



Date: June 2, 2008

To: State Legislation Committee

From: *fw* Patrick H. West, City Manager *PHW*

Subject: **Governor's May Revise of the FY 2008-09 State Budget**

On Wednesday, May 14, the Governor released the May Revise to the FY 2008-09 State Budget. Every year in May, the Governor issues an update to his January proposed budget, which includes updated revenue and expenditure forecasts. This memo provides an overview of the major programs of interest, including direct impacts to Long Beach that can be identified.

BACKGROUND INFORMATION

In January, the projected budget deficit for FY 2008-09 was \$14.5 billion. Left unaddressed, the projected gap would grow to \$24.3 billion based on updated revenue projections, revised caseload estimates and higher costs. The single largest factor contributing to this increase is a \$6 billion decrease in estimated General Fund revenues. During the Special Session of the Legislature, lawmakers reduced the overall budget deficit, thereby leaving a remaining budget gap of \$17.2 billion.

The Governor's May Revise proposes borrowing against Lottery revenues, imposes strict spending cuts in the current and future budget years, and does not raise taxes. It also calls for the creation of the Revenue Stabilization Fund (also known as the Rainy Day Fund), where revenues above a reasonable, long-term average rate of growth will be deposited. Monies in the Rainy Day Fund will only be available for transfers to the General Fund to bring revenues up to the long-term average in years with below-average revenue growth, such as 2008-09.

If the Budget Stabilization Act, which would authorize the use of monetized lottery profits to fund the Rainy Day Fund, fails passage by voters on the November 2008 ballot, a fail-safe mechanism will be triggered which will enact a temporary one-cent sales tax increase. This increase would remain in effect until the Rainy Day Fund has reached the targeted fund balance (15 percent of General Fund tax revenues) or until June 30, 2011. Californians would then receive tax rebates equal to the aggregate amount of revenues collected during the temporary sales tax increase.

The FY 2008-09 budget consists of \$101.8 billion in total expenditures and \$104.7 billion in total resources available. Below are highlights from the May Revise that are of interest to the City. Specific Long Beach impacts are summarized in Attachment A.

LOCAL REVENUE TAKEAWAYS

The May Revise does not propose any revenue takeaways from local governments. Proposition 1A was not suspended, which would have allowed the State to borrow up to \$9 million in Long Beach property taxes, and Proposition 42, which funds local street and road improvements, remains fully funded.

However, the 10 percent reductions proposed in the Governor's January budget for the Public Library Foundation, as well as several public safety and health and human services programs, are still actively being proposed.

PUBLIC SAFETY

The May Revise proposes to replace \$151.8 million in General Fund dollars that currently support the Juvenile Probation Program with Temporary Assistance for Needy Families (TANF) Block Grant funds, and transfer the General Fund amount to the Department of Social Services.

The 10 percent reductions in the Citizen's Option for Public Safety (COPS) per-capita grants and the Booking Fee Reimbursement Program recommended in the Governor's January budget are still being actively proposed. This would result in a total reduction to Long Beach of \$101,000.

HEALTH AND HUMAN SERVICES

The May Revise proposes \$627 million in further General Fund cuts to Health and Human Services programs. However, the impact to Long Beach appears to be largely unchanged, as the reductions generally relate to services provided at the county level. The Long Beach Department of Health and Human Services estimates these reductions in funding for various programming totaling approximately \$430,665. The department has accounted for these reductions in its FY 2009 budget and the remainder of the FY 2008 fiscal year.

Proposed changes to Medi-Cal in the May Revise will require monthly re-certification in order for participants to maintain their eligibility. This may result in an increased number of people being unable to meet these requirements, which means more uninsured individuals and greater use of emergency room services.

SENIOR SERVICES

The May Revise contains a number of additional cuts to programs and funds related to senior services. Targeted for \$110.7 million in further reductions is In-Home Supportive Services (IHSS), which provides individuals who are blind, disabled, or over age 65 with personal assistance and in-home support so they can live in their homes rather than in an assisted living facility.

