of hazardous wastes and reduce the amounts of hazardous wastes that are generated in the state. The department is primarily funded from fees and taxes assessed on persons that generate, store, treat, or dispose of hazardous wastes. The department is located in Sacramento.

The budget proposes total expenditures of $159.0 million ($20.1 million General Fund), a decrease of $4.53 million (2.8 percent) from the current-year budget.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	32,728	20,106	-$12,622	-38.6
Hazardous Waste Control Account	41,026	46,991	5,965	14.5
Site Remediation Account	8,664	7,850	-814	-9.4
Unified Program Account	955	981	26	2.7
California Used Oil Recycling Fund	339	337	-2	-0.6
Hazardous Substance Accounts	6,873	5,539	-1,334	-19.4
Expedited Site Remediation Trust Fund	0	2,441	2,441	0.0
Toxic Substances Control Account	36,422	36,258	-164	-0.5
Federal Trust Fund	26,727	26,053	-674	-2.5
Other Funds	2,913	3,564	651	22.3
Reimbursements	6,925	8,921	1,996	28.8
Total	$163,572	$159,041	-$4,531	-2.8

3980 Office of Environmental Health Hazard Assessment

This Office of Environmental Health Hazard Assessment (OEHHA) was created in 1991 as part of the California Environmental Protection Agency to evaluate the health risks of chemicals in the environment. OEHHA currently (1) develops and recommends health-based standards for chemicals in the environment, (2) develops policies and guidelines for conducting risk assessments, and (3) provides technical support for environmental regulatory agencies.

The budget proposes total expenditures of $10.8 million ($8.7 million General Fund), a decrease of $4.2 million (28.1 percent) from the current-year budget.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$12,004	$8,707	-$3,297	-27.5
Environmental Lic Plate Fund	775	800	25	3.2
Federal Trust Fund	20	0	-20	-100.0
Reimbursements	2,277	1,339	-938	-41.2
Total	$15,076	$10,846	-$4,230	-28.1

Issues

General Fund Reductions. The Governor's budget proposes to reduce OEHHA's total budget by approximately 30%. This reductions will cause OEHHA to lay off 23 positions (25% of its workforce) of highly skilled individuals.

The department has stated, "With a significantly reduced workforce, OEHHA will not be able to meet its statutory mandates and deadlines in Proposition 65, fuels, indoor air, and SB 950, the Birth Defect Prevention Act programs." OEHHA will have to eliminate many activities like pesticide worker health and safety assessment, development of environmental indicators for Cal EPA, and the identification of future environmental problems and solutions. The Children's Health Program and the Worker Health Safety Program will not be eliminated, though progress will be slowed.

OEHHA plays a vital role of environmental protection by being the risk assessment arm of Cal EPA. Its work is integral to other boards, commissions, and departments within Cal EPA in providing the scientific expertise to identify environmental risks and solutions. Given the connection to several other Cal EPA programs, the Legislature should examine possible long term funding solutions by identifying the nexus between OEHHA's risk assessment efforts and those boards, departments, and commissions that benefit.

PUBLIC SAFETY AND CRIMINAL JUSTICE

0820 Department of Justice

It is the responsibility of the Attorney General to uniformly and adequately enforce the laws of the State of California. Under the direction of the Attorney General, the Department of Justice (DOJ) enforces state laws, provides legal services to state and local agencies, and provides support services to local law enforcement agencies. There are five primary divisions within the department, including (1) Civil Law, (2) Criminal Law, (3) Public Rights, (4) Law Enforcement, and (5) Criminal Justice Information Services. In addition, DOJ's programs include the Division of Gambling Control, the Firearms Division, Executive Programs, and the Directorate and Administration Divisions.

The budget proposes $606.7 million for the Department of Justice. Of these funds, $152 million is for the Division of Law Enforcement, $255.6 million supports the Civil Law, Criminal Law, and Public Rights Programs, and $152.5 million is for the Criminal Justice Information Services Program, which includes the Hawkins Data Center and other information technology functions of the department. Overall spending would decrease by $31.1 million, or 4.9 percent, from the revised current-year budget. General Fund support would decrease by $14.4 million, or 4.5 percent from the revised current-year budget to $302 million.

Highlights

Executive and Directorate Programs. The Directorate Program consists of the Attorney General's Executive Office, Equal Opportunity Employment Office, and Opinion Unit. The Division of Executive Programs maintains internal and external department communications. It consists of the Office of Legislative Affairs, Crime Violence Prevention Center, special programs, and various communication offices. Budget adjustments include:

- A reduction of $600,000 for various operating and equipment expenses.
- A reduction of $1.5 million related to elimination of the Cal-Gang grant program.

Civil Law, Criminal Law, and Public Rights Divisions. The Civil Law Division provides legal services to state agencies and constitutional officers in the areas of licensing, government law, health, education, welfare, regulation, and taxation. The Criminal Law Division represents the state in all criminal matters before the appellate and supreme courts and defends the state in actions filed by state inmates under the Federal Civil Rights Act. The Public Rights Division provides legal services to state agencies and Constitutional Officers in the areas of civil rights, natural resources, land law, consumer law, and child support enforcement. Major budget adjustments include:

- A reduction of 5 positions and $1.8 million in the Civil Law Division.
- A reduction of $1.6 million in the Criminal Law Division for the *Plata v. Davis* lawsuit related to inmate medical care at the Department of Corrections The budget continues funding $4.2 million for this case, primarily for compliance monitoring.
- An increase of $1.3 million for legal expenses to continue the state's defense in *Williams v. State of California*, a constitutional challenge to the state's kindergarten-through high school education system.
- A reduction of $3.2 million related to the elimination of the Spousal Abusers' Prosecution Program.
- An augmentation of $5.7 million to fund specialist counsel for the continuing Lloyd's of London litigation.
- An augmentation of $2.5 million to continue the defense of the *Hyatt v. Franchise Tax Board* case.

Divisions of Law Enforcement, Gambling Control, and Firearms. The Division of Law Enforcement is organized into five bureaus, including Investigation, Narcotic Enforcement, Forensic Services, Western States

Information Network, and Criminal Intelligence. The Division of Gambling Control investigates qualifications of individuals that apply for gambling licenses and monitors the conduct of licensees. The Firearms Division processes licenses/permits to possess, manufacture or sell dangerous weapons; administers the gun show producer and assault weapon registration programs; conducts firearms dealer and manufacturer inspections; and conducts the safe handgun and firearms safety device certification programs. Major adjustments include:

- A reduction of 13 positions and $8.7 million from the General Fund in the Division of Law Enforcement. Of this amount, $3.5 million is related to a proposal to charge local agencies for forensic analysis services.
- An augmentation of $1.5 million and 13 positions to begin eliminating the current backlog of cases awaiting forensic analysis.

Criminal Justice Information Services Division. The Criminal Information Services Division was created in 1998-99 to include three former Division of Law Enforcement bureaus (Bureau of Criminal Information and Analysis, Bureau of Information and Identification, and the Western States Information Network) with the Hawkins Data Center and establishing the Criminal Justice Information Services Division. The budget for the division is proposed to decrease by $4.5 million, or 2.9 percent, below current-year expenditures. Major adjustments include:

- A reduction of $2 million from the General Fund and 14 positions related to the reduction or elimination of various programs.
- A reduction of $1.3 million General Fund and $2.2 million in reimbursements to reflect the transfer if the Child Support Program to the Department of Child Support Services.

Selected Issue

Forensic Services Fees. As noted above, the budget proposes a reduction of General Fund support for the Bureau of Forensic Services by $3.5 million ($7.1 million for full year) and an increase in reimbursement funding by an equal amount. These reimbursements would be funded by fees for forensic analysis charged to local agencies. The DOJ has 11 forensic labs around the state which provide services for counties that do not have their own facilities. Since 1972, the state has provided forensic analysis services at no charge for law enforcement agencies in 46 counties. These services include crime scene investigations, casework analysis, ballistics analysis, and DNA analysis and profiling.

In previous years, the LAO has noted that one option for savings would be to transfer costs of the regional forensic labs to the local law enforcement agencies that use the services. Last year, the LAO estimated that the savings generated by shifting 100 percent of costs for forensic services would be approximately $16 million. The Legislature may wish to obtain additional information regarding the proposal to ensure that it makes sense from a policy perspective, does not lead to inequitable administration of justice, and is not overly burdensome to administer.

5240 Department of Corrections

The Department of Corrections (CDC) is responsible for the control, care, and treatment of men and women who have been convicted of serious crimes and entrusted to the department's Institution and Community Correctional programs. In addition, the CDC maintains a Health Care Services Program to address inmate health care needs and a civil narcotics treatment program for offenders with narcotic addictions.

The budget proposes $5.3 billion for the CDC, which is an increase of $40.2 million, or 0.8 percent, above the current-year budget. General Fund expenditures are proposed to increase by $53.1 million, or l percent above current-year expenditures. The increase is due primarily to cost factors related to the projected increase in the inmate populations, and increased workers' compensation costs.

Authorized positions for the department are proposed to increase by a net 816 positions for a total of 46,174 positions. This increase is due primarily to increased population projections and related programmatic changes.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$5,096,077	$5,149,208	$53,131	1.0%
Federal Trust Fund	2,350	2,386	36	1.5%
Inmate Welfare Fund	47,366	50,009	2,643	5.6%
Special Deposit Fund	155	1,010	855	551.6%
Reimbursements	90,559	74,045	-16,514	-18.2%
Total	$5,236,507	$5,276,658	$40,151	0.8%

Highlights

Institution Program. The California Department of Corrections is required by statute to accept convicted felons and civilly committed nonfelon narcotic addicts from California courts when their sentence is imprisonment in a state correctional facility. It is the department's responsibility to provide safe and secure detention facilities to protect society from further criminal activities and to provide necessary services such as food, clothing, medical care, psychiatric and counseling services and training, including academic and vocational education.

The department estimates the inmate population to increase from 160,661 on June 30, 2003 to 161,039 by June 30, 2004, an increase of 378 inmates, or 0.2 percent. The population projections estimate that the population will remain relatively flat through 2008, with an estimated inmate population of 161,199 by June 30, 2008. The actual population on June 30, 2002 was 157,979, a decrease of 3,518 from the previous year.

Major budget adjustments for the Institutions Program include:

- An increase of $5.5 million and 75 positions to implement a standardized Administrative Segregation housing staffing pattern for all institutions, provide resources for a consultant to address standardized staffing for various missions, housing type, and physical plant, and to provide funding for three gang debriefing teams.
- An increase of $21.1 million and 114 positions in the current year and $14.7 million and 327 positions in the budget year to address the impact of sick leave usage for posted positions in Bargaining Unit 6.
- A reduction of $2.6 million in the current year due to the proposed elimination of the Arts in Corrections Program. This proposal would make the Handicraft program, a leisure time activity, available statewide.
- A reduction of $10.2 million in the budget year related to the closure of Northern California Women's Facility and conversion of the facility to a male reception center. The proposal identifies $11 million in capital outlay costs in the budget year for upgrades to the facility, and notes that there will be substantial start up costs for reactivating the facility.
- $220 million in lease revenue bonds for the study, preliminary plans, working drawings, and construction of a new condemned inmate complex at San Quentin prison.
- An assumption that California will receive $154.5 million in federal funds to offset the incarceration of undocumented persons.

Health Care Services Program. The California Department of Corrections is mandated to provide health care to the inmate population. The mission of the Health Care Services program is to manage and deliver health care to the inmate population statewide consistent with adopted standards for quality and scope of services within a custodial environment. The program strives to achieve this mission by providing cost-effective, timely, and competent care. Additionally, the program promotes inmate responsibility for their health.

The Health Care Services program is in the process of implementing a multidisciplinary, multiple service statewide health care delivery system. The delivery system seeks to provide inmates with timely access to staff, facilities, equipment, and procedures to diagnose and treat medical, dental, and mental health problems. Standardized screening and comprehensive mental health evaluations, licensed 24-hour medical care, adequate and timely mental health crisis care, and ongoing medical, dental, and mental health outpatient treatment are the basic components of the Health Care Services program. The program currently operates four licensed hospitals and a skilled nursing facility for female inmates. In addition, the department operates a hospice care wing at the California Medical Facility and an HIV unit at the California Institution for Men.

The proposed budget for the Health Care Services program is $939.2 million, an increase of $52.3 million, or 5.9 percent, above current-year expenditures. In recent years, the budget for the Healthcare Services Division has increased greatly due in large part to increases for contract medical costs, and the rise in costs for medical and psychiatric supplies. The 2003-04 budget proposes no increases for medical and psychiatric supplies or contract medical costs.

Major budget adjustments for the Health Care Services program include:

- An increase of $4.2 million and 37.8 positions related to Coleman court order mandates for the Mental Health Services Delivery System. The proposal seeks positions and recruitment and retention funding to increase the number of acute psychiatric beds at Corcoran Hospital and the Skilled Nursing Facility at Central California Women's Facility.
- An increase of $1.5 million and 21 positions to establish a Correctional Treatment Center (CTC) at the California Institute for Women and to maintain compliance with requirements for CTC licensure at Central California Women's Facility.
- Reappropriation of $4 million General Fund for the Madrid Patient Information System. The Budget Act of 2001 appropriated $7.9 million. CDC indicates that it is in the process of procuring the new system.

Community Correctional Program. The primary objective of this program is to increase the rate and degree of successful reintegration and release to society of adult offenders released from state prison to the jurisdiction of the Parole and Community Services Division. This objective is attained by providing support services, community program referral, control of behavior, and by increasing community awareness and understanding.

The department estimates that the parole population will be 117,233 by June 30, 2003. For 2003-04, the CDC projects population to decrease by 1,846, or 1.6 percent, for a total of 115,387 by June 30, 2004. This projection accounts for recent population trends and the estimated impact of Proposition 36 on the parole population.

Central Administration. The objective of the Central Administration program is to provide executive and administrative services to assure the overall success of the department's Institutions, Health Care Services, and Community Correctional programs. This program consists of the Executive Division, Support Services, and Field Operations. Major budget adjustments include:

- A one-time increase of $32.8 million in the current year and a base budget increase of $115.8 million in 2003-04 to address a budget shortfall for workers' compensation. Expenditures for workers' compensation have increased from $68.9 million in 1995-96 to an estimated $185.6 million in the budget year.
- An increase of $2.4 million in the current year and $6.7 million in the budget year for the increased operational costs associated with the new bargaining unit 6 contract. This proposal also requests $12 million for 2004-05 and $15.7 million for 2005-06. These amounts would provide funding for estimated increased costs related to legal representation, sick leave for permanent intermittent employees, survivor benefits, reductions to the institution vacancy plan, and parole agent workload.

- An increase of $12.9 million in the current year and $9.7 million in the budget year for increased costs of electricity and natural gas.

Selected Issues

Prison Reform Alternatives.

Over the last twenty years, the institution population at the California Department of Corrections (CDC) has increased significantly. The inmate population has grown from 23,500 in 1980 to 157,979 in 2002. Much of this increase has been driven by state sentencing changes. The inmate population growth was accommodated by building 21 new prisons and by adding beds to some of the 12 previously existing prisons. To address the demand for the housing of maximum security (level IV) inmates, in 1999 the Legislature authorized construction of the Delano II maximum security prison.

In stark contrast the rapid inmate population growth that CDC experienced in the 1980s and 1990s, CDC is now projecting virtually flat growth through 2008, and for the first time, experienced a decrease in population between 2001 and 2002. Proposition 36, which diverted nonviolent drug possession offenders into treatment, has played a role in stabilizing the inmate population.

Since 1980-81 the total budget for CDC has grown from $408.6 million to $5.1 billion in 2001-02. The proposed budget for the departments within the Youth and Adult Correctional Agency make up 9 percent of total General Fund expenditures. In light of this year's severe fiscal crisis, the Subcommittee may wish to consider policy changes that will prioritize the use of costly state prison resources. The Legislative Analyst and others have suggested a number of proposals in two broad categories:

Nonviolent offenders. According to the LAO's 2002-03 *Analysis*, 55 percent of the CDC's population are incarcerated for nonviolent offenses. These offenses include Petty Theft with a Prior, Drug Possession for Sale, Drug Possession, Grand Theft, DUI, Forgery/Fraud, Receiving Stolen Property, Other Property Offenses, and Vehicle Theft.

Parole Violators. CDC now supervises over 115,000 parolees. These parolees will be returned to custody for technical parole violations at a rate of 52% (not including parolees convicted of new crimes). California has the highest rate of parole violations in the nation. On average these "returned to custody" parole violators will spend an average of 4.5 months in prison for their violation. In a 1998 study, the National Council on Crime and Delinquency estimated that these parole violators occupy 21,155 prison beds -- about 13% of CDC's total capacity.

Potential prison reform alternatives for savings at the CDC include*:*

Intermediate Sanctions for Technical Parole Violators. California incarcerates more parole violators than the combined total of all other states in the country. In calendar year 2001, 74,280 parolees were returned to custody for parole violations, constituting approximately 17 percent of the total prison population. Approximately 53,860 of these parole violators were returned to prison for administrative or technical parole violations and minor criminality (such as petty theft and simple drug possession). According to the CDC the cost to incarcerate this parole violator population was $340 million. One alternative may be to implement graduated sanctions for non-serious, non-violent parolees. The CDC estimates that a program of providing intermediate sanctions for parole violators such as day reporting centers, electronic monitoring, home detention, and Community Correctional Reentry Centers, together with additional parole agents for pre-release planning and transition services would provide net savings of $77.2 million in the budget year, $99.7 million in 2004-05, and $189.3 million in 2005-06.

Direct Discharge from Prison. Last year the LAO raised the option of adopting Legislation to exempt certain non-violent, non-drug sale offenders from parole supervision. The CDC indicates that budget year savings would be $33.2 million as CDC implements the changes, with savings of approximately $113 million in 2004-05. The types of commitment offenses for individuals who would no longer be under parole supervision include: Petty Theft with a Prior, Receiving Stolen Property, Forgery/Fraud, Other Property Crimes, Possession of a Controlled Substance, Grand Theft, Vehicle Theft, Possession of a Weapon, Escape, Hashish Possession, Burglary (1st and 2nd), and Driving Under the Influence.

Early Discharge from Parole. Under this option, parolees with nonviolent offenses who have served a certain amount of "clean time" on parole would be eligible for early discharge from parole. Last year during the budget process, the LAO estimated that the amount of saving would depend upon the length of clean time prior to discharge, ranging from $50 million for six months to $23 million for 12 months.

Early Release from Prison. Under this option, inmates would be released to parole 1 to 12 months early. This option excludes lifers, strikers, sex registrants, and violent or serious offenders from early release. CDC estimates that the potential savings range from $10.1 million in 2003-04 and $20.1 million in 2004-05 for one month early release to $131.7 million in 2003-04 and $261 million in 2004-05 for 13 month early release.

Elderly Inmates – Release to Parole. This option provides that non-violent, non-serious offenders 60 or over would be released directly to parole. Last year during the budget process, the LAO estimated that first year savings from this option would total $3.4 million.

Removing State Prison as an Option for Certain Offenses. The CDC estimates budget year savings of $28.8 million (based on implementation in January 2004) could be achieved by removing state prison as an option for the following offenses: Petty Theft with a Prior, DUI, Other Property Offenses (Perjury, Bribery, etc.), Drug Possession, Hashish Offenses, Receiving Stolen Property, Drug Possession for Sale, Vehicle Theft, Grand Theft, Forgery/ Fraud.

Parole in Lieu of Prison for Inmates with Short Commitments. This option provides that certain non-violent, non-serious, non- sex registrant offenders with short commitments would go directly to parole rather than to prison. Savings under this option would vary depending upon how you define short commitments. CDC will provide estimates for inmates with commitments of 3, 6, 9, and 12 months. Assuming partial year implementation, the option would provide savings of $1 million for commitments of 3 months up to $24.8 million for commitments for up to 12 months in 2003-04 and $2.5 million for 3 months up to $132 million for 12 months in 2004-05.

Closure of NCWF. The budget proposes closure of the Northern California Women's Facility and conversion of the facility into a male reception center. The budget year savings are estimated at $10.2 million. Conversion of this facility into a male reception center will require at least $11 million in capital outlay expenditures, in addition to substantial costs for reactivation of the facility. The change to a male reception center would require legislation.

5430 Board of Corrections

The Board of Corrections (BOC) works in partnership with city and county officials to develop and maintain standards for the construction and operation of local jails and juvenile detention facilities and the employment and training of local corrections and probation personnel. The BOC also disburses training funds and administers the federal Violent Offender Incarceration/Truth-in-Sentencing (VOI/TIS) Grant, the Juvenile Hall/Camp Restoration program, the Repeat Offender Prevention Project, the Juvenile Crime Enforcement and Accountability Challenge Grant program, and the Mentally Ill Offender Crime Reduction Grant program. The BOC allocates these funds to public, private, or private/nonprofit participants in the local corrections community. The BOC is composed of 13 members—10 appointed by the Governor—confirmed by the Senate, and represents specific elements of local juvenile and adult criminal justice systems and the public. Statutory members are the Secretary of the Youth and Adult Correctional Agency, who serves as Chair, and the Directors of the Departments of Corrections and Youth Authority.

The budget for the BOC proposes $132.1 million, an increase of $2.8 million, or 2.1 percent above current-year expenditures. The General Fund portion of the budget reduces by $30.8 million to $44.8 million. This decrease is due primarily to the completion of General Fund grant programs from previous years. The Federal Funds are proposed to increase by $50.8 million to $84.3 million, primarily due to a new federal Violent Offender Incarceration/Truth-in-Sentencing grant.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$75,623	$44,813	-$30,810	-40.7%
Corrections Training Fund	19,623	2,401	-17,222	-87.8%
Federal Trust Fund	33,466	84,256	50,790	151.8%
Reimbursements	588	588	$0	0.0%
Total	$129,300	$132,058	$2,758	2.1%

Highlight

- The budget proposes a reduction of $16.2 million from the Corrections Training Fund associated with the partial reimbursement of tuition, travel, per diem, and staff replacement costs for training local correctional officers. The portion of local correctional officer training costs paid for by the state would become the responsibility of local correctional agencies. The budget proposes transfer of $10.1 million from the Correctional Training Fund to the General Fund.

5440 Board of Prison Terms

Chapter 1139, Statutes of 1976 (SB 42), established the Community Release Board in 1977. The Board was renamed the Board of Prison Terms (BPT) effective January 1, 1980 with the enactment of Chapter 255, Statutes of 1979 (SB 281). The BPT considers parole release and establishes the length and condition of parole for all persons sentenced to prison under the Indeterminate Sentence Law, persons sentenced to prison for a term of less than life under Penal Code section 1168 (b), and persons serving a sentence of life with possibility of parole. The BPT has nine commissioners appointed by the Governor and confirmed by the Senate. Each commissioner serves a four-year term. The Governor designates the chairperson of the BPT and deputy commissioners are employed by the BPT in civil service positions. Their duties include hearing and deciding cases.

The budget for the BPT proposes $30.6 million, a decrease of $1.7 million or 5.5 percent from anticipated current-year expenditures. The budget adjustments include a reduction of $1.2 million General Fund and 15 positions from state operations, and a further reduction of $443,000 and 3 positions to reflect a decrease in projected life prisoner and parole revocation hearing workloads.

Summary of Expenditures (dollars in thousands)	2001-2002	2002-2003	$ Change	% Change
General Fund	$30,958	$28,732	-$2,226	-7.2%
Reimbursements	81	81	0	0.0%
Total	$31,039	$28,813	-$2,226	-7.2%

5460 Department of the Youth Authority

The goals of the Youth Authority (YA) are to provide public safety through the operation of secure institutions, rehabilitate offenders, encourage restorative justice, transition offenders back to the community, and support local government and intervention programs. The budget proposes expenditures of $414 million for the YA, a decrease of $12.2 million, or 2.9 percent from anticipated current year expenditures. The primary reason for this reduction is the projected decrease in the YA's ward and parole populations. The ward population is projected to decrease by 105 wards from the amount projected in the 2001 Budget Act to 5,340 wards by June 30, 2003. The budget proposal projects the ward population to decrease by another 245 wards, or 4.6 percent resulting in a June 30 2004 population of 5,095. The parole population is projected to decrease by 210 cases to 3,830 by June 30, 2004.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$354,596	$336,757	-$17,839	-5.0%
1988 County Correctional Bond	58	0	-58	-100.0%
State Lottery Education Fund	526	528	2	0.4%
Federal Trust Fund	1,456	1,472	16	1.1%
Reimbursements	69,611	75,285	5,674	8.2%
Total	$426,247	$414,042	-$12,205	-2.9%

Highlights

Major Budget Adjustments

- An augmentation of $3.4 million to reimburse the Department of Mental Health to staff and equip a 20-bed Inpatient Mental Health Facility at the Southern Youth Correctional Reception Center and Clinic.
- An increase of $7.1 million in reimbursements from counties and a corresponding savings in General Fund to adjust for inflation the County Sliding Scale Fee assessed to counties for commitments to the Youth Authority.

Selected Issue

Closure Plan. The ward population at CYA has decreased significantly in recent years, from over 10,000 wards in 1996 to an estimated population of 5,095 at the end of the budget year. In the same period the budget for the CYA has only decreased from $429 million to $414 million. The average annual cost per ward is nearly $50,000. While the CYA has closed down some living units within its existing facilities, in order to achieve greater savings, the Legislature directed CYA to prepare a facility closure plan that would close at least three facilities by June 2007. In January, CYA submitted a plan to close two facilities and would convert one facility to an all female facility.

8100 Office of Criminal Justice Planning

The goal of the Office of Criminal Planning (OCJP) is to improve the criminal justice system by providing financial and technical assistance to local jurisdictions, state agencies, and the private sector, providing education and training for citizens, and providing technical support to the administration. The OCJP is organized into three programs: Administration, Criminal Justice Projects, and the California Anti-Terrorism Information Center. Funding for the Criminal Justice Projects Program is budgeted at $247.2 million, a decrease of $12.7 million, or 4.9 percent, from the current-year. The budget includes $6.7 million for the California Anti-Terrorism Information Center.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$70,459	$64,582	-$5,877	-8.3%
Prosecutors/Defenders Training Fund	859	864	5	0.6%
Peace Officers' Training Fund	0	0	0	n/a
Victim Witness Assist Fund	17,011	17,083	72	0.4%
High Tech Theft Apprehension Fund	14,285	14,285	0	0.0%
Less funding provided by General Fund	-14,031	-14,031	0	0.0%
Less funding provided by Fed Funds	-254	-254	0	0.0%
Federal Trust Fund	175,119	168,253	-6,866	-3.9%
Reimbursements	3,084	3,084	0	0.0%
Total	$266,532	$253,866	-$12,666	-4.8%

Highlights

- The budget assumes reductions of $3.6 million in the current year and the budget year from various local assistance grant programs.
- The budget transfers the Domestic Violence Shelter Program to the Department of Health Services.

Selected Issues

Domestic Violence Shelter Program. In October 2002, the Bureau of State Audits (BSA) released its report which reviewed the domestic violence programs administered by OCJP and the Department of Health Services (DHS). The report raised concerns regarding the administration of the programs by both OCJP and DHS. In addition, among its findings, the report indicates that many of OCJP's and DHS's activities for awarding grants and conducting oversight of shelter-based grant recipients overlap. To improve the efficiency of the state's domestic violence programs and reduce overlap of administrative functions, BSA recommends that the Legislature consider implementing four alternatives:

- Continue to coordinate the departments' activities on projects in which they both have interests in improving shelters, and work together to identify opportunities that might allow each department to focus on funding specific activities.
- Issue a joint application for both departments' shelter based programs but have each department continue its separate oversight.
- Combine the shelter-based activities at one department.
- Consolidate all domestic violence programs at one department.

As noted, the budget proposes to combine the shelter-based programs at DHS. The Legislature may wish to consider the options provided by BSA and other proposals to create a program structure for domestic violence shelters that provides appropriate guidelines, adequate technical assistance, and non-duplicative oversight.

Local Assistance Reductions. The budget proposes to continue reductions proposed in the current year for various local assistance grant programs. The table below highlights the proposed reductions.

2002- 2003 Budget Authority	Amount		
Program Name	Previous Grant	Reduction	Proposed Budget
Victims Legal Resource Center	86,000	-45,000	41,000
Family Violence Prevention	97,000	-47,000	50,000
Homeless Youth	441,000	-45,000	396,000
Youth Emergency Telephone	169,000	-42,000	127,000
Child Sexual Abuse & Exploitation	1,000	-1,000	0
Child Sexual Abuse Prevention & Training	336,000	-34,000	302,000
Community Crime Resistance	461,000	-230,000	231,000
Career Criminal Apprehension	1,154,000	-288,000	866,000
Career Criminal Prosecution	3,987,000	-350,000	3,637,000
Serious Habitual Offender	273,000	-136,000	137,000
Vertical Prosecution – Statutory Rape	8,361,000	-1,591,000	6,770,000
Evidentiary Medical Training	682,000	-34,000	648,000
Vertical Defense of Indigents	346,000	-174,000	172,000
Public Prosecutor/Defender Training	14,000	-6,000	8,000
Suppression of Drug Abuse in Schools	768,000	-78,000	690,000
Gang Violence Suppression	2,321,000	-236,000	2,085,000
Multi-Agency Gang Enforcement Consortium	124,000	-31,000	93,000
Rural Crime Prevention	3,541,000	-200,000	3,341,000
Total	**$23,162,000**	**-$3,568,000**	**$19,594,000**

The Legislature may wish to review other local assistance programs to determine if additional adjustments should be considered. For example, no reductions were proposed for OCJP's two largest grant programs, the War on Methamphetamine Program which provides $15 million to central valley and northern rural counties to target anti-methamphetamine efforts, and the High Technology Theft and Apprehension Program which provides $13.3 million from the General Fund to support regional High Technology Task Forces which target high technology crime.

8120 Commission on Peace Officer Training and Standards

The Commission on Peace Officer Training and Standards (POST) is responsible for raising the competence level of law enforcement officers in California by establishing minimum selection and training standards, and improving management practices. The proposed budget for POST is $28.7 million, a reduction of $23.7 million, or 45.2 percent from the estimated current year expenditures. This decrease is due to the elimination of the local assistance program that partially reimburses local law enforcement agencies for certain training costs. The portion of local law enforcement officer training costs paid by the state would be the responsibility of local law enforcement agencies. The budget proposes transfer of $14.3 million from the Peace Officers' Training Fund to the General Fund.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$1	$1	$0	0.0%
Peace Officers' Training Fund	51,172	27,485	-23,687	-46.3%
Reimbursements	1,259	1,259	0	0.0%
Total	$52,432	$28,745	-$23,687	-45.2%

ENERGY

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3360 Energy Resources, Conservation, and Development Commission

The California Energy Commission (CEC) develops and implements California's energy policy. Specifically, the Commission (1) maintains historical energy data and forecasts future statewide energy needs; (2) sites and licenses thermal power plants; (3) promotes energy efficiency and energy conservation programs and regulations; (4) develops renewable energy resources and alternative energy technologies; and (5) plans for and directs state response to energy emergencies. The Commission's mission is to assess, advocate and act through public-private partnerships to improve energy systems that promote a strong economy and a healthy environment.

Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$250	$0	-$250	-100.0
St. Energy Conservation Assis. Acct.	$6,778	$37,500	30,722	453.3
Less Ln Repay. to St. En. Cons. & Assis. Acct.	($3,820)	($4,703)	-883	0.0
Mot. Vehicle Acct, St. Trans. Fund	$126	$125	-1	-0.8
Diesel Emission Red. Fund	$224	$0	-224	-100.0
Pub. Int. Res., Dev. & Dem. Fund	$116,166	$66,982	-49,184	-42.3
Renew. Resource Trust Fund	$108,613	$183,456	74,843	68.9
Loc. Juris. Energy Assis. Acct.	$4,203	$1,328	-2,875	-68.4
Less Repay. to Loc. Juris. En. Assis. Acct	($796)	($913)	-117	0.0
Energy Resources Programs Acct.	$47,797	$46,388	-1,409	-2.9
Energy Tech. Res., Dev. & Dem. Acct	$2,765	$958	-1,807	-65.4
Less Loan Repay. To Energy Tech. Res., Dev. & Dem. Acct.	($232)	($75)	157	0.0
Loc. Gov. Geo. Res. Rev. Subacct, Geo. Res. Dev. Acct.	$6,119	$1,300	-4,819	-78.8
Petrol. Violation Escrow Acct.	$440	$434	-6	-1.4
Katz Schoolbus Fund	$0	$1,988	1,988	0.0
Federal Trust Fund	$9,165	$9,024	-141	-1.5
Reimbursements	$12,519	$6,245	6,274	-50.1
Renewable Energy Loan Loss Reserve Fund	$9,900	$0	-9,900	-100.0
Total	**$320,217**	**$350,037**	**$29,820**	**9.3**

Highlights

Significant increases in expenditures include the following:

- The budget increases the expenditure from the Renewable Resource Trust Fund by $75 million, but the fund realizes no significant change in its revenue stream. This fund rewards new renewable resource projects, subsidizes old ones and finances research of other specified renewable energy projects.
- The CEC will issue a $30 million revenue bond. The proceeds of the bond will be placed in the State Energy Conservation Assistance Account and loaned to local public entities for specified energy efficiency projects.
- The budget proposes a $2 million increase in funding from the Katz Schoolbus Fund to finance phase 5 of the Katz Safe Schoolbus Clean Fuel Efficiency Demonstration Program, providing CEC with resources to replace approximately 20 pre-1977 school buses and administer the program through June 30, 2004.

Decreases from the following funds partially offset the increases described above:

- $49 million from the Public Interest Research, Development and Demonstration Fund,
- $10 million from the Renewable Energy Loan Loss Reserve Fund, and
- $19 million from twelve other funds, including the General Fund

Issues

Fee Report. The Legislature required the CEC to submit a report by January 1, 2003 detailing alternative fee structures for both: (a) developers seeking approval for site power plants and (b) generators. The intent was to find a revenue stream to cover the ongoing compliance costs associated.

The report requirement was in response to the Governor's 2002 budget proposal to raise fees on power plants and a recommendation from the Legislative Analyst's Office (LAO) to raise fees on plants and generators. The subcommittee raised many concerns about implementation of the Governor's proposal and the LAO recommendation when the commission's budget was heard.

The Commission recommended that the current funding mechanism (charges to electricity ratepayers) remain intact to maintain the perception of the Commission's independence and objectivity. Nevertheless, it is acknowledged that imposing a fee on developers to reimburse the General Fund would avoid the perception problem and would balance the costs and benefits of the Siting and Compliance Program between developers and ratepayers.

Raising Fees? Last year, the Legislature authorized the commission to raise the Energy Resources Protection Account (ERPA) fee. The fee may be increased each November. Does the commission intend to raise the fee in November 2003?

8660 Public Utilities Commission

The California Public Utilities Commission (PUC) is responsible for the regulation of utilities and transportation industries to ensure the delivery of stable, safe, and economical services. The PUC traditionally has met this responsibility by enforcing safety regulations and/or controlling industry rates for service.

The budget proposes a reduction in the commission's budget from $1.5 billion in the current year to $1.3 billion in the budget year, reducing expenditures by $217 million, almost 15 percent. The budget and accompanying material provides very little detail about what changes in the commission's budget justify such a large year-to-year reduction.

Highlights

No General Fund Cost. Just as in the current year, there is no General Fund appropriation proposed for 2003-04. In 2001-02, the Legislature appropriated $150 million (General Fund) to the commission.

Universal Telephone Programs. The Administration appears to be proposing the following reductions in appropriations associated with the Universal Telephone Program.

High Cost Fund-B	-$55.3 million
Universal Lifeline Telephone Service Trust Fund	- 45.7
California Teleconnect Fund	-120.1

Neither the budget nor the required Budget Change Proposal (BCP) provide any information about how the reduction was calculated or whether the program can sustain the reduction.

Rural Grants. AB 140 (Strom Martin) establishes a grant program to improve rural telephone infrastructure. The Administration proposes making the first grants of the program in the budget year, at a total cost of $10.1 million.

Issues

Administration of the Universal Telephone Accounts Need Greater Scrutiny. Last year, the Legislature transferred over $300 million from the High Cost fund, on the grounds that the accounts had unused surpluses. The Legislature assumed the funds could be transferred without hurting services or requiring an increase in the surcharges which supply the funds. During the Interim, it appeared that the commission intended to adjust fees within the universal telephone service program. It is not clear whether the changes were the result of the transfers. The commission may wish to explain the likely changes and whether the transfers affected the funds' ability to meet statutory program requirements.

In the budget, the Administration proposes reducing by $130 million expenditures from certain lifeline accounts. Why is the change being made? Will it reduce services?

Rural Grant Program. Last year, the Legislature deferred approving the Rural Grant program until the commission developed a grant application and award criteria. It was not clear last year whether the Administration had a plan for allocating the funds to their highest and best use. The Legislature required the commission to submit a report, no later than January 15, 2003, on the likely benefits and costs of the grants. As of February 9, the commission has not submitted the report. Before the Legislature authorizes the start-up of a $10 million program, it should have the benefit of the commission's report.

ORA Report. The subcommittee relaxed certain requirements on the budget of the commission's Office of Ratepayer Advocate. In exchange for reduced reporting requirements, the subcommittee proposed and included in the trailer bills statutory language requiring the office to report its budget to the fiscal committees when the Governor released the budget. As of February 9, the commission failed to file the report on ORA's budget.

