

THE GOVERNOR'S BUDGET FOR 1984-85

MARCH 7, 1984

LEGISLATIVE ANALYST

STATE OF CALIFORNIA

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STATEMENT BY THE LEGISLATIVE ANALYST TO
THE ASSEMBLY COMMITTEE ON WAYS AND MEANS

MR. CHAIRMAN AND MEMBERS:

FOR THE FIRST TIME IN THREE YEARS, THE LEGISLATURE'S CHOICES IN PUTTING A BUDGET TOGETHER FOR CALIFORNIA WILL NOT BE CONFINED TO EITHER RAISING TAXES OR CUTTING SERVICES. THE ECONOMIC RECOVERY HAS BROADENED YOUR FISCAL OPTIONS CONSIDERABLY. AT THE SAME TIME, HOWEVER, I AM MINDFUL -- AND I KNOW YOU ARE -- THAT THREE SUCCESSIVE YEARS OF BUDGET REDUCTIONS HAVE CREATED PENT-UP DEMANDS FOR CATCH-UP INCREASES. THUS, EVEN THOUGH YOU WILL HAVE MORE RESOURCES TO WORK WITH IN PREPARING A BUDGET FOR 1984-85, YOUR TASK IN ALLOCATING THOSE RESOURCES WILL, BY NO MEANS, BE EASY.

THE PURPOSE OF MY REMARKS THIS MORNING IS TWOFOLD. FIRST, I WANT TO PUT THE GOVERNOR'S BUDGET FOR 1984-85 IN PERSPECTIVE. IN DOING SO, I WILL NOT TRY TO TELL YOU WHAT'S IN THE BUDGET; YOU ALREADY KNOW THAT. RATHER, I WILL GIVE YOU OUR ASSESSMENT OF WHAT THE BUDGET MEANS IN TERMS OF SERVICE LEVELS WITHIN VARIOUS PROGRAM AREAS. SECOND, I WANT TO IDENTIFY AND COMMENT ON SOME OF THE KEY FISCAL ISSUES THAT YOU WILL FACE IN ACTING ON THE GOVERNOR'S BUDGET.

I. THE BUDGET IN PERSPECTIVE

TABLE 1 SHOWS THE LEVEL OF GENERAL FUND REVENUES AND EXPENDITURES FOR THE CURRENT AND BUDGET YEARS AS THEY APPEAR IN THE BUDGET DOCUMENT. IT ALSO SHOWS THE REVENUE AND EXPENDITURE ESTIMATES FOR THE CURRENT YEAR, BASED ON LAST YEAR'S BUDGET DOCUMENT.

Table 1
 Condition of the General Fund
 1983-84 and 1984-85
 (in millions)^a

	1983-84		1984-85 Proposed
	Original Estimate	Current Estimate	
Beginning Balance	-\$1,628 ^b	-\$521	\$205
Revenues and Transfers	22,479	23,368	25,826
Expenditures	<u>21,677</u>	<u>22,641</u>	<u>25,076</u>
Ending Balance	-\$826	\$205	\$954
Reserves (-)	<u>-253</u>	<u>-105</u>	<u>-4</u>
Unrestricted Balance, End-Of-Year	-\$1,079	\$100	\$951

- a. Source: Governor's Budgets for 1983-84 and 1984-85. Details may not add to total due to rounding.
- b. Budget estimate adjusted to reflect (1) unfunded 1982-83 deficit of \$1,458 million acknowledged in 1983-84 Governor's Budget and (2) impact of court decision in Valdez v. Cory.

THE TABLE ILLUSTRATES HOW DRAMATICALLY THE OUTLOOK FOR THE STATE'S GENERAL FUND HAS CHANGED IN JUST 12 MONTHS. INSTEAD OF A \$1.6 BILLION DEFICIT (THE ESTIMATE FOR JUNE 30, 1983), THE GOVERNOR'S BUDGET SHOWS NEARLY A \$1 BILLION SURPLUS (THE ESTIMATE FOR JUNE 30, 1985).

BEFORE DISCUSSING THE BUDGET'S PROJECTIONS FOR REVENUES AND EXPENDITURES IN 1984-85, LET ME BRIEFLY EXPLAIN WHY THE STATE'S FISCAL OUTLOOK HAS IMPROVED SO MARKEDLY.

A. WHY THE FISCAL OUTLOOK HAS TURNED AROUND

TABLE 2 SHOWS THE FACTORS RESPONSIBLE FOR THE \$1.2 BILLION IMPROVEMENT IN THE GENERAL FUND CONDITION PROJECTED FOR JUNE 30, 1984.

Table 2
 Factors Responsible For Improvement in Projected
 General Fund Condition as of June 30, 1984
 (in millions)

June 30, 1984 Balance, as Projected in January 1983		-\$1,079
Changes Due To:		
<u>Legislative Action</u>		
AB 28x	+\$610	
Other Legislative Actions to Increase Revenues	<u>+395</u>	
Subtotal, Legislative Action	+\$1,005	
<u>Increased Revenues Attributable to the Economic Recovery:</u>		
1982-83	\$338	
1983-84	<u>494</u>	
Subtotal, Economic Recovery	+\$832	
<u>Other Factors:</u>		
Expenditure Shortfall in 1982-83	\$+122	
Other	<u>+185</u>	
Subtotal, Other Factors	+\$307	
<u>Legislative and Gubernatorial Action on 1983-84 Expenditures (Net)</u>	-\$964	
Total, All Changes		<u>\$1,179</u>
June 30, 1984 Balance, as Projected in January 1984 ^a		+\$100

a. Details may not add to total due to rounding.

AS THE TABLE INDICATES, TWO FACTORS ARE PRIMARILY RESPONSIBLE FOR THE IMPROVEMENT:

- o FIRST, ACTION TAKEN BY THE LEGISLATURE TO INCREASE REVENUES AND REDUCE EXPENDITURES HAS RESULTED IN A GAIN TO THE GENERAL FUND OF ABOUT \$1 BILLION.
- o SECOND, A STRONGER-THAN-EXPECTED PERFORMANCE BY THE STATE'S ECONOMY HAS RESULTED IN ADDITIONAL REVENUES OF \$832 MILLION FOR 1982-83 AND 1983-84.

