



MEMORANDUM
OFFICE OF THE
COUNTY EXECUTIVE
COUNTY OF PLACER

TO: Honorable Board of Supervisors

FROM: Thomas M. Miller, County Executive Officer
By Graham Knaus, Finance and Budget Operations Manager

DATE: January 25, 2011

SUBJECT: FY 2011-12 State Budget Update

Action Requested

Accept an update on the recently released FY 2011-12 Proposed State Budget.

Background

On January 10, 2011, Governor Jerry Brown released his \$127.4 billion (\$84.6 billion State General Fund) FY 2011-12 Proposed Budget. The Proposed Budget projects a \$25.4 billion deficit over 18 months (\$8.2 billion in the current year and \$17.2 billion in FY 2011-12).

To address the deficit, the Governor proposes a roughly 50/50 split between cuts (\$12.5 billion) and tax increases (\$12.0 billion). The budget proposes to borrow \$1.9 billion from special funds to close the remaining deficit, leaving a \$1 billion reserve. The approach largely relies on solutions that would create significant county fiscal and programmatic implications. In addition, the bulk of the solutions are contingent upon a potential June 2011 Statewide Special Election to extend tax increases set to expire June 30, 2011 as well as redistribute funding from existing voter approved initiatives. The tax increases proposed to be extended for an additional five years include Sales Tax (one percent – \$4.5 billion), Personal Income Tax (.25 percent for all tax brackets – \$4.8 billion), Vehicle License Fee (.5 percent – \$1.4 billion), and Dependent Exemption Credit (reduce credit from \$309 to \$99 - \$1.2 billion). These tax increases were originally approved by the Legislature February 2009.

Proposed State Solutions

The Governor's proposed solutions include program cuts (\$5.8 billion in Health and Human Services – mostly to client benefits), re-hauling the approach to local economic development, Realignment of public safety and health and human services responsibilities from the State to counties (\$5.9 billion), extension of tax increases (\$12.0 billion), and a payment deferral to K-12 schools to FY 2012-13 (\$2.2 billion). The budget proposes to continue to suspend a number of mandates with key exceptions for Law Enforcement and AB 3632 (Mental Health Services to Special Education Students). The budget would also continue existing payment deferrals through next year. However, in contrast to the last several January State budget proposals that relied heavily on mid-year cuts that did not materialize, the Proposed Budget includes little emphasis on mid-year cuts.

Expedited Timeframe

The Proposed Budget relies on quick action by the Legislature to put solutions in place or on the ballot. Specifically, the proposal would require all statutory changes to be approved by the Legislature no later than March 2011. Doing so would allow sufficient time for a June 2011 Special Election on the extension of tax increases and redirection of existing voter approved initiatives.

Legislative Action

The Senate and Assembly Budget Committees have already held overview hearings on the proposals and are scheduled to start deliberations on the Proposed Budget on January 26, 2011. The Legislative Analyst's Office (LAO) has opined that the Governor's proposal is a good starting point for addressing the State deficit but fiscal risks remain such as the \$1.2 billion in assumed revenue due to the sale of State buildings and optimistic savings assumptions.

Table 1 summarizes the list of proposed solutions.

Table 1

Major Expenditure Solutions	18 Month Statewide Impact
Reduction to the Medi-Cal Program	\$ 1.7 billion
Eliminate Redevelopment Agencies	\$ 1.7 billion
Reduction to the CalWORKs Program	\$ 1.5 billion
Shift transportation debt funding from General Fund to transportation weight fees	\$ 1.1 billion
Reduction to the University of California and California State University	\$ 1.0 billion
One-time shift of Mental Health Services Act funds (Proposition 63)	\$ 861 million
Reduction to the Department of Development Services	\$ 750 million
Shift some adult and all juvenile offenders to local jurisdictions	\$ 600 million
Reduction to In-Home Supportive Services	\$ 500 million
Savings from State employee compensation reductions	\$ 308 million
Reduction to Social Security Income/State Supplemental Program	\$ 190 million
Other Solutions	\$ 2.3 billion
Total Expenditure Solutions	\$ 12.5 billion
Major Revenue Solutions	
Extend the current 1.0 percent Sales Tax rate increase	\$ 4.5 billion
Extend the 0.25 percent Personal Income Tax surcharge	\$ 3.3 billion
Maintain the dependent exemption credit at the current level	\$ 2.0 billion
Extend the 0.5 percent Vehicle License Fee increase	\$ 1.4 billion
Mandatory single-sales factor Corporate Tax	\$ 1.4 billion
Eliminate Enterprise Zone Tax Credits	\$ 900 million
Adopt other revenue measures	\$ 500 million
Less – Increase in the Proposition 98 guarantee	(\$2.0 billion)
Total Revenue Solutions	\$ 12.0 billion

Realignment Proposal

The Proposed Budget would “realign” \$10 billion in Public Safety and Health and Human Services programs over four years. The proposed Realignment would occur in two phases, with the first to be implemented in FY 2011-12 and the second to be implemented in FY 2014-15.

