Minor Capital Outlay

We recommend deletion of Item 894-301-036(d) for minor capital outlay, for a savings of $34,400.

Budget Item 894-301-036(d) requests an appropriation of $34,400 for the 1981–82 minor capital outlay program ($100,000 or less per project). The amount requested represents 50 percent of the Military Department's request for minor capital outlay. Neither the department nor the Department of Finance has identified the projects to be funded from the requested amount. Consequently, we have no basis on which to evaluate the proposal, and we recommend that the funds be deleted.

TAX RELIEF SUMMARY

Item 910

Summary of State Tax Relief Expenditures

The state provides local tax relief, both as subventions to local governments and as direct payments to eligible taxpayers, through ten different programs, each of which is funded under a separate item. Table 1 summarizes, by program, total tax relief expenditures for the prior, current, and budget years.

Table 1
Tax Relief Expenditures
Summary by Program[a]
(in millions)

Tax Relief Program	*Actual 1979–80*	*Estimated 1980–81*	*Proposed 1981–82*	*Change Amount*	*Change Percent*
Senior citizens' property tax assistance	$24.5	$21.0	$21.0	—	—
Senior citizens' property tax deferral	3.2	3.5	5.0	$1.5	42.9%
Senior citizen renters' tax assistance	46.3	51.5	51.5	—	—
Personal property tax relief	224.4	495.7	493.2	−2.5	−0.5
Homeowners' property tax relief	328.2	332.0	126.0	−206.0	−62.0
Open space subventions to local government	13.2	14.0	14.0	—	—
Payments to local governments for sales and property tax revenue losses	2.5	3.0	3.4	0.4	13.3
Renters' tax relief	357.5	405.0	425.0	20.0	4.9
Substandard housing	0.1	0.1	0.1	—	—
Alternative energy tax credits	—	1.5	5.0	3.5	233.3
Total, Tax Relief Expenditures	$1,000.0	$1,327.2	$1,144.2	−$183.0	−13.8%

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

Of the $1,144.2 million budgeted for tax relief in 1981–82, $493.2 million, or about 43 percent of the total, is proposed for subvention to local governments as reimbursement for revenue losses resulting from personal property tax relief (consisting largely of the 100 percent business inventory exemption). Another $126 million will be used to fund homeowners' property tax relief, which is provided as a subvention to local governments to reimburse them for revenue losses resulting from the $7,000 homeowners' property tax exemption. This is less than the full current law cost of the homeowners' exemption because the budget proposes to reduce this reimbursement in order to capture a portion of the 1978–79 unsecured taxes collected by local agencies. Tax relief for renters will require $425 million, and is provided as a refundable income tax credit. A total of almost $78 million will go to low- and moderate-income senior citizens and disabled persons through

TAX RELIEF SUMMARY—Continued

three different programs, which provide direct cash assistance to both homeowners and renters (in amounts that are inversely related to income) and allow senior homeowners to postpone the payment of property taxes. The remaining budgeted expenditures of $22.5 million have been requested for subventions to local government for property tax revenue losses resulting from enforceable open space restrictions under the California Land Conservtion Act of 1965 (the Williamson Act), for sales and property tax revenue losses resulting from specified statutory changes under Chapter 1406, Statutes of 1972 (SB 90), for payments to local governments consisting of income taxes generated by the disallowance of deductions on substandard housing, and for alternative energy tax credits.

Increase in Current Year Costs

The $1,327 million estimated to be spent during the current year is an increase of about $327 million over the $1 billion appropriated for tax relief in the Budget Act of 1979. This net increase primarily results from two factors: (1) an increase in the cost of renters' tax relief, and (2) a $271 million increase in personal property tax relief due to the complete exemption of business inventories by Chapter 1150, Statutes of 1979 (AB 66).

As shown in Table 1, the $1,144 million budgeted for 1981–82 represents a 13.8 percent *decrease* from the $1,327 million estimated to be spent in the current year. This decrease reflects the effect of the proposals discussed below.

1978–79 Unsecured Taxes and Cost-of-Living Adjustment

The Governor's Budget proposes to reduce state reimbursements for the homeowners' and business inventory exemptions in order to capture 1978–79 unsecured property taxes collected by cities, counties, and special districts as a result of a recent state Supreme Court decision regarding the appropriate property tax rate to be used in levying these taxes. The budget proposes to reduce the homeowners' exemption reimbursements by $209 million and the business inventory reimbursements by $26 million, for a total reduction of $235 million in 1981–82.

The budget also proposes to limit the cost-of-living adjustment for the business inventory reimbursement to 4.75 percent in 1981–82, instead of the 13.1 percent adjustment called for by existing law.

Without these proposed changes, the General Fund cost of tax relief would be $1,428 million for 1981–82. This is $101 million, or 7.6 percent more than the current year cost of these programs.

New Energy Tax Credits

Chapter 903, Statutes of 1980, provides for a refundable income tax credit for a portion of the cost of solar energy systems. Chapter 904, Statutes of 1980, provides for a refundable income tax credit for a portion of the cost of energy conservation measures.

SENIOR CITIZENS' PROPERTY TAX ASSISTANCE

Item 910–101(a) from the General Fund — Budget p. GG 165

Requested 1981–82	$21,000,000
Estimated 1980–81	21,000,000
Actual 1979–80	24,522,330
Requested increase None	
Total recommended reduction	$2,000,000

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. ***Senior Citizens' Property Tax Assistance. Reduce Item 910-101-001(a) by $2,000,000, to correct over-budgeting.*** 1624
2. Senior Citizens' Property Tax Assistance. Recommend Budget Bill language to permit more flexibility in the payment of claims in this program and the Senior Citizen Renters' Assistance program. 1624

GENERAL PROGRAM STATEMENT

The Senior Citizens' Property Tax Assistance program provides partial reimbursement for property taxes paid by homeowners with less than $12,000 of household income who are (1) 62 years and over or (2) totally disabled, regardless of age. Assistance varies inversely with income, and ranges from 96 percent of the tax for homeowners with household incomes not exceeding $3,000 to 4 percent of the tax for those with incomes between $11,500 and $12,000. Senior citizens' property tax assistance is available only on that portion of taxes paid on the first $34,000 of full value, after taking into account the $7,000 homeowners' property tax exemption. Assistance disbursed in 1981–82 will be based on taxes paid in 1980–81.

Table 1 shows the total number of approved claimants and the total assistance they received in the years 1977–78 through 1980–81. The table also presents data on average income, average property taxes and average assistance received for all claimants. Preliminary data indicate that in 1980–81, the average income of the 188,193 claimants was $6,673. The average property tax paid was $258, and the average assistance equaled $101, or approximately 39 percent of the amount paid.

Table 1

Senior Citizens' Property Tax Assistance

1977–78 through 1980–81

	Actual 1977–78	*Actual 1978–79*	*Actual 1979–80*	*Preliminary 1980–81*
Number of claimants	325,667	280,459	234,901	188,193
Total assistance[a] (in millions)	$77.8	$70.6	$24.5	$18.6
Per Claimant Averages:				
Household income	$6,318	$6,525	$6,571	$6,673
Property taxes	579	647	263	258
Assistance:				
Amount	239	252	104	101
Percent of taxes	41.3%	38.9%	39.7%	39.1%

[a] Based on Franchise Tax Board workload data and differs somewhat from fiscal year expenditures shown in the budget.

SENIOR CITIZENS' PROPERTY TAX ASSISTANCE—Continued

ANALYSIS AND RECOMMENDATIONS

We recommend that Item 910-101-001 (a) be reduced by $2,000,000 to reflect the continuing decline in participation in the program.

The budget proposes an appropriation of $21 million from the General Fund for support of the Senior Citizens' Property Tax Assistance program in 1981–82. This amount is the same as estimated expenditures in the current year.

Continuing Decline in Participation

The 1980 Budget Act appropriated $24.5 million for disbursement in the 1980–81 fiscal year, based on an estimated 236,000 claimants. As of December 1980, however, only 188,193 persons had applied. As a result, expenditures were estimated at only $18.6 million in the current year. Several thousand additional claims are anticipated for the current year. On this basis, we estimate 1980–81 expenditures at $19.5 million, or $1.5 million lower than the revised budget estimate. Table 2 compares claims received to date with the original estimates for the current year.

Table 2
Senior Citizens' Property Tax Assistance Program
Comparison of Estimated and Actual Program Activity

1980–81	*Number of Claimants*	*Total Assistance*
Budget estimates	236,000	$24,500,000
Preliminary actuals [a]	188,193	18,600,000

[a] As of December 1980.

Chapter 569, Statutes of 1978, was expected to increase participation significantly, due to the extension of assistance to the totally disabled. For the current year, however, of the 192,000 claimants expected to participate, only 8,000 disabled persons and 184,000 nondisabled persons are actually participating in the program. This level of participation indicates that the original estimates for the current year were high, and that participation in the program by *nondisabled* persons is continuing to decline.

There are several factors that have contributed to the decline in participation in the current year. First, relief paid for the current year reflects the lower property tax payments resulting from Proposition 13. Because of reduced average property tax liability, some persons probably determined that assistance was no longer meaningful or necessary. Second, inflation has pushed the income of more of the participants toward or over the $12,000 limit, so that some are no longer eligible and others are receiving less assistance than before.

Our analysis indicates that the $21 million requested for 1981–82 is probably more than will be claimed. The request does not give adequate recognition to the rate of decline in participation by nondisabled seniors during the last three years. While it is possible that more totally disabled persons made eligible by Chapter 569 will become aware of the program and apply for benefits, our analysis indicates that any increase is likely to be offset by the continuing decline in participation by the nondisabled. Therefore, we recommend a reduction in this item of $2.0 million to correct overbudgeting.

Control Language

We recommend Budget Bill language be adopted to permit more flexibility in the payment of claims in this program and the Senior Citizen Renters' Assistance program.

Because there is some uncertainty concerning the level of participation in both this program and the senior citizen renters' program in the budget year, we believe that the Franchise Tax Board should be permitted greater flexibility in the payment of claims. This would allow any deficit in one program to be made up with surplus from the other. Therefore, we recommend that the following language be included in this item:

"Provided further that any unexpended balance in this item may be used to make payments to senior citizen renter claimants under Item 910-101-001(c).

SENIOR CITIZENS' PROPERTY TAX POSTPONEMENT

Item 910-101(b) from the General Fund — Budget p. GG 166

Requested 1981–82	$5,000,000
Estimated 1980–81	3,500,000
Actual 1979–80	3,246,120
Requested increase $1,500,000 (+42.9 percent)	
Total recommended reduction	None

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. We recommend that legislation be enacted to repeal the inflation adjustment to the income limit for eligibility for the Senior Citizens' Property Tax Postponement program. 1626

GENERAL PROGRAM STATEMENT

The property tax postponement program allows eligible homeowners to defer payment of all or a portion of the property taxes on their residences. Deferred taxes are paid to local governments by the state, which puts a lien on the property to assure that the taxes are paid when the property is transferred. Thus, the program is essentially a loan to the eligible property owners by the state, to be repaid when the property is sold. Interest is charged on amounts deferred at 7 percent annually. The cost of this program to the state is the foregone interest due to the difference between this rate and the interest paid by the Pooled Money Investment Fund, which is currently 10.4 percent.

To be eligible for the program, persons must be 62 years of age or older, own and occupy the property, have an equity of 20 percent of full value and meet specified income limits. The income limits are adjusted annually to account for changes in the cost of living. To postpone taxes for the current year, a person must have had a household income of less than $26,800 in 1979. The income limit for the budget year will be determined in March 1981, and is estimated at $30,700. The program is now administered solely by the State Controller's Office. This Budget Bill item appropriates funds to the Controller from which the payments to local governments will be made.

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

The budget proposes $5.0 million from the General Fund for payments to local governments for reimbursement of postponed property taxes in 1981–82. This is $1.5 million (42.9 percent) more than the estimated current year expenditure. Table 1 summarizes the results of the program from 1978–79 through 1980–81.

SENIOR CITIZENS' PROPERTY TAX POSTPONEMENT—Continued

Table 1
Senior Citizens' Property Tax Postponement Program
Summary of Activity
1978–79 Through 1980–81

	Actual 1978–79	*Actual 1979–80*	*Estimated 1980–81* [a]
Certificates issued	8,573	7,654	8,100
Certificates used	7,054	6,175	7,100
Total appropriation	$10,000,000	$4,200,000	$3,500,000
Total amount postponed [b]	$2,856,560	$3,390,736	3,983,000
Average amount postponed	$405	$550	$561

[a] As of January 1981.
[b] Based on Controller workload data and will differ slightly from fiscal year expenditures shown in the budget.

Current Year Deficiency Anticipated

As shown in Table 1, total expenditures for the postponement program for 1979–80 were up almost 19 percent over 1978–79, despite the fact that the number of certificates *used* for those two years declined by 879. The increase in spending resulted from an increase in the average amount of taxes postponed by each claimant, from $405 to $550. Staff of the State Controller's Office are uncertain why this increase occurred. However, they believe that it may have resulted from a large number of first-time participants who, as opposed to persons renewing, may have higher claims because delinquent *prior year* property tax liabilities are included in the amount postponed.

Because the average amount postponed was underestimated during the budget process last year, there will be a deficiency in this item for the current year. The Controller's Office expects approximately 500 additional certificates to be issued for 1980–81. Based on these additional certificates and assuming a slight increase in the percentage of certificates *used* which the Controller anticipates, the shortfall should be about $700,000. The Controller's Office expects to request the additional funds in several months when it has better information about the amount required.

Assuming moderate growth in the number of certificates issued and the average amount per claim, our analysis indicates that the budget request is reasonable. If, as the Controller expects, 8,600 certificates (total) are issued for 1980–81, this is a 12.3 percent rate of growth over 1979–80. If comparable growth occurs for 1981–82 and the average amount per claim increases slightly (2 percent), this would result in budget year costs of just over $4.5 million. However, because the increase in the average amount paid could be greater in view of the past year's experience, we believe that this estimate is conservative. We will have better information concerning the average amount per claim at the time of budget hearings on this item.

Inflation Adjustment Unnecessary

We recommend that legislation be enacted repealing the inflation adjustment to the income limit for eligibility for the Senior Citizens' Property Tax Postponement program.

Existing law requires an annual inflation adjustment to be made to the income limit used to determine whether senior citizens are eligible to postpone payment of their property taxes. To postpone taxes in 1980–81, a person must have had a household income of $26,800 in 1979. For the budget year this limit is estimated at $30,700, a 14.5 percent increase over the current year. The Governor's Budget does not propose to limit this inflation adjustment to 4.75 percent, as is the case with most other statutorily required inflation adjustments.

We do not believe further adjustments in the income limit are warranted at this time. The postponement program is designed to enable senior citizens who do not have the sufficient cash to pay annual property taxes to defer those taxes until their house is sold. A $30,700 income limit, however, permits participation by senior citizens for whom payment of property taxes should not be difficult. Based on U.S. Bureau of Labor Statistics information, an income of $30,700 for a retired couple is equivalent to a $72,800 income for a family of four, in terms of a comparable living standard. We question whether continued inflation adjustments are appropriate in view of (1) the high income limit projected for the budget year, (2) the state's current fiscal situation, and (3) the Governor's proposals to limit cost of living adjustments for other programs to less than their statutorily required amounts.

For these reasons we recommend that the Legislature enact legislation which would repeal this inflation adjustment.

SENIOR CITIZEN RENTERS' TAX ASSISTANCE

Item 910-101(c) from the General Fund — Budget p. GG 166

Requested 1981–82	$51,500,000
Estimated 1980–81	51,500,000
Actual 1979–80	46,325,220
Requested increase None	
Total recommended reduction	None

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

	Analysis page
1. Senior Citizen Renters' Tax Assistance. Recommend Budget Bill language to permit more flexibility in the payment of claims in this program and the Senior Citizen Homeowners' Assistance program.	1628

GENERAL PROGRAM STATEMENT

This program provides tax relief to renters 62 years and over, and to totally disabled persons of any age, if their total household income is less than $12,000. Assistance varies inversely with income, and assumes that all renters pay the equivalent of $250 in property taxes. Actual assistance ranges from $240 (96 percent of $250) for persons with less than $3,000 of total household income, to $10 (4 percent of $250) for persons with income between $11,500 and $12,000. This assistance is in addition to the personal income tax credit provided all renters under Item 910-101(h).

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

The Governor's Budget proposes an appropriation of $51.5 million from the General Fund for the Senior Citizen Renters' Tax Assistance program in 1981–82. This amount is the same as estimated expenditures in the current year. Table 1 displays the participation and costs of the program from 1978–79 through 1980–81.