Although the Governor withdrew his proposal to reduce permitted hours of domestic and related services such as cleaning and shopping for recipients, he proposed the following alternative reductions:

- Limiting provision of domestic and related services to IHSS recipients with the highest levels of need, as measured by a functional index score of 4 or higher.
- The provision of other IHSS services to all recipients regardless of their functional index score will not be impacted (\$52.0 million).
- Requiring a share-of-cost for recipients with average functional index scores below 4 (\$27.7 million).

The revised budget additionally limits state participation in the wages of IHSS workers to the state minimum wage plus \$0.60 per hour for benefits (\$186.6 million). It maintains the 10 percent reduction of county administrative funding for IHSS,

along with a corresponding reduction in county workload. Specifically, this proposal would change the timeframe for re-assessing the condition of IHSS recipients from every 12 months to every 18 months. This would result in a savings of \$24.4 million (\$10.2 million of the General Fund).

The May Revise also contains the following cuts to other senior services:

- Proposes retaining funds from the January 2009 federal cost-of-living adjustment (COLA) for the Supplemental Security Income/State Supplementary Payment program, rather than passing them through to recipients, for savings of \$108.8 million. This is in addition to maintaining suspension of the June 2008 and June 2009 state COLAs (\$300.3 million).
- Maintains the elimination of the following optional Medi-Cal services for adults not in long-term care: chiropractors, incontinence creams and washes, acupuncture, adult dental, audiology, optometrists, opticians/optical labs, podiatry, psychology, and speech therapy (\$134.0 million).
- Maintains the elimination of payment of Medicare Part B benefits on behalf of Medi-Cal enrollees with an unmet share of cost. The administration assumes that these persons will pay the Part B premiums (almost \$100 per month) themselves. If not, then these persons will have to pay out of pocket for outpatient services up to their share of cost (\$66.5 million).
- Eliminates the Cash Assistance Program for Immigrants, which provides benefits to aged, blind, and disabled legal immigrants, resulting in savings of \$111.2 million.

INFRASTRUCTURE BOND IMPLEMENTATION

Proposition 1B: Transportation Bonds

The revised budget maintains the State's commitment to funding local infrastructure projects through Proposition 1B bond funds. It includes \$350 million to provide funding to local transit agencies for capital projects; \$500 million in Trade Corridors Improvement funds; and \$200 million in State and Local Partnership Program funds.

Proposition 1C: Housing Bonds

The revised budget maintains the proposed implementation of Proposition 1C reflecting a decrease of \$202 million, from \$973 million in 2007-08 to \$771 million in 2008-09. This includes \$30 million in planned awards for the Housing Urban-Suburban-and-Rural Parks Program. Proposition 1C expenditures reflect HCD's best estimate as to how much funding can be spent during the year.

Proposition 84: Water & Parks Bonds

The revised budget proposes to use \$13.5 million of Proposition 84 funds, rather than previously committed General Fund monies, for Colorado River water management projects. Existing law committed \$235 million of the General Fund for projects to reduce California's annual use of Colorado River water. \$13.5 million is the remaining balance of that commitment.

The May Revise maintains funding for a number of other Proposition 84 projects including:

- *Urban Greening/Forestry*: \$9.8 million to fund urban greening projects as a strategy to meet the greenhouse gas emission reduction goals (\$4.4 million), and to continue an urban forestry grant program (\$5.4 million).
- *Natural Communities Conservation Plan*: \$25 million for grants to local agencies to develop Natural Communities Conservation Plans.
- *Coastal Conservancy Programs*: \$89.1 million to carry out projects relating to the enhancement and development of the Santa Ana River Parkway, San Francisco Bay Area Conservancy Program, Monterey Bay, San Diego Bay and other projects statewide.
- *Ocean Protection Council*: \$26.4 million to improve the protection and management of California's ocean and coastal resources.
- *Capital Outlay and Grants*: \$8 million for capital outlay and local assistance projects in the Los Angeles and San Gabriel Rivers watersheds.
- *Grants to Local Corps and Watershed Restoration Projects*: \$33.3 million to provide \$12.5 million in grants to local conservation corps and \$3 million to the State Corps for projects to improve public safety and improve and restore watersheds, and \$20 million in grant funding to support local conservation corps programs and local resource conservation activities.