TOGETHER, THESE AND OTHER FACTORS HAVE ADDED \$2.1 BILLION TO THE GENERAL FUND, PERMITTING AN INCREASE IN EXPENDITURES OF \$964 MILLION ABOVE THE LEVEL PROPOSED IN THE GOVERNOR'S BUDGET FOR 1983-84.

B. THE OUTLOOK FOR GENERAL FUND REVENUES IN 1984-85

THE OUTLOOK FOR GENERAL FUND REVENUES IN 1984-85 IS EXTREMELY POSITIVE. THE GOVERNOR'S BUDGET PROJECTS THAT REVENUES WILL REACH NEARLY \$26 BILLION NEXT YEAR -- AN INCREASE OF \$2.5 BILLION OVER THE CURRENT-YEAR LEVEL. IN TERMS OF PURCHASING POWER, THIS REPRESENTS AN INCREASE OF 4 PERCENT OVER WHAT WILL BE COLLECTED IN 1983-84.

MY COLLEAGUES AND I SHARE THE ADMINISTRATION'S OPTIMISM REGARDING THE NEAR-TERM REVENUE OUTLOOK. IN FACT, IF THE ECONOMIC RECOVERY CONTINUES THROUGHOUT 1984-85 AS THE DEPARTMENT OF FINANCE ASSUMES, WE ESTIMATE THAT REVENUES FOR THE CURRENT AND BUDGET YEARS, COMBINED, WILL BE ABOUT \$70 MILLION ABOVE THE DEPARTMENT'S ESTIMATE.

WHAT DO THESE REVENUE PROJECTIONS MEAN FOR THE EXPENDITURE SIDE OF THE BUDGET? THEY IMPLY THAT SUFFICIENT FUNDS WILL BE AVAILABLE TO THE LEGISLATURE IN 1984-85 (1) TO MAINTAIN THE EXISTING LEVEL OF SERVICE IN

EACH PROGRAM AREA, (2) TO FULLY FUND THE INCREASES CALLED FOR BY SB 813, AND (3) STILL LEAVE MONEY AVAILABLE FOR INITIATING NEW PROGRAMS, ENHANCING EXISTING PROGRAMS, CREATING A "RAINY DAY" FUND, OR PROVIDING FURTHER TAX RELIEF. WE ESTIMATE THAT THE AMOUNT LEFT OVER AFTER PROVIDING FOR CURRENT SERVICES AND SB 813 WOULD BE ABOUT \$1.2 BILLION.

LET ME NOW TURN TO THE GOVERNOR'S PROPOSALS FOR UTILIZING THE NEARLY \$26 BILLION IN REVENUES THAT ARE EXPECTED TO BE AVAILABLE IN THE BUDGET YEAR.

C. THE OUTLOOK FOR GENERAL FUND EXPENDITURES IN 1984-85

THE GOVERNOR PROPOSES TO SPEND \$25.1 BILLION FROM THE GENERAL FUND IN 1984-85. THIS IS AN INCREASE OF 10.8 PERCENT, OR \$2.4 BILLION, ABOVE THE CURRENT-YEAR LEVEL. IN REAL TERMS (THAT IS, EXPENDITURES ADJUSTED TO RECOGNIZE THE EFFECTS OF INFLATION ON PURCHASING POWER), THE INCREASE AMOUNTS TO 4.2 PERCENT.

THE INCREASE IN INFLATION-ADJUSTED EXPENDITURES PROPOSED BY THE GOVERNOR WOULD BE THE FIRST SUCH INCREASE SINCE 1980-81, AND WOULD FOLLOW THREE CONSECUTIVE YEARS OF REDUCTIONS. THESE REDUCTIONS HAVE BROUGHT EXPENDITURES IN THE CURRENT YEAR TO A LEVEL THAT, IN TERMS OF PURCHASING POWER, IS ABOUT 12 PERCENT LESS THAN WHAT THE STATE SPENT IN 1980-81.

ANOTHER WAY OF PUTTING THE PROPOSED LEVEL OF GENERAL FUND EXPENDITURES IN PERSPECTIVE IS TO DISREGARD THE AMOUNT EARMARKED FOR LOCAL GOVERNMENT FISCAL RELIEF UNDER AB 8 AND COMPARE THE ADJUSTED BALANCE WITH WHAT THE STATE SPENT IN PRIOR YEARS. WHEN THIS IS DONE, WE FIND THAT THE LEVEL OF INFLATION-ADJUSTED EXPENDITURES PROPOSED FOR 1984-85 IS SLIGHTLY ABOVE WHAT IT WAS UNDER GOVERNOR REAGAN'S LAST BUDGET (1974-75). IN CONTRAST, THERE ARE 20 PERCENT MORE CALIFORNIANS NOW THAN THERE WERE THEN.

LET ME MAKE TWO OBSERVATIONS ABOUT THE 10.8 PERCENT INCREASE PROPOSED IN THE GOVERNOR'S BUDGET. FIRST, THE ONGOING INCREASE IS SIGNIFICANTLY LESS THAN 10.8 PERCENT. THIS IS BECAUSE ABOUT \$400 MILLION OF THE \$2.4 BILLION INCREASE IS ONE-TIME IN NATURE. THIS AMOUNT CONSISTS OF THE CATCH-UP STRS INCREASE (\$211 MILLION) AND THE REPAYMENT OF THE LOS ANGELES COUNTY LOAN (\$200 MILLION).