The proposal would do the following:

Phase 1 Realignment – The Proposed Budget would transfer \$5.9 billion in broadly defined public safety program and fiscal responsibilities to counties. Existing State responsibilities to be realigned include CalFIRE, Adult Parole, “Low-Level” Offenders currently housed in State prisons, Juvenile Probation, Court Security, Booking Fees and

both State law enforcement funding, Child Welfare Services, Adult Protective Services, Substance Abuse Treatment, and Mental Health. Much of the realignment would be funded contingent upon the proposed Sales Tax and Vehicle License Fee increase extensions although the proposal also includes a one-time redirection of \$861 million in Mental Health Services Act Funds (Proposition 63) to fund FY 2011-12 mental health mandates. At this point, it is unclear how the Realignment would be structured should the tax increases expire June 30, 2011.

Phase 2 Realignment – The Proposed Budget would implement Phase 2 Realignment consistent with the timing of Federal health care reform in 2014. The Proposed Budget cites Federal health care reform as a trigger for the shift in county indigent costs from counties to the State. There are few details but it does appear to seek to shift currently county-administered health programs (In-Home Supportive Services, California Children Services, and likely Medi-Cal) to the State in exchange for complete county fiscal responsibility for CalWORKs, Child Care, Food Stamps, and Child Support. In total, Phase 2 would realign \$2.8 billion in State-County program and fiscal responsibilities.

Estimated Placer County Impacts

Based on an initial analysis of the information available, we estimate that the Governor's Proposed Budget could impact \$30 million in direct County funding from the cuts and the proposed Realignment with a significant portion of that amount tied to the proposed tax increase extensions. Departments continue to analyze impacts and these estimates will likely change as further details emerge and proposals evolve through the legislative process.

Public Safety

The Governor's Budget proposes significant policy, responsibility and funding shifts for Public Safety, including: low-level adult offenders; adult parole violators; juvenile offenders; and Court Security.

Low-Level Offenders – Proposed Budget requires that low-level, non-violent, non-sex offenders serve their terms locally either in jail and/or on probation, and thus transfers the responsibility to counties to manage offenders (estimated by the Sheriff's Office to be approximately 150 offenders per year).

Adult Parole – Proposal shifts responsibility for adult parolees to county probation departments. County would assume supervisory responsibility for all parolees upon their release from state prison (estimated by the Sheriff's Office to be approximately 620 offenders per year).

Juvenile Justice Programs – Proposal fully eliminates the State’s Division of Juvenile Justice by June 30, 2014, and shifts responsibility to counties to house, treat, and supervise all juvenile offenders (estimated by the Probation Department to be up to ten juvenile offenders per year).

Court Security – Proposal stipulates responsibility for the provision of Court Security would remain with County Sheriff Departments. However, the Governor’s plan would cap Court Security funding and would shift responsibility to Counties and Courts for negotiating local service levels and funding of future cost increases.

Although these policy shifts are proposed to come with funding, preliminary analysis suggests that new costs borne at the local level may not be fully covered.

One component of the tax increase extensions targets revenues dedicated to local Public Safety program funding. Placer County receives approximately \$1.9 million in Vehicle License Fee (VLF) revenues annually. Should this revenue source not be sustained, impacts to Placer County include: \$825,000 loss to Probation’s Juvenile Justice programs; \$980,000 loss to the Sheriff’s Office; and \$70,000 loss to the District Attorney’s Office. Thus far, the Governor has pledged his support to maintain funding for local public safety programs.

Health and Welfare

The Governor proposes to permanently shift to counties full responsibility for funding and administration of several key programmatic areas within Health and Human Services. In addition, funding for direct services to constituents would be significantly impacted.

Veterans Services – The Proposed Budget would completely eliminate State support for County Veterans Services Offices, including elimination of the Operation Welcome Home Program (\$200,000 potential cut to the County).

Mental Health Services – The realignment proposal transfers full responsibility from the State to counties for a number of existing mental health mandates. For FY 2011-12 only, this would include a one-time redirection of Proposition 63 (Mental Health Services Act) to mandated mental health services resulting in the loss of early/preventive mental health services to 400 Placer County families. Beginning in FY 2012-13, existing mental health mandates would be funded through the tax increase extensions. This would include realigning AB 3632 (Mental Health Services to Special Education Students) from the State to counties.

