

THE GOVERNOR'S BUDGET FOR 1983-84

FEBRUARY 28, 1983

LEGISLATIVE ANALYST

STATE OF CALIFORNIA

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THE GOVERNOR'S BUDGET FOR 1983-84
STATEMENT TO THE SENATE FINANCE COMMITTEE
FEBRUARY 28, 1983

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

IN ENACTING AB 28X, THE LEGISLATURE HAS PUT IN PLACE A MECHANISM DESIGNED TO AVOID A DEFICIT IN THE STATE'S GENERAL FUND AT THE END OF FISCAL YEAR 1983-84. IT IS WITH THIS MECHANISM AS A BACKGROUND THAT I WOULD LIKE TO SUMMARIZE OUR CONCLUSIONS REGARDING THE GOVERNOR'S BUDGET FOR THE UPCOMING FISCAL YEAR.

I. AN OVERVIEW OF THE GOVERNOR'S BUDGET

THE AB 28X TRIGGERS

DESCRIPTION. AB 28X HAS PLACED INTO LAW TWO PROVISIONS THAT COULD TRIGGER A ONE-CENT SALES TAX INCREASE IN ORDER TO SUPPLEMENT THE AMOUNT OF REVENUES AVAILABLE TO THE GENERAL FUND UNDER EXISTING LAW. THESE TRIGGERS ARE INTENDED TO SERVE TWO ENTIRELY DIFFERENT PURPOSES:

- TRIGGER #1 (OCTOBER 15, 1983) IS YOUR PARTIAL INSURANCE POLICY AGAINST FURTHER REVENUE SHORTFALLS. IT WOULD RESULT IN A ONE-CENT SALES TAX INCREASE, EFFECTIVE NOVEMBER 1, ONLY IF ACTUAL GENERAL FUND REVENUE COLLECTIONS DURING THE FIRST

100 DAYS OF THE BUDGET YEAR FALL SHORT OF THE AMOUNT ANTICIPATED IN THE GOVERNOR'S BUDGET BY \$150 MILLION OR MORE. CONSEQUENTLY, YOU CANNOT RELY ON THIS TRIGGER TO HELP FINANCE THE DEFICIT PROJECTED FOR THE CURRENT YEAR THAT WILL BE ROLLED OVER INTO THE BUDGET YEAR.

- TRIGGER #2 (JANUARY 10, 1984) IS YOUR DEFICIT-FINANCING MECHANISM. IT WOULD RAISE THE SALES TAX BY ONE CENT IF THE DIRECTOR OF FINANCE PROJECTS A YEAR-END GENERAL FUND BALANCE OF LESS THAN \$100 MILLION AFTER THE CARRY-OVER DEFICIT HAS BEEN FINANCED.

THESE TWO TRIGGERS ARE DISPLAYED IN DIAGRAM 1

ARE THE TRIGGERS FAIL-SAFE? THESE PROVISIONS OF AB 28X GO A LONG WAY TOWARD ASSURING THAT, UNLIKE 1981-82 AND 1982-83, FISCAL YEAR 1983-84 WILL NOT END WITH THE GENERAL FUND IN THE RED. THEY DO NOT, HOWEVER, GUARANTEE THE AVOIDANCE OF A YEAR-END DEFICIT IN 1983-84. A DEFICIT COULD STILL RESULT ON JUNE 30, 1984 UNDER ONE OF THREE CIRCUMSTANCES:

- THE ECONOMY--AND THEREFORE, GENERAL FUND REVENUES--DO NOT PERFORM AS WELL DURING THE SECOND HALF OF 1983-84 AS NEXT YEAR'S BUDGET ANTICIPATES.

WERE THIS TO HAPPEN, THE STATE COULD END THE YEAR IN THE HOLE, JUST AS IT DID IN 1981-82.

- GENERAL FUND EXPENDITURES TURN OUT TO BE MORE THAN \$100 MILLION HIGHER THAN THE AMOUNT ANTICIPATED IN THE 1983-84 COLUMN OF NEXT YEAR'S BUDGET. THIS COULD OCCUR, FOR EXAMPLE, IF COURT DECISIONS PUSHED UP GENERAL FUND COSTS, AS THEY DID IN THE CURRENT YEAR.
- THE ADMINISTRATION, IN AN EFFORT TO AVOID AN INCREASE IN THE SALES TAX ON FEBRUARY 1, PROPOSES A SERIES OF CHANGES IN THE BUDGET ADOPTED FOR 1983-84 WHICH THE LEGISLATURE IS UNWILLING TO APPROVE. THIS WOULD SHORT-CIRCUIT THE SALES TAX TRIGGER, BUT LEAVE THE GENERAL FUND IN DEFICIT ON JUNE 30, 1984.

NOTWITHSTANDING THESE POSSIBILITIES, HOWEVER, WE CONCLUDE THAT THE AB 28X TRIGGERS PROVIDE THE LEGISLATURE WITH A REASONABLE DEGREE OF PROTECTION AGAINST THE KIND OF "CRISIS BUDGETING" THAT HAS FORCED UPON YOU IN THE PAST AND CURRENT YEARS.

WHAT IS THE LIKELIHOOD OF THE TRIGGERS BEING PULLED?

CURRENT OUTLOOK. THE QUESTION THAT I'M SURE IS ON MOST EVERYBODY'S MIND THESE DAYS IS: WILL ONE OF THE TWO AB

28X TRIGGERS BE PULLED? TABLE 1 PROVIDES A STARTING POINT FOR DEVELOPING AN ANSWER TO THIS QUESTION.