SECOND, THERE ARE A LOT OF PROGRAM MANAGERS AND AGENCY HEADS OUT THERE WHO CANNOT RELATE TO THE 10.8 PERCENT INCREASE IN EXPENDITURES THAT I ATTRIBUTE TO THE GOVERNOR'S BUDGET FOR 1984-85. THIS IS BECAUSE THE 10.8 PERCENT FIGURE IS MERELY AN AVERAGE OF INDIVIDUAL PROGRAM CHANGES, SOME OF WHICH ARE SUBSTANTIALLY ABOVE OR BELOW THE AVERAGE INCREASE. TABLE 3 ILLUSTRATES THIS UNUSUALLY LARGE VARIATION IN THE RATE AT WHICH DIFFERENT PROGRAMS ARE PROPOSED TO GROW.

Table 3

Proposed 1984-85 General Fund Expenditures,
By Major Category^a
(dollars in millions)

	<u>Amount</u>	<u>Share of Total</u>	<u>Change from 1983-84</u>	
			<u>Amount</u>	<u>Percent</u>
1. Health and Welfare ^b				
Medi-Cal	\$2,042	8.1%	\$23	1.2%
County Health	854	3.4	8	0.9
SSI/SSP	1,101	4.4	4	0.3
AFDC Grants	1,563	6.2	71	4.8
Repayment of L.A. County Loan	200	0.8	200	d
All Other	<u>1,997</u>	<u>8.0</u>	<u>150</u>	<u>8.1</u>
Subtotal, Health and Welfare	\$7,757	30.9%	\$456	6.2%
2. Education				
K-12	\$9,065	36.2%	\$827	10.0%
STRS Contribution	536	2.1	516	d
University of California California State University	1,447	5.8	337	30.3
Community Colleges ^c	1,149	4.6	201	21.2
All Other	<u>1,030</u>	<u>4.1</u>	<u>9</u>	<u>0.9</u>
Subtotal, Education	\$13,334	53.2%	\$1,902	16.6%
3. Other				
Youth and Adult Correctional Agency	\$963	3.8%	\$119	14.1%
Resources	325	1.3	36	12.5
All Other	2,698	10.8	-77	-2.7
Subtotal, Other	<u>\$3,986</u>	<u>15.9%</u>	<u>\$78</u>	<u>2.0%</u>
Totals	\$25,076	100.0%	\$2,435	10.8%

- a. Based on amounts shown in Governor's Budget. Details may not add to totals due to rounding.
- b. Includes the Secretary for Health and Welfare, and the Office of Economic Opportunity. Does not include the Child Development Programs Advisory Committee.
- c. Does not reflect the enactment of AB 1xx (Ch 1xx/84) or AB 470 (Ch 3/84).
- d. Percentage change equals or exceeds 100 percent.

AS THE TABLE SHOWS, EXPENDITURES FOR EDUCATION WOULD INCREASE BY 16.6 PERCENT UNDER THE GOVERNOR'S BUDGET, WHILE SPENDING ON CORRECTIONAL PROGRAMS WOULD INCREASE BY MORE THAN 14 PERCENT.

OBVIOUSLY, IF PROGRAMS ACCOUNTING FOR MORE THAN ONE-HALF OF TOTAL GENERAL FUND EXPENDITURES ARE BUDGETED TO INCREASE BY ABOUT 16.5 PERCENT, AND IF THE OVERALL INCREASE IN EXPENDITURES IS 10.8 PERCENT, SIMPLE ARITHMETIC TELLS US THAT OTHER MAJOR COMPONENTS OF THE BUDGET MUST SHOW LITTLE OR NO GROWTH. IN FACT, THE INCREASES PROPOSED FOR THREE PROGRAMS THAT ACCOUNT FOR NEARLY ONE-FIFTH OF ALL GENERAL FUND EXPENDITURES IN 1983-84 TEND TO BALANCE OFF THE INCREASES PROPOSED FOR EDUCATION AND CORRECTIONS. THESE THREE PROGRAMS -- MEDI-CAL, COUNTY HEALTH SERVICES, AND SSI/SSP -- ARE SLATED TO RISE BY LESS THAN 1 PERCENT IN THE BUDGET YEAR.

HOW DOES THE BUDGET STACK-UP AGAINST CURRENT SERVICE REQUIREMENTS? (BY "CURRENT" SERVICE REQUIREMENTS, I MEAN THE AMOUNT NEEDED TO CONTINUE THIS YEAR'S LEVEL OF SERVICES IN THE BUDGET YEAR AND FULLY FUND EXISTING LAW.) IN TOTAL, THE GOVERNOR'S BUDGET WOULD BUY MORE SERVICES IN 1984-85 THAN THE CURRENT-YEAR LEVEL. IN SOME INDIVIDUAL AREAS, HOWEVER, SUCH AS HEALTH AND WELFARE, THE LEVEL OF SERVICES WOULD DECLINE RELATIVE TO WHAT CURRENT LAW REQUIRES. SURPRISINGLY ENOUGH, THE AMOUNT OF FUNDING PROPOSED FOR K-12 EDUCATION IS ALSO LESS THAN CURRENT LAW/CURRENT SERVICES REQUIREMENTS. WHEN WE ADJUST THE EXPENDITURE FIGURES IN THE BUDGET TO ELIMINATE THE DISTORTING EFFECTS OF FUNDING SHIFTS PROPOSED BY THE GOVERNOR, WE FIND THAT THE AMOUNT REQUESTED FOR K-12 EDUCATION IS \$240 MILLION LESS THAN WHAT IS REQUIRED TO MAINTAIN CURRENT SERVICES AND FULLY FUND CURRENT LAW (SB 813).

THUS, THE BUDGET IS, INDEED, AN EXPRESSION OF THE ADMINISTRATION'S PRIORITIES. IN SOME PROGRAM AREAS, IT PROVIDES INCREASES ABOVE CURRENT SERVICE REQUIREMENTS TOTALING \$860 MILLION. IN OTHER AREAS, IT LIMITS SPENDING TO LEVELS THAT, IN TOTAL, ARE \$600 MILLION BELOW CURRENT SERVICE REQUIREMENTS.