SENIOR CITIZEN RENTERS' TAX ASSISTANCE —Continued

Table 1
Senior Citizen Renters' Tax Assistance
1978–79 Through 1980–81 [a]

	Actual 1978–79	*Actual 1979–80*	*Preliminary 1980–81*
Number of claimants	79,253	268,336	286,225
Total assistance	$5,282,391	$46,325,220	$47,744,460
Average assistance	$67	$173	$167

[a] Based on Franchise Tax Board's workload data and therefore differs slightly from fiscal year amounts shown in the budget.

As shown in Table 1, participation in 1979–80 is significantly higher than it was in 1978–79. This is due to Chapter 569, Statutes of 1978, which (1) expanded eligibility to include totally diabled persons under 62, and (2) revised the reimbursement schedule by (a) increasing the annual household income limit from $5,000 to $12,000, (b) raising the reimbursement percentages, and (c) increasing the statutory property tax equivalent from $220 to $250.

Participation Slightly Above Expectations

Preliminary data from the Franchise Tax Board (FTB) indicate that actual participation in 1980–81 will be slightly higher than originally expected. Table 2 compares the claims paid to date (November 1980) for 1980–81 with the original estimates for the current year.

Table 2
Senior Citizen Renters' Tax Assistance Program
Comparison of Estimated and Actual Program Activity
1980–81

1980–81	*Number of Claimants*	*Total Assistance*
Budget estimates	280,700	$48,000,000
Preliminary actuals	286,225	$47,744,460

As shown in Table 2, costs for the 1980–81 program were originally estimated at $48 million. Preliminary amounts paid are still below that figure, despite the increase in the number of participants, because the average amount per participant has declined from $173 for 1979–80 to $167 for 1980–81.

The Franchise Tax Board expects participation for the current year to total 300,000, of which 76,000 will be disabled persons and 224,000 will be nondisabled persons. This will bring the 1980–81 cost of the program to $50.1 million, or $1.4 million less than the amount estimated in the budget.

The budget request reflects the uncertainty over future participation in this program. FTB anticipates a slight decline in participation by nondisabled seniors in 1981–82. Participation, particularly by the disabled, may be low due to the fact that the program is relatively new and unknown. Therefore, increased awareness could result in increased participation. The budget provides for about 7 percent growth in the program from the current year to 1981–82. On the basis of the information currently available, we believe that the budget request is reasonable.

Control Language

We recommend Budget Bill language be adopted to permit more flexibility in the payment of claims in this program and the Senior Citizen Homeowners' Assistance program.

Because there is some uncertainty concerning the level of participation in both this program and the Senior Citizen Homeowners program in the budget year, we believe that the Franchise Tax Board should be permitted greater flexibility in the payment of claims. This would allow any deficit in one program to be made up with the surplus from the other. Therefore, we recommend that the following language be included in this item:

"Provided that any unexpended balance in this item may be used to make payments to senior citizen homeowner claimants under Item 910-101-001(a)."

PERSONAL PROPERTY TAX RELIEF

Item 910–101(d) from the General Fund — Budget p. GG 167

Requested 1981–82	$493,219,563
Estimated 1980–81	495,675,000
Actual 1979–80	224,401,936
Requested decrease $2,455,437 (−0.5 percent)	
Total recommended reduction	None

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. We recommend that the Legislature direct the Controller to audit claims for 1980–81 business inventory exemption reimbursements. 1629
2. We recommend that the Legislature delay action on this item until any statutory changes affecting the business inventory exemption reimbursement have been made. 1632

GENERAL PROGRAM STATEMENT

The Personal Property Tax Relief program currently reimburses local governments for the property tax revenue losses resulting from the complete exemption granted to owners of business inventories. Local governments are also reimbursed under this program for revenue losses due to the complete exemption of livestock head-day taxes and special provisions for assessing motion picture films and baled cotton.

Chapter 1150, Statutes of 1979 (AB 66), increased the business inventory exemption to 100 percent beginning in 1980–81, and provided for the reimbursement of local property tax revenue losses on a formula basis. Generally, the formula fixed the reimbursements at twice the 1979–80 amounts, and requires increases in the reimbursements for future years based on increases in the cost of living and population.

ANALYSIS AND RECOMMENDATIONS

We recommend that the Legislature direct the Controller to audit claims for the 1980–81 business inventory exemption reimbursements.

The budget requests an appropriation of $493.2 million for 1981–82 personal property tax relief, primarily for reimbursements for the business inventory exemption. This is a 0.5 percent decrease from the amount for the current year as estimated in the budget. The budget request reflects the effect of two legislative proposals supported by the administration. The first would reduce the cost-of-living adjustment for this item. The second would reduce business inventory exemption reimbursements in order to capture a portion of the 1978–79 unsecured property taxes collected by local agencies. These proposals are discussed below.

PERSONAL PROPERTY TAX RELIEF—Continued

Current Year Deficiency Anticipated

Table 1 displays costs for this item for the years from 1979–80 through 1981–82, as estimated in the budget. (We have adjusted the amounts shown for 1981–82 to reflect the effect of the cost of living and unsecured property tax proposals discussed below.) The estimate of $495.7 million for 1980–81 represents a 121 percent increase over 1979–80 costs due to the complete exemption of business inventories from property taxation.

Table 1
Personal Property Tax Relief
Summary of Expenditures
1979–80 Through 1981–82
(in thousands)

	Actual 1979–80	*Estimated 1980–81*	*Proposed 1981–82*	*Percent Change*
Business inventory exemption	$221,302	$491,021	$488,393	−0.5%
Motion picture films	1,066	1,009	1,009	—
Livestock head-day tax exemption	2,034	3,645	3,818	4.75
Totals	$244,402	$495,675	$493,220	−0.5%

The Controller, however, reports that claims for the business inventory and livestock head-day tax exemption for the current year total $501.4 million. This amount, plus an amount for the motion picture film reimbursements paid under this item, means that the total 1980–81 cost ($502.4 million) will be $9 million more than the $493.4 million appropriated for this year.

Chapter 1150, Statutes of 1979 (AB 66), provided for the complete exemption of business inventories and specified that the reimbursement of the local property tax revenue loss resulting from this exemption was to be made on a formula basis. Reimbursements for 1980–81 are to be computed by doubling the reimbursement in 1979–80 that was attributable to the $4 local tax rate, and then increasing the amount by the appropriate "inventory tax factor" for each jurisdiction. For cities, counties, and special districts, this factor is the percent change in the cost of living plus the percent change in the population of the jurisdiction. For schools, the factor is the percent change in the cost of living plus the percent change in average daily attendance (ADA) of the school or community college district.

At the time of budget hearings on this item last year, we estimated the aggregate statewide inventory tax factor to be approximately 19 percent. Using information reported to the Board of Equalization concerning the amount of business inventory assessed value for 1979–80, the total estimated reimbursements required for the inventory and livestock exemptions for 1980–81 comes to $485 million, as compared to the $501.4 million claimed. Claims reported by the Controller for the current year would, on this basis, require a statewide inventory tax factor of 23 percent. One possible explanation for this discrepancy is the fact that the information reported to the Board of Equalization represents the assessed value of business inventory *before* adjustments have been made for property tax roll corrections for escape assessments and assessor errors.

Because of the magnitude of this discrepancy and the amount involved, we believe that the Controller should audit 1980–81 business inventory exemption reimbursement claims. Therefore, we recommend that the Legislature direct the Controller to audit these claims by adopting the following supplemental report language:

"It is the intent of the Legislature that the Controller audit local agency claims for the 1980–81 business inventory exemption reimbursements."

Change in Reimbursement Formula

Chapter 610, Statutes of 1980 (AB 1994), modified the computation of inventory reimbursements beginning with the 1981–82 fiscal year. The act specifies that for 1981–82 and future years, the sum of the 1980–81 reimbursements for all jurisdictions in each county is to be increased by the *county* inventory tax factor. The resulting amount is then to be distributed to local agencies in proportion to property tax revenues. Thus, separate factors for different types of jurisdictions will no longer be used.

Chapter 610 made a number of other changes in existing law. Specifically, it:

- Reduced the state reimbursement for the 100 percent livestock head-day tax exemption for 1980–81 from 200 percent of the 1979–80 reimbursement to 170 percent of that amount (plus an adjustment for the inventory tax factor).
- Provided for local redevelopment agencies to receive a portion of the business inventory exemption reimbursements. This does not increase the overall cost of the reimbursement because the redevelopment agency shares come from other local agencies. There is an increase in state school funding costs, however, to replace funds shifted from schools to redevelopment agencies.
- Defined certain aircraft as inventory subject to the 100 percent exemption. Reimbursements to account for this change were also provided.
- Provided a state reimbursement for the exemption of baled cotton from property taxation.

Reduction for 1978–79 Unsecured Tax Levy Collections

The Governor's Budget proposes that the business inventory exemption reimbursements be reduced so as to, in effect, redirect to the state a portion of the 1978–79 unsecured property tax levies collected by cities, counties and special districts. This proposal is discussed in detail in the A-pages of this Analysis.

In August 1980, the California Supreme Court ruled that Proposition 13's tax rate limitation does not apply to the tax rate used for the 1978–79 unsecured tax roll. Thus, the use of higher pre-Proposition 13 tax rates is required in taxing this property for 1978–79. Chapter 1354, Statutes of 1980 (AB 2169), imposed a "freeze" on the collection of the additional taxes in the 36 counties which applied the Proposition 13 tax rate to the unsecured roll.

The budget proposes to permit local agencies and schools to collect the additional taxes when the freeze expires on July 1, 1981. The budget, however, also proposes to capture $26 million of the unsecured taxes collected by cities, counties, and special districts by reducing the personal property tax relief payments by the amount collected up to $26 million. An additional $209 million would be recovered by reducing the homeowner's exemption reimbursements.

There is some question as to whether the homeowners' exemption reimbursements can legally be reduced to capture unsecured taxes. If they cannot be reduced, the entire reduction could possibly be taken from the business inventory reimbursements to local agencies. The budget proposes to make these reductions in proportion to the amount of unsecured taxes collected by each local agency. It is not necessarily the case, however, that *individual* local agencies will receive sufficient inventory exemption reimbursements to offset the amount of unsecured taxes they would collect.

PERSONAL PROPERTY TAX RELIEF—Continued

Cost-of-Living Adjustment

The $493.2 million requested in the budget also reflects a special adjustment in the cost-of-living factor used for the business inventory and livestock head-day tax reimbursements. The budget proposes to increase 1980–81 reimbursements for these exemptions by 4.75 percent, rather than by 13.1 percent as existing law requires. Thus, the budget request reflects the effect of two factors: (1) a reduction of $26 million to recover a portion of 1978–79 unsecured taxes collected by local agencies, and (2) a cost-of-living increase of $23.5 million (4.75 percent).

In the A-pages of this Analysis, we discuss the general issue of providing a 1981–82 statutory or discretionary inflation adjustment. Whatever final decision that is made by the Legislature on this issue should be applied to all programs that warrant an inflation adjustment. For the personal property tax relief reimbursements each 1 percent cost-of-living adjustment would increase General Fund expenditures by $5.0 million.

Because the budget proposals concerning the capture of unsecured taxes and cost-of-living adjustments would significantly affect expenditures under this item, we believe that the amount to be appropriated should reflect these changes if they are made.

Budget Year Requirements Uncertain

We recommend that the Legislature delay action on this item until any statutory changes affecting the business inventory reimbursement have been made.

We estimate the cost of the business inventory exemption reimbursement in 1981–82, under current law, would be $563.6 million. This is based on: (1) an estimated 13.1 percent adjustment for the changes in the cost of living (11.1 percent) and *county* population (2.0 percent), as required by Chapter 610, and (2) the current year estimate of $501.9 million (including aircraft inventory). (The budget mistakenly shows the statutory cost of living adjustment as 16.6 percent.) Table 2 displays the estimated 1981–82 current law cost for all of the property tax reimbursements paid under this item. Chapter 610 provides for the reimbursement of the baled cotton exemption. Claims totaling $1,132,852 have been filed for 1980–81. We have included an amount to reimburse this exemption in our estimate of 1981–82 costs.

Table 2
Estimated Current Law Cost for Personal Property Tax Relief
1981–82
(in thousands)

	Estimated Cost
Business inventory exemption	$563,560
Livestock head-day tax	4,122
Motion pictures	1,009
Baled cotton	1,281
Total	$569,972

HOMEOWNERS' PROPERTY TAX RELIEF

Item 910-101 (e) from the General Fund — Budget p. GG 167

Requested 1981–82	$126,000,000
Estimated 1980–81	332,000,000
Actual 1979–80	328,218,256
Requested decrease $206,000,000 (−62.0 percent)	
Total recommended reduction	None

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. We recommend that the Legislature direct the Department of Finance to comment on the legal and technical feasibility of reducing homeowners' property tax exemption reimbursements. 1633

GENERAL PROGRAM STATEMENT

The homeowners' property tax exemption is $7,000 of the full value of an owner-occupied dwelling. For the budget year, this exemption will provide almost 4.2 million homeowners with an estimated average property tax reduction of $80. The state reimburses local government for all revenue losses resulting from the exemption.

ANALYSIS AND RECOMMENDATIONS

We recommend that the Legislature direct the Department of Finance to comment on the legal and technical feasibility of reducing homeowners' property tax exemption reimbursements.

The Governor's Budget requests $126 million for the Homeowners' Property Tax Exemption Program in 1981–82. This is a 62 percent decrease from the current year expenditure of $332 million, as estimated in the budget. This amount reflects the effect of the budget proposal to redirect to the state a portion of the unsecured property taxes collected by local agencies for 1978–79 by reducing the homeowners' exemption reimbursement by $209 million. This proposal is discussed in detail in the A-pages of this *Analysis*, and to a more limited extent below.

Table 1 summarizes the number of claims, exempt assessed value, and our estimate of expenditures related to the Homeowners' Property Tax Exemption program.

Table 1
Homeowners' Property Tax Exemption
Summary of 1979–80 to 1981–82 Expenditures [a]

	Actual 1979–80	*Estimated 1980–81*	*Estimated 1981–82*	*Percent Change*
Claimants (thousands)	4,015	4,107	4,189	2.0%
Exempt Assessed Value (millions)	$28,024	$28,676	$29,323	2.3
Per Claimant Averages				
Exempt assessed value	$6,980	$6,982	$7,000	0.3
Tax benefit	82	81	80	−1.2
Full Value Property Tax Rates	$1.17	$1.16	$1.14	−1.7
Expenditure (millions)	$328.2	$333.6	$335.0	0.4

[a] Beginning with 1981–82, property will be assessed for tax purposes at 100, rather than 25, percent of its full value. The figures for 1979–80 and 1980–81 have been modified to facilitate comparison with 1981–82. Tax rates have been adjusted as well.

HOMEOWNERS' PROPERTY TAX RELIEF—Continued

As the table indicates, the budget estimates that current year costs under this program will be $332 million. The Controller, however, reports that claims for $333.6 million for 1980–81 have already been filed, which is $3.4 million less than the $337 million *appropriated* for 1980–81. The amount claimed indicates that the effective tax rate was $1.16 ($4.64 on a 25 percent assessment ratio basis), which represents a slight decline from 1979–80 in the rate levied for the purpose of retiring voter-approved debt.

Because the homeowners' exemption is fixed at $7,000 of full value, state costs for this program are not affected by changes in *property values* or the limits on assessed value growth set by Proposition 13. State costs depend only on the *number of homeowners* and the *level of tax rates* applicable to owner-occupied property. The Controller's figure of $333.6 million for the current year is $5.4 million, or 1.6 percent, higher than the actual amount reimbursed in 1979–80. Thus, the savings due to the decline in the tax rate was more than offset by the 2.3 percent increase in the number of claimants.

Our estimate of $335 million for 1981–82 represents a 2 percent increase in the number of claimants. This is consistent with growth in this program for the last several years. It is anticipated that this growth will be partially offset by a slight decline in the tax rate levied for voter-approved debt, from $1.16 to $1.14.

Reduction for 1978–79 Unsecured Tax Levy Collections

The Governor's Budget proposes that the Homeowners' Property Tax program be reduced to, in effect, redirect to the state a portion of the 1978–79 unsecured property tax levies collected by cities, counties and special districts. This proposal is discussed in detail in the A-pages of this Analysis.

In August 1980, the California Supreme Court ruled that Proposition 13's tax rate limitation does not apply to the tax rate used for levying taxes on the 1978–79 unsecured tax roll. Thus, the use of higher pre-Proposition 13 tax rates is required for taxing this property for 1978–79. Chapter 1354, Statutes of 1980 (AB 2169), imposed a "freeze" on the collection of the additional taxes in the 36 counties which applied the Proposition 13 tax rate to the unsecured roll.

The budget proposes to permit local agencies and schools to collect the additional taxes when the freeze expires on July 1, 1981. The budget, however, also proposes to offset $209 million of the unsecured taxes collected by cities, counties, and special districts by reducing the homeowners' exemption reimbursement by the amount collected up to $209 million. (An additional $26 million would be recovered by reducing the personal property tax relief payments.)

