

# 2003-04 Budget and Local Government



Legislative Analyst's Office

March 14, 2003

# What's the Magnitude of the Problem?

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- ▶ **Estimates of the budget shortfall range from \$27 billion to 35 billion**
- ▶ **Differences due primarily to definitional reasons**

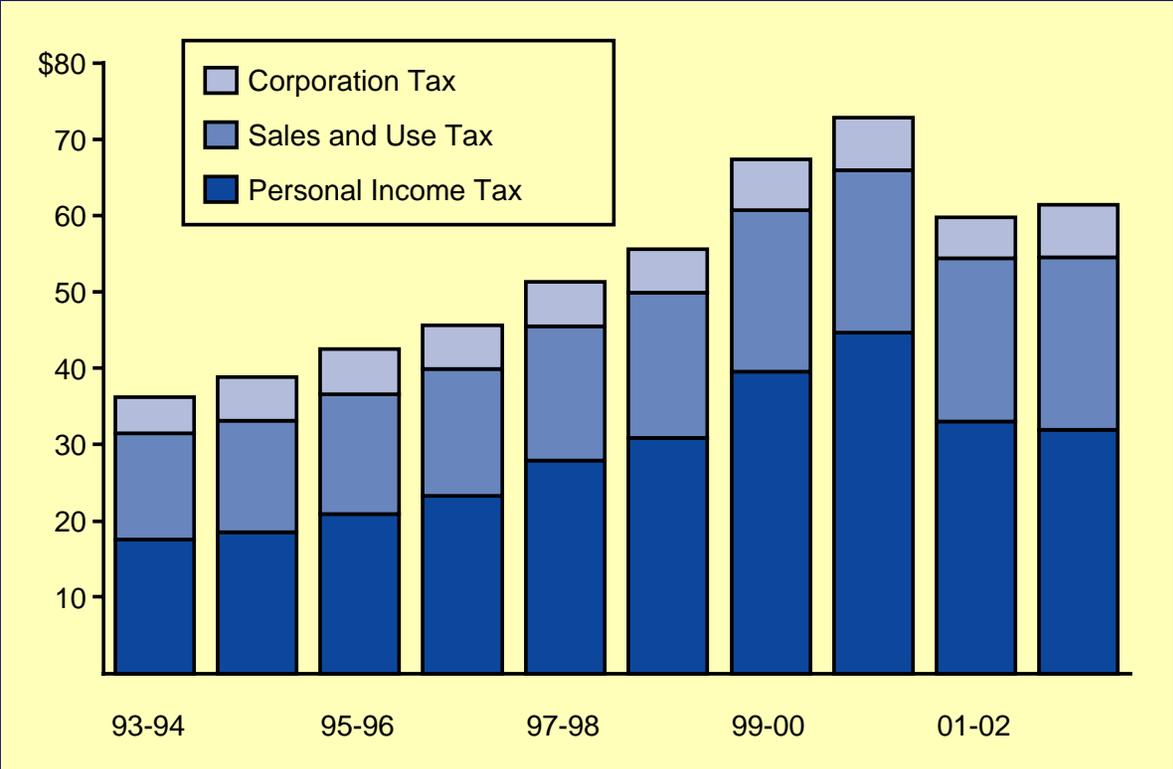
# How Did Such a Problem Arise?

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- ▶ **Passage of *2002-03 Budget Act* left an underlying problem of over \$10 billion**
- ▶ **Deterioration in state's revenue performance**