I NOTED A FEW MOMENTS AGO THAT PROJECTED REVENUES AND CARRY-OVER RESERVES EXCEED CURRENT SERVICE/CURRENT LAW REQUIREMENTS BY ABOUT \$1.2 BILLION. THE GOVERNOR'S SPENDING PLAN DOES NOT COMMIT THE FULL AMOUNT OF THESE REVENUES TO INDIVIDUAL PROGRAMS. INSTEAD, THE GOVERNOR PROPOSES TO SET ASIDE \$950 MILLION IN THE RESERVE FOR ECONOMIC UNCERTAINTIES. THIS AMOUNT IS EQUAL TO ABOUT 3.8 PERCENT OF GENERAL FUND EXPENDITURES.

I THINK THE GOVERNOR'S PROPOSAL TO HOLD BACK THIS AMOUNT AS A FORM OF INSURANCE AGAINST REVENUE SHORTFALLS AND UNANTICIPATED EXPENDITURES MAKES SENSE. I WILL HAVE MORE TO SAY ABOUT THIS ASPECT OF THE BUDGET LATER IN MY TESTIMONY.

D. THE SIZE OF THE STATE'S WORKFORCE

BEFORE I TURN TO SPECIFIC FEATURES OF THE BUDGET AND THE MAJOR ISSUES FACING THE LEGISLATURE IN 1984-85, LET ME MAKE A FEW COMMENTS ABOUT ANOTHER BROAD DIMENSION OF THE BUDGET -- THE LEVEL OF STAFFING PROPOSED BY THE GOVERNOR.

THE NUMBER OF STATE EMPLOYEES NEEDED TO DELIVER PUBLIC SERVICES DEPENDS PRIMARILY ON TWO FACTORS: THE WORKLOAD ASSOCIATED WITH THE DELIVERY OF THOSE SERVICES AND STAFF PRODUCTIVITY. AS I NOTED EARLIER, THE GOVERNOR PROPOSES TO INCREASE BY ABOUT 4 PERCENT THE LEVEL OF GOODS AND SERVICES FINANCED BY THE STATE IN THE BUDGET YEAR. NORMALLY, MORE

PERSONNEL-YEARS WOULD BE REQUIRED TO PROVIDE THESE ADDITIONAL GOODS AND SERVICES. THE BUDGET, HOWEVER, PROPOSES TO REDUCE THE NUMBER OF PERSONNEL-YEARS BY 4,880, RELATIVE TO THE CURRENT-YEAR LEVEL. ACCORDING TO THE BUDGET, THIS REDUCTION WAS MADE POSSIBLE BY "INCREASED EFFICIENCIES."

NATURALLY, WE APPLAUD THE GOVERNOR'S EFFORTS TO INCREASE THE EFFICIENCY OF THE STATE'S WORKFORCE. I MUST TELL YOU, HOWEVER, THAT THE REDUCTION IN PERSONNEL-YEARS FOR WHICH THE ADMINISTRATION SHOULD BE GIVEN CREDIT IS CONSIDERABLY LESS THAN 4,880. MOREOVER, WE FIND THAT MOST OF THE REDUCTIONS IN PERSONNEL-YEARS PROPOSED FOR 1984-85 ARE DUE TO FACTORS OTHER THAN INCREASED EFFICIENCIES.

WE DISCUSS THIS MATTER AT SOME LENGTH IN OUR ANALYSIS OF THE PROPOSAL (PERSPECTIVES AND ISSUES, PAGE 152). OUR FINDINGS CAN BE SUMMARIZED AS FOLLOWS:

- o FIRST, THE NUMBER OF STATE PERSONNEL-YEARS IN THE CURRENT YEAR, AS ESTIMATED BY THE ADMINISTRATION, IS NEARLY 6,000 ABOVE THE ACTUAL NUMBER OF STATE PERSONNEL-YEARS IN 1982-83.
 - THIS IS THE LARGEST INCREASE IN STAFFING FOR ANY YEAR SINCE PROPOSITION 13 WAS APPROVED BY THE VOTERS.
 - IT ALSO REFLECTS THE FACT THAT SINCE THE 1983 BUDGET ACT WAS CHAPTERED, THE ADMINISTRATION HAS ESTABLISHED 2,200 POSITIONS ADMINISTRATIVELY.
- o SECOND, A LARGE PORTION OF THE REDUCTION IN PERSONNEL-YEARS SHOWN IN THE BUDGET FOR 1984-85 DO NOT REFLECT ACTIONS TAKEN BY THE ADMINISTRATION, AND INSTEAD CAN BE ATTRIBUTED TO:

--THE AUTOMATIC ELIMINATION OF SOME POSITIONS ESTABLISHED ADMINISTRATIVELY IN THE CURRENT YEAR.

--THE TERMINATION OF LIMITED-TERM POSITIONS THAT, PURSUANT TO PRIOR LEGISLATIVE ACTION, WILL EXPIRE AUTOMATICALLY BY JUNE 30, 1984.

--THE ASSUMPTION THAT AUTHORIZED POSITIONS WILL BE VACANT FOR LONGER PERIODS IN THE BUDGET YEAR THAN THEY WERE IN THE CURRENT YEAR ("SALARY SAVINGS").

o THIRD, ANOTHER LARGE PORTION OF THE REDUCTIONS IN PERSONNEL-YEARS CAN BE ATTRIBUTED TO FACTORS THAT, IN OUR JUDGEMENT, HAVE LITTLE TO DO WITH "INCREASED EFFICIENCIES." THESE FACTORS INCLUDE:

--REDUCED WORKLOAD--FOR EXAMPLE, THE DECLINE IN UNEMPLOYMENT INSURANCE CLAIMS (864 PERSONNEL-YEARS).

--FEDERAL LAW CHANGES--FOR EXAMPLE, THE TERMINATION OF THE CETA PROGRAM (56 PERSONNEL-YEARS).