There are a number of problems associated with this proposal. First, the California Constitution (Article XIII, Section 25) requires the state to provide local agencies with reimbursement for the homeowners' exemption *in the same fiscal year* in which the revenue loss occurs. Thus, it is not clear that, legally, the state could reduce the homeowners' exemption reimbursement by any amount.

Second, it may not be possible to recover $209 million from local agencies by using the homeowners' exemption. The reductions would be made in proportion to the amount of unsecured taxes collected by each agency. We estimate that cities, counties, and special districts will receive no more than $200 million, or about 60 percent, of the total $335 million homeowners' exemption reimbursement estimated for 1981–82. Moreover, it is not necessarily the case that *individual* agencies will receive sufficient homeowners' reimbursements to offset the amount of unsecured taxes they collect.

Legislation has been proposed to reduce reimbursements to cities, counties, and special districts in the manner proposed in the budget. We recommend that the

Legislature direct the Department of Finance to comment during budget hearings on the legal and technical feasibility of reducing homeowners' property tax exemption reimbursements.

OPEN-SPACE PAYMENTS TO LOCAL GOVERNMENTS

Items 910-101 (f) from the General Fund — Budget p. GG 167

Requested 1981–82	$14,000,000
Estimated 1980–81	14,000,000
Actual 1979–80	13,214,634
Requested increase None	
Total recommended reduction	None

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. We recommend that the Legislature amend the Williamson Act to (1) limit application of the act to those lands actually threatened by development and (2) permit the state the opportunity of providing input into local decisions concerning cancellation of open space contracts. 1637

GENERAL PROGRAM STATEMENT

The Constitution authorizes the Legislature to provide for the assessment of land at less than market value if it is under enforceable restrictions. Under the California Land Conservation Act of 1965 (the Williamson Act) and related open space laws, cities and counties may enter into contracts with landowners to restrict the use of property to open space and agricultural use. In return for restricting the use of the property, the land is assessed at less than market value, thereby lowering the landowner's cost for holding the property as open space.

Open space subventions provide replacement revenues to cities and counties to compensate for reduced property tax revenues on open space and agricultural land.

The Secretary of the Resources Agency, through the Department of Conservation, administers subventions to cities and counties.

ANALYSIS AND RECOMMENDATIONS

We recommend approval

Section 16140 of the Government Code appropriates General Fund money for open space subventions to counties and cities. However, Budget Act appropriations have superseded the statutory appropriation since the subventions began in 1972.

The budget requests $14 million for subventions to the 48 counties and 21 cities which are expected to have a total of about 16 million acres under Williamson Act contracts during 1981–82. The subvention for cities and counties is determined by a formula which bases the amount of money provided for each acre of land under contract on the type of land and its location. For this purpose, land is classified as "prime" or "nonprime". "Prime" agricultural land is defined as land rated as class I or II in the Soil and Conservation Service land use capability classification, or other comparable classification.

Method of Valuing Open-Space Land Revised

Immediately after the passage of Proposition 13, the Board of Equalization ruled that land under open space contracts was to be assessed according to the initiative's assessment rules. That is, land under contract that had not undergone a transfer of ownership was to be assessed according to its *1975* capitalized income (restricted) value, with the 2 percent inflation factor applied for each year after 1978–79. The capitalized income valuation technique represents an attempt to value the land according to the income it will produce when used for agriculture (or other open space use) rather than according to the price that a buyer is willing to pay to acquire the land for development purposes.

Chapter 242, Statutes of 1979 (AB 1488), reversed the board's rule by declaring that land under contract is to be valued on a *current* capitalized income basis. After the enactment of Chapter 242, a number of instances were discovered where the land valued under its provisions had been assessed at a value equal to or greater than the unrestricted value under Proposition 13. Consequently, the Legislature enacted Chapter 1075, Statutes of 1979 (AB 501) and Chapter 1273, Statutes of 1980 (AB 2298). Chapter 1075 provides that, unless the county or landowner objects, the assessed value of land under an open space contract shall not be greater than the unrestricted assessed value under Proposition 13. The statute also specifies that payment of the state subvention shall be made only when the land's restricted value is less than its unrestricted Proposition 13 value. Chapter 1273 allows local authorities to lower the assessed value of land under a Williamson Act contract so that it does not exceed a specified percentage of the land's unrestricted Proposition 13 value. The chapter specifies a maximum reduction which ranges between 20 and 30 percent, depending on the type of land and its location.

Impact of Proposition 13

Our analysis indicates that Proposition 13 has had a significant impact on the effectiveness of this program. In particular, the initiative has reduced the value of the tax break resulting from the application of restricted use valuation techniques. This is because the difference in the *value* at which the properties are assessed has been reduced, as has the *tax rate* applied to those values. Whereas prior to passage of Proposition 13, lands not under contract were experiencing rapid increases in value for tax purposes, these lands can now increase in value by no more than 2 percent per year (assuming no change in ownership). Lands under contract, however, are valued on a *current* capitalized income basis, so that if the *income* which can potentially be generated by the property increases, the property value for tax purposes increases correspondingly. This is particularly the case for certain high value crops grown on prime lands. For many of these parcels, the restricted value actually equals or exceeds the unrestricted Proposition 13 value. In these cases, participation in the Williamson Act may actually increase the owner's tax liability. In any event, it appears that the more valuable agricultural lands are likely to be receiving a lower level of tax relief over time. This may be reversed if county supervisors allow the reduced assessments provided by Chapter 1273, but even this may not be a sufficient inducement for a landowner to forego other options for the required 10 year period. In fact, a number of county assessors contacted by our office stated that the reduction in the value of the tax break is resulting in a significant increase in the number of contract holders seeking to terminate their contracts in the current year.

Amendments to Existing Law

We recommend that the Legislature amend the California Land Conservation Act (Williamson Act) to (1) limit the application of the act to those lands actually threatened by development and (2) permit the state an opportunity to provide input into local decisions concerning the cancellation of open space contracts.

Under the provisions of the Williamson Act, local governments are authorized to place specified parcels of land under contract and provide a property tax reduction to the property owner. The law further empowers local governments to cancel such a contract for specified reasons. The criteria governing these two procedures, however, are fairly broad and, as a result, fail to significantly restrict or guide these local decisions. Consequently, due to the economic forces working on local government, the decisions these governments make are often contrary to statewide interests concerning the use of agricultural and open space lands.

Land Not Threatened by Development. Table 4 shows those acres of land under open space contract for the 1979–80 fiscal year, by type of government and type of land.

Table 4
Actual Open Space Acreage Under Contract in Counties and Cities for 1979–80

	Urban Prime Land	*Other Prime Land*	*Nonprime Land*	*Total Acreage*
Counties	558,501	4,454,412	11,130,147	16,143,060
Cities	8,810	731	26,816	36,357
Totals	567,311	4,455,143	11,156,963	16,179,417

According to the table, approximately 89 percent of the "prime" land is located outside of urban areas. In addition, we estimate that as much as 80 percent of the nonprime land is also located outside of urban areas, and is presumably not threatened by development. Reimbursement for these unthreatened lands amounts to approximately \$3.6 million of the \$14 million subvention request. Our analysis indicates that this is probably not an effective use of state funds.

The criteria defining lands eligible for open-space contracts are the only input the state has into local open-space decisions. Thus, the lack of specificity in these criterion significantly reduces the influence of statewide considerations on local decision makers. Consequently, strengthening these standards would afford the state greater influence over the conversion of open space lands and the expenditure of state funds.

Therefore, we recommend that the Legislature enact amendments to the California Land Conservation Act (Williamson Act) which redefine the existing criteria delineating the types of land qualifying for protection so as to limit the application of the act to only those lands actually threatened by development.

State Input. Current law allows local governments, upon the request of a landowner, to cancel an open space contract. Upon the approval of the local government, a cancellation terminates the contract and eliminates the property tax reduction and the corresponding state subvention. The state has limited involvement in cancellation procedures, and often learns of a cancellation when an owner applies for a waiver of the prescribed cancellation penalty (the law requires payment to the state of a substantial cancellation penalty) or when the local government files its subvention request.

The statutes governing cancellations are fairly specific in detailing those reasons for which cancellations are justified. Local governments, however, often have cancelled contracts protecting lands vital to the state's agricultural economy and interests. The state Department of Conservation, in its review of requests for

OPEN-SPACE PAYMENTS TO LOCAL GOVERNMENTS—Continued

waiver of the cancellation penalties, has discovered numerous cancellations which fail to meet the statutory criteria. The department has considered contesting some of these cancellations in the courts, and has succeeded in at least one instance in acquiring a judgment against the local government. This overturned the cancellation and reestablished the open space contract.

While the department may enjoy some success through legal avenues, the process is costly and can leave the landowner uncertain as to the fate of his property for an extended period of time. A more appropriate alternative would be to allow the Department of Conservation to provide input, when warranted, into the initial cancellation decision. This action might reduce, if not eliminate, the need for legal action, and could be geared to allow the department to have some input in all cancellation hearings. Requiring the landowner to file with the state when he initially applies for cancellation would provide the needed information without increasing local expenses. The state could then be apprised of all proposed cancellations and would be able to present testimony when warranted.

Consequently, we recommend that the Legislature enact amendments to the California Land Conservation Act (Williamson Act) requiring every contract holder seeking cancellation of his contract to notify the state Department of Conservation of his intent when the initial request for cancellation is filed.

PAYMENTS TO LOCAL GOVERNMENTS FOR SALES AND PROPERTY TAX REVENUE LOSS

Items 910-101(g) from the General Fund — Budget p. GG 167

Requested 1981–82	$3,350,700
Estimated 1980–81	2,960,100
Actual 1979–80	2,477,500
Requested increase $490,600 (+13.2 percent)	
Total recommended reduction	$186,670

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS	Analysis page
1. *Certificated Aircraft. Reduce Item 910-101-001(g) by $179,000.* Recommend reduction due to overestimate of reimbursement for certificated aircraft exemption.	1640
2. Documented Fishing Vessels. Recommend that the Legislature direct the Department of Finance to comment on the underestimate of costs for documented fishing vessel exemption. Also recommend legislation to conform exemption to change in assessment ratio.	1640
3. *Sales Tax Reimbursements. Reduce Item 910-101-001(g) by $7,670.* Recommend reduction to adjust for inconsistent reimbursement of sales tax revenue losses.	1641
4. Veterans' Property Tax Exemption. Recommend that the Legislature direct the Controller to audit claims for reimbursement. Also recommend that the Legislature direct the Controller to require a breakdown of county claims by statute.	1641
5. Property Tax Exemption Statutes. Recommend that the Legislature direct Department of Finance to propose funding for three statutes.	1643

GENERAL PROGRAM STATEMENT

Chapter 1406, Statutes of 1972, as amended by Chapter 1135, Statutes of 1977, requires the state to reimburse local government for the net loss resulting from sales or property tax exemptions enacted after January 1, 1973. The budget identifies 14 statutes which have ongoing funding requirements and thus necessitate annual Budget Act appropriations. All of the statutes are funded from this single budget item. This allows the State Controller flexibility to cover deficits resulting from some statutes with surplus funds for others.

ANALYSIS AND RECOMMENDATIONS

The budget estimates that required reimbursements in 1981–82 will be $390,600, or slightly over 13 percent, higher than those estimated for the current year.

The amounts budgeted for the following statutes in 1981–82 appear appropriate, and we recommend that they be approved.

	Estimated 1980–81	*Requested 1981–82*
Chapter 1165, Statutes of 1973	$30,000	$48,400

This statute requires the lands governed under a wildlife habitat contract shall be valued on a restricted basis similar to the method of valuing open space lands.

	Estimated 1980–81	*Requested 1981–82*
Chapter 928, Statutes of 1979	$5,000	$5,000

This measure exempts the intangile value of business records, including the information they contain or the value of their use. Title records are an example of documents having intangible value which became exempt from taxation under this statute.

	Estimated 1980–81	*Requested 1981–82*
Chapter 1077, Statutes of 1980	$1,000,000	$407,000

This statute exempts from sales taxes the sale or use of gasohol which is motor vehicle fuel composed of a blend of gasoline and alcohol.

The budget requests an appropriation for reimbursements under this statute for 1981–82 which is substantially less than the amount appropriated by the act in 1980. This reflects the fact that the amount appropriated by that statute was based on an estimate of the sales tax revenue loss associated with an earlier version of the bill than was actually enacted. The amount requested for the budget year reflects the appropriate reimbursement.

	Estimated 1980–81	*Requested 1981–82*
Chapter 1348, Statutes of 1980	$940,000	$900,000

This statute exempts from sales taxes the sale or use of noncarbonated and noneffervescent bottled water.

The budget requests $900,000 to reimburse local agencies for the revenue loss caused by this act in 1981–82. This amount is 4 percent less than the amount appropriated by the act for the loss during the first year in which it was effective. This reduction reflects the fact that the amount appropriated by Chapter 1348 was based on an estimate of the revenue loss resulting from an earlier version of the

PAYMENTS TO LOCAL GOVERNMENTS FOR SALES AND PROPERTY TAX REVENUE LOSS—Continued

bill than was finally enacted. The amount requested in the budget year reflects the apropriate reimbursement.

Overestimate for Aircraft Reimbursment

We recommend a reduction of $179,000, due to an overestimate in the reimbursement for certificated aircraft.

	Estimated 1980–81	*Requested 1981–82*
Chapter 610, Statutes of 1980	$41,219	$226,000

This statute excludes from the computation of certificated aircraft (commercial aircraft) assessed value any time spent in California prior to the aircraft's first revenue flight. As of January 1981, the Controller reported that claims totalling $41,217 had been filed for this statute. Current law requires the 1981–82 reimbursement for this statute to be computed on a formula basis. The 1980–81 amount for *all* jurisdictions in ech county is to be increased by the change in *county* population and the cost of living for 1981–82. This adjustment is 13.1 percent. Accordingly, an appropriation of $47,000 is adequate for this statute for the budget year. It should be noted that, unlike most programs with cost-of-living adjustments, the budget does not propose to reduce the adjustment for this statute.

Change in Assessment Ratio Should Be Reflected

We recommend that legislation be enacted to conform the commercial fishing vessel exemption to the change in the assessment ratio which will take place beginning in 1981–82. We also recommend that the Legislature direct the Department of Finance to comment on the underestimate of costs for this statute.

	Estimated 1980–81	*Requested 1981–82*
Chapter 18, Statutes of 1980	$275,000	$300,000

This statute provides that documented commercial fishing vessels (including sport fishing vessels) are to be assessed at 1 percent, rather than 25 percent, of full cash value. Reimbursements for this statute are exclusively related to the revenue loss resulting from the reduced assessment of sport fishing vessels.

Up to and including the 1980–81 fiscal year, property has been assessed for tax purposes at 25 percent of full value. Beginning in 1981–82, property will be assessed at 100 percent of full value, but property tax *rates* will be adjusted to keep tax liability at the same level. In order to maintain comparability between commercial fishing vessels and other property, we recommend that legislation be enacted to provide that beginning in 1981–82, fishing vessels shall be assessed at 4 percent of full value. If legislation conforming this exemption to the change in the assessment ratio is not made, the cost of this reimbursement will be increased fourfold.

As of January 1981, the Controller reported that claims totalling $354,000 had been paid for this statute. They were unable to explain the significant increase over the amount for 1979–80. On the basis this estimate, however, we recommend that the Legislature direct the Department of Finance to comment on the apparent shortfall in the budget request, and if additional funding is required, to submit a budget amendment letter.

Increases in Sales Tax Loss Reimbursements Should be Consistent

We recommend that Item 910-101-001 (g) be reduced by $7,670 to adjust for the inconsistent increases in reimbursements for four statutes which result in local sales tax revenue losses.

Estimated current year costs and amounts requested for 1981–82 for these statutes are shown as displayed in the Governor's Budget.

	Estimated 1980–81	*Requested 1981–82*
Chapter 765, Statutes of 1979	$2,200	$2,500

This act exempts from sales taxes goods sold by certain nonprofit library associations which perform services for public libraries.

	Estimated 1980–81	*Requested 1981–82*
Chapter 1048, Statutes of 1979	$13,100	$14,000

This statute exempts from sales taxes meals served to residents of senior citizens' boarding homes.

	Estimated 1980–81	*Requested 1981–82*
Chapter 645, Statutes of 1980	$7,000	$17,800

This statute exempts from sales taxes meals for elderly persons residing in a condominium.

	Estimated 1980–81	*Requested 1981–82*
Chapter 1246, Statutes of 1980	$100,000	$235,000

This statute partially exempts factory-built housing from the sales tax.