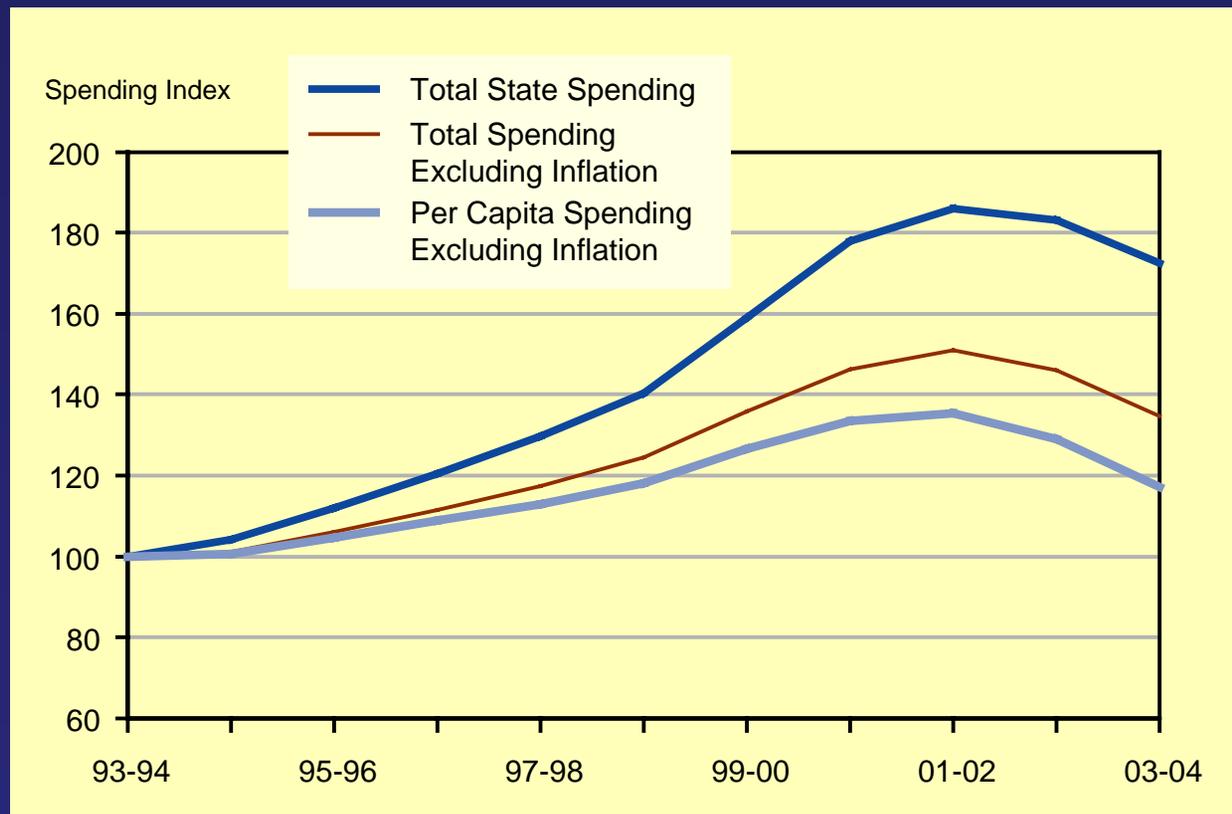
# California's Dramatic Revenue Fall-off

General Fund Revenues From Major Taxes  
(In Billions)



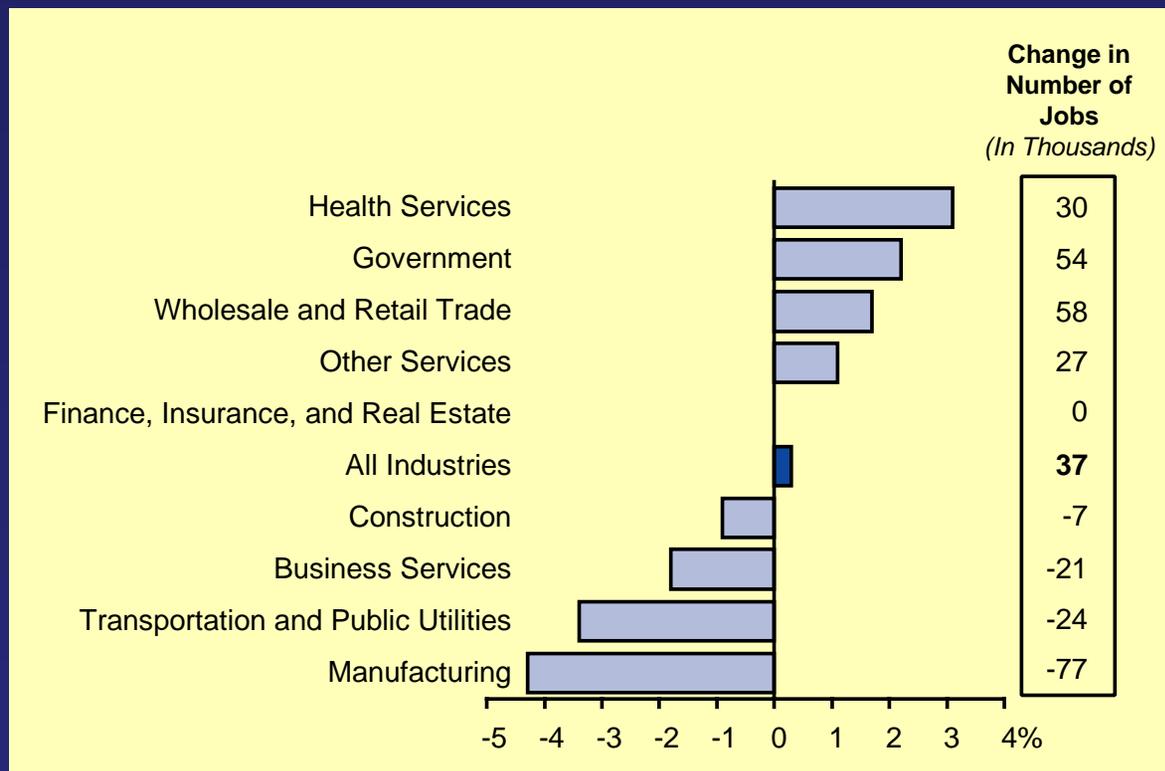
# Spending Adjusted for Inflation And Population