STATE TRANSIT ASSISTANCE PROGRAM

The revised budget eliminates a proposed increase for the State Transit Assistance Program, which provides funding to local transit agencies, and instead maintains the program's 2007-2008 level of funding at \$306 million. January's proposed budget funded the program at \$743 million; the additional funds will instead be used to offset General Fund expenditures for K-12 home-to-school transportation and debt service on current and prior year transportation-related General Obligation bonds.

STATE HIGHWAY FUNDING

State Highway Account, State Transportation Fund

The May Revise proposes loans from various special funds to provide one-time funding to the General Fund to help close the budget gap. These loans include \$200 million from the State Highway Account, which funds capital outlays and local assistance programs.

State Highway Operation and Protection Program (SHOPP)

Funding for the State Highway Operation and Protection Program (SHOPP) is \$100 million less than proposed in the Governor's January Budget due to further declines in projections for gasoline excise tax (per gallon) revenues (gasoline usage year over year also is down). Total excise tax revenues are projected to be \$225 million lower in 2008-09, but \$125 million in carryover funds from 2007-08 will be available to offset part of the shortfall. Total funding for SHOPP will be approximately \$2.5 billion in 2008-09.

SHOPP includes a range of rehabilitation projects that are intended to reduce hazardous road conditions, preserve bridges and roadways, enhance and protect roadsides, and improve operation of the state highway system. SHOPP is funded primarily from the State Highway Account from the State's two-thirds share of fuel excise tax revenues, weight fees, and federal funds.

CAREER TECHNICAL EDUCATION

The revised budget continues the same level of across-the-board cuts for most K-12 categorical programs that were proposed in January, including various Career Technical Education programs. However, it also maintains \$500 million for the Career Technical

Education Facilities Program, to create and equip facilities so that students can acquire skills necessary for technical careers. In addition, local assistance for Career Technical Education remains at the 2007-2008 level of \$20 million.

K-12 SCHOOLS & COMMUNITY COLLEGES

The Governor's January budget proposed to suspend Proposition 98 and reduce the Proposition 98 General Fund contribution to \$39.6 billion. However, the May Revise proposes to restore \$1.8 billion in funding for K-12 education and community colleges to fully fund the minimum Proposition 98 Guarantee in 2008-09. The Proposition 98 Guarantee for 2008-09 is projected to grow to \$56.8 billion, of which \$41.4 billion is from the General Fund.

The May Revise does not include cost-of-living adjustment (COLA) increases, which were included in the Governor's January budget. The \$2.4 billion COLA would have represented a 4.94 percent statutory increase and included:

- \$1.8 billion for Revenue Limits
- \$168.7 million for Special Education
- \$82.8 million for Child Care Programs
- \$62.3 million for Class Size Reduction
- \$52.9 million for the Targeted Instructional Improvement Grant
- \$49.1 million for Economic Impact Aid
- \$247.4 million for Various Categorical Programs

Proposition 98, the voter-approved constitutional amendment, guarantees minimum funding levels for K-12 schools and community colleges. The guarantee, which went into effect in the 1988-89 fiscal year, determines funding levels according to multiple factors including the level of funding in 1986-87, general fund revenues, per capita personal income, and school attendance growth or decline.

HIGHER EDUCATION

Since 2004, the University of California (UC) and California State University (CSU) have participated in a Higher Education Compact agreement with the Governor. The Compact provides a six-year resource plan to address annual base budget increases including general support increases of up to 5 percent, enrollment growth of 2.5 percent, student fee increases that may not exceed 10 percent, and other key program elements through 2010-11.

While the State's current budget deficit will prevent fulfillment of the provisions in the Higher Education Compact, additional General Fund resources are being provided to limit mandatory undergraduate fees to an increase of 7.4 percent for UC students and 10 percent for CSU students. Since an approved State budget is not expected until at least the Fall, and the May Revise did not include funding to cover mandatory cost increases, the CSU Board of Trustees recently voted to approve a \$276 per year fee increase, in order to provide appropriate planning and lead time for students prior to the Fall semester.

