

PAYMENT OF INTEREST ON GENERAL FUND LOANS

Item 9620 from the General Fund

Budget p. GG 175

Requested 1987-88	\$1
Estimated 1986-87.....	0
Actual 1985-86	0
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 own 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 be invested in taxable securities. The Legislature has expressed its intent that the state use external, rather than internal, borrowing whenever it is advantageous to the state.

The interest paid on external loans is funded by a continuous appropriation in the Government Code, not out of the appropriation made in this item.

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

The budget requests \$1 for payment of interest on the loans made to the General Fund from *internal* sources in 1987-88. Although \$1 obviously would not be sufficient were the General Fund forced to borrow from internal sources, some amount must be appropriated in order to maintain this item in the budget; and thereby allow a deficiency appropriation in the event that an emergency requires extensive internal borrowing.

Our analysis indicates that the state is not likely to borrow from internal sources requiring the payment of interest in order to meet its cash needs in the budget year. Nevertheless, it would be prudent to maintain this option. Accordingly, we recommend that the item be approved.



HEALTH BENEFITS FOR ANNUITANTS

Item 9650 from the General
Fund

Budget p. GG 183

Requested 1987-88	\$126,505,000
Estimated 1986-87	117,731,000
Actual 1985-86	107,923,000
Requested increase \$8,774,000 (+7.5 percent)	
Total recommended reduction	None

GENERAL PROGRAM STATEMENT

This appropriation provides the state's contribution toward monthly health and dental insurance premiums for annuitants of retirement systems to which the state contributes as an employer. These systems are the Judges', Legislators', Public Employees', and State Teachers' Retirement Systems. For the latter two systems, the health insurance premium contribution is made only on behalf of retired *state* employees.

This program offers a degree of post-retirement security for employees and their dependents by contributing toward the cost of state-approved health insurance plans. Government Code Section 22825.1 expresses legislative intent that the state pay an average of 100 percent of *health* insurance costs for active employees and annuitants, and 90 percent of such costs for the dependents of employees.

This appropriation also provides the state's contribution toward *dental* insurance premiums for annuitants of the Judges', Public Employees', and State Teachers' Retirement Systems. The State Employee's Dental Care Act does not stipulate the same intent with regard to the state's contribution toward premium costs as that set forth in Section 22825.1. Currently, the state is paying 100 percent of dental premium costs, with the exception of the "family" plan for highway patrol officers (where the state pays 90 percent of the cost) and all three plans for correctional officers (where the state pays 97 percent of the cost).

OVERVIEW OF THE BUDGET REQUEST

The budget proposes an appropriation of \$126,505,000 from the General Fund for payment of health and dental insurance premiums in 1987-88. This is \$8,774,000, or 7.5 percent, more than estimated current-year expenditures. The increase is attributable solely to the projected growth in the number of annuitants.

The budget proposes expenditures of \$109.5 million for the payment of health insurance premiums. This is \$7.1 million, or 7 percent, more than estimated 1986-87 expenditures. Proposed expenditures for dental insurance premiums are \$17 million, which is \$1.6 million, or 11 percent, more than estimated current-year expenditures. These amounts proposed for 1987-88 do *not* include funds for premium rate increases. The budget proposes to fund a projected 5.5 percent increase in health premium rates and a projected 7.2 percent increase in dental premium rates through a \$6.7 million appropriation provided in the Augmentation for Employee Compensation item (9800-001-001).

The state contributions for these programs are paid initially from the General Fund. Special fund agencies are assessed pro rata charges for these costs, which are then credited to the General Fund. Approximately

one-third of the state's contribution is recovered from special fund agencies.

The increases in the number of annuitants and state costs for the health and dental care programs are shown in Table 1. The costs in this table *include* the amounts budgeted in Item 9800-001-001 for health and dental premium rate increases.

Table 1
Health and Dental Benefits
Annuitants and Costs
1985-86 through 1987-88
(dollars in thousands)

	Number of Annuitants			State Costs			Percent Change From 1986-87
	Actual 1985-86	Est. 1986-87	Prop. 1987-88	Actual 1985-86	Est. 1986-87	Prop. 1987-88	
<i>Health Benefits</i> <i>(by Retirement System)</i>							
Public Employees'	62,658	66,362	70,364	\$92,914	\$100,394	\$112,953	12.5%
District Agricultural Em- ployees'	289	306	325	428	461	515	11.7
Legislators'	90	90	90	139	142	150	5.6
State Teachers'	304	307	310	426	444	473	6.5
Judges'	539	571	606	857	929	1,039	11.8
Subtotals, Health Benefits	(63,808)	(67,636)	(71,695)	(\$94,764)	(\$102,370)	(\$115,130)	(12.5%)
<i>Dental Benefits (by Retirement System)</i>							
Public Employees'	46,194	50,826	55,919	\$12,899	\$15,057	\$17,752	17.9%
District Agricultural Em- ployees'	289	306	325	81	94	111	18.1
Legislators'	41	45	50	12	14	16	14.3
State Teachers'	114	125	138	33	38	44	15.8
Judges'	428	471	518	134	158	186	17.7
Subtotals, Dental Benefits	(47,066)	(51,773)	(56,950)	(\$13,159)	(\$15,361)	(\$18,109)	(17.9%)
Totals	—	—	—	\$107,923	\$117,731	\$133,239	13.2%

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

Our analysis indicates that the proposed increases are reasonable.