Index Value = 100 in 1993-94



# California's Job-Gaining and Job-Losing Industries in 2002

Percent Change in Jobs  
December 2001 Through December 2002



# Governor's Proposed Solutions

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	<b>Amount (Billions)</b>	<b>Percent of Total</b>
<b>Program savings</b>	<b>\$13.7</b>	<b>40%</b>
<b>Realignment</b>	<b>8.2</b>	<b>24</b>
<b>Shifts to local governments</b>	<b>5.1</b>	<b>15</b>
<b>Shifts/Transfers/Loans</b>	<b>7.6</b>	<b>21</b>

# State Revenues in 2003-04

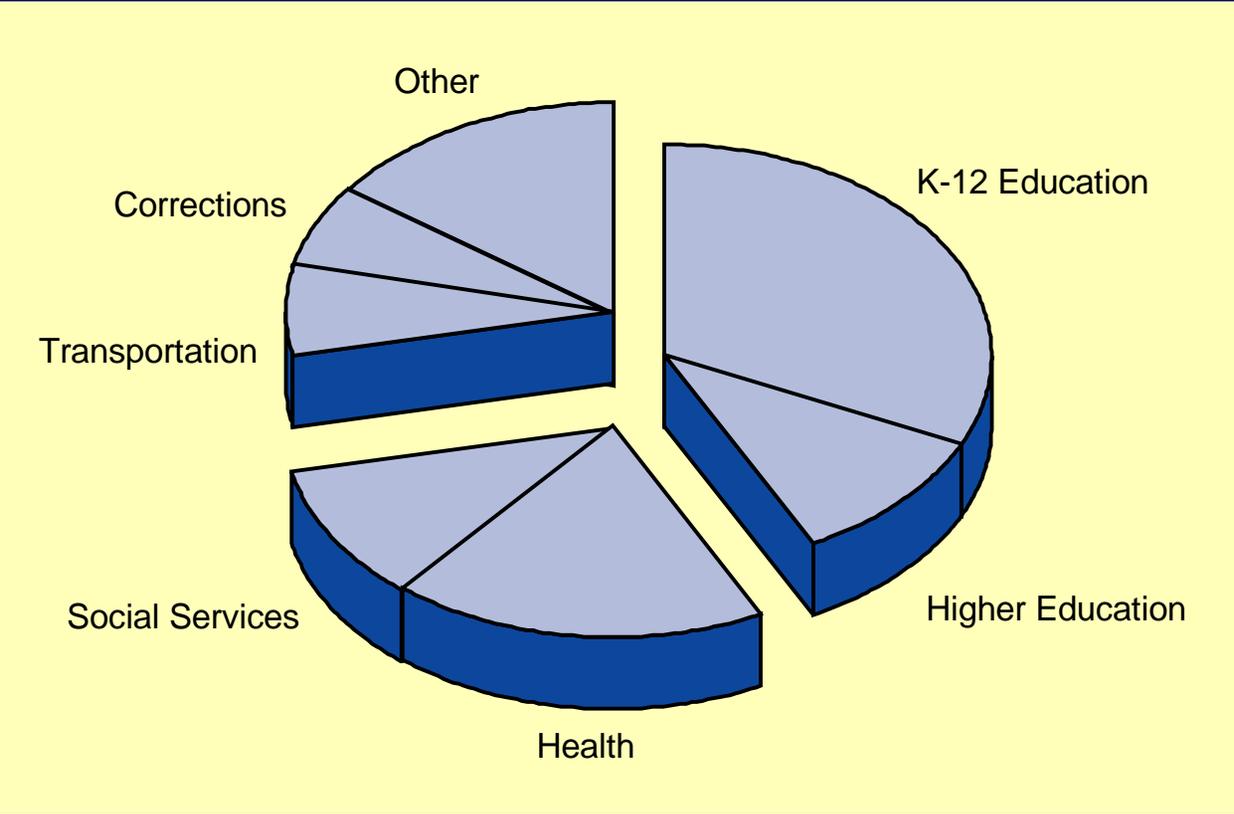
(In Billions)

General Fund Revenues	Total State Revenues \$96.1 Billion	Special Funds Revenues
Personal Income Tax \$33.6		Proposed Realignment Revenues \$8.2
Sales and Use Tax 23.2		Motor Vehicle-Related Taxes 7.6
Corporation Tax 6.4		Sales and Use Tax 2.5
All Other 6.0		Tobacco-Related Taxes 2.0
<b>Total</b> <b>\$69.2</b>		All Other 6.7
		<b>Total</b> <b>\$26.9</b>