Section 2230 of the Revenue and Taxation Code provides that funds shall be provided in the budget to reimburse local agencies for sales tax losses. That section states that the amount in the budget shall be increase each year by the estimated percentage change from the prior year in total local sales tax revenues distributed to local agencies. For the 1981–82 fiscal year, that percentage change is estimated to be 14.1 percent. The amounts requested in the budget for these four statutes for 1981–82, however, is $269,300, which is a 17.4 percent increase over the amounts estimated for the current year. (The amount shown for Chapters 645 and 1246, Statutes of 1980, for the current year are partial-year amounts, covering only the first six months' revenue loss.) Consequently, we recommend a reduction of $7,760 in the amount requested for these statutes.

Current Year Deficiency Anticipated

We recommend that the Legislature direct the Controller to identify the amount claimed for each of the veterans' exemption statutes separately. We also recommend that the Legislature direct the Controller to audit claims for these statutes.

The following four statutes extended the provisions of the veterans' property tax exemption. Estimated current-year costs and amounts requested for 1981–82 for these statutes, as displayed in the Governor's Budget, are shown.

	Estimated 1980–81	*Requested 1981–82*
Chapter 16, Statutes of 1973	$78,000	$90,000

This measure increased the property tax exemption for blind veterans residing

PAYMENTS TO LOCAL GOVERNMENTS FOR SALES AND PROPERTY TAX REVENUE LOSS—Continued

in corporate-owned residences from $5,000 to $10,000 of assessed value.

	Estimated 1980–81	*Requested 1981–82*
Chapter 961, Statutes of 1977	$200,000	$230,000

This statute extends disabled veterans' property tax exemption benefits to the unmarried surviving spouses of disabled veterans who died prior to January 1, 1977, but who would have been eligible for the exemption under laws in effect on that date.

	Estimated 1980–81	*Requested 1981–82*
Chapter 1273, Statutes of 1978	$152,000	$175,000

This measure extends disabled veterans' benefits to disabled veterans and their unmarried surviving spouses if the veteran's disability is the result of a disease incurred during miliary service.

	Estimated 1980–81	*Requested 1981–82*
Chapter 1276, Statutes of 1978	$610,125	$700,000

This statute increases from $10,000 to $15,000 of assessed value the property tax exemption for disabled veterans, and their surviving spouses, whose income satisfies the criteria for the Senior Citizens' Property Tax Postponement program.

The 1980–81 Budget Bill appropriated $570,000 for these four statutes for the current year. As of January 1981, however, the Controller reported that claims for $1,040,125 had been filed, 82 percent more than the amount estimated for the current year. Primarily because of the increase in claims submitted under these statutes, the Controller anticipates a deficiency of about $530,000 in this item for the current year. This amount is not included in the administration's summary of proposed deficiency appropriations (Budget page GG 203).

During the 1980–81 budget process, the Legislature adopted supplemental language which directed the Controller to require counties to report the amounts claimed for each of these four statutes separately. The Controller, however, failed to direct counties to do so. Consequently, it is not possible to determine which of these statutes is responsible for the increase in costs for the current year. (The current year amounts shown above are simply estimates based on prior year amounts.)

We do not have sufficient information to determine what caused the unanticipated increase in claims for these statutes for 1980–81. We believe, however, that there is significant potential for confusion over the amount of property tax revenue loss that is *reimbursable* under these statutes. For this reason, we believe that for the Controller should audit local agency claims for these statutes for 1979–80 and 1980–81. Accordingly, we recommend that the Legislature direct the Controller to audit these claims and require counties to identify the amount claimed for each of these statutes separately by adopting the following supplemental report language:

"It is the intent of the Legislature that the Controller audit claims for the veterans' property tax exemption statutes for the 1979–80 and 1980–81 fiscal years, and that the Controller require counties to identify the amount of reimbursement claimed by statute.

Funding for Three Statutes Not Provided

We recommend that the Legislature direct the Department of Finance to propose funding for three property tax exemption statutes for which claims for reimbursement have been filed.

The budget fails to request funding for three property tax exemption statutes for which claims for reimbursement have been filed with the Controller.

Chapter 866, Statutes of 1978, exempts from property taxation church parking lots owned by a governmental agency. The Controller reports that claims totalling $3,636 have been filed for this statute for the current year. Chapter 588, Statutes of 1979, exempts personal property owned or used by a nonprofit student bookstore. The Controller reports that claims for $1,054,874 have been filed for the current year. Chapter 172, Statutes of 1980, adjusts the amounts paid for late-filed claims for the veterans' property tax exemption. Claims filed for the current year for this statute total $16,646.

Each of these statutes required the Controller to report to the Legislature concerning the amount of claims filed so that funds could be provided for reimbursement of revenues lost. Ordinarily, the Controller notifies the Department of Finance that funds will be required during the current year to cover reimbursements. Funding for future fiscal years is then requested in the budget. The Controller apparently failed to notify the department of the claims that have been filed. Therefore, we recommend that the Legislature direct the department to propose funding to reimburse these property tax exemption statutes.

RENTERS' TAX RELIEF

Item 910-101(h) from the General Fund — Budget p. GG 168

Requested 1981–82	$425,000,000
Estimated 1980–81	405,000,000
Actual 1979–80	357,526,234
Requested increase $20,000,000 (+ 4.9 percent)	
Total recommended reduction	None

GENERAL PROGRAM STATEMENT

The Renters' Tax Relief program provides a flat payment to qualified renters without regard to age or income. Qualified renters include persons who (1) are residents of California and (2) rented and occupied a dwelling in California as their principal residence on March 1. Married persons are generally entitled to one credit. The renters' credit is not available to persons who (1) rent property that is exempt from property taxes, (2) are claimed as a dependent for income tax purposes by persons with whom they are living, or (3) receive the homeowners' property tax exemption. A partial credit is available for persons with less than 12 months' residence. The program is administered through the Personal Income Tax program as a refundable credit. That is, the credit is applied first to any income taxes due, with the balance refunded to the renter. Persons with no income tax liability must file a return to receive the tax relief payment.

Chapter 1207, Statutes of 1979 (AB 1151), increased the amount of the renters' credit, beginning with the 1979 income year, from $37 per renter to $60 for single renters and $137 for married couples, heads of households, and surviving spouses. The act also made changes in the allocation of the credit to married couples living separately and persons who are nonresidents for a portion of the year.

RENTERS' TAX RELIEF—Continued

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

The Governor's Budget proposes an appropriation of $425 million in the budget year, which is an increase of $20 million, or 4.9 percent, over the estimated current year expenditure.

Table 1 displays information on the number of claimants and the expenditures under this program for the 1979–80 through 1981–82 fiscal years.

Table 1
Renters' Tax Relief Program
Summary of Claimants and Expenditures [a]

Claimants	*Actual 1979–80*	*Estimated 1980–81*	*Proposed 1981–82*
Number	4,063,477	4,240,000	4,400,000
Percent increase over prior year	—	4.3%	3.8%
Expenditures			
Amount	$357,526,234	$405,000,000	$425,000,000
Percent increase over prior year	—	13.3%	4.9%

[a] Number of claimants based on income year data; amounts paid reflect fiscal year data.

The significant increase in expenditures for 1980–81 (13.3 percent) reflects the effect of two factors. First, a large percentage of *1979* renters' credit claims (about 8 percent) were paid after June 30, 1980, causing the expenditures to be carried over into 1980–81. Second, the Franchise Tax Board anticipates that a higher percentage of *1980* claims will be paid before June 30, 1981, resulting in a higher level of 1980–81 expenditures.

The appropriation for 1981–82 is based upon an anticipated 4.4 million claimants, which is a 3.8 percent increase over the estimated participation during the current year.

Table 2 shows the distribution of these claimants by status (single, joint, head-of-household, and other renters) used to estimate program costs.

Table 2
Renters' Tax Relief Program
Breakdown of Claimants by Filing Status [a]
(in thousands)

	Estimated 1980–81	*Estimated 1981–82*
Single	2,209	2,293
Joint	1,370	1,421
Head-of-household	585	607
Other	76	79
Totals	4,240	4,400

[a] Based upon the distribution of claimants for the 1979 income year, as reported by the Franchise Tax Board.

Current Year Savings Anticipated

A total of $418 million was appropriated for this program in 1980–81. However, the cost of the program in the current year is estimated at $405 million. Thus, there is an anticipated savings of approximately $13 million for this program in 1980–81.

SUBSTANDARD HOUSING

Item 910-101 (i) from the General Fund — Budget p. GG 168

Requested 1981–82	$100,000
Estimated 1980–81	79,471
Actual 1979–80	107,817
Requested increase $20,529 (+25.8 percent)	
Total recommended reduction	$45,529

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. ***We recommend that Item 910-101-001 (i) be reduced by $45,529 to reflect the existing balance of the Local Agency Code Enforcement and Rehabilitation Fund.*** 1646
2. We recommend that legislation be enacted to limit the amount of any disbursements from the Local Agency Code Enforcement and Rehabilitation Fund to the amount actually collected in the prior fiscal year. 1646

GENERAL PROGRAM STATEMENT

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

Chapter 238, Statutes of 1974, disallowed certain income tax deductions when taken on rental housing which is in violation of state or local housing codes. Chapter 1286, Statutes of 1978, provided that the additional tax revenues generated by this provision are to be transferred from the General Fund to the Local Agency Code Enforcement and Rehabilitation Fund (LACERF) in the next fiscal year. The funds are then distributed by the State Controller to the cities and counties in which the specific properties were located.

These funds are to be used by local agencies for (1) code enforcement activities, (2) low-income housing rehabilitation, and (3) minimizing displacement resulting from code enforcement. The Department of Finance is required to estimate the allocation of funds for transfer by the Controller, by October 1 of each year.

ANALYSIS AND RECOMMENDATIONS

The Governor's Budget proposes an appropriation of $100,000 for this program in 1981–82, an increase of 25.8 percent over the amounts distributed in the current year.

Table 1 displays the allocation of funds to local agencies for 1980–81, the second year of the program. As shown in the table, the City and County of San Francisco received $74,978, or about 94 percent of the total $79,471 distributed. The table shows that in 1980–81, only three local agencies received funds from this program.

SUBSTANDARD HOUSING—Continued

Table 1
Local Agency Code Enforcement and Rehabilitation Fund
Distribution of Funds to Local Agencies
1980–81

	Amount
San Francisco City and County	$74,978
Los Angeles City	4,449
San Joaquin County	44
Total	$79,471

Chapter 1286 provides that local agencies shall notify the Franchise Tax Board (FTB) of housing code violations they have identified once the taxpayer has been given a period of time to bring the substandard property into compliance. Thus, a local agency's share of Code Enforcement and Rehabilitation Fund monies is a direct function of its code enforcement activity.

Budgeting for Revenue Disbursements

We recommend that Item 910-101-001(i) be reduced by $45,529 to reflect the existing balance of the Local Agency Code Enforcement and Rehabilitation Fund. We also recommend that legislation be enacted to limit the amount of any disbursements from the LACERF to the amount actually collected in the prior fiscal year.

As required by Chapter 1286, our office recently completed a report analyzing the Substandard Housing Abatement Program. As we noted in the report, the language of Chapter 1286 requires that an *estimate* of the "net amount collected" during the preceding fiscal year due to the denial of tax deductions be made by the Department of Finance and included in the Budget Bill for appropriation by the Legislature. The language further specifies that this amount be transferred by the Controller to the LACERF on July 1 of the budget year, and distributed to each local agency in proportion to the amounts in the funds coming from taxpayers residing in that locality.

For the 1980–81 fiscal year, an estimate of $125,000 was appropriated by the Legislature for transfer to the fund. However, the FTB later reported to the Department of Finance that only $79,47 had been *collected* during the 1979–80 fiscal year. Notwithstanding this fact, the law appears to require that the full $125,000 be distributed. We believe this to be contrary to the Legislature's intent that only revenues generated by the disallowance of tax deductions be returned to local agencies. Accordingly, we recommend that legislation be enacted to limit the amount transferred to the LACERF to the *amount actually collected* in the prior fiscal year. This will require that the transfer be made *after* the statutory date of July 1. However, as the disbursements are not made until October and the collections are known by the end of August, this should be no problem.

It should be noted that the Controller, acting on the advice of the Department of Finance, has actually distributed only the $79,471. The balance of the amount transferred ($45,529) remains in the fund, and according to the Controller's Office, will not revert to the General Fund at the close of the current fiscal year. Therefore, we also recommend that this item be reduced by $45,529 to reflect this balance.

ALTERNATIVE ENERGY TAX CREDITS

Item 910-101(j) from the General Fund — Budget p. GG 168

Requested 1981–82	$5,000,000
Estimated 1980–81	1,500,000
Actual 1979–80	—
Requested increase $3,500,000 (+133.3 percent)	
Total recommended reduction	None

GENERAL PROGRAM STATEMENT

This item provides funding for refundable income tax credits associated with the installation of energy conservation and solar energy equipment.

Chapter 1082, Statutes of 1977, permitted taxpayers to take income tax credits equal to 55 percent of the cost of solar energy systems and *related* energy conservation measures, up to $3,000 on single-family dwellings. On other property, the credits were limited to 25 percent of the cost if that cost exceeds $12,000. The credits authorized by Chapter 1082 were not refundable, however, so that if a taxpayer's income tax liability was less than the amount of the credit, the full value of the credit could not be realized.

Chapter 903, Statutes of 1980, extended the credit through the 1983 income year and provided that the credit shall be refundable for single taxpayers with adjusted gross incomes up to $15,000, or taxpayers filing joint returns with incomes up to $30,000. With a refundable credit, the full value of the credit is realized regardless of the level of tax liability.

Chapter 904, Statutes of 1980, provides for an income tax credit of up to $1,500 for 40 percent of the cost of energy conservation measures *not* associated with a solar energy system. If the cost of the conservation measure exceeds $6,000, the credit is limited to 25 percent of the cost. Energy conservation measures covered include: ceiling insulation, weather-stripping, reduced-flow devices on shower heads, and covers for swimming pools. This credit is effective beginning with the 1981 income year, and is refundable for those taxpayers with incomes up to the limits specified for the solar energy system credit.

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

The Governor's Budget proposes an appropriation of $5 million for this program in 1981–82. This amount is intended to fund the cost of refunds paid to taxpayers who claim credits for solar energy systems or energy conservation measures.

The amount requested in the budget reflects a high degree of uncertainty over the cost of these credits in 1981–82. Chapter 903 appropriated $1.5 million for refunds for the solar energy systems credit for 1980–81, the first year this credit is refundable. This amount was based on the Franchise Tax Board's estimate of the number of taxpayers who would receive all or part of their credit as a refund. The $5 million requested in the budget for 1981–82 represents the cost of refunds for the *second year* for energy system credits and the *first year* for energy conservation measures as provided for by Chapter 904.

Given the lack of experience with the credits to date, we have no basis for recommending a change in the amount requested for this item.

FEDERAL REVENUE SHARING

Item 954 from the General Fund — Budget p. GG 175

Requested 1981–82	$180,300,000
Estimated 1980–81	276,200,000
Actual 1979–80	276,200,000
Requested decrease $95,900,000 (−34.7 percent)	
Total recommended reduction	None

GENERAL PROGRAM STATEMENT

The State and Local Fiscal Assistance Act of 1972 (general revenue sharing) was enacted on October 20, 1972, as a means of providing financial aid to state and local governments. The allocation of general revenue sharing funds among the recipient governments for each entitlement period is made according to statutory formulas using data such as population, general tax effort, and income tax collections.

The State and Local Fiscal Assistance Amendment of 1976 extended the program to September 30, 1980. No substantive changes were made to the allocation formulas. The new law, however, requires recipient governments to hold public hearings on proposed uses of the funds.

In fiscal year 1973–74, federal revenue sharing funds were appropriated for educational apportionments and for the costs of welfare payments under the State Supplementary Payment program (SSP). For fiscal years 1974–75 through 1977–78, funds were appropriated to the State School Fund for public school apportionments. For fiscal years 1978–79 through 1980–81, funds were appropriated solely for the support of the SSP program in order to ensure compliance with federal requirements for an "audit trail" and nondiscrimination in the use of revenue sharing funds.

During the current year, the state received the last two revenue sharing payments under that portion of the federal program which expired September 30, 1980.

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

The Governor's Budget proposes that the *entire* remaining balance of the Revenue Sharing Fund, including interest, be appropriated to the General Fund. This amount—$180.3 million—is budgeted for the SSP program (Item 518 of the Governor's Budget) in 1981–82.

Future Funds Dependent on Reduction in Categorical Grants

Congress did not provide funds for the *state* share of revenue sharing for the 1981 federal fiscal year (October 1980 through September 1981). *Authorization* for funding was provided, however, for federal fiscal years 1982 and 1983. This legislation provides that the provision of revenue sharing funds to a state is contingent on a dollar-for-dollar *reduction* in federal categorical grant funds provided to that state. The details of this trade-off have yet to be specified. For this reason, no additional funds have been included in the budget for 1981-82.