--CHANGES IN ACCOUNTING PROCEDURES--FOR EXAMPLE, MOVING THE PRISON INDUSTRIES AUTHORITY "OFF BUDGET" (327 PERSONNEL-YEARS).

o FINALLY, A LITTLE LESS THAN ONE-FOURTH OF THE CUTS SHOW UP IN THE UNIVERSITY OF CALIFORNIA'S BUDGET, WHERE THE STATE DOES NOT EXERCISE ANY POSITION CONTROL. THUS, THE SAVINGS REPORTED FOR THE UNIVERSITY MAY BE MORE A HOPE THAN A CERTAINTY.

IN SHORT, WE DO NOT FIND THE BUDGET'S ESTIMATE OF STAFF SAVINGS RESULTING FROM "INCREASED EFFICIENCIES" TO BE DEFENSIBLE.

E. THEMES IN THE GOVERNOR'S BUDGET

OUR PROGRAM-BY-PROGRAM ANALYSIS OF THE GOVERNOR'S BUDGET IS FAR TOO EXTENSIVE FOR ME TO SUMMARIZE HERE. LET ME, INSTEAD, JUST MENTION SEVERAL OF WHAT WE PERCEIVE TO BE THE PRINCIPAL THEMES IN THE GOVERNOR'S BUDGET.

1. "CATCH-UP." IN A NUMBER OF AREAS, THE BUDGET PROPOSES INCREASES IN FUNDING OVER CURRENT-YEAR LEVELS TO COMPENSATE FOR RECENT CUTS IN EFFECTIVE SERVICE LEVELS. SPECIFICALLY, "CATCH-UP" INCREASES ARE PROPOSED FOR:

- STATE EMPLOYEE SALARIES
- FACULTY SALARIES
- CAL GRANT AWARD LEVELS
- INSTRUCTIONAL EQUIPMENT
- BUILDING MAINTENANCE
- HIGHWAY PLANNING AND CONSTRUCTION
- LOCAL MENTAL HEALTH PROGRAMS
- STATE HOSPITAL EQUIPMENT

FOR THE MOST PART, OUR ANALYSIS FINDS THAT THESE INCREASES ARE WARRANTED, ALTHOUGH IN SOME INSTANCES WE HAVE WITHHELD RECOMMENDATION ON THE EXACT AMOUNT OF THE INCREASE PENDING THE RECEIPT OF MORE INFORMATION.

2. INVESTMENT. THE BUDGET PROPOSES TO INCREASE SPENDING FOR CAPITAL OUTLAY, EQUIPMENT, INFORMATION PROCESSING TECHNOLOGY, TELECOMMUNICATIONS, AND OTHER ITEMS THAT WOULD IMPROVE THE STATE'S ABILITY TO DELIVER SERVICES IN A COST-EFFECTIVE MANNER. OUR ANALYSIS INDICATES THAT MOST OF THESE INCREASES MAKE SENSE, ALTHOUGH AGAIN WE HAVE FOUND IT NECESSARY TO WITHHOLD RECOMMENDATION IN THOSE CASES WHERE SUFFICIENT DETAILS ON THE PROPOSED LEVEL OF EXPENDITURES ARE LACKING.

3. CUTBACKS. IN SEVERAL AREAS, THE BUDGET PROPOSES TO CONTINUE CUTS IN SERVICE LEVELS INITIATED BY THE GOVERNOR IN THE CURRENT FISCAL YEAR. THE THREE AGENCIES THAT ARE MOST REPRESENTATIVE OF THIS THEME ARE THE DEPARTMENT OF INDUSTRIAL RELATIONS, THE AGRICULTURAL LABOR RELATIONS BOARD, AND THE COASTAL COMMISSION. IN EACH OF THESE CASES, OUR ANALYSIS CONCLUDES THAT THE STAFFING AND FUNDING LEVELS PROPOSED IN THE BUDGET PROBABLY ARE NOT SUFFICIENT TO ACCOMMODATE WORKLOAD REQUIREMENTS UNDER EXISTING LAW. AN ILLUSTRATION OF THIS CAN BE FOUND IN THE DEPARTMENT OF INDUSTRIAL RELATIONS, WHERE THE BUDGET PROPOSES TO ELIMINATE POSITIONS FOR ELEVATOR AND PRESSURE VESSEL INSPECTIONS, EVEN THOUGH 40 PERCENT OF THE ELEVATORS AND STEAM BOILERS IN THE STATE CURRENTLY ARE OVERDUE FOR THE ANNUAL INSPECTIONS REQUIRED BY STATE LAW.

ANOTHER PROGRAM THAT WOULD BE CUT-BACK FROM THE CURRENT SERVICE LEVEL IS THE WORK ACTIVITY PROGRAM IN THE DEPARTMENT OF REHABILITATION.

4. PROGRAM EXPANSIONS. IN ADDITION TO THE INCREASES THAT I MENTIONED A FEW MOMENTS AGO, THE BUDGET PROPOSES TO INCREASE STATE FUNDING IN THREE PROGRAM AREAS: HAZARDOUS SUBSTANCE CONTROL, BUSINESS AND ECONOMIC DEVELOPMENT, AND UNIVERSITY RESEARCH. OUR ANALYSIS GENERALLY CONFIRMS THE NEED TO EXPAND THE STATE'S HAZARDOUS SUBSTANCE CONTROL PROGRAM. IN FACT, WE FORESEE THE NEED FOR SIGNIFICANT INCREASES IN THE FUTURE IF ALL UNCONTROLLED HAZARDOUS WASTE SITES IN THE STATE ARE TO BE CLEANED UP. IN CONTRAST, HOWEVER, WE CANNOT VERIFY THE NEED FOR INCREASES IN TOURISM ADVERTISING AND UNIVERSITY RESEARCH, AND ACCORDINGLY, WE RECOMMEND THAT THESE FUNDS BE DELETED FROM THE BUDGET BILL.

