

SENIOR CITIZENS' PROPERTY TAX ASSISTANCEItem 9100-101 (a) from the
General Fund

Budget p. GG 160

Requested 1986-87	\$5,364,000
Estimated 1985-86	6,311,000
Actual 1984-85	7,839,000
Requested decrease \$947,000 (-15.0 percent)	
Total recommended reduction	None

GENERAL PROGRAM STATEMENT

The Senior Citizens' Property Tax Assistance program provides partial reimbursement for property taxes paid by homeowners with less than \$12,000 of household income who are (1) 62 years old and over, or (2) totally disabled, regardless of age. Assistance varies inversely with income, and ranges from 96 percent of the tax for homeowners with household incomes not exceeding \$3,000, to 4 percent of the tax for those with incomes between \$11,500 and \$12,000. The state provides senior citizens' property tax assistance only for taxes paid on the first \$34,000 of property value, after taking into account the \$7,000 homeowners' property tax exemption. Assistance provided in 1986-87 will be based on taxes paid in 1985-86.

OVERVIEW OF THE BUDGET REQUEST

The budget proposes that \$5,364,000 be appropriated for the cost of this program in 1986-87—\$947,000 less than estimated current-year expenditures. The budget assumes that participation in the program will drop from 80,000 persons in the current year to 59,000 in the budget year.

ANALYSIS AND RECOMMENDATIONS*We recommend approval.*

Ever since Proposition 13 was approved by the voters in 1978, both the number of participants and the average value of assistance provided by the Senior Citizens' Property Tax Assistance program have declined steadily. As a result, program expenditures are estimated to fall by 54 percent between 1979-80 and the current year. Table 1 displays recent trends in the levels of program participation, average claim, and expenditures. The table also presents information on the claimant's average income and average property taxes paid.

As displayed in Table 1, the average paid claim was \$93.25 in 1982-83. By 1984-85, the last year for which data are available, the average claim had fallen to \$92.52. In the same period, participation had dropped to 84,153, which amounts to an average annual decline of 16 percent. With both the average claim and the level of participation falling, program expenditures fell from \$11.1 million to \$7.8 million between 1982-83 and 1984-85.

Data from the Franchise Tax Board (FTB) indicate that program levels will continue to fall through the current year in a manner consistent with these trends. Based on these data, we estimate that 70,695 claims will be filed (a drop of 14 percent) and that the average claim will be \$89.92 (a drop of 2.8 percent) in 1985-86. Current-year expenditures, as a consequence, will fall to \$6,357,000.

Table 1
Senior Citizens' Property Tax Assistance
1982-83 through 1985-86

	<i>Actual</i> 1982-83 ^a	<i>Actual</i> 1983-84 ^a	<i>Actual</i> 1984-85 ^a	<i>Estimated</i> 1985-86 ^b
Number of Claimants:				
Senior	111,718	92,256	78,834	66,178
Disabled	6,910	5,907	5,319	4,518
Total.....	118,628	98,163	84,153	70,696
Total Assistance (in millions)	\$11.1	\$9.0	\$7.8	\$6.4
Per Claimant Averages:				
Household income	\$7,042	\$7,143	\$7,113	\$7,210
Property taxes.....	\$263	\$270	\$273	\$277
Assistance:				
Amount	\$93.25	\$91.66	\$92.52	\$89.92
Percent of taxes	35.4%	34.5%	33.9%	32.5%

^a Source: Franchise Tax Board.

^b Legislative Analyst's office estimates.

We expect that participation will continue to fall at a rate consistent with historical trends. Specifically, our analysis indicates that participation will fall by about 15 percent, to 60,137 persons while the average claim will fall by about 0.9 percent to \$89.13 in the budget year. On the basis of these estimates, we project budget-year expenditures of \$5,360,000 in 1986-87. This amount is almost identical to the amount proposed in the budget. Thus, our analysis indicates that the proposed expenditure level is sufficient and accordingly, we recommend that the amount be approved as budgeted.

SENIOR CITIZENS' PROPERTY TAX DEFERRAL

Item 9100-101 (b) from the
 General Fund

Budget p. GC 161

Requested 1986-87	\$8,500,000
Estimated 1985-86.....	8,576,000
Actual 1984-85	7,200,000
Requested decrease \$76,000 (-0.9 percent)	
Total recommended reduction	\$1,500,000

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis
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1. *Senior Citizens' Property Tax Deferral. Reduce Item 9100-101(b) by \$1.5 million.* Recommend reduction to correct for overbudgeting.