TABLE 1

PORTION OF THE 1982-83 GENERAL FUND DEFICIT THAT
CAN BE FINANCED WITH REVENUES PROJECTED FOR THE BUDGET YEAR
(IN MILLIONS)

PROJECTED DEFICIT, JUNE 30, 1983 (AS SHOWN IN THE GOVERNOR'S BUDGET)		\$1,457
FACTORS INCREASING THE DEFICIT SINCE THE BUDGET WAS SUBMITTED: COURT DECISION IN VALDES V. CORY		177
IMPACT OF ACTIONS TO REDUCE THE DEFICIT:		
EXECUTIVE ORDER	\$-70	
AB 28X	<u>-568</u>	
SUBTOTAL		<u>-\$638</u>
PROJECTED DEFICIT, JUNE 30, 1983 (CURRENT ESTIMATE)		\$996
AMOUNT IN THE RESERVE THAT CAN BE APPLIED TO THE DEFICIT:		
RESERVE, AS SHOWN IN THE BUDGET	\$650	
LESS: FUNDS ALREADY COMMITTED BY EXISTING LAW	<u>-100</u>	
AMOUNT AVAILABLE TO FINANCE THE DEFICIT		<u>-550</u>
PROJECTED DEFICIT, JUNE 30, 1984 (CURRENT ESTIMATE)		\$446
MINIMUM RESERVE BALANCE SPECIFIED BY AB 28X		<u>100</u>
AMOUNT OF ADDITIONAL REVENUES/EXPENDITURE SAVINGS NEEDED TO AVOID A SALES TAX INCREASE		\$546

AS THE TABLE SHOWS, IF CURRENT REVENUE AND EXPENDITURE ESTIMATES PROVE TO BE ON TARGET, THE GENERAL FUND WILL END THE BUDGET YEAR WITH A DEFICIT OF \$446 MILLION. UNDER THESE CIRCUMSTANCES, TRIGGER NO. 2 WOULD BE PULLED ON JANUARY 10, 1984, AND THE STATE PORTION OF THE SALES TAX WOULD INCREASE FROM 4.75 PERCENT TO 5.75 PERCENT ON FEBRUARY 1. THUS, IF CURRENT PROJECTIONS HOLD, AN INCREASE IN THE SALES TAX WILL OCCUR NEXT YEAR.

HOW COULD A SALES TAX INCREASE BE AVOIDED? AS NOTED EARLIER, AB 28X WILL AUTOMATICALLY INCREASE THE SALES TAX ON FEBRUARY 1, 1984 UNLESS THE DIRECTOR OF FINANCE PROJECTS A GENERAL FUND BALANCE ON JUNE 30, 1984 OF AT LEAST \$100 MILLION AFTER THE CARRYOVER DEFICIT HAS BEEN FULLY LIQUIDATED. CONSEQUENTLY, ONE OF TWO THINGS MUST OCCUR IF A SALES TAX INCREASE IS TO BE AVOIDED IN 1983-84:

- GENERAL FUND REVENUES MUST EXCEED THE AMOUNTS PROJECTED IN THE BUDGET FOR 1982-83 AND 1983-84 BY AT LEAST \$546 MILLION.
- THE LEGISLATURE OR THE GOVERNOR MUST REDUCE EXPENDITURES FROM THE LEVELS CALLED FOR IN THE GOVERNOR'S BUDGET BY AT LEAST \$546 MILLION.

(OF COURSE, A COMBINATION OF HIGHER-THAN-ANTICIPATED REVENUES AND EXPENDITURE REDUCTIONS TOTALING AT LEAST \$546 MILLION WOULD ALSO FORESTALL A TAX INCREASE UNDER AB 28X.)

AT THIS POINT, I WILL TURN TO THE GOVERNOR'S REVENUE AND EXPENDITURE ESTIMATES AND EXAMINE THEM FROM THE STANDPOINT OF WHETHER IT IS REALISTIC TO EXPECT CHANGES OF THIS MAGNITUDE.

REVENUES PROJECTED IN THE GOVERNOR'S BUDGET

REASONABLENESS OF THE ESTIMATES. THE RESULTS OF OUR DETAILED ANALYSIS OF THE GOVERNOR'S REVENUE ESTIMATES FOR THE CURRENT AND BUDGET YEARS APPEAR ON PAGES 51-93 OF THE 1983-84 BUDGET: PERSPECTIVES AND ISSUES. GENERALLY, WE CONCLUDE THAT:

- THE DEPARTMENT OF FINANCE'S ECONOMIC FORECAST IS IN LINE WITH THOSE PUBLISHED BY OTHER PUBLIC AND PRIVATE FORECASTERS (SEE TABLES 26 AND 27, PAGES 67-68 OF PERSPECTIVES AND ISSUES).
- THE REVENUE PROJECTIONS FOR THE CURRENT AND BUDGET YEARS ARE REASONABLE, GIVEN THE DEPARTMENT'S ECONOMIC FORECAST.

AT THE PRESENT TIME, WE BELIEVE THAT REVENUES ARE MORE LIKELY TO EXCEED, THAN TO FALL SHORT OF, THE BUDGET PROJECTIONS. SINCE THE BUDGET WAS PREPARED, MOST OF THE SIGNALS THAT HAVE BEEN SENT BY THE ECONOMY HAVE BEEN ENCOURAGING FROM A REVENUE STANDPOINT. FOR EXAMPLE, DOMESTIC CAR SALES AND HOUSING HAVE BEEN IMPROVING, NEW

UNEMPLOYMENT INSURANCE CLAIMS HAVE FALLEN, THE PRIME INTEREST RATE HAS BEEN CUT, AND THERE HAS BEEN A DRAMATIC REDUCTION IN INVENTORIES. WHILE THESE FACTORS DO NOT, BY THEMSELVES, GUARANTEE A SUSTAINED ECONOMIC RECOVERY, THEY CERTAINLY GIVE THE APPEARANCE THAT THE ECONOMY IS PULLING OUT OF THE RECESSION.

