



## MAY REVISION 2010-11

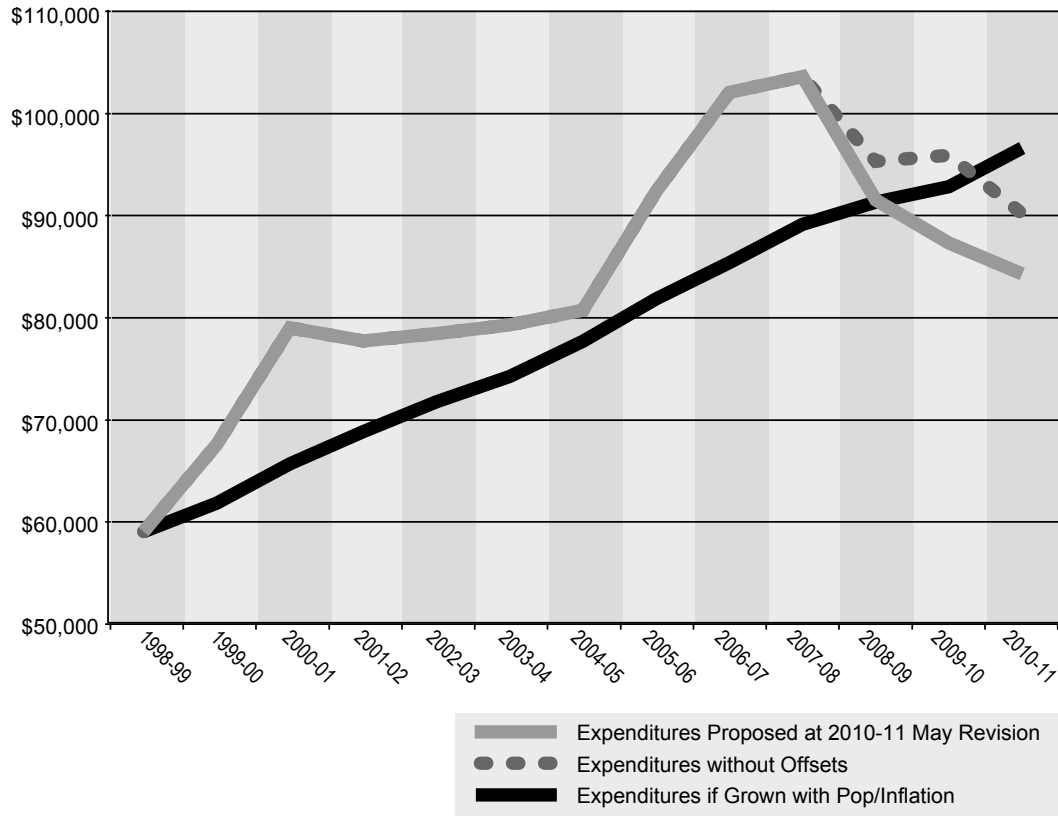
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### INTRODUCTION

In January, California, like the rest of the nation, was slowly emerging from the most severe economic downturn since the Great Depression, and faced a significant budgetary imbalance. The Governor's Budget proposed spending reductions and alternative funding solutions to address a \$19.9 billion projected budget gap. As proposed, it would bring overall General Fund spending to a level well below what it was a decade ago, in 1998-99, adjusted for population and inflation growth. (See Figure INT-01.) The Governor's Budget closed the budget gap while maintaining State funding for schools at the current year level, fully funding the Proposition 98 guarantee, and increasing funding for higher education, without raising taxes.

While there continue to be signs the economy is slowly improving, California continues to confront serious budgetary problems. The May Revision continues to fully fund K-12 education, increases funding for the University of California, the California State University, and the California Community Colleges to avoid further tuition increases or deep cuts to the classroom. It fully funds the CalGrant program. It also avoids additional reductions in funding for Child Welfare Services, foster care, public safety, and the Judiciary. To balance the Budget in the face of significant revenue losses, legal constraints and federal funding restrictions, the May Revision proposes deep reductions and program eliminations.

Figure INT-01  
**Proposed General Fund Spending**  
**Would Remain Below Population and Inflation Growth**  
 (Dollars in Millions)



## RE-DEFINING THE BUDGET GAP

In January, California’s projected budget gap for the fiscal year 2010-11 was \$19.9 billion. The Governor declared a fiscal emergency and called upon the Legislature to adopt \$8.9 billion in solutions in the Special Session. Given the necessary time for budget solutions to achieve their full value and the scope of the problem, the Governor proposed adopting these budget solutions before March 1, as delays in the adoption of these proposals would result in the loss of more than \$2 billion in budgetary solutions and necessitate deeper cuts.

