



2002-03

CALIFORNIA Governor's Budget

May Revision

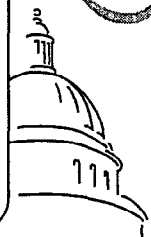
The May Revision to Governor Davis' January Budget provides updated economic and revenue forecasts, as well as the latest caseload, enrollment, and population information for programs in the education, public safety, and health and human services areas.

This Budget continues to be driven by the precipitous decline in revenues from the personal income tax on capital gains and stock options, brought on by the weak performance of the stock market through 2001 and the economic aftermath of September 11th. The effect of the national recession can be seen in state budgets throughout the country: 45 states face budget deficits as a result of unanticipated revenue losses. California's problem is unique in magnitude because of the state's size, but is otherwise similar to other states in nature.

The May Revision to the Governor's 2002-03 Budget addresses a projected \$23.6 billion gap between expenditures and revenues through the 2002-03 fiscal year, or 30 percent of the General Fund. In addition to the \$12.5 billion gap identified in the January Budget, this Revision proposes adjustments to address an expected additional \$9.5 billion revenue loss, and \$1.6 billion in additional cost pressures. It proposes to address the shortfall through a combination of spending reductions and revenue proposals, as well as the maximum fiscally responsible level of fund shifts, loans, accelerations, transfers, and deferrals.

This balanced approach recognizes the consensus opinion of economists that California's economy is already recovering from the brief recession, in contrast with the much longer and deeper downturn of the early 1990s. Most sectors have experienced job growth since last November. Manufacturing is again expanding in a portion of the state; the state's tourism industry has improved after suffering a major blow from the September 11th terrorist attacks; and real estate markets have heated dramatically.

Overview



2002-03

This Budget protects the Administration's top priorities: public education, public safety, children's health insurance, and critical senior care programs, while avoiding significant tax increases which would otherwise be necessary.

Furthermore, in addition to the 6,600 positions eliminated since 1999 under this Administration, the 2002-03 May Revision eliminates an additional 4,000 state government positions. The first priority for elimination in each department will be vacant positions not required to maintain critical public health and safety functions. The Administration will establish a process to facilitate the elimination of filled positions in accordance with state laws, regulations, and Memoranda of Understanding with represented employees.

**2002-03 May Revision
Addressing a \$23.6 Billion Gap
(Dollars in Millions)**

	Amount	Percent of Solution
Program Reductions	\$7,597	32.1%
Tobacco Settlement Securitization	4,500	19.0%
Loans	1,729	7.3%
Fund Shifts	1,327	5.6%
Temporary VLF Offset Reduction	1,276	5.4%
Net Operating Loss (NOL) Deferral (2 year)	1,200	5.1%
Deferral of Education Disbursements (1 month)	1,149	4.9%
Debt Restructuring	1,083	4.6%
Federal Funding Increases	1,081	4.6%
Federal Tax Conformity/Tax Compliance	938	4.0%
Other Accelerations & Transfers	734	3.1%
Fund Transfers	553	2.3%
Cigarette Tax Increase	475	2.0%
Total	\$23,642	100.0%



The Economy

The national and California economies began to recover from their 2001 recessions sooner than expected. National economic output soared in the first quarter of 2002, in large part because businesses filled orders by increasing production rather than dipping further into inventories. That will largely be a one-time boost to output, however, and the pace of growth appears to have slowed in the second quarter. Still, manufacturing is expanding in much of the nation after contracting for nearly two years. Consumers remain relatively upbeat and continue to spend. Major stock market indexes continue to slide, however, as corporate profits have yet to meet investors' expectations.

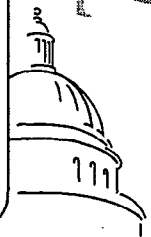
California was quicker than the nation to begin to recover. Job growth resumed in the state in December, while the nation had to wait until April. In both the State and the nation, however, the number of new jobs is not yet keeping up with the number of people joining the labor force, and unemployment has yet to fall. Rising hotel/motel occupancy rates indicate that tourism in much of the state is recovering from the devastating blows of the September 11th terrorist attacks. In addition, manufacturing is expanding in the California regions where that sector is surveyed. While Southern California continues to fare better economically than the San Francisco Bay Area, there are signs that the Silicon Valley's economic downturn is at or near bottom. Both the California and national economies should accelerate in the second half of the year and into 2003.

The Nation

The first national recession of the new millennium will likely go on record as one of the mildest in the post-World War II period. Inflation-adjusted gross domestic output (GDP) fell in only one quarter—the third quarter of 2001. Output rebounded in the fourth quarter at a 1.7 percent annual rate before surging almost 6 percent in the first quarter of 2002. No official decision has been made yet on the end of the recession, but a late-2001/early-2002 date is likely.

Private businesses reduced inventories at an annual rate of \$36.2 billion in the first quarter, following a record decrease of \$119.3 billion in the fourth quarter of 2001. That slowing of inventory paring contributed \$83 billion, or more than 60 percent, of the overall gain of \$134 billion in inflation-adjusted GDP in the first quarter. Inventory adjustments like this are common near the end of recessions, as businesses try to align their inventories with lower sales levels. The adjustments become smaller as

The Economy



they near the desired levels. That appears to be happening in the current quarter. Further growth in output depends on increases in consumer spending, business fixed investment, government spending, and net exports.

Both consumer and government spending increased in the first quarter. Consumption grew by a healthy 3.5 percent. While not as large as the increase in the fourth quarter of last year, when consumers took advantage of generous buyer incentives on purchases of new autos, the most recent results demonstrate that consumer spending continues to underpin the economy. Government spending grew even more rapidly, 7.9 percent. Over half of that increase was for national defense.

Business fixed investment and net exports, on the other hand, pulled down economic growth in the first quarter. Business fixed investment was down only slightly with a decline in nonresidential construction largely offsetting an increase in home building. Investment in equipment and software was off only slightly. The decline in nonresidential construction was not surprising given the run-up in office and industrial vacancy rates in 2001. Home sales and residential construction were boosted by lower mortgage rates.

Net exports (exports minus imports) fell quite sharply in the first quarter, as imports grew more quickly than exports. The U.S. economy improved more than the economies of most of our major trading partners, resulting in a bigger boost in American demand for imported goods and services than in foreign demand for American-made goods and services.

Monthly statistics since the beginning of 2002 reflect the strong growth in the first quarter and more modest growth in the second quarter. Particularly encouraging, the Institute for Supply Management's survey of national manufacturing showed that manufacturing expanded for the third month in a row in April after contracting the prior 18 months. April's index was down slightly from the March reading, suggesting some slowing of growth. Also, the University of Michigan's Consumer Sentiment Index has trended upward in the last seven months despite dropping twice in the last three months. The Middle East conflict, rising gasoline prices, and sluggish job markets have led consumers to conclude that prospects six months down the road look better than current conditions.

Consumers are more concerned about job prospects, however. Employers have been cautious about hiring new employees. Not yet convinced about the strength and sustainability of the recovery, employers have opted toward increasing the hours of their existing workforce. Over 40,000 non-farm payroll jobs were added in April, but that was the first significant gain since May 2001. National unemployment stayed within a 5.4 percent to 5.8 percent range for six months before jumping to 6 percent in April.

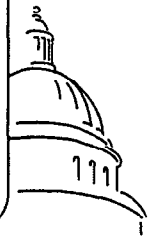


Job gains should pick up in the second half of 2002. A considerable amount of fiscal stimulus is being added to the economy. The cut in federal tax rates that took effect at the beginning of the year has boosted consumers' disposable income, giving them the means to continue spending. In addition, spending on defense and homeland safety will pick up sharply in the second half of 2002 and in 2003. Moreover, the economy will continue to be buoyed by the considerable monetary policy easing of last year. Construction, however, will not be adding to economic growth until well into 2003. Furthermore, net exports will be a drag on the economy until the economies of the nation's major trading partners pick up. In addition, business spending on new equipment will be spotty until late 2002 or early 2003. But, on balance, growth of the national economy is expected to pick up in the second half of 2002 and further in 2003.

California

California got a jump on the nation in beginning to recover from recession. Jobs in the state began to pick up in December 2001—four months before they started to come back in the nation. From November 2001 to April 2002, the state gained 22,500 jobs while the nation lost 197,000. As in the nation, job growth in California did not keep up with the number of people coming into the labor force, and unemployment edged up. Still, the transition from consistent monthly job losses to small gains and losses is a major milestone in the recovery process. Significant swings from monthly job losses to monthly job gains have occurred in nondurable goods manufacturing, wholesale and retail trade, engineering and management consulting, construction, and hotels and other lodging. In addition, job losses have slowed considerably in business services and durable goods manufacturing. Sharp declines in job losses in electronic equipment and industrial machinery manufacturing are particularly encouraging for the prospects of the state's high-tech sector.

Good news about the state's manufacturing sector is coming from other sources as well. Recent surveys indicate that manufacturing is expanding in two of the state's largest manufacturing centers. A quarterly survey conducted by researchers at Chapman University in Orange County showed that the county's manufacturing sector recovered strongly in the first quarter of 2002, with both production and new orders increasing substantially. Similar results were found for the Inland Empire manufacturing sector in a monthly survey conducted by researchers at California State University, San Bernardino. Manufacturing in the combined Riverside County-San Bernardino County metro area has expanded for four consecutive months. In both Orange County and the Inland Empire, the timing of the recovery of local manufacturing coincided with the recovery of manufacturing nationally.



2002-03

The health of the state's tourism industry has improved in recent months but is not back to where it was before the September 11th terrorist attacks. In addition to stabilizing industry employment, hotel/motel occupancy rates in major state metropolitan areas have picked up in recent months, reflecting increased travel. A sizable increase in the San Jose metropolitan area in February was particularly encouraging. Average room rates are down, however, hurting lodging industry profitability.

Low mortgage rates, a disappointing stock market, and perhaps the fear of being left behind have heated up California residential real estate markets. Home sales surged in the first quarter of 2002, with existing home sales up 18 percent from a year earlier. San Francisco Bay Area sales were up 29 percent in March from a year ago. Home prices continue to soar: the median price of existing homes sold in the state exceeded \$300,000 for the first time in March.

The Forecast

The state's economic recovery will pick up as the year unfolds, but job growth will likely be modest for the next few months as employers gauge the strength and sustainability of the recovery. By the fourth quarter of 2002, jobs will be up about 1 percent from a year earlier and growing at an annualized rate of about 2.5 percent on a quarter-to-quarter basis. The economy will go into 2003 with good momentum, and job growth from the fourth quarter of 2002 to the fourth quarter of 2003 will be 2.7 percent. The unemployment rate—a lagging indicator—will likely remain above 6 percent for the rest of 2002 before trending downward in 2003.

Personal income will grow by 3 percent during 2002 and 6.2 percent during 2003, and will track employment more closely than in the last two years. Employee stock option and bonus income fell sharply from an estimated \$78 billion in 2000 to \$44 billion in 2001. It is projected to fall again in 2002, to \$31 billion, before increasing in 2003 to \$36 billion. The drop in 2002, reflecting an assumption of only modest gains in the stock market, will reduce personal income growth in 2002. However, the effect on personal income growth will be considerably less than what occurred in 2001, when employee stock option and bonus income fell by \$34 billion.

Construction will not be a source of growth in 2002. Residential construction will be up modestly, at best. Demand for affordable housing is high, but supply is significantly constrained. Nonresidential construction will fall in light of jumps in office and industrial vacancy rates and declines in rent that have occurred in the last year and a half in much of the state. The San Francisco and San Jose metropolitan areas, in particular, have seen office vacancy rates soar with the failure of many dot-com companies and the slowdown in the high-tech sector. But there are also pockets of high office vacancy in Southern California—Orange County, for example. Nonresidential construction will bounce back in 2003.



Figure ECON-1

Selected U.S. Economic Indicators

	2001	Forecast	
		2002	2003
Real gross domestic product, (1996 dollar) (Percent change)	1.2	2.1	3.6
Personal consumption expenditures	3.1	3.3	3.2
Gross private domestic investment	(8.0)	1.5	7.3
Government purchases of goods and services	3.6	3.8	2.7
GDP deflator (1996=100) (Percent change)	2.2	1.7	2.4
GDP, (Current dollar) (Percent change)	3.4	3.8	6.1
Federal funds rate (Percent)	3.92	2.04	4.00
Personal income (Percent change)	4.9	3.3	5.6
Corporate profits before taxes (Percent change)	(17.4)	(7.7)	7.6
Nonfarm wage and salary employment (Millions)	132.2	131.5	133.5
(Percent change)	0.4	(0.5)	1.4
Unemployment rate (Percent)	4.8	5.7	5.7
Housing starts (Millions)	1.61	1.58	1.56
(Percent change)	2.1	(1.6)	(1.3)
New car and light truck sales (Millions)	17.1	16.0	16.7
(Percent change)	(1.4)	(6.5)	4.3
Consumer price index (1982-84=100)	177.1	180.6	185.5
(Percent change)	2.8	2.0	2.7

*Forecast based on data available as of April 2002.
Percent changes calculated from unrounded data.*

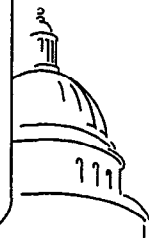


FIGURE ECON-2

Selected California Economic Indicators

	2001	Percent Change	Forecast		2003	Percent Change
			2002	Percent Change		
Personal income (\$ billions)	\$1,099.54	-0.5%	\$1,158.4	5.4%	\$1,229.7	6.2%
Nonfarm W&S employment (thousands)	14,487	-1.1%	14,628	1.0%	15,022	2.7%
Mining	25	3.2%	24	-2.3%	23	-4.2%
Construction	751	1.3%	733	-2.4%	761	3.8%
Manufacturing	1,812	-7.7%	1,815	0.2%	1,870	3.0%
High technology	478	-9.6%	474	-0.8%	493	4.0%
Transportation/utilities	723	-3.6%	722	-0.1%	755	4.6%
Wholesale & retail trade	3,307	-0.5%	3,361	1.6%	3,461	3.0%
Finance group	846	2.3%	866	2.4%	894	3.2%
Services	4,607	-1.6%	4,692	1.8%	4,822	2.8%
Government	2,417	3.6%	2,415	-0.1%	2,436	0.9%
Unemployment rate	6.0%		6.4%		5.7%	
Housing permits (thousands of units, annual rate)	149	-0.2%	153	2.7%	148	-3.1%
Consumer price index (Dec-Dec)	181.8	2.5%	187.4	3.1%	191.9	2.4%

Forecast based on data available as of April 2002.
Data are for the 4th quarter, except where otherwise noted.
Percent changes are 4th quarter to 4th quarter.



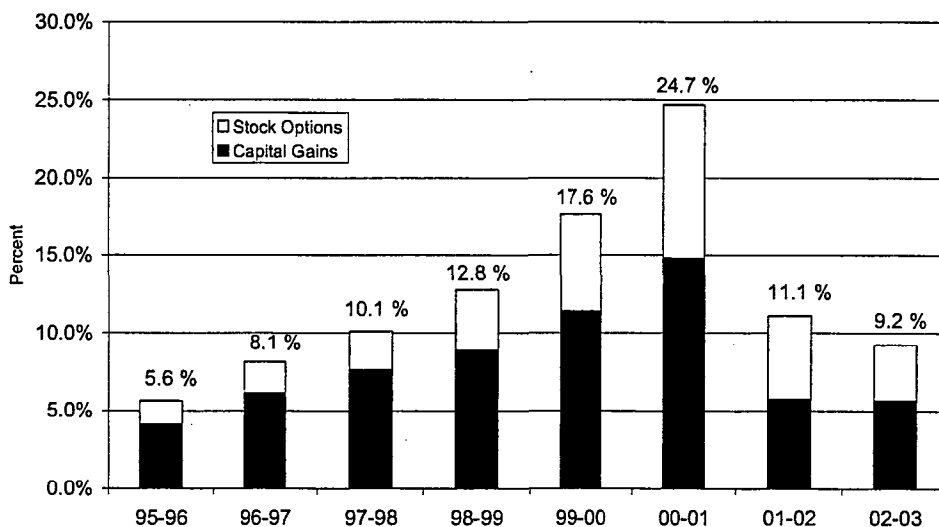
Revenue Estimates

General Fund revenues are expected to be below the Governor's January Budget by \$3.3 billion in 2001-02 and \$0.7 billion in 2002-03. Over the two years, the reduction is approximately \$4 billion. These revenue estimates include a number of proposals to assist in addressing the State's fiscal problem.

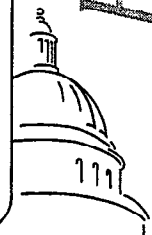
The phenomenal revenue surge that the State experienced over the last several years was largely driven by stock market activity, which propelled extraordinary capital gains and stock option income. Capital gains realizations reached almost \$118 billion in 2000—an exceptional increase from the \$21 billion level just five years earlier. Stock options, which are reported as wages for tax purposes, are estimated to have peaked in 2000 to reach roughly \$78 billion from the \$8 billion level five years earlier. As a consequence, the growth in these components represented an increasing portion of the General Fund revenue base. In 2000-01, capital gains realizations and stock options contributed nearly one-quarter of all General Fund revenue, a dramatic increase from their 5.6 percent share in 1995-96. Given the turnaround in the stock market, capital gains and stock options are expected to account for only about 11 percent of General Fund revenues in 2001-02, a decrease of over 50 percent from the prior year. This can be seen in Figure REV-1.

FIGURE REV-1

**Capital Gains and Stock Options
as a Percent of General Fund Revenue**



Revenue Estimates



The growth and decline in capital gains and stock options is reflective of movements in the stock market. For example, the technology-heavy NASDAQ, in which the bulk of California's Silicon Valley companies are traded, had a December close of 1,052.1 in 1995. The NASDAQ then peaked in March 2000 at 5,048.6 and closed in December of that year at 2,470.5. Since that time, the index has continued to trend downward, closing at 1,950.4 in December 2001, and at 1,688.2 in April 2002. Thus, as of the April 2002 close, nearly one-third of the NASDAQ's value has been lost since the end of 2000, and nearly two-thirds since the peak. This decline is driving the reductions expected in capital gains and stock options.

The forecast also includes the effect of the May Revision proposals to address the revenue setback that the State is experiencing. These proposals include the following:

- ❖ A two-year suspension of net operating loss provisions, which is expected to increase revenues by \$1.2 billion in 2002-03.
- ❖ Conformity with federal law regarding accounting for bad debt reserves for large banks, which is expected to increase revenues by \$255 million in 2002-03.
- ❖ An increase in the tobacco excise tax of \$0.50, which is expected to increase revenues by \$475 million in 2002-03.
- ❖ Allowing the Franchise Tax Board and the Board of Equalization to waive penalties and interest on delinquent tax accounts, which is expected to increase revenues by \$145 million in 2002-03.
- ❖ Other proposals including increasing collections activities at the Franchise Tax Board, ensuring proper auditing of tax credits, and improving the effectiveness of the tax protest and settlement programs. These proposals are expected to increase revenues by \$361 million in 2002-03.
- ❖ A reduction in the vehicle license fee offset from 67.5 percent to 25 percent for the 2003 calendar year. This proposal is expected to reduce expenditures by \$1.276 billion in 2002-03.

Personal Income Tax

The personal income tax forecast has been reduced by \$4.595 billion in 2001-02 and by \$5.548 billion in 2002-03. The budget year estimate includes the effect of the pension and individual retirement account conformity package, which was passed by the Legislature and signed by the Governor on May 8, 2002, as well as the Administration's proposals identified above.



The dramatic decline in cash receipts has heavily influenced the forecast revision. April's receipts were 45 percent lower than those of April 2001. The year-over-year declines were across-the-board in all of the personal income tax receipt components.

As indicated above, the weakness in the current year, which carries forward into the budget year, is assumed to be primarily driven by a drop in capital gains as well as by lower wage growth due to reduced stock option income. Based on year-to-date cash receipts, capital gains for the 2001 tax year are estimated to have decreased by 60 percent, to \$47 billion, and are projected to slowly recover with a 5 percent increase in 2002. Stock options are estimated to have dropped by almost 45 percent, to \$44 billion, in 2001 and are forecast to decline by another 30 percent in 2002, to \$31 billion.

Sales and Use Tax

The sales and use tax forecast has been increased by \$376 million in the current year and \$108 million in the budget year.

Through April, sales tax receipts are \$261 million above the 2002-03 Governor's Budget forecast. This may be indicative of the recovering economy and particularly strong vehicle sales in the third quarter of 2001.

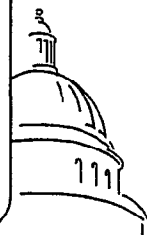
Sales tax revenue over the next year is expected to show very moderate growth. For calendar year 2002, no growth in taxable sales is expected, while 6 percent growth is expected for calendar year 2003.

Corporation Tax

The corporation tax forecast has been increased by \$397 million in 2001-02 and \$1.428 billion in 2002-03.

Factors responsible for the revision in the forecast include:

- ❖ An increase in the revised estimate for net accruals for 2001-02, based on updated information from the Franchise Tax Board.
- ❖ An increase in taxable profits in 2002-03, which was more than offset by greater-than-anticipated losses due to corporations increasing their utilization of tax credits and other corporate tax incentives.



- ❖ The May Revision proposal to suspend for two years the net operating loss provisions in current law and to enact several other proposals, including conformity with federal law regarding accounting for bad debt reserves for large banks. These proposals have increased the forecast from the Governor's Budget.

