BOARD OF SUPERVISORS
AGENDA LETTER

Clerk of the Board of Supervisors
105 E. Anapamu Street, Suite 407
Santa Barbara, CA 93101
(805) 568-2240

Agenda Number:

Department Name:	CEO
Department No.:	012
For Agenda Of:	2/9/10
Placement:	Departmental
Estimated Tme:	30 minutes
Continued Item:	No
If Yes, date from:	
Vote Required:	Majority

TO:	Board of Supervisors	
FROM:	Department Director(s)	Michael F. Brown, County Executive Officer
	Contact Info:	Jason Stilwell, Assistant CEO, 568-3413 Terri Nisich, Assistant CEO, 568-3400
SUBJECT:	**Report on Governor's Proposed FY 2010-11 State Budget**	

County Counsel Concurrence
As to form: N/A

Auditor-Controller Concurrence
As to form: N/A

Recommended Actions:

It is recommended that Board of Supervisors:

a) Accept and file a report on the Governor's Proposed FY 2010-11 State Budget; and

b) Communicate the impacts the budget would have on County services to the Governor and Santa Barbara County legislative delegation.

Summary Text:

With billions of dollars of temporary budget solutions from last fiscal year set to expire and the economy recovering slowly, California once again faces a staggering budget problem. The Governor submitted his proposed FY 2010-11 Budget on January 8, 2010, declaring a fiscal emergency and projecting a State General Fund deficit of $19.9 billion through the end of FY 2010-11. This projection consists of a General Fund deficit of $6.6 billion at the end of FY 2009-10, assuming no corrective budget actions are taken by the Legislature; an additional $12.3 billion deficit in FY 2010-11; and a $1 billion reserve. Approximately $8 billion, or 35% of the Governor's budget, relies on funding or flexibility to be provided by actions of the federal government: $1 million in FY 2009-10 and $6.9 billion in FY 2010-11.

These federal funds and federal approval of flexibility to make reductions in various programs are at the core of the Governor's budget proposal. If the federal government fails to provide the requested relief, the Governor proposed a "triggering" of revenue increases and program reductions of approximately $6.9 billion, including elimination of significant health and human service programs. The remainder of the Governor's proposal consists of various fund shifts, including a transportation tax proposal and ballot initiatives to allow use of Proposition 10 and Proposition 63 funds to help balance the budget.

Background:

Budget Gap: On February 20, 2009, the State adopted a 17-month budget that included $36 billion in solutions to solve the budget deficit and required voter approval of certain budget referenda. However, the failure of the propositions to garner passage by the voters during the special election in May 2009 and the further decline in revenues resulted in an additional $24 billion budget gap. On July 28, 2009, the State adopted amendments to the FY 2009-10 Budget to address the ongoing budget shortfall exacerbated by the continued decline in revenues. The accumulation of $60 billion in budget solutions adopted in FY 2009-10 addressed the largest budget gap the state had ever faced.

However daunting the budget process was in 2009, the State now faces an additional $19.9 billion budget gap, an estimate the Legislative Analyst's Office claims is "more optimistic than ours." Indeed, the gap between revenues and expenditures is growing amidst an already sluggish economy. This projection consists of a General Fund deficit of $6.6 billion at the end of FY 2009-10, assuming no corrective budget actions are taken by the Legislature; an additional $12.3 billion deficit in FY 2010-11; and a $1 billion reserve.

As indicated in the chart below, the reasons for the budget gap include: the inability of the state to achieve previous budget solutions in several areas; the effects of several adverse court rulings; additional costs associated with population-driven and caseload-driven entitlement programs; and for FY 2010-11, the expiration of various one-time and temporary budget solutions approved in 2009.

