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CWDA

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To: All County Social Service Directors and Fiscal Officers

From: CWDA Staff

Pages: 1

RE: State Budget Update #23 – Legislature Approves Majority-Vote Democratic Budget Package

Today both houses of the Legislature approved, by a majority vote, an \$18 billion package developed by Democrats that includes \$7.3 billion in budget cuts, \$9.3 billion in tax increases, and \$1.5 billion in other solutions to address the state's budget crisis. The package is intended to soften the impacts of the state's decision yesterday to halt funds for thousands of public works projects statewide. Democrats indicated their proposal would accelerate the availability of bond funds for "ready-to-go" infrastructure projects. The proposal comes after weeks of tense negotiations between Democrats and Republicans on bridging a projected \$40 billion shortfall over 18 months. Democrats called this a "stop the bleeding" package, and noted it does not eliminate the need to find further budget solutions in 2009.

The entire budget package included 17 bills, some of which were approved by simple majorities, others approved by supermajorities. The revenue bills, SB 2X and SB 9X, were approved by simple majority votes of Democrats in each house. The health and human services trailer bill, which implements the SSI/SSP and CalWORKs COLA cuts noted below, was approved by a supermajority.

Though state law requires taxes to be passed by a two-thirds supermajority of each legislative house, Democrats contend their tax hikes require a majority vote because they would be revenue-neutral within a single bill. The bill reduces sales and excise taxes on gasoline, and then raises an equivalent amount in general sales tax, oil severance tax, and a personal income tax surcharge. Republicans objected to the package on policy grounds, disputed the legality of enactment without a supermajority, and promised to pursue a lawsuit to overturn the package. On Wednesday the Governor asked for contracting reform and more permanent cuts as his price for approving the budget, but Democrats said they would not wait for a deal before moving forward. The Governor has not indicated whether he will sign or veto the package.

Revenue Changes

The Democrats' plan eliminates gasoline sales and excise taxes used for transportation purposes, and replaces those taxes with a mix of taxes (sales, oil severance and personal income surcharge) that will be used to bolster the General Fund. This action will bring \$5.7 billion into the General Fund.

To replace the transportation dollars, the Democratic plan institutes a “user fee” of 39 cents for gasoline consumption in California. The new fee would increase the amount of funds for the state highway account by \$500 million annually and for local streets and roads by \$643 million annually. In addition, the fee will be indexed to adjust with inflation. Because it is a user fee, the revenues have to be used for transportation purposes.

In addition, the Democratic plan reworks the “triple flip” enacted in 2004. The “triple flip” increased the state sales tax by a quarter cent, reduced local sales tax by a quarter cent and shifted property taxes from schools to local governments to make up for loss in local sales tax money. The state General Fund backfilled schools for the loss of property tax money.

The Democratic plan ends the local quarter cent local sales tax reduction, eliminating the need to shift property tax from schools to local governments, thereby ending the General Fund obligation to backfill school funding. The result is an additional \$1.5 billion to the General Fund.

Additionally, the Democratic plan establishes new 3 percent income tax withholding requirements for independent contractors. Specifically, the plan requires businesses to withhold 3 percent of payments they make to independent contractors exceeding \$600 each year, relieving businesses from having to file 1099 forms. This action generates \$2 billion for 2009-10.

The net effect of these tax changes would be:

- The sales tax will rise three-quarters of a percent.
- Many taxpayers will pay an additional 2.5 percent on their income tax bills.
- Independent contractors will have 3 percent income tax withheld.
- Motorists will see an increase of 13.5 cents per gallon of gasoline.

Budget Cuts

Health and Human Services:

- SSI/SSP. Reduces SSI/SSP grants in 2009 back to the 2008 level and suspends the budget year state COLA. Together these actions will save about \$177 million in the current year and about \$500 million in the budget year.
- CalWORKs. Suspends the budget year CalWORKS COLA to save about \$100 million.
- Regional Centers. Reduces, by three percent, certain payments for services delivered to individuals with developmental disabilities for the period from December 1, 2008 to June 30, 2010, as proposed by the Governor. This results in a reduction of \$26 million General Fund for 2008-09 and \$60 million in 2009-10.
- Also reduces the Regional Center Operations’ budget by \$3 million General Fund in 2008-09 and \$12.2 million in 2009-10 by suspending certain case management ratios and administrative requirements.

Education:

- Current Year Reductions. Reduces Proposition 98 spending by the \$2.5 billion level proposed by the Governor. However, this package of reductions does not follow the Governor's proposal to cut school district revenue limits, and instead targets specific programs that mitigate direct impacts on classroom instruction.
- Settle-Up Solutions. Adopts a variation of the LAO's proposal to count a portion of current year spending as "settle-up" dollars rather than Proposition 98 dollars. This does not

reduce current year education spending, but does provide additional Proposition 98 flexibility in the budget year.

- CSU and UC Reductions. Adopts the Governor's proposal to cut \$132 million from the UC and the CSU.

Local Government:

- Local Public Safety Programs. Approves the Governor's proposal to eliminate General Fund support for various local law enforcement programs which saves approximately \$189 million in the current year and \$500 million in the budget year. These cuts are mitigated by reallocating Vehicle License Fee revenues (\$92 million in the current year and \$359 million in the budget year) to support these local programs.
- Williamson Act Local Backfill. Approves the Governor's proposal to eliminate the \$34.7 million backfill to counties. This does not, however, make any changes to the underlying program to preserve agricultural land.

Transportation:

- State Transit Assistance. Reduces annual funding for the State Transit Assistance (STA) from \$306 million to \$150 million. The Governor had proposed to eliminate the program entirely.
- Fund Shifts. Achieves \$185 million in General Fund solutions by shifting eligible Motor Vehicle Account funds and Tribal Compact revenues to the General Fund.

Various Other:

- Judicial Branch Solutions. Achieves \$91 million in solutions from the Judicial Branch with a reduction to the 2008-09 COLA for the trial courts and a one-time transfer from the Trial Court Improvement Fund to the General Fund.
- Office of Emergency Services. Eliminates \$30 million in funding for the gang initiative and various other programs.
- Employee Compensation. Reduces funding for employee compensation by \$240 million in the current year and \$417 million in the budget year, however, the savings is required to be negotiated through the collective bargaining process.