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SENIOR CITIZENS' PROPERTY TAX DEFERRAL—Continued**GENERAL PROGRAM STATEMENT**

The Senior Citizens' Property Tax Deferral program allows eligible homeowners to postpone payment of all or a portion of the property taxes on their residences, with the state paying local governments on their behalf. The state also puts a lien on the property to assure that the taxes are paid when the property is transferred. Thus, under this program the state essentially provides a loan to the eligible property owners, which is repaid when the property is sold. Interest is charged on amounts deferred at a rate tied to the yield on investments made by the Pooled Money Investment Account. This Budget Bill item appropriates funds to the State Controller, who administers the program and pays local governments on behalf of the participating senior citizens.

OVERVIEW OF THE BUDGET REQUEST

The budget proposes \$8,500,000 for the Senior Citizens' Property Tax Deferral program in 1986-87. This is a reduction of \$76,000, or 0.9 percent, from estimated current-year expenditures.

ANALYSIS AND RECOMMENDATIONS

We recommend that the Legislature reduce the amount budgeted for this program by \$1.5 million, or 18 percent, to correct for overbudgeting.

At the time the budget was prepared, the State Controller's office (SCO) had estimated that 10,247 claims would be approved in 1985-86, representing an increase of 2.7 percent over the prior year. It also estimated that expenditures would increase to \$8,576,000, an increase of 19 percent. These estimates imply that, while the average claim for the other two senior citizens' property tax assistance programs has been falling in recent years, the average claim for this program will rise from \$722 to \$837. The proposed expenditure level in the budget is based on the SCO estimates.

Participation Will Decline. More-recent data than were available when the budget was prepared indicate that the SCO and the Department of Finance have overestimated the level of participation, and therefore the level of expenditures for the current year. Based on these later data, we estimate that participation will actually decline by about 3.4 percent, from 9,979 claims in 1984-85 to 9,645 in 1985-86. This reduction in participation has occurred despite recent legislation to expand eligibility to mobilehome owners and disabled persons, and reverses a long-standing trend of increasing annual participation.

The decline may be attributable to two programmatic changes made by Chapter 1051, Statutes of 1983. First, this legislation lowered the income ceiling for new claimants (from \$34,000 to \$24,000). Second, the legislation provided that the interest rate charged participants would be based on the yield earned by the Pooled Money Investment Fund, rather than a fixed 7 percent simple interest rate. Because this fund's annual yield has been between 30 percent and 50 percent higher than the flat 7 percent rate, the cost of deferring taxes has been increased.

Reflecting the reduced level of participation, program expenditures are likely to be less than budgeted in the current year. Assuming that the average value of these claims will remain at the 1984-85 level (\$722), we estimate that current-year program expenditures will drop to less than \$7

million, an amount \$1.6 million below what is reflected in the budget. Although no data on the average claim value for 1985-86 is available at this time, it does not appear that an increase is likely.

For the budget year, the Department of Finance requests \$8.5 million for this program, based on its assumption that 13,750 persons will participate. This participation level is 43 percent higher than the most-recent estimate for the current year.

Our review of the decline in participation during the current year indicates that 1986-87 program expenditures will be significantly lower than what is reflected in the budget. Even if program participation and the average claim remain at the current-year level, we estimate that program expenditures will not exceed \$7 million in the budget year. Accordingly, we recommend that the Legislature reduce by \$1.5 million the amount budgeted for the Senior Citizens' Property Tax Deferral Program.

SENIOR CITIZEN RENTERS' TAX ASSISTANCE

Item 9100-101(c) from the General Fund

Budget p. GG 161

Requested 1986-87	\$26,285,000
Estimated 1985-86.....	29,205,000
Actual 1984-85	33,237,000
Requested decrease \$2,920,000 (-10.0 percent)	
Total recommended reduction	None

GENERAL PROGRAM STATEMENT

This program provides tax relief to renters who are 62 years old and over, and to totally disabled persons regardless of age, if their total household income is less than \$12,000. Assistance varies inversely with income, and assumes that all renters pay the equivalent of \$250 in property taxes. Actual assistance ranges from \$240 (96 percent of \$250) for persons with less than \$3,000 of total household income, to \$10 (4 percent of \$250) for persons with income between \$11,500 and \$12,000. This assistance is in addition to the personal income tax credit provided to all renters under Item 9100-101(g).