Table 1: Summary of Budget Gap

SHORTFALL IN FY 2010-11 GOVERNOR'S BUDGET (dollars in billions)	
Projected 2010-11 Deficit	$6.9
Revenue Decline	$3.4
Federal & State Court Litigation	$4.9
Erosions of Previous Solutions	$2.3
Population/Caseload Growth	$1.4
Rebuild Reserve	$1.0
Total Shortfall	**$19.9**

To solve the deficit, the Governor's Budget proposes a combination of spending reductions, alternative funding, fund shifts, and additional federal funds to close the $19.9 billion budget gap. Given the re-emergence of a current year shortfall and the necessary time for budget solutions to achieve their full value, the budget would have to be adopted immediately during the Special Session of the Legislature. Delays in adoption of the Governor's proposals until the enactment of the FY 2010-11 budget would result in the loss of up to $2.4 billion in budgetary solutions and thereby necessitate even deeper reductions in FY 2010-11 budget.

Table 2: Proposed Budget Solutions to Resolve Gap

PROPOSED BUDGET SOLUTIONS (dollars in billions)	2009-10	2010-11	Total	%
Expenditure Reductions	$1,034	$7,475	$8,509	43%
Federal Funds	$8	$6,905	$6,913	35%
Alternative Funding	$150	$3,736	$3,886	20%
Fund Shifts & Other Revenues	$0	$572	$572	3%
Total	**$1,192**	**$18,688**	**$19,880**	**100%**

State's Cash Situation: In addition to confronting the budget gap, the State Controller warned the Governor and Legislature on January 22, 2010 that the state could run out of cash before the end of this fiscal year and urged them to make $2.7 billion in solutions to avoid delays in payments. In fact, recently released revenue and expenditure estimates shows that the State's cash position for the remainder of the current fiscal year will be weak from approximately March 30 through April 21. This upcoming shortfall is shallower in depth and shorter in duration than the State's cash problems in the spring of 2009, when the problem started earlier in the year and grew progressively worse with each passing month. According to the Controller's projections, California will drop below its $2.5 billion prudent minimum cash balance on March 30 by $1.3 billion. On April 1, the State will be in the red by $197 million, and resources to pay bills are not expected to return to safe levels until April 21. Barring any unforeseen circumstances, such as a spike in expenditures or steep decline in revenues, $2.7 billion in cash solutions are necessary to avoid a cash shortage in the current fiscal year.

However, even with the passage of the Governor's proposed budget solutions during the current special session, at least another $2 billion in cash solutions are required to protect the cash balance in the current fiscal year alone. The Controller warned that if there is failure to make any progress on the combined $19.9 billion two-year budget problem during the current special session and allow a stalemate to continue into the new fiscal year, the State will once again face the difficult task of averting a cash crisis beginning in July. The State's cash position will drop below the $2.5 billion prudent cushion during the middle of July, and starting July 29, the cash deficit will reach a negative $1.1 billion. From that date forward, the State's inability to meet all of its payment obligations in a timely fashion and the severity of its cash problems will amplify with each passing week and month.

Federal Revenue and "Trigger" Reductions: As mentioned, the Governor has identified a number of areas in which the federal government has mandated or failed to fully fund programs for which the state must provide funding. According to the Governor's budget, federal mandates, including spending requirements, constraints on program reductions, and federal court decisions delaying reductions of services have contributed more than $1.4 billion toward the current budget gap. The state is demanding additional flexibility in managing certain program costs and additional federal reimbursement for certain programs.

These requests total $6.9 billion in new federal funding assumed in the Governor's budget proposal. If the state fails to secure these additional funds by July 15, 2010, the Administration has developed a list of permanent expenditure reductions that will occur, totaling $4.6 billion in General Fund reductions. In addition to the expenditure reductions, the Governor proposes one-year revenue increases of $2.4 billion. The trigger reductions affecting the County include the following:

- Elimination of the CalWORKs Program ($1 billion)
- Elimination of the Healthy Families Program ($126 million)
- Elimination of the IHSS Program ($495 million)
- Redirect additional county savings associated with CalWORKs and IHSS reductions ($325 million)
- Fund existing mental health services with Proposition 63 funding ($847 million)
- Reduce Medi-Cal eligibility to the minimum allowed under current federal law and eliminate most remaining optional benefits ($532 million)
- Eliminate non-court required inmate rehabilitation programs, implement banked parole for low-risk serious and violent offenders, expand crimes where convicted felons will serve time in local jails, and increase the number of parolees each agent will supervise ($280 million)