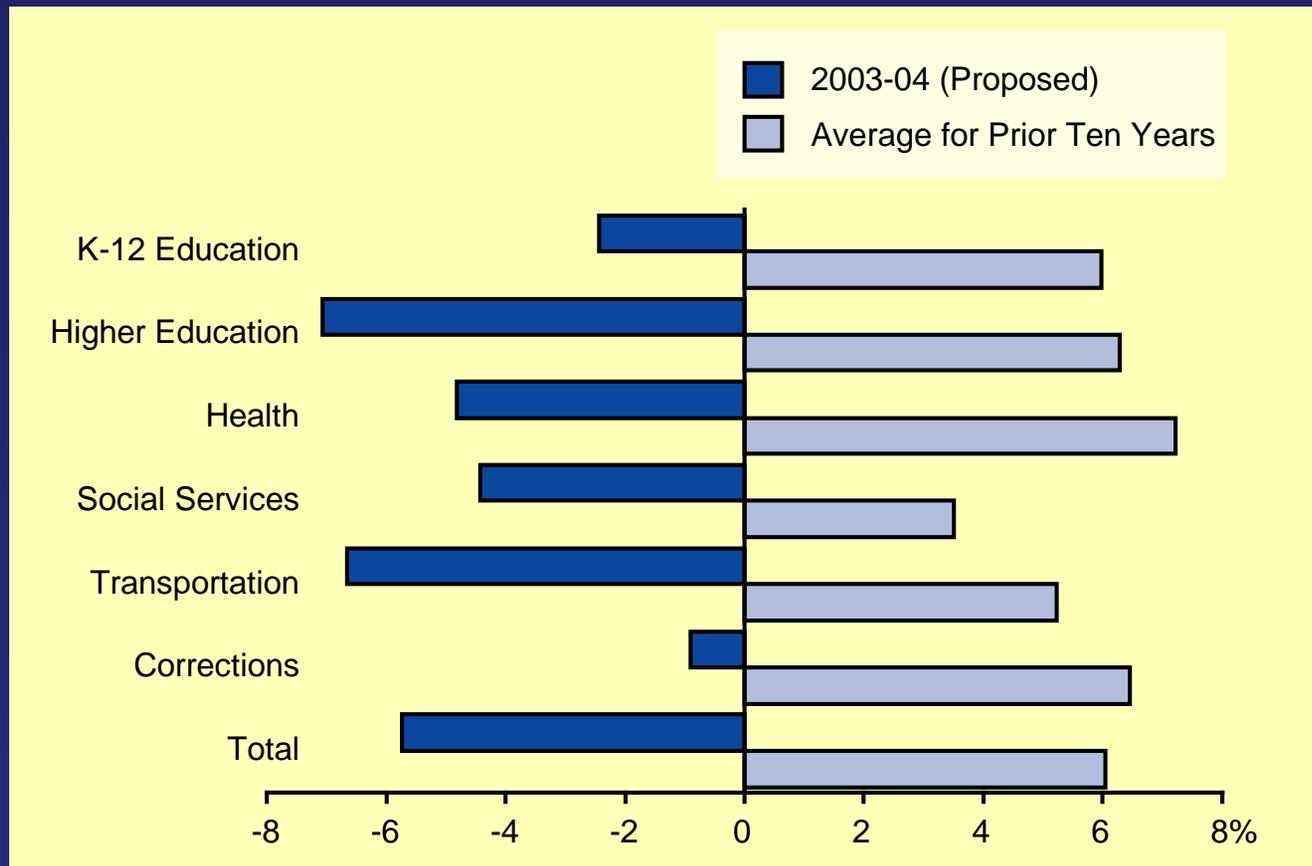
# Proposed Total State Spending By Major Program Area

2003-04



# Growth in Total State Spending By Major Program Area

Annual Percent Change • 2003-04 and Prior Ten Years



# LAO Assessment of Governor's Budget

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- ▶ **If Fully Adopted, Budget Is Balanced**
- ▶ **Balance Achieved Only If Dramatic Actions Taken**
- ▶ **Many Threats Exist**

