

Summary

The 1995 Budget Act was signed into law by Governor Wilson on August 3, 1995. The Budget Act and related trailer legislation authorize total state spending of \$58.6 billion in 1995-96, including \$43.3 billion from the General Fund—an increase of 3.9 percent over 1994-95. The budget package is designed to eliminate the \$629 million deficit carried over from 1994-95 and end 1995-96 with the budget in balance.

Improved revenue collections late in 1994-95 and downward adjustments to estimates of caseload and enrollment growths, reduced the budget gap faced by the state from \$2 billion in January to \$1.3 billion in June. The budget package addressed this gap primarily through \$0.9 billion of program reductions and savings (primarily in welfare and health programs) and by shifting \$0.3 billion of costs to the federal government (mostly by assuming additional federal funds for immigrant costs).

Overall, the budget relies on federal actions to achieve almost \$800 million of savings. In, addition to immigrant funding, most of the budgeted savings in welfare and health programs require either federal law changes or administrative waivers. Consequently, the success of the 1995-96 budget plan depends to a large extent on the actions of Congress and the Clinton Administration.

Major features of the budget include the following:

- ❖ **Increased K-12 Education Funding.** Per-pupil spending will increase by more than \$200 from the level

Summary

provided in the 1994 Budget Act. In part, the increased funding reflects the initial implementation of a proposed settlement of the *CTA v. Gould* lawsuit challenging the state's Proposition 98 loan mechanism and repayment requirements.

- ❖ ***Welfare Grant Reductions.*** The budget package reduces statewide grant levels and establishes regional grant levels that will be lower in counties with less-expensive rental housing costs.

Chapter 1

The 1995-96 Budget Package

In this chapter, we discuss the 1995-96 budget problem faced by the Legislature and the Governor and the how the budget package addressed that problem.

THE 1995-96 BUDGET PROBLEM

The 1995-96 budget problem grew out of a continuation of the budget problems that had plagued the state as a result of the recession of the early 1990's.

1994-95 Plan Fell Short

In July 1994, when the 1994-95 budget plan was adopted, there existed an accumulated General Fund budget deficit estimated to be about \$2 billion. The 1994-95 budget plan was intended to eliminate this accumulated deficit over a two-year period (1994-95 and 1995-96). That budget plan called for paying off \$1 billion of the deficit by the end of 1994-95 and eliminating the remaining \$1 billion deficit in 1995-96, when the state would end the year with a balanced budget.

By January 1995, however, it became clear that the 1994-95 budget plan would not achieve its goal of a balanced budget in 1995-96. While the estimated 1994-95 year-end deficit had declined to \$740 million, General Fund spending was projected to exceed revenues by more than \$1.2 billion in 1995-96 absent corrective action. As a result, the state faced a budget deficit that would reach \$2 billion by the end of 1995-96.

Federal Funds Assumptions Proved Too Optimistic. The projected \$2 billion budget gap was not the result of poor economic performance or unanticipated caseload growth. In fact, revenue growth was outpacing estimates, and caseload growth was moderating slightly. However, the 1994-95 budget plan had relied on the assumption that the state would receive a total of \$3.6 billion of new federal funds for immigrant-related costs over the two-year period. By January 1995, federal actions had committed less than \$300 million of that amount, and the prospects for most of the remaining \$3.3 billion appeared poor. This massive shortfall in the realization of assumed federal funding overwhelmed the underlying improvement in budget trends, resulting in the \$2 billion budget gap.

Final Budget Gap Fell to \$1.3 Billion. By May 1995, when the Governor released his May Revision budget updates, the size of the 1995-96 budget gap facing the state had declined to \$1.8 billion, primarily due to slower growth in health and welfare caseloads and prison populations, and to savings from a reestimate of state borrowing expenses. The final budget gap dropped further—to about \$1.3 billion—as a result of improved revenue collections late in 1994-95 and downward revisions to the estimated growth of K-12 school enrollment and welfare caseloads in 1995-96.

THE GOVERNOR'S BUDGET PROPOSALS

Figure 1 outlines the Governor's original January proposal to address the 1995-96 budget gap and his revised budget proposal presented in May. The two proposals were quite similar. Both relied on reductions to welfare and health programs for most of their savings. The bulk of the remaining savings were to come from assumed additional federal funds for immigrant-related costs (although at a more modest level than assumed in the 1994-95 budget package) and from a net state savings resulting from a major realignment of program responsibilities and funding between the state and the counties. Both plans also proposed a major tax reduction, phased in over three years starting with the 1996 tax year. Although both plans resulted in a balanced budget at the end of 1995-96, neither plan provided a significant budget reserve.

Figure 1
**Governor's Proposals to Address
The 1995-96 Spending Gap
January Budget and May Revision**

(In Billions)

	January Budget	May Revision	Change
Program reductions/savings			
SSI/SSP	\$0.5	\$0.6	\$0.2
AFDC	0.4	0.5	0.1
Medi-Cal	0.4	0.3	-0.1
Other savings/ augmentations (net)	0.1	0.2	0.1
Subtotals	\$1.4	\$1.7	\$0.2
Cost shifts			
To federal government	\$0.6	\$0.3	-\$0.3
To counties	0.2	0.1	-0.2
Subtotals	\$0.9	\$0.4	-\$0.5
Tax reductions	-\$0.2	-\$0.2	—
Total budget solutions	\$2.1	\$1.8	-\$0.2
Budget gap	\$2.0	\$1.8	-\$0.2

Detail may not add to totals due to rounding.

The major changes that occurred in the May Revision were a \$500 million reduction in state savings due to a drop in assumed federal funds, and a reduction in program realignment savings. These reduced state savings were offset by the \$200 million decrease in the budget gap and about \$300 million of additional program reductions (primarily deeper welfare cuts), thereby keeping the budget in balance.

Health and Welfare Reductions

Welfare Grant Reductions. The Governor proposed major reductions and limitations to welfare grants. Grants provided under Aid to Families with Dependent Children (AFDC) would be reduced by 7.7 percent, with an additional 15 percent cut after six months on aid.

Grants provided under the SSI/SSP program (which serves low-income elderly, blind, and disabled persons) were proposed to be reduced by 11.5 percent for individuals and 13.5 percent for couples in the May Revision. The Governor also proposed a two-year time limit on AFDC grants and certain eligibility restrictions for AFDC and SSI/SSP grants. These welfare reductions accounted for a total savings of \$1.1 billion in the May Revision. In addition to approval by the Legislature, almost all of these savings required either federal law changes or administrative waivers.

Medi-Cal Reductions. The Governor proposed more than \$300 million of savings in health services provided to low-income persons under the Medi-Cal program. The bulk of the savings were to come from eliminating nine optional (not federally required) services, such as adult dental care, and from eliminating prenatal services for undocumented immigrant women.

Federal Funds

The January Budget assumed that the federal government would provide almost \$600 million of new funding to the state in 1995-96 (beyond the \$245 million already authorized) for costs associated with illegal immigrants and refugees. Most of this funding was to cover the full state cost for Medi-Cal health services to illegal immigrants and for the incarceration of illegal immigrant felons. The May Revision reduced the amount of Medi-Cal funding (based on the President's budget proposal) and eliminated the refugee funding, bringing the amount of new federal immigrant funding assumed in the budget down to \$273 million.

State/County Program Realignment

The January budget proposed to shift to the counties \$1.9 billion of state costs for AFDC grants, foster care and child welfare services. Most of these costs were proposed to be offset by shifting a total of \$1.6 billion in state resources to the counties via increased trial court funding and subventions of sales tax revenue. The proposal resulted in a net state savings (and equivalent net cost to counties) of \$241 million in 1995-96. The May Revision increased funding to the counties and reduced the net state savings to \$75 million.

Tax Reduction Proposal

The January and May budget proposals both included the Governor's tax reduction proposal. That proposal would have continued the existing temporary high-income tax brackets, scheduled to sunset in 1996, but would have phased-in over three years a 15 percent reduction in all individual and business income tax rates. The May Revision estimated the net revenue reduction from the proposal in 1995-96 at \$179 million, with much larger impacts in subsequent years.

The Trigger and Proposition 98 Loan Repayments

Based on the May Revision budget proposal, the Department of Finance estimated that the state would end 1995-96 with a cash "cushion" of about \$1.8 billion of unused borrowable special fund balances. This cushion would avoid the need to make across-the-board spending reductions under last year's "trigger" legislation, which requires action to prevent any projected year-end cash shortfall.

Cash Cushion Included Loan Repayments. Budgeted Proposition 98 loan repayments provided \$706 million of the \$1.8 billion cash cushion. These loans had been provided as off-budget spending to schools and community colleges in 1992-93 and 1993-94 and were to be repaid as cash offsets against their future Proposition 98 entitlements from the state under a statutory formula. Consequently, the proposed loan repayments would result in the state spending \$706 million less on a cash basis than the amount of budgeted Proposition 98 spending. The education community contended that the loans were invalid under Proposition 98 and that there should not be any cash deductions from their state entitlements, and their position had prevailed in a trial court decision in the *CTA v. Gould* lawsuit.

THE ADOPTED BUDGET PACKAGE

In addition to the 1995 Budget Act, the 1995-96 budget package includes several related measures enacted to carry out the budget agreement. Figure 2 lists these budget "trailer bills."

Figure 2	
1995-96 Budget Plan Major Implementing Legislation	
Measure	Description
AB 817 Hoge (Ch 313/95)	<ul style="list-style-type: none"> • Victims of crime program.
AB 825 W. Brown (Ch 308/95)	<ul style="list-style-type: none"> • Education provisions (K-12 and higher education).
AB 904 Bowler (Ch 304/95)	<ul style="list-style-type: none"> • Local juvenile justice facilities.
AB 908 Brulte (Ch 307/95)	<ul style="list-style-type: none"> • Welfare grant reductions. • Social services
AB 910 Speier (Ch 381/95)	<ul style="list-style-type: none"> • Consumer regulatory boards.
AB 911 Vasconcellos (Ch 305/95)	<ul style="list-style-type: none"> • Drug/Medi-Cal. • Health services.
AB 1371 Weggeland (Ch 306/95)	<ul style="list-style-type: none"> • GAIN Program.
SB 146 Maddy (Ch 310/95)	<ul style="list-style-type: none"> • Transportation Seismic Retrofit Bond Act.
SB 493 Maddy (Ch 194/95)	<ul style="list-style-type: none"> • Proposition 99 funds.
SB 1170 Lockyer (Ch 311/95)	<ul style="list-style-type: none"> • Teenage pregnancy prevention.
SB 1344 Solis (Ch 312/95)	<ul style="list-style-type: none"> • County welfare administration match.

