

May 12, 2011

The Honorable John A. Pérez
Speaker of the California State Assembly
State Capitol
Sacramento, CA 95814

Dear Mr. Speaker:

Thank you very much for your recent letter seeking our ideas for solving the state's fiscal crisis. As Assembly Republicans have done throughout the process - and will continue to do going forward - we are happy to put forward our specific proposals to help California close our remaining \$15.4 billion budget deficit.

The budget approach that we outline today represents the common-sense solutions that we believe can be embraced by Democrats and Republicans alike in enacting a reasonable no-tax increase, budget compromise.

Our budget approach does not ask Californians to pay a \$55 billion tax increase to fuel unsustainable government programs and a 31 percent increase in state spending over 3 years. As a matter of principle, we believe that raising taxes on struggling families and employers is the worst thing we could do right now, for our economic and budget recovery and for our efforts to jumpstart the economy and bring back private-sector jobs.

The Assembly Republican proposals that we put forward today represent our roadmap to a no tax increase budget. These are specific and detailed proposals to balance the budget with no new taxes.

Budgets are a reflection of our priorities as a state. Facing a \$15.4 billion deficit, we are under no illusion that crafting a balanced budget is an easy task by any stretch of the imagination. But the news that California has taken in \$2.5 billion in unanticipated tax revenue in the past four months shows that we can balance the budget and protect the priorities of working families like education and public safety - without raising taxes on overburdened Californians.

Keep in mind that the nearly all of the components of our Republican budget roadmap have been proposed by the non-partisan sources we all trust, such as the Legislative Analyst's Office or the Bureau of State Audits, and key budget stakeholders like the University of California, or even by Governor Brown himself.

Specifically, the Assembly Republican roadmap to a no tax increase budget would:

- **Protect Education** - Like every California parent, Assembly Republicans are concerned about the impact the budget will have on classroom dollars. Our roadmap dedicates the \$2.5 billion in unanticipated tax revenue, which is "real money in the bank," to fully fund the Proposition 98 constitutional minimum funding guarantee for schools. It also rejects the additional \$4.1 billion in cuts to K-12 and \$847 million in cuts to higher education as outlined in the LAO letter to Senator Leno. Assembly Republicans will fight any attempt to suspend Proposition 98.
- **Protect Law Enforcement, Reject Dangerous Realignment Scheme** - Instead of increasing the Vehicle License Fee, the Assembly Republican roadmap would provide \$500 million from the General Fund to support law enforcement programs that would have been funded through the VLF. This is the same mechanism through which these programs were funded as recently as two years ago. We also reject the dangerous public safety realignment plan in Assembly Bill 109, which would result in the early release of thousands of dangerous criminals into our communities. By providing zero funding, our plan would stop this dangerous realignment scheme.
- **Eliminate Waste and Abuse** - Our roadmap embraces specific proposals outlined by the Bureau of State Audits and the University of California to end waste and abuse in areas like Medi-Cal eligibility and inmate health care. These are areas where actual waste and abuse have already been found and

No Tax Increase Budget

Total Problem: \$26.5 billion

Solutions adopted to date:

| | |
|--------------------------------|------------------|
| Trailer Bills | - \$11.2 billion |
| Budget Bill Reductions (SB 69) | -\$ 2.8 billion |
| Hospital Fee (SB 90) | -\$ 0.3 billion |

Increased Revenues

| | |
|------------------------------------|-----------------|
| Unanticipated Current Year Revenue | -\$ 2.5 billion |
| Increased Revenue 2011-12 | -\$ 2.5 billion |

Fund Republican Priorities

| | |
|------------------------------------|-----------------|
| Education | +\$ 2.0 billion |
| Local Law Enforcement and veterans | +\$ 0.5 billion |

Governor's Proposals

| | |
|----------------------------------------|-------------------------|
| Managed Care Fee | -\$0.1 billion |
| Governor's cuts rejected by Democrats* | -\$1.3 billion |
| Redevelopment | <u>-\$1-1.7 billion</u> |

Revised Deficit **\$6.6 -\$7.3 billion**

*Note: Democrats rejected \$1.7 billion of the Governor's proposed cuts.