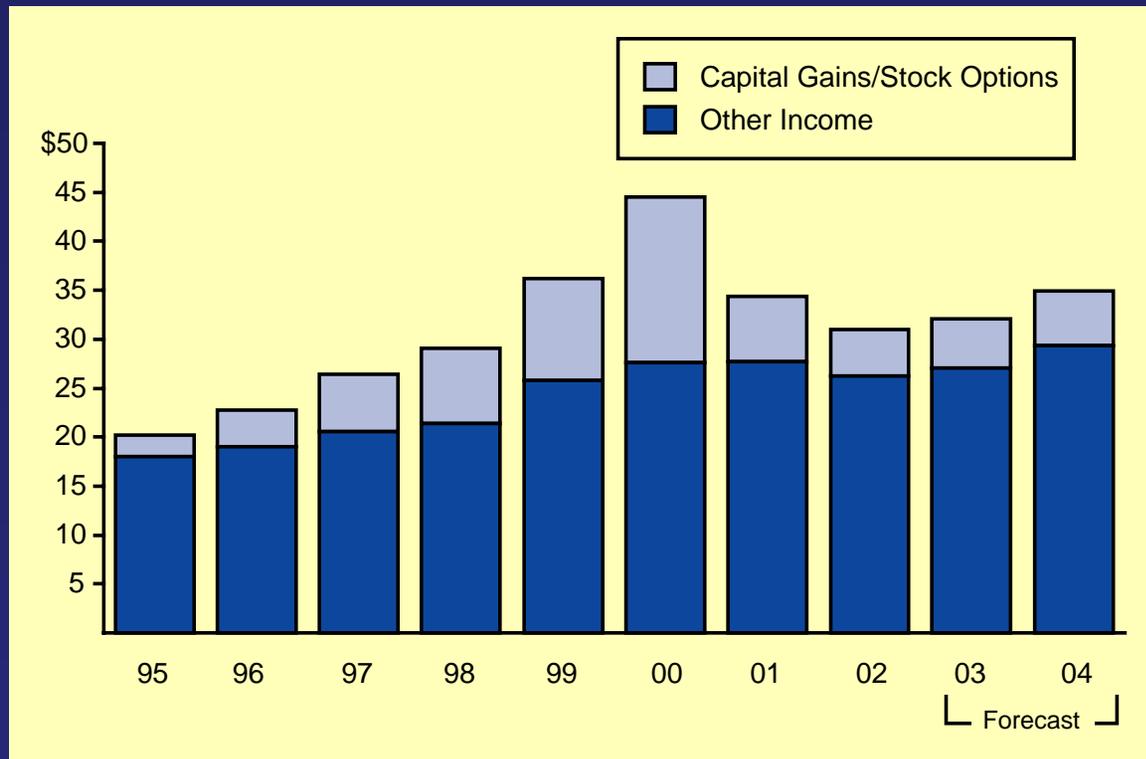
# Solving the Budget Puzzle

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- ▶ **Budget Gap About a Third of Spending**
- ▶ **Ongoing Budget Problem: \$18 Billion**
- ▶ **Proposition 98 “Takes” Half of New Taxes**
- ▶ **Need Two-Thirds of Legislature**
  - **Pass Budget**
  - **Raise Taxes**

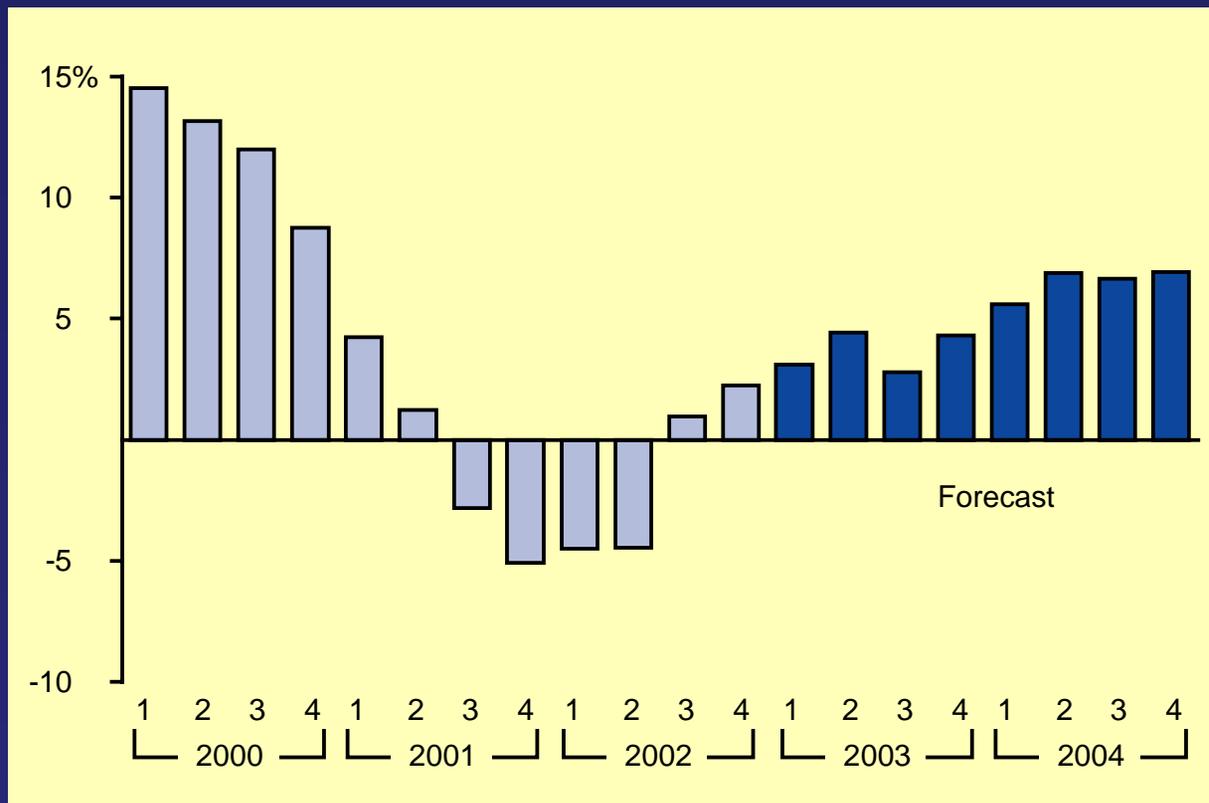
# After Plunging, PIT Liabilities to Grow Moderately