Differences from May Revision. The budget package adopted by the Legislature differed from the Governor's May Revision proposal in several major areas, as follows:

- ❖ The adopted reductions in welfare grants and health programs generate roughly half as much savings as the May Revision proposals.
- ❖ The adopted budget did not include the Governor's proposed tax reduction, nor did it extend the temporary high-income brackets.
- ❖ The state/county realignment proposal was not adopted.
- ❖ Proposition 98 loan repayments were reduced to \$150 million, as part of a tentative settlement of the *CTA v. Gould* lawsuit agreed to by the Governor. The reduced repayments resulted in increased assistance to schools and community colleges.

Overall, the program reductions and savings in the adopted budget total about \$600 million less than the total of the reductions proposed in the May Revision. The difference was made up by the \$500 million improvement to the budget gap that was recognized after the May Revision, and by not adopting the tax reduction proposal. The adopted budget ends 1995-96 in balance, but, like the Governor's May Revision proposal, without a meaningful reserve.

Budget Strategy Differs From 1994-95. Figure 3 (next page) identifies the major actions taken to close the final \$1.3 billion budget gap, together with the Administration's estimates of the fiscal effect of each action. As the figure shows, almost three-fourths of the gap was addressed by program reductions or savings. This approach contrasts with the strategy employed in the 1994-95 budget package, which relied primarily on cost shifts to the federal government and counties, and on cost deferrals (including a planned carryover deficit) to resolve a much larger \$4.5 billion budget gap.

Figure 3

**Major Actions Taken
To Close the 1995-96 Budget Gap**

(In Billions)	
Budget Gap (May Revision)	\$1.8
Recognize later improvements	-0.5
Final Gap	\$1.3
Budget Solutions	
Program reductions/savings	
Reduce SSI/SSP and AFDC welfare grants	\$0.4
Medi-Cal rate restrictions/cost controls	0.2
Restrict benefits for legal immigrants and drug/alcohol disability	0.1
Corrections—various reductions and project deferrals	0.1
Shift special fund monies to General Fund programs	0.1
Other savings	0.2
Augment for child health and teen pregnancy programs	-0.1
Subtotal	\$0.9
Shift Costs to Federal Government	
Additional reimbursements for illegal immigrant costs	\$0.3
Revenues	
Expanded tax collection/compliance efforts	\$0.1
Total Solutions	\$1.3

Detail may not add to totals due to rounding.

**Summary of Actions Taken
To Close the Budget Gap**

In brief, the major actions taken to close the 1995-96 budget gap consisted of the following:

- ❖ **Program Reductions/Savings—\$0.9 Billion.** Reductions to welfare grants in the AFDC and the SSI/SSP programs provide the largest amount of savings. The budget package reduces grants by 4.9 percent statewide and by an additional 4.9 percent in low-cost counties (as measured by rental housing costs). A variety of Medi-Cal rate restrictions and cost

controls for dental, long-term care and hospital services provide the second largest amount of savings. The budget also achieves savings by restricting eligibility for health and welfare benefits to legal immigrants who have sponsors and to persons with drug or alcohol dependencies.

❖ **Shift to Federal Government—\$0.3 Billion.** The budget relies on cost shifts to the federal government to address more than \$300 million of the budget gap. The bulk of this savings is from assumed additional funding for the incarceration costs of illegal immigrant felons and for the cost of emergency Medi-Cal services to undocumented persons.

❖ **Revenue Collection and Compliance—\$0.1 Billion.** The budget assumes enactment of federal legislation to collect delinquent state taxes from federal tax refunds and includes additional revenues from enhanced audit and collection activities by the state's tax agencies.

Increased Funding For Education and Corrections

K-12 Education. Per-pupil spending will increase by more than \$200 from the level provided in the 1994-95 budget package. A portion of this funding increase is due to the expenditure of more than \$550 million that had been proposed as loan repayment offsets by the Governor. Instead, schools will receive this money (although \$360 million will not be made available until next summer, pending final settlement of the *CTA v. Gould* lawsuit).

Higher Education. State General Fund support for UC and CSU increases modestly (by 4.9 percent and 1.5 percent, respectively). General Fund support for community colleges increases by almost 10 percent, but overall funding grows by less than 4 percent due to stagnant property tax growth. The budget package does not include any undergraduate student fee increases.

Corrections. Spending for correctional programs grows by 8.6 percent in 1995-96 (including budgeted federal funds for immigrant costs).

No Trigger "Pull" Anticipated by Budget Plan

The administration estimates that the adopted budget package will enable the state to end 1995-96 with about \$1.9 billion of unused borrowable special fund balances. Under last year's trigger legislation, this cash cushion would avoid the need to make across-the-board cuts or to borrow across fiscal years from external sources. The official determination of the state's projected cash position for trigger purposes will be made by the State Controller on October 15.

Chapter 3 of this report more fully discusses the significant elements of the budget package as they relate to major program areas.

Budget Plan's Projected General Fund Condition

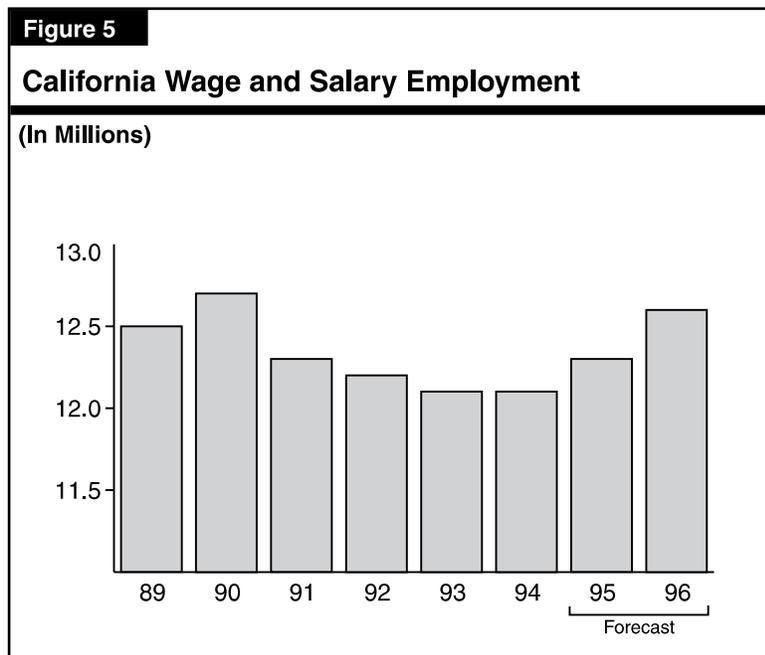
Figure 4 shows the General Fund condition for 1994-95 and 1995-96 as estimated by the Department of Finance, based on the 1995-96 budget package.

Figure 4			
1995-96 Budget Plan			
Estimated General Fund Condition			
((In Millions))			
	1994-95	1995-96	Percent Change
Prior-year balance	-\$1,168	-\$347	
Revenues and transfers	42,553	44,057	3.5%
Total resources available	\$41,385	\$43,710	
Expenditures	\$41,732	\$43,421	4.0%
Ending fund balance	-\$347	\$289	
Reserve	-\$629	\$28	
Other obligations	\$282	\$261	

Detail may not add to totals due to rounding.

The General Fund ended 1994-95 with an estimated deficit of \$629 million. Under the budget package, this deficit will be eliminated in 1995-96. Budgeted spending from the General Fund for 1995-96 is \$43.4 billion—an increase of 4 percent from 1994-95.

Modest Revenue Growth Assumed. General Fund revenues are projected to be \$44.1 billion in 1995-96, an increase of \$1.5 billion, or 3.5 percent, over 1994-95. This includes an increase of \$1.5 billion (8.1 percent) in personal income taxes and \$877 million (6 percent) in sales and use taxes, partially offset by a reduction of \$816 million in bank and corporation taxes. The bank and corporation tax decline is attributable primarily to two factors—a large one-time gain realized in 1994-95 from a court decision involving the state’s taxation of multinational corporations, and the phasing in of investment tax credit legislation enacted in 1994. In the absence of these factors, total 1995-96 revenue growth would be more in the range of 6 percent, reflecting moderate economic expansion. Figure 5 shows, for example, that employment is projected to rise moderately through 1995 and through 1996. It is projected to surpass its pre-recession peak by the end of 1996.



BUDGET RELIES ON FEDERAL ACTIONS

The budget relies on federal actions to achieve almost \$800 million of savings. Figure 6 lists these budget proposals. In addition to increased funding for immigrant costs, almost all of the savings from welfare grant reductions and eligibility restrictions require either federal legislation or a federal administrative waiver. Furthermore, in addition to the \$800 million of budgeted savings from new federal actions, \$245 million currently authorized for the incarceration of illegal immigrant felons remains contingent on final federal budget actions. Consequently, the success of the state's 1995-96 budget plan depends to a large extent on the actions of Congress and the Clinton administration.

Figure 6

1995-96 Budget Plan Solutions Requiring Federal Action

(In Millions)

Costs for Illegal Immigrants

Medi-Cal services	\$105
Incarceration of felons	168 ^a
Subtotal	\$273

Other Proposals

Federal legislation needed

SSI/SSP grant reductions	\$226 ^b
Bar sponsored immigrants from Medi-Cal/AFDC	54
Eliminate state fee for SSI/SSP	48
Eliminate drug/alcohol abuse disability for SSI/SSP	44

Waiver needed

AFDC grant reductions	141
Subtotal	\$513

Total **\$786**

^a Amount budgeted in excess of estimated \$245 million from existing authorizations and appropriations.

^b Excludes currently allowable savings (approximately \$20 million).

ADDITIONAL FACTORS COULD AFFECT THE BUDGET OUTLOOK

In addition to the federal actions discussed above, a number of other potential developments could affect the budget outlook in 1995-96. Revenue collections, as always, are subject to economic developments, and uncertainties in the current economic outlook provide both potential upside and downside risks. In addition, developments that will bear watching include the following:

- ❖ **Welfare Reform.** Congress currently is completing action on a major welfare reform proposal, which would convert AFDC to a block grant. Proposals now under consideration would reduce federal funding and allow states more program flexibility. The initial reduction of federal funds would be relatively small in 1995-96 but could be several hundred million dollars annually starting in 1996-97.
- ❖ **PERS v. Wilson.** A trial court has found in favor of PERS' contention that the state illegally deferred its retirement contributions for employees for several years. If the decision is affirmed on appeal, the potential cost to the state could be more than \$1 billion.
- ❖ **Federal Audit Exception.** The state is pursuing an administrative appeal of a federal audit exception which would require the state to share with the federal government some of its past savings from the use of excess employee retirement funds. The amount at stake is more than \$100 million.
- ❖ **Property Tax Revenues to Schools.** Any shortfall in property tax revenues to schools and community colleges would require an offsetting increase in state aid under Proposition 98. Preliminary information indicates that there may have been a shortfall in final 1994-95 property tax receipts by

schools and community colleges. A property tax shortfall of one percent would be equivalent to about one hundred million dollars.