8665 Consumer Power and Conservation Financing Authority (CPA)

Senate Bill 6 (Burton), Chapter 10 of the 2001-02 First Extraordinary Session, established the authority. Under the bill, the authority may take actions, including issue revenue bonds, for the purposes of:

- Establishing and financing activities to supplement the state's power supplies and ensure sufficient electricity supplies at reasonable prices,
- Financing natural gas transportation and storage,
- Achieving adequate energy reserve capacity within five years,
- Financing replacement or retrofit of old and inefficient power plants, and
- Ensuring supply sufficiency.

Highlights

In 2002, the Legislature changed the funding source of the CPA from the General Fund to a special fund. The special fund source is a $10 million loan, to be repaid when the CPA begins generating interest income from the projects it finances.

Issues

- ***Repaying the Start Up Loan in the Current Year.*** The CPA was to have repaid $1 million of its loan on June 30, 2003. It will only be able to repay about half the loan. Through the deficiency process, the Legislature has authorized the authority to extend the loan for six months, making January 1, 2004 the new due date for the first loan payment. The Legislature may have to monitor more closely the authority's income and revenue streams.
- ***Energy Resources Investment Plan Is Due Soon.*** The CPA's authorizing statute requires it to submit an annual *Energy Resources Investment Plan* on February 15. The plan addresses issues of supply, reliability, and environmental quality. It outlines a strategy for cost-effective energy resource investments, including a financing plan. The subcommittee will want to consider the findings of the report and take testimony on the plan.
- ***Report on the Authority's Long Term Budgetary Needs.*** The subcommittee proposed, and the conference committee concurred in, a supplemental report requirement that the authority report on the needs of the authority. The report was to answer the question: How can the Legislature determine

whether the authority is properly funded? The report was due on December 31, 2002. Before considering the authority's budget, the subcommittee may want to review this report.

8770 Electricity Oversight Board

The Electricity Oversight Board (EOB) is part of the regulatory oversight structure that was established by the legislation restructuring California's electricity industry in 1996. The board is charged with ensuring the reliability of the electricity transmission system and in the power market.

The budget proposes total expenditures of $3.7 million ($0 General Fund), an increase of $4,000 (0.1 percent) from the current-year budget.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$231	$0	-$231	-100.0
PUC Utilities Reimbursement Acct.	3,003	3,226	223	7.4
Energy Resources Protection Acct	471	483	12	2.5
Total	$3,705	$3,709	$4	0.1

Issues

Funding Levels of the EOB. Last year, the Legislature spent considerable time examining the role of the EOB and justifications for its current funding level. The Legislature was critical of its budget near $4 million (50% OE&E) despite losing both of the board's original purposes of overseeing the now-defunct Power Exchange and overseeing the Independent System Operator.

The Legislature requested a report addressing the board's role in the electricity regulatory field and specific schedules and workloads justifying the upkeep of its $3.7 million budget. The report was recently transmitted to the Legislature detailing the Board's role and workload schedules.

The report concludes that the EOB's main role is as an advocate on behalf of the state to the Federal Energy Regulatory Commission (FERC). In the report, the EOB does concede that multiple agencies (the Public Utilities Commission and the Department of Water Resources) advocate on behalf of the state before FERC. Although, the EOB contends that they present different roles in advocating to FERC.

While the report is rich in detail of the dockets and legal efforts the EOB has before FERC, the report sidesteps the specific workload and equipment schedules saying:

> "As a practical matter, it is extremely difficult to accurately attribute a specific resource allocation to each (FERC) docket… Many FERC cases proceed in alternating spurts and lulls. A matter may require several people to work feverishly for a few days to answer a motion or for a week to write a brief and then may sit for several months awaiting the next order from a judge."

In light of this report, the EOB has confirmed they may have redundant activities with other departments in their advocacy before FERC, or at least could be functioning under another department. Also, the EOB has yet to produce a precise workload and equipment schedules for justification of their $3.7 million budget as requested by the Legislature last year. Until accurate assessments of definitive activities of the EOB and the subsequent workload are available, the Legislature will not be able to properly evaluate on this budget item

GENERAL GOVERNMENT

OVERVIEW

The departments, boards, and commissions under Subcommittee 2's jurisdiction are:

- Office of Emergency Services (OES)
- Native American Heritage Commission (NAHC)
- California Horse Racing Board (CHRB)
- Department of Food & Agriculture (CDFA)
- Seismic Safety Commission (SSC)
- California Law Review Commission (CLRC)
- Commission on Uniform State Laws (CUSL)

The CHRB, and the NAHC all have reasonable reductions or fund shifts proposed and will not be discussed. The OES, the CDFA, the SSC, the CLRC, and the CUSL all have significant proposals that warrant discussion.

0690 Office of Emergency Services

The Office of Emergency Services (OES) coordinates emergency activities to save lives and reduce property losses during disasters and acts as the state's conduit for federal assistance related to recovery from disasters. OES provides leadership assistance and support to state and local agencies in planning and preparing for the most effective use of federal, state, local, and private resources in emergencies. The emergency planning is based on a system of mutual aid in which a jurisdiction first relies on its own resources and then call for assistance from its neighbors.

The budget proposes total expenditures of $651.9 million ($58.8 million General Fund) for state operations and local assistance, a decrease of $71.5 million (9.9 percent) below the current year. As can be seen in the table below, the majority ($66 million) of this reduction is due to a decrease in federal funds. In the last several years, the federal government has used an accelerated payment schedule in order to pay out existing disaster claims. As a result of this effort, the number of claims for disaster assistance is anticipated to decrease in the budget year.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$56,110	$50,847	-$5,263	-9.4
Other Funds	4,720	3,798	-922	-19.5
Federal Trust Fund	660,511	595,178	-65,333	-9.9
Reimbursements	2,113	2,113	0	0.0
Total	$723,454	$651,936	-$71,518	-9.9

Highlights

General Fund Reductions. The budget proposes General Fund reductions of $8.1 million in the budget year. Most of the reduction is attributed to $5.1 million in reduced local assistance, although the remaining $3 million will cause significant staff reductions in the Pasadena office and North Coast office, including the elimination of the Annual Earthquake Campaign and the Dam Safety Program. The office states that these reductions will "severely hinder OES's public safety mission and its ability to fulfill its proactive role in a manner that the public has rightfully come to expect."

8570 Department of Food and Agriculture

The department promotes and regulates the state's agricultural industry through:

- Eradication and control of harmful plant and animal pests and diseases.
- Marketing, exporting, and other related assistance for various agricultural commodities.
- Assurance of true weights and measures in commerce.
- Financial and administrative assistance to the state's 80 district, county, and citrus fairs.

The budget proposes total expenditures of $269.3 million ($86.6 million General Fund) a decrease of $32.3 million (10.7 percent) from the current-year budget.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
State Operations & Local Assistance				
General Fund	$91,970	$86,598	-$5,372	-5.8
Agriculture Fund, Totals	96,645	93,381	-3,264	-3.4
Agricultural Export Promo Acct	600	600	0	0.0
Fairs and Exposition Fund	19,238	19,826	588	3.1
Satellite Wagering Account	12,663	12,599	-64	-0.5
Harbors & Watercraft Rev Fund	989	1,171	182	18.4
Agriculture Building Fund	1,606	1,606	0	0.0
Agriculture Building Fund, Sect. 625	90	90	0	0.0
Less expenditures already reflected in other appropriations for CDFA	(1,696)	(1,696)	0	0.0
Other Funds	1,466	1,000	-466	-31.8
Federal Trust Fund	65,891	42,681	-$23,210	-35.2
Reimbursements	8,498	7,638	-860	-10.1
Pierce's Disease Management Account	20,736	20,936	200	1.0
Less Funding Provided by the General Fund/Federal Trust Fund	(17,396)	(17,403)	(7)	0.0
Total	$301,300	$269,027	-$32,273	-10.7

Highlights

Hawaii Medfly Rearing Facility. The CDFA is requesting $11 million for a new Medfly Rearing Facility to help increase and stabilize sterile medfly production for the PRP. The department currently relies on a combination of one production facility operated by itself and two United States Department of Agriculture (USDA) facilities in Hawaii and Guatemala. The department contends that rising demand for USDA medflys and the debilitated condition of its current production facility has made supplying the PRP difficult. This project would double medfly production by building a second production facility which would provide a sufficient and stable source of medflies for the PRP. The department estimates that it will cost an additional $1.9 million to equip the facility and $1.35 million in annual ongoing operating costs.

General Fund Reductions. The budget proposes just under $5 million in General Fund reductions to various programs in this department. The impacted programs include the Weed and Vertebrate Program, the Biological Control Program, Agriculture Inspection Stations, and the "Buy California" Program.

Agriculture Fund Loan Extension. The budget proposes extending repayment of a $15 million loan to the General Fund last year 2004-05.

Issues

Medfly Preventive Release Program. The budget proposes $8.9 million from the General Fund and 138 positions to provide for Mediterranean Fruit Fly (medfly) preventative control efforts on an ongoing basis. The department began efforts to control the impact of the medfly on California's agricultural industry in 1975. Since 1980, the state has spent around $150 million from the General Fund to support this effort, with a similar amount provided by the federal government.

The current Preventative Release Program (PRP) began in 1996 and involves raising sterile medflies and releasing them throughout a 2,500 square mile area in the Los Angeles Basin. Total program costs are approximately $18 million annually, shared equally between the state and federal government. The Legislature approved this as a five-year program with a June 30, 2001 sunset date. In both FY 2001-02 and FY 2002-03, the program was extended on one-year basis.

Two years ago, the Legislature directed CDFA to provide information detailing how the funding source for the PRP could be shifted in whole, or in part from the General Fund to the Agriculture Fund. A report was requested, due January 10, 2002, from the department to investigate alternative funding sources for the program. The PRP was funded for that budget year.

Last year, the department did not submit the report. The LAO recommended legislation to develop an assessment program that would equitably distribute half of the cost of the PRP across those industries that most benefit from the absence of the medfly, with the other half coming from the General Fund. The Legislature again requested a report for alternative funding sources for this program. The department agreed to contract with the University of California to study alternative funding sources for the PRP. The Legislature then reluctantly approved $9.2 million for the program on a one-year basis.

This year, the Administration proposes a $8.9 million budget for the PRP and to make it a permanent expenditure of the General Fund. Also proposed in the budget is capital outlay project of $11 million for a new Medfly Rearing Facility in Hawaii to be funded by the General Fund (see ***Highlights*** section below).

Until the Legislature receives a report from the department, it is extremely difficult to consider any alternative revenue source for the PRP. In light of the condition of the General Fund and the lack of responsiveness by the department to Legislative requests for the past two years, the Legislature should consider delaying approval for the PRP program and the related capital outlay project until a assessment proposal or alternative revenue source can be secured for the long term viability of this program.

8690 Seismic Safety Commission

The Seismic Safety Commission was established to improve earthquake preparedness and safety in California. Specifically, the commission is responsible for providing a consistent framework for earthquake-related programs and coordinating the administration of these programs throughout the state government. The 17-member commission performs policy studies, reviews programs, investigates earthquake incidents, and conducts hearings on earthquake safety. The commission advises the

Legislature and the Governor on Legislative proposals, the state budget, and grant proposals relating to earthquake safety.

The budget proposes total expenditures of $959,000 ($0 General Fund) a decrease of $197,000 (17 percent) from the current-year budget.

Summary of Expenditures (dollars in thousands)	2002-2003	2003-2004	$ Change	% Change
General Fund	$881	$0	-$881	-100.0
Insurance Fund	0	884	884	0.0
Earthquake Emergency Investigations Account	100	0	-100	-100.0
Reimbursements	175	75	-100	-57.1
Total	$1,156	$959	-$197	-17.0

Highlights

Funding for the Seismic Safety Commission. The budget proposes shifting funding support for the commission from the General Fund to the Insurance Fund. The insurance fund would raise the additional revenue through a proposed earthquake insurance policy fee of $1 per policy sold statewide.

8830 California Law Revision Commission

The primary objective of the California Law Revision Commission is to make recommendations to the Governor and the Legislature for revision of the law. The CLRC assists the Governor and the Legislature in keeping the law up to date by studying complex subjects, identifying major policy questions for legislative attention, gathering the views of interested persons and organizations, and drafting recommended legislation for consideration.

Issues

Elimination of the Commission. The CLRC is proposed for elimination. Last year, the commission was funded through the General Fund for $660,000 and has 5 staff positions. The CLRC provides an commonly unknown, yet valuable service to the Legislature, most recently in recommending code changes to facilitate municipal and superior court consolidation in California, amongst other projects. In light of the condition of the General Fund, possible reductions of $95,000 for the budget year have been identified as an alternative to elimination.

8840 Commission on Uniform State Laws

In conjunction with other states, the Commission on Uniform State Laws (CUSL) drafts and presents to the Legislature uniform laws deemed desirable and practicable by the National Conference of Commissioners on Uniform State Laws for adoption by various states.

Highlights

Elimination of the Commission. The CUSL is proposed for elimination. Last year, the commission was funded through the General Fund for $138,000.

SUBCOMMITTEE NO. 3

HEALTH, HUMAN SERVICES, LABOR, and VETERANS AFFAIRS

HEALTH

HEALTH AND HUMAN SERVICES OVERVIEW

Summary of Mid-Year Reductions

In December, the Governor proposed mid-year reductions which contained significant policy changes and program reductions for health and human services programs. Specifically, the Administration proposed reductions of over $439 million (General Fund), including reversions, program reductions, fund shifts, and restructuring, for 2002-03 and over $1.5 billion (General Fund) for 2003-04.

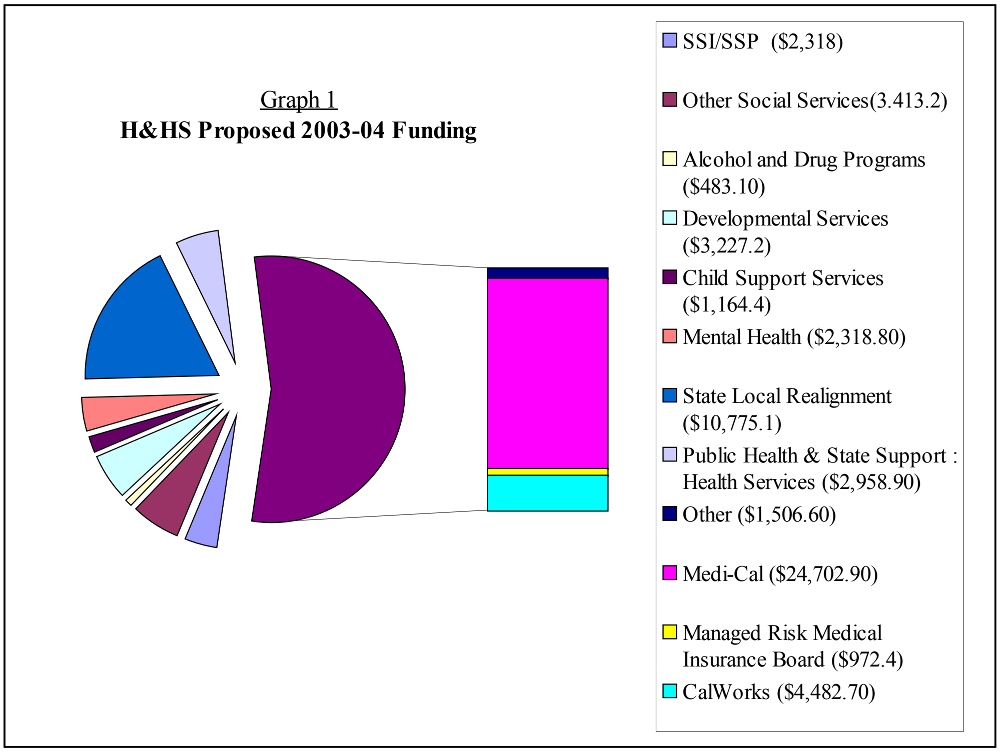
At the time of the publishing of this analysis, the Special Session mid-year reduction bill contained reductions of about $260 million (General Fund) for health and human services for 2002-03. Key items of reduction included the following:

- Suspending the SSI/SSP COLA for June 2003 for savings of $24.1 million (General Fund).
- Suspending the CalWORKs COLA for savings of $12.2 million (TANF federal block grant funds).
- Shifting $142.7 million in General Fund support for the purchase of services for consumers with developmental disabilities who are served by Regional Centers to federal fund support by expanding the Home and Community Based Waiver.
- Reducing the Prostate Cancer Treatment Program for savings of $10 million (General Fund).

The Legislature opted to defer decision on several of the Mid-Year Reductions to the budget year in order to afford the public, constituency groups and themselves with the opportunity to more thoroughly discuss and debate these substantive policy issues through the budget and policy committee processes.

Summary of Governor's Proposed 2003-04 Budget

The Governor's budget for health and human services proposes a total of $61.4 billion in combined state and federal funds as noted in the table. The General Fund portion is $15.1 billion, or 24.1 percent of the state's total General Fund expenditures.



The General Fund portion reflects a net decrease of $7.882 billion, or 34 percent, over the revised 2002-03 budget. The Administration's proposed General Fund decrease assumes (1) adoption of the Governor's Mid-Year Reduction adjustments, including adjustments which significantly affect the budget year and (2) a shift to the counties of $7.9 billion in General Fund expenditures for health and human services programs through the proposed Realignment.

The Governor's proposed budget for health and human services is built upon the following *key* assumptions:

- Shifts $7.9 billion in estimated health and human services program expenditures to the counties under a Realignment proposal (discussed below).
- Reduces Medi-Cal and non-Medi-Cal provider rates by a total of 15 percent for savings of $1.427 billion ($720.5 million General Fund). The savings level assumes adoption of trailer bill language to enact a ten percent reduction as of April 1, 2003, and an additional 5 percent reduction by July 1, 2003.
- Recommends legislation to suspend the annual cost-of-living-adjustment for SSI/SSP grants for savings of $372.3 million (General Fund). This proposed legislation would not affect the pass through of the federal SSI cost-of-living-adjustment.

- Recommends legislation to reduce the SSI/SSP payment standard to the minimum federally required level for savings of $662 million (General Fund). This proposal would reduce grants by 6.5 percent ($708 for individuals and $1,225 for couples), and would make 14,387 individuals completely ineligible for SSI/SSP and all associated services.
- Seeks legislation to reduce the maximum aid payment under CalWORKS by 6.2 percent for savings of over $235 million (TANF federal block grant funds). A family of three would receive $637 per month of eligibility. No General Fund savings are achieved through this proposal.
- Proposes legislation to rescind the 1931(b) Medi-Cal eligibility expansion (currently at 100 percent of federal poverty) and to reinstate the "100-hour a month work limit" for savings of $236 million ($118 million General Fund). These savings estimates assume that about 293,000 low-income, uninsured adults will not be eligible for Medi-Cal coverage.
- Seeks legislation to rollback the extension for the Aged and Disabled Medi-Cal eligibility category from 133 percent of federal poverty to the SSI/SSP income level for savings of $127.6 million ($63.8 million General Fund). This savings estimate assumes that 48,300 aged recipients and 20,540 disabled recipients are eliminated from Medi-Cal coverage. Under this rollback, the Medi-Cal income threshold would be $708 per month maximum for individuals and $1,225 per month maximum for couples. Individuals and couples above these income levels would have to pay a share-of-cost (i.e., spend down) in order to receive Medi-Cal coverage. Generally, the primary Medi-Cal benefit these individuals typically need is access to pharmacy services.
- Recommends legislation to reinstate the Quarterly Status Report effective April 1, 2003 and to change statute regarding the determination of Medi-Cal eligibility for savings of $10 million ($5 million General Fund) in 2002-03 and $170 million ($85 million General Fund) in 2003-04. These savings estimates assume that 33, 900 adults will be terminated from Medi-Cal coverage in 2002-03 and 193,123 adults are dropped in 2003-04.
- Eliminates eight Medi-Cal Optional Benefits effective April 1, 2003 and an additional ten benefits as of October 1, 2003 for savings of $126.5 million ($63.2 million General Fund) in 2002-03 and $723.7 million ($361.8 million General Fund) in 2003-04.
- Proposes to grant the Department of Developmental Services broad authority through legislation to institute statewide standards for the purchase of services for individuals with developmental disabilities who receive services through the Regional Center system for savings of $100 million (General Fund) in 2003-04.
- Assumes a savings of $51.8 million (General Fund) by requiring a 25 percent county share-of-cost for the federal penalty levied against California due to the state's delay in implementing an automated system for the collection of child support.

Each of these proposals as well as others are discussed in more detail below under each department.

Summary of Governor's Proposed Realignment

The proposed Realignment package consists of four components in the health and human services area (over $7.9 billion), plus a court security plan for the Trial Courts ($300 million). The Administration states that this proposed Realignment package would be *entirely* separate and distinct from the Realignment of 1991-92.

From a fiscal perspective the Administration assumes the following:

- General Fund Savings $8.154 billion

• State Operations Reductions	($3 million)
• Shift Proposition 99 Funds to counties	$58 million
• Child Care COLA and Stage 3 Growth	$64 million
• **Cost to Counties**	**$8.273 billion**
• Estimated Revenues from Tax Changes	$8.334 billion
• Proposition 99 and Proposition 10 Backfill	($96 million) ($58 million is Proposition 99)
• Proposition 99 Funding	$58 million
• **Estimated Total Revenues**	**$8.296 billion (Reserve of $23 million)**

The proposed new dedicated Realignment revenue would stream from the following sources:

• Sales Tax increase of one percent	$4.584 billion
• Personal Income Tax (10-11 percent)	$2.580 billion
• Tobacco Excise Tax ($1.10 increase)	$1.170 billion
• **Revenues from Tax Changes**	**$8.334 billion**

For health and human services, the Administration proposes four components: (1) "Healthy Communities", (2) "Long-Term Care", (3) "Children and Youth", and (4) "Mental Health and Substance Abuse". These four components consist of the following:

- $2.7 billion for Healthy Communities, including a 15 percent share-of-cost (non-federal share) for Medi-Cal, a 50 percent share-of-cost for CalWORKS Employment Services and CalWORKS Administration, Food Stamp Administration, all of the community clinic programs, Cash Assistance for Immigrants, and numerous public health programs;

- $2.6 billion for Long-Term Care, including nursing homes and the In-Home Supportive Services (IHSS) Program;

- $2.3 billion for Children and Youth, including Child Care, Child Welfare Services, Foster Care Grants and Administration, Adoption Assistance, Kin Gap, and Child Abuse Prevention and Treatment; and

- $306 million for Mental Health and Substance Abuse, including local programs for drug and alcohol services (Proposition 36 funding), the Integrated Services for Homeless Adults, the Children's System of Care Program, and Drug Courts.

The Administration proposes trailer bill legislation for each of these components. At this juncture, the language is crafted broadly to express the Legislature's intent to enact legislation to (1) transfer the specified program and its non-federal share of expenditures, (2) maintain state oversight of said programs, and (3) become operative only if dedicated revenues are enacted for this purpose.

The proposal assumes that 2003-04 fiscal allocations to counties would be based on the proposed level of funding for counties for each of the programs, absent Realignment, in order to avoid program disruptions in the budget year. However for 2004-05, the Administration assumes that a single allocation would be made to counties based on a formula to be developed through discussions. As such, this would potentially serve as a type of "block grant" to the counties whereby the counties could conceivably shift funding across programmatic areas.

The Legislature may want to consider several factors when reviewing this proposal. First, any transfer of program and fiscal responsibility should be designed to assist both the state and counties in maximizing their service delivery responsibilities. If service delivery is maximized, the program participants will likely be better served and program efficiencies will more likely occur.

Second, the dedicated revenues provided for the program transfers should have a growth rate that is comparable with the anticipated growth of the program being transferred. If this is uncertain, a trigger mechanism should be considered in order to bring forth an expenditure or revenue discussion. The Realignment of 1991-92 included a "poison pill" provision for this purpose.

Third, the programs transferred should be programs that allow counties and constituency groups flexibility to craft innovative approaches that utilize community-based resources and services. Under the Realignment of 1991-92, mental health services were re-focused and shifted from a model heavily reliant on state hospital services to a model that now offers a broader array of community based options. Both fiscal incentives and policy flexibility were made available to allow for innovation and some experimentation.

Each of the four health and human services components are discussed in more detail below, under each applicable department.

HEALTH

0530 California Health and Human Services Agency

The California Health and Human Services Agency (CHHS) administers the state's health, social services, rehabilitative and employment programs. The Secretary of the CHHS advises the Governor on major policy and program matters and oversees the operation of the agency departments. The purview of the CHHS includes the departments of Aging, Alcohol and Drugs, Community Services and Development, Developmental Services, Health Services, Mental Health, Rehabilitation, Social Services, and Employment Development, the Health and Human Services Data Center, the Office of Statewide Health Planning and Development, and the Managed Risk Medical Insurance Board, and the Emergency Medical Services Authority.

Through the Budget Act of 2001 and SB 456 (Speier), Statutes of 2001, the Office of Health Insurance Portability & Accountability Act (HIPAA) Implementation was created. This office resides within the CHHS.

The Office of HIPAA Implementation has statewide responsibility for the implementation of the federal HIPAA. The portion of HIPAA dealing with administrative simplification requires all billing and other electronic data transmissions to be standardized, as well as establishing new standards for the confidentially and security of this information. The office was established to direct and monitor this process.

Summary of Funding

The budget proposes expenditures of $5.9 million ($4.3 million General Fund), or an increase of about $800,000 over the revised 2002-03 budget, and 33 positions for the agency. Of this amount, almost $3.6 million and 11 positions are for the Office of HIPAA Implementation. The Office of HIPAA Implementation was reduced by $823,000 (General Fund) on a one-time only basis as part of the Governor's Mid-Year Adjustment proposal.

2400 Department of Managed Health Care

The purpose of the Department of Managed Health Care (DMHC) is to protect the public through administration and enforcement of laws regulating health care plans. The administration of these laws involves a variety of activities including licensing, examination, and responding to public inquiries and complaints. The program enforces its laws through administrative and civil action. Specifically, the DMHC licenses health care plans, conducts routine financial and medical surveys, and operates a consumer services toll-free complaint line.

The DMHC has three advisory boards--the Advisory Committee on Managed Care, the Clinical Advisory Board, and the Financial Standards Solvency Board. In addition, the Office of the Patient Advocate located within the DMC will help ensure that the needs of managed care consumers are heard and met.

Summary of Funding

The budget proposes total expenditures of $34.5 million (Managed Care Fund) and 297 personnel-years for the DMHC, which includes $2.1 million for the Office of Patient Advocate. This reflects a net increase of $1.9 million (Managed Care Fund) over 2002-03. The $1.9 million (Managed Care Fund) difference is primarily due to two items. First, a one-time only reduction of $558,000 and 14 positions was enacted as part of the Governor's Mid-Year Reduction proposal. Second, an increase of $834,000 (Managed Care Fund) is proposed for 2003-04 to reduce the department's salary savings level to seven percent. This will fund positions currently required to be kept vacant.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
Health Care Service Plans	$30,615	$32,409	$1,794	5.9
Office of Patient Advocate	2,018	2,135	117	5.8
Total, Health Plan Program	$32,633	$34,544	$1,911	5.9

4120 Emergency Medical Services Authority

The overall responsibilities and goals of the Emergency Medical Services Authority (EMSA) are to (1) assess statewide needs, effectiveness, and coordination of emergency medical service systems; (2) review and approve local emergency medical service plans; (3) coordinate medical and hospital disaster preparedness and response; (4) establish standards for the education, training and licensing of specified emergency medical care personnel; (5) establish standards for designating and monitoring poison control centers; (6) license paramedics and conduct disciplinary investigations as necessary; (7) develop standards for pediatric first aid and CPR training programs for child care providers; and (8) develop standards for emergency medical dispatcher training for the "911" emergency telephone system.

Summary of Funding

The Administration proposes to eliminate the EMSA and transfer it to the Department of Health Services as part of the Mid-Year Reduction proposal. This proposed transfer would result in savings of $342,000 ($132,000 General Fund) due to staffing adjustments. The Legislature opted not to proceed with the transfer at this time and may have further discussion during future budget deliberations.

It should be noted that the Administration's budget assumes total funding of $14.9 million ($3.9 million General Fund) within the DHS, to reflect the proposed transfer, for all of the emergency medical services activities.

4250 California Children and Families Commission

The California Children and Families First Act of 1998 created this commission effective December 1998. The Commission consists of nine members—seven voting members and two ex-officio members. Three of the members are appointed by the Governor, two by the Senate Rules Committee, and two by the Speaker of the Assembly.

The commission is responsible for the implementation of comprehensive and integrated solutions to provide information and services promoting, supporting, and improving the early childhood development of children through the age of five. These solutions are to be provided either directly by the commission or through the efforts of the local county commissions.

Funding is provided through a 50-cent-per-package surtax on cigarettes, as of January 1, 1999, and an equivalent surtax on other tobacco-related products, as of July 1, 1999. These revenues are deposited in the California Children and Families Trust Fund. As required by the proposition, a portion of these revenues are transferred to the Department of Health Services to backfill for specified decreases in Proposition 99 funds (i.e., Cigarette and Tobacco Product Surtax Funds).

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
Administrative Functions	$6,212	$6,273	61	1
Local Assistance—Counties	542,288	451,856	(90,432)	16.6
Mass Media Account	48,365	35,737	(12,628)	26.1
Education Account	55,246	29,775	(25,471)	46.1
Child Care Account	28,832	18,132	(10,700)	37.1
Research & Development Account	39,924	18,147	(21,777)	54.5
Unallocated Account	19,634	12,066	(7,568)	38.5
Total Expenditures	$740,501	$571,986	($168,515)	22.7

Summary of Funding

The budget proposes total expenditures of $572 million (special trust funds) for a decrease of $168.5 million over the revised current year. This reduction is due to a decline in revenues and a decline in carry-over funds which were available in the first year of implementation and have since been expended. It should be noted that the budget proposes to provide $62 million (Cigarette and Tobacco Surtax Funds) to backfill for the anticipated loss of revenue associated with the Governor's proposed realignment proposal.

The California Children and Families Commission funds must be used to supplement, not supplant, existing funds. The funds are distributed across accounts as required by Proposition 10. The funds are continuously appropriated pursuant to Section 30131.3 of the Revenue and Taxation Code.

The commission began funding initiatives using the various accounts in January 2000. These projects address recognized needs related to children's health care, child care and development, and family literacy.

4260 Department of Health Services

The goals of the Department of Health Services (DHS) are to (1) promote an environment that contributes to human health and well-being; (2) assure the availability of equal access to comprehensive health services using public and private resources; (3) emphasize prevention-oriented health care programs; (4) promote the development of knowledge concerning the causes and cures of illness and the means of delivering health services to the public; and (5) assure economic expenditure of public funds to serve those persons with the greatest health care needs.

The budget proposes expenditures of $27.7 billion ($7.6 billion General Fund), or a decrease of $4.6 billion ($ 3.7 billion General Fund) over the revised 2002-03 budget. Of the total budget amount, $26.8 billion is for local assistance and $837.3 million is for state support. State support expenditures include funds for 5,674 personnel-years.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
Program Source				
Health Care Services	$31,295,224	$26,636,486	($4,658,738)	(14.9)
Public and Environmental Health	886,314	964,516	78,202	8.8
State Mandated Local Programs	9	9		
State Administration	42,539	44,957	2,418	5.7
Emergency Medical Services Authority	--	14,939	14,939	100
Totals, by Program Source	$32,224,086	$27,660,907	($4,563,179)	(14.2)
Funding Source				
General Fund	$11,257,762	$7,555,551	($3,702,211)	(32.9)
Federal Funds	18,256,638	17,663,143	(593,495)	(3.3)
Other Funds	2,709,686	2,442,213	(267,473)	(9.9)
Totals, by Fund	$32,224,086	$27,660,907	($4,563,179)	(14.2)

The Medi-Cal Program

Summary of Funding

The entire Medi-Cal budget proposes expenditures of $27.7 billion ($7 billion General Fund, $3 billion Reimbursements from Counties). This reflects a *net* decrease of almost $3.6 billion (General Fund), or 33.9 percent less than the revised 2002-03 budget. This significant net reduction is attributable to several key factors, including the following:

- Transfers 15 percent of Medi-Cal benefit costs to the counties, along with a revenue stream, for savings of $1.6 billion (General Fund).
- Transfers fiscal responsibility, but not policy administration, of long-term care services to the counties, along with a revenue stream, for savings of $1.4 billion (General Fund).
- Reduces Medi-Cal and non-Medi-Cal provider rates by a total of 15 percent for savings of $1.427 billion ($720.5 million General Fund). The savings level assumes adoption of trailer bill language to enact a ten percent reduction as of April 1, 2003, and an additional 5 percent reduction (for a total of 15 percent) by July 1, 2003.
- Proposes legislation to rescind the 1931(b) Medi-Cal eligibility expansion (currently at 100 percent of federal poverty) and to reinstate the “100-hour a month work limit” for savings of $236 million ($118 million General Fund). These savings estimates assume that about 293,000 low-income, uninsured adults will not be eligible for Medi-Cal coverage.

- Proposes legislation to rollback the extension for the Aged and Disabled Medi-Cal eligibility category from 133 percent of federal poverty to the SSI/SSP income level for savings of $127.6 million ($63.8 million General Fund). This savings estimate assumes that 48,300 aged recipients and 20,540 disabled recipients are eliminated from Medi-Cal coverage.
- Proposes legislation to reinstate the Quarterly Status Report effective April 1, 2003 and to change statute regarding the determination of Medi-Cal eligibility for savings of $10 million ($5 million General Fund) in 2002-03 and $170 million ($85 million General Fund) in 2003-04. These savings estimates assume that 33, 900 adults will be terminated from Medi-Cal coverage in 2002-03 and 193,123 adults are dropped in 2003-04.
- Eliminates eight Medi-Cal Optional Benefits effective April 1, 2003 and an additional ten benefits as of October 1, 2003 for savings of $126.5 million ($63.2 million General Fund) in 2002-03 and $723.7 million ($361.8 million General Fund) in 2003-04.

Summary of Caseload

A. Description of Caseload. Presently about 6.5 million people, or one in five Californians, are eligible for Medi-Cal in any given month. According to the DOF, Medi-Cal provides health insurance coverage to 17.3 percent of Californians. Of the total eligibles about 45 percent, or 2.8 million people, are categorically-linked to Medi-Cal through enrollment in public cash grant assistance programs (i.e., SSI/SSP or CalWORKS).

Almost all Medi-Cal eligibles fall into four broad categories of people: (1) aged, blind or disabled; (2) families with children; (3) children only; and (4) pregnant women. Generally, Medi-Cal eligibility is based upon family relationship, family income level, asset limits, age, citizenship and California residency status. Other eligibility factors can include medical condition (such as pregnancy or medical emergency), share-of-cost payments (i.e., spending down to eligibility), and related factors that are germane to a particular eligibility category.

When eligibility is determined by the county, the county generally follows a hierarchy that would be most beneficial for the family. It should also be noted that there are about 170 categories or “aid codes” under which one may qualify for Medi-Cal, and that the Medi-Cal eligibility manual is over 1,800 pages long.

Generally, men and women who are not elderly and do not have children or a disability *cannot* qualify for Medi-Cal, no matter how low-income they are.

Over 1.5 million of the eligibles, or almost 25 percent of the total, are low-income persons who are aged (65 years or older), blind or disabled. Aged, blind and disabled individuals are eligible for Medi-Cal services through three different eligibility categories:

(1) SSI/SSP recipient and therefore categorically eligible for Medi-Cal (80 percent of the eligibles);

(2) “Medically Needy” individuals who are *not* receiving SSI/SSP and have incomes at 133 percent of poverty or below (15 percent of the eligibles); and

(3) Long Term Care individuals who are residing in nursing homes (4 percent of the eligibles).

Of these approximate 1.5 million eligibles, the disabled comprise about 61 percent of the total, the aged 37 percent and the blind almost two percent. It should be noted that over 60 percent of the aged or disabled Medi-Cal eligibles also have federal Medicare coverage. Since Medi-Cal is the payor of last resort, it is cost-beneficial for Medi-Cal to pay an individual’s Medicare premium, as well as deductibles and copayments in order to shift certain medical expenditures to 100 percent of federal funding. On the other hand, Medi-Cal provides on-going long-term care services and prescription drug coverage to these individuals whereas Medicare does not offer this costly coverage.

The “Medically Needy” category of Medi-Cal eligibility allows participation on a spend-down basis. This means that Medi-Cal will pay the portion of any qualifying medical expense that exceeds the person’s “share-of-cost”. The share-of-cost is the amount by which that individual’s income or assets exceeds the applicable Medi-Cal limits.

About 3.8 million eligibles, or 61 percent of the total eligibles, are in uninsured families with children. These people are eligible for Medi-Cal through three different eligibility categories:

(1) CalWORKS-linked family and therefore categorically eligible for Medi-Cal (41 percent of the eligible families but only 25 percent of the total Medi-Cal eligibles);

(2) 1931 (b) families who are families *not* receiving CalWORKS, have two-parents and have incomes at or below 100 percent of poverty;

(3) Medically Needy families who are families *not* receiving CalWORKS, have incomes at or below 100 percent of poverty and must spend down to be eligible for Medi-Cal.

In addition to the above outlined categories, uninsured children are also eligible for Medi-Cal through distinct categories of eligibility established just for children and *not* linked to CalWORKS or SSI/SSP. These categories are generally based upon a family’s income level, the age of the child and medical need (i.e., potential share of cost). A total of 435,000 children are estimated to be eligible in 2003-04 through the following categories:

(1) The 100 percent of poverty program provides coverage for children aged 6 though 18 years (148,00 estimated children);

(2) The 133 percent of poverty program provides coverage for children aged 1 through 5 years (132,000 estimated children);

(3) The Medically Indigent program provides coverage for children under age 21 who are in intact families where the parent(s) are employed (155,000 estimated children).