As Figure INT-02 shows, various factors have changed the 2010-11 deficit from the \$19.9 billion projected in January. The solutions adopted in the Special Session, combined with additional federal funds and administrative actions reduced the size of

Figure INT-02  
**Changes in the Budget Gap**  
 (Dollars in Billions)

Budget Shortfall Projected in the 2010-11 Governor's Budget	-\$19.9
Special Session Approved Solutions	1.4
Achieved Federal Funds	0.7
Revenue Decline	-0.6
Cost Increases	-0.5
Increase in Reserve	-0.2
<b>Total Budget Solutions Proposed</b>	<b>-19.1</b>

the problem by \$2.1 billion. Revenue estimates are \$0.6 billion lower. Federal law, court decisions, population and caseload growth, as well as the need for a prudent reserve, increase the size of the problem by \$0.7 billion.

With all of these adjustments, the May Revision projects a budget gap of \$19.1 billion. This figure is comprised of a current year shortfall of \$7.7 billion, a budget year shortfall of \$10.2 billion and a modest reserve of \$1.2 billion.

In addition to the changes in the size of the problem, losses in available budgetary solutions have created a need for additional solutions and spending cuts. These losses include:

- Delays in the adoption of budgetary solutions that led to the loss—\$2.8 billion.
- Policy changes in the areas of higher education, public safety and funding for the state parks—\$0.5 billion.
- The update of federal funds to reflect Congressional Action, the President's proposed budget, and new information.

## **CLOSING THE BUDGET GAP**

The May Revision proposes additional solutions to close the budget gap. Figure INT-03 shows the categories of solutions proposed. Various fund shifts, alternative funding, and other revenues, including a \$650 million loan of excise taxes on gasoline, account for \$3.4 billion.

Figure INT-03  
**Proposed Budget Solutions**  
 (Dollars in Millions)

	<b>Governor's Budget</b>	<b>May Revision</b>	<b>Total</b>	
Expenditure Reductions	\$5,844.5	\$6,523.4	\$12,367.9	64.6%
Federal Funds	1,967.9	1,414.1	3,382.0	17.7%
Alternative Funding	1,025.9	252.4	1,278.3	6.7%
Fund Shifts and Other Revenues	477.1	1,636.5	2,113.6	11.0%
	<u>\$9,315.4</u>	<u>\$9,826.4</u>	<u>\$19,141.8</u>	100.0%

Federal funds account for \$3.4 billion in solutions, a reduction from the Governor’s January Budget proposal. Proposed federal funds include \$1.7 billion from the extension of the temporary increase in the Federal Medical Assistance Percentage (FMAP), \$125 million from the extension of other enhanced federal funding provided under the American Recovery and Reinvestment Act, and \$1.6 billion in additional federal funds for health and human services and for the Department of Corrections and Rehabilitation. Congress and President Obama’s Administration have already acted on several funding requests and it is anticipated that Congress will act on a number of other funding requests, including the proposed extension of the temporary FMAP increase, later this year. The Administration will work with legislative leaders and continue to monitor progress on securing the proposed level of federal funds. The Governor will propose additional solutions to the Legislature for inclusion in the Budget in the event the federal government does not provide the additional funding in the timeline anticipated.

Spending reductions account for \$12.4 billion in solutions. The proposed spending reductions reflect the severe constraints the state faces when balancing the Budget. Federal court rulings have prevented the state from achieving \$2.4 billion in savings since 2008-09 and actions by the federal receiver over prison medical care have increased costs by \$1.1 billion. Federal and state maintenance-of-effort requirements and other legal constraints have also increased costs and substantially restricted the areas of the Budget that can be reduced. As a result, the state’s choices are more limited and more difficult. The May Revision’s proposals to eliminate child care programs, with the exception of pre-school and after school care, to eliminate the California Work Opportunity and Responsibility to Kids Program, (CalWORKs) program, and to reduce funding for local mental health services by approximately 60 percent are the result of these constraints.

As the Legislative Analyst has noted, balancing this year's Budget will be a daunting challenge that will require very difficult choices. The May Revision is a reflection of this challenge and of the difficult but necessary changes required to address this year's budget gap. Last year, California closed a \$60 billion budget gap and successfully managed its cash reserves to avert a fiscal crisis. This year will require the same difficult decisions. As he did last year, the Governor will propose permanent budget reform and creation of a strong "Rainy Day Fund", to prevent a future budget crisis of the magnitude California faces today.

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### **PLAN TO ADDRESS ANTICIPATED CASH SHORTFALL**

The May Revision continues to project that the state will have sufficient cash to repay the entire \$8.8 billion of RANs in May and June 2010 as scheduled. Legislation enacted in the Special Session provided the state additional tools to manage cash in July and during key months of the budget year. Proposals to close the budget shortfall will substantially reduce this cash gap. In addition to budget solutions, the state will need to obtain external financing early in the fiscal year. Additional cash solutions may be required to reduce the need for external borrowing. At the Governor's direction, the Department of Finance has begun working with the State Controller's Office and the State Treasurer's Office to develop additional cash solutions as needed to meet the state's financial obligations.

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