UNIVERSAL TELEPHONE SERVICE PROGRAM

Item 9695 from the Universal Telephone Service Fund

Budget p. GG 186

Requested 1986-87 transfer	\$20,000,000
Recommendation	None

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. Fund Transfer. Recommend that the Department of Finance report at budget hearings on the conditions governing the proposed UTSF loan to the General Fund. 1410

GENERAL PROGRAM STATEMENT

Chapter 1143/83 established the Universal Telephone Service Program, which provides low-cost basic telephone service to low-income persons. The program, which is administered by the Public Utilities Commission, is financed by a tax (not to exceed 4%) on intrastate long distance telephone calls. Tax revenues are deposited in the Universal Telephone Service Fund (UTSF). The PUC establishes the criteria for program eligibility and sets the tax rate annually to assure sufficient revenues for the program.

ANALYSIS AND RECOMMENDATIONS

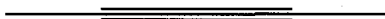
Budget Bill Does Not Specify Terms of UTSF Transfer

We recommend that the Department of Finance report at budget hearings on the conditions governing the proposed UTSF transfer to the General Fund.

The budget proposes to transfer \$20 million from the UTSF to the General Fund on June 30, 1987. Discussions with the PUC indicate that the transfer is to be treated as a loan to the General Fund; however, the Budget Bill does not treat it as such.

From July 1, 1984 until the end of the 1985-86 fiscal year, the UTSF accumulated a surplus of about \$77 million. In order to reduce the surplus, the commission reduced the tax rate from 4.0 percent to 1.5 percent at the beginning of the current year. Even at this lower rate, the fund will have sufficient revenues to support both program expenditures in 1986-87 and 1987-88 and the proposed current-year General Fund transfer. Unless the loan is repaid by 1988-89, however, the commission will have to increase the tax rate to cover projected expenditures in that year.

Our analysis indicates that the UTSF can provide the proposed \$20 million transfer without affecting the near-term fiscal condition of the fund. In addition, we believe the transfer should take the form of a loan, as is apparently the intent of the administration. The UTSF tax mechanism was intended to finance a specific telephone-related service, not to provide general tax revenue to the General Fund. In order to ensure that the transfer is a loan, we recommend that the Department of Finance report at budget hearings on the conditions governing the proposed UTSF transfer to the General Fund.



**WORKING CAPITAL ADVANCES, PRISON INDUSTRY
AUTHORITY—REVERSION**Item 9720-495 to the General
Fund

Budget p. GG 187

ANALYSIS AND RECOMMENDATIONS

We withhold recommendation on the proposed reversion, pending a report from the Prison Industry Authority (PIA) and the Department of Finance during budget hearings on (1) how PIA will finance its expansion activities if the reversion is approved, and (2) why any savings from industry expansion activities should be applied to reduce PIA's General Fund loan balance, rather than reduce its subsidy from the 1986 Prison Construction Fund.

The budget proposes to revert to the General Fund the unencumbered balance of funds provided to the Prison Industry Authority (PIA) as a loan pursuant to Ch 1413/85. Specifically, the measure provided a \$15.9 million General Fund loan to the PIA for expansion of new industry programs in new prisons. PIA advises that approximately \$12.1 million has already been expended. The Department of Finance indicates that the unexpended balance of \$3.8 million will not be needed because recent legislation—Ch 532/86 (AB 4356)—provided a direct appropriation of \$62 million from the 1986 Prison Construction Fund for the same purpose. This appropriation, however, was not a loan but a direct state subsidy to PIA.

We are concerned about the proposed reversion for several reasons. First, documentation provided by PIA shows that the \$62 million subsidy provided by Ch 532/86 and the \$15.9 million loan provided by Ch 1413/85 will, in fact, be needed in order for PIA to open industries in the new prisons and provide employment for inmates. PIA staff recently indicated that PIA may incur some savings, but no savings have been identified.

Second, if PIA does incur savings, we question whether the unneeded funds should be applied to reduce the \$15.9 million loan balance instead of the \$62 million subsidy. Both the loan and the subsidy were provided for expansion of industry programs, and any savings could be reverted to either the General Fund or the 1986 Prison Construction Fund. Although the loan will eventually be repaid to the General Fund with interest, there is no mechanism for PIA to repay the state for the subsidy.