FURTHERMORE, GENERAL FUND REVENUES DURING THE MONTHS OF DECEMBER AND JANUARY WERE \$107 MILLION HIGHER THAN THE AMOUNT ANTICIPATED IN THE BUDGET. THIS PATTERN APPEARS TO BE CONTINUING IN FEBRUARY, ALTHOUGH WE WON'T HAVE ANY FIRM FIGURES ON FEBRUARY COLLECTIONS FOR ANOTHER 10 DAYS TO 2 WEEKS.

UNCERTAINTY. MUCH AS YOU DISLIKE HEARING IT, I MUST ONCE AGAIN EMPHASIZE THE UNCERTAINTY SURROUNDING THESE AND EVERYONE ELSE'S ECONOMIC AND REVENUE PROJECTIONS. UNFORTUNATELY, WE CAN BE NO MORE CONFIDENT ABOUT OUR REVENUE FORECASTS THAN WE CAN BE ABOUT THE COURSE OF THE FEDERAL RESERVE BOARD'S MONETARY POLICY, CONGRESSIONAL ACTION ON THE PRESIDENT'S BUDGET FOR 1984, THE PRICING POLICIES THAT WILL BE FOLLOWED BY PETROLEUM EXPORTING COUNTRIES, OR THE WEATHER.

THE RANGE OF UNCERTAINTY REGARDING THE PERFORMANCE OF THE ECONOMY IN THE FUTURE IS WIDE ENOUGH THAT ANY BUDGET YOU

ENACT COULD BE THROWN OUT OF KILTER. AS SHOWN IN TABLE 39, PAGE 89 OF PERSPECTIVES AND ISSUES, ALTERNATIVE ECONOMIC ASSUMPTIONS THAT ARE WELL WITHIN THE RANGE OF POSSIBILITY COULD LEAVE THE GENERAL FUND WITH \$1.6 BILLION LESS OR \$1.4 BILLION MORE THAN WHAT THE BUDGET ANTICIPATES.

I REPEAT, HOWEVER, THAT IN MY JUDGMENT, REVENUES ARE MORE LIKELY TO EXCEED, THAN TO FALL SHORT OF, THE BUDGET ESTIMATES. UNFORTUNATELY, SO ARE EXPENDITURES.

THE LEVEL OF EXPENDITURES PROPOSED BY THE GOVERNOR

REASONABLENESS OF THE ESTIMATES. OUR ANALYSIS CLEARLY DEMONSTRATES THAT THE COST OF RUNNING STATE GOVERNMENT IN 1983-84 WILL EXCEED THE \$21.7 BILLION ESTIMATE SHOWN IN THE GOVERNOR'S BUDGET UNLESS THE PROGRAM LEVELS PROPOSED BY THE GOVERNOR ARE REDUCED. IN SHORT, THE BUDGET IS UNDERFUNDED.

IN SAYING THAT THE BUDGET IS UNDERFUNDED, I AM NOT REFERRING TO THOSE POLICY DECISIONS MADE BY THE ADMINISTRATION IN PUTTING TOGETHER THE BUDGET FOR 1983-84 THAT LEFT NUMEROUS PROGRAMS WITH LESS MONEY THAN THEY RECEIVED IN THE CURRENT YEAR. THIS, OF COURSE, IS THE GOVERNOR'S PPREROGATIVE. NOR AM I REFFRRING TO THE LEGISLATION ENACTED IN 1982 FOR WHICH THE GOVERNOR DOES NOT REQUEST FUNDING. HERE AGAIN, AS A STATEMENT OF HIS PRIORITIES (RATHER THAN YOURS), THE BUDGET IS COMPLETE.

WHAT I AM REFERRING TO IS THE NUMEROUS INSTANCES IN WHICH THE BUDGET DOES NOT PROVIDE SUFFICIENT FUNDS TO ACCOMPLISH EITHER WHAT THE ADMINISTRATION ITSELF PROPOSES TO ACCOMPLISH OR WHAT THE STATE CONSTITUTION REQUIRES.

FOR EXAMPLE, ITEM 9620 OF THE BUDGET BILL REQUESTS \$1 MILLION TO PAY INTEREST ON LOANS TO THE GENERAL FUND. TO SAY THAT THIS AMOUNT IS INSUFFICIENT TO PAY THE INTEREST ON LOANS CONTEMPLATED BY THE ADMINISTRATION IS AN UNDERSTATEMENT OF THE FIRST ORDER. WE ESTIMATE THAT THE \$1 MILLION BUDGETED FOR THIS PURPOSE WILL BE EXHAUSTED 10 DAYS INTO THE FISCAL YEAR. MORE LIKE \$75 MILLION WILL BE NEEDED TO PAY INTEREST ON LOANS TO THE GENERAL FUND DURING 1983-84.

OTHER BUDGET ITEMS THAT APPEAR TO BE UNDERFUNDED INCLUDE THE FOLLOWING:

- DEPARTMENT OF HEALTH SERVICES: MEDI-CAL WORKLOAD AND COURT DECISIONS (\$31,345,000)
- DEPARTMENT OF REHABILITATION: WORK ACTIVITY CASELOAD GROWTH (\$6,000,000)
- DEPARTMENT OF THE YOUTH AUTHORITY: PROJECTED WARD POPULATION (UNKNOWN)
- DEPARTMENT OF CONSERVATION: MAMMOTH LAKES VOLCANIC HAZARD MONITORING (UNKNOWN)

● DEPARTMENT OF SOCIAL SERVICES: FRAUD EARLY
DETECTION AND PREVENTION PROGRAM (UNKNOWN)

A MORE COMPLETE LISTING OF PROGRAMS THAT APPEAR TO BE
UNDERFUNDED IN THE GOVERNOR'S BUDGET APPEARS IN APPENDIX I.