Uninsured pregnant women with family incomes at or below 200 percent of poverty are also eligible for Medi-Cal. Depending upon several eligibility factors, pregnant women can be covered under several of the above reference eligibility categories. Based on the latest data available, there were over 224,000 Medi-Cal deliveries in 2000.

B. Caseload Estimate For Budget Year and Affect of Eligibility Proposals. The revised caseload for 2002-03 of 6.5 million eligibles is 9.5 percent above the revised 2001 Budget Act level. However due to the Administration’s proposed reductions in eligibility, the budget assumes a total of less than 6.3 million eligibles for 2003-04, for a *net* reduction of 209,000 eligibles, or 3.2 percent less from the revised 2002-03.

The Administration proposes five key policy changes which if enacted, would significantly reduce Medi-Cal eligibility. Specifically, these proposals include:

- Rescinding the 1931 (b) eligibility category to eliminate about 293,000 people;
- Reinstating the Quarterly Status Report to eliminate about 193,000 people;
- Rolling back the Aged, Blind and Disabled Program from 133 percent to 100 percent of poverty to eliminate almost 69,000 people;

- Establishing new standards for counties to make Medi-Cal redeterminations to eliminate about 563,000 people in 2003-04 due to making timely redeterminations; and
- Eliminating the second-year of availability for Transitional Medi-Cal coverage to eliminate about 1,800 people from coverage.

These proposals are discussed in further detail under the "Issues" section below.

Summary of Reductions

- Transfers 15 percent of Medi-Cal benefit costs to the counties, along with a revenue stream, for savings of $1.6 billion (General Fund).
- Transfers fiscal responsibility, but not policy administration, of long-term care services to the counties, along with a revenue stream, for savings of $1.4 billion (General Fund).
- Reduces Medi-Cal and non-Medi-Cal provider rates by a total of 15 percent for savings of $1.427 billion ($720.5 million General Fund) in 2003-04. The savings level assumes adoption of trailer bill language to enact a ten percent reduction as of April 1, 2003, and an additional 5 percent reduction (for a total of 15 percent) by July 1, 2003. The Legislature did not adopt the current year reduction.
- Proposes legislation to rescind the 1931(b) Medi-Cal eligibility expansion (currently at 100 percent of federal poverty) and to reinstate the "100-hour a month work limit" effective April 1, 2003 for savings of $12.4 million ($6.2 million General Fund) in 2002-03 and $236 million ($118 million General Fund) in 2003-04. These savings estimates assume that about 293,000 low-income, uninsured adults will not be eligible for Medi-Cal coverage in the budget year. The Legislature did not adopt the current year reduction.
- Proposes legislation to rollback the extension for the Aged and Disabled Medi-Cal eligibility category from 133 percent of federal poverty to the SSI/SSP income level for savings of $127.6 million ($63.8 million General Fund). This savings estimate assumes that 48,300 aged recipients and 20,540 disabled recipients are eliminated from Medi-Cal coverage.
- Proposes legislation to reinstate the Quarterly Status Report effective April 1, 2003 and to change statute regarding the determination of Medi-Cal eligibility for savings of $10 million ($5 million General Fund) in 2002-03 and $170 million ($85 million General Fund) in 2003-04. These savings estimates assume that 33, 900 adults will be terminated from Medi-Cal coverage in 2002-03 and that 193,123 adults are dropped in 2003-04. The Legislature did not adopt the current year reduction.
- Eliminates eight Medi-Cal Optional Benefits effective April 1, 2003 and an additional ten benefits as of October 1, 2003 for savings of $126.5 million ($63.2 million General Fund) in 2002-03 and $723.7 million ($361.8 million General Fund) in 2003-04. The Legislature did not adopt the current year reduction.
- Proposes legislation to establish standards for counties to meet regarding Medi-Cal redeterminations and assumes that because of these new standards, 563,135 Medi-Cal recipients will be terminated from enrollment for savings of $388 million ($194 million General Fund).
- Eliminates the supplemental payment to long-term care facilities that have a collective bargaining agreement to the compensation of care giver staff for savings of $25 million in 2003-04.
- Eliminates the second-year of coverage for people enrolled in the Transitional Medi-Cal Program which would terminate about 1,800 people from coverage and result in savings of $2 million (General Fund).

- Limits who can prescribe the drug Serostim (human growth hormone) to be only those physicians who are certified as being HIV specialists for savings of $7.5 million ($3.8 million General Fund).
- Proposes to implement new utilization and payment controls on various Medi-Cal services for savings of $76 million ($38 million General Fund).
- Eliminates funds of $6.2 million ($3.1 million General Fund) for the BabyCal Program which educates high risk pregnant women about the importance of early and ongoing prenatal care, the consequences of smoking, drinking and drug use during pregnancy, and the availability of programs to help women achieve healthy birth outcomes.
- Eliminates funds of $8.6 million ($3.1 million General Fund) for outreach for the enrollment of children in Medi-Cal and the Healthy Families Program. This adjustment would leave a total of $1.3 million ($650,000 General Fund) available to fund toll-free telephone lines which are used to provide program information to various interested parties, including potential enrollees.

Summary of Increases

- Implements the Childrens Disability Prevention Program (CHDP) Gateway effective July 1, 2003 by providing an increase of $231.5 million ($112.1 million General Fund) to provide for up to two-months of pre-enrollment coverage and to fund those who are Medi-Cal eligible. (It should be noted that the baseline CHDP budget is adjusted downward to reflect this shift to Medi-Cal.)
- Establishes an intergovernmental transfer program whereby public-operated Medi-Cal managed care entities, including County Organized Health Care Systems and the eleven Local Initiatives, would transfer funds to the state to be matched with federal funds to provide safety net providers with resources to strengthen their Medi-Cal provider networks. An additional $263.6 million in federal funds is anticipated to be received through this new mechanism.
- Appropriates $187.9 million ($94 million General Fund) for local assistance and $8.1 million ($4 million General Fund) for county administration to conform with the provisions of *Craig v Bonta'* which requires the state to provide Medi-Cal benefits to persons who are terminated from SSI/SSP effective June 30, 2002. In addition, the DHS must submit an implementation plan to the court pertaining to its planned compliance with Section 14005.37 of Welfare and Institutions Code regarding Medi-Cal eligibility redeterminations.
- Proposes legislation to implement a 6.5 percent provider "quality assurance fee" on Intermediate Care Facilities-for the Developmentally Disabled (ICF-DD) which would be used to obtain federal matching funds to provide a rate adjustment and offset a portion of General Fund expenditures.
- Augments by $31 million (federal funds) to provide a match to public funds (city, county or health district) provided as certification payments to Distinct-Part Nursing Facilities as allowed under existing statute.
- Provides the rate adjustment for hospital outpatient services as agreed to in the Orthopaedic Hospital Settlement for an increase of $207.2 million ($103.6 million General Fund) in the budget year. It should also be noted that the state paid its lump sum payment of $175 million (General Fund) in May 2002 but the $175 million in matching federal funds is still pending approval with the Centers for Medicare and Medicaid (CMS).
- Proposes an increase of $43.3 million ($21.6 million General Fund) to recognize a mid-year (January 2004) implementation of regulations pertaining to the nurse-to-patient ratio for hospitals as required in AB 394 (Kuehl), Statutes of 1999.

- Provides $1.846 billion ($923.2 million Intergovernmental Transfer Funds and $923.2 million federal funds) for payments to Disproportionate Share Hospitals (qualifying public and private hospitals) which reflects an increase of $46.8 million over the current year due to federal law which allows for a Consumer Price Index adjustment. It should also be noted that the state's "administrative fee" of $85 million which is used to offset General Fund expenditures for Medi-Cal is still in effect.
- Appropriates $72.4 million (federal funds) to continue to provide funds to qualifying teaching hospitals for services pertaining to inpatient clinical teaching and medical education activities that are provided to Medi-Cal recipients.
- Increases by $19.3 million ($9.6 million General Fund) funds for Medi-Cal services provided by Federally Qualified Health Centers and Rural Health Clinics to reflect the Medicare Economic Index increase as provided for in federal law.
- Provides a one-time increase of $33.4 million ($16.7 million General Fund) for county welfare department administrative costs.
- Increases by a total of $12.8 million ($6.4 million General Fund) to implement express lane eligibility in Medi-Cal for children as provided for in AB 59, Statutes of 2001 (Cedillo) and SB 493, Statutes of 2001 (Sher) including using information obtained from the National School Lunch Program as well as Food Stamps to make Medi-Cal eligibility determinations. Of this amount, $11.2 million is for health care services with the remaining amount to be appropriated for county administration.
- Augments by $1.3 million ($670,000 General Fund) to hire (1) a contractor to perform medical reviews associated with grievances involving medical issues and expedited state fair hearings, and (2) five Administrative Law Judges plus clerical support at the Department of Social Services to adjudicate an anticipated increase in state fair hearings due to recently enacted federal regulations pertaining to the Balanced Budget Act of 1997.
- Requests an increase of $1.2 million ($585,000 General Fund) for 12 positions for audit staff to recover overpayments relating to Medicare Cross Over billing issues.
- Augments by $896,000 ($448,000 General Fund) to hire nine positions to conduct various oversight activities related to proposed legislative changes which would establish standards for counties to meet regarding Medi-Cal redeterminations and other requirements.
- Increases by $954,000 ($239,000 General Fund) for 15 positions to increase estate recoveries in Medi-Cal. It is anticipated that these positions will generate $13 million in General Fund savings annually.
- Proposes an increase of $508,000 ($198,000 General Fund) to provide a cost of living increase to Los Angeles County for their licensing and certification contract.
- Requests an increase of $2.1 million ($707,000 Health Facility Citation Penalty Fund) for 29 positions to implement a new initiative to promote quality of care and quality of life for nursing home residents by implementing a statewide expansion of the Health Facility Consumer Assistance Center pilot project.
- Requests an increase of $1.6 million ($805,000 General Fund) for 19 positions to address staffing shortages in the Licensing and Certification--Complaint and Fingerprint Investigation Units.
- Augments by $266,000 (total funds) to fund three limited-term positions to implement pending changes to the Disproportionate Share Hospital (DSH) Program as a result of federal requirements,

including those to be imposed by the Office of Inspector General and the Centers for Medicare and Medicaid (CMS).

- Requests an increase of $259,000 (total funds) to fund three positions to provide assistance to schools relating to claiming reimbursements for Medi-Cal administrative activities and related matters.
- Proposes an increase of $930,000 ($232,000 General Fund) for three positions and a contract to complete development of the Enhanced Medi-Cal Budget Estimate Redesign (EMBER) project.
- Provides $211,000 ($53,000 General Fund) for three positions to increase revenues through personal injury recoveries.
- Proposes $230,000 ($115,000 General Fund) for three limited-term positions to continue the Long-Term Care Integration Pilot Program.
- Appropriates $614,000 ($283,000 General Fund) to fund a contract and four limited-term positions to conduct compliance activities, craft regulations and complete an independent assessment regarding a pilot Medi-Cal Waiver program pertaining to continuous skilled nursing as enacted in AB 359 (Aroner), Statutes of 1999.
- Provides an increase of $149,000 ($75,000 General Fund) for two positions to implement the ICF-DD quality assurance fee program.
- Provides $87,000 (total funds) for a position to implement and administer AB 915 (Frommer), Statutes of 2002 to provide supplemental reimbursements to Adult Day Health Care Centers and acute care hospital outpatient departments owned by specified public entities that provide services to Medi-Cal recipients.

Issues for the Medi-Cal Program

1. 15 Percent Transfer of Medi-Cal Benefit Costs to Counties. As part of the "Healthy Families" Realignment proposal, the Administration proposes to shift 15 percent (non-federal share) of Medi-Cal benefit costs to the counties for a savings of $1.620 billion (General Fund). The counties would use revenues obtained from newly proposed tax adjustments to fund this share of cost. As presently proposed the state would retain authority regarding eligibility criteria, benefits offered, reimbursement rate levels and all other policy aspects of Medi-Cal administration.

Medi-Cal is a complex program which is driven by federal law and regulation, case law and legal settlement agreements, state law and regulation, and trends in overall health care such as the absence of employer-sponsored coverage, continually rising health care costs and changes in the methods of medical practice.

Changes in federal Medicare policy can also significantly affect policy choices and expenditures in Medi-Cal. For example, Medi-Cal provides long-term care services and pharmacy benefits whereas Medicare does not. As such, many elderly and disabled individuals who are dually eligible for both programs obtain these benefits through Medi-Cal.

In reviewing this proposal within the context of the principles established in crafting the Realignment of 1991-92, it does not appear to be a constructive fit. An entitlement program with the complexities inherent in the Medi-Cal Program does not afford local government with the opportunity to identify innovative ways to recast the program or even to shift expenditures to more of a community-based, lower cost model of service, as was effectuated under the mental health program Realignment of 1991-92. It is very unlikely that discretion of any modicum would be granted to counties due to the need to maintain certain federal requirements, particularly the need to ensure that Medicaid (Medi-Cal) recipients receive a like level of service no matter where they live in the state (i.e., the statewideness factor).

Question also arises as to the reliability of the revenue stream to sustain a 15 percent share of Medi-Cal benefit costs even in the near term. A recent study by the federal Centers for Medicare and Medicaid Services (CMS), as published in *Health Affairs*, shows that overall health care spending in the United States rose by 8.7 percent from 2001 to 2002. The major contributing factors sited were the rising cost of prescription drugs, hospital care and Medicaid expenditures, particularly for the aged, blind and disabled populations.

2. Realignment of Long-Term Care Nursing Homes to the Counties. As part of the "Long-Term Care" Realignment proposal, the Administration shifts the cost (non-federal share) of skilled nursing facility care to the counties for General Fund savings of $1.4 billion. This includes all skilled nursing facilities (freestanding as well as distinct-part facilities), but does not include Intermediate Care Facilities for the Developmentally Disabled (ICF-DD). Federally mandated benefits such as pharmacy would remain the responsibility of the state for those eligible individuals residing in these facilities.

Generally, nursing home expenditures are primarily driven by the acuity of the patient, direct care staffing needs, the existing labor market, and quality assurance standards. Counties will have little, if any, control over these factors. This component of realignment suffers the same limitations as the proposal to shift 15 percent of the share of Medi-Cal costs to the counties. It does not offer local government the opportunity to identify innovative ways to recast the program or even to shift expenditures to more of a community-based model. It simply has the counties serve in a caretaker capacity with no where to go for program expenditures, except up.

Shifting expenditures for skilled nursing care to the counties runs contrary to recent sweeping changes enacted by the Legislature to make major reforms regarding quality of care issues, direct care nursing staff to patient ratios, and restructuring options for changing the existing Medi-Cal reimbursement rate methodology. Many of these reforms would be left in mid-stream or not completed at all if expenditures are shifted. Counties could be left in the untenable position of trying to fund program expenditures with no ability to modify policy.

In addition, it is unclear how the state's implementation of the United State's Supreme Court's decision in *Olmstead v L.C.* (527 US 581 (1999)) would be affected by this realignment proposal. Under Olmstead the court ruled, among other things, that an individual with a disability has a right to live in a community setting as long as certain conditions are met. This would include some existing residents of nursing homes. The California Health and Human Services Agency is presently crafting an Olmstead Plan, to be provided to the Legislature by April 1, 2003, in which options for meeting Olmstead needs are to be discussed. Therefore, it would be beneficial for the Legislature to review this plan in the context of this realignment proposal.

3. Reinstate Quarterly Status Reports (QSR). The Administration proposes legislation to reinstate the Quarterly Status Report (QSR) effective April 1, 2003 *and* to change statute regarding the determination of Medi-Cal eligibility. Savings of $5 million (General Fund) in 2002-03 and $85 million (General Fund) in 2003-04 are estimated for this action. These savings estimates assume that 33,900 adults will be terminated from Medi-Cal coverage in 2002-03 and that 193,123 adults are dropped in 2003-04. With respect to the mid-year proposal, the Legislature chose to deny it and to focus on the budget year.

Under the QSR process, families participating in Med-Cal only (non-cash aid) are required to complete a detailed form about income and other personal information *every* three months (quarterly), even if there is no change in the families circumstance. Medi-Cal coverage is discontinued if the form is not promptly returned.

The Budget Act of 2000 eliminated the QSR process in favor of a streamlined system whereby families are required to self report within 10-days of any change in circumstance (such as a change in income). Elimination of the QSR reduced administrative processing, maintained the families health care coverage, and simplified Medi-Cal to conform with the Healthy Families Program.

Prior to the elimination of the QSR, many Medi-Cal recipients were terminated from coverage even though they still qualified for services simply because they did not submit a QSR.

The Administration's proposed language would significantly erode existing statute (SB 87, Statutes of 2000) by deeming Medi-Cal recipients who fail to return the QSR as being uncooperative and automatically terminated from benefits. This aspect of the Administration's proposal goes beyond simply reinstating the QSR.

Chapter 1088, Statutes of 2000 (SB 87, Escutia), generally requires that in instances when Medi-Cal eligibility has been terminated on one basis, that a review must be conducted to determine if the individual is eligible for Medi-Cal under other circumstances. All avenues of potential Medi-Cal eligibility are to be reviewed to determine ongoing eligibility. It should be noted that under the Craig v Bonta' lawsuit, the court ruled in favor of the plaintiffs, and has, among other things, required the DHS to submit an implementation plan regarding compliance with Section 14005.37 of Welfare and Institutions Code regarding Medi-Cal eligibility redeterminations.

Reinstatement of the QSR would achieve savings by terminating adults from Medi-Cal who are still likely eligible for Medi-Cal but simply did not return the QSR. The majority of recipients affected by this change would be adults (non-cash aid) enrolled in Medi-Cal managed care plans. However as discussed below, children could also be effected.

There are several concerns with this proposal. First, these Medi-Cal recipients are very low-income wage earners—usually working people who have left CalWORKS and need medical coverage. Their circumstance is not likely going to change significantly and if it does, the recipient is required to report a change within 10 days. In addition, county eligibility offices can and often do monitor changes in Medi-Cal recipients' earnings using the state's automated wage reporting system; therefore, program eligibility can be checked prior to a recipients annual re-determination period.

Second, individuals dropped from Medi-Cal for not returning a QSR will likely seek medical assistance at county indigent health clinics or the emergency room. Safety net hospitals would lose Medi-Cal revenues and likely have to provide coverage to more uninsured.

Third, a key concern with this proposal is its interaction with the Administration's proposal to eliminate the 1931 (b) Medi-Cal eligibility category. If a Medi-Cal recipient (adult, non-cash aid) does not return their QSR and is dropped from Medi-Cal, they likely will *not* be able to re-apply for Medi-Cal due to the elimination of the 1931 (b) category. This issue is discussed further in item two below.

Fourth, elimination of the QSR was intended to reduce over time Medi-Cal Administration costs in order to make the program more efficient and effective. Over the past two fiscal years, county Medi-Cal administration has been reduced by $459 million ($229 million General Fund) to reflect several cost reductions. If the QSR is reinstated, counties will need substantially more funding in order to re-program computer systems, train eligibility workers, and hire additional staff to process the additional paperwork.

Fifth, it would severely erode existing statute (SB 87, Statutes of 2000) by deeming Medi-Cal recipients who fail to return the QSR as being uncooperative and automatically terminated from benefits. As such, these individuals would not have their eligibility status reviewed by the county, nor would they be eligible to receive Transitional Medi-Cal Program coverage even if they would otherwise quality (low-income) for the benefits.

Sixth, 37 other states allow parents participating in Medicaid to annually renew their coverage. In fact, a federal review conducted of California in 2000 expressed grave concerns that a significant number of Medi-Cal recipients were losing coverage because the QSR was not being returned. In response to this criticism, the Davis Administration noted that it was eliminating the QSR requirement to facilitate the retention of families.

Further, there could be *unintended* consequences for children if this proposal is adopted. Many families apply to Medi-Cal as a family unit (parents and children). Subsequently, unless county computer systems are modified to distinguish between family members who are subject to the QSR and family members who are not, children could lose their Medi-Cal coverage inappropriately through a processing error. This is a realistic concern since a federal review conducted in California in 2001 found numerous inconsistencies in the operation of Medi-Cal computer systems across counties. In addition, parents receiving a Medi-Cal termination notice may mistakenly believe that their entire family, including children, are being dropped from enrollment.

Pregnant women, CalWORKS-linked adults, and the aged, blind, and disabled Medi-Cal recipients are not affected by this QSR proposal.

4. Rescission of 1931 (b) Medi-Cal Eligibility. The Administration proposes legislation to rescind the 1931 (b) Medi-Cal eligibility expansion (currently at 100 percent of federal poverty) *and* to reinstate the "100-hour a month work limit". This proposal would limit eligibility to families with incomes up to about 61 percent of poverty (annual income of $11,041 for a family of four). With respect to employment, two-parent families would become *ineligible* for Medi-Cal if the principle wage earner works *more* than 100 hours a month (about 23 hours a week), no matter their low-income level.

The proposal assumes an April 1, 2003 implementation with savings of $12.4 million ($6.2 million General Fund) in 2002-03 and $235.9 million ($118 million General Fund) in 2003-04. These savings estimates assume that 58,578 adults will not be eligible for Medi-Cal coverage in 2002-03 and that 292,890 adults will not be eligible for Medi-Cal coverage in 2003-04. After full implementation, the DOF estimates savings of $985.1 million ($492.6 million General Fund) annually. With respect to the mid-year proposal, the Legislature chose to deny it and to focus on the budget year.

Here are examples of how Medi-Cal eligibility would be changed and made more complex under this proposal:

- Two-parent working families applying for Medi-Cal where the primary wage earner works *more* than 100-hours per month will no longer qualify for Medi-Cal at *any* income level.
- Two-parent working families applying for Medi-Cal where the primary wage earner works *less* than 100-hours per month, will be eligible for the 1931 (b) category if their incomes are under 61 percent of poverty. If their incomes are between 61 percent and 75 percent, they would qualify for Medi-Cal under the Medically Needy category. If there income is above 75 percent of poverty, they would qualify under the Medically Needy category with a share-of-cost.
- Single-parent families and those two-parent families where one is disabled can qualify for the 1931 (b) category if their incomes are below 61 percent of poverty. If their incomes are between 61 percent and 75 percent, they qualify for the Medically Needy category. If there income is above 75 percent of poverty, they would qualify under the Medically Needy category with a share-of-cost.

Families enrolled in Medi-Cal now (recipients) who rely on the applicant income test (families with unearned income, such as disability income) will only quality for the 1931 (b) category if their incomes are under 61 percent of poverty. If their incomes are between 61 percent and 75 percent, they qualify for the Medically Needy category. If there income is above 75 percent of poverty, they would qualify under the Medically Needy category with a share-of-cost.

The Budget Act of 2000 expanded eligibility for Medi-Cal to include families with income up to 100 percent of the federal poverty level. This action was in response to a federal Welfare Reform law change (Section 1931 (b) of the Social Security Act) which enabled states to grant Medicaid eligibility to anyone who would have met the income, resource and deprivation rules (such as children with an absent, decreased, incapacitated, or unemployed parent) of the AFDC Program as it existed on July 16, 1996 (date selected by Congress).

The concept behind this federal policy was to maintain health coverage for families that leave welfare for work, eliminate the incentive to be on welfare in order to receive health care coverage, and to make health care available for working, very low-income families.

The Administration's proposal would deny health care coverage through the Medi-Cal Program to hundreds of thousands of low-income, working families. These are families which are low-income, *not* receiving cash-assistance, and who need health care coverage because their employers do not provide it.

As illustrated by the eligibility examples provided above, this proposed policy change serves as a *disincentive* to work full-time, to maintain family unity, and to move off of CalWORKS. Many families would not qualify for Medi-Cal even though they meet the low-income test because they are working more than 100-hours a month. If they lose health care coverage, they can spiral back into CalWORKS and potential poverty. If desired, the 1931 (b) eligibility category could be reduced *without* reinstating the 100 hour a month work limit.

Children are also affected by this proposal. While the proposed changes are intended to make more parents ineligible for Medi-Cal, the fact is that the entire family loses coverage. The children would have to re-apply for eligibility under the Medi-Cal for Children Program (the 100 percent and 133 percent poverty programs).

This proposal also interacts with the Administration's proposal to reinstate the Quarterly Status Report (QSR). If an existing 1931 (b) category recipient loses Medi-Cal because they do not return their QSR, they are dropped from Medi-Cal and likely would *not* be eligible for Medi-Cal due to the elimination of the 1931 (b) category. This is particularly true for those who are working more than 100 hours a month.

This proposal also affects a families eligibility for Transitional Medi-Cal services. Currently when a family loses 1931 (b) eligibility because their income goes above 100 percent of poverty, they can still potentially obtain up to two years of coverage. The purpose of this federal law for transitional services is to assist families to move into self-sufficiency. However, families in the Medically Needy category are not eligible for Transitional Medi-Cal services. Subsequently families with incomes above 61 percent of poverty who will no longer qualify for 1931 (b) but will qualify for the Medically Needy category will *not* be eligible for Transitional Medical services.

The proposal would also require some families to pay a share of cost each month in order to obtain their Medi-Cal health care coverage. Families currently enrolled in the 1931 (b) program have no share of cost. Under the Administration's proposal families with incomes above 75 percent of poverty would have to pay a share of cost.

The proposal would also add additional complexity to Medi-Cal eligibility determinations. Changes to county computer systems, as well as county eligibility worker training, would be needed to implement this proposal. However the Administration's cost estimate does not take this into consideration.

5. **Eliminates 18 Optional Medi-Cal Benefits.** The Administration proposes legislation effective April 1, 2003 to eliminate eight Medi-Cal Optional Benefit categories as part of the Governor's Mid-Year Reduction process for savings of $126.5 million ($63.3 million General Fund). For the budget year, ten additional benefits are slated for elimination for a total of 18 benefits for savings of $723.7 million ($361.8 million General Fund). These reductions are outlined in the table below.

Optional Benefit Category	2002-03 Mid-Year Proposal (April 1, 2003) (General Fund Savings)	2003-04 Governor's Proposed (General Fund Savings)
Adult Dental Services	$48.5 million	$211.8 million
Medical Supplies (diabetic supplies, IV supplies, wound care, asthma supplies, contraceptive supplies)	12.9 million	54.3 million
Van Transportation		31.5 million
Hospice		13.7 million
Durable Medical Equipment		12.5 million
Optician and Laboratory Services		14.5 million
Optometry		9.2 million
Podiatrist	995,000	4.3 million
Acupuncture	666,000	2.9 million
Prosthetics		2.1 million
Hearing Aids		2.9 million
Psychologist	57,000	229
Chiropractor	100,000	399
Independent Rehabilitation Facility	5,000	23
Occupational Therapy	4,000	15
Physical Therapy		30
Orthotics		640
Speech and Audiology		728
TOTAL GF SAVINGS	**$63.3 million**	**$361.8 million**

Exempt from the proposal are services to children under 21 years of age and residents of long-term care facilities. Federal law precludes the elimination of these services from these individuals.

However, individuals with developmental disabilities would not be exempt from the Administration's proposal. As such, it is likely that Regional Centers would need to purchase these benefits for consumers at 100 percent General Fund expenditure, in lieu of obtaining partial matching federal funds. These costs have not yet been calculated by the Administration.

As noted above, the three categories of adult dental services, medical supplies and van transportation (i.e., non-emergency medical transportation) account for over 80 percent of the proposed savings. Denial of adult dental services, van transportation or certain medical supplies such as asthma supplies will likely result in increased emergency room visits for pain and other medical services and subsequently, result in additional costs.

In addition, there may be increased costs due to the delay in recipients receiving treatment and ultimately requiring more acute care services. For example, van transportation is primarily provided for dialysis patients. As such, the elimination of this benefit means that fragile dialysis patients could have renal failure for lack of transportation access.

Another example pertains to adult dental services. At the direction of the Administration, the Budget Act of 2001 added preventive periodontal services and treatment for pregnant women to the scope of Medi-Cal benefits because it saves money by decreasing neonatal intensive care services. It has been well documented that periodontal disease affects the embryo, often causing pre-term low birth pre-term low birth weight babies. These services could *not* be provided if Adult Dental services are eliminated. For example, denial of some medical supplies or Adult Dental benefits may result in increased emergency room visits for pain and other medical services.

In lieu of eliminating these benefits, one could implement selective cost containment measures. For example, the adult dental benefit could be restructured to capitate the amount of service a recipient obtains.

It should also be noted that the DHS was given authority in the Budget Act of 2002 to contract for certain medical supply items which was estimated to save $9 million (General Fund) in 2002-03. It may be possible to include other medical supply items in this process to reduce expenditures and to even re-calculate how mark-up is determined for some incontinence supplies or related items.

Elimination of selected Medi-Cal Optional Benefits has been proposed on five prior occasions—1990, 1992, 1993,1994 and 1995. Even during these difficult fiscal times, the proposal was denied by the Legislature.

6. Reduces Medi-Cal *and* Non-Medi-Cal Rates by 15 Percent. The Administration proposes legislation to reduce *both* Medi-Cal *and* Non-Medi-Cal provider rates by 10 percent across-the-board effective April 1, 2003 to achieve savings of $479.3 million ($90.4 million General Fund) within the Medi-Cal Program for 2002-03, and by a total of 15 percent for 2003-04 to achieve savings of $1.428 billion ($720.5 million General Fund) within the Medi-Cal Program for 2003-04. The legislation would continue the reduction for three years through 2005-06 (ending as of July 1, 2006). This is the first time that an across-the-board rate reduction has been proposed.

For Medi-Cal providers, the rate reduction **includes** nursing home facilities, Intermediate Care Facilities for Developmentally Disabled (ICF-DD), physician services, pharmacy, dental services, managed care plans, home health, medical transportation, and other medical services. This is the first time that nursing home facilities have been included in a rate reduction.

The rate reduction also includes Non-Medi-Cal programs, including the California Children's Services (CCS) Program, the Family Planning, Access, Care and Treatment Program (Family PACT), the State-Only Family Planning Program, the Genetically Handicapped Persons Program, and the Breast and Cervical Cancer Early Detection Program. The proposed trailer bill legislation would also provide the Director of the DHS authority to identify in regulations *other* programs in which providers shall be paid rates of payment that are identical to the rates paid under Medi-Cal.

The following table summarizes the rate reduction affect to Medi-Cal Programs for 2003-04. (The Non-Medi-Cal programs are discussed under the Public Health and Environmental Health Section, below.)

Medi-Cal Service Category	2003-04 Governor's Proposed (July 1, 2003) (15 percent) (General Fund Savings)
Nursing Home Facilities (including ICF-DD)	$253.2 million
Managed Care Plans	211.5 million
Physicians Services	76.6 million
Other Services (adult day health, hospice, hearing aids, AIDS waiver, and others)	46.3 million
Other Medical Services (podiatry, occupational therapy, acupuncture and others)	30.1 million
Pharmacy Services	23.7 million
ICF-DD Facilities	30.4 million
Dental Services	23.8 million
Home Health	13 million
Early Periodic Screening Diagnostic and Treatment (EPSDT) Services	2 million
Medical Transportation	9.8 million
TOTAL SAVINGS	**$720.5 million**

Exempt from the reduction are: hospital inpatient services, hospital outpatient services, state operated facilities—i.e., Developmental Centers and State Hospitals for the mentally ill—, and Federally Qualified Health Centers/Rural Health Centers. Hospital inpatient services are exempt since the state negotiates inpatient services through the CMAC, and hospital outpatient services are addressed in the Orthopaedic Settlement Agreement. Federal law prohibits an across-the-board rate reduction for FQHC/RHC facilities since a cost-based or prospective payment system is used.

There is some evidence that the rates paid to providers could affect access to health care and the quality of care to patients. A recent national analysis of Medicaid physician rates by The Urban Institute concluded that physician fee levels affect both access and outcomes for Medicaid patients.

In the Budget Act of 2000, most services provided under Medi-Cal received rate adjustments. This action was not an across-the-board rate increase, but instead targeted services for which Medi-Cal physician rates were relatively low in comparison to the Medicare Program. Generally, other than annual adjustments for nursing home rates, there had not been a rate increase for most Medi-Cal services prior to the Budget Act of 2000 since 1986.

A Pricewaterhouse study completed last year found that, even after accounting for the rate increase provided in 2000, Medi-Cal rates continue to lag behind those of other purchasers of health care coverage in California. Another study released last year found that while the 2000 Medi-Cal rate increases were substantial, they collectively only brought the Medi-Cal provider rates from 58 percent to 65 percent of California's average Medicare payment rates.

Inclusion of nursing homes in this reduction may be particularly problematic due to staffing standards and wage requirements, federal regulations, and the industry's dependence on Medi-Cal payments (two-thirds of the over 1,500 homes depend on Medi-Cal reimbursement). In addition, a State Plan Amendment would be required since the federal government requires these rates to be developed on an annual basis through a methodology contained in the state's Medicaid State Plan.

7. Rollback of Aged, Blind and Disabled Medi-Cal Eligibility for Medically Needy. The Budget Act of 2000 extended "no cost" Medi-Cal eligibility to Aged, Blind and Disabled individuals with incomes up to 133 percent of federal poverty. These individuals have low-incomes but either do *not* qualify for, or choose not to participate in, the SSI/SSP Program. Currently, individuals can have income of up to $969 per month and couples can have income of up to $1,332 per month and qualify for "no cost" Medi-Cal.

The Administration proposes to roll this expansion back to cover only those eligibles with income up to the SSI/SSP income level or $708 per month for an individual (96 percent of poverty) and $1,225 per month for a couple (123 percent of poverty). The budget assumes savings of $127.6 million ($63.8 million General Fund) by eliminating 48,302 aged individuals and 20,538 disabled individuals from "no cost" Medi-Cal.

Many of these individuals could still obtain coverage under Medi-Cal but they all would need to pay a share-of-cost each month to receive services. This share-of-cost payment would of course be significant for people on fixed, low-incomes. (The share-of-cost is the amount by which that individual's income or assets exceeds the applicable Medi-Cal limits.)

8. Establish Standards for County Eligibility Determinations of Medi-Cal. The Administration proposes enactment of legislation which would establish standards for counties to meet regarding Medi-Cal eligibility determinations and redeterminations, and assumes that because of these new standards 563,135 Medi-Cal recipients, or almost 9 percent of the eligibles, will be terminated from enrollment for savings of $388 million ($194 million General Fund) in local assistance. The proposal also requests an increase of $896,000 ($448,000 General Fund) for state support to fund 9 positions to oversee the counties activities and to measure their performance.

Draft trailer bill legislation obtained from the Administration would establish county performance standards in several areas, including (1) completing eligibility determinations for several types of applications, including disability determinations, (2) processing newborn referral requests, and (3) conducting Medi-Cal redeterminations. All of these processes would need to be completed within specified timeframes as noted in the legislation or a county may, at the department's discretion, have their Medi-Cal county administration allocation reduced by two percent in the following year.

In order to facilitate the counties meeting these proposed performance standards, the budget provides an increase of $97.2 million ($48.6 million General Fund) over two years, including $54.9 million for 2002-03 and $42.3 million for 2003-04. The Administration contends that this adjustment would provide "full funding" for the counties to meet this potential obligation. However, it should be noted that even with this increased funding level, "full funding" would not be achieved due to reductions of over $450 million (total funds) taken from county Medi-Cal administration in prior years.

Further discussions will need to occur in order to recast the proposal to make it more equitable to fully address Medi-Cal enrollment standards, not just disenrollment, and to appropriately fund county administration..

9. Quality Assurance Fee of 6.5 Percent for Intermediate Care Facilities--Developmentally Disabled (ICF-DD). As part of the Mid-Year Reduction package, the Administration proposes to enact legislation effective April 1, 2003 which requires ICF-DD facilities and state Developmental Centers to pay the state an assessment of 6.5 percent on the total rate per patient day. This assessment would then be used by the state to draw down matching federal funds. A portion of these new federal funds would be used to offset General Fund expenditures and to provide for a rate increase to ICF-DD facilities.

The Legislature postponed enactment pending resolution of the Governor's proposed 15 percent Medi-Cal rate reduction (which includes ICF-DD facilities) and its impact on this proposal, as well as a need to clarify how Developmental Center rates would be affected. Federal law requires ICF-DD facilities and Developmental Centers to be treated the same when it pertains to tax assessments on provider categories.

The Administration assumes total increased revenues of $5 million in the current year and $20 million annually. Of these new revenues, 75 percent would be provided back to these ICF-DD facilities as a provider rate increase. (In essence, this rate increase amounts to a pay back of the assessment fee plus half of the federal fund amount.) The remaining 25 percent of these funds would be used to offset $2.5 million (General Fund) for 2002-03 and $10 million (General Fund) for 2003-04.

It should be noted that the Administrations savings estimate will need to be modified. This is particularly true with respect to the Developmental Centers (DCs) where no fiscal assumptions have yet been developed. According to the Administration, a number of issues need to be resolved before an accurate estimate can be provided for the DCs. For example, the DCs also serve some individuals who are not eligible for Medi-Cal—such as forensic residents. The tax could not be applied to these individuals.

In addition to the need for statutory change, the state would need to submit a Medicaid State Plan amendment to the federal CMS for approval. It should be noted that several other states have implemented similar programs for their ICF-DD populations.

This is an excellent idea for the ICF-DD facilities for it enables the state to obtain additional federal funds and to use a portion of those funds to enhance the quality of care for individuals with developmental disabilities. It should be noted that ICF-DD facilities are almost 100 percent reliant on Medi-Cal funding and could equally benefit from the rate adjustment.