Third, as we indicate in our analysis of the Department of Corrections' capital outlay budget (please see Item 5240-301), funds available in the 1986 Prison Construction Fund will be inadequate to fund construction of projects for the Departments of Corrections and the Youth Authority that have already been approved by the Legislature. Consequently, the Legislature may wish to reallocate any savings from PIA's expansion to cover anticipated costs of the construction program, such as contractor claims.

Because of these questions, we withhold recommendation on the proposed reversion, pending a report from the PIA and the Department of Finance during budget hearings on (1) how PIA will finance its expansion activities if the proposed reversion is approved, and (2) why any savings from industry expansion activities should be applied to reduce PIA's loan balance, rather than reduce the subsidy provided by Chapter 532.

AUGMENTATION FOR EMPLOYEE COMPENSATION: CIVIL SERVICE, EXEMPT AND STATUTORY EMPLOYEES

Item 9800 from the General Fund and various other funds

Budget p. GG 188

Requested 1987-88	\$109,476,000
Recommendation pending	109,476,000

1987-88 FUNDING BY ITEM AND SOURCE

Item—Description	Fund	Amount
9800-001-001—Compensation Increase	General	\$61,371,000
9800-001-494—Compensation Increase	Special	28,930,000
9800-001-988—Compensation Increase	Nongovernmental cost	19,175,000
Total		\$109,476,000

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. 1987-88 Compensation Increases. Withhold recommendation on \$109.5 million, pending review of memoranda of understanding and compensation proposals for nonrepresented state employees. 1413
2. Physical Fitness Pay. Recommend that the Departments of Finance and Personnel Administration report at budget hearings on their plans for physical fitness incentive pay in 1987-88. 1414
3. Budget Format. Recommend the adoption of Budget Bill schedules to provide more detailed information. 1415

OVERVIEW OF THE BUDGET REQUEST

The Governor's Budget proposes three appropriations totaling \$109.5 million for compensation increases for all state employees except those in higher education. The General Fund would provide \$61.4 million, or 56 percent, of the total. The amount appropriated in these items would provide: (1) \$84.2 million for a "general compensation increase" of up to 3 percent for state employees, *beginning January 1, 1988*; (2) \$18.9 million to cover projected premium rate increases in existing health and dental benefits for state employees; and (3) \$6.7 million to cover benefit rate increases for annuitants. (Please see our analysis of Item 9650 for a complete discussion of annuitants' costs.)

Funds appropriated in this item will be allocated for salary and benefit enhancements for *represented* employees based on the results of the collective bargaining process; consequently, the *actual* amounts allocated for the various components of these employees' compensation could vary from those proposed by the administration. Memoranda of understanding produced through the bargaining process will be submitted to the Legislature for approval of any changes agreed to between labor and management that involve the expenditure of funds. This item also covers the costs of compensation increase for *nonrepresented* employees (such as managerial, confidential and legislative employees).

The \$109.5 million proposal does *not* include compensation increases proposed for employees of the University of California, the California State University and Hastings College of the Law. The Governor's Budget for 1987-88 includes funds for these increases in the support budgets of the individual segments or colleges (please see our analysis of Items 6440, 6610 and 6600, respectively, for a description of the higher education employee compensation packages).

ANALYSIS AND RECOMMENDATIONS

A Review of the Current-Year Employee Compensation Program

Under the State Employer-Employee Relations Act (SEERA), the Legislature has the responsibility to approve all provisions of negotiated agreements (called memoranda of understanding or MOUs) which require either (1) the expenditure of funds or (2) a change in law, before the provisions of an MOU can be implemented. The Legislature passed four bills in 1985 (SB 578, AB 1252, SB 1203, and AB 1199) which approved the MOUs for the twenty employee bargaining units, thereby ratifying the changes agreed to between labor and management for 1985-86 and 1986-87. This was the first time the state and employer organizations negotiated two-year agreements.

The Legislature appropriated \$298.7 million from all funds (\$165.3 million from the General Fund) in the 1986 Budget Act to finance employee compensation increases in 1986-87. Because the MOUs covered a two-year period, this amount was appropriated in the individual *departmental* budgets, rather than allocated from this item as in past years. The major provisions funded by this amount are:

- A 5 percent salary increase effective July 1, 1986;
- Maintenance of health and dental benefits; and
- A new vision care benefit for represented employees effective July 1, 1986 (nonrepresented employees received this benefit effective February 1, 1986).

In some cases departments did not receive funding in 1986-87 for certain benefits (such as the cost of health premium increases) and had to absorb the costs of these benefits in their support budgets. To fund these "absorbable" costs, departments had to: (1) redirect funds from other activities; or (2) request additional support to fund either the absorbable provisions or activities from which the funds were redirected.

Employee Compensation Increases in 1987-88

We withhold recommendation on funds for employee compensation increases proposed in the Budget Bill, pending review of memoranda of understanding (MOUs) and compensation proposals for nonrepresented state employees.