HEALTH BENEFITS FOR ANNUITANTS

Item 965 from the General Fund — Budget p. GG 187

Requested 1981–82	$41,219,000
Estimated 1980–81	38,774,000
Actual 1979–80	29,872,260
Requested increase $2,445,000 (+6.3 percent)	
Total recommended increase	Pending

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. Funding for Premium Increase. Withhold recommendation, pending determination of the actual increase in health insurance premiums. 1650

GENERAL PROGRAM STATEMENT

This appropriation provides the state's contribution toward payment of monthly health insurance premiums for annuitants of retirement systems to which the state contributes as an employer. These systems include the Judges', Legislators', Public Employees', and Teachers' Retirement Systems. For the latter two systems, this health insurance contribution is limited to retired state employees.

This program offers a degree of post-retirement security for employees and their dependents by paying one of the following amounts toward the monthly premium of a state-approved insurance plan: (1) $49 for the annuitant only, (2) $90 for an annuitant with one dependent, and (3) $117 for an annuitant with two or more dependents. These contribution levels were authorized by the 1980 Budget Act and became effective July 1, 1980. The prior state contribution rates were $43, $79, and $102, respectively.

ANALYSIS AND RECOMMENDATIONS

The budget proposes an appropriation of $41,219,000 from the General Fund for payment of health insurance premiums in 1981–82. This is $2,445,000, or 6.3 percent, more than estimated current-year expenditures. The increase is attributable only to the projected growth in the number of annuitants, which is shown in Table 1.

Table 1
Annuitant and Health Benefit Cost Projections

Retirement System	*Number of Annuitants*			*State Costs (thousands)*		
	Estimated 1980–81	*Projected 1981–82*	*Percent Increase*	*Estimated 1980–81*	*Projected 1981–82*	*Percent Increase*
Judges	427	454	6.3%	$345	$367	6.4%
Legislators	98	104	6.1	77	82	6.5
Employees	46,128	49,024	6.3	38,128	40,532	6.3
Teachers	275	293	6.5	224	238	6.3
	46,928	49,875	6.3%	$38,774	$41,219	6.3%

The state contributions are paid initially from the General Fund. Special fund agencies are assessed pro rata charges for their retired employees which are then credited to the General Fund.

HEALTH BENEFITS FOR ANNUITANTS—Continued

Premium Cost Increase Not Budgeted

We withhold recommendation, pending determination by the Public Employees' Retirement System of the actual increase in health insurance premiums.

Current law expresses legislative intent to pay an average of 100 percent of health insurance costs for annuitants and 90 percent of health insurance costs for their dependents. As premium costs for this insurance rise, the state's contribution must also increase proportionally to maintain the same percentage of state contributions.

The amount proposed for this item in 1981–82 does not provide for an inflationary increase in health insurance premiums. When this analysis was written, the Public Employees' Retirement System (PERS) anticipated a health insurance premium increase of about 15 percent for 1981–82. The precise amount of any increase, however, will not be known until May or June 1981, when the new premiums are adopted.

PROVISION FOR EMPLOYEE COMPENSATION CIVIL SERVICE, EXEMPT, STATUTORY, ACADEMIC AND NONACADEMIC EMPLOYEES

Item 980 from the General Fund and various other funds — Budget p. GG 194

Requested 1981–82	Not specified
Total recommended change	Pending

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS *Analysis page*

1. Executive Salaries. Recommend Committee on Executive Salaries be activated to adjust salaries of state officials. 1658
2. Compensation Increase. Recommend SPB submit information to the Legislature for evaluating compensation increases. 1661
3. Health Insurance Cost Data. Recommend PERS, in cooperation with the Department of Finance, annually submit specified cost data relative to employee health insurance. 1661

ANALYSIS AND RECOMMENDATIONS

The Governor's Budget does not propose a specified amount for compensation increases for state employees. It indicates (on page A-30), however, that $509 million is available in the General Fund which could be used for discretionary increases in a number of programs, including employee compensation and those with statutory cost-of-living adjustments (COLA's).

The Governor's Budget has not allocated these funds to specific programs; this has been left to the Legislature.

The budget makes *no* provision for salary increases to those state employees who are not paid from the General Fund. These employees represent about 36 percent of total state employment.

The cost of providing various salary increases to the major categories of state employees is indicated in Table 1. This table shows that each 1 percent increase in state salaries will increase General Fund costs by $34.3 million, and special fund costs by $9.3 million.

Table 1
Cost of Providing Various Salary Increases For State Employees (Excluding Judges)

		Amount of Increase (thousands)		
Employee Group	*Fund*	*1 Percent*	*5 Percent*	*9 Percent*
Civil Service and related	General	$16,706	$83,530	$150,354
	Special	9,285	46,425	83,565
	Other	9,859	49,295	88,731
(Totals, civil service and related)		($35,850)	($179,250)	($322,650)
University of California (UC):				
Academic	General	$4,752	$23,760	$42,768
Nonacademic	General	4,384	21,920	39,456
(Totals, UC)		($9,136)	($45,680)	($82,224)
California State University and Colleges (CSUC):				
Academic	General	$5,170	$25,850	$46,530
Nonacademic	General	3,334	16,670	30,006
(Totals, CSUC)		($8,504)	($42,520)	($76,536)
Total Costs		$53,490	$267,450	$481,410
	General	(34,346)	(171,730)	(309,114)
	Special	(9,285)	(46,425)	(83,565)
	Other	(9,859)	(49,295)	(88,731)

Lump-Sum Payment (SB 91)

Chapter 192, Statutes of 1979 (SB 91), authorized a lump sum payment to state employees.

During fiscal year 1978–79, state employees were not granted a salary increase. Chapter 192 was enacted to partially compensate state employees for the reduction in their purchasing power during that year. This measure provided a lump-sum payment to each eligible state employee equal to the additional compensation the employee would have received had his or her salary been increased by 7 percent effective October 1, 1978. If the payment had been spread over the period July 1, 1978, to June 30, 1979, it would be equivalent to a 5.25 percent increase for the entire fiscal year. The act appropriated $207.6 million ($135 million General Fund) to cover the cost of the lump-sum payment.

The Governor vetoed this measure, but his veto was overridden on July 2, 1979, and the measure became law.

Lump-Sum Payment Issue was in the Courts. In November 1979, the Third District Court of Appeals ruled that the lump-sum payment was unconstitutional. The court held that such a payment would violate a provision in the State Constitution which prohibits granting extra compensation to public employees for work already performed. The case, however, was appealed to the State Supreme Court.

In December 1980, the State Supreme Court ruled that Chapter 192 did not violate the State Constitution and, as a result, the lump-sum payments were issued.

A Review of 1980 Salary Program

Increases in the Budget Act. The 1980 Budget Act provided $499 million (all funds) to fund a salary increase program for state employees consisting of three elements:

- A 9.75 percent *across-the-board* increase for all state employees.
- A requirement that each employee receive a minimum monthly increase of $100.
- Funds to realign salaries of certain classifications.

EMPLOYEE COMPENSATION
CIVIL SERVICE, EXEMPT, STATUTORY, ACADEMIC AND NONACADEMIC EMPLOYEES—Continued

Twenty-Three Percent of Civil Service Employees Were Paid Above Prevailing Rates. One side effect of granting an across-the-board salary increase was that, according to the State Personnel Board, 31,100 state employees, or 23 percent of the civil service work force, were paid *above* prevailing rates in the private sector and other governmental units as of July 1, 1980. The board estimates the current year cost of these payments above prevailing rates is $9,236,000 ($2.9 million General Fund, $3.6 million special funds, and $2.7 million other funds).

Judicial Salaries

Court Ruling on Judicial Salaries. Chapter 1183, Statutes of 1976 (AB 3844), (a) froze judges' salaries on January 1, 1977, for 18 months and (b) limited subsequent annual judicial salary increases to a maximum of 5 percent. Prior to the enactment of Chapter 1183, judicial salaries were increased each September 1 by the percentage increase in the California Consumer Price Index during the prior calendar year.

In 1980, the California Supreme Court, in the *Olson* v. *Cory* case ruled that Chapter 1183 was partly inconsistent with the Constitution because it, among other things, impaired the employment contracts between certain judges and the state. Specifically, the Court ruled that in the case of judges who were in office before January 1, 1977 (when Chapter 1183 became effective), neither the salary freeze nor the 5 percent limit on subsequent increases could be applied until those judges began new terms of office.

The court's ruling resulted in a two-tier salary structure for judges, one based on the 1976 law and a higher one based on the prior law.

Pensions of certain retired judges and their survivors also increased as a result of the Supreme Court's ruling, because pension benefits are tied to active judges' salaries. Generally, a retired judge receives an allowance equal to either 65 percent or 75 percent of the current salary paid to the judge holding the office to which the retired judge was last elected.

Proposition 11, enacted by the voters at the November 1980 statewide election, amended the State Constitution to produce the following effects:

- It eliminated, effective January 1, 1981, the additional pay being received by each judge whose base salary was increased as a result of the Supreme Court's ruling.
- It eliminated, effective January 1, 1981, the additional pension benefits being received by each retired judge (or survivor) as a result of the Court's ruling.
- It authorizes the Legislature to terminate expected *increases* in judges' salaries *during* their term of office, provided that such action does not cause a reduction in the actual salaries paid to judges during their term.
- It specifically provides that salaries of judges are not considered an obligation of contract.

Chapter 835, Statutes of 1980 (SB 2060), increased, effective January 5, 1981, the annual salary of:

- Superior court judges from $56,915 to $59,686, an increase of $2,771, or 4.9 percent.
- Municipal court judges from $52,366 to $54,506, an increase of $2,140, or 4.1 percent.

Historical Comparison of Salary Increases

Table 2 compares the annual salary increases received by superior court judges, employees in private business, state civil service employees, state statutory officers (those officials whose salaries are specified by statute) and state legislators, from fiscal years 1967–68 through 1980–81.

Table 3 shows both the dollar amounts and percentages by which the 1980–81 salary level exceeds the 1967–68 level for each such group, and the percentage change in the Gross National Product Personal Consumption Deflator (price index) between 1967–68 and 1980–81.

Table 2
Comparison of Annual Salary Increases Received by Judges, Employees in Private Business, State Civil Service Employees, Statutory Officers and State Legislators, from 1967–68 Through 1980–81

	Superior Court Judges		*Private Employment*[b]	*Civil Service Percent Increase*		*Statutory Officers*	*State Legislators*	
	Salary[a]	*Increase*	*Average Increase per Employee*	*Increase in total Payroll*	*Average Increase per Employee*	*Percent Increase*	*Salary*	*Percent Increase*
1967–68	$25,000	—	4.5%	4.9%	5.1%	—	$16,000	—
1968–69	30,572	22.3%	4.8	5.3	5.7	5.0%	16,000	—
1969–70	31,816	4.1	6.7	5.6	5.6	11.5	16,000	—
1970–71	33,407	5.0	4.7	5.0	5.2	—	19,200[e]	20.0%
1971–72	35,080	5.0	6.6	—	—	—	19,200	—
1972–73	36,393	3.7	6.3	8.3	9.0	5.0	19,200	—
1973–74	37,615	3.4	6.2	12.9	11.7	12.5	19,200	—
1974–75	40,322	7.4	6.3	5.3	5.0	5.0	21,120[f]	10.0
1975–76	45,299	12.3	8.2	7.1[c]	6.7[c]	—	21,120	—
1976–77	49,166	8.5	7.3	6.6	[d]	1.9	23,232[g]	10.0
1977–78	49,166	—	6.5	7.5	7.1	7.5	23,232	—
1978–79	51,624	5.0	7.4	—	—	—	25,555[h]	10.0
1979–80	54,205	5.0	7.0	15.0	14.5	15.0	25,555	—
1980–81	59,686	10.1	10.5	10.0	10.0	9.75	28,111[i]	10.0

[a] Increases effective each September 1, until 1977–78. Pursuant to Chapter 1183, Statutes of 1976, judicial salaries in effect January 1977 were frozen until June 30, 1978 and, thereafter, such salaries were increased each July 1 (beginning in 1978) by the lower of (1) the percentage increase in the California Consumer Price Index during the prior calendar year or (2) 5 percent. Pursuant to Chapter 1018, Statutes of 1979, judicial salaries are to be increased effective each July 1 (beginning in 1980) by the lower of (1) the average percentage increase in state civil service salaries or (2) 5 percent. The California Supreme Court ruled that in the case of judges who were in office before January 1, 1977 (when Chapter 1183 became effective), neither the salary freeze nor the 5 percent limit on subsequent increases could be applied until the judges began new terms of office. The salaries indicated from 1977–78 through 1979–80 are for judges not affected by the Court's ruling. Proposition 11, enacted by the voters in November 1980, eliminated, effective January 1, 1981, the additional pay being received by judges whose base salaries were increased by this ruling. Chapter 835, Statutes of 1980, among other things caused all Superior Court judges' salaries to increase from $56,915 to $59,686 effective January 5, 1981.

[b] Based on salaries in effect each March, as surveyed by the State Personnel Board. (For example, the 10.5 percent increase indicated on the bottom line represents the increase from March 1979 to March 1980).

[c] Does not include one-time bonus of $400 paid to employees having a maximum salary of $753 or less on July 15, 1975.

[d] Not calculated by State Personnel Board because of flat salary increases.

[e] Effective January 1971.

[f] Effective December 1974.

[g] Effective December 1976.

[h] Effective December 1978.

[i] Effective December 1980.

EMPLOYEE COMPENSATION
CIVIL SERVICE, EXEMPT, STATUTORY, ACADEMIC AND NONACADEMIC EMPLOYEES—Continued

During the 13-year period, the index increased 126.4 percent, while salaries were increased as follows:

1. Private employees—145.7 percent.
2. Civil service employees—144.8 percent.
3. Judges—138.7 percent.
4. Statutory officers—100.8 percent.
5. Legislators—75.7 percent.

Table 3
Comparison of Amounts by Which 1980–81 Salaries Exceed 1967–68 Salaries for Judges, Private Employees, State Civil Service Employees, Statutory Officers and Legislators in Relation to the Gross National Product Consumption Expenditure Price Index During that Period

	Superior Court Judges	*Private Employees*[a]	*State Civil Service*[b]	*Statutory Officers*[c]	*State Legislature*	*GNP Consumption Personal Price Index*
1980–81 Salary Level	$59,686	$39,317	$39,172	$32,122	$28,111	187.7%
Less 1967–68 Salary Level	25,000	16,000	16,000	16,000	16,000	82.9
Amount of Increase	$34,686	$23,317	$23,172	$16,122	$12,111	104.8
Percent Increase	138.7%	145.7%	144.8%	100.8%	75.7%	126.4%

[a] Based on hypothetical employee (1) earning $16,000 in February 1967 and (2) receiving annual increases each March equivalent to the average increase in private employment as surveyed by the State Personnel Board.

[b] Based on hypothetical employee (1) earning $16,000 on June 30, 1967, and (2) receiving annual increases equivalent to the average increaes for the total civil service payroll. (Civil service salaries actually are adjusted individually on a class-by-class basis.)

[c] Based on hypothetical statutory officer earning $16,000 on June 30, 1967. (All statutory officers presently receive the same annual percentage increases.)

Constitutional Salaries Have Fallen Behind

Table 4 presents a comparison of the increases in salaries during the period 1967–68 to 1980–81 for:

- The seven state constitutional officers.
- The chairman and members of the State Board of Equalization.
- Selected statutory officers.

The table also shows the percentage increase in the GNP Personal Consumption Deflator (price index) during the same period.

The table shows that, from 1967–68 to 1980–81, the index increased 126.4 percent, while salaries increased as follows:

1. Governor—11.3 percent.
2. Attorney General—48.4 percent.
3. Lieutenant Governor, Controller, Treasurer, Secretary of State and Superintendent of Public Instruction—70 percent.
4. Chairman, Board of Equalization—131.4 percent.
5. Members, Board of Equalization—134.0 percent.
6. Director of Finance—98.0 percent.
7. Director of Corrections—119.0 percent.
8. Director of Veterans Affairs—109.6 percent.

Table 4
Comparison of Amounts by Which 1980–81 Salaries Exceed 1967–68 Salaries For State Constitutional Officers, Board of Equalization Members, And Selected State Statutory Officers in Relation to the Change in the GNP Personal Consumption Deflator (Price Index) During that Period

	State Constitutional Officers			*Board of Equalization*		*Selected Statutory Officers*			*GNP Personal Consumption Deflator (Price Index)*
	Governor	*Attorney General*	*Others*[a]	*Chairman*	*Members*	*Director of Finance "Level I"*[b]	*Director of Corrections "Level II)"*[c]	*Director of Veterans Affairs "Level III"*[d]	
1980–81 Salary Level	$49,100	$47,500	$42,500	$48,597	$47,972	$60,026	$51,468	$47,160	187.7%
Less 1967–68 Salary Level	44,100	32,000	25,000	21,000	20,500	30,319	23,500	22,500	82.9
Amount of Increase	$5,000	$15,500	$17,500	$27,597	$27,472	$29,707	$27,968	$24,660	104.8
Percent Increase	11.3%	48.4%	70.0%	131.4%	134.0%	98.0%	119.0%	109.6%	126.4%

[a] Lieutenant Governor, Controller, Treasurer, Secretary of State and Superintendent of Public Instruction.