California Annual PIT Liabilities, by Source  
(In Billions)



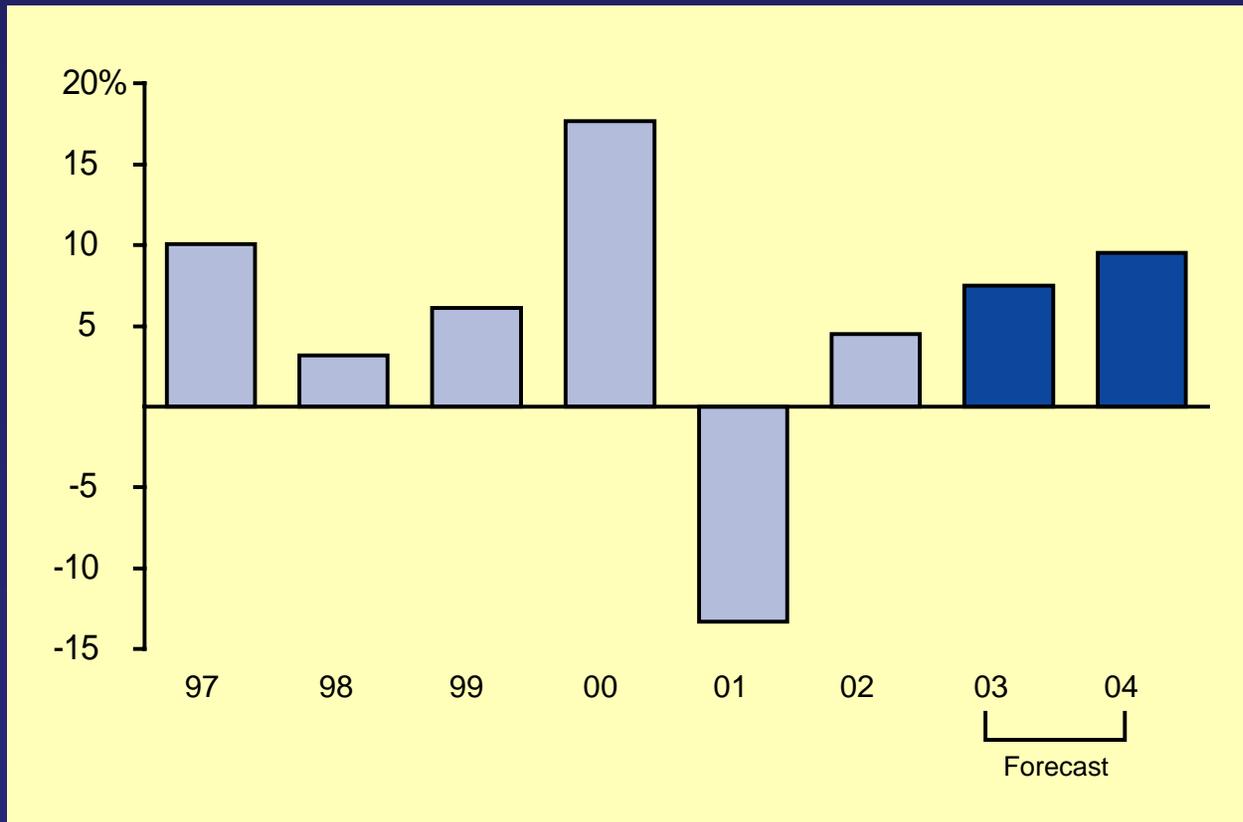
# Taxable Sales Slowly Improving

Year-to-Year Percent Change, by Quarter



# Profits on Upswing

Percent Change in California Taxable Corporate Profits



# Local Government Plays Major Role in State Budget Solutions

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<b>\$8.20 Billion</b>	<b>Realignment</b>
<b>4.20</b>	<b>VLF Backfill</b>
<b>1.20</b>	<b>Mandates</b>
<b>.75</b>	<b>Redevelopment</b>
<b>.30</b>	<b>Other</b>