SECOND, THE BUDGET IS UNDERFUNDED IN THAT IT DOES NOT
MAKE ADEQUATE PROVISION FOR THE COST OF THE PENDING LOCAL
GOVERNMENT CLAIMS BILL. CLAIMS APPROVED BY THE BOARD OF
CONTROL THROUGH JANUARY 1982 AMOUNT TO \$185 MILLION.
ACCORDING TO THE DIRECTOR OF FINANCE, HOWEVER, THIS AMOUNT
WILL HAVE TO BE FINANCED WITHIN THE \$150 MILLION RESERVE FOR
FUTURE FINANCIAL LEGISLATION--CLEARLY AN IMPOSSIBLE TASK
UNLESS THE LEGISLATURE CHOOSES NOT TO FUND SOME OF THESE
CLAIMS.

THIRD, THE BUDGET IS COUNTING ON \$260 MILLION IN
UNIDENTIFIED SAVINGS TO HOLD SPENDING IN 1983-84 TO \$21.7
BILLION. MOST OF THESE SAVINGS (\$200 MILLION) ARE EXPECTED
TO RESULT FROM THE WORK OF GOVERNMENT EFFICIENCY TEAMS THAT
THE GOVERNOR PROPOSES TO ESTABLISH.

I HEARTILY APPROVE OF THE GOVERNOR'S PROPOSAL TO SEEK
HELP FROM THE PRIVATE SECTOR IN MAKING GOVERNMENT MORE
EFFICIENT. TO TAKE THE NEXT STEP, HOWEVER, AND COUNT ON
THESE SAVINGS IN PREPARING THE BUDGET FOR 1983-84 IS, IN MY
JUDGMENT, UNWISE. THIS IS NOT JUST COUNTING CHICKENS BEFORE

THE EGGS ARE HATCHED; IT'S COUNTING THEM BEFORE THE POOSTEP HAS BEEN BROUGHT TO THE HEN HOUSE.

CAN FURTHER CUTS IN THE GOVERNOR'S BUDGET BE MADE?

DESPITE THE FACT THAT THE GOVERNOR HAS PRESENTED YOU WITH AN EXTREMELY TIGHT BUDGET, WE BELIEVE FURTHER CUTS IN SPENDING LEVELS ARE FEASIBLE. IN FACT, OUR ANALYSIS OF THE 1983-84 BUDGET BILL INDICATES THAT \$507 MILLION IN FURTHER SPENDING REDUCTIONS (ALL FUNDS) ARE WARRANTED ON ANALYTICAL GROUNDS. OF THE TOTAL, \$274 MILLION IN REDUCTIONS ARE IN GENERAL FUND ITEMS. AS TABLE 2 SHOWS, WHEN THE POTENTIAL SAVINGS FROM THESE GENERAL FUND REDUCTIONS ARE ADDED TO THE ADDITIONAL RESOURCES THAT WOULD BE MADE AVAILABLE TO THE GENERAL FUND IF ALL OUR RECOMMENDATIONS WERE APPROVED, THE RESULT IS A NET POTENTIAL IMPROVEMENT IN THE GENERAL FUND CONDITION OF \$495 MILLION.

TABLE 2

IMPACT OF LEGISLATIVE ANALYST'S FISCAL RECOMMENDATIONS ON
THE GENERAL FUND AND SPECIAL FUNDS
(IN MILLIONS)

	<u>GENERAL FUND</u>	<u>SPECIAL FUNDS</u>	<u>TOTAL</u>
APPROPRIATION REDUCTIONS	\$273,822	\$233,003	\$506,825
APPROPRIATION AUGMENTATIONS	<u>-3,991</u>	<u>-10,737</u>	<u>-14,728</u>
SUBTOTAL, NET IMPACT OF RECOMMENDATIONS ON APPROPRIATIONS	\$269,831	\$222,266	\$492,097
REVENUE REDUCTIONS	-\$48	-\$41,116	-\$41,164
REVENUE AUGMENTATIONS	<u>75,743</u>	<u>--</u>	<u>75,743</u>
SUBTOTAL, NET IMPACT OF RECOMMENDATIONS ON REVENUES	\$75,695	-\$41,116	-\$34,579
TRANSFER OF FUNDS TO GENERAL FUND	\$49,034	--	\$49,034
CHANGE SOURCE OF SUPPORT FROM GENERAL FUND TO OTHER FUNDS	<u>100,080</u>	<u>--</u>	<u>100,080</u>
NET EFFECT ON FUND CONDITION	\$494,640	\$181,150	\$675,790

OF COURSE, WE ARE WELL AWARE OF THE FACT THAT AS YOU CONSIDER OUR RECOMMENDATIONS TO REDUCE SPENDING, YOU WILL ALSO BE UNDER INTENSE PRESSURE TO ADD TO THE GOVERNOR'S BUDGET. OUR ANALYSIS INDICATES THAT FROM THE STANDPOINT OF PURCHASING POWER, THE PROPOSED BUDGET IS 7.3 PERCENT LESS THAN THE BUDGET FOR THE CURRENT YEAR. IN FACT, IF YOU EXCLUDE LOCAL GOVERNMENT FISCAL RELIEF, YOU HAVE TO GO BACK 10 YEARS (TO 1973-74) TO FIND A GENERAL FUND BUDGET THAT COULD BUY LESS SERVICES THAN THE ONE PROPOSED BY THE GOVERNOR FOR 1983-84.

II. SUGGESTIONS FOR FACILITATING ACTION ON THE GOVERNOR'S BUDGET 1983-84

CLEARLY, YOU FACE AN EXTREMELY DIFFICULT TASK IN PUTTING TOGETHER A BUDGET FOR 1983-84. WHILE I KNOW OF NO WAY THIS TASK CAN BE MADE EASY, I HAVE SOME SUGGESTIONS WHICH I BELIEVE CAN MAKE IT EASIER FOR YOU TO ACCOMPLISH YOUR OBJECTIVES WITHIN THE LIMITS OF AVAILABLE FUNDS.