5. INCREASE LOCAL GOVERNMENT'S FISCAL FLEXIBILITY, STABILITY, AND INDEPENDENCE. A FIFTH MAJOR THEME REFLECTED IN THE BUDGET IS THE NEED TO

ALTER THE STATE'S RELATIONSHIP WITH LOCAL GOVERNMENTS IN A VARIETY OF AREAS. OUR ANALYSIS FINDS SEVERAL OF THESE PROPOSALS TO HAVE MERIT, INCLUDING:

- o THE CONSTITUTIONAL AMENDMENT TO RESTORE LOCAL GOVERNMENT'S ACCESS TO THE GENERAL OBLIGATION BOND MARKET.
- o THE REPLACEMENT OF THE SB 90 CLAIMS PROCESS WITH SOME FORM OF BLOCK GRANT FOR REIMBURSING LOCAL MANDATED COSTS.
- o SOME OF THE PROGRAM REALIGNMENTS.

AT THE SAME TIME, WE DO NOT BELIEVE THAT THE GOVERNOR'S PROPOSALS FOR ALTERING THE STATE-LOCAL FISCAL RELATIONSHIP NECESSARILY WILL BRING ABOUT A QUANTUM INCREASE IN LOCAL GOVERNMENTS' FISCAL STABILITY.

6. EMPLOYMENT REDUCTIONS. AS I'VE ALREADY NOTED, THE ADMINISTRATION HAS MADE A SIGNIFICANT EFFORT TO REDUCE THE NUMBER OF STATE EMPLOYEES. WHERE THESE REDUCTIONS ARE JUSTIFIED ON A WORKLOAD OR EFFICIENCY BASIS, WE HAVE NO PROBLEM WITH THEM. OUR REVIEW INDICATES, HOWEVER, THAT IN MANY CASES, DECISIONS ON STAFFING LEVELS SEEM NOT TO HAVE BEEN MADE ON THE BASIS OF PROGRAM NEEDS.

FOR EXAMPLE, THE BUDGET PROPOSES TO SUBSTITUTE CONTRACTED HIGHWAY MAINTENANCE FOR MAINTENANCE WORK PERFORMED BY STATE STAFF. WHILE THIS WOULD REDUCE THE NUMBER OF STATE EMPLOYEES, IT WOULD INCREASE THE COST OF MAINTENANCE WORK BY OVER \$1 MILLION -- NOT A VERY GOOD DEAL FROM THE TAXPAYERS' STANDPOINT. SIMILARLY, THE BUDGET PROPOSES TO REPLACE 35 PERSONNEL-YEARS OF SEASONAL HELP IN THE DEPARTMENT OF FORESTRY WITH CALIFORNIA CONSERVATION CREWS (WHO ARE NOT CONSIDERED STATE EMPLOYEES). HERE AGAIN, WHILE THE SUBSTITUTION WOULD REDUCE THE NUMBER OF STATE WORKERS, IT WOULD REQUIRE THE DEPARTMENT TO PAY 47 PERCENT MORE FOR WORKERS THAT HAVE BEEN FOUND TO BE 50 PERCENT - 75 PERCENT LESS PRODUCTIVE.

II. MAJOR ISSUES FACING THE LEGISLATURE

IN THE COMPANION DOCUMENT TO THE ANALYSIS (PERSPECTIVES AND ISSUES), WE IDENTIFY 16 ISSUES THAT WE BELIEVE WARRANT YOUR ATTENTION IN THE MONTHS AHEAD. THE ANALYSIS ITSELF, OF COURSE, IDENTIFIES MANY MORE ISSUES THAT DO NOT CUT ACROSS PROGRAM LINES AND CAN BE DISCUSSED IN CONNECTION WITH INDIVIDUAL ITEMS OF THE BUDGET BILL. LET ME MENTION BRIEFLY WHAT I CONSIDER TO BE AMONG THE MORE IMPORTANT OF THESE ISSUES AND OFFER SOME SUGGESTIONS FOR ADDRESSING THEM.

1. HOW LARGE SHOULD THE RESERVE FOR ECONOMIC UNCERTAINTIES BE?
(PERSPECTIVES AND ISSUES, PAGE 162)

ONE OF THE MOST DIFFICULT ISSUES YOU FACE IN 1984 IS HOW MUCH MONEY SHOULD BE WITHHELD FROM THE SPENDING STREAM AND SET ASIDE IN THE STATE'S RAINY DAY FUND AS A HEDGE AGAINST REVENUE SHORTFALLS AND UNANTICIPATED EXPENDITURE INCREASES. IT IS ALSO ONE OF THE MOST IMPORTANT ISSUES YOU FACE. I SAY THIS BECAUSE THE OUTLOOK FOR GENERAL FUND REVENUES BEYOND THE BUDGET YEAR IS NOT NEARLY AS POSITIVE AS THE OUTLOOK FOR 1984-85. THIS IS DUE ALMOST ENTIRELY TO ONE FACTOR: THE PROSPECT OF \$200 BILLION - \$300 BILLION DEFICITS IN THE FEDERAL BUDGET CONTINUING THROUGHOUT THE BALANCE OF THIS DECADE AND INTO THE 1990s.

FRANKLY, I DON'T SEE HOW THE NATION'S CREDIT MARKETS CAN ACCOMMODATE FEDERAL BORROWING DEMANDS OF THIS MAGNITUDE WITHOUT JEOPARDIZING THEIR ABILITY TO SATISFY THE BORROWING NEEDS OF BUSINESS, HOMEBUYERS, AND CONSUMERS. AS THESE COMPETING DEMANDS FOR CREDIT COLLIDE, INTEREST RATES WILL SHOOT UP, JEOPARDIZING CONTINUATION OF THE ECONOMIC RECOVERY. UNDER THESE CIRCUMSTANCES, CALIFORNIA WILL NEED A HEALTHY RESERVE TO BACK UP THE GENERAL FUND, PERHAPS AS EARLY AS 1985-86.