[b] Under existing law (Gov't. Code Section 11550), the Director of Finance and the various agency secretaries currently receive the same salary.

[c] Under existing law (Gov't Code Section 11552), the Director of Corrections, 19 other department heads and members of the Public Utilities Commission currently receive the same salary.

[d] Under existing law (Gov't. Code Section 11554), the Director of Veterans Affairs, 8 other agency heads and the State Architect currently receive the same salary.

EMPLOYEE COMPENSATION CIVIL SERVICE, EXEMPT, STATUTORY, ACADEMIC AND NONACADEMIC EMPLOYEES—Continued

As noted previously, state civil service salaries increased by an average of 144.8 percent from 1967–68 to 1980–81.

Department Heads' Salaries Have Been Surpassed

Until recent years, each department director received a higher salary than any of his or her subordinates. As indicated above, however, state civil service salaries have been increased over the years by a significantly larger percentage than salaries of statutory and constitutional officers. As a result, many civil service employees currently receive higher salaries than their own department heads.

At our request, the SPB surveyed nine departments known to have at least some civil service employees who are paid more than their respective department heads, to determine the incidence of this situation. The survey results are shown on Table 5, which indicates that in the nine departments surveyed, the maximum salary for a total of 586 employees in civil service positions exceeded the director's salary.

Table 5
Sample of Departments Known to Have Civil Service Positions With a Maximum Salary Higher Than the Salary of the Department Head

Department	*Number of Employees in Positions Having a Maximum Salary Above the Director's Salary*
Corrections	140
Education	17
Transportation	10
Health Services	85
Developmental Services	220
Mental Health	72
Office of Statewide Health Planning and Development	2
Rehabilitation	5
Social Services	35
Total	586

Department Heads' Salaries Will Fall Farther Behind Unless Corrective Measures Are Taken.

The number of employees being paid more than their respective department heads will increase significantly in future years, causing serious salary distortions and inequities, unless steps are taken to adjust salaries of statutory and constitutional officers. This problem is particularly acute with respect to the 7 constitutional officers because, under the State Constitution (Article V, Section 12), their salaries may not be changed during their elected term of office. Consequently, January 1983 is the next date on which salaries of constitutional officers can be adjusted. If they are not adjusted by that date, the present salary rates will remain in effect until January 1987.

Legislature's Efforts to Make Compensation of State Officials More Equitable

In recent years, the Legislature has taken a number of actions to make the compensation of state officials more equitable.

Increased Salaries of Constitutional Officers and Realigned Statutory Salaries. In 1969, the Legislature enacted Chapter 1599 which:

1. Increased salaries of the seven state constitutional officers effective January 1971 as follow:
   - Governor—from $44,100 to $49,100.
   - Attorney General—from $39,132 to $42,500.
   - Lieutenant Governor, Controller, Treasurer, Secretary of State and Superintendent of Public Instruction–from $25,000 to $35,000.
2. Adjusted salaries of statutory officers by:
   - Combining them into several uniform levels.
   - Adjusting them so as to restore a more equitable relationship with salaries of top level civil service and exempt employees.

Committee on Executive Salaries. Chapter 1599, Statutes of 1969, also created a Committee on Executive Salaries for the purpose of assisting the Governor and Legislature in maintaining equitable internal salary relationships among the various state executives.

The committee is to consist of the following: (1) the Governor's Appointment Secretary, (2) two members of the Senate, appointed by the Senate Rules Committee, (3) two members of the Assembly appointed by the Speaker, (4) the Chairman of the Commission on California State Government Organization and Economy, (5) a member of the Commission on California State Government Organization and Economy appointed by the chairman of the commission, (6) a member of the State Personnel Board, and (7) the Director of the Department of Finance.

Staff assistance to the committee is to be supplied jointly by the Department of Finance, the Legislative Analyst, and the State Personnel Board.

A chairman was not designated, however, *and the committee has never met.*

Public Officers Compensation Commission. The Legislature, through Resolution Chapter 130, Statutes of 1975 (ACR 129), established a Public Officers Compensation Commission on a temporary basis to:

- Study matters relating to compensation and benefits of the seven state constitutional officers, members of the judiciary and members of the Legislature.
- Submit to the Legislature a proposed constitutional amendment for implementing the commission's findings and recommendations.

The commission was chaired by the Chairman of the Commission on California State Government Organization and Economy, and consisted of 14 other members selected in accordance with specified criteria. It submitted a proposed constitutional amendment which was approved by the Legislature and placed on the ballot in 1978 as Proposition 12. The proposition would have (1) repealed the Legislature's constitutional duty to set pay and benefits for elected state officials and (2) established a special commission for this purpose. Proposition 12, however, was not approved by the voters.

Increased Salaries of Constitutional Officers. In 1977, the Legislature enacted Chapter 1099 which increased, effective January 1979, salaries of all constitutional officers except the Governor (who said he did not want a salary increase) as follows:

- Attorney General—from $42,500 to $47,500.
- Lieutenant Governor, Controller, Treasurer, Secretary of State and Superintendent of Public Instruction—from $35,000 to $42,500.

EMPLOYEE COMPENSATION
CIVIL SERVICE, EXEMPT, STATUTORY, ACADEMIC AND NONACADEMIC EMPLOYEES—Continued

Committee on Executive Salaries Should be Activated

We recommend that the Legislature adopt supplemental report language (1) designating the Chairman of the Commission on California State Government Organization and Economy as Chairman of the Committee on Executive Salaries and (2) directing the chairman to activate the committee, so as to provide the Legislature with a better basis for adjusting the salaries of state executives in a consistent and equitable manner.

As noted above, the Legislature, through Chapter 1599, Statutes of 1969, established the Committee on Executive Salaries for the specific purpose of assisting the Legislature and the Governor in adjusting salaries of state executives. The committee, however was never activated.

We believe the committee should be activated in order to provide the Legislature with a basis for adjusting salaries of state officials in a consistent and equitable manner in relation to state civil service salary rates.

Accordingly, we recommend that supplemental language be adopted as follows:

"The Chairman of the Commission on California State Government Organization and Economy shall:

1. Serve as Chairman of the Committee on Executive Salaries (in accordance with Sections 11675-9 of the Government Code).
2. Take action necessary to activate the committee in order to develop recommendations for adjusting salaries of state constitutional and statutory officers in a manner which is (1) internally consistent and (b) equitable in relation to state civil service salary rates."

CIVIL SERVICE AND RELATED EMPLOYEES

At the time this analysis was prepared, there was no basis for estimating how many state civil service employees, if any, will be represented in collective negotiations over salary and benefit levels for the budget year. It had not been determined when exclusive bargaining agents will be certified or how many employees will be represented by exclusive bargaining agents.

Legislation Replaces Prevailing Rate System With Good Faith Negotiation Procedures

Traditionally, state civil service salaries and benefits have been adjusted on the basis of (1) State Personnel Board (SPB) surveys of salaries and benefits received in nonstate employment, (2) salary and benefit increase recommendations contained in the board's annual report to the Governor and Legislature, (3) action by the Legislature and Governor on the budget act, and (4) SPB allocation of funds appropriated for salary increases, among occupational classes.

Chapter 1159, Statutes of 1977 (SB 839), which became operative July 1, 1978, provides for a formal, bilateral employee relations system for most state civil service employees. Under its provisions, the Governor or his designee is required to "meet and confer in good faith" with employee organizations which have been selected by a majority of employees within individual bargaining units in an effort to reach agreement relative to "wages, hours and other terms and conditions of employment." Such agreements are to be formalized in memorandums of understanding. Any provision in such a memorandum requiring the expenditure of funds (for example, negotiated salary or benefit increases) is subject to approval by the Legislature. Mediation is required if the parties are unable to reach agreement.

The Public Employment Relations Board (PERB) is responsible for (1) determining appropriate bargaining units (that is, designating the specific civil service classifications which are to be combined in separate units for representation by individual employee organizations) and (2) conducting elections to determine which, if any, of the competing employee organizations will serve as the exclusive bargaining agent for each such unit.

Implementing Collective Negotiations

The PERB completed the civil service unit determination process in November 1979 and designated a total of 20 separate bargaining units.

The next major step toward implementing collective negotiations is the conducting of elections to determine which employee organizations will be the exclusive representatives of the individual units. To qualify, an organization must be certified by the PERB as having received a majority of the valid votes cast by the employees in a given unit. (If the majority vote for "no representative," no organization will be certified.)

Various employee organizations have formally requested that the PERB conduct such elections, and the board has determined which of these organizations qualify to appear on the ballot. To qualify, an organization must demonstrate "proof of support" by securing the signatures of at least 30 percent of the employees in a unit.

After the board determined that an organization had qualified, competing organizations were allowed during the following 30-day period to qualify for the ballot. To do so, competing organizations that qualified demonstrated proof of support by securing the signature of at least 10 percent of the employees in the particular unit. After an election is completed and the results are certified, the winning organization, if there is one, has the right to act as the exclusive bargaining representative of all employees in the particular bargaining unit, in accordance with the provisions of Chapter 1159.

According to PERB staff, employee organizations may be certified as the exclusive representative for some of the bargaining units prior to July 1, 1981.

Legal Action Challenges the Constitutionality of Chapter 1159

In January 1979, the Pacific Legal Foundation filed on behalf of a group of state employees, a lawsuit challenging the legality of Chapter 1159. The suit contended that Chapter 1159 removes constitutionally based responsibilities of the State Personnel Board (SPB). In February 1979, a similar but independent lawsuit was filed by the State Attorney General. In March 1980, the Third District Court of Appeals ruled that Chapter 1159 is unconstitutional because it conflicts with the constitutional power of the SPB to set salaries. The case, however, has been appealed to the California Supreme Court, which heard the oral arguments regarding it in December 1980, but has not yet rendered a decision. Consequently, it is uncertain at this time whether or when good faith collective negotiations will take place with respect to state civil service employees.

Problems the Legislature Faces in Providing for Compensation Increases Under the Provisions of Chapter 1159

In our 1978 Analysis (pages 1082–1083) we described a number of significant problems that the Governor and Legislature will face in budgeting for compensation increases under the provisions of Chapter 1159. We noted, among other things, that:

1. No agreed upon standards will exist for determining the appropriate increase for state employees.
2. It will be difficult for the Legislature to evaluate and act on negotiated increases in a meaningful manner.

EMPLOYEE COMPENSATION
CIVIL SERVICE, EXEMPT, STATUTORY, ACADEMIC AND NONACADEMIC EMPLOYEES—Continued

In the past, prevailing rates in nonstate employment have provided an objective basis for determining compensation increases. By replacing the prevailing rate approach with collective negotiations, Chapter 1159 has removed the objective basis for salary-setting. Consequently, it will be much more difficult to select and justify an amount for salary increases. While it is expected that the SPB will continue collecting data on nonstate salary rates which will provide some basis to the Legislature in evaluating negotiated increases, these data will not be conclusive, given the spirit of Chapter 1159.

Furthermore, it is not clear how increases will be determined for employees not covered by collective negotiations. Under Chapter 1159, the SPB will continue to adjust salaries of state civil service employees who are (1) designated as "management," "supervisory," or "confidential" employees or (2) in bargaining units not represented by exclusive bargaining agents.

Alternative Criteria the Legislature Might Use for Evaluating Compensation Increases

There are several criteria which the Legislature might use for evaluating compensation increases (1) negotiated by the administration and (2) proposed by the SPB for employees not represented in the collective bargaining process.

Negotiated Increases. Criteria which might be used for evaluating negotiated increases include:

1. Prevailing salary rates in comparable nonstate employment.
2. Increases in the GNP Personal Consumption Deflator (price index), the California Consumer Price Index (CCPI) or other indexes.
3. Recruitment and retention problems which exist for individual state classifications.
4. Cost-of-living increases granted by the state to other programs where a major share of the funding is used for salaries of local governmental employees.

Increases Proposed by the SPB. As stated previously, the SPB will continue to adjust salaries of management, supervisory, and confidential employees as well as employees in units not represented by exclusive bargaining agents. However, it is uncertain at this time what bases will be used to determine the amounts of such adjustments.

Confidential employees and employees in units not represented by exclusive bargaining agents might have their salaries adjusted on the basis of:

1. Prevailing rates.
2. Increases in the GNP Personal Consumption Deflator, the CCPI or other indexes.
3. Recruitment and retention problems.
4. Increases received by employees represented by exclusive bargaining agents.

Management and supervisory employees might have their salaries adjusted on the basis of:

1. Prevailing rates.
2. Increases in the GNP Personal Consumption Deflator, the CCPI or other indexes.
3. Recruitment and retention problems.
4. Increases received by employees represented by exclusive bargaining agents.
5. Percentage differentials between their salaries and the salaries of the employees they supervise.

Information Needed for Legislative Decision Making Under the Provisions of Chapter 1159

We recommend that the SPB submit information to the Legislature that will assist it in (1) evaluating increases negotiated by the administration and (2) determining increases appropriate for employees not represented in the collective bargaining process.

The information needed by the Legislature for evaluating compensation increase proposals will depend on which criteria the Legislature chooses to apply. While there will be no easy way for evaluating such proposals, the following information should be useful for this purpose.

1. Salaries paid for comparable work in nonstate employment
2. Recruitment and retention problems which exist with respect to individual state civil service classifications.

Increases for "management" and "supervisory" employees might be determined, at least to some extent, using standard percentage relationships between their salaries and the salaries of those they supervise.

In order for the Legislature to have at least *some* basis for (1) evaluating negotiated increases for employees covered by collective negotiations and (2) determining appropriate increases for other state employees, we recommend that the SPB:

1. Propose alternative methods by which salaries of managers and supervisors might be adjusted, including, but not limited to, the use of, standard percentage differrentials by which their salaries should exceed the salaries of employees they supervise.
2. Provide to the Legislature, upon its request, the following information:
   a. For each bargaining unit and also for "confidential" employees:
      (1) The calculated salary lag for each major occupational group and the funds required to eliminate the lag.
      (2) the nature and extent of recruitment or retention problems with respect to each classification.
   b. For "managers" and "supervisors" in each major occupational group:
      (1) the calculated increase necessary for maintaining the percentage differential in 1, above, based on negotiated increases (and increases proposed by the SPB for employees not covered by collective negotiations).
      (2) The funds required for such increases.

EMPLOYEE BENEFITS

Health Benefit Cost Data should be Provided for Legislative Decision-Making

We recommend that the PERS, in cooperation with the Department of Finance, annually report to the Legislature, beginning June 1, 1981, on the cost of maintaining the state contribution rate for employee health insurance.

The state pays the major portion of premiums for health insurance provided to active and retired civil service and related employees, and employees of the CSUC. As expressed in Section 22825.1 of the Government Code, the Legislature's intent is that the state pay 100 percent of the premium cost for coverage of these employees and annuitants and an average of 90 percent for coverage of their dependents.

Annual premium increases, which take effect in August, depend on:

1. ***Inflation:*** The additional amount required for providing the same level of coverage.

EMPLOYEE COMPENSATION
CIVIL SERVICE, EXEMPT, STATUTORY, ACADEMIC AND NONACADEMIC EMPLOYEES—Continued

2. ***New mandated benefits:*** The cost of providing a new benefit required by federal or state law. (For example, in 1979–80 maternity benefits were added to state health insurance plans because they were mandated by federal law.)
3. ***Benefit enhancements:*** The cost of providing an additional or increased benefit. (For example, in 1979–80 the Kaiser Health Plan was changed to require the covered individual to pay only $1 per prescription for outpatient drugs. Formerly, the price was based on the wholesale cost of the drug.)

Changes in the coverage of and premiums for state employee health insurance result from negotiations between PERS staff and the insurance carriers. These annual negotiations typically are completed late in May and are subject to approval by the PERS Board. Funding for the state portion of the increased costs resulting from these negotiations is included in the annual budget bill.

Changes in coverage and premiums for annuitants correspond with those made for active civil service and related employees and employees of the CSUC. Because most UC employees are not eligible for health insurance coverage under the PERS, traditionally funds are appropriated to provide them with comparable benefit improvements.

The 1980 increase in health benefit costs was due entirely to the increased cost of maintaining existing coverage. A significant portion, however, of the 1979 increase was due to benefit improvements negotiated by the PERS.

Table 6 shows the amounts by which the monthly state contribution was increased, effective August 1979, and the portion of the increase attributable to (1) enhanced coverage and (2) existing coverage and mandated new benefits.