FIGURE REV-2

**General Fund Revenue Forecast
Reconciliation with the Governor's Budget Forecast**

(Dollars in millions)

	Governor's Budget	May Revision	Change Between Forecasts	
Fiscal 00-01				
Personal Income Tax	\$44,614	\$44,614	\$0	0.0%
Sales & Use Tax	21,277	21,277	0	0.0%
Corporation Tax	6,899	6,899	0	0.0%
Insurance Tax	1,497	1,497	0	0.0%
Other Revenues	3,321	3,321	0	0.0%
Transfers	<u>-6,180</u>	<u>-6,180</u>	<u>0</u>	<u>0.0%</u>
Total	\$71,428	\$71,428	\$0	0.0%
Fiscal 01-02				
Personal Income Tax	\$38,455	\$33,860	-\$4,595	-11.9%
Sales & Use Tax	21,165	21,541	376	1.8%
Corporation Tax	5,261	5,658	397	7.5%
Insurance Tax	1,560	1,656	96	6.2%
Other Revenues	2,982	3,264	282	9.5%
Transfers	<u>7,660</u>	<u>7,796</u>	<u>136</u>	<u>1.8%</u>
Total	\$77,083	\$73,775	-\$3,308	-4.3%
Change from Fiscal 00-01	\$5,656	\$2,348		
% Change from Fiscal 00-01	7.9%	3.3%		
Fiscal 02-03				
Personal Income Tax	\$42,605	\$37,057	-\$5,548	-13.0%
Sales & Use Tax	22,850	22,958	108	0.5%
Corporation Tax	5,869	7,297	1,428	24.3%
Insurance Tax	1,656	1,759	103	6.2%
Other Revenues	4,753	7,454	2,701	56.8%
Transfers	<u>1,572</u>	<u>2,078</u>	<u>506</u>	<u>32.2%</u>
Total	\$79,305	\$78,603	-\$702	-0.9%
Change from Fiscal 01-02	\$2,222	\$4,828		
% Change from Fiscal 01-02	2.9%	6.5%		



Education

Preserving Reforms and Core Education Programs

Although the reduction in available General Fund resources provides significant challenges to maintaining funding for core programs, the May Revision maintains education as the Administration's highest priority by providing funding at the Proposition 98 Test 2 level; fully funding growth and cost of living adjustments, including funding for apportionments at two percent; maintaining the Governor's Budget funding level for the California Community Colleges; and making focused reductions in higher education programs outside core classroom instruction.

The current federal budget provides \$738 million in new funding associated with the No Child Left Behind Act, which is proposed for appropriation in the May Revision. This new federal program is closely aligned with California's recent efforts to improve accountability, create challenging standards, develop materials and curricula aligned with those standards, and assist and intervene in under-performing schools. Where allowable under federal rules, the Administration proposes to use these funds to enhance existing state reform programs. In view of the State's current budget challenge, program expansions previously proposed from the General Fund are proposed to be funded from these new federal funds.

Key Initiatives Preserved

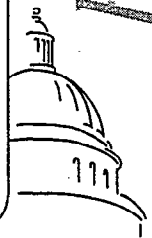
TEACHER DEVELOPMENT AND RECRUITMENT

The May Revision preserves \$110 million for the Math and Reading Professional Development Program through a combination of State and federal funds. Additionally, over \$131 million in federal funds is provided for training over half of the state's K-3 teachers to teach reading using the new standards-aligned materials in 2002-03, and further \$5 million is provided to increase standards-aligned teacher training in science.

The May Revision preserves \$87 million for the Peer Assistance Review program to help the development of new teachers, and \$119 million through a combination of State and federal funds for recruitment of highly qualified teachers.

In total, these funds will allow the State to fund standards-aligned training for approximately 86,000 of California's 300,000 teachers.

Expenditures



INSTRUCTIONAL MATERIALS

Assisting schools in providing students with standards-aligned textbooks remains a priority. Therefore, the May Revision sustains a total of \$480 million for this Initiative. To enhance fiscal flexibility and minimize reductions that otherwise would be necessary, the revised proposal shifts funding from the Proposition 98 Reversion Account to Proposition 98 General Fund for one-time incentive funds for standards-aligned reading/language arts materials (\$150 million), and school and K-4 classroom library materials (\$80 million). The remaining \$250 million represents base funding for K-12 instructional materials. The revised proposal also gives schools piloting materials until June 30, 2003 to purchase reading materials and receive incentive funds.

From the original Governor's Budget proposal, a \$75 million reduction for science equipment and \$70 million reduction for materials (\$50 million for reading/language arts materials and \$20 million for school and K-4 classroom library materials) are necessary to help with the budget solution. Additional funding for instructional materials is available to many schools through the increase in federal funding:

CLASS SIZE REDUCTION

In addition to preserving existing state funding for class size reduction, the May Revision directs \$206.7 million of federal funds to class size reduction, an increase of \$32 million over the 2001-02 level.

ASSISTING LOW PERFORMING SCHOOLS

The May Revision maintains the Governor's Budget level of \$190 million for the Intermediate Intervention/Under Performing Schools Program, and reflects an increase of \$7 million in federal funds for the Comprehensive School Reform program. The May Revision includes \$12.5 million for intervention in schools sanctioned for failing to make performance increases after participating in State or federal assistance programs for low performing schools. The Administration proposes legislation to accompany the budget to create a framework for the State's intervention in sanctioned schools.

BEFORE AND AFTER SCHOOL EXPANSION

The May Revision preserves the \$75 million commitment to expand Before and After School Care. The Governor's Budget proposed providing services to an additional 79,000 children in kindergarten through 9th grade. The January proposal included



\$45 million of additional State funding plus a reinvestment of \$30 million from proposed child care reform savings. Although the Administration has deferred its child care reform proposal, the May Revision continues the Administration's commitment to provide for full year annualization of the \$7.5 million General Fund expansion approved in Senate Bill 1 of the 2001-02 Third Extraordinary Session; \$41.2 million in new local assistance grants through 21st Century Community Learning Center funds; and an additional \$4.1 million of Proposition 98 General Fund for expansion, with a funding priority for middle schools.

Proposition 98 Guarantee

2001-02	-\$1,911.5 million
2002-03	\$848.4 million

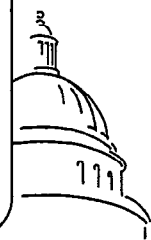
The General Fund savings in the current year result from a combination of the following: (1) a deferral of \$1.15 billion in current year programs to the budget year, with no net program reductions; (2) a shift of fund source for \$503 million in current year programs; (3) an increase in property taxes of \$193 million; and (4) naturally occurring savings offsetting growth in costs for a net savings of \$66 million. The current year total funding level remains the same; the General Fund savings do not result in any program reductions.

Combining the years 2001-02 and 2002-03, Proposition 98 funding is \$537 million lower than the Governor's Budget level, a 0.6 percent change.

The May Revision proposes to defer a total of \$1.149 million in undisbursed balances of 2001-02 program expenditures until July 2002. The funding of these programs from 2002-03 appropriations will delay payment by only a month.

Program	Dollars in millions
Instructional Time and Staff Development Reform Program	\$76
Standardized Testing and Reporting Program	61
Beginning Teacher Support and Assistance	39
Targeted Instruction Improvement Block Grant	713
High Achieving/Improving Schools (GPA)	144
Community Colleges	116

In the Governor's Budget, the minimum funding level for the budget year was established by Test 2, which adjusts the prior guarantee level for growth in attendance and the change in per capita personal income. The estimate in the Governor's Budget of the personal income change, which was based on the



economic forecast at that time, predicted per capita personal income would decline by 3.01 percent. In late April, the version of personal income that is used for calculating the guarantee and the State appropriations limit was released by the U.S. Department of Commerce. The new factor of -1.27 percent, coupled with a 0.3 percent increase in average daily attendance and prior year adjustments, results in an increase in the Test 2 level of \$1.184 billion.

The May Revision proposes to fully fund the Test 2 level including full repayment of the maintenance factor of \$3.9 billion. The proposed funding level exceeds the minimum required repayment by \$870 million in 2002-03.

The General Fund share of the guarantee increases by \$848 million. Of the \$335 million projected increase in local property taxes allocated to education, \$115 million results from proposals to establish Education Revenue Augmentation Fund allocations for multi-county special districts and redevelopment agencies.

FIGURE EDU-1

**Proposition 98
January vs. May Revision
(Dollars in thousands)**

2001-02	January Proposal	May Revision	Change
General Fund	\$31,404,751	\$29,493,343	-\$1,911,408
Local Revenue	13,571,871	13,762,699	\$190,828
Total Guarantee	\$44,976,622	\$43,256,042	-\$1,720,580
2002-03	January Proposal	May Revision	Change
General Fund	\$31,354,202	\$32,202,626	\$848,424
Local Revenue	14,629,176	14,964,402	\$335,226
Total Guarantee	\$45,983,378	\$47,167,028	\$1,183,650
Total Two-Year Funding	\$90,960,000	\$90,423,070	-\$536,930

FUNDING THE GUARANTEE

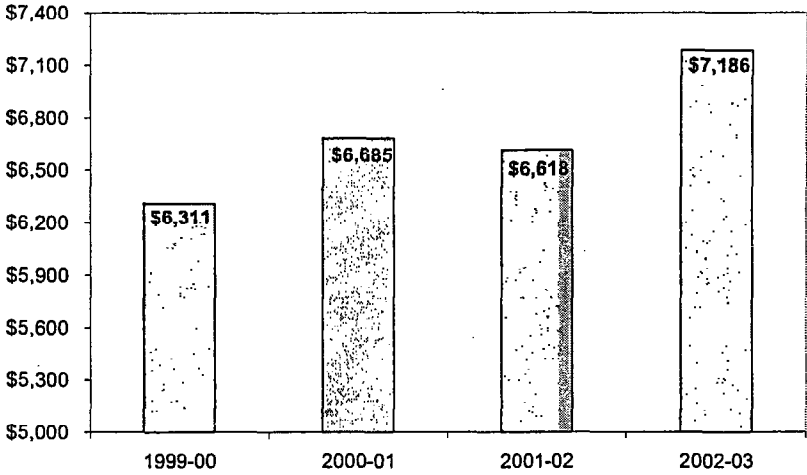
In order to fund the General Fund share of the guarantee, \$1.15 billion in undisbursed 2001-02 General Fund appropriations are proposed to be deferred until 2002-03 through current year special legislation. These appropriations will be counted toward the 2002-03 guarantee, and none of the deferred programs will incur a reduction.



In order to provide additional savings, 2001-02 expenditures of \$503 million for education programs are now proposed to be funded from the Proposition 98 Reversion Account (which does not count toward a current guarantee since its funds were previously appropriated and counted). This produces one-time savings for the General Fund in 2001-02. Additional savings of \$105 million are captured in 2001-02 to reflect actual expenditure levels. The reductions in 2001-02 Proposition 98 appropriations totaling \$1.912 billion leaves the total appropriation at \$5.5 billion above the Test 3 guarantee level in the current year.

FIGURE EDU-2

**K-12 Education Funding Per Pupil
Proposition 98**

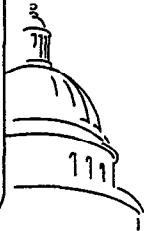


Funding per pupil under Proposition 98 continues to increase. Appropriations for 2001-02 will provide a funding level of \$6,618 per pupil. Per pupil funding of \$7,186 in 2002-03 represents an increase of 8.6 percent over the current year.

K-12 Education

2001-02	-\$1,380.9 million
2002-03	\$137.8 million

The May Revision reduces funds for K-12 Education by \$1,243.1 million over two years in General Fund resources compared to the Governor's Budget, a 2 percent reduction. These adjustments largely mirror those described in the section above. Total General Fund allocations of \$31.5 billion for K-12 education now represent 41.1 percent of the General Fund budget.



Current Year

School district and county office of education revenue limit appropriations decrease \$138.9 million, resulting primarily from significant increases in local property taxes that are partially offset by increased estimates of average daily attendance (ADA) and other miscellaneous adjustments. The May Revision includes estimated K-12 ADA growth of 1.9 percent, up from 1.5 percent in the Governor's Budget.

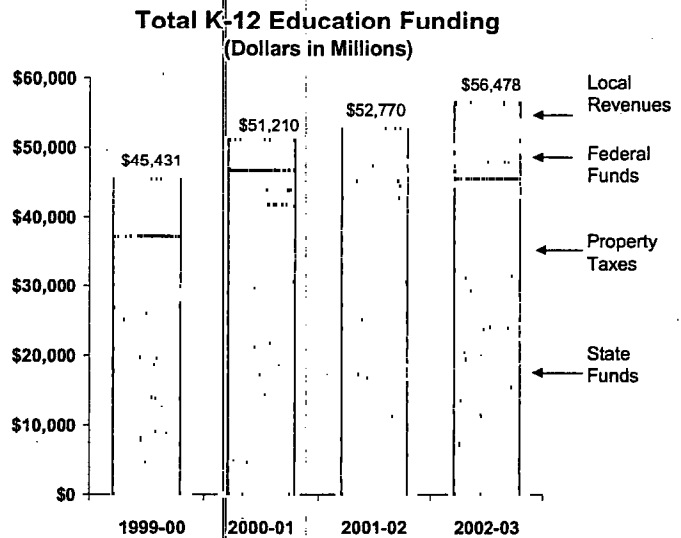
Budget Year

In the budget year, the revised ADA growth is up slightly, from 1.07 percent to 1.37 percent (about 42,000 ADA higher than the January estimate). The total number of ADA is estimated to be 5,800,896 in 2001-02 and 5,880,576 in 2002-03.

Funds available to K-12 education in 2001-02 from all sources are increasing from \$52.8 billion to \$56.5 billion in 2002-03

a 7 percent increase. In addition to \$1.8 billion of General Fund growth, local property taxes grow by \$1.1 billion, and federal funds grow by \$0.9 billion.

FIGURE EDU-3



GROWTH ADJUSTMENTS

The May Revision provides over \$290 million in new funds to provide an increase in the statutory growth rate from 1.07 percent to 1.37 percent. Major enrollment adjustments include an increase of \$166.6 million for K-12 school district apportionments, \$9.8 million for county office of education apportionments, \$10.3 million for special education, and \$3.5 million for categorical programs in the former Mega-item. Other major adjustments include significant costs to pay for reductions in the PERS offset funding of \$97 million for school district apportionments and \$7.8 million for county offices of education. The PERS adjustments reflect the Administration's withdrawal of the proposed PERS deferral and the increase in the PERS employer contribution rate calculated at 2.89 percent of projected salaries.



COST OF LIVING ADJUSTMENT (COLA) REVISIONS

The May Revision also makes adjustments to the amount provided for K-12 COLA as the statutory rate has been recomputed and adjusted from 2.15 percent to 1.66 percent. This change results in decreases in various K-12 categorical programs (\$12 million). The May Revision proposes to provide \$107.6 million to raise the COLA rate for general purpose apportionments (for school districts and county offices) and special education to a higher rate of 2 percent.

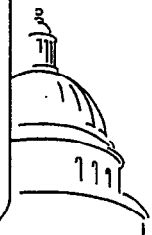
CHILD CARE

Reform Proposal—The Governor's Budget proposed significant reforms to child care programs in the areas of eligibility, copayments, and reimbursement limits in an attempt to make the system more equitable and to curb the rapidly increasing costs of continuing services in Stage 3 for prior CalWORKs recipient families. Although significant discussions with stakeholders and the Legislature have taken place since January, there has been no agreement reached with the Administration on a package of reforms that can be implemented in time to increase the number of child care slots and appreciably reduce costs for the budget year.

Therefore, the May Revision proposes to suspend the reform proposal, restore programs to baseline levels as adjusted for revised caseload projections, and extend services, through the budget year only, for all prior CalWORKs families who reach the time limits for transitional benefits. The Administration expects reform discussions to resume with the Legislature and stakeholders next year within the context of implementing federal reauthorization of the Temporary Assistance for Needy Families program.

The May Revision also includes several proposals aimed at improving the system. These include improving the methodologies for determining annual adjustments to eligibility and reimbursement rates; enhanced accountability and fraud detection; and an update of the information necessary to estimate the effects of policy changes. These improvements should help lay a better foundation for discussion to restructure the child care system. Stage 3 caseload projections estimate a need for \$358.5 million in the budget year, escalating to \$747.8 million in 2005-06. It is unclear how the State will meet those out-year costs absent restructuring.

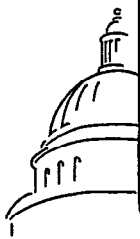
Caseload Changes and Adjustments—Changes to Department of Education-administered child care programs reflect an overall net cost reduction of \$29.6 million, including Proposition 98 cost decreases (\$115.2 million), which are offset by additional one-time federal funds and prior year State program savings (\$47.4 million)



EXPENDITURES

and new federal No Child Left Behind funding (almost \$42 million). Significant programmatic changes (after adjustments necessary to restore baseline program costs to reverse the assumed reform savings) include:

- ❖ \$103.7 million net increase to fully fund the budget year Stage 3 cohort (\$58.3 million Proposition 98 and \$45.4 million in various one-time federal and prior year State savings). The total average monthly caseload for the new cohort is estimated at 16,800, a decrease of about a 1,000 compared to January.
- ❖ \$22.2 million Proposition 98 reduction in baseline costs for the continuing costs of the current Stage 3 caseload into the budget year based on a reduced caseload estimate. The total average monthly caseload is estimated at 41,200, a decrease of almost 3,000, compared to January.
- ❖ \$85.9 million Proposition 98 reduction in baseline costs for Stage 2 based on reduced caseload estimates. The total average monthly caseload is estimated at 109,200, a decrease of approximately 21,400 compared to January. The drop in estimated caseload is primarily due to individuals meeting their five-year federal time limit for CalWORKs, thus removing the initial influx of clients from the caseload.
- ❖ \$2 million setaside for legislation aimed at increasing fraud detection and compliance improvements to ensure limited subsidies are retained for the neediest families.
- ❖ \$30.1 million net increase for Before and Afterschool programs consisting of an \$11.1 million dollar Proposition 98 reduction and a \$41.2 million increase from new No Child Left Behind federal funding. This reduction still leaves an increase of \$33.8 million of State funds for this purpose and an overall program increase of \$75 million.
- ❖ \$49.7 million Proposition 98 reduction to delete the shift in State funds to SDE child care made in the January Budget that was intended to retain Stage 1 anticipated reform savings for expansion of the regular child care system. The baseline cost increase for Stage 1 is reflected in the Department of Social Services budget, and adjustments have been made there to reflect revised caseload and related Stage 1 cost adjustments.
- ❖ \$5.9 million COLA reduction to reflect a change in the COLA factor from 2.15 percent to 1.66 percent (\$4.7 million Proposition 98 and \$1.2 million federal funds).



2002-03

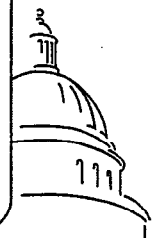
Federal Education Reform: No Child Left Behind (NCLB) Act

The Federal NCLB Act provides California with approximately \$738 million in increased funding which is proposed to be used to further the following policy objectives of the Administration: 1) increasing accountability, 2) enhancing parental involvement, 3) tracking student performance, 4) improving teacher and administrator quality, and 5) increasing local flexibility. Specific proposals are outlined below.

IMPROVING THE QUALITY OF INSTRUCTION

The federal NCLB will complement the State's existing instructional quality efforts by providing funding, as follows:

- ❖ \$131.1 million for K-3 teachers to attend high quality teacher training programs, such as those operated by UC for reading, and purchase standards-aligned reading materials. Targeting these funds for professional development will allow the State to ensure that about 52,400 of the approximately 92,000 K-3 teachers receive this critical training as expeditiously as possible.
- ❖ \$315 million to improve teacher, paraprofessional, and administrator quality, and increase the number of highly qualified teachers in the classroom.
- ❖ \$206.7 million for K-3 class size reduction.
- ❖ \$78.3 million, for a total of \$110 million, for the Mathematics and Reading Professional Development Program, to provide K-12 teachers with professional development in these subjects.
- ❖ \$30 million for the Teaching As A Priority Block Grant, to recruit credentialed teachers to work in low-performing schools.
- ❖ \$8.3 million for competitive grants to school districts that form professional development consortia.
- ❖ \$5 million for the University of California-operated California Subject Matter Project for Science.
- ❖ \$1.6 million for the Principal Training Program.



ENHANCING ACCOUNTABILITY

Title VI, Part A, of the NCLB will provide California over \$28.9 million in 2002-03 to develop and implement the State's system of assessments. The May Revision proposes to use \$20.1 million of these funds to continue strengthening the State's system of assessments and accountability. The remaining \$8.8 million will be used for activities that may become necessary once more information regarding the requirements of the NCLB become available. The proposed uses of the \$20.1 million include:

- ❖ \$10.3 million for data gathering and to develop longitudinal databases, including unique student identifiers to obtain the individual student-level assessments required by the NCLB.
- ❖ \$5.1 million for the development and refinement of the High School Exit Exam, Standardized Testing and Reporting Exam, and the English Language Development Test.
- ❖ \$1.9 million for activities to ensure that pupils in Special Education or alternative schools are able to participate in the State's system of assessments and accountability.
- ❖ \$900,000 for an information campaign to help parents, teachers, and pupils become more informed regarding standards and statewide assessments and their role in the accountability system.

The May Revision also includes \$17.9 million and 63.5 positions (33.5 new or limited-term extensions, and 30 redirections from existing position authority) for NCLB-related state operations to address workload requirements necessary for administering the new and expanded federal program (i.e., awarding grants, ensuring compliance, providing technical assistance, and more).

PROVIDING FOR SCHOOL IMPROVEMENT

The May Revision proposes an increase of approximately \$300 million for improving academic achievement for economically disadvantaged students, including \$6.5 million for implementing sanctions for schools that have not shown progress in improving academic performance. Use of these funds will be prioritized to meet the needs of the lowest performing schools first and to make progress toward the goal that a highly qualified teacher will be in every classroom.

Additionally, an increase of approximately \$30 million is proposed for computers in the classroom and professional development.



ENHANCING INSTRUCTION FOR STUDENTS WITH SPECIAL NEEDS

Recognizing that students with special needs require enhanced instruction, the May Revision directs NCLB funds for the following:

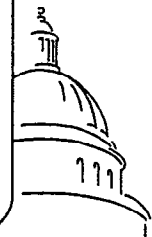
- ❖ An expansion of approximately \$69 million for ensuring that all English language learners obtain English proficiency and obtain a high level of academic success.
- ❖ An increase of approximately \$25 million for meeting the special needs of migrant, homeless, rural, or other targeted populations.

IMMEDIATE INTERVENTION/UNDERPERFORMING SCHOOLS PROGRAM (II/USP)

In October 2002, an estimated 50 schools may be subject to sanctions pursuant to the II/USP, which requires the State to sanction schools that fail to make progress in improving their Academic Performance Index (API) scores during the two years of implementation grants. In consultation with the State Board of Education (SBE), the Superintendent of Public Instruction (SPI) may choose from a menu of options including: (1) require the district to contract with a school assistance team to work with the school on a plan to assist the school in meeting growth targets, or (2) State take-over/assignment of a management team to the school.