OVERVIEW OF THE BUDGET REQUEST

The budget proposes an appropriation of \$26,285,000 from the General Fund for the Senior Citizen Renters' Tax Assistance program in the budget year. This is \$2,920,000, or 10 percent, less than the administration's estimate of current-year expenditures.

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

Since 1981-82, the Senior Citizen Renters' Tax Assistance program has shown marked declines in both participation and the average claim, causing program expenditures to fall. For the current year, the Department of Finance estimates that expenditures will drop by 11.5 percent to \$29.2 million. More-recent data from the Franchise Tax Board (FTB) indicate

SENIOR CITIZEN RENTERS' TAX ASSISTANCE—Continued

that program expenditures will fall by only 10.6 percent, to \$29.5 million. Table 1 shows the number of approved claimants and the total assistance they received in the years 1982–83 through 1985–86. It also presents data on the average income, the average property taxes, and the average assistance received, for all claimants.

Table 1
Senior Citizen Renters' Tax Assistance
1982–83 through 1985–86

	<i>Actual</i> 1982–83 ^a	<i>Actual</i> 1983–84 ^a	<i>Actual</i> 1984–85 ^a	<i>Estimated</i> 1985–86 ^b
Number of Claimants:				
Senior.....	202,597	187,108	176,345	164,621
Disabled.....	82,182	73,311	70,029	65,903
Totals.....	284,779	260,419	246,374	230,524
Total Assistance (in millions).....	\$41.9	\$36.1	\$33.0	\$29.5
Per Claimant Averages:				
Household income.....	\$5,848	\$6,052	\$6,152	\$6,338
Assistance.....	\$147	\$139	\$134	\$128

^a Source: Franchise Tax Board
^b Legislative Analyst's office estimates.

In estimating budget-year expenditures, the Department of Finance assumed that expenditures would drop by 10 percent from its estimate for the current year, to \$26.3 million. Our analysis of the program's current-year expenditure level, and the likely rate at which expenditures will drop in the budget year, indicates that the proposed expenditure level is sufficient. Accordingly, we recommend that the amount be approved as budgeted.

HOMEOWNERS' PROPERTY TAX RELIEF

Item 9100-101 (d) from the General Fund

Budget p. GG 162

Requested 1986–87.....	\$336,200,000
Estimated 1985–86.....	335,200,000
Actual 1984–85.....	331,919,000
Requested increase \$1,000,000 (+0.3 percent)	
Total recommended reduction.....	None

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis
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1. Homeowners' Property Tax Relief. Recommend that the Legislature direct the Department of Finance, at the time of budget hearings, to comment on the apparent underfunding of this item.

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GENERAL PROGRAM STATEMENT

The Constitution grants a \$7,000 property tax exemption on the full value of an owner-occupied dwelling, and requires the state to reimburse local governments for the resulting tax loss. This item provides the funds for these Constitutionally-required reimbursements.

OVERVIEW OF THE BUDGET REQUEST

The budget proposes expenditures of \$336.2 million for Homeowners' Property Tax Relief in 1986-87. This is an increase of \$1 million, or three-tenths of a percent, above the current-year estimate of expenditures contained in the budget.

ANALYSIS AND RECOMMENDATIONS

We recommend that the Department of Finance, at the time of budget hearings, comment on the apparent underfunding of the Homeowners' Property Tax Relief program.

Table 1 displays information on the costs and levels of participation in the program since 1982-83. The data for the current year are based on information from the Board of Equalization and the State Controller's office. According to this data, an estimated 4,320,000 claimants will participate in the program during the current year, suggesting a 1.4 percent increase in participation over the number of participants in 1984-85. Since 1982-83, the number of claims filed has increased at an average annual rate of eight-tenths of one percent.

The increased participation rates for the current year can be explained, in part, by improved conditions for homeownership. According to the Department of Finance, the mortgage rate fell by 7.6 percent in 1985. At the same time, total personal income rose by 8.1 percent in California. Together, the reduction in the cost of financing and the increased income helped make homes more affordable, thereby increasing the number of eligible claimants in 1985-86. According to the Department of Finance, mortgage interest rates and personal income will continue to improve through the budget year.

Our analysis indicates that, at a minimum, program participation in 1986-87 should increase at a rate consistent with historical trends.