1. EXPAND THE BUDGET PROCESS TO INCLUDE A REVIEW OF TAX EXPENDITURES (PAGES 116-121 OF PERSPECTIVES AND ISSUES)

IF EVER THERE WAS A YEAR IN WHICH A RIGOROUS REVIEW OF SO-CALLED "TAX EXPENDITURES" WAS WARRANTED, THIS IS IT.

ONE WAY OF LOOKING AT THE GOVERNOR'S BUDGET FOR 1983-84 IS TO OBSERVE THAT THE ADMINISTRATION IS PROPOSING A

1.7 PERCENT (\$379 MILLION) DECREASE IN GENERAL FUND EXPENDITURES AND A 7.7 PERCENT (\$639 MILLION) INCREASE IN "TAX EXPENDITURES"--THE AMOUNT "SPENT" THROUGH THE TAX SYSTEM AS A RESULT OF THE VARIOUS TAX EXCLUSIONS, EXEMPTIONS, PREFERENTIAL TAX RATES, CREDITS AND DEFERRALS. I QUESTION WHETHER THIS PROPOSED ALLOCATION OF RESOURCES AVAILABLE TO THE GENERAL FUND REFLECTS YOUR PRIORITIES AS WELL AS THE GOVERNOR'S.

SPECIFICALLY, I QUESTION WHETHER THE FOLLOWING SETS OF PROPOSALS REFLECTED IN THE BUDGET ARE CONSISTENT WITH YOUR OBJECTIVES:

- REDUCE STATE SUPPORT FOR THE DEPARTMENT OF AGING'S "BROWN BAG" PROGRAM (PROVIDES FOOD TO LOW-INCOME ELDERLY PERSONS) BY \$155,000, AND INCREASE THE STATE SUBSIDY FOR CANDY PURCHASES BY \$5 MILLION.
- REDUCE SUPPORT FOR COUNTY HEALTH SERVICES BY \$25 MILLION, AND INCREASE THE STATE SUBSIDY FOR LOCAL GOVERNMENT BORROWING BY \$7 MILLION.
- ELIMINATE FUNDING FOR MERIT PAY INCREASES TO STATE EMPLOYEES, AND CONTINUE THE STATE SUBSIDY FOR FEDERAL MILITARY EMPLOYEES.

CONSEQUENTLY, I URGE YOU TO SUBJECT TAX EXPENDITURES TO THE SAME TYPE OF RIGOROUS REVIEW THAT WILL BE GIVEN TO DIRECT BUDGET EXPENDITURES.

2. EXPAND THE BUDGET PROCESS TO INCLUDE A REVIEW OF STATE MANDATES
(PAGES 177-180 OF THE PERSPECTIVES AND ISSUES; PAGES 1316-1318 OF THE ANALYSIS.)

IN FIVE YEARS, THE COST OF REIMBURSING LOCAL GOVERNMENTS FOR THE EXPENSES THEY INCUR IN COMPLYING WITH STATE MANDATES HAS SHOT UP LIKE A ROCKET, RISING AT AN AVERAGE ANNUAL RATE OF 40 PERCENT. NO LONGER CAN THE COST OF THESE MANDATES BE IGNORED IN SETTING PRIORITIES FOR STATE SPENDING. IN FACT, WE ESTIMATE THAT THE COST OF REIMBURSING LOCAL GOVERNMENTS FOR MANDATED COSTS WILL EXCEED \$250 MILLION IN THE BUDGET YEAR.

AS A CONSEQUENCE, I BELIEVE YOU SHOULD SCRUTINIZE THE COST AND BENEFITS OF THESE MANDATES, USING THE SAME STANDARDS YOU APPLY TO OTHER PROGRAMS FUNDED IN THE BUDGET. SPECIFICALLY, I RECOMMEND THAT YOU ESTABLISH A PROCESS WHEREBY THE STATE AND LOCAL GOVERNMENTS, IN A COOPERATIVE EFFORT, SEEK TO IDENTIFY MANDATES THAT DO NOT WARRANT THE COST TO THE STATE OF PAYING FOR THEM.

3. ADOPT A CONSISTENT POLICY TOWARD INFLATION/COST-OF-LIVING ADJUSTMENTS BEFORE BUDGET HEARINGS
(PAGES 125-129 OF PERSPECTIVES AND ISSUES.)

OUR ANALYSIS INDICATES THAT THERE IS NO CONSISTENCY REGARDING TO HOW INFLATION OR COST-OF-LIVING ADJUSTMENTS ARE TREATED IN THE BUDGET. GENERALLY, THOSE PROGRAMS

CATEGORIZED AS "LOCAL ASSISTANCE" ARE BUDGETED FOR A 3 PERCENT INCREASE IN ORDER TO COMPENSATE FOR INFLATION, WHILE SIMILAR PROGRAMS OR ACTIVITIES CATEGORIZED AS STATE OPERATIONS ARE BUDGETED TO RECEIVE INCREASES OF 5 PERCENT OR MORE. CONSEQUENTLY, IN MANY CASES THE FUNDING LEVELS PROPOSED BY THE ADMINISTRATION REFLECT BUDGET ACCOUNTING PROCEDURES, RATHER THAN POLICY CONSIDERATIONS.

ACCORDINGLY, WE SUGGEST THAT THE FULL COMMITTEE DECIDE PRIOR TO SUBCOMMITTEE HEARINGS WHAT ITS POLICY TOWARD INFLATION/COST-OF-LIVING ADJUSTMENTS WILL BE.

4. LIMIT THE JUDICIARY'S OPPORTUNITY TO THWART LEGISLATIVE PRIORITIES
(PAGES 201-204 OF THE PERSPECTIVES AND ISSUES;
PAGES 869-873 AND 1069 OF THE ANALYSIS.)