Foster Care and Child Welfare Services – The realignment proposal transfers full responsibility to counties for Foster Care and Child Welfare Services to children who are abused or neglected.

Adult Protective Services – The realignment proposal transfers full responsibility to counties for emergency services to seniors who are victims of abuse or neglect.

Eligibility – The Proposed Budget includes substantial reductions to program eligibility in a number of health and human services programs including CalWORKs, In-Home Supportive Services, and Medi-Cal. Most of the reductions are directly targeted to clients so may result in significant indirect impacts on county services.

Land Use and Governance

Transportation – Last year, the Legislature adopted a Gas Tax Swap that eliminated funding for Proposition 42 (approx \$3.5M in dedicated Transportation funding to Placer County) and replaced it with an increase in the excise tax. With the November 2010 passage of Proposition 26 (requires two-thirds majority vote on a number of fees), the Gas Tax Swap was eliminated. The Proposed Budget would reinstitute the Gas Tax Swap with a two-thirds vote of the Legislature followed by approval at the June Special Election. The State Controller has continued to remit gas tax revenues to local governments under the old formula and staff is cautiously optimistic that the Legislature will take action to clarify funding by affirming the Gas Tax Swap.

Williamson Act – The Proposed Budget eliminates the current year \$10 million statewide appropriation for Williamson Act subvention payments and provides no ongoing funding. This would effectively eliminate the program resulting in a \$50,000 cut to the County.

General Government

Fire Service – The Proposed Budget realigns fire services in the most highly populated State Responsibility Areas (SRA) to Local Responsibility Areas (LRA) serviced by local fire agencies. The proposal, if enacted, would shift fiscal responsibility beginning in FY 2011-12. However, broadening the definition of LRAs may not occur until FY 2012-13 due to the magnitude of the work involved for the California Board of Forestry and Fire Protection to identify the SRAs appropriate for transfer to LRAs.

The proposal raises substantial concern for the solvency of independent fire districts as well as fiscal impacts to Placer County. Depending upon the magnitude of the realignment, fire agencies (including Placer County) may assume significant added cost risk for fire suppression within their local service areas. It is vital for realignment to include state revenues on per-acre basis commensurate with the shift in responsibility areas from the State in order for fire districts to remain solvent and preclude the County from assuming the fire suppression responsibilities in those areas.

Library – The Proposed Budget would eliminate all State support to the County Library (\$84,000 cut) which is compounded by the third consecutive year of declining dedicated property tax revenue. These reductions would result in service impacts throughout the county library system potentially impacting service hours, the literacy program, and/or children's library services.

Cash Flow – The Proposed Budget continues the existing payment deferrals which will reduce the amount of cash available as well as result in lost investment income. The Proposed Budget would also defer the FY 2011-12 payment for pre-2004 mandate reimbursements.

Redevelopment/Economic Development Proposal

The Governor's Budget proposes to implement a new approach to economic development at the local level as well as phase out the existing funding mechanism for redevelopment agencies (RDAs). The proposal would be a mixed bag to counties and local agencies as it would both take away and redistribute local funds. Specifically, the proposal would do the following:

Honor Existing Obligations – Reconstitute RDAs to focus only on paying off existing debt and meeting contractual obligations already in place (\$2.2 billion). The Legislative Analyst's Office has indicated that the current obligated amount may exceed \$3 billion.

Sweep Unencumbered Balances – Existing unencumbered RDA balances would be swept by the State to address the deficit (\$1.7 billion).

FY 2011-12 Redistribution – Residual funds would be allocated to counties, cities, and schools based on existing statutory redevelopment "pass-through" formulas (\$1.1 billion). In addition, for FY 2011-12, \$210 million would be allocated to counties, cities, and schools based on existing property tax distribution formulas.

New Local Taxing Authority – Amend the Constitution to provide for 55.0 percent voter approval for limited tax increases and bonding against local revenues for development projects such as are currently done by RDAs.

Ongoing Redistribution – Beginning in FY 2012-13, the ongoing RDA revenues would be distributed to counties, cities, schools, and non-enterprise special districts based on existing property tax distribution formulas. The redistributed funding will equal the amount of funds currently dedicated for ongoing redevelopment/economic development activities and would instead become general purpose revenue to be prioritized by local agencies.

Enterprise Zones – Repeal all enterprise zones and sweep all unencumbered balances effective January 1, 2011 (\$581 million State benefit).

Next Steps/Conclusion

- Legislature has begun initial budget review – thorough vetting to begin January 26.
- Legislative political context will drive outcomes.
- Estimated County impacts likely to change as details emerge and proposals evolve in Legislature.
- Upcoming BOS Budget workshops to discuss local challenges related to FY 2011-12 County Budget.