



Budget Conference Committee 2010-2011 Budget Package

October 6, 2010

Conferees

Senator Denise Moreno Ducheny, Chair

Assemblymember Bob Blumenfield, Vice Chair

**Members: Senator Bob Dutton, Senator Bob Huff, Senator Mark Leno, Senator Alan Lowenthal,
Assemblymember Connie Conway, Assemblymember Felipe Fuentes, Assemblymember Jim Nielsen, and
Assemblymember Nancy Skinner**

2010-11 BUDGET PACKAGE

The 2010-11 budget package closes the budget gap and moves California forward.

As California begins to emerge from the global recession, the 2010-11 budget provides a way forward to protect the public structures of education, public safety, infrastructure, and vital services. The budget does not increase any tax rates and implements significant ongoing reform in the areas of budget and public pensions.

In the 2010 May Revision, the Governor identified a budget shortfall of \$17.9 billion. He offered a total of \$19.1 billion in budget “solutions” to close the shortfall and generate a reserve of \$1.2 billion.

The negotiated budget package includes approximately \$18.3 billion in General Fund “solutions” to close the gap, and provides a final reserve of approximately \$323 million.

General Budget Framework

The budget package includes a combination of significant expenditure reductions, federal relief, additional revenues, and fund shifts. In addition to addressing the 2010-11 budget, the package includes many ongoing solutions and permanent reforms. The 2010-11 budget package includes proposals to reduce the deficit with solutions that fall into the following categories (dollars in billions based on preliminary scoring):

Starting Problem.....	-\$17.9
• Expenditure Reductions	7.5
• Federal Funds	5.3
• Additional Revenues	2.5
• Fund Shifts, Other Revenues	2.8
• Alternative Funding	0.5
• Baseline Workload Adjustments.....	-0.2
Total Solutions.....	\$18.3
Final Reserve	\$0.3

2010-11 BUDGET MAJOR PROPOSALS

K-14 Education. Maintains modest increase in education funding on a per-pupil programmatic basis for 2010-11, and begins paying “settle-up” payments for the 2009-10 fiscal year with a \$300 million payment in 2010-11. This budget provides ongoing Proposition 98 funding of \$49.7 billion and through a new deferral of \$1.9 billion and one-time funds brings total state funding for schools and community colleges to \$52.5 billion.

- **Increases K-12 Per Pupil Funding.** Provides over \$300 per-pupil more than the Governor’s May Revision proposal on a programmatic basis. Programmatic spending under the budget plan is proposed to be just under \$8,000 per pupil.
- **Preserves Integrity of Proposition 98.** Rejects the Governor’s legally-suspect proposal to manipulate the Proposition 98 guarantee and rather proposes a direct suspension of the guarantee for one year at a specific funding level. As the LAO has noted, suspension of the Proposition 98 guarantee reduces legal or Constitutional ambiguity over the maintenance factor created as part of last year’s budget agreement. Thus, the suspension keeps last year’s budget promises and enables funding for schools to grow as the economy rebounds.
- **Implements mandate reform.** Begins reforms of some K-14 mandate requirements by suspending some less-important mandates and clarifying law to permanently eliminate or reduce other mandate costs. Funds the anticipated cost of mandates for 2010-11.
- **Child Care.** Rejects the elimination of child care funding, as proposed in the Governor’s May Revision.
- **Community Colleges.** Provides \$126 million for enrollment growth for 26,000 new students. Also provides an additional \$35 million to restore categorical programs and \$25 million for an Economic and Workforce Development program to develop programs to meet emerging workforce needs. Includes a new deferral of \$189 million paid in 2011-12.

Higher Education. Provides \$5.5 billion from the General Fund for support of the University of California and California State University systems. Funding is above the 2009-10 level and includes full funding for enrollment growth and an augmentation of approximately \$199 million for each segment to backfill previous cuts to the systems.

Health and Human Services. The budget makes a number of reductions in health and human services programs, but rejects the Governor’s proposals to eliminate CalWORKs, community mental health programs, Adult Day Health care, and the significant reductions proposed to the In-Home Supportive Services program.

The negotiated budget also restores or partially restores several programs that were vetoed by the Governor in 2009-10. The most significant being the restoration of funding for child welfare services and the Office of AIDS.

Public Safety. The negotiated budget does include corrections savings of over \$1.1 billion, primarily from reduced inmate medical care costs. The budget proposal does not include a “realignment” of state inmates to the counties.

State Employees. The budget package reduces spending for state employees by about \$1.5 billion consistent with collective bargaining agreements that have already been reached or are in negotiation. This is \$500 million less than what the Governor has proposed.

Federal Funds. The budget package assumes new or extended federal funds to provide \$5.3 billion in budget solutions. This amount is less than the \$6.9 billion assumed in the Governor’s January Budget.

Revenues. The negotiated budget includes \$2.5 billion in revenue solutions. More than half of this, \$1.4 billion, is from the Legislative Analyst’s revenue forecast, which was \$1.4 billion higher than the Governor’s May Revision – three months into the fiscal year, this additional revenue has already been realized. The remainder of the revenue change is from the following:

- **Extend the Net Operating Loss (NOL) suspension:** The budget continues the suspension of the NOL corporate tax benefit for an additional two years, which results in increased tax revenue of about \$1.2 billion in 2010-11. Over 90 percent of all corporations are exempted from this suspension.
- **Corporate underpayment penalties and “Cost of Performance” rule change.** The budget proposal revises recent corporate tax law changes related to penalties assessed when a corporation underpays their tax liability by more than \$1 million. The budget proposal also restores the old “cost of performance” rules for the sourcing of intangibles and services related to calculation of multi-state apportionment. These changes will reduce tax revenue by about \$132 million in 2010-11.