OUR ANALYSIS INDICATES THAT IN THE CURRENT FISCAL YEAR ALONE, COURT DECISIONS HAVE "COST" THE STATE'S GENERAL FUND \$431 MILLION. THE JUDICIAL BRANCH'S ACTIONS IN OVERTURNING DECISIONS MADE BY A MAJORITY (OFTEN, A TWO-THIRDS MAJORITY) OF THIS LEGISLATURE HAS THREE SERIOUS CONSEQUENCES. SPECIFICALLY, THEY:

- A. MAKE IT DIFFICULT FOR THE LEGISLATURE TO SET PRIORITIES IN THE BUDGET PROCESS AND MAKE THESE PRIORITIES STICK.

- B. MAKE IT DIFFICULT FOR THE LEGISLATURE TO CONTROL STATE EXPENDITURES AND KEEP THE GENERAL FUND BUDGET IN BALANCE.
- C. FORCE THE LEGISLATURE TO MAKE DEEPER CUTS IN PROGRAM AREAS TO WHICH IT ASSIGNS A HIGHER PRIORITY.

WE BELIEVE THERE ARE SEVERAL STEPS THE LEGISLATURE COULD TAKE THAT WOULD MINIMIZE (THOUGH CERTAINLY NOT ELIMINATE) THE POTENTIAL FOR THE COURTS TO OVERTURN LEGISLATIVE PRIORITIES. THESE STEPS INCLUDE:

- DEFINING LEGISLATIVE INTENT MORE CLEARLY IN THE LEGISLATION IT ENACTS.
- SIMPLIFYING THE PROCEDURAL REQUIREMENTS WHICH ADMINISTRATIVE AGENCIES MUST FOLLOW IN IMPLEMENTING THE LAWS PASSED BY THE LEGISLATURE.

ACCORDINGLY, I RECOMMEND THAT THIS COMMITTEE HOLD OVERSIGHT HEARINGS ON HOW THE PROCESS FOR ENACTING AND IMPLEMENTING LEGISLATION CAN BE IMPROVED SO AS TO PREVENT THE COURTS FROM OVERTURNING LEGISLATIVE SPENDING AND POLICY DECISIONS.

5. DECIDE HOW TIDELANDS OIL REVENUES SHOULD BE ALLOCATED
BEFORE BUDGET HEARINGS
(PAGES 121-124 OF THE PERSPECTIVES AND ISSUES.)

WE CONTINUE TO BELIEVE THAT YOUR FISCAL FLEXIBILITY WOULD BE ENHANCED SIGNIFICANTLY IF TIDELANDS OIL AND GAS REVENUES WERE DEPOSITED DIRECTLY IN THE GENERAL FUND, INSTEAD OF IN NUMEROUS SPECIAL FUNDS. IN SAYING THIS, I DO NOT MEAN TO IMPLY THAT THE PROJECTS AND ACTIVITIES FINANCED BY THESE SPECIAL FUNDS ARE SECOND-CLASS CITIZENS. MY RECOMMENDATION MERELY REFLECTS THE FACT THAT ANY OR ALL OF THESE PROJECTS AND ACTIVITIES COULD BE SUPPORTED FROM THE GENERAL FUND IF YOU ASSIGN TO THEM A SUFFICIENTLY HIGH PRIORITY. THE CURRENT ARRANGEMENT, HOWEVER, MAY LOCK YOU INTO FUNDING PROJECTS THAT HAVE A LESSER PRIORITY.

I REALIZE, HOWEVER, THAT YOU MAY CHOOSE TO RETAIN THESE REVENUES IN ONE OR MORE SPECIAL FUNDS ORIENTED TOWARD CAPITAL OUTLAY. IF YOU CHOOSE TO DO SO, HOWEVER, I RECOMMEND THAT YOU DECIDE AT THE OUTSET HOW TIDELANDS OIL AND GAS REVENUES ARE TO BE ALLOCATED BETWEEN THE GENERAL FUND AND THE VARIOUS SPECIAL FUNDS THAT RECEIVE THESE REVENUES UNDER EXISTING LAW. WHILE IT IS TRUE THAT THE COMMITTEE CAN REALLOCATE THESE REVENUES AT ANY TIME PRIOR TO ENACTMENT OF THE BUDGET BILL, PAST EXPERIENCE HAS DEMONSTRATED THAT IT IS MUCH EASIER TO DO SO BEFORE SPECIFIC FUNDING COMMITMENTS ARE MADE.

6. ESTABLISH A SPECIAL CAPITAL OUTLAY SUBCOMMITTEE
(PAGES 148-156 OF PERSPECTIVES AND ISSUES.)

OUR ANALYSIS INDICATES THAT THE STATE'S CAPITAL OUTLAY NEEDS ARE CONSIDERABLY GREATER THAN THE AMOUNT OF FUNDING AVAILABLE TO MEET THOSE NEEDS. WE BELIEVE THE LEGISLATURE CAN ENSURE THAT SUCH FUNDS AS ARE AVAILABLE ARE USED IN THE MOST PRODUCTIVE MANNER POSSIBLE IF IT EVALUATES STATEWIDE CAPITAL OUTLAY NEEDS AS A SINGLE PROGRAM AND APPLIES ITS PRIORITIES ON A STATEWIDE BASIS. AUTHORIZATION OF PROJECTS ON A DEPARTMENT-BY-DEPARTMENT BASIS MAY RESULT IN FUNDING FOR SOME PROJECTS TO WHICH THE LEGISLATURE WOULD ASSIGN A LOWER PRIORITY, WHEN COMPARED WITH OTHER STATEWIDE NEEDS.

THUS, IN ORDER TO IMPROVE THE LEGISLATURE'S ABILITY TO REVIEW AND CONTROL CAPITAL OUTLAY PROGRAMS, I RECOMMEND THAT YOUR FISCAL COMMITTEE ESTABLISH A SUBCOMMITTEE TO CONSIDER ALL CAPITAL OUTLAY PROGRAMS.