Fiscal year 1987-88 will be the sixth year that state employee compensations increases will be subject to collective bargaining. Until the new or amended MOUs are submitted for the Legislature's consideration, together with the increases proposed by the administration for employees not covered by collective bargaining, we have no basis for evaluating (1) the nature or magnitude of increases proposed, or (2) the amount of funds required to implement these increases. Therefore, we withhold recommendation on this item, pending review of these proposals.

AUGMENTATION FOR EMPLOYEE COMPENSATION: CIVIL SERVICE, EXEMPT AND STATUTORY EMPLOYEES—Continued**Physical Fitness Incentive Pay**

We recommend that the Departments of Finance and Personnel Administration report at budget hearings on their plans for physical fitness incentive pay in 1987-88.

As a result of provisions in several 1985-87 collective bargaining agreements, certain classifications of state civil service employees are eligible for physical fitness incentive pay. In general, these provisions require the state to pay eligible employees—primarily public safety and peace officers—an additional \$65 per month for successfully completing a physical fitness test. In the case of one MOU (for Bargaining Unit 5, Highway Patrol), eligible *senior* officers who pass the test receive a total of \$130 per month in fitness pay. Subsequent to these bargaining agreements, the Department of Personnel Administration (DPA) decided to make fitness pay available to eligible managers and supervisors in the affected departments, in accordance with its policy of granting additional benefits to nonrepresented employees which are “comparable” to benefits for the rank and file.

Consequently, the state now is required to pay certain employees an additional \$780 or \$1,560 per year simply because they are physically able to perform the jobs for which they were hired. Those eligible employees who are not physically able to perform their jobs do not get the bonus; they do, however, receive their full salary.

Is Fitness Pay a Sound Idea? Last year, we expressed our concerns about budget requests for physical fitness incentive pay for the Departments of Corrections and the Youth Authority (please see the *1986-87 Analysis*, pages 1019-20 and 1072-73). During the budget hearings for these departments, the fiscal subcommittees expressed concerns as well about whether this type of compensation is reasonable. If this benefit is included in 1987-88 MOUs, the Legislature will have an opportunity to review the provision’s appropriateness when considering the legislation implementing the agreements. With regard to nonrepresented employees, the Legislature can take whatever action it feels is appropriate through this item.

Partial Funding in Budget Year. Our analysis also has identified a budgeting problem with regard to the physical fitness pay program. Specifically, the budget does not treat the various departments with eligible employees in the same manner. Table 2 shows those departments with the largest number of employees receiving fitness pay. It indicates that the budget does not include *any* funding in 1987-88 for this benefit in two departments (Corrections and Youth Authority). If this pay provision is included again in the next Bargaining Unit 6 agreement, the departments will face a combined deficiency of over \$4 million in the budget year (please see our discussion of this issue in Items 5240 and 5460 in this *Analysis*). The budget does propose, however, to fund fitness pay costs for other departments (such as Highway Patrol, Parks and Recreation, and Fish and Game) in 1987-88. In at least one case (the Department of Justice), the budget includes funding for the department’s eligible represented employees but *not* for nonrepresented employees.

There is no reason for the Department of Finance to treat departments differently in the funding of fitness pay costs. In addition, it is unclear to

us why the DPA needs to grant this same benefit to *nonrepresented* managers and supervisors. Ostensibly, physical fitness pay would seem to be a benefit appropriate only for the rank and file. In light of these concerns, we recommend that the Departments of Finance and Personnel Administration report at budget hearings on their plans for physical fitness incentive pay in 1987-88.

Table 2
Physical Fitness Incentive Pay
Major Departments Affected
1987-88
(dollars in thousands)

Department (By Bargaining Unit)	Number of Eligible Employees ^a			Estimated Cost (All Funds)		
	Rep- resented	Nonrep- resented	Total	Rep- resented	Nonrep- resented	Total
Unit 5:						
Highway Patrol	4,336	843	5,179	\$6,242	\$1,316	\$7,558
Unit 6:						
Corrections.....	3,839	1,439	5,278	2,995 ^b	1,122 ^b	4,117 ^b
Youth Authority	1,247	500	1,747	973 ^b	390 ^b	1,363 ^b
Unit 7:						
Fish and Game	372	45	417	290	35	325
General Services (State Police) ..	309	9	318	201	7	208
Justice	333	26	359	200	20 ^b	220
Parks and Recreation	423	212	635	330	165	495
Totals	10,860	3,074	13,933	\$11,231	\$3,055	\$14,286
Costs Funded in 1987-88 Governor's Budget				\$7,263	\$1,523	\$8,786
Unfunded Costs.....				3,968	1,532	5,500

^a Based on positions authorized for 1986-87.

^b Costs not funded in department's budget.

More Detail Needed in Budget Schedule

We recommend that the Legislature amend the Budget Bill to include more specific information in this item.