Primary Care, Family Health, Public Health & Environmental Health

Summary of Decreases and Fund Shifts

- Transfers fiscal responsibility of $143.3 million (savings of $66.6 million General Fund, and a fund shift of $18.7 million in federal funds and $58 million in Proposition 99 Funds) in family health and public health programs, along with a new revenue stream, to the counties as part of the "Healthy Communities" Realignment proposal. (This is discussed further, below.)

- Proposes to suspend for one year the $20.2 million (General Fund) appropriation for the County Medical Services Program (CMSP). This $20.2 million has been suspended for the past several years since the CMSP has had reserve funds available. However, it is unknown at this point how the Governor's Realignment proposal may eventually affect this program since he is proposing to transfer all county health services back to the counties.

- Reduces by $10 million (Tobacco Settlement Fund) in 2002-03 and $15 million (General Fund) in 2003-04 the Prostate Cancer Treatment Program due to lack of utilization. The proposed budget year reduction would leave $5 million available for the program. The Legislature did adopt the current year reduction.

- Proposes to eliminate funding for the Cancer Research Program for savings of $12.5 million (General Fund) in 2003-04. The Legislature did not adopt the current year reduction of $6.5 million (General Fund).

- Eliminates the Rural Demonstration Project funds of $3 million (General Fund) which was used for infrastructure development at rural hospitals, clinics and private physicians' offices, including the purchase of mobile health vans and medical/dental equipment, assistance to complete seismic retrofitting for rural hospitals, and the payment of salaries to address provider shortages in rural areas.
- Deletes $1.1 million (General Fund) for domestic violence prevention outreach which was intended to find underserved populations who are potentially in need of services but not using shelter programs. This proposed reduction represents 50 percent of the funding used for these outreach purposes. These underserved populations have historically included women of color and teens. Presently there are 15 contracts funded at $150,000 each. To implement the Administration's proposal, either each contract would need to be reduced by half (or a similar factor), the number of contracts would need to be reduced, or a combination of the two actions could be done. The Administration has not yet proposed an approach.
- Reduces by almost $1.3 million (General Fund) HIV education and prevention, including $1 million in funds historically allocated to the Department of Education, $150,000 used to assist local health departments in federally required evaluation of local intervention activities, $50,000 for a focus group study of risk behaviors for gay men and $34,000 for a contract with a correction facility to provide HIV-related training to clinical staff who work with inmates.
- Reduces by $1.7 million (General Fund) support for the Family Planning Outreach Information and Education Project which is designed to decrease teen and unintended pregnancy through prevention education.
- Eliminates the TeenSMART Outreach Program which provides prevention education information to adolescents for savings of $848,000 (General Fund).
- Eliminates the Teen Pregnancy Prevention Media Campaign which provides prevention education information to adolescents for savings of $7.8 million (General Fund).
- Eliminates the Botulism Immune Globulin (BIG) Program due to fund insolvency for savings of $2 million ($500,000 General Fund and $1.5 million special fund).
- Reduces by $2.8 million (General Fund) state support by reducing costs associated with DHS owned and operated facilities, reducing out-of-state travel, and eliminating the distribution of Calstars Reports.
- Proposes to eliminate the Gynecological Cancer Information Program for savings of $150,000 (General Fund) in 2003-04. The Legislature did not take this reduction as proposed in the Mid-Year Reduction package.
- Deletes funding for Valley Fever Vaccine Research for savings of $700,000 in 2003-04. The Legislature did adopt the Mid-Year Reduction proposal to reduce by $350,000 in the current year.
- Reduces state support by 47 positions and $3.3 million ($1.9 million General Fund, $600,000 federal funds and $800,000 special funds) to reflect the Administration's proposed realignment proposal.
- Eliminates the funds used to produce informational materials for the Newborn Hearing Screening Program for savings of $290,000 (General Fund).

Summary of Increases

- Provides $112.3 million (various special funds) to reflect funding made available from Proposition 50—Water, Security, Clean Drinking Water, Coastal and Beach Protection Act of 2002—to facilitate various statewide water security improvements and to provide safe drinking water grants and loans to local water agencies.

- Augments by $70.2 million (various special funds) (one-time only) to reflect available federal grants and a three-year extension of 10.5 positions in the Small Water System Technical Assistance Program.
- Continues to provide $20 million (federal funds) for the Community Challenge Grants Program which promotes community-based strategies to prevent teenage pregnancy and absentee fatherhood.
- Recommends an increase of $15.5 million (federal funds) in 2002-03 and $84.4 million (federal funds) in 2003-04 for the Women, Infants and Children Supplemental Nutrition (WIC) Program to reflect adjustments in the federal grant. The 2002-03 increase would serve an additional 24,000 participants and the 2003-04 increase would serve an additional 127,000 participants.
- Proposes a *net* increase of $2.3 million (total funds) for the AIDS Drug Assistance Program (ADAP). This net increase consists of the following components:
    - Reduction of $7.2 million (General Fund) to reflect implementation of proposed copayment legislation which would establish a three-tiered income-based system to require ADAP clients to assume a copayment obligation on a per prescription basis. Revenues from the copayment would be used to fund ADAP.
    - Increase of $8.3 million (General Fund) to make adjustments to the ADAP funding base.
    - Increase of $8 million (one-time only) in drug manufacturer rebates, which have recently been collected, to offset General Fund support.
    - Increase of $1.240 million in drug manufacturer rebates which will be on-going.
- Provides $4 million in General Fund support to backfill for $4 million in federal Maternal and Child Health block grant funds to continue funding of domestic violence shelters at their current year level. The $4 million in federal block grant funds was available on a one-time only basis last year.
- Appropriates an additional $1.7 million (federal grant funds) to support cervical cancer screening for women enrolled in both the Breast and Cervical Cancer Control Program and the Breast Cancer Early Detection Program.
- Requests $1.6 million ($864,000 General Fund) for equipment and ongoing information technology costs for the Richmond Laboratory Campus.
- Requests an increase of $405,000 ($234,000 General Fund) to fund five positions to develop, implement and operate a drug rebate program for the California Children's Services Program (CCS) and the Genetically Handicapped Persons Program (GHPP).
- Requests an increase of $316,000 ($205,000 General Fund) to fund three positions and a contract to contain rising costs in the Genetically Handicapped Persons Program (GHPP), including revising regulations regarding GHPP eligibility, checking for third-party payor responsibility, reviewing all requests for blood factor products that are over $25,000, and conducting outreach and education activities on the proper use of the program.
- Increases by $1.3 million (Radiation Control Fund) to implement the provisions of SB 2065 (Kuehl), Statutes of 2002, regarding developing an inventory for low-level radioactive waste generators, including developing and implementing regulations, creating a comprehensive data base system, and preparing summary reports. The funds will be used to hire six positions and to enter into two contracts in order to complete the work.

- Provides an increase of $360,000 (Radiation Control Fund) to meet requirements enacted by AB 2214, Statutes of 2002 regarding low-level radioactive waste disposal, including (1) developing regulations and site suitability standards for a disposal facility, (2) conducting industry outreach activities to encourage interest in submitting applications, and (3) encouraging waste reduction practices by users.
- Increases by $750,000 (Health Statistics Fund) to contract out functions relating to implementation of SB 247, Statutes of 2002, including to develop and implement a single statewide database of imaged birth and death records and to be able to electronically redact signatures from these certificates.
- Establishes a special fund—Lupus Foundation of American—in order to disburse up to $250,000 (Tax Check Off funds) for activities related to the prevention, treatment and research of Lupus.
- Provides an increase of $488,000 (Food Safety Fund) to continue the Food Safety Industry Education and Training Program.
- Provides $125,000 (Reimbursements) to fund two limited-term positions to carry out the School Health Connections Program and policy-related activities.

Issues for Primary Care, Family Health, Public Health and Environmental Health

1. "Healthy Communities" Realignment—Public Health Components. The Administration proposes to realign several programs in the overall public health area for a total fund shift of $143.3 million (savings of $66.6 million General Fund, and a fund shift of $18.7 million in federal funds and $58 million in Proposition 99 Funds). This includes the following programs and their expenditures (total funds):

• Expanded Access to Primary Care(EAPC)	$30.3 million (total funds)
• Indian Health Program	$6.5 million (General Fund)
• Rural Health Clinic & Clinic Grants in Aid	$ 8.8 million (General Fund)
• Seasonal Agricultural & Migrant Workers Program	$ 6.9 million (General Fund)
• Adolescent Family Life Program	$22.2 million (total funds)
• Black Infant Health Program	$ 8 million (total funds)
• Local Health Department –Maternal & Child Health	$ 7.4 million (total funds)
• County Health Services Public Health Subvention	$ 2 million (total funds)
• California Healthcare for Indigent Persons Program	$46 million (Proposition 99)
• Rural Health Services	$ 4.3 million (Proposition 99)
• Managed Care Counties	$926,000 (Proposition 99)

A. Clinic Programs: The community clinic programs, including EAPC, Indian Health, Rural Health Clinic, Seasonal Agricultural & Migrant Workers and Clinic Grants in Aid, are programs that provide funds to non-profit community-based clinics. Generally, each of these programs operates through an application process whereby the DHS, using extensive clinic data, awards funding based upon patient levels of service, uncompensated care, level of historically under served populations and related factors. Three of the programs—American Indian Health, Rural Health Clinics and Seasonal Agricultural & Migrant Workers—are designed to provide assistance for underserved, often medically needy populations.

These programs were never designed to be county-operated for several reasons. First, community-based clinics provide services to very low-income, uninsured individuals, including children, who have medical needs. These services are not county specific nor neatly bound by a geographic county line, for medical services are often regionally-focused and provided based on medical need and demand.

Second, community-clinics are significant providers of health care to the uninsured in most counties, yet often receive a minor share of the county health care budget for their care. Therefore shifting funding may enable some counties to withdraw some portion of their own funds from this responsibility which would result in further erosion of safety net funding.

Third, the programs allocate funds based upon data-driven needs. This requires the clinics who receive funding to analytically present their funding need. If these funds are transferred to the counties, the programs may end up being purely formula-driven and therefore, not responsive to changing demographics and medical service area needs.

B. Maternal & Child Health Programs—AFLP and Black Infant Health. The Adolescent Family Life Program (AFLP) and Black Infant Health Program are two highly successful, highly evaluated programs which have been in existence for numerous years. Both programs utilize non-profit, community-based providers for services. Neither of these programs operate statewide. Both serve selected, targeted geographic areas due to funding limitations and need.

The AFLP provides counseling, education and support services for pregnant and parenting teens, including fathers, and their infants. The Black Infant Health Program conducts targeted, coordinated activities to address underlying causes of infant mortality, low birth weight and other poor reproductive health outcomes of high-risk African American women. The program also supports the development of projects that evaluate and refine effective models of practice in the areas of health behavior modification, prenatal care outreach, prevention, and the role of men in parenting. It is one of the few state programs that directly addresses health disparities within the African American population.

Both of these programs are operating well, have outcome measurements, utilize community-based experts and are not geographic-specific to counties. Further, the federal Title V Maternal and Child Health block grant funds require these programs to provide data and meet certain other federal requirements. These types of programs are more effectively operated with the state serving as the overall fiscal agent, not counties.

C. California Healthcare for Indigent Persons (CHIP) Program and Rural Health Services (RHS). A key purpose of Proposition 99 funds was to fund medical services on behalf of those who are unable to pay. In addition, as directed by the Proposition itself, the funds must be used to supplement and not supplant existing funding. As such, the CHIP and RHS were initiated in 1989 as a legislative result of the passage of Proposition 99. These two programs are intended to assist providers in funding their uncompensated care costs for providing needed health care services to indigent individuals.

Existing state statute distributes Proposition 99 funds to the CHIP and RHS programs based on a formula which allocates moneys for hospitals, physicians and other types of providers for uncompensated indigent health care services. These funds are provider specific, not county specific.

In addition, funding for both programs, particularly CHIP has significantly deteriorated over the past two years. For example, the Budget Act of 2002 appropriated a total of $89.7 million for CHIP whereas $46 million is proposed for 2003-04 for a reduction of over 52 percent.

The funding for these two programs is small, not relevant to county boundaries and would require some modicum of additional monitoring (to determine supplementing versus supplanting) if passed to the counties. It does not make good policy sense.

2. Proposition 99-Funded Programs. Expenditures of $314.6 million (Proposition 99-Funded Accounts) are proposed in 2003-04 for health-related programs, including funds allocated to the DHS, MRMIB, UC research, and OSHPD. Of the total amount, $135.4 million is allocated for programs administered by the DHS.

Overall, total revenues for Proposition 99 continue to rapidly decline. This decline was escalated due to increases in the tobacco product surtax that were adopted through Proposition 10. Proposition 10 holds harmless the Health Education Account and the Research Account of Proposition 99, but does not provide a backfill for the other health care accounts.

The budget year reflects a reduction of $33 million in revenues from the revised current year. This reduction, coupled with higher expenditures for the Access for Infants and Mothers (AIM) Program has resulted in the Administration proposing adjustments to several of the DHS programs.

The DHS funding level reflects the following key proposals:

- Shifts funding for the California Healthcare for Indigent Persons Program ($46 million), Managed Care County Allocation (926,000), Rural Health Services Program ($4.3 million) and Expanded Access to Primary Care (EAPC) Program ($6.8 million) to the counties, along with a total of $58 million (Proposition 99 Funds), as part of the Governor's Realignment proposal entitled "Healthy Communities".
- Eliminates funding for the Comprehensive Perinatal Outreach Program for a reduction of $1.3 million.
- Reduces the Anti-Tobacco Media Campaign by $4.4 million leaving an appropriation of $16.7 million for this purpose.
- Reduces the Local Lead Agencies by $1.5 million leaving an appropriation of $15 million for this purpose.
- Reduces the Breast Cancer Early Detection Program by $1.7 million (Proposition 99 Funds) to reflect a corresponding increase in federal grant funds. As such, the program will remain at its present funding level of $33.3 million.
- Decreases by $2.3 million (Proposition 99 Funds) DHS administration to primarily reflect the shift of certain programs to the counties as contained in the Governor's Realignment proposal—Healthy Communities.

3. AIDS Drug Assistance Program. ADAP is a subsidy program for low and moderate income persons with HIV/AIDS who have no health care coverage for prescription drugs and are not eligible for the Medi-Cal Program.. Under the program, individuals receive drug therapies through participating local pharmacies under subcontract with a statewide contractor. The state provides reimbursement for drug therapies listed on the ADAP formulary (about 146 drugs currently).

The budget proposes a *net* increase of $2.3 million (total funds) for the AIDS Drug Assistance Program (ADAP). This net increase consists of the following proposed components:

- Reduction of $7.2 million (General Fund) to reflect implementation of proposed copay legislation.
- Increase of $8.3 million (General Fund) to make adjustments to the ADAP funding base.
- Increase of $8 million (one-time only) in drug manufacturer rebates, which have recently been collected, to offset General Fund support.
- Increase of $1.240 million in drug manufacturer rebates which will be on-going.

The Administration's copay proposal would establish a three-tiered income-based system to require ADAP clients to assume a copay obligation on a per prescription basis ($30, $45 or $50 per script). ADAP clients with incomes of 200 percent of poverty or less would be exempt from the copay requirements. Based on the information provided by the DHS, about 6,000 ADAP clients, or 24 percent of the total clients, would be affected by the proposed copay.

The table below outlines how the DHS derived its estimate of savings.

Poverty Level	Estimated Clients	Percent Of Clients	Estimated Scripts	Copay Per Script	TOTAL Estimated Copay
100% or less	10,851	43.41%	338,607	$0	$0
101% - 200%	8,151	32.60%	255,284	$0	$0
201% - 300%	3,708	14.83%	126,926	$30	**$3,807,790**
301% - 400%	1,930	7.72%	68,106	$45	**$3,064,768**
400% or more	269	1.08%	8,862	$50	**$443,077**
Unknown	90	0.36%	929	$0	N/A
TOTAL	**25,000**	**100.00%**	**798,713**		**$7,315,636 Maximum Level**

According to the DHS information an average individual between 200 and 300 percent of poverty could be expected to pay about $1,026 annually for their prescriptions ($30 per). Using the sliding fee scale, an average individual between 300 and 400 percent of poverty would pay about $1,588 annually. Given this level of expenditure, the Legislature may want to consider adjustments to the copay proposal, as well as consider additional options, such as reviewing the level of drug manufacturer rebates and whether additional program efficiencies could be obtained.

4. California Children's Services (CCS) Program. CCS depends on a network of specialty physicians, therapists and hospitals to provide medical care to financially eligible, enrolled children. It is the oldest managed care program in the state and the only one focused specifically on children with special health care needs.

Total program expenditures of $141.4 million ($69.5 million General Fund, $61.5 million County Realignment Funds, $4.7 million federal Maternal & Child Health block grant funds, $2.6 million drug rebates, $260,000 patient fees, and $2.8 million other funds) are proposed for 2003-04. Key changes proposed for CCS include the following:

- Decrease of $3 million (General Fund) to reflect a 15 percent provider rate reduction effective July 1, 2003.
- Assumes implementation of drug rebates for blood factor product for savings of $5.2 million ($2.6 million General Fund) effective July 1, 2003.

Through the Budget Act of 2000, the CCS Program was provided a rate increase of 39 percent. Other than a five percent increase granted in 1999, no rate adjustment had been provided since 1982. These rate adjustments resulted from data obtained from the Senate Office of Research and their comprehensive report on the program (published in 2000), plus rate analyses conducted by the DHS, as well as the American Academy of Pediatrics and specialty physician groups.

To reduce these rates would conceivably result in significant problems that were experienced previously. For example, it was documented that (1) many provider groups were having extreme difficulty retaining and hiring for pediatric subspecialty positions, (2) patients were experiencing tremendous waiting times to receive necessary subspecialty services (three months to a year depending on the service), and (3) patients in rural and suburban areas were having to travel long distances to find a doctor authorized by CCS.

In lieu of the proposed rate adjustment, the Legislature may want to consider other cost saving options, such as using utilization controls on certain pharmaceuticals, medical supplies and laboratory services or other related program efficiencies.

5. Genetically Handicapped Persons Program (GHPP). The GHPP provides diagnostic evaluations, treatment services and medical case management services for adults with certain genetic diseases, including cystic fibrosis, hemophilia, sickle cell disease, Huntington's disease, and certain neurological metabolic diseases.

Expenditures for the GHPP have been rapidly increasing over several years as noted in the chart below. In fact, the program increased well over 320 percent from 1996 to 2001 (the last year that actual expenditures are available). Of the $36 million proposed for expenditure in 2003-04, the DHS estimates that about $29.9 million, or 83 percent, is needed for program participants with Hemophilia.

Fiscal Year	Actual General Fund Expenditures
1996-97	$12 million
1997-98	$16.5 million
1998-99	$23.8 million
1999-2000	$34.9 million
2000-01	$31.2 million
2001-02	$38.8 million
2002-03	$32 million (plus $6.6 million in drug rebates) (Estimated)
2003-04	$28.5 million (plus $7.6 million in drug rebates) (Proposed)

Through the Budget Act of 2002, authority was provided to the DHS to negotiate drug rebates for blood factor products. Blood factor products are used extensively in the program, primarily to treat Hemophilia, and are very expensive. These products are clinically complex and are usually made through the purification of plasma proteins or a process of genetic engineering. Prescriptions are usually written as brand name products and cannot be considered interchangeable.

The budget proposes expenditures of $36 million ($28.5 million General Fund) for the GHPP to fund an average total caseload of 1,881 individuals. This reflects an average cost of about $19,138 per program participant. In order to curtail expenditures, the Administration proposes the following adjustments:

- A 15 percent rate reduction, effective July 1, 2003, for savings of $4.2 million (General Fund);
- An increase of $1 million, for a total of $7.4 million, in drug rebates by contracting with all major blood factor manufacturers;
- Establishment of several cost contain measures, including implementation of utilization controls on blood factor products, assuring that other health care coverage is utilized prior to accessing the GHPP and implementing a more efficient system for the assessment and collection of client participation fees for a total savings of $1 million (General Fund).

The Legislature may also want to work with the Hemophilia Centers to seek other cooperative solutions that may be feasible without jeopardizing the health of program participants.

4280 Managed Risk Medical Insurance Board

The Managed Risk Medical Insurance Board (MRMIB) administers programs, which provide health coverage through private health plans to certain groups without health insurance. The MRMIB administers the (1) Healthy Families Program, (2) Major Risk Medical Insurance Program, and (3) Access for Infants and Mothers (AIM).

The budget proposes total expenditures of $972.4 million ($92.3 million General Fund, $511.6 million Federal Trust Fund, $220 million Tobacco Settlement Fund, and $148.5 million in other funds) for all programs administered by the Managed Risk Medical Insurance Board. Of this amount, $7.1 million is for state operations and $965.3 million is for local assistance.

The budget proposes key changes to the Healthy Families Program and the Access for Infants and Mothers Program. These are discussed in more detail below.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
Program Source				
Major Risk Medical Insurance (including state support)	$41,220	$40,082	($1,138)	(2.8)
Access for Infants & Mother (including state support)	$96,461	$117,488	$21,027	21.8
Healthy Families Program (including state support)	$706,673	$814,780	$108,107	15.3
Totals, Program Source	$844,354	$972,350	$127,996	15.2
General Fund	$31,285	$92,310	$61,025	195
Federal Funds	$445,867	$511,585	$65,718	14.7
Tobacco Settlement Fund	$234,752	$220,000	($14,752)	(6.3)
Other Funds	$132,450	$148,455	$16,005	12
Total Funds	$844,354	$972,350	$127,996	15.2

The Healthy Families Program

Summary of Funding.

The Healthy Families Program provides health, dental and vision coverage through managed care arrangements to children in families with incomes up to 250 percent of the federal poverty level. Families pay a monthly premium and copayments as applicable. The benefit package is modeled after that offered to state employees. Eligibility is conducted on an annual basis.

A total of $814.8 million ($85.3 million General Fund, $220 million Tobacco Settlement Fund and $498.5 million Federal Title XXI Funds, and $11 million Reimbursements) is proposed for the Healthy Families Program, including state administration. Of this amount, $809.7 million ($83.6 million General Fund, $220 million Tobacco Settlement Fund, $495.2 million Federal Title XXI Funds and $10.9 million Reimbursements) is for local assistance.

The budget assumes a total enrollment of 768,232 children as of June 30, 2004, for an increase of 99,715 children over the revised current year enrollment level. This enrollment figure is based on the sum of four population segments as follows:

- Children in families up to 200 percent of poverty: 556,755 children
- Children in families between 201 to 250 percent of poverty: 148,789 children
- Children in families who are legal immigrants: 25,573 children
- Child Health Disability Prevention (CHDP) Gateway Access: 37,115 children

The Administration assumes that net enrollment growth in the budget year will begin to slow as total enrollment reaches the end of the universe of potential eligible children and disenrollments and new enrollments equal out.

Summary of Key Adjustments.

- Assumes deferral of the parental coverage expansion until July 1, 2006. The Legislature had proposed to implement the parental coverage expansion as of October 1, 2002 but funding for this was vetoed by the Governor in the Budget Act of 2002.
- Eliminates the Rural Health Demonstration Projects for savings of $4.6 million ($1.7 million General Fund).
- Provides an increase of $108.3 million (increase of $54.3 million General Fund, $61.4 million Federal Title XXI Funds and $3 million in Reimbursements and a decrease of $10.4 million in Tobacco Settlement Funds) for increased enrollment of 99,715 children and related expenses.
- Deletes all funding for Healthy Families Outreach, certified application assistance training and payments. (This is discussed under the Department of Health Services item.)

Issues for the Healthy Families Program

Proposed Elimination of the Rural Health Demonstration Projects. The budget proposes to eliminate the Rural Health Demonstration Project funds used in the Healthy Families Program for savings of $4.6 million ($1.7 million General Fund and $2.9 million federal Title XXI funds).

The Rural Health Demonstration Projects are an integral component of the Healthy Families Program. They have been used to develop and enhance existing health care delivery networks for special populations and to address geographic access barriers. Specifically, the funds have been used to extend community clinic hours, expand telemedicine applications, provide bilingual specialty health care services, provide mobile medical services and dental services, and rate enhancements to increase HFP provider networks in remote areas. According the Rural Demonstration Project 2002 Fact Book, over 238 projects have been funded with very successful and measurable, results.

The Legislature should consider options to continue the funding of these valuable projects.

Access for Infants and Mothers Program

Summary of Funding

The Access for Infants and Mothers (AIM) Program provides health insurance coverage to women during pregnancy and up to 60 days postpartum, and covers their infants up to two years of age. Eligibility is limited to families with incomes from 200 to 300 percent of the poverty level (including the application of Medi-Cal income deductions). Eligible women select coverage from one of the nine participating health plans. Subscribers pay premiums equal to 2 percent of the family's annual income plus $100 for the infant's second year of coverage.

A total of $117.5 million ($97.3 million Perinatal Insurance Fund, $7.1 million General Fund, and $13.1 million in Title XXI federal funds), including state support is proposed for AIM. Of this amount, $116.5 million is for local assistance. A total of 9,531 women and 138,237 infants are expected to enroll in AIM in 2003-04.

Currently, AIM offers coverage through 9 contracted health plans.

Summary of Key Adjustments.

- Increases by $20.9 million over the revised 2002-03 budget to provide coverage to an additional 1,245 women and 23,970 infants.
- Assumes savings of $977,000 (Proposition 99 Funds) by consolidating AIM infants into the Healthy Families Program.

Issues for the Access for Infants and Mothers Program

1. Consolidation of AIM. Over the past several years, costs and enrollment for AIM have exceeded budgeted levels. As a result, the MRMIB has submitted several requests to the Legislature for additional funds in order to avoid having to cap enrollment levels. At the same time, the primary funding source for AIM (Proposition 99 Funds) has continued to decline.

The MRMIB also notes that a separate program, such as AIM, with specialized services for cost-intensive enrollees makes it difficult to negotiate rates with health plans because the risk cannot be spread across a large purchasing pool (i.e., these are pregnant women only, no other enrollees). This in turn, limits the number of health plans willing to participate in the program.

As such, the Administration has proposed to consolidate AIM and enroll eligible infants into the Healthy Families Program at birth while continuing to provide women with prenatal and postpartum care through AIM. The MRMIB states that by merging AIM in this manner, the state should be able to obtain lower health plan rates for infants via the Healthy Families Program (larger risk pool), as well as achieve other economies of scale through consolidating certain program administration.

The Administration assumes savings of $977,000 (Proposition 99 Funds) in 2003-04 for this consolidation (January 1, 2004 effective date), with net annual savings of $10.2 million (total funds).

Specifically, infants in families between 200 and 250 percent of poverty would be funded through the Healthy Families Program using General Fund and federal Title XXI funds (35 percent/65 percent). AIM infants in families between 250 and 300 percent of poverty (above the Healthy Families Program income threshold) would be funded with 100 percent state funds (General Fund and Proposition 99 Funds).

It should be noted that this proposal will potentially affect expenditures in the California Children's Services (CCS) Program. This is because children enrolled in the Healthy Families Program are also eligible for CCS services if they meet the medical eligibility criteria. Therefore, MRMIB can potentially obtain better AIM rates because the risk of having high cost, medically involved infants is shifted to the CCS Program where the state and county pick-up the costs. The potential cost shift to the CCS Program is unknown at this time.

2. AIM Outreach Funding. The budget proposes to appropriate $2 million (Proposition 99 Funds) to conduct a wide variety of outreach activities, including (1) presentations and trainings for insurance agents, healthcare plans, schools and government agencies, (2) developing and distributing advertisements for television and print media, and (3) organizing media events.

This funding proposal is inconsistent with the Administration's approach in other health care programs where outreach, education, and information assistance has been stripped from the budget. For example, all of the outreach funding for Medi-Cal for children and Healthy Families has been deleted, funding for education activities in TeenSMART has been deleted, information regarding the Newborn Hearing Screening Program has been deleted and there are many other examples.

AIM has been over its estimated caseload every budget year since 1998. As such, outreach funding could be deleted during a time of fiscal crisis and used to support other health care service programs funded by Proposition 99 funds.

4300 Department of Developmental Services

The Department of Developmental Services (DDS) administers services in the community through 21 Regional Centers and in state Developmental Centers for persons with developmental disabilities according to the provisions of the Lanterman Developmental Disabilities Services Act. To be eligible for services, the disability must begin before the consumer's 18th birthday, be expected to continue indefinitely, present a significant disability and be attributable to certain medical conditions, such as mental retardation, autism, and cerebral palsy.

The purpose of the department is to (1) ensure that individuals receive needed services; (2) ensure the optimal health, safety, and well-being of individuals served in the developmental disabilities system; (3) ensure that services provided by vendors, Regional Centers and the Developmental Centers are of high quality; (4) ensure the availability of a comprehensive array of appropriate services and supports to meet the needs of consumers and their families; (5) reduce the incidence and severity of developmental disabilities through the provision of appropriate prevention and early intervention service; and (6) ensure the services and supports are cost-effective for the state.

Summary of Funding

The budget proposes total expenditures of $3.227 billion ($1.957 billion General Fund), for a *net* increase of $281.6 million ($130.9 million General Fund) over the revised 2002-03 budget, to provide services and supports to individuals with developmental disabilities living in the community or in state Developmental Centers.

Of the total amount, $2.537 billion is for services provided in the community, $655.1 million is for support of the state Developmental Centers, $35.4 million is for state headquarters administration and $4,951 is for state-mandated local programs.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
Program Source				
Community Services Program	$2,259,667	$2,536,710	$277,043	12.3
Developmental Centers	$655,560	$655,132	-428	--
State Administration	$30,438	$35,389	4,951	16.3
State Mandated Local Program	$4	$4		
Total, Program Source	$2,945,669	$3,227,235	$281,566	9.6
Funding Source				
General Fund	1,826,777	1,957,632	130,855	7.2
Federal Funds	49,589	51,695	2,106	4.2
Program Development Fund	2,059	1,931	-128	-6.2
Lottery Education Fund	2,057	2,057		
Reimbursements: including Medicaid Waiver, Title XX federal block grant and Targeted Case Management	1,065,187	1,213,920	148,733	14
Total	$2,945,669	$3,227,235	$281,566	9.6

Community-Based Services Highlights

Summary of Funding for Community-Based Services Provided through Regional Centers.

The DDS contracts with 21 not-for-profit Regional Centers (RCs) which have designated catchment areas for service coverage throughout the state. The RCs are responsible for providing a series of services, including case management, intake and assessment, community resource development, and individual program planning assistance for consumers. RCs also purchase services for consumers and their families from approved vendors and coordinate consumer services with other public entities.

The budget proposes expenditures of $2.537 billion ($1.574 billion General Fund) for community-based services, provided via the RCs, to serve a total of 193,100 consumers living in the community. This reflects an increase of $277 million ($126.7 million General Fund), or 12.3 percent, over the revised 2002-2003 budget.

The funding level includes $432.2 million for RC operations and over $2.1 billion for local assistance, including funds for the purchase of services for consumers, program development assistance, the Early Start Program, and habilitation services. About 193,100 consumers are anticipated to be service through the Regional Centers. This reflects an increase of 9,560 consumers, or 5.2 percent over the current-year.

It should be noted that in reviewing the past five years of actual fiscal data (1996 to 2001), the budget for total program expenditures (including Regional Center operations and purchase of services) has increased by over 107 percent from $996.9 million (total funds) in 1996 to almost $2.1 billion (total funds) in 2001.

Summary of Key Reductions

- Reduces by $100 million (General Fund) the Purchase of Services category by assuming the adoption of legislation as of April 1, 2003 to implement “statewide purchase of services standards”.
- Decreases by $101 million in General Fund support to reflect a commensurate backfill in reimbursements obtained from the Department of Health Services for increased receipts in federal funding obtained from expanded activities primarily associated with the Home and Community Based Waiver.
- Reduces by $65.7 million in General Fund support due to a corresponding increase in federal Title XX Social Services Block Grant reimbursements obtained from the Department of Social Services.
- Assumes the receipt of $31.5 million in revenues obtained through the implementation of a parental copayment for families with children ages 3 to 17 years living at home that access Regional Center services and who are *not* eligible for Med-Cal.
- Assumes a reduction of $2.1 million (General Fund) through implementing a change in eligibility to conform the definition of substantial disability to the federal standard. The federal standard requires the clinical determination of significant limitations in three or more of the seven major life activities.
- Continues the suspension of using Purchase of Service funds for the start-up of any new non-Community Placement Plan programs as enacted in AB 442, Statutes of 2002, the trailer legislation for the Budget Act of 2002.
- Continues the deferral of the intake and assessment process from 60 days to 120 days as enacted in AB 442, Statutes of 2002, the trailer legislation for the Budget Act of 2002.

Summary of Key Augmentations

- Increases by $114.8 million (General Fund) to recognize the transfer of the Habilitation Program from the Department of Rehabilitation to the DDS.
- Augments by $204.7 million (General Fund) to fund additional costs at the Regional Centers attributable to higher utilization of Purchase of Services by consumers and to reflect projected caseload growth of 10,870 consumers.
- Provides $790,000 to continue to pass through the federal portion of the SSI/SSP increase to Community Care Facilities (CCFs), effective January 1, 2004. About 20,800 people with developmental disabilities reside in 4,500 CCFs licensed by the Department of Social Services. As such, over 50 percent of consumers living in out-of-home placement settings reside in CCFs. Since the Budget Act of 1998, annual SSI/SSP increases have been passed through to CCF providers.
- Augments by $1.8 million (General Fund) DDS headquarters support to fund 24 new positions to implement a parental copayment assessment program.
- Provides $159,000 ($139,000 General Fund) for DDS to seek a Home and Community-Based Services Independence Plus Waiver to continue and expand the Self-Determination Projects.

Issues for Community-Based Services

1. **Current-Year Deficiency Concerns.** The revised 2002-03 budget as proposed in January reflects a deficiency of $40 million ($13.7 million General Fund, and $26.3 million Reimbursements) for the Regional Centers. This *initial* deficiency reflects preliminary data only. Consequently, this deficiency request will need to be updated in the May Revision when additional department data is available. Of this initial estimate, almost $30 million is attributable to increased utilization of services by

consumers. As such, it is likely that the base-line budget for 2003-04 will also need to be increased at the May Revision, absent any other corrective adjustments.

2. Implement Statewide Standards for the Purchase of Services. A decrease of $100 million (General Fund) is assumed through enactment of statewide purchase of services standards. The Administration is seeking approval of legislation in the Special Session in order to achieve full-year savings in the budget year. Though the proposed language is referred to as establishing "statewide standards" for the purchase of services, the language does not function in this manner. It simply provides the DDS with broad reduction authority.

For example, the language does *not* articulate any principles, process, or framework that would address what the standards would be nor how they would be applied on a statewide basis. Instead, the proposed language grants very broad authority to the DDS to: (1) prohibit any consumer services or supports by type (such as Respite), (2) limit the type, duration, scope, location, amount, or intensity of *any* services and supports provided to consumers through the purchase of services by the Regional Centers, and (3) impose payment reductions and closure days on categories of vendors in order to insure that Regional Centers stay within their budgeted appropriation level.

In addition, the language explicitly states that consumers may *not* appeal a change in their services or supports if (1) the type of service or support has been prohibited through the actions of the DDS, or (2) the individual service or support has been reduced at the direction of the DDS in order to ensure that Regional Centers stay within their budgeted appropriation level.

The language also expresses that it is not the Legislature's intent to endanger a consumer's health or safety, nor place a consumer in a more restrictive setting in violation of the Olmstead Decision (1999, 527 U.S. 581). However, it is unclear how the DDS and RCs are to monitor this in order to assure something inappropriate does not occur.

The Administration has not provided any fiscal detail as to how the savings are to be achieved, because none exists. The savings figure simply assumes that the $52 million (General Fund) unallocated reduction taken in the Budget Act of 2002 is subsumed in the proposed statewide standards and that additional funds are obtained to achieve the round savings figure of $100 million (General Fund).

In reviewing the 2000-01 actual expenditures for the Regional Center purchase of services line item, it is evident that $100 million in General Fund savings would be near impossible to achieve unless certain services are eliminated and provider rates in other service categories are reduced. This is because certain service categories—such as residential services and supported living—would be extremely difficult to reduce since these are fundamental services whose costs reflect staffing standard requirements, housing needs and basic amenities. These two service categories constitute 30 percent of expenditures for the purchase of services.

Other service categories such as Behavioral Services, Medical Care and Services, Medical Equipment and Supplies, and Therapy Services may be difficult to reduce for a reduction might endanger the health, safety and life of an individual. In addition, expenditures for these services are relatively small.

The other significant service categories include Adult Day Programs (22 percent of expenditures), Respite Services (7 percent), Transportation Services (7 percent), and Infant Development Services (4 percent). After the Residential Services category, these services reflect the highest expenditures. Finally, there are some very small categories, such as Social Recreational Activities and Camp Services; however, these expenditures are relatively minor so their elimination would not amount to much savings.

Given the nature of the above outlined expenditures, it is likely that a significant level of the Administration's proposed reduction would need to come from Adult Day Programs, Respite, Transportation and some more minor cost areas such as Social Recreational Activities.

If purchase of service reductions are to be enacted, it is recommended to completely re-craft the language to establish a more comprehensive framework for service determinations, including stakeholder community participation, and to establish a more reasonable savings level that recognizes the need to not reduce certain core services.

3. Enhanced Federal Funds and the Home and Community-Based Waiver. Over the course of the past two years, the state has been aggressively pursing additional federal funds, most notably under the Home and Community-Based Waiver. Under this Waiver, California can offer "nonmedical" services to individuals with developmental disabilities living in community settings who would otherwise require the level of care provided in a hospital, nursing facility, or intermediate care facility, or related conditions. Use of these "waiver services", such as assistance with daily living skills and day program habilitation, enable people to live in less restrictive environments such as in their home.