To ensure that the assistance teams and management teams are effective in helping these schools improve academic performance, the May Revision proposes to:

- ❖ Provide \$50,000 per school site for costs associated with the initial assessment and planning activities of the intervention or takeover team (\$2.5 million).
- ❖ Provide funding of up to \$150 per pupil based on an approved plan (\$6 million).
- ❖ Provide funding to build capacity for addressing a larger number of schools subject to sanctions in future years when more under performing schools are expected to be identified (\$4 million).



- ❖ Require that these schools make significant growth on the API within two years.
- ❖ Require a *dollar-for-dollar match* by the district.
- ❖ Make funding contingent upon approval of a plan by the SBE as recommended by the SPI.

California State Library

2001-02	—
2002-03	-\$15.6 million

Due to the State's current fiscal constraints, the May Revision proposes the following program reductions:

- ❖ \$610,000 for the California Library Services Act.
- ❖ \$750,000 for civil liberties education services.
- ❖ \$2.4 million for the Library of California.
- ❖ \$11.8 million for the Public Library Foundation.



Higher Education

California Community Colleges

2001-02	-\$109.3 million
2002-03	\$115 million

Current Year

Current year Proposition 98 General Fund expenditures for the California Community Colleges (CCC) decreases by \$109.3 million which includes a current year deferral (-\$115.6 million) of undisbursed allocations to the budget year and to reflect reduced savings from a slightly lower estimate of property tax revenues (\$6.3 million).

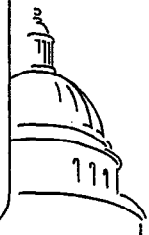
Budget Year

Total revenues for the CCC are estimated to be \$6.6 billion from all funds in 2002-03, a \$326.9 million increase over the revised estimate for 2001-02.

The May Revision proposes a net \$115 million Proposition 98 General Fund increase for local assistance. The increase reflects the following changes:

- ❖ A restoration of \$20 million for the Special Services for CalWORKs program, which will leverage a 1-to-1 local match, thus increasing services to CalWORKs recipients at community colleges a total of \$40 million. The services provided are aimed at increasing self-sufficiency and include work-study, job development, and coordination with county agencies.
- ❖ A net decrease of \$20.6 million resulting from increased local revenue that offset state costs (\$13.7 million), a reduced statutory COLA factor of 1.66 percent (\$20.2 million), and an increase of \$13.3 million to reflect a policy decision to provide a 2 percent COLA for apportionments.
- ❖ An increase of \$115.6 million to reflect the deferral of current year undisbursed funds into the budget year.

The May Revision proposes no additional reductions for the CCC.



University of California (UC)

2001-02	—
2002-03	-\$162.4 million

In light of the State's current fiscal constraints, the May Revision proposes reducing the UC's General Fund by a net \$162.4 million from the level proposed in the Governor's Budget, as outlined below. These reductions are intended to have no direct effect on core classroom instructional needs.

AUGMENTATIONS

- ❖ \$5.4 million to fully fund a projected enrollment increase of 600 full-time equivalent (FTE) students. This brings total budgeted enrollment growth, including summer enrollment, to 8,597 FTE students.
- ❖ \$2.8 million to address increased costs of annuitant health and dental benefits.

Reductions from the Governor's Budget include:

- ❖ \$5.15 million to reduce funding for K-12 Internet2.
- ❖ \$32.08 million to reduce funding for research.
- ❖ \$29 million to reduce funding, on a one-time basis, for Information Technology, Instructional Equipment, Library Materials, and Deferred Maintenance.
- ❖ \$8.4 million to eliminate funding for the UC College Preparatory Initiative.
- ❖ \$750,000 to eliminate funding for the Arts Bridge Program.
- ❖ \$509,000 to eliminate funding for UC All Campus Collaborative on Outreach Research (ACCORD).
- ❖ \$12.01 million to eliminate funding for K-12 School-University Partnerships.
- ❖ \$1.94 million to eliminate funding for Central Valley Outreach Programs.
- ❖ \$4.7 million to reduce funding for Graduate and Professional School Outreach.
- ❖ \$11.3 million to reduce funding for the Subject Matter Projects.



- ❖ \$50.86 million to reduce funding for the Professional Development Institutes. Instead of direct State funding, school districts will be able to utilize new federal funds from the No Child Left Behind Act for this successful staff development program.

The following technical change is proposed:

- ❖ \$13.8 million in savings as a result of lower overall costs, and additional reimbursements available to offset the costs, of lease purchase payments.

California State University (CSU)

2001-02	—
2002-03	-\$50.4 million

Due to the change in the State's fiscal outlook, the May Revision proposes reducing the CSU's General Fund by a net \$50.4 million from the level proposed in the 2002 Governor's Budget, as outlined below. These reductions are intended to have no direct impact on core classroom instructional needs.

AUGMENTATIONS

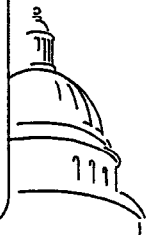
- ❖ \$19.5 million to fully fund a projected enrollment increase of 3,008 FTE students. This brings total budgeted enrollment growth, including summer enrollment, to 15,278 FTE students.
- ❖ \$38,000 to address increased cost of annuitant dental benefits.

Reductions from the Governor's Budget include:

- ❖ \$43 million to reduce funding, on a one-time basis, for Information Technology, Instructional Equipment, Library Materials, and Deferred Maintenance.
- ❖ \$6 million to eliminate funding for the Education Technology Professional Development Program.
- ❖ \$21 million to reflect proposed trailer bill language to convert the Governor's Teaching Fellowships from scholarships to assumptions of loan repayments.

The following technical change is proposed:

- ❖ \$209,000 augmentation to address increased insurance costs related to lease purchase payments.



Student Aid Commission (SAC)

2001-02	-\$10 million
2002-03	-\$78.9 million

Cal Grants: The May Revision proposes sufficient resources to fully fund awards for all eligible participants under the Cal Grant Entitlement Program and fully funds Cal Grant Competitive Programs. Based on the latest estimates from the SAC, the number of eligible applicants for Cal Grant Entitlement awards will be 5,000 fewer than projected in the Governor's Budget. In addition, the number of current year renewal entitlement and competitive awards is lower than originally estimated by the SAC, resulting in current year savings of \$10 million. Based on that information, the SAC has also revised its assumptions on acceptance rates, which results in further cost savings in 2002-03. Consequently, the May Revision reflects a reduction of \$58 million from the amount included in the Governor's Budget.

CalSOAP: Given the need to increase financial aid awareness and outreach activities to ensure all eligible students apply and obtain financial aid, whether in the form of loans or grants, the Governor's Budget proposes a shift in the emphasis of the California Student Opportunity and Access Program (CalSOAP) to focus more on financial aid awareness and outreach activities. As a result, the May Revision proposes a shift of \$8.6 million for CalSOAP from the General Fund (including \$990,000 in Proposition 98 General Fund) to reimbursements from the Federal Family Education Loan Program, consistent with the federal requirements for the use of those funds.

Due to the decline in General Fund revenues, the May Revision proposes reductions from the Governor's Budget as follows:

- ❖ \$5.26 million to eliminate funding for the California Work Study Program. Institutional based financial aid programs already provide significant funding for this purpose.
- ❖ \$4 million to reduce the number of new Cal Grant C awards from 7,761 awards to 4,796 awards.
- ❖ \$3 million to reduce the number of new Cal Grant T awards from 2,495 awards to 1,746 awards.



California Postsecondary Education Commission (CPEC)

2001-02	—
2002-03	-\$2.8 million

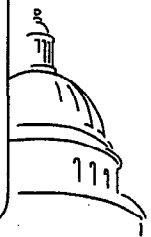
In light of the change in the State's fiscal outlook, the May Revision proposes reducing CPEC's General Fund by \$2.8 million from the level proposed in the Governor's Budget to reflect elimination of 43.2 positions and related operating expenses and equipment, and TERADATA services received from the Teale Data Center.

Scholarshare Investment Board (SIB)

2001-02	-\$4 million
2002-03	-\$8 million

The May Revision proposes sufficient resources to fully fund awards to all eligible students under the Governor's Scholarship Programs administered by the SIB. Given the latest estimate of the number of high school students that meet the criteria to receive a scholarship under the Governor's Distinguished Mathematics and Science Scholars Program, the May Revision proposes an \$8 million reduction in funding for this purpose. The remaining \$6 million is sufficient to provide 2,400 scholarships.

In addition, based on the actual number of eligible participants for the Governor's \$1,000 Scholars Program Awards being lower than originally estimated, it is expected that there will be approximately \$4 million in savings in 2001-02.

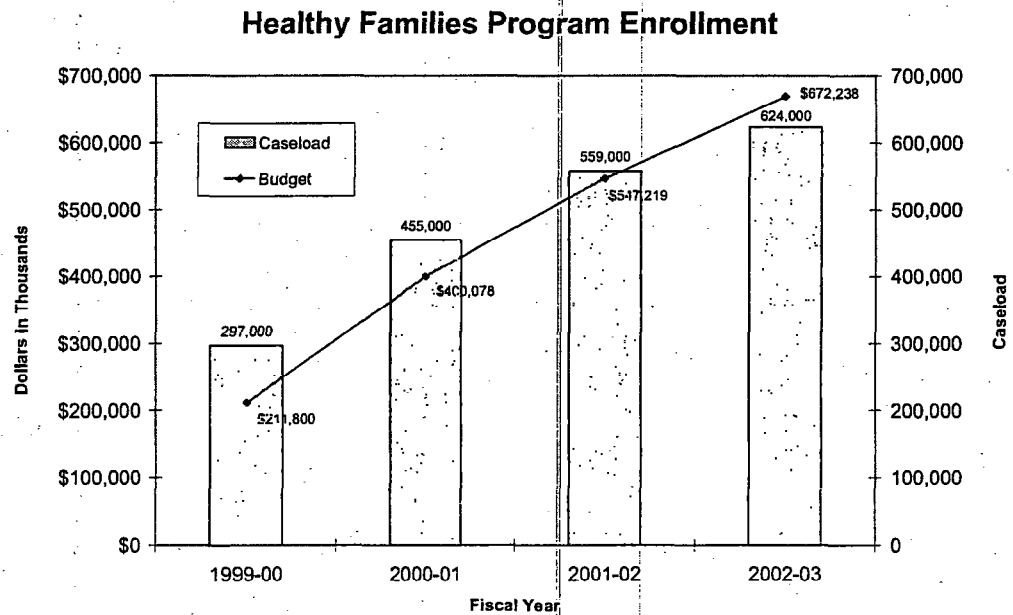


Health and Human Services

Healthy Families Program

Providing health care coverage to uninsured children remains a high priority for this Administration. Currently, more than 538,000 children are enrolled in the Healthy Families Program (HFP) with a total of 559,000 expected to be enrolled by the end of June 2002. It is expected that by June 30, 2003, a total of 624,000 children will be provided low-cost, comprehensive health care coverage through the HFP. See Figure HHS-1.

Figure HHS-1



The May Revision continues funding to facilitate the enrollment and eligibility of uninsured children into the HFP, as follows:

- ❖ \$2.6 million (\$1.4 million Tobacco Settlement Fund [TSF]) to establish a two-month HFP to Medi-Cal coverage bridge.



- ❖ \$270,700 (\$94,000 TSF) to support Rural Health Demonstration Projects that will allow children in migratory families to retain HFP coverage when they move between counties.
- ❖ \$588,000 (\$288,000 General Fund) for additional caseload resulting from implementation of the Child Health and Disability Prevention Gateway Program.

Health Insurance Portability and Accountability Act

In August 1996, the federal Health Insurance Portability and Accountability Act (HIPAA) was enacted. The purpose of the HIPAA is to improve the portability and continuity of health insurance coverage, provide administrative simplification, revise security procedures, and combat waste in health care service delivery. The HIPAA requires specific national standards for coding and tracking medical information, administrative simplification, and security and privacy of individual patient medical records. The management of activities related to the HIPAA will be complex as it affects many different areas within State agencies and programs. To ensure the successful implementation of HIPAA regulations, the Administration established the Office of HIPAA Implementation (OHI) within the Health and Human Services Agency to assume statewide leadership in this important endeavor. In addition, Chapter 635, Statutes of 2001 (SB 456), establishes specific requirements for the OHI to meet in its role as statewide HIPAA coordinator.

STATEWIDE HIPAA FUNDING

The May Revision increases General Fund expenditures for the HIPAA by \$194,000 while total funds are reduced by \$7.1 million. This funding is in addition to \$92.3 million (\$24.3 million General Fund) proposed in the Governor's Budget. The revised budget provides a total of \$85.2 million (\$24.5 million General Fund) for this purpose. The Administration recognizes the importance of this federal legislation and is working toward full compliance. The overall reduction in the May Revision will not adversely affect any critical compliance activities.

Figure HHS-2 reflects the anticipated 2002-03 HIPAA expenditures by department.

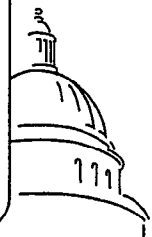


Figure HHS-2

**2002-03 HIPAA Funding
(Dollars in Thousands)**

Department	Governor's Budget		May Revision		Overall Funding	
	GF	TF	GF	TF	GF	TF
Health Services	\$16,751	\$78,622	-\$4,170	-\$12,500	\$12,581	\$66,122
Alcohol and Drug Programs	3,021	6,042	-750	-1,500	2,271	4,542
Mental Health	1,211	2,422		0	1,211	2,422
Developmental Services	1,257	2,514	51	101	1,308	2,615
Statewide Health Planning and Development	0	99		0	0	99
Health and Human Services Agency	2,045	2,624	2,645	2,895	4,690	5,519
Aging			130	200	130	200
Corrections			898	898	898	898
Youth Authority			591	591	591	591
Social Services			665	1,603	665	1,603
Personnel Administration				225	0	225
CalPERS				223	0	223
Veteran's Affairs			134	134	134	134
Total	\$24,285	\$92,323	\$194	-\$7,130	\$24,479	\$85,193

Department of Health Services

MEDI-CAL

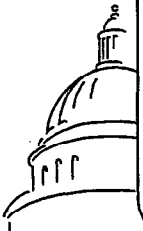
2001-02 **\$87.1 million**
2002-03 **-\$758.3 million**

Current Year

The May Revision includes total Medi-Cal expenditures of \$27.1 billion (\$9.8 billion General Fund), an increase of \$324.8 million above the Governor's Budget. General Fund expenditures for Medi-Cal have increased by \$87.1 million, or 0.9 percent.

The number of persons projected to be eligible for Medi-Cal in 2001-02 is expected to decrease by 268,300 to 5,926,700 eligibles. This represents a decrease of about 4.3 percent below the level projected in the Governor's Budget. The revised caseload is 12.1 percent above 2000-01 caseload.

The net General Fund increase includes the following significant adjustments:



- ❖ \$72.5 million increase in the cost of inpatient services.
- ❖ \$70.8 million increase due to higher than anticipated caseload growth resulting from the elimination of quarterly status reports.
- ❖ \$7.8 million increase for higher county administrative costs.
- ❖ \$2.3 million increase to provide a managed care rate increase for the Santa Barbara Health Authority.
- ❖ \$28.9 million in estimated additional savings due to increased anti-fraud activities.
- ❖ \$15.7 million in estimated savings resulting from smaller than anticipated increases in caseload growth resulting from continuous eligibility for children.
- ❖ \$11.9 million in savings attributable to additional supplemental and federal drug rebates.
- ❖ \$9.8 million in estimated net savings due to a variety of other increases and decreases affecting the Medi-Cal program.

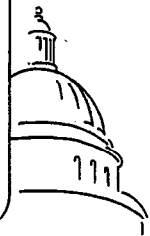
Budget Year

The May Revision includes total Medi-Cal expenditures of \$25.8 billion (\$9.3 billion General Fund), a decrease of \$1.1 billion (\$758.3 million General Fund) below the Governor's Budget.

The average monthly Medi-Cal caseload is expected to decrease by 490,600 beneficiaries to 6,008,500 eligibles. This represents a decrease of 7.5 percent below the Governor's Budget.

The budget year includes the following significant General Fund adjustments:

- ❖ \$73.3 million increase in the cost of inpatient services.
- ❖ \$9.1 million in increased costs to provide a long-term care rate increase.
- ❖ \$4.5 million increase to provide a managed care rate increase for the Santa Barbara Health Authority.
- ❖ \$105.9 million in estimated additional savings due to increased anti-fraud activities.
- ❖ \$17.1 million in savings attributable to additional supplemental and federal drug rebates.



- ❖ \$584.4 million in reduced expenditures due to a variety of other increases and decreases affecting the Medi-Cal program including the following significant reductions.

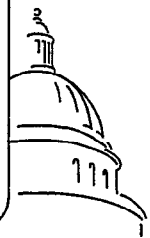
GENERAL FUND REDUCTIONS

Continued weakness in the stock market and the economy have caused State revenue receipts to be below forecast since the release of the Governor's Budget. The May Revision revenue estimate significantly reduces the available General Fund resources for the current and budget years. This revenue reduction, combined with expenditure adjustments required for enrollment, caseload, and population changes, necessitates the reduction or elimination of various program proposals included in the January Governor's Budget. In light of the State's fiscal constraints, the Administration is proposing the following reductions:

- ❖ **Selected Medi-Cal Optional Benefits**—\$526 million (\$263 million General Fund) for the elimination of certain Medi-Cal optional benefits.
- ❖ **Medi-Cal Quarterly Status Reports**—\$310.8 million (\$155.4 million General Fund) to reinstate Medi-Cal quarterly status reporting. This proposal will not affect the eligibility of children in Medi-Cal. In January 2001, the Administration established continuous eligibility for children. The 2002-03 Budget includes a total of \$374 million (\$187 million General Fund) to provide continuous eligibility for 471,550 children. Since 2000-01, the Administration has provided a total of \$654.6 million (\$327.3 General Fund) for this purpose.
- ❖ **1931(b) Medi-Cal Program**—\$184.2 million (\$92.1 million General Fund) to rescind the expansion of the 1931(b) Medi-Cal program, which had expanded Medi-Cal eligibility to two-parent working families with income up to 100 percent of the federal poverty level. This proposal will primarily affect two-parent income households who apply for Medi-Cal, but will retain current two-parent income recipients. Other applicants and some current beneficiaries (children and single parents) would still qualify for free Medi-Cal through another eligibility category or would qualify for Medi-Cal with a share-of-cost.
- ❖ **Provider Rate Reductions**—\$94 million (\$47 million General Fund) to further reduce Medi-Cal provider rates below the level proposed in the Governor's Budget.
- ❖ **Chapters 894 and 897, Statutes of 2001 (AB 59 and SB 493) Medi-Cal Expansion**—\$51.6 million (\$25.8 million General Fund) to defer the Medi-Cal expansion associated with the National School Lunch and Food Stamp programs. This expansion is proposed to be deferred until July 2005.



- ❖ **Early and Periodic Screening, Diagnosis, and Treatment Program**—\$65.1 million (\$35 million General Fund) to reflect the reduction of the State's share of the cost of growth in the Early and Periodic Screening, Diagnosis, and Treatment Program and Therapeutic Behavioral Services Program.
- ❖ **Disproportionate Share Hospital Program Administrative Fee**—\$31 million General Fund to increase the Disproportionate Share Hospital administrative fee. This General Fund decrease, combined with the \$55.2 million General Fund reduction already proposed in the Governor's Budget for this purpose, results in a total increase of \$86.2 million in the State administrative fee for 2002-03.
- ❖ **Pharmacy Reimbursement**—\$23.8 million (\$11.9 million General Fund) to rescind prescription drug reimbursement increases totaling \$0.40 per claim.
- ❖ **Medi-Cal/Healthy Families Program Outreach for Children**—\$18.6 million (\$7.2 million General Fund) to reflect the elimination of Medi-Cal/Healthy Families Program (HFP) media advertising. Important activities that facilitate the enrollment of children into Medi-Cal and the HFP will be continued. These activities include application assistance and a toll-free information help line.
- ❖ **Medical Case Management Program Expansion**—\$9 million (\$4.5 million General Fund) in savings achievable through the expansion of the Medical Case Management Program, which provides care to severely ill Medi-Cal beneficiaries in their home, avoiding more costly institutional care.
- ❖ **Dental Cleanings and Exams**—\$7.9 million (\$4 million General Fund) to limit dental cleanings and basic exams to one visit annually. This benefit was expanded in the 2000 Budget Act to include two dental cleanings and basic exams annually.
- ❖ **Contracting for Durable Medical Equipment and Lab Services**—\$6.6 million (\$3.3 million General Fund) to reflect savings as a result of competitively contracting for durable medical equipment and lab services.
- ❖ **Implementation of Chapter 684, Statutes of 2001 (AB 1075)**—\$499,000 (\$250,000 General Fund) to reduce 6.5 positions included in the Governor's Budget for workload associated with Chapter 684. This legislation requires the Department of Health Services to develop staffing ratios and a new reimbursement methodology for nursing facilities. Despite this reduction, the Administration will continue to move forward with this important effort.
- ❖ **County Administration**—\$175.9 million (\$87.9 million General Fund) to reflect a 20 percent reduction in Medi-Cal county administration funding.



FEDERAL MEDICAL ASSISTANCE PERCENTAGE

The Federal Medical Assistance Percentage is the percentage of Medicaid costs reimbursed by the federal government and is based on U.S. Bureau of Census estimates of state population. The Governor's Budget proposed a \$400 million General Fund reduction in various departments and a corresponding increase in federal funding in the current year in anticipation of federal legislation that would provide an additional \$400 million to offset the cost of Medi-Cal services. In light of the continuing discussion of this issue in Congress, the May Revision now proposes this adjustment in 2002-03.

PUBLIC HEALTH

2001-02	\$1.3 million
2002-03	\$27.8 million

CASELOAD PROGRAMS

Current Year

The May Revision includes an increase of \$2.3 million General Fund, or 0.2 percent above the \$150.6 million provided in the Governor's Budget, due to an increase in caseload and health care costs in the California Children's Services (CCS), Child Health and Disability Prevention (CHDP), and Genetically Handicapped Persons programs.

Budget Year

The May Revision includes an increase of \$10.4 million General Fund, or 9.4 percent above the \$110.6 million provided in the Governor's Budget, due to an increase in caseload and health care costs in the CCS and Genetically Handicapped Persons programs. In addition, the May Revision proposes to provide budget year funding of \$35.7 million General Fund and \$56.7 million Tobacco Settlement Fund (TSF) for the CHDP program.