I APPRECIATE THE DIFFICULTIES YOU FACE IN BUILDING A RESERVE ALMOST FROM THE GROUND UP. A DOLLAR SET ASIDE IN THE RESERVE IS A DOLLAR THAT CANNOT BE USED TO MEET THE DEMANDS OF THOSE WHO DEPEND ON THE STATE FOR SERVICES. FURTHERMORE, I RECALL CLEARLY HOW THE PUBLIC BALKED AT A RESERVE THAT WAS PERCEIVED TO BE -- AND, IN FACT WAS -- EXCESSIVE, AND I KNOW YOU DO NOT WANT TO RUN THAT RISK AGAIN.

NEVERTHELESS, I BELIEVE THE STATE MUST HAVE A HEALTHY RESERVE IN ORDER TO PROVIDE FOR THE CONTINUITY OF ESSENTIAL SERVICES -- AND TO BUY YOU TIME -- IN THE EVENT THAT THE ECONOMY DOES NOT PERFORM AS EXPECTED. WHILE THE AMOUNT PROPOSED BY THE GOVERNOR -- \$950 MILLION -- IS LARGE IN ABSOLUTE TERMS, IT IS BY NO MEANS EXCESSIVE GIVEN THE AMOUNT OF GENERAL FUND REVENUES AT RISK. IN FACT, IF THE DEPARTMENT OF FINANCE'S PESSIMISTIC ECONOMIC SCENARIO WERE TO MATERIALIZE, THE REVENUE SHORTFALL IN 1984-85 WOULD BE \$1.7 BILLION -- NEARLY TWICE THE PROPOSED RESERVE.

I RECOMMEND THAT YOU APPROVE THE GOVERNOR'S PROPOSAL.

2. HOW CAN THE LEGISLATURE MAINTAIN ADEQUATE CONTROL OVER THE NEW PRISON CONSTRUCTION PROGRAM?
(ANALYSIS, PAGE 1359)

THE BUDGET REQUESTS ABOUT \$95 MILLION FROM THE GENERAL FUND TO FINANCE THE CONSTRUCTION OF NEW PRISONS. YOU HAVE ALREADY AUTHORIZED EACH OF THE PRISONS FOR WHICH THESE FUNDS ARE REQUESTED. THUS, WHAT YOU MUST DECIDE NOW IS HOW MUCH IS NEEDED FOR THESE PRISONS IN THE BUDGET YEAR AND HOW THE MONEY SHOULD BE USED.

IF YOU LOOK TO THE ANALYSIS FOR HELP IN MAKING THESE DECISIONS, I AM SORRY TO SAY YOU WILL COME UP EMPTY-HANDED. THIS IS BECAUSE NEITHER THE GOVERNOR'S BUDGET NOR THE DEPARTMENT OF CORRECTIONS HAS PROVIDED THE INFORMATION THAT YOU MUST HAVE IN ORDER TO ACT ON THE REQUEST. EVEN NOW,

INFORMATION IS LACKING ON (1) THE SPECIFIC SITES AT WHICH THE FUNDS WILL BE SPENT, (2) CORRECTIONAL PROGRAMS FOR THE NEW FACILITIES, (3) MASTER PLANS, (4) PRELIMINARY PLANS, (5) COST ESTIMATES, AND (6) EQUIPMENT LISTS.

WITHOUT THIS INFORMATION, I DON'T SEE HOW YOU CAN REVIEW THIS REQUEST FOR NEARLY \$100 MILLION IN A MEANINGFUL FASHION.

THIS INFORMATION SHOULD BE FORTHCOMING BEFORE YOU ARE ASKED TO APPROPRIATE THE FUNDS REQUESTED. IF WHAT'S PAST IS PROLOGUE, HOWEVER, A LOT OF THE INFORMATION YOU NEED PROBABLY WILL NOT BE PROVIDED IN TIME FOR YOU TO EVALUATE IT BEFORE COMPLETING ACTION ON THE BUDGET. WITHOUT THIS INFORMATION, YOU WILL HAVE TO DECIDE WHETHER TO FUND THE PROJECTS BASED ON YOUR FAITH IN THE DEPARTMENT'S ABILITY TO CARRY OUT THE PROJECTS IN ACCORDANCE WITH YOUR POLICIES, OR DELETE THE FUNDS FROM THE BUDGET BILL AND RUN THE RISK OF BEING HELD RESPONSIBLE FOR DELAYING THE CONSTRUCTION PROGRAM. NEITHER ALTERNATIVE IS VERY APPEALING. I SUSPECT THAT UNDER THESE CIRCUMSTANCES, WE WILL BE RECOMMENDING THE LATTER COURSE OF ACTION, SINCE RECENT EXPERIENCE INDICATES THAT REVIEW OF PROPOSED CONSTRUCTION EXPENDITURES AFTER THE FUNDS HAVE BEEN APPROPRIATED GENERALLY DOES NOT PROVIDE FOR THE TYPE OF LEGISLATIVE OVERSIGHT AND CONTROL THAT YOU RIGHTLY INSIST UPON WITH RESPECT TO STATE SPENDING GENERALLY.

3. HOW CAN THE LEGISLATURE ENSURE THAT ITS PRIORITIES ARE ADDRESSED BY TAX EXPENDITURE PROGRAMS?
(PERSPECTIVES AND ISSUES, PAGE 131)

LAST YEAR, I CALLED THIS COMMITTEE'S ATTENTION TO THE DISPARITY IN THE DEGREE TO WHICH DIRECT SPENDING THROUGH THE BUDGET AND "SPENDING" THROUGH THE TAX SYSTEM WERE CONTROLLED. UNFORTUNATELY, FOR WHATEVER REASON, THE DEPARTMENT OF FINANCE HAS CHOSEN NOT TO PROVIDE DATA ON TAX EXPENDITURES IN 1984-85, SO I CANNOT TELL YOU WHETHER THIS DISPARITY STILL EXISTS.

I CAN TELL YOU, HOWEVER, THAT BETWEEN 1981-82 AND 1983-84, TAX EXPENDITURES INCREASED BY 22.3 PERCENT, WHILE DIRECT GENERAL FUND EXPENDITURES INCREASED BY 4.4 PERCENT.