The Waiver has allowed the state to conserve General Fund dollars by shifting Medicaid (Medi-Cal) eligible beneficiaries to Waiver services while granting flexibility and assisting the state in complying with the Coffelt Settlement and the Olmstead Decision.

The budget proposes to capture an increase of almost $101.5 million in additional federal funds obtained through a series of program changes. Of this amount, (1) $92.1 million will be used as a General Fund backfill in the Purchase of Services line-item, (2) $6.5 million is proposed for Regional Center Operations support, (3) $1.6 million is proposed for transportation providers to complete certain billing requirements, and (4) $1.3 million is proposed for certain Headquarters support functions.

The DDS proposes to obtain these increased federal revenues by conducting the following activities:

- Increasing the cap on the number of consumers the state can enroll in the Home and Community-Based Waiver from 46,447 to 55,000 consumers.
- Increasing the percentage of contracted services eligible for federal reimbursement under the Home and Community-Based Waiver.
- Adding and redefining selected services offered under the Home and Community-Based Waiver.
- Implementing a system to capture funding for the administrative costs incurred by the Regional Centers that pertain to Waiver functions.
- Recalculating and revising the method used for making rate determinations under the state's Targeted Case Management Program.
- Obtaining federal matching funds for some transportation services.

The above proposed activities are reasonable proposals in order to obtain enhanced federal funds. Most of these options will require federal approval through Medicaid (Medi-Cal) State Plan Amendments and in some cases, Waiver amendments. Further, some system modifications in the areas of vendor billing, Regional Center billing, and the like will need to be thought through and completed.

In addition to the above items, there is further potential to obtain more federal funding. For example, there is potential to restructure or add more services to the Waiver, particularly in the areas of respite care and education services. In addition, some administrative functions may qualify for a 75 percent federal match instead of the 50 percent match that is assumed in the proposal. Further research on this issue is forthcoming.

Also it should be noted that the state is not yet claiming reimbursement under the Home and Community-Based Waiver for the South Central Los Angeles Regional Center; however, discussions are ongoing to bring them under the Waiver. This alone could increase federal funding by an additional $5 million.

4. Proposed Implementation of a Parental Copayment Assessment Program for Services. The budget assumes increased revenues of $31.5 million through the implementation of a Parental Copayment Assessment Program to be enacted through trailer bill legislation. This program would require parental financial participation for children who live at home and receive services from Regional Centers. The key components of this copayment program are as follows:

- Copayments would be assessed on families with children ages 3 to 17 years living at home that access Regional Center services and who are *not* eligible for Med-Cal.
- Copayments would be assessed on families at or above 200 percent of the federal poverty level, based on annual adjusted *gross* income as provided by the Franchise Tax Board.
- Families would pay up to a maximum of 10 percent of their gross income for the cost of services provided through the Regional Center for the child. For example, a family making $50,000 annually would pay up to $5,000 (10 percent), not to exceed the costs of services purchased for the child. The entire copayment amount would have to be paid within one year of the initial assessment.

It should be noted that the Administration's proposal does not utilize a sliding-fee methodology. All applicable families with incomes 200 percent of poverty or above would be required to pay up to a maximum of 10 percent of their families' annual gross income.

The budget also requests an increase of about $1.8 million (General Fund) and 24 new positions for DDS headquarters to develop and implement the program.

5. Proposed Revision of Eligibility Definition. The budget proposes savings of $2.1 million (General Fund) through legislation which would apply the federal standard for "substantial disability" to existing state eligibility criteria. The federal standard requires the clinical determination of significant limitations in three or more of the seven major life activities. These major life activities would address clinical capacity in the areas of communication, learning, mobility, self-care, self-direction, economic self sufficiency, and independent living. The Administration states that the new standard would be applied prospectively so that those currently receiving services will not be affected.

Based on existing consumer characteristics, the DDS estimates that about 400 persons per year would *not* be eligible for Regional Center services. These estimated 400 persons would generally be school age children or young adults with mild mental retardation, or another disability, without severe medical or behavioral needs. The DDS further states that the clinical judgement of the Regional Centers in applying the proposed new standard for substantial disability would be the key determining factor.

State Developmental Center Highlights

Summary of Funding for the State Developmental Centers

The DDS operates five Developmental Centers (DCs)—Agnews, Fairview, Lanterman, Porterville and Sonoma. Porterville is unique in that it provides forensic services in a secure setting. In addition the department leases Sierra Vista, a 54-bed facility located in Yuba City, and Canyon Springs, a 63-bed facility located in Cathedral City. Both facilities provide services to individuals with severe behavioral challenges.

The budget proposes expenditures of $690.5 million ($368.5 million General Fund), including state support of $13.8 million, to serve 3,596 residents who reside in the state Developmental Center system. This reflects a caseload decrease of 71 residents and a marginal net decrease in funds of $428,000 as compared to the revised 2002-03 budget.

According to DDS data, the average cost per person residing at a DC is about $179,000 annually. Due to differences between the DCs, including resident medical and behavioral needs, overall resident population size, staffing requirements, fixed facility costs and related factors, the annual cost per resident varies considerably and is as follows:

- Canyon Springs $255,574 annual cost per resident
- Sierra Vista $213,923
- Agnews $208,935
- Lanterman $158,336
- Sonoma $157,530
- Fairview $147,690

Summary of Key Adjustments

- Reduces by $6.3 million ($3.7 million General Fund) and 91 Level-of-Care staff based on the revised DC population level.
- Reduces by $386,000 ($187,00 General Fund) and 8 Non-Level of Care staff based on the revised DC population level.
- Augments by $44.5 million (Public Building Construction Fund) for preliminary plans, working drawings and construction of a 96-bed expansion in the secured treatment area at Porterville Developmental Center.
- Augments by $5.7 million (Public Building Construction Fund) for preliminary plans, working drawings and construction of a recreation complex in the secured treatment area at Porterville Developmental Center.
- Provides an additional $406,000 ($237,000 General Fund) and five new state positions to complete investigations of consumer safety at the DCs in a timely manner.
- Increase of $20.2 million ($11.8 million General Fund) for employee compensation.
- Increase of $12.2 million ($7.1 million General Fund) for employer retirement contributions.
- Increase of $1.1 million for State Compensation Insurance Fund costs.

Issues for the Developmental Centers

Bay Area Project and Future Closure of Agnews. The Administration proposes to develop a strategic plan to among other things, develop community capacity and resources to facilitate the eventual transfer of individuals from Agnews DC to either an appropriate community setting or to another DC. The actual closure of Agnews would not occur until the end of June 2005, at the earliest.

This proposal would establish a project team to begin assessing available resources and identifying additional resources necessary to transition consumers. No additional funding is being requested for this purpose. All budget year expenditures would be absorbed within the Sacramento headquarters.

4440 Department of Mental Health

The Department of Mental Health (DMH) administers the Bronzan-McCorquodale and Lanterman-Petris-Short Acts providing delivery of mental health treatment services through **(1)** a state-county partnership and **(2)** the involuntary treatment of the mentally-disabled. The DMH is responsible for the operation of five state hospitals and the acute psychiatric units at the California Medical Facility in Vacaville and the Salinas Valley State Prison.

The budget proposes expenditures of $2.319 billion ($786.8 million General Fund) for mental health services. This reflects a decrease of $60.2 million, or 7 percent, over the revised 2002-03 budget. Of the total amount, $1.588 billion is for local assistance, $693.1 million is for the state hospitals, $19.3 million is for department support, and $6 million (General Fund) is for state mandated local programs.

In addition, it is estimated that almost $1.174 billion will be available in the Mental Health Subaccount (County Realignment Funds) which does not directly flow through the state budget. This amount does not include the estimated $14 million which may be made available from the Vehicle License Collection Account.

Further, an appropriation of $21.5 million ($736,000 General Fund and $20.8 million Public Building Construction Fund) is provided for capital outlay purposes.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
Program Source				
Community Services Program	$1,577,648	$1,625,631	$47,983	3
Long Term Care Services	659,608	693,121	$33,513	5
State Mandated Local Programs	6	6		
Total, Program Source	$2,237,262	$2,318,758	$81,496	3.6
Funding Source				
General Fund	$846,960	$786,789	($60,171)	
Federal Funds	60,834	60,839	5	
Reimbursements	1,325,684	1,467,919	142,235	
Other Funds	3,784	3,211	(573)	
Total Department	$2,237,262	$2,318,758	$81,496	

Community-Based Mental Health Services Highlights

Summary of Funding for Community-Based Mental Health Services. The budget proposes expenditures of almost $1.588 billion ($224.3 million General Fund) for community-based local assistance, including the Conditional Release Program and state mandated local claims. This reflects an increase of $131.9 million (total funds) and a reduction of $95.9 million (General Fund) as compared to the revised 2002-03 budget.

In addition, it is estimated that $1.095 billion will be available in the Mental Health Subaccount (County Realignment Funds) which does not directly flow through the state budget. This estimate is based on the following revenue estimates:

• Sales Tax	$820,568,000
• Vehicle License Fee Account	$265,784,000
• Vehicle License Fee Growth Account	$8,718,000
• Sales Tax Growth Account	$-0-

Realignment revenues deposited in the Mental Health Subaccount, as established by formula outlined in statute, are distributed to counties until each county receives funds equal to the previous year's total. Any realignment revenues above that amount are placed into a growth account. Generally, first claim on the distribution of growth funds are caseload-driven social services programs. Any remaining growth (i.e., "general" growth) in revenues is then distributed according to a formula in statute.

As discussed in a recently released report on mental health realignment (AB 328 Realignment Data, Department of Mental Health, February 5, 2003), due to continued caseload growth in Child Welfare services and Foster Care, as well as cost increases in the In Home Supportive Services (IHSS) Program, growth distributions to the Mental Health Subaccount and Health Subaccount have been substantially reduced.

Summary of Key Reductions and Fund Shifts

- Reduces by $46 million ($23 million General Fund) the state allocation provided to County Mental Health Plans for implementing Mental Health Manage Care.
- Shifts $74.9 million in expenditures for the Integrated Services to the Homeless Program and the Children's System of Care Program to the counties to reflect the Governor's "Mental Health" Realignment proposal. If a dedicated, reliable revenue source is provided for this purpose, this transfer of responsibility makes programmatic sense. Counties have done an excellent job at operating both programs effectively and efficiently, as noted through several independent evaluations of both programs.
- Decreases by $15 million (General Fund--Proposition 98) to reflect the elimination of the Early Mental Health Initiative Program.

Summary of Key Augmentations

- Increases by $230.4 million (Reimbursements from the DHS for Medi-Cal) to reflect adjustments for the continued expansion of the Early Periodic Screening Diagnosis and Treatment (EPSDT) and Therapeutic Behavioral Services (TBS). The Department of Finance states that the full effect of cost control measures implemented by the Legislature through AB 442, Statutes of 2002, trailer bill to the Budget Act of 2002, will not be realized until 2004-05. However, the proposed $230.4 million increase does assume a smaller growth rate.
- Continues to provide $1.2 million (General Fund) for supplemental funding for Community Treatment Facilities (CTFs). This level of funding provides a supplement of $2,500 per child per month. According to the DMH, five CTFs are currently in operation with two additional programs under development.
- Provides $6.2 million ($1.7 million General Fund) and one new state position (limited-term) to implement federally required External Quality Reviews of County Mental Health Plans to ensure that the department's Mental Health Managed Care Waiver is brought into compliance with new federal regulations governing the operation of Medicaid managed care programs.

- Increases by $4 million (federal reimbursements) for the Healthy Families Program to reflect a caseload adjustment.
- Augments by $345,000 (General Fund) and five new state positions to comply with AB 1454, (Thomson), Statutes of 2002, which requires the DMH to provide fingerprint images to the DOJ for a criminal background check on administrative and direct care staff of Psychiatric Health Facilities and Mental Health Rehabilitation Centers prior to their licensure or license renewal.

Issues for Community-Based Mental Health

Mental Health Managed Care. The state's Mental Health Managed Care Program operates under a federal waiver whereby County Mental Health Plans are responsible for the provision of public mental health services, including those for Medi-Cal recipients.

Under this model the County Mental Health Plans, through a system of contracts with the state, are at risk for the state matching funds for services provided to Medi-Cal recipients. An annual state General Fund allocation is provided to County Mental Health Plans for this purpose, though counties also use a substantial amount of county realignment funds—Mental Health Subaccount-- to draw down federal matching dollars. Based on the most recent estimate of expenditure data for 2001-02, of California's state share of cost for Mental Health Managed Care, County Mental Health Plans provided a 46 percent match while the state provided a 54 percent match.

The state General Fund allocation is usually updated each fiscal year to reflect adjustments as contained in Chapter 633, Statutes of 1994 (AB 757, Polanco). These adjustments have typically included, changes in the number of eligibles served, factors pertaining to changes to the consumer price index for medical services, and other relevant cost items.

The Administration proposes to reduce by $46 million ($23 million General Fund) the amount the state provides to the counties for Mental Health Managed Care. Both the short-term and long-term effect of this action is to cost shift mental health services more to the counties. This proposal continues the Administration's direction to substantially reduce General Fund support for mental health services, other than the State Hospitals. About $164 million (General Fund), or 34 percent of the General Fund, was reduced from community-based mental health services in the Budget Act of 2002.

The proposed reduction will likely result in County Mental Health Plans serving fewer individuals and having difficulty in meeting statutory and contractual responsibilities related to the provision of Mental Health Managed Care services.

In fact, the state and counties are having difficulty in presently meeting needs and requirements. As noted in the Independent Assessment of California's Mental Health Managed Care Program, prepared by the Department of Finance (May 2002 and released November 2002), the state needs to address numerous issues regarding client access to services, quality of services, performance outcome measures, and program management functions.

Another report—Psychiatric Hospital Beds in California: Reduced Numbers Create Potential Crisis (prepared by the California Institute for Mental Health, August 2001)--, discusses the significant shortfall of inpatient psychiatric beds in California, as well as the lack of adequate capacity of the existing mental health system to provide alternative care for those clients in need of urgent care.

With respect to alternatives, there may be opportunities to obtain additional federal funds. First, the DMH could be directed to analyze the feasibility of expanding California's Home and Community-Based Waiver to include mental health services. Chapter 887, Statutes of 2002 (SB 1911, Ortiz), directed the DMH to conduct this analysis contingent on receipt of funding for this purpose. However given this fiscal environment, the DMH should be proceeding with this anyway.

Second, the DMH should also investigate whether California can obtain additional federal funds through the Medicaid Rehabilitation Option. Under this federal option, implemented in 1993, California has been able to draw down hundreds of millions in increased federal reimbursement. It is likely that some existing services could be included in this option in order to draw down additional federal funds.

2. Second Level Treatment Authorization Request Appeals. The Administration proposes to eliminate the second level Treatment Authorization Request (TAR) appeals process for savings of $126,000 (General Fund) in 2003-04. The savings comes from the elimination of two state positions. No trailer bill language has been proposed for this action.

Existing state regulation (Title 9, Section 1850.305) provides that a psychiatric hospital may file a second level TAR appeal when payment issues have not been resolved at the first level appeal (between the hospital and a County Mental Health Plan).

Typically, a second level TAR appeal involves disagreements between a hospital (non-county owned or operated facility) and a County Mental Health Plan regarding the number of bed days the county will reimburse.

For example, a hospital claims 15 days of inpatient services for a particular client and the County Mental Health Plan will only approve 10 days. As such, the hospital appeals the additional 5 days to the state. The state can either agree or disagree with the hospital. According to DMH statistics, the DMH agrees with County Mental Health Plans about 88 percent of the time.

It should also be noted, that the DMH's role in the second level TAR appeals process has inserted the department into judicial disputes between hospitals and County Mental Health Plans. According to the DMH, 29 lawsuits have been filed in this area.

The proposal continues the Administration's direction to further reduce the state's role in providing oversight of mental health services. In this case, oversight of inpatient hospital psychiatric services.

County Mental Health Plans are concerned about this proposal because hospitals who want to appeal a County Mental Health Plan denial of payment can go directly to the courts, and the DMH would no longer be involved in the case.

This is really a policy area that needs to be clarified more, rather than a fiscal, budgetary issue. Broader policy issues exist that affect the provision of inpatient psychiatric services and the payment for them.

With respect to the fiscal issue, the hospitals and/or County Mental Health Plans could reimburse the state for the workload associated with the two positions currently used by the DMH.

Highlights for the State Hospitals and State Support

The budget proposes expenditures of $660.4 million ($513.4 million General Fund) for the State Hospitals for a *net* increase of almost $15.4 million (increase of $18 million General Fund and decrease of $2.6 million in County Realignment Funds) over the revised 2002-03 budget.

Further, an appropriation of $21.5 million ($736,000 General Fund and $20.8 million Public Building Construction Fund) is provided for capital outlay purposes.

Major budget proposals are as follows:

- Proposes an augmentation of over $3.5 million (General Fund) and 47 positions to continue activation activities associated with the secure treatment facility at Coalinga.

- Increases by $3.7 million (General Fund) to reflect half-year funding for level-of-care staff and operating expenses to fund an increase of 94 penal code beds.
- Increases by $2.3 million (General Fund) and 31 positions to fund an increase of 27 beds for Mentally Disordered Offenders.
- Provides $11.4 million ($9.5 million General Fund and $1.9 million in Realignment Funds) for operating expense increases in the areas of outside medical care, food and pharmaceuticals.
- Requests $3.5 million (Reimbursements) and 50 positions from the California Youth Authority for the operation of a 20-bed correctional treatment center serving wards who require an intermediate level of inpatient mental health care. The program will operate under the acute psychiatric license of Metropolitan State Hospital, but will be physically located within the Southern Youth Correction Reception Center and Clinic (CYA facility).
- Provides $16.9 million (Public Building Construction Fund) for the purchase of equipment for Coalinga State Hospital. All areas of hospital operations are represented in this request, including the health care clinic, automotive maintenance, information processing systems, hospital police, surgery suite, and dining areas.
- Provides $832,000 (Public Building Construction Fund) for preliminary plans to construct a new kitchen facility and renovate all existing seven satellite kitchens and dining facilities at Metropolitan State Hospital.
- Increases by $7.6 million (Public Building Construction Fund) for the construction phase of a project to provide fire, life and safety modifications at Patton State Hospital.
- Proposes $3.4 million (Public Building Construction Fund) to upgrade the electrical system at Patton State Hospital.

HUMAN SERVICES

4130 Health and Human Services Agency Data Center

The Health and Human Services Agency Data Center (HHSDC) seeks to increase efficiency and effectiveness in the use of electronic data processing resources by providing services to departments and agencies within the Health and Human Services Agency in a consolidated manner. HHSDC is supported entirely by reimbursements from departments that contract with the data center for services.

The HHSDC has two general components: operations and systems management. The operations component provides computer services, telecommunications support, information systems, and training support to departments in the Health and Human Services Agency. The systems management component manages five major projects for the Department of Social Services. These include (1) the Statewide Automated Welfare System (SAWS), automating eligibility and administrative functions for CalWORKS, Food Stamps, Medi-Cal, Foster Care, Refugee and County Medical Services programs; (2) the Child Welfare Services/Case Management System (CWS/CMS) for the Child Welfare Services, Foster Care and Adoptions programs; (3) the Statewide Fingerprint Imaging System (SFIS) to identify duplicate applicants for CalWORKS and Food Stamps benefits; (4) the Electronic Benefit Transfer (EBT) program to deliver assistance benefits to eligible recipients through electronic funds transfer; and (5) the Case Management, Information and Payrolling System (CMIPS) for the In-Home Supportive Services program. The HHSDC budget is increased by $16 million in spending authority, an increase of 5.2 percent.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
HHSDC Revolving Fund	$315, 587	$331,900	$16,313	5.2
(Operations)	[133,134]	[117,566]		
(Systems Management Services)	[182,453]	[214,334]		
Total	$315,587	$331,900	$16,313	5.2

Summary of Augmentations

- Increases by $7.2 million the HHSDC spending authority to fund various infrastructure improvements and changes to better meet customer needs. This funding will support operational/disaster recovery services for critical information technology systems, upgrades of the current information technology infrastructure, staffing resources, and a new lease.
- Increases spending authority by $35.2 million. This amount includes a $30.5 million increase for ongoing maintenance and operations needs of the CWS/CMS system and $4.7 for the design,

development, integration and implementation of the Expanded Adoptions Subsystem, a system necessary to meet federal requirements.

- Increases funding for the Electronic Benefits Transfer Program by $7.5 million to add another 27 counties to the EBT system. A total of 46 counties will have implemented the EBT system by the end of the 2003-2004 fiscal year.
- Provides an increase of $795,000 to continue the planning phase for a new CMIPS system, which manages case information and processes payroll for the IHSS program.

Issue

- The Statewide Fingerprint Imaging System works to identify duplicate applicants for CalWORKS and Food Stamps benefits. It seeks to protect program integrity by deterring or detecting duplicate-aid fraud. Specifically, SFIS matches fingerprint images of program applicants against a database containing fingerprint images of existing program participants. California has spent an estimated $53.7 million on SFIS and continuing program costs are estimated to be $10.7 million per year.

  The California State Auditor recently evaluated the level of fraud detected through SFIS, the level of fraud deterrence resulting from the system and SFIS's deterrence of eligible applicants, and the system's cost-effectiveness. The Auditor found that the Department of Social Services did not know the extent of duplicate-aid fraud before implementing SFIS. The Auditor's review suggests that the extent of known duplicate-aid fraud before SFIS was implemented appears not to have been significant. The Auditor concludes that the level of detected duplicate-aid fraud has been very small, that there is insufficient evidence to substantiate SFIS's cost-effectiveness, and that the system may run counter to legislative and federal efforts to increase participation in the Food Stamps Program among eligible individuals. The audit raises concerns about the system's goals and suggests that SFIS may be more effective at deterring eligible individuals from seeking assistance than protecting program integrity.

  The Legislature may wish to consider whether continuation of SFIS is justified, whether the Administration can demonstrate SFIS's effectiveness in protecting program integrity and present convincing evidence that the benefits of the program outweigh its deterrent effect among eligible individuals. The Legislature may wish to consider the cost-effectiveness of the SFIS program and its impact on legislative goals to increase participation in the Food Stamps Program among eligible individuals.

4140 Office of Statewide Health Planning and Development

The Office of Statewide Health Planning and Development (OSHPD) develops plans, policies and programs to assist health care delivery systems in meeting the needs of Californians. OSHPD has four major program areas: (1) healthcare cost and quality analysis; (2) healthcare workforce development; (3) facility/hospital development, including Cal-Mortgage Loan Insurance; (4) health care information. The budget is reduced by $2.3 million, a 4.1 percent reduction. This reduction eliminates in its entirety the general fund contribution to OSHPD.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$4,725	$0	-$4,725	-100.0
Federal Trust Fund	1,499	1,285	-$214	-14.2
Special Funds	44,607	48,724	4117	9.2
Reimbursements	4,577	3,118	-1,459	-31.8
Total	$55,408	$53,127	-$2,281	-4.1

Summary of Reductions

- Reduces general fund support for the Family Physician Training Program by $4.5 million and offsets this reduction with revenue from a new surcharge imposed on specific medical licenses.

- Eliminates the Health Professions Career Opportunity Program (HPCOP) for general fund savings of $143,000. The HPCOP program seeks to increase the number of health professionals who work in underserved communities by providing recruitment and mentoring services to undergraduate students from underrepresented minorities and disadvantaged backgrounds.

Summary of Augmentations

- Provides a $450,000 increase to implement AB 3050, Chapter 351, Statutes of 2002, to collect and disseminate outpatient data from all of California's emergency departments and ambulatory surgery centers. This proposal will result in the collection of 11.3 million additional records and is intended to improve California's ability to make informed decisions on health care policies. The proposed funding will support facility compliance and outreach, regulation formation, fee collection processes, and the development of outpatient data products.

4170 Department of Aging

The Department of Aging is the state agency designated to coordinate resources to meet the long term care needs of older individuals, to administer the federal Older Americans Act and the State Older Californians Act, and to work with Area Agencies on Aging to serve elderly and functionally impaired Californians. The Department provides services under (1) Senior Nutrition Services; (2) Senior Community Employment Services; (3) Supportive Services and Centers; and (4) Special Projects. The Department's budget is reduced by $2.2 million (1.2 percent) in the budget year. General Fund contribution to the Department is reduced by 16.7 percent.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$38,342	$31,910	-$6,432	-16.7
State HICAP Fund	1,604	1,604		
Federal Trust Fund	138,182	139,124	942	0.7
Federal Citation Penalties Fund		2,332	2,332	100.0
Reimbursements	5,941	6,866	925	15.6
Total	$184,069	$181,836	-$2,233	-1.2

Summary of Reductions

- Reduces funding for the Senior Nutrition Program by $2.9 million. This program serves meals to seniors in congregate settings and delivers meals at home, 5 days a week, to frail, isolated or homebound seniors. This reduction will result in the loss of $4.7 million in federal matching funds and the elimination of 5,100 seniors from the program.

- Eliminates the Senior Companion Program for general fund savings of $2 million. This program, which is funded with a combination of state, local and federal funds, provides low-income senior volunteers a modest stipend for providing light respite care and peer support to frail elders. Last year, 432 seniors provided 452,000 hours of service to 2,615 frail elders through this program.

- Eliminates the Foster Grandparent Program for savings of $1.1 million. This program provides modest stipends to low-income seniors that serve special needs children for an average of 20 hours per week. Volunteers work in various settings including health care facilities and emergency shelters.

- Eliminates the Brown Bag Program for savings of $865,000. The Brown Bag Program provides surplus and unmarketable edible fruits, vegetables and other unsold food products to low-income seniors who are eligible for SSI/SSP.

- Eliminates the Senior Housing and Information Center for savings of $787,000. The Center serves as an information clearinghouse on senior housing options and home modification resources. Its mission is to promote opportunities for Californians to live safely in their homes throughout their lifetimes.

- Eliminates the Respite Registry Program for savings of $135,000. The Program provides temporary or periodic services for frail elderly or adults with functional impairments to relieve persons who are providing care. It also recruits and screens providers and matches respite providers to clients.

Summary of Augmentations

- Provides $1 million in federal funds and $200,000 in redirected state funds for the Senior Farmers' Market Nutrition Program, which provides coupons to low-income seniors to purchase fresh fruits and vegetables at Certified Farmers Markets.

- Increases by $2.3 million funding for the State Long-Term Care Ombudsman Program to support a 50 percent program expansion. Funding will be derived from the Federal Penalty Citation Account and will be partially supplemented by federal matching funds. The Ombudsman Program serves residents of California's 7,400 Skilled Nursing Facilities, Distinct Part Skilled Nursing Facilities and Residential Care Facilities for the Elderly. Services are provided by a combination of paid staff and volunteers working at thirty-five local programs across the state. Program staff and volunteers investigate and resolve complaints, visit residents on a regular basis, provide consultation to facilities, and conduct community education sessions. This funding will increase volunteer staff by at least 650 individuals.

Issues

- <u>Are the proposed program reductions cost effective?</u>

The budget proposes elimination of various community-based service programs designed to foster senior independence and to allow seniors to continue living in their own homes. The proposals will generate $7.8 million in general fund savings for the 2003-2004 fiscal year.

The programs proposed for elimination provide services that may be critical to the ability of seniors to live independently. For example, the Senior Nutrition Program provides home delivered meals to 55,000 seniors who are homebound due to illness, incapacity, disability, or who are otherwise isolated. Reportedly, for many seniors, home delivered meals are the only contact they have with the outside world and are critical to their ability to remain at home. Without these visits, some of the unserved 5,100 seniors may face institutionalization in a nursing home. Similarly, the elimination of the Senior Companion Program and the resulting loss of services delivered by senior volunteers to frail elders may increase the number of seniors who seek services from other programs such as IHSS.

The elimination or reduction of these services when considered in concert with other proposals such as reductions of SSI/SSP grants may threaten the ability of some seniors to live independently and may result in increased demand for more costly services like IHSS and nursing home care. The Legislature may wish to consider the cost effectiveness and resulting cost avoidance of the programs proposed for elimination. The Legislature may also wish to consider the overall budget impact and the out-year budget impact of the proposed reductions. To the extent that program reductions result in increased institutionalization, these program reductions may result in significant out-year program costs.

4180 Commission on Aging

The Commission on Aging advises the Governor, Legislature, and state and local agencies on the problems and needs of older Californians. The Commission works with local Area Agencies on Aging, and it sponsors and coordinates the California Senior Legislature. The Commission is funded with a combination of federal funds, and voluntary tax contributions. The proposed budget is reduced by $41,000 over current year spending, a reduction of 5.9 percent.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
California Seniors Special Fund	$62	$62	$0	
Federal Trust Fund	374	286	-88	-23.5
California Fund for Senior Citizens	249	296	47	18.8
Total	$685	$644	-$41	-5.9

4200 Department of Alcohol and Drug Programs

The Department of Alcohol and Drug Programs (DADP) receives and disburses federal and state alcohol and drug funds to plan, develop, implement and evaluate a statewide system for alcohol and other drug intervention, prevention, detoxification, treatment and recovery services. The Department is the lead agency in the implementation of Proposition 36 (the Substance Abuse and Crime Prevention Act of 2000). Appropriations in the budget year are proposed to decrease by $91.3 million (15.8 percent).

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$232,811	$5,673	-$227,138	-97.5
Sale of Tobacco to Minor Control Acct.	-2,000	-2,000	0	0.0
Driving-Under-the-Influence Program Licensing Fund	1,573	1,573	0	0.0
Narcotic Treatment Program Licensing Fund	1,450	1,550	100	-6.8
Audit Repayment Trust Fund	67	67	0	0.0
Federal Trust Fund	274,717	275,266	549	.1
Resident Run Housing Revolving Fund	39	39	0	0.0
Reimbursements	65,813	200,976	135,163	205.0
Substance Abuse Treatment Trust Fund (non-add)	[120,087]	0		
Total	$574,470	$483,144	-$91,326	-15.8

Summary of Reductions and Adjustments

- Realigns drug and alcohol programs, including Drug Medi-Cal and Proposition 36 funded programs, for general fund savings of $231 million.

- Reduces Drug Medi-Cal funding by $7.6 million in the current year and $2.6 million in the budget year. These changes are related to caseload adjustment, reductions in cost, and changes in utilization of services.

- Provides $4 million in federal funds to implement science based substance abuse prevention programs and practices at the local level that target youth and to increase collaboration and coordination at the state level among agencies with prevention initiatives that target youth and young adults.

Issues

- Realignment of alcohol and drug treatment programs
  The budget proposes to realign multiple alcohol and drug treatment programs to counties for general fund savings of $231 million. The realigned programs include Drug Medi-Cal services, drug court programs, Proposition 36 funding and non-Medi-Cal alcohol and drug services. The realignment proposal lacks specificity regarding how alcohol and drug treatment programs will operate within realignment. Establishing specific parameters to govern how these programs will work when realigned is essential to ensuring compliance with Proposition 36 and adequate availability of services. For example, California will need to maintain spending at the federally required maintenance-of-effort level to assure continued receipt of federal funds within realignment. The state will need to develop a system to track Drug Medi-Cal expenditures within the context of realignment to maximize the state's use of matching federal funds. The state will also need to assure Proposition 36 funding and programs are administered in accordance with legal requirements. The Governor's Proposed Budget and its implementing legislation do not specify whether counties will be given increased flexibility to significantly alter programs, reduce services, or otherwise contain costs. The budget does not specify if counties will have expanded program authority or whether the programs

will essentially operate as currently crafted. The Legislature may wish to ask the Administration to clarify how these programs will be modified as a result of realignment, what if any additional flexibility will be granted to counties and how realignment will affect service delivery. Despite the need for technical development, the realignment of drug and alcohol programs may provide an opportunity for innovation at the local level and a chance to address barriers to individuals accessing services within the Drug Medi-Cal program.

- State at risk of losing $95 million in federal funds.
  Federal law establishes that California must maintain general fund spending on drug and alcohol programs at an amount equal to the average of the state's spending in the previous two years to assure continued receipt of federal Substance Abuse and Treatment funds. If the state does not meet its maintenance of effort requirement, its federal funds are reduced by an amount equal to the state's under funding of its maintenance of effort.

  Proposition 36, a voter based initiative approved in 2000, requires that certain non-violent offenders and parolees who use or possess illegal drugs receive drug treatment and intensive supervision in the community instead of being incarcerated. The Proposition also requires the appropriation of $120 million annually for five years to finance its implementation. In the 2005-2006 fiscal year California will no longer be obligated to make this appropriation.

  Since the Proposition 36 appropriation is time limited, the Administration wants to exclude these funds from MOE calculations to reduce its out-year obligation to drug and alcohol treatment programs. The federal government recently disapproved California's proposal to exclude Proposition 36 funds from its MOE calculations. California intends to challenge the federal ruling. If the state's efforts fail, California stands to lose $95 million in federal funds due to not meeting its MOE in the budget year.

4700 Community Services

The Department of Community Services and Development administers programs in three main areas: (1) Low Income Home Energy Assistance Programs (LIHEAP and CaLIHEAP), (2) Department of Energy Weatherization Assistance Program (WAP), and (3) federal Community Services Block Grant. The department also verifies eligibility of applicants for the California Alternative Rates for Energy Program offered by utility companies, administers the Naturalization Services Program and the Lead-Based Paint Abatement and Prevention Program, and participates in the multi-department California Mentor Program for at-risk youths. Programs are administered through a statewide system of community agencies. The Governor's Budget proposes to eliminate the Department of Community Services and Development and to transfer its responsibilities to the Department of Social Services.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$5,378	$0	-$5,378	
Petroleum Violation Escrow Account	0	0	0	
Federal Trust Fund	150,902	0	-$150,902	
Reimbursements	9,235	0	-$9,235	
Energy Programs	[97,959]	[0]		
Community Services	[60,932]	[0]		
Naturalization Services	[6,624]	[0]		

Total	$165,515	$0	-$165,515	-100.0

Summary of Reductions

- Consolidates the Department of Community Services and Development with the Department of Social Services. Shifts $155.1 million in federal funds (Low-Income Home Energy Assistance Program and Community Services Block Grant) from the Department of Community Services and Development to the Department of Social Services due to the consolidation. The budget estimates a reduction of $922,000 in state administration costs and proposes to shift these funds to local assistance. There are no general fund savings associated with the proposed consolidation.

- Eliminates the Naturalization Services Program to realize savings of $7.9 million ($2.9 million general fund).
- Eliminates the Mentoring Program for savings of $1 million general fund. The program supports community-based organizations that operate mentoring programs serving at-risk youth. It seeks to increase the number of trained mentors, increase the number of mentor-mentee matches, increase the number of mentor hours available, increase awareness and support of local mentor programs and reduce the rate of teenage pregnancy, alcohol and drug use, school dropout and gang violence.

Issues

- Consolidation of Community Services and Development within Social Services
  Since its inception in 1964 to provide technical assistance to local agencies developing and administering community action programs, the Department of Community Services and Development has been restructured several times. The program has been consolidated with the Employment Development Department and with the Health and Human Services Agency. Since 1996, the department has existed as a stand-alone department within the Health and Human Services Agency.

  The budget consolidates the Department of Community Services and Development with the Department of Social Services to improve efficiency in state government. The budget assumes a reduction of $922,000 in state administration costs and proposes to shift these funds to local assistance. The proposal will not result in any general fund savings.

  The effect of this proposal on program accountability and the ability of community action programs to operate efficiently may hinge on factors that are currently undefined. For example, the Governor's Budget does not specify what branch of the Department of Social Services will assume the responsibilities transferred from the Department of Community Services and Development. The budget and proposed legislation do not outline the organizational structure or principles that will guide program implementation within DSS. The proposal lacks mechanisms to assure the federal grants are administered in a centralized manner and to provide clear channels of responsibility and accountability. The Legislature may wish to further develop key elements of this proposal.

- Elimination of the Naturalization Services Program
  The budget proposes to eliminate the Naturalization Services Program to realize savings of $7.9 million ($2.9 million general fund). The program assists legal permanent residents to obtain citizenship. It conducts outreach, provides citizen preparation and assistance, skills assessments, and advocacy/follow-up through contract services provided by community agencies. It assists an average of 7,400 individuals per year in the completion of citizenship applications. The program spends an average of $350 per person served.

5160 Department of Rehabilitation

The Department of Rehabilitation assists people with disabilities to obtain and retain employment and to maximize their ability to live independently in the community. The department operates the Vocational Rehabilitation Services program, funded primarily with federal funds, to provide vocational services to persons with disabilities. Some of these services are provided through cooperative agreements with other state and local agencies (education, mental health, welfare). The department provides habilitation services, vocational and supported employment services for persons with developmental disabilities, using state funds and federal Home and Community Services Medicaid reimbursements. It also provides support services for Community Rehabilitation Programs, including independent living centers. The budget is anticipated to be $343.8 million ($43.1 million General Fund), a decrease of 28.4 percent and a decrease in the overall general fund contribution of 72.1 percent.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$154,645	$43,100	-$111,545	-72.1
Vending Stand Account	3,360	3,421	61	-1.8
Federal Funds	293,640	289,481	-4,159	-1.4
Reimbursements	28,691	7,818	-20,873	-72.7
Total	$480,336	$343,820	-$136,516	-28.4

Summary of Reductions

- Reduces provider rates in the Work Activity Program (WAP) by 5 percent to realize savings of $3.1 million. The program provides work experience and ancillary work-related services in a sheltered setting to persons with developmental disabilities.
- Reduces provider rates in the Supported Employment Program (SEP) by 5 percent for savings of $3.2 million. SEP provides competitive employment opportunities and necessary training and ancillary support services to enable clients to learn necessary job skills and maintain employment.
- Suspends WAP rate adjustments through 2005-2006 to realize savings of $12.3 million.
- Transfers the Habilitation Services Program from the Department of Rehabilitation to the Department of Developmental Disabilities (DDS) and consolidates it within the Regional Centers for total savings of $1.5 million general fund. The total funds transferred to DDS are $116 million.