Table 1
Homeowners' Property Tax Relief
1982-83 Through 1985-86

	Actual 1982-83 ^a	Actual 1983-84 ^a	Actual 1984-85 ^a	Estimated 1985-86 ^b
Claimants (thousands)	4,214	4,256	4,262	4,320
Percent change from prior year	1.1%	1.0%	0.1%	1.4%
Tax reimbursement (millions)	\$334.0	\$334.0	\$331.9	\$335.5
Percent change from prior year	0.1%	0.0%	-0.6%	1.1%
Average tax benefit	\$79.26	\$78.48	\$77.91	\$77.66
Percent change from prior year	1.1%	-1.0%	-0.7%	-0.3%
Exempt assessed valuation (billions)	29.4	29.6	29.8	30.2
Property tax rate ^c	1.131%	1.126%	1.113%	1.109%

^a Source: State Controller's Office, Department of Finance.

^b Legislative Analyst's office estimates.

^c Including debt service.

HOMEOWNERS' PROPERTY TAX RELIEF—Continued

For 1986–87, the budget proposes expenditures of \$336.2 million, an increase of \$700,000 over our estimate of current-year expenditures. When preparing its proposal, the Department of Finance did not project the level of participation or average claim. Rather, it assumed that expenditures would rise by one-third the amount which they rose in the current year.

We find no compelling rationale for estimating program costs in this manner. More importantly, the estimate appears unrealistically low. If the average claim continues to fall by an amount consistent with historical trends, only 18,000 additional claims (an increase of 0.4 percent) would have to be filed in the budget year to reach the expenditure level proposed by the administration. If, on the other hand, Finance had assumed that participation and the average claim would change in a manner consistent with historical trends, it would have proposed expenditures of about \$338.2 million—\$2 million more than what the budget includes. Given the likelihood that the existing conditions in the housing market will result in higher participation than what historical trends would suggest, expenditures in 1986–87 could be even higher.

We recommend that, at the time of the budget hearings, the Department of Finance comment on the likelihood that expenditures for this program will be within the amount proposed in the budget.

OPEN-SPACE PAYMENTS TO LOCAL GOVERNMENTS

Item 9100-101(e) from the General Fund

Budget p. CG 162

Requested 1986–87	\$14,000,000
Estimated 1985–86.....	13,800,000
Actual 1984–85	13,972,000
Requested increase \$200,000 (+1.4 percent)	
Total recommended reduction	None

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. Open-Space Payments to Local Governments. Recommend that, at the time of budget hearings, the Department of Finance comment on the apparent underfunding of this item.

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GENERAL PROGRAM STATEMENT

Existing law requires the state to provide replacement revenue to cities and counties in order to compensate them for reduced property tax collections on open-space and agricultural land. The Secretary of the Resources Agency, through the Department of Conservation, administers the subvention program.

Under the California Land Conservation Act of 1965 (familarly known as the Williamson Act), cities and counties may enter into contracts with landowners to restrict the use of property to open-space and agricultural purposes. In return for the restriction, the land is assessed at less-than-

market value, thereby lowering the landowner's costs for holding the property as open space or agricultural land. For the purposes of this act, "agricultural use" is defined to mean use of land for the purpose of producing an agricultural commodity for commercial purposes.

State compensation to cities and counties is based on the type of land under contract, rather than on the actual property tax loss. There are four classifications into which property under contract is categorized, each yielding a different reimbursement rate. These are:

- "\$8 Urban Prime"—for land that is either (a) within an incorporated city with a population of 25,000 or more, or (b) within three miles of a city with such a population.
- "\$5 Urban Prime"—for land that is either (a) within an incorporated city with a population between 15,000 and 25,000, or (b) within three miles of a city in this population range.
- "\$1 Other Prime"—for all other prime agricultural land.
- "40 cents Nonprime"—for nonprime land.

Under current law, each contract runs for 10 years, and is automatically renewed each year unless either the landowner or local government files for "nonrenewal." The state does not provide compensation if a contract is "nonrenewed" or canceled. Once a contract is nonrenewed, taxes on the property gradually return, over a 10-year period, to the level at which comparable nonrestricted property is taxed.

As an alternative to nonrenewal, the landowner may petition the local government to cancel the contract. If cancellation is granted, the landowner must (1) pay a substantial cancellation fee to the state (generally about 12.5 percent of the open space valuation), and (2) pay a specified charge to the local government so that it can recapture a portion of the tax benefits enjoyed by the landowner during the term of the contract.