❖ ***Use of Proposition 99 Funds.*** The budget's use of about \$61 million of Proposition 99 tobacco tax funds to help finance certain health programs has been enjoined as the result of a lawsuit. This action could result in budget pressure to replace at least a portion of the affected funding.

❖ ***Social Services Savings.*** On the positive side, the Department of Social Services reports that its final spending for local assistance in 1994-95 was about \$46 million less than estimated in the budget package, in part due to somewhat slower caseload growth.

Chapter 2

State Expenditures

In this chapter, we discuss total state spending from all funds under the 1995-96 budget plan and year-to-year changes in these spending amounts. We show how spending is divided among the major program areas in 1995-96 and discuss 1995-96 spending in the context of spending trends during the previous decade.

TOTAL STATE SPENDING

Figure 1 shows the total amount of state expenditures under the budget plan adopted for 1995-96 and compares it to total state spending in 1994-95. The figure includes spending from the General Fund, special funds and selected bond funds. Our figures include adjustments (as noted in Figure 1, next page) to the Administration's spending amounts in order to make the figures more comparable from year-to-year and to better reflect actual state spending levels.

Growth of Special Fund Spending Outpaces Overall Spending Growth. Budgeted state spending will total \$58.6 billion in 1995-96, an increase of \$2.1 billion (3.7 percent) over total spending in 1994-95. General Fund spending increases by \$1.6 billion (3.9 percent) compared with 1994-95. The rate of growth of spending from special funds (6.1 percent) is considerably higher than the growth rate of overall spending, primarily due to a large increase in budgeted transportation spending for seismic safety improvements and highway construction in 1995-96. Spending from selected bond funds

Figure 1

**The 1995-96 Budget Plan
Total State Expenditures**

(In Millions)

	Estimated	Enacted	Change from 1994-95	
	1994-95	1995-96	Amount	Percent
General Fund (adjusted) ^a	\$41,682	\$43,321	\$1,639	3.9%
Special Funds ^b	13,773	14,615	842	6.1%
Budget Totals	\$55,455	\$57,936	\$2,481	4.5%
Selected Bond Funds	1,091	706	-385	-35.3%
Total state spending	\$56,546	\$58,642	\$2,096	3.7%

^a Excludes Proposition 98 loan repayments (\$50 million in 1994-95 and \$100 million in 1995-96).
^b Includes Local Public Safety Fund expenditures.

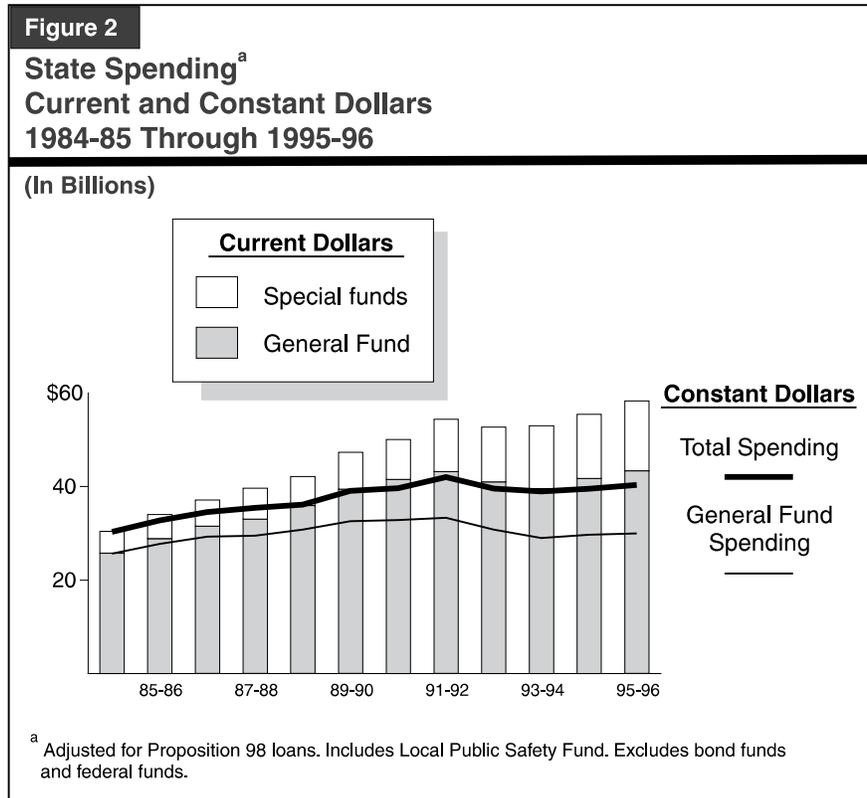
declines sharply, by \$385 million (35 percent), reflecting the shrinking amount of uncommitted funds remaining from prior voter-approved general obligation bond acts. Spending amounts shown in Figure 1 for selected bond funds do not include approximately \$500 million of planned capital outlay spending in 1995-96 from the proceeds of lease-payment bonds.

Most of the state's expenditures are from the General Fund. In 1995-96, General Fund expenditures will amount to \$43.3 billion, or 74 percent of total state spending reflected in Figure 1.

STATE SPENDING TRENDS SINCE 1984-85

To put this year's budget into perspective, Figure 2 shows state spending trends since 1984-85. Total state spending grew rapidly from 1984-85 to 1991-92, but spending growth stopped between 1991-92 and 1994-95, in large part due to revenue constraints associated with the recession. Spending growth resumes in 1995-96 under the budget package, but at a more modest pace than occurred throughout the latter half of the 1980s. Total spending in 1995-96 will

exceed total spending in 1991-92 by a projected \$3.2 billion. However, after adjusting for inflation, total spending in 1995-96 will be 4.5 percent less than its 1991-92 peak.



In percentage terms, spending from special funds has grown more than twice as fast as General Fund spending since 1984-85. The relatively rapid growth of spending from special funds reflects two major trends. First, legislation and voter initiatives have established new programs financed by fees or dedicated tax revenues (such as Proposition 99 tobacco taxes) and also have increased gasoline taxes and other special fund revenues. Second, since 1991-92, the Legislature has acted to shift some traditional General Fund costs and revenues to special funds. For example, in 1991-92 a half-cent increase in the state sales tax was enacted, and the revenues were placed in a special fund to defray certain health and welfare costs that the state shifted to the counties.

Spending by Major Program Area

Budgeted state spending from the General Fund and special funds totals \$58 billion in 1995-96. Figure 3 shows how this total spending is divided among the major program areas and compares this allocation of spending with the programmatic allocation of state spending in 1984-85.

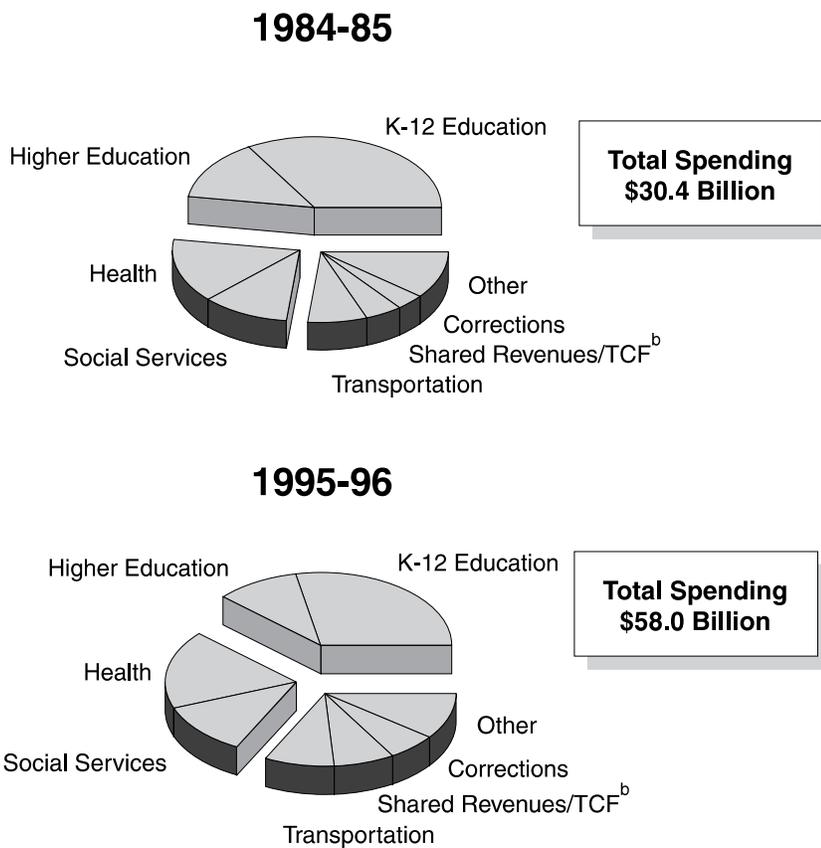
Education's Share of Spending Is Largest, but Shrinking. Education continues to receive the largest share of state spending (38 percent), but its slice of the state spending "pie" has shrunk considerably since 1984-85, when almost half of total state spending was for education programs. In part, education's smaller share of state spending reflects the replacement of some state support for K-14 education with property tax revenues shifted from local governments to schools and community colleges. In contrast with education, the share of state spending devoted to health and social services programs has grown slightly since 1984-85—from 26 percent to 29 percent. Most of this growth has been for health programs.

Prison Costs Grow Rapidly. Corrections' share of total spending, while still relatively small, has grown rapidly—from 3.6 percent in 1984-85 to 6.2 percent in 1995-96. This growth reflects the rise in the inmate population and the increased costs of financing and operating prisons.

Local Aid Increase Mitigates Property Tax Shift. The percentage of state spending provided as shared revenues and other general aid to local governments has increased from 4.7 percent in 1984-85 to 7.4 percent in 1995-96. This increased share of state spending devoted to local aid reflects allocations to local governments from state sales tax revenues in the Local Public Safety Fund, which began in 1993-94. However, these allocations primarily were intended to mitigate the shift of property taxes from local governments to K-14 education, so that the decline in education's slice of the spending pie and the increase in the slice devoted to spending on local aid are related.