The May Revise also proposes 30 percent of projected Cal Grant costs be shifted from the General Fund to Temporary Assistance for Needy Families (TANF) Block Grant reimbursements from the Department of Social Services. The Cal Grant program, administered by the California Student Aid Commission, provides grant funds to eligible

prospective and current students that will be attending a qualifying California college, university, or career or technical school. Students can receive up to \$9,700 a year to pay for expenses including tuition, room and board, books, and other related supplies and materials.

REVIEW BY THE LEGISLATIVE ANALYST'S OFFICE (LAO)

On Monday, May 19, the Legislative Analyst's Office (LAO) released its analysis of the Governor's May Revise. The LAO believes that the proposed plan to securitize the lottery by borrowing \$15 billion against future profits is too optimistic and could exacerbate the State's financial problems. If these expected profits fail to materialize, the portion of lottery funds that go toward education could fall below current levels by about \$5 billion over the next twelve years combined.

The LAO also has concerns regarding the Governor's proposed budget reforms and believes that the proposed Rainy Day fund, which places a cap on how much of these funds may be transferred into the General Fund, would lock away lottery profits, making them unavailable for use in balancing the State's budget, even while the State could continue to run multi-billion dollar deficits. The Governor's budget reforms could also lead to across-the-board reductions in programs and services.

The LAO's proposed budget reforms include:

- Increasing the size of the current reserve requirements established in Proposition 58 to 10 percent of annual General Fund spending and making it more difficult for lawmakers to access these funds, thereby leading to more cost-conscious budgetary decisions to guard against financially over committing the State.
- Using the Rainy Day fund to capture some of the excess revenues the State experiences during prosperous economic times, thereby allowing spending levels to remain constant and bringing stability to the budgeting and appropriations processes.
- Eliminating tax credits for dependent children and seniors, and for companies that can claim research and development, as well as for hiring low-income workers.

In order to help reduce the State's budget deficit, the LAO is proposing that \$1.2 billion be taken from redevelopment agencies over the next 5 years to offset the State's obligations to schools. The LAO proposes the following three recommendations on how redevelopment agencies can help the State close its budget gap:

- Capture prior-year underreported redevelopment pass-through payments, which would reduce State obligations by an estimated \$70 million per year.
- Modify the redevelopment pass-through process to ensure funds are provided and reported on an ongoing basis, which should result in another \$28 million per year in savings to the State in reduced payments to schools.
- Require redevelopment agencies to contribute an additional 5 percent of their tax increment revenues to pass-through payments to schools (such as ERAF payments), which will offset the State's backfill to schools by around \$200 million.

While the LAO's report shows the ERAF (Education Revenue Augmentation Fund) cut for only one year, it has been learned that the LAO is assuming the cut will be made for 5 years in her estimates of future State deficits, which could lead to a permanent shift of ERAF funds from redevelopment agencies.

The LAO has revised its proposal on how the Legislature could successfully transition the supervision responsibilities of state parolees to counties. One of the two basic features of this new alternative financing proposal includes shifting Vehicle Licensing Fee (VLF) revenue that currently goes to cities (estimated by the LAO at \$149 million) and the DMV (estimated by the LAO at \$363 million) to counties to support state parole realignment. If this proposal were to be accepted by the Legislature, Long Beach would lose \$2.2 million in VLF revenue.

NEXT STEPS

We will continue to monitor the status of the State's budgeting process and strongly advocate against any proposed revenue takeaways from cities or redevelopment agencies, as the Legislature will now have the opportunity to create its own version of the budget. If you have any questions or require additional information, please contact Tom Modica, Manager of Government Affairs, at 8-5091.

Cc: Mayor and Members of the City Council
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Attachment
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POTENTIAL IMPACTS/BENEFITS FROM THE GOVERNOR'S FY 09 MAY REVISION OF THE STATE BUDGET

MAY 14, 2008

The State is projecting a \$24.3 billion deficit for FY 2008-09; after a special session of the Legislature made a down payment to address the deficit, the gap remaining is \$17.2 billion. The Governor's May Revise proposes borrowing against Lottery revenues, imposes strict spending cuts in the current and future budget years, and does not raise taxes. The FY 08-09 Budget consists of \$101.8 billion in total expenditures and \$104.7 billion in total resources available.