The Budget Bill currently lists only one program under each funding source in this item: the employee compensation program itself. This program, however, has several components, including compensation increases for represented and nonrepresented employees, and benefit rate increases for annuitants. As in past years, the Governor's Budget does not include separate information on the funding proposed for each of these individual components.

Our review of this item indicates that the lack of program detail hinders legislative understanding and review of the budget. In order to improve the information provided, we recommend that the Legislature amend the Budget Bill to include the following schedule:

9800-001-001—For augmentation for Employee Compensation	61,371,000
Schedule:	
(a) 10.01 Civil Service Employees—Represented	42,820,000
(b) 10.02 Civil Service Employees—Exempt and Excluded	8,687,000
(c) 20 Judicial and Statutory Employees	1,050,000

AUGMENTATION FOR EMPLOYEE COMPENSATION: CIVIL SERVICE, EXEMPT AND STATUTORY EMPLOYEES—Continued

(d) 30 Superior Court Judges	785,000
(e) 40 Legislative	1,295,000
(f) 50 Rate Increases for Retired Annuitants	6,734,000

Schedules similar to the above should be included for the special funds and nongovernmental cost funds allocations as well.

PAYMENT OF SPECIFIED ATTORNEY FEES

Item 9810 from the General
Fund and various funds

Budget p. GG 189

Requested 1987-88	\$975,000
Estimated 1986-87	—
Actual 1985-86	630,000
Requested increase \$975,000 (+100 percent)	
Total recommended increase	None

1987-88 FUNDING BY ITEM AND SOURCE

Item—Description	Fund	Amount
9810-001-001—Attorney fees	General	\$505,000
9810-001-494—Attorney fees	Special	150,000
9810-001-988—Attorney fees	Nongovernmental Cost	320,000
Total		\$975,000

GENERAL PROGRAM STATEMENT

This item provides funds for the payment of attorney fee claims, settlements, and judgments against the state arising from actions in either state or federal courts.

Generally, those court-awarded attorney fees which relate to a legal action that brings about the enforcement of an "important right" and results in a "significant benefit to the public" may be financed from this item.

The language in this item specifies that for claims related to actions arising in state courts (1) individual payments from the item shall not exceed a maximum hourly rate of \$90, and (2) a payment made from this item constitutes full satisfaction for the claim.

The budget proposes an appropriation of \$975,000 from various funds for payment of court-awarded attorney fees in 1987-88.

ANALYSIS AND RECOMMENDATION

We recommend approval.

Action on 1986 Budget Bill. The 1986 Budget Bill originally proposed expenditures of \$800,000 from this item for both state and federal court-awarded attorney fee claims. The measure's provisions for judgments arising in state courts restricted payments to (1) a maximum hourly rate of \$90 and (2) notwithstanding the hourly rate provision, a total of

\$100,000 for a single action. Other provisions declared legislative intent that federal courts should be guided in their award of attorney fee judgments by these same dollar limitations.

During hearings on the 1986 Budget Bill, the Legislature modified these provisions. These modifications removed both the \$100,000 cap for a single award, and all restrictions on awards made pursuant to federal law. In addition, the Legislature deleted the amounts provided for payment of attorney fees awarded by federal courts. Further revisions restricted hourly rate payments to the maximum hourly rate the state pays to private attorneys for performing services on behalf of the state. At the time, the Department of General Services indicated that these rates ranged from \$200 to \$300 per hour.

Subsequently, the Governor vetoed Item 9810 on the basis that the revisions did not provide a reasonable cap on hourly rates paid to attorneys who successfully sue the state. The Governor's veto message directed that attorney fee claims received in the current year should proceed through the Board of Control claims process for payment, and that these claims should be subject to the same dollar restrictions which were proposed originally in the 1986 Budget Bill.

Proposed Restoration of the Item. The 1987 Budget Bill proposes to restore the attorney fee item, and appropriates \$975,000 for both federal and state court awards. In addition, the bill contains provisions which limit to \$90 the maximum hourly rate payable for attorney fee judgments generated by a state court. No limit on the total payment for a single claim is proposed, and no restrictions are proposed for actions arising in federal court. The proposed appropriation of \$975,000 is \$345,000, or 55 percent, more than actual expenditures for this item in 1985-86. The Board of Control advises that as of January 1987, they had approved attorney fee claims in the current year totaling \$65,000. The board indicates that these claims will be submitted for legislative review in its semi-annual judgment bill.

Our analysis of the administration's proposal to restore the attorney fee budget item, along with the specified hourly rate control provisions, indicates that the proposal will provide a means for prompt and orderly payment of attorney fee claims, while providing for legislative oversight of the payment of court-awarded attorney fees. Accordingly, we recommend approval of this item.