Benefit enhancement alone increased the monthly state contribution by $1 for coverage of the employee only and by $2 for coverage of employees with one or more dependents. On an annual basis, the total cost of increasing the monthly state contribution rate for affected employees and annuitants (and for providing for comparable benefit improvements for UC employees) is approximately $16.4 million ($10.8 million General Fund). Of this amount, approximately $4 million ($2.6 million General Fund) is attributable to the benefit enhancements.

Table 6
Increase in State Contribution Rate for Employee Health Insurance Effective August 1979

	State Monthly Contribution		*Increase Effective August 1979*		
Coverage	*August 1978 through July 1979*	*August 1979 through July 1980*	*Total Increase*	*For Existing Coverage and Mandated New Benefits*	*For Enhanced Coverage*
Employee only	$38	$43	$5	$4	$1
Employee and one dependent	72	79	7	5	2
Employee and two or more dependents	92	102	10	8	2

Source: Public Employees' Retirement System.

Because the Legislature was not told how much of the funds requested to *maintain* health benefit coverage actually was intended to *enhance* these benefits, *the Legislature provided funds in the 1979 Budget Act for enhancing health benefit coverage of state employees without making a conscious decision to do so.* In order for the Legislature to receive information necessary for making informed decisions regarding employee health insurance, we recommend that supplemental language be adopted to read as follows:

"The PERS, in cooperation with the Department of Finance, shall report annually, beginning June 1, 1981, to the Joint Legislative Budget Committee and each legislative fiscal committee, the cost of:

a. Maintaining the current state contribution rate for health insurance benefits for civil service and related employees and employees of the CSUC.
b. Providing comparable benefit improvements for University of California employees.
c. Providing comparable benefits for state annuitants.

These cost estimates should identify the additional amounts required to provide:

a. New benefits, if any, mandated by state or federal law.
b. Additonal or increased benefits negotiated by the PERS."

POSTSECONDARY EDUCATION SALARIES

Academic Salaries

A decision on 1981–82 salary increases for the University of California (UC) and the California State University and Colleges (CSUC) faculty should be deferred until the California Postsecondary Education Commission (CPEC) publishes its final projections in April. These projections will show the academic salary increases necessary for UC and CSUC to achieve parity with faculty in their comparison institutions.

Comparison Institutions

Senate Concurrent Resolution No. 51 of the 1965 General Session directed the Coordinating Council for Higher Education (CPEC, since April 1, 1974) to submit annually to the Governor and the Legislature a faculty salary and fringe benefit report. The report compares California faculty salaries to those in a group of postsecondary education institutions that are comparable to the two California segments.

Since 1972–73, the UC comparison institutions have been:

1. Harvard University
2. Stanford University
3. Yale University
4. State University of New York (Buffalo)
5. Cornell University
6. University of Illinois
7. University of Michigan (Ann Arbor)
8. University of Wisconsin at Madison

The CSUC comparison institutions since 1973–74 have been:

1. State University of New York (Albany)
2. State University of New York College (Buffalo College of Arts and Science)
3. Syracuse University
4. University of Southern California
5. University of Hawaii
6. University of Wisconsin (Milwaukee)
7. University of Nevada

EMPLOYEE COMPENSATION
CIVIL SERVICE, EXEMPT, STATUTORY, ACADEMIC AND NONACADEMIC EMPLOYEES—Continued

8. University of Oregon
9. Portland State University
10. University of Colorado
11. Illinois State University
12. Northern Illinois University
13. Southern Illinois University
14. Indiana State University
15. Iowa State University
16. Wayne State University
17. Western State University
18. Bowling Green State University
19. Virginia Polytechnic Institute and State University
20. Miami University (Ohio)

CPEC Preliminary Report

A preliminary report on faculty salaries was prepared by CPEC in December 1980 for use in formulating the Governor's Budget. A second report, corrected for actual current-year salaries at comparison institutions, will be published in April 1981.

Table 7
All Ranks Average Salary Required at the University of California and the California State University and Colleges to Equal the Comparison Institution Projections for 1980–81 and 1981–82

Institution	*UC and CSUC Salaries in 1980–81*	*Comparison Institutions Salary Projections*		*Comparison Inst. Projections Lead UC and CSUC by:*	
		1980–81	*1981–82*	*1980–81*	*1981–82*
University of California	$32,281	$31,289	$33,157	−3.07%	+2.71%
California State University and Colleges	$28,787	$26,489	$28,041	−7.98%	−2.59%

Table 8
UNIVERSITY OF CALIFORNIA
Percentage Change in UC Estimated 1980–81 All Ranks Average Salary Required to Equal the Comparison Group Projections for 1980–81 and 1981–82, Based on Five-Year Compound Rate of Increase in Comparison Group Salaries (Equal Weight to Each Comparison Institution)

Academic Rank	*UC Average Salaries 1980–81*	*Comparison Group Projected Salaries*		*Percentage Change Required in UC Salaries*	
		1980–81	*1981–82*	*1980–81*	*1981–82*
(1)	*(2)*	*(3)*	*(4)*	*(5)*	*(6)*
Professor	$37,905	$36,920	$39,177	−2.60%	−3.36%
Associate Professor	25,390	24,857	26,261	−2.10	+3.43
Assistant Professor	21,044	19,389	20,463	−7.86	−2.76
All Ranks Average	$32,281 [a]	$31,289 [a]	$33,157 [a]	−3.07%	+2.71%

[a] Based on projected UC 1981–82 staffing: Professor, 2,862.60; Associate Professor, 1,070.49; Assistant Professor, 776.03. Total staff: 4,709.12.

The preliminary report indicates that faculty in the California segments currently are paid *more* than faculty at the comparison institutions. Specifically, faculty at UC enjoy a salary advantage of 3.07 percent, while faculty at CSUC enjoy a 7.98 percent salary advantage. These differentials are shown in Table 7.

If the Legislature wished to maintain salary parity in 1981–82 the CPEC data indicate that UC faculty should be given a 2.71 percent salary increase, and CSUC faculty should be given *no* increase. In fact, even with no increase, CSUC faculty would still receive 2.59 percent more than faculty at their comparison institutions.

The figures in Table 7 assume that the comparison institutions maintain the same rate of salary growth in 1980–81 and 1981–82 that they have over the past five years. Tables 8 and 9 show the detailed calculations, by academic rank, for UC and CSUC, respectively.

Table 9
CALIFORNIA STATE UNIVERSITY AND COLLEGES
Percentage Change in CSUC Estimated 1980–81 All Ranks Average Salary Required to Equal the Comparison Group Projections for 1980–81 and 1981–82, Based on Five-Year Compound Rate of Increase in Comparison Group Salaries (Weighted by Total Faculty by Rank in all Comparison Institutions)

Academic Rank	*CSUC Average Salaries*	*Comparison Group Projected Salaries*		*Percentage Change Required in CSUC Salaries*	
	1980–81	*1980–81*	*1981–82*	*1980–81*	*1981–82*
(1)	*(2)*	*(3)*	*(4)*	*(5)*	*(6)*
Professor	$33,359	$31,146	$32,989	−6.63%	−1.11%
Associate Professor	25,850	23,802	25,187	−7.92	−2.56
Assistant Professor	21,069	19,045	20,077	−9.61	−4.71
Instructor	18,407	14,887	15,714	−19.12	−14.63
All Ranks Average	$28,787 [a]	$26,633 [a]	$28,185 [a]	−7.48%	−2.09%
Less Turnover and Promotions		−144	−144	0.50	0.50
Adjusted Total		$26,489	$28,041	−7.98%	−2.59%

[a] Based on CSUC staffing: Professor, 5,753; Associate Professor, 3,202; Assistant Professor, 1,940; Instructor, 185. Staff Total: 11,080.

Segmental Requests and Governor's Budget

Table 10 compares the 1981–82 salary increase proposals for academic and nonacademic staff made by the two segments of higher education, CPEC, and the Governor. Each 1 percent of salary increase will cost $4.7 million for UC academic staff and $4.4 million for UC nonacademic staff. The corresponding costs for CSUC are $5.2 million and $3.3 million, respectively.

Table 10
UC and CSUC Salary Comparison Data For 1981–82
(amounts in millions)

	UC		*CSUC*		
	Percent	*Amount*	*Percent*	*Amount*	*Totals*
Segments Request	9.50%	$86.8	17.70%	$150.5	$237.3
Governor's Budget [a]	4.75	43.4	4.75	40.4	83.8
CPEC Report	2.71	24.7	−2.59	−22.0	2.7

[a] The Governor's Budget contains no recommended salary increase figure. However, a 4.75 percent cost of living increase is proposed for many other items of the budget. See accompanying text for more details.

EMPLOYEE COMPENSATION
CIVIL SERVICE, EXEMPT, STATUTORY, ACADEMIC AND NONACADEMIC EMPLOYEES—Continued

The UC Regents have requested a 9.5 percent salary increase in 1981–82, at a projected cost of $86.8 million. The Regents' salary agenda item cites projected inflation levels and other economic circumstances such as housing costs and health care as being important considerations in their salary request. The Regents' agenda states that:

"The university does not seek in this recommendation to make up for accumulated lags in real income due to inflation, nor is it the intention to index the salary request to the past or anticipated rate of inflation. Rather, 9.5 percent reflects our best judgment of the required increase for University of California faculty to retain their competitive standing."

By contrast, the CSUC Board of Trustees' request of 17.7 percent consists of an 11 percent increase to maintain current purchasing power in 1981–82 and 6.7 percent to begin to address and remedy the loss in purchasing power of the CSUC faculty during the past 12 years. The Trustees' agenda item states:

"That, since the faculty of the California State University and Colleges have fallen behind for the past 12 years and that their present salary reflects a decline of 26.7 percent in real income during this period, the Trustees hereby request the Legislature to address and remedy this decline, under a formula previously adopted which would gradually remedy this loss by an additional 6.7 percent increase."

The Governor's budget contains no recommended salary increase figure. Rather, the budget indicates that $509 million is available in the General Fund for employees' compensation and other cost-of-living adjustments. Table 10 shows what the dollar impact would be if a pay increase of 4.75 percent were granted to UC and CSUC employees. This is the same percentage increase budgeted for many programs that have statutory cost-of-living adjustments.

Table 11
Comparison Results, Segment Requests
Increase Granted State Civil Service
Increase and Changes in the U.S. Personal Consumption Deflator [a] 1969–70 through 1981–82

	CPEC Comparison Methodology Result		Segment Request		Increase Granted		State Civil Service Increase Granted	Percent Change in U.S. GNP Personal Consumption Deflator
	UC	CSUC	UC	CSUC	UC	CSUC		
1969–70	5.2	5.2	5.3	5.2	5.0	5.0	5.6	4.7
1970–71	7.2	7.0	7.2	7.0	0.0	0.0	5.2	4.4
1971–72	11.7	13.0	11.2	13.0	0.0	0.0	0.0	3.9
1972–73	13.1	13.0	13.1	13.0	9.0	8.4	9.0	4.1
1973–74	6.4	8.8	6.4	7.5	5.4	7.5	11.7	8.0
1974–75	4.5	4.2	4.5	5.5	5.5	5.3	5.3	9.7
1975–76	11.0	9.7	11.0	10.4	7.2	7.2	6.7	6.0
1976–77	4.6	4.6	4.6	7.2	4.3	4.3	6.6	5.4
1977–78	5.3	5.3	6.8	8.5	5.0	5.0	7.5	6.1
1978–79	3.3	3.3	9.3	9.9	0.0	0.0	0.0	8.0
1979–80	10.1	10.1	16.0	14.4	14.5	14.5	14.5	9.8
1980–82	5.0	0.8	10.5	11.0	9.8	9.8	9.8	10.0
1981–82	2.7	−2.6	9.5	17.7	—	—	—	9.5 est.

[a] All data, except change in GNP consumption deflator, are from CPEC salary report for 1981–82. GNP consumption data developed from federal government reports.

Past History of Increases

Table 11 shows the following data for the period 1969–70 through 1981–82:

- the yearly CPEC methodology results for UC and CSUC,
- the requests from the segments,
- the increases granted by the state for UC and CSUC,
- the salary increase for state civil service granted by the state, and
- the U.S. GNP Personal Consumption deflator.

For the past three years, the segments have received the same increase as state civil service employees.

Table 12 shows the cost of various percentage increases in faculty and nonfaculty salary.

Table 12
Funding Needed for Salary Increase for UC and CSUC Academics and Nonacademics (in millions)

Salary Change	*UC*	*CSUC*	*Totals*
−2.59 (CSUC need)[a]	NA	−$22.0	NA
+1.00[b]	$9.1	8.5	$17.6
+2.71 (UC need)[a]	24.7	NA	NA
+4.75 (Governor's Budget)	43.4	40.4	83.8
+9.50 (UC request)	86.8	80.8	167.6
+17.70 (CSUC request)	161.7	150.5	312.2

[a] CSUC and UC need based on CPEC salary report.

[b] Each 1 percent of salary increase will cost $4.7 million for UC academic staff and $4.4 million for UC nonacademic staff. The corresponding costs for CSUC are $5.2 million and $3.3 million, respectively.

AUGMENTATION FOR PRICE INCREASES

Item 982 from the General Fund and various special funds — Budget p. GG 197

Requested 1981–82	$14,829,000
Estimated 1980–81	13,146,000
Actual 1979–80	12,400,000
Requested increase (excluding amount for salary increases) $1,683,000 (+12.8 percent)	
Total recommended reduction	Pending

1981–82 FUNDING BY ITEM AND SOURCE

Item	Description	Fund	Amount
982-001-001	Price Increase Augmentation	General	$9,565,000
982-001-494	Price Increase Augmentation	Special	2,862,000
982-001-988	Price Increase Augmentation	Nongovernmental	2,402,000
Total			$14,829,000

AUGMENTATION FOR PRICE INCREASES—Continued

ANALYSIS AND RECOMMENDATIONS

Withhold recommendation, pending decision of U.S. Postal Rate Commission on anticipated postage rate increase.

This item provides $14,829,000 for price increases not included in the budget requests of individual agencies. The funds are intended to be allocated to individual department budgets based on demonstrated need.

Postage Rate Increase Is Anticipated

The Department of Finance has provided $14,829,000 in Item 982 to cover the cost to the state of an anticipated postage rate increase. This increase, if approved, would become effective in March of 1981.

Last year, the U.S. Postal Service requested a general postage rate increase averaging 33 percent above the structure of rates currently in effect. The Postal Rate Commission is expected to rule on the request by February 28, 1981.

The Department of Finance has provided $14.8 million to the General, special and nongovernmental cost funds to cover the additional costs that would result if the increase granted by the commission were equal to that requested by the Postal Service. The commission, however, indicates that the rate increase actually granted could be either higher or lower than the level initially requested. Therefore, we withhold recommendation on the amount requested for this item, pending the final decision by the commission in February.

DEPARTMENT OF FINANCE—UNALLOCATED
(Polychlorinated Biphenyls)

Item 983 from the General Fund (unsecured property tax roll) — Budget p. GG 198

Requested 1981–82	$30,000,000
Recommendation pending	30,000,000

ANALYSIS AND RECOMMENDATIONS

We withhold recommendation on Item 983-001-001, for an unallocated amount to replace polychlorinated biphenyls (PCB) substances in state facilities.

The budget includes $30 million for the purpose of containment, replacement, storage and disposal of hazardous electrical transformers and switches containing PCBs. Expenditure of this amount would be by Executive Order of the Department of Finance to various state agencies in augmentation of their respective support or capital outlay appropriations.

Neither specific state agencies that would receive these funds nor the amounts to be allocated to each is known at this time. The Governor's Budget states that a preliminary review of state facilities indicates that PCB-filled electrical equipment is currently used in facilities under the jurisdiction of the Departments of Developmental Services, Mental Health, Corrections, Youth Authority, General Services and the State University and Colleges.

The State Architect has advised us that his office is currently contracting with private consultants for the purpose of undertaking an in-depth engineering study to identify the specific location of hazardous PCB-filled electrical equipment. This study will include a survey of all state locations (approximately 94 sites), and also identify potential sites for storage of the PCB material and equipment. Presumably, one site would be located in northern California and one in southern California. The study should be completed in April or May 1981. According to the State Architect, this study will cost approximately $300,000. The source of these funds has not been identified and the expenditure has not been reported to the Legislature.

PCBs are nonflammable, insulating liquids which have been used primarily in electrical transformers and capacitors as a dielectric fluid. The PCB substances have been found to be highly toxic and can seriously harm the health of human beings if certain concentrations are ingested over certain periods of time. Consequently, the use, storage and disposal of PCB substances are strictly controlled by regulations adminisistered by the Environmental Protection Agency of the federal government. No health hazards exists when the electrical equipment encasements are tightly sealed. The problems arise from PCB substances leaking from the encasements. It is our understanding, however, that the administration's proposal is to replace all equipment containing PCB regardless of the condition of the equipment.