CHDP PROGRAM GATEWAY TO COMPREHENSIVE HEALTH CARE

The May Revision includes \$2.7 million (\$836,000 General Fund) to augment the CHDP program. This funding will be used to develop an Internet pre-enrollment application for Medi-Cal and the Healthy Families Programs (HFP).



The CHDP currently provides health assessments to approximately 1.1 million children each year. However, the program does not directly provide follow-up treatment for conditions found during the health assessment or provide dental or vision services.

Most of the children covered by the CHDP program are also eligible for comprehensive health care under Medi-Cal or the HFP. The May Revision proposes to use the CHDP program as a gateway to streamline enrollment into these comprehensive health care programs.

Under this plan, pre-enrolled children will be immediately eligible, for up to two months, for a CHDP health assessment and for comprehensive medical care provided through Medi-Cal or the HFP.

CANCER RESEARCH

The May Revision restores the \$25 million reduction made to the Cancer Research Program included in the Governor's Budget, by including \$12.5 million General Fund to match private funding sources. Cancer research funding is primarily directed to projects addressing gender-specific cancers.

ADULT INFLUENZA VACCINE PURCHASE

The May Revision includes an increase of \$2.6 million General Fund to fund price increases of \$3.70 per dose for the adult influenza vaccine. The Budget provides funding for 700,000 doses of the vaccine through local distribution centers, primarily to senior citizens. This increase more than doubles the Administration's support of vaccines for the elderly.

PUBLIC HEALTH PREPAREDNESS AND RESPONSE

The May Revision includes an increase of \$50.8 million in federal grant funding, provided by the federal Centers for Disease Control and Prevention (CDC) and the Health Resources and Services Administration, to support anti-bioterrorism activities by the State and its 58 counties, except Los Angeles County, which has been provided direct grant funding. These funds will be used to upgrade infectious disease surveillance and investigation, enhance the readiness of hospital systems to deal with large numbers of casualties, and expand public health laboratory and communications systems capability. The federal funds are provided to California to meet seven critical "Focus Areas," as outlined in Figure HHS-3.

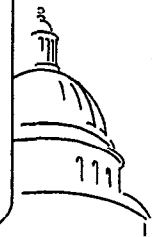


Figure HHS-3

Public Health Preparedness and Response

Focus Area	Dollars in Millions	Percent of Total Funding
Planning & Readiness Assessment	\$19.5	38
Surveillance & Epidemiological	10.4	21
Biologic Laboratory Capacity	6.7	13
Chemical Laboratory Capacity ^{1/}	0.0	0
Communications & Information Technology	6.4	13
Health Risk Communications	2.6	5
Education & Training	5.2	10
Totals	\$50.8	100

^{1/} No additional funds will be expended on this focus area because the State already possesses this capacity.

The activities to be funded through this grant are vitally important to the security of California and the country. It is CDC's intent that the activities identified in recipient work plans should be pursued vigorously with as little time lost in start-up as possible.

Specifically, of the \$50.8 million available, the May Revision proposes \$16.3 million to develop and enhance State-level preparedness, \$9.1 million to be distributed to the Emergency Medical Services Authority to upgrade hospital preparedness planning, and \$25.4 million in direct subventions to counties for development of local anti-bioterrorism activities.

DOMESTIC VIOLENCE SHELTER GRANTS

The May Revision includes an increase of \$900,000 Domestic Violence Education and Training Fund to continue funding ten domestic violence shelters that received current year funding through the Nine West legal settlement. This 5 percent increase continues the Administration's support of emergency shelters, transitional housing, legal assistance, and counseling for the victims of domestic violence.

AIDS DRUG ASSISTANCE PROGRAM

The May Revision includes an increase in total funding of \$1.3 million for the AIDS Drug Assistance Program (ADAP) to fund higher caseload in the Diagnostic Assay Program. Total funding for the ADAP is \$190.5 million, an increase of \$50.8 million (\$27.8 million General Fund), or 26.5 percent, since the 1999 Budget Act.



GENERAL FUND REDUCTIONS

Due to changes in the State's fiscal outlook, the May Revision proposes the reduction or elimination of various program proposals included in the Governor's Budget. Funding for public health and the Department of Health Services' Administration programs for 2002-03 totals \$2.7 billion (\$667 million General Fund), or \$164.9 million (\$133.8 million General Fund and \$31.1 million TSF) above the amount provided in 1999-00. Specifically, the May Revision reflects the following reductions:

- ❖ **Youth Anti-Tobacco Program**—\$35 million TSF proposed for allocation to local tobacco prevention programs targeted at high school and college-aged persons.
- ❖ **Expanded Access to Primary Care (EAPC) Program**—\$17.5 million TSF for the EAPC program. The Governor's Budget proposed to shift CHDP caseload to Medi-Cal and the Healthy Families Program. The Governor's Budget provided this augmentation to provide health screening and immunizations to children receiving CHDP services who would not have been eligible for Medi-Cal or the Healthy Families Program. Consistent with restoration of funding for the CHDP, the May Revision proposes to eliminate this augmentation for the EAPC program.

TOBACCO SETTLEMENT FUNDS

The 1998 Master Tobacco Settlement requires tobacco companies to make payments to the states totaling an estimated \$206 billion nationally through 2025. California is projected to receive an estimated \$25 billion over 25 years. In 2001-02, the State is projected to receive \$488.2 million, an increase of \$13.2 million over the amount estimated in the Governor's Budget. In 2002-03, the State is projected to receive \$474.4 million, the same amount estimated in the Governor's Budget. Local governments will receive an equal amount. For programs funded in 2002-03 using Tobacco Settlement Funds, see Figure HHS-4.

The May Revision reflects the following changes in the Tobacco Settlement Funding proposed in the Governor's Budget:

- ❖ **Healthy Families Program**—A decrease of \$11.4 million below the \$229.9 million included in the Governor's Budget. This decrease is the result of a projected caseload decline in the program.
- ❖ **Access to Infants and Mothers**—An increase of \$2.7 million above the \$1.6 million included in the Governor's Budget. This increase is the result of projected caseload growth in the program.

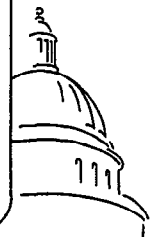


Figure HHS-4

**Tobacco Settlement Fund
(Dollars in Thousands)**

Revenues	\$474,400
Prior Year Carryover	68,627
	<hr/>
Total Resources	\$543,027
	<hr/>
Expenditures:	
Healthy Families Program	229,867
Access for Infants and Mothers (AIM)	4,296
Medi-Cal Expansion:	
Section 1931(b) of Title XIX of the Social Security Act	206,055
Breast and Cervical Cancer Treatment	21,733
State-Only Breast and Cervical Cancer Treatment	11,130
Child Health and Disability Prevention	49,946
Prostate Cancer Treatment	20,000
	<hr/>
Total Expenditures	\$543,027
	<hr/>
Ending Balance	\$0

- ❖ **CHDP Program**—The Governor's Budget proposed to shift CHDP caseload to Medi-Cal and the Healthy Families Program. As discussed in the "CHDP Gateway to Comprehensive Health Care" issue above, the May Revision restores \$49.9 million TSF for the CHDP and includes additional funding for system enhancements that will allow the CHDP program to serve as a gateway to Medi-Cal and the Healthy Families Program.
- ❖ **Medi-Cal Expansions**—An increase of \$79 million above the \$127.1 million provided in the Governor's Budget to expand Medi-Cal eligibility to poor or low-income families with incomes at or below 100 percent of the federal poverty level (FPL).
- ❖ **Breast and Cervical Cancer Treatment**—An increase of \$4.9 million for Breast and Cervical Cancer treatment to underinsured individuals whose income is below 200 percent of the FPL. This increases total funding for the program to \$21.7 million.



- ❖ **Tobacco Settlement Securitization Payments**—The Governor's Budget included \$62 million in 2002-03 and \$190 million for 22 years thereafter to securitize \$2.4 billion in bonds backed with tobacco settlement revenues. The May Revision proposes to securitize an additional \$2.1 billion, for a total of \$4.5 billion, to accelerate revenues to the General Fund. In addition, the May Revision proposes to delay interest and principal payments on the securitized bonds until 2003-04. This will reduce Tobacco Settlement Fund expenditures by \$62 million in the budget year.

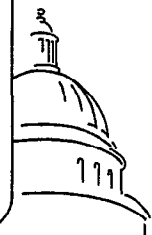
The May Revision continues to fund the following programs from the Tobacco Settlement Fund at the level proposed in the Governor's Budget:

- ❖ **State-Only Breast Cancer Treatment**—\$11.1 million to provide breast cancer treatment to uninsured or underinsured individuals whose income is below 200 percent of the FPL and not eligible for Medi-Cal.
- ❖ **Prostate Cancer Treatment**—\$20 million to provide prostate cancer treatment to uninsured or underinsured individuals whose income is below 200 percent of the FPL.

CIGARETTE AND TOBACCO PRODUCTS SURTAX FUND—PROPOSITION 99

Proposition 99 revenues for the current year and the budget year are projected to decrease by \$6 million and \$21 million, respectively. In addition to these revenue declines, prior year adjustments have been reconciled, resulting in resource decreases of \$30.1 million in the Health Education Account and \$1.4 million in the Unallocated Account. However, Access for Infants and Mothers program costs are projected to decline by \$6.8 million in the budget year, minimizing some of the effect of these resource declines.

To address these shortfalls, the May Revision proposes to eliminate the \$23 million Media Campaign augmentation originally provided in 1999-00 (at the time proposed as a one-time increase), the \$3.5 million augmentation provided in the Governor's Budget for the Breast Cancer Early Detection program, \$4.8 million provided to the County Medical Services Program, and pro-rated reductions in Cancer Control programs, County Health Services programs, Comprehensive Perinatal Outreach, and Children's Hospitals.



Managed Risk Medical Insurance Board

2001-02	<i>-\$0.4 million</i>
2002-03	<i>-\$6.5 million</i>

HEALTHY FAMILIES PROGRAM

Current Year

The May Revision includes an overall expenditure decrease of \$2.4 million (\$462,000 General Fund). This expenditure decrease is due primarily to lower than anticipated caseload growth in State-only funded children. The Healthy Families Program (HFP) is expected to serve a total of 559,000 children by June 30, 2002, which is consistent with the caseload anticipated in the Governor's Budget.

Budget Year

The May Revision projects overall expenditures to increase by \$20.7 million (\$17.3 million Tobacco Settlement Fund [TSF] and \$20 million General Fund) above the level anticipated in the Governor's Budget. The HFP is expected to serve a total of 624,000 children by June 30, 2003, which is 20,000 children less than the caseload projected in the Governor's Budget. This reflects a lower rate of caseload growth in the program.

Since the beginning of this Administration, children's caseload within the HFP has grown from 50,000 to an expected 624,000 children by the end of June 30, 2003, for an increase of 574,000 children, or 1,148 percent. Additionally, expenditures for the program have grown from a total of \$59.4 million (\$15.6 million State funds) in fiscal year 1998-99 to an expected \$672.2 million (\$250.2 million State funds) by the end of fiscal year 2002-03, or 1,032 percent.

ACCESS FOR INFANTS AND MOTHERS PROGRAM

Current Year

An average of 510 women per month are expected to enroll in the Access for Infants and Mothers program, compared to 540 as originally estimated in January. This represents a 5.6 percent decrease. Current year expenditures are expected to decrease by \$2.9 million due to a lower than anticipated enrollment of second year infants in the program.



Budget Year

Caseload is expected to decrease by 0.7 percent for mothers and infants. An average of 562 women per month are estimated to enroll in the program, down from 616 women reflected in the Governor's Budget. Expenditures are anticipated to increase by \$3.6 million (\$2.6 million TSF) due to an increase in the average monthly capitation rates.

The budget for this program has increased from \$41.7 million (\$37.5 million Perinatal Insurance Fund) in 1998-99 to \$84 million (\$71.6 million Perinatal Insurance Fund) in 2002-03 for a total increase of \$42.3 million, or 101 percent. Since 1998-99, caseload has grown from 4,460 women and 74,100 infants to an expected total of 6,738 women and 115,138 infants in 2002-03, or an increase of 55 percent in women's enrollment and 51 percent in infants' enrollment.

Department of Developmental Services

2001-02	-\$92.9 million
2002-03	-\$186.9 million

DEVELOPMENTAL CENTERS**Current Year**

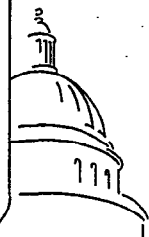
The May Revision includes a net reduction of \$2.7 million General Fund as the result of changes in the amount of federal reimbursements, comprised of the following:

- ❖ **Medi-Cal Billing Adjustment**—A \$3.1 million reduction resulting from a Medi-Cal billing rate adjustment and increased reimbursements for services delivered at the Sierra Vista facility.
- ❖ **Canyon Springs**—A \$430,000 increase as a result of delays in federal certification.

Budget Year

The May Revision includes a net reduction of \$2.7 million General Fund as the result of changes in the amount of federal reimbursements, comprised of the following:

- ❖ **Developmental Center Population Increase**—Growth of 31 clients is projected for 2002-03 and necessitates an additional \$4.2 million (\$2.6 million General Fund) and 69 level-of-care positions.
- ❖ **Medi-Cal Billing Adjustment**—A \$6 million General Fund decrease and a commensurate increase in federal funds as a result of Medi-Cal funding adjustments.



- ❖ **Canyon Springs**—A \$748,000 General Fund increase due to delays in certification of the Canyon Springs facility. The Department of Developmental Services (DDS) is actively working with the Department of Health Services and the federal Centers for Medicare and Medicaid Services to develop and implement corrective action plans to remedy the certification problems.

REGIONAL CENTERS

Current Year

The May Revision includes a net reduction of \$90.2 million General Fund as the result of changes in the amount of federal reimbursements, comprised of the following:

- ❖ **Increased Federal Reimbursements**—A \$48 million General Fund decrease and a commensurate increase in federal reimbursements as a result of the Administration's proposal to increase the number of Regional Center consumers under the Home and Community-Based Services Waiver (Waiver). This issue was addressed in an April Finance Letter.
- ❖ **Enhancing Federal Financial Participation**—An \$8.4 million General Fund increase for Regional Center operations to provide the additional personnel (\$4 million) necessary to add and maintain consumers under the Waiver and to bring Regional Center information systems into conformity with federal reporting requirements (\$4.4 million). This issue was addressed in an April Finance Letter.
- ❖ **Title XX Fund Shift**—A \$50.6 million General Fund decrease and a commensurate increase in federal reimbursements to reflect a fund shift for the Regional Centers. Under this proposal, Title IV-E funds are being used for Child Welfare Services Emergency Assistance Case Management activities in order to free up Temporary Assistance to Needy Families (TANF) dollars. These TANF dollars can then be transferred to Title XX and used in lieu of General Fund in the DDS.

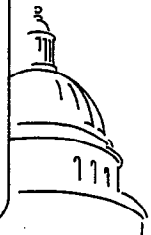
Budget Year

The Regional Center population is not projected to increase above the 182,230 clients estimated in the Governor's Budget. The implementation of state-wide standards for purchase of services combined with extension of Regional Center intake and assessment periods is expected to lessen the growth in demand for Regional Center services.



The May Revision includes a net reduction of \$184.2 million General Fund primarily as the result of changes in the amount of federal reimbursements, comprised of the following:

- ❖ **Increased Federal Reimbursements**—A \$106.7 million General Fund decrease and a commensurate increase in federal reimbursements is included as a result of the Administration's proposal to increase the number of Regional Center consumers under the Waiver. This issue was addressed in an April Finance Letter.
- ❖ **Enhancing Federal Financial Participation**—An increase of \$15.2 million General Fund for Regional Center operations is included in the revised budget to provide additional personnel required to add and maintain Waiver clients. This issue was addressed in an April Finance Letter.
- ❖ **Non-Community Placement Plan Adjustments**—Costs for Regional Center purchase of services will decrease by a total of \$7.4 million General Fund. These savings are the result of suspending non-community placement plan start-up activities and a more accurate estimate of community placement plan costs.
- ❖ **Extending Intake Assessment Timeframes**—Regional Center operations will decrease by a net \$3 million General Fund due to an extension of the time allowed for intake and assessment (-\$4.4 million), and a more accurate estimate of community placement plan costs (\$1.4 million).
- ❖ **South Central Los Angeles Regional Center Federal Certification**—A decrease of \$11.4 million General Fund and a corresponding increase in federal reimbursements is reflected as a result of anticipated federal certification.
- ❖ **Title XX Fund Shift**—A \$70.9 million General Fund decrease and a commensurate increase in federal reimbursements reflects a fund shift for Regional Centers. Title IV-E funds are being used for Child Welfare Services Emergency Assistance Case Management activities in order to free up TANF dollars. These TANF dollars can then be transferred to Title XX and used in lieu of General Fund in the DDS.



Department of Rehabilitation

2001-02	- \$6.2 million
2002-03	- \$4.4 million

Current Year

The May Revision reflects a net General Fund savings of \$6.2 million. Significant adjustments include savings of \$286,000 in the Vocational Rehabilitation Program (VRP) resulting from a decrease in the number of job coach hours provided; and a savings of \$5.6 million in the Habilitation Services Program (HSP) attributable to a decline in both attendance days and job coach hours. The HSP savings will reduce the need for the deficiency funding reflected in the Governor's Budget from \$12.8 million to \$7.2 million.

Budget Year

The May Revision reflects a net General Fund decrease of \$4.4 million. The Governor's Budget assumed savings of \$5.9 million General Fund would be achieved through restructuring the HSP. After careful review of potential restructuring alternatives, it has been determined that only \$2.2 million General Fund savings would be reasonably achievable. Therefore, the May Revision includes a restoration of \$3.7 million General Fund. However, the restoration is offset by a decrease in HSP expenditures of \$8.1 million General Fund based on an adjustment in the projection of the number of days clients would attend the Work Activity Program and a decline in the number of job coach hours that would be utilized. Also, costs in the VRP are projected to increase by \$124,000 General Fund due to a 1.7 percent growth in caseload.

Department of Mental Health

2001-02	- \$4.2 million
2002-03	- \$7.4 million

LONG-TERM CARE/STATE HOSPITALS

Current Year

The May Revision includes \$4.2 million in General Fund reductions in long-term care, primarily as the result of a new methodology for estimating state hospital population. The revised state hospital population estimate is based on additional data on the number of patients in the first nine months of 2001-02 that were not available in the fall. The General Fund reductions are comprised of the following:

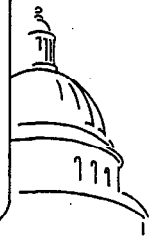


- ❖ **State Hospital Population**—As a result of a state hospital caseload reduction of 54 judicially committed/Penal Code patients below the Governor's Budget, a current year savings of \$2.9 million General Fund is expected. Caseload is expected to decline from 4,565 patients to 4,511 patients. This decline in caseload will result in the elimination of 33.5 positions (31.8 personnel years).
- ❖ **Sexually Violent Predator Evaluations**—A General Fund augmentation of \$411,000 is proposed to reflect additional evaluations of Sexually Violent Predators. This increase will fund additional evaluations, to be performed by private contractors, as well as additional costs for evaluator testimony.
- ❖ **State Compensation Insurance Fund**—The Governor's Budget included funding for an advance deposit for anticipated worker's compensation claims. However, these advance deposits are no longer required, and the May Revision includes a reduction of \$2.1 million (\$1.6 million General Fund) to reflect this change.

Budget Year

Funding for long-term care and state hospitals is anticipated to decrease by \$17.5 million General Fund, as a result of an additional nine months of data with which to estimate the number of patients and a new methodology to estimate caseload. Significant adjustments are as follows:

- ❖ **State Hospital Population**—A reduction of 171.8 positions (163.1 personnel years) and a savings of \$12.3 million (\$14.8 million General Fund savings and an increase of \$2.5 million realignment reimbursements) is reflected for a net reduction of 87 judicially committed/Penal Code patients from the Governor's Budget, from 4,687 patients to 4,600 patients.
- ❖ **Recruitment and Retention Pay Differentials for the Salinas Valley Psychiatric Program**—State hospital reimbursements are increased by \$554,000 to reflect newly approved recruitment and retention pay differentials for various level-of-care professional and nursing staff for the Salinas Valley Psychiatric Program at Salinas Valley State Prison.
- ❖ **State Hospital Mental Health Treatment Program for the California Youth Authority**—State hospital reimbursements are increased by \$3.1 million to reflect the establishment and operation of a 20-bed intermediate care inpatient mental health program at the Southern Youth Reception Center and Clinic for the California Youth Authority beginning October 2002. This adjustment results in an increase of 44 positions (33 personnel years).



- ❖ **Delay in the Salinas Valley Psychiatric Program**—The May Revision includes a reduction of \$1.5 million in reimbursements to reflect a delay in activation of the Salinas Valley Psychiatric Program until September 2002.
- ❖ **Non-Level-of-Care Staff at Atascadero and Patton State Hospitals**—The Governor's Budget included an increase for non-level-of-care staff at Atascadero and Patton State Hospitals. However, the May Revision population estimate has been reduced in 2002-03 and the new positions are no longer required. Accordingly, reducing the non-level-of-care staff at Atascadero and Patton State Hospitals will result in savings of \$3.1 million and a decrease of 39.5 positions (33.7 personnel years).

GENERAL FUND REDUCTIONS

In light of the State's current fiscal constraints, the May Revision proposes the reduction or elimination of various program proposals included in the Governor's Budget. However, even after these changes, funding for community mental health programs is \$42.9 million General Fund, or 13.3 percent, above the funding level provided in 1999-00. Specifically, the Administration proposes the following reductions:

- ❖ **Adult and Children's Systems of Care**—\$42.6 million to eliminate the programs.
- ❖ **Integrated Services for Homeless Adults Program**—\$10 million for the Integrated Services for Homeless Adults program, leaving \$55.6 million for this program.
- ❖ **Managed Care Rates**—\$5.6 million for Managed Care to rescind the Medi-Cal rate increase provided in 2000-01 for psychologists and psychiatrists.
- ❖ **Early and Periodic Screening, Diagnosis, and Treatment (EPSDT) and Therapeutic Behavioral Services (TBS)**—\$35 million in the EPSDT program to reflect a new requirement for counties to fund a 10 percent share-of-cost for growth in the program.
- ❖ **Program Reversions**—\$3.1 million in reversions to capture current year savings, including: \$867,000 from the Integrated Services to the Homeless Program, \$750,000 from the Institutions for Mental Disease Transition Pilot, \$900,000 from the Supportive Housing Program, and \$625,000 from the Dual Diagnosis projects.