Alternative Revenue Sources: In addition to federal revenue, the Governor proposes a variety of "alternative funding" solutions. These solutions provide funding for a wide variety of programs/projects, but move the costs away from the General Fund. The proposals that impact the County include:

- *Tranquillon Ridge Oil Revenues*: A reduction of $140 million in the General Fund and replacement with revenue generated from the Tranquillon Ridge oil lease. It is estimated that the Tranquillon Ridge oil lease will generate $1.8 billion in advanced royalties over the next 14 years. This revenue will be used to fund state parks. The Governor's Budget assumes that the State Lands Commission will approve the Tranquillon Ridge proposal. If not approved by the Commission, legislation would be necessary.

- *California Children and Families Act of 1998 (Proposition 10)*: A reduction of $550 million in the General Fund through a redirection of Proposition 10 funding from the California Children and Families Commission budget to high priority state programs serving children. This proposal includes shifting (for five years) approximately 50 percent of the Proposition 10 revenues currently directed to state and local accounts within the Commission's budget ($242 million in FY 2010-11) and a one-time sweep of state and local reserves ($308 million). The redirected funds will be used to support children enrolled in programs administered by the Department of Social Services and the Department of Developmental Services. Implementation of this proposal will require voter approval. The Governor anticipates this initiative will be included in the June 2010 election. This proposal is similar to the failed Proposition 1D at the May 2009 special election. Over a five-year period, this amounts to a $10-11 million reduction in funding for local programs in Santa Barbara County, which could in turn affect approximately 9,000 children. The redirection of funding will most likely result in the loss of local "safety net" programs, staff positions, services for young children and their families such as health, education, early intervention and basic needs and the loss in the infrastructure of First 5 Santa Barbara. The redirect would also significantly impact the ability to draw down funding through matching federal, state and private funds.

- *Mental Health Service Act (MHSA) (Proposition 63)*: Reduces by $452.3 million in General Fund and substitutes with Mental Health Services Act (Proposition 63) funding for a portion of the EPSDT program and a portion of the Mental Health Managed Care program. This requires amending the non-supplantation and maintenance-of-effort provisions of Proposition 63 and requires voter approval. The Governor anticipates this initiative will be included in the June 2010 election. Please note that a ballot measure to redirect MHSA funds failed in the May 2009 special election.

- *Transportation*: The Governor proposes to eliminate the sales tax on gasoline, proceeds of which fund Prop 42, currently valued for FY 2010-11 at $1.573 billion for Prop 42 and $879 million for the spillover account. As a replacement for the sales tax elimination, the Governor proposes to institute a 10.8-cent excise tax on gasoline (Highway User Tax Account or HUTA) increase that falls short of being revenue neutral by approximately $976 million, or the equivalent of a 5-cent per gallon tax cut. Under the proposal, the total excise tax would increase to 28.8-cents per gallon, whereas the existing combined Prop 42 and HUTA taxes currently equal 34-cents. The proposal does not affect the current distribution of the 18-cent HUTA. The 10.8-cent excise tax increase would be allocated as follows: $629 million for the State Transportation Improvement Program (STIP); $629 million for local streets and roads; and $603 million for the General Fund for transportation bond debt service. The summary of the Governor's budget proposal indicates that the excise tax distribution will be adjusted in the future to account for the growing debt service on the transportation bonds. It is unclear whether this would mean an annual increase in the gas tax equivalent to the growth in bond debt service as reported by Transportation California, or if the State would simply change the distribution formula and take the funds from either cities and counties and/or the STIP. Considering that the existing HUTA formula is left intact combined with this replacement revenue, local streets and roads are estimated to receive $1.72 billion in 2010-11, or $858 million for counties.

Expenditure Reductions: Some of the major budget proposals affecting the County are illustrated below.