7. HOLD THE ADMINISTRATION ACCOUNTABLE FOR MAKING ITS BUDGET "WHOLE"

AS NOTED EARLIER IN THIS STATEMENT, THE GOVERNOR'S BUDGET IS REplete WITH INSTANCES IN WHICH NOT ENOUGH MONEY IS REQUESTED TO ACCOMPLISH WHAT THE ADMINISTRATION ITSELF PROPOSES TO ACCOMPLISH OR WHAT THE STATE CONSTITUTION REQUIRES. IN THE PAST, WHEN CONFRONTED WITH SIMILAR

INSTANCES OF UNDEPFUNDING, YOU HAVE OFTEN LET THE ADMINISTRATION OFF THE HOOK BY ADDING THE NECESSARY FUNDS TO THE BUDGET,

WE SUGGEST THAT WHENEVER THE DEPARTMENT OF FINANCE ACKNOWLEDGES THE NEED FOR ADDITIONAL FUNDS BEYOND THOSE REQUESTED IN THE GOVERNOR'S BUDGET, THE COMMITTEE DEFER ACTION ON THE ITEM UNTIL A BUDGET AMENDMENT ("FINANCE LETTER") HAS BEEN SUBMITTED THAT FORMALLY REQUESTS THE FUNDS. WE BELIEVE THAT THE LEGISLATURE SHOULD HOLD THE ADMINISTRATION RESPONSIBLE FOR MAKING ITS BUDGET "WHOLE," AND SHOULD NOT TAKE ON THIS BURDEN BY "AUGMENTING" THE GOVERNOR'S BUDGET.

8. GIVE THE ADMINISTRATION A DATE CERTAIN FOR PROVIDING THE INFORMATION NEEDED TO PERMIT LEGISLATIVE REVIEW OF THE BUDGET

WE HAVE FOUND IT NECESSARY TO DEFER RECOMMENDATIONS ON OVER \$3.9 BILLION OF THE \$21.7 BILLION IN EXPENDITURES PROPOSED BY THE ADMINISTRATION. IN SOME CASES, WE DID SO IN RECOGNITION OF THE FACT THAT MORE COMPLETE INFORMATION WILL BE AVAILABLE AT A LATER STAGE IN THE PROCESS. IN OTHER CASES, HOWEVER, IT REFLECTS THE FACT THAT THE ADMINISTRATION HAS NOT PROVIDED SUFFICIENT INFORMATION TO PERMIT LEGISLATIVE REVIEW OF ITS PROPOSALS. THIS IS ESPECIALLY TRUE OF THOSE PROPOSALS THAT WOULD:

1. ESTABLISH THREE NEW STATE BLOCK GRANTS.
2. REDUCE THE NUMBER OF ATTORNEYS IN THE LINE DEPARTMENTS.
3. REDUCE FUNDING FOR PROGRAMS IN THE ENVIRONMENTAL AREA.

WE SUGGEST THAT THE COMMITTEE GIVE THE ADMINISTRATION A DATE CERTAIN FOR SUBMITTING ALL OF THE SUPPORTING INFORMATION NEEDED TO PERMIT LEGISLATIVE REVIEW OF THE BUDGET. IT IS PARTICULARLY IMPORTANT THIS YEAR THAT NECESSARY SUPPORTING INFORMATION BE SUBMITTED PROMPTLY BECAUSE MANY OF THE SIGNIFICANT CHANGES PROPOSED IN THE BUDGET WERE DEVELOPED WITHOUT THE PARTICIPATION OF THE LINE AGENCIES.

9. INSIST ON BETTER INFORMATION REGARDING MEMORANDUMS OF UNDERSTANDING NEGOTIATED BY THE ADMINISTRATION WITH REPRESENTATIVES OF STATE EMPLOYEES
(PAGES 185-197 PERSPECTIVES AND ISSUES.)

IN MY OPINION, THE STATE'S INITIAL EXPERIENCE WITH COLLECTIVE BARGAINING WAS COMPLETELY UNSATISFACTORY FROM THE STANDPOINT OF LEGISLATIVE REVIEW AND APPROVAL. THE LEGISLATURE WAS GIVEN ONLY A SHORT TIME IN WHICH TO CONSIDER AND ACT ON THE MEMORANDUMS OF UNDERSTANDING (MOUs) PRESENTED TO IT, AND WAS NOT GIVEN THE INFORMATION IT NEEDED TO MAKE THE REVIEW PROCESS MEANINGFUL.

FOR EXAMPLE, LAST JUNE THE LEGISLATURE WAS ADVISED THAT THE COST OF THE MOUS FOR 1982-83 WAS \$94 MILLION, WHEN IN FACT IT HAS TURNED OUT TO \$146 MILLION. THIS HAS HAD THE EFFECT OF INCREASING THE SIZE OF THE GENERAL FUND DEFICIT IN THE CURRENT YEAR AND PUTTING SOME LEGISLATIVE PRIORITIES IN JEOPARDY.

SO THAT THE LEGISLATURE WILL HAVE A MEANINGFUL OPPORTUNITY TO CARRY OUT ITS RESPONSIBILITIES UNDER THE STATE'S TWO COLLECTIVE BARGAINING LAWS, I RECOMMEND THAT YOUR COMMITTEE:

- A. DIRECT THE DEPARTMENT OF PERSONNEL ADMINISTRATION, THE UNIVERSITY OF CALIFORNIA, AND THE CALIFORNIA STATE UNIVERSITY TO SUBMIT FOR LEGISLATIVE REVIEW MEMORANDUMS OF UNDERSTANDING AND OTHER PROPOSALS FOR COMPENSATION INCREASES NO LATER THAN MAY 15.
- B. REQUIRE THE DEPARTMENT OF FINANCE TO VERIFY THE ESTIMATES OF ALL COSTS (REGARDLESS OF WHETHER THEY ARE CONSIDERED TO BE "ABSORBABLE") PRIOR TO FINAL LEGISLATIVE ACTION ON THE BUDGET.