Department of Alcohol and Drug Programs

2001-02	-\$2.8 million
2002-03	\$1.1 million

Current Year

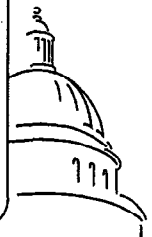
General Fund costs for the Department of Alcohol and Drug Programs will decrease by \$2.8 million, reflecting a decrease of 14,026 in estimated Drug Medi-Cal caseload and higher rates paid for services. The rates are determined by taking the average rates from settled cost reports. The rates fluctuate each year.

- ❖ **Regular Drug Medi-Cal**—Caseload is expected to be 10.8 percent lower than projected in the Governor's Budget. The decrease is driven primarily by a 15.8 percent lower than expected utilization of Outpatient Drug Free counseling services. Costs will decrease by \$2.9 million General Fund, or 6.3 percent, from the Governor's Budget.
- ❖ **Perinatal Drug Medi-Cal**—Caseload is estimated to decrease by 0.3 percent, or 21 clients, from the 6,698 included in the Governor's Budget. Costs, however, are expected to increase by \$38,000 General Fund, or 1.5 percent.

Budget Year

General Fund costs are estimated to increase by \$1.8 million, reflecting an increase in the estimated Perinatal Drug Medi-Cal caseload and higher average rates paid for services.

- ❖ **Regular Drug Medi-Cal**—The estimated caseload for Regular Drug Medi-Cal will decrease by 1,955, or 1.5 percent, below the Governor's Budget. However, costs are expected to increase \$1.4 million General Fund, or 3.1 percent.
- ❖ **Perinatal Drug Medi-Cal**—Caseload is projected to increase 30.8 percent, or approximately 2,108 clients, above the Governor's Budget. Costs are expected to increase \$385,000 General Fund, only 14.2 percent, due to a decrease in units-of-service per client and lower average rates for some services, primarily in the Perinatal Residential program.



GENERAL FUND REDUCTIONS

Due to the change in the State's fiscal outlook, the May Revision proposes a reduction of \$1.5 million (\$750,000 General Fund) originally included in the Governor's Budget for compliance with the federal Health Insurance Portability and Accountability Act. The reduction in the May Revision will not adversely affect critical compliance activities.

Department of Social Services

2001-02	\$15.7 million
2002-03	-\$169.8 million

CALWORKS

The 2001-02 average monthly CalWORKs caseload of 507,000 represents a 2.4 percent decrease from 2000-01. For 2002-03, the caseload is expected to be 524,000, or 9,000 below the Governor's Budget projection, a 3.3 percent increase from the 2001-02 projection.

The May Revision continues to meet the federally-required combined state and county Temporary Assistance for Needy Families (TANF) maintenance-of-effort (MOE). For 2001-02 and 2002-03, the MOE will be met at the \$2.7 billion level. For 2001-02, total CalWORKs-related expenditures are estimated to be \$6.8 billion including the transfer to the Department of Education (CDE) for child care and county expenditures. For 2002-03, total CalWORKs related expenditures are anticipated to be \$7.4 billion.

Major General Fund and TANF Block Grant changes proposed for 2001-02 include:

- ❖ **Assistance Payments**—A \$19.6 million decrease due to lower than projected caseload, partially offset by an increase in the average grant cost per person.
- ❖ **Child Care**—A \$14.9 million increase for CalWORKs child care due to an increase in Stage One child care caseload. Funding has already been transferred to Stage One from the Child Care Reserve to address this caseload increase.



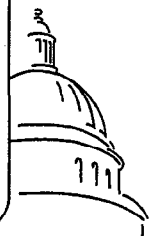
Major changes proposed for 2002-03 include:

- ❖ **Community Colleges**—A restoration of \$20 million for the California Community Colleges (CCC) CalWORKs program. This Proposition 98 funding is countable toward the federally-required TANF MOE. The Administration expects the CCC to provide a 1-to-1 local match from its increased discretionary funds to continue the provision of services under this program.
- ❖ **Employment Services**—A \$120 million one-time augmentation to CalWORKs employment services. Funding for this purpose will be redirected from county performance incentives.
- ❖ **Assistance Payments**—A \$23.3 million increase due to an increase in the average grant cost per person and the implementation of prospective budgeting, partially offset by a reduction in the cost of implementing new federal regulations affecting the vehicle resource limit rules for CalWORKs eligibility.
- ❖ **TANF Block Grant Reserve**—A \$50 million increase in the TANF Block Grant reserve for contingencies, making the total reserve \$90 million. This funding will be available for unanticipated needs in any program for which TANF funds are appropriated, including CalWORKs benefits, employment services, county administration, and child care. The funding to increase this reserve has been redirected from the Child Care Reserve.

CALWORKS CHILD CARE

The May Revision reflects a decrease of \$16.8 million for CalWORKs Stage One child care administered by the Department of Social Services (DSS) in 2002-03. This decrease is due primarily to: (1) a decrease in Stage One child care caseload, (2) a decrease in county administration costs for child care, and (3) savings resulting from not making child care payments in Los Angeles County beyond 30 days in arrears. These savings are partially offset by a loss of projected savings resulting from the child care reform proposed in the Governor's Budget.

In addition, the May Revision reflects an increase of \$46.9 million for CalWORKs Stage Two child care administered by the CDE. This increase is due to revised child care caseload data and the loss of savings from the child care reform proposal. The Child Care Reserve is decreased by \$56.3 million to reflect a decrease in child care costs and a \$50 million redirection to the TANF Block Grant reserve for contingencies to assure that sufficient funds are available if unanticipated needs arise after enactment of the budget.



The May Revision also reflects the addition of \$230,000 General Fund and 3.0 positions for increased workload to provide estimates and synthesize data received from a variety of organizations that is necessary for budgetary and policy decisions associated with the ongoing discussions relating to restructuring the State's child care system.

FOOD ASSISTANCE PROGRAMS

CALIFORNIA FOOD ASSISTANCE PROGRAM

The May Revision includes an increase of \$92.2 million General Fund for the California Food Assistance Program (CFAP), to reflect the delayed restoration of federal Food Stamp eligibility for a limited number of recipients in the budget year. However, the net General Fund impact of the delay will be substantially less than this amount due to the fact that a share of these costs are countable towards the State's CalWORKs maintenance-of-effort requirement.

The CFAP provides food stamp benefits to documented persons who are not eligible for federal Food Stamps solely because of their immigration status. The Governor's Budget assumed that all program recipients would become eligible for Food Stamps effective July 2002. However, the current federal budget bill for Food Stamps will only restore federal eligibility for a small number of recipients in October 2002 and to approximately 75 percent of recipients in April 2003.

FOOD STAMP ERROR RATE

The May Revision includes \$11.6 million General Fund for the State's portion of the Federal Fiscal Year (FFY) 2001 Food Stamp error rate penalty. The State's FFY 2001 error rate of 17.4 percent exceeded the national average by 8.7 percentage points. The remaining \$104.2 million of the federal sanction will be assessed on those counties whose error rates contributed to the federal sanction. The DSS intends to negotiate with the U.S. Department of Agriculture to reduce the penalty.

QUARTERLY REPORTING

The Administration proposes to address the State's Food Stamp error rate by shifting reporting requirements for Food Stamp and CalWORKs beneficiaries from a monthly system to a quarterly system. Forty-two other states no longer require monthly reporting for Food Stamp recipients. A quarterly reporting system will reduce county administrative paperwork and costs, and will decrease the likelihood



of administrative errors that contribute to the Food Stamp error rate. The May Revision includes \$557,000 General Fund to implement quarterly reporting in the budget year. The DSS anticipates that quarterly reporting will result in county administration savings of \$16.9 million annually, beginning in 2003-04.

SUPPLEMENTAL SECURITY INCOME/STATE SUPPLEMENTARY PAYMENT PROGRAM

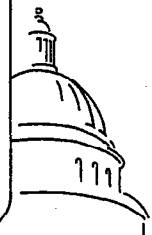
Total General Fund expenditures for the Supplemental Security Income/State Supplementary Payment (SSI/SSP) Program are \$2.8 billion in 2001-02 and \$3 billion in 2002-03, which represent decreases from the Governor's Budget of \$14.7 million in the current year and \$67.4 million in the budget year. Caseload for the SSI/SSP Program is projected at 1,103,000 recipients in 2001-02, and 1,126,400 recipients in 2002-03. Significant adjustments include:

- ❖ Reductions of \$8.2 million in 2001-02 and \$2.1 million in 2002-03, due to lower than anticipated caseload growth and a lower average grant in the SSI/SSP Program. The year-to-year caseload growth is projected at approximately 2.1 percent.
- ❖ Reductions of \$6.4 million in the current year and \$11.2 million in the budget year in the Cash Assistance Program for Immigrants (CAPI), due to lower than anticipated caseload growth. On a year-to-year basis, the CAPI caseload is projected to grow at approximately 4 percent.
- ❖ A reduction of \$54.3 million, discussed below in the "General Fund Reductions" section.

IN-HOME SUPPORTIVE SERVICES

General Fund expenditures for the In-Home Supportive Services (IHSS) program are below the levels reflected in January by \$15.6 million in the current year and \$28.6 million in the budget year. Caseload is projected to be 274,000 recipients in 2001-02 and 296,800 in 2002-03. Significant adjustments include:

- ❖ Increases of \$18.4 million and \$34.9 million in the current and budget years, respectively, due primarily to higher caseload in the Personal Care Services Program and increased average service hours per IHSS case.
- ❖ Reductions of \$25.3 million and \$48.8 million in the current and budget years, respectively, due to delays in counties providing wage and/or benefit increases to Public Authority individual providers.



- ❖ Reductions of \$6.7 million in the current year, and \$7.1 million in the budget year, to reflect the currently anticipated schedule for contract-mode counties moving to their respective Maximum Allowable Contract Rates.
- ❖ A reduction of \$16.7 million in county administration, discussed in the "General Fund Reductions" section.

CHILD WELFARE SERVICES

General Fund expenditures will increase by \$27.2 million in the current year, and \$26.5 million in the budget year. The May Revision reflects the following significant increases, in addition to various reductions which are detailed separately below:

- ❖ An increase of \$27.1 million in the current year and \$38.4 million in the budget year to reflect a shift of the cost of Child Welfare Services (CWS) Emergency Assistance Case Management activities from TANF to Title IV-E, which requires a General Fund match. The TANF funds will be used to offset costs in the Title XX program, which will result in a net General Fund savings in the budget of the Department of Developmental Services.
- ❖ An increase of \$11 million in the budget year to reflect increased Child Welfare Services/Case Management System (CWS/CMS) utilization charges and caseload adjustments.

FOSTER CARE

The May Revision includes an increase in General Fund costs of \$2.2 million in the current year, due to growth in Foster Group Homes and the Seriously Emotionally Disturbed Program caseload. In addition, the May Revision reflects a decrease of \$3.7 million General Fund in the budget year to reflect revised participation rates and delayed county implementation of the Supportive Transitional Emancipation Program.

AUTOMATION PROJECTS

The Statewide Automated Welfare System (SAWS) and the Statewide Fingerprint Imaging System (SFIS) assist in the administration of the CalWORKs, Food Stamps, California Food Assistance, and Foster Care programs. These automation systems further the Administration's goal of providing quality services as efficiently as possible while preventing fraud and reducing long-term costs.



SAWS Los Angeles Eligibility, Automated Determination, Evaluation, and Reporting (LEADER) Consortium System—The May Revision funds critical LEADER programming using \$5.4 million in administrative savings achieved due to LEADER implementation. With this funding, the LEADER system will be updated to incorporate the Medi-Cal Section 1931(b) program, the Medi-Cal mail-in application, expanded languages for client notification letters, and other program changes.

GENERAL FUND REDUCTIONS

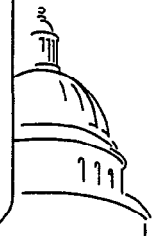
Due to the lower level of General Fund resources available, the May Revision proposes the following reductions:

CalWORKs

- ❖ **Reinstatement of Senior Parent Deeming**—\$12.1 million as a result of reinstating the deeming requirements for the parents of minor parents (referred to as “senior parents”) living at home. Under this proposal, the senior parent’s income would be “deemed” to the grandchild, and therefore counted for the purpose of determining eligibility of the grandchild for cash assistance. Senior parents’ income was formerly deemed under the Aid to Families with Dependent Children program, which preceded the CalWORKs program.
- ❖ **County Administration**—\$71.9 million in CalWORKs county administration. Over the course of this Administration, the level of total funding for CalWORKs administration has increased by \$118.7 million while CalWORKs caseload has declined by more than 52,000 cases during the same time period. This reduction is a smaller proportion of CalWORKs county administration than the 20 percent reduced from county administration funding for other programs. This is to maintain some flexibility for counties to redirect funding within their County Program Grant for critical needs as increased numbers of recipients reach their five-year time limit for cash assistance.

County Administration

The 2002-03 Governor’s Budget included a total of \$76.5 million General Fund for county administration of the Foster Care program, \$635.5 million General Fund for county administration of the Food Stamps program, and \$176.4 million General Fund for county administration of the In-Home Supportive Services (IHSS) program. These totals represent an increase of \$176.9 million for county administration in these programs since the Governor took office in 1999.



In light of the State's fiscal constraints, the May Revision reflects a \$61 million General Fund reduction in county administration funding to eliminate the cost-of-doing business provided in 2000-01 for the Foster Care and Food Stamps programs (\$12 million), and a 20 percent reduction to county administration funding in the Foster Care, Food Stamps, and IHSS programs (\$49 million).

Adult Programs

- ❖ **Suspend Pass-Through of Federal Cost-of-Living Adjustment**—\$54.3 million to suspend the pass-through of the January 1, 2003, federal cost-of-living adjustment (COLA) for the SSI/SSP Program. The suspension of the pass-through of the federal COLA is consistent with actions in 1991 and 1994, when General Fund revenues also declined significantly. The May Revision retains \$3 billion General Fund for this program in 2002-03, which is \$175 million General Fund above the 2001-02 revised funding level. Compared to the 1999 Budget Act, funding for this program has increased \$509 million, or nearly 21 percent. The monthly SSI/SSP grant levels would not be lowered due to this reduction and would remain at \$750 for individuals and \$1,332 for couples.
- ❖ **Special Circumstances Program**—\$4.5 million to eliminate the Special Circumstances Program. Due to previous reductions in General Fund revenues, this program was suspended from 1992 to 1998.
- ❖ **Enhanced Adult Protective Services Program**—\$5.6 million in the Enhanced Adult Protective Services (APS) Program. This program was augmented by \$30.2 million General Fund during this Administration. The May Revision still retains \$60.7 million General Fund for the APS Program in 2002-03, including \$30.2 million for the Enhanced APS Program.

Children Services

- ❖ **CWS Augmentation**—\$17.2 million in the CWS augmentation. The Budget retains an augmentation of \$93.7 million (\$57.1 million General Fund) to provide emergency child welfare services, and continues the base funding adjustment of \$135.2 million (\$62.4 million General Fund) for county social workers.
- ❖ **Discretionary Cost-of-Doing Business Increases for Basic CWS**—\$10.8 million to eliminate the discretionary cost-of-doing business increases proposed in January for the CWS basic costs.
- ❖ **Discretionary Cost-of-Doing Business Increases for Adoptions Program**—\$9.1 million to eliminate the discretionary cost-of-doing business increases granted for the Adoptions Program since the 2000 Budget Act.



The elimination of these cost-of-doing business increases is consistent with the suspension of COLAs for other social services programs, as most of those programs did not receive comparable increases during this period.

Automation Projects

- ❖ **SAWS Consortium IV**—\$5 million for SAWS Consortium IV project development. It is the intent of the Administration that the Consortium will pursue the renegotiation of the project vendor contract to reduce vendor costs.
- ❖ **Interim SAWS Consortium**—\$554,000 for Interim SAWS (ISAWS) maintenance and operations. Installation of replacement mainframes in December 2001 has reduced maintenance and operations costs for the ISAWS.
- ❖ **SAWS Statewide Project Management**—\$315,000 for SAWS oversight consultant activities. The May Revision maintains \$500,000 for consultants to identify and mitigate technical risks to the SAWS projects.
- ❖ **Statewide Fingerprint Imaging System**—\$570,000 for SFIS consultant activities. Independent Verification and Validation and other routine consultant activities will be eliminated or deferred with minimal risk to project maintenance and operations.

Department of Child Support Services

2001-02	-\$25.2 million
2002-03	\$88 million

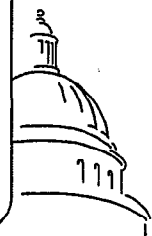
Current Year

The May Revision includes a decrease of \$25.2 million General Fund compared to the Governor's Budget. This results primarily from savings of \$24.6 million due to delays in hiring staff and other program implementation issues associated with local child support agencies.

Budget Year

The May Revision includes an increase of \$88 million General Fund, predominately in local assistance funding (\$87.4 million). The May Revision includes the following major adjustments:

- ❖ \$89.7 million General Fund increase to reflect the cost of the alternate federal penalty levied on the State because of the delay in implementing a single, statewide-automated child support collection system. The Governor's Budget anticipated that federal legislation would be enacted to provide relief from the



estimated \$181.3 million in federal penalties that would have accrued in 2002-03. It is now anticipated that legislation will be enacted to establish 1997 as the base year upon which penalties are calculated. This would reduce the federal penalty from \$181.3 million to \$89.7 million in 2002-03. Approximately one-half of this increase in General Fund costs will be offset by charging counties a share of the costs of the penalty, which is being reflected as General Fund revenue.

- ❖ A redirection of \$1.7 million (\$568,000 General Fund) to establish six contract positions to act as Pre-Interim Statewide Systems Management Consortia Project leaders. These positions will act as the State's on-site representatives to ensure that DCSS directives are carried out on time and within budget, and to ensure that the Department's strategic vision regarding automation systems is effectively implemented at the local level.
- ❖ A net decrease of \$2.3 million General Fund to reflect various adjustments for county automated system enhancements, postage, and the Foster Parent Training Fund.
- ❖ \$1.1 million (\$383,000 General Fund) to implement the California Insurance Intercept Project (CIIP). This project will enable the DCSS to increase collections of child support debts by enabling the DCSS to match child support obligors who file and receive an award in personal injury cases. Additional collections as the result of insurance intercepts are projected at \$3.4 million.
- ❖ \$550,000 (\$187,000 General Fund) to provide additional resources to conduct child support State hearings as the result of increased caseload. Pursuant to Chapter 803, Statutes of 1999, the DCSS provides both custodial and non-custodial parents the opportunity to have specific types of child support complaints defined in statute come before a State hearing, provided the parties first exhaust the local child support agency complaint resolution process. Additional resources are required to allow the DCSS and the Department of Social Services Office of Administrative Hearings to address applicants' concerns within the timeframe defined in statute.

Child support collections are now projected to be \$2.4 billion in 2002-03. While this is a decrease of \$3.9 million, or 0.2 percent, from the amount projected in the Governor's Budget, the increase in 2002-03 is \$177.7 million, or 8 percent, over current year collections. The General Fund share of collections is projected to increase by \$4.9 million due the efforts of additional collections staff hired by the Franchise Tax Board, and anticipated benefits from collections due to the proposed new CIIP.



Office of Statewide Health Planning and Development

2001-02	—
2002-03	-\$0.5 million

Budget Year

As a result of the State's current fiscal constraints, the May Revision proposes a reduction of \$500,000 General Fund for the Song-Brown Family Physician Training Program (Song-Brown). The May Revision includes a total of \$4.3 million (\$3.9 million General Fund) for this program that provides financial support to educational institutions to expand the training slots for primary care physicians, nurse practitioners, and physician assistants. This reduction will result in the decrease of nine primary care physician-training slots.

However, consistent with the Administration's commitment to increase the number of nurses in California, this reduction will have no impact on the number of training slots available for nurse professionals. The revised Governor's Budget provides a special fund augmentation of \$1.1 million for scholarship and loan repayment funds to an additional 90 nursing students in the Health Professions Education and Registered Nurse Education programs.

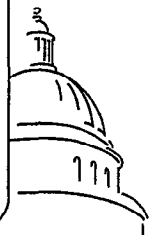
Emergency Medical Services Authority

2001-02	—
2002-03	-\$0.8 million

The May Revision includes increased federal spending, as well as General Fund reductions, which are described in detail below.

HOSPITAL BIOTERRORISM PREPAREDNESS PROGRAM

The May Revision includes an increase of \$9.1 million to implement a federal grant for California hospitals and other health care organizations to address bioterrorism preparedness. In the wake of the terrorist attacks of September 11th, and the subsequent anthrax threat, hospitals and emergency medical services providers have expressed concern about California's preparedness for a bioterrorist event. This federal grant funding provides an invaluable opportunity for hospitals and health care providers to focus on bioterrorism preparedness. Of the grant funds, \$8.5 million will be distributed directly to local hospitals and emergency medical organizations



to develop an effective, coordinated medical response to a biological attack, and the balance will be used for a statewide bioterrorism needs assessment and program administration.

GENERAL FUND REDUCTIONS

Due to the current fiscal condition of the State, the May Revision proposes the reduction or elimination of various program proposals included in the Governor's Budget. However, total funding for the Emergency Medical Services Authority (EMSA) has increased by \$4.1 million, or 43 percent since 1999. Specifically, the May Revision reflects the following reductions:

- ❖ **Poison Control System**—\$400,000 for the California Poison Control System, leaving \$7.6 million (\$3.6 million General Fund) for support of the system.
- ❖ **Administrative and Local Assistance Reduction**—\$474,000 for State operations and local assistance.

These reductions represent a 10 percent decrease in the General Fund provided in the Governor's Budget for the EMSA.

Employment Development Department

2001-02	-\$1.5 million
2002-03	-\$1.3 million

The May Revision provides for several changes to Employment Development Department (EDD) programs that are primarily federally funded. Highlights of significant changes are described below.