Figure 3

**Total State Spending by Major Program^a
1995-96 versus 1984-85**



^a Excludes bond funds and federal funds.

^b Includes local Subventions of vehicle license fees. Local Public Safety Fund and Trial Court Funding (TCF) grants.

Chapter 3

Major Features Of the 1995 Budget Plan

This chapter provides a description of the major features of the 1995-96 budget plan. It includes individual discussions of the budget actions within each of the major program areas, as well as discussions of the budget actions that affect revenues.

K-12 EDUCATION

In this section, we describe the major features of the budget package as they relate to the Proposition 98 minimum funding guarantee and K-12 schools. Most of the package's education provisions are contained in the education trailer bill—Ch 308 95 (AB 825, W. Brown).

Proposition 98 Provisions

Proposition 98 provides K-12 schools and community colleges a guaranteed minimum level of funding. The Proposition 98 portion of the budget package:

- ❖ Provides overall K-12 funding of \$4,309 per pupil in 1994-95 and \$4,435 per pupil in 1995-96, an increase of \$126 per pupil. The 1994-95 funding level provides schools with an additional \$92 per pupil above the level provided in the 1994 Budget Act.

- ❖ Fully funds K-12 growth and provides a 2.7 percent cost-of-living adjustment (COLA) for general purpose and categorical programs.
- ❖ Increases total funding for community colleges by \$103 million.

Proposition 98 Funding. The budget provides \$26.2 billion (\$16.1 billion General Fund) in Proposition 98 funding for K-14 programs in 1995-96. This exceeds the amount provided in 1994-95 by \$1.1 billion (\$925 million General Fund, \$125 million local property taxes). This amount is the minimum needed to fully fund the Proposition 98 funding guarantee in 1995-96.

Figure 1 summarizes for 1994-95 and 1995-96 the effect of the budget package on the three major recipients of Proposition 98—schools, community colleges, and other agencies. As the figure shows, the funding level for K-12 schools is \$4,309 per pupil for 1994-95, which is \$92 per pupil more than was provided in the 1994 Budget Act. These additional funds resulted from an increase in the Proposition 98 funding guarantee due to higher-than-projected General Fund revenues during 1994-95.

The 1995 Budget sets average per-pupil funding for 1995-96 at \$4,435, or \$126 above the adjusted per-pupil funding level provided in 1994-95.

As Figure 1 also displays, community college funding in 1995-96 increases by \$103 million from the adjusted level provided in 1994-95. We discuss the community college's budget in the higher education section of this report.

CTA v. Gould. The amounts contained in Figure 1 for 1995-96 include \$360 million that will not be immediately available to school districts. This is because these funds are appropriated contingent upon settlement of the *CTA v. Gould* lawsuit, which contests the legality of \$1.8 billion in Proposition 98 loans made in the 1992 and 1993 Budget Acts. A tentative settlement of the lawsuit was devel-

Figure 1

**Proposition 98 Programs
1995 Budget Act and Education Trailer Bill^a**

(Funding In Millions)

	Revised 1994-95	Budgeted 1995-96
K-12 programs		
State appropriations	\$13,807	\$14,682
Local taxes	8,543	8,671
Subtotals	\$22,350	\$23,353
<i>Average daily attendance</i>	<i>5,187,120</i>	<i>5,265,068</i>
<i>Amount per pupil</i>	<i>\$4,309</i>	<i>\$4,435</i>
Community colleges		
State appropriations	\$1,177	\$1,293
Local taxes	1,369	1,364
Fees	178	170
Subtotals	\$2,725	\$2,827
Other agencies	\$89	\$92
Loan repayments	\$50	\$100
Totals		
State appropriations	\$15,123	\$16,167
Local taxes	9,912	10,035
Fees	178	170
Adjusted totals	\$25,213	\$26,372

^a Assumes proposed settlement of CTA vs Gould.

oped during budget discussions. If the lawsuit is settled, the \$360 million will be distributed to schools in August 1996.

Under the proposed settlement:

- ❖ **Paying Off the Loans.** The \$1.8 billion in loans would be paid off over eight years. About half—\$825 million—would be repaid by K-14 programs through offsets against state Proposition 98 funding. The education trailer bill includes repayments from K-14 programs totaling \$150 million (\$50 million in 1994-95 and \$100 million in 1995-96). Proposed future annual repayments from K-14 pro-

grams would range from \$100 million to \$125 million over the period 1996-97 through 2001-02. The remaining \$935 million of the loans would be repaid by counting them as non-Proposition 98 General Fund spending amounts. The non-Proposition 98 repayments would increase from \$50 million in 1996-97 to \$225 million in 2001-02.

- ❖ **Increasing the Base.** The Proposition 98 minimum funding level would be increased by \$500 million. First, \$275 million would be added to the long-term Proposition 98 funding minimum. The year in which schools would actually achieve this increase would depend on the growth of the state's economy and General Fund tax revenues. Second, the \$225 million in non-Proposition 98 loan repayments made in 2001-02 (discussed above) would be used in 2002-03 to provide a permanent increase in Proposition 98 spending for schools.

K-12 Program Impacts

General Purpose Funding. The budget provides a total of \$17.7 billion (\$9.2 billion General Fund) for general purpose funding to school districts and county offices of education in 1995-96. This represents an increase of \$157 per pupil from the amount provided in 1994-95. Figure 2 displays the major actions that result in the 1995-96 increase. As the figure illustrates, in addition to providing a 2.7 percent COLA, general purpose funding is increased for all districts by an average of \$33 per pupil (0.9 percent). The budget also includes an equalization payment for "low wealth" districts which will narrow the differences in per-pupil funding among school districts.

Categorical Programs. The 1995 Budget Act also increases funding for K-12 categorical programs by more than \$360 million (see Figure 3.) The largest amount (\$160 million) was provided for growth and COLA funding for certain categorical programs that are not part of the categorical mega-item (such as child development and adult educa-

Figure 2
General Purpose Funding Increases
1995 Budget Act and Education Trailer Bill

(Dollars in Millions)

Action	Amount
Provides a 2.7 percent cost-of-living adjustment	\$ 457
Includes an additional 0.9 percent across-the board increase (revenue limit deficit reduction)	175 ^a
Provides an equalization appropriation for districts with lower-than-average funding levels	155 ^a

^aFunding contingent upon settlement of the *CTA v. Gould* lawsuit.

tion). An additional \$136 million was provided in the form of a categorical block grant, \$26 million set aside for a new state assessment program, \$20 million for expansion of the state preschool program, and \$20 million for expansion of the Healthy Start Program.

The categorical block grant generally provides growth and COLA funding to programs that are supported through the categorical mega-item. The growth and COLA funds, however, are not appro-

Figure 3
Major K-12 Categorical Program Increases
1995 Budget Act and Education Trailer Bill

(Dollars in Millions)

Program	Amount
Growth and COLA for selected categorical programs	\$160
Categorical program block grant	136
New state assessment program	26 ^a
State preschool augmentation	20
Healthy Start augmentation	20 ^b

^a\$15 million contingent upon settlement of the *CTA v. Gould* lawsuit.

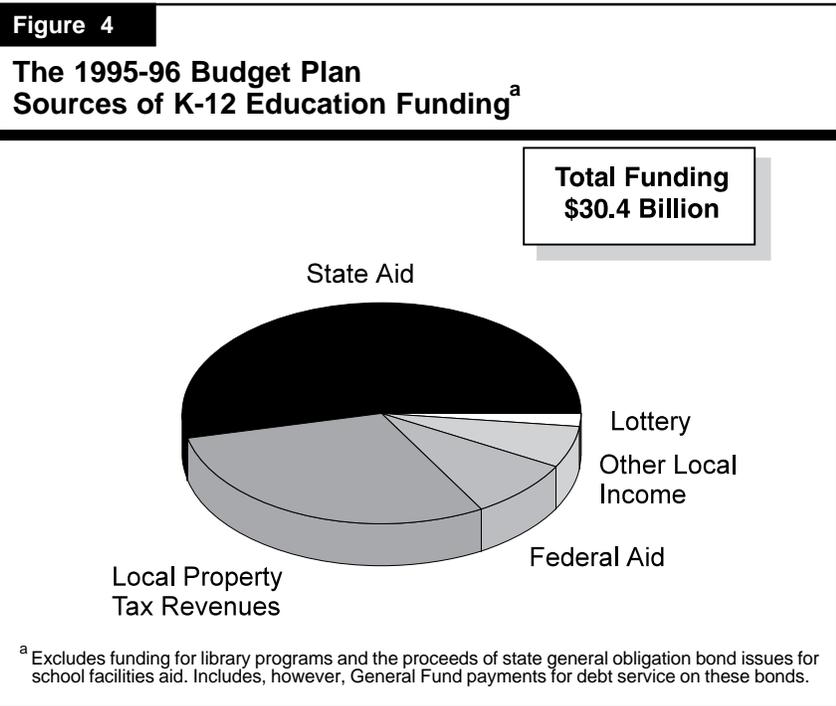
^b\$10 million contingent upon settlement of the *CTA v. Gould* lawsuit.

priated to specific programs. Instead, the funds are provided as a block grant that will permit school districts flexibility to allocate the additional funds to programs funded through the mega-item. The funds are distributed in an equal amount per ADA, rather than in proportion to the amount of categorical funds each district receives.

1994-95 Funding Increases. As discussed above, funding for schools in 1994-95 increased by \$92 per pupil due to increased General Fund revenues as part of the education trailer legislation. The most important of these actions was the creation of a \$280 million block grant that provides K-12 districts \$50 per pupil for any one-time purpose. An additional \$60 million was appropriated for deferred maintenance, instructional materials, and education technology.