No Tax Increase Budget

Additional Solutions Needed to Solve Remaining \$6.5-7.2 billion deficit:

| | |
|-----------------------------------------------|-----------------------------------------|
| K-14 Education cuts | 0 |
| Higher Education cuts | 0 |
| State Employee reduction | -\$1.1 billion |
| 2 day a month furlough courts (LAO) | -\$130 million |
| Reduce Medi-Cal Eligibility Errors (BSA) | -\$300 million |
| Resolve drug rebate backlog (BSA) | -\$200 million |
| Prison Medical Care (UC proposal) | -\$400 million |
| Redevelopment 98 fix (LAO) | -\$288 million |
| Redevelopment 98 fix long-term (LAO) | -\$ 0 million |
| Increased Prop 10 & 63 funding | -\$2.4 billion |
| Increased Prop 99 funding (LAO) | -\$115 million |
| Suspend QEIA (LAO) | -\$450 million |
| Competition | -\$700 million |
| Operating Budget Reduction | -\$600 million |
| Delay Internal Borrowing Repayment | -\$500 million |
| Pharmacy provider fee/Increased reimbursement | -\$100 million |
| Delay Diesel Retrofit (LAO) | -\$ 63 million |
| Scale Back Information Tech Projects (LAO) | -\$ 75 million |
| Recognize lower-than-anticipated UI | |
| Loan Costs (LAO) | <u>-\$ 60 million</u> -\$7.4 billion |

Reserve

\$ 100 million -\$800 million

NO TAX INCREASE BUDGET

Assembly Republicans understand that while the cuts are not easy, the Legislature can make strategic choices to preserve important programs and eliminate waste and administrative overhead.

California's economic recovery is fragile and more than 12 percent of Californians are still unemployed. Now would be the worst time to raise taxes. Instead, the state should be making it easier to create jobs, not making the problem worse.

Adopted Solutions

-\$14.3 billion

- To date, the Legislature has adopted \$14.3 billion in solutions-- \$11.2 billion were outlined in the trailer bills, \$2.8 billion is contained in the budget bill passed by the Assembly Democrats and \$300 million was included in Senate Bill 90.

Use of Additional Revenues:

\$5 billion

- **Increased Revenues Reduce the 2010-11 Budget Deficit.** The \$26 billion deficit includes shortfalls in the current fiscal year. Revenues have come in \$2.5 billion over anticipated revenues. These revenues reduce the 2010-11 deficit. There are two more months in the fiscal year (which ends on June 30th) and revenues are trending higher.
- **Increased Revenues in the 2011-12 Budget Year.** To be conservative, the Republican proposal includes only an additional \$2.5 billion in 2011-12. The increased revenues reflect the fact that revenues exceeded expectations in 2010-11 and that important economic indicators, such as the Personal Income Tax (PIT) withholding, suggest that there will be increased revenues in 2011-12. (Note: PIT revenues are up 13% over last year) If the non-partisan Legislative Analyst's May Revise estimates for 2011-12 does not include an increase in revenue, Assembly Republicans will present additional budget solutions.

Republican Priorities:

\$2.5 billion

- **Rejects Any Education Cut.** Democrats have been emphasizing the Leno letter and its proposed \$4.1 billion cut to education. It would take a suspension of Proposition 98 to cut \$4.1 billion out of the education budget.
 - Assembly Republicans will not vote to suspend 98.
 - Assembly Republicans believe that any increased revenues in 2011-12 should be used to eliminate any proposed education reduction.
 - Assembly Republicans would include flexibility. Whether or not there are increased revenues in 2011-12, Republicans believe that school districts should be given the flexibility to meet the fiscal challenges of running schools which will allow them to focus on core programs and put the needs of our children first.
- **No Additional Higher Education Cuts.** Democrats have suggested an additional \$1 billion cut to higher education. (Leno letter). Republicans believe that increased revenues eliminate the need for any additional higher education cuts.
- **Protect Law Enforcement Funds.** In 2009, a portion of the Vehicle License Fee (VLF) (.15%) was increased and designated to fund local law enforcement programs (COPS, JJCP, etc.). These programs had previously been funded by the General Fund. This tax increase sunsets on June

30, 2011. The Republican proposal provides \$500 million to fund these vital public safety programs. (Note: prior to the 2009 budget, these programs were funded out of the General Fund.)

- **Rejects the Governor's Realignment proposal.** To date, only one realignment proposal has been passed by the Legislature-- Assembly Bill 109. Republicans overwhelmingly opposed the proposal. Fortunately, according to the Governor's own signing statement, AB 109 will not go into effect without dedicated funding. Therefore, by not funding AB 109, Republicans can effectively stop the realignment of over 40,000 felons from state incarceration into county custody.
- **Restores funding for county veteran's offices.** Restore the reduction of General Fund Support for the County Veteran Service Offices. The CVSOs assist veterans in obtaining federal benefits for which they are eligible. The Democrats budget bill achieves \$7.3 million in savings by reducing General Fund support for state operations and local assistance for the County Veteran Service Offices (CVSOs) and Operation Welcome Home at CDVA from \$9.9 million to just \$2.6 million. Operation Welcome Home was implemented by the state in 2010 to connect Iraq and Afghanistan veterans to services that can help them transition successfully to civilian life.