BECAUSE TAX EXPENDITURE PROGRAMS ALLOCATE RESOURCES IN MUCH THE SAME WAY THAT THE BUDGET BILL DOES, THEY ARE A REFLECTION OF SPENDING PRIORITIES. WITHOUT ONGOING LEGISLATIVE REVIEW OF THESE EXPENDITURES, HOWEVER, THERE IS NO WAY OF KNOWING WHETHER THESE PROGRAMS REFLECT YOUR PRIORITIES. PUT ANOTHER WAY, TO THE EXTENT THAT YOU DO NOT REVIEW TAX EXPENDITURES ON A REGULAR BASIS, YOU MAY BE LETTING AN AMOUNT EQUAL TO NEARLY 40 PERCENT OF THE GENERAL FUND BUDGET GET AWAY FROM YOU.

WE MAKE SEVERAL SUGGESTIONS IN THE PERSPECTIVES AND ISSUES DOCUMENT AS TO HOW YOU CAN IMPROVE YOUR CONTROL OF THESE PROGRAMS.

4. HOW CAN THE LEGISLATURE INTRODUCE SOME STABILITY AND PREDICTABILITY TO THE SETTING OF STUDENT FEES AT UC AND CSU?
(ANALYSIS, PAGE 1649)

I'M SURE THAT THE PHRASE YOU LEAST WANT TO HEAR RIGHT NOW IS "STUDENT FEES." PRESUMABLY, YOU'VE STABILIZED FEES AT THE COMMUNITY COLLEGE LEVEL FOR THE NEXT THREE YEARS. NO SUCH STABILITY OR PREDICTABILITY, HOWEVER, EXISTS AT THE OTHER TWO SEGMENTS OF HIGHER EDUCATION.

IN OUR ANALYSIS, WE RECOMMEND THAT YOU ADOPT A LONG-TERM POLICY TOWARD STUDENT FEES SO THAT YOU CAN AVOID HAVING TO DEAL WITH THIS ISSUE YEAR-AFTER-YEAR. WE ALSO SUGGEST A NUMBER OF PRINCIPLES ON WHICH WE THINK, SUCH A POLICY SHOULD BE BASED. IN THE MEANTIME, WE RECOMMEND THAT YOU NOT FURTHER RESTRICT THE PERMISSIBLE USES FOR STUDENT FEE REVENUES, AS THE GOVERNOR PROPOSES IN THE BUDGET.

5. SHOULD THE LEGISLATURE GIVE LOCAL GOVERNMENTS MORE FLEXIBILITY IN ADMINISTERING STATE PROGRAMS?
(PERSPECTIVES AND ISSUES, PAGE 165)

ONCE AGAIN, THE GOVERNOR HAS PROPOSED MAJOR PROGRAM REALIGNMENTS IN THE HEALTH AREA WHICH WILL REQUIRE YOU TO CONSIDER WHAT THE PROPER BALANCE IS BETWEEN STATE CONTROL AND LOCAL FLEXIBILITY IN THE ADMINISTRATION OF STATE PROGRAMS. EMBODIED IN FIVE SEPARATE BILLS THAT WILL BE COMING BEFORE YOU IN THE MONTHS AHEAD, THE PROPOSED REALIGNMENTS WOULD REDUCE STATE ADMINISTRATIVE STAFF AND TRANSFER VARIOUS STATE RESPONSIBILITIES TO THE LOCAL LEVEL. IN EVALUATING THESE PROPOSALS YOU WILL HAVE TO WEIGH THE POTENTIAL BENEFITS FROM THE REALIGNMENTS -- GREATER RESPONSIVENESS TO LOCAL CONDITIONS -- AGAINST THE POTENTIAL COSTS -- THE LOSS OF STATEWIDE UNIFORMITY WITH REGARD TO MINIMUM SERVICE AND ELIGIBILITY STANDARDS.

6. HOW CAN THE LEGISLATURE IMPROVE THE EFFECTIVENESS AND COORDINATION OF THE STATE'S HAZARDOUS SUBSTANCES CONTROL PROGRAM?
(PERSPECTIVES AND ISSUES, PAGE 174)

ANOTHER MAJOR ISSUE FACING YOU IS HOW TO IMPROVE THE EFFECTIVENESS OF THE STATE'S EFFORTS TO CLEAN UP AND CONTROL HAZARDOUS SUBSTANCES. THE PROBLEMS CREATED BY HAZARDOUS SUBSTANCES HAVE DEVELOPED SLOWLY OVER THE YEARS, AND CONSEQUENTLY THEY HAVE NOT BEEN DEALT WITH IN A COMPREHENSIVE MANNER. THIS IS EVIDENT IN THE FACT THAT 12 DIFFERENT STATE DEPARTMENTS SHARE RESPONSIBILITY FOR DEALING WITH THIS PROBLEM. HERE IS A CLASSIC CASE WHERE SHARED RESPONSIBILITY CAN LEAD TO NO ACCOUNTABILITY.

OUR ANALYSIS INDICATES THAT THE CURRENT MECHANISMS FOR PLANNING AND COORDINATING THE ACTIVITIES OF THESE 12 DEPARTMENTS ARE NOT ADEQUATE. WHILE THE PROPOSALS MADE IN THE BUDGET TO IMPROVE THE EFFORTS OF THESE 12

AGENCIES GENERALLY REPRESENT A STEP IN THE RIGHT DIRECTION, YOUR OVERSIGHT IS REQUIRED TO PUSH THESE EFFORTS ALONG.

IN ADDITION TO THESE ISSUES, YOU WILL HAVE TO DEAL WITH THE PERENNIAL ISSUES OF COLLECTIVE BARGAINING (P&I, PAGE 227), COST-OF-LIVING ADJUSTMENTS (P&I, PAGE 145), AND SB 90 REIMBURSEMENTS (P&I, PAGE 205). I WON'T TAKE THE TIME TO DISCUSS THESE ISSUES NOW; THEY ARE DISCUSSED IN THE PERSPECTIVES AND ISSUES.

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