RESERVE FOR CONTINGENCIES OR EMERGENCIES

Item 9840 from the General
Fund, special funds and non-
governmental cost funds

Budget p. GG 190

Requested 1987-88	\$4,500,000
Amount Appropriated by 1986 Budget Act	4,500,000
Total recommended reduction	None

1987-88 FUNDING BY ITEM AND SOURCE

Item—Description	Fund	Amount
9840-001-001—Reserve for contingencies or emergencies	General	\$1,500,000
9840-001-494—Reserve for contingencies or emergencies	Special	1,500,000
9840-001-988—Reserve for contingencies or emergencies	Nongovernmental Cost	1,500,000
9840-011-001—Reserve for contingencies or emergencies (Loans)	General	(2,500,000)
Total		\$4,500,000

ANALYSIS AND RECOMMENDATIONS*We recommend approval.*

The budget proposes three appropriations totaling \$4.5 million for allocation by the Department of Finance to state agencies in 1987-88. These funds may be allocated for expenses resulting from unforeseen contingencies and emergencies not covered by specific appropriations. The appropriations consist of \$1.5 million each from the General Fund, special funds and nongovernmental cost funds.

Item 9840-011-001 appropriates an additional \$2.5 million for temporary loans to state agencies whose operations are in danger of being curtailed because of a delay in the receipt of reimbursements or revenue. The loans made under this item must be repaid by the end of the fiscal year in which they are made.

The amounts requested for 1987-88 are the same as what was provided in the 1986 Budget Act.

General Fund Deficiencies

The amount appropriated for contingencies and emergencies in the Budget Act is not intended to cover all unforeseen needs that will arise during the fiscal year. In recent years, the Legislature has appropriated only a nominal amount in this item, primarily to cover minor emergencies that arise during the first part of the fiscal year. Most of the money needed to cover deficiency spending is provided by the annual deficiency bill, which appropriates funds in augmentation of this reserve item. Additional money to cover deficiency spending is authorized in: (1) individual departmental deficiency bills, (2) Budget Act language that allows agencies to spend more than the amount specifically appropriated by the Legislature, and (3) other authorizations for deficiencies, such as when funding is provided in the Budget Act for deficiencies incurred in a prior year.

A Disturbing Trend. Table 1 displays the amounts spent or

proposed for expenditure from the General Fund out of this item and other sources over the last 10 years. It shows that General Fund deficiencies have increased from \$32.3 million in 1978-79 to an estimated \$477.1 million in the current year, a 15-fold increase. In four of the last five years, deficiency expenditures have exceeded \$350 million.

In effect, about 40 percent of the original General Fund reserve estimate has been "wiped out" by subsequent deficiency expenditures during this period. As a result, in recent years the reserve has provided less protection against an economic downturn which could substantially reduce state revenues. Also, the Legislature's ability to establish spending priorities for the subsequent budget year has been restricted because these current year deficiencies have had "first call" on available resources.

Current Year Deficiencies. As shown in Table 1, we estimate that \$477 million will be needed from the General Fund to cover deficiencies in 1986-87. This amount consists of (1) the \$301 million proposed to be funded in the annual deficiency bill, (2) \$83 million from other General Fund sources reflected in the Governor's Budget, and (3) \$93 million in additional current year deficiencies not recognized by the Department of Finance.

Reserve for Contingencies and Emergencies. The major General Fund deficiency allocations from the reserve anticipated by the Department of Finance in the current year are:

Health and Welfare

- \$178.3 million to cover a shortfall in funding for Medi-Cal, including \$14.6 million to fund abortions, and
- \$37.2 million to fund the SSI/SSP program resulting from (1) a lower federal COLA offset and (2) higher caseload.

Corrections

- \$66.1 million to provide for a larger-than-anticipated inmate and parolee population.

Other Deficiencies Shown in Budget. Other parts of the budget also provide for deficiency payments. These will total \$83 million and consist of:

Health and Welfare

- \$78.2 million in increased expenditures by the Department of Social Services, to pay increased costs for AFDC due primarily to additional caseload.

Education (K-12)

- \$4.8 million to cover a shortfall in funding for special education. The budget estimates a \$12.9 million shortfall in the current year and proposes to fund it in 1987-88 by redirecting savings from school apportionment programs. Our estimate differs due to an \$8.1 million double-budgeting error contained in the budget.

Other Potential Deficiencies. We estimate that another \$93 million not recognized in the budget will probably be required to cover the following additional current year deficiencies:

Education (K-12)

- \$55.3 million to cover a shortfall in school desegregation funding. This represents the 1986-87 portion of a total two-year deficiency of \$98 million, and
- \$29.2 million to offset lower-than-anticipated federal child care reimbursements for the Greater Avenues for Independence (GAIN) pro-

RESERVE FOR CONTINGENCIES OR EMERGENCIES—Continued

gram. The Department of Education has sent notification of this deficiency to the Department of Finance, but it has not yet been approved. A similar deficiency may occur in 1987–88. Language in both the 1986 Budget Act and the proposed 1987 Budget Bill permits the Director of Finance to augment the appropriation in the event of a shortfall in federal reimbursements.