Issues

- Transfer of the Habilitation Services Program to the Department of Developmental Disabilities
  The Habilitation Services Program (HSP) provides a range of services to persons with developmental disabilities, and blind and deaf-blind individuals to assist them in reaching and maintaining their highest level of vocational potential. The majority of HSP clients are persons with developmental disabilities who receive work experience and ancillary work related services in a sheltered setting through the Work Activity Program or competitive employment opportunities and training and ancillary support services through the Supported Employment Program. These services are an entitlement under the Lanterman Act.

Not-for-profit entities and job coaches generally provide Habilitation Services Program services. The Department of Rehabilitation is responsible for administering the program, monitoring compliance with program requirements and reimbursing providers. HSP serves over 18,000 clients annually and has a total budget of $138.7 million ($117.7 million general fund).

The Budget transfers the Habilitation Services Program from the Department of Rehabilitation to the Department of Developmental Disabilities and consolidates program administration. The budget assumes increased administrative efficiencies as a result of the proposed transfer and estimates net savings of $1.5 million general fund. The proposal does not assume any new funding to the Regional Centers for program administration.

The 2002 Budget Act required the Department of Rehabilitation and the Department of Developmental Disabilities to provide a report on the Habilitation Services Program rates and consumer eligibility, and to make recommendations for streamlining and consolidating programs, if such changes are warranted. The Legislature may wish to consider the findings and recommendations of the forthcoming report when evaluating this proposal.

The Legislature may wish to consider the effects of this proposal on client services and to further develop how the program will function within DDS. Currently, the proposal does not outline how program administration will be modified as a result of the transfer. It does not address how the WAP and SEP program rate structure will be reconciled with Regional Center rate structures. It does not specify the licensing process and requirements under which the program will operate and does not specify how the DDS and Regional Centers will reimburse providers. The result of this transfer and its impact on client services may hinge on the development of a clear and specific transition plan that is workable for the departments, providers and clients.

- <u>WAP and SEP provider rate reductions</u>
  The Budget reduces provider rates in the Work Activity Program and the Supporter Employment Program by 5 percent to realize savings of $6.3 million in general fund. Rates in the Supported Employment Program will be lowered from $28.33 to $26.91 per job coach hour, their pre-1998 rate level. The proposed reductions may significantly diminish provider participation in the program and may result in reduced client services. The Legislature may wish to consider the effect of this proposal on clients' ability to access services and the extent to which reductions in WAP and SEP services may lead to individuals participating in more costly programs.
- The Budget proposes to suspend WAP rate adjustments for the 2003-2004 fiscal year to realize savings of $12.3 million. Since WAP rates are adjusted biennially and 2003-2004 is a rate setting year, suspension of the rate adjustment will continue the current rates until the 2005-2006 fiscal year.

5175 Department of Child Support Services

The Department of Child Support Services (DCSS), established as of January 1, 2000, administers the child support enforcement program operated by local child support agencies. The Department provides state direction to assure that child support amounts are established, collected, and distributed to families, including securing child and spousal support, medical support, and determining paternity. The Department continues to have responsibility for addressing federal fiscal sanctions related to California's failure to develop adequate systems in the past. The department oversees local program and fiscal operations, administers the federal Title IV-D state plan for securing child support, and establishes performance standards for California's child support program. The budget anticipates collections of $2.3 billion in the budget year. The department's overall budget decreases by $17.8 million (1.5 percent).

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Funds	$465,023	$470,172	$5,149	1.1
Federal Funds	406,484	388,597	-$17,887	-4.4
Reimbursements	443	443		
Child Support Collection Recovery Fund	310,243	305,148	-$5,095	-1.6
Total	$1,182,193	$1,164,360	-$17,833	-1.5

Summary of Reductions

- Reduces by $108.8 million ($37 million general fund) funding for local child support departments. This reduction reflects the actual expenditure levels for local child support administration for the 2001-2002 fiscal year, as well as other program reductions.

- Proposes legislation to require a 25 percent county share of cost for the federal penalty levied against California due to the state's delay in implementing a single statewide-automated system for the collection of child support and assumes additional general fund revenue of $51.8 million.

- Eliminates the transfer of child support collection revenues to the Foster Parent Training Fund for an increase of $2.6 million general fund revenue.

Summary of Augmentations

- Provides an increase of $18.9 million to fully fund the alternative federal penalty. The total penalty in the 2003-2004 fiscal year amounts to $207.1 ($155.3 million General Fund).

- Transfers $1.3 million from the Department of Justice to the Department of Child Support Services to support transfer of the California Parent Locator Service and the California Central Registry to DCSS.

Summary of Issues

- Federal Child Support Penalty
  Since the late 1990s California has been assessed penalties by the federal government due to the state's failure to develop a statewide automated system for the collection of child support. The penalties are a percentage of program administration costs and the percentage rises over time. California has reached the maximum percentage level and will pay $207.1 million in the budget year. The Budget provides an increase of $18.9 million to fully fund the penalty. It also proposes a 25 percent county share of the federal penalty to provide $51.8 in new general fund revenues in the budget year. California is in the early stages of developing the California Child Support Automated System (CCSAS) which when implemented on a statewide basis will obviate federal penalties.

- Elimination of the Foster Parent Training Fund
  California transfers the difference between the state share of child support foster care collections and the base level of the estimated share of child support foster care collections, up to a maximum of $3 million, to the Foster Parent Training Fund. This funding supports foster parent training programs offered by the Chancellor's Office of the California Community Colleges and is used to leverage $3.4

million in federal matching funds. The programs provide training to facilitate the development of foster family homes and small family homes to care for children who have special needs.

A recent federal audit of California's Child Welfare Services System found that California is not operating in substantial conformity in all evaluated outcome areas and five of the seven evaluated factors. The areas reviewed include whether California protects children from abuse and neglect, keeps children safely in their homes whenever possible, provides children permanent and stable living situations, and provides children appropriate services to meet their educational, mental health and physical needs. The audit identified foster parent training as an area where California needs to improve. The Legislature may wish to consider the appropriateness and wisdom of reducing foster parent training programs particularly in light of the recent federal audit.

- <u>Reduction of child support administration funding</u>
  Currently, child support administration funding is provided to counties in a lump sum. Counties have discretion in allocating these resources to the different departmental activities. The Budget proposes to reduce overall funding for local child support administration by $108.8 million ($37 million general fund). The state department plans to work with counties to target funding reductions to areas that will cause the least disruption to the critical functions of child support collections, establishment of paternity and improving program performance. The Legislature may wish to carefully consider this proposal and ensure that reductions in local assistance do not result in reduced revenue due to scale backs in collection activities.

- <u>Elimination of Health Insurance County Incentive</u>
  Current law provides an administrative incentive payment of $50 to county programs for obtaining third-party health coverage available from non-custodial parents. The budget proposes to suspend this program, and to claim savings of $3.2 million General Fund as a result. The Legislature may wish to consider the extent to which these incentives result in cost avoidance due to decreased participation in public health insurance programs.

5180 Department of Social Services

The Department of Social Services administers a variety of programs that have four major goals: 1) providing temporary cash assistance and services to encourage low-income families with children to attain self-sufficiency by moving from welfare to permanent employment; 2) providing social services to elderly, blind, disabled and other adults and children, protecting them from abuse, neglect and exploitation, and helping families stay together and in the community; 3) regulating group homes, preschools, foster care homes, day care and residential care facilities to ensure they meet established health and safety standards; and 4) conducting disability evaluations and providing benefit payments for federal and state programs serving the aged, blind and disabled. The department's total budget decreases by $807.4 million, a decrease of 4.5 percent. General Fund appropriations decrease by $3.9 billion, or 47.7 percent.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$8,123,229	$4,244,241	-$3,878,988	-47.7
Emergency Food Assistance Fund	309	462	153	49.5
Cont. Care Provider Fee Fund	967	942	-25	-2.5
Technical Assistance Fund	3,151	3,055	-96	-3.0
Certification Fund	1,163	1,122	-41	-3.5
Child Health and Safety Fund	1,358	1,308	-50	-3.6
Employment Training Fund	30,000	21,432	-8,568	-28.5
State Children's Trust Fund	1,938	1,942	4	.2
Federal Funds	6,498,334	5,848,361	-649,973	-10.0
Reimbursements	1,829,218	3,095,440	1,266,222	69.2
Transitional Housing for Foster Youth Fund	602	907	305	50.6
County Funds (Non-add)	[1,273,978]	[3,737,618]	[2,463,640]	193.3
Total	$17,764,247	$16,956,830	-$807,417	-4.5

CalWORKs

Prior to 1996, welfare was a federal entitlement under the Aid to Families with Dependent Children. The 1996 federal welfare reform law, Temporary Assistance for Needy Families (TANF), eliminated the federal entitlement, introduced work participation requirements, provided for services designed to support employment and gave states block grant funding and program flexibility. The California Work Opportunity and Work Responsibility to Kids (CalWORKs) program, California's implementation of TANF, became operational January 1, 1998. The CalWORKs program provides eligible low-income families monthly cash benefits and a variety of services, including employment services, childcare, and substance abuse treatment and mental health services, designed to support employment assist families in moving to self-sufficiency within time limits imposed by federal and state law. It requires participants to meet work participation requirements as a condition of receiving aid and sets a 60-month lifetime limit on aid for adults in the program, unless they meet specified exemption criteria. CalWORKs operates under guidelines set at the federal and state levels. It is overseen by the California Department of Social Services and administered locally by counties.

County welfare departments are provided a block grant and given flexibility to design and carry out the program within the state and federal program guidelines. County staff determine eligibility for the program, provide case management for recipients, including the development of welfare-to-work plans and referrals for services such as mental health and substance abuse treatment, domestic violence services, learning disability screenings, education, training, child care, housing assistance, and transportation. While state law establishes specific eligibility requirements, counties are given considerable flexibility to design welfare-to-work services.

Caseload

CalWORKs provides cash benefits and welfare-to-work services to children and their parents or caretaker relatives who meet specified eligibility criteria including having a family income below the CalWORKs maximum aid payment, having less than $2000 in resources, and having a car valued at $4,650 or less.

The average family of three must have a net income below $7,644 per year or 51 percent of the federal poverty level to be eligible for CalWORKs. CalWORKs recipients are required to participate in welfare-to-work activities and perform a minimum of 32 hours of work activities per week to remain eligible for benefits.

After peaking in 1994-95, the CalWORKs caseload has dropped by 46 percent through 2002. This decline is due to a combination of demographic trends (such as decreasing birth rates for young women), California's economic expansion, and full implementation of welfare reform. After years of declines, the Department of Social Services estimates caseload will increase by 1.9 percent in 2002-2003 and .8 percent in 2003-2004. The budget assumes that the CalWORKs average monthly caseload will be 517,472.

Program funding

CalWORKs is currently funded through an annual federal block grant of $3.7 billion and state-matching funds of $2.7 billion. California's $2.7 billion federally required state share is based on welfare spending in 1994, adjusted downward for achievement of certain work participation goals. Federal law requires states to spend TANF funds on current and former welfare recipients with some limited exceptions. Accordingly, California spends most federal funds on CalWORKs, and directs some TANF funds and some of the state's share-of-cost to activities in other departments including the Kinship Guardianship Assistance Program, services for persons with developmental disabilities and juvenile camps.

The Budget proposes total CalWORKs funding of $6.67 billion, $5.8 billion of which will be spent on the CalWORKs program, and $852 million to support non-CalWORKs federally allowable activities. This constitutes a $715 million, or 11 percent decrease in CalWORKs expenditures from the current year. The budget reduces general fund expenditures on CalWORKs by $901 million or by 36 percent.

The CalWORKs budget includes the following major components:

- Proposes legislation to suspend the annual cost of living adjustment for CalWORKs grants for the 2002-2003 and the 2003-2004 fiscal years to generate $252.4 million in savings, $80 million of which are estimated to be general fund savings.

- Reduces the maximum aid payment under CalWORKs by approximately 6.2 percent to $637 for a family of 3 to generate savings of $235.2 million none of which are general fund. This proposal will result in some families becoming ineligible for CalWORKs and for associated program services.

- Assumes a net savings of $440.1 million ($169.6 for grants, $204.6 for services and $65.8 for childcare) because thousands of recipients will reach their total 60-month time limit of eligibility. Upon reaching their time limit, participants who are working continue being eligible for services. Children remain eligible for safety net grants after the time limit is reached.

- Proposes a 50 percent county share of cost for CalWORKs employment services and administration for general fund savings of $543.7 million. These savings are associated with the proposed realignment of CalWORKs administration and employment services.

- Reduces CalWORKs administration by $56.3 million due to the implementation of prospective budgeting by September 1, 2003. Prospective budgeting will require beneficiaries to report their earnings and other eligibility related information on a quarterly basis instead of every month. The budget assumes savings due to significant decreases in the number of reports counties will process.

- Transfers $65.7 million in TANF funds to the Department of Developmental Disabilities.

- Provides a one-time augmentation of $241.5 million for CalWORKs employment services.

Issues

- Proposed suspension of CalWORKs cost of living adjustments
  The Budget suspends the 2002-2003 and 2003-2004 cost-of-living adjustments (COLA) for the CalWORKs program to realize savings of $252.4 million, $80 million of which are estimated general fund savings. Current law provides an annual cost of living adjustment for CalWORKs grants that is based on the California Necessities Index. The scheduled cost of living adjustments will increase the maximum CalWORKs grant from $679 to $729. Suspension of the cost-of-living adjustment will maintain grants at their current level and will not keep pace with cost of living increases such as rising housing costs. The Senate approved legislation in this year's special session to suspend the CalWORKs COLA for the 2002-2003 fiscal year.

- Proposed CalWORKs grant reductions
  The budget reduces the maximum aid payment under CalWORKs by approximately 6.2 percent to $637 for a family of 3. This proposal generates non-general fund savings of $235.2 million.

  This proposal reduces CalWORKs grants by $42 per month. The reduction will be partially offset by a $19 increase in monthly food stamps benefits. Overall, families will experience a decrease in their income from 78 to 76 percent of the federal poverty level or from $974 to $951 per month.

  In addition to decreasing resources available to very low-income families, the budget's grant reduction will make some families ineligible for CalWORKs and for associated program services. Individuals that have been participating in welfare-to-work activities and who are actively employed are most likely to lose CalWORKs eligibility as a result of the proposed grant reductions. These individuals may lose their health insurance coverage, childcare services, transportation and other services essential to their continued employment. The Budget does not estimate the number of people who will become ineligible as a result of reducing grants. It also does not appear to include savings for the resulting caseload decrease and reduced utilization of services.

  The proposed grant reductions may also lower the statewide CalWORKs work participation rates. Families who become ineligible as a result of grant reductions are most likely working and contributing to California's work participation rates. The termination of aid to families that are working, combined with effects of working families reaching their time limit, may result in lower work participation rates. Lower work participation rates may in turn increase the federally required state match by $181.7 million and may result in federal penalties. The Budget does not estimate the impact of the grant reductions on California's work participation rates.

  It is not clear that the Administration intended to reduce caseload and restrict access to services. The Administration may wish to clarify its intent with this proposal. For example, did the Administration intend to eliminate benefits and services for people who would otherwise remain eligible for welfare-to-work services? What services will these people continue to receive? What administrative procedures will be necessary to ensure individuals who become ineligible for benefits continue receiving services? The Administration may wish to consider the impact of this proposal on the ability of welfare recipients to retain employment and the estimated impact of this proposal on California's work participation rate.

  The Legislature may wish to consider the consequences of these grant reductions including their impact on the ability of welfare recipients to obtain and retain employment and effects on California's work participation rate. Are these reductions cost effective even if they do not result in any general fund savings?

- Realignment of CalWORKs employment services and administration
  The Budget proposes to realign CalWORKs administration, CalWORKs employment services and Stages 2 and 3 of childcare. Under realignment counties will assume funding responsibility for Stages 2 and 3 of childcare and for 50 percent of the cost for CalWORKs employment services and administration. For the 2002-2003 fiscal year, the budget estimates expenditures for CalWORKs administration and employment services to remain at their current level. This level of funding has not been adjusted since the 2000-2001 fiscal year and was reduced by $49 million in 2002-2003, leading to an estimated county under funding of $297 million. The budget estimates that under realignment counties will contribute $1 billion to fund CalWORKs, $881 million more than they were required to contribute last year.

  The proposal to realign CalWORKs employment services and administration appears feasible. Counties have been responsible for program administration and the provision of welfare-to-work services since 1998. The program caseload is relatively stagnant and not expected to increase significantly in the foreseeable future. Federal law requires that most TANF funding be spent on current and former welfare recipients thus ensuring that realigned dollars will be used to serve the welfare population. However, the budget lacks important details regarding the proposed realignment. For example, it does not specify how CalWORKs administration and employment services will be modified. It is unclear whether counties will be given increased flexibility to restrict access to services or otherwise contain costs. The budget does not specify if counties will have expanded program authority or whether the program will essentially remain the same. The Legislature may wish to clarify how the CalWORKs program will be modified as a result of realignment, what if any additional flexibility will be granted to counties and how realignment will affect the ability of welfare recipients to access services. The Legislature may also wish to consider the effect of realigning employment services on county efforts to encourage the transition of recipients from welfare to work and how the proposed realignment will affect existing county incentives. For example, will it be cheaper for counties to reduce the availability of employment services and reduce its efforts to support the transition of beneficiaries from welfare to work resulting in higher welfare caseloads? The Legislature may wish to consider the appropriateness of realigning employment services and may want to consider other alternatives such as increasing the county-share of cash grants.

  The United States Congress is expected to approve TANF Reauthorization in the current Congressional Session. The TANF Reauthorization bill proposed by the President makes significant changes to TANF including higher work participation requirements, reductions in the number and types of activities that can be counted as work, and changes in the way in which participation is calculated. To the extent that TANF Reauthorization makes major changes to the program, California will likely need to revisit and revise CalWORKs. Program costs may increase as a result of changes in TANF and CalWORKs. The Administration may wish to consider the interaction between realignment and the prospect of TANF Reauthorization. The Legislature may wish to consider the appropriateness of realigning components of CalWORKs on the verge of TANF Reauthorization.

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

The SSI/SSP program provides cash grants to persons who are elderly, blind and/or too disabled to work and who meet the program's federal income and resource requirements. Individuals who receive SSI/SSP are categorically eligible for the Aged, Blind or Disabled Medi-Cal Program with no share of costs, for the In-Home Supportive Services Program and may be eligible for other programs designed to keep individuals living in the community like the Multipurpose Senior Services Program.

The SSI/SSP program is administered by the federal Social Security Administration. The Social Security Administration determines eligibility, computes grants, and disburses monthly payments to recipients. The state contributes the State Supplementary Program portion of the program.

More than 1.1 million Californians receive SSI/SSP. Over two-thirds of recipients are disabled, 30 percent are elderly, and two percent are blind.

Caseload

The budget estimates that program caseload will grow by 2.2 percent in the 2002-2003 fiscal year and by 1.9 percent in the 2003-2004 fiscal year. The total caseload for 2003-2004 is estimated to be 1,148,176. Due to changing demographics and a projected increase in California's aging population, the SSI/SSP program caseload is likely to continue its growth in future years.

Program Funding

The budget estimates basic program costs for the SSI/SSP program for the 2003-2004 fiscal year to be $7.4 billion ($2.8 general fund). The Budget proposes significant reductions to the SSI/SSP program. Specifically, it:

- Suspends the 2002-2003 and 2003-2004 state funded cost-of-living adjustments for the SSI/SSP program for savings of $372.3 million.

- Reduces SSI/SSP grants to the federally required maintenance of effort level for savings of $662.4 million. The budget reduces the total SSI/SSP grant by 6.2 percent to a maximum grant of $708 for individuals and $1,225 for couples.

The Budget also proposes significant changes to the Cash Assistance Program for Immigrants (CAPI) which is a state funded program that provides cash benefits to aged, blind and disabled legal immigrants who became ineligible for SSI as part of welfare reform. CAPI grant levels are linked to the SSI/SSP grant levels, thus the budget reduces CAPI grants at the same rate as SSI/SSP grants for savings of $3.5 million. The budget also realigns the program to the counties.

Issues

- <u>Suspension of state SSI/SSP cost of living adjustment</u>
  The Budget suspends the 2002-2003 and 2003-2004 cost of living adjustments for the SSI/SSP program to realize savings of $372.3 million. Current law provides an annual state cost of living adjustment for SSI/SSP grants, which is based on the California Necessities Index. The scheduled cost of living adjustments will increase the maximum SSI/SSP grant for an individual from $757 to $805. The budget does propose to continue pass-through of the federal SSI COLA. Suspension of the state cost-of-living adjustment will maintain grants at a level that does not keep pace with cost-of-living increases such as rising housing costs. The Senate approved legislation in this year's special session to suspend the SSI/SSP COLA for the 2002-2003 fiscal year.

- <u>Reduction of SSI/SSP grants to the federally required maintenance of effort level</u>
  The budget reduces SSI/SSP grants to the federally required maintenance of effort level for savings of $662.4 million general fund. It reduces total SSI/SSP grant by 6.2 percent to a maximum grant of $708 for individuals and $1,225 for couples.

This proposal reduces SSI/SSP grants by $49 per month for individuals and by $119 for couples. The income of SSI/SSP recipients will decrease from 102.5 percent to 95.9 percent of the federal poverty level for individuals and from 135 percent to 123 percent of the federal poverty level for couples. In addition to decreasing resources available to low-income aged, blind and disabled individuals, the budget's grant reduction will make approximately 14,500 individuals ineligible for SSI/SSP benefits. These 14,500 individuals will also lose their categorical eligibility for Medi-Cal and the In-Home Supportive Services Programs and may need to pay a share-of-cost each month to continue receiving services. The share-of-cost is based on the amount by which that individual's income or assets exceed the applicable Medi-Cal limits. The required share-of-cost payment would, of course, be significant for people on fixed, low-incomes. Individuals who cannot afford to pay the share-of-cost, and who are adversely affected by other budget reductions including cuts to the Senior Nutrition Program and the Brown Bag Program, may see their system of care crumble and may face institutionalization at a significantly higher cost to the state.

The Legislature may request that the Administration clarify its intent with this proposal. For example, does the Administration intend to eliminate benefits and services for people who would otherwise remain eligible? What services will these people become ineligible for and how will the loss of these services affect the individual's ability to remain in the community? What administrative procedures will be necessary to ensure individuals who become ineligible for benefits to continue receiving other services they remain eligible for?

The Legislature may wish to consider the consequences of these grant reductions including their impact on the ability of aged, blind and disabled individuals to continue living independently and the potential costs associated with individuals becoming ineligible for no cost Medi-Cal and IHSS. Are these reductions cost effective?

- <u>Realignment of the Cash Assistance Program for Immigrants</u>
  The Cash Assistance Program for Immigrants (CAPI) provides cash benefits to legal immigrants who are not eligible for the SSI/SSP program due to their date of entry. The program was created after federal welfare reform law made these individuals ineligible for the federal program. CAPI is funded by the state and administered by counties. Currently it does not require a county share-of-cost. The Budget proposes to realign CAPI to the counties for general fund savings of $95.3 million.

  Realignment of CAPI may be feasible from a technical standpoint. Counties have been responsible for program administration since the program's inception. The program caseload is relatively stagnant and not expected to increase in the foreseeable future. Legislation approved in 2001 made the program a state entitlement, and the realignment proposal does not change its status at this time. The Administration may wish to clarify how, if at all, the CAPI program will be modified as a result of realignment, what, if any, additional flexibility will be granted to counties and how realignment will affect immigrant access to services.

  The Department of Social Services (DSS) was recently challenged in court regarding statutory interpretation as it relates to determining a person's date of entry for purpose of establishing CAPI eligibility. The lawsuit alleges that California has illegally denied benefits to eligible immigrants. DSS argues that the date a person "entered the United States" does not mean physical entry, but rather means the date the person became a lawful permanent resident. The statute literally reads "entered the United States". Plaintiffs' argue that the statutory language means exactly what it states, "entered the United States", and that the department's denial of benefits to elderly immigrants who entered the U.S. before 1996 but did not adjust their immigration status until a later date is illegal. The Court's ruling in this case may impact caseload and result in caseload increases. The Administration and the

Legislature may wish to consider the impact of this litigation on program caseload and the proposed realignment.

Food Stamps

The Food Stamps program provides eligible low-income families and individuals food stamps benefits at no cost. The program is overseen by the Department of Social Services and is administered by the counties. The Food Stamps program will serve an estimated 1.9 million persons, approximately 144,000 more than last year. The projected caseload increase is mostly the result of restoration of federal food stamp benefits to immigrants who had lost these benefits as a result of the welfare reform law.

The U.S. Department of Agriculture funds the benefit value of food stamps. The federal government also funds 50 percent of the program's administrative costs. The remaining 50 percent is split between the state and counties at a ratio of 70 percent to 30 percent respectively.

The state also administers the California Food Assistance Program (CFAP), a state-only food stamp program for legal non-citizens. The restoration of federal food stamps benefits to legal immigrant will dramatically reduce CFAP beneficiaries in the budget year. The estimated caseload at the end of the budget year is approximately 5,000.

The budget proposes a series of major adjustments to the Food Stamps Program. Specifically, the budget:

- Realigns food stamps administration costs and the CFAP program to counties for general fund savings of $282.6 million.
- Reduces funding for food stamps and CFAP administration by $18.5 million due to the implementation of prospective budgeting effective October 1, 2003. Prospective budgeting will require beneficiaries to report their earnings and other eligibility related information on a quarterly basis instead of every month. The budget assumes savings due to significant decreases in the number of reports counties will be required to process.

Issues

- <u>Realignment of the Food Stamps Program and the California Food Assistance Program</u>
  The budget proposes to realign Food Stamps Program administration and the California Food Assistance Program for general fund savings of $282.6 million. This proposal may be feasible from a technical standpoint as the counties have historically administered the program and already participate in funding administrative costs for the Food Stamps Program. However, the proposed realignment should be considered in the context of a series of changes that will significantly affect program operations.

  The Food Stamps program faces substantial federal penalties due to the state's high error rates. Although the state has initiated reforms in efforts to reduce its error rates (such as implementation of prospective budgeting) California currently faces significant federal penalties. The state is making progress in reducing its error rates, however it is likely to face similar penalties in the foreseeable future. Under current regulations, counties are liable for 90 percent of the federal penalty. Under realignment, counties will likely be responsible for 100 percent of future penalties and for financing system changes necessary to implement the state's plan for corrective action.

  Additionally, California is in the process of implementing the federally required Electronics Benefits Transfer system, which replaces paper food stamps with a debit card system. Findings from the initial implementation efforts suggest that significant training and follow-up is necessary to ensure proper use of the cards.

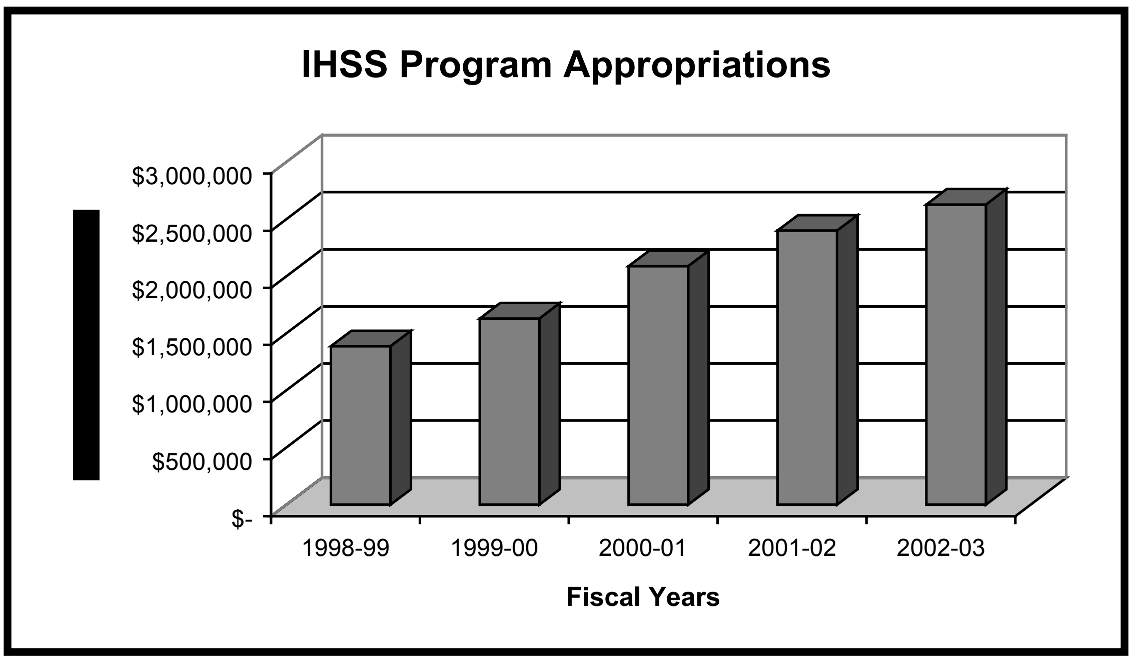
Lastly, recent changes in federal law restored Food Stamps eligibility for tens of thousands of legal immigrants. It is in California's best financial interest to transition eligible individuals from the California Food Assistance Program to the federal Food Stamps Program promptly. Effecting the transition of beneficiaries from one program to the other will require significant resources at the local level.

The Administration may wish to clarify how, if at all, the Food Stamps and CFAP programs will be modified as a result of realignment and how it foresees the counties and the state will cope with the aforementioned program changes in the realignment model. What if any additional flexibility will be granted to counties and how will realignment affect the ability of low-income individuals to access food benefits?

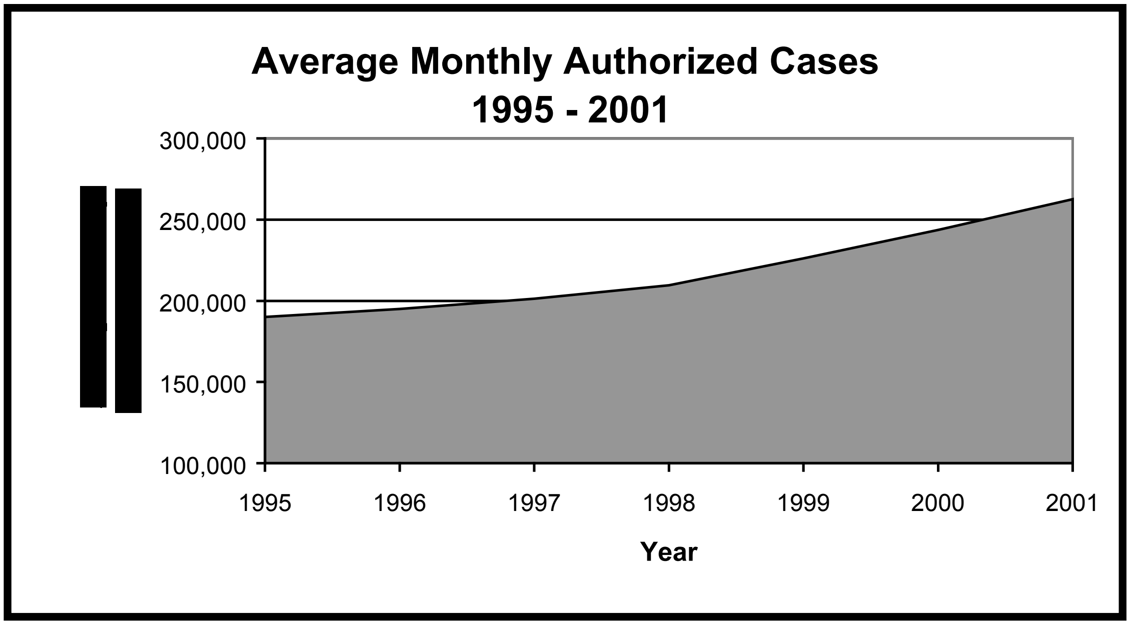
In-Home Supportive Services (IHSS)

The In-Home Supportive services (IHSS) program provides services to aged, blind or disabled individuals that allow them to remain safely in their own homes as an alternative to out-of-home care. Services include domestic services (meal preparation, laundry), nonmedical personal care services, assistance while traveling to medical appointments, teaching and demonstration directed at reducing the need for support, and other assistance. Services are provided through individual providers hired by the recipient, county contracts with service providers, or through welfare staff. 74 percent of the persons receiving IHSS are provided federally reimbursable services through the Personal Care Services program of the Medicaid program. The remaining are served through the State's IHSS Residual Program.

The total cost of the IHSS program has nearly doubled from $1.39 billion in fiscal year 1998-99 to $2.63 billion in 2002-03. In 2003-2004, the total IHSS program budget will be $3.2 billion ($15.8 million General Fund) compared to $2.8 billion ($1.1 billion General Fund) in 2002-2003. The budget reflects a 14 percent increase in one year.



The IHSS program's rate of growth has been fueled by two factors: increased caseload and higher provider rates. Demographic trends have increased and will continue to increase the number of eligibles. Wage increases have also contributed to caseload growth as higher wages have made it easier for beneficiaries to hire providers and fully utilize the program. IHSS cases increased 38 percent from 1995 to 2001. This rapid growth is expected to continue in the future, given demographic and utilization trends. Caseload is estimated to average 320,622 per month in the budget year, an increase of 7.8 percent over the current year.



Recent Program Changes

Effective January 2003, the state requires that counties act as or select an employer of record for IHSS providers. A total of 53 counties have established public authorities to meet the employer of record mandate and collectively bargain with IHSS workers. An additional county will establish a public authority by the end of the budget year. The budget assumes that providers working for a Public Authority will serve over 90 percent of the caseload in the budget year.

Current state law provides that the state share in provider rate increases above the state minimum wage in Public Authority and non-profit consortium counties. The state participates in provider wages up to $9.50 and individual health benefits up to $0.60 per hour. For subsequent years, the law requires that the state participate in total wages and individual health benefits up to $12.10 per hour, not to exceed $1.00 per hour increase in any fiscal year, when general fund revenues meet specified targets. The budget proposes suspension of the IHSS wage increase for the budget year. It also proposes realignment of the IHSS program to counties, and presumably ends the state participation in IHSS wage increases.

Issue

Proposed realignment of the IHSS program.

The budget proposes to realign the In-Home Supportive Services Program to counties and requires counties to fund 100 percent of non-federal program costs. Prior to the first realignment, IHSS was principally funded through state sources with minor federal block grant funding. Counties bore approximately two percent of the total cost. In 1991, counties became responsible for 35 percent of the non-federal cost. The 1993 creation of the Personal Care Services Program (PCSP) brought in federal funding for this program totaling $1.2 billion in fiscal year 2002-03. The budget calls for counties to fund 100 percent of the non-federal cost of this program.

Realignment of this program may be technically feasible, however it runs contrary to recent legislative initiatives, such as state participation in IHSS wage increases, and is substantively complicated. There also is a significant difference between the projected rate of growth for the program and for the proposed county funding sources. The Legislature may wish to consider how this program operate when realigned, whether realigning this program is consistent with recent Legislative initiatives, and the effect of realigning this program with a revenue source whose rate of growth is substantially less than the projected rate of growth for the program. The budget proposal lacks critical details governing how the IHSS program will operate once realigned. For example, the budget and its implementing legislation do not specify if and how the IHSS program will be modified. It is unclear whether counties will be given increased flexibility to restrict access to services or otherwise contain costs. It does not have the necessary parameters to assure available federal funds will be maximized through the PCSP program or requirement that ensure the IHSS Residual Program continue to exist. How will this proposal balance federal requirements that services be provided consistently across the state with the counties' need for flexibility? The Legislature may wish to consider how the IHSS program will be modified, what, if any, additional flexibility will be granted to counties and how realignment will affect the ability of low-income aged, blind and disabled individuals to access services.

Child Welfare and Foster Care

The Foster Care program provides support payments for children in out-of-home care, including foster homes, foster family agencies, residential treatment for seriously emotionally disturbed children and group homes. The caseload for foster care is estimated to be 75,000, a decrease of 1.2 percent. In addition, the Adoption Assistance program provides subsidies to promote the placement of hard-to-place adoptive children. The caseload is expected to be 61,000, an increase of 12 percent over current year. Finally, the Kin-GAP program provides support to children in long-term stable placements with relatives. The projected caseload is 16,000 children, reflecting an increase of 24.1 percent.

Children's Services includes Child Welfare Services (CWS) to provide programs to protect children from abuse, neglect and exploitation. Programs include Emergency Response, Family Maintenance, Family Reunification and Permanent Placement. Adoptions Services provides adoption services through state and county agencies. Child Abuse Prevention services provides grant funds to local agencies for prevention and intervention. These programs spend $2.2 billion total funds for local assistance.

The significant fiscal and programmatic issue currently facing the CWS program is the new federal outcome monitoring system required by the Adoptions and Safe Families Act. California has had its first audit which included a review of whether California protects children from abuse and neglect, keeps children safely in their homes whenever possible, and provides children appropriate services to meet their needs. The federal audit concluded that California is not operating in substantial conformity in all evaluated outcome areas and five of the seven evaluated factors. California now has to negotiate a Program Improvement Plan (PIP) with the federal government. The plan will outline what steps California will take to improve its outcomes and must include timeframes for achieving improvement. The federal findings strongly suggest that the PIP will require new investments into the CWS program.