<u>Heath and Human Services</u>
The largest proposed budget cuts occur in health and human service expenditures. The Governor's FY 2010-11 budget proposes cuts of $2.4 billion, or an 8% decrease from the revised FY 2009-10 budget year. For context, last year's budget reductions totaled $1 billion, or a 3% reduction. **The attached spreadsheets contain detailed impacts of these proposals on the Department of Social Services, the Alcohol, Drug, and Mental Health Services Department, and the Public Health Department (including impacts of the trigger reductions).**

The following reductions are proposed to take effect on July 1, 2010:

- *Medi-Cal*: The Governor proposes various measures to cut Medi-Cal costs through unspecified limits on services, utilization controls, and increased cost sharing with benefit recipients through copayment requirements or premiums. The collective savings from those proposals is $750 million. (Some such changes may require federal approval.) The proposal also would save $294 million in FY 2009-10 and FY 2010-11 combined by eliminating full-scope Medi-Cal services for certain immigrants, eliminating adult day health care benefits, delaying payments to institutional providers, and rescinding a family planning rate increase. Expanded antifraud efforts are proposed to reduce costs by $26 million.

- *Healthy Families Program*: The Governor proposes to reduce Healthy Families Program eligibility from 250 percent of the federal poverty level (FPL) to 200 percent in addition to eliminating vision coverage under the program. This will save an estimated $10.5 million in the current budget year and $63.9 million in 2010-11. The Governor wants this change to take effect on May 1 in order to achieve current year savings. Furthermore, the state scores a conforming $3.9 million decrease in the California Children's Services (CCS) program for beneficiaries who were previously eligible under the Healthy Families Program. The Governor also proposes to increase premiums for families with incomes from 151 percent to 200 percent of the FPL. The premium increase include $30 per child or $90 maximum increase per family with three or more children (currently, these families pay $16 per child or $48 maximum). This proposal would not affect families with an income under 150 percent of the FPL. The Governor saves $21.7 million from both the premium increase and the elimination of the HFP vision benefit.

- *CalWORKs Program*: The Governor proposes three reductions in the CalWORKs program: 1) reducing CalWORKs grants by 15.7 percent; 2) reducing child care provider reimbursements (no other detail was provided); and 3) eliminating the Recent Noncitizen Entrants program, which provides benefits to legal immigrants who have been in the U.S. less than five years (24,000 people). The Governor saves $146.1 million in FY 2010-11 if these cuts become effective in June. The Governor also notes that these cuts, if enacted, would also create a $42.7 million savings in the Department of Developmental Services and $18.3 million in the California Student Aid Commission.

- *IHSS Program*: The Governor is again attempting to limit the provision of services to current and prospective IHSS recipients by eliminating all services for recipients with a Functional Index (FI) score of 4 or less, or 87 percent of the current recipient population. The 2009-10 budget includes IHSS service eliminations for those with a FI under 2 and is currently being litigated. There is currently an injunction in place preventing the state from implementing the service cuts. In addition, the Governor wants to reduce the state's participation in wages for IHSS workers down to the state minimum wage of $8.00 per hour. The state's share of 60 cents per hour for benefits would be unchanged. Together, the reduction of the state's wage participation and the elimination of services for those below a functional index of 4 would save the state an estimated $77.9 million in FY 2009-10 and $872.6 million in FY 2010-11. These estimates assume a current year implementation.

- *Substance Abuse Offender Treatment Program*: The Governor proposes to zero out funding ($18 million) for the Substance Abuse Offender Treatment Program. No support for Proposition 36 is provided for in the Governor's proposed budget.

- *Supplementary Security Income/State Supplementary Payment (SSI/SSP)*: The Governor proposes to reduce SSI/SSP grants to individuals by $15 per month (from $845 to $830), which would bring them down to the federal minimum. Individual grants were reduced down to the federal minimum last year. As proposed in previous years, the Governor also wants to eliminate the Cash Assistance Program for Immigrants (CAPI). These two proposals combined will save the state $21.8 million in 2009-10 and $285.1 million in FY 2010-11 if enacted by June 1.