# Realignment in Nut Shell

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- ▶ **Increases Taxes**
  - Sales Tax
  - Personal Income Tax
  - Cigarette Tax
- ▶ **Shifts Program Responsibilities and Funding**
- ▶ **Taxes Not Counted Under Proposition 98**

# Key Question

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**Would Some Programs Benefit From  
Decentralized Program Control?**



# Which Programs Would Benefit From Local Control?

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*“We should... know over which matters local tribunals are to have jurisdiction and when authority should be centralized . . .”*

**Aristotle's Politics**



# Programs Usually Better Controlled and Funded by **State**

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## ▶ **Programs Where:**

- Statewide Uniformity Vital
- Statewide Objectives Are Overriding Concern
- Purpose Is Income Redistribution

## ▶ **Why State Control?**

- Reduces Inappropriate Service Level Variation

# Programs Usually Better Controlled and Funded by **Counties**

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## ▶ **Paramount**

- Innovation
- Responsiveness to Community Interests
- Efficiency

## ▶ **Why Local?**

- Facilitates Access to Decision-making Process
- Allows Community Standards and Priorities to Influence Allocation of Scare Resources

# What About “Linked” Programs?

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- ▶ **Often Programs Come in Clusters**
- ▶ **Better For One Government To Control All**
- ▶ **Why One Government?**
  - **Reduces Incentives for Cost Shifting Among Programs**
  - **Fosters Cross-Program Collaboration**

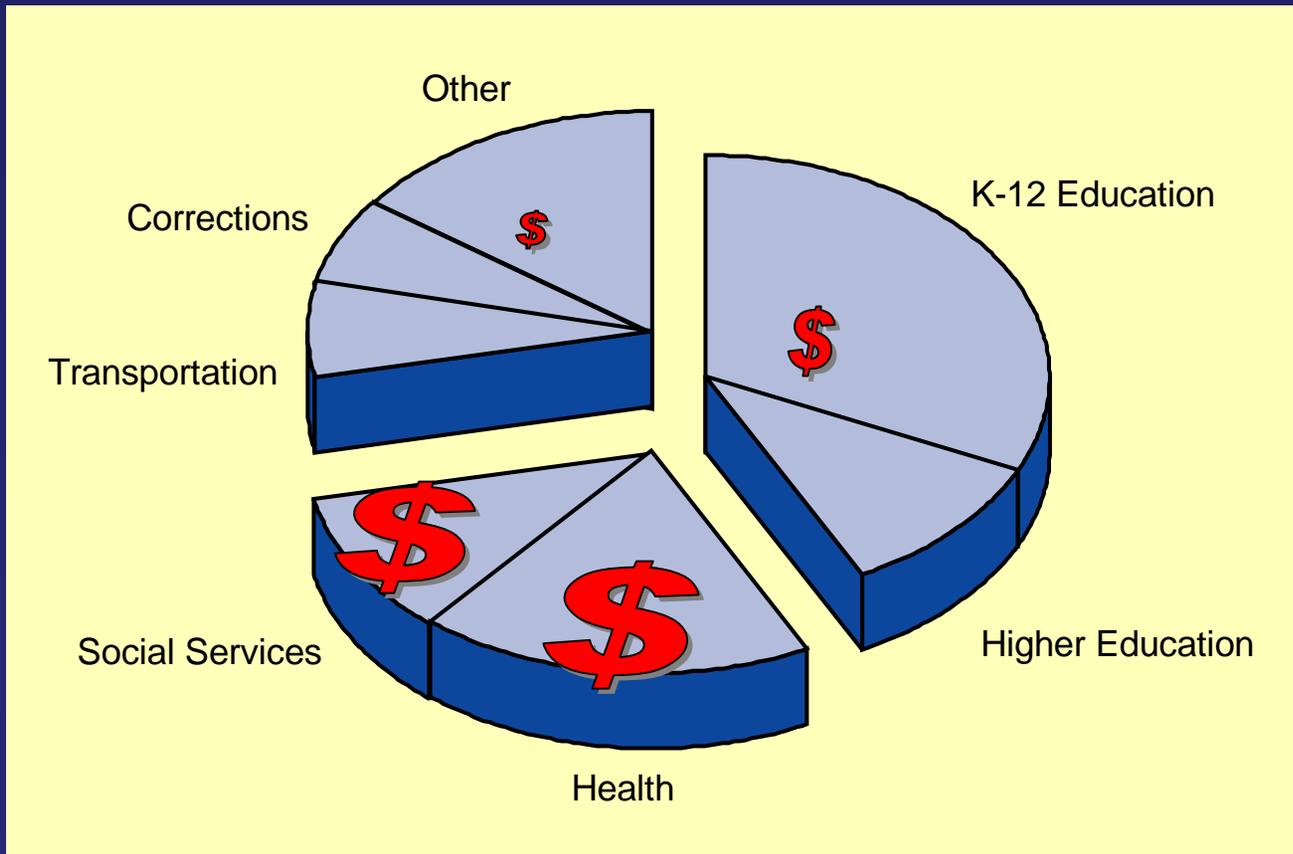
# What If Program Responsibility Must Be Shared?