K-12 Funding From All Sources

In 1995-96, funding available for expenditure on K-12 education from all sources—including both Proposition 98 and non-Proposition 98 funding—will total \$30.4 billion (see Figure 4). This amount represents an increase of \$1.1 billion, or 3.8 percent, over what was

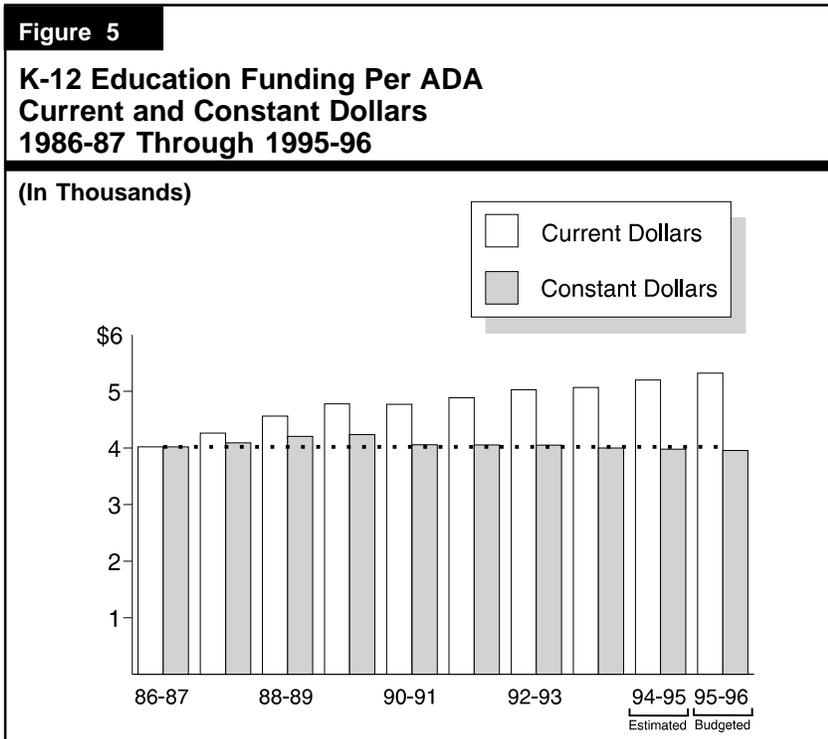


available in 1994-95. Of the \$30.4 billion in total funding, 90 percent is from state and local sources—77 percent provided under Proposition 98 and 13 percent from non-Proposition 98 sources. Non-Proposition 98 funding from state and local sources includes primarily (1) state General Fund payments to the State Teachers' Retirement System and for debt service on school construction bonds and (2) local revenues from such sources as developer fees, sales of equipment and supplies, cafeteria revenues, and interest income.

Other major sources of funding are:

- ❖ Federal aid—\$2.5 billion (8.4 percent of total funding).
- ❖ Lottery revenues—\$568 million (1.9 percent of total funding).

Figures 5 (below) and 6 (next page) show total K-12 funding per unit of average daily attendance (ADA)—in both current and “constant”



(inflation-adjusted) dollars—for the years 1986-87 through 1995-96. They show that per-ADA funding in inflation-adjusted dollars has basically held steady, decreasing 1.6 percent during the ten-year period. While the budget significantly increases funding per student, Figure 6 shows that, after adjusting for inflation, per-ADA funding from all sources has continued to decline.

Figure 6

**K-12 Education Funding
By Funding Source and Per ADA
Current and Constant Dollars
1986-87 Through 1995-96**

	Funding (Millions)					Total Funding	ADA (000s)	Current Dollars Per ADA	Constant Dollars Per ADA
	State Aid	Local Property Tax Levies	Federal Aid	Other Local Income	Lottery				
1986-87	\$12,174	\$3,804	\$1,167	\$979	\$411	\$18,535	4,612	\$4,019	\$4,019
1987-88	12,486	4,108	1,345	1,592	590	20,121	4,723	4,260	4,089
1988-89	13,568	4,466	1,517	1,767	911	22,229	4,872	4,563	4,203
1989-90	15,013	4,797	1,634	1,943	781	24,168	5,060	4,777	4,233
1990-91	15,770	5,252	1,770	1,770	602	25,164	5,273	4,772	4,056
1991-92	16,510	5,642	2,041	1,845	432	26,470	5,416	4,887	4,053
1992-93	16,255	6,841	2,257	1,786	479	27,618	5,495	5,026	4,051
1993-94	14,881	8,605	2,332	1,830	556	28,205	5,562	5,071	3,999
1994-95 (Estimated)	15,390	8,992	2,464	1,875	568	29,288	5,632	5,200	3,979
1995-96 (Budgeted)	16,276	9,107	2,541	1,921	568	30,413	5,715	5,322	3,955
Cumulative Change									
Amount	\$4,102	\$5,303	\$1,374	\$942	\$157	\$11,879	1,103	\$1,303	-\$64
Percent	33.7%	139.4%	117.8%	96.2%	38.2%	64.1%	23.9%	32.4%	-1.6%

HIGHER EDUCATION

Figure 7 shows funding for each major segment of higher education for 1994-95 and 1995-96 from selected fund sources. After adjusting for one-time funding, ongoing support for higher education increases moderately. Of the three major higher education segments, the University of California experienced the largest increase (5.3 percent). Funding support for the CSU (adjusted for one-time funding in 1994-95) increased by 4.4 percent, while community college support increased by 3.6 percent.

Figure 7

Higher Education Budget Summary Selected Funding Sources^a 1994-95 and 1995-96

(Dollars in Millions)	Estimated 1994-95	Budget 1995-96	Change From 1994-95	
			Amount	Percent
University of California				
General Fund	\$1,825.4	\$1,915.5	\$90.1	4.9%
Professional fee increases (net)	—	5.8	5.8	—
Totals	\$1,825.4	\$1,921.3	\$95.9	5.3%
California State University				
General Fund	\$1,599.2	\$1,623.5	\$24.3	1.5%
Additional fee revenues (net)	—	2.1	2.1	—
Totals	\$1,599.2	\$1,625.6	\$26.4	1.7%
California Community Colleges^b				
General Fund (Proposition 98)	\$1,177.3	\$1,293.2	\$115.9	9.8%
General Fund (Non-Proposition 98)	3.5	—	-3.5	-100.0
Property taxes	1,368.8	1,363.8	-5.0	-0.4
Total fee revenues (net)	178.4	170.2	-8.2	-4.6
Totals	\$2,728.0	\$2,827.2	\$99.2	3.6%
Student Aid Commission^b (Cal Grants)				
General Fund	\$226.2	\$230.6	\$4.4	1.9%

^a General Fund figures exclude General Obligation bond debt service and community college retirement costs.

^b Local assistance only.

The budget package assumes there will be no undergraduate student fee increases. (See Figure 8.)

Figure 8

**Higher Education Student Fees
1993-94 Through 1995-96**

	Annual Fee Per Full-Time Student			Change From 1994-95	
	1993-94	1994-95	1995-96	Amount	Percent
University of California					
Undergraduate/graduate	\$3,454	\$3,799	\$3,799	—	—
Law ^a	3,830	6,175	8,175	\$2,000	32.4%
Business ^a	3,454	5,799	7,799	2,000	34.5
Medicine ^a	3,830	6,175	7,175	1,000	16.2
Dentistry/Veterinary Medicine ^a	3,454	5,799	6,799	1,000	17.2
California State University	1,440	1,584	1,584	—	—
California Community Colleges^b	390	390	390	—	—

^a Fees charged to new students.
^b Excludes BA degree holders, who are charged \$50 per credit unit until January 1, 1996.

The University of California (UC)

The 1995 Budget Act provides \$90.1 million (4.9 percent) more in General Fund support for the UC in 1995-96 compared to 1994-95. The Legislature rejected the administration's proposed \$380 (10 percent) general fee increase and instead provided \$28.5 million from the General Fund to backfill 75 percent of the net amount that would have been collected through the higher fees (\$38 million). The Legislature approved fee increases of up to \$2,000 for new students enrolled in professional programs (law, business, medicine, dentistry, and veterinary medicine), as proposed by the UC. Including funds available as a result of the professional student fee increases, the UC will experience an increase of \$95.9 million, or 5.3 percent, above 1994-95. In addition, the 1995-96 budget plan for the UC:

- ❖ Provides a 3 percent faculty salary increase and a 1.5 percent staff salary increase on October 1, 1995 and merit salary increases for faculty and staff.
- ❖ Authorizes a \$25 million loan for certain priority-one deferred maintenance projects.
- ❖ Redirects \$5.5 million from teaching hospitals for deferred maintenance.
- ❖ Provides for the full phase-in of an increase in the budgeted student-faculty ratio from 17.6 to 18.7.

The Legislature's plan also includes an unspecified reduction of \$9.5 million related to the partial backfill of the fee revenues.

We anticipate UC student enrollment to increase slightly—to approximately 151,000—in the budget year to reflect slight increases in the Master Plan eligible student population. The Legislature expressed its intent in the *Supplemental Report of the 1995 Budget Act* for the UC to continue to accept all applicants who are fully eligible under the Master Plan in 1995-96 and 1996-97.

The California State University (CSU)

The 1995 Budget Act provides \$24.3 million (1.5 percent) more in General Fund support for the CSU in 1995-96 compared to 1994-95. The increase understates actual budget-year growth, as 1994-95 expenditures included \$41 million in one-time spending.

The Legislature rejected the administration's proposed \$156 (10 percent) general fee increase and instead provided \$22.5 million from the General Fund to backfill 75 percent of the net amount that the higher fees would have generated (\$30 million). The Legislature also rejected an additional \$90 fee increase proposed by the CSU for graduate and post-baccalaureate students. However, the Legislature provided no backfill for the estimated \$2.1 million in foregone fee revenues. Excluding the one-time funding in 1994-95, the CSU budget-year increase is \$67.8 million or 4.4 percent.

The 1995-96 budget plan for the CSU also:

- ❖ Provides for an enrollment increase of 2,000 full-time-equivalent (FTE) students, for a total budgeted enrollment level of 252,000 FTE students (plus roughly 350 students at the California Maritime Academy).
- ❖ Provides \$37.5 million for faculty and staff salary increases (to be determined through collective bargaining).
- ❖ Provides \$6.6 million for “quality enhancements”.
- ❖ Authorizes a \$24 million loan for certain priority-one deferred maintenance projects.

The Legislature’s plan also includes an unspecified reduction of \$7.5 million related to the partial backfill of the fee revenues.

California Community Colleges (CCC)

The 1995 budget package increases funding for community colleges local assistance by \$99.2 million (3.6 percent) compared to the revised 1994-95 appropriation. The Legislature’s budget actions also increase the community colleges’ 1994-95 General Fund appropriation by \$73 million—\$47 million to backfill a local property tax shortfall and \$26 million for deferred maintenance and instructional equipment.

As Figure 8 shows, the Legislature rejected the administration’s proposed \$2 per credit unit fee increase. This leaves community college fees at \$13 per credit unit, or \$390 per full-time student. The Legislature provided almost \$20 million to backfill the net amount that would have been collected through the higher fees. The Legislature also rejected the administration’s proposal to extend the differential fee for BA degree holders—\$50 per credit unit—which will expire on January 1, 1996. However, the Legislature provided no backfill for the estimated \$5 million loss in differential fee

revenues. The Legislature approved the administration's proposed reduction of \$15.2 million related to past-year declines in the enrollment of BA degree holders.

