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May 6, 2011

Hon. Kamala D. Harris
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Krystal Paris
Initiative Coordinator

Dear Attorney General Harris:

Pursuant to Elections Code Section 9005, we have reviewed the proposed constitutional and statutory amendment related to the budget process (A.G. File No. 11-0009).

BACKGROUND

The State Budget Process

An Annual Budget Process. The State Constitution gives the Legislature power to appropriate state funds and make midyear adjustments to those appropriations. The annual state budget act is the Legislature's primary method of authorizing expenses for a particular fiscal year. The Constitution requires that (1) the Governor propose a balanced budget by January 10 for the next fiscal year (beginning July 1) and (2) the Legislature pass the annual budget act by June 15. The Governor may then either sign or veto the budget bill. The Governor may also reduce or eliminate specific appropriations items using his or her "line-item veto" power. The Legislature may override a veto with a two-thirds vote in each house. Once the budget has been approved by the Legislature and the Governor, the Governor has only limited authority to reduce spending during the year without legislative approval.

Balanced Budget. In March 2004, the state's voters passed Proposition 58. Among other changes, the measure requires that the Legislature pass a balanced budget each year. This means that the projected financial resources for the year must equal or exceed projected spending.

Fiscal Emergencies. Proposition 58 also allows the Governor to declare a fiscal emergency if he or she determines after the budget has been enacted that the state is facing substantial revenue shortfalls or spending overruns. In such cases, the Governor must propose legislation to address the fiscal emergency, and call the Legislature into special session. If the Legislature fails to pass and send to the Governor legislation to address the budget problem within 45 days, it is prohibited from (1) acting on any other bills or (2) adjourning until such legislation is passed.

Requirements for Budget and Infrastructure Planning. State law provides that state departments should develop budgets that define their programs' objectives and budget for those objectives each year. The Governor is required to submit to the Legislature a five-year infrastructure plan each year.

The Appropriations Process

Outside of the annual state budget, the Legislature can also create new state programs that cost money or reduce tax levels by passing a new law. Any new law that costs money is typically referred to a committee in each house of the Legislature called the Appropriations Committee. These committees assess the likely cost of the legislation and decide whether to recommend the passage of the legislation by each house. There is currently no firm requirement in the Constitution to show how such a program will be funded. A new law created through this process will generally require funding in subsequent state budgets.

PROPOSAL

Changes Budget to a Two-Year Process

Governor Would Submit a Budget Every Odd Numbered Year. Under this measure, in each odd numbered calendar year the Governor would submit a budget for the two subsequent fiscal years. For example, in January 2013 the Governor would submit a budget for the fiscal year beginning in July 2013 and for the fiscal year beginning in July 2014. In even numbered years, the Governor could submit an update for either of the two years covered by the previous submission. The measure does not change the requirement that a balanced budget is in place by the beginning of each fiscal year.

Changes Date for Passage of Budget by Legislature. Under this measure, the date by which time the Legislature is required to pass a budget is changed from June 15 to June 25.

Requires an Additional Update on Projections of State Budget. Currently the administration is only required to submit updated projections of the state revenue and expenditures twice a year (once in January and again in May). Under this measure, the administration would be required to submit additional updates each year.

Governor Given Power to Reduce Spending and Other Budget Duties

New Expenditure Reduction Authority for the Governor. The proposed measure provides that if the Legislature has not sent bills to the Governor addressing a fiscal emergency by the 45th day following the issuance of the fiscal emergency proclamation, the Governor may reduce or eliminate any existing appropriation contained in the budget act for that fiscal year that is not otherwise required by the Constitution or federal law. The total amount reduced cannot exceed the amount necessary to balance the budget. The Legislature may override all or part of the reductions by a two-thirds vote of each house.

Additional Information Required in Governor's Budget Proposals. Under this measure, the Governor would have to submit performance standards for state agencies and programs, and state projections of anticipated expenditures and revenues for the next five fiscal years. The

Governor's recommendations for expenditure reductions or additional revenues would have to include an estimate of the "long-term impact" the proposals would have on the California economy.

Requirements to Identify Funds to Pay for Program Expansions

The proposed measure contains several provisions to constrain the state's ability to create or expand state programs—particularly those that would result in a net increase in state costs or net decrease in state revenues of more than $25 million. Lawmakers would have to identify additional revenues or reductions in existing expenditures to cover any such net change in state costs or revenues.

Performance Standards for State Programs

This measure amends the Constitution to require the Legislature to establish a process to review the performance of state programs at least once every ten years. State departments would be required to develop and maintain data that track the outcomes of their programs and propose law changes to improve those outcomes.

FISCAL EFFECT

This measure likely would result in various fiscal effects for the state (additional spending and/or savings).

Additional Spending. New state spending would likely be needed to develop and use new performance standards, analyze the fiscal implication of legislation, and implement other budget process requirements resulting from the measure. In particular, new information technology expenditures could result to address these new requirements. These costs could total in the tens of millions of dollars annually.

Other Fiscal Effects of This Measure. There may be more significant fiscal effects than those described above that are impossible to estimate precisely. This measure makes significant changes to the way the state budgets its funds, considers legislation, and monitors the outcomes of its programs. These changes may result in a number of fiscal effects for the state and local governments affected by state budgetary decisions, including:

- ***Giving the Governor Midyear Authority to Reduce Spending.*** In some years, this measure would allow the Governor to reduce spending below the level that might result under existing constitutional provisions. This could result in some programs' share of total spending rising and others falling.

- ***Requiring Identification of Funding for Additional State Costs.*** This measure could make creating or significantly expanding programs more difficult because it requires identification of funding sources for some such efforts. This could result in less state and local spending on ongoing programs in future years.
- ***Requiring New Efforts to Maintain Program Outcomes.*** The measure's requirements for new data concerning program outcomes could result in different spending decisions by future Legislatures. These requirements could result in greater or less state spending on particular programs.

SUMMARY OF FISCAL EFFECT

This measure would have the following major fiscal effects:

- Increases in state spending—potentially tens of millions of dollars per year—to administer new budgeting process requirements.
- Potentially significant, but unknown, fiscal effects for the state and local governments affected by state budgetary decisions.

Sincerely,

Mac Taylor
Legislative Analyst

Ana J. Matosantos
Director of Finance