UNEMPLOYMENT AND DISABILITY INSURANCE

Current Year

The May Revision includes increased benefits of \$2.4 billion for the Unemployment Insurance (UI) and Disability Insurance (DI) programs resulting from the economic downturn following the September 11th terrorist attacks. In addition, the Administration has recently enacted the following two bills increasing UI benefit disbursements to unemployed Californians:

- ❖ Chapter 409, Statutes of 2001 (SB 40) provides UI benefit increases to claimants who filed after January 1, 2002. Weekly UI benefit increases will be phased-in annually from 2002 through 2005.



- ❖ Chapter 4, Statutes of 2002, Third Extraordinary Session (SB 2XXX) allows these benefit increases to be available retroactively to individuals who became unemployed after September 11, 2001.

Budget Year

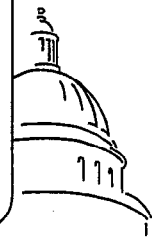
The May Revision includes a \$1.2 billion increase for UI and a \$295.3 million increase for DI benefits in 2002-03. This increase is based primarily on a 26 percent increase in UI benefit payments from the last EDD estimate in October 2001, and is associated with the economic downturn.

REED ACT ALLOCATION

On March 9, 2002, the President signed an economic stimulus bill, which includes a one-time \$8 billion Reed Act distribution to states. California's share totals \$936.9 million. Reed Act funds may be used for UI benefits, or for administration of UI, Job Service, or Veteran Employment programs within the EDD. The May Revision proposes to use Reed Act funding for the administration of the employment program, resulting in General Fund savings of \$1.5 million in the current year and \$1.2 million in the budget year. In addition, increased special fund transfers to the General Fund of \$4.2 million in current year and \$33.2 million in budget year will be achieved by the use of Reed Act funds for administration of UI and employment services programs funded with special funds. The May Revision assumes that the remaining Reed Act funds will remain in the UI Trust Fund.

Labor and Workforce Development Agency

The May Revision proposes a redirection of \$32,000 General Fund and \$1.4 million in additional special and federal fund reimbursements from the EDD to support the operations of the California Labor and Workforce Development Agency, which is proposed pursuant to Governor's Reorganization Plan No. 1 of 2002. The Agency will be comprised of the Department of Industrial Relations, the EDD, the Agricultural Labor Relations Board, and the California Workforce Investment Board.



Public Safety

Department of Justice

2001-02	—
2002-03	\$2.7 million

AUGMENTATIONS

The May Revision proposes the following augmentations for the Department of Justice (DOJ):

California Anti-Terrorism Information Center (CATIC)—An increase of \$13.4 million General Fund and 78 positions to continue and expand funding for the CATIC program, which provides investigative assistance to local and federal law enforcement, intelligence gathering, and a statewide informational database to analyze terrorist activities within the State. This expansion would provide additional field and intelligence agents, along with a headquarters unit, to enhance the capabilities of the program. The Administration intends to reimburse the General Fund for this cost from future allocations of federal security-related funds.

Richmond DNA Laboratory—\$1.6 million General Fund for additional lease and tenant improvement costs for the Richmond DNA Laboratory.

GENERAL FUND REDUCTIONS

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes reductions totaling \$12.3 million, as follows:

California Gang, Crime and Violence Prevention Partnership Program—\$1.5 million for the California Gang, Crime and Violence Prevention Partnership Program.

Spousal Abuser Prosecution Program—\$800,000 for the Spousal Abuser Prosecution Program.

Department of Justice Programs—\$10 million for allocation by the Department to its various divisions and programs.



Department of Corrections

2001-02	\$18.1 million
2002-03	\$185.9 million

INMATE/PAROLEE POPULATION/CASELOAD CHANGES

Current Year

Based upon the Department of Corrections' (CDC) spring estimates, the May Revision reflects an estimated June 30, 2002, population of 156,846 inmates. This is 437 more inmates than that projected in the Governor's Budget, and results in a cost of approximately \$9.8 million General Fund and \$219,000 Inmate Welfare Fund. The revised population estimate represents a decrease of 4,651 inmates (2.9 percent) from the June 30, 2001, population level.

The projected June 30, 2002, parolee population is 120,830. This is an increase of 307 parolees from the number projected in the Governor's Budget. The revised population estimate and related program changes results in a net increase of \$7.1 million. The revised parolee population estimate represents an increase of 1,194 parolees (1 percent) over the June 30, 2001, level.

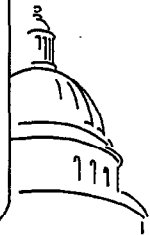
The net effect of the changes listed above is a cost to the General Fund of \$16.9 million and a cost to the Inmate Welfare Fund of \$219,000.

Budget Year

Based upon the CDC's spring estimates, the May Revision reflects a June 30, 2003, population of 154,672 inmates, which is 1,049 fewer inmates than projected in the Governor's Budget. This decrease and related program changes result in a reduction of approximately \$3.5 million General Fund and an increase of \$19,000 Inmate Welfare Fund. The revised inmate population estimate reflects a decrease of 2,174 inmates (1.4 percent) from the revised June 30, 2002, population estimate.

The spring population estimate for parolees as of June 30, 2003, is 119,865, which is 3,054 more parolees than projected in the Governor's Budget. This increase and related program changes result in a net increase of approximately \$5.5 million. The revised parolee population level projected for the budget year represents a decrease of 965 parolees (0.8 percent) from the revised population estimate for June 30, 2002.

The net effect of the augmentations listed above is a cost to the General Fund of \$2 million and a cost to the Inmate Welfare Fund of \$19,000.



AUGMENTATIONS

The May Revision proposes the following augmentations for the CDC:

Structural Workers' Compensation Shortfall—\$42.1 million one-time increase to fund the increased cost of workers' compensation.

Utilities—\$18 million to fund the Department's increased utilities costs.

Overtime—\$9.8 million to fund overtime for specified posted custody positions on a limited-term basis.

Contract Medical—\$115.5 million to address increased costs for contracted medical services to provide medically necessary health care services to inmates.

Board of Prison Terms Injunction—\$1.1 million to fund increased CDC workload associated with the permanent injunction against the Board of Prison Terms pursuant to the *Armstrong v. Davis* lawsuit.

Bargaining Unit 6 Contract Operational Costs—\$2.3 million in 2001-02 and \$4.7 million in 2002-03 to cover operational costs associated with the provisions of the Bargaining Unit 6 Memorandum of Understanding authorized by Chapter 1, Statutes of 2002.

Postage Increase—\$528,000 to cover the increased costs of postage related to the recent rise in the postal rates announced by the U.S. Postal Service.

Inmate Medical Services (Plata Lawsuit)—\$21.9 million to begin implementation of system-wide improvements in the provision of inmate health care services consistent with the requirements of the stipulated agreement in the *Plata* class action lawsuit, as well as a pilot Hepatitis C treatment program at Pelican Bay State Prison, as required by the court order in the *Madrid* lawsuit.

Mental Health Services Delivery System—Coleman Lawsuit Compliance—\$8.1 million to provide resources for additional mental health crisis beds, Psychiatric Services Unit beds, and increased nursing care of inmates in mental health crisis beds.

Correctional Treatment Center Licensure—\$1.2 million to obtain licensure for five Correctional Treatment Centers (CTC) in 2002-03 and two additional CTCs in 2003-04.



Recruitment and Retention Bonuses—Department of Mental Health and CDC—\$1.6 million to reimburse the Department of Mental Health for recruitment and retention bonuses for various classifications at Salinas Valley State Prison, and for recruitment and retention bonuses for CDC at Salinas Valley State Prison and the neighboring Correctional Training Facility for similar classifications.

Health Insurance Portability and Accountability Act (HIPAA)—\$898,000, on a one-year limited-term basis, to assess the potential impact of HIPAA on the Department and determine solutions and regulatory considerations for implementation.

Inmate Welfare Fund Budget Increase—\$542,000 Inmate Welfare Fund in 2001-02 and 2002-03 for the costs of prison canteens, as well as other inmate related projects and activities.

Local Assistance Augmentations—\$9.2 million on a one-time basis to fund increased costs for reimbursements to local jurisdictions for detaining State prisoners and parolees and parole revocation proceedings.

GENERAL FUND REDUCTIONS

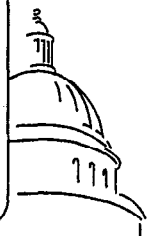
Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes reductions totaling \$50.7 million for the CDC, including:

Delaying Substance Abuse Treatment Beds and Aftercare at the California Rehabilitation Center—\$2.5 million in one-time savings associated with a delay in implementation of in-prison and aftercare services for a 200-bed substance abuse treatment expansion, and aftercare savings related to delayed implementation of a 300-bed expansion.

Reducing Civil Addict Program—\$10 million from placing a 954 inmate cap on the number of Civil Addict commitments in the CDC.

Increasing Work Credits for Fire Camp Inmates—\$16.7 million associated with increasing the sentence credits for inmates assigned to fire camps from one day of credit for every day assigned to a camp to two days of credit for every day assigned to a camp.

Eliminating Monthly Range Training Program—\$3.6 million resulting from the elimination of the Monthly Range Training program, due to implementation problems.



Paroles Reduction—\$16 million reduction in the Community Correctional Program (Paroles) within the CDC. This reduction will be implemented by reducing non-critical parolee services, which will not affect parolee oversight or public safety.

Additional Security at Patton State Hospital—\$427,000 to reflect reduced staffing associated with a lower actual population than that projected in the Governor's Budget at Patton State Hospital.

Delayed Activation of Salinas Valley State Prison Psychiatric Unit—\$1.1 million in 2001-02 and \$1.5 million in 2002-03 to reimburse the Department of Mental Health as a result of a four-month delay in the activation of the Salinas Valley Psychiatric Unit.

Department of the Youth Authority

2001-02	\$2.2 million
2002-03	-\$2 million

WARD/PAROLEE POPULATION/CASELOAD CHANGES

Current Year

For 2001-02, the May Revision estimate for the year-end institution population is 5,930, a decrease of 430 from the projection included in the Governor's Budget. This population decline, offset by a significant decline in the level of county reimbursements, will result in a General Fund increase of \$2.1 million. In addition, the Youth Authority projects a year-end parole population of 4,150, a decrease of 80 from the projection included in the Governor's Budget, which results a General Fund savings of \$118,000.

Budget Year

For 2002-03, the year-end institution population is projected to be 5,445, which is 655 fewer than anticipated in the Governor's Budget. The combined effect of declining population and a significant decrease in the level of county reimbursements will result in a General Fund increase of \$5.4 million. The Youth Authority projects a year-end parole population of 4,080, a decrease of 75 from the level assumed in the Governor's Budget, resulting in a savings of \$31,000.

AUGMENTATIONS

The May Revision proposes the following augmentations for the Department of the Youth Authority:



Mental Health Reorganization—\$1 million to initiate the reorganization of the Department's mental health delivery system to a case management model.

Postage Increase—\$32,000 to cover the increased postage costs related to the recent rise in the postal rates announced by the U.S. Postal Service.

Conditions of Confinement Class Action Lawsuit—\$3.5 million for additional staff and resources to aid the Department with the discovery and defense of a class action lawsuit.

Special Program Resources—Savings of \$619,000 and a redirection of \$1.3 million associated with the activation of 100 additional Specialized Counseling Program beds.

Bargaining Unit 6 Contract Operational Costs—\$157,000 in 2001-02 and \$628,000 in 2002-03 to cover operational costs associated with the provisions of the Bargaining Unit 6 Memorandum of Understanding.

Lease Revenue Payment—\$2,000 for lease revenue payments to reflect the increased cost of property insurance.

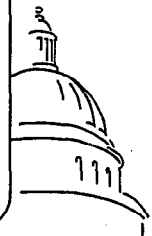
Health Insurance Portability and Accountability Act (HIPAA)—\$591,000 on a one-year, limited-term basis to assess the potential impact of HIPAA on the Department and determine solutions and regulatory considerations for implementation.

GENERAL FUND REDUCTIONS

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes reductions totaling \$12.6 million General Fund for the Youth Authority, including:

Adjusting County Sliding Scale Reimbursements—\$7.6 million General Fund reduction and a \$7.6 million increase in Reimbursements associated with adjusting sliding scale fees by inflation.

Paroles Reduction—\$5 million in the Parole Services Program (Paroles) within the Department. This reduction will be implemented by reducing non-critical parolee services, which will not affect parolee oversight or public safety.



Office of Criminal Justice Planning

2001-02	—
2002-03	-\$28.6 million

GENERAL FUND REDUCTIONS

Due to the reduction in available General Fund resources for 2002-03, the May Revision proposes a \$28.6 million reduction to the Office of Criminal Justice Planning, including:

Local Assistance Grants—A 50 percent reduction in local assistance grants totaling \$19.4 million.

War on Methamphetamine—A reduction of \$5 million for local assistance funding, leaving a funding level of \$10 million.

High Technology Theft Apprehension and Prosecution Program—A reduction of \$4.2 million in local assistance funding for this activity, leaving a funding level of \$10 million.

Office of the Inspector General

2001-02	—
2002-03	-\$1 million

GENERAL FUND REDUCTION

Due to a reduction in available General Fund resources, the May Revision proposes a \$1 million reduction to the Office of the Inspector General.

Board of Corrections

2001-02	—
2002-03	-\$31.9 million

GENERAL FUND REDUCTIONS

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes a reduction of \$31.9 million for the Board of Corrections, including:



Eliminating Support Funding Related to Juvenile Justice Program—Elimination of \$275,000 to reflect the deletion of the Juvenile Justice Crime Prevention Act funding.

Community Law Enforcement and Recovery (CLEAR) Program—A reduction of \$2 million to the CLEAR Program in Los Angeles County, and reappropriation of \$2 million of prior year funds to continue total CLEAR funding at \$3 million in 2002-03.

Challenge Grant II Funding—A decrease of \$12.3 million for the Challenge Grant II program to reflect elimination of fourth-year grant funding.

Mentally Ill Offender Crime Reduction (MIOCR) Grant—A decrease of \$17.3 million for the MIOCR Grant program to reflect elimination of third-year grant funding.

Board of Prison Terms

2001-02	-\$0.2 million
2002-03	-\$0.2 million

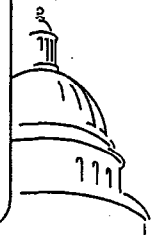
HEARING WORKLOAD ADJUSTMENT

The May Revision proposes reductions of \$193,000 in 2001-02 and \$223,000 in 2002-03 due to revised workload estimates associated with the projected number of parole consideration and parole revocation hearings.

Financial Assistance to Local Governments

Notwithstanding the change in the State's fiscal outlook, the May Revision continues to provide for the following:

- ❖ \$18.5 million for technology grants to local law enforcement, a decrease of \$16.9 million from the Governor's Budget.
- ❖ \$121.3 million for the Citizens Option for Public Safety (COPS) and Juvenile Crime Prevention programs, a decrease of \$111.3 million from the Governor's Budget. The COPS Program would be funded at \$121.3 million while funding for the Juvenile Crime Prevention Program would be eliminated.



Resources and Environmental Protection

Proposition 40 - Natural Resources

The California Clean Water, Clean Air, Safe Neighborhood Parks and Coastal Protection Act of 2002 (Proposition 40) approved by the voters in March 2002 provides \$2.6 billion for protection of the environment and the development of recreational opportunities for the people of California. When combined with the \$2.1 billion provided by the Safe Neighborhood Parks, Clean Water, Clean Air, and Coastal Protection Act of 2000 (Proposition 12), and the \$1.97 billion provided by the Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Act of 2000 (Proposition 13), an unprecedented total of \$6.7 billion will be expended over the next few years to improve the quality of life in California. The May Revision includes \$803.5 million from Proposition 40 for a variety of state and local parks, open space, river protection, clean beaches, water and air quality, and development and restoration of historical and cultural facilities.

RIVER PARKWAYS

The Administration continues its commitment to establishing and enhancing river parkways throughout the state. Proposition 40 river parkway initiatives will protect open space, preserve habitat, and provide recreational opportunities along numerous rivers from the North Coast through the Central Valley to Southern California. The May Revision provides \$83.1 million for the following areas:

- ❖ \$37.5 million for various river parkway projects in Southern California
- ❖ \$13.5 million for projects in the Sierra and Central Valley
- ❖ \$9.6 million for Central Coast rivers
- ❖ \$2 million for projects in the North Coast
- ❖ \$18 million for the San Gabriel and Lower Los Angeles Rivers and Mountains Conservancy
- ❖ \$5 million, including \$2.5 million in reimbursements for the San Joaquin River Conservancy



CLEAN BEACHES, WATER QUALITY AND WATERSHED PROTECTION

The coastline is one of the most important characteristics of California—it is a major force in the economy, provides for year-around recreation, is a major draw for tourism, and provides irreplaceable habitat for hundreds of wildlife species. Polluted beaches pose a serious health threat that results in closures. Inland water quality problems affect the health of the coastline. The May Revision includes \$73 million for a variety of grants for urban stormwater projects, wastewater facilities, water recycling, and nonpoint source control projects.

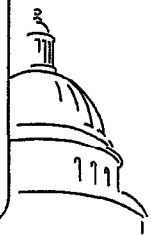
In addition, the Administration continues its efforts to minimize beach closures by focusing on the most popular beaches with water quality problems. The May Revision provides an additional \$23 million to further beach cleanup efforts over the next year. Coupled with previous allocations of bond funds, more than \$54 million has been provided to California communities for projects to improve beach water quality since last year.

The May Revision also provides over \$68 million for critical watershed protection projects such as the Bolsa Chica lowlands, Ballona Creek, the San Francisco Bay wetlands, and Palo Corona Ranch. Acquisition and restoration of watersheds is critical to prevent the loss of unique habitats and species, and to improve water quality.

HISTORICAL AND CULTURAL PRESERVATION AND LOCAL PARKS

The Administration is committed to preserving California's richly diverse cultural heritage and its unique historical resources. The May Revision includes \$107 million to acquire, develop, and protect significant resources by providing \$68 million for Historical and Cultural Preservation Opportunity Grants, \$27 million to California State Parks for four key historical projects, and \$12 million for the California Historic Preservation Competitive Grant Program.

As the population of California grows, the demands for local recreational opportunities grow. Toward satisfying this need, the May Revision provides \$80 million for projects specified in Proposition 40. Additional funds for local facilities will be allocated in future years upon completion of the development of guidelines and criteria as required by Proposition 40.



Secretary for Resources

2001-02	—
2002-03	-\$2.1 million

AUGMENTATIONS

The May Revision proposes the following augmentations:

- ❖ \$9.861 million federal funds for the Coastal Impact Assistance Program to mitigate the effects of oil and gas production along the California coastline.
- ❖ \$7.641 million Proposition 13 for River Parkway projects along the San Gabriel, San Dieguito, San Diego, and Tuolumne rivers.
- ❖ \$1.887 million Proposition 12 for the Folsom Powerhouse State Park. The Powerhouse is located along the American River in the City of Folsom and contains the original turbines installed in the 1800s, when high voltage electric power was first sent over transmission lines to downtown Sacramento.

GENERAL FUND REDUCTIONS

In light of the State's current fiscal constraints, the May Revision proposes a \$2.125 million fund shift from the General Fund to the Environmental License Plate Fund for the California Legacy Project and the California Ocean Resources Management Program. The Legacy Project is currently assessing the state's natural resources and habitat and developing a long-term set of priorities and targets for future investment in resource protection, habitat acquisition, and preservation.

California Conservation Corps

2001-02	—
2002-03	-\$7.2 million

GENERAL FUND REDUCTION

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes to reduce \$7.2 million and 10 positions for the Training and Work Program. The total number of corps members will be reduced from approximately 2,150 to 1,725. This reduction will be accomplished through normal attrition; no corps members will be released from the program early.



Energy Resources Conservation and Development Commission

2001-02	—
2002-03	-\$600,000

The May Revision proposes the following reductions:

- ❖ \$600,000 General Fund and 7 positions for power plant siting and certification activities.
- ❖ \$566,000 Local Government Geothermal Resources Development Account for local government geothermal grants and projects. Over the last several months, the price of electricity has fallen significantly. The program relies on royalty payments that are directly tied to the price of electricity. As a result, there is a need to correspondingly reduce program expenditures.

Department of Forestry and Fire Protection

2001-02	\$30 million
2002-03	\$1.5 million

AUGMENTATIONS

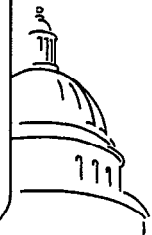
The May Revision proposes the following augmentations:

- ❖ \$30 million in 2001-02 for emergency fire suppression. Total emergency fire suppression costs for 2001-02 are projected to be \$130 million.
- ❖ \$1.5 million in 2002-03 for aircraft pilots and a maintenance services contract. This contract is critical to fire suppression efforts.

State Lands Commission

2001-02	—
2002-03	-\$600,000

The May Revision proposes a reduction of \$600,000 for the Mineral Resources Management and Land Management Programs offset by an increase of \$150,000 reimbursements, for a net reduction of \$450,000.



Wildlife Conservation Board

2001-02	-\$14 million
2002-03	—

GENERAL FUND REDUCTION

Given the State's current fiscal constraints, the May Revision proposes a \$14 million reduction to be offset with Proposition 40 funding for acquisition of sensitive habitat related to the University of Merced Grasslands Project.

California Coastal Commission

2001-02	—
2002-03	-\$1.1 million

GENERAL FUND REDUCTION

The May Revision proposes a \$1.1 million reduction for the Coastal Management Program. Approximately \$9.1 million General Fund and \$5.4 million special funds remain for managing and protecting coastal resources.

Department of Parks and Recreation

2001-02	—
2002-03	\$11.2 million

AUGMENTATIONS

The May Revision proposes the following augmentations:

- ❖ \$8.1 million General Fund and \$901,000 Off Highway Vehicle Trust Fund to implement the Transition Plan for Accessibility in State Parks, pursuant to the Americans with Disabilities Act.
- ❖ \$3.1 million General Fund for public safety and maintenance services to provide immediate public access to four properties in metropolitan Los Angeles: Lower Topanga Canyon, Mulholland Gateway, Cornfields, and Taylor Yards.



Department of Water Resources

2001-02	—
2002-03	-\$31.4 million

The May Revision proposes \$20 million Proposition 13 to provide grants to local agencies for projects that increase flood protection, protect agricultural land, and preserve and enhance wildlife habitat.