Various State Agencies

- \$8.2 million in additional deficiency notifications sent to the Department of Finance pursuant to Control Section 27 of the 1986 Budget Act which have not yet been approved.

Table 1
General Fund Deficiency Expenditures
1978–79 through 1987–88
(dollars in thousands)

	<i>Reserve for Contingencies or Emergencies</i>		<i>Actual Amount Allocated to Agencies</i>	<i>Individual Departmental Deficiency Bills</i>	<i>Other</i>	<i>Total Amount Allocated</i>
	<i>Amount Appropriated Budget Act</i>	<i>Deficiency Act</i>				
1978–79	\$1,500	\$11,000	\$12,193	\$20,082	—	\$32,275
1979–80	1,500	25,646	26,208	7,461	—	33,669
1980–81	1,500	18,600	19,005	39,799	\$121,935	180,739
1981–82	1,500	2,500	25,545	138,118	48	163,711
1982–83	1,500	431,500	332,101	2,318	47,477	381,896
1983–84	1,500	118,460	109,531	—	93,565	203,096
1984–85	1,500	423,850	417,017	2,200	10,000	429,217
1985–86	1,500	335,523	329,373	16,552	13,236	359,161
1986–87	1,500	300,873 ^a	300,873 ^b	410 ^a	175,787 ^c	477,070
1987–88	1,500 ^a	—	—	—	—	—

^a Proposed.

^b Total amount of 1986–87 allocations anticipated by the Department of Finance as of January 1987.

^c Legislative Analyst's Office.

Deficiencies in Special Funds and Nongovernmental Cost Funds

Tables 2 and 3 show deficiencies in special and nongovernmental cost funds, respectively, since 1978–79, the first year in which there was legislative control and oversight of these funds.

Table 2
Reserve for Contingencies or Emergencies
Appropriations and Allocations from Special Funds
1978–79 to 1987–88
(dollars in thousands)

	<i>Appropriated in Budget Act</i>	<i>Deficiency Appropriation</i>	<i>Allocated to Agencies</i>	<i>Unexpended Balances</i>
1978–79	\$1,500	—	\$254	\$1,246
1979–80	1,500	—	821	679
1980–81	1,500	\$1,000	1,859	641
1981–82	1,500	5,000	5,121	1,379
1982–83	1,500	4,500	3,115	2,885
1983–84	1,500	20,652	21,365	787

1984-85.....	1,500	22,303	21,049	1,254
1985-86.....	1,500	26,086	26,162	1,424
1986-87.....	1,500	4,682 ^a	4,682 ^b	1,500 ^a
1987-88.....	1,500 ^a	—	—	—

^a Proposed.

^b Total amount of 1986-87 allocations anticipated by the Department of Finance as of January 1987.

In 1986-87, special fund deficiency allocations are estimated at \$4.7 million, which is \$21.5 million less than the \$26.2 million allocated in 1985-86. The major special fund allocations proposed for 1986-87 are: (1) \$1.4 million from the Benefit Audit Fund to expand efforts to recover fraudulent Unemployment Insurance payments, and (2) \$760,000 from the Special Account for Capital Outlay (SAFCO) to pay a portion of the cost of relocating the California Conservation Corps' training academy.

Table 3
Reserve for Contingencies or Emergencies
Appropriations and Allocations from Nongovernmental Cost Funds
1978-79 to 1987-88
(dollars in thousands)

	<i>Appropriated in Budget Act</i>	<i>Deficiency Appropriation</i>	<i>Allocated to Agencies</i>	<i>Unexpended Balances</i>
1978-79.....	\$1,500	—	\$676	\$824
1979-80.....	1,500	\$5,300	6,271	528
1980-81.....	1,500	—	610	890
1981-82.....	1,500	—	279	1,221
1982-83.....	1,500	351,250	275,682	77,068
1983-84.....	1,500	3,639	3,639	1,500
1984-85.....	1,500	3,435	3,438	1,497
1985-86.....	1,500	4,540	3,887	2,153
1986-87.....	1,500	487 ^a	487 ^b	1,500 ^a
1987-88.....	1,500 ^a	—	—	—

^a Proposed.

^b Total amount of 1986-87 allocations anticipated by the Department of Finance as of January 1987.

The budget proposes \$487,000 in deficiency allocations from nongovernmental cost funds, which is \$3.4 million less than the \$3.8 million allocated in 1985-86. The major allocation is \$210,000 from the 1984 Prison Construction Fund to cover costs of reviewing construction permits.