Based on current estimates of local property tax revenues by the Department of Finance (DOF), the funding provided to community colleges for 1995-96 is sufficient to fund a 3.07 percent COLA and 1995-96 enrollment growth of 1.17 percent. This would translate into a total FTE of about 880,000. The Community Colleges Chancellor's Office, however, has expressed concern that property tax revenues may not reach the level projected by the DOF. To the extent that property tax revenues are less than the amount estimated, the Chancellor's Office indicates that funding for enrollment growth in 1995-96 will be reduced accordingly.

The Legislature adopted supplemental report language directing the CCC Chancellor's Office to identify outcome measures and performance standards which can be used to assess the performance of individual colleges and the community college system as a whole. The Chancellor's Office must report these measures and standards to the Legislature by November 30, 1996.

Student Aid Commission (SAC)

Figure 7 shows an increase of \$4.4 million (1.9 percent) in Cal Grant funding. Of this amount, \$3 million is to fund changes in the college attendance patterns of Cal Grant students and \$1.4 million is to backfill a loss of federal funds.

The Legislature adopted Budget Act language requiring the commission to contract with the Bureau of State Audits for reviews of the extent to which the SAC has (1) addressed concerns raised in an independent review of the automated Financial Aid Processing System (FAPS) and (2) ensured competition in a request for proposal the commission intends to release to procure a maintenance contractor for FAPS. The Legislature also expressed its intent in supplemental report language that the SAC develop a strategic plan for addressing the impact that various changes (including the phase-in of direct lending, the implementation of federal law changes,

and improvements in information technology) are having on the ability of the SAC to function in a competitive loan guarantee environment.

HEALTH & SOCIAL SERVICES

In this section, we describe the major features of the health and welfare funding in the budget package. The 1995-96 budget for health and welfare programs includes \$13.9 billion from the General Fund. This represents a slight decrease (less than 1 percent) from the prior year.

Anticipated health and welfare caseloads will increase at rates ranging from 2 percent to 5 percent. However, the *cost* of caseload increases is partially offset by anticipated receipt of additional federal funds and a variety of savings actions adopted as part of the 1995-96 budget plan.

Figure 9 shows the major General Fund changes in these programs that were adopted in the 1995-96 budget. As the figure shows, the largest savings result from grant reductions in the Supplemental Security Income/State Supplementary Program (SSI/SSP) (\$246 million) and the Aid to Families with Dependent Children (AFDC) Program (\$141 million)

AFDC Program

The AFDC Family Group (FG) and Unemployed Parent (U) Programs provide cash grants to low-income families with children. The AFDC Foster Care Program provides grants to pay for the care of children placed in foster family homes or group homes. The budget plan provides \$3.1 billion from the General Fund for the AFDC Program in 1995-96. This represents a decrease of 4.8 percent from estimated 1994-95 expenditures.

Regional Grant Reductions. The budget reduces AFDC grants by 4.9 percent, with an additional 4.9 percent reduction for recipients residing in low-cost counties (as measured by rental housing costs), effective October 1995, for a General Fund savings of \$141 million

Major Features
of the 1995
Budget Plan

Figure 9

**Health and Welfare Programs
Major 1995-96 Policy Changes
General Fund**

(Dollars in Millions)

Program/Issue	Change from Prior Law
AFDC	
Reduce grants based on two regions	-\$140.5
Bar sponsored aliens from eligibility	-23.7
Use Employment Training Fund for GAIN Program	-20.0
Eliminate grant differential for <i>Edwards v. Carlson</i> cases	-11.5
Make GAIN Program more employment-oriented	-8.0
SSI/SSP	
Reduce grants based on two regions	-246.4
Assume elimination of federal administration fee	-48.1
Eliminate substance abuse as qualifying disability	-21.8
Medi-Cal	
Assume federal funds for undocumented persons	-105.0
Reduce costs of dental benefits	-90.6
Eliminate prenatal benefits for undocumented persons	(-57.7) ^a
Bar sponsored aliens from eligibility	-30.1
Establish transitional care rate for nursing homes	-30.0
Eliminate substance abuse as disability for SSI/SSP	-22.1
Assume no net increase in negotiated hospital rates	-22.0
Medicare/Medi-Cal cost separation in nursing facilities	-11.6
Public Health	
Establish Cal REACH program	20.0 ^b
Establish teen pregnancy prevention program	12.0
Expand childhood immunization	20.0

^a Implementing legislation was not enacted to achieve these savings.

^b Funding included in budget but implementation legislation was not enacted.

in 1995-96. This will reduce the monthly grant for a three-person family from \$594 to \$565 in high-cost counties and to \$538 in low-cost counties. The high-cost counties are Alameda, Contra Costa, Los Angeles, Marin, Monterey, Napa, Orange, San Diego, San Francisco, San Luis Obispo, San Mateo, Santa Barbara, Santa Clara, Santa Cruz, Solano, Sonoma, and Ventura. The reduction applied to all recipients will terminate June 30, 1996, and the additional reduction to recipients living in low-cost counties will be ongoing. (See Figure 10.)

Figure 10

**AFDC and SSI/SSP Monthly Grants
1994-95 and 1995-96**

	1994-95	1995-96	Change	
			Amount	Percent
AFDC^a				
Low-cost counties	\$594 ^b	\$538	-\$56	-9.4%
High-cost counties	594 ^b	565	-29	-4.9
SSI/SSP—Individual^c				
Low-cost counties	\$614	\$556	-\$58	-9.5
High-cost counties	614	584	-30	-4.9
SSI/SSP—Couples^c				
Low-cost counties	\$1,102	\$996	-\$106	-9.6
High-cost counties	1,102	1,048	-54	-4.9

^a Family of three.

^b Reflects 2.3 percent (\$13) reduction authorized in the 1994 Budget Act, but not implemented because federal waiver still pending.

^c Aged or disabled persons. Excludes federal cost-of-living adjustment, effective January 1996.

Greater Avenues for Independence (GAIN) Program. The budget includes a transfer of \$20 million from the Employment Training Fund to support the GAIN Program, for a corresponding General Fund savings in 1995-96. The budget also assumes AFDC grant savings of \$8 million (General Fund) from enactment of GAIN Program changes designed to make the program more employment-oriented (AB 1371, Weggeland).

Edwards v. Carlson. Beginning in 1992-93, the *Edwards v. Carlson* decision required the state to provide higher AFDC grants in certain cases (a caretaker relative and nonsibling children). In 1995, the U.S. Supreme Court reversed this lower court decision. The budget reflects the Governor's proposal to eliminate the grant differential, for a General Fund savings of \$11.5 million in 1995-96.

Teen Pregnancy Disincentive Program. The Legislature adopted the Governor's proposal to require AFDC parents under age 18 to live in the home of their parent or guardian except under certain circumstances, such as when the health or safety of the teen or her child would be jeopardized. The budget assumes that grant savings would be offset by child welfare services costs, for no net fiscal effect in 1995-96.

SSI/SSP

The SSI/SSP is a state- and federally-funded program that provides grants to low-income aged, blind, and disabled persons. The Budget Act appropriates \$2.1 billion from the General Fund for the program in 1995-96, which is a decrease of less than 1 percent from estimated 1994-95 expenditures.

Regional Grant Reductions. The budget reduces SSI/SSP grants by 4.9 percent, with an additional 4.9 percent reduction for recipients residing in low-cost counties, effective December 1995, for a net General Fund savings of \$246 million in 1995-96. This will reduce the monthly grants for aged and disabled individuals (the largest category of recipients) from \$614 to \$584 in high-cost counties and to \$556 in low-cost counties. The reduction applied to all recipients will terminate June 30, 1996, and the additional reduction to recipients living in low-cost counties will be ongoing. (See Figure 10.)

Elimination of Federal Administrative Fee. The budget assumes enactment of federal legislation, effective October 1995, to eliminate the federal fee for administering state-funded supplemental benefits, for a General Fund savings of \$48 million in 1995-96.

Medi-Cal Program

The California Medical Assistance (Medi-Cal) Program provides health care services to public assistance recipients and other qualified persons who cannot afford to pay for these services. The federal government provides \$8.5 billion for the program, and the budget appropriates \$6.1 billion in matching funds from the state General Fund in 1995-96. This represents an increase of 1 percent over estimated General Fund expenditures in 1994-95.

Services to Undocumented Persons. The budget assumes receipt of \$105 million in federal funds to partially offset state costs for emergency health services provided to undocumented immigrants. The budget also assumes elimination of the state-only program providing prenatal benefits to undocumented women, for a General Fund savings of \$58 million in the budget year. However, implementing legislation was not enacted to achieve the savings in prenatal benefits to undocumented women.

Optional Benefits. While the Legislature rejected the Governor's proposal to eliminate optional benefits, it did reduce the costs of the dental program. Specifically, the budget (1) defers cost-of-living adjustments for dental rates in 1995-96, for a General Fund savings of \$39.8 million, and (2) reduces rates an average of 14 percent and eliminates two procedures for an additional savings of \$50.8 million.

Sponsored Aliens. The budget assumes enactment of federal legislation to prohibit immigrants who are sponsored by a U.S. citizen from receiving Medi-Cal or Aid to Families with Dependent Children (AFDC) benefits for five years. This would result in General Fund savings of \$30 million in the Medi-Cal Program and \$24 million in the AFDC Program in 1995-96.

Transitional Care Rate. The budget establishes a higher reimbursement rate for nursing facilities (effective January 1996) as an incentive to accept certain patients who would otherwise remain in acute care hospitals at a higher cost. This results in an estimated General Fund savings of \$30 million in 1995-96.

Qualifying Disability for SSI/SSP Benefits. The budget assumes enactment of federal legislation to eliminate alcohol or drug abuse as a qualifying disability for the Supplemental Security Income/State Supplementary Program (SSI/SSP) program. This would result in General Fund savings of \$22 million in SSI/SSP grants and \$22 million in Medi-Cal benefits in 1995-96.

Hospital Payments. The budget assumes that the California Medical Assistance Commission will negotiate no net increase in hospital inpatient reimbursement rates in 1995-96, for an estimated General Fund savings of \$22 million from base budget projections.

Medi-Cal/Medicare Cost Separation. Medi-Cal long term care rates are currently determined using a methodology which combines the costs of services provided to both Medi-Cal and Medicare patients. The budget establishes a new rate-setting methodology which separates out the Medicare costs. This results in an estimated General Fund savings of \$11.6 million in 1995-96.