In addition, \$31.4 million will be transferred from the State Water Project to the General Fund in settlement funds received from the Independent Systems Operator for power purchased on behalf of investor-owned utilities prior to the Governor's January 2001 Emergency Proclamation.

CALFED Bay-Delta Program

2001-01	—
2002-03	-\$12.9 million

GENERAL FUND REDUCTIONS

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes a \$12.9 million reduction for various CALFED programs, including Water Use Efficiency, Levees, Watershed, Drinking Water Quality, and Science Programs. However, these reductions will be partially offset by an additional \$11 million Proposition 13 for the CALFED Water Use Efficiency Program, which will provide funding for urban water conservation projects and promote more efficient water management practices.

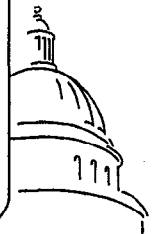
Air Resources Board

2001-02	—
2002-03	-\$9 million

GENERAL FUND REDUCTIONS

In light of the State's current fiscal constraints, the May Revision proposes the following reductions:

- ❖ \$6 million for incentive grants to promote the purchase of electric vehicles.



- ❖ \$3 million for air monitoring programs, leaving approximately \$2 million General Fund and \$10 million special funds to continue air monitoring activities.

Department of Pesticide Regulation

2001-02	—
2002-03	-\$3.4 million

GENERAL FUND REDUCTIONS

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes a reduction of \$3.4 million and 23 positions from food tolerance assessments, total maximum daily load, toxic air contaminant standards, and pest management grant programs. Approximately \$13.6 million General Fund and \$42.7 million other funds will remain for these programs.

State Water Resources Control Board

2001-02	—
2002-03	-\$6.2 million

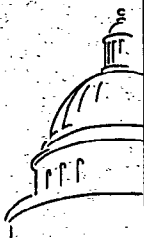
GENERAL FUND REDUCTIONS

In light of the State's current fiscal constraints, the May Revision proposes a reduction of \$6.2 million in stormwater contracts related to nonfiler search activities, providing technical and financial assistance to local agencies to facilitate compliance with permits, and promoting best management practices for the control of stormwater pollution.

Department of Toxic Substances Control

2001-02	—
2002-03	(\$15 million)

The May Revision proposes a \$15 million loan from the Hazardous Waste Control Account (HWCA) to the General Fund, to be paid back beginning in 2004-05. The HWCA is used for hazardous waste management activities, including regulation, permitting, and enforcement. These HWCA resources are available because of an unanticipated increase in revenues.



Office of Environmental Health Hazard Assessment

2001-02	—
2002-03	<i>-\$1.4 million</i>

GENERAL FUND REDUCTIONS

Due to the recent steep decline in General Fund revenues, the May Revision proposes a reduction of \$1.4 million and 10.5 positions from scientific literature research, technical services for development of risk assessments, and evaluations of contaminants. Approximately \$12.2 million General Fund and \$3.2 million other funds will remain for these programs.

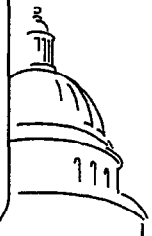
Public Utilities Commission

2001-02	—
2002-03	<i>\$7.9 million (special fund)</i>

AUGMENTATIONS

The May Revision proposes the following augmentations:

- ❖ \$950,000 Public Utilities Commission Utilities Reimbursement Account (PUCURA) and 10 two-year limited-term positions to conduct rate-setting proceedings for Department of Water Resources energy procurement costs.
- ❖ \$871,000 PUCURA and 11 positions to conduct energy, telecommunications, and water utility audits.
- ❖ \$2,077,000 PUCURA and 19.5 positions to develop power plant performance standards and perform operation and maintenance inspections of facilities, pursuant to Chapter 16, Statutes of 2001, and Chapter 19, Statutes of 2002, both of the Second Extraordinary Session (AB 28XX and SB 39XX, respectively).
- ❖ \$4 million PUCURA to retain legal counsel for continued assistance with Pacific Gas and Electric bankruptcy issues and the Commission's alternative reorganization plan.



2002-03

Electricity Oversight Board

2001-02	-\$620,000
2002-03	-\$730,000

GENERAL FUND REDUCTIONS

The May Revision proposes General Fund reductions of \$620,000 in 2001-02 and \$730,000 in 2002-03 for the development and enforcement of power plant operating and maintenance protocols. Chapter 19, Statutes of 2002 of the Second Extraordinary Session (SB 39XX), reassigned most of these responsibilities to the Public Utilities Commission.

Capital Outlay

LEASE REVENUE DEBT COSTS

2001-02	—
2002-03	-\$37.7 million

The May Revision proposes reductions of \$37.7 million General Fund and \$6 million special fund in lease revenue debt costs. These savings result from changes in bond sale schedules and decreases in project costs.

Business, Transportation, and Housing

Department of Housing and Community Development

2001-02	—
2002-03	-\$14.4 million

AUGMENTATION

The May Revision proposes an increase of \$120,000 to redirect three positions on a three-year limited-term basis to perform mobilehome parks inspections.



GENERAL FUND REDUCTIONS

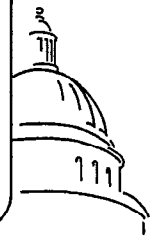
Due to the change in the State's fiscal outlook, the May Revision includes the following reductions:

Farmworker Housing Program—\$8.5 million for the Farmworker Housing program in light of the housing bond placed on the November 2002 ballot pursuant to Chapter 26, Statutes of 2002, which includes funds for this program.

Emergency Housing Assistance Program—\$6 million for the Emergency Housing Assistance Program, leaving \$5.3 million in resources available for this program.

In addition to the reductions above, the May Revision proposes the following transfers, loans, and fund shifts:

- ❖ **Child Care Facilities Financing Program**—An increased transfer of \$1.322 million from the Child Care and Development Facilities Loan Guarantee Fund to the General Fund.
- ❖ **Consolidated Predevelopment Loan Program**—A shift of \$110,000 in funding from the General Fund to the Predevelopment Loan Fund for the Consolidated Predevelopment Loan Program.
- ❖ **Mobilehome Purchase Program**—An increased loan of \$2.1 million from the Mobilehome Purchase Fund to the General Fund.
- ❖ **CalHOME Program**—A transfer of \$5.6 million from the Self-Help Housing Fund to the General Fund. The transferable funds were originally appropriated in the 2000 Budget Act.
- ❖ **Farmworker Housing Program**—A transfer of \$3 million from the Farmworker Housing Grant Fund to the General Fund. The transferable funds were originally appropriated in the 2000 Budget Act.
- ❖ **Interregional Planning Partnership Program**—A transfer of \$1.3 million from the Housing Rehabilitation Loan Fund to the General Fund. The transferable funds were originally appropriated in the 2000 Budget Act.



Department of Real Estate

2001-02	—
2002-03	—

Due to the change in the State's fiscal outlook, the May Revision includes an increased loan of \$1 million from the Real Estate Commissioners Fund to the General Fund.

Department of Transportation

2001-02	—
2002-03	-\$34.5 million

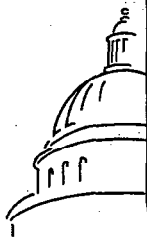
BUDGET ADJUSTMENTS

The May Revision proposes the following adjustments:

Project Delivery Workload—A reduction of \$38.1 million and 550 positions/379.5 personnel years reflecting an adjustment of staffing and related program resources required to deliver projects included in the adopted 2002 State Transportation Improvement Program. The Administration intends to pursue the establishment of additional positions administratively to the extent that viable options are identified for advance delivery that would require additional staffing in the budget year.

Establishment of Transportation Finance Bank Revolving Loan Program—An increase of \$3 million to establish a revolving loan program to provide flexible, short-term financing to public entities and public/private partnerships for the purpose of delivering transportation projects in California.

Extending Highway Work Zone Awareness Campaign—A redirection of \$5 million for one year to continue and expand the multi-lingual media/advertising campaign to increase public awareness of hazards in highway work zones. Caltrans will also analyze existing work zone accident and various cost data to determine whether the campaign has been successful in reducing work zone accidents, claims, litigation, and worker's compensation costs.



BUDGET REDUCTIONS

Due to the change in the State's fiscal outlook, the May Revision also includes the following:

State Highway Account Loan—A current-year loan of \$50 million from the State Highway Account to the General Fund under Article XIX, Section 6, subdivision (b) (2) of the California Constitution.

Transportation Congestion Relief Fund Loan—An increased loan of \$373 million from the Transportation Congestion Relief Fund to the General Fund. No projects will be delayed as a result of this loan.

SPECIAL TRANSPORTATION PROGRAMS

2001-02	—
2002-03	-\$17.3 million

Statutory Formula Adjustment—The May Revision includes a reduction of \$17.3 million for Special Transportation Programs. This reduction results in a revised funding level of \$98 million, which reflects the statutorily required allocation of the program.

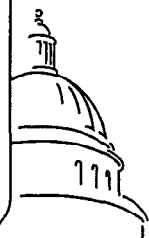
Department of California Highway Patrol

2001-02	—
2002-03	\$3.9 million (special fund)

AUGMENTATIONS

The May Revision proposes the following augmentations from the Motor Vehicle Account in anticipation of reimbursement from federal funds:

Border Security Equipment—An increase of \$3.1 million for the purchase, installation, and operation of nuclear weapon detection devices in order to enhance the security of California, its citizens, and infrastructure. These devices will be installed and operated at a total of eight inspection facilities located on or near the border of the State or at ports of entry that are staffed with California Highway Patrol personnel.



Security Personnel—An increase of \$649,000 for six additional officers to provide the security on and around the Golden Gate Bridge .

The May Revision also includes an increase of \$73,000 to fund a postage increase effective July 1, 2002.

Department of Motor Vehicles

2001-02	—
2002-03	\$3.1 million

The May Revision proposes an increase of \$2.554 million to fund a postage increase effective July 1, 2002.

Technology, Trade and Commerce

2001-02	—
2002-03	-\$17.4 million

GENERAL FUND REDUCTIONS

Due to the change in the State's fiscal outlook, the May Revision includes the following reductions:

Biomass to Energy Grant Program—\$2 million for the Biomass to Energy Grant Program.

Foreign Trade Office Program—\$2 million for the Foreign Trade Office Program.

Manufacturing Technology Program—\$2.7 million for the Manufacturing Technology Program.

Office of Military Base Reuse and Retention—\$1 million for the Office of Military Base Reuse and Retention.

Film Commission—\$300,000 in operating and equipment funding for the Film Commission.

Office of Foreign Investment—\$239,000 for support of the Office of Foreign Investment.



Office of Export Development—\$400,000 for support of the Office of Export Development.

Marketing and Communications Division—\$627,000 for support of the Marketing and Communications Division.

Division of Science, Technology and Innovation—\$803,000 for support of the Division of Science, Technology and Innovation.

Business Development Support—\$538,000 for support of the business development programs.

The May Revision proposes to suspend the following programs until the State's fiscal outlook improves:

Next Generation Internet Centers—A reduction of \$1 million for the Next Generation Internet Centers.

Rural e-Commerce Grant Program—A reduction of \$1 million for the Rural e-Commerce Grant Program.

Space Industry Development Grant Program—A reduction of \$1 million for the Space Industry Development Grant Program.

Additionally, the May Revision proposes to eliminate the following programs:

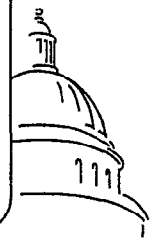
Defense Adjustment Matching Program—A reduction of \$500,000 to reflect the elimination of the Defense Adjustment Matching Program.

Regional Trade Offices—A reduction of \$2.566 million to reflect the elimination of the Regional Trade Offices.

Regulation Review Unit—A reduction of \$89,000 to reflect the elimination of the Regulation Review Unit.

Office of Permit Assistance—A reduction of \$226,000 to reflect the elimination of the Office of Permit Assistance.

Economic Development Support—A reduction of \$448,000 to reflect the elimination of the Economic Development Support Program.



FUND TRANSFERS AND LOANS

The May Revision includes the following transfers and loans to the General Fund:

Small Business Loan Guarantee Fund—A transfer of \$2.7 million from the Small Business Loan Guarantee Fund.

Infrastructure Bank Fund—A transfer of \$8 million from the Infrastructure Bank Fund.

Rural Economic Development Infrastructure Revenue Bond Fund—A transfer of \$8.4 million from the Rural Economic Development Infrastructure Revenue Bond Fund.

Petroleum Underground Storage Tank Financing Account—A loan of \$17 million from the Petroleum Underground Storage Tank Financing Account.

Petroleum Financing Collection Account—A loan of \$1 million from the Petroleum Financing Collection Account.

Local Government

FINANCIAL ASSISTANCE TO LOCAL GOVERNMENTS

2001-02	—
2002-03	-\$38.2 million

Due to the decline in the amount of General Fund resources available, the May Revision eliminates \$38.2 million to cities and special districts for reimbursement of booking fees paid to counties and other cities.

The May Revision also proposes to require multicounty special districts and community redevelopment agencies to pay into the Educational Revenue Augmentation Fund (ERAF). Multicounty special districts would annually pay approximately \$45 million in to the Educational Revenue Augmentation Fund (ERAF) while community redevelopment agencies would pay \$75 million.



Tax Relief

2001-02	—
2002-03	-\$1.305 billion

In light of the State's current fiscal constraints, the May Revision deletes \$39 million in subventions to local governments for property tax losses incurred by enrolling agricultural land in Williamson Act contracts.

The Administration also proposes to temporarily reduce the Vehicle License Fee (VLF) offset level from 67.5 percent to 25 percent on January 1, 2003. This was the VLF offset level in effect when the Administration took office in 1999. This proposal will result in a General Fund savings of \$1.276 billion in 2002-03 and \$1.1 billion in 2003-04. Local governments would continue to receive their current level of funding.

Judicial Branch

Judiciary

2001-02	—
2002-03	-\$2.8 million

GENERAL FUND REDUCTION

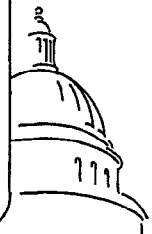
Judiciary Reduction—Due to the decline in available General Fund resources, the May Revision proposes a one-time funding reduction of \$2.8 million for the Judiciary.

State Trial Court Funding

2001-02	—
2002-03	-\$49.6 million

AUGMENTATION

The May Revision proposes \$9.6 million General Fund for increased costs associated with providing security at trial court facilities.



GENERAL FUND REDUCTION

Trial Court Funding Reduction—In light of the State's current fiscal outlook, the May Revision proposes a one-time reduction of \$59.2 million to the Trial Court Trust Fund with a corresponding \$59.2 million reduction to the General Fund transfer to the Trial Court Trust Fund.

General Government
Department of General Services

2001-02	—
2002-03	\$23,000

AUGMENTATION

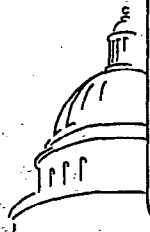
The May Revision proposes an augmentation of \$1.5 million General Fund to reflect the transfer of executive information technology funds from the Department of Information Technology to the Department of General Services (DGS).

GENERAL FUND REDUCTIONS

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes reductions totaling \$1.5 million for DGS, including:

California Portal—\$1.2 million General Fund for operation of the California Portal.

Asbestos Abatement/Underground Storage Tanks—\$300,000 to be allocated by the Department to the Asbestos Abatement Program and the Underground Storage Tank Program.



Department of Consumer Affairs

2001-02	—
2002-03	<i>-\$0.2 million</i>

GENERAL FUND REDUCTIONS

In light of the State's current fiscal constraints, the May Revision proposes a reduction of \$215,000 for the Department of Consumer Affairs' Office of Privacy Protection, Consumer Relations and Outreach Division, and the State Athletic Commission.

Labor and Workforce Development Agency

2001-02	—
2002-03	<i>\$1.8 million</i>

AUGMENTATION

The May Revision proposes a redirection of \$1.8 million (all funds) and 17 positions from the Employment Development Department, the Department of Industrial Relations, and the California Workforce Investment Board to support the operations of the California Labor and Workforce Development Agency, which is proposed to be established pursuant to Governor's Reorganization Plan No. 1 of 2002.

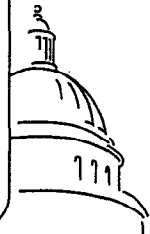
Department of Industrial Relations

2001-02	—
2002-03	<i>-\$2.5 million</i>

AUGMENTATIONS

The May Revision proposes the following increases to the Department of Industrial Relations:

Postal Rate Increase—\$174,000 (\$141,000 General Fund, \$33,000 other funds) to cover the increased postage costs related to the rise in postal rates by the U.S. Postal Service effective July 1, 2002.



2002-03

AB 749 Base Budget Realignment—A General Fund augmentation of \$563,000, and a corresponding special fund reduction of \$563,000 to realign the base budget for the Commission on Health and Safety and Workers Compensation effective January 1, 2003, pursuant to the provisions of AB 749 (Chapter 6, Statutes of 2002).

GENERAL FUND REDUCTIONS

Due to the decline in available General Fund resources, the May Revision proposes the following reductions:

Divisions of Labor Standards Enforcement and Apprenticeship Standards—\$2 million reflecting the 2001-02 General Fund augmentation to these divisions.

Elevator Inspection Fund Shift—\$1 million, with a corresponding increase of \$1 million Elevator Safety Account to continue the Elevator Safety Inspection Program at the existing level.

Governor's Office

2001-02	—
2002-03	-\$0.2 million

GENERAL FUND REDUCTION

Due to the change in the State's fiscal outlook, the May Revision proposes a reduction of \$200,000 for the Governor's Office, resulting in a reduction of 8.5 percent including the Governor's Budget and the May Revision.

Lieutenant Governor's Office

2001-02	—
2002-03	-\$50,000

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes a reduction of \$50,000 for the Lieutenant Governor's Office, resulting in a reduction of 6.8 percent including the Governor's Budget and the May Revision.



Secretary of State

2001-02	—
2002-03	-\$950,000

Due to the State's current fiscal constraints, the May Revision proposes a reduction of \$950,000 from the Secretary of State's Office and its operations, resulting in a reduction of 7.8 percent including the Governor's Budget and the May Revision. This reduction is not intended to adversely affect election-related functions and activities.

Department of Insurance

2001-02	—
2002-03	-\$1.8 million

GENERAL FUND REDUCTION

The May Revision proposes a decrease of \$1.8 million General Fund and a corresponding increase of \$1.8 million from the Insurance Fund to reflect a transfer of funding to support the Premium Tax Program.

Office of Emergency Services

2001-02	—
2002-03	-\$5 million

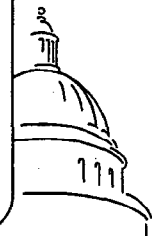
Due to the recent decline in General Fund revenues, the May Revision proposes a reduction of \$5 million from local disaster assistance funding for the Office of Emergency Services.

California Science Center

2001-02	—
2002-03	-\$1.1 million

GENERAL FUND REDUCTIONS

In light of the State's current fiscal constraints, the May Revision proposes a reduction of \$1.1 million General Fund to be allocated to various programs, including Education, the California African American Museum, and Exposition Park Management.



Office of the State Public Defender

2001-02	—
2002-03	<i>-\$0.3 million</i>

GENERAL FUND REDUCTION

Due to the decline in available General Fund resources, the May Revision proposes a reduction of \$250,000 to reflect the elimination of currently vacant positions.

Office of Planning and Research

2001-02	—
2002-03	<i>-\$0.5 million</i>

GENERAL FUND REDUCTIONS

Due to the change in the State's fiscal outlook, the May Revision proposes reductions totaling \$511,000 for the Office of Planning and Research (OPR), including:

Cesar Chavez Day of Service and Learning Grant Program—\$139,000 for the Cesar Chavez Day of Service and Learning Grant Program.

OPR Support Budget—\$372,000 for the support of OPR and the Governor's Office on Service and Volunteerism.

Military Department

2001-02	—
2002-03	<i>-\$1.8 million</i>

GENERAL FUND REDUCTIONS

Due to the decline in available General Fund resources for 2002-03, the May Revision proposes the following reductions:

- ❖ \$900,000 for the Army National Guard, the Air National Guard, Support to Civil Authority, and the State Military Reserve Programs without any adverse effects relating to preparedness.
- ❖ \$900,000 for the California Cadet Corps and Youth Programs.



In addition, the May Revision proposes a reduction of \$6 million federal funds to reflect the discontinuation of the bridge guarding security mission at four bridges.

Department of Veterans Affairs

HEADQUARTERS

2001-02	—
2002-03	\$0.1 million

The May Revision proposes \$134,000 for an assessment of the changes needed to business processes and to develop an implementation plan, to ensure Department of Veterans Affairs programs are compliant with the federal Health Insurance Portability and Accountability Act.

YOUNTVILLE HOME

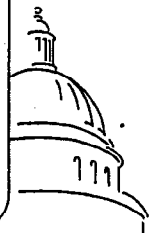
2001-02	—
2002-03	\$1.3 million

The May Revision proposes a reduction of \$1.3 million General Fund and a corresponding increase of \$1.3 million federal funds. These changes are due to an increase in the United States Department of Veterans Affairs (USDVA) per diem rate.

BARSTOW HOME

2001-02	—
2002-03	-\$0.5 million

The May Revision proposes a \$533,000 reduction in General Fund, a \$278,000 reduction in reimbursements, and a \$114,000 increase in federal funds. These changes are due to an increase in the USDVA per diem rate and a reduction in the budgeted census level due to a delay in reaching full occupancy at the Home, as well as minor adjustments to lease revenue.



CHULA VISTA HOME

2001-02	—
2002-03	<i>-\$0.9 million</i>

The May Revision proposes a \$867,000 reduction in General Fund, a \$290,000 reduction in Reimbursements, and a \$398,000 increase in federal funds. These changes are due to an increase in the USDVA per diem rate and a reduction in the budgeted census level due to a delay in reaching full occupancy at the Home.

Department of Information Technology

2001-02	—
2002-03	<i>-\$2.8 million</i>

GENERAL FUND REDUCTIONS

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes a reduction of \$2.8 million for the Department of Information Technology. Of this amount, \$1.5 million will be transferred to the Department of General Services to provide funding for executive information technology services. The Administration intends to work with the Legislature to restructure state information technology governance and oversight functions.