KEY DIFFERENCES FROM CONFERENCE

The vast majority of the budget proposal is consistent with the August 27, 2010 conference version of the 2010-11 budget (AB 1636). Below are key differences between the proposed budget package and the conference version.

Less Revenue Increases. As referenced above, the budget package contains only \$2.5 billion in additional revenue assumptions. The budget package relating to revenues has been modified since the August 27, 2010 conference version as follows:

- No longer delays new corporate tax cuts including the Elective Single Sales Factor change for apportioning corporate income and the new tax credit sharing rules.
- No longer includes revenues from a new Oil Severance Tax and a corresponding reduction in the state sales tax.
- No longer includes any revenues related to tax reform.
- No longer includes various tax enforcement efforts, including requiring the collection of Sales and Use Tax by out-of-state Internet retailers.

K-14 Education Spending. The budget package now includes the following key changes to K-14 education spending:

- Provides an additional \$300 million in settle-up payments to schools in the budget year.
- Changes K-12 school spending accounting to defer \$1.7 billion in payments into the next fiscal year. This reduces the amount of money the state spends in the 2010-11 fiscal year, but provides the same level of programmatic funding for schools.
- Changes California Community Colleges spending accounting to defer \$189 million in payments into the next fiscal year.
- Provides for an additional \$20 million in Career Technology funds for the California Community Colleges.

Health and Human Services. The budget package includes the following changes since the August 27, 2010 conference version as follows:

- Continues to protect child care, but assumes an additional reduction of \$48 million through a modest reduction in the license-exempt rates and a small reduction in administrative funds.

- Reduces the unallocated reduction in hours to the In-Home Supportive Services (IHSS) program to 3.6 percent and assumes additional caseload savings based on actual caseload numbers in 2009-10. These reductions, along with a new provider fee, will provide \$300 million in General Fund relief in the budget year, which is an additional \$50 million over what was assumed in the prior conference version.
- Continues to maintain health programs, but scores additional General Fund savings related to shifting expenditures to special fund sources and federal funds. Also includes reduction of discretionary General Fund expenditures related to immunizations and a new proposal to contain costs at the State mental hospitals.

Other Changes. The budget package also includes the following additional changes:

- Provides an additional \$4.2 million General Fund and \$314,000 special fund for the County Veteran Service Offices (CVSOs) to improve Operation Welcome Home services for returning veterans. When combined with current funding, the CVSOs funding level will be \$8.5 million in 2010-11.
- Includes no realignment proposals to shift inmates from state prison to county jails.
- Shifts over \$13 million in water quality and water rights program expenditures from fees to the General Fund.

BUDGET REFORM

Budget Reform. Makes three major changes to create a stronger "rainy day fund" for California.

1. Makes the existing Proposition 58 rainy day fund larger and makes it harder to suspend an annual contribution.
 - Increases the maximum size of the state rainy day fund from 5 percent to 10 percent of General Fund revenue.
 - Requires the State to always make the three percent payments into the rainy day fund, except in years when the State has a deficit big enough to start using the rainy day funding.
 - Allows half of the annual payment into the rainy day fund to be used for one-time infrastructure and debt service.
2. Restricts the use of the funds in the rainy day fund to rainy days.
 - Funds can be used to cover a budget shortfall—up to the previous year's expenditures adjusted for inflation and population growth.
 - Includes a "50-25-25 regulator" provision that prevents using all of the rainy-day funds in one year.
 - If the rainy day fund exceeds 10 percent of General Fund Revenue, annual payments to the fund stop and any excess funding can be used for one time purposes as specified.
3. Captures "unanticipated revenue" for additional rainy day fund contributions.
 - The Department of Finance creates a projection of expected revenue based on the state's last twenty years of revenue performance.
 - Any revenue that is received above that trend line is "unanticipated" and must be put in the rainy day fund.
 - Any new revenue that is needed to meet our Proposition 98 obligation is excluded, so Proposition 98 is fully funded without encroaching on funding for other programs.

PENSION REFORM

Pension Reform. Makes the following changes to state pensions for new state employees hired on or after November 10, 2010. These changes would impact state employees in bargaining units that do not currently have a Memorandum of Understanding (MOU) with the state, as well as employees of the California State University, the judicial branch of government, the Legislature, and classified school employees. These changes do not apply to current employees.

- **Rolls Back SB 400 Pension Benefits.** New state employees' retirement benefits would be returned to the pension benefit levels that existed prior to the adoption of SB 400 (Chapter 555, Statutes of 1999) as detailed in the chart below:

Retirement Category	Current Retirement Formulas	Proposed Formulas
Miscellaneous (including classified school employees)	2% at Age 55 (up to 2.5% at 63)	2% at Age 60 (up to 2.418% at 63)
Industrial	2% at Age 55 (up to 2.5% at age 63)	2% at Age 60 (up to 2.418% at age 63)
State Safety	2.5% at Age 55	2% at Age 55
Peace Officer and Firefighters, with the State, CSU, Legislature and Judicial branch	3% at Age 50	2.5% at Age 55

- **Ends Pension "Spiking."** Requires three-year final compensation method of calculating benefit levels for new state employees who are not already under this calculation method.
- **Transparency.** Requires additional analysis and oversight of CalPERS' actuarial assumptions.