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- ▶ **Cost Shares Should Reflect Level of Control for Program and Related Programs**
- ▶ **Why?**
  - Promotes Efficiency in Expenditures
  - Discourages Inappropriate Cost Shifting
  - Increases Accountability to Public

# Governor's Realignment Reduces State Spending by \$8.2 Billion

Programs in Proposed 2003-04 Budget Affected by Realignment



# Overarching Considerations

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## ▶ Programs, Not Taxes, Should Be Focus

- Long Term Change
- State Has Other Options

## ▶ Counties Need Program Control

- Realize Benefits of Local Control
- Align Program Costs and Revenues





# Overarching Considerations

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## ▶ Roughly Match Revenues and Spending

- Realigned Program Growth: 7% to 8%
- *Long Term* Revenue Growth: 5.5% to 6%
- One-time Revenue Drop Off in 2004-05

## ▶ Details Matter

- Funding Allocations, Pots, Reserve, Timing, Outcome Measurement, 1991 Realignment

## ▶ Achieving Consensus Critical

# Which Programs Should Legislature Consider for Realignment?

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- ▶ **Administration's List — \$5.1 Billion**
- ▶ **LAO Identified Programs — \$4 Billion**
- ▶ **Notes**
  - **Not All Changes Possible by July 1, 2003**
  - **Many Issues Still To Be Resolved**

# Health Programs

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## *Administration*

**Medi-Cal Benefits**  
**Medi-Cal Long Term Care**  
**Public Health**  
**Services For Homeless**  
**System of Care**  
**Substance Abuse**  
**Treatment**  
**Drug Courts**

## *LAO*

**Medi-Cal Administration**  
**Other Long Term Care**  
**Women's Shelter**  
**EPSDT**  
**Mental Health Managed Care**  
**Other Mental Health**

# Social Services Programs

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## *Administration*

**Child Welfare Services**  
**Foster Care—grants and Administration**  
**Adoptions Assistance**  
**Adult Protection**  
**Kin-GAP**  
**Cal Works—administration and Services**  
**Food Stamp—administration**  
**IHSS**  
**Programs for Immigrants**

## *LAO*

**Adoptions Program**  
**Cal WORKS Grants**  
**Automation Projects**

# Other Programs

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## *Administration*

**Child Care**  
**Court Security**

## *LAO*

**Juvenile Justice**  
**Adult Parole and Return to  
Custody**  
**Cops/ Challenge Grants**  
**13 Mandates**

# Vehicle License Fee Proposal

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- ▶ **Budget proposed to eliminate backfill to local governments (non-realignment)**
- ▶ **LAO position:**
  - Inappropriate for locals to “pay” for state tax relief
  - Would cause significant disruption to local budgets

# VLF—Current Status

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- ▶ **Recent opinion made public that the Director of Finance can pull the trigger**
- ▶ **Not clear if and/or when action will result**
- ▶ **Not clear whether it will be challenged**

# Mandates

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- ▶ **Budget proposes deferring payment on all general government mandates**
  - Total liability of \$1.2 billion by end of 2003-04
- ▶ **LAO: Recommend either:**
  - Funding these mandates or
  - Suspending or deleting them

# Redevelopment

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- ▶ **Budget proposes:**
  - One-time \$500 million hit
  - Ongoing shift—beginning at \$250 million
- ▶ **LAO Options:**
  - One-time hit could be backfilled with bond funds

# Other Local Government Proposals

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- ▶ **Williamson Act Open Space**
  - Budget deletes all funding
  - LAO: phase out over time
  
- ▶ **Booking Fee Reimbursements to Cities**
  - Budget eliminates
  - LAO: raised no issues

# What Next?

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- ▶ **Usually: Hearings, May Revision, Conference, Budget by Early Summer**
- ▶ **2003 So Far**
  - Hearings, Many “No Action”
  - Little Action on Realignment
  - Current-Year Cuts