Public Health

The Department of Health Services administers a broad range of public health programs, including (1) programs that complement and support the activities of local health agencies controlling environmental hazards, preventing and controlling disease, and providing health services to populations who have special needs and (2) state-operated programs such as those which license health facilities and certain types of technical personnel.

Reaching Early Access for Children's Health (REACH) Program. The budget includes \$20 million from the General Fund (and \$20 million in assumed federal funds) to expand outpatient health care services effective April 1996 to children in low-income households, which currently pay a share of cost for such services or do not qualify for services. The program would cover children, aged 0-5, who are legal residents and whose family income levels fall between 133 percent and 200 percent of the federal poverty level. However, implementing legislation for this program was not enacted.

Teen Pregnancy Prevention Program. The Budget Act appropriates \$12 million from the General Fund for a comprehensive teen pregnancy prevention program. Funding will go towards a media campaign (\$5.8 million), local intervention programs (\$2.9 million), increased enforcement of statutory rape laws (\$2.4 million), and an AFDC informational campaign (\$1 million).

Distribution of Proposition 99 Revenues is Changed. The Legislature adopted legislation (Ch 194/95 [SB 493, Maddy]) to decrease the percentage of Proposition 99 revenues (the Tobacco and Health Protection Act of 1988) allocated to the Health Education and Research accounts, and increase the revenues to the Physician Services and Unallocated accounts, for 1995-96. This was in response to an earlier court ruling that statutory appropriations of Proposition 99 funds from the Health Education and Research accounts for certain health programs violated the provisions of the proposition. Senate Bill 493 was designed to permit the expenditure of \$63.7 million for various health and related programs. However, implementation of the bill has been enjoined by the Superior Court.

Child Immunization Program. The budget provides \$20 million from the General Fund (equivalent to the savings from free federal vaccines) for a program to raise immunization rates among children. Funds will support the provider rate increases (\$9 million), grants to improve outreach (\$4 million), development of a local immunization tracking system (\$3.3 million), grants to expand services (\$3.5 million), and state administration (\$200,000).

Substance Abuse Treatment

The Department of Alcohol and Drug Programs (DADP) performs Medi-Cal related functions under an agreement with the Department of Health Services.

Drug/Medi-Cal Program. The Legislature rejected the Governor's proposal to eliminate the Drug/Medi-Cal program (D/MC), but adopted certain cost-containment measures, for an estimated General Fund savings of approximately \$50 million in 1995-96 (to be redirected to drug treatment services). Specifically, the budget legislation:

- ❖ Reduces the maximum rates providers can bill for substance abuse treatment services.
- ❖ Establishes a maximum reimbursement rate for outpatient group counseling in a drug-free setting.
- ❖ Limits the provision of day care habilitative and perinatal services to pregnant and postpartum women.
- ❖ Limits the provision of outpatient “drug-free” services to pregnant and postpartum women, effective July 1, 1996, if the May 1996 projected cost for the D/MC program exceeds \$60 million (General Fund) for 1995-96.

Long-Term Care for Developmentally Disabled Clients

Individuals with developmental disabilities reside in state-operated developmental centers (DCs) or receive services in the community through regional centers.

Closure of Stockton DC. Due to the rapidly declining population in the DCs, the budget reflects the closure of the Stockton DC, for an estimated savings of \$2.5 million in all funds (no General Fund) in 1995-96. The Department of Developmental Services estimates the ongoing annual savings will be about \$13.2 million (\$7.2 million General Fund).

Savings Depend on Federal Action

As indicated above, a number of the provisions that result in savings in the budget require action at the federal level in order to be implemented. Figure 11 (next page) lists these provisions.

Figure 11

**Budget Savings Requiring Federal Action
Health and Social Services Programs
1995-96**

(Dollars in Millions)

	Implementation Date	General Fund Savings
Federal Legislation		
SSI/SSP grant reduction	12-1-95	\$246
Bar sponsored aliens from benefits	10-1-95	54
Eliminate SSP administrative fee	10-1-95	48
Eliminate drug/alcohol abuse as SSI/SSP disability	10-1-95	44
Federal Budget Appropriation		
Funds for Medi-Cal services to undocumented persons	10-1-95	105
Federal Waiver		
AFDC grant reduction	10-1-95	141

JUDICIARY AND CRIMINAL JUSTICE

In this section, we describe the major features of the budget package as they relate to judiciary and criminal justice programs (courts, adult and youth corrections, and other justice-related programs). The 1995-96 budget for these programs totals \$4.7 billion, including \$4.4 billion from the General Fund and \$287 million from state special funds. This amount is about \$723 million below the level proposed by the Governor in January. This reduction is primarily due to the Legislature's rejection of the state-county realignment proposal, thereby reducing General Fund support for the Trial Court Funding Program by \$592 million below the proposed level.

As compared to 1994-95, the General Fund amount represents an increase of \$296 million, or about 6.5 percent, above estimated spending for these programs. The budget assumes that the state will receive \$413 million in federal funds to offset the costs of incarcerating and supervising undocumented felons in state prisons and the Youth Authority. If General Fund expenditures are adjusted to account for these federal funds (as the Governor did in his January budget), total General Fund expenditures would actually decrease by \$84 million, or 1.8 percent, since 1994-95.

Figure 12 shows the major changes in the 1995 Budget Act relative to the Governor's Budget.

Figure 12	
Judiciary and Criminal Justice Programs Major 1995-96 Changes to the Governor's Budget—General Fund	
(In Millions)	
Program/Issue	
Trial Court Funding	
Reject state-county realignment	-\$591.7
Department of Corrections	
Eliminate inflation adjustments	-\$30.5
Reduce funds for costs of salary increase provided in 1994-95	-17.0
Eliminate lease funds for San Bernardino County jail	-11.5
Department of the Youth Authority	
Increase monthly charges to counties for commitments	-\$11.9 ^a
Implement sliding scale charge for county commitment of less serious offenders	-9.3 ^a

^a Implementing legislation not enacted.

Judiciary

The 1995 Budget Act provides \$165 million for support of the state judiciary, which includes the California Supreme Court, the Courts of Appeal, Judicial Council, and the Commission on Judicial Performance. This represents an increase of \$14.2 million, or 9.4 percent, above 1994-95 expenditures. The increase is primarily due to caseload and rate increases for court-appointed counsel services and increased staffing to legislatively approved levels.

Trial Court Funding

In January, the Governor proposed about \$1.3 billion for support of the Trial Court Funding Program, which was roughly a two-fold increase, as part of his state and county restructuring proposal. The Legislature ultimately rejected the proposal and deleted \$592 million of the proposed increase. Thus, the budget provides a total of \$663 million (\$508 million from the General Fund and \$155 million from penalty and fine revenues) for support of local trial courts in 1995-96. This level of state support covers about 37 percent of statewide trial court expenses in 1995-96, or about 1 percent more than the state's 36 percent share paid in 1994-95.

Department of Corrections

The budget provides a total of \$3.3 billion (\$3.2 billion from the General Fund and \$59 million from special and bond funds) for support of the California Department of Corrections (CDC). This represents an increase of about 8 percent above the 1994-95 level and is primarily due to projected increases in inmate and parole populations. The most significant reductions below the level initially requested by the Governor in January were elimination of funds proposed to lease a jail in San Bernardino County in order to house state prison inmates (\$11.5 million), elimination of funds for inflation adjustments (\$30.5 million), and reduction in funds for the annualized costs of employee pay increases granted in 1994-95 (\$17 million). Instead of receiving additional funds to cover these costs, the department will have to absorb these last two reductions within its existing budget. The budget also includes a net reduction of about \$38.1 million below the January request to reflect changes in caseload estimates contained in the May Revision.

Inmate and Parole Caseloads. The Legislature considered a number of changes that would have saved money by reducing the number or length of stay of offenders in prison and on parole. None of these changes were included in the final budget, however. The budget is based on the administration's projected inmate population of about 142,500 inmates by June 30, 1996, an increase of approximately 11 percent over 1994-95. The parole population is projected to reach about 94,000 parolees by June 30, 1996, an increase of about 1 percent.

New Prisons. The budget includes \$27 million to activate new prisons in Lassen and Monterey Counties and to fully open a new prison in Madera County that was activated in 1994-95. These facilities are designed to house a total of about 5,500 inmates. The budget also includes \$126 million (\$116 million in bond funds and \$10 million in the General Fund) for construction of 16,500 emergency beds in 22 existing institutions.

Federal Funds for Incarceration and Supervision of Undocumented Felons. The budget assumes receipt of \$413 million in federal funds to offset the state's costs for the incarceration of undocumented inmates and wards in state prison and the Youth Authority, as well as the supervision of undocumented immigrant parolees. This amount represents an increase of \$380 million over the amount the state received in 1994-95 and is about \$168 million higher than existing federal authorizations and appropriations for this purpose.

Department of the Youth Authority

The budget provides \$345 million (\$343 million from the General Fund and \$1.5 million from special and bond funds) for support of the Department of the Youth Authority. The General Fund amount is \$13.4 million, or 3.7 percent, less than 1994-95 expenditures. The budget includes an augmentation of \$9.7 million from the General Fund (including \$3.3 million in Proposition 98 funds) to cover the costs of the projected increase of 5.5 percent in the Youth Authority's ward population and 4.8 percent in the parole population. These increases were offset by elimination of one-time expenditures in 1994-95 and reductions that were to be offset by increases in fees charged to counties for commitments to the Youth Authority.

Increases in County Fees for Youth Authority Commitments. The budget assumed enactment of a trailer bill, AB 906 (Aguiar), with two provisions that would increase the fees paid by counties, thereby partially offsetting the state's costs of commitments to the Youth Authority. The department's General Fund budget was reduced by \$21.3 million in anticipation of passage of AB 906.

The first provision would increase from \$25 to \$150 the monthly charges paid by counties for Youth Authority commitments, based on changes in inflation since the fee was established in 1961. This change would result in a General Fund savings of \$11.9 million. The second provision would institute a "sliding scale" whereby counties would pay additional fees to cover the costs of less serious offenders who are committed to the Youth Authority. This change would result in a General Fund savings of \$9.3 million.

Assembly Bill 906 was not enacted, however, and, no other legislation was enacted that contained the fee increases. Consequently, the department will have to absorb this as an unallocated reduction or propose a deficiency. The budget totals prepared by the Department of Finance assume that these savings will not be realized and the Youth Authority will receive a deficiency allocation of \$21.3 million.