Pending Governor's Proposal:

- **Managed Care Fee** **Savings-\$100 million**
Extends the industry-supported fee on Medi-Cal Managed Care plans for an additional 3 years. Revenues from the fee are used to provide a reimbursement rate increase to Medi-Cal Managed Care plans and to fund children's health care in the Healthy Families Program. This is an industry supported fee.
- **Governor's proposed cuts are adopted.** **Savings- \$1.3 billion**
The Democrats rejected \$1.7 billion of the Governor's cuts. There are approximately \$1.5 billion of the cuts that could still be achieved. It is assumed that the Governor supports his proposed budget cuts. The Republican proposal assumes all of the pending Governor's proposals are adopted, except for the limits on doctor visits, prescription drugs and durable medical equipment, and cuts to the Multipurpose Senior Service Program and local library funding. The Legislative Analyst's office is assessing whether potential savings have been eroded, since these cuts were not adopted with the prior package. If there are reduced savings that are not made up by an increase in additional revenues in 2010-11 or 2011-12, Republicans will provide additional solutions.
- **Redevelopment.** **Savings-\$1-\$1.7 billion**
The Republican proposal assumes either the Governor's proposal is adopted (with fixes discussed below related to Proposition 98) or the CRA proposal is adopted. The plan scores \$1 to \$1.7 billion in savings, depending on which plan is adopted.

Additional Reductions:

The Assembly Republican proposal adopts numerous proposals suggested by the Legislative Analyst. Both Assembly Republicans and Senator Leno asked the LAO for savings ideas. The lists were very different. Assembly Republicans asked for alternatives to avoid taking deep cuts in education. Additionally, the Assembly Republican proposal pulls from the Bureau of State Audits list of reforms.

➤ **The State must do its fair share. (LAO)** **Savings-\$1.1 billion**

The Assembly Republican proposal assumes the state will save \$1.1 billion in state employee costs. This represents a 10% reduction of employee costs. The Democrat budget does not control employee costs. Instead, they add approximately 1,000 new employees.

➤ **2 day a month furlough court workers (LAO)** **Savings-\$130 million**

A two day a month furlough will provide important savings without significantly disrupting the court system.

➤ **Republican cuts focus on eliminating waste and fraud. (BSA)** **Savings: \$500 million**

Governor Brown asked the State Auditor to identify savings. These proposals have not been incorporated into the Democrat proposal to date. Two proposals from the state auditor (Reduce Medi-Cal errors and reduce drug rebate backlog) that are in the Assembly Republican proposal would save \$500 million

➤ **UC Prison Health Care Proposal** **Savings-\$400 million**

The cost of providing health care to state prisoners has been the fastest growing part of the corrections budget. After the receiver took control of the system in 2006, medical costs skyrocketed. They reached \$2.5 billion a year, including mental health care. The cost of health care for each inmate per year in California is approximately \$11,600, while prison healthcare costs \$5,757 in New York; \$4,720 in Florida; \$4,418 in Pennsylvania; and \$2,920 in Texas. While costs have increased dramatically, it has not improved the quality of care enough to take the system out of federal court receivership. This proposal would have the state contract out the correctional medical care system. Last year's proposal had the UC system assume the responsibility. Republicans would contract with any qualified provider who could increase the quality of care, while reducing the overall cost of care. The proposal has an initial startup cost of \$24 million and annual savings of \$530 to \$870 million. Assembly Republicans have used a conservative estimate of \$400 million in 2011-12 in recognition of the institutional barriers which may make it difficult for the full savings to be quickly achieved.

➤ **Redevelopment Proposition 98 fix (LAO)** **Savings-\$288 million**

Redevelopment agencies have been set up and in some cases they do not utilize the school property tax increment. This pass through of property taxes is normally counted for purposes of calculating the state's Proposition 98 obligation. A small number of pass-throughs are not counted currently. This proposal would count all RDA pass-through funds in the Proposition 98 calculation.

➤ **Redevelopment Long-term Fix** **Savings \$0 (2011-12)- \$17 billion (over 10 years)**

Under existing property tax allocations, the state's obligation to backfill property taxes for schools would end if redevelopment agencies are eliminated (unless the state is in Test 1). The Governor's proposal changes existing law and excludes property tax returned to schools from the Proposition 98 calculation. Under the Governor's proposal, the state would have to continue to "backfill" property taxes even though those property taxes were paid to schools. Over 10 years, the state forgoes approximately \$17 billion in state General Fund savings. This proposal retains existing law which would count local property tax increment.

➤ **Increased Prop 10 & 63 funding(LAO) Savings-\$2.4 billion**

The Governor's budget proposal includes a shift of Proposition 10 and 63 funds to offset General Fund expenditures. This proposal increases the shift. \$975 million of this increased shift would come from one-time reserves the Department of Finance has identified for Proposition 63 services.