10. IMPROVE THE FISCAL INFORMATION AVAILABLE TO THE
LEGISLATURE
(PAGES 204-209 OF PERSPECTIVES AND ISSUES.)

FINALLY, I RECOMMEND THAT YOU ACT TO IMPROVE THE QUALITY OF THE FISCAL INFORMATION ON WHICH YOU DEPEND IN ACTING ON, AND MONITORING THE IMPLEMENTATION OF, THE BUDGET FOR THE STATE. SPECIFICALLY, I RECOMMEND THAT:

- A. THE LEGISLATURE ENACT LEGISLATION REQUIRING THE DEPARTMENT OF FINANCE TO INCLUDE SPECIFIC INFORMATION IN ITS FISCAL FORECASTS, AND TO PRESENT THESE FORECASTS ON FOUR SEPARATE OCCASIONS DURING EACH FISCAL YEAR.
- B. LEGISLATION BE ENACTED TO REQUIRE THE DEPARTMENT OF FINANCE TO PRESENT UPDATED ESTIMATES OF MAJOR SPECIAL FUNDS REVENUES CONCURRENT WITH THE PRESENTATION OF UPDATES FOR GENERAL FUND REVENUES DURING THE FISCAL YEAR.
- C. SUPPLEMENTAL REPORT LANGUAGE BE ADOPTED DIRECTING THE DEPARTMENT OF FINANCE TO UPDATE CFIS GENERAL FUND AND SPECIAL FUND BUDGET DATA FOR THE PRIOR YEAR, CURRENT YEAR, AND BUDGET YEAR, IMMEDIATELY FOLLOWING PUBLISHED REVISIONS OF EXPENDITURE DATA BY THE DEPARTMENT OF FINANCE IN MAY AND NOVEMBER; AND

D. A NEW CONTROL SECTION BE ADOPTED IN THE 1983 BUDGET ACT REQUIRING THE DEPARTMENT OF FINANCE TO PUBLISH THE TOTAL NUMBER OF PERSONNEL-YEARS AND ESTIMATED SALARY SAVINGS FOR EACH DEPARTMENT AND AGENCY PERIODICALLY DURING THE YEAR.

* * * * *

AMONG THE 1,100 RECOMMENDATIONS IN THE ANALYSIS ARE OTHER SUGGESTIONS THAT I THINK WILL FACILITATE LEGISLATIVE ACTION ON THE BUDGET BILL. YOUR STAFF IN THE LEGISLATIVE ANALYST'S OFFICE STANDS READY TO ASSIST YOU IN ANY WAY WE CAN AS YOU PROCEED WITH THE DIFFICULT TASK BEFORE YOU.

THANK YOU.

AB 28X SALES TAX TRIGGER MECHANISM

TRIGGER # 1

October 15, 1983
Revenues \$150M Less
Than Projected?

Yes

November 1, 1983
Tax Rate is 5 3/4%

January 15, 1984
Is 1983/84 ending surplus
at least \$100 million?

Yes

5 3/4% Tax Rate continues
until May 1, 1984, and then
returns to 4 3/4%

February 1, 1985
Tax Rate decreases to
3 3/4% or 4 1/4%, depending
on Governors' finding

Tax Rate returns to 4 3/4%
when revenue loss offsets
earlier revenue gain

No

TRIGGER # 2

January 10, 1984
Surplus less than \$100 million
on June 30, 1984?

Yes

February 1, 1984
Tax Rate is 5 3/4%

March 15, 1984 and each
month thereafter:
Has tax raised enough revenue
to yield a \$100 million surplus?

Yes

Tax Rate returns
to 4 3/4%

No

No New Tax

No

Programs that Appear to be Underfunded
in the Governor's Budget

<u>Budget Items</u>	<u>Analysis Page</u>
1. Public Employees Retirement System: Reimbursements for mandated costs imposed on local governments (unknown)	255
2. Department of Conservation: Mammoth Lakes volcanic hazard monitoring (unknown)	532
3. California Coastal Commission: Reimbursements for mandated costs imposed on local government (unknown)	626
4. Department of Parks and Recreation: Workload resulting from (a) transfer of 85,000 acres of property from the Department of General Services to the department, and (b) completion of capital outlay acquisition and development projects for the state parks system (unknown)	634
5. Department of Water Resources: Flood control subventions to reimburse local government costs under the program (\$17,000,000)	692
6. Department of Health Services: Medi-Cal workload and court decisions (\$31,345,000)	861
7. Department of Health Services: Conversion to the new fiscal intermediary contract (unknown)	903
8. Department of Developmental Services: Diversion and special pilot projects (unknown)	932
9. Department of Rehabilitation: Work activity caseload growth (\$6,000,000)	1,046
10. Department of Social Services: Fraud Early Detection and Prevention program (unknown)	1,073
11. Department of the Youth Authority: Projected ward population (unknown)	1,245
12. Department of Education: Reimbursement for mandated costs (rubella immunization) (\$539,000)	1,384
13. Department of Education: California High School Proficiency Examination (\$164,000)	1,445
14. State Teachers Retirement System: Reimbursements for mandated costs imposed on local governments (unknown)	1,463

15. California State University: Enrollment (\$467,166)	1,623
16. Assistance to Counties for the Defense of Indigents (\$2,500,000)	1,783
17. Workers' Compensation Benefits for Subsequent Injuries: Reimbursement for mandated costs (cancer presumption) imposed on local governments (unknown)	1,844
18. Payment of interest on General Fund loans (unknown)	1,958

Other Potential Unfunded Costs

1. Department of Education: Claims submitted by school districts for costs incurred in connection with court ordered desegregation activities (\$82,081,507)	1,386
2. Local Government Claims Bills: Claims approved by Board of Control through December 1982 (\$185,000,000)	--
3. Unidentified Savings:	
a. Private Sector Task Force on Efficiencies and Economies (\$200,000,000)	--
b. Other unidentified savings (\$60,000,000)	--