Issue

<u>Realignment of the Foster Care Program, Kin-GAP, Adoption Assistance and Child Welfare Services</u>
The budget realigns the Foster Care Program, Kin-GAP, Adoption Assistance, and Child Welfare Services. All of these programs are currently administered by counties and require a county share-of-cost.

Programs	Current County Sharing Ratio	Realignment County Sharing Ratio
Foster Care Grants	60%	100%
Foster Care Administration	30%	100%
Kin-GAP	50%	100%
Adoption Assistance	25%	100%

Caseload growth varies across the programs. The Kin-GAP program is experiencing the most rapid growth at a rate of 24 percent in the current year. The Foster Care Program has experienced a caseload decline. This trend may change as historically the Foster Care Program rate of increase and decline has been precipitous and unpredictable. The Adoptions Assistance program caseload is expected to increase by 12 percent in the budget year. Generally, expenditures for the aforementioned programs have recently increased.

The Foster Care Program, Adoption Assistance, and Child Welfare Services are facing different kinds of challenges and developments likely to alter program operations. For example:

- A 1999 workload study found that social worker caseloads in California are excessively high for minimal levels of case management for vulnerable children and families. The optimal caseload standards are half of the current budgeting standards. As a result of this study, the state provided moderate increases to support workload relief. This funding was reduced in the current year and is proposed for realignment in the budget year. The current staffing levels compromise the ability of social workers to do their job and will likely have a negative impact on California's ability to meet the new federal performance standards.

- The Adoption Assistance Program is adapting to a new emphasis on expediting and increasing the number of adoptions. Recent federal legislation will likely reinforce these trends, as it requires courts to expedite the termination of parental rights after a shorter reunification period. The federal Adoptions and Safe Families Act created a new outcomes accountability system, which threatens sizable penalties for states that do not meet or show significant improvement towards meeting the new federal outcomes. The new federal outcomes include timely establishment of permanent situations for foster children.

- The Foster Care Program, among other challenges, is facing a serious shortage of providers, particularly foster family homes and intensive treatment facilities for seriously troubled children.

Realignment of these programs may be technically feasible, however, it is substantively complicated. The Legislature may wish to consider the proposed realignment in light of the impending changes to the Child Welfare Services system. The budget proposal lacks critical details governing how the programs will operate once realigned. For example, the budget and its implementing legislation do not specify how state oversight of the realigned programs will work. It is unclear whether counties will be given increased flexibility to significantly alter programs, to restrict access to services or otherwise contain costs. The budget does not specify if counties will have expanded program authority or whether the programs will essentially operate as crafted in state and federal laws. How will the proposed realignment balance federal requirements that services be provided consistently across the state and that there be a single administering agency with the counties' need for flexibility? The Administration may wish to clarify how these programs will be modified as a result of realignment, what, if any, additional flexibility will be granted to counties and how realignment will affect access services. The Legislature may wish to consider how it can structure realignment in a manner that assures appropriate state oversight and compliance with federal requirements. How will the state ensure counties comply with state and federal requirements when it will provide no funding for the child welfare system?

Independent Adoptions Program

The Independent Adoptions Program facilitates adoptions when an agreement has been reached between birth and adoptive parents. Essentially the Department of Social Services (DSS) serves as the investigative arm of the Court and makes a recommendation to approve or deny a petition for adoption. As part of the investigation, the DSS adoption specialist, within a specified timeline, completes a safety and welfare check, interviews petitioners and all persons required to consent to the adoption, and conducts a full investigation to assess the appropriateness of the adoption.

Issue:

<u>Proposed elimination of the Independent Adoptions Program</u>
The budget proposes to eliminate this program to realize savings of $2.8 million.

The Legislature may wish to consider the impact of this proposal on the rate in which children are adopted in California. Specifically, the Legislature may wish to consider the differences between individuals served by this program and those served by private adoption agencies, the varying costs of alternative adoption processes, and feasible alternatives to the state program that assure an efficient adoption system in California comprised of alternative adoption models. The Legislature may wish to consider alternatives such as increasing the fees paid by program participants to support the program's continuation.

Adult Protective Services

The Adult Protective Services (APS) program serves adults who may be victims of abuse or neglect in their homes or in community care facilities. The program is overseen by the Department of Social Services and administered by the counties. Legislation in 1998 created the current statewide system. The Legislation expanded the categories of people required to report suspected abuse, and defined the types of abuse required to be reported. It also required counties to provide emergency response systems, emergency shelter and food, and in-home protective services to elderly and dependent adults in danger of or known to be abused, neglected or exploited. The law established a county maintenance of effort (MOE) requirement of $11 million, which represents the amount counties were spending on services prior to 1998.

Funding for the program increased in the years following enactment of the 1998 reforms. Total funding since 1999-00 has remained relatively stable until fiscal year 2002-03, when the program's general fund contribution was decreased by $5.6 million. According to county estimates, current program funding is $15.6 million less than needed to provide mandated services. Total program expenditures are $72.2 million in the budget year. The average monthly caseload is estimated to be 14,200 persons, slightly decreased from the current year.

Issue:

Realignment of the Adult Protective Services Program
The Adult Protective Services Program is proposed for realignment to the counties for general fund savings of $50.2 million. Realignment of this program may be technically feasible. However, the current proposal lacks critical details regarding how the program will work when realigned. For example, the budget and its implementing legislation do not specify whether counties will be given increased flexibility to significantly alter programs, reduce services, limit required activities or otherwise contain costs. The budget does not specify if counties will have expanded program authority or whether the program will essentially operate as crafted in state law. The Administration may wish to clarify how these programs will be modified as a result of realignment, what, if any, additional flexibility will be granted to counties and how realignment will affect service delivery.

Community Care Licensing

The Community Care Licensing Division (CCLD) of the Department of Social Services is responsible for licensing over 85,000 community care facilities across the state. These facilities have the capacity to serve over 1.4 million clients requiring different types of care and supervision. Licensees include childcare facilities, certified family homes, foster family agencies, residential care facilities for the elderly, residential care facilities for the chronically ill, adoption agencies, transitional housing and adult day care. Currently, the CCLD is required to visit licensees on an annual or triennial basis to ensure compliance with health and safety requirements. The budget reduces CCLD funding by $7.5 million and proposes significant revisions to the licensing methodology to realize the proposed savings.

- Eliminates requirement that licensees be visited annually or triennially.
  The budget proposes to eliminate the requirement that licensees be visited annually or triennially and instead require the department to visit annually the following facilities:

  1. Facilities owned or operated by a licensee on probation or against whom an accusation is pending;
  2. Facilities subject to a plan of compliance requiring an annual inspection;
  3. Facilities subject to an order to remove a person from a facility;
  4. Facilities that require an annual visit as a condition of federal financial participation such as facilities serving developmentally disabled clients.

  All other facilities would be subject to an annual inspection based on a 10 percent random sampling method. The department will continue to visit on an annual basis a limited number of facilities if 10 percent of those facilities does not represent a statistically significant sample. The department will also continue to investigate all complaints and conduct legally required visits.

  The proposed changes to current annual and triennial visit requirements will result in 20% of licensees being visited every year. However, there is no requirement that licensees be visited at least once within a set time period. The Legislature may wish to consider the effect of this proposal on health and safety and may want to consider requiring that all facilities be visited at least once within an established time period.

- Transfers the responsibility for investigating less serious complaints lodged against certified family homes to licensed foster family agencies. Recent legislation transferred the responsibility for investigating complaints lodged against certified family homes from licensed foster family agencies to the DSS. The proposed transfer reverses the recently enacted legislation.

The Legislature transferred the responsibility to investigate complaints to the department in part because of concerns regarding a potential conflict of interest for foster family agencies that investigate complaints against certified family homes. Foster family agencies (FFA) contract with or operate certified family homes and are responsible for placing youth in these homes. Given this relationship and general shortages of providers, FFAs may be reluctant to investigate a complaint that may result in the loss of one of their providers or partners. The Administration may wish to provide specific information to appease concerns regarding the possible conflict of interest for FFAs and to assure this proposal does not compromise health and safety.

- Increases fee revenue to support the CCLD**.**
  The budget and implementing legislation propose to increase licensing fees to provide non-general fund support of the CCLD. The budget doubles license fees for childcare centers and family child care homes, eliminates aggregate fees for childcare centers, introduces fees for foster family agencies based on the number of certified family homes they operate, and increases fees for residential facilities and adult day care by 25 percent. The state is the principal client or primary payer of services for most facilities that will be effected by the proposed increases. The Administration may wish to consider the potential pressure for higher reimbursement rates that may result from increased licensing fees and the impact of the fee increases on the availability of program providers.

LABOR

0559 Secretary for Labor and Workforce Development Agency

The secretary is a new cabinet-level appointment authorized by SB 1236, and effective January 1, 2003. The secretary will be responsible for coordinating and enforcing labor law in the state. The new Workforce Development Agency includes the Employment Development Department, Department of Industrial Relations, Workforce Investment Board, and the Agricultural Labor Relations Board.

The budget proposes an appropriation of $2.3 million for the first full year of the agency. The agency has 16 personnel years.

Issue

Update on Start-Up. The agency began functioning under the terms of the Governor Reorganization Plan Number 1 (2002) on July 2, 2002. As such, the Secretary and his staff will have had some experience running the agency. The subcommittee may wish to pursue these questions:

- All new agencies experience transition difficulties in their first year, even if there is not a major deficit and hiring freeze imposed. What difficulties has the agency had during its start up? Will it need changes to its statutory authority?
- The agency has specific statutory duties. What are the agency's plans for meeting the statutory duties? Does the agency have goals for meeting its statutory responsibilities? How will it know if it is successful in meeting its statutory duties?

7100 Employment Development Department

The Employment Development Department (EDD) links employers and job seekers. The department provides services through four main functions: (1) employment-related services; (2) tax collections and benefit payments; (3) employment training programs; and (4) Workforce Investment Act activities. The Governor proposes a budget of $10.6 billion ($21.5 million General Fund), an increase of 17.9 percent over the current year.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$22,898	$21,550	-$1,348	-5.8
EDD Contingent Fund	18,751	17,888	-863	-4.6
Employment Training Fund	83,867	75,313	8,554	-10.1
Welfare to Work Fund-Federal	3,608	0	-3,608	-100.0
Disability Fund	3,472,701	3,590,935	118,234	3.4
Consolidated Work Program Fund	631,931	582,166	-49,765	-7.8
Unemployment Administration-Federal	618,659	602,316	-16,343	-2.6
Unemployment Fund-Federal	7,998,753	5,662,509	-2,336,244	-29.2
School Employees Fund	84,416	57,560	-26,856	-31.8
Reimbursements	24,928	25,040	112	.4
Total	$12,960,512	$10,635,277	-$2,325,235	-17.9

Employment Related Services. The program facilitates a match between employers' needs and job seekers skills. Services are delivered through California's One-Stop Career Systems.

Highlights

- ***Data Collection***. The budget directs the department to consult with researchers, employers groups, labor organizations and other state agencies on the feasibility of collecting additional data from employers. The department will report to the Legislature by December 31, 2003. The department also will assess and report on the capability of and cost of enhancements for the current database system, cost of revising forms and/or questionnaires, personnel costs for collection and inputting the data, and additional time required to collect, input and process the additional data collected.

- ***Continuation of Reed Act Funds for the Job Service Program.*** The budget continues $25.1 million in federal Reed Act funds in 2003-04 for the Job Services Program. In 2002-03, these funds were reduced from EDD's Contingent Fund and were replaced by Reed Act funds.

- ***Continuation of Reed Act Funding for Unemployment Insurance Administration.*** The budget appropriates $15.4 million in Reed Act funds to replace the discontinued Special Reed Act distributions formerly used to augment federal Unemployment Insurance funding.

- ***Trade Adjustment Assistance (TAA).*** The budget proposes $17,049,000 (Unemployment Administration Fund) and the establishment of 27.4 personnel years (temporary help). The additional funds would help the department to access full federal TAA funding.

- ***Restoration of State Funding for Benefit Audit Fund***. The budget appropriates $9.3 million (Reed Act funds) to fund benefit audit activities. A one-time Reed Act appropriation was used for this purpose in the current year in 2002-03.

Tax Collection and Benefits. EDD administers this program to form monetary relief to individuals who undergo periods of unemployment or temporarily disability. This program contains two systems; the Unemployment Insurance (UI) program and the Disability Insurance (DI) program. These systems are based upon insurance principles, with the employer and employee paying tax contributions to funds that provide benefits. The system includes the following activities: collecting taxes, determining benefit eligibility based upon claims, managing caseloads, processing payments to claimants recovering overpayments, and disputes involving claims or tax liabilities.

Employment Training Programs. EDD administers the Employment Training Tax from employers who participate in the Unemployment Insurance system, and uses the funds in performance-based contracts to provide training to unemployed workers in high-wage, high-skill jobs, and to retrain incumbent workers in businesses challenged by out-of-state competition. EDD administers federal Welfare to Work funds from the Department of Labor, providing transitional assistance for recipients of CalWORKs. EDD coordinates the Workforce Investment Act, which provides federal funds for Adult Employment and Training, Youth Activities and Dislocated Workers Employment and Training. The majority of these funds are administered through local Workforce Investment Agencies; up to 15% is reserved for discretionary projects at the statewide level.

Highlights

- **Employment Training Fund.** The budget includes an unallocated redcution of $612,000 and 11.0 personnel years .

- **Workforce Investment Act (WIA). The budget proposes to fund** through three programs: Adult Employment and Training, Youth Activities, and Dislocated Workers Employment and Training. Adult Employment and Training provides universal core services to all adults, plus training and other services to economically disadvantaged adults facing serious barriers to employment. Youth Activities provide economically disadvantaged youth with training and other services to prepare them with the skills necessary to obtain unsubsidized employment, completion of secondary or post-secondary education, entrance to military services or qualified apprenticeship. Dislocated Workers Employment and Training provide rapid response services to workers affected by plant closures and layoffs and provides training and other services.

7120 State Workforce Investment Board

The Workforce Investment Board directs the implementation of the Workforce Investment Act. The Board assists the Governor with developing and modifying the five-year Workforce Investment Plan, designating Local Workforce Investment Areas, establishing Local Workforce Investment Boards, reviewing Local Workforce Investment Areas Plans, providing oversight of local workforce education and training programs, and negotiating performance standards with the Department of Labor.

7300 Agricultural Labor Relations Board

The Agriculture Labor Relations Board (ALRB) collects secret ballot elections to determine collective bargaining representation in agriculture and for investigating and resolving unfair labor practice disputes. The ALRB is divided into two major programs: (1) Board Administration of the Agricultural labor Relations Act; and (2) General Counsel Administration of the Agricultural Labor Relation Act. Recent legislation, Senate Bill 1156 and Assembly Bill 2596, add the Agricultural Employer-Employee Collective Bargaining and Mediation Law to the Labor Code effective January 2003. The legislation requires the board to mediate certain collective bargaining agreements.

Issue

The budget provides no increased funding to implement SB 1156 and AB 2596. Can the board implement the legislation within its existing resources?

7350 Department of Industrial Relations

The Department of Industrial Relations (DIR) is intended to protect the workforce, improve working conditions, and advance opportunities for profitable employment. The department has three major programs: The adjudication of workers' compensation disputes, the prevention of industrial injuries and deaths and the enforcement of laws relating to wages, hours and working conditions.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$125,097	$63,278	-$61,819	-49%
Special Funds	81,890	77,489	4,401	18
Workers' Compensation Administration Fund	45,689	103,702	58,013	127
Total	$252,676	$244,469	-$124,233	-31%

Highlights

- **Implementation of AB 749.** AB 749 increases workers' compensation benefits and requires reforms in the administration of the program. DIR seeks a budget augmentation of $9.3 million to implement the provisions of AB 749.
- ***Increase User Fees for Workers' Compensation Program.*** The budget eliminates General Fund support for the Workers' Compensation Division, for a General Fund savings of $24.6 million in 2002-03 and $73.7 million in 2003-04. The General Fund support is replaced with revenue from a fee imposed on employers. To implement this provision, the Administration proposes a statutory law change to increase the fees.

Issues

"User Fee" Could Be Controversial. The Administration proposes a significant increase in the fee imposed on employers for the workers' compensation program. The proposal would raise employer costs by $24 million (half year) in the current year and $70 million in the budget year. The fee proposal was introduced in the First Extraordinary Session, as SB 10x, but was not taken up when the Senate considered the December Revision. If the fee increase is not approved but the Legislature does not augment the budget with General Fund money, what will the department do to close the $70 million hole in its workers' compensation division?

AB 749 Implementation. The Legislature augmented the department's budget last year to begin the implementation of the bill. Although the Governor vetoed aspects of the augmentations, he did agree to begin implementation. As a result of the veto, certain aspects of the implementation of AB 749 were deferred until 2003-04. Now, however, because the December Revision deferred the start-up of AB 749 in the current year, it is not clear what aspects of the AB 749 mandates can be implemented in the budget year. For example, where there policy and fiscal implications of deferring implementation for another year? Can the Legislature do anything in the budget year to expedite full implementation in the budget year?

VETERANS' AFFAIRS

0553 Office of the Inspector General for Veterans' Affairs

The inspector has responsibility for reviewing the operations and financial condition of the state's veterans' programs, including the State Farm and Home Purchase Program ("Cal-Vet") and the veterans' homes. The budget falls from $514,000 in the current year to $457,000 in the budget year, a 14 percent reduction.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$423	$358	-$65	-15.4%
Special Funds	$91	$99	8	8.8
Total	$514	$457	-$73	-14.2%

Issue

Meeting the Office's Statutory Mission The inspector has testified that he cannot meet his statutory mandates for independence and oversight at the funding level provided over the last two years.. Now that the office is sustaining another large reduction, the Legislature should consider ways to either augment the inspector's resources or limit his statutory responsibilities.

8955 Department of Veterans' Affairs

The Department of Veterans' Affairs (DVA) provides services to qualified veterans and eligible members of the National Guard. Specifically it:

- Assists eligible veterans and their dependents in obtaining federal and state benefits.
- Makes below-market loans to qualified veterans for homes and farms. The loans made through the California Veterans Farm and Home Purchase Program (the "Cal-Vet program") are capitalized from the proceeds of revenue bond sales.
- Operates veterans' homes in Yountville (Napa County), Barstow (San Bernardino County), and Chula Vista (San Diego County). The homes provide medical care, rehabilitation, and residential home services.

The budget reduces total expenditures from $336 million in the current year to $328 million.

Highlights

Restoration of Domiciliary Member Fees to 55 Percent. The budget increases the monthly member fee from 47.5 percent to 55 percent. Until 2001, the fees had been 55 percent, but were reduced at the request of veterans. The fee increase raises $1.2 million. By increasing the member fee, the department reduces its reliance on the General Fund by a comparable amount.

Disabled Veterans Business Enterprise. The budget shifts the outreach program from the Department of General Services to the Department of Veterans Affairs. Consistent with this change, DVA's reimbursements increase by an amount to cover the full cost of the new responsibilities.

Issues

Member Fee Increase. The fee increase is scheduled to be imposed on July 1**.** By the time members are admitted to the home, most if not all are on a fixed income. It is not clear to what extent members can afford the fee increase, particularly given the short notice provided them.

Cashflow Report. The department has experienced significant cash management problems, and has sought short term loans to manage its budget. In recent years, the department has been unable to repay the loans. To help the Legislature monitor the department's cashflow, the Legislature required the department to report on cashflow twice yearly. The first report was due two months ago, but has not been submitted to the Legislature. Without the report, it is not clear if the department is managing its cashflow in the current year and whether the department will repay any of the loans due this year. More importantly, to the extent the department is experiencing cash management problems, the Legislature cannot properly respond to problems if the department fails to provide adequate information.

Report on Lags in Billings. The department has had difficulty securing reimbursement for the health services it renders. Some of the difficult arises because the department has been late in making claims to insurance companies and the federal government. The department knows that as an account ages, the likelihood of collecting falls. In the recent past, the department has had significant lags in making claims. The Legislature, as a condition of appropriating funds for the homes, asked the department to report on its progress in making timely claims. The report is late. Although department staff have said that DVA is making progress in reducing billing lags, the Legislature cannot adequately assess the progress without the required report.

SUBCOMMITTEE NO. 4

TRANSPORTATION, PUBLIC SAFETY, and STATE ADMINISTRATION

Transportation

State Administration

Judiciary and Criminal Justice

TRANSPORTATION

OVERVIEW

Governor's Transportation Financing Proposal Still Lacks Detail and Information

As part of the 2002-2003 mid-year revision, the Governor proposed various fund shifts and transfers from transportation to the General Fund. In total, the Governor's re-financing proposal identified nearly $1.8 billion from transportation. However the majority of these savings were based primarily on budget-year actions, and not all savings were attributable to the General Fund. Key provisions of the proposal included the following:

- Suspend the $1.05 billion transfer of the sales tax on Gasoline from the General Fund to the Transportation Investment Fund (TIF) for the 2003-04 fiscal year. The result of this action will eliminate $678 million from the TCRF, $147 to the State Transportation Improvement Program (STIP), $147 million for local streets and roads, and $74 million to the Public Transportation Account.
- Cancel the $500 million General Fund loan repayment to the TCRF scheduled for the 2003-04 fiscal-year.
- Transfer $100 million from the TCRF balance to the General Fund.

Prior to the start of the 1st Extraordinary Session this year, Senate policy and fiscal staff prepared an analysis of the mid-year transportation proposals. Focusing on the TCRP items, staff identified numerous issues that needed to be resolved before the subcommittee could make an informed decision regarding these proposals. Specifically, staff identified issues with the overall lack of detail and intent regarding the future of the TCRP. As discussed in later in this analysis, the Administration indicated its desire to merge the TCRP with the STIP, thus eliminating the TCRP all together. Subsequently staff recommended that the Senate defer action on all budget-year items until the Administration provided a more detailed and thorough proposal.

The Governor's 2003-04 Budget, released on January 10, does not address the issues and concerns staff identified for the members. It is clear that no further information, nor detail will be provided for the TCRP/TIF proposals. The Administration states that their plan is to have the Transportation Commission (CTC) work with locals to identify and re-prioritize TCRP and STIP projects. The following analysis highlights the weaknesses of this approach.

<u>TCRP or STIP Projects will not Receive Funding</u>
A major component of the Governor's proposal is to shift administrative responsibility for the Traffic Congestion Relief Program (TCRP) from Caltrans to the Transportation Commission (CTC). Although the Administration has not provided trailer bill language that specifies how the CTC will administer the TCRP, the Administration proposes to shift the TCRP projects into the STIP. Based on the limited

information provided to the Legislature at the time this analysis was prepared, the Governor's proposal will result in a $1.5 billion reduction to the TCRP. (See Appendix A for background/history of the TCRP). Additionally, **<u>the Administration has not identified a revenue stream to fund both STIP and TCRP projects</u>** if this proposal is approved.

The TCRP authorized $4.9 billion for 159 specific projects over a 5–year period. If the TCRP projects are to be incorporated into the STIP, the Regional Transportation Planning Agencies (RTPAs) will have to prioritize TCRP projects in relation to their existing STIP projects. Given the status of the State Highway Account (discussed further in the next section), and the anticipated reduction of federal funds, the STIP cannot absorb the commitments made in the TCRP. A likely scenario will require the RTPAs to reconfigure their Regional Transportation Improvement Programs (RTIP; local portion of the STIP) and determine which projects to continue funding and which projects to defer or eliminate altogether.

<u>Transportation Revenues are Down, and Expenditures Have Increased</u>
State and federal revenues for the STIP are significantly lower than projected in the 2002 STIP fund estimate. According to new estimates released by Caltrans to the CTC, the STIP is projected to have a $4 billion cash shortfall over the next five years. The projected cash balance in the SHA for the current fiscal year is a $173 million shortfall. The SHA deficit increases to $634 million for the 2003-04 fiscal year.

The STIP revenue reduction can be attributed to the following factors:

- Projected $566 million federal Revenue Aligned Budget Authority (RABA) funding increase over the next five years will not occur.
- Anticipated 20 percent increase in federal funds for the 2003-04 fiscal year will not occur. Caltrans estimates a $600 million total reduction of Federal revenues.
- Loss of truck weight fees due to the implementation of SB 2084. The new truck weight fee system was intended to be revenue neutral. However, Caltrans projects an annual revenue reduction of $163 million beginning this fiscal year.
- Lower TIF transfer as a result of gasoline sales tax revenue decline. (Approximately $74 million lower in 2003-04).

Annual expenditures from the State Highway Account have increased significantly in response to efforts to speed the delivery of capital projects and reduce the traditionally high cash balances in the SHA. During the 2001-02 fiscal year, SHA expenditures exceeded account revenues by approximately $1 billion. Expenditures are projected to exceed revenues between $500 million and $1 billion annually over the next three years because of the continuing emphasis on accelerated project delivery.

<u>Transportation Impacts</u>
The Governor's budget revision has already had an effect on the TCRP and the STIP. The CTC on December 12, 2002 voted to suspend all new financial allocations for projects in the TCRP and the STIP at least until February 2003. Projects which earlier were given allocations and are in various stages of completion have been put in limbo.

Short Term Effects: The proposed loss of gasoline sales revenues and the related loan forgiveness to the TCRP has resulted in the CTC's December action to freeze project funding allocations for two months. This action has delayed 64 funding allocations. This, in turn is forcing local transportation agencies to ponder whether to sign pending contracts, order rail and other equipment or make other binding current year and future commitments. Agencies do not know whether or when funding might resume for projects in progress. Local agencies fear contractor lawsuits if funding is delayed or curtailed for projects under contract or those where preliminary work or resource marshaling has begun.

The Governor's transportation proposal is, in a technical sense, heavily-weighted toward the 2003-04 budget-year. However, the short-term effects are real and significant, as in the above-described project allocation freeze. The proposed funding suspension not only involves funds for the Traffic Congestion Relief Program, but the resulting allocations freeze is across the board and includes STIP projects, too.

Longer Term Effects: The loss of the sales tax revenues in the Budget Year will leave the TCRP approximately $1.5 billion short of the funds needed for the approved, and statutorily – endorsed, congestion relief projects. This is equivalent to approximately 25% of the funds promised for the program over its six years. The Governor's Proposal suggests that these underfunded projects should compete with other approved state and local transportation projects (in the STIP). Essentially, the situation would be one of too many projects chasing too few dollars.

The competition for remaining funding between TCRP and STIP projects would require the delay and/or abandonment of numerous transportation projects, especially in greater Los Angeles and the Bay Area, due to the concentration of TCRP projects in those two regions. The Department of Transportation and regional transportation agencies would have to reconstitute their respective transportation programs, either formally or informally. Project delays would increase the projects' ultimate costs while project abandonment would impede statewide mobility and increase congestion. The state would fall further behind in its attempts to maintain and expand the transportation infrastructure.

Legislative Options

These proposed reductions come at a time when transportation revenues are already below projections. As previously mentioned, the SHA has a projected cash shortfall of $173 million in the current fiscal year and a $634 million shortfall in the 2003-04 budget-year. The Legislature needs to address the financial status of the highway account even without funding issues posed by the Governor's refinancing proposal.

The Governor's budget revision proposals have thrown a cloak of uncertainty over both the Traffic Congestion Relief Program (TCRP) and the State Transportation Improvement Program (STIP). While the administration has suggested that it intends to fold the TCRP projects into the STIP, it has proposed neither a trailer bill to achieve that objective nor a revenue source to fund all of the projects demanding revenue.

For the Legislature to consider meaningful alternatives to the Governor's mid-year proposals, the Administration must articulate their intent with respect to the future of the Transportation Congestion Relief Plan (TCRP) and the fiscal instability and deficiencies of the current STIP.

The following are issues and options for the Legislature to consider.

Is the administration's proposal to reduce funding to the TCRP a one-time action, or is the proposal part of a broader effort to repeal the TCRP entirely and require regional agencies to fund TCRP projects on their own and through the STIP process?

Staff Comment: If the proposal is a one-time reduction, the Legislature could simply modify the Governor's proposal by allowing the reduction now and requiring the General Fund to pay back the amount reduced at a future date (essentially extending the timeframe for the TCRP). If the proposal is to repeal the TCRP, see number 2 below.

Given the current condition of the State Highway Account (SHA), the STIP cannot absorb the TCRP projects. Therefore, will the administration propose additional resources to fund those projects? If not, numerous TCRP projects will simply go without funding and will have to be delayed or cancelled.

Staff Comment: The Legislature approved the TCRP projects in statute. To the extent that Members want to see the projects continue, they may wish to consider additional sources of revenue to fund the projects (e.g., statewide gas tax, regional gas tax, allow local to raise their own transportation revenues with a majority vote, etc.).

Will the administration propose to suspend the gasoline sales tax transfer from the General Fund to the Transportation Investment Fund over more than one fiscal year?

Staff Comment: If the administration proposes to suspend the gasoline sales tax transfer indefinitely as suggested, the condition of transportation funding will significantly diminish. While the General Fund would benefit from this action, over $1 billion in annual funding would be lost for TCRP and STIP projects, local street and road maintenance, and transit operating and capital investments.

A broader issue to consider is the transportation sector's partial reliance on gasoline sales tax revenues from the General Fund. Notwithstanding the constitutional dedication of these funds to transportation, General Fund appropriations for transportation will likely be targeted for reductions as this budget crisis continues and future crises emerge. Policymakers should consider whether the volatility and vulnerability associated with this financing structure—and the project casualties and delays caused by constant funding instability—is an acceptable situation. Members may wish to consider adopting more stable sources of transportation funding that would not rise or fall based on the General Fund's condition. Options could include looking at traditional transportation user fees or assisting local governments in raising their own transportation revenues.

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2660 Department of Transportation

The Department of Transportation (Caltrans) constructs, operates and maintains a comprehensive state system of 15,200 miles of highways and freeways and provides intercity passenger rail services under contract with Amtrak. The state highway system comprises less than 9 percent of the total roadway mileage in California but handles approximately 54 percent of the miles traveled. The department also has responsibilities for congestion relief, transportation technology, environmental and worker protection, and airport safety, land use and noise standards. Caltrans' budget is divided into six primary programs: Aeronautics, Highway Transportation, Mass Transportation, Transportation Planning, Administration, and the Equipment Service Center.

The budget proposes total expenditures of $6.4 billion, a decrease of $673.5 million (9.5 percent) from the current-year budget. .

Issue

Department Proposes to Eliminate Significant Number of Positions

Caltrans proposes to eliminate a total of 1845.9 positions (1344.9 personnel years) in the 2003-2004 budget-year. Specifically the department proposes the following position reductions:

• Expiring limited-term positions	-105.7
• Expiring limited-term transportation permit positions	-15
• Reduction in enhanced services to locals positions	-30.5
• Elimination of Traffic Congestion Relief Program (TCRP) Positions	-1,223.7
• Position reduction through attrition to generate State Highway Account savings	-471

The Governor states in the budget summary that the positions associated with the TCRP are being eliminated due to the uncertainty surrounding the program. The 1,223.7 TCRP positions were authorized when the TCRP was created in statute. Since the Administration's proposal is to re-prioritize TCRP projects with the STIP, Caltrans is anticipating a decrease in workload demand in the likely scenario that TCRP projects are not carried forward. Essentially the proposal to eliminate the TCRP positions presumes the decision to delete funding for the TCRP projects in the budget-year and possibly beyond.

The Administration has declared that is committed to restoring the level of positions needed to deliver high-priority TCRP projects if alternative financing is identified to continue funding the TCRP projects, or transportation agencies reprioritize projects within their regions to retain such projects.

The subcommittee will not have the official proposal until the department submits the Capital Outlay Support (COS) finance letter prior to the May revision. Caltrans has to establish its capital outlay workload demand for the upcoming budget-year in order to determine its staffing needs. This process has put the Legislature in a position of having to make difficult decisions regarding state staff and contracting out positions in a very limited time frame. The subcommittee on average has less than one week to approve, modify, or deny the Administration's COS budget proposal.

In light of the department's unofficial proposal to eliminate 1223.7 positions from the TCRP, and the likely reductions in the COS staffing budget, staff will recommend the subcommittee deny all position reduction proposals. By the time Caltrans' budget is heard on April 23, staff recommends the Subcommittee request that Caltrans and Finance provide the 2003-04 COS budget proposal, including all documentation used to establish the COS budget.

2665 High-Speed Rail Authority

The California High-Speed Rail Authority (HSRA) was created by Chapter 796, Statutes of 1996, to direct development and implementation of inter-city high-speed rail service that is fully coordinated with other public transportation services. The HSRA is required to prepare a plan for the financing, construction, and operation of a high-speed network for the state that would be capable of achieving speeds of at least 200 miles per hour. The HSRA has completed its business plan, initial finance plan, and currently is completing an initial program EIR and related technical studies.

Issues

Uncertain Future of the HSRA

The Administration proposes to consolidate the HSRA with Caltrans, beginning in the 2003-2004 budget-year. As stated in the Governor's budget summary, the Administration seeks to "bring the transportation expertise of Caltrans to the high-speed rail project." If approved, the HSRA board would continue to exist, but Caltrans staff would assume responsibility for support and administration of the program. This proposal could provide as much as $589,000 (thousand) in special fund(s) savings.

Caltrans rationale for eliminating the HSRA is that the department has both experience and knowledge with rail capital projects through the Mass Transportation program and the partnership with Amtrak. However, the decision to designate Caltrans as the lead agency for the high-speed rail project does raise questions, including whether the department has relevant expertise or experience with "high-speed" rail issues.

First, given the department's notorious track record with project delivery, is it wise to have Caltrans assume the lead on a project that is arguably the biggest public works project in California over the past 40 years?

Second, the timing of this proposal is questionable. Senate Bill 1856 (Costa, Chapter 697, Statutes of 2002) authorizes a $9.95 billion bond measure on the ballot in 2004 to help fund the planning and construction of the high-speed rail passenger system. How will the Administration's proposal affect the long-term viability of the program? Could eliminating the HSRA jeopardize the passage of the high-speed rail bond?

Given some of the policy concerns with the Administration's proposal, the fiscal and policy committees should try to resolve these issues before taking action on this item.

2740 Department of Motor Vehicles

The Department of Motor Vehicles (DMV) regulates the issuance and retention of drivers' licenses and provides various revenue collection services. The DMV also issues licenses and regulates occupations and businesses related to the instruction of drivers, as well as the manufacture, transport, sale and disposal of vehicles.

The budget proposes total expenditures of $681.9 million, a decrease of $4.2 million (0.6 percent) from the current-year budget.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$1,598	$1,114	($484)	-30.3
State Highway Acct.	41,005	59,727	18,722	45.7
Motor Vehicle Acct.	355,297	389,272	33,975	9.6
New Motor Vehicle Board Acct.	1,703	1,708	5	0.3
Motor Vehicle License Fee Acct	269,609	213,079	(56,530)	-21.0
Motor Carriers Permit Fund	3,033	0	(3,033)	-100.0
Harbors and Watercraft Revolving Fund	2,066	4,503	2,437	118.0
Reimbursements	11,859	12,524	665	5.6
Total	$686,170	$681,927	($4,243)	-0.6

Highlights

Additional Fees Proposed to Protect the Motor Vehicle Account

The MVA is the primary funding source for DMV and the California Highway Patrol (CHP). Over the past few years program expenditures from the MVA have increased significantly while revenues to the account have remained relatively stable. Additional pressures have been put on the MVA as a result of CHP's homeland security responsibilities. The budget assumes $74.5 million in federal funds to offset these costs, however the MVA remains the fund source until the federal funds are available. In light of these issues, the Administration is proposing additional fees to help stabilize the MVA. Specifically the new and adjusted fees include the following:

		Amounts	
New MVA Fees for 2003-04	**Projected Revenues ($ in thousands)**	**Old Fee Whole Dollars**	**New Fee Whole Dollars**
Increase ID fees from $6 to $20 for non-seniors; seniors free	8,745	$6	$20
Activate Business Partner Automation Program fee and increase from $2 to $3	1,950	Authorized in current statute at $2.00 but fee has never been implemented.	$3
Increase Non-Commercial Driver's License fees, from $15 for five years to $24 five years.	30,100	$15	$24
Increase Vehicle Registration base from $28 to $31 and increase the two CHP $1 surcharges to $2 each - a total VR increase of $7.00	94,850	$28.00 base plus two $1 surcharges - totals $30	$31.00 base plus two $3 surcharges - totals $37
Standardize various transaction fees to $15.00	15,500	Existing fees range from $2.00 to $15.00	$15 each
New Public Safety Surcharge - to offset MVA expenditures	30,940	New surcharge, currently does not exist.	Up to 2% percent on intrastate telephone calls (0.25% for 2003-04).

These fees are expected to generate approximately $194 million in revenues for the MVA, and provide a 3 percent reserve in the account.

STATE ADMINISTRATION

LEGISLATIVE/EXECUTIVE

This section includes the budgets of constitutional officers, the Legislature, and agency secretaries. Departments with reductions or augmentations other than normal operating expenses or elimination of vacant positions are highlighted.

0650 Office of Planning and Research

The Office of Planning and Research (OPR) provides policy research for the Governor on land-use, growth planning issues and California Environmental Quality Act provisions. The budget proposes total expenditures of $54 million, of which $4.2 million is from the General Fund. This budget includes federal funding of $48.3 million for California's AmeriCorps program.

Issues

Cesar Chavez Day of Learning Grants. SB 984 (Polanco) of 2000 established Cesar Chavez Day as a state holiday for state employees and authorized school districts to establish a minimum day and provide one hour of instruction on the life of Cesar Chavez. The bill also appropriated annual grants of $5 million to engage school pupils in community service on Cesar Chavez Day. The program serves more than 300 schools statewide.