OVERVIEW OF THE BUDGET REQUEST

The budget proposes an appropriation of \$14,000,000 for open-space payments to local governments in the budget year. This is \$200,000, or 1.5 percent, above the amount that the Governor's Budget indicates will be expended in the current year.

ANALYSIS AND RECOMMENDATIONS

We recommend that, at the time of budget hearings, the Department of Finance comment on the apparent underfunding of the open-space subvention program.

Table 1 details the cost and number of acres under Williamson Act contracts from 1982-83 through 1985-86. The data shown for 1985-86 is our estimate, and is based on information from the Department of Conservation and individual cities and counties. The table shows that program expenditures have increased steadily since 1982-83. We estimate that expenditures will rise to \$14.1 million in the current year, representing a 0.8 percent increase over 1984-85. This is \$300,000 more than the amount shown in the budget document for 1985-86.

OPEN-SPACE PAYMENTS TO LOCAL GOVERNMENTS—Continued

Table 1
Acres Under Williamson Act Contracts and
Open-Space Payments to Local Governments
1982-83 through 1985-86

Land Category	Acres			
	Actual 1982-83 ^a	Actual 1983-84 ^a	Actual 1984-85 ^a	Estimated 1985-86 ^b
\$8 Urban Prime.....	557,334	553,906	615,141	623,083
\$5 Urban Prime.....	95,043	94,898	110,146	96,689
\$1 Other Prime.....	4,550,532	4,546,980	4,521,283	4,618,258
\$0.40 Nonprime.....	9,976,324	10,185,253	9,952,283	9,984,318
Totals				
Acres	15,179,233	15,381,037	15,198,853	15,322,348
Expenditures	\$13,474,949	\$13,526,819	\$13,974,054	\$14,080,094

^a Source: Department of Conservation, individual cities and counties.

^b Legislative Analyst's office estimates.

As the table indicates, the total *number* of acres under contract has increased by 0.9 percent between 1982-83 and 1985-86. A disproportionate amount of this growth, however, is attributable to the category receiving the highest per-acre reimbursement. Consequently, program *expenditures* have risen at a rate four times faster than the number of acres. In part, the growth in land classified as \$8 Urban Prime is due to the population growth in cities. As discussed in last year's *Analysis*, when a city's population rises above 25,000, land previously classified as \$1 Other Prime or \$5 Urban Prime may be reclassified as \$8 Urban Prime. Thus, if a city with fixed boundaries experiences population growth sufficient to raise its population above 25,000, the land within a three-mile radius of the city will be reclassified into the higher reimbursement category. Similarly, when a city annexes property such that Williamson Act land is brought within the three-mile radius, that land, formerly classified at the 40-cent or \$1 reimbursement rate, may also be reclassified.

For the budget year, we expect that the increase in program expenditures will continue. Assuming a conservative growth rate, we estimate that these expenditures will amount to \$14.2 million, \$200,000 more than what is proposed in the budget. Accordingly, we recommend that, at the time of budget hearings, the Department of Finance comment on the apparent underfunding of this item.

RENTERS' TAX RELIEF

Item 9100-101 (f) from the General Fund

Budget p. GG 163

Requested 1986-87	\$475,000,000
Estimated 1985-86.....	460,000,000
Actual 1984-85	446,098,000
Requested increase \$15,000,000 (+3.3 percent)	
Total recommended reduction	None

GENERAL PROGRAM STATEMENT

The Renters' Tax Relief program provides a fixed payment to persons who are residents of the state and who rent dwellings in California as their principal places of residence on March 1. No age or income limitations apply to renters claiming relief under this program. The credit is \$60 for single renters, \$137 for married couples, heads of households, and surviving spouses, \$69 for married persons filing separately, and \$99 for heads of households with joint custody of their children.

The program is administered through the Personal Income Tax program as a refundable credit. That is, the credit is applied first to any income taxes due, with the balance (if any) paid directly to the renter. Persons with no income tax liability must file a return to receive the tax relief payment. Table 1 provides information about program participation.

Table 1
Renters' Tax Relief Program^a
Number of Renters' Credit Claimants
By Income Year
(in millions)

	<i>Actual</i> 1983	<i>Estimated</i> 1984	<i>Estimated</i> 1985	<i>Estimated</i> 1986
Single	2.26	2.40	2.50	2.61
Joint	1.54	1.54	1.53	1.55
Other ^b	0.72	0.73	0.75	0.79
Total	4.45	4.67	4.78	4.95
Percent change from prior year	4.2%	4.9%	2.4%	3.6%

^a Source: Department of Finance.