Key elements of the Governor's May Revise budget include:

- **A constitutional amendment, the Budget Stabilization Act (BSA):** To address volatile revenues and over-spending. It calls for the creation of the Revenue Stabilization Fund (RSF) where revenues above a reasonable, long-term average rate of growth will be deposited. Monies in the RSF will only be available for transfers to the General Fund to bring revenues up to the long-term average in years with below-average revenue growth, such as 2008-09.
- **Borrowing against improved performance of the California Lottery:** The revised budget proposes to improve performance of the lottery by providing operational flexibility and increasing participation. It also proposes to securitize future revenues resulting from the improved performance of the lottery to fund the RSF. It is anticipated that the proposed bonds will yield \$5.1 billion in revenue for the state budget in 2008-09, after providing education the \$1.2 billion in annual funding from the lottery that it currently receives.
- **Retaining the vast majority of proposed 10 percent reductions across the board:** Most of these cuts were retained for General Fund departments and programs, Boards, Commissions, and elected offices (including the legislative and judicial branches), except where a reduction is in conflict with the State Constitution or impractical.
- **No new taxes:** No new taxes are being proposed in the Governor's budget, except for the potential fail-safe mechanism of a 1 percent sales tax increase if lottery revenues fall short or if the lottery ballot measure is not approved by voters in the November 2008 general election.
- **An increase of \$83 million in 2008-09 revenues compared to the January proposal:** Revenues include \$3.3 billion in 2007-08 from the sale of authorized Economic Recovery Bonds, \$1.9 billion from a change in accrual accounting, \$5.1 billion of lottery proceeds in 2008-09 from the proposed fund transfer from the Revenue Stabilization Fund to the General Fund, and \$1.4 billion in other initiatives.
- **Cuts to Health and Human Services:** \$627 million in reductions to health and human services programs, in addition to the \$4.5 billion in cuts proposed in January.
- **Maintains Education Funding:** Restores \$1.8 billion General Fund for K-12 education and community colleges to fully fund the minimum Proposition 98 Guarantee in 2008-2009.
- **Reductions to Public Safety Programs:** A \$115.2 million reduction for the California Department of Corrections and Rehabilitation, rather than the \$378.9 million reduction proposed in January. Savings will be achieved through operational and programmatic changes and a decrease in the inmate population, without releasing any inmates prior to their anticipated release date.
- **Funding for State Parks:** Proposes \$13.3 million in funding for the Department of Parks and Recreation. Removed proposed reductions that would have resulted in the closing of 48 state parks out of 278 existing parks; instead, fees at popular parks will be increased.

POTENTIAL IMPACTS/BENEFITS FROM THE GOVERNOR'S FY 09 MAY REVISION OF THE STATE BUDGET

MAY 14, 2008

Budget Impacts On Key Program Areas/Accounts

State Highway Operation & Protection Program (SHOPP)

- Total funding for 2008-09 for SHOPP will be \$2.5 billion
- This amount is \$100 million less than what was proposed in the Governor's January budget, due to project declines in the gasoline excise tax (per gallon) revenues (gasoline usage year over year is also down).
- Total excise tax revenues will be \$225 million lower in 2008-09, but will be offset by \$125 million in carryover funds from 2007-08.

State Transportation Fund

- Proposes loans totaling \$288.7 million from various special funds to provide one-time funding to the General Fund to help close the budget gap.
- Special funds impacted by these loans include:
 - State Highway Account – Loss of \$200 million
 - Bicycle Transportation Account – Loss of \$6 million
 - Environmental Enhancement and Mitigation Program Fund – Loss of \$4.4 million
- Other special funds impacted include a loss of \$12.9 million to the Housing Rehabilitation Loan Fund.
- Budget trailer legislation is proposed that would provide the State Highway Account authority to borrow from the Pooled Money Investment Account to reduce the need to carry a large cash balance.

Juvenile Probation Funding

- Proposes to replace \$151.8 million in General Fund that currently supports the Juvenile Probation Program with Temporary Assistance for Needy Families (TANF) Block Grant Funds, and transfer the General Fund to the Department of Social Services.