Agricultural Labor Relations Board

2001-02	—
2002-03	<i>-\$0.5 million</i>

Due to the State's current General Fund constraints, the May Revision proposes a reduction of \$519,000 for the Agricultural Labor Relations Board.

Workers' Compensation Benefit Program

2001-02	—
2002-03	<i>-\$1 million</i>



GENERAL FUND REDUCTIONS

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes a reduction of \$1 million for this program, with a corresponding increase of \$1 million from the Subsequent Injuries Moneys Account.

California Arts Council

2001-02	—
2002-03	-\$16.3 million

GENERAL FUND REDUCTIONS

Due to the change in the State's fiscal outlook, the May Revision proposes reductions totaling \$16.3 million for the California Arts Council, including:

State Operations—\$1.1 million for state operations, leaving \$1.5 million to administer remaining grant programs.

Local Assistance—\$15.1 million for local assistance projects and grant programs, which will leave \$6 million for the Arts in Education Program, \$5 million for Organizational Support Grants, and \$2 million for the Tools for Tolerance Program at the Simon Wiesenthal Center.

Department of Food & Agriculture

2001-02	—
2002-03	-\$7.1 million

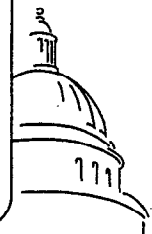
GENERAL FUND REDUCTIONS

Due to the recent decline in General Fund revenues, the May Revision proposes reductions totaling \$7.1 million for the Department of Food and Agriculture, including:

Measurement Standards—\$180,000 for the Measurement Standards Program.

Plant Pest Diagnostic Lab Program—\$580,000 for the Plant Pest Diagnostic Lab Program.

Buy California—\$3 million for the Buy California Program.



General Agricultural Activities—\$800,000 for market and commodities research.

Wildlife Services and Nuisance Control—\$983,000 for the Wildlife Services and Nuisance Control Program.

Pierce's Disease Management and Control—\$1.57 million for the Pierce's Disease Program and related state operations.

Reimbursable State Mandates Program

2001-02	- \$30 million
2002-03	- \$216.1 million

Due to the lower level of General Fund resources available for 2002-03, the May Revision proposes a reduction of \$168.3 million to reflect the suspension of payment for various reimbursable state mandate claims received by the State.

An amendment to Section 11.80 of the 2002-03 Budget Bill is proposed to reflect the removal of a set-aside amount of \$30 million to address potential deficiencies in mandate appropriations for the 2002-03 fiscal year. In addition, the Department of Finance will not be allocating the \$30 million set-aside pursuant to Section 11.80 of the 2001 Budget Act (Chapter 106, Statutes of 2001) for deficiencies in mandates from prior-year appropriations, providing a savings of \$30 million in 2001-02.

Finally, budget bill language is proposed to authorize the reversion in existing balances for various past-year mandate appropriations to retain savings of funds that have not yet been expended to pay local mandate claims, resulting in a savings of \$17.8 million for 2002-03.

Franchise Tax Board

2001-02	—
2002-03	\$9.352 million

Due to the change in the State's fiscal outlook, the May Revision proposes the following:

- ❖ Increasing the settlement program by four positions and \$520,000 to reduce the backlog in the Franchise Tax Board's (FTB's) settlement program.
- ❖ Increasing collections staff by 51 positions and \$3.78 million to increase the FTB's tax collection activities.



- ❖ Adding 41 positions and \$3.289 million to allow the FTB to waive penalties and interest on delinquent accounts.
- ❖ Adding two positions and \$260,000 to accelerate the completion of protested tax appeals.
- ❖ Providing 14 positions and \$799,000 to expand the Integrated Non-File Compliance (INC) Project.

State Retirement Contributions

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM (CALPERS)

2001-02	—
2002-03	\$75.9 million

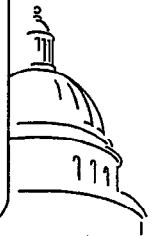
State Employer Retirement Contribution Rates

As a result of CalPERS' June 30, 2001 actuarial valuation of the retirement system, the State's 2002-03 obligation to CalPERS is estimated to increase by \$75.9 million General Fund (\$154.5 million total funds) from the Governor's Budget. As the General Fund payment to CalPERS is made on a quarterly basis, one quarter in arrears, the total General Fund payment for 2002-03 will be \$583.8 million.

STATE TEACHERS' RETIREMENT SYSTEM (STRS)

2001-02	—
2002-03	\$42.7 million

General Fund contributions to STRS will increase by \$42.7 million for 2002-03 (from \$932.8 million to \$975.5 million). This is due to a higher-than-anticipated increase in the 2001 calendar year teacher payroll base, which is the basis for the statutory formula.



2002-03

Health and Dental Benefits for Annuitants

2001-02	-\$27.6 million
2002-03	\$23 million

The May Revision includes an increase of \$23 million General Fund (from \$553.6 million to \$576.6 million) for annuitant health and dental benefits in 2002-03 due primarily to health premium increases. In addition, a decrease of approximately \$27.6 million General Fund in the current year is reflected due to lower-than-anticipated health benefit expenditures as a result of lower enrollment.

Employee Compensation

2001-02	—
2002-03	\$54.5 million

The Administration has successfully negotiated Memoranda of Understanding (MOUs) with 19 of the 21 Collective Bargaining Units (Units). Of the 19 MOUs, 15 have been ratified and 4 are awaiting ratification by either the membership of the Units, the Legislature, or both. The Administration continues to negotiate with the 2 Units without MOUs. Generally, for excluded employees, the Administration authorized salary and benefit adjustments similar to those provided to corresponding represented employees.

The May Revision includes \$89.5 million (\$54.5 million General Fund) for employee compensation over the amount included in the Governor's Budget. The additional employee compensation costs are primarily the result of significant increases in health benefit premiums, since, generally, the employer's maximum monthly health benefit contribution will increase to absorb two-thirds of the weighted average premium increase of health maintenance organizations effective January 2003. Additionally, there are increased costs resulting from the four collective bargaining agreements recently adopted.



Other General Fund Adjustments

The May Revision also includes the following General Fund adjustments:

Control Section 4.20—Reduction in Health Benefits Administrative Fee

- ❖ \$2.7 million in General Fund savings from a one-time reduction in the health benefit administrative fee paid to the California Public Employees' Retirement System (CalPERS).

Control Section 3.80—Premium Offset for Employer-paid Life Insurance

- ❖ \$827,000 in General Fund savings as a result of a one-time offset for employer-paid life insurance premiums. The demutualization proceeds received from the State's carrier for employee life insurance will provide the offset.

DEPARTMENT OF PERSONNEL ADMINISTRATION

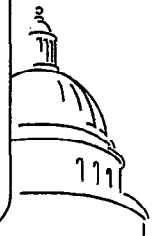
- ❖ \$149,000 General Fund augmentation and one position to address the increased collective bargaining workload.
- ❖ \$1.8 million General Fund reduction for the Rural Health Care Equity Program. This adjustment reflects the anticipated decrease in the number of State employees and annuitants without access to a CalPERS contracted Health Maintenance Organization, beginning January 2003.

Statewide Issues

Significant Federal Funding Adjustments

The May Revision updates several of the federal funding increase proposals contained in the Governor's Budget, as follows:

Medi-Cal Offset—Congress is currently considering multiple proposals and legislative vehicles to address states' needs for Federal Medical Assistance Percentage (FMAP) funding relief. Thus, \$400 million in additional federal relief is anticipated in 2002-03 rather than in 2001-02 as proposed in the Governor's Budget.



Child Support System Penalty Relief—The Governor's Budget assumed that California would receive a waiver of federal penalties imposed due to delayed implementation of a statewide automated child support system, for an estimated \$181.3 million in General Fund savings. The May Revision anticipates federal legislation will be enacted to provide approximately one-half the relief, resulting in relief of only \$89.7 million. The penalty will be shared between the State General Fund (\$44.9 million) and counties (\$44.8 million).

Food Stamps for Legal Immigrants—The May Revision includes an increase of \$92.2 million General Fund for the California Food Assistance Program (CFAP), to reflect the delayed restoration of federal Food Stamp eligibility for a limited number of recipients in the budget year. However, the net General Fund impact of the delay will be substantially less than this amount due to the fact that a share of these costs are countable towards the State's CalWORKs maintenance-of-effort requirement.

Bridge Security—Responsibility for protecting the state's bridges will be shifting from the National Guard to the California Highway Patrol. The May Revision includes an increase of six officers to provide a level of security, specifically for the Golden Gate Bridge, above that proposed in the Governor's Budget. While the receipt of federal funds for these activities in 2002-03 is still expected, the expenditure of funds for these activities is proposed from the Motor Vehicle Account, to be repaid by the subsequent receipt of federal funds.

Furthermore, the events of September 11th prompted calls for greater security on the state's heavily used toll bridges and major non-toll bridges in San Diego, Long Beach, and the San Francisco Bay Area. The Budget includes \$24.2 million to install 276 new cameras, associated communications, and monitoring stations on these bridges. State Highway Operations and Protection Program funds have been used to pay these one-time costs. However, it is anticipated that federal funds will be received to offset these costs. An April 1 Finance Letter included \$755,000 in ongoing federal funds to maintain this bridge security system.

Controlling the Growth of State Government

In spring 2000, the Administration moved aggressively to control the growth of State government by eliminating 3,500 excess vacant positions. Subsequently, the Administration continued this effort by eliminating an additional 600 positions in 2000-01 and 2,500 positions in 2001-02. The Administration now proposes in the May Revision to eliminate an additional 4,000 positions, for a total of over 10,000 positions eliminated, to further constrain the growth of the State bureau-



cracy and ensure funds are not budgeted for unnecessary positions in the future. These reductions will be specified by departments in detailed plans to be submitted to the Director of Finance by July 1, 2002.

Eliminating Excess Vacant Positions

In July 2000, Section 12439 of the Government Code was amended to require the State Controller to abolish positions that are vacant continuously for six consecutive pay periods during a fiscal year. The Bureau of State Audits recently released a report suggesting that some departments may be transmitting inappropriate personnel transactions to the State Controller in order to circumvent the provisions of Section 12439. The Administration proposes substantial amendments to Government Code Section 12439 to prohibit departments from circumventing its provisions and to direct the State Controller to abolish positions continuously vacant for six months even when the period of vacancy crosses fiscal years. The amendments will also clarify the conditions under which some continuously vacant positions should not be abolished. These changes will permit the Administration and the Legislature to more easily identify and eliminate unnecessary positions.

General Obligation Bonds and Commercial Paper Debt Service

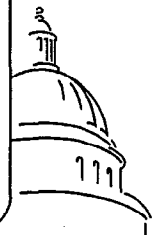
2001-02	-\$14.6 million
2002-03	\$11.7 million

Current Year

The Governor's Budget anticipated current year General Obligation (GO) bond debt service expenditures of approximately \$2.541 billion. A Finance Letter dated February 14, 2002, reduced debt service by \$223 million to reflect the State Treasurer's debt restructuring plan for fiscal year 2001-02. In addition, to reflect savings from Commercial Paper costs, accrued interest, and premiums from bond sales that occurred in November 2001 and February and April 2002, there will be additional savings of \$14.6 million in the current year.

Budget Year

The Governor's Budget anticipated budget year GO bond debt service expenditures of approximately \$2.572 billion. A Finance Letter dated February 14, 2002, reduced debt service by \$859.8 million to reflect the State Treasurer's debt restructuring plan for fiscal year 2002-03. Additionally, there will be a net increase of \$11.7 million in the budget year due primarily to increased Commercial Paper costs and an increase in the sales volume for fixed rate bonds in the fall of 2002. The increased costs will



be partially offset by lower than estimated interest costs for the spring 2002 sales and a reduction in the sales volume for variable rate bonds in the fall of 2002 and spring of 2003.

The net General Fund decrease will be \$2.9 million over the two fiscal years.

Statewide Software Licenses

The May Revision proposes adding Control Section 11.10 to the budget. This control section requires the Department of Finance to notify the Legislature before a department enters into or amends a statewide software license contract where the value of the contract or amendment is greater than \$1.5 million. Departments are required to prepare a business case review for statewide software license purchases and submit the business case to the Department of Finance and the Department of Information Technology for review and approval.

2002-03 State Appropriations Limit Calculation

Pursuant to Article XIII B of the California Constitution, the 2002-03 State Appropriations Limit (SAL) is estimated to be \$59.591 billion. The revised limit is the result of applying the growth factor of 0.46 percent. The revised 2002-03 limit is \$1.092 billion above the \$58.499 billion estimated in January. This increase is due to changes in the following factors:

	January Percentage	May Revision Percentage
Per Capita Personal Income	-3.01	-1.27
State Civilian Population	1.89	1.83
K-14 Average Daily Attendance	1.37	1.63

The SAL for 2001-02 does not change since it was statutorily established by Section 12.00 of the 2001 Budget Act.



Payment of Interest on General Fund Loans

2001-02	- \$10 million
2002-03	\$254 million

Current Year

The Governor's Budget anticipated the interest cost on internal borrowing to be \$30 million General Fund. Based upon actual costs through mid-April and anticipated costs through the end of the fiscal year, the May Revision estimates the interest cost on internal borrowing to be \$20 million.

The Governor's Budget included \$95 million for interest cost on external borrowing. There is no change to the interest cost on external borrowing for 2001-02. The Revenue Anticipation Notes were sold at a cost of \$95 million. The total 2001-02 General Fund savings are \$10 million.

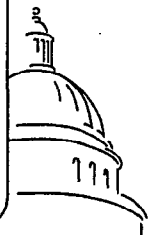
Budget Year

The Governor's Budget anticipated the interest cost on internal borrowing to be \$50 million General Fund. The May Revision continues this assumption.

The Governor's Budget anticipated the interest cost on external borrowing to be \$56 million General Fund. This estimate was based upon the assumption that \$2.5 billion Revenue Anticipation Notes (RANs) would be issued in October 2002 and redeemed in June 2003.

The Administration has been monitoring the State's cash condition closely with the State Controller's Office and the State Treasurer's Office. On April 25, 2002, the Governor approved the Controller's request to establish the General Cash Revolving Fund, the initial step necessary to issue Revenue Anticipation Warrants (RAWs). The Controller is anticipated to sell \$7.5 billion of RAWs in June 2002. The structure and maturity date(s) of RAWs and the sizing of RANs to be issued in 2002-03, if needed, have not been determined yet. Based upon the above, the revised estimate for external borrowing costs is \$310 million, or an increase of \$254 million. The estimate should be sufficient to cover the interest cost of RAWs and RANs, if needed, and any credit enhancement that may be required.

The May Revision estimates are preliminary pending completion of cash flow projections. The need for internal and/or external borrowing will ultimately be based on the cash flow projection for the Budget Act together with new information when available, rather than the May Revision or the Governor's Budget.

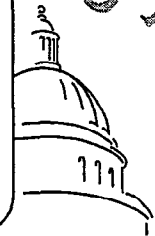


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**2002-03 May Revision
General Fund
Budget Summary
(Dollars in Millions)**

	<u>2001-02</u>	<u>2002-03</u>
Prior Year Balance	\$2,986	-\$123
Revenues and Transfers	<u>\$73,775</u>	<u>\$78,603</u>
Total Resources Available	\$76,761	\$78,480
Expenditures	<u>\$76,884</u>	<u>\$76,491</u>
Fund Balance	-\$123	\$1,989
Budget Reserves		
Reserve for Liquidation of Encumbrances	\$1,473	\$1,473
Special Fund for Economic Uncertainties	-\$1,596	\$516

Summary Charts



2002-03 Revenue Sources
(Dollars in millions)

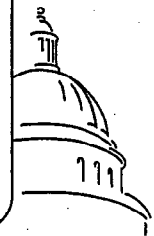
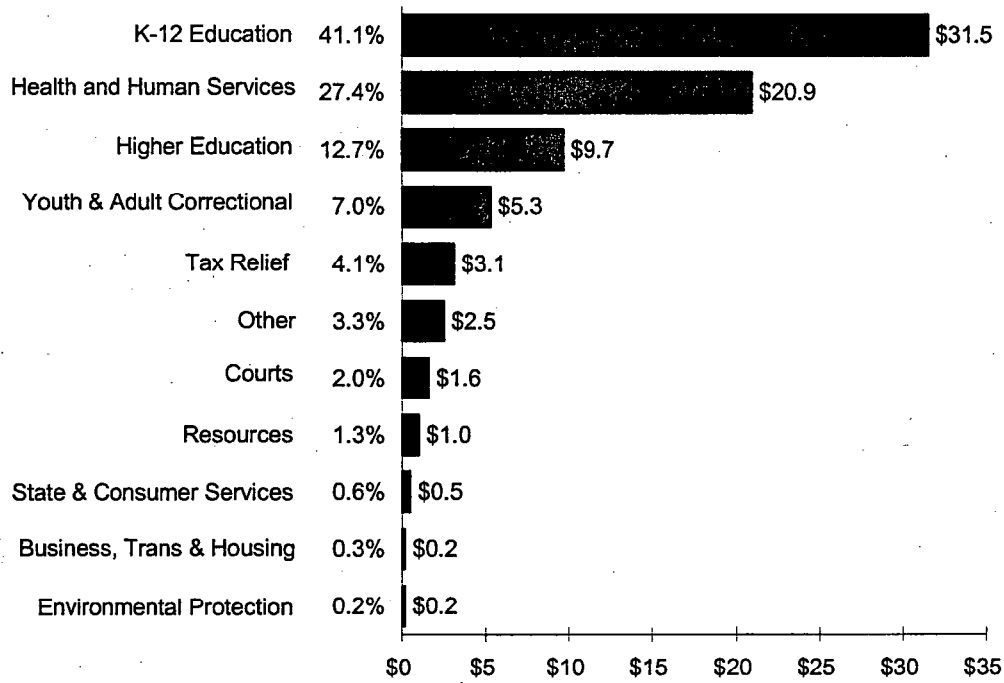
	<u>General Fund</u>	<u>Special Fund</u>
Personal Income Tax	\$37,057	-
Sales Tax	22,958	\$2,516
Corporation Tax	7,297	-
Highway Users Taxes	-	3,244
Motor Vehicle Fees	26	5,181
Insurance Tax	1,759	-
Estate Taxes	646	-
Liquor Tax	288	-
Tobacco Taxes	596	941
Other	<u>7,976</u>	<u>4,458</u>
Total	\$78,603	\$16,340

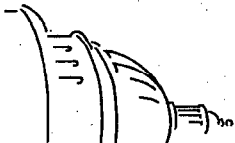
**2002-03
General Fund Expenditures
by Agency**
(Dollars in Millions)

	<u>2001-02</u>	<u>2002-03</u>
Legislative, Judicial, Executive	\$2,659	\$2,523
State and Consumer Services	714	471
Business, Transportation & Housing	645	223
Technology, Trade, and Commerce	74	54
Resources	1,545	965
Environmental Protection	436	179
Health and Human Services	22,103	20,934
Youth and Adult Correctional	5,544	5,339
K-12 Education	30,015	31,454
Higher Education	9,778	9,720
General Government/Tax Relief	<u>3,371</u>	<u>4,629</u>
Total	\$76,884	\$76,491



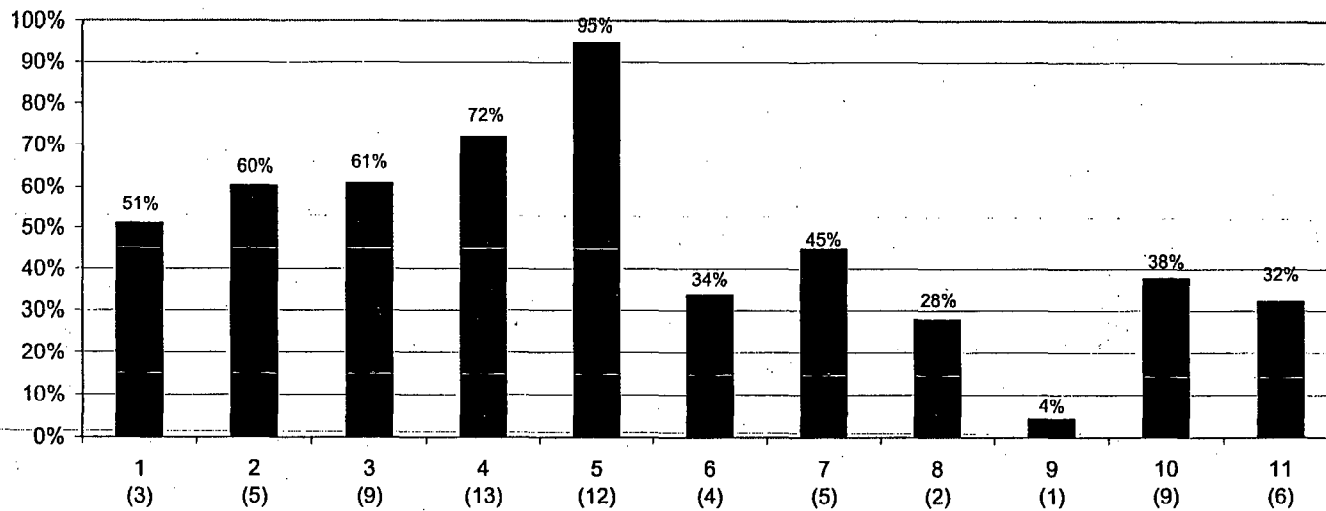
**2002-03 General Fund Expenditures
(Dollars in Billions)**





General Fund Expenditure Growth Comparison Since 1959 in Four-Year Increments

(The parenthetical number beneath each bar represents the number of times faster GF expenditures grew compared to population during each four-year period.)



1. 1958-59 (\$1.2)
to 1962-63 (\$1.9)

3. 1966-67 (\$3.0)
to 1970-71 (\$4.9)

5. 1974-75 (\$8.3)
to 1978-79 (\$16.3)

7. 1982-83 (\$21.8)
to 1986-87 (\$31.5)

9. 1990-91 (\$40.3)
to 1994-95 (\$42.0)

11. 1998-99 (\$57.8)
to 2002-03 (\$76.5)

2. 1962-63 (\$1.9)
to 1966-67 (\$3.0)

4. 1970-71 (\$4.9)
to 1974-75 (\$8.3)

6. 1978-79 (\$16.3)
to 1982-83 (\$21.8)

8. 1986-87 (\$31.5)
to 1990-91 (\$40.3)

10. 1994-95 (\$42.0)
to 1998-99 (\$57.8)

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