RESERVE FOR CONTINGENCIES OR EMERGENCIES—REAPPROPRIATION

Item 9840-490 from the General Fund and various funds

Budget p. GG 190

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

This item reverts any unexpended balances from the appropriations made in the 1986 Budget Act to the Reserve for Contingencies or Emergencies (Items 9840-001-001, 9840-001-494, and 9840-001-988), to the unappropriated surplus of the General Fund, special funds, and nongovernmental cost funds, respectively, effective June 30, 1987.

The amounts reverted on June 30, 1987 are reappropriated by this item to the Reserve for Contingencies or Emergencies (Items 9840-001-001, 9840-001-494, and 9840-001-988), effective July 1, 1987. The reappropriated funds thus would be made available during the budget year for allocation by the Director of Finance to cover any additional costs associated with any 1986-87 deficiencies discovered after the fiscal year ends.

UNALLOCATED CAPITAL OUTLAY—PROJECT PLANNING

Item 9860-301-036 from the General Fund, Special Account for Capital Outlay

Budget p. GG 198

Requested 1987-88	\$300,000
Recommended approval	300,000

ANALYSIS AND RECOMMENDATIONS

Project Planning

We recommend approval of \$300,000 requested under Item 9860-301-036 for statewide project planning.

The budget provides \$300,000 to finance the development of cost estimates for new projects which the Department of Finance (DOF) anticipates will be included in the budget for 1988-89 and 1989-90. The request is \$100,000, or 50 percent, more than estimated 1986-87 expenditures for this purpose. These funds would be allocated by the Department of Finance.

Funds for statewide planning of new capital outlay proposals traditionally are included in the Budget Bill to ensure that the Legislature will have the information it needs when considering capital outlay requests for the following year.

The department indicates that recent changes in the administrative procedures of the state's capital outlay process will allow budget packages to be prepared several months earlier. Under the new procedures, departments are required to submit project proposals to DOF no later than March 2, one year in advance of the Governor's Budget. Previously, de-

partments submitted this information in June and subsequently received planning funds from DOF early in the fiscal year. The DOF anticipates allocating the proposed 1987-88 funds for the preparation of budget packages for the (1) 1988-89 Governor's Budget in the first two quarters of the budget year, and (2) 1989-90 Governor's Budget in the second two quarters of the budget year. This change in procedures should result in (1) an earlier submittal of detailed project cost information, and (2) a more even budget package workload schedule in the Office of State Architect and Office of Project Development and Management. For these reasons, we recommend approval.

UNALLOCATED CAPITAL OUTLAY—MATCHING FUNDS FOR ENERGY GRANTS

Item 9860-301-782 from the
Higher Education Capital
Outlay Bond Fund

Budget p. GG 198

Requested 1987-88	\$800,000
Recommended reduction	300,000

ANALYSIS AND RECOMMENDATIONS

We recommend a reduction of \$300,000 requested under Item 9860-301-782 for matching energy grants because of overbudgeting.

Further, we recommend that the budgeted funds be available for one year rather than two years.

The budget includes \$800,000 for working drawings and construction of energy conservation projects that are expected to be partially funded through federal grants for energy conservation. This amount is \$300,000 (60 percent) more than the \$500,000 included for this purpose in the 1986 Budget Act.

These funds would be allocated by the Department of Finance (DOF) for the highest priority projects identified by the University of California, the California State University, the California Maritime Academy, and the California Community Colleges. The DOF would be required to report proposed allocations to the Legislature at least 30 days prior to allocation of the funds. The funds would be available for allocation during the 1987-88 and 1988-89 fiscal years. This lump-sum appropriation would ensure that the state realizes the greatest return on its investment under the federal grant program by funding the highest-priority projects statewide.

Amount is Overbudgeted. According to the California Energy Commission staff, the federal government has historically allocated 25 percent of the total amount made available for projects in California to the state-funded higher education projects usually included under this item. The commission staff indicate that approximately \$2 million in federal funds will be available to finance projects in California during 1987-88. Thus, no more than \$500,000 in state funds should be necessary to match federal funding for projects on a 50-50 basis. Consequently, we recommend deletion of \$300,000 requested for this purpose.

UNALLOCATED CAPITAL OUTLAY—MATCHING FUNDS FOR ENERGY GRANTS—Continued

Funds Should Not be Available for Two Years. The Budget Bill specifies that these funds are available for allocation by DOF in 1987-88 and 1988-89.

It is not necessary to make these funds available for more than one fiscal year. If DOF does not authorize expenditures in the amount of \$500,000 for matching energy grants prior to the end of 1987-88, the balance would revert to the bond fund where it would be available for appropriation by the Legislature. Additional funding for this purpose in 1988-89 should be considered separately, in the course of deliberations on the 1988 Budget Bill.

Moreover, the commission indicates that any projects financed under this item will be approved and federal funds will be available early in the budget year. Thus, it will not be necessary for these funds to be available in 1988-89. Consequently, we recommend that the Budget Bill language be modified to indicate that the funds be available for the 1987-88 fiscal year only.