K Thru 12 Education

- Proposes \$1.8 billion in additional funding for K-12 education and community colleges to fully fund the minimum Proposition 98 Guarantee in 2008-09.
- Total Proposition 98 funding for K-14 education programs will increase year over year by \$193 million.

Higher Education

- The State's current budget deficit will prevent fulfillment of the provisions in the Higher Education Compact, additional General Fund resources are being provided to limit mandatory undergraduate fees to an increase of 7.4% for UC students and 10% for CSU students.
- Proposes 30% of projected Cal Grant costs be shifted from the General Fund to TANF Block Grant reimbursements from the Department of Social Services.

POTENTIAL IMPACTS/BENEFITS FROM THE GOVERNOR'S FY 09 MAY REVISION OF THE STATE BUDGET

MAY 14, 2008

Positive City of Long Beach Impacts

- The Governor **did not** suspend Proposition 1A (2004), which would enable the borrowing of local government property tax. The State has the ability to borrow up to \$9 million in Long Beach property tax.
- The Governor **did not** borrow from Proposition 42, which was recently protected by Proposition 1A (2006). Proposition 42 is fully funded, which could mean up to \$4.7 million for Long Beach local streets and road improvements in FY 09.
- The Governor **did not** postpone the \$8 million in Proposition 1B local streets and roads funding Long Beach is expecting this fiscal year.
- The Governor is recommending aggressive implementation of both Proposition 1B and 1C, which will provide grants for many important City programs. A list of bond areas the City may benefit from is included below:

<u>Proposition 1B</u>	<u>Proposition 1C</u>
<ul style="list-style-type: none">○ \$500 million for Trade Corridors○ \$200 million for State/Local Partnerships○ \$1,547 million for Corridor Mobility○ \$1,186 for the State Transportation Improvement Program (STIP)○ \$250 million for Air Quality○ \$58 million for Port Security○ \$216 million for State Highway Operations and Protection Program (SHOPP)○ \$65 million for Grade Separation Program	<ul style="list-style-type: none">○ \$188 million for Affordable Homeownership○ \$194 million for Multifamily Rental Housing○ \$24 million for Emergency Housing Assistance○ \$200 million for Infill Incentives Grant Program○ \$95 million for Transit Oriented Development○ \$30 million for Housing Urban-Suburban and Rural Parks

**POTENTIAL IMPACTS/BENEFITS FROM THE GOVERNOR'S FY 09 MAY REVISION OF THE STATE
BUDGET**

MAY 14, 2008

Negative City of Long Beach Impacts

Description of Impact	Department	Estimated FY 09 Reduced Amounts
10 percent reduction in Citizen's Option for Public Safety per-capita grants	Police Department	\$95,000
10 percent Booking Fee Reimbursement Program reduction	Police Department	\$6,000
Public Library Foundation reduced by 10 percent	Library Services	\$29,000
AIDS/Youth Health Programs	Health and Human Services	\$181,070
Maternal and Child Health Programs	Health and Human Services	\$52,917
Communicable Disease	Health and Human Services	\$40,950
Public Health Emergency Preparedness	Health and Human Services	\$11,832
Epidemiology Investigations	Health and Human Services	\$946
10 percent reduction in Environmental Health (includes water quality and recreational water testing programs)	Health and Human Services	\$5,000
10 percent reduction in SB 90 – Mandated Cost Reimbursement	Health and Human Services	\$14,400
Vehicle License Fee (VLF) Funds Used to Support Core Public Health Activities	Health and Human Services	\$10,000
MEDI-CAL Revenue*	Health and Human Services	\$113,550
Substance Abuse Program	Health and Human Services	\$23,563
Emergency Shelter Program for local governments (1,900 fewer available shelter beds statewide)**	Health and Human Services	\$0
TOTAL		\$ 584,228

*122,000 individuals are currently enrolled in Medi-Cal and SCHIP programs, and the proposed State budget may result in an estimated 10 percent of them becoming ineligible to receive health coverage. It is estimated that up to 2,000 individuals (1,000 children) may lose coverage locally.

**The Department of Health and Human Services does not directly receive any State Housing and Community Development (HCD) Emergency Housing Assistance Program funds; however, several Long Beach shelters do receive these funds, such as the Winter Shelter.