➤ **QEIA (LAO) Savings-\$450 million**

In 2004-05 and 2005-06, a coalition of education groups claimed that the Legislature appropriated education funds below the required minimum funding level. (After suspending Prop 98 in 2004-05, revenues increased. The education community claimed the state "owed" them funds from that increase.) The CTA sued (*CTA, et al. v. Schwarzenegger, et al.*) The Governor's office entered into negotiations with CTA and settled. Their settlement was codified by SB 1133 (2006). SB 1133 created the Quality Education Investment Act (QEIA) which required the state to refund the "under-appropriation" (\$3 billion in total) to a narrow group of schools. The state owes approximately \$1.6 billion of the \$3 billion. This proposal would suspend the payment for one-year.

➤ **Competition. Savings-\$700 million**

Assembly Republicans believe that government programs should be run efficiently and cost-effectively. This proposal adopts a number of proposals that would reduce the cost of government:

1. **Electronic Court Reporting (\$100 million).** In a Jan. 24 report to the Legislature, the LAO cited a 1991-94 pilot study in California that said electronic reporting could save the state from \$28,000 to \$42,000 a year per courtroom. The federal government and 45 states already use at least some electronic reporting. California is one of them. In Sacramento, the county has gone digital in eviction and traffic court and electronic on the daily misdemeanor calendar.
2. **Contract Out Facilities Maintenance and Administrative Functions at State Hospitals/Child Support/DD Facilities (\$200 million).** Current General Fund spending in the state hospitals is approximately \$1.1 billion while spending for Developmental Centers is approximately \$310 million. Contracting out administrative functions (food service and janitorial) would save \$130 million. Contracting out child support collections would reduce overhead and has the potential to increase collection could save the state \$76 million (The state's current collection rate is only 53.4%).
3. **Centralized Eligibility Initiative (\$400 million).** Improve public access, performance and reduce costs by centralizing eligibility system.

➤ **Increased Prop 99 Funds (LAO) Savings-\$115 million**

Proposition 99 funds can be reallocated with a 4/5ths vote in furtherance of the Proposition. In the 1990s, the Legislature shifted Proposition 99 funds to direct health care services. This proposal would shift \$115 million of Proposition 99 funds to offset health care service costs related to smoking.

➤ **Operating Expenses and Equipment Reduction Savings-\$600 million**

This proposal makes an unallocated reduction to departments' operating (non-personnel) expenses. It amounts to less than five percent of total General fund budgeted for operations.

➤ **Delay Internal Borrowing Repayment. Savings-\$500 million**

During the last few fiscal years, the state has borrowed from state special funds to avoid cutting programs. The 2011-12 budget had a scheduled repayment of \$700 million. The Governor delayed repaying \$200 million to offset the cancelation of the proposed sale of state properties. This proposal expands the Governor's delayed repayment.

- **Delay Diesel Retrofit (LAO)** **Savings-\$63 million**
The Governor's budget assumes the state will purchase new diesel equipment or retrofit existing equipment to meet the state's AB 32 mandate. This proposal suspends the purchase for one year.
- **Scale Back Information Tech Projects (LAO)** **Savings-\$75 million**
- **Recognize lower-than-anticipated UI Loan Costs (LAO)** **Savings-\$60 million**

mechanisms to eradicate them have already been identified. These proposals would save nearly \$1 billion.

- **Reduce the Cost of Program Delivery** - With real programs on the budget chopping block, taxpayers are demanding that lawmakers spend tax dollars as efficiently and effectively as possible. By enacting reforms to introduce competition in the delivery of services, such as allowing agencies to contract out with private firms for non-essential services like food service and transportation, along with other reforms to cut operating costs, we can save \$1.2 billion.
- **Adopt Remaining Solutions Proposed by Governor Brown** - There are up to \$3.2 billion in cuts and other savings proposed by Governor Brown that have not yet been enacted by the Legislature. Our budget roadmap includes many of these pending solutions, including a modified version of the Governor's redevelopment plan.
- **State Must Do Its Fair Share** - Local governments, school districts and the private sector have had to reduce their workforce. State government workers must also do their part. Our roadmap rejects your caucus' proposal to grow our state workforce by 1,000 new government workers, and instead makes \$1.1 billion in additional savings in the state workforce. Taxpayers shouldn't have to pay higher taxes to shield government workers from contributing their fair share.

We trust that you will see the Assembly Republican roadmap to a no tax increase budget as a detailed and thoughtful proposal to help the state close its remaining \$15.4 billion budget deficit, protect our core priorities like education and public safety and get California on the road to economic recovery.

On behalf of Assembly Republicans, I wish to extend my hand of bipartisan cooperation as we work to balance the budget without raising taxes. In addition, we look forward to working with you and your caucus and Governor Brown on long term reforms to end this constant cycle of budget deficits such as enacting a real spending cap and reining in the costs of gold-plated public pensions.

Respectfully,

CONNIE CONWAY
Assembly Republican Leader