The December Revision proposed that the $5 million annual appropriation for Cesar Chavez Day of Learning Grants be reduced by $4,750,000 in 2002-03. In addition, the budget proposes suspending the grants for the 2003-04 through 2005-06 fiscal years.

0860 State Board of Equalization

The State Board of Equalization (BOE), the Franchise Tax Board (FTB), and the Employment Development Department are the state's major tax collection agencies. BOE collects state and local sales and use taxes and a variety of business and excise taxes and fees, including those levied on gasoline and diesel fuel, alcoholic beverages and cigarettes, as well as others. BOE also assesses utility property for local property tax purposes, oversees the administration of the local property tax by county assessors, and serves as the appellate body to hear specified tax appeals, including FTB decisions under the personal income tax and bank and corporation tax laws. The budget includes $321.4 million or 0.4 percent more than the current-year level.

Issues

Administration of the Cigarette and Tobacco Products Tax Program. The budget proposes to augment the budget to implement the pilot program in Chapter 881, Statutes of 2002, which requires BOE to replace the current cigarette stamps and meter impressions with encrypted stamps or meter impressions that can b e read by a scanning or similar device. The budget includes $294,000 ($34,000 GF) in the current year for implementation costs and $678,000 ($77,000 GF) in the budget year for on-going costs.

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0954 Scholarshare Investment Board

Issue

The Governor's Merit Scholarships provide $1,000 scholarship savings accounts to ninth through eleventh grade students based on their Stanford - 9 standardized test scores.

The Distinguished Math and Science Scholars Program provides $2,500 scholarships to those students who qualify to receive the $1,000 Governor's Merit Scholarships and who achieve the highest scores on advanced placement tests in calculus and either of the biology, chemistry or physics exams. Eligibility was expanded in 2001 to include students who took AP tests prior to January 1, 2000 and otherwise met test score criteria and those students who achieved equivalent levels on an International Baccalaureate test.

The budget proposes to appropriate $15.4 million to fund grants for only the 11^{th} grade students. The 9^{th} and 10^{th} grade students would receive their awards only after completion of the 11^{th} grade. This proposal would result in savings of $39.6 million in 2003-04.

STATE AND CONSUMER SERVICES AGENCY

This section includes the budgets of the Science Center; the Department of Consumer Affairs (including all bureaus, boards programs and divisions), Department of Fair Employment and Housing, Franchise Tax Board, Department of General Services, State Personnel Board, Public Employees' Retirement System, and State Teachers' Retirement System. Departments with reductions or augmentations other than normal operating expenses or elimination of vacant positions are highlighted.

1110 Department of Consumer Affairs

The Department of Consumer Affairs is responsible for promoting consumer protection while supporting a fair and competitive marketplace. The department serves as an umbrella for 18 semi-autonomous boards and 11 bureaus and programs that regulate over 180 professions. The 2003-04 budget for Consumer Affairs, boards, bureaus, and divisions totals $337 million, which is less than one percent higher than the current year funding.

Bureau of Automotive Repair. The budget proposes 3.6 additional personnel years in the current year and 20.2 in the budget year for the implementation of the enhanced Smog Check

The budget proposes to transfer $2.0 million in the current year and $3.3 million in the budget year from the High Polluter Repair or Removal Account to the Vehicle Inspection Repair Fund to repay a loan provided from that fund in the 2001-02 fiscal year. The 2001-02 budget contained a transfer of $50 million from the High Polluter Repair or Removal Account to the General Fund. The 2001-02 mid-year revision also transferred an additional $44 million in 2001-02.

This has reduced expenditures for the Consumer Assistance Program that pays qualified consumers who voluntarily choose to retire their-high polluter vehicles. The program also pays a portion of the consumer's repair bill in order to bring a vehicle into compliance with the requirements of the Smog Check Program. Expenditures for this program were $46.4 million in 2000-01 and $31.9 million in 2001-02. The budget proposes to reduce expenditures to $21.1 million in the current year and $20.4 million in the budget year due to the transfer of the funds to the General Fund and the loan repayment.

Board of Architectural Examiners-Landscape. The budget proposes a loan of $1 million from the California Board of Architectural Examiners-Landscape Architects Fund to the General Fund. This would leave a fund balance of $525,000, or about 75 percent of the annual expenditures.

Board of Barbering and Cosmetology. Effective January 1, 2003 the Board of Barbering and Cosmetology replaces the Bureau of Barbering and Cosmetology. There is an augmentation of $609,000 to automate written examinations for all license categories.

Contractors' State License Board. The budget proposes a loan of $5 million from the Contractors' License Fund to the General Fund. The $11 million current year loan has a repayment date of September 2003. This proposed loan and the repayment of the current year loan would leave a 2003-04 fund balance of $10.7 million or about 23 percent of the annual expenditures.

Dental Board. The budget proposes a loan of $5 million from the State Dentistry Fund to the General Fund, in addition to the current year loan of $5 million approved in last year's budget. This proposed loan would leave a 2003-04 fund balance of $1.7 million or about 24 percent of the annual expenditures.

Acupuncture Board. The budget proposes a loan of $1 million from the Acupuncture Fund to the General Fund. This proposed loan would leave a 2003-04 fund balance of $1.0 million or about 33 percent of the annual expenditures.

Court Reporters Board. The budget proposes a loan of $1 million from the Court Reporters Fund to the General Fund. This proposed loan would leave a 2003-04 fund balance of $551,000 or about 87 percent of the annual expenditures.

Board of Vocational Nursing and Psychiatric Technicians. The budget proposes a loan of $1 million from the Vocational Nurse Examiners Fund to the General Fund. This proposed loan would leave a 2003-04 fund balance of $1.8 million or about 42 percent of the annual expenditures.

The budget also proposes a loan of $1 million from the Psychiatric Technicians Account Vocational Nurse and Psychiatric Technician Examiners Fund to the General Fund. This proposed loan would leave a 2003-04 fund balance of $395,000 or about 33 percent of the annual expenditures.

Bureau of Security and Investigative Services. The budget proposes a loan of $4 million from the Private Security Services Fund to the General Fund. This proposed loan would leave a 2003-04 fund balance of about $2 million or about 28 percent of the annual expenditures.

1700 Department of Fair Employment and Housing

The objective of the Department of Fair Employment and Housing (DFEH) is to protect the people of California from unlawful discrimination in employment, housing, and public accommodations, and from the perpetration of acts of hate violence. The budget year expenditures are proposes at $16.6 million ($12.6 million GF), which is a decrease of 24 percent from the current year.

In the current-year, the mid-year revision proposed to revert $837,000 and 9 PYs related to vacant positions. In addition, the department lost nine PYs and $472,000 ($361,000 GF) due to Control Section 31.60, which called for the abolition of vacant positions. The workload related to these positions was funded through a one-time federal funding augmentation of $1.6 million.

The budget proposes to reduce the budget by an additional $3.1 million (GF) and 45 PYs. This is a reduction of nearly one-fifth of the staffing of the department. This proposal would also result in the closure of two field offices and reductions in a third office. This reduction would result in a major increase in the number of backlogged housing cases.

1730 Franchise Tax Board

The Franchise Tax Board (FTB) administers the Personal Income Tax and the Bank and Corporation Tax Laws, and the Senior Homeowners and Renters' Assistance program. In addition, FTB provides processing services through contracts with other governmental agencies and performs audits and field investigations of campaign statements and lobbyist reports authorized by the Political Reform Act. The board began collecting delinquent child support payments under a permanent program last year. FTB is funded at $445.2 million, of which $402.8 million is General Fund. This amount is $16.5 million or 3.5 percent less than budgeted in the current year.

Issues

Integrated Non-Filer Compliance (INC). The INC program pursues taxpayers that do not file returns, but have tax liabilities over $200. These individuals have income subject to taxes that have not filed a tax return. Of the budget year reduction of $16.5 million, $11.8 million is due to completion of the Integrated Nonfiler Compliance Project. Thus, these savings are due to the completion of a limited-term program rather than a reduction in services.

E-File Tax Practitioner. FTB is proposing the implementation of a program to mandate e-file for tax professionals who handle a high volume of California tax returns (100 or more) and currently submit those returns on paper. The mandatory program would affect only PIT returns. This program would result in savings of $1.4 million (GF) and 50.5 PYs. Tax practitioners filing returns for 100 or more taxpayers include about 10,000 of the 40,000 tax professionals who conduct business in California. These practitioners, however, prepare about 60 percent of the personal income tax returns filed.

The customer of a tax practitioner that prepares 100 or more tax returns would not have the choice of filing a hard copy of their return themselves.

This same proposal was rejected by the Legislature last year.

Augmentation for Implementation of City Business Tax Disclosure. The budget requests increased reimbursement authority of $355,000 and 4.4 PYs to implement Chapter 915, Statutes of 2001 (AB 63, Cedillo), which authorized FTB to disclose confidential tax information to city business tax officials. These costs will be fully reimbursed by the cities that use the information.

The information is used by city tax officials to identify individuals that report business income on state returns but do not have an active city business license within their city jurisdictional boundaries.

A similar request for funding of this chaptered legislation was denied by the Legislature last year.

Political Reform Audit Program. The budget proposes to change the funding for the Political Reform Audit Program. Currently, this program is funded from the General Fund. The budget proposes to establish a new special fund (the Political Reform Audit Fund) to cover expenses of compliance audits. This proposal would impose a fee on candidates filing for elected public offices, lobbyists, lobbying firms, lobbyist employers, and certain political committees for deposit in the newly established fund. The new fee is proposed to generate $1.36 million to pay for the audit costs.

1760 Department of General Services

The Department of General Services (DGS) provides management review and support services to state departments. The DGS is responsible for the planning, acquisition, design, construction, maintenance, and operation of the state's office space and properties. It is also responsible for the procurement of materials, data processing services, communication, transportation, printing, and security.

The budget for DGS is proposed at $837.1 million, of which $3.0 million is General Fund. The total budget is about $32 million or 3.7 percent less than in the current year. The General Fund support is reduced from $110.2 million in 2001-02 and $17.0 million in the current year to $3.0 million in the budget year.

Issues

Rate Increase for the State Emergency Telephone Number Account (911 Account). The budget proposes an increase in the fee charged on intrastate calls from 0.72% to 1.00%. This will increase revenues to this account by $46.6 million to a total of $181.2 million. The increased revenues will be allocated to the following departments: a) CHP - $41 million, b) Health Services - $3.6 million, and c) Forestry and Fire Protection - $2.6 million. These are funding shifts rather than new revenues for new programs.

1920 State Teachers' Retirement System (STRS)

The budget proposes to reduce the General Fund payment for teacher purchasing power maintenance by $500 million in 2003-04. The proposal provides that the state would make a statutory commitment to restore the funds if purchasing power protection cannot be maintained at the 80 percent level through July 1, 2036. This action must be taken during the current fiscal year. The actuary for STRS has stated that the elimination of this payment would be actuarially unsound.

BUSINESS, TRANSPORTATION, AND HOUSING AGENCY

This section includes the budgets of the departments of Alcoholic Beverage Control, Financial Institutions, Corporations, Housing and Community Development, Office of Real Estate Appraisers, Real Estate, Transportation Commission, and Transportation. Departments with reductions or augmentations other than normal operating expenses or elimination of vacant positions are highlighted.

2180 Department of Corporations

The Department of Corporations administers and enforces state laws regulating securities, franchise investment, lenders, and fiduciaries. The budget is proposed at $28.3 million (State Corporations Fund).

Issues

The budget proposes an increase of $3.2 million and 28.5 positions to transfer the regulation, enforcement, administration, and spending authority of the Office of Real Estate Appraisers to the Department of Corporations.

2240 Department of Housing and Community Development

A primary objective of the Department of Housing and Community Development (HCD) is to expand housing opportunities for all Californians. The department administers housing finance, economic development, and rehabilitation programs with emphasis on meeting the shelter needs of low-income persons and families and other special need groups. It also administers and implements building codes, manages mobilehome registration and titling, and enforces construction standards for mobilehomes.

The HCD budget is proposed to increase from $446.1 million in the current year to $647.2 million in the budget year. The General Fund support in the current year is $15.1 million and is proposed at $13.4 million in the budget year. In 2001-02, the total budget for HCD was $305.4 million, of which $91.7 million was from the General Fund.

Issues

Proposition 46 (Housing and Emergency Shelter Trust Fund Act of 2002). This November 2002 bond measure authorized $2.1 billion for various housing programs. Local project bond expenditures will be $255 million in the current year and $463 million in 2003-04. Projects are as follows:

LOCAL PROJECTS	In Millions	
	2002-03	**2003-04**
State and Local Homeownership Programs for Lower Income Families	$59.1	$107.6
Farmworker Housing Projects	25.0	64.7
Affordable Multifamily Rental Housing, Supportive Housing, Student Housing and Local Housing Trust Funds.	109.7	193.5
Homeless Shelters and Transitional Housing	31.0	31.0
Financial Incentives to Communities that Increase Housing Production	25.0	25.0
Downpayment Assistance For Communities that Reduce Barriers to Housing		24.0
Preservation of Affordable Low-Income Housing	4.8	17.2

Farmworker Housing Grants. The budget proposes reducing Farmworker Housing grants from $17.6 million to $14 million in the budget year.

Emergency Housing Assistance Grants. The Emergency Housing and Assistance Program (EHAP) provides capital grants and operating funds for emergency shelters, transitional housing, and services for homeless individuals and families. Proposition 46 included $195 million for this program, but the funds are restricted to capital grants to shelter providers. The funds in the budget are for operating costs, which cannot be funded from Proposition 46 bond funds.

In 2001-02, this program received $13.3 million. In the current year, the December Revision proposed that the grant of $5.3 million be reduced to $4 million. The Senate and Assembly both rejected this proposed reduction. The budget proposes to continue funding in 2003-04 at the $4 million level.

This program could not adequately fund programs when it was funded at $13.3 million. There are requests totaling more than the $5.3 million budgeted in the current year. A further reduction in this program will deprive homeless persons.

Housing Preservation Research Contract.

The budget proposes to eliminate funding in the current and budget year for a $65,000 (GF) contract to maintain and update the statewide database on assisted housing units at risk of conversion. HCD proposed awarding the contract to the California Housing Partnership Corporation (CHPC) and CHPC has been doing work under the contract since July. The Senate rejected eliminated funding for this contract in the First Extraordinary Session. Eliminating funding for this contract would jeopardize state and local efforts to use bond funds dedicated to preserving at-risk housing developments.

2310 Office of Real Estate Appraisers

The Office of Real Estate Appraiser (OREA) administers a program for licensing of real estate appraisers in federally related loan transactions. The budget proposes to transfer the functions and $3.3 million in funding for OREA to the Department of Corporations effective July 1, 2003. The Administration contends this will save $150,000.

TECHNOLOGY, TRADE AND COMMERCE AGENCY

Managing the state's economic development efforts is the primary responsibility of the (TTCA). Its major programs are Economic Development, International Trade and Investment, Marketing and Communications and Tourism. The department also provides low-cost financing to public agencies for a variety of infrastructure and public improvements through the California Infrastructure and Economic Development Bank.

The TTCA budget for 2001-02 was $184.1 million ($71.9 million GF). The current year budget, adjusted for the December Revision, is budgeted at $156.4 million. The Senate rejected the elimination of the Biomass Grants in the First Extraordinary Session, so the adjusted current year budget would be $160.4 million ($45.6 million). The budget year is proposed at $108.6 million ($21.4 million GF).

The 2002-03 budget for TTCA reduced by $30 million, including an unallocated reduction of $2 million to the foreign trade offices and an unallocated reduction of $10 million to the department.

Issues

Manufacturing Technology Program (MTP). This program is intended to improve the competitiveness of California small- and medium-sized manufacturers to create and retain high-wage, high-skill jobs. California's public and private sectors invest in MTP to sustain the state's leadership role in manufacturing through the formation of joint state/federal/academic/private sector partnerships that provide targeted solutions for industry needs. The program requires one-third federal/two-thirds other funding requirement.

This program was funded at $2.7 million in 2002-03.

California Technology Investment Partnership (CalTIP). The budget proposes to eliminate funding for this program, which provides matching funds for federal grant money to small- and medium-sized businesses to assist in the development of marketable technologies. Grants are typically $150,000 to $200,000 and used to match federal funds, although matching funds can come from other sources including private funds. This program included funding of $4 million in 2001-02 and $3 million in 2002-03.

From 1993-94 through the 2001-02, the state has provided $45.6 million (GF). The state investment has been matched by $250.6 million in federal funds and $249.6 million in private funds.

Film California First Program. The budget proposes to eliminate funding of $2.1 million in the current year and $1.8 million in the budget year for Film California First Program. This reduces the program from the 2001-02 level of $12.9 million (GF) to $11.0 million in the current year and $11.2 million in the budget year.

Military Base Reuse and Retention Program. The budget proposes to eliminate funding for this program. This program was funded at $1.9 million in 2001-02 and $0.9 million in the current year. Funding for this program was reduced in the current year because the next round of base closures has been delayed to 2005.

Export Finance, Export Development, and Foreign Investment. The California Export Finance Office (CEFO) seeks to expand California employment and income opportunities by promoting increased exports of California goods and services, including agricultural commodities by providing California exporters, particularly small- and medium-sized manufacturers, exporters, and agricultural enterprises with information and technical assistance. Funding for this program and other global economic programs was reduced from $9.3 million in the current year to $5.4 million in the budget year.

Office of Tourism. The budget proposes to eliminate funding of $7.5 million (GF) for the Agency's Tourism Division.

GENERAL GOVERNMENT

Departments with reductions or augmentations other than normal operating expenses or elimination of vacant positions are highlighted.

8260 California Arts Council

The California Arts Council (CAC) budget was funded at $49.7 million in 2001-02 and $21.5 million in the current year. Most of this reduction ($20 million) was attributable to no funding provided for district-specific projects. In addition, local grants were reduced by $9 million. The budget proposes expenditures of $13.6 million in the budget year.

Issues

Arts in Education Program. Under the program, the state assists artists and arts organizations to enhance the capacity of California schools to teach the arts and to use the arts to teach other subject matters. The budget provided $7.2 million (General Fund) in local augments for this program in the current year. The budget proposes to reduce this amount by $2.7 million (40 percent) in the budget year.

Organization Support Grants. This program provides matching grants that leverage local private and public dollars for over 800 arts organizations throughout the state. This program was funded at $10.9 million in 2001-02 and $7.6 million in the current year. The budget proposes to reduce funding by $3.0 million (40 percent) for funding of $4.4 million in 2003-04.

8380 Department of Personnel Administration

The Department of Personnel Administration manages the nonmerit aspects of the State's personnel system.

Issues

Rural Health Care Equity Program. This program subsidizes additional health care costs for state employees and annuitants that live in areas with no managed care. The budget proposes to eliminate the program for annuitants for savings of $11.5 million in the current and budget year. The program for state employees is subject to collective bargaining.

The Senate and Assembly both rejected the proposal to eliminate this funding in the current year in the First Extraordinary Session.

8885 Commission on State Mandates

The Commission on State Mandates is a quasi-judicial body that makes the initial determination of state mandated costs. Support costs for the department are proposed at $1.3 million in 2003-04.

Issues

State Mandated Local Cost Reimbursement. The 2002-03 budget deferred payments to local governments for state-mandated local programs. The mandates are still in effect and the Constitution requires the state to reimburse local agencies for these costs including interest on the deferred amount. This deferral includes reimbursements for 2002-03 mandate claims, prior-year deficiencies, and newly identified mandate claims. The LAO estimates the state's costs to pay these deferred claims will total about $800 million.

The proposed budget requests continued deferral of local reimbursement payments. The LAO estimates that the deferral of these payments will total $1.2 billion at the end of the 2003-04 fiscal year. If these mandates are not suspended, the costs will continue to be a state obligation.

9100 Tax Relief

California offers a variety of tax relief programs by appropriating funds through a reduction in rates or nonrefundable tax credits. The state also provides the following tax relief through the appropriation of funds for payments to individuals or reimbursement of local agencies. Relief proposed in 2003-04 is $1.6 billion, or 50.2 percent, less than the amount provided in 2002-03. This decline is due to the elimination of Open Space Subventions and the elimination of the general-purpose backfill to local governments of the Vehicle License Fee (VLF) offsets.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
Senior Citizens' Property Tax Deferral	$12,800	$11,900	-$900	-7.0
Senior Citizens' Property Tax Assistance	36,501	37,961	1,460	4.0
Senior Citizen Renters' Tax Assistance	151,735	157,805	6,070	4.0
Homeowners' Property Tax Relief	414,213	419,600	5,387	1.3
Open Space Subventions	39,000	0	-39,000	-100.0
Substandard Housing	44	44	0	0.0
Vehicle License Fee Offset	2,585,291	987,014	-1,598,277	-61.8
State-Mandated Local Programs	3	3	0	0.0
Total	$3,239,587	$1,614,327	-$1,625,260	-50.2

Issues

Vehicle License Fee Subventions to Cities and Counties. The budget proposes to eliminate the VLF backfill to cities and counties commencing in February 2003 for current year savings of $1.3 billion and budget year savings of $2.9 billion. The budget does not eliminate the backfill for county realignment funds or funds related to the Orange County bankruptcy. The Senate and Assembly both rejected the proposal to eliminate the current year VLF backfill in the First Extraordinary Session.

The budget does not propose increasing the VLF to ensure that both the state and local governments are held harmless. The Senate approved AB 1105 in August 2002 and AB 4 X in the First Extraordinary Session in 2003, which would have clarified the mechanism for reducing the VLF offset if there is a shortfall in General Fund revenues available to reimburse local governments. This would result in annual General Fund savings of approximately $3.8 billion when there are insufficient General Fund revenues. The Governor stated that he would veto AB 4 X, but at the time this report was prepared that had not occurred.

Open Space Subventions. This program allows cities and counties to contract with landowners to limit the use of land to agricultural, scenic, and open space purposes. In exchange, these properties are assessed at other than market value based on their limited use. The budget proposes to eliminate subventions in the current year for savings of $39 million (GF).

9210 Local Government

The Local Government Finance item proposes $330 million in funding for local agencies. The state provides other assistance to local governments, primarily counties, through other direct programs budgeted in other items in the budget. Health and Human Services has numerous programs where the state and counties jointly provide funding for services. State funding is included in Public Safety for such issues as local crime labs and suppression of high intensity drug trafficking areas.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
High-Technology Grants for Local Law Enforcement	$18,500	$18,500	0	0.0
Reimbursement for Booking Fees	38,220	0	-38,220	-100.0
Property Tax Loan Program	51,500	60,000	8,500	16.5
Rural and Small County Law Enforcement	18,500	18,500	0	0.0
Citizens' Option for Public Safety (COPS)	232,600	232,600	0	0.0
Special Supplemental Subventions	1,400	0	-1,400	-100.0
State-Mandated Local Programs	0	0	0	0.0
Local Grants	750	850		
Total	$361,470	$330,450	-$31,020	-8.6

Issues

Redevelopment Agencies. The budget proposes a transfer of $250 million or the growth in property tax revenues for redevelopment agencies to ERAF in 2003-04. This would reduce General Fund appropriations to K-14 education by the same amount. This transfer is proposed to increase to the full amount of "diverted " redevelopment agency property tax allocation (approximately $1.3 billion) over time.

The budget also proposes a property tax transfer of $500 million from the low and moderate income housing funds of local redevelopment agencies to ERAF in the current year. Redevelopment agencies (unlike cities, counties, and special districts) did not receive any state "bail-out" or property tax transfers from school districts as a result of the enactment of Proposition 13. The Senate rejected this proposal in the First Extraordinary Session.

Booking Fees. The budget proposes elimination of $38.2 million (GF) in booking fee reimbursements in the budget year.

Funds for Counties for Administration of the Property Tax. The budget proposes funding of $60 million to assist counties with the administration of the property tax. This program has traditionally resulted in expenditures of about $51 million.

Citizens' Option for Public Safety (COPS) and Juvenile Crime Prevention Programs. The COPS program funds local law enforcement, sheriffs' departments for jail construction and operations, and district attorneys for prosecution. In 2000, this program was expanded to include funding for county juvenile crime prevention programs. Funding for this program is extended for one more year at the current-year level of $232.6 million.

Technology Grants for Local Law Enforcement. The budget extends funding of $18.5 in one-time funding for local law enforcement agencies to purchase high-technology equipment for crime prevention and suppression into 2003-04. This program was funded at $35.4 million in 2001-02..

Rural and Small County Law Enforcement Grants. As part of the 2001-02 budget compromise, an annual appropriation of $18.5 million was provided in statute to provide grants to county sheriffs in the 37 smallest counties. Each county received a grant of $500,000.

9800 Augmentation for Employee Compensation

The budget proposes savings of $855 million ($470 million GF) for deferring scheduled salary increases, lowering or freezing future salary or benefit expenditures, layoffs, furloughs, and other similar personnel actions. Most of these savings are dependent upon collective bargaining agreements.

JUDICIARY

0250 Judicial

The Judicial budget includes support for the California Supreme Court , the courts of appeal , and the Judicial Council of California. There are 105 appellate court justices and seven Supreme Court justices. The Judicial Council, including the Administrative Office of the Courts, is the administrative and policy-making body of the judiciary.

The budget proposes total expenditures of $344.8 million for the Judicial branch. This amount is an decrease of $483,000, or 0.1 percent, below the current year. General Fund support would increase by $348,000, or 0.1 percent, for a total of $289.4 million. Of the total proposed, $38 million is for the Supreme Court, $172 million is for the operation of the Courts of Appeal, $142.2 million is for the Judicial Council, and $10.4 million is for the California Habeas Corpus Resource Center. Total authorized positions for the four entities would increase by 2.

Summary of Expenditures (dollars in thousands)	2002-03	2003-04	$ Change	% Change
General Fund	$289,061	$289,409	$348	0.1
Motor Vehicle Account	137	135	-2	-1.5
Court Interpreters Account	84	84	0	0.0
Family Law Trust Fund	3,019	3,019	0	0.0
Federal Trust Fund	4,700	4,710	10	0.2
Judicial Branch Workers' Compensation Fund	0	3		
Reimbursements	48,327	47,485	-842	-1.7
Total	$345,328	$344,845	-$483	-0.1

Highlights

Current-Year Savings Assumed in the Budget

- An unallocated General Fund reduction of $8.5 million, or 2.9 percent of the total General Fund budget.

Budget Year Reduction

- A reduction of $17.7 million, or 5.1 percent of total funding for the judiciary. During the budget process, the Judicial Council will provide a plan for allocating these reductions.

Proposed Increase

- $635,000 within the AOC to implement the Trial Court Interpreter Employment and Labor Relations Act.

Selected Issues

Appellate Filing Fee Increase. The budget proposes legislation to increase the appellate filing fee from $265 to $630, effective July 1, 2003. This increase would result in $2.1 million in revenues to the General Fund. The Legislature may wish to consider the impact of this increase, which would make California's appellate filing fee the highest in the country.

Unallocated Reduction. As noted above, the budget proposes a reduction of $17.7 million for the budget year. For the current year, the AOC has indicated that it will achieve the necessary savings of $8.5 million, through holding positions vacant, delaying employee promotions and reclassifications, restricting travel, reducing temporary help, deferring contracts, and reducing the number of Judicial Council and Advisory Committee meetings. During the budget process, the Judicial Council will be providing the Legislature with a plan for the allocation of the $17.7 million in budget year reductions. The Legislature may wish to review the allocation of the reductions to help insure that the reductions are appropriate and limit adverse impacts on access to justice.

0390 Contributions to Judges' Retirement System

The Judges' Retirement System (JRS I) funds retirement benefits for justices and judges of the Supreme Court, the courts of appeal, and superior courts. Retirement benefits are based on age, years of service, compensation of active judges, and eligibility as determined by specific sections of the Judges' Retirement Law. The JRS I is funded by the Judges' Retirement Fund, which receives revenue from the General Fund and certain filing fees, as well as employee contributions equal to 8 percent of the judges' salaries.

Chapter 879, Statutes of 1994, established the Judges' Retirement System II (JRS II). Unlike its predecessor, JRS II is designed to be fully funded from employer and employee contributions on a prospective basis. The major differences for JRS II include an increased retirement age and a cap on COLAs for retirement benefits of 3 percent annually. All judges elevated to the bench on or after November 9, 1994 are required to participate in JRS II. There are currently 1,610 authorized judges and justices in the state of California. The majority of these judges participate in the JRS I plan.

The number of retired annuitants is projected to increase by 34 to a total of 1,553. The budget proposes expenditures of $121.7 million.

0450 State Trial Court Funding

The Trial Court Funding item provides state funds for support of the state's local trial courts. Since the passage of Proposition 220 on the June 1998 ballot, which allowed for the unification of the superior and municipal courts in a county, the court systems in all 58 counties have unified.

The proposed total budget for the state's trial courts is $2.2 billion. This amount is a decrease of $5.2 million, or 0.2 percent, from the current year. The General Fund portion is proposed to decrease by $301.3 million from $1.1 billion to $791 million. The major factor for the decrease is the proposed $300 million realignment of court security.

Summary of Expenditures (dollars in thousands)	2001-02	2002-03	$ Change	% Change
General Fund	$1,092,413	$791,146	-$301,267	-27.6
Trial Court Improvement Fund	136,745	109,132	-27,613	-20.2
Other Sources	980,110	1,303,763	323,653	33.0
Total	$2,209,268	$2,204,041	-$5,227	-0.2

Highlights

Current Year Savings Assumed in the Budget

- An unallocated reduction of $36 million.

Budget Year Reduction

- An unallocated reduction of $116 million, or 5.3 percent of the total trial court funding budget. During the budget process, the Judicial Council will provide a plan for allocating this proposed reduction.

Other Adjustments:

- Savings of $300 million General Fund by providing a dedicated revenue source for court security. Under this realignment proposal, a portion of the tax increases totaling $300 million would be transferred to the Trial Court Trust Fund for court security purposes, resulting in a savings of $300 million General Fund.
- A reduction of $22 million by allowing courts to contract with various sworn law enforcement agencies to provide security in the courts.
- A reduction of $31 million for implementing electronic recording of court proceedings and $5.5 million in savings related to court ownership of transcripts.
- An increase of $20 million to pay for increased court staff retirement costs.
- An increase of $32.6 million for ongoing courthouse security costs related to increases in the contractual costs of negotiated salary increases and for increased benefits and retirement contributions.
- An increase of $4.5 million for anticipated court interpreter workload growth.
- An increase of $3.9 million to implement the Trial Court Interpreter Employment and Labor Relations Act. The Act requires the trial courts to employ spoken language interpreters as court employees rather than independent contractors on or after July 1, 2003.

Revenue Adjustments:

- **Various Fee Increases**. The budget assumes revenues of $66.2 million from new and increased fees to offset General Fund support for the trial courts. The fees include a $20 court security fee per court filing ($34 million), increasing the trial motion fee from $23 to $33 ($1.2 million), and transferring various undesignated fees on court related activities from the counties to the courts ($31 million).

Selected Issues

Undesignated Fees. The Lockyer-Isenberg Trial Funding Act of 1997 (Chapter 850, Statutes of 1997) and other recent trial court funding legislation made changes in the distribution and amount of court-related fees. An important part of the financing mechanism for the state's new fiscal responsibility for the trial courts was the requirement that local governments transfer a variety of court-related fees collected by trial courts and local governments to the state's trust fund. However, Chapter 850 did not designate which entity--the state or local governments--would retain a number of court-related fees. Some of the undesignated court fees include fees for postponement, change of venue, filing for Writ of Execution, and the civil assessment fee. The amount of each fee varies from $1, to as much as $1,000.

The budget proposes to transfer a portion of those undesignated fees from counties to courts. The Legislature may wish to review the proposal to ensure that the proposed fees are related to court-related activities and that the proposed transfer of fees makes sense from a policy perspective.

Electronic Recording. As noted above, the budget proposes savings of $31 million for implementing electronic recording for certain court proceedings and $5.5 million in savings related to court ownership of transcripts. The Legislature may wish to review the estimates for savings and consider the policy implications of implementing electronic recording.

Court Security. Court security costs for the trial courts have increased in the last several years. The proposed budget includes several measures intended to provide additional revenues and flexibility for security services. Specifically, the budget proposes a General Fund reduction of $34 million, and a projected increase of $34 million in revenues generated by collecting a security surcharge fee in all civil cases, and in all criminal cases that result in a conviction. The budget also assumes savings related to a change in law that would allow local courts to contract with law enforcement agencies,. other than the county sheriff, for court security. Finally, the budget proposes that $300 million from new taxes offset General Fund expenditures for court security.

APPENDIX

TIMELINE FOR THE 2003-04 BUDGET BILL

Wednesday	January 8	Senator Burton releases *Review of the December Revision*
Friday	January 10	• Governor submits State Budget to the Legislature. • Committee releases *Quick Summary of Governor's Proposed Budget*.
Wednesday through Friday	January 15 through 17	Committee conducts hearings on December Revision
Tuesday	January 21	Committee conducts overview hearing of the budget. Department of Finance presents budget and the Legislative Analyst provides initial review.
Wednesday	February 13	Committee releases *Overview of the 2003-04 Budget Bill.*
Wednesday	February 19	Legislative Analyst submits *Analysis of the 2003-04 Budget* to the Legislature.
Thursday	February 27	Committee conducts hearing on revenues.
Monday	March 3	Subcommittees begin hearings.
Thursday	April 10	Spring Recess begins.
Monday	April 21	Legislature reconvenes.
Thursday	May 1	Department of Finance submits final capital outlay revisions.
Wednesday	May 14	Governor delivers May Revision to the Legislature.
Friday	May 23	Subcommittees complete hearings.
Tuesday	May 28	Committee meets to adopt subcommittee reports. Committee releases *Major Action Report.*
Thursday	May 30	Senate votes on Senate budget bill.
Monday	June 4	Conference Committee may begin. Conference *Agenda* available from committee.
Sunday	June 8	Conference Committee completes work.
Friday	June 13	Senate and Assembly vote on budget bill and budget trailer bills.
Sunday	June 15	Legislature must pass budget to meet constitutional deadline for passage of the budget.

STAFF ASSIGNMENTS

CRIMINAL JUSTICE/CORRECTIONS	Alex MacBain
EDUCATION	
K-12	Kim Connor
Higher Education	Amy Supinger
ENERGY	
	John Barnato
	Gabe Meyer
ENVIRONMENTAL PROTECTION	Jon Barnato
LABOR	Kim Collins
LOCAL GOVERNMENT	Judi Smith
HEALTH	Diane Van Maren
RESOURCES	Frank Vega
REVENUES	Judi Smith
SOCIAL SERVICES	Ana Matosantos
STATE ADMINISTRATION	Judi Smith
TRANSPORTATION	Frank Vega
VETERANS AFFAIRS	Kim Collins
COMMITTEE ASSISTANTS	Glenda Higgins
	Rose Morris
RECEPTIONIST	Mary Teabo

CALIFORNIA STATE BUDGET HISTORY

Fiscal Year	Bill and Chapter No.	Date Passed and Chaptered		Total Budget ($ Billions)
1965-66	AB 500/757	6-18	6-30	4.0
1966-67[a]	SB 1XX/2	6-30	6-30	4.7
1967-68	AB 303/500	6-29	6-30	5.0
1968-69	SB 240/430	6-28	6-29	5.7
1969-70	SB 255/355	7-3	7-3	6.3
1970-71	AB 525/303	7-4	7-4	6.6
1971-72[b]	SB 207/266	7-2	7-3	6.7
1972-73[c]	SB 50/156	6-15	6-22	7.4
1973-74	AB 110/129	6-28	6-30	9.3
1974-75	SB 1525/375	6-28	6-30	10.3
1975-76	SB 199/62	6-26	7-1	11.5
1976-77	SB 1410/320	7-1	7-2	12.6
1977-78	AB 184/219	6-24	6-30	14.0
1978-79	AB 2190/359	7-5	7-6	18.8
1979-80	SB 190/259	7-12	7-13	21.5
1980-81	AB 2020/510	7-16	7-16	24.5
1981-82[c]	SB 110/99	6-15	6-28	25.0
1982-83	AB 21/326	6-30	6-30	25.3
1983-84	SB 123/324	7-19	7-21	26.8
1984-85[c]	AB 2313/258	6-15	6-27	31.0
1985-86[c]	SB 150/111	6-13	6-28	35.0
1986-87[c]	AB 3217/186	6-12	6-25	38.1
1987-88	SB 152/135	7-1	7-7	40.5
1988-89	AB 224/33	6-30	7-8	44.6
1989-90	SB 165/93	6-29	7-7	48.6
1990-91	SB 899/467	7-28	7-31	51.4
1991-92	AB 222/118	6-20/7-4	7-16	55.7
1992-93	AB 979/587	8-29	9-2	57.0
1993-94	SB 80/55	6-22	6-30	52.1
1994-95	SB 2120/139	7-4	7-8	57.5
1995-96	AB 903/303	8-2	8-3	56.8
1996-97	SB 1393/162	7-8	7-15	61.5
1997-98	AB 107/282	8-11	8/18	67.2
1998-99	AB 1656/324	8-11	8-21	71.9
1999-00	SB 160/50	6/16	6/29	81.3
2000-01	AB 1740/52	6/22	6/30	99.4
2001-02	SB 739/106	7/21	7/26	103.3
2002-03	AB 425/379	9/1	9/5	98.9

[a] *1966 Second Extraordinary Session.*
[b] *First year budget was to be enacted by June 15.*
[c] *June 15 constitutional deadline met (5).*

INDEX