^b Includes head of household, surviving spouse, and married filing separately.

ANALYSIS AND RECOMMENDATIONS***We recommend approval.***

As displayed in the budget document, the department estimates that program expenditures will be \$460 million (a 3.1 percent increase over prior-year levels) in 1985-86, and \$475 million (a 3.3 percent increase) in 1986-87. The department also estimates that 4.8 and 5 million renters will participate in the current and budget years, respectively.

Percentage of Population Claiming the Renters' Credit Grows. To

RENTERS' TAX RELIEF—Continued

verify the appropriateness of the claims levels projected in the budget, we compared the ratio of the renters' credit claimants to the state's population. Recent trends in participation suggest that a greater percentage of the state's population is claiming this credit. As displayed in Table 2, between 1982-83 and 1985-86 the ratio of claimants to population has increased from 17.3 percent to 18.4 percent.

Table 2
Trends in Population
and the Number of Renters' Credit Claimants

<i>Fiscal Year</i>	<i>California Population "</i>	<i>Claimants</i>	<i>Percentage of Population</i>
1982-83.....	24,722,270	4,270,000	17.3%
1983-84.....	25,152,433	4,590,000	18.2
1984-85.....	25,575,744	4,670,000	18.3
1985-86.....	25,997,563	4,780,000	18.4

^a Source: Population Research Unit, Department of Finance.

Assuming that this trend continues through the budget year, the department's estimate of 5 million claimants represents a reasonable estimate of program participation. Accordingly, we recommend that this item be approved as budgeted.

SUBSTANDARD HOUSING

Item 9100-101 (g) from the General Fund

Budget p. GG 163

Requested 1986-87	\$120,000
Estimated 1985-86.....	102,000
Actual 1984-85	98,000
Requested increase \$18,000 (+17.6 percent)	
Total recommended reduction	None

GENERAL PROGRAM STATEMENT

The Substandard Housing program provides funds to local agencies for the support of housing code enforcement and rehabilitation activities.

Assembly Bill 475 (Ch 238/74) disallows certain income tax deductions for rental housing that has been found to be in violation of state or local housing codes. Assembly Bill 3515 (Ch 1286/78) provides that the additional tax revenues generated by Ch 238/74 are to be transferred from the General Fund to the Local Agency Code Enforcement and Rehabilitation Fund (LACERF). These funds are distributed by the State Controller to the cities and counties in which the properties found to be in violation of the state or local housing codes are located. Local agencies use these funds for code enforcement activities, housing rehabilitation, and related activities.

Generally, two fiscal years elapse between the time when housing code violations are reported and when the additional tax revenues generated by these violations are distributed to local governments. Table 1 presents information on program activity between 1981-82 and 1984-85.

Table 1
Substandard Housing Program Activity
1982-83 through 1984-85

	1982-83	1983-84	1984-85	Percent Change
Number of noncompliance notices received	470	685	747	9.1%
Number of local agencies submitting notices	16	13	16	23.1
Revenue collected	\$138,000	\$142,186	\$160,531	12.9

Source: Franchise Tax Board.

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

The budget proposes that \$120,000 be transferred from the General Fund to the LACERF in 1985-86 under the Substandard Housing Program. This amount represents the actual revenues generated through the disallowance of deductions during the 1984-85 fiscal year, minus FTB's projected costs (\$40,000) for administering the program. The request is justified, and we recommend that this item be approved as budgeted.

PAYMENT OF INTEREST ON GENERAL FUND LOANS

Item 9620 from the General Fund

Budget p. GG 174

Requested 1986-87	\$1
Estimated 1985-86.....	0
Actual 1984-85	0
Requested increase—None	
Total recommended reduction	None

GENERAL PROGRAM STATEMENT

Whenever cumulative cash disbursements exceed cumulative incoming revenues, the General Fund must borrow monies to cover these disbursements. This borrowing, which is done on a short-term basis, often requires the payment of interest.

To meet the General Fund's short-term cash needs, the state may borrow either internally, from the unexpended balances in its various funds, or externally, through the issuance of short-term borrowing instruments. External borrowing is preferable because the state can lend money at a higher interest rate than the rate at which it must borrow. This is because when the General Fund borrows externally, it does so at *tax-exempt* interest rates, whereas when it borrows internally, it does so, in effect, at *taxable* interest rates—since most of the funds borrowed would otherwise