Because of the strict regulations regarding the handling and storage of PCB, the logistics for a program of the magnitude proposed would be complex. When a piece of equipment is removed from use, it must be properly handled and stored. Currently, the state has no storage facilities for this purpose. Thus, if the state is to store the PCBs and related equipment, such facilities must be developed and staffed before all state-owned equipment is replaced. Furthermore, transporting these items must be done carefully. We believe the Legislature should be advised of the potential state liability—in the event of spillage during transportation or storage—before approving funds for this program. An alternative to the state's transporting/storing this material would be to contract with a private firm to transport/store the material.

Complete replacement of all such electrical equipment within the budget year may be impossible because of manufacturing and delivering time for the replacement equipment. Presumably, the consultant's study will address these issues.

Until the consultant's study is completed and available for review, the magnitude of the problem of hazardous PCB equipment cannot be determined. Because PCBs were used in a high percentage of electrical transformers and capacitors manufactured between 1929 and 1971, if the state is to replace all such state-owned equipment, we would estimate that the proposed $30 million would not be adequate. On the other hand, tightly sealed electrical equipment—even though it may contain PCBs—is not hazardous and federal regulations do not require that such equipment be replaced. We recommend that these items remain in service and that the administration establish a strict system of monitoring any such equipment left in service.

Hazardous equipment identified by the consultant's study, in conformance with Environmental Protection Agency regulations should be replaced as soon as possible. We withhold recommendation on the requested amount, pending receipt and review of the consultant's study.

RESERVE FOR CONTINGENCIES OR EMERGENCIES

Item 984 from the General Fund and various special funds — Budget p. GG 199

Requested 1981–82	$4,500,000
Appropriated by the Budget Act of 1980	4,500,000
Total recommended reduction	None

1981–82 FUNDING BY ITEM AND SOURCE

Item	Description	Fund	Amount
984-001-001	Reserve for Contingencies or Emergencies	General	$1,500,000
984-001-494	Reserve for Contingencies or Emergencies	Special	1,500,000
984-001-988	Reserve for Contingencies or Emergencies	Nongovernmental Cost	1,500,000
984-011-001	Reserve for Contingencies or Emergencies (Loans)	General	(2,500,000)
Total			$4,500,000

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. General Services Exemption. Recommend deletion of language exempting appropriations from the Service Revolving Fund from appropriation limits. 1672

ANALYSIS AND RECOMMENDATIONS

The budget proposes appropriations totaling $4,500,000, consisting of $1,500,000 each from the General Fund, special funds and nongovernmental cost funds, by the Department of Finance to state agencies for expenses resulting from unforeseen contingencies and emergencies not covered by specific appropriations.

Item 984-011-001 appropriates an additional $2,500,000 to provide for temporary loans to state agencies whose operations are in danger of being curtailed because of delayed receipt of reimbursements or revenue. The loans are to be repaid or accrued for repayment by the end of the fiscal year in which they are made.

Legislature Strengthened Control and Reporting Provisions

Prior to 1978–79, the annual Budget Act contained a single item which appropriated $1.5 million from the General Fund to enable the Department of Finance to allocate funds to state agencies for unforeseen contingencies and emergencies. The Legislature strengthened control and reporting provisions regarding such expenditures by adding language to the 1978 Budget Act which:

1. Separately defined emergencies as those situations which, in the judgment of the Director of Finance, require immediate action to avert undesirable consequences, or to preserve the public peace, health or safety.
2. Required that the Legislature be notified within 10 days of such an emergency expenditure.
3. Separately defined contingencies as situations which, in the judgment of the Director of Finance, constitute cases of actual necessity.
4. Required that 30-days advance notification be given to the Legislature before contingency expenditures are authorized.

The Legislature also added two separate items to the 1978 Budget Act in order to apply the same definitions, procedures and appropriation limits to special and nongovernmental cost funds, except the Service Revolving Fund (Department of General Services), which was exempted from the appropriation limits. As a result, for the first time, special and nongovernmental cost funds were subject to the same legislative oversight regarding emergency and contingency expenditures as the General Fund.

The Legislature further strenghtened its fiscal control by adding language to the 1979 Budget Act prohibiting General Fund loans under provisions of the Reserve for Contingencies or Emergencies which would require repayment from a future legislative appropriation. The improved control and reporting provisions are contained in the 1981 Budget Bill.

Appropriation Unlikely to Meet All Demands on the Reserve

The $1.5 million appropriation from the General Fund is a token amount which has been significantly less than actual deficiencies in every year since 1959–60. To satisfy actual requirements, a deficiency appropriation must be enacted toward the end of each fiscal year.

Table 1 displays the amounts budgeted and allocated for contingencies or emergencies, along with the deficiency appropriations from the General Fund since 1971–72. The table shows that the Department of Finance anticipates a deficiency appropriation of $18.6 million for the current year. This amount would supplement the $1.5 million appropriated for the current year for contingencies and emergencies in the 1980 Budget Act. The total amount available would then be $20.1 million. As of January 1981, the department anticipated or had approved allocations to state agencies of $19,004,553, which would leave a balance of $1,095,447 for unforeseen contingencies and emergencies for the remainder of 1980–81. Typically, however, total allocations and the deficiency appropriation are substantially higher than the amounts estimated in the Governor's Budget.

Table 1
Reserve for Contingencies or Emergencies
Appropriations and Allocations from the General Fund
1971–72 to 1981–82

	Appropriated	*Allocated to Agencies*	*Deficiency Appropriation*
1971–72	$1,000,000	$4,993,871	$4,918,009
1972–73	1,000,000	8,076,724	7,500,000
1973–74	1,500,000	5,644,544	10,900,000
1974–75	1,500,000	15,112,367	14,700,000
1975–76	1,500,000	24,918,959	30,520,089
1976–77	1,500,000	11,200,217	11,550,000
1977–78	1,500,000	18,969,869	17,500,000
1978–79	1,500,000	12,192,578	11,000,000
1979–80	1,500,000	26,207,778	25,646,471
1980–81	1,500,000	19,004,553[a]	18,600,000[b]
1981–82 (proposed)	1,500,000	—	—

[a] Total amount of current-year allocations made and anticipated by the Department of Finance as of January 1981.
[b] Estimated.

Table 2 displays corresponding information with respect to special and nongovernmental cost funds since 1978–79, the first year in which legislative control and oversight was extended to these funds.

RESERVE FOR CONTINGENCIES OR EMERGENCIES—Continued

Table 2
Emergency Fund Appropriations and Allocations from Special and Nongovernmental Cost Funds
1978–79 to 1981–82

	Special Funds			*Nongovernmental Cost Funds*		
	Appropriated	*Allocated to Agencies*	*Deficiency Appropriation*	*Appropriated*	*Allocated to Agencies*	*Deficiency Appropriation*
1978–79	$1,500,000	$253,817	—	$1,500,000	$675,711	—
1979–80	1,500,000	821,310	—	1,500,000	6,271,858	5,300,000
1980–81	1,500,000	187,051[a]	—	1,500,000	383,619[a]	—
1981–82 (proposed)	1,500,000			1,500,000		

[a] Total amount of current-year allocations made and anticipated by the Department of Finance as of January 1981.

Other Deficiencies

As indicated in Table 1, the budget proposes a deficiency appropriation of $18.6 million to supplement the amounts appropriated in the 1980 Budget Act for defraying contingency or emergency expenses. The budget proposes additional deficiency appropriations totaling $118,953,613 ($114,616,682 General Fund) for 1980–81 in the budgets of various individual agencies. These deficiencies are detailed on pages GG 203 and 204 of the Governor's Budget. Of the total amount, $102,520,446 is allocated to the Department of Health Services for the Medi-Cal program. The Medi-Cal funds are requested for additional caseload, other workload increases, and delayed receipt of federal funds pending certification of the Medi-Cal claims processing system.

Service Revolving Fund Deficiencies Not Reported

We recommend the deletion of language in Item 984 which exempts appropriations from the Service Revolving Fund from the appropriation limits for contingencies and emergencies.

As discussed earlier, the appropriation limits in Item 984 do not apply to allocations for emergencies and contingencies from the Service Revolving Fund. However, the Department of Finance is required to follow the same notification procedure with respect to all such allocations from this fund, pursuant to language which has been included in each Budget Bill since 1978.

The Department of Finance has authorized increases in the Budget Act appropriations from the Service Revolving Fund amounting to $2,201,850 in 1978–79 and $1,826,554 in 1979–80. Our analysis indicates that these deficiency authorizations were unnecessary because the Service Revolving Fund had unexpended balances of $33,687,138 in 1978–79 and $13,431,499 in 1979–80. In addition, the Department of Finance has not complied with the notification procedure when approving contingency or emergency appropriations from this fund. In order to ensure the reporting of such augmentations, we recommend the deletion of the language exempting the Service Revolving Fund appropriations from the limit.

Department of Finance

DEVELOPMENT OF INFORMATION TECHNOLOGY

Item 985 from the General Fund — Budget p. GG 205

Requested 1981–82	$5,000,000
Estimated 1980–81	—
Actual 1979–80	—
Total recommended reduction	$5,000,000

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

Analysis page

1. ***Delete Item. Reduce by $5 million.*** Recommend deletion of item because established procedures provide a more appropriate method for funding EDP projects. 1673

GENERAL PROGRAM STATEMENT

Item 985 proposes a new program under which the Department of Finance would administer information technology demonstration projects and support statewide electronic data processing (EDP) projects. The Governor's Budget states that legislation is being proposed to establish an Information Technology Revolving Fund as a vehicle to finance selected projects. Savings generated by these projects would be used to replenish the fund.

ANALYSIS AND RECOMMENDATIONS

The budget proposes a General Fund appropriation of $5 million for the development of information technology. These funds would be transferred to the Information Technology Revolving Fund for allocation to specific projects. In accordance with control language proposed in Item 985, the fiscal committees and the Joint Legislative Budget Committee would be notified at least 30 days prior to any allocation from the fund. This notification would include an explanation of the necessity for the allocation.

We have discussed the proposed program with the Chief of the State Office of Information Technology (SOIT) in the Department of Finance, the office which would administer the program. According to SOIT, proposals would be solicited from state agencies to fund EDP projects for which no funding has been specifically provided in the budget. From these proposals, SOIT would select those which offered the greatest potential for savings, and fund their development costs from the Information Technology Revolving Fund. Departments receiving "grants" would be required to reimburse the fund from savings generated by project implementation. All projects would have to be supported by an approved feasibility study report prepared in accordance with the State Administrative Manual (Section 4920 et seq.).

Proposed Program Circumvents Established Procedures

We recommend that Item 985 be deleted, for a General Fund savings of $5 million, because estlablished procedures provide a more appropriate method for funding EDP projects.

The Legislature has given the Department of Finance broad authority to control the state's uses of EDP technology. This authority is expressed in Section 11710 et seq. of the Government Code. The Legislature has also established in Government Code Sections 11700 and 11701 the policy of encouraging the appropriate uses of

DEVELOPMENT OF INFORMATION TECHNOLOGY—Continued

EDP technology to improve the effectiveness of state programs. In addition, the State Administrative Manual contains detailed EDP policies and procedures which are intended to guide departments in the implementation of the Legislature's general policy direction.

Taken as a whole, existing legislative and administrative policies and the state's *normal* budgeting procedures provide a more appropriate framework within which state agencies may justify requests for funding of EDP projects. This budget proposal is not consistent with the established framework because it would allow departmental expenditures for *unspecified* EDP projects from the Information Technology Revolving Fund without the benefit of review by the legislative fiscal committees.

Although control language proposed in Item 985 requires the Department of Finance to notify the Legislature of any proposed expenditure, we believe that this procedure would not be a desirable substitute for the Legislature's traditional method of reviewing all proposed departmental expenditures at the time the budget is heard. Also, the statement in the Governor's Budget that the program is necessary to support projects ". . . for which implementation funding is not currently available . . . " is contradicted by the fact that $5 million *is* proposed to fund such projects.

Throughout this *Analysis*, we make recommendations relative to funding of EDP projects and related computing equipment. In numerous instances, significant deficiencies in departmental proposals for new information systems have been identified. Some of these new systems are very costly and have a significant impact on departmental operations. Careful planning and thorough review of these projects is essential, and legislative review of such projects must be maintained.

For all of these reasons, we recommend that the funds be deleted. Instead we suggest that if the administration knows of any EDP projects "for which implementation funding is not currently available," it submit these projects to the Legislature in the form of a budget amendment, so as to allow for normal legislative review and approval. The savings resulting from our recommendation would be "available" to fund those projects that are justified.

UNALLOCATED CAPITAL OUTLAY

Item 986-30 from the General Fund, Special Account for Capital Outlay — Budget p. GG 206

Requested 1981–82	$400,000
Recommended approval	400,000

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

This item provides $400,000 for preliminary planning of projects proposed to be financed from the General Fund, Special Account for Capital Outlay, in 1982–83. The funds would be allocated by the Department of Finance. An item for this purpose has historically been included in the Budget Bill. The proposed amount would provide for approximately $27 million in construction for new project proposals, assuming the historical ratio of planning to construction (1.5 percent). A program of this magnitude seems reasonable.

AUGMENTATION FOR OFFICE OF ADMINISTRATIVE LAW SERVICES

Item 988 from the General Fund and various funds — Budget p. GG 211

Requested 1981–82	$3,500,000
Estimated 1980–81	3,500,000
Actual 1979–80	-0-
Requested increase (excluding amount for salary increases) None	
Total recommended reduction	None

1981–82 FUNDING BY ITEM AND SOURCE

Item	Description	Fund	Amount
988-001-001	Support of various General Fund agencies	General	$2,300,000
988-001-494	Support of various special fund agencies	Special	1,100,000
988-001-988	Support of various nongovernmental cost fund agencies	Nongovernmental cost	100,000
Total			$3,500,000

GENERAL PROGRAM STATEMENT

Chapter 567, Statutes of 1979 (AB 1111), established the Office of Administrative Law as an independent state agency to provide executive branch review of all proposed and existing regulations promulgated by other state agencies. In addition, Chapter 567 requires that state agencies review all of their current regulations. The statute also requires that each of the 25 titles in the Administrative Code be reviewed by specified dates, ranging from June 30, 1981 to June 30, 1986. (The OAL workplan, however, calls for all agencies to have completed the review of their regulations by July 31, 1982.) Finally, the law provides for various departments to reimburse the OAL for review services.

ANALYSIS AND RECOMMENDATIONS

We recommend approval.

The Department of Finance is proposing $3.5 million as an "augmentation for OAL services" to be made available to state agencies unable to absorb the "incremental 1981–82 internal regulations review costs." The $3.5 million proposed would be split among the General Fund ($2.3 million), special funds ($1.1 million) and nongovernmental cost funds ($100,000) to broadly reflect the existing split of support of state agencies promulgating regulations. These funds would be allocated by the Department of Finance to state agencies unable to absorb the cost of reviewing their regulations in accordance with Chapter 567.

The 1980 budget Act also appropriated $3.5 million for this purpose. The Legislature added control language requiring that 30 days' notice be given to the Legislature before these funds could be expended. The same control language is included in the 1981 Budget Bill.

As noted in our analysis of OAL (Item 891-001-001), the Legislature authorized

AUGMENTATION FOR OFFICE OF ADMINISTRATIVE LAW SERVICES—Continued

the Department of Finance to allocate $1,488,010 of the $3.5 million appropriation directly to the OAL, because it was infeasible for OAL to incorporate its start-up costs into a relatively few agency billings. The Governor's Budget indicates that $1,439,400 of this amount will be expended by OAL in the current year, leaving a balance of $2,060,600 for allocation during the remainder of the current year to agencies which are unable to absorb their internal review costs during 1980–81.

The total amount of increased agency cost resulting from Chapter 567 has not yet been determined. However, to assure that the cost of implementing Chapter 567 is held to a minimum, we recommend that the Department of Finance allocate the funds based on the following criteria:

1. ***Agencies should be required to meet the new workload requirements with existing resources.***
2. ***Additional funds should be allocated only in those situations where existing staff is clearly not capable of meeting statutory deadlines.*** If, on an agency-by-agency basis, the Director of Finance believes additional resources are required to meet short-term costs such as overtime or clerical assistance, the funds from the proposed augmentation should be used.

CONTROL SECTIONS

Sections 4 through 37 of the Budget Bill are the so-called "control sections" which place limitations upon the expenditure of certain appropriations, extend or terminate the availability of certain specified prior appropriations, define the authority of the Director of Finance with respect to reductions and transfers within and between categories of expenditure and contain the usual severability and urgency clauses.

Although significant fiscal policy is contained in these sections, particularly with respect to extending the availability of prior appropriations, these sections have not been received by us in time to permit adequate review for purposes of recommendations to be incorporated in this analysis. These control sections will be analyzed and a recommendation thereon made to the committees in hearings on the Budget Bill.