State Support of County Probation Camps and Ranches Not Enacted. Assembly Bill 906 also included an appropriation of \$32.7 million to the Youth Authority for distribution to approximately 21 counties to support county probation camps and ranches that house juvenile offenders. As we indicated above, AB 906 was not enacted, nor was any other bill that contained the funds for the county camps and ranches.

TRANSPORTATION

Support. The 1995-96 budget provides about \$1.6 billion from various special funds for support of the Department of Transportation (Caltrans)—about 5 percent less than in 1994-95. The reduction is the net result of several large budget adjustments, including:

- ❖ The budget reduces (1) support in various programs throughout Caltrans by \$67 million and (2) capital outlay support by \$71 million. These reductions result in a decline in Caltrans staff of 1,129 personnel-years.
- ❖ The budget also imposes a \$28 million reduction that Caltrans will have to absorb within its existing budget to fund the full-year costs of salary increases granted in 1994-95. The budget also reduces \$30 million from various programs including administration, vehicle purchase, and local planning of transportation projects.
- ❖ The budget includes \$18 million for Caltrans to comply with a court order that it reduce toxic contamination of wastewater runoff from roads and from Caltrans' facilities.

Local Assistance. The budget provides \$845 million for local assistance programs—about 8 percent less than in 1994-95. The reduction results mainly from appropriating \$100 million, rather than the statutory level of \$200 million, for the State-Local Transportation Partnership Program. This program provides state matching funds for local transportation projects.

Capital Outlay. The budget provides \$2.4 billion for transportation capital outlay projects—about 33 percent more than in 1994-95. The increase is made possible by appropriating in 1995-96 federal and state transportation funds that are expected to be received in future years. Specifically, the budget assumes that in 1995-96 Caltrans will

obligate \$1.7 billion of future federal transportation funds and will also borrow up to \$147 million against future state gas tax revenues. The budget also provides funds for seismic retrofit including \$81 million for state highway bridges and \$56 million for toll bridge seismic retrofit through March 1996. In addition, the Legislature has authorized a \$2 billion general obligation bond that, subject to voter approval, would provide a new funding source for seismic retrofit of state highway bridges and toll bridges.

Transfers to the General Fund. The budget shifts \$77 million from the State Highway Account to the General Fund in order to pay for debt service on state rail bonds in 1995-96. The budget also includes a \$54 million transfer of revenues from document sales from the Motor Vehicle Account to the General Fund. In 1994-95, the budget made similar types of funding shifts.

NATURAL RESOURCES

The budget provides a total of about \$1.0 billion (about \$430 million General Fund) for natural resources programs in 1995-96. This amount includes about \$834 million to support various resources agencies and conservancies, and \$162 million for local assistance and capital outlay. This amount is about \$155 million (13 percent) less than estimated 1994-95 expenditures.

In particular, the 1995 budget provides \$4.5 million from the Harbors and Watercraft Revolving Fund over three years to Los Angeles County for operational costs, contingent on the county accepting fee title for eight beaches from the state. If the county does not accept fee title for these beaches, then the Department of Parks and Recreation will continue to operate the beaches, at a cost in 1995-96 of about \$6.8 million from the General Fund.

The 1995 budget also includes:

- ❖ \$19.4 million from the California Beverage Container Recycling Fund for support of the Depart-

ment of Parks and Recreation. This is a new funding source for the department and offsets General Fund costs.

- ❖ \$20 million for the Department of Forestry and Fire Protection for emergency fire fighting operations.

ENVIRONMENTAL PROTECTION

The 1995 budget provides about \$631 million for environmental protection programs, including about \$561 million to support various environmental protection agencies, and \$70 million for local assistance. This amount is about \$5 million (1 percent) less than estimated 1994-95 expenditures—reflecting the following major changes:

- ❖ A \$10 million increase in the Underground Storage Tank Cleanup Fund Program which is supported by assessments on tank owners.
- ❖ A reduction of \$12.3 million in grants and loans for local water reclamation and wastewater treatment facility construction, mainly due to a depletion in bond funds to provide a state match for federal funds.
- ❖ A reduction of \$7.3 million in support for various programs in the Department of Toxic Substances Control, in part to provide \$4.1 million for an expedited hazardous waste site cleanup pilot program.

CAPITAL OUTLAY

As shown in Figure 13 (next page), the 1995 Budget Act includes almost \$700 million for capital outlay (excluding transportation and the State Water Project). This amount is \$187 million less than

proposed by the Governor. Major legislative changes to the Governor's Budget proposal included the following:

- ❖ A reduction of \$137 million in general obligation bond funds for seismic retrofit of state buildings. In general, this reduction represents a deferral of funding for the construction phase of these projects because construction was not scheduled to begin in 1995-96.
- ❖ Reductions totaling \$58 million (General Fund and lease-payment bonds) in projects for the Department of Corrections. This amount includes \$42 million in reductions for the emergency housing program and \$16 million from deferring the construction phase of two infrastructure projects.
- ❖ Deletion of \$27 million from lease-payment bonds that was proposed for development of a new headquarters building for the Office of Emergency Services.

Figure 13

1995-96 Capital Outlay Programs^a

(In Millions)	
Legislative/Judicial/Executive	\$0.1
State and Consumer Services	31.3
Transportation	20.3
Resources	66.9
Health and Welfare	5.9
Corrections	143.3
Higher Education	399.7
General Government	23.3
Total	\$690.8

^aExcluding highways and the State Water Project.

- ❖ An increase of \$33 million from lease-payment bonds for two community college construction projects.

Bond Debt Service

Current Debt Service Costs. We estimate that the state's General Fund debt service payments on long-term bonds (general obligation and lease-payment) will be about \$2.3 billion during 1995-96. This is about 5.3 percent of estimated General Fund revenues.

Future Debt Service Costs for Bond Appropriations in the 1995-96 Budget Act. The budget includes appropriations totaling about \$640 million from bond funds. This amount consists of \$140 million from general obligation bonds and \$500 million from lease-payment bonds. These bonds will be used for the following purposes:

- ❖ Capital outlay projects of state agencies and the community colleges (\$570 million).
- ❖ Capital planning and bond program administrative costs of certain state agencies (\$33 million).
- ❖ Local government capital projects (\$35 million).

The state's General Fund debt service costs for these bonds would begin after 1995-96 and would average about \$50 million annually for about 25 years until the bonds are paid off.

Transportation Seismic Retrofit Program. The Legislature approved one bond measure for the March 1996 ballot. As discussed under the Transportation section, the 1995 budget package includes a \$2 billion general obligation bond measure, Ch 310/95 (SB 146, Maddy), to finance earthquake safety improvements to the state's transportation system. If approved by the voters, the state's General Fund debt service costs for these bonds would begin after 1995-96 and would average around \$140 million for about 25 years until the bonds are paid off.

GENERAL GOVERNMENT

Business and Labor Employee Compensation

Under approved memoranda of understanding (MOUs), represented state employees (other than employees of the University of California and the California State University) received a 3 percent general salary increase (GSI) on January 1, 1995. The Department of Personnel Administration approved an identical increase for nonrepresented employees. The full-year, 1995-96 costs due to this GSI, however, are provided only for that portion attributable to employees directly engaged in public safety, 24-hour care, or revenue-generating activities within 15 specified departments. The amounts needed to pay the GSI to other state employees will be borne by departments and agencies from existing support funds.

Negotiations are underway for new MOUs, but have been completed only for bargaining unit 5 (highway patrol officers). The budget does not include funds for new employee compensation costs that may be included in these prospective MOUs. Any MOUs requiring the expenditure of state funds would be subject to approval by the Legislature through the enactment of legislation. When this report was written, SB 544 (Dills) contained approval of the proposed unit 5 MOU and appropriated \$17.1 million from the Motor Vehicle Account and other special funds for additional salary and benefit costs of the MOU in 1995-96. According to the Department of Personnel Administration, these costs will total about \$30 million in 1996-97.

Unallocated Reductions

The 1995 Budget Act includes two control sections requiring the Department of Finance to reduce General Fund appropriations by a statewide total of \$45 million. Section 3.75 mandates \$10 million of savings resulting from reductions in managers, supervisors, or administrative costs. Section 3.90 imposes an unallocated reduction of \$35 million to state operations. The Legislature exempted various departments and other entities from the provisions of one or both of the control sections.

Department of Insurance

The Legislature approved a \$9.4 million augmentation from the Insurance Fund for the Department of Insurance to conduct Proposition 103 rate rollback hearings. The department expects many insurance companies to request evidentiary hearings before they will meet their rate rollback obligation. This augmentation will be financed by a 47 percent increase in the fee the department charges to administer Proposition 103.

REVENUES

Budget Actions to Increase Collections

The 1995-96 budget package includes the following actions to enhance revenue collections:

Collections from Federal Tax Refunds. The budget assumes that the federal government will enact legislation to collect delinquent state taxes out of refunds owed to federal taxpayers (the state currently provides a similar service for the federal government). Congress is currently considering this legislation, which the budget estimates would generate state revenues of \$85 million in 1995-96.

Enhanced Audit and Collection Activities. The Legislature added a total of \$7 million to the budgets of the Franchise Tax Board and the State Board of Equalization to fund additional personnel to enhance audit and collection activities. These audit and collection activities will increase tax revenues by an estimated \$61 million in 1995-96.

Governor's Proposed Tax Reductions Not Included in the 1995-96 Budget

The budget package does not include the tax reductions proposed by the Governor in January and May. Instead, these proposals are being considered in legislation separate from the budget package.

Phased-In Income Tax Reduction Proposal. Under this proposal, the current temporary 10 percent and 11 percent income tax rates for high-income taxpayers, scheduled to sunset in 1996, would have

remained in effect. However, those rates and most other business and personal income tax rates then would have been reduced by 5 percent increments each year over a three-year period beginning in 1996. The Franchise Tax Board estimated that this proposal would have resulted in a net revenue reduction of \$179 million in 1995-96 and a cumulative net revenue reduction for the first four fiscal years of \$7.1 billion.

The revenue estimate for the 1995-96 budget package includes the effect of the sunset of the higher income tax rates in 1996 (a loss of \$325 million in 1995-96).

Other Proposals. The adopted budget also does not include two other tax changes proposed by the Governor in the May Revision. One change would have liberalized the tax credit for hiring employees in enterprise zones (\$10 million 1995-96 revenue loss). The second change would have conformed state tax law with federal tax law regarding cancellation of debts and the treatment of credits and deductions related to passive business income (\$34 million 1995-96 revenue loss).