- *California Food Assistance Program*: The Governor, as he did in the 2009 budget, proposes to eliminate the California Food Assistance Program effective June 1, for a savings of $3.8 million in the current year and $56.2 million in FY 2010-11.

Agriculture

- *Williamson Act*: The Governor's budget includes only $1,000 for Williamson Act subventions. This is consistent with the Governor's previous reduction, which eliminated $34.7 million for the program in the FY 2009-10 budget.

General Government

- *Elections*: The Governor included in his budget a reimbursement for county costs associated with last May's special election, which was called to let the voters decide various budget measures. The state's share of the cost for that election was $68.2 million and attempts to have that amount reimbursed last year were unsuccessful.

- *Proposition 1A Interest*: While it will not have any effect on local revenues, it is worth noting that the budget proposal includes $90.8 million for interest payments on the Proposition 1A bonds sold in FY 2009-10.

- *Mandates*: The Governor's budget proposal continues to suspend all mandates suspended in the current fiscal year, amounting to savings of $137 million. When the state suspends mandates, counties have the option of funding the services at their own cost or not providing the service at all. The mandates that remain in effect deal with elections, public safety, or property tax administration. These mandates receive a proposed funding increase of $4 million over 2009-10 levels. The Governor also proposes to defer this year's payment ($95 million) for pre-2004 (pre-Proposition 1A) mandate reimbursements. The state had deferred mandate payments for several years prior to the passage of Proposition 1A, and had accrued a debt of more than $1 billion dollars. The provisions of Proposition 1A and state statute allow the state to repay that debt over a period of fifteen years, but the state has deferred these amortized payments for the last few years. These are statutorily required to be repaid completely by FY 2020-21.

Public Safety

- *Criminal Justice*: The Governor's budget assumes savings related to proposed statutory changes to require that offenders convicted of certain non-serious, non-violent, non-sexual offense felonies serve a maximum sentence of one year in county jail in lieu of a state prison sentence. The administration estimates this would reduce costs by $25 million in FY 2009-10 and $292 million in FY 2010-11. This would impact the Sheriff's Department by virtue of an increase in the county jail population. The implementation of jail terms instead of prison terms for certain felonies would result in more local bed days in a jail system that is already dealing with over crowding. This would also likely result in more early releases and more offenders coming to the Probation Department. Probation expects that 1% of any prison population reductions as a result of this change would result in offenders being returned to Santa Barbara County. Furthermore, the Governor is proposing a reduction in AIDS drug assistance program funding to inmates in county jails, a savings of approximately $9.5 million in FY 2010-11. This would eliminate the subsidy provided to pharmacies for AIDS drugs dispensed to County jail inmates. If dispensing continues at current levels, the cost to the Sheriff's Department would increase approximately $50,000.

Conclusion: The Legislature faces incredibly daunting challenges in balancing the budget during the current fiscal emergency special session, as well as its regular session, this year. The Governor’s trigger cuts, to take effect if federal funding is less than the Governor hopes for, are painful and in some cases draconian. The Legislative Analyst’s Office reports that it is reasonable to assume the state will secure some additional federal funding and flexibility; however, securing all of the federal relief the Governor seeks is very unlikely. Nevertheless, the Legislature has 45 days (until February 22, 2010) to address $8.9 billion of the $19.9 billion problem. Moreover, in order to make the major expenditure reductions that will be required in this budget, the Legislature and the Governor will need to agree to a framework to solve much of the budget problem by the end of March. Delays in adoption of the Governor’s proposals until the enactment of the FY 2010-11 budget would result in the loss of up to $2.4 billion in budgetary solutions and thereby necessitate even deeper reductions in the FY 2010-11 budget.

Fiscal and Facilities Impacts: Actual and hypothetical impacts are stated in the Board letter.

Attachments:

1. State Budget Impacts for DSS, ADMHS, and Public Health
2. PowerPoint Presentation

Authored by: Kimbra McCarthy, CEO Analyst 568-3261

cc:

Department Heads
Assistant County Executive Officers
CEO Fiscal and Policy Analysts
Recognized Employee Organizations